MACRO-ECONOMIC DEVELOPMENTS AND OUTLOOK: FY 2024/25 AND MEDIUM-TERM BUDGET

PRESENTATION AT THE PUBLIC SECTOR HEARINGS HELD AT THE KENYA SCHOOL OF MONETARY STUDIES, NAIROBI

THE NATIONAL TREASURY AND ECONOMIC PLANNING

13th December 2023

PRESENTATION OUTLINE

1. Global Macroeconomic Developments
2. Domestic Macroeconomic Developments and Outlook
3. FY 2023/24 Budget Implementation and Supplementary Budget 1 for FY 2023/24
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5. Medium Term Sector Ceilings, FY 2024/25 – FY 2026/27
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1.1: Global Macroeconomic Economic Developments

- **Global** economy is experiencing challenges arising from:
  - Global supply chain disruptions due to ongoing conflicts in Eastern Europe and the Israeli-Palestinian war;
  - High interest rates limiting access to credit and exacerbating debt servicing costs;
  - Significant losses and damages due to frequent extreme weather events; and
  - Elevated commodity prices such as oil on account increased geopolitical fragmentation and global oil supply cuts.
- As such, **global growth** is projected to slow down to **3.0% in 2023 and 2.9% in 2024** from 3.5% in 2022
- **Advanced economies** are projected to record a slower growth of **1.5% in 2023 and 1.4% in 2024** from 2.6% in 2022 mainly driven by lower growth in the Euro Area.
- Growth in the **emerging market and developing economies** is projected to decline relatively modestly, from 4.1% in 2022 to **4.0% in both 2023 and 2024**, although with notable shifts across regions

1.2: Global Macroeconomic Developments cont..

- In **sub-Saharan Africa**, growth is projected to decline to **3.3% in 2023 from** 4.0% in 2022 reflecting worsening climate change related shocks, inflationary and exchange rate pressures, and domestic supply issues, including, notably, in the electricity sector.
  - Growth in the region is expected to rebound to **4.0% in 2024**, picking up in four fifths of the sub-Saharan Africa's countries, and with strong performances in non-resource intensive countries.

	Growth (%)			
	Actual		Projected	
Economy	**2021**	**2022**	**2023**	**2024**
World	6.3	3.5	3.0	2.9
Advanced Economies	5.4	2.6	1.5	1.4
Of which: USA	*5.9*	*2.1*	*2.1*	*1.5*
Euro Area	*5.3*	*3.3*	*0.7*	*1.2*
Emerging and Developing Economies	6.8	4.1	4.0	4.0
Of which: China	*8.4*	*3.0*	*5.0*	*4.2*
India	*9.1*	*7.2*	*6.3*	*6.3*
Sub-Saharan Africa	4.7	4.0	3.3	4.0
Of which: South Africa	4.7	1.9	0.9	1.8
Nigeria	3.6	3.3	2.9	3.1
Kenya*	7.6	4.8	5.5	5.5

2.1: Domestic Macroeconomic Developments and Outlook

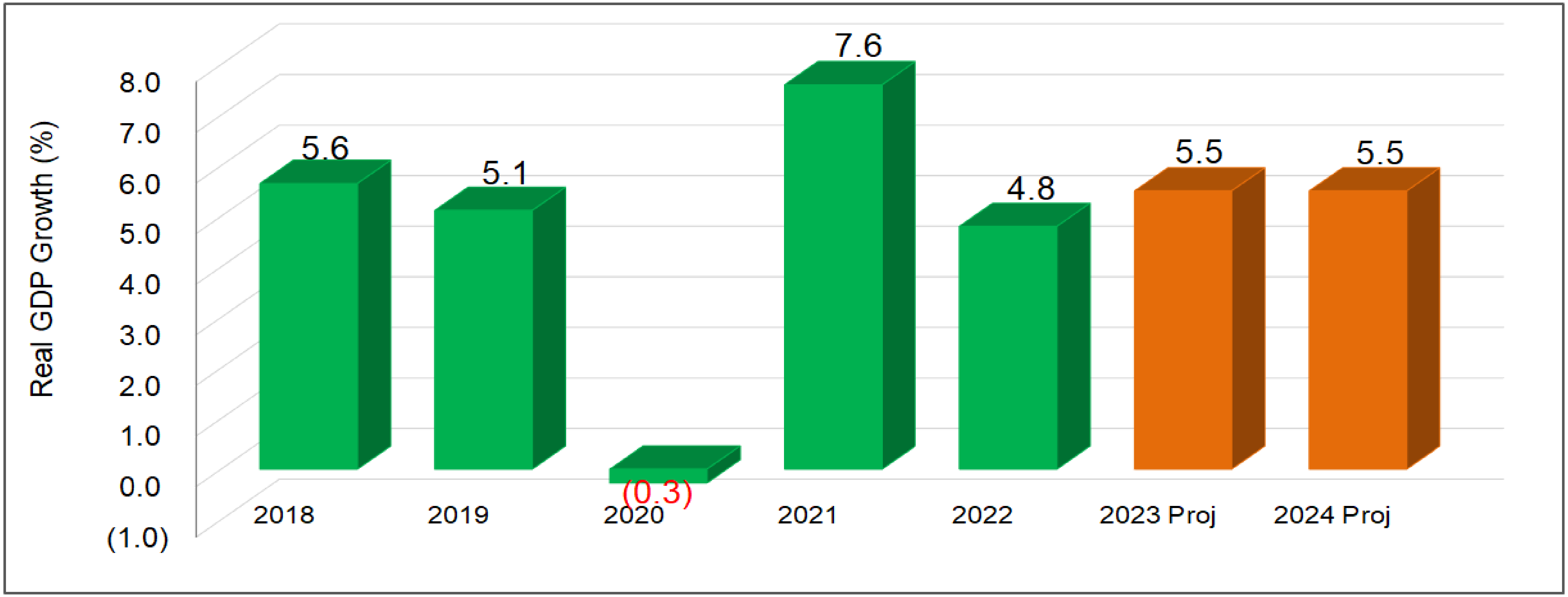
- Despite the challenging environment, the Kenyan economy is demonstrating resilience with growth performance well above the global and SSA average.
- In the first half of 2023, the economic growth averaged **5.45% (5.5% Q1 and 5.4% Q2).** This growth was primarily underpinned by:
  - A rebound in the **agriculture sector** (6.0% Q1 and 7.7% Q2) following improved weather conditions and the impact of fertilizer and seed subsidies provided to farmers by the Government.
  - Resilient industrial and **services sectors** with robust performance in:
    - Information and communication: Driven by increases in wireless internet and fiber-to-home subscriptions,
    - Accommodation and food services: Driven by recovery in tourism,
    - Financial and insurance: Due to increased yield on investment and increased return on deposits by commercial banks; and
    - Real estate: Supported by sustained expansion of the construction industry.

