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Fourth Quarter National Government Budget Performance 2019/20

Executive Summary

By the end of the fourth quarter of 2019/20, national government ministries, department and agencies (MDAs) managed to utilize 89% of their approved budget of Ksh 2.85 trillion. This means that about Ksh 316.2 billion remained unspent. Overall performance in government spending in 2018/19 was however marginally better, by two percentage points than in 2019/20.

Trend analysis for 2016/17 to 2019/20 confirmed, albeit progressive improvement, that the biggest challenge is on uptake of development budget relative to recurrent budget. Despite slip up in performance, uptake of development budget was higher in 2019/20 than in 2018/19. The three least performers, with the highest proportion of unspent funds, over 15%, are Agriculture, Rural and Urban Development, Social Protection, Culture and Recreation and Education sectors in that order implying poor results in service delivery to citizens.

Notably, overall performance by sectors mask salient issues. The Infrastructure and Information, Communication Technology with substantially high absorption rate (90%) had a project, power generation with one of the lowest absorption rates (54%). The earmarked geo-thermal power generation project may end up delaying/stalling and incurring attendant penalties including cost overruns due to insufficient funds.

The primary causes of low budget execution are related to the unpredictability of public funds and overall delays in timely release of funds to spending units. On the former, there are questions around optimistic revenue projections, evident by widening the gap between actual revenue collected against revenue projections. As a consequence, this leads to frequent revision of the budgets to accommodate the shortfall in revenue. Reduced realization of revenue receipts were impacted negatively by COVID 19 pandemic. Findings also note delays in release of cash, often in quarter three and four, which leaves MDAs with little time to utilize these funds.

Furthermore, under release/non-release of funds according to the approved budget is the other notable challenge. Nearly half of target appropriation in aid was not realized and 34% of donor financed portion of development was not released at all owing to various administrative hurdles including lengthy and complex procurement procedures and unpredictability of off-budget donor funds.

To this end, the IEA proposes the need for the government to strengthen revenue forecasting capacity to improve the predictability of public funds; strengthen and enforce reporting of AiA and scale down projections donor disbursements in subsequent financial years for more accurate budget planning. In addition, the reintegration of off-budget donor funds is not only key in enhancing reporting but also overall transparency. These actions are key to averting rise in pending bills, volatility in planning and budgeting, and citizen well-being.

1.0 Introduction

Budget implementation by end of the fourth quarter of 2019/20 was punctuated by disruptions to economic activities from the effects of the COVID 19 pandemic which was declared a pandemic on the 13th of March 2020 by WHO. As a result, two supplementary budgets were introduced, one in early April to cater for the response to the pandemic and another one just before end of the financial year 2019/20, making it a total of three. This report uses the 2019/20 National Treasury Fourth Quarterly Economic and Budgetary Review Reports and Office of the Controller of Budget's Fourth Quarter Budget Implementation Reports to assess and analyze how the national government of Kenya budgetary management is faring against its own targets. In addition, this is brief seeks to highlight key implementation challenges and gaps and propose corrective measures.

IEA provides this analysis every quarter. For more reports, please visit www.ieakenya.or.ke

2.0 Overall Revenue Performance Analysis

The National Treasury had by the end of financial year 2019/20 received Ksh 58.4 billion short of its annual revised revenue target of Ksh 2,635.4 billion from both domestic and external sources[1]. This translated to a performance of 97.8%. Nevertheless, the actual total revenue receipts of Ksh 2,578 billion dipped marginally by almost 2% in 2019/20 relative to the previous financial year.

Specifically, total revenue and grants (excluding borrowing) received amounted to Ksh. 1,753.4 billion against a target of Ksh. 1,899.8 billion, by the end of June 2020 (see table 1). This performance in revenue and grants was below target by Ksh. 146.4 billion (7.6% gap). Tax revenue which contributed about 56% of total receipts into the Consolidated Funds, had impressive performance of 99.1% relative to revised estimates. Notably, albeit contributing only 6% of total revenue receipts in 2019/20 was impressive performance in collection of investment revenue, mainly dividends from state owned enterprise (parastatals). Investment revenue receipts significantly went up from Ksh 26.8 billion in 2018/19 to Ksh 103.4 billion, representing massive growth of 285.8%. The other notable performance was collection from import duty and taxes on international trade that were above the target by 2.1% and 5.7% respectively. For the latter, however actual collection reduced by 8.3% relative to collection in 2018/19.

Conversely, underperformance in overall revenue receipts was attributed to less than optimal collection of non-tax revenue which missed its target by 18.4%, with the major culprit being ministerial appropriation in aid (AiA)[2]. Equally realization of proceeds from overall domestic borrowing which was short by 16% and external grants from development partners which missed the target by 76.8% are the other reasons behind overall revenue underperformance.

Figure: 2.5: Trends in Auditor Opinions for the Ministry of Agriculture (National Government)

	2018/19 Actual	2019/20		Deviation (%)	% Growth 2019/20 vs 2018/19
		Actual	Target		
Total Revenue (a+b)	1,701.7	1,733.6	1,864.8	-7.6	1.9
a. Ordinary Revenue	**1,499.8**	**1,573.4**	**1,615.4**	**-2.7**	**4.9**
Import duty	106.9	98	95.9	2.1	-8.3
Excise duty	194.3	195.3	201.2	-3.0	0.5
PAYE	393.4	399.2	399.4	-0.1	1.5

[1]OCOB (August 2020) National Government Budget Implementation Review Report for the FY 2019/20. Republic of Kenya Office of the Controller of Budget.

