



Central Bank of Kenya

2020 Survey Report on MSME Access to Bank Credit

June 2021



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LIST OF ABBREVIATIONS

CBK	Central Bank of Kenya
CRBs	Credit Reference Bureaus
GDP	Gross Domestic Product
MFBs	Microfinance Banks
MRPs	Money Remittance Providers
MSEA	Micro and Small Enterprises Act (2012)
MSMEs	Micro, Small and Medium Enterprises
NPLs	Non Performing Loans

1. Background

Micro, Small and Medium Enterprises (MSMEs) play a significant economic role in creating employment and driving economic growth. The availability of adequate finance for investment and day-to-day business operations is a critical enabling factor for the long-term viability and growth of MSMEs.

With financial inclusion being a key part of CBK's strategic objectives, CBK endeavours to better understand both the demand and supply side factors that influence the availability and extent of formal financing accessible to market participants, including MSMEs. These efforts are aimed at identifying and addressing any impediments that might constrain access to formal financing by MSMEs.

The Central Bank of Kenya (CBK) conducted the 2020 FinAccess Business Supply-Side Survey on Bank Financing of MSMEs' ("The Survey") to determine the status of banking sector funding to MSMEs in Kenya as at December 31, 2020. The report provides findings on various indicators, including the definition of MSMEs, the amounts, pricing and tenors of credit disbursed, the primary credit products available to MSMEs and the sectoral distribution of MSME credit within the banking sector. The 2020 survey follows on from a previous MSME survey conducted in 2017 and aims at evaluating changes in access levels since the last survey. Coming in the wake of the coronavirus (COVID-19) pandemic, the 2020 survey also sought to evaluate the impact of the pandemic on MSMEs access to bank credit.

2. MSME Definition

The contribution of MSMEs to Kenya's GDP has grown increasingly over time from minimal to significant levels. As per the last Kenya National Bureau of Statistics MSME Survey conducted in year 2016, MSMEs were estimated to have contributed approximately 33.8 percent to national GDP in 2015¹. MSMEs are also a major provider of employment and livelihoods. In the five years to December 2019, MSMEs in the informal sector are estimated to have created more than half of total new job opportunities, especially in the low-income cadres. In 2019, approximately 768,000 new jobs of the 846,000 thousand created during the year were generated in MSMEs. These constituted approximately 90 percent of new jobs². MSMEs therefore play an important role in enhancing economic prosperity and social well-being

In defining MSMEs, the 2020 Survey differed from the 2017 Survey, which allowed respondent institutions to use their internal MSMEs classification criteria in completing the Survey. For definition purposes, the 2020 Survey adopted the definition of MSMEs set out under the Micro and Small Enterprises Act (2012) [MSEA Act 2012], and the Public Finance Management (Amendment) Act, (No. 2) of 2020. Under the MSEA Act, MSMEs are classified by either their annual turnover, the number of employees engaged or by their total financial investment.

¹ <https://www.knbs.or.ke/?wpdmpo=2016-msme-basic-report>

² <https://www.knbs.or.ke/?wpdmpo=economic-survey-2020>

The specific definitions for each category are as follows:

- **Micro enterprise** – any firm with an annual turnover not exceeding **Ksh.500,000** and employing (or rather engaging) **1-9 people**. The total assets and financial investment or the registered capital of the enterprise does not exceed **Ksh.10 million** in the manufacturing sector and does not exceed **Ksh.5 million** in the service and farming sector.
- **Small enterprises** – Any firm with an annual turnover of between **Ksh.500,000** and **Ksh.5 million** and engaging 10-49 employees. In the manufacturing sector, investment in plant and machinery should be between **Ksh.10 million**

and **Ksh.50 million** and registered capital of the enterprise between **Ksh.5 million** and **Ksh.25 million** in the service and farming sector.

- **Medium enterprises** – Any firm with an annual turnover of between Ksh.5 – 100 million and engaging between 50-250 employees; in the manufacturing sector, total assets and investment in plant and machinery or the registered capital of the enterprise does not exceed **Ksh.250 million**; in the service and agricultural sectors, investment in equipment or registered capital of the enterprise does not exceed **Ksh.125 million**.

Table 1 below presents the statutory definitions of MSMEs as used in the Survey.

Table 1: Statutory Definition of MSMEs

Category	Sector	Annual Turnover (Ksh)	No. of Employees	Assets/ Investment (Ksh)
Micro	All	≤ 500,000	<10	
Small	All	500,000<x<5,000,000	10<x<49	
Medium	Manufacturing	5,000,000<x<100,000,000	50<x<250	125,000,000
	Service / Farming	5,000,000<x<100,000,000	50<x<250	250,000,000
	Other	5,000,000<x<100,000,000	50<x<250	As determined by Cabinet Secretary

Source: Micro and Small Enterprises Act (2012)

3. Survey Respondents

The Survey sought information from all licensed commercial banks, mortgage finance institutions and microfinance banks. Data on the state of MSME financing as at December 2020 was received from 38 commercial banks, 1 mortgage finance company and 14 microfinance banks.

4. Overview of Findings

- As at December 2020, the Kenyan banking sector's total net assets stood at Ksh.5.4 trillion, with gross loans and advances accounting for Ksh.3.1 trillion. Total customer deposits were Ksh.4.1 trillion³.
- There were 915,115 active MSME loan accounts in the banking industry as at December 2020, with a total value of Ksh.638.3 billion; a 42 percent increase from 646,018 active loan accounts valued at Ksh.413.9 billion as at the last MSME lending survey in December 2017. Of this total, commercial banks and mortgage finance companies cumulatively disbursed Ksh.605 billion (95 percent) while microfinance banks disbursed Ksh.33.3 billion (5 percent).
- The active MSME loan accounts as at December 2020 constitute a 42 percent increase from 646,018 active accounts existing as at December 2017. The cumulative value of the MSME loan portfolio as at December 2020 (Ksh.638.3 billion) also rose by 54.2 percent from Ksh.413.9 billion reported in December 2017.
- The proportion of the MSME loan portfolio to the total banking sector loan book as at December 2020 stood at 20.9 percent compared to 19.2 percent as at the end of 2017.
- Lending to MSMEs generated Ksh.70.8 billion for the banking industry, representing 12.2 percent of the total income generated from lending by the banking industry. However, this was a proportionate drop from the Ksh.74.1 billion (or 15.2 percent) recorded in year 2017.
- On average, MSME borrowers took 30 months to repay loan facilities as at December 2020, compared to 2017 where the average loan tenor for MSMEs ranged from 15 to 40 months. Loans to micro enterprises had the shortest average repayment period at 18 months, with small and medium enterprise loans taking 30 and 41 months, respectively, to repay.
- The average interest rate on MSME loans ranged from 10 percent to 21 percent in 2020, with commercial banks and microfinance banks charging averages of 12 and 15.6 percent respectively. Average interest rates per institutional category were 16.6 percent for micro enterprises, 12.4 percent for small enterprises and 12.3 percent for medium enterprises.
- MSMEs continued to be a significant source of funding for the banking industry, accounting for 14 percent and 57 percent of total customer deposits held in commercial banks and microfinance banks, respectively.

³ 2020 Bank Supervision Annual Report,

https://www.centralbank.go.ke/uploads/banking_sector_annual_reports/468154612_2020%20Annual%20Report.pdf

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- Banks have designed various credit products targeting MSMEs. More than 60 percent of all commercial banks offer products targeting all the three categories of MSMEs, i.e. micro, small and medium-sized enterprises. 10 percent of commercial banks offer products targeting only enterprises in the medium category, while 8 percent offer products targeting enterprises in the small and medium categories. 60 percent of microfinance banks offer products targeting all three MSME categories, while 36 percent offer products targeting only micro and small enterprises.
 - In commercial banks, the largest credit allocation as at December 2020 was to MSMEs in the trade sector (34.2 percent), followed closely by real estate, and transport and communication sector at 22.2 percent and 10 percent, respectively. The agriculture and financial services sectors had the lowest allocation at 3.7 percent and 1.9 percent respectively.
 - In microfinance banks, the largest proportion of lending to the MSME loan portfolio was to the trade sector (45.4 percent), followed by the real estate and agricultural sectors at 13.7 percent and 12.6 percent, respectively. The energy and mining sectors had the lowest allocation at 0.5 percent and 0.2 percent, respectively.
 - In the view of the respondents, the COVID-19 crisis in 2020 had a significant impact on MSMEs' access to credit. 53 percent of commercial banks rated the pandemic's impact as high while 39 percent rated it as moderate. 51 percent of microfinance banks rated the impact as high while 46 percent rated it as moderate.
 - A total of 72,559 MSME loan facilities in the banking industry valued at Ksh.234.7 billion were restructured in 2020 as a measure to reduce the impact of the COVID-19 pandemic on MSME borrowers. These constituted 0.6 percent of total loan accounts and 7.8 percent of the total value of the gross loan portfolio as at December 2020. By comparison, in 2019, commercial and microfinance banks restructured a total of 4,348 loan facilities valued at Ksh.20.6 billion. These constituted approximately 0.05 percent of total loan accounts and 0.8 percent of the total value of the gross loan portfolio as at December 2019.
 - Of the 915,115 MSMEs loan accounts in the banking industry as at December 2020, 204,802 accounts valued at Ksh.98.7 billion were classified as non-performing. This amounted to 22.4 percent of total MSME loan accounts and 15.5 percent of the total value of outstanding MSME loans. Non-Performing Loans (NPLs) in MSMEs also made up 22.0 percent of total banking industry NPLs as at December 2020 which stood at approximately Ksh.436 billion. This is significantly higher than the NPLs for MSME loans in December 2017 which stood at Ksh.56.4 billion or 13.6 percent of the overall MSME loan portfolio of 413.9 billion.
 - In the 12 months to December 2020, a total of 6,253 MSME loans valued at Ksh.2.6 billion were written-off, with commercial banks and microfinance banks writing off Ksh.2.3 billion and Ksh.0.29 billion, respectively. The total accounts written off constitute 0.6 percent of total MSME loan accounts and 0.4 percent by value.
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5. Banking Sector Structure

As at December 31, 2020, the Kenyan banking sector comprised of the Central Bank of Kenya (CBK), as the primary regulatory authority, 39 banking institutions (38 commercial banks and 1 mortgage finance company), 14 Microfinance Banks (MFBs), 9 representative offices of foreign banks, 1 mortgage refinance company, 3 Credit Reference Bureaus (CRBs), 17 Money Remittance Providers (MRPs), 67 foreign exchange (forex) bureaus and 8 non-operating bank holding companies.⁴

As at December 31, 2020, the Kenyan banking sector had total net assets and total deposits of approximately 5.4 Trillion and Ksh.4.2 trillion respectively. Total loan accounts stood at 11.4 million while the total number of deposit accounts (in both commercial and microfinance banks) stood at 72.5 million. **Table 2** below gives a summary of the banking sector's asset and deposit base as at December 31, 2020.

Table 2: Banking Sector Asset Base as at December 2020

Total Net Assets	Gross Loans and Advances	Total Deposits	Total No. of Loan Accounts	Total No. of Deposit Accounts
Ksh. Trillion	Ksh. Trillion	Ksh. Trillion	Million	Million
5.4	3.1	4.1	11.4	72.5

Source: Central Bank of Kenya

6. MSME Loan Portfolio Performance as at December 2020

6.1 Size and Distribution

As at December 2020, there were 915,115 active MSME loan accounts in the banking sector valued at Ksh.638.3 billion. This was a 42 percent increase from 646,018 active loan accounts valued at Ksh.413.9 billion as at the last MSME lending survey in December 2017. Over the three-year period between 2017 and 2020, the number of MSME loan accounts and loan values grew at an annual average of 12 and 16 percent, respectively. The proportion

of MSME loan accounts to the overall banking sector loan accounts was relatively constant at 8.0 percent in 2020 and 8.3 percent in 2017.

Commercial banks and mortgage finance institutions held 67 percent of the total MSME's loan accounts in the banking sector as at December 2020 while microfinance banks held the remaining 33 percent.

On a collective basis, 83 percent of total loan accounts were held by micro enterprises, 12 percent by small enterprises and 5 percent by medium enterprises as depicted in **Figure 1(a)** below.

