

## ***“My Chat with a Bank CEO”***

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***Mr. Munir Ahmed, Managing Director of National Bank of Kenya (NBK)***

***Chat Summary***

***Wednesday, 23 January 2013***

***Topic: The Interest Rates Environment***

***Time: 10.00 am -11.15 am***



If you had the opportunity to chat with a Bank CEO, what would you talk about?

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**Kenya Bankers Association**

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**Interest Rate Environment (Continued)**

**Interest Rates Perspective**

**MunirAhmed:** I’m happy to take your questions and have a fruitful discussion on this topical issue...the interest rate environment

**capitalfmkenya:** Nderitu on twitter asked; Historically, from 1991 until 2012, Kenya Interest Rate averaged 15% reaching an all-time high of 84.67% in July of 1993 and a record low of 0.83% in September of 2003. do you think that the interest rate will remain at the same in the next 5years and when

**MunirAhmed:** Nderitu thanks for joining us...historically interest rates have generally been going down...in the early 1990s there was the liberalisation of rates and that led to the volatility you mention...subsequently as the financial market matured we have seen that rates have been trending down, with the exception of 2011 when we had the currency depreciation which led CBK intervene with an increase in rates. We expect that the downward trend in rates will be sustained so long as the economic growth and external shocks dont upset the environment

**camaumo:** How will it impact Banks in Kenya either negatively or positively when the interest rates go lower than they are right now?

**MunirAhmed:** camaumo thank you, a low interest rate environment is conducive to higher volumes of lending or higher credit growth and is therefore supportive of bank business growth...when rates go up, borrowing volumes decline and default rates increase...so just like their customers, banks prefer lower interest rate regime

**lucymell:** What is your institution doing to cushion itself from the drop of income with the downward trend of the CBK rate?

**MunirAhmed:** lucymell thanks for your question...like all businesses this is a volume and margin issue...interest rate drop doesnt necessarily mean a margin drop. Volumes will increase when interest rates drop and the margin, which is the difference between what you pay for the funds and what we earn on the lending, would ideally be maintained

**samsa:** if banks borrow from VBK using CBR, why do they have to double the interest rates charged to the customers

**MunirAhmed:** Samsa thanks for your question, this is a misconception...when banks borrow from CBK it is at 6 per cent ABOVE the CBR...so the CBR is really a signal tool to indicate the intention on interest rates. Usually when banks do borrow from CBK it is as a last resort...banks are expected to source their funds from the market...so CBK penalises banks when they borrow from CBK...hence the 6 per cent margin they ‘charge’

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**Interest Rate Environment (Continued)**

**Lucymell:** why do banks have to use the +6 margin from the cbr?

**MunirAhmed:** lucymell let me clarify, the 6 per cent is the margin on top of the CBR ...this is what banks have to pay if they resort to borrowing from the CBK...weve discussed earlier that banks typically do not borrow from CBK because it is a lender of last resort and doing so has penalty implications

**Musa:** Hello, I wonder why interest rate for banks is too high, yet saccoes are offering 12%.

**MunirAhmed:** Musa thanks for joining us...it is important to differentiate between SACCOS and banks. SACCOS are cooperatives for the mutual benefit for the members, whereas banks have investors (shareholders) with an expectation of return for their investment....the structure, products, and cost base of the two (SACCOS and banks) are vastly different, hence different interest rates

**aquinas:** so what is the future of interest rates

**MunirAhmed:** Aquinas....we've answered this good question...predicting interest rates is difficult for the number of factors we have discussed...but we can say on our current economic outlook overall rates are trending down

**capitalfmkenya:** Wanza, on face book asked; Analysts have alluded to the fact that despite many Kenyans urging banks to increase the interest customers gain on deposits, current deposit levels are still too low to fund the deposit interest. Will this change in future and when?

**MunirAhmed:** Wanza thanks for joining us via Facebook...to answer the question on deposit rates....moneterised savings are lower as a proportion to the GDP which means the deposit levels are low ...this is because the alternative savings vehicles like property and physical assets tend to be the preferred savings options for most Kenyans, and therefore the deposit rates are actually not a disincentive to savings levels in Kenya

**DreamCatcher:** @Munir Ahmed Good morning. What are the specific market forces that affect the interest rates in Kenya? What are the major forces that cause the instability of the interest rates in the market?

