A REVIEW OF IMF-KENYA FISCAL CONSOLIDATION IMPLEMENTATION

OKOA UCHUMI FISCAL CONSOLIDATION PUBLIC EDUCATION CAMPAIGN

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Abbreviations and Acronyms

BoP	Balance of Payment
CBK	Central Bank of Kenya
ECF	Extended Credit Facility
EFF	Extended Fund Facility
FC	Fiscal Consolidation
FDI	Foreign Direct Investments
GDP	Gross Domestic Product
GoK	Government of Kenya
IFMIS	Integrated Financial Management Information System
IMF	International Monetary Fund
KUCCPS	Kenya Universities and Colleges Central Placement Service
M1	Money Held by the Public
MDAs	Ministries, Departments and Agencies
MPCC	Monetary Policy Consultation Clause
PAYE	Pay-As-You-Earn
PFMA	Public Finance Management Act
PV	Present Value
REER	Real Effective Exchange Rate
SAP	Structural Adjustment Programs
SOE	State-Owned Enterprise
VAT	Value Added Tax

Executive Summary

This is *Okoa Uchumi Campaign* monitoring and reporting framework and the results of the first review of the fiscal consolidation program. It has been prepared to guide the monitoring of recommendations made in the *Okoa Uchumi Campaign* report titled *Kenya Debt Crisis: Unpacking Fiscal Consolidation 2021,* and the IMF supported fiscal consolidation program implementation. The framework lays out the public debt campaign components and the fiscal consolidation programme, in terms of the activities to be implemented to achieve the objectives and their performance indicators. The framework presents the fiscal consolidation programme in terms of the goals, objectives and the activities, defines the relationships between factors key to implementation and articulates the internal and external elements that relate to and affect the programme's performance. This provides a monitoring framework to inform the *Okoa Uchumi Campaign* efforts to track progress of the fiscal consolidation programme. Based on the framework, the first review of the fiscal consolidation programme implementation has been done, out of which the following observations and conclusions have been made:

1. Kenya's public debt continues to rise. As at the end of June 2021, the total public debt stock was Kshs 7.7 trillion, an increase from Kshs 6.7 trillion in June 2020, resulting to a public debt of 72.6 per cent of GDP in 2021/2022 Financial Year from 70.2 per cent of GDP in 2020/2021 Financial Year.
2. The foreign debt increased from Kshs 3.8 trillion in 2020/2021 Financial Year to Kshs 4 trillion in the current Financial Year 2021/2022. The increase in foreign debt emanated from Kenya's fourth Eurobond issuance, a commercial debt.
3. The proposal to amend the Public Finance Management Regulations 2015 to replace the current nominal legal ceiling on public debt (that is KShs 9 trillion and close to being reached) with a medium-term debt-to-GDP anchor of 55 per cent of GDP in present value (PV) terms will serve to create more room for government borrowing. Whether the country chooses a nominal legal public debt ceiling, or a medium-term debt-to-GDP will not resolve the underlying public debt problem. The root cause of the public debt problem must be addressed, and these include poor oversight mechanisms, value for money challenges in public projects, weaknesses in planning, budgeting and execution.
4. Recurrent expenditure continues to account for more than 70 per cent of the national budget, meaning that development expenditure allocation is less than 30 per cent. This is contrary to the *Public Finance Management Act 2012 section 15(2)(a)* that provides, "*a minimum of 30 per cent of the national budget shall be allocated to the development expenditure.*" In this regard, the National Treasury continues to violate the law.
5. As of 30th June 2021, the Kenyan Government paid KShs 1,657,544,758.23 on commitment fees on loans that have not been utilised, despite the signing of loan agreements.
6. The broad money expansion of 10 and 11 per cent is in line with the fiscal consolidation programme objective of inflation target. However, this continues to make current account unfavorable, uncompetitive exchange rate continues and therefore the persistent need for external debt and wasteful need to maintain foreign reserves at four months of imports. In cases where the reserves are low, borrowing is being used to increase reserves. This can simply be evaded by freely floating exchange rate. The flexible exchange rate should serve as

a shock absorber, strengthening external sector resilience. Inflation-Focused Monetary Policy continues to make the economy unproductive.

7. Kenya's goods are coming under pressure from foreign products, and this is evident from expanding current account deficit. The current account deficit is expected to expand as projected from the current minus 4.6 to minus 5.5 by the end of the fiscal consolidation programme.
8. Kenya's export earnings are expected to decline in the next financial year from 10.1 per cent in the 2020/2021 Financial Year to 9.9 per cent in the 2021/2022 Financial Year. This is together with remittance by Kenyans in the diaspora, which has been a key source in providing stability to the Shilling but has been hit hard by the COVID-19 pandemic. This means that financing of dollar-dominated public debt will remain a burden on the taxpayer. This can be avoided when the economy is promoted to largely produce to meet its domestic demand.
9. Fiscal deficit increased to 8.7 in the 2021/2022 Financial Year from 7.8 per cent of GDP recorded in the previous Financial Year 2020/2021.
10. 64.1 per cent of tax revenue collected is spent towards public debt servicing leaving less funds towards other budget votes.
11. Despite the high cost of production emanating from high taxation and more so on inputs, the Government of Kenya is unable to use taxation as a means of lowering cost of production to keep up the need to raise revenue as demanded in the programme conditions. Taxation in Kenya is majorly about tax revenue collection with little regard to the impact on businesses and households. This makes Kenya unattractive to both domestic and foreign investors. Some examples of harmful taxes affecting manufacturers are minimum tax (currently in court), VAT on plant and machinery, annual inflation adjustment for excisable goods in Kenya, excise duty on plastic packaging and resins. This also harms final consumers.
12. The Kenyan Government is incurring over KShs 400 billion in tax expenditures annually. This emphasises the importance of transparent disclosures of tax expenditures, especially considering the underperformance of revenues in recent years and the growing pressures on controlling the national budget deficit. The KRA cites tax expenditures as a major impediment to its ability to meet revenue targets, with tax expenditures estimated at KShs 478 billion in 2017.
13. The government is pursuing revenue-based fiscal consolidation to stabilise public debt. The effect of this is a reduction of aggregate demand in the economy, resulting to further contraction. This is evidenced by economic indicators available in the year 2021.
14. The placement of government sponsored students to private universities through the Kenya Universities and Colleges Central Placement Service (KUCCPS), a State Corporation, needs to be stopped. Instead, the placement of government- sponsored students should be to public universities to utilise the idle capacity being experienced in the public universities. This should be done together with reforms geared at improving governance in these institutions while safeguarding the objective of access to education by poor students. Any reform must be carefully evaluated given that universities play a critical role in human capital development
15. The audits of all COVID-19-related expenditures in 2019/2020 Financial Year have been completed, including audits of all spending by ministries, departments and agencies (MDAs), and forensic audits of COVID-19 funds utilised by National Government entities, Kenya

Medical Supplies Authority (KEMSA) and counties. The IMF notes that the production of multiple audits has provided a high degree of transparency, notwithstanding the short delay in publication of the final audits. While KEMSA published reports with information on awarded contracts and beneficial ownership of the companies, the Public Procurement Information Portal has yet to publish beneficial ownership information. This key planned step should be implemented as a matter of priority. The KEMSA audit found numerous violations of the law on public procurement and public finance management, and inefficiencies in the procurement process. The Director of Public Prosecutions has been petitioned to open charges against individuals involved. There is need for the public to know the consequences of adverse reports and the mechanisms to ensure programmatic actions to seal identified weaknesses and follow-up on the same.

