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LETTER OF TRANSMITTAL TO THE MINISTER FOR FINANCE

In accordance with Section 54 of the Central Bank of Kenya Act, I have the honour to present to you the Annual Report of the Central Bank of Kenya for the financial year 2001/2002. The Report reviews the performance of the economy and provides the Statement of the Audited Accounts of the Bank for the financial year ended June 30, 2002.

The Kenyan economy recovered to expand by a modest 1.2% in 2001 compared with a contraction of 0.2% in 2000. The expansion was led primarily by the agricultural and manufacturing sectors. The agricultural sector expanded by 1.2% in 2001 compared with the 2.1% decline in 2000. In tandem, the manufacturing sector expanded by 0.8% compared with the 2.1% decline in 2000. The monetary policy thrust during the reporting period remained to contain inflation within a 5% target. The Central Bank restrained inflationary pressures by adopting a tight monetary policy stance that enabled the Bank to maintain inflation below the set single digit target.

The overall balance of payments improved substantially due to both reduced current account deficit and increased capital account surplus. Consequently, the level of the country's gross foreign exchange reserves remained fairly healthy at 5.2 months of imports cover. Heavy pressure was put on government finances during the year ending June 30, 2002, however, owing to the non-disbursement of external budgetary support. As a result, the domestic borrowing requirement to finance the budget deficit increased substantially from the previous fiscal year. To moderate the impact of this increased government borrowing requirement on short-term interest rates, the Central Bank continued to pursue its domestic debt restructuring programme in favour of long-dated instruments. This strategy resulted in the ratio of long-dated Treasury bonds in the total secured domestic debt rising to 47% by June 2002 from 23% in April 2001.

The banking sector, as measured by the various internationally accepted prudential guidelines, remained relatively stable. This notwithstanding, more intensified and focused effort to strengthen the sector was made including the amendment of the enabling legislation to consolidate the regulation and supervision of building societies under the Banking Act. Additionally, the Central Bank developed other operational guidelines geared towards enhancing corporate governance and banking supervision. The Central Bank further continued to encourage banking institutions to make adequate provisioning for bad and doubtful debts. This specific policy thrust afforded a marginal reduction in the level of non-performing loans during the review period although, no doubt, this category of loans still continues to pose a real threat to the long-term stability of the banking industry.

Reform efforts to modernize the country's payments system were also intensified. During the review period, the Central Bank and commercial banks jointly established a National Payments System Steering Committee to formulate and improve the requisite policies and regulations. This bold initiative has afforded the realization of some substantial improvements in the payment and settlement arrangements, including the full automation of the Clearing House where clearing of cheques has been reduced from 14 days to 3 days. In addition, the Central Bank has initiated an electronic clearing project by which clearing items will be transacted by the end of calendar year 2002.

NAHASHON N NYAGAH
GOVERNOR

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Central Bank of Kenya

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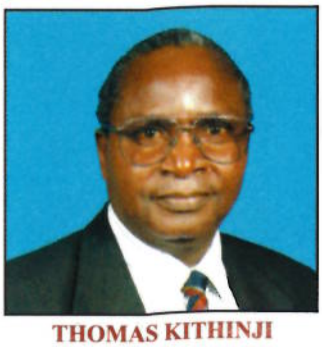
Permanent Secretary, and Head of the Public Service

DR. EDWARD SAMBILI
Deputy Governor
Central Bank of Kenya

MWAGHAZI MWACHOFI
Permanent Secretary
Ministry of Finance and Planning



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Skylark Africa Insurance Brokers

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Communication Concepts Ltd.

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Principal, College of Humanities & Social Sciences, University of Nairobi

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JOHN K. MURUGU
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JACINTA W. MWATELA (Mrs.)
Director, Supplies & Services

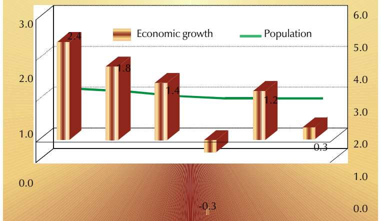
JONATHAN K. BETT
Director, Finance

LAWRENCE C. KUNGU
Executive Director, Kenya School of Monetary Studies

NICHOLAS M. KIRITU
Chief Internal Auditor

Introduction

CHART 1: REAL GDP & POPULATION GROWTH RATES, 1997 - JUNE 2002



Sources: Economic Survey and Central Bank of Kenya

The economy made a modest recovery in 2001 to expand by 1.2% in real terms from the 0.2% decline in 2000. The recovery was largely driven by increased agricultural production following favourable weather conditions, which through linkages supported economic activities in the manufacturing and services sectors. The pace of economic recovery has, however, been slow mainly due to inefficiencies attributed to the poor state of physical infrastructure and partly due to the persistently low investor confidence.

TABLE 1: GROSS DOMESTIC PRODUCT & SECTOR SHARE AT CONSTANT 1982 PRICES

Main sectors	Annual Growth (%) 2000/[1]	2001/[1]	2001/[2]	2002/[2]	Shares in GDP (%) 2001
Agriculture	-2.1	1.2	0.4	0.5	24.1
Manufacturing	-2.0	0.8	0.1	0.4	13.0
Trade, Restaurants & Hotels	1.0	1.3	0.6	0.2	2.4
Financial Services	0.4	1.0	0.8	0.7	12.7
Building & Construction	-1.4	-0.5	-1.3	-0.4	6.2
Transport & Communications	2.0	3.1	2.8	2.3	10.6
Government Services	0.7	0.7	0.6	0.6	14.7
Others of which	0.7	1.6	0.6	0.7	16.3
Non-monetary	*1.2*	*1.7*	*0.6*	*0.9*	*5.7*
Domestic services	*2.4*	*2.6*	*1.0*	*0.6*	*2.9*
Ownership of dwellings	*1.4*	*1.8*	*1.0*	*1.5*	*5.7*
Other	*-0.7*	*-0.5*	*-2.0*	*2.1*	*2.0*
TOTAL	**-0.2**	**1.2**	**0.5**	**0.6**	**100.0**

Notes

1 From the Economic Survey, 2002.

2 Annualised estimates for January to June 2001 and 2002

2 Includes forestry and fishing, mining and quarrying, electricity and water, and other sectors less imputed bank charges

Sources: CBS, HCDA, Sisal, Sugar and Pyrethrum Boards

Performance by Sectors

Agriculture

Agriculture, which accounts for 24.1% of GDP, expanded by 1.2% in 2001 compared with a decline of 2.1% in 2000. The recovery in agriculture reflected the favourable weather conditions in 2001 which, in turn, supported increased production in key sub-sectors. However, performance indicators of major agricultural commodities during the first half of 2002 were mixed (Table 2). Among the cash crops, horticultural produce increased by 5.1% in the first half of 2002 compared with 3.4% increase in the first half of 2001, while sugar cane output increased by 24.0% compared with a decline of 24.8% over the same period in 2001. Output of tea, pyrethrum and sisal, however, declined by 7.5%, 29.7% and 2.3%, respectively, in the first half of 2002 compared with 42.6%, 88.3% and 5.4% increases in a similar period in 2001. Coffee production declined by 15.4% in the first half of 2002 compared with a decline of 38.6% in a similar period in 2001.

TABLE 2: PERFORMANCE OF MAJOR AGRICULTURAL COMMODITIES (%)

Activity	2000	2001	Jan-Jun	
			2001	2002
Tea	**-5.0**	**24.7**	42.6	**-7.5**
Horticulture	0.2	-4.0	3.4	**5.1**
Coffee	52.4	-44.3	-38.6	**-15.4**
Sugar cane	-10.7	-9.9	-24.8	**24.0**
Pyrethrum	-5.0	5.1	88.3	**-29.7**
Sisal	-2.3	8.4	5.4	**-2.3**
Maize	-10.0	87.1		
Wheat	33.3	87.0		
Milk	-23.9	8.0		

Sources: CBS, HCDA, Sisal, Sugar and Pyrethrum Boards

With regard to food crops and dairy products, substantial improvements were recorded with wheat, maize and milk output increasing by 87.1%, 87.0% and 8.0%, respectively, in 2001. The respective output of maize and milk had declined by 10% and 23.9%,while that of wheat increased by 33.3% during a similar period in 2000. The performance of cash crop, food crop and livestock production is expected to pick up over the year following improved weather conditions.

Manufacturing

The manufacturing sector, which accounts for 13.0% of GDP, expanded by 0.8% in 2001 compared with a decline of 2.1% in 2000. The recovery in the sector is attributed to the normalisation of hydroelectric power supply and increased supply of raw inputs from the agricultural sector. The performance of the manufacturing sector during the first half of 2002 showed signs of continued recovery as reflected by the following developments:

- The consumption of electricity, a major industrial input, increased by 2.3% between January and June 2002 compared with 4.8% decline in a similar period in 2001.

- Imports of goods used in the sector, namely chemicals and related products, and machinery and transport equipment increased by 4.5% and 58.7% in the first four months of 2002 compared with 11.7% and 25.6% increases in a similar period in 2001. Imports of crude materials, however, declined by 16.5% in the first four months of 2002 compared with 14.7% increase in the same period of 2001. Imports of minerals and lubricants also declined by 27.3% compared with an increase of 8.2% in a similar period in 2001. The consumption of fuel oils also remained depressed.

- Manufactured exports increased by 14% during the first four months of 2002 compared with an increase of 9.6% in the first four months of 2001. The improved performance was partly due to increased exports of textiles and fabrics, which expanded by 209.3% in the first four months of 2002 compared with a decline of 11.9% in a similar period in 2001. The expansion was facilitated by the increased access to the United States market through the African Growth and Opportunities Act (AGOA).

Table 3 shows the production of some selected manufactured items. Cement, soda ash, galvanised sheets, mineral water and processed sugar increased by 2.1%, 2.2%, 6.0%, 14.1% and 23.1%, respectively, during the first half of 2002 while assembled vehicles declined by 20.4% due to strong competition from the relatively cheaper imported units.

The recovery in the sector is expected to continue following the favourable tax measures announced in the 2002/03 Budget, particularly the removal of duty on capital equipment and other intermediate inputs. The increased accessibility to the wider EAC and COMESA regional market, and access to the United

States market through the AGOA is also expected to support the performance of the manufacturing sector.

TABLE3: GROWTH IN PRODUCTION OF SELECTED MANUFACTURES (%)

Item	January - June	
	2001	2002
Galvanised sheets (MT)	2.6	6.0
Mineral water ('000 litres)	8.4	14.1
Soda ash (MT)	27.5	2.2
Cement (MT)	13.3	2.1
Assembled vehicles (units)	14.4	-20.4
Processed Sugar (MT)	-26.4	23.1

Source: Central Bureau of Statistics and Sugar Board

Building and Construction

Indicators show continued slow down in the sector during the first half of 2002. The building and construction sector remained subdued in 2001 and declined in real terms by 0.5% compared with a 1.5% decline in 2000. The consumption of cement, the main input in the sector, declined by 5.1% compared with 29.1% decline in a similar period in 2001. The depressed activity in the sector partly reflects the limited construction projects undertaken by the Government due to budgetary constraints, and the general slowdown in the economy.

Transport, Storage and Communications

Activity in the sub-sector slowed down during the first half of 2002, with the growth in volume of cargo handled through the port of Mombasa increasing by 1.8% compared with a growth of 28.7% in a similar period in 2001, while total cargo carried by the Kenya Railways Corporation declined by 2.4% during the first half of 2002 compared with a decline of 8.0% during the first half of 2001. Throughput by Kenya Pipeline Company declined by 6.6% in the period compared with 7.9% increase in the first half of 2001. Passengers through Jomo Kenyatta

International Airport (JKIA) also declined by 2.9% during the first quarter of 2002 compared with an increase of 20.0% in the first quarter of 2001.

The transport and communications sectors expanded in real terms by 3.1% in 2001 compared with 2.0% in 2000. The improvement in the sector was partly due to respective increases in imports of goods and services by sea and air by 22.1% and 14.1% in 2001, and a 12.3% increase in export volumes by sea. The throughput of petroleum products by the Kenya Pipeline Company also increased by 45.6% in 2001. In the communication sub-sector, following liberalisation, cellular phone subscriptions increased from 85,000 in 2000 to 668,000 in 2001.

Trade, Restaurants and Hotels

The performance of trade, restaurants and hotels expanded in real terms by 1.3% in 2001 compared with 1.0% in 2000. Performance in the tourism sub-sector, however, slowed down in the first half of 2002, with the number of visitors arriving at JKIA declining by 18.2% compared with 18.5% increase in a similar period in 2001 reflecting deterioration in the global economic and political environment. Visitors arriving at Moi International Airport, Mombasa (MIAM), also declined by 9.6% during the first half of 2002. As a result, earnings from the sub-sector declined by 21.6% during the first half of 2002 compared with 24.9% increase in a similar period in 2001. The low inflation environment in the domestic economy is expected to stimulate aggregate demand, thus promoting general trade activity.

Financial Services

Financial services, which account for 10.6% of GDP, expanded in real terms by 1.0% in 2001 compared with a growth of 0.4% in 2000. Banking institutions' profits before tax declined to Ksh 3.3bn during the first half of 2002 from Ksh 5.0bn realised during the comparable period of 2001. The slowdown in profitability partly reflected the negative impact of non-performing loans (NPLs), as well as reduced interest income given the prevailing low interest environment. Provisions for bad and doubtful debts increased to Ksh 4.5bn during the review period from Ksh 3.8bn during the first half of 2001. However, as a result of restructuring and other cost cutting measures, total expenses of the banking sector declined by 6.1% to Ksh 26.3bn between January and June 2002 compared with Ksh 28.0bn in a similar period in 2001. Lending business of the banks was also constrained by the uncertainty created by the Donde Bill (CBK Amendment Act, 2000).

