SBM bank

ELITE BANKING

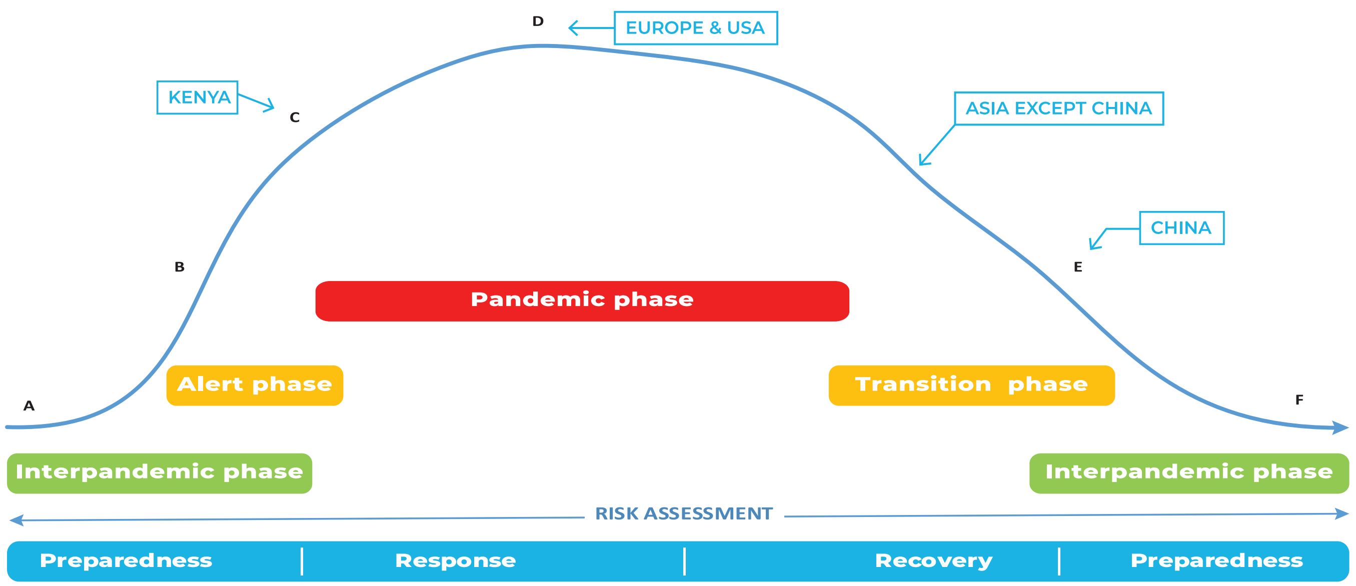
Covid-19 Pandemic Economic Impact & Outlook

May 2020

Pandemic Background & Outlook

PANDEMIC BACKGROUND & OUTLOOK

The chart below is an ordinary continuum of pandemic phases based on global average cases reported over time.



Source: www.cdc.gov

PANDEMIC BACKGROUND & OUTLOOK

Infections and casualties as at 26th May 2020 in different regions

REGION	INFECTIONS	FATALITIES	TREND AND LIKELY PERIOD TO CONTAINMENT
Asia	1,011,056	28,360	1. Growth of infection has slowed down 2. Vaccine under trial 3. Expected containment in 3 to 6 months
Europe	1,944,149	169,829	1. Cases of infection rising 2. Vaccine and cure on trial 3. Expected containment in 6 to 18 months
USA	1,725,808	100,625	1. Cases of infection rising 2. Vaccine and cure on trial 3. Expected containment in 6 to 18 months
Africa	121,873	3,628	1. Cases testing positive on the rise and low number of infections could be due to level of testing 2. Region has experienced lowest level of fatalities 3. Containment could anytime between 6 to 18 months dependent on soon the vaccine and cure being tested in developed regions will be promoted to commercial production and distribution
Kenya	1,348	52	1. Same as other countries in Africa 2. So far there has been 114 recoveries

