CENTRAL BANK OF KENYA

Remarks by

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at the

MARKET LEADERS FORUM COCKTAIL

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Members of the Market Leaders Forum,
Officials from the Treasury,
My Colleagues at the Central Bank,
Ladies and Gentlemen,

It is my great pleasure to be with you this evening. Allow me to make a few remarks on the achievements of MLF this year. I will also briefly highlight the challenges we are currently facing this Financial Year and propose the way forward for our financial markets so as to achieve faster growth and stability:

Market Leaders Forum

Starting from 2003, the original Market Leaders Forum objectives were to lengthen the tenor of government securities and to raise money to meet Treasury's requirements. Having pushed the tenor to 25 years and with the market ready to take up even a 30 year bond, the first objective has been met. The second objective will always remain but with improved fiscal policy it has become much easier to manage.

The Forum, therefore, needs to be restructured in terms of representation and it needs to aim at influencing policy at stakeholders level so that we can consolidate the gains for the betterment of Kenya. In short: the Forum needs a new mandate, new course, and new players. We would like to brainstorm on this and parade/rank the options we should start with to show quick results.

1. This occasion comes at the heels of a very successful FY 2009-10 with respect to raising money for the government where annual target amount was achieved by April 2010. By June 2010, CBK had raised 100.3 percent of target, ensuring stable interest rates and introduction of new products that were well received by the market. In FY 2010/11, 48 percent of the target Ksh.105.3bn has been raised so far.

2. *Implementation of Benchmark Bonds Programme:* Successful issuance of benchmark Treasury Bonds and reopening as from April 2009 have been critical steps towards addressing the Bond Market fragmentation problem and creating liquidity necessary for development of a firm and reliable yield curve.
3. *Extending the Yield Curve:* To minimize rollover risks but at the same time provide a benchmark for pricing long term capital, the Bank issued a 25-year bond,

the longest maturity in Africa, with the exception of South Africa. The paper issued in June 2010 and reopened immediately thereafter, has been very active at the secondary market.

4. *Issuance of Infrastructure Bonds;* Building on the success of the debut Infrastructure Bond in February 2009, the Bank raised Ksh.32.9 billion in the FY 2009/10 and Ksh.30.6 billion in FY 2010/11 through Infrastructure Bonds to fund key projects in Roads, Energy and Water Sectors. All the offers were oversubscribed including the biggest one tranche Infrastructure Structure Bond of Ksh.30.5 billion in August 2010. Consequently, corporate issuers like KenGen Ltd, Safaricom, some commercial banks and mortgage firms have taken advantage of the growing bond market to raise long term funds to finance their capital projects. This is the road to realization of a deep and vibrant bond market.

   i. *Longer Maturity Profile of domestic debt* - the average maturity profile of domestic debt in government securities rose from 3 years 9 months in June 2009 to 4 years 7 months by June 2010 then to 5 years 1 month or ratio 23:77 in Bills and Bonds by November 2010. With a functioning secondary bond market in place, the Government no longer faces rollover risks associated with short term debt.

   ii. *Secondary market for bonds:* With the adoption of the Automated Trading System (ATS) in November 2009 and increased reopening of benchmark bonds, turnover at NSE has risen from Ksh.107.85 billion in 2009 to Ksh.443.50 billion just in the period January – November 2010. ATS linkage between the NSE and CBK ensures simultaneous exchange of securities and cash settlement using the KEPSS (RTGS) infrastructure on DvP basis, ensuring efficiency of trading in terms of safety of transactions and price discovery. The overall effect has been a firmed up yield curve, oversubscriptions in primary auctions and declining bond yields due to improved market confidence.

   iii. *Market-Makers framework:* The Bank hosted a successful two-day workshop for stakeholders in November 2010, in preparation for its commencement expected within this Financial Year. This was to sensitize stakeholders on the finalized Market Makers Operational Guidelines and Code of Conduct for Market Makers in Government Securities (GSMM).

To summarise, where do we want to go now:

(a) The financial market is deep and vibrant as evidenced by the World Bank report on 'Ease of Doing Business' which has placed Kenya's financial sector third in Sub-Saharan Africa.

(b) MLF has already achieved one of its key objectives of lengthening of maturity profiles of fixed income securities. The focus going forward, MLF is to be reconstituted so as to be able to guide policy.

(c) Policy directions should be enhanced and revised now to guide market behavior.

Marketing

The department seems to have gone slow on marketing the bonds. We need to address the critical issue of popularizing and marketing Governmentt securities. But this also calls for a new direction at both the CBK and the MLF. A well functioning National Debt Office will go a long way to alleviating this, since it will be in constant touch with the markets.

With these remarks, ladies and gentlemen, I wish you a pleasant evening and thank you for coming.