Inaugural Entrepreneurship Workshop – Nairobi

Presentation by:
Andrew Bulemi.

Thursday, 8thNovember 2019

County government Borrowings and Investment opportunities for revenue

SOURCES OF

COUNTY REVENUE

IN KENYA

afrocave.com

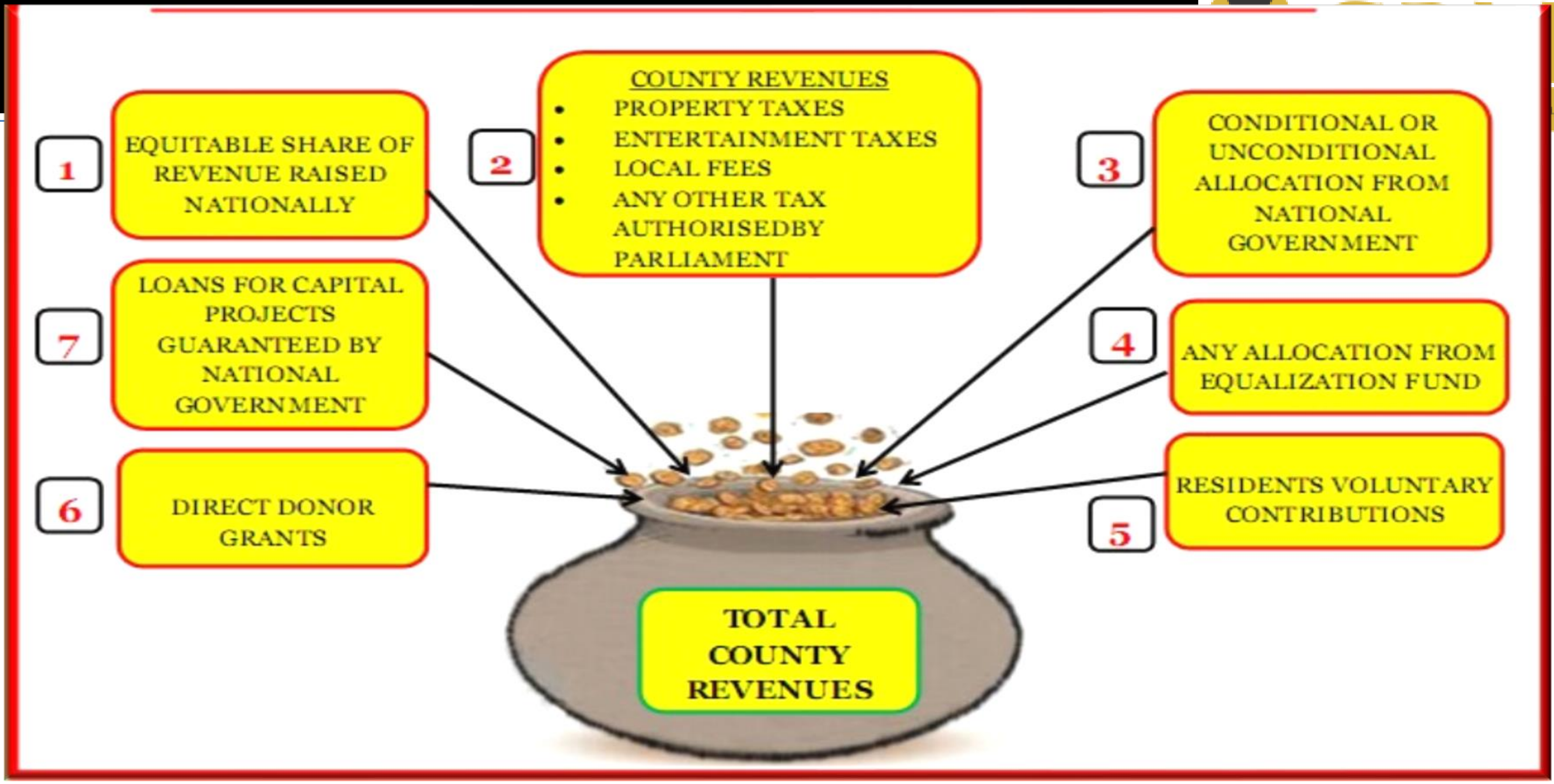
Content

The topics to be covered include:

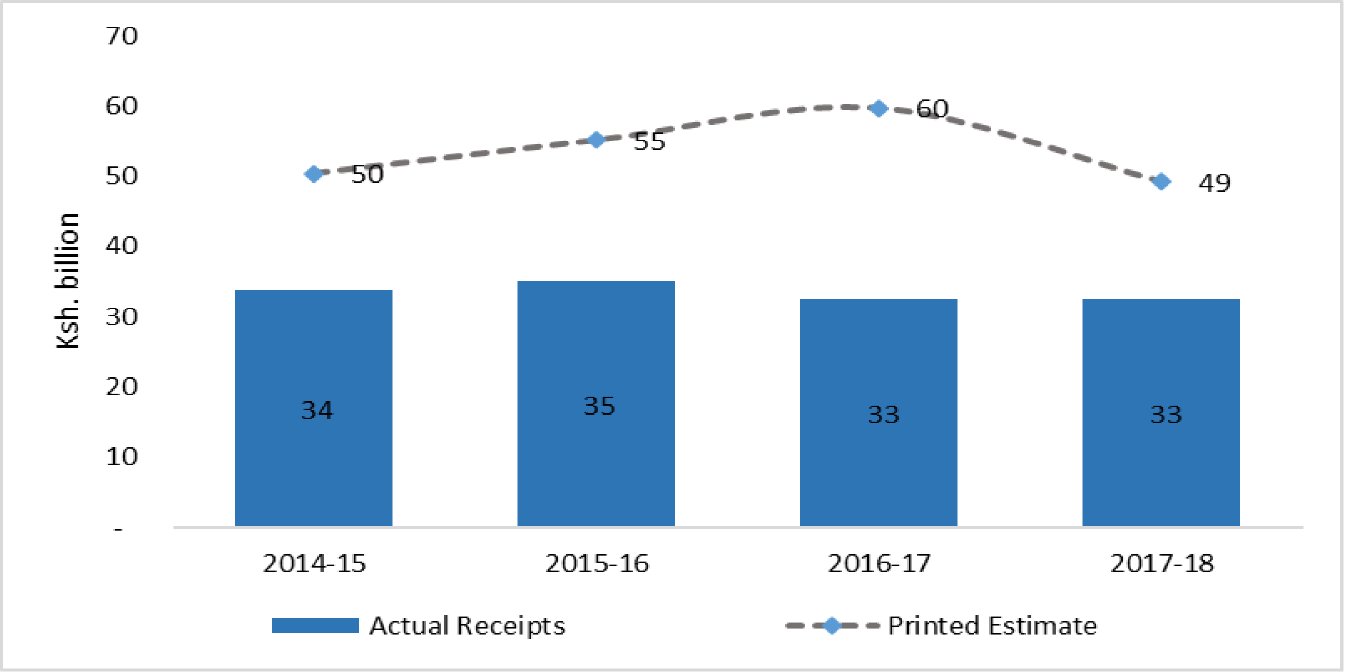
1. Sources of revenue for county governments
2. Loans(borrowings)
3. Investment by the county government
4. Recommendation and conclusion

