Kenya: Analysis of the 2016 Budget Review and Outlook Paper (BROP)

December 2016

KEY FINDINGS

- Revenue and expenditure performance were both below target in 2015/16. Actual revenue and expenditure growth were also both below the average for recent years. Expenditure grew at a slightly lower rate than revenue in 2015/16, resulting in a lower deficit.

- While the Budget Review and Outlook Paper (BROP) suggests that Kenya is containing the wage bill, the analysis in BROP 2016 does not represent the full costs of government employment. This makes it difficult to know how well the wage bill is being managed.

- The approved 2016/17 budget was not realistic, leading to a fall in the projections for revenue and expenditure in BROP 2016. The decline in development expenditure was anticipated by Treasury, which previously indicated that the government was unlikely to collect almost half the external financing in the proposed budget. Parliament, however, approved this unrealistic budget. BROP projections for revenue for 2017/18 are also unrealistic in light of past growth rates.

- In 2017/18, Treasury is proposing to reduce the share of the budget for energy and infrastructure, while education and public administration and international relations will take an increasing share.

- The BROP 2016 provides inadequate explanations for past performance and weak justifications for new proposals. Although the Budget Policy Statement 2017 was published shortly after the BROP this year due to the compressed budget calendar, it introduces a number of changes from BROP that are not explained. This includes increasing the size of domestic revenue versus domestic borrowing, and changing the share of the budget going to different sectors.

BACKGROUND

The Budget Review and Outlook Paper (BROP) is a backward and forward looking paper. It comprises three key elements:

1. Review of budget performance from the most recent financial year (2015/16).
2. Updated expectations for key economic indicators and implications for budget performance in the current year (2016/17) and upcoming year (2017/18).
3. Proposed sector distribution of the budget for the coming financial year (2017/18).

Each of these three elements should be accompanied by adequate justifications or explanations. We consider the adequacy of explanations here, but we will develop this concept further in a forthcoming publication. Due to the compressed calendar this year, the Budget Policy Statement (BPS) 2017 was released early as this analysis was underway. Where appropriate, we also refer to the BPS 2017 in this analysis.

REVENUE PERFORMANCE

The BROP provides performance details for the three main sources of revenue:

- Ordinary revenue – funds that are mainly generated from taxes and fees.
- Appropriations in Aid (AiA) – funds collected directly by ministries or agencies either from user fees or from international donors.
- Grants – funds from international donors that are channeled through the National Treasury.

The government projected to raise Ksh. 1.37 trillion in total revenue and external grants in 2015/16 (BROP Table 1).[1] The 2016 BROP shows that only Ksh. 1.27 trillion (93 percent of this target) was raised. As Table 1 shows, this is a slight improvement in performance from 2014/15, and above the average performance between 2011/12 and 2014/15. As in previous years, under-collection of revenues was driven by AiA and external grants. AiA performance declined by 7 percentage points, from 76 percent of the target in 2014/15 to 69 percent in 2015/16. The performance of external grants improved in 2015/16 as compared to the previous year, and was above the average for the past four years. However,

[1] See http://treasury.go.ke/component/jdownloads/category/23-budget-review-outlook-paper.html?Itemid=-1

collections remain below 50 percent. Performance in collecting ordinary revenue has consistently been better, though still slightly below target.

TABLE 1. REVENUE PERFORMANCE AS A PERCENTAGE OF TARGET AMOUNTS

	2011/12	**2012/13**	**2013/14**	**2014/15**	***Average (2011/12-2014/15)***	**2015/16**
Total revenue and grants	90%	88%	97%	92%	*92%*	93%
Ordinary revenue	95%	94%	100%	96%	*97%*	98%
Appropriation in aid	72%	74%	93%	76%	*79%*	69%
External grants	36%	28%	50%	42%	*39%*	45%

Sources: IBP Kenya calculations from BROP 2012 (Table 2), BROP 2013 (Table 2), BROP 2014 (Table 1), BROP 2015 (Table 1), and BROP 2016 (Table 1).
Notes: The actual and target revenue figures are obtained from the most recent BROP. For example, the actual revenue for 2014/15 is obtained from the 2016 BROP, while the revenue target for the same year is in the 2015 BROP. This is done to ensure use of the most updated actual collections data available.

How realistic were the revenue targets that were set for 2015/16? The revenue projected for 2015/16 was 10 percent higher than the projected revenue in 2014/15. The average projected growth in the three previous periods was 14 percent, therefore the projected growth in 2015/16 does not appear to have been unreasonable compared to previous years. However, comparing targets from one year to another can be misleading if these targets are systematically too ambitious.

