CAPTAIN OF INDUSTRY PROFILES
Kenya's Golden Hands

Kenyans reaping from key monetary reforms under Professor Ndung'u at CBK

Professor Njuguna Ndung'u
Governor of the Central Bank of Kenya

BY JACKSON OKOTH

Since his appointment as governor of the Central Bank of Kenya, in March 2007, Professor Njuguna Ndung'u has steered the institution towards implementation of various reforms that have resulted in a vibrant and most modern monetary system in the region.

Upon his appointment, Professor Ndung'u committed to prioritize policies that would enable CBK support the Government's development goals as espoused in Vision 2030.

IMPROVED MONETARY POLICY COORDINATION

The monetary policy stance adopted since 2007 has been successful as reflected by robust economic growth, a low and stable inflation regime and decreased volatility in the interbank rate.

In addition, the Central Bank Rate (CBR) has effectively co-ordinated movement in short-term interest rates that has made CBR gain acceptance as a signaling mechanism for the monetary policy stance. Indeed, the financial markets eagerly await the announcement from the Monetary Policy Committee (MPC) meetings on the CBR. Monetary policy communication has been enhanced through the regular meetings between the MPC and Chief Executive Officers (CEOs) of commercial banks, the media and MPC market perception surveys targeting banks and the real sector.

Along the way, however, the effective discharge of this mandate was slowed by challenges that were not foreseen. First, the post –election disruptions in early 2008 derailed the economy from its high growth trajectory that had been recorded since 2003. Secondly, the subprime mortgage in the US, the euro crises in the Euro zone and the MENA (Middle East & North Africa) political crises, precipitated economic shocks that negatively affected the economy. Nevertheless, the Bank rapidly mobilized the tools of monetary policy to ensure that neither the post-election problems nor the international financial problems became embedded in the Kenyan economy. The effectiveness of the monetary policy actions has also been improved through regular review of the monetary policy framework to facilitate transmission efficiency and reduce transmission lags. By scaling up financial inclusion, deepening the financial and bond markets, the initiatives to improve the transmission of monetary policy impulses have borne fruit.

FINANCIAL SECTOR REFORMS

Kenya can boast of having a dynamic financial sector that has grown notably in the last decade. The key reason for this growth has been a commitment to financial sector reforms by the Government, through its Economic Recovery Strategy (ERS), 2003 – 2007 and the current economic blue print, Kenya Vision 2030; and various financial sector initiatives aimed at enhancing the sector's growth and development. Central Bank of Kenya, in line with its financial sector mandates under these reforms, has been in the forefront in pushing for more affordable financial services for Kenyans while maintaining the stability, efficiency and integrity of the financial system.

The banking sector, under the oversight of the Central Bank of Kenya, has contributed to this growth and development, positively transforming the lives of millions of Kenyans. This has been witnessed by a significant growth of banking sector service points which have exponentially grown over the years. This includes the dramatic multiplication in the number of customer deposit accounts; with majority being micro-accounts holding less than Ksh 100,000. The effects of these transformations have been felt in increased levels, reach and depth of access to financial services in the country and by extension the growth and development of Kenya's economy. In 2002, only about one million Kenyans had access to banking services and by the end of 2012, more than 20 million Kenyans had access to banking services.

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Retired President H.E. Mwai Kibaki launching the book, 'Kenya: Policies for Prosperity', in February 2011. The book was edited by the Professor Njuguna Njugung'u, Paul Collier and Chris Adams, and tackles contemporary economic policy issues in Kenya.

These remarkable indicators were made possible through specific financial sector policy & regulatory reforms and attempts to further build the financial infrastructure under the ambit of the Central Bank. They include:

