AIB-AXYS AFRICA

FY24/25 BUDGET POLICY STATEMENT REVIEW

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AIB-AXYS 2024 Budget Policy Statement Review

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The 2024 Budget Policy Statement (BPS) themed "**Sustaining Bottom-Up Economic Transformation Agenda for Economic Recovery and Improved Livelihoods**," forms part of the Medium-Term Plan IV (2023-2027) themed Bottom-up Economic Transformation Agenda. The incumbent regime continues to execute bold policy responses to mitigate the adverse impact of geoeconomic shocks such as supply-chain disruptions, elevated interest rates and losses occasioned by extreme weather events.

The fiscal policy stance for the FY 2024/25 aims to support the Bottom-Up Economic Transformation Agenda (BETA) through **a growth-friendly fiscal consolidation plan**. The targeted outcomes of budget implementation are **to bring down the cost of living, increase employment, enhance equitable distribution of income, social security while also expanding the tax revenue base, and increasing foreign exchange earnings.** The policy framework aims to reignite economic growth by focusing on five core pillars: Agriculture, Micro, Small and Medium Enterprises (MSMEs), Housing and Settlement, Healthcare, and the Digital and Creative Economy.

KEY POLICY FOCUS AREAS

- **Agriculture**

The objective is to augment food production while mitigating costs through targeted subsidies for essential farm inputs such as fertilizers, seeds, seedlings, and irrigation support. Additionally, efforts will be directed towards enhancing post-harvest management and fostering agricultural market development.

- **Micro, Small and Medium-Sized Enterprises**

The focus here lies in fostering a conducive business environment through initiatives such as the establishment of industrial parks and incubation centers. Moreover, measures to facilitate access to affordable finance and streamline business licensing processes are highlighted to stimulate entrepreneurial endeavors.

- **Housing and Settlement**

The strategy aims to deliver at least 250,000 affordable housing units annually, provide long-term affordable housing finance schemes, and create job opportunities by engaging Technical and Vocational Education and Training (TVET) graduates and local artisans.

- **Affordable Healthcare**

Healthcare reforms include the establishment of a Social Health Insurance Fund and a shift towards preventive and promotive healthcare measures. Enhanced access to healthcare services will be pursued through the engagement of Community Health Promoters at the household level.

- **Digital Economy**

This pillar underscores the importance of investing in digital infrastructure and accelerating the digitization and automation of government services. Initiatives such as the national digital ID program, exemplified by Maisha Namba, are slated to drive progress in this domain.

The 2024 Budget Policy Statement (BPS) targets to narrow the fiscal deficit to 3.9% of GDP in FY 24/25, down from an estimated 5.1% of GDP in FY 23/24. However, it is worth noting that this adjustment hinges on the assumption of bolstered fiscal revenue, targeting a rise to 19.1% of GDP by FY 2024/25 through targeted revenue enhancement measures. Despite these ambitions, concerns linger regarding the feasibility of achieving revenue targets, particularly considering recent fiscal revenue shortfalls. The optimistic nature of these targets underscores the need for prudence and proactive measures to address revenue shortfalls.

The projected total fiscal spending and transfers for FY 2024/25 stands at KES 4.2Tn, marking a 12.1% increase compared to the preceding year. This growth is primarily attributed to escalated interest payments and augmented allocations for development expenditure, aligning with the government's developmental agenda. To bridge the anticipated deficit, the government intends to pursue a mix of external and domestic borrowing. External borrowing is estimated at KES 326.2 Bn while domestic borrowing is projected at KES 377.7 Bn. This financing strategy aims to balance fiscal requirements while managing debt sustainability concerns.