A more realistic way to evaluate the target for 2015/16 is to look at the actual revenue performance over the past few years and compare that to the target. On average, actual revenue grew 14 percent per year between 2011/12 and 2014/15. As shown in Table 2 below, the projected revenue growth in 2015/16 based on the actual revenue collected in 2014/15 was 20 percent, which was above average growth of actual revenue collected and higher than growth in any single year between 2011/12 and 2014/15. This suggests that the growth targets were unrealistic. This is especially so for AiA and external grants, which were projected to grow by 52 percent and 135 percent respectively against 2014/15 actual revenues. Our calculations suggest that 2015/16 was also below average in terms of revenue performance for all sources, exacerbating the problem of unrealistic targets.

TABLE 2. HOW REALISTIC WERE THE 2015/16 TARGETS?

	Changes in actual revenue between 2011/12 and 2012/13	Changes in actual revenue between 2012/13 and 2013/14	Changes in actual revenue between 2013/14 and 2014/15	Average actual revenue growth 2011/12-2014/15	Changes in actual revenue between 2014/15 and 2015/16	Changes in revenue estimates (target) between 2014/15 and 2015/16	Projected revenue estimates (target) in 2015/16 against actual revenue in 2014/15
Total revenue and grants	13%	19%	10%	14%	12%	10%	20%
Ordinary revenue	13%	18%	12%	14%	12%	11%	15%
Appropriation in aid	18%	21%	-7%	11%	5%	16%	52%
External grants	37%	29%	4%	23%	5%	-1%	135%

Sources: BROP 2012 (Table 2), BROP 2013 (Table 2), BROP 2014 (Table 1), BROP 2015 (Table 1). and BROP 2016 (Table 1).
Notes: The revenue figures are obtained from the most recent BROP. For example, for actual revenue for 2014/15 is obtained from the 2016 BROP and compared to the target for the same year as in the 2015 BROP.

BOX 1. JUSTIFICATIONS AND EXPLANATIONS FOR REVENUE PERFORMANCE

The 2016 BROP provides some explanation for the failure to achieve revenue targets, but they do not address the root causes of poor performance or propose any meaningful solutions.

What are the root causes of poor performance in revenue?

There is no explanation of why external grants underperformed, but there is some explanation of AIA under-collection. The BROP indicates that the under-collection of AIA was due to underreporting by government spending units (Page 2, paragraph 9). It is obvious that the explanation for grants is inadequate. What about for AIA? The explanation relates to the problem, but seems to fall short of identifying the root cause. Why are MDAs underreporting? Further, we cannot tell whether there are specific MDAs that have continuously had this problem over the last few years. Thus the explanation is inadequate because it does not explore differences among the ministries. For ordinary revenue, it is unclear why we under-collected some but not all taxes (excise tax and other income tax performed well). The narrative suggests all taxes other than excise performed poorly, but, as we have seen, other income tax also performed above target. Thus the narrative is not consistent with the data. There is also no recognition that targets might be unrealistic.

What solutions have been put forward for persistent problems?

Underreporting of AiA is a persistent problem that has been mentioned in previous BROPs. However, there is no discussion of how this continuing problem has been dealt with or will be dealt with in the BROP. The lack of a proposal for resolving the matter suggests that the government has not fully explained the nature of the problem. There is also no explanation of why AiA performance improved somewhat from last year, since there has been no change to the explanations offered in previous years.

EXPENDITURE PERFORMANCE

The BROP provides performance details for overall expenditure, and a breakdown for expenditure by Ministries, Departments, and Agencies (MDAs), debt repayment, and various funds.

The total actual expenditure for the year was 87.7 percent of the approved budget. Total actual spending (including MDAs, debt, etc.) grew by 8.7 percent between 2014/15 and 2015/16, which is significantly lower than the growth in actual spending between 2013/14 and 2014/15 of nearly 23.6 percent.

The total actual expenditure for MDAs was 80.7 percent of the approved budget estimates of Ksh 1.49 trillion, an improvement by 5 percentage points from MDA absorption in 2014/15. This was mainly due to an improvement of absorption of development allocation by 10 percentage points (see Table 3).

TABLE 3. MINISTRIES, DEPARTMENTS, AND AGENCIES ABSORPTION RATES, 2011/12 TO 2015/16

	2011/12	**2012/13**	**2013/14**	**2014/15**	**2015/16**
MDAs expenditure	% Budget absorption	% Budget absorption	% Budget absorption	% Budget absorption	% Budget absorption
Recurrent expenditure	92%	92%	91%	93%	90%
Development expenditure	78%	71%	77%	59%	69%
Total MDAs expenditure	86%	84%	86%	76%	81%

Source: IBP Kenya Calculations from BROP 2012 (Table 3); BROP 2013 (Table 3)[2]; BROP 2014 (Table 3); BROP 2015 (Table 3) and BROP 2016 (Table 3).

[2] In 2013/14, 2014/15 and 2015/16 we were able to draw these figures from a detailed breakdown of MDA spending only. This was not available in 2011/12 and 2012/13, so we used total development figures, which may include other items not funded through MDAs. For recurrent expenditure we added only wages and salaries and operations and maintenance leaving out domestic interest, foreign interest, and pensions.

