PARLIAMENTARY SERVICE COMMISSION

THE MP's BUDGET WATCH

Budget Digest Vol. 3 June 2010

Disclaimer

The parliamentary Budget Office (PBO) is a non-partisan professional office of the Kenya National Assembly whose primary function is to provide timely and objective information and analysis concerning the national budget and economy.

Preface

The budget Digest Vol. 3 of June 2010 is one of a series of reports on the state of the budget and the economy that the Parliamentary Budget Office (PBO) produces in collaboration with Research Department with support from State University of New York, Kenya Parliamentary Strengthening Programme. It unpacks the salient issues underpinning the 2010/11 budget. The document was spearheaded by the Parliamentary Budget Office. A detailed list of contributors appears in Appendix 3.

The report is designed to provide Members of Parliament and other stakeholders with an in-depth analysis of the Budget. The Objective is to facilitate informed budgetary role of members while enriching debate and scrutiny.

Contents

"Was this a grass root budget? Has the unit of service delivery turned into constituency? Can every part of the country expect to have more nurses, more teachers, and access a computer? The road sector has been allocated huge resources; does this signify an end to potholes and muddy roads? For the experts' their verdict is that this was a very ambitious budget that presents difficulties in actualizing. Indeed, they claimed that the country was running on one engine-the domestic economy and if it stalls, the country would be in serious trouble"

I. INTRODUCTION

1. This years' budget was prepared at a time when the country had received adequate rains and against a backdrop of political stability and an economy that had showed signs of recovery. The key expectation as the Minister for Finance read the speech whose theme was **"Towards inclusive and Sustainable Rapid Economic Growth Rate"** was the quest to achieve a sustainable economic growth that ensures equity in wealth distribution based on available resources.
2. The Minister in his budget speech outlined the strategic framework that the government will follow leading to the country returning to the growth pattern attained in 2007 of 7% is sustained and thereafter accelerating growth further to reach the vision 2030 annual target of 10% in the course of the next five years. The strategic Framework of achieving this is underpinned by maintaining macroeconomic stability; fully implementing the East African Common Market Protocol; facilitating Business Development for wealth and employment creation; and investing in security for economic recovery.
3. Fundamental to this strategic framework is the urgent need for the Minister to address unemployment challenges, institute structural reforms aimed at increasing productivity and improving business climate, scaling up implementation of the socio-economic projects in marginalized areas as well as dedication of resources in infrastructure for the attainment of the faster development.

II. SALIENT MACROECONOMIC ISSUES UNDERPINNING THE 2010/11 BUDGET AND THE MEDIUM TERM

5. The Government budget affects, and in turn is affected by, the performance of the economy. As such, policy decisions regarding the overall levels of spending and taxes are influenced by the performance of the economy. Indeed, economic growth impacts both spending and taxes. Accelerated economic growth reduces outlays because debt, and corresponding interest payments on that debt, is reduced marginally. According to the economic survey, the economy posted a real growth in GDP of 2.6 percent in 2009 compared to 1.6 percent in 2008. Table 1 gives the key drivers of the economy in 2008 and 2009.

Table1: Sectoral analysis of the Economy in 2008 and 2009

Sector	2008	2009
Hotels and restaurants	-36.1%	42.8%
Construction	8.20%	14.1%
Manufacturing	3.5%	2.0%
Transport and communication	3.10%	6.4%
Financial intermediation	2.70%	4.6%
Fishing	-13.2%	7.4%
Agriculture and forestry	-4.10%	-2.6%
Mining and Quarrying	2.90%	-4.2%
Electricity and Water Supply	5.40%	-3.1%

Source: Economic Survey, 2010

From the above figures, it is evident that the 2.6 percent was mainly driven by:

- Resurgence of activities in the tourism sector
- Resilience in the building and construction industry; and
- Transport and communication sector.

6. According to the Budget Speech, it is forecasted that in 2010/2011, a 5.1% GDP growth rate will be attained. This is based on the premise that the economy is recovering from global financial crisis and the effects of post election violence. This growth rate target may be quite difficult to attain since there are key issues of concern among them, ***low investment levels and over reliance on the domestic market to spur growth***.

7. Kenya's economy is susceptible to economic imbalances occasioned by high vulnerability to domestic shocks and its inability to fully insulate itself to future external crises. Thus the economy will be termed to be running on One Engine[1]. "Running on One Engine", reflects the structural imbalance of Kenya's current economy—Kenya's strong engine is domestic consumption while its weak engine is exports".

8. In addition, the uncertainty surrounding the debt crisis in the EU is likely to negatively impact on Kenya's growth prospects. According to the World Bank Report, ***sectors which are mainly producing for the domestic market such as the service sectors and construction were the main drivers of growth***. ***Will these same sectors be the same drivers for the***

[1] **Kenya Economic Report Update, June 2010, Edition No.2.**

attainment of the targeted growth and how well is the budget aligned to ensure such sectors are able to spur the high growth target remains a challenge.

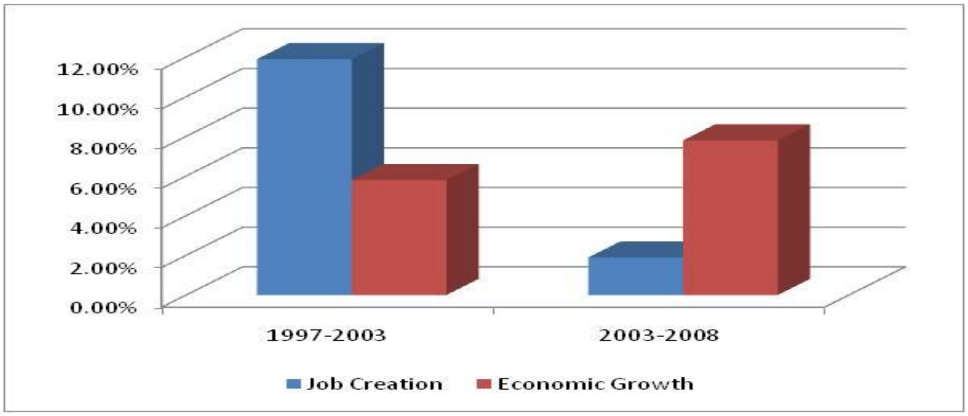
9. The forecast rate of economic growth of 5.1 percent for Fiscal Year 2010/11 will not only depend on local but also on the external environment. The economic activities of major trading partners such as the European Union (EU) will also have an impact on the performance of the (Kenyan) economy. The European financial system is currently in the throes of recovery from the stresses suffered in the last financial year triggered by concerns and fears of the solvency of several governments. In addition, the growth prospects in Kenya will also depend on the success of full implementation of the EAC Common markets protocol (EAC is a major destination of Kenya's exports). For Kenya to achieve and sustain high levels of growth there is need to unlock the export potential. Of particular importance is the need to address the dilapidated link roads to the regional market as well as addressing other structural reforms geared towards reducing the cost of doing business, including unlocking the potential of the port of Mombasa.

Employment Creation

10. Available data show a negative correlation between periods of high economic growth and dwindling levels of employment (Figure 1). This evidence is attributed to government' pursuance of a policy on wealth creation at the expense of job creation. The *Jua Kali* sector which is the major employer– has been largely ignored in favour of the formal sector. Affordable credit to SMEs as a key incentive to the sector among others is yet to be addressed.