Containment will be realized upon achievement of either or both of the following
Formulation, testing and approval of a vaccine

1. The advanced countries are likely to introduce a vaccine in 6-18 months, but the vaccine will take sometime for widespread distribution in Africa.
2. Reduction of rate of infection and fatalities to a level that eliminates fear of infection

GLOBAL ECONOMIC OUTLOOK

GLOBAL ECONOMIC OUTLOOK

The pandemic is affecting Global economic performance in different ways including the following

1. Overstretching health facilities globally
2. Significant disruption of trade flows through lockdowns and closure of international entry points
3. Reduction in working hours and production capacities
4. Costs and challenges associated with working offsite, particularly in developing economies where infrastructure is not well developed
5. Disruption of social setups arising from the social distancing measures implemented in various regions. Effect of such disruption is higher levels of stress and anxiety at work place

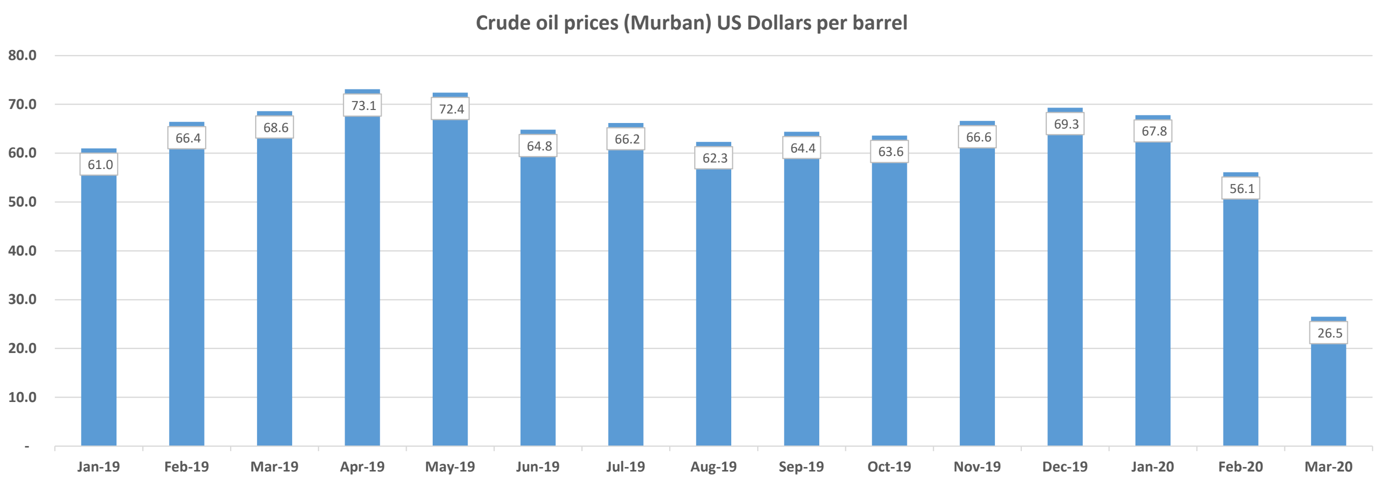
REGION	2020-PRE	2020-POST	2021	Comment
Asia	5.8%	-0.6%	7.8%	1. India GDP for 2020 and 2021 post pandemic estimated at 1.9% and 7.4% respectively 2. China GDP for 2020 and 2021 post pandemic estimated at 1.2% and 9.2% respectively 3. Asia is likely to attract more capital inflow (production contracts) post pandemic
Europe	2.6%	-7.5%	4.7%	1. Effect of the pandemic is substantial but making containment strides 2. More accommodative fiscal and monetary policies by the respective authorities expected to support economic restoration
USA	2.0%	-5.9%	4.7%	1. Effect of the pandemic is substantial but making containment strides 2. More accommodative fiscal and monetary policies by the respective authorities expected to support economic restoration
Africa	3.5%	-1.6%	4.1%	1. The region has, so far, not been as adversely affected like the Western countries hence stands a better chance of quicker spring back 2. Likelihood of sizeable inflow of capital, if attractive polices and infrastructure is put in place
Global	3.3%	-3.0%	5.8%	1. World Bank estimates Global GDP of between -2.1% and -5.1% in 2020 2. Asia which has most of the production contracts in the world was hit hard by the pandemic 3. Likelihood of emotional and economic backlash against China by other market players with economic ties with China

