

## AFRICA RISK CONSULTING

### Kenya Monthly Briefing March 2018

#### Kenya Summary 5 March 2018

*President Uhuru Kenyatta (2013-present) completes the appointment of his cabinet, promoting his allies to strategic posts and marginalising those of deputy president William Ruto. Kenyatta does not include members of the opposition National Super Alliance (NASA). The increasingly divided NASA fails to hold a planned National People's Convention amid calls for a national referendum on governance reforms. Kenya successfully lists a \$2 billion Eurobond at competitive yields despite a Moody's Investors Service downgrade and Kenya's failure to disclose that it lost access to its \$1.5 billion International Monetary Fund (IMF) standby credit facility.*

#### Kenyatta completes second-term cabinet appointments

President **Uhuru Kenyatta** (2013-present) completed the appointment of his cabinet with the swearing in of nine new cabinet secretaries on 16 February.<sup>1</sup> The cabinet appointments suggest that Kenyatta is looking to consolidate power at the expense of his deputy president and probable successor, **William Ruto**. Kenyatta has tasked the new cabinet appointments with delivering his ambitious five-year '**Big Four**' policy priorities.<sup>2</sup> Kenyatta set out the 'Big Four' initiative after his inauguration in November 2017. The 'Big Four' comprises projects that will improve national and food security, create 500,000 affordable homes, increase manufacturing capacity, and deliver affordable healthcare through broadened **National Hospital Insurance Fund (NHIF)** coverage.<sup>3</sup> Kenyatta has placed close allies at the top of ministries central to the 'Big Four'.

*"This move has resulted in Kenyatta snatching some ministries from Ruto and in so doing, breaking away from the unwritten gentleman's agreement that saw the two leaders split ministries on a 50-50 basis in 2013."<sup>4</sup>*

In the **Jubilee Alliance** government's first term between 2013 and 2017, Kenyatta's **National Alliance Party (TNA)** and Ruto's **United Republican Party (URP)** split ministries.<sup>5</sup> During appointments in the first term, Kenyatta and Ruto announced the new cabinet jointly in an elaborate ceremony that conveyed the idea of a genuine partnership.<sup>6</sup> However, there was no joint ceremony to announce the newly appointed cabinet.

The agriculture ministry, which was headed by Ruto's close ally, **Willy Bet**, is now under **Mwangi Kiunjuri**, a politician from Kenyatta's **Kikuyu** ethnic group.<sup>7</sup> The former energy cabinet secretary, **Davis Chirchir**, a confidante of Ruto,<sup>8</sup> was not amongst the new appointees. Ruto allies who remain in the cabinet have "*had their wings clipped.*"<sup>9</sup> The lands cabinet secretary, **Farida Karoney**, has lost responsibility for housing, which was unbundled from the lands ministry and transferred to the transport and infrastructure development ministry, which remains under **James Macharia**, a close

<sup>1</sup> Standard, 18 Feb 2018.

<sup>2</sup> Standard, 18 Feb 2018.

<sup>3</sup> Kenya presidency, 13 Dec 2017.

<sup>4</sup> Source, journalist, Nairobi.

<sup>5</sup> Source, Kenya analyst, UK.

<sup>6</sup> Source, Kenya analyst, UK.

<sup>7</sup> Source, journalist, Nairobi.

<sup>8</sup> Source, journalist, Nairobi.

<sup>9</sup> Source, journalist, Nairobi.

ally of Kenyatta.<sup>10</sup> **Fred Matiang'i**, a politically powerful confidante of Kenyatta, remains the interior and government coordination cabinet secretary.<sup>11</sup> The transport and infrastructure development and interior ministries have a combined budget of \$5 billion, representing approximately a quarter of the total national budget, highlighting their significance to the delivery of the 'Big Four'.

Kenyatta also used new appointments to the cabinet to reward politicians who were instrumental in the ruling **Jubilee Party's** victory in the 2017 election. **Rashid Mohammed Achesa** was appointed the sports cabinet secretary.<sup>12</sup> Achesa is a former boxer who was pivotal to the Jubilee Party's inroads in the opposition strongholds of western **Kenya**.<sup>13</sup> The **East African Community** and **Northern Corridor** development cabinet secretary, **Peter Munya**, is the former **Meru County** governor, who was appointed to reward Meru voters who overwhelmingly backed the Jubilee Party. The new labour minister, **Ukur Yatani**, was the former **Marsabit County** governor who lost his governorship during the last election. Yatani's appointment was also to reward Marsabit voters for backing the Jubilee Party.<sup>14</sup>

There is popular scepticism about whether the cabinet secretary appointments can deliver the promise of the 'Big Four'.