[2]Ministerial AiA comprises revenue that specific ministries, department and agencies generate from services offered in terms of user fees. For example, the Ministry of Immigration charges fees for application and issuance of passports. Authority to spend these funds without having to remit to the Consolidated Fund comprises revenue known as Appropriation in Aid (AiA).

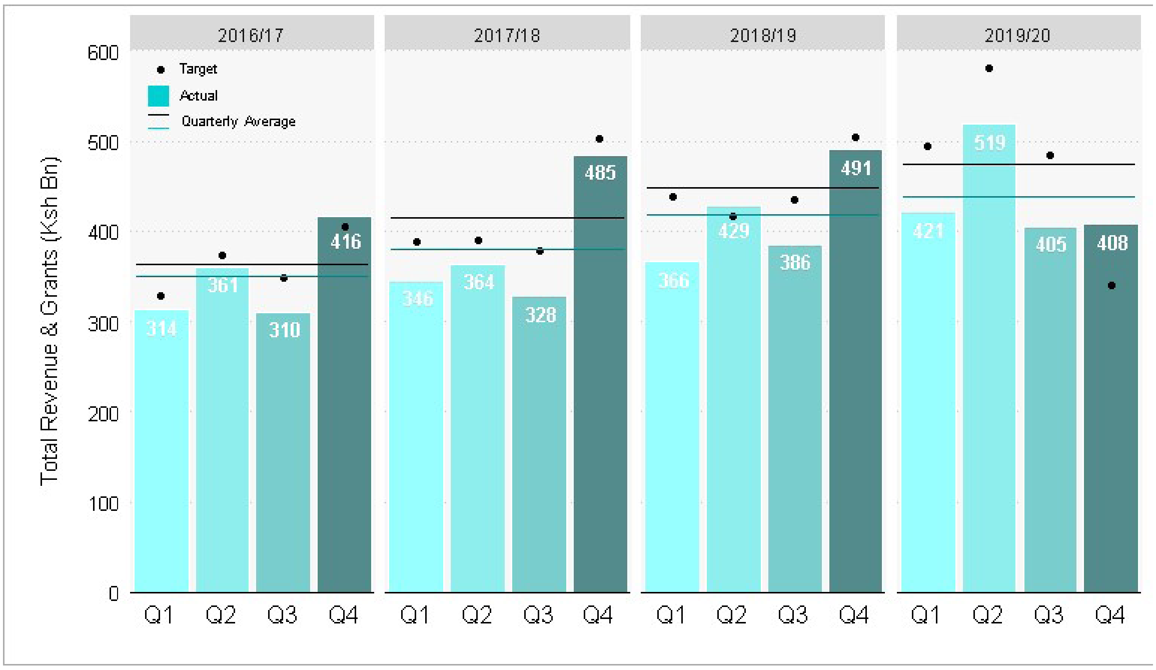
	2018/19 Actual	2019/20		Deviation (%)	% Growth 2019/20 vs 2018/19
		Actual	Target		
Other income tax	291.9	307.7	320.9	-4.3	5.4
VAT local	230.8	213.9	228.2	-6.7	-7.3
VAT Imports	183.4	169.8	171.9	-1.2	-7.4
Investment Revenue	26.8	103.4	104.6	-1.2	285.8
Traffic Revenue	4.1	3.6	4.6	-27.8	-12.2
Taxes on int'l trade and IDF	24.2	30	28.3	5.7	24.0
Other income tax	44.1	52.5	60.4	-15.0	19.0
b. Appropriation in Aid	**201.9**	**160.2**	**249.4**	**-55.7**	**-20.7**
o/w Railways Dev't Levy	21.3	23.3	22.7	2.6	9.4
c. External Grants	**19.7**	**19.8**	**35**	**-76.8**	**0.5**
Total Revenue and External Grants	**1,721.4**	**1,753.4**	**1,899.8**	**-8.3**	**1.9**

Source: National Treasury 4th QEBR 2019/20

Although we have witnessed an upward trend in receipts of total revenue and grants[4] in absolute terms from Ksh 1.40 trillion (against a target of Ksh 1.47 trillion) in 2016/17 to Ksh 1.75 trillion (against a target of Ksh 1.90 trillion) in 2019/20, the common story, however, is government missing revenue targets (figure 1). In fact, this story has been pervasive for the last decade and thus a public policy concern.

Nevertheless, the missing piece in this story and as evident from figure 1 is that the gap between revenue collected against the target has been widening. This gap widened from 3.8% in 2016/17 to 7.8% in 2019/20 as visualized by the quarterly average lines for revenue target (above) and the one for the actual revenue collected. The extent of economic activities and other factors including administration of revenue collection being held constant, the widening gap is in part attributed to optimistic revenue forecasting. Lack of appropriate forecasting model and capacity is often blamed for inaccurate revenue forecast. It is also important to note that optimistic revenue projections are often driven in guise of widening budget deficit due to growing appetite for government expenditure.