Government Services

The Government services, which accounted for 14.7% of GDP in 2001, grew by 0.7% in both 2000 and 2001. Public investment in growth promoting activities such as the maintenance and building of physical infrastructure is expected to remain depressed due to budgetary constraints following delays in the resumption of external financial assistance.

Consumption, Savings and Investment

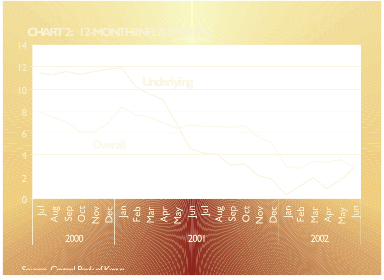
Public sector consumption increased by 8.1% in 2001, largely as a result of increased house allowance for civil servants, while private consumption rose by 14.0% in 2001 compared with an increase of 13.1% in 2000. Consequently, the overall consumption increased by 12.9% in 2001 compared with an increase of 12.6% in 2000.

In spite of the economic recovery in 2001, savings and investment continued to deteriorate. Nominal investment as a proportion of GDP declined to 14.5% in 2001 from 15.4% in 2000. The financing of investment from domestic savings also declined, with domestic savings as a proportion of GDP falling to 6.5% in 2001 from 7.3% in 2000. Consequently, employment in the modern sector (public and private) fell by 1.1% between 2000 and 2001, while urban unemployment rate stood at 25.1% in 2001. The decline in investment and savings as a ratio of GDP reflects the weak economic performance as a result of structural inefficiencies such as poor physical infrastructure and insecurity in some parts of the country.

Outlook for 2002

The economy is expected to stay on the recovery path during the remaining part of the year, supported by improved performance in agriculture, manufacturing and service sectors. The stability in the macroeconomic environment is also expected to support the recovery process. The pace of economic recovery still remains fragile due to a combination of factors including, in particular, the poor state of the physical infrastructure and low investor confidence associated with delayed resumption of external support. Uncertainties arising from the pending general elections are also expected to suppress the momentum of economy activity. The recent increase in the price of crude oil in light of the real possibility of renewed tensions in the Middle East may also undermine the recovery process.

Overview



During the financial year 2001/02 inflation[1] was contained within the 5% target reflecting largely the sustained implementation of prudent monetary policy by the Central Bank. The stability in the shilling exchange rate, the favourable weather conditions and the modest increase in crude oil prices during the financial year also supported the achievement of low inflation.

Overall Inflation

Inflationary pressures gradually eased during the first half of the financial year 2001/02, with the overall 12-month inflation declining from 4.2% in July 2001 to 1.8% in December (Table 4). The reduced inflationary pressures during the period largely reflected increased supply of basic food items and reduced international prices of crude oil. Crude oil prices declined from

TABLE 4: MONTH-ON-MONTH INFLATION (%)

	2001						2002					
	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun
Overall	4.2	4.0	3.1	3.2	2.1	1.8	0.4	1.1	1.9	0.9	1.7	2.8
Underlying	6.6	6.6	6.5	6.6	5.7	5.1	3.0	2.8	3.4	3.4	3.5	2.9

Source: Central Bureau of Statistics

US $ 25.0 per barrel in July 2001 to US $ 19.1 in December. During the third quarter of the financial year, the overall 12-month inflation rose from 0.4% in January 2002 to 1.9% in March mainly due to the increase in crude oil prices from US $

[1] Inflation analysis is based on a new Consumer Price Index (CPI) introduced by the Central Bureau of Statistics in place of the old CPI. It is based on the 1993/94 Urban Household Budget Survey (UHBS) compared with the old index, which was based on the 1982 UHBS. The new CPI has an extended coverage to other twelve towns, besides Nairobi, monthly surveys of housing costs imputed in the past and revised menu of goods and services and basket weights to reflect changes in consumption patterns. The new index is also more flexible with respect to replacement of goods, which are no longer traded in the market. Other notable features include increased weights ascribed to the food category of goods and the lower income group.

19.7 per barrel in January 2002 to US $ 24.0 per barrel in March, following tensions in the Middle East. The overall 12-month inflation thereafter declined to 0.9% in April but accelerated to 1.7% and 2.8% in May and June 2002, respectively. This was due to increases in the prices of maize and maize products following maize exports to the deficit areas in the Southern African region. The transportation problems caused by heavy rains in major food producing areas also caused temporary shortfalls in the supply of green groceries. The overall average annual inflation declined from 9.4% in June 2001 to 2.3% in June 2002.

Underlying inflation

The underlying 12-month inflation rate, which excludes food prices (non-food inflation), declined from 6.6% in July 2001 to 3.0% in January 2002 (Table 4). It, however, rose temporarily from 2.8% in February 2002 to 3.4% and 3.5% in April and May, respectively, largely due to increases in crude oil prices. The underlying inflation fell to 2.9% in June 2002 following a downward adjustment of electricity tariffs, which more than offset the increase in paraffin prices resulting from the additional tax on the commodity introduced in the 2002/03 budget.

Inflation as measured by the consumer price index that excludes food and energy prices fell from 5.6% in July 2001 to 5.0% in December, and to 3.5% in April before rising slightly to 3.6% and 3.7%, respectively, in May and June 2002. This favourable inflation outcome was attributed to the prudent monetary policy stance adopted by the Central Bank.

Inflation by Categories of Goods and Services

Inflation in the food category declined during the first half of the financial year from 2.8% in July 2001 to negative 1.9% in January 2002 following improvement in food supply due to favourable weather conditions. The food component, however, rose to 0.7% and 2.8% in March and June 2002, respectively.

Most of the increase was in the price of maize and maize products resulting from increased demand for maize exports to the deficit areas in the Southern African region. The transportation bottlenecks associated with heavy rains in major food producing areas also caused temporary shortfalls in the supply of green groceries. The drinks and tobacco category experienced the highest inflation ranging between 9.5% and 12.3% during the financial year. Inflation in housing averaged 7% during the first half of the financial year but declined to 4.6% in January 2002 before rising slightly to 5.5% in June 2002.

Inflation Outlook

Inflation is forecast to remain within the 5% target during the remainder of the financial year 2002/03. The envisaged low inflation environment will be supported by prudent monetary policy thereby forestalling any sustained inflationary threat. The continued relative stability in the shilling exchange rate is also expected to keep inflation low. Some inflationary pressure may, however, emerge if oil prices were to escalate on account of the uncertainties and fears being created by the possibilities of renewed tensions in the Middle East.

Overview

The main objective of monetary policy in the year to June 2002 remained the achievement of low and stable inflation. Thus, in June 2001 the Bank developed and implemented a monetary programme aimed at supporting a 2.6% economic growth and containing inflation within the 5% target by June 2002 (Table 5). Towards this end, the programme envisaged a growth in broad money supply, M3X, of 11.1% in the year to June 2002. Consistent with this, reserve money, the basis of monetary expansion and the operational target for the control of money supply, was programmed to increase by 9.1%.

TABLE 5: MONEY SUPPLY AND ITS SOURCES (KSH BN)

	Jun 1999/2000	Jun 2000/01	Jun 2001/02	Jun 2001/02 Original	Target Revised
1.0 Liability					
Money Supply					
Money supply, M2 1/	287.6	287.2	317.3		
Money supply, M3 2/	309.6	305.5	331.6	344.6	326.1
Money supply, M3X 3/	347.5	354.7	378.3	391.1	370.4
Money supply, M3XT 4/	424.2	446.6	483.9	490.9	473.0
2.0 Assets (2.1+2.2)	378.1	264.3	283.0	391.1	370.4
2.1 Net foreign assets 5/	**97.0**	**0.8**	**1.8**	**98.8**	**93.5**
Central Bank	**77.8**	**1.6**	**4.7**	**76.1**	**76.3**
Banking Institutions	**19.2**	**-0.8**	**-6.5**	**22.7**	**17.2**
2.2 Net domestic assets (2.21+2.22)	281.1	263.5	281.2	292.3	276.9
2.21 Domestic Credit (2.210+2.211)	330.8	324.6	342.0	406.9	359.3
2.210 Government (net)	83.2	68.7	94.7	76.5	85.4
2.211 Private sector and other public sector	247.5	255.9	247.2	330.4	273.8
2.22 Other assets net	-49.7	-61.1	-60.7	-114.5	-82.3
Memorandum Item:					
Reserve Money 6/	75.7	69.3	76.9	78.1	76.0

1/ Money Supply, M2, is money supplied by CBK and commercial banks. It comprises currency outside banking institutions, other non-banking institutions' deposits with the CBK, demand, savings & time deposits as well as certificates of deposits held by the private sector & parastatals with commercial banks. It excludes deposit placement of the central and local Government.

2/ Broad money, M3, comprises M2 and call, 7-days, savings & time deposits as well as certificates of deposits held by the private sector & parastatals with NBFIs. M3 excludes deposits of both the central & local Government with NBFIs, and all cross deposits of both commercial banks and NBFIs.

3/ Broad money, M3X, comprises M3 plus foreign currency deposits held by residents with banking institutions.

4/ Broad money, M3XT, includes M3X & outstanding Government Treasury securities with the non-banking public.

5/ NFA valued at constant exchange rate of Ksh 78.95 to the US $ (September 30th, 2001)

6/ Reserve money comprises currency in circulation & commercial banks balances held with the Central Bank.

Source: Central Bank of Kenya

The programme was developed with high expectations of economic recovery given the favourable conditions prevailing at that time. Notable were the adequate rainfall that was expected to spur agricultural production, the downward trend in interest rates, high expectation of resumption of external budgetary support under the IMF Poverty Reduction and Growth Facility (PRGF), and the stability in the shilling exchange rate.

The anticipated prospects for rapid economic recovery did not materialise following the continued withholding of donor funds, low levels of domestic investment and the September 11 terrorist attacks on the United States. The attacks, adversely affected prospects for Kenya's exports and in particular tourism. In addition, relations with development partners were not normalised and, therefore, prospects for external budgetary support deteriorated. These developments necessitated the scaling down of real GDP growth to 1.4% for year to June 2002 from the earlier forecast of 2.6%. In line with these developments, a revised monetary programme, which adopted a tighter monetary policy framework was designed and implemented from November 2001 through June 2002. The expansion in money supply, M3X, was restricted to 5.2% for the period and that of reserve money to 6.1% compared with the earlier targets of 11.1% and 9.1% respectively. The 5% inflation target for the period was however retained.

Money and Credit

All the money supply aggregates rose more rapidly in the year to June 2002 relative to the targets and monetary expansion in the year to June 2001. The increase in money supply reflected the economic recovery with real GDP growing by 1.2% in 2001 compared with 0.2% decline in 2000 (Table 6). The expansion in money supply in the year to June 2002 was, however, moderated through the Central Bank's active intervention in the domestic money market which partially sterilized excess liquidity using Repo sales. Consequently, Repo holdings by commercial banks increased more rapidly in the year to June 2002 by 64.4% compared with 57.4% increase in the year to June 2001. Money supply, M3, increased by 8.5% compared with a 6.5% target growth and a decline of 1.3% in the year to June 2001, while broad money supply, M3X, which includes M3 and residents' foreign currency deposits increased by 6.7% compared with 4.2% target growth in the year to June 2002 and 2.1% growth in the twelve months to June 2001. Reflecting partly the growth in M3X and partly the increase in holdings of Government securities by the non bank public, broader money supply, M3XT, which comprises M3X plus non-bank holdings of Government securities increased by 8.4% compared with 5.7% target growth and 5.3% increase in the year to June 2001.

TABLE 6: RESERVE MONEY PERFORMANCE/1 JUL - JUN 2002 (Ksh m)

	Actual (A)	Prog. Target (B)	Performance C = (A-B)	RM Deviation
July				
Reserve Money	72,514	71,362		1,152
Net Foreign Assets	67,627	66,986	641	
Net Domestic Assets	4,888	4,376	512	
August				
Reserve Money	72,828	73,227		-399
Net Foreign Assets	68,752	70,289	-1,537	
Net Domestic Assets	4,076	2,938	1,138	
September				
Reserve Money	72,503	73,377		-874
Net Foreign Assets	70,065	70,778	-713	
Net Domestic Assets	2,438	2,599	-161	
October				
Reserve Money	73,023	73,059		-36
Net Foreign Assets	70,953	70,953	0	
Net Domestic Assets	2,070	2,106	-36	
November				
Reserve Money	75,371	73,920		1,451
Net Foreign Assets	70,738	72,896	-2,158	
Net Domestic Assets	4,633	1,024	3,609	
December				
Reserve Money	78,082	76,627		1,455
Net Foreign Assets	74,146	72,912	1,234	
Net Domestic Assets	3,937	3,715	222	
January				
Reserve Money	76,349	76,400		-51
Net Foreign Assets	74,800	73,078	1,722	
Net Domestic Assets	1,549	3,322	-1,773	
February				
Reserve Money	75,951	75,800		111
Net Foreign Assets	75,765	73,127	2,638	
Net Domestic Assets	186	2,673	-2,487	
March				
Reserve Money	76,278	75,253		1,025
Net Foreign Assets	76,971	75,534	1,437	
Net Domestic Assets	-693	-281	-412	
April				
Reserve Money	76,076	75,025		1,051
Net Foreign Assets	77,842	75,504	2,338	
Net Domestic Assets	-1,766	-479	-1,287	
May				
Reserve Money	77,271	75,500		1,771
Net Foreign Assets	77,474	75,965	1,509	
Net Domestic Assets	-591	-466	-125	
June				
Reserve Money	77,285	76,000		1,285
Net Foreign Assets	77,628	76,268	1,360	
Net Domestic Assets	-343	-268	-75	

1/ Monthly Averages

Source: Central Bank of Kenya

The source of the expansion in money supply over the year to June 2002 was increases in net domestic assets (NDA) of the banking system and to a lesser extent net foreign assets (NFA). The NDA increased by 6.7% compared with 4.8% target growth in the year to June 2002 and 6.3% decline in the year to June 2001 while NFA increased by 6.4% compared with 2.5% target and 37.3% growth in the year to June 2001. The sources of money supply fluctuated from one month to another throughout the year to June 2002. The trend of NFA was even more volatile, declining by 4.4% in November 2001 and thereafter increasing more rapidly by 9.0% in December 2001 before declining by 1.6% in January 2002.