⁴ 2020 Bank Supervision Annual Report,

https://www.centralbank.go.ke/uploads/banking_sector_annual_reports/468154612_2020%20Annual%20Report.pdf

Of the 67 percent held in commercial banks, 54 percent were loans to micro enterprises, 8 percent to small enterprises and 5 percent to medium enterprises. Of the 33 percent held in microfinance banks, 29 percent were loans to micro enterprises and 4 percent to small enterprises. Loans to medium enterprises constituted approximately 0.3 percent of the loan portfolio in microfinance banks.

The proportion of MSME loans to the total banking sector loan portfolio as at December 2020 stood at 20.9 percent, a slight increase from 19.2 percent in December 2017.

The value of MSME loans by commercial banks and mortgage finance companies as at December 2020 amounted to Ksh.605 billion or 95 percent of the total MSME loan portfolio while loans held

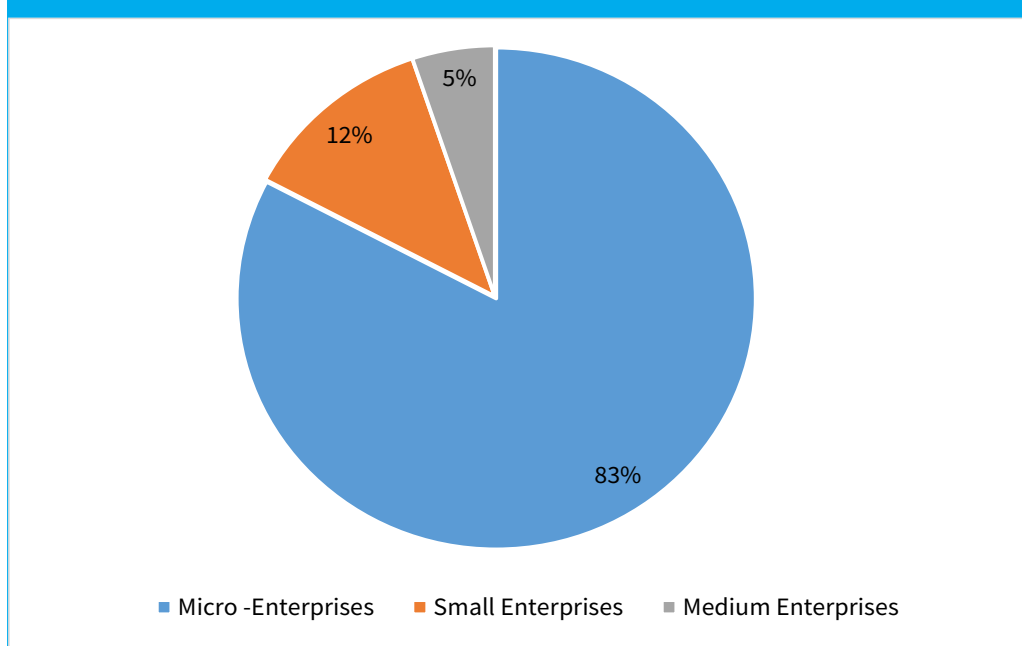
by microfinance banks stood at approximately Ksh.33.3 billion or 5 percent.

Of the Ksh.605 billion held in commercial banks, medium enterprises held the highest portion at Ksh.342.4 billion, small enterprises held approximately Ksh.221 billion while micro enterprises held the least amount at Ksh.42 billion as highlighted in **Figure 1(b)** below.

Of the Ksh.33.3 billion lent by microfinance banks, small enterprises held the highest amount at Ksh.13.8 billion, medium enterprises held Ksh.13.3 billion while micro enterprises held the least at Ksh.6.1 billion also highlighted in **Figure 1(b)** below.

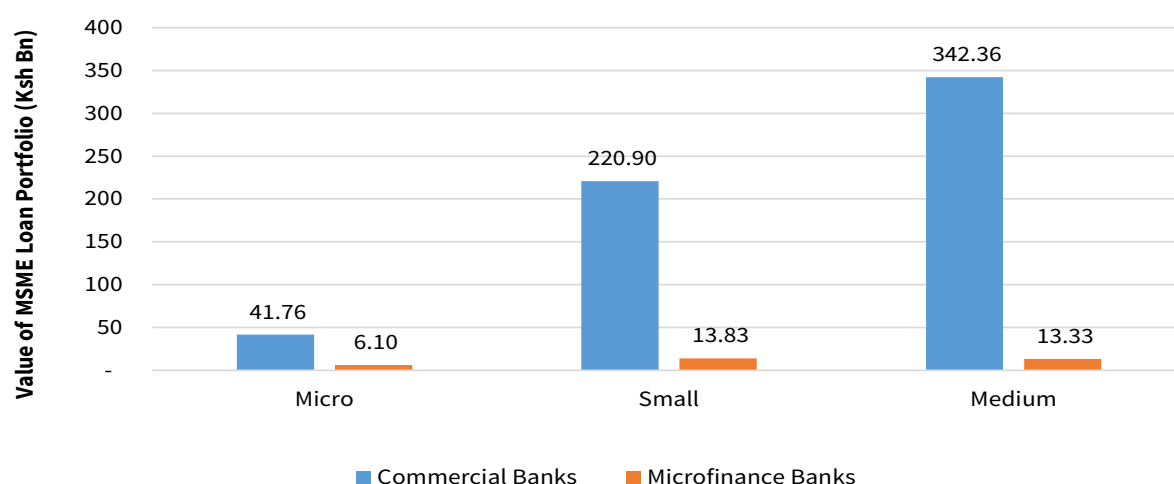
The above distribution is presented graphically in **Figures 1(a) and (b)** below.

Figure 1(a): Distribution of Banking Sector MSME Loan Accounts as at December 2020



Source: MSME Survey Data, 2020

Figure 1 (b): Distribution of the MSME Lending Portfolio by Value in December 2020



Source: MSME Survey Data, 2020

6.2 Average Loan Size

Overall, the average loan size across all categories as at December 2020 stood at approximately Ksh.697,500 compared to Ksh.1.16 million in the 2017 survey. Average loan sizes for specific enterprise categories were as follows:

- Loans from commercial banks as at December 2020 averaged Ksh.86,000, Ksh.2.9 million and Ksh.7.7 million for micro, small and medium enterprises respectively. This compares to Ksh.498,651 (micro), Ksh.3.2 million (small) and Ksh.14.4 million (medium) in 2017.
- Average loans from microfinance banks in 2020 stood at Ksh.23,000, Ksh.400,000 and Ksh.4.5 million for micro, small and medium enterprises respectively. This compares to Ksh.131,895 (micro), Ksh.1.25 million (small) and Ksh.4.2 million (medium) in 2017.

The reduction in the average loan size is largely attributable to a differential increase in the value of the loan portfolio as compared to the number of loan accounts. A possible contributing factor is the growth in mobile-based and digital credit disbursement channels between 2017 and 2020. These channels made it possible for institutions to extend low-value loans to a wider client base than was earlier the case with traditional service channels. As a result, the number of overall loan accounts rose at a higher rate than did the overall amounts borrowed, bringing down the average loan values across all MSME service categories.

A further contributing factor in 2020 is the subdued business environment that followed the outbreak of the COVID-19 pandemic. This resulted in reduced new borrowing and suppressed growth in lending, thereby bringing down the overall average loan sizes.

Table 3 below presents the comparative average loan sizes (in Ksh. million) for commercial banks and microfinance banks for the years 2017 and 2020.

Table 3: Average MSME Loan Sizes 2017 - 2020						
Category	Commercial Banks		Microfinance Banks		Overall	
	2020	2017	2020	2017	2020	2017
	(Ksh M)	(Ksh M)	(Ksh M)	(Ksh M)	(Ksh M)	(Ksh M)
Micro	0.086	0.5	0.02	0.13	0.06	0.13
Small	2.9	3.2	0.4	1.25	2.1	3.1
Medium	7.7	14.4	4.5	4.27	7.5	1.4
Overall	1	2	0.1	0.16	0.7	1.16
Source: MSME Survey Data, 2020						

6.3 Income Generated from the MSME Portfolio

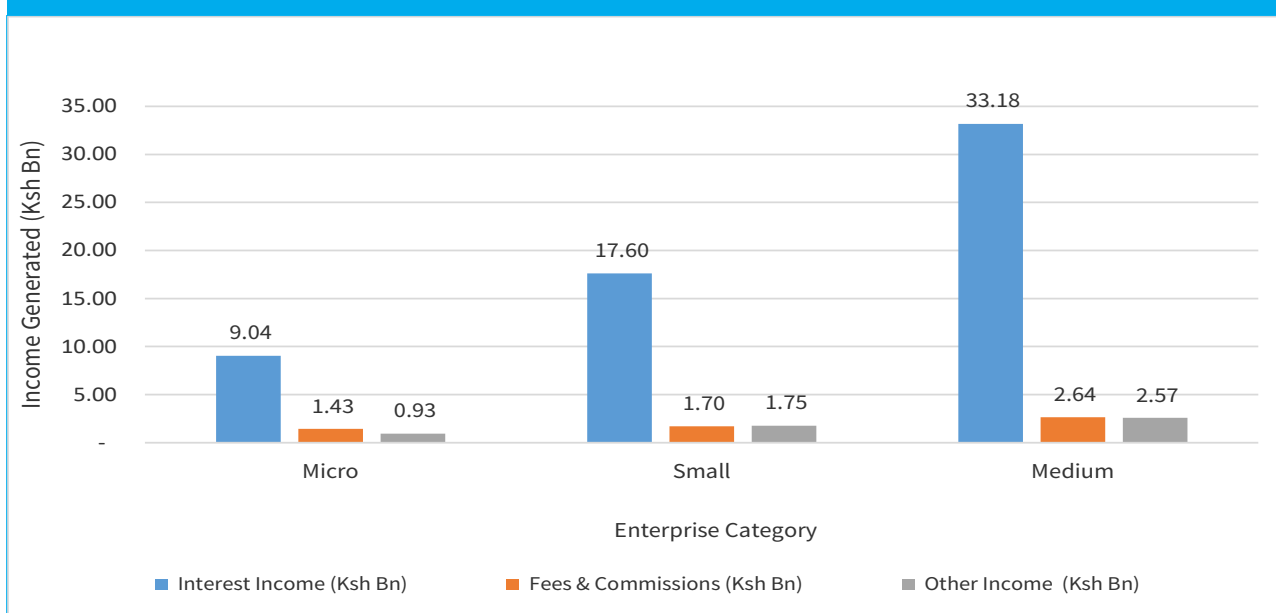
The banking sector generated approximately Ksh.70.8 billion in revenue in the 12 months to December 2020 from the MSME loan portfolio. This represented 12.2 percent of the banking sector's overall lending-related income for the year. Of this total revenue:

- Ksh.38.4 billion (54.2 percent) was generated from loans to medium enterprises. This comprised Ksh 33.2 billion in interest income, Ksh 2.6 billion in fees and commissions and Ksh.2.6 billion in other income.
- Ksh.21 billion (29.7 percent) was from loans to small enterprises. This comprised Ksh.17.6 billion in interest income, Ksh.1.7 billion in fees and commissions and Ksh 1.8 billion in other income.

- Ksh.11.4 billion (16 percent) was from loans to micro enterprises. This comprised Ksh 9 billion in interest income, Ksh 1.4 billion in fees and commissions and Ksh.0.9 billion in other income.

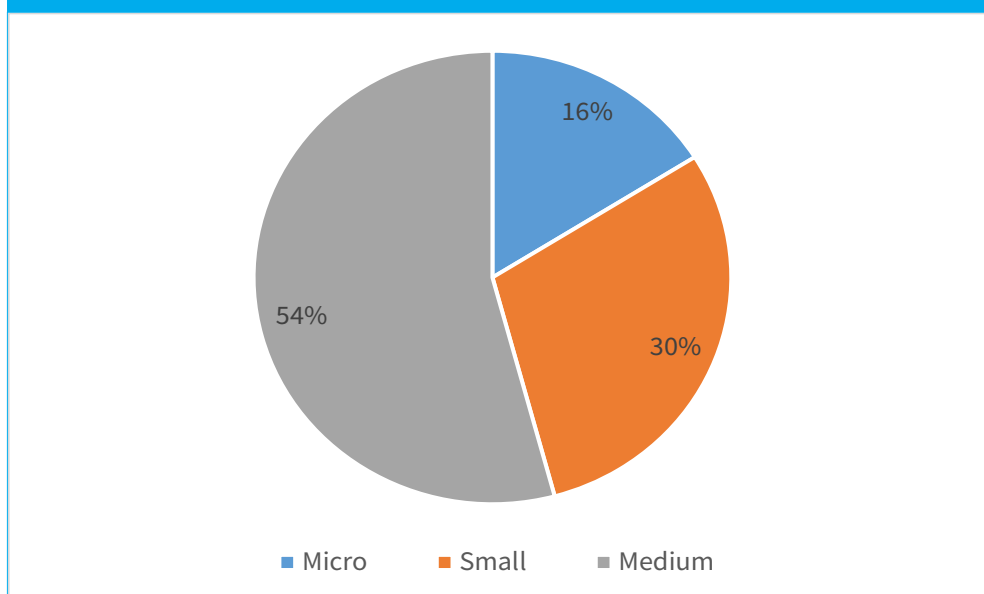
The overall revenue from MSME lending in 2020 declined by approximately 10 percent from the 2017 revenue of Ksh.74.1 billion. Overall income also declined as a proportion of the banking sector's overall lending-related income from 25.2 percent in 2017 to 12.2 percent in 2020. The decline is largely attributable to the slump in demand for MSMEs loans as a result of the economic slow-down in 2020 arising from the COVID-19 pandemic, which curtailed new borrowing and increased NPLs across many sectors. **Figures 2** and **3** below illustrate the above income distribution.

