REPUBLIC OF KENYA

MINISTRY OF FINANCE

MONTHLY DEBT BULLETIN

MAY 2012

1.0 PUBLIC DEBT

1.1 Introduction

As at end May 2012, public and publicly guaranteed debt stood at Kshs 1,609.90 billion or 48.9 percent of GDP (see Table 1). The increase of 0.81 percent over the end April 2012 position is attributed to depreciation of the Kenya shilling and increased disbursements from external creditors. External debt rose by Ksh 20.14 billion to stand at Ksh 721.04 billion, while domestic debt declined by Ksh 7.18 billion to stand at Ksh 888.86 billion in May 2012. (See Table 1).

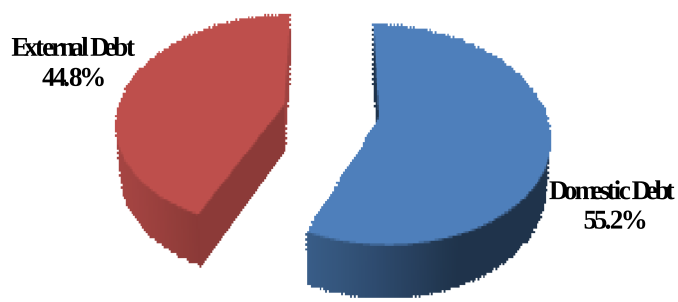
Table 1: Size of public debt, in billion

Debt Category	Kshs	USD
Domestic Debt	888.86	10.24
External Debt	721.04	8.30
Total	1,609.90	18.54

Source: Ministry of Finance

The structure of public and publicly guaranteed debt shows that 55.2 percent of the total debt is domestic debt while the rest is external debt as shown in Chart 1.

Chart 1: Composition of public debt



Source: Ministry of Finance

1.2 Cost/Risk Characteristics of Public Debt

Reflecting Government external debt strategy of contracting or guaranteeing external loans with highly concessional terms to minimise interest rate cost, the average interest rate and grace period on the external debt portfolio was 0.8 percent and 7.2 years, respectively. In addition, the average maturity period for external loans was 26.1 years while the average grant element was 63.4 percent.

As an indication of the success in lengthening the maturity structure of domestic debt to minimise refinancing risk in line with the Medium Term Debt Strategy, the average maturity profile of outstanding Government domestic debt stood at 5 years 4 months at end May 2012.

1.3 Movement in Exchange Rates

Table 2 shows market indicative end-month foreign exchange rates for the period March 2012 to May 2012. The Kenya shilling appreciated against the Sterling Pound and the Euro by 0.7 percent and 2.4 percent respectively and and depreciated against the USD Dollar and the Japanese Yen by 4.3 percent and 6.1 percent respectively. The Kenya shilling stood at Kshs 86.83 to the US Dollar at end May 2012. These movements have implications on both the size of the external debt and the cost of debt service.

