



KENYA

April 2021

REQUESTS FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY AND AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—PRESS RELEASE; STAFF REPORT; AND STATEMENT BY THE EXECUTIVE DIRECTOR FOR KENYA

In the context of the Requests for an Extended Arrangement Under the Extended Fund Facility and an Arrangement Under the Extended Credit Facility, the following documents have been released and are included in this package:

- A **Press Release** including a statement by the Acting Chair of the Executive Board.
- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on April 2, 2021, following discussions that ended on February 12, 2021, with the officials of the Kenya on economic developments and policies underpinning the IMF arrangements under the Requests for an Extended Arrangement Under the Extended Fund Facility and an Arrangement Under the Extended Credit Facility. Based on information available at the time of these discussions, the Staff Report was completed on March 19, 2021.
- A **Debt Sustainability Analysis** prepared by the Staffs of the IMF and the International Development Association (IDA).
- A **Statement by the Executive Director** for Kenya.

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IMF Executive Board Approves US\$2.34 Billion ECF and EFF Arrangements for Kenya

FOR IMMEDIATE RELEASE

- IMF Board approves SDR 1.655 billion (about US\$2.34 billion) ECF and EFF arrangements for Kenya.
- The three-year financing package will support the next phase of the authorities' COVID-19 response and their plan to reduce debt vulnerabilities while safeguarding resources to protect vulnerable groups.
- The Fund-supported program will also advance the broader reform and governance agenda, including by addressing weaknesses in some state-owned enterprises (SOEs) and strengthening transparency and accountability through the anticorruption framework.

Washington, DC – April 2, 2021: On April 2, 2021, the Executive Board of the International Monetary Fund (IMF) approved 38-month arrangements under the [Extended Credit Facility](#) (ECF) and the [Extended Fund Facility](#) (EFF) for Kenya in an amount equivalent to SDR 1.655 billion (305 percent of quota or about US\$2.34 billion) to support the next phase of the authorities' COVID-19 response and address the urgent need to reduce debt vulnerabilities.

Approval of the ECF/EFF enables immediate disbursement of about US\$307.5 million, usable for budget support. This follows Fund emergency support to Kenya in May 2020 (100 percent of quota, equivalent to US\$739 million at the time of approval, see Press Release [No. 20/208](#)).

Kenya was hit hard at the onset by the COVID-19 pandemic. With a forceful policy response, the economy has been picking up heading into 2021 after likely posting a slight contraction of 0.1 percent in 2020. Even with this recovery, challenges remain in the return to durable and inclusive growth, and past gains in poverty reduction have been reversed.

The COVID-19 shock also exacerbated the country's pre-existing fiscal vulnerabilities. Kenya's debt remains sustainable, but it is at high risk of debt distress. To address debt-related risks, the authorities have taken action to hold the fiscal deficit and debt ratios to 8.7 and 70.4 percent of GDP, respectively, this fiscal year. Fiscal and balance-of-payments financing needs remain sizable over the medium term. Support from the G-20 under the Debt Service Suspension Initiative (DSSI) and development partners will contribute to closing the financing gap in 2021 along with financing from capital markets.

The authorities' program would set a basis for a resurgence of growth and shared prosperity. Building on critical steps already taken, it aims to reduce debt vulnerabilities through a multi-year fiscal consolidation effort centered on raising tax revenues and tightly controlling spending, safeguarding resources to protect vulnerable groups. It will also advance the structural reform and governance agenda, including by addressing weaknesses in some state-owned enterprises (SOEs) and strengthening transparency and accountability through the anticorruption framework.

Finally, it will strengthen the monetary policy framework and support financial stability. Against the backdrop of extraordinary uncertainty, the program incorporates flexibility, including by recognizing near-term challenges related to tax yields in the current stressed economic environment and possible contingent liabilities from the SOE sector.

At the conclusion of the Executive Board's discussion, Ms. Antoinette Sayeh, Deputy Managing Director and Acting Chair, stated:

"The authorities' program charts a clear path to reduce debt-related risks. It will bring the primary balance below its debt-stabilizing level during the EFF/ECF arrangements and restore tax revenue—which had been falling even before the COVID-19 shock—back to levels achieved in recent years. The authorities should continue to provide necessary support to the economy and secure space for social and development spending even as they have appropriately reversed some extraordinary measures, including the temporary tax cuts which ended in January, 2021.

"The near-term reform agenda should also focus on urgent structural policy challenges. As financial weaknesses in some state-owned enterprises (SOEs) have emerged as a key source of fiscal risks, the ability to manage these risks should be strengthened while ensuring that any support provided to SOEs is consistent with Kenya's limited fiscal space. Fiscal structural reforms should prioritize revenue administration, spending efficiency, and fiscal transparency. Continuing improvement in the anti-corruption framework through steps to enhance transparency and accountability and the AML/CFT agenda are also essential.

"The Central Bank of Kenya's (CBK) proactive policy stance has provided essential support during a very challenging period. Monetary policy should remain accommodative in the context of the inflation targeting regime, the exchange rate should continue to function as a shock absorber, and close supervision of credit risks and provisioning should be maintained.

"The program supported by EFF/ECF arrangements with the Fund provides a strong signal of support and confidence. It is also subject to notable risks, including from uncertainty about the path of the pandemic, and steadfast pursuit of the program objectives will be essential also considering the upcoming political calendar. The Kenyan authorities have demonstrated strong commitment to fiscal reforms during this unprecedented global shock, and Kenya's medium-term prospects remain positive".

Kenya: Selected Economic Indicators, 2020–23

	2020	2021	2022	2023
	Est.	Proj.	Proj.	Proj.
Output				
Real GDP growth (%)	-0.1	7.6	5.7	6.1
Prices				
Inflation - average (%)	5.3	5.0	5.0	5.0
Central government finances (fiscal year)¹				
Revenue (% GDP)	17.2	17.0	16.8	17.6
Expenditure (% GDP)	25.0	25.7	24.3	23.5
Fiscal balance (% GDP)	-7.8	-8.7	-7.5	-5.8
Public debt (% GDP)	65.8	70.4	72.6	72.9
Money and Credit				
Broad money (% change)	10.6	11.8	10.6	11.4
Credit to private sector (% change)	7.7	7.7	7.8	10.1
Policy rate, end of period (%)	7.0	...	...	...
Balance of payments				
Current account (% GDP)	-4.8	-5.3	-5.4	-5.5
Reserves (in months of imports)	4.6	4.6	4.3	4.1
External debt (% GDP)	35.6	37.8	37.6	36.7
Exchange rate				
REER (% change)	-1.5	...	...	...

Source: Kenyan authorities and IMF staff estimates and projections.

¹ Based on fiscal year (i.e., 2020 represents 2019/20).



KENYA

REQUESTS FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY AND AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY

March 19, 2021

EXECUTIVE SUMMARY

Context. Kenya has been hit hard by the COVID-19 pandemic. Despite a forceful policy response by the authorities, the socio-economic impact has been significant. The shock has also exacerbated the country's pre-existing fiscal vulnerabilities, pushing Kenya into high risk of debt distress. While the economy is now recovering, fiscal and balance-of-payments financing needs remain sizable over the medium term.

Request for financing under the Extended Fund Facility (EFF) and the Extended Credit Facility (ECF). Financing through the Rapid Credit Facility (RCF) in May 2020 provided initial support for Kenya's response to COVID-19. The authorities are now requesting a 38-month extended arrangement and an ECF arrangement to support the next phase of their response. Total blended access is proposed at SDR 1.655 billion (305 percent of quota)—SDR 1,248 million (230 percent of quota) from the EFF arrangement and SDR 407 million (75 percent of quota) from the ECF arrangement—to help meet balance-of-payments and budget-support needs. The arrangements are expected to catalyze support from other official lenders and capital market financing.

Policy priorities. The authorities' program, which anchors the proposed EFF/ECF, aims to stabilize the economy and set a basis for a resurgence of growth and shared prosperity. Building on critical steps that have already been taken, it aims to reduce debt vulnerabilities through a multi-year fiscal consolidation effort centered on raising tax revenues and tightly controlling spending while safeguarding resources to protect vulnerable groups. It will also advance the structural reform and governance agenda, including by addressing weaknesses in state-owned enterprises (SOEs) and strengthening the anticorruption framework. Finally, it will strengthen the monetary policy framework and support financial stability.

Key risks. Risks to the program are sizable, stemming from uncertainties about the persistence of the COVID-19 shock. Accordingly, the program incorporates flexibility, including by recognizing near-term challenges for tax yields in the current stressed economic environment and contingent liabilities from the SOE sector. Potential pressures from a planned constitutional referendum and 2022 elections are also a risk factor.

Approved By:

**Annalisa
Fedelino (AFR)
and Martin
Kaufman (SPR)**

The mission team consisted of Mary Goodman (head), Tobias Rasmussen (Resident Representative in Nairobi, Kenya), Valerio Crispolti, Jehann Jack, Gabor Pula (all AFR), Lahcen Bounader (FAD), Majid Bazarbash (MCM), Sergio Rodríguez (SPR), Pasquale Di Benedetta, Jane Duasing, and Alice French (all LEG), James Maina and Kevin Tuitoek (Resident Representative office) with assistance from Francine Nyankiye, Amparo Gamboa González, and Fernando Morán Arce (all AFR) and Christine Odwogi (Resident Representative office). Executive Director Ita Mannathoko and Senior Advisor Ted Sitimawina (both OED) participated in the discussions. Discussions were held remotely from Washington, D.C. during October 28–November 17, 2020 and December 9–20, 2020, and January 11–22, 2021 and February 2–12, 2021. The team met with Cabinet Secretary for the National Treasury and Planning, Mr. Ukur Yatani; Governor of the Central Bank of Kenya (CBK), Dr. Patrick Njoroge; Head of the Public Service, Dr. Joseph Kinyua; the Principal Secretary for the National Treasury, Dr. Julius Muia; Deputy Governor of the CBK, Ms. Sheila M'Mbijjewe; and other senior government and CBK officials. Staff also had productive discussions with the parliamentary budget office and representatives of the private sector, civil society organizations, and development partners.

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CONTEXT

1. The Kenyan economy was performing well prior to the COVID-19 shock, though with some emerging challenges. Kenya achieved stable and healthy growth in the decade prior to the COVID-19 crisis and made progress in reducing poverty and inequality.¹ Removal of interest rate caps in November 2019 had opened the door to an increase in private credit growth to support private investment. A key challenge in recent years had been a steady decline in government revenues as a share of GDP alongside large infrastructure investments and growing reliance on non-concessional borrowing, which contributed to increase fiscal deficits and debt vulnerabilities.

2. The COVID-19 shock hit Kenya's economy hard and exacerbated existing vulnerabilities. Reduced economic activity and increased fiscal pressures pushed Kenya into high risk of debt distress.² Financial assistance through the RCF in May 2020 provided temporary support, but absent a sizeable and sustained multiyear fiscal adjustment effort, the debt ratio would continue to increase. The authorities have set out a medium-term plan to stabilize the economy and set a basis for a resurgence of growth and shared prosperity. The plan is laid out in the Post-COVID Economic Recovery Strategy launched in December 2020 and in the Budget Policy Statement presented to Parliament in February 2021. A busy electoral calendar awaits, including a likely referendum on constitutional amendments later in 2021 and a general election in August 2022, but economic planning has proceeded apace.³

3. Against this backdrop, the authorities are requesting 38-month arrangements under the EFF and the ECF. The arrangements aim to support the authorities' efforts to promote the nascent economic recovery and address the urgent need to reduce debt vulnerabilities in the next several fiscal years. Access is proposed at SDR 1.655 billion (305 percent of quota) to help meet Kenya's sizable balance-of-payments and budget-support needs, including by catalyzing support from other official lenders and capital market financing.

RECENT ECONOMIC DEVELOPMENTS

4. The global pandemic has delivered a large shock to Kenya. In the second quarter of 2020, real GDP growth contracted by 5.5 percent year-on-year, driven by declines in manufacturing, hospitality-related services, and education.⁴ Reported unemployment doubled to 10.4 percent.

¹ Republic of Kenya: Staff Report for the 2018 Article IV Consultation and Establishment of Performance Criteria for the Second Review Under the Stand-by Arrangement—[IMF 18/295](#).

² Republic of Kenya: Request for Disbursement under the Rapid Credit Facility—[IMF 20/156](#).

³ The proposed constitutional amendments are an outcome of the [Building Bridges Initiative](#), a cross-party endeavor to promote unity through wide-ranging legislative and institutional reforms, including a more broad-based and inclusive executive structure, enhanced judicial accountability, and increased devolution to local governments.

⁴ A methodological adjustment to account for school closures in line with best practice—tracking the steep decline in hours taught as well as teacher salaries paid—meant a very large contraction in education real output, later reversed with school reopening.

Agriculture remained strong, boosted by favorable weather conditions, partly offsetting the shock. Construction and some services sub-sectors also maintained positive growth.

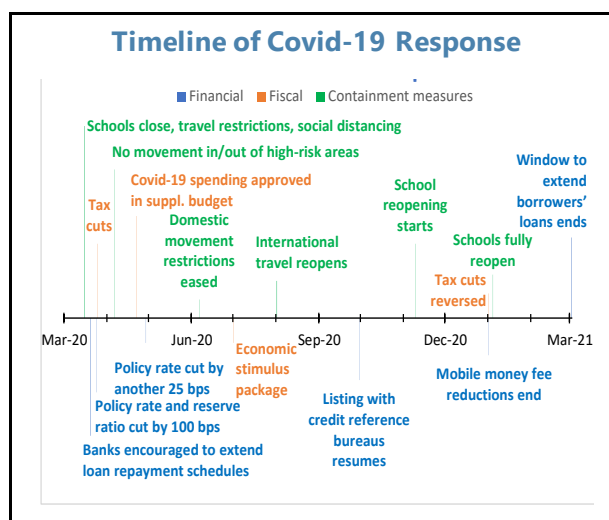
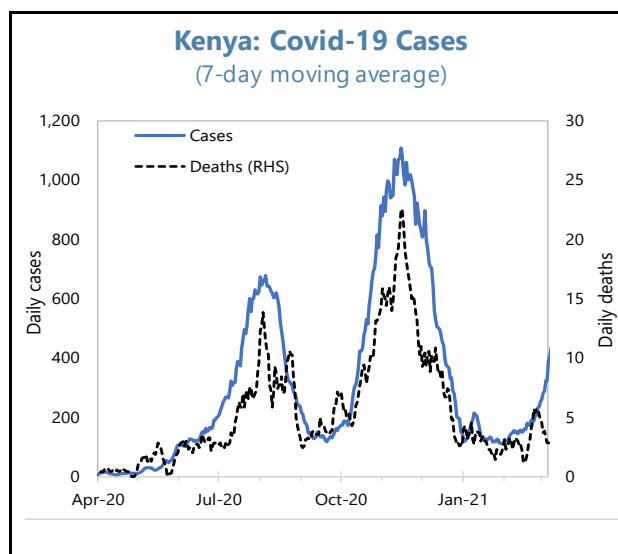
Box 1. COVID-19 and the Authorities' Response

First detected in Kenya in mid-March 2020, COVID-19 has spread in two waves, with peaks in late July and mid-November. The overall disease burden in Kenya has been limited, with about 2.1 confirmed cases per 1,000 population and a fatality rate of less than 2 percent as at mid-March 2021.

The authorities responded quickly and forcefully to the COVID-19 shock. Starting in March 2020, measures included establishment of isolation facilities, quarantine of at-risk persons, travel restrictions, bans on large gatherings, closure of schools and universities, imposition of social distancing and mask wearing requirements, and a country-wide nighttime curfew. Further measures, including domestic movement restrictions were added in April 2020. The capacity of the health system to detect and treat cases was scaled up in parallel. By end-September 2020 the number of isolation beds for infectious diseases reached 7,411, up from a total of 8 at the start of March.

Economic measures included:

- **Financial support.** In March 2020, the CBK cut the policy rate and the cash reserve ratio by 100 bps each; tripled the tenor on liquidity-injecting reverse repo instruments; and encouraged banks to extend repayment terms on previously performing loans. Further use of mobile money was also encouraged, leveraging Kenya's advanced position in this area (Box 2). In April 2020, the policy rate was cut another 25 bps to 7 percent, and the listing of negative credit information with credit reference bureaus was suspended for six months for borrowers whose loans had previously been performing.
- **Earmarked government spending.** The supplementary budget for FY2019/20 provided additional resources (0.4 percent of GDP) to key areas, including health, cash transfers to vulnerable groups, and liquidity support via accelerated payment of VAT refunds and pending bills. This was followed by a stimulus package (0.5 percent of GDP) in the FY20/21 budget that provided additional funding in these areas, support to hard-hit sectors, and a jobs program for youth.
- **Temporary tax cuts.** Starting April 2020, the standard VAT rate was reduced from 16 to 14 percent; the personal income tax top rate and the standard corporate income tax rate were reduced from 30 to 25 percent; and the turnover tax on small businesses was reduced from 3 to 1 percent.



Box 1. COVID-19 and the Authorities' Response (concluded)

- *Credit guarantee scheme for small businesses.* The government launched a credit guarantee scheme for SMEs in December 2020 with initial seed capital of Ksh 10 billion and is working with development partners to expand it.

Measures were gradually lifted as the pandemic subsided. In successive steps since early July 2020, the nighttime curfew was shortened, local and international flights resumed, and limits on attendance at public gatherings were relaxed. Schools and universities started to reopen in October and reopened fully in January 2021. The bulk of the tax cuts were reversed starting January 1. Remaining containment measures include a 10pm to 4am curfew, restrictions on operating practices of bars and restaurants, and caps on attendance at various types of gatherings.

5. The economy has staged a recovery. The decline in GDP growth moderated to -1.1 percent year-on-year in the third quarter, as retail and wholesale trade and transportation services rebounded, complementing activity in construction and agriculture (Figure 1). High frequency indicators point to a continuing recovery at the end of last year and moving into this year. Overall, the economy likely posted a slight contraction of -0.1 percent in 2020. With core inflation stable at under 3 percent, headline inflation remained close to the mid-point of the central bank's target range despite increasing fuel prices.

6. The current account proved resilient against the backdrop of the shock. Strong remittances, solid horticultural exports and lower imports narrowed the current account deficit to 4.8 percent of GDP in 2020. Heightened capital market volatility led to reduced capital inflows and a decline in FDI. The shilling acted as a shock absorber during the shock, with an 8 percent depreciation against the US dollar overall in 2020. Reserves declined to \$8.0 billion by end-January 2021 (from \$9.1 billion at end-2019), and coverage remains adequate at 4.4 months of prospective imports.

7. A Rapid Credit Facility (RCF) disbursement in May helped weather the initial COVID-19 impact. Faced with an immediate healthcare and economic shock and a broad interruption in frontier markets' access to international capital markets, Kenya relied on the RCF (Ksh 78.3 billion or \$739 million) and an augmented World Bank DPO (\$1 billion) to meet crisis-related financing needs in FY19/20. Domestic financing of government also increased.

Use of RCF Funds

	Ksh bn.	%
Total	78.3	100
Health	21.0	27
Social protection	17.3	22
Liquidity support (VAT refunds, pending bills)	21.9	28
Youth employment program	10.0	13
Education support, food relief, and other	8.2	10

Source: Kenyan National Treasury

Governance Spending Response to COVID-19¹

	2019/20		2020/21	
	Ksh bn	% of GDP	Ksh bn	% of GDP
Total	40.1	0.39	58.0	0.52
Youth Programs			10.0	0.09
Education ²			6.5	0.06
Health	4.9	0.05	1.7	0.02
Environment			3.8	0.03
Infrastructure			5.4	0.05
Agriculture			5.0	0.04
Tourism ³			6.0	0.05
Liquidity Support ⁴	23.1	0.23	14.3	0.13
Social Protection	10.0	0.10	1.0	0.01
Food Relief and Others	2.1	0.02	4.3	0.04

Sources: Kenyan authorities and IMF staff calculations.

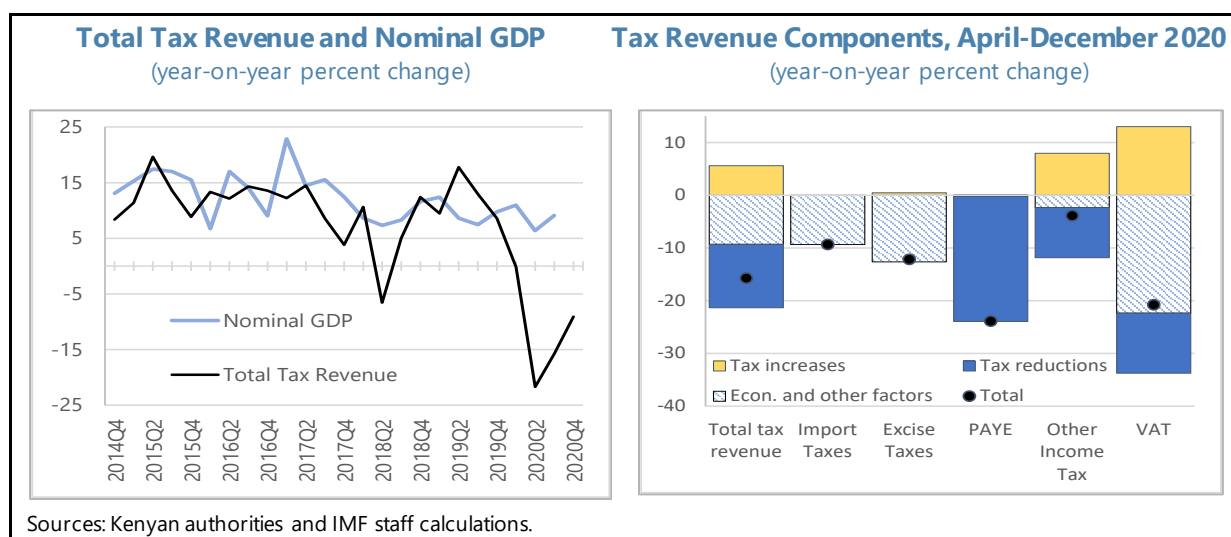
¹ For 2019/20 additional spending in suppl. budget of April 2020 (excl. reorientation of spending within existing budget lines), and for 2020/21 the economic stimulus package.

² Infrastructure, teachers support.

³ Facility renovation, marketing, conservancy support.

⁴ Clearance of pending bills, VAT refunds, credit guarantee scheme.

8. While the COVID-19 shock interrupted planned fiscal consolidation, the authorities have limited the fallout on the fiscal accounts. The emergency tax package that took effect in April 2020 included meaningful measures to broaden the tax base by eliminating costly VAT exemptions and corporate income tax preferences. Nevertheless, revenue fell sharply as reduced economic activity and disruptions to tax administration took a heavy toll. On the spending side, the 0.4 percent of GDP in additional COVID-19-related temporary expenditures in FY19/20 were offset with restraint of about 0.6 percentage of GDP in other areas (MEFP, ¶11). As a result, the FY19/20 fiscal deficit was contained at 7.8 percent of GDP, a level similar to that of the previous year (7.7 percent of GDP in FY18/19).⁵ Public debt rose to about 66 percent of GDP in FY19/20 (from 62 percent in FY18/19).



9. Pressures on borrowers' balance sheets have risen but financial sector vulnerabilities remain contained. The banking sector was well-capitalized, liquid, and profitable at the beginning of 2020, but the shock exacerbated preexisting asset quality weaknesses. Performance on regulatory ratios has remained strong to date, with a capital adequacy ratio of 19.2 percent and liquidity ratio of 55 percent at end-2020, well above the statutory requirements. Banks' NPL ratio rose from 12.7 percent in February to 14.1 percent in December 2020. The CBK has indicated that at end-year about 54 percent of system loans had been restructured to support performing borrowers impacted by the pandemic. While most of these arrangements have already come to an end, some borrowers may struggle to remain current. With larger banks, in particular, increasing forward-looking provisioning in line with IFRS9 guidelines, bank profits declined notably in 2020, with return on equity falling to 14 percent in December from 20 percent earlier in the year.

10. The external position of Kenya in 2020 was broadly in line with the level implied by fundamentals and desirable policies (Annex II). Fiscal consolidation under the EFF/ECF arrangements would help strengthen Kenya's external position and over time support private sector

⁵ The FY19/20 budget originally targeted a deficit of the overall fiscal balance of 5.6 percent of GDP.

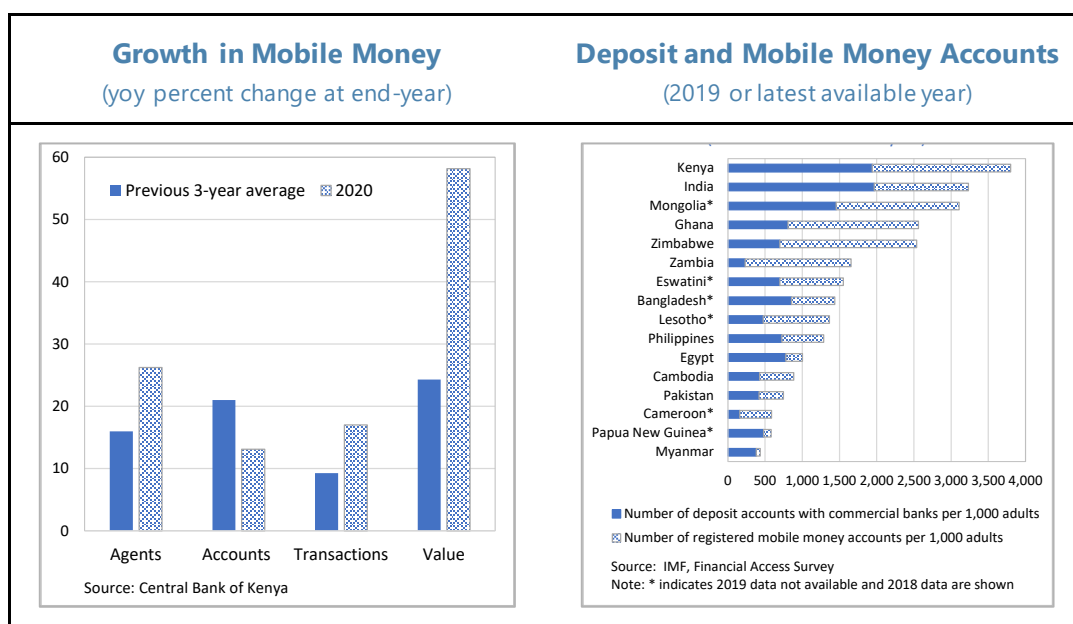
growth. An improvement in Kenya's competitiveness would be necessary to curtail the prolonged decline of Kenya's share of world exports.

Box 2. Mobile Money During the Pandemic

Kenya instituted a range of measures to promote mobile money usage to reduce the physical contact associated with using cash and the risk of spreading COVID-19. Encouraged by the CBK and in coordination with commercial banks, mobile money providers waived charges for small transactions for transfers between mobile money wallets and bank accounts, and for balance inquiries on linked bank accounts. Additionally, the CBK approved increases in the maximum value of any one transaction, of total daily transactions, and of the amount that could be held in mobile wallets. The measures were all put in place in March and extended to end-December 2020.

The measures helped reduce physical exchange of cash while also expanding access to finance.

Mobile money usage had fallen in the first weeks of the pandemic as the country went into lockdown but then grew strongly. Transaction volume and value, which had fallen by 20 and 14 percent year-on-year in April 2020, surged to 17 and 58 percent growth, respectively, by December 2020. The number of mobile money accounts, already among the highest across low and middle-income countries, rose to 2,058 per 1,000 adults at end-2020.



Mobile money also played an important role in social protection initiatives. Cash transfer schemes instituted by government and a range of development partners were ramped up during the pandemic to reach some 1.8 million households in 2020 from 1.2 million in 2019, with each typically receiving for a limited period transfers amounting to about \$10 per week directly to their mobile money accounts.

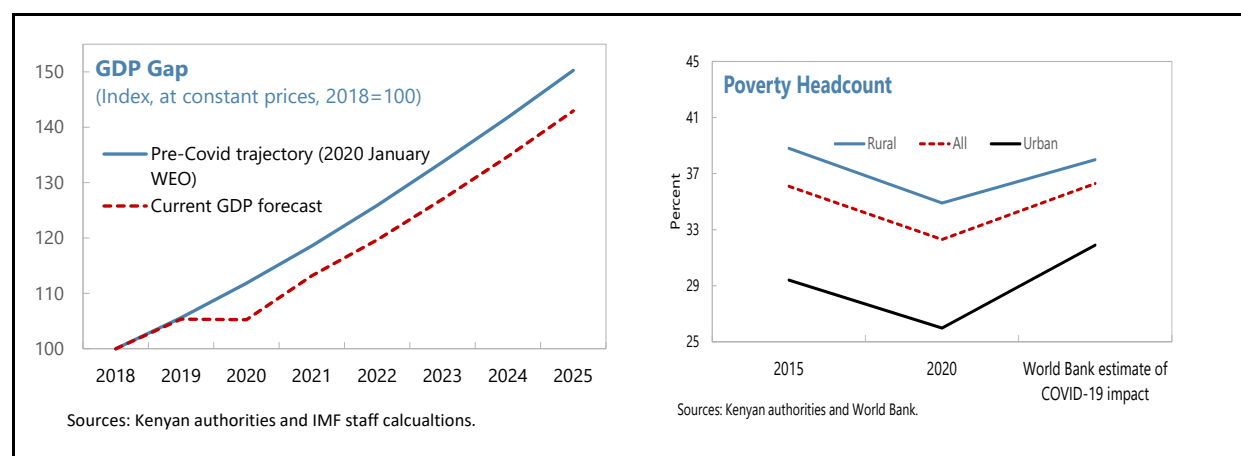
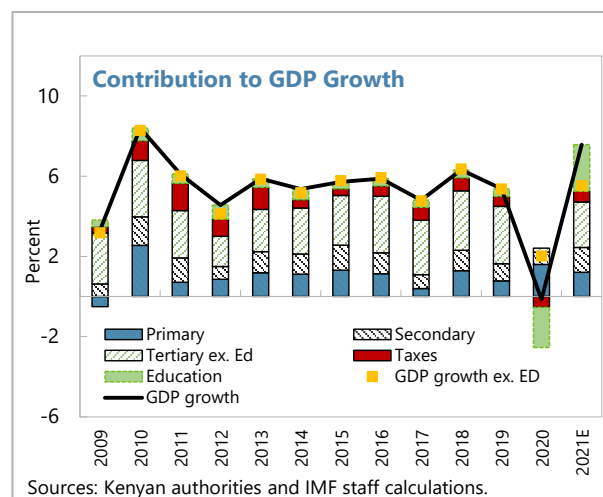
OUTLOOK AND RISKS

11. The economy is expected to rebound in 2021, though the outlook is subject to high uncertainty. In 2021, growth is expected to reach 7.6 percent driven partly by base effects and despite continued weakness in tourism and a slowdown in agriculture after 2020's exceptionally

good harvest. Despite rising global oil prices, inflation is expected to remain contained by the generally moderate recovery in domestic demand. The current account deficit is projected to widen modestly, in line with recovering oil prices and increased capital imports.

12. Kenya's medium-term outlook is positive, but the pandemic's socio-economic impact will take time to reverse.

The COVID-19 shock erased the poverty reduction gains of the last 5 years, as initial estimates by the World Bank suggest that the pandemic increased the poverty rate to 36 percent, raising the number of poor by 2 million. The planned fiscal consolidation and accompanying structural reforms would protect fiscal space for the authorities' development agenda while also supporting private credit and investment, leading to higher and more inclusive medium-term growth. With the fading of the COVID-19 shock, the economy is expected to settle at its potential growth rate (roughly 6 percent) over the medium term. Exports of goods and services are projected to reach 13.3 percent of GDP in 2025, broadly the same share as observed in 2018.⁶



13. Risks to the outlook remain tilted to the downside (Annex I). A more protracted pandemic at the global or regional levels could trigger a sharp rise in the global risk premia, which would undermine Kenya's nascent economic recovery and increase debt vulnerabilities. Main domestic risks include lower agricultural output due to adverse weather conditions or worsening locust invasions; an uptick of political tensions and violence around the upcoming constitutional referendum and general elections; possible further sizable SOE losses and materialization of contingent liabilities of SOEs not offset by compensatory measures, which could weigh heavily on public debt; deterioration in Kenya's security situation; and challenges in implementing the

⁶ See External Sector Assessment (Annex II) for a discussion on export performance and longer-term competitiveness challenges.

economic policy agenda, including the revenue mobilization and expenditure rationalization initiatives. Upside risks include a faster-than-projected rebound in economic activity and government revenue resulting from accelerated vaccine deployment or otherwise. Lower oil prices would improve Kenya's terms of trade.

14. The authorities viewed the growth outlook somewhat more positively than staff. They expected growth in 2020 to be about 0.6–0.8 percent, supported by the agricultural and construction sectors and a strong rebound in trade and transportation. They pointed to the high level of uncertainty and difficulties in capturing recent developments in economic statistics as traditionally compiled, noting that reported downturns in manufacturing and employment may have been overstated. They also envisaged that full implementation of their reform agenda would lead to growth of at least 6½ percent over the medium term.

Box 3. COVID-19 Vaccine Deployment in Kenya

Kenya began vaccinating against COVID-19 in early March. This was done using vaccines obtained via the COVAX initiative, which over time is expected to provide vaccines sufficient to cover 20 percent of the population. Beyond that, Kenya plans to procure vaccines for another 10 percent of the population. The government's plan would roll out vaccines in three phases stretching into mid-2023 to progressively cover the most vulnerable groups, subject to global vaccine availability. In the near term, with most vaccines expected to be provided for free by COVAX and with the World Bank expected to support vaccine delivery with a \$50 million loan, costs of vaccine deployment would largely be covered at least through the current fiscal year. Costs could increase over time, however, especially if the vaccination program is scaled up.

Phase I (Q3 & Q4, FY 2020/2021)	<ul style="list-style-type: none"> • Vaccine supply limited • Focus: Rapidly reaching critical target populations • Priority Group: Front line Health Care Workers (HCWs- Including CHWs) Critical/ Essential Workers • Target Population: 1.25 Million
Phase II (FY 2021/2022)	<ul style="list-style-type: none"> • Larger number of vaccine doses available • Focus: Rapidly reaching target populations most vulnerable to severe disease and death • Priority Group: Persons >50 years and those >18 years with co-morbidities • Target population: 9.76 Million
Phase III (FY 2022/2023)	<ul style="list-style-type: none"> • Sufficient supply of vaccine doses • Focus: Ensuring equitable vaccination of other vulnerable groups • Priority Groups: Persons > 18 years in congregate settings, Hospitality and tourism industry • Target Population: 9.8 Million

Source: Kenyan Ministry of Health, National COVID-19 Vaccines Deployment and Vaccination Plan, 2021.

PROGRAM POLICIES

The authorities' reform agenda will address the immediate needs of the COVID shock while reducing vulnerabilities and supporting durable and inclusive medium-term growth. The authorities' Letter of Intent and Memorandum of Economic and Financial Policies (MEFP) set objectives to: (1) support their COVID-19 response, while reducing debt vulnerabilities via multi-year fiscal consolidation centered on raising tax revenues; (2) advance the broader structural reform and governance agenda, including by addressing weaknesses in SOEs and continuing to strengthen the anti-corruption framework; and (3) strengthen the monetary policy framework and support financial stability.

A. Supporting the Authorities' COVID Response While Reducing Medium-Term Debt Vulnerabilities

15. The program will support the response to the COVID-19 shock. The authorities have appropriately prioritized policy action to cushion the impact of the pandemic and have increased support for impacted groups (MEFP, ¶12 and ¶14). The program will protect health and social expenditures, while gradually unwinding emergency expenditures in other non-priority areas. This is supported by an indicative target for priority social spending (TMU, ¶27) for transfers to vulnerable groups (e.g., children, people with disabilities, the elderly), free primary and secondary education, food programs, health coverage and insurance, and vaccination and immunization programs.

16. The overarching objective of the fiscal strategy is to first stabilize and then reduce the public debt burden, as set out in the 2021 Budget Policy Statement. This will be achieved

through a multi-year consolidation effort that brings the primary deficit below its debt-stabilizing level by FY23/24 and keeps the debt-to-GDP ratio on a firmly declining trend thereafter (DSA, Table 2). A key pillar of the strategy is to bring the tax-to-GDP ratio back to levels achieved in recent years (from 12.9 percent of GDP in FY20/21 to 15.6 percent in FY23/24), so as to generate resources to meet Kenya's development needs. This objective is supported by measures already taken as well as a commitment to undertake further tax policy measures of 0.8–0.9 percent of GDP per year in FY22/23

Tax Policy Changes (full-year impact) ¹		
	Ksh bn	% of GDP
Tax changes effective April 2020 (net)	-105.0	-1.0
Tax relief	-186.3	-1.8
CIT rate cut ²	-33.8	-0.3
PIT rate cut ²	-81.6	-0.8
PIT personal relief	-19.0	-0.2
VAT rate cut ²	-49.4	-0.5
Gross transaction value	-2.6	0.0
Revenue-raising measures	81.3	0.8
CIT changes	28.2	0.3
VAT exemption eliminations	51.1	0.5
Other	2.0	0.0
Measures effective July 2020	14.8	0.1
PIT exemption eliminations	0.3	0.0
Excise duty	1.5	0.0
VAT exemption eliminations	7.7	0.1
Fees and levies	5.4	0.0
Measures effective January 2021 (excl. tax reversals)	27.5	0.2
CIT (incl. new minimum and digital taxes)	27.5	0.2
Total before reversal of tax cuts	-62.7	-0.7
Total after reversal of tax cuts on Jan 1, 2021	102.0	1.0
Source: Kenyan authorities and IMF staff calculations.		
¹ Estimates based on pre-COVID tax base. Actual yields from reversal in near term likely smaller due to reduction of tax base following COVID-19.		
² Reversed on January 1, 2021.		

and FY23/24 (MEFP, ¶22–¶24) and ongoing efforts to strengthen revenue administration (MEFP, ¶27). These steps will be accompanied by action to reduce recurrent spending by 2.1 percentage points of GDP (from 20.0 percent of GDP in FY20/21 to 17.9 percent in FY23/24), while protecting social priority expenditures (including for COVID-19 vaccines) and development spending.

17. The program builds on crucial measures already taken by the authorities to contain fiscal and debt vulnerabilities (MEFP, ¶22).

- On the revenue side, in addition to the base broadening measures enacted in April and June 2020—in line with past IMF advice—the authorities repealed the bulk of the emergency tax cuts introduced in April 2020 with effect from January 1, 2021.⁷ These, along with other tax measures effective on January 1 would in normal times have been expected to yield additional revenue of 2.0 percent of GDP. Given the currently elevated uncertainty, however, staff conservatively estimates the yield of these measures at 1.26 percent of GDP on a full-year basis (text table). The authorities have also intensified their efforts to expedite judicial procedures to collect outstanding tax debts and anticipate payment of dividends from public sector entities (expected yield about 0.3 percentage points of GDP).
- On the expenditure side, in February 2021 the government submitted to Parliament a FY20/21 supplementary budget consistent with program objectives (*prior action*). It limits recurrent spending (particularly for transfers and entitlements) and better prioritizes domestically-financed projects, while providing some limited support to SOEs hit by the shock.

Revenue Measures Implemented on Jan. 1, 2021
(projected near-term yield in percent of GDP; full-year impact)

Total	1.26
Restore top PIT rate	0.52
Restore CIT standard rate to previous level	0.22
Restore VAT standard rate to previous level	0.32
Introduce minimum alternative tax at 1% of gross turnover	0.18
Introduce digital services tax at 1.5% of gross transaction value	0.02

Sources: Kenyan authorities, and IMF staff projections.

As a result, the fiscal deficit and debt ratios are expected to be contained to 8.7 and 70.4 percent of GDP, respectively, in FY20/21. This level of the fiscal deficit is appropriate, given pressures on revenue and spending. Greater fiscal adjustment would risk undermining the nascent recovery and worsening debt dynamics.

18. The fiscal targets for FY21/22 are ambitious and reflect a projected normalization in economic activity. The fiscal deficit is expected to decline by 1.2 percentage points of GDP with an improvement of 1.6 percentage points in the primary balance. Tax mobilization is expected to improve by 0.6 percent of GDP, driven largely by the full-year impact of the January 2021 tax measures.⁸ Expenditure outlays would decline by 1.4 percentage points of GDP reflecting the unwinding of COVID expenditures (0.5 percent of GDP) and further expenditure restraint (MEFP,

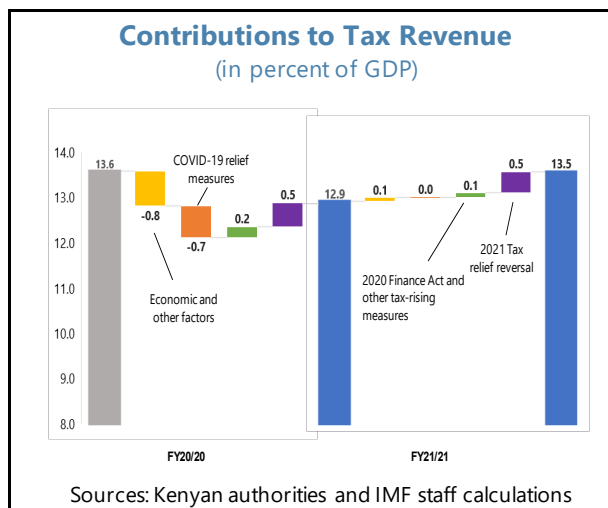
⁷ To maintain the cushion for the low-income earners, the authorities maintained the personal relief on income tax and the lower turnover tax (1 percent) on small businesses introduced in April 2020.

⁸ The full resumption of revenue administration activities is conservatively estimated to improve tax collection by 0.1 percentage points of GDP in FY21/22 from its currently depressed level.

¶23). The authorities will submit to Parliament their FY21/22 budget consistent with program targets by end-April 2021 (**structural benchmark**). Fiscal risks from SOEs are elevated, and the FY21/22 deficit may need to accommodate some SOE extraordinary budgetary support (MEFP, ¶137).

19. Fiscal consolidation measures beyond FY21/22 aim to protect high-priority service delivery and investment programs.

On the revenue side, the focus remains centered on broadening the tax net and reducing remaining tax exemptions (including in VAT). In this regard, past IMF technical assistance has identified a range of tax measures that the authorities could consider to significantly improve collection going forward. Durable progress in revenue mobilization also rests on continuous efforts to strengthen revenue administration in line with past Fund advice (MEFP, ¶127). On the expenditure side, efforts aim at restraining recurrent expenditure—particularly through a gradual reduction in the wage bill and transfers to public sector entities—and improving the efficiency and effectiveness of government spending consistent with recommendations in the recent Public Expenditure Review undertaken by the World Bank (MEFP, ¶128–¶130). To ensure prudent management of available public resources, the program envisages further strengthening public financial management (PFM) systems, particularly in the area of budget control and execution processes, cash management, and public investment management—including related to PPPs and associated fiscal risks (MEFP, ¶131–¶135).



20. The financing strategy under the program recognizes Kenya's external debt vulnerabilities.

The authorities have shifted their financing strategy to prioritize concessional financing, and with the recovery of market access in recent months the authorities plan commercial borrowing—in limited amounts to safeguard external debt sustainability. While Kenya is at high risk of debt distress and subject to zero limits on non-concessional borrowing, the authorities have requested, and staff supports, non-zero limit exceptions for project financing and debt management operations (MEFP, Table 1). In this context, commercial borrowing will be used (i) to finance projects that are critical for Kenya's development strategy and have high economic and social returns and for which concessional financing is not available;⁹ and (ii) to proceed with liability management operations. This approach is consistent with the Fund's Debt Limit Policy.¹⁰ During the first 18-months of the program, \$4.8 billion of government external borrowing will be concessional compared to \$2.3 billion in commercial borrowing (Eurobond issuance) for project financing (see

⁹ These projects are in many cases financed by bilateral or multilateral development partners, with the share of financing varying by project. The non-concessional funds will finance the Government of Kenya portion (local component) of these projects.

¹⁰ The relevant program debt limits will be updated via formal request to the Executive Board in subsequent reviews with the entry into force of the updated Debt Limit Policy Guidance Note.

