Kenya – Business sentiment rebounds in September

- **Kenyan business sentiment recovered in September, rising 14.5% m/m to 63.9.**
- **In Q3 business sentiment averaged 58.1, down from 64.1 in Q2 and 59.4 a year ago**
- **Despite greater optimism, risks from a weaker exchange rate and higher inflation remain**

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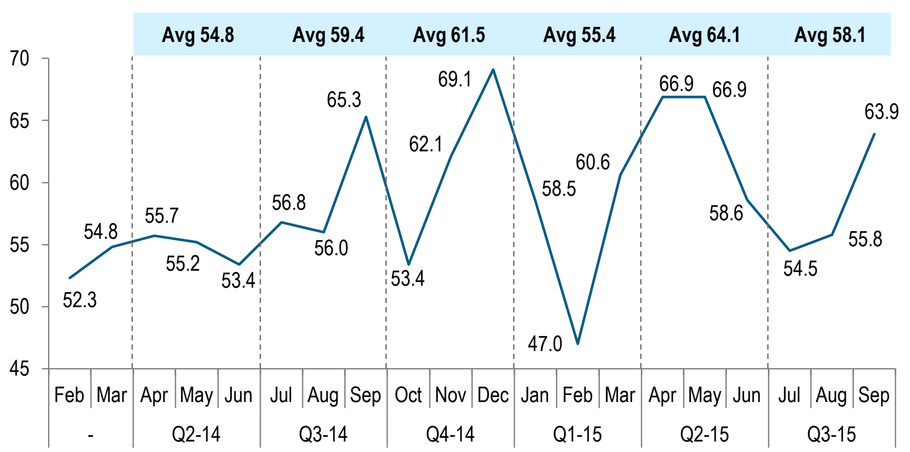
Summary

Business Sentiment in Kenya rebounded in September. The Standard Chartered-MNI Business Sentiment Indicator (BSI) rose to 63.9 in September, the second-highest print in 2015, recovering from three months of softer sentiment. Gains in order backlogs, production and new orders drove the increase.

All five of the components that make up the BSI rose in September, with order backlogs up 39.8% m/m (a 15% weight in the headline indicator), production up 15.7% m/m (25% weight) and new orders up 13.1% m/m (35%). Supplier delivery times (10%) and employment (15%) also increased. An increase in new orders, reflecting stronger domestic demand, likely contributed to higher order backlogs and supplier delivery times. Kenyan firms have also reported increasing production in response, and employment reached a four-month high as firms reported increasing the size of their work forces.

12 out of the 15 current conditions indicators increased in September. This follows a fall in 9 out of 15 current conditions indicators in August, and 10 out of 15 in July. 11 of 15 future indicator measures also increased from August levels. Kenyan business's assessment of both current conditions and the near-term outlook is much more positive than it was in August. While conditions are improving, there are still headwinds. Sentiment for Q3 as a whole was still softer despite the rebound in September. Business sentiment averaged 58.1 in Q3-2015, down from 64.1 in Q2, and 59.4 a year ago. However, this is still above the key '50' level, indicative of an economic expansion.

Figure 1: Kenya BSI rose in September to 63.9
Standard Chartered-MNI Kenya Business Sentiment Indicator



Source: MNI, Standard Chartered Research

While overall sentiment was much more positive in September, risks remain to the outlook. Kenyan shilling (KES) volatility and depreciation continue to be concerns. The currency has depreciated c.14% since the start of the year and 1.5% in September alone. Kenyan firms continue to report that the impact of the exchange rate is a problem and anticipate further FX weakness. The inflationary impact of KES weakness has also driven future expectations of input prices and prices received higher. Input-price future expectations for September reached their highest level since November 2014. For now, firms continue to report being able to pass higher input prices on to consumers, mitigating some of the impact on their financial positions. Despite hopes that a weaker exchange rate could lead to improved competitiveness and stronger international demand for Kenyan goods, there has yet to be any evidence of this. Export orders dropped by 33.4% m/m in September.

A quick recap of our BSI methodology

The Standard Chartered-MNI BSI for Kenya is a diffusion index, summarising in a single number how optimistic businesses feel about current and future economic conditions.

