Mbaya & Associates

CERTIFIED PUBLIC ACCOUNTANTS (K)

Table of Contents

SIGNIFICANCE OF AGRICULTURE IN KENYA'S ECONOMY

INTRODUCTION

- Agriculture is the art and business of cultivating soil, producing crops and raising livestock.
- Agribusiness denotes the collective business activities that are performed from farm to fork. It covers the supply of agricultural inputs, the production and transformation of agricultural products and their distribution to final consumers. Agribusiness is one of the main generators of employment and income worldwide.
- Agribusiness is characterized by raw materials that are mostly perishable, variable in quality and not regularly available. The sector is subject to stringent regulatory controls on consumer safety, product quality and environmental protection. Traditional production and distribution methods are being replaced by more closely coordinated and better planned linkages between agribusiness firms, farmers, retailers and others in the supply chains.

Historical Development in Agribusiness

- According to a World Bank report in 2013, stated that about two thirds of the world population poor are mainly concentrated in rural areas, which are predominantly agriculture-oriented areas. Therefore in respect to poverty eradication and raising the welfare standards of the population; more focus should be put on transitioning from subsistence agriculture to agri-business.
- Business management is aimed at developing analytical and cognitive skills of micro and small rural entrepreneurs to cope with decision-making and problem-solving for their enterprises. The use of sound financial management practices in agriculture is quickly becoming necessary for survival and are a required for outstanding economic performance. Many simple financial management practices have a strong relationship to farm financial performance. Among other things, farmers who take the time to prepare a written or computerized cash flow analysis of their investment projects are much more profitable than their peers who either did not conduct the analysis or those that “did it the analysis in their head”

Performance of the Agricultural Sector in Kenya

- According to the GEA report (UNEP, 2014), Agriculture is the mainstay of Kenyan economy, contributing to 24 per cent of national GDP valued at KSh 342 billion (USD 4.5 billion) and another 27 per cent indirectly valued at KSh 385 billion (USD 5.1 billion) in 2012 (GoK, 2012). This sector in Kenya is large and complex, with a multitude of public, parastatal, non-governmental and private actors, accounting for 65 per cent of Kenya's total exports (GoK, 2012). Moreover, the sector employs over 40 per cent of the total population and over 70 per cent of the rural population. Agriculture also provides livelihoods (employment, income, and food security needs) for more than 80 per cent of the Kenyan population (FAO, 2010). Therefore, the sector is not only the driver of Kenya's economy, but also the means of wellbeing for the majority of the Kenyan people (GoK, 2012).

- In Kenya, the agricultural sector comprises six major sub-sectors, namely
- (1) industrial crops;
- (2) food crops;
- (3) horticulture;
- (4) livestock;
- (5) fisheries and
- (6) forestry.

