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# Monetary Policy Statement June 2003

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## OBJECTIVES OF THE CENTRAL BANK OF KENYA

### Principal Objects of the Bank

The principal objects of the Bank as laid down in the Central Bank of Kenya Act are to:

- (i) formulate and implement monetary policy directed to achieving and maintaining stability in the general level of prices; and
- (ii) foster the liquidity, solvency and proper functioning of a stable market-based financial system.

### Secondary Objects of the Bank

Without prejudice to the generality of the above two principal objects, the Bank's secondary objectives are to:

- (i) formulate and implement foreign exchange policy;
- (ii) hold and manage its foreign exchange reserves;
- (iii) license and supervise authorised dealers in the money market;
- (iv) promote the smooth operation of payments, clearing and settlement system;
- (v) act as a banker and adviser to, and as fiscal agent of the Government; and
- (vi) issue currency notes and coins.

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LEGAL BASIS FOR THE PUBLICATION OF THE  
MONETARY POLICY STATEMENT

This Statement is made pursuant to Section 4(b) of the Central Bank of Kenya Act, which states that:

- (i) The Bank shall at intervals of not more than six months, submit to the Minister a monetary policy statement for the next twelve months which shall:
  - (a) specify the policies and the means by which the Bank intends to achieve the policy targets;
  - (b) state the reasons for adopting such policies and means;
  - (c) contain a review and assessment of the progress of the implementation by the Bank of monetary policy during the period to which the preceding policy statement relates.
  
- (ii) The Minister shall lay every statement submitted under subsection (1) before the appropriate committee of the National Assembly not later than the end of the subsequent session of Parliament after the statement is so submitted.
  
- (iii) The Bank shall:
  - (a) cause every monetary policy statement submitted under subsection (1) and its monthly balance sheet to be published in the Gazette; and
  - (b) disseminate key financial data and information on monetary policy to the public.
  
- (iv) In subsection (ii), the expression ‘appropriate committee’ means the committee of the National Assembly appointed to investigate and inquire into matters relating to monetary policy.

## 1. IMPLEMENTATION OF MONETARY POLICY FOR THE TWELVE MONTHS TO JUNE 2003

### 1.1 Key Elements of the Policy

Inflation control remained the key focus of monetary policy

The monetary policy stance adopted for calendar year 2003 aimed to contain inflation below 5%. It was designed to allow real gross domestic product (GDP) to recover to 3.0% growth in 2003 from 1.1% in 2002 and 1.2% in 2001. The momentum for economic recovery in 2003 was expected to originate from several factors including (1) renewed investor confidence in the economy after conclusion of the general elections in December 2002 and peaceful transition thereafter (2) expected reduction in the cost of transacting business through renewed commitment by the Government to fight corruption and to implement key reforms in various sectors of the economy (3) prospects for resumption of donor support in the second quarter of 2003 and (4) increased access to external markets accruing from a reduction of restrictive trade practices by the country's major trading partners.

The impetus for the higher growth in domestic output was expected from the agricultural sector, supported largely by favorable weather conditions. A spill over to the other sectors through the strong linkages with agriculture was also expected. Lastly, fiscal incentives particularly in reduced duty and VAT rates on raw materials, machinery and other intermediate inputs as contained in the budget for fiscal year 2002/03 were also expected to impact favorably on domestic output.

There was a more expansionary fiscal policy to cater for election pledges made by the new government

With the adoption in February 2003 of a more expansionary fiscal policy stance for the rest of the financial year ending June 2003, the task for monetary policy became more challenging. The expansionary fiscal policy stance resulted from the Government's commitment to universal primary education and more affordable general health care in line with its key election pledges to Kenyans. Reflecting these expenditure developments, the Government projected its budget deficit to widen to Ksh 57bn from Ksh 31.8bn initially projected for the year to June 2003. With donor pledges estimated at Ksh 10.3bn, the balance of Ksh 46.7bn was to be raised from domestic sources.