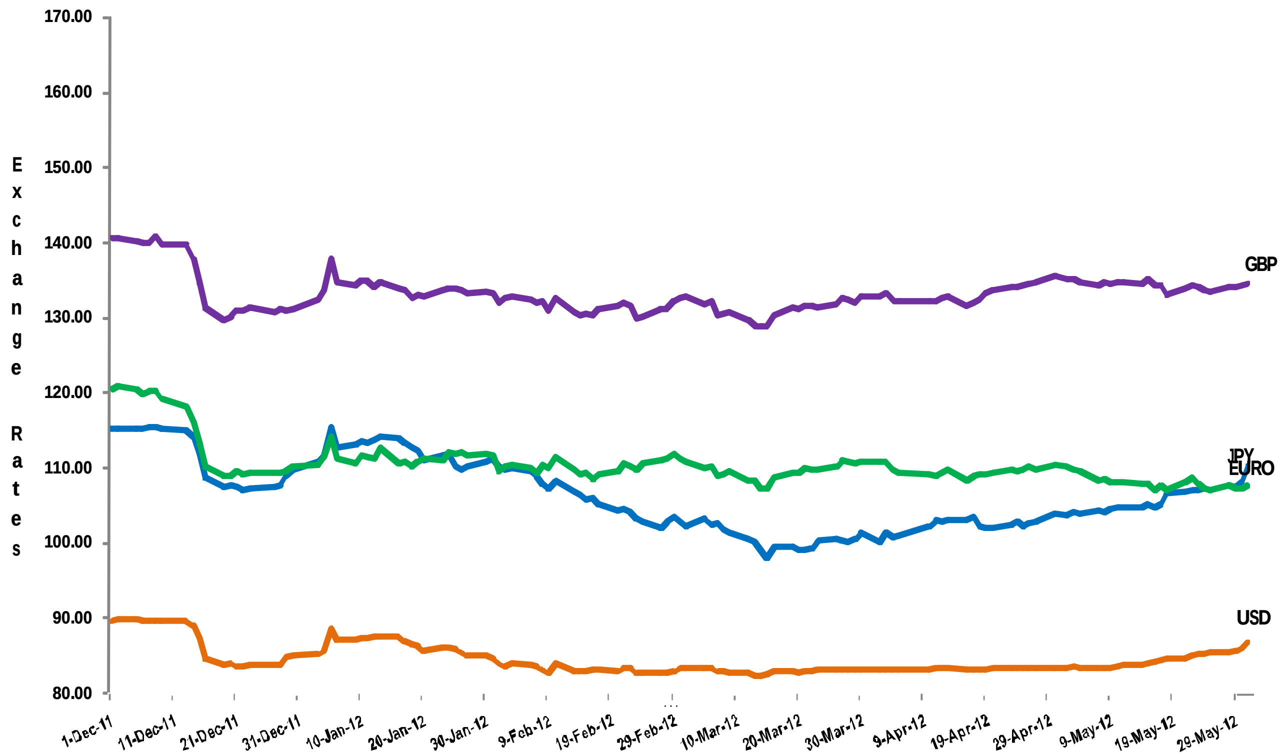
Table 2: Movement in exchange rates

Currency	March 2012	April 2012	May 2012
US Dollar	83.06	83.22	86.83
STG Pound	132.75	135.51	134.51
Euro	110.86	110.30	107.61
JPY(100)	101.34	103.84	110.22

Source: Central Bank of Kenya

Chart 2 shows the trends in daily exchange rates between Kenya Shilling and the four major foreign currencies from December 2011 to May 2012. In the second half of the fiscal year 2011/12, the US Dollar, Sterling Pound and the Euro have remained relatively stable.

Chart 2: Kenya Shilling Exchange Rate



Source: Central Bank of Kenya

2.0 EXTERNAL DEBT

2.1 Size of Public and Publicly Guaranteed External Debt

Overall, public and publicly guaranteed external debt increased by Kshs 20.14 billion to Kshs 721.04 billion in May 2012 from Kshs 700.90 billion in April 2012 as shown in Table 3.

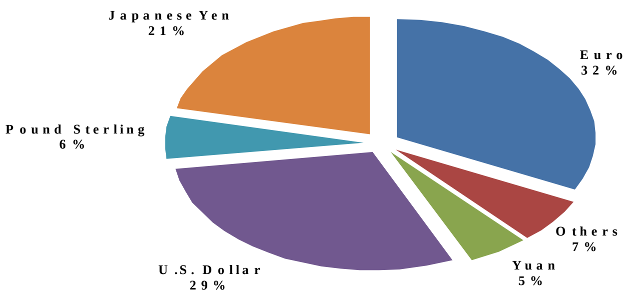
Table 3: External debt stock, in billions

	April 2012		May 2012	
	Kshs	USD	Kshs	USD
Bilateral	205.78	2.47	209.64	2.41
Multilateral	433.86	5.21	447.31	5.15
Guaranteed	46.19	0.56	48.95	0.56
Others	15.07	0.18	15.14	0.17
Total	700.90	8.42	721.04	8.30

Source: Ministry of Finance

There was an increase across all the creditor categories due to increased disbursements and depreciation of the Kenya shilling against the US dollar and the Japanese Yen. The major increase was in the multilateral category due to disbursements from IDA.The high proportion of debt from official external sources demonstrates a conscious effort to contract loans on concessional terms. Chart 3 below illustrates that 32 percent of Kenya's external debt is denominated in the Euro while about 7 percent is in other currencies e.g. Kuwait Dinar, Swiss Franc, etc.

