Sustainability in Debt Management

County Governments Financing budgets through issuance of Bonds

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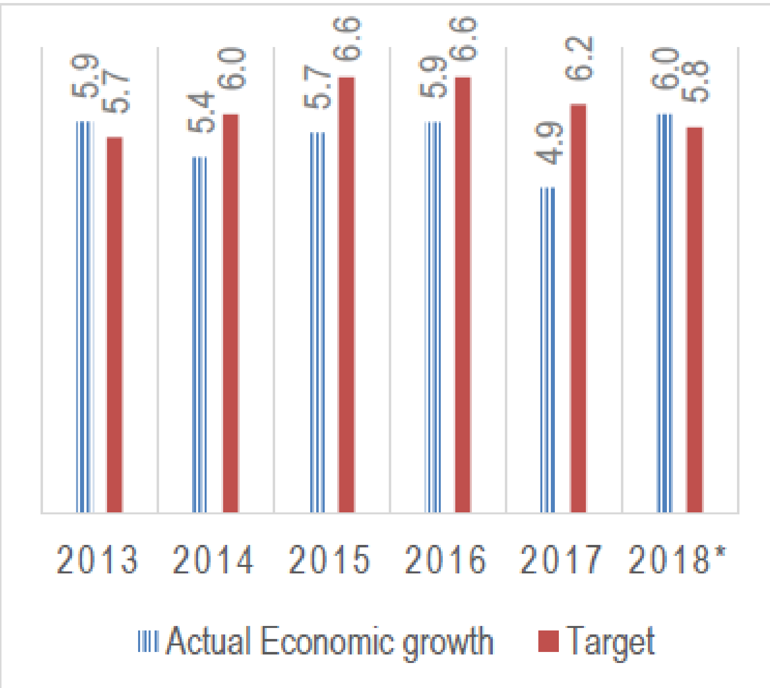
1.0 Economic Outlook

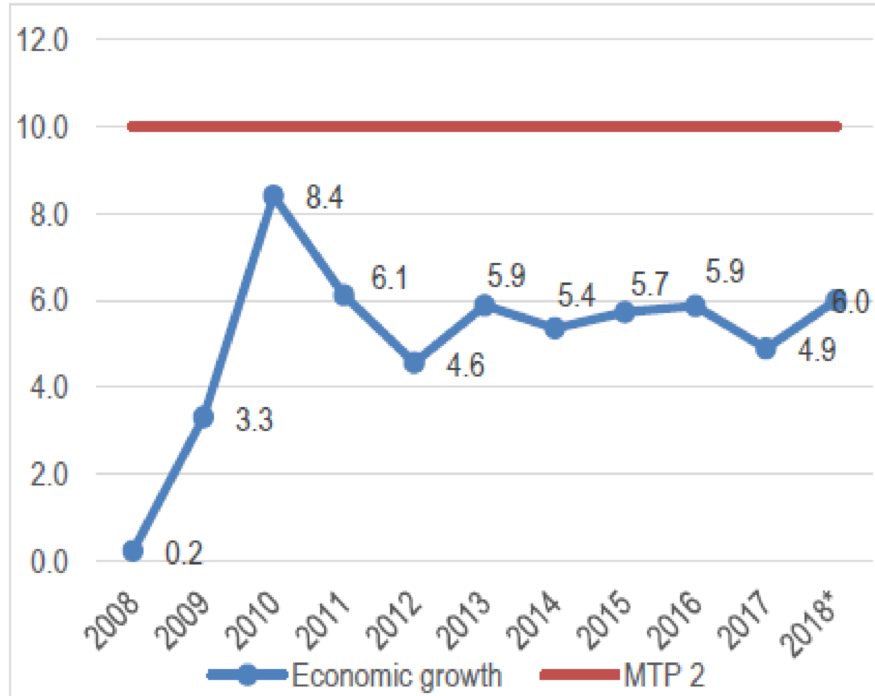
Figure 1: Actual vs Target Economic growth



Source: KNBS, BPS (various issues)