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Domestic financing of the budget deficit was largely from the non-bank sector

The Government programmed to depend more on the non-bank sector for domestic borrowing. With the share of Central Bank net lending to Government in net domestic credit held at 8-10%, and that of banks' net lending declining gradually from 40.5% in December 2002 to 34% by June 2003, the share of the non-bank sector financing was expected to rise from 51.5% in December 2002 to 58.8% by June 2003. The declining share of bank financing was expected to encourage banks to meet increased credit demands and thus support the programmed expansion in domestic output by the private sector .

The Central Bank set out to pursue prudent monetary policy

Accordingly, the Central Bank geared itself to pursue a monetary policy stance that would help sustain a stable macroeconomic environment . This strategy would maximize the Bank's contribution towards the realization of inflation and GDP growth targets over 2003 and 2004. Interest rates and exchange rates were also key indicators of a stable economic environment. The Bank expected a declining trend of interest rates observed since July 2001 and a relatively stable shilling exchange rate.

Restoration of IMF support was expected in the January-June 2003 period

The expected restoration of relations with the IMF, continued to revive hopes for external budgetary support from Kenya's principal development partners. While Government needed external financial resources to reconstruct and maintain the dilapidated road network and to finance the additional expenditures generated by the provision of free primary education, the restoration of relations with the IMF was critical for the revival of business confidence, which had continued to decline since the suspension of the IMF support in late 2000.

Among the key indicators of economic performance shown in Table 1, the annual growth of money supply (M3X)<sup>1</sup> was to increase from 6.7% in June 2002 to 7.0% by June 2003. Meanwhile, the reserve money<sup>2</sup>, which is the basis for deposit money creation by commercial banks, was projected to increase by 6.6% in the twelve months to June 2003.

**TABLE1: MONETARY PROGRAMME FOR DEC. 2002 - DEC 2003 (Ksh m) 1/**

	2002				2003	
	Mar (Act)	Jun (Act)	Sep (Act)	Dec (Act)	Mar (Proj)	Jun (Proj)
<b>1. Monetary Survey</b>						
Money supply (M3X)	366,051	378,276	387,365	406,009	399,424	404,856
Annual % change	2.1	6.7	8.4	10.2	9.1	7.0
Net Foreign Assets	95,440	97,040	96,992	102,150	99,887	102,075
Annual % change	6.6	6.4	4.6	8.7	4.7	5.2
Net Domestic Assets	270,611	281,236	290,374	303,859	299,537	302,781
Annual % change	0.6	6.7	9.7	10.7	10.7	7.7
<b>2. Central Bank Balance Sheet</b>						
Reserve money	75,779	76,881	78,589	88,453	81,895	81,951
Annual % change	8.2	10.9	12.6	11.8	8.1	6.6
Net Foreign Assets	77,663	77,832	76,165	70,274	79,350	81,690
Annual % change	23.0	16.5	4.1	(7.1)	2.2	5.0
Net Domestic Assets	(1,884)	(951)	2,424	18,179	2,544	261
Annual % change	(127.3)	(138.0)	(172.0)	416.9	(235.0)	(127.4)

1/ Actuals end-months, and expected monthly averages for CBK balance sheet projections

## 1.2 Progress in Implementation of Monetary Policy, January-June 2003

The reserve money program under-performed in the 6 months to June 2003 by exceeding set targets by between 3.1% and 6.9% as shown in Table 2. The excess reserve money originated from net domestic assets (NDA) of the Bank as the net foreign assets (NFA) remained close to the monthly targets except for January and May. Within the NDA, the excess reserve money reflected substantial redemption of treasury bills held by commercial banks under open market operations (OMO) and advances

<sup>1</sup> Broad money supply, M3X, is the intermediate target of Central Bank monetary policy. M3X is defined to include currency held by the non-bank public and Kenya shilling and foreign currency denominated deposits of the non-bank private sector.