Most of the increase in NDA during the year was in domestic credit. Domestic credit expanded by 5.4% and accounted for 97.1% of the NDA growth in the year to June 2002. All the credit expansion was to the Government as the private and other public sectors repaid 3.4% of their domestic debt. Net Government indebtedness to the banking system in the year to June 2002 therefore, increased by 37.9%. The credit expansion comprised increases of Ksh 9.2bn from the Central Bank and Ksh 16.8bn from commercial banks. Other assets net of other liabilities of the banking system meanwhile increased by 0.8% in the year to June 2002 compared with 22.9% decline in the year to June 2001.

Credit to the Private and Other Public Sectors

Credit to the private and other public sectors declined by Ksh 8.7bn or 3.4% in the year to June 2002 compared with 3.4% increase in the year to June 2001 (Table 7). Net credit to other public sector institutions declined by Ksh 3.2bn following loan repayments by parastatals, while credit to the private sector declined by Ksh 5.4bn. Among the private sector activities, Ksh 10.8bn was repaid by trade, mining and quarrying, manufacturing, business services and real estate activities which offset Ksh 5.4bn new credit to transport and communication, consumer durables, building and construction, agriculture and finance and insurance and other activities. An analysis of private sector credit on a month by month basis showed that the sector repaid credit in the period July 2001 through March 2002 with the trend reversing in the June 2002 quarter when new borrowings were recorded especially in April and June 2002. The upward trend in credit over the period after December 2001 through to June 2002 reflected the economic recovery process, which began in 2001.

TABLE 7: CREDIT TO PRIVATE AND OTHER PUBLIC SECTORS (KSH BN)

	2001 Jun		2002 Jun		Annual Change		Jun '01 - Jun '02
	Ksh bn	Share (%)	Ksh bn	Share (%)	Ksh bn	(%)	% dist. of ann. change in credit to private sector
1. Credit to other public sector	**9.9**	**3.9**	**6.6**	**2.7**	**-3.2**	**-32.9**	
Local government	-0.5	-0.2	-0.5	-0.2	0.1	-10.8	
Parastatals	10.4	4.1	7.1	2.9	-3.3	-31.8	
2. Credit to private sector	**246.0**	**96.1**	**240.6**	**97.3**	**-5.4**	**-2.2**	**100.0**
Agriculture	22.7	8.9	23.0	9.3	0.3	1.1	-4.6
Manufacturing	56.9	22.2	55.5	22.5	-1.4	-2.4	25.4
Trade	49.7	19.4	43.7	17.7	-6.0	-12.1	110.2
Building and construction	19.5	7.6	20.0	8.1	0.5	2.7	-9.5
Transport & communications	10.4	4.1	11.7	4.7	1.3	12.0	-22.9
Finance & insurance	14.8	5.8	14.9	6.0	0.1	0.6	-1.6
Real estate	20.8	8.1	20.2	8.2	-0.6	-2.9	11.1
Mining and quarrying	4.1	1.6	2.0	0.8	-2.1	-52.3	39.2
Private households	10.6	4.2	10.6	4.3	0.0	-0.5	0.9
Consumer durables	4.4	1.7	5.6	2.3	1.3	29.5	-23.5
Business services	26.2	10.3	25.6	10.3	-0.7	-2.6	12.4
Other activities	5.8	2.3	7.8	3.2	2.0	35.1	-37.2
3. TOTAL (1+2) *	**255.9**	**100.0**	**247.2**	**100.0**	**-8.7**	**-3.4**	

* Absolute and percentage changes may not necessarily add-up due to rounding

Source: Central Bank of Kenya

Reserve Money

Reserve money, that is currency in circulation and deposits of both commercial banks and NBFIs at the Central Bank, increased by 10.9% in the twelve months to June 2002 compared with 8.5% decline in the year to June 2001 (Table 8). The increase in reserve money in the year to June 2002 was in banks' deposits at the Central Bank, which rose by 10.5%, and in currency in circulation, which increased by 11.1%. The expansion in reserve money was attributedwholly to a build up of the Bank's net foreign assets as net domestic assets declined.

In the year to June 2002, NFA expanded by 18.1% compared with 13.7% target growth and 25.0% increase in the year to June 2001. This reflected the Bank's accumulation of foreign exchange reserves through purchases from commercial banks. The NDA of the Central Bank, however, declined by 127.9% in the year to June 2002 compared with 88.8% decline in the year to June 2001, largely reflecting enhanced activity by the Central Bank in the sale of Repos under the open market operations.

TABLE 8: RESERVE MONEY & ITS SOURCES (KSH BN)

		2001 Jun	2002 Jun	Change Absolute	%	Target Jun	Deviation
1	Net Foreign Assets	65.9	77.8	11.9	18.1	76.0	1.9
2	Net Domestic Assets	3.4	-1.0	-4.4	-127.9	0.0	-1.0
	2.1 Government Borrowing (net)	10.8	20.0	9.2	85.5	21.6	-1.6
	2.2 Advances & Discounts	-13.7	-23.4	-9.7	70.9	-25.3	1.9
	2.3 Other Domestic Assets (net)	6.3	2.4	-3.9	-61.8	3.4	-1.0
3	Reserve Money	69.3	76.9	7.6	10.9	76.0	0.9
	3.1 Banks Deposits at CBK	22.2	24.8	2.6	11.9	26.0	-1.2
	3.2 NBFIs Deposits at CBK	0.4	0.2	-0.3	-57.6	0.2	0.0
	3.3 Currency in Circulation	46.7	51.9	5.2	11.1	49.8	2.1

Source: Central Bank of Kenya

The decline in the NDA reflected the following:

- Increase in net indebtedness of the Bank to commercial banks by 70.9% due to mop up of excess liquidity through open market operations that led to an increase in Repo holdings by 64.4% in the twelve months to June 2002.

- Decrease in other domestic assets of the Central Bank by 61.8% in the year to June 2002 compared with 22.7% decline in the year to June 2001.

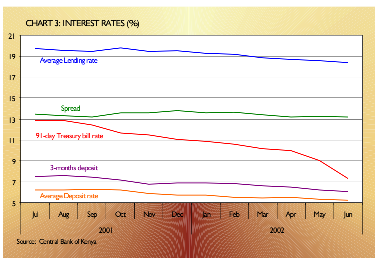
The decline in NDA was moderated by the 85.5% expansion in net credit to the Government following reduction of own deposits at the Bank.

Monetary Policy Management

In order to contain inflationary pressures, the Bank continued to influence the level of money supply through the operational target, the reserve money. The Bank through Open Market Operations (OMO) targeted the reserves of commercial banks by selling to them Treasury bills which in turn influenced the intermediate money supply target, M3X. The Central Bank pursued a tight reserve money programme throughout the twelve months to June 2002, and more extensively from November 2001 following the review of the targets. The monetary policy implementation was generally successful with reserve money either within or marginally above target. In the period under review, the Bank intensified interventions in the market, which resulted in a 64.4% increase in commercial bank holding of Repos under the open market operations to Ksh 26.8bn.

Through prudent liquidity management, the Bank confined the underlying inflation within the 5% target thereby achieving the Bank's principal objective of maintaining price stability. This was consistent with the stability observed in the shilling exchange rate and in the key nominal interest rates. Consequently, the underlying month-on-month inflation declined from 6.6% in July 2001 to 2.9% in June 2002.

Interest Rates



Interest rates continued to decline in the twelve months to June 2002 following the downward trend in the 91-days Treasury bill rate (Table 9 and Chart 3). The 91-days Treasury bill rate increased in the three months to September 2001 but resumed the declining trend thereafter through to June 2002. The decline reflected excess liquidity in the banking system as well as the emergence of a more competitive spirit amongst the major investors. Investors were attracted by the relatively high return, safety and liquidity properties of the Treasury bills. This continued to exert downward pressure on the interest rates. The Government, on the other hand, reduced its weekly

TABLE 9: INTEREST RATES (%)

	2001						2002					
	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun
Treasury bill**	12.9	12.8	12.4	11.6	11.5	11.0	10.9	10.6	10.1	10.0	9.0	7.3
Average Lending Rate (1)	19.7	19.5	19.4	19.8	19.4	19.5	19.3	19.2	18.9	18.7	18.5	18.4
Average Deposit rate (2)	6.2	6.2	6.3	6.2	5.9	5.7	5.7	5.5	5.4	5.5	5.3	5.2
3-month deposit	7.5	7.6	7.4	7.2	6.8	6.9	6.9	6.8	6.6	6.5	6.2	6.1
Spread (1-2)	13.5	13.3	13.2	13.6	13.6	13.8	13.6	13.7	13.4	13.2	13.2	13.2

**** 91-Days Treasury Bill**

Source: Central Bank of Kenya

borrowing from the domestic economy progressively. Early in the financial year, the weekly borrowings stood at Ksh 8.5bn and declined progressively to a maximum of Ksh 4.5bn by December 2001. It, however, increased again to Ksh 6.5bn by the last week of June 2002. This enabled the Government to effectively use the longer dated Treasury bond issues to lengthen the maturity profile of domestic debt over the review period.

Developments in interest rates in the year were as follows:

- The 91-day Treasury bill rate rose to 12.4% in September 2001 from 12.1% in June 2001. The upward trend since September 2001 quarter reversed in October and the rate was 7.3% in June 2002.

- Average lending rate in the banking system declined to 18.4% in June 2002 from 19.3% in June 2001. Average deposit rate also declined to 5.2% from 6.4% over the same period.

- Despite the decline in the average lending interest rate over the period, the interest rate spread remained stable at an average of 13.4%. The high spread partly reflected the disproportionate decline in the interest rates on bank deposits relative to the decline in lending rates.

Structure of the Banking System

The number of commercial banks decreased from 49 in June 2001 to 46 by June 2002. This followed liquidation of one bank, merger of two banks and a take-over of another. Non-bank financial institutions (NBFIs) declined to five in June 2002 from seven in June 2001 as two institutions merged with their parent banks. Commercial bank branch network increased by 32 from 465 in June 2001 to 497 as at end of June 2002. As has been the trend in the past, most of the new branches opened during the year are located in Mombasa and Nairobi.

The banking sector continued to be dominated by eight commercial banks, which accounted for 72.1% of the total assets and 72.5% of deposit base. Among the NBFIs, one institution with assets worth over Ksh 5bn dominated the sector and accounted for 62.0% of the total assets.

The number of foreign exchange bureaus increased from 47 in June 2001 to 48 as at the end of June 2002 after the re-opening of an institution that was previously closed. The moratorium on the licensing of new foreign exchange bureaus imposed in October 1999 is, however, still in force.

Balance Sheet Structure

The balance sheet of the banking sector improved marginally during the period under review. The sluggish growth of the sector was partly attributed to the uncertainty surrounding the implementation of Central Bank of Kenya (Amendment Act 2000) seeking to reimpose interest rate controls and partly due to the slowdown in economic recovery. Consequently, major banking institutions restructured their balance sheets mainly by reducing their exposure to loans and advances in favour of low risk government securities.

Assets

The total assets of the banking system increased by 0.8% to Ksh 436.5bn at the end of June 2002 from Ksh 432.9bn at the end of June 2001 (Table 10). Gross loans and advances, comprising 48% of banks' assets, however, decreased by 5.0% to Ksh 287bn in June 2002 from Ksh 302bn in June 2001. The decline in loans and advances is attributed to the uncertainties surrounding the Central Bank of Kenya (Amendment) Act 2000, which made banks reluctant to extend credit.

TABLE 10: BANKING INDUSTRY PERFORMANCE INDICATORS (KSH M)

Performance Indicators	2000 June	2001 June	2002 June	% change over June 2001
Assets	433,360	432,878	436,548	0.9
Deposits	326,852	331,894	343,827	3.6
Gross loans	289,180	302,122	287,275	-5.0
Total Loans*	259,800	262,613	245,515	-6.6
Specific Provisions	32,410	34,479	30,276	-12.2
Non-performing Loans*	84,047	82,914	75,532	-8.9
Net Non-performing Loans**	51,637	48,435	42,256	-12.8
Total NPLs/Total Loans	32.4%	31.6%	30.8%	
Net NPLs/Total Advances	19.9%	18.4%	17.2%	
Provisions/ NPLs	38.6%	41.6%	40.1%	
Capital & Reserves	51,213	55,917	52,738	-5.7
Profit/(Loss) Before tax	4,211	5,035	3,284	-34.8
Liquid Assets/ Deposit liabilities	44.0%	42.0%	42.9%	
Cash Ratio	13.5%	10.2%	10.8%	

* Total Loans and Non-performing Loans exclude suspended interest.