*Estimates

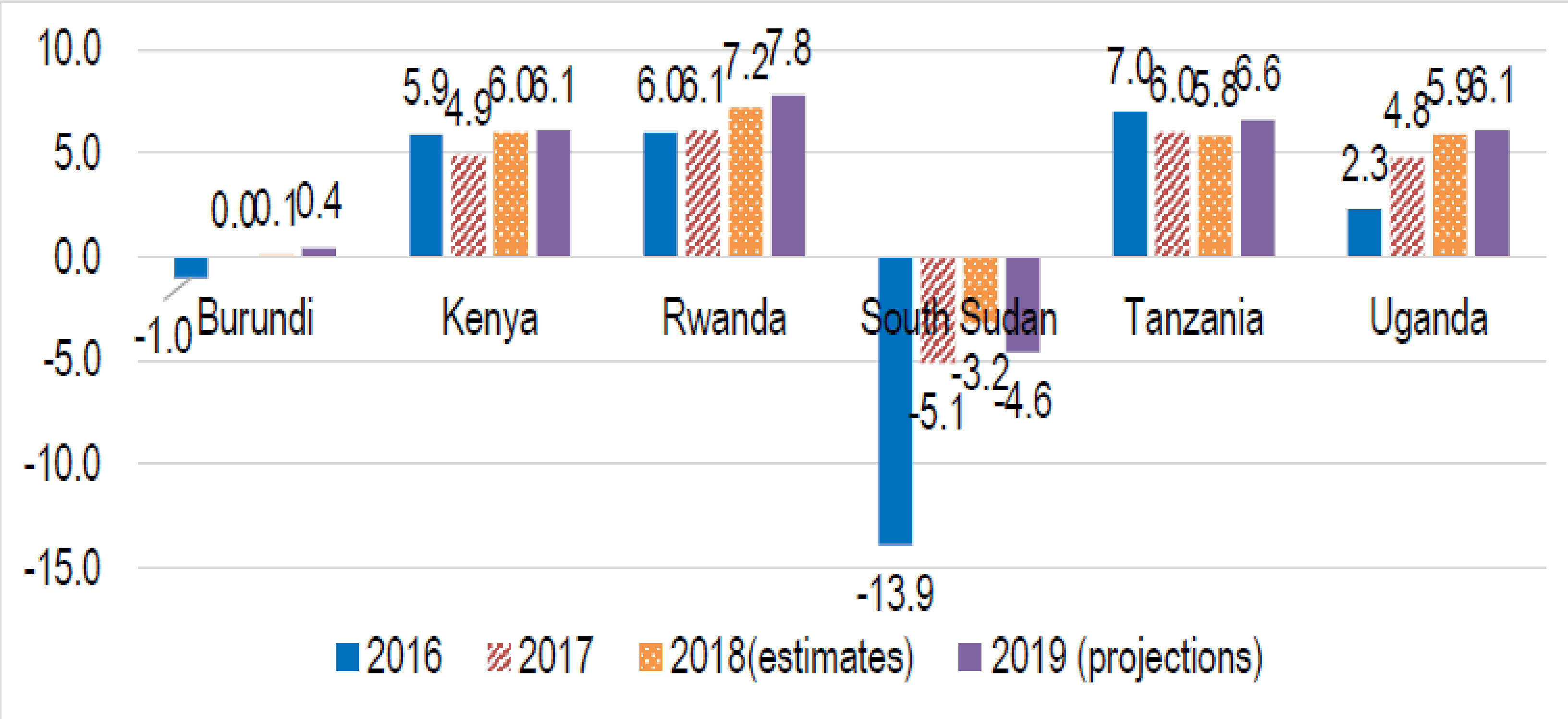
Figure 2: Economic Growth (2008-2018)