Figure 2: Income Generated on the MSME Loan Portfolio as at December 2020



Source: MSME Survey Data, 2020

Figure 3. MSME Income Distribution across Enterprise Categories in 2020

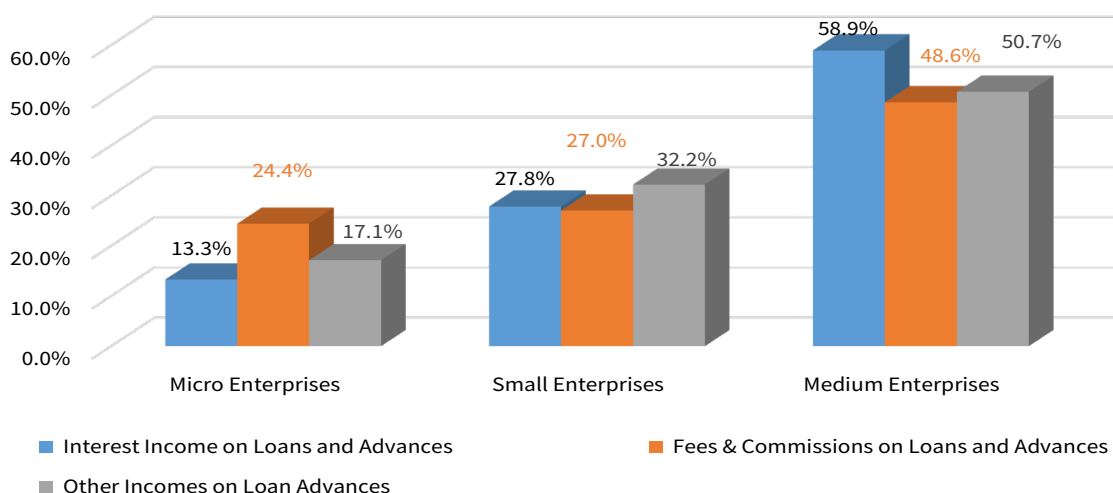


Source: MSME Survey Data, 2020

For commercial banks, the revenue contribution from micro enterprises in 2020 stood at 11 percent of overall revenue while small and medium-sized enterprises contributed 28 and 58 percent respectively. Loan interest formed the bulk of income from MSMEs at 84 percent of total income,

with fees and other income contributing 8 percent each. 59 percent of interest income was derived from medium-sized enterprises, 28 percent from small enterprises and 13 percent from microenterprises. A similar distribution pattern was also observed for fees and other interest income (see **Figure 4**).

Figure 4: Commercial Banks - MSMEs Income Distribution across Enterprise Categories in 2020

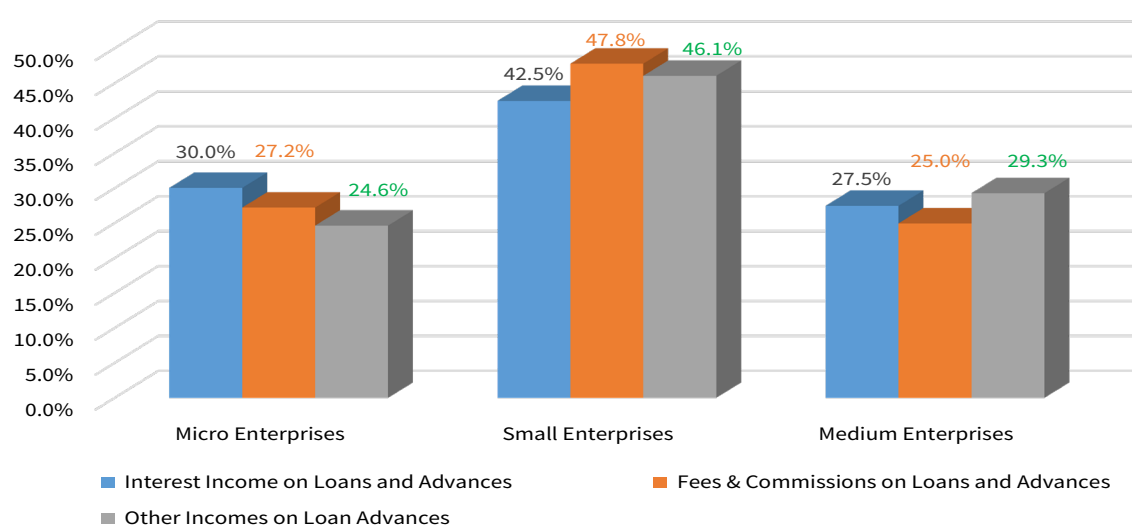


Source: MSME Survey Data, 2020

In microfinance banks, income from MSME lending in 2020 was composed of 86 percent in interest income, 9 percent in fees and commissions, and 5 percent in other income. Interest income was derived from medium-sized enterprises (30 percent), small enterprises (42 percent) and micro enterprises (28 percent). Fees and commissions

were derived from medium-sized enterprises (25 percent) small enterprises (48 percent) and microenterprises (27 percent). Other income was derived from medium enterprises (25 percent), small enterprises (46 percent) and micro enterprises (29 percent). The income structure for microfinance banks is presented in **Figure 5** below.

Figure 5: Microfinance Banks - MSMEs Income Distribution across Enterprise Categories in 2020



Source: MSME Survey Data, 2020

6.4 Loan Tenors

The average loan tenor for MSMEs across both commercial and microfinance banks stood at 30 months as at December 2020. In commercial banks, the tenor ranged from 18 months (for micro enterprises) to 40 months (for medium enterprises). In microfinance banks, the tenor ranged from 18 months for micro enterprises to 42 months for medium enterprises. This differed from the average loan tenure for MSMEs in 2017 which ranged from 15 to 40 months within commercial banks, and from 15 to 34 months within microfinance banks.

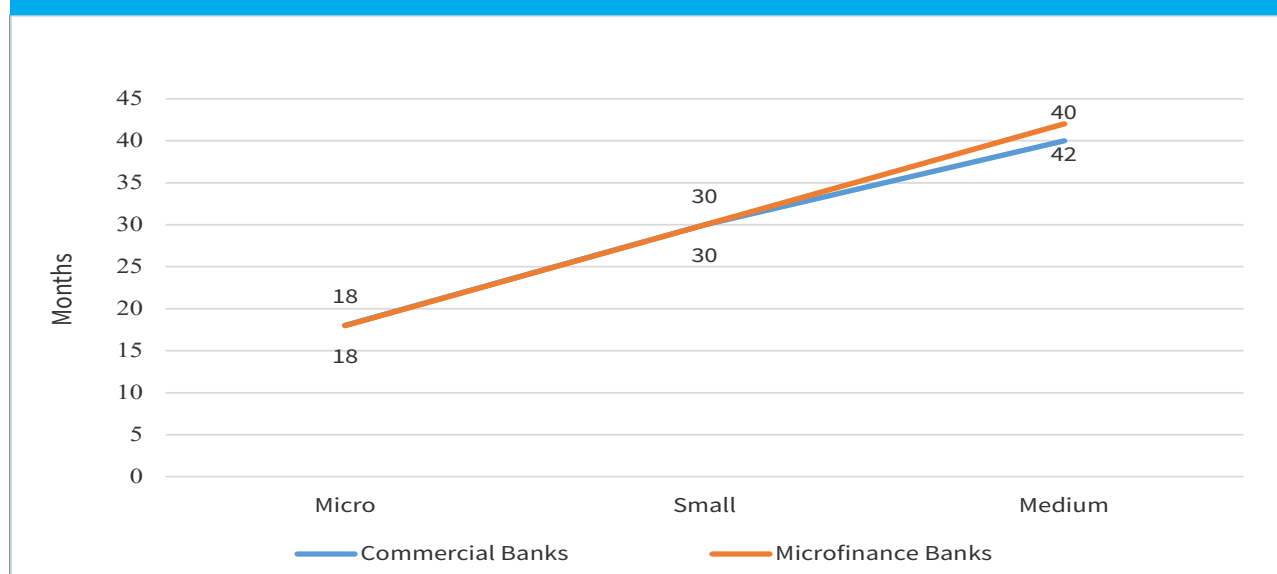
The repayment of loans by small and medium enterprises took on average 30 and 41 months respectively (**Table 4** and **Figure 6** below). The relatively shorter tenor of loans to micro enterprises as compared to small and medium enterprises is partially attributable to the lower amounts extended to micro enterprises as compared to the other two categories.

Table 4: Average Loan Tenors for MSME Loans as at December 2020 (Months)

Category	Micro	Small	Medium	Average
Commercial Banks	18	30	40	29
Microfinance Banks	18	30	42	30
Average	18	30	41	30

Source: MSME Survey Data, 2020

Figure 6: MSME Average Loan Tenor 2019 - 2020



Source: MSME Survey Data, 2020

6.5 Interest Rates on MSME Loans

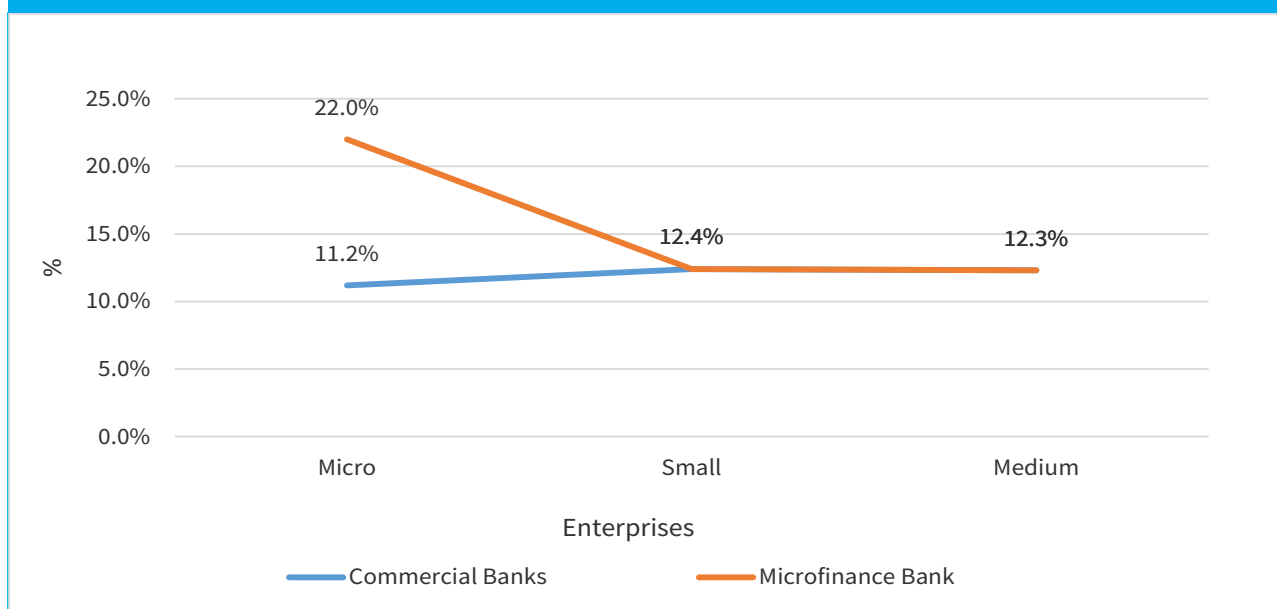
The average rate of interest charged on facilities to MSMEs as at December 2020 was 14 percent, and ranged from 21 percent for the highest-priced and 10 percent for the lowest priced facilities. Within specific categories, interest charges were as follows:

- Commercial banks charged between 11.2 and 12.3 percent on average, which are slightly higher compared to 2017 where it ranged from 10.0 percent to 12.1 percent. Medium enterprises paid the highest rates at 17.6 percent while small enterprises paid the lowest at 7.4 percent.

