REPUBLIC OF KENYA

Parliamentary Budget Office

UNPACKING OF THE BUDGET POLICY STATEMENT FOR FINANCIAL YEAR 2023/2024 AND THE MEDIUM TERM.

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INTRODUCTION

1. The National Treasury submitted the 2023 Budget Policy Statement (BPS) to Parliament on Tuesday, 14th February 2023 pursuant to Section 25 of the Public Finance Management Act, 2012. This is the first Budget Policy Statement to be prepared under the Kenya Kwanza Government and it sets out the priority programs, policies and reforms of the administration that will be implemented in the Medium-Term and indeed, the next five years. The Theme of the Budget Policy Statement is "***Bottom-Up Economic Transformation Agenda for Inclusive Growth***". This is in line with the Manifesto of the new administration that is founded on a bottom-up approach to economic transformation.

2. The 2023 BPS has been conceptualized against a backdrop of global economic slowdown occasioned by the lingering effects of the COVID-19 pandemic, the ongoing Russia-Ukraine conflict, elevated global inflation, prolonged supply chain disruptions and the effects of the ongoing drought that have exacerbated the urgency on food security and climate change effects. These dynamics are further compounded by a constrained fiscal space limiting government's ability to respond effectively through fiscal policy.

3. The BPS proposes expenditure ceilings for the national government including those of Parliament and the Judiciary, as well as indicative transfers to county governments for the next financial year. This has been undertaken through an assessment of the macroeconomic forecasts and financial outlook with respect to government revenue, expenditures and borrowing for the next financial year and over the medium term.

4. Once deliberated and approved by Parliament, the BPS will form the basis for the preparation of the national budget for financial year 2023/2024 and over the medium term. It should also form the basis for the Division of Revenue Bill, 2023 and for the county fiscal strategy papers which should be aligned to the national development agenda.

EVALUATION OF BUDGET POLICY STATEMENT

5. The unpacking of the supplementary budget has been undertaken using five-point criteria as follows:
    i. Comprehensiveness, Clarity and Credibility
    ii. Alignment to the National Development Agenda
    iii. Credibility of the Macroeconomic Framework
    iv. Linking Sector Priorities to Hard Budget Constraints
    v. County Resource Allocation

Criterion 1

Comprehensiveness, Clarity and Credibility:

This criterion assesses whether the document adheres to set down legal requirements and whether it provides all information required for Parliament to make an informed decision

6. The adequacy of the information provided in the Budget Policy Statement is assessed by querying eleven key items as outlined in the table below:

Table 1: compliance to legal provisions

	QUERY	OBSERVATION	LEGAL UNDERPINNING
1	Does the BPS provide a sound macroeconomic framework underlying fiscal policy over the medium term?	The BPS contains this information. A review of the macro framework is in section 3	PFM Act, 25(4)(a) PFM regulations 27(1) (c), 28 and NA. SO 232(2)
2	Does the BPS provide a medium-term fiscal framework in respect of revenues, expenditure and borrowing?	This is provided.	PFM Act, 25(4)(b) PFM regulations 27(1) (d), 29 and NA. SO 232(2)(a)
3	Does the BPS provide a summary of programmes that are of national interest for the forthcoming year?	This is information has been provided	PFM regulations 27(1) (f)
4	Does the BPS propose expenditure limits for the national government, Parliament and Judiciary and indicative transfers to county governments?	This Information has been provided.	PFM Act, 25(4)(c) PFM regulations 34 and NA. SO 232(2)(c)
5	Does the BPS indicate total resources to be allocated to individual programmes and projects and the outputs expected?	Information has been provided.	PFM Act, 25(4)(c) & NA. SO 232(2)(e)
6	Does the BPS contain a list of proposed projects and their respective expenditure ceilings, reconcilable to the total proposed ceilings for development expenditure?	Information not provided.	NA. SO 232(2)(f)
7	Does the BPS detail the criteria used to allocate or apportion the available public resources among the various programmes and projects?	Information has been provided.	NA. SO 232(3)

8	Has the National Treasury taken into account the resolutions passed by Parliament?	Some National Assembly resolutions were not adhered to.	PFM, 25(8)
9	Does the BPS contain a statement of its adherence to fiscal responsibility principles?	This information has been provided	PFM Act, 15 PFM regulations 26 and NA. SO 232(2)(c)
10	Does the BPS contain a statement of Fiscal Risks?	No information has been provided with regard to contingent liabilities as well as National Government pending bills	PFM regulations 27(2)
11	Has the principle of public participation been adhered to?	Public participation was undertaken.	Constitution Article 201(1 a), PFM Act, 25(9)

7. A critical review of the submitted document revealed that most of the information has been provided. However, there is some critical missing information such as information on National Government pending bills, State Corporation losses and outstanding payments, and budgetary expenditures by economic and functional classifications. The National Treasury and Economic Planning has also not submitted a list of proposed projects for the identified period with their respective expenditure ceilings that are reconcilable to the total proposed ceilings for development expenditure as required under National Assembly Standing Order 232 (2) (e).

8. It is noted that according to PFM regulations 27(5), the ceiling for development expenditure and personnel spending of the national government budget approved by Parliament should be binding for the next two budget years. However, this has never been adhered to. Going forward, Parliament may consider enforcing this regulation for the sake of predictability in development spending.

Criterion 2

Alignment to the National Development Agenda

This criterion evaluates the policies underpinning the Budget Policy Statement and whether they are aligned with the medium-term policy and strategic priorities of the government as provided for in the policy documents.

9. **The National Development Agenda is predicated on the Kenya Kwanza Manifesto, the Vision 2030 and the African Union Agenda 2063.** The Manifesto endeavours to adopt a bottom-up approach to economic transformation. The Vision 2030 seeks to transform the country to a middle-income status by 2030 and is implemented through five-year Medium-Term Plans (MTP). The AU Agenda 2063 envisages realization of Africa's full potential in development, culture and peace and to establish flourishing, inclusive and prosperous societies.

10. This BPS has been developed at the sunset of the third medium term plan but before the finalization of the fourth MTP that is supposed to provide anchorage to the annual development plans outlined in BPS. Both the Vision 2030 and the AU Agenda 2063 are cognizant of the role of the key pillars defined in the BPS in economic transformation.

11. **The Budget Policy Statement is anchored on five pillars and twelve enablers that are broadly expected to contribute to six broad objectives.** These pillars include Agriculture, MSME Economy, Housing and Settlement, Healthcare, and Digital and Creative Economy. The choice of these sectors as the key pillars is informed by their potential to turnaround the economy given their impact on growth, household welfare and their interlinkages with other sectors. The enablers to the turnaround strategy include Infrastructure; Manufacturing; Blue Economy; the Services Economy, Environment and Climate Change; Education and Training; Women Agenda; Social Protection; Sports, Culture and Arts; and Governance.

12. **Prioritization of pillars and enablers has been based on sectors with huge potential** to significantly impact the majority of the population with the least initial investment requirement given the prevailing resource constraints. The identified pillars and enablers are broadly expected to contribute towards six strategic objectives including lowering the cost of living, creating employment opportunities, eradicating hunger, improving fiscal space, increased foreign exchange earnings, and inclusive growth.

13. **The Budget Policy Statement has alluded to a sequencing criterion based on the timeframe for the impacts to be felt**. This ranges from quick wins that take up to six months, short-term that take up to 18 months, medium-term that take up to 36 months, and long-term those whose impact takes over 36 months to materialize. Whereas this is plausible, the same has not been reflected in specific policy pronouncements. Looking at specific commitments, they are neither ranked in any order of priority nor sequenced as proposed. It's not therefore possible to group or cluster the policies in terms of the sequencing criteria.

Pillar 1: Agricultural Transformation and Inclusive Growth

14. **The Vision 2030 clearly outlines the place of Agriculture as an engine of growth.** More specifically it expounds on critical interventions such as expanding land under irrigation, three tier approach to fertilizer cost reduction including manufacturing it locally, enhancing production and productivity, value addition and realization of disease-free zones to promote livestock-based value chains.

15. **The MTP3 of the Vision 2030 under the Big Four Agenda sought to achieve 100 percent food and nutrition security by the year 2022.** However, despite the interventions proposed therein, the country is facing one of the most severe food insecurities in recent times. This is manifested both in food affordability and availability.

16. **The African Union Agenda 2063 underlines the need to consolidate the modernization of African agriculture and agro-businesses.** This is to be achieved through scaled up value addition, increased productivity, and economically empowering women and youth by enhancing access to financial resources for agricultural investment. This is expected to contribute to eradication of hunger, create employment opportunities and enhance self-reliance and independence of the African Nations.

17. The Policy pronouncements and proposed interventions under the BPS are in line with the Kenya Kwanza Manifesto and also seek to address the aspirations of the Vision 2030 and AU Agenda 2063. **While the convergence of ideology on what needs to be done is welcome, the implementation of previous interventions has not borne much of the desired outcomes**. The proposed interventions majorly seek to enhance irrigable land, access to affordable working capital, access to inputs and extension services and deployment of modern risk management tools. This will in turn raise productivity, reduce dependence on imports and increase farmer incomes.

18. **Previous efforts in this endeavour include the farm input subsidy programme through the E-voucher programme that has not been fully implemented**, the crop and livestock insurance programmes that have also not been fully realized as well as efforts to bring more farmland under irrigation have also been hampered including the Galana-Kulalu project. Before new initiatives and approaches are fully adopted, there is need to unravel the bottlenecks that have hindered success of previous similar interventions. Some of the proposed interventions on along the value chains do not comprehensively address the underlying bottlenecks.

19. **The Budget Policy Statement has not highlighted specific interventions on reduction of post-harvest losses**. According to FAO1, Kenya loses on average about 30-40% of its agricultural produce in post-harvest losses due to spillage and degradation during handling, storage, and transportation between farms and distribution to markets. The BPS has only highlighted provision of bulk milk coolers under the dairy sub sector and not for other critical value chains.

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[1] Food Loss Assessments: Causes and Solutions Case Studies in Small-scale Agriculture and Fisheries Subsectors in Kenya. FAO 2014.

Post-harvest losses are unique in that they represent an expense already incurred by farmers but doesn't contribute to their overall welfare.

20. **The Vision 2030 proposes the development of the Agricultural Land Use Master Plan to address the shortcomings of the current land tenure system**. However, the BPS has not given the strategic direction on land tenure system. The post-independent land tenure system gives exclusive user rights to the land owners. Elaborate residential and business investments set up near urban centres have progressively taken up agricultural land, with no foreseeable end to this phenomenon. The culture of intergenerational transfer of land through sub-division has also aggravated the land problem. Without sorting out the land issue, mechanization and intensive agricultural practices may remain a mirage.

Pillar 2: Transforming the Micro, Small and Medium Enterprise Economy

21. **The MSME economy presents one of the most underutilized resources in the country that can turnaround the economy.** To optimize on the sector, the BPS proposes to improve business environment for MSMEs, promote access to affordable finance, rationalize business licensing and taxation processes and establishment of business development centres. Whereas these proposals are plausible, the focus on MSME is not new.

22. **Since independence, every administration has put in place some policy measures to promote MSME development.** The Sessional Paper No. 10 of 1965 on African Socialism and its application to planning in Kenya vouched for the decentralization of economic power through local capital formation to enhance indigenous business enterprises. The Vision2030 identified development of MSME industrial parks as flagship projects to foster manufacturing. More recent efforts include the enactment of the Micro and Small Enterprise Act that among others established the Micro and Small Enterprises Authority, Micro and Small Enterprises Development Fund, Micro and Small Enterprises Tribunal, Registrar of Micro and Small Enterprises, and Micro and Small Enterprises Infrastructure Development. Therefore, most of the interventions in the BPS are enshrined in the provisions of MSE Act.

23. **Previously, more emphasis has been put on the manufacturing arm leaving out some critical actors within the MSME continuum.** This is the case for MTP3 of the Vision 2030 and also the AU Agenda 2063 that commits to developing the African private sector through engagement and a conducive climate, fostering Pan-African businesses through the growth of regional manufacturing hubs and scaled up intra-Africa trade. The move to recognize the broader MSME may play a vital role in formalization of the informal sector

24. **The BPS has not provided an elaborate strategy to align and mainstream coordination of various actors for better need targeting.** For instance, Kenya Industrial Estates undertakes construction of industrial estates/incubators; Micro and Small Enterprises Authority has been constructing and equipping Constituency Industrial Development Centres. It has so far constructed over 160 CIDCs with most yet to be equipped. The NG-CDF in partnership with Telcom Kenya has been establishing Constituency Digital Innovation Hubs. This is just to indicate the level of duplication of functions in the MSME arena. The multiplicity of institutions and interventions has brought more confusion than light to the sector.

25. **The BPS has further committed to a conditional grant to the county governments towards establishment of aggregated industrial parks**. An allocation of Ksh. 100 million per county has been provisioned in FY 2023-24. This may require further interrogation given previous performance of conditional grants such as the leasing of medical equipment scheme.

26. **There are several government-backed funds that are designed to support various categories of MSMEs.** The BPS proposes to enhance access to affordable finance through SACCOs, venture capital, equity funds, and long-term debt for start-ups and growth-oriented SMEs through the recently launched Financial Inclusion Fund among other interventions. Other closely related funds include the Youth Enterprise Development Fund, Women Enterprise Development Fund, Uwezo Development Fund, Micro and Small Enterprises Development, and the Credit Guarantee Scheme that is all geared toward enhancing access to affordable financing for various categories of MSMEs.

27. **However**, these ***efforts towards affordable financing have remained disjointed and operating in silos, limiting their potential impacts. The BPS has not indicated any fundamental distinction from the existing funds nor the complementarity mechanism that will be undertaken to leverage the shortfall of these previous efforts.*** Previously, there have been efforts to merge these interventions into one single Biashara Fund, while this proposal was commendable it also did not see the light of day.