a) Licensing of deposit taking microfinance institutions (DTMs) to serve the lower end of the Kenyan populace, particularly small and micro enterprises and low income populations1 previously locked out of the formal financial sector.
b) Introduction of agency model for banks and deposit taking microfinance institutions in 2009 and 2012, respectively, to permit banks and deposit taking microfinance institutions to offer specified banking services through third parties (agents), to push forward financial inclusion frontiers in un-served areas. This has led to more than 18,000 approved bank agents' facilitating over 51 million transactions valued at over Ksh 268 billion leveraging on mobile phone technology. Agency banking is an initiative that CBK expects to propel the levels of formal financial inclusion.
c) Facilitation of mobile phone financial services (MFs); With over 20 million people served by over 60,000 agents handling over USD 40 million worth of MFS transactions per day in Kenya, the provision of mobile phone finance services, which started in 2007 in Kenya is now celebrated all over the African continent and the world over. All these, with the stability and integrity of the financial system remaining intact. A trend setter in Africa, Kenya's mobile finance services solution has played a significant role in increasing access to financial services to Kenyans cost effectively.
d) Entrenching Credit Information Sharing to expand access to credit by tackling the twin problems of information asymmetry (moral hazards and adverse selection) and lack of physical collateral. Lenders are able to obtain a comprehensive credit history of borrowers at fairly reasonable cost than before.
e) The development of the Infrastructure Bond Program; The infrastructure bonds target infrastructure projects in each fiscal year under the Public Investment Program. In collaboration with the Treasury, the Bank has issued 20-year, 25-year and 30-Year bonds. The 30-Year Bond is specially intended to support the buildup of national savings, as envisaged in the Vision 2030. The proceeds are used in development of social and economic infrastructure including the implementation of the new Constitution.
f) Lowering cost of doing business: Currency Centres have been established in Nyeri, Nakuru and Meru. This is the first phase whose collaboration with Kenya Bankers Association has seen the CBK partner with commercial banks to distribute currency and lower transactions costs .
g) Deposit Insurance Mechanism: The Central Bank has spearheaded the development and transition in the Kenya deposit insurance system through the enactment of the Kenya Deposit Insurance Act, 2012, which will establish the Kenya Deposit Insurance Corporation (KDIC).
h) The Central Bank has implemented and facilitated other innovative solutions including; the introduction of shariah compliant banking products; modernisation of the payments, settlements and clearing systems; and extension of the maturity profile of the Government Debt as the appointed fiscal agent.

Despite these remarkable developments in the Kenyan financial sector, there still remains great need for further investment and growth of the financial sector. Towards this end, investments in building innovative solutions will continue to remain critical. Deepening the financial sector will reduce costs of doing business and cost of funds to facilitate investments.

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Professor Ndung'u, the face behind Kenya's financial stability and vibrancy

BY JACKSON OKOTH

It is a chilly and cloudy Wednesday morning, at 9.45 am as we are quickly taken through stringent security checks before being ushered into a waiting lounge located in the executive wing of the Central Bank of Kenya (CBK). After a brief meeting with protocol officials, we soon step into the expansive office of a jovial Professor Njuguna Ndung'u, the Governor, and a conversation revolving around the country's bubbling financial sector infrastructure begins almost immediately. "I first reported at the CBK on a Sunday where I got a brief from the then Permanent Secretary at the Treasury. That was all. There were no handover notes and, therefore, I had to find where to begin from," said Prof. Ndung'u. These are his immediate recollections on his impressions and feelings when he reported for duty on March 4th, 2007. He now looks back and in retrospect, says that this is a tradition that he may have to break away from when his time to make an exit comes.

It is through interaction with departmental heads and operational directors that Professor Ndung'u, an accomplished economist, teacher and trainer was able to compass through the maze that he had inherited. An academic, who had spent most of his time in teaching and researching in policy areas, Professor Ndung'u was rather surprised when he was spotted to run affairs at the CBK. Upon settling down, Professor Ndungu immediately put his energies into driving a monetary policy agenda for Kenya. This was a familiar territory for the Professor who had immensely continued in setting up the Kenya Institute for Public Policy Research and Analysis (KIPPRA), an autonomous government think tank established in May 1997. "It is the macro model for Kenya, which we created at KIPPRA in 2000, that is still in use at the Treasury today," said Professor Ndung'u. It was first adopted by the then Finance Minister Chris Okemo, who used this model to drive its growth, tax revenue and fiscal strategy.

It was also during this period that the Donde Bill, legislation crafted by parliament seeking to control the level of interest rates charged on loans by commercial banks, was drafted. But Professor Ndungu advised against it and as a result it fell apart.

Prof Ndung'u is an Associate Professor of Economics at the University of Nairobi and holds a PhD in economics from the University of Gothenburg, Sweden, and Master's and Bachelor's degrees in Economics from the University of Nairobi.

"I have written papers covering several topics including dynamics of inflation in Kenya during my PhD thesis, works that have also be adopted by the International Monetary Fund," said Professor Ndung'u.

To be in charge of Kenya's top monetary policy organ and supervisor of the country's financial infrastructure has not spared Professor Ndung'u all challenges that come with the job.

