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LOW TAX YIELD THREATENS DEFICIT CUTS

The taxman's below-par showing stands in the way of the Treasury's plan to halve budget deficits and slow down accumulation of debt stock in five years, analysts at Fitch Ratings have said. Kenya targets to reduce fiscal deficit from 7.2% of gross domestic product (GDP) in the year ended June 2018 to 6.3% in the current year ending June, 5.6% in the year starting July 2019 and further to 3.1% in the year ending June 2023.Fitch says that weak growth in revenue, largely tax receipts, presents the biggest challenge to Kenya's fiscal consolidation plan. Ordinary revenue fell short of KShs.774.99 billion target by KShs.52.70 billion in the first half of the current financial year ending in June. This came on the back of slower recovery in private sector activity from the twin shocks of prolonged elections and biting drought in 2017.

FUEL LEVY IN POWER BILLS HITS 5-YEAR HIGH

The fuel cost levy in May electricity bills has jumped by the biggest margin in five years on reduced use of cheaper hydro-power following poor rains. The dry weather forced Kenya to generate more electricity using diesel, setting the stage for a rise in electricity prices through the monthly adjusted fuel surcharge levy. Energy and Petroleum Regulatory Authority (EPRA) data shows that fuel levy — which is influenced by the share of electricity from diesel generators —rose to KShs.3.75 per kilowatt hour (kWh), up from KShs.2.75 last month. The KShs.3.75 charge took effect on Friday for pre-paid consumers with postpaid users set to feel the pain from next month. The additional charges will be highest rise since May 2014 when the fuel levy rose by KShs.2.03.

COURT EXTENDS ORDERS ON HOUSING LEVY

The High Court has extended orders barring the government from implementing the 1.5% housing levy until May 27.The order was issued on Monday by Justice Maureen Onyango in Nairobi to allow for the consolidation of the various cases filed against the plan. The Jubilee government plans to take 1.5% of workers' gross salary in the formal sector to set up a housing fund. But various parties including the Central Organization of Trade Union (COTU), Trade Union Congress of Kenya, Consumers Federation of Kenya (COFEK) and the Federation of Kenyan Employers (FKE) have filed suits challenging the levy.

FUEL COST UP KSHS.107BN ON GLOBAL PRICE SURGE

Kenya's fuel import bill has gone up by KShs.107 billion in the past two years following a sharp rise in global crude oil price amid increasing local consumption. Data by Central Bank of Kenya (CBK) shows that in the 12 months to April 2019, petroleum product imports stood at KShs.344.8 billion ($3.41 billion) compared to KShs.299.6 billion in the corresponding period in 2018. In the year to April 2017 the figure was KShs.237.8 billion. The price of a barrel of crude has in the past two years gone up by more than 50% to $68.80 (KShs.6,950), having sold at $49.50 in April 2017.

The sharp rise in fuel costs has weighed significantly on household budgets due to the knock-on effect of transport costs on the price of goods, and is also a negative factor on the current account by eating up a larger slice of the country's dollar reserves. Diesel consumption went up by 55,520 metric tons equivalent to 3% to 2.18 million metric tons in the 12 months to February 2019 compared to a similar period in 2018, while consumption of super petrol rose by 150,000 metric tons or 12% to 1.38 million metric tons. Jet fuel consumption rose from 563,900 metric tons in the 12-months to February 2018 to 679,040 metric tons in the year to February 2019.

COOKING GAS USE RISES TO KSHS.15BN ON LOGGING BAN

The extended ban on logging in government forests triggered a 42,000 ton increase in cooking gas usage as imports rose to an all-time high of 240,484 tons valued at KShs.15 billion. The 21% increase was further informed by the government's decision to increase kerosene retail prices from KShs.66.99 in 2017 to KShs.90.06 last year through a tax rise, putting the cost out of reach of majority of poor households. Kerosene is a must-have for most urban families and is mainly used for cooking and lighting homes in areas yet to be linked to the national grid and off-grid power solutions.

