Public Disclosure Authorized
Public Disclosure Authorized
Public Disclosure Authorized
Public Disclosure Authorized

KENYA ECONOMIC UPDATE

April 2017 | Edition No. 15

HOUSING

Unavailable and Unaffordable

WORLD BANK GROUP

HOUSING

Unavailable and Unaffordable

© 2017. World Bank Group

This work is a product of the staff of The World Bank with external contributions. The findings, interpretations, and conclusions expressed in this work do not necessarily reflect the views of The World Bank, its Board of Executive Directors, or the governments they represent.

The World Bank does not guarantee the accuracy of the data included in this work. The boundaries, colors, denominations, and other information shown on any map in this work do not imply any judgment on the part of The World Bank Group concerning the legal status of any territory or the endorsement or acceptance of such boundaries.

Rights and Permissions
The material in this work is subject to copyright. Because The World Bank Group encourages dissemination of its knowledge, this work may be reproduced, in whole or in part, for noncommercial purposes as long as full attribution to this work is given.

Any queries on rights and licenses, including subsidiary rights, should be addressed to the Office of the Publisher, The World Bank, 1818 H Street NW, Washington, DC 20433, USA; fax: 202-522-2422; e-mail: pubrights@worldbank.org.

Photos
© World Bank

TABLE OF CONTENTS

ABBREVIATIONS AND ACRONYMS i
FOREWORD ii
ACKNOWLEDGEMENTS iii
EXECUTIVE SUMMARY v

PART 1: THE STATE OF KENYA'S ECONOMY

1. Recent Economic Developments: 2016 in Retrospect 2
   - 1.1 Economic Activity in Kenya Remained Robust in 2016 2
   - 1.2 Growth was Broad-based with the Service Sector Being the Most Dynamic 2
   - 1.3 The Macroeconomic Environment was Stable in 2016 4
   - 1.4 Fiscal Consolidation Remains a Challenge 6
   - 1.5 Financial Markets Faced a Tough Environment in 2016 9

2.The Changing Economic Landscape and Kenya's Growth Prospects 10
   - 2.1 Emerging Head and Tail Winds Influencing the Economic Landscape 10
   - 2.2 How Will These Emerging Head and Tail Winds Impact on Growth Prospects? 12

3. Downside Risks to the 2017 Growth Outlook 14
   - 3.1 Domestic Risks 14
   - 3.2 External Risks 15

4. Policies 15
   - 4.1 Kenya Needs to Safeguard its Robust Performance and Accelerate Growth Potential 15
   - 4.2 Prudent Fiscal and Monetary Policies will be Critical to Safeguard Macro Stability 16
   - 4.3 Structural Reforms will be Required to Unleash Further Productivity Gains 16

PART 2: SPECIAL FOCUS

5. Affordable Housing and Housing Finance 24
   - 5.1 Housing and Housing Finance in Kenya – Unaffordable and Unavailable 26
   - 5.2 Investing in Affordable Housing Pays Off 27
   - 5.3 What is Holding Back Affordable Housing? 27
   - 5.4 It's More Than Finance Constraining Affordable Housing 30
   - 5.5 Innovative Instruments to Address Financing Can Be Catalytic 32
   - 5.6 Regulatory Reforms for Unleashing Housing Finance Supply and Demand 37
   - 5.7 Accompanying Housing Finance Reforms 38
   - 5.8 What Role can the Government Play? 39

REFERENCES 42
STATISTICAL TABLES 43

LIST OF FIGURES

Figure 1: Annual GDP growth ... 2
Figure 2: Contribution by sector to GDP growth ... 2
Figure 3: Contribution to GDP growth by service sector ... 3
Figure 4: Agricultural growth year-on-year ... 3
Figure 5: Leading Economic Indicators year-to-date growth rates ... 4
Figure 6: Contribution to GDP growth by Industry ... 4
Figure 7: After remaining within the target band for 2016, headline inflation breached it in 2017 ... 4
Figure 8: Energy and food Inflation have been the main drivers of headline inflation in recent months ... 4
Figure 9: Central Bank Rate ... 5
Figure 10: The Exchange rates has remained relatively stable since the beginning of 2016 ... 5
Figure 11: Current Account Balance improves ... 5
Figure 12: Capital Account (% of GDP) ... 5
Figure 13: Fiscal Deficit (% of GDP) ... 6
Figure 14: Breakdown of Government Expenditure ... 6
Figure 15a: Revenue Targets Vs Actual (% of GDP) ... 7
Figure 15b: Breakdown of Government Revenue (% of GDP) ... 7
Figure 16: External Debt Vs Domestic Debt (% of public debt as at Sept16) ... 9
Figure 17: Composition of External and Domestic Debt ... 9
Figure 18: Government T-Bill rates ... 9
Figure 19: NSE 20 Share Index ... 9
Figure 20: Historical rainfall pattern over long rains (March-May) ... 11
Figure 21: Projected rainfall pattern for the upcoming long rains (March-May 2017) ... 11
Figure 22: Fiscal Deficit (% of GDP) ... 12
Figure 23: Accumulated response of GDP to real oil price increase ... 13
Figure 24: Accumulated response of inflation to real oil price increase ... 13
Figure 25: GDP growth and Output gap ... 14
Figure B.2: Annual Targets Vs. Actual Collections, Kshs. ... 22
Figure B.4: Trends in remittances, ODA and FDI to Kenya ... 24
Figure B.5a: Urban and Rural Population (millions) ... 26
Figure B.5b: Total Housing Needs (000s) ... 26
Figure 26: Mortgage Loans Outstanding as % of GDP (2015/16) ... 28
Figure 27: Four Levers to Address Global Affordable Housing Challenges ... 30
Figure 28: Systematically Addressing Affordable Housing ... 30

LIST OF TABLES

Table 1.1: Medium Term Growth Outlook (percent, unless stated) ... 14
Table 1.2: Affordability Calculator ... 29

LIST OF BOXES

Box B.1: Is Kenya Loosing Competitiveness in the East African Market? ... 20
Box B.2: Trends in County Level Fiscal Management ... 22
Box B.3: M-Akiba: Another First For Kenya ... 23
Box B.4: Diversifying Financing Sources Via Floating a Diaspora Bond ... 24
Box B.5: Kenya's Growing Population and its Housing Needs ... 26
Box B.6: Findings of the Kenya Mortgage Refinance Company (KMRC) feasibility ... 33
Box B.7: The Nigeria Mortgage Refinance Company ... 34
Box B.8: The Moroccan Guarantee Scheme for Low Income Housing Finance ... 34
Box B.9: Testing the Water: A PPP in Affordable Housing in Kenya ... 35
Box B.10: A SMART Demand Side Subsidy Mechanism: France - The Zero Percent Housing Loan ... 35
Box B.11: India Lending Model for Informal Borrowers and Informal Property ... 36

ABBREVIATIONS

CBK	Central Bank of Kenya
CBR	Central Bank Rate
EAC	East African Community
EAP	East Asian Pacific
FY	Financial Year
FEWSNET	Famine Early Warning System Network
FDI	Foreign Direct Investment
FOGARIM	Moroccan Government Mortgage Program
GDP	Gross Domestic Product
H1, H2	First Half, Second Half
HMF	Housing Microfinance
HS	Harmonized System
HOFINET	Housing Finance Information Network
IMF	International Monetary Fund
KEU	Kenya Economic Update
KMRC	Kenya Mortgage Refinance Company
KUSCCO	Kenya Union of Saving & Credit Co-operatives
LAPSSET	Lamu Port-South Sudan-Ethiopia-Transport
LOC	Line of Credit
LR	Local Revenue
MAD	Moroccan Dirham
MFIs	Microfinance Institutions
MRC	Mortgage Refinance Companies
MTP	Medium Term Plan
MNOs	Mobile Network Operators
NACHU	The National Cooperation Housing Union
NBFIs	Non-Bank Financial Institutions
NEER	Nominal Effective Exchange Rate
NEDI	North and North-Eastern Development Initiative
NHB	National Housing Bank
NMRC	Nigeria Mortgage Refinance Company
NSSF	National Social Security Fund
NIM	Net Interest Margin
OCED	Organization for Economic Cooperation and Development
ODA	Official Development Assistance
OSR	Own Source of Revenue
O&M	Operations and Maintenance
PAYE	Pay As You Earn
PPPs	Public-Private Partnership
PFM	Public Finance Management
Q1,2,3,4	Quarter One, Two, Three, Four
REER	Real Effective Exchange Rate
SACCOs	Savings and Credit Cooperative Organizations
SASRA	SACCO Societies Regulatory Authority
SGR	Standard Gauge Railway
T-Bill	Treasury Bill
TMRC	Tanzania Mortgage Refinance Company
UK	United Kingdom
UN	United Nations
USA	United States of America
USD	United States Dollar
US	United States
VAT	Value Added Tax
WBG	World Bank Group

FOREWORD

It is my pleasure to present the fifteenth edition of the World Bank's *Kenya Economic Update*, at a critical juncture for Kenya as it transitions from the completion of the Second Medium Term Plan (MTP-II, 2013-2017) to MTP-III (2018-2022), which is currently under preparation. The report has four main messages.

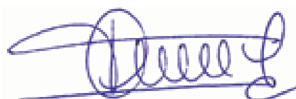
First, Kenya's economic growth continued to outperform its peers in 2016. In contrast to the slump in economic growth in Sub-Saharan Africa to 1.5 percent (a three decade low), growth in Kenya accelerated for the third consecutive year reaching 5.8 percent. Kenya's robust growth performance was supported by lower oil prices, favorable agriculture output in the first half of 2016, a tourism sector rebound, strong inward remittances, a relatively stable macroeconomic environment and improvements in the steady easing of certain supply-side constraints due to earlier public investments.

Secondly, due to emerging headwinds, economic activity in Kenya will encounter some speed bumps in the near to medium term which will likely impact MTP-II implementation and should inform the scope of the MTP-III. These headwinds include, the ongoing drought, depressed private sector credit growth, the rise in oil prices, and fiscal pressures. However, the completion of phase one of Standard Gauge Railway and a projected strengthening of the global economy is expected to provide some tailwind. The net effect of these changes in the economic landscape will likely cause near term growth to moderate to 5.5 percent in 2017 before picking up to 6.1 percent by 2019 as headwinds (e.g. drought) subside.

Third, sustaining Kenya's robust growth will require safeguarding its hard earned macroeconomic stability by continuing to implement prudent fiscal and monetary policies. The consolidation of the fiscal stance in line with the Medium Term Fiscal Framework should help anchor macroeconomic stability and create the fiscal space for a public investment drive supportive of the medium term plans. Further, given the systemic importance of the banking sector, addressing the unintended consequences of the interest rate caps should help strengthen financial intermediation in the Kenyan economy.

Finally, while Kenya's growth has been robust, there are latent opportunities to accelerate growth to levels necessary to achieve Vision 2030. This report identifies some of these growth and job-creation opportunities as well as the need to address a critical social need by supporting the development of the housing market for lower income households in Kenya. On the demand side, a key constraint to housing is finance. The report addresses policy measures that can be taken to alleviate the housing finance problem, including those that have worked well in other middle income countries.

The World Bank remains committed to working with key Kenyan stakeholders to identify potential policy and structural issues that will enhance economic growth and keep Kenya on the path to upper middle income status in accordance with the aspirations of Vision 2030. The semi-annual Kenya Economic Update offers a forum to discuss these development trends. We hope that you too will join us in debating topical policy issues that can contribute to fostering growth, shared prosperity and poverty reduction in Kenya.



Diariétou Gaye
Country Director for Kenya
World Bank

ACKNOWLEDGEMENTS

This fifteenth edition of the *Kenya Economic Update* was prepared by a team led by Allen Dennis. The team included Mehnaz Safavian, Jane Kiringai, Simon Christopher Walley, Christine Awiti, Celina Mutie, Rajiv Daya, Uloaku Oyewole, and Patrick Nderitu.

The team acknowledges contributions from Keziah Muthembwa, Vera Rosauer, Anne Khatimba, Charles Muiru, Robert Waiharo, Dasan Bobo and Sarah Farhat.

The report benefitted from insights of several peer reviewers including Gerard Kambou and Loic Chiquier, as well as comments from Catherine Masinde and Sheila Kamunyori.

The team also received overall guidance from Abebe Adugna Dadi (Practice Manager, Macroeconomic and Fiscal Management), James Seward (Practice Manager, Finance and Markets); Kevin Carey (Lead Economist, Macroeconomic and Fiscal Management), Johan Mistiaen (Program Leader for Kenya, Uganda, Rwanda and Eritrea) and Diarietou Gaye (Country Director for Kenya, Uganda, Rwanda and Eritrea).

Partnership with key Kenyan policy makers was instrumental in the production of the report. On March 9, 2017, a draft report was presented at the 21st Economic Roundtable. The meeting was attended by senior officials from The Treasury, The Central Bank of Kenya, The Kenya Revenue Authority, The Kenya Institute for Public Policy Research and Analysis, The Ministry of Land, Housing and Urban Development and The International Monetary Fund.

EXECUTIVE SUMMARY

Economic activity in Kenya remained robust in 2016. For the third consecutive year economic activity in Kenya picked-up, reaching an estimated of 5.8 percent in 2016, once again placing Kenya among the fastest growing economies in Sub-Saharan Africa. Kenya's growth momentum in 2016 was supported by a stable macroeconomic environment, low oil prices, favorable harvest in the first half of 2016, rebound in tourism, strong remittance inflows, and an ambitious government infrastructure drive to relieve supply side constraints.

Near term GDP growth is expected to dip on account of headwinds, however over the medium term GDP growth should pick-up. Given headwinds from the ongoing drought, weak credit growth, and the pick-up in oil prices, GDP growth is expected to decelerate to 5.5 percent in 2017, a 0.5 percentage point mark down from earlier forecasts. However, over the medium term, we expect these headwinds to ease (rains are expected to return to normal in 2017), and together with the projected steady strengthening of the global economy, rebound in tourism, resolution of some of the underlying causes of slow credit growth, and the easing of some supply-side constraints related to the completion of some major infrastructure projects, GDP growth is expected to accelerate to 5.8 percent and 6.1 percent in 2018 and 2019 respectively, consistent with the underlying growth potential of the Kenyan economy.

Downside risks to Kenya's outlook remain broadly unchanged. Identified risks include from domestic sources such as the potential for fiscal slippages, drought conditions being prolonged beyond 2017, and security concerns. External risks to Kenya's growth prospects could emanate from weaker than expected growth among Kenya's major trading partners and uncertainties related to US interest rate hikes that could lead to a strengthening of the dollar and destabilizing capital flows from emerging and frontier markets including from Kenya.

Going forward, prudent macroeconomic policies will help safeguard Kenya's robust economic performance. Kenya's relatively stable macroeconomic environment has been supportive of its growth performance in recent years. Maintaining macroeconomic stability calls for continued implementation of prudent fiscal and monetary policies. On the fiscal front, given the elevated levels of the deficit as well as the lowering of margins for maneuver due to the rise in debt stocks, the implementation of the Medium Term Fiscal Framework which seeks to bring the deficit down to 4.3 percent by FY19/20 is a step in the right direction. Fiscal consolidation however, needs to be implemented in such a way as not to compromise public investments in critical infrastructure that will unlock the economy's productive capacity. Secondly, given low private sector credit growth and the ongoing unintended adverse effects of interest rate caps the Banking Amendment Act needs to be revisited.

Further, structural reforms can accelerate the growth potential of the Kenyan economy. While Kenya's growth has been robust in recent years, it still falls short of the levels envisaged in the Medium Term Plan II and what is required to transform Kenya into an upper middle income economy by 2030. Reaching the target higher level of growth is possible, but will however require an acceleration in the pace of structural reforms. The report highlights select areas that hold potential to accelerate Kenya's growth potential. First, beyond changes to the Banking Amendment Act **access to credit by the private sector** could be improved by strengthening credit reporting to the Credit Reference Bureaus; creating a central electronic collateral registry; developing a framework to promote property as collateral; completing the computerization of land registries; and implementing the National Payments System Act and regulations. Secondly, efforts to influence the competiveness of agricultural input (seeds, fertilizer, leasing machinery etc.) and output markets (including from tariff and non-tariff barriers) can help address low **productivity in the agricultural sector**. Last but not least, new engines for economic development need to be supported. One such sector is in addressing the huge housing deficit, especially among lower income households. Unlocking the residential **housing market** through the development of the housing finance market can provide a wide range of income opportunities through the construction sector and related industries.

The focus section of this report is dedicated to analyzing Kenya's housing market and the policies that can be put in place to make housing more affordable to many Kenyans.

Indeed, the Constitution of Kenya 2010 establishes the right to housing as an enforceable socio-economic right. It states that 'every person has the right to accessible and adequate housing and to reasonable standards of sanitation'. This key priority for the Government of Kenya has been reiterated in the country's first medium term plan (MTP I, 2009-2012) and second medium term plan (MTP for 2013-17) under the Vision 2030 Strategy. These blueprints have targeted the provision of 200,000 housing units annually for all income levels. However, production of housing units — currently at less than 50,000 units annually — has been well below the targeted level, culminating in a housing deficit of over 2 million units, with nearly 61 percent of urban households living in slums. This deficit continues to rise due to fundamental constraints on both the demand and supply side of housing provision and is exacerbated by an urbanization rate of 4.4 percent, equivalent to 0.5 million new city dwellers every year.

Numerous benefits can be attributed to improving access to housing finance, including economic growth, job creation, and deepening of the financial sector. There are various global examples supporting the "housing multiplier effect" as every dollar spent directly on a housing unit results in various indirect benefits to the country. Kenya has the right fundamentals in place to achieve results on a scale of significant magnitude. Collaborative efforts between government and the private sector are required, however it is imperative to create a supportive policy and regulatory environment so that the suggested tools can be effectively leveraged.

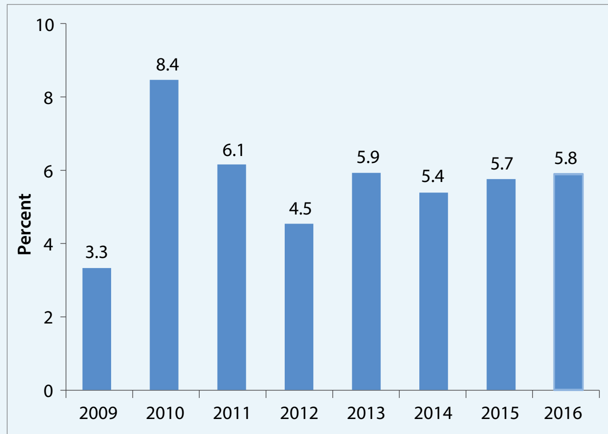
A crucial aspect of the problem lies in the ever growing affordability gap in the housing market, and lack of financing for both developers and end users. The inaccessibility of affordable housing finance is highlighted by the fact that there are fewer than 25,000 mortgages outstanding in Kenya. Mortgage debt in 2015 represented 3.15 percent of GDP and this is substantially lower than developed countries. Banks have limited access to long-term funding and few institutions have accessed the capital markets to fund mortgages. Of particular interest is the fact that less than 10 percent of all housing credit comes in the form of mortgages from the banking sector – the remainder of housing finance comes from SACCOs and housing cooperative networks. These institutions are therefore integral to any meaningful financing solution. However, SACCOs have only one main source of liquidity, which are member deposits. Without access to longer term sources of finance, their loan portfolio will be unable to grow further.

Financing solutions can play a catalytic role in stimulating both supply and demand of affordable housing, and can help create momentum for other underlying reforms outside the sector. On the supply side, such solutions that have been used in other emerging markets include the creation of Mortgage Refinance Companies (MRCs), the provision of Housing Finance Guarantees, and developing Public-Private Partnerships (PPPs) for Affordable Housing. Focusing on affordability and the provision of products aimed at informal income can increase the demand for financial products for housing. Examples implemented in other emerging markets include Interest Rate/Down Payment Buy Downs and a focus Housing Microfinance through microfinance institutions and SACCOs. Experiences from these other jurisdictions is that the creation or focus by Government on such initiatives can also lead to wide consultation and the creation of inter-ministerial committees dedicated to needed reforms for the affordable housing agenda.

Innovative financing instruments must also be accompanied by policy reforms to be effective. Such reforms include the standardization of mortgage contracts, the establishment of appropriate mortgage foreclosure regulations, a clear legal and regulatory framework for mortgage-backed securities and covered bonds and creation of a conducive environment to mobilize long-term domestic capital. Underpinning these reforms is the imperative inclusion of cooperatives and SACCOs in affordable housing.

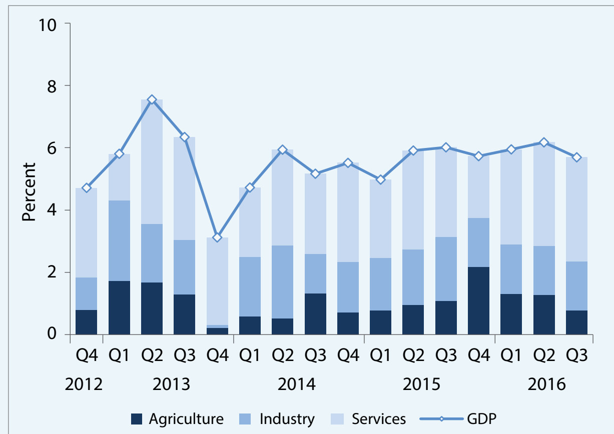
The Government of Kenya could rely on the private sector to provide financing for affordable housing, with government actively supporting the sector by creating the right environment for lenders and developers. Such support can come in the form of working with the private sector to attract financing through catalytic financing instruments, improving access to land, providing basic infrastructure, improving the efficiency of processes (e.g. accelerating mortgage registration and title transfers) and improving the credit and macroeconomic environment.

GDP growth remained robust in 2016
Annual GDP growth



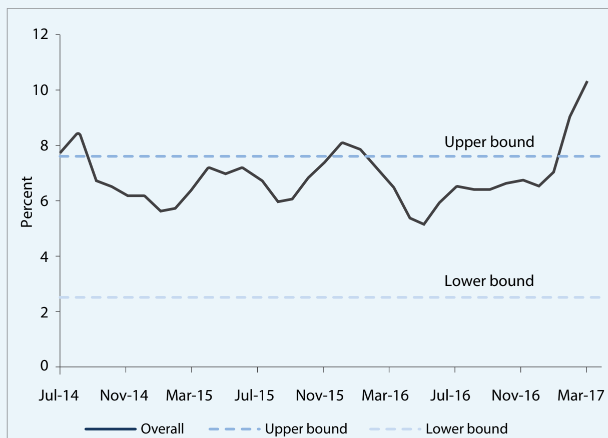
Source: Kenya National Bureau of Statistics; Note: 2016 is an estimate

…driven primarily by a pick-up in the services sector
Contribution by sector to GDP growth



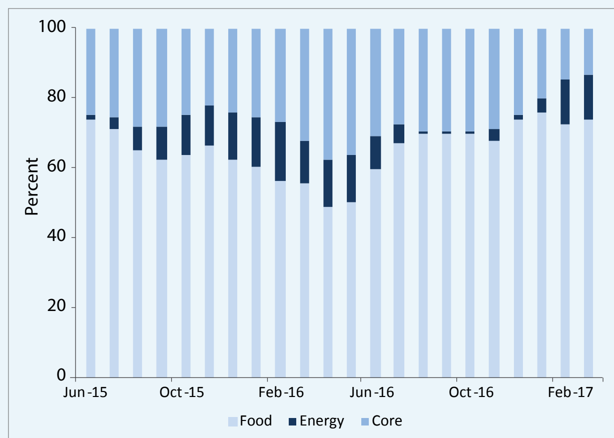
Source: World Bank computation based on data from Kenya National Bureau of Statistics

The stable macroeconomic environment supported economic activity in 2016
Inflation



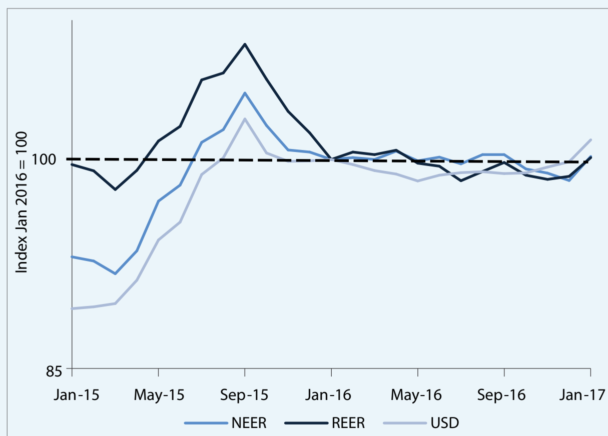
Source: Kenya National Bureau of Statistics

Core inflation remains subdued, however the recent drought and rise in oil prices have contributed to a surge in inflation



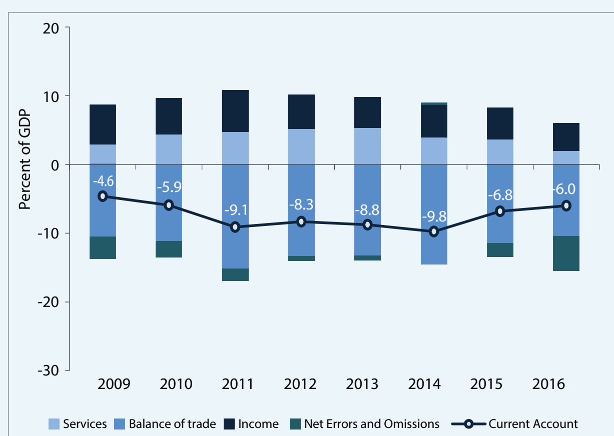
Source: World Bank computation based on data from Kenya National Bureau of Statistics

The shilling was relatively stable in 2016



Source: Central Bank of Kenya

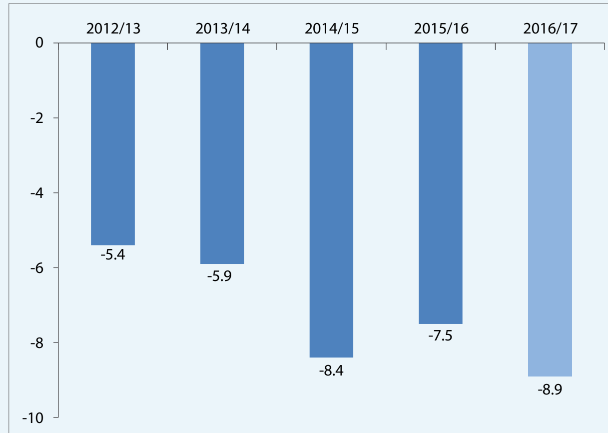
…and lower oil prices contributed to an improvement in current account balance
Current account balance



Source: Central Bank of Kenya

Fiscal consolidation remains a challenge

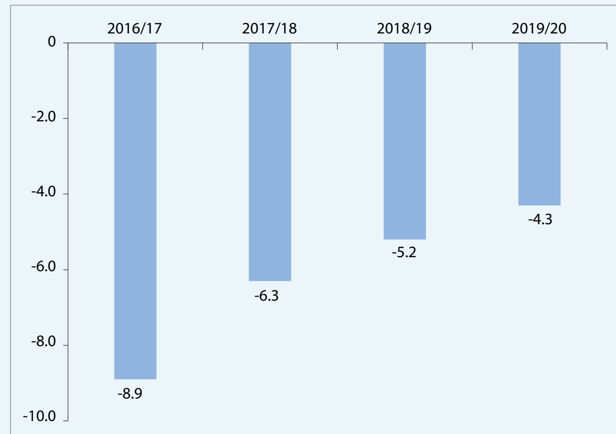
Fiscal deficit (% of GDP)



Source: The National Treasury

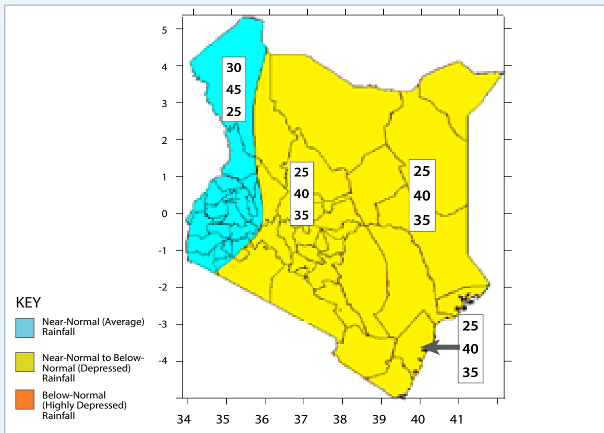
…however the Medium Term Fiscal Framework points to a pathway of fiscal consolidation

Fiscal deficit (% of GDP)



Source: The National Treasury

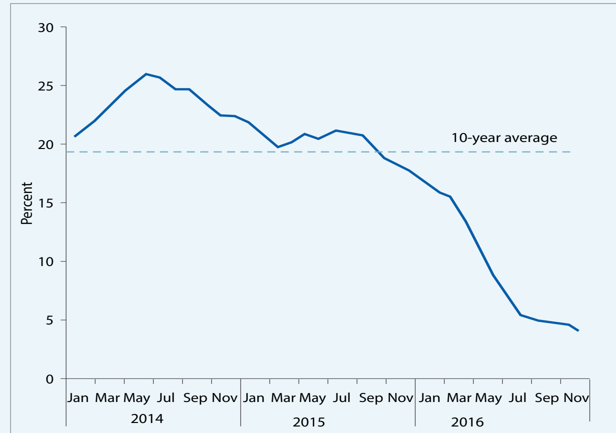
Rainfall projections suggest that the upcoming long rains (March-May 2017) will be depressed across the country



Source: Kenya Meteorological Department

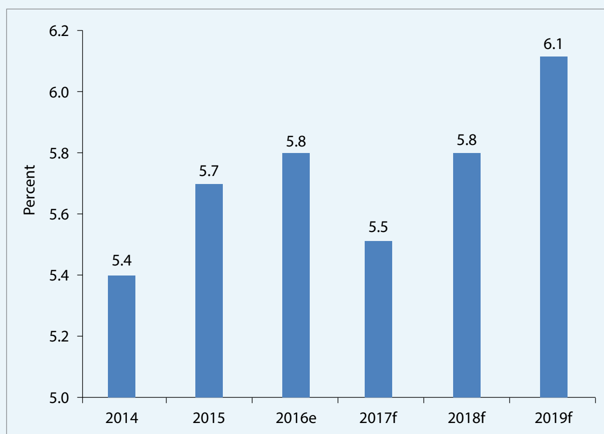
….and private sector credit growth remains well below the historical average

Credit to Private Sector



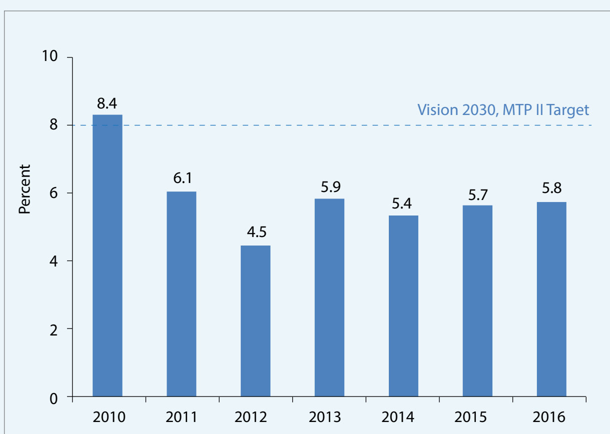
Source: Central Bank of Kenya

Near term growth is expected to dip on account of emerging headwinds, but expected to rebound in the near term as headwinds ease-off



Source: World Bank

Though Kenya's growth remains robust, to attain its aspiration of becoming an upper middle-income economy by 2030 will require even higher levels of growth



Source: World Bank

The State of Kenya's Economy

1. Recent Economic Developments: 2016 in Retrospect

1.1 Economic Activity in Kenya Remained Robust in 2016

1.1.1. **For the third consecutive year, economic activity in Kenya picked-up.** Kenya's economy is estimated to have expanded by 5.8 percent in 2016, 0.1 percentage points higher than the previous year, and the fastest pace of expansion since 2011 (Figure 1). Against a background of weaknesses in several emerging markets and Sub-Saharan economies where GDP growth decelerated, this economic performance was even more remarkable.

