EXECUTIVE SUMMARY

- Global growth declined to 2.4% in 2015 as compared to a growth of 2.6% in 2014 according to a World Bank report.
- China's economy slowed down in 2015 to 6.9% down from 7.3% in 2014 making it the slowest growth for china in 25 years. The slowdown affected many countries especially the ones that export to China.
- Increased oil production across the world, rising fuel efficiency and collapsed consensus among oil producers have all contributed to the collapse of oil prices.
- Kenya's economy is likely to expand at a healthy pace this year on the back of public infrastructure projects, expected gains in most sectors and a stable Macro Environment.

GLOBAL ECONOMY

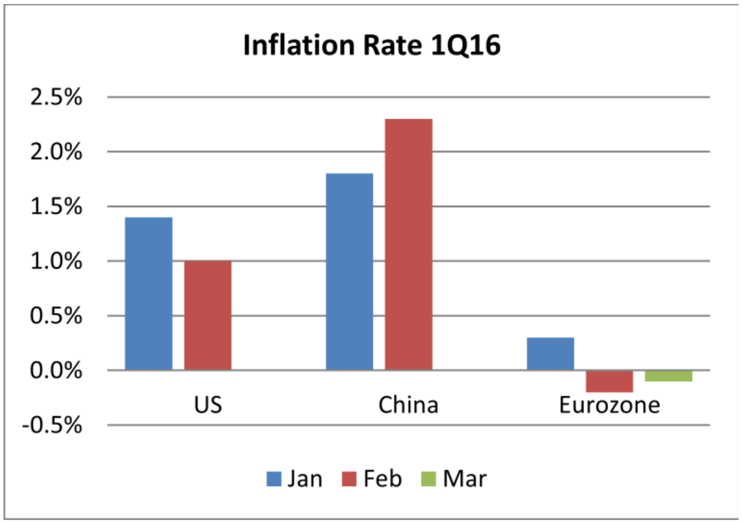
In 2015, the Global economy grew 2.4% decelerating from a growth of 2.6% in 2014. The weak performance was due to a growth decline in emerging and developing economies amid post-crisis lows in commodity prices, weaker capital flows and suppressed global trade. In 2016, World Bank projects a modest global growth at 2.9%.

World Bank Estimates for Selected Countries' GDP Growth

Economies	2015(es)	2016(f)
World	**2.4%**	**2.9%**
High Income	**1.6%**	**2.1%**
US	2.5%	2.7%
China	6.9%	6.7%
Eurozone	1.5%	1.7%
Emerging Markets	**3.7%**	**4.2%**
South Africa	1.3%	1.4%
Brazil	-3.7%	-2.5%
Developing Markets	**3.1%**	**3.7%**
Nigeria	3.3%	4.6%
Angola	3.0%	3.3%
Zambia	3.5%	3.8%
Zimbabwe	1.0%	2.8%
Egypt	4.2%	3.8%
EAC	**2.9%**	**5.8%**
South Sudan	-5.3%	5.8%
Uganda	5.0%	5.0%
Rwanda	7.4%	7.6%
Tanzania	7.2%	7.2%
Burundi	-2.3%	3.5%
Kenya	5.4%	5.7%

ANALYST CERTIFICATIONS AND REQUIRED DISCLOSURES BEGIN ON PAGE 21

ADVANCED ECONOMIES



Source: Bloomberg, AIB

The **United States'** economy recorded a growth of 2.5% in 2015 compared to 2.2% in 2014. With the fall in energy prices, investment in the oil and gas industry has plummeted even as consumers have spent only part of their savings from lower gasoline prices. As a result, the U.S. economy has received little overall gain from the decline. The U.S. central bank lifted borrowing costs in December for the first time in nearly a decade from 0.25% to 0.5%, but uncertainty over the impact on the U.S. economy of slower growth in China and Europe since the beginning of the year has driven policymakers to hold off on any further rate hikes since then. Purchasing Managers Index (PMI) stood at 51.8 in March 2016, up from 49.5 in Feb 2016 signifying an increase in production activity in the US economy.

China's growth rate in 2015 was recorded at 6.9% decelerating from 7.3% in the previous year making it the slowest growth for china in 25 years. The country's economy suffered the economic slowdown due to decreases in exports, as well as turbulence on the stock market that has erased hundreds of billions of dollars in wealth.

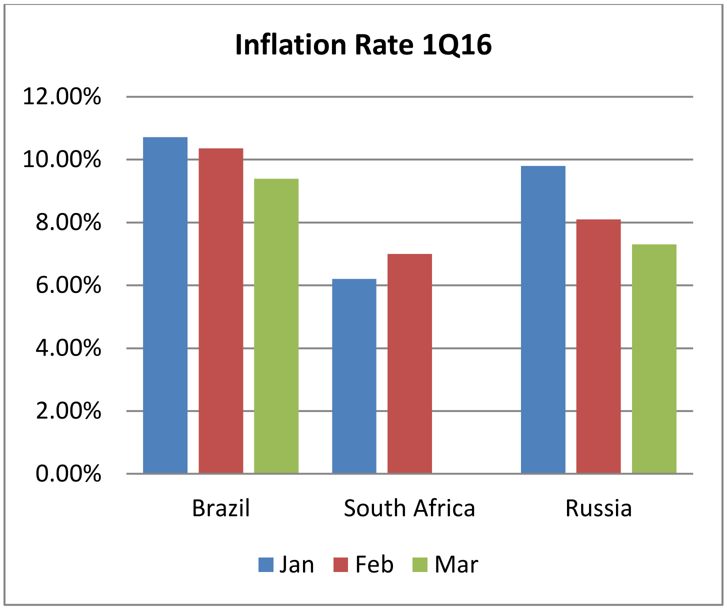
With growing debt and too much housing and factory capacity economists project a tougher year ahead. It is however expected that China will steer its economy to a more consumption and services-led growth. In a bid to halt the continued economic slowdown, China's parliament have approved a new five-year plan, laying out the economic and social development blueprint that sets a target of an average annual economic growth of above 6.5%. The Chinese Purchasing managers' index returned to growth in March 2016 for the first time since July 2015 coming at 50.2 from 49 in Feb 2016.

The **Eurozone** economy advanced 1.5% on average in the year 2015 compared to 0.8% growth in 2014. Diminishing fiscal consolidation and healing labor markets are underpinning domestic demand, although conditions vary across countries. The outlook for growth in 2016 now looks uncertain following the sharp falls in European equity markets, particularly of banking shares, since the start of the year. This setback to stock markets undermines consumer and business confidence and is likely to drag down growth. The slowdown in China and emerging economies, which account for a quarter of euro-zone exports, will also harm the recovery by hurting exporting companies.

In a meeting in March of this year, The European Central Bank in a bid to loosen the monetary policy decided to cut its main interest rate from 0.05% to 0% and cut its bank deposit rate, from -0.3% to -0.4%. They also stepped up the pace of quantitative easing (QE) from €60bn to €80bn a month. It propped the effect with unlimited four-year loans to banks at near-zero cost, hoping this will limit the damaging side-effects of negative rates for banks. The markets reacted wildly to this package of measures, which surged at first and then plummeted on creeping fears that the bank has exhausted its policy options and may be defenseless against a fresh shock.

EMERGING MARKETS

Emerging markets recorded a growth of 3.7% in 2015. That is almost half the growth registered in 2010 which stood at 7.5%. During the five years since 2010, these markets have recorded declining growth seemingly hitting the bottom in 2015. Factors leading to a declining growth include a combination of



*Source: Bloomberg, AIB, *Selected Countries*

Structural growth moderation in some of the larger countries and cyclical factors such as spillovers from weaknesses in advanced economies, changing external financing conditions and domestic policy tightening.