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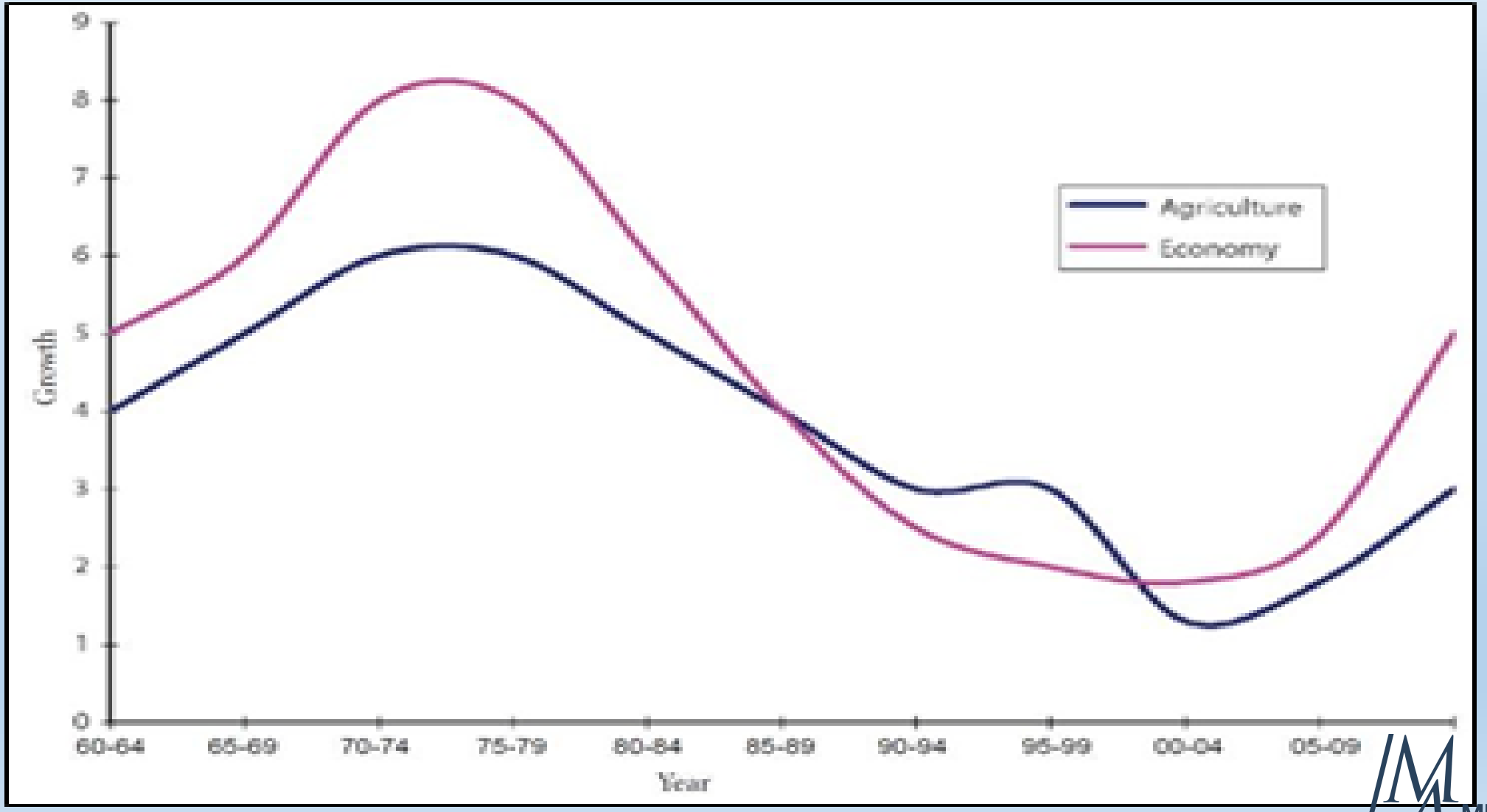
- In Kenya, economic growth is highly correlated with the development of agriculture (Graph 1). In the first two decades after independence, the agricultural sector, as well as the national economy, recorded the most impressive growth in sub-Saharan Africa growing at average rates of 6 per cent per annum for agriculture and 7 per cent for the national economy (GoK, 2009).
- This growth was driven by ample available land and better use of technology. Moreover, the government provided support to agricultural extension and research, agricultural inputs, marketing, credit and agro-processing, as well as to the establishment of agricultural institutions (including farmers' cooperatives). An average of 13 per cent of the national budget was allocated to this sector during this period

Graph 1: Trends in agricultural and economic growth



- However, this rapid growth was not sustained. The sector shrank to an average annual growth rate of 3.5 per cent in the 1980s and fell further to an average rate of 1.3 per cent in the 1990s (GoK, 2009). The main reasons for this decline included low investment, mismanagement, virtual collapse of agricultural institutions and negligence of agricultural extension and research. During this period, the government was implementing Structural Adjustment Programmes (SAPs), which encouraged poorly sequenced privatization in the sector and saw budgetary allocation to agriculture declining to 2 per cent or less of the national budget (GoK, 2011).

