Central Bank of Kenya

ANNUAL REPORT

AND FINANCIAL STATEMENTS

2020/2021

The Race for Your Future (detail)
Extelcoms House Murals

A depiction of Kenyan athletes in motion racing in a marathon and a young girl – late for school – almost matching their speed, giving context into why we run.

The murals painted on Extelcoms House are the largest in East and Central Africa, and the fourth largest in Africa. They are 2,280m^2 and cover all four sides of the base of the building. Painted in bright colours, the murals tell the story of a Nation and its dreams for a future. The story starts with a little girl running to school, reminiscent of the Tom and Mary primary text books of old, chasing her dreams the only way she knows how. Ahead of her is a depiction of Kenyan athletes; a band of men and women who have always brought this country – not just a sense of pride – but also an identity on the global stage.

The murals were painted by Viktart: viktart@deepseastudios.com, and his team of 8 artists from DeepSea Studios working an 11-hour day for 8 weeks.

LETTER OF TRANSMITTAL

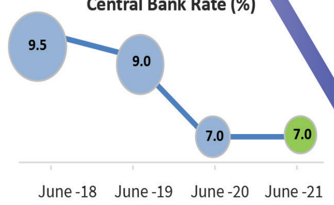
In accordance with Section 54 of the Central Bank of Kenya Act, it is my honour to present to you, Honourable Cabinet Secretary of the National Treasury and Planning, the Annual Report of the Central Bank of Kenya for the Financial Year 2020/21. The Annual Report contains economic and financial developments and the financial performance of the Central Bank of Kenya for the Financial Year ended June 30, 2021.

Patrick Njoroge

Dr Patrick Njoroge
Governor

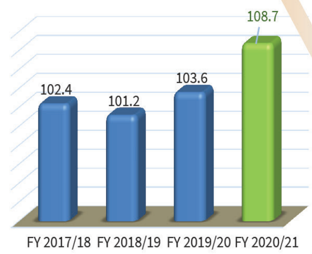
HIGHLIGHTS

Central Bank Rate (%)



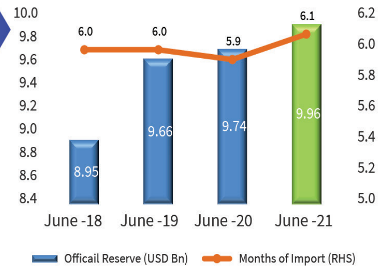
An accommodative monetary stance was maintained to support the economy without comprising the price stability objective.

Average Exchange Rate (KSh/US$)



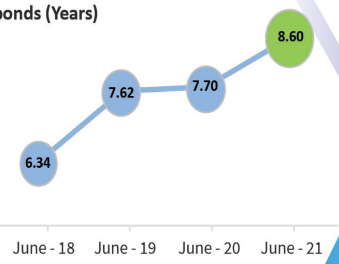
The exchange rate weakened in line with global developments.

Official Foreign Exchange Reserves



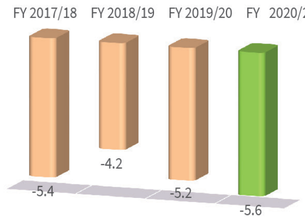
The official forex reserves remain adequate and above the statutory requirements.

Average Time to Maturity for bonds (Years)



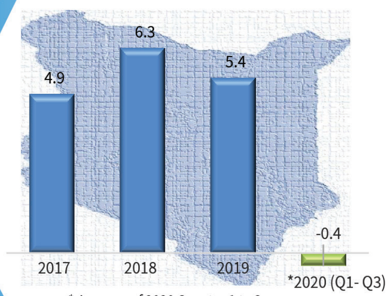
The average time to maturity for bonds has continued to increase.

Current A/C Deficit (% of GDP)



The current account balance remained relatively stable.

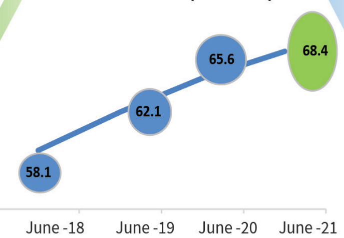
Real GDP Growth (%)



** Average of 2020 Quarter 1 to 3*

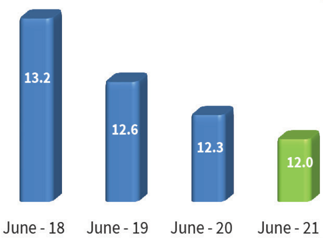
The economy remained resilient.

Public Debt (% of GDP)



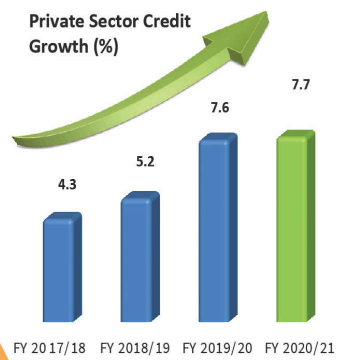
Public debt increased reflecting COVID-19 recovery measures.

Average Lending Rate (%)



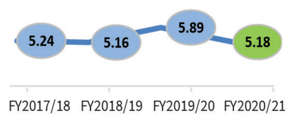
The lending rate declined thereby supporting access to affordable credit.

Private Sector Credit Growth (%)



Credit to the private sector remained resilient.

Average Inflation Rate



Inflation remained within the midpoint of target band.

OUR VISION

The Vision of the Bank is to be a World Class Modern Central Bank.

OUR MISSION

To formulate and implement monetary policy for price stability, foster a stable market-based financial system and ensure sound national payment system.

MANDATES

Article 231 of the Constitution of Kenya and Sections 4 and 4A of the Central Bank of Kenya (CBK) Act outline the key mandate of Central Bank of Kenya (CBK) as to:

i) Formulate and implement Monetary Policy directed to achieving and maintaining stability in the general level of prices.
ii) Foster the liquidity, solvency and proper functioning, efficient, sound and stable market-based financial system.
iii) Formulate and implement such policies as best to promote the establishment, regulation and supervision of efficient and effective payment, clearing and settlement systems.
iv) Design, issue and manage efficient distribution of quality currency (notes and coins) that are easily accepted and secure against counterfeiting.
v) Support the Government's economic and financial policies including its objectives for growth and employment.

The other mandates of the Bank include:- formulating and implementing foreign exchange policy; effective management of the nation's foreign exchange reserves; licensing and supervising authorised dealers; act as banker and adviser to, and fiscal agent of the Government.

Commitment

The Board, Management and staff are committed to implementing the Bank's mandate as stipulated in the Constituion of Kenya and the CBK Act.

Efficiency & Effectiveness

The Bank will at all times undertake its operations in the most cost efficient and effective manner while maintaining high standards of performance in execution of its mandate.

Transparency, Accountability and Integrity

The Board, Management and staff will always act in a transparent and accountable manner when handling all the affairs of the Bank both internally and with external parties so as to uphold the Bank's image at all times. In addition, the Bank will uphold high standards of ethics, integrity and honesty as guided by the Constitution, act in an ethical manner as guided by the Leadership and Integrity Act and Public Officers' Ethics Act, and observe high moral standards.

Diversity and Inclusiveness

The Bank appreciates and embraces the differences in its employees' skill set and abilities and encourages consultations and inclusiveness in pursuit of its mandate across departments. This is aimed at maximising productivity and enhancing the Bank's overall performances.

Professionalism and Relevance

The Board, Management and staff will always endeavour to offer quality services to its internal and external stakeholders, diligently observing high professional standards at all times and respecting the rules and regulations set by the Bank. All initiatives and activities undertaken remain relevant to the Bank's strategic objectives in pursuit of its core mandate.

Innovativeness

The Bank will encourage, nurture and support creativity and the development of new ideas and processes for the continued improvement of organisational performance.

Mutual Respect and Team Work

Mutual respect shall at all times be observed internally amongst colleagues and when dealing with the Bank's external clients. In addition, the Board and staff will cooperate and collaborate to enhance performance and create a healthy work environment.

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ABBREVIATIONS AND ACRONYMS

AACB	Association of African Central Banks
AMCP	African Monetary Cooperation Programme
CBK	Central Bank of Kenya
COMESA	Common Market for Eastern and Southern Africa
COVID-19	Corona Virus Disease 2019
CRBs	Credit Reference Bureaus
CRR	Cash Reserves Requirement
EAC	East African Community
EAMU	East African Monetary Union
EAPSS	East Africa Payments System
EDW	Enterprise Data Warehouse
EMDEs	Emerging Markets & Developing Economies
FY	Financial Year
GDP	Gross Domestic Product
IMF	International Monetary Fund
KEPSS	Kenya Electronic Payments and Settlement System
KNBS	Kenya National Bureau of Statistics
KSh	Kenya Shillings
MFBs	Microfinance Banks
MNOs	Mobile Network Operators
MPC	Monetary Policy Committee
MSME	Micro, Small and Medium Enterprise
NDA	Net Domestic Assets
NFA	Net Foreign Assets
NFNF	None-Food-None-Fuel
NPL	Non-Performing Loan
OPEC	Organisation of the Petroleum Exporting Countries
PSPs	Payment Service Providers
REPSS	Regional Payment and Settlement System
RTGS	Real Time Gross Settlement
SSA	Sub-Saharan Africa
TRWA	Total Risk Weighted Assets
USD	United States Dollars
VAT	Value Added Tax
WEO	World Economic Outlook

FOREWORD BY THE GOVERNOR

I am pleased to present the Central Bank of Kenya's (CBK) Annual Report for the Financial Year 2020/21. The financial year began against a backdrop of the global coronavirus (COVID-19) pandemic and measures taken by authorities across the world to mitigate the adverse demand and supply-side effects of the pandemic. Critical productive and social sectors of the economy particularly health and education were significantly affected. The COVID-19 pandemic revealed the great resilience of the Kenyan spirit in adversity. The Kenyan economy continues to recover from the effects of the pandemic, supported by policy measures implemented by the Government to mitigate the adverse economic and financial effects of the pandemic, and gradual reopening of the economy and easing of COVID-19 restrictions. Similarly, the pace of global economic recovery has continued to strengthen, largely supported by relaxation of COVID-19 restrictions particularly in the major economies, and the ongoing deployment of vaccines.

The CBK continued to fulfil its core mandates of maintaining price stability and ensuring a stable market-based financial system during the financial year. The Monetary Policy Committee (MPC) maintained an accommodative monetary policy stance with the objective of supporting economic recovery and moderating the adverse effects of COVID-19 on Kenyans, and ensured that the banking system remained liquid and continued to function smoothly. The accommodative policy stance also supported banks' lending to the private sector. Inflation remained well anchored within the target range during the financial year.

The banking sector witnessed continued stability and resilience during the financial year, with strong liquidity and capital adequacy ratios. At the onset of the COVID-19 pandemic in March 2020, CBK and MPC rolled out a number of emergency measures to mitigate the anticipated adverse effects of the pandemic. These measures provided liquidity to the banking sector, mitigated the adverse impact of the pandemic on bank borrowers, and facilitated the use of mobile money. The measures ensured continued provision of financial services and provided a buffer against a more adverse impact on the economy. CBK monitored closely the implementation of these measures throughout the year. At the close of the 2020/21 financial year, there was considerable hope regarding recovery from the pandemic.

Looking ahead, CBK will roll out a new strategic plan to guide its activities in the next three years. At the core of the strategic plan is the maintenance of a low and stable inflation nested, on continued coordination of monetary and fiscal policies to sustain macroeconomic stability and revamp the economy in the post Covid-19 period.

Dr. Patrick Njoroge
Governor

STATEMENT BY THE CHAIRMAN OF THE BOARD

The Central Bank of Kenya successfully implemented its Strategic Plan 2018/2021 despite the severity of the COVID-19 pandemic. I am pleased to observe that the Bank took various containment measures to support the economy, the banking sector and ensure safety of its staff. I observe the relative success of the measures undertaken at a very difficult time. I commend the staff of the Central Bank for their resilience during a very trying period.

The FY2020/2021 marked the final phase in implementation of the CBK's Strategic Plan for 2018-2021, aligning the Bank on the theme ***"Leveraging Innovative Technologies and Systems"*** to drive the vision of becoming a ***Modern World Class Central Bank.***

Among the milestones during the year included:

- Significant progress in the implementation of an Enterprise Data Warehouse (EDW) to facilitate near-real time data capture and analysis.
- Completed recruitment process of Directors and Assistant Directors in most departments.
- Rolled out improved human resource frameworks including the human resource realignment process, new learning and development framework.
- On September 18, 2020, CBK announced the licensing of the Kenya Mortgage Refinance Company Plc (KMRC) as the first mortgage refinance company in Kenya to provide long term finance to primary mortgage lenders (commercial banks, mortgage finance companies, microfinance banks and Savings and Credit Co-operatives) to support the Government's Big Four Agenda of providing affordable housing to a wider segment of Kenya's populace.
- The CBK transferred to the Government Consolidated Fund Ksh. 5 billion on February 17, 2021 as an exceptional distribution from CBK's General Reserve Fund to support funding needs especially in the COVID-19 period.
- On October 21, 2020, H.E. President Uhuru Kenyatta opened the CBK Kisii Currency Centre to serve seven counties (Kisii, Nyamira, Migori, Bomet, Homa Bay, and parts of Narok and Kericho), with a population of over 7 million people contributing about 12 percent of Kenya's GDP.
- On January 26, 2021, CBK joined H.E. President Uhuru Kenyatta in the Groundbreaking Ceremony for the Kenya Police Leadership Academy in Ngong, Kajiado County. The CBK is supporting the development of the Academy that will provide the National Police Service with modern training facilities for its senior leadership. In turn, this arrangement will allow CBK to build on land leased from the National Police Service and provide adequate accomodation for CBK's Police Officers in Nairobi.

On behalf of the Board, I wish to sincerely thank the Bank Management and entire staff for the commitment and dedication to duty, and support to the Board, especially during this difficult year. Despite the ongoing challenges, the future remains very hopeful.

Mr. Mohamed Nyaoga
Chairman,
CBK Board of Directors

BOARD OF DIRECTORS

Mr. Mohamed Nyaoga
Chairman

Dr. Patrick Njoroge
Governor

Dr. Julius Muia
PS, The National Treasury

Mrs. Nelius W. Kariuki
Member

Mr. Samson K. Cherutich
Member

Mr. Ravi J. Ruparel
Member

Mrs. Rachel Dzombo
Member

MEMBERS OF THE MONETARY POLICY COMMITTEE


Dr. Patrick Njoroge
Governor


Mrs. Sheila M'Mbijjewe
Deputy Governor


Dr. Margaret Chemengich
External Member


Dr. Julius Muia
PS, The National Treasury


Prof. Jane K. Mariara
External Member


Dr. Benson Ateng'
External Member


Mr. Humphrey Muga
External Member


Mr. David Luusa
Director, Financial Markets


Prof. Robert Mudida
Director, Research

SENIOR MANAGEMENT

Dr. Patrick Njoroge
Governor

Mrs. Sheila M'Mbijjewe
Deputy Governor

Mr. Kennedy K. Abuga
Director, Governor's Office (Board Secretary)

Mr. David Luusa
Director, Financial Markets

Ms. Caroline Mackola
Director, Finance (Appointed on February 22, 2021)

Mr. Anthony N. Gacanja
Director, Information Technology

Mr. Gerald Nyaoma
Director, Bank Supervision

Mr. Raphael O. Otieno
Acting Director, Research

SENIOR MANAGEMENT

Mr. Moses M. Ngotho
Acting Director, Finance
(Until February 21, 2021)

Ms. Beth Kithinji
Director, Internal Audit and Risk Management
(Appointed on May 10, 2021)

Ms. Darliah Mbugua
Director, Human Resources
(Appointed on September 1, 2020)

Mr. Stephen Muriu
Director, General Services

Mrs. Matilda Onyango
Acting Director, Internal Audit and Risk Management
(Retired on May 10, 2021)

Mr. Paul K. Wanyagi
Acting Director, Currency Operations

Ms. Terry W. Ng'ang'a
Acting Director, Human Resources
(Until August 31, 2020)

Mr. Michael Eganza
Director, Banking and National Payments
(Appointed on January 4, 2021)

Mr. William Nyagaka
Director, Kenya School of Monetary Studies

Mr. Patrice Odude
Acting Director, Strategic Management

Mr. Mwenda K. M'Marete
Acting Director, Banking and National Payments
(Until January 4, 2021)

1.0 GLOBAL ECONOMY

1.0 GLOBAL ECONOMY

According to the July 2021 IMF World Economic Outlook Update, global output growth should rebound strongly to 6.0 percent in 2021, before slowing to 4.9 percent in 2022. A 0.5 percentage-point revision for 2022 is largely driven by the expected strong growth outturn in advanced economies, partly reflecting additional fiscal support, associated positive spillovers across economies and the anticipated vaccine-powered recovery in the second half of the year **(Table 1.1).**

Growth prospects in the advanced economies are expected to reach 5.6 percent in 2021 before slowing to 4.4 percent in 2022, owing to pent-up demand fueled by accumulated savings in 2020, as well as improved contact-intensive activities. However, there is a significant divergence in growth recovery prospects, with the US and United Kingdom growth expected to return to pre-pandemic levels in the second half of 2021, further supported by positive spillovers to trading partners. Japan, on the other hand, is partially offsetting the strong growth momentum for the group due to sharp rise in the COVID-19 cases in the first half of 2021 that led to imposition of tighter restrictions. Most advanced economies are expected to recover in 2021 as follows: United States (7.0 percent), the United Kingdom (7.0 percent), Canada (6.3 percent), Spain (6.2 percent), France (5.8 percent), Italy (4.9 percent), Germany (3.6 percent) and Japan (2.8 percent) **(Table 1.1).**

Growth in emerging market and developed economies is expected to accelerate to 6.3 percent in 2021, largely reflecting increased rollout of vaccine, relaxation of containment measures, aggressive public spending, and central bank liquidity support. China is projected to expand at an annual rate of 7.5 percent in 2021. However, India's growth momentum slowed following the outbreak of the COVID-19 Delta variant at the beginning of the second quarter of 2021. Latin America's growth is projected to pick up to 5.8 percent, with growth for Brazil (5.3 percent) and Mexico (6.3 percent), reflecting better-than-expected first quarter outturns, favorable spillovers, and booming terms of trade. Economic activity in Sub-Saharan Africa (SSA) is expected to grow by 3.4 percent in 2021, which is significantly lower than several other emerging regions and below the pre-pandemic trend, with tourism-dependent economies suffering the most. Nigeria and South Africa are expected to grow at rates of 2.5 and 4.0 percent, respectively, and by 2.6 percent (Nigeria) and 2.2 percent (South Africa) in 2022 **(Table 1.1).** Owing to their economic size, Nigeria and South Africa's prospects have a considerable influence on overall sub-saharan African economic trends.

Global trade volumes are expected to increase by 9.7 percent in 2021 before slowing to 7.0 percent in 2022, driven by a strong rebound in merchandise volumes, while cross-border services trade (tourism, transportation) is expected to remain subdued in the short term **(Table 1.1).** Oil prices are expected to rise by 30 percent in 2021 from their low point in 2020, owing in part to supply restrictions imposed by OPEC (Organisation of the Petroleum Exporting Countries, which includes Russia and other non-OPEC oil exporters). Metal prices are expected to rise sharply in 2021, owing largely to China's recovery, while food prices are expected to rise. Global financial conditions have remained stable with minimal volatilities and are expected to continue supporting global growth prospects in the medium-term despite inflationary pressures experienced mostly in the advanced economies and a few of emerging market and developing economies.

Uncertainty surrounding the global growth prospects remains high despite the expectation of mass rollout of vaccine across economies, additional policies support, increased social safety nets and accommodative financial conditions. The risks of a pandemic resurgence, vaccine-resistant strains, and operational threats such as vaccine development and delivery delays remain significant. Tighter financial conditions, which imply a re-evaluation of market dynamics, a rise in core sovereign yields, and a reassessment of inflation risks, could all result in a rapid repricing of financial assets.

1.0 GLOBAL ECONOMY

Table 1.1: Actual and Projected Output in Selected Countries/Regions

	Actual		Estimates	Projections	
Country/Region	**2018**	**2019**	**2020**	**2021**	**2022**
World Output	**3.6**	**2.8**	**-3.2**	**6.0**	**4.9**
Advanced Economies	**2.2**	**1.6**	**-4.6**	**5.6**	**4.4**
United States	2.9	2.2	-3.5	7.0	4.9
Euro area	1.9	1.3	-6.5	4.6	4.3
Japan	0.3	0.0	-4.7	2.8	3.0
United Kingdom	1.3	1.4	-9.8	7.0	4.8
Emerging Market and Developing economies	**4.5**	**3.7**	**-2.1**	**6.3**	**5.2**
Emerging and Developing Asia	6.3	5.4	-0.9	7.5	6.4
China	6.7	6.0	2.3	8.1	5.7
India	6.1	4.0	-7.3	9.5	8.5
Emerging and Developing Europe	3.2	2.5	-2.0	4.9	3.6
Russia	2.5	2.0	-3.0	4.4	3.1
Latin America and the Caribbean	1.1	0.1	-7.0	5.8	3.2
Brazil	1.3	1.4	-4.1	5.3	1.9
Sub-Saharan Africa	3.2	3.2	-1.8	3.4	4.1
South Africa	1.9	0.2	-7.0	4.0	2.2
Nigeria	0.8	2.2	-1.8	2.5	2.6
Middle East, North Africa, Afghanistan and Pakistan	**1.8**	**1.4**	**-2.6**	**4.0**	**3.7**

Source: IMF, World Economic Outlook, July 2021 update

2.0 COVID-19 RESPONSE AND MITIGATION MEASURES

2.0 COVID-19 RESPONSE AND MITIGATION MEASURES

Coronavirus (COVID-19) Pandemic

The coronavirus (COVID-19) was declared a global pandemic in March 2020, by the World Health Organization. The pandemic precipitated an unprecedented global health and economic crisis. In Kenya, the first COVID-19 case was announced on March 13, 2020, and CBK immediately took a frontline position in ensuring that the Kenyan financial sector remained resilient despite the threats posed by the pandemic. CBK immediately instituted a series of emergency measures to mitigate the health and economic effects of the pandemic.

Measures to Mitigate the Impact of COVID-19 Pandemic

The measures were informed by:

- The need to reduce cash transactions and facilitate digital transactions, primarily to abate the risk of COVID-19 contact transmission.
- The need to cushion borrowers from the likely adverse economic effects arising from the COVID-19 pandemic while safeguarding banking system soundness.
- Supporting operations of the financial institutions by ensuring there was adequate liquidity to support both banks and borrowers as a result of the pandemic.
- Ensuring business continuity for both the financial institutions as well as for CBK to ensure that institutions have resilient frameworks to effectively address emerging pandemic risks in the banking sector.
- Ensuring health and safety of bank customers and staff.

Digital platforms - This was the first set of emergency measures announced on March 16, 2020, by CBK in conjunction with commercial banks and Payment Services Providers (PSPs). The immediate objective was to reduce the risk of transmission of COVID-19 by handling banknotes and coins. The measures included;

- Removal of charges for low value mobile money transactions for up to Ksh.1,000.
- The transaction limit for mobile money was increased to Ksh.150,000 from Ksh.70,000.
- The daily limit of transactions for mobile money was increased to Ksh.300,000 from Ksh.140,000.
- The mobile money wallet limit was increased to Ksh.300,000 from Ksh.140,000.
- The monthly total limit for mobile money transactions was eliminated.
- The tariff for mobile money transactions for Ksh.70,000 was applied for transactions up to Ksh.150,000.
- PSPs and commercial banks were to eliminate charges for transfers between mobile money wallets and bank accounts.

The emergency measures applied from March 16, 2020 to June 30, 2020, and were extended to December 31, 2020. Thereafter, the measures were allowed to expire by end of December 2020.

Affordable credit- On March 23 and April 29, 2020, the Monetary Policy Committee (MPC) lowered the Central Bank Rate to 7.25 percent from 8.25 percent and to 7.00 percent from 7.25 respectively to signal the banking sector to lower lending and deposit rates to support the provision of affordable credit to Kenyans. Similarly, on March 23, MPC reduced the Cash Reserve Ratio (CRR) to 4.25 percent from 5.25 percent, releasing KSh.35.2 billion as additional liquidity availed to banks to directly support borrowers that are distressed as a result of COVID-19.

Restructuring personal/household and other loans by banks - On March 18, 2020, CBK announced measures to cushion borrowers on the adverse effects of the pandemic as follows.

- Banks to provide relief to personal and household borrowers on their loans based on their circumstances arising from the pandemic.

- Micro, Small and Medium-sized Enterprises (MSMEs) and corporate borrowers to contact their banks for assessment and restructuring of their loans based on their respective circumstances arising from the pandemic.

2.0 COVID-19 RESPONSE AND MITIGATION MEASURES

- CBK to provide flexibility to banks with regard to requirements for loan classification and provisioning for loans that were performing as at March 2, 2020, and whose repayment period was extended or were restructured due to the pandemic.

The relief granted under the emergency measures would only apply to borrowers whose loan repayments were up to date as at March 2, 2020, and classified under the normal category per the CBK Prudential Guideline on Risk Classification of Assets, Provisioning and Limitation of Interest on Non-Performing Loans.

Business Continuity - On March 25, 2020, CBK instructed banks to activate their precautionary measures to ensure continuity of operations.

Guidance Note on Pandemic Planning for the banking sector- On March 27, 2020, CBK issued a Guidance Note on Pandemic Planning for the banking sector. The Note set out the minimum standards that institutions should develop to establish sound and effective business continuity management practices to address pandemics. The key requirement was for banks to report pandemic incidences to CBK within 24 hours.

Impact and Outcomes of COVID-19 Mitigation Measures

Digital Platforms - The measures to incentivize mobile money facilitated low value mobile money transactions and expanded usage of mobile money with higher limits.

- The monthly volume of person-to-person transactions increased by 87 percent between February and December 2020.
- Over the same period, the volume of transactions below Ksh. 1,000 increased by 114 percent, while 2.8 million additional customers are using mobile money.
- Business-related transactions also recorded significant growth over the same period.
- The measures lapsed on December 31, 2020.

Reduction of Cash Reserve Ratio (CRR)

- Ksh.32.8 billion (93.1 percent) of the Ksh.35.2 billion freed from the reduction in CRR disbursed by CBK to the banks as at June 30, 2021.
- Disbursements to banks were approved based on justification for lending to deserving borrowers affected by COVID-19 pandemic.

Restructuring of loans

- This measure expired on March 2, 2021.
- Cumulatively, since March 2020, loans amounting to Ksh.1.7 trillion were restructured by end February 2021, accounting for 57 percent of the banking sector gross loans.
- During the one-year period the emergency measures were in place, over 300,000 loan accounts mainly in the Personal and Household, Trade, Real Estate, Manufacturing, and Transport and Communication Sectors were restructured.
- These sectors have borne the brunt of the impact of the COVID-19 pandemic. This measure provided space to borrowers to ride through the pandemic, mitigate job losses and pivot their business models to the 'new normal'.
- For banks, the restructuring provided time to build additional capital and liquidity buffers to take them through the pandemic period and beyond.
- Following repayments, expiry of the restructuring period and reversion of loans to normal terms, the outstanding restructured loans as at end June 2021, amounted to Ksh.494.2 billion or 16 percent of the total gross loans.
- Over 94 percent of the outstanding restructured loans at end June 2021, were performing as per the restructured terms.
- CBK is closely monitoring the unwinding of the outstanding restructured loans to ensure the continued stability of the banking sector.

Pandemic planning – Banks continued offering services across the country in branches and through digital channels during the pandemic. Over 90 percent of bank branches remained open even in *locked down* areas.

3.0 DOMESTIC ECONOMY

3.0 DOMESTIC ECONOMY [1]

3.1 Real Sector

After growing strongly at 5.2 percent in the first quarter of 2020, the advent of COVID-19 in March 2020 saw the economy contract significantly by -5.5 percent in the second quarter of 2020 arising from disruptions to supply-chains, reduced external demand and local demand shocks due to measures that were put in place to control the spread of the virus. However, the economy started recovering in the third quarter in which the contraction narrowed to -1.1 percent. The Services sectors were the most adversely affected including Education; Wholesale and Trade; Transport and Storage; and Accommodation and Restaurants **(Table 3.1 and Chart 3.1).**

Table 3.1: Real Gross Domestic Product and Related Aggregates

Main Sectors	Growth Rates (Percent)					
	2019*	Q1 2020	Q2 2020	Q3 2020	Q1-Q3 2019	Q1-Q3 2020
1. Agriculture	**3.6**	**5.8**	**7.3**	**6.3**	**3.6**	**6.4**
2. Non-Agriculture (o/w)	**5.9**	**4.9**	**-9.2**	**-2.7**	**5.9**	**-2.4**
2.1 Industry	**4.7**	**4.4**	**-0.5**	**4.9**	**4.9**	**2.9**
Mining & Quarrying	2.5	9.5	10.0	18.2	3.2	12.6
Manufacturing	3.3	2.9	-3.9	-3.2	3.5	-1.4
Electricity & water supply	7.0	6.3	-0.6	4.7	7.2	3.3
Construction	6.4	5.3	3.9	16.2	6.6	8.6
2.2 Services	**6.7**	**5.5**	**-11.6**	**-5.3**	**6.6**	**-3.9**
Wholesale & Retail Trade	6.6	6.4	-7.0	-2.5	6.7	-1.3
Accommodation & restaurant	10.3	-9.3	-83.2	-57.9	10.9	-45.1
Transport & Storage	7.8	6.1	-11.4	2.9	7.2	-0.9
Information & Communication	9.0	9.8	4.6	7.3	8.6	7.5
Financial & Insurance	6.6	6.2	4.2	5.3	6.5	5.3
Public administration	8.1	6.7	5.7	9.6	8.7	7.3
Professional, Administration & Support Services	4.9	4.4	-15.3	-12.3	4.8	-7.9
Real estate	5.3	4.4	2.3	5.3	5.4	4.0
Education	5.4	5.3	-56.2	-41.9	5.4	-31.2
Health	5.8	5.8	10.3	5.6	5.7	7.3
Other services	5.1	2.2	-8.5	-4.5	5.5	-3.6
FISIM	6.1	5.0	3.7	7.7	6.2	5.5
2.3 Taxes on products	**4.4**	**3.4**	**-14.2**	**-4.2**	**4.3**	**-5.2**
Real GDP Growth	**5.4**	**5.2**	**-5.5**	**-1.1**	**5.3**	**-0.4**
** Revised*						
*** Provisional*						

Source: Kenya National Bureau of Statistics

[1] *This Annual Report incorporates economic data from KNBS that was available as at September 3, 2021. In particular, GDP data that was released by KNBS on Septemeber 9, 2021, has not been incorporated.*

3.0 DOMESTIC ECONOMY

Agriculture

Growth in the Agricultural sector was strong, supported by favourable weather conditions that led to increased crop production. The sector grew by 6.4 percent in the first three quarters of 2020 compared to 3.6 percent in the same period of 2019, and contributed 1.5 percentage points to overall GDP growth.

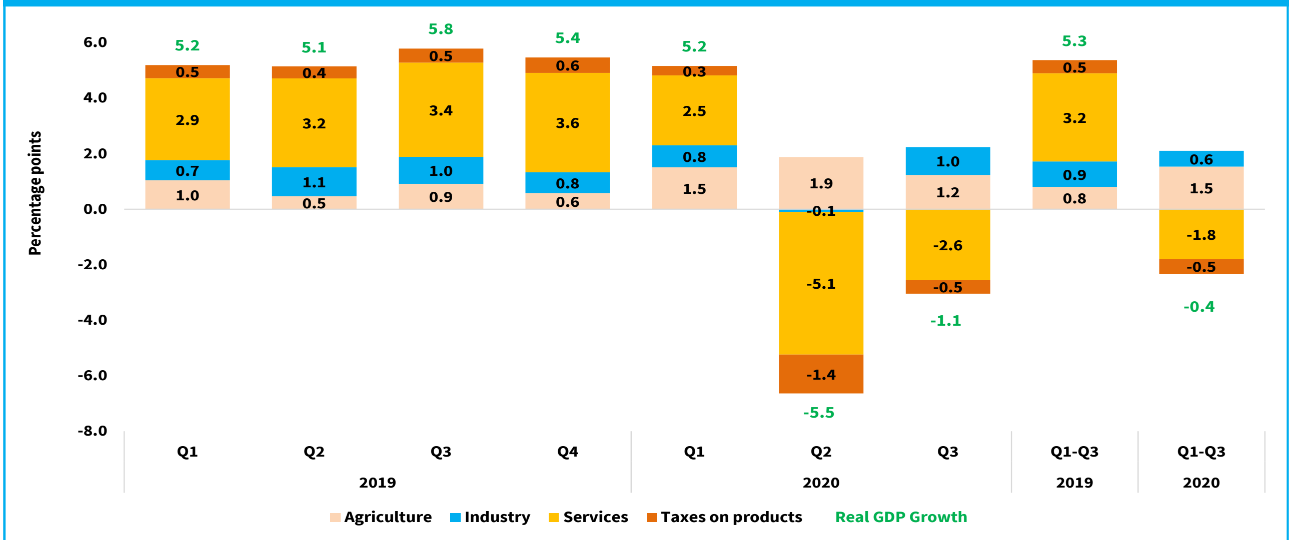
Services

The Services sector contracted by -3.9 percent in the first three quarters of 2020 compared to a growth of 6.6 percent in the same period of 2019, as it was severely affected by the domestic and global COVID-19 containment measures. As a result, a significant reduction in activity was witnessed in Education, Accommodation and Restaurant, Wholesale and Retail Trade, and Transport and Storage.

Industry

Growth in Industry slowed to 2.9 percent in the first three quarters of 2020 compared to 4.9 percent in the same period of 2019. The slowdown was mainly attributed to suppressed activity in the Manufacturing sector due to the COVID-19 pandemic. However, Construction and Mining and Quarrying sectors recorded strong growth in the period under review.