** Net Non-performing Loans exclude specific provisions.

Source: Central Bank of Kenya

Other major assets were government securities and balances at the Central Bank of Kenya, which comprised 20% and 6% of total assets, respectively. Holding of government securities by the banking system increased by 13.4% to Ksh 89.1bn in June 2002 from Ksh 78.6bn in June 2001 reflecting the banking industry's risk aversion to extending credit and their preference to invest in government securities.

Asset Quality

The quality of the assets as measured by the level of non-performing loans to total loans continued to pose a major threat to stability of the banking sector. Non-performing loans (NPLs) stood at Ksh 75.5bn and accounted for 31% of total loans in June 2002 compared with Ksh 82.9bn or 32% of total loans in June 2001. The decline in NPLs is attributed to the liquidation of one major bank that had substantial NPLs. In line with the decline in NPLs, specific provisions for bad and doubtful loans declined to Ksh 30.3bn in June 2002 from Ksh 34.5bn in June 2001. In view of the relatively high level of non-performing loans, the Central Bank continued to encourage institutions to make more prudent provisioning for bad and doubtful debts.

Deposits

The banking system held deposits of Ksh 344bn at the end of June 2002, which represented an increase of approximately 3.6% over the June 2001 level of Ksh 332m (Table 11). Time deposits held by commercial banks comprised 38.4% of funds while demand and savings deposits accounted for 35.0% and 23.2% of total deposits, respectively. Time deposits for NBFIs including mortgage finance companies accounted for 78.6% of their total deposits while savings deposits accounted for 19.4%.

TABLE 11: COMPOSITION OF DEPOSITS (KSH M)

BANKS	2000 June	2001 June	2002 June	Share in 2002 (%)
TYPE OF DEPOSITS				
Demand deposit	94,133	104,005	115,332	35.0
Kenya shillings	70,255	75,782	87,721	26.6
Foreign Currency	23,879	28,223	27,611	8.4
Time Deposits	131,237	122,473	126,512	38.4
Kenya shillings	117,980	101,854	107,848	32.7
Foreign Currency	13,256	20,620	18,664	5.7
Saving Deposits	69,143	73,366	76,286	23.2
Kenya shillings	68,904	73,086	76,066	23.1
Foreign Currency	238	280	220	0.1
Sub-Total	**294,513**	**299,845**	**318,130**	**96.5**
Kenya shillings	257,140	250,722	271,635	82.4
Foreign Currency	37,373	49,123	46,495	14.1
Others**	11,199	13,785	11,410	3.5
Total	**305,712**	**313,630**	**329,540**	**100.0**
NBFIs* (in Kenya shillings)				
TYPE OF DEPOSITS				
Time Deposits	18,010	15,397	11,235	78.6
Saving Deposits	3,532	2,526	2,774	19.4
Sub-Total	**21,543**	**17,924**	**14,009**	**98.0**
Others**	596	341	278	2.0
Total	**22,139**	**18,265**	**14,287**	**100.0**
Grand Total	**327,851**	**331,895**	**343,827**	**100.0**

*NBFIs are not licensed to hold foreign currency deposits.

** Others: Include accrued interest on deposits, interbank balances and balances of foreign currency accounts of non-residents.

Source: Central Bank of Kenya

Profitability

The profitability of the banking industry improved substantially in 2001 with gross profits before tax increasing to Ksh 8.9bn from Ksh 2.8bn in 2000 (Table 12). The increase in profit was attributed partly to the liquidation of a major bank that had been weighing down the banking system with huge losses and partly due to the reduced losses reported by some major loss-making banks. The charge for bad and doubtful debts, a significant expense item in the sector, declined substantially by 43.7% to Ksh 7.7bn in December 2001 from Ksh 13.7bn in December 2000, contributing to the increase in profits. A total of 41 banking institutions made a cumulative profit of Ksh 11.5bn while eleven institutions made a cumulative loss of Ksh 2.6bn in 2001, resulting in total profit of Ksh 8.9bn for the entire industry.

TABLE 12: BANKING INDUSTRY PROFITS (KSH M)

	Dec-00 12 months	Jun-01 6 months	Dec-01 12 months	Jun-02 6 months
Total Income	67,689	33,077	61,428	29,610
Expense before Provisions	51,172	24,251	44,822	21,798
Profit before Provisions	16,517	8,826	16,606	7,814
Provisions for bad debts	13,721	3,791	7,746	4,530
Profit before tax	2,796	5,035	8,860	3,284

* Figures exclude building societies.

Source: Central Bank of Kenya

Results for the six months period to June 2002 showed a 34.8% decline in profitability in the banking sector compared with profits over a similar period in 2001. During this period, 42 institutions made profits of Ksh5.7bn while nine institutions made losses of Ksh 2.4bn, giving an overall gross profit before tax of Ksh 3.3bn compared with Ksh 5.0bn over the six months to June 2001.

The banking sector remained fairly liquid with the average liquidity ratio standing at 42.9% at the end of June 2002, well above the minimum statutory requirement of 20%. Similarly, cash ratio averaged 10.8% in June 2002 and was above the minimum statutory requirement of 10%.

Capital and Reserves

The capital and reserves of the banking system decreased by 5.7% to Ksh 52.7bn in June 2002 from Ksh 55.9bn in June 2001 due to the liquidation of one commercial bank. Consequently, capitalization, as measured by capital to deposit ratio, declined from 17.0 % to 15.3%. The ratio of total capital to total risk weighted assets improved marginally from 16.0% to 16.8%, well above the minimum statutory requirement of 12% during the same comparable period.

Measures to Strengthen the Banking Sector

The banking sector continued to be relatively stable in the year to June 2002. To further strengthen and streamline the banking sector, the following measures were undertaken:

(i) The Banking Act was amended as follows:

- To allow the sharing of information among banking institutions and between Central Bank and banking institutions.

- To allow mortgage finance companies to engage in other types of lending, while retaining their core business. Mortgage finance companies are now authorised to advance short- and long-term credit, including personal loans. In addition, they are no longer limited to the types of securities they can take against an advance unlike previously when they were mainly restricted to security in form of land.

- To make it mandatory for building societies to be members of the Deposit Protection Fund Board (DPFB) in order to protect small depositors in the event of an institution collapsing.

(ii) The Building Societies Act was amended as follows:

- To provide the Central Bank of Kenya with powers to regulate, control and intervene in the management of building societies.

- To allow building societies to grant other types of loans other than residential mortgages secured by land.

(iii) To facilitate cross-border and consolidated supervision of the banking sector, the Bank continued to work closely with the Bank of Tanzania and the Bank of Uganda in order to harmonise the banking laws, regulations and supervision practices in the East African region.

In the current financial year 2002/03,the Bank will focus on the following:

- Enhancing transparency and accountability in financial reporting of banking institutions by requiring mandatory quarterly publication of un-audited financial statements in the print media.
- Resolving the problem of the large stock of non-performing loans that has been a major threat to the stability of the banking sector.
- Developing legislation that will facilitate passage of information on loan defaulters to credit reference bureaus.
- Pursuing measures and adopting appropriate procedures to facilitate banking mergers.
- Impressing on those banks without automated teller machines (ATM) on the need to take advantage of the recently launched ATM shared facility in order to cope with technological advancement in the banking sector.
- Encouraging banking institutions to submit electronically the various periodic returns with the objective of achieving speedy and accurate processing of data.

Government budgetary operations in fiscal year 2001/02 resulted in a budget deficit on a commitment basis of Ksh 22.3bn or 2.4% of GDP, compared with a budget deficit of Ksh16.5bn in fiscal year 2000/01 and target deficit of Ksh 8.2bn. On a cash basis, government fiscal operations also deteriorated to a deficit of Ksh 27.9bn or 3.0% of GDP from Ksh 13.4bn deficit in fiscal year 2000/01. The Government financed the deficit largely through domestic borrowing. The increase in the deficit reflected a Ksh 22.2bn shortfall in revenue and the financing in 2001/02 fiscal year of Ksh 14.9bn expenditures for the previous year (Table 13).

TABLE 13: BUDGET OUTTURN (KSH BN)

	FY 2000/01	FY 2001/02		Over(+)/
	Actual	Actual*	Target	Below (-)
1. TOTAL REVENUE & GRANTS	**216.4**	**203.3**	**224.7**	**-21.4**
Revenue	192.3	196.5	218.6	-22.2
Tax Revenue	163.2	163.4	179.0	-15.6
Non Tax Revenue	14.7	15.4	18.9	-3.6
Appropriations-in-Aid	14.4	17.7	20.7	-3.0
External Grants	24.1	6.8	6.0	0.8
2. TOTAL EXPENDITURE AND NET LENDING	**232.9**	**225.6**	**232.9**	**-7.3**
Recurrent Expenditure	198.9	200.7	200.2	0.5
Development Expenditure	34.0	25.0	32.7	-7.8
3. DEFICIT ON A COMMITMENT BASIS (1-2)	**-16.5**	**-22.3**	**-8.2**	**-14.1**
	(-2.0)	(-2.4)	(-1.0)	
4. ADJUSTMENT TO CASH BASIS	**3.1**	**-5.6**	**-6.5**	**0.9**
5. DEFICIT ON A CASH BASIS	**-13.4**	**-27.9**	**-14.7**	**-13.2**
	(-1.6)	(-3.0)	(-1.7)	
6. DISCREPANCY: Expenditure (+) / Revenue (-)	**-0.3**	**-0.5**	**0.0**	**-0.5**
7. FINANCING	**13.1**	**27.4**	**14.7**	**12.7**
Domestic (Net)	0.6	39.8	23.1	16.6
External (Net)	12.5	-13.3	-8.4	-4.9
Capital Receipts (privatisation)	0.0	1.0	0.0	1.0

* Provisional
** Figures in parentheses are deficit to GDP Ratio (%)

Sources: Central Bank of Kenya and Treasury

Revenue and Grants

Government receipts including grants amounted to Ksh 203.3bn or 22.0% of GDP in 2001/02 fiscal year, a decline of Ksh 13.1bn from Ksh 216.4bn or 25.6% of GDP in 2000/01 fiscal year. The decline in government receipts was attributed to a sharp fall in external grants inflows by Ksh 17.3bn. This decline in receipts was however partially offset by Ksh 4.2bn increase in Government revenues over the 2001/02 fiscal year. The receipts which were Ksh 21.4bn below the Ksh 224.7bn target, comprised Ksh 196.5bn government revenue and Ksh 6.8bn grants.

Expenditure and Net Lending

During the 2001/02 fiscal year, the Government continued to pursue tight expenditure control in order to contain the budget deficit. The tight controls on expenditure, together with non disbursement of program finance by development partners resulted in lower expenditure and net lending of Ksh 225.6bn or 24.5% of GDP, compared with a target of Ksh 232.9bn or 25.3% of GDP. The components of the expenditure and net lending were as follows:

- Recurrent expenditure increased by Ksh 1.8bn to Ksh 200.7bn, representing 88.9% of total expenditure and comprised the following:
  - Expenditure on wages and salaries of Ksh 77.6bn compared with Ksh 68.1bn in the previous fiscal year; and
  - Interest payments of Ksh 30.3bn compared with Ksh 31.0bn in 2000/01. Interest on domestic debt amounted to Ksh 23.7bn and that on foreign debt was Ksh 6.6bn.
- Development expenditure amounted to Ksh 25.0bn and was Ksh 9.0bn lower than in the previous fiscal year.

Financing

The budgetary operations in fiscal year 2001/02 resulted into a financing requirement of Ksh 45.0bn, an increase of Ksh 16.4bn over fiscal year 2000/01. The Government covered the financing requirement through the following sources:

- Ksh 17.3bn borrowing from commercial banks;
- Ksh 13.3bn borrowing from non bank sources;
- Drawing down its deposits at the Central Bank by Ksh 13.5bn; and
- Ksh 1.0bn privatisation proceeds through sale of its shares in Mumias Sugar Company.

The borrowed funds, together with the drawdown of deposits and privatization proceeds were utilized in making repayments of Ksh 13.3bn and Ksh 4.2bn to the external sources and Central Bank, respectively. The balance of Ksh 27.4bn was utilized to finance the budget deficit.

Government public debt stood at Ksh 613.8bn as at end of June 2002. This represented 66.7% of GDP and was Ksh 8.0bn higher than the debt stock in June 2001. Of the Ksh 613.8bn overall debt, domestic debt was Ksh 236bn or 38.4% of the total stock while foreign debt amounted to Ksh 377.8bn, representing 61.6% of public debt.

Domestic Debt

Public domestic debt increased by Ksh 24.2bn to Ksh 236bn at end of June 2002 from Ksh 211.8bn in June 2001 (Table 14). The increase in domestic debt was as a result of increased government borrowing to finance the budget deficit.