Source: KNBS

Regional Comparison

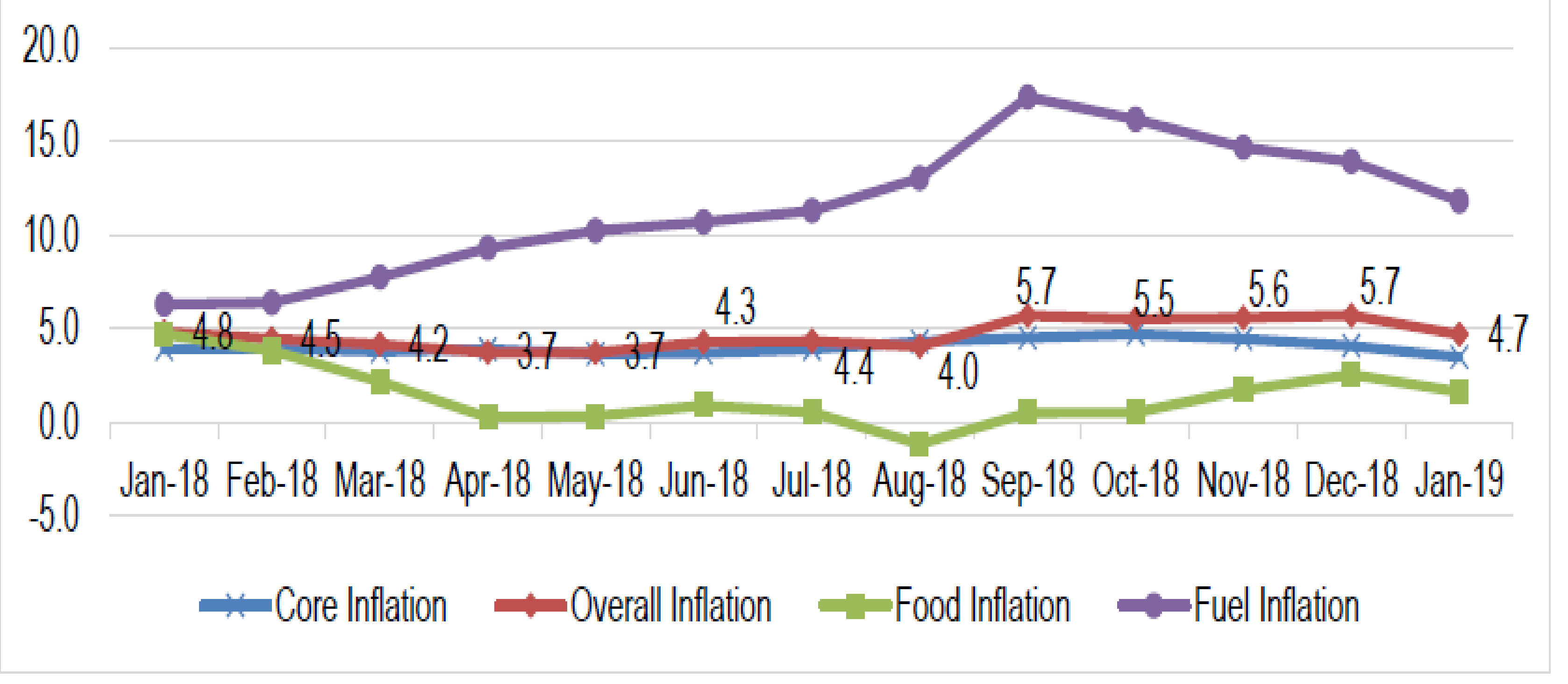
Figure 3: EAC's Economic Growth



Source: IMF WEO, October 2018

Inflation

Figure 4: Trends in Inflation



Source: KNBS

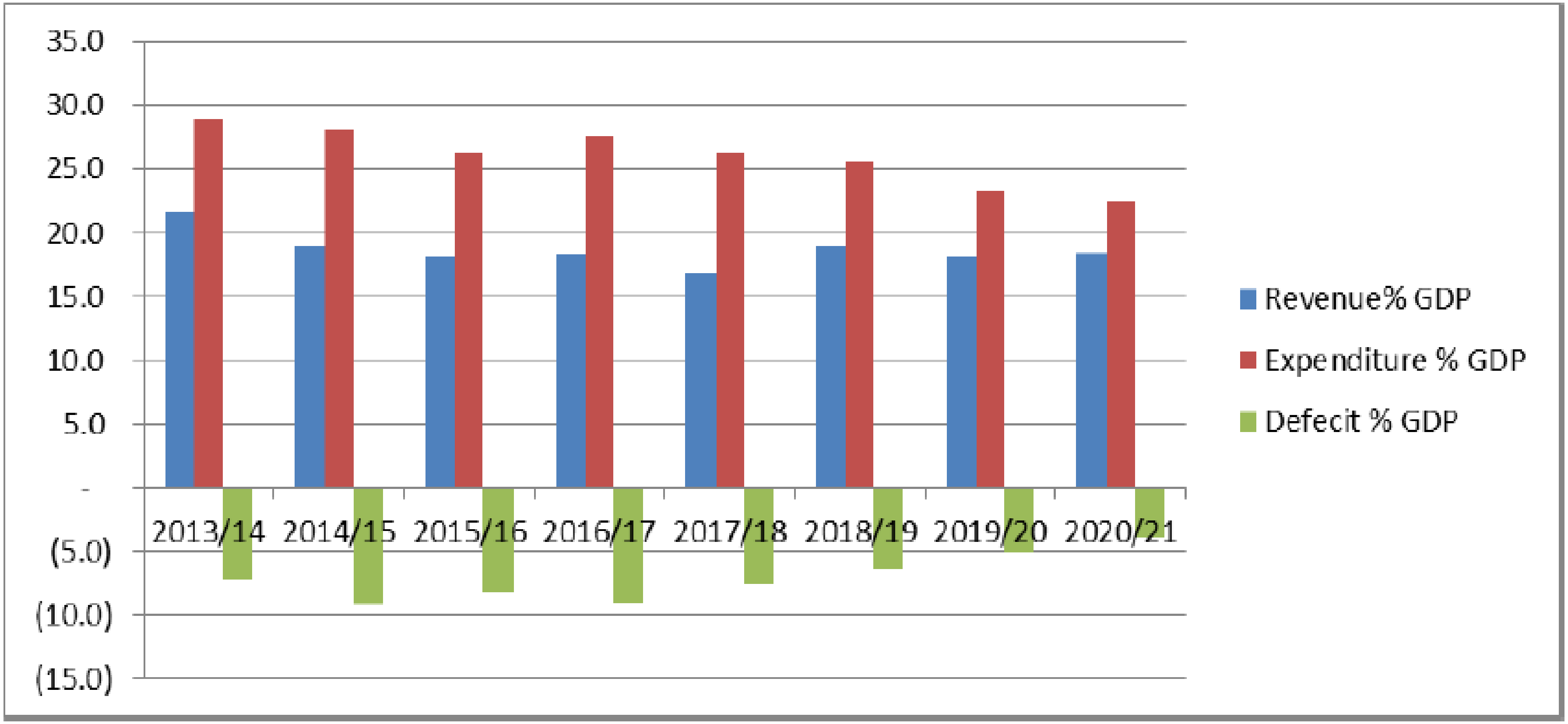
2.0 Public Debt

- All financial obligations attendant to loans raised or guaranteed and securities issued or guaranteed by GoK
- Government, like any other economic unit, collects revenue and spends it. In some instances, expenditures will exceed receipts or sudden surge in government expenditure
- Public Debt is a charge on the Consolidated Fund - Art 214;
- Public debt may be internal (domestic) or external

Public Debt

- PFM Act , 2012 Sec 49 – 65 with regard to National and Section and Sec 140 – 147 with regards to Counties;
- The Act repealed the External Loans & Credit Act, Internal Loans Act & the National Government Loans Guarantee Act
- These provided a legal framework for Government to raise loans outside Kenya, within Kenya & to guarantee loans extended to public entities

Figure 5: Revenue, Expenditure and Deficit as a Share of GDP (%)