Chart 3.1: Contributions to Real GDP Growth



Source: Kenya National Bureau of Statistics

3.0 DOMESTIC ECONOMY

3.2 Inflation

Overall inflation remained well anchored around the target range in the FY2020/21. This implies that it has been relatively resilient to short-term shocks. It increased to 6.3 percent in June 2021, from 4.6 percent in June 2020, driven by elevated fuel and food prices **(Table 3.2 and Chart 3.2).**

Table 3.2: Developments in Inflation (Percent)

	2020							2021					
	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21
Overall 12-month inflation	4.6	4.4	4.4	4.2	4.8	5.3	5.6	5.7	5.8	5.9	5.8	5.9	6.3
Food Inflation	8.1	6.6	5.4	5.2	5.8	6.1	7.2	7.4	6.9	6.7	6.4	7.0	8.5
Fuel Inflation	5.5	8.7	10.9	10.9	12.2	11.0	11.3	12.1	13.8	15.8	14.8	14.3	13.5
Non-(Food & Fuel) Inflation	1.7	1.6	1.9	1.7	2.3	2.7	2.6	2.4	2.2	2.3	2.4	2.5	2.6
Three months annualised	3.0	-0.5	-0.1	1.1	4.7	8.4	12.7	11.3	9.7	7.2	7.9	5.8	4.6

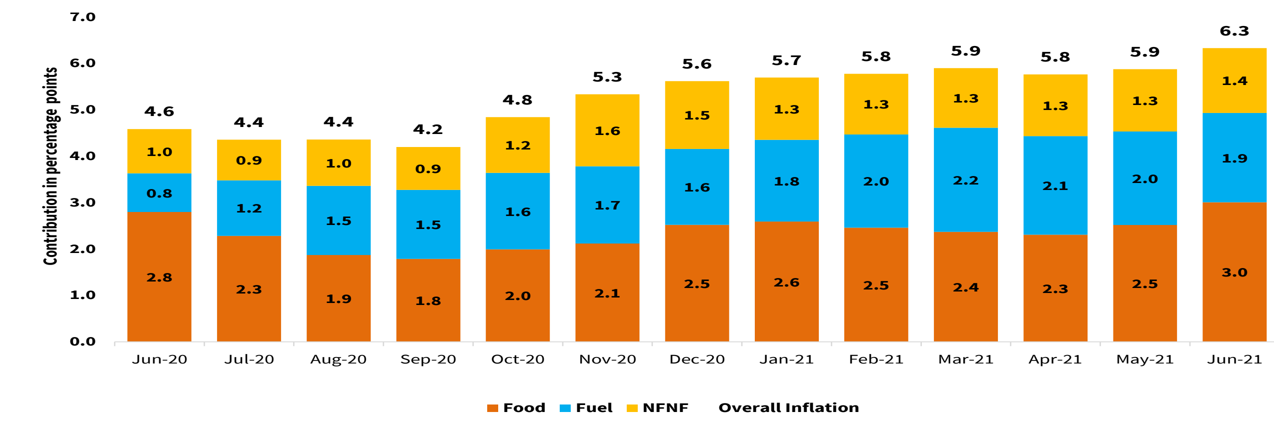
Source: Kenya National Bureau of Statistics and CBK

Non-Food-Non-Fuel (NFNF) inflation remained low and stable during FY2020/21, reflective of muted demand pressures in the economy. It increased to 2.6 percent in June 2021, from 1.7 percent in June 2020. The increase in NFNF in the year to June 2021 partly reflected implementation of excise tax measures in October 2020 which affected the prices of cigarettes, petroleum jelly, spirits, wines and beer.

Fuel inflation remained elevated during the FY2020/21, driven by high energy prices and the impact of COVID-19 containment measures in the transport sector. It increased to 13.5 percent in June 2021, from 5.5 percent in June 2020.

Food inflation remained stable in the FY2020/21. Despite favourable weather conditions, food inflation increased to 8.5 percent in June 2021 from 8.1 percent in June 2020, reflective of higher prices of selected key food items.

Chart 3.2: Contributions of Food, Fuel, and Non-Food-Non-Fuel Inflation to Overall Inflation



Source: Kenya National Bureau of Statistics and CBK

3.0 DOMESTIC ECONOMY

3.3 Balance of Payments

The Current Account

During the FY2020/21, the current account deficit widened to USD 5,518 million compared with USD 5,077 million in the FY2019/20 **(Table 3.3).** The higher deficit was attributed to lower service receipts, which more than offset improved earnings from strong agricultural exports, resilient diaspora remittances and savings from oil imports.

Goods Account

The deficit in the goods account remained stable at USD 9,527 million in the FY2020/21 compared with USD 9,460 million in the previous year reflecting an increase in merchandise exports coupled with a pickup in intermediate imports. Imports of intermediate goods increased in the FY2020/21 reflecting pent up domestic demand and increased economic activities from the third quarter of 2020 onwards, as COVID-19 related restrictions domestically and globally eased.

Imports from China accounted for 23.8 percent of total imports to Kenya during the year to June 2021 making it the largest source of imports. During the period, imports from the European Union accounted for 14.8 percent of total imports and rose to USD 2,356 million, while the share of imports from Africa decreased to 11.7 percent, equivalent to USD 1,858 million from 12.5 percent the previous year.

The performance of merchandise exports improved by 7.9 percent to USD 6,398 million in the FY2020/21. Exports of agricultural commodities remained strong reflecting robust international demand for horticulture (fruits and vegetables) that surpassed pre-pandemic levels. In addition, the performance of cut flower exports improved in the second half of 2020 following the resumption of demand in the international markets, especially the European Union, and increased availability of adequate freight space.

Kenya's exports to Africa improved to USD 2,574 million in FY2020/21 compared with USD 2,213 million in FY2019/20, reflecting increased exports to EAC and Common Market for Eastern and Southern Africa (COMESA) regions. The share of exports to East African Community (EAC) increased to 24.9 percent in FY 2020/21 from 23.5 percent in FY2019/20. Although the share of exports to the rest of the world declined, those to the United Kingdom and Netherlands increased from 7.3 percent and 7.1 percent in the FY2019/20 to 7.4 percent and 8.5 percent, respectively, in the FY2020/21 **(Table 3.4).**

Services Account

Receipts from transport and travel services remained subdued due to COVID-19 related disruptions. As a result, the balance in the services account worsened by USD 1,150 million in FY2020/21 from a surplus of USD 1,028 million in FY2019/20. The reduction was mainly due to lower receipts from travel and transport services following COVID-19 related disruptions to international travel and transport following income shocks and travel restrictions.

Primary and Secondary Income Account

The balance on the primary income account improved by USD 302 million. The surplus on the secondary income account rose from USD 5,013 million in FY2019/20 to USD 5,485 million in the FY 2020/21 mainly on account of the recovery of remittances in key source countries following faster than expected economic revival.

Remittances

Remittance inflows increased by 6.0 percent to USD 305.9 million in June 2021. In the year to June 2021, total remittance inflows stood at USD 3,383 million compared to USD 2,809 million in the same period in 2020, a 20.5 percent increase. The United States continues to be the largest source of remittances to Kenya, accounting for 58.8 percent of remittances in the year to June 2021 and has experienced a robust economic recovery from COVID-19 in 2021.

3.0 DOMESTIC ECONOMY

Table 3.3: Balance on Current Account (USD Million)

Item	FY 2019/20*	FY 2020/21				FY 2020/21**	FY 2020/21-2019/20	
		Jul-Sep Q1	Oct-Dec Q2	Jan-Mar Q3	Apr-Jun Q4		Absolute Change	Change %
Current Account	**-5,077**	**-1,333**	**-1,323**	**-1,481**	**-1,381**	**-5,518**	**-442**	**8.7**
Goods	**-9,460**	**-2,122**	**-2,316**	**-2,569**	**-2,520**	**-9,527**	**-67**	**0.7**
Exports (fob)	**5,924**	**1,516**	**1,474**	**1,739**	**1,670**	**6,398**	**475**	**8.0**
o.w Coffee	203	47	43	75	73	238	36	17.5
Tea	1,216	282	282	326	299	1,189	-27	-2.2
Horticulture	931	233	265	334	289	1,122	191	20.5
Oil products	63	18	15	11	13	56	-7	-11.0
Manufactured Goods	369	111	107	106	131	455	86	23.3
Raw Materials	347	76	80	115	96	367	20	5.8
Chemicals and Related Products	445	119	124	113	126	482	37	8.3
Miscelleneous Man.Articles	531	163	154	144	181	642	111	20.9
Re-exports	816	174	114	197	150	635	-181	-22.2
Other	968	283	291	311	302	1,186	218	22.5
Imports (fob)	**15,384**	**3,638**	**3,790**	**4,308**	**4,189**	**15,925**	**542**	**3.5**
o.w Oil	2,689	526	554	717	782	2,579	-110	-4.1
Chemicals	2,456	682	631	774	750	2,837	381	15.5
Manufactured Goods	2,793	720	784	910	879	3,292	500	17.9
Machinery	3,016	698	689	698	646	2,731	-285	-9.5
Transport Equipment	1,445	384	362	377	362	1,485	39	2.7
Food	1,715	324	394	474	434	1,627	-88	-5.1
Other	3,567	705	937	1,023	901	3,566	-1	0.0
Services	**1,028**	**-25**	**9**	**-80**	**-26**	**-122**	**-1,150**	**-111.9**
Transport Services (Net)	**551**	**-65**	**-35**	**-91**	**-70**	**-260**	**-811**	**-147.2**
Travel Services (Net)	**621**	**107**	**66**	**83**	**118**	**373**	**-248**	**-39.9**
Other Services (Net)	**-144**	**-67**	**-22**	**-73**	**-74**	**-235**	**-91**	**63.2**
Primary Income (Net)	**-1,657**	**-405**	**-307**	**-221**	**-422**	**-1,355**	**302**	**-18.2**
Secondary Income (Net)	**5,013**	**1,218**	**1,291**	**1,390**	**1,586**	**5,485**	**473**	**9.4**

** Revised*

***Provision*

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Source: CBK

3.0 DOMESTIC ECONOMY

Table 3.4: Kenya's Direction of Trade

IMPORTS	(in millions of US dollars)		Share of Imports (%)		EXPORTS	(in millions of US dollars)		Share of Exports (%)	
	Year to June		Year to June			Year to June		Year to June	
Region/Country	**2020**	**2021****	**2020**	**2021**	**Region/Country**	**2020**	**2021****	**2020**	**2021**
Africa	**1,929**	**1,858**	**12.5**	**11.7**	**Africa**	**2,213**	**2,574**	**40.2**	**40.2**
Of which					*Of which*				
South Africa	547	401	3.6	2.5	Uganda	623.11	791.24	10.5	12.4
Egypt	419	448	2.7	2.8	Tanzania	309.84	315.84	5.2	4.9
Others	963	1,009	6.3	6.3	Egypt	182.04	185.63	3.1	2.9
					Sudan	71.64	73.27	1.2	1.1
EAC	**568**	**632**	**3.7**	**4.0**	South Sudan	176.13	180.62	3.0	2.8
COMESA	**1,092**	**1,053**	**7.1**	**6.6**	Somalia	100.39	114.30	1.7	1.8
Rest of the World	**13,461**	**14,063**	**87.5**	**88.3**	DRC	128.76	221.57	2.2	3.5
Of which					Rwanda	231.25	247.18	3.9	3.9
India	1,766	1,872	11.5	11.8	Others	390.32	444.07	6.6	6.9
United Arab Emirates	1,169	1,170	7.6	7.3					
China	3,430	3,793	22.3	23.8	**EAC**	**1,395**	**1,595**	**23.5**	**24.9**
Japan	893	847	5.8	5.3	**COMESA**	**1,481**	**1,810**	**25.0**	**28.3**
USA	555	580	3.6	3.6	**Rest of the World**	**3,714**	**3,825**	**62.7**	**59.8**
United Kingdom	293	298	1.9	1.9	*Of which*				
Singapore	70	64	0.5	0.4	United Kingdom	433.84	470.87	7.3	7.4
Germany	407	380	2.6	2.4	Netherlands	419.37	545.40	7.1	8.5
Saudi Arabia	915	750	5.9	4.7	USA	473.48	491.50	8.0	7.7
Indonesia	580	475	3.8	3.0	Pakistan	490.67	477.97	8.3	7.5
Netherlands	211	507	1.4	3.2	United Arab Emirates	368.32	292.91	6.2	4.6
France	229	214	1.5	1.3	Germany	116.47	140.56	2.0	2.2
Bahrain	6	46	0.0	0.3	India	43.46	102.33	0.7	1.6
Italy	203	232	1.3	1.5	Afghanistan	37.17	5.70	0.6	0.1
Oman	65	220	0.4	1.4	Thailand	24.45	18.65	0.4	0.3
Others	2,668	2,614	17.3	16.4	Others	1,307	1,279	22.0	20.0
Total	**15,390**	**15,921**	**100.0**	**100.0**	**Total**	**5,927**	**6,398**	**100.0**	**100.0**
EU	2,066	2,356	13.4	14.8	EU	1,296	1,502	21.9	23.5
China	3,430	3,793	22.3	23.8	China	151	165	2.6	2.6

***Provisional*
Source: CBK

Table 3.5: Balance on the Capital and Financial Account (USD Million)

ITEM	FY 2019/20*	FY 2020/21				FY 2020/21**	FY 2020/21-2019/20	
		Jul-Sep Q1	Oct-Dec Q2	Jan-Mar Q3	Apr-Jun Q4		Absolute Change	Change %
Capital account credit	146	**36**	**28**	**84**	**273**	**421**	**275**	**189**
Capital account credit	146	36	28	84	273	421	275	189
Capital account: debit	0	0	0	0	0	0	0	0
Financial Account	**-4,598**	**-295**	**-424**	**-699**	**-2,779**	**-4,198**	**399**	**-9**
Direct investment: assets	160	39	33	31	509	612	452	283
Direct investment: liabilities	839	93	150	109	143	495	-344	-41
Portfolio investment: assets	1,111	252	337	227	256	1,072	-39	-3
Portfolio investment: liabilities	-61	-6	11	75	1,098	1,177	1,239	-2,016
Financial derivatives: net	4	11	-19	14	3	9	5	125
Other investment: assets	430	-103	995	398	-332	958	528	123
Other investment: liabilities	5,525	409	1,608	1,185	1,974	5,177	-348	-6

** Revised*
***Provisional*
Source: CBK

3.0 DOMESTIC ECONOMY

Capital and Financial Account

The capital account recorded increased inflows by USD 275 million in the FY2020/21, due to increased project grants. The financial account recorded stable net inflows of USD 4,198 million in FY 2020/21 compared to USD 4,598 million in the previous year, reflecting Kenya's issuance of USD 1 billion Sovereign Bond in June 2021 in the international capital markets and inflows from international financial institutions, particulary the World Bank and International Monetary Fund, for the Government's economic program **(Table 3.5).**

3.4 Government Budget

Government budgetary operations in the FY2020/21 resulted in a preliminary deficit including grants (from the financing side) of KSh 867.7 billion (7.8 percent of GDP) compared to KSh 790.8 billion (7.8 percent of GDP) in the previous year. The deficit which was supported by improved revenues was however, below the target level of 8.7 percent of GDP indicatably better than expected economic recovery and improved fiscal consolidation **(Table 3.6 and Chart 2.3).**

Table 3.6: Statement of Central Government Operations in KSh Billion

		FY 2018/19	FY 2019/20	FY 2020/21		Over(+) / Below (-) Target	% change FY 2020/21- FY 2019/20	FY 2020/21 % share to GDP
		Actual	Actual	Preliminary	Target-Revised Budget II Approved			
1.	**REVENUE & GRANTS**	**1,724.1**	**1,756.8**	**1,809.6**	**1,910.6**	**-101.0**	**3.0**	**16.2**
	Revenue	1,704.4	1,737.0	1,738.4	1,837.8	-99.5	0.1	15.6
	Tax Revenue	1,437.9	1427.5	1,484.8	1,469.5	15.3	4.0	13.3
	Non Tax Revenue	61.8	145.9	77.3	109.3	-32.1	-47.1	0.7
	Appropriations-in-Aid	204.6	163.6	176.4	259.0	-82.7	7.8	1.6
	External Grants	19.7	19.8	71.2	**72.8**	-1.6	259.2	0.6
2.	**EXPENDITURE AND NET LENDING**	**2,433.7**	**2,565.4**	**2,753.0**	2,885.9	**-132.9**	**7.3**	**24.6**
	Recurrent Expenditure	1,531.1	1,645.2	1,767.0	1,820.5	-53.5	7.4	15.8
	Development Expenditure	541.9	594.9	595.2	666.5	-71.3	0.0	5.3
	County Transfers	360.7	325.3	390.8	398.9	-8.1	20.1	3.5
	Other	0.0	0.0	0.0	**0.0**	0.0	0.0	0.0
3.	**DEFICIT (incl Grants) on a commitment basis (1-2)**	**-709.6**	**-808.6**	**-943.4**	-975.3	**31.9**	**16.7**	**-7.8**
	Deficit (incl Grants) on a commitment basis (% of GDP)	-7.6	-7.9	-7.8	-8.7	1.0	-2.2	-0.1
4.	**ADJUSTMENT TO CASH BASIS**	**0.0**	**11.8**	**0.0**	**0.0**	**0.0**	**-100.0**	**0.0**
5.	**DEFICIT ON A CASH BASIS**	**-709.6**	**-796.8**	**-943.4**	-975.3	**31.9**	**18.4**	**-7.8**
	Deficit on a cash basis (% of GDP)	-7.6	-7.8	-7.8	**-8.7**	1.0	-0.8	-0.1
6.	**DISCREPANCY: Expenditure (+) / Revenue (-)**	**11.4**	**-6.0**	**-75.7**	**0.5**	**-76.3**	**1,154.9**	**-0.7**
7.	**FINANCING**	**721.1**	**790.8**	**867.7**	**975.8**	**-108.1**	**9.7**	**7.8**
	Domestic (Net)	306.5	450.4	492.5	560.0	-67.6	9.3	4.4
	External (Net)	414.5	340.4	375.2	415.8	-40.6	10.2	3.4
	Capital Receipts (net of restructuring costs)	2.9	2.6	6.3	0.0	6.3	140.8	0.1
	Others	0.0	0.0	0.0	0.0	0.0	0.0	0.0

Source: The National Treasury-Provisional Budget Outturn, June 2021

The deficit in FY2021/22 is projected to further decline to 7.5 percent of GDP, which will be financed by net domestic financing of KSh 658.5 billion (5.3 percent of GDP) and net external financing of KSh 271.2 billion (2.2 percent of GDP). The Government remains committed to the fiscal consolidation over the medium term.

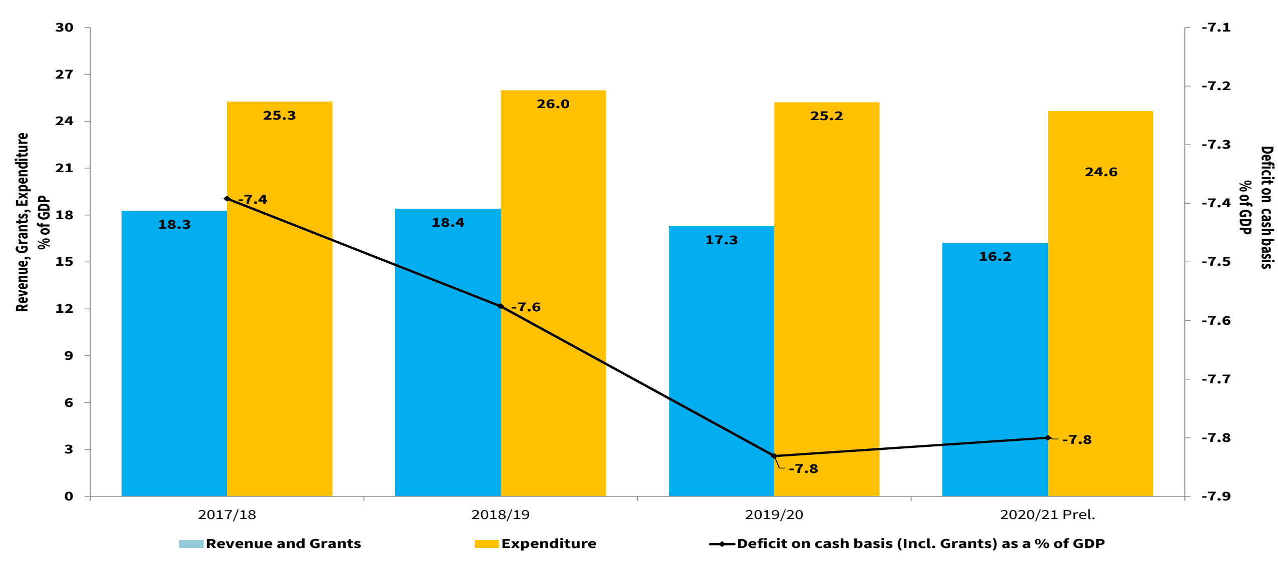
Government Revenue

Government revenue (including grants) in FY2020/21 increased by 3.0 percent to KSh 1,809.6 billion (16.2 percent of GDP) compared to the previous fiscal year. The increase was reflected in both revenues and grants. Tax revenue accounted for 85.4 percent of revenues and increased by 4.0 percent mainly on account of increases in inflows from import, excise and value added taxes. Non-tax revenue decreased by 47.1 percent largely due to increased equity withdrawals on parastatal deposits. Appropriations-In-Aid and external grants increased by 7.8 percent and 259.2 percent, **(Table 3.6)** respectively on account of increased appropriations towards development and increases in programme and project grants.

Expenditure and Net Lending

Government expenditure and net lending increased by 7.3 percent to KSh 2,753.0 billion (24.6 percent of GDP) in FY2020/21 but remained below the programmed target. The increase in expenditures mainly reflected a rise in recurrent expenditures and county transfers which increased by 7.4 percent and 20.1 percent, respectively. Recurrent expenditure accounted for 64.2 percent of total government expenditure **(Chart 3.3).**

Chart 3.3: Government Budget Performance



Source: The National Treasury-Provisional Budget Outturn, June 2021

Financing

Net domestic borrowing during FY 2020/21 amounted to KSh 491.3 billion. The borrowing comprised KSh 230.9 billion from Commercial Banks, KSh 327.0 billion from Non-Banking Financial Institutions and KSh 1.2 billion from non-residents and repayment of 67.9 billion to the Central Bank **(Table 3.7).**

3.0 DOMESTIC ECONOMY

Table 3.7: Domestic Financing (KSh Billion)

		FY2017/18	FY2018/19	FY2019/20	FY2020/21
1.	**From CBK**	(26.9)	13.6	49.7	(67.9)
2.	**From commercial banks**	124.3	126.9	235.4	230.9
3.	**From Non-banks**	172.8	160.3	165.8	327.0
4.	**From Non-Residents**	3.0	2.8	5.2	1.2
	Change in Credit from banks(From 30th June 2020)	97.4	140.5	285.1	163.0
	Change in Credit from non-banks(From 30th June 2020)	172.8	160.3	165.8	327.0
	Change in Credit from non-residents(From 30th June 2020)	3.0	2.8	5.2	1.2
5.	**Total Change in Dom. Credit (From 30th June 2020)**	273.2	303.7	456.1	491.3
NB. Treasury Bills are reflected at Cost					

Source: CBK and National Tresury June 2021 Quarterly Economic and Budgetary Review

Outlook for FY 2021/22

In the budget estimates for FY2021/22 total revenue (including Appropriations-in-Aid and grants) is projected at KSh 2.1 trillion (17.0 percent of GDP) while Government expenditure and net lending is projected at KSh 3.0 trillion (24.5 percent of GDP). The overall budget deficit including grants is, therefore, projected at KSh 929.7 billion (or 7.5 percent of GDP) to be financed through net external borrowing of KSh 271.2 billion (or 2.2 percent of GDP) and net domestic financing of KSh 658.5 billion (or 5.3 percent of GDP). This reflects improved fiscal consolidation.

3.5 Public Debt

Kenya's public and publicly guaranteed debt increased by 15.2 percent during the FY2020/21, with both domestic and external debt increasing at 16.4 percent and 14.2 percent, respectively. Public debt profile comprised of 47.9 percent and 52.1 percent of domestic and external debt respectively. The ratio of public debt to GDP rose to 68.4 percent in June 2021 from 65.6 percent in June 2020 reflecting the impact of the COVID-19 pandemic on revenue and expenditures in the first half of the FY2020/21 **(Table 3.8).**

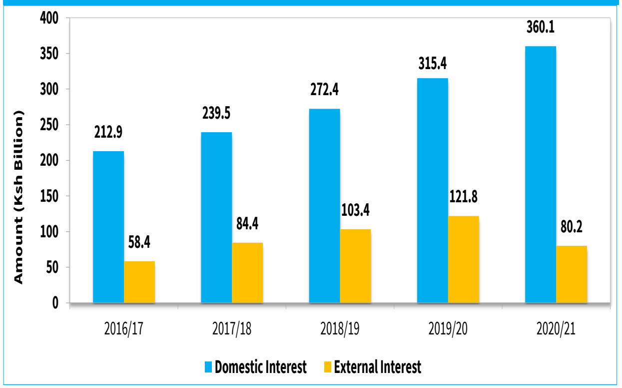
Domestic Debt

The increase in domestic debt was mainly driven by increased uptake of Treasury bonds by 28.4 percent. This brought the ratio of Treasury bonds to bills to 78.4:21.6 surpassing the government's medium-term objective of achieving 70:30 ratio of Treasury bonds to Treasury bills. This goal was accomplished through issuance of medium- and long-term Treasury bonds during the fiscal year. Consequently, Treasury bills decreased by 13.5 percent to Ksh 784.8 billion from Ksh 907.7 billion in the FY 2019/20 **(Table 3.8).**

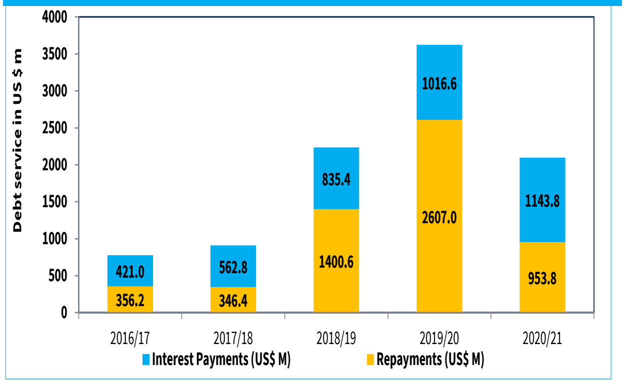
External Debt

Kenya's public and publicly guaranteed external debt increased by 14.2 percent to KSh 4,015.3 billion **(Table 3.8).** This growth was majorly on account of disbursements from International Development Association (IDA), June 2021 Eurobond, Development Bank of China and the Italian government. Government's efforts to improve the structure of Kenya's public and publicly guaranteed external debt resulted into increased concessionality as the proportion of debt owed to multilateral lenders increased by 3.7 percentage points while that of commercial creditors decreased by 1.6 percentage points. This improved debt structure was aimed at enhanced debt sustainability.

3.0 DOMESTIC ECONOMY



Source: The National Treasury



Source: The National Treasury and CBK

Public Debt Service

Cumulative interest and other charges on domestic debt increased by 23.3 percent while that on external debt decreased by 12.7 percent during the FY2020/21 **(Chart 3.4)**. Total external debt service decreased during the FY2020/21. There was a significant reduction in principal repayments majorly due to the absence of one-off repayments of commercial loans during the FY 2020/21 which contributed to increased debt service sustainability **(Chart 3.5).**

Table 3.8: Public Debt

	June 2017		June 2018		June 2019		June 2020		June 2021*	
	KSh bn	%	KSh bn	%	KSh bn	%	KSh bn	%	KSh bn	%
DOMESTIC DEBT										
Securitised debt	**2,100.5**	**99.4**	**2,413.8**	**97.4**	**2,723.5**	**97.8**	**3,127.1**	**98.4**	**3,634.7**	**98.3**
Treasury Bills	768.5	36.4	901.9	36.4	975.3	35.0	907.7	28.6	784.8	21.2
Of which Repo Treasury bills	24.4	1.2	23.3	0.9	21.1	0.8	20.5	0.6	19.4	0.5
Treasury Bonds	1,332.0	63.1	1,511.9	61.0	1,748.1	62.8	2,219.4	69.9	2,849.9	77.1
Non Securitised debt	**11.1**	**0.5**	**65.0**	**2.6**	**62.0**	**2.2**	**50.4**	**1.6**	**63.0**	**1.7**
Overdraft at CBK	0.0	0.0	56.8	2.3	57.3	2.1	47.1	1.5	59.3	1.6
others	11.1	0.5	8.1	0.3	4.7	0.2	3.3	0.1	3.3	0.1
TOTAL DOMESTIC DEBT	**2,112.3**	**100.0**	**2,478.8**	**100.0**	**2,785.5**	**100.0**	**3,177.0**	**100.0**	**3,697.7**	**100.0**
(as a % of GDP)	27.6		29.1		29.9		31.2		32.8	
(as a % of Total Debt)	47.9		49.2		48.0		47.5		47.9	
EXTERNAL DEBT										
Bilateral	724.8	31.6	816.1	31.9	996.1	32.9	1,074.3	30.6	1,142.1	28.4
Multilateral	841.9	36.7	821.0	32.1	914.4	30.2	1,321.6	37.6	1,659.7	41.3
Comm. Banks	712.1	31.0	906.4	35.4	1,095.8	36.2	1,102.3	31.4	1,195.6	29.8
Export Credit	15.9	0.7	16.7	0.7	16.9	0.6	17.6	0.5	17.9	0.4
TOTAL EXTERNAL DEBT	**2,294.7**	**100.0**	**2,560.2**	**100.0**	**3,023.1**	**100.0**	**3,515.8**	**100.0**	**4,015.3**	**100.0**
(as a % of GDP)	30.0		30.0		32.5		34.5		35.6	
(as a % of Total Debt)	52.1		50.8		52.0		52.5		52.1	
TOTAL PUBLIC DEBT	**4,407.0**		**5,039.0**		**5,808.6**		**6,692.8**		**7,713.0**	
(as a % of GDP)	57.5		59.1		62.4		65.6		68.4	
** Provisional*										

Source: The National Treasury and CBK

4.0 REGIONAL INTEGRATION DEVELOPMENTS

4.0 REGIONAL INTEGRATION DEVELOPMENTS

Background

During the FY2020/21, the CBK participated in regional integration initiatives under the EAC, COMESA and the Association of African Central Banks (AACB). The initiatives involved harmonising economic and financial policies among partner states, strengthening regional financial sector supervision, and integrating regional financial systems. The aim of these integration efforts is increased intra-regional trade, higher economic growth rates of partner countries and regional peace.

The integration initiatives are evaluated against criteria that are specified in monetary cooperation programmes, with monetary and financial system integration targets. The following highlights Kenya's progress towards meeting the targets.

The EAC Monetary Cooperation Programme

During the year, Kenya became the chair of the EAC, and therefore the CBK took over the chairmanship of the Monetary Affairs Committee (MAC). The CBK worked with the other EAC Central Banks to coordinate activities and programmes towards establishing the East African Monetary Union (EAMU), which will encompass a single currency area and an East African Central Bank. In preparation for the EAMU, the EAC Partner States have agreed to attain and maintain for at least three consecutive years four macroeconomic convergence criteria; namely, a ceiling on overall inflation of 8 percent; a ceiling on fiscal deficit, including grants, of 3 percent of GDP; a ceiling on gross public debt of 50 percent of GDP in net present value terms; and a floor of foreign exchange reserves cover of 4.5 months of imports.

In FY2020/21, Kenya met the EAMU Convergence criteria on inflation and foreign exchange reserves. However, the country did not meet the criteria on fiscal deficit and gross national debt because of increased public spending to mitigate the adverse impact of COVID-19 on businesses and households, reduced tax revenue due to the pandemic, and continued public investment in physical infrastructure.

The COMESA Monetary Cooperation Programme

The overarching objective of the COMESA Monetary Cooperation Programme is the establishment of a Monetary Union by the year 2025. Towards this end, partner states are expected to maintain a number of primary (preconditions for convergence) and secondary (reinforcement conditions) convergence criteria **(Table 4.1).** In FY2020/21, Kenya met the COMESA Convergence Criteria on inflation and foreign reserve adequacy. However, challenges remain in attaining the criteria related to revenue and debt.

Table 4.1: Convergence Criteria under the COMESA Monetary Programme

Primary Criteria	Secondary Criteria
Overall budget deficit to GDP ratio (including grants) not exceeding 5 percent.	Variability of the nominal exchange rate against the US dollar not exceeding ± 10 percent, with a target of ± 5 percent.
Annual average inflation rate of 7 percent with a band of +/- 1 percent.	General Government debt to GDP ratio of less than 65 percent.
Central bank financing of the budget as a share of the previous year's tax revenue not exceeding 5 percent, with a target of 0 percent.	Total tax revenue to GDP ratio of not less than 20 percent.
External reserves of equal to or more than 3 months of imports of goods and non-factor services, with a target of more than 6 months.	Government capital investment to tax revenue ratio of not less than 20 percent.

Source: CBK

4.0 REGIONAL INTEGRATION DEVELOPMENTS

The Association of African Central Banks (AACB)

The African Monetary Cooperation Programme (AMCP) is implemented by the Association of African Central Banks (AACB) with a view to establishing a monetary union, with a single currency and a common central bank, among AACB member states. During the year under review, Kenya met the criteria on inflation, central bank credit to government, external reserves, exchange rate variability and government capital investment. The convergence criteria under the AMCP are provided below.

Table 4.2: The Convergence Criteria under the AMCP

Primary Criteria	Secondary Criteria
Annual average inflation rate not exceeding 7 percent (Target ≤ 3 percent by 2038).	General Government debt to GDP ratio of not more than 65 percent.
Overall budget deficit/GDP ratio of not more than 5 percent (Target ≤ 3 percent by 2033).	Total tax revenue to GDP ratio of not less than 20 percent.
Minimize the central bank financing of the budget to below 5 percent (Target 0 percent by 2038).	Nominal Exchange Rate Variability ±10 percent (Target ± 5 percent).
External reserves of equal to or more than 3 months of imports of goods and non-factor services (Target ≥ 6 months by 2038).	Ratio of Government Capital Investment to Tax Revenue of not less than 30 percent.