Summary Table of Projected External Borrowing Program in DSA, ¶9). The borrowing plan under the program allows for another \$5 billion Eurobond issuance to be used exclusively for debt management operations, which could include a refinancing of the 2024 Eurobond and retiring of relatively expensive syndicated loans.¹¹ Given Kenya's financing needs, the domestic market is projected to be an important source of public financing, particularly during the early phase of the program.

21. The authorities emphasized reducing debt vulnerabilities as a key priority to support Kenya's developmental agenda. They stressed that recent measures to improve tax performance and broaden the tax base in the midst of the pandemic and Cabinet's approval of the FY20/21 supplemental budget are testament to their strong commitment to fiscal consolidation. They expressed interest in follow-up TA from the Fund to support their commitment to identifying tax policy measures to achieve the tax path under the program in FY22/23 and FY23/24. On debt management issues, the authorities emphasized their efforts to extend the maturity of domestic debt and the need to pursue a financing strategy that balances domestic and external financing, utilizes concessional financing where available, and accesses private capital markets judiciously.

B. Structural Reforms

22. The structural reform agenda during the first phase of the program will address urgent policy needs. In the near term, key priorities will be addressing challenges in SOEs and governance. Going forward, supporting employment creation and social inclusion via a vibrant and competitive business environment will move toward the center of the agenda.

Addressing SOEs' Financial Challenges

23. State-owned enterprises have emerged as an important source of fiscal risk. The profit of public entities outside the budgetary central government declined by a third in FY19/20, to Ksh 62.5 billion (0.6 percent of GDP), as many SOEs saw reduced profits and a handful showed large losses. While the deteriorating income position of the SOE sector reduces its contribution to the budget, additional fiscal pressures could arise from SOE debt on-lent or guaranteed by the government (DSA, ¶12).

24. For several SOEs, the COVID-19 shock exacerbated preexisting underlying financial weaknesses. For example, public universities have been registering persistent losses for an extended period. Kenya Power has over the last five years experienced declining financial performance driven by increasing costs, below-expectation demand growth, and tariff approval delays. Despite rising revenues, Kenya Railways saw a significant worsening in profitability in FY19/20 as it started to service on-lent loans contracted by the national government for construction of the Single Gauge Railway. Kenya Airways, which like other airlines was hard hit by the travel restrictions introduced in early 2020, had been accumulating losses since 2015.

¹¹ Market-based operations will be considered to improve the present value of external debt and debt service profile.

25. A staged approach is envisaged to evaluate the extent of fiscal risks from the SOE sector and begin addressing them. The key components are:

- A financial evaluation of the 9 SOEs with largest fiscal risks to the FY2020/21 budget will be completed by end-March 2021 (**prior action**). The evaluation will cover Kenya Airways, Kenya Airports Authority, Kenya Railways Corporation, Kenya Power, Kenya Electricity Generating Company, Kenya Ports Authority and the three largest public universities. This evaluation will serve as a basis for extraordinary SOE support to these SOEs in FY20/21, which should be limited to exigent needs (the supplementary budget provides for 0.3 percent of GDP).
- By end-May 2021, National Treasury will prepare an in-depth forward-looking financial evaluation of the top 15-20 SOEs representing the largest fiscal risks as well as a strategy for addressing financial pressures in the SOE sector, including a framework for deciding on interventions and reforms while taking into account the limited fiscal space and the program's fiscal targets (**structural benchmark**).

26. Reforms to improve the oversight, monitoring, and governance of SOEs will aim to enhance their resilience. Concrete measures (MEFP, ¶138) will include completing a draft blueprint that will identify necessary actions and legal reforms to enhance governance (by July 2021 supported by IMF TA); developing an integrated monitoring and reporting system (by September 2021); establishing a performance management monitoring and evaluation framework; and initiating a review of institutional structures.

27. Transparency of fiscal risk reporting will be improved. By end-September 2021, an expanded fiscal risk analysis that quantifies contingent liabilities from high-risk SOEs and PPPs will be included in the annual Budget Review and Outlook paper (**structural benchmark**). The authorities also committed to scale-up resources at the Treasury's Government Investment and Public Enterprises (GIPE) Department, while expressing interest in continued IMF technical assistance in the areas of fiscal risk analysis and legal reforms.

Governance

28. The authorities' governance reform agenda reflects priorities to enhance the anti-corruption framework. Key pillars of the agenda include the promotion of fiscal transparency via publishing procurement information including beneficial ownership data of companies awarded contracts; operationalizing the Access to Information Act; review of the current legal framework for asset declarations of senior public officials and conflict of interest rules; and, given that corruption is inextricably intertwined with the need to launder its proceeds, an effective implementation of AML/CFT measures.

Box 4. Audit of COVID-19 Spending and other Governance Reform Initiatives

Audit of Covid-19 related spending. Under the May RCF, the authorities committed to the post-crisis auditing of samples of crisis-related expenditures by their independent audit office and publication of the results. The Auditor General has made good progress towards a comprehensive audit of all COVID-related spending in FY2019/20, the results of which are expected to be published by end-May 2021 (**structural benchmark**). A forensic audit of spending going through the Kenya Medical Supplies Authority (KEMSA) and covering the 13 March—31 July period was presented to Parliament in September 2020.¹ It found numerous violations of the Procurement and the Public Finance Management Acts and inefficiencies in the procurement process. Parliament subsequently initiated investigations of the infringements identified by the audit.

Public procurement. The authorities have taken steps to implement the 2015 Public Procurement and Asset Disposal Act with the issuance of the 2020 Public Procurement and Asset Disposal Regulations, which provides a legal framework for implementation of electronic procurement by all public entities. The Public Procurement Information Portal (PPIP) was launched in July 2018.² Under Executive Order No.2 of 2018, public procuring entities are to publish comprehensive information on all awarded public tenders including beneficial ownership information. KEMSA has made available information on beneficial ownership of companies awarded contracts in the year to September 2020.³ However, the PPIP portal has yet to publish beneficial ownership information.

Anti-Corruption. The authorities have adopted a broad anti-corruption legal framework and enacted laws that are contributing to enhanced governance and transparency such as the Access to Information Law (2016), the Leadership and Integrity Act (2012), Ethics and Anti-Corruption Commission Act (2012), Public Officer and Ethics Act (2003), Anti-Corruption and Economic Crimes Act (2003) and Law on Bribery (2016). Operationalization and effective implementation of these laws, however, remains incomplete. Recently, additional resources were provided for the law enforcement agencies (LEAs), including the Ethics and Anti-Corruption Committee (EACC) and the Department of Public Prosecution (DPP) who are now able to hire specialized experts to assist in the prosecution of corruption cases.

AML/CFT reforms. The authorities have taken steps to strengthen the AML/CMT framework in the areas of cash transaction monitoring and reporting by banks, offsite and onsite AML/CFT supervision, and enforcement actions. They also conducted a demonetization exercise in 2019 by withdrawing the old generation Kenya Shilling 1,000 note, which had been used for illicit financial flows both in Kenya and the broader region.

^{1/} [SPECIAL AUDIT REPORT -KEMSA.pdf \(parliament.go.ke\)](https://www.parliament.go.ke/SPECIAL_AUDIT_REPORT_-_KEMSA.pdf).

^{2/} [PPIP | Public Procurement Information Portal \(tenders.go.ke\)](https://www.tenders.go.ke/PPIP/).

^{3/} <https://www.kemsa.co.ke/tender-awards/>.

- **Making public procurement information available.** The authorities plan to ensure that comprehensive information on public tenders, including beneficial ownership information of the awarded entities, are publicly available on the government procurement information portal, and that bidders are subject to dissuasive sanctions for non-compliance (**structural benchmark**). Work on the State Procurement Portal is being expedited to be completed by end-April 2021. This will be complemented by reforms in train to strengthen procurement in public investment (MEFP, ¶53).
- **Operationalizing the Access to Information Act.** Enacted in 2016, this critical piece of legislation is overdue, and next steps to fully implement it—through the enactment of the regulations and introducing proactive disclosure across ministries—are key to enhancing

transparency and accountability. Standards for digitization and automation of records also will be developed to ensure compliance with minimum access to information requirements (MEFP, ¶56/(i)/1).

- **Review and strengthening of the preventive anti-corruption framework.** The current framework for preventing conflict of interest and disclosure of asset and interest declarations of senior public officials should be strengthened as a high priority. The ongoing review will aim at establishing a uniform disclosure regime, strengthening sanctions on misreporting, and improving accessibility of the asset declarations (MEFP, ¶56/(i)/2).
- **Strengthening AML/CFT measures to support anti-corruption efforts.** Effective implementation of customer due diligence measures for politically exposed persons would help prevent laundering proceeds of corruption, particularly in the financial sector. Ongoing initiatives are underway through the National Risk Assessment (NRA) process and in preparation for the Mutual Evaluation (ME) exercise by the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) expected this year. Risk-based AML/CFT supervision should be further strengthened through offsite and onsite supervision targeted at risks of laundering of proceeds of corruption. By June 2021, the authorities will formulate the National AML/CFT Strategy and Action Plan to address any deficiencies identified in the NRA. The strategic priorities of the Financial Reporting Centre, which is committed to strengthening the use of financial intelligence to trace proceeds of corruption by sharing relevant financial intelligence with law enforcement agencies, will be developed in the context of this exercise (MEFP, ¶56/(i)/3).

29. The authorities highlighted several areas for near-term focus. This will include implementation of the Access to Information Act (with possible technical assistance from the Fund's Legal Department); upgrading the financial disclosure and the conflict of interest framework for senior officials; and ensuring that the centralized public procurement portal reports comprehensive information (including beneficial ownership information).

C. Strengthening the Monetary Policy Framework and Safeguarding Financial Stability

30. The CBK's accommodative monetary policy stance remains appropriate. The CBK's measures since the outbreak of the COVID-19 crisis to buffer shocks and ease market liquidity pressures have been consistent with the central bank's medium-term inflation target of 5 percent +/- 2.5 percentage point (ppt) band,¹² while ensuring the continued good functioning of domestic capital markets. The exchange rate has continued to be allowed to function as a shock absorber with foreign exchange interventions used only to minimize excessive volatility.

31. In the coming months, the CBK intends to move ahead with its workplan to continue strengthening the monetary policy framework. The necessity of responding to the COVID shock

¹² A monetary policy consultation clause (MPCC) with a 5 percent +/- 2.5 ppt band is proposed to monitor inflation performance, providing for a consultation with the Executive Board if inflation falls outside the band (TMU, ¶23).

brought other priorities to the fore, but with the shock now receding the CBK plans to publish a white paper by end-June 2021 outlining planned reforms to improve the monetary policy framework drawing on inputs from many sources (**structural benchmark**) (MEFP, ¶41).

32. Widespread preemptive loan restructurings to ease liquidity pressures for many borrowers have been coming to an end, and performance of these loans is being monitored closely. The initiative, which involved household and corporate borrowers accounting for a reported 54 percent of banking system loans by value, avoided the potential for widespread insolvencies. About 90 percent of restructurings were carried out by large banks who follow forward-looking IFRS9 guidelines for expected loss provisioning and are well-capitalized. Supervisory and regulatory processes continue to aim at ensuring prudent asset classification and provisioning practices. In August 2020, the CBK instructed banks to revisit their capital planning (ICAAP) to assess resilience of their portfolios to the pandemic shock and potentially to curtail dividend payments. The new credit guarantee scheme can play an important role in supporting new credit to SMEs.

33. The CBK has implemented most of the recommendations from the September 2019 safeguards assessment. The assessment found that the CBK Board and Audit Committee have maintained strong oversight of operations, and the external audit and financial reporting practices continue to be aligned with international standards. Priority recommendations to strengthen the internal audit function and enhance the management of foreign reserves have been implemented.

34. Overall, the authorities emphasized that the speedy and forceful policy reaction to the COVID-19 shock, including monetary policy easing, emergency liquidity provision and preemptive loan restructurings, had provided essential support to the economy under stress. They viewed that exchange rate flexibility had been used effectively as a shock absorber. They noted that close monitoring of the post-shock economic and financial market situation, including loss provisioning and the impact on banks' earnings and capital buffers of restructured loans, would continue. In this context, loan classification and provisioning rules will continue to be fully applied as arrangements roll off, ensuring that any potential losses are recognized as accurately as possible.

FINANCING AND PROGRAM MODALITIES

35. The authorities request 38-month arrangements under the EFF and the ECF to meet the medium-term nature of Kenya's balance of payments adjustment needs.

36. Kenya's public debt is sustainable. Debt indicators, such as debt service as a share of exports and revenues, have worsened due to the shock. Fiscal adjustment under the program will reduce debt-related risks and put debt as a share of GDP firmly on a declining path by the end of the arrangements. Given the return of more normal global market conditions, staff expect the authorities to be able to access the Eurobond market at reasonable prices.

37. Kenya faces fiscal and BOP financing gaps through the program period. These gaps are particularly large during the first two years of the program. Proposed financing under the arrangements would partially fill these gaps, combined with relief from the G20 under the DSSI (approximately \$0.6 billion) as well as budget support from other development partners (\$1.6 billion in 2021). If DSSI creditors elect to provide relief on debt service coming due in the second half of 2021, this could provide additional exceptional financing

38. Combined access of 305 percent of quota under the arrangements is proposed to help Kenya cover these fiscal and external financing needs. With ECF access capped at the applicable PRGT norm of 75 percent of quota given earlier Fund financing, staff proposes SDR 1,248.44 million (230 percent of quota) from the EFF and SDR 407.09 million (75 percent of quota)

from the ECF. The program is fully financed through June-2022 with good prospects for the remainder of the arrangements. The authorities will also seek grants from donors or additional concessional lending from the African Development Bank or other IFIs.

39. Given the high degree of uncertainty surrounding the baseline and the unusually large risks in the early period due to COVID-19, the program design addresses heightened uncertainty in particular for the first two reviews. The pandemic's unique nature and associated high degree of uncertainty translates into larger than usual risks to the outlook and fiscal outcomes, including uncertainties about tax yields and contingent liabilities from the SOE sector. Meeting targets may become unrealistic or overly constrain policy if the shock's magnitude, duration, or impact are worse than expected. This could occur even with full implementation of the agreed policy agenda. By explicitly acknowledging the heightened uncertainty associated with the first two reviews (covering FY20/21), the focus would remain on the policy actions critical to achieving program objectives, with adequate flexibility to respond to COVID-related exogenous shocks. In this context staff proposes the following monitoring modalities:

- **Quarterly monitoring.** Through the second review, staff proposes program monitoring on a quarterly basis to ensure close engagement during a period of high uncertainty. From the second review, with the expectation of reduced uncertainty, program monitoring would be conducted on a semi-annual basis.
- **IT on tax collection.** In recognition of the uncertainty surrounding the yield of tax measures during the pandemic, the program will include an IT on tax collection (floor) for the first two

Kenya: Central Government Financial Operations, 2019/20–2023/24
(in percent of GDP)

	2019/20	2020/21	2021/22	2022/23	2023/24
	Prel		Projected		
Revenue	17.3	17.0	16.8	17.6	18.6
Expenditure	25.1	25.7	24.3	23.5	22.9
Overall Balance	(7.8)	(8.7)	(7.5)	(5.8)	(4.3)
Financing	7.8	6.7	6.3	5.3	3.9
Net Foreign Financing	3.3	1.7	1.1	0.9	1.1
Project loans	1.5	2.2	2.2	2.2	2.2
Program loans	2.3				
IMF RCF	0.7				
Commercial borrowing	0.1	3.2	3.9	0.8	0.7
Standard Gauge Railway	0.4	0.1	0.0	0.0	0.0
Repayments	(1.0)	(3.8)	(5.0)	(2.0)	(1.8)
Net Domestic Financing	4.5	5.0	5.2	4.4	2.8
Financing gap		(2.0)	(1.2)	(0.5)	(0.4)
<i>Potential additional sources</i>					
IMF (EFF/ECF)		0.7	0.5	0.5	0.4
DSSI Relief		0.6			
World Bank		0.7	0.7		
Memo item:					
Primary Balance	(3.5)	(4.6)	(3.0)	(1.1)	0.2

Sources: Kenyan authorities and IMF staff calculations.

program reviews (TMU, ¶14). During this period, in case of any tax shortfall that would compromise achievement of the primary deficit PC, the authorities are committed to identifying expenditure offsets (MEFP, ¶25) and depending on the extent and nature of the shortfall potentially additional tax measures. From the third review, the IT will be converted into a PC as COVID-19 uncertainty recedes.

- **Structural benchmarks.** In the first year of the program, structural benchmarks (MEFP, Table 2) would provide an additional means of measuring policy implementation in conjunction with the elements described above. Once the crisis recedes, the focus of structural benchmarks would be expanded to cover the broader range of reform priorities and structural measures necessary to achieve the program's overall objectives.
- **Adjustor on COVID-19 vaccine-related spending.** Due to the current uncertainty surrounding the global availability of COVID-19 vaccines and the cost and timing of Kenya's COVID-19 vaccination campaign, the program includes adjustors on PCs (primary fiscal balance, concessional borrowing limit, and the net international reserves) to enable undertaking a more accelerated COVID-19 vaccination program if this becomes feasible before the costs can be incorporated into the program baseline (TMU, ¶17 and ¶19).
- **Adjustor on net international reserves (NIR).** The NIR adjustor under the program PC will be symmetric for budget loans and commercial borrowing (other than debt management purposes). For program and project grants the adjustor would be asymmetric, i.e. the NIR target would be adjusted only in case of shortfalls of inflows compared to the baseline (TMU, ¶19). The CBK stressed that it would have been preferable to apply the asymmetric adjustor, which is used for grants, also to non-grant budget flows under the NIR adjustor.
- **Adjustor on extraordinary SOE support.** In line with the end-May structural benchmark and in recognition of the potential fiscal costs associated with addressing weakness in SOE sector, from July 1, 2021 to end-June, 2023 the program will include an adjustor on the primary balance target to absorb half of extraordinary support to SOEs up to 1 percentage point of GDP in such support, on a cumulative basis (TMU, ¶17). The other half of such costs and any support exceeding this amount will require equivalent offsetting measures to meet program targets.

40. Limits will be set on new borrowing. Reflecting Kenya's elevated debt risks, a PC is set on new foreign currency non-concessional borrowing. PCs will also be set on new foreign currency concessional borrowing and new domestic guarantees granted by the central government.

41. Kenya's capacity to repay the Fund is adequate. The total amount of outstanding credit to the Fund based on existing and prospective drawings would be SDR 1,301.4 million, or 239.7 percent of quota, at end-2021. This would peak at SDR 2,198 million, or 405 percent of quota in 2024 and then steadily decline. Fund credit outstanding will peak at 2.2 percent of GDP, while public debt service will peak over 112 percent of exports and about 79 percent of revenue, compared to 2.4 percent of GDP, 11.4 percent of exports and 17.3 of revenue for the median PRGT country). Associated servicing risks would be mitigated by expected increased access to concessional financing in the early years of the program and by progress in putting debt on a downward

trajectory. The materialization of downside risks such as worse-than-expected growth or a pullback of international investors from frontier markets in the medium term could place stress on Kenya's capacity to repay the Fund. However, given the likelihood of continued access to concessional financing in such a scenario, and in light of Kenya's strong track record of servicing debts to the Fund and other creditors, Kenya's ability to repay the Fund would remain adequate.

STAFF APPRAISAL

42. Kenya has been hit by an unprecedented external shock. Following the onset of COVID-19 and a sharp contraction in the second quarter of 2020, growth has been recovering strongly since mid-2020. However, important challenges remain in securing a durable and inclusive recovery.

43. The authorities responded quickly with broad-based policy actions to cushion the blow to the economy. The government quickly implemented a series of tax relief and targeted expenditure measures to ease the negative impact of the shock on households and firms. At the same time, important steps were taken to begin shoring up tax revenues and contain the overall impact on the deficit. The CBK also acted promptly to improve liquidity conditions, maintain financial market functioning, and temporarily ease the impact of the shock on borrowers.

44. However, the COVID-19 shock has exacerbated preexisting vulnerabilities. Disruptions to the economy and temporary tax cuts have led to significantly lower tax revenues. Along with necessary COVID-related spending, this meant an interruption in planned fiscal consolidation in FY19/20 and a moderate widening of the deficit in FY20/21, which is appropriate given the circumstances. Kenya's debt is sustainable, though debt vulnerabilities have increased, and Kenya is at high risk of debt distress.

45. The COVID-19 shock has also created fiscal and external financing gaps over the next several years. While international capital markets have reopened for frontier markets following the initial pullback, Kenya should prioritize concessional over external non-concessional borrowing to meet financing needs in the coming years. Financing from donors, domestic sources, and G20 debt relief under the DSSI will help meet Kenya's financing needs. External non-concessional borrowing should be limited to supporting critical growth-enhancing investment projects and to debt management operations when conditions are favorable.

46. The Fund-supported program will anchor the next phase of the authorities' pandemic response and a multi-year consolidation effort centered on raising tax revenues and firm expenditure control. By bringing the primary deficit below its debt-stabilizing level during the program period, debt as a share of GDP would be put firmly on a downward trajectory. Tax revenue would be brought back from current low levels to the levels achieved in recent years, generating the resources to help meet Kenya's development needs. Recent tax changes, including a range of base-broadening measures and the reversal of temporary cuts put in place last April, have been critical steps in this direction. The authorities' commitment to undertake further tax policy measures during the program is also an essential element of the strategy. Supported by continuous improvement in

revenue administration and careful prioritization of expenditures, these steps will allow maintaining needed social and development spending while delivering on the urgent need to reduce debt-related vulnerabilities.

47. Financial weaknesses that have emerged in some SOEs are an important source of fiscal risk. The program follows a staged approach to evaluate potential contingencies and ensure that the needed strategy to address SOE challenges will be consistent with Kenya's limited fiscal space. Looking forward, building up the National Treasury's capacity to monitor these risks and embedding more effective reporting on fiscal risks from SOEs and public private partnerships into the annual budget process will be important.

48. Immediate structural reform priorities will aim at improving fiscal governance and reducing the possibilities for corruption. The agenda will encompass fiscal structural reforms (revenue administration improvements) and spending efficiency (public financial management and public investment measures) as well as increasing fiscal transparency; and improvements in the authorities' anti-corruption framework. On the anti-corruption front, the work of the Auditor General, following up on irregularities that had emerged in procurement of health care equipment during the pandemic, should improve confidence, as will the publication of audits covering all COVID-related expenditures in FY19/20 and disclosure of beneficial ownership information of companies that are awarded contracts.

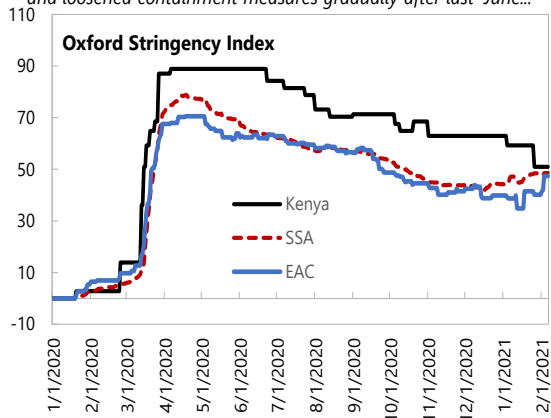
49. The authorities have pursued an appropriately accommodative monetary stance in the face of the COVID-19 shock. They should maintain this stance so long as inflation and inflation expectations remain well-anchored within the CBK's target band. A monetary policy consultation clause (MPCC) is proposed to monitor inflation performance. The CBK appropriately allowed the shilling to act as a shock absorber in the face of the COVID-19 shock. It should continue to do so and use FX intervention only to minimize excessive volatility. The forthcoming white paper on plans for strengthening the monetary policy framework will support monetary policy implementation.

50. The authorities should continue to closely monitor potential risks to financial stability. The banking sector remains well-capitalized and liquid, and steps taken by the CBK helped to avoid acute stresses in the banking sector caused by the COVID-19 shock. However, the shock has exacerbated preexisting asset quality issues, and close supervision of credit risks and adequacy of provisioning should be maintained. To support new credit to SMEs, the new credit guarantee scheme can play an important role, and it should avoid assuming undue exposure to banks' troubled borrowers or creating large contingent liabilities.

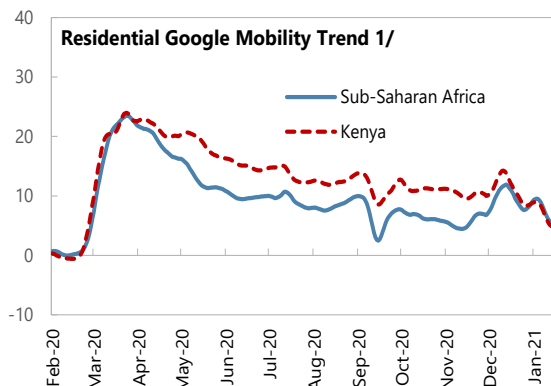
51. Staff supports the authorities' request for 38-month arrangements under the EFF and the ECF. Kenya faces protracted balance of payments and fiscal financing needs, which will need to be addressed via the envisaged fiscal adjustment and structural policies under the program, including with a focus on competitiveness. The authorities' strong demonstrated commitment to fiscal reforms during this unprecedented global shock is a key consideration in staff's support for the program.

Figure 1. Kenya: Real Sector Developments

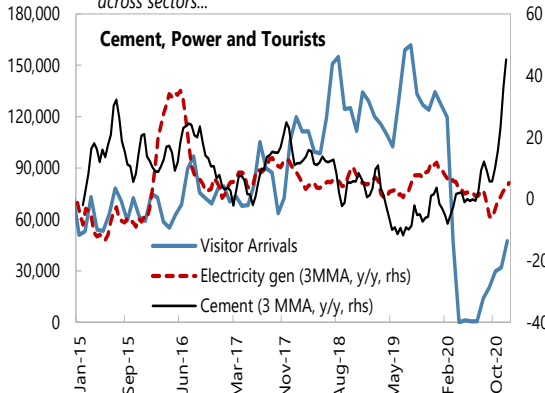
The authorities reacted forcefully to the COVID-19 outbreak and loosened containment measures gradually after last June...



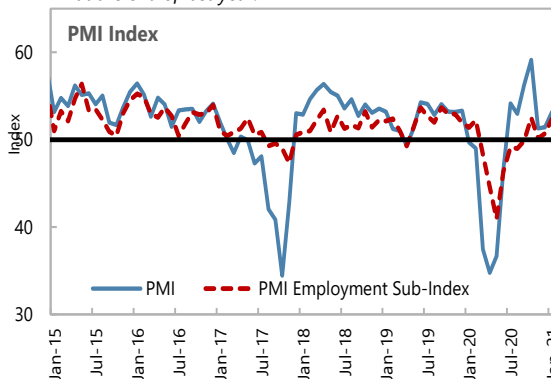
... with more stringent measures resulting in more restrained mobility in Kenya compared to SSA peers until early 2021.



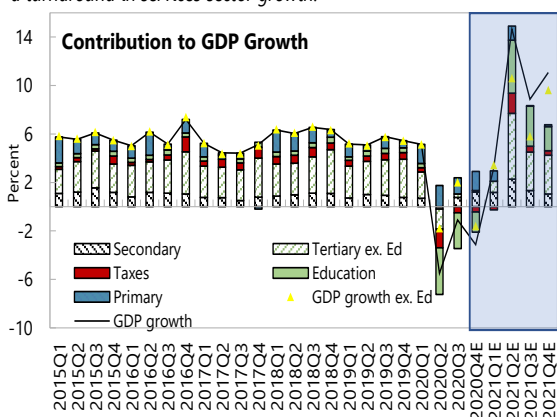
The recovery in the third quarter was strong, but uneven across sectors...



... and was followed by a modest rebound in employment at the end of last year.

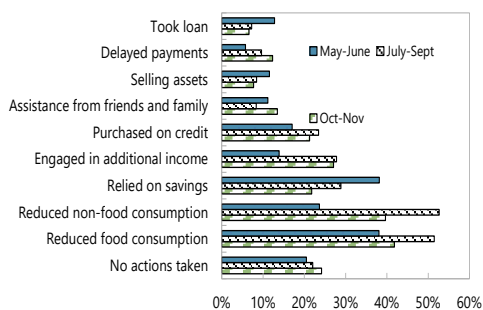


In 2021 GDP growth will be driven by strong base effects, and a turnaround in services sector growth.



The socio-economic impacts of the crisis are severe and will be persistent. Reducing food and non-food consumption continue to be the most commonly used coping mechanisms, while the use of savings has declined.

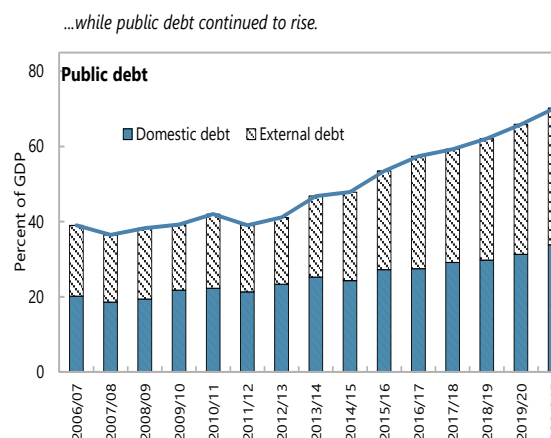
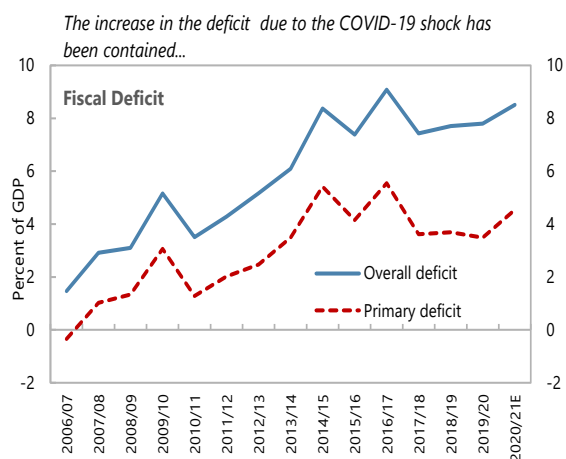
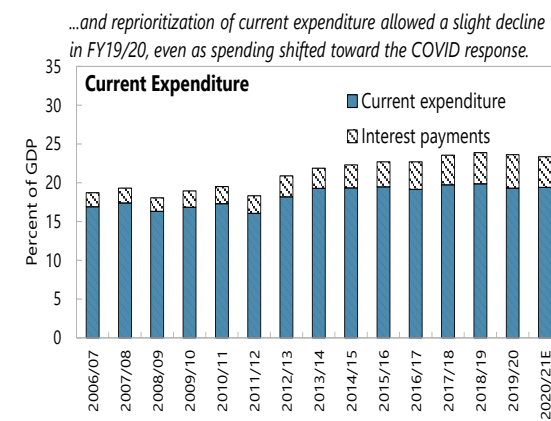
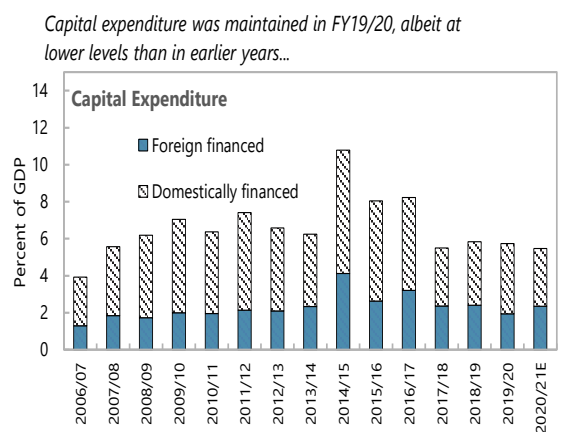
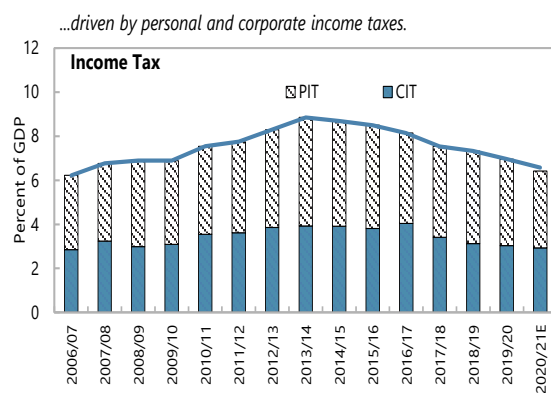
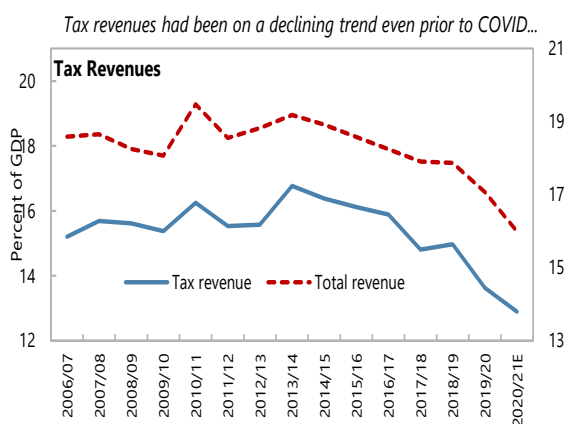
Strategies used to cope with the impact of the crisis



Sources: Kenyan authorities, Oxford COVID-19 Government Response Tracker, Markit Economics, World Bank and IMF staffs' Calculations and projections.

1/ The series captures mobility trends for places of residence. 7-day moving averages.

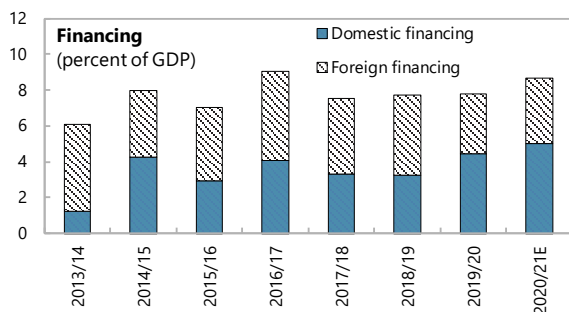
Figure 2. Kenya: Fiscal Sector Developments



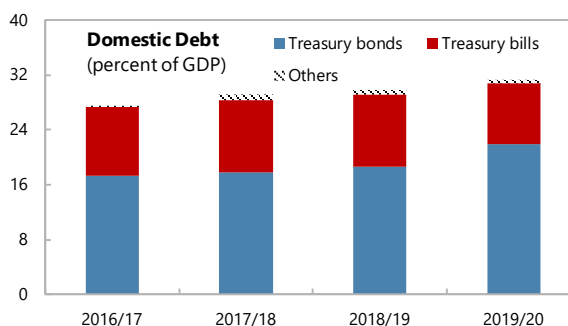
Sources: Kenyan authorities and IMF staff calculations and projections.

Figure 3. Kenya: Financing

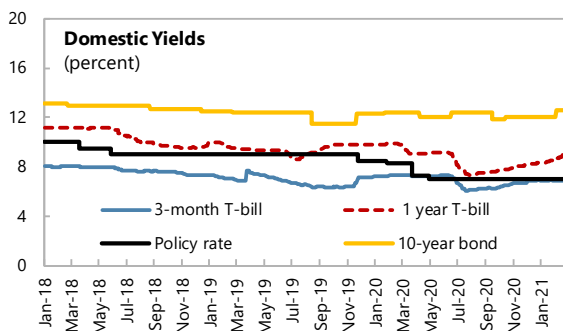
As the COVID-19 shock hampered access to international markets, reliance on domestic financing has increased in FY19/20 and FY20/21 ...



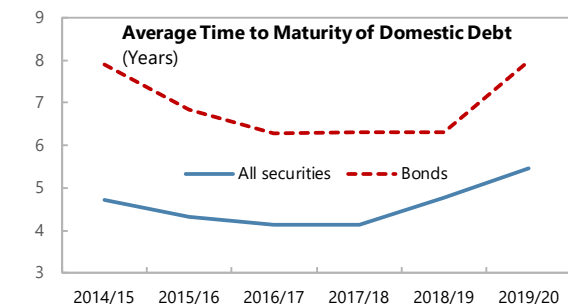
... increasing the stock of domestic debt.



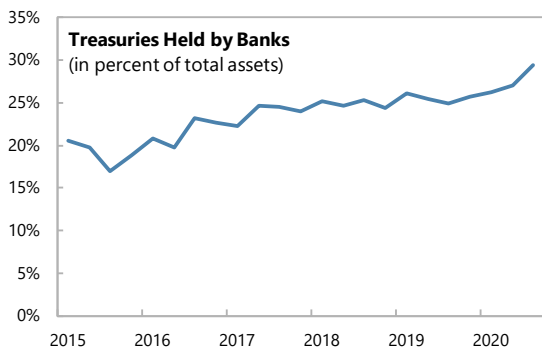
Nevertheless, financing conditions in the domestic market remained favorable towards longer-term securities...



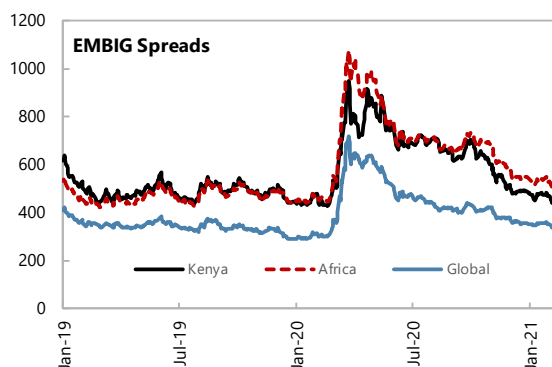
... allowing the government to further improve the maturity profile of its domestic debt.



Facing heightened uncertainty, commercial banks increased their exposure to the sovereign ...



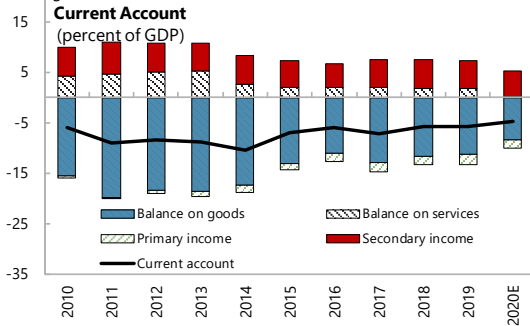
... as global external financing conditions gradually returned to pre-COVID levels.



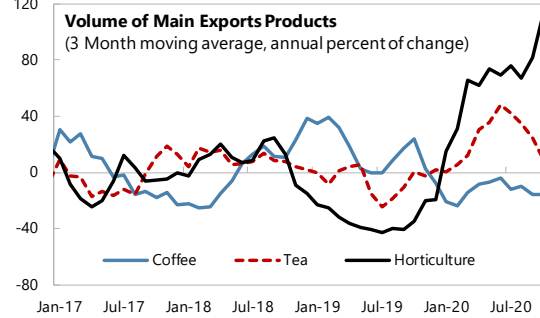
Sources: Kenyan authorities, Bloomberg and IMF staff calculations and projections.

Figure 4. Kenya: External Sector Developments

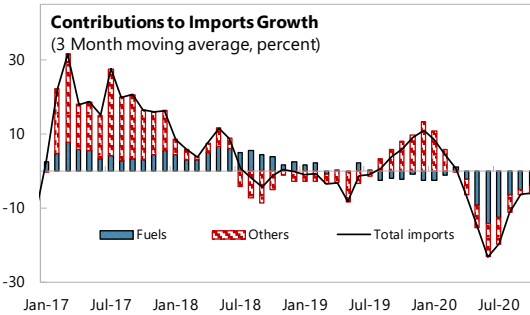
The current account deficit narrowed in 2020 with a declining goods deficit.



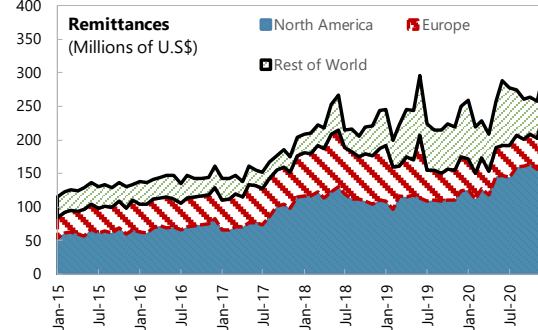
Despite initial disruptions in global supply chains, exports were resilient last year due to strong horticulture and tea exports...



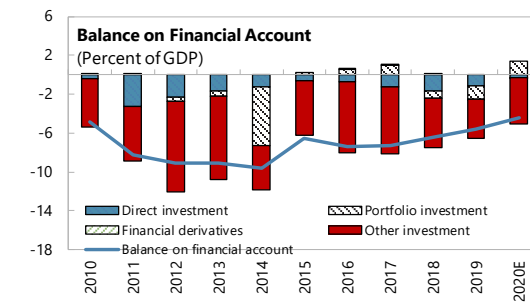
... while imports were held back by low commodity prices and weak domestic demand.



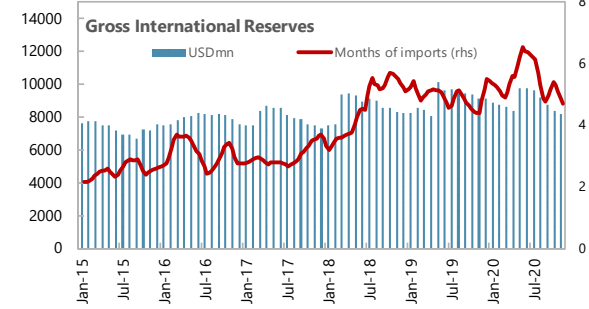
Remittances increased by 10 percent in 2020, driven by transfers from North America.



The COVID shock led to a reduction in FDI and net portfolio inflows, limiting sources of BOP financing.



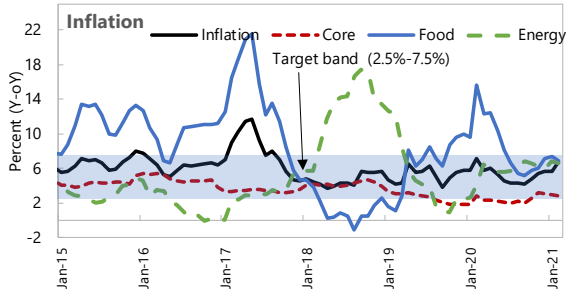
FX reserves declined by \$ 0.8 billion between end-2019 and end-2020, but are still above adequate levels.



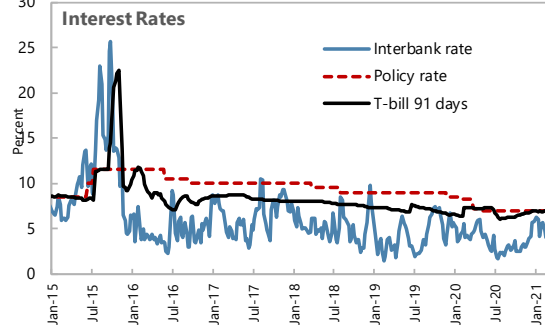
Sources: Kenyan authorities and IMF staff estimates.

Figure 5. Kenya: Monetary and Exchange Rate Developments

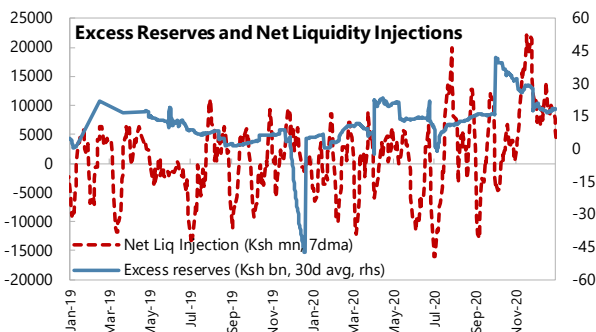
Headline inflation eased on low core inflation and moderating food prices driven by strong agricultural production.



