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CBK.

IKEN08104

17th November 2011

Dear Mr. Rey,

Subject: Contribution Agreement STABEX 1992/93 FMO-Central Bank of Kenya
Decision Capacity Building Project

Following further joint review of draft report by my staff, staff from Central Bank and your staff, we have factored in further comments and observations and are pleased to submit a revised final narrative and financial report for Project No. 1KEN08104 Central Bank of Kenya Decision Capacity Building Project for the period January 2009 to December 2010.

We take this opportunity to thank you most sincerely for the valuable contribution and collaboration we enjoy.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Christopher Gakahu'.

Christopher Gakahu
Deputy Country Director (P) a.i

Mr. Bernard Rey
Head of Operations
European Union
P. O. Box 45119-00100
Nairobi, Kenya



**FINAL REPORT
FOR THE PERIOD JANUARY 2009 TO DECEMBER 2010**

**Reporting Agency: United Nations Development Programme
Country-Kenya**

PART 1: DESCRIPTION

1.1	Beneficiary of grant	United Nations Development Programme (UNDP)
1.2	Name and title of the Contact person	Alfredo Teixeira, Deputy Country Director-Programmes (DCD-P)
1.3	Name of partners in the Action	UNDP, European Commission
1.4	Title of the Action	Central Bank of Kenya (CBK) Capacity Building Project
1.5	Contract number	Project ID. 00062433
1.6	Start date and end date of the action	January 2009 to December 2010
1.7	Target country	Kenya
1.8	Final beneficiaries and/or target groups (including numbers of women and men)	Central Bank of Kenya (CBK)
1.9	Countries in which activities took place if different from 1.7 above	N/A

PART 2: ASSESSMENT OF THE IMPLEMENTATION OF ACTION ACTIVITIES

2.1: EXECUTIVE SUMMARY OF THE ACTION

The Central Bank of Kenya (CBK) requested technical assistance in the form of three Advisors to the Governor aimed at improving the Bank's macroeconomic and monetary policy management capacity, promoting and deepening of domestic debt markets and generally reforming the Bank to become a premier institution not only as regulator but also a first class monetary policy formulator and implementer, and a source of frontier knowledge. The Overall project output included a strengthened analyses and decision support capacity of the three Departments of CBK focussing specifically on developing strategic plans for each of the three departments, training selected staff in adapted models, tools, systems for economic analysis and decision-guidance, accurate macroeconomic forecasts and analyses and improved signalling component of government securities.

During the implementation period, the bank managed to recruit technical advisors; Mr. John Kanda for the Research and Policy Analysis (commenced duty in February 2009) and Mr. Onchera G. Maiko research and Analysis for Monetary Operations and Debt Management (MODM) (though on the 27th October 2010). Despite having advertised the vacancy for the Currency Operations & Branches Administration (COBA) several times the bank did not manage to engage a candidate.

2.2: ACTIVITIES AND RESULTS

2.2.1: Project Governance

Notably, the implementation of the project was through a **Joint-Contribution Agreement**, signed between the European Commission (EC) and UNDP on 31st December 2008. This was in addition to the Protocol of Implementation signed between the EC, Ministry of Finance and CBK. Specifically, CBK was responsible for the delivery of programme activities to achieve specified results, as set forth in the Annual Work Plan whereas UNDP provided logistical and technical support. In order to operationalize the decisions made by the Steering committee (SC), Technical committee meetings were regular and were taking place almost every month.

2.2.2: Recruitment of Technical Advisors (TAs) for COBA and MODM Departments

Efforts towards recruitment of additional TAs for COBA and MODM Departments proceeded as planned. Following a consultative meeting between CBK and UNDP in February 2010, the vacant positions of TA for COBA and MODM were re-advertised by UNDP. To this end, advertisements were placed in the local dailies in March, 2010 and April, 2010. From this process, a total of seven (7) applications were received: one (1) for COBA and six (6) for MODM.