Source: CBK

5.0 CENTRAL BANK OPERATIONS

5.0 CENTRAL BANK OPERATIONS

5.1 Monetary Operations

Monetary Policy

Monetary policy during the FY2020/21 was aimed at maintaining inflation at the target of 5.0 percent with a flexible margin of 2.5 percent on either side. Additionally, an accomodative monetary policy aimed at mitigating the adverse economic effects arising from the COVID-19 pandemic. Overall inflation remained within the target range throughout the year, while non-food-non-fuel inflation remained below 5.0 percent, indicating muted demand pressures in the economy.

The Monetary Policy Committee (MPC) held six bi-monthly meetings between July 2020 and June 2021. During these meetings, the MPC retained the Central Bank Rate (CBR) at 7.00 percent noting that the accommodative monetary policy stance remained appropriate, as inflation expectations remained well anchored within target range, and the economy was operating below its potential level.

Money Supply

Annual growth in money supply, M3, moderated to 6.3 percent in FY2020/21 compared to 9.1 percent in FY2019/20, mainly reflecting a decrease in net lending to government on account of increased government deposits at the Central Bank. Additionally, the decline in net foreign assets of the banking system also contributed to moderate growth of money supply, reflecting a relatively lower level of net reserves compared to similar period in FY 2020/21. However, the increase in lending to the private sector partly cushioned the decline in money supply **(Table 5.1)** which was in line with the accomodative monetary policy stance. On the liability side, the decrease in money supply was reflected in slower growth in

Table 5.1: Monetary Aggregates

		End Month Level (KSh Billion)			Annual Growth Rate (Percent)			Annual Absolute Change (KSh Billion)		
		2018/19	2019/20	2020/21	2018/19	2019/20	2020/21	2018/19	2019/20	2020/21
Components of M3										
1.	**Money supply, M1 (1.1+1.2+1.3)**	**1,575.5**	**1,692.9**	**1,775.2**	**10.5**	**7.5**	**4.9**	**149.9**	**117.4**	**82.3**
	1.1 Currency outside banks	196.9	210.9	225.9	-9.8	7.1	7.1	-21.3	13.9	15.0
	1.2 Demand deposits	1,212.8	1,350.0	1,409.9	7.6	11.3	4.4	86.0	137.2	60.0
	1.3 Other deposits at CBK 1/	165.8	132.2	139.5	104.2	-20.3	5.5	84.6	-33.6	7.3
2.	**Money supply, M2 (1+2.1)**	**2,943.7**	**3,227.6**	**3,373.5**	**9.8**	**9.6**	**4.5**	**261.9**	**283.9**	**145.8**
	2.1 Time and saving deposits	1,372.7	1,538.7	1,600.0	9.1	12.1	4.0	114.4	165.9	61.3
3.	**Money supply, M3 (2+3.1)**	**3,564.2**	**3,890.0**	**4,133.8**	**9.2**	**9.1**	**6.3**	**301.6**	**325.8**	**243.8**
	3.1 Foreign Currency Deposits	620.5	662.4	760.3	6.8	6.7	14.8	39.7	41.9	98.0
Sources of M3										
1.	**Net foreign assets 2/**	**939.9**	**886.0**	**779.7**	**24.2**	**-5.7**	**-12.0**	**183.0**	**-54.0**	**-106.2**
	Central Bank	941.0	918.1	831.7	20.1	-2.4	-9.4	157.4	-22.9	-86.3
	Banking Institutions	-1.1	-32.1	-52.0	-95.9	2,855.8	61.9	25.6	-31.1	-19.9
2.	**Net domestic assets (2.1+2.2)**	**2,624.3**	**3,004.0**	**3,354.1**	**4.7**	**14.5**	**11.7**	**118.6**	**379.7**	**350.0**
	2.1 Domestic credit	3,490.0	3,930.3	4,391.7	7.8	12.6	11.7	252.7	440.3	461.4
	2.1.1 Government (net)	890.5	1,148.7	1,406.1	19.5	29.0	22.4	145.5	258.1	257.5
	2.1.2 Private sector	2,503.0	2,693.2	2,901.1	5.2	7.6	7.7	122.6	190.2	207.9
	2.1.3 Other public sector	96.4	88.4	84.4	-13.8	-8.3	-4.5	-15.4	-8.0	-4.0
	2.2 Other assets net	-865.6	-926.2	-1,037.6	18.3	7.0	12.0	-134.1	-60.6	-111.4
Memorandum items										
4.	**Overall liquidity, L (3+4.1)**	**4,799.1**	**5,367.7**	**5,829.9**	**10.5**	**11.8**	**10.7**	**455.3**	**568.6**	**576.3**
	4.1 Non-bank holdings of government securities	1,234.9	1,477.7	1,790.3	14.2	19.7	22.5	153.7	242.8	332.5

Absolute and percentage changes may not necessarily add up due to rounding
1/ Includes county deposits and special projects deposit
2/ Net Foreign Assets at current exchange rate to the US dollar.

Source: CBK

deposits, partly arising from increased investment in government securities.

Domestic Credit

Annual growth in net domestic credit moderated to 11.7 percent in FY2020/21 from 12.6 percent in FY2019/20, reflecting a decline in net lending to the government **(Table 5.2).** Net lending to government grew by 22.4 percent in FY 2020/21 compared to 29.0 percent in FY2019/20, mainly reflecting increased government deposits at Central Bank, supported by receipts from international finance institutions and issuance of sovereign bond which occurred towards the end of the financial year. Net credit to other public sector also declined due to repayments by parastatals.

Private sector credit growth remained resilient during the FY2020/21, growing at 7.7 percent in FY2020/21 compared to 7.6 percent in FY 2019/20, supported by an accommodative monetary policy stance and improved economic activity. Strong lending was recorded in manufacturing, transport and communication, finance and insurance, and consumer durables **(Table 5.2).** Lending to private corporates was mainly for short-term working capital requirements, and the lending to households was supported by digital platforms, including mobile loans as well as secured lending through the check-off system.

Reserve Money

Reserve money increased by KSh 22.9 billion in FY2020/21 compared to a decline of KSh 12.9 billion in the previous financial year, mainly due to an increase in net domestic assets of the Central Bank that offset the decline in net foreign assets. The increase in net domestic assets was largely due to an increase in net lending to commercial banks, on account of relatively lower open market operations compared to similar period in 2020. The decline in net foreign assets of the Central Bank mainly reflected scheduled government debt servicing and other central bank operations **(Table 5.3)**.

Table 5.2: Banking Sector Net Domestic Credit

		End Month Level (KSh Billion)		Annual Growth Rate (Percent)		Annual Absolute Change (KSh Billion)	
		2019/20	2020/21	2019/20	2020/21	2019/20	2020/21
1.	**Credit to Government**	**1,148.7**	**1,406.1**	**29.0**	**22.4**	**258.1**	**257.5**
	Central Bank	-62.8	-50.2	-66.9	-20.0	126.9	12.6
	Commercial Banks & NBFIs	1,211.5	1,456.3	12.2	20.2	131.3	244.9
2.	**Credit to other public sector**	**88.4**	**84.4**	**-8.3**	**-4.5**	**-8.0**	**-4.0**
	Local government	4.4	6.6	16.8	51.2	0.6	2.3
	Parastatals	84.0	77.8	-9.4	-7.4	-8.7	-6.2
3.	**Credit to private sector**	**2,693.2**	**2,901.1**	**7.6**	**7.7**	**190.2**	**207.9**
	Agriculture	88.1	91.3	2.2	3.7	1.9	3.2
	Manufacturing	397.2	429.4	11.1	8.1	39.6	32.2
	Trade	489.2	498.8	9.4	1.9	42.1	9.5
	Building and construction	114.2	116.5	4.6	2.0	5.1	2.3
	Transport & communications	200.7	224.4	14.9	11.8	26.0	23.7
	Finance & insurance	95.8	106.8	3.2	11.5	3.0	11.0
	Real estate	395.8	411.8	4.9	4.0	18.3	16.0
	Mining and quarrying	14.6	12.7	10.0	-13.0	1.3	-1.9
	Private households	443.3	457.7	3.2	3.2	13.7	14.4
	Consumer durables	253.5	312.7	15.2	23.4	33.4	59.2
	Business services	154.4	162.4	5.3	5.2	7.8	8.0
	Other activities	46.4	76.7	-3.7	65.2	-1.8	30.3
4.	**Total (1+2+3)**	**3,930.3**	**4,391.7**	**12.6**	**11.7**	**440.3**	**461.4**

Source: CBK

5.0 CENTRAL BANK OPERATIONS

Table 5.3: Reserve Money and its Components

		End Month Level		Annual Growth Rate (Percent)		Annual Absolute Change (KSh Billion)	
		2019/20	2020/21	2019/20	2020/21	2019/20	2020/21
1.	**Net Foreign Assets**	**918.1**	**831.7**	**-2.4**	**-9.4**	**-22.9**	**-86.3**
2.	**Net Domestic Assets**	**-491.2**	**-382.0**	**-2.0**	**-22.2**	**10.0**	**109.2**
	2.1 Government Borrowing (net)	-62.8	-50.2	-66.9	-20.0	126.9	12.6
	2.2 Commercial banks (net)	-131.0	-6.1	514.2	-95.3	-109.7	124.9
	2.3 Other Domestic Assets (net)	-300.7	-328.8	2.4	9.3	-7.1	-28.1
3.	**Reserve Money**	**426.9**	**449.8**	**-2.9**	**5.4**	**-12.9**	**22.9**
	3.1 Currency outside banks	210.9	225.9	7.1	7.1	13.9	15.0
	3.2 Bank reserves	216.0	223.9	-11.0	3.6	-26.8	7.8
	3.2.1 Required Reserves	153.5	167.0	-12.2	8.8	-21.4	13.5
	3.2.2 Cash in Till	46.9	51.2	-10.7	9.2	-5.6	4.3
	3.2.3 Excess Reserves	15.5	5.6	1.6	-64.0	0.2	-9.9

Source: CBK

5.2 Interest Rates

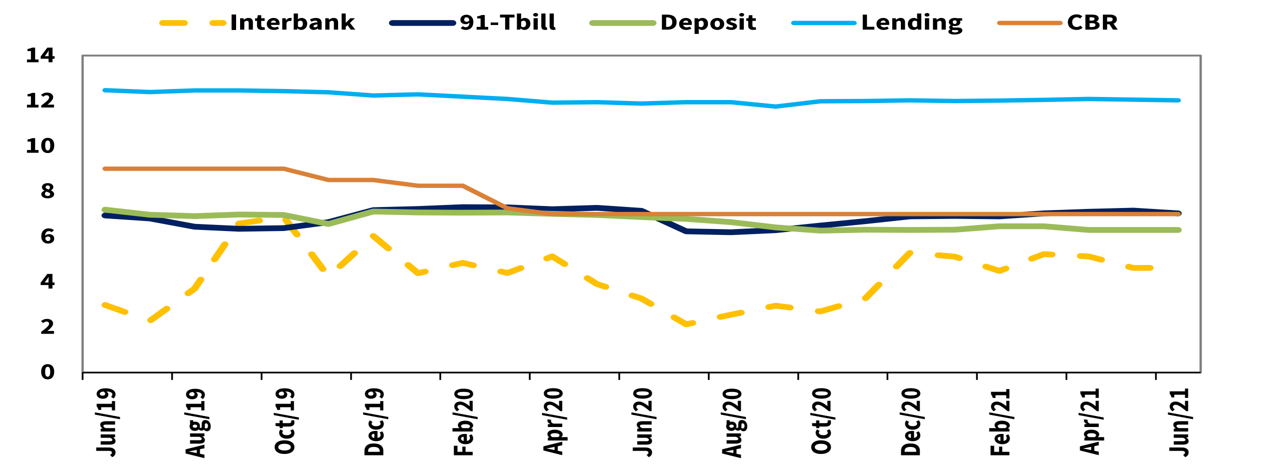
Short Term Rates

Short term interest rates remained relatively stable and low during FY2020/21 supported by accommodative monetary policy stance and ample liquidity conditions in the market **(Chart 5.1).** The average interbank interest rate was 4.01 percent in FY2020/21 compared with an average of 4.64 percent in FY2019/20. The average interbank rate remained below the CBR, partly reflecting improved liquidity distribution across the bank tiers. The average 91-day Treasury bill rate declined slightly from 6.94 percent to 6.74 percent, while the average 182-day Treasury bill rate decreased from 7.80 percent to 7.31 percent.

Commercial Bank Rates

Commercial banks average lending rate also remained relatively stable at about 12 percent in the FY2020/21, reflecting the accommodative monetary policy stance. Similarly, the average commercial banks deposit rate was relatively stable at 6.41 percent.

Chart 5.1: Interest Rates (Percent)



Source: CBK

5.3 Foreign Exchange Operations and Reserves Management

Exchange Rate

The Kenya foreign exchange market remained resilient in the FY2020/21 despite the impact of COVID-19 on the economy. The resilience has been supported by a relatively stable current account deficit and balanced forex flows including the positive impact of the recovery of diaspora remittances in early 2021. The resilience of the foreign exchange market also reflected Kenya's diversified economy and export markets which provided a cushion against adverse effects of external shocks. During the first quarter of the FY, the Kenya shilling exchanged at 107.94 against the USD and weakened to 109.75 in the third quarter before strengthening to 107.76 per dollar in the fourth quarter **(Table 5.4).** Overall, with the onset of the COVID-19 pandemic, the shilling weakened 4.5 per cent vis-à-vis the US dollar in line with experiences of other emerging and developing economies resulting in a 2.4 per cent depreciation for the FY2019/20. Among regional currencies, the local unit gained 6.1 per cent against the South African Rand but weakened 6.0 per cent and 4.1 per cent against the Ugandan shilling and Tanzanian shilling, respectively.

Table 5.4: Kenya Shilling Exchange Rates

	2017/18	2018/19	2019/20	FY2020/21				Annual Average 2020/21	% change 2020/21_2019/20
				Q1 Jul-Sep	Q2 Oct-Dec	Q3 Jan-Mar	Q4 Apr-Jun		2020/21
US Dollar	102.37	101.16	103.58	107.94	109.49	109.75	107.76	108.74	5.0
Pound Sterling	137.86	130.94	130.51	139.35	144.50	151.25	150.67	146.44	12.2
Euro	122.14	115.44	114.49	126.12	130.44	132.43	129.91	129.72	13.3
100 Japanese Yen	92.84	91.09	95.03	101.70	104.79	103.71	98.52	102.18	7.5
South Africa Rand	7.99	7.14	6.66	6.38	7.00	7.33	7.62	7.08	6.4
Uganda Shilling*	35.74	36.94	35.87	34.20	33.78	33.48	33.17	33.66	-6.2
Tanzania Shilling*	22.01	22.76	22.26	21.50	21.18	21.22	21.52	21.36	-4.1
Rwanda Franc*	8.29	8.82	9.05	8.92	8.98	9.04	9.29	9.06	0.1
Burundi Franc*	17.15	17.76	18.07	17.87	17.69	17.71	18.26	17.88	-1.0

* Units of currency per Kenya Shilling

Source: CBK

Foreign Reserves

The official foreign Exchange Reserves in the FY2020/21 remained significantly above the statutory requirement of 4.0 months of import cover **(Table 5.5)** and the EAC foreign exchange reserves convergence criterion of 4.5 months of import cover. This position continued to provide adequate cover and a buffer against short-term shocks in the foreign exchange market. As at the end of June 2021, official foreign exchange reserves stood at USD 9,957 million (6.1 months of import cover) compared to USD 9,740 million at end of June 2020 (5.9 months of import cover).

5.0 CENTRAL BANK OPERATIONS

Table 5.5: Foreign Exchange Reserves and Residents' Foreign Currency Deposits

USD Million (End of Period)	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21
1. Gross Reserves	13,681	12,585	12,603	12,552	12,992	12,886	12,839	12,850	12,904	12,745	14,741	12,745	14,741
of which:													
Official	9,740	8,765	8,363	8,196	8,297	8,009	7,802	7,741	7,842	7,872	9,957	7,872	9,957
import cover*	5.9	5.4	5.1	5.0	5.1	4.9	4.8	4.7	4.8	4.8	6.1	4.8	6.1
Commercial Banks	3,941	3,820	4,240	4,356	4,695	4,878	5,037	5,109	5,062	4,874	4,784	4,874	4,784
2. Residents' foreign currency deposits	6,557	6,448	6,719	6,781	7,076	7,124	7,373	7,362	7,280	7,136	7,223	7,136	7,223

*Based on 36 month average of imports of goods and non-factor services

Source: CBK

5.4 Banking Sector Developments

During the financial year ended June 30, 2021, the Kenyan banking industry comprised of 38 commercial banks, 1 mortgage finance company, 14 microfinance banks, 9 representative offices of foreign banks, 67 foreign exchange bureaus, 17 money remittance providers and 3 credit reference bureaus. In addition, CBK approved:

- 90 percent acquisition of Jamii Bora Bank Ltd by the Co-operative Bank of Kenya Ltd. The bank was then renamed Kingdom Bank Ltd.
- 100 percent acquisition of Uwezo Microfinance Bank Limited by Salaam African Bank of Djibouti on March 25, 2021.
- Liquidation of Chase Bank Limited (Under Receivership) on April 16, 2021.
- Liquidation of Charterhouse Bank Limited (under statutory management) on May 7, 2021.

Performance of the Banking Industry

The industry balance sheet expanded by 9.1 percent in the year to June 2021, on account of increased loans and advances and government securities, which both accounted for 80.3 percent of total assets. Customer deposits accounted for 73.2 percent of total liabilities **(Table 5.6).**

Table 5.6: Extracts of Statement of Comprehensive Income (Ksh Billion)

	Jun-20	Jun-21	Absolute Change	% Change
Cash	63.96	64.33	375.10	0.60
Balances at CBK	316.72	246.82	-69.90	-22.10
Placements	277.64	384.92	107.28	38.60
Government Securities	1,521.71	1,761.21	239.50	15.70
Other Investments	63.95	57.34	-6.61	-10.30
Loans & Advances (Net)	2,651.50	2,798.24	146.74	5.50
Other Assets	312.34	367.13	54.79	17.50
Total Assets	5,207.82	5,679.99	472.17	9.10
Customer Deposits	3,903.62	4,249.41	345.79	8.90
Other Liabilities	534.67	579.79	45.12	8.40
Capital & Reserves	769.52	850.79	81.27	10.60
Total Liabilities and Shareholder's Funds	5,207.82	5,679.99	472.17	9.10

Source: CBK

Gross Loans and Advances - increased by 6.9 percent to Ksh 3.1 trillion in June 2021 from Ksh 2.9 trillion in June 2020. Key sectors that drove this growth were Transport and Communication (11.9 percent), Tourism, Restaurants and Hotels (11.4 percent), Energy and Water (10.7 percent) and Personal and Household (10.1 percent) **(Table 5.7).**

Table 5.7: Kenyan Banking Sector Gross Loans, KSh Billion

Sectors	Jun-20	Jun-21	Absolute Change	% Change
Mining & Quarrying	211.4	236.5	25.1	11.9
Tourism, Restaurant & Hotels	94.7	105.5	10.7	11.3
Transport & Communication	103.5	114.6	11.1	10.7
Manufacturing	797	877.2	80.2	10.1
Personal/Household	403.6	439.2	35.6	8.8
Real Estate	100.5	106.4	5.9	5.9
Building & Construction	118.9	125.2	6.3	5.3
Agriculture	92.4	97.3	4.9	5.3
Trade	429.6	448	18.4	4.3
Energy & Water	532.7	537.7	4.9	0.9
Financial Services	24.5	22.6	-1.9	-7.7
Total	2,908.70	3,110.10	201.4	6.9

Source: CBK

Capital Adequacy - In June 2021, core capital and total capital to total risk weighted assets ratios were 16.5 percent and 18.9 percent respectively. They were above the statutory minimum ratios of 10.5 percent and 14.5 percent respectively. Similarly core capital to total deposits ratio was 16.8 percent in 2021 as compared to 16.7 percent in June 2020. The ratios were above the statutory minimum of 8.0 percent.

Asset Quality - deteriorated with the gross non-performing loans (NPLs) to gross loans ratio increasing from 13.1 percent in June 2020 to 14.0 percent in June 2021.Transport and Communication, Mining and Quarrying, Real Estate, Building and Construction and Energy and Water recorded the highest increase in NPLs **(Table 5.8).** The increased NPLs was mainly attributed to a challenging business environment as a result of the adverse effects of the coronavirus (COVID-19) pandemic.

Table 5.8: Kenyan Banking Sector Gross Non-Performing Loans (KSh Billion)

Sectors	Jun-19	Jun-20	Absolute Change	Change (%)
Agriculture	21.1	44.8	23.7	112.3
Building & Construction	1.9	2.8	0.9	47.4
Energy and Water	52.6	68.2	15.6	29.7
Financial Services	25.2	31.7	6.5	25.8
Manufacturing	11.7	13.6	1.9	16.2
Mining & Quarrying	13.9	15.3	1.4	10.1
Personal/ Household	69.6	71.7	2.1	3
Real Estate	94.9	97.4	2.5	2.6
Tourism, Restaurant & Hotels	19.1	19.5	0.4	2.1
Trade	64.1	63.8	-0.3	-0.5
Transport & Communication	7.9	6.6	-1.3	-16.5
Total	382	435.3	53.3	14

Source: CBK

Profitability - The annual profit before tax increased by 11.3 percent from Ksh 134.1 billion in June 2020 to Ksh 149.2 billion in June 30, 2021, driven by Ksh 58.2 billion increase in income compared to Ksh 43.1 billion increase in expenses reflecting a robust recovery from the COVID-19 pandemic despite continued concerns about new variants. The increase in total income is attributed to Ksh 16.2 billion increase in earnings from advances and Ksh 31.9 billion increase in earnings from government securities. Total expenses increased by 10.7 percent annually from Ksh 404.1 billion in June 2020 to Ksh 447.2 billion in June 2021 due to a 47.1 percent increase in bad debt charge.

- ***Liquidity*** - remains strong with the overall liquidity ratio in June 2021 standing at 57.0 percent compared to 52.8 percent in June 2020. These were above the minimum statutory level of 20 percent.

5.0 CENTRAL BANK OPERATIONS

Performance of Microfinance Banks (MFBs)

Microfinance banks (MFBs) recorded the following performance during the year:

- Customer deposits increased by 8.6 percent from Ksh 46.8 billion in June 2020 to KSh 50.8 billion in June 2021.
- Total assets decreased from Ksh 77.2 billion in June 2020 to Ksh 76.0 billion in June 2021.
- Asset Quality improved with a decrease in gross NPLs from Ksh 14.2 billion in June 2020 to Ksh 12.3 billion in June 2021.
- Capital Adequacy - core capital to risk weighted assets ratio decreased from 14.0 percent in June 2020 to 10.5 percent in June 2021 and the total capital to total risk weighted assets decreased from 16.3 percent as at June 2020 to 14.3 percent in June 2021. However, the ratios were both above the minimum requirements of 10 percent and 12 percent respectively.
- Profitability declined to a loss of Ksh 2.4 billion in the twelve months to June 2021, compared to a loss of Ksh 1.0 billion recorded in the twelve months to June 2020.

Agency Banking

As at June 2021, there were 20 commercial banks and 3 microfinance banks that had contracted 79,995 and 1,314 active agents respectively since the inception of agency banking in 2010. The number of banking transactions via agents cumulatively increased from 815.3 million in June 2020 to 975.5 million transactions in the year to June 2021. Similarly, the value of banking transactions increased cumulatively from Ksh 5.7 trillion in June 2020 to Ksh 7.3 trillion in June 2021.

Legal and Regulatory Developments

The Kenya Mortgage Refinance Company (KMRC) Plc was granted a licence to conduct mortgage refinance business in Kenya on September 3, 2020. The establishment of mortgage refinance companies in Kenya is aimed at developing an active secondary mortgage market in Kenya for provision of long-term funding to primary mortgage lenders including commercial banks, microfinance banks and Savings and Credit Co-operatives (SACCOs).

Credit Guarantee Scheme The Government of Kenya, through the Public Finance Management Regulations (2020), set up a Ksh 3 billion Credit Guarantee Scheme (CGS). The CGS was operationalised on October 13, 2020. The objective of the CGS is to cushion participating commercial banks, providing them with confidence to extend loans to high-risk borrowers more efficiently and at affordable terms. The CGS is expected to support MSMEs' working capital, acquisition of assets and recovery from the COVID-19 pandemic impacts. The participating commercial banks are tasked with ensuring that the MSMEs meet certain requirements to access the CGS including being compliant with tax obligations, business permits and good credit scoring. These measures are key in measuring the risk of the participating MSMEs.

Measures to Mitigate the Impact of COVID-19 Pandemic

In March 2020, CBK announced emergency measures to ensure that the Kenyan banking sector remained resilient despite the threats posed by the coronavirus pandemic. The measures included encouraging use of digital platforms for transactions, lowering of the Central Bank Rate and Cash Reserve Ratio (CRR), and restructuring of loans by banks.

The cumulative restructured loans as at February 29, 2021, when the measure lapsed, were Ksh 1.8 trillion accounting for 57.1 percent of the banking sector's gross loans as at February 2021. As at June 30, 2021, the total outstanding restructured loans was Ksh 494.2 million or 15.9 percent of the gross loans outstanding loans of Ksh 3,110.1 billion. The top sectors which benefitted from the loan restructuring were Tourism, Trade, Transport and Communication.

The restructuring of loans gave flexibility, on loan repayments to borrowers to restructure their finances. Further, it provided banks with space to build their capital and liquidity buffers.

5.0 CENTRAL BANK OPERATIONS

As at June 30, 2021, commercial banks and microfinance banks had accessed Ksh 32.8 billion freed from the reduction in CRR from 5.25 percent to 4.25 percent to support restructuring of loans. This accounted for 93.1 percent of the Ksh 35.2 billion freed from the reduction of CRR. The 93.1 percent utilisation shows that the funds freed from reduction of CRR provided relief to borrowers to address the impact of COVID-19 pandemic. The top sectors which benefited from the reduction in CRR were Tourism, Trade, and Transport and Communication.

The emergency measures expired between December 2020 and March 2021.

Banking Sector 2021 Outlook

The banking industry is projected to remain stable and resilient in FY2021/22. Operational risk is expected to remain elevated with the continued COVID-19 infections. Credit risk is expected to ease in the short term. CBK will continue working with banks to enhance the resilience of the sector.

5.5 Developments in Currency Operations

Infrastructure Development for Improved Currency Operations

As part of CBK's effort to improve access to its services across the country, a new Centre was established in Kisii and was officially opened by H.E. President Uhuru Kenyatta on October 21, 2020. The Kisii Centre is a state-of-the-art facility, equipped with the latest IT and currency-handling technologies. The Centre will serve seven counties in the region (Kisii, Nyamira, Migori, Bomet, Homa Bay, and parts of Narok and Kericho). The Centre established in partnership with the Kenya Bankers Association (KBA) will offer currency services to bank branches in the region, opportunities for investment in Government securities (Treasury bills and bonds), and general banking services to County Governments.

Currency in Circulation

Currency in circulation increased by Ksh 19.35 billion, an increase of 7.5 percent compared to an increase of 3.3 percent in the previous financial year. Below is the detailed composition of Currency in Circulation:

Table 5.9: Composition of Currency in Circulation

	June 2020	June 2021	
	Ksh Billion	Ksh Billion	Growth (%)
Banknotes	9.42	9.75	3.50
Coins	257.79	277.14	7.51
Total Currency in Circulation	248.36	267.39	7.66

Source: CBK

Cash Inflows and Outflows

Deposits by banks during the financial year increased by 1.1 percent to Ksh 577.4 billion while withdrawals increased by 1.7 percent to Ksh 596.7 billion partly reflecting increased digital transactions. This represents a total net outflow of Ksh 19.4 billion **(Table 5.10)**.

Table 5.10: Currency in Circulation

Inflow (Deposits)	2019/2020	FY2020/21
	Ksh Billion	Ksh Billion
Banknotes	570.8	577.198
Coins	0.232	0.151
Total Inflows	**571.032**	**577.35**
Demonetisation		
Demonetised Currency	7.386	-
Outflow (Withdrawals)		
Banknotes	-586.33	-596.23
Coins	-0.41	-0.47
Total Outflows	**-586.732**	**-596.704**
Net Outflows	**-8.314**	**-19.354**

Source: CBK

5.6 Banking Services and National Payments

The year FY2020/21 was a challenging year due to the COVID-19 (Coronavirus) pandemic. However, this was matched with significant resilience and growth that was recorded in the National Payments System (NPS). The policy measures that CBK undertook in 2019/2020 were implemented throughout FY2020/21 , thereby enabling the NPS to play its role in cushioning the economy, businesses and the public against the spread and impact of COVID-19.

5.0 CENTRAL BANK OPERATIONS

Policy developments and measures to mitigate COVID-19

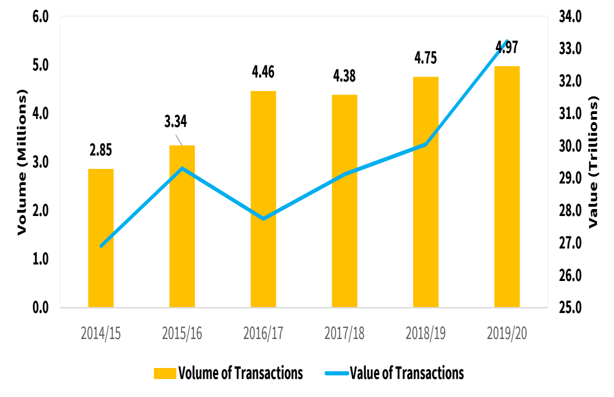
The year FY2020/21 was the first full financial year in which CBK implemented the COVID-19 measures that were announced towards the end of the previous year (March 2020). The measures were aimed at increasing the use of mobile payments to reduce COVID-19 transmission. Overall, these measures led to significant resilience and growth in mobile payments. The number of active mobile money customers increased by over 2.2 million comparing July 2020 and June 2021, while the volume and value of person-to-person transfers increased by 29 percent and 17 percent respectively, in the same period. The value of pay bill and till payments increased by 54 percent and 42 percent respectively, in the same period. This growth attests to the timelines and effectiveness of CBK's actions. In the year, CBK finalised public consultation on the draft National Payments System Vision and Strategy 2021 - 2025. This document will provide the overarching framework for improving payment services anchored on the pillars of trust, security, choice, usefulness and innovation.

Migration to new KEPSS platform

The New Generation Kenya Electronic Payment and Settlement System (NG-KEPSS) has modernised the payments space in Kenya. The NG KEPSS efficiency and scalability supports futuristic business needs ranging from increased volumes to extended operating hours. In the year FY2020/21, the system processed 6.087 million transaction messages valued at KSh 34.70 trillion compared to 4.97 million transaction messages valued at KSh 33.23 trillion in 2019/20 **(Chart 5.2).**

The SWIFT ISO 20022 standards is an emerging global and open standard for payments messaging. It creates a common language and model for payments data across the globe. Subsequently, the Kenyan payments industry has commenced arrangements to migrate to the SWIFT ISO 20022 standards and this includes the NG KEPSS. In order to augment the benefits of the upgraded system and upcoming changes in the payments industry, the community is reviewing the KEPSS Rules and Procedures for implementation in the year FY2021/22.

Chart 5.2: Volume and Value of KEPSS Transactions



Source: CBK

Authorisation of Payment Service Providers (PSPs)

In the year, CBK granted authorisation to Pesapal Limited to carry out the business of a Payment Service Provider (PSP). This brings the total number of authorised PSPs to eight, thereby deepening the growth of payment service delivery in Kenya. CBK also approved a number of product enhancements and pricing requests by PSPs in order to improve affordability, service delivery to customers, and innovation in general. CBK also vetted and approved a number of new officials at various levels of PSPs, thereby increasing effective governance and control of PSPs under CBK's purview.

NPS Circulars and Oversight

To ensure effective oversight based on various NPS laws, CBK undertook a range of measures aimed at promoting market discipline and effective compliance. In addition, two important circulars were issued in the year. One was aimed at mitigating risks posed by fraudulent and unlicensed financial schemes, and the second one on the roll out of "Pricing Principles" (customer-centricity; transparency and disclosure; fairness and equity; choice and competition; affordability). The Principles were aimed at implementing a gradual and orderly withdrawal of some COVID-19 mitigation measures in the short-term, and going forward, promote customer-centric and affordable service delivering in the long-term.

Regional Payment and Settlement Systems

The KEPSS interfaces with two regional payment systems, the East Africa Payment System (EAPS) used by traders and banks to make payments in the East African Community (EAC) region and settlement takes place in the EAC Partner States currencies i.e. KES, UGX, TZS and RWF and the Regional Electronic Payment and Settlement System (REPSS) for the COMESA countries whose settlement takes place in USD and EUR. In FY2020/21, banks sent 28,053 transactions worth about USD 440.5 million over the EAPS network. The leading currency utilised for EAPS payments in value terms was the Kenya shilling with a total value of USD 314.5 million which represented 71.4 percent of the total, while UGX was leading in volume terms with 14,229 transactions which represented 50.7 percent of the Total. A total of 1141 messages were transacted over the REPSS network valued at USD 83.2 million.

SWIFT Customer Security Program

The Bank coordinated implementation of SWIFT Customer Security Program 2020. This is a global program that involves all commercial banks putting in place security controls safeguarding against cyber attacks. The Kenyan financial industry achieved a 97 percent compliance level. In addition, the CBK Department through the SWIFT National Member Group (NMG) facilitated industry compliance with universal confirmations enabling banks to track their transactions end to end.

5.7 Domestic Debt Operations in FY 2020/21

Successful Government budget funding

The domestic debt market was conducted against the ongoing backdrop of COVID-19 and economic slowdown across the globe. The approach towards government funding was guided by the following key priorities:

i. Meet the domestic borrowing target.
ii. Manage the cost of debt by developing and maintaining a well-priced stable yield curve.
iii. Minimise debt maturity risk by extending bond tenor and targeting a higher ratio of T-Bonds to T-Bills.
iv. Contribute to stable liquidity flows.
v. Support market development.