Sources: National Treasury

Table 1-2: Trends in Kenya's Total Public Debt in (Ksh million)

DEBT TYPE	Jun-13	Jun-14	Jun-15	Jun-16	Jun-17	June-18
DOMESTIC DEBT						
Central Bank	39,170	65,700	63,335	99,856	54,506	110,782
Commercial Banks	524,505	617,221	730,419	927,307	1,142,889	1,266,457
Sub-total: Banks	563,675	682,921	793,754	1,027,163	1,197,395	1,377,239
Non-bank Financial Institutions	486,880	601,406	626,690	787,970	915,315	1,101,596
Total Domestic	**1,050,555**	**1,284,327**	**1,420,444**	**1,815,133**	**2,112,710**	**2,478,835**
As a % of GDP	23.4%	25.5%	24.4%	27.1%	27.6%	28.0%
As a % of total debt	55.5%	53.0%	50.0%	50.3%	47.9%	49.1%
EXTERNAL DEBT						
Bilateral	217,970	248,636	405,562	491,864	669,840	759,017
Multilateral	507,920	593,397	680,192	794,798	839,722	825,299
Commercial Banks	58,928	234,799	276,937	432,377	634,109	830,652
Suppliers Credits	15,207	16,452	16,628	16,628	15,303	16,725
Sub-Total	**800,025**	**1,093,284**	**1,379,319**	**1,735,667**	**2,158,974**	**2,431,693**

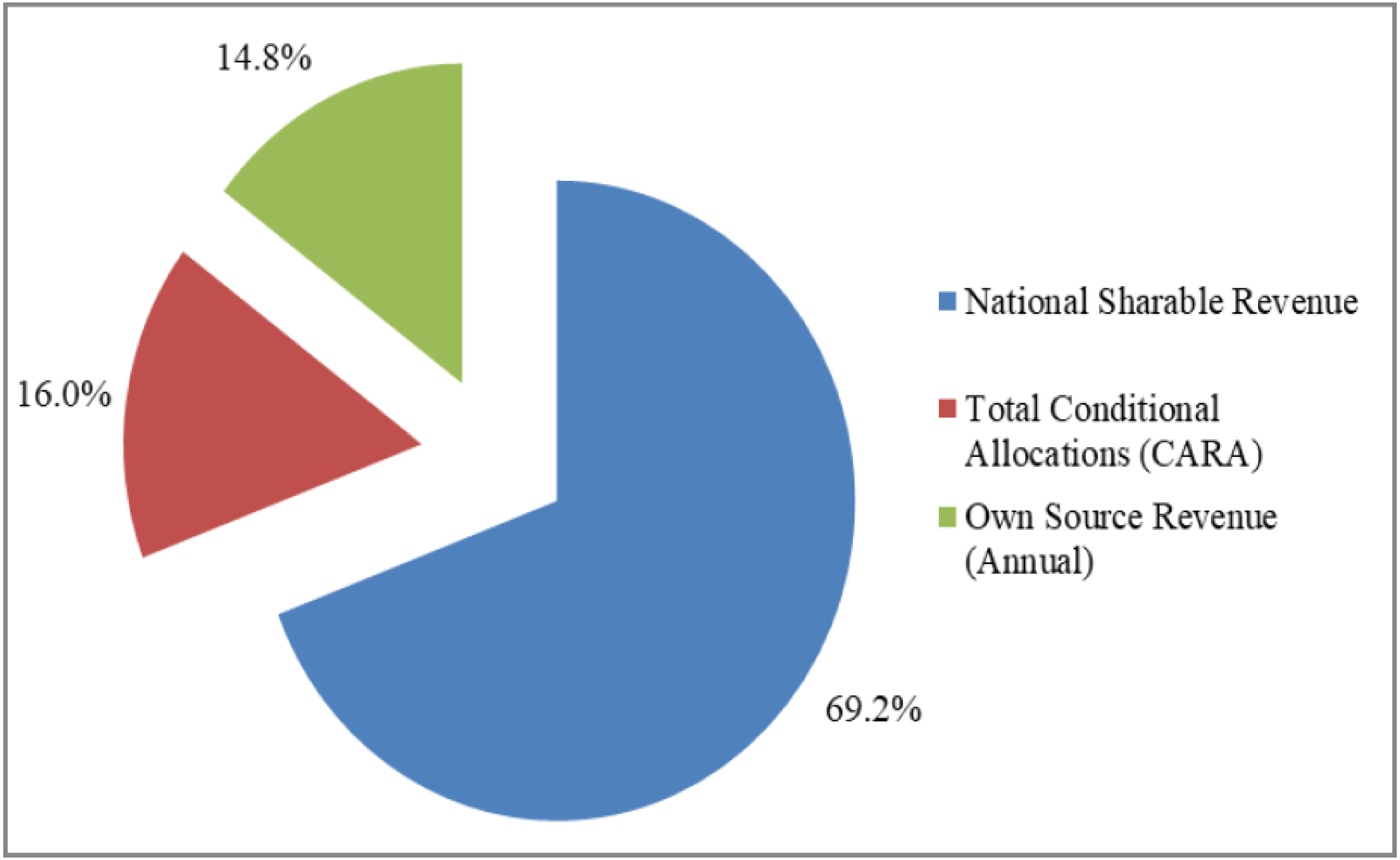
Table 1-2: Trends in Kenya's Total Public Debt in (Ksh million)