Four (4) candidates were therefore short listed for interviews held on May 17, 2010. The top two contenders were thereafter invited for final interviews held on July 2, 2010. Mr. Onchera G. Maiko emerged as the best candidate and took up the position on October 27, 2010. Efforts to recruit a TA for COBA were not successful despite a fourth round. Although the Bank approached the Swedish Central Bank with a view to seconding an expert to fill the vacant position, this was not possible due to staffing constraints at the Swedish Central Bank. It was therefore recommended that an alternative strategy for technical assistance be sought and put in place in the future.

2.2.3: Support to targeted CBK Departments

CBK departments managed to set up links with foreign Central Banks (and other relevant bodies) to facilitate longer term co-operation in areas relevant to the needs of the Bank. This was undertaken through study tours, attachments and workshops. For ease of reference, a detailed report is classified and presented under the various CBK departments.

(a) Currency Operations and Branch Administration Department

- Three staff in this department undertook a study tour and were attached to Reserve Bank of India. The study focused on currency management and narrowed on currency distribution channels, counterfeit trend analysis and prevention, business continuity plans, currency management systems, currency processing and destruction and security.

- A delegation of two senior officials from Swedish Central Bank visited the Central Bank's COBA Department in January 2010 and made a number of observations and recommendations relating to Currency Policies, Strategies and Operations. Arising from the visit, the Department drew up a five year action plan for implementation of the items agreed upon.
- A team of six undertook a one-week attachment to the Swedish Central Bank on 24th and 28th June 2010. The objectives of the attachment were to review the currency management structure at the Swedish Central Bank, review security management and cash operation activities in Cash in Transit (CIT) firm. The team noted that at the Swedish Central Bank offices in Mölndal and Stockholm and the Loomis cash processing facilities in Mölndal, the Swedish economy is plastic money based. It noted that Swedish Central Bank has progressively relinquished itself from retail cash handling, a function that is now successfully managed by the commercial banks and CIT firms. This resulted to integration of systems and an enhanced efficiency in cash processing environment. Based on these observations, the recommendations arising from the attachment were communicated to the Bank's senior management and are currently being implemented systematically.
- Four (4) officers undertook a one week study tour to the Reserve Bank of Germany from 22nd to 26th March, 2010. The three Branch Managers of Mombasa, Kisumu and Eldoret in addition to an Engineer from the Head Office visited the Central Bank of Germany with a view of giving the Branch Managers an appreciation of modern ways of currency management and counterfeits detection, analysis and prevention. The choice of Central Bank of Germany for the study was based on its structure and information technology systems that have successfully supported development in the automation of currency management in the Euro Zone. The study tour was organized through the Central Bank of Germany Centre for Technical Central Bank Cooperation, with which the CBK has a working agreement for technical support in capacity development.
- The CBK team was able to appreciate a highly automated cash management system that includes the processing equipment, the processes used, the standardized cash containers and the elaborate security surveillance systems. The team also visited the National Analysis Centre sections for damaged currency and counterfeit analysis in the Mainz Branch of the Central Bank of Germany. The team also got an overview of the IT systems that support the Cash Management Cycle and provide requisite management reports.
- The team made several recommendations on how cash management in CBK could be improved with available technology and infrastructure to enhance efficiency of existing systems and shorten cash processing to meet the objectives set out in the COBA Department's Strategic Plan.

- Two (2) members of staff from COBA attended the Advanced Banknote Managers course at De la Rue in the UK from June 21 to July 2, 2010. The focus of the training was currency production/printing processes; principles of security features in bank note papers, banknote durability issues, paper grammage, counterfeits and counterfeiting and public education. The team's recommendations included the need for CBK to consider incorporation of second generation security features in its notes as well continuous public education in order to fight counterfeiting.

(b) Monetary Operations and Debt Management Department

Four (4) staff undertook a study attachment to the Polish Central Bank in the area of primary and secondary markets with the key focus areas being government securities primary market, government securities secondary market, market structure and financial literacy. Other three (3) staff undertook a study at the Czech Central Bank. The study focused on evaluation of monetary policy framework, liquidity management and market analysis, liquidity forecasting and strategies used in conducting monetary policy.