Each month, we poll c.200 businesses that represent different sectors of Kenya's economy

We partner with MNI, a well-known data provider that has long produced the Chicago PMI, among other indicators, to construct the Standard Chartered-MNI BSI. Each month, up to 200 formal-sector businesses, active in different segments of Kenya's economy, respond to questions on Kenya's current and future economic conditions. Although most of the respondents polled are Nairobi-based, with some in Mombasa, the businesses that they represent are active across Kenya.

While small and medium-sized enterprises (SMEs) are represented, so are corporates with a regional East Africa presence, both listed and unlisted. The responses of our panel of companies are collated to generate a single number that captures sentiment. The headline BSI (current conditions index) for Kenya is made up of a number of components, with different weights assigned: new orders (a 35% weight), production (25%), employment (15%), order backlogs (15%) and supplier delivery times (10%).

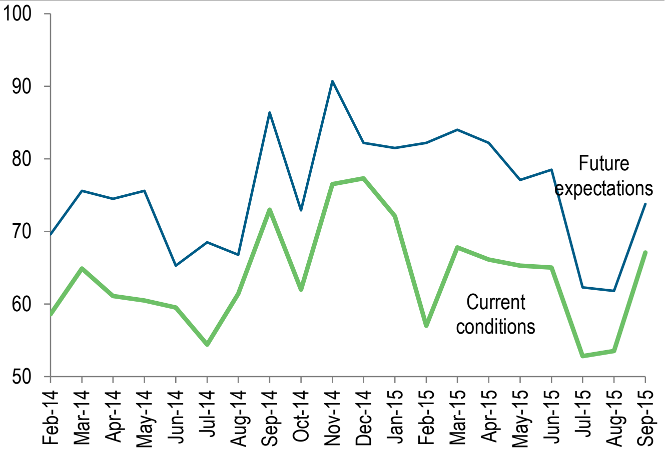
A headline BSI reading above 50 is typically consistent with economic expansion

Respondents are asked whether business activity has increased, decreased, or remained the same, compared with the previous month. They are also asked about their expectations over the next quarter. We use this information to calculate a diffusion indicator, by adding the percentage share of positive responses to half of the percentage of respondents reporting no change. An indicator above 50 shows an expansion. An indicator below 50 indicates a contraction. A result of 50 means no change.

Questions are asked on a number of key business metrics, including orders, production, pricing, inventories, credit availability and the impact of exchange-rate trends. These questions are provided at the end of this report (Figure 17). Data collation for Kenya was initiated in February 2014. The short survey history means that it is not yet possible to adjust for seasonality. Nonetheless, we can still observe how sentiment might be changing from month to month, based on our representative panel of companies. We believe that the receipt of timely information on economic performance can help a range of stakeholders, both in the private sector and in policy circles, with their economic decision-making.

Figure 2: Overall business conditions

Current conditions rose 25.4% m/m



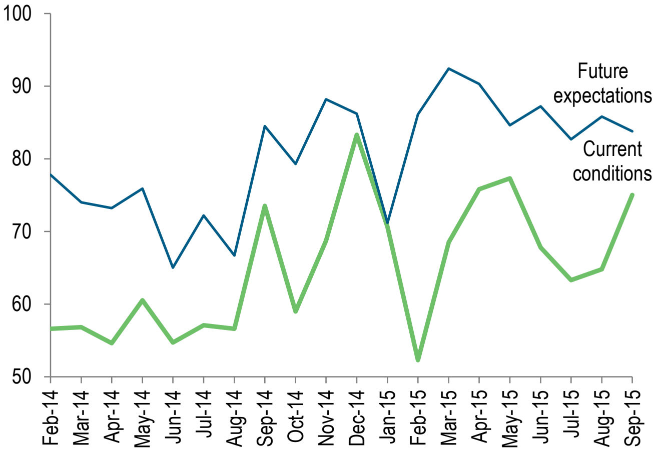
Source: MNI, Standard Chartered Research

Overall business conditions improved strongly

Overall business conditions increased sharply in September. The current conditions indicator increased 25.4%m/m to 67.1, its highest level since March 2015. Future expectations also rebounded from a series low in August, increasing 19.4% m/m to 73.8.