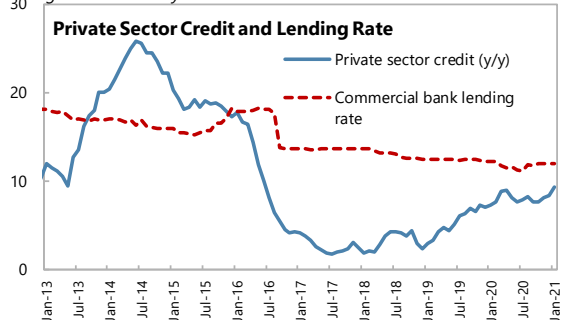
Domestic markets have remained liquid, supported by CBK policy measures



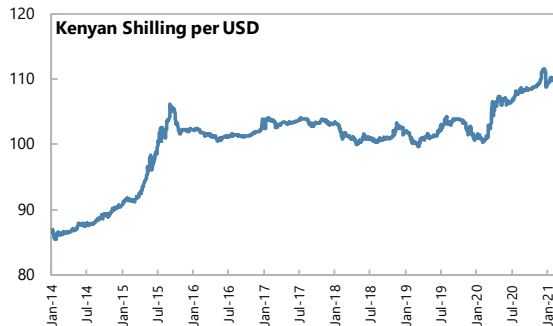
...and as seen by above average levels of excess reserves.



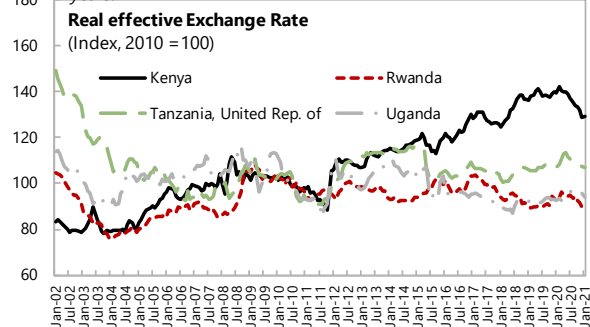
The COVID-19 shock halted the acceleration in private credit growth underway.



The KES depreciated following COVID-19 shock...



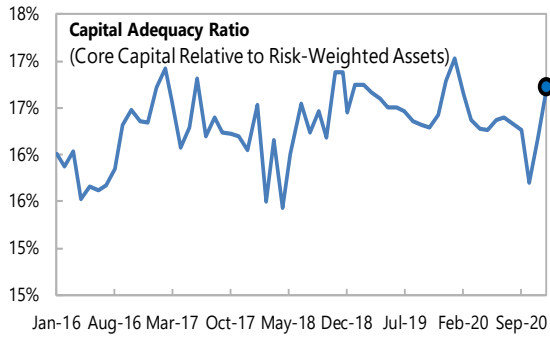
...leading to a reversal in the real appreciation seen in recent years.



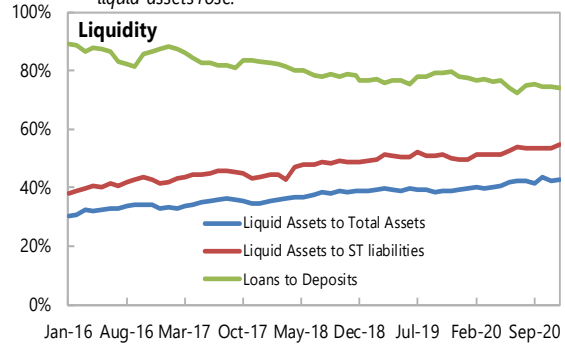
Sources: Kenyan authorities and IMF staff calculations.

Figure 6. Kenya: Financial Soundness Indicators

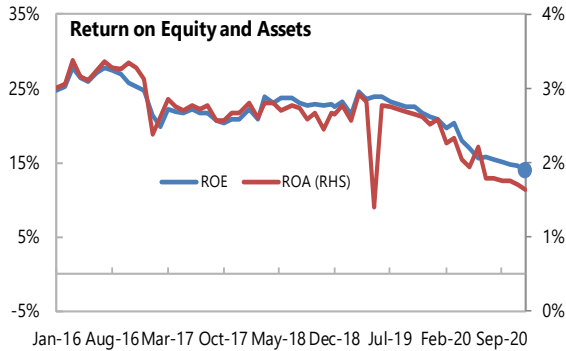
Kenyan banks remain well-capitalized overall.



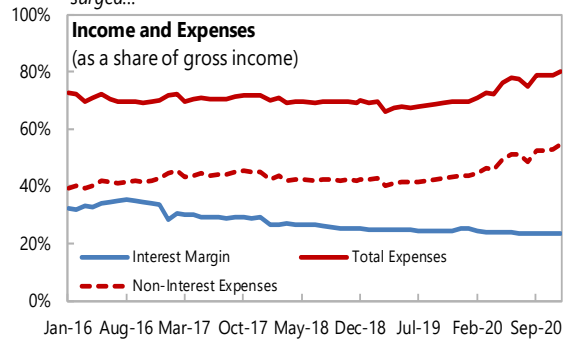
The loan-to-deposit ratio has declined as appetite for liquid assets rose.



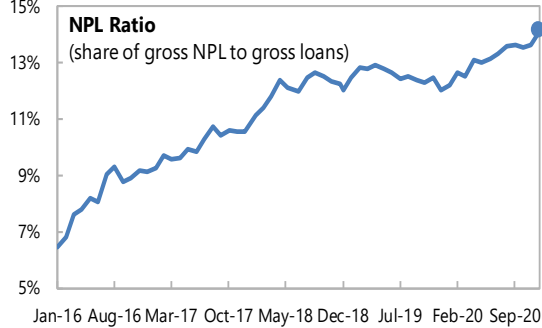
The banking sector's profitability declined...



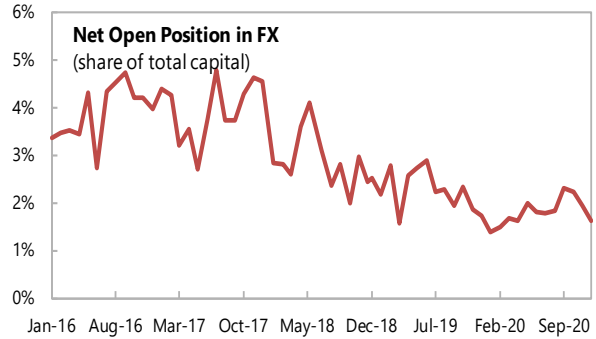
... as interest margins narrowed and non-interest expenses surged..



... due to the cost of NPL provisioning following the rapid increase in NPLs.



Banks' FX risk exposure remained contained.



Sources: CBK and IMF Staff Calculations.

Table 1a. Kenya: Selected Economic Indicators, 2017/18–2024/25
(Fiscal year basis) ¹

	2017/18	2018/19	2019/20	2020/21	2021/22	2022/23	2023/24	2024/25
	Actual		Est.			Projected		
(Annual percentage change, unless otherwise indicated)								
Output, prices, and exchange rate								
Real GDP	5.5	5.8	2.6	3.7	6.6	5.9	6.1	6.1
GDP deflator	4.9	2.4	5.8	5.6	4.3	4.8	5.0	5.1
CPI (period average)	5.2	5.2	5.0	5.0	5.0	5.0	5.0	5.0
CPI (end of period)	4.3	5.7	5.0	5.0	5.0	5.0	5.0	5.0
Core inflation (period average) ²	4.2	3.4	2.4	2.2	3.7	5.2	5.0	5.0
Exports volume	-0.5	0.7	3.1	10.2	11.8	10.0	9.7	9.2
Imports volume	-0.2	-1.3	3.3	5.6	12.4	12.8	11.3	9.8
Exchange rate (Kenyan shilling/US\$)	102.4	101.3	103.6	.	.	.	.	.
Real effective exchange rate (depreciation, -)	-0.3	8.3	1.2	.	.	.	.	.
Money and credit								
Broad money (M3)	10.4	9.2	8.4	.	.	.	.	.
Reserve money	7.4	2.5	-2.9	.	.	.	.	.
Credit to non-government sector	4.3	5.2	7.7	.	.	.	.	.
Policy rate	9.5	9.0	7.0	.	.	.	.	.
M3/GDP (percent)	38.4	38.0	38.0	.	.	.	.	.
NPLs (percent of total gross loans)	10.9	11.9	12.3	.	.	.	.	.
(Percent of GDP, unless otherwise indicated)								
Central government budget								
Total revenue, grants and unidentified tax policy measures	18.2	18.0	17.2	17.0	16.8	17.6	18.6	18.4
Tax revenues	14.8	15.0	13.6	12.9	13.5	14.7	15.6	15.6
Non-tax revenues	3.1	2.9	3.4	3.7	3.0	2.6	2.7	2.5
Grants	0.3	0.2	0.2	0.4	0.4	0.3	0.3	0.3
Expenditure	25.3	25.7	25.0	25.7	24.3	23.5	22.9	22.1
Current	19.7	19.8	19.3	20.0	19.3	18.4	17.9	17.2
Capital	5.5	5.8	5.7	5.7	5.0	5.0	5.0	4.9
Primary balance	-3.6	-3.7	-3.5	-4.6	-3.0	-1.1	0.2	0.5
Excluding SGR related spending	-2.9	-2.8	-3.0	-4.4	-3.0	-1.1	0.2	0.5
Cash Adjustment	-0.4	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
Overall balance	-7.4	-7.7	-7.8	-8.7	-7.5	-5.8	-4.3	-3.7
Excluding SGR-related spending	-6.7	-6.8	-7.3	-8.6	-7.5	-5.8	-4.3	-3.7
Excluding grants	-7.8	-7.9	-8.0	-9.1	-7.9	-6.2	-4.7	-4.0
Net domestic borrowing	3.3	3.3	4.5	5.0	5.2	4.4	2.8	2.4
Public debt								
Public gross nominal debt	59.3	62.0	65.8	70.4	72.6	72.9	71.4	69.2
Public net nominal debt	53.3	56.6	61.4	66.0	68.2	68.6	67.0	64.8
Public gross debt, PV	51.8	54.2	59.5	62.7	63.6	63.8	63.1	62.0
Public net debt, PV	45.8	48.8	55.1	58.3	59.2	59.4	58.8	57.6
Gross domestic debt	29.2	29.7	31.2	33.9	36.2	37.4	36.8	35.8
Gross external debt	30.1	32.3	34.6	36.5	36.5	35.5	34.6	33.4
Investment and saving								
Investment	14.6	14.2	13.3	13.2	13.5	14.5	16.0	17.4
General government	5.5	5.9	5.8	5.7	5.0	5.0	5.0	4.9
Nongovernment	9.1	8.3	7.5	7.5	8.5	9.5	11.0	12.5
Saving	9.0	9.5	8.9	8.5	8.2	9.1	10.5	11.8
General government	-1.8	-1.8	-2.2	-3.3	-2.8	-0.3	2.0	2.5
Nongovernment	10.7	11.4	11.1	11.8	11.0	9.4	8.5	9.3
External sector								
Exports (goods and services)	13.3	12.6	10.9	10.6	11.5	12.1	12.7	13.1
Imports (goods and services)	-22.9	-21.0	-19.0	-19.1	-20.8	-21.7	-22.4	-23.0
Current account balance (including grants)	-5.7	-4.7	-4.4	-4.7	-5.4	-5.4	-5.5	-5.6
Gross international reserves								
In billions of US\$	8.9	9.5	9.7	10.1	9.5	9.9	10.6	12.0
In months of next year imports	5.6	6.2	6.0	5.3	4.5	4.2	4.1	4.2
Memorandum items:								
GDP at current market prices (Ksh billion)	8,501	9,367	10,175	11,146	12,389	13,754	15,331	17,095
GDP per capita (nominal US\$)	1,815	1,946	2,020	2,082	2,172	2,268	2,384	2,514

Sources: Kenyan authorities and IMF staff estimates and projections.

¹ Fiscal years are from July 1 to June 30.

² Excluding food and fuel.

Table 1b. Kenya: Selected Economic Indicators, 2018–25
(Calendar year basis)

	2018	2019	2020	2021	2022	2023	2024	2025
	Actual		Est.			Projected		
(Annual percentage change, unless otherwise indicated)								
Output, prices, and exchange rate								
Real GDP	6.3	5.4	-0.1	7.6	5.7	6.1	6.1	6.1
GDP deflator	2.4	4.0	8.2	3.9	4.6	5.0	5.1	5.1
CPI (period average)	4.7	5.2	5.3	5.0	5.0	5.0	5.0	5.0
CPI (end of period)	5.7	5.8	5.6	5.0	5.0	5.0	5.0	5.0
Core inflation (period average) ¹	4.2	2.6	2.3	2.1	5.3	5.0	5.0	5.0
Exports volume	1.6	-0.9	6.4	13.9	10.0	10.1	9.3	9.1
Imports volume	-8.5	6.5	0.3	10.9	13.7	12.0	10.6	9.0
Exchange rate (Kenyan shilling/US\$)	101.2	102.1	106.2	.	.	.	.	.
Real effective exchange rate (depreciation, -)	3.5	4.8	-1.5	.	.	.	.	.
Money and credit								
Broad money (M3)	10.1	5.6	10.6	11.8	10.6	11.4	11.0	11.5
Reserve money	12.1	-6.3	3.9	11.2	10.1	11.0	10.6	11.2
Credit to non-government sector	2.4	7.1	7.7	7.7	7.8	10.1	10.8	12.8
Policy rate	9.0	8.5	7.0	.	.	.	.	.
M3/GDP (percent)	37.5	36.2	37.0	37.0	37.0	37.0	36.9	36.9
NPLs (percent of total gross loans)	12.0	12.0	13.2					
(Percent of GDP, unless otherwise indicated)								
Central government budget								
Total revenue, grants and unidentified tax policy measures	18.2	17.7	17.3	16.9	17.3	18.2	18.5	18.9
Tax revenues	15.0	14.3	13.4	13.2	14.2	15.2	15.6	16.0
Non-tax revenues	3.0	3.2	3.6	3.3	2.8	2.6	2.6	2.5
Grants	0.3	0.2	0.3	0.4	0.4	0.3	0.3	0.3
Expenditure	25.6	25.4	25.7	25.0	24.0	23.2	22.6	22.1
Current	19.9	19.6	19.9	19.6	18.9	18.2	17.6	17.2
Capital	5.7	5.8	5.8	5.4	5.0	5.0	5.0	4.9
Primary balance	-3.7	-3.6	-4.1	-3.7	-2.0	-0.4	0.3	0.9
Excluding SGR-related spending	-2.9	-3.0	-3.8	-3.7	-2.0	-0.4	0.3	0.9
Overall balance	-7.4	-7.7	-8.4	-8.1	-6.6	-5.1	-4.0	-3.2
Excluding SGR-related spending	-6.6	-7.1	-8.1	-8.0	-6.6	-5.1	-4.0	-3.2
Excluding grants	-7.6	-7.9	-8.7	-8.5	-7.0	-5.4	-4.3	-3.5
Net domestic borrowing	3.3	3.9	4.8	5.1	4.8	3.6	2.6	3.0
Public debt								
Public gross nominal debt	60.2	62.1	68.7	71.5	72.9	72.3	71.8	70.0
Public net nominal debt	54.5	57.2	64.3	68.5	70.1	69.5	67.7	66.7
Public gross debt, PV	51.8	56.6	62.4	63.0	64.2	63.4	62.9	61.1
Public net debt, PV	46.1	51.6	58.0	60.0	61.4	60.6	58.8	57.8
Gross domestic debt	29.6	30.6	33.0	33.7	35.4	35.6	36.1	35.0
Gross external debt	30.6	31.5	35.6	37.8	37.6	36.7	35.7	35.0
Investment and saving								
Investment	14.3	13.8	12.8	13.4	14.0	15.0	17.0	17.9
General government	5.7	5.8	5.8	5.4	5.0	5.0	5.0	4.9
Nongovernment	8.6	8.0	7.0	8.0	9.0	10.0	12.0	13.0
Saving	8.6	8.0	8.0	8.0	8.6	9.5	11.4	12.3
General government	-1.8	-2.0	-2.8	-3.1	-1.5	0.9	2.3	3.4
Nongovernment	10.4	10.0	10.8	11.1	10.2	8.7	9.1	8.9
External sector								
Exports (goods and services)	13.2	12.1	10.0	11.2	11.8	12.4	12.9	13.3
Imports (goods and services)	-23.0	-21.4	-18.2	-20.4	-21.3	-22.1	-22.8	-23.3
Current account balance (including grants)	-5.7	-5.8	-4.8	-5.3	-5.4	-5.5	-5.6	-5.6
Gross international reserves								
In billions of US\$	8.1	9.1	8.3	9.3	9.6	10.2	11.0	12.9
In months of next year imports	4.8	6.1	4.6	4.6	4.3	4.1	4.1	4.3
Memorandum items:								
GDP at current market prices (Ksh billion)	8,892	9,740	10,525	11,767	13,011	14,497	16,165	18,025
GDP per capita (nominal US\$)	1,889	2,004	2,035	2,129	2,214	2,323	2,446	2,582

Sources: Kenyan authorities and IMF staff estimates and projections.

¹ Excluding food and fuel.

Table 2a. Kenya: Central Government Financial Operations 2019/20–2024/25¹
(billions of Kenyan Shilling)

	2019/20		2020/21		2021/22		2022/23		2023/24		2024/25	
	Prel.	Supp I	Proj.	BPS 21	Proj.	BPS 21	Proj.	BPS 21	Proj.	BPS 21	Proj.	
Revenues and grants	1,753.4	1,898.0	1,898.0	2,080.0	2,080.0	2,426.6	2,426.6	2,844.5	2,844.5	3,149.1	3,149.1	
Revenue	1,733.6	1,849.2	1,849.2	2,033.9	2,033.9	2,379.7	2,379.7	2,796.4	2,796.4	3,099.8	3,099.8	
Tax revenue (including unidentified tax measures)	1,383.9	1,433.3	1,433.3	1,667.4	1,667.4	2,024.1	2,024.0	2,387.5	2,387.6	2,667.7	2,667.7	
Income tax	706.9	733.0	733.0	834.5	834.4	997.3	942.7	1,178.6	1,057.5	1,316.2	1,181.2	
Personal income	399.2	388.7	388.7	435.9	435.9	512.7	489.0	608.7	546.2	676.6	607.2	
Corporate income	307.7	344.3	344.3	398.5	398.5	484.6	453.7	569.9	511.3	639.6	574.0	
Import duty (net)	98.0	96.3	96.3	119.0	119.0	144.9	136.9	170.4	152.9	187.5	168.3	
Excise duty	195.3	208.8	208.8	241.0	241.0	297.2	280.9	346.9	311.2	389.7	349.7	
Value-added tax	383.7	395.2	395.2	472.9	472.9	584.7	552.7	691.6	620.6	774.3	694.9	
Domestic	213.9	206.2	206.2	249.0	249.0	304.3	275.4	350.4	314.4	387.4	347.7	
Imports	169.8	189.0	189.0	223.9	223.9	280.4	277.2	341.2	306.2	386.8	347.2	
Nontax revenue	349.7	416.0	416.0	366.5	366.5	355.7	355.7	408.8	408.8	432.1	432.1	
Investment income	46.0	45.1	45.1	30.0	30.0	31.5	31.5	33.1	33.1	34.7	34.7	
Other	143.4	115.7	115.7	78.2	78.2	86.0	86.0	95.7	95.7	105.0	105.0	
Ministerial and Departmental Fees (AIA)	137.0	228.0	228.0	230.5	230.5	207.7	207.7	246.9	246.9	256.1	256.1	
Railway Levy	23.3	27.2	27.2	27.8	27.8	30.4	30.4	33.2	33.2	36.3	36.3	
Grants	19.8	48.7	48.7	46.1	46.1	46.9	46.9	48.1	48.1	49.3	49.3	
Project grants	15.2	41.3	41.3	43.6	43.6	46.9	46.9	48.1	48.1	49.3	49.3	
Program grants	4.6	7.4	7.4	2.5	2.5	0.0	0.0	0.0	0.0	0.0	0.0	
Expenditure and net lending	2,545.0	2,864.5	2,864.5	3,010.0	3,010.0	3,202.0	3,227.0	3,495.6	3,510.6	3,762.9	3,780.6	
Recurrent expenditure	1,961.1	2,226.0	2,226.0	2,400.9	2,387.6	2,531.5	2,535.5	2,735.9	2,739.8	2,928.5	2,946.2	
Transfer to counties	325.3	383.0	383.0	409.8	385.3	406.5	400.5	412.3	408.8	417.5	425.2	
Interest payments	437.2	458.7	458.7	560.6	560.6	644.0	644.0	695.6	695.6	713.8	713.8	
Domestic interest	315.4	340.0	340.0	421.7	421.7	482.4	482.4	508.0	508.0	518.7	518.7	
Foreign interest due	121.8	118.7	118.7	138.9	138.9	161.5	161.5	187.6	187.6	195.1	195.1	
Wages and benefits (civil service)	449.9	493.9	493.9	524.5	535.8	550.7	560.7	588.3	595.8	635.3	645.3	
Civil service reform	0.0	7.3	7.3	21.6	21.6	22.9	22.9	23.8	23.8	24.8	24.8	
Pensions and Other Consolidated Fund Services	89.6	115.3	115.3	137.0	137.0	152.9	152.9	167.9	167.9	192.6	192.6	
Defense and NSIS	138.0	152.0	152.0	156.9	156.9	161.9	161.9	170.0	170.0	170.0	170.0	
Other	521.1	615.7	615.7	590.4	590.4	592.5	592.5	677.9	677.9	774.5	774.5	
Development and net lending	583.9	638.5	638.5	609.1	622.4	670.5	691.5	759.8	770.7	834.4	834.4	
Domestically financed	385.6	366.9	366.9	324.4	339.0	357.7	378.8	409.8	420.8	444.4	444.4	
of which: SOEs emergency funding			36.3									
Foreign financed	197.6	271.6	271.6	284.7	283.4	312.7	312.7	349.9	349.9	390.0	390.0	
of which: SGR project	44.8	11.9	11.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Net lending	0.7	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Overall balance including measures (cash basis, incl. grants)	-791.5	-966.6	-966.6	-930.0	-930.0	-775.3	-800.4	-651.2	-666.0	-613.8	-631.5	
Financing	791.5	966.6	966.6	930.0	930.0	775.3	800.4	651.2	666.0	613.8	631.5	
Net foreign financing	338.5	428.5	410.1	267.3	282.6	263.1	195.4	173.8	238.3	154.3	226.6	
Disbursements	440.1	785.7	767.2	880.6	896.0	542.2	474.5	455.8	520.3	381.1	453.5	
Project loans	152.3	241.7	241.7	273.5	273.5	302.0	302.0	338.8	338.8	377.6	377.6	
Program loans	237.0	179.5	161.1	131.8	143.5	134.6	66.9	3.5	68.0	3.5	75.8	
of which: IMF (RCF+ proposed EFF/ECF)	78.3	79.0	77.6	58.4	58.4	66.4	66.4	67.3	67.3	0.0	0.0	
Non-concessional	5.9	352.5	352.5	475.3	478.9	105.6	105.6	113.6	113.6	0.0	0.0	
Standard Gauge Railway	44.8	11.9	11.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Repayments due	-101.6	-357.2	-357.2	-613.4	-613.4	-279.1	-279.1	-282.1	-282.1	-226.9	-226.9	
Net domestic financing	453.1	538.1	556.5	662.8	647.4	512.2	605.0	477.4	427.7	459.5	404.9	
<i>Memorandum items:</i>												
Nominal GDP	10,156.6	11,168.5	11,145.6	12,393.1	12,389.0	13,759.9	13,754.5	15,373.1	15,331.2	17,128.4	17,095.0	
Primary balance incl. grants	-354.3	-507.8	-507.8	-369.4	-369.4	-131.4	-156.4	44.5	29.6	100.0	82.3	
Debt Service (DS) Relief			71.0									
Repayment					-8.5		-17.3		-17.4		-17.6	
Total gross public debt, gross	6,693.3	7,849.8	7,849.8	8,997.3	8,997.3	10,032.8	10,032.8	10,943.8	10,943.8	11,831.7	11,831.7	
external debt	3,515.8	4,072.4	4,072.4	4,518.0	4,518.0	4,888.6	4,888.6	5,302.9	5,302.9	5,708.5	5,708.5	
domestic debt	3,177.5	3,777.4	3,777.4	4,479.3	4,479.3	5,144.1	5,144.1	5,641.0	5,641.0	6,123.1	6,123.1	
Total net public debt	6,248.2	7,361.3	7,361.3	8,454.3	8,454.3	9,429.9	9,429.9	10,271.9	10,271.9	11,082.4	11,082.4	
Unidentified tax policy measures	0	0	0	0	0	111	111	135	135	28	28	
Pending bills	56.0											
Government deposits ²	445.1											

Sources: Kenyan authorities and IMF staff estimates and projections.

¹ Fiscal year runs from July to June.

² Includes KSh21.9 billion of RCF funds spent in early FY2020/21.

Table 2b. Kenya: Central Government Financial Operations 2019/20–2024/25 ¹
(in percent of GDP)

	2019/20		2020/21		2021/22		2022/23		2023/24		2024/25	
	Prel.	Supp I	Proj.	BPS 21	Proj.	BPS 21	Proj.	BPS 21	Proj.	BPS 21	Proj.	
Revenues and grants	17.3	17.0	17.0	16.8	16.8	17.6	17.6	18.6	18.6	18.4	18.4	
Revenue	17.1	16.6	16.6	16.4	16.4	17.3	17.3	18.2	18.2	18.1	18.1	
Tax revenue (including unidentified tax measures)	13.6	12.9	12.9	13.5	13.5	14.7	14.7	15.6	15.6	15.6	15.6	
Income tax	7.0	6.6	6.6	6.7	6.7	7.3	6.9	7.7	6.9	7.7	6.9	
Personal income	3.9	3.5	3.5	3.5	3.5	3.7	3.6	4.0	3.6	4.0	3.6	
Corporate income	3.0	3.1	3.1	3.2	3.2	3.5	3.3	3.7	3.3	3.7	3.4	
Import duty (net)	1.0	0.9	0.9	1.0	1.0	1.1	1.0	1.1	1.0	1.1	1.0	
Excise duty	1.9	1.9	1.9	1.9	1.9	2.2	2.0	2.3	2.0	2.3	2.0	
Value-added tax	3.8	3.5	3.5	3.8	3.8	4.3	4.0	4.5	4.0	4.5	4.1	
Domestic	2.1	1.9	1.9	2.0	2.0	2.2	2.0	2.3	2.1	2.3	2.0	
Imports	1.7	1.7	1.7	1.8	1.8	2.0	2.0	2.2	2.0	2.3	2.0	
Nontax revenue	3.4	3.7	3.7	3.0	3.0	2.6	2.6	2.7	2.7	2.5	2.5	
Investment income	0.5	0.4	0.4	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	
Other	1.4	1.0	1.0	0.6	0.6	0.6	0.6	0.6	0.6	0.6	0.6	
Ministerial and Departmental Fees (AIA)	1.3	2.0	2.0	1.9	1.9	1.5	1.5	1.6	1.6	1.5	1.5	
Railway Levy	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	
Grants	0.2	0.4	0.4	0.4	0.4	0.3	0.3	0.3	0.3	0.3	0.3	
Expenditure and net lending	25.1	25.7	25.7	24.3	24.3	23.3	23.5	22.8	22.9	22.0	22.1	
Recurrent expenditure	19.3	20.0	20.0	19.4	19.3	18.4	18.4	17.8	17.9	17.1	17.2	
Transfer to counties	3.2	3.4	3.4	3.3	3.1	3.0	2.9	2.7	2.7	2.4	2.5	
Interest payments	4.3	4.1	4.1	4.5	4.5	4.7	4.7	4.5	4.5	4.2	4.2	
Domestic interest	3.1	3.1	3.1	3.4	3.4	3.5	3.5	3.3	3.3	3.0	3.0	
Foreign interest due	1.2	1.1	1.1	1.1	1.1	1.2	1.2	1.2	1.2	1.1	1.1	
Wages and benefits (civil service)	4.4	4.4	4.4	4.2	4.3	4.0	4.1	3.8	3.9	3.7	3.8	
Pensions and Other Consolidated Fund Services	0.9	1.0	1.0	1.1	1.1	1.1	1.1	1.1	1.1	1.1	1.1	
Defense and NSIS	1.4	1.4	1.4	1.3	1.3	1.2	1.2	1.1	1.1	1.0	1.0	
Other	5.1	5.5	5.5	4.8	4.8	4.3	4.3	4.4	4.4	4.5	4.5	
Development and net lending	5.7	5.7	5.7	4.9	5.0	4.9	5.0	5.0	5.0	4.9	4.9	
Domestically financed	3.8	3.3	3.3	2.6	2.7	2.6	2.8	2.7	2.7	2.6	2.6	
of which: SOEs emergency funding	0.0		0.3									
Foreign financed	1.9	0.0	2.4	0.0	2.3	0.0	2.3	0.0	2.3	0.0	2.3	
of which: SGR project	0.4	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Net lending	0.0	2.4	0.0	2.3	0.0	2.3	0.0	2.3	0.0	2.3	0.0	
Overall balance incl. measures and grants (cash basis)	-7.8	-8.7	-8.7	-7.5	-7.5	-5.6	-5.8	-4.2	-4.3	-3.6	-3.7	
Financing	7.8	8.7	8.7	7.5	7.5	5.6	5.8	4.2	4.3	3.6	3.7	
Net foreign financing	3.3	3.8	3.7	2.2	2.3	1.9	1.4	1.1	1.6	0.9	1.3	
Disbursements	4.3	7.0	6.9	7.1	7.2	3.9	3.5	3.0	3.4	2.2	2.7	
Project loans	1.5	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	2.2	
Program loans	2.3	1.6	1.4	1.1	1.2	1.0	0.5	0.0	0.4	0.0	0.4	
of which: IMF (RCF+ proposed EFF/ECF)	0.8	0.7	0.7	0.0	0.5	0.0	0.5	0.0	0.4	0.0	0.0	
Non-concessional	0.1	3.2	3.2	3.8	3.9	0.8	0.8	0.7	0.7	0.0	0.0	
Standard Gauge Railway	0.4	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Repayments due	-1.0	-3.2	-3.2	-5.0	-5.0	-2.0	-2.0	-1.8	-1.8	-1.3	-1.3	
Net domestic financing	4.5	4.8	5.0	5.3	5.2	3.7	4.4	3.1	2.8	2.7	2.4	
<i>Memorandum items:</i>												
Primary balance incl. grants (Central government)	-3.5	-4.6	-4.6	-3.0	-3.0	-1.0	-1.1	0.3	0.2	0.6	0.5	
Debt Service (DS) Relief			0.6									
Repayment					-0.1		-0.1		-0.1		-0.1	
Total gross public debt, gross	65.9	70.4		72.6	72.9	71.4	71.4	71.4	71.4	69.2	69.2	
of which: external debt	34.6	36.5		36.5	36.5	35.5	35.5	34.6	34.6	33.4	33.4	
of which: domestic debt	31.3	33.9		36.2	36.2	37.4	37.4	36.8	36.8	35.8	35.8	
Total gross public debt, PV	59.5	62.7		63.6	63.6	63.8	63.8	63.1	63.1	62.0	62.0	
Total net public debt	61.5	66.0		68.2	68.2	68.6	68.6	67.0	67.0	64.8	64.8	
Unidentified tax policy measures	0.0	0.0		0.0	0.0	0.8	0.8	0.9	0.9	0.2	0.2	
Pending bills	0.6											

Sources: Kenyan authorities and IMF staff estimates and projections.

¹ Fiscal year runs from July to June.

Table 3. Kenya: Monetary Survey Dec. 2018–Dec. 2021

(In billions of Kenyan shillings, unless otherwise indicated)

	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21
	Act.	Act.	Act.	Act.	Act.	Act.	Act.	Act.	Act.	Proj.	Proj.	Proj.	Proj.
Central Bank of Kenya (CBK)													
Net foreign assets	739	747	941	872	833	801	918	805	738	675	865	755	768
Net domestic assets	-247	-291	-501	-464	-372	-355	-491	-353	-269	-200	-394	-241	-255
Net domestic credit	-69	-96	-208	-198	-168	-117	-217	-86	33	108	-78	83	76
Government (net)	-95	-99	-190	-182	-182	-119	-89	-177	-32	-22	-103	-83	-60
Commercial banks (net)	23	-1	-21	-19	11	-1	-131	88	61	127	21	163	133
Other items (net)	-179	-195	-294	-266	-204	-238	-274	-267	-301	-309	-315	-324	-331
Reserve money	492	456	440	408	461	446	427	452	470	475	471	514	512
Currency outside banks	230	225	197	158	199	198	211	218	234	217	219	249	248
Bank reserves	262	231	243	250	262	247	216	235	236	258	252	265	264
Banks													
Net foreign assets	-25	-27	-1	-36	-29	-33	-33	-56	8	-32	-33	-34	-34
(in millions of US dollars)	-249	-273	-11	-347	-285	-314	-307	-514	73	-290	-300	-300	-300
Reserves	262	231	243	250	262	247	216	235	236	258	252	265	264
Credit to CBK	-23	1	21	19	-11	1	131	-88	-61	-127	-21	-163	-133
Net domestic assets	2,865	2,959	2,996	3,052	3,073	3,214	3,295	3,490	3,508	3,587	3,777	3,981	3,933
Net domestic credit	3,473	3,603	3,676	3,745	3,807	3,904	3,992	4,227	4,276	4,446	4,379	4,608	4,590
Government (net)	953	1,063	1,080	1,077	1,124	1,156	1,211	1,373	1,375	1,491	1,383	1,527	1,452
Other public sector	101	100	96	100	92	91	88	89	91	95	97	101	101
Private sector	2,419	2,441	2,500	2,569	2,591	2,658	2,692	2,765	2,810	2,860	2,899	2,981	3,037
Other items (net)	-608	-644	-681	-694	-734	-690	-697	-737	-768	-858	-603	-627	-657
Total deposits	3,078	3,164	3,259	3,285	3,296	3,430	3,609	3,581	3,691	3,687	3,974	4,050	4,031
Monetary survey													
Net foreign assets	714	720	940	835	804	768	885	749	746	644	832	722	734
Net domestic assets	2,624	2,695	2,624	2,638	2,720	2,893	2,978	3,094	3,245	3,343	3,466	3,657	3,624
Net domestic credit	3,381	3,508	3,490	3,567	3,628	3,789	3,906	4,053	4,248	4,427	4,280	4,528	4,534
Government (net)	858	964	891	894	941	1,037	1,122	1,196	1,343	1,469	1,280	1,443	1,392
Other public sector	101	100	96	100	92	91	88	89	91	95	97	101	101
Private	2,422	2,444	2,503	2,572	2,595	2,661	2,695	2,769	2,813	2,863	2,902	2,984	3,041
Other items (net)	-757	-813	-866	-929	-909	-896	-928	-959	-1,003	-1,084	-814	-871	-909
M1	1,478	1,520	1,575	1,460	1,525	1,595	1,667	1,666	1,720	1,711	1,792	1,826	1,876
Money and quasi-money (M2)	2,756	2,838	2,944	2,866	2,904	3,019	3,201	3,181	3,250	3,233	3,386	3,450	3,544
M2 plus resident foreign currency deposits (M3)	3,338	3,415	3,564	3,473	3,524	3,661	3,864	3,843	3,991	3,986	4,297	4,379	4,358
M3 plus nonbank holdings of government debt (L)	4,557	4,697	4,896	4,865	4,927	5,180	5,416	5,520	5,743	5,736	6,183	6,301	6,271
Memorandum items													
	(growth in percent yoy, excluding multipliers and velocity)												
M2	8.0	10.8	9.8	6.7	5.4	6.4	8.7	11.0	11.9	7.1	5.8	8.5	9.0
M3	10.1	12.5	9.2	6.5	5.6	7.2	8.4	10.7	13.2	8.9	11.2	13.9	9.2
Deposits	10.6	12.9	8.1	8.8	7.1	8.4	10.8	9.0	12.0	7.5	10.1	13.1	9.2
Reserve money	12.1	9.1	2.5	-9.4	-6.3	-2.4	-2.9	10.9	1.9	6.6	10.3	13.7	9.1
Net domestic credit	4.6	13.9	7.8	8.7	7.3	8.0	11.9	13.6	17.1	16.8	9.6	11.7	6.7
Government (net)	13.6	54.3	19.5	16.1	9.7	7.5	26.0	33.7	42.7	41.7	14.1	20.7	3.6
Private	2.4	4.3	5.2	7.0	7.1	8.9	7.7	7.6	8.4	7.6	7.7	7.8	8.1
Net domestic assets of the banking sector	4.4	15.3	4.7	4.7	3.7	7.3	13.5	17.3	19.3	15.5	16.4	18.2	11.7
NDA growth (as percent of the base period M3)	2.7	8.6	2.7	2.7	2.1	4.2	7.2	9.4	10.7	8.7	9.0	10.2	6.6
Multiplier (Average M2/RM)	6.0	6.0	6.1	6.3	6.5	6.7	6.9	6.9	7.0	7.1	7.0	6.9	6.9
Multiplier (Average M3/RM)	7.2	7.3	7.4	7.7	7.9	8.1	8.3	8.3	8.6	8.6	8.6	8.6	8.6
Velocity (GDP/M2)	3.3	3.3	3.3	3.3	3.4	3.4	3.4	3.4	3.3	3.3	3.3	3.3	3.3
Velocity (GDP/M3)	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.8	2.7	2.7	2.6	2.6	2.7

Sources: Kenyan authorities and IMF staff estimates and projections.

Table 4a. Kenya: Balance of Payments, 2017–25
(BPM6 presentation, in millions of U.S. dollars, unless otherwise indicated)

	2017	2018	2019	2020	2021	2022	2023	2024	2025
	Actual		Est.		Projections				
Current account	-5,685	-5,048	-5,552	-4,744	-5,649	-6,099	-6,647	-7,265	-7,857
Trade balance	-10,186	-10,201	-10,679	-8,377	-10,170	-11,519	-12,857	-14,384	-15,847
Goods: exports, f.o.b.	5,801	6,088	5,872	6,035	7,068	7,776	8,650	9,597	10,583
Coffee	230	232	205	209	247	281	313	336	364
Tea	1,424	1,370	1,115	1,248	1,362	1,465	1,591	1,743	1,903
Horticulture	829	1,055	991	1,097	1,390	1,527	1,675	1,854	2,007
Other	3,319	3,431	3,560	3,481	4,069	4,504	5,070	5,663	6,309
Goods: imports, f.o.b.	15,987	16,289	16,551	14,412	17,239	19,296	21,507	23,980	26,430
Oil products	2,727	3,386	3,310	2,468	3,763	3,939	4,119	4,387	4,687
Other	13,260	12,902	13,242	11,944	13,476	15,356	17,388	19,593	21,742
Capital imports	4,678	4,540	4,686	4,100	4,633	5,276	6,025	6,837	7,614
Services balance	1,556	1,596	1,767	239	488	874	1,174	1,530	1,839
Services, credit	4,648	5,477	5,621	3,834	4,840	5,555	6,349	7,193	8,077
Transportation	1,624	1,960	2,200	1,053	1,679	2,032	2,460	2,851	3,265
Travel	916	1,073	1,007	419	588	731	867	1,070	1,266
Services, debit	3,092	3,881	3,854	3,595	4,351	4,680	5,175	5,663	6,238
Transportation	1,032	1,397	1,448	1,172	1,500	1,679	1,872	2,087	2,300
Goods and services balance	-8,630	-8,605	-8,912	-8,138	-9,682	-10,645	-11,683	-12,854	-14,008
Primary income, balance	-1,509	-1,449	-1,925	-1,579	-1,979	-2,077	-2,224	-2,291	-2,352
Credit	141	199	218	-3	99	157	182	192	371
Debit	1,650	1,648	2,144	1,576	2,078	2,235	2,406	2,483	2,722
Secondary income, balance	4,454	5,006	5,285	4,973	6,012	6,623	7,260	7,880	8,502
Credit	4,510	5,054	5,340	5,025	6,064	6,678	7,318	7,942	8,568
Remittances	1,947	2,697	2,796	3,094	3,434	3,862	4,255	4,547	4,944
Debit	56	48	55	51	52	55	58	62	66
Capital account	184	263	208	130	382	392	396	392	406
Financial account	-5,558	-6,535	-6,239	-3,535	-3,150	-5,366	-5,958	-7,529	-9,415
Foreign direct investment	-1,010	-1,463	-1,132	-244	-361	-478	-614	-780	-973
Direct investment, assets	257	164	205	155	165	166	166	179	186
Direct investment, liabilities	1,266	1,628	1,337	398	526	643	780	959	1,159
Portfolio investment	789	-627	-1,312	1,389	1,312	1,471	1,533	1,598	1,665
Portfolio investment, assets	665	1,082	955	1,202	1,370	1,533	1,600	1,669	1,742
Portfolio investment, liabilities	-124	1,708	2,268	-187	58	62	66	71	77
Equity and investment fund shares	-126	-293	14	-271	60	63	68	73	79
Debt securities	3	2,001	2,254	84	-2	-2	-2	-2	-2
o/w Eurobond issuance	750	2,000	2,100	0	0	0	0	2,000	0
Financial derivatives	4	11	-5	-9	0	0	0	0	0
Other investment	-5,342	-4,457	-3,789	-4,672	-4,101	-6,359	-6,877	-8,347	-10,108
Other investment, assets	180	920	573	1,012	835	807	885	842	845
Other investment, liabilities	5,523	5,377	4,362	5,684	4,936	7,166	7,762	9,189	10,952
Net errors and omissions	-175	-728	148	313	0	0	0	0	0
Overall balance ("+" indicates a surplus)	-117	1,022	1,042	-765	-2,116	-341	-293	657	1,964
Reserves and related items	-117	1,022	1,042	-765	-2,116	-341	-293	657	1,964
Reserve assets (gross)	-236	876	889	-819	997	350	559	858	1,814
Use of Fund credit and loans (net)	-119	-146	-154	-53	848	424	601	201	-150
Disbursements (Proposed ECF/EFF Program) /1	0	0	0	0	979	503	646	232	0
Repayments	119	146	154	53	131	79	46	31	150
DSSI 2021H1 2/	0	0	0	0	639	0	0	0	0
Unidentified Financing 3/	0	0	0	0	0	268	252	0	0
Exceptional financing	0	0	0	0	1,625	0	0	0	0
Memorandum items:									
Gross official reserves (end of period)	7,150	8,144	9,116	8,284	9,280	9,630	10,189	11,047	12,861
(in months of next year's imports)	4.3	4.8	6.1	4.6	4.6	4.3	4.1	4.1	4.3
(in months of 3-year-rolling average imports) 4/	4.9	5.3	5.5	5.1	5.6	5.5	5.1	5.0	5.2
(in percent of M3)	23.6	24.4	25.9	21.3	21.3	20.0	19.0	18.5	19.4
WEO oil price (APSP; US\$)	52.8	68.3	61.4	41.3	58.5	54.8	52.5	51.3	50.7
Terms of trade 5/	3.4	3.3	2.6	9.4	-4.3	1.3	1.1	0.3	-0.2

Sources: Kenyan authorities and IMF staff estimates and projections.

1/ Past disbursements included to Other Investments.

2/ Debt service coming due in 2020H1. Assumes DSSI Modalities: one-year grace period; five-year repayment period.

3/ No DSSI debt service relief assumed in 2021H2 on debt service due to G20 creditors. Scheduled debt service to DSSI creditors in 2022 and 2023 assumes rollover rate of 90 percent.

4/ CBK definition of reserve cover: in months of imports of goods and services over the previous 36 months (annualized rolling average).

5/ Percentage change, goods and services.