- Microfinance banks charged between 12.3 percent and 22 percent on average on MSME loans, compared to 2017 where it ranged from 19.0 percent to 19.9 percent. The highest reported rate was charged on micro enterprises at 33 percent and the lowest stood at 15 percent for medium sized enterprises.
- In general, the average range between the highest and lowest priced facilities stood at 10 percent.

Figure 7 below depicts the average interest rates charged on loans to each of the three MSME categories in year 2020 by both commercial and microfinance banks.

Figure 7: Average Interest Rates on MSME Facilities in 2020



Source: MSME Survey Data, 2020

6.6 Product Analysis

With a view to better serving the needs of MSMEs, banks have designed various products tailored to address the sector's specific needs. More than 60 percent of all commercial banks offer products targeting all the three categories of MSMEs, i.e. micro, small and medium-sized enterprises. 10 percent of commercial banks offer products targeting only enterprises in the medium category, while 8 percent offer products targeting enterprises in the small and medium categories. 60 percent of microfinance banks offer products targeting all three MSME categories, while 36 percent offer products targeting only micro and small enterprises.

Within commercial banks and microfinance banks, the typical term loans and bank overdrafts accounted for over 90 percent of the MSME loan portfolio as at December 2020. Other MSMEs products such as contract financing, performance bonds, bid bonds, invoice discounting, bank guarantees, letters of credit and warehouse receipts are also used but to a much lower extent, collectively accounting for the remaining 10 percent.

6.7 MSME Deposits

As at December 2020, there were a total of 5.82 million MSME deposit accounts held by financial

institutions, representing 8 percent of the 72.48 million deposit accounts within the banking sector. Commercial banks and mortgage finance companies held 74.8 percent of the MSME deposit accounts, while microfinance banks held the remaining 25.2 percent.

Deposits held by MSMEs as at December 2020 amounted to Ksh.577.6 billion or 14 percent of the total deposit liabilities (Ksh.4.01 trillion) in commercial banks. MSME deposits in microfinance banks amounted to Ksh.25.74 billion or 52.2 percent of overall deposits (Ksh.49.37 billion) held by microfinance banks as highlighted in **Table 5(a)** below.

Previously as at December 2017, MSME deposits accounted for 20.2 percent of total deposit liabilities for commercial banks and 70.7 percent of deposit liabilities in microfinance banks. The decline in the proportion of MSME deposits to overall deposits may be attributed to a proportionately larger increase in non-MSME deposits than in MSME deposits over the three-year period. **Tables 5 (a), (b)** below present the value of deposits held in both commercial banks and microfinance banks in December 2020 and December 2017 as a proportion of overall banking sector deposits.

Table 5(a): MSMEs Deposits Held in Commercial Banks

Year ending Dec	MSME Deposits	Total Customer Deposits	MSME Deposits/Total Customer Deposits (%)
	(KSh Billion)	(KSh Billion)	
2020	577.6	4,011	14.4
2017	585.8	2,899	20.2

Source: MSME Survey Data, 2020 and 2020 BSD Annual Report

Table 5(b): MSMEs Deposits Held in Microfinance Banks

Year ending Dec	MSME Deposits	Total Customer Deposits	MSME Deposits / Total Customer Deposits (%)
	(KSh Billion)	(KSh Billion)	
2020	25.7	49	52.2
2017	27.5	39	70.7

Source: MSME Survey Data, 2020 and 2020 BSD Annual Report

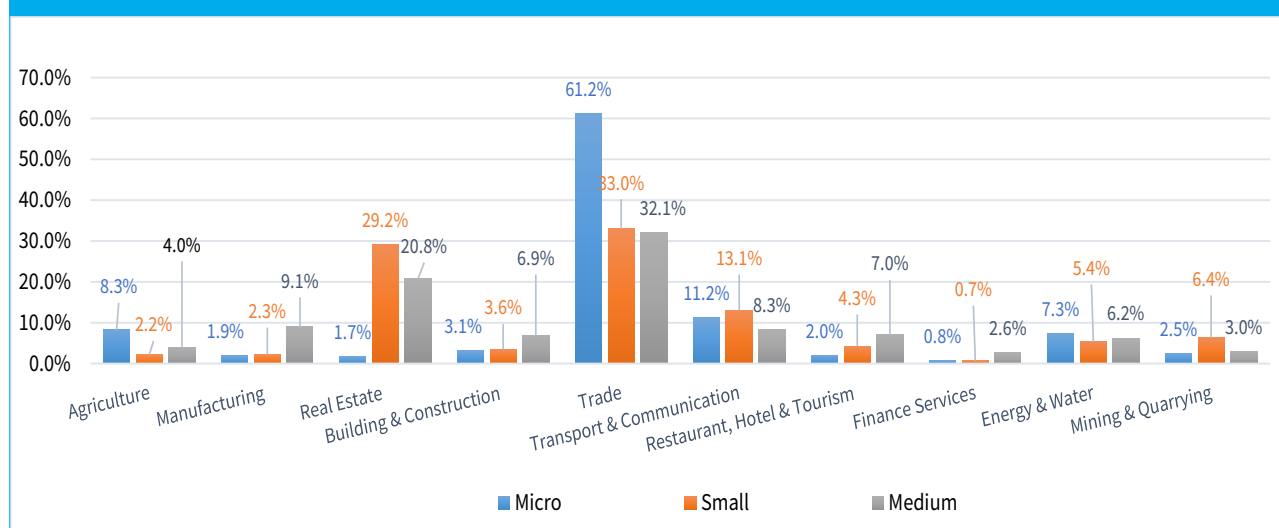
The above data indicates the significant role played by deposits from MSMEs as a source of funding for the banking sector, particularly for microfinance banks in which MSME deposits account for more than half the total customer deposits.

7. Sectoral Allocation of MSME Loans

As at December 2020, the largest proportion of MSME loans from commercial banks was extended

to the trade sector (34.2 percent), followed closely by real estate, and transport and communication sector at 22.2 percent and 10 percent, respectively. The agriculture and financial services sectors had the lowest allocation at 3.7 percent and 1.9 percent respectively.

The sectoral allocation of MSME loan portfolio in commercial banks is illustrated in **Figure 8** below.

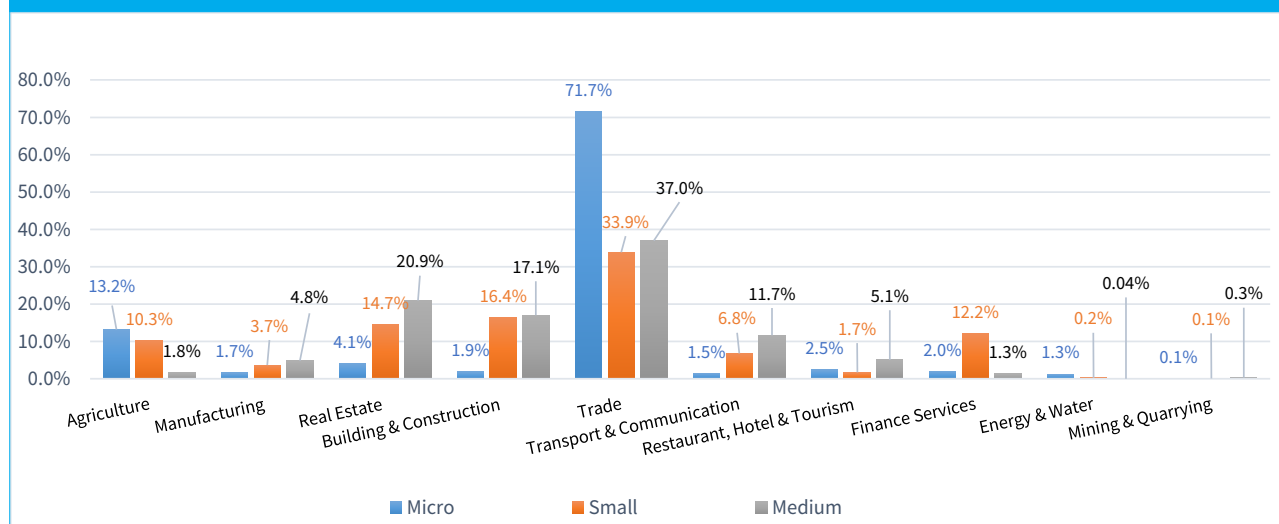
Figure 8: Sectoral allocation of MSME Loan Portfolio in Commercial Banks as at December 2020

Source: MSME Survey Data, 2020

In microfinance banks, the largest proportion of the MSME loan portfolio was extended to the trade sector (45.4 percent), followed distantly by real estate, building and agricultural sectors with 13.7 percent and 12.6 percent respectively. The energy

and mining sectors had the lowest allocation at 0.5 percent and 0.2 percent respectively. The sectoral allocation of MSME loan portfolio in microfinance banks is illustrated in **Figure 9** below.

Figure 9: Sectoral allocation of MSME Loan Portfolio in Microfinance Banks as at December 2020



Source: MSME Survey Data, 2020

8. Demand for Credit in the MSME Sector

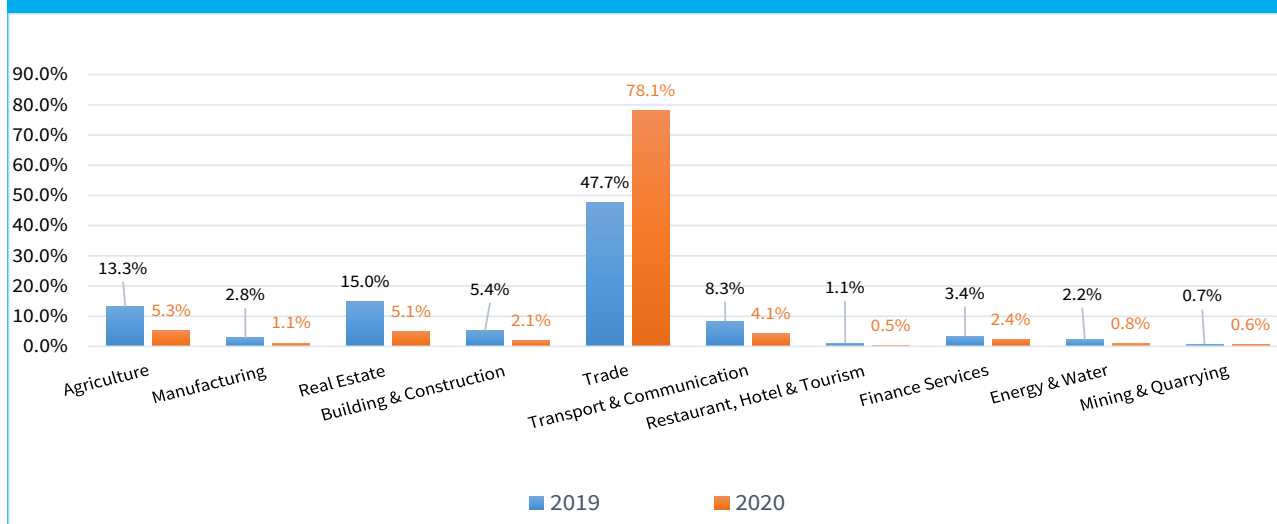
Within 2019 and 2020, commercial and microfinance banks received loan applications from MSMEs worth approximately Ksh.740 billion, of which Ksh.546 billion (74 percent) was approved.

Commercial banks received credit applications worth 688.4 billion in both 2019 and 2020, of which Ksh.496 billion (72 percent) were approved. In the micro enterprise category, the trade, agriculture and real estate sectors received the most credit from commercial banks while the hospitality,

energy and water, mining and quarrying sectors received the least. In the small enterprise category, the trade, real estate and transport sectors were the largest beneficiaries while the hospitality, energy and water, mining and quarrying sectors received the lowest proportion of credit.