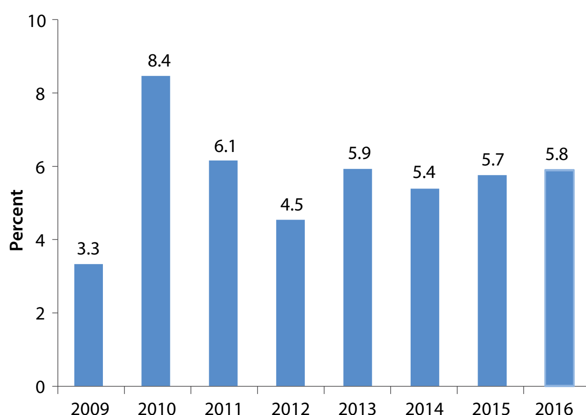
1.1.2. **Tail winds from the global economy, exogenous factors and domestic developments supported economic activity in 2016.** Unlike oil exporting countries whose economies have been battered by the slump in commodity prices (e.g. Nigeria and Angola), Kenya, being an oil importer, benefitted from the slump in oil prices, particularly in the first half of 2016, and this provided further impetus to the Kenyan economy. Similarly, earlier good rains supported favorable harvests in 2016, particularly in the first half of the year. Further the tourism sector, which had slowed down since the 2013 terrorist attacks, rebounded in 2016, as key source countries lifted travel warnings on account of an improving security situation. Lastly, domestic developments such as the government's infrastructure drive aimed at easing supply side constraints and a stable macroeconomic environment, supported economic activity in 2016. Notwithstanding these favorable developments, the weakness in external demand and the sharp deceleration in credit growth to the private sector weighed down on growth performance in 2016.

1.1.3. **Kenya's growth is inching closer to the East African Community (EAC) high performers**. While Kenya's growth has lagged behind her EAC peers, with Tanzania and Rwanda averaging 7.1 and 7.3, respectively, between 2014 and 2016, Kenya's growth is inching closer to the EAC average. At an estimated 5.8 percent in 2016, Kenya's growth is lower than the EAC average by 0.2 percentage points compared to 1.0 percentage points in 2014. Estimated at 6.9 percent in 2016, Tanzania's growth will be sustained at 6.8 percent in 2017 and is expected to pick up to 7.4 percent in 2018, supported mainly by strong growth in the industrial sector. On the other hand, the Ugandan economy slowed down in 2016 by 0.4 percentage points to 4.6, but is expected to pick up in 2017 to 5.6 percent driven by an industry sector that is set to pick up pace.

1.2 Growth was Broad-based with the Service Sector Being the Most Dynamic

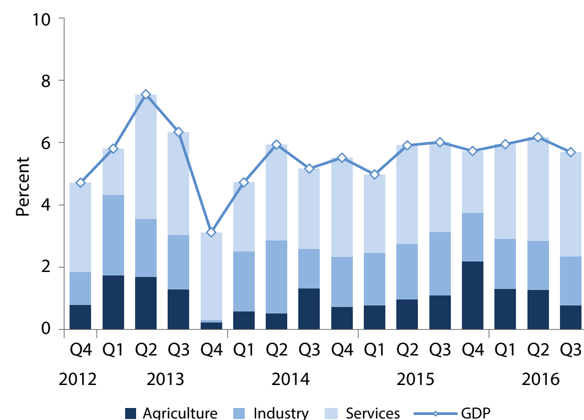
1.2.1. **The service sector sustained its vibrancy in 2016.** The service sector, which accounts for some 50 percent of GDP, contributed 3.2 percentage points to Kenya's GDP growth for the first three quarters of 2016. In other words, some 54 percent of Kenya's growth in 2016 derived from the strength of the service sector (Figure 2). Performance among various service sub-sectors was, however, mixed. Driven by the rebound in the tourism sector, accommodation and restaurant sub sector, whose contribution to GDP growth was negative in 2015, tourism grew by 6.9 percent for the first three quarters of 2016, contributing some 0.41 percentage points to GDP growth. Another service sub-sector whose growth accelerated in 2016 was transport and storage, which largely benefitted from lower fuel prices.

Figure 1: Annual GDP growth



Source: Kenya National Bureau of Statistics;
Note: 2016 is an estimate

Figure 2: Contribution by sector to GDP growth



Source: World Bank computation based on data from Kenya National Bureau of Statistics

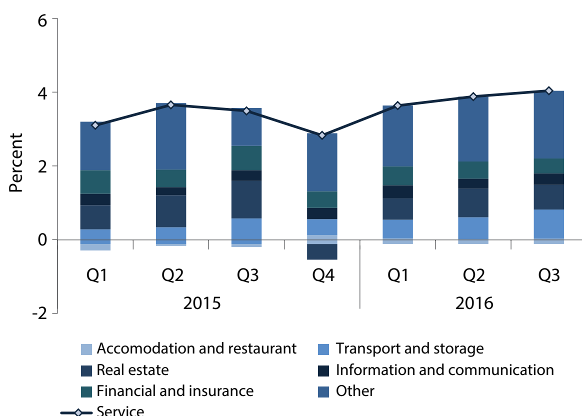
1.2.2. However, the vibrancy previously witnessed in some service sectors dimmed in 2016. In contrast, while Kenya's real estate sector remained buoyant in 2016, it expanded at a slower pace in 2016 (7.6 percent in the first three quarters of 2016 compared with 9.8 percent over the same period in 2015). The deceleration could be reflective of the slowing private sector credit growth. Similarly, in 2016, the financial sector contributed 0.3 percentage points to GDP growth, a decline by half compared to its contribution to GDP of some 0.6 percentage points in 2015 (Figure 3). The decline in the contribution of the financial services is consistent with tougher environment faced by Kenyan banks in 2016 — tighter regulatory conditions for the provisioning of bad debts and lower interest margins resulting from the Banking Amendment Act. However, on a positive note, innovations in mobile technology and its application in the banking sector have continued rapidly and with it financial inclusion. For instance, notwithstanding the sluggishness of credit growth through traditional channels, Equity Bank reported a spike in lending through its mobile banking platform to Ksh 30billion in the first three quarters of 2016 from Ksh 1.5billion over the same period in 2015. Data from the CBK also supports this general trend as both the number and value of transactions over the same period for 2016 grew by some 36.4 and 19.5 percent, respectively.

1.2.3. The agriculture sector's performance was dependent on rains, leading to a year of two halves. Agricultural output grew at 4.9 percent in first three quarters of 2016, which was higher than the 4.0 percent growth realized over the same period in 2015. As a result, the sector's contribution to growth increased by 0.2 percentage points from that of the 2015 (Figure 4). However, reflecting the rain-dependent nature of Kenya's agriculture sector, 2016 witnessed two halves in terms of agricultural performance. Having benefitted from earlier rains, harvests in the first half of 2016 were solid. However, given the delayed rains during the long, rainy season (March-May), agricultural output growth weakened later in the year.

1.2.4. All key commodities were affected by weather patterns in 2016. Tea production increased in Q1 2016 compared to Q1 2015 (Figure 5). However, the bright spell came to an end with tea production experiencing a drop in subsequent quarters to 2015 levels, a development attributable to changing weather conditions. Similarly, coffee and horticulture production saw an increase in Q1 of 2016, however, in Q2 and Q3 2016, it declined and is expected to have been even lower in Q4 2016 due to the delayed and less than average rains.

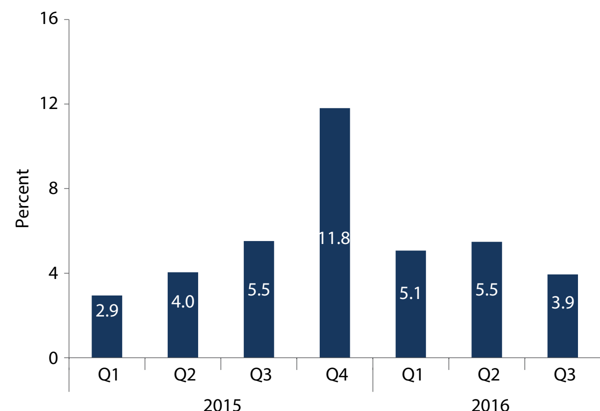
1.2.5. Weighed down by sluggish manufacturing and construction, industrial output growth decelerated in 2016. For the first three quarters of 2016, Kenya's industrial sector expanded by 5.6 percent compared to the 7.3 percent recorded in 2015. As a result, its contribution to GDP growth decelerated to 1.6 percentage points from 1.8 percentage points over the same period in 2015 (Figure 6). Much of this deceleration in growth can be attributed to sluggish/below par growth in the manufacturing sector and lesser dynamism in the construction sector. At 9.5 percent, the latter sector's growth was still bristle, even if less than the 13.5 percent recorded in 2015. Both sub-sectors growth performance was undermined by the sharp deceleration in credit growth. The sluggishness of the manufacturing, which grew at 2.4 percent in 2016, can be attributed to competitiveness challenges in the sector. This is reflected in the systematic loss of market share to their competitors both on the domestic market (e.g. in Cement production) as well as in key manufactured export markets in the EAC.

Figure 3: Contribution to GDP growth by service sector



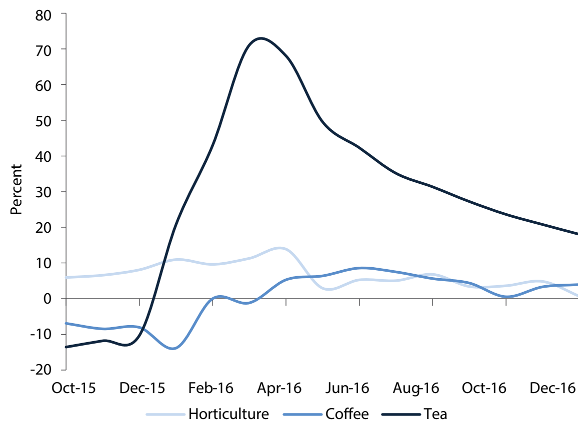
Source: Kenya National Bureau of Statistics

Figure 4: Agricultural growth year-on-year



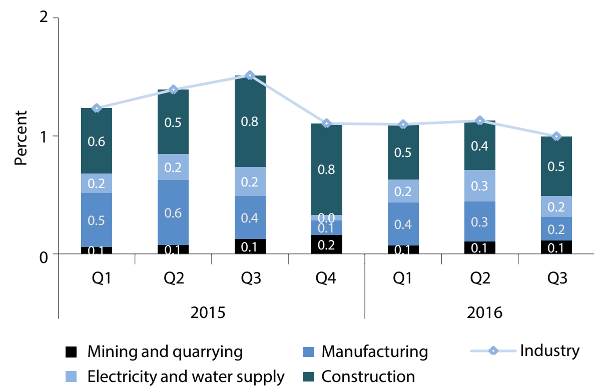
Source: Kenya National Bureau of Statistics

Figure 5: Leading Economic Indicators year-to-date growth rates



Source: Kenya National Bureau of Statistics

Figure 6: Contribution to GDP growth by Industry

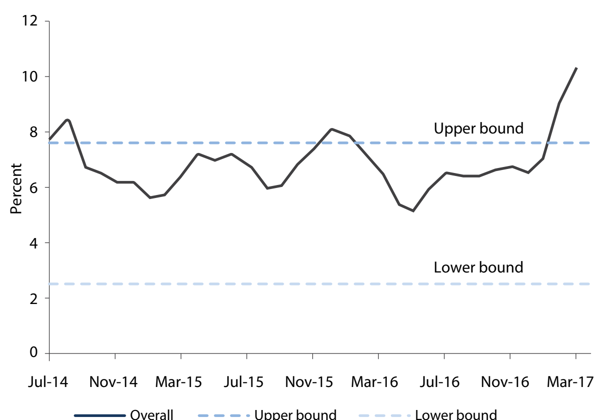


Source: Kenya National Bureau of Statistics

1.3 The Macroeconomic Environment was Stable in 2016

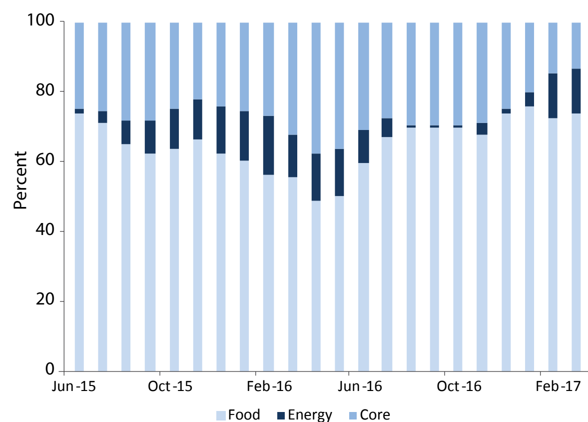
1.3.1. Inflation moderated in 2016, however unfavorable weather has since led to a surge in food inflation in recent months. From an 18-month high of 8.0 percent at the end of 2015, headline inflation declined to 6.4 percent in December 2016 (Figure 7). This was driven in part by lower oil prices as reflected in lower energy inflation, which stood at a historical low of 0.1 percent in December 2016 compared to 2.9 percent at the beginning of the year. Reflecting underlying subdued demand pressures and the waning pass-through effects from earlier volatility in the shilling, core inflation declined to 3.4 percent in December 2016 from 5.4 percent at the beginning of the year. Trends in food price inflation reflected the effects of the changing weather patterns. In the earlier half of the year when rainfall patterns supported favorable harvests, food inflation sharply decelerated from 13.3 percent in December 2015 to a low of 6.6 percent in June 2016. However, adverse rainfall patterns in the second half of the year drove food inflation to a near year high of 11.2 percent at the end of 2016. This rise in food inflation has persisted in 2017, reaching 18.6 percent in March 2017 and contributed some 76 percent of headline inflation (compared to 59 percent in May 2016, when agricultural output was more favorable), thereby showing that the rise in food prices has been the main driver of headline inflation (Figure 8). Along with the rise in food prices, energy inflation is also on the rise, reflecting the pass-through of higher oil prices in global markets to the domestic market. Notwithstanding subdued demand pressures, as reflected in low core inflation (a 5-year low of 3.3 percent in March 2017), the increase in both food and energy inflation led to the breaching of upper end of the inflation corridor (7.5 percent) in February and March 2017, with headline inflation rising to 9.0 and 10.3 percent respectively.

Figure 7: After remaining within the target band for 2016, headline inflation breached it in 2017



Source: Kenya National Bureau of Statistics

Figure 8: Energy and food Inflation have been the main drivers of headline inflation in recent months

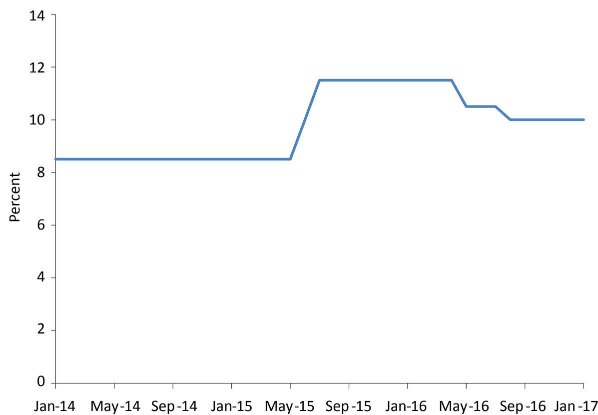


Source: World Bank computation based on data from Kenya National Bureau of Statistics

1.3.2. **The benign inflationary environment enabled the Central Bank to adopt a more accommodative monetary stance in 2016.** With inflation on a downward trajectory (in particular core inflation), policy rates were twice cut by a total of 150 basis points in 2016, thereby partially unraveling the 2015 interest rate hikes that were needed at the time to stabilize the macroeconomic environment (Figure 9). However, despite the interest rate cuts, the deceleration in private sector credit growth, which commenced in 2014, continued unabated in 2016. By December 2016, credit growth to the private sector had dropped to a worryingly 13-year low of 4.3 percent. The ability of the CBK to influence credit growth through policy rates has however been compromised, given the direct linking of the CBR rate with the statutory interest rate ceiling (under the Banking Amendment Act), while yields on "risk free" government securities remain unimpeded. In other words, given the risk premium above government securities, policy rates set too close to risk-free government securities does not incentivize banks to lend to the private sector.

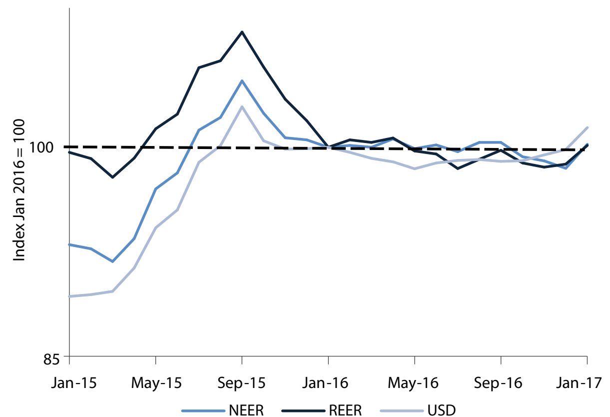
1.3.3. **Although depreciating towards the year's end, the shilling remained generally stable in 2016.** For the year 2016, the shilling depreciated by -1.5 and -1.2 percent on a nominal and real effective exchange rate basis (Figure 10). The decline in oil prices, strong remittance inflows and government borrowing in foreign currency, supported an earlier moderate appreciation of the shilling. However, seasonal increase in import demand towards the end of the year and the commencement of a hiking cycle by the US Federal Reserve which led to a strengthening dollar, combined to see a slide in the shilling in the Q4 2016 and the beginning of 2017. Kenya was not alone in the end of year slide in the value of its currency. Indeed, the strengthening of the dollar and the shifting market sentiment against emerging market assets impacted the currencies of several frontier and emerging markets. At 4.6 months of import cover, Kenya has an adequate import cover ratio. In addition, it has further buffers given the availability of the $1.5 billion IMF Standby Arrangement and Credit Facility.

Figure 9: Central Bank Rate



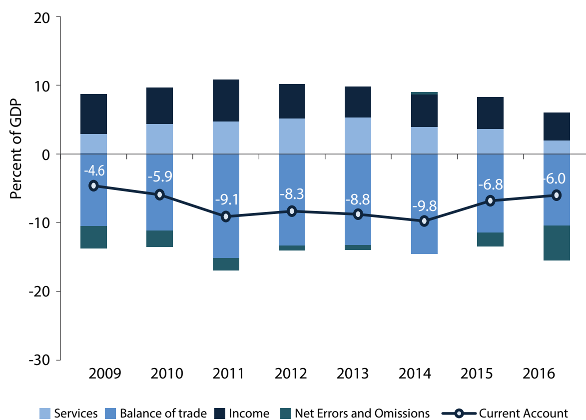
Source: Central Bank of Kenya

Figure 10: The Exchange rates has remained relatively stable since the beginning of 2016



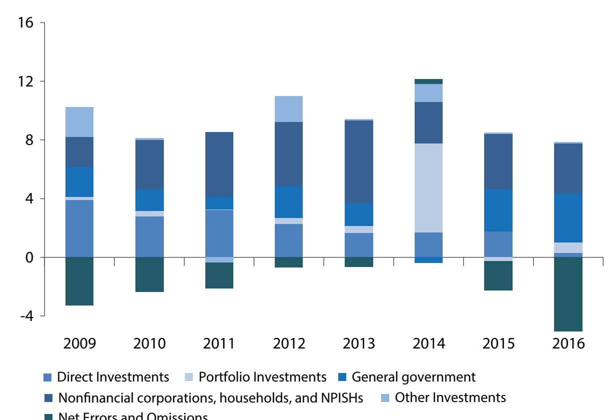
Source: Central Bank of Kenya

Figure 11: Current Account Balance improves



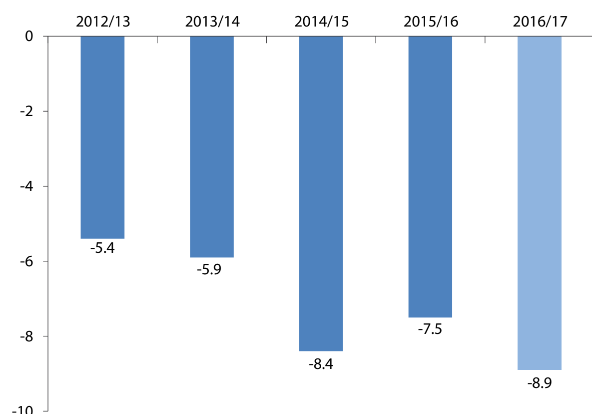
Source: Central Bank of Kenya

Figure 12: Capital Account (% of GDP)



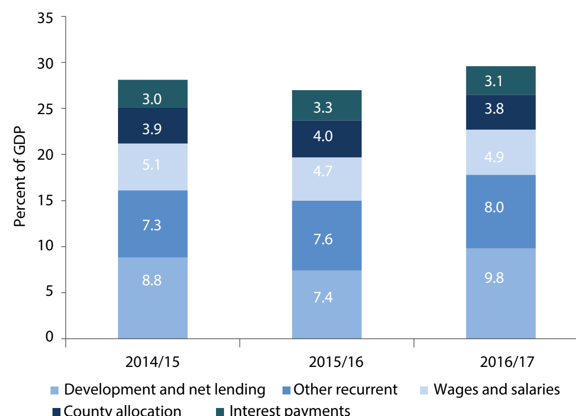
Source: Central Bank of Kenya

Figure 13: Fiscal Deficit (% of GDP)



Source: The National Treasury

Figure 14: Breakdown of Government Expenditure



Source: The National Treasury

1.3.4. **Overall, the current account position improved in 2016 to a 5-year low.** The current account balance fell to a 67-month low of 5.5 percent of GDP in May 2016. However, increasing oil prices in the latter half of the year contributed to a moderate expansion of the current account deficit to 6.0 in December 2016 (Figure 11). Besides developments in oil prices, the current account balance has been supported by increased diaspora remittances, which increased by 11.4 percent in the first three quarters of 2016 (remittances are estimated at 2.3 percent of GDP). In addition, traditional exports such as tea, coffee and horticulture performed well in H1 2016, driven by increasing commodity prices and good rainfall. However, overall export performance was weak, on account of Kenya's weakening exports to the EAC market (see Box B.1). On the financing of the current account deficit, inflows to the financial account improved in 2016 to about 11.0 percent of GDP compared to 8.0 percent in 2015. This was driven by increase in portfolio flows. However, there remains a large portion of the financial flows that are unclassified as the net errors and omissions remains sizeable at 5.0 percent of GDP.

1.4 Fiscal Consolidation Remains a Challenge

1.4.1. **The fiscal deficit declined from 8.4 percent of GDP in FY14/15 to 7.5 percent in FY15/16 (Figure 13).** Kenya's medium-term fiscal policy is anchored by its commitment to achieve convergence with the East African Community Monetary Union protocols, including the attainment of a 3.0 percent of GDP (inclusive of grants) fiscal deficit by FY2020/21. In FY15/16 fiscal consolidation was driven by adjustments on the expenditure front (i.e. from 28.2 percent of GDP in FY14/15 to 27.1 percent in FY15/16), in particular from reductions in development spending (Figure 14). In recent years, the government has embarked on an ambitious infrastructure drive (roads, railways, ports and power projects) to help relieve supply-side constraints and crowd-in private investment. The ambitious infrastructure plan drove the share of development spending to 8.8 percent of GDP in FY14/15 from 6.3 percent a year earlier. However, in FY15/16 development spending was moderated, thereby supporting the commencement of the fiscal consolidation. In contrast to development spending, recurrent spending has inched up by some 0.2 percentage points to 15.6 percent of GDP in FY15/16 (and is expected to rise to 16 percent in FY16/17). This reflects the challenges in containing both the rising interest payments on public debt as well as spending on wages and salaries.

1.4.2. **The pathway towards fiscal consolidation is a step in the right direction.** Fiscal consolidation should help anchor Kenya's macro stability, reduce crowding out pressures, contain the pace of debt accumulation (which has implications for lowering future interest payments) and contribute towards a more favorable sovereign debt credit rating which should help reduce the cost of external borrowing.