The pandemic is not yet contained and the time it will take globally get to transition phase remains uncertain. Most analysist have taken September 2020 as the transition month. The projections we get revised as and when it becomes evident that pandemic spread will not be contained by September 2020.

Globally, crude oil industry is a key sector in the international market

1. It is a common denominator in all sectors globally, either as a source of energy or raw materials for production
2. Large volumes of trades with high values are transacted daily with oil as the underlying commodity, hence any disruption will be felt across the global economy
3. In the recent past, reduction in production capacities and travels bans has resulted in unforeseen drastic decrease in oil consumption. The aftermath of this has been collapse of oil crude prices as well as decrease in retail pump prices of fuel
4. Some of the large economies in Asia thrive on revenues generated from export of crude oil. Adverse effects of reduced oil consumption and crash of prices is forcing these economies to dig deeper into state coffers as well as explore ways of diversification of revenue generation
5. Pre-pandemic China, USA, India, Japan and Russia accounted for over 45% of total global oil consumption, hence total lockdown in these economies have greatly contributed to the reduction in oil consumption
6. Post pandemic consumption will rise sharply as global economies rush to restoration, but prices will lag due to existing oil reserves

CRUDE OIL PRICES (MURBAN) US DOLLARS PER BARREL



Source: Abu Dhabi National Oil Company

KENYA ECONOMIC OUTLOOK

THE PANDEMIC IN KENYA

1. The first case of this infection was reported in Kenya on 13th March 2020 and since then other cases have been identified.
2. As at 27 April 2020 there were 363 reported cases, 14 deaths and 114 recoveries across the country. To curb spread of the infection, the following measures have been effected by the Government and corporates
   a. Restriction of movement in and out of Nairobi metropolitan, Mombasa, Kilifi and Mandera counties
   b. National wide curfew restricting movements between 7.00pm and 5.00am
   c. Enforcement of Public Health Act that includes use of face masks in public areas
   d. Reduction of number of people that can be accommodated in PSV
   e. Banning of all public gatherings including places of worship, funerals, weddings and other social gatherings
   f. Campaigns on social distancing, washing hands and use of sanitizers. This has also been made mandatory in all premises visited by the public
   g. Establishment of isolation centers at National and County levels equipped with testing kits, personal protection equipment and other sanitary items required in such facilities
   h. Businesses invoked their BCP that includes
      - Activation of their Disaster Recovery Sites
      - Formation of Committees for management of the pandemic related issues
      - Formation of “blue” and “white” teams either working in different places or in shifts
      - Working from home formulae
      - Reduced operations and working hours
   i. The Government formed a Crisis Management Committee Team to manage the pandemic at National level
   j. Closure of all international entry points for passengers

THE PANDEMIC IN KENYA (CONT...)