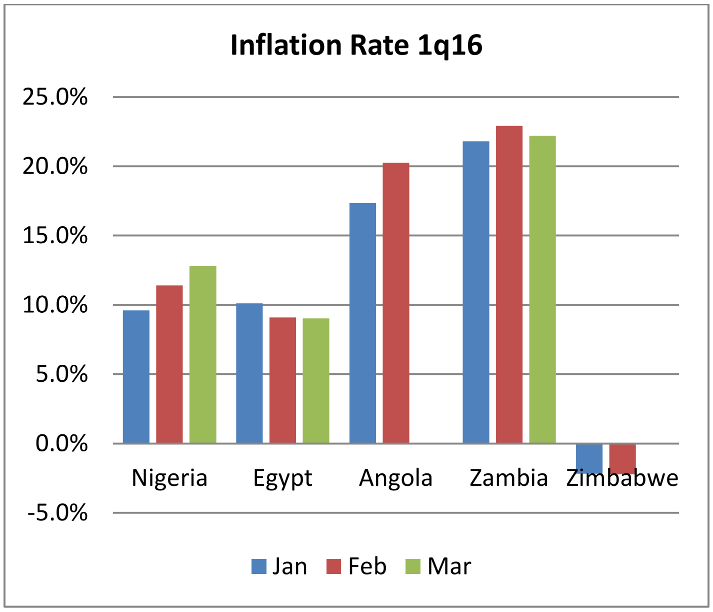
In **Brazil**, for example, economy suffered from the slowdown in commodities prices for things like oil, iron and copper. Brazil rapidly increased its exports to China over the past decade. That means the slowdown in China is extra painful for Brazil. Inflation in Brazil rose over 10%, the highest in 12 years. Brazil's currency is the worst performing currency among major emerging markets declining by about 31% against the dollar so far in 2016.

Also worth noting is **South Africa**. In December 2015, the country saw three finance ministers appointed in one week. The country's stock market dropped by nearly 3%, with finance shares plunging over 13% in the two days after the announcement. The rand lost 9% against the dollar, and government bonds slumped before the President re-appointed a much preferred finance minister. This saw the rand slightly bounce back 5% against the dollar and stocks recovered. But the market rebound did little to change the grim outlook for the South African economy.

A recovery is however expected for emerging markets with growth rate projected at 4.2% in 2016. Some of the main reasons for this are a stable oil and commodity prices. Many emerging markets depend on commodities like oil, iron and copper to power their economy. Low commodity prices aren't good for emerging markets, but stable prices are better than volatile ones. That stability could encourage investors to come back into emerging markets.

Another factor is the settling down of China's slowdown. Several countries were affected by this slowdown given China is the biggest market for goods produced by some nations. With the Chinese buying fewer goods or commodities, the net effect is a slow economy and low commodity prices in these countries. Like commodities, many experts believe China's growth may slow down more in 2016, but not at a faster pace. A more stable China bodes well for the countries that depend on it.

AFRICA



*Source: Bloomberg, AIB, *Selected countries.*

South Africa's economic prospects have seldom seemed so grim. The poor performance of the mining and manufacturing sectors has left the economy overly dependent on retail sales to support growth. With unemployment stuck at around 25%, debt elevated and consumer confidence still near multi-year lows. This is deemed unsustainable. Expectation is that the Reserve Bank of South Africa will tighten policy further in 2016 as food and energy prices push up inflation and the United States' Federal Reserve tightening means the rand will remain under pressure in 2016. A period of prolonged slow growth will put more pressure on South Africa's credit rating, which was recently downgraded to BBB- by international ratings agency Fitch.

Nigeria's economy will continue to struggle in 2016 as a result of low oil prices and high import costs. Growth in the economy in recent quarters has been significantly less than in previous years. Growth in the third quarter of 2015 was 2.84%, slightly higher than in the second quarter but still well below the average growth rate of 5.32 achieved between 2011 and 2014. This decrease can be attributed to the decline in the oil price as well as non-oil sectors that suffered setbacks during the year as political uncertainty coupled with supply shocks weighed on economic activity. Nigeria depends heavily on oil for both exports and government revenues, and therefore movements in the oil price have a large effect on the economy. Low oil prices have led to strains in the balance of payments and pressure on the naira. Nigeria remains a crucial economy for investors and remains a much better prospect over its great economic rival South Africa. This is because there is a tremendous long term potential and the current swings in commodity prices are expected to stabilize in future.

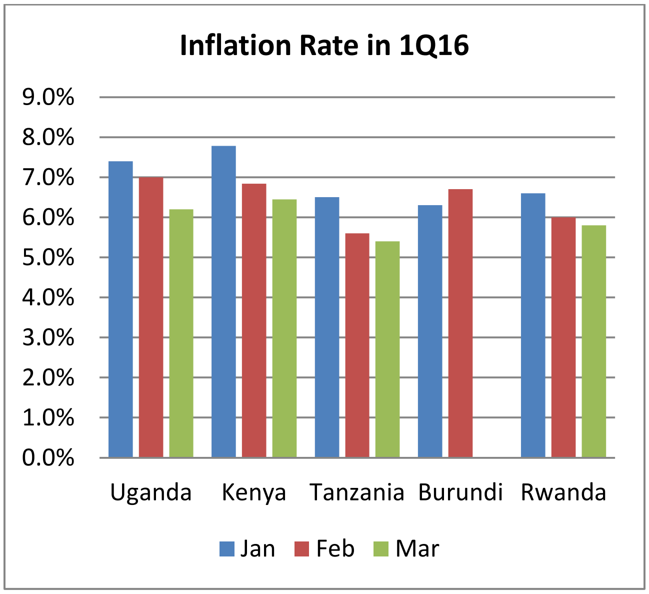
Like Nigeria, The **Angolan** economy has been hit hard by subdued oil and commodities prices. The government held talks with the World Bank in January to secure a USD 450 million loan, which could be available by June this year. In response to dwindling supply of U.S. dollars, the Central Bank has limited its supply only to strategic sectors of the economy, such as oil and health. The Angolan government has responded to sliding oil revenues by significantly cutting spending.

Zambia's economy grew approximately 3.5% in 2015. This is a smaller value compared to 5.6% recorded the previous year. The country is experiencing a sharp trade shock as low copper prices and mine shutdowns pummel export earnings. Export earnings have declined by almost 50% year-on-year while the currency has tumbled forcing the government to invite an IMF team for talks. Structural power shortages and a potential drought are likely to depress growth further in 2016.

Growth is likely to slip further in **Zimbabwe** in 2016 given the impending drought and depressed commodity outlook. Zimbabwe's trade deficit is likely to expand as export revenues fall sharply while imports remain stubbornly high. The World Bank expects Zimbabwe's GDP to grow by 2.8% on the back of infrastructural projects. Zimbabwe still has enormous potential for sustained growth and poverty reduction given its generous endowment of natural resources, existing stock of public infrastructure and comparatively skilled human resources. It's imperative that the re-engagement with the international community remains on track and is accelerated if Zimbabwe is to avert economic collapse.

Egypt's economic growth is forecasted to slow to 3.8% in fiscal year 2016 from 4.2% expected in 2015, according to World Bank. This is driven by a large drop in exports driven by faltering activity in the tourism sector amid persistent security concerns. A foreign currency shortage facing Egypt's economy in recent years is also expected to persist through at least part of the current fiscal year, contributing to the low forecast. The contraction in foreign currency inflows that would accompany a shrinking tourism industry would not only negatively impact growth, but would aggravate the existing foreign currency shortage. Nonetheless, World Bank expects growth to pick up in later years, driven by investment.

EAST AFRICAN ECONOMIES



Source: Bloomberg, AIB

Global inflation is likely to remain subdued due to excess capacity and the projected low commodity prices, especially oil prices. Overall, expectation is stable EAC currencies in 2016 compared to 2015, though occasional currency turbulences cannot be ruled out given the differences in monetary policies in major global economies. Alongside we see the graph of Inflation rate for the EAC countries (*Excluding South Sudan)*

South Sudan

The monthly CPI increased by 17.8% to 517.1 February 2016 from 438.8 in January 2016. Over this period the price for food and non-alcoholic beverages increased by 18.2%, health decreased by 4.2% and restaurants and hotel decreased by 1%. The increased in the price of food and non-alcoholic beverages was mainly caused by higher prices in bread and cereals.