16. Public consultations on the regulations to enable the implementation of the Access to Information Act, 2016 should be followed by tabling in Parliament for swift approval. Additionally, the government was to finalise the review of the legal framework on asset declaration and conflict of interest rules for senior public officials by September 2021. However, this is late and needs to move quickly to effectively adopt and operationalise the system as directed by the IMF. This should be done transparently to expose corruption.
17. The government proposal to adopt a two-stage approach where a common payroll system (linked to IFMIS) is first developed for MDAs and counties, and subsequently extended to Semi-Autonomous Government Agencies (SAGAs) that wholly depend on Exchequer resources is late for implementation and should be put in place to curb corruption. This should ensure quick integration of all government payment systems and ensuring that no payments are made out of IFMIS.

1.0 Introduction

At the beginning of 2021, Kenya's public debt situation was observed to be at high risk and headed to a crisis. Further, Kenya's overall macroeconomic outlook has not been pleasant over the years. Because of this, the Government of Kenya outlined measures to address the situation. It entered into an arrangement with the International Monetary Fund (IMF) on supported fiscal consolidation and structural adjustment programme. Based on this IMF supported fiscal consolidation programme and the economic conditions in Kenya, The Institute For Social Accountability (TISA), under the *Okoa Uchumi Campaign*,[1] conducted a study titled *Kenya Debt Crisis: Unpacking Fiscal Consolidation 2021*.[2] The specific objectives of the study were: to evaluate Kenya's debt composition, cost and sustainability; to assess the role of public expenditure trends in Kenya's debt; to analyse and review the monetary policy and its role in Kenya's debt crisis; and to undertake a review and analysis of the IMF fiscal consolidation programme. The study reviewed Kenya's public debt situation, tax policy and the IMF supported fiscal consolidation programme and gave recommendations.

The study found that Kenya's public debt situation was at high risk owing to consistent fiscal deficits. The stock of public debt was on the rise and stood at around 70 per cent of nominal Gross Domestic Product (GDP). Out of this, external debt accounted for over 52 per cent of the total public debt. Despite the dire need for Kenya to boost her foreign earnings to cover up for the perpetual rising debt, data shows that Kenya has been losing international market share since 2013, while the other non-resource intensive Sub-Saharan Africa countries are on average gaining market share. Equally, Foreign Direct Investments (FDI) net inflows were on a decline. It was because of an overvalued currency that Kenya's competitiveness ranking was consistently declining. The Central Bank of Kenya (CBK) was engaging in periodic foreign exchange interventions to purportedly, smooth volatility of the Kenyan Shilling. It has maintained a heavily managed exchange rate that was not flexible enough to absorb external price shocks. This was evident given that the real effective exchange rate had been on an appreciating trend over the years despite economic fundamentals showing otherwise. In addition, Kenya's public expenditure had been rising higher than the rise in revenue, propagating the

[1] Okoa Uchumi Campaign seeks to build citizen voice and demand into critical national monetary and fiscal prioritization areas where citizen voice is presently missing. It will target women, youth and other vulnerable groups that bear the brunt of poor debt governance through the deprivation of basic services and punitive taxation measures which reinforce the cycle of poverty. The campaign aims to link debt/ national revenue decisions to every-day lives of citizens as a basis for building citizen demand. The campaign will bolster civil society campaigns for political accountability in debt management, towards the sustainable resolution of Kenya's debt crisis, and the attainment of balanced budgets which support socio economic inclusion.

[2] https://resources.tisa.co.ke/2021/10/12/kenya-debt-crisis-unpacking-fiscal-consolidation/

public debt problem. Between the year 2013/14 and 2019/20, public expenditure had grown by 112.4 per cent, yet the ordinary revenue increased by 94.4 per cent over the same period.

It is based on the study's findings and the IMF-supported fiscal consolidation implementation that *Okoa Uchumi Campaign* is preparing a monitoring and reporting framework. This is to guide monitoring of the study's recommendations on Kenya's public debt and the IMF fiscal consolidation programme implementation. The framework lays out public debt components and the IMF fiscal consolidation programme, in terms of the activities to be implemented to achieve the objectives and their performance indicators. This framework will equally help in synthesising the IMF fiscal consolidation programme in terms of the goals, objectives and the activities. It will also define the relationships between factors key to implementation and articulate the internal and external elements that relate to and affect the programme's performance. This will eventually provide a monitoring framework to inform *Okoa Uchumi Campaign* efforts to track progress of the IMF fiscal consolidation programme.

1.1 Unpacking of Kenya's IMF Supported Fiscal Consolidation Programme

In April 2021, the IMF officially approved the fiscal consolidation programme for Kenya, anchored in the Extended Fund Facility (EFF)/ Extended Credit Facility (ECF) whose aim is to stabilise Kenya's economy and set a basis for a resurgence of growth and shared prosperity. The fiscal consolidation goals, objectives and their measures are summarised in Table 1.1. The table summarises the IMF fiscal consolidation programme's goals, objectives, and activities to be implemented to achieve the objectives and their indicators that will be used to show their implementation. The table also gives the status of the programme based on the first and second IMF review exercise and *Okoa Uchumi Campaign* surveillance.

Table 1.1: Unpacking Fiscal Consolidation Programme: Objectives, Measures and their Targets

IMF - FC Main Goals	Policy Objectives	Measures/Activities	Target and Indicators	Observations
Supporting the COVID-19 Response While Reducing Medium-	Policy action to cushion the impact of the pandemic and increased support for	The government to use part of the fiscal space from unwinding earlier emergency spending to extend targeted support to sectors affected by the pandemic	✓ Expand and accelerate COVID-19 vaccination campaign, with a scaled-up target of 14.5 million people by July 2022	✓ KShs 2 billion allocation in 2021/22 budget for vaccine ✓ Social protection expenditure is currently about 0.2% of GDP

Term Debt Vulnerabilities	impacted groups (Social Protection Initiatives)	(This will be through protecting health especially vaccination and immunisation programmes, and social expenditures through transfers to vulnerable groups)	✓ Priority social spending indicated on fiscal budget allocations	This shows no change from the previous allocations
	Fiscal consolidation effort that brings the primary deficit below its debt-stabilising level by 2023/2024 Financial Year and keeps the debt-to-GDP ratio on a firmly declining trend.	✓ This will be through reducing recurrent spending ✓ Gradual unwinding of emergency expenditures, reduction in the wage bill and transfers to State-Owned Enterprises (SOEs). Give only limited support to SOEs ✓ Improving the efficiency and effectiveness of government spending ✓ Strengthening Public Finance Management (PFM) systems, particularly in budget control and execution processes, cash management, and public investment management including related to Public Private	✓ Reduce recurrent expenditure from 20% of GDP in the 2020/2021 Financial Year to 17.9% in the 23/24 Financial Year ✓ Recurrent Expenditure to be 19.7% of GDP in 2021/2022 Financial Year ✓ Use of present value PV on debt to bring debt-to-GDP anchor of 55% of GDP ✓ Lower the primary balance by 1.6 percentage points of GDP ✓ Move away from commercial loans to concessional loans	✓ The borrowing of $5 billion Eurobond to be used exclusively for debt management operations that includes refinancing of the 2024 Eurobond. This is a negation of the goal of Reducing Medium-Term Debt Vulnerabilities ✓ The Amendment to the PFM Regulations to replace the current nominal legal ceiling on debt issuance (at KShs 9 trillion) with a medium-term debt-to-GDP anchor of 55% of GDP in present value (PV) terms is a zero-sum-game ✓ The amendment to the PFM Regulations could open public debt ceiling