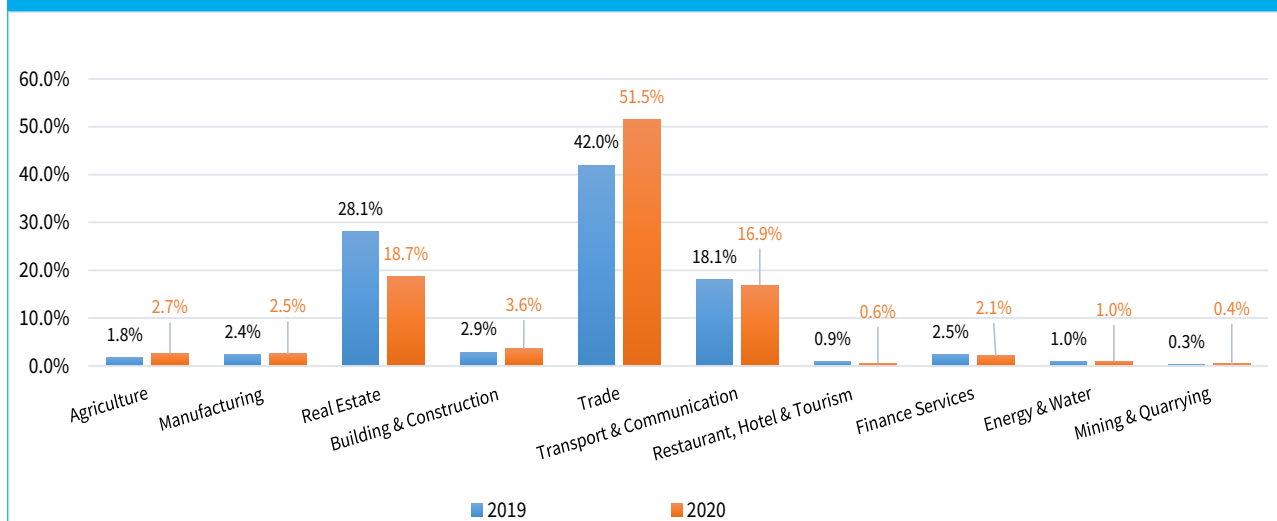
In the medium enterprise category, trade, real estate and transport sectors received the highest amount of credit from commercial banks while the hospitality, agriculture and mining sectors had the lowest approvals. **Figures 10 (a), (b) and (c)** present the sectoral distribution of loan approvals by commercial banks in 2019 and 2020.

Figure 10(a): Credit to Micro-enterprises to Total MSME Loan Portfolio in 2019-20 – Commercial Banks



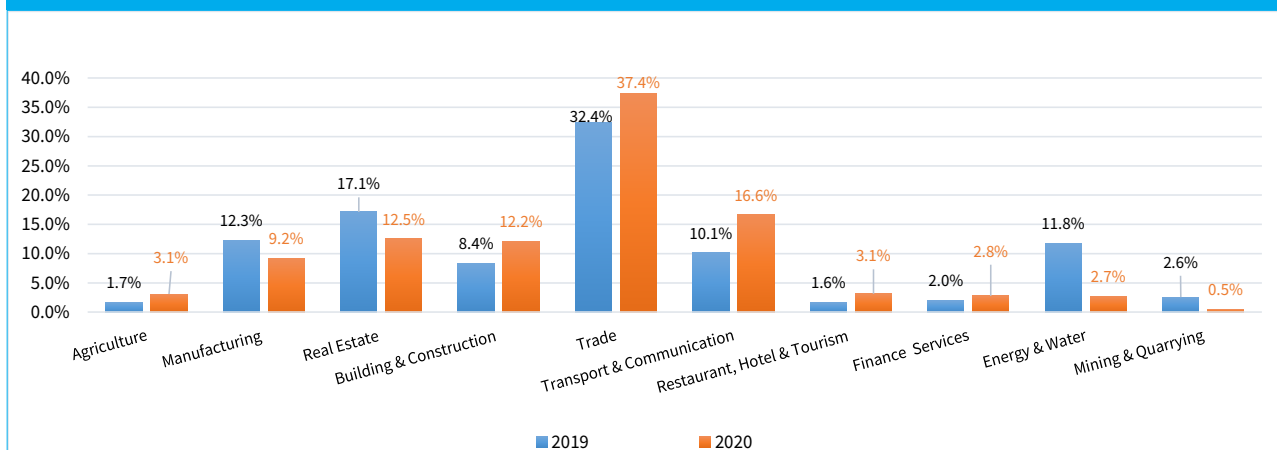
Source: MSME Survey Data, 2020

Figure 10(b): Credit to Small Enterprises to Total MSME Loan Portfolio in 2019-20 – Commercial Banks



Source: MSME Survey Data, 2020

Figure 10(c): Credit to Medium Enterprises to Total MSME Loan Portfolio in 2019-20 - Banks



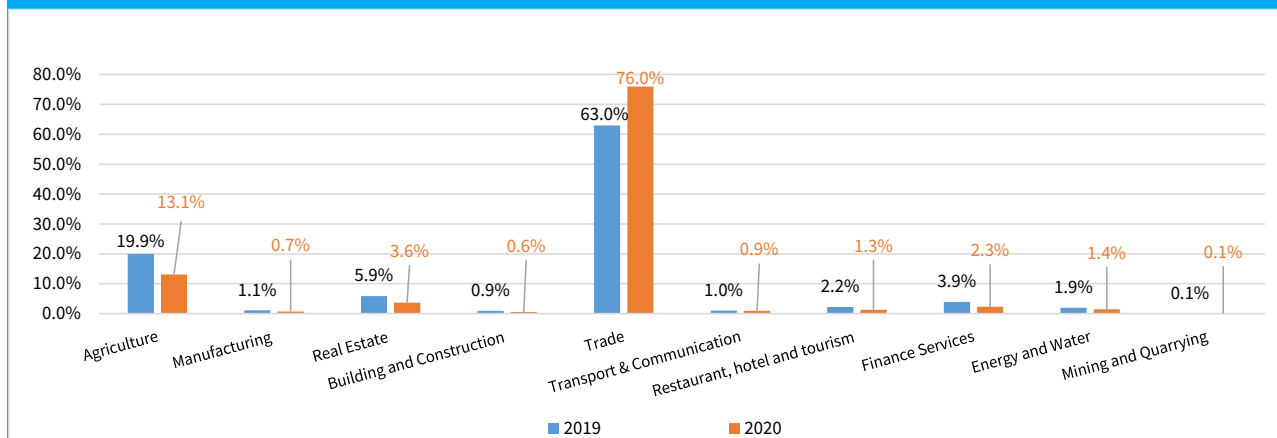
Source: MSME Survey Data, 2020

Microfinance banks received credit applications worth Ksh.50 billion in both 2019 and 2020, of which Ksh.2 billion (4 percent) were approved. In the micro enterprise category, the trade, and agriculture sectors received the most credit from microfinance banks while the energy and water, mining and quarrying sectors received the least. In the small enterprise category, the trade, agriculture, real estate and construction sectors were the largest beneficiaries while the while the energy and water,

mining and quarrying sectors received the lowest proportion of credit.

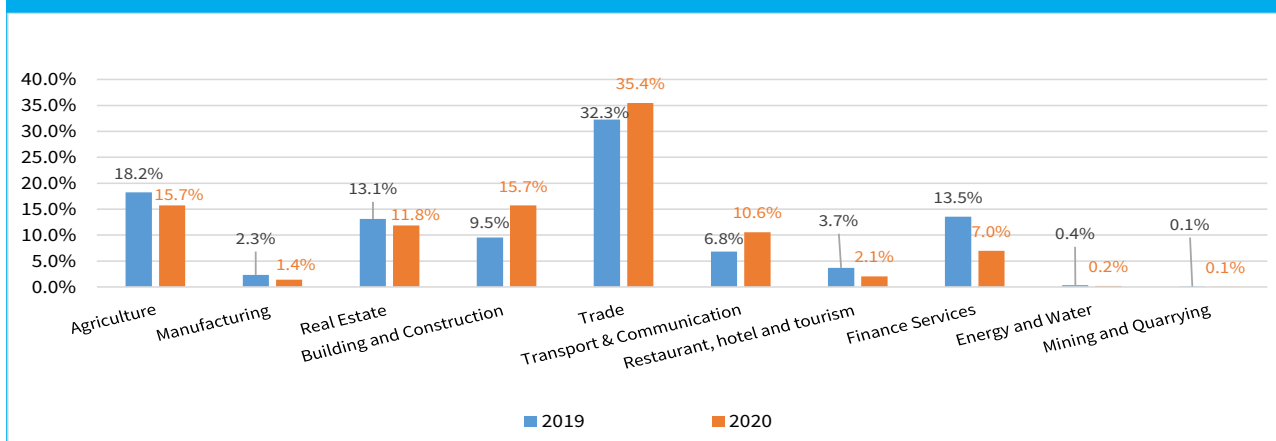
In the medium enterprise category, trade, real estate, construction and agriculture sectors received the highest amount of credit from microfinance banks while the hospitality, energy and water and mining sectors had the lowest allocation. **Figure 11 (a), (b) and (c)** below present the sectoral distribution of loan approvals by microfinance banks in 2019 and 2020.

Figure 11(a): Credit to Micro Enterprises to Total Loan Portfolio in 2019-20 - Microfinance Banks



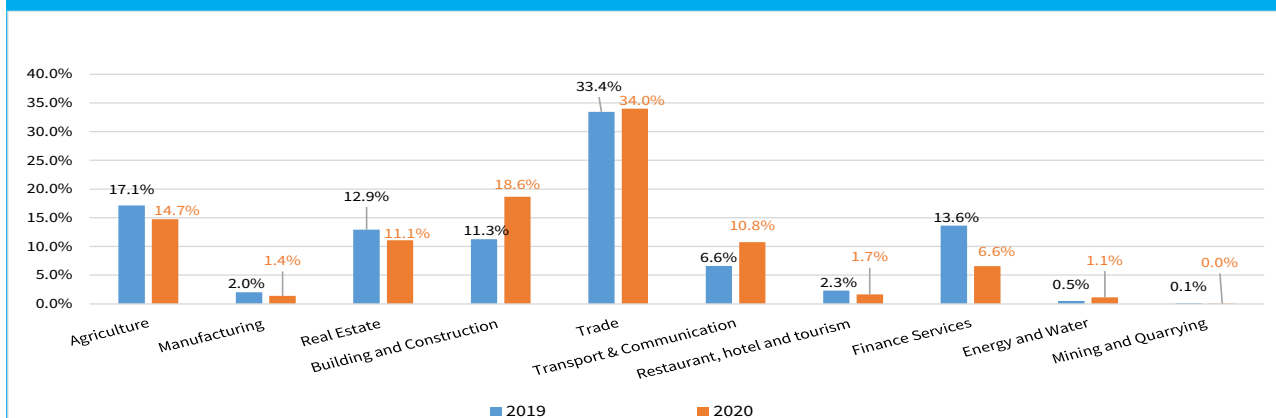
Source: MSME Survey Data, 2020

Figure 11(b): Credit to Small Enterprises to Total Loan Portfolio – Microfinance Banks



Source: MSME Survey Data, 2020

Figure 11(c): Credit to Medium Enterprises to Total Loan Portfolio – Microfinance Banks



Source: MSME Survey Data, 2020

9. COVID-19 Pandemic and Its Impact on the Banking Sector

The majority of respondent institutions indicated that the COVID-19 global pandemic had a significant impact on MSMEs' access to finance. Overall, 54 percent of commercial bank respondents rated the pandemic's impact as high, 40 percent as moderate, while 6 percent rated the impact as low. Similarly, 50 percent of respondent microfinance banks

rated the impact as high, 44 percent as moderate and 6 percent as low. According to the responses, the impact was even across all three sizes of enterprise – micro-, small and medium. The ratings point to the disruptive impact which the COVID-19 pandemic had on both financial institutions and on their customers' access to credit. A summary of respondents' ratings of the pandemic's impact on MSME's access to finance is presented in **Table 6** below.

Table 6: Impact of the COVID-19 Crisis on Enterprises' Access to Finance

Institution	Percentage of Respondents Indicating Rating			
	High	Moderate	Low	Total (%)
Commercial Banks	54	40	6	100
Microfinance Banks	50	44	6	100

Source: MSME Survey Data, 2020

9.1 Restructured MSME Loans and Non-Performing Loans (NPLs)

A total of 72,559 MSME loan facilities in the banking industry valued at Ksh.234.7 billion were restructured in 2020. These constituted 0.6 percent of total loan accounts and 7.8 percent of the total value of the gross loan portfolio as at December 2020. The restructuring was largely aimed at enabling borrowers to better manage their credit performance. In 2020, restructuring was largely prompted by the adverse impact of the COVID-19

pandemic and sought to cushion affected borrowers by easing debt servicing terms.