<sup>2</sup> Reserve money comprises deposits of banking institutions held with the Central Bank, plus currency in circulation.

Reserve money was above target in the six months to June 2003

to banks. The failure to roll over maturing treasury bills (repos) sold under the OMO was attributed to a tendency to shift to the higher yielding treasury bonds away from the treasury bills and repos bills whose yields were declining, and the reduction in the weekly sales of treasury bills by Government to facilitate restructuring of domestic demand in favor of the longer dated Treasury bond. The weekly volume of the Treasury bills auctioned had been reduced to Ksh 4.6bn in May 2003 from Ksh 5.5bn previously.

TABLE 2. RESERVE MONEY PERFORMANCE JUNE 2002 TO JUNE 2003 1/

	2002		2003					
	Jun	Dec	Jan	Feb	Mar	Apr	May	Jun
<b>1. Liabilities</b>								
Reserve Money								
Actual	76272	86149	85910	85361	84492	83638	84442	87637
Target	76000	83010	83274	81590	81895	81152	80948	81951
Deviation (Ksh. m)	272	3139	2636	3771	2597	2486	3494	5686
(%)	0.36	3.78	3.17	4.62	3.17	3.06	4.32	6.94
<b>2. Assets</b>								
Net Foreign Assets								
Actual	77628	70848	73427	78639	79858	80770	82888	81259
Target	76268	77744	78280	78815	79350	79885	80919	81690
Deviation (Ksh. m)	1360	-6895	-4853	-176	508	885	1970	-430
Net Domestic Assets								
Actual	-1356	15301	12484	6722	4634	2868	1554	6377
Target	-268	5266	4994	2775	2544	1267	29	261
Deviation (Ksh. m)	-1088	10034	7490	3947	2089	1601	1525	6116

Monthly averages  
Source: Central Bank of Kenya

There was a sharp growth in money supply, M3X

Broader domestic liquidity measured by money supply, M3X, increased sharply in the six months to June 2003, thereby exceeding the monthly targets over the first half in 2003 as shown in Table 3.

TABLE 3: EVOLUTION OF SELECTED MONETARY AGGREGATES (ANNUAL PERCENTAGE CHANGES)

	RM		M 3		M 3 X		M 3 X T	
	Act.	Targ.	Act.	Targ.	Act.	Targ.	Act.	Targ.
2001								
Dec	1.8	2.4	2.5	5.7	2.3	5.3	6.1	10.3
2002								
Jan	3.4	2.8	2.0	7.3	0.0	5.4	4.3	9.1
Feb	4.4	2.7	4.4	8.6	3.1	7.0	7.3	10.4
Mar	8.2	2.2	3.9	6.9	2.1	5.2	5.7	8.4
Apr	2.5	2.8	4.2	5.3	2.0	3.4	6.3	7.4
May	8.0	5.7	6.1	5.9	4.8	4.6	7.5	6.8
Jun	10.9	9.7	8.5	6.4	6.7	4.9	8.4	6.3
Jul	16.7	10.4	8.7	4.7	7.6	4.4	8.6	5.7
Aug	5.0	6.6	11.3	5.6	10.9	5.2	11.6	8.5
Sep	12.6	5.3	8.1	5.2	8.4	4.8	10.6	9.0
Oct	6.9	6.3	7.2	1.2	7.0	1.5	9.5	7.4
Nov	9.1	6.4	8.4	1.6	9.6	1.9	13.6	6.5
Dec	11.8	4.9	8.8	6.8	10.2	6.5	12.8	10.3
2003								
Jan	13.4	13.1	10.8	9.6	12.7	9.0	13.8	10.0
Feb	11.7	10.6	9.6	9.3	10.8	8.9	11.7	9.5
Mar	11.0	8.1	9.9	9.5	11.7	9.1	13.1	12.3
Apr	8.0	7.7	7.7	8.1	9.7	7.9	11.9	11.9
May	9.4	5.7	8.5	8.1	10.6	7.9	12.8	12.8
Jun	10.8	6.6	9.3	7.0	10.9	7.0	12.4	11.8

Source: Central Bank of Kenya

At 10.9%, the growth of M3X remained close to the 10.2% annual growth experienced through December 2002 but was well above the 6.5% target expansion for the year to June 2003. A significant part of the monetary expansion originated from the growth of domestic credit to both the Government and the private sectors. It was also boosted by a build up in net foreign assets held by commercial banks.

