Njuguna Ndung'u: Kenya's Ksh.18.5 billion infrastructure bond

Address by Prof Njuguna Ndung'u, Governor of the Central Bank of Kenya, during the Launch of the Ksh 18.5 billion Infrastructure Bond Issue, Nairobi, 28 January 2009.

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1.0. Background

Since 2001, the Government pursued a deliberate policy action to restructure domestic debt, with a view to developing a vibrant bond market for generating long term finance. The success in lengthening the maturity profile of debt instrument has been phenomenon.

Several measures were instituted to facilitate development of a robust bond market

(a) In 2003, the government lowered the cash ratio for commercial banks to release liquidity held with a view to reducing interest rates.

(b) The Government also streamlined its domestic Borrowing Cash Plan in favour of bonds. As a result, the volume of Treasury bonds rose from Ksh.80 billion in June 2001 to Ksh.318 billion by end December 2008. The Proportion of long term debt to total domestic debt was reversed from 70:30 and now stands on average at 70:30.

But what is needed now are bonds specific to projects of a developmental nature. Infrastructure financing is one such target. The government organized the first ever Infrastructure Bond Conference on October 27-28, 2008 at the Kenya School of Monetary Studies. The ambition was to launch a series of infrastructural bonds to finance targeted projects and emulate other countries like: South Africa, Ghana, Botswana, Nigeria, Malaysia, and Singapore, among others have used capital markets to finance infrastructure projects. It is against this background that the government is launching this first infrastructure bond as a starting point.

2.0. Projects/sectors to be funded

Kenya aspires to be firmly interconnected through sophisticated network of roads, railways, ports, airports, and also provide water and sanitation facilities, and telecommunications as a key pillar of economic development in the Vision 2030 blueprint. But the challenge is the huge capital outlay required, leading to the initiative we are starting today. This recognition of infrastructure provision has been recognized as an inhibition in competitive production due to heavy transaction costs.

The targeted projects are well documented in the prospectus. We may in future allow a monitoring process for these projects to completion.

3.0. The features of this infrastructure bond

Given the long term nature of the projects, the infrastructure bond will be of 12 years to maturity with face value of Ksh.18.5bn. This issue is meant to create impact to the market. However, the infrastructure bond will be redeemed partially in 2015, 2017 and 2021 as an attractive feature for medium term investors who may wish to recoup investment back before expiry of the life of the bond. It will also help Treasury at redemption given the huge amount involved.

A number of incentives have been given to make the issue attractive and successful. They include; exemption from withholding tax on interest income, we have revised agency commission upwards, the bond will qualify for statutory liquidity requirements; the bond will be listed for trading at the Nairobi Stock Exchange, the holders can use it as collateral to acquire loans from banks and banks can pledge it as collateral for repos. The infrastructure bond also gives attractive coupon rate of 12.5% p.a. The minimum placement amount will be Kshs.100,000.00 while any additional amounts will be in multiples of Kshs.50,000.00.

The bond will be issued under the provisions of the Internal Loans Act Cap 420 and the Capital Markets Authority Act Cap 485A.

This pioneer infrastructure bond is expected to lay ground for government agencies to issue their own specific infrastructure bonds. Moreover, future infrastructure bonds will be structured alongside the balance sheets of the issuer where stream of earnings from funded projects will be used to service the bonds. Such bonds will be issued strictly under the Capital Markets Authority's Asset Backed Securities regulations.

Honorable Minister, Distinguished guests, ladies and gentlemen, it is my hope and prayer that this Infrastructure Bond will be attractive and be fully subscribed to finance our infrastructure – a necessary condition for our economic development.