Some MDAs, such as the National Intelligence Service, the National Land Commission, the Ministry of Defence, the Public Service Commission, the Ministry of Sports, Culture and Arts, and the National Police Service Commission spent almost all the funds allocated to them (above 99 percent). However, other MDAs struggled to absorb their budget allocations. The Ministry of Environment, Natural Resources, and Regional Development Authorities and the State Department of Transport spent less than half of their budgets (see Table 4).

TABLE 4. BEST AND WORST PERFORMING MINISTRIES, DEPARTMENTS, AND AGENCIES BY ABSORPTION RATES, 2015/16

Ministry/Department/Commissions	Actual (Ksh. billions)	Target (Ksh. billions)	Variance	% Total expenditure to total target
National Intelligence Service	21,486	21,507	-21	99.9%
National Land Commission	1,527	1,529	-2	99.9%
Ministry of Defense	92,180	92,347	-167	99.8%
Public Service Commission	1,129	1,113	-4	99.6%
Ministry of Sports, Culture, and Arts	6,679	6,710	-31	99.5%
Independent Police Oversight Authority	255	396	-141	64.4%
Ministry of Foreign Affairs and International Trade	9,355	16,527	-7,172	56.6%
Ministry of Water and Irrigation	20,572	41,019	-20,447	50.2%
Ministry of Environment, Natural Resources, and Regional Development Authorities	10,088	21,315	-11,227	47.3%
State Department of Transport	68,734	170,323	-101,589	40.4%
Total (all MDAs)	1,205,709	1,494,599	-288,890	80.7%

Source: BROP 2016 (Table 3).

Overall, total national expenditure was projected to grow by 9 percent above the previous year's target (see Table 5) while MDA expenditure was projected to grow by 6 percent from the previous year's target. This is a much lower growth rate than the previous year's expectations (28 percent for both national and MDA expenditure). As we saw with revenues, however, comparing expenditure targets without looking at actual expenditure growth from year to year can be misleading.

The last column of Table 5 shows the targets for 2015/16 against the actual expenditure in 2014/15. These figures can be compared to the average annual growth in the fourth column. It is clear that the expenditure targets were highly ambitious. Total MDA expenditure growth is above the average for the past several years, but far below target, especially for development spending. Total national expenditure growth is much lower than average and also far below target.

TABLE 5. HOW REALISTIC WERE THE 2015/16 EXPENDITURE TARGETS?

Expenditure	Changes in actual expenditure between 2011/12 and 2012/13	Changes in actual expenditure between 2012/13 and 2013/14	Changes in actual expenditure between 2013/14 and 2014/15	Average actual expenditure growth 2011/12 and 2014/15	Changes in actual expenditure between 2014/15 and 2015/16	Changes in expenditure estimates (targets) between 2014/15 and 2015/16	Projected revenue estimates (target) in 2015/16 against actual expenditure in 2014/15
Recurrent MDAs expenditure	25%	-6%	7%	9%	22%	14%	22%
Development MDAs expenditure	-1%	7%	28%	11%	-5%	-2%	67%
Total MDAs expenditure	15%	-2%	14%	9%	12%	6%	39%
Total expenditure	18%	19%	24%	20%	9%	9%	24%

Sources: IBP Kenya calculation from BROP 2012 (Table 3), BROP 2013 (Table 3), BROP 2014 (Tables 2 and 3), BROP 2015 (Tables 2 and 3), and BROP 2016 (Tables 2 and 3).
Note: The total expenditure figures are obtained from the most recent BROP. For example, actual total expenditure for 2014/15 is obtained from the 2016 BROP and compared to the target for the same year as in the 2015 BROP. This includes MDAs and other expenditure such as county transfers.

The absorption rate has reduced significantly for some key sectors. The water and natural resources and energy, infrastructure and ICT sectors had the highest increase and decrease in absorption rate respectively in 2015/16. There was a significant improvement in the absorption rates for the governance, justice, law and order and agriculture. The BROP offers no explanation for variations in performance at sector level.

TABLE 6. CHANGE IN SECTOR EXPENDITURE PERFORMANCE BETWEEN 2014/15 AND 2015/16

Sectors	Absorption 2014/15	Absorption 2015/16	Change in Sector Expenditure Performance
Energy, Infrastructure & ICT	49.26%	64.43%	15.16%
Governance, Justice, Law & Order	78.71%	90.05%	11.33%
Agriculture	76.65%	84.79%	8.14%
Public Administration & International Relations	84.53%	89.26%	4.73%
Social Protection, Culture & Recreation	85.03%	87.95%	2.92%
General Economic and Commercial Affairs	94.59%	94.94%	0.35%
National Security	99.91%	99.83%	-0.07%
Education	96.02%	89.11%	-6.91%
Health	79.63%	69.97%	-9.66%
Environment Protection, Water & Natural Resources	82.71%	49.88%	-32.83%
Average absorption/change	82.70%	82.02%	-0.68%

Source: IBP Kenya Calculations based on BROP 2015 (Table 3) and BROP 2016 (Table 3).