1. Sources of revenue for county governments

Sources of revenue for county



County government Revenue Performance

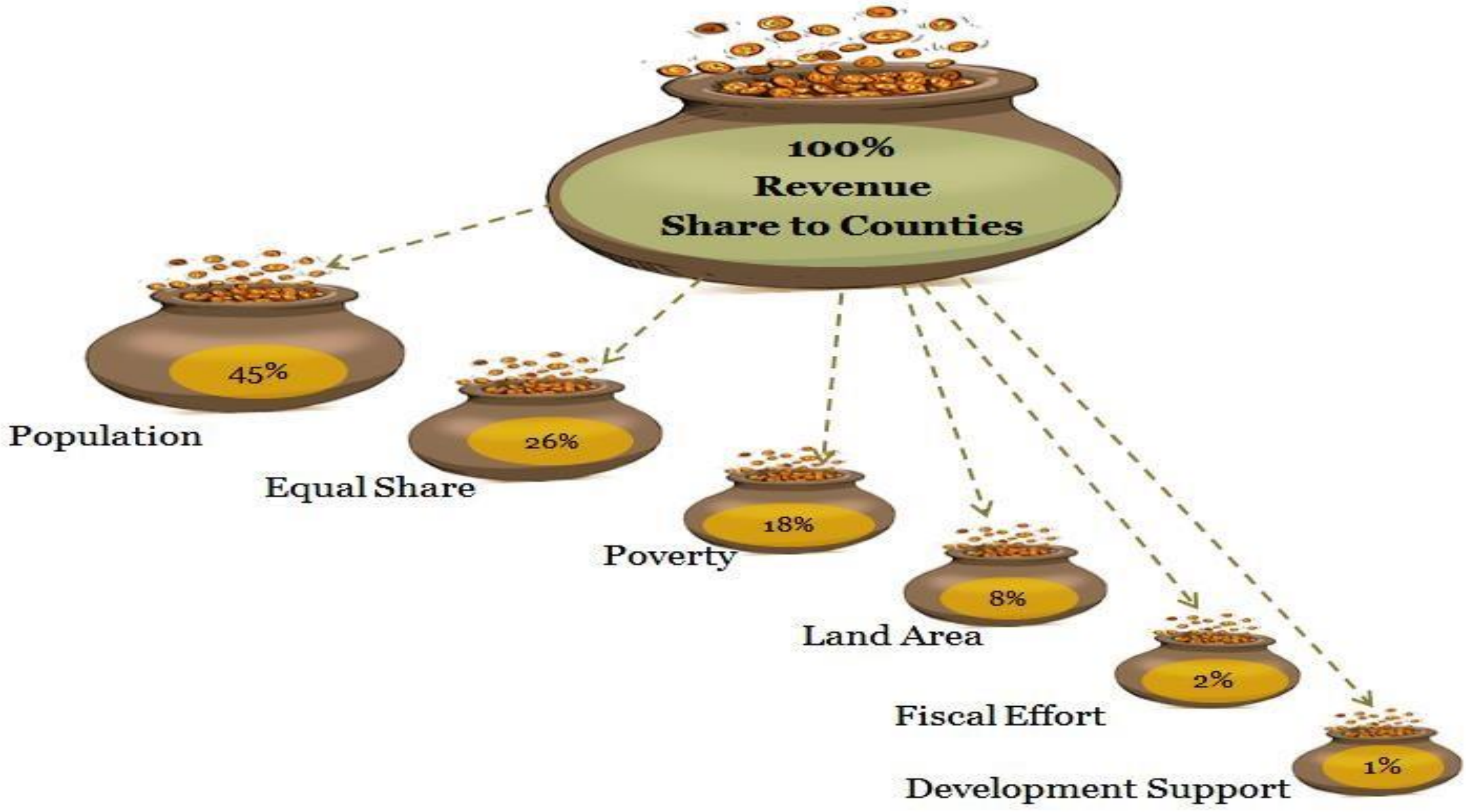


Source: world bank review

Equitable share raised nationally

- This is the largest source revenue for county governments.
- It should not be less than 15% of the revenue raised nationally
- The revenue sharing formula developed by commission on Revenue Allocation (CRA) is used to divide the equitable share among the counties. Threshold used include: **population, land area, basic equal share, poverty level and fiscal responsibility.**

The summary of second revenue sharing formula by (CRA)



2. Loans/Borrowings

Borrowing as a source of funding for county government

A County Executive Committee member for finance may, on behalf of the county government, raise a loan for that Government's purposes, only if the loan and the terms and conditions for the loan are set out in writing and are in accordance with:

- Article 212 of the Constitution;
- Sections 58 and 142 of PFM Act;
- The fiscal responsibility principles and the financial objectives of the county government set out in its most recent County Fiscal Strategy Paper;
- The debt management strategy of the county government over the medium term

Preconditions for loan guarantee

The PFM Act sets preconditions for loans Guarantee

- The loan is for a capital project;
- the borrower is capable of repaying the loan, and paying any interest or other amount payable in respect of it;
- The financial position of the borrower over the medium term is likely to be satisfactory;
- The terms of the guarantee comply with the fiscal responsibility principles

Borrowing as a source of funding for county government

❖ Borrowing includes Treasury bill, treasury bonds, corporate bonds; sovereign bonds and external loans acquired by the entity or any other debt the County Government may take on will be treated on cash basis and recognized as receipts during the year of receipt. Some of the pre-requisites to counties obtaining loans are:

- The county government can only access a loan if the national government guarantees the loan
- The county assembly must approve any loans that the county government intends to borrow
- All loan guarantees provided by the national government have to be approved by the parliament

- The county government's recurrent expenditure shall not exceed the county government's total revenue;
- over the medium term a minimum of 30% of the county government's budget allocated to the development expenditure;
- The county government's expenditure on wages & benefits shall not exceed a percentage of the county government's total revenue;
- a reasonable degree of predictability with respect to the level of tax rates and tax bases shall be maintained

Kind of borrowings by the county government

- Long term loans: Only for capital projects

- Short term borrowings: To manage county's cash flows. The amount borrowed should not be more than 5% of the county's last audited financial accounts.