DEBT TYPE	Jun-13	Jun-14	Jun-15	Jun-16	Jun-17	June-18
GUARANTEE DEBT						
Bilateral	39,667	41,278	39,495	56,487	52,728.80	56,371
Multilateral	3,870	3,943	4,439	4,044	4,667.00	4,547
Commercial	0	0	0	0	77,783.80	75,788
Sub-Total	**43,537**	**45,221**	**43,934**	**60,531**	**135,180**	**136,706**
Total External debt	**843,562**	**1,138,505**	**1,423,252**	**1,796,198**	**2,294,153**	**2,568,399**
As a % of GDP	18.8%	22.6%	24.4%	26.8%	30.0%	29.0%
As a % of total debt	44.5%	47.0%	50.0%	49.7%	52.1%	50.9%
GRAND TOTAL	**1,894,117**	**2,422,832**	**2,843,696**	**3,611,331**	**4,406,863**	**5,047,234**
Total debt As a % of GDP	**42.1%**	**48.0%**	**48.8%**	**53.8%**	**57.5%**	**57.1%**
GDP (in Ksh million)	**4,496,000**	**5,044,236**	**5,831,528**	**6,709,671**	**7,658,138**	**8,845,854**

3.0 Source of County Financing

The main sources of financing to counties are

1. Equitable share accounting for over 80 percent,
2. Conditional grants from both National government as well as proceeds from loans and grants from development partners and
3. Counties own source revenue mainly raised from several tax streams such as business permits, imposition of property rates, in line with the Article 209 of the Constitution.


14.8%
16.0%
69.2%
National Sharable Revenue
Total Conditional Allocations (CARA)
Own Source Revenue (Annual)