- The agriculture sector began to revive in 2000, with an average growth rate of 2.4 per cent. This was driven by the governments' efforts, especially after 2003, to recognize agriculture as a priority sector, key to economic growth in the context of the Economic Recovery Strategy for Employment and Wealth Creation (ERS) and the Strategy for Revitalizing Agriculture (SRA). The government gradually started to invest more in the sector and to increase budgetary allocation to an average of 4.5 per cent of the total national budget (GoK,2009). The sector reached a high growth rate of 6.1 per cent in 2007 (GoK, 2009).
- However, these gains were affected by many adverse factors, including the post-election violence in 2008, multiple crises caused by global food prices, escalating fuel prices in 2008, and the financial crises of 2008/2009 (GoK, 2009). In 2008, the agricultural sector grew at a negative rate of 4.1 per cent (see Table 4). The effect of these factors was further aggravated by severe drought and erratic rainfall in 2009 which continued to dampen agriculture output.

- In 2010, growth in the agriculture sector rebounded. Vibrant internal demand for major staples, livestock products and horticultural goods, and growth in key export sub-sectors such as coffee, tea, pyrethrum, horticulture, and cut flowers, were important factors that contributed to this recovery (GoK, 2010). In 2012, agricultural output grew by 3.8 per cent, more than twice its growth in 2011 (Table 4), thanks largely to better weather conditions. The government is undertaking important legal and institutional reforms in the sector, in addition to increasing allocation of resources towards irrigation, and improved access to inputs, especially fertilizer and seeds (KIPPRA, 2013).

Table 1: Performance of the agriculture sector in Kenya (2010 2014)

Item	2010	2011	2012	2013	2014*
GDP growth rate at 2001 constant prices (%)	1.5	2.7	5.8	4.4	4.6
Growth rate of agriculture and forestry sector at 2001 constant prices (%)	-4.1	-2.6	6.4	1.5	3.8
Contributions of agriculture and forestry sector to GDP at current prices (%)	22.3	23.5	21.4	24	26

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Strategies and Policies through Agri-business

- In order to put Kenya back on a strong economic growth path, the government embarked on the formulation of a wide range of policies aimed at economic reconstruction and the rehabilitation of collapsed agricultural infrastructure and institutions. In 2003, the ERS was launched as a blueprint for economic development with an overall goal of creating more jobs and wealth to move the country from poverty to prosperity. The ERS gives high prominence and priority to agriculture and recognizes it as the backbone of the economy. Its rapid growth is necessary to generate wealth and employment deeming the need for enhanced agribusiness. In addition, the strategy recognizes that revival of agricultural institutions and investment in agricultural research and extension are essential for sustainable economic growth (GoK, 2009).

- As a response to the ERS, the Government of Kenya, as mentioned above, launched the SRA in 2004. The SRA states that the Vision of the Government is “to transform Kenya’s agriculture into a profitable, commercially oriented and internationally and regionally competitive economic activity that provides high quality gainful employment to Kenyans” (GoK, 2009). The target set by SRA for agricultural growth was for an average annual rate of 3.1 per cent during 2003-2007 and was predicted to reach over 5 per cent by 2007.

- The ERS was a 5-year plan, expected to expire in the financial year 2007/2008. In June 2008, the Government launched the Kenya Vision 2030 as the new long-term development blueprint for the country (GoK, 2009). The Vision of this blueprint is “a globally competitive and prosperous country with a high quality of life by 2030.” It aims to change Kenya into “a newly industrializing, middle-income country providing a high quality of life to all its citizens in a clean and secure environment.” The Vision is underpinned by three pillars: the economic pillar aiming to achieve a sustained economic growth rate of 10 per cent per annum in 2030; the social pillar seeking to create cohesive and equitable social development in a clean and secure environment, and the political pillar aspiring to realize an accountable democratic system. Table 5 below outlines the country’s main targets that it hopes to achieve by 2020.

GOK outlines the following interventions to facilitate rapid growth in the sector:

- Review and harmonize legal, regulatory and institutional frameworks;
- Restructure and privatize non-core functions of parastatals and sector ministries;
- Improve delivery of research, extension and advisory services;
- Improve access to quality inputs (fertilizer, hybrid seeds, equipment) and financial services; and
- Improve access to both domestic and external markets

Due to implementation of the above strategies and policies, Agriculture remains an important fundamental in economic development as it contributes to approximately 37% of the gross domestic product (GDP) and constitutes 43% of the export earnings.