By comparison, in 2019, commercial and microfinance banks restructured a total of 4,348 loan facilities valued at Ksh.20.6 billion. These constituted approximately 0.05 percent of total loan accounts and 0.8 percent of the total value of the gross loan portfolio as at December 2019. **Table 7** below presents a summary of the total loan accounts and values thereof restructured in 2019 and 2020.

Table 7: Restructured Loans in 2019/20

	Number of Restructured Loans		Value of Restructured Loans	
	2019	2020	2019	2020
Commercial Banks			Ksh Bn	Ksh Bn
Micro Enterprises	2,067	45,262	1.43	10.66
Small Enterprises	955	17,732	3.37	66.03
Medium Enterprises	565	5,798	15.5	152.79
Total	3,587	68,792	20.31	229.48
Microfinance Banks				
Micro Enterprises	659	1,402	0.05	0.9
Small Enterprises	39	2,017	0.03	1.87
Medium Enterprises	31	348	0.2	2.46
Total - Microfinance Banks	761	3,767	0.27	5.24
Overall total	4,348	72,559	20.58	234.72

Source: MSME Survey Data, 2020

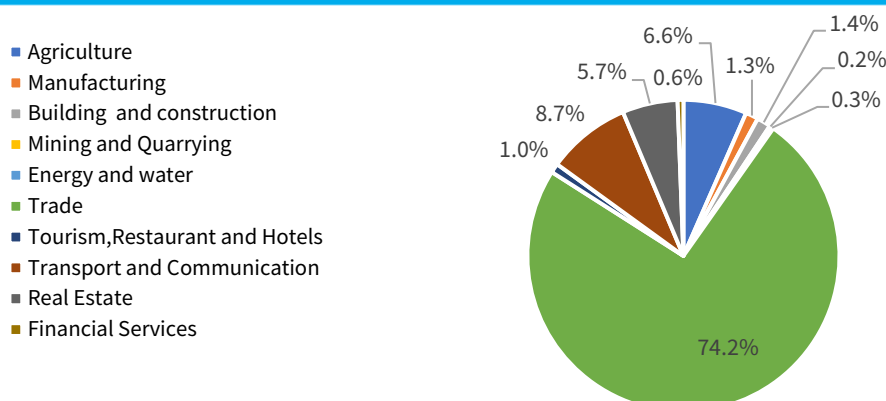
9.2 Restructured Loans (RLs) in 2019 and 2020

The trade sector had the largest share of restructured loans in 2020, accounting for 74.2 percent of the total, while the mining and quarrying sector had the lowest share with 0.2 percent. Others were the transport and communication sector (8.7 percent); agriculture sector (6.6 percent); real estate (5.7 percent). Other sectors had less than 1.5 percent each. In value terms, the real estate

sector accounted for 30.9 percent of restructured loans followed closely by the trade sector with 29.4 percent, transport and communication sector with 12.3 percent, while the rest of the sectors had less than 10 percent.

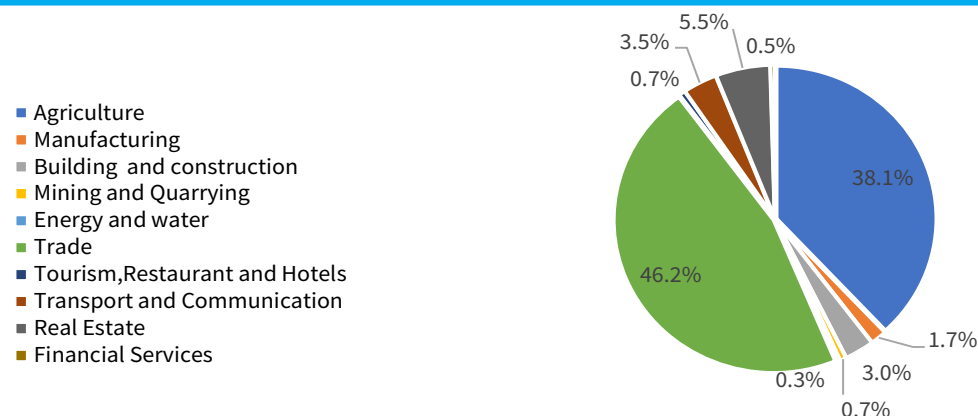
Figures 12(a), (b) and **13(a), (b)** below present a sectoral analysis of the numbers and values of restructured loans in both 2019 and 2020. **Figures 14 (a) and (b)** presents the numbers and values of the restructured facilities by sector for both years in percentage.

Figure 12(a): Number of Restructured Loans by Sector - 2020 - Commercial Banks



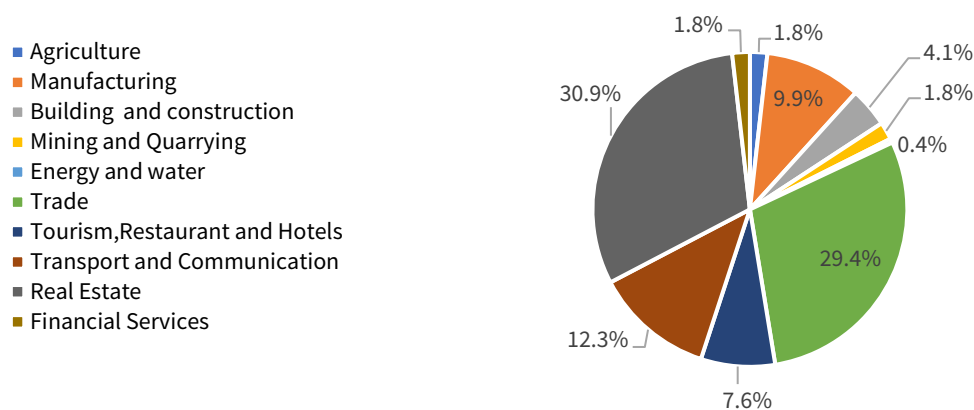
Source: MSME Survey Data, 2020

Figure 12(b): Number of Restructured Loans by Sector - 2019 - Commercial Banks



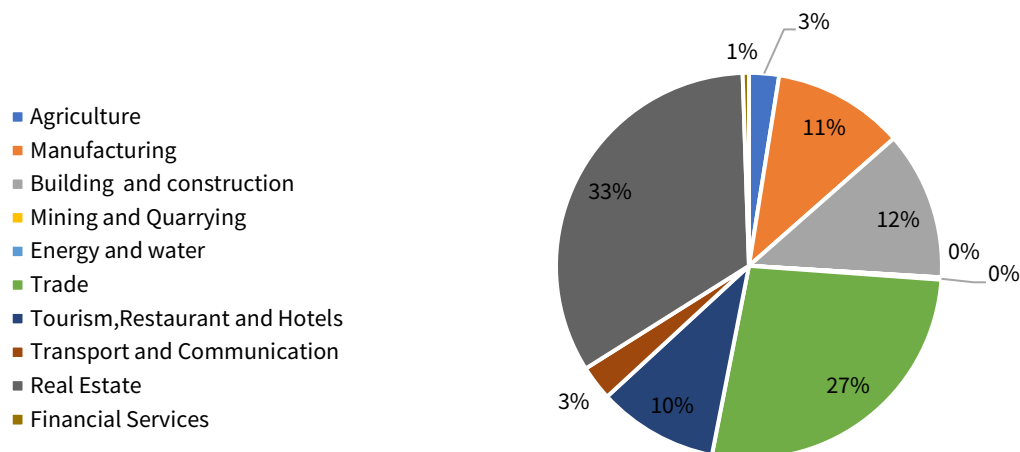
Source: MSME Survey Data, 2020

Figure 13 (a): Value of Restructured Loans by Sector - 2020 - Commercial Banks



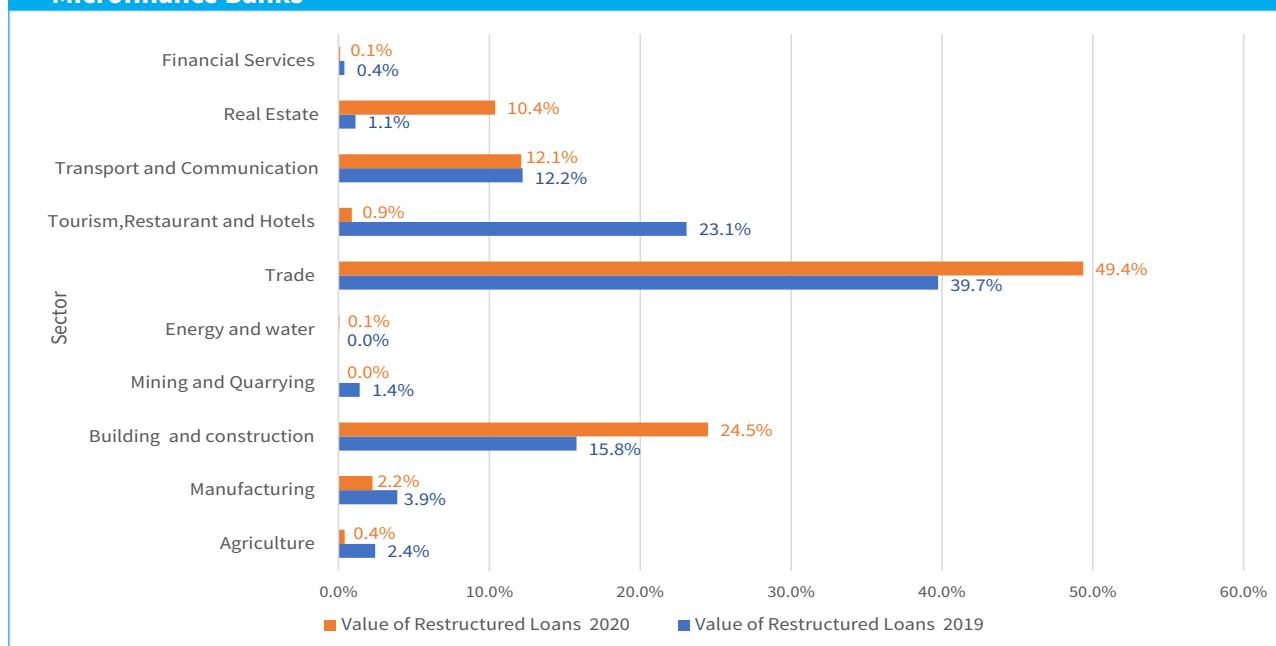
Source: MSME Survey Data, 2020

Figure 13(b): Value of Restructured Loans by Sector - 2019 - Commercial Banks



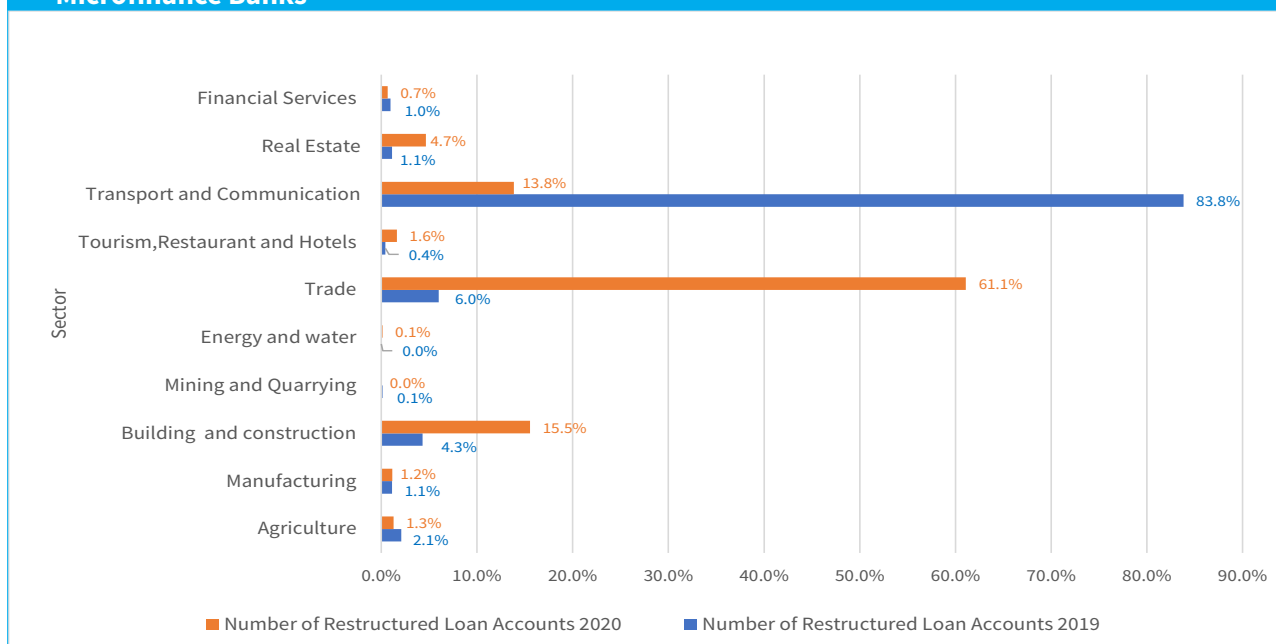
Source: MSME Survey Data, 2020

Figure 14 (a): Number of Restructured Loans by Sector in 2019 and 2020 (in Percentage) - Microfinance Banks