Table 4b. Kenya: Balance of Payments, 2017–25
(BPM6 presentation, in percent of GDP)

	2017	2018	2019	2020	2021	2022	2023	2024	2025
	Actual			Est.	Projections				
Current account	-7.2	-5.7	-5.8	-4.8	-5.3	-5.4	-5.5	-5.6	-5.6
Trade balance	-12.9	-11.6	-11.2	-8.5	-9.6	-10.2	-10.6	-11.1	-11.3
Goods: exports, f.o.b.	7.3	6.9	6.2	6.1	6.7	6.9	7.2	7.4	7.5
Coffee	0.3	0.3	0.2	0.2	0.2	0.2	0.3	0.3	0.3
Tea	1.8	1.6	1.2	1.3	1.3	1.3	1.3	1.3	1.4
Horticulture	1.0	1.2	1.0	1.1	1.3	1.4	1.4	1.4	1.4
Other	4.2	3.9	3.7	3.5	3.8	4.0	4.2	4.4	4.5
Goods: imports, f.o.b.	20.2	18.5	17.4	14.5	16.3	17.1	17.8	18.4	18.8
Oil products	3.5	3.9	3.5	2.5	3.5	3.5	3.4	3.4	3.3
Other	16.8	14.7	13.9	12.1	12.7	13.6	14.4	15.1	15.5
Capital imports	5.9	5.2	4.9	4.1	4.4	4.7	5.0	5.3	5.4
Services balance	2.0	1.8	1.9	0.2	0.5	0.8	1.0	1.2	1.3
Services, credit	5.9	6.2	5.9	3.9	4.6	4.9	5.3	5.5	5.8
Transportation	2.1	2.2	2.3	1.1	1.6	1.8	2.0	2.2	2.3
Travel	1.2	1.2	1.1	0.4	0.6	0.6	0.7	0.8	0.9
Services, debit	3.9	4.4	4.0	3.6	4.1	4.2	4.3	4.4	4.4
Transportation	1.3	1.6	1.5	1.2	1.4	1.5	1.5	1.6	1.6
Goods and services balance	-10.9	-9.8	-9.3	-8.2	-9.1	-9.4	-9.7	-9.9	-10.0
Primary income, balance	-1.9	-1.7	-2.0	-1.6	-1.9	-1.8	-1.8	-1.8	-1.7
Credit	0.2	0.2	0.2	0.0	0.1	0.1	0.2	0.1	0.3
Debit	2.1	1.9	2.2	1.6	2.0	2.0	2.0	1.9	1.9
Secondary income, balance	5.6	5.7	5.5	5.0	5.7	5.9	6.0	6.1	6.1
Credit	5.7	5.8	5.6	5.1	5.7	5.9	6.1	6.1	6.1
Remittances	2.5	3.1	2.9	3.1	3.2	3.4	3.5	3.5	3.5
Debit	0.1	0.1	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Capital account	0.2	0.3	0.2	0.1	0.4	0.3	0.3	0.3	0.3
Financial account	-7.0	-7.4	-6.5	-3.6	-3.0	-4.8	-4.9	-5.8	-6.7
Foreign direct investment	-1.3	-1.7	-1.2	-0.2	-0.3	-0.4	-0.5	-0.6	-0.7
Direct investment, assets	0.3	0.2	0.2	0.2	0.2	0.1	0.1	0.1	0.1
Direct investment, liabilities	1.6	1.9	1.4	0.4	0.5	0.6	0.6	0.7	0.8
Portfolio investment	1.0	-0.7	-1.4	1.4	1.2	1.3	1.3	1.2	1.2
Portfolio investment, assets	0.8	1.2	1.0	1.2	1.3	1.4	1.3	1.3	1.2
Portfolio investment, liabilities	-0.2	1.9	2.4	-0.2	0.1	0.1	0.1	0.1	0.1
Equity and investment fund shares	-0.2	-0.3	0.0	-0.3	0.1	0.1	0.1	0.1	0.1
Debt securities	0.0	2.3	2.4	0.1	0.0	0.0	0.0	0.0	0.0
o/w Eurobond issuance	0.0	2.3	2.2	0.0	0.0	0.0	0.0	1.5	0.0
Financial derivatives	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Other investment	-6.8	-5.1	-4.0	-4.7	-3.9	-5.6	-5.7	-6.4	-7.2
Other investment, assets	0.2	1.0	0.6	1.0	0.8	0.7	0.7	0.6	0.6
Other investment, liabilities	7.0	6.1	4.6	5.7	4.7	6.4	6.4	7.1	7.8
o/w Public commercial borrowing	1.3	1.1	1.6	0.6	1.1	1.1	0.5	0.5	1.0
Net errors and omissions	-0.2	-0.8	0.2	0.3	0.0	0.0	0.0	0.0	0.0
Overall balance ("+" indicates a surplus)	-0.1	1.2	1.1	-0.8	-2.0	-0.3	-0.2	0.5	1.4
Reserves and related items	-0.1	1.2	1.1	-0.8	-2.0	-0.3	-0.2	0.5	1.4
Reserve assets (gross)	-0.3	1.0	0.9	-0.8	0.9	0.3	0.5	0.7	1.3
Use of Fund credit and loans (net)	-0.2	-0.2	-0.2	-0.1	0.8	0.4	0.5	0.2	-0.1
Disbursements (Proposed ECF/EFF Program) 1/	0.0	0.0	0.0	0.0	0.9	0.4	0.5	0.2	0.0
Repayments	0.2	0.2	0.2	0.1	0.1	0.1	0.0	0.0	0.1
DSSI 2/	0.0	0.0	0.0	0.0	0.6	0.0	0.0	0.0	0.0
Unidentified Financing 3/	0.0	0.0	0.0	0.0	0.0	0.2	0.2	0.0	0.0
Exceptional financing	0.0	0.0	0.0	0.0	1.5	0.0	0.0	0.0	0.0
Memorandum items:									
Gross official reserves (end of period)	9.0	9.3	9.6	8.4	8.8	8.5	8.4	8.5	9.2
Exports of goods and nonfactor services	13.2	13.2	12.1	10.0	11.2	11.8	12.4	12.9	13.3
Imports of goods and nonfactor services	24.1	23.0	21.4	18.2	20.4	21.3	22.1	22.8	23.3

Sources: Kenyan authorities and IMF staff estimates and projections.

Table 5. Kenya. Financial Soundness Indicators of the Banking Sector,
March 2019–December 2020

	Mar-19	Jun-19	Sep-19	Dec-19	Jan-20	Feb-20	Mar-20	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20
Capital adequacy																
Regulatory capital to risk-weighted assets	18.4	18.2	18.3	18.8	18.9	18.7	18.5	18.4	18.5	18.5	18.4	18.4	18.2	17.6	18.2	19.2
Regulatory tier 1 capital to risk-weighted assets	16.7	16.5	16.3	16.8	17.0	16.6	16.4	16.3	16.3	16.4	16.4	16.3	16.3	15.7	16.2	16.7
Total capital to total assets	14.3	14.1	14.2	14.8	15.1	14.7	14.5	14.5	14.4	14.2	14.0	14.1	14.2	14.2	13.9	14.6
Asset quality																
Non-performing loans to total gross loans ¹	12.8	12.7	12.4	12.0	12.2	12.7	12.5	13.1	13.0	13.1	13.3	13.6	13.6	13.5	13.7	14.1
Bank provisions to NPLs	61.9	62.5	65.8	62.9	66.9	65.3	66.1	64.8	66.3	67.3	67.7	68.5	70.4	72.4	54.8	55.4
Non-performing loans net of provisions to capital	19.2	18.9	17.2	16.1	15.6	16.9	16.7	18.0	17.3	16.9	17.0	16.9	15.9	14.8	14.5	15.3
Earning assets to total assets	91.2	90.5	91.3	91.9	93.3	92.2	92.1	92.6	92.8	91.6	92.8	93.4	93.8	94.4	94.0	93.6
Earning and profitability																
Return on assets (ROA)	2.9	2.8	2.7	2.5	2.6	2.3	2.3	2.1	1.9	0.7	1.8	1.8	1.8	1.8	1.7	1.6
Return on equity (ROE)	24.6	23.8	22.5	21.2	20.8	19.6	20.4	18.0	17.0	15.6	15.8	15.5	15.1	14.8	14.5	13.8
Interest margin to gross income	24.9	24.8	24.4	25.2	25.2	24.2	24.1	23.8	24.1	24.1	23.7	23.7	23.6	23.6	23.7	23.6
Non-interest expenses to gross income	40.3	41.4	42.6	43.9	43.9	44.8	46.3	45.9	49.3	51.4	51.2	48.5	52.6	52.7	53.1	54.6
Liquidity																
Liquid assets to total assets	39.8	39.6	38.5	39.3	39.9	40.2	39.8	40.3	40.4	41.9	42.1	42.2	41.5	43.4	42.4	42.5
Liquid assets to short-term liabilities	51.2	50.6	50.9	49.7	49.8	51.1	51.4	51.2	51.3	52.8	53.9	53.2	53.2	53.3	53.3	54.6
Liquid assets to total deposits	53.6	53.1	52.9	53.2	54.1	54.5	53.8	54.1	54.4	55.6	56.1	56.8	55.8	56.2	56.8	57.1
Total loans to total deposits	75.7	75.4	79.2	77.7	77.5	76.6	77.0	76.3	76.5	74.2	72.4	74.9	75.3	74.6	74.4	74.3
Sensitivity to market risk																
Net open position in foreign exchange to capital	1.6	2.9	1.9	1.7	1.4	1.5	1.7	1.6	2.3	1.8	1.8	1.8	2.3	2.2	1.9	1.6
Interest bearing assets to interest bearing liabilities	122.7	121.2	125.5	124.4	126.7	124.8	124.4	124.3	125.0	121.6	123.6	125.9	126.1	125.6	125.8	125.6
FX currency denominated assets to total assets	15.1	15.2	15.4	15.1	15.4	15.4	15.8	16.0	16.0	15.6	15.6	15.7	15.3	17.6	15.3	15.3
FX currency denominated liabilities to total liabilities	23.5	23.9	24.5	24.4	24.4	24.6	24.7	25.3	25.1	24.3	24.4	24.5	24.1	25.2	25.8	26.4
Spread between lending and deposit rate	6.1	5.9	5.5	5.6	5.6	5.6	5.6	5.5	5.4	5.5	5.4	5.4	5.3	5.4	5.4	5.5

Source: Central Bank of Kenya.

¹The data for Chase Bank in receivership and Charterhouse Bank under statutory management have been excluded from May 2016 onward.

Table 6. Kenya: Proposed Schedule of Approval, Prospective Reviews and Available Purchases and Loans, 2021–24

Availability Date	Condition	Available Purchases under GRA			Available Loans under PRGT			Total Available Purchases and Loans		Total Available USD millions
		SDR millions	Percent of quota	USD millions	SDR millions	Percent of quota	USD millions	SDR millions	Percent of quota	
April 2, 2021	Approval of the 38-month EFF and ECF arrangements	141.13	26.00	203.56	75.99	14.00	109.61	217.12	40.00	313.17
June 20, 2021	Completion of the first EFF-ECF reviews and observance of continuous and end-March 2021 performance criteria.	198.12	36.50	285.77	86.85	16.00	125.27	284.97	52.50	411.04
November 7, 2021	Completion of the second EFF-ECF reviews and observance of continuous and end-June 2021 performance criteria.	135.70	25.00	195.73	48.85	9.00	70.46	184.55	34.00	266.20
May 7, 2022	Completion of the third EFF-ECF reviews and observance of continuous and end-December 2021 performance criteria.	141.13	26.00	203.56	38.00	7.00	54.81	179.13	33.00	258.38
November 7, 2022	Completion of the fourth EFF-ECF reviews and observance of continuous and end-June 2022 performance criteria.	135.70	25.00	195.73	38.00	7.00	54.81	173.70	32.00	250.54
May 7, 2023	Completion of the fifth EFF-ECF reviews and observance of continuous and end-December 2022 performance criteria.	181.84	33.50	262.28	43.42	8.00	62.63	225.26	41.50	324.92
November 7, 2023	Completion of the sixth EFF-ECF reviews and observance of continuous and end-June 2023 performance criteria.	184.55	34.00	266.20	43.42	8.00	62.63	227.97	42.00	328.82
May 7, 2024	Completion of the seventh EFF-ECF reviews and observance of continuous and end-December 2023 performance criteria.	130.27	24.00	187.90	32.56	6.00	46.96	162.83	30.00	234.87
Total		1,248.44	230.00	1,800.75	407.09	75.00	587.19	1,655.53	305.00	2,387.93

Source: IMF staff estimates.

Table 7. Kenya: Indicators of Fund Credit, 2021–30

	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030
Fund obligations based on existing credit										
(In millions of SDRs)										
Total	80.4	50.5	21.7	0.1	54.4	108.7	108.7	108.7	108.7	54.4
Principal	80.3	50.3	21.6	0.0	54.3	108.6	108.6	108.6	108.6	54.3
Charges and interest	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Obligations to the Fund from existing and prospective credit										
(In millions of SDRs)										
Principal	80.4	50.5	21.7	0.1	82.7	215.9	295.3	367.8	394.9	343.9
Charges and interest	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
SDR Assessments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
SDR Charges	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
GRA Charges	1.7	5.7	8.8	12.4	13.1	12.6	11.6	9.9	7.8	5.6
GRA Surcharges	0.0	0.0	0.0	3.2	4.6	3.7	1.7	0.0	0.0	0.0
GRA Service Charges	2.4	1.4	1.8	0.7	0.0	0.0	0.0	0.0	0.0	0.0
Obligations to the Fund from existing and prospective credit										
In millions of U.S. dollars										
	113.8	71.4	30.7	0.2	117.0	305.4	417.7	520.3	558.7	486.5
In percent of gross international reserves										
	1.2	0.7	0.3	0.0	0.9	2.3	3.0	3.4	3.4	2.7
In percent of exports of goods and services										
	1.0	0.5	0.2	0.0	0.6	1.5	1.9	2.2	2.1	1.7
In percent of GDP										
	0.1	0.1	0.0	0.0	0.1	0.2	0.2	0.3	0.3	0.2
In percent of quota										
	14.8	9.3	4.0	0.0	15.2	39.8	54.4	67.8	72.8	63.4
Outstanding Fund credit based on existing drawings										
(end-of-period, all PRGT)										
In millions of SDRs	614.7	564.4	542.8	542.8	488.5	380.0	271.4	162.8	54.3	0.0
In percent of quota	113.2	104.0	100.0	100.0	90.0	70.0	50.0	30.0	10.0	0.0
Outstanding Fund credit based on existing and prospective drawings										
(end-of-period)										
In millions of SDRs	1,301.4	1,603.9	2,035.5	2,198.3	2,115.8	1,900.0	1,604.9	1,237.2	842.4	498.6
In millions of U.S. dollars	1,840.9	2,268.8	2,879.4	3,109.7	2,993.0	2,687.8	2,270.2	1,750.2	1,191.7	705.4
In percent of gross international reserves										
	19.8	23.6	28.3	28.1	23.3	20.5	16.0	11.5	7.3	4.0
In percent of exports of goods and services										
	15.5	17.0	19.2	18.5	16.0	13.2	10.2	7.3	4.6	2.5
In percent of GDP										
	1.7	1.9	2.2	2.2	2.0	1.6	1.3	0.9	0.6	0.3
In percent of quota										
	239.7	295.5	375.0	405.0	389.8	350.0	295.7	227.9	155.2	91.9
Memorandum items:										
Exports of goods and services (in billions of U.S. dollars)	11.9	13.3	15.0	16.8	18.7	20.3	22.2	24.1	26.2	28.4
Gross international reserves (in billions of U.S. dollars)	9.3	9.6	10.2	11.0	12.9	13.1	14.1	15.3	16.4	17.7
Debt service, existing drawings (in millions of U.S. dollars)	10,269	10,846	11,864	13,999	12,695	12,262	13,796	16,819	16,948	19,068
Quota (in millions of SDRs)	542.8	542.8	542.8	542.8	542.8	542.8	542.8	542.8	542.8	542.8
SDR per USD (as at September 28, 2020)	0.71	0.71	0.71	0.71	0.71	0.71	0.71	0.71	0.71	0.71

Sources: Fund staff estimates; and projections.

Table 8. Kenya: External Financing Requirements and Sources, 2018–25

	2018	2019	2020	2021	2022	2023	2024	2025
	Actual		Est.	Projected				
	(USD mn)							
Total requirements	6,715	8,374	6,357	7,570	8,146	8,674	11,365	10,276
Current account deficit	5,048	5,552	4,744	5,649	6,099	6,647	7,265	7,857
Capital outflows	1,667	2,821	1,613	1,921	2,047	2,027	4,101	2,419
Repayments of MLT loans (public sector)	1,503	1,867	1,458	1,756	1,881	1,861	1,922	2,233
Portfolio investment (sovereign bond)	0	750	0	0	0	0	2,000	0
Foreign direct investment abroad	164	205	155	165	166	166	179	186
Total sources	7,737	9,416	5,592	5,454	7,805	8,381	12,022	12,240
Public sector	8,195	7,761	3,941	3,830	4,099	3,650	6,244	5,384
Project grants	263	208	130	382	392	396	392	406
MLT loan disbursements to public sector	5,933	5,454	3,810	3,448	3,707	3,253	3,852	4,978
Portfolio investment (sovereign bond)	2,000	2,100	0	0	0	0	2,000	0
Private sector	-458	1,655	1,651	1,624	3,705	4,732	5,778	6,856
Foreign direct investment in Kenya	1,628	1,337	398	526	643	780	959	1,159
Other net flows (including errors and omissions)	-2,086	318	1,252	1,097	3,062	3,952	4,819	5,697
Financing gap (- = excess of financing)	-1,022	-1,042	765	2,116	341	293	-657	-1,964
Additional financing sources	-1,022	-1,042	765	2,116	341	293	-657	-1,964
IMF (net)	-146	-154	-53	848	424	601	201	-150
Disbursements (Proposed ECF/EFF Program) 1/	0	0	0	979	503	646	232	0
Repayments	146	154	53	131	79	46	31	150
Multilateral financing	0	0	0	1,625	0	0	0	0
DSSI 2/	0	0	0	639	0	0	0	0
Unidentified Financing 3/	0	0	0	0	268	252	0	0
Reserve accumulation(- = increase)	-876	-889	819	-997	-350	-559	-858	-1,814
	(percent of GDP)							
Total requirements	7.6	8.8	6.4	7.1	7.2	7.2	8.7	7.3
Total sources	8.8	9.9	5.6	5.1	6.9	6.9	9.2	8.7
Capital inflows	10.0	11.0	4.9	5.3	6.9	6.9	9.7	10.1
IMF (net)	-0.2	-0.2	-0.1	0.8	0.4	0.5	0.2	-0.1
Reserve accumulation (- = increase)	-1.0	-0.9	0.8	-0.9	-0.3	-0.5	-0.7	-1.3

Sources: Kenyan authorities and IMF staff estimates and projections.

1/ Past disbursements are included in MLT loans to government.

2/ Debt service coming due in 2020H1. Assumes DSSI modalities: one-year grace period; five-year repayment period.

3/ Scheduled debt service to DSSI creditors in 2022 and 2023 assumes rollover rate of 90 percent.

Annex I. Risk Assessment Matrix¹

Source of Risks	Likelihood /Time Horizon	Expected Impact on Economy	Policy Response
Potential External Shocks			
<p>Covid-19 resurgence</p> <p>Limited access to, and longer-than-expected deployment of vaccines in some countries—combined with dwindling policy space—prompt a reassessment of their growth prospects.</p>	<p>Medium Short to Medium Term</p>	<p>High. This could adversely impact growth, spur capital outflows from the private sector and pressure the exchange rate. Fiscal balances would worsen, including due to balance sheet scarring in the private sector, and debt vulnerabilities would rise further.</p>	<ul style="list-style-type: none"> ▪ Reprioritize spending to support the vulnerable while compressing overall expenditure to contain the negative fiscal-debt impact. ▪ Maintain exchange rate flexibility. ▪ Accelerate reforms to address structural weakness affecting competitiveness.
<p>Sharp rise in global risk premia exposes financial and fiscal vulnerabilities. A reassessment of market fundamentals (e.g., in response to adverse Covid-19 developments) triggers a widespread risk-off event. Financing difficulties extend to sovereigns with excessive public debt.</p>	<p>Medium Short to Medium Term</p>	<p>High. This could trigger capital outflows from the private sector and hamper capital market access by the sovereign. The exchange rate would depreciate, the fiscal balances would worsen, and debt vulnerabilities would rise further.</p>	<ul style="list-style-type: none"> ▪ Compress expenditure to contain the negative fiscal-debt impact. ▪ Maintain exchange rate flexibility.
<p>Oversupply and volatility in the oil market.</p>	<p>Medium Short to Medium Term</p>	<p>High. This would be a positive shock for Kenya, easing potential external balance pressures from other sources.</p>	<ul style="list-style-type: none"> ▪ If needed to meet fiscal objectives, capitalize on lower fuel prices by aligning fuel VAT to the standard rate.
<p>Cyber-attacks</p>	<p>Medium Short to Medium Term</p>	<p>Medium. Such attacks can trigger financial instability or widely disrupt socio-economic activities.</p>	<ul style="list-style-type: none"> ▪ Continue reforms to strengthen cyber security capabilities at both government and private sector level.
<p>Higher frequency and severity of natural disasters</p>	<p>Medium /Low Short to Medium Term</p>	<p>High. This would lead to slower growth, an increase in food inflation, pressures on public spending and the current account, and adversely affect vulnerable households.</p>	<ul style="list-style-type: none"> ▪ Guard against second-round effects on inflation. ▪ Use targeted programs to help vulnerable groups and reprioritize spending.

¹ The Risk Assessment Matrix (RAM) shows events that could materially alter the baseline path (the scenario most likely to materialize in the view of IMF staff). The relative likelihood is the staff's subjective assessment of the risks surrounding the baseline ("low" is meant to indicate a probability below 10 percent, "medium" a probability between 10 and 30 percent, and "high" a probability between 30 and 50 percent). The RAM reflects staff views on the source of risks and overall level of concern as of the time of discussions with the authorities. Non-mutually exclusive risks may interact and materialize jointly. "Short term" and "medium term" are meant to indicate that the risk could materialize within 1 year and 3 years, respectively

Source of Risks	Likelihood /Time Horizon	Expected Impact on Economy	Policy Response
Potential Domestic Shocks			
A resumption of adverse weather conditions or locust invasion	Medium Short Term to Medium Term	High / Low. Depending on the geographical area impacted this could lead to lower agricultural production and slower growth, an increase in food inflation, pressures on public spending and the current account, and adversely affect vulnerable households.	<ul style="list-style-type: none"> ▪ Use targeted programs to help vulnerable groups and reprioritize spending. ▪ Guard against second-round effects on inflation if necessary.
Political risks	Medium Short to Medium Term	High. Political violence could emerge around the planned 2021 referendum and 2022 presidential election as seen in previous elections.	<ul style="list-style-type: none"> ▪ Remain committed to reforms under the program.
Emergence of greater-than-expected weaknesses in the SOE sector	Medium Short to Medium Term	Medium. This would create additional fiscal pressures, potentially leading to further crowding out of the private sector, although the magnitude would be highly uncertain.	<ul style="list-style-type: none"> ▪ Carry out financial evaluation of health of top SOEs. ▪ Prepare and carry out strategy for addressing SOE financial pressures.
Deterioration in security situation	Medium Short to Medium Term	High. This would adversely affect recovery of the tourism sector, foreign direct investment and portfolio inflows and, in turn, growth.	<ul style="list-style-type: none"> ▪ Reprioritize fiscal spending to accommodate security needs; and ▪ Maintain policies to improve macro fundamentals (e.g., structural and governance reforms). ▪ Strengthen and robustly implement AML/CFT framework to help prevent, detect, and disrupt the financing of terrorism.
Risks from poor implementation capacity, fiscal pressures in the run-up to the election, and weak program ownership	Low Short to Medium Term	Medium. This would lead to higher budget deficits, which would increase debt ratios, crowd out private investment, and ultimately weaken growth.	<ul style="list-style-type: none"> ▪ Remain committed to fiscal targets and reforms under the program.

Annex II. External Sector Assessment

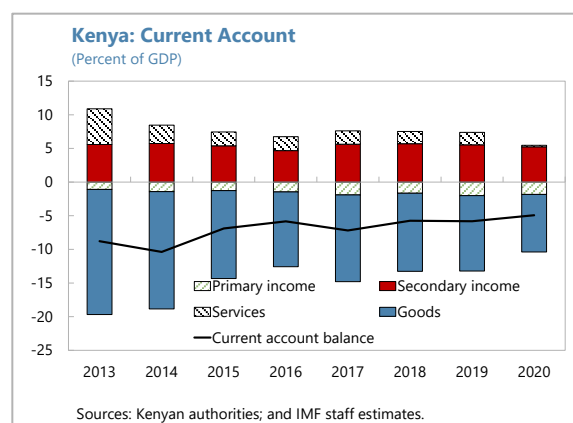
Kenya's overall external position in 2020 was broadly in line with the level implied by fundamentals and desirable policies. Fiscal consolidation under the proposed program supported by the EFF and ECF arrangements would help to strengthen Kenya's external sector position and support private sector growth with exchange rate flexibility allowing the economy to absorb external shocks. Further attention to improving Kenya's competitiveness would help curtail the recent decline of Kenya's share of world exports.

A. Current Account

1. Kenya's current account deficit amounted to 4.8 percent of GDP in 2020—one percentage point lower than in 2019 and below the 2015-19 average (6.3 percent of GDP). The

smaller current account (CA) deficit reflects an improved trade balance and deteriorated service account. Due to lower oil prices and domestic growth, imports in percent of GDP declined from 17.4 in 2019 to 14.5 in 2020; exports remained slightly above 6 percent of GDP in both years. The service account surplus observed in 2019 (1.9 percent of GDP) almost disappeared due to lower transportation and tourism receipts on account of the COVID-19 shock. The 2020 primary income deficit, which captures mainly interest payments on external debt, improved about 0.5 percent of GDP.

Remittances reached 3.1 percent of GDP—0.2 percentage points higher than in 2019, reflecting the strong positioning of the Kenyan diaspora in labor markets abroad, particularly in North America.



2. The CA deficit is projected to widen to 5.3 percent of GDP in 2021 and gradually increase to 5.6 percent of GDP over the medium term. Kenya's recovery from the COVID-19 shock and higher oil prices are shaping CA developments in 2021. While higher global growth will support higher exports, stronger domestic demand and higher oil prices are increasing imports across the board, leading to a wider current account deficit despite better tourism and transport receipts and remittances flows. Over the medium term, capital imports are expected to gradually increase reflecting improved domestic conditions. Oil imports are expected to remain around 3.5 percent of GDP, reflecting projected oil prices under the baseline. Export growth is supported by Kenya's improving business environment, key infrastructure projects coming to completion, and large potential in the agricultural sector. Services are projected to gradually increase over the medium term as the tourism sector return to normal after the COVID-19 shock. Remittances are also projected to gradually increase. CA projections under the baseline are subject to downside risks, particularly from weather conditions and commodity prices—which could affect food and oil imports.

3. The EBA-lite CA model indicates a CA gap of -0.3 percent of GDP in 2020. It is based on the estimated cyclically adjusted CA of -4.4 percent of GDP and a CA norm of -4.1 percent of GDP. The CA is assessed to be broadly in line with the level implied by fundamentals and policies in 2020. The contribution of policy gaps to the current account gap is 2.2 percent of GDP, with the fiscal deficit being the main contributor (1.6 percent of GDP). The positive gap captures the relatively larger world fiscal deficit compared with Kenya—10.3 percent of GDP compared with 8.5 percent of GDP, respectively. Informed by these developments the external balance is assessed to be broadly in line with the level implied by fundamentals and desirable policies.

Kenya: EBA-Lite Results, 2020		
(percent of GDP, unless otherwise indicated)		
	CA model	REER model
CA-Actual	-4.8	
Cyclically Adjusted CA	-4.4	
CA Norm (from model) ^{1/}	-4.1	
CA Gap	-0.3	-0.9
Elasticity	-0.09	
REER Gap (in percent)	3.0	9.1

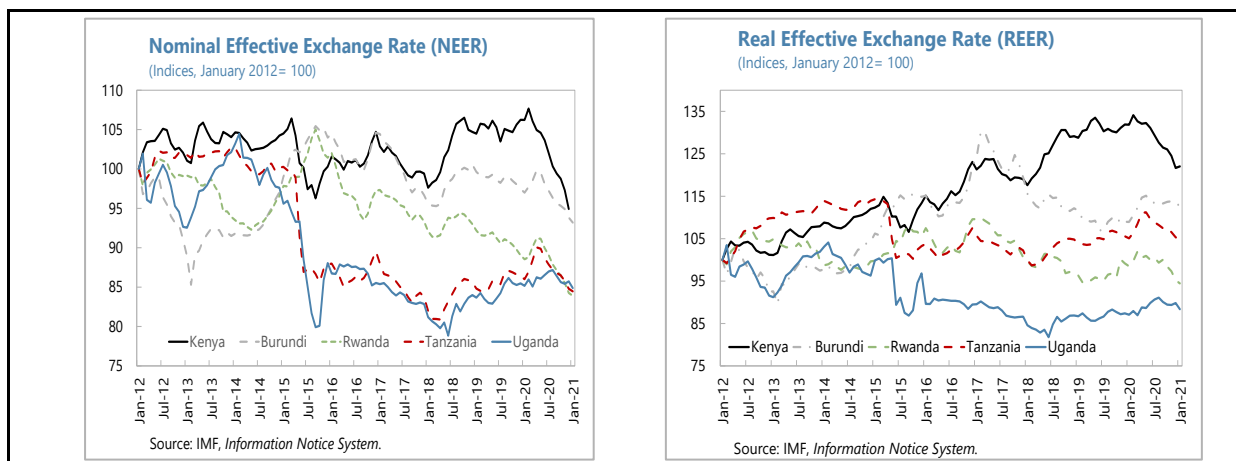
^{1/} Cyclically adjusted, including multilateral consistency adjustments.
Sources: Kenyan authorities and IMF staff calculations.

B. Real Exchange Rate

4. Kenya's real effective exchange rate (REER) has been on an appreciating trend in recent years. Despite a stable nominal effective exchange rate (NEER), relatively higher inflation rate than in trading partners had in recent years contributed to medium-term real appreciation, and Kenya's REER had appreciated more than its regional peers.¹ In 2020 the appreciating trend reversed, and the annual average REER depreciated slightly by 1.5 percent compared to 2019. Since March 2020 the REER has gradually depreciated as the exchange rate absorbed some of the impact of the COVID-19 shock, which has reduced sources of foreign exchange for Kenya. By December 2020, the REER had depreciated by about 8 percent compared with December 2019.

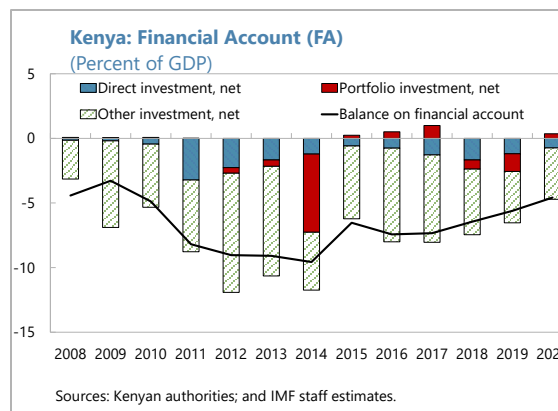
5. The EBA-lite REER model suggests a gap of 9.1 percent for 2020. The REER data used in the model is the Fund's standard REER index. Taking into account the results of the EBA-lite CA model, staff assesses the REER gap to be in the range of 3 percent and 9.1 percent.

¹ The United States, China, South Africa, United Kingdom, Japan, India, Germany, France, the United Arab Emirates, Uganda, Netherlands, Italy, Belgium, and Tanzania are the major trading (export) partners of Kenya. They together account for about 75 percent of Kenya's exports. For the purposes of Kenya's REER calculation, world inflation is a weighted average of the aforementioned countries' inflation indices.



C. Capital and Financial Accounts

6. In 2020, Kenya's current account deficit was largely financed by financial flows. Other net investment flows amounted to 4.7 percent of GDP, reflecting government borrowing, including IMF emergency support, as well as borrowing by other financial corporations (non-banks). Reflecting the impact of the COVID-19 shock on retained earnings, FDI net inflows reached only 0.2 point of GDP—one percentage point of GDP lower than in 2019. Volatility in global financial markets driven mainly by the COVID-19 shock reduced portfolio flows into Kenya, as well as the government's appetite for external commercial borrowing.



D. Reserve Adequacy and FX Intervention

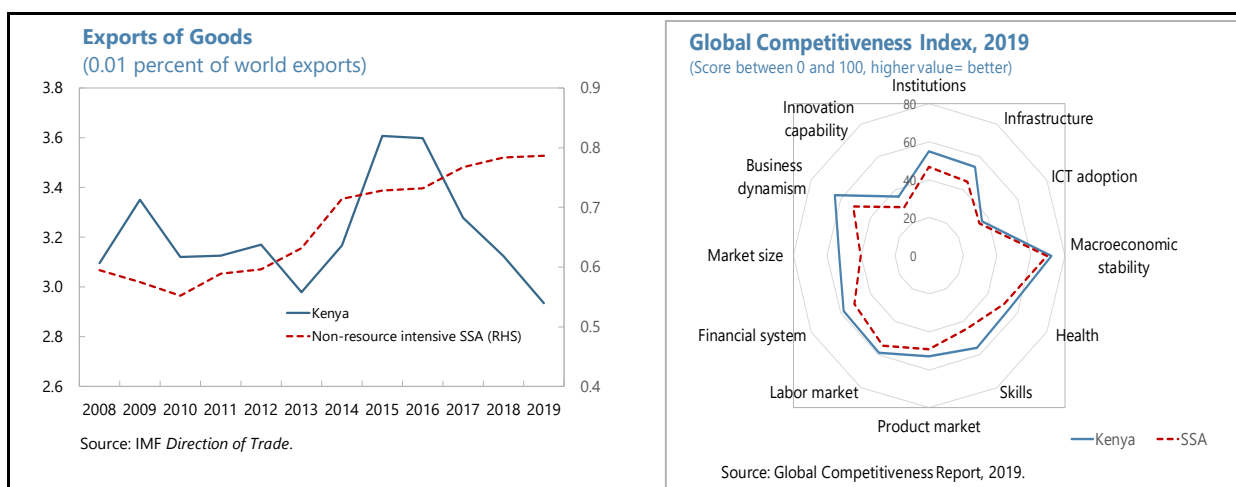
7. Reserve coverage seems comfortable. At end-2020, reserves stood at US\$8.4 billion, compared to US\$9.1 billion at end-2019. Reserve coverage was equivalent to 8.4 percent of GDP, about 4.6 months of next year's imports, and about 150 percent of the IMF's reserve adequacy metric for credit-constrained economies.²

8. Maintaining exchange rate flexibility would help the economy absorb potential shocks. The CBK engages in periodic FX interventions to smooth volatility in the Kenyan shilling. Given the CBK's credibility, well-anchored inflation expectations, and adequate reserve coverage, there is scope for greater exchange rate flexibility to absorb external shocks.

² The reserve adequacy metric for credit-constrained economies is calculated by measuring the benefit of holding reserves against the costs. The benefits are the lower probability of a crisis and the reduction in the severity of a crisis, while the cost is measured based on an economy's external funding costs. The model suggests that the optimal level of reserves for Kenya is 3.1 months of imports.

E. Competitiveness Measures

9. While export performance has been weak, Kenya continues to improve the business environment, suggesting a mixed picture with respect to developments in competitiveness. In the past, Kenya had a strong orientation to global markets as part of its development strategy. Exports of goods and services to GDP remained above 20 percent from 2001 to 2012 and averaged 19 percent during 1998-2020. In recent years, however, Kenya has suffered weak export performance. More recent data shows that Kenya has been losing market share since 2015, while the other non-resource intensive SSA countries were on average gaining market share. While Kenya has continued to implement reforms to facilitate the ease of doing business, Kenya's competitiveness rank slightly declined to 95 (from 93 in 2018) out of 141 economies in 2019 according to the World Economic Forum's Global Competitiveness Index.³ To support durable and inclusive medium-term growth, policies to strengthen competitiveness, including the business environment, will be part of the discussion agenda with the Kenyan authorities as part of the program under the EFF and ECF arrangements. Furthermore, increasing the efficiency in the use of public resources in connection with the agenda to address financial risks from SOEs should also enhance competitiveness.



³ In line with the Use of Third-Party Indicators in Fund Reports from 2017, we present scores for several indicators in a cross-country context. The World Economic Forum's Global Competitiveness Index is entirely based on survey data. The Global Competitiveness Report has been published annually since 2004 and provides information on 141 economies currently.

Annex III. Capacity Development Priorities

Kenya is a high-intensity capacity development (CD) country. CD focuses on tax policy and revenue administration, public financial management, monetary policy operations, the regulatory and supervisory framework for the financial sector, AML/CFT supervision and the functioning of the financial intelligence unit, and government finance, national accounts, and balance of payment statistics. Below are the priorities by department per the current Capacity Development Strategy Note.

CD Priorities		
Dept	Topics	Objectives
FAD	Public Financial Management	Comprehensive, credible, and policy-based budget preparation; improved PIM; improved coverage and quality of fiscal reporting; improved asset and liability management; strengthened identification, monitoring, and management of fiscal risks.
FAD	Revenue Administration	Strengthen revenue administration management and governance arrangements and core tax functions; and improve customs operations. Repeat TADAT review; redesign high net worth individuals function; develop capacity in digital services tax practices and assessment of legislative framework, processes and procedures; develop a framework for exports and imports data matching; customs monitoring of oil exports; and post clearance audit and risk management.
FAD	Tax Policy	Continue to advance agenda for reducing tax expenditures and broadening the tax base in line with Fund TA recommendations (e.g., by following up on modernization of the property tax) to reverse the declining trend of tax revenues. Undertake follow-up mission in FY21/22 to review progress in policy refinement, implementation, and revenue outcomes.
MCM	Financial Supervision and Regulation	Enhance risk-based supervision and Basel II/III implementation. Strengthen supervisory processes in non-banks.
MCM	Central Bank Operations	Continue to enhance the organizational risk management framework, including internal controls.
MCM	Monetary and Macroprudential Policy	Accelerate the modernization of the monetary policy framework and operations and integrate FPAS into monetary policy decision making. Develop and strengthen macroprudential policy tools (heatmaps, network analysis, financial soundness indicators, financial stability analysis tools).
STA	Government Finance Statistics	Monthly GFS (for budgetary central government), quarterly GFS (for central government), and annual GFS (for public sector) are compiled according to GFSM 2001/2014 and disseminated on a timely basis.
STA	Real Sector Statistics	New exports and imports indexes are compiled and published. Sector accounts are compiled and published.
LEG	Rationalization of SOE portfolio	Triage of SOE portfolio. Institutional centralization of the ownership function for SOEs.

Source: Kenya – Capacity Development Strategy Note.

Appendix I. Letter of Intent

Nairobi, Kenya
March 19, 2021

Ms. Kristalina Georgieva
Managing Director
International Monetary Fund
700 19th St, NW
Washington, DC 20431

Dear Ms. Georgieva:

The COVID-19 pandemic has been a shock of historic proportions, with major negative repercussions on the global population and economy. The disease has taken a devastating human toll and efforts to prevent its spread have required great sacrifices. Many lives have been lost and economies, including Kenya's, have been severely disrupted. As of end-January 2021, Kenya had recorded about 100 thousand cases and almost 1,800 fatalities in a population of over 50 million. While our capacity to combat COVID-19 has increased, the battle against the virus is not over as new cases have surged in March 2021. As a result, containment measures introduced last year have been partially lifted. We are also implementing measures to put the economy back on a path of robust, sustainable, and inclusive growth.

Our overall aim is to stabilize the economy and set a basis for a resurgence of growth and shared prosperity. In this regard, our economic program has four main objectives: (1) in the near term, ensure an effective COVID-19 response that maintains support for our health sector and those most impacted by the shock to the economy; (2) reduce debt vulnerabilities through a revenue-driven fiscal consolidation so that the ratio of public debt to GDP stabilizes and is put firmly on a downward path during the program; (3) advance the structural reform and governance agenda and address weaknesses in state-owned enterprises; and (4) strengthen the monetary policy framework and support financial stability.

To support these objectives, we wish to request 38-month arrangements under the Extended Fund Facility (EFF) and the Extended Credit Facility (ECF), with blended access at 305 percent of quota (SDR 1,655 million)—SDR 1,248 million (230 percent of quota) from the EFF arrangement and SDR 407 million (75 percent of quota) from the ECF arrangement—to be disbursed as budget support. Along with support from development partners and other financing sources, including from our participation in the G20 Debt Service Suspension Initiative, the proposed arrangements will fill our fiscal and external financing gaps as we embark on a multi-year consolidation effort.

The proposed arrangements include a series of quantitative performance criteria and indicative targets, with some of the indicative targets transitioning to performance criteria over the course of the program in recognition of the still elevated level of economic uncertainty resulting from the pandemic. It also includes a series of structural benchmarks covering reform actions that will bolster economic performance.

We believe that the policies and actions set out in the attached Memorandum of Economic and Financial Policies (MEFP) will enable us to achieve our program objectives. Should further measures be necessary, we will consult in advance with the IMF on their adoption, in accordance with applicable IMF policies. We are committed to working closely with IMF staff to ensure that the program is successful and will provide the IMF with the relevant information necessary for monitoring our progress.

We authorize the publication of this letter of intent, the attached MEFP, the technical memorandum of understanding, and the related staff report upon clearance with the authorities.

Sincerely yours,

/s/

Hon. (Amb.) Ukur Yatani, EGH
Cabinet Secretary
National Treasury & Planning

/s/

Dr. Patrick Njoroge, CBS
Governor
Central Bank of Kenya

Attachment I. Memorandum of Economic and Financial Policies

Nairobi, Kenya, March 19, 2021

I. BACKGROUND

1. This memorandum has been prepared against the backdrop of the unprecedented shock of the COVID-19 pandemic. The pandemic has upended lives and livelihoods across the world. Kenya has not been spared. While the overall spread of the disease in Kenya has been limited, with about 1.9 confirmed cases per 1,000 population and a fatality rate of less than 2 percent as of end-January 2021, COVID-19 remains a serious concern. The virus continues to spread and remains a major risk to public health. Moreover, the attendant economic disruption has caused widespread losses of income. Our development goals have suffered a significant setback, and we face an arduous task of returning to a path of sustained and inclusive growth.

2. Kenya's economy was performing strongly up to the onset of COVID-19. Real GDP growth averaged 5.8 percent in the decade up to 2019 and inflation was well contained. The external position was comfortable, with the current account deficit narrowing to 5.8 percent of GDP in 2019. Growth in credit to the private sector was picking up, buoyed by the removal in November 2019 of the interest rate cap that had been imposed in September 2016. Public debt had increased to 62.1 percent of GDP in 2019, owing to heavy infrastructure investments in previous years, but was expected to decline with efforts to reduce the fiscal deficit. Coming on the back of a locust outbreak and severe flooding in many parts of the country, the outbreak of COVID-19 in early 2020 was a devastating shock that has significantly altered the economic landscape.

3. Kenya moved quickly to contain the spread of COVID-19 and ramp up the capacity of its health system. An inter-ministerial committee was established in end-February 2020 to lead the country's COVID-19 response, two weeks before the first case was confirmed in the country. A series of containment measures were introduced in March 2020, including establishment of isolation facilities, quarantine of at-risk persons, travel restrictions, bans on large meetings, closure of schools and universities, and a country-wide nighttime curfew. Further measures, including restrictions on movement in and out of high-risk counties, were added in April. With continued efforts to strengthen treatment capacity, the number of isolation beds for infectious diseases was raised from a total of 8 at the start of March 2020 to 7,411 at end-September 2020.

4. Containment measures were eased as health sector capacity was raised. By mid-2020, a gradual reopening of the economy was underway. In successive steps since early July, the nighttime curfew was shortened, local and international flights resumed, and limits on attendance at public gatherings were relaxed. Schools and universities started to reopen in October and reopened fully in January 2021. The relaxation of containment measures has been cautious, however, and adjustments have been made according to the evolution of the disease. A second wave of COVID-19 cases that peaked in early November necessitated some tightening of movement restrictions. Current containment measures include a 10pm to 4am curfew, restrictions on operating practices of bars and restaurants, and caps on attendance at various types of gatherings.