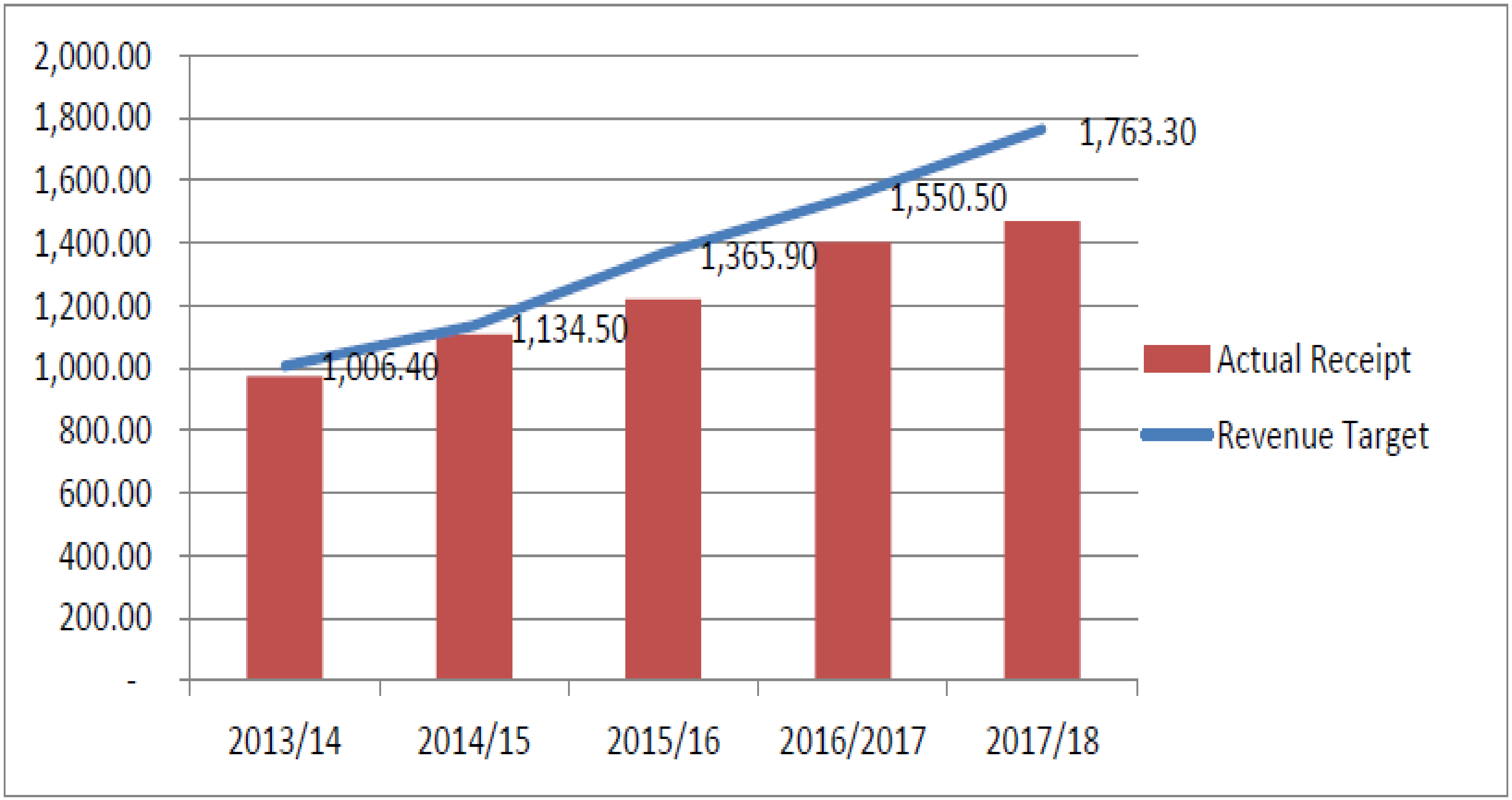
Source of County Financing cont..

- According to Art 202, cumulatively from financial year 2013/14 a total of Kshs 1,767.3 billion has been allocated to the county governments from the nationally raised revenues.
- This comprises of equitable share of Kshs 1,572.8 billion and additional Kshs 194.5 billion in form of conditional grants from the national government share for specific programmes and policies.

Source of County Financing cont..

- The equitable share is calculated on the basis of the most recent audited accounts of revenue received, as approved by the National Assembly.
- The Approval of the Audited Accounts has been lagging behind to the detriment of the counties.
- The latest audited revenue account relate to FY 2014/15 where total revenue stood at Kshs 1,038 billion.

Figure 6: Revenue targets versus actual revenue receipts during FY 2013/14 – 2017/18