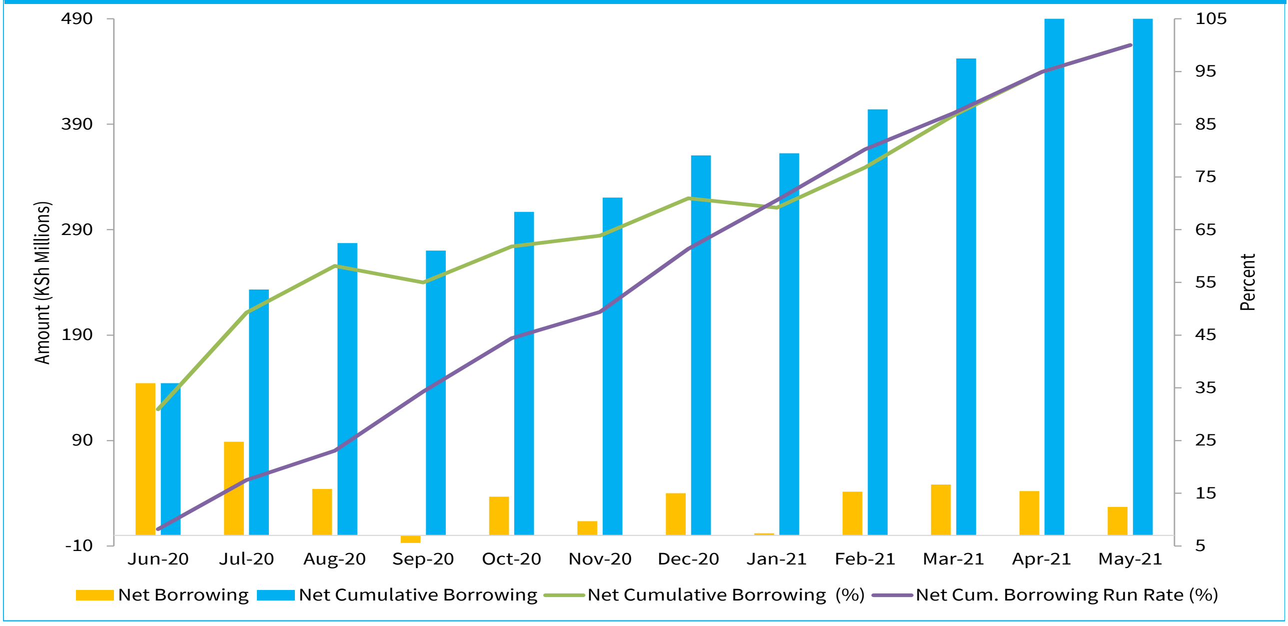
In line with these key priorities, the domestic debt market performed well during the year with sustained yield curve stability, lengthening of the maturity profile of domestic debt and increased secondary bond market liquidity, by 46 percent to KSh 771 billion in FY2020/21 from KSh 529 billion in FY2019/20. The borrowing target of KSh 521.9 billion in FY2020/21 was successfully achieved as illustrated in **Chart 5.3.**

Successful Debt Maturity Lengthening

The Average Time to Maturity (ATM) for Treasury bonds improved to 8.6 years by June 2021 from 7.7 years in June 2020 (up 11.7 percent), extending the bond maturity in line with the desired domestic debt priorities **(Chart 5.4a).** This was achieved through consistent issuance and reopening of medium to longer term Treasury bonds. Gross Treasury bonds issued during the year amounted KSh 788 billion, of which bond reopening, new bond issuance and infrastructure bonds accounted for 60 percent, 9 percent and 31 percent respectively. The T-bills to bonds ratio improved to 21:79 by end-June 2021 compared to 29:71 in June 2020 **(Chart 5.4b & 5.4c).**

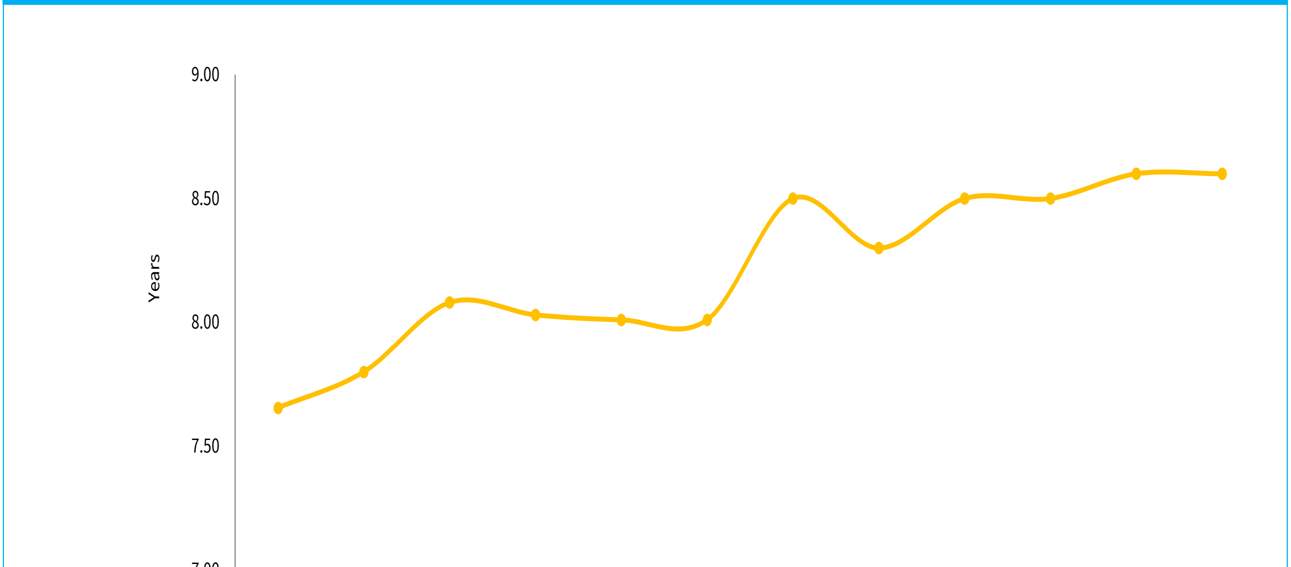
5.0 CENTRAL BANK OPERATIONS

Chart 5.3: Domestic Borrowing Programme in FY 2020-2021



Source: CBK

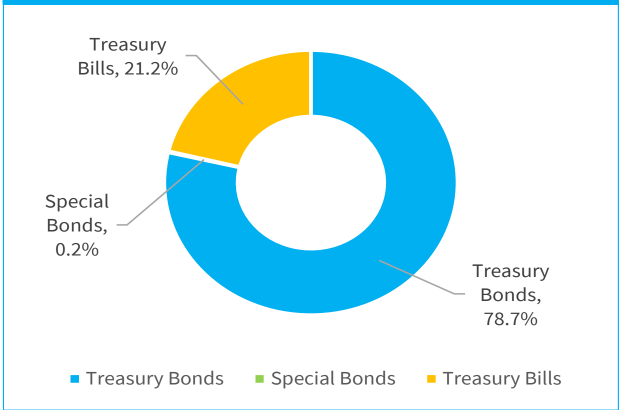
Chart 5.4a: Average Maturity (Years) of Treasury Bonds



	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21
ATM*-T.bonds (Years)	7.65	7.80	8.08	8.03	8.01	8.01	8.50	8.30	8.50	8.50	8.60	8.60

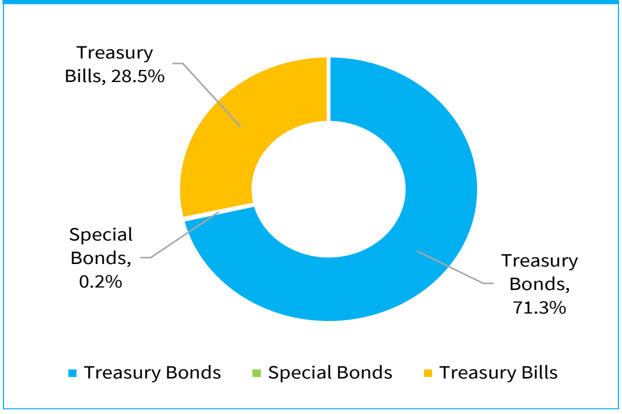
Source: CBK

Chart 5.4b: Government Securities Stock by Instrument, June 2021



Source: CBK

Chart 5.4c: Government Securities Stock by Instrument, June 2020

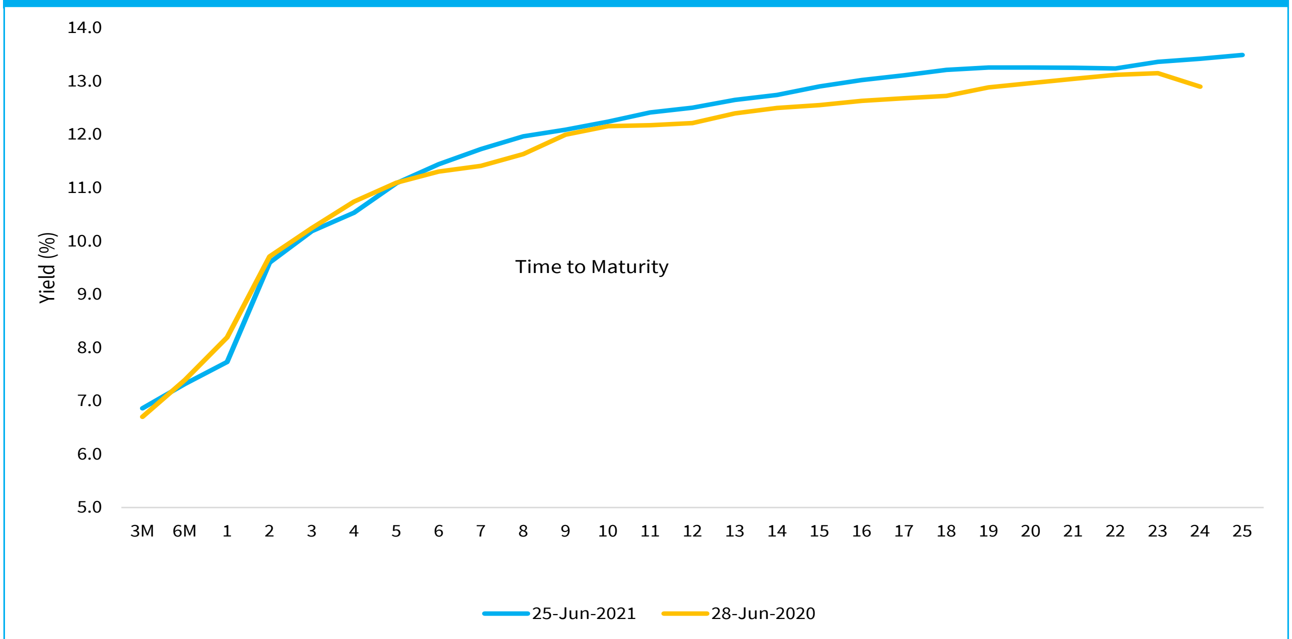


Source: CBK

Sustained Yield Curve Stability

Issuance of large size bonds through re-opening of benchmark tenors continued to increase market liquidity, reduced bond fragmentation and helped maintain a well-priced stable yield curve **(Chart 5.5a).** T-bill interest rates were stable, declining steadily with narrowing spreads towards end-June 2021 **(Chart 5.5b).**

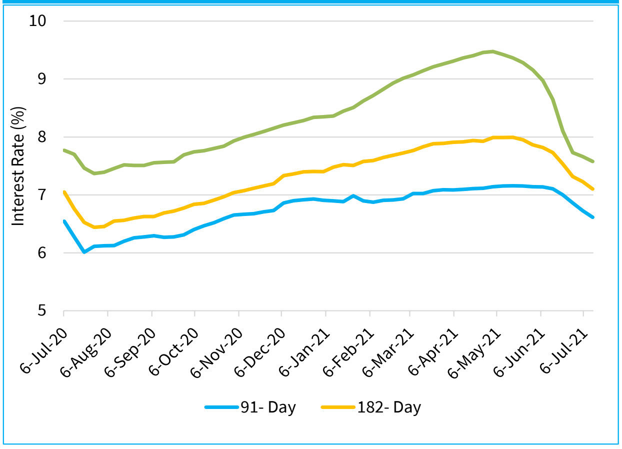
Chart 5.5a: Governtment Securities Yield Curve



Source: CBK

5.0 CENTRAL BANK OPERATIONS

Chart 5.5 b: Treasury Bills Interest Rates



Source: CBK

Central Securities Depository (CSD) System

To enhance efficiency of domestic debt operations and to further develop the market, the Bank has embarked on implementation of a new Central Securities Depository (CSD) system as part of key market infrastructure. The system has the following advantages: Firstly, the CSD system is envisioned to play a crucial role in monetary policy implementation and to promote public interest, financial stability and financial market development.

Secondly, the system is expected to deliver excellent levels of registry, custodial and settlement services for both primary and secondary market operations. In this case, the system is envisioned to improve market liquidity distribution, enhance liability management strategies, promote capital market growth and position Kenya as the preferred financial hub in the region.

Thirdly, the system will have the capacity to provide electronic registry for all Government and CBK securities which will meet the needs of all issuers, holders, asset managers and other interested parties.

The project implementation is on course and is expected to be completed in May 2022.

6.0 STRATEGIC PLAN 2021-2024

6.0 STRATEGIC PLAN 2021-2024

The milestones that were achieved during the 2018-21 strategy period set the stage for the 2021-24 strategic plan to move the Bank closer to the realisation of its vision of being a ***World Class and Modern Central Bank.***

The strategic initiatives that will drive the realisation of the 2021-24 Strategic Objectives are grouped in to four broad areas namely: ***Automation, People and Culture, Risk Management and Operational Excellence.***

Automation:

During this strategy period, and building on the enhanced information technology infrastructure, the Bank will undertake upgrade of a number of its operating systems and review processes. The systems / applications that are to be enhanced or installed include the integration of the Enhanced Data Warehouse (EDW) with financial institutions data submission systems; the upgrade of the Core Banking system; the upgrade of the Enterprise Resource Planning application, the adoption of a new Debt Management system; the installation of an integrated reserves management system; and the automation of Communication and Legal services operations. This will be accompanied by a review of the operating policies, procedures and manuals.

People and Culture:

Staff remain the most critical resource the Bank takes prides in. To consolidate gains recorded in the previous planning period, the Bank will finalise the ongoing human resource transformation initiatives. The adoption and application of the revised staff rules and regulations should facilitate timely and amicable resolution of any issues that may arise as a result of the ongoing HR transformation exercise. Staff development will remain a focus area to enhance skills and competencies to cope with emerging work demands. The Bank will also entrench a culture that promotes productivity which will facilitate the achievement of the strategic objectives.

Risk Management:

Internally, the Bank will continue improving its control environment so as to mitigate risks while ensuring that operations flow seamlessly. A risk aware culture in regards to operations and information technology will be enhanced. Jurisprudence in matters relevant to the Bank will be expanded for institutional memory and future reference. Additionally, the Bank will work towards enhancing its capital base in line with its operations.

Externally, the Bank commits to mitigating and managing risk in the banking and financial sector in general through legislation and effective oversight of participants. Specifically, the legal framework on payment systems will be revised to manage revolutions witnessed in the recent past and prepare for the future. Oversight will be extended to cover digital credit and consumer protection. Guidelines to govern the conduct of players in the foreign exchange market will also be developed.

Operational Excellence:

Successful implementation of the Bank's mandate is dependent on efficiencies of internal processes and effective governance structures. In its pursuit to becoming World Class and Modern, the Bank will endeavour to improve its efficiency and effectiveness in various areas such as entrenching a modern monetary policy framework and enhancing data availability and analysis to inform policy; service delivery to both internal and external stakeholders to positively impact on their experiences and satisfaction; enhancing internal and external communication and upgrading security surveillance to Bank premises. The provision of modern and fit for purpose physical infrastructure will greatly enhance the working environment.

7.0 FINANCIAL PERFORMANCE FOR THE YEAR ENDED JUNE 2021

REPUBLIC OF KENYA

OFFICE OF THE AUDITOR-GENERAL

Enhancing Accountability

REPORT

OF

THE AUDITOR-GENERAL

ON

CENTRAL BANK OF KENYA

FOR THE YEAR ENDED
30 JUNE, 2021

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BANK INFORMATION
FOR THE YEAR ENDED 30 JUNE 2021

BOARD OF DIRECTORS

Mr. Mohammed Nyaoga	Chairman
Dr. Patrick Njoroge	Governor
Dr. Julius Muia	Principal Secretary, The National Treasury
Mr. Samson Cherutich	Member –(Reappointed on 5 December, 2020)
Mrs. Nelius W. Kariuki	Member –(Reappointed on 5 December, 2020)
Mrs. Rachel Dzombo	Member – (Reappointed on 5 December, 2020)
Mr. Ravi J. Ruparel	Member - (Reappointed on 5 December, 2020)

SENIOR MANAGEMENT

Dr. Patrick Njoroge	Governor
Mrs. Sheila M'Mbijjewe	Deputy Governor

HEADS OF DEPARTMENT

Mr. Kennedy Abuga	Director – Governor's Office (Board Secretary)
Mr. William Nyagaka	Director - Kenya School of Monetary Studies
Mr. David Luusa	Director - Financial Markets Department
Mr. Gerald Nyaoma	Director - Bank Supervision Department
Mr. Antony Gacanja	Director - Information Technology Department
Mr. Stephen Muriu	Director - General Services Department
Ms. Darliah M. Mbugua	Director - Human Resource and Administration Department- (Appointed on 1 September 2020)
Mr. Michael Rundu Eganza	Director - Banking, National Payments Department- (Appointed on 4 January 2021)
Ms. Caroline Mackola	Director - Finance Department – (Appointed on 22 February 2021)
Ms. Beth Kithinji	Director - Internal Audit Department and Risk Management Department – (Appointed on 11 May 2021)
Prof. Robert Mudida	Director - Research Department - (Appointed on 1 July 2021)
Ms. Terry Nganga	Acting Director - Human Resource and Administration Department – (Until 30 August 2020)
Mr. Paul Wanyagi	Acting Director - Currency Operations and Branch Administration Department
Mr. Mwenda Marete	Acting Director - Banking, National Payments Department – (Until 3 January 2021)
Mr. Moses Ngotho	Acting Director - Finance Department – (Until 21 February 2021)
Mr. Raphael Otieno	Acting Director - Research Department - (Until 30 June 2021)
Mrs. Matilda Onyango	Acting Director - Internal Audit Department and Risk Management Department – (Retired on 10 May 2021)
Mr. Patrice Odude	Acting Director- Strategic Management Department - (Retired on 12 July, 2021)

REGISTERED OFFICE AND PRINCIPAL PLACE OF BUSINESS
Central Bank of Kenya Building
Haile Selassie Avenue
P.O. Box 60000
00200 Nairobi, Kenya
Tel.(+254) (020) 2860000

BRANCHES

Mombasa Branch	Kisumu Branch	Eldoret Branch
Central Bank of Kenya Building	Central Bank of Kenya Building	Kiptagich House
Nkrumah Road	Jomo Kenyatta Highway	Uganda Road
P.O. Box 86372	P.O. Box 4	P.O. Box 2710
80100 Mombasa	40100 Kisumu	30100 Eldoret

BANK INFORMATION (continued)
FOR THE YEAR ENDED 30 JUNE 2021

CENTRAL BANK CENTRES

Nyeri Centre
Kenya Commercial Bank Building
Kenyatta Street
P.O. Box 840
10100 Nyeri

Meru Centre
Co-operative Bank Building
Njuri Ncheke Street
P.O. Box 2171
60200 Meru

Nakuru Centre
Kenya Commercial Bank Building
George Morara Street
P.O. Box 14094
20100 Nakuru

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ABSA Bank Building
Sotik Road
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Amolo & Gacoka Advocates.
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Nairobi

PRINCIPAL AUDITOR

The Auditor – General
Anniversary Towers
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00100 Nairobi

DELEGATED AUDITOR

Ernst & Young LLP
Kenya-Re Towers, Upper Hill, Off Ragati Road
P.O. Box 44286
00100 Nairobi

STATEMENT OF CORPORATE GOVERNANCE FOR THE YEAR ENDED 30 JUNE 2021

1.0 Statement of Corporate Governance

The Central Bank of Kenya (the "Bank"/"CBK") is wholly owned by the Government of Kenya. The Bank is established by and derives its authority and accountability from Article 231 of the Constitution of Kenya. The Bank is committed to maintaining the highest standards of integrity, professionalism and ethics in all its operations.

1.1 Board of Directors

The Central Bank of Kenya Act (the "Act") provides that the Board of Directors (the "Board") shall be composed of a Chairperson, a Governor, Principal Secretary to The National Treasury who is a non-voting member and eight Non-Executive Directors. The law requires that the President appoints the Chairman and Governor after a competitive process and approval of Parliament. Other than the Principal Secretary to The National Treasury who is an ex-officio member, all the Non-Executive Directors of the Board are also appointed by the President with the approval of Parliament. All the Board members are appointed for a term of four (4) years each and are eligible for reappointment for a term of four (4) years provided that no Board member holds office for more than two (2) terms.

All the Non-Executive Directors are independent of management and free from any business or other relationship, which could interfere with the exercise of their independent oversight.

The Board meets once every two (2) months and has a formal schedule of agenda items due for deliberations. The Directors are given appropriate and timely information to enable them to provide and maintain full and effective direction and control over strategic, financial and operational issues of the Bank. The Board is not involved in the conduct of day-to-day business as this is the responsibility given to the Governor by law. It however, retains the responsibility of approving the policies of the Bank.

The table below shows the Board of Directors' appointment dates and contract end dates.

No.	Name	Position	Discipline	Date of Appointment	Contract end date
1.	Mr. Mohammed Nyaoga	Chairman	Lawyer	Reappointed on 18 June 2019	17 June 2023
2.	Dr. Patrick Njoroge	Governor	Economist	Reappointed on 18 June 2019	17 June 2023
3.	Principal Secretary/ The National Treasury	Executive Officer	Economist	Permanent	Permanent
4.	Mrs. Nelius Kariuki	Member	Economist	Reappointed on 5 December 2020	4 December 2024
5.	Mr. Ravi Ruparel	Member	Financial Sector Expert	Reappointed on 5 December 2020	4 December 2024
6.	Mr. Samson Cherutich	Member	Accountant	Reappointed on 5 December 2020	4 December 2024
7.	Mrs. Rachel Dzombo	Member	Management Expert	Reappointed on 5 December 2020	4 December 2024

STATEMENT OF CORPORATE GOVERNANCE (continued)
FOR THE YEAR ENDED 30 JUNE 2021

The Members of the Board (all Kenyans) in the year ended 30 June 2021 and their attendance and the number of meetings held in the year were as follows:

No.	Name	Position	Discipline	Meetings Attended
1.	Mr. Mohammed Nyaoga	Chairman	Lawyer	9
2.	Dr. Patrick Njoroge	Governor	Economist	9
3.	Principal Secretary/ The National Treasury	Executive Officer	Economist	8
4.	Mrs. Nelius Kariuki	Member	Economist	9
5.	Mr. Ravi Ruparel	Member	Financial Sector Expert	9
6.	Mr. Samson Cherutich	Member	Accountant	9
7.	Mrs. Rachel Dzombo	Member	Management Expert	9

The remuneration paid to the Directors for services rendered during the financial year 2020/2021 is disclosed in Note 29 to the financial statements. The Non-Executive Directors are paid a monthly retainer fee and a sitting allowance for every meeting attended. There were no loans to Non-Executive Directors during the year while Executive Directors are paid a monthly salary and are eligible for staff loans.

1.2. Secretary to the Board

The Board Secretary provides technical and secretarial services as well as corporate governance and logistical support to the Board. He facilitates efficient policy making interface with policy implementation. The Board Secretary also advises the Board on legal matters. In conjunction with the Chairman, the Board Secretary ensures good and timely information flow among the Board members, the Board Committees and Management. All members of the Board and Management have access to the Board Secretariat services.

1.3. Audit Committee

The members of the Audit Committee in the year ended 30 June 2021 were Mr. Samson K. Cherutich (Chairman), Mr. Ravi J. Ruparel, Mrs. Nelius W. Kariuki and Mrs. Rachel Dzombo. The members are all Non-Executive Directors with experience in Accounting, Auditing, Finance and Management. The Committee meets once every two (2) months and as necessary. The Terms of Reference of the Audit Committee cover five (5) major areas, namely: Internal Control System, Risk Management, Financial Reporting and Related Reporting Practices, External and Internal Audits.

The Audit Committee's mandate, under Internal Control, includes ensuring that internal control and risk management is planned, structured and implemented at the Bank. The Committee also ensures that internal and external audit recommendations are implemented.

The mandate relating to Financial Reporting and Related Reporting Practices requires the Audit Committee to review the annual financial statements of the Bank, the external auditor's opinion and their comments on internal controls and other observations. The Committee also reviews significant accounting and reporting issues and their impact on financial reports and legal matters that could significantly impact on the financial statements, among other financial reporting responsibilities.

With regard to External Audit, the Audit Committee reviews the external auditor's proposed audit scope, approach and audit deliverables, and reviews the financial statements before submission to the Board for consideration and approval.

STATEMENT OF CORPORATE GOVERNANCE (continued)
FOR THE YEAR ENDED 30 JUNE 2021

The Committee's mandate on Internal Audit covers review of the activities and resources of the internal audit function, including the effectiveness, standing and independence of the internal audit function within the Bank. It also covers review of the internal audit plan and follow up of the implementation of internal audit findings and recommendations. The Audit Committee reports to the Board of Directors on the standing and independence of the internal audit function within the Bank. The Audit Committee also reports to the Board of Directors on internal audit scope, approach and deliverables.

The Committee Members' positions, disciplines and number of meetings attended for the year ended 30 June 2021 were as follows:

No.	Name	Position	Discipline	Meetings Attended
1.	Mr. Samson Cherutich	Chairman	Accountant	10
2.	Mr. Ravi Ruparel	Member	Financial Sector Expert	10
3.	Mrs. Nelius Kariuki	Member	Economist	10
4.	Mrs. Rachel Dzombo	Member	Management Expert	10

1.4. Human Resources Committee (HRC)

The members of the HRC in the year ended 30 June 2021 were Mrs. Nelius Kariuki (Chairman), Mr. Samson Cherutich, Mrs. Rachel Dzombo and Mr. Ravi Ruparel. The members are all Non-Executive Directors with experience in Accounting, Management and Business.

The HRC of the Board performs an advisory role to the Bank's Board in the fulfilment of the following oversight responsibilities:

a) Monitor the formulation and implementation of Human Resources Policies in the Bank;
b) In relation to staff matters, they ensure the Bank's compliance with the Kenyan Constitution, Laws of Kenya, CBK regulations and its own code of conduct;
c) Perform any other Human Resources related functions as assigned by the Board.
d) Monitor the implementation of Board resolutions relating to the HRC of the Board.

The goal of the committee is to drive the HR function at the Bank to attain best in class global standards.

The members of the Human Resources Committee in the year ended 30 June 2021 and their attendance of the meetings held in the year were as follows:

No.	Name	Position	Discipline	Meetings Attended
1.	Mrs. Nelius Kariuki	Chairman	Economist	6
2.	Mr. Samson Cherutich	Member	Accountant	6
3.	Mrs Rachel Dzombo	Member	Management Expert	6
4.	Mr. Ravi Ruparel	Member	Financial Sector Expert	6

1.5. Monetary Policy Committee (MPC)

Section 4D of the Central Bank of Kenya (Amendment) Act 2008 establishes the Monetary Policy Committee (MPC). The MPC is responsible for formulating monetary policy and is required to meet at least once every two (2) months. The MPC comprises the:

STATEMENT OF CORPORATE GOVERNANCE (continued) FOR THE YEAR ENDED 30 JUNE 2021

i) Governor who is the Chairman
ii) The Deputy Governor who is the Deputy Chairperson
iii) Two (2) members appointed by the Governor from the CBK. Of the two members:
   a) one shall be a person with executive responsibility within the Bank for monetary analyses and;
   b) one shall be a person with responsibility within the Bank for monetary policy operations.
iv) Four (4) external members appointed by the Cabinet Secretary for The National Treasury
v) Principal Secretary for the National Treasury or his Representative

External members of the MPC are appointed for an initial period of three (3) years each and may be reappointed for another final term of three (3) years. The quorum for MPC meetings is five (5) members, one of whom must be the Chairman or Deputy Chairperson.

The MPC held six (6) meetings in the year ended 30 June 2021, and attendance was as follows:

No.	Name	Position	Discipline	Meetings Attended
1.	Dr. Patrick Njoroge	Chairman	Economist	6
2.	Mrs. Sheila M'Mbijjewe	Deputy Chairperson	Finance/ Accountancy	6
3.	Dr. Margaret Chemengich	Member (External)	Economist	6
4.	Prof. Jane Kabubo-Mariara	Member (External)	Economist	6
5.	Dr. Benson Ateng'	Member (External)	Economist	6
6.	Mr. Humphrey Muga	Member (External)	Economist	6
7.	Mr. Musa Kathanje	Representative of the Principal Secretary, The National Treasury	Economist	6
8.	Mr. David Luusa	Member (Internal)	Economist	6
9.	Mr. Raphael Otieno	Member (Internal)	Economist	6

1.6. Management Structure

The positions of Governor and Deputy Governor are set out in the CBK Act Cap 491 of the Laws of Kenya. The Governor and the Deputy Governor constitute the Central Bank's Senior Management. As the Chief Executive of the Bank, the Governor assigns duties to the Deputy Governor.

There are 13 Directors who head up the key departments of the Central Bank, using structure, oversight, governance and control of the key areas. Senior Management and departmental heads have frequent meetings in the running of the Bank, many of these meetings are organised in structured frameworks to ensure clarity, transparency and success of the outcomes.

1.7. Code of Ethics

The Bank is committed to the highest standards of integrity, behaviour and ethics. A formal code of ethics for all employees has been approved by the Board and is fully implemented. All employees of the Bank are expected to avoid activities and financial interests, which could give rise to conflict of interest with their responsibilities in the Bank. Strict rules of conduct embedded in the *Staff Rules and Regulations and the Employment Act 2007* apply to the entire Bank's staff.

1.8. Internal Controls

The Management of the Bank has put in place a system of internal control mechanisms to ensure the reporting of complete and accurate

STATEMENT OF CORPORATE GOVERNANCE (continued)
FOR THE YEAR ENDED 30 JUNE 2021

accounting information. Procurement of goods and services is strictly done in accordance with the *Public Procurement & Disposal Act, 2015 and Regulations, 2020.* In all operational areas of the Bank, workflows have been structured in a manner that allows adequate segregation of duties.

1.9. Authorizations

All the expenditure of the Bank must be authorized in accordance with a comprehensive set of the Bank policies and procedures. There is an annual Budget approved by the Board and a Procurement Plan approved by the Senior Management before commencement of the financial year. The Board of Directors receives regular management accounts comparing actual outcomes against budget as a means of monitoring actual financial performance of the Bank.

1.10. Internal Audit and Risk Management

The internal audit function and risk oversight is performed by Internal Audit Department. The department is responsible for monitoring and providing advice on the Bank's risk and audit framework. All reports of Internal Audit Department and Risk Management Unit are availed to the Audit Committee of the Board.

1.11. Transparency

The Bank publishes an Annual Report, Monthly Economic Review, Weekly Releases, Statistical Bulletin and Bi-annual Monetary Policy Statements. In addition, the Bank issues policy briefs to The National Treasury on both the Monetary and Fiscal policies. On an annual basis, the Financial Statements of the Bank are published in the Kenya Gazette and placed in the Bank's website.

2.0 Financial Performance

The Bank's financial performance is primarily affected by the Monetary Policy stance adopted, interest rates and changes in exchange rate. The Bank's financial performance is presented on page 52 of these financial statements.

During financial year ended 30 June 2021, the Bank recorded a net surplus of KShs 36,993 million compared to KShs 41,530 million in financial year ended 30 June 2020. The surplus is included as part of the General Reserve Fund.

During the financial year ended 30 June 2021, the Bank's operating surplus was KShs 11,723 million (2020: KShs 17,055 million) due to lower rates offered on foreign deposit placements and the one-off gain on demonization of old currency that was realised in the prior year. An unrealised foreign exchange gain of KShs 25,270 million was recorded during the year ended 30 June 2021 (2020: KShs 24,475 million) due to the strengthening of the USD. The Bank also recorded a fair value loss on fixed income securities of KShs 6,321 million (2020: gain of KShs 8,452 million) as a result of a decline in market prices. The loss recorded during the year has been presented in other comprehensive income.

In addition, an actuarial gain on retirement benefit asset of KShs 676 million (2020: gain of KShs 1,949 million) was also earned. There was an overall revaluation increase of KShs 1,319 million on land and buildings recorded during the year in the consolidated statement of comprehensive income. This valuation is performed every 3 years in line with the Bank's Fixed assets management policy.

The Bank's assets increased to KShs 1,449,056 million (2020: KShs 1,350,434 million) mainly attributed to increase in funds on lent to the Government of Kenya from the International Monetary Fund and net inflows from banking institutions. Liabilities increased to KShs 1,232,562 million (2020: KShs 1,154,419 million) mainly due to from the International Monetary Fund.

REPORT OF THE DIRECTORS
FOR THE YEAR ENDED 30 JUNE 2021

The Directors submit their report together with the audited financial statements for the year ended 30 June 2021, which shows performance of the Bank during the year and the state of affairs of Central Bank of Kenya (the "Bank"/" CBK") as at the year end.

1. INCORPORATION

The Bank is incorporated by Article 231 of the Constitution of Kenya, 2010.

2. PRINCIPAL ACTIVITIES

The Bank is established and administered under the Constitution of Kenya, 2010 with the principal object of formulating and implementing monetary policy directed at achieving and maintaining stability in the general level of prices. It is also the responsibility of the Bank to foster liquidity, solvency and proper functioning of a stable market-based financial system. The Bank also acts as banker, advisor and fiscal agent of the Government of Kenya.