		Partnership (PPPs) and associated fiscal risks ✓ Amendment to the PFM Regulations to replace the current nominal legal ceiling on debt issuance (at KSh9 trillion) with a medium-term debt-to-GDP anchor of 55 percent of GDP in present value (PV) terms		
	To bring the tax-to-GDP ratio back to levels achieved in recent years to generate resources to meet Kenya's development needs	✓ Strengthen revenue administration ✓ Digitisation of tax ✓ Resumption or replacement of the CMT ✓ Tax base-broadening ✓ Increase compliance	✓ Submit to Parliament a budget for the 2021/22 Financial Year consistent with the programmed deficit target ✓ Increase revenue from 12.9 % of GDP to 15.6 in 2023/2024 Financial Year ✓ 2021/2022 Financial Year tax to GDP ratio to be 13.5% ✓ Increase audits of firms, using risk-based	✓ Reversals already implemented ✓ Budget for 2021/22 Financial Year was not consistent with the programmed deficit target ✓ There is need to relook at tax holidays to companies especially in Export processing zones (EPZs) and Special Economic Zones – reduction of tax expenditures

			approaches to selected taxpayers with focus on industry sectors with large gaps in compliance identified by the IMF VAT-Gap analysis by end December 2021	
	Better prioritisation of domestically and foreign financed projects	✓ Reduce dependence on foreign financing of infrastructural projects ✓ Improve on costing	✓ Domestic mobilisation of resources ✓ Target high return expenditure	✓ No measures shown on 2021/22 fiscal budget ✓ Independent costing measures need to be adopted
Structural Reforms	To undertake a financial evaluation of the SOEs with largest fiscal risks to the 2020/21 Financial Year budget	✓ To prepare an in-depth forward-looking financial and structures evaluation of the top 15-20 SOEs representing the largest fiscal risks ✓ A strategy for addressing financial pressures in the SOE sector, including a framework for deciding on interventions ✓ Establishing a performance management	✓ An in-depth forward-looking financial evaluation of the top 15-20 SOEs representing the largest fiscal risks by May 2021 ✓ A draft blueprint that identifies necessary actions and legal reforms to enhance governance by July 2021 ✓ Developing an integrated	✓ Not met ✓ Restructuring of public universities has resulted to some increasing school fees

		monitoring and evaluation framework ✓ An expanded fiscal risk analysis that quantifies contingent liabilities from high-risk SOEs (to be included in the annual Budget Review and Outlook paper by end of September 2021)	monitoring and reporting system by September 2021 ✓ Fiscal risk analysis that quantifies contingent liabilities from high-risk SOEs (to be included in the annual Budget Review and Outlook paper by end of September 2021)	
	Promotion of fiscal transparency and accountability in SOEs	✓ This is to be achieved via publishing procurement information including beneficial ownership data of companies awarded contracts ✓ Operationalising the Access to Information Act ✓ Review of the current legal framework for asset declarations of senior public officials and conflict of interest rules	✓ Publish the audit of COVID-19 related expenditure by end of May 2021 ✓ Access to Information Act by September 2021 ✓ Beneficial ownership data be made public ✓ Reforms to strengthen the PFM systems by 2021/22 fiscal year ✓ Integration of all government payment systems and ensuring that no payment is made out of IFMIS	✓ Audits of all 2019/2020 Financial Year COVID-19-related expenditures completed. This audit report not availed to the public ✓ Kenya has a broad anti-corruption legal framework; the need is to focus on the operationalisation and implementation of these laws to detect and deter corruption ✓ There are no elaborate

		✓ Effective implementation of Anti-Money Laundering and Combating the Financing of Terrorism measures ✓ Audit of COVID-19 related spending to be published by end of May 2021 ✓ Review and strengthening of the preventive anti-corruption framework		mechanisms to ensure actions to seal identified weakness and follow-up in audits ✓ One apparent weakness is weak oversight of the PFM by Parliament
Strengthen the Monetary Policy Framework and Support Financial Stability	The CBK to publish a white paper by end of June 2021 outlining planned reforms to improve the monetary policy framework drawing on inputs from many sources	✓ Medium-term inflation target of 5% and ±2.5 percentage point band ✓ Commercial banks to consult the CBK for approval of dividend payments ✓ Law to be in place to enable the CBK to regulate and supervise non-bank digital lenders and to enhance the regulatory and supervisory framework for microfinance institutions	✓ Inflation target of 5% and ±2.5 percentage point band ✓ CBK white paper by end of Financial Year 2021/2022	✓ Need to review the foreign exchange policies and make it more competitive ✓ Move on dividends payments is illegal as this should be a share holders' decision. Risks legal challenges ✓ The monetary policy should be more responsive to promotion of domestic production

		✓ The CBK to strengthen its macroeconomic modelling and forecasting frameworks		
Data	Enhanced economic statistics with a range of new statistical surveys	✓ General government fiscal outturns on a quarterly basis by June 2022 ✓ Annual fiscal data of the public corporation sector by December 2021 ✓ Migration of the fiscal framework to GFSM 2014 by December 2021 ✓ Monthly, quarterly and annual GFS for public sector are compiled according to GFSM 2014 and disseminated on a timely basis	✓ General government fiscal outturns on a quarterly basis by June 2022 ✓ Annual fiscal data of the public corporation sector by December 2021 ✓ Migration of the fiscal framework to Government Finance Statistics Manual 2014 (GFSM 2014) based concepts by December 2021	✓ Some adjustments on these targets have been forwarded to IMF and have been accepted ✓ Meeting these targets will go a long way in harmonisation of the data availed to the public by various government agents

Source: *IMF, 2021*

The fiscal consolidation programme is based on Kenya undertaking various governance and structural reforms as observed in Table 1.1. One of the conditions for this facility was for Kenya to fully implement fiscal consolidation policies and within the timeframe. This agreement is underpinned by highlighted undertakings which are anchored in a robust monitoring and reporting framework by the IMF. In monitoring the programme performance, the National Treasury and the CBK are required to provide to the IMF the information at the frequency and within the reporting deadlines specified under the programme arrangements. The National Treasury and the CBK transmit promptly to IMF any revisions done on the programme. For any information (and data) that is (are) relevant for

assessing performance against programme objectives but is (are) not specifically defined in the programme, the National Treasury and the CBK will consult IMF. The National Treasury and the CBK will transmit promptly to IMF staff any data revisions, as well as other information necessary to monitor the arrangements with the IMF. The IMF committed to support the programme within 38-month EFF and ECF arrangements which will have quarterly reviews.