2.2: Domestic Macroeconomic Developments: All economic sectors recorded positive growths in the first half of 2023, though the magnitudes varied across activities.

Sectors	Annual Growth Rates		Quartely Growth Rates			
	2021	2022	2022 Q1	2022 Q2	2023 Q1	2023 Q2
1. Primary Industry	**0.5**	**(1.0)**	**(0.4)**	**(1.5)**	**5.8**	**7.6**
1.1. Agriculture, Forestry and Fishing	(0.4)	(1.6)	(1.7)	(2.4)	6.0	7.7
1.2 Mining and Quarrying	18.0	9.3	23.8	16.6	3.3	5.3
2. Secondary Sector (Industry)	**6.8**	**3.5**	**4.4**	**4.2**	**2.4**	**1.8**
2.1. Manufacturing	7.3	2.7	3.8	3.6	2.0	1.5
2.2. Electricity and Water supply	5.6	4.9	3.2	5.6	2.5	0.8
2.3. Construction	6.7	4.1	6.0	4.5	3.1	2.6
3. Tertiary sector (Services)	**9.6**	**6.7**	**8.5**	**7.7**	**6.0**	**5.9**
3.1. Wholesale and Retail trade	8.0	3.8	4.9	4.1	5.7	4.2
3.2. Accomodation and Restaurant	52.6	26.2	40.1	44.0	21.5	12.2
3.3. Transport and Storage	7.4	5.6	7.7	7.2	6.2	3.0
3.4. Information and Communication	6.1	9.9	9.0	11.2	9.0	6.4
3.5. Financial and Insurance	11.5	12.8	17.0	16.1	5.8	13.5
3.6. Public Administration	6.0	4.5	6.2	3.8	6.6	3.8
3.7. Others	10.8	5.2	6.7	5.5	4.9	5.0
of which: Professional, Admin & Support Services	7.1	9.4	13.1	10.9	7.3	5.5
Real Estate	6.7	4.5	6.0	5.0	5.2	5.8
Education	22.8	4.8	4.6	4.4	3.6	4.5
Health	8.9	4.5	5.7	4.4	5.4	5.0
Taxes less subsidies	11.9	7.0	9.5	6.1	5.3	3.8
Real GDP	**7.6**	**4.8**	**6.2**	**5.2**	**5.5**	**5.4**