Source: MSME Survey Data, 2020

Figure 14 (b): Value of Restructured Loans by Sector in 2019 and 2020 (in Percentage) - Microfinance Banks



Source: MSME Survey Data, 2020

9.3 Performance of Restructured Loans as at December 2020

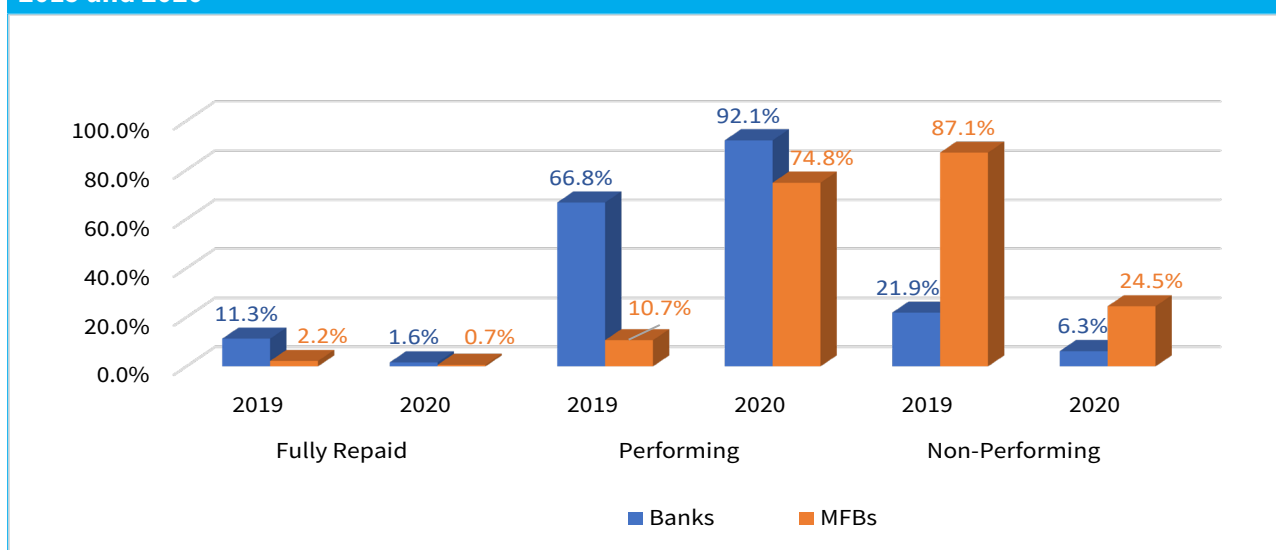
The Survey also sought to establish the performance, as at December 2020, of the loans restructured in 2019 and 2020. Data was sought on the number of restructured loans that were fully repaid as at December 2020, those performing, and those non-performing. Based on the findings, only 1.6 percent of restructured loans in commercial banks were fully repaid in 2020, compared to 11.3 percent in the previous year. Of the loans restructured in 2020, 92.1 percent were performing at the end of the year. For restructured loans that were non-performing, 6.3 percent remained non-performing in 2020 compared to 21.9 percent in 2019.

Microfinance banks had a similar experience; 0.7 percent of the restructured loans were fully repaid in 2020, compared to 2.2 percent that were fully repaid in 2019. 74.8 percent of the outstanding restructured loans were performing in 2020, significantly higher

than the 10.7 percent recorded in 2019. For the loans restructured in 2019 that were non-performing, 24.5 percent were non-performing in 2020 compared to 87.1 percent in 2019.

The high percentage of restructured loans in 2020 that were performing at the end of the year could largely be attributed to the impact of CBK's emergency measures announced in March 2020. In a bid to cushion borrowers from the adverse effects of the COVID-19 pandemic, CBK urged banks in March 2020 to work with borrowers to restructure deteriorating facilities that were performing at the beginning of the pandemic but whose performance was adversely affected by the negative effects of the pandemic. Subsequently, in 2020, 6.3 percent of restructured loans were non-performing compared to 21.9 percent in 2019, reflecting the impact of CBK's intervention. **Figure 15** below highlights the performance of the restructured facilities in both commercial banks and microfinance banks in 2019 and 2020 (in percentage).

Figure 15: Performance of restructured loans in commercial banks and microfinance banks- 2019 and 2020



Source: MSME Survey Data, 2020

9.4 Performance of Loans Restructured in 2019 and 2020 per enterprise category

In terms of the performance of restructured loans by the various businesses, both in 2019 and 2020, the highest percentage (12.4 percent and 1.7 percent, respectively) of restructured loans that were fully repaid was in medium-sized enterprises. However, in 2020, there was a decrease in the proportion of formerly restructured loans that were fully repaid.

This may be attributed to the subdued economic and business environment that resulted from the COVID-19 pandemic, causing debt servicing difficulties.

In 2019, restructured loans held by micro enterprises had the highest level of performance at 76.0 percent, while in 2020 small enterprises loans had the highest performance level of 94.3 percent. **Table 8 (a)** and **(b)** below present the breakdown of the performance by category of business enterprise.

Table 8(a): Performance of Loans Restructured in 2019-2020 - Banks

2019	Performance of RLs in Percentage - Banks		
	Fully Repaid (%)	Performing (%)	Non-Performing (%)
Micro Enterprises	9.8	76.0	14.2
Small Enterprises	6.9	68.3	24.8
Medium Enterprises	12.4	65.5	22.1
Overall	11.3	66.8	21.9
2020			
Micro Enterprises	1.5	90.6	7.9
Small Enterprises	1.6	94.3	4.1
Medium Enterprises	1.7	91.3	7.1
Overall	1.6	92.1	6.3

Source: MSME Survey Data, 2020

For microfinance banks, in 2020, most of the restructured loans by the various businesses were performing accounting for 74.8 percent, 24.5 percent were non-performing and 0.7 percent had

been fully paid. In terms of performance by the type of enterprise, the highest percentage (20.5 percent in 2019 and 1.8 percent in 2020) of restructured loans that were fully repaid was in micro enterprises.

Table 8(b): Performance of Loans Restructured in 2019-2020 – Microfinance Banks

2020	Performance of RLs in Percentage - MFBs		
	Fully Repaid (%)	Performing (%)	Non-Performing (%)
Micro Enterprises	1.8	95.9	2.3
Small Enterprises	1.4	91.5	7.1
Medium Enterprises	0.9	55.6	43.5
Overall	0.7	74.8	24.5
2019	Performance of RLs in Percentage - MFBs		
	Fully Repaid (%)	Performing (%)	Non-Performing (%)
Micro Enterprises	20.5	2.0	77.5
Small Enterprises	3.1	18.0	78.9
Medium Enterprises	1.3	10.4	88.4
Overall	2.2	11	87.1

Source: MSME Survey Data, 2020

9.5 Non-Performing Loans within the MSMEs Sector

Of the 915,115 MSMEs loan accounts in the banking industry as at December 2020, 204,802 accounts valued at Ksh.98.7 billion were classified as non-performing. This amounted to 22.4 percent of total MSME loan accounts and 15.5 percent of the total value of outstanding MSME loans. NPLs in MSMEs also made up 22.0 percent of total banking

industry NPLs as December 2020 which stood at approximately Ksh.436 billion. This significant proportion of NPLs points to the debt-servicing difficulties that MSMEs continue to grapple with partly due to the adverse effects of the COVID-19 pandemic. By comparison, the level of NPLs in MSMEs in December 2017 was relatively lower at Ksh.56.4 billion or 13.6 percent of the overall MSME loan portfolio of Ksh.413.9 billion as highlighted in

Table 9 below.

Table 9: MSME Credit Facilities – Asset Quality

Year ending Dec	No. of NPLs	Value of MSME NPLs	Total Value of MSME Loan Portfolio	Value of MSME NPLs / Total NPLs %
		(KSh. Billion)	(KSh Billion)	
2020	204,802	99.0	638.3	14.6
2017	101,424	56.4	413.9	13.6

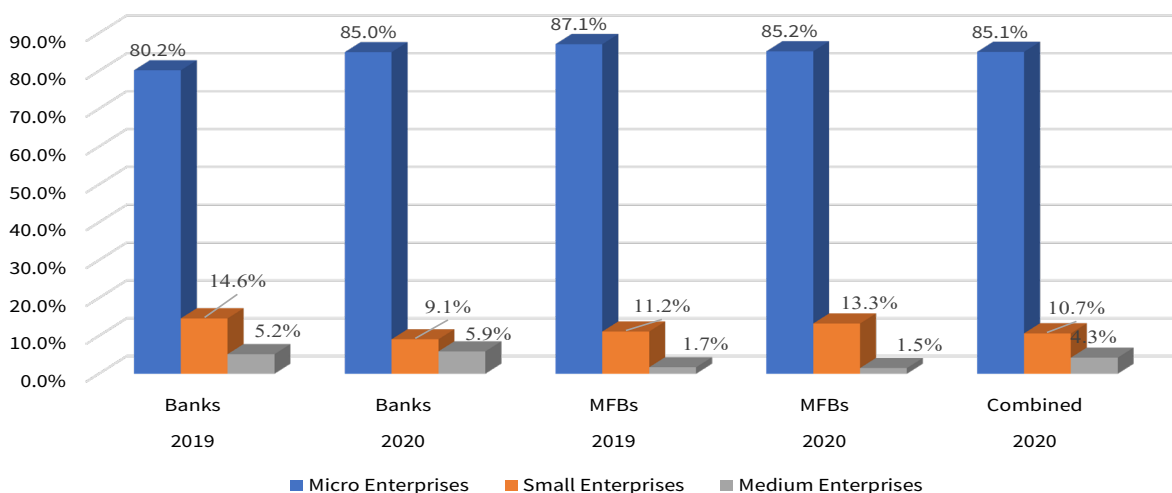
Source: MSME Survey Data, 2020

On the distribution of NPLs as at December 2020, micro enterprises accounted for 85.1 percent of the total non-performing loan accounts and 7.8 percent of the value of non-performing loans; small enterprises accounted for 10.7 percent of the total non-performing loan accounts and 24.1 percent of

the value of non-performing loans; while medium-sized enterprises accounted for 4.3 percent of the non-performing loan accounts and 68.0 percent of the value of non-performing loans for MSMEs.

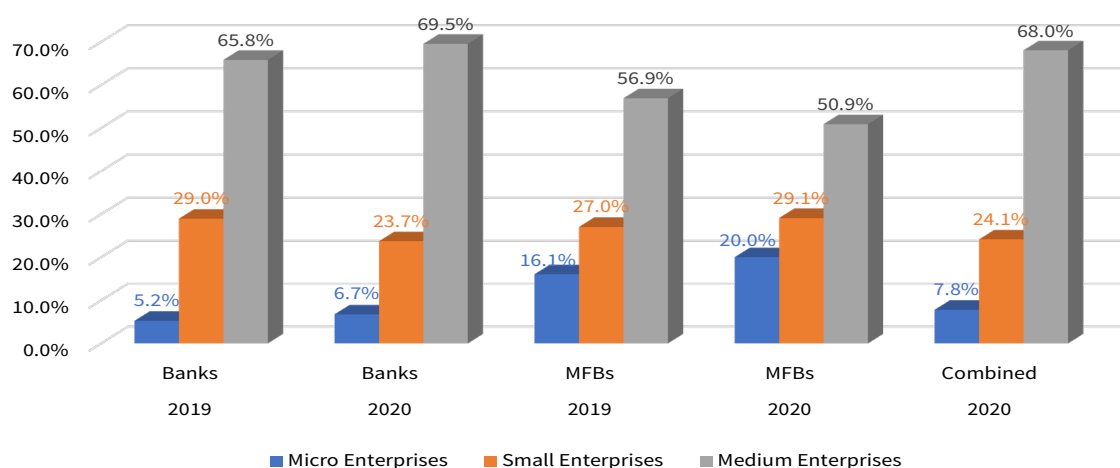
Figure 16 (a) and (b).