Figure: 2.5: Trends in Auditor Opinions for the Ministry of Agriculture (National Government)



Source: The National Treasury | Quarterly Economic and Budget Review (QEBR) various issues

[4]Total Revenues and Grants comprise Ordinary Revenue, A.I.A and Grants

2.1 Performance in Domestic Resource Mobilization

Performance of domestic resource mobilization is often synonymous with performance by Kenya Revenue Authority (KRA) given that it accounts for the bulk, about 93% of total ordinary revenue (both tax and part of non-tax income) that is received by the National Treasury. The remaining revenue component not collected by KRA as seen from table 1 are two. The first is investment revenue which is collected directly by the Department of Government Investment and Public Enterprises, National Treasury. The other is traffic revenue collected by the National Transport and Safety Authority (NTSA). By end of the fourth quarter, ordinary revenue was 2.7% behind its target as seen from table 1. Were it not for the fact the national budget was revised twice, the second time in early April 2020, driven by the need to not only make expenditure provisions for response to COVID 19 but to also factor in expected fall in revenue, the deviation (difference between actual ordinary revenue collected and the annual target) would have been wider. Indeed, further loss of revenue was as a result of tax relief measures taken to mitigate against the effects of COVID 19 pandemic. Following this dual effect, the anticipated ordinary revenue target was revised downwards from Ksh 1,877 billion to Ksh 1,643 billion. The World Bank estimate of revenue losses is Ksh 39.3 billion while that of Parliament Budget Office (PBO) is Ksh 122.3 billion[5].

The best performance by KRA and as alluded earlier was in the collection of trade taxes through its Custom Services department which surpassed its target. Performance of other domestic taxes including income tax, VAT, and excise duty through KRA's Domestic Taxes Department was only slightly off the mark. In contrast, the lowest-performing agency was NTSA in regard to the collection of traffic and license fees. It is not clear the reasons behind this performance but it is likely due to declining number of licenses issued to public service vehicles and perhaps low compliance levels as well.

Furthermore, figure 1 presents peculiar issues in regard to the understanding inflow of domestic resources (ordinary revenue) and implications for financing the budget. Nominal revenue receipts are highest in the second and the fourth quarter for the period 2016/17 to 2019/20. This coincides with periods when revenue collection is highest on revenue sources such as corporate tax. When denominated by quarterly GDP[6] as shown in figure 2, it follows a similar trend and pattern.

It is not clear from a cursory view what explains this phenomenon. However, theoretically, when the economy is doing well, revenues are expected to be on the rise and vice versa. This is based on the fact that performance in tax revenues (ordinary revenues) is directly proportional to performance in economic growth. In fact, KNBS reports show that quarterly economic growth went up from 5.2% in quarter 1 of 2019/20 to 5.5% in quarter 2 but there was a dip in quarter 3 to 4.9%. This denotes positive correlations (relationship) between revenue performance and economic growth. Although results for Q4 of 2019/20 have not been released, projections show an imminent contraction of the economy at the height of increasing effects of COVID 19 pandemic. For example, the service sector, that has over the years remained resilient was affected significantly especially the hospitality and transportation sub-sectors. Indeed, all the other sectors including agriculture and industry were equally affected and thus the reasons behind the anticipated slowdown. Figure 2 summarizes variations of tax revenues across the quarters in relation to the quarterly economic output. A higher change in the revenue-to-GDP ratio is ideal, it implies that the growth of tax revenue is higher compared to growth in GDP at that point in time. What figure 2 reveals however is a general downward trend of tax revenue-to-GDP ratio, from 17.0% to 15.4%% over the period 2016/17 to 2019/20. This is in actual sense below the government's target of 18%.

Moreover, a similar trend is observed for the quarter-on-quarter[7] averages of tax revenue-to-GDP ratio revenues. Overall, this implies that growth in GDP is not resulting in the corresponding yield in tax revenues, suggesting