The budget deficit including grants on a cash basis, widened to Ksh 33.4bn in the year to June 2003 from Ksh 27.9bn the previous year. The widening of the deficit reflected a shortfall in revenue and grants relative to budget targets of Ksh 9.9bn and increase in expenditure to finance the free primary school education program and cover increases in emoluments to public servants. The budgetary developments resulted in Ksh 54.9bn financing requirement of which Ksh 33.9bn was used to fund the budget deficit and make Ksh 13.0bn in net repayment of external debt. The Government raised Ksh 46.9bn of the total financing requirement from the domestic money market, of which commercial banks and the non-banking sectors funded Ksh 34.8bn and Ksh 17.7bn, respectively. However, owing to Ksh 5.6bn reduction in net credit from Central Bank, net credit to Government from banking institutions increased by Ksh 29.1bn or 30.7% and accounted for 70.7% of the Ksh 41.1bn monetary expansion.

Credit to the private sector expanded by Ksh 12.1bn or 4.9%, representing 29.4% of the growth in money supply. It however fell below the 7.2% target expansion. The credit expansion in the current year occurred largely in the July-December 2002 period, by 3.7%, compared to the deceleration to 1.2% growth in bank credit to the sector between January and June 2003. Expansion in the earlier period reflected financing for the expansion of the mobile phone services in the transport and communications sub-sector and pick up in consumer credit during the November-December 2002 festive season. Meanwhile, the slow growth in credit extension to the private sector during the year to June 2003, in general, and the deceleration in the January-June 2003 period, reflect sluggish economic performance and supply side constraints including stringent lending conditions. Bank credit extension to the private sector was inhibited more by structural factors than monetary factors especially in the backdrop of the excessive liquidity in the inter-bank money market. The excess liquidity partly reflected net redemptions of funds initially locked up under OMO repurchase arrangements between the Central Bank and commercial banks, and partly the lowering of the weekly treasury bill auction volume to Ksh

There was slow growth in credit to the private sector



4.6bn in May 2003 from Ksh 5.5bn that prevailed in the 10 months to April 2003. The excess liquidity in the inter bank market, largely on account of inadequate OMO sales of treasury bills, was attributed to the repo rate -Treasury bill rate anchor which made investments in repo transactions less attractive when the 91 days Treasury bill continued to decline from 7.3% in June 2002 through 5.8% in May and 3.0% in June 2003.

Viewed from the assets side, the banking institutions' liquidity remained high during the year with banks liquidity dominated by investments in Government securities and balances both at the Central Bank and among banks. The attraction of Government securities to investors continued to reflect the stronger appeal of the securities in respect of both the potential earnings and safety relative to the private sector securities.

*Considerable upward pressure on domestic prices was experienced in the January-June 2003 period*

As shown in Table 4, the overall inflation increased markedly between January 2003 and May 2003. The overall 12-month inflation surged from 6.5% in January 2003 to a peak of 14.9% in May before easing to 13.7% in June 2003. The temporary pressure on the overall inflation over the first five months of 2003 arose from transitory shortfalls in the supply of basic food items caused by the unfavorable weather conditions in 2002 through the first quarter of 2003, and the upsurge in retail prices of petroleum products caused by the war in Iraq.