Pillar 3: Housing and Settlement

28. **The AU Agenda 2063 aspires to provide access to affordable and decent housing to all in sustainable human settlements**. Equally, the Vision 2030 envisages an adequately and decently housed Nation in a sustainable environment. The medium-term plan for 2012 was to increase annual production of housing of housing from the then 35,000 units to 200,000 units per annum. However, up to date, the annual production of housing units as per KNBS still stands at around 50,000 units.

29. **The BPS proposes to close the housing gap by facilitating delivery of 250,000 houses per year**. This is to be achieved by restructuring affordable long-term housing finance scheme to guarantee off take of houses from developers thereby growing the number of mortgages from 30,000 to 1,000,000 by enabling low-cost mortgages of Ksh 10,000 and below. There will also be efforts to build linkages with the Juakali sector to enhance job creation.

30. **The BPS only alluded to alleviating the financial constraints without addressing other challenges on affordable housing** The real estate sector in Kenya has its share of challenges that have hindered the achievement of the sought affordable housing units. These include those related to land acquisition process, cost of construction materials, quality of construction works and inadequate support infrastructure.

31. **Affordable housing was one of the pillars of the big four agenda, which sought to deliver 500,000 affordable housing units between 2017-2022**. However, the pillar was able to deliver less than 5000 units partly due to low budget allocation. The government has previously put in place several interventions for homeowners and property developers to enhance home ownership, but little progress has been made. These interventions range from tax incentives, waiver on imported materials for the affordable housing program, and

operationalization of Kenya Mortgage Refinancing Company to enhance access to mortgages among other interventions. There is need for a comprehensive framework that brings into play the county governments in delivery of this pillar.

Pillar 4: Healthcare

32. **The BPS is cognizant that a healthy population translates to a healthy nation**. This is in line with Vision 2030 that envisages an efficient and high quality healthcare system based on preventive rather than curative approaches. The pillar is even more important in the wake of the Covid-19 pandemic which has demonstrated that even the most advanced healthcare systems can easily be overwhelmed by unforeseen emergencies and as such the need to continuously strengthen the resilience and coverage of healthcare services.

33. **The BPS proposed interventions include reforming the National Hospital Insurance Fund from an occupational scheme to a social security scheme.** The accruing benefits will be based on household contribution rather than individual contributions. Other proposals include improvement of procurement of medical supplies, expansion of healthcare infrastructure, deployment of state-of-the-art medical information management system and centralized human resource management system in conjunction with County governments.

34. This will further be achieved through employment and payment for community healthcare workers. More specifically, recruitment of additional 20,000 medical professionals, establishment of emergency cancer treatment fund, Ksh. 50 billion for retired officers' medical scheme, Ksh. 100 billion towards cofunding strategic programmes for HIV, TB, Malaria, blood transfusion, family planning and reproductive health.

35. **The Vision 2030 has also underlined the need for an efficient and affordable healthcare system for improved livelihoods**. This was envisaged to be achieved through shifting of the healthcare focus from curative to preventive. The Vision notes the need for revitalization of community healthcare centres, development of an inclusive national health insurance system and proper management of healthcare professionals. This was further amplified through MTP3 under the Big four agenda on provision of universal healthcare.

36. **The role of human resource management in the healthcare sector is a devolved function** while the national government offers the overall policy guideline and coordination. However, the BPS commits to prioritizing the recruitment of additional healthcare workers to strengthen healthcare service delivery. It has not alluded to the envisaged implementation modalities.

Pillar 5: Digital Superhighway and Creative Economy

37. **The final pillar of transformation in the 2023 BPS is Digital Superhighway and Creative Economy**. The pillar has proposed a number of measures including expanding broadband connectivity by over 100,000 KMs, Automation of Government services by revamping the huduma services, developing of business process outsourcing (BPO) industry, promoting software development for export, and reducing the cost of data and calls among others.

38. **This pillar is viewed as an enabler of delivering other interventions efficiently and effectively**. The pillar consists of two components; on one hand, is the digital superhighway that constitutes the requisite infrastructure and support systems, and on the other, the human

ingenuity, talents, and creativity in the realm of arts, filmmaking, and music among others. Some interventions are to be realized in collaboration with the county government but it is not elaborate how they are integrated to the County Development plans.

39. This is in line with the vision 2030 that is cognizant of the role of science, technology and innovation in enhancing national development. More specifically, the vision 2030 notes the need to mainstream information technology in delivery of government services as well as availing the requisite infrastructure to support private businesses that are reliant on internet broadband. **The BPS has not provided for policy direction on revitalization and maintenance of the aging national infrastructure as well as coordination with the sub national government on interventions to be undertaken at the county level**.

Enablers

40. The BPS provides an extremely detailed account on the various interventions within the enablers, namely Infrastructure; Manufacturing; Blue Economy; the Services Economy, Environment and Climate Change; Education and Training; Women Agenda; Social Protection; Sports, Culture and Arts; and Governance. However, while extremely detailed, it is noted that most of these interventions are broadly stated and not very specific in nature.

41. **The location and intended beneficiaries of many of the interventions are not clearly stated and the implementation framework isn't very clear**. The specifics of implementing the plan will perhaps be clearly elucidated with the finalization of the Medium-Term Plan 4 which is expected to be the anchor document for the Bottom-up Economic Transformation Agenda (BETA). The government should therefore move with speed to finalize the MTP IV in order for the missing links to be made clear including resource framework, implementing units, targeted beneficiaries, key outputs and timelines.

42. **The value chains and value chain approach proposed in the BPS is conceivable, however, it falls short of an elaborate and logical implementation framework**. The value chain approach is ideally based on a logical framework that envisages all the stages from pre-production to value addition and the marketing stages. The proposed interventions are not expressly structured out and aligned to the specific stages, as such, if some bottlenecks are not addressed at one stage of the value chain, that may result to collapse of the entire value chain rendering the rest of the interventions futile.

Criterion 3

Credibility of the Macroeconomic Framework

This criterion considers the quality of assumptions underpinning the macroeconomic outlook and the credibility of the numbers/outlook for the macro variables. It considers assumptions underpinning the fiscal policy outlook and assesses their credibility.

Economic Growth

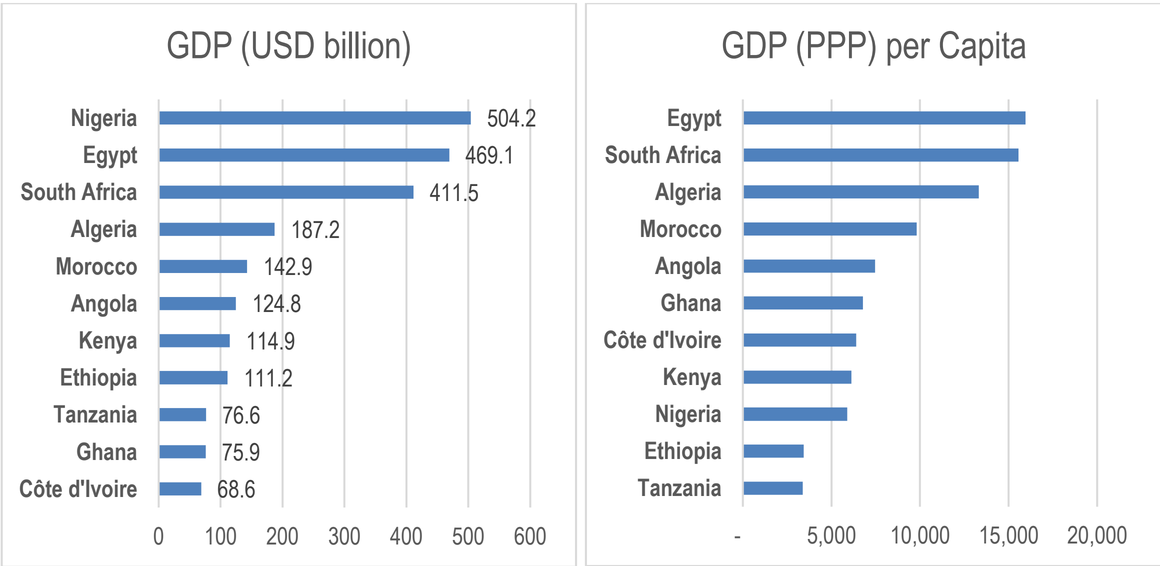
43. **African economies are estimated to grow at an average of 4.0 percent in 2023 which is higher than the global average of 2.9 percent.** This is an improvement from 3.8 percent for the African economies and a decline from 3.4 percent for the global economy in 2022. The positive outlook for Africa[2] is anchored on favourable commodity prices; restored security in oil-producing countries such as Nigeria; anticipated peaceful elections to be held in 2023 by 10 African countries; a steady outlook for Asia which will ignite a favourable market as it accounts for 40 percent of Africa's merchandise exports and rising demand for Africa's natural resources such as minerals, renewable energy and foodstuffs as advanced economies implement pro green economic initiatives.

44. **The downside risks to the positive outlook include climate change related extreme weather conditions such as drought and floods.** This may be compounded further by weak domestic demand; insecurity in the Horn of Africa; weaker exchange rate to the US Dollar that will affect net-importing countries and high interest rates that would increase the risk of debt distress for some African countries.

45. **Kenya is the 7th largest African economy in terms of Gross Domestic Product (GDP).**[3] In 2022, the largest economy was Nigeria (USD 504.2 billion) followed by Egypt (USD 469.1 billion). However, in terms of GDP at purchasing power parity per capita, which is the GDP divided by a country's population and adjusted for cost of living, Egypt had the highest followed by South Africa as illustrated in Figure 1.

[2] "Africa's Macroeconomic Performance and Outlook" January 2023 by the African Development Bank
[3] IMF's WEO Database, October 2022

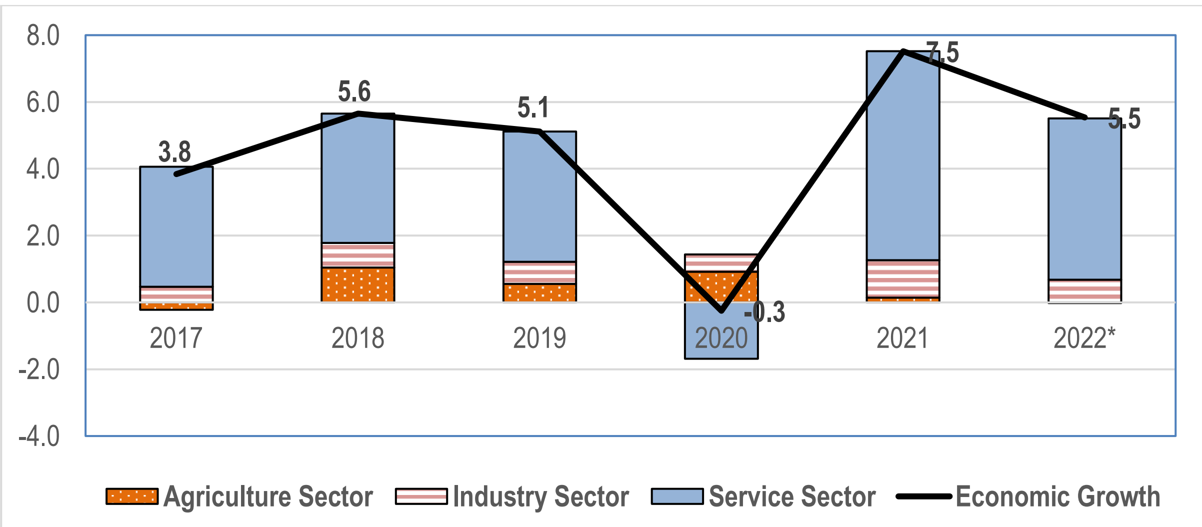
Figure 1: Cross-country comparison of selected African Countries in 2022



Source: IMF

46. **The 2023 Budget Policy Statement projects that the Kenyan economy will grow by 6.1 percent in 2023 from an estimated growth of 5.5 percent in 2022.** In terms of fiscal years, the economic growth is projected at 5.8 percent in the FY 2022/23 and 6.1 percent in the FY 2023/24. This growth will be supported by private sector growth, recovery in agriculture sector, labour market recovery, improved consumer confidence and resilient remittances.

Figure 2: Trend in Contribution to Economic Growth (%)



Source: KNBS

*Average for 9 months

47. **The Service Sector[4] has been driving the economy indicating a continued shift from agricultural activities to services depicting Kenya's status as a lower middle-income country with a rising middle-class.** The contribution of the service sector to economic growth has expanded in the past decade except for 2020 when the Covid-19 restrictions set-back activities in the sector. However, the economy rebounded from the effects of the pandemic, recording a growth of 7.5 percent in 2021 (Figure 2). Notably real estate and finance & insurance activities displayed a consistent increase in the share of real GDP.

48. This infers continued expansion in the financial and insurance activities enabled by mobile banking where the value of mobile money transactions increased from Kshs. 3.4 trillion in 2016 to Kshs. 6.9 trillion in 2022[5]; online transactions; block chain technology and other financial innovations. In addition, the real estate continued to expand to meet the demand of the middle-class households. For instance, the actual value of residential building plans approved increased from Kshs. 75.2 billion in 2012 to 100.7 billion in 2022, while the actual value of non-residential buildings declined from Kshs. 115.2 billion to Kshs. 29.8 billion during the same period.

49. **The agriculture sector continued to contract in 2022 depicting the challenges facing this sector which is mainly weather reliant**. The sector recorded a -0.9 percent for the three quarters of 2022 as the country continues to experience drought. According to the Famine Early Warning Systems Network, the country is experiencing its 5th consecutive season of below average rainfall and has drastically affected the availability of water and forage for livestock and reduced crop production. According to the Kenya Bureau of National Statistics, there was a decline in the growth of vegetable exports in metric tonnes by -5.6 percent and coffee exports in metric tonnes by -30.3 percent during the third quarter of 2022.