Sales of timber from government forests dropped by 83.6% from 881,800 cubic meters in 2017 to 144,200 cubic meters in 2018.Softwood sales dropped from 798,400 cubic meters in 2017 to 30,900 cubic meters in 2018. The sale of hardwood timber sourced from private farms increased from 83,400 cubic meters in 2017 to 113,300 cubic meters in 2018.

TEA PRICE AT 10-MONTH HIGH ON LOW SUPPLY

Tea prices at the Mombasa auction have hit a 10-month high after months of poor performance as volumes declined by 2.3 million kilos. Data from the East African Tea Traders Association (EATTA) indicate a kilo fetched KShs.235 last week against KShs.225 in the previous sale marking the highest price recorded this year. The price kicked off at KShs.215 a kilo in the first sale of 2019 before taking a downward trend to touch a four-year low of KShs.193 early last month. The volumes have been coming down as the drought that ravaged the country in the first quarter cut supply of green leaf to factories.

TEA SALES TO PAKISTAN DOWN BY OVER A THIRD IN THE FIRST THREE MONTH

Tea exports to Pakistan fell 37% in the first quarter of the year compared with a similar period last year following low prices witnessed at the auction A market report by the Tea Directorate indicates volumes exported to Kenya's leading tea buyer dropped from KShs.15 billion in the first three

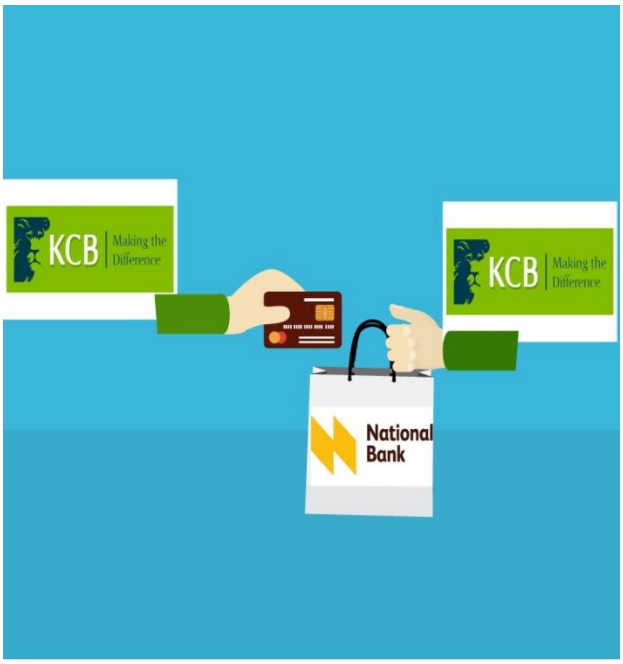
months of last year to KShs.10 billion in the period under review. The low earnings were attributed to depressed prices in the first quarter, which stood at KShs.220 per kilo compared with KShs.290 in the corresponding period last year.

According to the regulator, Pakistani purchased 49.3 million kilograms of the commodity in the first quarter representing 33% of the total volume exported after declining from the previous 54 million kilos. A total of 137 million kilograms was exported through the auction during the period with 43 countries importing the beverage, which was up from 32 countries in the corresponding period of last year.

NEW LUXURY CAR SALES DROP 60% IN Q1

Sales of new luxury cars dropped 60 per cent in the first quarter ended March on the back of stock outs of BMW, Porsche, Bentley and Jeep brands. Unit sales of the dealers including DT Dobie and Inchcape Kenya stood at 26 in the review period compared to 65 a year earlier, according to statistics from the Kenya Motor Industry Association (KMI).

Sales performance in the high-end car segment was much worse than in the overall new vehicle market that recorded a 14.5 per cent drop in orders to 2,741 units in the same period. The industry-wide slump was attributed to difficulty in accessing loans and slow registration by the National Transport and Safety Authority (NTSA).There were no Jeep, Bentley, Porsche or BMW sales in the review period, resulting in one of the worst quarters for luxury car dealers.