Short-term borrowing

- Is issued to manage a county's cash flow. For example, sometimes a county may run short of cash while waiting for a revenue transfer from national government and would need to borrow money for just a few weeks. Short-term borrowing for cash flow is allowed, but it is also restricted.

- The law permits a county to borrow for no more than a year for this purpose, and the amount that may be borrowed is no more than 5 percent of the county's last audited financial

Effects of Interest Rate Cap in Kenya's Banking Sector

The interest rate cap brought some negative effects on the general economy, with the effects more severe in 2017 than in 2018. However, some recovery has been witnessed in 2018 with increases in growth of credit to the private sector, and general economic growth. Market power in the banking sector is likely to influence interest rate spreads, with the few large banks likely to have the advantage. Nevertheless, the law has generally succeeded in bringing down interest rate spreads.

Hence the CBK needs to be granted exclusive powers to implement both the monetary policy rules in Kenya and come up with policies that ensure competitive and efficient banking industry.

Factors that a bank takes into consideration when determining the rate it charges to its borrowers

These factors include the cost of funds, the lending risk, the Treasury bill rates on the risk free public sector borrowing, rate of savings relative to borrowing, the fundamental macroeconomics indicators like inflation and exchange rates, the level of non-performing loans and the Bank's administrative and operating costs.

These factors determine the rate of interest to be applied hence might vary from one bank to the other.