*"During his first term, Kenyatta announced grand projects including the **Galana-Kulalu 1.2-million-acre Irrigation Scheme and Food Security Project** that came to naught. There was also the school laptop project that was marred by tender wars from the onset. The **Standard Gauge Railway (SGR)**, Kenya's biggest infrastructure project at \$4 billion, is yet to become popular with transporters despite repeated pledges that the train would cut transportation costs and thereby direct cargo from trucks to the rail."<sup>15</sup>*

Parliament approved the new cabinet secretaries on 14 February after opposition **National Super Alliance (NASA)** members of parliament boycotted the nomination debate.<sup>16</sup> Jubilee's majority meant the boycott did not impact the nomination process. This suggests Kenyatta should be able to force through the necessary policies to enact the 'Big Four' even if the NASA continues to boycott the political process in protest at proven electoral mismanagement and unsubstantiated allegations of electoral fraud during Kenyatta's electoral victory.<sup>17</sup>

Tension between Kenyatta and Ruto will provide the backdrop for Kenyatta's second and constitutionally final term ahead of the 2022 election. The issue of succession has an ethnic hue, with Ruto's ethnic **Kalenjin** increasingly dissatisfied with Ruto's failure to secure government appointments and contracts and a perception that Ruto has made too many concessions to Kenyatta and his Kikuyu.<sup>18</sup>

### The NASA calls for referendum on governance reforms

The NASA called for a referendum on governance reforms on 10 February.<sup>19</sup> The NASA does not have the parliamentary numbers needed to secure a referendum, suggesting the opposition roadmap is unlikely to succeed. The NASA said the opposition would hold a **National People's Convention** on 28 February to agree on political reforms to the structure of elections, the national government and devolution.<sup>20</sup> However, the NASA failed to hold the scheduled convention, apparently due to the

<sup>10</sup> Source, journalist, Nairobi.

<sup>11</sup> Source, journalist, Nairobi.

<sup>12</sup> Standard, 18 Feb 2018.

<sup>13</sup> Source, journalist, Nairobi.

<sup>14</sup> Source, journalist, Nairobi.

<sup>15</sup> Source, journalist, Nairobi.

<sup>16</sup> Citizen TV, 15 Feb 2018.

<sup>17</sup> Source, Kenya analyst, UK.

<sup>18</sup> Source, journalist, Nairobi.

<sup>19</sup> The East African, 12 Feb 2018.

<sup>20</sup> The East African, 12 Feb 2018.

opposition of senior officials aligned to deputy leader **Kalonzo Musyoka**.<sup>21</sup> Once the NASA holds its convention, it plans to refer its resolutions to referendum.<sup>22</sup> The NASA suggested it would bypass parliament whose approval is required for the holding of an official referendum. NASA strategist **David Ndi** said the coalition would use the "power of the people" to secure the referendum.<sup>23</sup> Ndi did not provide additional details but said,

*"We are not doing legal things, we are doing legitimate things."*<sup>24</sup>

On the same day as the NASA set out its referendum plans, foreign diplomats including **United States (US)** ambassador **Robert Godec**, **United Kingdom (UK)** high commissioner **Nic Hailey**, and **Canada** high commissioner **Sara Hradecky** called on NASA leader and defeated presidential candidate **Raila Odinga** to recognise Kenyatta as Kenya's legitimately elected president.<sup>25</sup> The diplomats warned Odinga that his obstructionist stance risks jeopardising his political legacy.<sup>26</sup> Odinga rejected their intercession:

*"We want to tell them in clear terms that Kenya is an independent country and the problems of Kenya will be solved by Kenyans themselves. They can only be but observers. Their only interest is to do business at the behest of their countries. They are not interested in our democracy."*<sup>27</sup>

Odinga's antagonistic response to Kenyatta's election victory has divided the opposition thereby reducing the incentive for Kenyatta to include opposition members in his new cabinet. Kenya will remain politically polarised unless Odinga loses his leadership of the NASA.