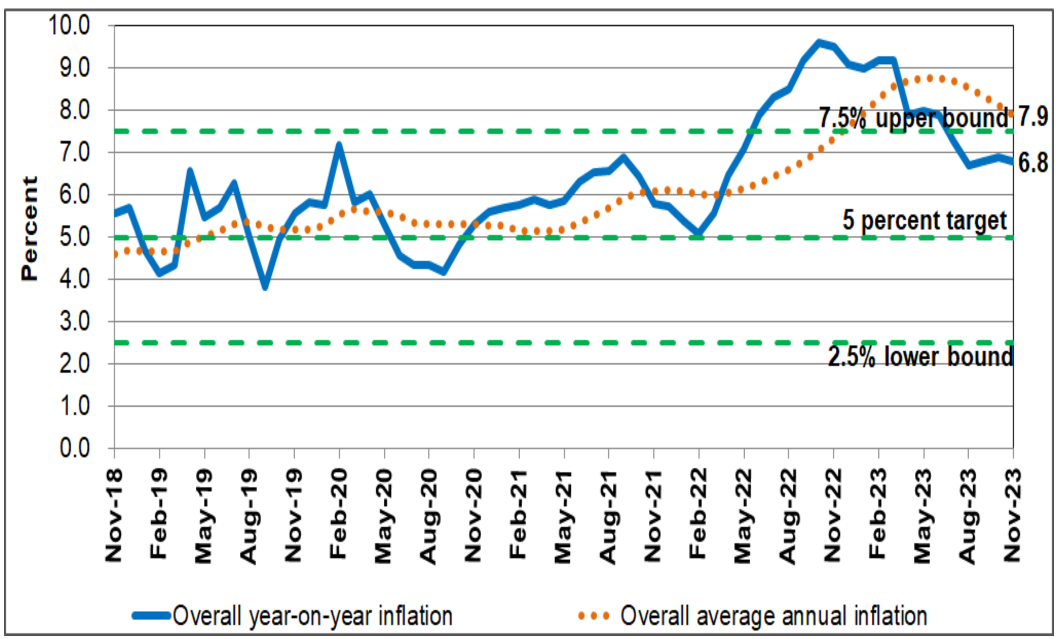
2.3: Domestic Macroeconomic Developments and Outlook cont'd....

- The economy is projected to have a growth of **5.5% in 2023 and 2024.** This growth outlook will be supported by:
  - Continued robust performance of the services sectors and the rebound in agriculture;
  - Resilient private domestic demand even as public sector consolidates;
  - Ongoing implementation of Government initiatives in priority sectors of BETA aimed to benefit people at the bottom of the income pyramid.
  - Focus on public-private-partnership (PPP) projects to support investments



2.4: Macroeconomic Indicators: Inflation eased and remained within the 7.5% upper target band in FY 2023/24 (July-November 2023).

- Inflation slowed down to **6.8% in November 2023** from a peak of 9.6% in October 2022 supported by lower food prices despite high fuel inflation.
- **Monetary policy stance remains tight** to anchor inflation expectations.
  - The CBR was raised to **12.5%** in December 2023 from **10.5%**.
  - The **interest rate corridor** established in August 2023 continues to ensure more effective transmission of monetary actions to market interest rates.

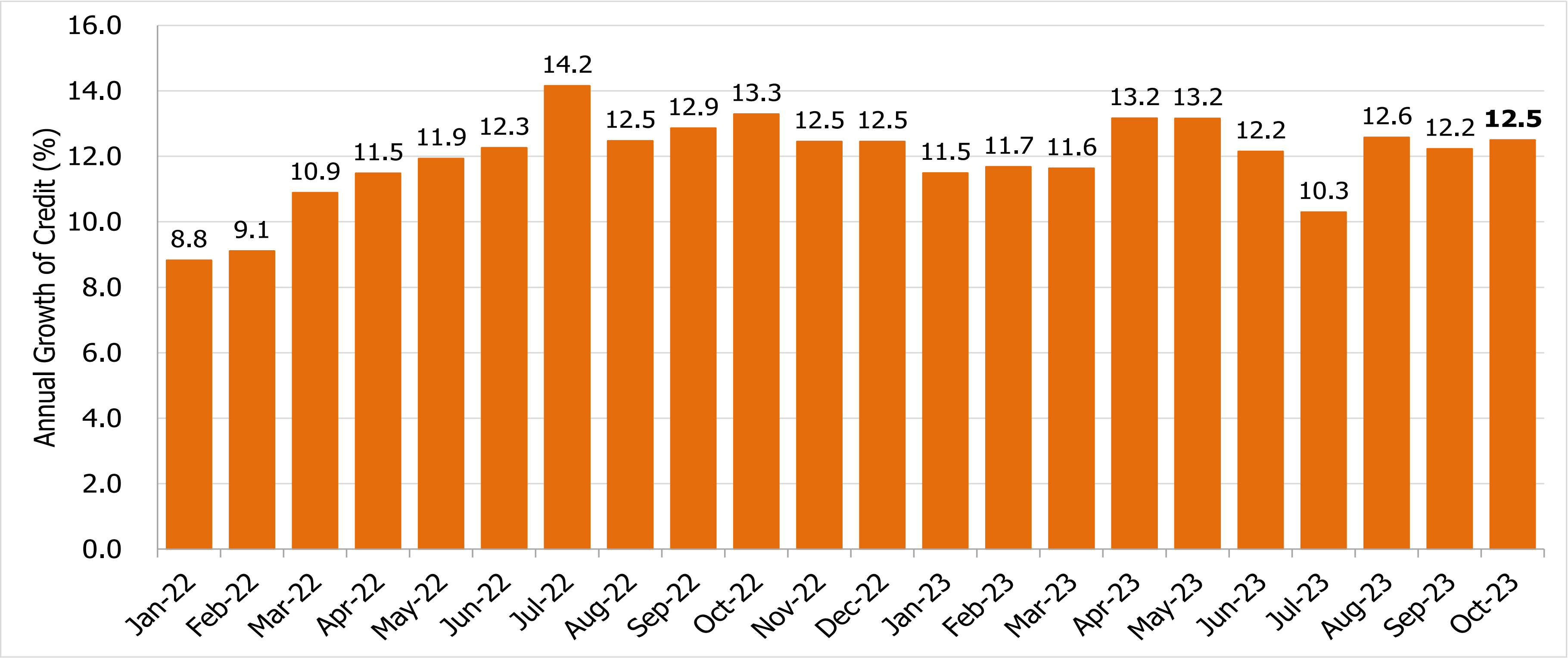


Overall inflation is expected to remain within the target range with **lower food prices** due to improved food supply supported by:

- favourable weather conditions; and
- Government interventions.