TABLE 14: PUBLIC DEBT (KSH BN)

	June 2001		June 2002*	
	Ksh bn	%	Ksh bn	%
DOMESTIC DEBT				
Securitised debt	**183.5**	**86.6**	**225.9**	**95.7**
Treasury Bills	137.5	64.9	118.1	50.0
of which repo t.bills	21.1	10.0	36.0	17.0
Treasury Bonds	44.5	21.0	106.3	45.1
Government Stocks	1.5	0.7	1.5	0.6
Non Securitised debt	**28.3**	**13.4**	**10.1**	**4.3**
Overdraft/Advances	12.5	5.9	9.2	3.9
Non-interest bearing debt	15.8	7.5	0.9	0.4
TOTAL DOMESTIC DEBT	**211.8**	**100.0**	**236.0**	**100.0**
EXTERNAL DEBT				
Bilateral	132.3	33.6	115.4	30.5
Multilateral	228.5	58.0	224.7	59.5
Comm. Banks	29.4	7.5	33.9	9.0
Export Credit	3.8	1.0	3.8	1.0
TOTAL EXTERNAL DEBT	**394.0**	**100.0**	**377.8**	**100.0**
TOTAL PUBLIC DEBT	**605.8**		**613.8**	
(as a % of GDP)		**71.6**		**66.7**

* Provisional

Sources: Central Bank of Kenya and Treasury

Kenya's domestic debt has in the past been dominated by short-term 91 day Treasury bills with weekly redemptions of Ksh 8.5bn. The Government, therefore, had to resort to the money market more frequently to source funds to finance the emerging budget deficit and to roll over maturing government securities. The frequent borrowing consequently exerted pressure on domestic interest rates.

In order to reduce pressure on domestic interest rates, the Central Bank implemented a debt restructuring programme in May 2001 aimed at reducing the share of the 91-day Treasury bills in the domestic debt while increasing the share of medium to long term bonds. The other objective of the new strategy was to develop a yield curve to guide the market in the pricing of primary issues of corporate bonds and the pricing of all securities traded in the Stock Market.

As part of the restructuring programme, the Central Bank issued fixed and floating rate bonds of various maturities worth Ksh 87.2bn during the fiscal year 2001/02. There were 17 bond issues worth Ksh 92bn, which attracted bids worth Ksh 120.8bn, resulting in an average subscription rate of 131%. The Government used part of the proceeds from the sale of Treasury bonds to redeem some of the outstanding Treasury bills (Table 15). As a result, Treasury bills stock which stood at Ksh 137.5bn, or 75.0% of the total securitised domestic debt, in June 2001 fell to Ksh 118.1bn or 52.3% at the end of June 2002.

TABLE 15: OUTSTANDING STOCK OF TREASURY BILLS BY HOLDER (KSH BN)

Holders		Jun-01		Jun-02	
		Ksh	%	Ksh	%
Banking Institutions		71.8	52.2	66.3	56.1
	Central Bank	21.2	15.4	36.0	30.5
	Comm. Banks	47.3	34.4	28.7	24.3
	NBFIs	3.3	2.4	1.5	1.3
Insurance Companies		9.5	6.9	8.7	7.4
Parastatals		9.3	6.8	4.6	3.9
of which NSSF		0.2	0.2	1.1	1.0
Building Societies		2.6	1.9	0.4	0.3
Others		44.3	32.2	38.0	32.2
Total		**137.5**	**100.0**	**118.1**	**100.0**

Source: Central Bank of Kenya

Following the successful re-launch of the longer term dated bonds, the outstanding stock of Treasury bonds increased to Ksh 106.3bn or 47.1% of securitised debt in June 2002 from

Ksh 44.5bn or 24.2% of securitised debt in June 2001. Of the Ksh 92bn Treasury bonds offered in the fiscal year 2001/02, the Government accepted bids worth Ksh 87bn. Over the twelve months, the Government redeemed Treasury Bonds worth Ksh 25.2bn, resulting in a net increase of Ksh 61.8bn in the stock of Treasury bonds (Table 16).

TABLE 16: OUTSTANDING STOCK OF TREASURY BONDS BY HOLDER (KSH BN)

Holders		Jun-01		Jun-02	
		Ksh	%	Ksh	%
Banking Institutions		13.1	29.4	47.1	44.3
	Central Bank	0.0	0.0	0.0	0.0
	Comm. Banks	12.5	28.2	45.8	43.1
	NBFIs	0.6	1.2	1.3	1.2
Insurance Companies		9.9	22.3	16.0	15.1
Parastatals		2.5	5.6	4.2	4.0
of which NSSF		0.2	0.4	0.0	0.0
Building Societies		0.1	0.3	1.6	1.5
Others		18.9	42.4	37.4	35.2
Total		**44.5**	**100.0**	**106.3**	**100.0**

Source: Central Bank of Kenya

Long term government stocks remained unchanged at Ksh 1.5bn in June 2002, the same level as in June 2001. Of the outstanding stocks, the National Social Security Fund (NSSF) held Ksh 0.8bn while the other non-bank sector held Ksh 0.7bn.

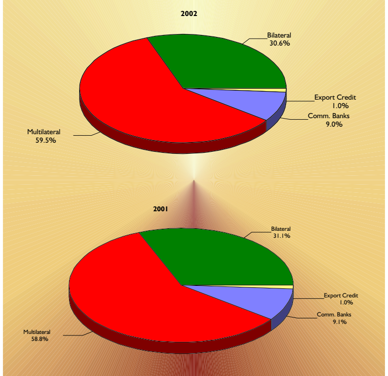
Domestic Debt Service

Government domestic debt service in fiscal year 2001/02 marginally increased to Ksh 23.7bn from Ksh 23.2bn in fiscal year 2000/01, reflecting increased government domestic borrowing. As a proportion of total government expenditure, domestic interest payments in the year were 10.5% compared with 10.0% in fiscal year 2000/01.

Of the Ksh 23.7bn domestic debt service, interest payment on Treasury bills amounted to Ksh 15.5bn or 65.4% compared with Ksh 17.1bn or 73.7% in the previous fiscal year. Interest paid on Treasury bonds and government overdraft at the Central Bank were Ksh 8.1bn and Ksh 2m, respectively, while interest payment on outstanding government stock was Ksh 0.1bn during the review period.

External Debt

CHART 4: EXTERNAL PUBLIC DEBT (US$ M)



Sources: Central Bank of Kenya and Treasury

External debt stock, including government guaranteed loans, decreased by 4.1% from Ksh 394.0bn at the end of June 2001 to Ksh 377.8bn at the end of June 2002 (Chart 4). This followed disbursements of Ksh 10.0bn and principal repayments of Ksh 26.8bn.

External debt continued to be dominated by multilateral and bilateral loans, which accounted for 90% of the total Long-term debt. As at the end of June 2002, multilateral debt accounted for 59.5%, bilateral debt 30.6%, commercial debt 9.0 % while suppliers credit was 1.0% of the total debt stock.

External Debt Service

Government external debt service in the 2001/02 fiscal year amounted to Ksh 33.0bn, compared with Ksh 15.1bn in 2000/01 fiscal year (Table 17). The lower payments in 2000/01 fiscal year was due to a successful external debt rescheduling of Ksh 21.8bn in principal repayments achieved in that fiscal year.

TABLE 17: DISTRIBUTION OF EXTERNAL PUBLIC DEBT

	Jun-99		Jun-00		Jun-01		Jun-02*	
	Ksh bn	%	Ksh bn	%	Ksh bn	%	Ksh bn	%
Bilateral	150.5	36.4	138.6	35.0	132.3	33.6	115.4	30.5
Multilateral	223.2	53.9	230.7	58.3	228.5	58.0	224.7	59.5
Commercial Banks	36.3	8.8	24.9	6.3	29.4	7.5	33.9	9.0
Export Credit	3.9	0.9	1.5	0.4	3.8	1.0	3.8	1.0
Total	**413.8**	**100.0**	**395.7**	**100.0**	**394.0**	**100.0**	**377.8**	**100.0**

*Provisional
Sources: Central Bank of Kenya and Treasury

As a proportion of revenue, external debt service in 2001/02 fiscal year stood at 16.8% compared with 7.8% during the previous year. Of the Ksh 33.0bn debt service, principal repayments accounted for Ksh 26.8bn, comprising Ksh 23.3bn central government debt service, Ksh 1.7bn repayment of government publicly guaranteed debt, and Ksh 1.8bn repayment of IMF debt by the Central Bank. Interest payments amounted to Ksh 6.2bn, comprising Ksh 5.8bn interest on central government debt service, Ksh 0.1bn interest on public guaranteed debt, and Ksh 0.2bn interest on IMF debt by the Central Bank.

During the year to June 2002, the overall balance of payments turned out a surplus of US$ 135m compared with a deficit of US$ 70m in the year to June 2001 (Table 18). The improvement in the overall balance of payments resulted from an increase in the capital account surplus and a narrowing in the current account deficit.

TABLE 18: BALANCE OF PAYMENTS (US$ M)

ITEM	Year to Jun 2001	Q1 Jul-Sep	Q2 Oct-Dec	Q3 Jan-Mar	Q4 Apr-June**	Year to June 2002**
OVERALL BALANCE	**-70**	**62**	**-23**	**20**	**76**	**135**
I. CURRENT ACCOUNT	**-293**	**-33**	**-142**	**-113**	**51**	**-237**
Goods	**-1627**	**-411**	**-381**	**-234**	**-215**	**-1241**
Exports (fob)	1872	462	431	520	494	**1906**
Coffee	126	21	15	17	27	**80**
Tea	461	100	88	128	97	**413**
Horticulture	249	48	57	72	66	**243**
Oil products	173	42	38	21	16	**116**
Other	863	250	233	282	289	**1054**
Imports (cif)	3499	873	812	754	709	**3148**
Oil	889	177	130	144	185	**636**
Chemicals	445	119	118	135	111	**484**
Manufactured Goods	406	113	99	100	102	**414**
Machinery & Transport Equipment	792	234	204	211	172	**821**
Other	967	230	261	164	138	**793**
Services	1334	377	239	122	266	**1005**
Non-factor services (net)	578	216	117	86	166	**586**
of which tourism	285	83	71	69	67	**289**
Income (net)	-116	-44	-43	-39	-23	**-150**
of which official interest	-117	-37	-26	-39	-25	**-127**
Current Transfers	872	205	165	74	124	**568**
Private (net)	737	183	143	57	107	**491**
Public (net)	135	22	22	17	16	**77**
II. CAPITAL & FINANCIAL ACCOUNT	223	95	119	133	24	**371**
Capital Tranfers (net)	63	17	17	20	18	**72**
Financial Account	160	78	102	113	7	**299**
Official, medium- & long-term	-214	-129	-4	-40	-17	**-190**
Inflows	284	38	46	50	47	**182**
Outflows	-498	-167	-50	-90	-65	**-372**
Private, medium- & long-term (net)	-1	66	30	-7	-35	**54**
Commercial Banks (net)	*-146*	*56*	*15*	*8*	*-18*	**60**
Other Private, medium- & long-term (net)	*145*	*10*	*15*	*-15*	*-17*	**-6**
Short Term and Errors & Ommissions (net)	277	141	76	160	59	**435**
Gross Reserves	**1466**	**1487**	**1459**	**1479**	**1563**	**1563**
Official	**955**	1054	1064	1077	1137	**1137**
in months of goods and non-factor	**3.1**	**3.4**	**3.5**	**3.5**	**3.5**	**3.5**
Commercial Banks	512	433	395	402	427	**427**

* Revised to reflect the new BOP presentation format
** Provisional

Source: Central Bank of Kenya

The Current Account

The current account deficit narrowed by US$ 57m to US$ 237m in the year to June 2002 from US$ 293m in the year to June 2001. The improvement in the current account reflected a reduction in the trade deficit following US$ 351m decline in imports which offset reduced inflows in the services account particularly transfers.

Merchandise Trade

The trade deficit narrowed to US$ 1,241m in the twelve months to June 2002 from US$ 1,627m in the twelve months to June 2001. This was attributed to a US$ 351m decrease in import payments. Export earnings rose by US$ 35m.

Exports

Exports amounted to US$ 1,907m in the year to June 2002 compared with US$ 1,872m in the year to June 2001 and was wholly due to increased earnings from non-traditional exports. Earnings from traditional exports, namely, coffee and tea, which account for 26% of all exports, fell by US$ 47m during the year. The decline in coffee export receipts was attributed to a 45% decline in coffee production to 42,698 tonnes in the year to June 2002 from 77,695 tonnes in the year to June 2001. Coffee prices, however, increased from US$ 1,335 per tonne to US$ 1,589 per tonne over the same period. Consequently, coffee export earnings fell to US$ 80m in the year to June 2002 from US$ 126m in the year to June 2001.

Unfavourable weather conditions adversely affected tea production in the twelve months to June 2002. Total tea production fell by 20,608 tonnes to 261,957 tonnes. Tea prices also fell to US$ 1,524 per tonne in the year to June 2002 from US$ 1,906 per tonne in the year to June 2001. Consequently, tea earnings fell by US$ 47m to US$ 413m in the year to June 2002 down from US$ 461m in the year to June 2001. Equally, horticulture and oil product export earnings declined by US$ 6m and US$ 56m, respectively, over the review period compared with the previous year.

The main export markets for Kenya in calendar year 2001 remained Uganda, the United Kingdom, Tanzania and the Netherlands with export values of Ksh 29.4bn, Ksh 16.5bn, Ksh 13.3bn, and Ksh 10.6bn, respectively. The share of merchandise exports from Kenya to the United States increased by 0.1% while exports to main European destinations, that is, the United Kingdom, the Netherlands, Germany, France and Belgium fell by 2.5%. Exports to the regional market, especially to Uganda increased by 1.3% while exports to Tanzania increased by 0.4%. The percentage shares of exports to Egypt and Pakistan, however, decreased by 0.3% and 1.3%, respectively.

