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KENYA



CENTRAL  
BANK OF  
KENYA

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## **BANKING CIRCULAR No. 6 OF 2008**

**TO: CHIEF EXECUTIVES OF COMMERCIAL BANKS**

### **INTRODUCTION OF THE INTER BANK ("Horizontal") MASTER REPURCHASE AGREEMENT (MRA).**

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A Repurchase Agreement (Repo) is a money market financial instrument, used to facilitate monetary operations and the development of liquid financial markets. In June 2006, Central Bank of Kenya (CBK) entered into a Master Repurchase Agreements (MRA) with commercial banks, to support the implementation of CBK's "Vertical" Repo program for monetary system liquidity management and Intra-Day Liquidity Facility (ILF) transactions.

The Central Bank of Kenya (CBK) has been facilitating the introduction of an additional Master Repurchase Agreement (MRA) for commercial banks, to govern repurchase transactions between commercial banks ("Horizontal" Repo). To facilitate its introduction, preliminary assessment, deliberations and related activities, were conducted through an Interbank Repo Committee comprising representation by CBK officials and a Treasurers Forum, representing approximately ten commercial banks, which was constituted by CBK in June, 2007. After extensive deliberations, the Committee agreed on the following key issues pertaining to the program:

- i) The consensus to adopt the Global Master Repurchase Agreement (GMRA) model developed by the International Securities Market Association (ISMA) and the Bond Market Association (BMA) in 2000. This was customized to suit the domestic market situation, taking cognizance of technological levels of development and state of the market.
- ii) The recommendation that CBK should circulate the proposed MRA, along with associated program description, explanatory notes, as well as a process flow document, to enable bank officers and associated



persons, appreciate the characteristics and operations of the proposed Horizontal Repo Program.

- iii) Following the amendment of the Internal Loans Act (ILA) in October 2007, the process of gazettelement of the regulations to the Act, to give it a commencement date, should be embarked upon. This is currently on course. The amended Act will explicitly recognize dematerialization and secondary trading of Government securities. Notwithstanding the preceding, the Bank, on considering the compelling mitigating factors for expedited rolling out Horizontal Repos, took a decision to fast track the implementation of this program, while awaiting gazettelement. Consequently therefore, the execution of the Master Repurchase Agreement (MRA) for Horizontal Repos and introduction of Horizontal Repos between banks should proceed. In the meantime the Bank will make a deliberate effort to ensure a speedy conclusion of the gazettelement process.
- iv) The importance of ensuring compliance with the Capital Markets Authority's (CMA) statutory provisions, with regard to Repos involving listed securities, was highlighted. Given the nature of the proposed facility, the Committee expressed the expectation that the Horizontal Repo transactions would be processed in a secure and efficient manner, which would result in Delivery versus Payment (DVP). Taking cognizance of that position, CBK sought and was granted approval by the Capital Markets Authority (CMA), for Repo transactions involving Treasury Bonds, conducted under the MRA, to be transferred without going through the securities exchange. This approval was granted on the understanding that the Horizontal Repo Program currently being introduced does not constitute an outright sale of securities but are essentially financing arrangements with a predetermined repurchase date.
- v) In customizing the MRA, the Committee recognized that certain provisions in the Global Master Repurchase Agreement (GMRA) do not conform to the existing infrastructure and/or market practices. For example, one such variation is with regard to clause 6(h) and (i) of the GMRA which provides for 'Settlement Netting'. In Kenya, CBK's settlement platform operates on a "Gross Settlement" basis. Accordingly and in order to address the identified differences, the CBK has introduced a Supplementary Annex No. 1 to the MRA to amend the relevant portions of the MRA whilst providing an explanation for the amendments. Also, whereas the GMRA provides for eligible



collateral to include government securities and other financial instruments, the Repo being introduced will allow only Government securities (i.e., Treasury bonds and bills) to be used as collateral.

Pursuant to this program being introduced, Horizontal Repos will be conducted between commercial banks. Banks participating in this facility will be required to execute and exchange Master Repurchase Agreements among themselves and notify CBK through a prescribed duly authorized letter listing counterparties to the agreement.

Any subsequent variations, amendments or changes to the Agreement will be dealt with similarly.

**The purpose of this Banking Circular is therefore to;**

1. Forward to all commercial banks, the following documents, in connection with the program:
  - i) Master Repurchase Agreement.
  - ii) Guidelines for the operations of Horizontal Repo Transactions.
  - iii) Process Flow Document.
  - iv) Code of Conduct
  - v) Letter of confirmation of executed MRA with counterparts
2. Advise all commercial banks that, effective **Friday, September 12, 2008**, CBK will introduce a Horizontal Repo transaction platform for inter-bank participants. This facility will be under the Monetary Operations & Debt Management Department of the Bank. All dealings, delivery and settlement instructions shall be conveyed via the prescribed SWIFT message types as set out in the attached guidelines and that;
3. Advise that only banks which will have executed and exchanged Horizontal Repo MRAs and have formally confirmed as such to CBK will be allowed to participate in Horizontal Repo Transactions.

  
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