**TABLE 4: INFLATION (%)**

	2002					2003						
	Jan	Mar	Jun	Sep	Dec	Jan	Feb	Mar	Apr	May	Jun	
<b>Overall</b>												
12-month <sup>3</sup>	0.4	1.9	2.8	1.8	4.1	6.5	7.5	10.2	11.6	14.9	13.7	
Annual average <sup>4</sup>	4.8	3.5	2.3	1.8	1.9	2.4	3.0	3.7	4.6	5.7	6.6	
<b>Underlying</b>												
12-month	4.1	4.1	3.7	1.7	2.7	3.0	3.4	3.5	3.5	3.2	3.2	
Annual average	5.3	5.1	4.6	3.7	2.9	2.8	2.8	2.7	2.7	2.7	2.7	

Source: Central Bank of Kenya

<sup>3</sup> The rate of change in the CPI over the same month in the previous year, sometimes referred to as the "annual" rate of change.

<sup>4</sup> Percentage change in the average CPI for the last 12 months over the average CPI for the previous 12-month period.

There was restrained pick up in policy sensitive inflation

The 12-month underlying inflation, which is computed by excluding food and energy prices, however, remained stable, rising slightly from 3.0% in January 2003 to 3.5% in March and April 2003 before easing to 3.2% in May and June 2003. The slow rate of the underlying inflation mainly reflects the success in the implementation of monetary policy. It also reflects the appreciation of the shilling against major world currencies.

The upsurge in the prices of petroleum products abated with the ending of the war in Iraq. On the other hand, the supply of basic food items began increasing in June 2003 due to the prevailing favourable weather conditions. Meanwhile, prices of most commodities declined reflecting the reduction in selected excise duties and standard VAT from 18% to 16%. Reflecting these factors, the overall inflation is expected to ease and the underlying to remain low and stable due to sustained implementation of prudent monetary policy over the July to December 2003 period.

## 2 MONETARY POLICY IN THE YEAR TO JUNE 2004

### 2.1 Current Economic Situation

#### 2.1.1 Inflation

As shown above, underlying inflation was successfully confined within the 3.5% target throughout the first half of 2003. The success in keeping underlying inflation at the desired level was attributed mainly to sustained implementation of a prudent monetary policy stance supported by strengthening of the shilling exchange rate which led to lower prices of imports.

#### 2.1.2 Domestic Output

Economic growth performance by sectors indicates good prospects for economic recovery in 2003. Favourable weather conditions experienced across the country and sub-sector specific tax incentives introduced by the Minister in this year's budget statement are expected to spur growth in agriculture in 2003. Over the first six months of 2003 coffee production increased by 42.9% compared with a decline of 22.6% in the first half of 2002. Horticultural crop exports increased by 25.3% in the first four months of 2003. The Kenya Tea Board projects 3.0% output growth in

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2003. With the prevailing weather conditions, bumper harvests of food crops and dairy products are expected.

Economic activity in the manufacturing sector is expected to pick up, driven mainly by the tax incentives introduced by the Minister in this year's budget and by increased supply of raw materials from agriculture. Contrary to expectation, performance in the tourism sector has been remarkable. In spite of adverse travel advisories issued by European and US governments, visitors passing through the Jomo Kenyatta and Moi international airports and by cruise ships increased by 23.3% in the first half of the year, compared with a decline of 17.4% in the first half of 2002.

Mobile phone services continued to be the locomotive for growth in the transport and communications sector. This role is expected to be enhanced by entry of a third operator in the last quarter of 2003. Throughput handled by the port of Mombasa and Kenya Pipeline Company respectively increased by 12.0% and 4.3% in the first half of 2003 compared with declines of 1.7% and 6.6% in a similar period of 2002. Passengers through JKIA increased by 4.3% in the first four months of 2003 compared with 2.2% in a corresponding period in 2002. Cargo carried by Kenya Railways declined by 8.5% in the first half of 2003. The on-going reforms in the sector including the recent re-introduction of railways transport services to Nanyuki imply potential for recovery of railway services.

