FY'2024/25 Budget Estimates Note

3rd May, 2024

On 30th April 2024, the National Treasury presented its Budget Estimates for the next fiscal year, FY'2024/25. Notably, the budget estimates recorded a 6.4% decrease to Kshs 3.9 tn from the previous estimates of Kshs 4.2 tn in the Budget Policy Statement for FY'2024/25 and a 2.2% increase from the Kshs 3.8 tn in FY'2023/24 as per Supplementary Budget II. Additionally, revenue is set to increase by 16.2% to Kshs 3.4 tn in FY'2024/25 from Kshs 2.9 tn in FY'2023/24. Furthermore, the allocation of resources has been aligned to priority programs and sectors under the Bottom-Up Economic Transformation Agenda, and the Medium-Term Revenue Strategy FY'2024/25-FY'2026/27. This is to ensure spending is directed towards the most critical needs considering the available resources.

As such, we will be reviewing the estimates and discuss the following:

i. A comparison of the Supplementary Budget II FY'2023/24 Budget and the Projected FY'2024/25 Budget as per the 2024 Budget Estimates,

ii. Analysis and House-view on Key Aspects of the 2024 Budget Estimates, and,

iii. Conclusion.

Section I: A comparison of the FY'2023/24 Supplementary Budget II and the Projected FY'2024/25 Budget as per the 2024 Budget Estimates

Below is a summary of the major changes as per the FY'2024/25 Budget Estimates:

Cytonn Report: Budget Estimates FY'2024/25 – FY'2023/2024 Comparison					
	FY'2022/2023 Budget Outturn	FY'2023/2024 Supplementary II Estimates (a)	FY'2024/2025 BPS	FY'2024/2025 Budget Estimates (b)	% change 2023/24 to 2024/25 (a/b)
Total revenue	2,360.5	2,886.1	3,435.0	3,354.2	16.2%
External grants	23.1	42.8	49.3	51.8	21.0%
Total revenue & external grants	**2,383.6**	**2,928.9**	**3,484.3**	**3,406.0**	**16.3%**
Recurrent expenditure	2,311.6	2,762.6	2,859.3	2,781.7	0.7%
Development expenditure & Net Lending	493.7	649.8	877.8	687.9	5.9%
County governments + contingencies	415.8	423.9	451.1	451.1	6.4%
Total expenditure	**3,221.0**	**3,837.5**	**4,188.2**	**3,920.7**	**2.2%**
Fiscal deficit including grants	**837.4**	**908.6**	**703.9**	**514.7**	**(43.4%)**
Deficit as % of GDP	5.9%	5.6%	3.9%	2.9%	(2.7%)
Net foreign borrowing	310.8	501.6	326.1	256.8	(48.8%)
Net domestic borrowing	459.5	407	377.7	257.9	(36.6%)
Total borrowing	770.3	908.6	703.9	514.7	(43.4%)
GDP Estimate	14,274.4	16,131.5	18,015.2	18,015.2	11.7%

Source: National Treasury, Amounts in Kshs bns

Some of the key take-outs include;

i. The FY'2024/25 Budget Estimates point to a 2.2% increase of the budget, to Kshs 3.9 tn from Kshs 3.8 tn in the FY'2023/24 Supplementary Budget II,

ii. Recurrent expenditure is set to increase by 0.7% to Kshs 2.78 tn, from Kshs 2.76 tn as per the Supplementary Budget II, while development expenditure is projected to increase by 5.9% to Kshs 687.9 bn from Kshs 649.8 bn as per the FY'2023/24 Supplementary Budget II. Under recurrent expenditures, interest payments expenditures increased by 18.3% to Kshs 1,009.9 bn, from Kshs 853.7 bn, while pension expenditures increased by 6.7% to Kshs 169.2 bn from Kshs 158.6 bn in the FY'2023/24 Supplementary Budget II,

iii. The budget deficit is projected to decline to Kshs 514.7 bn (2.9% of GDP) from the projected Kshs 703.9 bn (3.9% of GDP) in the FY'2023/24 Supplementary Budget II; in line with the International Monetary Fund's (IMF's) recommendation, in a bid to reduce Kenya's public debt requirements,

iv. Revenue is projected to increase by 16.2% to Kshs 3.4 tn, from Kshs 2.9 tn in the FY'2023/24 Supplementary Budget II, with measures already in place to work towards increasing the amount of revenue collected in the next fiscal year,

v. Total borrowing is expected to decline by 43.4% to Kshs 514.7 bn from Kshs 908.6 bn as per the FY'2023/24 Supplementary Budget II, in a bid to reduce Kenya's public debt burden which is estimated at 67.2% of GDP currently, 12.2% points above the East African Community (EAC) Monetary Union Protocol, the World Bank Country Policy and Institutional Assessment Index, and the IMF threshold of 55.0%, and,

vi. Debt financing of the 2024/25 budget is estimated to consist of 49.9% foreign debt and 50.1% domestic debt, from 55.2% foreign and 44.8% domestic as per the FY'2023/24 Supplementary Budget II.