### Kenya issues \$2 billion Eurobond despite concerns about debt sustainability

Kenya successfully listed a \$2 billion Eurobond at competitive yields on the **London Stock Exchange** on 21 February.<sup>28</sup> The successful issuance shows investor confidence despite several blows to its public financial management credibility. Kenya received a \$14 billion order book.<sup>29</sup> The Eurobond was two-tranche: \$1 billion in 10-year notes with a yield of 7.25%, and \$1 billion in 30-year notes with a yield of 8.25%.<sup>30</sup> Kenyatta pledged to use the funds judiciously, after the opposition accused the government of mismanagement and fraud related to funds from the \$2 billion Eurobond issuance in 2014.<sup>31</sup> Regional media has, however, already criticised the treasury cabinet secretary, **Henry Rotich**, for a lack of transparency due to his refusal to publish a prospectus for the Eurobond.<sup>32</sup>

The successful issuance was despite **Moody's Investors Service** downgrading Kenya's issuer rating from B1 to B2 with a stable outlook on 13 February.<sup>33</sup> Moody's had started a downgrade review in October 2017.<sup>34</sup> Moody's warned about a deterioration in Kenya's fiscal position due to increased debt levels and deteriorated debt affordability.<sup>35</sup> Moody's forecast that government debt will increase from 41% of gross domestic product (GDP) in 2011/2012, to 56% of GDP in 2016/2017, and 61% in 2018/2019.<sup>36</sup> Moody's warned that infrastructure-related development, depressed revenue collection

<sup>21</sup> www.pulselive.co.ke.

<sup>22</sup> The East African, 12 Feb 2018.

<sup>23</sup> The East African, 12 Feb 2018.

<sup>24</sup> The East African, 12 Feb 2018.

<sup>25</sup> The East African, 12 Feb 2018.

<sup>26</sup> The East African, 12 Feb 2018.

<sup>27</sup> The East African, 12 Feb 2018.

<sup>28</sup> Standard, 21 Feb 2018.

<sup>29</sup> Standard, 21 Feb 2018.

<sup>30</sup> Standard, 21 Feb 2018.

<sup>31</sup> Reuters, 22 Feb 2018.

<sup>32</sup> East African, 25 Feb 2018.

<sup>33</sup> Moody's, 13 Feb 2018.

<sup>34</sup> Moody's, 13 Feb 2018.

<sup>35</sup> Moody's, 13 Feb 2018.

<sup>36</sup> Moody's, 13 Feb 2018.

and the increased cost of debt will increase fiscal deficits.<sup>37</sup> Moody's expects the primary deficit to be above 4% of GDP over the next two years.<sup>38</sup> Moody's warned about debt affordability, noting that government interest payments as a share of revenue increased from 13.7% in 2012/2013 to 19% in 2017/2018.<sup>39</sup> Moody's expects the ratio to reach 20% in 2018.<sup>40</sup> Moody's warned about the shift in debt profile from concessional to commercial and semi-concessional debt, noting that the proportion of commercial external debt to total external debt increased from 7% to 31% between June 2013 and June 2017.<sup>41</sup> Short-term domestic debt will increase from 3.3% of GDP in 2011/2012 to 9.4% in 2016/2017.<sup>42</sup> Moody's warned that the government's financing requirements and increased reliance on commercial external debt and short-term domestic debt will increase liquidity risks.<sup>43</sup> Moody's acknowledged the government's fiscal consolidation and resilience efforts, but warned these will only have an impact on fiscal performance in the longer term.<sup>44</sup> Financing needs will increase from 19% of GDP in 2016/2017 to 22% by 2018/2019.<sup>45</sup>

Moody's said the stable outlook was due to Kenya's relatively diversified economy, government deposits within the domestic banking sector, and growth prospects of between 6 and 6.5%, which will protect the government from economic shocks.<sup>46</sup> Moody's also praised Kenya's relatively deep capital market and mature financial sector, which affords the government some capacity to issue domestically in local currency and with longer tenors.<sup>47</sup>

Moody's said a ratings upgrade could follow structural fiscal reforms that will eventually reduce Kenya's debt obligations and reduce liquidity risks.<sup>48</sup> Moody's said a further downgrade could follow fiscal slippage, which would increase pressure on Kenya's debt profile.