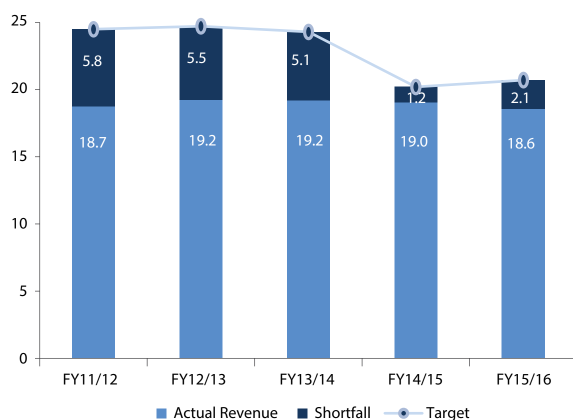
1.4.3. **However, the fiscal deficit is projected to rise in FY16/17 primarily on account of an increase in development spending.** In contrast to the consolidation that took place in FY15/16, the fiscal deficit is projected to rise to 8.9 percent of GDP in FY16/17. Given the projected increase in revenues (as a share of GDP), the increase in the deficit is being driven by an expansionary fiscal stance, with government expenditures increasing from 27.1 percent of GDP in FY15/16 to 30.0 percent in FY16/17. Of the 2.9 percentage points of GDP increase in government expenditures in FY16/17, 83 percent of that was due to

an increase in development spending (from 7.4 percent of GDP in FY15/16 to 9.8 percent in FY16/17), with the remainder attributable to an increase in recurrent spending. Excluding, development spending and county allocations, government expenditures are up by 0.4 percentage points of which 0.2 percentage point of GDP is due to an increase in wages and salaries. The significantly higher deficit, however, assumes that there will be a full execution of the development budget in FY16/17. Given the track record of 31 percent under-execution rate for development spending, it is likely deficit outturns could be lower than current projections. Nonetheless, given the already elevated deficit levels, any further increase is a cause for concern and risks undoing Kenya's hard earned macroeconomic stability.

1.4.4. **There is a need to recreate fiscal space to support the public investment drive.** Indeed, the projected rise in the fiscal deficit brings to the fore, the difficulty authorities face in creating the necessary fiscal space through reductions in the share of recurrent spending, and expansion of the revenue base in order to carry out the ambitious public investment drive without straining public finances. Recent wage agitations among public sector workers (doctors, lectures, nurses and teachers) continue to put pressure on current and future wage bills. Further, reflecting the rise in debt levels, interest payments are also taking a large share of expenditures (from 2.1 percent of GDP in FY11/12 to a projected 3.2 percent in FY16/17). The challenges in constraining recurrent expenditures thereby reduces fiscal space for the much needed capital spending, and makes it more challenging to pursue the pathway of medium-term fiscal consolidation.

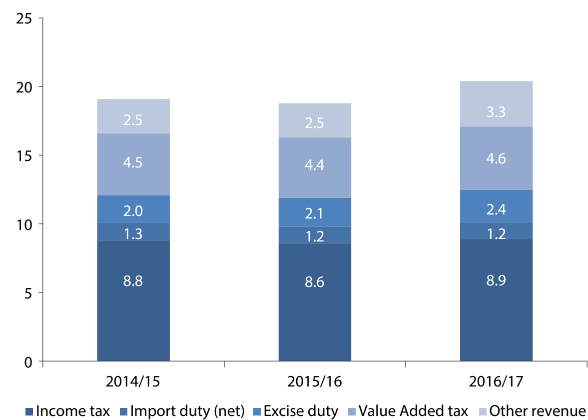
1.4.5. **Recreating fiscal space will require improvements in revenue performance.** In part, the challenge of fiscal consolidation has been the underperformance of government revenues. Over the past few years, revenue targets have persistently been above the actuals (Figure 15a). In the fiscal year ended 2016, preliminary revenue estimates suggest that at 18.8 percent of GDP, revenues underperformed by some 1.4 percentage budgeted revenues and were at their lowest level in a decade (Figure 15b). Thus far in FY 2016/17, the weak revenue performance appears to be continuing with monthly revenue collections averaging Ksh 94.8 billion against a target of Ksh 111billion. With respect to taxes, the shortfalls in revenue vis-à-vis targets have come from weaknesses in import related tax sources (duties and VAT), reflecting the drop in imports on account of lower oil as well as capital imports. Pay as You Earn (PAYE), the single largest revenue category, has also underperformed. As a share of GDP, Kenya's revenue performance compares favorably to most Sub-Saharan African countries, nonetheless it still remains below the optimal level and the previous collection high of 20.5 percent in FY2010. Among challenges impacting on the ability for the exchequer to receive/collect higher tax revenues include administrative challenges, tax leakages, challenges in income tax collection post devolution, and ongoing adaptation to the new VAT and excise tax laws. Besides the weakness in revenues from tax-related sources, there has been an even more significant underperformance of external grants with respect to targets. For the first three months of FY16/17, the deviation from target amounts is about 91 percent.

Figure 15a: Revenue Targets Vs Actual (% of GDP)



Source: The National Treasury

Figure 15b: Breakdown of Government Revenue (% of GDP)



Source: The National Treasury

1.4.6. **Some measures are being undertaken to address the weaknesses in revenue performance.** The government has taken steps to improve tax administration with the main aim of capturing a larger share of the tax base and decreasing tax fraud through: (i) the integration of KRA IT systems with IFMIS; (ii) the rolling out of new Customs Management System that will permit integration of the various tax departments to provide additional and more consistent information on importers; (iii) initiatives to strengthen revenue at the county level; (v) an improvement in valuation in benchmarking in order to address the undervaluation of importers.

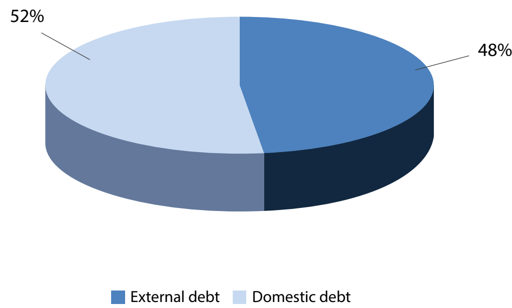
1.4.7. **There has been a shift towards external financing of deficits in recent years.** In FY14/15 domestic financing accounted for some 53.7 percent of total financing of the deficit. However, in the fiscal year ending 2016 and thus far in FY16/17, there has been a trend shift toward financing of a greater share of the deficit through external sources. In FY 15/16, external financing accounted for 54.7 percent of the deficit, while it is projected to account for 56.5 percent in FY16/17. Apart from the support to the exchange rate, the shift in foreign financing should help alleviate crowding out of the private sector in the domestic credit market. Nonetheless, the increased debt in foreign currency also carries with it potential risks, which in recent years has been heightened by the jitteriness of global financial markets. This calls for a continued sustenance of the stable macroeconomic environment and the need to increase policy buffers (both fiscal, monetary and reserves) to be able to have the policy space to adequately respond to external market events.

1.4.8. **While public debt is sustainable, the margin for further debt accumulation has narrowed.** Net public debt increased by 9.8 percentage points to 48.7 percent of GDP in FY15/16. The joint IMF/World Bank Debt Sustainability Analysis observes that debt in Kenya is still sustainable and is within the required margins. External financing as a share of total financing has increased over the years to stand at 48.0 percent in FY15/16 (Figure 16 and Figure 17), with commercial borrowing becoming increasingly important, leaving external debt repayment vulnerable to higher costs of borrowing and exchange rate risks. On the domestic front, commercial bank debt remains the most important source of lending to the government at 52.0 percent of total domestic lending. With changes to the regulatory environment inadvertently incentivizing banks to invest in government securities rather than intermediating productive ventures in the private sector, there is a risk that this could compromise future growth prospects.

1.4.9. **While there has been progress on county level fiscal governance, more remains to be done.** County governments have experienced remarkable progress after challenges faced in their first year of devolution. Budget execution has moved from 64.9 percent in FY13/14 to 90.2 percent in FY15/16. Nevertheless, four key challenges require urgent attention. These are: (i) the slow growth in Own Source of Revenue (OSR), (ii) low execution rate of development spending which still falls short of the requirement, (iii) accumulating pending bills; and, (iv) the rising wage bill which constitutes a significant share of county budgets (see Box B.2).

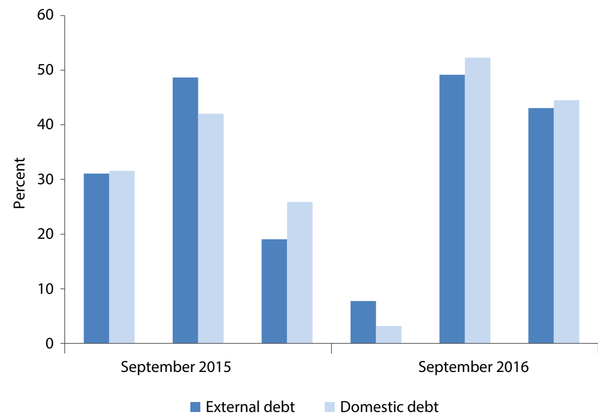
1.4.10. **The Government is seeking to raise funds to finance infrastructure spending through the launch of M-Akiba.** On 23rd March, 2017 the National Treasury launched a world first retail level mobile-phone based government bond auction platform – M-Akiba. The purpose of the M-Akiba bond is to mobilize domestic funds to support government infrastructure projects. Until M-Akiba, the minimum amount required to participate in the government bond market was Ksh 50,000, however, under M-Akiba the minimum investment required is Ksh 3000, thereby making it more affordable to a wider cross section of Kenyan society. The March launch is a pilot and seeks to raise Ksh. 150 million. The main launch is expected in June, with a target amount of Ksh 4.85 billion to be raised. Just six days after the launch of M-Akiba it is reported that at least 61,000 Kenyans had registered on the M-Akiba platform and some Ksh75.2 million (50.2 percent of the target amount) had been raised (see Box B.3).

Figure 16: External Debt Vs Domestic Debt (% of public debt as at Sept 16)



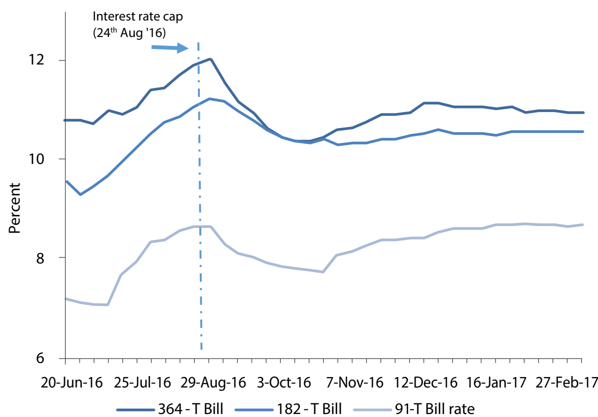
Source: The National Treasury

Figure 17: Composition of External and Domestic Debt



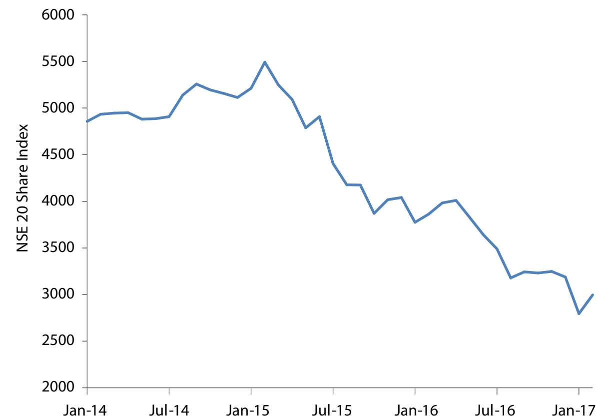
Source: The National Treasury

Figure 18: Government T-Bill rates



Source: Central Bank of Kenya

Figure 19: NSE 20 Share Index



Source: Financial Times

1.5 Financial Markets Faced a Tough Environment in 2016

1.5.1. The Banking sector remains fundamentally sound, despite recent headwinds. Kenyan banks remain well capitalized, with capital adequacy ratios above the statutory requirements. As of September 2016, industry-wide regulatory capital to risk-weighted assets was 19 percent, return on equity was 27 percent and liquid assets to short-term liabilities was 42.9 percent. Further, the banking industry remains the single largest industry contributor to corporate income taxes. Nonetheless, the banking sector was rocked by a number of developments in 2016. First, following the wave of receiverships in 2015, another lower tiered bank was placed under receivership in April 2016, which resulted in flight to safety sentiments among depositors as well as episodic tightening of liquidity in the interbank market with the lower tiered banks facing greater challenges. However, the liquidity facility promptly put in place by the Central Bank of Kenya is helping to mitigate the situation. Secondly, stricter guidelines on the provisioning of bad debts led to a spike in recorded non-performing loans by banks. Thirdly, the coming into effect of the Banking Amendment Act has reduced the Net Interest Margins (NIM) of the sector.

1.5.2. Banks are adjusting to the new regulatory environment. The effects of changes to the rules of the game on the banking industry are still evolving. However, there are some early preliminary patterns emerging. The legislation on interest rates cap introduced in August 2016, which pegs the private sector lending rate to the CBR, inadvertently made yields on government securities relatively attractive, hence banks have increased their holdings of government T-Bills and bonds (Figure 18). This has contributed to the decline in yields of government securities since August 2016, as banks showed their preference for government paper which is perceived to be "risk free" compared to lending to the private sector. Further, though it is still early days, there is evidence of credit rationing as some banks have announced plans to curtail new unsecured consumer

loans and loans for motor vehicle purchases. Last but not least, banks have indicated that they plan to contain costs by laying-off workers (so far estimates are over 1000 workers) and adopting technological innovations to reduce costs. While all banks are affected by the regime change the lower tiered banks are likely to be the hardest hit since they had lowest margins (due to higher funding costs) prior to the introduction of the caps in the interest rate.

1.5.3. The stock market continued its bear run in 2016. The stock exchange index declined by 21.1 percent year on year in December 2016. Among other factors, uncertainty due to Brexit, the introduction of the interest rates cap in August 2016, which saw listed commercial bank share values decline, contributed to the continued bearish run in the second half of the year. On the contrary, on a year-to-date basis through the first two months of 2017 there was an increase of 7.2 percent of the index (Figure 19 above).

2. The Changing Economic Landscape and Kenya's Growth Prospects

2.1 Emerging Head and Tail Winds Influencing the Economic Landscape

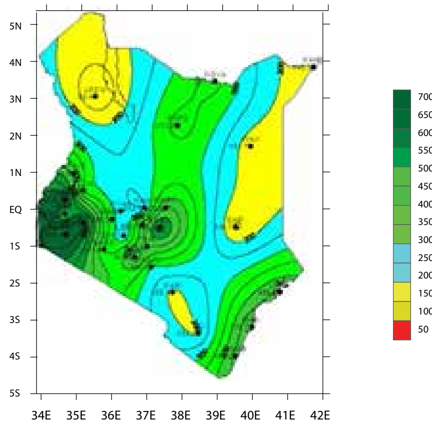
2.1.1. Kenya's economic prospects will be affected by the emerging economic winds of change. We identify four main headwinds and two tailwinds, which are factored in the growth outlook as part of the baseline scenario. While a number of them might have already commenced in earlier years, we see the full force of these economic winds of change becoming more prominent than earlier over the forecast horizon. Consequently, they are likely have a stronger influence on near and medium term economic prospects in Kenya.

2.1.2. The ongoing drought is set to dampen economic activity. Due to the prevailing La Nina conditions in the Indian Ocean, Kenya is currently facing a severe drought. The Meteorological Department of Kenya reports that the rainfall during the October-December 2016 short rainy season was generally depressed throughout the country. The seasonal rainfall onset was late, and the distribution, both in time and space, was also poor throughout the country. Further, most areas in the country received less than 75 percent of their historical rainfall averages. The weather outlook for March-May 2017 (long-rains) continues to look dire over Eastern part of Kenya, however, few parts of Western Kenya are likely to receive near-normal rainfall (Figure 20 and Figure 21). With most of Kenya's agriculture being rain-fed, the contribution of the agriculture is expected to be significantly lower. There have already been several reports on failed crops, dying herds, and increased food insecurity in the hardest hit places (Northeastern and Northwestern). This is not limited to only the arid regions. FEWSNET reports that there is likely to be a total maize crop failure in the southeastern and coastal marginal agricultural areas. Further the leguminous crop harvest is likely to be some 60-80 percent below average in the main agricultural zones.

2.1.3. The drought will have spillovers to the rest of the economy. Beyond the agriculture sector, the drought will have knock-on effects on the rest of the economy through higher electricity prices, as the shortfall in hydro-power will be made-up with more expensive diesel powered plants. This is because hydroelectric power contributes over 40.0 percent of Kenya's power mix and is also the cheapest energy source, this is therefore likely to also lead to a rise in energy inflation, which until recently has been decelerating. Given both of these effects, it is not surprising that drought years in Kenya are generally associated with a deceleration in GDP growth by about 0.6 percentage points. Our estimates suggest that for every 100mm shortfall in rain, GDP declines by some 0.3 - 0.5 percentage points. Further, the drought has fiscal and external balance implications given the need to import food staples.

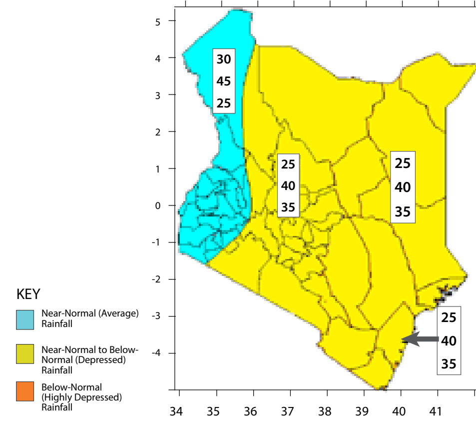
2.1.4. The weakness in credit growth to the private sector will dampen economic activity. As noted earlier, credit growth is hovering at a 13-year low of 4.3 percent, compared to the 10-year average of about 19 percent. Given that the underlying supply-side factors that are weighing on bank lending to the private sector are likely to prevail, we don't expect credit growth to reach its long-term average in the near term. As a consequence, we expect economic activity in those sectors that have traditionally been intensive in the use of bank loans to be hit the hardest. This will impact on durable household purchases (e.g. cars, houses) and firms in manufacturing, construction and real estate industries, all of which will subdue domestic demand and Kenya's growth prospects.

Figure 20: Historical rainfall pattern over long rain (March-May)



Source: Kenya Meteorological department

Figure 21: Projected rainfall pattern for the upcoming long rains (March-May 2017)



Source: Kenya Meteorological department

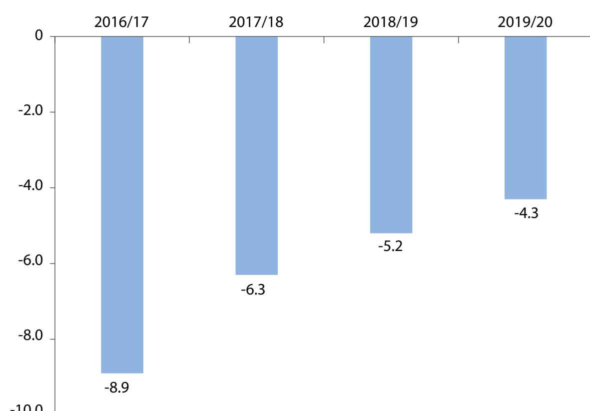
2.1.5. Fiscal consolidation will be a headwind in the medium term. While the effect of the drought and the slowdown in credit growth are likely to be the two dominant headwinds, economic activity will be impacted by the post medium term fiscal consolidation plans. We expect the impact from fiscal consolidation to be modest as the projected path to a lower deficit is gradual (Figure 22). Based on the projected government expenditure plans (both consumption and development spending) will still expand in real terms in FY16/17. Further, the pathway to fiscal consolidation is also reliant on improvements in domestic revenue mobilization (revenue to GDP ratio expected to increase from 18.8 percent in FY15/16 to 21.5 percent in FY19/20) rather than full adjustment on the expenditure front. For FY17/18 we expect the fiscal consolidation to be lower than projected as historically, election years are often characterized by increased recurrent spending. Indeed, the recent escalation in various public service worker strike actions, and the rising interest rate obligations will make it difficult for the government to place a tight cap on its recurrent spending in the near term. Fiscal consolidation will be supported by measures to boost domestic revenue mobilization (revenue administration, new tax measures, re-introduction of withholding VAT and rationalization of tax expenditures). On the expenditure front, the completion of the first phase of the Standard Gauge Railway—the single most important driver of public investment spending—in recent years should be supportive of fiscal consolidation.[1] Secondly, one-off election related expenses will no longer be repeated post-August 2017. Hence, we expect fiscal consolidation to pick-up pace in more earnest post-elections in FY18/19 and beyond. We expect the government's fiscal consolidation plans to help anchor macroeconomic stability.

2.1.6. The terms of trade gains from declining oil prices are set to wane. With global oil prices set to rise on recent agreements between major oil exporters, the positive terms of trade effect that Kenya and several other oil importers have enjoyed will be curtailed. The World Bank projects prices to reach $60/barrel by 2019. This represents a steady increase in prices so should be able to be absorbed by the Kenyan economy as opposed to the destabilizing sharp hike in oil prices that occurred in 2011/2012. The rise in oil prices is thereby expected to contribute to a pick-up in the import bill with the deficit in current account expected to be higher in 2017 than in 2016, though still below peak levels since the oil price increase is expected to be marginal. Further, we estimate that on an accumulated basis, an increase in oil prices dampens GDP growth by some 0.35 percentage points and increases inflation by 2.5 percent over ten quarter period (Figure 23 and Figure 24).

2.1.7. As the US Fed embarks on interest rate hikes, credit conditions to emerging and frontier markets, including Kenya, could become tighter. On the external front, with the US Federal reserve set to carry out further hikes in interest rates, the US dollar is set to further strengthen. The slide in emerging market currencies that occurred following the rate hike in November 2016 could re-occur, including that of the shilling. Further, the cost of accessing funds from international capital markets (syndicated lending, Eurobonds, etc.) is also likely to increase with higher US interest rates. On the other hand, these effects could be moderated by increased remittances given a global economy that is forecast to strengthen in 2017 (Box B.4). Hence, tapping into the savings of the diaspora could also help alleviate the anticipated tighter conditions.

[1] The second phase is projected to be less expensive than the first phase since most of the locomotives that will use the SGR were purchased during the first phase.

Figure 22: Fiscal Deficit (% of GDP)



Source: The National Treasury

2.1.8. On the upside, economic activity in Kenya will be lifted by the tailwinds of a strengthening global economy and the soon-to-be-operational Mombasa-Nairobi Standard Gauge Railway. The strengthening global economy and the completion of major infrastructural projects should provide impetus/tail winds to economic activity. Tourism is already rebounding. With the expected strengthening of the global economy, this should further strengthen the recovery in that sector. Both remittances (about 2.3 percent of GDP in 2016) and merchandise exports are also expected to benefit from an expanding global economy. Further the first phase of the SGR project is due to be completed with operations starting in 2017. This should provide further impetus to the economy via the creation of new businesses along the path of the railway and significantly contribute to the competitiveness of the economy as imported inputs for firms and exports are received faster at a lower transportation costs. Further, the SGR should help relieve some congestion at the port as well as along the Nairobi-Mombasa corridor. In addition to the SGR, other infrastructure projects such as the Mombasa Port Development Project, LAPSSET and ongoing investments in renewable energy (Geothermal Development) projects should improve the investment climate and help relieve some of the binding supply side constraints to growth.

2.2 How Will These Emerging Head and Tail Winds Impact on Growth Prospects?

2.2.1. Near term growth is expected to dip on account of headwinds. However, over the medium term growth should pick-up. Given the headwinds of the ongoing drought, weak credit growth, fiscal consolidation and the rise in oil prices adversely impacting on economic activity in 2017, we project GDP growth to decelerate to 5.5 percent in 2017, a 0.5 percentage point mark down from earlier forecasts. However, over the medium term, we expect these headwinds to ease and together with the projected steady strengthening of the global economy and the benefits of completed major infrastructure projects, GDP growth is expected to accelerate to 5.8 percent and 6.1 percent in 2018 and 2019 respectively, consistent with the underlying growth potential of the Kenyan economy (Table 1.1 and Figure 25). Although the medium term prospects for Kenya's economy remains robust, the distribution of the benefits of this growth are not likely to be broadly shared unless policies are implemented to bridge high levels of inequality of opportunities.

2.2.2. Consumption will remain the main driver of growth on the demand side in 2017, albeit at a slower pace. The changing economic winds are set to impact household consumption, the most important demand driver (about 70 - 80 percent of GDP). The drought is expected to reduce farmer incomes and increase the number of food insecure people there by weighing down on consumption, notwithstanding fiscal injections by the government (both national and counties) to ameliorate/mitigate the worst effects of it. The purchasing power of urban dwellers is likely to be curtailed as both food and energy price inflation rise. In recent years, consumers have benefitted from successive years of oil price declines, however, given that oil prices are expected to rise (even if moderate) the earlier stimulus provided by the lower prices will not be there in the near term. Consumption spending by the rising middle-income class is also likely to be dampened by the tightening of credit conditions as evidenced in the deceleration of credit growth. As a result, we expect the growth in demand for consumer durables such as cars and houses to be weaker since they are more dependent on bank loans and also tend to be income elastic (unlike food staples). The extent of the slowdown in consumption growth will, however, be partially mitigated by recent announced widening of income tax brackets and tax relief by 10 percent starting January 2017, since this effectively increases disposable income. Another mitigating factor will be the expected rise in remittances, given the strengthening of the global economy.

2.2.3. Investment growth will slow down in 2017, but pick-up thereafter. An expansionary fiscal stance, in particular public spending on infrastructure to relieve supply side constraints, has been an important driver of economic growth in recent years. Under the proposed

Figure 23: Accumulated response of GDP to real oil price increase

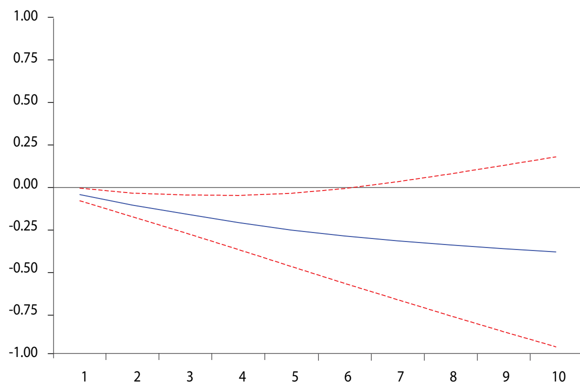
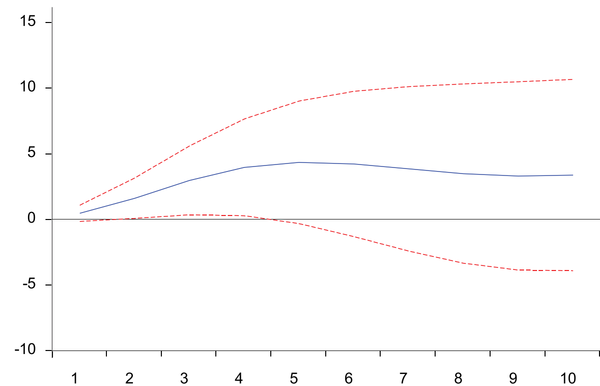


Figure 24: Accumulated response of inflation to real oil price increase



Note: Quarterly accumulated impulse responses functions to a Cholesky one standard deviation innovation in oil prices by a VAR model including real oil prices, real effective exchange rate, GDP, inflation and yields on 91-day TBills yields. All data are quarterly, from 2005Q4 to 2016Q2

fiscal consolidation plans, the government envisions a decline in development spending by some 2.6 percentage points of GDP in FY17/18. The removal of this stimulus to the economy is likely to dampen the contribution of public investments to GDP growth in the short-run. However, in the long run, this should help anchor macroeconomic stability, with fiscal deficits and debt levels trending lower. Private business investment is also expected to be weaker on account of the tighter lending conditions, as evidences in the deceleration of credit growth (private sector credit growth has steadily declined from 20.9 percent in July 2015 to its current levels of below. On the external front, we expect foreign direct investment (FDI) and portfolio flows into the country to be weakened as investors typically adopt a wait-and-see attitude during the run-up to elections. Given Kenya's relative attractiveness in the sub-region, we expect investment flows to pick-up after the elections. However, the banking sector which has attracted significant investment flows in the past is likely to be less attractive unless the provisions within the Banking Amendment Act are revisited.

2.2.4. The contribution of net exports to GDP is likely to weaken on account of the expected pick-up in oil prices. Like many oil importers, Kenya has benefitted from a significant terms of trade gain as a result of low oil prices. In 2016 the share of fuel and lubricants as a share of GDP was 14.4 percent compared to an average of 21.6 percent in 2014. Hence the rise in oil prices is expected to put upward pressure on the current account deficit over the forecast horizon. Reflecting the commencement of this trend the share of oil imports for the second half of 2016 (when oil prices were higher) increased by 2.0 percentage points of GDP to 15.4 percent compared to the first half of the year. However, the effects from the rise in oil is expected to be partially counteracted by lower machinery imports as a result of the coming to an end of some major public infrastructure investments. Further, import growth will also be dampened by the ongoing slowdown in credit growth. In addition, remittances, merchandise exports and tourism receipts are expected to rise on account of a stronger global economy. Overall, unlike the marginal positive contribution of net exports to GDP observed in 2016, we expect the net exports contribution to turn negative, consistent with its historical performance.