2.5: Macroeconomic Indicators: Credit to private sector remains resilient partly reflecting improving business conditions and demand for working capital.

- Lending to the private sector by commercial banks grew by **12.5% in October 2023** compared to 13.3% in October 2022.
- Strong credit growth was observed in; manufacturing (18.4 percent), transport and communication (16.2 percent), trade (9.9 percent), and consumer durables (10.8 percent).



2.6: External Sector Developments: The foreign exchange market remained relatively stable.

- Recovery to pre-COVID-19 levels in the tourism sector; Tourist arrivals improved by 34.1 percent in the 12 months to October 2023, compared to a similar period in 2022.
- Improvement in receipts from tea and manufactured exports. Receipts from chemicals and manufactured exports increased by 5.1 percent and 13.9 percent, respectively. The increase in manufactured exports receipts reflects strong regional demand.
- Resilient remittances which amounted to **USD 4,165 million in the 12 months to October 2023, and were 4.2% higher** compared to a similar period in 2022.
- Imports declined by 14.9 percent in the 12 months to October 2023 compared to a growth of 14.7 percent in a similar period in 2022, mainly reflecting lower imports across all categories except food.

As a result, current account deficit improved to 3.7 percent of GDP in the 12 months to October 2023, and is projected at 4.1 percent of GDP in 2023 and 4.2 percent of GDP in 2024.

The official foreign exchange reserves, at USD 6,746 million (3.62 months of import cover), continue to provide adequate cover and a buffer against any short-term shocks in the foreign exchange market.

3.1: FY 2023/24 Budget Implementation: Summary of Budget performance by end October 2023

- Budget execution in the first four months of FY 2023/24 progressed relatively well with revenues recording **a growth** of **13.0%** compared to a growth of 11.9% in the same period in FY 2022/23.
  - This revenue performance was however below target by **Ksh 47.6 billion mainly** on account of a shortfall in **ordinary revenues of Ksh 59.1 billion**
  - Over the course of the fiscal year, revenue performance is anticipated to improve in light of improved tax administration.
- Expenditures were below target by **Ksh 244.6 billion** on account of below target disbursements towards both recurrent expenditure and development expenditures.
  - The below target performance in expenditures is largely explained by the shortfalls in revenue performance and liquidity constraints.
- Fiscal operations of the Government by end of October 2023 resulted in an **overall deficit including grants** of **Ksh 58.4 billion (0.4% of GDP) against a target of Ksh 254.7 billion (1.6% of GDP).**

3.2: Supplementary Budget 1 for FY 2023/24

- In the first four months of the financial year, budget implementation has been negatively impacted by significant pressure points and elevated risks, including:

i. **By end October 2023**, ordinary revenue collection at **Ksh 713.9 billion** was below target by **Ksh 59.1 billion.**

ii. Expenditure requests received from MDAs to cover salaries, operations and maintenance, Government funded development projects and Development partners funded projects of over Ksh 291.4 billion had been made to the National Treasury.

- The elevated domestic interest rates and depreciation of the exchange rate.
- Need to maintain the primary balance consistent with the fiscal consolidation path by accommodating additional requests within the approved budget ceilings: **Reallocation possibilities, except those of the security and education sectors**.
- All MDAs expected to settle any carryovers as a first charge against the budgetary allocations for the FY 2023/24.

3.3: Supplementary Budget 1 for FY 2023/24: Revised Fiscal Framework for the FY 2023/24 Budget, therefore, has

- **Total revenues** projected at **Ksh 3,047.6 billion** (18.9% GDP) with:
  - Ordinary revenues projected at Ksh 2,576.8 billion (16.0% of GDP).
  - Ministerial A-I-A projected at Ksh 470.8 billion (2.9% of GDP)
- **Total expenditures** projected at **Ksh 3,981.8 billion** (24.7% of GDP) of which:
  - Recurrent Ksh 2,793.9 billion (17.3% of GDP)
  - Development of Ksh 762.6 billion (4.7% of GDP)
  - **Transfers to County Governments** projected at Ksh 423.9 billion (2.6% of GDP).
- **The budget deficit including grants** projected at Ksh 886.6 billion (**5.5% of GDP) from the Budget Estimates of Ksh 718.9 billion (4.4% of GDP)**

4.1: Bottom-Up Economic Transformation Agenda (BETA)

- The Government begun the journey of reducing the cost of living and improving livelihoods, while at the same time fostering a sustainable inclusive economic transformation through the implementation of the **Bottom-Up Economic Transformation Agenda**. This was meant to reverse the economic recession.
- The development agenda recognizes the importance of managing the cost of living through well-functioning markets to enhance productivity, availability and affordability of goods and services for all citizens
- The interventions target five core priority areas namely:
  - Agricultural Transformation and Inclusive Growth;
  - Support to Micro, Small and Medium Enterprise (MSMEs);
  - Focus on affordable Housing and Settlement for job creation given the linkage along the value chain;
  - Provision of Universal Healthcare; and
  - Focus on Digital Superhighway and Creative Industry to support e-commerce.