Also South Sudan's annual inflation rate surged to 109.9% in December 2015, as food, clothing, alcoholic beverage and utility costs increased. Given that more than 90% of South Sudan's government revenue is generated by oil sales, Low global oil prices meant substantial losses in government revenue for South Sudan. In the same December, the country devalued its currency by 84% as the authorities abandoned their fixed peg for a floating rate, surrendering to prices charged in the black market and which had made well-connected South Sudanese rich as they traded on the difference with the official rate. In a bid to improve their economic welfare, the government and rebels agreed a power-sharing formula in the beginning of the year that is expected to stabilize the country ahead of elections expected in early 2018. The country is also expected to benefit from its recent inclusion in the East African Community due to ease of trade.

Uganda

The annual headline inflation has been on a general downward trend in the first three months of the year. The main driver was the Annual Food Crops Inflation which decreased by 6.8% on average for the first quarter this year. In addition, the Annual Energy, Fuel and Utilities (EFU) Inflation decreased to 7.9% on average for the first quarter too. The CPI Index however increased marginally averaging 157.19.The International Monetary Fund (IMF) revised Uganda's growth forecast for the 2015/16 fiscal year to 5% from the 5.8% it predicted in May. The cut in GDP is attributed to the global and regional challenges, the sharp shilling depreciation driving and an increase in inflation. Supported by public investment, real GDP growth reached 5% in 2015 and is expected to remain at that level in 2016. The Bank of Uganda's last year tightened policies in response to rising inflation and also continues to monitor the financial system, which remains sound despite increased vulnerabilities. Thus we forecast a stable outlook for Uganda going to the second quarter.

Tanzania

Latest data from the Tanzanian National Bureau of statistics show that the annual headline inflation decreased to 5.6% from 6.5% in January. The CPI however increased marginally to 101.44 from 100.71 in January. Annual Food and Non-alcoholic beverages index was the main factor for the changes according to the statistics. The economy gained steam in the last quarter of the year 2015 and expanded 7.1% in annual terms. According to World Bank, Tanzania was among several countries in Africa which have posted robust economic growth despite weak global economic conditions. The newly elected President Magufuli cracked the whip on several government agencies effectively reducing wasteful expenditure that was eating a huge portion of tax payer's money. The country's economic growth is expected to remain close to 7% in 2016.

Rwanda

Rwanda's Inflation dropped to 6% in the month of February from 6.6% in January. The country however recorded an increased CPI of 105.2 from 104.7 mainly due to the rising prices of Food and non-alcoholic beverages index by 8.1% YOY, 'Housing, water, electricity, gas and other fuels by 2.8% and 'Transport' by 5.1%. Rwanda, one of the smallest economies in Africa, has been able to make important economic and structural reforms and sustain its economic growth rates over the last decade. Growth in 2015 was slightly stronger than expected and inflation remained contained as revenue collection and budget execution were broadly in line with expectations. Also due to recent declines in international commodity prices export receipts have reduced substantially. Mining activity in Rwanda has already been affected, with exports for 2015 and the near term forecasted to drop substantially. Looking forward, Rwanda's policies should remain focused on sustaining high growth through growth-enhancing public investment, encouraging private investment, and diversifying exports.

Burundi

Latest Statistics shows that Burundi's Consumer Price index remained flat at 110.4 in February from 110.3 January. Inflation however increased marginally to 6.7% in February from 6.3%. The main factor was food inflation that increased to 10.9% from January. The country has been in turmoil since the incumbent president Nkurunziza said he would run for a third term in office. The uncertainty caused growth to shrink by an estimated 7.5% in 2015 to a negative value of approximately -2.3%. Revenue collection dropped 10% in 2015 due to the political unrest. Despite all this, World Bank forecasts Burundi's economic growth to expand by 3.5% betting on the security situation to improve and a revival of economic activities, especially the industrial sector.

THE KENYAN ECONOMY

Kenya will be one of the few bright spots in Sub Saharan Africa and is generally considered the economic, commercial, and logistics hub of East Africa. Kenya has benefited from low oil prices, which caused the country's trade deficit to narrow in late 2014 and early 2015. The IMF projects Kenya's economy in 2016 to expand by 5.9%, a better prospect to the 5.3% growth recorded in 2015. The major growth drivers are expected to be agriculture, real estate and financial services, other sectors to watch are that of transport and communication.

Infrastructure spending such as that of the Standard Gauge Railway is expected to ease congestion and reduce the time taken to transport goods to different parts of the country and those on transit while the cargo handling infrastructure at the Mombasa port has already boosted port traffic by 7.5% in 2015 by reducing the turnaround for ships.

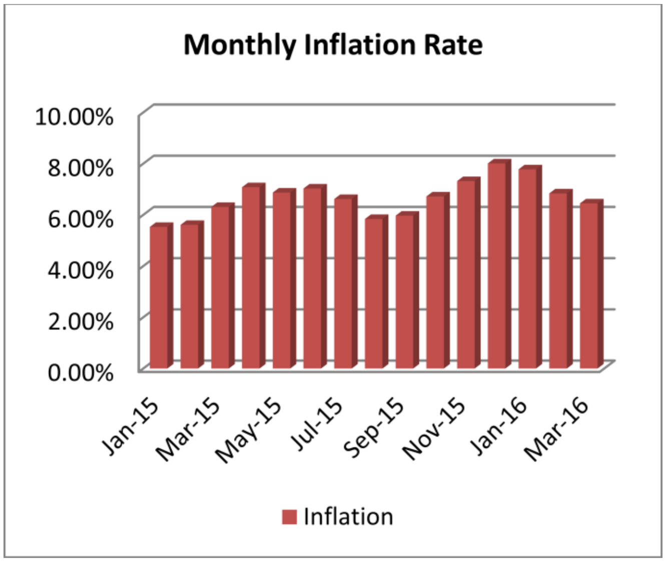
Current Infrastructure development is also expected to greatly boost the services sector which will continue to be a large contributor to GDP growth and foreign exchange revenue.

Macro-Economic Indicators

Inflation

The overall inflation rate dropped further in the month of March to a six-month low of 6.45% down from 6.84% in February 2016.

The modest reduction is attributed to a decline in petrol and diesel prices and transport costs. Fuel prices have generally been on a downward trend from mid-2014. In 2016, fuel prices have traded at between 27-42 per barrel. Kenya as a net importer of oil has benefited from this reduction reflected on the reduced cost of electricity and fuel prices. Expectation is that oil prices will remain at their current levels going into the second and third quarter of 2016.



Source: KNBS, AIB

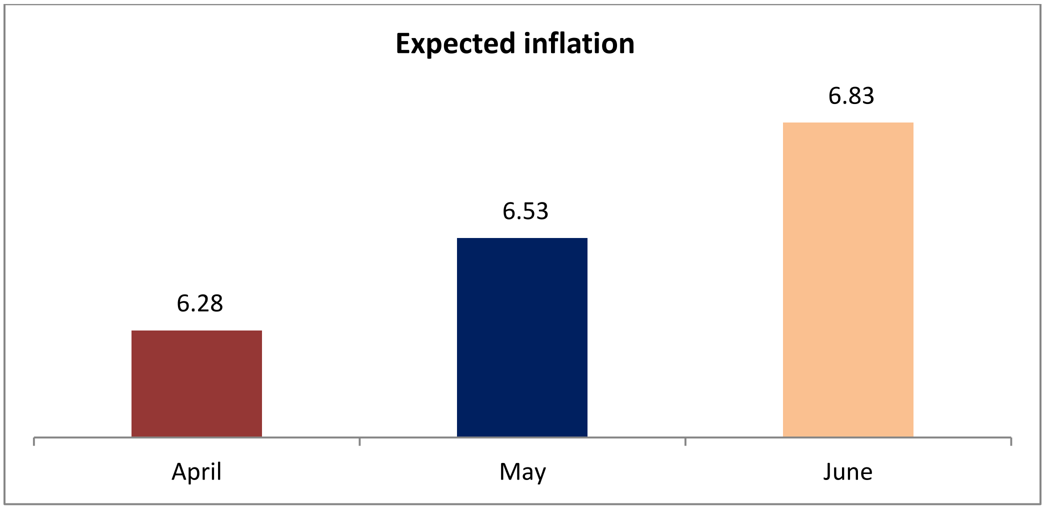
Global oil prices are still low hence keeping fuel and transport costs lower. We also do not expect to see increases in electricity costs due to the current lower fuel costs, reduced thermal usage as well as the expected increase in generation from hydro plants in this long rains season.