KCB, NBK MERGER TO CREATE GIANT BANK KSHS.1 TRILLION ASSETS

The planned merger between Kenya's biggest lender by assets, KCB Group, and the State-owned National Bank of Kenya (NBK) is set to create a giant bank whose combined balance sheet is expected to hit KShs.1 trillion in three years. KCB, which also operates in Uganda, Tanzania, Rwanda, Burundi and South Sudan, last month offered to buy NBK through a share swap of one KCB share for every 10 of NBK.

KCB proposes to maintain NBK as a standalone subsidiary of KCB Group for a period of two years post-acquisition and thereafter fully integrate NBK into KCB Bank Kenya. The combined giant lender will tower over rivals both locally and in the region with a mega balance sheet of KShs.828 billion as per the two lenders' December 2018 disclosures. KCB Group's balance sheet stood at KShs.714 billion while NBK's stood at KShs.114 billion at the close of last year.

CHINA COULD OPEN MARKET FOR FRESH PRODUCE

China has hinted at plans to open its market for more fresh produce from Kenya following successful entry of stevia and frozen avocado. China's ambassador to Kenya, Mr. Wu Peng, said the two countries have been working on a raft of trade pacts that could relax the stringent quality demands and open the populous nation's market to Kenya's fresh avocado and horticultural products.

Last year, Beijing and Nairobi signed an agreement on the export of frozen avocados, which makes Kenya the first African country to export the commodities to China. The two states also struck a deal on export of stevia to China and have since signed an MoU on sanitary and phytosanitary (plant quality standards), which pave the way for Kenya's access of horticultural products into the Chinese market.

Q1 MILK INTAKE FALLS BY 9M LITRES AS SUPPLY SLUMPS

Milk intake in the formal market dropped by nine million litres between January and March maintaining pressure on shelf prices. Data by the Kenya Dairy Board (KDB) indicates supply to processors declined from 54 million kilos in January to 45 million kilos last month as the industry grappled with the effects of a prolonged drought. About 80% of milk in the country is sold to Kenyans unprocessed with processors only taking 20% of the entire amount.

"CMA director of regulatory policy and strategy Mr.Luke Ombara said the net foreign buying and improved financial performance mainly by listed commercial banks helped boost activities on the bourse"

USED CLOTHES IMPORTS UP A THIRD TO KSHS.17BN

Second hand clothes imports jumped 30% in 2018, marking the highest quantity shipped in more than five years at 177,160 tons valued at KShs.16.9 billion, even as apparel exports shot up. In 2017, traders spent KShs.13 billion to ship in 135,868 tons of used clothes consignments while 2016 saw 131,940 tons worth KShs.12.9 billion brought in.

Interestingly, while the market for second-hand clothes and shoes appears to be growing, 22 Kenyan apparel factories enjoyed a 25.8% increase in export sales at KShs41.6 billion from 2017's KShs.33 billion earnings. The export processing zones-based factories that employ 46,248 Kenyans shipped out men, women and children cloth wear to global retail chains including the 1,014-store JC Penney (US and Puerto Rico), Wal-Mart (US), Kohl's (US), Macy's (US), Jones New York (US), Dollar General (US) and Ross (US).

FOREIGN INVESTORS AT NSE IN 3-MONTH BUYING SPREE

Foreign investors at the Nairobi Securities Exchange (NSE) in April recorded a net buying position, extending the trend to the third straight month. Fresh data compiled by Standard Investment Bank (SIB) shows foreign investors closed April with net foreign portfolio inflow of $0.35 million (KShs.35.39 million).This, added to net buying in February and March, brings cumulative buying to KShs.1.96 billion. It deepens the reversal of back-to-back net buying that had gripped the NSE for the 16 months to January 2019.