4.2: The Bottom-Up Economic Transformation Agenda (BETA)

- Key enablers for BETA: (i) Infrastructure; (ii) Manufacturing; (iii) Blue Economy; (iv) Services Economy, (v) Environment and Climate Change; (vi) Education and Training; (vii) Women Agenda; (viii) Social Protection; (ix) Sports, Culture and Arts; (x) Youth Empowerment and Development Agenda; (xi) Governance; and (xii) Foreign Policy and Regional Integration.

- The National Government is collaborating with County Governments to create an enabling environment that attracts investments in the BETA programmes.

- Special focus of the Agenda is placed on increased employment, more equitable distribution of income, social security while also expanding the tax revenue base, and increased foreign exchange earnings.

- Implementation of BETA will be through **9 targeted value chains** as follows: (i) Leather; (ii) Cotton; (iii) Dairy; (iv) Edible Oils; (v) Tea; (vi) Rice; (vii) Blue Economy; (viii) Natural Resources Including Minerals & Forestry); and (ix) Building Materials.

5.1: Medium Term Sector Ceilings, FY 2024/25 – FY 2026/27 Budget and the Criteria for Resource Allocation

- Consistent with the fiscal stance, the **hard budget ceiling** for the FY 2024/25 budget is **Ksh 2,547.8 billion** which comprise of **Ksh 1,644.3 billion** in **recurrent expenditures** and **Ksh 903.5 billion in development expenditures**.
- All the spending units have been urged to critically review, evaluate and prioritize budget allocations to the **BETA** priorities by increasing investments in:
  - Agricultural Transformation and Inclusive Growth;
  - Micro, Small and Medium Enterprise (MSME);
  - Housing and Settlement;
  - Healthcare; and
  - Digital Superhighway and Creative Industry.
- Further, the MDAs have been encouraged to adopt efficiency in allocation of resources through cost budgeting and reviewing the portfolio of externally funded projects.

5.2: Medium Term Sector Ceilings, FY 2024/25 – FY 2026/27

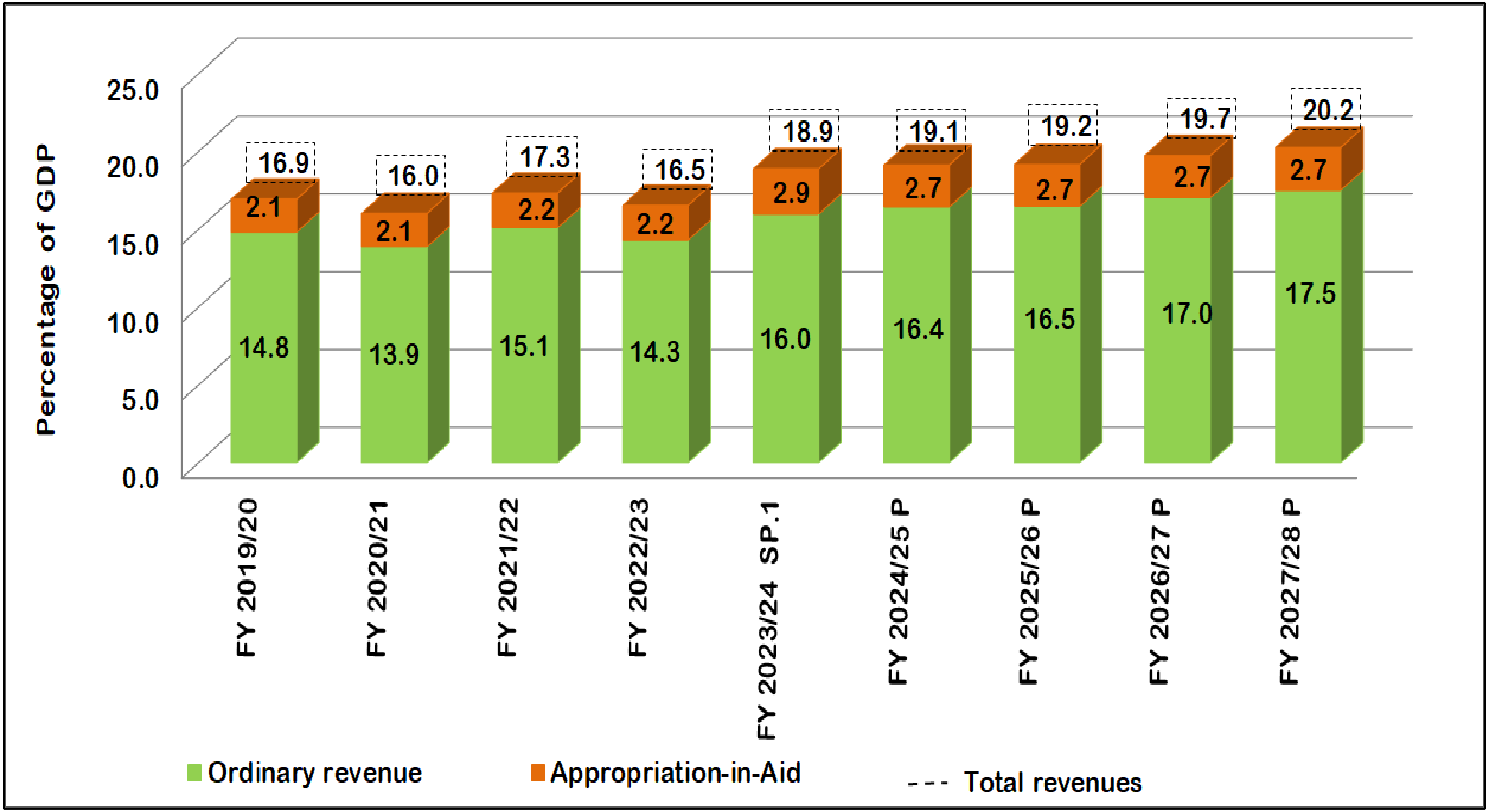
- Education sector will receive the highest share of the total ministerial expenditure in FY 2024/25 at 26.3%, followed by Energy, infrastructure and ICT sector at 21.2%.

