

# Kenya Business Forecast Report Q2 2014

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## Abstracts

### Core Views

The International Criminal Court investigation targeting President Uhuru Kenyatta created fears of a political crisis between the court and African states that accuse it of bias, but we believe this is unlikely.

The case has been suspended for technical reasons, and a lack of evidence may lead to its cancellation. Even if restarted, we believe that a compromise will avoid a stand-off between the court and the African Union.

Kenya's economy will accelerate in 2014, growing by 6.1% in real terms. This will be Kenya's fastest rate of GDP expansion since 2007, and BMI believes that growth will stabilise near 6.0% between 2014 and 2018. Rapid economic growth in the other East African Community states will spur demand for Kenyan goods and services.

Inflation will remain restrained over 2014 due to lower energy prices and a firming shilling. Slightly faster price growth is likely later in the year, however, due to rising food prices.

A reduction in Kenya's trade deficit and strong service sector growth will cause the country's wide current account deficit to narrow from 8.7% of GDP in 2014 to 6.0% in 2018. Capital and financial inflows will keep the deficit covered, though we note that a dependence on short-term investment inflows leaves the economy vulnerable to external shocks.

Accelerating economic growth will increase government revenue, but we expect rising public spending to keep pressure on Kenya's fiscal balance. The country's budget deficit will narrow in 2013/2014 compared to 2012/2013, but will remain approximately

7.0% of GDP for the duration of our forecast.

### **Major Forecast Changes**

Climactic factors pose a serious risk to Kenya's agricultural production; poor rains would harm economic growth, spur high inflation, and also necessitate large-scale food imports, putting pressure on the already stretched balance of payments position.

While not our key forecast, a political crisis caused by Uhuru Kenyatta's refusal to appear at his trial could seriously strain Kenya's relationship with Western powers.

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### CHAPTER 1: POLITICAL OUTLOOK

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Kenyatta Prosecution Unlikely To Go Ahead

A lack of valid evidence has led the International Criminal Court to postpone its prosecution of Kenyan President Uhuru Kenyatta, and we doubt that the controversial trial will be restarted in 2014. Prosecutors allege that their witnesses are being deterred from testifying by a campaign of intimidation, a charge that the president's supporters deny. The trial's collapse would prevent a political clash between the ICC and African states that accuse it of bias.

Table: Political Overview

Long-Term Political Outlook

Ethnic Polarisation Remains Key Challenge

Despite the terrorist attack on the Westgate shopping centre, the politicisation of sharp ethnic divisions remains the key threat to Kenya's long-term political stability. Although the 2013 elections were peaceful, voting patterns show that the electorate continues to cast ballots according to ethnicity. Meanwhile, President Uhuru Kenyatta, elected in 2013, is facing charges at the International Criminal Court. This will complicate the country's relations with the West. Terrorism linked to Kenya's military involvement in Somalia is likely to remain a risk, but it does not pose a systemic threat to political stability.

### CHAPTER 2: ECONOMIC OUTLOOK

SWOT Analysis  
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Growth Moving Up A Gear

Below-expectations GDP expansion in H213 has not led us to adjust our growth forecasts for 2014, and we still see Kenya's economy expanding by 6.1%. The country's economic acceleration will gain momentum over the year, and we believe growth will

stabilise around 6.0% over the duration of our 2014-2018 forecast period.

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Price growth in Kenya has been slowing since October 2013, and we believe that year-on-year inflation in East Africa's largest economy will remain constrained in Q114. A strong shilling and lower energy prices will prevent a major uptick in inflation, but higher food and transportation costs could cause price growth to accelerate later in the year.

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A reduction in Kenya's trade deficit and strong service sector growth will cause the country's wide current account deficit to narrow from 8.7% of GDP in 2014 to 6.0% in 2018. Capital and financial inflows will keep the deficit covered, though we note that a dependence on short-term investment inflows leaves the economy vulnerable to external shocks.

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Accelerating economic growth will increase government revenue, but we expect rising public spending to keep pressure on Kenya's fiscal balance. The country's budget deficit will narrow in 2013/2014 compared to 2012/2013, but will remain approximately 7.0% of GDP for the duration of our forecast. The creation of 47 county-level governments poses a significant risk to budget discipline

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