The government rejected a number of Moody's negative observations. Treasury budget director general **Geoffrey Mwau** said the fiscal deficit was expected to decrease from 8.9% of GDP in 2016/2017 to 7% at the end of the current financial year and to below 5% within three years.<sup>49</sup> Mwau accused Moody's of underestimating Kenya's economic fundamentals. On the same day as Moody's downgrade, the finance ministry published a budget outlook paper projecting that growth will increase from 4.8% in 2017 to 5.8% in 2018.<sup>50</sup> The budget outlook paper projects that the budget deficit will decrease from 8.9% of GDP in 2016/2017 to 6% in 2017/2018 and to 3% by 2022.<sup>51</sup> The overall budget is expected to increase from 2.32 trillion Kenyan shillings (KSh) (\$22.9 billion), or 27% of GDP, in 2017/2018 to KSh 2.49 trillion (\$24.6 billion), or 26% of GDP, in 2018/2019.<sup>52</sup>

In a second blow to Kenya's economic credibility, The **International Monetary Fund (IMF)** confirmed on 21 February that Kenya lost access to its \$1.5 billion standby credit facility in June 2017.<sup>53</sup> The **Central Bank of Kenya's (CBK)** continued insistence that it has access to the standby credit facility raises questions about the transparency of Kenya's public financial management. The facility, in place since March 2016, includes \$495m in interest-free credit repayable over eight years

<sup>37</sup> Moody's, 13 Feb 2018.

<sup>38</sup> Moody's, 13 Feb 2018.

<sup>39</sup> Moody's, 13 Feb 2018.

<sup>40</sup> Moody's, 13 Feb 2018.

<sup>41</sup> Moody's, 13 Feb 2018.

<sup>42</sup> Moody's, 13 Feb 2018.

<sup>43</sup> Moody's, 13 Feb 2018.

<sup>44</sup> Moody's, 13 Feb 2018.

<sup>45</sup> Moody's, 13 Feb 2018.

<sup>46</sup> Moody's, 13 Feb 2018.

<sup>47</sup> Moody's, 13 Feb 2018.

<sup>48</sup> Moody's, 13 Feb 2018.

<sup>49</sup> Reuters, 14 Feb 2018.

<sup>50</sup> Reuters, 14 Feb 2018.

<sup>51</sup> Reuters, 14 Feb 2018.

<sup>52</sup> Reuters, 14 Feb 2018.

<sup>53</sup> FT, 21 Feb 2018.

and \$990m repayable with interest over five years.<sup>54</sup> The facility remains in place, even though Kenya has lost its capacity to draw upon it.<sup>55</sup> IMF country representative **Jan Mikkelsen** said that Kenya lost access due to the government's failure to complete "a planned review" of the facility following repeated breaches of IMF budget deficit targets.<sup>56</sup> The IMF facility required the government to narrow its budget deficit to 3.7% of GDP in the 2018/2019 financial year.<sup>57</sup> The review was reportedly repeatedly delayed due to Kenya's prolonged 2017 general election.<sup>58</sup> According to Mikkelsen, the IMF informed both the treasury and the CBK at the time that Kenya had lost access to the standby credit facility.<sup>59</sup> However, the CBK continued to refer to its access to the standby credit facility as recently as its monetary policy committee statement on 22 January.<sup>60</sup> Withdrawal of access to the standby credit facility leaves foreign reserves as Kenya's only available currency buffer. Kenya's foreign reserves amount to \$7.24 billion, equivalent to 4.8 months of import cover.<sup>61</sup>

An IMF team visited **Nairobi** in February to discuss a successor to the standby credit facility, which is due to expire at the end of March.<sup>62</sup> The IMF said the availability of another programme will depend on a fiscal trajectory and declining budget deficit sufficient to stabilise Kenya's debt profile, and significant revisions to the legal cap on commercial interest rates.<sup>63</sup>

Kenya's creditworthiness is of increased concern due to increased levels of public debt, with its external debt stock particularly concerning without the buffer that the IMF's standby credit facility previously provided. Kenya faces several upcoming debt obligations in the short and medium term. In April, a \$750m syndicated commercial loan is due, after the government negotiated a six-month extension with the majority of creditors. In mid-2019, the five-year tranche of the 2014 Eurobond worth \$750m matures.