2.0 The Okoa Uchumi Campaign Monitoring and Reporting Framework

The *Okoa Uchumi Campaign* prepared a report titled *Kenya's Debt Crisis: Unpacking Fiscal Consolidation 2021* that reviews Kenya's public debt situation, tax policy and the IMF fiscal consolidation and gives recommendations. The specific concerns of the study were: Public debt risks stemming largely from fiscal deficits, foreign borrowing and cost of borrowing; Prudent fiscal management whose main concern included development-recurrent budgeting in line with the Public Finance Management Act (PFMA), public debt finance use, adherence to prudent public finance management and commitment to the law in public finance; Use of monetary policy with main concerns including how monetary policy has been used in promoting productivity and competitiveness in Kenya; the IMF proposals, and the extent to which they address Kenya's debt and fiscal distress.

Most importantly, the report identifies significant asymmetries in Kenya's IMF-supported fiscal consolidation and structural adjustment programmes that are already having dire consequences on the economy. The report made it findings which included: The risky borrowing behavior; Kenyans being overtaxed; monetary policy effectively subsidising imports; the rapid build-up of public debt; and the fiscal consolidation policies and structural adjustment programmes that may not be consistent with Kenya's macroeconomic environment. The study then made recommendations based on the findings.

Table 2.1 summarises the study's goals, objectives and the findings. It is on the basis of the findings that a baseline is developed, and their indicators used to form the monitoring baseline. Table 2.1, therefore, forms the monitoring and reporting framework.

Table 2.1: Kenya Debt Crisis: Unpacking Fiscal Consolidation, 2021 Study's Findings and Monitoring and Reporting Framework

Goal	Objectives	Findings	Baseline	Indicators
Sustainable Public Debt	Management of the Fiscal Deficit	Fiscal Deficit is on an expansion path. The deficit is higher than annual economic growth causing the public debt risk	✓ Budget Deficit as a % of GDP is at 14% ✓ Fiscal Balance (% of GDP) stands at 7.8%	✓ Budget Deficit as a % of GDP ✓ Fiscal Balance (% of GDP)
	Foreign Borrowing and public debt	Foreign borrowing has been on the rise and has surpassed	✓ Foreign Debt at KShs 3.516 trillion (52% of	✓ Foreign Debt as % of Total Debt ✓ External Debt (%

		domestic. This borrowing is largely on project finance debt	External Debt) (35.6 % of GDP) ✓ BOP position is a deficit of KShs 152.5 billion in 2020	of GDP) ✓ Amount of BoP deficit in each year
	Cost of Borrowing and public debt	There has been an increase in use of commercial debt and cost of borrowing	✓ Commercial loans at 36.25% of foreign debts	✓ Commercial loans as % of foreign debt
Prudent Fiscal Management	Government borrowing and development expenditure	Government is borrowing to finance recurrent expenditures	✓ 78% allocation on Recurrent Expenditure against 22% on Development Expenditure	✓ % of fiscal budget allocation to development and recurrent expenditure
	Supplementary budgeting and public participation	Fiscal Budget undergoes mutilation through numerous supplementary adjustments without public participation	✓ Supplementary budgets within a financial year needs to be capped to a maximum of one	✓ No. of supplementary budgets in a financial year
	Commitment fees and prudent fiscal management	High wastages noted to be incurred through commitment fees	✓ As of 30th June 2021, the Government paid KShs1.7 billion on commitment fees	✓ Reporting of commitment fee ✓ Total commitment fees in a financial year
	Strict observance of the budget execution rules and regulations	Over 70% of budget allocation done to recurrent expenditure Fiscal Budget overshooting over the years. A minimum of 30% of the budget not being allocated to development expenditure	✓ Section 15 of the PFM Act not being adhered to	✓ Planned vs Implemented Budget (% Deviation) ✓ % of budget allocation to development

	Transparency and accountability and fiscal management	Most of data, especially on commercial loans, not available to the public IMF and government agreements are not open for public scrutiny There is weak oversight by Parliament	✓ Access to Information Act to be in place by September 2021 ✓ Beneficial ownership data to be made public ✓ Reforms to strengthen the PFM systems to be done by 2021/22 Financial Year ✓ No public payment is made out of IFMIS	✓ Access to Information Act in place ✓ Beneficial ownership data available to the public ✓ Reforms conducted on PFM Act ✓ All government payment systems using IFMIS ✓ Actions taken on the audit reports
Prudent use of Monetary Policy	Monetary Policy and Productivity in Kenya	Kenya uses monetary policy mainly to manage its exchange rate	✓ Broad Money Expansion (% of Change) stands at 10.6	✓ Broad Money Expansion as % of Change
	Monetary Policy and Competitiveness in Kenya	There is decreased costs of imports and increased international prices on domestically produced goods	✓ Current Account (% of GDP) stands at -4.8 ✓ Overvalued REER	✓ Current Account (% of GDP) trend
IMF-supported Fiscal Consolidation Programme	Macroeconomic Stabilisation	IMF expects the economy to recover in the Financial Year 2021/2022 to above 6% The Public Expenditure expected to decline to below 23 % in 2023 Fiscal Balance (% of GDP) to reduce to below 5% in 2023	✓ Real GDP Growth observed to be at -0.1 ✓ Public Expenditure stands at 25% of GDP ✓ Fiscal Balance at 7.8% of GDP ✓ Debt-to-GDP ratio at 70% ✓ Commercial debt at 36% of foreign borrowing ✓ 40:60 in reference to	✓ Real GDP Growth Rate per financial year. ✓ Expenditure (% of GDP) ✓ Fiscal Balance as % of GDP ✓ Debt-to-GDP ratio per financial year. ✓ Commercial loans as % of total debt ✓ Tax-to-GDP ratio at 15.6% in 2023/2024 Financial Year

		Keep the debt-to-GDP ratio on a firmly declining trend Bring the tax-to-GDP ratio to 15.6% in FY23/24 Reduce recurrent spending to 17.9% in Financial Year 2023/2024 Government is to limit recurrent spending and better prioritise	domestic vs foreign borrowing ✓ Budget Deficit as a % of GDP is at 14% ✓ Fiscal Balance (% of GDP) stands at 7.8%	✓ Recurrent spending at 17.9% in 2023/2024 Financial Year
	Support to the response to COVID-19 shock	Government expected to protect health and social expenditures There will be transfers to vulnerable groups Prioritise on vaccination and immunisation programmes	✓ Expenditure to health as % of total expenditure is at 26% ✓ Expenditure to social protection as % of total expenditure is at 0.2%	✓ % Allocation to Social Sector per financial year ✓ Total Transfer payments to OVCs ✓ Total no. vaccinated against COVID-19
	Governance	Government commits to promote Fiscal Transparency Operationalising the Access to Information Act	✓ Publication of procurement information including beneficial ownership data of companies awarded contracts ✓ To review the current legal framework for asset declarations of senior public	✓ Publication of procurement information data of companies awarded contracts by end of Financial Year 2021/2022 ✓ Review of the current legal framework for asset declarations of senior public officials and conflict of

			officials and conflict of interest rules ✓ Comprehensive review of tax-exempt products ✓ Achieving processing of all compliant customs entries within 24 hours	interest rules by December 2021 ✓ By December 2021, complete a comprehensive review of end-use of exempt products ✓ By June 2021, achieving processing of all compliant customs entries within 24 hours
	Strengthen revenue administration	Tax mobilisation is to be achieved through tax reversal, repeal of the bulk of the emergency tax cuts introduced in April 2020, expedition of judicial procedures to collect outstanding tax debts and broadening tax base	✓ Removal of tax exemptions ✓ CMT introduction and court ruling ✓ Tax revenue at 13% of GDP ✓ Broadening of tax base ✓ Review of tax exemptions	✓ Total revenue as a percent of GDP increment from 13% ✓ New tax revenues from expanded tax base ✓ Repeal of tax exemptions ✓ Reporting of tax expenditures