5. The economy was hard hit at the onset of the pandemic but is now recovering.

Disruptions to international trade and transport and curtailment of normal activity had a marked negative impact on the economy. In 2020Q2, real GDP contracted by 5.5 percent year-on-year, led by an 83 percent decline in accommodation & food services and a 56 percent decline in education. Services overall contracted by 11.7 percent. The secondary sector contracted by 1 percent, driven by a 3.9 percent decline in manufacturing. Since the third quarter, however, economic activity has generally been picking up along with the relaxation of COVID-19 containment measures. With a rebound in industry and services, real GDP growth turned positive quarter-on-quarter and the year-on-year rate rose to -1.1 in 2020Q3. Agriculture, which has benefitted from above-average rainfall, maintained strong growth of 6–7 percent through the year. Manufacturing, one of the hardest hit sectors, has started showing signs of recovery as evident in some of the leading economic indicators.

6. Inflation has remained within the target range (5 ± 2.5 percent), as disruption to supply chains from COVID-19 was limited and did not translate into significant price pressures.

Over the past year, the y/y rate of headline inflation has ranged between 7.4 percent and 4.2 percent, with the 5.7 percent y/y rate in January 2021 being close to the average rate of 5.2 percent in 2019 and 5.4 percent in 2020. The broadly stable headline inflation over the past year was supported by reduced food price inflation in the first half of 2020, resulting from the strong performance of agriculture, which compensated for an increase in fuel prices. Non-food/non-fuel inflation has remained relatively low at consistently under 3 percent over the past year.

7. The external sector has generally been resilient. Buoyed by robust performance of agricultural products, especially tea and non-flower horticulture, goods exports in 2020 rose by 3.3 percent compared to 2019. Over the same period, imports declined by 12.5 percent mainly due to lower oil prices. Remittances have held up well, rising by 10.7 percent in 2020, despite the global downturn. These developments helped compensate for a sharp drop in income from travel services, which was heavily impacted by the cessation of international passenger travel from late March to the start of August. As a result, the current account deficit narrowed to an estimated 4.8 percent of GDP in 2020 from 5.8 percent in 2019. The resilience of the external sector has supported the shilling, which compared to other frontier market currencies depreciated by a relatively modest 9.5 percent against the US dollar over the 12 months to end-January. Moreover, the flexible exchange rate regime allowed the foreign exchange market to cope with the extreme COVID-19 shock. The bulk of the exchange rate movement took place in March 2020 when international market disruptions spiked due to COVID-19 related uncertainties. Reserves have remained adequate throughout the year (4.71 months of imports at end-January).

8. Enhancing the use of digital platforms. Following consultations between the Central Bank of Kenya (CBK), authorized Payment Service Providers (PSPs) and commercial banks, limits on mobile money transactions were enhanced and charges on low value transactions (of up to Ksh 1,000) eliminated in March 2020. The measures were in effect until end-2020. These temporary measures supported a notable increase in both transaction volumes and values of low value transactions and transfers between bank and mobile e-wallets. This comes against the backdrop of a gradual shift

towards digital platforms and less utilization of physical access channels. Transactions outside bank branches have increased from 90 percent before the pandemic to over 94 percent during the pandemic. Further, an additional 2.8 million Kenyans, or 10 percent of the active mobile money subscription base, are now using mobile money following the measures. Moreover, mobile money has been the backbone for the cash transfer during the pandemic, with mobile money accounts held by more than double the adult population.

9. Notwithstanding borrowers' reduced income, the banking system remains well-capitalized, profitable, and liquid. Banks overall were on a solid footing ahead of COVID-19, with strong liquidity and capital buffers thanks to earlier reforms in prudential regulations that have helped them build resilience to absorb the shock. Recognizing the need for an early and proactive response, the Central Bank of Kenya (CBK) acted in March 2020 to support the economy and offset the contractionary impact of the pandemic by easing monetary conditions and providing liquidity to ensure the continued effective functioning of local money markets. The Central Bank Rate (CBR) was reduced by 125 bps, from 8.25 percent to 7.25 percent in March and further to 7.0 percent in April and the Cash Reserve Ratio was reduced by 100 bps, while the maximum tenor on liquidity-injecting reverse repo instruments was increased from 28 to 90 days. These steps have secured the good functioning of Kenya's domestic markets while the health of the financial sector has been preserved: the capital adequacy ratio and liquidity ratio have remained at healthy levels: 19.2 percent and 54.6 percent, respectively, at end-December. Deposits grew by 13.2 percent in the year to December and the interbank rate has remained mostly in the 2-6 percent range since June. At the same time, the ratio of non-performing loans increased from 12.3 percent in February to 14.1 percent in December. Increases in NPLs were noted in the transport and communications, trade, real estate, and agriculture sectors mainly due to the subdued business environment. Banks continue to make provisions for NPLs. Banks' return on equity declined from 19.6 percent in February to 13.8 percent in December.

10. A large proportion of borrowers have benefited from temporary relief on their outstanding loans, considerably easing financial constraints from the shock. In order to support businesses and households impacted by the pandemic, the CBK encouraged banks to restructure the loans for borrowers who were current on their payments before the onset of the pandemic. By end-December 2020, relief measures were provided to borrowers accounting for 54.2 percent of the banking system's gross loans in form of three, six and twelve months of moratoria (either interest or both principal and interest payments) considering borrower-specific circumstances. One-fifth of restructured loans were personal loans, with forty percent of all personal loans benefitting from this relief. Among restructured business loans, trade, manufacturing, real estate and agriculture were the largest beneficiaries. About 90 percent of total relief was extended by large banks. The CBK is closely monitoring the implications of loan restructuring on banks' earnings and capital but the impact has been contained so far.

11. The impact of the pandemic on government finances has been severe. Before the onset of COVID-19, the overall deficit had started to narrow, with total revenue growth outstripping expenditure growth (y/y changes of 13.7 percent and 10.8 percent, respectively, in the 12 months to

February 2020). The Budget Policy Statement from February 2020 accordingly projected a deficit of 6.3 percent of GDP for FY2019/20, down from 7.7 percent of GDP in FY2018/19. The picture changed markedly after the onset of COVID-19, with a sharp downturn in revenue and new expenditure requirements leading to a deficit of 7.8 percent of GDP in FY2019/20 despite scaling back on non-COVID-related spending. The impact has extended into FY2020/21. During April-December 2020, total revenue fell by 15.8 percent y/y, with large reductions across most tax types. At the same time, expenditure contracted by 2.6 percent y/y as we prioritized spending to the most vulnerable groups and parts of the economy while making savings elsewhere.

12. The lower revenue is partly the result of tax cuts to assist the private sector. The Tax Amendment Act introduced in April 2020 cut the standard corporate income tax rate from 30 to 25 percent; almost doubled the tax-free threshold (to about \$225 per month) and reduced the top rate from 30 to 25 percent under the personal income tax; reduced the standard VAT rate from 16 to 14 percent; and reduced the turnover tax on small businesses from 3 to 1 percent. These tax cuts provided significant relief to taxpayers and helped limit the dislocation of private sector activity. Without this stimulus, the economic downturn seen in the second quarter would likely have been significantly worse. We estimate the cost of these tax cuts at 1.9 percent of GDP on a full-year basis, corresponding to roughly 10 percentage points of the decline in revenue observed since April. It should be noted, however, that the disruption to the economy means that such estimates are subject to more uncertainty than would normally be the case.

13. To strengthen government finances and enhance the efficiency of the tax system, we have taken a series of revenue-enhancing measures in line with Fund recommendations. The Tax Amendment Act from April removed multiple tax exemptions and incentives, principally under the VAT and corporate income tax, for a full-year impact of 0.8 percent of GDP. Additional tax exemptions and new revenue measures were introduced in the Finance Act 2020 from June for a full-year impact of 0.4 percent of GDP. The main component here is a minimum alternative tax under the corporate income tax, levied at 1 percent of turnover that became effective on January 1, 2021, with an expected full-year yield of 0.2 percent of GDP. This tax will reduce the scope for tax avoidance and tax evasion, helping ensure that everyone pays their fair share.

14. On the spending side, we have as part of our COVID-19 response allocated funds to support the health sector, protect vulnerable groups, and stimulate activity in key areas. This included Ksh 40 billion (0.4 percent of GDP) in COVID-related interventions introduced as part of a supplementary budget for FY2019/20 and a Ksh 58 billion (0.5 percent of GDP) stimulus package in the FY2020/21 budget. The first of these packages focused on resourcing the health sector, providing liquidity support to businesses through accelerated payment of VAT refunds and pending bills, and cash transfers to urban poor. The second package focused on stimulating activity in hard-hit sectors, with an emphasis on creating youth employment.

15. IMF support has greatly assisted our COVID-19 response. The Rapid Credit Facility from May (100 percent of quota, USD 739 million) helped see us through the initial phase of the shock. In line with commitments in our letter of intent of April 30, the use of RCF resources and other COVID-related spending has been carefully and transparently accounted for as at end-June 2020,

72 percent of the funds had been utilized, and the remainder was used in the second half of 2020. The funds were used to support COVID-19 interventions of the Ministry of Health (27 percent); transfer payments by the State Department for Social Protection (22 percent); a youth employment program (13 percent); liquidity support to businesses, including payment of VAT refunds (13 percent) and pending bills (15 percent); and other COVID-related interventions (10 percent). A comprehensive audit by the Auditor General of all COVID-related spending in FY2019/20 is underway and the results will be published by end-May 2021 (structural benchmark).

16. With the pandemic still ongoing and the economy remaining under significant pressure, we are now requesting 38-month arrangements under the Extended Fund Facility (EFF) and the Extended Credit Facility (ECF) to support the next phase of our COVID-19 response. The Fund-supported program will direct resources to priority areas and over time reduce debt vulnerabilities through a multi-year fiscal consolidation. The arrangements (305 percent of quota, disbursed as budget support) would fill fiscal and external financing gaps and anchor macroeconomic stability as we implement our economic program.

II. MACROECONOMIC OUTLOOK

17. Our baseline outlook is for a gradual recovery in economic activity from the trough in the second quarter of 2020, with negative output gaps lasting into early 2021. This outlook is predicated on a path for the global economy in line with projections in the January 2021 World Economic Outlook Update. Depending as it does on the evolution of the pandemic, the outlook is subject to large uncertainty.

- Economic growth is projected to recover gradually from the sharp drop in the second quarter of 2020. Our program framework assumes conservatively that real GDP will contract by 0.1 percent in 2020. Growth in 2021 is projected at 7.6 percent, partly driven by a rebound in education as schools started to reopen in 2020Q4 and opened fully at the start of 2021. Over the medium term, growth is projected to settle at about 6 percent, with a slightly increasing trend as the program anchors confidence and boosts investment and lending to the private sector. Inflation is projected to remain near the mid-point of the CBK target range in 2020 and through the medium term.
- The key aim of the program is to reduce the fiscal deficit and over time put the ratio of public debt to GDP on a downward trajectory. In recognition of continued near-term pressures, including the need to maintain support for our healthcare response to the pandemic and programs targeted at those most impacted by the shock to our economy, as well as depressed revenue and costs associated with state-owned enterprises (SOEs), the program targets a deficit of 8.7 percent of GDP in FY2020/21. With strengthening revenue and contained spending, the deficit is then expected to decline gradually to 4.3 percent of GDP in FY2023/24. The ratio of public debt to GDP is expected to peak at 73.0 percent in FY2022/23 and then start declining.
- The fiscal adjustment and accompanying structural reforms would free up space for banks to finance private credit and investment, improve market sentiment, and protect productivity-

enhancing development spending. The external current account is projected to widen modestly from 4.8 percent of GDP in 2020 to 5½ percent of GDP over the medium term, in line with recovering oil prices and increased capital imports, even as exports rise on increased investment. Reserve coverage would remain adequate.

18. There are significant risks to the outlook. Another flare-up in COVID-19, in Kenya or its trading partners, could lead to renewed disruptions to trade and tourism and require broader reinstatement of containment measures. A deterioration in global sentiment toward emerging markets could disrupt international capital flows and pressure Kenya's external position. Weather risks could adversely affect agriculture, as could another wave of the locusts that plagued large parts of the country last year. Delays in fiscal consolidation and structural reforms could raise financing pressures and reduce medium-term growth. Upside risks include a faster-than-projected rebound in economic activity and government revenue.

III. PROGRAM OBJECTIVES

19. Our primary policy objective is to enable a strong post-COVID recovery with robust, inclusive growth. Our plans are outlined in the Post COVID-19 Economic Recovery Strategy that is currently being finalized. The economic core of our plan, which will be supported by the proposed EFF/ECF arrangements, is based on prudent macroeconomic management and structural reforms to anchor macroeconomic stability and stimulate investment. Fiscal consolidation will be achieved by raising revenue and by reducing waste and inefficiencies in spending while protecting developmental spending. The latter will be centered on our Big Four Agenda for food security, affordable housing, manufacturing, and affordable healthcare. Our key policy priorities are:

- **COVID-19 response.** Ensure provision of required health services, address urgent needs of vulnerable groups, and support economic activity.
- **Fiscal policy.** Undertake growth-friendly fiscal consolidation to preserve debt sustainability by bolstering revenue primarily through broadening of the tax base and curtailing overall spending while prioritizing high-impact social and investment expenditure.
- **Public financial management.** Decisively increase the efficiency, effectiveness, and transparency of public spending to eliminate waste and achieve better value for money.
- **Monetary policy.** Strengthen the monetary policy framework by refining policy operations to keep short-term interest rates stable and close to the policy rate.
- **Access to affordable finance.** Transform the banking sector to one that works “for and with Kenyans” and is anchored on pillars of customer centricity, risk-based credit pricing, transparency, and ethical banking.
- **Financial stability.** Safeguard financial stability by enhancing prudential regulation and supervision and enhancing operational tools in the context of increasing financial sector complexity.
- **Structural reforms.** Deepen structural reforms to improve the business environment and boost investment, employment creation, and potential growth.

- **Governance.** Enhance institutional oversight arrangements, strengthen preventive frameworks to improve accountability and foster good governance, and move towards overall greater transparency.
- **Statistics.** Improve data quality in line with international best practices to support economic policymaking, transparency, and accountability.

IV. PROGRAM POLICIES

A. Fiscal Policy

20. Policy objective: For the near term, our key objective is to ensure an effective response to COVID-19 through initiatives to bolster health services, protect vulnerable groups, and support hard-hit parts of the economy. Given the rapid build-up of debt-related risks resulting from the shock, our near-term response efforts would be carefully prioritized to contain further increases in public debt. As the pandemic fades, reducing debt vulnerabilities would become the primary objective of the program. As such, we aim to progressively reduce the fiscal deficit to put the ratio of public debt to GDP on a firmly declining path within the program period. This will lower financing risks and facilitate expansion in credit to the private sector, supporting economic growth.

21. Fiscal consolidation will be growth friendly. We aim to take significant revenue-raising measures, focusing on further reducing tax expenditures to improve the efficiency of the tax system. We will also carefully prioritize spending and eliminate waste while protecting growth-enhancing expenditures. Consolidating recent initiatives, we will continue with our zero-based budgeting process where all government spending must be justified, the policy of no new investment projects, and the review of externally funded projects to ensure performance and realignment with the Big Four Agenda. To support debt sustainability, we will exercise caution in contracting non-concessional borrowing and prioritize concessional borrowing to reduce debt servicing costs. We will during the coming year revisit the legal debt ceiling to ensure it remains consistent with program targets.

22. For FY2020/21 we are targeting an overall fiscal deficit of 8.7 percent of GDP. The deficit this year will unavoidably be higher than the 7.8 percent of GDP recorded in FY2019/20, as we now face the full-year impact of COVID-19 on both revenue and expenditures. In addition, where government in FY2019/20 received 0.7 percent of GDP from a mop-up of liquidity at parastatals, several SOEs whose operations have been adversely affected by COVID-19 will this fiscal year require budgetary support. Against this backdrop, to promote the health of government finances, we are taking major steps to boost revenue, prioritize spending, improve the efficiency of public sector operations, and reduce financing costs.

- **Broadening of tax base.** Revenue-enhancing measures enacted in April and June (Text Table 1) with a view to broadening the tax base and raising the efficiency of the tax system have an estimated full-year yield of Ksh 124 billion (1.2 percent of GDP). This excludes inflation adjustments to excise taxes introduced in October 2020, which had an estimated revenue yield of Ksh 6 billion in FY2020/21.

Text Table 1. Kenya: Revenue-Increasing Measures Introduced in 2020		
	Effectiveness date	Full-year revenue impact (Ksh million)
Tax Law Amendment Act (April 2020)		81,291
Corporate Income Tax (CIT)		28,153
Disallow 30% of electricity cost incurred in addition to the normal electricity expense	25 Apr. 2020	2,700
Discontinue exemption of interest earned on contribution paid to Deposit Protection Fund from tax	25 Apr. 2020	5,200
Reduce investment deduction rate from 150% to 100%	25 Apr. 2020	14,743
Increase rate on non-resident dividends from 10% to 15%	25 Apr. 2020	3,000
Other measures	25 Apr. 2020	2,510
Value Added Tax (VAT)		51,118
Expand the VAT base by removing the exclusion of excise duty and levies from taxable value of petroleum	15 May, 2020	4,825
Remove plant and machinery from VAT exemptions	25 Apr. 2020	16,556
Remove supplies for construction of power generating plant from VAT exemptions	25 Apr. 2020	29,340
Other measures	25 Apr. 2020	397
Other taxes		2,020
Finance Act (June 2020)		47,072
Introduction of a minimum income tax payable by all companies at 1 % of the gross turnover	1 Jan. 2021	21,000
Introduction of tax on digital services at 1.5% of the gross transaction value	1 Jan. 2021	2,000
Other income tax measures	1 Jan. 2021	4,501
Fees and levies, various changes	1 July, 2020	5,383
Excise duty, various changes	1 July, 2020	1,500
VAT exemption removals	1 July, 2020	7,654
Pay-as-you-earn (PAYE) exemption removals	1 July, 2020	300
Total Revenue-Raising Measures		123,629

- **Reversal of tax cuts.** With economic activity now rebounding, and given the need to bolster government revenue, we reversed effective 1 January 2021 most of the tax cuts introduced in April 2020 (Text Table 2), which was a major milestone in upholding our policy commitment towards fiscal consolidation. This entails additional revenue estimated at Ksh 115 billion on a full-year basis (1.0 percent of GDP).

Text Table 2. Kenya: Tax Cuts Introduced in April 2020 and Their End-Date

	Sunset date	Full-year revenue costs (Ksh million)	Full-year revenue gains from reversal (Ksh million) ¹
CIT: reduction of standard rate from 30% to 25%	1 Jan. 2021	33,757	23,630
PAYE:		100,546	55,091
Increase personal relief from Ksh 16,896 to Ksh 28,800/month	Retained	18,987	0
Revise tax brackets and reduce top tax rate from 30% to 25%	1 Jan. 2021	81,559	57,091
VAT: reduction of standard rate from 16% to 14%	1 Jan. 2021	49,379	34,565
Turnover tax on small businesses reduced from 3% to 1%	Retained	2,630	0
Total value of tax cuts	--	186,312	--
Of which reversed on 1 January 2021		164,695	115,286

¹ Gains from revenue reversals are projected to be temporarily lower as the economy recovers.

- **Expenditure control.** Confronted with significant expenditure demands, including financing our COVID-19 response and Big Four initiatives, we are taking measures to reduce expenditure in less critical areas. Among others, we have via a recent budget circular put a freeze on all new recruitment without National Treasury's approval; required that any adjustments of remuneration and benefits be sanctioned by the Salaries and Remuneration Commission (SRC); focused the development budget on completion of ongoing projects; and stopped commencement of any new project not approved by the National Treasury.
- **SOEs.**¹ The COVID-19 shock has created acute financial stress in several fully or partially government owned entities. These include Kenya Airways, Kenya Power, and multiple universities, who have all experienced steep drops in revenue. In many cases, SOEs were already struggling financially before the pandemic, and the added financial stresses have necessitated government liquidity support. As a result of immediate requirements that have been identified, we plan to spend a total of Ksh 36 billion on extraordinary SOE support in FY2020/21. All such extraordinary support is being based on careful evaluation of need and accompanied by steps to ensure that the entities are put on a sound footing (see Section C below).
- **Financing.** External non-concessional financing will be confined to (i) funding essential projects integral to our development program for which concessional financing is not available and (ii) debt management purposes via operations that would result in both a reduction in the net present value of public debt and an improved debt service profile. Such external financing will complement our domestic financing and help prevent an unnecessary crowding-out of private sector credit. To help reduce financing pressures stemming from the

¹ SOEs are in the context of this MEFP used to refer to all commercial and non-commercial State Corporations as well as companies, such as Kenya Airways, where the state has large minority ownership.

still elevated fiscal deficit, we requested in December 2020 debt service relief under the G20 Debt Service Suspension Initiative. As a participant in this initiative, we expect to defer debt service totaling about USD 639 million that would have fallen due in the first half of 2021 to subsequent years.

- **Supplementary budget.** The above measures are reflected in a supplementary budget that was presented to Parliament in early February (**prior action for the program**). Aligned with the proposed program, the supplementary budget targets total revenue and grants of Ksh 1,898 billion, total expenditure of Ksh 2,864 billion, and total financing of 966 billion.

23. For FY2021/22 we are targeting a fiscal deficit of 7.5 percent of GDP, a 1.2 percentage point reduction from this year's expected outturn. Total revenue including grants is projected to reach 16.8 percent of GDP, as increased tax revenue of 0.6 percent of GDP (driven largely by the full-year impact of the tax measures taking effect on 1 January 2021) is partially offset by lower non-tax revenue. Total expenditure is projected to decline by 1.4 percent of GDP, as budgetary outlays for SOEs and for COVID-related spending decline, reflecting continued tight expenditure control in other areas. We will by end-April 2021 submit to Parliament a budget for FY2021/22 that is consistent with the 7.5 percent of GDP deficit target (structural benchmark).

24. For the following years, we will continue revenue mobilization and tight expenditure control, with a view to reducing the deficit to 4.3 percent of GDP by FY2023/24. A key priority will be to raise the ratio of revenue to GDP to well above pre-COVID levels to create space for growth-enhancing investments and priority social spending. To achieve this, we plan to introduce additional tax policy measures to yield 0.8 percent of GDP in FY2022/23 and 0.9 percent of GDP in FY2023/24. We will also progressively reduce recurrent expenditure as a ratio to GDP, by containing growth in the wage bill and in spending on goods and services, while keeping development spending steady at close to 5 percent of GDP.

25. The uncertainty associated with the COVID-19 crisis entails high risks to our fiscal program. The uncertainty is particularly pronounced for government revenue, where a deeper-than-expected economic fallout of the crisis could depress tax receipts. Possible channels include lower-than-expected yield from recent tax measures and disruptions to tax administration leading to lower tax compliance. To ensure that the program performance criterion for the primary fiscal balance is met, any revenue shortfall relative to program targets will be compensated by us taking additional revenue measures or curtailing non-critical spending (focusing on domestically-financed capital expenditure), in consultation with IMF staff.

B. Fiscal Structural Reforms

26. In addition to measures already taken, we will continue to make our tax system more efficient by streamlining exemptions. Our own analyses and IMF TA have identified substantial tax expenditures associated with a long list of tax exemptions and incentives. The proliferation of tax expenditures in past years has made our tax system less efficient, has contributed to a decline in the revenue-to-GDP ratio, and has generally not had the desired effect (e.g., price reductions for

consumers or expansion of production). To strengthen transparency and enhance oversight, we will start publication of an annual report on tax expenditures and their budget implications (structural benchmark for September 2021). While we have already taken significant measures to reduce tax expenditures, we believe there is room for further streamlining of our tax system. IMF TA has identified potential revenue gain of 2.6 percent of GDP within the VAT from further removal of exemptions outside agriculture and limiting of zero-rating. IMF TA has also identified revenue potential of 0.8 percent of GDP from more equitable taxation of capital income as well as substantial potential for further revenue from excise taxes. The new minimum alternative tax is a valuable tool in an equitable approach to taxation that has the potential for further enhancements. We will act within these areas to reach the programmed revenue targets, closely coordinating with the Kenya Revenue Authority (KRA) to ensure administrability and timely implementation of tax policy change.

27. Complementing our planned tax policy initiatives, we are intensifying efforts to strengthen revenue administration.

Initiatives underway include: enhancing tax and customs debt management, including by leveraging the iTax debt module; strengthening audits; developing and implementing risk-based frameworks to support targeted tax enforcement; expanding the number of taxpayers by identifying new or non-compliant income earners; stepping up post-clearance audit and risk management; enhancing exemptions compliance; improving customs scanning; strengthening monitoring of petroleum trade; and applying enhanced methods for import valuation. We are also enhancing use of import valuation tools (e.g. BIDM, CRSP) and implementing a new integrated customs management system (iCMS) to strengthen integrity, entrench best practices in risk management, and support automated entry processing. Key objectives include:

- Strengthening audit function by setting up audit teams in the large and medium taxpayer offices. We will by end-2021 have increased by 30 percent the number of Level II audits of firms, using risk-based approaches to select taxpayers with focus on sectors with large gaps in compliance identified by the IMF VAT-Gap analysis (structural benchmark for end-2021).
- Strengthening post-clearance audit by increasing assigned staffing from the current 21 to 45 before end-June 2021 and by re-focusing audits on high-risk sectors giving priority to large and medium importers.
- By December 2021, enhancing valuation methods in customs by using data analysis (i.e. mirror data analysis and tax and customs data matching) to identify and focus enforcement actions on the major valuation gaps by sectors or commodities.
- By December 2021, completing a comprehensive review of end-use of exempt products to rein in abuse and complete audit of all exemptions over the past 5 years to detect misuse.
- By June 2021, achieving processing of all compliant customs entries within 24 hours.
- By June 2021, developing and implementing risk-based compliance strategies for two to three non-compliant sectors (i.e. professionals, high net worth individuals, real estate sector) and the extractive sector, including ensuring the KRA's participation in cost audits in the upstream petroleum sector.

28. We will eliminate waste and improve the efficiency of government expenditure. The recent Public Expenditure Review (PER) that we completed with the World Bank identified options for expenditure rationalization that would yield savings estimated at 2.6 percent of GDP. These centered on strengthened government procurement (0.9 percent of GDP), improved wage-bill management (0.2 percent of GDP), and rationalization of the public investment project pipeline (1.5 percent of GDP). Actions in these and other areas will allow us to achieve the programed expenditure targets.

29. Strengthening public procurement can help drive increased efficiency in government spending. The PER finds that standardization and use of framework agreements in contracts could significantly reduce transaction costs in government procurement, boost bargaining power, and secure lower prices. To this end, we are developing an e-procurement system linked to our Integrated Financial Management Information System (IFMIS) to automate application of the Procurement Act and regulations. An agreed roadmap and strategy for e-procurement was approved in December 2020 and we aim to have a system developer identified by end-April 2021. This initiative is being complemented by steps to enhance transparency in public procurement that will support oversight and accountability. To advance the efficiency and transparency in public procurement, we will:

- Pilot by December 2021 and apply by December 2022 the new e-procurement system across Government Ministries, Departments, and Agencies (MDAs).

30. Controlling the government wage bill can also yield significant savings. To help protect high priority social and development spending in the context of limited fiscal space, we intend to gradually reduce the ratio of the government wage bill to GDP by about 0.5 percentage points by FY2023/24. This will be accomplished through continued restraint in hiring and wage awards (including in the 4-year wage agreement that will come into effect in FY2021/22) and by improved wage-bill management. On the latter, the PER finds that regular cleaning of the payroll to eliminate ghost workers, a review and rationalization of the number of allowances, and improved functionality of government payroll management systems could make a significant contribution to increasing efficiency and reducing government expenditure. We will take the following actions in this area:

- By June 2021, harmonize and rationalize the categories, rates, and rules for allowances.
- By June 2021, issue decision to implement across MDAs, Counties, and SAGAs (Semi-autonomous Government Agencies) a common payroll system linked to IFMIS (structural benchmark). Payrolls would prior to being transferred to the new common system be cleaned and audited.
- By December 2022, complete the automation of personnel expenditure using the new payroll system in at least 50 percent (by value) of MDAs, Counties, and SAGAs.

31. Strengthening public investment management (PIM) will be key to securing our developmental objectives. Effective PIM is critical to achievement of our Big Four Agenda. Kenya's public investment plan includes some 4,000 projects, but many of these have been slow to execute. This has resulted in about \$10 billion of committed but undisbursed official development assistance,

much of it on concessional terms. The PER identified 522 dormant projects and potential one-off expenditure savings of about 1.5 percent of GDP from cancelling one-third of these. More generally, ineffective use of available project financing hampers service delivery, entails avoidable commitment fees on undisbursed funds, increases our reliance on expensive commercial financing, and worsens our public debt vulnerability.

32. We have taken significant steps to strengthen PIM. We are now applying on a temporary basis a project management system linked to IFMIS to undertake a stocktaking exercise to bring clarity to the status of projects and associated commitments, and we have already completed the work for most of the sectors. We are developing a framework for project appraisal and selection as well as an automated project management information system. We are addressing obstacles to the flow of funds from development partners, by endeavoring to ensure that: (i) administrative delays are addressed; (ii) budget appropriations are adequate to honor outstanding and planned commitments; and (iii) counterpart funds are made available. To further strengthen PIM, we will:

- By March 2021, complete the ongoing stocktaking of existing projects and associated commitments in the areas of education, health, and infrastructure, enter the results in the Hyperion system, and identify projects to be rationalized (structural benchmark).
- By July 2021, appoint a substantive director for the PIM department.
- By July 2021, fully operationalize new PIM framework, covering all phases of the public investment project cycle, including provisions relating to the identification, economic appraisal, selection, implementation, and monitoring and evaluation of all proposed, active, and completed projects.
- By July 2021, ensure that all new projects are based on clearly defined criteria and pre-determined costing methodologies in line with the PIM regulations and guidelines.

33. Public Financial Management (PFM). Our development agenda is anchored on prudent management of available public resources. As such, we will continue to strengthen expenditure control and improve the efficiency and effectiveness of public spending through necessary public financial management reforms. Focus areas include strengthening budget processes, IFMIS functionality, commitment controls, and cash management. Having strengthened our IFMIS infrastructure, we are adding functionality to the system and enhancing controls. We have introduced a new Cash Management Framework. We will in accordance with that framework limit monthly exchequer releases consistent with aggregate in-year cash and debt plans approved by the Cash Management Committee, which will be regularly revised in line with up to date forecasts. We will also be reviewing the number of extra-budgetary units with a view to consolidating these and, where appropriate, bring them within the perimeter of the budgetary central government. In addition, we will:

- By March 2021, initiate regular quarterly reporting on pending bills, covering MDAs, Counties, SAGAs and State Corporations (SCs) (structural benchmark).
- By June 2021, develop IFMIS to capture all outstanding commitments when the obligations are entered. This will be accompanied by steps to require that all MDA commitments are

immediately entered and only valid once entered on IFMIS with penalty for failure to comply.

- By July 2021, automate cashflow plans and exchequer for MDAs and Counties, such that, exchequer requests will be processed online through IFMIS.
- By July 2021, strengthen functionality of IFMIS to cover multi-year commitments, pending bills, procurement and cash plans, and budgeting for allowances.
- By June 2022, ensure that all MDA budget proposals for 2022/23 have been prepared using a common costing approach, which by then will have been built into the Hyperion budget preparation system and elaborated in a budget costing manual.
- By June 2022, we will have developed a functional system of commitment control where the only valid financial commitments are those that have been entered on IFMIS and where all government issued contracts are accompanied by an IFMIS-linked certificate of validity.

34. Public debt management. As part of strengthening debt management, we are enhancing debt reporting, lengthening maturities, and avoiding bunching of repayments to mitigate refinancing risks. The structure and functions of the Public Debt Management Office (PDMO) are being enhanced to oversee debt management as envisioned in the PFM Law, and we are establishing an Investor Relations Unit to strengthen communication with the outside world. To deepen the domestic debt securities market, the National Treasury is working with CBK to implement several reforms. We have strengthened the auction management process by implementing the Treasury Mobile Direct platform for retail sale of government securities, and enabled auction of bids by banks through internet banking. Additionally we are (a) further strengthening market infrastructures and auction management processes for government securities by developing the Central Securities Depository System; (b) maintaining a smooth yield curve for domestic debt securities; (c) supporting the enhancement of market structure and conduct through treasurers and dealers of commercial banks; (d) lengthening the maturity profile of government debt securities; (e) enhancing transparency through publication of auction rules and guidelines and (f) strengthening the bond benchmark building program. Regarding external debt, we are proactively working to ensure increasing utilization of committed concessional financing. Our participation in the G20 Debt Service Suspension Initiative will help reduce financing pressures. Looking further ahead, we will:

- By July 2021, have issued regulations and a service contract for the Public Debt Management Office to make operational the framework for debt management envisioned in the PFM Act.
- By October 2022, in our regular reporting on public debt, expand the coverage of public debt to include non-guaranteed public sector debts (including arrears) not currently included.

35. Public Private Partnerships (PPPs). Given the limited fiscal space, we are revamping the PPP Unit in the National Treasury to support efficient and sustainable scaling up of our PPP program without undue fiscal risks. This has included appointing a Director-General for the PPP Unit to provide strong leadership and strategic oversight. To ensure that only projects with the highest

socio-economic returns are undertaken, we are in the process of creating and institutionalizing a joint PIM-PPP planning framework. This will help streamline the decision process of determining whether projects should be procured through the traditional public sector method or as PPPs. We are also strengthening coordination between PDMO and the PPP Unit for effective control of fiscal exposure, as envisioned in the PPP Act. Other specific actions include:

- By March 2021, commencing implementation of a revised institutional structure for the PPP Unit as provided in the PPP Act.
- By July 2021, fully operationalizing the PPP Project Facilitation Fund through creation of a budget line for annual funding.

36. Pension reform. To put pensions on a sustainable footing, we are introducing a funded pension scheme for public sector workers, the Public Service Superannuation Scheme (PSSS). We are also increasing efficiency by digitalizing our pension management system, a process we aim to have completed by June 2022. The PSSS commenced at the start of 2021 and will over time replace the current *pay-as-you-go* system. Participants in PSSS will include all new public sector workers and current workers under the age of 45. PSSS contributions will be paid into a Public Service Fund supervised by the Retirement Benefits Authority. PSSS will allow portability of pension benefits, facilitating free movement of staff into and out of the public sector.

C. State-Owned Enterprises

37. We will take a staged approach to evaluate, monitor and manage the financial problems in SOEs. The current pressures facing many SOEs have accentuated long standing challenges in a sector characterized by overlapping mandates, low profitability, weak governance and poor value for money. To address this, the key components of the approach are: (i) in the very near term, an evaluation of financial health and FY2020/21 fiscal needs of the SOEs that pose the highest fiscal risk to the FY2020/21 budget; and over the next few months, (ii) completion of an in-depth analysis of the financial vulnerabilities of the largest and most exposed firms in the sector and (iii) development of a strategy to address fiscal risks from SOEs, including a framework for deciding on interventions. Any provision of extraordinary support will be in line with this framework. In addition, we will embark on fundamental reforms to strengthen frameworks for SOE corporate governance. This will all be complemented by robust ongoing monitoring of SOEs' financial condition and deeper evaluation of fiscal risks from SOEs. Specific elements of the plan include:

- Complete financial evaluation of the 9 SOEs with largest fiscal risk to the FY20/21 budget, to include projection of related urgent fiscal needs in FY2020/21 supported by clear presentation of their necessity (**prior action**). The entities will be selected based on largest financial and fiscal risks and will include Kenya Airways, Kenya Airports Authority, Kenya Railways Corporation, Kenya Power and Lighting PLC, Kenya Electricity Generating Company PLC, Kenya Ports Authority, and three of the largest universities. Our analysis, which will apply IMF-developed tools, will cover baseline assessment; expenditure, revenue, and debt drivers; COVID-19 impact; factors determining the size of remedial measures; modality of

remedial measures and impact on the fiscal framework. This evaluation will be the basis of any extraordinary SOE support in FY2020/21, which will be limited to exigent needs.

- By end-May 2021, prepare a strategy for addressing financial pressures in the SOE sector including an in-depth forward-looking financial evaluation of the top 15-20 SOEs representing the largest financial and fiscal risks, a framework for deciding on interventions, and reforms to rationalize the SOE sector (structural benchmark).
- The SOEs for the financial evaluation will be selected according to transparent criteria and the analysis will include a forward-looking assessment of cash flows and of associated fiscal risks. The financial evaluation will inform any extraordinary SOE support in FY2021/22.
- The strategy for addressing financial pressures in the SOE sector will include a framework for deciding on interventions and reforms to rationalize government involvement in the sector and ensure the viability of SOEs' continued operations. It will reflect the limited fiscal space and be consistent with programmed fiscal targets. Given the broad implications, the IMF team will be closely consulted as the strategy is developed. We will also engage an independent outside financial advisor with appropriate expertise to evaluate the financial situation and least cost restructuring options of Kenya Airways.

38. We will continue to improve oversight and governance arrangements of the SOE

sector. Following recommendations from the task force on parastatal reforms completed in 2013, the framework for SOEs has been enhanced with the State Corporation Act of 2012 and issuance in 2015 of a code of good corporate governance that clarifies expected good practices in SOE management and oversight. State Corporation Advisory Committee (SCAC) is leading implementation of the new set of norms, and efforts are bearing fruit in improving board composition and reporting. We will continue to introduce further governance arrangements that enhance management and oversight of SOEs. The results of the SOEs evaluation will shed light on the fiscal risks, and in line with the restructuring plans there will be a need to reform the governance of the SOEs that we will decide to retain moving forward. At the same time, there will be a need to rationalize the SOE portfolio to ensure that overlapping SOE mandates are resolved. This includes:

- By July 2021, completing a draft blueprint that will indicate the needed legal reforms as well as the implementation actions to operationalize efficiency in oversight and management of SOEs (to be supported by IMF TA).
- Developing by September 2021 an integrated monitoring and reporting system, that will be accessible by relevant oversight entities including among others the line ministries, National Treasury, and SCAC, which will operate both as a database and an early warning system to facilitate proactive rapid response interventions on policy and regulatory compliance targets.
- Enhancing the performance management setting, monitoring and evaluation framework for commercial state corporations, and facilitate the necessary capacity building, development of guidelines, rewards and sanctions framework.
- Initiating a review of institutional structures across MDAs, SAGAs, and SCs. This review and an action plan to eliminate duplicate functions will be piloted in at least one sector by

December 2021. The exercise will subsequently be rolled out in other sectors based on a roadmap agreed by July 2021.

39. To inform decision making we will strengthen risk analysis and monitoring of the broader public sector. Specifically, we will:

- By end-September 2021, start including in the annual Budget Review and Outlook paper an expanded fiscal risk analysis that quantifies contingent liabilities stemming from high-risk SOEs and initiates coverage of PPPs (structural benchmark). The analysis will include specific coverage of high-risk SOEs and any other entities that are incurring financial difficulties or rely on direct or indirect government support. The analysis will also report on the expected costs of guarantees and on risk exposure to completed and planned PPPs nearing completion. Risk mitigation measures should also be discussed.
- By September 2021, apply strengthened budgeting and reporting templates for SAGAs and SCs using an automated Management Information System.

D. Monetary Policy

40. Policy objectives: Our primary policy objectives are to: (i) maintain headline inflation within our target range (5±2.5 percent); (ii) maintain a flexible exchange rate regime, with market interventions only in response to excess exchange rate volatility; and (iii) further improve the monetary policy framework. A monetary policy consultation clause (MPCC) with a 5 percent +/- 2.5 ppt band will help monitor inflation performance, providing for a consultation with the Executive Board to be triggered if inflation falls outside the band (TMU, ¶23).

41. We are strengthening the monetary policy framework. Following the removal of interest rate caps, which had hindered monetary policy effectiveness, we will publish by June 2021 a white paper outlining reforms to strengthen the monetary policy framework (structural benchmark). In this regard, and as conditions permit with the normalization following the COVID-19 shock, the reforms will focus on:

- i). Refining our macroeconomic modeling and forecasting frameworks.
- ii). Improving the operations of financial markets, including fully developing by December 2021 a Centralized Security Depository that will improve monetary policy transmission and promote efficiency and transparency in the government domestic debt market. In developing financial markets, CBK has rolled-out Treasury Mobile Direct (mobile platform for government securities) and Internet Banking, installed the Enterprise Data Warehouse (EDW) for near-real time data capture and analysis, and is currently assisting ACI-Kenya and the Treasurers forum with the formation of a strong financial association for the domestic market.
- iii). Improving communication of monetary policy decisions to make them more effective.

42. The monetary policy framework will be supported by recent reforms to strengthen CBK's internal capacity and enhance monetary policy transmission. The key reforms are outlined below:

- Repeal in November 2019 of interest rate caps on commercial bank loans under section 33B of the Banking Act. The caps had led to a rationing of credit, particularly to the most vulnerable, such as Micro, Small, and Medium Enterprises (MSMEs). This reform has restored the clarity of monetary policy decisions and is expected to strengthen the transmission of monetary policy.
- Strengthening of the CBK balance sheet to enhance the Bank's capacity to fulfil its mandate. In July 2018 the CBK's authorized share capital was increased from Ksh 5 billion to Ksh 50 billion. The paid-up share capital was gradually increased from Ksh 5 billion to Ksh 35 billion.
- The CBK issued a new generation of coins and banknotes on December 11, 2018 and May 31, 2019, respectively. The new generation currency notes were designed to conform to the requirements of Article 231 of Kenya's Constitution, and have additional security features.
- Demonetization of the old series Ksh 1,000 note was successfully concluded on September 30, 2019. The demonetization was aimed at addressing concerns of illicit financial flows and corruption, as well as increased risks of counterfeits targeting the large denomination. These posed a threat to the credibility of the Kenyan currency.
- Strengthening of the CBK systems, processes, and people. This includes stabilizing the information technology systems through upgrades of the core banking system, the T24, and Kenya Electronic Payments and Settlements System (KEPSS). Realignment of the Central Bank structure was undertaken to reflect its mandate in a new automated, integrated, and fast-paced world. This involved realigning departments, staff, and their functions and processes. Other recent initiatives include a roll-out of a mobile-based service designed to facilitate investment in government securities by retail investors known as the Treasury Mobile Direct. In addition, the CBK is rolling out the CSD system mentioned above.

E. Financial Sector

43. Policy objectives: Safeguarding financial stability and expanding access to affordable finance remain our key priorities as the financial sector supports the economy through the COVID-19 pandemic. We will continue to take steps to improve prudential regulation and supervision, with a view to addressing the increased complexity of the financial sector. Our objective is to promote sustainability and resilience of the Kenyan financial sector along four pillars: customer centricity; risk-based credit pricing; transparency; and ethical practices. This will enhance the financial sector's capacity to provide affordable financial services to Kenyans.

44. The banking sector is stable and resilient, as it supports the economy through the COVID-19 pandemic. Core capital and total capital adequacy ratios as at December 31, 2020 were at 16.7 and 19.2 percent respectively, above the statutory minimums of 10.5 and 14.5 percent. The

liquidity ratio at end-December stood at 54.6 percent above the statutory minimum of 20 percent. The gross Non-Performing Loans to Gross Loans ratio stood at 14.1 percent in December up from 12.3 percent in February 2020. Increases in NPLs were noted in the transport and communications, trade, real estate, real estate, and agriculture sectors mainly due to the COVID-19 pandemic related slow down.

45. We have put in place financial sector measures to mitigate the adverse impact of COVID-19. Over the crisis period, the Central Bank of Kenya (CBK) implemented a range of measures aimed at cushioning the banking sector and the wider economy from the adverse impact of the pandemic. These measures include monetary, financial, prudential and other regulatory measures. CBK's measures have been taken in coordination with other Government interventions seeking to address the social, economic and medical consequences of COVID-19.

46. Enhancing the use of digital platforms: In consultation with authorized Payment Service Providers (PSPs) and commercial banks, limits on mobile money transactions were enhanced and charges on low value transactions (of up to Ksh 1,000) eliminated. These measures remained in effect until the end of 2020. There was, accordingly, a notable increase in both transaction volumes and values of low value transactions and transfers between bank and mobile e-wallets. This is indicative of a gradual shift towards digital platforms and less utilization of physical access channels. Anti-Money Laundering and Combatting the Financing of Terrorism (AML/CFT) checks also have been strengthened to guard against abuses.