Figure 3: Production

Current conditions rose 15.7% m/m



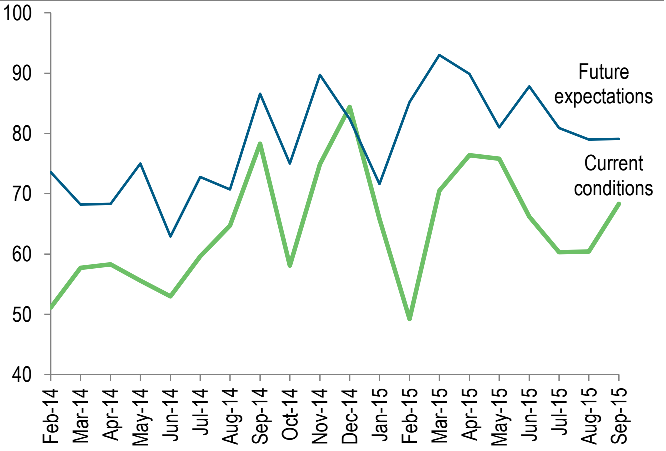
Source: MNI, Standard Chartered Research

Production current conditions rose

Kenyan businesses reported increased production in September to meet an improvement in the demand indicators. Production current conditions rose in September, up 15.7% m/m, helping to drive the increase in the headline indicator. Production accounts for 25% of the headline. Future expectations, however, fell 2.3% m/m as businesses are less optimistic about the production outlook than they were in August. However, with the future expectations indicator at 83.8, this still indicates businesses expect production to increase further in the near future.

Figure 4: New orders

Current conditions rose 13.1% m/m



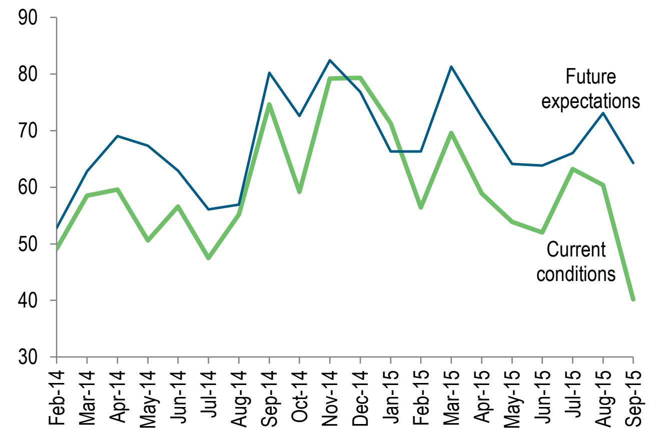
Source: MNI, Standard Chartered Research

New orders improved in September

New orders current conditions rose 13.1% m/m in September to 68.3. Future expectations also increased slightly by 0.1% m/m.

Figure 5: Export orders

Current conditions collapsed 33.4% m/m



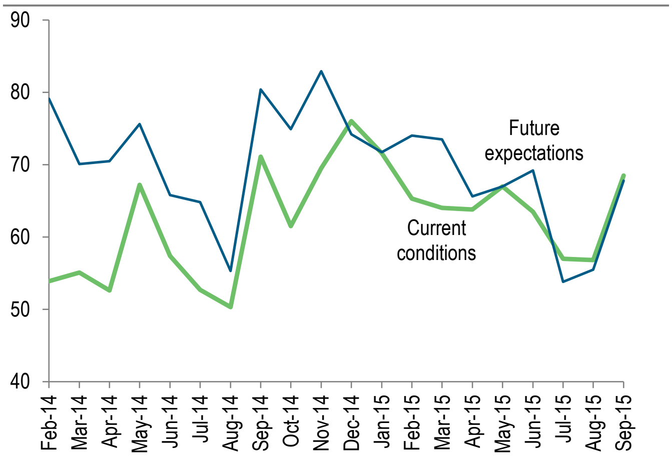
Source: MNI, Standard Chartered Research

Export orders collapsed

While new orders increased in September, export orders collapsed. Current conditions were down 33.4% m/m to a series low of 40.2, while future expectations also fell 12%.