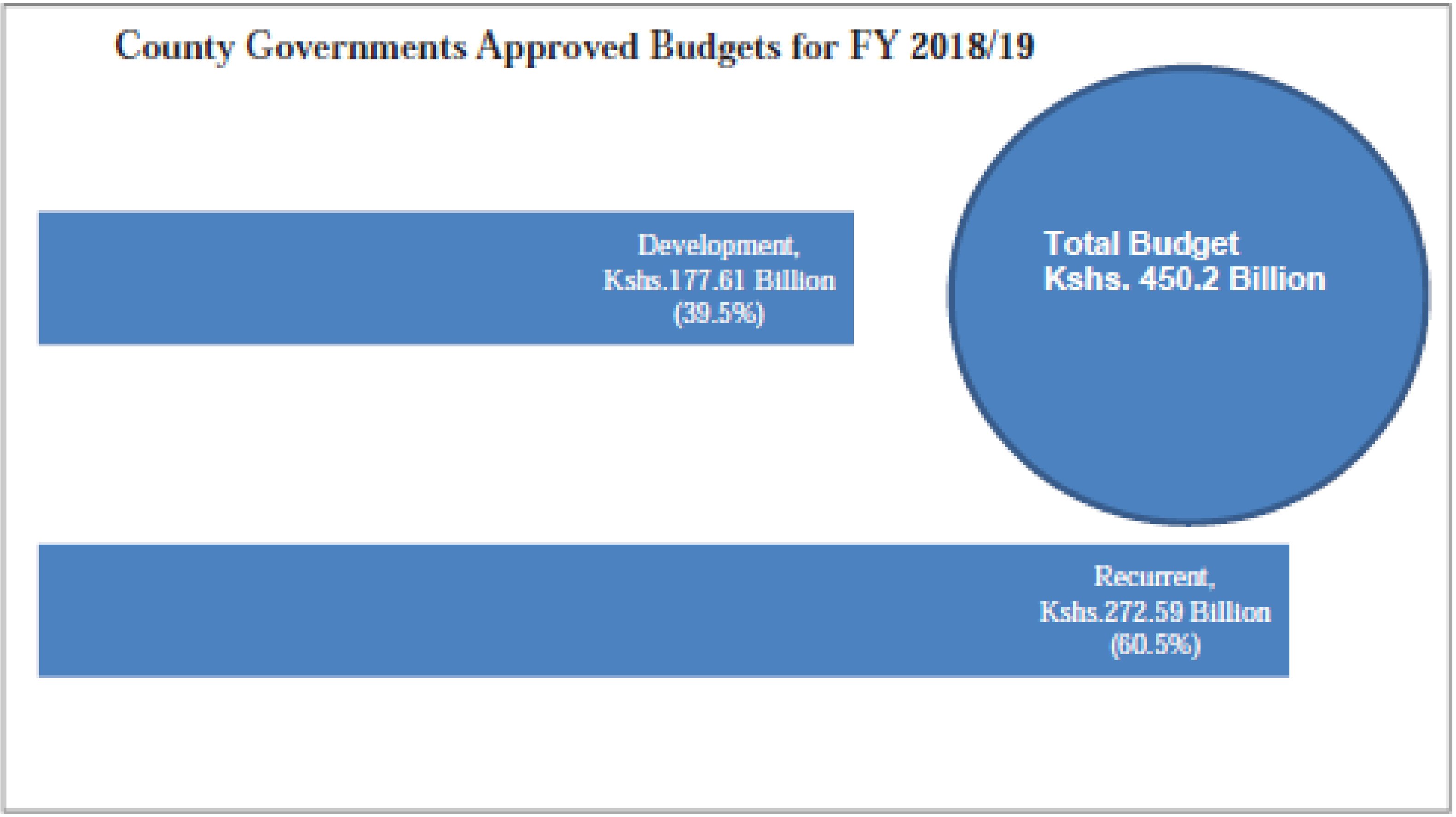


Source: National Treasury

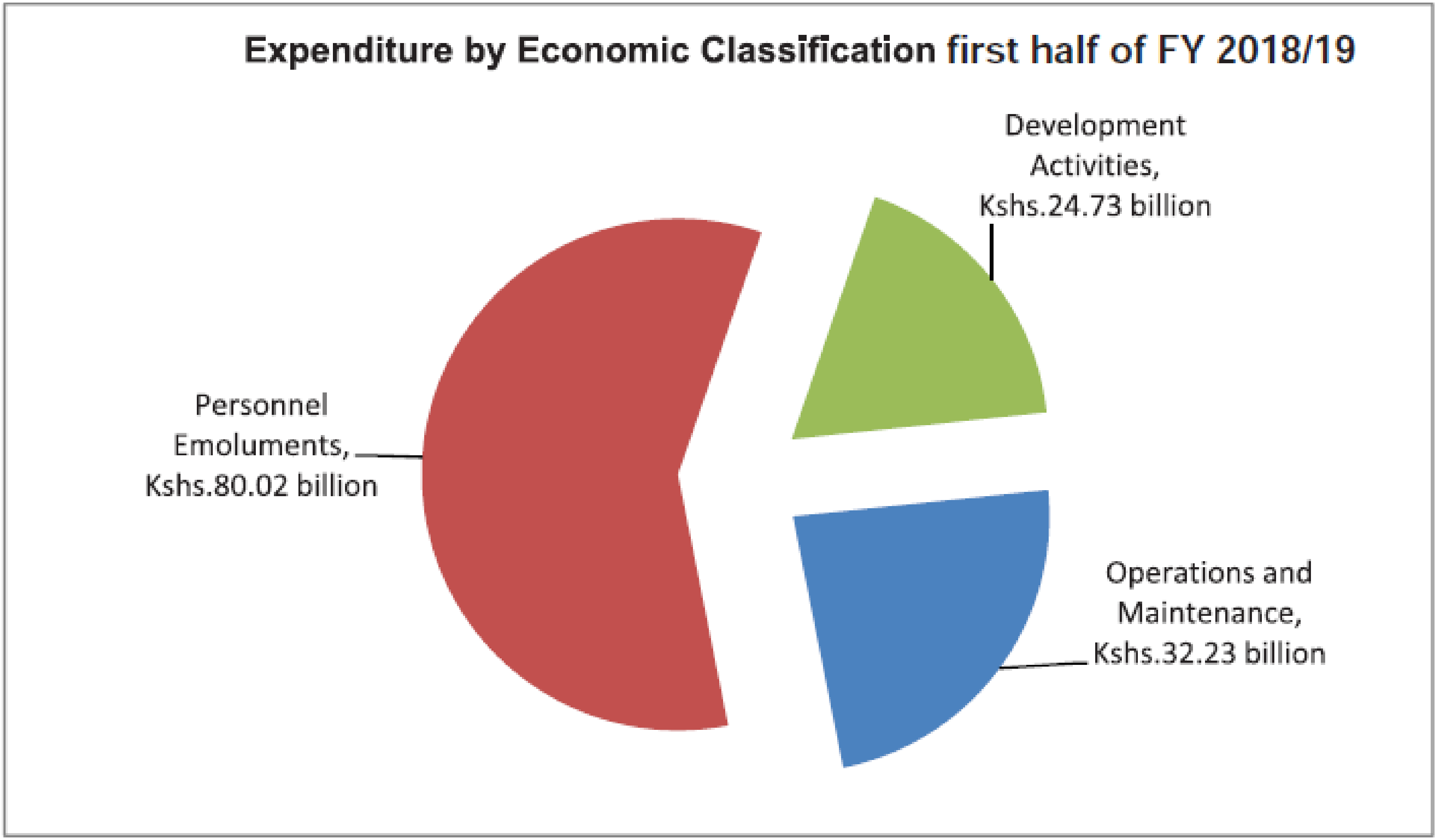
Source of County Financing cont..

