Public Debt, Deficits and Supplementary Budgets

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Introduction

Public Debt continues to be a critical aspect of public finance management in Kenya. High levels of borrowing and increasing debt servicing amounts are creating fiscal pressure, especially on social services and funding to counties. The transparency and accountability of how the borrowed monies have been spent is important in answering two critical questions: 1) Where has the money been spent? 2) Was there value for the money borrowed?

The growth of Kenya’s public debt stock and repayment costs has become a central part of public debate as these directly or indirectly impact the budget, delivery of services and the economy. The public debt includes domestic (stock 50% as of September 2022) and external (stock 50% as of September 2022). IBP Kenya’s study on the state of Kenya’s public Debt: the thin line between a rock and a hard place shows that overall public debt has been increasing in recent years. Specifically, at the end of June 2022, Kenya’s total debt stock stood at Kshs 8.6 trillion compared to Kshs. 0.63 trillion two decades ago.

Despite the Supplementary Budgets’ being crucial in the fiscal space as it addresses unforeseen expenditure needs, the changes made during these decisions are sometimes adverse, as there are possible shifts in the initial funded priorities. Additionally, it has become a platform often used to expand the size of the deficit in recent years. This begs the question, what is the intersection between supplementary budgets, deficit, and public debt?
While the Supplementary Budgets are supposed to address unforeseen expenditure needs, for Kenya, it has become a common feature and part of the budget process, and hardly a financial year ends before the government passes at least two Supplementary Budgets. We must remember that there are no opportunities for the public to participate in this budget decision.

Some of the observations in the recent Supplementary Budgets include:

- Introduction of new budget lines.
- Budget cuts to basic services.
- Transparency on information on Supplementary Budgets remains limited.
  Sometimes the financial side of the budget changes significantly, but the same does not happen on the non-financial information, i.e., service targets.
- Limited explanations and justifications for budget adjustments, especially below the MDAs level.
- Increases underspending rather than curing it.

**What is the current debt position?**

Public borrowing has grown unsustainably, driven mainly by expenditure growth that outstrips revenue. Both approved and revised estimates (through supplementary budget) have continued to increase the deficit levels approved in the Budget Policy Statement that sets the total size of the budget. Raising the ceiling to KES. 9 trillion and later to KES. 10 trillion has only increased the unbridled appetite for loans.

- The increasing levels and the changing composition of debt in Kenya have led to more burdensome debt servicing requirements, which increasingly impact Kenya’s ability to deliver services and meet its obligations for intergovernmental transfers to counties. In the last two years, Kenya’s borrowing from the domestic debt has been growing as external debt slowly declined, and in the previous FY 2021/22, the shares approached a 50-50 ratio.
The poor budget credibility in Kenya’s budget has increased the need to borrow. The growing deficit within a financial year is the main problem which could be cited as the driver of surging debt in Kenya. High deficits, which in the past have grown significantly in the revised budgets in relation to the approved budgets. As shown in table 1, the fiscal deficit has always gone upward within the year.

### Table 1: Fiscal Deficit in Approved and Actual Expenditure (Kshs. Billion)

<table>
<thead>
<tr>
<th>Year (Billion)</th>
<th>Deficit in the Proposed Budget in the BPS</th>
<th>Deficit in At the end of the Year</th>
<th>Increase in the deficit within the year</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014/15</td>
<td>-367.0</td>
<td>-732.0</td>
<td>59%</td>
</tr>
<tr>
<td>2015/16</td>
<td>-332.2</td>
<td>-732.6</td>
<td>37%</td>
</tr>
<tr>
<td>2016/17</td>
<td>-555.4</td>
<td>-871.6</td>
<td>57%</td>
</tr>
<tr>
<td>2017/18</td>
<td>-682.4</td>
<td>-670.4</td>
<td>15%</td>
</tr>
<tr>
<td>2018/19</td>
<td>-418.2</td>
<td>-760.6</td>
<td>15%</td>
</tr>
<tr>
<td>2019/20</td>
<td>-629.9</td>
<td>-789.9</td>
<td>25%</td>
</tr>
<tr>
<td>2020/21</td>
<td>-614.1</td>
<td>-965.7</td>
<td>57%</td>
</tr>
<tr>
<td>2021/22</td>
<td>-976.1</td>
<td>-823.4</td>
<td>-16%</td>
</tr>
</tbody>
</table>

* Projections as the budget is still under implementation.

