

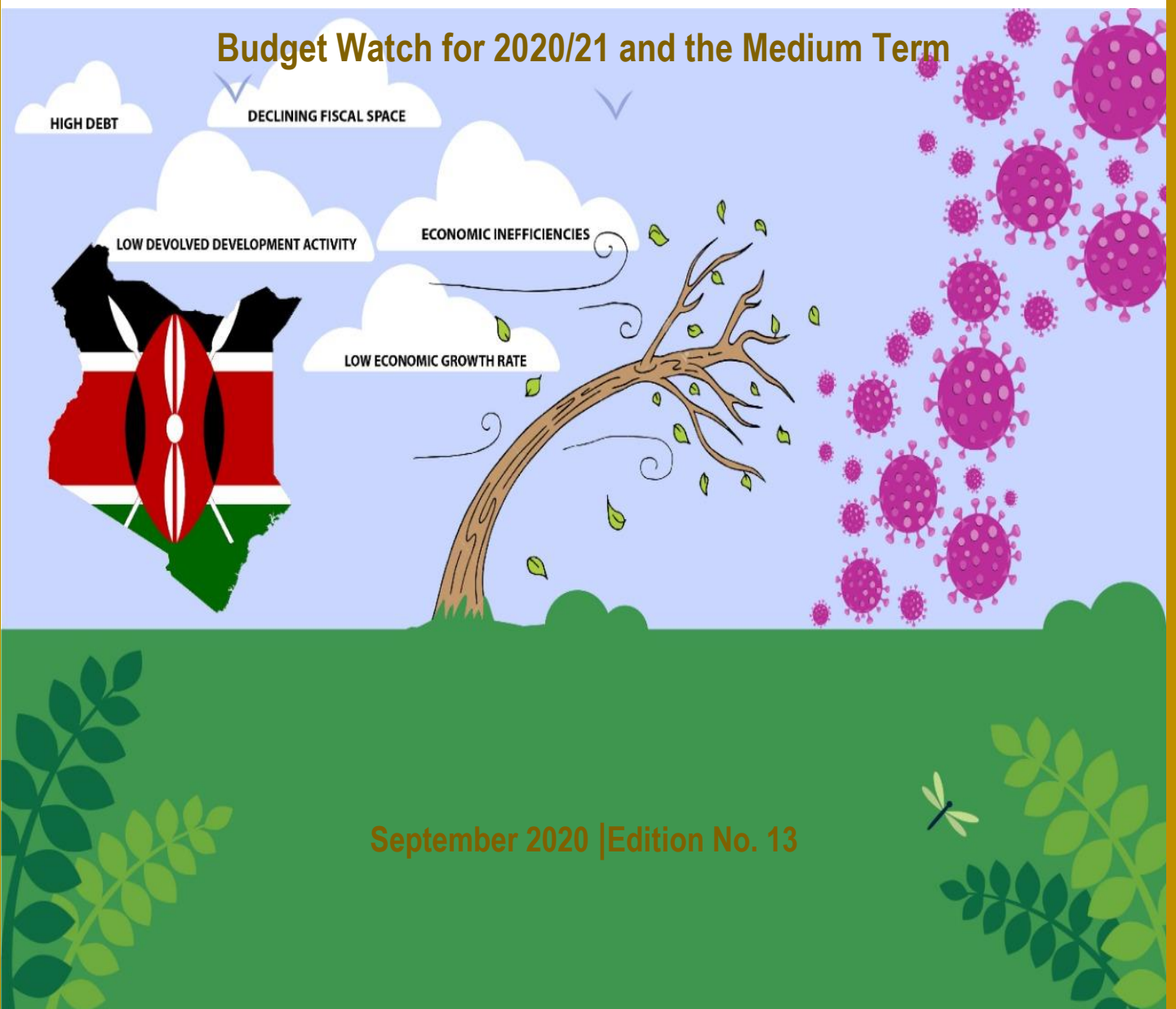


REPUBLIC OF KENYA

PARLIAMENTARY SERVICE COMMISSION  
Parliamentary Budget Office

*THE CLOUDS ARE GATHERING AS THE WINDS  
BLOW AWAY THE PANDEMIC*

**Budget Watch for 2020/21 and the Medium Term**



September 2020 | Edition No. 13

### **Disclaimer**

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The Budget Watch disseminates findings by the Parliamentary Budget Office on key issues regarding implementation of the budget estimates in a particular financial year. The 13<sup>th</sup> edition of the Budget Watch has been prepared to facilitate monitoring of the budget for the financial year 2020/2021 by the Legislature and other stakeholders. The findings, interpretations and conclusions expressed in this publication are entirely those of the authors. They do not necessarily represent the views of the Parliament of the Republic of Kenya.

This report is available at the Parliament’s website ([www.parliament.go.ke](http://www.parliament.go.ke))

## List of Acronyms and Abbreviations

ASAL                      Arid and Semi-Arid Land

ADB	African Development Bank
ADP	Annual Development Plan
BPS	Budget Policy Statement
CBK	Central Bank of Kenya
CFS	Consolidated Fund Services
CFSP	County Fiscal Strategy Plan
CoB	Controller of Budget
ERS	Economic Recovery Strategy
FY	Financial Year
GDP	Gross Domestic Product
GOK	Government of Kenya
HELB	Higher Education Loans Board
ICT	Information, Communication and Technology
KM	Kilometres
KNBS	Kenya National Bureau of Statistics
KPIs	Key Performance Indicators
KPLC	Kenya Power and Lighting Company
KSHS	Kenya Shillings
MDAs	Ministries, Departments and Agencies
MoU	Memorandum of Understanding
MSE	Micro and Small Enterprise
MT	Metric Tonnes
MTDS	Medium Term Debt Management Strategy
NHIF	National Hospital Insurance Fund
NMS	Nairobi Metropolitan Services
NSE	Nairobi Securities Exchange
OVCs	Orphans and Vulnerable Children
PBO	Parliamentary Budget Office
PMI	Purchasing Manager Index
PWDs	People with disabilities
REREC	Rural Electrification and Renewable Energy Corporation
SEZ	Special Economic Zone
SMEs	Small and Medium Enterprises
TVET	Technical and Vocational Education and Training
UHC	Universal Health Coverage
US	United States
VAT	Value Added Tax
VTC	Vocational Training Centre

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## Chapter One:

# Macroeconomic Context and Revenue Outlook

*“The pandemic will end eventually, but its impact on the economy will persist long after to remind us of the poor investments we have made in the health sector”*

## 1.0. Global economic downturn: can the 2020/2021 budget steer the economy through the stormy waters?

**The 2020/2021 budget is a crisis budget that must balance between mitigating the socio-economic impact of a health pandemic while still providing adequately for existing administrative and economic needs.** This budget is being implemented at a time when the economy is navigating uncharted waters on account of the COVID-19 pandemic. This is a challenging context for the government given the highly uncertain economic outlook of the country and the expected impact on revenue performance. Though the government has set aside funds in the budget to mitigate the adverse effects of COVID-19 on the economy, a worsening of the crisis could easily weaken the economy further thereby constraining the fiscal space and reducing the ability of the government to respond adequately to the crisis.

**The 2020/2021 budget has proposed a stimulus package to alleviate the economic burden of the health crisis particularly on the vulnerable households. However inherent accountability issues may hinder the achievement of targeted results of this stimulus.** The eight point economic stimulus programme contained in this budget is expected to cushion vulnerable citizens and businesses adversely affected by the COVID-19 pandemic. It proposes several interventions which include the following: rehabilitation of access roads and foot bridges, wells, water pans and underground tanks in ASAL areas; the *Kazi Mtaani* programme for unemployed youths; improving education outcomes through the improvement of infrastructure, increased capitation and recruitment of intern teachers; provision of affordable credit to businesses; fast-tracking payment of VAT refunds and pending bills; purchase of locally assembled vehicles to safeguard jobs; tourism promotion as well as interventions under agriculture and food security. Furthermore, the 2020/2021 budget also provides an allocation of Kshs.4.3 billion for the hunger safety net programme.

**The loss of income occasioned by the COVID -19 pandemic has been significant and the proposed interventions, while useful, may not fully alleviate the economic burden particularly in vulnerable households.** Indeed, even before the pandemic struck, unemployment was high in the country especially for the youth; many poor people especially the urban poor with little income were already skipping meals and serving short term menial jobs; the health sector was ill-equipped; the SMEs were struggling to survive and access credit from banks and the country as a whole was not and has never been food secure. The pandemic has therefore simply worsened an already existing dire situation and exposed the soft underbelly of the country's economic growth story. Despite the country's relatively reasonable economic growth over the past few years, it has failed to translate into meaningful and reliable employment opportunities for the youth resulting in short term unsustainable interventions such as the *Kazi kwa Vijana* programme and now the *Kazi Mtaani* initiative. These programmes offer small stipends to the youth in exchange for short term menial jobs that do not translate into meaningful, employable skills. In addition, the budgetary allocation of Ksh. 4.3 billion for the hunger safety net programme is simply not adequate to alleviate the needs of those experiencing financial distress, given the prevailing statistics on the impact of COVID-19 on households.

**Significant interventions have been carried out to strengthen the healthcare system– but gaps still exist.** In the Budget Statement for 2020/2021, the Cabinet Secretary of the National Treasury reported that in response to the pandemic, the government was implementing the following interventions in healthcare: Kshs.1.2 billion for the recruitment of an additional cohort of 5,000 healthcare workers to



support local health staff for a period of one year; Kshs. 500 million to supply 20,000 locally made beds and beddings to public hospitals; and Kshs. 25 million to support the establishment of 50 modern walkthrough sanitizers at border points and main hospitals across the country. This is in addition to other resource allocations to various sub-sectors under health as well as all public hospitals in order to improve the functionality of the health sector.

**Concern over alleged misuse of COVID-19 funds is hampering the fight against the pandemic.** A recent report by the Ministry of Health giving a breakdown of how the COVID-19 funds have been utilized stirred controversy as members of the public questioned the costs of some of the procured/leased items. The perception that the emergency funds are being misused is a blow to the fight against the pandemic as it has generated mistrust and apathy among the citizens with some downplaying the gravity of the pandemic or dismissing it altogether. In times of emergency, misuse of funds can happen due to lack of adequate time to carry out proper scrutiny. It is important for the legislature to continually demand full disclosure, transparency and accountability and periodically review the use of the COVID-19 funds especially those outside the budget process, in order to ensure that the intended purpose is served. A forensic audit of funds spent towards this pandemic since March to end of August will re-assure Kenyans and those who contributed funds for this emergency of accountability.

## 1.1. Macroeconomic context of the 2020/2021 budget

### 1.1.1. Global economic outlook

**A global recession is looming due to severe disruptions brought about by COVID-19 containment measures which have significantly weakened economic activity.** Supply and demand shocks brought about by total/partial lockdowns and other directives aimed at ensuring social distancing is upheld are expected to reduce consumption, investment, and hamper both domestic and international trade [1,2]. As a result, some projections have indicated that the looming global recession may be greater than the global financial crisis. The IMF is projecting a global GDP contraction of -4.9% in 2020 whereas the World Bank is projecting a contraction of -5.2%. It should be noted that even before the COVID-19 pandemic erupted, the global economic outlook was lacklustre, with a modest growth forecast estimated at 2.5<sup>1</sup> to 3.3%<sup>2</sup> for 2020 – and these were downgrades from previous forecasts. The COVID-19 pandemic has therefore significantly worsened an already bad situation.

**Sub-Saharan Africa which escaped the worst of the global financial crisis is projected this year to go into its first recession in 25 years [1].** The African Development Bank (AfDB) projects that Africa's economy is likely to contract in 2020 as a result of the ongoing health crisis. The continent's real GDP is expected to contract by between 1.7% and 3.4% in 2020 as opposed to the pre-Covid-19 projection of 3.9% growth. The revised projections suggest that Africa will experience GDP losses of between \$145.5 billion and \$189.7 billion. The worst affected economies will be those that rely on commodity exports, tourism, volatile financial flows and those with high debt burdens [2]. It is estimated that between 25 million to 30 million jobs in Africa could be lost as a result of the Covid-19 pandemic [2]. Informal sector

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<sup>1</sup> World Bank projections, January 2020 Global Economic Prospects Report

<sup>2</sup> IMF Projections, World Economic Outlook, January 2020

jobs, accounting for 89% of all employment in sub-Saharan Africa, are likely to be the worst affected by the Covid-19 pandemic [5].

### 1.1.2. Domestic economic outlook

**Domestically, the COVID-19 containment measures have disrupted demand and supply chains leading to a significant weakening of economic activity.** On the demand side, mitigation strategies such as dusk to dawn curfew, the ban on public gatherings and closure of bars and restaurants significantly reduced working hours and disrupted operations of some businesses resulting in loss of employment. As a result, income from work has dipped significantly since March 2020. Within the first five weeks of the pandemic, income from work reduced by almost one third among low-income households in Kenya [7]. Subsequently, over 80% of people living in Kenya's informal settlements reported a partial or total loss in income due to the Covid-19 pandemic [6]. More households are expected to experience a dip in income over the coming months especially if new Covid-19 infections trigger further mitigation measures in the next few months. The reduced household incomes have adversely affected demand for goods and services.

**Productivity losses experienced between March and June 2020 are expected to persist for the rest of the year.** A study by the KNBS indicates that as of June 2020, 48% of Kenyans reported having worked fewer hours during the pandemic. 76% of those that worked fewer hours stated that the stay at home advisory was the main reason for reduced working hours while 21% indicated that their work prospects were hampered by the cessation of movement order [8]. As a result, many households have experienced considerable loss of income and this has had a negative impact on household spending. Going forward, reduced expenditure on non-essential items is expected to persist for the remainder of 2020 and possibly 2021 due to uncertainty about how long the pandemic and its economic impact will last. Also, Kenyans may continue facing reduced working hours for the better part of the coming financial year since the stay at home advisory is expected to remain in place. Indeed, many businesses have scaled-down operations due to disruptions in their supply chains as well as the decline in demand. A slowdown in global production along with COVID-19 restrictions including the ban on air travel adversely affected the supply of goods to Kenya. This is expected to improve slowly as countries ease their COVID-19 restrictions.

### 1.1.3. Risks to the macro-economic outlook

**The macro-framework for the 2020/2021 budget comprises an economic growth projection of 2.5% in 2020 that is expected to rebound to 5.8% in 2021.** It is expected that this growth will be supported by a stable macroeconomic environment with inflation remaining within the target range, increased private consumption and an expanded export base once the world borders re-open. Ongoing budgetary interventions especially government investments in the Big Four agenda are expected to provide the necessary impetus that will boost aggregate demand. However, this outlook is susceptible to a number of risks which if they materialize, could lead to lower than projected economic growth. The risks to domestic growth performance are embedded in inflation, the external sector, domestic investments etc

## ***Inflation***

**Though inflation has remained broadly within target and was estimated at 4.59% in June, 2020, it is still a key factor to watch for due to the expected impact on vulnerable households.** So far, declining demand and reduced money in circulation due to reduced economic activity has resulted in manageable inflation levels. The estimated inflation rate of 4.36 percent in July 2020 is a reduction from the June inflation rate of 4.59 percent mostly on account of a reduction in food prices as well as lower cost of water vendor services, house maintenance and some house rents. Going forward, the biggest risk to inflation is likely to emanate from fuel prices, desert locust upsurge, below average rainfall and the ongoing health crisis.

**The current fuel price dynamics pose a significant risk to inflation.** In July 2020, the Energy Regulatory Authority announced higher fuel prices, citing the recovery of crude oil prices as well as the increase in the petrol levy from Ksh.0.4 to Ksh.5.40. The easing of travel restrictions and phased reopening of most economies including the resumption of air travel is expected to increase demand for oil. International crude oil prices have improved significantly since May 2020 and by early July, were estimated to average 43 dollars per barrel<sup>3</sup>. Fuel is a major component in production and transportation and may, therefore, increase the price of goods and the cost of transportation. Higher diesel prices will also result in higher electricity prices due to the fuel levy component thereby increasing production costs. Notably, Kenya's petroleum pricing system has not been very responsive to changes in global oil prices. Benefits of low global crude oil prices are rarely passed on to the consumer due to many other factors such as levies and taxes determining the pricing of fuel.

**Though the population of the desert locusts has declined, they still remain a threat in some counties particularly in the Northern region.** The food and agriculture organization (FAO) indicated that by mid-July, less than 5% of the desert locust swarms would be remaining in the country as most were likely to migrate northwards into Ethiopia and South Sudan, facilitated by the prevailing winds. However, with the change of winds during the October – December short rains season, there is risk of re-invasion of the desert locusts from Ethiopia, Somalia and Yemen into Kenya.

**Below average October to December rainfall is likely to adversely affect food security outcomes.** According to information provided by the famine early warning systems network, seasonal forecasts project a likelihood of below average rainfall during the October-December short rains season as well as the March – May 2021 long rains season<sup>4</sup>. Furthermore, the floods that occurred during the March to May long rains season delayed planting in some areas and destroyed crops and eroded soil in other areas. Thus food production from this season may be slightly below average. This will have an adverse impact on food security outcomes in late 2020 and early 2021 and is likely to lead to increased food prices thereby increasing headline inflation.

## ***External sector***

**The export sector appears to have largely withstood the effects of COVID-19 in the second quarter of 2020.** Available statistics from the KNBS indicate that the value of total exports increased from Ksh.43.20 billion in April 2020 to Ksh. 48.5 billion in June 2020. This is however a slight underperformance compared to the performance in 2019 of Ksh. 48.8 billion in April to Ksh.51.2 billion in

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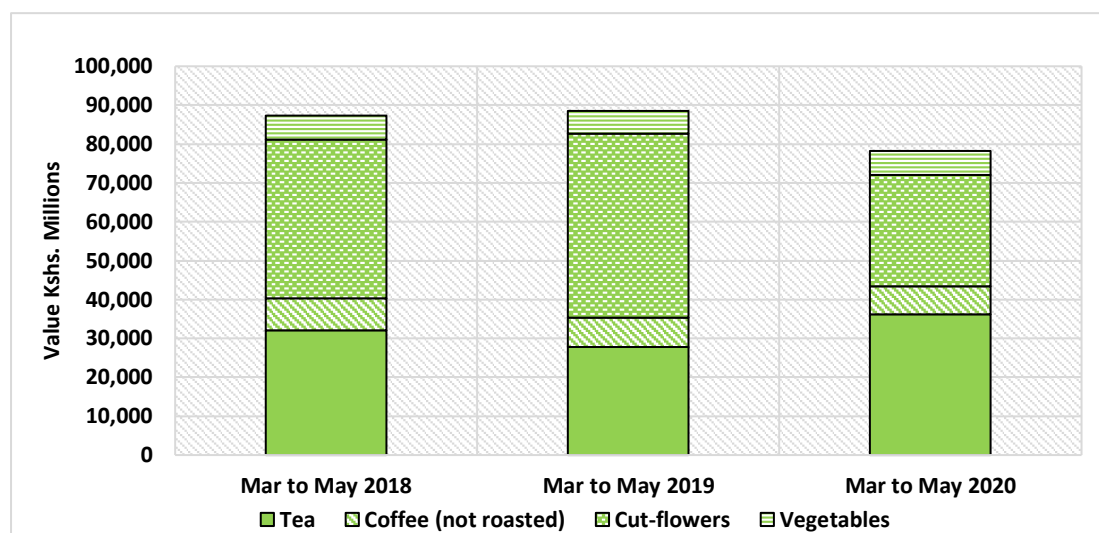
<sup>3</sup> Oil Market Report

<sup>4</sup> <https://fews.net/east-africa/kenya/food-security-outlook/june-2020>

June. The KNBS statistics indicate that Food and beverages accounted for 49.4 percent of total exports whereas non-food industrial supplies accounted for 26.35 percent of total exports by end of June 2020.

**Horticultural exports underperformed in the second quarter of 2020, but the decline was only moderate.** Between March and May 2020, the combined value of key agricultural exports such as tea, coffee, cut-flowers and vegetables was only about Kshs. 10 billion below its 2019 value. Available statistics reveal a significant increase in earnings for tea from March to May compared to a similar period in 2019. Tea earnings are reported to have increased by approximately Ksh. 8.3 billion between March and May compared to the same period in 2019. Fruits and vegetables also registered increased earnings in the same period by Kshs.4.5 billion and 370 million respectively compared to a similar period in 2019. On the other hand, the flower industry seems to have borne the brunt of the pandemic and registered a decline by Ksh. 4.4 billion in April and May compared to a similar period in 2019. Coffee also registered a slight decline in earnings by Ksh. 177 million between March and May compared to a similar period in 2019<sup>5</sup>.

Figure 1: Agricultural Exports



Source of Data: Kenya National Bureau of Statistics

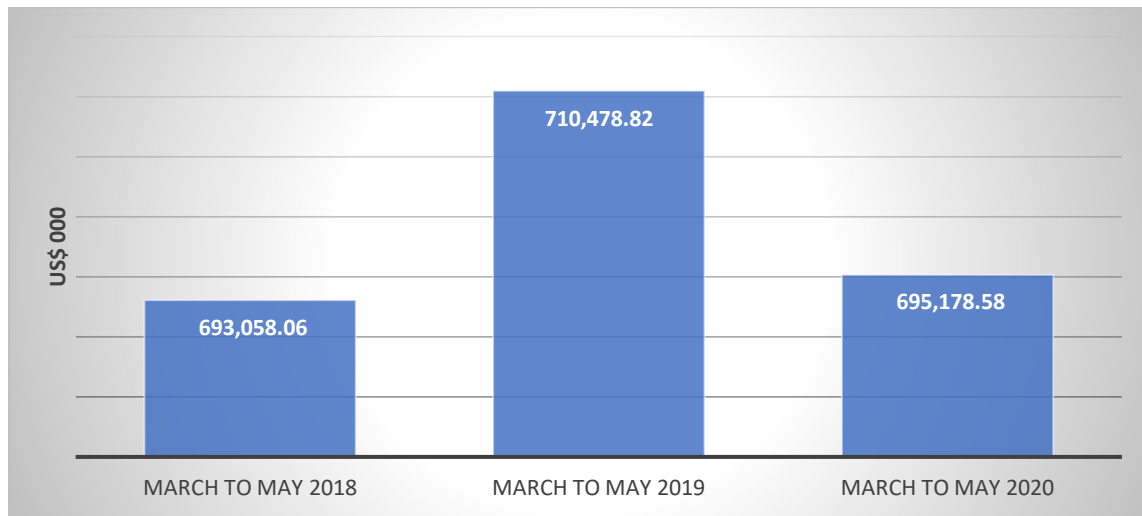
**Going forward, the risks to the export sector are likely to emanate from factors that will affect crop production such as below average rainfall performance and a desert locust upsurge.** Kenya's exports are largely agricultural and any factors adversely affecting agricultural production will significantly affect exports. Since agricultural exports are the main alternative for earning foreign exchange in the coming financial year, the poor performance of this sector will directly impact foreign reserves which are needed to cover foreign debt repayment.