3. RESULTS AND SURPLUS

The surplus for the year was KShs 36,993 million (2020: KShs 41,530 million) made up of KShs 11,723 million (2020: KShs 17,055 million) realized surplus and KShs 25,270 million (2020: KShs 24,475 million) unrealized surplus. In 2020 the Bank had an exceptional realized gain of KShs 7.4 billion in respect of a demonetization exercise carried out in the year. The surplus has been included as part of the General Reserve Fund. The directors recommended an exceptional transfer of operational surplus in the year to 30 June 2021 of KShs 5,000 million on 12 February 2021. The directors further recommend a final transfer of operational surplus in the year to 30 June 2021 of KShs 5,500 million (2020: KShs 2,500 million) to the Consolidated Fund.

4. BOARD OF DIRECTORS

The members of the Board of Directors who served during the year and up to the date of this report are listed on page 40.

5. AUDITOR

The Auditor - General is responsible for the statutory audit of the Bank's Financial Statements in accordance with Section 35 of the Public Audit Act, 2015. Section 23(1) of the Act empowers the Auditor-General to appoint other auditors to carry out the audit on his behalf. Accordingly, Ernst & Young LLP were appointed to carry out the audit for the year ended 30 June 2021 and report to the Auditor - General. However, Ernst & Young LLP have audited the Bank for three years and are due for rotation after 30 June 2021.

By Order of the Board

Kennedy Abuga
Board Secretary

3 September 2021

STATEMENT OF DIRECTORS' RESPONSIBILITIES
FOR THE YEAR ENDED 30 JUNE 2021

The Directors are responsible for the preparation of financial statements for each financial year that give a true and fair view of the state of affairs of the Bank as at the end of the financial year and of the Bank's financial performance. The Directors also ensure that the Bank keeps proper accounting records that disclose, with reasonable accuracy, the financial position of the Bank. They are also responsible for safeguarding the assets of the Bank.

The Directors accept responsibility for the preparation and fair presentation of financial statements that are free from material misstatements whether due to fraud or error. They also accept responsibility for:

(i) Designing, implementing and maintaining internal control necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error;

(ii) Selecting and applying appropriate accounting policies; and

(iii)Making accounting estimates and judgments that are reasonable in the circumstances.

The Directors are of the opinion that the financial statements give a true and fair view of the state of the financial position of the Bank as at 30 June 2021 and of the Bank's financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards and the requirements of the *Central Bank of Kenya Act.*

These financial statements are prepared on a going concern basis, taking into account the legal mandate and responsibilities of the Bank, in particular is monetary policy, financial stability and payment system leadership.

Approved by the Board of Directors and signed on its behalf by:

Chairman, Board of Directors
Mr. Mohammed Nyaoga

3 September 2021

Patrick Njoroge

Governor
Dr. Patrick Njoroge

3 September 2021

REPUBLIC OF KENYA

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OFFICE OF THE AUDITOR-GENERAL

Enhancing Accountability

HEADQUARTERS
Anniversary Towers
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NAIROBI

REPORT OF THE AUDITOR-GENERAL ON CENTRAL BANK OF KENYA FOR THE YEAR ENDED 30 JUNE, 2021

PREAMBLE

I draw your attention to the contents of my report which is in three parts:

A. Report on the financial statements that considers whether the financial statements are fairly presented in accordance with the applicable financial reporting framework, accounting standards and the relevant laws and regulations that have a direct effect on the financial statements.

B. Report on Lawfulness and Effectiveness in use of public resources which considers compliance with applicable laws, regulations, policies, gazetted notices, circulars, guidelines and manuals and whether public resources are applied in a prudent, efficient, economic, transparent and accountable manner to ensure government achieves value for money and that such funds are applied for intended purpose.

C. Report on Effectiveness of Internal Controls, Risk Management and Governance which considers how the entity has instituted checks and balances to guide internal operations. This responds to the effectiveness of the governance structure, the risk management environment, and the internal controls developed and implemented by those charged with governance for orderly, efficient and effective operations of the entity.

An unmodified opinion does not necessarily mean that an entity has complied with all relevant laws and regulations, and that its internal control, risk management and governance systems are properly designed and were working effectively in the financial year under review.

The three parts of the report are aimed at addressing the statutory roles and responsibilities of the Auditor-General as provided by Article 229 of the Constitution and the Public Audit Act, 2015. The three parts of the report, when read together constitute the report of the Auditor-General.

REPORT ON THE FINANCIAL STATEMENTS

Opinion

The accompanying consolidated financial statements of Central Bank of Kenya set out on pages **55 to 131**,which comprise the consolidated statement of financial position as at 30 June, 2021, and the consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information have been audited on my behalf by Ernst and Young LLP auditors appointed under Section 23 of the Public Audit Act, 2015 and in accordance with the provisions of Article 229 of the Constitution of Kenya. The auditors have duly reported to me the results of their audit and on the basis of their report, I am satisfied that all the information and explanations which, to the best of my knowledge and belief, were necessary for the purpose of the audit were obtained.

In my opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of the Central Bank of Kenya as at 30 June, 2021, and of its consolidated financial performance and its consolidated cash flows for the year then ended, in accordance with International Financial Reporting Standards (IFRSs) and comply with the Central Bank of Kenya Act, Cap 491 of the Laws of Kenya and the Public Finance Management Act, 2012.

Basis for Opinion

The audit was conducted in accordance with International Standards of Supreme Audit Institutions (ISSAIs). I am independent of the Central Bank of Kenya Management in accordance with ISSAI 130 on Code of Ethics. I have fulfilled other ethical responsibilities in accordance with the ISSAI and in accordance with other ethical requirements applicable to performing audits of financial statements in Kenya. I believe that the audit evidence obtained is sufficient and appropriate to provide a basis for my opinion.

Key Audit Matters

Key audit matters are those matters that, in my professional judgement, are of most significance in the audit of the financial statements. There were no key audit matters to report in the year under review.

Other Matter

1. Failure to Maintain the Required Number of Non-Executive Directors

As was reported in the previous year, the Central Bank Act, Cap 491 of 2014, Part IV - Management, Section 11(1)(d) provides that there shall be eight (8) other Non-Executive Directors of the Board. During the year under review, the Bank had in place four (4) Non-Executive Directors transacting business on its behalf. There was no amendment to the Central Bank Act to provide for reduction in the number of Directors.

2. Lack of the Second Deputy Governor

In addition, the Central Bank of Kenya Act, Cap 491 Section 13B(1) states that, "There shall be two Deputy Governors who shall be appointed by the President through a transparent and competitive process and with the approval of Parliament". During the year under review, only one Deputy Governor was in office. There was no amendment to the Central Bank Act to provide for reduction in the number of Deputy Governors.

Other Information

The Directors are responsible for the other information, which comprises the Statement of Corporate Governance, Directors' Report and the Statement of

Directors' Responsibilities. The other information does not include the financial statements and my auditor's report thereon.

My opinion on the consolidated financial statements does not cover the other information and I do not express any form of assurance or conclusion thereon.

REPORT ON LAWFULNESS AND EFFECTIVENESS IN USE OF PUBLIC RESOURCES

Conclusion

As required by Article 229(6) of the Constitution, based on the audit procedures performed, I confirm that, nothing has come to my attention to cause me to believe that public money has not been applied lawfully and in an effective way.

Basis for Conclusion

The audit was conducted in accordance with ISSAI 4000. The standard requires that I comply with ethical requirements and plan and perform the audit to obtain assurance about whether the activities, financial transactions and information reflected in the financial statements are in compliance, in all material respects, with the authorities that govern them. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

REPORT ON EFFECTIVENESS OF INTERNAL CONTROLS, RISK MANAGEMENT AND GOVERNANCE

Conclusion

As required by Section 7(1)(a) of the Public Audit Act, 2015, based on the audit procedures performed, except for the matter described in the Basis for Conclusion on Effectiveness of Internal Controls, Risk Management and Governance section of my report, I confirm that, nothing else has come to my attention to cause me to believe that internal controls, risk management and overall governance were not effective.

Basis for Conclusion

Delayed Winding up of the Kenya School of Monetary Studies (KSMS)

I draw attention to Note 29(vi) to the financial statements which states that the Kenya School of Monetary Studies, (KSMS) is a subsidiary of the Bank, owned and managed by the Bank. In accordance with Article 29 of the Memorandum and Articles of Association, the number of Directors should not be less than three (3) or more than ten (10) and should be appointed by the School in a General Meeting. For the last six (6) years, the School has existed without a functional Board of Directors and has been proposed for winding up. The dissolution of the School as a legal entity was Gazetted on 24 April, 2020. This was in an effort to address concerns regarding governance and internal controls at KSMS, and to align its objectives and financial reporting framework with that of CBK. However, as at the date of this report, KSMS had not been dissolved.

Consequently, it is critical that CBK Management follows up and expedites the conclusion of the dissolution process.

The audit was conducted in accordance with ISSAI 2315 and ISSAI 2330. The standards require that I plan and perform the audit to obtain assurance about whether effective processes and systems of internal control, risk management and governance were operating effectively. In all material respects, I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my conclusion.

Responsibilities of Management and the Board of Directors

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs), and for maintaining effective internal control as Management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error and for its assessment of the effectiveness of internal control.

In preparing the consolidated financial statements, Management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless Management is aware of the intention to liquidate the Bank or to cease operations.

Management is also responsible for submission of the financial statements to the Auditor-General in accordance with the provisions of Section 47 of the Public Audit Act, 2015.

In addition to the responsibility for the preparation and presentation of the financial statements described above, Management is also responsible for ensuring that the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities which govern them, and that public resources are applied in an effective manner.

Those charged with governance are responsible for overseeing the financial reporting process, reviewing the effectiveness of how the bank monitors compliance with relevant legislative and regulatory requirements, ensuring that effective processes and systems are in place to address key roles and responsibilities in relation to governance and risk management, and ensuring the adequacy and effectiveness of the control environment.

Auditor-General's Responsibilities for the Audit

The audit objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion in accordance with the provisions of Section 48 of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISSAIs will always detect a material misstatement and weakness when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

In addition to the audit of the financial statements, a compliance audit is planned and performed to express a conclusion about whether, in all material respects, the activities, financial transactions and information reflected in the financial statements are in compliance with the authorities that govern them in accordance with the provisions of Article 229(6) of the Constitution and submit the audit report in compliance with Article 229(7) of the Constitution.

Further, in planning and performing the audit of the financial statements and audit of compliance, I consider internal control in order to give an assurance on the effectiveness of internal controls, risk management and governance processes and systems in accordance with the provisions of Section 7(1)(a) of the Public Audit Act, 2015 and submit the audit report in compliance with Article 229(7) of the Constitution. My consideration of the internal control would not necessarily disclose all matters in internal control that might be material weaknesses under the ISSAIs. A material weakness is a condition in which the design or operation of one or more of the internal control components, does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Because of its inherent limitations, internal control may not prevent or detect misstatements and instances of non-compliance. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies and procedures may deteriorate.

As part of an audit conducted in accordance with ISSAIs, I exercise professional judgement and maintain professional scepticism throughout the audit. I also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Management.

- Conclude on the appropriateness of the Management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in the auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify my opinion. My conclusions are based on the audit evidence obtained up to the date of my audit report. However, future events or conditions may cause the Bank to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information and business activities of the Bank to express an opinion on the financial statements.

- Perform such other procedures as I consider necessary in the circumstances.

I communicate with the Management regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that are identified during the audit.

I also provide Management with a statement that I have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on my independence, and where applicable, related safeguards.

CPA Nancy Gathungu, CBS
AUDITOR-GENERAL

Nairobi

27 September, 2021

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 30 JUNE 2021

	Notes	2021 KShs' million	2020 KShs' million
Interest income	4	17,084	22,308
Interest expense	5	(2,026)	(4,618)
Net interest income		15,058	17,690
Fees and commission income	6(a)	3,000	3,000
Net trading income	6(b)	13,237	11,753
Other income	7(a)	1,044	982
Demonetization of old currency	7(b)	-	7,388
Operating income		32,339	40,813
Impairment allowance expense on financial assets	8	(4,333)	(8,627)
Operating expenses	9(a)	(16,283)	(15,131)
Operating surplus before unrealized gains		11,723	17,055
Unrealised gains:			
Foreign exchange gain		25,270	24,475
Surplus for the year		36,993	41,530
Other comprehensive income:			
Items that are or may be subsequently reclassified to profit or loss:			
Debt instruments at fair value through other comprehensive income:			
Net change in fair value during the year	10(a)	(6,321)	8,452
Reclassification to income statement	10(b)	(7,329)	(3,020)
Changes in Impairment allowance	8	81	17
		(13,569)	5,449
Items that will not be reclassified to profit or loss:			
Land and building revaluation increase	18(b)	3,879	-
Actuarial gain on retirement benefit asset	20	676	1,949
		4,555	1,949
Other comprehensive income for the year		(9,014)	7,398
Total comprehensive income for the year		27,979	48,928

CONSOLIDATED STATEMENT OF FINANCIAL POSITION
AS AT 30 JUNE 2021

	Notes	2021 KShs' million	2020 KShs' million
ASSETS			
Balances due from banking institutions	11	430,968	369,505
Funds held with International Monetary Fund (IMF)	12(a)	2,201	3,255
Securities and advances to banks	13	59,540	55,561
Loans and advances	14	3,131	3,274
Debt instruments at fair value through other comprehensive income	15	664,991	724,892
Equity instruments at fair value through other comprehensive income	16	10	10
Other assets	17(a)	5,541	5,595
Gold holdings	17(b)	106	106
Right-of-use assets	18(a)	114	222
Property and equipment	18(b)	33,105	31,618
Intangible assets	19	1,784	1,224
Retirement benefit asset	20	7,639	6,537
IMF On-Lent to Government of Kenya (GOK)	21(a)	160,638	79,702
Due from Government of Kenya	21(b)	79,288	68,933
TOTAL ASSETS		1,449,056	1,350,434
LIABILITIES			
Currency in circulation	22	277,129	257,792
Investment by banks	23	-	6,997
Deposits from Banks and Government	24	728,001	732,187
Due to IMF	12(b)	221,174	151,841
Other liabilities	25	6,258	5,602
TOTAL LIABILITIES		1,232,562	1,154,419
EQUITY			
Share capital	26(a)	35,000	35,000
General reserve fund	26(b)	155,368	128,199
Fair value reserve	26(c)	(1,054)	12,515
Revaluation reserve	26(d)	21,680	17,801
Consolidated fund	26(e)	5,500	2,500
TOTAL EQUITY		216,494	196,015
TOTAL LIABILITIES AND EQUITY		1,449,056	1,350,434

The financial statements were authorised for issue by the Board of Directors on 3 September 2021 and signed on its behalf by:

Chairman of the Board
Mr. Mohammed Nyaoga

Patrick Njoroge
Governor
Dr. Patrick Njoroge

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 30 JUNE 2021

Year ended 30 June 2021	Notes	Share Capital KShs' million	General Reserve KShs' million	Revaluation Reserve KShs' million	Fair value Reserve KShs' million	Consolidated Fund KShs' million	Total KShs' million
At 1 July 2020		35,000	128,199	17,801	12,515	2,500	196,015
Surplus for the year		-	36,993	-	-	-	36,993
Net change in fair value of debt instrument at FVOCI		-	-	-	(6,321)	-	(6,321)
Net amount reclassified to the income statement on sale and maturity of debt instruments at FVOCI		-	-	-	(7,329)	-	(7,329)
Net change in Impairment allowance on debt instruments at FVOCI		-	-	-	81	-	81
Revaluation gain	18(b)	-	-	3,879	-	-	3,879
Actuarial gain on retirement benefit asset	20	-	676	-	-	-	676
Total comprehensive income for the year		-	37,669	3,879	(13,569)	-	27,979
Transactions with owners							
-Transfer to consolidated fund	26(e)	-	(10,500)	-	-	10,500	-
-Payments out of consolidated fund	26(e)	-	-	-	-	(7,500)	(7,500)
At 30 June 2021		35,000	155,368	21,680	(1,054)	5,500	216,494

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (continued)
FOR THE YEAR ENDED 30 JUNE 2021

Year ended 30 June 2020	Notes	Share Capital KShs' million	General Reserve KShs' million	Revaluation Reserve KShs' million	Fair value Reserve KShs' million	Consolidated Fund KShs' million	Total KShs' million
At 1 July 2019		20,000	109,608	17,801	7,066	4,000	158,475
Surplus for the year		-	41,530	-	-	-	41,530
Net change in fair value of debt instrument at FVOCI		-	-	-	8,452	-	8,452
Net amount reclassified to the income statement on sale and maturity of debt instruments at FVOCI		-	-	-	(3,020)	-	(3,020)
Net change in Impairment allowance on debt instruments at FVOCI		-	-	-	17	-	17
Actuarial gain on retirement benefit asset	20	-	1,949	-	-	-	1,949
Total comprehensive income for the year		-	43,479	-	5,449	-	48,928
Additional share capital	26(a)	15,000	(15,000)	-	-	-	-
Transactions with owners							
-Transfer to consolidated fund	26(e)	-	(9,888)	-	-	9,888	-
-Payments out of consolidated fund	26(e)	-	-	-	-	(11,388)	(11,388)
At 30 June 2020		35,000	128,199	17,801	12,515	2,500	196,015

CONSOLIDATED STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 30 JUNE 2021

	Notes	2021 KShs' million	2020 KShs' million
OPERATING ACTIVITIES			
Cash used in operating activities	27	(65,484)	(43,555)
Interest received		17,084	22,308
Interest paid		(2,026)	(4,618)
Interest paid on lease liabilities	18(a)	(22)	(7)
Cash used in operating activities		(50,448)	(25,872)
INVESTING ACTIVITIES			
Purchase of property and equipment	18(b)	(2,884)	(3,394)
Purchase of intangible assets	19	(723)	(546)
Proceeds from disposal of property and equipment		12	64
Net change in debt instruments at fair value through other comprehensive income		40,478	(181,615)
Net change in securities and advances to banks		(18,102)	(31,979)
Net change in funds held with International Monetary Fund (IMF)		1,054	(2,247)
Net cash generated from/(used in) investing activities		19,835	(219,717)
FINANCING ACTIVITIES			
Payment of principal portion of lease liabilities	18(a)	(171)	(158)
Receipts from International Monetary Fund (IMF)	28(b)	77,190	79,702
Repayments to the International Monetary Fund (IMF)	28(b)	(7,894)	(11,634)
Net cash generated from financing activities		69,125	67,910
Net increase/(decrease) in cash and cash equivalents		38,512	(177,679)
Cash and cash equivalents at the beginning of the year		451,154	628,833
CASH AND CASH EQUIVALENTS AT THE END OF THE YEAR	28(a)	489,666	451,154

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 30 JUNE 2021

1. GENERAL INFORMATION

Central Bank of Kenya (the "Bank"/" CBK") is established under Article 231 of the Constitution of Kenya. The Central Bank of Kenya is responsible for formulating monetary policy, promoting price stability, the payment system and performing other functions conferred on it by the Act of Parliament. The Bank is wholly owned by the National Treasury. The Bank acts as banker, advisor and agent of the Government of Kenya.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of these Financial Statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

(a) Basis of preparation

The financial statements are prepared in compliance with International Financial Reporting Standards (IFRS). The measurement basis applied is the historical cost basis, except where otherwise stated in the accounting policies below. The financial statements are presented in Kenya Shillings (KShs), rounded to the nearest million.

(b) Changes in accounting policies and disclosures

New and amended standards and interpretations

The following amendments became effective during the period:

New standards or amendments	Effective for annual period beginning on or after
Definition of a Business (Amendments to IFRS 3)	1 January 2020
Interest Rate Benchmark Reform (Amendments to IFRS 9, IAS 39 and IFRS 7)	1 January 2020
Definition of Material (Amendments to IAS 1 and IAS 8)	1 January 2020
Amendments to References to Conceptual Framework in IFRS Standards	1 January 2020
COVID-19-Related Rent Concessions (Amendments to IFRS 16)	1 June 2020

These amendments and interpretations apply for the first time in the period, but do not have an impact on the financial statements of the Bank. Below are the new standards or amendments which affect the Bank:

COVID-19-Related Rent Concessions (Amendments to IFRS 16)

On May 28 2020, the IASB issued Covid-19-Related Rent Concessions - amendment to IFRS 16 Leases. The amendments provide relief to lessees from applying IFRS 16 guidance on lease modification accounting for rent concessions arising as a direct consequence of the Covid-19 pandemic. As a practical expedient, a lessee may elect not to assess whether a Covid-19 related rent concession from a lessor is a lease modification. A lessee that makes this election accounts for any change in lease payments resulting from the Covid-19 related rent concession the same way it would account for the change under IFRS 16, if the change were not a lease modification. The amendment applies to annual reporting periods beginning on or after 1 June 2020. Earlier application is permitted. This amendment had no significant impact on the financial statements of the Bank.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(b) Changes in accounting policies and disclosures (continued)

New and amended standards (continued)

Amendments to IAS 1 and IAS 8 Definition of Material

The amendments provide a new definition of material that states, "information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity." The amendments clarify that materiality will depend on the nature or magnitude of information, either individually or in combination with other information, in the context of the financial statements. A misstatement of information is material if it could reasonably be expected to influence decisions made by the primary users. These amendments had no significant impact on the Bank financial statements.

Conceptual Framework for Financial Reporting issued on 29 March 2018

The Conceptual Framework is not a standard, and none of the concepts contained therein override the concepts or requirements in any standard. The purpose of the Conceptual Framework is to assist the IASB in developing standards, to help preparers develop consistent accounting policies where there is no applicable standard in place and to assist all parties to understand and interpret the standards. This will affect those entities which developed their accounting policies based on the Conceptual Framework.

The revised Conceptual Framework includes some new concepts, updated definitions and recognition criteria for assets and liabilities and clarifies some important concepts. These amendments had no impact on the Bank.

Standards issued but not yet effective

The standards and interpretations that are issued, but not yet effective, up to the date of issuance of the Bank's financial statements are listed below:

New standards or amendments	Effective for annual period beginning on or after
Interest Rate Benchmark Reform – Phase 2 – Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16	1 January 2021
Covid-19-Related Rent Concessions beyond 30 June 2021 – Amendment to IFRS 16	1 April 2021
Reference to the Conceptual Framework (Amendments to IFRS 3)	1 January 2022
Property, Plant and Equipment: Proceeds before Intended Use (Amendments to IAS 16)	1 January 2022
Onerous Contracts Cost of Fulfilling a Contract (Amendments to IAS 37)	1 January 2022
AIP IFRS 1 First-time Adoption of International Financial Reporting Standards – Subsidiary as a first-time adopter	1 January 2022
AIP IFRS 9 Financial Instruments – Fees in the '10 per cent' test for derecognition of financial liabilities	1 January 2022
AIP IAS 41 Agriculture – Taxation in fair value measurements	1 January 2022
IFRS 17 Insurance Contracts	1 January 2023

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(b) Changes in accounting policies and disclosures (continued)

Standards issued but not yet effective (continued)

New standards or amendments	Effective for annual period beginning on or after
Classification of liabilities as current or non-current (Amendments to IAS 1)	1 January 2023
Definition of Accounting Estimates - Amendments to IAS 8	1 January 2023
Disclosure of Accounting Policies - Amendments to IAS 1 and IFRS Practice Statement 2	1 January 2023
Deferred Tax related to Assets and Liabilities arising from a Single Transaction – Amendments to IAS 12	1 January 2023
Sale or Contribution of Assets between an Investor and its Associate or Company (Amendments to IFRS 10 and IAS 28)	To be determined

The Bank has not early adopted any standards, interpretations or amendments that have been issued but are not yet effective. The following standards and interpretations are expected to affect the Bank financial statements when they become effective.

Amendments to IAS 1: Classification of Liabilities as Current or Non-current
In January 2020, the IASB issued amendments to paragraphs 69 to 76 of IAS 1 to specify the requirements for classifying liabilities as current or non-current. The amendments clarify:

- What is meant by a right to defer settlement
- That a right to defer must exist at the end of the reporting period
- That classification is unaffected by the likelihood that an entity will exercise its deferral right
- That only if an embedded derivative in a convertible liability is itself an equity instrument would the terms of a liability not impact its classification

The amendments are effective for annual reporting periods beginning on or after January 1 2023 and must be applied retrospectively. The Bank is currently assessing the impact the amendments will have on current practice and whether existing loan agreements may require renegotiation.

Property, Plant and Equipment: Proceeds before Intended Use – Amendments to IAS 16
In May 2020, the IASB issued Property, Plant and Equipment — Proceeds before Intended Use, which prohibits entities deducting from the cost of an item of property, plant and equipment, any proceeds from selling items produced while bringing that asset to the location and condition necessary for it to be capable of operating in the manner intended by management. Instead, an entity recognises the proceeds from selling such items, and the costs of producing those items, in profit or loss. The amendment is effective for annual reporting periods beginning on or after 1 January 2022 and must be applied retrospectively to items of property, plant and equipment made available for use on or after the beginning of the earliest period presented when the entity first applies the amendment. The amendments are not expected to have a material impact on the Bank.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(b) Changes in accounting policies and disclosures (continued)

Standards issued but not yet effective (continued)

Definition of Accounting Estimates - Amendments to IAS 8

In February 2021, the IASB issued amendments to IAS 8, in which it introduces a definition of 'accounting estimates'. The amendments clarify the distinction between changes in accounting estimates and changes in accounting policies and the correction of errors. Also, they clarify how entities use measurement techniques and inputs to develop accounting estimates.

The amendments are effective for annual reporting periods beginning on or after 1 January 2023 and apply to changes in accounting policies and changes in accounting estimates that occur on or after the start of that period. Earlier application is permitted as long as this fact is disclosed. The amendments are not expected to have a material impact on the Bank.

Covid-19-Related Rent Concessions beyond 30 June 2021 Amendments to IFRS 16

On 28 May 2020, the IASB issued Covid-19-Related Rent Concessions - amendment to IFRS 16 Leases The amendments provide relief to lessees from applying IFRS 16 guidance on lease modification accounting for rent concessions arising as a direct consequence of the Covid-19 pandemic. As a practical expedient, a lessee may elect not to assess whether a Covid-19 related rent concession from a lessor is a lease modification. A lessee that makes this election accounts for any change in lease payments resulting from the Covid-19 related rent concession the same way it would account for the change under IFRS 16, if the change were not a lease modification.

The amendment was intended to apply until 30 June 2021, but as the impact of the Covid-19 pandemic is continuing, on 31 March 2021, the IASB extended the period of application of the practical expedient to 30 June 2022.The amendment applies to annual reporting periods beginning on or after 1 April 2021.

The Bank has not received Covid-19-related rent concessions but plans to apply the practical expedient if it becomes applicable within allowed period of application.

Disclosure of Accounting Policies - Amendments to IAS 1 and IFRS Practice Statement 2

In February 2021, the IASB issued amendments to IAS 1 and IFRS Practice Statement 2 Making Materiality Judgements, in which it provides guidance and examples to help entities apply materiality judgements to accounting policy disclosures. The amendments aim to help entities provide accounting policy disclosures that are more useful by replacing the requirement for entities to disclose their 'significant' accounting policies with a requirement to disclose their 'material' accounting policies and adding guidance on how entities apply the concept of materiality in making decisions about accounting policy disclosures.

The amendments to IAS 1 are applicable for annual periods beginning on or after 1 January 2023 with earlier application permitted. Since the amendments to the Practice Statement 2 provide non-mandatory guidance on the application of the definition of material to accounting policy information, an effective date for these amendments is not necessary.

The Bank is currently assessing the impact of the amendments to determine the impact they will have on the Bank's accounting policy disclosures.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) Basis of consolidation

The consolidated financial statements comprise the financial statements of the Bank and its subsidiary, Kenya School of Monetary Studies, as at 30 June 2021. Kenya School of Monetary Studies is a subsidiary of the Bank. The Bank has the power to govern the financial and operating policies generally of the school. The subsidiary was fully consolidated from the date on which control was transferred to the Bank.

The Bank uses the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the group. Acquisition-related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair value at the acquisition date.

The excess of the aggregate of the consideration transferred and the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the Bank's share of the identifiable net assets acquired is recorded as goodwill. If this is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in profit or loss.
Inter-company transactions, balances and unrealised gains on transactions between group entities are eliminated on consolidation. Unrealised losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Bank.

(d) Functional currency and translation of foreign currencies

Functional and presentation currency
Items included in the financial statements are measured using the currency of the primary economic environment in which the Bank operates (the "Functional Currency"). The financial statements are presented in Kenya Shillings ("KShs") which is the Bank's functional currency.

Transactions and balances
Foreign currency transactions are translated into the functional currency using exchange rates prevailing at the dates of the transactions or valuation where items are re-measured.

Monetary assets and liabilities denominated in foreign currencies are translated at the functional currency spot rates of exchange at the reporting date.

All foreign exchange gains and losses are presented in profit or loss within 'foreign exchange gains/ (losses)'.

(e) Currency Inventory

The Bank's inventory is comprised of new currency notes and coins. Inventories are stated at the sum of the production costs. Cost is determined using the first-in, first-out (FIFO) method.

Bank notes printing expenses and coin minting costs for each denomination which include ordering, printing, minting, freight, insurance and handling costs are initially deferred. Based on the currency issued into circulation, the respective proportional actual costs incurred are released to profit or loss from the deferred costs account. The deferred amount is recognised as 'deferred currency expenses' in other assets and represents un-issued bank notes and coins stock.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Financial instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Financial assets

Initial recognition and measurement

Financial assets are classified, at initial recognition, and subsequently measured at amortised cost, fair value through other comprehensive income (OCI), and fair value through profit or loss.

The classification of financial assets at initial recognition depends on the financial asset's contractual cash flow characteristics and the Bank's business model for managing them. The Bank initially measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs.

In order for a financial asset to be classified and measured at amortised cost or debt instruments at fair value through OCI, it needs to give rise to cash flows that are 'solely payments of principal and interest (SPPI)' on the principal amount outstanding. This assessment is referred to as the SPPI test and is performed at an instrument level.

The Bank's business model for managing financial assets refers to how it manages its financial assets in order to generate cash flows. The business model determines whether cash flows will result from collecting contractual cash flows, selling the financial assets, or both.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the market place (regular way trades) are recognised on the settlement date, i.e., the date that the Bank receives the asset on purchase or delivers the asset on sale.

Subsequent measurement

For purposes of subsequent measurement, financial assets are classified in four categories:

- Financial assets at amortised cost (debt instruments)
- Financial assets at fair value through OCI with recycling of cumulative gains and losses (debt instruments)
- Financial assets designated at fair value through OCI with no recycling of cumulative gains and losses upon derecognition (equity instruments)
- Financial assets at fair value through profit or loss

Financial assets at amortised cost (debt instruments)

This category is the most relevant to the Bank. The Bank measures financial assets at amortised cost if both of the following conditions are met:

- The financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows; And
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial assets at amortised cost are subsequently measured using the effective interest (EIR) method and are subject to impairment. Gains and losses are recognised in profit or loss when the asset is derecognised, modified or impaired.

The Bank's financial assets at amortised cost includes balances due from banking institutions, funds held with IMF, securities and advances to banks, loans and advances, other assets (sundry debtors), IMF On-Lent to GOK and due from Government of Kenya.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Financial instruments (continued)

Financial assets (continued)

Subsequent measurement (continued)

Financial assets at fair value through OCI (debt instruments)

The Bank measures debt instruments at fair value through OCI if both of the following conditions are met:

- The financial asset is held within a business model with the objective of both holding to collect contractual cash flows and selling; And
- The contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

For debt instruments at fair value through OCI, interest income, foreign exchange revaluation and Impairment allowance or reversals are recognised in profit or loss and computed in the same manner as for financial assets measured at amortised cost. The remaining fair value changes are recognised in OCI. Upon derecognition, the cumulative fair value change recognised in OCI is recycled to profit or loss.

The Bank's debt instruments at fair value through OCI includes investments in fixed income securities. Fixed income securities comprise Government debt securities issued by sovereign governments, Municipal bonds and bonds issued by international financial institutions.

Financial assets designated at fair value through OCI (equity instruments)

Upon initial recognition, the Bank can elect to classify irrevocably its equity investments as equity instruments designated at fair value through OCI when they meet the definition of equity under IAS 32 Financial Instruments: Presentation and are not held for trading. The classification is determined on an instrument-by-instrument basis.

Gains and losses on these financial assets are never recycled to profit or loss. Dividends are recognised as other income in profit or loss when the right of payment has been established, except when the Bank benefits from such proceeds as a recovery of part of the cost of the financial asset, in which case, such gains are recorded in OCI. Equity instruments designated at fair value through OCI are not subject to impairment assessment.

The Bank elected to classify irrevocably its non-listed equity investments under this category as it intends to hold these investments for the foreseeable future.

Financial assets at fair value through profit or loss

Financial assets at fair value through profit or loss include financial assets held for trading, financial assets designated upon initial recognition at fair value through profit or loss, or financial assets mandatorily required to be measured at fair value. Financial assets are classified as held for trading if they are acquired for the purpose of selling or repurchasing in the near term. Derivatives, including separated embedded derivatives, are also classified as held for trading unless they are designated as effective hedging instruments. Financial assets with cash flows that are not solely payments of principal and interest are classified and measured at fair value through profit or loss, irrespective of the business model. Notwithstanding the criteria for debt instruments to be classified at amortised cost or at fair value through OCI, as described above, debt instruments may be designated at fair value through profit or loss on initial recognition if doing so eliminates, or significantly reduces, an accounting mismatch.

Financial assets at fair value through profit or loss are carried in the statement of financial position at fair value with net changes in fair value recognised in profit or loss.