**MunirAhmed:** DreamCatcher thank you for your question... The factors affecting interest rates are both macro and bank specific reasons, this includes inflation rate expectation, risk free rate, deficit financing of government, average cost of funds in the market, cost of liquidity among others...so you see the Central Bank Rate is just one of the determinants of the interest rate environment

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**Interest Rate Environment (Continued)**

**Lowering Interest rates**

**chebasila:** Hey, why has it taken long for your bank to bring down interest rates for their customers.

**DKanake:** To be honest, with such high interest rates, in my honest opinion, banks in Kenya are profiteers especially the micro finance institutions which lend to the poor at such exorbitant rates. Also, the middle class in Kenya are 'wannabe rich' so they are acquiring 'debt' they can't afford

**Chebasila:** Good work u are doing at NBK. Why has it taken long for u to effect change of interest rates??

**MunirAhmed:** Thank you for your questions...we will comment briefly about NBK...as most of the banks, we did reduce our lending rates in line with all the other commercial banks as the CBR trended down. But there is always a lag in changing the rates. Lets talk briefly about why there is a lag

....Banks source deposits so you need to adjust prices on both sides ...deposits and lending...so it takes time for these price adjustments to take effect. Let me share an example, for instance the fixed deposit rate funds are locked in say for 3 months or 6 months or longer, so a bank can't adjust their deposit rates until they mature, which means on the lending side, you can't adjust your loan rates

**johnnjiru:** so in short it means that banks (read: NBK) will have to wait until the deposits have matured before they can lower their lending rates?

**MunirAhmed:** johnnjiru thank you, yes that is true, banks have to get their average cost of funds to a level where your margins are not adversely affected to a significant extent... On a long term trend, the economic outlook is positive, which implies interest rates will trend downwards

**David:** Good morning. I refer to my story in today's Business Daily on interest rates. Today more small banks have announced rate cuts in today's papers. I understand that large banks were leading in cutting thier rates when CBK started bringing down the CBR last year and I understand that the CBR is not the only factor that determines base lending rates. However, in your view, why does it seem that it is mainly small and medium sized banks which are announcing rate cuts this year?

**MunirAhmed:** David thank you for joining us...we read your article in Business Daily....since July last year, most banks have consistently cut their rates...it is just a question of timing and speed of reaction as we have discussed on this platform...you are likely to see more banks announce rate cuts

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#### **Interest Rate Environment (Continued)**

**AANDUURU:** what needs to be done to ensure the rates come down in order to spur general growth?

**MunirAhmed:** AANDUURU thank you for your question, we've discussed that rates have been coming down...things that will improve prospects for lower interest rates are lower inflation rate, lower borrowing by the Government, and reducing infrastructure costs of banks eg legal costs, collateral registration, security, etc

#### **Economic & Market Environments**

**DKanake:** Why are interests rates so high in Kenya vis 19-30% yet in the first world they are at 4-6%?

**MunirAhmed:** DKanake thank you for joining us...as David's article has shown us, the average lending rate is about 15 to 18 per cent from CBK statistics...it is not a good comparison to benchmark Kenya against the developed world interest rate because of the drivers of interest rate in Kenya is significantly different...for example inflation is usually double digit in our market and for banks to have a positive real rate of return their interest rates have to be higher...developed world inflation is historically low...in some markets it is between 0 to 3 percent...hence lower interest rates

**Shawn:** Kenya as a growing economy how does it affects credit and the rate of interests and my earlier question hasn't been addressed.

**MunirAhmed:** Shawn...thank you for your questions...to answer your point on Kenya's economic development and rates...when the economy is doing fine, it means the business community is doing well and therefore the risk profile for the market lowers therefore rates tend to go down...on the other side, low interest rates also promote economic growth, however this is provided that the credit is for investment rather than for consumption...when credit is directed to consumption, it increases inflation it is counter productive for the economy because the regulator will likely raise the interest rate

**KESUSD:** The issue of the high interest rate spread in Kenya definitely affects economic growth. I've two questions 1. is the pressure to keep it high from need to return a good profit of high operating costs 2. to what extent would having superbanks, the likes of Nigerian giants, help reduce the spread?

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**Interest Rate Environment (Continued)**

**MunirAhmed:** KESU you raise a good point...to clarify a few issues....

The average spreads of the Kenyan banking sector are single digit, so they actually are not high given the status of inflation in the economy at the moment. The spreads are also market determined and have several factors influencing, primary one being inflation rate expectation, and the risk free rate, and others unique to each bank eg operating cost, profit margins required by shareholders etc

The second part to KESU\'s question was on \'superbanks\'...in my opinion when you have 43 banks provide more competition which actually lowers the spread, than when you have few \'super banks\'

**capitalfmkenya:** Franklin Odour from facebook asked ; how do you Identifying Rising Rate Environments

**MunirAhmed:** Franklin Odour thank you for joining us via Facebook...weve discussed a number of factors that bear on the interest rate, but broadly the inflation expectation rate and the deficit financing by the government are the two primary items that you look at that impact interest rates. I should add that predicting interest rate is complicated by the number of factors that impacted it as we discussed in response to DreamCatchers question earlier

**DreamCatcher:** @MunirAhmed. Why is it that some banks have been able to source for lower and fixed interest funds from companies such as IFC. However, these reduced costs have not been passed on to the consumers?