**The decline in remittances is set to disproportionately affect poorer households who rely on them for household consumption, investment and accumulation of savings [12–14].** During the pandemic, 80% of surveyed households have reported that cash remittances they have received have been below pre-pandemic levels with 40% reporting remittances had decreased significantly[8]. The expected decline in remittances from abroad which stand at about 3% of GDP and had replaced Kenya's principal domestic exports such as tea and international tourism as the main source of foreign exchange is expected to negatively impact foreign reserves which are needed to cover the increasing foreign debt

<sup>5</sup> KNBS, Leading Economic Indicators, May 2020

repayment. Between March and May 2020 diaspora remittances declined by **US\$ 15 million** relative to a similar period in 2019 see figure 2.

Figure 2: Total Diaspora Remittances (USD '000)

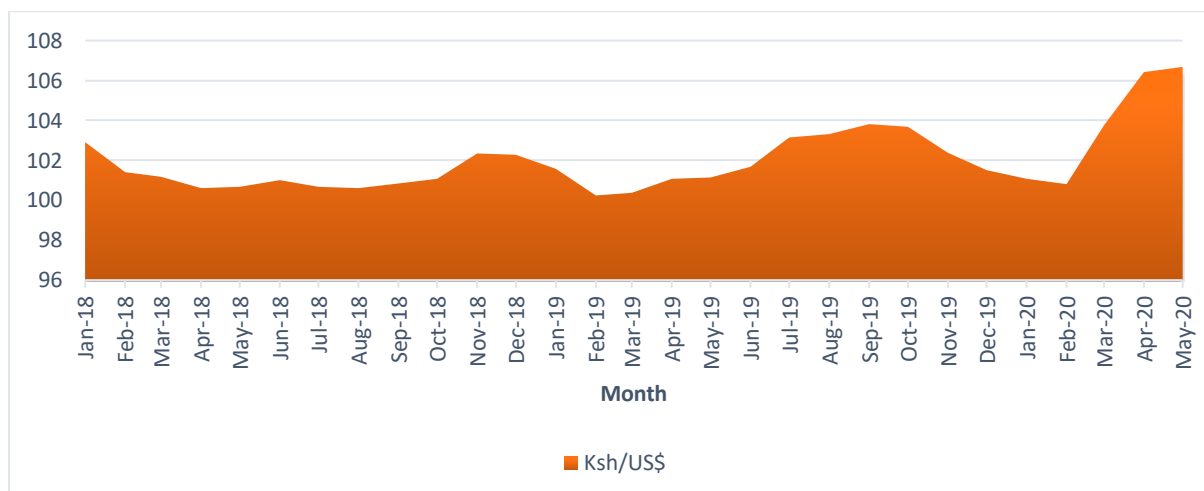


Source of Data: Central Bank of Kenya

Dwindling diaspora remittances are expected to worsen as countries in North America and Europe, the source of about 80% of Kenya's remittances, go into recession. A drop in diaspora remittances coupled with the slump in international tourism has left agricultural exports as the main alternative for earning foreign exchange.

Subdued exports and diaspora remittances, coupled with the increasing demand for US dollars globally as investors shy away from uncertainty associated with the impact of the Covid-19 pandemic on other riskier assets, has contributed to the depreciation of the Kenya Shilling. Between January 2020 and May 2020, the Kenya shilling depreciated by about 6% (see figure 3). Continued depreciation of the Kenya Shilling may contribute to higher debt service obligations in the current financial year.

Figure 3: Exchange rate KHz/US\$

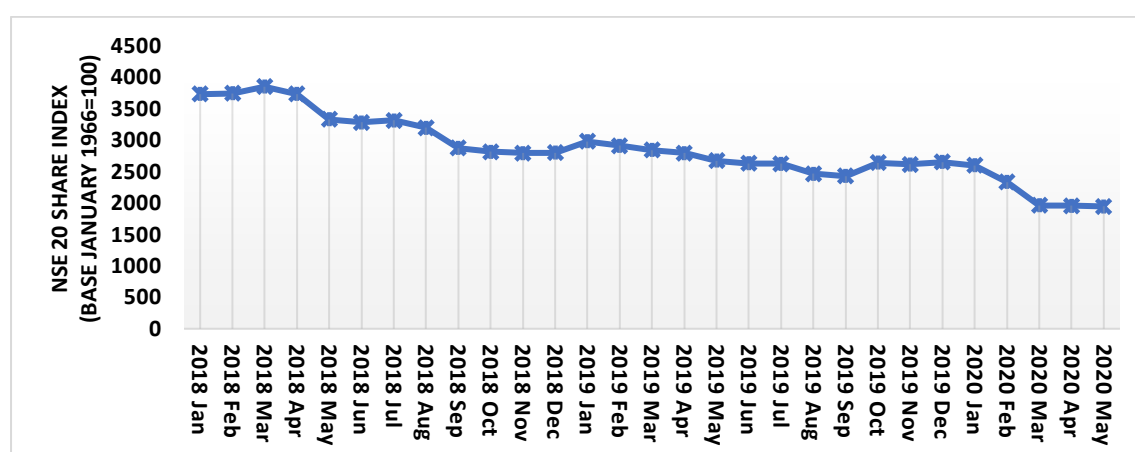


Source of Data: Central Bank of Kenya

## The capital market

**The Covid-19 pandemic is having a negative impact on the capital market.** The NSE 20 Share Index has contracted during the Covid-19 pandemic, from 2,337 points in February 2020 to 1,948 points in May 2020. This is partly attributed to the social distancing measures which have been found to have a direct negative impact on stock market returns due to their effect on economic activities[15]. With companies facing pandemic related distress, some facing the prospect of delisting, and new entrants postponing their listing plans, the risk of market concentration is expected to be exacerbated in the next couple of years. In the fourth quarter of 2019, the market value of the top five companies by market capitalization was 73% [16].

Figure 4: Performance of the Nairobi Securities Exchange



Source of Data: Kenya National Bureau of Statistics

## The Services sector

**The Accommodation & restaurant sector is arguably the worst hit sector by the COVID-19 pandemic and is estimated to have contracted by 9.3% in the 1<sup>st</sup> quarter of 2020 compared to a growth of 10.2% in 2019.** This performance is expected to have worsened in the second quarter between April and June due to stiffer restrictions announced in late March. This sector is highly dependent on the tourism sector which is estimated to have incurred a loss of about Ksh.85 billion due to the pandemic and is projected to recover by only 30% between July and December<sup>6</sup>. Other sectors under the service industry that have been adversely affected by the pandemic include the wholesale and retail sector, and the transportation and storage sector. Going forward, the phased reopening of the economy from early July could improve performance of these sectors but so long as the crisis continues, the impact will be very limited. International tourism is unlikely to pick in the second half of the year and with social distancing measures still in place, accommodation and restaurant is likely to operate below capacity for the rest of the year. The wholesale and retail sector could also benefit from the phased reopening but is likely to experience setbacks due to the reduction in consumer spending that is likely to persist to the end of the year. On the other hand, the lifting of movement restrictions and resumption of travel is expected to improve performance of the transportation and storage sector.

<sup>6</sup> Ministry of Tourism & Wildlife, media briefing, June 29, 2020



## **In view of the foregoing, is the economic growth outlook feasible?**

Due to the fluidity of the ongoing situation, it is difficult to accurately predict economic growth performance for 2020. The outcome will largely depend on the length and depth of the crisis. A surge in infections without a breakthrough in medical interventions may trigger stiffer COVID-19 containment measures in the course of the year. Furthermore, the situation is still evolving for some businesses and the impact of the early COVID-19 containment restrictions continues to be felt particularly in the accommodation and restaurant sector. Production is likely to remain muted due to declined demand and investment prospects are likely to be kept on hold pending outcome of the crisis. This will further exacerbate the impact of job losses on livelihoods.

**In view of the foregoing**, the projected real GDP growth for 2020 is between 1% and 2%<sup>7</sup>. This is nonetheless an improvement from the previous forecast of -1.5% to 1% in April 2020 due to the general easing of COVID-19 restrictions which have brought about a slight improvement in business activity as illustrated by the PMI index; and the better than expected performance of the country's agricultural exports.

**Despite the economic burden presented by the health pandemic, the situation has presented an opportunity for the country to boost the local industries.** Given the unprecedented demand for Personal Protective Equipment (PPEs) such as masks, gloves and gowns for the protection of frontline healthcare workers as well as the general public, many apparel manufacturers including SMEs in the Textiles and Apparel sector have taken to producing fabric masks and protective gowns to deal with the pandemic. Notably, RIVATEX in Eldoret and KICOTEC in Kitui have stepped up production of face masks and are receiving support from the government through the COVID-19 fund to enable continued production. Other local industries such as Haco industries are producing hand sanitisers. This is a significant boost to the manufacturing industry in Kenya and could potentially alleviate, to a small extent, the increasing unemployment problem. Going forward, this new capacity can be expanded to enable the country reduce its reliance on imported goods.

### **Keep an Eye On:**

- i. **Re-introduction of stiffer COVID-19 containment restrictions** – A worsening of the crisis could lead to reintroduction of stiffer restrictions leading to a further deterioration of economic activity. Ideally, an effective COVID-19 containment strategy should entail high level of testing, isolation and treatment as well as effective containment of vulnerable populations to mitigate severity of impact.
- ii. **Global economic performance** – A recession particularly in the country's trading partners is likely to adversely affect demand for Kenyan exports. Furthermore, tourism inflows and diaspora remittances may decline significantly if the economies of the source countries are hard hit by the pandemic thereby reducing the country's foreign exchange reserves.

## **1.2. Revenue prospects during the COVID-19 pandemic**

### **1.2.1. Tax Revenue**

**In the past, the National Treasury has consistently set unattainable revenue targets at the start of each Financial Year.** To illustrate, in FY 2019/2020, the revenue target set in the printed budget

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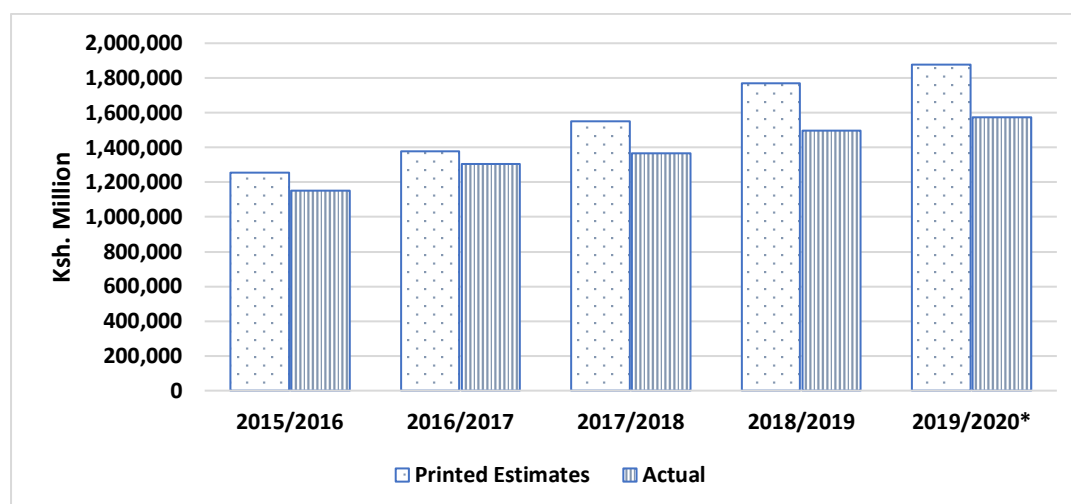
<sup>7</sup> PBO projections

estimates was Kshs. 1.88 trillion. This was initially revised to Kshs.1.84 trillion during the first supplementary budget then was further revised downwards to Kshs.1.64 trillion during second supplementary budget. However, as of June 2020, ordinary revenue collected during FY 2019/20 stood at Kshs.1.58 trillion. This is **Kshs. 300 billion** (16%) below the target that was set at the beginning of the financial year.

Table 1: Ordinary revenue performance FY 2019/2020

2019/2020 Ordinary revenue performance				
	Printed Estimates (Kshs.)	Supplementary Budget I (Kshs.)	Supplementary Budget II (Kshs.)	Actual receipts as of 30 <sup>th</sup> June 2020 (Kshs.)
<b>Total Ordinary Revenue</b>	1,877,176,497,191	1,843,812,537,631	1,643,400,000,000	1,575,195,550,892.39

Figure 5: Ordinary revenue performance



**Revenue is expected to underperform in the current financial year.** The National Treasury projects that ordinary revenue will decline from Kshs. 1,643.4 billion (16.1% of GDP) billion in 2019/20 (revised estimates II) to **Kshs. 1,621.4 billion (14.4% of GDP)** in 2020/21. A number of revenue enhancement measures have been introduced which could potentially mitigate the anticipated revenue decline. The recent tax policy changes which introduced new taxes and removed many hitherto, as well as existing tax incentives in the tax system are discussed elsewhere in this paper.



Table 2: Revenue projections by the National Treasury

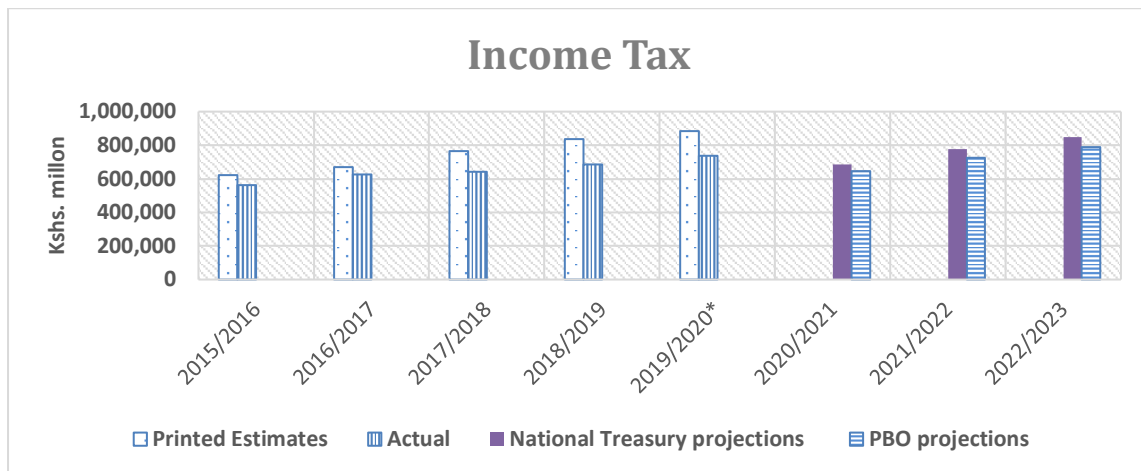
	Actual (Ksh million)					National Treasury projections (Kshs. Million)		
	2015/16	2016/17	2017/18	2018/19	2019/20*	2020/21	2021/22	2022/23
<b>Revenue and grants</b>	<b>1,284,388</b>	<b>1,463,610</b>	<b>1,548,903</b>	<b>1,690,772</b>	<b>1,927,400</b>	<b>1,906,700</b>	<b>2,185,200</b>	<b>2,414,800</b>
<b>Total Revenue</b>	<b>1,254,791</b>	<b>1,439,506</b>	<b>1,522,419</b>	<b>1,671,070</b>	<b>1,892,900</b>	<b>1,870,600</b>	<b>2,139,100</b>	<b>2,367,900</b>
<b>Ordinary Rev</b>	<b>1,152,544</b>	<b>1,306,504</b>	<b>1,365,063</b>	<b>1,496,930</b>	<b>1,643,400</b>	<b>1,621,500</b>	<b>1,871,700</b>	<b>2,077,900</b>
Tax revenue	1,069,825	1,219,501	1,259,113	1,400,566	1,443,500	1,514,800	1,759,000	1,953,600
Income tax	560,762	625,050	640,546	685,389	736,300	685,000	776,600	846,500
VAT	289,213	339,034	357,129	413,186	412,600	481,600	567,700	635,300
Import duty	79,638	89,943	93,685	107,702	93,400	106,800	137,400	159,000
Excise duty	140,212	165,474	167,753	194,289	201,200	241,400	277,300	312,800
Other	82,719	87,003	105,950	96,364	199,900	106,700	112,700	124,300
Appropriation-in-Aid	102,247	133,002	157,356	174,140	226,800	221,900	237,000	255,800
Rail levy					22,700	27,200	30,400	34,200
<b>Grants</b>	<b>29,597</b>	<b>24,104</b>	<b>26,484</b>	<b>19,702</b>	<b>34,500</b>	<b>36,100</b>	<b>46,100</b>	<b>46,900</b>
o/w project grants						33100		

\*supplementary budget II

**A decline in income tax collection is expected to be a major driver of the expected decline in tax revenues over the period 2020/2021.** Income loss by workers across most sectors due to the Covid-19 pandemic is expected to have a direct negative impact on income tax revenue in 2020/21 FY. The loss of income will disproportionately affect workers in the travel, hotel and tourism sectors which has ground to a halt due to the pandemic. Global international travel is expected to remain subdued in 2020/21. Further, virtualization may change conferencing/business travel in the future thus dimming prospects for workers in the travel and accommodation sectors.

Subdued exports of major cash crops are also expected to negatively impact the incomes of workers employed in the agricultural export supply chain. Further, as workers in other sectors are laid off due to depressed demand, some formal sector workers will be pushed into the harder to tax informal sectors. Given that income tax accounts for about 50% of tax revenues, the performance of income tax will be a key determinant of the revenue available to finance the 2020/21 budget. PBO projects that income tax revenue will decline from about 7.2% of GDP in 2019/20 to between 5.8% and 6% of GDP in 2020/2021 (See figure 6).

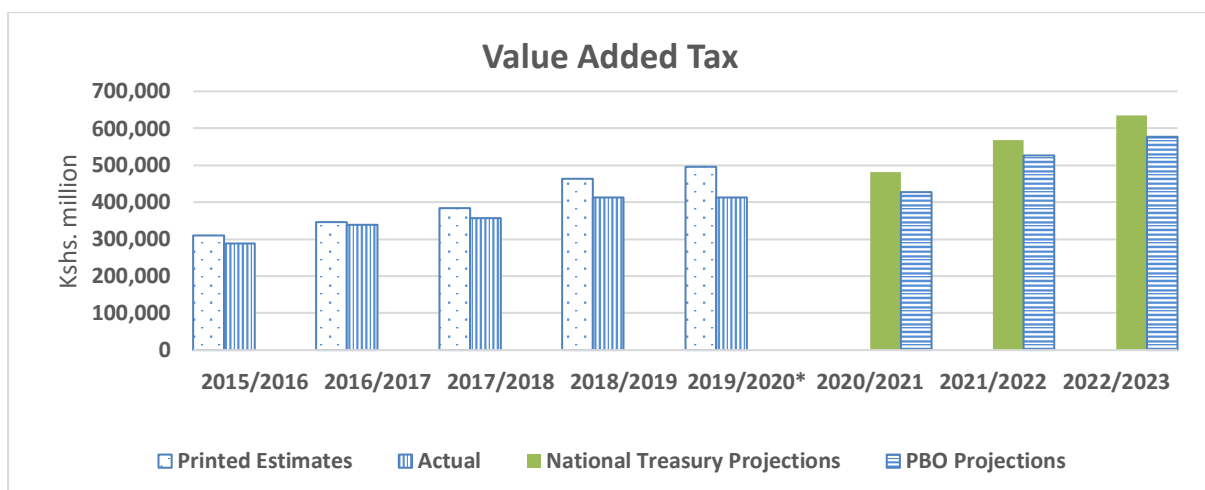
Figure 6: Income tax projections



\*Supplementary estimates II

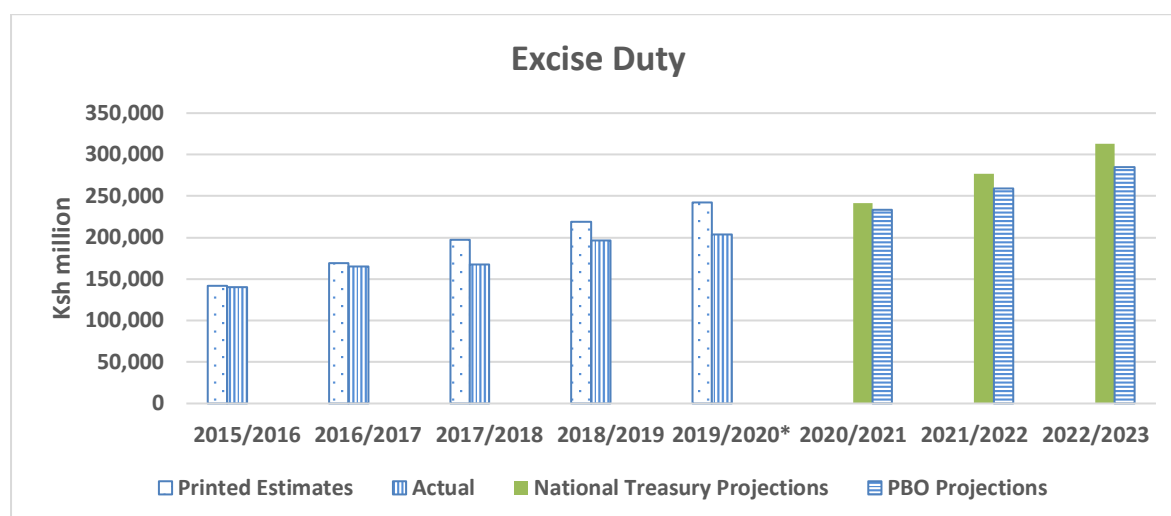
The (under)performance of revenue from VAT, which accounts for close to 30% of tax revenues is also a significant determinant of the expected revenue collection in 2020/21 FY. The partial or total loss in income by workers in the informal sector who make up about 80% of Kenya’s workforce is expected to significantly reduce consumption in 2020/21. In 2019, KNBS reported that 60% of workers in the informal sector were in the **Wholesale & retail trade sector and the hotels & restaurants sectors**. With the pandemic negatively affecting the aforementioned sectors directly, private consumption which accounts for over 70% of Kenya’s GDP is expected to remain below the pre-pandemic projections. Further, uncertainty about how long the pandemic will last is likely to change purchasing behaviour with many households holding off on purchasing non-essential items. Consequently, PBO projects that the VAT revenue as a share of GDP will decline from about 4% in 2019/20 to 3.8% in 2020/21. Figure 7 and Figure 8 presents PBO and National Treasury VAT and Excise Duty projections.