Source: *Campaign Platform, 2021*

The indicators in Table 2.1 will be followed and reported against as per the target. The reporting will entail recording whether the target is met, partially met, or not met. The data as recorded in the official government data will be utilised and compared to all other data from various sources like IMF and primary data collected by the platform. The results will then inform the conclusion of the status of programme implementation.

3.0 Review, Observations and Effects of the Fiscal Consolidation Programme Implementation

It is upon the *Okoa Uchumi Campaign* Monitoring and Reporting Framework and the first review by the IMF of the fiscal consolidation programme that the following observations have been derived and the effects that have emanated in the process of programme implementation discussed. Table 3.1 gives the baseline as from Table 2.1 (monitoring and reporting framework), observations and the expected outcome over the programme implementation period.

Table 3.1: Fiscal Consolidation Implementation Indicators

Indicators	**2020**	**2021**	**2022**	**2023**	**Status (2021)**
Real GDP Growth	-0.1	7.6	5.7	6.1	Not Met
Inflation	5.3	5.0	5.0	5.0	Met
Revenue (% of GDP)	13.2	17.0	16.8	17.6	Not Met
Expenditure (% of GDP)	25.0	25.7	24.3	23.5	Not Met
Fiscal Balance (% of GDP)	-7.8	-8.7	-7.5	3-5.8	Not Met
Public Debt (% of GDP)	65.8	70.4	72.6	72.9	Not Met
Broad Money Expansion (% of Change)	10.6	11.8	10.6	11.4	Met
Credit to Private Sector (% of Change)	7.7	7.7	7.8	10.1	Met
Current Account (% of GDP)	-4.8	-5.3	-5.4	-5.5	Met
Reserves (in months of imports)	4.6	4.6	4.3	4.1	Met
External Debt (% of GDP)	35.6	37.8	37.6	36.7	Met

Source: IMF, 2021

The red marked indicators are in the monitoring and reporting framework (in Table 2.1). Under the programme, solid growth is expected over the programme period. This is despite a slowdown in 2020 driven by the global COVID-19 shock and the downturn on the economy experienced before the pandemic. This is expected to largely be the case even to the end of 2021. The target is therefore indicated as not met. The programme places the recovery up-look on manufacturing and services, particularly education, transportation and trade (wholesale and retail). The expected growth, according to IMF and Kenyan Government, is in line with the historical trend. The expectation under the baseline was that the economy will rebound from the COVID-19 shock and will settle at its potential growth (roughly 6 per cent) over the medium to long term. This is based on the premise that the poor economic performance (-0.1) experienced in 2020 was due to the pandemic. However, the *Okoa Uchumi Campaign* pinned the problem largely on unproductive economy that largely depends

on imports. The expected economic growth rate of 7.6 could therefore be overenthusiastic given that the main fundamental concerns are yet to be addressed. Other indicators in the monitoring and reporting framework and their effects are discussed below.

A. Reduction of Public Debt

Reduction of public debt is to be attained through consistent reduction of public deficit, reduction of the foreign borrowing and reduction in the cost of borrowing. Fiscal deficit increased from 7.8 in the 2020/2021 Financial Year to 8.7 in the 2021/22 Financial Year. Consequently, the gross public debt increased to KShs 7.7 trillion as of 30th June 2021. The stock of debt comprises 52.1 per cent external debt and 47.9 per cent domestic debt, an increase from the previous period. Therefore, the targets on reducing public debt through reduced fiscal deficit and foreign borrowing were not met. The fiscal balance as a percentage of GDP is therefore going to expand in the period. Interestingly, inasmuch as the programme is meant to address the public debt problem, it has permitted public debt to expand as a percentage of GDP over the programme period.

In terms of foreign borrowing and restraint from commercial borrowing, out of the KShs 7.7 trillion public debt stock, a third of it is made up of commercial debt such as Eurobonds and syndicated loans. The burden of servicing these debts that are dollar-dominated from dollar exports is increasingly becoming a burden after crossing the recommended threshold. This means, that the country's debt sustainability in the short-term is off track and the target thereof not met. Table 3.2 represents the recent public debts trend.

Table 3.2: Public Debt Trend (KShs Million)

Year	Month	Domestic Debt	External Debt	Total
2021	June	3,697,093.18	4,015,299.38	7,712,392.57
2021	May	3,686,891.72	3,799,018.81	7,485,910.53
2021	April	3,632,914.80	3,778,131.44	7,411,046.24
2021	March	3,569,840.57	3,769,866.74	7,339,707.31
2021	February	3,531,182.93	3,814,288.77	7,345,471.70
2021	January	3,532,561.52	3,819,699.66	7,352,261.18
2020	December	3,488,541.18	3,793,285.24	7,281,826.42
2020	November	3,482,653.56	3,771,808.47	7,254,462.03
2020	October	3,457,644.63	3,705,644.24	7,163,288.87
2020	September	3,457,106.50	3,663,491.22	7,120,597.72
2020	August	3,402,500.73	3,666,321.29	7,068,822.02

2020	July	3,273,551.44	3,638,506.49	6,912,057.93
2020	June	3,178,421.28	3,515,810.78	6,694,232.06
2020	May	3,153,143.94	3,496,428.84	6,649,572.77
2020	April	3,119,415.80	3,317,330.98	6,436,746.77
2020	March	3,070,189.38	3,212,634.23	6,282,823.61
2020	February	3,040,964.55	3,117,038.57	6,158,003.12
2020	January	3,003,700.30	3,112,897.95	6,116,598.25

Source: *CBK, 2021*

Public debt had surged to KShs 7.7 trillion by June 2021, driven mainly by foreign debt. The foreign debt increased from KShs 3.8 trillion in 2020/2021 Financial Year to KShs 4 trillion in the current Financial Year 2021/2022. This increase in foreign debt emanated from the issuance of a Eurobond, a commercial debt. Kenya is now at elevated risk of debt distress as determined by the IMF. Addressing the emerging fiscal and public debt vulnerability risks would require considering the domestic market productivity that will also enhance revenue.

B. Prudent Fiscal Management

Prudent fiscal management can be achieved in several ways including allocating government borrowings to development expenditure only, capping the numbers of supplementary budgets, elimination of commitment fees, strict observance of the budget execution rules, transparency and accountability. This means strict adherence to the principles of fiscal responsibility.