a. To alleviate the impact of the Pandemic on Citizens and businesses the Government has introduced the following measures
    i. Amendment of the Finance Bill to reduce tax burden as follows
        - Reduction of VAT from 16% to 14%
        - Shortened PAYE tax brackets with the highest rate reduced from 30% to 25%
        - Personal relief increased from KShs 1,400 to KShs 2,400
        - Corporate tax reduced from 30% to 25%
        - Turnover tax for small tax payers reduced from 3% to 1% with definition of small tax payer being increased from turnover of KShs 0.5 million to KShs 1 million.
        - Exemption of VAT from personal protection equipment
    ii. CBK issued guidelines to Banks on accommodative measures for borrowers whose loans get into arrears as a result of the pandemic. These includes
        - Facility restructuring without treating the facility as NPL
        - No listing of facilities falling into arrears due to effects f the pandemic
        - Reduction of cash ratio from 5.25% to 4.25%, with intention of using the resultant liquidity to cater for the restructures referred to above
        - Extension of repo period from 28 days to 90 day
    iii. Amendment of the Law of Contract to include COVID-19 as one of the force majeure
    iv. Encouraged online financial services providers to review down transaction charges
b. Other measures that the Government is likely to consider in near future includes
    i. A fund to cater for supply of basic necessities to the needy
    ii. A fund to be awarded to specific identified businesses as part of economic restoration effort
    iii. Special lines of credit to particular sectors either funded directly by the Government or indirectly through Government development partners
    iv. More growth incentives in form of tax reliefs for sectors providing essential goods/services in the short run
    v. In the mid and long term, there is a likelihood of deployment of both monetary and fiscal policies to support capital inflow into sectors that fuel economic growth
    vi. Amendment of labour laws to protect employees from redundancy decisions

ECONOMIC OUTLOOK OF THE PANDEMIC IN KENYA

Measures taken to curb the pandemic has disrupted business operations across the economy. Some of the measures taken by business in response include the following

1. Reduction of operating capacities
2. Temporary closures of some of the highly impacted businesses like hospitality industry
3. Either layoffs or pay cuts for staff

Economic analysts have given varied views on expected economic growth but the common observation by all is a reduced growth in 2020

Economic Factor	Projection before Pandemic	Estimated impact of the Pandemic
GDP	Kenya GDP projected growth in 2019 was 5.4% and was estimated to grow by 6.4%, 6.1% and 6.3% in 2020, 2021 and 2022 respectively *Source: Kenya Bureau of Statistics*	1. GDP projected growth by IMF is 1% and 6.1% for 2020 and 2021 respectively 2. Central bank of Kenya has projected GDP to grow by 3.4% in 2020 and later Treasury issued a statement that GDP growth is likely to be as low as 2.5% in 2020. Treasury estimates a growth of 6.0% in 2021 3. Renown economist has projected Kenya GDP decline in 2020 of 3% based on projected expenditure for the remaining period to December 2020 4. Renown economic analyst projects a GDP decline of 2.1% and growth of 7.2% in 2020 and 2021 respectively, based on expected revenue generation in the two years 5. Globally, all indications are a decline in GDP growth in 2020; • IMF projects a decline of 3% • World Bank indicates a decline of between 2.1% to 5.1% • McKinsey in partnership with Oxford Economics estimates a decline of 7% and likelihood of recovery to pre-pandemic GDP performance by end of 2022 In view of the above, it is very unlikely that the performance of the economy will generate a GDP of more than 2%.

<table>
<tr><td>Inflation rate</td><td>In 2019 inflation remained within the target range of 2.5% to 7.5%, and in most cases between 4% and 5%. Food and oil prices were a key factor in the inflation rates movements. It was projected that the rate would remained within the range in 2020 but tending towards to upper limit depending on performance of agricultural sector.</td><td>The movement restrictions, both at local and international markets, is likely to lead to shortage of food and other trade commodities. At the same time there is reduced demand for crude oil and hence crude oil prices are on a downward trend. The reduced crude oil demand will potentially persist for good part of 2020. Whereas shortage in food and trade commodities will put upward pressure on prices, this will be moderated down by the reducing crude oil prices. There is also regulatory goodwill to keep prices at bay. Hence overall inflation is expected to remain anchored within the target in the rest of the year.</td></tr>
<tr><td rowspan="3">Interest rates</td><td>No major variations in lending rates were observed after repeal of the interest rate cap, mainly because Banks were yet to come up with risk based pricing models as required by Central Bank of Kenya. As result most of the local currency lending was at an average of 12.2% as at Feb 2020</td><td>There is looming credit slow down and a tendency by lenders to increase local currency lending interest rates. However the ongoing regulatory interventions is likely to keep changes in lending interest rates minimal. In the latest MPC meeting the CBR was reduced further by 25 basis points to 7.0% in a bid to boost flow of cheap loans in the economy.</td></tr>
<tr><td>Interest on Government securities was stable even after removal of the lending rates cap law. A 10-15 years bond continued attracting 12.3% and was expected to remain that range through out 2020. Below are the current Treasury Bills rates
<table><tr><th>TERM</th><th>RATE</th></tr><tr><td>91 Days</td><td>7.3%</td></tr><tr><td>182 days</td><td>8.1%</td></tr><tr><td>364 days</td><td>9.2%</td></tr></table></td><td>In this uncertain situation investors will tend to move away from long term investments to short term and other more solid investments like gold. This will have the following implication
Reduced liquidity of long term bond market
Increase in appetite for Treasury bills and bonds of less than 5 year maturity.
In the circumstances, interest rates on short term investments will move downwards and long term bond market activity remarkably go down.</td></tr>
<tr><td>Average monthly Interbank market rates have fluctuated in the last 12 months hitting a low of 2.3% in July 2019 and a high of 7.0% in October 2019. The rates have remained stable since the start of the year averaging 4.4%. No wider fluctuations were expected as the market was expected to remain liquid.</td><td>At the backdrop of the credit squeeze, liquidity in the market will remain, hence rates not expected to materially fluctuate outside the current range.</td></tr>
</table>