**MunirAhmed:** Dreamcatcher...thanks...any funds from development multilateral agencies are passed on to the targeted sectors with only the risk margin added...so the customers do get the rate benefit that the development agency was after

**DKanake:** What do you think of the Islamic banking concept because I think it is the fairest lending concept in Kenya. I have worked in banking and I know that amortisation starts working against you if you take loans to be repaid in more than 6 months.

**MunirAhmed:** I\'ll take the last question...I see the point raised by DKanake about islamic banking. Islamic banking is principally asset backed, or real economic transaction backed financing. Islamic banking and conventional banking are different in that Islamic banking profit sharing where both parties fix the rate of return; where as most conventional banking is on a variable interest rate basis.So to answer DKanake, there are benefits to both Islamic Banking and Conventional Banking

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##### **Other Questions**

**Capitalfmkenya:** Kisia from twitter asked; what are the factors that may influence the performance of a bond portfolio when we have changes in the interest rate

**MunirAhmed:** Thanks Kisia for joining us via twitter...on bond prices when rates go up the price goes down, and vice versa so it is an inverse relationship between the two...however the overall return on the bond will depend on the coupon rate as well as the yield over its maturity...and there is a distinction between corporate bonds and public/government bonds ... as you have to add the risk factor for corporate bonds...

**vincecurter:** Good morning, mine is on a marketing perspective. With a controlled interest rate, how do you position your bank product to remain competitive in the face of cut throat environment (many Player)?

**MunirAhmed:** Thanks Vincecurter, bank interest rates are market determined and that promotes better access to credit than if it is controlled. So to continue to answer Vincecurter...competition is healthy, it helps improve performance and banks welcome it

**KESUSD:** Mr Munir, we are glad the local banks, like yours, are competing well with the MNCs. However, in the when it comes to forex interest, they are almost always more expensive. What is the solution to this? what are the local banks doing about it? when do you see them catching up?

**MunirAhmed:** KESUSD thank you for your question, the FX rate depends on the sourcing of your foreign currency funds...MNCs have got access to their parent companies to access cheaper lines of FX

**kagasi:** Hi Munir, as a young investor, what investment properties can i get into that will give me the highest rate of return in the short term?

**MunirAhmed:** kagasi thank you for joining us...properties are not short term but there are various options that you have, including bank deposits, T-bills, bonds, and equities are areas you can look at but you should always seek the advise of a financial professional

##### **General Comments**

**David:** Thank you for the chat today...very interesting discussion....

**samsa:** its been an educative discussion. Thanks Munir for taking us through. Next discussion should be on forex

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**Lucymell:** Thank you MunirAhmed for your time. It was informative

**DreamCatcher:** Thanks Munir for the valuable insights.

**cliffmuyera:** Very informative session, most appreciate it

**MunirAhmed:** Id like to thank the Kenya Bankers Association, KBA, for organising this forum, and Id like to encourage the customers of the banking sector to talk to their bankers in case they need further understanding of interest rates

**HabilO:** Thank you Mr. Munir for this informative session. Some of the issues will be built upon for the future sessions.

**Unanswered Questions**

**jndungo:** What is NBK doing to attract the youth to use your services

**Edwin\_munyiri:** In that case how do you market loans to customers in such a market? With high interest rates coupled with a general increase in the average?

**capitalfmkenya:** hi Ahamed, Mr Otieno on want to know... what is an implicit interest rate?

**capitalfmkenya:** wanjiru asked on facebook how do you Invest in a Rising Rate Environment

**samsa:**banks repatriate to CBK for all deposits mobilised. Right? Then why would CBK then lend you back the money which you have deposited with them? Where does this penalty arise?

**Cde\_monomotapa:** Hi all. Is there a direct corelation to Cost of Funds & Money mkt? If any, how is it arrived at.

**onesii69:** hello? Just wanted to know why are kenyan banks so behind in terms of export finance facilities compared to S.A. and asian banks, esp the ones structured around collateral managers, mind you considering the risks are so low.?

**Daniel:** Your thoughts on mobile banking platform

**DreamCatcher:** @MunirAhmed. What are some of the things that need to be in place so that Kenyans can enjoy low interest rates and/or fixed interest rates?