The *Kenya Debt Crisis: Unpacking Fiscal Consolidation 2021* report showed an upward trajectory of national government recurrent expenditure. The high proportion of recurrent expenditure in the national budget is said to be highly unsustainable and a ticking time bomb. From the Financial Year 2014/2015 the recurrent expenditure accounts for over 70 per cent of the national budget which is contrary to the Public Finance Management Act, 2012 which stipulates that over the medium term a minimum of 30 per cent of the national and county government's budget shall be allocated to the development expenditure. This has not been the case with development expenditure falling below 20 per cent from 2017/2018 Financial Year to 2020/2021 Financial Year. Thus, there is an urgent need to enforce this threshold to ensure that recurrent expenditure has a ceiling of 70 per cent as provided for in the Public Finance Management Act, 2012. The realignment of expenditure from recurrent to development would release resources to development programmes that would yield significant economic returns. The National Treasury calculates the ratio of recurrent to development

expenditure using total ministerial expenditure to adhere to fiscal responsibility principles. However, the allocation to development expenditure as a percentage of the total national expenditure is 22 per cent and therefore does not conform to the Public Finance Management Act, 2012. The indicator is therefore not met.

From the Controller of Budget Report 2021, a total of KShs 70,167,610,083.00 from Sovereign Bond Proceeds was realised and National Treasury allocated it as follows:

Table 3.3: 2021/2022 Actual Recurrent and Development Budget Allocation

	Amount (KShs)	Percentage
RECURRENT	18,158,971,684.65	29.52
DEVELOPMENT	120,951,111.60	0.20
PD.79	367,584,701.55	0.60
PG.029	15,973,626,828.50	25.96
C/REQ.057/20/21	26,902,500,000.00	43.73

Source: *Controller of Budget, 2021*

This contravenes the Constitution Article 201(c) and section 15(2)(c) of the Public Finance Management Act, 2012 which states that: *"Over the medium term, the national government's borrowings shall be used only for the purpose of financing development expenditure and not for recurrent expenditure".* The National Treasury should therefore ensure all requests are in line with Constitution Article 201(c) and section 15(2)(c) of the Public Finance Management Act, 2012.

The payment of commitment fees continues to rise *(a fee that a lender may charge a borrower to whom it has agreed to extend credit, generally charged for lines of credit not yet used, the commitment fee is a way of guaranteeing the bank will keep the funds available)*. This shows the inefficiency of the implementing agency that has been granted the loan in their effective absorption of the funds in completion of their projects. As of 30th June 2021, the Kenyan Government paid KShs 1,657,544,758.23 as commitment fees on loans that had not been utilised even after signing of loan agreements. The indicator is therefore not met.

The Kenyan Government in agreement with IMF, is to develop a medium-term debt anchor of 55 per cent of GDP in present value (PV) terms. The government and IMF argue that the debt-to-GDP ratio in PV terms for countries like Kenya where a significant share of borrowing is on concessional terms, measuring debt in PV terms, gives a more accurate picture of the burden represented by a given level of debt. It is however noted that the government intends to create further borrowing room given that the current public debt ceiling of KShs 9 trillion is almost reached. The public finance

management principles require transparency and accountability by the National Treasury to Parliament and the public on its plans and progress towards achieving the public debt anchor within a specific timeframe. The Public Finance Management Act, 2012 and Public Finance Management Regulations, 2015 set the statutory debt ceiling at KShs 9 trillion. The 2021 Medium Term Debt Strategy proposes to expand the statutory public debt limit to accommodate the fiscal deficits in the 2021/2022 Financial Year and into the medium term. This is against the spirit of lowering the public debt.

C. Prudent Monetary Stance that Promotes Domestic Production and Competitiveness

The *Kenya Debt Crisis: Unpacking Fiscal Consolidation 2021* report notes that Kenya uses monetary policy to manage its exchange rate. When there is pressure on currency to depreciate, CBK mops excess liquidity to curtail aggregate demand. Although this safeguards Kenya against the risk of the exchange volatility, it denies Kenya the gain from depreciation of the Kenya Shilling. The gain would emanate from increased costs of imports and reduced price on exports. Broad Money Expansion (% of Change) of 10 and 11 per cent, shown in Table 2.1, is in line with the programme objective of inflation target. However, this will not stimulate productivity in Kenya and therefore, will make the current account remain unfavorable, increase external debt as predicted and indicated in Table 3.1. This will then prompt borrowing to maintain the foreign reserves at four months of imports as is the requirement of the programme. Kenya's goods are coming under pressure from foreign products. This data is shown in Table 3.4.

Table 3.4: Monetary Indicators

	Overall Liquidity	M1	ER (KShs/$)	Import Cover (Months)	Curr Acc Bal ($ B)	Credit to Gvt (Annual Growth)	Credit to Prv Sct (Annual Growth)	Lending rate	Imports (KShs B)
Jul (20)	14.1	11.4	107.27	5.9	-4.8	32.1	7.8	11.94	121.6
Aug (20)	14.6	12.7	108.14	5.6	-5	36.1	8.2	11.94	138.8
Sep (20)	14.2	14.1	108.41	5.4	-4.9	33.7	7.6	11.75	137.8
Oct (20)	15.2	17.8	108.64	5.1	-4.9	39	7.6	11.98	143.4
Nov (2)	17.5	20.5	109.25	5	-4.8	47.4	8.1	11.99	145.2
Dec (20)	17.3	12.8	110.59	5.1	-4.6	42.7	8.4	12.02	139.1
Jan (21)	17.7	12.6	109.83	4.9	-4.4	35.7	9.3	12	161.5
Feb (21)	15.8	10.6	109.68	4.8	-4.5	32.6	9.6	12.02	160.7
Mar (21)	13.5	7.6	109.73	4.7	-4.9	35.7	7.7	12.05	159.7
Apr (21)	13.3	7.7	107.95	4.8	-5	236.9	6.7	12.08	187.1
May (21)	11.8	7.8	107.43	4.8	-5.2	44	7.1	12.06	161.8
Jun- (21)	10.9	5.1	107.81	6.1	-5.5	22.4	7.7	12.02	162.2
Jul (21)	11.1	6.3	104.14	5.9	-5.7	26.9	6.1	12.09	

Sources: CBK, 2021

Table 3.2 shows some of the macroeconomic indicators in the country as observed by the Kenya National Bureau of Statistics (KNBS) and Central Bank (CBK) over the period July 2020 to July 2021. The imports are on the rise as shown in the table. This is so even as imports cover depicts an increase showing borrowing needs. The imports are favoured by the strong Shilling that is supported by the contractionary monetary policy indicated by the country declining liquidity and M1. Current account, consequently, is on a decline owing to increase in imports. The lending rates, however, are at their lowest but not helping to stimulate private sector credit uptake. This concept is to a considerable extent ignored in the fiscal consolidation programme. This would give an indication that the monetary policy needs a refocus. The *Kenya Debt Crisis: Unpacking Fiscal Consolidation 2021* report is, therefore, said to conflict with IMF supported fiscal consolidation programme on this aspect.