Imports

During the year to June 2002, the value of imports declined to US$ 3,148m. The decline was mainly in private sector imports, reflecting the sharp drop in oil imports by 28.5%. Imports of chemicals, manufactured goods and machinery and transport equipment rose by 9.0%, 1.9% and 3.6%, respectively.

The main sources of imports in the year 2001 were the United States, United Arab Emirates, the United Kingdom and Saudi Arabia with import values of Kshs 38.3bn, Kshs 38.3bn, Kshs 24.3bn and Kshs 16.0bn, respectively. The share of imports from the traditional sources in Europe and the Middle East decreased by 1.3% and 6.1%, respectively. Import share of goods from Japan declined by 0.2% while the import share from the United States increased by 9.6% mainly due to the purchase of aircraft by Kenya Airways. Import share of goods from South Africa, however, declined by 3.9%.

Invisibles

The surplus on the services account narrowed by US$ 329m to US$ 1,005m during the year to June 2002 mainly due to a fall in the travel account and in private transfer receipts. The increase in net interest payments by US$ 30m also contributed to the reduced surplus in the services account.

Tourism earnings increased by US$ 4m to US$ 289m in the year to June 2002, while grants fell by US$ 304m from US$ 872m to US$ 568m, mainly reflecting decreased private transfers. Net private receipts declined from US$ 737m to US$

491m while official transfers also declined from US$ 135m to US$ 77m. The decline in transfers by US$ 304m during the reporting period was largely due to the reduction in drought-related external assistance following improved weather conditions.

Capital and Financial Account

The capital and financial account had a net inflow of US$ 371m in the year to June 2002 compared with US$ 223m in the year to June 2001. Most of the increase was in the financial account, which rose by US$ 139m, as the capital account improved by US$ 9m. The performance of the financial account partly reflected the increase in private capital inflows by US$ 57m and partly the US$ 126m decline in official external payments.

Short-term capital flows decreased to US$ 152m in the year to June 2002 from US$ 367m in the year to June 2001. This resulted from reduced inflows of US$ 198m as outflows increased by US$ 16m. Net medium- and long-term private inflows and net direct investment declined by US$ 48m and US$ 71m, respectively. Net foreign assets of commercial banks, however, decreased by US$ 206m.

Disbursements from multilateral and bilateral sources declined by US$ 103m from US$ 284m in the year to June 2001 to US$ 182m in the year to June 2002 following the continued withholding of external assistance under Poverty Reduction and Growth Facility. Official capital outflows also declined from US$ 498m in the year to June 2001 to US$ 372m in the year 2002 reflecting reduction in external debt repayments.

Foreign Exchange Reserves

Following the improved balance of payments position, foreign exchange reserves of the banking system rose by US$ 97m to stand at US$ 1,563m (equivalent to 5.1 months of imports of goods and non-factor services) at the end of June 2002 compared with US$ 1,466m at the end of June 2001. This was mainly due to a US$ 182m increase in gross official foreign exchange reserves to US$ 1,137m at the end of June 2002 from US$ 955m the previous year. The foreign exchange reserves of commercial banks, however, declined to US$ 427m at the end of June 2002 from US$ 512m at the end of June 2001.

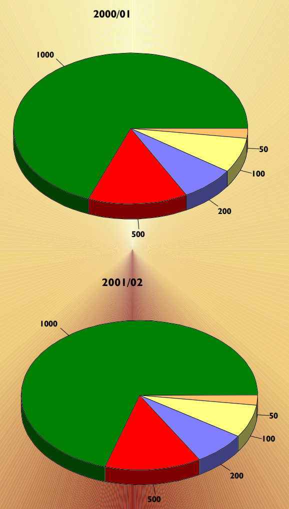
Overview

As provided for by the Central Bank of Kenya (Amendment Act) 1996, the Central Bank of Kenya continued to promote the safety and efficiency of the payments system in Kenya. Accordingly, the Bank discharged its overall responsibility of ensuring that the payments system facilitates financial system stability and the smooth implementation of monetary policy. Besides being the sole issuer of currency, the Central Bank has other main roles in the national payments system, namely, providing clearing and final settlement of payment obligations and participating in the system as banker to commercial banks and to the Government of Kenya.

Modes of Payment

Cash Payments

CHART 5: COMPOSITION OF ISSUED BANK NOTES BY DENOMINATION (KSH BN)



Source: Central Bank o Kenya

Cash comprising currency in circulation remained the most widely used form of payment because it has the advantage of convenience and immediate final transfer of value. Currency issued by the Central Bank rose to Ksh 122.6bn as at the end of June 2002 from Ksh 104.8bn as at the end of June 2001. Currency in circulation was dominated by the Ksh 1,000 and Ksh 500 denomination with their shares in total currency standing at 70.4% and 13.0%, respectively, as at the end of June 2002 (Table 19 and Chart 5). The currency issued totalled Ksh 122.6bn while deposits by commercial banks amounted

TABLE 19: CURRENCY ISSUED BY DENOMINATIONS (KSH M)

Denominations	2000/2001	2001/2002
1000.00	72,055.00	85,675.00
500.00	14,117.00	15,775.00
200.00	8,026.10	8,979.20
100.00	7,768.40	8,705.70
50.00	2,132.05	2,515.35
20.00	350.22	334.56
10.00	232.68	366.44
5.00	110.03	174.95
1.00	47.71	24.57
0.50	1.91	11.08
0.01	0.06	0.05
0.05	-	-
TOTAL	104,841.25	122,569.00

Source: Central Bank of Kenya

to Ksh 113.2bn. There was, therefore, a net currency issue of Ksh 9.4bn during the period under review (Table 20).

TABLE 20: CURRENCY INFLOWS AND OUTFLOWS (KSH M)

Inflow (deposits by banks)	2000/2001	2001/2002
Bank notes	100,224.00	112,505.00
Coins	652.00	694.00
Total	**100,876.00**	**113,199.00**
Outflow (withdrawal by banks)		
Bank notes	104,099.00	121,651.00
Coins	743.00	911.00
Total	**104,841.00**	**122,562.00**
Net	**-3,965.00**	**-9,363.00**

Source: Central Bank of Kenya

Cheques

The cheque has traditionally dominated non-cash payments accounting for 95% of all non-cash payments. Banker's cheques are used mainly for large value payments. In the year 2001, the average daily volume of cheques cleared through the Nairobi Clearing House amounted to 50,000 cheques valued at Ksh 10.5bn. High value payments of more than Ksh 10m took two days to clear, while low retail value payments nationally took three days. A single format for all types of cheques based on the Magnetic Ink Character Recognition (MICR) technology was recently introduced.

Payment Cards

The use of card-based payment system has increased significantly in recent years. These comprise credit cards, debit cards and pre-paid cards. The credit card is the most commonly used although debit cards are also becoming increasingly popular. Credit card business in Kenya has increased substantially over the last five years with the number of cards issued rising from 14,914 in 1997 to 45,893 in 2001. Consequently, outstanding credit card loans and advances has risen from Ksh 842m in June 1999 to Ksh 1954m in June 2002.

Developments Planned for the Payments System

The Central Bank of Kenya and the Kenya Bankers Association (KBA) have established the National Payments System (NPS) Committee. The main focus of the Committee is to formulate policies and regulations aimed at improving the efficiency of payments. The projects planned for implementation by the Committee include introduction of a multi-currency foreign cheque clearing arrangement and the introduction of shared automated teller machines (ATMs).

Local Foreign Cheque Clearing Arrangement

A self regulating local foreign currency clearing club comprising thirteen member banks has been in existence since August 1994 when the Central Bank authorized commercial banks to open foreign currency accounts with cheque book facilities. Non-members currently clear foreign cheques by aligning with a member bank to act as its clearing agent. The NPS Committee is, however, implementing a banking sector-wide local foreign cheque clearing arrangement, which should be operational by end of 2002. The main features of this arrangement are:

- Nairobi Automated Clearing House (ACH) to operate a multi-currency cheque clearing System under its own Rules and Regulations.
- It is to be an open access membership.
- Participating banks to maintain an account in US Dollar, the Euro and Sterling Pound and with a minimum of US$ 10,000 working day credit balance.
- The Central Bank to ensure smooth payment flows, institute risk management devices, guarantee the security and integrity of the system and meet the highest international standards.

Shared ATM/POS SWITCH

The shared automated teller machines (ATMs) is a project comprising a consortium of eighteen banks whose objective is to establish shared ATMs. The shared ATMs will operate under a trade name Kenswitch (Kenya Switch). The testing of the project has been going on and the project is expected to be completed by end of calendar year 2002.

Enabling Legislation

The Central Bank, in consultation with other stakeholders, intends to introduce an Electronic Transactions law. An Electronic Funds Transfer (EFT) Bill has already been drafted and is awaiting presentation to Parliament. The bill is intended to provide a legal framework establishing the rights, liabilities and responsibilities of participation in electronic funds transfer system. The Government has also adopted the UNCITRAL Model Law on E-Commerce and E-Systems. The draft Information Technology Bill 2002 is also currently under discussion by stakeholders.

Other Initiatives of the NPS

Some initiatives are either in the pilot or proposal stages. Those in the pilot stage include direct debit to facilitate payment of utilities and electronic clearing arrangement. The proposed initiatives include electronic exchange of information and promotion of SWIFT to facilitate Real Time Gross Settlement between banks.

During the year ending June 2002, the Bank continued to be represented in the East African Payments Systems Committee, which is charged with the development and harmonisation of payment systems within the region. Among the achievements of the Committee are automation of the three countries' clearing houses based on the E.A. Common Data Transfer Standards; development of guidelines for licensing and regulating E-money schemes and products; formation of E.A. SWIFT Technical Working Groups; harmonisation of Definition of Payment Systems; Concepts and Terms; checklist for payment systems oversight; and development of Risk Management Measures.

CENTRAL BANK OF KENYA
DIRECTORS' REPORT
FOR THE YEAR ENDED 3O JUNE 2002

The directors submit their report together with the audited financial statements for the year ended 30 June 2002, which disclose the state of affairs of the Bank.

INCORPORATION

The Bank is incorporated under the Central Bank of Kenya Act (the Act)

PRINCIPAL ACTIVITIES

The Central Bank of Kenya is established and administered under the Act with the principal object of formulating and implementing monetary policy directed to achieving and maintaining stability in the general level of prices. It is also the responsibility of the Bank to foster the liquidity, solvency and proper functioning of a stable market-based financial system.

RESULTS

The results for the year are set out on page 44.

DIVIDEND

The Board of Directors recommends the payment of a dividend of Ksh 2,110 million (2001: Ksh 2,290 million) to the Government of Kenya of which, Ksh 1 billion is to be applied to recover the amounts due from the Government of Kenya.

DIRECTORS

The directors who served during the year and up to the date of this report are listed on page iii.

AUDITORS

In accordance with the Bank policy of rotating audit firms every four years, the Board of Directors appointed Pricewaterhouse Coopers in place of the outgoing auditors, KPMG Peat Marwick, to join Ernst & Young as joint auditors of the Bank for the financial year 2001/2002.The appointment of Ernst & Young and Pricewaterhouse Coopers as auditors of the Bank for the financial year 2002/2003 shall be recommended to the Board of Directors of the Bank for consideration and approval.

By order of the Board

SECRETARY

20th September 2002

CENTRAL BANK OF KENYA
STATEMENT OF DIRECTORS' RESPONSIBILITIES
ON THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 JUNE 2002

We, the directors certify that:

1. We are responsible for the preparation of financial statements, which present a true and fair view of the state of affairs of the Bank and of its operating results.

2. The financial statements have been prepared in accordance with International Accounting Standards and comply with the Central Bank of Kenya Act.

3. We are responsible for safeguarding the assets of the Bank.

4. We are responsible for establishing and maintaining systems of internal control designed to provide reasonable assurance as to the integrity and reliability of the Bank's financial reporting.

5. The directors are of the opinion that the financial statements for the year ended 30th June 2002 fairly present the financial position and operating results of the Bank.

6. Nothing has come to the attention of the directors to indicate that the Bank will not remain a going concern for at least the next twelve months from the date of this statement.

Signed on behalf of the Board of Directors by:

______________________ **Governor**

______________________ **Director**

Dated 28/09. 2002

REPORT OF THE JOINT AUDITORS TO THE MEMBERS OF CENTRAL BANK OF KENYA

We have audited the financial statements set out on pages 44 to 60. We have obtained all the information and explanations which to the best of our knowledge and belief were necessary for the purposes of our audit. The financial statements are in agreement with the books of account.

RESPECTIVE RESPONSIBILITIES OF DIRECTORS AND AUDITORS

As stated on page 42, the directors are responsible for the preparation of financial statements, which give a true and fair view of the state of affairs of the Bank and of its operating results. Our responsibility is to express an independent opinion on the financial statements based on our audit and to report our opinion to you.

BASIS OF OPINION

We conducted our audit in accordance with International Standards on Auditing. Those standards require that we plan and perform our audit to obtain reasonable assurance that the financial statements are free from material misstatement. An audit includes an examination, on a test basis, of evidence supporting the amounts and disclosures in the financial statements. It also includes an assessment of the accounting policies used and significant estimates made by the directors, as well as an evaluation of the overall presentation of the financial statements.