Figure 6: Productive capacity

Current conditions rose 20.6% m/m



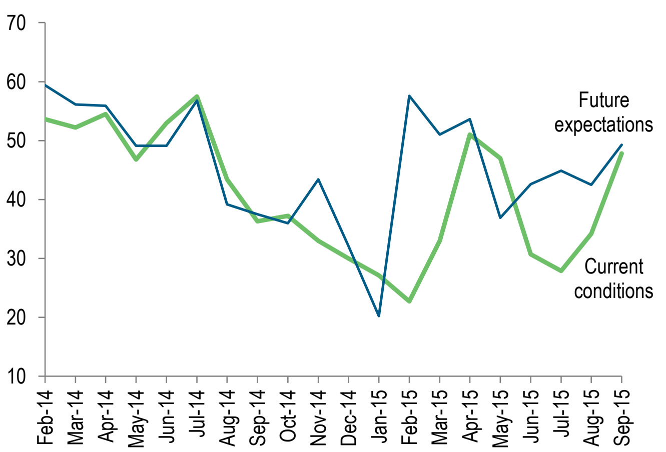
Source: MNI, Standard Chartered Research

Firms reported improved productive capacity

Kenyan businesses reported that productive capacity is improving in September. The current conditions indicator rose 20.6%m/m to 68.5, its highest level since January 2015. Future expectations are also for improved productive capacity, with the indicator up 22.2% m/m in September.

Figure 7: Order backlogs

Current conditions surged 39.8% m/m



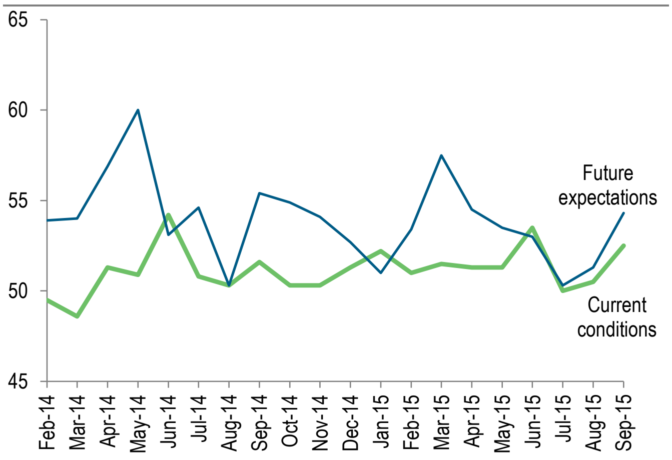
Source: MNI, Standard Chartered Research

Order backlogs surged

Order backlogs increased 39.8% m/m in September as firms reported an improvement in order backlogs. Order backlogs contribute 15% to the headline BSI, so the rapid increase helped to drive gains in the BSI. Both the current conditions and future expectations indicators remain in negative territory below 50, though.

Figure 8: Employment

Current conditions rose 4.0% m/m



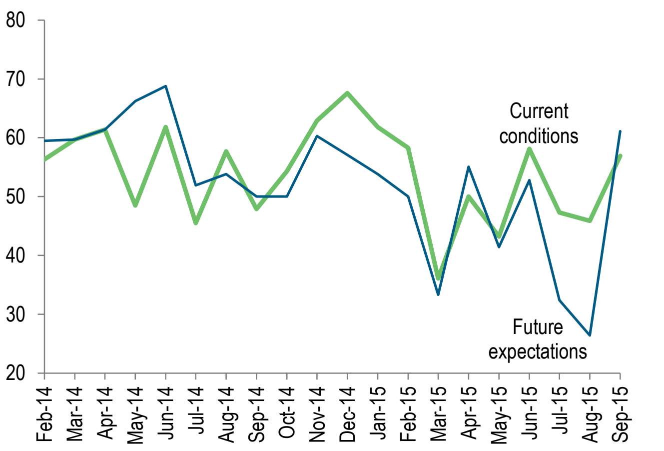
Source: MNI, Standard Chartered Research

Employment intentions improved marginally

Both employment current conditions and future expectations continued to improve in September. Current conditions rose 4.0% to 52.5, while future expectations increased 5.8%. This indicator has been volatile. Over the history of our BSI, firms have yet to indicate stronger employment intentions, with a more sustained improvement in economic activity likely needed first.