11. In this year's budget, the Minister attempted to mitigate this by setting up a **Kshs.3.8 billion** revolving fund to be disseminated through banks and financial systems. The Minister also in his attempt to create an enabling environment for SME's to expand employment opportunities proposed a series of structural reforms e.g. enhancing access to credit and fast tracking, license application among others. The accessibility of these funds is however, not guaranteed and the potential of reaching the intended clientele base remains to be seen. Arguably, other similar funds such as the youth enterprise fund and the women's kitty continue to face myriad of problems with regards to modalities of disbursement.

Figure 1: Comparison between Economic Growth and Employment



12. The other key intervention in the budget is the " **Kazi Kwa Vijana"** which is poised to support creation of jobs particularly in the rural areas. To this end, there is need to put in a strategy that goes beyond just job creation to skills development. This calls for enhancing skills formation, agricultural productivity (targeting resource poor farmers), and enabling and empowering "jua kali".

Inflation and Monetary Policies

13. The ultimate goal of monetary policy is to promote a macroeconomic environment that is both stable and supportive of economic growth, the expansion of decent employment, and reduction of poverty. The 2010/11 budget has been prepared against a backdrop of reduced inflation levels to a tune of less than 5% (from double digit figures in the financial year 2008/09). ***Inflation target of 5% was based on the earlier methodology and hence the figure as highlighted in the budget speech ought to be lower due to the revision in measurement.*** More importantly, some of the components of inflation that impact on purchasing power exhibit volatility owing to seasonal changes in food prices.

14. Evidence shows that[2] the current monetary policy regime has not substantially supported positive real interest rate, which is key in promoting private investment, economic growth, and employment.

15. Concerning the conduct of monetary policy, the approach taken by the CBK has not been well targeted in the sense that is has not been able to shift in line with the changes in the environment. Monetary policy should be designed to provide economic stimulus during

[2] **"Expanding Descent Employment in Kenya: The Role of Monetary Policy, Inflation Control, and Exchange Rate (International Poverty Centre, March 2007).**

periods of contraction and treat inflation differently depending on whether inflation is resulting from excess aggregate demand or shocks from the domestic front as well as external environment. The design of the Kenyan monetary policy framework seems not to have adhered to this principle.

Exchange Rate

16. Exchange rate movements affect economic growth, employment, living standards and the distribution of resources between sectors that trade both at global markets levels and those that produce for domestic consumption. Therefore, appropriate exchange rate policies are critical in designing appropriate economic programmes that can succeed in promoting growth and employment creation. ***Available evidence shows that the Kenyan shilling has been overvalued since 1995.*** In addition, ***the foreign exchange market in Kenya faces serious structural weaknesses that need to be addressed.*** Among the very urgent measure is putting in place a transparent and accessible foreign exchange market.

III. RESOURCE MOBILIZATION FOR FINANCING THE 2010/2011 BUDGET

Table 2: Summary of Resource Outturn for 2010/11

Table 2: Summary of Resources Outturn in Kshs. Million										
	2009/10 original	2009/010 (revised)	Budget Policy Statement (2010/11)	2010/11 (Printed)	Deviation (BPS - Printed Est.	% of Expenditure (09/010)	% of Expenditure BPS (010/011)	% of Expenditure Printed (010/011)	2009/010 (Revised) % of GDP	2010/011 (Printed) % of GDP
Ordinary Revenue	463,642	522,766	580,000	609,639	-29,639	58.94%	70.60%	61.04%	21.12%	22.03%
Other Revenues (AIA Including LATF)	41,753	42,807	49,200	70,973	-21,773	4.83%	5.99%	7.11%	1.73%	2.56%
Loans	68,500	66,500	75,300	102,721	-27,421	7.50%	9.17%	10.28%	2.69%	3.71%
Grants	35,300	31,200	38,800	40,357	-1,557	3.52%	4.72%	4.04%	1.26%	1.46%
Total Receipts	**609,195**	**663,273**	**743,300**	**823,690**	-80,390	**74.78%**	90.48%	**82.47%**	**26.79%**	**29.77%**
Total Expenditure	865,620	887,019	821,500	998,824	-177,324	100.00%	100.00%	100.00%	35.83%	36.10%
Deficit (Financed as shown below)*	**194,962**	**202,962**	**153,500**	**167,215**	**-13,715**	**22.52%**	**18.69%**	**16.74%**	**8.20%**	**6.04%**
: New borrowing (Treasury Bills / Bo	76,650	93,150		73,702		8.85%		10.50%	3.76%	2.66%
: Infrastructure Bonds	32,850	32,850		31,587		3.79%		3.70%	1.33%	1.14%
: Domestic Debt Rollover	76,506	76,506		61,442		8.84%		8.63%	3.09%	2.22%
: Italian Debt Swap	456	456		484		0.05%		0.05%	0.02%	0.02%
: Privitization Proceeds	6,000	-		-		0.69%		0.00%	0.00%	0.00%
: Other Receipts	2,500	-		-		0.29%		0.00%	0.00%	0.00%
Nominal GDP Based on the Budget Strategy Paper	2,546,600	2,475,400	2,805,000	2,767,200						
*The BPS Does not the breakdown of the financing items										

17. According to the Budget Speech, the total revenue target for fiscal year 2010/11 is KShs.688.6 billion comprising of Kshs. 609.6 billion of ordinary revenue and Kshs.78.9 billion of Appropriations in Aid (including LATF). Compared to the Budget Policy Statement; this represents an increase of Kshs. 59.3 billion shillings. ***One key observation is that there is a huge variation between the Budget Policy Statement (BPS) and the Budget speech*** especially as concern Appropriation in Aid. However, a further analysis indicates part of the Kshs. 29.7 billion an amount comprising of Kshs.15 billion is A-I-A from universities which is not new or additional resources. It was a process of enhancing the comprehensiveness of the budget by including all sources of revenue.

18. Compared to the BPS, ordinary revenue rose by Kshs.29.6 billion. However, given the economic fundamentals, it is apparent that the revenue target of 24.9 percent of GDP is overly ambitious and it is unlikely to be met. Indeed, the **Minister did indicate that the revenue target for Financial Year 2009/10 will not be met and therefore the projections for 2010/11 ought to be revised downwards in order to accommodate this lower expectation**.

19. Overall, given that ordinary revenues and specifically tax revenue finance the largest share of the budget, it is of paramount important for the Ministry of Finance to provide details of revenue gain/loss resulting from Discretionary Tax Measures (DTMs). Indeed, from the budget speech 2010/11, a sizable amount of revenues will come from tax administrative measures. Coupled with the fact that ordinary revenue is expected to grow by 13.1% and nominal GDP is envisaged to grow at 11.8%. This calls for Treasury to provide details of expected revenue from tax administrative measures.

20. Concerning Total expenditure and net lending, the difference between the Budget Policy Statement and the Printed Estimates is Kshs.95.5 billion (an increase of 12%). This raises the issue whether the Budget Policy Statement served as a guide to the budget. Indeed, **the Budget Committee report on the Budget Policy Statement clearly indicated the preference to reduce overall expenditure in order to contain the deficit and eventually tame the domestic debt level.**

21. The projected deficit has increased by Kshs.36 billion from the BPS level of Kshs.192.3 billion. **It is important to note that the report that was tabled and adopted by the house on the BPS clearly indicated that the deficit should not exceed Kshs.192.3 billion yet it is now projected at Kshs.228.4 billion. On the other hand, the report indicated that the net domestic borrowing should not exceed Kshs.95.3 billion and it is now projected at Kshs.102.7 billion.**

22. Does the Financing numbers add up? The government adopted the GFS classification in 2005 and has been using it to produce the estimates of expenditure as well as the estimates of revenue. All these documents are expected to support the financial statement. As much as the Estimates of revenue are supposed to capture all finances it has been observed that at times it leaves out the resources collected in form of appropriations in aid in recurrent as was the case in the 2010/2011 revenue booklet. Below is a detailed analysis of financing the 2010/11 budget.