50. **The Budget Options for 2023[6] discusses in depth options available for the agriculture sector that can be funded through the budget.** Some of the non-weather-related challenges affecting the agriculture sector include lack of access to quality farm inputs such as seeds and fertilizers especially for the small-scale farmers; poor farming methods as farmers use the wrong quantity of fertilizers; high post-harvest losses; limited access to financing. The options to revitalize the sector include

- Allocation of Ksh. 15 billion for the agricultural input subsidy programme to target 200,000 MT of subsidized fertilizer and other assorted farm inputs;
- Restructure the e-voucher input management system to achieve efficiency and effectiveness in the supply of farm inputs;
- Allocation of Ksh. 1.5 billion for the provision of extension services- counties to employ agricultural extension officers given that it is a critical tool for improving productivity;
- Allocation of Ksh. 300 million to ensure the full implementation and operationalization of the Warehouse Receipt Systems;

[4] Consists of Wholesale & retail trade; Transport & storage; Accommodation & food service; Information & communication; Financial & insurance; Real estate; Education; Human Health & social work; Public administration & defence; Education; Professional, scientific & technical activities; other activities

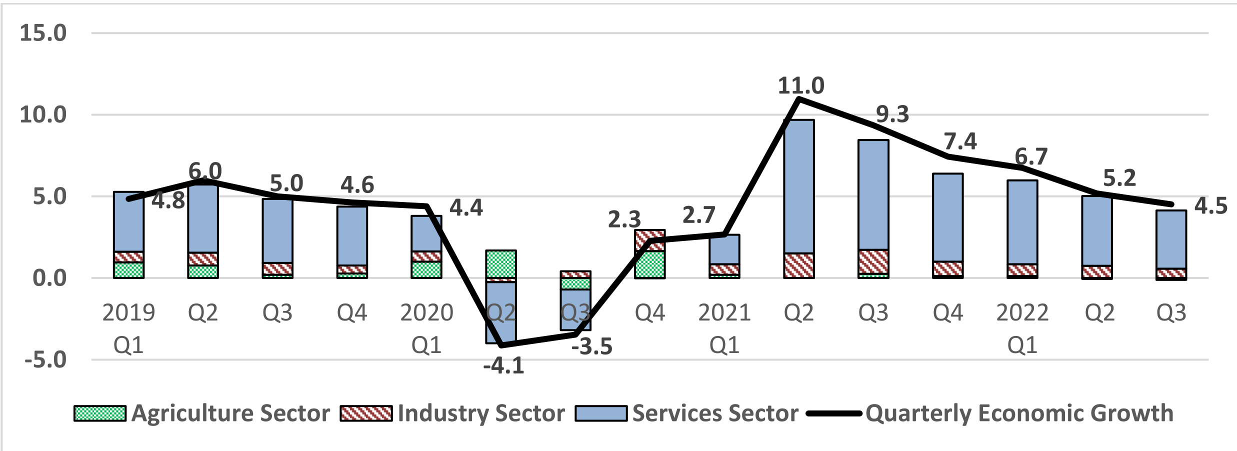
[5] Data available up to September 2022

[6] A publication by the Parliamentary Budget Office- Kenya

- Provision of Ksh. 200 million for procurement of mobile grain driers or grain drying centres and cold storage systems at the community level and especially where WRS is not accessible. Farmers can be organized into groups for the operation and management of these facilities;
- Provision of Ksh. 7.2 billion as credit or working capital to farmers through well-managed farmer organizations or cooperatives. The actualization of the warehousing receipt system will also play a critical role in credit provision;
- Allocation of Ksh. 3 billion to be provided as a subsidized loan product specifically designed for the production of key food staples for the Strategic Food Reserve.

51. **The economy is moving back to precovid-19 as portrayed by the trend of quarterly economic growth which has consistently declined from 9.3 percent in the 3rd quarter of 2021 to 4.5 percent in the 3rd quarter of 2022.** The decline was persistent in the Agriculture and Industry sectors due to the negative effects of drought. For instance, milk intake reduced from 209.3 million litres in 3rd quarter of 2021 to 187.0 million litres in a similar period in 2022. The service sector also remained stable supported by activities in ICT, evident by increased internet and mobile services; accommodation and restaurants evident by increased visitor arrivals and transport and storage where there was growth in the number of passengers and freight transported by SGR.

Figure 3: Contribution to Quarterly Economic Growth 2019 -2022



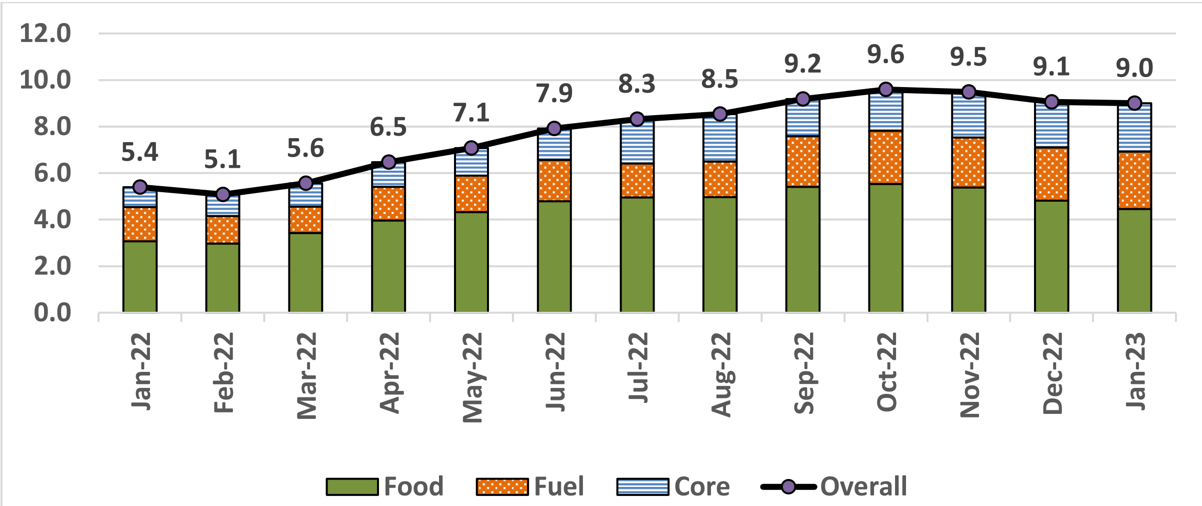
Data Source: KNBS

52. **The high growth of 6.1 percent envisaged in the 2023 Budget Policy Statement will be achieved in a scenario that focuses more on fiscal consolidation, investment in Agriculture and MSMEs in line with BETA.** These two sectors are ranked as priority sectors that have the potential to increase household income that will support increased private consumption and savings hence economic growth. Given that the government plans to undertake fiscal consolidation, it would mean a reduction of spending in non-priority areas of the budget. **On the other hand, a lower growth of 5.3 percent in 2023 would be achieved in a scenario that depicts, continued external shocks, drought conditions and ignores fiscal consolidation plans.** This implies continued emergency responses to drought; depleting foreign exchange reserves as a cushion to exchange rate shocks; increased cost of living as food prices continue to rise and tight global financial conditions that weaken domestic demand.

Inflation

53. **Inflation stood at 7.6 percent in 2022 from 6.1 percent in 2021 implying a rise in the cost of living.** Inflation persistently increased from 5.4 percent in January 2022 to 9.0 percent by January 2023, remaining above the upper target of 7.5 percent. The increase was on account of a rise in food inflation as prices of food increased emanating from supply shocks from below-average rainfalls that affected food production. In addition, the depreciating Kenyan Shilling to the USD resulted in increased prices of imported food items. Fuel inflation also remained high despite the decline in international oil prices (MURBAN-ADNOC) from 117.7 USD in June 2022 to 81.6 USD per Barrel in January 2023, pointing to lagged periods of oil imports coupled by exchange rate effect of a stronger USD. In addition, the end of the fuel subsidy meant that pump prices remained elevated for the better part of the year as the oil marketers recouped their investment. Indeed, high inflation has resulted in high cost of living that detrimentally affects the low-income households where in most cases it is not matched by an increase in wage earnings.

Figure 4: Trend in Contribution to Overall Inflation



Source: KNBS, PBO

54. **Core inflation has been on an upward trajectory from 2.1 percent in January 2022 to 5.1 percent by January 2023 because of underlying cost-push factors.** This is an indication that other than the main drivers of overall inflation arising from food and fuel, there has been a significant push in other components whose contribution to inflation has increased such as Restaurants & Accommodation Services; Furnishings & Household Equipment; Personal Care & Social Protection; and Recreation, Sports and Culture. This is likely from spill-over effects of a weakening Kenyan Shilling that results in higher cost of imported goods and services.

55. **Going forward, the outlook for overall inflation is that it is likely to remain high but decline towards the upper target of 7.5 percent in 2023.** The decline will be supported by continued lower international crude oil prices which will in turn lower fuel inflation; the easing of the US monetary stance could also lessen the exchange rate impact on imported food prices and

non-food commodity prices are projected to decline globally in 2023[7]. However, owing to the prevailing effects of the drought and expected below average rainfall for the long-rain season (March- May 2023), the inflation target of 5.8 percent for 2023 in the BPS may not be achieved.

Table 2: Contribution to overall Inflation from various categories

Category	**Jan 22**	**Feb 22**	**Mar 22**	**Apr 22**	**May 22**	**Jun 22**	**Jul 22**	**Aug 22**	**Sep 22**	**Oct 22**	**Nov 22**	**Dec 22**	**Jan 23**
Food & Non-alcoholic Beverages	57.0	58.6	61.7	61.2	61.0	60.6	59.5	58.3	58.9	57.6	56.8	53.2	49.5
Alcoholic Beverages, Tobacco & Narcotics	2.2	2.2	2.2	1.9	1.8	1.6	1.6	1.8	1.8	2.5	2.7	2.7	3.1
Clothing & Footwear	1.2	1.3	1.1	1.0	0.9	0.9	0.8	0.8	0.9	0.9	0.9	1.1	1.1
Housing, Water, Electricity, Gas and other Fuels	14.5	14.3	13.6	12.2	13.1	13.3	9.7	9.5	12.3	11.5	10.0	10.6	12.5
Furnishings, Household Equipment and Routine Household Maintenance	3.6	4.1	4.5	4.1	4.4	4.6	4.3	4.5	4.6	4.5	4.4	4.3	4.1
Health	0.5	0.5	0.6	0.5	0.4	0.3	0.4	0.5	0.5	0.5	0.6	0.6	0.7
Transport	12.8	9.0	6.7	10.2	9.2	9.1	8.0	8.5	11.4	12.4	12.6	14.7	14.9
Information & Communication	3.8	4.0	3.5	2.9	2.8	2.5	8.3	8.1	0.8	0.9	1.0	1.0	1.0
Recreation, Sports & Culture	0.2	0.3	0.4	0.3	0.7	0.7	0.6	0.6	0.7	0.7	0.8	0.9	1.1
Education Services	1.1	1.0	0.9	0.8	0.8	0.8	0.7	0.6	0.6	0.6	0.8	0.8	1.4
Restaurants & Accommodation Services	0.3	2.1	2.3	2.8	2.7	3.2	3.8	4.3	4.5	4.8	5.6	6.1	6.2
Personal Care, Social Protection and Miscellaneous Goods & Services	2.4	2.4	2.4	1.8	2.0	2.1	2.2	2.5	2.8	3.0	3.5	3.7	3.9
Insurance and Financial Services	0.3	0.2	0.2	0.2	0.1	0.1	0.1	0.1	0.1	0.1	0.3	0.3	0.3
TOTAL	100	100	100	100	100	100	100	100	100	100	100	100	100
Inflation Rate	**5.4**	**5.1**	**5.6**	**6.5**	**7.1**	**7.9**	**8.3**	**8.5**	**9.2**	**9.6**	**9.5**	**9.1**	**9.0**

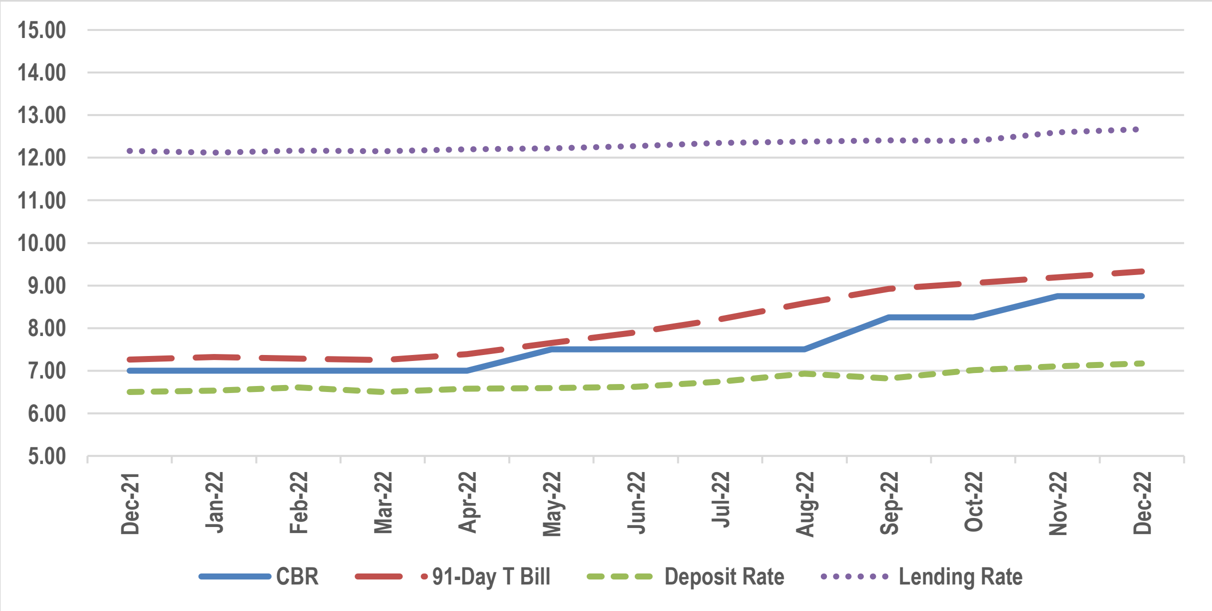
Source: PBO, KNBS

[7] IMF's World Economic Outlook update January 2023

Interest Rates and Credit

56. **The CBR rate rose from 7 percent in November 2021 to 8.75 percent in November 2022 and remained unchanged as of January 2023, illustrating a tightening of the monetary policy by the Central Bank aimed at subduing inflation.** The 91-day T-Bill rate rose from 7.3 percent in January 2022 to 9.5 percent in January 2023 indicating a high cost of short- term domestic borrowing. The lending rate remained stable but the rates have been rising slowly from 12.2 percent in December 2021 to 12.7 percent in December 2022, which indicates a slight rise in the cost of borrowing by individuals. The deposit rate on the other hand rose from 6.5 percent in December 2021 to 7.2 percent in December 2022 indicating that the return for individuals saving with banks is increasing. As a result, the interest rate spread declined from 5.7 percent in December 2021 to 5.5 percent in December 2022.