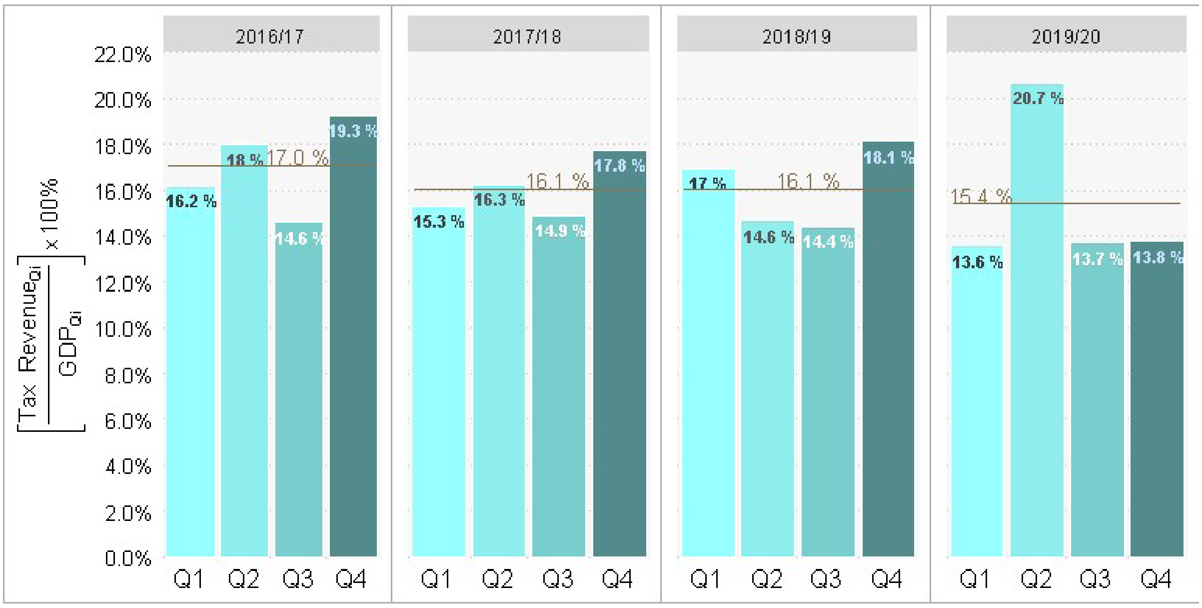
[5]The World Bank estimate of revenue losses is Ksh 39.3 billion while that of Parliament Budget Office (PBO) is Ksh 122.3 billion

[6]GDP – Gross Domestic Product which is a measure of size of the economy

[7]Quarter-on-quarter (QOQ) refers to comparison of one fiscal quarter and the previous fiscal quarter

among other issues, constraints related to the changing structure of the economy. Other attributable factors include inadequacies of revenue administration and collection system resulting in leakages as well as questions on compliance level.

Figure 2: Trends in % Tax Revenue (Ordinary Revenue) to GDP



Source: The National Treasury | Quarterly Economic and Budget Review (QEBR)

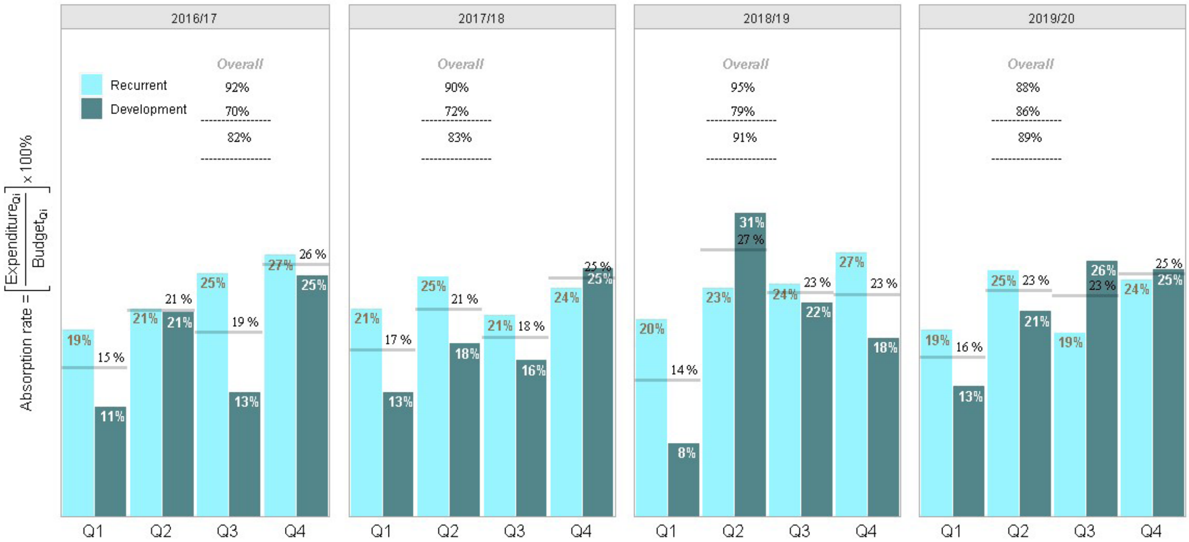
2.2 Emerging Issues

- Modest economic growth is not translating to improved revenue yield due to changing structure of the economy. For example, our reliance on the agricultural sector which contributed to over 30% to GDP in 2019 compared to declining manufacturing sectors is evident of this economic structural issues given that realized taxes from the former are significantly lower.
- There is need for the government to put in measures to stimulate economic rebound post COVID pandemic towards progressive revenue path.
- Untimely revenue inflows are a potential for liquidity risks among MDAs (spending units). It is important to note that management of the cash flows captured as revenue receipt to the National Treasury and how it is consequently released to spending units is critical in ensuring smooth budget implementation.

3.0 Government Spending

This section reviews and analyses national government budget implementation in terms of ability of national government spending units (MDAs) to utilize their approved budget to achieve planned outputs. This is often defined as absorptive capacity and measured by absorption rates. This section assesses absorption of funds and how this affects budget execution given its implications on service delivery. By the end of the fourth quarter, out of an annual budget of Ksh 2.85 trillion the Ministries, Departments and Agencies (MDAs) for the national government failed to spent Ksh 316.2 billion (11% of annual budget). A breakdown of the annual budget shows that the proportion of unspent budget was relatively higher for development budget, 14% compared to 12% for recurrent budget (see figure 8). Overall performance in government spending was better in the previous year where a smaller proportion of the aggregate annual budget remained unspent (8.8%) compared to 11% for 2019/20. Although overall government spending performance was better in 2018/19, the portion of unspent development budget was comparatively higher by seven percentage points. This implies more constraints to spending of development budget for 2018/19 relative to 2019/20.