The Bank does not have any financial assets classified under this category.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Financial instruments (continued)

Financial assets (continued)

Classes of financial instruments

Category (as defined by IFRS 9)		Class (as determined by the Bank)		2021	2020
				KShs' million	KShs' million
Financial assets	Financial assets at amortized cost	Securities and advances to banks		59,540	55,561
		Funds held with IMF		2,201	3,255
		Net advances to staff and banks under liquidation		3,131	3,274
		Other assets (classified as financial assets)		349	500
		Due from Government	Government term loan	20,009	21,783
			IMF On-Lent to GOK	160,638	79,702
			GOK Overdraft facility	59,279	47,150
		Balances due from banking institutions	Foreign currency denominated term deposits and current account balances	430,968	369,505
	Financial assets at Fair value through other comprehensive income	Fixed income securities	World Bank managed and internally managed fixed income portfolios	664,991	724,892
		Equity	Investment securities	10	10
Financial liabilities	Financial liabilities at amortised cost	Deposits from banks	Cash reserve ratio and current account deposits	336,115	450,764
		Due to IMF		221,174	151,841
		Investments by banks		-	6,997
		Other liabilities		5,952	5,343
		Deposits from Government institutions		391,886	281,423

Impairment of financial assets

Overview of Expected Credit Loss (ECL) principles

The Bank recognizes Impairment allowance for expected credit losses "ECL" for financial assets that are debt instruments and are not measured at FVTPL.

The Bank measures Impairment allowance at an amount equal to lifetime ECL except for the following for which they are measured as 12-month ECL:

- Fixed income securities that are determined to have low credit risk at the reporting date; and

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Financial instruments (continued)

Financial assets (continued)

Impairment of financial assets (continued)

- other financial instruments for which credit risk has not increased significantly since initial recognition.

The Bank considers a debt security to have low credit risk when its credit risk rating is equivalent to the globally understood definition of 'investment-grade'. 12-month ECL is the portion of ECL that represents the ECLs that result from default events on a financial instrument that are possible within the 12 months after the reporting date. Financial instruments for which a 12-month ECL is recognised are referred to as 'Stage 1 financial instruments'. Life-time ECL are the ECLs that result from all possible default events over the expected life of the financial instrument. Financial instruments for which a lifetime ECL is recognised but which are not credit-impaired are referred to as 'Stage 2 financial instruments'. Financial instruments that are considered credit – impaired are referred to as 'Stage 3 financial instruments'. The Bank records an allowance for the lifetime ECL.

Measurement of ECL

ECL are a probability-weighted estimate of credit losses and are measured as follows:

- financial assets that are not credit-impaired at the reporting date: as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the Bank in accordance with the contract and the cash flows that the Bank expects to receive);
- financial assets that are credit-impaired at the reporting date: as the difference between the gross carrying amount and the present value of estimated future cash flows;

Credit impaired financial assets

At each reporting date, the Bank assesses whether financial assets carried at amortised cost and debt financial assets carried at FVOCI are credit-impaired (referred to as 'Stage 3 financial assets'). A financial asset is 'credit impaired' when one or more events that have a detrimental impact on the estimated future cash flows of the financial asset have occurred. Evidence that a financial asset is credit-impaired includes the following observable data:

- significant financial difficulty of the borrower or issuer;
- a breach of contract such as a default or past due event;
- the restructuring of a loan or advance by the Bank on terms that the Bank would not consider otherwise;
- it is becoming probable that the borrower will enter bankruptcy or other financial reorganization; and,
- the disappearance of an active market for a security because of financial difficulties.

In making an assessment of whether an investment in sovereign debt is credit-impaired, the Bank considers the following factors:

- The market's assessment of creditworthiness as reflected in the bond yields;
- The rating agencies' assessments of creditworthiness;
- The country's ability to access the capital markets for new debt issuance;
- The probability of debt being restructured, resulting in holders suffering losses through voluntary or mandatory debt forgiveness; and,
- The international support mechanisms in place to provide the necessary support as 'lender of last resort' to that country, as well as the intention, reflected in public statements, of governments and agencies to use those mechanisms. This includes an assessment of the depth of those mechanisms and, irrespective of the political intent, whether there is the capacity to fulfil the required criteria.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Presentation of allowance for ECL in the statement of financial position

Impairment allowance for ECL are presented in the statement of financial position as follows:

- financial assets measured at amortized cost: as a deduction from the gross carrying amount of the assets;
- debt instruments measured at FVOCI: no Impairment allowance is recognized in the statement of financial position because the carrying amount of these assets is their fair value. However, the Impairment allowance is disclosed and is recognized in the fair value reserve with a corresponding charge to profit or loss.

(f) Financial instruments

Financial assets

Derecognition

A financial asset (or, where applicable, a part of a financial asset or part of a group of similar financial assets) is primarily derecognised (i.e., removed from the Bank's consolidated statement of financial position) when:

- The rights to receive cash flows from the asset have expired

Or

- The Bank has transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the received cash flows in full without material delay to a third party under a 'pass-through' arrangement; and either (a) the Bank has transferred substantially all the risks and rewards of the asset, or (b) the Bank has neither transferred nor retained substantially all the risks and rewards of the asset, but has transferred control of the asset.

When the Bank has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if, and to what extent, it has retained the risks and rewards of ownership. When it has neither transferred nor retained substantially all of the risks and rewards of the asset, nor transferred control of the asset, the Bank continues to recognise the transferred asset to the extent of its continuing involvement. In that case, the Bank also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Bank has retained.

Continuing involvement that takes the form of a guarantee over the transferred asset is measured at the lower of the original carrying amount of the asset and the maximum amount of consideration that the Bank could be required to repay.

Write-offs

Loans and debt securities are written off (either partially or in full) when there is no reasonable expectation of recovering a financial asset in its entirety or a portion thereof. This is generally the case when the Bank determines that the borrower does not have assets or sources of income that could generate sufficient cash flows to repay the amounts subject to the write-off. This assessment is carried out at the individual asset level.

Recoveries of amounts previously written off are included in 'Impairment allowance on financial instruments' in profit or loss.

Financial assets that are written off could still be subject to enforcement activities in order to comply with the Bank's procedures for recovery of amounts due.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Financial instruments (continued)

Financial liabilities

Initial recognition and measurement

Financial liabilities are classified, at initial recognition, as financial liabilities at fair value through profit or loss, loans and borrowings, payables, or as derivatives designated as hedging instruments in an effective hedge, as appropriate.

All financial liabilities are recognised initially at fair value and, in the case of loans and borrowings and payables, net of directly attributable transaction costs. The Bank's financial liabilities include investment by banks, deposits from banks and government, due to IMF and other liabilities.

Subsequent measurement

The measurement of financial liabilities depends on their classification, as described below:

Financial liabilities at fair value through profit or loss

Financial liabilities at fair value through profit or loss include financial liabilities held for trading and financial liabilities designated upon initial recognition as at fair value through profit or loss.

Financial liabilities are classified as held for trading if they are incurred for the purpose of repurchasing in the near term.

Gains or losses on liabilities held for trading are recognised in profit or loss. Financial liabilities designated upon initial recognition at fair value through profit or loss are designated at the initial date of recognition, and only if the criteria in IFRS 9 is satisfied.

The Bank has not designated any financial liability as at fair value through profit or loss.

Loans and borrowings

This is the category most relevant to the Bank. After initial recognition, interest-bearing loans and borrowings are subsequently measured at amortised cost using the EIR method. Gains and losses are recognised in profit or loss when the liabilities are derecognised as well as through the EIR amortisation process.

Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included as finance costs in profit or loss.

This category generally applies to deposits from bank and government, due to IMF, investment by banks and other liabilities.

Derecognition

A financial liability is derecognised when the obligation under the liability is discharged or cancelled or expires.

When an existing financial liability is replaced by another from the same lender on substantially different terms, or the terms of an existing liability are substantially modified, such an exchange or modification is treated as the derecognition of the original liability and the recognition of a new liability. The difference in the respective carrying amounts is recognised in profit or loss.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Financial instruments (continued)

Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(g) Sale and repurchase agreements

Securities sold subject to repurchase agreements ('repos') are reclassified in the financial statements as pledged assets when the transferee has the right by contract or custom to sell or repledge the collateral; the counterparty liability is included in investments by banks.

Securities purchased under agreements to resell ('reverse repos') are recorded as advances to banks. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method. Securities lent to counterparties are also retained in the financial statements.

The Bank from time to time mops up money from the financial market ('repos') or injects money into the market ('reverse repos') with maturities of 4 - 7 days. The Bank engages in these transactions with commercial banks only. These have been disclosed in the financial statements as advances to banks.

(h) Cash and cash equivalents

Cash and cash equivalents include cash in hand, deposits held at call with banks and other short-term highly liquid investments with original maturities of three months or less.

For the purpose of the consolidated statement of cash flows, cash and cash equivalents consist of balances due from banking institutions, fixed income securities and securities and advances to banks with maturities of less than three months.

(i) Property and equipment

Land and buildings comprise mainly branches and offices. All equipment used by the Bank is stated at cost, net of accumulated depreciation and accumulated Impairment allowance, if any. Work in progress is stated at cost net of accumulated Impairment allowance, if any. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Land and buildings are measured at fair value less accumulated depreciation and Impairment allowance recognised after the date of revaluation. Valuations are performed with sufficient frequency to ensure that the carrying amount of a revalued asset does not differ materially from its fair value. Valuations are carried out every three years.

A revaluation surplus is recorded in OCI and credited to the asset revaluation surplus in equity. However, to the extent that it reverses a revaluation deficit of the same asset previously recognised in the profit or loss, the increase is recognised in profit and loss. A revaluation deficit is recognised in profit or loss, except to the extent that it offsets an existing surplus on the same asset recognised in the asset revaluation surplus.

Subsequent expenditures are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Bank and the cost of the item can be measured reliably. The carrying amount of the replaced part is de-recognised. All other repair and maintenance costs are charged to profit or loss during the financial period in which they are incurred.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(i) Property and equipment (continued)

Freehold land is not depreciated. Depreciation of other assets is calculated using the straight-line method to allocate their cost or revalued amounts to their residual values over their estimated useful lives, as follows:

Asset classification	Useful life	Depreciation rate
Leasehold land	Over the period of the lease	
Buildings	20 years	5%
Motor vehicles	4 years	25%
Furniture and equipment	5 - 10 years	10-20%
Computers	4 years	25%

No depreciation is charged on work in progress and assets held in clearing accounts. Depreciation of property and equipment is made from date of placement to use and it ceases when the asset is obsolete, classified as held for sale, fully depreciated or derecognized as per policy.

An item of property, plant and equipment and any significant part initially recognised is derecognised upon disposal (i.e., at the date the recipient obtains control) or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in profit or loss when the asset is derecognised.

The residual values, useful lives and methods of depreciation of property, plant and equipment are reviewed at each financial year end and adjusted prospectively, if appropriate.

(j) Intangible assets

Costs associated with maintaining computer software programmes are recognised as an expense as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the Bank are recognised as intangible assets when the following criteria are met:

(i) It is technically feasible to complete the software product so that it will be available for use;
(ii) Management intends to complete the software product and use or sell it;
- there is an ability to use or sell the software product;
- it can be demonstrated how the software product will generate probable future economic benefits;
- adequate technical, financial and other resources to complete the development and to use or sell the software product are available; and,

(iii) The expenditure attributable to the software product during its development can be reliably measured.

Directly attributable costs that are capitalised as part of the software product include the software development employee costs and an appropriate portion of relevant overheads.

Other development expenditures that do not meet these criteria are recognised as an expense as incurred. Development costs previously recognised as an expense are not recognised as an asset in a subsequent period.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

Computer software development costs recognised as assets are amortised over their estimated useful lives, which does not exceed three years. Computer software under installation and not yet placed in use is held in software clearing account and not amortized until commissioned.

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised on the basis of the expected useful lives. Software has a maximum expected useful life of 5 years.

(k) Impairment of non-financial assets

Assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. In assessing the value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). The impairment test also can be performed on a single asset when the fair value less cost of disposal or the value in use can be determined reliably. Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date.

Impairment allowance of continuing operations are recognised in profit or loss in expense categories consistent with the function of the impaired asset, except for properties previously revalued with the revaluation taken to OCI. For such properties, the impairment is recognised in OCI up to the amount of any previous revaluation. Impairment allowance recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists.

A previously recognised impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognised. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount or exceed the carrying amount that would have been determined, net of depreciation or amortisation, had no impairment loss been recognised for the asset in prior years. Such reversal is recognised in profit or loss unless the asset is carried at a revalued amount, in which case, the reversal is treated as a revaluation increase. An impairment loss recognised for goodwill is not reversed in a subsequent period.

(l) Employee benefits

The Bank operates a defined benefit scheme and a defined contribution pension scheme. The schemes are funded through payments to trustee-administered funds on a monthly basis.

On the defined contribution scheme, the Bank pays fixed contributions to the scheme. The payments are charged to the profit or loss in the year to which they relate. The Bank has no further payment obligation once the contributions have been paid.

The defined benefit plan defines an amount of pension benefit that an employee will receive on retirement, dependent on age, years of service and compensation.

The assets of the scheme are held by the Bank in an independent trustee administered fund.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) Employee benefits (continued)

The asset recognised in the statement of financial position in respect of defined benefit pension plans is the present value of the defined benefit obligation at the end of the reporting period less the fair value of plan assets, together with adjustments for unrecognised past-service costs. The defined benefit obligation is calculated annually by independent actuaries using the projected unit credit method. The present value of the defined benefit obligation is determined by discounting the estimated future cash outflows using interest rates of government bonds that are denominated in the currency in which the benefits will be paid, and that have terms to maturity approximating to the terms of the related pension obligation.

Past-service costs are recognised immediately in profit or loss, unless the changes to the pension plan are conditional on the employees remaining in service for a specified period of time (the vesting period). In this case, the past-service costs are amortised on a straight-line basis over the vesting period.

The Bank and all its employees contribute to the National Social Security Fund, which is a defined contribution scheme.

A defined contribution plan is a retirement benefit plan under which the Bank pays fixed contributions into a separate entity. The Bank has no legal or constructive obligations to pay further contributions if the fund does not hold sufficient assets to pay all employees the benefits relating to employee service in the current and prior periods.

The Bank's contributions to the defined contribution schemes are charged to profit or loss account in the year in which they fall due.

The estimated monetary liability for employees' accrued annual leave entitlement at the reporting date is recognised as an expense accrual.

(m) Income tax

Section 7 of the Income Tax 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.

(n) Provisions

Provisions are recognised when: The Bank has a present legal or constructive obligation as a result of past events; it is probable that an outflow of resources will be required to settle the obligation; and the amount has been reliably estimated. Provisions are not recognised for future operating losses.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation at a rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognised as interest expense.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(o) Surplus funds

The Central Bank of Kenya Act (Cap 491) allows the Bank to retain at least 10% or any other amounts as the board, in consultation with the minister, may determine, of the net annual profit (surplus) of the bank after allowing for the expenses of operations and after provision has been made for bad and doubtful debts, depreciation in assets, contributions to staff benefit funds, and such other contingencies and accounting provisions as the Bank deems appropriate.

(p) Share capital

Ordinary shares are classified as 'share capital' in equity.

(q) Leases

The Bank assesses at contract inception whether a contract is, or contains, a lease. That is, if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

Bank as a lessee

The Bank applies a single recognition and measurement approach for all leases, except for short-term leases and leases of low-value assets. The Bank recognises lease liabilities to make lease payments and right-of-use assets representing the right to use the underlying assets.

Right-of-use assets

The Bank recognises right-of-use assets at the commencement date of the lease (i.e., the date the underlying asset is available for use). Right-of-use assets are measured at cost, less any accumulated depreciation and Impairment allowance, and adjusted for any remeasurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognised, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Right-of-use assets are depreciated on a straight-line basis over the lease term as follows:

Buildings	1 to 5 years
Equipment	1 to 5 years

The right-of-use assets are also subject to impairment. Refer to the accounting policies in Note 2(k) Impairment of non-financial assets.

Lease liabilities

At the commencement date of the lease, the Bank recognises lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments.

In calculating the present value of lease payments, the Bank uses its incremental borrowing rate at the lease commencement date because the interest rate implicit in the lease is not readily determinable. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made. In addition, the carrying amount of lease liabilities is remeasured if there is a modification, a change in the lease term or a change in the lease payments.

The Bank's lease liabilities are included in Other liabilities (see Note 25).

Short-term leases and leases of low-value assets

The Bank applies the short-term lease recognition exemption to its short-term leases of buildings and equipments (i.e., those leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option). It also applies the lease of low-value assets recognition exemption to leases of equipments that are considered to be low value. Lease payments on short-term leases and leases of low-value assets are recognised as expense on a straight-line basis over the lease term.

Bank as a lessor

Leases in which the Bank does not transfer substantially all the risks and rewards incidental to ownership of an asset are classified as operating leases. Rental income arising is accounted for on a straight-line basis over the lease terms and is included in revenue in the statement of profit or loss due to its operating nature.

(r) Interest income and expense

Interest income and expense for all interest-bearing financial instruments are recognised in profit or loss using the effective interest method.

The effective interest method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument to the net carrying amount of the financial asset or liability on initial recognition. When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument, and any revisions to these estimates are recognised in profit or loss. The calculation includes amounts paid or received that are an integral part of the effective interest rate of a financial instrument, including transaction costs and all other premiums or discounts.

If a financial asset is measured at FVOCI or FVTPL, the amounts that are recognised in profit or loss are the same as the amounts that would have been recognised in profit or loss if the financial asset had been measured at amortised cost.

The Bank calculates interest income on financial assets, other than those considered credit-impaired, by applying the EIR to the gross carrying amount of the financial asset.

When a financial asset becomes credit-impaired (and is therefore regarded as 'Stage 3'), the Bank calculates interest income by applying the EIR to the net amortised cost of the financial asset. If the financial asset cures and is no longer credit-impaired, the Bank reverts to calculating interest income on a gross basis.

(s) Fee and commission income

The Bank earns from the Government of Kenya a commission of 1.5% of amounts raised through its agency role in the issuance of Treasury bills and bonds. The annual commission income is limited to KShs 3 billion as per the agreement between the Bank and The National Treasury effective 1 July 2007. In addition, the Bank earns commissions from other debt instruments issued to meet funding requirements of State Corporations.

Fees and commissions are generally recognised on an accrual basis when the service has been provided. Fees and commission income are recognised at an amount that reflects the consideration to which the Bank expects to be entitled in exchange for providing the services.

The performance obligations, as well as the timing of their satisfaction, are identified, and determined, at the inception of the contract. The Bank has generally concluded that it is the principal in its revenue arrangements because it typically controls the services before transferring them to the customer.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(t) Commitments on behalf of the Kenya Government and National Treasury

The Bank issues Treasury bills and bonds on behalf of the National Treasury. Commitments arising on such transactions on behalf of Kenya Government and the National Treasury are not included in these financial statements as the Bank is involved in such transactions only as an agent.

(u) Currency in circulation

Notes and coins in circulation are measured at fair value. Currency in circulation represents the nominal value of all bank notes and coins held by the public and commercial banks. The Bank demonetises currency denominations that it considers no longer suitable for circulation through a Gazette Notice.

(v) Loan due from the Government of Kenya

The loan due from the Government of Kenya arose from overdrawn accounts which were converted to a loan with effect from 1 July 1997 after an amendment to the Central Bank of Kenya Act to limit the Bank's lending to Government of Kenya to 5% of Government of Kenya audited revenue.

On 24 July 2007, a deed of guarantee was signed between the Government of Kenya and Central Bank of Kenya in which the government agreed to repay the loan at KShs 1.11 billion per annum over 32 years at 3% interest per annum. The security held is lien over cash balances, stock, treasury bonds and such other government securities as are specified in Section 46 (5) of the Central Bank of Kenya Act.

The loan due from the Government of Kenya is categorised as a debt instrument at amortised cost.

(w) Funds held at/due to International Monetary Fund (IMF)

Kenya has been a member of the International Monetary Fund (IMF) since 1966. The Bank is the designated depository for the IMF's holdings of Kenya's currency. IMF currency holdings are held in the No. 1 and No. 2 Accounts, which are deposit accounts of the IMF with the Bank.

Borrowings from and repayments to the IMF are denominated in Special Drawing Rights (SDRs). The SDR balances in IMF accounts are translated into Shillings at the prevailing exchange rates and any unrealized gains or losses are accounted for in accordance with accounting policy on foreign currencies.

On a custodial basis, the Bank holds a non-negotiable, non-interest bearing and encash able on demand promissory notes issued by the Treasury in favour of the IMF in its capacity as the IMF's depository. The security issued is in part payment of Kenya's quota of IMF.

(x) Fair value measurement

The Bank measures financial instruments such as debt instruments at fair value through other comprehensive income, and non-financial assets such as land and buildings and gold holdings, at fair value at each balance sheet date.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either:

- In the principal market for the asset or liability
  Or
- In the absence of a principal market, in the most advantageous market for the asset or liability

The principal or the most advantageous market must be accessible by the Bank.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(x) Fair value measurement (continued)

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Bank uses valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximising the use of relevant observable inputs and minimising the use of unobservable inputs.

All assets and liabilities for which fair value is measured or disclosed in the financial statements are categorised within the fair value hierarchy, described as follows, based on the lowest level input that is significant to the fair value measurement as a whole:

- Level 1 — Quoted (unadjusted) market prices in active markets for identical assets or liabilities
- Level 2 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is directly or indirectly observable
- Level 3 — Valuation techniques for which the lowest level input that is significant to the fair value measurement is unobservable

For assets and liabilities that are recognised in the financial statements at fair value on a recurring basis, the Bank determines whether transfers have occurred between levels in the hierarchy by re-assessing categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the end of each reporting period.

External valuers are involved for valuation of land and buildings. Involvement of external valuers is determined after every three years. Selection criteria include market knowledge, reputation, independence and whether professional standards are maintained. Valuers are normally rotated every three years.

For the purpose of fair value disclosures, the Bank has determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy, as explained above.

Fair-value related disclosures for financial instruments and non-financial assets that are measured at fair value or where fair values are disclosed, are summarised in the following notes:

- Disclosures for valuation methods, significant estimates and assumptions Notes 3, 15, 17(b), 18(b) and 31
- Quantitative disclosures of fair value measurement hierarchy Note 31
- Debt instruments at fair value through other comprehensive income Note 15
- Gold holdings Note 17(b)
- Land and buildings Note 18(b)

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES

The preparation of the Bank's consolidated financial statements requires management to make judgements, estimates and assumptions that affect the reported amount of revenues, expenses, assets and liabilities, and the accompanying disclosures, as well as the disclosure of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods. In the process of applying the Bank's accounting policies, management has made the following judgements and assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year.

Existing circumstances and assumptions about future developments may change due to circumstances beyond the Bank's control and are reflected in the assumptions if and when they occur. Items with the most significant effect on the amounts recognised in the consolidated financial statements with substantial management judgement and/or estimates are collated below with respect to judgements/estimates involved.

Impairment allowance on financial assets

The measurement of Impairment allowance under IFRS 9 across all categories of financial assets in scope requires judgement, particularly, the estimation of the amount and timing of future cash flows and collateral values when determining Impairment allowance and the assessment of a significant increase in credit risk.

These estimates are driven by a number of factors, changes in which can result in different levels of allowances.

The Bank's ECL calculations are outputs of complex models with a number of underlying assumptions regarding the choice of variable inputs and their interdependencies. Elements of the ECL models that are considered accounting judgements and estimates include:

- The Bank's internal credit grading model, which assigns PDs to the individual grades.
- The Bank's criteria for assessing if there has been a significant increase in credit risk and so allowances for financial assets should be measured on a Lifetime ECL basis and the qualitative assessment.
- The segmentation of financial assets when their ECL is assessed on a collective basis.
- Development of ECL models, including the various formulas and the choice of inputs.
- Determination of associations between macroeconomic scenarios and, economic inputs, such as unemployment levels and collateral values, and the effect on PDs, EADs and LGDs (Explanation of the terms: PDs, EADs and LDGs are included in Note 30(i)).
- Selection of forward-looking macroeconomic scenarios and their probability weightings, to derive the economic inputs into the ECL models.

It has been the Bank's policy to regularly review its models in the context of actual loss experience and adjust when necessary. Further details about the ECLs are provided in Notes 8, 11, 13, 14, 17 and 30(i).

Post-retirement benefits

Post-retirement benefits are long term liabilities whose value can only be estimated using assumptions about developments over a long period. The Bank has employed actuarial advice in arriving at the figures in the financial statements (Note 20 which includes assumptions). The Board of Directors considers the assumptions used by the actuary in their calculations to be appropriate for this purpose.

Fair value of financial assets

The fair value of financial instruments that are not traded in an active market and off market loans are determined by using valuation techniques. See Note 31 for additional disclosures.

3. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES (continued)

Property and equipment

Land and buildings are carried at fair value; representing open market value determined periodically by internal professional valuers. See Notes 18(b) and 31 for additional disclosures.

Leases - Estimating the incremental borrowing rate

The Bank cannot readily determine the interest rate implicit in the lease, therefore, it uses its incremental borrowing rate (IBR) to measure lease liabilities. The IBR is the rate of interest that the Bank would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the right-of-use asset in a similar economic environment. The IBR therefore reflects what the Bank 'would have to pay'.

The Bank estimates the IBR using observable inputs i.e. market interest rates.

Determining the lease term of contracts with renewal and termination options – Group as lessee

The Bank determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised.

4. INTEREST INCOME	2021 KShs' million	2020 KShs' million
Interest income calculated using the effective interest method		
Financial assets – debt instruments at amortised cost	7,391	11,587
Financial assets at fair value through other comprehensive income	9,693	10,721
	17,084	22,308
Interest income from debt instruments at amortised cost		
Interest on term deposits	2,055	4,856
Interest on Government of Kenya loan	626	666
Interest on Government of Kenya overdraft	2,208	3,245
Interest on staff loans and advances	102	104
Interest on advances to banks	2,082	2,142
Other interest income*	318	574
	7,391	11,587
Interest income from debt instruments at fair value through other comprehensive income comprises:		
Internally managed portfolio	9,186	10,093
Externally managed portfolio – (World Bank Reserve Advisory & Management Partnership)	507	628
	9,693	10,721

*Other interest income mainly comprises interest from overnight lending to banks.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

	2021 KShs' million	2020 KShs' million
5. INTEREST EXPENSE		
Interest expense calculated using the effective interest method		
Interest on monetary policy issues – investments by banks	1,897	4,355
Interest expense – IMF	129	263
	2,026	4,618
6. (a) FEES AND COMMISSION INCOME	3,000	3,000

Fees and commission relate to income the Bank earns from the Government of Kenya through its agency role in the issuance of Treasury bills and bonds.

	2021 KShs' million	2020 KShs' million
(b) NET TRADING INCOME		
Net gain on sale of foreign exchange currencies	8,328	7,437
Net gain on disposal of financial assets at fair value through other comprehensive income	4,909	4,316
	13,237	11,753
7. (a) OTHER INCOME		
Licence fees from commercial banks and foreign exchange bureaus	296	291
Penalties from commercial banks and foreign exchange bureaus	29	36
Rental income	49	57
Kenya School of Monetary Studies operating income - hospitality services and tuition fee	19	271
Gain on disposal of property and equipment	11	-
KEPSS Billing revenue	328	301
Miscellaneous income	312	26
	1,044	982
(b) DEMONETIZATION OF OLD CURRENCY	-	7,388

This amount relates to 7,388,000 pieces of older series of KShs 1,000 note that were not returned on conclusion of the demonetisation exercise on 30 September 2019. The value of these notes represented an operational surplus and was transferred to the exchequer on 20 March 2020 to support the National Government's efforts against the COVID-19 pandemic.

	2021 KShs' million	2020 KShs' million
8. IMPAIRMENT ALLOWANCE ON FINANCIAL ASSETS		
The table below shows the ECL charges on financial instruments:		
Impairment allowance on staff loans (Note 14)	5	3
Impairment allowance on balances due from banking institutions (Note 11)	17	87
Impairment allowance on securities and advances to banks (Note 13)	(4,274)	(8,700)
Impairment allowance on debt instruments at fair value through other comprehensive income	(81)	(17)
	(4,333)	(8,627)

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

9. (a) OPERATING EXPENSES

	2021 KShs' million	2020 KShs' million
Employee benefits (Note 9(b))	4,740	5,121
Currency production expenses	2,090	3,047
Property maintenance and utility expenses	1,830	1,910
Depreciation of property and equipment (Note 18(b))	2,125	1,695
Amortisation of intangible assets (Note 19)	163	159
Depreciation of right -of -use asset (Note 18(a)	135	133
Interest on leases liabilities (Note 18(a)	12	21
Provision for impairment loss on other assets (Note 17(a))	17	17
Work-in-Progress (WIP) write off	590	-
Auditor's remuneration	11	11
Transport and travelling costs	146	197
Office expenses	175	216
Postal service expense	232	208
Legal and professional fees	352	500
Loss on disposal of property and equipment	-	18
Revaluation decrease on land and buildings (Note 18(b))	2,560	-
Other administrative expenses	1,105	1,878
	16,283	15,131

(b) EMPLOYEE BENEFITS

	2021 KShs' million	2020 KShs' million
Wages and salaries	4,162	4,181
Pension costs – Defined contribution plan	448	421
Medical expenses	395	342
Other staff costs	36	291
Directors' emoluments (Note 29(ii))	51	60
Net income relating to the retirement benefit asset (Note 20)	(352)	(174)
	4,740	5,121

10. (a) CHANGES IN FAIR VALUE OF INVESTMENTS

Fair value changes on debt instruments at fair value through other comprehensive income:

	2021 KShs' million	2020 KShs' million
Internally managed portfolio	(5,803)	8,183
Externally managed portfolio – RAMP	(518)	269
	(6,321)	8,452

(b) RECLASSIFICATION TO THE INCOME STATEMENT

Net amount reclassified to the income statement on sale and maturity of debt instruments at FVOCI:

	2021 KShs' million	2020 KShs' million
Internally managed portfolio	7,091	2,680
Externally managed portfolio – RAMP	238	340
	7,329	3,020

This amount relates to reclassification on sale or maturity of debt instruments.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

11. BALANCES DUE FROM BANKING INSTITUTIONS	2021 KShs' million	2020 KShs' million
Current accounts	135,329	39,341
Foreign currency denominated term deposits	221,053	243,473
Accrued interest on term deposits	104	60
Special project accounts	33,374	57,520
Domestic foreign currency cheque clearing	40,576	28,426
REPSS clearing and regional central banks	543	713
	430,979	369,533
Impairment allowance	(11)	(28)
	430,968	369,505

An analysis of changes in the impairment allowance of balances due from banking institutions is as follows:

	2021 KShs' million	2020 KShs' million
At start of the year	28	115
Movement in impairment allowance (Note 8)	(17)	(87)
At 30 June	11	28

A reconciliation from the opening balance to the closing balance of the Impairment allowance based on year end stage classification is disclosed in Note 30 (i).

Special project accounts relate to amounts received by the Government of Kenya (or its ministries) for specific projects or purposes. An equal and corresponding liability is recorded and disclosed under "Deposits from banks and government" (Note 24).

12. FUNDS HELD AT/ DUE TO INTERNATIONAL MONETARY FUND (IMF)

		2021 SDR million	2021 KShs' million	2020 SDR million	2020 KShs' million
(a)	Assets				
	IMF balances (SDR asset account)	14	2,201	22	3,255
(b)	Liabilities				
	International Monetary Fund Account No. 1	20	3,048	20	2,886
	International Monetary Fund Account No. 2	-	5	-	4
	International Monetary Fund – PRGF Account	114	17,566	212	31,124
	Rapid Credit Facility	543	83,448	543	79,702
	Extended Credit Facility	163	25,035	-	-
	Extended Fund Facility	339	52,155	-	-
	IMF - SDR Allocation account	260	39,917	260	38,125
		1,439	221,174	1,035	151,841

The Bank received SDR 502.09 million (2020: SDR 542.8 million relating to Rapid Credit Facility (RCF)) from the Fund for direct budget support of the Government of Kenya initiatives towards COVID-19 pandemic. These funds were released to the Bank under Extended Credit Facility (ECF) and Extended Fund Facility (EFF) and represent a debt due from the Government of Kenya to the IMF. This debt is recognised in the books of the CBK, but on-lent to the government through the National Treasury.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

12. FUNDS HELD AT/ DUE TO INTERNATIONAL MONETARY FUND (IMF) (continued)

Kenya's quota in IMF of SDR 542.8 million (2020: SDR 542.8 million) is not included in the financial statements of the Bank as these are booked in the National Treasury who are the Government of Kenya's Fiscal Agent. Allocations of SDR 260 million (2020: SDR 260 million) are included in the financial statements of the Bank as the custodian of the Government of Kenya. The repayment of IMF facilities is currently bi-annual and Poverty Reduction Growth Facility (PRGF) attracts nil interest until advised by IMF. The Rapid Credit Facility will be paid within a period of five years from November 2025 to May 2030. ECF will be paid quartely within a period of 5 years from October 2026 to June 2031. EFF will be paid quartely within a period of six years from October 2025 to June 2031.