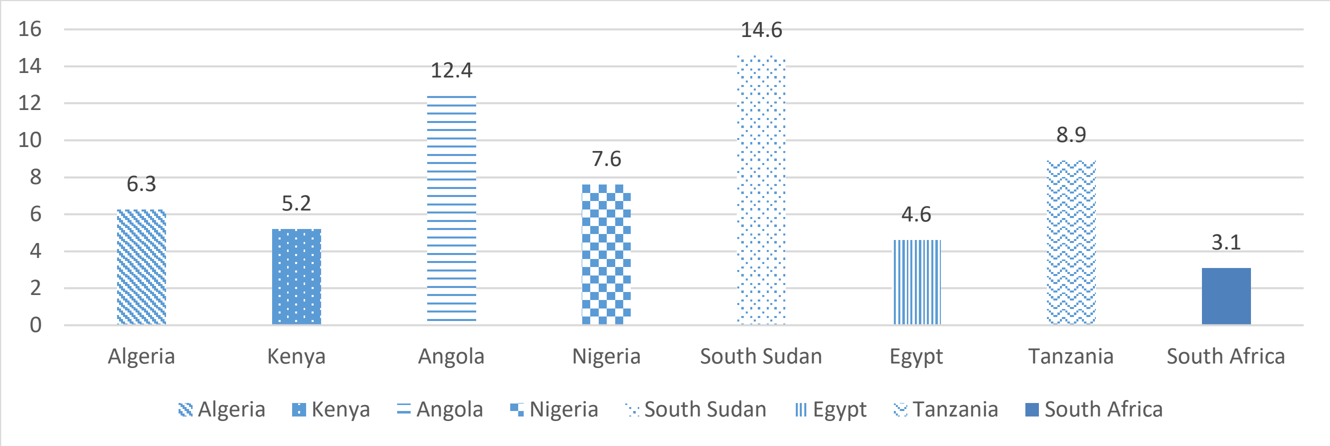
Figure 5: Trend in selected interest rates



Data source: Central Bank of Kenya

57. **The average interest rate spread for Kenya for the past five years was 5.2 percent which is relatively low compared to other selected African countries.** Countries such as South Sudan and Angola had double-digit interest rate spread of 14.6 percent and 12.4 percent respectively implying that their banks earn a high profit margin on loans given to borrowers relative to the deposit rate charged for obtaining funds from borrowers. For banks to operate efficiently, they should obtain funds at relatively low rates from depositors but also lend to borrowers at relatively low rates. Lower interest rate spreads are therefore considered favourable.

Figure 6: Average Interest rate spread for selected African Countries

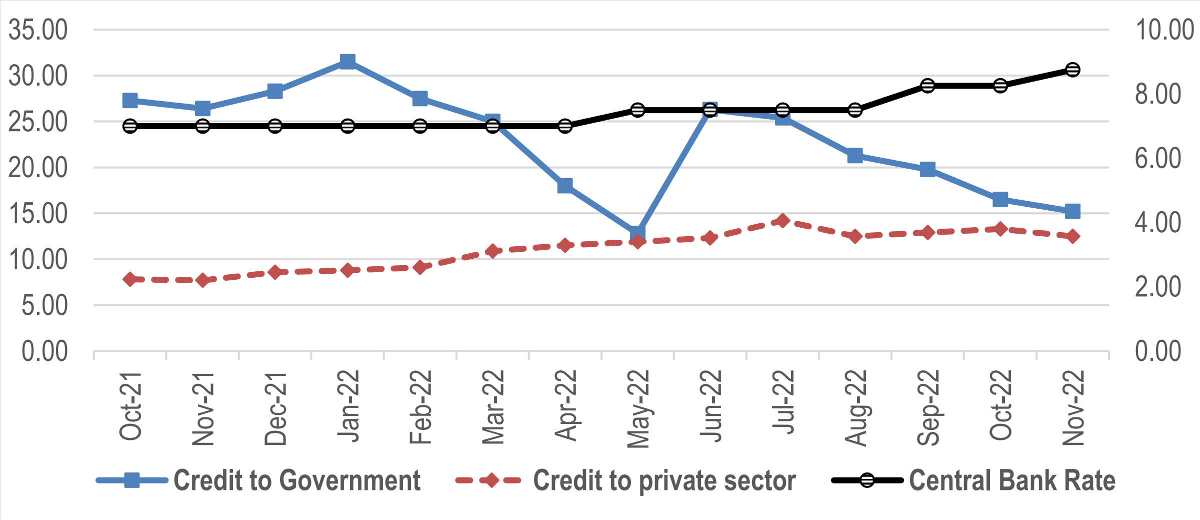


Data Source: World Bank

58. **Credit growth indicates a gradual shift from Government to the Private Sector as the Central Bank of Kenya raised the Central Bank Rate to anchor inflationary pressures.** Credit to Government declined significantly from 31.5 percent in January 2022 to 15.2 percent in November 2022 while credit to private sector increased from 8.8 percent to 12.5 percent during the same period. This is a favorable indication that the private sector credit has not been crowded out by the government and it also implies that the government is accumulating less debt from the domestic market. The demand for credit in the private sector was particularly high in mining, transport and communication, agriculture, manufacturing, business services, trade, and consumer durables sectors. Going forward, the credit growth to the private sector is expected to rise in 2023 with the Central Bank Rate remaining unchanged as inflation is projected to decline.

59. **Money supply grew from 6.1 percent in December 2021 to 7.2 percent in December 2022 on account of growth in the Net Domestic Assets occasioned by growth in lending to the private sector.** This is an indication that the demand for credit by the private sector is increasing as economic activity improves. Credit to the government declined as well as lending to other public sector. The BPS highlights that this is due to repayments by county governments and parastatals. Notably, there was a decline in Net Foreign Assets and this is attributed to a reduction in reserves at the Central Bank due to scheduled debt service as well as an increase in commercial bank borrowing from foreign sources.

Figure 7: Trend in Central Bank Rate and growth in Credit (%)



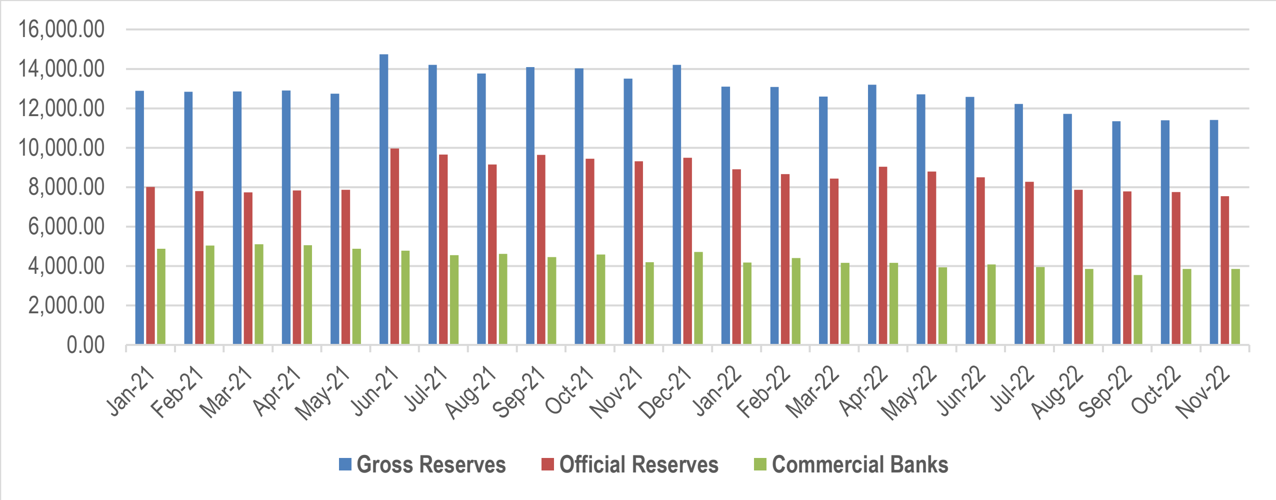
Source: CBK

a) External Sector

60. **The overall Balance of Payments improved from a deficit of USD 976.8 million in November 2021 to a surplus of USD 2.2 billion in November 2022.** The capital account improved from USD 196.1 million to USD 1.3 billion. This indicates an improvement in the capital inflows in the country. The current account improved from a deficit of USD 5.8 billion to deficit of USD 5.7 billion supported by recovery in international travel in the services account and the diaspora remittances in the secondary income. Notably, the merchandise goods account worsened in this period as a result of a high import bill majorly caused by an increase in the prices of crude oil in the global market. On the other hand, the financial account slightly declined from USD 6.7 billion to USD 6.6 billion as a result of a decline in portfolio investments.

61. **Foreign reserves proxied by months of import cover breached the target of 4 months by the second week of February 2023 and stood at 3.84 months. Reserves declined from 5.6 to 4.2 months of import cover from November 2021 to November 2022.** The BPS highlights that the foreign exchange reserves are strong and the months of import cover were above the threshold of 4 months. However, the months of import cover have also been on a declining trend in the period under review. The foreign exchange reserves declined from USD 13.5 billion in November 2021 to USD 11.4 billion in November 2022. Official reserves held by the Central Bank declined from USD 9.3 billion to USD 7.5 billion while reserves held by the commercial banks declined from USD 4.1 billion to USD 3.8 billion.

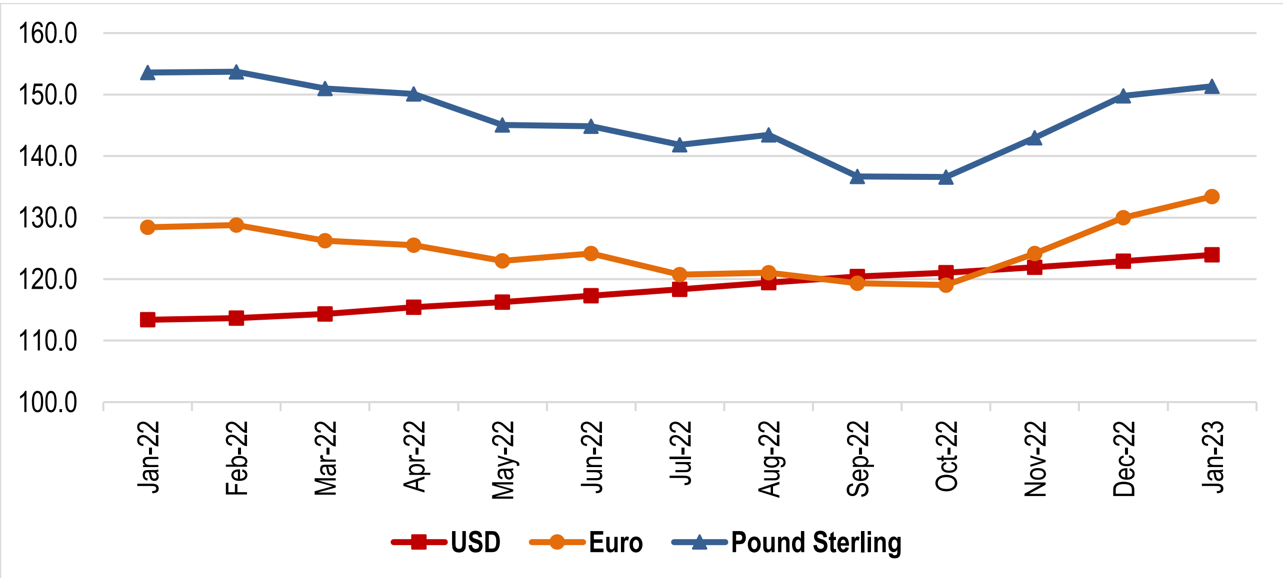
Figure 8: Foreign Exchange Reserves



Data Source: Central Bank of Kenya

62. **The BPS notes that the foreign exchange market has remained stable despite the strengthening of the US Dollar and uncertainties regarding the Russia-Ukraine War which led to the depreciation of most currencies against the dollar.** The Kenya shilling depreciated against the US Dollar from 113.4 in January 2022 to 123.9 in January 2023. This was occasioned by a scarcity of the US Dollar due to the Federal Reserve's monetary policy stance of raising interest rates to tackle inflation. As a result, most countries experienced capital flight and in the case of Kenya, this was also coupled by a deterioration of the foreign exchange reserves in this period. The outlook for the remainder of the financial year is a rise in the USA Federal Reserve policy rate, which is likely to ease a further weakening of the Kenyan Shilling to the US Dollar.

