PESA Editorial

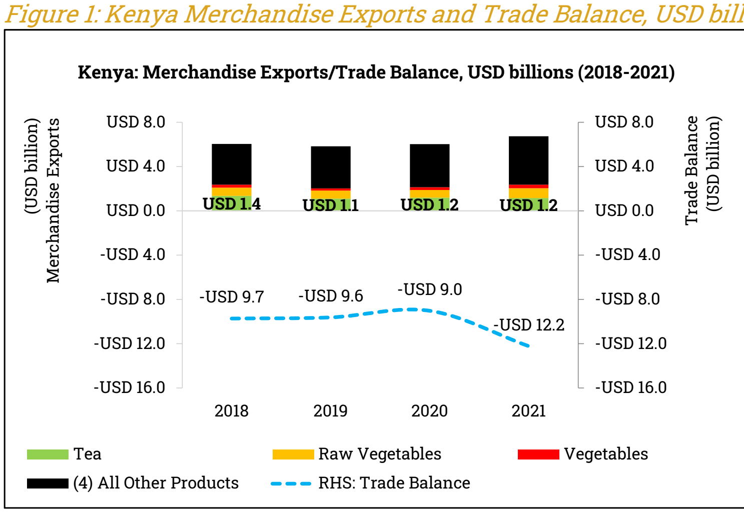
Republic of Kenya

2H2022/23

Accurate and balanced analysis of the political economy in Kenya.

Kenya's exports have had a slower growth rate since the recovery from the shock caused by the COVID-19 pandemic. The country's total merchandise exports recovered to USD 6.8 billion in 2021. Kenya has a relatively diversified export profile and earnings from tea have continued decreasing to USD 1.2 billion (approx. 17.2% of total exports) in 2021. Other top exports from Kenya include raw and processed vegetables. These exports contributed USD 1.2 billion (approx. 17.8% of total exports). Kenya's export earnings from raw vegetables have continued increasing to USD 886.2 million in 2021; and earnings from processed vegetables have continued increasing to USD 315.9 million in the same period. Kenya's trade deficit continued widening beyond the historical medium-term average of -USD 9.5 billion for 2018 to 2020, to -USD 12.2 billion in 2021.

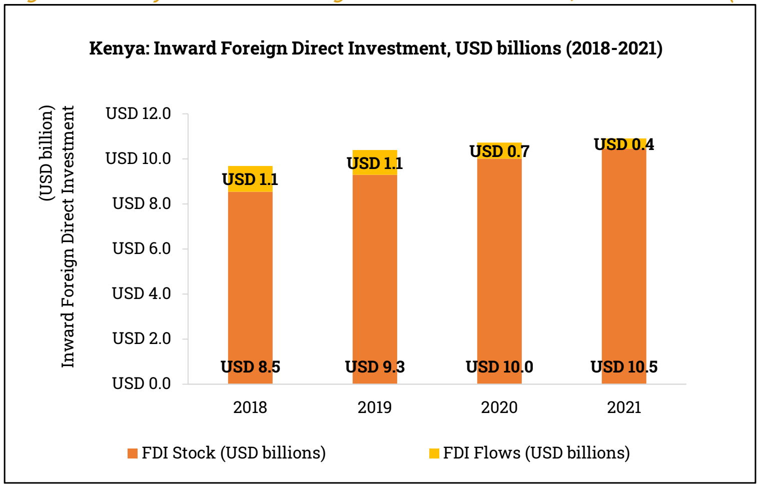
Figure 1: Kenya Merchandise Exports and Trade Balance, USD billions (2018-2021)



Source(s): UNCTAD 2023, *UNCTADStat Database*, United Nations Conference on Trade and Development: Geneva. Available At: https://unctadstat.unctad.org/ [Last Accessed: 1 February 2023].

Total merchandise export earnings have continued increasing which relieved the pressure caused by the reduced net FDI inflows (foreign capital being invested domestically). Kenya's FDI inflows decreased to USD 448.1 million in 2021. Nonetheless, Kenya's FDI stock has gradually continued increasing from an annual average of USD 9.3 billion for 2018 to 2020 to USD 10.5 billion in 2021. This does not bode well for Kenya as a country that is aiming to attract more foreign investment to diversify its economy away from the reliance on tea exports. However, this could also signify the limited economic opportunities in the economy, which would signify slow progress for the national economic diversification strategy.

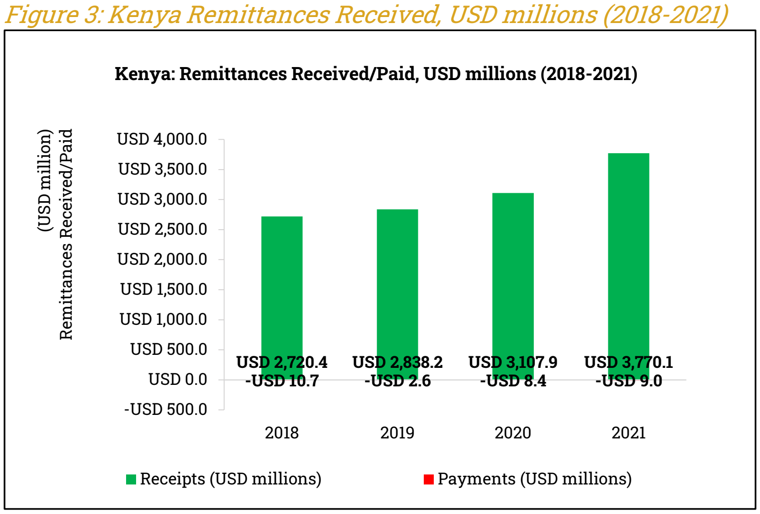
Figure 2: Kenya Inward Foreign Direct Investment, USD billions (2018-2021)



Sources: UNCTAD 2023, *UNCTADStat Database*.