### Figure 2: Fiscal Deficit as % of GDP

- Debt Servicing and ordinary revenue growth- Debt service is the cash required to cover the repayment of interest and principal on a debt for a particular period. The growth in debt repayment has been a concern as the growth rate has been much more significant than the growth in expected revenue. For instance, the total public debt service increased from Kshs. 780.6 billion in 2020/21 to Kshs. 1169 billion in 2021/22.
The increasing proportion of ordinary revenue absorbed by Debt has become a serious threat in limiting resources available for public spending on essential public goods and services like health, education etc. As debt service grows from one year to the next, the allocations to counties have been dropping because the Debt directly eats into the shareable revenue between the two levels of government.

Additionally, revenue plays a significant role in determining when and how budgets will be revised. The current government is aggressively finding ways to boost revenues despite the increased cost of living, and the high debt repayments basically drive all this.

Overreliance on foreign sources of funding. The capital-heavy sectors depend more on loans to fund their budgets, and there has been relatively low budget absorption on development. Generally, during the FY 2015/16 through to FY 2019/20, on average, the Energy, Infrastructure, and ICT sector had about 44 percent of their budget funded through loans across the five years. Additionally, the 2021 Supplementary I budget highlights some downward revisions, especially on capital projects due to rationalized donor funding.
Transparency on debt issues has remained limited, and when information is made public, it is quite late. For the Supplementary budgets, too, there are transparency issues; for example, the CBTS 2022 Modular research on how transparent supplementary budgets are, shows that only five of the 40 counties that assented to the supplementary budgets in FY 2020/21 published the documents. However, just half of the required information was provided. As we deliberate on the transparency of Supplementary budgets, it’s important to reflect on the situation of the national-level supplementary budgets.

What government has done on public debt and supplementary budgets

The country has, on paper, committed towards fiscal consolidation, which means that expenditures would be rationalized, and the deficit reduced. The preparation and approval process has been devoid of public participation, even though critical decisions are usually taken through supplementary budgets. In some instances, priorities set in the approved estimates are shifted, hence the need for citizens to engage in this process.

The new government proposed increasing the revenue collection base to tame expenditures with the proposed 300 billion cut in the current financial year 2022/23. The fiscal reforms should not negatively affect the provision of basic services, which are felt mainly by the vulnerable population.

According to IMF, if the recent debt trend continues, Kenya may face an unsustainable debt burden, which is already in high distress. Notably, IMF is working with the government on fiscal consolidation that has targeted subsidies and revenue-raising measures.
The PFM Act requires that public debt and obligations remain at sustainable levels. Parliament should always be at the forefront to ensure the debt ceilings and further borrowings are well monitored and adhered to. In addition, parliament should open up spaces for public input during the approval of supplementary budgets.

There has been some improvement in debt transparency. The National Treasury has tried to provide information on public debt, and there is a need to do more to facilitate more involvement through public engagement on public debt issues. Additionally, the Parliamentary Budget Office provides the annual reports, debt register, and debt analysis.

What next?

As PFM practitioners, we are faced with a difficult task. The first is to push for greater transparency in the process of borrowing. There is a need for more accessible and timely information on public debt, which includes consistency, accuracy, and timely provision of information on public debt.

Secondly, parliament should be stricter when reviewing and approving budget estimates and supplementary budgets to avoid increasing the deficit. The practitioners should continue putting the government to task for what they promise.

Thirdly, the Supplementary Budgets should be more open and inclusive to the public views. Parliament should continue opening up spaces for public input while approving supplementary budgets.

Parliament and Civil Society Organizations should play oversight to ensure that austerity measures don’t end up cutting services meant to benefit the most vulnerable households, such as prices of basic food commodities, social protection etc.
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