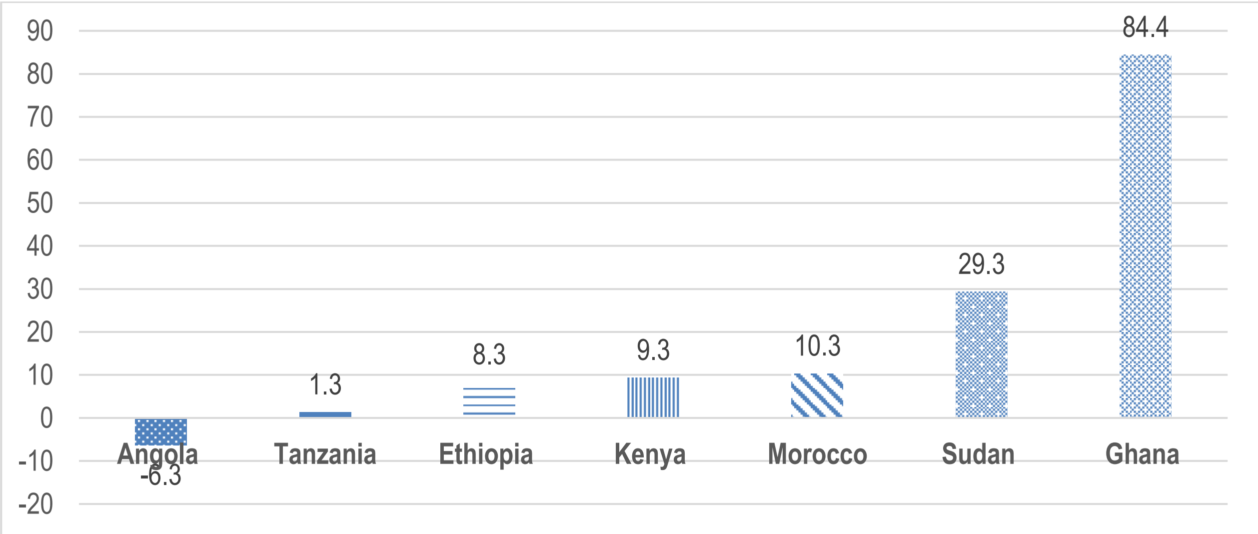
Figure 9: Trend in Kenyan Shilling Exchange Rate



Source: Central Bank of Kenya

63. In comparison with other selected African countries, the depreciating shilling performed better than the currencies of Morocco, Sudan and Ghana against the US Dollar. Notably, the Kenyan Shilling has been sustained by diaspora remittances from Kenyans living abroad which have been increasing over time.

Figure 10: Performance of Selected Currencies against the US Dollar from January 2022-January 2023.



Source: World Bank

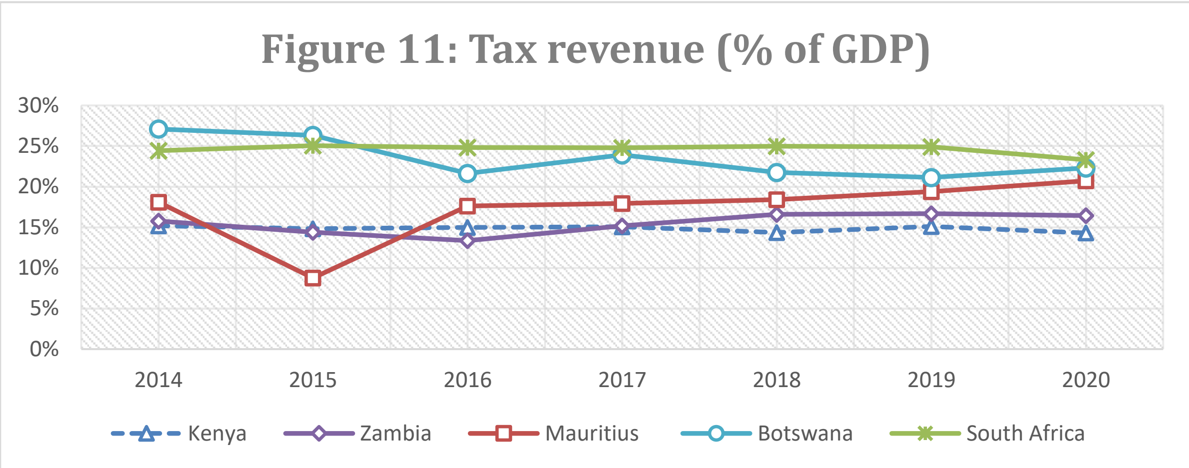
Criterion 4

Linking Sector Priorities to Hard Budget Constraints

This criterion reviews the fiscal framework and considers whether the priority areas identified in the BPS have been reasonably funded within the hard budget constraints

Fiscal Framework for FY 2023/24 and the Medium Term

64. **Kenya's ordinary revenue collection as a share of GDP has stagnated at around 15 percent over the last decade.** Tax policy measures that have been included in previous Budget Policy Statements have failed to expand the tax base and enhance revenue collection relative to economic output. Consequently, Kenya has lagged behind other comparable African countries whose tax revenue collection is between 20 percent and 25 percent.



Source: World Development Indicators (Last updated 22/12/2022)

65. **The National Treasury expects to expand ordinary revenue collection as a share of GDP from the preliminary actual of 15.0 percent in 2021/22 FY and projected 15.1% in 2022/23 to 15.8% in 2023/24.** To achieve this the government has undertaken to finalise the development of the National Tax Policy Framework and the Medium-Term Revenue Strategy (MTRS) which will provide a comprehensive approach to undertaking effective tax system reforms which will boost tax revenues and improve the tax system over the medium term.

66. **The goals of the Medium-Term Revenue Strategy include boosting ordinary revenue as a share of GDP to 25 percent.** This is to be achieved partly by increasing the tax compliance rate from 70 percent to 90 percent by the year 2030. These proposals are laudable however, since the tax policy strategy and framework are yet to be finalised, there is a risk that the significant growth in revenue expected in 2023/24 FY may not be realised.

67. **The BPS has outlined a raft of proposed tax administration measures.** These include rolling out the electronic Tax Invoice Management System (eTIMIS), Integration of KRA tax system with Telecommunication companies, mapping of rental properties and enhanced compliance through hampering the prevalence of counterfeit excisable products stamps in the market if implemented well may slightly boost revenue collection in the short-run while others, such as

the expansion of the tax base in the informal sector by targeting MSME may need careful consideration if they are to be effectively implemented.

68. **Total expenditure and net lending as a share of GDP has remained around 25 percent over the last decade.** This is as opposed to an average of around 20 percent between 2007 and 2013. One of the drivers of higher expenditure was the increase of statutory expenditures such as payment of interest payment on public debt which increased from below 2 percent of GDP to around 4.5 percent.

69. **The National Treasury projects that total expenditure and net lending will decrease from 23.4 percent in 2022/23 to 22.5 percent in 2023/24.** The proposed strategies aimed at slowing down the growth in expenditure include the elimination of non-priority expenditures, the elimination of consumption subsidies, the use of public-private partnerships (PPPs) in commercially viable projects, rolling out of e-procurement system, the implementation of the superannuation pension scheme and rolling out of the Public Investment Management System (PIMIS). The full rollout of PIMIS and the end-to-end e-procurement system will ensure that Kenyans get value for money in the delivery of public investments. However, the team that is setting up the two systems should take cognisance of past shortcomings in similar endeavours where huge investments in systems such as e-promis failed to achieve the intended outcomes.

70. **The proposals aimed at improving efficiency are laudable and if implemented well may contribute to curtailing expenditure growth over the medium term.** However, it should be noted that some of the items that have driven the growth in expenditure as a share of GDP such as interest payment on public debt may remain high over the next three years. The use of PPPs as alternative financing for projects will serve to reduce the growing demand for debt-financed development expenditures if bottlenecks that have been experienced during the implementation of past PPP projects in some sectors such as energy and road transport are addressed.

71. **The combined impact of the policies aimed at increasing tax revenue collection and curtailing the growth in expenditures if fully implemented is expected to reduce the fiscal deficit:** The fiscal deficit including grants is expected to decline from Ksh. 833.9 billion (5.7 percent of GDP) in 2022/23 to Ksh. 720.1 billion (4.4 percent of GDP) in 2023/24. However, as a result of some of the risks discussed above including possible over-projection of revenue growth and challenges associated with reducing the growth in total expenditure net lending in the short-run it is expected that the deficit for 2023/24 may remain above Ksh. 800 billion (over 5 percent of GDP)[8].

[8] See PBO's Budget Options for FY 2022/23 and the Medium-Term

Table3: Fiscal Framework for the FY 2023/24 budget and the Medium Term

Fiscal Framework in Ksh. Billion							
	2020/21	2021/22	2022/23	2022/23	2023/24	2023/24	2024/25
	Actual	Prel Actual	Budget Est	Suppl No.1	BPS	BPS	BPS
Revenue and grants	**1,815.1**	**2,230.8**	**2,495.7**	**2,560.2**	**2,943.0**	**3,280.4**	**3,723.2**
Total Revenue	**1,783.7**	**2,199.8**	**2,462.4**	**2,528.8**	**2,894.9**	**3,231.1**	**3,670.0**
Ordinary Revenue	**1,562.0**	**1,917.9**	**2,141.6**	**2,191.9**	**2,571.2**	**2,878.6**	**3,294.2**
Income tax	694.1	876.7	997.3	1,004.3	1,198.5	1,305.7	1,500.1
VAT	410.8	523.1	584.7	587.7	703.3	804.7	926.2
Import duty	108.4	118.3	144.9	145.9	173.3	199.4	229.0
Excise duty	216.3	252.1	297.2	297.2	352.7	401.1	460.0
Other tax revenue	132.5	147.7	117.5	156.8	143.3	167.8	178.9
Appropriation-in-Aid	221.7	281.9	320.8	336.8	323.8	352.5	375.8
Grants	31.3	31.0	33.3	31.4	48.1	49.3	53.2
Total expenditures & net lending	**2,749.5**	**3,027.8**	**3,358.6**	**3,394.1**	**3,663.1**	**3,991.9**	**4,457.9**
Recurrent expenditure	2,271.0	2,352.7	2,271.0*	2,349.9*	2,459.3*	2,667.5*	2,917.9*
Wages & salaries National gvt	493.0	520.0	537.2	539.6	600.0	645.3	703.4
Pensions & Other CFS	112.9	122.4	150.6	145.3	170.6	192.9	217.6
Interest	495.1	578.0	690.6	675.8	775.1	833.6	885.2
On domestic debt	388.8	456.8	553.4	537.4	628.3	680.9	730.8
On foreign debt	106.3	121.1	137.2	138.4	146.9	152.7	154.4
Operation and maintenance	652.1	866.1	866.7	885.1	822.7	896.6	1,003.9
Contribution to civil ser pension fund	3.3	-	25.9	31.9	28.5	31.3	34.4
Development & net lending	**553.9**	**540.1**	**676.6**	605.8	769.3	901.5	1,092.1
Development expenditure	553.9	540.1	667.3	577.3	744.2	871.5	1,062.9
Net lending	-	-	2.3	14.7	17.2	22.2	19.6
Contingency Fund	-	-	4.0	2.0	5.0	5.0	5.0
Transfer to Counties	399.0	352.4	407.0	436.3	429.6	417.9	442.9
Equitable Share	346.2	340.4	370.0	399.6	385.4	380.6	405.6
Conditional Allocation	52.8	12.0	37.0	36.7	44.2	37.3	37.3
Parliamentary service	29.2	32.7					
Judicial Service	14.3	16.2					
Equalization Fund	-	-	7.1	13.9	7.9	7.9	9.6
Overall balance including Grants	**(934.4)**	**(797.0)**	**(862.9)**	**(833.9)**	**(720.1)**	**(711.5)**	**(734.6)**
Overall balance excluding grants	**(965.7)**	**(828.0)**	**(896.2)**	**(865.3)**	**(768.2)**	**(760.8)**	**(787.9)**
Adjustment to cash basis	5.1	11.9	-	-	-	-	-
Deficit incl grants cash basis	**(929.3)**	**(785.1)**	**(862.9)**	**(833.9)**	**(720.1)**	**(711.5)**	**(734.6)**
As a Share of GDP							
Revenue and grants	15.9%	17.5%	17.8%	17.6%	18.1%	18.0%	18.2%
Total Revenue	15.6%	17.3%	17.6%	17.4%	17.8%	17.8%	18.0%
Ordinary Revenue	13.7%	15.0%	15.3%	15.1%	15.8%	15.8%	16.1%
Total expenditures and net lending	24.1%	23.7%	24.0%%	23.4%	22.5%	22.0%	21.8%
Overall balance including grants	**-8.2%**	**-6.3%**	**-6.2%**	**-5.7%**	-4.4%	-3.9%	-3.6%
Overall balance excluding Grants	**-8.5%**	**-6.5%**	**-6.4%**	**-6.0%**	-4.7%	-4.2%	-3.9%
Nominal GDP	**11,407**	**12,751**	**14,002**	**14,522**	**16,290**	**18,180**	**20,437**
.*Includes an allocation for Parliament and The Judiciary.							

72. **To finance the projected fiscal deficit for FY 2023/24 of Ksh. 720.1 billion, the National Treasury proposes to borrow Ksh. 521.5 billion from the domestic market**. The increase in domestic borrowing by an estimated Ksh. 83 billion relatives to the proposed 2022/23 supplementary No 1 budget estimates may have a negative impact on the availability of credit to the private sector. Further, in order to meet external debt obligations there is a proposal to seek external commercial financing of Ksh. 110 billion in 2022/23 FY and Ksh. 270 billion in FY 2023/24. This additional foreign commercial debt is expected to increase future statutory expenditures that are not channelled towards service delivery.