OPINION

In our opinion, proper books of account have been kept and the financial statements give a true and fair view of the state of the Bank's financial affairs at 30 June 2002 and of its profit and cash flows for the year then ended and comply with International Accounting Standards and the Central Bank of Kenya Act.

Certified Public Accountants

Ernst & Young and Pricewaterhouse Coopers

Ernst & Young	Pricewaterhouse Coopers
Kenya - Re Towers, Upperhill	The Rahimtulla Tower
Off Ragati Road	Upper Hill Road
P O Box 44286	P O Box 43963
00100 Nairobi, Kenya	00100 Nairobi, Kenya

Dated 20th September 2002

CENTRAL BANK OF KENYA
PROFIT AND LOSS ACCOUNT
FOR THE YEAR ENDED 30 JUNE 2002

	Note	2002 Ksh m	2001 Ksh m
Interest income	1	3,413	4,437
Interest expenses	2	(2,266)	(2,033)
Net interest income		1,147	2,404
Fee and commission income		4,256	4,289
Net foreign exchange income/ (expense)	3	5,390	(576)
Other operating income	4	149	166
Operating income		10,942	6,283
Operating expenses	5	(3,326)	(2,838)
Bad and doubtful debts expense		(2)	(10)
Net profit from ordinary activities		7,614	3,435
Charge in respect of deferred receivable	10	(1,801)	(1,000)
Net profit		5,813	2,435
Dividends:			
Interim dividends – paid in the year		-	1,000
Proposed final dividend for the year		2,110	1,290
		2,110	2,290

Source: Central Bank of Kenya

CENTRAL BANK OF KENYA

BALANCE SHEET

AS AT 30 JUNE 2002

ASSETS	**Note**	**2002 Ksh m**	**2001 Ksh m**
Balances due from banking institutions and gold holdings	6	88,463	74,734
Items in the course of collection		5,669	7,351
Investments in government securities	7	1,619	1,420
Loans and advances	8	5,909	7,395
Deferred receivables	9	-	1,801
Other assets	10	227	439
Retirement benefit asset	11	287	289
Property and equipment	12	831	633
Due from Government of Kenya	13	54,559	55,559
TOTAL ASSETS		157,564	149,621
LIABILITIES			
Currency in circulation		51,867	46,677
Deposits	14	67,326	79,776
Amounts repayable under repurchase agreements	15	27,127	16,878
Other liabilities	16	683	252
TOTAL LIABILITIES		147,003	143,583
EQUITY AND RESERVES			
Capital	18	1,500	1,500
General reserve fund		7,951	4,248
Proposed dividend		1,110	290
TOTAL EQUITY AND RESERVES		10,561	6,038
TOTAL LIABILITIES AND EQUITY		157,564	149,621

The financial statements were approved by the Board of Directors on 25th September 2002 and signed on its behalf by:

....

Governor Director

Source: Central Bank of Kenya

CENTRAL BANK OF KENYA
STATEMENT OF CHANGES IN EQUITY
FOR THE YEAR ENDED 30 JUNE 2002

Year ended 30 June 2001	**Share capital Ksh m**	**General reserve fund Ksh m**	**Proposed dividends Ksh m**	**Total Ksh m**
Balance at start of year	1,500	4,103	1,000	6,603
Net profit for the year	-	2,435	-	2,435
Dividends:				
-Final proposed for 2001	-	(2,290)	2,290	-
-Final for 2000 paid	-	-	(1,000)	(1,000)
-Applied to amounts due from Government of Kenya	-	-	(1,000)	(1,000)
-Interim for 2001 paid	-	-	(1,000)	(1,000)
Balance at end of year	1,500	4,248	290	6,038
Year ended 30 June 2002				
Balance at start of year	1,500	4,248	290	6,038
Net profit for the year	-	5,813	-	5,813
Dividends:				
-Final proposed for 2002	-	(2,110)	2,110	-
-Applied to amounts due from Government of Kenya	-	-	(1,000)	(1,000)
-Final for 2001 paid	-	-	(290)	(290)
Balance at end of year	1,500	7,951	1,110	10,561

Source: Central Bank of Kenya

CENTRAL BANK OF KENYA
CASH FLOW STATEMENT
FOR THE YEAR ENDED 30 JUNE 2002

	Note	2002 Ksh m	2001 Ksh m
OPERATING ACTIVITIES			
Net cash from operating activities	17 (a)	4,864	11,332
INVESTING ACTIVITIES			
(Investments)/ liquidation of government securities		(199)	1,631
Purchase of property and equipment		(386)	(71)
Proceeds from sale of property and equipment		4	2
(Investment in)/ liquidation of IMF-SDR accounts		(49)	44
Net cash generated (absorbed by)/ from investing activities		(630)	1,606
FINANCING ACTIVITIES			
Dividends paid		(290)	(2,000)
Currency in circulation		5,190	3,827
Net cash from financing activities		4,900	1,827
Net increase in cash and cash equivalents		9,134	14,765
Cash and cash equivalents at beginning of year		68,822	55,076
Foreign exchange revaluation gains/ (losses)		4,727	(1,019)
Cash and cash equivalents at end of year	17 (b)	82,683	68,822

Source: Central Bank of Kenya

CENTRAL BANK OF KENYA
ACCOUNTING POLICIES
FOR THE YEAR ENDED 30 JUNE 2002

The principal accounting policies adopted in the preparation of these financial statements are set out below:

(a) Basis of preparation and form of preparation

(i) Basis of preparation

The financial statements are prepared in accordance with International Accounting Standards (IAS). The financial statements are presented in millions of Kenya shillings (Ksh million) and are prepared under the historical cost convention as modified by the revaluation of certain financial instruments.

(ii) Form of presentation

In exceptional circumstances, as allowed by Section 36 of the Act, the Bank may act as the "lender of last resort" to financial institutions in difficulty in order to prevent a loss of confidence in spreading through the financial system as a whole. In some cases, confidence can best be sustained if the Bank's support is disclosed only when the conditions giving rise to potential instability in the economy have improved. Although the financial effects of such operations are included in the financial statements of the Bank, these statements may not explicitly identify such support.

(b) Revenue recognition

Income is recognised in the period in which it is earned. Income is not accrued if its recoverability is considered doubtful.

(c) Translation of foreign currencies

Transactions in foreign currencies during the year are converted into Kenya Shillings at rates ruling at the transaction dates. Assets and liabilities at the balance sheet date, which are expressed in foreign currencies, are translated into Kenya Shillings at rates ruling at that date. The resulting differences from conversion and translation are dealt with in the profit and loss account in the year in which they arise.

(d) Employee benefits

The Bank's employees are eligible for retirement benefits under a defined benefit plan provided through a separate fund. The defined benefit plan is funded by the Bank and the Deposit Protection Fund Board, a related party.

The Bank's net obligation in respect to the plan is calculated by estimating the amount of future benefits that employees have earned in return for their service in the current and prior periods; that benefit is discounted to determine the present value and the fair value of any plan assets is deducted. The calculation is performed by a qualified actuary using the Projected Unit Credit Method.

Where the calculation results in a benefit to the Bank, the recognised asset is limited to the net total of any unrecognised actuarial losses and past service costs and the present value of any future refunds from the plan or reduction in future contributions to the plan. Actuarial gains and losses are charged to the profit and loss account over the remaining working lives of the employees participating in the scheme.

The Bank also makes contributions to a statutory pension scheme, the National Social Security Fund (NSSF). Contributions to the scheme are determined by local statute and are shared between the employer and employee.

The Bank also provides free medical treatment to its entire staff and their children.
The estimated monetary liability for employees' accrued leave entitlement at the balance sheet date is recognised as an expense accrual.

(e) Property and equipment

Items of property and equipment are stated at purchase price less accumulated depreciation.

Depreciation is computed on the straight line basis over the estimated useful lives of the assets at the following rates:

Land and building	10%
Motor vehicles, furniture and equipment	50%

(f) Financial assets and liabilities

The Bank presents financial assets and liabilities, and the associated income and expense streams, by distinguishing between foreign currency and local currency activities. Foreign currency activities mainly arise from the Bank's foreign reserves management function. Local currency activities mainly reflect the assets and liabilities associated with monetary policy implementation, issuance of currency in circulation and banking activities.

The separate reporting of these activities, is considered to provide a better presentation of the Bank's financial position, financial performance and risk profile.

All financial assets and liabilities are recognised on a trade date basis. The purchases and sales of financial assets and liabilities are recognised from the date the Bank commits to purchase/ sell the financial instrument.

(i) Investment securities

Investments in securities include debt securities which management intends to hold until maturity and are stated at cost adjusted of amortisation premiums and discounts over the period to maturity. To determine amortised cost, investments are grouped into their respective currencies and only if the group cost is lower than recoverable amounts a provision is made against that group. Interest and discounts earned on investment securities are reported as interest income.

(ii) Currency in circulation

Currency issued by the Bank represents a claim on the Bank in favour of the holder. The liability for currency in circulation is recorded at face value in the Balance Sheet.

(iii) Repurchase and reverse-purchase transactions

Securities issued by the Bank for monetary policy operations with an agreement to repurchase are disclosed in the balance sheet as liabilities and are stated at sales price. The difference between the sales price and the face value (repurchase price) represents interest expense and is accrued and amortised over the term of the contract.

(iv) **Other assets and liabilities**

The following financial assets and liabilities are valued and recognised in financial statements at transaction date value:

-Loans and advances
-Deposit

(g) Loans and provisions for loans impairment

As the lender of last resort, the Bank may grant loans or advances for fixed periods not exceeding six months to commercial banks that pledge Government securities specified by the Bank.

In its capacity as the fiscal agent and banker to the Government, the Bank may make direct advances to the Government for the purpose of offsetting fluctuations between receipts from the budget revenue and the payments of the Government. The total amount of advances to the Government outstanding shall not exceed five percent of the gross recurrent revenue of the Government as shown in the Appropriation Accounts for the latest year for which those accounts have been audited by the Controller and Auditor-General.

The Bank also operates a staff loans scheme for its employees for the provision of facilities such as house and car loans.

The Bank determines the terms and conditions for granting of the above loans with reference to the prevailing market interest rates and may determine different rates for different classes of transactions and maturities.

Specific provisions for doubtful debts are made in respect of advances. The provisions are based on periodic evaluations of advances and take account of past loss experience, economic conditions and estimated value of any underlying collateral and are charged to the profit and loss account.

When a loan is deemed uncollectable, it is written off against the related provision for impairments. Subsequent recoveries are credited to the income statement if previously written off.

(h) Cash and cash equivalents

For purposes of presentation of cash flows in the financial statements, cash and cash equivalents consist of balances held in current accounts and term deposit and investments in foreign treasury bills and gold holdings.

(i) Taxation

No provision for tax is made as Section 7 of the Act exempts the Bank from any taxation imposed by law in respect of income or profits. This exemption includes stamp duty in respect of instruments executed by or on behalf of the Bank.

(j) Dividends Payable

Dividends are recognised as a liability in the period in which they are declared. Proposed dividends are disclosed as a separate component of equity.

(k) Comparatives

Where necessary, comparative figures have been adjusted or extended to conform with changes in presentation in the current year.

CENTRAL BANK OF KENYA
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 30 JUNE 2002

		2002 Ksh m	2001 Ksh m
1	**Interest Income**		
	Foreign investments earnings	2,738	3,685
	Local investments earnings	583	654
	Other interest earnings	92	98
		3,413	4,437
2	**Interest expenses**		
	Interest on monetary policy issues	2,229	1,987
	Interest paid to IMF	31	40
	Interest on customer deposits	6	6
		2,266	2,033
3	**Foreign exchange income / (expenses)**		
	Gains on sale of foreign exchange	663	443
	Foreign exchange revaluation gain / (loss)	4,727	(1,019)
		5,390	(576)
4	**Other operating income**		
	Rent received	16	15
	Proceeds from disposal of property	4	2
	Tuition fees and other charges	85	77
	Miscellaneous receipts	44	72
		149	166
5	**Operating expenses**		
	The following items are included within operating expenses:		
	- Depreciation	188	318
	- Auditors' remuneration	5	3
	- Staff costs	1,762	1,394

The average number of employees during the year was 1260 (2001: 1274).

		2002 Ksh m	2001 Ksh m
6	**Balances due from banking institutions and gold holdings**		
	Current accounts	2,720	3,116
	Term deposits	79,951	65,696
	Gold holdings	12	10
	Cash and cash equivalents	82,683	68,822
	Accrued interest on foreign investments	231	647
	Special Drawing Rights	71	22
	Total own resources	82,985	69,491
	Special project accounts	5,478	5,243
		88,463	74,734

CENTRAL BANK OF KENYA

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 30 JUNE 2002

	2002 Ksh m	2001 Ksh m
7 Investment in government securities		
Government stock	742	706
Treasury bonds	120	185
Treasury bills	757	529
	1,619	1,420

	2002 Ksh m	2001 Ksh m
8 Loans and advances		
Advances to banks under liquidation	8,245	8,275
Overnight advances to banks	-	107
Other advances to banks	2,313	1,102
Government overdraft account (Note 19)	-	2,862
Advances to employees (Note 19)	1,547	1,383
IMF funds on-lent to the Government	2,079	1,968
	14,184	15,697
Provision for bad and doubtful debts	(8,275)	(8,302)
Net advances as at 30 June	5,909	7,395
Movement in the provisions for bad and doubtful debts is as follows:		
At start of year	(8,302)	(8,331)
Additions in the year	(2)	(10)
Recoveries in the year	29	39
At end of year	(8,275)	(8,302)

Section 46(3) of the Act sets the limit of the Government of Kenya's overdraft facility at 5% of the Gross Recurrent Revenue as reported in the latest audited accounts. This limit, as in the previous year, stands at Ksh 8,753,160,998 which is based on the Government accounts for 1997/1998, which are the latest audited accounts.