Food and Non-Alcoholic Drinks' Index increased by 1.39% due to significant increases in food prices mainly cabbages, Irish potatoes, peas and fresh packeted milk.

Millers have warned that the prize of maize flour may increase in the coming weeks following a grain shortage. The price of 2kg packet of maize flour has increased by an average of Kshs 5 over the past 2 months on high maize costs whose prices have increased to Kshs 2,500 per 90 kg bag from Kshs 2,000.

We expect the food index to continue the upward trend in April, May and June due to the dry season experienced in the first quarter of 2016. Maize prices are also expected to be on an upward trend upto August 2016 when the next harvest is expected.

The increase in food prices is however expected to be offset by a decrease in fuel, electricity and transport costs thus maintaining inflation at stable levels i.e. between 6.28%-6.83%.



Source; AIB estimates

The expected higher food prices will mainly affect the lower income groups where the rate of inflation is expected to be higher compared to the middle and upper income categories.

Currency

The Kenyan Shilling recorded mixed performance within the 1st quarter of 2016 closing at Kshs. 102.29 to the US dollar. The best performance was recorded in the month of February mainly aided by donor inflows into the country plus revenues from the tea and tourism sector. The decline in global fuel prices has significantly reduced the import bill thus easing pressure on the shilling. The CBK's foreign exchange reserves also ended the first quarter of 2016 at USD 7.377 million (4.7 months of import cover) hence continuing to provide an adequate buffer against short term shocks.

On the global front, the Kenyan shilling has recorded some slight improvement in comparison to other major currencies in the first quarter of 2016.

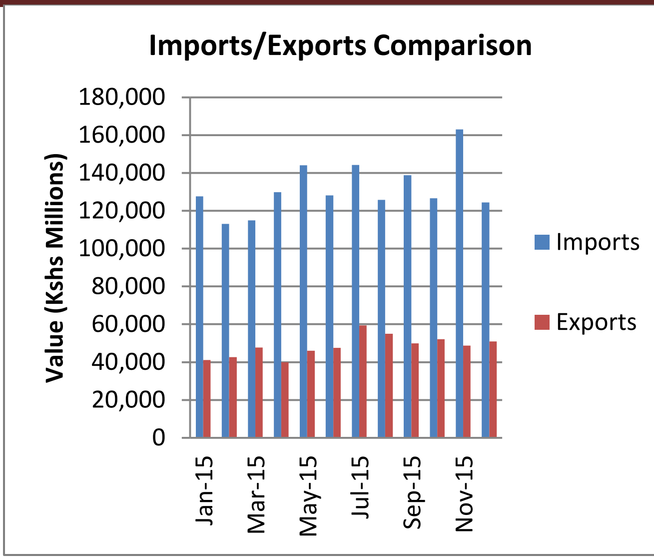
	31-Dec	29-Jan	29-Feb	31-Mar	MoM% Change	YOY% Change
USD/KES	102.31	102.28	101.70	102.29	0.58%	-0.01%
EUR/KES	111.78	111.68	111.48	111.72	0.22%	-0.05%
GBP/KES	151.80	146.57	141.56	151.68	7.15%	-0.08%
JPY(100)/KES	84.97	86.03	89.48	84.97	-5.04%	0.00%
YUAN/KES	15.75	15.55	15.55	15.75	1.31%	0.02%
RUPEE/KES	1.54	1.50	1.48	1.55	4.47%	0.40%
KES/UGX	32.99	33.95	32.97	33.09	0.37%	0.31%
KES/TZS	21.11	21.39	21.51	21.12	-1.83%	0.03%
RAND/KES	6.58	6.31	6.36	6.55	3.06%	-0.39%

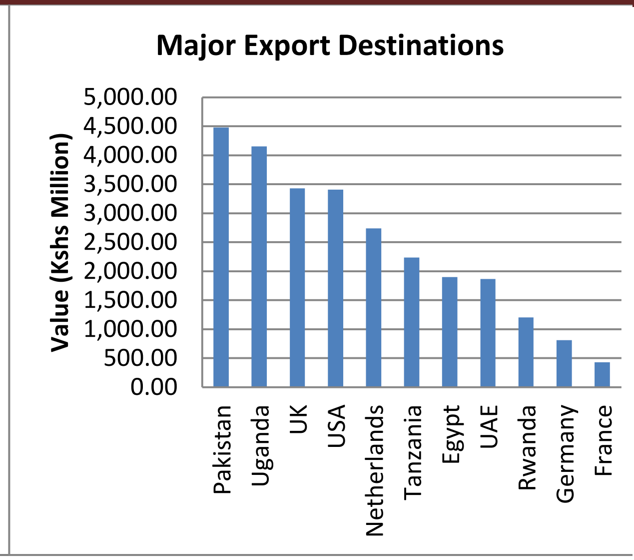
Source: Central Bank, AIB

Going to the second quarter, we expect the shilling to remain stable. The fundamental pressure on the shilling however still remains given ongoing infrastructure spending. CBK monetary policies, increased donor and diaspora remittances, increased agricultural inflows and the lower fuel prices are expected to temporarily cushion the shilling against any shocks.

Balance of Trade

Latest data from the Central Bank of Kenya shows that last year, Kenya recorded the highest monthly trade deficit in November at Kshs 114 billion. The trade deficit in Dec 2015 was 73.6 billion, a significant improvement. On average, monthly trade deficit stood at Kshs. 83 billion in 2015, a drop from Kshs. 90.6 billion the previous year, The average volume of trade slightly increased by 8.39% to 180 billion from 179.6 billion in 2014. The decrease in deficit means that the value of exports increased mainly due to a weaker shilling and lower oil prices.

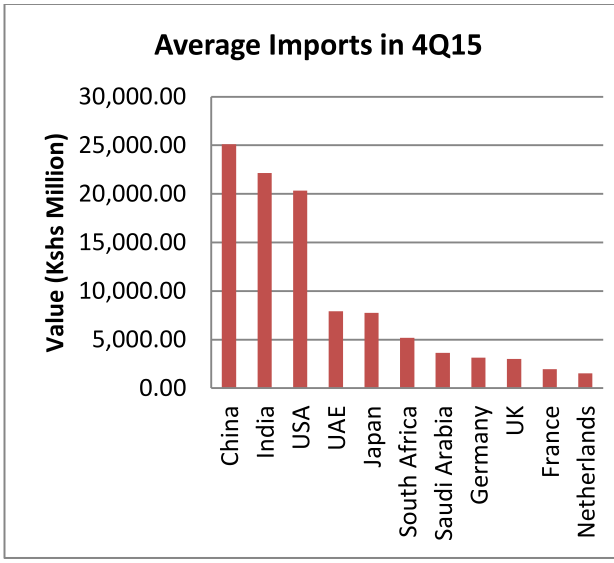


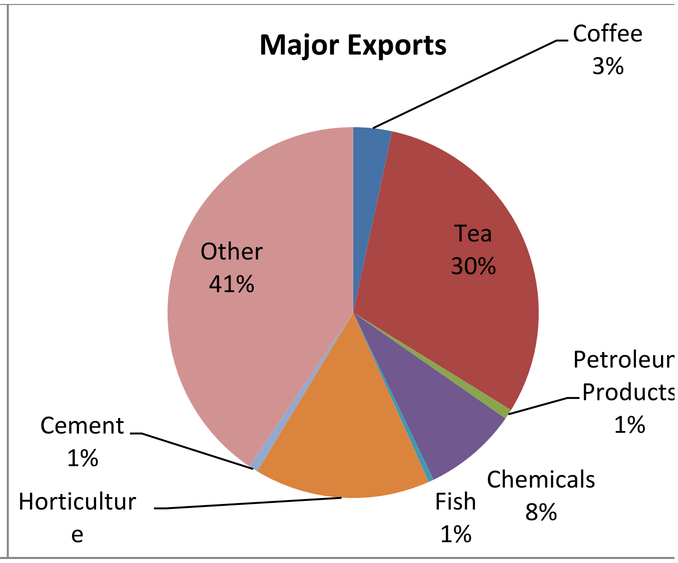


Source: KNBS, AIB

The major destination for Kenya's export has always been Uganda, although recently in November 2015, the value of Kenyan exports to Pakistan surpassed Uganda mainly due to a stronger Kenya shilling in 2015 compared to its counter parts in the East African region as well as an increase in exports to the Middle East countries. Exports to the Middle East are expected to continue in the future mainly supported by the lifting of sanctions against Iran which is expected to take in more exports from Kenya including beverages and livestock. From the graph above we can compare Kenya's main export destinations as at end of 2015.