The following was undertaken;

- An inception Report was prepared at the commencement of the TA's assignment in October 2010 as required. The report highlights the key activities to be undertaken by the TA including capacity building in the areas of Bond Analytics, Reserves Management and Bank Risk.
- The department identified the need to enhance capacity of its members and technical staff on monetary policy implementation through training and study visits to selected Central Banks which included the Czech Central Bank. The Bank was chosen because of its success in the conduct of monetary policy and primary dealership for government debt instruments which would be of benefit the MODM Department. To actionalize this, visits to the Czech Central Bank were made in October 2009 and to the Polish Central Bank in November 2009. The lessons learnt from the study tours have been compiled and include issuance calendar for debt instruments, including Treasury Bills and Bonds, non competitive auctions, Treasury bonds switching auctions, Treasury bond buy-back auctions, sale of Treasury Securities on the retail market, determination of the cut-off and dissemination of results and public debt strategy. Additionally, the team obtained information on the institutional structure of the securities market and Primary Dealership and public investor education and awareness. These lessons have been implemented, with the Department having organized an East Africa sub-regional Workshop on Public Education and Awareness as part of the requirements of the Monetary Affairs Committee (MAC) and invited a resource person from the Polish Central Bank. The Department has also participated in two Workshops organized by the Polish Central Bank under the sponsorship of Financial and Legal Sector Assistance Programme (FLSTAP) and the UNDP Project. One of these workshops was held from 5th to 9th October 2009 at Czech Central Bank, Prague and the other one was held from 25th to 27th November 2009 at Polish Central Bank, Warsaw.
- Additionally, a second TA for Monetary Operations and Securities Markets Development (MOSMD) was brought on board in October 2010. Through his technical support, the following was undertaken:

- ✓ Supported by the TA, the Financial Markets team undertook a variety of activities viz: Revision of the Debt Auction Market Methodology; reconstituting Market Leaders Forum to ensure that it continues to provide policy direction that ensures that market reforms meet objective of raising capital in a cost effective manner that supports growth and developmental targets; updating the Debt Borrowing Program; development of the framework for educating and marketing to investors in government debt with view to enabling issuance of debt at optimal rates.
- ✓ Strategized on implementation of technical programs that are aimed at streamlining efficiency of bidding and information dissemination program during the 1st half of 2011.
- ✓ Completed Review of proposed CBK "Investment Guidelines & Procedures". Based on past experience, the TA provided written and verbal guidance on best investment practice and experience of other central banks.

(c) Research Department

During the project period, eight (8) staff were trained in monetary block model and later participated in the development of the same. Additionally, high level policy reviews were conducted for other banks within the East African countries on convergence of monetary and fiscal policies and analyses.

The Technical Advisor undertook several activities in support of the Department as follows:

- Coordinated the CBK/University of Oxford Book Project "*Kenya Policies for Prosperity*" (Payment logistics, final proofs and general administration of the book project). The book, which was launched in February, 2011 was published with support from EC and UNDP in addition to other funders including IDRC, USAID, AfDB and DFID.
- Attended African Economic Research Consortium Special Senior Policy Seminar as a Discussant, drafted a paper on "Debt Relief in Africa and their Success" for the Governor as an input for a book and wrote a framework paper on "How to Restructure the Central Bank Rate" for CBK.
- In collaboration with other experts the TA wrote two chapters for the book "*Kenya: Policies for Prosperity: Banking Sector Stability, Efficiency and Outreach in Kenya and Growth Analysis and Diagnostics for Kenya*"; and with the Macro modelling team papers, produced two Papers on "*Review of Macro Models and Theoretical Framework of the CBK Macro Models*"
- Developed three ToRs for activities to be undertaken by Research Department and the MPC: (i) CBK Macro Model Peer Reviewers, (ii) Research Consultancy for Interbank, and (iii) the Evaluation of the operations of Monetary Policy Committee.

2.5: Outcome on final beneficiaries and/or target group and the situation in the target country

Despite the inability by the project to attract TAs in good time (one department did not manage to attract a TA), the outcome of the results has been quite impressive. The TAs in place re-pumped the banks capacity in the areas of specialization. Additionally, the study visits by the bank staff enhanced their capacity to deliver in specific expert areas as evidenced by this report and the current performance of the bank.

