



Banking, Finance & Projects

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KENYA

- Kenya 2026 Banking Law Reforms: KESONIA, risk-based pricing and the mandatory loan transition explained



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Kenya 2026 Banking Law Reforms: KESONIA, risk-based pricing and the mandatory loan transition explained

The Central Bank of Kenya (CBK), in exercise of its powers under the CBK Act and the Banking Act, has introduced a raft of measures that have revolutionised lending in Kenya.

KESONIA: The technical foundation of risk-free rates

Kenya's banking framework is moving from bank specific base lending rates to a more transparent, risk based, and supervision led system to strengthen market confidence, improve monetary policy transmission and align with international best practices.

Following the review by the CBK of the application of the risk-based credit model (RBCM) that was introduced in 2019, the CBK noted that banks were not strictly adhering to RBCM since each bank used its own specific internal base rate for lending transactions. Additionally, not all Kenya shilling variable loans were priced on the borrower's risk profile.

The CBK then engaged various stakeholders in a bid to streamline lending practices, with the result that the CBK would introduce a common reference rate (the Kenya Shilling Overnight Interbank Average

(KESONIA)) to be adopted by banks in determining loan pricing. This was to ensure transparency in lending and alignment with global best practices, given that internationally recognised base rates such as the Secured Overnight Funding Rate (SOFR) and Sterling Overnight Index Average (SONIA) are derived from short-term market rates.

Additionally, each bank would determine its own premium (known as K), which would be added to KESONIA. The CBK and the stakeholders also agreed to a phased implementation of the revised model to ensure that there was no market disruption. The shift to the revised model was to commence in September 2025 for new variable Kenya shilling-denominated loans, with a mandatory transition deadline of 28 February 2026 for existing variable Kenya shilling-denominated loans.

Consequently, the CBK has modernised the benchmark interest rate framework by introducing KESONIA as the common base rate for variable rate Kenya shilling loans.

What is KESONIA and how does it affect my loan?

Simply put, KESONIA is an average of the overnight interest rate at which banks lend and borrow unsecured funds, which was previously known as



the average overnight interest rate. It is dependent on the volume of overnight bank transactions, as it is a weighted average.

Given that daily interbank activity may vary from time to time, KESONIA varies based on the average volume of transactions for a particular interest period (30 days). Changes in KESONIA will invariably affect the interest rates.

How does the CBK determine KESONIA?

The CBK collects data from overnight interbank lending transactions, which could be up to KES 60 billion a night, and calculates the weighted average of those transactions. The CBK also compounds the daily overnight rates in each day over an interest period (preferably 30 days) to determine the KESONIA compounded index.

The CBK will publish the KESONIA rate and the KESONIA compounded index daily at the start of business (at 9h00) for rates applicable to the previous day, with the last published rate applying over weekends and public holidays.

How does the overnight interbank market work?

Banks lend and borrow from each other overnight at a particular interest rate to meet liquidity requirements, with such loans being outstanding for typically one day or less. It is the data in respect of such lending activity that the CBK then collects for purposes of determining the average.

The Risk-Based Credit Pricing Model

How the KESONIA plus premium formula works

Banks are required to display on the Total Cost of Credit website their respective total cost of credit (TCC). TCC comprises (i) KESONIA, (ii) the premium (K) and (iii) a component of the borrower's risk profile.

Final lending rate = KESONIA + Premium (K)

Breaking down the K factor: borrower risk, operating costs, and shareholder return

The premium (K) is made up of a bank's operating costs, the return to shareholders (profit) and the borrower's risk premium. Pricing differentiation occurs through the "K", which is determined by each bank and is specific to each borrower. According to the Total Cost of Credit website, the K ranges from as low as 5.5% to as high as 14.5%.

A borrower's credit risk assessment is based on the borrower's probability of default and is drawn from a borrower's credit history, repayment behaviour, existing debts and the quality of any security offered by the borrower. Together, they produce a credit risk premium that sits at the heart of the "K" factor.

The second element is the bank's cost of doing business, which includes the bank's operating costs such as salaries and directors' allowances, repairs and maintenance, rent and other operating expenses. Thirdly, the bank will consider the return to its shareholders, being the profit.

Why must existing loans transition by February 2026?

The CBK allowed banks a six-month grace period to allow a seamless transition to KESONIA for existing variable-rate Kenya shilling loans, with the deadline being 28 February 2026. With effect from 1 September 2025, KESONIA applies to all new variable-rate Kenya shilling-denominated loans. The transition period was to allow banks to publish their weighted average lending rates and all costs associated with the lending on the Total Cost of Credit website that was jointly developed by banks and the CBK.



Does the transition to KESONIA apply to all loans?

KESONIA only applies to variable-rate Kenya shilling-denominated loans. Fixed-rate loans and foreign currency loans are also excluded from the revised model, given that these kinds of transactions have unique contracting arrangements that determine their pricing.

Foreign currency loans also commonly reference the relevant currency specific benchmarks, including SOFR for US dollars, €STR for Euros, and SONIA for British pounds.

What happens if KESONIA is unavailable?