Agricultural products are central to Kenya's export industry with tea being the single largest export followed by horticulture. Other export items include textiles, coffee, tobacco, iron and steel products, petroleum products, cement. Kenya imports mostly machinery and transportation equipment, petroleum products, motor vehicles, iron and steel, resins and plastics.

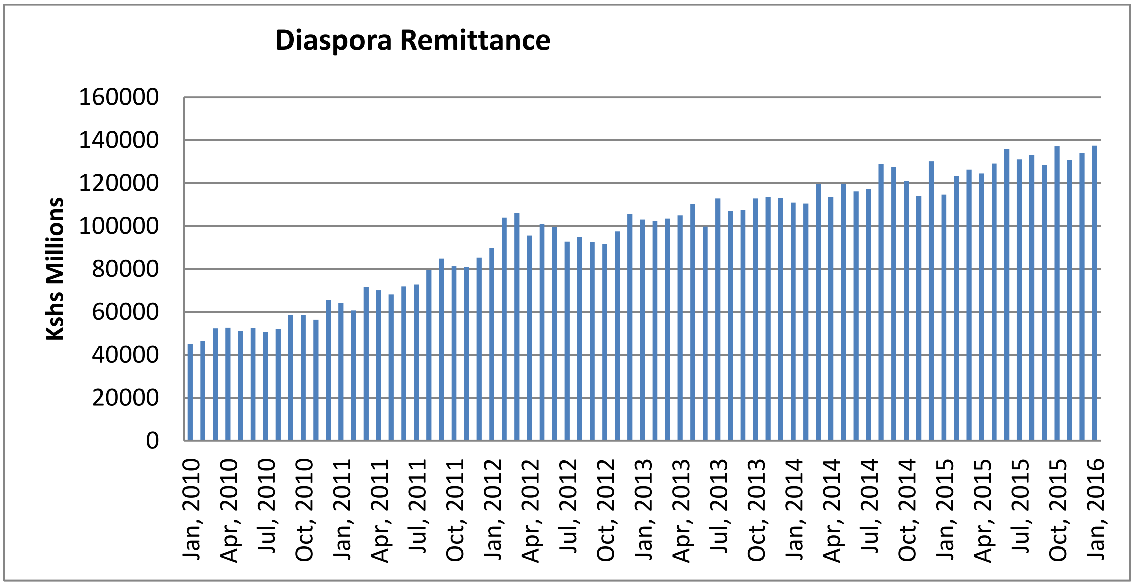




Source: KNBS,AIB

Diaspora Remittances

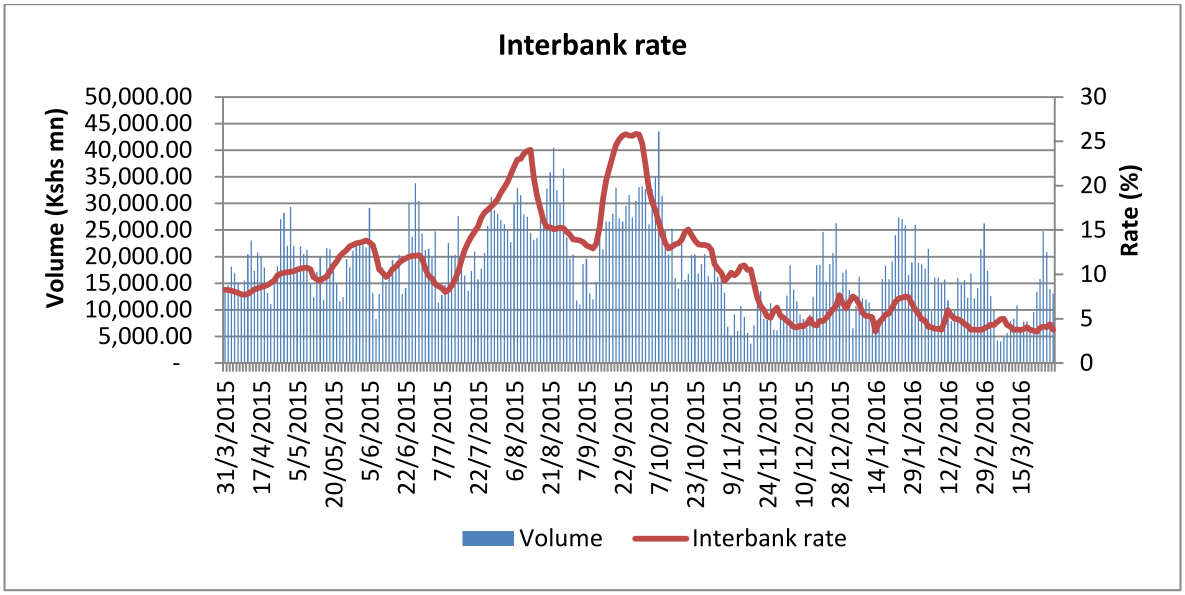
Kenya's Diaspora remittances hit an average of Ksh12.9 billion shillings in 2015. In January this year, diaspora remittances stood at Ksh13.7 billion. Data from the Central Bank of Kenya (CBK) indicates that diaspora remittances have been rising consistently since 2010 despite the volatile economic environment in the US and Europe. Remittances inflow increased by 17.99% in 2015 to stand at 168.5 billion shillings from 142.8 billion shillings compared to 10.7% growth in 2014. The rise is attributed mainly to government efforts in encouraging Kenyans living in the Diaspora to invest in government securities. These remittances other than bringing a relief to the local shilling have consequently become a key source of foreign exchange alongside tea, horticulture and tourism. Diaspora remittances have contributed more than KES 700 billion to the Kenyan economy in the last 5 years and the trend is expected to continue into the future more so as Kenyans living abroad are investing in real estate in the country.