D. IMF-supported Fiscal Consolidation Programme

From the general observation of the IMF-supported fiscal consolidated programme, Table 3.5 gives the base of selected macroeconomic indicators and their expected performance in the process of the programme implementation.

Table 3.5: Selected Macroeconomic Indicators and their Projections

Indicator	2019	2020	2021(Projection)	2022 (Projection)
Real GDP Growth (%)	5.4	-0.1	6.3	6.4
Inflation Rate (Average)	5.2	5.3	5.5	5.0
Revenue (% of GDP)	18	17.2	17.1	17
Expenditure (% of GDP)	25.7	25	27.7	24.6
Fiscal Balance (% of GDP)	-7.7	-7.8	-8.6	-7.5
Public Debt (% of GDP)	62.0	65.8	70.6	73.0
External Debt (% of GDP)	31.5	35.6	38.5	38.4
Current Account (% of GDP)	-5.8	-4.6	-5.3	-5.5
Reserves (in months of import)	6.1	4.7	4.8	4.4
REER (% change)	-2.6	-3.2	-1.5	

Source: *IMF (2020)*

The IMF indicators as shown in the table are used in evaluating the performance and the conditions prescribed under the Indicative Targets (IT), Performance Criteria (PC) and Structural Benchmarks (SB). The Projections of Kenya's economic growth rate are currently highly uncertain. The economic outcome will hinge on how the pandemic plays out internationally and within Kenya, along with policy actions, and the responses of households and firms. The spread of more

infectious COVID-19 variants, coupled with political uncertainty ahead of the August 2022 presidential elections, clouds the outlook. The focus that projects GDP growth of 5.3% in 2021 and 5.4% in 2022, which is down 0.1 percentage points looks unrealistic. The elevated uncertainty regarding the growth outlook makes it appropriate to consider different plausible scenarios, and their implications for the economy.

Kenya's public debt continues to surge. In the initial stages, reduction of government spending and cost cutting measures were promoted. The National Treasury revised its borrowing numbers in the current financial year from KShs 800 billion to KShs 1 trillion to cover the expected tax revenue shortfall. This is in addition to further commercial borrowing. With this trend, the programme risks running to the results of previous SAPs.

It is worth noting that in the process of implementation of the programme, some social programmes are going to be affected and this is already working against the objectives. Some of these programmes include higher education. In an assessment of public universities in February 2017, the Auditor General listed 11 of the country's institutions of higher learning as being insolvent. Public universities rely largely on government funding to meet their financial needs, but the subsidies have not matched the growth in student numbers and inflationary changes, leaving them with deficits. This has been made worse by depressed revenues from the parallel programme (privately funded students). Currently, the government can only meet about 61 per cent of the total cost of a degree programme in public universities, while those in private universities are funded at about 32 per cent. The remaining 40 per cent is shared between parents and the universities. For the Financial Year 2021/2022, the government slashed funding to its public universities by US$400 million. The universities were given US$1.13 billion, down from the US$1.53 billion the government planned to spend. This has left public universities with no option but to increase school fees. The University of Nairobi has taken lead on this and has doubled the school fees in the current academic year. Other public universities are in the process of doing the same. Additionally, it is observed that, even though public universities in Kenya are struggling financially and having underutilised capacity, the government continues to sponsor more that 50 percent students to private universities through the Kenya Universities and Colleges Central Placement Service (KUCCPS), a State Corporation that is meant to provide career guidance and select students for admission into universities in Kenya.

On taxation, expecting revenue growth of 17 per cent of GDP from the current 13.2 per cent is equally a long shot. The history, as elaborated in the *Kenya Debt Crisis: Unpacking Fiscal Consolidation 2021* report, shows an unproductive tax system existing in Kenya especially on direct taxes. This is further shown on Table 3.6.

Table 3.6: Performance of Tax Revenue in Kenya – 2012/13 to 2020/21

Year	Pay As You	Other Income	VAT	Excise Duty	Import Duty	Other	Total Exchequer	GDP*
2012/13	211,061	182,981	183,219	88,030	57,897	36,323	759,511	4,536,001
2013/14	252,974	200,710	233,558	104,698	66,596	60,446	918,982	5,079,670
2014/15	277,068	229,066	264,872	114,952	73,733	62,283	1,021,974	5,849,132
2015/16	312,032	248,988	290,843	142,591	80,966	61,412	1,136,833	6,734,060
2016/17	336,596	291,452	336,572	163,236	86,861	58,343	1,273,060	7,794,026
2017/18	364,104	278,277	356,777	168,062	93,713	79,314	1,340,248	8,468,218
2018/19	392,693	296,042	409,526	195,731	105,209	75,472	1,474,673	10,030,206
2019/20	399,411	307,739	383,713	198,032	151,274	92,071	1,532,236	10,752,992
2020/21	376,991	308,022	481,612	244,807	162,704	95,695	1,669,832	
Percentage Contribution of Total Revenue								
2012/13	27.80%	24.10%	24.10%	11.60%	7.60%	4.80%	100.00%	16.70%
2013/14	27.50%	21.80%	25.40%	11.40%	7.20%	6.60%	100.00%	18.10%
2014/15	27.10%	22.40%	25.90%	11.20%	7.20%	6.10%	100.00%	17.50%
2015/16	27.40%	21.90%	25.60%	12.50%	7.10%	5.40%	100.00%	16.90%
2016/17	26.40%	22.90%	26.40%	12.80%	6.80%	4.60%	100.00%	16.30%
2017/18	27.20%	20.80%	26.60%	12.50%	7.00%	5.90%	100.00%	15.80%
2018/19	26.60%	20.10%	27.80%	13.30%	7.10%	5.10%	100.00%	14.70%
2019/20	26.1%	20.1%	25%	12.9%	9.9%	6.0%	100.00%	14.2%
2020/21	22.6%	18.6%	28.8%	14.9%	9.7%	5.9%	100.00%	13%

Source: *KNBS, Economic Survey, 2021*

From the table, income tax accounts for over 48 per cent of the total exchequer revenue. It is followed by VAT. Income tax shows a decline from 28 per cent for PAYE and 24 per cent for other income taxes all through from the Financial Year 2012/2013 to 22.6 per cent and 18.6 per cent in 2020/2021 respectively, mirroring declining performance in direct tax. This is despite tax policy reforms that have been implemented. Consequently, tax effort is on the decline even as GDP rises, a clear case of an unproductive tax system. Kenya's low tax efforts could be due to factors such as inadequate fiscal policy, low taxable capacity of the economies, leakages in revenue collection and weak enforcement and a large informal sector. It could also mean that high tax rates are pushing some sectors to informal sector to avoid high tax. The below par performance in the estimated potential emanates from declining tax efforts in direct taxation. Therefore, more effort is required

towards identifying more revenue mobilisation opportunities in this area to enable the country to attain higher revenue collection to finance its development needs and promote economic growth. This should be implemented by reviewing the tax expenditure in the country. According to the 2021 Tax Expenditure Report, Kenya incurs more than KShs 400 billion annually in tax expenditures. This is the case even when tax incentives given to Export processing zones (EPZs) and the Special Economic Zones are not considered. There is, therefore, need to conduct serious cost-benefit-analysis of the investment's incentives given in the country.