The share of the budget spent on wages has been a matter of public debate in recent years. According to the BROP, wages continued to rise in 2015/16 by about 3.2 percent. This is less than the rate of inflation and lower than the rate of revenue growth, meaning that the share of total revenue (excluding grants) used to pay wages is falling (from 26.9 to 24.8 percent).

However, the reported public wage bill in the BROP seems not to include all wages. The BROP 2016 states that wages are “for teachers and civil servants including the police” and appears to exclude state corporations. We compared the wage bill in the BROP to figures from two other sources: the 2016 Annual National Government Budget Implementation Review Report (BIRR) from the Controller of Budget (COB), and the Economic Survey 2016. The COB figure for MDAs personnel costs was Ksh 311 billion in 2015/16, similar to (but slightly higher than) the BROP figure. It appears that COB figures may also exclude state corporations. How much wage employment is there in state corporations? The Economic Survey 2016 estimates that in state corporations fully held by the government, wage employment in 2015 was over Ksh 78 billion.[3] This does not include majority owned corporations. The failure to account for such workers suggests that the total wage bill presented in the BROP is underestimated.

TABLE 7. HOW BIG IS THE WAGE BILL IN KENYA? (KSH BILLIONS)

	2013/14	2014/15	2015/16
BROP 2016 Actual total wage bill (in billions)	281	298	307
COB BIRR total wage bill (in billions)	268	283	312
Economic survey 2016 parastatals wage bill	66	74	78

Source: BROP 2016 (Table 4), Economic Survey, 2016 (Table 4.6), COB BIRR 2014 (Table 3.9) 2015 (Table 3.12) 2016 (Table 3.4). Parastatals includes only wholly government owned state corporations.

BOX 2. JUSTIFICATIONS AND EXPLANATIONS FOR EXPENDITURE PERFORMANCE

The BROP does not explain variations in performance at the MDA level. In BROPs from the last few years, the Treasury has identified poor reporting on development spending from subnational units as a major reason for underperformance in development absorption. However, there are no further details about the magnitude of this problem or how it can be solved.

Are the root causes of expenditure performance given?

The BROP offers generic explanations for overall expenditure performance such as "low absorption," which is a description rather than an explanation and does not point toward possible resolutions. BROP 2015 highlighted delays in procurement as well as non-inclusion of expenditure from districts and some donor-funded projects as challenges. While failure to capture sub-county and donor expenditure is mentioned in BROP 2016, nothing is said about procurement as an explanation of poor performance in 2015/16. It is unclear if this means that procurement challenges have been resolved.

Does the BROP explain differences in performance between MDAs?

There is no explanation of performance at MDA level that differentiates between better and worse performing ministries, despite their considerable differences. For example, why did the National Intelligence Service and National Land Commission manage to absorb almost all their allocation while the State Department of Transport is among the MDAs with the lowest absorption for two consecutive years? It is also not clear what pushed the Ministry of Land, Housing and Urban Development and the Ministry of Sports Culture and Arts to spend more than their budget estimates.

What solutions have been put forward for persistent challenges?

The BROP 2016 suggests that persistent challenges in development absorption will be dealt with by accounting officers "realistically prepar[ing] budgets" and "convening quarterly meetings of the Aid Effectiveness Group"

[3] See the Economic Survey 2016, page 77 (Table 4.6). Available at http://www.knbs.or.ke/index.php?option=com_content&view=article&id=369:economic-survey-2016&catid=82:news&Itemid=593

to improve coordination with donors. These proposals are not connected to clear explanations of challenges. For example, why are accounting officers not producing realistic budgets and how will their incentives change to encourage them to do so? In addition, the paragraphs on these remedies are identical to those in the BROP 2015 (paragraph 32-35), suggesting nothing has been done since then to address spending challenges.

DEFICIT AND DEBT

The overall fiscal deficit for 2015/16 was 31 percent of the total expenditure, a slight decrease from previous years. The 2016 BROP projects that the deficit will drop slightly in 2016/17 to 30 percent of total spending. Table 8 shows the relationship between the deficit and public debt. Public debt continued to rise by a substantial amount in 2015/16, both in absolute terms and as a share of GDP.

TABLE 8. BUDGET DEFICIT AND PUBLIC DEBT BETWEEN 2013/14 AND 2017/18

	2013/14 (actual)	**2014/15 (actual)**	**2015/16 (actual)**	**2016/17 (projections)**	**2017/18 (projections)**
Fiscal deficit (commitment basis excluding grants) (billions)	326	532	544	618	596
Total expenditure (billions)	1,301	1,640	1,782	2,074	2,237
Deficit as a % of the total expenditure estimates	25%	32%	31%	30%	27%
Public debt	2,423	2,844	3,618	3,850	2,377
Public debt to GDP	48%	49%	56%	53%	
	Growth between 2013/14 and 2014/15	**Growth between 2014/15 and 2015/16**	**Growth between 2015/16 and 2016/17**		
Fiscal deficit growth	63%	2%	14%		
Public debt growth	17%	27%	6%		

Sources: IBP Kenya calculations based on BROPs 2014-2016, Annex Table 2.
Notes: We calculated public debt by adding up "external debt" and "domestic debt (gross)" and compared this with the nominal GDP as provided by the BROP. Net domestic debt is obviously lower in absolute terms than gross debt, but the trend is still rising debt and debt/GDP over the period.