Data from the Capital Markets Authority (CMA) shows that in the first quarter of 2019, average foreign investors' participation in the bourse was at 74.91% compared to 57.37% recorded in a similar

quarter last year. CMA director of regulatory policy and strategy Luke Ombara said the net foreign buying and improved financial performance mainly by listed commercial banks helped boost activities on the bourse. Equity turnover for the first quarter stood at KShs.45.25 billion.

TREASURY BILLS HIT KSHS.1TRN AS DEBT TENOR DROPS

Government borrowing via Treasury bills has piled up to a record KShs.1 trillion defying Debt Management Office's push to lengthen the maturity of its debt. Fresh data from Central Bank of Kenya (CBK) shows that between the last week of December and the first week of this month, stock of T-bills has increased by KShs.99.45 billion 11%.

The pace of growth is faster than the 9.5% exhibited by Treasury bonds despite the falling yields. T-bills, excluding repos, now account for 37.22% of KShs.2.74 trillion domestic debts. This defies the Treasury's medium-term debt management strategy for financial years 2018/19 to 2020/21, which intended T-bills not to be above 20%.

KSHS.300BN DEBT PAYMENT TO KICK-START NSE BOND MARKET

The secondary bonds market at the Nairobi bourse has been tipped to witness higher activity in the next two months from inflows of rising maturing debt amid expected lower appetite for new borrowing by the Government. The injection of funds from the new Eurobond issue coupled with the Government being ahead of schedule in domestic borrowing mean that State is not under pressure to borrow much from primary Treasury bill and bond issues.

In May and June, domestic debt maturities amount to KShs.170 billion and KShs.132.8 billion respectively adding up to KShs.302 billion. The rising injections from the maturing debt are already being felt in the money market. The inter-banking rate, which was rising throughout April and in the first week of May has retreated by a percentage point to 5.4 percent in the past one week, indicating that banks are increasingly holding more liquidity.

STATE BACKED MORTGAGE FIRM TO LEND AT BELOW 10%

Kenyans earning KShs.150000 and below per month are set to get house loans from local financial institutions at rates below 10% after the country launched its first secondary mortgage financier Thursday. The Kenya Mortgage Refinance Company (KMRC), a Treasury-backed lender, is expected to cut the cost of home loans to single digit from the current market rate of about 13.5%.

Kenyans who opt to buy their houses in Nairobi will qualify for loans of up to KShs.4 million with those residing outside the capital securing up to KShs.3 million. KMRC's funds will not be directly available to individual borrowers. It will lend money to financial institutions at low cost, enabling them to write home loans at single-digit rates. Borrowers of the loans will be allowed to acquire either apartments or free-standing property.

FOREIGNERS TURNOVER AT THE NSE RISES TO 75PC

Foreign investors accounted for a higher share of turnover at the Nairobi Securities Exchange (NSE) in the first four months of the year compared to the same period last year as their market sentiment turned to the buy side. Market data shows they accounted for a monthly average of 75% of traded turnover in the period, compared to 59% in the first four months of 2018.

The investors have also returned to a net inflow position this year, at KShs.813 million, compared to the KShs.9.5 billion in net outflows recorded in the four months to April 2018. The higher activity and inflows had backed the market to a 12% gain in the period to April, although most of these have been eroded in the slide that has hit the market in the past three weeks.

OWNERS OF 10% STAKE IN MICROFINANCE BANKS FACE FIRST CBK VETTING

The Central Bank of Kenya will start vetting shareholders in microfinance banks owning at least a 10% stake, if proposed regulations seeking to boost governance are adopted. The CBK says in the draft Microfinance Bill, 2019 that people holding at least 10% stake will be regarded as significant shareholders. This scripts the first time the regulator has defined a significant owner of microfinance banks, and an upgrade of the current law that only limits individual ownership at 25%.

For banks, any person holding 5% or more of the share capital is regarded as significant shareholder and is vetted by the CBK before being allowed to hold such stake. The Central Bank may require an institution to submit to it on a periodic basis, a list of current shareholders of the institution showing shares held on own account, by nominees and the individual ultimate beneficiaries of shares held by nominees or corporate shareholders. Experts reckon that it's critical for CBK to vouch for the fitness and character of owners of microfinance banks given they now control deposits in excess of KShs.40 billion.

