

Cytonn Note on the Monetary Policy Committee Meeting for September 2016

The Monetary Policy Committee (MPC) is set to meet on Tuesday 20th of September, to discuss the way forward with regard to monetary policy and possible actions on the Central Bank Rate (CBR). In their previous meeting, MPC maintained the CBR at 10.5% owing to stable and favourable macroeconomic factors characterized by stable inflation and exchange rates.

However, this meeting is quite different from the others given the MPC will be meeting for the first time after the enactment of the Banking Act Amendment Bill, 2015, which capped lending rates at 4.0% above the CBR and a floor on the deposit rates at 70% of the CBR. This now means that the MPC will have credit pricing to consider in their decision making.

A number of macro-economic indicators have changed since the July 2016 MPC meeting as summarized in the table below:

Key Macro-Economic Indicators – Kenya					
Indicators	Expectations at start of 2016/2017 Fiscal Year	Experience since the last MPC meeting on July 25, 2016	Going forward	Probable CBR Direction (Last MPC Meeting)	Probable CBR Direction (This month)
Government Borrowing	Government is expected to borrow Kshs. 229.0 bn for the 2016/2017 financial year	The government has been ahead of its domestic borrowing target having borrowed Kshs. 67.4 bn for the current fiscal year against a target of Kshs 53.0 bn. The Government has postponed foreign borrowing to Q4'2016	Given the signing of the Banking (Amendment) Bill, 2015 into law, we expect that banks will have a preference to lending to the government hence we do not expect pressure on government borrowing going forward	Neutral	Neutral
Kenya Revenue Authority	KRA to miss the revenue collection target	The KRA met their 2015/2016 fiscal year target of Kshs. 1.2 tn	We expect the government to meet on the revenue collections due to (i) the passing of the Tax Procedural Bill and reforms in the Kenya Revenue Authority to eradicate corruption (ii) Positive macro-economic environment which is expected to support corporate earnings growth	Negative	Neutral
Inflation	Above the CBK target of 7.5%	Declined to 6.4% in the month of August	We expect Inflation rate to remain below the CBK's upper limit of 7.5%	Negative	Neutral
Exchange rate (USD/Kshs)	To remain stable supported by strong dollar reserves and improved foreign exchange inflows through improved diaspora remittances and tea exports	The shilling has appreciated 0.3% against the dollar	The shilling to remain stable in the short to medium term supported by (i) foreign exchange reserves equivalent to 5.1 months of import cover, and (ii) increased dollar inflows from tourism and remittances. We are however likely to see upward pressure in the short term driven by volatility in the stock market	Neutral	Neutral

Banking Sector	We expect improved governance, following the closure of Imperial and Dubai Banks and consolidations within the banking industry	The Banking Amendment Act, 2015 was enacted to law capping lending rates at 4% above the CBR and deposit rates at 70% of the CBR	We expect increased regulations with banks employing strategic initiatives and innovation to derive value as interest rate caps set in	Neutral	Neutral
Liquidity	Liquidity expected to improve given high maturities of government securities	The money market has been liquid with the interbank averaging 5.0%. However, liquidity has been skewed towards large banks as indicated by the activities in the reverse repo market	We expect the money market to be liquid however skewed towards the larger banks	Neutral	Neutral

Conclusion

With the above state of affairs in the money market environment, all indicators are neutral towards the MPC decision on CBR. In light of this, we are of the view that MPC will maintain the CBR at 10.5%.