We also consulted the Controller of Budget reports to look at the burden of debt repayment each year. Debt repayment has also continued to rise (by roughly Ksh 28 billion), but in 2015/16, debt repayment as a percentage of the total actual revenue (excluding grants) reduced relative to 2014/15.[4]

[4] The COB BIRR figures are the best we have available for the period, but they do not match Treasury's figures in other sources. For example, in the Kenya Gazette, the figures are: 2012/13 -Ksh 227.6 billion; 2013/14- Ksh 416.2 billion and 2015/16 (11 months only)- 387.5 Ksh billion.

TABLE 9. PUBLIC DEBT REPAYMENT 2013/14-2015/16

	2013/14 (actual)	2014/15 (actual)	2015/16 (actual)
Public debt repayment (in billions)	279	393	421
Ordinary revenue (in billions)	919	1,032	1,158
Debt repayment as a % of the total actual revenue	30%	38%	36%

Source: Ordinary revenue from BROP 2015 (Table 1), BROP 2016 (Table 1) and debt repayment from COB BIRR (2014 Table 3.7, 2015 Table 3.9 and 2016 Table 3.2).

UPDATES TO THE FISCAL EXPECTATIONS AND IMPLICATIONS FOR BUDGET PERFORMANCE IN THE CURRENT YEAR (2016/17) AND UPCOMING YEAR (2017/18)

The 2016 BROP indicates that the economy is projected to grow by 6.1 percent in 2016/17. This is marginally lower (6.0 percent) in the recently released Budget Policy Statement (BPS) 2017. Both rates are above the 2015/16 expansion of 5.8 percent. Why does government expect increased growth this year? Comparing the BROP 2016 and the BPS 2017, it is not clear: the BROP speaks about growth in the manufacturing sector, construction, and sustained "delivery of inputs" to the agriculture sector. But the BPS speaks of infrastructure development, domestic demand, and tourism. There is no single coherent view of the drivers of growth in these documents.

Inflation is projected to be 5.6 percent for the year in both BROP 2016 and BPS 2017, above the 5 percent predicted in the BPS 2016. This is not explained, but the BPS 2017 does mention higher food prices in recent months as a driver of inflation.

The BROP adjusts the budget targets for 2016/17 to take into account performance in 2015/16. This has resulted in a reduction in both revenue and expenditure targets in 2016/17. Expenditure is projected to fall by 9 percent (Ksh 201.5 billion) and revenue by 3 percent (Ksh 44 billion). Recurrent expenditure is projected to increase by 1.3 percent (Ksh 15 billion) from the allocation in the 2016/17 budget. The decrease in proposed expenditure is driven by a decline of Ksh 216 billion (26.5 percent) in total development expenditure, while recurrent spending is rising slightly. The BROP 2016 does not clarify which specific sectors will be reduced to achieve this, nor which revenue sources will be shy of initial projections.

The 2016 BROP revision of the development budget was anticipated in the 2016/17 budget. When the budget was tabled in Parliament in April, the Treasury indicated that total external financing was not likely to be fully realized. Despite the expectation that only Ksh 195 billion of the external grants proposed were going to be received, the Treasury budgeted more than twice this amount.[5] Most of the external financing was to the State Department of Transport (Ksh 126 billion), State Department for Energy (Ksh 81 billion), and State Department of Infrastructure (Ksh 55 billion).[6] However, the BROP does not actually mention this earlier concern in explaining the decline in expected expenditure.

The large decline in expenditure and smaller decline in revenues has led to a reduction in the proposed deficit of Ksh 157 billion. This translates into a large decline in foreign financing (down by Ksh 175 billion) and grants (down by Ksh 41 billion), but an increase in domestic financing (up by Ksh 59 billion). It is not clear why there is a shift in the relative weight given to foreign and domestic borrowing in the BROP.

Notably, the BPS 2017 reverses some of these expectations. It projects a small further reduction of the development expenditure for the year 2016/17 by Ksh 10.3 billion, but in other ways is inconsistent with the BROP. For example, while the BROP projects a decline in total revenue of Ksh 44 billion from the original budget, the BPS projects an increase of Ksh 18 billion against the original budget. This seems related to another major difference between the BPS and BROP: the BROP showed an increase in domestic financing (borrowing), while the BPS shows domestic financing is set to reduce by Ksh 67.8 billion. The increase in domestic revenue and decrease in domestic borrowing is driven by projected increases in specific revenue sources: excise duty, investment income, and ministerial AiA. There is no explanation of these revenue increases in the BPS 2017.