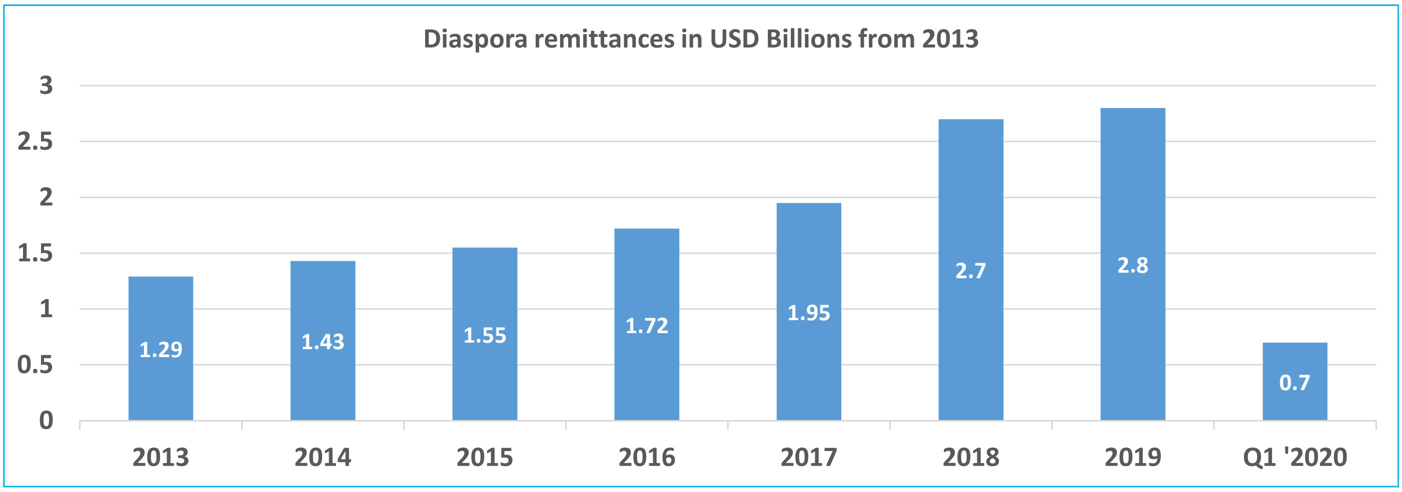
Foreign exchange rates	In 2019 KES exchange to the dollar was at KES 100.9 per dollar in January and closed at KES 101.3 per dollar in December, with a spike to KES 104.1 per dollar in July. The shilling was expected to remain relatively stable against the dollar in 2020 with a bias to a 2.4% depreciation by year end supported by: • The narrowing of the current account deficit • High levels of forex reserves, at March 2020 was USD 7.9 billion, equivalent to 4.8 months of import cover • Regulatory supportive activities in the money market, such as repurchase agreements and selling of dollars. • Foreign capital inflows, with investors looking to participate in the domestic equities market • Improving diaspora remittances supported by increased uptake of financial products by the diaspora due to financial services firms, particularly banks, targeting the diaspora, and new partnerships between international money remittance providers and local commercial banks making the process more convenient.	Fluctuation in the exchange rate of the Shilling to the dollar is likely to be affected by the following: 1. Reduced exports as a result of lower demand in the destination markets 2. Reduction in diaspora remittances into the country owing to the fact that the economies of origin have been adversely affected by the pandemic. Consistently from 2018 diaspora remittances have accounted for around 3% of the GDP 3. Post COVID, there will be demand for Dollars as businesses put efforts to restock. However, this also be moderated down by the following • Low prices of crude oil which translates into lower demand for dollar despite constant consumption. • As much as markets will open up, there is likelihood of travel restrictions, this will curtail demand for dollar for travel 4. Tourism, a major earner of dollars, will lag in picking up, and most likely it will take up to 2022 to restore 5. The ongoing regulatory interventions and accommodative monetary policies 6. Potential inflows from borrowing from international lenders like World Bank and IMF. Kenya is at 58% National debt compared to IMF/World Bank threshold of 74% The permutations of the above factors is likely to result in a depreciation of about 5% of Shilling by end of 2020 compared to the rates at the beginning of the year. Hence it is estimated that the dollar FX rate will close at KShs 107 per dollar, by end of the year.