Sector	Allcations in Ksh Billion			%Share In Total Ministerial Expenditure		
	2024/25	2025/26	2026/27	2024/25	2025/26	2026/27
AGRICULTURE, RURAL & URBAN DEVELOPMENT (ARUD)	85.8	93.6	97.4	3.37	3.41	3.25
ENERGY, INFRASTRUCTURE AND ICT	541.1	567.1	580.1	21.24	20.66	19.36
GENERAL ECONOMIC AND COMMERCIAL AFFAIRS (GECA)	57.3	62.5	54.7	2.25	2.28	1.82
HEALTH	143.1	151.4	156.7	5.62	5.52	5.23
EDUCATION	670.0	730.2	790.0	26.30	26.61	26.37
GOVERNANCE, JUSTICE, LAW AND ORDER (GJLO)	250.2	271.8	306.7	9.82	9.90	10.24
PUBLIC ADMINISTRATION AND INTERNATIONAL RELATIONS (PAIR)	332.9	404.1	533.3	13.07	14.73	17.80
NATIONAL SECURITY	253.6	237.6	244.3	9.96	8.66	8.15
SOCIAL PROTECTION, CULTURE AND RECREATION	72.6	73.9	75.8	2.85	2.69	2.53
ENVIRONMENT PROTECTION, WATER AND NATURAL RESOURCES	141.1	152.2	156.7	5.54	5.54	5.23
GRAND TOTAL	**2,547.8**	**2,744.5**	**2,995.7**	**100.0**	**100.0**	**100.0**

6.1. Fiscal Policy for FY 2024/25 and Medium-Term Budget

- **The fiscal policy stance**: Supports the Bottom-Up Economic Transformation Agenda (BETA) through a growth **friendly fiscal consolidation plan**.
- Emphasis will be placed on aggressive revenue mobilization through a combination of tax administrative and tax policy reforms that include:
  - Implementation of the Finance Act 2023 that targets to boost revenue collection (approx.1.5% of GDP). This will lead to a tax effort of 16.0% of GDP in FY 2023/24;
  - Implementation of the Medium-Term Revenue Strategy (MTRS) that will further strengthen tax revenue mobilization efforts to 20.2% of GDP over the medium term; Anchor Policy is the National Tax Policy that was approved by Parliament
  - Focus on non-tax measures that MDAs can raise through the services they offer to the public e.g. Ministry of Lands, Immigration and citizen services among others;
  - Strengthen Tax Administration -KRA: Scale up use of technology to seal leakages; enhancements of iTax and Integrated Customs Management System (iCMS); and use of e-TIMS (Tax Invoice Management System).

6.2: The proposed revenue mobilization measures target to increase revenues from the projected 18.9% of GDP in FY 2023/24 to 19.1% of GDP in FY 2024/25 and further to 20.2% of GDP by FY 2027/28.