Figure 3: Trends in Absorption Rates



Source: Controller of Budget | Budget Implementation and Review Reports (QEBR)

Further disaggregated information of absorption rates trends across quarters for period of 2016/17 to 2019/20 as shown in figure 3 confirms that the common challenge for the national government is less than optimal absorption (low uptake) of development budget. Specifically, development budget across the four financial years recorded lower absorption rates compared to the rates for recurrent budget. It therefore is important to underscore that under spending of development budget implies that completion of capital related projects will be delayed/stall, thus undermining service delivery benefits to citizens.

Notably, the national government has made progressive improvement in reducing the proportion of unspent development funds by the end of the financial year, from 2016/17 to 2018/19 albeit a dip in 2019/20. This is shown by the narrowing gap between quarterly-average of actual total expenditure against quarterly average target (see figure 3).

Moreover, a breakdown of national government spending in 2019/20 shows variations in terms of percentage of unspent funds against annual recurrent and development budget across sectors. On the one hand, the best performing sectors with the least unspent funds, less than 8% are the GJLOS, Energy, Infrastructure and ICT and National Security in that order (see table 2). On the other hand, the least performers, with the highest percentage of unspent funds, over 15%, are Agriculture, rural and urban development; Social Protection, culture and recreation and Education in that order.

Table 2: Absorption Rates for Recurrent and Development Budget by Sectors in 2019/20

	Recurrent				Development			
	Exchequer Issues (Ksh Bn)	Actual Expend. (Ksh Bn)	Propor-tion of releases spent (%)	% of funds not spent against annual target	Exchequer Issues (Ksh Bn)	Actual Expend. (Ksh Bn)	Proportion of releases spent (%)	% of funds not spent against annual target
Agriculture, Rural and Urban Development	17.1	17.2	100.6	41.1	25.9	34.5	133.2	20.1
Education	410.7	413	100.6	13.9	9.7	16.7	172.2	20.9
Energy, Infrastructure and Information, Communi-cation Technology	**12.6**	**76.5**	**607.1**	**14.1**	**180.4**	**345.3**	**191.4**	**9.4**
Environmental Protec-tion, Water and Natural Resources	16.8	19.6	116.7	19.8	29.2	52.9	181.2	13.1

	Recurrent				Development			
	Exchequer Issues (Ksh Bn)	Actual Expend. (Ksh Bn)	Proportion of releases spent (%)	% of funds not spent against annual target	Exchequer Issues (Ksh Bn)	Actual Expend. (Ksh Bn)	Proportion of releases spent (%)	% of funds not spent against annual target
General Economic and Commercial Affairs	8.3	8.5	102.4	46.4	16.2	15.7	96.9	11.9
Governance, Justice, Law and Order	186.6	184.5	98.9	5.6	10.7	13.2	123.4	-1.5
Health	53	66.7	125.8	12.4	30.4	38.8	127.6	11.4
National Security	138	137.7	99.8	7.4	2.2	8	363.6	16.6
Public Administration and International Relations	149.7	156	104.2	7.3	59.4	62.6	105.4	25.4
Social Protection, Culture and Recreation	37.2	31.3	84.1	19.6	21.5	26.8	124.7	30.1
Total	1,030	1,111	107.9	12.2	385.6	614.5	159.4	13.8

Source: 4th Quarter OCOB Implementation and Review Report 2019/20

Further disaggregation show that the least performing sectors, with lowest uptake of recurrent budget for 2019/20 and by a significant proportion are the General Economic and Commercial Affairs and Agriculture, Rural and Urban Development sector with 46.4% and 41% unspent funds respectively On the other hand, least performing sectors on the development side are Social Protection, Culture and Recreation and Public Administration and International Relations with 30% and 25% unspent funds respectively.