Figure 7: VAT revenue projections



\*Supplementary estimates II

Figure 8: Excise duty projections



\*Supplementary estimates II

**Fiscal expansion due to Covid-19 related expenditures coupled with dwindling tax revenues is expected to worsen the fiscal deficit in FY 2020/21.** The National Treasury projects that the fiscal deficit (excluding grants) as a share of GDP, will worsen from **-7.3%** in 2017/18 to **-7.6%** in 2020/2021. However, this should be regarded as a conservative projection. Due to the economic shocks of the pandemic, the fiscal deficit in the coming year is expected to range between **-7.9%** and **-9%**. The prevailing high fiscal deficit implies that Kenya will have limited room for a fiscal response to the impact of the Covid-19 pandemic on poor and vulnerable households, especially if its economic shocks persist for an extended period.

#### Keep an Eye On:

- i. **Income tax revenue:** The measures put in place to curb the spread of the Covid-19 virus will contribute to income/Job losses across most sectors. Consequently, Income tax is expected to be between 5 and 10 percent below the target set in the 2020/21 FY printed estimates.
- ii. **Value Added Tax and Excise Duty:** The Covid-19 pandemic is expected to have a negative impact on private consumption for the better part of this FY. Therefore, if the Covid-19 mitigation measures remain in place, revenue collection from VAT is expected to be between 7 and 12 percent below target. Similarly, excise duty revenue is expected to be between 2 and 6 percent below target.

#### 1.2.2. Tax policy during the COVID-19 pandemic and likely economic implication

Tax policy is one of the tools the government uses to grant incentives to the tax payers so as to reduce their tax liability with the aim of encouraging investment to spur economic growth. The other tool relates to the revenue enhancement measures through the introduction of new taxes or removing the existing tax expenditures.

In order to cushion individuals, corporations and other businesses against the COVID-19 pandemic, the government introduced various taxation measures, whose likely implication is to reduce targeted tax liability and also removing many tax incentives inherent in the taxation system in order to enhance revenue collection, among others. These are discussed hereunder:

i. **Introduction of revenue measures to raise additional revenue**

The recent policy shift has been leaning towards the introduction of new revenue measures aimed at raising additional revenue to finance the budget. These include the following:

**The introduction of minimum tax:** - a new tax under the Income Tax Act, known as minimum tax was introduced through the Finance Bill, 2020. The tax which comes into effect on 1<sup>st</sup> of January, 2021 shall be charged at the rate of 1% of the gross turnover. Ideally, the tax is seeking to enhance fairness and also facilitate the expansion of the tax base so as to improve on the revenue yield. Advertently, this tax seems to mainly target businesses in loss making positions by demanding a portion of their turnover. This tax will ensure that all businesses regardless of profit position, shall contribute to revenue yield either through the usual Corporate Income Tax in the event of being on a positive profit position or minimum tax if in a negative profit position. The tax is scheduled to be paid in quarterly instalments on the 20<sup>th</sup> day the Fourth, sixth, ninth and twelfth month of the year of income.

**The Digital Service Tax:** - this tax was introduced at the rate of 1.5% of the gross transaction value in the provision of services in the digital market place. The tax is targeted at non-resident persons who do not have a permanent establishment in Kenya. In the recent days, it is noted that an array of transactions and business activities have been shifting to the digital platforms. For instance, e-commerce has been on the rise<sup>8</sup> and it is estimated that about 30% of firms in the country are selling their products online. In 2014, the Communication Authority estimated that e-commerce market was about KSh. 4.3 billion. Fast forward to 2020 and beyond, it is anticipated that with the internet penetration of close to 90%, the outlook is likely to be much more promising. This calls for re-engineering of the taxation system to capture such activities, lest, substantive revenue is potentially forgone.

**Expansion of the excise duty tax base by the reducing the threshold of alcohol strength for spirits from 10% to 6% for taxation purposes:** - the reduction of threshold of alcohol strength for purposes of taxation implies that more spirituous drinks under this category which are taxed at KSh. 200 per litre shall now be captured in the tax net. However, increased taxation or imposition of taxes to commodities such as these is a delicate balancing where the need to raise additional revenue is weighed against the shifting of the market to contrabands and counterfeits<sup>9</sup> that may be encouraged by the price differentials, which is likely to affect the economy of the county as well as the health of the partakers.

ii. **Abolition of the existing tax incentives**

The latest tax policy changes led to the overhaul of so many tax incentives that have been inherent in the tax laws for quite a long time. Whereas some of them had outlived the purpose for which they were established, others had posed a huge risk of distortions to the taxation system without a concrete benefit

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<sup>8</sup> <https://ca.go.ke/industry/ecommerce-development/>; <https://ecommerceguide.com/news/kenyan-ecommerce-set-major-growth/>

<sup>9</sup> <https://movendi.ngo/news/2019/04/20/kenya-big-alcohol-against-alcohol-tax-increase/>

accruing to the economy. Originally, this was intended to provide incentives to encourage some activities to thrive so as to spur economic growth. However, it is believed that in 2018 alone, the government lost about KSh. 535 billion<sup>10</sup> through tax expenditures which was about 35.7% of the total ordinary revenue collected in 2018/19. This is a large amount, considering the fact that it was not far from the fiscal deficit recorded around the same period.

**Removal of allowable deductions:** - the income tax statute has previously contained several types of income that was allowed as deductions especially by businesses and corporations. This means that they are allowed to knock off some types of income from the taxable income before calculating the tax liability. Ideally, it was expected that this incentive would offer some form of relief to taxpayers in order for them to reduce their tax liability and subsequently pass the benefit to the economy. However, there appears to be no sufficient evidence that the objective was achieved. Therefore, to modernize the law and align it to the Constitution as well as the Public Finance Management Act with regard to the principles of public finance, the incentive was removed. The full list of the allowable deductions is attached in **annex 1**.

**Removal of exempt income incentive:** - there existed a wide range of income, under the income tax law that was exempt from taxation under the income tax and it was removed through the Tax Laws (Amendment) Act, 2020 and the Finance Act, 2020. Other than reducing the list of exempt income in order to raise additional revenue, this endeavour also modernized the tax law by extinguishing some antiquated incentives that date as back as 1970s and are no longer relevant. A list is attached in **annex 2**.

**Changes in the Value Added Tax (VAT) exemption and zero rated regimes:** - the VAT law was re-enacted in 2013 and this exercise witnessed the removal of a superfluity of items in the exemption and zero rate regimes. This significantly improved the revenue yield. However, the long list of items seems to have gradually made their way back through various Finance Acts and other legislative means. This may have potentially undermined revenue collection in addition to rendering the tax administration cumbersome. Therefore, the overhaul of these incentives at a time such as this was timely and this is likely to substantively enhance the revenue yield. The list is attached in **Annex 3**.

### iii. Overhaul of the investment deductions regime

The **investment deduction (ID)** regime was overhauled and replaced with a modern and progressive system which ensures that the deduction is done in a phased manner so as to ensure that at least businesses contribute to the tax yield even as they deduct some portion of investment capital from taxable pay. It is worth noting that the regime that existed prior to April, 2020 seemed to contain a myriad of deductions some of which may not have been well targeted. It is believed that this is one of the single-most source of revenue loss associated with poor performance of corporation income tax since investors are allowed to deduct their capital expenses from taxable income up to 100% (and in some cases reaching 150% in recent amendments to the income tax). It takes quite a very long time before all the investment expenditure is recouped for a firm to start paying taxes. The changes collapsed the investment deductions are in four categories, that is: construction of buildings, installation of machinery, installation of fibre optic cable and farm works. The deduction range from the highest of 50% and reduces progressively to 10%. Further details are presented in **annex 4**.

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<sup>10</sup> The National Treasury report to the National Assembly's Finance and National Planning Committee

#### iv. Introduction of tax incentives to cushion the vulnerable and/or spur economic growth

**Reduction of Turnover Tax (ToT) from 3% to 1% of gross turnover:** - the reduction of turnover tax was aimed at cushioning businesses especially the Micro, Small and Medium Enterprises (MSMEs) who are believed to bear the brunt of economic turmoil that has been occasioned by the COVID-19 pandemic. Linked to this also, is the change of thresholds turnover of below KSh. 5 million to a range of KSh. 1 million to KSh. 50 million and even incorporated businesses within this range are at liberty to choose whether to pay turnover tax or corporation income tax. Further, the change removed the then existing presumptive tax which had been introduced earlier on to facilitate enforcement of turnover tax.

**Reduction of the Pay-As-You-Earn (PAYE) top taxation band from 30% to 25% and exemption of income below KSh. 24,000:** - the PAYE taxation bands were reduced from 5 to 4 and reworked such that the lowest band was set at 25%. This, coupled with the enhancement of personal relief from KSh. 1,408 to KSh. 2,400 per month and exemption from PAYE persons earning below KSh. 24,000 per month were intended to provide relief to PAYE tax payers so to avail additional income to the economy which, ideally can only be spent, saved or invested, all of which are avenues of supporting economic growth even beyond the pandemic period. It seems that this is one of the incentives that are very effective in its intended purpose because, increased disposable income to households has the greatest benefit since it is one of the most important determinants of demand<sup>11</sup>. **PAYE bands in annex 5**

**Reduction of Corporate Income Tax (CIT) from 30% to 25%:** - the corporation tax was reduced to 25% and the understanding was that the businesses and companies will apply the savings arising from this tax incentive not only to cushion themselves against the effects of the pandemic but also cushion their employees by retaining them in the payroll. However, since the implementation of this incentive, together with the one on reduction of **VAT from 16% to 14%**, there are indications that companies are still struggling with cushioning their employees and prices of commodities which are subjected to VAT do not depict any significant difference before and after the introduction.

**Clarity in the taxation of pension payments by persons over the age of 65 years:** - the confusion that had been occasioned by the existence of two provisions with similar numbering was cleared. It is noted that there were two provisions both occupying paragraph 53 of Part I of the First Schedule (income exempt from tax). The first one was “the monthly pension granted to a person who is 65 years of age or more”, which was introduced to the Income Tax statute through the Finance Act of 2007. The other one was “income from employment paid in form of bonuses, overtime and retirement benefits” which was introduced through the Finance Act of 2016.

Therefore, to comprehensively address the matter by retaining the tax exemption of monthly pension paid to retirees who have attained 65 years but removing the exemption on bonuses and overtime (since the minimum taxable income had been shifted to KSh. 24,000 and above), both paragraphs were deleted and the correct one re-introduced which is “the monthly pension granted to a person who is 65 years of age or more”. Therefore, this implies that the monthly pension to persons aged 65 years or more is exempt from income tax.

#### v. Value added tax on transfer of business as a going concern

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<sup>11</sup> <https://www.thebalance.com/consumer-spending-definition-and-determinants-3305917>

Value Added Tax (VAT) on **transfer of businesses as a going concern (TOGC)** has undergone major policy changes in recent times; moving from zero rate, to exemption and finally to standard rate with effect from April, 2020. The implication is that this matter is now considered as a supply that is liable to VAT at standard rate. A review of other jurisdictions reveals that the transfer of businesses as a going concern is out of the scope of the VAT. However, there are always set conditions that must be fulfilled in order for such a transaction to be regarded as such. Some of the standard conditions<sup>12</sup> are such as the requirement that:

- i. The transfer should be whole of independent parts of the business which is capable of independent operations (the assets such as good will, machinery, premises etc must be part of the arrangement);
- ii. The transfer must be to a registered VAT taxpayer, meaning there is no anticipated disruptions regarding VAT treatment before and after the transfer;
- iii. The recipient must commit to continue with the same kind of business. Not identical but it should be clear that it is the business that is being bought and not the assets of the business;
- iv. What to do with the land must be clearly addressed (whether it is being sold with the business or not and if sold whether it is taxable or not);
- v. Safeguards must be instituted against immediate consecutive transfers of the business.

It is noted that Kenya does not have a group taxation and relief regime to consider transfer of businesses as a going concern. This implies that there are no conditions in place to ascertain the intention of transfer of business on whether it is indeed a transfer of business or it is merely a transfer of assets. These two ought to be treated differently. When the former is determined, then it falls out of the scope of the VAT if the set conditions such the ones highlighted above are met. Otherwise, if the latter is ascertained, then it becomes just the normal business that should be subjected to VAT taxation in the usual manner.

Therefore, whereas the definition of business, according to the Transfer of Businesses Act provides that it is a trade or occupation other than a profession carried out with a view to profit, it is imperative to evaluate the VAT issue on the transfer of businesses as a going concern to ensure that there is a clear demarcation between what constitutes a supply to be subjected to VAT and what can be considered a transfer of businesses as a going concern which is out of scope of VAT. This may be done by introducing group taxation and relief regime in Kenya which shall impose conditions to be fulfilled for the consideration of transfer of businesses as a going concern for purpose of VAT application. Otherwise, the current taxation regime treats transfer of businesses as a going concern as being the same as the normal business of supply. These two ought to be accorded different treatments.

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<sup>12</sup> Government of the United Kingdom Value Added Tax, VAT Notice 700/9  
(<https://www.gov.uk/guidance/transfer-a-business-as-a-going-concern-and-vat-notice-7009>)



## Keep an eye on:

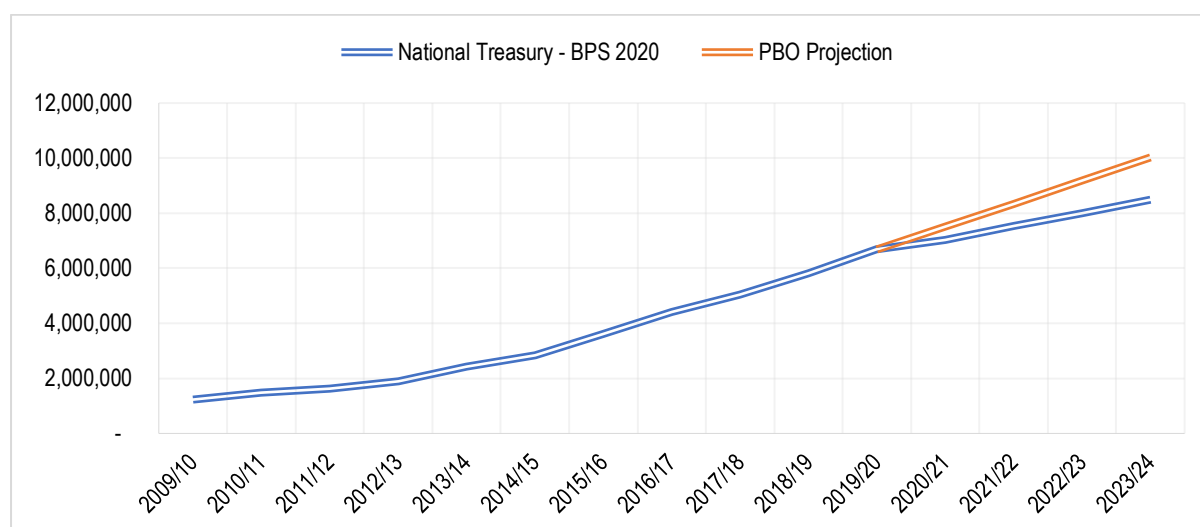
- i. The expected enhanced revenue yield that shall be occasioned by, **first**, the introduction of new tax measures such as the Minimum Tax (MT) and Digital Service Tax (DST). **Second** is the overhaul of the tax incentives regime such as the modernization of Investment Deductions (ID) regime. **Third**, the removal of several items from the allowable deductions and exempt income under the Income Tax. With robust tax administration in these areas, these measures would revolutionize and substantively increase the revenue collection.
- ii. The reduction of the corporation income tax (CIT) from 30% to 25% which is an incentive meant to reduce the tax liability and encourage companies to keep employees in the payroll especially this time of the global pandemic. The successful implementation of this incentive and its attendant promise would help alleviate the impact of the COVID-19 on the workers in these corporations.
- iii. The reduction of Turnover Tax (ToT) for eligible businesses from 3% to 1% of the annual turnover which is intended to grant reprieve, especially to the Micro, Small and Medium Enterprises (MSMEs) to cushion them against the effects of slackened economic activities, occasioned by COVID-19.
- iv. The reduction of the Value Added Tax (VAT) from 16% to 14% whose ultimate aim is to reduce the prices of commodities so as to provide relief to the consumers at such a time when household income levels are expected to dwindle. The efficacy of this incentive may be evaluated since there seem to initial indications that prices of most commodities have not adjusted in response to the reduction in the tax rate.
- v. The removal of several items from the Value Added Tax zero rate and exemption regime so as to address distortions inherent in the tax system, promote fairness and enhance revenue yield to finance the provision of public goods and services for all. This status need to be maintained to guarantee enhanced revenue and simplified tax administration.



### 1.3. Debt Management for FY 2020/2021 and the Medium Term

Kenya's public and publicly guarantee debt stock is projected to increase over the medium term owing to the impact of low generation of domestic revenue and pressure from expenditure on on-going programs. As at June 2020, the national debt stock had reached Kshs. 6.6 trillion (Kshs. 873 billion or 15% increase) and is projected to reach Kshs. 7.5 trillion by June 2021<sup>13</sup>. In previous financial years, the primary balance grew on account of significant expenditure on infrastructural projects, energy production as well as social expenditures. The impact of COVID-19 on the economy is expected to adversely affect revenue generation. Given the current and projected expenditure demands, it is estimated that the Kenyan debt stock could reach Kshs. 9.2 trillion in FY 2022/23.

Figure 9: National Debt Stock, FY 2009-10 to FY 2023-24 (KHz. Millions)



Source: National Treasury & PBO Projections

**Fiscal space is projected to decline therefore limiting the flexibility of fiscal planning in the medium term.** Debt servicing expenditures are estimated to utilize up to 49% of ordinary revenues in FY 2020/21. This implies that at best, only approximately 51% of nationally raised revenues will be available for FY 2020/2021 budget implementation. Moreover, given that the current public finance management framework has capped the national debt stock at Kshs. 9 trillion, at the current borrowing rate<sup>14</sup>, it is anticipated that there will be little borrowing space beyond three years. Implementation of the FY 2020/21 budget should therefore be critical of the following; a) implementing the budget taking into consideration financial and information<sup>15</sup> requirements required for a successful medium term fiscal policy implementation, b) utilizing debt & revenue resources for initiatives that maximise positive impact on private and public investment & c) careful management of other non-debt related expenditures that cause rigidities within the fiscal framework i.e. pensions or funds that are charged directly to the national government revenue.

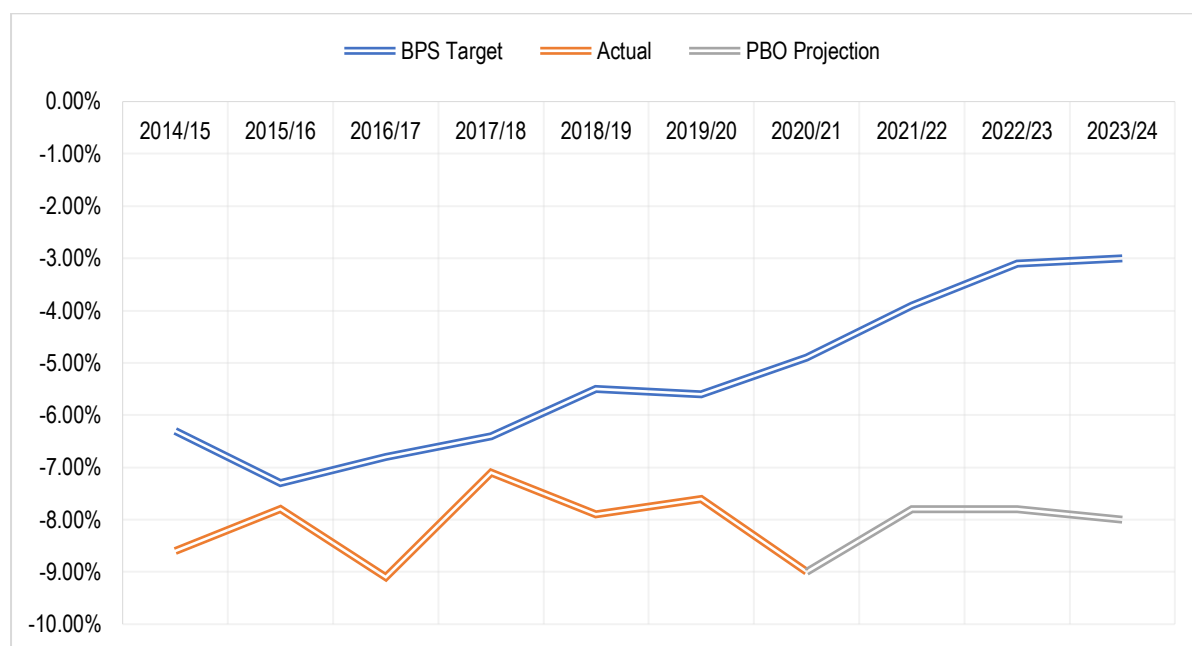
<sup>13</sup> According to the National Treasury the fiscal deficit for FY 2020/21 is estimated at Kshs. 840.6 billion

<sup>14</sup> Based on a zero fiscal consolidation scenario and 3-year fiscal deficit average (FY 2017/19, FY 2018/19 and FY 2019/20) which indicated that approximately Kshs. 767 billion is required annually to finance the budget.