### 2.1.3 Outlook

*There are high prospects for economic recovery in 2003*

Prospect for the accelerated economic recovery are based on renewed investor confidence in the economy after both the peaceful general elections and transition period, expected reduction in the cost of transacting business through renewed commitment by the Government to fight corruption and to implement key reforms in various sectors of the

economy, and likelihood of the resumption of donor support in 2003. Moreover, increased access to external markets accruing from the reduction of restrictive trade practices by the country's major trading partners will continue to boost economic activity, in general, and the manufacturing sector, in particular.

## 2.2 Monetary Programme for the year to June 2004

### 2.2.1 Objectives

As in the previous year, the Central Bank will continue to pursue a monetary policy that aims to contain inflation at 3.5% while supporting the projected recovery of economic growth to 2.2% by June 2004 from 1.4% estimated in the year to May 2003. Within the envisaged stable macroeconomic framework, the Central Bank projects the exchange rate to depreciate gradually between June 2003 and June 2004. The modest depreciation in the shilling is attributed to domestic demand pressure arising from the programmed economic recovery. It is anticipated that the domestic import driven demand for foreign exchange will subdue pressures to appreciate accruing from increased foreign exchange supply through donor budgetary support and other private inflows on the strength of the resumption of IMF support early in September 2003. Lending interest rate are expected to decline to stability at lower levels during the year.

On the external sector, the Central Bank will build its unencumbered gross foreign exchange reserves to US \$1.2bn by June 2004 from US \$1.0bn as at end June 2003. Most of the build up will be achieved with donor inflows for budgetary support.

A more expansionary fiscal policy stance is projected by the Government in the fiscal year 2003-04 than in the previous year, largely due to additional expenditure arising from new financial commitments on free universal primary education in public schools, increased emoluments for public sector employees, increased allocation to public activity in the building and construction sector for the rehabilitation of the road network and the provision of affordable general health care. As a result, the budget deficit

Prudent monetary policy and stable macro-economic environment is expected to prevail in the year to June 2004

Moderate build up of official foreign exchange reserves with inflows from donor budgetary support is expected

Fiscal policy is to remain expansionary

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including grants on cash basis, is projected to widen from Ksh33.9bn in fiscal year 2002-03 to Ksh 62.4bn in the year to June 2004. The Government programs to finance Ksh 30.0bn from external sources and the balance of Ksh 32.4bn from domestic sources.

Dependence on non-bank sources of domestic financing for the budget...and more bank credit is to be channelled to the private sector

For domestic financing, the Government will depend more on non-bank sources. With the share of Central Bank net lending to Government in net domestic credit being kept at 8%, and the share of banks net lending declining gradually from 44.3% in June 2003 to 37.5% by June 2004, the share of the non-bank lending will rise from 49.9% to 54.5% over the same period. The declining share of bank financing is expected to encourage banks to extend more credit to the private sector and thus support the programmed expansion in domestic output.

A lower cash ratio regime with a wider deposit base was adopted

In the monetary program, the reserve money, which forms the base for money supply, incorporates recent changes in the cash ratio regime contained in the Government Budget for fiscal year 2003-04. The cash ratio was revised from a monthly average of 10% subject to a daily minimum of 8%, to a daily minimum of 6% effective 1<sup>st</sup> July 2003. The cash ratio deposit base was also widened to include residents' foreign currency deposits. Unlike in the past when deposits in the cash ratio account were accessible to banks for intra-day clearing, as long as banks built the balances up to the daily minimum requirement by close of day to avoid penalty on default, the new regime separates the cash ratio account from banks' clearing account at the Central Bank. Balances held in the cash ratio account are no longer available for intra-day trading. The reserve money program therefore features a minimum holding in commercial bank's clearing accounts at the Central Bank for precautionary purposes. These deposits constitute the excess reserves held by commercial banks at the Central Bank.