	2002 Ksh m	2001 Ksh m
9 Deferred receivable		
At start of year	1,801	-
Disposal proceeds on property and equipment	-	2,807
Prior year over accrual reversed	-	(6)
Charge for the year	(1,801)	(1,000)
At end of year	-	1,801

The deferred receivable account relates to the disposal proceeds of the Times Tower from the Government of Kenya. The entire balance outstanding has been fully amortised in this financial year through the profit and loss account.

	2002	2001
10 Other assets	**Ksh m**	**Ksh m**
Impersonal accounts	-	357
Sundry debtors	227	82
	227	439

11 Retirement benefit asset

The amounts recognised in the balance sheet are determined as follows:		
Present value of funded obligations	4,384	3,790
Fair value of plan assets	(4,713)	(4,140)
Present value of net asset	(329)	(350)
Unrecognised actuarial gain	42	61
Asset in the balance sheet	(287)	(289)
The amounts recognised in the profit and loss account are as follows:		
Current service costs	269	224
Interest costs	349	304
Expected return on plan assets	(379)	(327)
Total expenses included in operating expenses	239	201
Movements in the net asset recognised in the balance sheet are as follows:		
Overstatement of asset in previous year	(1)	-
Employer contributions	(236)	(228)
Movement in the asset recognised in the balance sheet	2	(27)
Actual return on plan assets	422	412

The principal actuarial assumptions at the balance sheet date were:

	2002	2001
Discount rate (p.a)	9%	9%
Salary increase (p.a)	7%	7%
Expected return on plan assets (p.a)	9%	9%
Future pension increases	0%	0%

The Bank's employees are eligible for retirement benefits under a defined benefit plan provided through a separate fund. The defined benefit plan is funded by the Bank and the Deposit Protection Fund Board, a related party. The retirement benefit asset is wholly recognised in the financial statements of the Bank while the Deposit Protection Fund Board recognised contributions to the fund as if it were a defined contribution scheme.

CENTRAL BANK OF KENYA

NOTES TO THE FINANCIAL STATEMENTS (Continued)

FOR THE YEAR ENDED 30 JUNE 2002

		Land and buildings Ksh m	Motor Vehicles Ksh m	Furniture and equipment Ksh m	Total Ksh m
12	**Property and equipment**				
	Cost				
	At start of year				
	-As previously stated	1,000	76	888	1,964
	-Reinstated assets	-	47	-	47
	As restated	1,000	123	888	2,011
	Additions	300	21	65	386
	Disposals	-	(2)	(4)	(6)
	At end of year	1,300	142	949	2,391
	Depreciation				
	At start of year				
	-As previously stated	468	68	795	1,331
	-Reinstated accumulated depreciation	-	47	-	47
	As restated	468	115	795	1,378
	On disposal	-	(2)	(4)	(6)
	Charge for the year	123	11	54	188
	At end of year	591	124	845	1,560
	Net book value				
	At 30 June 2002	709	18	104	831
	At 30 June 2001	532	8	93	633

Assets with acquisition cost of Ksh 47 million were initially recorded at net book values. In the current year, the values were adjusted to reflect the assets' costs with corresponding adjustments to accumulated depreciation.

		2002 Ksh m	2001 Ksh m
13	**Due from Government of Kenya**		
	Recoverable from future dividends:		
	Balance at start of year	18,642	19,642
	Recovery in the year	(1,000)	(1,000)
	Balance at end of year	17,642	18,642
	Loan due from Government	36,917	36,917
		54,559	55,559

Under Section 51 of the Act, the amount outstanding in the revaluation account at 1 July 1997 is recoverable from future dividends payable to the Government of Kenya. This amount attracts no interest and has no fixed repayment period. The directors are confident that this amount will be recovered in full out of future distributable profits of the Bank.

Pursuant to Section 46(4) of the Act, the overdrawn accounts of the Kenya Government were converted to a loan with effect from 1 July 1997. The loan is unsecured, interest free and has no fixed repayment period.

14 Deposits	2002 Ksh m	2001 Ksh m
Banks -Kenya	24,594	21,965
-External	16	8
Non-bank financial institutions	424	671
Other public entities and project accounts	7,767	7,970
International Monetary Fund	9,579	10,805
Government of Kenya	24,946	38,357
	67,326	79,776

15 Amounts repayable under repurchase agreements

These are securities issued and utilised by the Bank for monetary policy purposes and are shown as a liability of the Central Bank of Kenya to the buyers. Securities sold under repurchase agreements worth Ksh 27,127million were outstanding as at 30 June 2002 (2001: Ksh 16,878million).

16 Other liabilities	2002 Ksh m	2001 Ksh m
Impersonal accounts	398	-
Sundry creditors	217	154
Refundable deposits	33	26
Commission for EEC Development deposits	15	50
Sundry suspense accounts	20	22
	683	252

17 (a) Cashflows from operating activities

Net profit for the year	5,813	2,435
Adjustments for:		
Charge in respect of deferred receivable	1,801	1,000
Depreciation	188	318
Defined benefit scheme costs	2	(27)
Gain on sale of property and equipment	(4)	(2)
Foreign exchange revaluation (gains)/ losses	(4,727)	1,019
Operating profit before working capital changes	3,073	4,743
Net decrease in loans and advances	1,486	3,762
Increase in amounts repayable under repurchase agreements	10,249	6,358
Decrease in deposits	(12,450)	(3,336)
(Increase)/ decrease in project accounts	(235)	1,197
Decrease in accrued interest on balances due from banking institutions	416	61
Decrease/ (increase) in items in the course of collection	1,682	(1,333)
Decrease / (increase) in other assets	212	(50)
Increase/ (decrease) in other liabilities	431	(70)
Net cash generated from operations	4,864	11,332

CENTRAL BANK OF KENYA
NOTES TO THE FINANCIAL STATEMENTS (Continued)
FOR THE YEAR ENDED 30 JUNE 2002

17 Cash and cash equivalents

(b) Cash and cash equivalents included in the cashflow statement comprise the following balance sheet accounts:

Current accounts and term deposits	82,671	68,812
Gold holdings	12	10
	82,683	68,822

18 Share capital

Authorised share capital	5,000	5,000
Issued and fully paid	1,500	1,500

19 Related party transactions

In the course of its operations, the Bank enters into transactions with related parties. Related parties include the Government of Kenya, as the ultimate owner of the Bank and the Deposit Protection Fund Board. Unless otherwise stated, all transactions between these entities take place at arm's length and with reference to market rates.

(i) Staff loans

The Bank also extends loan facilities to its members of staff including the Governor and the Deputy Governor. Loans and advances (Note 8) include advances to employees, which as at 30 June amounted to Ksh 1,547 million. (2001: Ksh 1,383 million.). The advances are at preferential rates of interest determined by the Bank.

19 Related party transactions (continued)

	2002 Ksh m	2001 Ksh m
(ii) Loans to directors		
At 1 July	1	-
Loans advanced during the year	13	1
Loan repayments	(3)	-
At 30 June	11	1
(iii) Directors emoluments:		
Fees	1	2
Other remuneration	13	13

(iv) Government of Kenya

Transactions entered into with the Government include:

(a) Banking services;
(b) Management of issue and redemption of securities at a commission; and
(c) Foreign currency denominated debt settlement and other remittances at a fee.

As at the close of business on 30 June, the following balances, which are included in various balance sheet categories, were outstanding:

	2002 Ksh m	2001 Ksh m
Due from Government of Kenya (Note 13)	54,559	55,559
Overdraft account (Note 8)	-	2,862
IMF funds on lent to the Government	2,079	1,968
Government of Kenya deposits (Note 14)	24,946	38,357
Investments in GOK Securities (Note 7)	1,619	1,420

(v) Deposit Protection Fund Board

The Bank has a close working relationship with the Deposit Protection Fund Board an entity incorporated under the Banking Act and provides it with staff and office accommodation. The costs incurred on behalf of The Deposit Protection Fund Board are fully reimbursed by the Board to the Bank. The Deposit Protection Fund Board is also a co-sponsor of the Central Bank of Kenya Staff Pension Fund.

The balance outstanding and included in other assets as at year end was Ksh 8 million (2001- Ksh 27 million).

Kenya School of Monetary Studies

The Kenya School of Monetary Studies is a registered legal entity wholly owned by the Central Bank. The School is operated as a department of the Bank and results of its operations are incorporated in the financial statements of the Bank.

CENTRAL BANK OF KENYA
NOTES TO THE FINANCIAL STATEMENTS (Continued)
FOR THE YEAR ENDED 30 JUNE 2002

20 Liquidity risk

The table below analyses assets and liabilities into relevant maturity groupings based on the remaining period at 30 June 2002 to the contractual maturity date.

Assets	On Demand Ksh m	Due within 3 months Ksh m	Due between 3-12 months Ksh m	Due between 1-5yrs Ksh m	Due after 5 years Ksh m	
Balances due from banking institutions and gold holdings	8,210	80,182	-	-	71	88,463
Items in the course of collection	5,669	-	-	-	-	5,669
Investments in government securities	-	757	-	120	742	1,619
Loans and advances	2,283	71	196	886	2,473	5,909
Other assets	227	-	-	-	-	227
Retirement benefit asset	-	-	-	-	287	287
Property and equipment	-	-	-	-	831	831
Due from Government of Kenya	-	-	-	-	54,559	54,559
Total assets	16,389	81,010	196	1,006	58,963	157,564
Liabilities						
Currency in circulation	-	-	-	-	51,867	51,867
Deposits	49,980	-	729	16,617	-	67,326
Amounts repayable under repurchase agreements	-	27,127	-	-	-	27,127
Other liabilities	683	-	-	-	-	683
Equity and reserves	-	-	-	-	10,561	10,561
Total liabilities and equity	50,663	27,127	729	16,617	62,428	157,564
Liquidity gap 2002	(34,274)	53,883	(533)	(15,611)	(3,465)	-
As at 30 June 2001						
Total assets	33,827	69,717	2,184	801	43,092	149,621
Total liabilities and equity	69,223	17,225	1,381	9,077	52,715	149,621
Liquidity gap 2001	(35,396)	52,492	803	(8,276)	(9,623)	-

21 Currency risk

The various currencies to which the Bank is exposed at 30 June 2002 are summarised in the table below (all expressed in Ksh million):

	USD	GBP	EURO	SDR	GOLD	OTHER	Total
Assets							
Balances due from banking institutions	26,339	38,439	23,504	-	-	98	88,380
Special Drawing Rights	-	-	-	71	-	-	71
Gold holdings	-	-	-	-	12	-	12
Total assets	26,339	38,439	23,504	71	12	98	88,463
Liabilities							
Balances due to IMF	-	-	-	9,579	-	-	9,579
Balances due to Commissions for EEC Development Fund.	-	15	-	-	-	-	15
Forex Bureaux Deposits	20	-	-	-	-	-	20
Total liabilities	20	15	-	9,579	-	-	9,614
Net balance sheet position 2002	26,319	38,424	23,504	(9,508)	12	98	78,849
As at 30 June 2001							
Total assets	35,958	27,821	10,446	22	10	477	74,734
Total liabilities	20	50	-	10,805	-	-	10,875
Net balance sheet position 2001	35,938	27,771	10,446	(10,783)	10	477	63,859

CENTRAL BANK OF KENYA
NOTES TO THE FINANCIAL STATEMENTS (Continued)
FOR THE YEAR ENDED 30 JUNE 2002

22 INTEREST RATE RISK

This table shows the extent to which the Bank's interest rate exposures on assets and liabilities are matched. Items are allocated to time bands by reference to the earlier of the next contrac-

	3 months or less Ksh m	Between 3 - 12 months KShs m	Over 1 year KShs m	Non-Interest bearing KShs m	Total Ksh m
Assets					
Balances due from banking institutions and gold holdings	82,914	-	-	5,549	88,463
Items in the course of collection	-	-	-	5,669	5,669
Investments in government securities	757	-	862	-	1,619
Loans and advances to banks	2,354	196	3,359	-	5,909
Other assets	-	-	-	227	227
Retirement benefit asset	-	-	-	287	287
Property and equipment	-	-	-	831	831
Due from Government of Kenya	-	-	-	54,559	54,559
Total assets	86,025	196	4,221	67,122	157,564
Liabilities and equity					
Currency in circulation	-	-	-	51,867	51,867
Deposits	-	729	16,617	49,980	67,326
Amounts repayable under repurchase agreements	27,127	-	-	-	27,127
Other liabilities	-	-	-	683	683
Equity and reserves	-	-	-	10,561	10,561
Total liabilities and equity	27,127	729	16,617	113,091	157,564
Interest sensitivity gap 2002	58,898	(533)	(12,396)	(45,969)	-
As at 30 June 2001					
Total assets	77,117	1,184	-	71,320	149,621
Total liabilities and equity	17,225	1,381	9,077	121,938	149,621
Interest sensitivity gap 2001	59,892	(197)	(9,077)	(50,618)	-