NATIONAL SHIPPING LINE REVIVAL PLAN SIGNALS LOWER FREIGHT COSTS

The revival of the State-owned Kenya National Shipping Line (KNSL) is set to trigger price wars with foreign-owned ships with the promise to offer discounted freight charges. Maritime and Shipping Principal Secretary Nancy Karigithu told Parliament that the Government will be able to influence pricing for imports, exports and insurance premiums through discounted rates. The dormant shipping line will be revived and allowed to take over the KShs.30 billion Kenya Ports Authority second container terminals, which was opened in September 2016 and can handle about 550,000 twenty- foot containers per year

CONTINENTAL FREE TRADE PACT COMES INTO EFFECT IN JUNE

The continental free trade area will come into effect at the end of this month after two more countries ratified the agreement. The Saharawi Republic and Sierra Leone submitted their instruments of ratification to the African Union last week, making the African Continental Free Trade Area (AFCFTA) to attain the threshold for

operationalization. This in theory implies that from July, Africans will be free to trade, work and move all over within the continent without restrictions as it is the case now.

The continental free trade area was signed by close to 50 countries at the AU Summit in March 2018 with Kenya being the second member to deposit the instruments of ratification at the AU headquarters in May 2018. The continental free trade will create one African market of 1.2 billion people, with a GDP of $2.5 trillion, which has the potential to boost intra-African trade by 52% by 2020, benefiting African producers, consumers and traders.

COFFEE PRICE UP 17% IN SECOND WEEK OF GOOD RUN

The price of coffee shot up by 17% in the week ended May 17th 2019. A market report by the Nairobi Coffee Exchange (NCE) indicates that a 50-kilogramme bag of coffee fetched KShs.10300 this week up from KShs.8800 recorded previously. Officials at NCE say the marginal improvement is attributed to increased demand for the commodity at the auction during the sale. The trading also saw Kenya's premium coffee grade AA value go up to KShs.11600 a bag compared with KShs.10100 fetched previously.

Kenya Economic Outlook

DOMESTIC DEBT COST AT 69 MONTH LOW ON RATE CAPS

The Treasury's short-term borrowing costs have dropped to a 69-month low, reflecting the prevailing low interest regime touched off by legal caps on loan charges. Yields on the benchmark three-month Treasury bills fell for the sixth straight week to an average 7.25% at the auction last Thursday. That was the lowest rate since March 14 (6.84%) when the returns to investors lending cash for three months sunk to a low last seen in late July 2013.

The Central Bank of Kenya (CBK) sold the 182-day T-bills for an average 7.96%, the first time the rate has slipped below 8% since August 1, 2013 auction when it averaged 6.87%.The CBK, the government's fiscal agent, further accepted one-year bids for 9.32%, which was unchanged from the previous week's but still marked the lowest yield since the auction on July 18, 2013 (9.06%).

VALUE OF DEALS FALL BY HALF IN QUARTER ONE

The value of investment and corporate deals in East Africa nearly halved in the first quarter of the year compared to a similar period in 2018, in the absence of large ticket offerings seen the previous year. Deals data compiled by I&M Burbidge Capital shows the total disclosed value of deals in the region stood at KShs.66 billion, compared to KShs.110 billion last year.

The majority of the deals so far this year have been in Kenya—largely private equity deals, mergers and acquisitions in the health, financial services and ICT sectors—I&M Burbidge said in its East Africa Financial Review report for quarter

KENYA HEADED FOR STABLE GROWTH, HEALTHY FOREX RESERVE, SHOWS STUDY

Kenya's economic growth is likely to increase to an average of 6% throughout 2020 to 2023, according to a new report from the Economist Intelligence Unit (EIU).In a generally upbeat analysis of foreign exchange availability and commercial credit for businesses across five key sub-Saharan African economies, the London-based EIU says that key economic indicators in Kenya show that although inflation will rise to nearly 6% this year the current account deficit should narrow to below 3% by 2023.The other economies analyzed in the study are Ethiopia, Nigeria, Tanzania and Zambia.