2.2.5. Although the medium term prospects for Kenya's economy remains robust, the distribution of the benefits of this growth are not likely to be broadly shared unless there is more emphasis in policies aimed at lowering inequality. Between 2006 and 2016, poverty incidence (under the official national poverty line) dropped from 46 percent to 36 percent.[2] The 10 percentage point decline reflects a consistent economic growth across most sectors of the economy as well as an expansion of the social safety nets targeting the poor. Nonetheless, the progress against poverty was slowed by uneven consumption growth across socio-economic groups and spatial dimensions; with the vast, low-density North and North-eastern Counties lagging behind, a situation partly explained by high levels of vulnerability to adverse climate shocks in these areas.

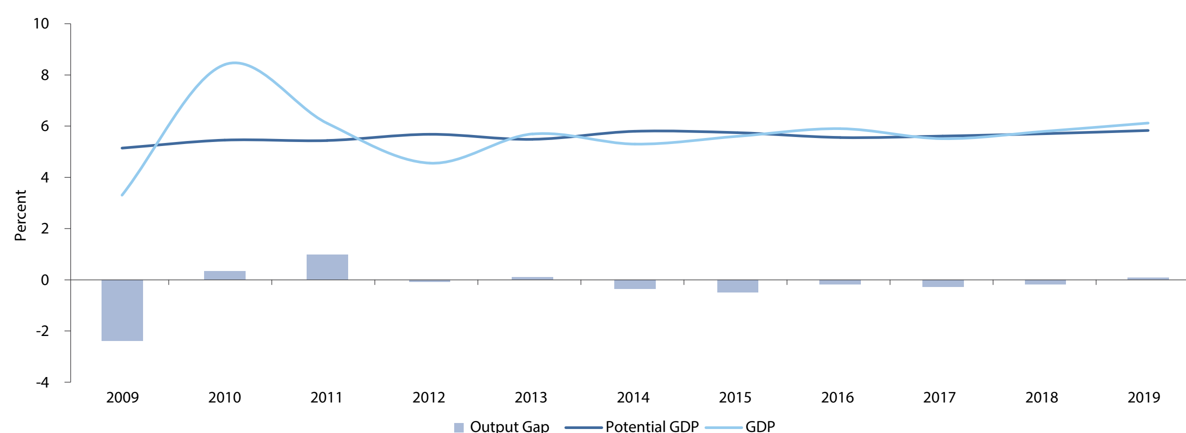
[2] *New poverty figures for Kenya will be updated by April 2017.*

Table 1.1: Medium term growth outlook (percent, unless stated)

	2014	2015	2016 e	2017 f	2018 f	2019 f
Real GDP Growth	5.4	5.7	5.8	5.5	5.8	6.1
Private Consumption	4.6	5.3	5.9	5.7	5.8	5.9
Government Consumption	6.0	15.4	4.5	1.5	1.1	0.8
Gross Fixed Capital Investment	14.6	4.9	2.0	7.8	9.4	10.8
Exports, Goods and Services	5.3	-0.9	4.0	4.0	4.3	4.8
Imports, Goods and Services	10.6	-1.2	5.0	4.5	5.1	5.7
Agriculture	3.5	5.6	5.6	5.4	5.4	5.4
Industry	6.5	6.9	5.7	5.7	5.6	5.6
Services	5.7	5.4	5.3	5.5	6.0	6.6
Inflation (Consumer Price Index)	6.9	6.6	6.5	8.0	6.8	6.5
Current Account Balance (% of GDP)	-10.3	-6.8	-6.0	-6.4	-7.2	-8.0
Fiscal Balance (% of GDP)	-7.2	-8.4	-8.9	-6.3	-5.2	-4.3

Source: World Bank and the National Treasury; Fiscal Balance is sourced from National Treasury and presented as Fiscal Years

Figure 25: GDP growth and Output gap



Source: World Bank

3. Downside Risks to the 2017 Growth Outlook

3.1 Domestic Risks

3.1.1. **Downside risks to Kenya's outlook remain broadly unchanged.** The downsides risks identified in the previous edition of the Kenya Economic Update continue to remain valid. Those identified risks included external risks, such as a slowdown in the global economy and uncertainties related to US interest rate hikes, and domestic risks such as a potential for fiscal slippages, poor rains, upcoming elections and security concerns. The downside risks considered here differ from the headwinds earlier noted in that the specific scenarios considered are not part of the baseline assumptions.

3.1.2. **However, drought conditions could turn out to be worse than expected.** While poor rains were considered a risk in the previous KEU, it is a current reality. Hence the baseline forecasts already takes this into account. Nonetheless, given that our baseline forecasts assumes the effect from an average drought year, if outturns for the long rainy season (March April May) tend to be worse than anticipated then this would represent a significant downside risks to the current outlook. We also assume that in 2018 and beyond the rainfall situation will return to normalcy. If that does not materialize, GDP growth will likely be lower than the anticipated pick-up in growth that currently projected.

3.1.3. Fiscal pressures could lead to a slippage from medium term pathway of fiscal consolidation. As noted earlier, the process of fiscal consolidation has commenced. Given current fiscal deficit levels, this is a necessary step, even if difficult. The National Treasury projects the deficit to decline from 7.5 percent in FY15/16 to 4.3 percent in FY19/20. While commendable there remain risks and challenges to the achievement of this medium term fiscal consolidation pathway. Not the least among these are the building pressures on recurrent spending (both wage agitations as well as interest payments), demands from county governments and the resolve to deliver on an ambitious (though necessary) infrastructure agenda in an environment. This is made all the more challenging in an environment where domestic revenue mobilization has been underperforming. The outlined fiscal consolidation remains achievable, but will require disciplined fiscal management.

3.1.4. Other domestic developments represent tail risks. Based on the current strong institutional frameworks, our baseline scenario is that the elections will occur without any significant disruption to economic activity. Further, given increased investment in the security apparatus, our baseline assumes that the improved security situation currently prevailing will persist over the forecast horizon. However, in the unlikely event that future developments differed, this will adversely impact investor confidence, dent the ongoing rebound in the tourism sector, and thereby reduce economic activity from projected levels.

3.2 External Risks

3.2.1. On the external side, a slowdown in the global economy and market jitteriness related to the lift-off of US interest rates could dent Kenya's growth prospects. After several years of weak growth, the global economy is projected to strengthen in 2017 and beyond. This strengthening of the global economy underpins the anticipated pick-up in Kenya's exports (in particular, horticulture products), remittance flows and tourist arrivals. However, this is not guaranteed, as has been observed recent years with the continuous downgrade in global economic growth. The global economy continues to reel under the burden of the legacy issues related to the global financial crisis that has bedeviled high-income countries, challenges in rebalancing of China's economy, and the adverse effects of the commodity price slump that has weakened several commodity exporting low and middle income economies.

3.2.2. Risks from global financial markets. Further, uncertainties related to future U.S interest rate hikes could lead to volatilities in global financial markets and destabilizing short-term capital outflows in emerging and frontier markets. With Kenya's increased integration with global capital markets, and dependence on a strong global economy for its exports, tourism industry and remittance inflows a weaker than expected development in the global economy could be detrimental to Kenya's future growth prospects. To the extent that this leads to "flight to safety sentiments" and a strengthening dollar (and other safe haven currencies) this could weaken the shilling with implications for Kenya's debt levels given the increasing share of foreign currency denominated debts.

4. Policies

4.1 Kenya Needs to Safeguard its Robust Performance and Accelerate Growth Potential

Despite, the ongoing economic weakness observed in several Sub-Saharan African economies and elsewhere among other frontier and emerging markets, Kenya's growth performance has been remarkably robust in recent years and medium term prospects remain bright, notwithstanding the projected near term dip in performance. Yet for Kenya to achieve the Vision 2030 goal of becoming a high middle-income country, it will need to pursue policies that will enable it safeguard the achievements of recent years as well as accelerate the pace of economic activity to be commensurate with other high performing sister East African economies such as Ethiopia and Tanzania. Higher growth rates, particularly, growth that benefits households in lower income brackets will be important to reduce relatively high levels of poverty (notwithstanding progress made in recent years) and inequality.

4.2 Prudent Fiscal and Monetary Policies will be Critical to Safeguard Macro Stability

Fiscal and monetary policies have played an important role in sustaining the macroeconomic stability that the Kenyan economy has generally experienced in recent years. This calls for the continued implementation of prudent fiscal and monetary policies going forward. On the fiscal front, given the elevated levels of the deficit as well as the lowering of margins for maneuver due to the rise in debt stocks, the implementation of the medium term fiscal framework which seeks to bring the deficit down to 4.3 percent by FY19/20 is a step in the right direction. To safeguard the long-term growth potential of the economy, fiscal consolidation needs to be implemented in such a way as not to compromise public investments in critical infrastructure that unlocks the productive capacity of the Kenyan economy. Secondly, given the effect the Banking Amendment Act is having on the muddling of monetary policy and the historically low private sector credit growth levels, it is important that the Act is reviewed with a view to eliminating it or making it significantly less restrictive. While this will not resolve all the issues related to credit access and costs, it will be an important step given recent economic developments.

4.3 Structural Reforms will be Required to Unleash Further Productivity Gains

4.3.1. Productivity levels in Kenya remain relatively low compared to its peers. However, research shows that over the long run the differences in the standard of living between inhabitants of a country is largely due to their productivity differentials. Policies play an important role in explaining productivity differentials. Policies can influence the allocation of resources in an optimal (e.g. towards the most productive use) or a sub-optimal way (when resources are misallocated to lower productive activities). There are several policies that can influence a country's productivity. We highlight 3 that are relevant for Kenya given recent economic developments.

4.3.2. Further, reducing the transactions cost environment in the delivery of credit could enhance further access to credit. First, access to credit could be improved by strengthening credit reporting to the Credit Reference Bureaus by including SACCOs, utilities and other issuers of credit facilities. This will allow lenders to use positive credit information to offer lower rates to a wider set of customers. Secondly, creating a central electronic collateral registry (for both moveable and immovable property) will reduce the cost of perfecting a security interest by banks. Thirdly, developing a framework to promote property (both moveable and immovable) as collateral. For instance, the computerization of land registries will enable the capture, management and analysis of geographically referenced land related data. Finally, the implementation of the National Payments System Act and regulations will operationalize infrastructure sharing by banks in order to reduce operational costs as well as encourage banking innovations such as agency banking, currency centers and mobile banking.

4.3.3. Improve agricultural sector productivity. Kenya's agriculture sector accounts for some 25 percent of GDP and employs the bulk of the work force, hence developments in that sector play (e.g. recent drought) are critical for Kenya's growth performance and progress in poverty reduction. Yet productivity in that sector remains low. Measures to improve the sector's productivity could look at efforts to influence the competiveness of both agricultural input and output markets. First, this could include efforts to approve and implement the seeds regulations and national performance trials so as to promote private investment in the seed sector and increase the availability of higher productivity seed varieties to farmers. Secondly, policies that crowd in the private sector in the sourcing and delivery of the subsidized and unsubsidized fertilizers to farmers can improve upon the availability of this critical input to farmers at the time they most need it. Thirdly, developing and implementing the leasing legal framework to promote agricultural mechanization (including value addition/agro-processing) could help improve agricultural productivity. Fourthly, approving the warehouse receipts bill can help improve competitiveness in the grains sector. Last but not least, reducing the various tariffs and non-tariff import barriers on food grains could reduce artificially inflated food grain prices on the local market.

4.3.4. At the regional level, market access could be enhanced by eliminating the myriad non-trade barriers trade costs that impede on intra-regional trade. Kenya's exports to the EAC has been weak in recent years (see Box B.1). Non-tariff barriers affecting intra-EAC trade include non-harmonized technical regulations, sanitary and phytosanitary requirements, customs procedures and documentation, rules of origin, police roadblocks and high costs of cross-border communications and digital transactions for the poorest citizens. A reduction in trade costs is expected to benefit all East African economies. In Kenya, it will favor its capital-intensive sector.

4.3.5. Consider new engines of economic growth, such as unlocking the potential of housing delivery for middle to lower income households. Kenya is missing a major opportunity for job creation, economic growth and addressing inequality by existence of a housing industry that falls short of addressing the needs of low income households. In Kenya, there's an estimated accumulated housing deficit of over 2 million units, and nearly 61 percent of households live in slums. Addressing this housing deficit will be good for economic growth, creating jobs, and deepening the financial sector. Unlocking the residential housing market through the development of the housing finance market can provide a wide range of income opportunities through the construction sector and related industries as evidenced in Columbia, India, and South Africa. In Colombia it is estimated that 5 additional jobs are added for every US$10,000 spent on housing construction. In India, each housing unit creates 1.5 direct and 8 indirect jobs; in South Africa, each housing unit creates 5.62 jobs for every housing unit. The next section focuses on affordable housing in Kenya and the policies that can be put in place to make housing more affordable to more Kenyans.

BOXES

Box B.1: Is Kenya loosing competitiveness in the East African market?

1. **Kenya's merchandise trade performance has been dismal in recent years, in particular its exports to the East African Community.** Kenya's merchandise exports contracted by an estimated 23.3 percent in 2016. In part, this reflects weakness in global trade. In the aftermath of the global financial crisis, global trade has been subdued on account of weak demand and structural factors (Matoo *et al*, 2015). Nonetheless, the contraction in Kenya's exports is not only due to weakness among its high-income trading partners. Worryingly, Kenya's exports to the EAC saw a significant decline in 2016, a region where growth has remained relatively resilient. Of further concern is that longer term trends show that Kenya's exports to the EAC have been on a decline for the past several years: export growth in value terms was some 29.5 percent in 2007 but has since contracted to a low of -8.9 percent in 2013. The decline in Kenya's exports to the region in recent years has occurred despite overall growth in EAC intraregional trade, reflecting the stronger growth performance of its regional trading partners. This begs the question whether Kenya is becoming increasingly less competitive in the EAC region?

2. **Decomposition of Kenya's export performance show that both agricultural and manufactured products contributed to the decline.** The loss in Kenya's exports to the region is particularly reflected in its trade with the region's two other large economies. While Ugandan and Tanzanian imports grew at 12.4 and 16.0 percent respectively over the 2000-2015 period, their imports from Kenya only increased by 4.3 percent and 6.3 percent. Agricultural products whose exports to the EAC has weakened the most over the past 10 years include: cereals (HS10), Products of milling industry; malt and starches (HS11), lac; gums, resins & other vegetable (HS13), animal or vegetable oils (HS15), sugar and sugar confectionery (HS17). For instance, in Uganda, Kenya's largest EAC market, the growth rate of (HS11) and (HS13) imports from Kenya declined by 25.3 percent and 11.6 percent respectively over the (2000 to 2015). Similarly, manufactured goods whose exports to the EAC has weakened the most over the past 15 years include: Chemical products (HS38), Plastics (HS39), Photographic or cinematographic (HS37), Raw hides and skins (HS41), Paper and paper boards (HS48), Glass and glassware (HS70) Iron & steel products (HS72) Electrical machinery & equipment (HS85), Motor vehicles (HS87) and Musical instruments; parts and ace (HS92). Further, in Tanzania, Kenya's second largest EAC market, the manufacturing imports growth from Kenya has declined by 6.2 percent over the compounded annual growth of fifteen years compared to 16.8 percent of its manufacturing imports to the World over the same period. The products that contributed to this growth include: (HS 37), (HS41) and (HS92). However, it needs to be mentioned that Kenya has also gained market share in a few select dynamic export markets including European Union, Asia and America. Nonetheless, the losses far outweigh these gains, thus leading to the overall declining trend. Given the importance of manufactured exports in supporting the diversification of Kenya's economy, the loss of market share in these products has implications for diversification of the Kenyan economy.

3. **How does Kenya regain its competitiveness in its backyard?** Kenya has become less competitive in the EAC due mostly to cheaper products to EAC markets from elsewhere, in particular East Asia (including China). For instance, in both Tanzania and Uganda, the share of East Asia (including China) exports has increased from some 45 percent to 60 percent over the past decade. This has not only driven down market shares of Kenya's exports but also that of other countries. However, for Kenya, the EAC market remains an important market, and provides a good platform to be able to compete globally. Reversing the decline in Kenya's competitiveness is of paramount importance and will require both domestic policy actions to improve the competitiveness of Kenyan firms as well as efforts on a regional level to improve market access for Kenyan products and a much freer flow of goods within the EAC.

4. **At the domestic level, this will require policy actions to address the very low levels of labor productivity in Kenya (even compared to the Sub-Saharan African average).** Labor costs in Kenya remain high relative to output and regional peers. While Kenya has invested in broadening access to education, the pay-off to educational investment has been low. Many educational assets sit idle because of mismatches, reinforcing the impression that Kenya is not making productive use of its available labor force. Several measures are needed to promote productivity. These include: (i) helping firm access skills, technology and information through, for example, technology extension or technology transfer programs; (ii) ensuring level playing field between informal and formal sector, by streamlining and reducing regulation and ensuring fair enforcement; (iii) decreasing the cost of doing business by addressing critical infrastructure gaps, especially in electricity, developing key financial infrastructure and special

programs to help enterprises access financing, and accelerate and facilitate international trade; (iv) supporting firm entry and exit, which is low in Kenya, by facilitating the starting up of a business, and simplifying the insolvency framework; (v) and, streamlining revenue raising schemes that are increasing the cost of doing business unduly in Kenya.

5. **At the regional level, market access could be enhanced by eliminating the myriad non-trade barriers trade costs that impede on intra-regional trade.** NTBs affecting intra-EAC trade include non-harmonized technical regulations, sanitary and phytosanitary requirements, customs procedures and documentation, rules of origin, police roadblocks and high costs of cross-border communications and digital transactions for the poorest citizens. A reduction in trade costs is expected to benefit all East African economies. In Kenya, it will favor its capital-intensive sector. Further, a reduction in non-tariff barriers is estimated to increase consumption of 0.16 percent in Kenya and 0.22percent in Tanzania. Without such action, Kenya will continue to lose out on market share in EAC, and this will be particularly important for not just its exports but the diversification of its economy since, compared to its exports to advanced economies, Kenya's exports are more diversified and include several non-agricultural or have more manufactured goods.

Box B.2: Trends in county level fiscal management

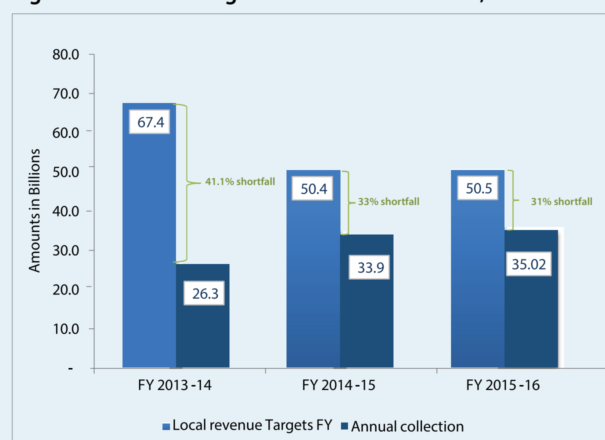
County governments have experienced remarkable progress after challenges faced in their first year of devolution, notably, budget execution has moved from 64.9 percent in 2013/14 to 90.2 percent in 2015/16. Nevertheless, four key challenges require urgent attention: (i) the slow growth in Own source of revenue (OSR); (ii) low execution rate of development spending which still falls short of the requirement; (iii) accumulating pending bills; (iv) and, the rising wage bill which constitutes a significant share of county budgets.

1. **County Governments' budget allocations grew by 12 percent in FY 2015/16.** The total budget amounted to Ksh. 367.4 billion in FY 2015/16 and Ksh. 326.4 and Ksh.228.6 in FY 2014/15 and FY 2013/14 respectively. The overall actual expenditure amounted to Ksh. 295.3 billion and Ksh.258.2 billion representing an 80 percent absorption rate of the budget. Development spending also witnessed a 14.5 percent improvement in absorption between FY2014/15 and FY 2015/16.

2. **County governments complied with the Public Finance Management Act, 2012, requirement that recurrent expenditure should not exceed total revenue.** The share of the Counties' aggregate recurrent expenditure for personnel and operations and maintenance (O&M) to total revenue (transfers from the National Government and own-source revenue) for FY 2015/16 was 56 percent 55 and 58 percent for FY 2014/15 and 2013/14 respectively.

3. **However, counties recorded a significantly slow growth in Own-Source Revenue (OSR).** Own Source Revenue grew by 28.9 percent from Ksh 26.3 billion in the FY 2013/14 to Ksh 33.9 billion in the FY 2014/15. However, the growth was significantly slower between FY 2014/15 and FY 2015/16 at 3.3 percent. The slow growth suggests that there is need for counties to apply fiscal effort and improve efficiency in own revenue collection.

Figure B.2: Annual Targets Vs. Actual Collections, Kshs.



Source: Controller of Budget

4. **County revenue forecasts seem more credible but there is still a significant shortfall between targets and actual collections.** Even after revising down the FY 2014/15 targets due to poor performance, the collections in FY 2015/16 remained below it. The report on county Own Source Revenue by National Treasury for eight County Governments highlights lack of credible forecasting methodology, lack of in-year monitoring and ambiguity of roles within County Governments in the revenue forecasting process as the main challenges facing the county governments. Recent audits also suggest there are gaps in tax administration leading to leakages.

5. **Forty-five (45) counties complied with the requirement in the PFM Act, 2012, that at least 30 percent of their budgets are allocated to development expenditure in FY 2015/16.** However, only 33 counties managed to achieve the 30 percent in actual development spending in FY 2015/16. This is a marginal improvement from FY 2014/15 where 31 counties met the required threshold in actual spending. With a few exceptions, counties that didn't meet this requirement are predominantly urban. Nairobi, Nakuru, Embu, Nyeri and Kiambu counties were below the 30 percent actual development spending marginally.

Policies to improve fiscal management at the County level

6. **There is need to enhance county own sources of revenue and ensuring their predictability.** Own source of revenue (OSR) forecasting has improved but growth has slowed down. To address this challenge, the government should ensure that loopholes and leakages in counties' revenue collection are sealed and also develop a policy through which local revenue raising activities will be better supported and coordinated.

7. **Budget execution can be improved. Counties have shown a positive trend in compliance with fiscal responsibility principles in recurrent and development budget allocations.** However, Cash shortages and slow procurement procedures have led to low development budget execution and an accumulation of pending bills. Counties have been constrained in their service delivery by an increasing wage bill and the need to meet various operational and maintenance expenditures. Consequently, there is therefore an urgent need for counties to contain their wage bill and align their procurement plans to cash flow plans.

Streamline the re-allocation of funds. Section 154(2) of the PFM Act 2012 provides limited power to accounting officer to reallocate approved fund. However, the county sector expenditure data shows a huge discrepancy between the final approved budget figures and the actual spending per sector. Therefore, there is a need to ensure that these shifts in sector priorities leading to reallocation of funds are regularized through a Supplementary Budget.

Box B.3: M-Akiba: Another First For Kenya

What is M-Akiba? On 23rd March, 2017 the National Treasury launched a world first retail level mobile-phone based government bond auction platform – M-Akiba ("Akiba" is the Swahili word for savings). The purpose of the M-Akiba bond is to mobilize domestic funds to support government infrastructure projects. Until M-Akiba, the minimum amount required to participate in the government bond market was Ksh 50,000, however, under M-Akiba the minimum investment required is Ksh 3000, thereby making it more affordable to a wider cross section of Kenyan society. The coupon rate for the three-year M-Akiba bond is fixed at a tax free rate of 10 percent per annum. Interest payments will be made every six months. The bond will be listed on the Nairobi Securities Exchange and tradeable by mobile phone. The M-Akiba bond market is expected to be liquid as there is expected to be a guaranteed buyer. Safaricom and Airtel are the participating Mobile Network Operators (MNOs). The March launch is a pilot and seeks to raise Ksh. 150 million. This pilot launch should help test the platform and address any implementation challenges before the main launch, which is expected in June, with a target amount of Ksh 4.85 billion to be raised.

What has been the result so far? M-Akiba bond builds on Kenya's success story of integrating technology and financial services in order to increase financial inclusion for Kenyans, and develop a savings and investment culture among ordinary Kenyans. Just six days after the launch of the M-Akiba it is reported that at least 61,000 Kenyans had registered on the M-Akiba platform and some Ksh75.2 million (50.2 percent of the target amount) had been raised. With 31 million Kenyans (64.4 percent of the population) having mobile money subscriptions, and with deposit rates at banks lower than the M-Akiba coupon rate there exist further potential for the government to raise funds, while supporting a savings culture. Notwithstanding the expected success of M-Akiba, participation in the government bond market will continue to be dominated by larger investors, pension fund managers, high net wealth individuals, and banks, as transactions through M-Akiba will be limited by maximum daily limits on what can be transferred through the MNOs and the fact that the likely participants of the M-Akiba bonds will be on the lower end of the income scale, most of whom are net borrowers.

Box B.4: Diversifying financing sources via floating a diaspora bond

1. Role of migration and remittances in the Kenyan economy

Kenyans have been migrating since the 1960s, with the main driver for migration being the search for better living conditions. Today, more than three (3) million Kenyans live abroad (Government of Kenya, 2014). In 2015, about 455,889 Kenyans migrated abroad and more than 75% went to developed countries especially the UK (33%), the USA (23%), Canada (6%), Australia (4%), and Germany (2%). Migrant remittance inflows have steadily increased since 2000 (Figure 1). In 2016, remittance inflows amounted to US$1.6 billion, representing 3.4% of the country's GDP, and projections indicate an upward trend for the coming years. The UK and the USA are the major remittance sending countries accounting for about 2/3 of total remittances in 2015. From 2001-2014, the amount of money sent annually by the Kenyan diaspora was on average six (6) times higher than what foreign direct investors sent and projections show the gap is likely to continue (Figure 1). In addition to remittances, Kenyans abroad have huge untapped potential especially regarding their skills, knowledge, networks, and savings. It is estimated that overseas Kenyans save over $2 billion annually (Source: The WBG's Migration and remittances Team).

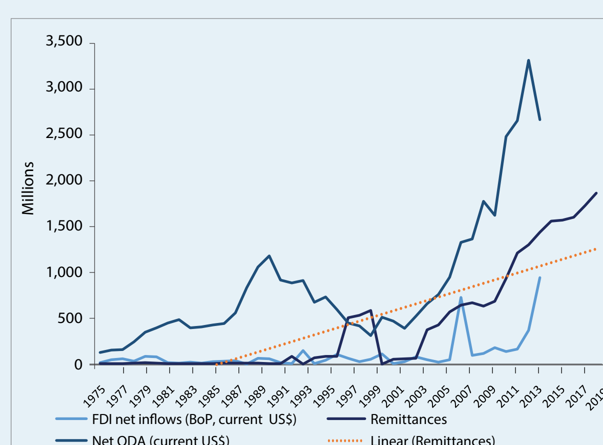
2. An opportunity to tap into the Kenyan diaspora savings through diaspora bonds

The Government of Kenya has recognized the diaspora plays a key role in the nation's economic development and it could support its Vision 2030. A Diaspora Policy was identified in 2014 and it recommends pursuit of a comprehensive remittance strategy and formulation of a policy to issue benchmark sovereign bonds that will finance the country's huge infrastructure gap. Because traditional development financing is difficult to obtain, Kenya has the opportunity to tap into its diaspora savings by issuing a diaspora bond — a retailed saving instrument marketed only to the diaspora, or friends of Kenya. This instrument could be used to finance infrastructure projects (i.e.: housing, schooling, hospitals, roads, etc.) with direct impact on the diaspora relatives or communities back home (Gnozi and Ratha, 2011). In the past, the country has dealt with its diaspora in this regard, with the issuance in 2011 of infrastructure bonds targeting the diaspora in particular. Diaspora generally has a lower country risk perception, which could allow them to accept lower interest costs. A few governments have used Diaspora bond across the world including Israel (since 1951), India (1991, 1998, 2000), Nepal (2010, 2011), the Philippines (2010), and Ethiopia (2011).

3. Not all diaspora bond initiatives have succeeded and key prior conditions are required

However, not all diaspora bond initiatives succeed. For instance, the government of Ethiopia issued diaspora bonds in 2011 to raise US$4.8 billion. However, these bonds were massively undersubscribed and in June 2016, the US Exchange Commission announced that the Government of Ethiopia violated securities laws and has to pay back US$6.5 million to more than 3,100 Ethiopian diaspora who are US citizens. Therefore, it is crucial for the government, before issuing the bonds, to insure that key prior conditions are met to guarantee its success. Special care needs to be taken with regard to the legal jurisdiction of issue, tenor and market size. Other important considerations include: the need to conduct diaspora surveys or surveys on focus groups to understand diaspora's characteristics, their saving profile, and attitude towards investing in their origin country, and designing the structure of the bond accordingly. Hiring legal and financial advisers would be crucial in order to insure proper registration and marketing of the bonds in the US, UK, and other investor destination countries.