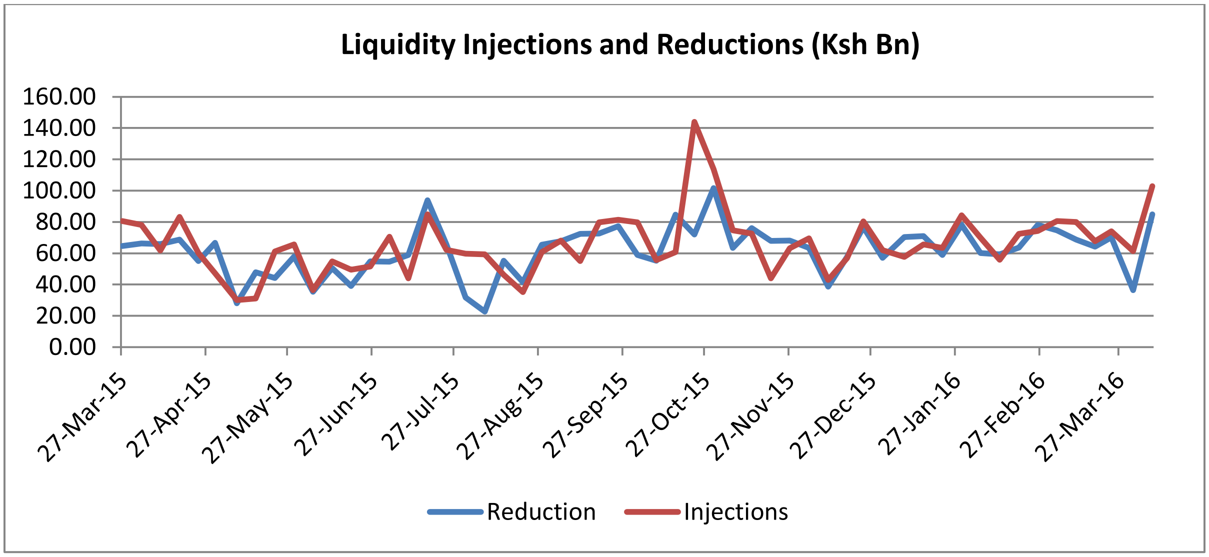
Source: Central Bank, AIB

Liquidity

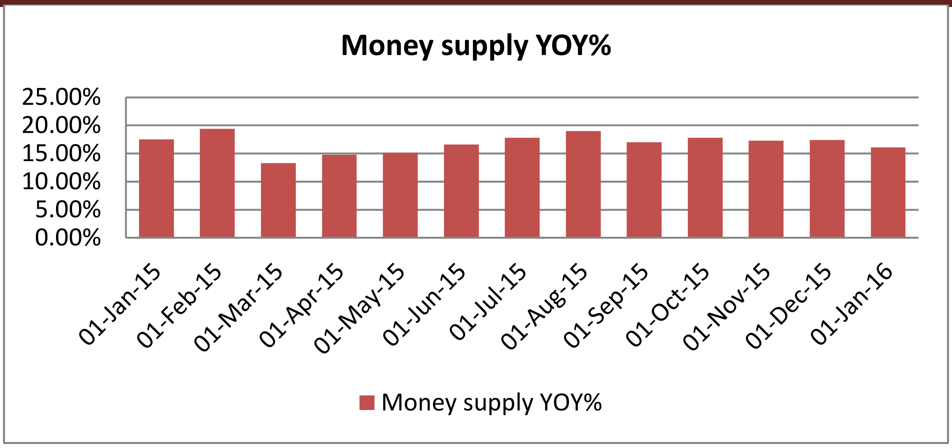
The money market was very liquid in the first quarter of the year exhibited by a lower interbank rate which averaged 4.86% compared to 9.55% in the previous quarter and 6.89% in the same quarter last year.



Government maturities were also high in the first 3 months of the year with a net injection of Ksh 71 billion. The high maturity trend is expected to continue into the 2nd and 3rd quarter of the year as the highly subscribed 182 and 364 papers bought during the high interest regime last year mature.



Money supply growth (M3) flattened in the 4th Quarter of 2015 having gone through fluctuating perches in the 1st half of the year.



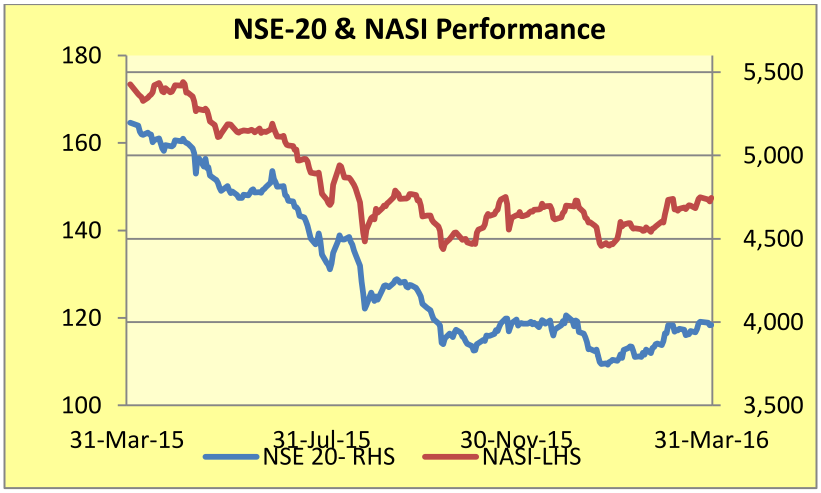
Source: Bloomberg, AIB

Equities Market

Capital gains tax, high inflation, increased interest rates and low foreign investor participation were the major highlights of the Stock Market in 2015. The market slump eroded the wealth of a number of investors last year tipping the scales in favor of a bear run. Last year the combined investor wealth lost was Ksh. 255 billion by market capitalization. The NSE-20 and the NASI also dipped 21% and 11% respectively. The decline however provided an opportunity for investors looking to enter the market at good bargains.

Turnover in the last quarter of 2015 was the lowest in the year standing at a 732 million average attributed mainly to the huge foreign investor outflow during the second and third quarter of 2015 on account of increased inflation and interest rates. In the first quarter of 2016, the bear run seems to have spilled over since the average turnover declined further to 590 million. This could be attributed to investors trading cautiously since most listed firms are releasing their end of year 2015 results. Last year saw up to 18 of the 62 listed firms declaring a profit warning due to a rough operating environment.

On the flip side, the NSE 20 and the NASI having dropped slightly in January picked themselves up relatively well during the remaining two months of the quarter closing at 3982.09 and 147.44 respectively. Below we can see the performance in Q1 of 2016.



Source: NSE, AIB

	29-Jan	29-Feb	31-Mar	MOM% Change
Equity+I Reit Turnover (KES)	779,109,991	254,657,290	612,759,773	140.62%
Total Volume Traded	17,619,624	8,767,091	33,305,810	279.90%
Market Cap (KES)	1,926.47	2,000.21	2,078.28	3.90%
Bond Turnover	1.11	1.80	2.12	17.58%
NSE 20 share Index	3,773.17	3,862.24	3,982.09	3.10%
NSE All share Index	136.81	142.03	147.44	3.81%
FTSE NSE Kenya 15 index	173.10	179.29	186.21	3.86%
FTSE NSE Kenya 25 index	173.45	179.73	186.57	3.81%
FTSE NSE Kenya Govt. Bond Index	89.03	88.84	89.28	0.50%
Foreign buys	610,323,589	103,574,913	461,169,500	345.25%
Foreign sales	339,386,886	188,231,414	174,871,153	-7.10%

Source: NSE, AIB

Fixed income market

Public debt

Figures from the Central bank show that Kenya's total debt hit the Ksh. 3 trillion-mark late last year closing 2015 at a Ksh. 3.155 trillion. Domestic debt closed at Ksh. 1.62 trillion while external debt was at Ksh. 1.54 trillion. Over the first quarter of this year, the government issued a 2-year treasury bond and re-opened a 5-year bond, three 10-year bonds and a 15-year bond totaling to Ksh. 85 billion. In addition to this the government raised more cash through treasury bills with offered amount at Ksh. 192 billion. In March of this year, Kenya secured a precautionary debt of 1.5 billion dollars from IMF to be utilized in the next 24 months in case of external shocks. IMF reiterates that Kenya has room to borrow more and spend on infrastructure as long as the projected revenues are realized.