Chart 3. Currency Composition

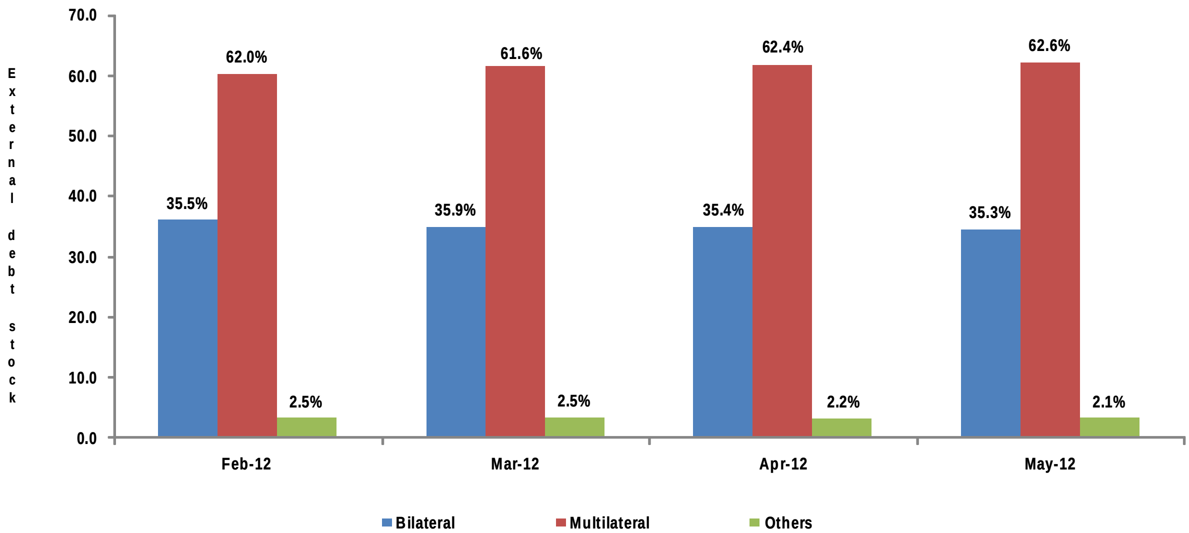


Source: Ministry of Finance

2.2 Structure of External Debt by Creditor

Official creditors account for 97.9 percent of the total public and publicly guaranteed external debt, out of which debts owed to multilateral creditors (Ksh 451.22 billion including Ksh 3.91 billion guaranteed debt owed to IDA) dominate the portfolio (62.6 percent of the total). Bilateral debt stands at Kshs 254.68 billion (35.3 percent of the total), which includes Kshs 45.04 billion guaranteed debt, as shown in Chart 4 and Annex 1.
In the multilateral category, IDA, ADB/ADF, IMF and EEC/EIB account for the largest proportion of external credit, while Japan, France and Germany are the leading creditors in the bilateral category. Supplier credit debt remains relatively unchanged as these debts are not being serviced due to the current disputes with the creditors (see Annex 1).

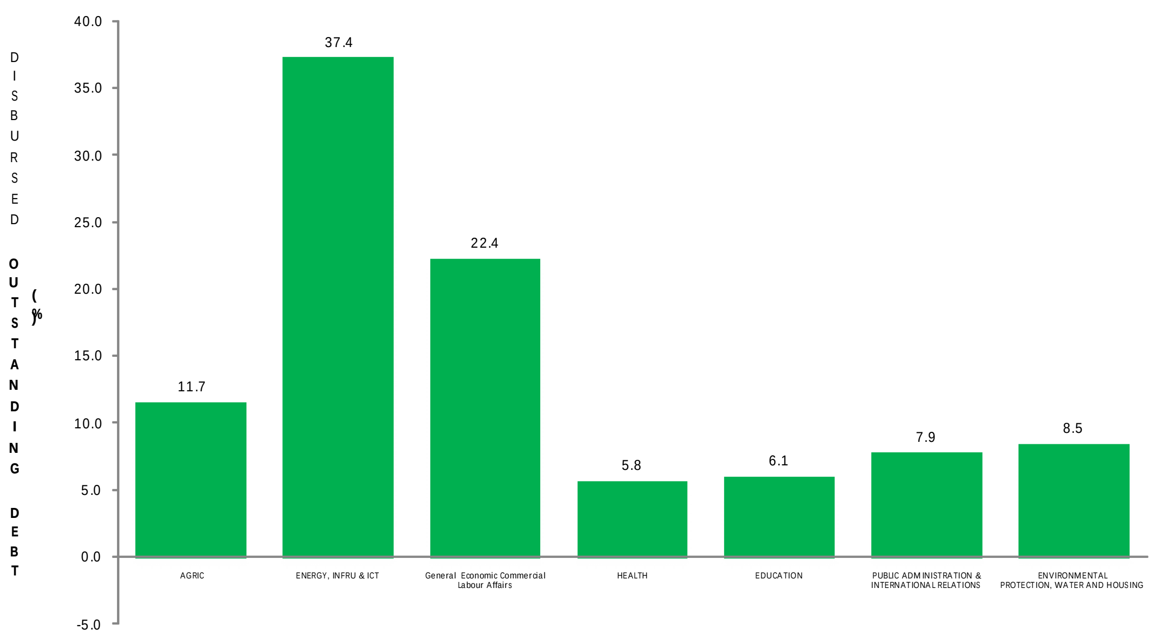
Chart 4: External Debt by Creditor



Source: Ministry of Finance

2.3 External Debt by Sector

Energy and Infrustructure sector has been receiving the biggest share of the extenal concessional loan, the sector has recieved more than 37 percent of the total external loan. The General economic, commercial and labour affairs is the second sector with 22 percent supporting the balance of payments and bugdetary support.