Table 4: Financing of the Fiscal Deficit (in Ksh. Billion)

	2020/21	**2021/22**	**2022/2023**	**2022/23**	**2023/24**
	Actual	**Prel Actual**	**Budget ESt**	**Suppl No. 1**	**BPS**
Fiscal Balance (incl. grants) Cash Basis	**(929.3)**	**(785.1)**	**(862.9)**	**(833.9)**	**(720.1)**
TOTAL FINANCING	**950.2**	**747.8**	**862.9**	**833.9**	**720.1**
NET FOREIGN FINANCING	**323.3**	**142.5**	**280.7**	**395.8**	**198.6**
Disbursements	451.6	327.1	521.8	619.5	674.2
Commercial Financing	114.3	0.0	105.6	110.0	270.0
o/w Export Credit- Commercial Financing	6.7	0.0	-	-	-
Sovereign Bond other Commercial Financing	107.6	0.0	105.6	110.0	-
External Debt Operations - Refinancing	-	-	-	-	270.0
Semi concessional Loans	-	-	-	-	-
Project Loans AIA	104.8	92.6	184.9	112.4	239.1
Project Loans Revenue	52.4	58.6	101.6	74.5	99.7
Project Loans SGR _Phase I_ AIA	4.6	-	-	-	-
Project Loans SGR _ PHASE 2A_AIA	6.9	-	-	-	-
Use of IMF SDR Allocation	-	40.8	-	47.3	-
Programme Loans	168.6	135.0	129.7	275.3	65.4
O/W P for R Programme Loans	11.0	4.0	3.5	15.5	3.5
IMF - RCF/ECF/EFF	76.9	29.1	63.2	116.9	61.9
Development Policy Operations - WB	80.8	86.3	44.0	124.0	-
Support for COVID-19 Vaccine Purchase	-	4.3	6.2	6.2	-
Development Policy Operations - ADB	-	11.3	12.7	12.7	-
Debt repayment - Principal	(128.3)	(184.5)	241.1)	(223.8)	(475.6)
NET DOMESTIC FINANCING	**626.9**	**605.3**	**582.2**	**438.1**	**521.5**
Financing gap	20.9	-37.3			

Budget For FY 2023/24 and the Medium Term

73. **The ordinary revenue projection for FY 2023/24 is Ksh. 2,571.2 million, which represents a 17 percent increase relative to the expected 2022/23 FY collection.** Despite expected enhanced revenue collection resulting from some of the tax policies presented in the BPS, a 17 percent increase in revenue collection may be unattainable. Historically ordinary revenue has grown in tandem with GDP at an average of around 10 percent, consequently, it is expected that ordinary revenue underperformance may result in a higher-than-expected fiscal deficit. The expected collection of Appropriations in Aid in 2023/24 FY is **Ksh. 323.8 billion** which is similar to the expected collection in FY 2022/23.

74. **The proposed budget ceiling for 2023/24 is Ksh. 3,663,147 million which represents an 8 percent increase from the 2022/23 approved budget.** The CFS expenditures are expected to surge by 14 percent. The main drivers of the increase in the CFS ceiling for 2023/24 FY include an increase of **Ksh. 74,857 million** in interest payments on domestic debt, an additional **Ksh. 19,997 million** in pension payments and an increase of **Ksh. 14,992 million** in payments of guaranteed loans.

Table 5: Budget Ceiling for 2022/23 FY and the medium term

Budget Ceiling for 2022/23 FY and the medium term (Ksh. Million)						
	2022/23	2023/24			2024/25	2025/26
Item	Approved Budget	BPS	Gross Change	% Change	BPS	BPS
Recurrent Estimates	1,403,904	1,485,105	81,201	5.8%	1,589,647	1,751,795
Development Estimates	715,355	766,973	51,618	7.2%	843,753	859,647
National Government	**2,119,259**	**2,252,077**	**132,818**	**6.3%**	**2,433,401**	**2,611,442**
Consolidated Fund Services	**869,343**	**991,341**	**121,998**	**14.0%**	**1,079,993**	**1,156,864**
County Equitable Share	**370,000**	**385,425**	**15,425**	**4.2%**	**380,645**	**405,646**
Total	**3,358,602**	**3,628,843**	**270,241**	**8.0%**	**3,894,039**	**4,173,951**

75. **The proposed ceiling for National Government expenditure in FY 2023/24 has been increased by Ksh. 132,818 million as compared to the 2022/23 FY approved budget estimates**. The resources have been allocated based on the following criteria;

I. Linkage of Programmes with the priorities that address the Bottom-Up Economic Transformation Agenda;
II. Linkage of the programme with the priorities of Medium-Term Plan IV of Vision 2030;
III. The degree to which a programme addresses job creation and poverty reduction;
IV. The degree to which a programme addresses the core mandate of the MDAs,
V. Cost-effectiveness and sustainability of the programme;
VI. The extent to which the Programme seeks to address viable stalled projects and verified pending bills; and
VII. Requirements for furtherance and implementation of the Constitution.

76. **The proposed development budget ceiling for 2022/23 FY is Ksh. 766,973 million:** These resources have been allocated to ongoing projects with a high impact on poverty reduction, projects that require counterpart funds and projects that cover the entire nation and contribute towards regional integration, social equity and environmental conservation. A summary of the sector allocations is provided in table 6.

Table 6: SUMMARY BUDGET CEILINGS FOR 2023/24 FY

Sector		Approved Budget	BPS	% Share in Budget	
		2022/23	2023/24	2022/23	2023/24
Agriculture, Rural & Urban Development	**Sub-Total**	**68,959.50**	**75,603.30**	**3.3%**	**3.4%**
	Rec. Gross	27,059.70	32,188.10	1.9%	2.2%
	Dev. Gross	41,899.80	43,415.20	5.9%	5.7%
Energy, Infrastructure & ICT	**Sub-Total**	**407,760.10**	**422,004.00**	**19.2%**	**18.7%**
	Rec. Gross	131,010.00	113,039.00	9.3%	7.6%
	Dev. Gross	276,750.10	308,965.00	38.7%	40.3%
General Economic & Commercial Affairs	**Sub-Total**	**26,032.00**	**51,725.30**	**1.2%**	**2.3%**
	Rec. Gross	19,076.80	22,655.80	1.4%	1.5%
	Dev. Gross	6,955.20	29,069.50	1.0%	3.8%
Health	**Sub-Total**	**122,519.30**	**154,012.00**	**5.8%**	**6.8%**
	Rec. Gross	68,503.00	80,374.00	4.9%	5.4%
	Dev. Gross	54,016.30	73,638.00	7.6%	9.6%
Education	**Sub-Total**	**544,519.50**	**597,187.00**	**25.7%**	**26.5%**
	Rec. Gross	515,600.70	562,874.00	36.7%	37.9%
	Dev. Gross	28,918.80	34,313.00	4.0%	4.5%
Governance, Justice, Law & Order	**Sub-Total**	**234,408.10**	**229,812.50**	**11.1%**	**10.2%**
	Rec. Gross	224,127.20	219,590.90	16.0%	14.8%
	Dev. Gross	10,280.90	10,221.60	1.4%	1.3%
Public Admin. & International Relations	**Sub-Total**	**356,857.60**	**308,829.10**	**16.8%**	**13.7%**

	Rec. Gross	177,982.10	195,061.70	12.7%	13.1%
	Dev. Gross	178,875.50	113,767.40	25.0%	14.8%
National Security	**Sub-Total**	**177,811.00**	**219,244.00**	**8.4%**	**9.7%**
	Rec. Gross	174,343.00	186,638.00	12.4%	12.6%
	Dev. Gross	3,468.00	32,606.00	0.5%	4.3%
Social Protection, Culture and Recreation	**Sub-Total**	**73,213.50**	**69,092.20**	**3.5%**	**3.1%**
	Rec. Gross	41,674.00	44,749.90	3.0%	3.0%
	Dev. Gross	31,539.50	24,342.30	4.4%	3.2%
Environment Protection, Water & Nat. Resources	**Sub-Total**	**107,178.20**	**124,568.00**	**5.1%**	**5.5%**
	Rec. Gross	24,527.50	27,933.00	1.7%	1.9%
	Dev. Gross	82,650.70	96,635.00	11.6%	12.6%
Total	**Total**	**2,119,258.80**	**2,252,077.40**	**100%**	**100%**
	Rec. Gross	**1,403,904.00**	**1,485,104.40**	**100%**	**100%**
	Dev. Gross	**715,354.80**	**766,973.00**	**100%**	**100%**

77. **The sector ceiling as a share of the total budget for FY 2023/24 has marginally increased for some priority sectors and declined for others:** The sectors that have additional funding include agriculture rural and urban development, general economic and commercial affairs, environment protection, water and natural resources, health and education while the ceiling for energy, infrastructure and ICT has declined. The shift in the sector shares reflects the government policy direction of redirecting resources away from large infrastructure projects and towards the pillars of the Bottom-up Economic Transformation Agenda. However, the ceilings for key pillars are not in tandem with the BETA targets and envisioned deliverables.

Criterion 5

County Resource Allocation

This criterion evaluates proposed resource allocation to counties as well as other proposed interventions to facilitate county resourcing and financial management.

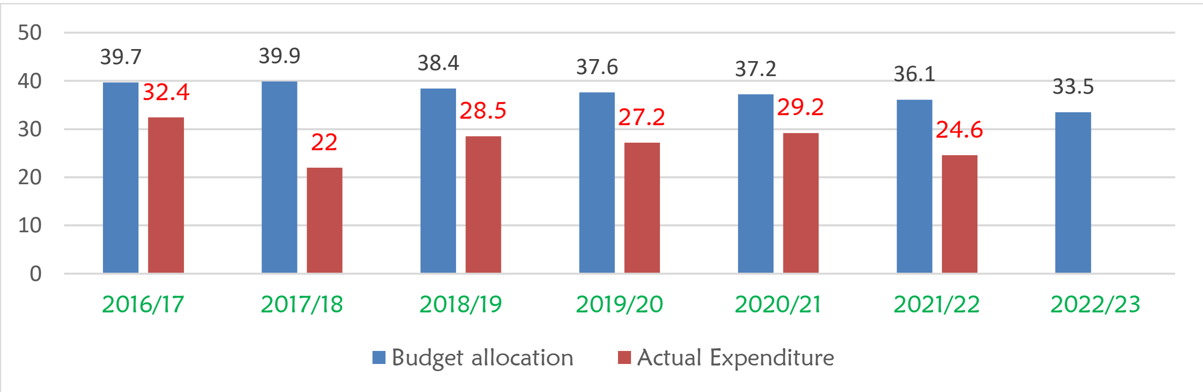
County Governments' Compliance with Fiscal Responsibility Principles

78. Section 107 of the PFM, Act 2012 elaborates on the principles of fiscal responsibilities in the management of the public finances at the sub-national governments. The county treasury is entitled to enforce the fiscal responsibilities on matters with regard to management of recurrent expenditures, development expenditures, wages and benefits for its public officers and the use borrowed funds by the government.

79. **Compliance with the Requirement on Development Spending as per section 107 (2) (b) of PFMA, 2012.** Counties are required to allocate a minimum of 30 percent of their total budget towards development. During the implementation of the FY 2021/22 budget all counties expect Nairobi and Kiambu met this legal requirement. The best performing county was Marsabit with 49 percent of the budget allocated towards development expenditures. On average 36.1 percent of County Governments' total budget was allocated to development in FY 2021/22.

80. **Although allocations meet the provided threshold during budgeting approval, the same is violated during actual implementation.** This undermines the credibility of the budget and violates a critical fiscal responsibility principle. This may partly be attributed to delayed exchequer releases by National government. For instance, by end of the first quarter of FY 2022/23, Counties had only spent Kshs.2.22 billion on development activities against the annual development budget of Kshs.160.58 billion. As such, it is highly unlikely that they will meet this target.

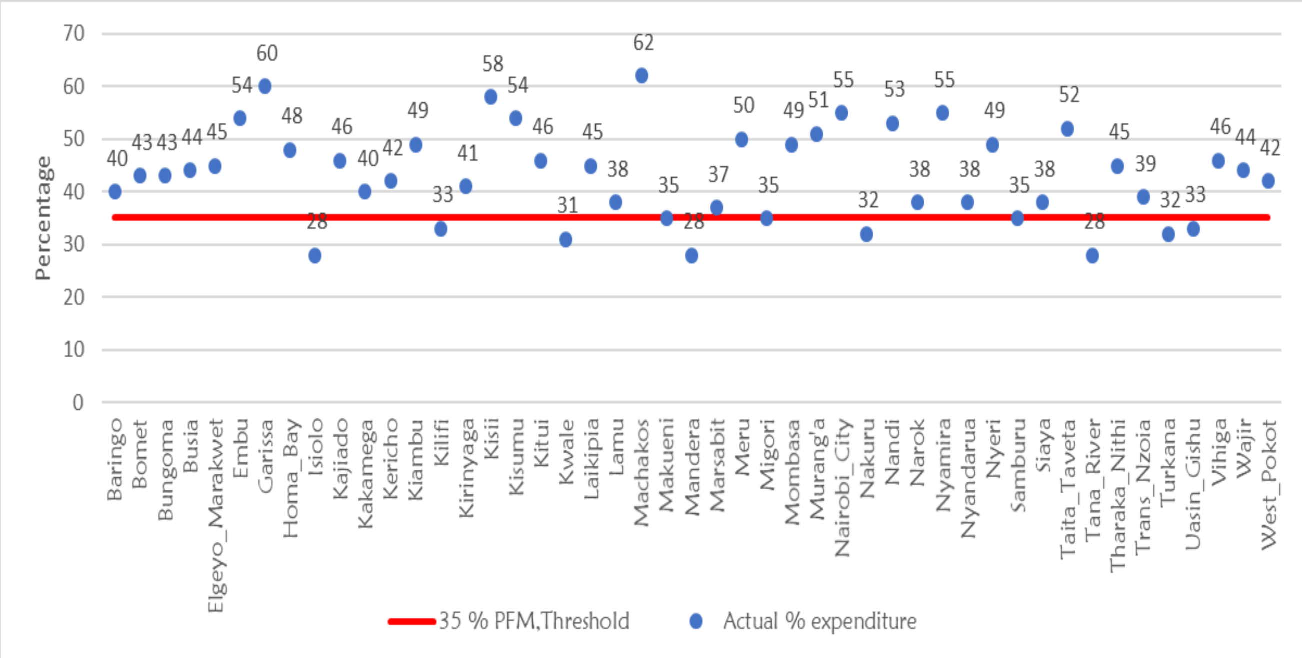
Figure 12: Development expenditure allocation and Actual Expenditures on development as Percentage of Total County Expenditures



Source of Data: Controller of Budget

81. **Compliance with the Requirement on Expenditure on Wages and Benefits in line with PFM Regulations**: County government's expenditure on wages and benefits to public officers is capped at 35 percent of the county government's total revenue, excluding those drawn from extractive natural resources. Figure 13 shows that counties have continually breached the threshold. This continued breach and significant deviation from the fiscal rules is a worrying trend which continue crowding out development resources at the county. Going forward county governments should demonstrate how they intend to adhere to this principle in the medium term.