<sup>15</sup> Information availability will be required to address COVID – 19 related economic uncertainty

**FY 2020/2021 will present difficult economic conditions for fiscal consolidation measures required to maintain debt at sustainable levels.** Reduced economic activity, subdued current account balance and slowdown in revenue generation is likely to adversely affect fiscal consolidation efforts. Furthermore, the magnitude of the economic stimulus to be undertaken in order to bring the economy is likely to require significant financing beyond what has already been provided for in the budget. Under these circumstances, it is difficult to implement fiscal consolidation measures. As a result, a widening of the fiscal deficit is anticipated. It should be noted that for the past 3 fiscal years, deficit financing has averaged (7.5) % of GDP. Under the prevailing circumstances, it is projected that the fiscal deficit for FY 2020/21 will range between 8% and 9%.

**Figure 10: Fiscal Deficit as a percentage of GDP**



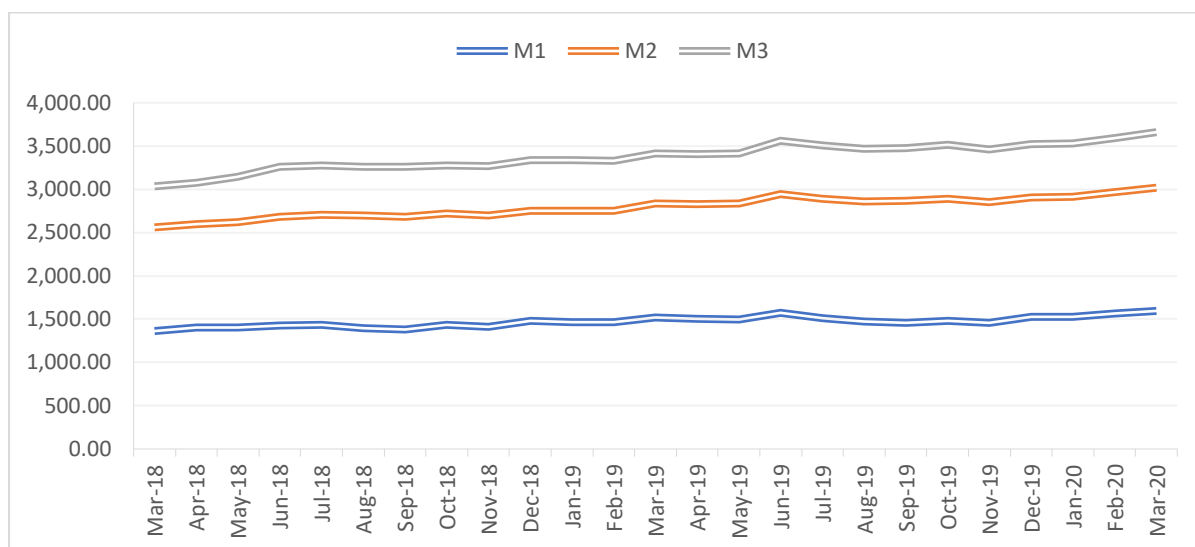
Source: Budget Policy Statement & PBO Projections

**Risks to the debt stock remain on the downside in FY 2020/21 and the medium term.** The rising external debt portfolio poses a high risk of debt distress in the absence of mitigating factors under the COVID-19 pandemic. Since the onset of COVID-19, external debt risk has persisted owing to domestic economic pressure, shocks on Kenya’s exports, non-conducive international financial market conditions for refinancing and the country’s reduced access to concessional financing. Prevailing depreciation of the Kenya shilling exchange rate presents a new but potent risk to external debt service and requires closer monitoring.

**Under domestic borrowing, despite the borrowing outlook indicating lower interest rates, interest rate risk and refinancing risk is high.** The MTDS 2020 indicated that i) domestic debt had a much lower Average Term to Maturity (5.7 years) compared to External debt (11.1 years), with a higher rate of debt maturing in one year (34.9% of debt maturing in one year as opposed to 3.9% for external debt) and ii) the domestic debt portfolio Weighted Average Interest Rate (at 11.4%) was much higher as compared to that of the external debt portfolio (4.2%). However the borrowing outlook is favourable due to low interest rates on account of the accommodative monetary policy being undertaken by the Central Bank<sup>16</sup>. Consistent reduction in the Central Bank Rate from 10% to 9.5% in March 2018 and further downwards to 7% by July 2020 has led to an overall increase in money supply.

<sup>16</sup> Central Bank Monetary Policy Press Release, July 2020

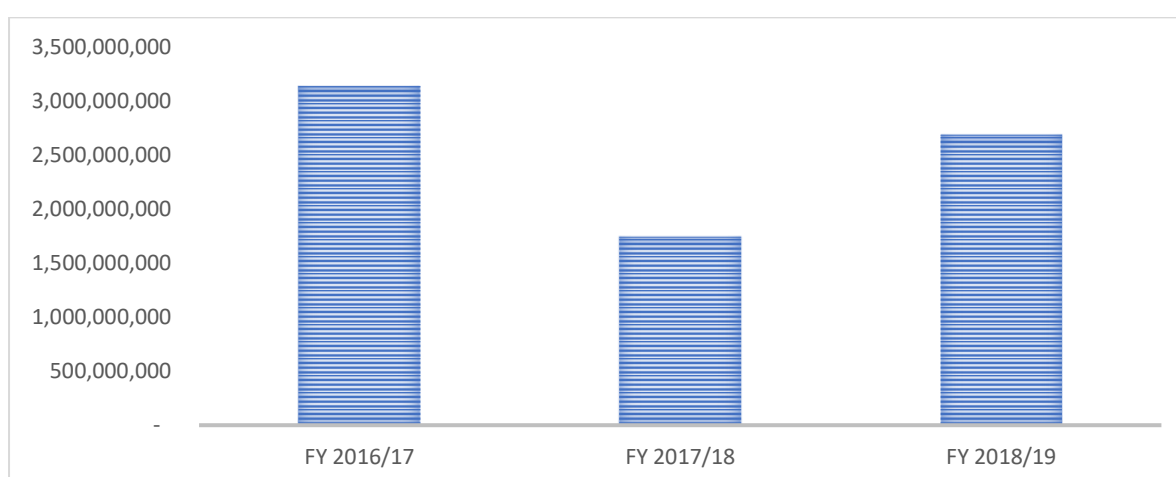
Figure 11: Money Supply, March 2018 – March 2020 (KHz. Billions)



Source: Central Bank Monthly Economic Indicators

Despite the planning of government financing for each financial year, the country continues to incur commitment fees arising from non-disbursement of external debt. Since FY 2015/16, a total of Kshs.7.6 billion has been incurred as commitment fees. This is an extra burden arising from debt disbursement inefficiencies due to late issuance of letters of credit and lack of allocation of the required counterpart funding. At the end of the third quarter of FY 2019/2020, only Kshs. 98.4 billion (42%) of the Kshs. 232.78 billion net foreign financing, had been disbursed. To increase efficiency of project implementation and reduce incurring commitment fees, a higher rate of disbursement will have to be achieved in FY 2020/21.

Figure 12: Incurred External Debt Commitment Fees



Source: Annual Public Debt Management Reports

Table 3: FY 2020/2021 Deficit Financing Framework (KHz. Billions)

<i>Financing source</i>	<b>BPS 2020</b>	<b>FY 2020/21 Approved Budget Estimates</b>	<b>Deviation</b>	<b>% Deviation</b>
<i>Commercial Financing</i>	3	6.2	3.2	107%
<i>Semi-Concessional Financing</i>	124.1	124.1	0	0%
<i>Project Loans</i>	242.9	250.5	7.6	3%
<i>Program &amp; Other Concessional Loans</i>	152	152	0	0%
<i>Debt Repayment</i>	174.1	179.6	5.5	3%
<i>Net Domestic Financing</i>	222.9	493.7	270.8	121%

Source: National Treasury FY 2020/21 Mwananchi Guide & BPS 2020

**Continuous creation of fiscal space should be a target.** Whilst the COVID-19 pandemic has created a need to increase expenditures, there is still room for continuous cost saving. For instance, some sectors such as the Education sector may spend less than what was allocated due to nationwide school closures for at least half of the financial year. Furthermore, work from home directives have reduced government travel therefore savings can be made from items such as foreign and domestic travel expenditure. Non-priority recurrent expenses can be deferred to the next financial year. As such, there is room for deficit reduction in the course of the fiscal year.

**Domestic debt servicing is a significant source of liquidity pressures in FY 2020/21 and the medium term.** In the current financial year, Public debt service expenses are projected to increase by Kshs. 157.1 billion (or 20%) to reach Kshs. 925.9 billion in FY 2020/21; of which Interest rate payments will account for 52% with domestic debt interest payments constituting up to 66%. Domestic debt redemptions will account for 59% of total Debt redemptions which have increased by 32% and currently account for 48% of total debt service. A Summary of debt servicing payments is as follows:

- a) Domestic debt interest payments will be composed primarily of Treasury bonds while external debt interest costs will largely involve payables to commercial debt creditors worth Kshs. 72.5 billion; interest payments to China (Exim Bank of China & China Development Bank) worth Kshs. 33.1 billion; and interest payments for projected new loans that will amount to Kshs. 29.4 billion.
- b) Domestic debt redemptions amount to Kshs. 179.6 billion, including an additional allocation of Kshs. 100 billion towards meeting any shortfall arising from treasury bill redemptions. External debt, large payments will be payable for maturing China related debt worth Kshs. 62.03 billion and a 7-year Trade Development Bank Syndicated Loan that was used to offset accruing Eurobond payments. A review of the CFS indicates the debt repayment policies are not cost-effective i.e. continuous use of expensive commercial loans, which worsen the refinancing challenges, are settled using syndicated loans which worsen both interest rate and the refinancing risks.

Table 4: Public Debt Servicing Expenses (KHz. Millions)

	FY 2019/20	FY 2020/21	FY 2021/22	FY 2022/23	FY 2023/24
Interest - Internal Debt	301,812	321,911	370,430	382,588	385,662
Interest - External Debt	131,868	162,434	166,821	173,950	183,692
Interest Payments, Sub-Total	433,680	484,345	537,251	556,538	569,354
Redemption - Internal Debt	213,691	261,955	246,810	336,623	357,165
Redemption - External Debt	121,477	179,640	239,393	257,612	258,457
Redemptions Payments, Sub-Total	335,168	441,595	486,203	594,235	615,622
<b>Public Debt Service Expenses</b>	<b>768,848</b>	<b>925,940</b>	<b>1,023,454</b>	<b>1,150,773</b>	<b>1,184,976</b>

Source: Respective Annual Approved Budget Estimates

**Contingent liabilities from debt guarantees are an additional risk to the debt management framework.** Contingent liabilities are obligations that arise when a particular event occurs and create in year fiscal risks<sup>17</sup> as they are not included in the budget estimates. Section 58 of the PFM Act requires the government to meet financial obligations of institutions that fail to meet their debt servicing expenses, that is, called up guarantees. Under the prevailing economic conditions that have reduced revenue generation, guaranteed institutions are likely to fail to meet their debt servicing obligations. Should this materialize, then the National government will be obliged to meet their expenses even though there is no provision for called guarantee in the FY 2020/2021 budget., this position might not hold given the depressed economic conditions that are likely to reduce incomes for guaranteed institutions. Furthermore, there are plans to introduce Credit Guarantee Scheme for SMEs which will also increase the overall public and publicly guaranteed debt stock.

**Keep an eye on:**

- i. Financial risk emanating from contingent liabilities. These specifically relate to called up guarantee arising from already guaranteed debt which if the national government is obliged to pay, will increase expenditure requirements mid-year. Furthermore, the anticipated Credit Guarantee Scheme will require enhancement in the oversight framework.
- ii. Disbursement rate of external debt in order to limit the overall cost of acquiring external debt that is occasioned by commitment fees incurred each financial year
- iii. Absorption rate of debt financed projects in order to increase efficiency of borrowed resources through increased oversight involving increased reporting on factors such as project status, cash disbursement etc.
- iv. Risks to debt sustainability, these will relate to exchange rate risk, refinancing risk, and interest rate risks rations of which occasion an increase of debt servicing expenses at a moment of tight fiscal space.

## 1.4. Monetary Policy

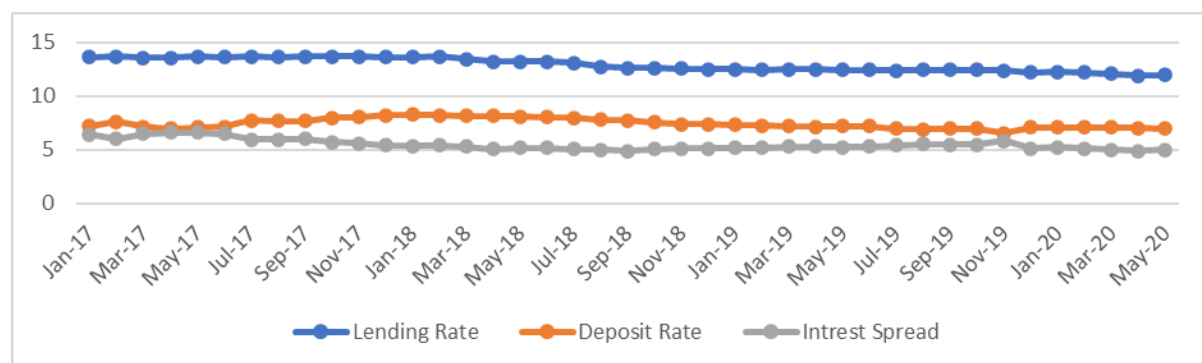
**To alleviate adverse economic effects of the lockdown, the Central Bank of Kenya (CBK) has initiated various measures to ensure that there is ample liquidity in the economy.** The CBK has lowered its policy rate by 125 basis points to currently stand at 7 percent. The lowering of the Central Bank Rate (CBR) signals commercial banks to lower their lending rate so as to make loans more affordable. The bank further lowered the Cash Reserve Ratio (CRR) by 100 basis point to 4.25 percent

<sup>17</sup> Government Finance Statistics Manual 2014

and increased the maximum tenor of repurchase agreements from 28 days to 91 days. This is meant to provide additional liquidity to commercial banks, thereby enabling them to extend new lending or restructure loans to affected borrowers. At the end of the first half of the year, commercial banks had restructured Kshs. 844.4 billion<sup>18</sup> worth of loans from the total banking sector loan book of Kshs. 2.9 trillion thereby providing some relief to borrowers.

**The lowering of the CBK policy rate reduced the interest spread to 4.99 percent by end of May 2020 compared to 5.13 percent at the end of December 2019 as shown in the figure below.** As the interest spread continues to narrow, there is a possibility of a decrease in profit margins in commercial banks due to low cost credit. This may deter commercial banks from lending to risky borrowers.

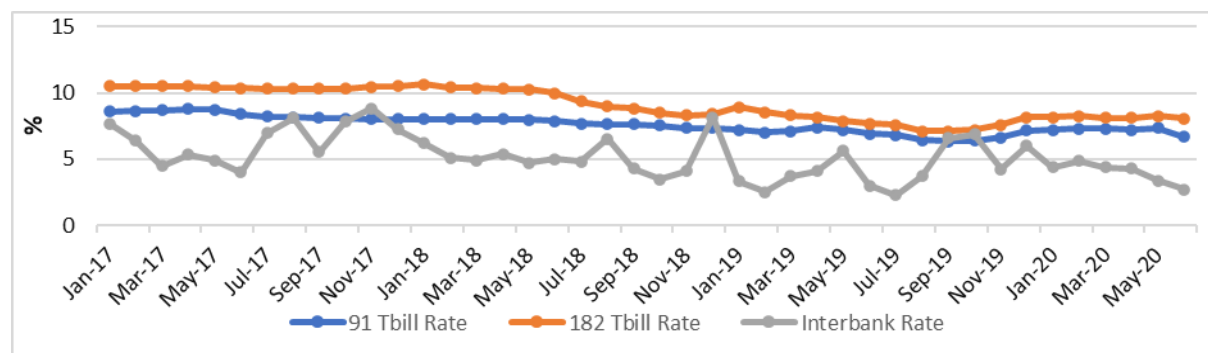
Figure 13: Commercial Weighted Interest Rates (Lending rate vs. Deposit rate) January 2017 to May 2020



Source: CBK, 2020

**The average yield rate for short-term government securities is declining, suggesting ample liquidity in the financial markets and expectations about future economic conditions.** The 91-day Treasury bill rate declined from 7.1 percent in December, 2019 to 6.7 percent in June, 2020. Similarly, the 182-day Treasury bill rate declined from 8.16 percent to 8.06 percent over the same period. The fall in the yields in government securities suggests ample availability of funds implying that commercial banks are exercising caution with respect to lending to the private sector and are instead lending to government. The decline of the interbank rate from 6.03 percent in December, 2019 to 2.7 percent<sup>[1]</sup> as at the end of June, 2020 suggests excess liquidity. This excess liquidity may be a result of government payments such as VAT refunds as well as reduction in lending due to weakening economy.

Figure 14: The Interbank Rate, 91 T-Bill and 182 T-Bill yields, January 2017 to June 2020

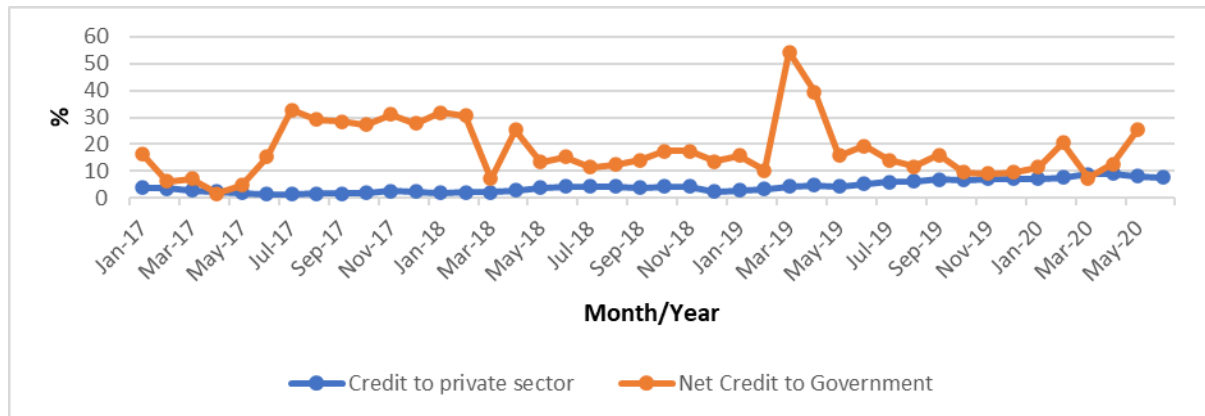


Source, CBK, 2020

18 Monetary Policy Committee Meeting, press release, 29th July 2020

**Private sector credit continues to experience sluggish growth and was estimated at 7.6 percent in the 12 months to June 2020.** Between January 2017 to November 2019, the uptake of loans by the private sector grew at an average growth rate of 4 percent. The low uptake of loans during this period was occasioned by the interest capping law which had capped interest charged by commercial banks at 4 percent above the CBR; as well as an increase in non- performing loans. This discouraged banks from lending to riskier borrowers and encouraged lending to government. Following the repeal of the interest cap law in November 2019, there has been a gradual uptake of credit as shown in the figure. As of the end of June, 2020, credit to private sector stood at 7.6 percent.

Figure 15: Annual Growth rate of credit to the private sector vs. Government, Jan 2017 to May 2020

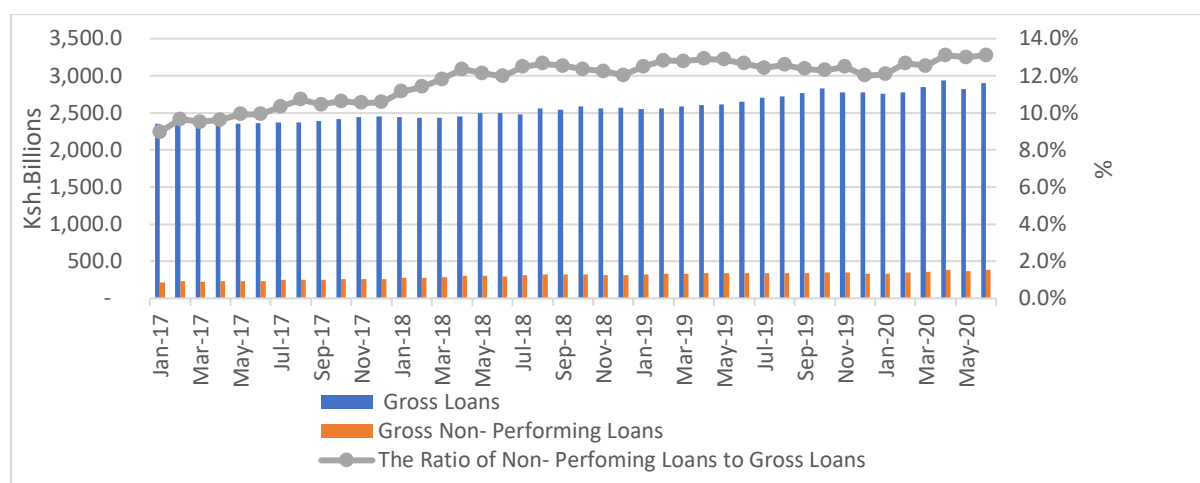


Source: CBK, 2020

**During the pandemic, private sector credit growth is expected to be muted.** Commercial banks have provided some relief to the private sector through loan restructuring so as to prevent defaults during the pandemic period. Despite this however, there has been an increase in non- performing loans and the ratio of non- performing loans (NPLs) to gross loans remains elevated at 13.1 percent compared to 12.1 percent at the beginning of the year. This can be attributed to deteriorating business conditions which have led to business underperformance resulting to declining wages and layoffs. Nevertheless, following the easing of the COVID-19 containment restrictions, there has been some improvement in private sector activity as denoted by the Stanbic Purchasing Managers Index which increased from 36.7 percent in May to 46.6 percent in June 2020. This has been attributed to increased export demand occasioned by the gradual opening of economies in Europe.