In case KESONIA is unavailable, borrowers have a fall back on the Central Bank Rate as the alternative reference rate. This continuity mechanism should be embedded in loan agreements as a standard contractual provision to prevent uncertainty.

Where can borrowers compare rates?

In 2017, the Total Cost of Credit website [Total Cost of Credit](#) a joint initiative of the CBK and the commercial banks, was developed. The website is in the process of being revamped to ensure that it accurately reflects information in relation to loan pricing across different banks, thereby enabling meaningful comparison of borrowing costs across banks.

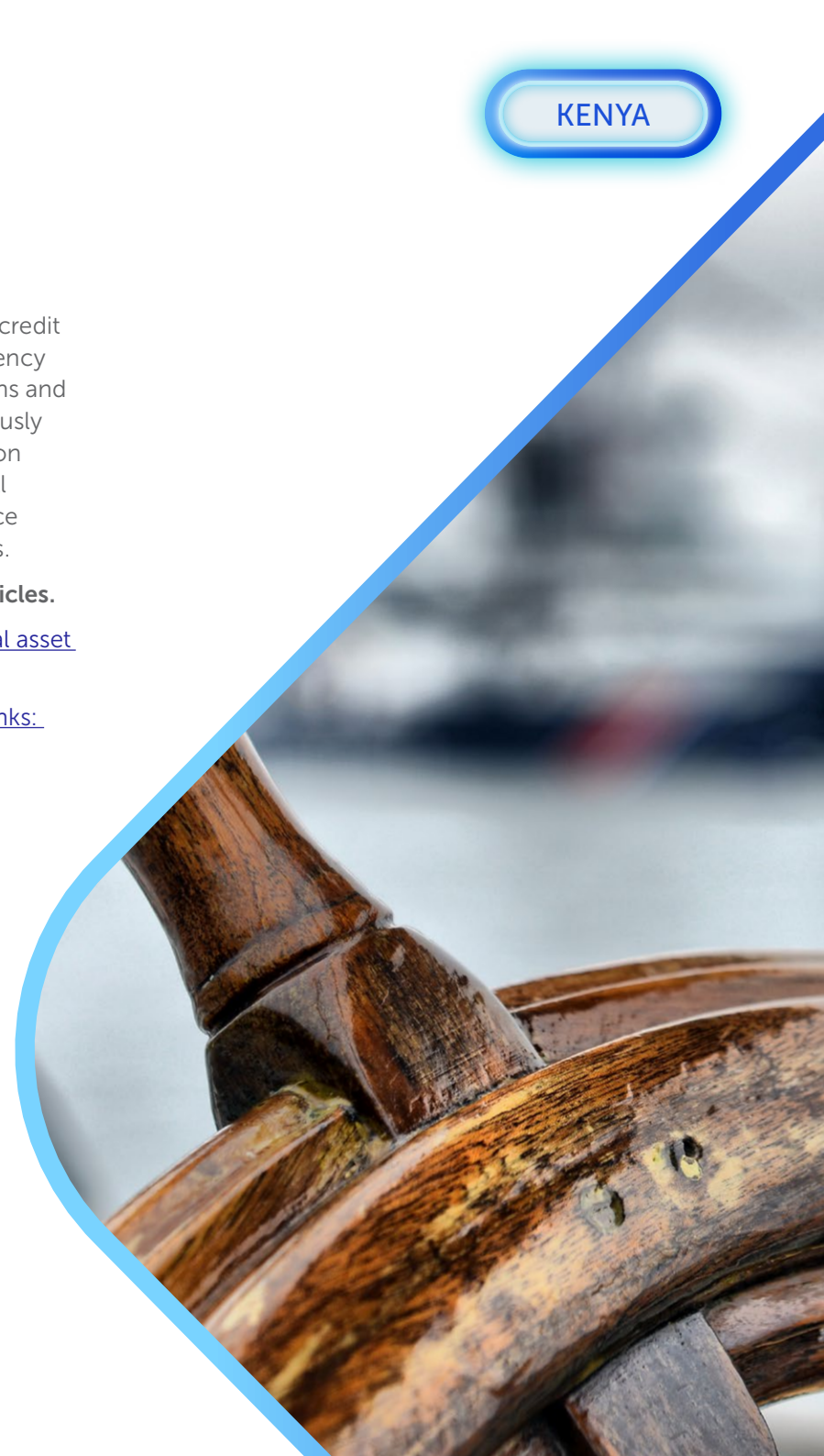
Conclusion

The banking law reforms introduce clarity in credit pricing models, which will promote transparency and reshape how banks assess risk, price loans and interact with customers. Banks that continuously update their customers on the implementation of the revised risk-based model contracts will be better able to comply smoothly and reduce regulatory, operational, and reputational risks.

You may also want to read the following articles.

- [Kenya VASP Act 2025: A new era for virtual asset regulation](#)
- [Capital management and planning for banks: when strategy must meet innovation](#)

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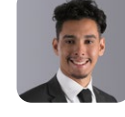
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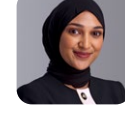
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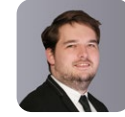
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Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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