Table 1: Proposed Budget Summary

	FY23/24 Initial Estimates	FY23/24 Supplementary Budget I	FY24/25 BPS Estimates	Change y/y
Total Revenue	**2,985.60**	**3,047.60**	**3,445.50**	▲ **15.4%**
Ordinary Revenue	2,571.20	2,576.80	2,958.60	▲ **15.1%**
Ministerial Appropriation in Aid	414.4	470.8	486.9	▲ **17.5%**
Expenditure and Net Financing	**3,746.60**	**3,981.50**	**4,198.80**	▲ **12.1%**
Recurrent expenditure	2,536.30	2,793.90	2,873.60	▲ **13.3%**
Development Expenditure	760.6	743.7	861.6	▲ **13.3%**
CFS - Interest and Pensions	975.9	1,119.6	1,229.7	▲ **26.0%**
County Transfers	429.7	423.9	438.9	▲ **2.1%**
Fiscal Deficit	**(761.1)**	**(934.0)**	**(753.3)**	▼ **(1.0%)**
Net External Financing	131.5	412.1	326.2	▲ **148.1%**
Net Domestic Financing	587.4	474.5	377.7	▼ **(35.7%)**

Source: National Treasury, AIB AXYS Estimates

MEDIUM TERM FISCAL POLICY

The government's medium-term fiscal policy is meticulously crafted to underpin the Bottom-Up Economic Transformation Agenda. At its core, this strategy endeavors to arrest the perennial ascent of public debt while concurrently optimizing service delivery across sectors vital to national development.

Revenue Mobilization:

- Implementation the National Tax Policy to enhance tax administration, ensure clarity in tax laws, and control tax expenditures.
- Execution the Medium-Term Revenue Strategy to strengthen tax revenue mobilization efforts to reach 20% of GDP by 2027/28.
- Focus on non-tax revenue measures through services provided by government ministries, departments, and agencies.
- Strengthening tax administration by the Kenya Revenue Authority through technology adoption, enhancing iTax and iCMS systems, and using e-TIMS.

Expenditure Reforms:

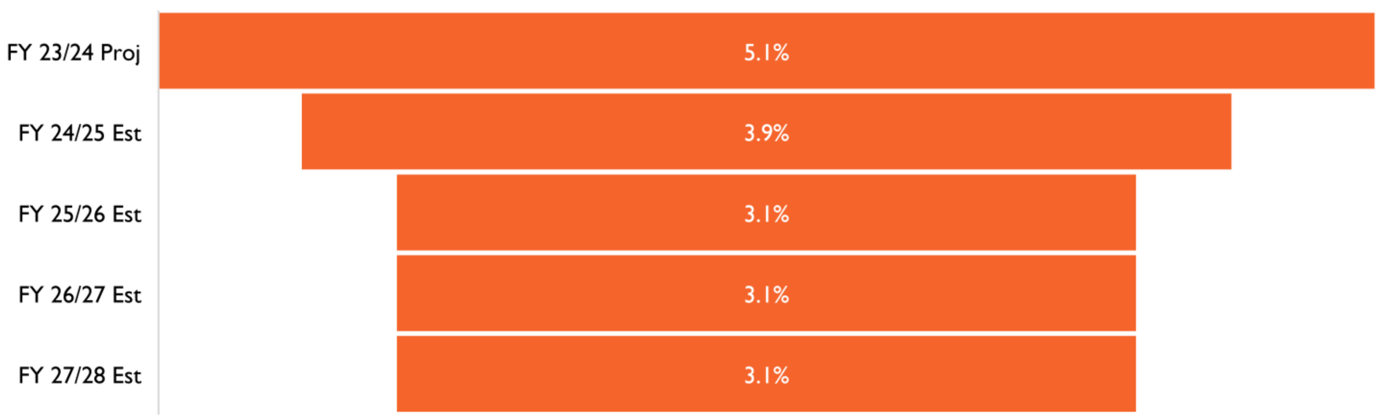
- Elimination of non-priority expenditures and rationalization of tax expenditures.
- Increase utilization of Public-Private Partnerships for commercially viable projects.
- Digitization of asset reporting through operationalizing the IFMIS asset module.
- Introduction an end-to-end e-Government Procurement System to enhance savings, efficiency, and transparency.
- Privatization and restructuring Government Owned Enterprises and Government Linked Corporations.

Deficit Financing Policy:

- Mobilization of resources mainly from multilateral and bilateral development partners.
- Utilization of commercial borrowing as a last resort to fund the fiscal deficit and repay maturing external debts.
- Meet net domestic financing requirements through Treasury bond issuances.
- Maximize concessional loans while limiting non-concessional and commercial external borrowing.