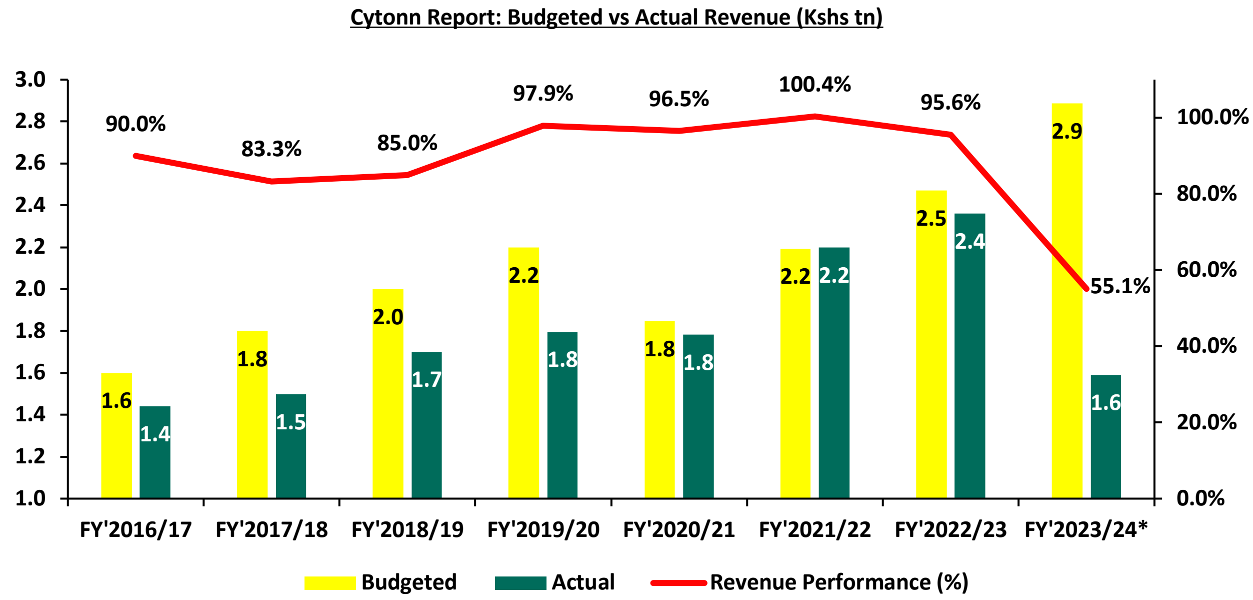
Section II: Analysis and House-view on Key Aspects of the FY'2024/25 Budget Estimates

Below we give our analysis and view on various aspects of the 2024 Budget Estimates:

1. **Revenue collection Fiscal Policy Framework:**

The estimates target a total revenue collection of Kshs 3.4 tn which is 18.6% of the GDP, where ordinary revenues are projected to come in at Kshs 2.9 tn or 16.2% of GDP. The ongoing reforms in tax policy and revenue administration will support revenue performance, as revenue collection is expected to be enhanced by tax amendments meant to broaden the tax base in the Finance Act 2024.

However, the performance of tax revenue collection has consistently remained below the set targets, on account of unfavorable business environment. According to the end of March 2024 Exchequer Issues, Kenya Revenue Authority (KRA) had only managed to collect Kshs 1.5 tn in tax revenue, which is 82.0% of the prorated Kshs 1.9 tn, and 61.5% of the FY'2023/24 estimates of Kshs 2.5 tn. The chart below represents revenue performance over the years;



**Revenue collection up to ninth month of the year*

The government's goal is to reduce the fiscal deficit and stabilize growth in public debt while ensuring debt sustainability. They intend to achieve this through a combination of revenue enhancement initiatives and expenditure rationalization. We are of the view that the higher targeted revenue collection will be driven by the prospects of an economic recovery, rather than higher taxes. The budget estimates indicated that the government is set to cut back on borrowing, with total net borrowing reducing to Kshs 514.7 bn, from Kshs 908.6 bn in FY'2023/24 Supplementary Budget II, and instead opt for higher taxation, widening the tax base and sealing tax leakages by incorporating the informal sector in tax collection.

2. **Expenditure Projections:**

As per the FY'2024/25 budget estimates, total expenditure is set to increase by 2.2% to Kshs 3.9 tn from Kshs 3.8 tn in the Supplementary Budget II FY'2023/24, which is a notable decrease from the Kshs 4.2 tn estimated in the earlier budget policy statement for FY'2024/25. Both rrecurrent and development expenditures are set to increase, with development expenditure expected to increase by a greater margin of 5.9% to Kshs 687.9 bn from Kshs 649.8 bn, with recurrent increasing by 0.7% to Kshs 2.78 tn, from Kshs 2.76 tn per the Supplementary Budget II. The increase in the recurrent expenditure has mainly been driven by the increased interest payments in the past given the high borrowing in the country, with interest payments expected to increase by 18.3% to Kshs 1,008.7 bn in FY'2024/25, from Kshs 853.7 bn in FY2023/24 as per the Supplementary Budget II. Despite the 5.9% increase in development expenditure, one of the key concerns over the period has been the proportion of recurrent expenditure compared to development spending which as per the estimates is expected to come in at 70.9% against 17.5%, respectively.