Category Source of revenue	**Amount in kshs.**
Ordinary Revenue	**609,639,337,937**
Appropriations in Aid (AIA)	**78,885,326,850**
Of Which: Recurrent	70,972,377,850
Development	7,912,949,000
LATF Adjustments	1,113,477,354
Total Revenue	**689,638,142,141**
Total Grants	40,362,617,981
Net Domestic Borrowing	105,288,904,052
Total	**835,289,664,174**
Loans	102,237,000,000
Domestic Debt Rollover	61,442,000,000
Grand Total	**998,968,664,174**

Notes:

i. The figure of **Kshs.609,639,337,937** in Ordinary Revenue is found in the Estimates of Revenue book and the details of the individual items.

ii. The figure of AIA amounting to Kshs.78,885,326,850 can be traced as follows:

a. AIA under Petroleum Development Levy Fund (PDL) of **Kshs.1,792,954,390**;Road Maintenance Levy (RML) of **Kshs.26,647,801,463** ; and Local Authorities Transfer Fund (LATF) of **Kshs.13,414,577,354** appear in the estimates of revenue under item 1140700,1140703, and 1110200, respectively. Thus, AIA totalling **Kshs.40,740,954,390** appear in the Estimates of Revenue book.

b. AIA in from of user charges collected and not part of estimates of revenue amounts to **Kshs.38,144,372,460.** This is available in the 2010/2011 estimates of recurrent and development expenditure.

iii. To get pure recurrent AIA of Kshs.36.024 billion, you take total AIA of Kshs.70,972,377,850 appearing in the summary of expenditure books less Road

Maintenance Levy of Kshs.22.648 billion (Kenya Roads Board) and LATF of Kshs.12.3 billion (Ministry of Local Government).

23. From the foregoing discussion it is apparent that the figures in the various budget documents balance and therefore the deficit therein is correct. **It is also important to note that** there are some anomalies (mathematical errors) in the Estimates of Revenue and Expenditure of State Corporations and experts from Parliamentary Budget Office have fully briefed the relevant departmental committees. The committees will deliberate on the issues raised and present a detailed report of the ministries as well parastatals under their watch to the House.

Highlights of salient tax measures

24. Taxation is a key aspect of any budget due to the fact that about 90% of the recourse requirements are raised in form of taxes. In the 2010/11 budget the Minister plans to raise a total of Kshs.688.6 billion in revenue. This consists of 609.64 billion (88.5%) ordinary revenue and Kshs.78.97 billion (11.45%) Appropriation-In-Aid, a 17.4% increase from kshs.586.3 billion in 2009/10. The fact that ordinary revenues/tax revenues account for close to 90% of expected revenues is fundamental and all efforts should have been made, through productive tax measures, to ensure that the revenues are successfully collected for implementation of the 2010/11 planned expenditures.

25. Despite the significant increase of 17% in targeted resource receipts requirements, there are no corresponding tax/revenue measures to ensure transformed revenue productivity. The pronouncements regarding tax measures are generally peripheral and only point to administrative initiatives to be undertaken by KRA. Indeed, available evidence shows that KRA is likely to miss its 2009/10 revenue target by not less than Kshs.10 billion. The administrative measures to be initiated by KRA include: introduction of automated valuation database system to strengthen the customs valuation, electronic cargo tracking system for effective monitoring of transit goods, integrated tax management system, and audit of forex bureaus.

26. Most of the proposed tax measures are in the category of import duties and are geared towards stimulating the manufacturing sector by reducing duties on some raw materials for iron and steel industry. Further, proposed reduction of duty on wheat and rice will further reduce taxes coupled with harming the local agricultural sector. On excise category, both malt and non malt beer have had their taxes increased with expectation that additional Kshs.2.5 billion will be raised.

Manufacturing

27. The manufacturing sector continues to play a pivotal role in Kenya's development. Direct formal employment in the manufacturing sector registered a growth of 0.5% from 264.1 thousand persons in 2008 to 265.3 thousand persons in 2009. However, the sector's contribution to the GDP growth has been consistently falling from a high of 10.5% in 2005 to 9.5% in 2009. In fact, the sector's growth has been reducing consistently from 6.3% in 2007 to 3.6% in 2008 and finally to 2.0% in 2009. This lackluster performance is of concern given that the sector has been identified as a key driver in the economy in the Vision 2030.

28. The challenges to the manufacturing sector include; high cost of production, competition from cheap imports, high taxes and low credit from financial institution and depressed demand for manufactured products. These challenges hamper the sector from realizing its full potential. The government therefore had the opportunity to come up with measures to facilitate improvement of demand and reduction of the challenges generally for the manufacturing. The minister attempted to institute some policies among them, scrapping import duties on certain inputs especially inputs of iron and steel industry. It is important to note that these measures, though welcome, fall short of the expectation in terms of rejuvenating this important sector. More robust tax incentives should have been considered to ensure that the manufacturing sector expands to create the needed jobs and improve output for domestic market and export.

IV. LINKING THE BUDGET TO THE NATIONAL STRATEGIC OBJECTIVES

29. The budget is the single most important means that is available to a country t*o deliver* its national agenda. The agenda for this country since the publication of the vision 2030 has been to transform Kenya into a globally competitive industrialized and prosperous country capable of providing high quality of life to all its citizens in a clean and secure environment. This agenda calls for a mechanism that ensures that available resources are shared equitably among competing needs, prioritized on the basis of how fast they can deliver the targeted results and outputs.

30. The various reforms in the budgeting process witnessed in the recent past were all aimed at making budgeting more transparent and participatory. The sectoral discussions were established with the aim of providing an opportunity to departments with similar output target to rationalize their needs. Moreover, the introduction of programme based budgeting was expected to guide decisions based on the expected outputs. Indeed, the Ministry of Finance has made efforts to mainstream programme budgeting by including programmes in the Budget Strategy Paper which are the same as were presented in Parliament in the Budget Policy Statement. However, other issues that Parliament approved when they were debating the report on the Budget Policy Statement were overlooked. For instance, the issue of linking outputs or performance indicators with resource allocation. Moving towards programme based budgeting should not be seen as a process of the willing but as a key strategy to achieve allocative efficiency where the basis of deciding what to finance is guided by expected outputs/results and in this way the credibility of the budget as a means to implement the national agenda shall be achieved.

31. Kenya has a potential to grow as envisioned in the Vision 2030 (above 5%) and as was witnessed in 2005-2007. However, these high growth rates will be attained only if there is a strategic move to re-orient expenditures to high priority areas through rationalization. In 2009/10 budget the Minister outlined several expenditures rationalization measures of which key was the provision of cars for senior Government officials. Kenyans did observe the withdrawal of the fuel guzzlers from use and expectations were high that the Minister would this year outline further measures. Although the Minister did not mention it in his budget speech a review of estimates of various Ministries and Departments indicates that there has been rationalization of provisions for foreign travel and training. However the rationale behind the provisions in the departments within the Ministry of Finance may not support the principal of rationalization of such expenditures. The increase in the development budget versus the recurrent budget is a positive move. However, there challenges with regard to absorption capacity of some of the sectors in particular infrastructure. In order to enhance absorption capacities there may need for the Treasury to come up with strategies and measures to ensure monies are not tied against Ministries that are not spending.