The fiscal consolidation plan aims to reduce the fiscal deficit, including grants, from a projected 5.1% of GDP in FY 2023/24 to 3.1% of GDP in FY 2027/28, while raising revenue collections to 20.2% of GDP and reducing total expenditures to 23.7% of GDP over the same period.

Chart 1: Budget Deficit as a % of GDP is Expected to Narrow



Source: National Treasury, AIB AXYS Estimates

BUDGETARY ALLOCATIONS

The government has estimated a total spending budget of KES 4.14Tn for fiscal year 2025, with allocations to all arms of government, transfer payments as well as county governments. This allocation scheme adheres to a value chain methodology, organized around five core clusters: Finance and Production Economy, Infrastructure, Land and Natural Resources, Social Sectors, and Governance and Public Administration.

Among the priority sectors receiving increased allocations are energy, infrastructure & ICT, healthcare, industry, trade, national security, social protection, environment conservation, water resources, and natural resource management.

County governments are set to receive a gross allocation amounting to KES 391.1Bn. Additionally, they will benefit from an extra KES 48.2Bn in conditional allocations sourced from loans and grants. Recognizing concerns regarding counties' adherence to fiscal responsibility principles and their performance in Own Source Revenue (OSR) collection, the BPS proposes measures aimed at aiding counties in enhancing their OSR.

This structured approach to budgetary allocations reflects a commitment to fostering economic growth, enhancing social welfare, and promoting effective governance at both the national and local levels, thereby aligning with the overarching objectives of the government's fiscal policy.

Table 2: Sectoral Budget Allocation

Budget Allocations	FY23/24 Supp. I Estimates (KES Bn)	FY24/25 BPS (KES Bn)	% Change
Education	689.6	666.5	▼ (3.4%)
Energy, Infrastructure & ICT	494.7	505.7	▲ 2.2%
Public Administration & IR	299.4	351.7	▲ 17.5%
Governance, Justice and Law	240.3	250.9	▲ 4.4%
National Security	199.3	244.4	▲ 22.6%
Health	138.8	147.6	▲ 6.3%
Environmental Protection	125.5	128.0	▲ 2.0%
Agriculture	98.1	87.8	▼ (10.5%)
Social Protection	72.9	72.2	▼ (0.9%)
General Economic and Commercial Affairs	72.4	56.7	▼ (21.7%)

Source: National Treasury, AIB AXYS Africa Research

Our View

The 2024-2025 Budget Policy Statement presents a coherent strategy to sustain Kenya's economic transformation agenda, underpinned by a multi-pronged approach to revenue mobilization, expenditure reforms, and prudent deficit financing.

Positive Factors:

- The government's multipronged approach to boosting fiscal revenue through tax policy reforms, administration technology upgrades, and the new Medium-Term Revenue Strategy is encouraging. If successfully implemented, it could improve tax buoyancy and narrow the fiscal deficit over the medium-term.
- Proposed expenditure reforms like eliminating non-priority spending, scaling up PPPs, digitizing asset reporting and procurement systems signal a commitment to enhancing efficiency, transparency, and service delivery. This bodes well for productive public capital outlays.
- Prioritizing growth engines like agriculture, MSMEs, housing and healthcare through supportive policies and budgetary allocations could catalyze economic activity, employment, and consumption demand. The emphasis on the digital economy augurs well for innovation and productivity gains.

Risk Factors:

- Ambitious revenue targets of 19.1% of GDP in FY2024/25 in a challenging operating environment, raises fears of fiscal underperformance given past lags in fiscal revenue collections.
- Escalating fiscal deficits via supplementary budgets and continued reliance on expensive debt financing, poses debt sustainability risks, especially in economic downturns.
- Vulnerability to global economic headwinds such as financial tightening, trade tensions, and supply chain disruptions, threatening the projected economic growth momentum.
- Implementation challenges, including overcoming institutional inertia and executing proposed reforms across various fronts in a timely and effective manner.

Overall, the BPS lays out a pragmatic fiscal roadmap aligned to supporting Kenya's economic resurgence and transformation agenda. Vigilant implementation, continuous monitoring, and a readiness to proactively manage emerging risks would be imperative to inspire investor confidence and catalyze sustainable growth over the policy horizon.

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