Figure 16(a): Number of Non-Performing Loans Accounts in 2019 - 2020



Source: MSME Survey Data, 2020

Figure 16 (b): Value of Non-Performing Loans in 2019 - 2020



Source: MSME Survey Data, 2020

9.6 MSME Loans written off in 2020

Owing to the generally subdued business environment resulting from the impact of COVID-19, a significant percentage of MSMEs borrowers either closed or significantly scaled down their business operations. As a result, non-performing loans that could not be restructured had to be written-off. The Survey data

indicates that, as at December 2020, a total of 6,253 loans valued at Ksh.2.6 billion were written-off, with commercial banks and microfinance banks writing off Ksh.2.3 billion and Ksh.0.29 billion, respectively.

Tables 10 (a) and **(b)** below present summaries of the numbers and values of NPLs written-off in 2020 by commercial banks and microfinance banks respectively.

Table 10(a): Non-performing Business Loans Written-off (In 2020) by Commercial Banks

	No. of Loans Written-Off	Value of Write-Offs (Ksh. Million)
Micro Enterprises	3,265	298
Small Enterprises	986	1,019
Medium Enterprises	1,523	983
Totals	5,774	2,300

Source: MSME Survey Data, 2020

Table 10 (b): Non-performing Business Loans Written-off (In 2020) by Microfinance Banks

	No. of Loans Written-Off	Value of Write-Offs (Ksh. Million)
Micro Enterprises	213	18
Small Enterprises	206	105
Medium Enterprises	60	171
Totals	479	294

Source: MSME Survey Data, 2020

9.7 Debt Recovery Costs in 2020

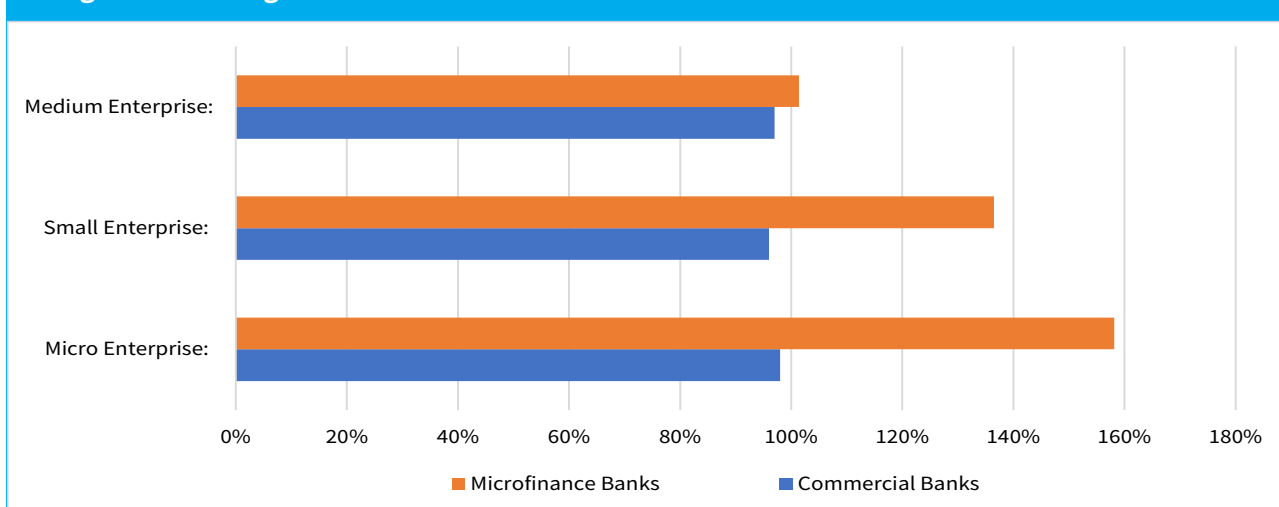
Once debt recovery measures were instituted to recover non-performing MSME loans, the average cost of recovery, as a percentage of the outstanding loan amount, stood at 6.3 percent for commercial banks and 12.9 percent for microfinance banks. In terms of the average recovery period for microfinance banks, NPLs in micro enterprises took the shortest duration to recover at 56 days compared to 91 days for small enterprises and 180 days for medium-sized enterprises. In commercial banks, the NPL recovery period averaged 215 days for micro enterprises, 270 days for small enterprises and 358 days for medium-sized enterprises. The relatively longer duration it took to recover NPLs from small and medium-sized enterprises is attributable to the relatively larger loan sizes held by borrowers in both categories compared to the average size of micro enterprise loans.

10. Collateral Requirements

Collateral requirements continue to be a major consideration for banks in extending credit to MSMEs in 2020 as was the case in 2017.

The responses indicate that lenders require MSMEs in all categories to avail collateral that is of sufficient value to fully or substantially cover the full value of the loan facility requested. **Figure 17** below presents the reported average values of collateral provided by MSMEs in both commercial and microfinance banks. Reported collateral values for commercial banks average slightly below 100 percent of loan amounts, while those for microfinance banks exceed 100 percent. This aligns with the findings of the 2017 report which established that MSMEs were expected to post collateral equivalent to more than 100 percent of the value of the loan facility irrespective of risk rating. In the 2020 findings, there appears to be less focus on alternative risk pricing mechanisms, such as internal ratings and credit scores, which could be used to gauge the debt repayment capacity of MSMEs.

Figure 17: Average Collateral Values for MSMEs Loans as at December 2020



Source: MSME Survey Data, 2020

11 Conclusion

The market for MSME financing is growing in Kenya and all commercial banks and microfinance banks seem keen to grow their engagement with MSMEs across all enterprise categories. The 42 percent increase in total active MSME loan accounts and 54.2 percent increase in the cumulative value of the MSME loan portfolio between 2017 and 2020 is a positive sign. However, this is countered by the increase in overall NPLs over the same period, particularly due to the COVID-19 global pandemic, as well as the uneven distribution in credit access across the MSME categories.

The Survey findings show that over 80 percent of the commercial banks and 100 percent of microfinance banks are at least offering one product for MSMEs clients. Such interest from the sector coupled with appropriately tailored products for MSMEs could improve the overall level of MSMEs financing significantly from current levels. The observations bring out the following key themes.

11.1 Product Diversity

The Survey shows the relatively narrow range of credit facilities utilized by MSMEs, centering largely on short-term term loans and overdrafts.

Within commercial banks, the term loans and bank overdrafts accounted for over 90 percent of the MSME loan portfolio. While these typical products can be useful to finance short-term needs of MSMEs such as working capital and modest growth, they are available mostly to well-established medium enterprises and exclude small and micro enterprises (start-ups) which may not be able to meet the terms and conditions of the said products. Owing to the high cost of these facilities, they are not appropriate for long-term business developmental needs and do not support growth.

The Survey established that the alternative financing instruments for MSMEs such as contract financing, performance bonds, invoice discounting, bank guarantees, letters of credit and warehouse receipts only accounted for 10 percent. Even though these products exist, they have had, until now, limited applicability to the MSME sector. Thus, there is need to broaden the finance options available and accessible to MSMEs to improve the MSMEs' capital structure and investment capacity, and reduce their reliance and vulnerability that tend to emanate from the typical loan products.

11.2 Performance of Restructured Loans

The Survey indicates that a significant proportion of the loans restructured in 2020 (over 90 percent in commercial banks and over 70 percent in microfinance banks) were performing in 2020. The high percentage of performing restructured loans could be partially attributed to the impact of the CBK's COVID-19 emergency measures announced in March 2020 that guided banks to work with borrowers to restructure deteriorating facilities that were performing at the onset of the pandemic.

11.3 Collateral Requirements

Banks have traditionally perceived MSMEs as risky borrowers due to the information asymmetry associated with them, their lower earnings and growth prospects compared to larger enterprises and lack of physical collateral. The Survey indicates that collateral requirements continue to be a major consideration for banks in extending credit to MSMEs, with lenders requiring MSMEs in all categories to post collateral that is of sufficient value to fully or substantially cover the full credit exposure. A majority of MSMEs do not possess the types of assets that are typically accepted by banks as collateral.

Collateral requirements therefore continue to be a major barrier for MSMEs in accessing formal credit. Ongoing reforms such as the strengthening of the moveable assets registry and appropriate security enforcement mechanisms would therefore go a long way in enhancing the bankability of MSMEs among lenders and easing MSMEs' access to credit.

A key limitation on the eligibility of many assets as collateral is the associated information asymmetry. Owing to the inability of many prospective lenders to ascertain with confidence the true ownership of many assets, both tangible and intangible, lenders are reluctant to accept many assets that could serve as collateral. In many instances, lenders may also lack the capacity to monitor use of the assets after credit is disbursed or ascertain completing claims on the said assets. Owing to the practical difficulties of recovery in the event of default, this informational constraint renders many types of assets ineligible as collateral and limits access to credit.

In this regard, data-driven innovations and algorithm-based financial technologies could be a possible solution in addressing this informational constraint. Artificial intelligence could be deployed to strengthen chattels registration, credit scoring, identification of security interests on assets and other informational techniques that could transform the credit underwriting process. For this to work, however, the integrity of credit databases and security registers, and their full visibility to lenders, are essential in enhancing lenders' confidence in information-based collateral creation and management systems.

This calls for concerted efforts between financial market participants and Government agencies towards the identification, deployment and maintenance of appropriate technologies that will promote the eligibility of a wider range of assets as loan collateral.

Annex

Commercial Banks and Mortgage Finance Companies⁵

- 1) Absa Bank Kenya Plc.
- 2) Access Bank Kenya Plc.
- 3) African Banking Corporation Limited.
- 4) Bank of Africa (K) Limited.
- 5) Bank of Baroda (K) Limited.
- 6) Bank of India.
- 7) Citibank N.A. Kenya.
- 8) Co - operative Bank of Kenya Limited.
- 9) Consolidated Bank of Kenya Limited.
- 10) Credit Bank Limited.
- 11) Development Bank of Kenya Limited.
- 12) Diamond Trust Bank (K) Limited.
- 13) DIB Bank Kenya Limited.
- 14) Ecobank Kenya Limited.
- 15) Equity Bank Kenya Limited.
- 16) Family Bank Limited.
- 17) First Community Bank Limited.
- 18) Guaranty Trust Bank Limited.
- 19) Guardian Bank Limited.
- 20) Gulf African Bank Limited.
- 21) Habib Bank A.G. Zurich.
- 22) HFC Limited.
- 23) I & M Bank Limited.
- 24) Kingdom Bank Limited.
- 25) KCB Bank Kenya Limited.
- 26) M - Oriental Bank Limited.
- 27) Mayfair CIB Bank Ltd.
- 28) Middle East Bank (K) Limited.
- 29) National Bank of Kenya Limited.
- 30) NCBA Bank Kenya Plc.
- 31) Paramount Bank Limited.
- 32) Prime Bank Limited.
- 33) SBM Bank (Kenya) Limited.
- 34) Sidian Bank Limited.
- 35) Spire Bank Limited.
- 36) Stanbic Bank Kenya Limited.
- 37) Standard Chartered Bank (K) Limited.
- 38) UBA Kenya Bank Limited.
- 39) Victoria Commercial Bank Limited.

b) Microfinance Banks

- 1) Caritas Microfinance Bank Limited.
- 2) Century Microfinance Bank Limited.
- 3) Choice Microfinance Bank Limited.
- 4) Daraja Microfinance Bank Limited.
- 5) Faulu Microfinance Bank Limited.
- 6) Kenya Women Microfinance Bank Plc.
- 7) Maisha Microfinance Bank Limited.
- 8) Muungano Microfinance Bank Limited.
- 9) Rafiki Microfinance Bank Limited.
- 10) Key Microfinance Bank Limited.
- 11) SMEP Microfinance Bank Limited.
- 12) Sumac Microfinance Bank Limited.
- 13) U&I Microfinance Bank Limited.
- 14) Uwezo Microfinance Bank Limited.

⁵Institutions that are either in receivership or liquidation were excluded from the Survey.



Central Bank of Kenya

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