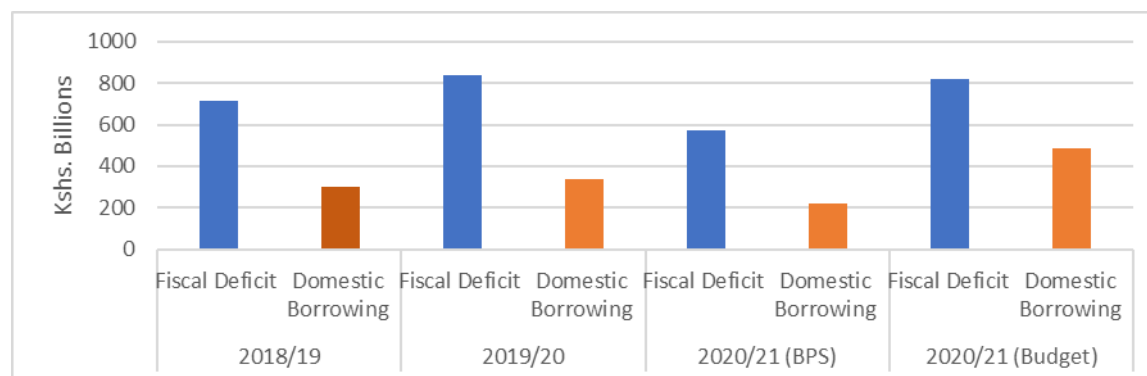
Figure 16: Gross Loans vs. Non-performing Loans



Source: CBK, 2020

**High appetite for borrowing by the government may further worsen the prospects of private sector recovery growth.** In the Financial Year 2020/21, the government plans to borrow Kshs. 486.2 billion<sup>19</sup> in the domestic market. Commercial banks will continue to lend to the government due to the lower risk. As earlier indicated, the measures instituted by the CBK to increase credit access have made it affordable for the government to access funds to finance its budget deficit which currently stands above Kshs. 820 billion.

Figure 17: Fiscal Deficit vs. Domestic Borrowing



Source: The National Treasury

**Keep an eye on:**

- i. **Increase of government borrowing in the domestic market:** As a result of the pandemic, most commercial banks are practicing a wait and see approach due to the rising credit risk caused by weakening economy. This has deterred commercial banks from lending to the private sector. The government should therefore not increase its borrowing as this may adversely affect private sector credit.

<sup>19</sup> Budget Summary for Financial Year 2020/21



- ii. **Growth of non- performing loans:** The ratio of non- performing loans (NPLs) to gross loans remains elevated. An increase in non-performing loans may discourage commercial banks to lend to the private sector.

## Chapter Two:

# Enhancing efficiency and effectiveness through budget implementation

*The choices we make today will directly affect the way the crisis unfolds and so the lives of billions of people. With the right measures, we can limit its impact and the scars it leaves. We must aim to build back better so that our new systems are safer, fairer and more sustainable than those that allowed the crisis to happen.*

*Guy Ryder, ILO's Director General*

## 2.0. Introduction

The total MDAs budget including the Judiciary and Parliament amounts to KSh 1,886.4 billion comprising of KSh. 1,253.1 billion for recurrent activities and KSh. 633 billion for development activities. Notably about 39 percent of the total development expenditure will be donor financed.

Table 5: Summary of Budgetary Allocation in KHz. Billions

	Recurrent	Development	Total
1. National Executive	869.8	627.3	1,497.1
o/w AIA	184.9	245.4	430.3
2. Commissions and Independent Offices	383.3	6.0	389.3
o/w AIA	1.2	-	1.2
<b>Total</b>	<b>1,253.1</b>	<b>633.3</b>	<b>1,886.4</b>

Source: Appropriations Act, 2020

The resources will be geared towards implementation of 158 programmes with specific Key Performance Indicators and targets spread across the three arms of government and other independent commissions and offices. Included in the budget, is an allocation of KSh. **53.7 billion** for various interventions under a stimulus package including youth empowerment and employment creation, improving education outcomes, health, road rehabilitation among others. The table below shows an analysis of outputs, key Performance Indicators (KPIs) and targets specific to the stimulus package.

Table 6: Analysis of Outputs and Key Performance Indicators

S/No.	Thematic Area	KSh. Millions	Output	KPI	Target
1.	Youth Empowerment	10,000	Youth and other Stakeholder Involvement	Number of Youth Involvement in post covid-19 economic revamping programmes	100,000
2.	Education	6,500	<ul style="list-style-type: none"> <li>Intern teachers to support transition 100%</li> <li>Classrooms constructed in secondary schools</li> <li>Locally fabricated desk</li> </ul>	<ul style="list-style-type: none"> <li>No. of Intern teachers recruited</li> <li>Number of classes constructed in public schools</li> <li>No of locally fabricated desks</li> </ul>	10,000 1,238 250,000
3.	Health	1,725	Increased access to health services	<ul style="list-style-type: none"> <li>No. of locally sourced beds and beddings to public hospitals</li> <li>No of diploma health interns</li> </ul>	20,000 5,000
4.	Environment and Water	3,822	Dykes constructed	<ul style="list-style-type: none"> <li>No of km of flood dykes constructed</li> <li>No of check dams constructed</li> </ul>	29 1
5.	Roads	5,410	Roads rehabilitated	No. of KMS of roads rehabilitated.	280
6.	Agriculture and Food Security	4,970	Improved farmers access to farm inputs	No of farmers using digital e-subsidy platform	304,158
7.	Tourism	6,000	Tourism facilities financed	No. of facilities financed	50

S/No.	Thematic Area	KSh. Millions	Output	KPI	Target
8.	Enhancing Liquidity to Businesses	14,312	Payments of outstanding bills	Amount of pending bills less than 3 million paid to local businesses	5 billion
9.	Social Protection	1,000	Households with vulnerable persons supported	No. of Households supported	833,000
	<b>Total</b>	<b>53,739</b>			

Source: The National Treasury

**The success of these interventions will depend on how the overall budget is implemented.** Beyond budgetary allocation, budget execution is critical to public service delivery to ensure that all outputs/targets are achieved as planned. As such public expenditure management and efficiency becomes necessary to reduce wastage.

## 2.1. Social Sector

### Access to Education amidst the COVID-19 pandemic

**The Education sector has been adversely affected by the COVID 19 pandemic with the government instituting nationwide school closures and deferring the entire 2020 academic year.** This is an unprecedented situation that has led to joblessness for a segment of the population that depends on the sector as a source of livelihood. The situation is worse for the private sector as some private learning institutions are reported to have closed permanently. However the savings to government are minimal as bulk of government spending in this sector is for personnel emoluments which continue to be paid despite closure of schools.

**The resumption of studies in January 2021 is dependent on the preparedness of the learning institutions to respond adequately to the threat posed by the pandemic.** This entails putting in place measures that will facilitate observation of social distancing guidelines as well as high standards of hygiene. Schools will be required to expand infrastructure including water, sanitation and hygiene (WASH) facilities as well as increasing learning amenities such as desks. To this extent, the sector has been allocated resources for infrastructural and allied interventions in the 2020/2021 budget which require urgent implementation. The period (July-December) when learners are out of school gives an opportunity for the sector to address infrastructural and WASH gaps aimed at containing the spread of the virus once studies resume. The implementation of the development budget for the sector in the first half (July- December) of the financial year 2020/21 will be a make or break situation. Prioritization of release of development funds for the sector is therefore highly critical.

**The Education budget also presents some opportunities for savings.** For instance, Capitation funds which are allocated per learner (at basic, tertiary and university level) to support operations and maintenance in learning institutions, account for 25% (Kshs 124.4 Billion) of the entire Education sector budget. The operations and maintenance includes aspects such as settlement of utility bills, infrastructure rehabilitation, and payment of salaries for teaching (in the case of universities) and non-teaching staff. However, given that the major users of various cost utilities are not in session for the first half of the financial year especially in basic learning institutions (primary and secondary), there is an opportunity to save some capitation resources.

Similarly, Kshs 400 million has been allocated to the examination waiver programme where the national examination (KCPE and KCSE) fees are catered for by the government. Given that national examinations will not be undertaken in 2020, this allocation may not be utilized.

The realized savings in these two areas may be a quick win for the sector and these resources may instead be applied to COVID-19 related interventions such as improving WASH facilities and providing additional desks in readiness for resumption of learning in 2021.

**Whereas some schools have been able to leverage on information communication and technology (ICT) to deliver learning services, many others have not been able to due to lack of access to requisite facilities.** Thus at the end of the year, there is likely to be a significant gap in learning between those who had access to online learning materials and those who did not.

**The 2020/21 approved budget for the sector is Kshs 505 Billion;** of which more than 50% of the allocation will cater for salaries to teachers in public primary and secondary schools under the Teachers Service Commission. The sector is implementing sixteen (16) programmes; each having set targets and outputs. Kshs 229.8 billion has been allocated to the traditional areas in the sector entailing support interventions that are aimed at improving the education outcomes. Some of these traditional interventions/priority areas are:

Table 7: Priority areas funded in 2020/2021

Sub-Sector	Allocation (Billions)	Key areas of priority/interventions funded
Basic Education	92.9	<ul style="list-style-type: none"> <li>▪ Capitation to learners (primary and secondary)</li> <li>▪ School infrastructure (Primary and secondary)</li> <li>▪ Examination waiver (Primary and secondary)</li> <li>▪ Digital Literacy programme (DLP)</li> <li>▪ Recruitment of 5,000 secondary school teachers</li> <li>▪ Recruitment of 10,000 intern teachers</li> </ul>
Technical Education	24.6	<ul style="list-style-type: none"> <li>▪ Capitation for TVET learners</li> <li>▪ TVET infrastructure support</li> <li>▪ Support to VTC's</li> </ul>
Higher Education	112.3	<ul style="list-style-type: none"> <li>▪ Capitation to University Students</li> <li>▪ HELB loans to students</li> <li>▪ Support to university infrastructure</li> </ul>
Total	229.8	

Source: National Treasury

**The education sector has also been allocated Kshs 4.3 Billion under the COVID 19 economic stimulus programme** to support the economic recovery plan and enhance sector preparedness in responding to the health pandemic. The stimulus programme is targeted at the following areas in the basic education subsector:

Table 8: COVID-19 economic stimulus programme for the sector

Area	Allocation (Kshs millions)
School infrastructure	560
Provision of 475,000 desks in public schools	1,940
Infrastructure in low cost boarding schools in ASAL areas	300
Recruitment of 10,000 contract (intern) teachers	1,200
Recruitment of 1,000 ICT interns to support Digital Literacy Programme (DLP)	300
Total	4,300

Source: National Treasury

**The focus of the stimulus programme is mainly school infrastructure which has been allocated Kshs 560 million.** This is in addition to infrastructural support to public primary and secondary schools totalling KHz 1.7 Billion. Thus, in 2020/21 the budgetary allocation for infrastructure support to basic learning institutions (primary and secondary) is Kshs 2.3 Billion. Additionally, Kshs 700 Million has been allocated to support infrastructural needs in low cost boarding schools in ASAL areas. It is critical to monitor the application of these funds particularly with regard to which schools will be supported (either rehabilitation of existing facilities or construction of new facilities).

**The basic education subsector has also been allocated Kshs 1.9 Billion in 2020/21 under the economic stimulus programme** for the purchase of 475,000 locally fabricated desks for public primary and secondary schools. The objective of this project is to implement social distancing among learners as well as create employment in the informal sector. Thus, it is important to know the schools which will receive the desks as well as the number of desks which will be procured.

**The construction of computer laboratories is another critical infrastructure related project in public primary schools.** This project began in financial year 2019/2020. In the current financial year, the project has been allocated Kshs 800 Million and the target is to construct 8000 computer laboratories in public primary schools with the aim of integrating ICT in learning in line with vision 2030. This project is critical because it is linked to the recruitment of ICT interns under the economic stimulus programme; an intervention that has been allocated Kshs 300 Million.

**In the tertiary and higher education subsectors, there are a number of ongoing infrastructural projects which are flagship projects within the sub sectors and have the capacity to support the preparedness of learning institutions to navigate the COVID 19 pandemic.** These include construction of tuition blocks, libraries and laboratories which are at various levels of completion.

Several capital projects in the tertiary and higher education sub-sectors are targeted for completion in 2020/21 and it is imperative to ensure that they are actually completed. These are indicated in table 9 below:

Table 9: Capital projects targeted for completion in 2020/2021

Sub-Sector	Project	2020/21 Allocation (Kshs. Mlns)	2020/21 Target set
Tertiary	GOK/ADB phase II equipping of Technical Training Institutes (TTI's)	1,836	100% completion
	GOK/China 130 equipping of TTI's	1,230	Equipping of the last 30 TTI's
Higher Education	Muranga University- Construction of science complex	32	100% completion
	Rongo University- Construction of tuition block	22	
	Kirinyaga University- Construction of multipurpose lecture theatre	18	
	Dedan Kimathi University- Construction of academic block and resource centre	57	

Source: National Treasury

**The equipping of Technical Training Institutes (TTI's) under a partnership between the national government and the African Development Bank as well as China is a flagship project in the tertiary sub-sector.** This project is aimed at operationalizing the TTI's through supply of various learning equipment in order to expand access to technical education and ensure the subsector contributes to job creation in the economy.

**In view of the foregoing, the following are the key areas to keep an eye on:**

- i.) The implementation of the education economic stimulus programme budget in the following areas: number of schools which will receive the 475,000 desks; and number and spread of low cost boarding schools in ASAL areas which will receive infrastructural support;
- ii.) The completion of the equipping of TTI's under the GOK/ADB and the GOK/China where the target for 2020/21 is 100% completion of equipping and equipping the remaining 30 TTI's in 2020/21 respectively.
- iii.) The application and distribution of the infrastructure funds for both public primary and secondary schools.
- iv.) The number of primary schools with computer laboratories under the Digital Literacy Programme where the target is construction of 8,000 computer laboratories in public primary schools.
- v.) The completion of the capital projects targeted to be completed in 2020/21 in various public universities

### **Achieving Universal Health Care amidst the COVID-19 pandemic**

**The health sector is arguably the most critical sector in the response to the COVID-19 health pandemic due to its critical role in containing the spread of the pandemic.** The implementation of Universal Health Coverage (UHC) is also a key programme under the sector budget and is one of the big four agenda aimed at expanding access to quality healthcare for all.

**The approved health sector budget for financial year 2020/2021 is Kshs 111.7 Billion.** This constitutes five programmes which will be implemented by the Ministry of Health and its various semi-autonomous agencies (SAGA's). The key strategic interventions and the targets set are indicated below.

**Table 10: Key strategic interventions in the Ministry of Health Budget**

<b>Key interventions</b>	<b>2020/21 allocation (Kshs Billions)</b>	<b>2020/21 Target</b>
Free maternity programme (Linda mama programme)	4.1	72% of deliveries conducted by skilled health workers
Provision of Health cover to the elderly and the vulnerable	1.9	195,000 vulnerable households covered
Scale up of UHC project	12.6	47 counties covered
Provision of Vaccines and immunizations	1.4	90% of children immunized
Construction of Regional cancer centres	1.3	One cancer centre completed
Provision of beds and beddings to public hospitals	0.5	20,000 beds and beddings
Provision of walk through sanitizers in public hospitals and at border points	0.025	50 walk through sanitizers

**Source: National Treasury**

The interventions highlighted above are critical since they are aimed at addressing pertinent concerns within the sector, such as reducing children mortality, reducing the high out of pocket health related expenditures among households as well as addressing the global health crisis.

**There are key areas to monitor during the implementation of the health sector 2020/21 budget:**

The first relates to the purchase of 20,000 locally sourced hospital beds which will expand hospitals bed capacity as well as expand treatment access for COVID 19 patients requiring critical care. Given that these beds are to be sourced locally, there is need to ensure that they meet the required medical standards. This is a responsibility of the Ministry of Health. Furthermore, the number of hospitals which will receive these hospital beds should be clearly stipulated with the determining factor being the COVID 19 burden in various regions.

The second area of focus is the implementation of UHC which began in 2018 and is expected to be fully implemented by 2022. After the piloting programme of UHC, the approach adopted for the delivery of UHC is in two aspects: firstly, the strengthening of the primary health system (county level) through ensuring provision of Health products and technologies - a responsibility assigned to the Kenya Medical Supplies Agency (KEMSA) and having requisite number of health human resources - a responsibility assigned to both levels of government. These two aspects of UHC delivery are supported by the inter-partnership agreements (IPA's) between the two levels of government.

**The sector has also been allocated Kshs 5.4 Billion which will be channelled to KEMSA for supply of essential health products and technologies (HPT's) to counties.** The target set is 100% UHC



HPT's refill rates. The risk here is procurement processes within KEMSA which may result to delays and failure to fully adhere to the procurement laws when purchasing the HPT's.

**The second aspect is the provision of social health insurance to vulnerable persons for patients accessing health service in level 4 to 6 health facilities.** The National Hospital Insurance Fund (NHIF) has been identified as the institution to provide social insurance. However for NHIF to offer social insurance, legal and administrative reforms are currently ongoing. Under the UHC, Kshs 6.3 Billion has been allocated for social health insurance. The risk here is the slow pace of reforms at the NHIF in order to transform it to a social insurance provider. This may hinder the utilization of the funds allocated.

**To ensure that the sector responds to the COVID 19 pandemic as well as ensure that implementation of UHC remains on course, the following are the key areas to keep an eye on during the implementation of the 2020/21 budget:**

- i. The rollout of the social health cover under a reformed NHIF as part of UHC where the 2020/21 target is to cover 195,000 vulnerable households;
- ii. The implementation of the Inter Partnership Agreements (IPA's) between the National and County governments in the provision of essential medicines for UHC under KEMSA where the target is 100% supply of health products and technologies to counties.
- iii. Track the progress in implementing interventions aimed reducing the COVID 19 infections in the country which includes recruitment of 5,000 health workers, provision of 20,000 hospital beds to hospitals, provision of 50 walk through sanitizers at border points and in hospitals as well as testing of 32,000 persons.
- iv. Fast tracking the governance issues related to accountability in the supply chain of health related goods and services.

### **Social Welfare for the Vulnerable**

**The COVID -19 Pandemic has significantly disrupted livelihoods.** The International Labour Organization (ILO) estimates that, in the second quarter of 2020, 195 million full-time workers lost employment globally. It is further estimated that by the end of this year, workers will lose \$ 3.4 trillion equivalent of income.<sup>20</sup>

Domestically, the disruption in the transport industry, the dusk to dawn curfew, closure of restaurants and entertainment joints coupled with restriction of movement for the most affected counties had an adverse effect on employment particularly in the informal sector. The resultant loss of income as a result of these measures has increased the vulnerable population in the country and hence the need for urgent policy interventions.

**The Social Protection sector plays a key role in alleviating the challenges associated with the Covid-19 pandemic** because of its central role in the provision of social assistance to the vulnerable including Older persons, Orphans, vulnerable children and the disabled.

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<sup>20</sup> The United Nations Department of Global Communications (DGC)

**In the Financial Year 2020/21, the Kenya Hunger Safety Net Programme has been allocated Kshs. 4.38 billion** to put 111,850 households under regular stipends. The aim of this programme is to cushion households deprived of livelihoods as a result of severe droughts in the ASALs.

**To enhance labour productivity, the National Industrial Training Authority, Kenya Youth Empowerment and Opportunities Project and the National Employment Authority were allocated Kshs.1.14 billion, Kshs.1.70 billion and Kshs.0.23 billion respectively.** With these resources, the three entities are expected to place 28,000 trainees on industrial attachment; train 22,000 youths and certify them on industrial skills; and secure 10,000 internship positions for graduates.

**To cushion the vulnerable in society from the loss of income and disruption of livelihoods, the National Social Safety net has an allocation of Kshs.29.76 billion** to be implemented majorly through the two projects of Cash Transfers and the Kenya Social and Economic Inclusion. The cash Transfers aims at supporting 833,000 households with older persons, 390,500 households with OVCs and 47,000 households with PWDS. It is estimated that 250,000 older persons aged over 70 years and above who are poor and vulnerable are not covered by the programme due to underfunding.

**The success of the Cash Transfer programme largely depends on the availability of exchequer.** The likelihood of revenue underperformance is therefore a significant challenge.

**Table 11: Summary of key priority programmes and projects for the FY 2020/21**

Vote	Programme	Key projects	Allocations ( millions)	Targets/ KPIs
1035	Accelerated ASAL Development (7,304 million)	1035100100 Kenya Hunger Safety Net Programme	4,383	111,850 beneficiary households under regular programme
		1035101800 Kenya Development Response to Displacement Impact project	3,500	20 boreholes drilled, 20 health facilities equipped and rehabilitated, 20 schools improved and equipped, 100,000 ha of land rehabilitated, 1,200 community groups facilitated to undertake livelihood activities
1184	0907000 Manpower Development, Employment and Productivity Management (3, 978 million)	1184002000 National Industrial Training Authority	1,145	28,000 trainees placed on industrial attachment
		1184101800 Kenya Youth Empowerment and Opportunities Project	1,700	22,000 youths trained and certified in industrial skill
		1184001700 National Employment Authority	225	10,000 graduates internship positions
1185	0909000 National Social safety Net ( 29,761 million)	1185001200 Cash Transfers	27,442	833,000 households with older persons supported with cash transfers, 390,500 households with OVC supported with cash transfer, 47,000 households with PWSD supported with cash transfers
		1185104000 Kenya Social and Economic Inclusion Project	2,319	8,300 households receiving nutrition sensitive cash transfers, 75% of NSNP beneficiaries enrolled in NHIF

Source: National Treasury and Appropriation Act, 2020.

### Keep an Eye on:

- i. The Timely release of the approved resources for cushioning the vulnerable in society especially the cash transfers under the National Social Safety Net and the Hunger Safety Net programmes so as to guarantee seamless and predictable flow of cash to the **1.38 million** beneficiary households under the two programmes
- ii. The progress in the distribution and placement of the **28,000** trainees in industrial attachment and the training and certification of **22,000** youth in industrial Skills to enhance labour productivity
- iii. Whether the Planned enrolment of **75%** of NSNP beneficiaries to the National Hospital Insurance Fund (NHIF) through the Kenya Social and Economic Inclusion Project is achieved, and ensure that at least 50% of the target is achieved by December, 2020.

**In response to the undesirable consequences of the COVID-19 pandemic on livelihoods, the National Hygiene Programme (NHP) dubbed *Kazi Mtaani* was conceptualized.** The initiative was designed to be implemented in two phases with the first phase implemented from 29<sup>th</sup> April 2020 to 26<sup>th</sup> June 2020. The first phase of the programme targeted slum areas in eight counties and benefitted a total of 31,689 vulnerable youths living in slums and informal settlements.