Where are the resources going?

32. The table below is an analysis and comparison in the allocation of resources according to the sectors. Bulk of resources went to Human resources where the Ministry of Education took the lion share followed closely by the Physical Infrastructure which accounted for 18% of total resources compared to last year where it accounted for 17%.

A SUMMARY OF THE ESTIMATES BY SECTOR IN PERCENTAGE				
	2009/10		**2010/11**	
Details of Vote	**Approved Gross Estimates**	**% Share of Total**	**Gross Estimates**	**% Share of Total**
Agriculture and Rural Development	30,243.43	3.41%	35,779.85	3.59%
Trade, Tourism and Industry	11,963.00	1.35%	11,531.80	1.16%
Physical Infrastcture	151,196.50	17.05%	182,127.57	18.27%
Environment, Water and Irrigation	39,321.70	4.43%	52,695.44	5.29%
Human Resource Development	177,544.32	20.02%	198,558.60	19.92%
Research, Innovation and Technology	62,684.46	7.07%	83,656.07	8.39%
Governance, Justice, Law & Order	81,837.91	9.23%	81,886.47	8.21%
Public Administration	45,139.55	5.09%	67,218.31	6.74%
Special Programmes	37,665.31	4.25%	37,801.72	3.79%
National Security	58,644.12	6.61%	57,835.68	5.80%
TOTAL Discretionary Expenditure	696,240.29	78.49%	809,091.50	81.17%
CONSOLIDATED FUND SERVICES	**190,777.55**	**21.51%**	**187,733.51**	**18.83%**
TOTAL EXPENDITURE OUTLAYS	**887,017.84**	**100.00%**	**996,825.02**	**100.00%**

Food Security

33. The importance of food security for any country is given greater impetus by the Millennium Development Goals 1 (MDG 1) which targets eradication of extreme poverty and hunger. Currently, anecdotal evidence show that Kenya is not well prepared to deal with climate change that will impact heavily on farm productivity and hence food security. Recent events occasioned by bumper harvest in traditionally food deficit regions exposed enormous under investment in these areas especially the post harvest handling and infrastructure development in the Agriculture and Rural Development (ARD) Sector.

34. Food security in Kenya and most of sub-Sahara Africa is increasingly coming under threat if new farming methods and diversified farm enterprises are not embraced. Incidentally, food security in Kenya has always been synonymous to maize availability which is the most widely grown staple crop. However, majority of the rural population is under increasing threat of malnutrition due to high rates of protein deficiency. Food insecurity breeds apathy among the food insecure populace and has a significant impact on productivity by the country's human capital.

35. Heavy reliance on rain fed Agriculture in Kenya is no longer sustainable as extraneous factors among them climate change and variability has disrupted weather patterns ultimately compromising food security. It becomes imperative that policy response to address this inherent lacuna is necessary focusing on particular targeted investments in the following critical areas:

- Value addition through development of cottage industries taking into consideration the areas of comparative advantage in terms of specific enterprises by region;
- Developing adequate storage capacity and post harvest management;
- Address cost build-up along the supply and production chain, and especially transport infrastructure to markets;
- Targeted policy and legislative coherence – including harmonization of legislation governing the sector to ensure coordinated approach to food security and related projects implementation;
- Pursue food policy implementation programmes to their logical completion – past efforts have often been abandoned midway leading loss of focus and traction; and
- Institute measures that ensure farmer participation in price determination.

36. A positive austerity measure under the 2009/2010 budgetary allocation and which has proved successful in improving food security is the Economic Stimulus Package (ESP). The food component of the ESP was meant to increase food security through rehabilitation of irrigation schemes and hence stabilize the country's Strategic Grain Reserves (SGR). It also seeks to improve the availability of maize and rice to Kenyans while contributing to improved nutrition and health. Ministries targeted under this component – Agriculture; Water and Irrigation; Regional Development Authorities; Youth Affairs and Sports. The first phase focused on rehabilitation of irrigation infrastructure and optimization of crop production in the existing public irrigation schemes. Whether this is long term government undertaking or not depends on future allocations and releases towards the food component.

37. Food security did receive adequate emphasis in the 2010/2011 budget speech. However, this has not addressed the recent upward review of the SGR which would serve as an avenue for improved food security. There appears to be a premature relief on the part of the government seen against allocation for national food security under the Ministry of State for Special Programmes has been reduced by 38.82 per cent - from Kshs.3.74 billion in 2009/10 FY to Kshs.2.31billion in 2010/2011 FY. It would however be more appropriate to channel this allocation through the productive sectors to cater for food security programmes and not entirely relief services.

38. Government efforts to diversify into non-traditional food items such as fish farming are likely to boost the national food security as communities embrace new and diversified dietary habits. Additional allocations to the food component under the ESP as reflected in the 2010/2011 FY add more impetus to the promising first phase.

Public Sector Reform

39. The public sector wage bill and the pension bill are always on the increase and as at the current financial year it stands at 2.68 % of the total expenditure. The government has moved the retirement age from 55 to 60 years. This occurrence in the medium term has led to no growth of the pension bill but in the future it will result in higher expenditures. This calls for the need to operationalise the contributory pension scheme in the civil service.

40. With regard to policy reforms targeting a reduction of the number of ministry or capping them at a definite number need to be fronted. The effects of such a policy would see the causal effects of a reduced wage bill stemming from a decrease in the number staffers drawing salaries from the exchequer.

Institutional and Governance Reforms

41. Institutional and governance reforms have been acknowledged as fundamental to development. Carrying out logical institutional governance reforms has been linked to faster development as they unlock service delivery. One of the three pillars in the Vision 2030 document is the political pillar. This has been identified as the software that will transform the country into a modern, globally competitive middle income offering a high quality of life to all citizens. Several reforms have been highlighted as necessary in the wider sector of governance, justice, law and order sector. The document outlines several flagship programmes for the medium term, which include constitutional reform, national cohesion, handling post election trauma among others. There are a number of specific recommendations the government is proposing in addition to Agenda 4 reforms. In the judiciary, there is a report of task force recommending issues such as establishment of a small claims court and the judicial service commission. In his budget, the Minister did make a scanty mention of strengthening governance reforms which only specified allocation of funds for civic education. It is necessary to emphasize that for these reforms to take effect in implementation to have effect the strategies have to be in place depicting the institutional framework for delivery. Parliament needs to take the Minister to task to demonstrate commitment to reforms by a clear policy proclamation on institutional reform.

42. In the first medium term plan of the Vision 2030, implementation policy framework of Agenda has been focused in as to receive prioritized allocation of 83.3 billion equivalent to 12.4% of total expenditure. Importantly, Members of Parliament need to be on the look out to ensure that this key sector not only realizes the allocations but track the institutional reform measures so as to ensure they are carried out effectively and efficiently to the desired results.

43. A World Bank report identifies an index that tracks progress on governance reforms. The aggregate governance indicators included in this index are fundamental ingredients to competitiveness. These indicators are; social and political stability, efficiency and predictability of the legal system, sound macroeconomic framework, efficient regulatory framework, efficient government services, and especially improved infrastructure.

44. The broad key reform areas in governance are the rule of law; electoral and political process; democracy, participation, transparency and accountability. The specific in each of these broad thematic areas and budgetary allocations are outlined in a later chapter. Another important aspect of economic governance closely related to transparency and accountability is the reform in the public financial management system. These set of reforms will go a long way in ensuring delivery of services, sealing of leakages as funds flow to grassroots, as well as accountability of the utilization of public resources.