47. Loan restructuring: Banks committed to discussing restructuring of loans with customers whose loans were performing as at March 2 but were adversely impacted by the pandemic. In the nine months to end-2020, a total of 401,096 loan facilities valued at Ksh 1.63 trillion (54 percent of the banking sector loan book of Ksh 3 trillion) have been restructured to enable borrowers cope with loan servicing challenges. We continue to closely monitor the performance of the restructured loans and their impact on banks' earnings and capital buffers.

48. Strengthening the Credit Referencing Mechanism: On April 8, the Credit Reference Bureau (CRB) Regulations, 2020 became effective refreshing the framework that had been in place since 2013. The revised Regulations in addition to supporting the risk-based pricing pillar of the banking sector charter provided for temporary suspension of listing of negative credit information in exceptional circumstances. Accordingly, and in light of the adverse impact of COVID-19, on April 14, CBK issued Banking Circular Number 7 and Number 8 of 2020, which temporarily suspended the sharing of negative credit information on credit facilities that became non-performing as from April 1 for six months from April 1 to September 30.

49. Business Continuity Planning: On March 27, CBK issued guidance to the banking sector on pandemic planning and business continuity. The guidance, which was aligned to protocols from the Ministry of Health, is aimed at monitoring the incidence of the pandemic in the sector and guiding responses thereto. In the pandemic period, over 90 percent of the bank branch network across the country has remained open. This includes in areas that were under COVID-19 movement restrictions.

50. To expand access to affordable credit to micro, small and medium sized enterprises (MSMEs) and support their recovery from the adverse impact of COVID-19, we have established a new credit guarantee scheme (CGS) to share the risk of new credit origination to MSMEs. The design of the CGS, which ensures risk sharing on a first-loss basis between participating banks and the scheme, is intended to incentivize the extension of the credit that will be essential in reactivating the economy as it comes through a period of very high uncertainty occasioned by COVID-19.

51. Ensuring Capital Adequacy during and beyond COVID-19 Pandemic. CBK has since 2016 adopted the Internal Capital Adequacy Assessment Program (ICAAP) in ensuring that banks hold adequate capital aligned to their risk profile and market niche. ICAAP is approved by each bank's board and is important in building the resilience of the banking sector. ICAAPs are a critical component of the ongoing Supervisory Review and Evaluation Process (SREP) carried out by CBK on each bank. SREP seeks to assess the risk profile of each bank and ensure that it has adequate capital and liquidity buffers. On August 14, CBK issued a Circular requiring banks and mortgage finance companies to re-submit by October 31, 2020 their ICAAP documents for 2020. The re-submitted ICAAP documents were required to take into account:

- The impact of the COVID-19 pandemic and mitigating measures taken by the institution.
- Measures taken and proposed to strengthen the balance sheet and maintain adequate capital and liquidity.
- Any proposed distribution of 2020 profits.

Banks were also required not to make any decisions on distribution of their 2020 profits before discussing the re-submitted ICAAP documents for 2020 with CBK. In line with existing requirements, banks will submit their 2021 ICAAPs by April 2021. In addition, in accordance with existing requirements all banks will publicly disclose their capital adequacy ratios by end-March 2021 based on audited end-year financial statements for 2020. We will publish the individual end-year bank capital adequacy ratios and the overall sector capital adequacy status in accordance with existing processes in the annual 2020 Bank Supervision Report by May 2021.

52. Towards the Banking Sector Vision. As it addresses current challenges from COVID-19, the banking sector remains on track towards realizing the vision outlined in CBK's Banking Sector Charter of a banking sector that works for and with Kenyans. Beyond the strategic uncertainties arising from the pandemic, the banking sector is set to emerge in a robust state. On the positive side, the pandemic has enhanced the sector's resilience and adaptability, with a shift to digital service channels and less reliance on physical "brick and mortar" channels. Our reform agenda remains on track including.

- a. **Banking Sector Resilience-** The need to build resilience and exploit emerging opportunities has led to increased consolidations and combinations among several players. During the pandemic period, three transactions have been completed, the acquisition of Mayfair Bank by CIB of Egypt, the acquisition of Transnational Bank by Access Bank of Nigeria and the acquisition of Jamii Bora Bank by Co-operative Bank of

Kenya Limited. Additionally, Kenyan banks have continued to expand regionally through acquisitions including in the Democratic Republic of Congo, Rwanda and Tanzania. CBK will continue with the focus of building a resilient banking sector with strong business models and governance frameworks that will support Kenya's post-pandemic recovery.

- b. **Moving towards real-time Supervision**-We are implementing a centralized Electronic Data Warehouse (EDW) that will merge all the different information sets provided by banks to CBK. Through Application Program Interfaces (APIs), we shall connect the EDW directly to banks to enable us to access data on a near real-time basis. This will significantly enhance the proactiveness of our offsite surveillance systems and provide a laser focus for our onsite inspections of banks. We are working with selected pilot banks as we move towards integrating the EDW with banks.
- c. **Maximizing opportunities from financial innovation while minimizing the resultant risks.** CBK continues to engage with domestic, regional and international partners to foster innovation while minimizing risks. In this regard, CBK together with the Monetary Authority of Singapore (MAS) co-hosted the 2020 Virtual Africa Hackathon in August. The Hackathon which attracted 74 applicants from 14 countries sought to identify technology solutions from African Fintechs addressing the health and economic impacts of COVID-19. The winner from Cameroon participated in the virtual Global Singapore Fintech Festival in December.
- d. **Governance of Bigtechs.** In October, the Dialogue on Global Digital Finance Governance was launched. The dialogue co-Chaired by the United Nations Development Program and CBK seeks to provide a platform for advancing consensus on policy and regulatory responses to the development of global digital financing platforms appropriate for developing countries contexts and economies.
- e. **Review of the Microfinance Act.** To accommodate considerable changes that have been experienced in the Microfinance industry over the years, CBK has been in the process of reviewing the existing regulatory and supervisory framework for microfinance banks. CBK finalized the review of draft Microfinance Bill, and it was forwarded to the State Law Office for consideration in December 2019. As at end of December 2020, the State Law Office had finalized legislative drafting of the Microfinance Bill ahead of publication and tabling of the Bill for consideration by the National Assembly.
- f. **Licensing of Kenya Mortgage Refinance Company.** On September 18, CBK licensed the Kenya Mortgage Refinance Company Plc (KMRC) as the first mortgage refinance company in Kenya. The license was granted pursuant to the CBK (Mortgage Refinance Companies) Regulations, 2019. KMRC's principal objective is to provide long term finance to primary mortgage lenders (commercial banks, mortgage finance companies, microfinance banks and Savings and Credit Co-operatives) to increase the availability and affordability of mortgage loans to the public.
- g. **The Central Bank of Kenya (Amendment) Bill, 2020 on Digital Lenders.** The Central Bank of Kenya (Amendment) Bill, 2020 (the Bill) was published on June 19. The principal objective of the Bill is to empower CBK to supervise and regulate digital lenders. The Bill proposes that the CBK acts as the regulator of digital lenders in Kenya, so as to ensure a

fair and non-discriminatory marketplace for access to credit. The Bill is currently under consideration by the National Assembly.

- h. **Strengthening the Anti-Money Laundering and Combating the Financing of Terrorism Framework (AML/CFT).** We have made significant progress on various fronts in improving the AML/CFT legal framework but more importantly in its implementation through various initiatives. From a broader perspective, we have strengthened cash transaction monitoring and reporting by banks, enhanced our offsite and onsite surveillance through targeted AML/CFT onsite inspections. Arising from AML/CFT violations identified during our inspections, we have enforced administrative sanctions and penalties. This includes penalties levied on banks, payment service providers, money remittance providers and other financial institutions. Additionally, we conducted a successful demonetization exercise in 2019 withdrawing the old generation Kenya Shilling 1,000 note. The demonetization was informed by the twin concerns of large banknotes, particularly the older 1,000-shilling series being used for illicit financial flows in Kenya and in the region. The other concern related to emergence of some counterfeits posing a threat to the credibility of the Kenyan currency. In crafting the demonetization strategy, we reviewed the experiences of other countries and regions that have carried out similar exercises, including Australia, European Union, Pakistan, United Kingdom and most recently India. Critical to the eventual success of the exercise were strong AML/CFT filters in banks that ensured that illicit funds were screened out of the financial sector. AML/CFT monitoring was scaled up by the Central Bank of Kenya with 15 targeted inspections conducted during this period on financial institutions. Financial institutions also scaled up their AML/CFT screening reporting over 3,000 Suspicious Transaction Reports (STRs) for further investigation.
- i. **National Risk Assessment (NRA).** In March 2019, the Government of Kenya embarked on the National Risk Assessment (NRA) on Money Laundering and Terrorism Financing. The main objective of the exercise is to identify and assess money laundering and terrorism financing threats and vulnerabilities at the national level. The exercise will cover the significant economic sectors including the financial sector. The findings of the exercise will assist Kenya to develop a national money laundering and terrorism financing national strategy as well as an action plan to address the deficiencies identified in Kenya's anti-money laundering and countering the financing of terrorism (AML/CFT) legal and institutional framework. The exercise is on-going with data collection from various sectors including the banking sector completed in December 2020.

F. Governance

53. We will continue to strengthen fiscal governance. On public procurement, and to prevent misuse of public funds, we have taken steps to implement the new Procurement Act, which provides a legal framework for implementation of electronic procurement by all public entities. It is now a requirement that public entities publish all procurement related information in line with open contracting standards and Executive Order No 2 of 2018. Given that procurement process is vulnerable to misuse for private gain and anonymity helps to hide illicit activities, we will ensure that

comprehensive information on public tenders awarded, including beneficial ownership information of the awarded entities, are publicly available on the government procurement information portal, and that bidders are subject to dissuasive sanctions for non-compliance (structural benchmark for end-June 2021). The State Procurement Portal will be expedited and completed by end-April 2021. This will be complemented by reforms being undertaken to strengthen procurement in public investment (paragraph 15). We will also strengthen the joint effort of the Competition Authority of Kenya and Public Procurement Regulatory Authority to ensure that any irregularities encountered in the procurement process can be met with appropriate penalties. Specifically, we will ensure that the MOU signed by both parties is cleared by the Attorney General and the National Treasury gazettes the necessary competition rules by end-March 2021.

54. We have over the last 10 years worked with global and regional partners, banks, payment service providers, money remittance providers and other financial institutions to strengthen our Anti-Money Laundering/Combating Financing of Terrorism (AML/CFT) legal and regulatory framework. We continue to move forward with strengthening of the AML/CFT framework as new technology and innovations transform the financial sector. In this regard, we will review the effectiveness of our AML/CFT measures in the context of the ongoing National Risk Assessment (NRA) and the Eastern and Southern Africa Anti-Money Laundering Group (ESAAMLG) mutual evaluation in the second half of 2021. From the NRA, we shall formulate the National AML/CFT Strategy and Action Plan by June 2021 to address identified gaps in the AML/CFT framework.

55. We have taken steps to fight corruption. This includes enacting laws that are contributing to enhanced governance and transparency such as the Access to Information Law (from 2016), the Leadership and Integrity Act (2012), Ethics and Anti-Corruption Commission Act (2012), Public Officer and Ethics Act (2003), Anti-Corruption and Economic Crimes Act (2003) and Law on Bribery (2016). The Bribery regulations and guidelines to assist public and private entities to establish procedures for the prevention of bribery have been developed and are going through public participation prior to submission to Parliament. We have also provided additional resources for law enforcement agencies (LEAs) involved in the fight against corruption, including the Ethics and Anti-Corruption Committee (EACC) and the Department of Public Prosecution (DPP) who are now able to hire specialized experts to assist in the prosecution of corruption cases. We have also set up the multi-agency taskforce to enhance coordination between LEAs and collaborating on corruption and economic crime cases. We have made headway in reducing the backlog of cases in courts and developed a case management system that has allowed us to reallocate resources based on need and collect statistics on workflow.

56. We will also step-up our efforts to enhance the effectiveness of the anti-corruption framework, namely by:

(i) Improving the capability of detection of corruption through a better implementation of the preventive measures, more precisely:

- 1) We view the effective implementation of the Access to Information Act as essential to enhance transparency and accountability. After the adoption of the Access to

Information Act, we have drafted the Regulations to operationalize the Act. By May 2021, we will therefore commence stakeholder and public consultations on the Regulations and provide resources to facilitate stakeholder and public participation to support compliance with the Act. Further, by March 2022, standards for digitization and automation of records will be developed to ensure that existing and proposed systems have the capacity to comply with minimum access to information requirements.

- 2) After successfully undergoing completion of the United Nations Convention Against Corruption (UNCAC) peer review process (both cycles 1 and 2), we have initiated the review of the current legal framework of asset declarations and conflict of interest rules for senior public officials to bring it in line with international best practices. The enhancement of the legal framework will, among others, (i) consolidate the wealth declarations and interest declarations of public officials into one uniform disclosure regime, (ii) rationalize the responsibility of analyzing and verifying the disclosures and imposing adequate sanctions for false declarations or failure to declare in a single agency, and (iii) enhance the role, responsibilities and capability of enforcement agencies to investigate, prosecute and sanction perpetrators of illicit enrichment and other corruption offenses.
- 3) We have noted the vulnerability of the financial sector to the risks posed by laundering of the proceeds of corruption, and we will, therefore, continue to use AML/CFT measures to support anti-corruption efforts. We will continue to support efforts of the Financial Reporting Centre (FRC) towards encouraging and strengthening the use of financial intelligence to trace proceeds of corruption by sharing relevant financial intelligence with law enforcement agencies. The FRC will also continue its partnership with the Multi Agency Team (MAT) to detect and deter corruption activities in the country. As we review the effectiveness of our AML/CFT regime in the context of the upcoming Mutual Evaluation by the Eastern and Southern Africa Anti-Money Laundering Group and considering the results of the national risk assessment, we will develop and adopt, by July 2021, the FRC's strategic priorities to bolster its functions and support further the anti-corruption efforts by analyzing financial intelligence related to the proceeds of corruption and disseminating the results to the relevant law enforcement agencies for investigations.
- 4) In order to prevent the misuse of companies to launder the proceeds of crimes, including corruption, we will ensure that all companies are required to submit accurate, complete and updated beneficial ownership information to the Registrar of Companies by end-January 2021.

(ii) Improving the enforcement of corruption offenses by ensuring cases are promptly processed through the criminal justice system.

- 1) We will continue to publish the status of all corruption cases on a public website in a timely manner as well as monitor corruption cases in the High Court Anti-Corruption Division and Anti-Corruption Magistrate's Court. This information will include parties to

the case, the judicial officer, court process stage, next date for hearing, and any reasons for adjournments.

- 2) We have established the National Council on Administration of Justice (NCAJ) - a high-level policy making group, to effectively implement and oversee the efficient, effective, and consultative coordinated approach in the administration and reform of the justice system.
- 3) To ensure the effective prosecution and sanction of corruption and economic crimes as required under the Anti-Corruption and Economic Crimes Act, we will (i) continue to enhance domestic coordination among law enforcement agencies through the Multi-Agency framework; and (ii) fully operationalize the recently established Anti-Corruption and Economic Division of the High Court and enhance the capacity of the Special Anti-Corruption Courts with a view to operationalize the day-to-day hearings of the corruption cases.

(iii) We will continue to collect data on commercial-related cases and consistently publish court decisions to enhance market certainty and to further strengthen the efficiency of the judiciary.

- 1) The Judiciary will publish data on backlog of all commercial, civil and land-associated cases on the judiciary website.
- 2) We shall support the mainstreaming of court annexed mediation in the Judiciary, with emphasis on the Environment, Lands and Commercial Courts.

G. Other Structural Reforms

57. Policy objective: We are deepening structural reforms to improve the business environment and thereby boost investment and employment creation. Much has been done to increase Kenya's growth inclusiveness, pushing the poverty rate down to 36.1 percent in 2015-16 from 46.6 percent in 2005-06 and the Gini index to 0.41 from 0.47. Kenya generally performs better than its peers in sub-Saharan Africa in terms of the Global Competitiveness Index published by the World Economic Forum. Recent business environment improvements include a significant simplification of processes to start a business and better provision of electricity. Kenya also ratified the African Continental Free Trade Area (AfCFTA) and COMESA-EAC-SAD FTA Tripartite agreements in 2018, to move further toward international and regional integration and boost our competitiveness. We have also initiated negotiations on a bilateral trade agreement with the USA and recently signed a trade deal with the United Kingdom, which allows duty- and quota-free access to that market on specified products and should ensure largely unchanged terms after Brexit.

58. Reforms are underway that will support growth in the period ahead. These include (i) reforming fertilizer subsidies through the introduction of an e-voucher program that will improve targeting and reduce vulnerabilities to corruption; (ii) establishing an agricultural commodities exchange that will make agriculture more efficient and reduce vulnerabilities to corruption in sales to the government's strategic food reserve; (iii) changing land use rules to help facilitate private

investment in housing; (iv) achieving universal health care; and (v) reducing the number of days to register a business with implementation of the Kenya Investment Policy.

59. Further reducing gender inequality is essential to unleash our full potential and reach our development goals. Gender equity has remained a focus for policymakers, with Kenya ranked 137 out of 189 countries on the UNDP's 2017 Gender Inequality Index, which constrains economic growth. We will put in place policies to reduce discrimination against women and further enforce implementation of existing gender-rebalancing laws and policies. We will expand health services targeted to women and encourage girls' retention in secondary and tertiary schools. We will further invest in infrastructure that improves households' access to running water, which will reduce time spent by women to fetch water. To boost women's entrepreneurship and economic independence, we will improve access to credit guarantee schemes.

H. Data Quality

60. Policy objectives: We view production and dissemination of high-quality economic statistics as the foundation for good policy through evidence-based decision making. To enhance our macroeconomic data, we will continue to improve the availability, quality, coverage, and timeliness of our statistics.

61. Data coverage, quality, and timeliness. We have enhanced economic statistics with a range of new statistical surveys, including Integrated Survey of Services, Study of Trade Margins, Study of Underground Economy, Study of Informal Transportation, Medium, Small and Micro Enterprises Survey, and Survey of Non-Profit Institutions. To improve macroeconomic data dissemination practices, we joined the Enhanced General Data Dissemination System (e-GDDS) initiative in December 2018. We released the Foreign Investment Survey in April 2019 and submitted international investment position (IIP) data series from 2008 to 2018 to the Fund in July 2020, which are available on the IMF website. We are also working toward improving the quality of our national accounts and government financial statistics and are receiving IMF technical assistance in these areas. The latter is expected to lead to the reporting of (i) general government fiscal outturns on a quarterly basis by June 2022 and (ii) annual fiscal data of the public corporations sector (including financial and non-financial corporations) by December 2021; and (iii) migration of the fiscal framework to GFSM 2014 based concepts by December 2021.

I. Program Monitoring

62. The program will be monitored based on periodic performance criteria, continuous performance criteria, Monetary Policy Consultation Clause, and indicative targets as set out in Table 1. Structural benchmarks set out in Table 2 will be used for monitoring progress on structural reforms. Detailed definitions and reporting requirements for all performance criteria are contained in the Technical Memorandum of Understanding (TMU) attached to this memorandum, which also defines the scope and frequency of data to be reported for program monitoring purposes. During the program period, the government will not introduce or intensify restrictions on payments and transfers for current international transactions or introduce or modify any multiple currency practice

without the IMF's prior approval, conclude bilateral payments agreements that are incompatible with Article VIII of the IMF's Articles of Agreement, or introduce or intensify import restrictions for balance of payments reasons. The first two reviews of the program will take place on or after June 20 and November 7, 2021, respectively.

Table 1. Kenya: Quantitative Performance Criteria and Indicative Targets, March 2021 – June 2022

(in billions of Kenyan shillings, unless otherwise indicated)

	2021			2022
	End March Prog.	End June Prog.	End Dec Prog.	End June Prog.
Quantitative performance criteria				
Fiscal targets				
Primary budget balance of the national government (- = deficit; floor) ¹	-405.9	-507.8	-202.9	-369.4
Tax revenue (floor) ^{1,2}	-	-	783.2	1,667.3
Monetary targets				
Stock of central bank net international reserves (floor, in millions of US\$) ³	5,901	7,547	6,536	6,203
Public debt targets				
Contracting and guaranteeing of new external non-concessional borrowing (ceiling, millions of US dollars) ⁴	3,407	3,407	6,407	7,612
o/w: Debt for a debt management purpose ^{4,5}	2,000	2,000	5,000	5,000
o/w: Debt for projects ^{4,6}	1,407	1,407	1,407	2,612
Contracting and guaranteeing of new external concessional borrowing (ceiling, millions of US dollars) ⁴	2,000	3,100	4,800	4,800
Public and publicly-guaranteed external payment arrears (ceiling) ⁷	0	0	0	0
New domestic guarantees granted by the central government (ceiling) ¹	5	5	5	5
Indicative targets				
Tax revenue (floor) ^{1,2}	996.2	1,433.3	-	-
Priority social expenditures of the national government (floor) ¹	293	391	205	397
Change in the stock of national government exchequer requests outstanding for 90 days or more (ceiling) ¹	0	0	0	0
Monetary policy consultation clause				
Upper band (annual, percentage points)	7.5	7.5	7.5	7.5
Center inflation target (annual, percentage points) ⁸	5.0	5.0	5.0	5.0
Lower band (annual, percentage points)	2.5	2.5	2.5	2.5

¹ Targets are cumulative flows from July 1, 2020 to June 30, 2021 and from July 1, 2021 to June 30, 2022; except for national government exchequer requests outstanding for 90 days or more that are cumulative from July 1, 2020.

² For the purpose of the program, the floor excludes taxes related to "Ministerial Appropriation in Aid" (i.e., RML, RDL, PDL), "Taxes on International Trade and Transactions (IDF fee)", "Capital gains", and "other taxes on goods and services".

³ For program monitoring, the daily average for the month when testing dates are due. Excludes encumbered reserves.

⁴ Cumulative from Program approval. Non-concessional borrowing exceptions.

⁵ In line with the Policy on Debt Limits, debt management operations that improve the overall public debt profile.

⁶ In line with the Policy on Debt Limits, financing for projects integral to the authorities' development program (includes Eurobond borrowing). The list of projects is specified in Annex I of the TMU.

⁷ Continuous.

⁸ Compliance will be evaluated based on the 12-month annual inflation average of the latest three months.

Table 2. Kenya: Proposed Structural Benchmarks		
Measure	Target Date	Macro-criticality
Present to Parliament a supplementary budget for FY2020/21 consistent with programmed targets.	Prior action	Anchor fiscal consolidation.
Complete financial evaluation of the 9 SOEs with largest fiscal risk to the FY2020/21 budget, to include projection of related urgent fiscal needs in FY2020/21 supported by clear presentation of their necessity.	Prior action	Reduce fiscal risks related to SOEs.
State-owned enterprises (SOEs) restructuring and governance		
Prepare a strategy for addressing financial pressures in the SOE sector including an in-depth and forward-looking financial evaluation of the top 15-20 SOEs representing the largest financial and fiscal risks, a framework for deciding on interventions, and reforms to rationalize the SOE sector.	End-May 2021	Reduce fiscal risks related to SOEs.
Include in the annual Budget Review and Outlook paper an expanded fiscal risk analysis that quantifies contingent liabilities stemming from high-risk SOEs and initiate coverage of PPPs.	End-September 2021	Improve transparency and accessibility of information on the broader public sector to improve fiscal policy planning and reduce fiscal risks.
Fiscal transparency		
Initiate regular quarterly reporting on pending bills, covering Ministries, Departments and Agencies (MDAs), Counties, Semi-Autonomous Government Agencies (SAGAs) and State Corporations (SCs).	End-March 2021	Enhance fiscal transparency in a critical area.
Publish the results of an audit of all COVID-19-related expenditures in FY2019/20.	End-May 2021	Safeguard public resource and enhance transparency and accountability.
Ensure that comprehensive information on public tenders awarded, including beneficial ownership information of the awarded entities, are publicly available on the government procurement information portal, and that bidders are subject to dissuasive sanctions for non-compliance.	End-June 2021	Reduce corruption risks by strengthening transparency and enhancing oversight.
Start publication of annual report on tax expenditures and their budget implications.	End-September 2021	Strengthen transparency and enhance oversight.

Table 2. Kenya: Proposed Structural Benchmarks (concluded)		
Measure	Target Date	Macro-criticality
Revenue collection		
Submit to Parliament a budget for FY2021/22 consistent with the programed deficit target.	End-April 2021	Ensure fiscal consolidation consistent with program objectives.
Increase by 30 percent the number of Level II audits of firms, using risk-based approaches to select taxpayers with focus on industry sectors with large gaps in compliance identified by the IMF VAT-Gap analysis.	End-December 2021	Increase compliance and tax revenue.
Public financial management		
Issue decision to implement across MDAs, Counties, and SAGAs a common payroll system linked to IFMIS.	End-June 2021	Contain growth and improve efficiency of expenditure and reduce corruption risks.
Public investment management		
Complete stocktaking of existing projects and associated commitments in the areas of education, health, and infrastructure, enter the results in the Hyperion system, and identify projects to be rationalized.	End-March 2021	Improve debt management and efficiency of spending.
Monetary policy framework		
Publish a white paper outlining strategy to strengthen and modernize the monetary policy framework.	End-June 2021	Strengthen the capacity to implement monetary policy effectively in the context of flexible inflation targeting.

Attachment II. Technical Memorandum of Understanding

Nairobi, Kenya, March 19, 2021

1. This memorandum sets out the understandings between the Kenyan authorities and the IMF regarding the definitions of quantitative performance criteria (QPCs) and indicative targets (ITs), their adjusters and data reporting requirements for the Extended Fund Facility (EFF) and Extended Credit Facility (ECF) arrangements.

2. For the purposes of the program, the National Government of Kenya (GOK) corresponds to the budgetary national government encompassing the activities of the national executive, legislative and judicial powers covered by the National Budget. Specifically, it includes the parliament, national judiciary, and executive including Ministries, Departments, Agencies (MDAs), and Constitutional Commissions and Independent Offices.

QUANTITATIVE PERFORMANCE CRITERIA AND BENCHMARKS

3. The program establishes quantitative performance criteria for March 31, 2021, June 30, 2021, December 31, 2021, and June 30, 2022 with respect to:

- the primary balance of the national government including grants, cash basis (**floor**);
- tax revenue of the national government (**floor**);¹
- the stock of net official international reserves (NIR) of the Central Bank of Kenya (CBK) (**floor**);
- contracting or guaranteeing of new external non-concessional borrowing by the national government and the CBK (**ceiling**);
- contracting or guaranteeing of new external concessional borrowing by the national government and the CBK (**ceiling**);
- accumulation of public and publicly guaranteed external public arrears (**continuous ceiling**);
- new domestic guarantees granted by the national government or assumption of state-owned enterprise (SOE) debt not reflected in the primary balance (**ceiling**); and
- a monetary policy consultation clause (**band**).

4. The program sets indicative targets for March 31, 2021, June 30, 2021, December 31, 2021, and June 30, 2022 with respect to:

- tax revenue of the national government (**floor**);²
- the change in the stock of national government exchequer requests outstanding for 90 days or more (**ceiling**); and
- priority social spending of the national government (**floor**).

¹ This QPC would be in place starting from the third review of the program.

² Starting from the third review of the program, this IT will be converted into a QPC.

PERFORMANCE CRITERION ON THE PRIMARY BALANCE OF THE NATIONAL GOVERNMENT

5. The **national government primary balance** on a cash basis is defined as national government revenues and grants minus expenditures and net lending, plus due interest payments. For the purpose of the program, all operations such as debt swap or exchange of financial assets between the national government and SOEs with negative equity as of end-June 2020 would be recorded as a reduction in net lending and an increase in grants to SOEs.

6. For program purposes, the **national government primary balance** on a cash basis will be measured from the financing side as the sum of the following: (a) the negative of net domestic financing of the national government; (b) the negative of net external financing of the national government; and (c) domestic and external interest payments of the national government. For the end-March 2021 and end-June 2021 test dates, and for the end-December 2021 and end-June 2022 test dates, the national government primary balance will be measured cumulatively from July 1, 2020 and July 1, 2021, respectively.

The above items are defined as follows:

- **Net domestic financing** of the national government is comprised of (1) net domestic bank financing (which would include items such as credit to the government from commercial banks and the CBK, including the overdraft facility; changes in bank holdings of government debt; and drawdown of government deposits held at commercial banks or the CBK); (2) net domestic nonbank financing (such as changes in non-bank holdings of government debt); (3) proceeds from privatization; and (4) any other borrowing securitized by, or otherwise to be repaid with national government revenue.
- **Net external financing** of the national government at actual transaction exchange rates is defined as the sum of:
 - disbursements of external project loans, including securitization;
 - disbursements of budget support loans;
 - the negative of principal repayments due on all external loans;
 - net proceeds from issuance of external debt;
 - any exceptional financing (including rescheduled principal and interest on external debt);
 - net changes in the stock of short-term external debt; and
 - any change in external arrears including interest payments.
- **Domestic and external interest payments** of the national government are defined as the due interest charges on domestic and external national government debt.

7. The following adjustors will apply to the target on the **national government primary balance**:

- The floor will be adjusted downward by half of any extraordinary SOE support in FY2021/22 and FY2022/23 up to a cumulative amount of 1.0 percent of GDP in such support over that period. Extraordinary SOE support is defined as spending on current and capital transfers to SOEs included in the GFS 2014 category "Grants to Other General Government Units" (item

263 and subitems), reported in Annex III Table “Expense (KSh. Millions)” available from the National Treasury’s publication [Quarterly Economic and Budgetary Review](#), in excess of the amounts specified in TMU Table 1. The current coverage of SOEs in the national government’s budget will be refined in subsequent reviews of the EFF/ECF arrangements to reflect the findings of the financial evaluation of key SOEs with largest fiscal risk to the FY2020/21 budget (prior action) as well as the medium-term objectives of the strategy to reform the sector (structural benchmark for end-May 2021).

	2021			2022
	Mar.	Jun.	Dec.	Jun.
Budgetary transfers to SOEs	625,336	833,781	437,735	875,470

Source: Kenyan authorities.
¹ Cumulative from July 1, 2020 for FY2020/21 and from July 1, 2021 for FY2021/22.

- The floor will be adjusted upward (downward) if budgetary program grants not specifically related to COVID-19 vaccination exceed (fall short of) the programmed amounts set out in TMU Table 2 below.
- If resources to finance COVID-19 vaccination become available by the 2nd Review of the EFF/ECF arrangements, the floor will be adjusted downward by the amount of foreign concessional project financing dedicated to COVID-19 vaccine interventions and any COVID-19 vaccine related import cost not covered by foreign concessional project financing. The rationale for this adjustment will be reassessed in the context of the 2nd Review of the EFF/ECF arrangements.

	2021			2022
	Mar.	Jun.	Dec.	Jun.
Program grants	5,182	7,404	1,125	2,500

Source: Kenyan authorities.
¹ Cumulative from July 1, 2020 for FY2020/21 and from July 1, 2021 for FY2021/22.

PERFORMANCE CRITERION ON THE NET INTERNATIONAL RESERVES OF THE CENTRAL BANK OF KENYA

8. The stock of net official international reserves (NIR) of the CBK will be calculated as the difference between total gross official international reserves and official reserve liabilities.

- **Gross official international reserves** are defined as the sum of:
 - the CBK’s holdings of monetary gold (excluding amounts pledged as collateral);
 - holdings of Special Drawing Rights (SDRs);
 - CBK holdings of convertible currencies in cash or in nonresident financial institutions (deposits, securities, or other financial instruments); and
 - Kenya’s reserve tranche position with the IMF.
- **Gross official usable international reserves** exclude:
 - pledged, swapped, or any encumbered reserve assets, including but not limited to reserve assets used as collateral or guarantees for third-party external liabilities;
 - deposits with Crown agents; and
 - precious metals other than gold, assets in nonconvertible currencies and illiquid foreign assets.
- **Gross official reserve liabilities** are defined as:
 - the total outstanding liabilities of the CBK to the IMF, excluding the SDR allocations;
 - convertible currency liabilities of the CBK to nonresidents with an original maturity of up to and including one year; and
 - commitments to sell foreign exchange arising from derivatives (such as futures, forwards, swaps, and options).

9. The following **adjustors** will apply to the target for NIR:

- If the total of (i) program loans, (ii) the revenue component of project loans and (iii) external commercial and semi-concessional borrowing—excluding for payments of principal of existing debt with the proceeds from newly issued debt for debt management purposes (¶21 bullet a)—exceeds (falls short) the programmed amounts set out in TMU Table 3 below, the target for NIR will be adjusted upward (downward) by the difference;
- If program grants or the revenue component of project grants falls short of the programmed amounts set out in TMU Table 3 below, the target for NIR will be adjusted downward by the difference;
- The NIR target will be adjusted downward by the full amount of import costs associated with COVID-19 vaccine purchases less any external project financing received for this purpose. The rationale for this adjustment will be reassessed in the context of the 2nd Review of the EFF/ECF arrangements.

Table 3. Kenya: Projected Government Grants and Borrowing¹

(US\$ millions)

	2021			2022
	Mar.	Jun.	Dec.	Jun.
Program loans and grants	577	1880	1039	1341
Of which: grants	48	67	5	22
Project loans and grants (revenue component)	525	825	284	740
Of which: grants	121	170	35	99
External commercial and semi-concessional borrowing	0	1125	0	1266

Source: Kenyan authorities.

¹ Cumulative from July 1, 2020 for FY2020/21 and from July 1, 2021 for FY2021/22.

- If the pledged DSSI relief exceeds (falls short of) the programmed amounts set out in TMU Table 4 below, the target for NIR will be adjusted upward (downward) by the difference.

Table 4. Kenya: DSSI Relief¹

(US\$ millions)

	2021			2022
	Mar.	Jun.	Dec.	Jun.
Total DSSI relief	433.7	639.4	0.0	0.0

Source: Kenyan authorities.

¹ Cumulative from July 1, 2020 for FY2020/21 and from July 1, 2021 for FY2021/22.

10. NIR is monitored in U.S. dollars, and, for program monitoring purposes, assets and liabilities in currencies other than the U.S. dollar shall be converted into dollar equivalent values, using the exchange rates as specified in TMU Table 5 below, and net international reserves will be computed as the daily average for the month of the applicable test date.

Table 5. Kenya: Program Exchange Rates

(Rates as of February 4, 2021)

Currency	Kenyan Shillings per currency unit	Currency units per US Dollar
US Dollar	109.8647	1.00
STG Pound	149.8768	0.73
Japanese Yen	1.045882	105.05
Canadian Dollar	85.7648	1.28
Euro	131.9809	0.83
Swiss Franc	122.2213	0.90
Swedish Kronor	13.0437	8.42
Danish Kronor	17.7509	6.19
Chinese Yuan	17.0114	6.46
Australian Dollar	83.662	1.31
SDR	157.464	0.70

Source: Central Bank of Kenya.

CONTINUOUS PERFORMANCE CRITERION ON THE PUBLIC AND PUBLICLY-GUARANTEED EXTERNAL PAYMENT ARREARS

11. Public and publicly-guaranteed external payment arrears to official and private external creditors are defined as overdue payments (principal or interest), which were not made by their contract due date nor during the applicable grace period thereafter, on debt contracted by the national government. Public and publicly-guaranteed external debt payment arrears (principal or interest) to official and private creditors are defined as overdue payments beyond 30 days after the original contract due date in order to allow sufficient time to process the due repayment after the original debtor has notified of its inability to pay. The definition excludes arrears relating to debt subject to renegotiation (dispute or ongoing renegotiation in accordance to both parties) or rescheduling. External debt is defined on a currency basis.

12. The performance criterion on the public and publicly-guaranteed external payment arrears is defined as a cumulative flow in gross terms from January 1, 2021 and applies on a continuous basis.

CEILING ON THE CONTRACTING OR GUARANTEEING OF NEW NON-CONCESSIONAL AND CONCESSIONAL EXTERNAL DEBT

13. For program purposes and this TMU, the definition of debt is set out in paragraph 8(a) of the Guidelines on Public Debt Conditionality in Fund Arrangements attached to [Executive Board Decision No.15688-\(14/107\)](#), adopted December 5, 2014.

14. External debt is any debt as defined in paragraph 13, which is denominated in foreign currency, i.e., currency other than Kenyan Shillings (KSh). For debt with original maturity of one year

or less, new debt would be measured as the change in the outstanding stock over the specified period. The ceiling does not apply to the use of Fund resources. External debt and its concessionality will be measured in U.S. dollars at program exchange rates.

15. The performance criterion or indicative target will include all forms of debt. For the purpose of these guidelines, the term “debt” will be understood to mean a current, i.e., not contingent, liability, created under a contractual arrangement through the provision of value in the form of financial and nonfinancial assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms; the primary ones being as follows:

- (i) loans, i.e., advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans and buyers’ credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements);
- (ii) suppliers’ credits, i.e., contracts where the supplier permits the obligor to defer payments until sometime after the date on which the goods are delivered or services are provided; and
- (iii) leases, i.e., arrangements under which property is provided which the lessee has the right to use for one or more specified period(s) of time that are usually shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement excluding those payments that cover the operation, repair, or maintenance of the property.

16. Under the definition of debt set out above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.

17. Performance criteria (ceiling) apply to the nominal value of new non-concessional external debt and the nominal value of new concessional external debt, contracted or guaranteed by the national government and/or the CBK. The ceiling applies to debt and commitments contracted or guaranteed for which value has not yet been received, including private debt for which official guarantees have been extended.

18. The ceiling on the nominal value of new concessional external debt, contracted or guaranteed by the national government and/or the CBK, would be adjusted upward for the full amount of any project financing dedicated to COVID-19 vaccine interventions. In this connection,

the authorities will consult with IMF staff on any planned external concessional borrowing for this purpose and the conditions on such borrowing before the loans are either contracted or guaranteed by the government. The rationale for this adjustment will be reassessed in the context of the 2nd Review of the EFF/ECF arrangements.

19. For program purposes, a debt is concessional if it includes a grant element of at least 35 percent, calculated as follows: the grant element of a debt is the difference between the net present value (NPV) of debt and its nominal value, expressed as a percentage of the nominal value of the debt. The NPV of debt at the time of its signing date of an underlying loan agreement is calculated by discounting the future stream of payments of debt service due on this debt. The discount rate used for this purpose is 5 percent. A debt with a grant element lower than 35 percent is considered non-concessional.

20. For any debt carrying a variable interest rate in the form of a benchmark interest rate plus a fixed spread, the PV of the debt would be calculated using a program reference rate plus the fixed spread (in basis points) specified in the debt contract. The program reference rate for the six-month USD SOFR is 0.04 percent and will remain fixed for the duration of the program. The spread of six-month Euro EURIBOR over six-month USD SOFR is -56 basis points. The spread of six-month JPY OIS over six-month USD SOFR is -8 basis points. The spread of six-month GBP SONIA over six-month USD SOFR is 1 basis point. For interest rates on currencies other than Euro, JPY, and GBP, the spread over six-month USD SOFR is 15 basis points.³ Where the variable rate is linked to a benchmark interest rate other than the six-month USD SOFR, a spread reflecting the difference between the benchmark rate and the six-month USD SOFR (rounded to the nearest 50 bps) will be added.

21. The performance criterion on contracting or guaranteeing new external non-concessional debt includes two sub-ceilings:

- a. Debt for debt management operations that improves the overall public debt profile; operations that improve the overall debt profile are operations that reduce the present value of external debt and improve the external debt service profile. Refinancing of principal payments—payments of principal of existing debt with the proceeds from newly issued debt for debt management purposes—will count against this sub-ceiling and must improve the overall public debt profile as specified. Refinancing of outstanding interest payments using the proceeds from non-concessional borrowing for debt management purposes is not permitted under this sub-ceiling and will result in non-observance of the performance criterion. This sub-ceiling shall be cumulative from the beginning of the program.
- b. Debt (including bond issuance) for financing projects integral to the development program for which concessional financing is not available; this sub-ceiling refers to debt to finance the projects specified in the list below (ANNEX I). Any contracting or guaranteeing of non-concessional external debt for projects other than those listed in

³ The program reference rate and spreads are based on the “average projected rate” for the six-month USD SOFR over the following 10 years from the Fall 2020 World Economic Outlook (WEO).

ANNEX I results in the non-observance of the performance criterion. This sub-ceiling shall be cumulative from the beginning of the program. Amounts applied toward this limit do not count toward the sub-ceiling on non-concessional borrowing for debt management purposes.

CEILING ON NEW DOMESTIC GUARANTEES GRANTED BY THE NATIONAL GOVERNMENT

22. National government guarantees on domestic borrowing include all guarantee commitments for (i) borrowing in domestic currency from residents and nonresidents; as well as (ii) guarantees extended by any SOE.

MONETARY POLICY CONSULTATION CLAUSE

23. The bands around the projected 12-month rate of inflation in consumer prices, as measured by the headline consumer price index (CPI) published by the Kenya National Bureau of Statistics, are specified in the TMU Table 6 below.

- If the observed average of the 12-month rate of CPI inflation for the three months preceding the test date falls outside the lower or upper bands specified in the TMU Table 6 below, the authorities will complete a consultation with the IMF Executive Board which would focus on: (i) the stance of monetary policy and whether the Fund-supported program remains on track; (ii) the reasons for program deviations, taking into account compensating factors; and (iii) proposed remedial actions if deemed necessary. When the consultation with the IMF Executive Board is triggered, access to Fund resources will be interrupted until the consultation takes place.

	end–Mar. 2021 Target	end–Jun. 2021 Target	end–Dec. 2021 Target	end–Jun. 2022 Target
Upper band	7.5	7.5	7.5	7.5
<i>Center point</i>	5.0	5.0	5.0	5.0
Lower band	2.5	2.5	2.5	2.5

Source: Kenyan authorities.

FLOOR ON TAX REVENUE OF NATIONAL GOVERNMENT (INDICATIVE TARGET AND QUANTITATIVE PERFORMANCE CRITERION)

24. Tax revenue of the national government are defined as the sum of personal income tax (PAYE), corporate income tax, import duties, excise duties, value added tax, and other taxes (e.g.,

alternative minimum tax, digital sales tax). For the purpose of the program, tax revenues exclude the following items presented in the monthly Budget Outturn Tables (BOT): taxes related to “Ministerial Appropriation in Aid” (i.e., RML, RDL, PDL), “Taxes on International Trade and Transactions (IDF fee),” “Capital gains,” and “other taxes on goods and services.”

INDICATIVE TARGET ON NATIONAL GOVERNMENT OUTSTANDING EXCHEQUER REQUESTS

25. For the purposes of the program, national government outstanding exchequer requests are defined as invoices for goods or services provided to the national government for which requisitions for payment have been received in the Integrated Financial Management Information System (IFMIS) but corresponding funds from the exchequer account have not been released.

26. The program ceiling for the change in the stock of outstanding exchequer requests refers to requisitions made after the start of July 2020 and invoices unpaid for 90 days or longer, disregarding any changes related to legal rulings or claims found invalid on bills originated before the start of the program.

INDICATIVE TARGET ON PRIORITY SOCIAL SPENDING

27. For the purposes of the program, priority social spending of the national government is defined as the sum of:

- cash transfers to orphans and vulnerable children,
- cash transfers to elderly persons,
- cash transfers to persons with severe disabilities,
- free primary education expenditure,
- free secondary education expenditure,
- school food and sanitary programs,
- free maternal healthcare,
- universal health coverage,
- health insurance subsidy for targeted categories (i.e., orphan, vulnerable children, the elderly, and people with disabilities), and
- spending for vaccination and immunization.

The floor on priority social spending of the national government is defined as the programmed amounts set out in TMU Table 7 in next page.

Table 7. Kenya: Priority Social Spending¹
(KSh. millions)

	2021			2022
	Mar.	Jun.	Dec.	Jun.
Priority Social Spending	292,611	390,978	205,395	397,320

Source: Kenyan authorities.

¹ Cumulative from July 1, 2020 for FY2020/21 and from July 1, 2021 for FY2021/22.

DATA REPORTING

28. To monitor program performance, the National Treasury and the CBK will provide to the IMF the information at the frequency and within the reporting deadlines specified in TMU Table 8 below. The authorities will transmit promptly to Fund staff any data revisions. For any information (and data) that is (are) relevant for assessing performance against program objectives but is (are) not specifically defined in this memorandum, the authorities will consult with Fund staff. The authorities will transmit promptly to IMF staff any data revisions, as well as other information necessary to monitor the arrangements with the IMF.

