



REPUBLIC OF KENYA
THE NATIONAL TREASURY AND PLANNING

NOTICE TO THE CENTRAL BANK OF KENYA ON THE PRICE STABILITY TARGET AND THE ECONOMIC POLICY OF THE GOVERNMENT FOR THE FINANCIAL YEAR 2020/21 BUDGET

As you are aware, the principal objectives of the Central Bank of Kenya (CBK) as captured under section 4 (subsections 1-3) of the Central Bank of Kenya Act, 2015, are:

1. To formulate and implement monetary policy directed to achieving and maintaining stability in the general level of prices;
2. To foster the liquidity, solvency and proper functioning of a stable market-based financial system; and
3. Subject to subsections (1) and (2), to support the economic policy of the Government, including its objectives for growth and employment.

In addition, subsections 4 and 5 provide that the Cabinet Secretary responsible for Finance shall specify at least once in every period of 12 months:

- a. The price stability target of the Government, in consultations with the Central Bank; and,
- b. Economic policy to be taken by the Government.

Further, under subsection 6, the Act requires the Cabinet Secretary to publish the Price Stability Notice in such a manner he considers fit and lay a copy of the Notice before the appropriate Committee of the National Assembly.

In compliance with the provisions of the CBK Act (2015), this notification sets out the price stability target and the economic policy to be undertaken by the Government in the FY 2020/21 as follows:

A. Price Stability Target

The inflation target shall be 5.0 percent, with a flexible margin of 2.5 percent on either side in the event of adverse shocks. This inflation target will be measured by the 12-month change in the Consumer Price Index (CPI) as published by the Kenya National Bureau of Statistics (KNBS). The inflation target is in line with the macroeconomic targets underpinning the FY 2020/21 budget and that of the Medium-Term Expenditure Framework (MTEF) period. The macroeconomic targets underpin the economic policies of the Government as detailed in the 2020 Budget Policy Statement and were developed by the inter-agency Macro Working Group while preparing the expenditure ceilings for the FY 2020/21 budget.

The Central Bank of Kenya (CBK) is therefore expected to achieve this inflation target and will be accountable to the Government and the general public for its attainment. Achieving this target will help preserve macroeconomic stability and reduce undesirable fluctuations in economic performance. The flexible margin of 2.5 percent on either side of the inflation target is to cater for effects of external shocks such as the adverse effects of the Covid-19 Pandemic and oil price variations. Domestically, shocks may emanate from rapid and severe changes in weather conditions that would affect agricultural output.

In the event that inflation rate published by KNBS, deviates from the target by more than 2.5 percentage points in either direction, the CBK will provide a letter indicating:

- i. The factors driving inflation away from the specified target by more than 2.5 percentage points in either direction;
- ii. The measure(s) which the CBK is taking to address the deviation; and
- iii. The time period within which the CBK expects inflation to return to the target.

A copy of this Notice will be shared with the appropriate Committee of the National Assembly, and in case of deviation from target, CBK will be expected to share a copy of the letter explaining the deviation to the Chairperson of the same Committee. If the deviation persists for three consecutive months after the initial letter, CBK will be expected to send another letter further explaining the deviation from the target.

In assessing the inflation developments, the Government will consider the prevailing economic conditions at the time.

B. Economic Policy to be taken by the Government

The economic policy of the Government in the FY 2020/21 budget draws from the national development agenda [Third Medium Term Plan (MTP III) of the Vision 2030] as detailed in the 2020 Budget Policy Statement and adjusted through the Budget Estimates as approved by Parliament in June 2020. The finalization of the FY 2020/21 budget was against a backdrop of a contracting global economy with severe economic disruptions occasioned by the Covid-19 Pandemic. The Pandemic has devastated many countries causing interruptions to global production, supply chains, trade flows, volatility in financial markets and tightening of global financial market conditions. Consequently, global growth is projected to contract by -4.9 percent in 2020. At the domestic scene, growth of Kenya's economy in 2020 is projected to decline to 2.5 percent from 5.4 percent in 2019 following the adverse impact of the Covid-19 Pandemic that severely affected most sectors of the economy. The various containment measures implemented by the Government that included restriction of movements into and out of some counties and night time curfew similarly affected economic activity.

In order to minimize the adverse effects of the pandemic on people and businesses, the Government outlined various fiscal and monetary policy measures. In addition, the Government through the FY 2020/21 budget will implement an Economic Stimulus Programme to stimulate economic activities in order to safeguard livelihoods, jobs, businesses and support industrial recovery. The Government is also developing a comprehensive Post-Covid-19 Economic Recovery Strategy that will re-position the economy on a steady and sustainable growth trajectory after the Pandemic.

Therefore, economic policy is tuned to support these Government initiatives including implementation of the priority "Big Four" Agenda. The Government will also continue to provide a conducive environment for the private sector to thrive by preserving macroeconomic stability, expanding infrastructure, improving security, implementing business regulatory reforms, expanding access to finance and instituting governance reforms.

To improve the business environment, macroeconomic stability and in particular price stability remain critical enablers. The fiscal policy underpinning the FY 2020/21 budget and that of the MTEF period will target to gradually reduce the fiscal deficit so as to stabilize growth of public debt and create fiscal space to fund Government programmes. This will in the process complement the monetary policy of the Bank. The fiscal deficit is projected to decline from 7.8 percent of GDP in FY 2018/19 to 7.5 percent of GDP in FY 2020/21 and below 4.0 percent of GDP over the medium term. The fiscal consolidation plan will be supported by revenue mobilization and rationalization of non-core expenditures particularly recurrent.

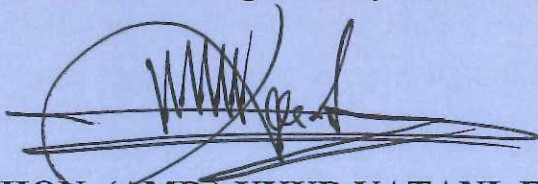
The above policy was outlined in the Budget Statement delivered to the National Assembly on 11th June 2020. It is therefore expected that the CBK will maintain inflation within the target range during the FY 2020/21 budget period.

Accountability

The Central Bank of Kenya and the Monetary Policy Committee is accountable to the Government for the price stability target set out in this Notice. In this respect, the accountability framework in terms of regular reporting will remain as outlined in sections 4B, 4C and 4D of the CBK Act, 2015. The format of reporting to the National Assembly remains as previously stated.

Revision of the Target

The revision of the inflation target will be set out in the budget for the FY 2021/22 and will take into account updates of the Government's economic policy objectives in the 2021 Budget Policy Statement.



HON. (AMB.) UKUR YATANI, E.G.H.

CABINET SECRETARY/THE NATIONAL TREASURY AND PLANNING

July 6, 2020