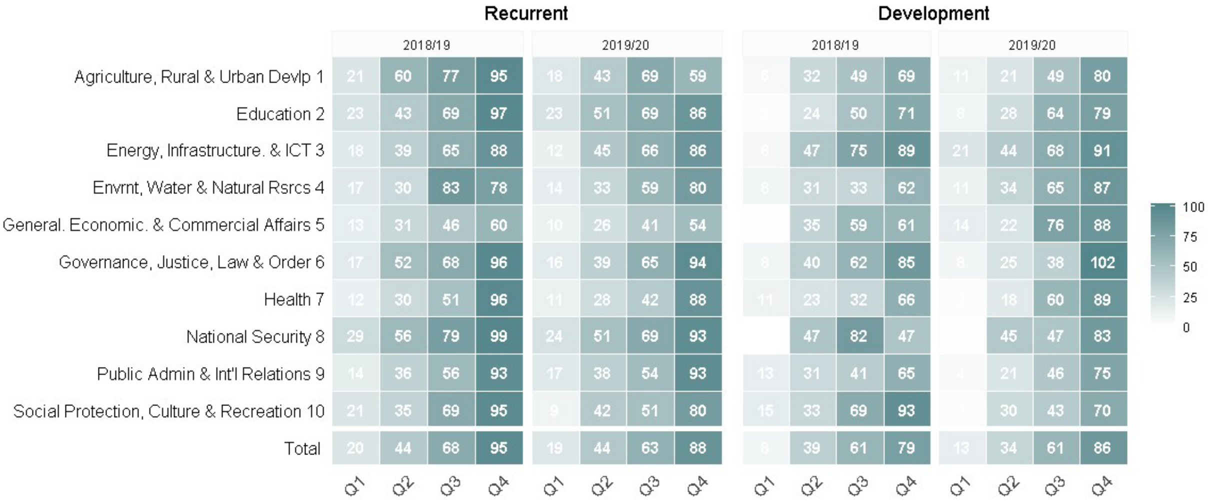
Overall performance by sectors however mask salient issues in terms of programmes or projects that are struggling in uptake of funds, requiring further scrutiny. For example, although the uptake of the budget for the Energy, Infrastructure and Information, Communication Technology has tremendously improved in the last two financial years (see fig 4), the power generation programme absorption rate was 54%. The other notable programmes that are struggling are devolution services (48.2%) and Government Advisory Services (54%) both under the Public Administration and International Relations sector and crop development and management (50%) and Development and Coordination of Blue Economy (55%) both under the Agriculture, rural and urban development sectors. Sports programme, (largely in charge of development of sports facilities) of the State Department of Sports had the lowest absorption rate (42.4%) under the Social Protection, Culture and Recreation Sector. Reports blame this on lack of funds. Of note too is the National Social Safety Net progtramme, that takes up just over half of the sector's budget with an absorption rate of 81.8%.

By and large, low absorption rates in the programmes noted above imply poor service delivery results to citizen in terms of delays in the earmarked geo-thermal power generation project and administration of National Social Safety Net programme., for example. Other negative consequences and financial risks arise whenever funds are not availed on time to pay suppliers or contractors resulting to penalties in form of project cost overruns. As a consequence, tax revenue has to be set aside to defray these cost as opposed to meeting other budgetary needs.

3.1 Comparing Spending by Sectors Across Quarters and Years

Disaggregation of MDAs absorption rates and comparison between 2018/19 and 2019/20 presents some interesting findings as shown in figure 4. Spending on recurrent budget side shows that although overall performance was better in 2018/19 relative to 2019/20, there was one sector, Environmental, water and natural resources that performed slightly better in 2019/20. Similarly, spending on development budget as was noted earlier, performed better in 2019/20 relative to 2018/19 but there was one sector, Social Protection, Culture and Recreation that performed better in 2018/19 relative to 2019/20.

Figure 4: Distribution of Cumulative absorption rates across sectors



Source: Controller of Budget | Budget Implementation and Review Reports (BIRR) various issues

Other notable facts are that by the end of Q2, the average spending for all the 10 sectors was less than 50% of their budgets, at 44% for recurrent in both 2018/19 and 2019/20. This was even lower for development activities at 39% and 34% in 2018/19 and 2019/20 respectively. Furthermore, 3 out 10 sectors had an absorption rate above 50% for recurrent spending by the end of Q2 in 2018/19, this reduced to 2 in 2019/20.

What is noticeable from figure 3 is that the absorption rates have tended to peaks in Q3 and Q4. Specifically, spending gradually peaks in Q4, Ksh 677 (29.3%) followed by, Q3: Ksh 604 (26.1%), Q2: Ksh 583 (25.2%) and lastly Q1: Ksh 449 (19.4%) which correlates with revenue mobilizations as observed in Figure 1. Smooth budget execution is hampered by uneven cash releases and in particular late disbursement towards the last two quarters of the financial year thus undermining service delivery.

3.2 Causes of Low Budget Execution

This, in summary highlights some of the key causes of low budget execution based on findings noted in the preceding sections

- **Unpredictability of public funds**

Adjustments on the original approved budget during the fiscal year by introduction of supplementary budgets have been a common feature in the budgeting process in Kenya. While this is within the legal provisions, section 44 of the Public Finance and Management Act, the frequency and the magnitude of the adjustments may divulge challenges and weaknesses as far as budget planning is concerned. This also reflects revenue projections challenges and in turn may lead to unpredictability of public funds.