13. SECURITIES AND ADVANCES TO BANKS

	2021 KShs' million	2020 KShs' million
Treasury bonds discounted	7,299	7,513
Treasury bills discounted	534	116
Accrued interest bonds discounted	231	241
Repo treasury bills (Injection)	10,963	21,041
Accrued interest repo	69	214
Liquidity support framework	55,471	36,949
Due from commercial banks	947	1,187
	75,514	67,261
Impairment allowance	(15,974)	(11,700)
	59,540	55,561

An analysis of changes in the impairment allowance of securities and advances to banks is as follows:

	2021 KShs' million	2020 KShs' million
At the start of the year	11,700	3,000
Charge to profit or loss (Note 8)	4,274	8,700
At 30 June	15,974	11,700

Year ended 30 June 2021	Maturity period			
	0-3 months KShs' million	4-12 months KShs' million	Over 1 year KShs' million	Total KShs' million
Treasury bills discounted	519	15	-	534
Treasury bonds discounted	-	77	7,222	7,299
Accrued interest bonds discounted	180	51	-	231
Repo treasury bills & bonds (Injection)	10,963	-	-	10,963
Accrued interest repo	69	-	-	69
Due from commercial banks	947	-	-	947
Liquidity support framework	-	-	39,497	39,497
	12,678	143	46,719	59,540

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

13. SECURITIES AND ADVANCES TO BANKS (continued)

Year ended 30 June 2020	Maturity period			
	0-3 months KShs' million	4-12 months KShs' million	Over 1 year KShs' million	Total KShs' million
Treasury bills discounted	46	70	-	116
Treasury bonds discounted	-	281	7,232	7,513
Accrued interest bonds discounted	39	202	-	241
Repo treasury bills & bonds (Injection)	21,041	-	-	21,041
Accrued interest repo	214	-	-	214
Due from commercial banks	1,187	-	-	1,187
Liquidity support framework	-	-	25,249	25,249
	22,527	553	32,481	55,561

14. LOANS AND ADVANCES

	2021 KShs' million	2020 KShs' million
Due from banks under liquidation	3,400	3,400
Advances to employees	3,179	3,327
	6,579	6,727
Impairment allowance	(3,448)	(3,453)
Net advances	3,131	3,274
The movement in the Impairment allowance is as follows:		
At 1 July	3,453	3,456
Movement in impairment allowance (Note 8)	(5)	(3)
At 30 June	3,448	3,453

15. DEBT INSTRUMENTS MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME

	2021 KShs' million	2020 KShs' million
Fixed income securities – Internally managed portfolio	629,146	690,431
Fixed income securities under World Bank RAMP	35,845	34,461
	664,991	724,892

Maturity analysis	Maturity period			
Year ended 30 June 2021	0-3 months KShs' million	4-12 months KShs' million	Over 1 year KShs' million	Total KShs' million
Fixed income securities – Internally managed Portfolio	44,523	188,014	396,609	629,146
Fixed income securities under World Bank RAMP	1,497	11,998	22,350	35,845
	46,020	200,012	418,959	664,991

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

15. DEBT INSTRUMENTS MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME (continued)

Maturity analysis	Maturity period			
	0-3 months	4-12 months	Over 1 year	Total
At 30 June 2020	KShs' million	KShs' million	KShs' million	KShs' million
Fixed income securities – Internally managed Portfolio	57,638	375,418	257,375	690,431
Fixed income securities under World Bank RAMP	1,484	10,104	22,873	34,461
	59,122	385,522	280,248	724,892

Fixed income securities decreased by KShs 59,901 million to KShs 664,991 million (2020: KShs 724,892 million) mainly due to sale/maturities of fixed income securities during the year under review.

16. UNLISTED EQUITY INVESTMENTS

	2021 KShs' million	2020 KShs' million
Unquoted equity securities at fair value through other comprehensive income	10	10

17. (a) OTHER ASSETS

	2021 KShs' million	2020 KShs' million
Prepayments	1,471	1,930
Deferred currency expenses	3,572	2,933
Sundry debtors	5,328	5,462
Items in the course of collection	110	211
Uncleared effects	39	21
	10,520	10,557
Impairment allowance	(4,979)	(4,962)
	5,541	5,595

All other assets balances are recoverable within one year.

The movement in the Impairment allowance is as follows:		
At start of the year	4,962	4,945
Increase in impairment allowance (Note 9(a))	17	17
At 30 June	4,979	4,962

(b) GOLD HOLDINGS

Gold holdings	106	106

18(a) RIGHT OF USE ASSETS

Year ended 30 June 2021	Leases relating to buildings KShs' million	Leases relating to equipment KShs' million	Total KShs' million
COST			
At 1 July 2020	151	204	355
Additions	28	-	28
Disposal	(1)	-	(1)
At 30 June 2021	178	204	382
ACCCUMULATED DEPRECIATION			
At 1 July 2020	62	71	133
Charge for the year	61	74	135
At 30 June 2021	123	145	268
CARRYING AMOUNT			
At 30 June 2021	55	59	114

Year ended 30 June 2020	Leases relating to buildings KShs' million	Leases relating to equipment KShs' million	Total KShs' million
COST			
Effect of adoption of IFRS 16 on 1 July 2019	148	204	352
Additions	3	-	3
At 30 June 2020	151	204	355
ACCCUMULATED DEPRECIATION			
At 1 July 2019	-	-	-
Charge for the year	62	71	133
At 30 June 2020	62	71	133
CARRYING AMOUNT			
At 30 June 2020	89	133	222

Set out below are the carrying amounts of lease liabilities (included under 'Other liabilities' in Note 25) and the movements during the period:

	2021 Kshs million	2020 KShs 'million
At start of the year	209	350
Additions	28	3
Accretion of interest	12	21
Payment of principal	(171)	(158)
Terminated lease	(1)	-
Payment of interest	(22)	(7)
At 30 June	55	209

18(a) RIGHT OF USE ASSETS (continued)

The maturity analysis of lease liabilities is disclosed in Note 30. The following are the amounts recognised in profit or loss:

	2021 KShs 'million	2020 KShs 'million
Depreciation expense for right-of-use assets	135	133
Interest expense on lease liabilities	12	21
Expense relating to short-term leases (included in Other administrative expenses	10	5
Total amount recognised in profit or loss	157	159

The Bank had total cash outflows for leases of KShs 193 million (2020: KShs 165 million) during the year. No impairment loss or reversals of impairment loss has been recognized in profit or loss during the period. The bank also had non-cash additions to the right-of-use assets and lease liabilities of KShs 28 million (2020: KShs 3 million).

CENTRAL BANK OF KENYA NOTES TO THE FINANCIAL STATEMENTS (continued) FOR THE YEAR ENDED 30 JUNE 2021

18(b). PROPERTY AND EQUIPMENT

Year ended 30 June 2021	Freehold land and buildings KShs' million	Leasehold land and buildings KShs' million	Work in progress KShs' million	Motor vehicles KShs' million	Furniture and equipment KShs' million	Total KShs' million
AT COST OR VALUATION						
At 1 July 2020	19,282	5,410	2,963	431	9,140	37,226
Additions	455	-	1,711	17	701	2,884
Revaluation	(753)	79	-	-	-	(674)
Capitalization of work in progress	545	-	(2,024)	-	1,479	-
WIP write off	-	-	(590)	-	-	(590)
Transfers	31	(31)	-	-	-	-
Disposal	-	-	-	(22)	(68)	(90)
At 30 June 2021	19,560	5,458	2,060	426	11,252	38,756
DEPRECIATION						
At 1 July 2020	928	227	-	385	4,068	5,608
Charge for the year	752	158	-	29	1,186	2,125
Revaluation	(1,622)	(371)	-	-	-	(1,993)
Disposals	-	-	-	(22)	(67)	(89)
At 30 June 2021	58	14	-	392	5,187	5,651
CARRYING AMOUNT						
At 30 June 2021	19,502	5,444	2,060	34	6,065	33,105

Work in progress relates to integrated security management system and office modernisation Phase III at Head Office.

The WIP write off represents consultancy costs for projects in the bank that were determined to be no longer feasible for implementation.

Land and buildings were revalued as at 30 June 2021 by Regent Valuers International (K) Ltd and SEC & M Co. Ltd. The valuation resulted in an overall revaluation increase of KShs 1,319 million.

NOTES TO THE FINANCIAL STATEMENTS (continued) FOR THE YEAR ENDED 30 JUNE 2021

18(b). PROPERTY AND EQUIPMENT (continued)

Year ended 30 June 2020	Freehold land and Buildings KShs' million	Leasehold land and Buildings KShs' million	Work in Progress (WIP) KShs' million	Motor vehicles KShs' million	Furniture and equipment KShs' million	Total KShs' million
AT COST OR VALUATION						
At 1 July 2019	12,820	4,913	8,579	459	8,381	35,152
Additions	-	497	846	5	2,046	3,394
Capitalization of work in progress	6,462	-	(6,462)	-	-	-
Disposal	-	-	-	(33)	(1,287)	(1,320)
At 30 June 2020	19,282	5,410	2,963	431	9,140	37,226
DEPRECIATION						
At 1 July 2019	451	114	-	390	4,196	5,151
Charge for the year	477	113	-	28	1,077	1,695
Disposals	-	-	-	(33)	(1,205)	(1,238)
At 30 June 2020	928	227	-	385	4,068	5,608
NET CARRYING AMOUNT						
At 30 June 2020	18,354	5,183	2,963	46	5,072	31,618

Work in progress relates to integrated security management system and office modernisation Phase III at Head Office.

Land and buildings were revalued on 31 May 2018 by Lloyd Masika Limited. Land was revalued on the basis of the open market value, while buildings were valued on the basis of depreciated replacement cost.

18(b). PROPERTY AND EQUIPMENT (continued)

The treatment of the revaluation changes in the current financial year in the financial statements is as follows:

Revaluation increase on fixed assets (Note 9(a))	2021 KShs' million
Freehold land	2,607
Buildings	521
Leasehold land	751
The revaluation increase has been posted to Other Comprehensive Income	3,879

Revaluation decrease on land and buildings (Note 9(a))	
Buildings	(2,259)
Leasehold land	(301)
Revaluation decrease has been charged to profit and loss	(2,560)

The overall revaluation increase is KShs 1,319 million.

Land and buildings are included in the level 3 of the fair valuation hierarchy.

The methods and significant assumptions applied in arriving at the revalued amounts are as follows:

- The Bank's residential properties are all owner-occupied. In carrying out the valuation, the Bank has assumed that the prospective rental income to be generated by the property is based on the prevailing rentals for similar properties within the same location.
- The Bank has taken into account comparable values of similar properties (plot, construction standards, design, lay out, size, location, current sale prices of vacant plots and those developed) to derive the market prices. These were obtained from market transactions of comparable properties.
- The Bank is in possession of all title deeds

The reported revaluation decrease arose mainly from buildings at the Kenya School of Monetary Studies (KSMS). KSMS is the training institution for the CBK. As with other Central Banks, the training institution supports the mandate of the Bank of supporting financial sector stability.
Financial participants in the Kenyan market and regionally can be upskilled on all matters financial, which then provides a strong, informed and well educated financial sector. This is a critical basis for stability and will support the vision of Kenya to be a financial centre in East and Central Africa.
In assessing the valuation methodology to use, the Valuer considered the following:

i. That the KSMS complex is not operated for profit but rather to support the CBK mandate of financial sector stability
ii. Volatility in the national and global economy and disruption in travel as a result of the Covid-19 pandemic that has a negative impact on the operations of KSMS.
iii. The Covid-19 pandemic outbreak which has negatively impacted property prices.

As a result of the above, the valuation method settled on was the Cost approach. Whereas the ongoing Covid-19 pandemic has depressed the global economy, we expect a reversal of the impact as result of the vaccine roll out and appropriate government interventions, and thus will impact future revaluations.

The remainder of the revaluation decrease relates to leasehold land that have been impacted by the slump in real estate prices.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

19. INTANGIBLE ASSETS

	Software KShs' million	Work in Progress KShs' million	Total KShs' million
Year ended 30 June 2021			
COST			
At 1 July 2020	2,428	741	3,169
Additions	57	666	723
At 30 June 2021	2,485	1,407	3,892
ACCUMULATED AMORTISATION			
At 1 July 2020	1,945	-	1,945
Charge for the year	163	-	163
At 30 June 2021	2,108	-	2,108
NET CARRYING AMOUNT			
At 30 June 2021	377	1,407	1,784
Year ended 30 June 2020			
COST			
At 1 July 2019	2,415	208	2,623
Additions	13	533	546
At 30 June 2020	2,428	741	3,169
ACCUMULATED AMORTISATION			
At 1 July 2019	1,786	-	1,786
Charge for the year	159	-	159
At 30 June 2020	1,945	-	1,945
NET CARRYING AMOUNT			
At 30 June 2020	483	741	1,224

Work in progress relates to implementation of enterprise data warehouse (EDW).

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

20. RETIREMENT BENEFIT ASSET	2021 KShs' million	2020 KShs' million
Present value of funded obligations	17,302	17,910
Fair value of plan assets	(32,048)	(30,270)
Net overfunding in funded plan	(14,746)	(12,360)
Limit on defined benefit asset	7,107	5,823
Retirement Benefit Asset	(7,639)	(6,537)
Movements in the net defined benefit asset recognised are as follows:		
At start of the year	6,537	4,328
Net income recognised in profit or loss (Note 9(b))	352	174
Net income recognized in other comprehensive income (OCI)	676	1,949
Employer contributions	74	86
At 30 June	7,639	6,537
Movements in the plan assets are as follows:		
At start of the year	30,270	30,640
Interest income on plan assets	3,382	3,847
Employer contributions	74	86
Employee contributions	37	43
Benefits expenses paid	(1,538)	(1,601)
Return on plan assets excluding amount in interest income	(32)	(2,659)
Prior year adjustments	(145)	(86)
At 30 June	32,048	30,270
Movements in the plan benefit obligation are as follows:		
At start of the year	17,910	16,423
Current service cost net of employees' contributions	229	275
Interest cost	1,986	2,036
Employee contributions	37	43
Actuarial loss due to demographic assumptions	-	11
Actuarial gain due to participants' movement	(682)	(1,004)
Actuarial (gain)/loss due to change in financial assumptions	(640)	1,727
Benefits paid	(1,538)	(1,601)
At 30 June	17,302	17,910

The principal actuarial assumptions at the reporting date were:	2021	2020
Discount rate (p.a.)	12.00%	11.50%
Salary increase (p.a.)	7.00%	7.00%
Future pension increases	3.00%	3.00%

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

20. RETIREMENT BENEFIT ASSET (continued)

Five-year summary	2021 KShs' million	2020 KShs' million	2019 KShs' million	2018 KShs' million	2017 KShs' million
Fair value of plan assets	32,048	30,270	30,640	30,279	28,464
Present value of funded obligations	(17,302)	(17,910)	(16,423)	(14,551)	(13,440)
Adjustment to retirement benefit asset	(7,107)	(5,823)	(9,889)	(9,144)	(6,827)
Net retirement benefit asset	7,639	6,537	4,328	6,584	8,197

Plan assets are distributed as follows:

	2021 KShs' million	%	2020 KShs' million	%
Quoted shares	6,722	20.97%	5,684	18.8%
Investment properties	8,828	27.55%	8,358	27.6%
Government of Kenya treasury bills and bonds	14,621	45.62%	14,667	48.5%
Commercial paper and corporate bonds	81	0.25%	219	0.7%
Offshore investments	575	1.79%	133	0.4%
Fixed and term deposits	681	2.12%	1,114	3.7%
Fixed assets	2	0.02%	1	-
Private Equity	284	0.89%	-	-
Net current assets	254	0.79%	94	0.3%
	32,048	100%	30,270	100%

Sensitivity of principal actuarial assumptions:

If the discount rate is 1% lower (higher), the present value of funded obligations would be KShs 18,628 million (increase by KShs 1,326 million). This sensitivity analysis has been determined based on reasonably possible changes of the assumption occurring at the end of 30 June 2021, while holding all other assumptions constant.

The other principal actuarial assumptions, that is salary increase and future pension increase are not expected to change materially because they are within the control of management and are approved in the Human Resource Policy on employee benefits. Additionally, any change is not expected to be material based on historical trends and may not have a linear impact on the present value of the fund obligation.

The Bank does not have any asset-liability matching strategies used to manage risk. The retirement benefit scheme is funded and hence the assets under the scheme are used to meet benefit payments as and when they arise. The timing of the benefit payments from the scheme are unknown as the fund comprises active members, pensioners and deferred pensioners.

The scheme is funded by contributions from employer and employees. The average duration of the defined benefit plan obligation at the end of the reporting period is 7.4 years (2020: 7.0 years). The Bank expects to pay KShs 80 million to its defined benefit plan in financial year ended 30 June 2022.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

21. (a) IMF On-Lent to GOK	2021 KShs' million	2020 KShs' million
Rapid credit facility	83,448	79,702
Extended credit facility	25,035	-
Extended fund facility	52,155	-
	160,638	79,702

The balance as at 30 June 2021 relates to IMF on-lent funds disbursed to the Government of Kenya by the International Monetary Fund (IMF) amounting SDR 542.8 million under Rapid Credit Facility and SDR 502.09 under ECF and EFF to mitigate the impact of COVID-19 pandemic. RCF will be paid half-yearly within a period of five years from November 2025 to May 2030. ECF will be paid quartely within a period of 5 years from October 2026 to June 2031. EFF will be paid quartely within a period of six years from October 2025 to June 2031.

(b) DUE FROM GOVERNMENT OF KENYA	2021 KShs' million	2020 KShs' million
Overdraft	59,279	47,150
Government loan	20,009	21,783
	79,288	68,933

Movement in the government loan is as follows:

At start of the year	21,783	22,229
Principal repayment	(1,665)	(555)
Interest charged	626	666
Interest paid	(735)	(557)
At 30 June	20,009	21,783

Section 46(3) of the *Central Bank of Kenya Act* sets the limit of the Government of Kenya's overdraft facility at the Bank at 5% of the Gross Recurrent Revenue as reported in the latest Government of Kenya audited financial statements. The limit for the year ending 30 June 2021 is KShs 75,453 million (2020: KShs 68,495 million) based on the gross recurrent revenue for the year ended 30 June 2019, which are the latest audited financial statements at the date of approval of these financial statements. Interest is charged at the Central Bank Rate, currently at 7%.

The Bank converted the Government of Kenya overdraft facility that exceeded statutory limit in 1997 into a loan at 3% interest repayable by 2039 and is guaranteed by a deed executed by the Cabinet Secretary, The National Treasury. Principal repayments of KShs 555 million are paid half yearly while interests accruing are paid monthly.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

22. CURRENCY IN CIRCULATION	2021 KShs' million	2020 KShs' million
Kenya bank notes	267,388	248,373
Kenya coins	9,741	9,419
	277,129	257,792
Movement in the account was as follows:		
At 1 July	257,792	249,509
Deposits by commercial banks	(577,361)	(571,022)
Withdrawals by commercial banks	596,704	586,732
Deposits by CBK	(6)	(39)
Demonetization of old currency	-	(7,388)
At 30 June	277,129	257,792

23. INVESTMENT BY BANKS

REPO securities sold to banks	-	6,997

The balance on 30 June 2020 relates to repurchase agreements contracted by the Bank to address excess liquidity and matures within a short period of between 7 to 14 days.

24. DEPOSITS FROM BANKS AND GOVERNMENT	2021 KShs' million	2020 KShs' million
Local commercial banks clearing accounts and cash ratio reserve	246,215	352,490
Local banks foreign exchange settlement accounts	37,394	25,824
External banks foreign exchange settlement accounts	2,851	2,620
Other public entities and project accounts	49,655	69,830
Government of Kenya	391,886	281,423
	728,001	732,187

25. OTHER LIABILITIES

Impersonal accounts	997	1,412
Sundry creditors	3,161	3,489
Lease liability (Note 18(a))	55	209
Refundable deposits	224	233
Leave accrual	259	235
Bond pending payables	1,515	-
Gratuity to staff members	47	24
	6,258	5,602

Impersonal accounts hold amounts due to ministries and departments of Government of Kenya.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

26. (a) SHARE CAPITAL	2021 KShs' million	2020 KShs' million
Authorised share capital:		
At 1 July and 30 June	50,000	50,000
Paid up share capital:		
At start of the year	35,000	20,000
Additional share capital	-	15,000
At 30 June	35,000	35,000

Ownership of the entire share capital is vested in the Principal Secretary to the National Treasury.

(b) GENERAL RESERVE FUND

The general reserve fund represents accumulated realized surpluses of KShs 50,136 million (2020: KShs 48,913 million) arising from normal operations of the Bank and unrealized gains of KShs 105,233 million (2020: KShs 79,287 million).

(c) FAIR VALUE RESERVE

The fair value reserve represents cumulative gains and losses arising from revaluation of debt instruments from cost to fair value based on the market values at the end of the reporting date.

(d) REVALUATION RESERVE

The revaluation reserve relates to unrealized revaluation gains on land and buildings that will not be recycled into profit or loss. The reserve is non-distributable.

(e) CONSOLIDATED FUND

The Consolidated Fund represents amounts proposed for distribution to the Government of Kenya from the General Reserve Fund.

Movement in the consolidated fund is as follows:

	2021 KShs' million	2020 KShs' million
At start of the year	2,500	4,000
Transfer from General reserve	10,500	9,888
Payments out of consolidated fund	(7,500)	(11,388)
At 30 June	5,500	2,500

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

27. CASH USED IN OPERATIONS

	2021 KShs' million	2020 KShs' million
Surplus for the year	36,993	41,530
Adjustments for:		
Depreciation of property and equipment (Note 18(b))	2,125	1,695
Amortisation of intangible assets (Note 19)	163	159
Amortisation of right-of-use assets (Note 18(a))	135	133
Work-in-Progress (WIP) write off (Note 9(a))	590	-
Gain on disposal of property and equipment (Note 7)	(11)	-
Loss on valuation of land and building	2,560	-
Loss on disposal of property and equipment (Note 9(a))	-	18
Impairment allowance on financial assets	4,350	8,714
Net interest income	(15,058)	(17,690)
Interest on lease liability (Note 9(a))	12	21
Provision for impairment loss on other assets (Note 9(a))	17	17
Net credit relating to the retirement benefit asset (Note 20)	(352)	(174)
Employer contributions on defined benefit asset (Note 20)	(74)	(86)
Demonetization of old currency (Note 7(b))	-	(7,388)
Reclassification from fair value reserve (Note 10(b))	(7,329)	(3,020)
Unrealised foreign exchange loss on due to IMF	37	120
Operating surplus before working capital changes	24,158	24,049
Changes in working capital:		
Loans and advances	148	92
Other assets	37	70
Due from Government of Kenya	(10,355)	10,623
Currency in circulation	19,337	15,671
Deposits	(4,186)	(8,813)
Investment by banks	(6,997)	6,997
IMF on-lent	(80,936)	(79,702)
Gold holdings	-	(25)
Consolidated fund (Note 26(e))	(7,500)	(11,388)
Other liabilities	810	(1,129)
Net cash used in operations	(65,484)	(43,555)

28. CASH AND CASH EQUIVALENTS

(a) For the purpose of the statement of cash flows, cash and cash equivalents include:

	2021 KShs' million	2020 KShs' million
Balances due from banking institutions (Note 11)	430,968	369,505
Financial assets – FVOCI (Note 15)	46,020	59,122
Securities discounted by banks and other advances (Note 13)	12,678	22,527
	489,666	451,154

(b) Changes in liabilities arising from financing activities

	2021	2020
At start of the year	151,841	83,653
Cash flow items:		
Repayments to IMF	(7,894)	(11,634)
Receipts during the year	77,190	79,702
Foreign exchange changes	37	120
At 30 June	221,174	151,841

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

29. RELATED PARTY TRANSACTIONS

In the course of its operations, the Bank enters into transactions with related parties, which include the Government of Kenya (the ultimate owner of the Bank).

The main transactions are ordinary banking facilities to government ministries included in Note 24 and lending to the Government of Kenya included in Note 21.

(i) Loans

The Bank extends loan facilities to the key management staff. The advances are at preferential rates of interest determined by the Bank. The repayment terms and collateral used are similar to those of loans and advances to other staff. Provisions on loans and advances to staff are arrived at using collective assessment approach. Provisions at 30 June 2021 are disclosed in Note 14. Collateral information is disclosed in Note 30. The repayment terms of the loans are between 3 years and 25 years.

Loans to key senior staff	2021 KShs' million	2020 KShs' million
At 1 July	52	50
Loans advanced during the year	7	23
Loan repayments	(33)	(21)
At 30 June	26	52

(ii) Directors' emoluments:

Fees to non-executive directors	17	18
Directors' travelling expenses	-	8
Other remuneration to executive directors	34	34
	51	60

(iii) Remuneration to senior staff	258	240
(iv) Post–employment pension to senior management	4	4

(v) Government of Kenya

Due from Government of Kenya (Note 21(b))	79,288	68,933
Government of Kenya Deposits (Note 24)	391,886	281,423
IMF On-lent to GOK (Note 21(a))	160,638	79,702
Interest earned from Government of Kenya – Loan (Note 4)	626	666
Interest earned from Government of Kenya - Overdraft (Note 4)	2,208	3,245
Fees and commission income (Note 6(a))	3,000	3,000
Loan principal repayment (Note 21(b))	1,665	555

Transactions entered into with the Government include:

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

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

29. RELATED PARTY TRANSACTIONS (continued)

(vi) Kenya School of Monetary Studies (KSMS)

The Kenya School of Monetary Studies (the "School") is a subsidiary of the Bank. It is primarily owned and managed by CBK and its financial statements have been consolidated in these financial statements.

The permanent staff working at KSMS are employees of CBK. Fixed assets are also wholly owned by the Bank and a letter of support is issued annually to the external auditor of the School as part of the commitment of the Bank for going concern purposes.

During the year under review, the school's physical developments projects were significantly completed.

	2021 KShs' million	2020 KShs' million
CBK-KSMS related transactions and balances		
Grants from CBK	562	468
Buildings	6,224	8,780
Land	8,100	4,250
Receivable from KSMS	59	59
Accumulated deficit	62	62

(vii) Central Bank of Kenya Pension Fund and Banki Kuu Pension Scheme 2012

The pension schemes (that is, the defined benefit and defined contribution schemes) are managed and administered by the Secretariat appointed by the sponsor. The costs of their operations are fully reimbursed to the Bank on a regular basis.

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES

The Bank's activities expose it to a variety of financial risks, including credit risk and the effects of changes in debt and equity market prices, foreign currency exchange rates and interest rates. The Bank's overall risk management programme focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on its financial performance.

Risk management is carried out by the Internal Audit and Risk Management Department under policies approved by the Board of Directors. Other organs that monitor the assessment and management of risks within the Bank include: Board Audit Committee.

(a) Strategy in using financial instruments
The bank holds foreign exchange reserves for the purpose of serving official foreign debt, paying non-debt government and Central Bank of Kenya expenditures abroad and intervention in the foreign exchange market to minimize volatility and facilitate its smooth functioning.

The foreign exchange reserves are managed via a governance framework anchored in legislation and a reserves management policy set by the Board of Directors. The policy sets the context within which the Strategic Asset Allocation, Investment guidelines and Investment Committee are operationalized in order to achieve the overarching principles of safety, liquidity and return.

(b) Risks facing the Bank

The following are the main types of financial risks that the Bank is exposed to in the course of executing its operations:

- Credit risk
- Market risk
- Liquidity risk

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk

Credit risk is the risk that the Bank will incur a loss because its customers or counterparties fail to discharge their contractual obligations. The Bank manages and controls credit risk by setting limits on the amount of risk it is willing to accept for individual counterparties and for geographical and industry concentrations, and by monitoring exposures in relation to such limits.

Credit risk arises from balances due from banking institutions, funds held with IMF, securities and advances to banks, IMF On-Lent to GOK, loans and advances, debt instruments at fair value through other comprehensive income, other assets (sundry debtors) and due from Government of Kenya.

Management of credit risk is carried out through the choice of counterparties. The Bank's choice of counterparties is confined to top international banks that meet the set eligibility criteria of financial soundness on long-term credit rating, short-term credit rating and capital adequacy.

The following table sets out the carrying amounts of the financial assets that are exposed to credit risk as at 30 June 2021 and 30 June 2020:

	2021 KShs' million	2020 KShs' million
Balances due from banking institutions	430,968	369,505
Funds held with International Monetary Fund (IMF)	2,201	3,255
Securities and advances to banks	59,540	55,561
IMF On-Lent to GOK	160,638	79,702
Loans and advances	3,131	3,274
Debt instruments at fair value through other comprehensive income	664,991	724,892
Other assets – sundry debtors	349	500
Due from Government of Kenya	79,288	68,933
	1,401,106	1,305,622

The Bank assesses the credit quality of these assets at every reporting date. None of the balances have had their terms renegotiated as a result of non-performance. Management monitors the credit exposure of staff on a continuous basis, taking into account their financial position, past experience and other factors.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Credit quality analysis

The following tables set out information about the credit quality of financial assets measured at amortised cost and debt instruments at FVOCI. Unless specifically indicated, for financial assets, the amounts in the table represent gross carrying amounts.

Explanation of the terms: 'Stage 1', 'Stage 2' and 'Stage 3' are included in Note 2(f). The credit ratings are obtained from recognized international credit rating agencies.

Year ended 30 June 2021

	Stage 1 KShs' million	Stage 2 KShs' million	Stage 3 KShs' million	Total KShs' million
Balance due from banking institutions				
Rated AAA	-	-	-	-
Rated AA- to AA+	111,771	-	-	111,771
Rated A- to A+	222,295	-	-	222,295
Rated BBB – BB	659	-	-	659
Unrated	96,254	-	-	96,254
Gross carrying amount	430,979	-	-	430,979
Impairment allowance	(11)	-	-	(11)
Net carrying amount	430,968	-	-	430,968
Debt instruments at fair value through OCI				
Rated AAA	657,885	-	-	657,885
Rated AA- to AA+	7,106	-	-	7,106
Carrying amount	664,991	-	-	664,991
Due from Government of Kenya				
Unrated	79,288	-	-	79,288
Funds with IMF				
Unrated	2,201	-	-	2,201
IMF On-Lent to GOK				
Unrated	160,638	-	-	160,638

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Credit quality analysis (continued)

Year ended 30 June 2021

	Stage 1 KShs' million	Stage 2 KShs' million	Stage 3 KShs' million	Total KShs' million
Securities and advances to banks				
Unrated	75,514	-	-	75,514
Gross carrying amount	75,514		-	75,514
Impairment allowance	(15,974)	-	-	(15,974)
Net carrying amount	59,540	-	-	59,540
Loans and advances				
Unrated	3,051	6	3,522	6,579
Gross carrying amount	3,051	6	3,522	6,579
Impairment allowance	(7)	-	(3,441)	(3,448)
Net carrying amount	3,044	6	81	3,131
Other assets				
Unrated	-	-	5,328	5,328
Gross carrying amount	-	-	5,328	5,328
Impairment allowance	-	-	(4,979)	(4,979)
Net carrying amount	-	-	349	349

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Credit quality analysis (continued)

Year ended 30 June 2020

	Stage 1 KShs' million	Stage 2 KShs' million	Stage 3 KShs' million	Total KShs' million
Balance due from banking institutions				
Rated AAA	36,248	-	-	36,248
Rated AA- to AA+	146,509	-	-	146,509
Rated A- to A+	109,007	-	-	109,007
Rated BBB – BB	807	-	-	807
Unrated	76,962	-	-	76,962
Gross carrying amount	369,533	-	-	369,533
Impairment allowance	(28)	-	-	(28)
Net carrying amount	369,505	-	-	369,505
Debt instruments at fair value through OCI				
Rated AAA	715,417	-	-	715,417
Rated AA- to AA+	9,475	-	-	9,475
Carrying amount	724,892	-	-	724,892
Due from Government of Kenya				
Unrated	68,933	-	-	68,933
Funds with IMF				
Unrated	3,255	-	-	3,255
IMF On-Lent to GOK				
Unrated	79,702	-	-	79,702

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Credit quality analysis (continued)

Year ended 30 June 2020

	Stage 1 KShs' million	Stage 2 KShs' million	Stage 3 KShs' million	Total KShs' million
Securities and advances to banks				
Unrated	65,114	-	2,147	67,261
Gross carrying amount	65,114		2,147	67,261
Impairment allowance	(9,553)	-	(2,147)	(11,700)
Net carrying amount	55,561	-	-	55,561
Loans and advances				
Unrated	3,166	11	3,550	6,727
Gross carrying amount	3,166	11	3,550	6,727
Impairment allowance	(3)	-	(3,450)	(3,453)
Net carrying amount	3,163	11	100	3,274
Other assets				
Unrated	-	-	5,462	5,462
Gross carrying amount	-	-	5,462	5,462
Impairment allowance	-	-	(4,962)	(4,962)
Net carrying amount	-	-	500	500

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Collateral and other credit enhancements

The Bank holds collateral and other credit enhancements against certain credit exposures. The following table sets out the principal types of collateral held against different types of financial assets.

	Notes	Percentage of exposure that is subject to collateral requirements		
		30 June 2021	30 June 2020	Principal type of collateral held
Advances to banks – Reverse repurchase arrangements and due from commercial banks	13	100	100	Kenya Government debt securities
Loans and advances – Loans to staff	14	100	100	Land and buildings, government securities, motor vehicles

At 30 June 2021, the Bank held advances to banks of KShs 11,910 million (2020: KShs 22,228 million), for which no Impairment allowance is recognised because of full collateral coverage. The fair value of the collateral held for Advances to banks was KShs 13,796 million (2020: KShs 26,137 million). These have been determined based on market price quotations at the reporting date.

Inputs, assumptions and techniques used for estimating expected credit loss

Significant increase in credit risk

When determining whether the risk of default of the invested amount on a financial instrument has increased significantly since initial recognition, the Bank considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Bank's historical experience and credit risk specialist's assessment and including forward-looking information.

The objective of the assessment is to identify whether a significant increase in credit risk has occurred for an exposure by comparing:

- the remaining lifetime probability of default (PD) as at the reporting date; with
- the remaining lifetime PD for this point in time that was estimated at the time of initial recognition of the exposure (adjusted where relevant for changes in prepayment expectations).

Credit risk grades/ratings

For assessing the risk of default, at initial recognition, the Bank assigns to each exposure credit risk grade/rating determined based on the credit risk assessment.

The Bank, at initial recognition, allocates each exposure to banks a credit risk grade based on a variety of data that is determined to be predictive of the risk of default and applies experienced credit judgement. Credit risk grades are defined using qualitative and quantitative factors that are indicative of risk of default. These factors vary depending on the nature of the exposure and the type of borrower. Credit risk grades are defined and calibrated such that the risk of default occurring increases exponentially as the credit risk deteriorates.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Inputs, assumptions and techniques used for estimating expected credit loss (continued)

Credit risk grades/ratings (continued)

Exposures are subject to ongoing monitoring, which may result in an exposure being moved to a different credit risk grade/rating. The monitoring typically involves use of the following information.

Foreign currency exposures	Domestic currency exposures	Other assets
Data from credit rating agencies, press articles, changes in external credit ratings Quoted bond prices for the counterparty, where available Actual and expected significant changes in the political, regulatory and technological environment of the counterparty or in its business activities	Internally collected data on banks and supervisory indicators Existing and forecast changes in business, financial and economic conditions	Repayment history – this includes overdue status and financial situation of the borrower. Existing and forecast changes in financial and economic conditions

PD estimation process

Credit risk grades/ratings are a primary input into the determination of the term structure of PD for exposures. The Bank collects performance and default information about its credit risk exposures analysed by counterparty as well as by credit risk grading/ratings. The Bank employs statistical models to analyse the data collected and generate estimates of the lifetime PD of exposures and how these are expected to change as a result of the passage of time.