Table 8. Kenya: Summary of Data to Be Reported

Information	Frequency	Reporting Deadline	Responsible Entity
1. Primary balance of the national government			
Net domestic bank financing (including net commercial bank credit to the national government and net CBK credit to the national government broken down in their main components)	Monthly	Within 20 days after month end.	CBK
Net nonbank financing of the national government	Monthly	Within 20 days after month end.	NT
Proceeds from privatization	Monthly	Within 20 days after month end.	NT
Debt service paid and coming due on domestic debt	Monthly	Within 20 days after month end.	CBK
Debt service paid and coming due on external debt	Monthly	Within 20 days after month end.	NT
Disbursements and repayment schedule of external concessional and non-concessional project loans, including securitization	Monthly	Within 20 days after month end.	NT
Disbursements and repayment schedule of budget support loans	Monthly	Within 20 days after month end.	NT
Disbursements and repayment schedule of on all external loans	Monthly	Within 20 days after month end.	CBK
Net proceeds from issuance of external debt	Monthly	Within 20 days after month end.	CBK
Any exceptional financing (including rescheduled principal and interest)	Monthly	Within 20 days after month end.	NT
Net changes in the stock of short-term external debt	Quarterly	Within 45 days after quarter end.	NT
Change in external arrears, including interest and principal, and penalties	Monthly	Within 20 days after month end.	NT
Stock and movements in MDAs' pending bills for prior fiscal years	Monthly	Within 20 days after month end.	NT
Stock of exchequer requests made after the start of July 2020 and unpaid for 90 days or more	Monthly	Within 20 days after month end.	NT
National government transfers to SOEs broken down in main categories based on GFS 2014 classification	Quarterly	Within 20 days after the end of the quarter.	NT
2. Public debt			
Stock of Treasury Bills and Bonds	Quarterly	Within 45 days after quarter end.	NT
Auctions of T-bills and T-bonds via primary dealers, including the number and value of submitted and accepted bids, minimum, maximum and weighted average interest rates and maturity dates	Weekly	Within 7 working days after the end of the week.	NT
Total new other domestic debt contracted or guaranteed	Monthly	Within 20 days after the end of the quarter.	NT in collaboration with CBK
Total new contracted external project loans	Monthly	Within 20 days after the end of the quarter.	NT
Total other new contracted or guaranteed external concessional debt	Monthly	Within 20 days after the end of the quarter.	NT in collaboration with CBK
Total new Eurobond issuances	Monthly	Within 20 days after the end of the quarter.	NT
Total new other non-concessional external debt contracted or guaranteed	Monthly	Within 20 days after the end of the quarter.	NT in collaboration with CBK

Table 8. Kenya: Summary of Data to Be Reported (concluded)

Information	Frequency	Reporting Deadline	Responsible Entity
3. Gross official international reserves			
CBK's holding of monetary gold (excluding amounts pledged as collateral)	Monthly	Within 20 days after the end of the month.	CBK
Holdings of SDRs	Monthly	Within 20 days after the end of the month.	CBK
CBK holdings of convertible currencies in cash or in nonresident financial institutions (deposits, securities, or other financial instruments)	Monthly	Within 20 days after the end of the month.	CBK
4. Official reserve liabilities			
Total outstanding liabilities of the CBK to the IMF excluding the SDR allocations	Monthly	Within 20 days after month end.	CBK
Convertible currency liabilities of the CBK to nonresidents with an original maturity of up to and including one year	Monthly	Within 20 days after month end.	CBK
Commitments to sell foreign exchange arising from derivatives	Monthly	Within 20 days after month end.	CBK
5. Other indicators			
Currency in circulation	Monthly	Within 20 days after month end.	CBK
Required and excess reserves	Monthly	Within 20 days after month end.	CBK
Concessional and non-concessional medium- and long-term external debt contracted or guaranteed by the national government and CBK	Monthly	Within 20 days after month end.	NT
Accumulation of national government external payment arrears	Monthly	Within 20 days after the end of the quarter.	NT
Social priority spending of the national government	Quarterly	Within 45 days after quarter end.	NT
Grants to government entities and total subsidies	Quarterly	Within 20 days after month end.	NT
Guarantees issued by the national government to counties, public enterprises, and all parastatal entities	Monthly	Within 20 days after the end of the quarter.	NT
Stock of guarantees extended by the national government	Monthly	Within 20 days after the end of the quarter.	NT
12-month CPI inflation	Monthly	Within 15 days after the end of the month.	KNBS
Financial Soundness Indicators (core and expanded) for other depository corporations	Quarterly	Within 20 days after quarter end.	CBK

Annex I. List of Projects

Project	Sector
1 Digital Learning	
2 E-Government Services	
3 ICT and BPO Development	Access to Universal Information
4 ICT Infrastructure Connectivity	
5 Cooperative Development and Management	
6 Fisheries, Aqua Culture and Blue Economy	
7 Food Security and Crop Diversification Project	
8 KAGRC Liquid Nitrogen	
9 Livestock Resources development and Management	Agricultural Production and Management
10 Mechanization of Agricultural Development Project	
11 National Value Chain Support Programme	
12 Promotion of Industrial Development and Investments	
13 Provision of Credit to MSMEs in Manufacturing sector- KIE	
14 Construction of Computer Labs to Support Digital Literacy Programme	
15 Infrastructure Development and Expansion of TVETs	
16 Renovation and expansion of infrastructure in public primary schools	
17 Renovation and expansion of infrastructure in public Secondary schools	Education
18 University Education	
19 Vocational Training and Research	
20 Vocational Training Centres Support (Youth Polytechniques)	
21 National Grid System	Energy
22 Rural Electrification	
23 Correctional Facilities	Enhanced Security
24 Digitization of Land registries	
25 Forests and Water Towers Conservation	
26 Irrigation and Drainage	
27 Processing and Registration of Title deeds	
28 Sanitation Infrastructure Development and Management	Environment Protection and Management
29 Sewerage Infrastructure Development	
30 Water Harvesting and Storage for Irrigation	
31 Water Resources Conservation and Protection	
32 Water Storage and Flood Control	
33 Construction of Affordable Housing Units	
34 Construction of Housing Units for National Police & Kenya Prison	Improvement of Housing Planning and Infrastructure
35 Construction of Markets and Fire Stations	
36 Kenya Informal Settlements Improvement & slum upgrading projects	
37 Construction of Roads and Bridges and Roads rehabilitation	
38 Expansion of Airports and air strips (Malindi, Lanet, Migori)	Improvement of Infrastructure
39 Lamu Port- South Sudan- Ethiopia - Transport (LAPSSET) Project	
40 Special Economic Zones (Naivasha & Dongo Kundu)	
41 Expansion of Courts	Improvement/Access to Justice
42 Establishment of Regional Cancer Centres	
43 Expansion of Referral Hospitals	
44 Forensic and Diagnostics	
45 Free Maternity Program	Universal Health Coverage
46 Managed Equipment Service-Hire of Medical Equipment for 98 Hospital	
47 Reproductive Maternal Neo-natal Child & Adolescent Health-RMNCAH	
48 Roll-out of Universal Health Coverage, COVID-19 response and mitigation strategy	
49 Human wildlife mitigation programme	
50 Maintenance of Access Roads and Airstrips in Parks	Wildlife conservation/Tourism Promotion and Marketing
51 Tourism Infrastructure Development and Promotion	



KENYA

REQUESTS FOR AN EXTENDED ARRANGEMENT UNDER THE EXTENDED FUND FACILITY AND AN ARRANGEMENT UNDER THE EXTENDED CREDIT FACILITY—DEBT SUSTAINABILITY ANALYSIS

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Joint Bank-Fund Debt Sustainability Analysis	
Risk of external debt distress	High
Overall risk of debt distress	High
Granularity in the risk rating	Sustainable
Application of judgment	No

Kenya's debt is sustainable, and its debt dynamics will be bolstered by the fiscal consolidation envisaged under the IMF supported program. While planned fiscal consolidation will help address debt vulnerabilities exacerbated by the global COVID-19 shock, the risk of debt distress continues to be assessed as high.¹ High deficits—from the past and generated by the current shock—combined with the sharp decline in export and economic growth caused by the pandemic, have deteriorated solvency and liquidity debt indicators, particularly when measured against Kenya's current debt-carrying capacity (evaluated as medium).² Kenya's debt indicators will improve as fiscal consolidation progresses and exports and output recover from the global shock, although improvement is particularly gradual for indicators in terms of exports. Sustained fiscal consolidation would stabilize debt towards the end of the program and bring it to more prudent levels over the medium term while securing resources to support social spending. Kenya has generally enjoyed strong access to international capital markets, and staff projections assume limited reliance on market financing over the coming three years and roll-over of existing Eurobonds. The DSA suggests that Kenya is susceptible to export and exchange rate shocks; more prolonged and protracted shocks to the economy would also present downside risks to the debt outlook.

¹ Kenya was first assessed as being at high risk of debt distress in May 2020. [IMF Country Report No. 20/156](#) (May 2020) contains the previous DSA conducted jointly with the World Bank.

² The Composite Indicator for Kenya is estimated at 3.01, which translates into a *Medium* Debt-Carrying Capacity Assessment, revised from *Strong*. It is based on the 2020 October WEO and CPIA vintage released on July 2020.

PUBLIC DEBT COVERAGE

1. Kenya's public debt includes obligations of the central government. Debt data include both external and domestic obligations and guarantees. The external DSA covers external debt of the central government and the central bank, as well as of the private sector; and stress tests apply to public and publicly guaranteed (PPG) debt. The public DSA covers both external and domestic debt incurred or guaranteed by the central government, and public domestic debt consists of central government debt. In this analysis, total public debt refers to the sum of public domestic and public external debt, however, it does not cover the entire public sector such as extra-budgetary units and county governments.³ Debt coverage excludes legacy debt of the pre-devolution county governments (whose size is modest).⁴ In comparison to peers, Kenya maintains a high standard of debt transparency. The external public debt register includes granular data disclosure, which could be more regularly updated.⁵ The DSA uses a currency-based definition of external debt, as nonresidents' direct participation in the domestic debt market, at about one percent of total outstanding government securities, is not significant.

2. The DSA includes contingent liability stress tests for SOEs, PPPs, and a financial market shock. In particular, the DSA incorporates:

- 3.1 percent of GDP to capture non-guaranteed debt of state-owned enterprises (SOEs) and Public Private Partnerships (PPPs). Notably, the baseline already incorporates the 0.3 percent of GDP assumed for SOE support as well as amounts borrowed directly by the Kenyan government and on-lent to SOEs.⁶
- 5 percent of GDP for a loan default financial market shock—a value that exceeds the existing stock of financial sector NPLs of about 4 percent of GDP.

BACKGROUND ON DEBT

3. Kenya's overall public debt has increased in recent years. Gross public debt increased from 48.6 percent of GDP at end-2015 to an estimated 69 percent of GDP at end-2020, reflecting high deficits, partly driven by past spending on large infrastructure projects, and in 2020 by the COVID-19 global shock. About half of Kenya's public debt is owed to external creditors.

4. Most of Kenya's external public debt remains on concessional terms. Nominal PPG external debt at end-2020 amounted to 35.6 percent of GDP, about four percentage points higher than at end-2019.

³ County governments have not been allowed to borrow without government guarantee since 2010 and borrowing requires National Treasury (NT) authorization while extra-budgetary units face no such constraint.

⁴ A new Constitution was approved by referendum in 2010, devolving substantial powers to 47 new county governments.

⁵ Debt statistics bulletins with PPG coverage and debt management strategies are regularly published. Also, the Budget Policy Statement publishes contingent liabilities.

⁶ This includes the external debt associated with the Standard Gauge Railway (SGR).

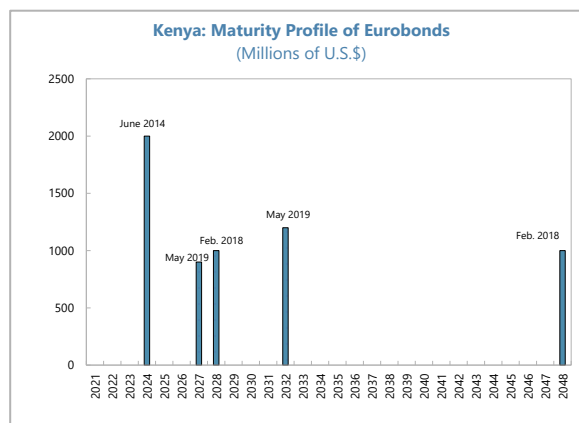
Kenya: Public Debt Coverage

Subsectors of the public sector	Subsectors Covered	
1 Central government	X	
2 State and local government		
3 Other elements in the general government		
4 o/w: Social security fund	X	
5 o/w: Extra budgetary funds (EBFs)		
6 Guarantees (to other entities in the public and private sector, including to SOEs)	X	
7 Central bank (borrowed on behalf of the government)	X	
8 Non-guaranteed SOE debt		

1 The country's coverage of public debt	The central government plus social security, central bank, government-guaranteed debt	
	Default	Used for the analysis
2 Other elements of the general government not captured in 1.	0 percent of GDP	0
3 SoE's debt (guaranteed and not guaranteed by the government) 1/	2 percent of GDP	2
4 PPP	35 percent of PPP stock	1.1
5 Financial market (the default value of 5 percent of GDP is the minimum value)	5 percent of GDP	5
Total (2+3+4+5) (in percent of GDP)		8.1

1/ The default shock of 2% of GDP will be triggered for countries whose government-guaranteed debt is not fully captured under the country's public debt definition (1.). If it is already included in the government debt (1.) and risks associated with SoE's debt not guaranteed by the government is assessed to be negligible, a country team may reduce this to 0%.

- At end-2020, multilateral creditors accounted for about 40 percent of external debt, while debt from bilateral creditors represented close to 33 percent. Of Kenya's bilateral debt, about 63 percent is owed to non-Paris Club members, mainly loans from China to finance construction of the Standard Gauge Railway (SGR) project.
- External commercial debt decreased in 2020, as the authorities prioritized concessional borrowing during the pandemic after several years of reliable access to global financial markets. Commercial debt (mainly Eurobonds and syndicated loans) accounted for about 26 percent of external public debt at end-2020—modestly above its share at end-2015. Eurobonds account for 70 percent of commercial debt (US\$6.1 billion), while syndicated loans represent 27 percent (about \$2.5 billion).



Kenya: External Public Debt

	2015		2016		2017		2018		2019		2020	
	US\$bn	Share	US\$bn	Share	US\$bn	Share	US\$bn	Share	US\$bn	Share	US\$bn	Share
Multilateral creditors	7.3	46.5	7.6	41.2	8.2	35.8	8.6	32.1	10.2	33.4	13.7	39.7
Bilateral creditors	4.7	29.8	6.3	33.8	7.6	33.3	8.8	32.8	10.1	33.0	11.3	32.7
Commercial creditors	3.6	22.7	4.5	24.2	6.9	30.1	9.2	34.4	10.2	33.1	8.9	25.9
Others (supplier credits)	0.2	1.0	0.1	0.8	0.2	0.7	0.2	0.6	0.2	0.5	0.6	1.7
Total	15.8	100	18.5	100	22.8	100	26.7	100	30.7	100	34.5	100

Source: Kenyan National Treasury.

5. Kenya's domestic public debt reached 33 percent of GDP at end-2020. Domestic debt is issued mostly in the form of Treasury bonds (about 70 percent of the total stock) and Treasury bills. The 91-day, 182-day, and 364-day average interest rates were 6.9 percent, 7.4 percent and 8.3 percent respectively in December 2020. The average time to maturity for government domestic debt securities increased from 5¾ years at end-2019 to 7.9 years at end-2020, as the authorities successfully implemented their strategy to lengthen the maturity profile of domestic debt. About half of government domestic debt securities are held by commercial banks, followed by pension funds.

UNDERLYING ASSUMPTIONS

6. Under the baseline scenario, solid growth is expected over the medium term. Despite a slowdown in 2020 driven by the global COVID-19 shock, medium-term growth prospects remain favorable and broadly in line with past performance. In 2021 the recovery will be driven by manufacturing and services, particularly education, transportation and trade (wholesale and retail)—activities that have recently rebounded after being particularly affected by the lockdowns implemented to address the health crisis. Estimated growth for 2021 is significantly affected by base effects, including the methodological approach that better captured the impact of school closures and their reopening; non-education growth is in line with the historical trend as some sectors show healthy recovery while others still face challenges. The expectation under the baseline is that, after this rebound from the COVID19 shock, the economy will settle at its potential growth (roughly 6 percent) over the medium to long term.⁷ Medium-term growth is supported by the reform agenda envisaged under the proposed EFF/ECF program, which should underpin a healthy investment rate, particularly private investment, as well as the favorable prospects for external demand propelling exports. Exports of goods and services are projected to reach 13.3 percent of GDP in 2025, broadly the same share as observed in 2018.⁸ Inflation is expected to remain close to the middle of the authorities' target range in the near and medium term.

Kenya: Selected Macroeconomic Indicators									
	2013	2014	2015	2016	2017	2018	2019	2020	
	Actual						Prel.		
Real GDP growth (percent)	5.9	5.4	5.7	5.9	4.8	6.3	5.4	-0.1	
CPI inflation, average (percent)	5.7	6.9	6.6	6.3	8.0	4.7	5.2	5.3	
CPI inflation, eop (percent)	7.1	6.0	8.0	6.3	4.5	5.7	5.8	5.6	
Current account balance (percent of GDP)	-8.8	-10.4	-6.9	-5.8	-7.2	-5.7	-5.8	-4.8	
Overall fiscal balance (percent of GDP) ¹	-5.2	-6.1	-8.4	-7.4	-9.1	-7.4	-7.7	-7.8	
Gross international reserves (in billions of US\$)	6.4	8.0	7.5	7.5	7.1	8.1	9.1	8.3	
Gross international reserves (months of imports)	3.8	5.4	5.6	4.7	4.3	4.8	6.1	4.7	
Total public debt (gross, percent of GDP) ¹	41.1	46.8	47.9	53.5	57.4	59.3	62.1	65.9	
Private investment (percent of GDP)	14.3	17.2	15.1	9.0	9.7	8.6	8.0	7.0	
Credit to the private sector (y/y growth, percent)	20.1	22.2	17.3	4.4	2.5	2.4	7.1	7.7	

Sources: Kenyan authorities and IMF staff estimates and projections.
¹ Fiscal years (e.g., 2020 refers to FY 2019/20).

⁷ For comparison, the DSF published at the time of the May RCF, which did not reflect the assumption of IMF program engagement as under the current EFF/ECF arrangements, assumed a long-term growth rate of 5.8 percent.

⁸ See the External Sector Assessment for a discussion on export performance and longer-term competitiveness challenges.

7. The fiscal deficit reached 7.8 percent of GDP in 2019/20, 1.2 percentage points less than the deficit approved in the supplemental budget. Tax revenues declined to 13.6 percent of GDP in 2019/20—reflecting the economic slowdown and policy measures to address the COVID-19 shock, but also the gradual downward trend observed since 2013/14. Kenya’s revenue collection remains in line with the regional average. The decline in the deficit since 2016/17 has been mainly achieved through spending cuts to both current outlays and development spending. With strong adjustment under the proposed program, Kenya would reach the average debt-stabilizing primary deficit, estimated at 1.2 percent of GDP, in 2023; over the medium term the overall deficit is expected to decline and stay below 4 percent of GDP, with the primary surplus at 0.5 percent of GDP. In 2021 a significant share of financing is expected to come in the form of concessional and semi-concessional borrowing, including from the IMF and other multilaterals; financing from commercial lenders is estimated at \$1.1 billion as part of the authorities plan’ to limit reliance on external commercial borrowing in the coming years to reduce debt-related vulnerabilities. Having generally enjoyed strong access to the international capital markets, the authorities are also considering debt management operations if market conditions are favorable; debt management operations are not reflected in the baseline. Kenya is also expected to tap global capital markets to roll over Eurobonds as they mature.

	2017	2018	2019	2020	2021	Long-term 1/
Real GDP Growth						
Current DSA	4.8	6.3	5.4	-0.1	7.6	6.0
Previous DSA (May 2020)	4.8	6.3	5.4	0.8	5.5	5.8
Primary Fiscal Deficit (percent of GDP)						
Current DSA	4.5	3.7	3.6	4.1	3.7	-1.0
Previous DSA (May 2020)	4.5	3.7	4.0	4.1	3.1	0.3
Non-interest Current Account (percent of GDP)						
Current DSA	5.0	4.1	3.8	2.8	3.5	3.6
Previous DSA (May 2020)	5.0	3.5	2.9	2.9	2.8	2.8

Source: IMF staff estimates.
1/ Average for 2027-41.

8. The current account deficit amounted to 4.8 percent of GDP in 2020—one percentage point lower than in 2019. The current account performance was supported by resilient exports—tea and horticulture—and lower global energy prices; tourism receipts contracted on account of the COVID-19 crisis, while remittances performed strongly. Over the medium term, staff projects a stable current account deficit, supported by exports recovering from the COVID-19 shock and moderate import growth as the pace of development expenditure, which has a high import content, stabilizes. Under the baseline the current account deficit is expected to be financed by a diversified set of sources, including FDI and financial and non-financial corporate borrowing.

9. The realism tools flag some optimism compared to historical performance, but staff is of the view that the projections are reasonable (Figure 4). While protecting social spending, the baseline scenario assumes an improvement of the primary balance of 3.7 percentage points of GDP over the next three years, which falls in the top quartile of the distribution for LICs. Staff is of the view that this is realistic and in line with the authorities’ plan for fiscal consolidation under the program as set out in the 2021 Budget Policy Statement (BPS). The authorities’ commitment to fiscal

consolidation, including actions taken during the pandemic to broaden the tax revenue base and identify offsets to compensate for COVID-related expenditures, provide assurances that the fiscal adjustment under the program is achievable (see ¶119). The global and domestic recovery from the COVID shock and base effects associated with the crisis, including the methodological approach that better captured the impact of school closures and their reopening, substantiate the near-term growth trajectory during planned fiscal consolidation. Export growth is projected to be slightly higher than the recent past, which is justified as exports recover from Kenya's early 2019 drought and the 2020 global shock. By 2025, exports of goods and services are projected to return to a similar level as the share of GDP observed in 2018, supported by Kenya's improving business environment, key infrastructure projects coming to completion, large potential in a range of agricultural products, and the Big 4 Agenda push to stimulate manufacturing with a strong export emphasis. In the outer years, it is assumed that Kenya will continue to depend on concessional financing as part of a continuing commitment to reduce debt-related vulnerabilities.

**Kenya: Summary Table of Projected External Borrowing Program
from April 1, 2021 to June 30, 2022**

PPG external debt	Volume of new debt		PV of new debt 1/	
	April 2021 - June 2022		April 2021 - June 2022 (program purposes)	
	USD million	Percent	USD million	Percent
By sources of debt financing	12,376	100	10,342	100
Concessional debt, of which	4,765	39	2,787	27
Multilateral debt	2,420	20	1,451	14
Bilateral debt	2,345	19	1,336	13
Other	0	0	0	0
Non-concessional debt, of which	2,611	21	2,555	25
Semi-concessional	282	2	226	2
Commercial terms	2,329	19	2,329	23
Debt for Debt Management Operations (Non-Concessional)	5,000	40	5,000	48
By Creditor Type	12,376	100	10,342	100
Multilateral	2,702	22	1,677	16
Bilateral - Paris Club	579	5	343	3
Bilateral - Non-Paris Club	1,766	14	993	10
Private	2,329	19	2,329	23
Private for Debt Management Operations	5,000	40	5,000	48
Uses of debt financing	12,376	100	10,342	100
Infrastructure	4,295	35	3,522	34
Social Spending	755	6	428	4
Budget Financing	2,326	19	1,391	13
Potential Debt Management Operations 2/	5,000	40	5,000	48

Source: IMF calculations using Authorities' data.

1/ Contracting and guaranteeing of new debt. The present value of debt is calculated using the terms of individual loans and applying the 5 percent program discount rate. For commercial debt, the present value is defined as the nominal/face value.

2/ "Planned potential borrowing for debt management operations to improve the debt profile (in terms of PV and debt service). Debt management operations are not reflected in the baseline.

COUNTRY CLASSIFICATION AND DETERMINATION OF SCENARIO STRESS TESTS

10. Kenya's debt carrying capacity is assessed as Medium, given an estimated Composite Indicator (CI) of 3.01. The CI captures the impact of various factors through a weighted average of an institutional indicator,⁹ real GDP growth, remittances, international reserves, and world growth. Kenya's CI is based on the October 2020 WEO and the World Bank's CPIA vintage released in July 2020. The debt carrying capacity, in turn, determines the PPG external debt thresholds and total public debt benchmarks.¹⁰

Kenya: Composite Indicator and Thresholds			
Country	Kenya		
Country Code	664		
Debt Carrying Capacity	Medium		
Final	Classification based on current vintage	Classification based on the previous vintage	Classification based on the two previous vintages
Medium	Medium 3.01	Strong 3.12	Strong 3.13
APPLICABLE		APPLICABLE	
EXTERNAL debt burden thresholds		TOTAL public debt benchmark	
PV of debt in % of Exports	180	PV of total public debt in percent of GDP	
GDP	40	55	
Debt service in % of Exports	15		
Revenue	18		

11. The revision to Kenya's debt carrying capacity assessment from Strong to Medium was primarily driven by the revision to global growth that occurred with the October 2020 WEO (see Text Table, page 8). The 10-year global growth average was downgraded from 3.5 percent in the previous assessment to 2.9 percent under the current assessment¹¹. With global growth having the largest weight, the revision explains close to 70 percent of the change in the composite indicator score. The downward revision to Kenya's 10-year average growth (from 5.7 percent to 5.1 percent), contributed about 14 percent of the fall in the composite indicator score. Lower reserves coverage contributed to a lower score, while higher remittances growth supported a higher score. Consistent with the shift to Medium debt carrying capacity, applicable thresholds under the LIC DSF also are reduced, as indicated above.

⁹ [The World Bank's Country Policy and Institutional Assessment \(CPIA\)](#).

¹⁰ See Guidance Note on the Bank-Fund Debt Sustainability Framework for Low Income Countries, Section V.

¹¹ Global growth projections have been revised up since October 2020 WEO, although the outlook remains uncertain.

Kenya: Sources of Change in the Assessment of Debt Carrying Capacity					
Component	Coefficients (A)	Current Assessment		Previous Assessment	
		10-year average values (B)	CI Score components (A*B) = (C)	10-year average values (B)	CI Score components (A*B) = (C)
Country Policy and Institutional Assessment (CPIA)	0.4	3.7	1.44	3.7	1.44
Real GDP growth, percent	2.7	5.1	0.14	5.7	0.16
Import coverage of reserves, percent	4.1	39.4	1.60	42.3	1.72
Import coverage of reserves ² , percent	-4.0	15.5	-0.62	17.9	-0.71
Remittances, in percent of GDP	2.0	3.0	0.06	2.8	0.06
Global growth, in percent	13.5	2.9	0.40	3.5	0.47
Composite Indicator (CI) Score			3.01		3.12
Composite Indicator (CI) Rating			Medium		Strong

12. Besides the six standardized stress tests, there are two tailored stress tests:

- One tailored stress test combines contingent liabilities of a one-time debt shock (equivalent to 8.1 percent of GDP) to capture a scenario reflecting both contingent liabilities from SOEs (equal to the indicated standard level of 2 percent of GDP), contingent liabilities from PPPs (equal to the indicated level of 35% of the existing PPP stock, or 1.1 percent of GDP) and a need for bank recapitalization (equal to the indicated standard level of 5 percent of GDP).
- The second tailored stress test is a market financing shock which is applied to low income countries with market access, such as Kenya. The scenario assesses rollover risks resulting from a deterioration in global risk sentiment, temporary nominal depreciation, and shortening of maturities of new external commercial borrowing.

EXTERNAL DEBT SUSTAINABILITY ANALYSIS

13. Debt indicators in terms of exports breach thresholds under the baseline driven by the slowdown in exports and higher external debt (Table 1, Table 3, and Figure 1). Higher debt, the debt amortization profile, and lower exports of goods and services caused by the COVID-19 shock help explain the breaches of one solvency (PV of PPG external debt-to-export ratio) and liquidity (debt-service-to-exports ratio) indicator. Based on the debt-carrying capacity analysis (2020 October-vintage WEO), the solvency indicator remains above threshold (180 percent) during 2021–27, while the liquidity indicator exceeds its threshold (15 percent) throughout the 10-year projection. The solvency indicator gradually declines as exports recover; the long-term decline in the liquidity indicator is interrupted by Eurobond repayments in 2024 and 2028. When compared with the May 2020 DSA, the reassessed classification of Kenya’s debt carrying capacity contributed to more protracted breaches.

14. The PV of PPG external debt as a share of GDP remains firmly below the 40 percent indicative threshold throughout the projection period (Table 1 and Figure 1). Reflecting fiscal consolidation efforts and a borrowing mix that favors concessional borrowing, this solvency indicator is expected to decline from 28.7 percent in 2021 to almost 17 percent in 2041. It also remains below the threshold under the most extreme shock—a one-time depreciation. The external

debt service-to-revenue ratio exceeds its threshold (18 percent) in 2024, reflecting the maturity of the Eurobond in that year. If market conditions are favorable, the authorities are considering debt management operations to further improve the already smooth debt service profile. Support provided by the G20 under the Debt Service Suspension Initiative (DSSI), requested by Kenya in January 2021, helped reduce debt service by about US\$640 million in 2021.

15. Standard stress test results highlight the sensitivity of debt indicators to exports (Figure 1 and Table 1). Specifically, under the most extreme shock scenario (shock to export growth), the PV of debt-to-exports and the debt service-to-exports ratios breach the threshold over the projection period. Under the most extreme scenario, the debt service-to-revenue ratio is above the threshold until 2025.

16. Market financing risks have receded for Kenya (Figure 5). The EMBI spread has fallen from 727 basis points in 2020Q1 to 498 basis points during the 3 months ending in January 2021 and remains below the threshold (570 basis points). Gross financing needs have also declined, from 15 percent of GDP at the time of the previous DSA to 13 percent of GDP currently, staying below the threshold (14 percent of GDP) that indicates high risks. As noted above, relief provided by the G20 under the DSSI reduced financing needs in 2021. Fiscal consolidation efforts under the proposed program would help reduce gross financing needs below the threshold except in 2024, when rollover of the Eurobond upon maturity will increase financing needs to 14.3 percent of GDP. As is the case for emerging and frontier economies, financing risks could be affected by global liquidity conditions. If global market conditions were to unexpectedly tighten, financing risks for Kenya may increase. The shift in the deficit financing mix towards domestic resources calls for monitoring risks, although the recent success in extending the maturity profile of domestic debt mitigates some domestic refinancing risk.

PUBLIC DEBT SUSTAINABILITY ANALYSIS

17. While average indebtedness in PV terms remains unchanged when compared with the last DSA, under the current baseline the public debt-to-GDP ratio remains above the 55 percent benchmark—for a country rated at medium debt-carrying capacity—until 2027 (Figure 2 and Table 2).¹² In PV terms, the average PV debt-to-GDP ratio amounts to 62.8 percent during 2020–25, 0.3 percentage point of GDP above the average figure discussed at the time of the DSA for the RCF (May 2020). Public sector debt is projected to increase from 62.4 percent of GDP (PV terms) in 2020 to 64.2 percent in 2022, followed by a gradual decline. It remains above the threshold until 2027. Supported by fiscal consolidation under the program, including revenue mobilization measures, the PV of public debt-to-revenue ratio would initially increase from 360 percent in 2020 to 373 percent in 2021, before gradually declining to 248 percent in 2030 and to 105 percent in 2040.

¹² Under *Strong* debt carrying capacity the threshold on PV of public debt is 70 percent of GDP.

18. The alternative scenarios indicate that the PV of debt-to-GDP ratio would remain above the indicative benchmark for most of the projection period (Figure 2 and Table 4).

Under the most extreme shock scenario (shock to GDP growth), the PV of the public debt-to-GDP ratio would breach the 55 percent benchmark for a country with medium debt-carrying capacity during 2021–35.

RISK RATING AND VULNERABILITIES

19. Kenya’s risk of debt distress remains high in the context of the ongoing global COVID-19 shock.

The shock has led to a sharp temporary decline in export and GDP growth and triggered a strong fiscal response, interrupting planned consolidation. Consequently, the mechanical signal from debt indicators has worsened, particularly those expressed in terms of exports. Potential risks associated with SOEs will be closely monitored under the Fund-supported program, inter alia through financial evaluations of the nine largest SOEs facing financial risks (*prior action*), with the number of SOEs assessed increasing to 15–20 before the end of FY20/21. This analysis will inform the development of a strategy to manage and reduce SOE-related risks (*structural benchmark*). Kenya’s external and public debt vulnerabilities also reflect high past deficits, partly due to large infrastructure projects. Given the assessment of debt-carrying capacity as medium, the mechanical signal indicates sustained breaches of solvency and liquidity indicators under the baseline scenario—the PV of external debt-to-exports and external debt service-to-exports ratios as well as PV of public debt-to-GDP. The larger breach of liquidity indicators in 2024 under the baseline is mainly attributed to a Eurobond repayment; staff projects Kenya should be able to roll this maturity over, given its historical record of strong global market access and commitment to fiscal consolidation under the proposed program. The DSA suggests that Kenya is susceptible to export and exchange rate depreciation shocks (Figure 1).

20. Kenya’s debt remains sustainable and supported by fiscal consolidation under the program.

With the debt-stabilizing primary balance achieved and surpassed during the program, debt would begin declining as a share of GDP already during the last year of the EFF/ECF arrangements. Indicators measured against exports will also gradually improve with the recovery of exports toward levels Kenya has achieved in recent years, supported by the post-pandemic global recovery and reforms under the EFF/ECF program to enhance competitiveness. Given the duration of mechanical threshold breaches under the baseline, consolidation efforts would need to be sustained after the program concludes to bring debt down to a healthier level.

- While the PV of public debt-to-GDP ratio remains above the indicative threshold (50 percent), the authorities’ commitment to fiscal consolidation under the program provides additional safeguards for debt sustainability. Important actions have already been taken to permanently broaden the tax revenue base in the midst of the pandemic, alongside expenditure savings to limit expansion of the deficit from the COVID-19 shock. The multiyear fiscal consolidation plan highlighted in the 2021 Budget Policy Statement (BPS) is premised on a more conservative approach to revenue projections and a commitment to additional policy steps to increase tax revenues and control expenditures under the EFF/ECF program with the specific objective of anchoring debt sustainability.

- Kenya's PV of external debt as a share of GDP is below the 40 percent indicative threshold and will gradually decline over time. The slowdown in exports on the back of the COVID-19 shock and the scheduled rollover of the 2024 Eurobond drive the breaches in PV of external debt to exports and external debt service to exports. Kenya's external debt indicators are expected to gradually improve as fiscal consolidation progresses, exports recover after the global shock dissipates, and Kenya makes progress to unlock its substantial export potential.
- In addition, in connection with Kenya's good prospects for capital market access at favorable terms, debt management operations (not reflected under the baseline) that seek to refinance syndicated loans and the 2024 Eurobond with long-dated debt instruments could offer a meaningful possibility to further improve the external debt profile.

21. Debt sustainability is also supported by Kenya's generally smooth debt service profile, the authorities' commitment to protect the public sector balance sheet from SOE-related contingent liabilities, and reasonable prospects for restoring Kenya's strong debt carrying capacity. While the protracted breaches of most debt burden indicators are a source of concern, including SOE-related contingent liabilities, there are mitigating factors that help support the debt sustainability assessment. The relatively smooth debt service profile—except for the 2024 Eurobond maturity—is on a clear declining trajectory over the projection period during which breaches are most pronounced, signaling a strengthening in debt servicing capacity. The authorities' commitment to absorb potential fiscal costs associated with materialization of SOE-related contingent liabilities with a limited impact on the programmed fiscal envelope will help avoid further deterioration in the public sector balance sheet. With global growth rebounding during the projection period, Kenya's track record of strong debt carrying capacity, and the authorities' commitment to pursue strong policies to replenish external buffers, there are reasonable prospects of restoring a strong debt-carrying capacity over the medium term, which will help reduce the number of indicators breaching the thresholds and the breaches' duration. Stable and strong remittances would also continue to be an important source for foreign currency receipts, helping offset the slowdown in tourism receipts.

22. The debt profile also calls for a strong debt management framework and its effective implementation. The authorities' active plans for managing their portfolio risks, including through refinancing maturities coming due on better terms to improve the overall debt profile, are a source of resiliency. In this context, the authorities are encouraged to further strengthen their debt management capacity to manage and prepare for large repayments of commercial borrowing. As part of this strategy, the authorities' plans to refinance loans at a longer maturity to limit refinancing risks is welcome. At the same time, concessional borrowing should continue to play an important role in financing investment projects due to its lower cost and longer maturity profile, while non-concessional borrowing should be limited to finance those projects that are critical for the authorities' development strategy and have high social and economic returns. Looking ahead, efficient investment in infrastructure will raise growth and export potential, both of which will support Kenya's external debt sustainability. Delivering on fiscal consolidation, while seeking to preserve social and development spending, would further reduce risks. At the same time, the authorities are encouraged to expand the coverage of public debt to include county governments,

extra budgetary units, and non-guaranteed SOE debt, and continue improving public debt management and revenue administration.

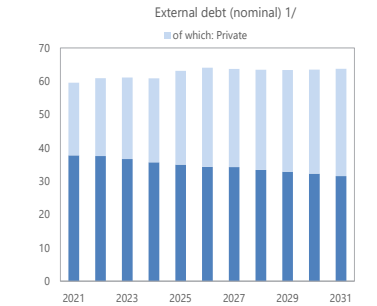
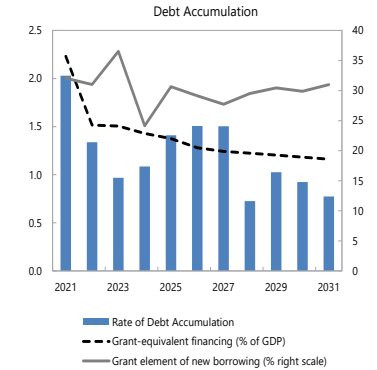
AUTHORITIES' VIEWS

23. While underscoring the high degree of uncertainty on the outlook, the authorities acknowledged that debt and debt service indicators have deteriorated, reflecting the adverse impact of the global COVID-19 shock that contributed to larger primary deficits and lower growth. They noted that higher public debt was driven by the increased utilization of external commercial financing of the past, although during 2020 Kenya avoided utilizing commercial borrowing and relied heavily on the domestic debt markets. The authorities emphasized their commitment to fiscal consolidation under the program, including continued efforts to improve tax revenues, strengthen exports to help improve liquidity and solvency debt indicators, and continue to rely on concessional financing. The authorities acknowledged that Kenya remains at high risk of debt distress—overall and external debt. They committed to limit the use of commercial borrowing to the amounts allowed under the IMF supported program and observe the IMF Debt Limits Policy. The authorities noted that they are actively seeking debt management operations to lower the costs of debt and refinancing risks, especially by seeking to refinance syndicated loans and the 2024 Eurobond with long-dated debt instruments. The authorities committed to implement reforms to deepen the domestic debt markets to enhance efficiency in the secondary market and lower the cost of government debt securities across the yield curve. The authorities also committed to increase debt transparency through expanded coverage and reporting of public debt.

Table 1. Kenya: External Debt Sustainability Framework, Baseline Scenario, 2018–41
(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 8/	
	2018	2019	2020	2021	2022	2023	2024	2025	2026	2031	2041	Historical	Projections
External debt (nominal) 1/	51.5	54.3	58.7	59.6	60.9	61.1	60.9	63.1	64.1	63.8	41.3	35.1	62.5
<i>of which: public and publicly guaranteed (PPG)</i>	30.6	31.5	35.6	37.8	37.6	36.7	35.7	35.0	34.3	31.5	24.1	19.0	34.7
Change in external debt	3.6	2.8	4.4	0.9	1.3	0.2	-0.3	2.3	0.9	0.3	-3.5		
Identified net debt-creating flows	-0.7	0.6	2.5	0.8	1.8	1.5	1.5	1.5	1.4	1.3	2.0	3.5	1.3
Non-interest current account deficit	4.1	3.8	2.8	3.5	3.6	3.6	3.8	3.7	3.7	3.6	4.0	5.8	3.7
Deficit in balance of goods and services	9.8	9.3	8.2	9.1	9.4	9.7	9.9	10.0	10.1	10.2	8.8	11.5	9.9
Exports	13.2	12.1	10.0	11.2	11.8	12.4	12.9	13.3	13.4	15.0	21.1		
Imports	23.0	21.4	18.2	20.4	21.3	22.1	22.8	23.3	23.5	25.2	29.8		
Net current transfers (negative = inflow)	-5.7	-5.5	-5.0	-5.7	-5.9	-6.0	-6.1	-6.1	-6.0	-6.8	-8.1	-5.5	-6.2
<i>of which: official</i>	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other current account flows (negative = net inflow)	0.0	0.0	-0.4	0.1	0.0	0.0	0.0	-0.2	-0.4	0.2	3.4	-0.2	-0.1
Net FDI (negative = inflow)	-1.7	-1.2	-0.2	-0.3	-0.4	-0.5	-0.6	-0.7	-0.7	-0.7	-0.6	-1.4	-0.6
Endogenous debt dynamics 2/	-3.1	-2.1	-0.1	-2.4	-1.4	-1.6	-1.7	-1.6	-1.6	-1.7	-1.5		
Contribution from nominal interest rate	1.7	2.0	2.0	1.8	1.8	1.9	1.8	1.9	1.9	1.9	1.1		
Contribution from real GDP growth	-2.7	-2.5	0.1	-4.2	-3.2	-3.5	-3.4	-3.4	-3.5	-3.6	-2.5		
Contribution from price and exchange rate changes	-2.1	-1.5	-2.1	...	...	...	...	...	...	...	...
Residual 3/	4.4	2.3	1.9	0.1	-0.4	-1.3	-1.8	0.8	-0.4	-1.0	-5.4	1.5	-0.9
<i>of which: exceptional financing</i>	0.0	0.0	0.0	-1.5	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Sustainability indicators													
PV of PPG external debt-to-GDP ratio	...	...	28.7	28.7	28.3	27.3	26.3	25.7	25.2	22.7	16.8		
PV of PPG external debt-to-exports ratio	...	...	288.3	255.8	239.2	219.8	204.2	193.6	188.5	151.5	79.8		
PPG debt service-to-exports ratio	19.6	31.9	26.5	19.1	22.7	20.1	29.7	18.4	17.1	16.1	7.9		
PPG debt service-to-revenue ratio	14.4	22.0	15.5	13.0	15.8	14.0	21.0	13.1	12.1	12.7	8.3		
Gross external financing need (Million of U.S. dollars)	17,743	21,052	23,612	27,875	30,583	36,489	44,486	49,323	55,874	74,955	88,395		
Key macroeconomic assumptions													
Real GDP growth (in percent)	6.3	5.4	-0.1	7.6	5.7	6.1	6.1	6.1	6.1	6.0	6.0	5.0	6.2
GDP deflator in US dollar terms (change in percent)	4.5	3.1	4.1	-0.5	0.6	1.1	1.5	1.7	1.8	0.1	0.1	4.4	0.7
Effective interest rate (percent) 4/	3.9	4.2	3.8	3.3	3.3	3.3	3.1	3.3	3.3	3.2	2.6	7.6	3.2
Growth of exports of G&S (US dollar terms, in percent)	10.7	-0.6	-14.1	20.7	12.0	12.5	11.9	11.1	8.7	8.4	8.4	1.3	10.9
Growth of imports of G&S (US dollar terms, in percent)	5.7	1.2	-11.8	19.9	11.1	11.3	11.1	10.2	9.0	7.7	5.3	3.5	10.1
Grant element of new public sector borrowing (in percent)	...	...	...	32.0	31.0	36.5	24.1	30.7	29.1	31.0	32.5	...	30.2
Government revenues (excluding grants, in percent of GDP)	18.0	17.5	17.0	16.5	17.0	17.9	18.2	18.6	18.9	19.0	20.3	18.4	18.4
Aid flows (in Million of US dollars) 5/	1,087	1,476	1,923	3,055	2,335	2,457	2,707	2,911	2,905	3,550	5,312		
Grant-equivalent financing (in percent of GDP) 6/	...	...	...	2.2	1.5	1.5	1.4	1.4	1.3	1.2	1.0	...	1.4
Grant-equivalent financing (in percent of external financing) 6/	...	...	...	36.5	37.0	42.4	28.7	35.9	34.7	37.4	40.9	...	35.8
Nominal GDP (Million of US dollars)	87,824	95,371	99,110	106,041	112,750	120,936	130,160	140,398	151,536	205,789	373,341		
Nominal dollar GDP growth	11.2	8.6	3.9	7.0	6.3	7.3	7.6	7.9	7.9	6.1	6.1	9.6	6.9
Memorandum items:													
PV of external debt 7/	...	...	51.8	50.5	51.6	51.7	51.6	53.9	55.0	54.9	34.1		
In percent of exports	...	...	519.9	450.1	436.7	417.2	399.6	405.4	410.8	366.8	161.6		
Total external debt service-to-exports ratio	135.1	161.1	213.7	205.7	202.8	218.0	240.0	241.6	253.0	224.0	96.0		
PV of PPG external debt (in Million of US dollars)	...	...	28,453	30,465	31,884	32,975	34,288	36,124	38,238	46,646	62,869		
(PVt-PVt-1)/GDPt-1 (in percent)	...	...	2.0	1.3	1.0	1.1	1.4	1.5	1.5	0.8	0.6		
Non-interest current account deficit that stabilizes debt ratio	0.4	1.0	-1.6	2.6	2.2	3.4	4.1	1.5	2.8	3.4	7.5		

Definition of external/domestic debt	Currency-based
Is there a material difference between the two criteria?	No



Sources: Country authorities; and staff estimates and projections.