Figure 5: Trends in the Budget Revisions (Revenue and Expenditure)

Source: The National Treasury | Quarterly Economic and Budget Review (QEBR)

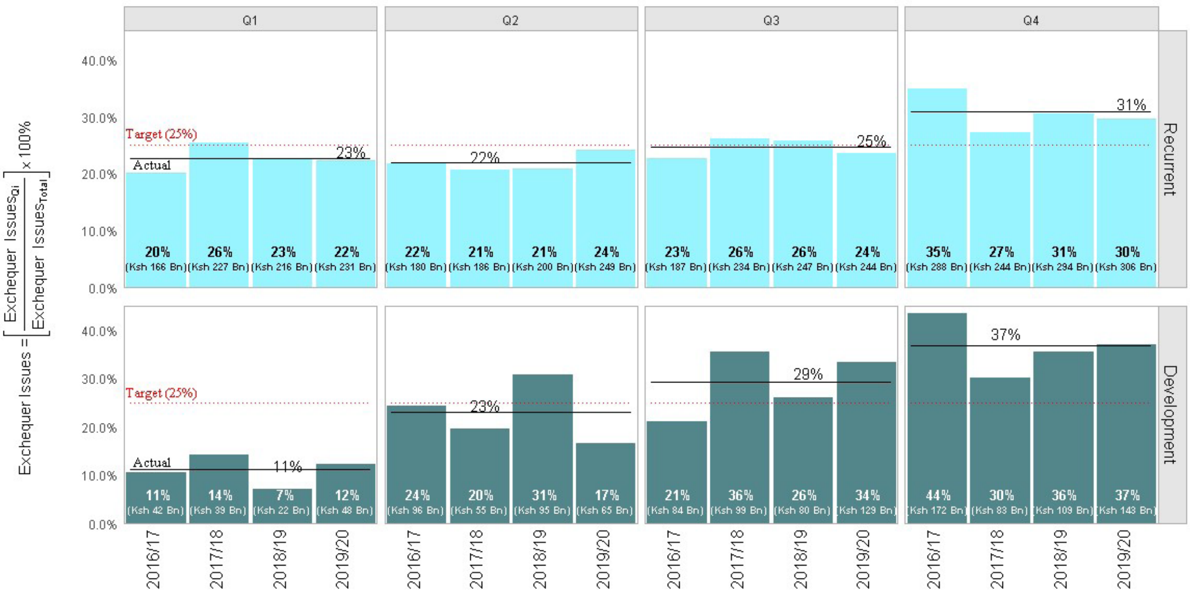
Figure 6 summarises budget revisions by MDAs[8] by noting deviations in the original budgets as approved at the beginning of the fiscal year (Q1) and the final budget at the end of the fiscal year (Q4). What we observe is that budget revisions have occurred both on estimates of revenue and expenditure and that in both cases, the direction of the revisions has been downwards. Of note is that the magnitude of the revisions has grown prominently on the revenue side than the expenditure side. Specifically, for 2019/20, respective adjustments on revenue and expenditure were downwards (11.9%) and (8.2%) respectively.

- **Delays in release of funds**

Overall delays in release of funds to spending units remains one of the challenges and causes of low budget execution. For example, whenever there are late releases, they disrupt budget execution and in particular affect implementation of on-going projects such as road maintenance which require continuous and predictable cash flow. Figure 6 shows quarterly distribution of cash disbursements to the MDAs by examining the share and amount issued at every quarter out of the annual disbursements. Ideally, about 25% of the total funds is expected to be disbursed on quarterly basis. In other words, by quarter 2 (half year), 50% of total funds should be disbursed, and eventually 100% by quarter 4.

[8]Ministries, Departments and Agencies (MDAs)

Figure 6: Quarterly exchequer issues



Source: Controller of Budget | Budget Implementation and Review Reports (BIRR)

Evidently, for both recurrent and development budget, most disbursements are received in Q3 and Q4. On average from 2016/17 to 2019/20, about 23% and 22% of the disbursements are issued in Q1 and Q2 respectively for recurrent spending compared to 25% and 31% issued in Q3 and Q4, implying delays in favour of the latter quarters. Equally for development budget, and over the same period, about 11% and 23% of the disbursements are issued in Q1 and Q2 compared to 29% and 37% issued in Q3 and Q4. This again implies delays in favour of the latter quarters, suggesting some catch up or compensation effect. As a result of delays in release of funds, MDAs invariably struggle to absorb these funds given limited time to the end of the financial year, reiterating an earlier noted point.

- **Funds not released (under release) according to approved budget**

It is clear that underutilization of budgetary provisions is not due to MDAs inability to spent available funds. This is shown in table 2 where expenditure for most of the sectors exceeded available funds (exchequer issues/releases). The only exception was two sectors, namely: *Social Protection, Culture and Recreation on the recurrent expenditure side and General Economic and Commercial Affairs on the development expenditure side.*

On the contrary, the challenge is with regard to under release of approved budget. Simply put, insufficient funds due to non-release of funds for whatever reasons is a key cause of low budget execution.

As seen in table 3 there is a portion of approved budget, either recurrent or development budget that is not released, comparing 2019/20 to 2018/19. In this table, the distinction between funds not released as a percentage of net budget (financed from government of Kenya-domestic revenue sources-exchequer issues) and gross which includes AiA for recurrent budget and funds from external sources (loans+grants) for development budget is made.

Table 3: % of approved budget not released

Item	2019/20		2018/20	
	Net Budget	Gross Budget	Net Budget	Gross Budget
Recurrent	6.1	14.4	3.6	10.1
MDAs	4.3	18.6	3.1	15.0
CFS	**8.3**	**8.3**	**4.1**	**4.1**
Development (MDAs)	**12.3**	**45.9**	**11.5**	**55.1**
Total	7.2	22.3	4.8	21.3

Source: National Treasury and OCoB

Unsurprisingly, the biggest proportion of funds not disbursed against approved budget is more pronounced with development expenditure compared to recurrent expenditure. Regarding the latter, the proportion of unreleased funds is on account of AiA. On the part of approved net development budget, funds not released increased marginally from 11.5% to 12.3%.