Additionally, despite a small proportion of the expenditure going to development expenditure, the government has continually underperformed in development projects, only achieving 48.9% of the estimates as per FY'2023/24 Supplementary Budget II as of the end of the ninth month of the year. Hence, the quality of fiscal consolidation remains a concern as a majority of the cuts to government expenditure falls on development spending, which could potentially compromise the growth potential of the economy. To reduce government expenditure, and in turn, what needs to be plugged in through borrowing, we suggest the following:

i. **Strict adherence to Expenditure rationalization framework** which is meant to cut down on spending. Following the revision of the fiscal framework, expenditure for FY'2024/25 has been adjusted to: a) Reduction on non-priority recurrent expenditure by 50.0%, and freezing foreign travel; b) Reduction of government grants to parastatals to not more than 70.0% of the approved budget; c) Scaling down government funding of capital projects and Development Partners' Funded projects by 30.0% and 25.0% respectively,

ii. **Encouragement of sustainable Public-Private Partnerships (PPPs)** which will involve the private sector in development and increase efficiency while reducing pressure on the government. The government should work towards a harmonized public investment policy that will be used to address some of the challenges facing the effectiveness of PPPs like poor project delivery and weak investment policy framework,

iii. **Reduction of the public wage bill** - through rationalization of the public office roles we currently have by getting rid of redundancies in the representation of counties and constituencies, etc., relooking at the salaries, allowances, and benefits earned,

iv. **Better efforts to fight corruption**, as funds lost to corruption are estimated at roughly a third of the national budget, Kenya has been engaged in the fight against corruption since the 1960s, without successfully being able to get rid of recurrent scandals involving huge sums of public funds, and,

v. **Development budget absorption needs to improve** as most fiscal years end in an under-absorbed development budget and an over-spent recurrent budget. Development projects need to be prioritized and better planning incorporated to match fund availability to project execution, and measures taken to improve the public procurement process; while also being prudent in recurrent spending.

3. **Deficit Financing:**

From the tabled estimates, the fiscal deficit is projected at 2.9% of GDP, the lowest in 15 years, whose funding will be through a net external borrowing of Kshs 256.8 bn coupled with a net domestic borrowing of Kshs 257.9 bn. The total new public debt requirement for FY'2024/25 is set to decline by 1.8% to Kshs 1.9 tn from Kshs 1.8 tn, in FY'2023/24, as per the Supplementary Budget II. For the Medium term, borrowed funds will be limited to purposes of financing development and not for recurrent expenditure, which is in line with the Public Finance Management (PFM) Act Section 15. Notably, according to the estimates, external borrowing to domestic borrowing composition is estimated to shift to 50:50, from 55:45 as per the FY'2023/24 Supplementary Budget II.

Considering the projected revenues and expenditures, for the medium-term, the government borrowings shall only be used for the purpose of financing development expenditure and not for recurrent expenditure. Additionally, the government remains keen on resource allocation to the Bottom-Up Economic Transformation Agenda (BETA), which aims to increase investments in main sectors like agriculture, MSMEs, affordable housing, healthcare, and digital infrastructure.

Section III: Conclusion

In line with the expectation, the FY'2024/25 budget estimates point to a less expansionary budget in a bid to stay within our means as a country, with the government hoping to keep its expenditure in check, while increasing the revenue significantly. The budget is however hinged on meeting the revenue collection targets, expected to be boosted by increased taxes, while increasing the tax revenue base and fixing the existing leakages, especially in the informal sector. This premise however ought to be a factor of economic recovery which is still uncertain given the uncertainty surrounding the economic growth, tough business environment, geo-political threats, and a volatile exchange rate. The fiscal deficit is estimated to reduce to 2.9% of GDP mainly as a result of a marginal increase in recurrent expenditure and an improvement in revenues. The latter will be highly dependent on how well the government will be able to implement some of the measures put in place and the economic performance. Debt sustainability remains a key concern, despite the country's public debt–to-GDP ratio having decreased to an estimated 67.2% currently, well above the set benchmark of 55.0%, from 70.2% in 2023, but a major increase over the last 10 years, from 44.3% as at the end of 2013 with more than half of the debt being external. In our view, there are still concerns on how the government will be able to meet its revenue collection targets given that KRA has not been able to meet its revenue collection targets for the current year FY'2023/24 owing to poor business environment and existing leakages.