Global economy enters 2018 from a position of strength

### Economics

**Global growth** of 3.9% in 2017 would be the fastest since 2011, and there are signs of further modest acceleration into early 2018

**Growth looks to be largely synchronised**, suggesting a resilient recovery

**Positive momentum** across confidence indices, manufacturing output and global trade

**Labour markets are tightening**, but core inflation so far remains comfortable

### Markets

**Global equities supported**, provided economic growth continues to drive profits

**US Fed signalling more hikes than market is pricing. Treasuries under pressure?**

**ECB to tighten**, ceasing asset purchases by Q3 – first hike late this year?

**EM priced to perfection?** Be wary the impact of a recovering dollar

### Key risks

**US policy uncertainty and Trump factor**

**European politics:** Brexit deadlines, German coalition, Italian election, Catalonia

**China’s ongoing adjustment**

**Geopolitics**

Source: Absa Research
SSA’s evolving economic outlook

Africa Rising
- Commodity tailwind
- Debt relief and releveraging
- Infrastructure

The perfect storm
- Over-reliance on commodities
- Policy “panic” / own goals
- FX pressure / monetary restrictions
- Fiscal rebalancing
- Drought

Source: IMF, Absa Research
Sub-Saharan Africa: How the new norm stacks up

Benchmarking SSA’s economic outlook

<table>
<thead>
<tr>
<th>2018 growth</th>
<th># SSA</th>
<th>%</th>
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<tbody>
<tr>
<td>&gt;5%</td>
<td>17</td>
<td>38</td>
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</table>

Source: Absa Research, IMF
Risks to be mindful of

Macro imbalances

Fiscal rebalancing
Debt sustainability
Infrastructure pay-off
Diversifying economies

Current account bal. (% GDP, 2018)

Fiscal bal. (% GDP, 2018)

Source: Bloomberg, IMF, Absa Research

Public debt (%GDP)

SSA credit rating

Source: Bloomberg, IMF, Absa Research
## Risks to be mindful of

### Policy uncertainty
- Angola
- Mozambique
- Nigeria
- Tanzania
- South Africa
- Zambia

### Political strain
- Ethiopia
- Kenya
- Tanzania
- Uganda
- Zambia
- Zimbabwe

### Global environment
- Politics of rage
- US policy uncertainty
- Brexit and Africa trade
- China’s adjustment
- Commodity demand
- Geopolitics

Source: Absa Research
The sharp FX deteriorations of 2016 have slowed

FX has generally depreciated in 2017, but at a slower pace

Value, per USD, Jan 2015 = 100

Source: Bloomberg, Absa Research
Recent trends in FDI flows into Africa

In $ terms, FDI into Africa has recovered

Largest sources of FDI

<table>
<thead>
<tr>
<th>#</th>
<th>$bn</th>
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<tbody>
<tr>
<td>US</td>
<td>91</td>
</tr>
<tr>
<td>France</td>
<td>81</td>
</tr>
<tr>
<td>China</td>
<td>66</td>
</tr>
<tr>
<td>UK</td>
<td>41</td>
</tr>
<tr>
<td>UAE</td>
<td>35</td>
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<td>S Africa</td>
<td>29</td>
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<tr>
<td>Japan</td>
<td>27</td>
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<tr>
<td>SZ</td>
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<tr>
<td>Spain</td>
<td>23</td>
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<td>Italy</td>
<td>20</td>
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<tr>
<td>Germany</td>
<td>19</td>
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<tr>
<td>India</td>
<td>18</td>
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<tr>
<td>Morocco</td>
<td>17</td>
</tr>
</tbody>
</table>

Source: EY Attractiveness Program Africa (May 2017), Absa Research
Recent trends in FDI flows into Africa

Where the FDI is going

- **Algeria (15)**: 17 projects
- **Tunisia (13)**: 18 projects
- **Tanzania (5)**: 22 projects
- **Ghana (4)**: 28 projects
- **C D'Ivoire (7)**: 34 projects
- **Kenya (2)**: 40 projects
- **Nigeria (17)**: 51 projects
- **Egypt (11)**: 79 projects
- **Morocco (1)**: 81 projects
- **S Africa (2)**: 139 projects

Source: EY Attractiveness Program Africa (May 2017), Absa Research
The effect of temperature on GDP per capita

Estimating the impact of a 1°C increase in temperature on economic activity

- Variance within a country
- Variance between countries
- Effects are non-linear
- Cool countries – generally helpful
- Warm countries – generally negative

Many low- and middle-income countries have little adaption capacity

Source: IMF World Economic Outlook (October 2017, chapter 3), Absa Research
Climate change will likely disproportionally impact Africa

Source: IMF World Economic Outlook (October 2017, chapter 3), Absa Research
The Barclays Africa Group Financial Markets Index

Discussing the openness, transparency and “attractiveness” of Africa’s financial markets

6 Pillars inform the discussion

Market depth – Products, market size, liquidity and depth

Access to FX – FX liquidity, capital restrictions, FX reporting, reserves sufficiency

Market transparency – Basel, accounting standards, tax environment, market reporting, ratings, minorities

Capacity of local investors – Pensions and local asset managers

Macro opportunity – Economic growth, competitiveness, data standards, budgets/MPC transparency, debt profile

Enforceability of agreements – Insolvency framework, netting and collateral positions, use of standard agreements

Source: Barclays Africa Group Financial Markets Index 2017, Absa Research
Political calm and improved weather prospects should lead a recovery in growth in 2018

Construction and Agriculture moving in opposite directions

Contribution to GDP growth by expenditure

Source: CBK, KNBS, Absa Research
Recovery in PMI is dramatic

Whole-economy PMI shows the concern – and relief

Source: Bloomberg, Markit
Tourism and agriculture contributing positively

Tourism arrivals resilient and receipts moving gradually higher

Agri export crops in context

Source: CBK, KNBS, Absa Research
Infrastructure still very much a theme

First phase of SGR delivered, but still much in the works.