Security Reforms

45. The concept of Security Sector Reform (SSR) was introduced in the 1990s to address the challenges of weak and badly governed security sectors, incapable of providing a basic level of security for their citizens, or in frequent violation of international norms on human rights. Actors in the security sector include the military, police, intelligence services, government bodies that monitor such organizations and those institutions charged with upholding the rule of law, including the judiciary and the penal system. Reforms in the security sector are aimed at offering an innovative approach to the reform of security governance. These reforms are seen as an essential precondition of sustainable development and are envisaged as encompassing the entire spectrum of security institutions, including the military, police, intelligence services and the penal system. Another perspective of reforms in the security sector is the approach and that lays emphasis on local ownership of the reform process; on principles of legality, accountability, and transparency; and on its embrace of a wide understanding of security, encompassing territorial integrity, state security, and individual security.

46. The vision for the security section in a “society free from danger and fear” and security of individuals and of property. Security is vital in achieving and sustaining economic growth and attracting investment both from within and outside the country. While funding to the Provincial Administration and Internal Security has had a slight increase targeted at covering investments in operations and maintenance communication, crime proofing, intelligence analysis and lack of a National Security policy remains a drawback in this sector. Outlined below are the key components and flagship programmes in security reforms;

- Phasing out of Police Prosecutors.
- Establishment of an independent Investigative Agency.
- Independence, political neutrality and national image of the Police Force(s).
- Establishment of a police service commission
- Police accountability and transparency.
- Police skills, capacities and professional competencies

Disaster Management

47. Kenya like many regions of the world continue to experience Hydro meteorological hazards like droughts, floods and man-made disasters like collapse of buildings with greater impact in terms of lives lost and livelihoods. Climate change owing to environmental degradation threatens to heighten these impacts by changing the frequency and/or intensity of extreme events and by bringing changes in conditions that may alter the underlying vulnerability of populations to hazards. These have threatened the sustainability of development processes and undermined progress toward poverty reduction.

48. Holistic management of disaster risk requires action to reduce impacts of extreme events before, during and after they occur. More to this is the technical preventive measures and aspects of socio-economic development designed to reduce human vulnerability to hazards. Approaches toward the management of climate change impacts also have to consider the reduction of human vulnerability under the ever changing levels of risk.

49. A key challenge and opportunity therefore lies in building a bridge between current and emerging disaster risk management efforts aimed at reducing vulnerabilities to extreme events and efforts to promote climate change adaptation. There is a need to understand better the extent to which current disaster management practices reflect future adaptation needs and assess what changes may be required if such practices are to address future risks.

50. Overall, there is need to strengthen preventive measures aimed at reducing loss of human lives, and loss of economic and environmental assets of communities through the following key interventions:

a) Climate risk and vulnerability information and assessment;
b) Institutional capacity and coordination both at national and community levels; and
c) Financing of disaster risk reduction and adaptation to climate change.

51. The budget affirmed climate change as a key challenge in economic development with the former being seen to increase vulnerability to disaster risks especially floods and droughts. In line with the budget 2010 theme "**towards inclusive and sustainable rapid economic growth"** the budget focused on livelihood rehabilitation of communities through development at grassroots level, rural areas and ASALs. However, the lack of a proper disaster management policy coupled with low investment in early warning systems and technologies means that we are not fully prepared for disasters and it therefore means we shall continue to act at the spur of the moment.

Tourism

52. Tourism is one of the six priority sectors that promise to raise GDP growth rate to 10% in tandem with Vision 2030. It is recognized as one of the sectors that make up the bulk of Kenya's GDP (57percent). In addition, it is a sector that is supported by other major sectors such as energy, telecommunications transport, and security. Vision 2030 identified the following areas as the opportunities and challenges to exploit in ensuring growth in the tourism sector for the realization of the vision goals;

a) Diversification of product and quality improvement,
b) Improving infrastructure including enabling sectors,
c) Marketing Kenya and improvement of security, and
d) Offering leadership and coordination in the sector.

53. The key economic and social indicators show that tourism earnings have recovered after a slump in mid 2008. The sector's performance indicators points to an impressive recovery in 2009, with a growth of 42.8%, the highest recorded by any sector in a decade considering its negative growth during the previous year.

Gross Domestic Product by Activity, 2005 – 2009 (Prices in Kshs)

Industry	**2005**	**2006**	**207**	**2008**	**2009**
Hotel and restaurant	19,357	24,207	29,612	23,745	39,421
% contribution to GDP	1.4	1.5	1.6	1.1	1.7
Growth rates of GDP	13.3	14.9	16.3	-36.1	42.8

Source: KNBS, Economic survey 2010

The above positive trends are attributed to:

a) Improved quality and volume of tourists owing to improved security,

b) Successful tourism promotion both locally and internationally, and

c) Political stability.

54. The role of Tourism sector in achievement of Vision 2030 cannot be over-emphasised. In the Budget speech, the Minister mentioned increased allocation to some sectors that are intended to argument the growth of tourism. Among them is the increase in allocation in the roads subsector, security, as well as improving the regulatory framework to support private sector led growth. Despite the positive move, the Minister did not address sector specific issues that affect the industry. One among them is the issue of domestic tourism and the need to develop human resources, particularly indigenous personnel, both for reasons of delivering quality services for tourists, as well as enhancing general skills of the local workforce. Achieving these broad objectives will potentially encourage sound utilization of local suppliers.

Agriculture and Rural Development

55. The Agriculture and Rural Development (ARD) sector still remains a major player in Kenya's future economic progress. Incentives to this sector must aim at stimulating and sustaining growth. Specifically, the share of overall budget allocated to the agriculture sector must be 10 per cent in line with the Maputo Declaration. Nonetheless, budget effectiveness is determined by its execution/implementation in line with sectoral policies. It is therefore imperative that budgetary allocations and implementation mechanisms are aligned to the ARD sector working group policy proposals.

Crop production

56. One of the most affected sectors of the economy in terms of policy and legislative obstacles is the agriculture sector. The importance of this sector to the realization of national food security may not be overemphasized. Majority of Kenyans live in rural areas and derive their livelihood from agriculture related activities, making agriculture a key economic driver for the country. The Strategy for Revitalizing Agriculture (SRA) 2004-2014 outlines the key policy goals as follows:

- Raising agricultural productivity through increased resource allocations;
- Exploiting irrigation potential;
- Commercializing agriculture;
- Reviewing comprehensively legal and policy framework for agriculture; and
- Improving governance in key agriculture institutions, especially cooperatives and farmer organizations.

57. The challenges currently facing crop production include: stagnation of agricultural productivity; over-reliance on rain fed agriculture; limited specialization and value addition; poor and inadequate marketing infrastructure; high prices of inputs; land subdivision and lack of a comprehensive lands use policy cultural inhibitions; limited ability to absorb allocated sector budgets; and recurrent drought conditions.

58. Low budgetary allocations and prioritization have not favoured agricultural sector growth and its contribution to GDP is declining further undermining the rural economy. The average allocation to the ARD sector for the period 2002/2003 to 2008/2009 is 4.3 per cent of the total national budget (KIPPRA 2009). This falls short of the 10 per cent of government budget recommended under the Maputo Declaration.