According to the Controller of Budget, during the 2020/2021 Financial Year, the total tax collected was KShs 1.5 trillion while the total public debt exchequer issues was KShs 863 billion, which constitutes about 58 per cent of the total tax collected. This shows that 58 per cent of tax revenue collected was spent towards public debt, leaving less funds towards other national budget votes. The Controller of Budget recommends renegotiating of public debt repayment agreements and slowing down of borrowing to ensure tax revenue collected is geared towards financing other components of the national budget.

The Controller of Budget also highlights instances in the year 2021 where the National Treasury borrowed from the domestic market to repay foreign debt. For instance, on 16th August 2021 PD:010/2021/2022 - Public Debt Repayment Request amounting to KShs 15,035,407,020.70 The National Treasury borrowed (T-Bonds of Kshs.15,035,407,020.70) from domestic market to repay foreign debt of which substantial amount (98 per cent) was towards syndicated loans repayments.

4.0 Conclusion and Recommendations

Based on the review and observations on the fiscal consolidation programme implementation, the following are the conclusions and recommendations:

1. Kenya's public debt continues to rise. As at the end of June 2021, the total public debt stock was KShs 7.7 trillion, an increase from KShs 6.7 trillion in June 2020, resulting to a public debt of 72.6 per cent of GDP in 2021/2022 Financial Year from 70.2 per cent of GDP in 2020/2021 Financial Year.
2. On foreign borrowing and restraint from commercial borrowing, the review finds that the foreign debt increased from KShs 3.8 trillion in the 2020/2021 Financial Year to KShs 4 trillion in the current financial year. The increase in foreign debt emanated from Kenya's fourth Eurobond issuance, a commercial debt.
3. The proposal to amend the Public Finance Management Regulations, 2015 to replace the current nominal legal ceiling on public debt issuance (that is KShs 9 trillion, and close to being reached) with a medium-term debt-to-GDP anchor of 55 per cent of GDP in present value (PV) terms will serve to create more room for government borrowing. The country choosing a nominal legal ceiling on public debt, or a medium-term debt-to-GDP will not resolve the underlying public debt problem. The root cause of the public debt problem must be addressed, and these include poor oversight mechanisms, value for money challenges in public projects, weaknesses in planning, budgeting, and execution.
4. The recurrent expenditure continues to account for over 70 per cent of the national budget which is contrary to the Public Finance Management Act, 2012, and the National Treasury continues to violate the law in this regard.
5. As of 30 June 2021, the national government paid KShs 1.7 billion on commitment fees on loans that have not been utilised, yet loan agreements have been signed.
6. The broad money expansion of 10 and 11 per cent is in line with the fiscal consolidation programme objective of inflation target. However, this continues to make current account unfavorable, uncompetitive exchange rate continues and therefore the persistent need for external debt and wasteful need to maintain foreign reserves at four months of imports. In cases where the reserves are low, borrowing is being used to increase reserves. This can simply be evaded by freely floating exchange rate. The flexible exchange rate should serve as

a shock absorber, strengthening external sector resilience. Inflation-Focused Monetary Policy continues to make the economy unproductive.

7. Kenya’s goods are coming under pressure from foreign product, and this is evident from the expanding current account deficit. The current account deficit is expected to expand as projected from the current minus 4.6 to minus 5.5 by the end of the fiscal consolidation programme.
8. Kenya's export earnings are expected to decline even in the next financial year from 10.1 per cent in 2020/2021 to 9.9 per cent in 2021/2022. This is together with remittance by Kenyans in the diaspora, which has been a key source that has provided stability to the Shilling, but which has been hit hard by the COVID-19 pandemic. This means that financing of dollar-dominated public debt will remain a burden on the taxpayer. This can be avoided when the economy is promoted to largely produce to meet its domestic demand.
9. Fiscal deficit increased to 8.7 in the 2021/2022 Financial Year from 7.8 per cent of GDP recorded in the previous Financial Year 2020/2021.
10. 64.1 per cent of tax revenue collected is spent towards public debt servicing, leaving less funds towards other budget votes.
11. Despite the high cost of production emanating from high taxation and more so on inputs, the Government of Kenya is unable to use taxation as a means of lowering cost of production to keep up the need to raise revenue as demanded in the programme conditions. Taxation in Kenya is majorly about tax revenue collection with little regard to the impact on businesses and households. This makes Kenya unattractive to both domestic and foreign investors. Some examples of harmful taxes affecting manufacturers are minimum tax (currently in court), VAT on plant and machinery, annual inflation adjustment for excisable goods in Kenya and excise duty on plastic packaging and resins. This also harms the final consumers.
12. The government is incurring over KShs 400 billion in tax expenditure annually. This emphasises the importance of transparent disclosures of tax expenditures, especially considering the underperformance of revenues in recent years and the growing pressures on controlling the budget deficit. The KRA cites tax expenditures as a major impediment to its ability to meet revenue targets, with tax expenditures estimated at KShs 478 billion in 2017.

13. The government is pursuing revenue-based fiscal consolidation to stabilise public debt. The effect of this is a reduction of aggregate demand in the economy, resulting to further contraction. This is evidenced by economic indicators available in 2021.
14. The placement of government sponsored students to private universities through the Kenya Universities and Colleges Central Placement Service (KUCCPS), a State Corporation, needs to be stopped. Instead, government-sponsored students should be placed in public universities to utilise the idle capacity being experienced in public universities. Additionally, reforms should be geared towards improving governance in these institutions while safeguarding the objective of access to education by poor students. Any reform must be carefully evaluated given that universities play a critical role in human capital development.
15. The audit of all COVID-19-related expenditures in 2019/2020 Financial Year has been completed, including audits of all spending by MDAs, and forensic audits of COVID-19 funds utilised by National Government entities, Kenya Medical Supplies Authority (KEMSA) and counties. The IMF notes that the production of multiple audits has provided a high degree of transparency, notwithstanding the short delay in publication of the final audits. While KEMSA published reports with information on awarded contracts and beneficial ownership of the companies, the Public Procurement Information Portal is yet to publish beneficial ownership information. This key planned step should be implemented as a matter of priority. The KEMSA audit found numerous violations of public procurement and the public finance management law and inefficiencies in the procurement process. Call is made that the Director of Public Prosecution opens charges against individuals involved. There is need for the public to know the consequences of adverse reports and the mechanisms to ensure programmatic actions to seal identified weaknesses and follow-up on the same.
16. The IMF recommends to the government that the public consultations on the regulations to enable implementation of the Access to Information Act, 2016 be followed by tabling in Parliament for swift approval. Additionally, the government should finalise the review of the legal framework on asset declarations and conflict of interest rules for senior public officials that was due in September 2021, hence the need for government to move quickly to effectively adopt and operationalise the system as directed by IMF. This should be done in a transparent manner to expose corruption.

17. The national government proposal to adopt a two-stage approach where a common payroll system (linked to IFMIS) is first developed for MDAs and counties, and subsequently extended to SAGAs that wholly depend on Exchequer resources is late for implementation and should be in place to curb corruption. This should ensure quick integration of all government payment systems and ensuring that no payment is made outside IFMIS.

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