Kenya Q3’2017 Balance of Payments Note

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Kenya’s current account balance worsened during Q3’2017, coming in at Kshs 145.4 bn from Kshs 112.8 in Q3’2016, a growth of 28.9%. This translate to current account balance of equivalent to 7.0% of GDP in Q3’2017 from 6.0% recorded in Q3’2016. This was as a result of imports rising by 20.3% to Kshs 450.9 bn from Kshs 374.8 bn in Q3’2016 mainly due to increased food and petroleum imports, faster than exports that rose by 2.6% to Kshs 145.0 bn from Kshs 141.3 bn in the same periods. The table below shows the breakdown of the various current account components, comparing Q3’2016 and Q3’2017:

all figures in Kshs bns unless stated otherwise

Annual Balance of Payments

Item	Q3'2016	Q3'2017	% Change
Merchandise Trade	(218.7)	(289.7)	32.5%
Services Trade	36.5	44.7	22.5%
Primary Income	(11.8)	(20.6)	74.9%
Secondary Income (Transfers)	81.2	120.2	48.1%
Current Account	(112.8)	(145.4)	28.9%
GDP at Current Prices (Q3’2017 Quarterly GDP Report by KNBS)	1,870.6	2,085.3	11.5%
% of GDP	*6.0%*	*7.0%*	*0.9%*

Key points from the table include:

i. The secondary income/transfers surplus increased by 48.1% to Kshs 120.2 bn from Kshs 81.2 bn in Q3’2016, driven by a 17.7% increase in diaspora remittances to Kshs 51.3 bn from Kshs 43.6 bn in Q3’2016,

ii. The merchandise trade deficit widened by 32.5% to Kshs 289.7 bn from Kshs 218.7 bn in Q3’2016 driven by a faster rise in imports than exports, at 20.6% and 2.4%, respectively. The increase in imports was due to a 1,450.2% and 19.6% increase in value of maize and petroleum products imports due to the subdued harvest that led to lower internal maize production, necessitating the importation of maize to meet the demand for maize flour, and rising global oil prices, respectively,

iii. In terms of exports by region, Africa remained the largest merchandise export destination with 38.8%, followed by Far East exports at 28.0%. The European Union accounted for 20.0% owing to increased demand from the UK, The Netherlands, France and Belgium, with tea remaining the largest export commodity, accounting for 27.9% of the total value of export commodities,

iv. In terms of imports by region, the Far East was the largest merchandise import source, accounting for 42.0% in Q3'2017 with China as the leading source with 19.6% down from 26.3%, though maintaining the top spot as Kenya's biggest import source,

v. As a result of the increase in trade deficits that outweighed the marginal increase in income surplus, the current account deficit widened faster than the growth in GDP at current prices (11.5%), resulting in the current account deficit worsening to 7.0% of GDP from 6.0% recorded in Q3'2016.

The continued widening of the current account in Q3'2017 affected the Kenya Shilling negatively during the quarter, as the shilling lost 2.0% against the dollar to close at Kshs 103.2 from Kshs 101.3 at the end of Q3'2016. However, we note that the forex reserves held by the Central Bank of Kenya declined by 3.9% in the same period to close the quarter at USD 7.5 bn (5.0 months of import cover) from USD 7.8 bn (5.2 months of import cover) at the end of Q2, which suggests that the CBK may have used the reserve to stabilize the currency as the current account balance widened. The government will have to put practical measures in place to improve the negative balance of trade in order to avoid shocks on the shilling going forward, which include: (i) supporting growth of the domestic manufacturing sector in order to reduce importation of goods that can be produced locally, (ii) encouraging "Made in Kenya" products and strengthening a national marketing body for such products abroad to boost exports, and (iii) providing incentives for exporters which the government is already planning for through the rolling out of Special Economic Zones (SEZs) in key urban areas including Mombasa, Lamu and Kisumu with incentives such as exemption on VAT, reduced corporate tax rates for a defined period, access to quality infrastructure, one-stop-shops for licenses, and facilitation of exportation of finished goods. However, with development-essential goods such as machinery & transport equipment being one of the largest contributors to the country's import while weather-dependent agricultural products make up more than 50.0% of our exports, we expect the trade balance to remain at a deficit in the medium term as the country develops.