Significance of Agriculture to Kenya's Economy

Agriculture has a great potential in ensuring increased economic growth and development in our country and this can be extrapolated by transitioning from subsistence agriculture to agri-business. These benefits include:

- It's a sector that establishes the industrialization framework through; supplying raw materials for industries, example timber for the paper manufacturing industry, skin and hides for leather making industry.
- It generates foreign currency through the export process of agricultural products. It creates a source of employment to the population through farming, business and research activities therefore raising the standard of living of individuals.

Continues…

- The purchasing power of the population is improved through income generation, hence creating a market for industrial products.
- Agriculture in itself is also a market for industrial goods such as machinery, equipment and fertilizers used in the farming process. It promotes and creates various off-farm activities such as transportation, research programmes that look for better and improved methods to be applied in farming and livestock activities, example Kenya Agricultural Institute (KARI).
- Agriculture ensures a constant food supply and food security for the population, this ensures that the work force fed with energy to supply labour to industries and other economic sectors.

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- It also saves the country funds that would have rather been used in the importing of food from other countries this in turn has a positive effect on the country's balance of payments and there is surplus money to invest in other areas of the economy such as social overheads; roads, hospitals.
- Above all it contributes towards rural-urban balancing; through the creation of employment in the rural areas it discourages rural to urban migration and this helps in the better distribution of incomes and balanced use of social amenities. Through all this multiplier effects agriculture is perceived to an engine of economic growth and development.

INTERNATIONAL ACCOUNTING STANDARDS

.Considering the importance and the strategic role that this sector has for the country, providing greater economic and social development.

.In this sense, the growth and strengthening of agribusiness are favorable for the economy, considering the economic and social consequences. Thus, the financial statements must be relevant, understandable and useful for the purpose of investment decision.

.The accounting standard for Biological Assets and Agricultural Produce proposes to regulate the accounting practices of companies that have live animal or plant, bringing significant changes to the companies' balance sheets, as the application of fair value in order to bring more timely information.

IAS 16 & IAS 41-AGRICULTURE

- IAS 16 permits the use of either a cost model or a revaluation model for property, plant and equipment, including bearer plants.
- The recognition, measurement and disclosure requirements in IAS 16 have not been modified for bearer plants.
- However, the amendments clarify that before bearer plants are in the location in the manner intended by the management, i.e before they mature, they are accounted for as self –constructed items of property, plant and equipment.

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- The produce growing on bearer plants is measured at its fair value less cost to sell are included in the profits or loss in the period in which they arise.
- A bearer plant is defined as a living plant that is used in the production or supply of agricultural produce ;is expected to bear produce for more than one period and has a remote likelihood of being sold as an agricultural produce, except for incidental scrap sales.

Amendment to the IAS 16 & 41

In accounting of the Agriculture sector, IAS 41.