Treasury Bonds

Q1 2016 T. Bond issues

	Offered (Billion)	Performance Rate	bids (Billion)	Weighted Average of Successful Bids
January				
2-Year (New)	35	105.25%	30.39	15.76%
10-Year (Re-Opened)			5.937	16.13%
February				
5-Year (Re-opened)	25	226.09%	29.69	13.95%
10-Year (Re-Opened)			26.83	13.92%
March				
10-Year (Re-Opened)	25	104.72%	13.71	14.39%
15-Year(Re-opened)			12.47	14.98%

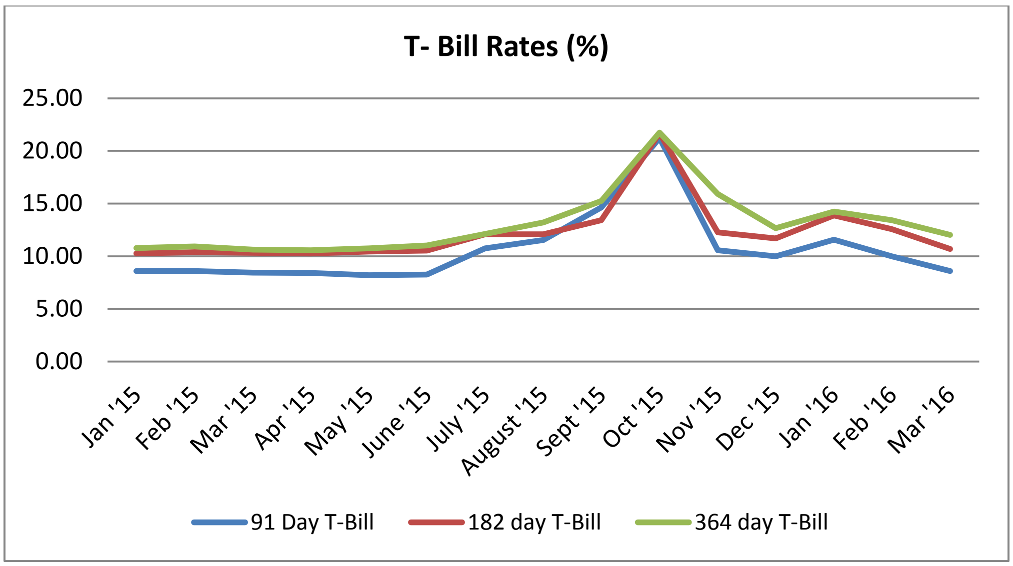
Source: Central Bank, AIB

The secondary bond market was more active at the bourse compared to the equities market as investors were seeking more guaranteed returns. Particularly in the month of March, average daily bond turnover stood at Kshs 3.29 billion compared to the previous month's turnover of Ksh 1.21 billion. On average, the daily bond turnover increased by 67% in Q1 to Kshs 1.88 billion from Kshs 1.12 billion in Q4 of 2015. The FTSE bond index however showed a more flat performance in the quarter with an average of 89.16.

Treasury bills

In 2015, T-bill rates were fairly stable for the first 6 months of the year then started to rise reaching its all-time high in October 2015 where the average T-bill rate was 22.26%. The spike in T-bill rates was directly linked to the government's borrowing 'spree' which also saw bank lending rates escalate to extreme highs hurting borrowers.

In the first quarter of 2016, demand for the 1-year T-bill security was consistently higher than the 91-day and 182-day T-bills. This was attributed to stable higher rates and falling inflation. The low participation in the two short term rates is also an indication that investors are expecting rates to remain low and stable in the short term. The rate for the 91-day T-bill at the beginning of the year stood at 10.85% with performance rate of 52.24% while the 182-day T-bill rate was at 12.76% with 56.51% performance rate. The 1-year T-bill rate then stood at 13.25% with 77.22% performance rate surpassing the demand for the other two shorter term securities. At the end of the quarter, the 91-day and 182-day T-bill rates stood at 8.41% (92.69% performance rate) and 10.73%(42.45% performance rate) respectively while the 364-day T-bill closed the quarter at 11.89%(72.76% performance rate) still a slightly higher demand than the other two securities.



Source: Central Bank, AIB

Interest rates

The central Bank of Kenya committee having met in mid-march retained the benchmark lending rate (CBR) and Kenya Banks Reference Rate (KBRR) steady at 11.5% and 9.87% respectively for the sixth consecutive time. The committee noted the need to anchor inflation, maintain overall price and financial sector stability. Market expectation was this value would be cut owing to the stability of the shilling and lower inflation. Due to the stability this rates are likely to spill over to the second quarter. The KBRR is computed as an average of the Central Bank Rate (CBR) and the two-month weighted moving average of the 91-day Treasury bill rate. The KBRR came about due to efforts by the CBK to deal with high interest rates set by banks. In February, the Central Bank of Kenya published average bank lending rates on its website showing the most expensive and least expensive lenders as a way to keep consumers aware.

The interbank rate is currently at the lowest point closing the quarter at 4.3720%. On average in quarter one of 2016 the rate was 4.91%, a huge improvement from the 9.55% recorded in Q4 of 2015. The average rate was also better than the 2015's Q1 figure of 6.89%.

Due to the stable exchange rate and the current low levels of inflation, the yields should is expected to remain at the current levels in the short term.

Other Major Factors

Tourism Activity

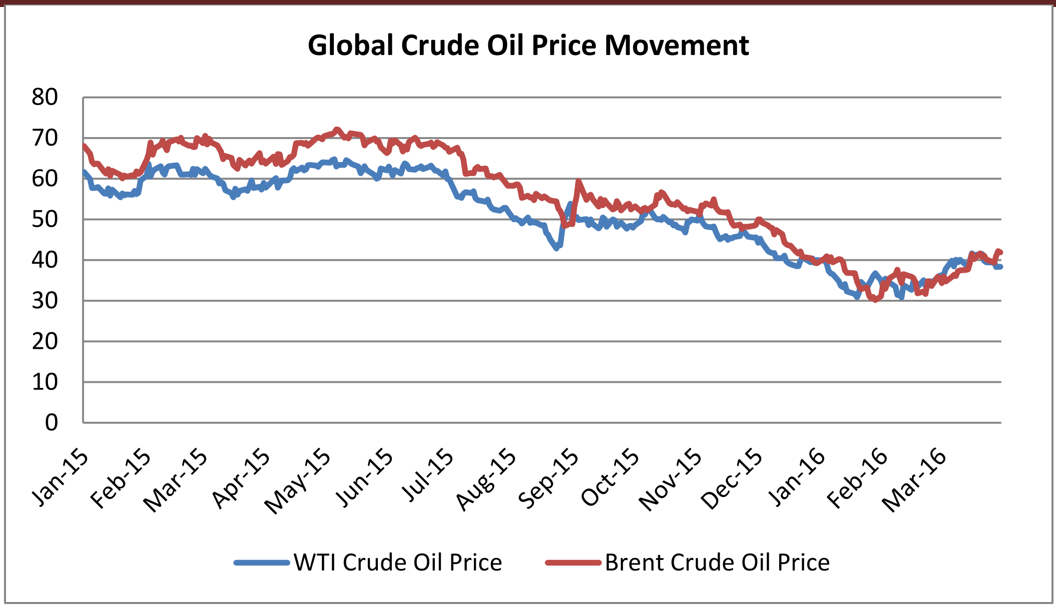
The tourism sector could experience a recovery this year as the state rolls out a list of new incentives to encourage local and foreign tourists visit wildlife parks and other scenic attractions. The country remained a prized tourist destination thanks to dramatic improvement of its image abroad as well as improved security. Kenya's tourism, especially at the Coast which accounts for almost 60% of all arrivals, suffered near collapse with terrorism two years ago. According to data from the Kenya bureau of Statistics, new tourist arrivals last year dropped to 13% to 748,771 from 861,369 in 2014 on the back of increased insecurity in the country.

Kenyans brand visibility was raised to new levels following high profile visits last year notably the President of the US visit. Recent policies and incentives implemented that include the creation of a standalone ministry to market the country, plus lifting of travel advisory bans by European countries will provide a cushion the industry from jitters about the 2017 General Election. Traditionally, fear of political instability in the run up to elections has spurred a slowdown in tourists visiting the Kenyan Coast, Kenya's main tourist catchment area.

Recovery of tourism will accelerate this year against a backdrop of improved security and state incentives. The announcement by the president on the waiver of park fees is a welcome move, and we expect more tourists in the parks and other wildlife areas. The move will also boost wildlife protection in the country. County governments are also running aggressive campaigns to showcase their regions as business and tourism hubs to the world. This is unlocking new avenues for tourism growth.

Oil Prices

So far in 2016, global oil prices have varied between $27 and $42 per barrel. Increased oil production across the world, rising fuel efficiency and collapsed consensus among oil producers have all contributed to the collapse of oil prices. We expect the global oil prices to remain at their current low levels in the next quarter of 2016.



Source: Bloomberg, AIB

Crude oil prices having hit 12-year lows, motorists expected these benefits to trickle down. The price of petroleum products in Kenya is not set by market interactions but by a formula that is set by the ERC.