The 2016 BROP also projects total revenue and expenditure for 2017/18. What are the targets and how realistic are they? The total revenue and grants projection for 2017/18 is Ksh 1.69 trillion, a 16.2 percent increase from the 2016/17 budget (using revised budget figures in BROP 2016). Ordinary revenue and AiA is expected to increase by 13.5 percent and 5 percent respectively, while grants are expected to increase by 63.7 percent from the revised 2016/17 budget (calculations based on BROP Annex Table 2).

Are these realistic targets? To answer this question, we looked at the 2017/18 projections against a reasonable estimate of 2016/17 actual revenue (see Table 10). Our projection of 2016/17 revenue is based on adjusting the actual 2015/16 revenue collections by the average annual growth rate of revenue over the previous five years. For example, for total revenue, we take the 2015/16 actual total revenue and

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[5] The Budget Summary for the Fiscal Year 2016/17 and Supporting Information, Page 1, Para 20. Available at http://www.treasury.go.ke/component/jdownloads/send/11-related-documents/6-budget-summary-for-the-fy-2016-2017-and-supporting-information.html

[6] The Development Budget Book 2016-17 Volume 1, Table II page ix-xii. Available at http://www.treasury.go.ke/component/jdownloads/send/6-budget/223-development-budget-book-2016-17-volume-1.html

grants figure of Ksh 1.268 trillion and adjust it by a factor of 13.6 percent, the average annual growth over the last five years, to calculate the 2016/17 projection of Ksh 1.439 trillion. We then compare the 2017/18 BROP figure for total revenue to that and calculate 2017/18 projected growth. In doing so, we can see that the 2017/18 figures are not realistic: projected growth of nearly 18 percent is above average and above most recent years. Projected revenue from AiA and grants is particularly unrealistic.

Turning to expenditure growth, the total expenditure and net lending projection for 2017/18 is Ksh 2.24 trillion, a 7.8 percent increase from the revised 2016/17 budget. This is below the average actual growth (17.2 percent) from 2011/12 to 2015/16, suggesting that it is realistic. The slower growth in expenditure in 2017/18, coupled with ambitious revenue targets, is leading to a reduction of the projected deficit in 2017/18 as compared to the revised 2016/17 budget (from Ksh 618 billion to Ksh 596 billion). However, if the revenue targets were reduced to a more realistic level, using average revenue growth for each source in recent years, the projected deficit would be higher in 2017/18 (Ksh 642 billion) rather than lower.

TABLE 10. HOW REALISTIC ARE THE REVENUE AND EXPENDITURE 2017/18 PROJECTIONS?

	Average actual growth 2011/12-2015/16	**IBP Kenya projection 2016/17 in billions (using average growth in actuals)**	**Projection 2017/18 in billions (2016 BROP)**	**Change 2017/18 (BROP) to 2016/17 (BROP projection)**	**Change 2017/18 (BROP to 2016/17 (IBPK projection)**
Ordinary revenue	13.8%	1318.0	1495.6	13.5%	13.5%
AIA (including railway development levy)	9.1%	86.9	145.3	5.0%	67.2%
Grants	18.8%	35.2	51.9	63.7%	47.6%
Total revenue and grants	13.6%	1439.9	1692.8	13.8%	17.6%
Total expenditure and net lending	17.2%	2088.4	2236.7	7.8%	7.0%

Source: IBP Kenya calculations. For actual revenues and expenditures see BROP 2012 and 2013 (Table 2 and 3), BROP 2014- 2016 (Table 1 & 2). For projection for 2016/17 and 2017/18 see BROP 2016 Annex Table 2.

BOX 3. JUSTIFICATIONS AND EXPLANATIONS FOR CHANGES IN CURRENT FINANCIAL YEAR

Does the BROP adequately explain the changes expected in the current financial year?

The BROP proposes reductions in revenue and expenditure. One reason given for the reductions is that the revenue and expenditure targets in 2015/16 were not met. Because revenue and expenditure was lower than anticipated in 2015/16, the baseline used to project 2016/17 is reduced, resulting in lower figures. However, this does not explain the specific areas where revenue or spending is expected to be lower. BROP 2016 does mention that this is mainly in the area of foreign-funded development expenditure, but no further details are provided. Moreover, no explanation is provided for the decision to shift deficit financing away from foreign sources and toward domestic sources.

Surprisingly, the BPS 2017, released shortly after the BROP 2016, actually increases revenue in 2016/17, moving in the opposite direction of the BROP. No explanation is provided for this sudden shift. There is generally more optimism about specific revenue sources in the BPS 2017, including investment income, excise duty, and ministerial AiA. Why? And why does Treasury suddenly reverse course on increasing domestic borrowing? No justifications are provided for these major shifts in such a short period.