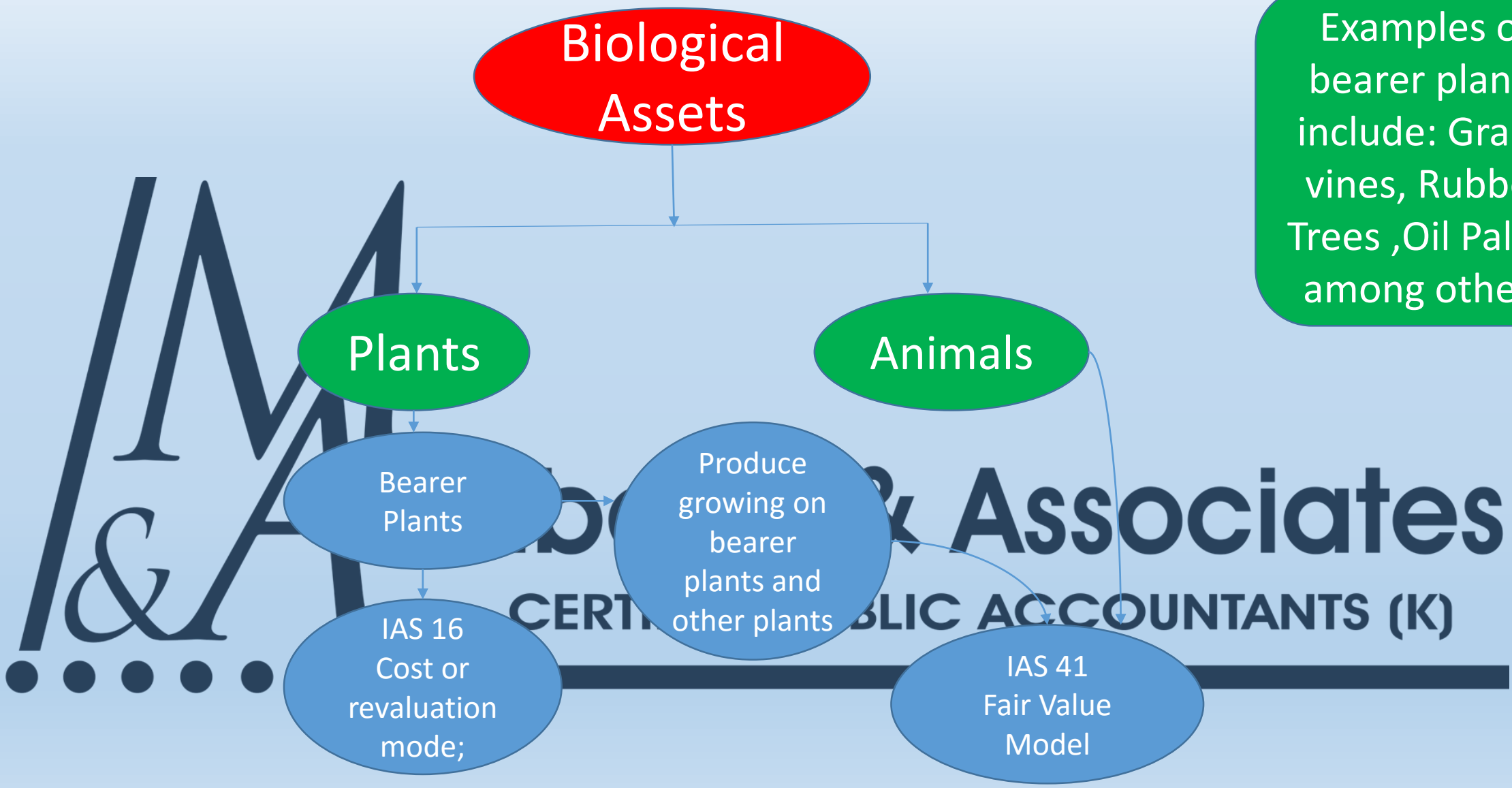
- Recently there has been an amendment in regards to 'bearer plants'(plants used solely for agricultural produce for several period) effective January 2016 that requires that all biological assets related to agricultural activity to be measured at fair value less cost to sell. This concept is based on the transformation that the biological assets go throughout it lifetime to produce.

- Once the bearer plant matures, Its no longer significant in generating future economic benefits apart from the agricultural produce it creates.
- The IASB decided that the bearer plants be accounted for same as property plant and equipment in IAS 16.
- The agricultural produce growing on the bearer plants remain under the scope of IAS 41 whereas the bearer plants are under the scope of IAS 16.

List of Acronyms

- ERS Economic Recovery Strategy
- KARI Kenya Agricultural Research Institute
- GoK Government of Kenya
- GDP Gross Domestic Product
- KIPPRA Kenya Institute for Public Policy Research and Analysis
- SRA Strategy for Revitalizing Agriculture
- SAP Structural Adjustment Programme
- GEA Green Economy Assessment
- UNEP United Nation Environment Programme

Picture



Examples of bearer plants include: Grape vines, Rubber Trees ,Oil Palms among others