- Section 107(2) of the PFM Act 2012 requires that Counties to allocate a minimum of 30 percent of their budget to development expenditure.
- The average development allocation by counties over the last six financial years has been 40% surpassing the legal requirement
- Similarly, Section 25(b) of the Public Finance Management County government Regulations, 2015 which puts a cap on county wage bill at 35% of total receipts.

Source of County Financing cont..



Source of County Financing cont..



Source of County Financing cont..

- However, it is observed constantly that spending on the recurrent expenditures are on average above 75% while for development spending the actual are on average below 50%.
- The bulk of the funds are utilized for recurrent spending leaving a small fraction for the wealth creation and capital generation.
- Most of these allocations are spent on salaries and wages, travel both domestic and foreign, use of goods and services, and other operations and maintenance.

4.0 Financing through Debt

- In accordance with sections 141 of the PFM Act 2012, county governments are conferred with power to borrow from external financiers with guarantees from the National Treasury.
- However, counties have not been able to utilize this window as a result of lack of approved borrowing framework.
- It has to be negotiated between the financiers and the national Treasury with concurrence of the IBEC.

Financing through Debt cont..

Counties can finance projects through debt instruments such as;

1. Commercial Loans
2. Public Private Partnerships
3. Corporate Bonds
4. Utility Bonds
5. Infrastructure Bonds
6. Municipal Bonds

Types of Bonds

- **Treasury Bonds** – are a secure investment that typically offer you interest payments every six months throughout the bond's maturity.
- **Corporate Bonds** – type of debt instrument issued by firms to investors. It has a coupon rate and maturity date.
- **Utility Bonds** – a type of financial guarantee ensuring a person or organization will pay for utilities on time.
- **Municipal Bonds** – are issued by county governments to raise money for public works projects like the construction and maintenance of bridges
- **Infrastructure Bonds** – are used by the government for specified infrastructure projects and returns from them are tax exempt

Challenges to Counties

1. National Treasury's delay in disbursing of funds – PFM Act 2012 requires every 15th of the month
2. Unchecked borrowing by National Treasury thereby putting a strain on revenues resulting into reduced equitable share to counties
3. Lack of fiscal framework for counties to borrow as envisaged under Section 141 of PFM Act 2012
4. Lack of a mechanism for undertaking county creditworthiness thereby making it difficult for investors to allocate risk associated with each
5. Inadequate capacity amongst counties to handle issuance of debt instruments

Are Counties Ready?

1. Legal framework - Section 141 of PFM Act 2012 and approval from County Assembly
2. Quality of Financial Statements – Unqualified Audit Reports
3. Functional IFMIS
4. Budget Absorption rate
5. Credit Rating for Counties
6. Citizen Trust
7. HR capacity

5.0 Conclusions

1. Capping of National Treasury borrowing to safeguard the country from risks inherent with debt
2. The ceilings set for the nation to be shared with counties
3. Provide regulations for counties fiscal borrowing as per section 141 of PFM Act 2012
4. Counties to undertake a Credit Worthiness assessment
5. Counties will get a rating of between AAA and D, with those with a rating of B- and above seen as creditworthy.

Thank You