59. It is difficult to have effective anti-poverty interventions without giving due attention to agriculture and rural sector development. Clear budget policy on the rural economy is the most basic step towards this endeavor. Among the key incentives in this area include; revitalization of the government, extension services to train small scale farmers; value addition; post harvest handling and storage, government subsidies on agricultural inputs, accelerated irrigation infrastructure development, support for commercialization of agriculture, ongoing privatization programme – especially for government owned sugar factories; addressing effects of climate change, credit availability, and ways of addressing the market distortion.

60. Among the incentives to spur growth in the crop production sub sector is the provision of funds to employ 6 extension officers per constituency under contractual terms. This is unlikely to spur productivity as contractual engagement of technical staff in other sectors has faced resistance. Allocation of funding for purchase of driers to reduce post harvest loses is reactionary since it does not address the underlying inadequate storage capacity in the country both at farmer level and the national grain handler – the National Cereals and Produce Board (NCPB). Additionally, infestation by pests and related preservation inputs prices have not been catered for.

61. Recent events in the maize sub-sector, for instance, have highlighted the fact that the sector is yet to benefit from the full liberalization. Market liberalization has so far failed to realize the intended goal of streamlining the cereal sub-sector with the entrance of private players further exposing the farmers to more risk and uncertainty. The free market forces of demand and supply have been distorted by exploitative middlemen of marketing.

62. The introduction of warehouse receipting is a major step forward in hedging and future commodity trading which is long overdue for a country whose economy is agro-based. This would require deepening investment on post harvest pest control for the sub-sector to reap the full benefits. Its implementation needs to be fast tracked to reign on the price distortions that are common phenomena after harvesting and devoid of rational market forces.

63. The momentum build by the ESP has been stepped up and more funds allocated to the food component. This allays the fear that programmes tend to be abandoned midway leading to loss of focus and traction. Food security can be achieved not only through production of food crops but also by offering incentives to other sub sectors. Industrial crops sub-sector has received inadequate attention in the 2010/2011 FY budget. The long awaited privatization of the sugar industry is still pending and local production of the commodity remains uncompetitive.

64. The agriculture sector is in dire need of urgent effective and speedy transition to command a meaningful presence in a liberal market economy. Agricultural produce marketing systems are underdeveloped and unable to remain competitive in the face of regional trade conventions and commitments, including WTO, COMESA, and the EAC. The budget is silent on ways to stimulate marketing under such regimes.

Livestock

65. Livestock production is one of the major activities in the sector practiced in all parts of the country either under the extensive pastoral system in the Arid and Semi Arid Areas (ASALs) or under intensive, ranching and smallholder systems. The pastoral and commercial ranch systems traditionally contribute to the supply of beef and small stock meat. Livestock production in the ASAL accounts for nearly 90% of the employment opportunities and nearly 95% of the family incomes. It also accounts for about 40% of the Agricultural GDP and about 30% of the farm gate value for agricultural commodities.

66. In the high rainfall areas of the country, dairy production is a key source of income to over 600,000 households. Production of sheep, goats and poultry was also promoted with the aim of reducing poverty. Dairy production has been impressive since 2003 indicated by an increase in milk production. The milk intake by processors has also increased due to increased processing capacity. A trickle-down effect has been experienced by dairy farmers through increased prices of milk delivered. Over the same period, export destinations have been diversified to cover the neighboring countries among them; Tanzania, Uganda, Rwanda, Burundi, Democratic Republic of Congo, Sudan and Ethiopia.

67. The resurgence of the dairy industry has boosted the other related and complementing areas like animal feeds, veterinary drugs, and packaging materials. The rehabilitation of the Kenya Meat Commission (KMC) and procurement of livestock from farmers has further seen a rise in beef production and marketing. This ready market is likely to boost production in the arid areas as livestock keepers are assured of a ready market.

68. Major constrains in the sub-sector include: Livestock Diseases outbreaks; recurring drought; insecurity and rustling. A number of incentives and development interventions in livestock keeping areas need to be enhanced, among them: livestock branding; creation/establishment of disease free zones; vaccination and disease control measures; establishment of modern satellite abattoirs and slaughter houses to ease marketing problems.

69. Among the highlights of the 2010/2011 FY budget to address the constraints in the sector is the substantial allocation towards dam construction to mitigate the adverse effects of drought in the ASAL areas. The staggered nature of allocations (across implementing government ministries/departments) for this purpose will complicate the implementation for lack of coordination. Further, electronic tagging will complement the traditional branding method to curb cattle rustling.

70. Livestock markets and particularly the export market need to be backed by a livestock upgrading programme in the ASAL areas. This has been largely overlooked in subsequent national budgets. Currently, livestock off-take is hampered by a poorly functioning marketing system with prices determined by middlemen in addition to lack of modern slaughter houses and storage facilities. The generous allocation to construct slaughter houses and mini ASAL areas and for establishment of leather processing factories is an attempt to address the livestock and allied product marketing gaps.

71. Government efforts to create disease free zones for beef destined for the export market is commendable. It is however misleading to provide for 100 additional veterinary officers who are far too few given the huge demand in the sub-sector. Equally, this number is inadequate to provide the stated 20 veterinary officers for even the a third of the ASAL districts.

Fisheries

72. The fishing industry in Kenya consists largely of capture fisheries in the internal and shared water masses in the country. Although fishing is small relative to GDP accounting for less than 1 percent, it generates substantial income to the people involved in it. Fish farming or aquaculture is on a very small scale despite the immense economic potential and transformation it portends. Majority of the rural population is under increasing threat of malnutrition due to high rates of protein deficiency.

73. Aquaculture has recently received the desired attention by the government after a prolonged low uptake of the technology. The 2009/10 FY budget mainstreamed fish farming by factoring Kshs.1.12 billion towards the construction of 200 fish-farming ponds covering 140 constituencies countrywide under the Economic Stimulus Package (ESP). An additional Kshs.120 million to construct a further 200 fish ponds in 20 more constituencies not covered in phase one.

74. Fish farming as a tool of economic development in Kenya is still limited by: lack of capital; low literacy levels that hamper technology transfer; predation and fish diseases; Cultural-related constraints; entrenched capture fisheries in fresh water masses; and lack of proper policy on aquaculture.

75. The case for sustained investment in aquaculture could be explained by unprecedented decline resulting from over-fishing and loss of biodiversity or ecological perturbation in the traditional fishery resources of Lake Victoria, lake Naivasha, Lake Turkana, Lake Baringo and other water masses. The associated processing and distribution activities form an important part of the regions' economy leading to over exploitation of fish resources through use of destructive fishing technology.

76. Despite the proposal in the 2010/2011FY budget to shift government role in fish farming to a facilitative function, it is not clear how the government intends to bring in the private sector, as no incentives have been extended to ensure their participation. The huge allocation towards production of fish seeds and fish feeds (Kshs.340 million and Kshs.1.2 billion respectively) may not be sustainable in the longer term and new approach to this must immediately be explored. With the heavy investment in production, processing and storage of fish, a lot more needs to be done on the marketing front. This is where the private sector has a vital role.