2.4 Projected Cumulative External Debt Service

Projected cumulative external debt service for the period to end May, 2012 stood at Kshs 29.47 billion. Principal and interest projections for the month of May 2012 were Kshs 0.71 billion and Kshs 0.49 billion, respectively. Multilateral and bilateral creditors constitute 51.3 percent and 48.7 percent, of the cumulative projected debt service, respectively during the period under review as shown in Table 4.

Creditor category	Principal	Interest	Total
Bilateral	11,286.58	3,055.26	14,341.84
Multilateral	12,046.08	3,078.87	15,124.95
Commercial	-	-	-
Total	23,332.66	6,134.13	29,466.79

Source: Ministry of Finance

2.5 Actual Cumulative External Debt Service

Actual cumulative debt service as at end May 2012 was Kshs 28.08 billion as reflected in Table 5. Actual principal and interest payments for the month of May 2012 was Kshs 1.02 billion and Kshs 0.62 billion respectively.

Table 5: Actual cumulative external debt service as at end of May 2012, in Kshs million

Credit category	Principal	Interest	Total
Bilateral	9,597.56	3,026.69	12,624.25
Multilaterals	12,080.59	3,376.15	15,456.74
Commercials	-	-	-
Totals	21,678.15	6,402.84	28,080.99

Source: Ministry of Finance

2.6 Budget Deviation

The actual cumulative debt service for May 2012 was below the projected debt service by Kshs 1.39 billion.

2.7 Guaranteed External Debt

Under the National Government Loans Guarantee Act, 2011, the government may issue guarantees so long as it does not exceed the ceiling which currently stands at Kshs 200 billion. The guaranteed external debt increased by Kshs 2.76 billion to Kshs 48.95 billion in May 2012 from Ksh 46.19 in April 2012. The increase is due to the depreciation of the Kenya shilling against the Japanese Yen which constitute over 90 percent of the guaranteed debt owed. Table 6 shows the disbursed outstanding guaranteed debt stock by creditor.

Table 6: Guaranteed outstanding debt by creditor, in Kshs million

Creditor	March 2012	April 2012	May 2012
Japan	37,602.80	41,868.42	44,438.57
Canada	365.46	366.17	382.04
U.S.A	211.79	212.20	221.40
IDA (KR Concessionaire)	3,737.50	3,744.74	3,907.13
Totals	41,917.55	46,191.53	48,949.15

Source: Ministry of Finance

3.0 DOMESTIC DEBT

3.1 Central Government Domestic Debt

As indicated in Table 7, Government net domestic debt decreased by Kshs 3.67 billion to Kshs 732.09 billion. This is attributed to increased Government deposits in Commercial Banks.

Table 7: Government domestic debt, in Kshs billion

	March 2012	April 2012	May 2012
Gross domestic debt	887.87	896.04	888.86
less			
Govt. deposits at CBK	-40.90	-43.30	-36.12
Govt. deposits at commercial banks	-104.18	-111.28	-114.95
Govt. advances to parastatals	-5.70	-5.70	-5.70
Net domestic debt	737.09	735.76	732.09

Source: Central Bank of Kenya

3.2 Government Domestic Borrowing

During the month of May 2012, Government securities worth Kshs 21.0 billion were advertised. Bids worth Kshs 44.91 billion were received, out of which, bids for the Treasury Bills and Treasury Bonds were Kshs 38.69 billion and Kshs 6.23 billion respectively. Successful bids amounted to Kshs 22.25 billion against the months redemptions of Kshs 2.57 billion leaving a surplus of Kshs 19.67 billion to exchequer.

Table 8: Government domestic borrowing, in Kshs million

	Treasury Bills	Treasury Bonds	Total
Advertised	18,000	3,000	21,000
Bids received	38,689	6,225	44,914
Successful bids	17,265	4,980	22,245
Redemptions (cost)	2,572	0	2,572
Net domestic borrowing	14,693	4,980	19,673

Source: Ministry of Finance

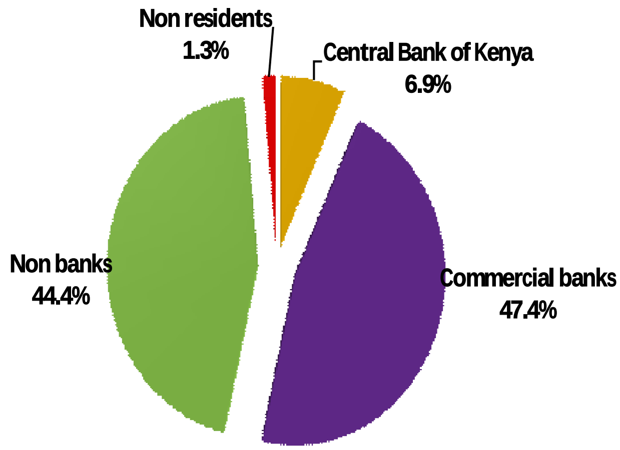
Table 9: Domestic debt instruments by holder, in Kshs billion