1/ Includes both public and private sector external debt.

2/ Derived as $[r - g - p(1+g)] / (1+g+p+g)$ times previous period debt ratio, with r = nominal interest rate; g = real GDP growth rate, and p = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Current-year interest payments divided by previous period debt stock.

5/ Defined as grants, concessional loans, and debt relief.

6/ Grant-equivalent financing includes grants provided directly to the government and through new borrowing (difference between the face value and the PV of new debt).

7/ Assumes that PV of private sector debt is equivalent to its face value.

8/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Table 2. Kenya: Public Sector Debt Sustainability Framework, Baseline Scenario, 2018–41
(In percent of GDP, unless otherwise indicated)

	Actual			Projections								Average 6/	
	2018	2019	2020	2021	2022	2023	2024	2025	2026	2031	2041	Historical	Projections
Public sector debt 1/	60.2	62.1	68.7	71.5	72.9	72.3	71.8	70.0	68.2	53.7	29.4	45.9	65.8
of which: external debt	30.6	31.5	35.6	37.8	37.6	36.7	35.7	35.0	34.3	31.5	24.1	19.0	34.7
Change in public sector debt	3.4	1.9	6.5	2.8	1.5	-0.7	-0.5	-1.8	-1.8	-2.7	-1.8		
Identified debt-creating flows	3.2	2.6	5.9	1.8	0.7	-1.5	-2.5	-3.1	-3.5	-2.7	-1.6	3.3	-2.0
Primary deficit	3.7	3.6	4.1	3.7	2.0	0.4	-0.3	-0.9	-1.3	-0.9	-0.4	3.7	-0.1
Revenue and grants	18.2	17.7	17.3	16.9	17.3	18.2	18.5	18.9	19.2	19.3	20.6	18.8	18.7
of which: grants	0.3	0.2	0.3	0.4	0.4	0.3	0.3	0.3	0.3	0.3	0.3		
Primary (noninterest) expenditure	21.9	21.3	21.4	20.6	19.3	18.6	18.2	18.0	17.9	18.4	20.2	22.5	18.5
Automatic debt dynamics	-0.5	-1.0	1.8	-1.9	-1.3	-1.9	-2.1	-2.3	-2.3	-1.7	-1.2		
Contribution from interest rate/growth differential	0.0	-0.1	1.4	-2.6	-1.9	-2.2	-2.2	-2.3	-2.3	-2.3	-1.7		
of which: contribution from average real interest rate	3.4	2.9	1.4	2.2	2.0	2.1	1.9	1.8	1.7	0.9	0.1		
of which: contribution from real GDP growth	-3.4	-3.1	0.1	-4.8	-3.9	-4.2	-4.1	-4.1	-4.0	-3.2	-1.8		
Contribution from real exchange rate depreciation	-0.5	-0.8	0.3	...	...	...	...	...	...	...	...
Other identified debt-creating flows	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Privatization receipts (negative)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Recognition of contingent liabilities (e.g., bank recapitalization)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Debt relief (HIPC and other)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Other debt creating or reducing flow (please specify)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Residual	0.2	-0.7	0.7	1.7	1.3	1.1	2.1	1.4	1.8	0.5	0.2	1.0	1.1
Sustainability indicators													
PV of public debt-to-GDP ratio 2/	...	...	62.4	63.0	64.2	63.4	62.9	61.1	59.5	45.4	22.6		
PV of public debt-to-revenue and grants ratio	...	...	360.0	372.6	370.8	348.7	339.2	324.0	309.3	234.8	110.0		
Debt service-to-revenue and grants ratio 3/	46.2	56.1	52.2	47.6	61.9	68.3	79.3	72.0	69.8	46.6	16.5		
Gross financing need 4/	12.1	13.5	13.2	11.8	12.7	12.9	14.4	12.7	12.1	8.1	3.0		
Key macroeconomic and fiscal assumptions													
Real GDP growth (in percent)	6.3	5.4	-0.1	7.6	5.7	6.1	6.1	6.1	6.1	6.0	6.0	5.0	6.2
Average nominal interest rate on external debt (in percent)	3.4	3.9	3.6	3.0	2.7	2.7	2.4	2.5	2.4	2.4	1.9	4.3	2.5
Average real interest rate on domestic debt (in percent)	8.5	6.9	2.6	5.8	5.6	5.4	5.2	4.8	4.7	3.4	1.8	2.5	4.6
Real exchange rate depreciation (in percent, + indicates depreciation)	-2.6	-3.2	1.1	...	...	...	...	...	...	...	...	-2.5	...
Inflation rate (GDP deflator, in percent)	2.4	4.0	8.2	3.9	4.6	5.0	5.1	5.1	5.1	5.1	5.1	7.5	5.0
Growth of real primary spending (deflated by GDP deflator, in percent)	2.5	2.4	0.7	3.5	-0.9	2.2	3.6	4.9	5.7	6.4	8.2	4.8	4.7
Primary deficit that stabilizes the debt-to-GDP ratio 5/	0.3	1.7	-2.5	0.9	0.6	1.1	0.2	0.9	0.5	1.8	1.5	-0.1	1.2
PV of contingent liabilities (not included in public sector debt)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		

Sources: Country authorities; and staff estimates and projections.

1/ Coverage of debt: The central government plus social security, central bank, government-guaranteed debt. Definition of external debt is Currency-based.

2/ The underlying PV of external debt-to-GDP ratio under the public DSA differs from the external DSA with the size of differences depending on exchange rates projections.

3/ Debt service is defined as the sum of interest and amortization of medium and long-term, and short-term debt.

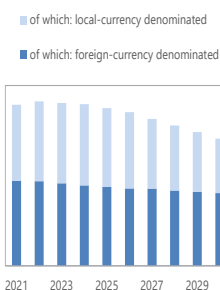
4/ Gross financing need is defined as the primary deficit plus debt service plus the stock of short-term debt at the end of the last period and other debt creating/reducing flows.

5/ Defined as a primary deficit minus a change in the public debt-to-GDP ratio (-: a primary surplus), which would stabilize the debt ratio only in the year in question.

6/ Historical averages are generally derived over the past 10 years, subject to data availability, whereas projections averages are over the first year of projection and the next 10 years.

Definition of external/domestic debt	Currency-based
Is there a material difference between the two criteria?	No

Public sector debt 1/



■ of which: held by residents
■ of which: held by non-residents

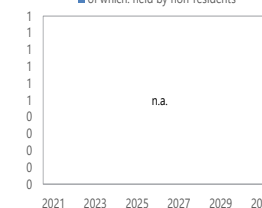


Table 3. Kenya: Sensitivity Analysis for Key Indicators of Public and Publicly Guaranteed External Debt, 2021–31
(In percent)

	Projections 1/										
	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
PV of debt-to GDP ratio											
Baseline	29	28	27	26	26	25	25	24	24	23	23
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2021–2031 2/	29	28	28	28	28	28	28	28	28	28	28
B. Bound Tests											
B1. Real GDP growth	29	29	30	29	28	28	27	26	26	25	25
B2. Primary balance	29	29	30	30	29	28	28	28	27	27	26
B3. Exports	29	30	32	31	30	30	29	29	28	27	26
B4. Other flows 3/	29	30	30	29	28	28	27	26	26	25	24
B5. Depreciation	29	36	30	29	29	28	28	27	27	26	26
B6. Combination of B1–B5	29	32	32	31	30	30	29	28	28	27	26
C. Tailored Tests											
C1. Combined contingent liabilities	29	30	30	29	28	28	28	28	27	27	26
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	29	32	30	30	29	28	28	27	26	26	25
Threshold	40	40	40	40	40	40	40	40	40	40	40
PV of debt-to-exports ratio											
Baseline	256	239	220	204	194	188	183	173	166	159	151
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2021–2031 2/	256	241	225	214	209	210	208	200	195	190	184
B. Bound Tests											
B1. Real GDP growth	256	239	220	204	194	188	183	173	166	159	151
B2. Primary balance	256	245	244	229	217	212	207	198	191	183	174
B3. Exports	256	306	379	352	333	324	313	296	282	268	253
B4. Other flows 3/	256	250	241	224	212	207	200	189	181	172	163
B5. Depreciation	256	239	194	181	171	167	162	154	148	143	137
B6. Combination of B1–B5	256	299	235	293	278	271	262	248	237	226	215
C. Tailored Tests											
C1. Combined contingent liabilities	256	257	240	224	213	210	205	197	190	183	175
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	256	239	220	205	195	189	183	173	165	157	150
Threshold	180	180	180	180	180	180	180	180	180	180	180
Debt service-to-exports ratio											
Baseline	19	23	20	30	18	17	17	20	17	17	16
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2021–2031 2/	19	22	19	28	18	16	16	19	16	16	16
B. Bound Tests											
B1. Real GDP growth	19	23	20	30	18	17	17	20	17	17	16
B2. Primary balance	19	23	21	31	20	18	18	22	18	19	18
B3. Exports	19	27	30	45	29	27	27	32	28	28	27
B4. Other flows 3/	19	23	20	30	19	18	18	21	18	18	17
B5. Depreciation	19	23	20	29	18	16	16	20	15	15	15
B6. Combination of B1–B5	19	26	28	41	26	24	24	29	24	24	23
C. Tailored Tests											
C1. Combined contingent liabilities	19	23	21	30	19	18	18	21	17	17	17
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	19	23	20	31	21	20	20	21	24	15	15
Threshold	15	15	15	15	15	15	15	15	15	15	15
Debt service-to-revenue ratio											
Baseline	13	16	14	21	13	12	12	15	12	13	13
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2021–2031 2/	13	15	13	20	13	12	12	14	12	12	12
B. Bound Tests											
B1. Real GDP growth	13	16	15	23	14	13	13	16	14	14	14
B2. Primary balance	13	16	14	22	14	13	13	16	14	14	14
B3. Exports	13	16	14	22	14	13	13	16	15	15	15
B4. Other flows 3/	13	16	14	22	14	12	13	16	14	14	14
B5. Depreciation	13	20	18	26	16	15	15	18	14	15	15
B6. Combination of B1–B5	13	17	16	24	15	14	14	17	15	15	15
C. Tailored Tests											
C1. Combined contingent liabilities	13	16	14	21	14	12	13	15	13	13	13
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	13	16	14	22	15	14	14	16	18	12	12
Threshold	18	18	18	18	18	18	18	18	18	18	18

Sources: Country authorities; and staff estimates and projections.

1/ A bold value indicates a breach of the threshold.

2/ Variables include real GDP growth, GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

3/ Includes official and private transfers and FDI.

Table 4. Kenya: Sensitivity Analysis for Key Indicators of Public Debt, 2021–31

(In percent)

	Projections 1/										
	2021	2022	2023	2024	2025	2026	2027	2028	2029	2030	2031
PV of Debt-to-GDP Ratio											
Baseline	63	64	63	63	61	59	57	54	51	48	45
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2021-2031 2/	63	64	66	68	70	71	72	72	72	72	72
B. Bound Tests											
B1. Real GDP growth	63	68	71	72	72	71	70	68	66	64	62
B2. Primary balance	63	67	71	70	68	66	63	60	57	54	51
B3. Exports	63	66	68	67	66	64	61	58	55	51	49
B4. Other flows 3/	63	66	66	66	64	62	59	56	53	50	47
B5. Depreciation	63	68	65	63	60	57	53	49	45	42	38
B6. Combination of B1-B5	63	64	68	68	66	64	61	58	55	52	49
C. Tailored Tests											
C1. Combined contingent liabilities	63	72	71	70	68	66	63	60	57	54	51
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	63	64	63	63	61	60	57	54	51	48	45
Public debt benchmark	55	55	55	55	55	55	55	55	55	55	55
PV of Debt-to-Revenue Ratio											
Baseline	373	371	349	339	324	309	294	279	264	249	235
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2021-2031 2/	373	372	362	367	369	371	374	375	375	375	375
B. Bound Tests											
B1. Real GDP growth	373	389	391	389	379	370	361	351	342	332	323
B2. Primary balance	373	386	390	378	361	345	329	313	296	281	265
B3. Exports	373	380	375	364	348	332	316	300	283	267	251
B4. Other flows 3/	373	378	364	353	337	322	307	291	275	259	244
B5. Depreciation	373	392	359	340	317	295	275	255	236	216	198
B6. Combination of B1-B5	373	372	376	365	349	333	317	301	285	269	254
C. Tailored Tests											
C1. Combined contingent liabilities	373	414	388	377	360	343	327	311	295	279	264
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	373	371	349	340	325	310	294	279	263	248	233
Debt Service-to-Revenue Ratio											
Baseline	48	62	68	79	72	70	59	56	52	49	47
A. Alternative Scenarios											
A1. Key variables at their historical averages in 2021-2031 2/	48	61	67	80	75	75	68	69	68	69	69
B. Bound Tests											
B1. Real GDP growth	48	64	75	89	82	80	70	69	65	64	62
B2. Primary balance	48	62	72	88	76	75	67	64	59	55	52
B3. Exports	48	62	69	80	73	70	60	57	54	51	48
B4. Other flows 3/	48	62	69	80	72	70	60	57	53	50	48
B5. Depreciation	48	60	68	79	71	68	58	56	51	49	46
B6. Combination of B1-B5	48	60	69	85	75	72	63	61	56	52	49
C. Tailored Tests											
C1. Combined contingent liabilities	48	62	79	84	75	77	67	64	56	53	50
C2. Natural disaster	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C3. Commodity price	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
C4. Market Financing	48	62	69	80	74	72	61	57	58	48	46

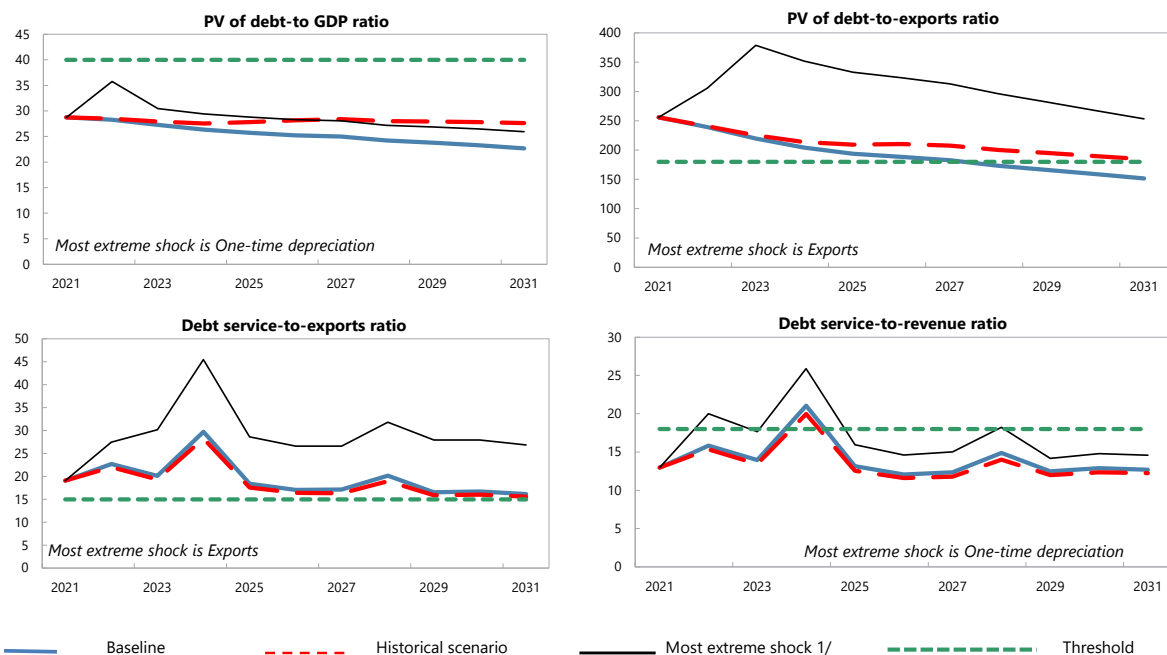
Sources: Country authorities; and staff estimates and projections.

1/ A bold value indicates a breach of the benchmark.

2/ Variables include real GDP growth, GDP deflator and primary deficit in percent of GDP.

3/ Includes official and private transfers and FDI.

Figure 1. Kenya: Indicators of Public and Publicity Guaranteed External Debt under Alternatives Scenarios, 2021–31



Customization of Default Settings			Borrowing Assumptions for Stress Tests*		
	Size	Interactions		Default	User defined
Tailored Tests			Shares of marginal debt		
Combined CLs	No		External PPG MLT debt	100%	
Natural Disasters	n.a.	n.a.	Terms of marginal debt		
Commodity Prices ^{2/}	n.a.	n.a.	Avg. nominal interest rate on new borrowing in USD	2.8%	2.8%
Market Financing	No	No	USD Discount rate	5.0%	5.0%
			Avg. maturity (incl. grace period)	22	22
			Avg. grace period	5	5

Note: "Yes" indicates any change to the size or interactions of the default settings for the stress tests. "n.a." indicates that the stress test does not apply.

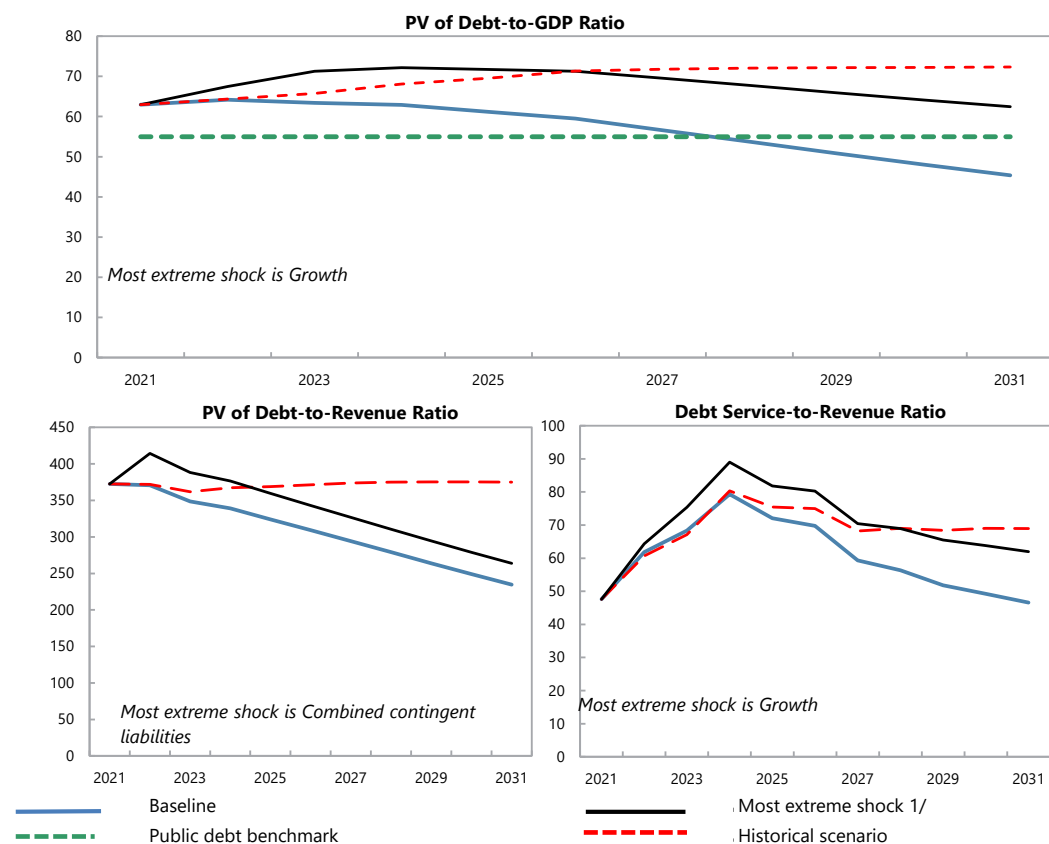
* Note: All the additional financing needs generated by the shocks under the stress tests are assumed to be covered by PPG external MLT debt in the external DSA. Default terms of marginal debt are based on baseline 10-year projections.

Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2031. Stress tests with one-off breaches are also presented (if any), while these one-off breaches are deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most extreme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

2/ The magnitude of shocks used for the commodity price shock stress test are based on the commodity prices outlook prepared by the IMF research department.

Figure 2. Kenya: Indicators of Public Debt Under Alternative Scenarios, 2021–31



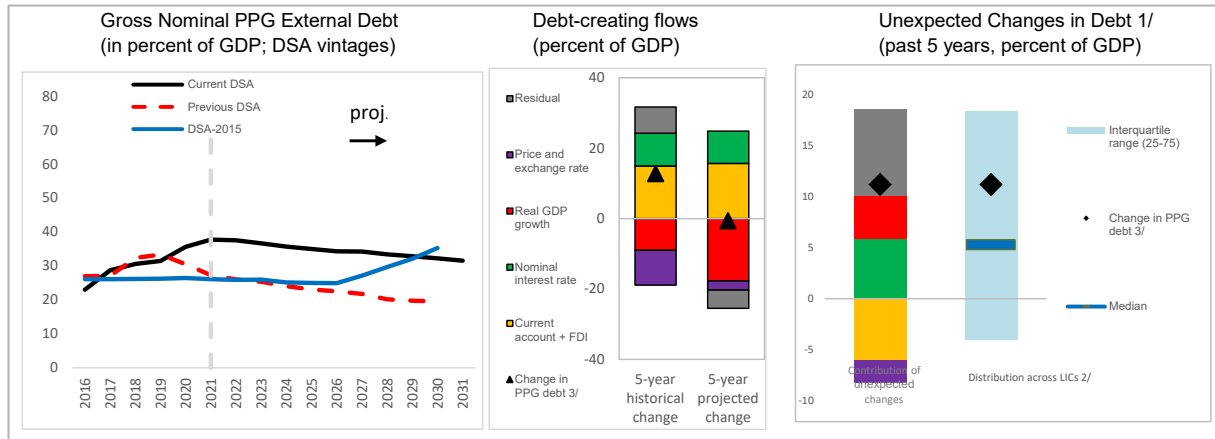
Borrowing Assumptions for Stress Tests*	Default	User defined
Shares of marginal debt		
External PPG medium and long-term	33%	33%
Domestic medium and long-term	45%	45%
Domestic short-term	21%	21%
Terms of marginal debt		
External MLT debt		
Avg. nominal interest rate on new borrowing in USD	2.8%	2.8%
Avg. maturity (incl. grace period)	22	22
Avg. grace period	5	5
Domestic MLT debt		
Avg. real interest rate on new borrowing	4.0%	4.0%
Avg. maturity (incl. grace period)	6	6
Avg. grace period	3	3
Domestic short-term debt		
Avg. real interest rate	1%	1%

* Note: The public DSA allows for domestic financing to cover the additional financing needs generated by the shocks under the stress tests in the public DSA. Default terms of marginal debt are based on baseline 10-year projections.

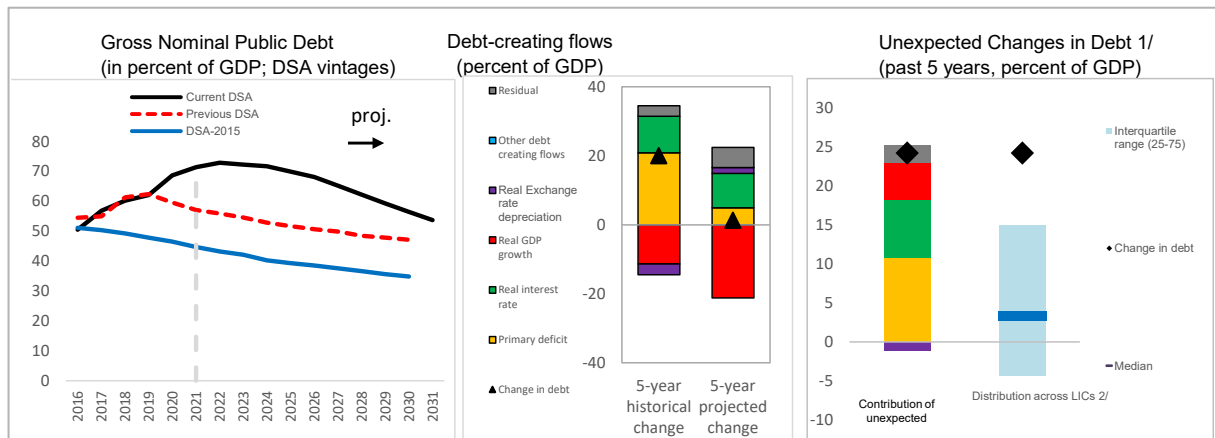
Sources: Country authorities; and staff estimates and projections.

1/ The most extreme stress test is the test that yields the highest ratio in or before 2031. The stress test with a one-off breach is also presented (if any), while the one-off breach is deemed away for mechanical signals. When a stress test with a one-off breach happens to be the most extreme shock even after disregarding the one-off breach, only that stress test (with a one-off breach) would be presented.

Figure 3. Kenya: Drivers of Debt Dynamics–Baseline Scenario External Debt



Public Debt



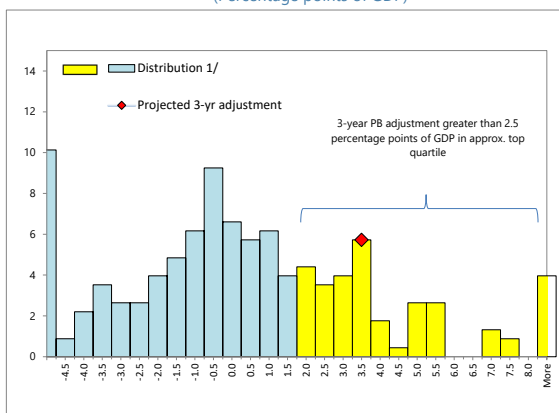
1/ Difference between anticipated and actual contributions on debt ratios.

2/ Distribution across LICs for which LIC DSAs were produced.

3/ Given the relatively low private external debt for average low-income countries, a ppt change in PPG external debt should be largely explained by the drivers of the external debt dynamics equation.

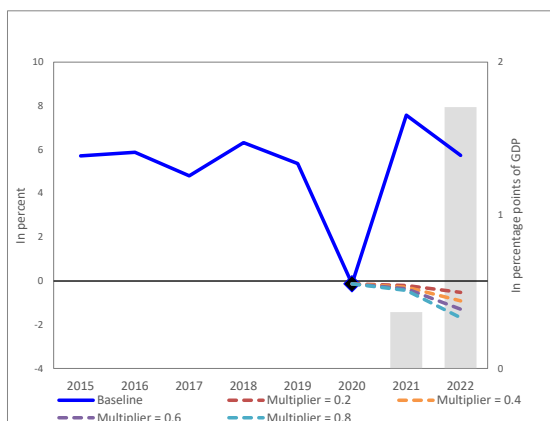
Figure 4. Kenya: Realism Tools

3-Year Adjustment in Primary Balance
(Percentage points of GDP)



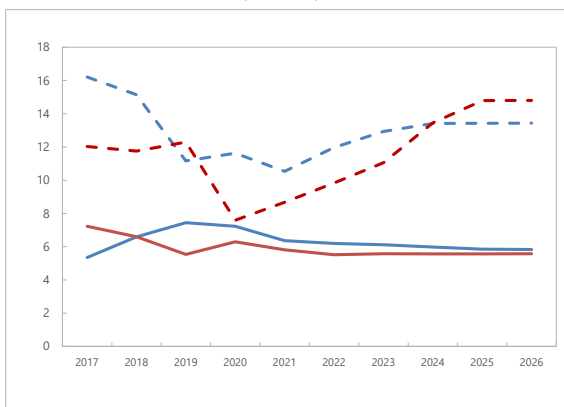
1/ Data cover Fund-supported programs for LICs (excluding emergency financing) approved since 1990. The size of 3-year adjustment from program inception is found on the horizontal axis; the percent of sample is found on the vertical axis.

Fiscal Adjustment and Possible Growth Paths 1/



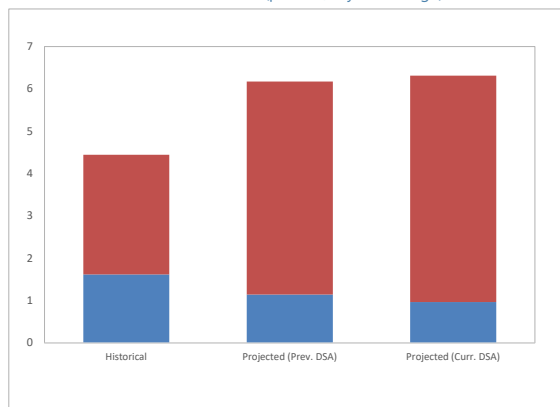
1/ Bars refer to annual projected fiscal adjustment (right-hand side scale) and lines show possible real GDP growth paths under different fiscal multipliers (left-hand side scale).

Public and Private Investment Rates
(% of GDP)



— Gov. Invest. - Prev. DSA — Gov. Invest. - Current DSA
 - - - Priv. Invest. - Prev. DSA - - - Priv. Invest. - Current DSA

Contribution to Real GDP growth
(percent, 5-year average)

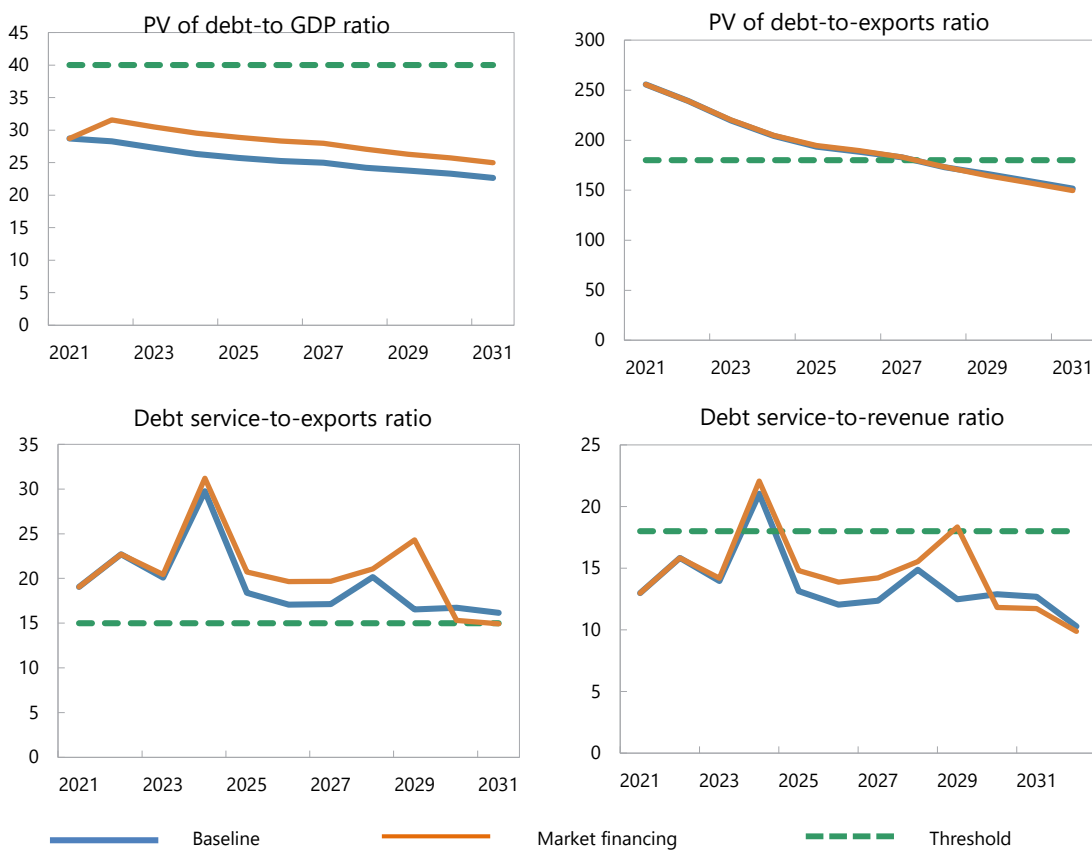


■ Contribution of other factors
 ■ Contribution of government capital

Figure 5. Kenya: Market-Financing Risk Indicators

	GFN	1/	EMBI	2/
Benchmarks	14		570	
Values	13		498	
Breach of benchmark	No		No	
Potential heightened liquidity needs	Low			

1/ Percent of GDP. Maximum gross financing needs (GFN) over 3-year baseline projection horizon.
 2/ Basis points. EMBI average spreads for Nov 2020 - Jan 2021.



Sources: Country authorities; and staff estimates and projections.

**Statement by the Executive Director, Ms. Ita Mary Mannathoko,
and by the Senior Advisor of the Executive Director, Mr. Ted Sitimawina
April 2, 2021**

I. Introduction

1. Our Kenya authorities appreciate the constructive engagement with staff during recent program negotiations for arrangements under the Extended Fund Facility (EFF) and the Extended Credit Facility (ECF). They broadly concur with the staff appraisal and policy recommendations.
2. The COVID-19 pandemic has upended steady and robust economic growth in Kenya that averaged almost six percent for a decade. Growth has declined significantly, while macroeconomic vulnerabilities have risen. While emergency measures were put in place quickly, and the emergency financing received under the Rapid Credit Facility (RCF) in May 2020—for which the government is grateful—has supported their response plan, fiscal and balance of payments needs remain. The authorities are determined to stabilize the economy and set a basis for resurgence of growth and shared prosperity through the Post COVID-19 Economic Recovery Strategy. The strategy seeks to enable an effective pandemic response by maintaining support to the health sector and the vulnerable; reduce debt vulnerabilities through revenue-based fiscal consolidation; advance the structural reform and governance agenda; strengthen the monetary policy framework; and support financial stability.
3. To support these objectives, our authorities request 38-month arrangements under the EFF and ECF with blended access at 305 percent of quota to be disbursed as budget support. They expect that together with support from development partners and other financing sources, including the G20 Debt Service Suspension Initiative, the proposed arrangements will fill the fiscal and external financing gaps over the medium term. The authorities have completed the required prior actions and look forward to Executive Directors' support for the arrangements.

II. Recent Economic Developments and Outlook

4. Real GDP growth dropped sharply from 5.4 percent in 2019 to an estimated -0.1 percent in 2020, reflecting severe disruption in economic activity. The typically resilient, critical services sector covering accommodation and food services was the most affected by domestic containment measures. The education sector also contracted, while agriculture benefitted from favorable weather and alongside construction remained strong. Following the partial lifting of containment measures, economic activity is rebounding with trade and transportation picking up. Medium-term prospects remain strong with growth projected at 7.6 percent in 2021, but the COVID-19 shock has given rise to substantial uncertainties around most estimates, particularly for the medium term.
5. Inflation has remained within the target range (5±2.5 percent), as disruptions to supply chains from the pandemic were limited and did not translate into significant price pressures. Over the past year, broadly stable headline inflation was supported by lower food price inflation in the first half of 2020 following the strong performance seen in agriculture, which compensated for higher fuel prices.

6. Kenya's external sector has remained resilient supported by agricultural exports, especially tea and non-flower horticulture. Exports of goods rose by 3.3 percent in 2020 while the value of imports declined by 12.5 percent reflecting lower oil import prices. Remittances rose, notwithstanding the global downturn. The net effect was that the current account deficit narrowed to an estimated 4.8 percent of GDP in 2020 from 5.8 percent in 2019. The flexible exchange rate served as a shock absorber, strengthening external sector resilience.

III. Fiscal Policy and Debt Management

7. During the program period and beyond, the authorities will pursue revenue-based fiscal consolidation to stabilize public debt and bring it onto a downward trajectory. The adjustment goal is to reduce the primary fiscal deficit to below its debt-stabilizing level. They will implement measures to broaden the tax base, as recommended by the IMF and enacted in April and June 2020. In addition, they are strengthening revenue administration and will implement further tax policy measures in the ensuing fiscal years. Our authorities' commitment to fiscal consolidation is reflected in the recent reversal of most emergency tax relief measures and the introduction of measures to improve tax performance in the midst of the pandemic.

8. On the expenditure side, measures will largely focus on rationalizing non-priority spending without compromising allocations to social and growth enhancing development programs. In this regard, the authorities will be guided by an indicative target to ensure that health and other social expenditures, including transfers to vulnerable groups and free primary and secondary education are protected. To ensure prudent management of available public resources, they will further strengthen public financial management (PFM), particularly in budget control and execution processes, and cash management.

9. A related near-term priority that the program will help sustain is to contain the impact of the pandemic, maintaining support for the health sector and those most impacted by the shock. Besides allocations to the health sector, spending will also protect vulnerable groups and stimulate economic activity in key areas. The support packages focus on providing liquidity support to businesses through accelerated payment of VAT refunds and pending bills to suppliers, cash transfers to urban poor, stimulating activity in hard-hit sectors, with an emphasis on creating youth employment, and supporting small and medium-sized businesses through a recently launched credit guarantee scheme. The authorities will also unwind emergency spending on non-priority areas, adding to the January 1, 2021 reversals of tax cuts.

10. On debt, the authorities are pursuing a financing strategy that balances domestic and external financing and utilizes concessional financing where available. They are also taking steps to extend the maturity of domestic debt. In recognition of external debt vulnerabilities, the authorities will confine external non-concessional financing to funding essential projects critical to the development agenda for which concessional financing is not available, and for liability management purposes. External financing in this manner would complement domestic financing and help prevent an unnecessary crowding-out of private sector credit. The authorities maintain their preference for an asymmetric net international reserves (NIR) adjustor also on non-grant budget flows, given the uncertainties around the timing of donor flows and their inherent import content.

IV. Monetary and Financial Sector Policies

11. The CBK remains committed to ensuring price stability in line with its mandate. In this regard, headline inflation will be kept within the target range of 5 ± 2.5 percent consistent with the monetary policy consultation clause (MPCC). Given the current environment, the CBK will maintain an accommodative monetary policy stance to support the economy as it recovers. The authorities note that their swift policy reaction to the COVID-19 shock, including monetary policy easing, emergency liquidity provision and pre-emptive loan restructurings, provided essential support to an economy under stress. The authorities will also maintain the flexible exchange rate policy which has served the economy well and will limit interventions to smoothing excess volatility.

12. The CBK has been working to strengthen its monetary policy framework and will publish a white paper by June 2021, outlining the requisite reforms. Once the COVID-19 shock abates and conditions permit, reforms will focus on refining the macroeconomic modeling and forecasting frameworks, and improving the operations of financial markets, including fully developing a Centralized Security Depository that will improve monetary policy transmission and promote efficiency and transparency in the government domestic debt market. In addition, they will improve communication of monetary policy decisions to make them more effective. The monetary policy framework will be supported by reforms carried out to strengthen CBK's internal capacity and enhance monetary policy transmission, including the repeal in November 2019 of interest rate caps on commercial bank loans under section 33B of the Banking Act. Additionally, to address concerns of illicit financial flows, corruption and counterfeits that targeted large denominations, the old series Ksh1,000 currency notes were demonetized successfully in an exercise that concluded on September 30, 2019.

13. Safeguarding financial stability and expanding access to affordable finance remain key priorities as the financial sector supports the economy through the COVID-19 pandemic. While the banking sector remains stable and resilient, supervisory and regulatory processes continue to focus on ensuring prudent asset classification and provisioning practices. In this context, the CBK advised banks to revisit their capital planning and reassess the resilience of their portfolios and potentially curtail dividend payments. They will continue to improve prudential regulation and supervision, with a view to addressing the increased complexity of the financial sector, including cyber challenges.

V. Structural Reforms

14. To complement ongoing efforts that strengthen PFM, our authorities will implement fiscal structural reforms to address challenges in state-owned enterprises (SOEs) and to advance governance reforms. The ongoing pandemic has aggravated some underlying challenges in some SOEs. To address those characterized by overlapping mandates, low profitability, weak governance and poor value for money, the authorities are taking a systematic approach to evaluate, monitor, and manage the financial challenges facing SOEs. An immediate action has been the evaluation of the financial health and fiscal needs of nine SOEs with the largest fiscal risks to the FY20/21 budget. This will be followed by an in-depth analysis of the financial vulnerabilities of the largest and most exposed firms in the sector and development of a strategy to address fiscal risks from the SOEs, including a framework to guide interventions. Overall, the reforms will aim to strengthen corporate governance and enhance oversight to limit the risk of contingent liabilities.

15. On governance, the reforms comprise four priorities that will seek to enhance the anti-corruption framework. First, the authorities plan to ensure that comprehensive information on public tenders, including beneficial ownership information of the awarded entities, are publicly available on the government procurement information portal. Second, operationalizing the Access to Information Act. Third, review of the current legal framework for asset declarations of senior public officials and conflict of interest rules. The ongoing review is expected to establish a uniform disclosure regime, strengthen sanctions on misreporting, and improving accessibility of the asset declarations. Fourth, the authorities are undertaking a national risk assessment on money laundering and terrorism financing that will help Kenya develop a national AML/CFT strategy as well as an Action Plan to address the deficiencies identified. At the same time, they are supporting the Financial Reporting Centre (FRC) work on encouraging and strengthening the use of financial intelligence to trace proceeds of corruption by sharing relevant financial intelligence with law enforcement agencies.

16. Our authorities also place a high premium on efforts to strengthen the business environment. Building on past reforms, they will continue to remove any impediments to facilitate investment-led inclusive growth, including reducing the number of days to register a business. At the same time, they are taking measures to boost productivity in the agriculture sector and to reduce gender inequality.

VI. Program Modalities

17. Given the huge uncertainty brought about by the pandemic, our authorities appreciate the program's design which focuses on indicative targets and quarterly reviews. However, they note that key variables in the macroeconomic framework that underpin a program are subject to rapid changes, and they emphasize the need for utmost care in interpreting the results. For instance, the WEO global growth projections used in the assessment of the debt carrying capacity have been superseded in the rapidly changing environment and the projection itself remains highly uncertain (DSA, ¶11).

VII. Conclusion

18. Our authorities reiterate their commitment to further strengthening macroeconomic stability and enhancing the resilience of the economy. In this connection, they will pursue a multi-year fiscal consolidation that should bring public debt on a downward trajectory while preserving space for growth friendly public investment, including in The Big Four. They look forward to Executive Directors' support for approval of the EFF and ECF arrangements to complement their efforts to contain the impact of the pandemic and reignite durable and sustainable growth. Our authorities expect that Fund financing will catalyze additional grant and concessional financing from development partners to augment ongoing efforts and support recovery.