Provision was made for banks' excess reserves in the clearing account at the Central Bank

Money supply, M3X, is programmed to increase by 6.4% in the year to June 2004

## 2.2.2 Monetary Programme Outlook

Consistent with the projected economic growth, inflation target, budget deficit financing by banking institutions and foreign exchange reserve target, broad money M3X is programmed to increase by 6.4% in the year to June 2004, as shown in Table 5. The monetary expansion will be supported by increases of 7.5% in the NDA and 3.0% in the NFA. With bank lending to Government easing from 30.7% growth in June 2003 to 1.9% in June 2004, NDA expansion will largely reflect bank lending to the private sector. The latter is programmed to accelerate from a growth of 4.9% growth to that of 9.0% over the same period. Meanwhile, the expansion in the NFA is expected wholly in Central Bank holdings on account of inflows from donor budgetary support as well as drawing from the IMF balance of payments support.

TABLE 5: MONETARY PROGRAMME FOR JULY 2003 - JUNE 2004 IN KSH (M) 1/

	2002				2003				2004	
	Mar (Act)	Jun (Act)	Sep (Act)	Dec (Act)	Mar (Act)	Jun (Act)	Sep (Pro)	Dec (Pro)	Mar (Pro)	Jun (Pro)
<b>1. Monetary Survey</b>										
Money supply (M3X)	366,051	378,276	387,365	406,009	408,817	419,419	422,486	433,284	439,481	446,234
Annual % Change	2.1	6.7	8.4	10.2	11.7	10.9	9.1	6.7	7.5	6.4
Net Foreign Assets	95,440	97,040	96,992	102,150	104,537	104,352	97,215	100,030	102,164	107,445
Annual % Change	6.6	6.4	4.6	8.7	9.5	7.4	0.2	(2.1)	(2.3)	3.0
Net Domestic Assets	270,611	281,236	290,374	303,859	304,280	315,067	325,271	333,254	337,317	338,788
Annual % Change	0.6	6.7	9.7	10.7	12.4	12.1	12.0	9.7	10.9	7.5
<b>2. Central Bank Balance Sheet</b>										
Reserve money	75,779	76,881	78,589	88,453	84,113	85,494	86,471	92,619	91,713	92,109
Annual % Change	8.2	10.9	12.6	11.8	11.0	11.2	10.0	4.7	9.0	7.7
Net Foreign Assets	77,663	77,832	76,165	70,274	79,136	81,482	75,964	78,779	80,913	86,194
Annual % Change	23.0	16.5	4.1	(7.1)	1.9	4.5	(0.3)	12.1	2.2	5.8
Net Domestic Assets	(1,884)	(951)	2,424	18,179	4,977	4,012	10,507	13,840	10,800	5,915
Annual % Change	(127.3)	(138.0)	(172.0)	416.9	(364.1)	(537.8)	333.5	(23.9)	117.0	47.4

1/ Actuals end-months, and expected monthly averages for CBK balance sheet projections

Source: Central Bank of Kenya

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### 2.2.3 Monetary Policy Instruments

The Central Bank will continue to manage domestic liquidity largely through open market operations with commercial banks.

The Bank will continue to manage monetary policy using the monetary targeting framework with reserve money (RM) as the operating target. In this regard, the Central Bank will continue to:

- Buy and sell Treasury bills or any other stipulated eligible government paper in the open market through repurchase agreements to influence the level of bank reserves.
- Require commercial banks to hold specified minimum cash deposits at the Central Bank, currently equivalent to 6% of their deposit liabilities.
- Provide, as a lender of last resort, liquidity to commercial banks but in a manner that will not compromise the monetary policy stance adopted for the year.

### 3 CONCLUSION

The Bank will provide a stable macro-economic framework in support of the envisaged economic recovery.

Sustained implementation of a prudent monetary policy by the Central Bank coupled with a relatively sound fiscal policy stance has enabled the economy to enjoy a stable macroeconomic situation for some years now. Even then, the economy has continued to perform below expectations. A major challenge is, therefore, to translate the stable macroeconomic environment into tangible and sustainable economic growth. On its part, the Central Bank will strive to ensure that low and stable inflation and a sound banking system are maintained.