Instrument/Holder	Commercial banks	Non banks	Central Bank of Kenya	Non residents	Total
Treasury bonds	336.98	347.08	3.80	4.46	692.32
Treasury bills	82.11	48.06	1.24	7.11	138.52
Others	2.01	0.07	55.95	0.00	58.03
Total	421.10	395.21	60.99	11.57	888.87
Percentage Holding	47.37	44.46	6.86	1.30	100.0

Source: Central Bank of Kenya

Commercial banks held the largest proportion of the outstanding Government debt securities amounting to Kshs 421.10 billion or 47.4 percent as shown in Table 9 and Chart 5. The non banks held 44.5 percent of the outstanding Government paper, mostly Treasury Bonds. The non banks category comprises non bank financial institutions, National Social Security Fund (NSSF), parastatals, insurance companies, building societies, pension funds and individuals. Government debt securities worth Kshs 11.57 billion or 1.3 percent were held by non residents who invest through nominee accounts in the local banks. Kshs 60.99 billion held by Central Bank of Kenya comprises the Government overdraft and Repo Treasury Bills used for execution of monetary policy.

Chart 5: Domestic debt by holder as at end May 2012

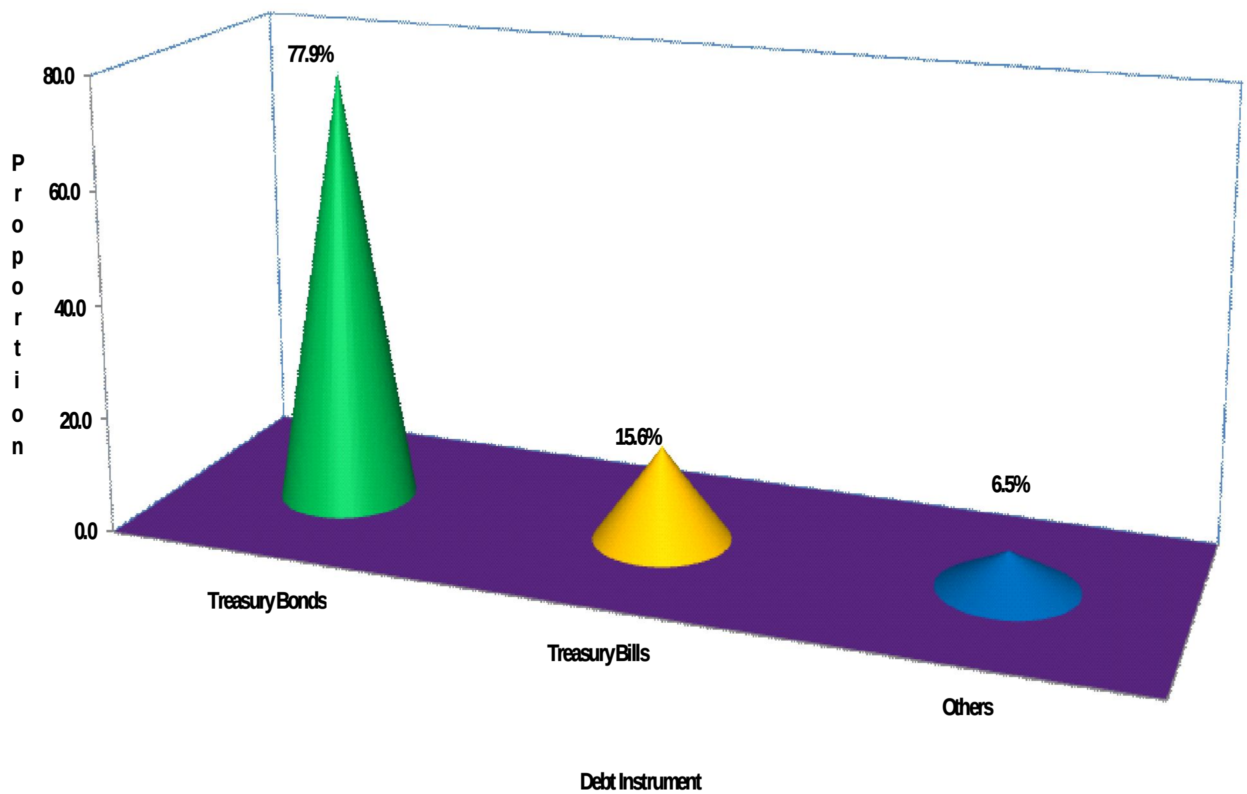


Source: Central Bank of Kenya

3.3 Domestic Debt by Instruments

Chart 6 shows that as at end May 2012 the composition of the domestic debt remained largely the same as the position in April 2012. 77.9 percent of Government domestic debt was in Treasury Bonds, 15.6 percent in Treasury Bills while the balance is mainly the Government overdraft at the Central Bank of Kenya. The structure of the holding is consistent with the debt strategy of holding more domestic debt on longer dated instruments to minimise refinancing risk and promote development of domestic markets for Goverment securities.

