PROGRESS IN IMPLEMENTATION OF BASEL ACCORDS BY CBK

Basel II

CBK began a process in 2007 of preparing a comprehensive roadmap for implementation of Basel II. This process involved:

1. **The implementation of Basel II prerequisites**:-

- Full adoption of Basel I in particular the market risk amendment that requires banks to set aside capital for market risk in addition to credit risk:

Status: The revised Capital Adequacy Prudential Guideline was amended in 2012 to incorporate provisions on capital charge for market risk and operational risk. The revised prudential guideline became effective on 1st January 2013. However, an observation period of 12 months was set for the impact of the provisions on the banks to be assessed. Consequently, the provisions took effect from 1st January 2014.

- Implementation of Risk Based Supervision(RBS):

Status: RBS has been fully implemented with the assistance of IMF's East AFRITAC.

- Full compliance with the Basel Core Principles for Effective Banking Supervision through the comprehensive review of the Banking Act that is under consideration by the Attorney General.

Status: According to an IMF/World Bank Financial Sector Assessment Program (FSAP) update conducted in September 2009, Kenya was fully or largely compliant with 18 Basel Core Principles, materially non-compliant with 6 principles and non-compliant with one principle. This was an improvement from the 2003 FSAP when Kenya was rated as compliant or largely compliant with 16 principles.

As per CBK's self assessment in December 2014, CBK was compliant with 22 BCPs and largely Compliant with 3 BCPs.

Further, following the issuance of the 29 revised Basel Core Principles in September 2012, CBK undertook a self-assessment in December 2014. The assessment indicated that CBK is compliant with 17 Basel Core Principles and largely compliant with 12 Basel Core Principles.

2. CBK conducted a survey in 2008 to assess the status of Kenyan banks vis a vis the requirements of Basel II.

Status: Majority of the institutions rated the level of awareness of Basel II as medium (on scale of high, medium and low). There was therefore need to enhance Basel II awareness in institutions.

Based on the findings of the 2008 survey CBK continued to engage the industry players on adoption of Basel II and other global best practices. Some of the Kenyan banks that are affiliated to global financial institutions have already adopted Basel II. Some of the aspects of Basel II on market discipline have already been implemented. The revised prudential Guideline on Publication of Financial Statements and Other Disclosures, requires banks to disclose both quantitative and qualitative financial data on a quarterly basis. This is as required under Pillar 3 of Basel II.

Basel III

1. The Central Banks of the EAC member states under the auspices of the Monetary Affairs Committee (MAC) have jointly reviewed Basel III and included the relevant aspects in their draft convergence criteria. The following aspects of Basel III have been included in Central Bank of Kenya's revised Prudential and Risk Management Guidelines, which became effective on 1st January 2013:-
   - Capital Conservation Buffer of 2.5% under the Capital Adequacy Prudential Guideline.
   - Definition of Tier I capital strengthened – Emphasis on permanent equity with high loss absorbency capacity.
   - Liquidity Measurements – Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) included under the Liquidity Risk Management Guideline.

2. Under the Basel III, the Basel Committee on Banking Supervision (BCBS) has proposed enhanced capital requirements for banks to enable them create adequate buffers to withstand shocks in times of economic and financial stress. The new minimum capital requirements are as below:-

   - Common Equity to Total Risk Weighted Assets – Increased to 4.5% from 2%.
   - Tier 1 Capital to Total Risk Weighted Assets – Increased to 6% from 4%.
   - Total Capital to Total Risk Weighted Assets – Retained at 8%.

Currently, the minimum capital requirements for Kenyan banks are already above the proposed minimums as shown below.

	Kenyan current minimum requirement	**Kenyan minimum requirement (inclusive of 2.5% capital conservation buffer effective 1st January 2015**	**Global minimum Standard**	**Excess buffer**
Tier 1 capital to Total Risk Weighted Assets	8%	10.5%	6%	4.5%
Total Capital to Total Risk Weighted Assets	12%	14.5%	8%	6.5%

This means the Kenyan banking sector capital requirements have factored in buffers to enable banks withstand shocks in times of economic and financial stress. However, CBK will continue to remain abreast with the global best practices and adapting them to our market's circumstances. Further, the increase of the minimum core capital of banks and mortgage finance companies to Kshs 1 billion (approximately USD 10 million) by 2012 have positioned Kenyan banks to exploit new market niches and absorb any emerging shocks.

Other initiatives to comply with Basel II, III and Basel Core principles

Issuance of the following Prudential and Risk Management Guidelines:-

- Country and Transfer Risk Management Guidelines.
- Consolidated Supervision Prudential Guideline.
- Consumer Protection Prudential Guideline.
- Stress Testing Prudential Guideline.
- Enhanced Corporate Governance Prudential Guideline.