

## KENYA

*Kenya lies in the highlands of East Africa with a coast on the Indian Ocean. Area: 582,644 km<sup>2</sup>. Population (1969 census): 10,890,000. Formerly a British colony, Kenya gradually became self-governing from 1961 and on 12 December 1963 became independent, remaining in the Commonwealth. Thriving agriculture (coffee, textile fibres and tropical fruit) and animal husbandry (about 8 million heads of cattle and as many sheep), with cheese manufacture and exports.*

### ORIGINS OF THE CENTRAL BANK

Encouraged by the success of the West African Currency Board<sup>1</sup>, the British colonial authorities decided to make similar arrangements for their East African dependencies, in order to lay the foundations of an orderly monetary system in these territories.

Accordingly, they set up the East African Currency Board in December 1919, which was to issue a common currency for Kenya and Uganda, the East African shilling, against sterling balances held in London. Part of these balances could be invested in government stock of the United Kingdom or other industrialized countries of the British Empire. In 1920, the area of the East

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<sup>1</sup> See under the heading NIGERIA.

African Currency Board was extended to Tanganyika, in 1936 to the island of Zanzibar and, during the second world war, to British Somaliland, to Aden and ultimately to the territories formerly belonging to Italian East Africa.

Initially, the East African Currency Board was exclusively concerned with the exchange of the currency of its own issue against sterling and *vice versa*. The circulation of bank notes, therefore, increased and decreased in close accordance with balance-of-payments surpluses or deficits.

After the second world war, the rigid mechanism of the Currency Board proved more and more inadequate to the monetary requirements of the territories concerned. As the use of money spread from an initially small class of business men mostly engaged in international trade to the African population at large, the sterling exchange standard had to be abandoned and currency management introduced. In September 1955 the Currency Board was, within certain limits, authorized to make fiduciary issues by buying securities issued or guaranteed by any of the governments in the Board's area.

Under the strain of post-war political vicissitudes, the currency union gradually crumbled. Ethiopia started issuing its own money in 1945; ex-Italian Somaliland withdrew in 1950 and in 1961, after its union with the former British Somaliland, founded a central bank of its own and issued a new currency. One after the other, the British dependencies in East Africa gained their independence within the Commonwealth; first Tanganyika in December 1961, then Uganda in October of the following year, and finally Zanzibar and Kenya. On 25 April 1964, Tanganyika and Zanzibar joined to form the United Republic of Tanzania, which, on 6 January 1966, set up its own central bank by the Bank of Tanzania Act.

Kenya and Uganda followed this example in May 1966, and that was the end of the East African Currency Board and the monetary union over which it presided.

#### ORGANIZATION OF THE CENTRAL BANK

The Central Bank of Kenya was established on 23 May 1966 and began its activities on 14 September of the same year with the first issue of the new national currency, the Kenya shilling. The capital of 26 million Kenya shillings was entirely subscribed by the government, which also appoints the Bank's top-ranking officers.

The highest authority of the Central Bank is its Board of Directors, which consists of the Governor, who is its chairman, the Deputy Governor, the Permanent Secretary to the Treasury and four directors. The members of the Board are appointed by the President of the Republic for terms of four years each and are eligible for reappointment. The Board of Directors has overall responsibility for the management of the Bank and for monetary and credit policy. The Governor, in his turn, has specific personal responsibilities as regards continuity in the management of the bank and supervision of its activities.

#### FUNCTIONS OF THE CENTRAL BANK

In the words of the law, the principal objects of the Central Bank of Kenya are to regulate the issue of notes and coins, to assist in the development and maintenance of a sound monetary, credit and banking system in Kenya conducive to the orderly and balanced economic development of the country and the external stability of the currency, and to serve as banker and financial adviser to the government. The Bank has the monopoly of issuing money

having force of legal tender in Kenya, at any rate since the notes and coins of the East African Currency Board ceased to be legal tender on 14 September 1967, after a year during which they could be exchanged at par for the new Kenya shilling. The Central Bank is, furthermore, responsible for exchange control and the management of the country's foreign exchange reserves, which must at all times cover a specified proportion of annual average imports.

#### THE CENTRAL BANK'S RELATIONS WITH THE STATE

The Central Bank of Kenya acts as the government's banker in two respects. First of all, it takes care of most of the cash transactions and credit operations connected with the budgets of the state and other public authorities, either through its own branches or, in localities where it has none, through commercial banks acting, for this specified purpose, as the Central Bank's agents.

Secondly, it helps in balancing the public finances both by direct lending to the Treasury and by measures designed to ensure the placing, and support the price, of public loan stocks, especially Treasury bonds. The Bank is authorized to make direct advances to the government at a rate of interest not less than 3 per cent and without any time limit, and also to purchase government securities and other public securities guaranteed by the government and to accept them as collateral for advances to commercial banks. The sum of these three items may not exceed 240 million Kenya shillings at any time, nor may the Bank hold more than 60 million shillings' worth of securities with a maturity of more than 12 months.