Remittances receipts have grown consistently over the period. Personal remittances received have been seemingly unaffected by COVID-19 and continued increasing from an annual average of USD 2.9 billion for 2018 to 2020 to USD 3.8 billion in 2021. Personal remittance payments to foreign nationals have been seemingly unaffected by COVID-19 and continued increasing from an annual average of USD 7.2 million for 2018 to 2020 to USD 9.0 million in 2021. Kenya has had net remittance inflows (net remittance receipts from the diaspora) which increased to USD 3.8 billion in 2021. This has affected the current account balance and strength of the KES over the period.

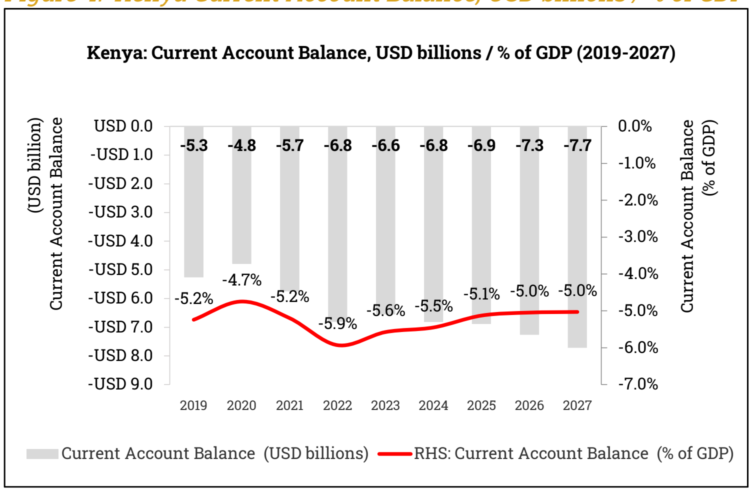
Figure 3: Kenya Remittances Received, USD millions (2018-2021)



Sources: UNCTAD 2023, *UNCTADStat Database*.

The KES has begun depreciating. In nominal terms, the KES has been very stable at an average appreciation of 0.2% against the USD for 2018 to 2020. The KES depreciated by -5.7% to an annual average of KES 109.6 per USD in 2021. Kenya's current account deficit continued widening beyond the historical medium-term average. In 2022, Kenya's current account deficit continued widening. In particular, Kenya seems to have been affected by the extensive drought affecting the Horn of Africa region which has deteriorated its agricultural output and exports. This has offset the positive impact of the rising global price of Kenyan tea which appreciated by 4.1% to USD 2.8 per kilogram in 2022 (2021: +5.2%; USD 2.7 per kg). In addition, Kenya has been affected by the higher fuel and food prices which continued appreciating due to lower global supply following the sanctions against Russian exports after its military exercises in Ukraine. This is also reflected in the projections for Kenya's current account balance.

Figure 4: Kenya Current Account Balance, USD billions / % of GDP (2019-2027)



Sources: IMF 2022, *World Economic Outlook Database: October 2022*, International Monetary Fund: Washington, D.C. Available At: https://www.imf.org/ Last Accessed: 1 February 2023]. **Note:** (*) Figures from 2021 onwards are projections from the IMF, 2022.

In 2023, Kenya's current account deficit is projected to narrow to -USD 6.6 billion (approx. -5.6% of GDP) despite being wider than the historical medium-term average. In the medium-term from 2024 to 2026, Kenya's current account deficit is projected to continue widening in nominal terms, to an annual average of USD -7.0 billion (approx. -5.2% of GDP). This illustrates a persistent deterioration in the current account balance due to the current adverse climatic conditions; and the rising cost of crucial food and fuel imports which is primarily driven by the impact of sanctions against Russia. Global food and fuel prices are expected to remain relatively elevated in 2023. However, this could change in the medium-term due to the expected easing of geopolitical tensions and the gradual transition away from fossil fuels. Therefore, Kenyan authorities are still faced with difficult times ahead. The uncertainty of climatic conditions and the reliance on agricultural export means that the drought could affect macroeconomic stability if the adverse climate conditions persist.

The issue of diversifying the Kenyan economy remains an elusive obstacle for the country. Kenya still has a significant potential to grow its exports from raw vegetables and vegetables. These represent the highest growth potential towards diversifying the Kenya's economy and export earnings. However, Kenyan need to develop their food processing as a means to increase domestic value-addition to its agricultural exports. Apart from this, Kenya should also deepen its integration in the COMESA and EAC regions and increase its intra-regional trade. This will provide an opportunity for Kenya's exports to compete against goods and services of comparable quality from the local regions. Moreover, Kenya can offset the risks with its traditional export markets by increasing its dependence on the local regions for its exports.

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Note:
In this publication, "KES" refers to Kenyan Shilling and "USD" refers to US Dollars. Unless otherwise indicated, all percentage comparisons are year-on-year.

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