EAC	Price (USD)
Tanzania	0.87
Kenya	0.91
Uganda	1.04
Rwanda	1.17
Burundi	1.24

Source: Bloomberg, AIB

According to ERC, half the amount Kenyans pay for fuel goes to at least seven Government taxes and levies. This means that even if the oil prices drop in the international market, it will only reflect on the Kenyan pump prices to some extent due to taxes. However an East African comparison shows that as at March, Kenya charged the second cheapest for petrol at 0.91 USD per litre following only Tanzania that charges slightly lower at 0.87 USD per litre.

East African Community Stock market integration

In January of this year, the officials from all the five East Africa Community member states while on a consultative meeting in Kigali agreed on a roadmap harmonization of the stock markets. Essentially what this means is that an investor with a CDS account in Kenya, for example, will be able to trade stocks in other East african countries without having to open another account in the other country. The argument was that international investor's no longer look at individual countries, but rather the region when making investment decisions. The integration of the EAC exchanges has the potential of attracting foreign direct investments into the region, which will translate into increased efficiency and faster growth of East African economies.

Introduction of Derivatives, GEMS, REITS at the Bourse

The NSE is on course to launch the derivatives market this year. This market will provide Kenyans with financial instruments that will enable them hedge their currency and investment risks. In addition, it will create a new investment opportunity for the local and international investors. The Exchange will also be launching Exchange Traded Funds (ETFs) which will target investors seeking investments in low volatile and cost effective opportunities.

The Exchange will also be seeking to increase the number of listings on all our market segments with focus on the Growth Enterprise Market Segment (GEMS) and the Real Estate Investment Trusts (REITS). During the year, the Exchange will also be upgrading the Automated Trading System (ATS) which will allow it to offer more availability to its trading members and better support its new product and service offerings.

Improved financial Inclusion

The number of Kenyans formally included by the financial system has grown by 50% in the last ten years. Over three-quarters (75.3%) of Kenyans are now formally included, up from 66.8% in 2013. Financial exclusion, which is now down to 17.4%, has more than halved since 2006. The three previous surveys of 2006, 2009, and 2013 have shown that Kenya has made significant progress in fostering financial inclusion, with the latest survey providing a ten year perspective on Kenya's financial landscape.

According to the 2016 report, growth in bank accounts has been driven by mobile bank accounts e.g. Mshwari and KCB M-Pesa while conventional bank savings accounts have decreased over the last decade. Mobile financial services and, to a lesser extent, informal groups are widely used by all livelihood categories. Those in salaried employment are intensive users of all financial services (MFSs) and are by far the dominant users of banks, insurance and SACCOs. While the dominant use of mobile financial services is still for interpersonal transfers, 42% of consumers use these services to make livelihood payments, interact with their financial institutions and pay for goods and services.

Kenyans most value their mobile financial services accounts and saving in a secret place. The most valued features of financial instruments are accessibility, use during emergencies and trust.

Construction boom in Kenya

Demand for commercial property is increasing because of rapid population growth, urbanisation and economic development in the country. This includes mixed-use developments, shopping malls, retail space and office units. Industry professionals have already noted the increased attraction of commuter towns in urban areas. Rapid population growth has led to physical growth of urban areas in towns including Ruaka, Thika, Kitengela, and Ongata Rongai. As Nairobi become slowly saturated, real estate developers and investors alike are turning their attention to fast-rising emerging urban areas like Meru and Kisumu amongst others where property is significantly cheaper as a result of higher land availability and lower building costs.

The last couple of months have seen a number of real estate investment trusts opening in the emerging markets, encouraging investment into the sector. In October last year, the Capital Markets Authority approved Kenya's first income REIT [I-REIT] by investment manager Stanlib Kenya. These projects are not only driving economic growth, they provide employment opportunities, and boost the value of surrounding properties. The government is also involved in a number of huge infrastructure projects among them the Standard Gauge Railway, Lappset project, Dongo Kundu Free Port, 220Kv Suswa Mega Substation and the upgrading of the Nairobi Public Transport system.

These projects are expected to improve the economic welfare of the country including reducing the ballooning debt deficit if the returns are realized.

Outlook

As from the topics above most economic indicators in the first quarter point to a positive outlook for Kenya going forward. The country's economy is likely to expand at a healthy pace this year on the back of public infrastructure projects and robust gains in most sectors, aided by a fast recovering tourism industry. General growth is also expected to slow down towards the end of 2016 in anticipation of 2017 elections.

However, few issues still constitute a risk to Kenya's macro-stability. This includes a large fiscal and current account deficits, an uncertain business environment as we approach the election year and run-away corruption at the helm of the country's leadership.

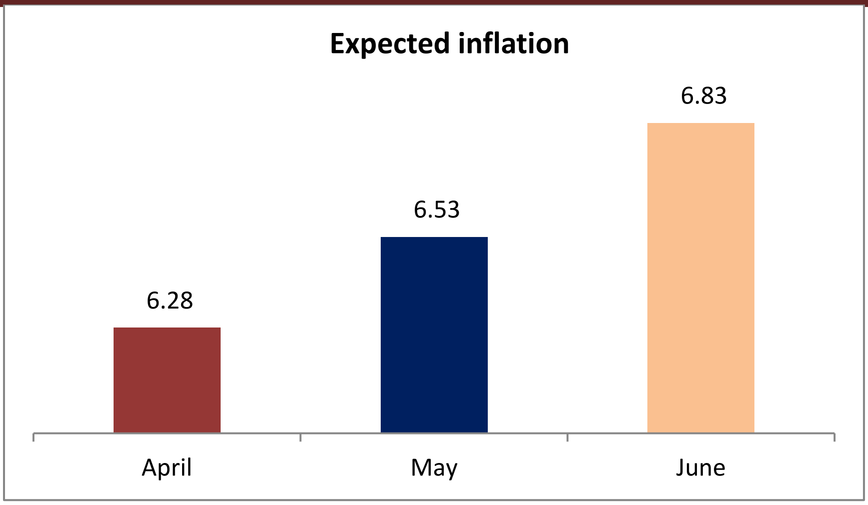
Several challenges need to be addressed in order to ensure long-term growth, including the subdued productivity in the agricultural and manufacturing sectors where majority of the country's exports come from. The planned improvements happening at the bourse will likely improve the country's prospect as a financial hub and eventually rope in more foreign investments in to the country.

In addition, Kenya's recently-secured USD 1.5 billion precautionary deal with the IMF provides the balance of payment with a buffer against potential external shocks, corruption and infrastructure bottlenecks.

Inflation Outlook

We expect overall inflation to remain within the CBK target range of 2.5%-7.5% on the back of lower fuel prices and electricity costs. Electricity costs are expected to drop due to the current lower fuel costs reduced thermal usage as well as the expected increase in generation from hydro plants in this long rains season.

Food inflation however will increase due to the dry season experienced in the first quarter of 2016. Maize prices are expected to be on an upward trend upto August 2016 when the next harvest is expected.



Interest Rates Outlook

In the last review, CBK maintained the CBR rate at 11.5% in a bid to still anchor inflationary pressures. With the current stable inflation, we do not expect to see any increases in CBR rate in the next review. The 91 day T-bill rate has also been on a downward trend which therefore means that the KBRR could be revised downwards in the next review (The KBRR is computed as an average of the Central Bank Rate and the two month weighted moving average of the 91-day T.bill rate).

Domestic borrowing pressure by the government has also reduced following the reduction of the borrowing target from Kshs 221 to Kshs 168 billion. Our calculation from the CBK net liquidity statistics shows net borrowings of approximately Kshs 146 billion as at the end of March 2016 leaving a deficit of only Kshs 22 billion which will easily be covered in the remaining 2 months. We therefore expect to see stable T.bill in the next three months.

Currency Outlook

We expect the shilling to remain stable at the 101-102 levels. The fundamental pressure on the shilling however still remains given the ongoing infrastructure spending. CBK tightened monetary policies, increased donor and diaspora remittances, increased agricultural inflows and the lower fuel prices are expected to temporarily cushion the shilling against any shocks.

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