Figure 9: Inventories

Current conditions rose 24.0% m/m



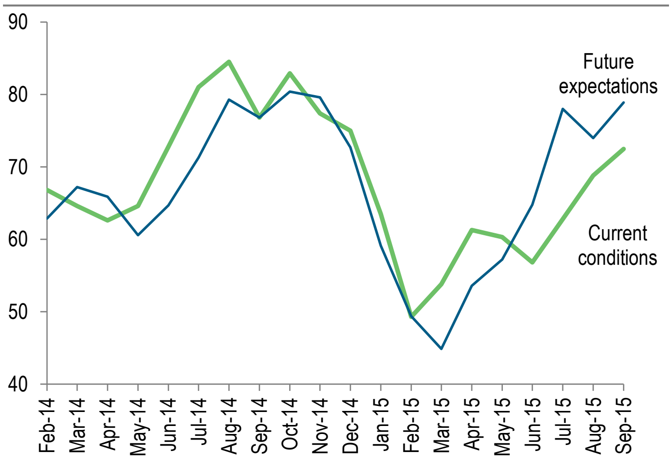
Source: MNI, Standard Chartered Research

Inventories increased

Inventories increased in September. Current conditions rose 24.0% to 56.9, while future expectations increased by a huge 131.4%. This was likely in part a reversal of the large fall seen in recent months, as firms reported expecting further increases in inventories in the coming months.

Figure 10: Input prices

Current conditions rose 5.4% m/m



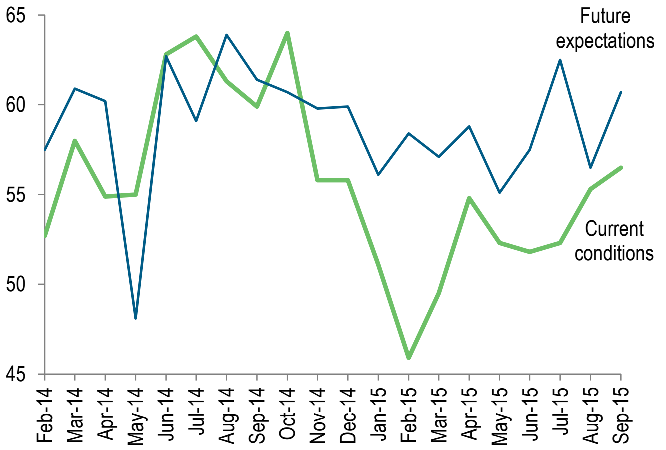
Source: MNI, Standard Chartered Research

Firms expect higher input prices

Although the authorities' official inflation figures indicate inflation has eased in August, Kenyan businesses reported that current input prices increased 5.4% m/m to 72.5. Future expectations also increased 6.6%. This likely reflects the inflationary impact of a weaker FX rate, and expectations for continued inflationary pressure in the coming months, with El Nino rains expected to add to inflationary pressures.

Figure 11: Prices received

Current conditions rose 2.2% m/m



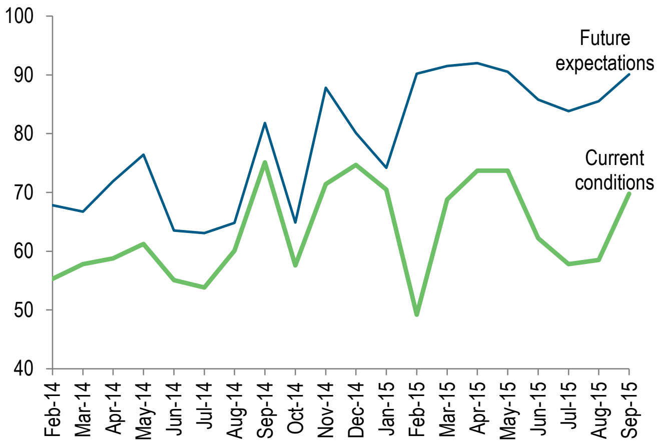
Source: MNI, Standard Chartered Research

Firms reported charging higher prices

Kenyan business report that prices received increased 2.2% m/m in September to 56.5. Future expectations increased 7.4% to 60.7, reversing the decline seen in August. Firms expect that they will be able to continue passing on higher prices to consumers.