Figure B.4: Trends in remittances, ODA and FDI to Kenya



Source: World Bank

Special Focus: Affordable Housing and Housing Finance

5. Affordable Housing and Housing Finance

5.1 Housing and Housing Finance in Kenya – Unaffordable and Unavailable

5.1.1. **Kenya is missing a major opportunity for job creation and economic growth** to formalize the housing industry and encourage it to better serve low income households. National and county governments could collaborate to create a productive cycle of savings and growth by fostering increased construction and financing of affordable housing.

5.1.2. **In Kenya, there's an estimated accumulated housing deficit of over 2 million units, and nearly 61 percent of urban households live in slums.**[3] This is because 244,000 housing units in different market segments are needed annually to keep up with demand, while current production is less than 50,000 units. As the supply of housing falls more and more behind the demand for housing, there's been an upward push against affordability. Many Kenyans are unnecessarily living in slum dwellings, because of limited supply and lack of affordability. So there is a critical need to deliver housing at the lower end of the income spectrum.[4] Given Kenya's growth and urbanization rates, the problem will only become more acute over the next decades without a serious focus on housing and the finance of housing for the average Kenyan (Box B.5).

5.1.3. **To date, the government's goal of increasing the formal supply of affordable housing is not being met.** Kenya's first medium term plan (MTP I, 2009-2012) of the Vision 2030 strategy had an initial target of providing 200,000 housing units annually for all income levels by 2012, but fell significantly short of this projection (only 3,000 units were provided between 2009 and 2012).[5] A second medium term plan for 2013-17 has a similar target of housing units, particularly focused on lower income households.[6]

Box B.5: Kenya's Growing Population and its Housing Needs

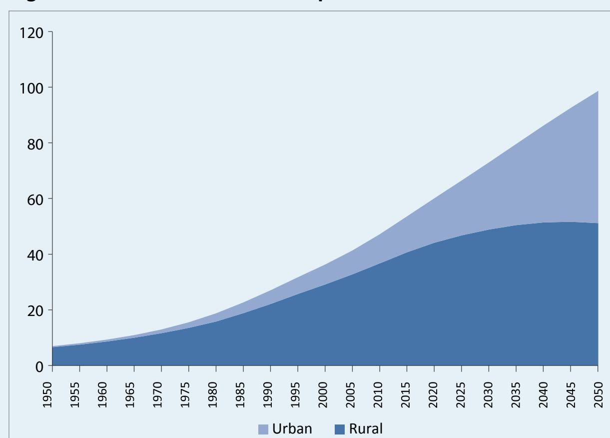
Urban and Rural Population (millions)
Urban & Rural

Kenya's urban population is growing at a rate of 4.4 percent per year, compared to 3.6 percent across sub-Saharan Africa. This urban growth is the equivalent of 0.5 million new city dwellers every year, compared to a 2.7 percent growth rate in the rural population, which still represents 0.7 million new rural inhabitants given the much larger starting size.

Total Housing Needs (000s)
Urban & Rural

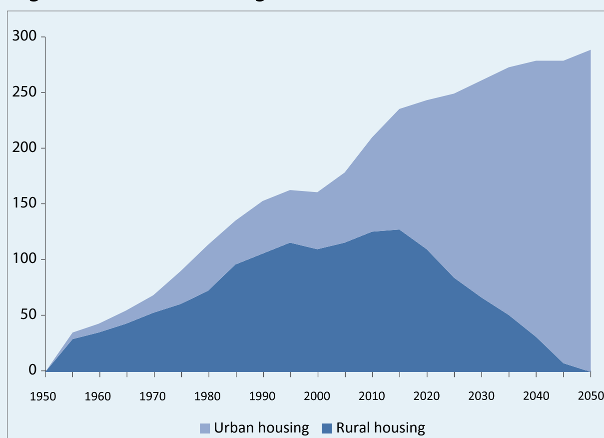
Total cumulative housing needs continue to grow steadily up to 2050 where they begin to level. Housing needs are slightly higher in rural areas currently but from 2018 onwards, the majority of new housing will be required in urban areas and will grow rapidly.

Figure B.5a: Urban and Rural Population (millions)



Source: World Bank calculations (2016) using UN Population data

Figure B.5b: Total Housing Needs (000s)



Source: Walley calculations (2016) using UN Population data

3 *Source: Habitat for Humanity, KUR, MDG definition of a slum.*

4 *According to the World Bank's Kenya Urbanization Review (2016), about 60 percent of Kenya's urban households live in housing that would be described as slum under the Millennium Development Goals.*

5 *Kenya Urbanization Review 2016.*

6 *Second Medium Term Plan 2013-2017, Transforming Kenya: Pathway to devolution, socio-economic development and national unity.*

5.1.4. While government's investments in housing are falling short, so are those of the private sector. Nairobi, for example, has a public target of developing 150,000-200,000 properties per year, but planning applications in 2013 were only 15,000 units. Furthermore, more than 80 percent of supply is for upper middle income (48 percent) and high income (35 percent), and only 2 percent for the lower income segments of the population.

5.1.5. Property prices in the formal market have been increasing, with Nairobi ranked as the highest priced city in Africa, creating an even greater affordability gap.[7] Prices in 2013 were nearly three times those in 2000, creating fewer opportunities for low and middle income families. The lowest price house formally built by a developer cost Ksh 1,342,106 ($15,300) in December 2012. But there is almost no supply on the market for less than Ksh 4 million ($43,956), especially in Nairobi.

5.2 Investing in Affordable Housing Pays Off

5.2.1. Addressing Kenya's housing shortage and housing affordability is not just about shoring up basic needs for the majority of the population, but will also be good for economic growth, creating jobs, and deepening the financial sector. Numerous benefits can be ascribed to improving access to housing finance and thereby housing. Homeownership has long been promoted as a way of giving individuals a stake in society and a stake in the economy. By having a stake that can increase in value, it provides an incentive for the homeowner to look after the property and also to maintain the neighborhood in which the house is situated. This theoretically results in lower crime levels and improved quality of life. Another social benefit that has been observed as arising from homeownership is lower fertility rates. This is a less intuitive benefit, but if the house is fully owned, parents in emerging markets (where there is no pension system) no longer have to rely on their children in their old age for somewhere to live. Further benefits include improved health, through better and safer construction, and improved sanitation.

5.2.2. The housing multiplier effect creates jobs for every house or housing unit constructed. Unlocking the residential housing market through the development of the housing finance market can provide a wide range of income opportunities through the construction sector and related industries as evidenced in Colombia, India, and South Africa. In Colombia it is estimated that 5 additional jobs are added for every US$10,000 spent on housing construction. In India, each housing unit creates 1.5 direct and 8 indirect jobs; in South Africa, each housing unit creates 5.62 jobs for every housing unit.[8] This is a central argument in favor of housing investment. The premise is that every unit spent on housing will generate a multiple amount of benefit for the economy, as it creates jobs through horizontal and vertical supply chains. This includes jobs in areas such as raw material production, mining, cement production, timber, and aggregates. In addition, there is also an impact on local economies where the construction jobs are created, and in the service industries linked to housing, such a mortgage lending, real estate agents, and retailers of home goods such as furniture or white goods.

5.3 What is Holding Back Affordable Housing?

5.3.1. A key constraint for low and middle income buyers comes down to limited supply of financing. Kenya has a dynamic mortgage industry, which is becoming increasingly competitive. A number of institutions are now in this sector, including banks, microfinance banks and Savings and Credit Cooperative Organizations (SACCOs). The mortgage market has grown at around 30 percent annually, based on data from the Central Bank of Kenya; however, the overall mortgage portfolio remains modest.

5.3.2. There are fewer than 25,000 mortgages outstanding in Kenya, with an average size of Ksh 8.3 million (US$80,000 at a current Ksh/USD rate of 103.7), up from Ksh 4.1 million in 2010, primarily as a result of higher property prices.[9] Mortgage debt in 2015 represented 3.15 percent of GDP and, as of December 31, 2015, the total mortgage book issued by commercial banks stood at Ksh 203 billion (about USD 2.1 billion) showing a growth of 24 percent over 2014. In comparison, mortgage debt to GDP ratios in other African countries outside of South Africa are relatively low (see Figure 26), particularly when contrasted to the more developed countries (for example, the USA has a mortgage debt to GDP ratio of 56 percent).

5.3.3. Currently, mortgage lending is funded almost entirely by short-term retail and institutional deposits and only a few financial institutions have accessed the capital markets. The appeal of Capital Markets is that they

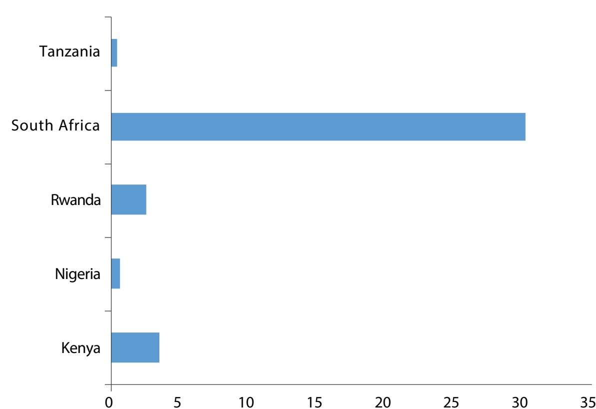
[7] *Knight Frank Prime Global Cities Index.*

[8] *Source: Viruly (2012), Tibaijuka, Anne. 2009. Building Prosperity: Housing and Economic Development. UN HABITIAT.*

[9] *Central Bank of Kenya. Mortgages, for the purposes of these statistics, relate to those mortgages extended by commercial banks under CBK regulation as at December 2015.*

provide the possibility of long-term funding for housing and reduce the liquidity risk. The potential to harness large pools of long-term funds (like pensions and insurance) for housing finance is very attractive and will deal with this asset-liability mismatch, lengthen the maturity of loans and improve affordability.[10]

Figure 26: Mortgage Loans Outstanding as % of GDP (2015/16)



Source: HOFINET and the Centre for Affordable Housing Finance 2016 yearbook

5.3.4. **In addition, there is little efficiency in the way banks originate loans or enforce loans.** For example, there is little standardization of mortgage market documentation, including loan underwriting, documentation or servicing procedures. Foreclosure law can be a source of delay and frustration due to frivolous and repeated appeals.

5.3.5. **Yet, less than 10 percent of all housing credit comes in the form of mortgages from the banking sector—the remainder of housing finance comes from SACCOs and housing cooperative networks.** The constraints for banks are mainly in terms of risk-return decisions, but housing finance is also considered to be relatively unattractive compared with investment in T-bills. The administrative burden of complex land transfer and mortgage registration is a further disincentive to increase the amount of mortgage finance. Moreover, reaching down-market requires assessing the credit risk of informal sector borrowers, which is problematic. The majority of informal sector borrowers are more interested in incremental financing and self-construction loans. The main providers of housing finance for this sector are the cooperative networks or the SACCOs.

5.3.6. **The share of SACCO-financed housing is estimated to be as high as <90 percent with banks providing the remainder of the finance.** SACCOs offer smaller formal mortgage loans through the KUSCCO Housing Fund and provide large amounts of unsecured loans used for self-construction. Some SACCOs are able to offer shorter medium term loans of as little as 1.05 percent per month interest (12.6 percent annually) for an amount of up to three times the savings balance held with the SACCO. Terms of loans can be for as many as seven years. Loans are typically unsecured, or at least not secured with a mortgage lien over a property. Despite limits on the amount and the shorter term, this type of credit is more easily accessible and is provided at a cheaper rate than many of the main banks can offer.

5.3.7. **Housing Cooperatives also play an equally important role in financing houses.** On one hand, they purchase land and resell to members with some financing support for self- building. Alternatively, they act as a full developer, with projects ranging from 10 houses to several hundred. In interviews with housing cooperatives it was found that they provide a good range of housing options with prices varying from as low as KSH600k up to KSH14 million. Location is a big factor in terms of determining the overall housing cost and the cost of infrastructure is a major determinant in the type of housing that is built. The cooperative housing provider has to break even and often the only way is to also build upper end housing where a larger premium can be charged.

5.3.8. **SACCOs and cooperatives are filling in the gap for financing houses, but themselves are held back by lack of finance.** Both SACCOs and housing cooperatives together are the main providers of housing finance in Kenya. While official statistics are not available, industry estimates suggest that the SACCO and cooperative sector are providing over 100,000 housing loans, with 10% being actual registered mortgages. The sector also provides these loans at more affordable rates, rarely exceeding 14% interest p.a. However, SACCOs have only one main source of liquidity, which are member deposits. Without access to longer term sources of finance, their loan portfolio will be unable to grow further.

[7] *Knight Frank Prime Global Cities Index.*
[8] *Source: Viruly (2012), Tibaijuka, Anne. 2009. Building Prosperity: Housing and Economic Development. UN HABITIAT. McKinsey (2012).*
[9] *Central Bank of Kenya.*
[10] *Walley, Simon. Developing Kenya's Mortgage Market, 2011.*

5.3.9. **Low or informal incomes, combined with high financing costs, are also holding back the demand for housing finance.** Mortgage loans remain unaffordable for most households. Prudent lending standards suggest that households should not allocate more than 33 percent of net monthly income towards their housing costs on an ongoing basis.[11] The actual cost of the property includes the cost of the land, be it for purchase or construction. The costs associated with the financing include the quantum of down payment and transaction costs (including charges, legal fees, and taxes). Other factors include loan duration, the maximum loan to value, the type of amortization, and the interest rate on the loan.

Table 1.2: Affordability calculator

	Ksh	USD
Maximum Payment to Income[13]	40%	
Cost of cheapest formally built property	KSh1.8 million	$17,315
Maximum Loan to Value	90%	
Cost to register a mortgage and title transfer	4.35%	
Interest Rate	14%	
Loan Duration	15 years	
Amortization	Declining Balance	
Monthly payment amount	KSH 21,168	$208
Implied annual income	KSH 635,048	$6,225
Required cash savings	KSH 253,440	$2,485

5.3.10. **Lack of affordability continues to keep high potential buyers out of the market.** (Table 1.2) shows that for the cheapest available property, an annual income of Ksh 635,000 ($6,200) is required, together with a substantial cash savings component of almost Ksh 250,000 ($2,500) to cover mortgage registration costs, down payment on the property, and title registration.[12]

5.3.11. **The majority of Kenyans have informal incomes and few can afford homes built by formal developers, resulting in mortgage lending being accessible to only a minority of the population.** Only about 10.2% of urban households could afford the cheapest newly built house in 2015, estimated to cost about Ksh 1.7 million / US$17,000. This price represents a drop in the minimum cost of a mortgageable property, which was previously set at Ksh 4 million (in 2011). The reason for this drop reflects the greater availability of lower priced housing offered by developers. There is no detailed data on supply, and there is certainly evidence that house prices generally are increasing but there has also been a move towards provision of more affordable housing by developers who may be feeling

[11] However, mean rents are 40.8% of income in Nairobi (Kenya National Housing Survey, 2012/2013). This suggests that many households will be willing to spend 40% of monthly income in the case of house purchase.

[12] The average loan is a15-year variable rate loan (maturities typically range between 15 to 20 years) with interest rates varying between 13-18 percent. The analysis assumes an interest rate of 14% in keeping with the recently instituted interest rate caps in Kenya (see below). Even if banks propose higher Loan to Values (LTVs) in locations where the prices of real estate collateral have been appreciating, these loans still remain out of reach for most borrowers. In August 2016, the Banking (Amendment) Act was signed into law. The new law caps lending and deposit rates at 400 bps above and 70 percent of the base rate set and published by the Central Bank of Kenya. There are some concerns that this may have an impact on all long-term financing but it remains to be seen how implementation plays out and how banks adjust to this new reality. Margins are high but differ between the largest banks, which dispose of a cheap retail deposit base (cost of funds around 4 percent), and other banks that depend on more expensive and volatile corporate deposits (around 12-13 percent). The former group has more room to further reduce margins if the competition drives them in that direction.

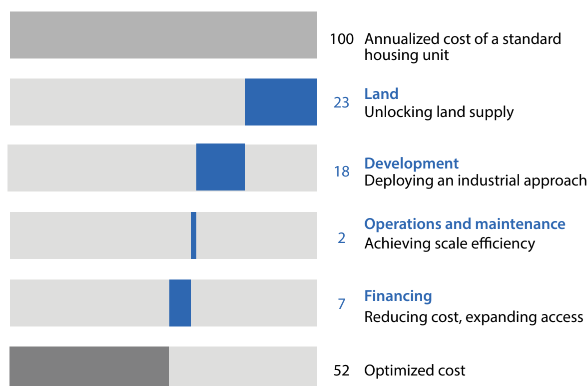
[13] See footnote 8 above.

that the top end luxury housing market is beginning to be saturated. It is worth noting that this does not represent a major shift, and the majority of formal housing is still at the top end, but there is some availability for housing closer to Ksh2 million that simply did not exist a few years ago.

5.4 It's More Than Finance Constraining Affordable Housing

5.4.1. A lack of affordable finance is only one of the barriers to greater supply of affordable housing, and making financing more available for home purchase or construction is also only one of the solutions. A recent McKinsey Global Institute report discusses the main 'levers' to reducing the cost of housing (see Figure 27).[14] In addition to financing, factors that impact overall affordability includes such factors as the overall construction costs; the cost of land; ancillary costs such as those associated with putting in utilities or access roads; and the costs of maintaining property (McKinsey, 2014). The demand side factors are more closely related to how the property is acquired and particularly the cost of financing. The modalities of the financing, such as the term of the loan and interest rates, will be the main factors determining whether a household is able to afford a property or not.

Figure 27: Four Levers to Address Global Affordable Housing Challenges

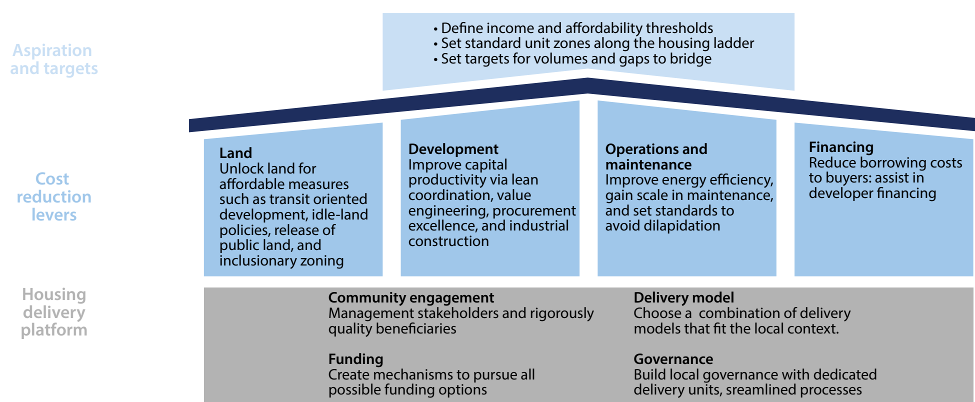


Source: McKinsey Global Institute

Figure 28 shows in a bit more detail the proposed dynamics in the McKinsey model. This provides a good system for application in Kenya. The Government, through a process of consultation with stakeholders, could consider each stage of the process, starting with target setting. In particular, the government could be clear about what it expects the market to do and at which point it is prepared to intervene to enhance access. Costs can then be assigned and benefits assessed to ensure best use of limited fiscal resources.

5.4.2. Cumbersome property titling/registration processes have often been one of the main constraints to providing urban land for housing. Difficulties or delays in obtaining clean titles leads to a decrease in investor appetite and also prevents households from being able to secure financing from banks.[15] The mapping and transparency of land ownership is also deficient, often making it difficult to have a clear sight of land right holders, even in the case of public land, which is said to be seldomly registered. However, in the *Doing Business* 2016 report, Kenya was recognized for its reforms in property registration, particularly for increasing the pace of property transfers by fully digitizing its records, improving electronic document management at the land registry and introducing a unified form for registration.[16] It is worth noting that despite all of

Figure 28: Systematically Addressing Affordable Housing



Source: McKinsey Global Institute

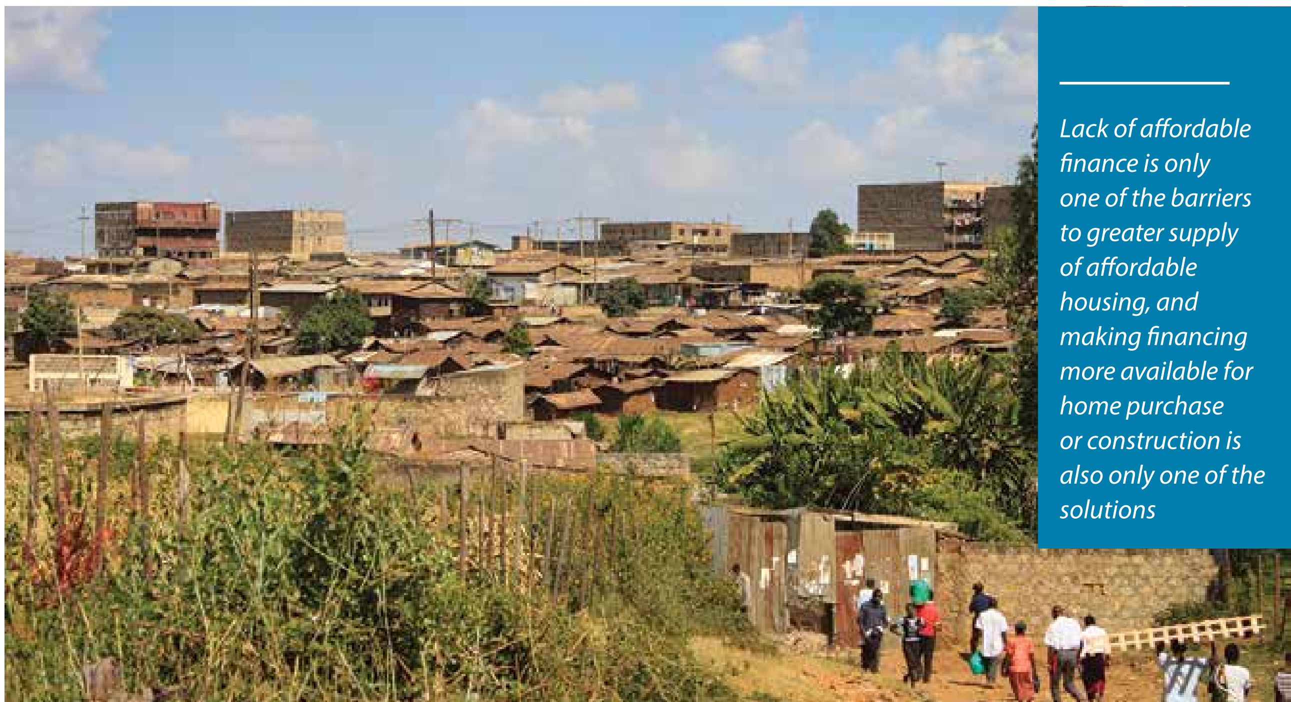
[14] McKinsey Global Institute. A blueprint for addressing the global affordable housing challenge. October 2014.
[15] World Bank. 2016a. Kenya Urbanization Review.
[16] World Bank. 2016b. Doing Business Report.

the reforms and new laws, operational difficulties remain in achieving the desired efficiency in registration. Some of the costs of difficulties associated with two types of registration are as follows: i) Registered Titles Act—cumbersome, slow, and uses voluminous documents. On average it takes four months to register a cash buyer and nine months to register a mortgage buyer, which is entirely too long – as opposed to the few days it should ideally take. These kinds of delays reduce the attraction of affordable housing as a business for developments and lenders. ii) Sectional Properties Act—supposed to be the easier registration system but the reality is that it is only used by tenant purchase schemes because they still own the Mother Title and the developed unit.

5.4.3. Land is very expensive in urban Kenya, and it does not help that speculators are driving prices upward further. Speculative behaviors have triggered rapid price increases since 2009, and the absence of tools to limit their impact has made this a major problem for land markets. There is also the limited supply of serviced land - insufficient capacity to develop infrastructure in parallel with urban expansion and land allocation or conversion. The responsibility for providing this infrastructure is then transferred to developers who in turn pass the related cost on to buyers through higher prices. Reliance on private developers to provide infrastructure results in inefficient and more costly solutions.

5.4.4. The cost of construction impacts developer financing and their appetite to move further down market. The National Housing Survey of 2012 notes that building materials account for 40 percent of housing costs.[17] Construction in Kenya is heavily dependent on the use of stone and cement, which means that any price movements or increase in taxation on these traditional materials will have a significant impact on the provision of affordable housing. There are also related construction costs in terms of permit fees that are constraining factors. The small scale of most developments also affects housing affordability. This is due to several factors, including the scattered developer industry comprising of many individual, unregistered developers,[18] insufficient equity capital of many developers more generally, and the challenge for the land administration to quickly deliver large volumes of titles. In addition, the possibility of granting a VAT exemption to affordable housing developments over 20 units, approved in principle by the government, has not been applied yet.

5.4.5. Kenya's devolved system of government means that county governments are now responsible for delivering affordable housing at the county level. County Governments can work with private sector developers and financiers to deliver affordable housing, including through Public-Private Partnerships and Joint Ventures. However, there are still growing pains with this system leading to



Lack of affordable finance is only one of the barriers to greater supply of affordable housing, and making financing more available for home purchase or construction is also only one of the solutions

[17] Kenya National Housing Survey 2012/2013.
[18] 2012/2013 Kenya National Housing Survey.

deficiencies in urban planning and stable land use rules.[19] Some developers have voiced concerns over lack of clarity on the scope of county functions, as well as the variances in approval/procurement processes across counties. These challenges will need to be addressed and trust built between the counties and the financiers and developers.

5.5 Innovative Instruments to Address Financing Can Be Catalytic

5.5.1. **While not sufficient on their own, financing solutions can play a catalytic role in stimulating both supply and demand of affordable housing, and can help create momentum for other underlying reforms outside the sector.** On the supply side, such solutions that the World Bank has employed in other emerging markets include the creation of Mortgage Refinance Companies (MRCs), the provision of Housing Finance Guarantees, and developing Public-Private Partnerships (PPPs) for Affordable Housing. Focusing on affordability and the provision of products aimed at informal income can increase the demand for financial products for housing. Examples implemented in other emerging markets include Interest Rate/Down Payment Buy Downs and a focus on Housing Microfinance through microfinance institutions and SACCOs. Experiences from these other jurisdictions is that the creation or focus by Government on such initiatives can also lead to wide consultation and the creation of inter-ministerial committees dedicated to needed reforms for the affordable housing agenda.

5.5.2. **A mortgage liquidity facility, or mortgage refinance company (MRC), can be an effective, low-cost institution with the main purpose of providing long term funding to lenders.** There are several reasons why a mortgage lender would look to a liquidity facility and the capital markets for funding, including: i) the lender may be capital-constrained (at least on the margin); ii) the lender may be liquidity constrained, and; iii) the lender may have cash flow risk management needs. An initial feasibility assessment of a Kenya Mortgage Refinance Company (KMRC) has been conducted by the World Bank and preliminary results are presented in Box B.6.

5.5.3. **The nature of an MRC is that it provides an institutional intermediary between mortgage lenders and capital markets.** In developing financial systems, it allows lenders to aggregate their funding needs through a single bond issuer. A key advantage is, therefore, that medium- or smaller-sized institutions are able to access funds on the same terms as larger ones. A second approach could be for MRC to be established as an off-balance-sheet funding provider where mortgages are bought and taken off the balance sheet of lenders and packaged for purchase by investors. The benefit of this approach is that it frees up capital for lenders and may enable them to expand at a faster rate. Whichever approach or combination of approaches is used, an MRC must be created as a private sector institution with private sector equity.

5.5.4. **Nigeria and Tanzania provide good examples of how the overall MRC projects created momentum, focus and pressure towards the resolution of issues outside of the immediate long term funding question.** In Nigeria, several linked actions have been undertaken with NMRC as a champion, helping to organize the sector and provide the necessary support to get the changes organized (see Box B.7). Specifically, this includes an industry wide agreement on Mortgage Underwriting Standards. This sets out a common set of criteria covering a broad range of points such as documentation, security, consumer information, minimum prudential standards, insurance and others. Further steps are now being worked on such as minimum underwriting standards for informal sector lending and minimum underwriting standards for Sharia compliant loans.