Chart 6: Domestic debt by instrument



Source: Central Bank of Kenya

3.4 Net Domestic Financing

Table 10 shows that as at end May 2012, the net domestic financing stood at Kshs 108.72 billion.

Table 10: Net domestic financing, in Kshs billion

	June-2011	May-2012	Change
Treasury Bills	123.53	126.22	2.69
Treasury Bonds	579.67	666.86	87.19
Long term Stock	0.00	0.00	0.00
Pre-1997 Govt. Overdraft debt	31.66	30.55	(1.11)
Other	8.11	25.68	17.57
of which Overdraft (from CBK)	7.57	25.37	(17.80)
Govt. deposits	89.95	87.56	(2.39)
Net Domestic Credit	653.03	761.75	108.72

Source: Central Bank of Kenya

3.5 Cumulative Domestic Interest Payments

As at end May 2012, Government actual cumulative domestic interest payments stood at Kshs 73.80 billion against the cumulative projected interest payments of Kshs 62.86 billion. Actual interest payments on Treasury Bonds and Treasury Bills amounted to Kshs 58.55 billion and Kshs 12.40 billion respectively. The cumulative variance of Kshs 10.94 billion is attributed to high interest rates for Government securities than was projected.

Table 11: Domestic interest payments, in Kshs million

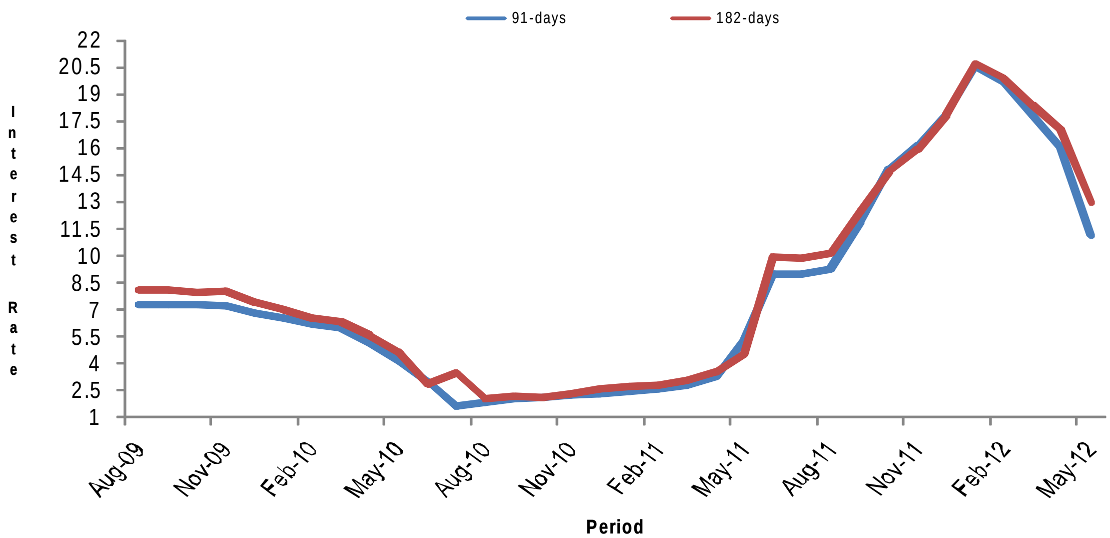
Type of debt	Projected	Actual	Variance
Treasury bonds	50,407.25	58,553.23	8,145.98
Treasury bills	10,461.32	12,395.81	1,934.49
Overdraft	1,143.70	2,850.75	1,707.05
Pre-1997 overdraft debt	848.67	0.00	(848.67)
Totals	62,860.94	73,799.79	10,938.85

Source: Central Bank of Kenya

3.6 Average Interest rates for Treasury Bills

Chart 7 shows the monthly trends on average interest rates for both the 91-day and 182-day Treasury Bills since August 2009. During the month of May 2012, the average interest rates for the 91-day Treasury bills declined by 483 basis points to 11.18 percent while the 182-day and 364-day Treasury bills decreased by 394 and 492 basis points respectively to 13.00 and 12.00 percent per annum respectively.