2.6: Materials produced

Several publications and reports were produced. These included reports written by the staff upon return from missions. Other works include *CBKs Investment Guidelines & Procedures*, *inception reports*, *Kenya Policies for Prosperity*, paper on *How to Restructure the Central Bank Rate for CBK*, *Review of Macro Models and Theoretical Framework of the CBK Macro Models* and a discussion note for the *CBK for G20 on Role of Macroeconomic Policy in Post Crisis World-Kenya Experience*.

2.7: Contracts (works, supplies and services) above 10,000 Euros

During the implementation period, no contract above 10,000 Euros was awarded.

2.8: Continuation and follow up actions after end of support by EU

As noted by the Bank, the greatest success of the project support was the development of the CBK Macroeconomic Model in the Research Department which will enable the Bank to improve its forecasts and policy analysis, improve support to the Monetary Policy Committee (MPC) as well as put in place policies to lower inflation down to below 5% target. In addition, the support of EC and UNDP towards the book *Kenya: Policies for Prosperity* enabled its eventual launch in February 2011. The book addresses key issues that face economic policy makers in the country.

Reforms in MODM have made the capital market and auction system more efficient, while reforms being undertaken by COBA have resulted in among other things, reduced operations costs for commercial banks.

Notably, support from the EC and UNDP has been instrumental in assisting the Bank to leverage implementation of various activities in the targeted Departments.

As a result of the support provided during the implementation period, the bank will continue fast-tracking reforms. Additionally, the longer term engagements/links established with other banks will enable CBK to continue exchanging technical/advisory information with their experts.

CBK will continue with her efforts to improve the performance of the three departments amongst others. Having developed the capacity of selected CBK staff, it is envisaged that they will continue to follow up related activities and ensure continued improvement in their departments.

2.9: Mainstreaming cross cutting issues

The three departments will continue working closely with a view to addressing cross-cutting issues and enhancing delivery of efficient and effective services

2.10: Monitoring and evaluation

During the project period, the steering committee and CBK continued to track the implementation of activities. The banks monitoring and evaluation system will continue apply in line with the approved policy.

2.11: Lessons learnt

- (a) It was difficult to outsource experts in central banking from the market.
- *Because of the short term nature of the assignments, prospective candidates had a fear factor in relinquishing their engagements.*
 - *It is important to define alternative approaches to resolving draw-backs to project implementation before a project is approved/an agreement is signed.*
- (b) The expectations in terms of remuneration were more than what had been factored in the project budget.
- *It is important to conduct a quick survey to determine market rates for staff to be hired and provide a variance for remuneration within limits before a project is approved/an agreement is signed.*

3.0: PARTNERS AND COOPERATION

3.1: Relationship between formal partners

During the implementation period, the partners maintained a formal relationship and each partner attended to specific roles as outlined in the project document/agreement. Partners met periodically to deliberate on the project implementation and provide further guidelines on issues related to implementation of the project.

3.2: Continuation of the partnership

The current partnership to support the CBK Capacity Building project terminated in December 2010 as per the project document duration and agreement. However, all parties can still negotiate further partnerships depending on the challenges/needs to be addressed and realignment with own policies.

3.3: Relationship with other organizations involved in the implementation of the action

All other parties involved during the implementation of the project were contacted depending on the gaps as identified by the bank eg; other banks which have now linked up with CBK. All involved conducted selves professionally and it is anticipated that even though the project had ended, backward-forward linkages will continue for the benefit of CBK and others.

3.4: Links and synergies with other actions

During the implementation period, the bank made links with other institutions eg; CBK/University of Oxford Book Project in supporting the book "Kenya Policies for Prosperity". These included IDRC, USAID, AfDB and DFID. The Bank also linked up with Swedish Central Bank for her Currency Policies, Strategies and Operations division.

Deliberate networks with Central Bank of Germany were established and the bank exposed Branch Managers to modern ways of currency management and counterfeits detection, analysis and prevention. CBK has a working agreement for technical support in capacity development.

3.5: Other EU grants

Not applicable under this agreement.

3.6: Evaluation of the cooperation with the services of the contracting Authority

During the implementation period, cooperation with the services of the contracting Authority was satisfactory.