5.5.5. **In Tanzania, a very good practical example was the focus on one of the key bottlenecks to mortgage lending faced by developers.** As they try to sell off completed housing to end users financed by mortgages, the developers experienced big backlogs in obtaining 'unit titles' i.e. the subdivision of their large developer land plot into individual units. This created a knock on effect on access to finance and meant that developers had to sit on their loans for longer periods, or provide additional forms of guarantee for the financing to flow. This made the whole process uneconomic, riskier and detrimental to overall growth and investment into the sector. The Tanzania Mortgage Refinance Company (TMRC) together with key stakeholders was able to mobilize all concerned parties and work through an approach to resolve this issue. This will take time, but would not have happened or been a point of focus had TMRC not been in existence.

5.5.6. **A housing guarantee mechanism for those with low incomes or employed in the informal sector could help expand access to housing finance.** Private Mortgage

[19] *A revision of the 1996 Physical Planning Act is under way.*

Insurance already exists in the Kenyan market, which attests to the level of market development; however, it remains a limited product. A larger scheme potentially supported by a public sector institution could assist in taking some of the credit risk associated with lending to those with lower incomes and expand access. Equally a large proportion of creditworthy potential borrowers are currently not able to access loans because they do not have a formal salary. A guarantee product that protects lenders against some potential losses incurred when lending to those in the informal sector could significantly expand access. Such a scheme currently operates in Morocco and has proven to be very successful (see Box B.8). A similar scheme has also just been initiated in India with the same premise of providing some credit protection for lenders reaching down to those on lower incomes or on informal incomes.

5.5.7. **PPPs for the provision and delivery of affordable housing as well as the attendant infrastructure is critical in reaching the scale of investment necessary.** There are numerous models on how public and private sectors work together both in the provisions of affordable housing and of urban infrastructure (see Box B.9). Having a clear set of guidelines and rules is very important. Transparency in the process will make it easier to attract and structure transactions. A typical PPP allows a private consortium to assume the financing risk and two or more phases of a housing project's lifecycle. This may include the design and construction phases of the project and the subsequent maintenance and operation of the government facility under a carefully contrived long-term lease. This is in contrast to the private sector's traditional role in urban infrastructure development where its involvement is limited to providing

Box B.6: Findings of the Kenya Mortgage Refinance Company (KMRC) feasibility[20]

The purpose of establishing KMRC would be to offer the housing finance market in Kenya a credible, professional and high quality large scale medium- to long-term refinance/liquidity provider. KMRC would serve as a secure source of long term funding at attractive rates while ensuring sound lending habits among primary mortgage lenders (PMLs), resulting in greater availability of fixed rate mortgages and longer available loan terms. This would, in turn, help improve the affordability of mortgages, increase the number of qualifying borrowers, and result in the expansion of the primary mortgage market and home ownership in Kenya while deepening the capital markets.

The preliminary analysis shows that after five years of operation, **KMRC could double the number of mortgages that would have been outstanding in Kenya if the market had grown organically.** This would mean a projected number of **140,000 mortgages outstanding compared to 70,000** (including SACCOs) by 2022, in the absence of the KMRC, with close to one third of the borrowers being of either lower or informal income (for a Ksh 3 million dwelling). **The facility would also increase the number of fixed rate mortgages and extend the term of such mortgages.** In order to reach these potential targets, the facility would require Ksh 1.5 billion in equity capital (primarily from market participants and other investors); it would also require an additional tier 2 capital investment and capital to finance an interest rate buy-down program and/or direct line of credit (LOC) to SACCOs, with a combined value of **US$250 million**.

With access to refinance over the next five years, **banks could originate an additional 60,000 mortgages for a total mortgage debt outstanding of Ksh 635 billion, more than three times the value of Ksh 203 billion today. KMRC could also offer both refinancing and 'pre-financing' to SACCOs, reaching an additional 25,000 SACCO borrowers over a five-year period.** The facility would be able to refinance only SACCO loans that are registered formal mortgages on titled properties, since KMRC bond investors would most likely accept only collateralized loans for refinance. It is estimated that **there are approximately 10,000 formal mortgages totaling Ksh 40 billion at SACCOs and that with access to KMRC this number would increase to 25,000 and Ksh 81 billion over the next five years.**

It is important to note that many of the essential preconditions for the development of housing finance are currently present in Kenya or are under discussion and the presence of KMRC can catalyze further reforms and improve the environment for affordable housing as evidenced in other countries.

[20] *It is important to recognize that the initial analysis was completed in the midst of implementation of the Banking (Amendment) Act of 2016 that capped lending and deposit rates at 400 bps above and 70 percent of the base rate set and published by the Central Bank of Kenya. The analysis suggests that benefits still accrue in terms of increased mortgage volumes and lower rates, irrespective of the prevailing regulatory environment. However, considerable uncertainty remains as to how the interest rate cap, as well as the floor on deposits will impact long-term lending and the funding of long-term lending*

Box B.7: The Nigeria Mortgage Refinance Company

The NMRC is a private sector company with a public sector purpose of developing the primary and secondary mortgage markets by raising long-term funds from the domestic capital market as well as foreign markets and thereby provide accessible and affordable housing in Nigeria. NMRC was incorporated on 24th of June 2013 as Nigeria Mortgage Refinance Company Plc.

It was developed as part of a wider Housing Finance Project supported by the World Bank through a US$300 million loan to the Federal Government of Nigeria. The program has three main components: i) development of a mortgage liquidity facility; ii) development of a housing finance guarantee product; and iii) development of housing microfinance pilot schemes.

The bulk of the funding was allocated to support NMRC's balance sheet and future growth. This was done by releasing up to US$250 million in tranches of Tier 2 equity. The release of the funds is dependent on performance and issuance of bonds. This differs from previous schemes where funding was provided as a straightforward credit line. The structure used in Nigeria allows the funds to be leveraged in the market, supports sustainable growth of the company and does not create misaligned incentives in terms of pricing of concessional funds versus cost-of-market funds.

NMRC completed its first bond issue in July 2015 for an amount of NGN 8 billion (US$40 million), as part of a NGN 140 billion (US$700 million) Medium-Term Note Program. The issuance was supported with a Federal Government Guarantee in recognition of the support that a new institution will need to go to market. As NMRC establishes itself, the objective is for it to go to the bond market on its own.

A key step, which NMRC has already completed in developing the market, is the creation of standard underwriting criteria. These detail the minimum quality standards that a mortgage loan must meet to be eligible for refinancing with NMRC. This effectively creates an industry minimum quality standard and helps with standardization and improved efficiency.

Pension funds in Nigeria have been eager for alternative investments to Government bonds and the bond issuance was well received and over-subscribed. As the mortgage market grows, it is expected that NMRC will be the leading private issuer in the country.

Box B.8: The Moroccan Guarantee Scheme for Low Income Housing Finance

Created in 2004, FOGARIM primarily targets low-income households with irregular earnings. It provides guarantees covering 70 percent of losses on mortgage loans. Given the type of income, the main selection criteria are prices (limited to US$25,000) and the level of monthly installments, capped at about the equivalent to US$200 (upper income threshold) and 40 percent of the households' income (lower threshold). Guarantees can be enforced after nine-month arrears, and once the foreclosure process has been initiated. After an initial phase where guarantees were granted for free, FOGARIM switched to a risk-linked premium system, where the amount of premiums is inversely linked to the size of the down payment.

In 2009, FOGARIM was merged with another guarantee fund that targets moderate-income civil servants, middle class independent workers and non-resident Moroccans buying or building houses up to US $100,000 in value. The consolidated fund, Damane Assakane, was guaranteeing MAD 9.3 billion at the end of 2010 (US$1.2 billion), while its own funds amounted to MAD 0.95 billion.

A reform of the guarantees was underway in 2011. In the "social housing" compartment, the price ceiling has been raised to US$100,000, and the maximum monthly installment to US$300. For other categories, the price ceiling should be removed but the guaranteed amount capped at US$50,000. Claim processing will be overhauled, with payment first and validity checks afterwards.

Box B.9: Testing the Water: A PPP in Affordable Housing in Kenya

In order to encourage increased private development of affordable housing the Bank is supporting a project proposed by Nakuru County Council in Naivasha in October 2016.

The project consists of the public sector providing land, providing a detailed feasibility study (in the initial phases funded and managed by the Bank), and inviting private developers to build housing serving lower income groups. The units will be for sale at the commercial risk of the developer.

Emphasis is being placed on preparing a feasibility study that provides highly detailed data on site conditions, available infrastructure, market demand and regulatory issues so as to minimize the risks for the private developer. Costs are being kept low (consultants costing a total of about $65,000), so as to establish a replicable methodology. Sketch designs are currently being prepared, and the RFP is scheduled to be completed by the end of March.

skilled labor under short-term contracts, with the delivery of the services being solely provided by the public authority. It is also important not to confuse PPPs with privatization, a situation where responsibility over the delivery of the public service is fully transferred to the private partner with little or no government oversight.

5.5.8. **Housing finance subsidies can be used as an incentive for low or informal income borrowers.** It is important, though, that any form of housing finance subsidy is transparent and can be carefully targeted. A mortgage subsidy program, for instance, could operate on the basis of a buy down of the monthly payment, so in effect part of the mortgage loan would be paid for by the borrower and another part by the mortgage subsidy (see Box B.10). The benefit of such a mechanism is that from the lenders point of view this is a regular mortgage loan at a regular price, so is entirely sustainable. From the fiscal authority point of view, the benefit is the leverage that can be obtained, because the subsidy only provides the affordability enhancement without the need to fully fund the whole mortgage loan. SMART subsidies can be used to obtain maximum leverage and use of fiscal resources.

5.5.9. **Housing Microfinance (HMF) is an adaptation of traditional microfinance loans that target small loans for self-help housing or progressive building,** including land purchase or access, provision of or improvement to services, as well as full or incremental house construction, renovation, or maintenance. Microfinance clients often make the economically rational choice to use business loans for housing needs in response to the lack of widespread access to housing finance. Despite having one of the most developed microfinance sectors in Sub-Saharan Africa, there is only limited penetration in the Kenyan market for housing microfinance lending.

Box B.10: A SMART Demand Side Subsidy Mechanism: France - The Zero Percent Housing Loan

Contrary to what its name could imply, the PTZ is a direct demand subsidy that lowers borrowing costs to households meeting certain income criteria. Main features:

- The PTZ is a loan. It can be extended by any credit institution that has entered an agreement with the State for that purpose
- It carries a 0% interest for maturities up to 25 years that vary depending on the family income
- The subsidy covers the difference between the Net Present Value of a PTZ and a housing loan at market conditions. It is allocated to the lender, initially through an up-front payment, now in the form of a tax reduction
- Eligibility criteria: income ceilings, fairly high (ex. 5,000€ per month for a 3 person household), and price ceilings. Both parameters vary with the household size and the location. Additional criteria include environmental standards.

Overall, a non-distortive mechanism (open to any credit institution, no impact on the lender's interest rate policy) that aims at ensuring fixed debt servicing-to-income ratio, a better approach than lump-sums with possible negative redistribution impact. One of the issues: discrepancy between the very large potential coverage (about 2/3 of households) and the public finance capacities.

5.5.10. HMF loans are generally unsecured, and granted to individual borrowers, rather than to groups of borrowers (as is sometimes the case with microenterprise loans). Housing-related microloans are on average larger than general microloans but seldom exceed the size of the lowest-level of readily available mortgage finance products. In certain cases, HMF products include additional financial and non-financial service elements, including:

- Savings schemes that establish the creditworthiness of a borrower prior to extension of a housing microloan and automatic re-extension of subsequent loans;
- Non-financial services such as housing-related information, design and building advice, and technical assistance for homebuilders linked to HMF; and
- In certain cases, housing microlenders institute systems and procedures to assist with procuring materials, in part to ensure that the loan is used for housing purposes.

5.5.11. HMF loans are also larger and for longer terms than traditional microfinance loans, and the loan proceeds would not produce a return through an investment into a business. This last point is an important one as it materially changes the lender's approach to selecting customers and assessing risk. Herein lies the greatest difficulty in adding housing microfinance to the product range of traditional microfinance lenders, as they do not have the skills or experience necessary to underwrite longer-term loans and on occasions take collateral.

5.5.12. When it comes to funding HMF, institutions that are registered as banks can rely on demand deposits, while Non-Bank Financial Institutions (NBFIs) seek savings accounts. Another distinction can be made among institutions offering HMF: (1) microfinance institutions that fund themselves on strictly commercial terms at market rates, and; (2) those that are also subsidized through various combinations of grants, donor, and government funds. Commercial borrowing may be facilitated by credit enhancements. Subsidy funding may take the form of infusions of capital or funds to increase liquidity. Box B.11 provides a current example of an initiative aiming to bridge

Box B.11: India Lending Model for Informal Borrowers and Informal Property

In May 2015, the National Housing Bank launched a "Special Urban Housing Refinance Scheme for Low Income Housing," which, for the first time, provides refinance for "loans secured either by collateral of property financed or alternatively secured." Until this point, most housing finance companies engaged only in mortgage-backed lending, although some innovative lenders had developed alternative security strategies such as the Self Help Group or Joint Liability Group Guarantee. However, these were being used in addition to, and not instead of, conventional property based security (albeit sometimes a quasi-mortgage). Indian law and banking regulations did not specifically prohibit housing finance operations that were not mortgage-backed, but seemed overwhelmingly to address only mortgage-backed lending, and there were no guidelines or directions relating to alternative security. This is perhaps one of the reasons for lack of innovation and expertise in alternative security in the housing finance sector.

In this respect, the "Special Urban Housing Refinance Scheme for Low Income Housing" is an important first step, as it clarifies to all concerned that NHB can also cater to alternatively secured lending. Subsequent steps in this direction, which can help mainstream alternatively secured lending, could include the issuance of guidelines for alternatively secured lending.

For lenders who seek to provide credit in this sector, the scheme, for the first time, also provides clarity on the building regulation requirement for informal and incremental housing in areas where formal approval systems may not be in place. Recognizing that urban low-income housing has very specific conditions and risks, the scheme provides environmental and social due diligence framework for primary lending institutions who seek refinance. The framework for environmental due diligence requires lenders to carry out technical assessments to ensure: i) housing in hazard prone locations, or in locations where it can have adverse environmental impact are avoided; ii) sites for housing have access to potable water and basic sanitation facilities (or explore options for additional funding to address these concerns); iii) screening of household occupations for hazardous or illegal trades and activities; and iv) the structural safety of the physical dwelling including compliance with safety standards and building regulations (in case of formal housing), and direct assessment of structural safety and load bearing capacity in case of informal/ incremental housing where formal approval systems are not in place. The framework for due diligence explicitly recognizes that formal building plan approval systems may not be available for potential low-income borrowers, and provides that this requirement may be replaced by technical assessment by the lender itself.

Source: Arkaja Singh, adapted from Case Study of Swarna Pragati Housing Microfinance in Rural Areas, November 2015

the gap between microfinance and mortgage finance by providing dedicated funding resources for the purpose of lending to the informal sector.

5.6 Regulatory Reforms for Unleashing Housing Finance Supply and Demand

5.6.1. ***Standardize mortgage contracts.*** Standardized forms and documentation have many benefits, including making mortgages comparable across financial institutions, and making it easier to package these mortgages for sale in the secondary market. An ancillary benefit of establishing a Mortgage Liquidity Facility is that its operations would contribute to the improvement of lending practices in Kenya and incentivize standardization of terms and conditions among lenders.

5.6.2. ***Ensure a conducive regulatory environment for housing finance products.*** For instance, a Mortgage Liquidity Facility that issues bonds as infrastructure bonds should not be subject to withholding tax and would be effectively tax exempt. This should not, however, prevent an assessment of the efficiency of the income tax exemption of infrastructure bonds, which can deter, through resulting high prices, non-taxable pension funds to buy them.

5.6.3. ***Establish appropriate mortgage foreclosure regulations.*** The current Foreclosure Law process works relatively well in most cases, but the potential is there for long drawn out cases through the use of repeated appeals. The recent amendment to the mortgage law provided a legitimate increase of the protection to borrowers. It would be useful however to keep the balance with creditors' rights to limit possible abuses of the process by willful defaulters.

5.6.4. ***Clarify and implement the legal and regulatory framework for mortgage-backed securities and covered bonds.*** The development of fixed rate options, which only capital markets can hedge, would be highly beneficial for the market since there is a high reluctance on the demand side to contract long-term debt on a floating rate basis. The Capital Markets Authority first needs to complete the legal and regulatory framework for securitization, which includes drafting amendments for the tax neutrality of the SPV/trust and changes to company law and insolvency law. More work is also needed specifically with respect to using clawback mechanisms to manage risk. In terms of covered bonds, the appetite exists among institutional investors for a secure and transparent instrument, so efforts should be made toward drafting and implementing a legal and regulatory framework to support the development of this market.

5.6.5. ***Create a conducive environment to mobilize long-term domestic capital and bridge the funding gap.*** Kenya's pension and insurance markets are well developed; with over Ksh 1 trillion in long-term investment funds, there is strong demand for high quality investments such as mortgage-related bonds. A supportive policy framework, improved regulatory environment, reliable indices etc. are all incentives that can be used to encourage the active participation of institutional investors in the market. The banking sector in Kenya remains largely liquid with substantial lending headroom in the mortgage sector before it hits liquidity constraints. Some market practitioners estimated that banks could double their mortgage portfolio through further deposit transformation. Only beyond that would they need to issue long-term mortgage securities among pension funds or insurance companies. Even the most active lenders do not see any urgency to issue, given the currently expensive conditions through capital markets. Nevertheless, the matching of assets and liabilities maturity should receive more consideration by the lenders and the regulators (including SACCO Societies Regulatory Authority (SASRA), charged with regulating SACCOs). Several structural challenges need to be addressed to realize the potential of the capital markets as a funding source over the coming years. There must also be a class of investors with the appetite and capacity for securities backed by mortgages (most likely insurance companies or pension funds).

5.6.6. ***Enhance the role of cooperatives and SACCOs in affordable housing.*** A deeper analysis, potentially backed up with a lender survey of the SACCO sector, together with the Housing Cooperative movement should explore the size and reach of housing finance through this channel. The potential for expanding access is much larger in this sector, given that the customer base is often made of those on lower incomes or working in the informal sector, which represents the majority of Kenyans. Such a study should explore: i) basic size, data, and products on offer by SACCOs and MFIs (which do not seem to have a well-developed offering for housing); ii) regulatory framework; iii) governance standards; iv) funding sources for longer-term credits; and v) potential linkages to affordable

housing supply solutions, for instance around the Ksh.1 million mark. In terms of regulation, neither housing cooperatives nor KUSCCO are directly regulated, unlike other financial institutions. At a minimum there should be a common and level playing field for all operators in the housing finance sector.

5.7 Accompanying Housing Finance Reforms

5.7.1. **Housing finance initiatives will be much more effective and yield better results if the overall housing and housing finance framework is operating efficiently.** Key actors will only be able to produce results if the enabling environment is supportive of affordable housing delivery models. The enabling environment covers all the processes and steps that have to be taken in the value chain. It also covers how effectively stakeholders are able to interact together towards a common aim. Is the legal framework appropriate? Is the cost of business acting as a deterrent? What are the bottlenecks in the system creating delays and adding costs? Do investors currently feel that affordable housing is an opportunity with realistic long-term returns? No single action will resolve the affordable housing challenge, but rather a series of small progressive steps across the housing value chain, which together can help bring housing into the reach of a larger proportion of the population.

a. Harmonization of Government Roles

Clearly define roles of national and county governments. With devolution, county governments have been given the responsibilities and functions for delivering public services at the county level, including housing delivery. The central government still plays a role though the Ministry of Transport, Infrastructure, Housing and Urban Development in terms of overall policy formulation and, in turn, the counties are responsible for implementation. However, in practice, there is still insufficient clarity on who is responsible for what. There needs to be a clear definition of roles and responsibilities in order to advance this agenda. At the national level, there also needs to be better coordination and enhanced communication between the National Treasury and the Ministry of Transport, Infrastructure, Housing and Urban Development. There is some level of communication in the form of a working group, but the flow of information needs to be formalized and operationalized to eliminate information gaps and design effective policy interventions.

b. Institutional Integration

Repurpose NHC and NSSF to play more targeted roles in extending its reach down market. NHC could take on a role as a land development agency specialized in the purchase of land, its improvement, and its resale to developers or to end–users after sub-division in clearly titled individual plots. NHC has a comfortable equity base provided by the government (to which can be added the latent capital gains on its land banks), which is not put to use for low-income housing today as it should. NHC could issue infrastructure bonds to leverage its equity, a fairly successful instrument in Kenya, although probably little used for urban infrastructure. The conditions of a partnership with the cooperatives that buy tracks of land for their members could also be explored.

The NSSF disposes of long-term funds that can be used for long-term investments. Typically, the housing investments made by the NSSF have been accessible only to formal middle to high income earners; however, the NSSF's law amendment in 2013 opened the system to independent and informal workers. An increase of NSSF contribution is considered, and a small voluntary savings-for pension scheme targeting the informal sector was introduced in 2011. A recent move by the National Treasury to permit the NSSF to place a percentage of its assets in financial institutions for onward lending could also be a means of opening up mortgages to more low-income borrowers. NSSF members can borrow at more favorable terms and at less than market interest rates.

c. Legal and Regulatory Policies

Large scale investment in the upgrading of land registries. **There is an immediate need to** align their operations with the new land laws; re-issue validated titles replacing those that are not recognized under the latter; and to speed up the correction of invalid records that deeply affect the reliability and credibility of land registries today. There are also capacity constraints that need to be addressed, in terms of quantitative and qualitative staffing as well as administrative resources. The recording of large-scale development or subdivision face bottlenecks due to limited processing capacity of land administration. These upgrades need to be carried out alongside the digitization of records. The expectation is that the regained reliability of registries will at once eliminate an important component of the current transaction costs—the intervention of several lawyers conducting due diligence checks.

A smarter approach to the role of government is one of actively supporting the sector by creating the right environment for lenders and developers to thrive

d. Access to Serviced Land

Develop a PPP framework not just for housing but also for urban land and infrastructure that will set clear rules for the sharing of cost and profits between public and private entities. It could provide a tool for capturing part of the land value appreciation to contribute to the financing of infrastructure. Such a framework would be especially useful to guide the counties newly entrusted with land management responsibilities, and contribute to build their capacities in this area. It would help scale up an approach that, prior to this, has been experimental through limited sporadic projects.

Establish a clear and transparent pricing methodology for the land and allocation process. Given the history of corruption in allocation of public land, it is necessary to revamp the system and improve data and information availability particularly around land management and administration. Several policy initiatives are currently underway to address some of these issues, one of note is the National Land Information Management System (to be established both at the national and county level) that will provide access to a range of online services from land searches to online payment of fees/land rent.

Provide basic infrastructure and services on the land. When infrastructure (water, transport networks, power, sanitation etc.) is not developed in parallel with urban expansion and land allocation or conversion, this responsibility is transferred to developers which results in inefficient solutions and more costly options. Provision of urban infrastructure could also be addressed through PPP transactions or joint ventures driven by county governments.

Provide incentives for housing construction. This includes fast-tracking approvals for housing construction permits and possible waivers or reduction in fees and taxes associated with housing construction. For instance, it may be useful to offset the corporate tax when a developer has to provide the trunk infrastructure for new construction.

Each of these policy options directly affects the overall affordability measures, whether it is by reducing overall construction costs, by reducing the cost of end user financing, or by extending the term of end user financing to make it more affordable. The specific recommendations are by no means exhaustive and also do not necessarily need to be implemented together; however, they each touch on a different affordability challenge and could work in unison to bring down overall costs.

5.8 What Role can the Government Play?

5.8.1. Increasingly governments are recognizing their responsibilities with regards to providing shelter for their citizens, beyond just political campaign pledges. In the past, such pledges would have been to build an extraordinary number of houses in an unrealistically short space of time. Inevitably those campaign pledges rarely

succeeded. A smarter approach to the role of government is one of actively supporting the sector by creating the right environment for lenders and developers to thrive. Where needed and if fiscal space permits, government intervention can also help provide for social housing in cases where the cost of shelter is too much for individual households to bear.

5.8.2. **In looking at the government's role, the target of any housing policy should be to meet the country's present and future housing needs.** This can include a range of tenure types from full market based housing, to rental housing to social housing (rental or to own). A key consideration though is the sustainability of any proposal in terms of how government resources are allocated. There are numerous examples of misplaced government housing developments, failed government housing banks and ineffective housing subsidy mechanisms. Too often good intentions form government get subverted by poor execution. Housing development is notorious for lack of transparency, and as such needs to be done in a careful way.

5.8.3. **The key areas where government can help in creating the right environment are first and foremost on the macro economic framework.** For any form of long term finance, having low interest rates is the most effective way to ensure affordability. If interested rates are low it becomes much easier to extend lending for a longer period thereby significantly lowering the cost of housing. In Kenya, inflation currently stands at just 6.68 per cent which is a promising position to help bring rates down to single digits. It is only then that it makes sense to do loans for over 15 years which offer significantly lower monthly payment rates.

5.8.4. **A second area for government intervention is on the overall policy environment.** This can cover many things in the case of Kenya, but in particular the bottlenecks and costs for housing finance and housing supply. Providing access to land titles and a secure creditor rights framework for secured lending is the foundation of any mortgage system. Policies to facilitate provision of long term financing instruments, such as those highlighted above, can have significant leverage effects that expand lending. Other areas of policy are also critical around urban planning, provision of infrastructure, tax policy and housing subsidies.

5.8.5. **A third area for government intervention is to increase the efficiency of processes.** Accelerating mortgage registration and title transfers could have significant impact on the ability of developers to reach scale in affordable housing developments, and to better manage their capital and liquidity constraints.

5.8.6. **A fourth area where the government can support housing is to work with the private sector in attracting financing through catalytic financing instruments.** For example, housing guarantees can provide comfort to private sector lenders to reach out to borrowers

Providing access to land titles and a secure creditor rights framework for secured lending is the foundation of any mortgage system.

with informal incomes. MRC's require government capital upfront, but otherwise rely on private investors and financiers (including SACCOs) to raise capital and expand their pool of lenders.

5.8.7. **Subsidizing housing can be a very good way of sharing economic benefits across society, however it is important to have a careful design which targets right segments of the population and a subsidy which does not last for whole life of mortgage loan.** Because housing is a long term commitment it does also need some special subsidy design to take this into account. It is really the first few years of a loan where the fixed monthly payments can out a strain on a household's ability to pay. A subsidy should only be there where it is truly bridging an affordability gap. Typically, after a few years, household income will have risen and the fixed monthly payment will be much more manageable and not require a subsidy. This is a prime reason why interest rate subsidies with no time limit can prove very expensive for the state, and actually have very limited long term impacts.

5.8.8. **In considering its role, the Government of Kenya should balance its fiscal capacity with its ability to create meaningful change in the housing sector.** The best approach at present would seem to be to rely on markets to provide funding while role of government is limited to improving access to land, providing basic infrastructure and improving credit environment. Over time as the system grows and becomes more relevant to middle and lower income households, some form of subsidy could be considered, targeted at the most needy.

REFERENCES

Arkaja Singh, adapted from Case Study of Swarma Pragati Housing Microfinance in Rural Areas, November 2015.

Centre for Affordable Housing Finance in Africa: Yearbook 2016 (7th Edition), September 2016.

Central Bank of Kenya. Bank Supervision Annual Report 2015.

Constantinescu, C.; Matoo, A.; and Ruta, M. 2015. The Global Trade Slowdown: Cyclical or Structural? International Monetary Fund. Working Paper, WP/15/6.

East African Community (EAC). Trade Report 2014, 2013, 2008 and 2006. Arusha.

Hassler, O. 2011. Housing and Real Estate Finance in Middle East and North Africa Countries.

Kenya National Bureau of Statistics.2016. Economic Survey 2016. Nairobi.

Kenya National Housing Survey 2012/2013.

McKinsey Global Institute. A blueprint for addressing the global affordable housing challenge. October 2014.

National Treasury. Budget Summary for the Fiscal Year 2017/18 and the Supporting Information. Nairobi.

National Treasury. 2017. Medium Term Budget Policy Statement. November 2016. Nairobi.

National Treasury. Quarterly Budget and Economic Review, various issues. Nairobi.

Republic of Kenya. Kenya Meteorological Department. Review of Weather in January and the Outlook for February 2017. Ref. No. KMD/FCST/4-2017/MO/02.

Viruly (2012), Tibaijuka, Anne. 2009. Building Prosperity: Housing and Economic Development. UN HABITAT.

World Bank. 2016a. Kenya Urbanization Review.