ECONOMIC OUTLOOK OF THE PANDEMIC IN KENYA

SECTOR DESCRIPTION	PANDEMIC IMPACT ASSESSMENT	SECTOR GDP CONTRIBUTION	GROWTH IN SECTOR					
			2018	2019	2020 PRE & POST PANDEMIC GROWTH			
			ACTUAL	ESTIMATE	BASELINE	MILD	MODERATE	ADVERSE
Agriculture	Low	18.3%	6.4%	4.6%	5.8%	5.7%	4.5%	3.2%
Mining and quarrying	Moderate	1.0%	2.8%	4.2%	4.5%	4.5%	3.5%	2.1%
Manufacturing	Moderate	9.6%	4.2%	3.7%	5.1%	3.6%	2.4%	1.2%
Energy and water	Moderate		7.9%	5.7%	6.1%	6.5%	5.7%	4.5%
Construction	High	5.9%	6.6%	6.7%	6.7%	6.4%	4.5%	3.2%
Wholesale & retail trade	High	8.7%	6.3%	5.5%	5.9%	5.1%	3.2%	2.3%
Accomodation & restaurant	High		16.6%	11.3%	12.4%	7.1%	(2.0%)	(10.0%)
Transport & storage	High	7.6%	8.8%	7.1%	7.3%	4.9%	3.7%	2.9%
Finance & insurance	Moderate	6.4%	5.6%	6.3%	7.7%	7.0%	5.1%	4.4%
Public & administration	Moderate		6.1%	6.2%	6.3%	6.3%	5.8%	5.1%
Profession & support services	Low		5.9%	6.0%	6.2%	5.5%	4.8%	4.1%
Real estate	High	8.6%	4.1%	5.0%	5.9%	5.7%	5.1%	3.4%
Education	High	7.1%	5.8%	5.6%	5.9%	5.9%	5.1%	3.4%
Health	Low	1.8%	4.5%	4.8%	5.0%	4.3%	5.5%	6.7%
Others	Moderate		4.9%	2.5%	2.5%	2.5%	2.1%	1.9%
ICT	Low	4.0%	11.4%	10.9%	10.1%	10.1%	11.4%	13.3%
Real GDP growth			6.3%	5.7%	6.2%	5.7%	4.5%	3.4%