The Central Bank, finally, administers the public debt, by issuing, paying interest on and redeeming government securities. Among the latter, 91-day Treasury Bills are important as a means

of stimulating active dealings on the credit market and, once this is well established, as a basis for open market operations and refinancing by the Central Bank. The success of Treasury Bill issues is assured by the Central Bank, which takes up any part of an issue which is not subscribed by the public, the banking system and other financial intermediaries, and which also rediscounts them for commercial banks and accepts them as collateral for advances to them, at a rate 0.50 points above that of the latest issue.

#### MONETARY AND CREDIT POLICY

Monetary stability is one of the prime objectives of the Central Bank, which, for purposes of credit control, has powers to instruct commercial banks to maintain certain liquidity ratios either of specified assets, or of the banks' cash balances deposited at the Central Bank, to their total deposit liabilities. In exceptional cases the Bank may pay interest on the cash balances the banks deposit with it under the reserve requirements.

The Central Bank of Kenya acts as the bankers' banker and refines them mainly by rediscounts and advances against securities. It accepts for rediscount only bills maturing within 180 days from the date of rediscount, or, if they relate to industrial or agricultural production, within 270 days. Advances may be granted for not more than 6 months, and are most often secured on negotiable securities issued or guaranteed by the government.

Finally, the Central Bank of Kenya has powers to issue instructions to commercial banks and other financial intermediaries regarding the volume and conditions of their credits, as well as to fix maximum rates of interest payable on different categories of deposits.



## THE BANKING SYSTEM

The decision of the three ex-British East African countries in 1965 to dissolve the monetary union under the East African Currency Board, had its bearing on the structure and functions of their commercial banking system. Until then, the banking systems of the three countries had close connections among themselves and all of them were largely dependent on the Kenya branches of British banks. These were, in fact, the main channel through which financial funds flowed from the economy of Kenya to Tanzania and Uganda on the one hand, and to Great Britain on the other. With the achievement of full independence and the dissolution of the monetary union, each country's banking system reshaped itself with particular reference to the requirements and the development of the local economy.

Kenya's banking system consists of commercial banks, the Post Office Savings Bank and, for industrial credit and for medium- and long-term loans, a development bank called Co-operative Bank of Kenya Ltd.

The commercial banks accept money on current account, on which they pay no interest, and on deposit accounts either as demand or time deposits. The latter bear interest at rates varying between 3 and 4.50 per cent, depending on their amount and the length of time for which they are tied. The Post Office savings banks specialize on savings deposits. Commercial bank credit goes in large part to finance foreign trade; it may be for the short or the medium term and mostly takes the form of credit lines on current account, discount of bills and advances against securities.

There are many public financial institutes which promote and finance fixed investment in agriculture, industry and housing. Agricultural investment is the special province of the Land and

Agricultural Bank, the Agricultural Finance Corporation, the Agricultural Development Corporation and the Cereals and Sugar Finance Corporation; for industry, there are the Development Finance Company of Kenya Ltd., and the Industrial and Commercial Development Corporation; housing credits come from the National Housing Corporation of Kenya and the Housing Finance Company of Kenya Ltd., and there are also building societies.

#### BANKING REGULATIONS

Banking activities in Kenya are governed by a banking act which came into force on 3 June 1969 and replaced an earlier dating from 1956. The new law was designed especially to strengthen safeguards for depositors and to fit bank activities into monetary and credit policy by aligning them with the aims and functions of the Central Bank and making them subject to supervision by the latter.

Banking is subject to government licence and to a minimum capital requirement of 100,000 Kenya pounds. The sum of any bank's paid-up capital and reserves may never be less than 5 per cent of its total deposit liabilities. Banks are, finally, required to maintain a specified liquid assets/deposits ratio, liquid assets including legal tender, balances held at the Central Bank, Treasury Bills and other easily negotiable foreign and domestic assets.

The Central Bank has powers to vary the proportion and composition of compulsory reserves, and this helps it in supervising the banking system. Banks are obliged to submit periodic reports to the Central Bank on their liquidity position and, in case they are unable to comply with the reserve requirements, must obtain its prior approval for further credit operations.

The Banking Act finally prohibits banks from granting any advance or credit facility against the security of their own shares, and from granting unsecured credit in excess of 500 Kenya pounds to any of their officers, or in excess of one year's emoluments to any of their employees. No single client may be extended credit exceeding 5 per cent of the lending bank's total deposit liabilities or 100 per cent of its paid-up capital.

Share capital in any company may be taken up only in a maximum amount of 25 per cent of a bank's paid-up capital and published reserves, and bank mergers are subject to approval by the Finance Minister.