The methodology for determining PDs for domestic commercial banks is based on the risk assessment techniques used for supervisory purposes. Factors considered by these techniques include the capital adequacy, credit risk, liquidity and profitability of the counterparty. The PDs are calculated as the average weighted PDs for each factor, where the weights are determined based on the importance of the factor.

For the assets denominated in foreign currency, the Bank uses 12-month PDs for sovereign and non-sovereign issuances, estimated based on Bloomberg's probability of default model which indicate a possibility of bankruptcy over 12 months for issuers per each respective rating category. The Bloomberg PD includes the estimates of forward-looking parameters such as GDP, forex rates, and interest rates.

For exposures to the Kenyan Government in domestic currency, the estimated PD considers the short-term maturity of such exposures, the absence of historical defaults and detailed assessments of the ability of the Kenyan Government to fulfil its contractual cash flow obligations in the short-term which considers also the macroeconomic indicators over the assessment period.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Inputs, assumptions and techniques used for estimating impairment (continued)

Determining whether credit risk has increased significantly
The Bank considers a financial instrument to have experienced a significant increase in credit risk, when one or more of the following quantitative, qualitative or backstop criteria have been put:

- Significant dip in operating results of counterparty.
- Credit distress necessitated extension to terms granted.
- Significant adverse changes in the financial and /or economic conditions affecting the counterparty.
- Significant change in collateral value which is expected to increase risk of default.
- Signs of cash flow / liquidity problems.

A backstop is applied, and the financial instrument considered to have experience a significant increase in credit risk if the counterparty is more than 30 days past due.
Days past due are determined by counting the number of days since the earliest elapsed due date in respect of which full payment has not been received. Due dates are determined without considering any grace period that might be available to the counterparty.

The Bank monitors the effectiveness of the criteria used to identify significant increases in credit risk by regular reviews to confirm that the criteria are capable of identifying significant increases in credit risk before an exposure is in default.

Definition of default

The Bank considers a financial asset to be in default when:

- the counterparty is unlikely to pay its credit obligations to the Bank in full, without recourse by the Bank to actions such as realizing security (if any is held); or
- the counterparty is past due more than 90 days on any material credit obligation to the Bank.

In assessing whether a counterparty is in default, the Bank considers indicators that are:
- qualitative – e.g. breaches of covenants;
- quantitative – e.g. overdue status and non-payment on another obligation of the same issuer to the Bank; and
- based on data developed internally and obtained from external sources.

Inputs into the assessment of whether a financial instrument is in default and its significance may vary over time to reflect changes in circumstances.

Incorporation of forward-looking information

In its ECL models, the Bank relies on Bloomberg credit risk model for provision of probabilities of default values for the both the investment counterparties and the sovereigns. The bank also relies on international credit rating agencies for credit rating information. Credit ratings are a tool, among others, that investors can use when making decisions about purchasing bonds and other fixed income investments. They express independent opinions on creditworthiness, using a common terminology that may help investors make more informed investment decisions.
As part of their ratings analysis, the external credit agencies as well as the Bloomberg credit risk model evaluate current and historical information and assess the potential impact of a broad range of forward-looking information.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Inputs, assumptions and techniques used for estimating impairment (continued)

Measurement of ECL

The key inputs into the measurement of ECL are the term structure of the following variables:

- Probability of default (PD);
- Loss given default (LGD);
- Exposure at default (EAD).

These parameters are derived from internally developed statistical models, globally recognized external developed statistical models and other historical data. They are adjusted to reflect forward-looking information as described above.

Probability of default (PD); PD estimates are estimates at a certain date, which are calculated based on statistical rating models, and assessed using rating tools tailored to the various categories of counterparties and exposures. These statistical models are based on internally and externally compiled data comprising both quantitative and qualitative factors. Transition matrixes data are used to derive the PD for counterparties. If a counterparty or exposure migrates between rating classes, then this will lead to a change in the estimate of the associated PD.

Loss given default (LGD); LGD is the magnitude of the likely loss if there is a default. The Bank estimates LGD parameters based on the history of recovery rates, or parameters calculated by international credit rating agencies and regulatory institutions, of claims against defaulted counterparties. The LGD models consider the structure, collateral, seniority of the claim, counterparty industry and recovery costs of any collateral that is integral to the financial asset.

Exposure at default (EAD); EAD represents the expected exposure in the event of a default. The Bank derives the EAD from the current exposure to the counterparty and potential changes to the current amount allowed under the contract including amortisation.

The EAD of a financial asset is its gross carrying amount. EAD estimates are calculated on a discounted cash flow basis using the effective interest rate as the discounting factor.

As described above, and subject to using a maximum of a 12-month PD for financial assets for which credit risk has not significantly increased, the Bank measures ECL considering the risk of default over the maximum contractual period over which it is exposed to credit risk, even if, for risk management purposes, the Bank considers a longer period. The maximum contractual period extends to the date at which the Bank has the right to require repayment of an advance.

Where modelling of a parameter is carried out on a collective basis, the financial instruments are grouped on the basis of shared risk characteristics that include: instrument type, credit risk grading; collateral type; date of initial recognition; remaining term to maturity; industry; and, geographic location of the counterparty

The groupings are subject to regular review to ensure that exposures within a particular group remain appropriately homogeneous.

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Inputs, assumptions and techniques used for estimating impairment (continued)

Measurement of ECL (continued)

For portfolios in respect of which the Bank has limited historical data, external benchmark information is used to supplement the internally available data. The portfolios for which external benchmark information represents a significant input into measurement of ECL comprise financial assets as follows:

	Exposure	Exposure		External benchmarks used	
	2021	2020			
	KShs' million	KShs' million		PD	LGD
Balances due from banking institutions	430,979	369,533		Bloomberg PD rating model	Basel II recovery studies
Debt instruments at fair value through other comprehensive income	664,991	724,892		Bloomberg PD rating model	Basel II recovery studies

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

An analysis of changes in the gross carrying amount and the corresponding ECL allowances in relation to the relevant financial assets is as follows:

Year ended 30 June 2021

Debt instruments at fair value through other comprehensive income	Stage 1 Gross carrying amount KShs' million	ECL KShs' million	Stage 2 Gross carrying amount KShs' million	ECL KShs' million	Stage3 Gross carrying amount KShs' million	ECL KShs' million	Total Gross carrying amount KShs' million	ECL KShs' million
At 1 July 2020	724,892	78	-	-	-	-	724,892	78
New assets originated or purchased	394,863	106	-	-	-	-	394,863	106
Asset derecognized or repaid	(476,644)	(27)	-	-	-	-	(476,644)	(27)
Accrued interest	1,028	-	-	-	-	-	1,028	-
Realised gains	(2,420)	-	-	-	-	-	(2,420)	-
Foreign exchange adjustments	29,593	-	-	-	-	-	29,593	-
Changes in risk parameters	-	2	-	-	-	-	-	2
Fair value changes	(6,321)	-	-	-	-	-	(6,321)	-
At 30 June 2021	664,991	159	-	-	-	-	664,991	159

Balances due from banking institutions								
At 1 July 2020	369,533	28			-		369,533	28
Net movement during the year	61,446	(17)	-	-	-	-	61,446	(17)
At 30 June 2021	430,979	11	-	-	-	-	430,979	11

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

An analysis of changes in the gross carrying amount and the corresponding ECL allowances in relation to the relevant financial assets is as follows:

Year ended 30 June 2021

	Stage 1 Gross carrying amount KShs' million	ECL KShs' million	Stage 2 Gross carrying amount KShs' million	ECL KShs' million	Stage3 Gross carrying amount KShs' million	ECL KShs' million	Total Gross carrying amount KShs' million	ECL KShs' million
Securities and advances to banks								
At 1 July 2020	65,114	9,553	-	-	2,147	2,147	67,261	11,700
New assets originated or purchased	368,604	6,421	-	-	-	-	368,604	6,421
Asset derecognized or repaid	(358,048)	-	-	-	(2,147)	(2,147)	(360,195)	(2,147)
Accrued interest	(156)	-	-	-	-	-	(156)	-
Transfer to Stage 3	-	-	-	-	-	-	-	-
Change in risk parameters	-	-	-	-	-	-	-	-
At 30 June 2021	75,514	15,974	-	-	-	-	75,514	15,974
Other assets								
At 1 July 2020	492	-	-	-	4,970	4,962	5,462	4,962
New assets originated or purchased	177	-	-		-	-	177	-
Asset derecognized or repaid	(311)	-	-	-	-	-	(311)	-
Transfer to Stage 3	(17)	-	-	-	17	17	-	17
At 30 June 2021	341	-	-	-	4,987	4,979	5,328	4,979
Loans and advances								
At 1 July 2020	3,172	4	11	-	3,544	3,449	6,727	3,453
New assets originated or purchased	781	3	-	-	-	-	781	3
Asset derecognized or repaid	(868)	(3)	-	-	(61)	(26)	(929)	(29)
Transfer to Stages	(33)	-	(5)	-	38	16	-	16
Changes in risk parameters	-	5	-	-	-	-	-	5
At 30 June 2021	3,052	9	6	-	3,521	3,439	6,579	3,448

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

An analysis of changes in the gross carrying amount and the corresponding ECL allowances in relation to the relevant financial assets is as follows:

Year ended 30 June 2020

Debt instruments at fair value through other comprehensive income	Stage 1 Gross carrying amount KShs' million	ECL KShs' million	Stage 2 Gross carrying amount KShs' million	ECL KShs' million	Stage3 Gross carrying amount KShs' million	ECL KShs' million	Total Gross carrying amount KShs' million	ECL KShs' million
At 1 July 2019	504,533	61	-	-	-	-	504,533	61
New assets originated or purchased	556,932	45	-	-	-	-	556,932	45
Asset derecognized or repaid	(365,842)	(17)	-	-	-	-	(365,842)	(17)
Accrued interest	775	-	-	-	-	-	775	-
Realised gains	1,296	-	-	-	-	-	1,296	-
Foreign exchange adjustments	18,746	-	-	-	-	-	18,746	-
Changes in risk parameters	-	(11)	-	-	-	-	-	(11)
Fair value changes	8,452	-	-	-	-	-	8,452	-
At 30 June 2020	724,892	78	-	-	-	-	724,892	78
Balances due from banking institutions								
At 1 July 2019	542,964	115			-		542,964	115
Net movement during the year	(173,431)	(87)	-	-	-	-	(173,431)	(87)
At 30 June 2020	369,533	28	-	-	-	-	369,533	28

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

An analysis of changes in the gross carrying amount and the corresponding ECL allowances in relation to the relevant financial assets is as follows:

Year ended 30 June 2020

Securities and advances to banks	Stage 1 Gross carrying amount KShs' million	ECL KShs' million	Stage 2 Gross carrying amount KShs' million	ECL KShs' million	Stage 3 Gross carrying amount KShs' million	ECL KShs' million	Total Gross carrying amount KShs' million	ECL KShs' million
At 1 July 2019	68,698	2,092	-	-	1,211	908	69,909	3,000
New assets originated or purchased	199,313	-	-	-	-	-	199,313	-
Asset derecognized or repaid	(202,113)	-	-	-	-	-	(202,113)	-
Accrued interest	152	-	-	-	-	-	152	-
Transfer to Stage 3	(936)	-	-	-	936	-	-	-
Change in risk parameters	-	7,461	-	-	-	1,239	-	8,700
At 30 June 2020	65,114	9,553	-	-	2,147	2,147	67,261	11,700
Other assets								
At 1 July 2019	322	-	-	-	4,953	4,945	5,275	4,945
New assets originated or purchased	427	-	-		-	-	427	-
Asset derecognized or repaid	(240)	-	-	-	-	-	(240)	-
Transfer to Stage 3	(17)	-	-	-	17	17	-	17
At 30 June 2020	492	-	-	-	4,970	4,962	5,462	4,962
Loans and advances								
At 1 July 2019	3,237	7	25	-	3,557	3,449	6,819	3,456
New assets originated or purchased	812	1	-	-	-	-	812	1
Asset derecognized or repaid	(858)	(2)	(8)	-	(38)	-	(904)	(2)
Transfer to Stages	(19)	-	(6)	-	25	-	-	-
Changes in risk parameters	-	(2)	-	-	-	-	-	(2)
At 30 June 2020	3,172	4	11	-	3,544	3,449	6,727	3,453

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Concentrations of credit risk

The Bank monitors concentrations of credit risk by geographic location and by counterparty type. An analysis of concentrations of credit risk is shown below.

Concentration by geographical location is based on the country of domicile of the issuer of the security. Concentration by counterparty type is based on the nature of the institution such as foreign governments, central banks and supranational institutions.

A segregation of the financial assets by geography is set out below:

Year ended 30 June 2021

	United States of America KShs' million	Germany KShs' million	United Kingdom KShs' million	Singapore KShs' million	Canada KShs' million	Kenya KShs' million	Others KShs' million	Total KShs' million
Balances due from banking institutions	151,636	49,961	24,900	13,792	31,731	7,467	151,492	430,979
Funds held with IMF	2,201	-	-	-	-	-	-	2,201
IMF On-Lent to GOK	-	-	-	-	-	160,638	-	160,638
Securities and advances to banks	-	-	-	-	-	75,514	-	75,514
Loans and advances	-	-	-	-	-	6,579	-	6,579
Debt instruments at fair value through OCI	588,033	12,235	-	-	2,844	-	61,879	664,991
Other assets - Sundry debtors	-	-	-	-	-	5,328	-	5,328
Due from Government of Kenya	-	-	-	-	-	79,288	-	79,288
Total financial assets	741,870	62,196	24,900	13,792	34,575	334,814	213,371	1,425,518

NOTES TO THE FINANCIAL STATEMENTS (continued) FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Concentrations of credit risk (continued)

A segregation of the financial assets by geography is set out below:

Year ended 30 June 2020

	United States of America KShs' million	Germany KShs' million	United Kingdom KShs' million	Singapore KShs' million	Canada KShs' million	Kenya KShs' million	Others KShs' million	Total KShs' million
Balances due from banking institutions	49,793	54,072	55,934	28,616	14,274	17,227	149,617	369,533
Funds held with IMF	3,255	-	-	-	-	-	-	3,255
IMF On-Lent to GOK	-	-	-	-	-	79,702	-	79,702
Securities and advances to banks	-	-	-	-	-	67,261	-	67,261
Loans and advances	-	-	-	-	-	6,727	-	6,727
Debt instruments at fair value through OCI	604,561	21,573	-	-	3,320	-	95,438	724,892
Other assets - Sundry debtors	-	-	-	-	-	5,462	-	5,462
Due from Government of Kenya	-	-	-	-	-	68,933	-	68,933
Total financial assets	657,609	75,645	55,934	28,616	17,594	245,312	245,055	1,325,765

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Concentrations of credit risk (continued)

A segregation of the financial assets by counterparty type is set out below:

Year ended 30 June 2021

	Balances due from financial institutions KShs' million	Securities and advances KShs' million	Fund held with IMF KShs' million	IMF-On Lent to GoK KShs' million	Loans and advances KShs' million	Fixed Income securities KShs' million	Due from GOK KShs' million	Other assets KShs' million	Total KShs' million
Central Banks	32,777	-	-	-	-	-	-	-	32,777
Foreign Governments	-	-	-	-	-	587,336	-	-	587,336
Supranational Institutions	62,699	-	2,201	-	-	50,600	-	-	115,500
Commercial Banks	335,503	67,450	-	-	3,400	-	-	-	406,353
Foreign Agencies	-	-	-	-	-	18,205	-	-	18,205
Government of Kenya	-	8,064	-	160,638	-	-	79,288	-	247,990
Others	-	-	-	-	3,179	8,850	-	5,328	17,357
	430,979	75,514	2,201	160,638	6,579	664,991	79,288	5,328	1,425,518

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(i) Credit risk (continued)

Concentrations of credit risk (continued)

A segregation of the financial assets by counterparty type is set out below:

Year ended 30 June 2020

	Balances due from financial institutions KShs' million	Securities and advances KShs' million	Fund held with IMF KShs' million	IMF-On Lent to GoK KShs' million	Loans and advances KShs' million	Fixed Income securities KShs' million	Due from GOK KShs' million	Other assets KShs' million	Total KShs' million
Central Banks	37,054	-	-	-	-	-	-	-	37,054
Foreign Governments	-	-	-	-	-	614,959	-	-	614,959
Supranational Institutions	54,484	-	3,255	-	-	79,352	-	-	137,091
Commercial Banks	277,995	59,392	-	-	3,400	-	-	-	340,787
Foreign Agencies	-	-	-	-	-	30,581	-	-	30,581
Government of Kenya	-	7,869	-	79,702	-	-	68,933	-	156,504
Others	-	-	-	-	3,327	-	-	5,462	8,789
	369,533	67,261	3,255	79,702	6,727	724,892	68,933	5,462	1,325,765

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(ii) Market risk

The Bank takes on exposure to market risk, which is the risk that fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk arises from open positions in interest rate, currency and equity, all of which are exposed to general and specific market movements and changes in the level of volatility of market rates or prices such as interest rates, foreign exchange rates and equity prices. The Bank separates exposure to market risk into either trading or non-trading portfolios. Market risk arising from trading and non-trading activities are concentrated in Bank Treasury and are monitored by management with oversight from the Monetary Policy Committee.

Trading portfolios include those positions arising from market-making transactions where the Bank acts as principal with commercial banks or the market.

Non-trading portfolios primarily arise from the interest rate management of the Bank's investment and monetary policy assets and liabilities. Non-trading portfolios also consist of foreign exchange and equity risks arising from the Bank's internally managed debt instruments at amortised cost and World Bank RAMP financial assets.

Interest rate risk

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

The Bank's interest rate risk arises from balances due from banking institutions, securities and advances to banks, debt instruments at FVOCI, loans and advances, due from the Government of Kenya and deposits from bank and Government. Borrowings issued at variable rates expose the Bank to cash flow interest rate risk which is partially offset by cash held at variable rates. Borrowings issued at fixed rates expose the Bank to fair value interest rate risk.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(ii) Market risk (continued)

Interest rate risk (continued)

The tables below summarise the Bank's financial assets and liabilities and analyses them into the earlier of contractual maturity or re-pricing.

At 30 June 2021	1 – 3 months KShs' million	4-12 months KShs' million	1 - 5 years KShs' million	Over 5 years KShs' million	Non-interest bearing KShs' million	Total KShs' million
Assets						
Balances due from banking institutions	430,979	-	-	-	-	430,979
Securities and advances to banks	12,678	143	39,752	22,941	-	75,514
Debt instruments at FVOCI	46,020	200,012	418,959	-	-	664,991
Funds held with International Monetary Fund (IMF)	-	-	-	-	2,201	2,201
Loans and advances	159	473	1,856	691	3,400	6,579
Other assets	-	-	-	-	5,328	5,328
IMF On-lent to GOK	-	-	-	-	160,638	160,638
Due from Government of Kenya	59,279	1,110	4,440	14,459	-	79,288
Total financial assets	549,115	201,738	465,007	38,091	171,567	1,425,518
Liabilities						
Deposits from banks and government	73,589	-	-	-	654,412	728,001
Other liabilities	-	-	-	-	5,952	5,952
Investment by banks	-	-	-	-	-	-
Due to International Monetary Fund (IMF)	-	-	-	-	221,174	221,174
Total financial liabilities	73,589	-	-	-	881,538	955,127
Interest sensitivity gap	475,526	201,738	465,007	38,091	(709,971)	470,391

As at 30 June 2021, increase of 10 basis points would have resulted in a decrease/increase in profit and equity of KShs 470 million (2020: KShs 429 million).

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(ii) Market risk (continued)

Interest rate risk (continued)

At 30 June 2020	1 – 3 months KShs' million	4-12 months KShs' million	1 - 5 years KShs' million	Over 5 years KShs' million	Non-interest bearing KShs' million	Total KShs' million
Assets						
Balances due from banking institutions	369,533	-	-	-	-	369,533
Securities and advances to banks	59,477	552	2,471	4,761	-	67,261
Debt instruments at FVOCI	59,122	385,521	280,249	-	-	724,892
Funds held with International Monetary Fund (IMF)	-	-	-	-	3,255	3,255
Loans and advances	163	428	1,741	995	3,400	6,727
Other assets	-	-	-	-	5,462	5,462
IMF On-lent to GOK	-	-	-	-	79,702	79,702
Due from Government of Kenya	47,259	1,110	4,440	16,124	-	68,933
Total financial assets	535,554	387,611	288,901	21,880	91,819	1,325,765
Liabilities						
Deposits from banks and government	176,494	-	-	-	555,693	732,187
Other liabilities	-	-	-	-	5,343	5,343
Investment by banks	6,997	-	-	-	-	6,997
Due to International Monetary Fund (IMF)	-	-	-	-	151,841	151,841
Total financial liabilities	183,491	-	-	-	712,877	896,368
Interest sensitivity gap	352,063	387,611	288,901	21,880	(621,058)	429,397

As at 30 June 2020, increase of 10 basis points would have resulted in a decrease/increase in profit and equity of KShs 429 million (2019: KShs 379 million).

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(ii) Market risk (continued)

Foreign exchange risk

The Bank takes on exposure to the effects of fluctuations in the prevailing foreign currency exchange rates on its financial position and cash flows. The Monetary Policy Committee sets limits on the level of exposure by currency which is monitored daily.

The table below summarises the Bank's exposure to foreign currency exchange rate risk as at 30 June 2021. Included in the table are the Bank's financial instruments categorised by currency:

At 30 June 2021	USD KShs' million	GBP KShs' million	EUR KShs' million	SDR KShs' million	Others KShs' million	Total KShs' million
Assets						
Balances due from banking institutions	207,710	26,124	21,539	-	175,614	430,987
Debt instruments at FVOCI	664,991	-	-	-	-	664,991
Funds held with International Monetary Fund (IMF)	-	-	-	2,201	-	2,201
Total financial assets	872,701	26,124	21,539	2,201	175,614	1,098,179
Liabilities						
Due to International Monetary Fund (IMF)	-	-	-	221,174	-	221,174
Deposits from banks and government	81,804	3,051	4,519	-	526	89,900
Total financial liabilities	81,804	3,051	4,519	221,174	526	311,074
Net position	790,897	23,073	17,020	(218,973)	175,088	787,105

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(ii) Market risk (continued)

Foreign exchange risk (continued)

At 30 June 2020	USD KShs' million	GBP KShs' million	EUR KShs' million	SDR KShs' million	Others KShs' million	Total KShs' million
Assets						
Balances due from banking institutions	150,714	24,093	33,791	-	160,935	369,533
Debt instruments at FVOCI	724,892	-	-	-	-	724,892
Funds held with International Monetary Fund (IMF)	-	-	-	3,255	-	3,255
Total financial assets	875,606	24,093	33,791	3,255	160,935	1,097,680
Liabilities						
Due to International Monetary Fund (IMF)	-	-	-	151,841	-	151,841
Deposits from banks and government	43,431	2,354	10,641	-	319	56,745
Total financial liabilities	43,431	2,354	10,641	151,841	319	208,586
Net position	832,175	21,739	23,150	(148,586)	160,616	889,094

As at 30 June 2021, if the shilling had weakened/strengthened by 5% against the major currencies with all other variables held constant, the im pact on the Bank's surplus and equity would have been:

- USD KShs 39,545 million (2020: KShs 41,609 million)
- British Pound KShs 1,154 million (2020: KShs 1,087 million)
- Euro KShs 851 million (2020: KShs 1,158 million)
- SDR KShs 10,949 million (2020: KShs 7,429 million).

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

30. FINANCIAL RISK MANAGEMENT OBJECTIVES AND POLICIES (continued)

(iii) Liquidity risk

Prudent liquidity risk management includes maintaining sufficient cash and marketable securities, and the availability of funding from an adequate amount of committed credit facilities. Due to the dynamic nature of the underlying businesses, Treasury maintains flexibility in funding by maintaining availability under committed credit lines.

Management monitors rolling forecasts of the Bank's liquidity reserve on the basis of expected cash flows.

The table below analyses the Bank's financial liabilities that will be settled on a net basis into relevant maturity groupings based on the remaining period at the reporting date to the contractual maturity date. The amounts disclosed in the table below are the contractual undiscounted cash flows. Balances due within 12 months equal their carrying amounts, as the impact of discounting is not significant.

	On demand KShs' million	0 – 3 months KShs' million	4-12 months KShs' million	1 - 5 years KShs' million	Over 5 years KShs' million	Total KShs' million
At 30 June 2021						
Deposits from banks and government	654,412	73,589	-	-	-	728,001
Due to International Monetary Fund (IMF)	-	-	10,264	23,324	187,586	221,174
Lease liability	-	19	21	19	-	59
Other liabilities	-	-	5,952	-	-	5,952
Total financial liabilities	654,412	73,608	16,237	23,343	187,586	955,186
At 30 June 2020						
Investment by banks	-	6,997	-	-	-	6,997
Deposits from banks and government	555,693	176,494	-	-	-	732,187
Due to International Monetary Fund (IMF)	-	963	15,661	16,879	118,338	151,841
Lease liability	-	25	162	32	-	219
Other liabilities	-	-	5,343	-	-	5,343
Total financial liabilities	555,693	184,479	21,166	16,911	118,338	896,587

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

31. FAIR VALUE OF ASSETS AND LIABILITIES

a) Comparison by class of the carrying amount and fair values of the financial instruments

The fair values of fixed income securities, equity investments and securities and advances to banks (rediscounted treasury bonds) are based on price quotations at the reporting date.

Management assessed that the fair value of balances due from banking institutions, funds held with International Monetary Fund, securities and advances to banks (Treasury bills discounted, accrued interest bonds discounted, repo treasury bills & bonds, accrued interest repo, liquidity support framework and due from commercial banks), other assets (sundry debtors), deposits from government and banks and other liabilities approximate their carrying amounts largely due to the short-term maturities of these instruments.

Fair values of the Bank's staff loans and due from Government of Kenya and due to International Monetary Fund are determined by using Discounting Cash Flows (DCF) method using discount rate that reflects the issuer's borrowing rate as at the end of the reporting period. This is shown in the table below:

	2021		2020	
	Carrying Amount KShs' million	Fair value KShs' million	Carrying amount KShs' million	Fair value KShs' million
Financial assets				
Securities and advances to banks (rediscounted treasury bonds)	7,299	7,909	7,513	8,137
Loans and advances	3,131	3,271	3,274	2,218
Due from Government of Kenya	79,288	74,951	68,933	62,992
Financial liabilities				
Due to International Monetary Fund	221,174	90,522	151,841	45,338

b) Fair value hierarchy

The table below shows an analysis of all assets and liabilities measured at fair value in the financial statements or for which fair values are disclosed in the financial statements by level of the fair value hierarchy. These are grouped into levels 1 to 3 based on the degree to which the fair value is observable.

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes equity securities and debt instruments on recognized exchanges.
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices).
- Level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes equity investments and land and buildings with significant unobservable components.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

31. FAIR VALUE OF ASSETS AND LIABILITIES (continued)

b) Fair value hierarchy (continued)

Year ended 30 June 2021	Level 1 KShs' million	Level 2 KShs' million	Level 3 KShs' million
Assets measured at fair value:			
Land and buildings	-	-	24,946
Debt instruments at fair value through other comprehensive income	664,991	-	-
Equity instruments at fair value through other comprehensive income	-	-	10
Gold holdings	106	-	-
Assets for which fair values are disclosed:			
Securities and advances to banks (rediscounted treasury bonds)	7,909	-	-
Loans and advances	-	3,271	-
Due from Government of Kenya	-	74,951	-
Liabilities for which fair values are disclosed:			
Due to International Monetary Fund	-	90,522	-

Year ended 30 June 2020	Level 1 KShs' million	Level 2 KShs' million	Level 3 KShs' million
Assets measured at fair value:			
Property and equipment			
Land and buildings	-	-	23,537
Debt instruments at fair value through other comprehensive income	724,892	-	-
Equity instruments at fair value through other comprehensive income	-	-	10
Gold holdings	106	-	-
Assets for which fair values are disclosed:			
Securities and advances to banks (rediscounted treasury bonds)	8,137	-	-
Loans and advances	-	2,218	-
Due from Government of Kenya	-	62,992	-
Liabilities for which fair values are disclosed:			
Due to International Monetary Fund	-	45,338	-

There were no transfers between levels 1, 2 and 3 in the year.

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

31. FAIR VALUE OF ASSETS AND LIABILITIES (continued)

b) Fair value hierarchy (continued)

The Bank's land and buildings were revalued during the year. The method of valuation of land and buildings is disclosed in note 18(b).

Description of valuation techniques used and key inputs to valuation of assets and liabilities

LEVEL 2	Valuation technique	Significant observable inputs	Range (weighted average) Interest rate
Loans and advances	DCF	Interest rate	12%
Due from Government of Kenya	DCF	Interest rate	7%
Due to IMF	DCF	Interest rate	0.14%
LEVEL 3			
Land and buildings	Market/Income /cost approach	Comparable sales of similar properties in the neighbourhood	-

Reconciliation of the opening balances to the closing balances of the fair values of property and equipment: -

	1 July 2020 KShs' million	Additions KShs' million	Change in Fair value KShs' million	Depreciation charge to profit or loss KShs' million	30 June 2021 KShs' million
Freehold land and buildings	18,354	1,032	869	(752)	19,502
Leasehold land and buildings	5,183	(31)	450	(158)	5,444
	23,537	1,001	1,319	(911)	24,946

The significant unobservable inputs used in the fair value measurement of the Bank's land and buildings are price per acre and estimated rental value per sqm per month and depreciated replacement cost. Significant increases (decreases) in any of those inputs in isolation would result in a significantly lower (higher) fair value measurement.

32. CONTINGENT LIABILITIES AND COMMITMENTS

The Bank is party to various legal proceedings. Based on legal advice, the directors believe that no loss will arise from these legal proceedings.

At 30 June 2021, the Bank had capital commitments of KShs 7,413 million (2020: KShs 5,610 million) in respect of property and equipment purchases.

All the commitments relate to future rent payable for various premises based on the existing contracts and projected renewals. The lease agreements are between the Bank and the landlords and have no provisions relating to contingent rent payable. The terms of renewal vary from one lease to another and may include a written notice to the lessors before the expiration of the leases and the lessors will grant to the lessee new leases of the said premises/properties for a further term as may be mutually agreed by the parties.

The escalation rate varies from property to property and is factored into the operating lease commitment values presented above.

Operating leases - Bank as a lessor

The Bank has entered into operating leases on its land and buildings consisting of certain office buildings. These leases have terms of between one and 30 years. All leases include a clause to enable upward revision of the rental charge on an annual basis according to prevailing market conditions. The lessee is also required to provide a residual value guarantee on the properties. Rental income recognised by the Bank during the year is KShs 49 million (2020: KShs 41 million).

Future minimum rentals receivable under non-cancellable operating leases as at 30 June are as follows:

	2021 KShs 'million	2020 KShs 'million
Within one year	35	68
After one year but not more than five years	-	35
More than five years	-	-
	35	103

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

33. MATURITY ANALYSIS OF ASSETS AND LIABILITIES

The table below shows an analysis of assets and liabilities analysed according to when they are expected to be recovered or settled.

Year ended 30 June 2021	Within 12 months KShs' million	After 12 months KShs' million	Total KShs' million
ASSETS			
Balances due from banking institutions	430,968	-	430,968
Funds held with International Monetary Fund (IMF)	2,201	-	2,201
IMF Funds on – lent to GOK	-	160,638	160,638
Securities and advances to banks	12,821	46,719	59,540
Loans and advances	625	2,506	3,131
Debt instruments at fair value through other comprehensive income	246,032	418,959	664,991
Equity instruments at fair value through other comprehensive income	-	10	10
Other assets	5,541	-	5,541
Gold holdings	-	106	106
Right-of-use asset – leases	-	114	114
Property and equipment	-	33,105	33,105
Intangible assets	-	1,784	1,784
Retirement benefit assets	-	7,639	7,639
Due from Government of Kenya	60,389	18,899	79,288
TOTAL ASSETS	758,577	690,479	1,449,056
LIABILITIES			
Currency in circulation	-	277,129	277,129
Deposits from Banks and Government	728,001	-	728,001
Due to IMF	10,264	210,910	221,174
Other liabilities	6,239	19	6,258
TOTAL LIABILITIES	744,504	488,058	1,232,562
NET ASSETS	14,073	202,421	216,494

NOTES TO THE FINANCIAL STATEMENTS (continued)
FOR THE YEAR ENDED 30 JUNE 2021

33. MATURITY ANALYSIS OF ASSETS AND LIABILITIES (continued)

Year ended 30 June 2020	Within 12 months KShs' million	After 12 months KShs' million	Total KShs' million
ASSETS			
Balances due from banking institutions	369,505	-	369,505
Funds held with International Monetary Fund (IMF)	3,255	-	3,255
IMF Funds on – lent to GOK	-	79,702	79,702
Securities and advances to banks	23,080	32,481	55,561
Loans and advances	591	2,683	3,274
Debt instruments at fair value through other comprehensive income	444,643	280,249	724,892
Equity instruments at fair value through other comprehensive income	-	10	10
Other assets	5,595	-	5,595
Gold holdings	-	106	106
Right-of-use asset – leases	-	222	222
Property and equipment	-	31,618	31,618
Intangible assets	-	1,224	1,224
Retirement benefit assets	-	6,537	6,537
Due from Government of Kenya	48,369	20,564	68,933
TOTAL ASSETS	895,038	455,396	1,350,434
LIABILITIES			
Currency in circulation	-	257,792	257,792
Investments by banks	6,997	-	6,997
Deposits from Banks and Government	732,187	-	732,187
Due to IMF	16,624	135,217	151,841
Other liabilities	5,570	32	5,602
TOTAL LIABILITIES	761,378	393,041	1,154,419
NET ASSETS	133,660	62,355	196,015

Notes

Notes

Central Bank of Kenya

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