Phase two of the programme has been allocated Kshs.10 billion in the FY 2020/2021 approved budget and targets to engage 282,617 vulnerable youths living in slums and informal settlements in urban areas across the 47 Counties for a duration of six and a half months<sup>21</sup>. It is expected that the youths will be engaged in productive labour based economic activities that will enhance money circulation and stimulate the economy.

**Implementation of the programme however, presents some challenges.** Firstly, coordination and execution of the programme is a significant challenge to implementation of the initiative. This is because the approved resources are spread under various votes, for instance, the State Department for Housing and Urban Development has been allocated Kshs. 3,000 million, State Department for Infrastructure has Kshs. 5,000 million, office of the president through NMS has been allocated Kshs. 1,155 million and the Ministry of Water has been allocated Kshs. 845 million. Thus clear coordination is paramount. Secondly, recruitment procedures for the programme are opaque and are prone to abuse, nepotism, favouritism and corruption. In addition, there are no clear expected outputs from the various activities in which the youth are engaged in.

**Keep an eye on:**

- i. Success in the roll out of the ***Kazi Mtaani*** initiative that is devoid of abuse, nepotism, favouritism and corruption to ensure proper identification of the target beneficiaries in all the Counties.

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<sup>21</sup> Ministry of Transport, Infrastructure, Public Works, Housing and Urban Development

## 2.2. Infrastructure

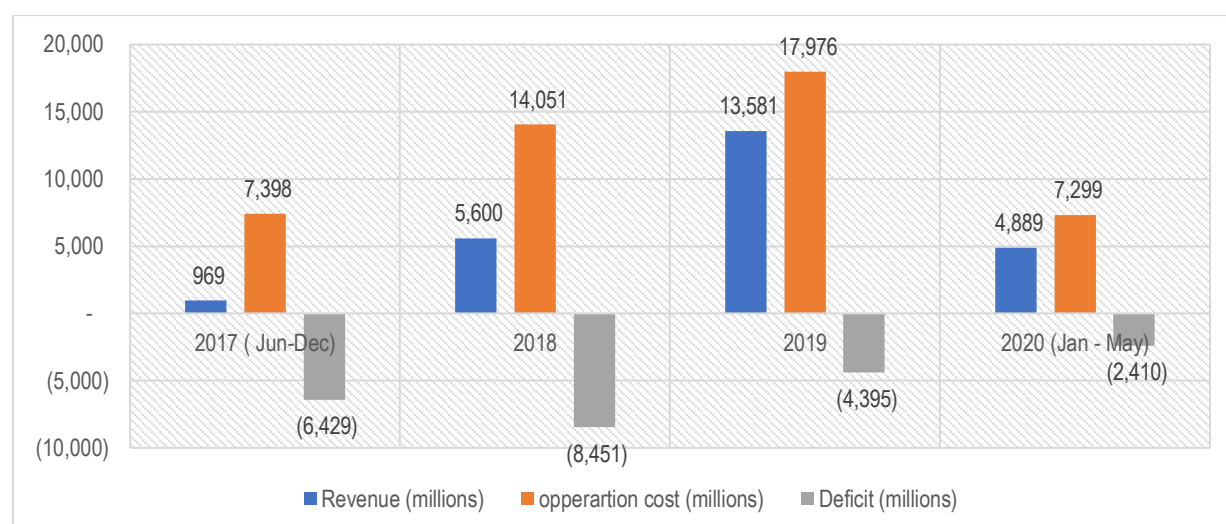
### 2.2.1. Enhancing Implementation of projects in the Transport Infrastructure

The government has continued to invest heavily in transport infrastructure and has invested in major infrastructure projects such as expansion of the road network, Airports, ports and the construction of the Standard Gauge Railway from Mombasa to Malaba. However, despite the huge investments in the sector, inadequate funding is still an impediment to project implementation. The sector has huge resource requirements due to the Capital intensiveness and huge portfolio especially in the road subsector which is implementing over one thousand projects across the country.

The issue of pending bills is a significant bottleneck facing the sector. It is estimated that the road sub-sector has accumulated an estimated Kshs. 80 billion worth of pending bills and there are pending bills worth Kshs. 40 billion accruing from the operational cost of the Standard Gauge Railway. In an attempt to address this, Kshs.60 billion was provided in the second Supplementary Estimates of 2019/2020. However, its utilization is yet to be reported on.

The SGR is not able to meet its financial obligation from its own revenue. An analysis of revenues and operational expenditures of the SGR reveals that the SGR is nowhere near meeting its financial obligations from its revenues. In this regard, thus there will be need to explore possibility of accessing the Railway Development Levy Fund (RDLF) to pay the outstanding Bills.

Figure 18: Analysis of annual revenues vs. operational expenditures of the Standard Gauge Railway (SGR) from June 2017 to May 2020



Source: Ministry of Transport, Infrastructure, Public Works, Housing and Urban Development

In the Financial Year 2020/21, the sector has been allocated Kshs. 237.14 billion of which Kshs. 189.59 billion is earmarked for expanding the road network while Kshs. 47.55 billion is to support ports and rail projects. In addition, the private sector plays a key role in upscaling and improving mobility through Transport infrastructure among them the Construction JKIA – James Gichuru Express way.

In the 2020/20 - 2022/23 Medium Term Expenditure Framework, the State Department for Infrastructure intends to construct 5,424 KM of roads, rehabilitate 836 KM through the low volume seal roads programme and maintain 103,062 Km of roads through the Road Maintenance Levy Fund. Out of the Kshs. 189.59 billion allocated to the State department for FY 2020/21, Kshs. 8.19 billion is for pending financial obligations of 65 projects which were 100% completed by February, 2020 (**see annex**). Despite completion, these projects have an outstanding balance of Kshs. 73.91 billion which will have adverse impact on the implementation of budgets of the coming financial years.

**Table 12: programmes and priority projects as well as expected KPIs for monitoring/oversight**

Vote	Programme	Key Project(s)	Allocation (millions)	KPIs/ Targets
1091	Road Transport	Construction, Rehabilitation, maintenance and design of road projects	189,591	Construction 1,808 Km . Rehabilitation 280 KM , maintenance 34,354 and design of multiple road projects
	Rail Transport (23,223)	1092100200 Development of Mombasa to Nairobi Standard Gauge Railway	2,000	100% completion
		1092104100 Development of Nairobi to Naivasha Standard Gauge Railway	18,094,	2 million passengers and 7.5 million tonnes of freight transported
	1092105500 Big Four projects	Dongo Kundu Special Economic Zone	3000	Functional port at Dongo Kundu -50% completion of port at Dongo Kundu
1092	Marine (15,233)	1092100100 Mombasa Port Development project	5,000	75% completion of construction
		1092103900 LAPSSET	6, 000	100% completion of the first three berths in Lamu port

Source: National Treasury & Appropriation Act, 2020

### Keep an eye on:

- i. Rationalization of projects in the roads subsector by removing the 65 completed projects from the budget books or indicating clearly what the resources are to be used for.
- ii. The progress and completion of the construction of 1,808 km of roads, Rehabilitation of 280 KMs of roads through Low Volume Seal and Maintenance 34,354 Km of roads through the Road Maintenance Levy Fund. Initial progress should be verified by December, 2020.

- iii. Progress in the settlement of pending bills with respect to SGR operations and Road projects. The Ministry should report on the status of the pending bills by end of the first half of the financial year.

### **Investing in Energy to spur Economic Growth**

**Provision of efficient energy infrastructure and affordable and clean energy services is a major catalyst in economic activities.** However, even though substantial resources in the sector have been deployed towards electricity modernization in the country, limited access and high energy costs especially for industrial production and commercial use continues to adversely affect the competitiveness of the economy. Furthermore, poor transport facilities and high cost of materials are significant bottlenecks in achieving higher capacity utilization for industrial and construction establishments, estimated at an average capacity of 63.6 per cent<sup>22</sup>. Despite recent policy impetus to scale up transmission and distribution including subsidized last mile connections for universal access to electricity by households, the connectivity and consumption target remains below committed levels. This is partly due to delays in completion of transmission lines and associated substations as well as other factors such as inappropriate pricing partly informed by generation obligations and variable costs (fuel cost, foreign exchange and inflation adjustments) which suppress electricity consumption.

**The onset of the COVID-19 pandemic appears to have worsened an already weak energy supply and consumption situation in Kenya.** Notably, reduced electricity demand occasioned by containment measures and declining incomes is a material risk to sector performance. Declining consumer demand is likely to be more disproportionately pronounced among some sector players such as the key power distributor - Kenya Power and its broader supply networks, taking into account its declining pre-crisis performance<sup>23</sup>, which reflected approximately 64% lower profit-after-tax in the year ended 2018. With the gradual phasing out of the COVID-19 containment measures, the electricity sector is expected to support economic recovery.

**The energy sector is one of the top priorities of the government due to its ability to spur economic growth as a critical enabler to the Big Four agenda.** Ensuring robust electricity generation and maintaining a stable electricity supply during the COVID-19 pandemic period is important for economic recovery. In FY 2020/21, the total budgetary allocation to the Energy sector is KSh 72.49 billion; of which 80% is under the Transmission and Power Distribution programme and 14% is for the Power Generation Programme which is critical for development of grid power infrastructure. Other programmes include the Administration Planning and Support Services Programme (1%) which supports project governance and necessary operational/technical needs; and the Alternative Energy Technologies Programme (5%) which comprises interventions such as installation and maintenance of solar projects targeting institutions and community boreholes, small hydropower projects, and other renewable energy initiatives such as the efficient use of biomass.

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<sup>22</sup> Economic survey , 2020

<sup>23</sup> [https://kplc.co.ke/img/full/zTKNb9GQqjoc\\_Profit%20Warning%20Announcement%20-%2019.09.2019.pdf](https://kplc.co.ke/img/full/zTKNb9GQqjoc_Profit%20Warning%20Announcement%20-%2019.09.2019.pdf) on 2019 profit warnings in excess of 25% net earnings compared to 2018 performance and Financial statement for FY 2018

A total of 72 total projects are currently under implementation with the outstanding cost to completion estimated at KSh 431.061 billion<sup>24</sup> (4% of GDP) in the medium term. Thus substantial resources will be required in future development budgets of the sector. In the last financial year, approximately 58 capital projects were under implementation. The additional projects are mainly Big Four related projects such as electrification of Dongu Kondu SEZ and Naivasha Industrial Park, electrification of hospitals and healthcare facilities.

**Budget execution challenges are an impediment to project implementation.** Emerging contractual risks such as bankruptcy of some contractors involved in construction of key transmission lines has delayed project timelines. This is particularly the case under the transmission lines and geothermal generation project in steam developed fields in Menengai in Nakuru. This is likely to lead to cost overruns and a delay in achieving least-cost power development objectives.

Other challenges to budget execution include:

- I. In year revisions affecting key projects such as street lighting, Power Transmission System Improvement Projects, electrification of Level 3 and Level 4 hospitals, connecting food processing plants and housing schemes as was the case in FY 2019/20;
- II. Outstanding pending bills which are likely to affect capacity of sector utilities to manage own operations and future implementation of energy infrastructure and connectivity projects on behalf of the government. Such arrangements which have also occasioned pending bills are mostly between REREC and KPLC, with outstanding claims under REREC and GoK amounting to KSh 12.76 billion for rural electrification including primary schools connectivity, among others;
- III. Lack of performance data for programmes and projects under implementation which are subsequently not reported by the Controller of Budget to parliament.

**High and uncompetitive pricing of energy remains a sticky point since prevailing tariffs are inconsistent with policy targets on cost of power for industry and households<sup>25</sup>.** Domestic and industrial power costs have remained high, despite the rising share of renewable energy sources in the national grid.

Key projects under implementation in the FY 2020/21 budget include last mile connectivity (Ksh 6.6 billion); Street lighting (Ksh 300 million); electrification of public facilities (Ksh 7.3 billion) and installation of transformers in constituencies (Ksh 900 million) by REREC; Olkaria – Lessos – Kisumu Transmission Line ( 5.9 billion); Machakos – Konza – Kajado – Namanga Transmission Line (Ksh 706 million); Bogoria - Silali geothermal exploration (Ksh 1.75 billion) and Menengai Geothermal projects (Ksh 2.37 billion) in Bogoria/West Pokot and Nakuru Counties respectively; and connectivity of Dongu Kundu SEZ (Ksh 2.00 billion) in Mombasa County. Timely completion of these projects will enhance grid stability and improve access to electricity as well as reduce system losses. For western Kenya in particular, completion of the Olkaria – Lessos – Kisumu Transmission Line will reduce the current reliance on power imports from Uganda.

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<sup>24</sup> 2020/21 Ministerial Submissions on the 2020/21 Budget Estimates with the outstanding projects costs as at March 2020 and including for projects running up-to 2027/2028,.

<sup>25</sup> Ministry of Energy past Submissions: Generation Tariff (US\$cts/kWh) of 7.41, Industrial/Commercial Tariff (US\$cts/kWh) of 9



### Keep an Eye On:

To realize access to electricity and upscale provision of affordable power, there is need to focus on the following key expected outputs and targets as well as related legal and policy measures:

- i. Progress in construction of 2,946 KM of transmission lines and 21 transmission substations. This includes 95% completion of the Olkaria – Lessos – Kisumu power lines which is beyond its completion timeline as well as 100% completion of the Loiyangalani - Marsabit 400 KV Transmission Line and Machakos Konza - Kajiado – Namanga transmission line and associated substations.
- ii. Construction and completion of 1,570 KM of distribution lines and 60 distribution substations - critical to the uptake of and improved access to electricity.
- iii. Electricity connection for 192,000 new customers under the Last Mile Electricity Connectivity and another 14,900 under electrification of public facilities under rural electrification.
- iv. The progress in the planned installation of 30,000 street lighting points with a target of 90, 000 in the medium term; and 1,958 transformer installations in constituencies across the country.
- v. Installation of 75 solar PVs in institutions and/or community boreholes and adoption of 30,000 clean cooking solutions in the period under consideration.
- vi. Pricing models used by the power distributors so as to ensure that both industrial and household power users receive affordable and internationally competitive power tariffs.

### 2.3. Food Security to all Kenyans

**Agriculture remains the leading driver of economic growth in Kenya and is the leading source of employment for most Kenyan citizens.** The sector has great potential for economic prosperity and has been identified as a key factor in enabling the country to achieve the economic growth rate of 10 per cent annually as envisaged in the Vision 2030. According to the Agricultural Sector Transformation and Growth Strategy, this growth rate can be achieved through the transformation of smallholder farmers from subsistence to an innovative, commercially-oriented and modern agricultural sector.

**The production of staple food has either declined or remained stagnant in the recent years.** The production of maize for instance declined from 42.5 million bags in 2015 to 39.8 million bags in 2019 according to data from the Ministry of Agriculture, Livestock, Fisheries and Cooperatives. Similarly, the production of beans declined from 8.5 million bags in 2015 to 8.3 million bags by 2019. The production of potatoes however has remained at 2.0 million bags over the same period (see Figure 19).

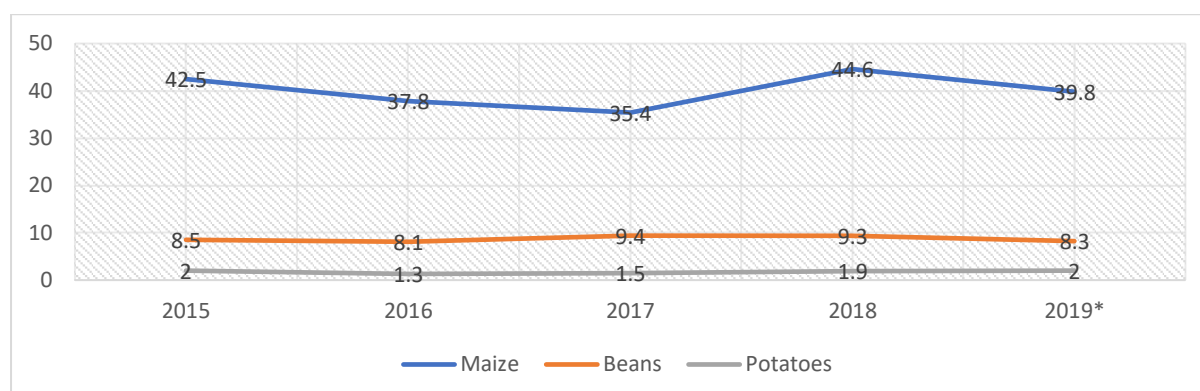
**Under the “Big Four” Agenda, the government is targeting to achieve food and nutrition security.** The overall strategy adopted by the government involves expanding irrigation schemes, supporting large-scale production of staples, increasing access to agricultural inputs, implementing programmes to support smallholder farmers and promoting the use of appropriate farming techniques among others<sup>26</sup>. Despite these measures, Kenya has remained a net food importer as shown in the table below.

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<sup>26</sup> BPS 2020 and the Medium Term



Figure 19: production of selected crops (Millions of bags)



Source: Ministry of Agriculture, livestock fisheries and cooperatives

Table 13: Importation of food in Kenya

S/No.	Commodity	Production in 000 MT	Imports in 000MT	Exports in 000 MT	Total Consumption	Net imports as % of Consumption
1.	Wheat and products	366	2,022	9	2,379	85
2.	Maize and Products	3,897	258	4	4,151	6
3.	Sorghum	288	141	58	371	22
4.	Rice	161	986	1	1,146	86
5.	Beans	1,150	49	17	1,182	3
6.	Fish and Sea food	134	45	9	170	21
7.	Meat	733	2	14	721	-2
8.	Fruits	2,882	35	255	2,662	-8

Source: KNBS

In FY 2020/2021, the overall budget for the sector is Ksh. 54.5 billion. The resources will fund a total of 8 key programmes within which approximately 80 projects will be implemented. To achieve food security and proper nutrition for all Kenyans, the government will continue to provide subsidized fertilizers to farmers in every planting season. In the 2020/2021 budget, 12 counties will benefit from government procured subsidized fertilizer using the e-voucher system where 98,500 farmers are expected to benefit. The government is also targeting to increase maize productivity from 40 million bags to 67 million bags through expansion of acreage under maize production.

To increase rice production, the government is targeting to expand the Mwea irrigation scheme by 10,000 acres through construction of dams, improvement of roads and other enabling infrastructure in the area. The intention is to increase rice productivity from 112,800 MT per acre to 271,000 MT through increasing the area under cultivation and subsidized mechanization. Further, the government will avail 4,000 MT of rice seed to farmers.

To increase fish production, the government targets to upgrade the aquaculture through research laboratory, accreditation and operationalization of 3 fish quality control laboratories and rehabilitation of fish landing sites in Lake Victoria.

**Crop production has not been affected significantly by the COVID-19 pandemic as farmers continue to work on their farms.** Thus it is expected that food availability will be largely adequate in the

post coronavirus period. However, there are numerous challenges facing the agricultural sector which will require critical focus during implementation of the 2020/21 budget. These include: dwindling arable land, increasing human population, low agricultural productivity, limited extension services, erratic and unreliable weather patterns, pest and disease prevalence, delivery and marketing of the agricultural products amongst others.

The following are the key projects and investments being implemented in the financial year 2020/2021:

- 1) **Kenya Livestock Insurance Scheme-** the objective of the project is to cushion vulnerable pastoral communities against drought. In the current financial year, the target is to insure 300,000 tropical livestock units across 12 counties.
- 2) **Regional Pastoral Livelihoods Resilience Project (RPLP)-** the objective of the project is to support pastoral and agro-pastoral communities in their efforts to reduce vulnerability to drought related shocks through participatory approaches. In the current financial year, the projects targets to: develop 14 boreholes and water pans; establish and rehabilitate 500 hectares under pastures and fodder; construct 7 livestock markets; procure and administer 10 million vaccines on cattle, sheep and goats.
- 3) **Modernization/Rehabilitation of the Kenya Meat Commission Factory-** the objective of the project is to provide market for livestock and livestock products. In the current financial year, the KMC seeks to produce and market 3,150 metric tonnes of meat and meat products and 234 metric tonnes of by-products.

#### **Keep an eye on:**

- i. **The implementation and establishment of livestock insurance schemes for insuring** planned 300,000 tropical livestock units across 12 counties.
  - ii. **Support to pastoral and agro-pastoral communities** where there will be drilling of 14 boreholes and water pans, rehabilitation/ establishment of 500 hectares under pastures and fodder; as well as procurement and administration of 10 million vaccines on cattle, sheep and goats.
- 
- 4) **Drought Resilience and Sustainable Livelihood Programme in the Horn of Africa-** in 2020/21, the target is to: rehabilitate 120 hectares of irrigation infrastructure; construct 44 water structures (earth dams, boreholes, water pans); and to plant 40 hectares of improved pastures.
  - 5) **Kenya Cereal Enhancement Programme (KCEP)-** The project targets to increase the productivity of smallholder farmers in cereal staples including maize, sorghum, millet, and associated pulses, and to support smallholder farmers to graduate from subsistence to commercial agriculture. During the FY 2020/21, the project targets to; provide 118,648 smallholders with production inputs and technological packages, train 18,119 small holder farmers on harvest and post-harvest management for improved management of grains; and refurbish 10 storage facilities.

**Keep an eye on:**

- i. **Provision of farm inputs and technological packages** where 118,648 smallholder farmers will be supplied with production inputs and technological packages.
- ii. **Training on harvest and post-harvest management.** 18,119 smallholder farmers are to be trained for improved management of grains.

**6) National Value Chain Support Programme-** the objective of the programme is to avail quality crop production inputs to farmers across 12 counties in 2020/21. The programme seeks to: procure 17,620 metric tonnes (MT) of subsidized fertilizers to benefit 98,500 farmers; procure 13,298 metric tonnes of lime, 1,121 metric tonnes of assorted seeds, and 113 metric tonnes of agro-chemicals; enrol 328,400 farmers using digital e-subsidy platform.

**Keep an eye on:**

- i. Procurement and distribution of 17,620 metric tons of subsidized fertilizers to 98,500 farmers.
- ii. Procurement of; 13,298 metric tonnes of lime, 1,121 metric tonnes of assorted seeds, and 113 metric tonnes of agro-chemicals;
- iii. Enrolment of 328,400 farmers using digital e-subsidy platform.