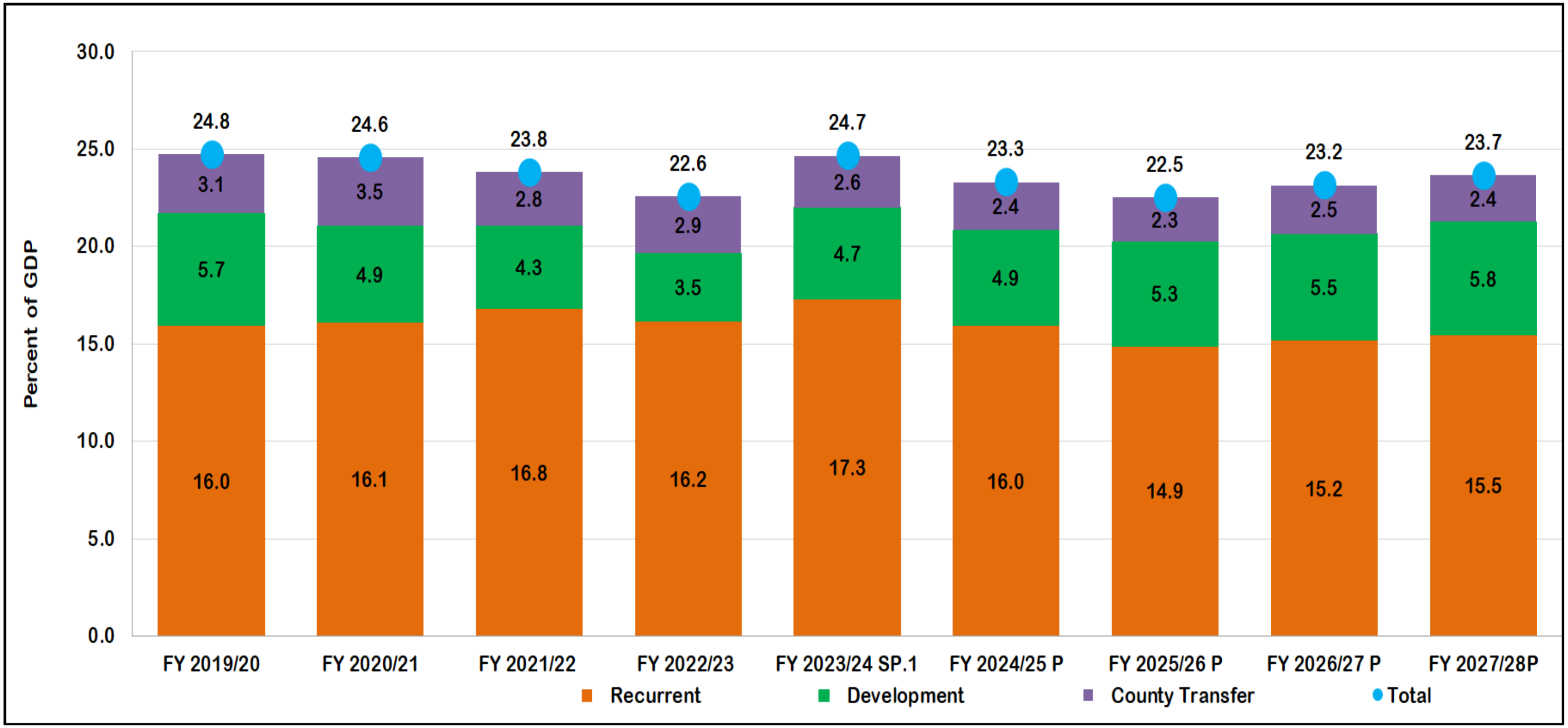
6.3. Fiscal Policy for FY 2024/25 and Medium Term Budget: Expenditures

Expenditure controls efforts include:

- Rationalize non-priority spending by seeking new savings in recurrent spending (covering arears such as travels, allowances, and hospitality);
- Rationalize non-priority capital projects through further rationalization of the portfolio of projects;
- Scale up the use of Public Private Partnerships financing for commercially viable projects; and roll out an end-to-end e-procurement system; and
- The clearance of pending bills and other government arrears remains a priority.