Chart 7: Average interest rates on Treasury Bills



Source: Central Bank of Kenya

3.7 Yields on Treasury Bonds

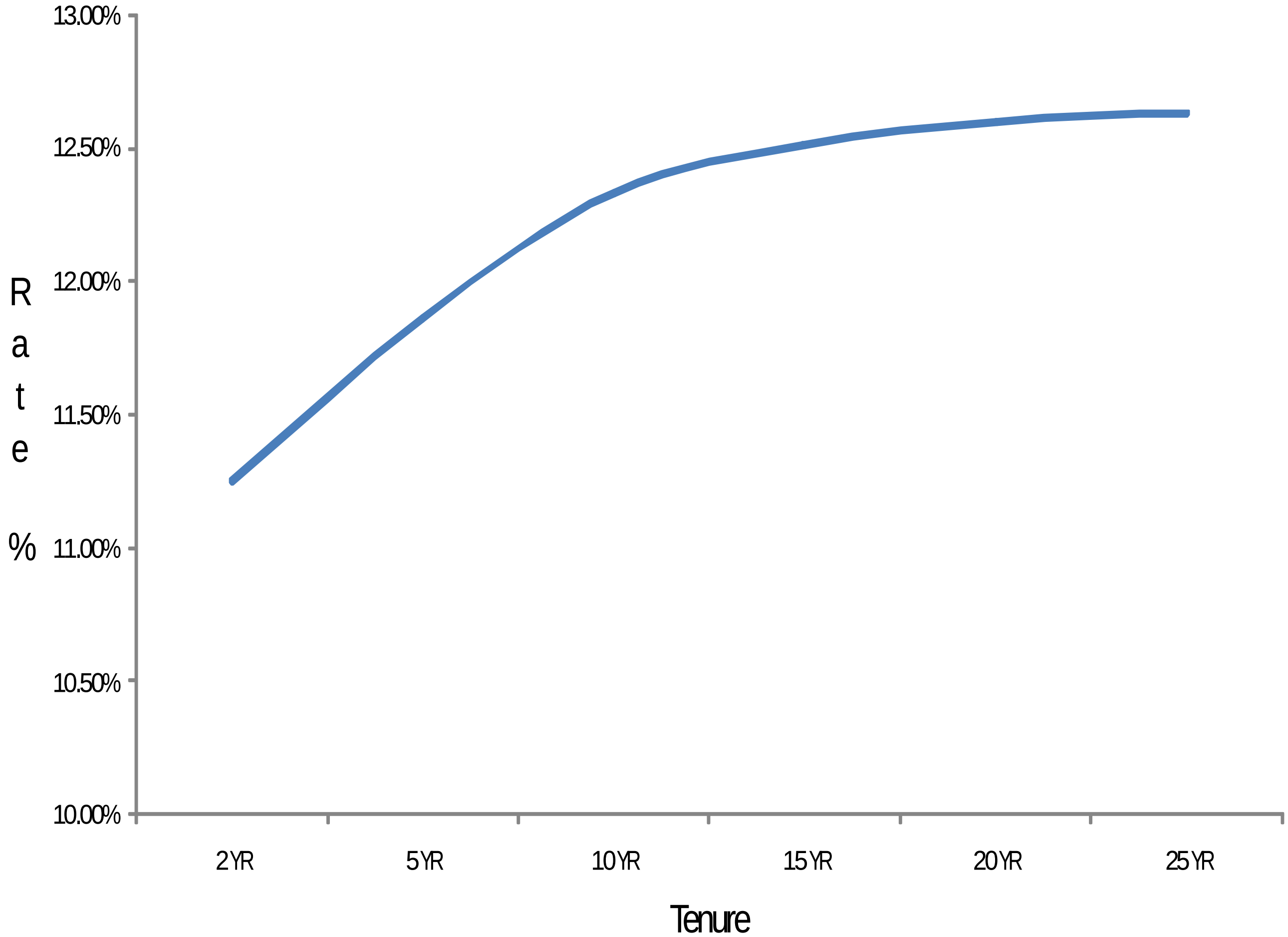
The Government has been implementing a Benchmark Bond programme to increase liquidity around selected Bonds and promote secondary trading. One of the key objectives of the programme is to lower both refinancing risk and cost of borrowing by the Goverment. Table 12 shows the yields on selected benchmark Treasury Bonds in the secondary market. The curve is upward sloping reflecting the current market trends with high yields at the long end of the market as illustrated in Chart 8.