PROVISIONAL SECTOR CEILINGS 2017/18

The total expenditure projection in the 2016 BROP for 2017/18 is Ksh 2.24 trillion, a 1.7 percent decrease from the original 2016/17 printed budget. The total expenditure passing through MDAs has decreased by 1.5 percent from the original 2016/17 printed budget (see Table 12). However, given that the 2016/17 budget will likely be nearly 9 percent below the original printed estimates (BROP projections), the 2017/18 budget for MDAs will probably end up above the 2016/17 spending levels. This is not explained further in the BROP, however.

The biggest shift in the relative share of the budget between 2016/17 and 2017/18 is for energy, infrastructure and ICT, which is set to decrease its share by 2.1 percentage points (see Table 12). Education and public administration are the major beneficiaries, with an increase of nearly one percentage point in the share of the budget going to each.

TABLE 11. CHANGES IN SECTOR ALLOCATIONS BETWEEN THE PRINTED BUDGET 2016/17 AND 2017/18 PROJECTIONS

Sector	Printed estimates sector ceilings 2016/17 (Ksh million)	BROP sector ceilings 2017/18 (Ksh million)	Change in allocation (Ksh million)	Sector share of total budget 2016/17 (printed budget)	Sector share of the total budget 2017/18 (BROP)	Change in sector share of total budget 2016/17 and 2017/18	Sector share of total budget 2017/18 (2017 BPS)	Change in sector share of total budget ceilings BROP 2016 and BPS 2017 for 2017/18
Agriculture, rural & urban development	46,544.2	46,598.1	53.9	2.8%	2.8%	0.0%	2.6%	-0.2%
Energy, infrastructure & ICT	529,162.9	486,253.3	(42,909.6)	31.5%	29.4%	-2.1%	26.7%	-2.7%
General economic & commercial affairs	23,666.2	19,922.9	(3,743.3)	1.4%	1.2%	-0.2%	1.2%	0.0%
Health	60,269.9	60,888.9	619.0	3.6%	3.7%	0.1%	3.4%	-0.3%
Education	339,924.4	349,860.5	9,936.1	20.3%	21.2%	0.9%	23.3%	2.1%
Governance, justice, law & order	195,518.0	192,837.3	(2,680.7)	11.7%	11.7%	0.0%	12.1%	0.4%
Public administration & international relations	224,909.7	235,444.1	10,534.4	13.4%	14.3%	0.9%	15.5%	1.2%
National security	124,045.2	126,104.5	2,059.3	7.4%	7.6%	0.2%	8.1%	0.5%
Social protection, culture & recreation	44,647.5	45,285.2	637.7	2.7%	2.7%	0.0%	2.7%	0.0%
Environment protection, water & natural resources	88,999.4	88,538.8	(460.6)	5.3%	5.4%	0.1%	4.4%	-1.0%
Total	*1,677,687.4*	*1,651,733.6*	*(25,953.8)*	*100.0%*	*100.0%*	*-1.5%*	*100.0%*	*0.0%*

Source: IBP Kenya calculations from 2016 BROP (Table 12) and BPS (Table 3.3)

The narrative in the 2016 BROP suggests that the education, health, and energy sectors will continue to receive the largest share of the budget, as they have in recent years. According to the narrative, the energy sector will take 29.4 percent of the budget, while the social sectors (education and health) will get 24.9 percent of the total MDAs allocation. Despite the energy, infrastructure, and ICT sector being singled out in the 2016 BROP as an area of priority, we have already seen above that its share of the budget is projected to decrease next year while education's share of the budget is projected to increase by 0.9 percentage points (9.9 billion). However, for health, the increase is projected at only 0.1 percentage points next year. It is unclear from the BROP which programs or projects are affected by these changes in budget shares.

Another key priority area for the government, highlighted in previous BROPs, is improving the business environment in Kenya through more investment in the security sector and the governance, justice, law, and order (GJLO) sector. The ceiling for the security sector is projected to rise from 7.4 percent in 2016/17 to 7.6 percent next year. The GJLO sector also received an increasing share of the budget last year. However, despite the sector being a priority for the 2017 election year, the share of total expenditure remains 11.7 percent as in the 2016/17 budget, suggesting that it is not a higher priority in 2017/18. Note that the budget for the sector is actually falling in 2017/18.

The BPS 2017 adds to the confusion about sector priorities. It further decreases the share of the total budget for the “priority” energy, infrastructure, and ICT sector in 2017/18 by 2.7 percentage points. Health, supposedly a priority in the BROP and the BPS, is now experiencing a decline in its share of the budget from 2016/17. Agriculture, rural and urban development, environment protection, as well as water and natural resources are also projected to decrease from the ceilings given in the 2016 BROP. Education is projected to increase further by 2.1 percentage points. Public administration and international relations, not mentioned as a priority in either document, will increase its share of the budget from the 2016 BROP. As in the BROP, the BPS 2017 projects no change in the share of the total budget for social protection, culture, and recreation from the 2016/17 printed budget. There are no explanations for any of the changes between the BROP and BPS.