He cites numerous situations during the past grand coalition government when it was difficult to separate friends from enemies.

Although some of the policy actions taken by CBK have had intense public reactions, Professor Ndung'u insists that policy measures by the institution need not be popular. "All measures we take will always end up being popular with some people while hurting others. It is not possible to occupy a neutral position or have a policy that does not affect anyone," said Professor Ndung'u.

There are times when the public reacts fiercely when the CBK allows the Kenya Shilling to depreciate, denying then opportunity to import luxury goods cheaply.

Apart from a stable exchange rate and eliminating currency speculators,

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Professor Ndungu is also credited with licensing more microfinance institutions, thereby bringing more Kenyans to the financial sector.

CBK has been pushing the concept of microfinance institutions to link up numerous small and medium-sized enterprises with the credit market. While major commercial banks have given the informal sector a wide berth, citing the huge risks involved in lending to this segment, microfinance institutions have come in to fill the void.

It has also been under Professor Ndung'u's watch that commercial banks have been able to shed off their brick and mortar models and linked up with agents. Kenyans are now able to perform basic banking functions such as withdrawals or deposits without visiting a physical banking hall.

CBK is also credited with giving space to mobile phone companies to run electronic money transfer services. All operators have a mobile cash transfer service platform, attracting the attention of commercial banks that have reacted by integrating their systems with these platforms.

"We have Mpesa, a platform for payment of goods and services, which has one of the best turnaround times in the world," said Professor Ndung'u.

In the past, lenders have had no information on their customers leading to a huge premium loaded on loan applications. But CBK has now licensed credit reference bureaus, solving the information asymmetry that has been affecting both borrowers and lenders.

In December 2009, Professor Ndung'u was awarded the order of the Burning Spear by the State. This was in recognition of his efforts to design an infrastructure bond programme, which became a vital source of funding during the height of the global financial crisis. He receives invitations to attend seminars and workshops the world over to explain how infrastructure bonds are designed and work.

It is also under his watch that CBK has been able to set up more currency centres in the country, a fact that has lowered cost of doing business for commercial banks. In the past, currency centres were only in Mombasa, Kisumu and Eldoret.

"We have since established currency centres in Nyeri, Nakuru and Meru, reducing the need for banks to come all the way to Nairobi for cash," said Professor Ndung'u.

The Deposit Insurance Fund has also had its mandate expanded to include risk minimization and resolution of problem banks. DPF offers protection to depositors holding upto Sh 100,000 in the bank account. This size of a depositor comprises 94 per cent of all the 17 million deposit accounts within the banking system.

The Governor also explained why banks do not respond quickly to CBK signals when asked to review interest rates on loans.

"The CBR can only be used as a negotiating tool but a borrower must also present a business proposal complete with rate of return on investment. The quality of collateral being offered also determines the rate of interest that a bank will charge," said Professor Ndung'u.

He explains that the role of monetary policy is like that of putting oil in a car or greasing the economy. "Most borrowers take up credit for consumption and this is a disaster. Even when interest rates are low, most people have no clue on how to negotiate with the banks," said Professor Ndung'u.

An accomplished scholar, Professor Ndung'u says he intends to write books on many topics after leaving the CBK. His second four-year term comes to a close in March 4th, 2015.

Professor Njuguna Ndung'u during the official launch of one of the currency centres outside Nairobi. [Pictures: Jonah Onyango]

GLANCE BOX

- Prior to his appointment as Governor of the Central Bank of Kenya, Prof. Ndung'u was the Director of Training at the African Economic Research Consortium. He has lectured in advanced economic theory and econometrics at the University of Nairobi, where he earned the title of Associate Professor of Economics.
- He also worked as the Regional Programme Specialist for the Eastern and Southern Africa Regional Office, Nairobi, of the International Development Research Centre (IDRC), Canada; and at the Kenya Institute for Public Policy Research and Analysis (KIPPRA) as a Principal Analyst/Researcher and Head of the Macroeconomic and Economic Modeling Division.

Prof. Ndung'u has had extensive research and teaching work in various fields of economics, including macroeconomics, microeconomics, econometrics and poverty reduction.

- He has published in international journals as well as chapters in various books on economic policy issues, inflation, interest rate and exchange rate issues, financial management, public sector growth, external debt, financial liberalization in Anglophone Africa, structural adjustment, as well as on employment and labour market issues.