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 2021/22 BUDGET

As you are aware, the principal objectives of the Central Bank of Kenya (CBK) as established in Cap 491, Section 4 (Subsection 1, 2 and 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 (1) and (2) above, to support the economic policy of the Government, including its objectives for growth and employment.

In addition, subsections 4 - 5 provides 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, subsection 6 of the Act requires the Cabinet Secretary to publish the Notice in such a manner he deems 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 taken by the Government in the FY 2021/22 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 increase in Consumer Price Index (CPI) as published by the Kenya

National Bureau of Statistics (KNBS). The inflation target is in line with the macroeconomic developments and targets underlying the FY 2021/22 budget and the Medium-Term Expenditure Framework (MTEF) for the period (FY 2021/22 - FY 2023/24). The macroeconomic targets support the economic policies of the Government as detailed in the 2021 Budget Policy Statement and were developed during the inter-Ministerial Macro Working Group while preparing the expenditure ceilings for the FY 2021/22 budget.

The Central Bank of Kenya (CBK) is therefore expected to achieve this 5.0 percent inflation target and will be accountable to the Government and the general public for its attainment. 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. Domestic shocks may emanate from unfavourable weather conditions that may affect agricultural output. Maintaining Inflation rate at these levels will help preserve macroeconomic stability and reduce undesirable fluctuations in economic performance.

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

- The factors driving inflation away from the specified target by more than 2.5 percentage points in either direction;
- The measure(s) which the CBK is taking to address the deviation; and
- 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 also 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 2021/22 budget draws from the national development agenda as outlined in the Third Medium Term Plan (MTP III) of the Vision 2030 and prioritized in the "Big Four" Agenda. The focus of the policies is to provide an enabling environment for a resilient and sustainable economic recovery. These policies are detailed in the 2021 Budget Policy Statement and affirmed in the Budget Summary for the Fiscal Year 2021/22.

The FY 2021/22 budget was prepared against a background of a projected global economic recovery amidst uncertainty relating to new COVID-19 mutations that could require broader reinstatement of containment measures. Global growth in 2021 is projected at 6.0 percent from a contraction of 3.3 percent in 2020.

The outbreak of Covid-19 pandemic adversely affected our Kenyan economic activities leading to closure of businesses and job losses especially in tourism, trade, transport, education, manufacturing sectors, among others. At the start of the pandemic, the Government provided tax reliefs (tax cuts) to businesses and people and rolled out various monetary and social policy measures to mitigate the effects of the COVID-19 Pandemic. The Government is also implementing the Economic Stimulus Programme (ESP) aimed at further increasing demand for local goods and services, cushioning vulnerable Kenyans, securing household food security for the poor, and creating employment and incomes.

To accelerate economic recovery and sustain inclusive growth, the Government will accelerate implementation of the ongoing strategic priorities under the "Big Four" Agenda on food and nutrition security, affordable housing, manufacturing, and universal healthcare. Further the Government is implementing interventions under the Economic Recovery Strategy to re-position the economy on an inclusive and sustainable growth trajectory.

Therefore, economic policy of the Government is geared towards fast tracking the implementation of programs and projects under the "Big Four" Agenda and the ongoing implementation of the Economic Recovery Strategy. 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.

In order to complement the monetary policy and anchor macroeconomic stability, the fiscal policy supporting the FY 2021/22 and the medium term budget framework is designed to reduce fiscal deficit and stabilize growth in public debt while strengthening debt sustainability. The policy will support the projected economic growth by ensuring development projects are implemented as planned. Fiscal deficit is therefore projected to decline from 8.7 percent of GDP in the FY 2020/21 to 7.7 percent of GDP in the FY 2021/22 and 3.6 percent of GDP by the FY 2024/25. This fiscal consolidation will be achieved through a combination of revenue enhancement initiatives, expenditure rationalization and development expenditure prioritization in the budget over the medium term as outlined in the 2021 Budget Policy Statement.

As outlined in the Budget Statement delivered to the National Assembly on 10th June 2021, price stability is one of the prerequisite for a stable macroeconomic outlook underpinning the FY 2021/22 budget. It is therefore expected that the CBK will maintain inflation within the target range during the FY 2021/22 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 2022/23 that will take into account updates of the Government's economic policy objectives in the 2022 Budget Policy Statement.

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CABINET SECRETARY/THE NATIONAL TREASURY AND PLANNING
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