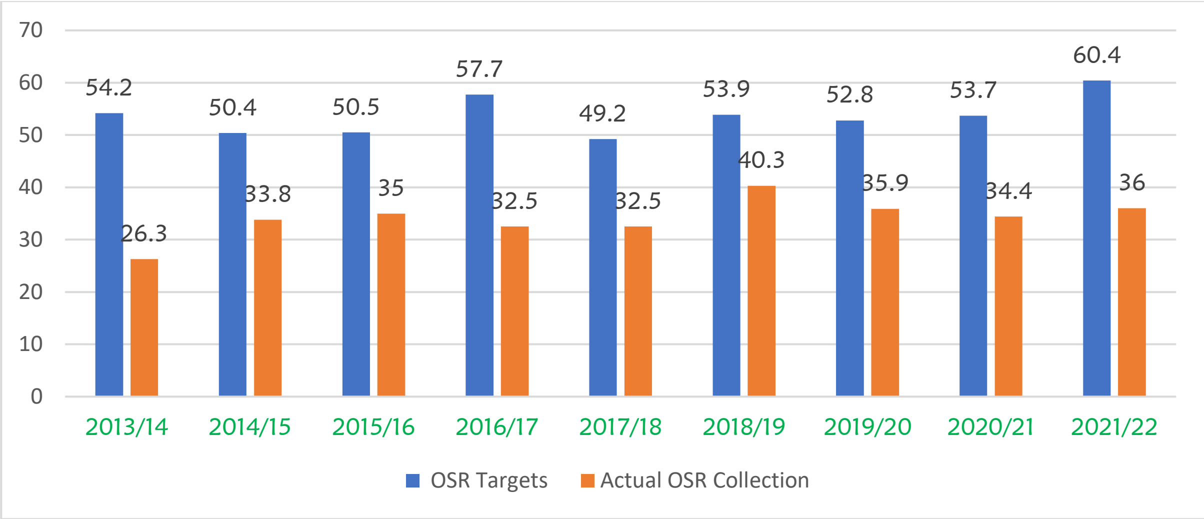
Figure 13: FY 2021/22 County Governments' Actual Expenditures on Wages and Benefits as a Percentage of Total Actual Revenue



Source of Data: 2023 Budget Policy Statement.

82. **Enhancement of County Governments' Own-Source-Revenue (OSR):** According to a report by CRA, the estimated revenue potential across the 47 counties is Ksh.215.6 billion. However, Counties were able to collect only Ksh.35.9 billion in FY 2021/22, implying that there is 83 percent Potential revenue gap across the counties. Annex 1, details the Actual OSR Collection for FY 2021/22 and the potential revenue estimates by CRA. Counties have continually recorded low OSR collections (Figure14). In the first quarter of FY 2022/23, counties had collected Ksh.6.1 billion against an annual target of Ksh.57 billion, representing a 10 percent performance.

Figure 14: Performance of OSR collections vs targets (FYs 2013/14-2021/22-Ksh.billion)



Source of Data: CRA

83. The Budget Policy Statement has highlighted a number of policy interventions to improve on the counties OSR collections in the coming financial year and the medium term. A summary of the key recommendations is as shown;

SN	Policy proposal	Responsible body
1.	Adoption of automatic and cashless payments systems as well as streamlining of taxation and fees structure.	County Governments
2.	Strengthening collaboration and data sharing between different organizations and departments	County Governments and other organizations and departments.
3.	Developing the National Rating Bill, and the County Government (Revenue Raising process) Bill,	National Treasury, County Governments and other Stakeholders
4.	Payments of Contribution in Lieu of Rates (CILOR)[9] due to counties and laying legal framework for claiming CILOR.	National Treasury, other stakeholders such as parliament.
5.	Developing a model tariffs and pricing policy	CRA, National treasury and other stakeholders.

Source of Data: BPS 2023

84. These policy interventions although clearly elaborated in terms of the objectives, do not speak to the extent to which they will assist the counties to realize the revenue shortfalls. There is no indicative amount of revenues or percentage performance in revenue generation that will be triggered through the policies.

[9] Contribution in Lieu of Rates (CILOR) are rates payable to the County Governments in respect of public land as provided for under the Valuation for Rating Act (Cap 266); Rating Act (Cap 267) and the Valuation for Rating (Public Land) Rules- **BPS 2023.**

85. Going to FY 2023/24, the policies on revenue collection should focus on sealing revenue leakages and reporting of actual revenue collections from different streams by county governments. Additionally, the government transformation agenda on Agriculture and the Micro, Small and Medium Enterprise (MSME) Economy, if well implemented would trigger substantial revenues across counties. The growth in these sectors will improve collections from agricultural transportation fees (cess), market trade centre fees and trade licenses fees.

86. **Prudent Management of Fiscal risks and the pending bills menace:** Huge pending bills have accumulated since inception of devolution amounting to Ksh.156.2 billion (2020 Audited Pending Bills), of which Ksh.48.1 billion was eligible and 108.1 was ineligible pending bills. As at December 2022, the total outstanding pending bills for counties amounted to Ksh. 131.35 billion. According to controller of budget only Ksh.22.1 billion had been cleared out of the Ksh.48.1 billion eligible pending bills, while only Ksh. 1.8 billion of the ineligibles pending bills had been paid as at 21st December, 2022. These accumulations risk sanctions from the National Treasury as provided for in Article 225 and Section 96 of the PFM Act. The decision to stop the transfer of funds to counties is by approval of Parliament.

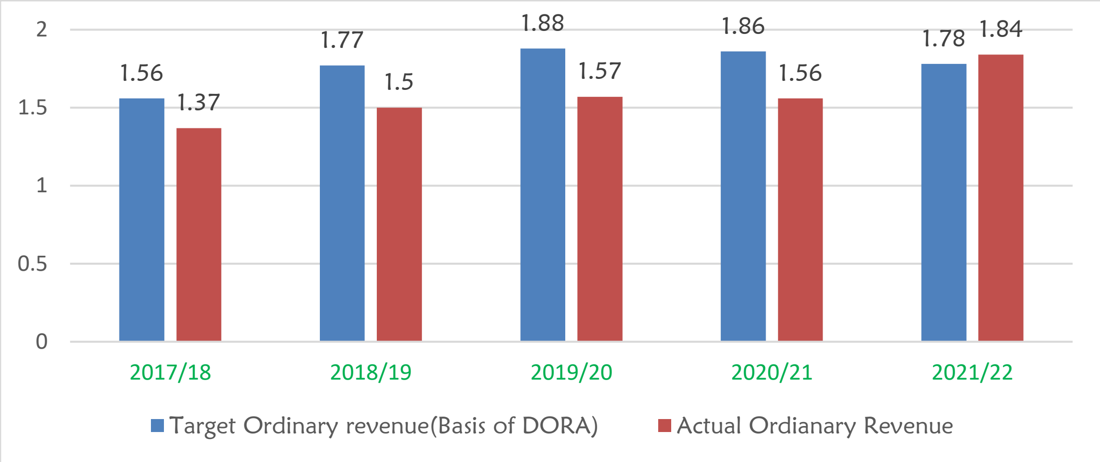
87. **The budget Policy statement has identified several measures to address the accumulation of the pending bills.** Counties are required to comply with the communication in Circular No.2/2022 dated 24th March 2022, regularly report on pending bills in accordance with the financial reporting template by the Public Service Accounting Standards Board (PSASB) and put in place monthly payment plans for outstanding pending bills. As constantly recommended by the Controller of Budget (CoB), county governments should settle all eligible pending bills as a first charge in the FY 2023/24 in line with Regulation 41 (2) of the Public Finance Management (County Governments) 2015. Further, National Treasury has committed to disburse equitable share of revenue to counties on time. If this is undertaken, it will assist in addressing the issue of pending bills.

Ordinary Revenue Performance and Division of Revenue

88. **Performance of ordinary revenue forms the basis of the division of revenue between the National and County Government**. Since FY 2016/17 ordinary revenue has underperformed by 27 percent on average, except in FY 2021/22 when revenues surpassed the targets by about 6 percent as shown in figure 15. The division of revenue Acts have routinely provided that any revenue underperformance should be borne by the national government. However, in the recent past the National Treasury has tied disbursement of the equitable share to the revenue performance. In FY 2023/24, the National Treasury should ensure transfer to counties are in line with the approved disbursement schedules for effective budget implementation in the counties.

89. **Revenue is expected to grow by 17 percent, from Ksh. 2,191.9 billion to Ksh.2,571.2 billion in FY 2023/24 (From 15.1% to 15.8% of GDP).** Out of this Ksh.7.9 billion is allocated to the equalization fund, leaving Ksh. 2,563.3 billion as the sharable revenue. The National Government is allocated Ksh. 2,177.9 billion while County Governments will receive Ksh.385.4 billion. This means only 15 percent of projected revenue for FY 2023/24 will be transferred to Counties, with 85 percent remaining at the National level.

Figure 15: Ordinary Revenue Targets vs. Actual Revenue receipts (Ksh trillion)



Source of Data: BPS 2023.

90. **County allocation has increased by Ksh.15.4 billion from the Ksh.370 billion allocated in FY 2022/23.** The increment is due to adjustment to revenue growth by Ksh.15 billion and an allocation of Ksh.425 million towards the transfer of library functions to the counties. It is noted that the amount is 24.5 percent of the last audited accounts amounting to Ksh. 1,573.42 billion for FY 2019/20.

91. The BPS indicates that the Ksh.385.4 billion allocation to the counties was informed by the following circumstance as presented in the matrix.

SN	Policy reasons	Observations
1.	The Ksh.385.4 billion in the FY 2023/24 is equivalent to **24.5 percent** of the last audited accounts approved by Parliament	The audited and approved amount for FY 2019/2020 is Ksh.1730.99 billion and not Ksh. 1573.42 billion as indicated in the BPS
2.	High level of debt financing in the contest of limited avenues to financing from domestic and international financial markets	The BPS envisages reforms on revenues (17.8% of GDP) and expenditure (22.3% of GDP); hence county equitable share of revenue should be guaranteed.
3.	Increased Government expenditure needs relating to drought intervention, fertilizer subsidy and the Hustlers Fund	Some of the identified government priorities relate to devolved functions, **hence funds should be seen to follow functions.**
4.	In the medium term, sharing of resources will be pegged on the financing constraints and not on the budget.	This contravenes Article 219 of COK; *County's' share of revenue shall be transferred without undue delay and without deduction*
5.	National Government continues to solely bear shortfalls in revenue in any given financial year, hence effecting cuts in national government budgets.	National Government has several instruments of raising revenues as compared to county governments (Article 209 of COK), hence this is not justifiable.

Source of Data: BPS 2023 and PBO observations.

Additional Allocations to Counties.

92. County Governments will further receive additional allocations of Ksh.44.3 billion in FY 2023/24 which comprises of; Ksh.11.1 billion From the National Government's share of revenue, and Ksh.33.19 billion from proceeds of external loans and grants. The aggregate allocation to county governments in FY 2023/24 amounts to Ksh.429.7 billion.
93. The conditional grants from the National Government's share of revenue are towards three specific projects meant to support some national policy objectives. They include; Ksh. 5.86 billion for leasing of medical equipment, Ksh.4.7 billion for operationalization of the national government's programme on aggregated industrial parks and Ksh.454 million for the construction of county headquarters.
94. The Medical Equipment Services (MES) project has faced numerous challenges before. The intergovernmental Partnership Agreements between the MoH and the County Governments are not provided in the BPS. In view of this the programme should be retired and the allocation be included in the County Governments' Equitable Revenue for FY2023/24.
95. Each county has been allocated Ksh. 100 million from programme of aggregated industrial parks. This conditional grant is to cater for initial costs in preparation for establishment of industries across the 47 counties. County governments may be required to provide land.
96. Additionally, counties will benefit from unconditional allocation of Ksh.108.7 million as remittances from court fines generated from county legislation. This is the amount which accrued from FY 2019/20, 2020/21 and 2021/22 from ten county Governments. As indicated in table 7, the money will be channelled to the respective County revenues Funds through the County Government Additional allocation act. However, these funds are actually county revenue collected by the Judiciary on behalf of the respective counties and hence the money does not qualify to be an additional allocation. The national treasury should fast track the development of a framework to ensure direct remittance of money to the respective county governments by the Judiciary.
97. The additional Conditional Allocations Financed from proceeds of loans and grants from Development Partners for Financial Year 2023/24 are as shown in table 7. The frameworks and conditions to be met by counties should be identified early enough to enable counties utilize the funds on time. Further, no information is provided on the expected outputs of these Programmes neither any performance indicators, and any set targets. Performance evaluation should be undertaken before resource allocations to ascertain viability of the projects.