4.0: VISIBILITY

The visibility of the Commission was assured as outlined in the EC-UN visibility guidelines. Throughout the period, visibility was achieved through various fora. The Project offices were branded and the contribution of EC and UNDP highlighted at relevant events including meetings, workshops, cocktails and advertisements.

NB:

At the request of EU, in this report, the following banks have been referred to indicated below:

	Bank known as:	EU Preferred name:
1.	<i>Deutsche Bundesbank</i>	<i>Germany Central Bank</i>
2.	<i>Riksbank</i>	<i>Swedish Central Bank</i>
3.	<i>Czech National Bank</i>	<i>Czech Central Bank</i>
4.	<i>National Bank of Poland</i>	<i>Polish Central Bank</i>

VII: FINANCIAL IMPLEMENTATION

PROJECT 1KEN08104 CENTRAL BANK OF KENYA DECISION CAPACITY BUILDING PROJECT

FINANCIAL REPORT FOR THE PERIOD JANUARY 2009-DECEMBER 2010

PROJECT TITLE: CENTRAL BANK OF KENYA DECISION CAPACITY BUILDING PROJECT

PROJECT NO. 00062433	Year I	Year II
Total project contributions:		
UNDP TRAC Funds	33,436.26	86,368.29
Funds received from the European Commission:	198,999.00	0.00
Total Contribution:	232,435.26	86,368.29
Disbursement		
UNDP TRAC funds-04000		
Institutionalization and reform (trainings & workshops)	33,436.26	65,217.41
EC Funds		
Technical advisory support-Senior Technical Advisors	77,208.00	96,492.00
Total expenditure:	110,644.26	161,709.41
Administrative costs:		
Max. 7%) total direct eligible costs of the action	5,404.56	6,754.44
Available Fund Balance		
UNDP TRAC Funds	0.00	2,284.63
EC Funds	121,791.00	19,894.44
Less: Administrative costs	5,404.56	6,754.44
Total Available Funds	116,386.44	13,140.00

Please note that all financial information described above is provisional until a certified financial statement has been issued by the UNDP Controllers office

Dated 30th June 2011.



Annual Financial Report to European Commission in Euros:

Number of the EC Agreement: STABEX 1992/1993 FMO-MSM/EA

Title of the Action: Central Bank of Kenya Decision Making Project

January 2009 - December 2010 in EUROS



EXPENSES	All Years		Year 1				Year 2	
	Unit	# of units	Unit Rate (EUR)	Costs (in EUR)	Unit	# of Units	Unit rate (in EUR)	Costs (in EUR)
1. Technical Assistance								
1.1 Local-Reimbursement for salary expenses (TA1)	Month	24	6,434	154,416	Month	12	6,434	77,208
1.2 Local-Reimbursement for salary expenses (TA 2)	Month	3	6,428	19,284	Month	-	-	-
2. Travel								
2.1 Reimbursement for seminar and related expenses	-	-	-	-	-	-	-	-
3. Other costs, reimbursable								
3.1 Advert Nation and Standard Media Group	-	-	-	-	-	-	-	-
6. Other								
7. Subtotal direct eligible costs of the Action 1-6 including potential future sources of funding	-	-	-	173,700	-	-	77,208	96,492
8. Provision for contingency reserve (max 5% of 7, subtotal of direct eligible costs of the Action)	-	-	-	-	-	-	-	-
9. Total direct eligible costs of the Action (7+8)	-	-	-	173,700	-	-	77,208	96,492
10. Administrative costs (max 7% of 9, total direct eligible costs of the Action)	-	-	-	12,159	-	-	5,404.56	6,754.44
11. Total eligible costs (9+10)	-	-	-	185,859	-	-	82,612.56	103,246.44

* Exchange rate considered as 1 EUR = 1.29 US\$

The European Commission may wish to publicise the results of Actions. Do you have any objection to this report being published on the EuropeAid website? If so, please state your objections here.

No.

Name of the contact person for the Action:



Christopher Gakahu
Deputy Country Director (P) a.i

Location: UNDP
Nairobi-Kenya

Signature

A handwritten signature in black ink, appearing to read 'Christopher Gakahu', written over a horizontal line.

17.11.2011