Kenya Q1’2019 Balance of Payments Note

The Kenya National Bureau of Statistics released the Quarterly Balance of Payments report for Q1’2019. In this note, we analyse the changes in the current account balance and the balance of payments before giving an outlook on both.

Current Account Balance

Kenya’s current account deficit improved by 32.7% during Q1’2019, coming in at Kshs 78.8 bn, from Kshs 117.1 bn in Q1’2018, equivalent to 3.2% of GDP, from 5.2% recorded in Q1’2018. This was mainly driven by:

(i) The 89.6% increase in the services trade balance to Kshs 60.7 bn, from Kshs 32.0 bn,
(ii) A 3.8% decline in the merchandise trade deficit to Kshs 239.0 bn, from Kshs 248.3 bn in Q1’2018, and
(iii) The 14.6% rise in the secondary income (transfers) balance, to Kshs 128.5 bn, from Kshs 112.2 bn in Q1’2018.

The table below shows the breakdown of the various current account components, comparing Q1’2018 and Q1’2019:

all figures in Kshs bns unless stated otherwise			
Q1’2019 Current Account Balance			
Item	**Q1'2018**	**Q1'2019**	**% Change**
Merchandise Trade Balance	(248.3)	(239.0)	**(3.8%)**
Services Trade Balance	32.0	60.7	**89.6%**
Primary Income Balance	(13.0)	(29.1)	**124.3%**
Secondary Income (Transfers) Balance	112.2	128.5	**14.6%**
Current Account Balance	**(117.1)**	**(78.8)**	**(32.7%)**
GDP at Current Prices (Q1’2019 Quarterly GDP Report by KNBS)	2,239.0	2,489.3	**11.2%**
Current Account Balance as a % of GDP	***(5.2%)***	***(3.2%)***	***(2.1%)***

Key take-outs from the table include:

i. The secondary income/transfers surplus increased by 14.6% to Kshs 128.5 bn, from Kshs 112.2 bn in Q1’2018, driven by various factors such as diaspora remittances which recorded a 2.9% increase to Kshs 67.9 bn, from Kshs 65.9 bn recorded in Q1’2018,
ii. The merchandise trade deficit contracted by 3.8% to Kshs 239.0 bn, from Kshs 248.3 bn in Q1’2018, driven by a 3.4% decline in merchandise imports to Kshs 397.1 bn, from Kshs 411.3 bn in Q1’2018. This improvement was however impeded by a 2.9% decline in merchandise exports to Kshs 158.2 bn from Kshs 162.9 bn recorded in a similar period in 2018. The decline in the merchandise imports was mainly on account of declines in the value of maize and; iron and steel imports by 82.4 % and 15.8% to Kshs 1.1 bn and Kshs 22.4 bn, respectively,
iii. In terms of exports by region, Africa remained the largest merchandise export destination with 34.1% of the total exports valued at Kshs 53.4 bn, a 1.1% decline from Q1’2018 total exports of Kshs 54.0 bn. The European region accounted for 25.6% of total exports, valued at Kshs 40.1 bn, a 6.6% increase from the Kshs 37.6 bn recorded in Q1’2018. Similarly, exports to the United States of America rose by 31.9% to Kshs 12.2 bn, from Kshs 9.3 bn in Q1’2018,
iv. In terms of imports by region, the European Union accounted for 15.7% of total imports in Q1’2019, valued at Kshs 66.0 bn, a 27.4% increase from the Kshs 51.8 bn recorded in Q1’2018. Asia was the largest merchandise import source, accounting for 61.2%, with the value of imports decreasing by 3.9% to Kshs 421.2 bn, from Kshs 438.5 bn recorded in Q1’2018. The decline was attributed to a decrease in imports from Malaysia (25.1%), India (22.9%), China (12.4%) and Japan (11.1%). Commodities that recorded marked reductions in import values from China included railway wagons and light emitting diodes, and,

v. As a result of the decline in the merchandise trade deficit, the increase in the services trade balance, and the increase in the secondary income balance, the current account deficit improved faster than the growth in GDP at current prices, resulting in the current account deficit improving to 3.2% of GDP, down from 5.2% recorded in Q1'2018.

Balance of Payments

Kenya's balance of payments surplus declined by 87.6% to Kshs 25.5 bn Q1'2019, from Kshs 205.5 bn in Q1'2019, translating to a balance of payments surplus equivalent to 1.0% of GDP in Q1'2019, from a surplus of 9.2% recorded in Q1'2018. The table below shows the breakdown of the various balance of payments components, comparing Q1'2019 and Q1'2018:

all figures in Kshs bns unless stated otherwise			
Q1'2019 Balance of Payments			
Item	**Q1'2018**	**Q1'2019**	**% Change**
Current Account Balance	(117.1)	(78.8)	**(32.7%)**
Capital Account Balance	8.4	4.3	**(49.3%)**
Financial Account Balance	333.2	95.7	**(71.3%)**
Net Errors & Omissions	(19.0)	4.4	**(123.3%)**
Balance of Payments	**205.5**	**25.5**	**(87.6%)**
GDP at Current Prices (Q1'2019 Quarterly GDP Report by KNBS)	2,239.0	2,489.3	**11.2%**
Balance of Payments as a % of GDP	***9.2%***	***1.0%***	***(8.2%)***

Key take-outs from the table include:

i. The current account deficit narrowed by 32.7% to Kshs 78.8 bn, from Kshs 117.1 bn in Q1'2018, mainly due to the 89.6% increase in the services trade balance, coupled with the 3.8% decline in the merchandise trade deficit to Kshs 239.0 bn from Kshs 248.3 bn in Q1'2018,
ii. The financial account balance declined by 71.3% to Kshs 95.7 bn, from Kshs 333.2 bn in Q1'2018, attributed to a decline in financial inflows. Thus, the gross official reserves stood at Kshs 853.1 bn as at end of Q1'2019 compared to Kshs 944.1 bn as at end of Q1'2018, and,
iii. The Balance of Payments (BoP) thus decreased by 87.6% to a surplus of Kshs 25.5 bn from a surplus of Kshs 205.5 bn in Q1'2018, mainly due to the 71.3% decline in the financial account balance, coupled with the 49.3% decrease in the capital account balance.

Conclusion

The narrowing of the current account in Q1'2019 affected the Kenya Shilling positively during the quarter, as the shilling remained stable against the dollar to close at Kshs 100.8 at the end of Q1'2019. The narrowing was supported by the decline in the merchandise trade balance, coupled with the increase in the services trade balance. While the improvement in the trade deficit is commendable, we are still of the view that the government has to focus on putting further practical measures in place to move to a surplus from the current deficit, which include:

(i) Continue supporting the growth of the domestic manufacturing sector in order to reduce importation of goods that can be produced and sourced locally. Policies such as: (i) reduction of import duties on raw timber from 10% to 0% to promote local production, the import duty on finished products to be retained at 25%, as proposed in the Budget 2019/2020, will aid in this;
(ii) Encouraging "Made in Kenya" products through customs reforms such as; an export levy of 10% will be charged on tanned and crust hides and skins to boost value addition and promote manufacturing of local leather products, and,

(iii) Cushioning local manufacturers by reducing import declaration fees from 2% to 1.5% on raw materials and intermediate goods and increasing that on finished goods from 2% to 3.5%.

However, with development-essential goods such as machinery & transport equipment being one of the largest contributors to the country's import bill 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, weighed down by imports for the ongoing infrastructure developments such as the second phase of the Standard Gauge Railway.