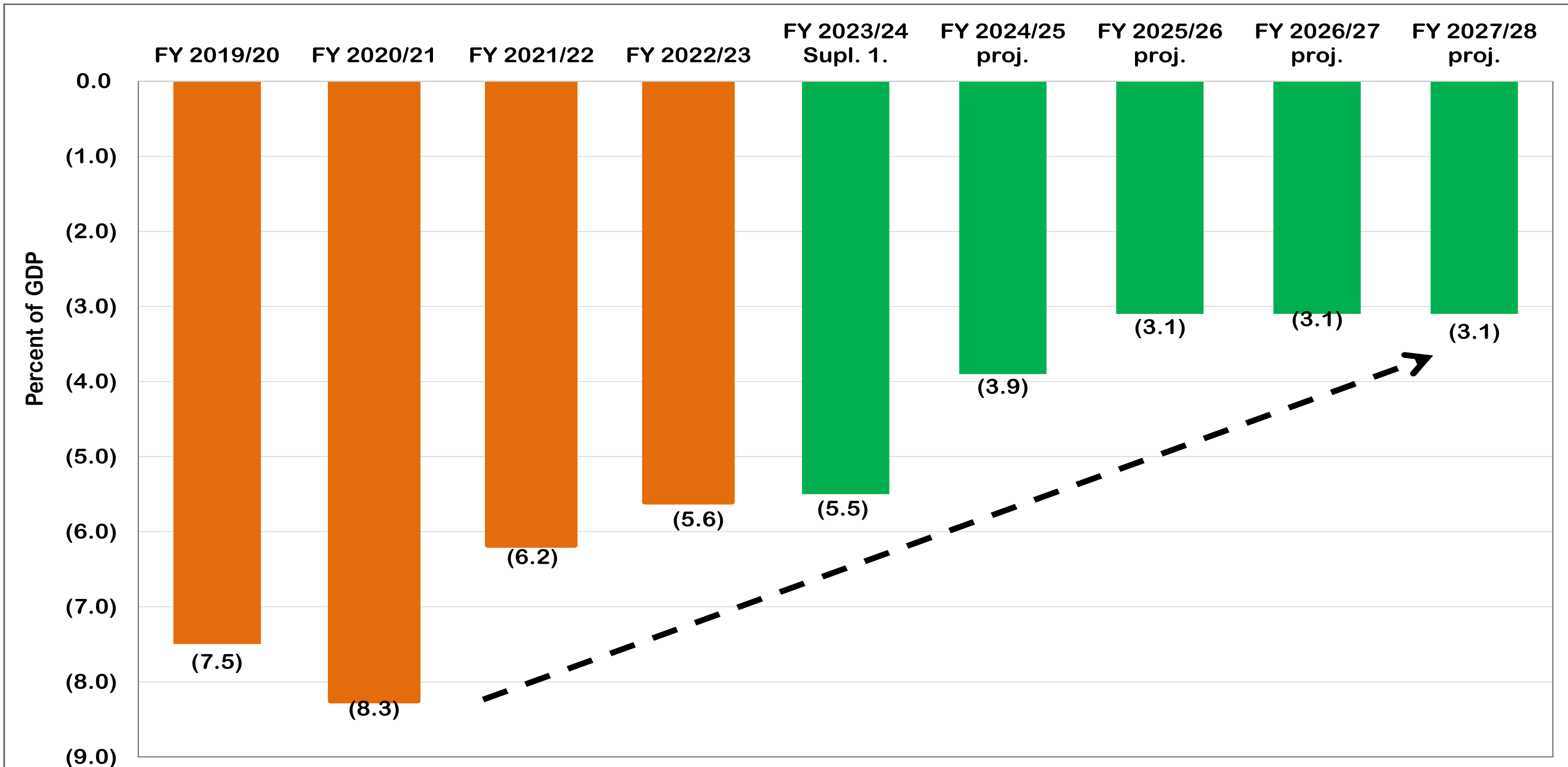
6.4: FY 2024/25 Budget: Reduction in total expenditures as a share of GDP from the estimated 24.4% in FY 2023/24 to 23.3% in FY 2024/25

- Reduction will be in recurrent spending: From 17.3% of GDP in FY 2023/24 to 16.0% in FY 2024/25 and further to 15.5% in FY 2027/28;
- Development spending will be retained at an average of 5.2% of GDP (from FY 2023/24 to FY 2027/28) so as not to impact on growth momentum



6.5: In line with the Fiscal Consolidation plan, the successful implementation of the revenue and expenditure measures would reduce the fiscal deficit and enhance primary surplus, thereby stabilizing public debt over the medium term

- Fiscal deficit including grants (as a share of GDP) is projected to reduce from 5.6% in FY 2022/23 to 3.9% in FY 2024/25 and 3.1% in FY 2027/28.



6.6: Economic Policy supported by the Kenya-IMF Program

- On 16th November 2023, IMF staff and the Kenyan Authorities reached staff-level agreement on:
  i. the sixth reviews of Kenya's economic program under the Extended Fund Facility (EFF) and Extended Credit Facility (ECF) arrangements;
  ii. an augmentation of access under the EFF/ECF totaling 130.3 percent of quota SDR 707.3 million, about US$938 million); and
  iii. the first review of the RSF.
- The agreement is subject to approval by Management and the Executive Board, which is expected in January 2024.
- Upon approval of 6th Review, Kenya would have immediate access to SDR 514.48 million (about US$682.3 million), including from the augmentation of access under the EFF/ECF arrangements (SDR469.25 million) and SDR45.23 million for the first review of RSF
  - This includes an augmentation of access under the EFF/ECF totaling 130.3 percent of quota SDR 707.3 million, about US$938 million)

7.1: Risks to the Macroeconomic Outlook

- **Domestic side**: Relate to unpredictable weather conditions due to the impact of climate change which could adversely affect agricultural production and result to domestic inflationary pressures.
  - **Tight Fiscal space:** Impact of the multiple shocks that have affected the global and the domestic economy leading to tight liquidity conditions for financing the budget.
- **On the external front:** Uncertainties in the global economic outlook stemming from the current geopolitical tension could result in higher commodity prices and slowdown the global economic recovery which could impact on the domestic economy.
  - Continued strengthening of US dollar against other global currencies arising from aggressive monetary policy tightening present significant risks to financial flows and puts pressures on the exchange rate with implication to growth and inflation.
- **Upside risks are mostly linked** to early easing of global financing conditions and lower international fuel and food prices, which would strengthen Kenya’s external balances. Faster than projected rebound in economic activities would result in higher Government revenues supporting fiscal consolidation.

THANK YOU