Global Economic Outlook

GOLD PRICES ELEVATED ON FURTHER TRADE ESCALATION

Following a surprise move by President Trump to impose 5% tariffs on all Mexican goods, risk sentiment has once again been rattled with equity markets taking a fresh leg lower, most notably auto stocks with exposure to Mexico. Alongside this, China had also stepped up their trade war rhetoric with reports further hinting that China could place an export ban of rare earth materials. In turn, the uncertainty regarding trade wars has spilled into the real economy with Chinese Manufacturing PMI falling into contractionary territory overnight

SOUTH AFRICAN RAND TUMBLES TO 5-MONTH LOW ON CABINET ANXIETY

South Africa's rand tumbled to a five-month low against the dollar early on 29th this month, extending losses in the previous session as global risk aversion and uncertainty over cabinet appointments hurt sentiment. At 0648 GMT, the rand traded at 14.8575 per dollar, 0.9% weaker than its New York close on Tuesday.

The unit was trading at its weakest levels since January 3. The rand fell more than 2% on Tuesday as deputy president David Mabuza was sworn in as a lawmaker after being cleared by the ruling African National Congress of bringing the party into disrepute

FIRST-QUARTER ECONOMIC GROWTH UP 3.1%, SLIGHTLY BETTER THAN WALL STREET EXPECTED

The U.S. economy grew by 3.1% to start the year, slightly better than expected and providing some relief at a time when recession fears are accelerating.

First-quarter gross domestic product beat the 3% Dow Jones estimate but was lower than the initial 3.2% projection from the Bureau of Economic Analysis. The decrease came due to downward revisions to nonresidential fixed and private inventory investment, two key drivers to GDP.

Exports rose 4.8% amid the increasingly bitter trade war between the U.S. and China, while imports,

which are a subtraction from GDP, declined 2.5%. The level of net exports contributed nearly 1 percentage point to the GDP gain.

CONSUMER PRICE INFLATION REMAINS BELOW TARGET IN JAPAN

With consumer price inflation projected to be well below the 2 per cent target over the next two years, the Bank of Japan has indicated its intention to continue with its quantitative and qualitative monetary easing (QQE) programme. When the QQE programme was introduced in 2012, the central bank expected to achieve its inflation target by 2019. The inflation rate in March stood at just 0.5 per cent. Despite ongoing labor shortages, which have contributed to the increasing number of business closures, wage growth remains insufficient to generate inflationary pressures. In February, real wages declined by 1.1 per cent compared to last year.

SUBDUED INFLATION ON AN UPWARD TREND

Inflation remains subdued in Europe, amid increasing upward wage pressure. The euro area saw inflation rise from 0.2 per cent in 2016 to 1.5 per cent in 2017 and 1.7 per cent last year. Inflation is expected to remain steady this year, as an easing in the upward pressure from energy prices is offset by increasing pressures on the domestic side. Employment has been increasing throughout the region, with unemployment falling to the point where in some sub-regions there is a shortage of labour. This is propelling stronger wage growth, which in turn is supporting domestic demand. As monetary policy is expected to remain more accommodative for a longer period than previously expected, this will continue to support investment and the construction sector in various countries. However, overall economic activity has slowed across the region as a result of the disruption in auto production, weaker confidence, and softer external demand. Inflation is forecast to remain within the ECB's policy target of below, but close to, 2 per cent.

Persistent labor shortages in countries that joined the European Union since 2004 spurred strong growth in nominal wages in 2018; in early 2019 this trend continued, threatening several economies with a wage-price spiral. In the Czech Republic, headline inflation reached 2.7 per cent in February, and contrary to global easing trend some central banks in the region may tighten monetary policy further this year.

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