## Planner

2018 **(Kenya)** *Capital FM*. Construction of **Nairobi-Mombasa** express highway due to begin;  
 14 – 16 March 2018 **Nairobi (Kenya)** *Press release*. **East Africa Oil & Gas Summit 2018**;  
 28 Oct 2018 **(Kenya)** *Daily Nation*. Daily direct flights to **New York (United States)** expected to begin.  
 Apr 2018 **(Kenya)** *Daily Nation*. \$750m syndicated commercial loan due for repayment.

## Chronology

2 Mar 2018 **(Kenya)** *Reuters*. **Africa Oil** expects to conclude agreement on crude export pipeline by middle of the year;  
 1 Mar 2018 **Nairobi (Kenya)** *Press release*. The treasury cabinet secretary, **Henry Rotich**, says the time is right to revisit the commercial interest rate cap;  
 28 Feb 2018 **Nairobi (Kenya)** *Press release*. **Safaricom Ltd** says its changed its name to **Safaricom Plc** as of 31 January;  
 26 Feb 2018 **(Kenya)** *Daily Nation*. NGO **Human Rights Watch** claims that security forces killed 37

<sup>54</sup> FT, 21 Feb 2018.

<sup>55</sup> Reuters, 21 Feb 2018.

<sup>56</sup> FT, 21 Feb 2018.

<sup>57</sup> FT, 21 Feb 2018.

<sup>58</sup> FT, 21 Feb 2018.

<sup>59</sup> FT, 21 Feb 2018.

<sup>60</sup> FT, 21 Feb 2018.

<sup>61</sup> Daily Nation, 21 Feb 2018.

<sup>62</sup> FT, 21 Feb 2018.

<sup>63</sup> FT, 21 Feb 2018.

people in **Nairobi** between September and November 2017 around presidential election rerun;

22 Feb 2018 **(Kenya)** *The Star*. Kenya raises \$2 billion in Eurobond issuance;

22 Feb 2018 **Nairobi (Kenya)** *The Star*. The **International Monetary Fund (IMF)** tells parliamentary budget committee that the government's debt levels are damaging investor sentiment;

20 Feb 2018 **Nairobi (Kenya)** *The Star*. The IMF confirms Kenya lost access to its \$1.5 billion standby credit facility in June 2017;

18 Feb 2018 **Nairobi (Kenya)** *Nairobi News*. The police kill suspected **al Shabaab** militant allegedly planning vehicle borne improvised explosive device attack in Nairobi;

17 Feb 2018 **Nairobi (Kenya)** *Daily Nation*. **Moody's Investors Service** downgrades three Kenya-based banks **KCB Group, Equity and Co-operative**, following downgrade of government;

16 Feb 2018 **Nairobi (Kenya)** *The Star*. Nine new cabinet secretaries take oath of office;

16 Feb 2018 **Nairobi (Kenya)** *Capital FM*. Opposition **National Super Alliance (NASA)** supporters protest outside **United States (US)** embassy over US criticism of leader **Raila Odinga**;

15 Feb 2018 **Nairobi (Kenya)** *Standard*. **High Court** rules deportation of NASA lawyer **Miguna Miguna** was legal;

13 Feb 2018 **Nairobi (Kenya)** *Daily Nation*. Moody's downgrades **Kenya's** issuer rating from B1 to B2 with a stable outlook;

13 Feb 2018 **Nairobi (Kenya)** *The Star*. The attorney general, **Githu Muigai**, resigns;

9 Feb 2018 **Nairobi (Kenya)** *Standard*. The High Court quashes government order proscribing the NASA's **National Resistance Movement** as a criminal organisation;

8 Feb 2018 **Nairobi (Kenya)** *Citizen TV*. **Citizen TV**, which was shut down by the government ahead of Odinga's 'swearing in' ceremony, resumes broadcasting;

7 Feb 2018 **Nairobi (Kenya)** *Capital FM*. Chief justice **David Maraga** issues statement calling on government to respect court orders;

7 Feb 2018 **(Kenya)** *CAJ*. **Tullow Oil** will invest over \$2 billion in the upstream oil sector, and expects production to begin in 2021/2022.