Table 12 :Yields on selected Treasury Bonds

Tenure	Rate (%)
2 YR	11.25%
5 YR	11.86%
10 YR	12.33%
15 YR	12.51%
20 YR	12.60%
25 YR	12.63%

Source: Central Bank of Kenya

Chart 8:Yields on selected Treasury Bonds



4.0 UNDERSTANDING THE GREECE DEBT CRISIS

4.1 Introduction

When Greece joined the Euro in 2001 her credit ratings rose and so Greece was able to borrow money at very low interest rates.With the cheap credit available, Greece made huge borrowing to the point where its debt to GDP stood at 115 percent in 2009. When the global financial crisis erupted in 2007-2008, Greece economy was affected by a number of shocks including inadequate government revenues due to rampant tax evasion. Greece was also giving generous social security and pension payments, and unrestrained spending finally took their toll on Greece. The problem-laden Greek economy was further hit when tourism and shipping, the country's primary industries, was affected severely due to the economic downturn. To show how things had deteriorated in Greece in 2009, the government's fiscal deficit was 13.6 percent of Greece's gross domestic product (GDP) which was the highest in the world.

4.2 Consequences of Debt Default

The fears that Greece was going to default on its debt because of these economic problems led to lenders demanding almost 10 percentage points premium over lending rates to compensate for the risk that they might not their money back, which worsened Greece's deficit. This confluence of events eventually led credit rating agency Standard & Poor's (S&P) to downgrade the Greek sovereign bonds to junk status. On April 27, 2010, S&P reduced Greece's long-term sovereign debt rating from BBB+ to BB+, the first notch in the junk category.

Other credit rating firms such as Moody's and Fitch Ratings followed and, as a result, yields from government bonds rose. The yield of Greece's 2-year government bond, for example, jumped from 10% in November 2010 to a whopping 110% one year later.

But opposition demands that the rescue package comes with strings attached: a tough series of public sector cuts designed to reassure international investors that the government can become creditworthy again.

4.3 Solutions

The EU came up with radical decisions which required Greece to undertake austerity measures. This meant huge spending cuts to return Greece on a sustainable path. Even with the large corrective measures Greece has agreed to undertake, its debt is projected to increase to 149 percent of GDP in 2012 before beginning to shrink in 2014. The snag is, this traditional market response is complicated by Greece's membership of the single-currency euro club. This means it cannot stimulate growth by devaluing its currency, and nor can it cut interest rates any further, which would help because these are decided by the European Central Bank in Frankfurt. Instead, the public sector cuts are almost certain to deepen the Greek recession, reducing tax revenues and making it even harder to service the debts in future.

ANNEX 1: STOCK OF PUBLIC AND PUBLICLY GUARANTEED DEBT BY SOURCE (IN KSHS MILLIONS)

CREDITOR	Stock at end April 2012	Stock at end May 2012	Change
CENTRAL GOVERMENT			
BILATERAL			
AUSTRIA	1,413.41	1,378.90	(34.51)
BELGIUM	7,691.20	7,450.00	(241.20)
CANADA	1,150.48	1,200.37	49.89
DENMARK	2,190.32	2,138.84	(51.48)
FINLAND	111.81	112.80	0.99
FRANCE	38,643.30	37,705.81	(937.49)
GERMANY	23,450.34	22,877.85	(572.49)
ITALY	2,925.95	2,856.65	(69.30)
JAPAN	61,213.77	64,971.46	3,757.69
NETHERLANDS	3,097.99	2,951.53	(146.46)
UK	2,092.52	2,077.09	(15.43)
USA	4,942.15	5,156.46	214.31
PARIS CLUB OTHERS	4,931.31	4,912.15	(19.16)
NON PARIS CLUB	51,927.93	53,854.09	1,926.16
o/w CHINA	44,885.01	46,583.06	(1,698.05)
Sub total	**205,782.48**	**209,644.00**	**3,861.52**
MULTILATERAL			
ADB/AFDB	63,031.48	62,619.33	(412.15)
EEC/EIB	11,355.73	11,077.69	(278.04)
IDA	278,386.43	290,944.83	12,558.40
IFAD	7,283.70	7,409.05	125.35
IMF	63,805.14	64,903.28	1,098.14
OTHERS	9,996.03	10,354.94	358.91
Sub total	**433,858.51**	**447,309.12**	**13,450.61**
SUPPLIERS CREDIT	**15,072.40**	**15,141.25**	**68.85**
Sub Total	**654,713.39**	**672,094.37**	**17,380.98**
GUARANTEED DEBT			
CANADA	366.17	382.04	15.87
JAPAN	41,868.42	44,438.57	2,570.15
USA	212.20	221.40	9.20
IDA(KR Concessionaire)	3,744.74	3,907.13	162.39
Sub Total	**46,191.53**	**48,949.15**	**2,757.62**
GOK+ GUARANTEED TOTAL	**700,904.92**	**721,043.52**	**20,138.60**

Source: Ministry of Finance