World Bank. 2016b. Doing Business Report.

STATISTICAL TABLES

Table 1: Macroeconomic environment

	2009	2010	2011	2012	2013	2014	2015	2016e
GDP growth Rates (percent)	3.3	8.4	6.1	4.5	5.9	5.4	5.7	5.8
Agriculture	-2.3	10.1	2.4	2.8	5.4	4.3	5.5	4.0
Industry	3.7	8.7	7.2	4.2	5.3	6.5	6.9	5.7
Manufacturing	-1.1	4.5	7.2	-0.6	5.6	2.5	3.6	3.5
Services	6.2	7.3	6.1	4.7	5.4	5.8	5.5	5.3
Fiscal Framework (percent of GDP)/[1]								
Total revenue	19.4	19.4	18.8	19.2	19.2	19.1	18.8	20.4
Total expenditure	24.0	23.5	23.7	25.1	25.6	28.2	27.1	30.0
Grants	1.0	0.5	0.4	0.5	0.5	0.5	0.4	0.4
Budget deficit (including grants)	-5.8	-3.4	-4.5	-5.4	-5.9	-8.4	-7.5	-8.9
Total debt (net)	36.6	39.1	37.0	38.5	43.7	44.8	48.7	45.3
External Account (percent of GDP)								
Exports (fob)	12.2	13.1	13.9	12.3	10.6	10.1	9.4	9.1
Imports (cif)	25.6	28.7	33.8	30.8	29.2	28.6	24.5	21.5
Current account balance	-4.6	-5.9	-9.1	-8.3	-8.8	-9.8	-6.8	-6.0
Financial account	-10.2	-8.1	-8.2	-11.0	-9.4	-11.4	-8.0	-10.9
Capital account	0.7	0.6	0.6	0.5	0.3	0.4	0.4	0.4
Overall balance	-3.0	-0.4	2.1	-2.4	-0.7	-2.4	0.4	-0.2
Prices								
Inflation	10.5	4.1	14.0	9.6	5.7	6.9	6.6	6.3
Exchange rate (average Ksh/USD)	77.4	79.2	88.8	84.5	86.1	87.9	98.2	101.5

Source: Kenya National Bureau of Statistics, National Treasury and Central Bank of Kenya
End of FY in June (e.g 2009 = 2009/2010)
[1]/Figures for 2015 are actuals for 2015/16

Table 2: GDP growth rates for Kenya and EAC

	2010	2011	2012	2013	2014	2015	2016e
Kenya	8.4	6.1	4.5	5.9	5.4	5.7	5.8
Uganda	5.7	9.4	3.8	3.6	5.2	5.1	4.6
Tanzania	6.4	7.9	5.1	7.3	7.0	7.0	7.4
Rwanda	7.3	7.9	8.8	4.7	7.0	6.9	6.3
Average	6.9	7.8	5.6	5.3	6.1	6.2	6.1

Source: World Bank
Note: e(estimate); f(forecast)

Table 3: Kenya Annual GDP

Years	GDP, current prices	GDP, 2009 constant prices	GDP/capita, current prices	GDP growth
	Ksh Billions	**Ksh Billions**	**US$**	**Percent**
2007	2151	2766	858	6.9
2008	2483	2772	939	0.2
2009	2864	2864	943	3.3
2010	3169	3104	992	8.4
2011	3726	3294	1013	6.1
2012	4261	3444	1185	4.5
2013	4745	3647	1261	5.9
2014	5402	3842	1368	5.4
2015	6235	4062	1377	5.7
2016	7159	4299		5.8

Source: Kenya National Bureau of Statistics and World Development Indicators
Note: 2016 is an estimate

Table 4: Sectoral contribution to GDP growth (Quarterly, Percent)

Year	Quarterly	Agriculture	Industry	Services	GDP
2012	Q1	0.8	0.7	2.6	4.1
	Q2	0.5	1.2	2.5	4.2
	Q3	0.6	2.3	2.3	5.2
	Q4	0.8	1.0	2.9	4.7
2013	Q1	1.4	2.6	2.0	6.0
	Q2	1.7	2.1	3.7	7.5
	Q3	1.1	1.7	3.7	6.5
	Q4	0.7	0.1	2.8	3.5
2014	Q1	1.1	1.7	2.4	5.2
	Q2	1.1	2.2	2.8	6.0
	Q3	1.4	1.1	2.1	4.6
	Q4	0.4	1.7	3.5	5.5
2015	Q1	2.1	1.6	2.0	5.7
	Q2	1.1	1.7	2.7	5.5
	Q3	0.8	2.3	2.8	5.9
	Q4	0.7	1.8	3.3	5.8
2016	Q1	1.5	1.2	3.3	6.0
	Q2	1.0	1.5	3.4	5.9
	Q3	0.6	1.5	3.5	5.7
	Q4	0.4	1.5	4.0	5.8

Source: World Bank, based on data from Kenya National Bureau of Statistics
Note: Agriculture = Agriculture, forestry and fishing
Industry = Mining and quarrying + Manufacturing + Electricity and water supply + Construction
Services = Whole sale and retail trade + Accommodation and restaurant + Transport and storage + Information and communication + Financial and insurance + Public administration + Proffessional administration and support services +Real estate +Education + Health + Other services + FISIM + Taxes on products

Table 5: Contribution by broad sub-sectors (Quarterly, percent)

	Quarterly	Agriculture contribution to GDP	Industry by sub sector contribution				Industries	Service by sub sector contribution						Services
			Mining and quarrying	Manufacturing	Electricity and water supply	Construction		Accomodation and restaurant	Transport and storage	Real estate	Information and communication	Financial and insurance	Other	
2012	Q1	0.8	0.1	-0.1	0.2	0.7	0.9	0.2	0.5	0.4	0.4	0.0	1.0	2.4
	Q2	0.5	0.2	-0.2	0.1	0.3	0.4	0.0	0.5	0.3	-0.2	0.3	2.3	3.3
	Q3	0.6	0.2	0.1	0.2	0.5	1.0	0.0	-0.1	0.3	-0.4	0.4	3.5	3.6
	Q4	0.8	0.2	0.0	0.2	0.4	0.9	0.1	-0.1	0.3	0.5	0.6	1.6	3.0
2013	Q1	1.4	0.2	1.0	0.1	0.4	1.7	-0.5	-0.6	0.3	0.4	0.6	2.7	3.0
	Q2	1.7	-0.2	0.8	0.2	0.4	1.3	0.0	0.1	0.3	0.3	0.6	3.3	4.5
	Q3	1.1	0.0	0.6	0.2	0.4	1.2	0.2	0.2	0.4	0.4	0.4	2.6	4.1
	Q4	0.7	-0.1	0.1	0.1	-0.1	-0.1	0.0	0.7	0.4	0.5	0.3	1.1	3.0
2014	Q1	1.1	0.1	0.5	0.1	0.3	1.1	-0.3	0.2	0.4	0.4	0.4	2.0	3.1
	Q2	1.1	0.2	0.8	0.1	0.7	1.8	-0.3	0.4	0.4	0.3	0.4	1.9	3.1
	Q3	1.4	0.0	0.1	0.2	0.4	0.7	-0.4	0.6	0.5	0.6	0.5	0.8	2.6
	Q4	0.4	0.2	-0.3	0.2	0.9	1.0	0.0	0.3	0.4	0.7	0.6	2.0	4.2
2015	Q1	2.1	0.1	0.3	0.2	0.6	1.2	-0.1	0.4	0.5	0.3	0.6	0.8	2.4
	Q2	1.1	0.1	0.3	0.3	0.6	1.3	0.0	0.6	0.5	0.2	0.5	1.2	3.0
	Q3	0.8	0.2	0.5	0.2	0.8	1.7	0.0	0.7	0.6	0.2	0.7	1.1	3.4
	Q4	0.7	0.1	0.4	0.1	0.7	1.3	0.1	0.4	0.7	0.3	0.5	1.7	3.7
2016	Q1	1.5	0.1	0.2	0.2	0.5	0.9	0.1	0.6	0.8	0.4	0.5	1.2	3.6
	Q2	1.0	0.1	0.6	0.2	0.4	1.3	0.1	0.6	0.8	0.3	0.5	1.3	3.5
	Q3	0.6	0.1	0.5	0.1	0.4	1.1	0.1	0.7	0.7	0.3	0.5	1.6	3.9
	Q4	0.4	0.1	0.3	0.1	0.6	1.1	0.2	0.5	0.6	0.5	0.3	2.3	4.3

Source: World Bank, based on data from Kenya National Bureau of Statistics
Note: Other = Whole sale and retail trade + Public administration + Proffessional, administration and support services + Education + Health + Other services + FISIM + Taxes on products

Table 6: Quarterly growth rates (percent)

Year	Quarter	Agriculture			Industry			Services			GDP		
		Quarter-on-Quarter	Year-on-Year	Four Quarter Moving Average	Quarter-on-Quarter	Year-on-Year	Four Quarter Moving Average	Quarter-on-Quarter	Year-on-Year	Four Quarter Moving Average	Quarter-on-Quarter	Year-on-Year	Four Quarter Moving Average
2012	1	48.9	3.5	2.6	-4.6	5.8	6.7	-1.0	4.4	5.2	7.5	4.7	5.4
	2	-10.6	2.1	2.3	-1.2	2.0	4.6	-1.3	5.3	5.2	-3.5	4.3	4.8
	3	-22.7	2.0	1.9	3.8	4.6	4.7	5.2	4.5	4.8	-1.5	4.5	4.5
	4	1.3	4.1	2.9	6.7	4.4	4.2	1.9	4.8	4.7	2.5	4.7	4.6
2013	1	52.2	6.5	3.9	-0.2	9.3	5.1	-2.4	3.3	4.4	8.6	5.8	4.9
	2	-10.4	6.8	5.1	-4.2	6.0	6.0	2.8	7.7	5.1	-1.9	7.0	5.7
	3	-22.9	6.6	6.1	4.6	6.8	6.6	2.4	4.8	5.1	-2.6	6.3	6.1
	4	-3.9	1.1	5.4	-0.4	-0.3	5.3	2.7	5.6	5.4	-0.6	3.1	5.7
2014	1	53.8	2.2	4.1	6.7	6.5	4.7	-2.8	5.2	5.8	10.3	4.7	5.4
	2	-10.4	2.1	2.8	-0.6	10.5	5.8	4.0	6.4	5.5	-0.8	5.9	5.0
	3	-19.3	6.8	2.9	-1.6	4.0	5.1	1.4	5.3	5.6	-3.3	5.2	4.8
	4	-6.6	3.8	3.5	0.6	5.0	6.5	3.5	6.1	5.8	-0.3	5.5	5.3
2015	1	52.5	2.9	3.7	8.2	6.6	6.5	-2.9	6.0	6.0	9.7	5.0	5.4
	2	-9.5	4.0	4.2	0.2	7.4	5.8	4.2	6.3	6.0	0.1	5.9	5.4
	3	-18.2	5.5	4.0	-1.1	7.9	6.7	1.7	6.6	6.3	-3.2	6.0	5.6
	4	-1.0	11.8	5.6	-1.4	5.7	6.9	0.3	3.3	5.5	-0.6	5.7	5.6
2016	1	43.3	5.1	6.3	8.3	5.7	6.7	0.5	6.9	5.7	10.0	5.9	5.9
	2	-9.1	5.5	6.6	0.3	5.9	6.3	4.2	6.9	5.9	0.3	6.2	6.0
	3	-19.4	3.9	6.3	-1.9	5.1	5.6	1.6	6.8	6.0	-3.6	5.7	5.9

Source: World Bank, based on data from Kenya National Bureau of Statistics

Table 7: Leading Economic Indicators year-to-date growth rates (Percent)

Year	Month	Horticulture	Coffee	Tea
2014	January	0.5	13.6	-0.9
	February	-4.6	-7.4	-6.1
	March	-4.7	9.1	-4.4
	April	-2.6	12.8	-2.2
	May	0.7	6.3	-0.9
	June	3.3	2.3	-0.2
	July	4.5	4.6	1.6
	August	5.0	-0.3	1.6
	September	5.0	-2.5	1.6
	October	4.1	-2.9	1.7
	November	3.4	-2.9	2.4
	December	3.0	-3.0	2.9
2015	January	-1.8	-10.3	-7.4
	February	1.7	-8.3	-16.3
	March	5.4	-7.5	-27.2
	April	5.0	-11.0	-30.6
	May	3.3	-9.5	-26.0
	June	1.6	-9.3	-22.2
	July	1.6	-12.5	-19.4
	August	1.2	-9.3	-17.0
	September	5.1	-9.7	-14.2
	October	5.9	-7.0	-13.6
	November	6.6	-8.5	-11.8
	December	8.1	-8.1	-10.3
2016	January	10.9	-13.9	20.8
	February	9.6	0.0	43.0
	March	11.3	-1.2	71.1
	April	13.9	5.3	68.0
	May	2.9	6.3	49.5
	June	5.2	8.5	42.3
	July	5.0	7.5	35.1
	August	6.8	5.6	31.3
	September	3.4	4.3	27.2
	October	3.6	0.5	23.6
	November	4.8	3.3	20.8
	December	0.7	3.9	18.0

Source: World Bank, based on data from Kenya National Bureau of Statistics

Table 8: Inflation

Year	Month	Overall Inflation	Food Inflation	Energy Inflation	Core Inflation
2014	January	7.2	10.1	5.5	5.4
	February	6.9	9.1	5.6	5.5
	March	6.3	8.3	4.7	5.4
	April	6.4	8.1	5.9	5.3
	May	7.3	8.9	8.1	5.6
	June	7.4	8.4	9.0	5.6
	July	7.7	9.1	9.1	5.5
	August	8.4	10.9	8.6	5.6
	September	6.6	8.4	7.2	4.4
	October	6.4	8.2	7.0	4.4
	November	6.1	7.5	6.4	4.6
	December	6.0	7.7	6.0	4.5
2015	January	5.5	7.7	4.5	4.1
	February	5.6	8.7	3.3	4.1
	March	6.3	11.0	2.9	3.9
	April	7.1	13.4	1.5	4.0
	May	6.9	13.2	0.3	4.2
	June	7.0	13.4	0.2	4.4
	July	6.6	12.1	0.6	4.4
	August	5.8	9.9	1.1	4.3
	September	6.0	9.8	1.5	4.4
	October	6.7	11.3	2.0	4.4
	November	7.3	12.7	2.3	4.2
	December	8.0	13.3	2.9	5.1
2016	January	7.8	12.7	2.9	5.4
	February	7.1	10.8	1.7	5.4
	March	6.5	9.4	2.1	5.4
	April	5.3	6.8	2.0	5.2
	May	5.0	6.6	1.8	4.7
	June	5.8	8.9	1.4	4.5
	July	6.4	10.8	0.9	4.4
	August	6.3	10.9	0.1	4.6
	September	6.3	10.9	0.2	4.6
	October	6.5	11.0	0.1	4.6
	November	6.7	11.1	0.6	4.7
	December	6.4	11.2	0.1	3.8
2017	January	7.0	12.5	0.7	3.3
	February	9.0	16.5	3.0	3.3
	March	10.3	18.6	3.3	3.3

Source: World Bank, based on data from Kenya National Bureau of Statistics

Table 9: Tea production and exports

Year	Month	Production MT	Price Ksh/Kg	Exports MT	Exports value Ksh million
2014	January	44,970	236	38,652	8,784
	February	33,774	203	33,514	7,317
	March	33,336	187	37,642	7,938
	April	39,975	188	37,439	7,782
	May	41,186	179	36,216	7,380
	June	31,945	178	39,011	7,692
	July	30,790	200	42,393	8,468
	August	26,756	191	38,121	7,974
	September	33,321	178	35,961	7,244
	October	45,368	180	37,637	7,444
	November	38,614	182	38,275	7,595
	December	45,071	182	41,631	8,379
2015	January	41,653	212	40,970	8,485
	February	24,276	221	41,086	9,313
	March	15,688	250	35,700	8,796
	April	23,837	258	28,262	7,189
	May	37,523	297	27,016	7,506
	June	32,286	319	35,915	11,263
	July	30,942	344	30,623	10,146
	August	28,410	330	27,687	9,481
	September	36,484	327	33,528	11,413
	October	41,343	333	40,246	13,538
	November	40,382	313	36,714	12,126
	December	46,387	309	42,779	13,768
2016	January	50308	279	36575	11013
	February	43969	253	43287	12199
	March	45330	234	37571	9887
	April	37571	214	39313	9517
	May	36573	223	44901	10658
	June	35603	243	52175	12613
	July	29285	246	42751	10679
	August	29462	234	39673	9993
	September	36785	236	33528	8454
	October	41342	243	29656	7548
	November	39903	273	41138	11123
	December	45103	273	39396	10811

Source: World Bank, based on data from Kenya National Bureau of Statistics

Table 10: Coffee production and exports

Year	Month	Production MT	Price Ksh/Kg	Exports MT	Exports value Ksh million
2014	January	2,850	293	3,169	1,055
	February	5,382	399	3,078	1,118
	March	6,212	459	4,584	1,533
	April	6,611	393	4,858	2,013
	May	3,747	349	4,594	2,024
	June	2,860	358	4,587	2,007
	July	1,292	315	5,425	2,383
	August	3,214	381	3,313	1,474
	September	3,424	404	3,944	1,722
	October	2,801	423	3,618	1,645
	November	1,703	410	3,718	1,747
	December	2,354	414	2,551	1,192
2015	January	2,795	412	2,844	1,307
	February	4,837	489	2,884	1,339
	March	5,571	378	4,290	2,025
	April	3,714	310	3,948	1,901
	May	2,969	289	4,383	2,236
	June	0	0	4,220	2,068
	July	2,086	339	3,938	1,943
	August	3,286	371	3,991	1,790
	September	2,643	364	3,405	1,617
	October	1,768	320	4,400	2,019
	November	1,268	337	2,769	1,244
	December	1,282	435	2,528	1,092
2016	January	3,432	462	2,449	1,184
	February	5,220	486	3,277	1,636
	March	6,835	437	4,169	2,206
	April	4,513	340	4,804	2,540
	May	4,731	263	4,814	2,170
	June	1,747	268	4,983	2,369
	July	568	324	3,987	1,798
	August	3,723	431	3,719	1,637
	September	3,284	437	3,173	1,399
	October	1,573	410	3,116	1,489
	November	2,374	468	3,929	1,691
	December	1,666	514	2,886	1,252

Source: Kenya National Bureau of Statistics

Table 11: Horticulture exports

Year	Month	Exports MT	Exports value Ksh. million
2014	January	18,494	8,376
	February	19,640	7,729
	March	18,834	9,741
	April	20,569	6,636
	May	19,858	7,533
	June	18,237	6,536
	July	17,114	6,138
	August	16,459	5,203
	September	18,488	5,479
	October	19,638	7,380
	November	17,089	7,815
	December	15,825	5,517
2015	January	18,170	6,413
	February	20,599	7,892
	March	21,259	10,510
	April	21,410	6,223
	May	19,160	6,300
	June	16,904	5,140
	July	17,359	8,551
	August	16,175	5,824
	September	25,188	8,187
	October	22,179	9,905
	November	19,428	8,095
	December	20,179	7,399
2016	January	20,160	10,927
	February	22,335	10,151
	March	24,313	11,139
	April	25,931	8,611
	May	10,783	7,004
	June	20,157	10,293
	July	17,981	5,577
	August	19,650	7,293
	September	20,924	6,659
	October	23,327	8,312
	November	22,772	7,641
	December	11,294	7,906

Source: Kenya National Bureau of Statistics

Table 12: Local electricity generation by source

Year	Month	Hydro KWh million	Geo-thermal KWh million	Thermal KWh million	Total KWh million
2014	January	339	179	226	747
	February	270	145	257	674
	March	287	171	279	737
	April	308	170	240	717
	May	250	191	296	737
	June	263	221	246	730
	July	254	258	252	763
	August	294	247	224	765
	September	278	293	164	735
	October	279	339	157	775
	November	307	322	122	751
	December	282	382	94	758
2015	January	278	388	109	776
	February	230	352	121	703
	March	246	377	134	757
	April	264	359	121	744
	May	301	380	103	784
	June	297	362	109	769
	July	305	353	143	801
	August	319	378	112	808
	September	306	389	99	794
	October	310	402	100	812
	November	300	393	89	782
	December	307	387	92	786
2016	January	322	392	93	808
	February	297	392	95	784
	March	335	383	112	830
	April	303	394	102	800
	May	334	403	92	830
	June	348	342	113	803
	July	337	393	110	840
	August	364	345	138	846
	September	349	335	137	821
	October	357	364	135	856
	November	315	369	158	842
	December	299	371	158	828
2017	January	252	380	197	830

Source: Kenya National Bureau of Statistics

Table 13: Soft drinks, sugar, galvanized sheets and cement production

Year	Month	Soft drinks Litres (thousands)	Sugar MT	Galvanized sheets MT	Cement MT
2014	January	39,007	64,298	22,090	454,960
	February	39,146	60,044	18,573	442,636
	March	40,320	63,365	21,267	478,416
	April	37,885	47,279	25,989	468,022
	May	40,430	44,094	27,433	464,695
	June	28,706	42,866	24,465	464,929
	July	33,790	55,912	21,779	503,428
	August	33,404	50,140	25,753	492,801
	September	35,899	47,915	26,126	499,479
	October	41,601	42,197	26,732	553,186
	November	40,134	34,455	25,763	545,041
	December	49,142	64,298	18,539	492,944
2015	January	41,348	63,227	21,304	511,298
	February	41,440	57,917	20,078	465,471
	March	48,865	63,389	22,797	550,556
	April	42,148	46,280	20,674	537,452
	May	36,874	44,081	23,132	516,513
	June	36,274	46,098	20,358	516,185
	July	32,086	47,957	18,415	570,904
	August	38,432	54,089	20,871	553,929
	September	40,176	61,069	20,581	561,235
	October	42,936	56,360	26,024	557,589
	November	40,025	43,401	25764	510,747
	December	49,966	48,089	16,938	486,306
2016	January	50,502	64,499	21,330	533,490
	February	45,237	59,863	20,102	531,813
	March	58,038	65,708	20,120	541,438
	April	44,429	48,802	23,109	568,253
	May	43,189	45,156	21,980	585,929
	June	39,191	53,797	20,180	547,238
	July	42,393	56,948	18,320	575,193
	August	39,331	52,232	24,190	591,612
	September	48,884	44,686	21,045	528,494
	October	46,131	48,929	18,328	573,034
	November	41,877	51,298	23,099	584,780
	December	52,185	46,422		558,112

Source: Kenya National Bureau of Statistics

Table 14: Tourism arrivals

Year	Month	JKIA	MIA	TOTAL
2014	January	75,906	19,853	95,759
	February	50,270	18,334	68,604
	March	76,561	15,041	91,602
	April	59,357	7,293	66,650
	May	54,334	3,967	58,301
	June	42,549	4,758	47,307
	July	78,902	7,764	86,666
	August	82,465	10,962	93,427
	September	53,743	6,778	60,521
	October	52,606	6,323	58,929
	November	51,480	7,153	58,633
	December	65,427	9,570	74,997
2015	January	40,846	10,107	50,952
	February	45,141	7,882	53,053
	March	66,121	6,958	73,079
	April	49,933	4,020	53,953
	May	50,764	2,511	53,275
	June	59,867	3,218	63,146
	July	72,515	5,728	78,243
	August	63,332	7,546	70,878
	September	54,162	5,114	59,276
	October	66,441	6,049	72,490
	November	53,622	7,718	61,340
	December	50,015	9,070	59,085
2016	January	65,431	9,407	74,838
	February	62,856	9,983	72,839
	March	49,996	8,551	58,547
	April	51,311	3869	55,180
	May	59,294	3,578	62,872
	June	64,451	4,182	68,633
	July	81,729	7,832	89,561
	August	87,141	9,817	96,958
	September	67,249	8,381	75,630
	October	63,229	9,015	72,244
	November	61,224	7,990	69,214
	December	67,602	10,267	77,869

Source: Kenya National Bureau of Statistics

Table 15: New vehicle registration

Year	Month	All body types (numbers)
2014	January	15,411
	February	17,779
	March	15,629
	April	12,789
	May	14,109
	June	14,011
	July	16,490
	August	32,401
	September	24,390
	October	17,214
	November	17,226
	December	20,608
2015	January	15,366
	February	17,409
	March	25,067
	April	20,730
	May	22,837
	June	25,070
	July	21,132
	August	17,360
	September	18,596
	October	18,740
	November	23,209
	December	22,308
2016	January	14,690
	February	12,771
	March	10,280
	April	13,699
	May	11,855
	June	22,428
	July	23,442
	August	18,288
	September	18,527
	October	13,018
	November	27,286
	December	27,431

Source: Kenya National Bureau of Statistics

Table 16: Exchange rate

Year	Month	USD	UK Pound	Euro
2014	January	86.2	142.0	117.5
	February	86.3	142.8	117.8
	March	86.5	143.8	119.6
	April	86.7	145.1	119.8
	May	87.4	147.3	120.1
	June	87.6	148.1	119.2
	July	87.8	150.0	119.0
	August	88.1	147.2	117.4
	September	88.8	145.0	114.7
	October	89.2	143.7	113.2
	November	90.0	142.0	112.3
	December	90.4	141.5	111.5
2015	January	91.4	138.5	106.3
	February	91.5	140.2	103.9
	March	91.7	137.5	99.4
	April	93.4	139.6	100.7
	May	96.4	149.1	107.5
	June	97.7	152.2	109.7
	July	101.2	157.5	111.4
	August	102.4	159.8	114.1
	September	105.3	161.5	118.2
	October	102.8	157.5	115.4
	November	102.2	155.4	109.8
	December	102.2	153.3	111.1
2016	January	102.3	147.5	111.1
	February	101.9	145.9	113.0
	March	101.5	144.2	112.6
	April	101.2	144.8	114.8
	May	100.7	146.3	114.0
	June	101.1	144.3	113.7
	July	101.3	133.4	112.1
	August	101.4	132.9	113.7
	September	101.3	133.2	113.5
	October	101.3	125.4	111.9
	November	101.7	126.3	110.0
	December	102.1	127.7	107.7
2017	January	103.7	128.0	110.2
	February	103.6	129.5	130.4

Source: Central Bank of Kenya

Table 17: Interest rates

Year	Month	Short-term			Long-term			
		Interbank	91-Treasury Bill	Central Bank Rate	Average deposit rate	Savings	Overall weighted lending rate	Interest rate spread
2014	January	10.6	9.3	8.5	6.6	1.6	17.0	10.5
	February	9.1	9.2	8.5	6.6	1.5	17.1	10.5
	March	6.6	9.0	8.5	6.6	1.6	16.9	10.3
	April	7.6	8.8	8.5	6.5	1.5	16.7	10.2
	May	7.8	8.8	8.5	6.4	1.5	17.0	10.6
	June	6.9	9.8	8.5	6.6	1.5	16.4	9.8
	July	8.0	9.8	8.5	6.6	1.3	16.9	10.3
	August	11.7	8.3	8.5	6.5	1.5	16.3	9.8
	September	7.4	8.4	8.5	6.6	1.5	16.0	9.4
	October	6.8	8.7	8.5	6.6	1.6	16.0	9.4
	November	6.9	8.6	8.5	6.7	1.5	15.9	9.2
	December	6.9	8.6	8.5	6.8	1.9	16.0	9.2
2015	January	7.2	8.6	8.5	6.7	1.6	15.9	9.3
	February	6.9	8.6	8.5	6.7	1.5	15.5	8.8
	March	6.8	8.5	8.5	6.6	1.5	15.5	8.8
	April	8.9	8.4	8.5	6.6	1.9	15.4	8.8
	May	11.1	8.3	8.5	6.6	1.5	15.3	8.7
	June	11.9	8.3	10.0	6.6	1.9	16.1	9.4
	July	13.4	10.6	11.5	6.3	1.4	15.8	9.4
	August	18.6	11.5	11.5	6.9	1.5	15.7	8.8
	September	21.3	14.0	11.5	7.3	1.7	16.8	9.5
	October	15.3	21.0	11.5	7.5	1.7	16.6	9.0
	November	8.9	12.3	11.5	7.4	1.3	17.2	9.8
	December	5.3	9.7	11.5	8.0	1.6	18.3	10.3
2016	January	6.4	11.2	11.5	7.6	1.6	18.0	10.4
	February	4.5	10.6	11.5	7.5	1.4	17.9	10.4
	March	4.0	8.7	11.5	7.2	1.4	17.9	10.7
	April	3.9	8.9	11.5	6.9	1.5	18.0	11.2
	May	3.6	8.2	10.5	6.4	1.6	18.2	11.8
	June	4.9	7.3	10.5	6.8	1.6	18.2	11.4
	July	5.5	7.4	10.5	6.6	1.7	18.1	11.5
	August	5.0	8.5	10.0	6.4	1.7	17.7	11.2
	September	4.9	8.1	10.0	6.9	3.8	13.9	6.9
	October	4.1	7.8	10.0	7.8	6.1	13.7	5.8
	November	5.1	8.2	10.0	7.7	6.1	14.3	6.7
	December	5.9	8.4	10.0	7.3	6.4	13.7	6.4