From table 1, nearly half of the projected AiA was not realized. This huge underperformance of AiA is according to Audit and Office of Controller of Budget reports attributed to under reporting and less than full disclosure especially by state corporations. Underreporting of AiA is sometimes driven by MDAs safeguarding what they have raised in revenue to cater for delays in disbursement of funds or during revenue shortfall. Despite clear guidelines for reporting as provided in the Public Finance Management Act, 2012, accounting and reporting of AIAs is still weak.

- **Dependence on volatile and unpredictable donor funds to finance development budget**

The percentage of approved development budget not released (46% in 2019/20 and 55% in 2018/19) is largely on account of delays in release of donor funds. Of note is that a substantial portion, about 38% in 2019/20 down from 49% in 2018/19 of development budget was donor financed. This means that of the 46% of approved development budget (Ksh 712.6 billion) not disbursed, about 34% was the portion financed from donor funds. Implementation of scheduled activities as per MDAs work plan is often affected whenever such events occur.

Delays in disbursement or withholding of funds by donors may be attributed to other related administrative challenges. One of the most common one is stringent disbursement procedures despite on-going efforts for harmonization and synchronization with government processes and timelines. Moreover, donors impose lengthy and complex procurement procedures not matched by governments initiatives to strengthen its procurement system. Tough reporting and accounting requirements, important as they may be for accountability and governance are the other set of administrative challenges.

It is important to note that not all donor funds are channeled through the government public finance system. There is a portion of donor funds (AiA) that is off-budget and is often channeled directly to projects being implemented by MDAs. These funds and how they flow is quite unpredictable and a contributor to low budget execution.

Overall, revenue performance also point to the possibility of over optimism by government planners about the levels of aid that can be disbursed in a given time[9]. Besides, timely completion of capital projects financed from borrowing may be adversely affected by attendant increases in cost due to time lapse. Further, lack of liquidity is often cited as a cause of the rise in pending bills[10] for MDAs. There is conflicting information on the quantum of outstanding pending bills. The OCOB notes that as at 30th of June 2020, 44 out of 71 MDAs reported cumulative pending bills amounting to Ksh 53.49 billion. National Treasury QEBR fourth quarter 2019/20 reports note that the amount is Ksh 334.2 billion (State corporations of Ksh 285.8 billion - 85.5% and Ministries/State departments Ksh 48.3 billion-14.5%). To this end, and based on Treasury Circular No7/2019 all MDAs are expected to prioritize payment of pending bills as a first charge in 2020/21.

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[9]Keng'ara R (2014) Effect of Funds Disbursement Procedures on Implementation of Donor Projects' in Homa Bay County, Kenya. Universal Journal of Accounting and Finance 2(1): 9-23, 2014 via www.hrpub.org

[10]Financial obligations at the end of the financial year that arise when a spending unit fails to settle payment for goods and services properly procured and delivered.

Key Messages

The National Treasury should strengthen the macro fiscal frameworks and revenue forecasting capacity in order to improve predictability of public funds:

The question of accuracy and capacity to undertake revenue forecasting is something that the National Treasury should pay close attention to as it has a bearing on resource allocation. The challenge is that the deviations between revenue projections and actual collection has been widening, indicating that the projections are set arbitrarily due to expenditure pressures. Therefore, a more appropriate model is critical backed by staff training for improved accuracy and budget credibility.

The Legislature should rein on the National Treasury to strengthen and enforce reporting of AiA

There is need for the National Treasury to strengthen and enforce reporting of AiA as provided for in the PFMA, 2012. This will go a long to improve transparency of information on off budget resources especially by government agencies (state corporations). Equally, this will also limit or improve oversight over any risk that may arise related to operations of these agencies.

Lack of information on AiA not only makes it difficult to conduct any analysis but it may also lead to malfeasance, thus undermining transparency and accountability. In this respect the Legislature should should exercise its oversight role by reining in on MDAs to account and report information on AiA for external pressure.

There is need for the national government to scale donor funds projections and strengthen reporting and integration of off-budget donor funds into government budget system

- **Modest donor funds projections:** The government should work with modest projections for expected donor funds especially for sectors that perennially have had low uptake of their development budget and where disbursement has been less than what was committed. This is important for a more accurate budget planning for projects and will deter delay in implementations and attendant risks.
- **The government and donors should come together and agree on simple, harmonized and synchronized donor disbursement procedures**: This is important to avert conflict and delays that are unduly time wasting leading to late disbursement or no disbursement at all.
- **We need more transparent accounting of off-budget donor financing:** When donors give money/grants "off budget" spent separately from government budget system this undermines reporting and transparency. Parliament could take steps to ensure that more aid is channeled through the budget and accounted at the level of MDAs.

NOTES

THE BUDGET FOCUS

The Institute of Economic Affairs is a public policy think tank which seeks to promote pluralism of ideas through open, active and informed debate on public policy issues by conducting policy research and analysis. IEA is independent of political parties, pressure groups and lobbies, or any other partisan interests.

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