**7) Food Security and Crop Diversification Project-** the project seeks to: improve the livelihoods of Miraa farmers; diversify food crops; and enhance food productivity. The livelihoods of miraa farmers is to be improved through construction of water pans, dams, boreholes and construction of miraa sheds. Food diversification is achieved through procurement and distribution of: green grams, cow peas, sorghum, beans, cassava, sweet potato vines, cashew nuts, coconut, macadamia, and certified potato seeds.

**Keep an eye on:**

- i. Procurement and distribution of: 250 MT of green grams; 100 MT of cow peas; 100 MT of beans; 100,000 sweet potato vines; 60,000 MT of subsidized high yielding maize seeds; 4,000 MT rice seeds; 100,000 macadamia seedlings; 100,000 cashew nuts seedlings to farmers.

**8) Fisheries, Aquaculture and the Blue Economy** is very essential in increasing food security and income. Fisheries and aquaculture are essential in delivering fast socio-economic benefits to the communities in the coastal areas. The 2020/21 budget will fund the Aquaculture Business Development Programme, Kenya Marine Fisheries and Socio-Economic Development, the exploitation of Living Resources under the Blue Economy, and rehabilitation of fish landing sites in L. Victoria.

### Keep an eye on:

- i. **Increased marine fish exports** where Kenya Marine Fisheries and Socio-economic development project will seek to export 4,350 metric tons of marine fish and fish products.
- ii. **Development of maritime spatial plan-** the spatial plan should be finalized 100 percent
- iii. **Rehabilitation of fish landing sites** where 6 fish landing sites in L. Victoria will be rehabilitated to 80% completion.

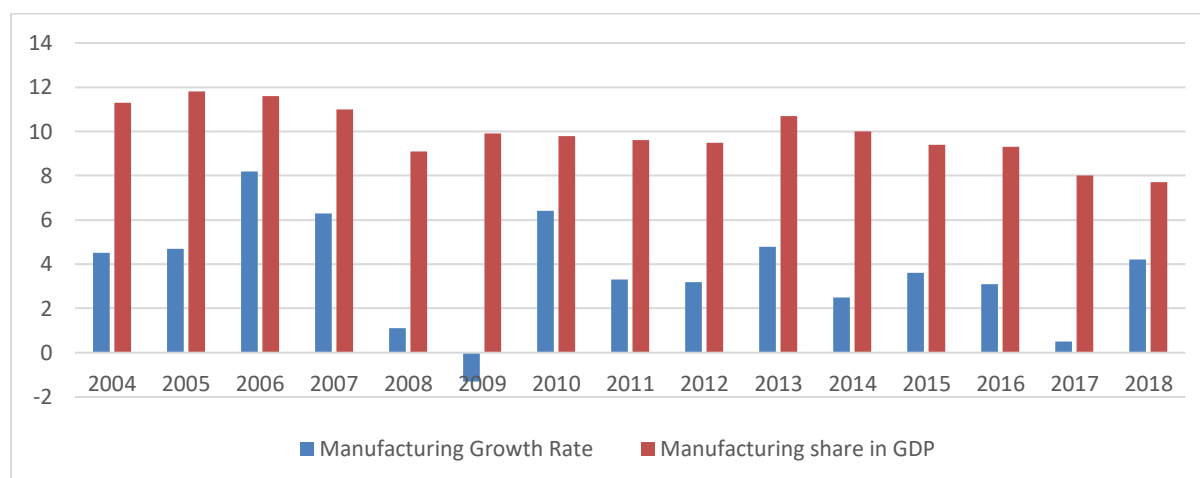
- 9) **Other key investments** in the sector include Kenya Climate Smart Agriculture Project (KCSAP), Fall Army Worm Mitigation, National Agricultural and Rural Inclusivity Project (NARIGP), Crop Insurance, and Cotton Industry Revitalization Project.

## 2.4. Manufacturing

**A robust, diversified and competitive Manufacturing Sector is critical to the transformation of the country into a middle-income economy.** The sector is critical to Kenya's economic growth and development and holds the key to the country's exports competitiveness particularly in agriculture. Through its forward and backward linkages with other sectors of the economy, manufacturing creates jobs which is required for the ever-growing population.

Even before the Vision 2030, the Economic Recovery Strategy (ERS) by the National Rainbow Coalition (NARC) government in 2004 put significant emphasis on improving the performance of the manufacturing sector. The period 2004–07 during which the ERS was implemented resulted in improved power supplies, increased supplies of agricultural products for agro- processing, tax reforms and tax incentives, more vigorous export promotion and liberal trade incentives that helped firms take advantage of the expanded market outlets. Figure 20 shows the high growth experienced during this period as a result of the policies initiated under the ERS.

Figure 20: Manufacturing annual growth rates and contribution to GDP

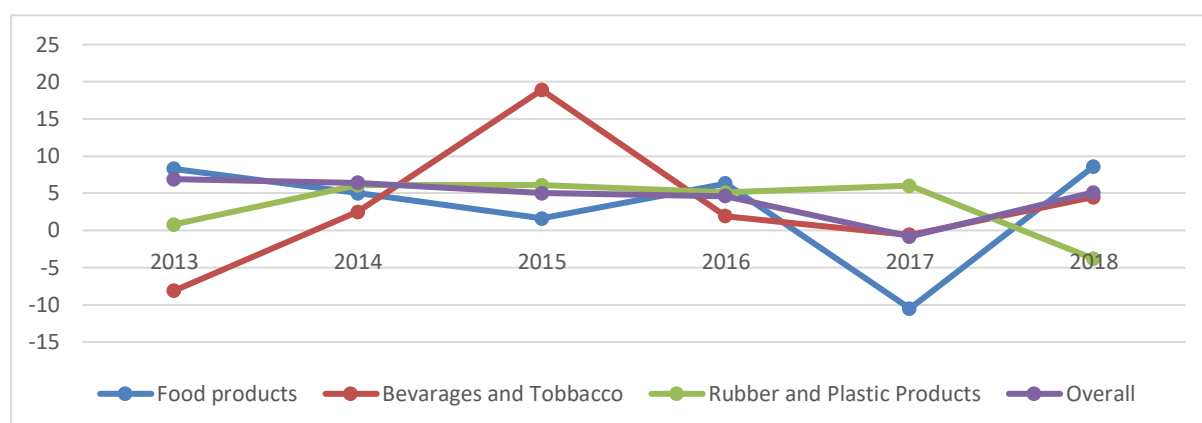


Source: KNBS

**In the medium term, the goal of the Sector is to increase its contribution to GDP from 7.7 per cent in 2018 to 15 per cent by 2022.** It should be noted however that over the period 2004-2018, the share of manufacturing to GDP has averaged below the 10 percent mark. This poor performance has been occasioned by numerous challenges facing the sector. According to the Kenya Association of Manufacturers Report (2019)<sup>27</sup>, the Manufacturing sector is 80 percent dominated by either Micro or Small Enterprises which account for only 20 percent of the manufacturing output. Many studies have shown that enterprises in this size category face similar problems. First, they are under-capitalized and face very poor transformation prospects. In addition, they have limited access to financial services and inadequate capacity to meet required quality and standards. The challenges are exacerbated by the start-up capital which is often borrowed from family and friends. Consequently, such firms invest very little, usually in used equipment. The firms are therefore less productive and less able to compete in external markets and domestically with imports majorly from South East Asia Countries<sup>28</sup>.

**There is no new capacity created by the manufacturing sector.** As illustrated in the figure 21, the percentage change in quantum indices of manufacturing production is on the decline suggesting Kenya is experiencing de-industrialization.

Figure 21: Growth in Quantum Indices of Manufacturing Production, 2013 - 2018



Source: KNBS

**While manufacturing should be driven by the private sector, the role of the government cannot be gainsaid.** The provision of an enabling environment is critical. The Big four agenda outlines various programmes and projects identified under the third medium plan of Vision 2030 that will improve manufacturing and increase its share in the GDP to 15 percent by 2022. However, over the past years, the government has failed to meet the set targets for these projects. Many projects particularly under the state department for Industrialization have not been completed as envisaged. The main challenges hampering effective project implementation include: some of the projects being implemented didn't undergo feasibility studies hence unforeseen challenges related to project implementation occur; budget

<sup>27</sup> KAM Report 2019

<sup>28</sup> [https://www.brookings.edu/wp-content/uploads/2016/07/L2C\\_WP25-1.pdf](https://www.brookings.edu/wp-content/uploads/2016/07/L2C_WP25-1.pdf)  
[https://kam.co.ke/kam/wp-content/uploads/2020/05/KPMG-KAM-Survey-The-impact-of-Covid-19-on-the-manufacturing-sector-in-Kenya\\_FINAL\\_19May2020-1.pdf](https://kam.co.ke/kam/wp-content/uploads/2020/05/KPMG-KAM-Survey-The-impact-of-Covid-19-on-the-manufacturing-sector-in-Kenya_FINAL_19May2020-1.pdf)

cuts effected through numerous supplementary budgets; delay in enacting enabling regulations; pending bills among others.

**The key projects currently being implemented to support manufacturing include** construction of Special Economic Zones in Mombasa and Naivasha; development of Textile Hub in Athi River; construction of Leather Industrial Park in Kenanie; construction and equipping of CIDCs; the Kenya Industry and Entrepreneurship project among others. Further the government had undertaken to operationalize the MSE fund by the end of the second Medium Term Plan (MTP); a project that is yet to materialize since the regulations are yet to be developed. The bulk of these projects are being implemented albeit at a lower than envisaged rate as indicated below.

**Table 14: Key Projects Supporting Manufacturing in KHz. Millions**

S/No.	Project	Total Cost	Estimated	Start date	End date	Actual Cumulative Expenditure	Allocation
1.	Dongo Kundu SEZ	100,000		2013/14	2020/21	95	177.2
2.	Kenanie Leather Park	4,409		2014/15	2020/21	2080	236.6
3.	Athi River Textile Hub	8,240		2014/15	2020/21	4631	295.7
4.	Modernization of Rivertext	-		2015/16	2020/21	4480	843.4
5.	Construction of Industrial Research Laboratories	5,500		2013/14	2020	2435	689.3
6.	Construction of Industrial Development Centres	1,529		2015	2021	154	281

Source: State Department for Industrialization

### Development of Freeport & Industrial Parks-SEZ at Dongo Kundu and Naivasha.

The Dongo Kundu project was started in 2013 but is being implemented slowly despite the conclusion of a MoU for concessionary loan from the Japanese government. While the ground breaking was done in October 2019, the project never kicked off as envisaged and the budgetary allocation of Ksh. 1.5 billion for the project was removed completely through the supplementary II budget of FY 2019/20 leaving the project with no resources for its activities. Key targets such as construction of Business centre to house one stop shop, construction of custom gatehouses and custom warehouses, perimeter wall and an administration block were never actualized. In FY 2020/2021, the project has been allocated Ksh. 172.2 million only which isn't enough for the project to take off and it is therefore likely to be delayed further.

Similarly, the Naivasha SEZ has experienced inordinate delays since its conception in 2013 partly due to lack of funds. In instances where there have been budgetary allocations, austerity measures have always led to budget cuts. For instance, in FY 2019/2020, the entire budgetary allocation of KSh. 1,132 million was cut during the supplementary budget process. As such, the project has failed to achieve its target within the stipulated timelines. So far, the only significant milestone recorded for the project relates to

compensation for land acquisition which was completed in 2019. Phase II of the project entails construction of the necessary infrastructure and is expected to last for three years.

**Keep an eye on:**

- i. The planned completion of basic infrastructure at Dongo Kundu SEZ by 15% through constructions of a centre to house one stop shop and construction of custom gatehouses and warehouses
- ii. The planned completion of basic infrastructure at Naivasha SEZ by 25% through construction of custom gatehouses and warehouses, perimeter wall, development of buffer zone and landscaping.

### **Development of Leather Industrial Park**

The construction of the Kenanie leather park has been started all over again with drawing up of a revised master plan after heavy rains in 2018 rendered 60 percent of the land unsuitable<sup>29</sup>. The project which was started in 2014 has also been regularly subjected to budget cuts which are often implemented through the supplementary budget. Failure to complete the project as scheduled will lead to delayed returns on investments. The budgetary allocation of **KSh. 236 million** is expected to facilitate completion of the common effluent treatment plant, construction of access roads as well as preliminaries towards the development of two tannery sheds, three footwear and leather goods sheds.

**Keep an eye on:**

- i. The planned completion of the common effluent treatment plant at Kenanie Industrial Leather Park by 40 percent.

### **Development of Athi River Textile Hub**

The project which was started in 2014 was designed to host a serviced textile city at the Export Processing Zone in Athi River in order to meet the manufacturing investments needs of garment marketing firms. It was envisaged that the project would attract 100 textile investment firms to take up investment opportunities relating to cotton ginning and yarn spinning, manufacture of textile fabrics and home fabrics among other ventures at the textile city and thereby create more than 200,000 jobs. However, this project has not been implemented as envisaged. Like Kenanie, it has been slow to attract investments and the infrastructure system that was to be provided is yet to be finalized on account of inadequate resources and budget cuts through supplementary budgets. The total cost of the project is estimated at KSh. 8.2 billion but so far only KSh. 3.6 billion had been expended as at December 2019. In FY 2020/2021, the project has been allocated KSh 297.5 million. These resources are targeted at construction of new internal access roads, repair and re-carpeting of the existing internal roads.

**Keep an eye on:**

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<sup>29</sup> Ministry of | Industry, Trade and Cooperatives submission to Departmental committee on Trade and Industry during the scrutiny of 2019/20 estimates

- i. The planned increase in investments in the EPZ by 35 percent with half year progress assessment to be done by December 2020.
- ii. The planned additional 62,000 jobs to protect livelihoods
- iii. The planned increase in exports by KSh. 75 billion to the United States under the AGOA scheme and the rest of the world.

### **Securing MSMEs jobs amidst COVID-19 pandemic**

As noted earlier, Kenya's manufacturing is 80 percent dominated by either Micro or Small Enterprises which account for only 20 percent of the manufacturing output. Many studies have shown that enterprises in this category face similar problems. The impact of COVID-19 on MSMEs is felt far much harder than larger manufacturing firms and access to finance is far more difficult as they are considered high risk enterprises<sup>30</sup>. To alleviate some of these challenges, the government is constructing Constituency Industrial Development Centres as incubation centres to support the MSME sector. Further, a budgetary allocation of KSh. 712 million has been provided in the FY 2020/21 budget for MSMEs to access finances. However, failure to provide a clear legal framework for the fund may impede access to this facility.

Further to sustain MSMEs during the COVID -19 period, the government will continue with its policy of "Buy Kenya Build Kenya" initiative. To this end the government intend to purchase 250,000 prefabricated desks and buy 20,000 hospital beds locally mainly through the ministries of Education and Health. Further the government will continue with the payment of historical pending bills owed to small businesses majorly in the State Department for Correctional Services and the National Youth Service among others.

### **Keep an eye on:**

- i. Completion of and equipping of 115 Constituency Industrial Development Centres
- ii. Facilitation of industrial incubation and financial support to MSMEs
- iii. Amount of loan disbursed to MSE through loans by MSE Authority
- iv. Development of an enabling SMEs policy

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<sup>30</sup> KPMG-KAM Joint Survey 2020



## Chapter Three:

# Enhancing Equity, transparency and accountability to achieve the devolution dream

***“A Man kept searching for his wallet under the street lamp because, he said when asked, it was too dark in the back street where he had lost it.”***

### 3.0. Introduction

**The advent of devolution in August 2010, ignited the hope of Kenyans for equitable development across all parts of the country.** For many years, centralized decision making with little participation at the grassroots level had led to poor service delivery at the local level. The 2010 Constitution provided for a basic minimum of 15% of the nationally raised revenues to be set aside to fund devolved functions. Seven years down the line, and still counting, equitable development across the entire country is still a dream. This is partly attributed to the amount of resources (equitable share) set aside to finance devolved functions, the efforts in raising local revenues and the fundamental issues of governance and accountability.

**County governments have specific functions outlined in the constitution but without sufficient resources and proper management, they may take a long time to efficiently and effectively deliver on these functions.** Transparency and Accountability are key pillars of governance. In the interest of the public every Kenyan must take responsibility for their activities in an accountable and transparent manner. Studies have shown that the higher the transparency and accountability in use of public resources, the better the stability and growth of the economy.

**The Budget is the only mechanism available for the county governments to deliver on each county government agenda which in turn contributes positively or negatively to the overall country development agenda.** It is not possible to implement well a badly formulated budget. Thus as much as some of the weaknesses in budget implementation at county level were inherited from the national government the key to efficiency in delivery of county level services lies in improved execution of the budget.

Budget execution just like in the national level calls for (i) ensuring that the budget is implemented as approved by the legislature<sup>31</sup> (ii) ensuring adherence to approved work plans, (iii) adhering to cash flow plans (i) predictable county exchequer releases and (v) control of commitments.

### 3.1. Do counties get what they need or what is available?

#### 3.1.1. County Equitable Share Compared to Sectors in National Government

Article 203 of Constitution outlines the criteria to be taken into consideration when determining the equitable share. This includes the need to ensure that the county governments are able to perform the functions allocated to them; the fiscal capacity and efficiency of county Governments; the developmental and other needs of the counties; the economic disparities within and among counties and the need to remedy them; and the desirability of stable and predictable allocation of revenue among others.

**The share of equitable share to Counties has reduced over the years, from 3.9% of Nominal GDP in 2014/15 to 2.8% in 2020/21 as shown in table 15.** This is due to overall resource scarcity as well as the rise of non-discretionary<sup>32</sup> expenditures which have created inflexibility in the overall resource envelope. It is noted that the county equitable share accounts for less resources than education and infrastructure sectors in the National Government. The major concern should thus be the process of

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<sup>31</sup> County Assemblies

<sup>32</sup> Non- discretionary in this case refers to public debt, interest payments and other related expenses

deciding on the minimum amount of resources to be set aside for counties beyond the issue of scarcity of resources.

**Table 15: County Equitable Share and allocation to National sectors as a share of GDP**

		2014/15	2015/16	2016/17	2017/18	2018/19	2019/20	2020/21
<b>A</b>	<b>Sectors</b>							
	Agriculture, Rural and Urban Development	1.4%	1.1%	0.7%	0.6%	0.7%	0.6%	0.5%
	Energy, Infrastructure and ICT	7.3%	6.2%	7.6%	4.6%	4.8%	4.5%	3.2%
	General Economics and Commercial Affairs	0.3%	0.3%	0.3%	0.2%	0.4%	0.3%	0.3%
	Health	0.9%	0.9%	1.0%	0.9%	1.0%	1.1%	1.0%
	Education	5.2%	5.0%	4.5%	4.9%	4.9%	4.9%	4.5%
	Governance, Justice, Law and Order	2.6%	2.5%	2.8%	2.5%	2.2%	2.1%	1.8%
	Public Administration and International Relations	3.8%	3.8%	2.8%	2.5%	2.4%	2.8%	2.7%
	National Security	1.7%	1.7%	1.7%	1.7%	1.6%	1.6%	1.4%
	Social Protection, Culture and Recreation	0.4%	0.5%	0.7%	0.6%	0.6%	0.7%	0.5%
	Environment protection, Water and Natural Resources	1.0%	0.9%	1.2%	0.9%	0.8%	0.9%	0.9%
<b>B</b>	<b>County Equitable Share</b>	<b>3.9%</b>	<b>4.0%</b>	<b>3.7%</b>	<b>3.5%</b>	<b>3.4%</b>	<b>3.1%</b>	<b>2.8%</b>

Source: PBO extraction from National Treasury publications and Controller of Budget publications.

**The current budget cycle does not provide a clear link between the process of determining the overall requirements for all counties (needs) and the estimation of the overall resource envelope.**

Thus the needs at the counties do not inform the vertical sharing of national resource envelope. The Budget cycle is provided for in the Public Finance management Act and the attendant regulations both for the National government and the counties and outlines the steps that are to be followed annually. Unfortunately the two budget processes at the National and county level run parallel to each other creating a situation where there is consideration of the needs of the counties before the finalization of the vertical distribution of the resources. In many countries where there is interdependence between governments, often, the financial years start in different months. In the United States of America for instance, the financial year for the states has a different timeframe from that of the federal budget year. This enables decisions at the states to inform the Federal and vice versa. It is important to look at the PFM act and as would be necessary, amend the financial years for the County Government and the national government to synchronize and establish a clear link between county resource bottom up process of establishing resource needs and the National process of top down of establishing the overall resource envelope.

**Keep an eye on:**

- (i) the key budget process dates for both the national and county governments to reduce delays in both the vertical and horizontal distribution of national raised resources.

**Table 16: The annual budget preparation and approval process**

Period	National	County
July –September	Initiation of budget cycle: Treasury Call Circular with guidelines, Launch of Sector Working Groups (SWGs) including the Macro Working group	Initiation of The county budget cycle; County Treasury call circular with guidelines, Launch of sector working Groups and production of ADPs <sup>33</sup>
October –December	Review, prioritization and finalization of SWG reports, Production of BROP <sup>34</sup> Public Participation/hearing	Review, prioritization, public participation, SWG reports, and production of C-BROP <sup>35</sup>
January-March	Submission of BPS <sup>36</sup> to Parliament, Agreement on Vertical Distribution of Resources (Division of Revenues legislation), agreement on Ministerial Ceilings.	Submission of C-FSP <sup>37</sup> to County Assembly. Agreement on Departmental Ceilings.
April	Agreement on Horizontal Distribution of Resources (County Revenue legislation) Distribution  Finalization and Submission to National Assembly of Annual Estimates of revenue and expenditure	Finalization of annual county estimates of revenue and expenditure and submission to county assemblies for review and approval
May – June	Review of annual Estimates of expenditure and approval:- annual appropriation and Finance act (revenue measures	Review of annual Estimates of expenditure and approval:- annual appropriation and Finance act (revenue measures

### 3.1.2. Counties Own Source Revenue

**Counties collect much less revenue than the estimated revenue base giving them less resources to deliver on required services.** Research<sup>38</sup> shows that the overall gap between the actual collection and revenue potential ranges between 35% to 94 %. This means many of the counties would be able to collect almost enough to equal what they are receiving from the National Government. The key revenues that counties collect are land and property rates, parking fees, market fees, lease rents, hospital or health services charges, single business permits among others.