Source: Central Bank of Kenya

Table 18: Money aggregate

Year	Growth rates (yoy)	Money supply, M1	Money supply, M2	Money supply, M3	Reserve money
2014	January	19.9	16.7	17.1	10.3
	February	20.3	17.8	16.2	9.9
	March	20.4	19.0	17.3	7.7
	April	16.9	16.1	16.6	17.7
	May	19.9	18.4	17.8	11.9
	June	21.3	18.8	18.2	12.6
	July	18.9	18.8	19.3	7.3
	August	21.0	20.0	21.8	15.2
	September	12.6	17.1	19.4	11.2
	October	12.9	18.4	18.9	13.5
	November	13.5	17.8	17.5	9.3
	December	13.2	18.6	16.7	18.5
2015	January	11.4	17.0	16.0	15.8
	February	10.0	17.2	18.6	11.5
	March	11.9	16.4	16.4	11.8
	April	13.4	17.2	17.3	12.0
	May	10.0	14.8	16.5	15.0
	June	9.6	16.4	18.6	14.9
	July	13.0	16.0	16.4	25.8
	August	10.5	14.3	14.0	2.9
	September	8.5	12.7	13.5	16.7
	October	10.8	13.6	13.6	24.5
	November	7.9	11.6	13.0	13.0
	December	8.5	12.4	13.7	3.3
2016	January	11.6	11.0	11.3	9.1
	February	10.7	10.2	9.5	9.2
	March	10.9	10.5	11.0	16.1
	April	10.0	8.1	7.9	9.0
	May	12.4	9.5	8.3	7.6
	June	13.0	8.9	7.9	4.9
	July	8.9	7.2	6.4	4.3
	August	9.6	6.6	6.6	6.8
	September	26.2	8.8	8.1	4.3
	October	25.4	7.2	7.1	-7.4
	November	26.7	6.9	6.7	0.5
	December	28.9	5.2	3.9	4.8

Source: Central Bank of Kenya

Table 19: Mobile payments

Year	Month	Number of Agents	Number of customers (Millions)	Number of transactions (Millions)	Value of transactions (Billions)
2014	January	114,107	25.8	67.1	178.5
	February	115,015	26.1	65.6	172.8
	March	116,196	26.2	74.0	192.7
	April	116,581	26.1	72.1	186.7
	May	117,807	25.8	74.5	198.1
	June	120,781	25.9	74.0	189.9
	July	122,462	26.2	77.5	201.0
	August	124,708	26.3	78.9	206.7
	September	124,179	26.3	78.2	206.3
	October	128,706	26.0	82.9	210.3
	November	121,419	24.9	81.0	203.2
	December	123,703	25.2	85.6	225.5
2015	January	125,826	25.4	81.7	210.5
	February	127,187	25.5	80.7	208.1
	March	128,591	25.7	90.3	231.8
	April	129,218	26.1	84.9	213.7
	May	129,735	26.5	89.9	230.2
	June	131,761	26.5	90.7	227.9
	July	133,989	26.7	94.0	238.9
	August	136,042	27.0	94.1	248.2
	September	138,131	27.3	96.3	247.5
	October	140,612	27.5	102.8	255.8
	November	142,386	28.1	101.3	236.4
	December	143,946	28.6	107.4	267.1
2016	January	146,710	29.1	108.1	243.4
	February	148,982	29.5	114.1	257.2
	March	150,987	30.7	121.7	273.6
	April	153,762	31.4	120.2	269.8
	May	156,349	31.3	122.6	277.9
	June	162,465	31.4	121.8	271.0
	July	167,072	32.3	127.0	281.9
	August	173,774	32.8	131.5	296.9
	September	173,731	33.4	130.7	283.9
	October	181,456	34.0	141.4	292.1
	November	162,441	34.3	140.8	291.2
	December	165,908	35.0	146.2	316.8

Source: Central Bank of Kenya

Table 20: Nairobi Securities Exchange (NSE20 Share Index)

Year	Month	NSE 20 Share Index
2014	January	4,856
	February	4,933
	March	4,946
	April	4,949
	May	4,882
	June	4,885
	July	4,906
	August	5,139
	September	5,256
	October	5,195
	November	5,156
	December	5,113
2015	January	5,212
	February	5,491
	March	5,248
	April	5,091
	May	4,787
	June	4,906
	July	4,405
	August	4,177
	September	4,174
	October	3,869
	November	4,016
	December	4,041
2016	January	3,773
	February	3,862
	March	3,982
	April	4,009
	May	3,828
	June	3,641
	July	3,489
	August	3,179
	September	3,243
	October	3,229
	November	3,247
	December	3,186
2017	January	2,794
	February	2,995

Source: Financial Times

Table 21: Central Bank Rate and Treasury Bills

Year	Month	Central Bank Rate	91-Treasury Bill	182-Treasury Bill	364-Treasury Bill
2014	January	8.5	9.3	10.4	10.6
	February	8.5	9.2	10.4	10.7
	March	8.5	9.0	10.3	10.5
	April	8.5	8.8	10.1	10.2
	May	8.5	8.8	9.9	10.1
	June	8.5	9.8	10.1	10.5
	July	8.5	9.8	10.4	11.0
	August	8.5	8.3	10.0	10.3
	September	8.5	8.4	9.4	10.3
	October	8.5	8.7	8.8	10.3
	November	8.5	8.6	8.9	10.2
	December	8.5	8.6	9.2	10.4
2015	January	8.5	8.6	9.6	12.1
	February	8.5	8.6	10.0	11.0
	March	8.5	8.5	10.3	10.7
	April	8.5	8.4	10.3	10.6
	May	8.5	8.3	10.3	10.7
	June	10	8.3	10.4	11.0
	July	11.5	10.6	11.0	11.6
	August	11.5	11.5	11.5	13.3
	September	11.5	14.0	12.5	15.2
	October	11.5	21.0	15.7	21.5
	November	11.5	12.3	16.3	15.2
	December	11.5	9.7	15.7	12.5
2016	January	11.5	11.2	13.0	14.1
	February	11.5	10.6	12.8	13.7
	March	11.5	8.7	12.6	12.3
	April	11.5	8.9	11.7	11.8
	May	10.5	8.2	10.7	11.6
	June	10.5	7.3	10.2	10.8
	July	10.5	7.4	9.9	10.9
	August	10.0	8.5	10.8	11.7
	September	10.0	8.1	10.8	11.0
	October	10.0	7.8	10.3	10.4
	November	10.0	8.2	10.3	10.8
	December	10.0	8.4	10.5	10.6
2017	January	10.0	11.0	10.5	11.0

Source: Central Bank of Kenya

Table 22: Nominal & Real Effective and USD Exchange Rates (Index January 2016 = 100)

Year	Month	NEER	REER	USD
2014	January	92.3	103.9	84.3
	February	92.3	103.8	84.3
	March	92.8	104.6	84.5
	April	93.1	104.4	84.8
	May	93.9	104.5	85.4
	June	93.8	104.4	85.6
	July	94.0	104.3	85.8
	August	93.8	103.2	86.1
	September	93.7	102.9	86.8
	October	93.5	103.2	87.2
	November	93.5	102.9	87.9
	December	93.3	101.7	88.4
2015	January	93.0	99.6	89.3
	February	92.7	99.2	89.4
	March	91.8	97.8	89.7
	April	93.4	99.2	91.3
	May	97.0	101.3	94.2
	June	98.1	102.4	95.5
	July	101.2	105.7	98.9
	August	102.1	106.2	100.1
	September	104.8	108.3	102.9
	October	102.4	105.8	100.5
	November	100.7	103.4	99.9
	December	100.5	101.9	99.9
2016	January	100.0	100.0	100.0
	February	100.1	100.5	99.6
	March	100.0	100.3	99.2
	April	100.6	100.7	98.9
	May	99.9	99.7	98.5
	June	100.2	99.5	98.9
	July	99.7	98.5	99.0
	August	100.3	99.1	99.1
	September	100.3	99.8	99.0
	October	99.3	98.9	99.0
	November	99.0	98.6	99.4
	December	98.5	98.8	99.8
2017	January	100.2	100.1	101.4

Source: World Bank, based on data from Central Bank of Kenya

Table 23: National Fiscal Position

Actual (percent of GDP)	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16 *	2016/17
Revenue and Grants	19.7	18.9	20.6	19.8	19.2	19.8	19.7	19.6	19.2	20.9
Total Revenue	18.6	18.2	19.6	19.3	18.8	19.3	19.2	19.1	18.8	20.4
Tax revenue	15.7	15.6	16.0	16.1	15.5	15.6	16.8	16.6	16.3	17.1
Income tax	6.8	6.9	7.2	7.5	7.8	8.3	8.9	8.8	8.6	8.9
VAT	4.8	4.7	4.9	5.0	4.4	4.1	4.6	4.5	4.4	4.6
Import Duty	1.4	1.4	1.4	1.3	1.3	1.3	1.3	1.3	1.2	1.2
Excise Duty	2.7	2.6	2.5	2.3	2.0	1.9	2.0	2.0	2.1	2.4
Other Revenues	1.4	1.4	2.0	1.5	1.6	1.7	1.3	1.2	1.3	1.4
Railway Levy	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.3	0.3	0.3
Appropriation in Aid	1.5	1.2	1.6	1.7	1.7	2.0	1.1	1.0	0.9	1.7
Grants	1.1	0.7	1.0	0.5	0.4	0.5	0.5	0.5	0.4	0.4
Expenditure and Net Lending	23.1	22.3	24.0	23.5	23.7	25.1	25.6	28.2	27.1	30.0
Recurrent	17.4	16.3	16.9	17.2	16.3	18.1	15.5	15.4	15.6	16.0
Wages and salaries	6.3	5.8	5.7	5.8	5.5	6.1	5.5	5.1	4.7	4.9
Interest Payments	2.1	1.9	2.1	2.2	2.1	2.7	2.7	3.0	3.3	3.1
Other recurrent	9.0	8.6	9.1	9.2	8.7	9.3	7.3	7.3	7.6	8.0
Development and net lending	5.7	6.0	7.1	6.4	7.4	6.8	6.3	8.8	7.4	9.8
County allocation	0.0	0.0	0.0	0.0	0.0	0.2	3.8	3.9	4.0	3.8
Contigecies	0.0	0.0	0.0	0.0	0.0	0.0		0.1	0.1	0.1
Parliamentary Service	0.0	0.0	0.0	0.0	0.0	0.0	0.4	0.4	0.3	
Judicial Service	0.0	0.0	0.0	0.0	0.0	0.0	0.3	0.2	0.2	
Fiscal balance										
Deficit excluding grants (commitment basis)	-4.4	-4.0	-4.6	-4.2	-4.9	-5.8	-6.4	-9.2	-8.3	-7.4
Deficit including grants (commitment basis)	-3.3	-3.4	-3.6	-3.6	-4.5	-5.4	-5.9	-8.7	-7.9	-7.0
Deficit including grants (cash basis)	0.3	-4.4	-5.8	-3.4	-4.5	-5.4	-5.9	-8.4	-7.5	-8.9
Financing										
Foreign Financing	0.3	1.5	0.8	0.8	2.8	1.9	2.1	3.7	4.1	3.9
Domestic Financing	-0.6	2.8	5.0	2.7	1.6	3.8	4.0	4.3	3.1	3.1
Total Public Debt (net)	33.4	35.4	36.6	39.1	37.0	38.5	43.7	44.8	48.7	45.3
External Debt	19.1	20.0	18.9	21.0	19.6	18.7	22.2	24.5	27.4	24.1
Domestic Debt (net)	14.3	15.4	17.7	18.1	17.4	19.8	21.5	20.3	21.4	21.2
Memo:										
GDP (Calender year current market prices, Ksh billion	2,483	2,864	3,169	3,726	4,261	4,745	5,398	6,224		
GDP (Fiscal year current market prices, Ksh billion)	2,317	2,673	3,017	3,448	3,994	4,503	5,072	5,811	6,586	7,435

Source: Quarterly Budget and Economic Review (various issues, the Budgetry Summary for the fiscal year 2017/18 and the supporting information, (February 2017): National Treasury
*Note: *indicate Preliminary results*

Table 24: 12-months cumulative balance of payments

BPM6 Concept (US$ million)

Actual (percent of GDP)	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
A. Current Account, n.i.e.	-505	-796	-1,821	-1,713	-2,371	-3,821	-4,205	-4,838	-5,998	-4,322	-3,817
Merchandise A/C	-3,243	-4,222	-5,593	-4,952	-6,216	-8,355	-9,315	-10,243	-11,319	-9,577	-7,861
Goods: exports f.o.b.	3,509	4,153	5,067	4,526	5,248	5,834	6,212	5,846	6,219	5,985	5,761
Goods: imports f.o.b.	6,752	8,375	10,659	9,479	11,464	14,189	15527	16,089	17,538	15,563	13,622
Oil	1,745	1,919	3,051	2,192	2,673	4,082	4,081	3,838	4,026	2,500	2,087
Services	1,013	1,263	1,377	1,084	1,744	1,994	2,602	2,926	2,405	2,329	1,260
Services: credit	2,431	2,938	3,260	2,904	3,789	4,131	4,990	5,130	5,066	4,496	4,046
Services: debit	1,418	1,675	1,883	1,820	2,045	2,138	2,387	2,204	2,662	2,167	2,786
Income	1,725	2,162	2,395	2,156	2,101	2,540	2,507	2,479	2889	2,795	2,538
B. Capital Account, n.i.e.	168	157	94	261	240	235	235	158	275	257	237
C. Financial Account, n.i.e.	-677	-2,247	-1,423	-3,782	-3,252	-3,425	-5,542	-5,183	-7,008	-5,070	-6,906
Foreign Direct Investments	-27	-1,001	-384	-1452	-1,117	-1,364	-1,142	-920	-1,045	-1,088	-194
Private Investments (Medium and Long-term)	21	16	25	-81	-156	1	-218	-273	-3,716	156	-447
Official Investments (Medium and Long-Term)	-671	-1,262	-1,064	-2,249	-1,979	-2,062	-4,182	-3,990	-2,248	-4,139	-6,265
D. Net Errors and Omissions	235	-805	-189	-1,215	-947	-734	-348	-134	168	-1,260	-3,197
E. Overall Balance	-575	-802	493	-1115	-174	896	-1223	-369	-1453	255	-129
F. Reserves and Related Items	575	802	-493	1115	174	-896	1223	369	1453	-255	129
Reserve assets	618	941	-480	1322	154	246	1455	859	1333	-361	38
Credit and loans from the IMF	-6	116	-17	199	-34	284	193	177	-119	-107	-91
Exceptional financing	48	23	30	8	13	858	38	312	0	0	0
Gross Reserves (USD Million)	3,331	4,557	4,641	5,064	5,123	6,045	7,160	8,483	9,738	9,794	9,588
Official	2,415	3,355	2,875	3,847	4,002	4,248	5,702	6,560	7,895	7,534	7,573
Commercial Banks	916	1,202	1,765	1,217	1,121	1,797	1,458	1,923	1,843	2,259	2,015
Import cover (calender year)	3.5	4.0	2.8	4.1	3.6	3.1	3.8	4.3	4.7	5.1	5.3
Imports cover (36 months import)	3.9	4.4	3.1	3.9	3.9	3.4	4.0	4.3	4.9	4.8	
Memo:											
Annual GDP at Current prices (USD Million)	25,826	31,958	35,895	37,022	40,000	41,953	50,411	55,101	61,395	63,398	

Source: Central Bank of Kenya

Table 25: Kenya's public and publicly guaranteed debt, June 2014 to September 2016

KShs. Millions	14-Jun	14-Sep	14-Dec	15-Mar	15-Jun	15-Sep	15-Dec	16-Mar	16-Jun	Sept16*
TOTAL PUBLIC DEBT (Net)	2217315	2103447	2275952	2394450	2601430	2723629	2844003	2938292	3217831	3133916
Lending	-5701	-5701	-5701	-5701	-5701	-5701	-5701	-5701	-5701	-5701
Government Deposits	-199815	-239554	-298879	-275083	-236565	-208869	-305496	-320041	-394856	-426911
Total Public Debt (Gross)	2422831	2348702	2580532	2675234	2843696	2938199	3155200	3264034	3618388	3566528
External Debt	1138504	1087828	1272583	1278108	1423253	1550233	1615183	1617506	1803255	1711973
Bilateral	289914	278547	389083	384607	445057	482203	481282	478883	539181	540589
Multilateral	597340	608022	612353	618456	684631	754599	751154	762089	812270	719292
Commercial Banks	234799	185163	255188	259746	276937	295642	366231	360175	442598	442886
Suppliers Credit	16451	16096	15959	15298	16628	17788	16516	16359	9206	9206
Domestic Debt	1284327	1260874	1307949	1397126	1420443	1387966	1540017	1646528	1815133	1854555
Central Bank	65700	63580	58286	64835	63335	107637	101386	102648	99856	58945
Commercial Banks	617221	601426	649940	715011	730419	682694	764399	829688	927307	969790
Non Banks & Nonresidents	601406	595868	599723	617280	626689	597635	674232	714192	787970	825820
(%) of Total public debt(gross)										
External Debt	47.0	46.3	49.3	47.8	50.0	52.8	51.2	49.6	49.8	48.0
Domestic Debt	53.0	53.7	50.7	52.2	50.0	47.2	48.8	50.4	50.2	52.0
% of External debt										
Bilateral	25.5	25.6	30.6	30.1	31.3	31.1	29.8	29.6	29.9	31.6
Multilateral	52.5	55.9	48.1	48.4	48.1	48.7	46.5	47.1	45.0	42.0
Commercial Bank & Supplier Credit	22.1	18.5	21.3	21.5	20.6	20.2	23.7	23.3	25.1	26.4
Commercial Banks	20.6	17.0	20.1	20.3	19.5	19.1	22.7	22.3	24.5	25.9
Suppliers Credit	1.4	1.5	1.3	1.2	1.2	1.1	1.0	1.0	0.5	0.5
% of Domestic debt										
Central Bank	5.1	5.0	4.5	4.6	4.5	7.8	6.6	6.2	5.5	3.2
Commercial Banks	48.1	47.7	49.7	51.2	51.4	49.2	49.6	50.4	51.1	52.3
Non Banks & Nonresidents	46.8	47.3	45.9	44.2	44.1	43.1	43.8	43.4	43.4	44.5

Source: National Treasury (Quarterly Economic Budgetary Review, November 2016)
*Note: *Provisional*

Table 26: Growth outlook

Annual growth (percent)	2014	2015	2016e	2017f	2018f	2019f
BASELINE						
GDP						
Revised projections	5.4	5.7	5.8	5.5	5.8	6.1
Previous projections (KEU 14)	5.3	5.6	5.9	6.0	6.1	
Previous projections (KEU 13)	5.3	5.6	5.9	6.1	6.2	
Private consumption	4.3	5.1	4.8	5.7	5.8	5.9
Government consumption	1.7	13.0	7.0	1.5	1.1	0.8
Gross fixed capital investment	14.2	6.7	-9.3	7.8	9.4	10.8
Exports, goods and services	5.8	6.2	0.6	4.0	4.3	4.8
Imports, good and services	10.4	1.2	-4.7	4.5	5.1	5.7
Agriculture	3.5	5.6	5.6	5.4	5.4	5.4
Industry	6.5	6.9	5.7	5.7	5.6	5.6
Services	5.7	5.4	5.3	5.5	6.0	6.6
Inflation (Consumer Price Index)	6.9	6.6	6.5	8.0	6.8	6.5
Current account balance (% of GDP)	-10.3	-6.8	-6.0	-6.4	-7.2	-8.0
Fiscal balance (% of GDP)	-8.4	-7.5	-8.5	-6.7	-5.4	-4.4
Debt (% of GDP)	49.0	47.9	48.3	48.0	47.2	46.0
Primary Balance (% of GDP)	-5.8	-5.0	-6.1	-4.3	-2.6	-2.0

Source: World Bank
Note: e (estimate); f (forecast)

Table 27: Credit to private sector

Year	Month	Total private sector annual growth rates	Agriculture	Manufacturing	Trade	Building and construction	Transport and communication	Finance and insurance	Real estate	Mining and quarrying	Private households	Consumer durables	Business services	Other activities
2014	January	20.5	-1.1	12.8	18.6	0.1	23.1	-13.6	23.3	-16.3	35.6	20.2	50.1	24.6
	February	21.5	3.4	16.8	20.2	5.4	31.2	12.1	24	-14	30.9	20.4	48.1	15.1
	March	22.7	7.7	17.3	25.2	2	44.8	39	28.4	-8.6	44	22.5	45.5	-14.6
	April	23.9	16.1	22.8	24.5	4.4	45.4	31.2	33.2	5.9	35.2	21.8	51	-15.5
	May	25	16.7	28.5	25.4	10.7	50.1	26.5	31.6	9.2	24.7	22	44	-3.4
	June	25.8	17.9	31.7	24.4	15.1	44.3	31.2	27.5	30.7	28.3	20.6	38.2	3
	July	25.5	18.8	27.5	25.9	9.4	42.3	37.8	30.8	24.3	30.2	20.3	36.5	1.8
	August	24.5	20.9	27	25.1	10.8	46.1	42.6	29.4	19.6	27.8	18.4	31.7	-0.2
	September	24.5	30.8	35.2	20.7	11.8	43.8	40.4	36.5	-0.5	23.8	16.4	44.1	-12.3
	October	23.6	36.8	32.7	18.7	10.3	45.4	75.1	35.7	3.5	38	11.4	27.5	-24.8
	November	22.2	32.1	29.8	19.7	11.3	45.2	66.9	31.6	1.9	38.9	12.4	28.9	-29.9
	December	22.2	27.9	30.7	21.2	13.6	45.6	68.4	32.4	-15.8	39.1	18.7	25	-32.3
2015	January	21.8	25.2	30.1	19.8	17.6	43	76.1	33.4	-3.8	35.2	14.2	24.8	-31.3
	February	20.7	24.7	27.5	21.5	11.6	38.6	79.6	29.1	-16.2	38.7	15.3	19.3	-31.4
	March	19.6	22.3	21.1	18.8	12.7	31.3	47.5	19.6	-20.1	28	12.4	27.8	-8.9
	April	19.9	20.8	21.6	23.6	12.6	32.3	49.2	17.7	-17.1	29.5	13.1	19.7	-8.9
	May	20.9	20.5	25.8	23	14.5	27	50.8	21.3	-13.7	31.5	11.6	16.4	-3.9
	June	20.5	24	20	25.9	15.5	33.8	43.3	19.4	-22.1	31.2	21.6	15.8	-11.1
	July	21.2	28.5	22.3	26.7	19.8	33.4	46.8	15.5	-17.9	28.6	21.5	25.3	-12.6
	August	21	28.7	25.3	25.9	22.1	30	50.5	15	-18	28.5	21	22.5	-14.2
	September	20.8	21.4	19.3	29.7	27.9	29	45.7	12.5	-5.4	26.6	19	15.9	-0.9
	October	19.5	17.2	20.2	23.6	37.6	32.1	26.4	9.8	-15.5	18.2	18	24.1	8.6
	November	18.7	12.5	20.8	22.2	34	32.3	28.5	10.6	-22.8	16.7	15.3	19.3	14.6
	December	18	14.1	16.2	21.3	30.7	26.5	0	6.2	-11.3	9.1	14.3	63.5	-1
2016	January	16.8	27.3	19.3	11.7	28.4	39.1	65.2	15.9	-9.3	9.3	39.9	-5.0	2.0
	February	16.0	31.7	22.0	9.2	23.6	36.3	61.7	17.3	1.7	6.7	36.8	-3.5	-3.1
	March	15.5	26.8	24.1	6.8	26.3	30.7	64.9	22.5	12.5	5.0	37.6	-5.0	-7.1
	April	13.5	23.5	18.3	7.0	26.2	28.5	70.2	23.5	5.3	5.0	35.0	-13.3	-11.8
	May	11.1	28.3	15.1	-2.1	19.3	25.5	58.7	17.7	3.2	5.1	9.3	1.6	3.5
	June	9.0	21.0	16.1	-1.3	15.9	22.8	59.4	20.2	-1.6	0.1	24.5	-13.7	-8.3
	July	7.1	12.0	15.3	-1.6	12.8	21.4	65.2	17.0	-4.5	-2.4	24.2	-16.7	-10.0
	August	5.4	5.8	2.2	0.7	11.2	26.3	48.7	18.3	-32.8	1.5	30.4	-25.1	-12.8
	September	4.8	1.2	-2.0	20.3	1.3	13.1	9.1	8.7	-33.7	7.8	30.1	-15.9	-29.6
	October	4.7	1.5	-4.3	18.0	-4.9	14.3	7.9	9.2	-36.4	7.3	32.9	-9.2	-27.0
	November	4.6	6.2	-4.0	24.3	-5.3	11.4	6.6	8.8	-21.3	7.8	37.1	-18.7	-33.0
	December	4.3	4.2	-7.0	22.3	-3.9	5.5	8.2	8.9	-19.1	9.0	31.6	-18.5	-22.5

Source: Central Bank of Kenya

KENYA ECONOMIC UPDATE

with special focus on affordable Housing

Kenya is at a critical juncture as it transitions from the completion of the Second Medium Term Plan (MTP-II, 2013-2017) to MTP-III (2018-2022), which is currently under preparation. The report has four main messages. First, Kenya's economic growth continued to outperform its peers in 2016. In contrast to the slump in economic growth in Sub Saharan Africa to 1.5 percent (a three decade low), growth in Kenya accelerated for the third consecutive year reaching 5.8 percent. Kenya's robust growth performance was supported by lower oil prices, favorable agriculture output in the first half of 2016, a tourism sector rebound, strong inward remittances, a relatively stable macroeconomic environment and improvements in the steady easing of certain supply-side constraints due to earlier public investments.

Secondly, due to emerging headwinds, economic activity in Kenya will encounter some speed bumps in the near to medium term which will likely impact MTP-II implementation and should inform the scope of the MTP-III. These headwinds include, the ongoing drought, depressed private sector credit growth, the rise in oil prices, and fiscal pressures. However, the completion of phase one of Standard Gauge Railway and a projected strengthening of the global economy is expected to provide some tailwind. The net effect of these changes in the economic landscape will likely cause near term growth to moderate to 5.5 percent in 2017 before picking up to 6.1 percent by 2019 as headwinds (e.g. drought) subside.

Third, sustaining Kenya's robust growth will require safeguarding its hard earned macroeconomic stability by continuing to implement prudent fiscal and monetary policies. The consolidation of the fiscal stance in line with the Medium Term Fiscal Framework should help anchor macroeconomic stability and create the fiscal space for a public investment drive supportive of the medium term plans. Further, given the systemic importance of the banking sector, addressing the unintended consequences of the interest rate caps should help strengthen financial intermediation in the Kenyan economy.

Finally, while Kenya's growth has been robust, there are latent opportunities to accelerate growth to levels necessary to achieve Vision 2030. This report identifies some of these growth and job-creation opportunities as well as the need to address a critical social need by supporting the development of the housing market for lower income households in Kenya. On the demand side, a key constraint to housing is finance. The report addresses policy measures that can be taken to alleviate the housing finance problem, including those that have worked well in other middle income countries.

The World Bank remains committed to working with key Kenyan stakeholders to identify potential policy and structural issues that will enhance economic growth and keep Kenya on the path to upper middle income status in accordance with the aspirations of Vision 2030. The semi-annual Kenya Economic Update offers a forum to discuss these development trends. We hope that you too will join us in debating topical policy issues that can contribute to fostering growth, shared prosperity and poverty reduction in Kenya.

World Bank Group
Delta Center
Menengai Road, Upper Hill
P. O. Box 30577 – 00100
Nairobi, Kenya
Telephone: +254 20 2936000
Fax: +254 20 2936382
http://www.worldbank.org/en/country/kenya

KENYA ECONOMIC UPDATE

Join the conversation:
Facebook and Twitter
@Worldbankkenya
#KenyaEconomicUpdate

Produced by Macroeconomic & Fiscal Management, Finance & Markets, Social Urban, Rural & Resilience and Poverty & Equity Global Practice