



Commercial Paper

Commercial Paper offers investors short-term investment opportunities at yields above the Kenyan Treasury bill rates. The variety of programs available in the Kenyan Commercial Paper market offers investors a spectrum of risk/reward profiles to suit their individual investment needs.

Commercial Paper is...

A short-term unsecured promissory note issued by corporations to finance working capital needs. By borrowing directly from investors via the market, Commercial Paper offers corporations an alternative to bank overdraft financing. Due to the high costs associated with bank overdrafts, Commercial Paper can offer high interest premiums to investors and still receive better rates than bank financing.

The most common tenors for Commercial Paper are 30, 60, 90, and 180 days. Commercial Paper facilities in Kenya range in size from Kshs. 100 million to 1 billion. The program size is the maximum amount a corporation can have outstanding (borrow) at any given time. All Commercial Paper programs must be reviewed and approved by the Capital Markets Authority on an annual basis. While the minimum investment is Kshs. 1 million, most investors are institutional and invest in blocks of Kshs. 10 million and larger.

Investment Benefits of Commercial Paper

- High interest premium over Kenyan Treasuries
- Flexible short-term tenors: 30, 60, 90 and 180-day paper available
- Selection and variety of risk/reward profiles, including guaranteed and non-guaranteed paper
- Regular availability

What Corporations can issue Commercial Paper?

Since Commercial Paper is an unsecured promissory note, any company issuing Commercial Paper must represent a good credit risk. Commercial Paper issuers are typically household names and have a substantial net worth. The Capital Markets Authority has the following approval requirements for companies wishing to issue Commercial Paper:

1. Minimum paid-up share capital of Kshs. 50 million
2. Corporate profit for two of the last three years preceding application
3. Three year average Debt/Equity ratio less than or equal to 400%
4. Three year average Operating Cash Flow/Total Debt greater than 40%

Kenyan corporations who do not meet these requirements can only issue Commercial Paper with a backing guarantee. Guarantor institutions are often large banks or insurance companies and must meet the Capital Markets Authority guidelines.

Some companies, currently issuing Commercial Paper in the Kenyan market, have been credit rated by Global Credit Rating Company (GCR). GCR is the only credit rating agency approved by the Capital Markets Authority. Credit Rating agencies provide independent third-party analysis and review of corporations and their credit risk. Companies currently offering Commercial Paper include Athi River Mining Ltd and Crown Berger Ltd.

Lower Cost for Borrowers means Higher Rates for Lenders

The interest rate paid on Commercial Paper must be set above the Treasury bill rate of the same maturity because government debt is inherently safer than private sector debt. As well, Commercial Paper interest rates are set below the prevailing bank overdraft rates because the funds are raised directly from investors avoiding the high cost of bank services (or intermediation). *Disintermediation*, or avoiding expensive bank services, allows corporations to save costs while paying high premiums to investors. In today's market, Commercial Paper programs pay premiums ranging from 0.5% to 2.5% above the 90-day Treasury bill.