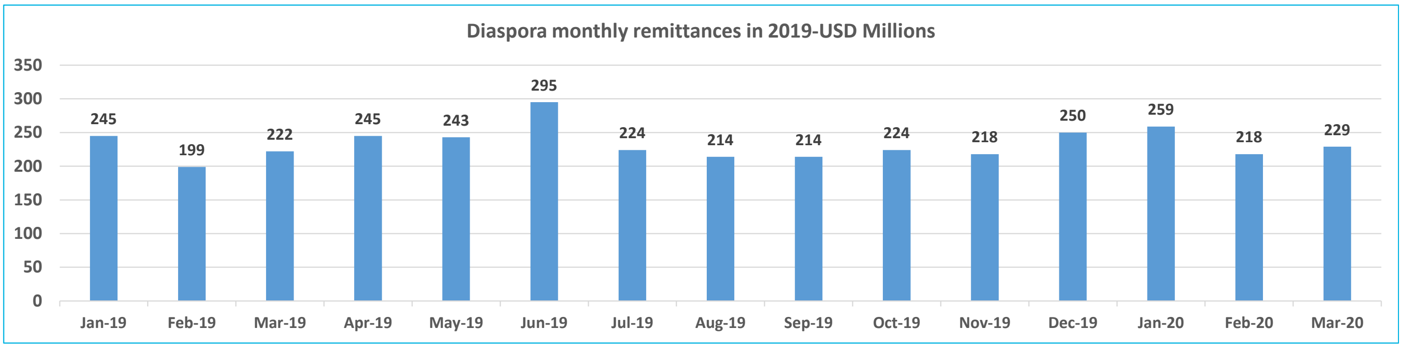
Source:
1. Growth estimates and economic contribution from CBK and Kenya Bureau of Statistics
2. Pandemic impact assessment is customized from an assessment done by Moodys

DIASPORA REMITTANCES



NOTES

1. Diaspora remittances have remained strong at about 3% of GDP since 2018
2. The economies of origination have projected a negative growth in 2020, hence the remittances will dwindle going forward
3. World Bank estimates decrease in diaspora remittances by 20%. This could be higher depending in extent of impact on originating economies.



COUNTRY	REGION	IMPORTS	EXPORTS
Uganda	Africa		8.2%
Tanzania	Africa		3.8%
Egypt	Africa		3.6%
Somalia	Africa		3.1%
South Africa	Africa	4.5%	
Pakistan	Asia	1.5%	8.5%
United Arab Emarates	Asia	7.4%	4.1%
China	Asia	23.0%	
India	Asia	9.8%	
Saudi Arabia	Asia	6.1%	
Japan	Asia	4.6%	
Indonesia	Asia	3.1%	
Netherlands	Europe		7.5%
United Kingdom	Europe		6.7%
German	Europe		2.6%
USA	USA	3.2%	8.7%

DISCLAIMER

This document has been prepared by SBM Bank Kenya Ltd for general circulation and is meant solely for information purpose, without taking into consideration any objective or goal of whoever is receiving this document. The material in this report has been sourced from various media, both local and international, believed to be reliable and in good faith by the Bank, but no representation or warranty, expressed or implied, is made as to their accuracy, completeness or correctness. Nothing in this material constitutes investment, legal, accounting or tax advice. SBM does not, in any way whatsoever, warrant expressly or impliedly the accuracy and completeness of the contents of this publication and shall not be liable for any loss or damage (including, without limitation, damages for loss of business or loss of profits) arising in contract, tort or otherwise suffered by any person / entity relying on the information contained in this report or arising from any shortcoming, defect or inaccuracy, through inadvertence or otherwise. This report has made various forward-looking statements with respect to the economy. By their nature, forward looking statements are based on assumptions and are subject to inherent risks and may not prove to be accurate. Readers are thus cautioned not to place undue reliance on forward looking statements. This report is owned by SBM Bank Kenya Ltd and no part of this publication may be reproduced or transmitted in any form or by any means, including photocopying and recording, or by any information storage and retrieval system without the permission of the organization.


SBM bank
THANK YOU