2010/11 FY Allocations by Sub-Sector

Vote	Sub-sector	Gross Recurrent Estimates		Gross Development Estimates	
		Recurrent	Recurrent		
		2010/11	**2009/10**	**2010/11**	**2009/10**
R09	Regional Development Authorities	818,77,470	820,142,800	7,482,433,130	4,306,007,305
R10	Agriculture	8,187,640,610	8,096,820,022	10,774,927,058	8,091,882,141
R19	Livestock Development	3,581,770,900	4,714,522,150	3,189,551,552	1,727,473,303
R22	Cooperatives Development and Marketing	991,460,520	951,426,690	171,540,000	186,200,000
R55	Forestry & Wildlife	4,794,908,000	4,285,643,500	2,874,055,420	2,691,804,225
R56	Fisheries Development	1,097,091,100	1,325,411,500	3,225,900,400	1,281,752,175
	TOTAL	**18,652,871,130**	**20,193,966,662**	**27,718,407,560**	**18,285,119,149**

Physical infrastructure

77. Infrastructure is one of the essential drivers of growth and overall development of the country. In fact, the minister, in his budget speech, recognized that the projected growth of 4.5% and 5.7% in 2010 and 2011 respectively will be driven mainly by increased investments in key sectors like infrastructure. A well developed infrastructure network has the potential to reduce the distance between regions resulting in integrated national market.

78. Vision 2030 envisions elevation of efficiency and quality of infrastructure that will deliver the anticipated growth and positions the country to be globally competitive and prosperous. The document has outlined certain policy reforms expected to achieve the foretasted physical infrastructure. The National Integrated Transport Plan (NITP); a legal framework to support Public Private Partnerships (PPPs); and Comprehensive Construction Industry Development Policy are such policies that have lapsed their target of being in place within two years of the Vision 2030 implementation period. It is important to note that the Minister allocated Kshs.50 million towards public private partnership secretariat under the Ministry of Finance. The question to pose is the effectiveness of the unit despite the lack of statutory establishment which should guide the whole process of Public Private Partnership (PPP). An increment in budget allocation towards infrastructure projects this financial year is welcome but more strategic measures are needed especially to enhance the absorption capacity which has been an on-going challenge.

i) Transport

79. Efficient transport is key to the development of any economy. It is essential in facilitating the delivery of goods and produce to markets by farmers and entrepreneurs in a timely and efficient manner. It also ensures convenience and affordability in movement of people. According to the 2010 Economic Survey, transport and storage grew by 4% in 2009 from 0.1% in 2008 attributed to the effects of post election violence. However, its contribution to the 2009 GDP growth went down to 7% from 7.6% in 2008. The sector however continues to reel under a number of challenges including lack of an integrated transport management policy to streamline the sector.

The current trend on Road Passenger Transport in Kenya

- Mass Transport - on the decline
- Buses - on the decline
- Matatus - on the rise
- Motor Cycles - on the increase
- Car Ownership - on increase
- Boda Boda – On the increase
- Walking - on the increase

80. The motor vehicle registration has been on the rise growing by about 40,000 vehicles per year, for example it grew from 121,831 in 2008 to 161,813 vehicles in 2009.This trend is of concern as it greatly contributes to the current congestion and traffic jam particularly in Nairobi and Mombasa. Much as the minister mentioned plans to deal with traffic jams there is deliberate strategy to deal with road traffic jams. The concern is whether there exists a political good will to promote Mass Transport which could substantially address traffic jams. The specific issues the budget needed to address include: Policy on vehicle importation, directed policies to tame increased road carnage, addressing existing pumping constraints of the pipeline, Mombasa port congestion and inadequacy of rail transport.

81. Road accidents have been on the increase since 2009, with 12,369 accidents compared with 9,093 in 2008. Even though the issue of road accident continues to take a huge toll on Kenyans through deaths and serious injuries, the minister mentioned no measures to address these accidents in the sub-sector. The minister however scrapped PSV license for drivers and conductors to enable more youth to access this document with ease.

82. The Railway sub-sector is important in providing freight to the local business as well as across the borders to Uganda, for example, unfortunately, its capacity has been on the decline with only 1.8m tonnage transported in 2008 reducing further to 1.4 million in 2009. This is mainly due to poor rail infrastructure and obsolete equipment. The Minister of Finance, in his 2009 budget speech provided Kshs.600 million for use in upgrading key commuter backbone railway lines in Nairobi. He further allocated Kshs.1.9 billion in 2010/11 budget towards the same project. The concern is whether the allocation would be adequate and how the projects would be fast tracked.

83. The issue of Mombasa Port is also important for efficiency in transport sub-sector. According to the 2010 Economic Survey (2010), the Port of Mombasa expanded its handling capacity by 16.1% from 16,415 tones in 2008 to 19,062 tonnes in 2009. The Minister also recognized that the inefficient port services has hindered Kenya's economy from exploiting its full potential. He spelt out that a Single Window Port Community based system will be pursued to facilitate effectiveness of the port. However, a closer look at the budget estimate books shows no budgetary allocation towards the same. How then will this be achieved without any budgetary provision?

84. Pipeline transportation increased capacity to 4,323.7 thousand cubic metres in 2009 from 3,848.6 thousand cubic metres in 2008 (growth of 12.3%). This capacity expansion should be enhanced to reduce the oil transportation by road which is a source of road accidents and deaths. Existing pumping capacity constraints should also be addressed. Overall, the total budget allocation to Transport Ministry increased by 26% from kshs.9.2 billion in 2009 to kshs.11.6 billion in 2010.

ii) Roads

85. Well maintained roads are important in unlocking the economic potential of any economy. The minister acknowledged this and subsequently allocated kshs.78.6 billion to roads development budget from kshs.58.5 billion in 2009/10(34% increase). The total allocation to the Ministry of roads stands at to kshs.104 billion in 2010/11 from kshs.80.3 in 2009, 78.6 billion being development from 58.5billion in 2009/10. Roads maintenance has specifically been allocated kshs.23.5 billion. Kenyans should hope that this will in effect translate the well maintained roads networks throughout the country.

86. Despite the enhanced resources allocation to the sub-sector, the issue of concern in the whole infrastructure sector and particularly roads sub-sector is absorption capacity constraints. Indeed, the minister acknowledged that this continues to be a major setback despite government attempts to improve it. There was however no strategic measures spelt out to deal with it except for the requirement that all accounting officers commit in their performance contracts for 2010/11 to improve the absorption rates to 90% and 80% for domestic and foreign financed development projects through development of time lined and benchmarked action plans for all projects.

iii) Energy

87. Provision of adequate secure, low cost and clean energy to meet the demand arising from the expanded production and economic activities should be the medium-term strategy of the government. The minister acknowledged that there is need to provide a predictable energy framework that enables local manufacturers to plan forward. despite the Government efforts to partner with private sector and other stakeholders, no formal legal framework (PPP) exists. This therefore frustrates the need for urgent containment of volatility in the cost of energy.

88. Some key challenges facing the sub-sector include: fluctuating cost of international oil prices (murban crude), constant sharp rise in power demand in the country, slow power development/generation capacity–thermal versus geothermal.

89. According to the Economic Survey (2010), power generation increased in 2009 to 39.7% for thermal and 24.5% for geothermal. More policies are needed towards promoting geothermal power to stabilize electricity prices and promote manufacturing. The resource allocation to the Ministry modestly increased to kshs.36.4 billion (Development-kshs.34.1billion and recurrent of kshs.2.3 billion) against kshs.33.1billion (development-kshs.33.1 billion and 0.5 billion recurrent) in 2009/10. However, the development allocation to Rural Electrification Authority decreased from kshs.7.9 billion in 2009/10 to kshs.5.43billion in 2010/11. This seems to contradict the government policy of expansion of electric power to rural areas through connection of additional customers with a view to opening up the rural areas.

iv) Public Works and Housing

90. The budget allocations for Public Works in 2010/11 increased to Kshs.6.5 billion from Kshs.5.6 billion in 2009/10. Similarly, the budget for housing increased from Kshs.2.97 billion in 2009/10 to Kshs.3.4 billion in 2010/11.