Figure 12: Financial position of your company

Current conditions rose 19.3% m/m



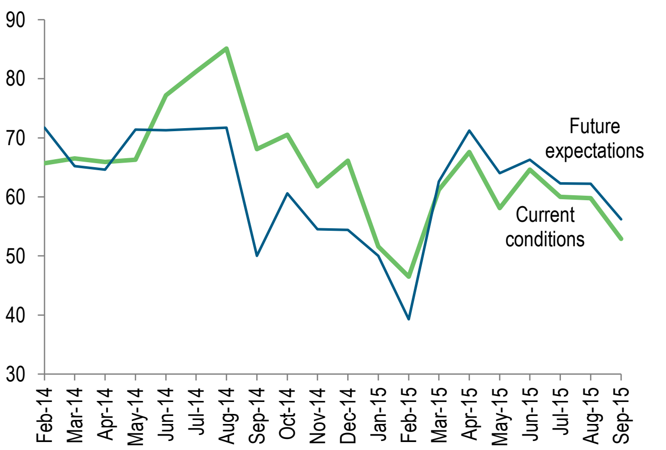
Source: MNI, Standard Chartered Research

Kenyan firms upbeat about financial positions

Kenyan firms were more positive about their financial positions in September. The current conditions indicator increased by a robust 19.3% m/m to their highest level since May 2015 at 69.8. Firms were also more optimistic about their financial positions in the short term; the future expectations indicator remained high at 90.1 in September. This finding is difficult to explain, given the upward pressure on market interest rates in September.

Figure 13: Interest rates paid

Current conditions fell 11.5% m/m



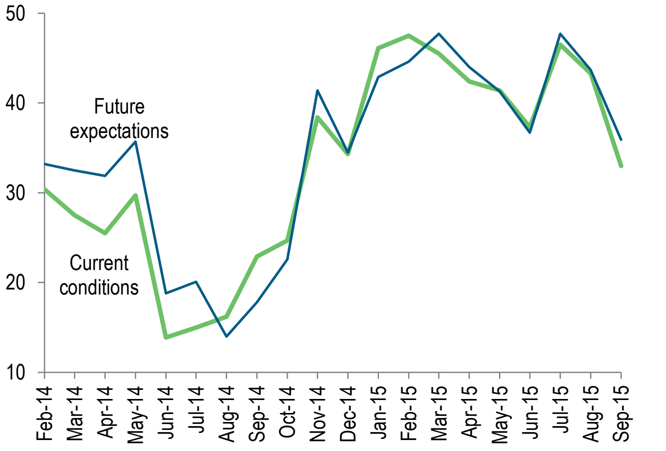
Source: MNI, Standard Chartered Research

Fewer firms reported higher interest rates

Both current conditions and future expectations for interest rates paid fell in September, reflecting a lower number of respondents indicating that interest rates paid had increased. The Kenya Banks Reference (KBRR) rate is reset on a six-month basis. Loans that are priced off the KBRR may not adjust fully until the new year.

Figure 14: Effect of the KES exchange rate

Current conditions fell 23.8% m/m



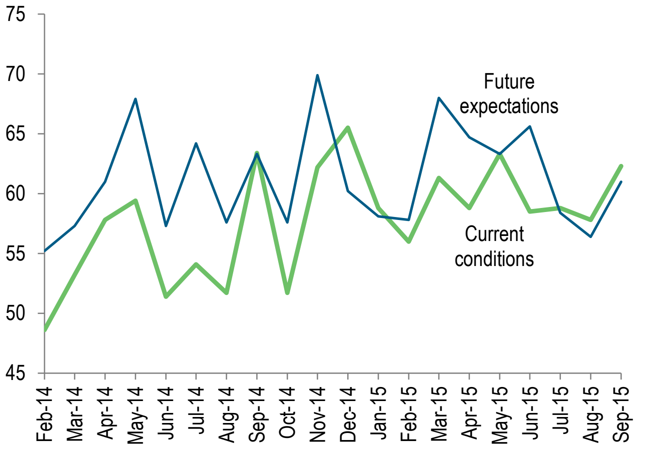
Source: MNI, Standard Chartered Research

The KES continues to hurt businesses

In September, more Kenyan businesses reported that the KES continues to be a concern. The KES has depreciated 1.6% since the start of the month and almost 17% since the start of the year. The current conditions indicator for the effect of the KES on Kenyan business dropped 23.6% m/m to 33.0, its lowest level since October 2014. Future expectations also dropped sharply, down 17.8% m/m, indicating Kenyan businesses expect more FX pressure to come.