Energy projects:
- Wind, solar, geothermal

Ports and airports:
- Lamu Port Project
- Embu International Airport,

Rail and Road:
- Phase 2 of SGR
- Road rehabilitation projects

Investment remains buoyant

Source: National Treasury, CBK, KNBS, Absa Research

16 January 2018
Credit rating agencies are watching the fundamentals

In October Moody’s placed Kenya’s B1 long-term issuer rating on review for downgrade.

Key drivers:

Persistent large primary deficits and high borrowing costs

Government liquidity pressure risk due to increasingly large financing needs.

Uncertainty over the direction of fiscal and economic policy, in part due to evolving political dynamics.

S&P’s October review actually upgraded the outlook from negative to stable

Source: Moody’s, S&P, Fitch, Bloomberg, Absa Research
Debt burden has increased sharply over the past five years

Fiscal deficit is large (and sticky)

Debt servicing as a focus

Source: National Treasury, CBK, Absa Research
Credit growth stalled

*Interest rate caps have been implemented in many periods over many countries*

Work by the IMF looking across countries suggest that the impact tends to be:

- Reduced access to finance for small borrowers
- Increase in (costly) informal lending
- Reduced transparency
- Reduced competition and innovation in the financial sector
- Adverse impact on financial inclusion
- Reduced monetary policy effectiveness

Source: IMF, CBK, Absa Research
CBK considerations

“...inflationary pressures in the economy were muted, and inflation was expected to continue to decline in the short term.” – CBK

Oil prices, cuts to subsidies are upside inflation risks

“The MPC continues to monitor the impact of the interest rate caps on the effective transmission of monetary policy.” - Patrick Njoroge

Cutting its policy rate may be ineffective due to the transmission challenges brought about by the interest rate capping law.

MPC probably wont adjust its policy rate until the rate cap is amended.

Source: CBK, Absa Research
External accounts suggest modest KES moves

Wider current account deficit

Financial account (USD bn)

We see KES at 106 by year-end

Source: CBK, Absa Research
## Forecasts

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<tbody>
<tr>
<td>Real GDP (% y/y)</td>
<td>5.4</td>
<td>5.7</td>
<td>5.9</td>
<td>4.6</td>
<td>5.5</td>
<td>5.9</td>
<td>6.2</td>
</tr>
<tr>
<td>GDP (USD bn)</td>
<td>61.4</td>
<td>63.8</td>
<td>70.5</td>
<td>76.7</td>
<td>83.6</td>
<td>90.8</td>
<td>99.5</td>
</tr>
<tr>
<td>Current account balance (% GDP)</td>
<td>-9.9</td>
<td>-6.9</td>
<td>-5.2</td>
<td>-6.8</td>
<td>-7.0</td>
<td>-7.1</td>
<td>-7.2</td>
</tr>
<tr>
<td>Gross reserves (USD bn)</td>
<td>7.5</td>
<td>7.1</td>
<td>7.0</td>
<td>7.1</td>
<td>7.8</td>
<td>8.0</td>
<td>7.9</td>
</tr>
<tr>
<td>Months of imports</td>
<td>4.0</td>
<td>4.2</td>
<td>5.5</td>
<td>4.9</td>
<td>4.6</td>
<td>4.1</td>
<td>3.8</td>
</tr>
<tr>
<td>Fiscal balance (% GDP)</td>
<td>-5.4</td>
<td>-8.7</td>
<td>-8.0</td>
<td>-8.8</td>
<td>-7.1</td>
<td>-5.6</td>
<td>-5.8</td>
</tr>
<tr>
<td>Public debt (% GDP)</td>
<td>54.6</td>
<td>48.4</td>
<td>53.9</td>
<td>60.7</td>
<td>61.3</td>
<td>62.0</td>
<td>62.6</td>
</tr>
<tr>
<td>CPI (% Dec/Dec)</td>
<td>6.0</td>
<td>8.0</td>
<td>6.4</td>
<td>4.5</td>
<td>6.2</td>
<td>5.8</td>
<td>6.1</td>
</tr>
<tr>
<td>USD/KES (eop)</td>
<td>90.6</td>
<td>102.3</td>
<td>102.5</td>
<td>103.2</td>
<td>106.0</td>
<td>108.5</td>
<td>110.8</td>
</tr>
</tbody>
</table>

Source: CBK, Treasury, KNBS, Absa Research
Q&A

Jeff Gable
Chief Economist
jeff.gable@absacapital.com
Absa, South Africa
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