3. Investment Opportunities

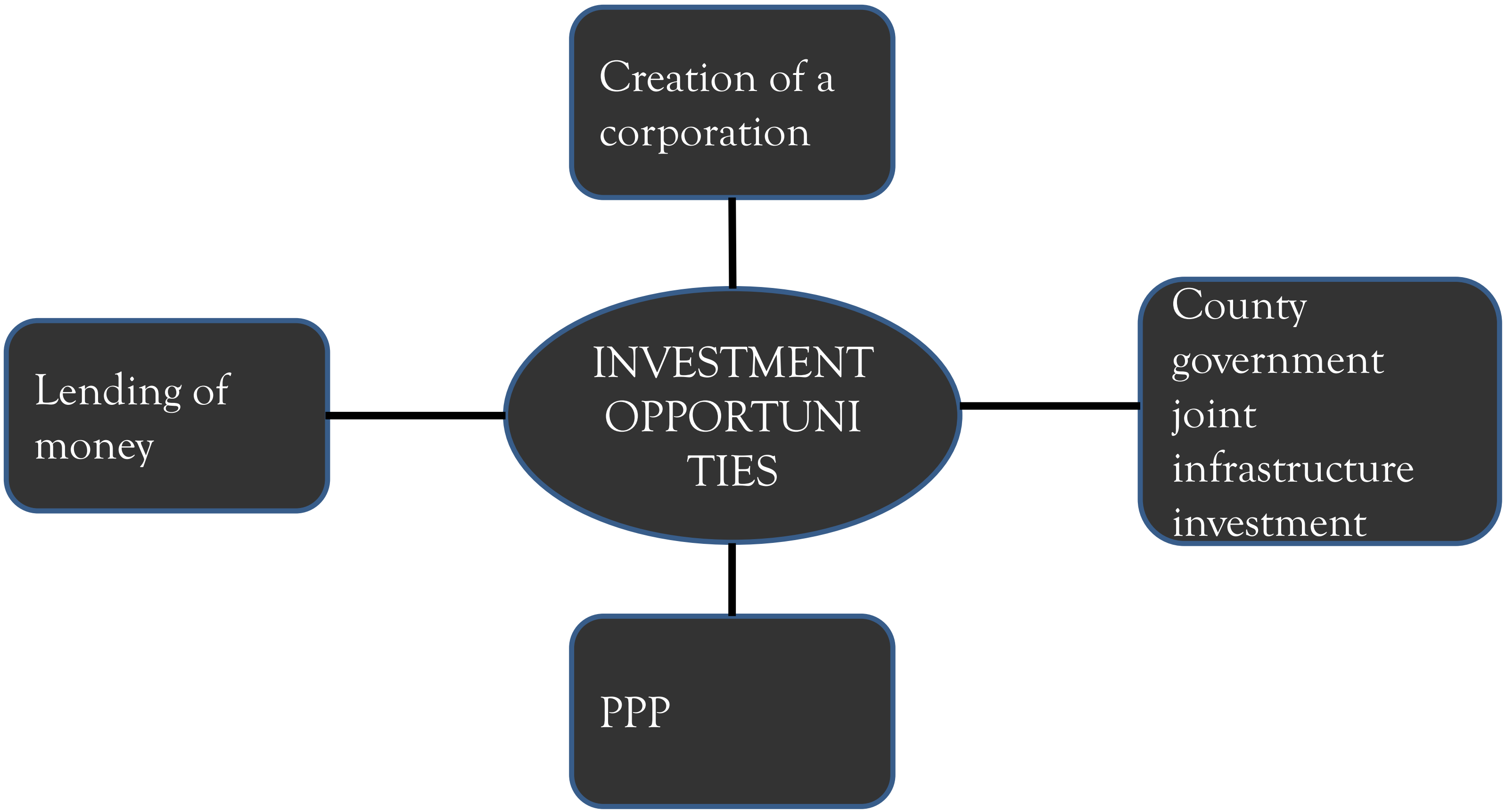
Investment opportunities

Investment as source of revenue

Credibility. Professionalism. Accountability

- This is a minor source of revenue and although an alternative one. Counties can receive returns or profits from undertaking investments (return on investments). That is, the counties can invest in some resources and the resulting returns or profits become revenue for the county government.
- It is important for the counties to compare the efficiency of different investments before investing and after investing (and receiving returns) to maximize revenue from this source.

Categories of investment opportunities



Creation of a corporation

- Counties may establish any county corporations they would like, subject to the approval of the County Executive Committee and only after taking into account the views of the County Treasury on the financial implications of creating the corporation.
- Once created, a county may only further invest in such a corporation with the approval of the County Executive Committee as a whole, and again taking into account Treasury recommendations
- County corporations must meet all of the same reporting requirements as other county departments or entities.

Lending of money by the county government

- A county government entity may lend money in accordance with PFM Act or any county legislation.
- Money loaned by the county government) is payable only from an appropriation for development expenditures; or
- from some other authority approved by the county assembly for the purpose for which the loan is made.

County government joint infrastructure investment.

- Regulations approved by Parliament shall prescribe financial relations with respect to joint infrastructure investments undertaken by counties and any joint infrastructure investments undertaken by counties shall be done in terms of those regulations.

- The Intergovernmental Budget and Economic Council may agree on regulations with guidelines for county government joint infrastructure investments

4. Conclusion and Recommendations

Conclusion and recommendation

The need of county government not to depend too much on National revenue transfer

- The counties have been spending more than the revenue allocated to them by the national government
- The counties' expenditures on recurrent and development have consistently increased since devolution . Total expenditure has increased over the last five financial years from Kshs. 169.4 billion in financial year 2013/14 to Kshs. 295.3 billion in financial year 2015/16.

County Revenue & Expenditure Analysis

ITEM	2013/14	2014/15	2015/16	2016/17
Revenue	216.3	262.35	294.79	312.82
National Transfers	190	2.5	259.77	280.30
Local Revenue	26.3	33.85	35.02	32.52
Recurrent	132.8	167.56	191.85	215.71
Personnel Emoluments	77.4	103.1	118.65	130.97
Operations & Maintenance	51.7	64.46	73.2	84.74
%Recurrent To Total Expenditure	78%	65%	65%	68%
Development	36.6	90.44	103.45	103.34
%Development To Total Expenditure	22%	35%	35%	32%
Total	169.4	258	295.3	319.06
Deficit/Surplus	46.9	4.35	-0.51	-6.23

- Expenditure in these years has been directly proportional to county revenue. i.e. Kshs. 216.5 billion in financial year 2013/14 to Kshs. 295 billion
- This demonstrates the county governments' dependency on national transfers which are generally adjusted to take account of increases in cost of living

- On the other hand, own source revenues have not been growing at a rate sufficient to complement national transfers. It will be very difficult to increase access to public services going forward without putting greater effort in raising additional revenues at the county level

Recommendations

- Ensure that the ongoing projects are completed before launching new projects and clear any pending bills and arrears owed to suppliers.
- Crowding in Private sector contribution to delivery of infrastructure projects
- Reduce Rigidity in recurrent spending (especially interest payments and transfers to counties, as well as compensation to employees).
- Improve budget execution and absorption of development budget
- Project management committee should ensure the ongoing infrastructure project are completed and suppliers paid within the specified timelines for optimal returns to investment and to spur private sector activity.
- Improved debt management could reduce interest payments through a plan to retire short-maturity and expensive commercial debt.
- Enhance own source revenue mobilization at the county level to reduce dependency on transfers from the national government.
- Capping of interest rates by the government