Figure 15: Supplier delivery times

Current conditions rose 7.8% m/m



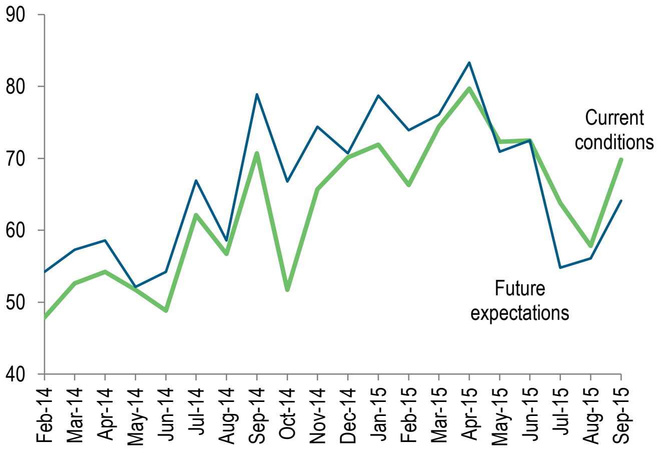
Source: MNI, Standard Chartered Research

Supplier delivery times rose 7.8%

Both current conditions and future expectations of supplier delivery times increased in September, perhaps an indication of higher economic activity. The current conditions indicator increased to 62.3 while future expectations rose to 61.0.

Figure 16: Availability of credit

Current conditions rose 20.8% m/m



Source: MNI, Standard Chartered Research

Availability of credit improved

Availability of credit improved in September, with both the current conditions and future expectations indicators increasing. Kenyan firms expect future credit conditions to improve. The future expectations indicator increased 14.3%m/m to 64.1, at odds with evidence of tighter liquidity in Kenya's banking system.

Figure 17: Understanding the questions

In order to aid comprehension of the survey, we reproduce the questions asked of respondents below

Productive capacity	Compared with a month ago, is the productive capacity of your company higher, the same or lower? Questions will also address the three-month outlook.
Production	Questions address what is happening to actual production – higher, the same, or lower? What about the three-month outlook?
Interest rates paid	How do the interest rates that you pay compare with a year ago? How do you expect the interest rate you pay to change in three months' time?
New orders	Compared with a month ago, are new orders higher, the same or lower? Do you think that new orders will be higher, the same or lower in three months?
New export orders	Compared with a month ago, are new export orders higher, the same or lower? Do you think new export orders in three months' time will be the same, higher or lower?
Exchange rate	Compared with a month ago, how is the FX rate affecting your business – helping, no impact or hurting? How do you think it will be affecting your business in three months' time?
Suppliers' delivery times	Compared with a month ago, are your suppliers' delivery times (of raw materials, consumables, etc.) higher, the same or lower? Do you think your suppliers' delivery times (of raw materials, consumables, etc.) in three months' time will be higher, the same or lower?
Number of employees	Compared with a month ago, is the number of your employees not enough, just right or too many? What do you expect it to be in three months' time?
Financial position of your company	An assessment of whether this is better, the same or worse.
Order backlogs	(For agricultural companies, there are no questions about order backlogs.)
Input prices	How do they compare with a month ago? Where are they expected to be in three months' time?
Prices you charge for your products	How do they compare with a month ago? Where are they expected to be in three months' time?
Availability of credit	Is it better, the same or worse than a year ago? Do you expect the availability of credit in three months to be better, the same or worse?
Inventory of finished goods	(For agricultural companies, there are no questions about inventories of finished goods.)
Overall business conditions	Are these improving, the same or worsening? What do you expect over the next quarter?

Source: Standard Chartered Global Research, MNI

A selection of comments from the Kenya panel of businesses

"There was an unexpected surge in demand this month, leaving us with a lot of orders that we have yet to fulfil

Rise in orders this month meant that we increased our output

We import a lot so the depreciation of the shilling has pushed up our costs

Modernising our factory has boosted our productive capacity

Sales from abroad were quieter this month

Headcount was higher this month as we took on more staff to meet growing demand

Our expenses were higher this month after fuel prices were hiked

Since our tax bill rose, we had to increase our prices

Good relationship with our bank means that we are always able to get a loan when we need one.

Our financial position is much better as better management has helped us to cut costs

We've temporarily stopped taking orders from abroad while we focus on meeting the demands of our domestic clients.

There is no shortage of banks willing to lend but the interest rates that they charge make borrowing an expensive proposition

Backlogs have risen over the past month but we hope to address these as soon as possible in order to satisfy our customers"

Source: MNI, Standard Chartered Research

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