**Own source revenues can enable the counties bridge the resource gap created by equitable share and also enforce law and order in fostering private sector led economic growth within counties.** However counties face barriers to effective revenue collection on account of weak forecasting of

<sup>33</sup> ADPs are the annual Development Plans that contain strategies and programs.

<sup>34</sup> BROP: Budget Review and Outlook Paper,

<sup>35</sup> C-BROP: County Budget review and Outlook Paper

<sup>36</sup> Budget Policy Statement

<sup>37</sup> County Fiscal Strategy paper.

<sup>38</sup> A study done by World Bank in 2018

collectable taxes, weak collection mechanisms and administrative issues that often lead to low enforcement and hence a high evasion rate.

Table 17: Counties revenue targets, actual and potential for 2013/14 to 2019/20

FY	Revenue Targets	Actual Revenue Collection	Potential	
			at 35%	at 94%
2013/14	54,207,798,427	26,296,089,510.00	35,499,720,838.50	51,014,413,649.40
2014/15	50,376,859,951	34,468,720,354	46,532,772,477.90	66,869,317,486.76
2015/16	50,539,746,840	36,905,771,161	49,822,791,067.35	71,597,196,052.34
2016/17	57,664,858,199	32,522,875,093	43,905,881,375.55	63,094,377,680.42
2017/18	49,219,014,037	32,491,694,261	43,863,787,252.35	63,033,886,866.34
2018/19	53,863,582,921	40,304,833,142	54,411,524,741.70	78,191,376,295.48
2019/20 *	57,824,660,000	37,380,440,000	50,463,594,000.00	72,518,053,600.00

Source: COB various issues and estimate for 2019/20, World Bank study

**The shortfall in equitable resources from the National Government and low collection of own source revenue is a major constraint to delivery of services at the county level.** The dream of devolution may take long to be achieved not unless the basic Minimum allocation of raised from 15% to 40% and efficiency in allocation and utilization of resources is enhanced.

### 3.2. Accountability and transparency in budget implementation

**Budget implementation at the county level should meet two major objectives of public finance namely; aggregate expenditure control, and operational efficiency.** This means the budget should be implemented as approved by the legislatures by instituting controls at the same time ensuring there is efficiency in the utilization of the voted resources. This however requires transparency and accountability systems for efficiency in implementation of the budget.

**Devolution has not yet translated to the envisioned equitable overall development in the country and this is partly due to the wastage brought about by inadequate accountability and lack of transparency in the management of resources.** Lack of transparency affects service delivery as both the beneficiaries of the services being delivered and those offering the services do not ensure public participation. In addition there is scarcity of information concerning the services offered and amount of resources used.

**The County Governments have continued to improve accountability for their finances through availing information even though this is inadequate to guarantee transparency.** Whereas at the National level there is a monthly publication of net exchequer issues in the Kenya Gazette, at the county level it is only the Controller of budget reports which have a time lag of more than three months and contain highly summarized information. In addition the end of year reports by the Auditor General also take time before they are discussed by the Legislature at the county level and the national level.

### Key principles on Budget Reporting

- **Budget Integrity:** Report on Budget as approved versus actuals- with details on agreed targets.
- **Operating performance:** Cost of programs versus actuals and results.
- **Comprehensiveness:** Ensuring all data on revenues and expenditures are captured.
- **Timeliness:-** information delayed is information denied. Reports must be on time and timely.
- **Budgetary accounting standards:** Implementing a commitment register  
Ick

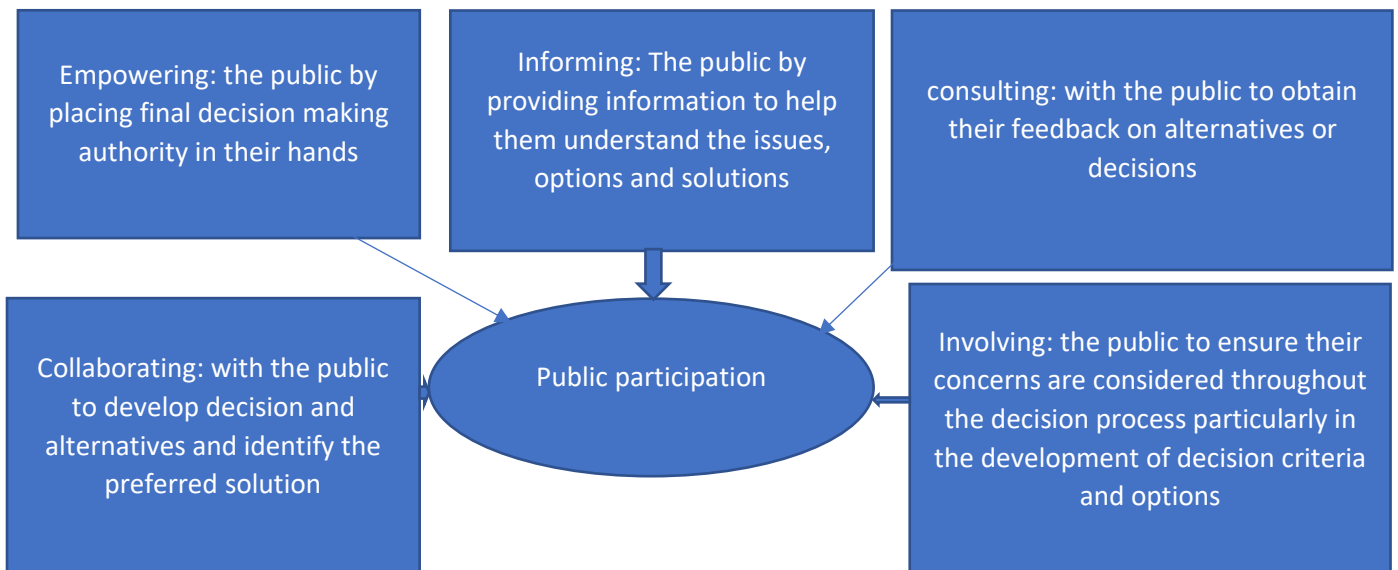
Enhancing transparency and accountability calls for wider and timely reporting on Budgets.

### 3.3. Enhancing Transparency through Public participation

There are three elements of public participation that need to be met for public participation to be successful as per the International Law association. Firstly, the decision making process needs to be transparent meaning the public should have access to information that is comprehensive and timely as per Article 35 of the constitution; secondly, the process should be consultative meaning that the public should participate in it; and thirdly, the public should have access to justice.

Public participation as required by the Constitution in Article 174 and in function 14 of the fourth schedule is key in decision making and takes different forms as shown in figure 22.

Figure 22: what public participation entails



Source: Ministry of Devolution and Planning

In planning and budget process, public participation in the county government should be undertaken from the initial stage of planning and preparation of County Integrated Development Plan (CIDP), County Annual Plan (ADP), County sectoral plans, Spatial Plans, Cities and Urban plans. The plans inform the development and approval of the budget where public participation should also be carried out. The County Budget Review and Outlook paper and County Fiscal Strategy Paper as well as the Finance Bill require budget participation.

**County government have carried out public participation since 2013/14 Financial year when the country implemented the devolved system of government.** However, majority of the counties do not meet even the minimum expectations as shown in figure 22. This is mostly as a result of inadequate resources and public participation activities that are carried out in an ad hoc manner with minimum publicity and few members of the public attending mainly to comply with constitutional requirements. The feedback on issues raised through public participation are also not provided to the public and no records are maintained on the issues raised for future reference particularly on the demands that might not be met in the short term.

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## **Annexes**

### ***Annex 1: list of allowable deduction removed from the Income Tax Act***

- i) The 30% of electricity cost incurred by manufacturers in addition to the normal electricity expense, subject to conditions set by the Ministry of Energy
- ii) Entrance fee or annual subscription paid during that year of income to a trade association which has made an election under Section 21(2) of this Act
- iii) Expenditure of capital nature incurred in that year of income by a person, on legal costs and other incidental expenses, relating to authorization and issue of shares, debentures and similar securities offered for purchase by the general public.
- iv) Expenditure of capital nature incurred in that year of income by a person, on legal costs and other incidental expenses, for purposes of listing on any securities exchange operating in Kenya, without raising additional capital
- v) Expenditure of capital nature incurred in that year of income by a person on rating for the purpose of listing on any securities exchange operating in Kenya
- vi) Club subscription paid by an employer on behalf of an employee
- vii) Expenditure of capital nature incurred in that year of income with prior approval by the Cabinet Secretary, by a person on the construction of a public school, hospital, road or any similar kind of social infrastructure

### ***Annex 2: Exempt Income that was removed from Income Tax Act***

- i) Income from public boards
- ii) Income from agricultural societies
- iii) Interest on tax reserve
- iv) Disturbance allowance for public servants
- v) Allowance on foreign travels
- vi) Emolument of officers of desert locust survey
- vii) Education grant paid by the government of the United Kingdom under agreement with the government of Kenya for public servants
- viii) Remuneration for international corporation administration
- ix) Income earned from working for a citizen of the United States of America on agricultural research
- x) Gains/profits from the UK atomic energy authority for discovery of uranium in Kenya

- xi) Income from listed bonds, notes, or similar securities to raise funds for infrastructure and other social services
- xii) Bonus, overtime and retirement benefits not exceeding 10%
- xiii) Dividends paid by a Special Economic Zone non-resident person
- xiv) Compensating tax regarding power producers under power purchase agreement
- xv) Interest from green bonds, among others

### **Annex 3: VAT exempt and zero rated goods and services proposed to be removed**

#### **(a) Proposed to be deleted from VAT exemption through the Tax Laws (Amendment) Act, 2020**

- i) Some helicopters and aeroplanes not exceeding 2,000 kg
- ii) Helicopters and aeroplanes parts
- iii) Mosquito nets
- iv) Hand-made fishing nets
- v) Fertilizers
- vi) Materials for animal feeds
- vii) Specialized equipment for solar and wind energy
- viii) Tractors, other than road tractors for semi-trailers
- ix) Materials for the manufacture of solar equipment
- x) Plastic biogas digesters
- xi) Biogas
- xii) Leasing of biogas producing equipment
- xiii) Parts for computer assembly
- xiv) Taxable goods for the construction of industrial parks
- xv) Inputs and raw materials for the for the manufacture of agricultural machinery
- xvi) Museums and natural history exhibits and specimens
- xvii) Chemicals, reagents, films etc for National Museums of Kenya
- xviii) Goods for construction of tourism facilities, recreational parks and conference facilities
- xix) Goods for clean cooking stoves
- xx) Inputs for clean cooking stove
- xxi) Stoves, cookers, barbeques etc
- xxii) Inputs for the manufacture of pesticides
- xxiii) Materials for the construction of grain storage facilities
- xxiv) Transfer of business as a going concern
- xxv) Goods for marine fisheries and fish processing

- xxvi) Goods under Special Operating Framework Arrangement with government
- xxvii) A motor vehicle for a returning public servant from foreign posting
- xxviii) Plant, machinery and equipment for the construction of plastic recycle plant

**(b) Exempt services proposed for removal from VAT Act**

- i) Insurance agency, insurance brokerage and stock exchange brokerage services
- ii) Construction of industrial parks
- iii) Entry fees for national parks and game reserves
- iv) Tour operators
- v) Construction of tourism facilities
- vi) Construction of liquefied petroleum gas (LPG) storage facilities
- vii) Assets transfer under Real Estate Investment Trusts (REITs)
- viii) Supplies made under Special Operating Framework Arrangement (SOFA) with government

**(c) Proposed to be removed from VAT Zero rate**

- i) Liquefied Petroleum Gas
- ii) Supply of ordinary bread
- iii) Inputs for the manufacture of agricultural pest control products
- iv) Materials for the manufacture of automotive and solar batteries

***Annex 4: Observations on the overhaul of Investment Allowance (Investment Deduction)***

The following are some key observations on the repeal of the Second Schedule of the Income Tax Act:

- i. Greatly simplifies the Schedule by repealing it to clearly provide for the rates of investment deductions or allowances and removing unnecessary exemptions or waivers.
- ii. Reduces proportion of investment deduction for machinery or buildings to maximum 50 % in the first year of use to previous ridiculous 100% to 150% deduction.
- iii. Reduces unfair treatment of various sectors and regions. For example, there is no categorization of what rates should apply for major towns or rest of the country, or on whether a company is in the SEZ or EPZ.
- iv. While large companies received these generous investment waivers and treatments, most small businesses have had to deal with high costs of initial investment.
- v. The repeal helps address the problem of excessive tax expenditure associated with low performance of corporate income tax in Kenya. It is therefore expected to improve corporate income tax collection post COVID-19.

- vi. Drops old, antiquated provisions dating 1960s and 1970s which are no longer applicable today.
- vii. Removes the Commissioners power to increase the rates of deduction arbitrarily
- viii. It should however be noted that for some industries like manufacturing, hotels buildings, and hospitals, ships building among others are only allowed a one-off 50% investment deduction while others are allowed to deduct up to 100% in successive years on a reducing balance.
- ix. Removes deductions related to wear and tear of machinery or investments.
- x. May affect rate of investment and FDI, but a simplified framework is better.

#### **Annex 5: PAYE bands**

*Pay-As-You-Earn (PAYE) taxation bands, where the highest was reduced from 30% to 25%*

<b>Previous PAYE Bands (KSh. P.M)</b>	<b>PAYE rate (%)</b>	<b>New PAYE Bands (KSh. P.M)</b>	<b>Rate (%)</b>
First 12,298	10	First 24,000	10
The next 11,587	15	The next 16,666.7	15
The next 11,587	20	The next 16,666.7	20
The next 11,587	25	Above KSh. 57,333.3	25
Above 47,059	30	-	-

**Annex 6: Completed Projects with allocation for FY 2020/21**

s/no.	Roads	Total cost	Start Date	End Date	Actual to Feb. 2020	Remain cost	% Completion	Allocation 2020/21
1	Nairobi Southern Bypass	25,116	Jul-10	Jul-15	22,131	2,985	100%	100
2	NCTIP: Rehabilitation of Sultan Hamud - Machakos Turnoff Road (A109)	5,170	Nov-06	Jul-12	4,806	364	100%	65
3	NCTIP: Rehabilitation of Njoro Turnoff - Timboroa Road	4,384	9-Oct-06	19-Mar-10	4,284	99	100%	99
4	NCTIP: Rehabilitation of Kericho - Nyamasaria Road	10,379	16-Sep-10	30-Oct-14	10,325	54	100%	5
5	NCTIP: Rehabilitation of Nyamasaria - Kisian Road	8,048	9-Feb-12	16-Jun-15	7,825	222	100%	5
6	EATTFP: Busia OBP	954	Jul-12	Jul-15	629	325	100%	20
7	EATTFP: One Stop Border Post at Lungalunga Border Crossing	633	5-Jul-12	30-Apr-15	613	20	100%	20
8	KTSSP: Rehabilitation Webuye - Kitale Road	6,026	10-Jan-13	May-19	5,330	696	100%	50
9	KTSSP: Rehabilitation Maji ya Chumvi - Bachuma Gate Road	5,548	3-Nov-14	Nov-19	5,504	45	100%	10
10	KTSSP: Interchanges at Nyahururu, Njoro, & Mau Summit Turnoffs	3,870	2-Feb-15	Dec-19	3,557	314	100%	10
11	KTSSP: Lake Victoria Ring Road	640	Jul-15	Oct-19	289	351	100%	40
12	Marsarbit- Turbi Road	13,756	Apr-11	Jun-17	13,630	126	100%	10
13	Mwatate - Taveta Road	10,916	May-14	Feb-18	10,542	374	100%	5
14	Magumu - Njambini Road	820	Mar-13	Mar-15	811	10	100%	2
15	Turbi - Moyale Road	13,531	Oct-12	Sep-16	13,250	282	100%	33
16	Ndanai - Gorgor Road	1,101	1-Jun-14	13-Jan-17	993	108	100%	20
17	Rodi Kopany - Ndhiwa - Karungu Road	1,544	Apr-12	Sep-17	1,340	204	100%	60
18	Kehancha-Suna - Masara Road	6,226	May-13	Jul-17	5,938	288	100%	10
19	Mariakani – Bamba (Rwc 096)	2,435	Apr-16	Oct-19	2,166	268	100.00	70
20	Kamatira - Cheptongei(D327/D329) RWC 10	3,369	May-16	May-19	2,421	949	100.00	110
21	Thekanda - Ndaraweta - Sasik - Singorwet - Leldaet	1,276	Jun-17	May-20	819	457	100.00	60

s/no.	Roads	Total cost	Start Date	End Date	Actual to Feb. 2020	Remain cost	% Completion	Allocation 2020/21
22	Lwakhakha - Korrosiondet - Tulienge - Sirisia - Namwela	1,610	Oct-16	Sep-18	1,036	574	100.00	50
23	Butere(Bukolwe) -Musanda - Bungasi - Sigomere - Ugunja	2,218	Dec-16	Nov-19	1,522	696	100.00	72
24	Kisima - Kibirichia - Kima - Ruiru	1,704	Aug-16	Feb-19	1,200	504	100.00	100
25	Kangeta - Muutine - Lare	652	Jun-17	Nov-18	315	337	100.00	85
26	Njegas - Mutito - Kagumo - Gatwe - Kangaita / Kiaga - Kianjege - Mukindori	1,253	Oct-16	Apr-19	1,224	29	100.00	100
27	Karima(A2) - Kianjege - Mukangu -Ndimaini - Karatina(A2) And Kiburu Kabonge	1,208	Oct-16	Apr-19	991	217	100.00	100
28	Imaroro - Mashru - Isara	3,038	Jun-17	Jun-20	2,110	928	100.00	90
29	Murang'a Town (Huhi Town Stn)-Karii Railway Stn-Muthingiriri-Marewa-Gakindu Bridge-Wandaka-Gikuu-Kayuy-Mirira	1,076	Aug-17	Jul-19	655	421	100.00	53
30	Modika - Nuno Road (phase II)	1,227	Mar-12	May-15	1,140	87	100%	6
31	Wajir - Buna -Moyale	206	May-12	May-15	186	20	100%	1
32	Eldoret - Webuye Road	6,512	Mar-11	Jul-16	6,441	72	100%	4
33	Nairobi - Thika Highway Improvement Project Lot 1 & 2	16,321	Jul-07	Jul-12	14,542	1,779	100%	300
34	Emali- Oloitoktok Road	5,140	Jun-08	Jul-12	4,972	168	100%	10
35	Jn. A109 (Changamwe round about) - Moi International Airport Access Road & Port Reitz Road	5,129	Apr-15	Oct-18	236	4,893	100%	10
36	Isiolo - Merille Road	6,332	Jun-07	Jul-10	6,267	65	100%	20
37	Kangema - Gacharage Road	4,468	1-Aug-12	Feb-16	4,029	438	100%	8
38	Elwak - Wargadud	505	Feb-16	Aug-18	505	-	100%	60
39	Bambo - Rhamu	635	Jan-16	Jul-18	634	1	100%	60
40	Kitale-Morpus (A1) (Lot No. 2)	431	Jun-16	Jun-18	430	1	100%	917

s/no.	Roads	Total cost	Start Date	End Date	Actual to Feb. 2020	Remain cost	% Completion	Allocation 2020/21
41	Morpus Junc b4- Marich Pass (A1) (Lot no. 3-Emergence maintenance	317	Jun-16	Jun-19	303	14	100%	50
42	NETIP: Lot 1_Isiolo – Kula Mawe	3,778	Aug-17	Feb-20	53	3,724	100%	60
43	NETIP: Lot 2_Kula Mawe - Modogashe	3,828	Aug-17	Feb-20	56	3,771	100%	60
44	NETIP: Lot 3_Modogashe - Samatar	3,858	Aug-17	Feb-20	109	3,749	100%	60
45	NETIP: Lot 4_Wajir – Wargetut	3,828	Aug-17	Feb-20	97	3,731	100%	60
46	NETIP: Lot 6_Wargetut – Elwak	3,778	Aug-17	Feb-20	52	3,725	100%	60
47	NETIP: Lot 7_Elwak - Rhamu	3,828	Sep-17	Mar-20	28	3,800	100%	60
48	Enjinja - Bumala Road	2,648	21-Oct-11	19-Jun-16	2,428	219	100%	20
49	Dundori-Oikalau-Njambini	65	Sep-16	Dec-20	65	1	100%	29
50	Dualling Thika - Kenol - Marua (A2-R)	28,000	25-May-17	Dec-21	-	28,000	100%	4,300
51	Sotik Roret-Sigowet D226 Roads	2,221	Sep-16	Sep-19	2,207	14	100%	43
52	Iten-Kapsowar Phase II-Kapsowar - Chebiemit	1,421	Jan-12	Mar-16	1,280	141	100%	50
53	Sigiri Bridge And Approaches	993	Aug-11	Jun-13	938	55	100%	20
54	Luanda-Akala	1,585	Nov-15	Feb-17	1,532	54	100%	0
55	Muthatari-Siakago/Rwc-059A	1,233	Aug-14	Feb-17	976	257	100%	40
56	Wamumu - Machanga Phase I	114	Feb-14	Sep-16	77	37	100%	10
57	Limo Hospital-Illula-Elgeyo Border-Moim Juntion And Tendwo-Bombo	2,159	May-19	Aug-20	2,090	69	100%	24
58	Mairi-Gatiani-Makomboki Gituru-Wanyaga Kimandi	1,459	Jul-10	Mar-19	768	691	100%	70
59	Waiyaki Way -Redhill Link Road	3,875	Mar-16	Mar-19	2,363	1,512	100%	150
60	Eastlands Roads (9.1 KM)	373	Mar-16	Mar-18	364	9	100%	100
61	Kahawa Westfly Over Bridge And Adjoining Accesses	403	May-16	Jul-18	396	8	100%	5
62	Eldoret Access Roads	747	Jun-17	Dec-18	597	150	100%	13
63	Industrial Area Roads	500	Feb-20	Aug-22	171	329	100%	5



s/no.	Roads	Total cost	Start Date	End Date	Actual to Feb. 2020	Remain cost	% Completion	Allocation 2020/21
64	Posta, Lotodo & Kacheliba Roads; Cereals-Chewoyet-Bendera Road	182	May-17	Nov-18	159	23	100%	10
65	District Hospital-Ndowasco RD-Showgound	164	May-17	Nov-20	108	56	100%	40
		<b>256,763</b>			<b>182,853</b>	<b>73,909</b>		<b>8,190</b>