Table 7- Additional Allocations to County Governments

S/N	Programme/ Project	Amount in CGAAA, 2022/23 (Ksh.)	Amount in CGAA, in FY 2023/24Ksh
	Additional Conditional/Unconditional Allocations from the National Government's Share of revenue		
1	Construction of County Headquarters	163,000,000	454,000,000
2	Court Fines from County legislation (Unconditional)	0	108,660,979
3	Aggregated industrial parks programme	0	4,700,000,000
4	Leasing of Medical Equipment	5,200,000,006	5,862,000,000
	Total	5,363,000,006	11,124,660,979

	Additional Conditional Allocations Financed from proceeds of loans and grants from Development Partners for Financial Year 2023/24.		
5	IDA (World Bank) credit (National Agricultural and Rural Inclusive Growth Project (NARIGP)	3,900,000,000	3,150,000,000
6	IDA (World Bank) credit National Agricultural Value Chain Development Project (NAVCDP)	1,820,000,000	8,250,000,000
7	IDA (World Bank) - Kenya Climate Smart Agriculture Project (KCSAP)	2,200,002,000	2,160,000,000
8	IDA (World Bank) credit: Water & Sanitation Development Project	3,500,000,000	5,350,000,000
9	DANIDA Grant - Primary Health Care in Devolved Context	1,018,125,009	577,500,000
10	IDA (World Bank) Credit (Financing Locally- Led Climate Action (FLLoCA) Program, County Climate Institutional Support (CCIS) Grant	1,034,000,000	517,000,000
11	IDA (World Bank) Credit (Financing Locally- Led Climate Action (FLLoCA) Program, County Climate Resilience Investment (CCRI)Grant	0	6,187,500,000
12	Sweden- Agricultural Sector Development Support Programme (ASDSP) II	655,175,274	72,797,253
13	German Development Bank (KfW)- Drought Resilience Programme in Northern Kenya (DRPNK)	410,000,000	765,000,000
14	World Bank - Emergency Locust Response Project (ELRP)	1,200,000,000	2,302,630,288
15	World bank - Kenya Informal Settlement Improvement Project (KISIP II)	1,300,000,000	3,269,530,746
16	IDA World Bank -Kenya Urban Support Programme (KUSP)	122,020,000	0
17	Kenya Livestock Commercialization Project (KELCLOP)	0	344,300,000
18	Aquaculture Business Development Project (ABDP)	0	245,879,120
	Total	17,159,322,283	33,192,137,407
	Grand total for Additional Allocations	**22,522,322,289**	**44,316,798,386**

Source: CGAAA,2022 & BPS 2023

98. Whereas one of the fundamental objectives of conditional grants is to promote specific national policy priorities, its permanence and inefficacy violate some crucial principles of conditional grants. Some of the identifiable gaps under conditional allocations include;

a) The funding aspect is characterized by discretionary transfers of both equitable share and the conditional grants.
b) There is no planning path for the conditional grants as they are haphazardly applied, with arbitrary introduction of new grants every year.
c) They suffer designed Shortcomings including overlapping objectives and failure to address vertical and horizontal fiscal spill overs or externalities as intended.
d) The grants lack measures of equity, efficiency, predictability, flexibility and accountability
e) There is little or no cost estimates while purportedly intended to fund National priorities.

Horizontal Allocation of Revenue among the County Governments

99. The sharing of revenue among the county Governments will be based on the third basis formula. This is the fourth year that the third basis for allocating revenues among the counties is in use. The parameters include; Population (18 percent); Health Index (17%); Agriculture Index (10 %); Urban Index (5%); Poverty Index (14 %); Land Area Index (8%); Roads Index (8 %); and Basic Share Index (20 %).

100. The application of the formula will still be based on the baseline allocation to each county equivalent to 50 percent of a county's actual allocation for FY 2019/20.This means Ksh.158.25 billion will be shared based on the FY 2019/20 county allocation index and the remaining Ksh. 226.75 billion shared using the third basis. The Ksh.425 million set aside from the county equitable share for library services will be shared among 33 county Governments. Given that, the third basis is still being applied partially on the County equitable share, its objectives may not fully be realized as contemplated in the formula and hence future reviews may not be fully informed.

Equalisation Fund

101. The Equalisation Fund is established under Article 204(1) of the Constitution, into which shall be paid one half per cent of all the revenue collected by the national government each year calculated on the basis of the most recent audited accounts of revenue received, as approved by the National Assembly. Allocations to the fund in FY 2023/24 is Ksh.7.9 billion which is equivalent to 0.5 percent last audited accounts (Ksh 1,573.42 billion for FY 2019/20).

102. However, it is notable that the audited and approved amount for FY 2019/2020 is Ksh.1730.9 billion. Based on this the allocation to the Equalization Fund for FY 2023/2024 would be Kshs.8.65 billion. The national treasury should revise the allocations to the fund by using the right amounts of most recent audited accounts as approved by the National Assembly of Ksh. 1730.9 billion for FY 2019/20.

103. Article 204(2) provides that the national government shall use the Equalisation Fund only to provide basic services including water, roads, health facilities and electricity to marginalised areas to the extent necessary to bring the quality of those services in those areas to the level generally enjoyed by the rest of the nation, so far as possible.

104. Total Statutory entitlement to the Fund as per the Constitution is Kshs.55.3 billion. However, the actual transfers to the Fund amount to Kshs. 12.4 billion, resulting to a total shortfall of Kshs.42.9 billion as per FY 2022/23. The BPS has not given any policy guidelines on measures to be taken to unlock the arrears in the allocations as well as disbursements from the fund for the previous financial years.

105. Further, there is need for the Equalisation Fund Board and The National Treasury to fast track the operationalization of the Fund, taking into account the time period of only seven (7) years left. The Board should swiftly and urgently facilitate the establishment of the various County technical committees as provided by Regulations 14, 16, and 18 of the Public Finance Management (Equalisation Fund Administration) Regulations,2021.

Emerging Issues and Policy Interventions

106. **Transfer of Functions and Cooperation between National and County Governments**: In order to facilitate full transfer of functions to county governments and resolution of any disputes thereof as provided for in Articles 6, 187 and 189 of the Constitution read together with the provisions in Intergovernmental Relations Act (IGRA), 2012, the Government purposes to develop relevant policy and legislation for operationalization of Articles 187 and 189. There is a draft amendment bill to the PFM Act, 2012 which is currently being processed for submission to the public for comments. BPS has further committed to transfer all the devolved function within six months. This will in turn facilitate the financing of transferred functions and cooperation between the two levels of governments for the better delivery of services.

107. **Integrated County Governments Revenue Management System**: The is a system being developed to enable counties migrate from the unintegrated revenue management systems which has high administrative costs and revenue leakages. This will enable County Governments to use a uniform system that seals revenue leakages and provides value for money invested in it. The key player here is the National treasury; hence it should move with speed to put this in place to curtail any further losses of public funds.

108. **Sharing of Mineral Royalty Revenue with County Governments and Communities**: The government envisages to operationalize section 183(5) of the Mining Act 2016, which provides for the sharing of revenues from mineral royalties. The law requires that the benefits be distributed as follows; seventy percent to the National Government; twenty percent to the County Government; and ten percent to the community where the mining operations occur. The State Department for Mining is tasked with development of regulations that will unlock the sharing of revenue from mineral royalties as envisaged in the act. The national treasury proposes that these funds be administered through the additional allocation to counties as unconditional grant. This is an important policy pronouncement which will boost county OSR and eventually improve the lives of the people.

109. **Transfer of the library services function.** The government has allocated Ksh.425 million in FY 2023/24 to facilitate the transfer of library services to county governments as envisaged in the fourth schedule of the constitution. The funds will be administered through equitable share of allocation in three phases as shown in table 8.

Table 8: Allocations towards library services in the medium term.

FY	Allocation	Remarks
2023/24	425,000,000	100 % Allocation of the Ksh.425 million
2024/25	318,750,000	75 % allocation of the ksh.425 million
2025/26	106,250,000	25 % allocation of the Ksh.425million

110. The annual allocation to library services over the next three years is Ksh. 425 million. Since the allocation is part of the equitable share of revenue for counties, the balances in the two financial years will be shared as equitable share to all counties. In the fourth year, the entire Ksh. 425 million (FY 2026/27) will be included as equitable share and the 33 counties with library service are expected to have integrated salaries of staff and operations of the library in to their payroll systems.

111. It is worth noting that the inclusion of Ksh. 425 million allocations to library services under the equitable share to counties presents a legal concern. The equitable share allocation already has a predetermined formula for disbursement among counties, which do not include library services as a parameter. Further, it is noted that Lamu County has been allocated Ksh.20.2 million in FY 2023/24 for library services yet it does not have a library. On the other hand, Makueni county has not been allocated resources yet it has library services.

112. **County Governments Public Finance Management:** The BPS has highlighted the challenges the County Governments have faced in in the management of public finance. They were identified in a multi-agency taskforce through the support of National Treasury. The identified challenges points to exacerbated fiduciary risks in county governments. This implies critical services at the county level are being denied. Although, a number of mitigation measures has been proposed, there no clear road map in the fight against corruption which the biggest contributor of the challenges.

Summary of PFM Challenges faced by CGs and proposed measures

S/N	Identified challenges	proposed measures
	➢ Weak linkage between planning and budget formulation ➢ High outstanding pending bills ➢ Low development budget absorption ➢ Under-performance in own-source revenue ➢ Failure to use the prescribed financial systems (such as IFMIS, IPPD among others) ➢ Non-adherence to fiscal responsibility principles ➢ Pilferage of public resources ➢ Inadequate understanding of the Office of the Controller of Budget's role in approval of county requisitions ➢ High wage bill ➢ Weaknesses in human resource management ➢ Weak oversight by County Assembly and a weakened internal audit function.	➢ Development of a National legislation on planning to guide planning at both levels ➢ of Governments ➢ Integration of national and county planning ➢ Development of a National resource mobilization strategy ➢ Operationalization of all IFMIS modules including pending bills, accounts receivables ➢ Monitoring and evaluation ➢ Development of a standardized framework for assets valuation in counties; fast-tracking the processing of Auditor General's reports in the County Assemblies and the Senate to strengthen oversight in the management of public finance functions in counties ➢ Customization of human resource policies by the Ministry of Public Service in consultation with the PSC, IGRTC and CGs ➢ Amendment of various Sections of PFMA, 2012 and continuous capacity building of County Governments officials on all PFM related areas.

ANNEXURES

Annex 1: Actual vs Potential County Own Source Revenue

Annex 1:detaied Actual FY 2021/22 OSR Collection and the potential revenue estimates by CRA study).					
S/N	County	Actual collections of revenues(Ksh.million)	Deterministic Frontier Analysis Revenue Potential(Ksh.million)	Top-Down Revenue Potential(Ksh.million)	% performance against Potential Revenue
1	Baringo	264.89	2,000.00	3,744.90	13%
2	Bomet	202.43	2,216.70	5,937.90	9%
3	Bungoma	368	1,874.30	5,910.10	20%
4	Busia	292.73	1,889.60	3,548.10	15%
5	Elgeyo_Marakwet	162.25	1,078.20	3,662.50	15%
6	Embu	394.54	1,465.90	2,835.20	27%
7	Garissa	65.62	810.6	919.5	8%
8	Homa_Bay	146.64	1,857.40	3,680.60	8%
9	Isiolo	107.83	581.5	692	19%
10	Kajiado	527.94	5,400.80	6,359.10	10%
11	Kakamega	1,226.07	5,876.80	6,731.00	21%
12	Kericho	566.82	2,104.20	5,305.00	27%
13	Kiambu	3,149.18	11,304.60	13,950.80	28%
14	Kilifi	827.49	2,690.70	3,386.40	31%
15	Kirinyaga	364.65	2,310.10	3,826.60	16%
16	Kisii	404.55	2,190.60	5,193.80	18%
17	Kisumu	982.78	28,187.30	6,667.20	3%
18	Kitui	361.27	1,603.10	3,030.70	23%
19	Kwale	302.68	3,271.90	2,165.00	9%
20	Laikipia	894.88	1,388.00	2,594.70	64%
21	Lamu	126.99	431	585.4	29%
22	Machakos	1,118.46	8,838.20	7,702.50	13%
23	Makueni	749.4	1,393.30	2,540.10	54%
24	Mandera	132.89	736.1	1,185.20	18%
25	Marsabit	99.56	565.6	1,083.80	18%
26	Meru	551.3	3,730.70	8,374.00	15%
27	Migori	385.39	3,741.80	3,892.00	10%
28	Mombasa	3,608.67	6,041.10	7,348.00	60%
29	Murang'a	520.31	3,726.30	6,066.70	14%
30	Nairobi_City	9,238.80	67,655.20	65,086.70	14%
31	Nakuru	1,707.44	10,965.70	14,273.30	16%
32	Nandi	275.65	1,411.00	4,353.20	20%
33	Narok	1,334.56	4,100.20	8,543.80	33%
34	Nyamira	166.48	1,957.60	3,849.20	9%
35	Nyandarua	473.06	1,548.60	3,300.90	31%
36	Nyeri	948.31	4,302.00	6,155.10	22%
37	Samburu	120.04	711.7	875.5	17%
38	Siaya	434.37	1,203.60	2,702.90	36%
39	Taita_Taveta	315.57	1,186.60	1,603.10	27%
40	Tana_River	72.26	335.5	522.3	22%
41	Tharaka_Nithi	234.29	758.1	1,467.50	31%
42	Trans_Nzoia	379.99	1,996.60	4,705.20	19%
43	Turkana	204.34	1,207.70	2,530.40	17%
44	Uasin_Gishu	858.34	2,775.00	5,222.40	31%
45	Vihiga	236.26	1,662.30	3,065.30	14%
46	Wajir	52.41	632.7	890.8	8%
47	West_Pokot	113.44	1,840.90	2507.5	6%
	Total	**36,071.82**	**215,557.40**	**260,573.90**	**17%**