The sector distribution in both the 2016/17 printed budget and 2016 BROP differ significantly from those in the approved BPS 2016 from last year (see Table 13). Neither the budget nor the BROP offer an explanation for this. These differences are most significant for energy, infrastructure, and ICT (sector share above the BPS 2016) and education, public administration and agriculture (shares below the BPS 2016), but all sectors are affected. The main driver of the change in relative sector shares is the substantial increase in the 2016/17 budget for development in the energy, infrastructure, and ICT sector, an increase of nearly Ksh 162 billion. This change led to an unrealistic development budget, as we saw earlier, and changed the sector shares from what was in the BPS 2016.

TABLE 12. COMPARING SECTOR CEILINGS IN THE BPS 2016 WITH THE 2016/17 BUDGET AND 2016 BROP

Details	Sector share of total MDA ceilings for 2016/17 (BPS 2016)	Sector share of total MDA budget (PBB 2016/17 and BROP 2016/17)	Change in sector shares
Energy infrastructure and ICT	24.53%	31.54%	7.01%
Social protection, culture & recreation	2.16%	2.66%	0.50%
General economic & commercial affairs	1.03%	1.41%	0.39%
Environment protection, water & natural resources	4.98%	5.30%	0.33%
Health	3.98%	3.59%	-0.38%
Governance, justice, law & order	12.20%	11.65%	-0.54%
National security	8.06%	7.39%	-0.67%
Agriculture, rural & urban development	4.36%	2.77%	-1.59%
Public administration & international relations	15.58%	13.41%	-2.17%
Education	23.13%	20.26%	-2.87%

Source: IBP Kenya calculations from BPS

Our final question is whether the sector proposals in the BROP are informed by the performance of sectors in the year 2015/2016. To see this, we can look at the absorption rates for each sector in 2015/16 and compare this to the change in the sector's share of the total budget projected for the year 2017/18 (see Table 13).

TABLE 13. ABSORPTION RATES 2015/16 VERSUS CHANGE IN SHARE OF THE TOTAL BUDGET

Sector	Sector budget absorption rate 2015/16	% Change in sector shares of the total budget 2016/17-2017/18
National security	99.8%	0.9%
General economic & commercial affairs	94.9%	-2.1%
Governance, justice, law & order	90.1%	0.9%
Public administration & international relations	89.3%	0.0%
Education	89.1%	0.1%
Social protection, culture & recreation	88.0%	0.2%
Agriculture	84.8%	0.0%
Health	70.0%	0.0%
Energy, infrastructure & ICT	64.4%	-2.1%
Environment protection, water & natural resources	49.9%	0.1%
Average absorption/change	82.0%	-0.2%

Source: IBP Kenya calculation from 2016 BROP (Table 3 and Table 12).

Despite recording very low absorption in environment protection, water and natural resources, this sector has been awarded a small increase in its share of the total budget in 2017/18. There is no obvious pattern here; the only sectors receiving a declining share of the budget in 2017/18 are the high performing economic and commercial affairs sector and the low performing energy sector. There is no reflection on these matters in the narrative either. Although the BROP contains data on absorption, it does not tell us anything about how sector performance has been incorporated into the decision-making process about sector shares for the coming year.

BOX 4. JUSTIFICATIONS AND EXPLANATIONS FOR PROVISIONAL CEILINGS

Are the underlying rationales for prioritizing certain sectors provided?

No. The section of the 2016 BROP describing priority sectors offers little explanation for changes from last year. It is largely copied from the 2015 BROP, making it difficult to learn about changes from last year. While the narrative suggests that the energy/infrastructure sector is a priority for the year 2017/18, the figures show that the sector's share of the budget is falling in 2017/18. Clearly the narrative cannot explain this. It is also unclear what informed the increase in the education sector or the public administration sector while, for example, the GJLO sector mentioned as a priority in the narrative is not seeing any increase in its share of the budget.

Is there a connection between the proposals for next year and past year performance?

Revenue: The BROP does not directly address how past revenue performance informs future revenue targets, which is one of the purposes of the document. For example, we can see in the BROP that Pay As You Earn (PAYE) tax has under-performed relative to target in 2015/16. The paper should, but does not, tell us how that has affected projections for PAYE going forward (the annex clubs together different income taxes making it difficult to tell what is projected specifically for PAYE). There is a general explanation of why revenues are expected to increase overall: revenue policy will be "underpinned by on-going reforms in tax policy and revenue administration." But there is no detail about what these reforms entail.

Expenditure: Although one purpose of the BROP is to connect a review of past performance to proposed changes in the coming year's budget, there is no specific reflection on how past absorption of funds has been incorporated into proposals for the future. When MDAs have low absorption rates, but are to receive higher budget shares in the coming year, this requires an explanation, as it raises questions about their ability to spend an increased budget. For example, there is an increase in the share of the budget going to the water sector, yet the sector only absorbed half of its budget in the previous year. There may be good reasons for this, but they are not presented in the BROP.