91. According to the 2010 Economic Survey (2010), the housing sector's contribution to the GDP reduced slightly from 5.2% in 2008 to 5.1% in 2009. The housing sector's growth also reduced from 3.7% in 2008 to 3.0% in 2009. Consumption of cement, a critical input in the construction industry, increased due to demand from on-going road constructions and CDF projects throughout the country. The scrapping of import duty on petroleum coke - a raw material for production of cement; intended to promote the construction industry by managing the input cost. However, it is important to note that the government might not be in a position to ensure that the cement manufacturers automatically pass on the benefit of reduced costs to the customers.

92. The challenges inherent in the housing sub-sector include: inadequacy of affordable and decent housing, low level of urban home-ownership, extensive and inappropriate dwelling units and persisting slums and squatter settlements. Much as the Minister of Finance did not specify policy measures targeting housing and public works, the ministries of Public Works and Housing respectively should strive to overcome the inherent challenges for the achievement of long term objectives of these key sub-sectors.

Environment, land, water and sanitation sector

93. Kenya is a water scarce country and the vision 2030 envisages access to clean water for all. The water sub-sector supports all the other sectors namely: manufacturing sector, services sector and the agricultural sector. In achievement of the aspirations as spelt out in the Vision 2030.There is need to move towards conservation of the existing water resources and diversification through harvesting of rain and underground water.

94. In addition, there is need for rehabilitation of hydro-meteorological data gathering and setting up of multipurpose dams (Rivers Nzoia and Nyando). Disposal of waste including the sewage is in dire need of intervention especially for the urban poor settlements and rural areas. The 2010/11 budget in addressing the issue of improving water access to all has increased the allocations to water services board that may go along way in improving the water and sanitation infrastructure. However, the challenge will be to ensure that there is adequate resources to maintain the infrastructure as well as ensuring that the resources collected from water users by the various water boards is applied efficiently and effectively.

95. In the recent past the area under irrigation has received a boost following targeted budgetary allocations through the ESP. However, Kenya's irrigation potential stands at 540,000 hectares but only 105,000 hectares is developed representing 19 per cent of the potential. Expansion of irrigable land is proposed to increase by an additional 4,500 hectares in the financial year 2010/11. The Minister for finance, in his budget speech, indicated the government's commitment to expand and diversify irrigation works through the Economic Stimulus Program in new areas like Challa in Taveta and Turkana among others. These are awaiting development of an execution framework expected to be completed by mid July 2010. In order to actualize on the irrigation works program, the Ministry of Finance needs to fast track the execution framework and also the disbursement of the funds for the program.

96. To develop Northern Kenya and other arid areas Ksh.3.8billion for expansion of water supply through dam construction was allocated for 2010/11. In addition, in order to enhance supply of water for crop irrigation and livestock, the minister for finance allocated Ksh.2 billion under Ministry of regional development for construction of about 25 medium size dams in arid parts of the country and additional ksh.375million allocations towards constructing mini-flood control dams and disilting of water pans in Northern Kenya.

Environment

97. By 2030 Kenya looks at becoming a nation with a clean, secure and sustainable environment pegged on environmental conservation, Pollution and waste management, enhanced disaster preparedness in all disaster prone areas and improved of capacity to tackle global climatic change.

98. The execution of the rehabilitation and restoration of Nairobi River under the Nairobi River basin programme is an example of a practical and sustainable measure in the management and conservation of our environment. In order to win the fight against environmental degradation law enforcement and raising environmental education awareness will need to be enhanced.

99. In addition, climate change has far reaching implications on sectors like agriculture, tourism, fishing and mining hence raising policy concerns. To coordinate the climate change issues the National Climate Change Response strategy has been developed. In the financial year 2010/11, there is an increased allocation to Ksh.128.7 million under the development vote to facilitate climate change activities. However, the under investment in early warning system is a concern and could impact negatively on the achievements made on conservation.

Lands

100. Land is the medium through which agricultural and economic activities are carried out. This calls for the introduction of land use policies for better utilization of high and medium potential lands. The fast tracking of the creation of the consolidated land registry and development of land use master plan are critical in unlocking the economic potential in the country. In light of this, the 2010/11 budget has recurrent provisions for computerization programme amounting to Ksh.230 million up from Ksh.9 million in 2009/10. Among the challenges experienced in the implementation of the land reforms include population pressure that leads to land fragmentation, unsustainable land use practices and land administration currently governed by many conflicting laws.

Sector allocations

	2009/10		2009/10	2010/11		2010/11
Ministry	**Rec (millions)**	**Dev(millions)**	**Totals**	**Rec (millions)**	**Dev (millions)**	**Totals**
Water	4,536	23,252	27,788	5,669	32,529	38,198
Environment	2,220	2,334	4,554	2,397	4,429	6,826
Lands	1,735	2,132	3,867	1,973	2,586	4,559
	8,491	**27,718**	**36,209**	**10,039**	**39,544**	**49,583**

Human Development Sector

101. The Kenya's long term planning document –The Vision 2030 recognizes that the country's main potential lies on its people. Indeed, the document identifies Human Resource Development as a key foundation for national socio-economic transformation. The education sector is one of the sectors that will contribute to the realization of the social pillar of Vision 2030 through transmission of skills and competencies necessary for effective participation in a knowledge based economy. Since 2003, the country has made considerable progress towards increasing the access of education and health services.

Table: Human Development Sector Resource allocations in millions (Kshs.)

SECTOR/ MINISTRY	2009/10(Kshs. Mln)	2010/11 (kshs.mln)
HEALTH		
1. **Medical Services**		
Recurrent	23,145.48	25,629.88
Development	4,460	6,953.87
Total Medical Services	27,605.48	32,583.75
2. Public Health		
Recurrent	7297	9594.28
Development	11,804.59	12,977.47
Total Public Health	**19101.59**	**22571.75**
TOTAL HEALTH SECTOR	**46,707.07**	**55,155.5**
3. Education		
Recurrent	117,284.60	131,479.76
Development	11,817.84	9,510.66
sub total education	**129,102.44**	**140,990.42**
4.**Higher Education**		
Recurrent	23,467.30	41,429.10
Development	3,747.66	7,804.23
Sub-total Higher Education	**27,214.96**	**49,233.33**
TOTAL EDUCATION SECTOR	**156317.4**	**190223.75**
TOTAL HDR SECTOR	**203,024.47**	**245,379.25**

Source: Estimate books, 2010

Education sector

102. The main education targets include: increasing primary net enrolment and completion rates to 100% by 2015; reducing regional drop-out and repetition rates and increasing primary to secondary transition levels to about 90% by 2012. Despite successes in education which include increased enrolment rates, the sector continues to face a number of challenges such as: enhancing access, participation, and provision of quality education at all levels; expansion of secondary education to cater for rising influx arising from Free Primary Education (PFE); finding sustainable options for financing education; reducing the unit cost and improving affordability of education; targeted support for marginalized groups. Others are setting up of centres of excellence; reduce regional disparities in primary school enrolment; access to post-primary level education and disparities in marginalized areas and adequately target students with special needs; address skewed distribution of both human and capital resources and the resultant under-utilization and overcrowding in some schools.

103. The Minister for Finance proposed several steps in 2010/11 to improve access and quality of education. These include allocation of more resources to support FPE and FSE; bridging the digital divide in the country and empowerment of children to actively participate in conservation of their environment in order to mitigate climate change variability. However, as much as efforts are being made to increase additional resources to free primary education there are issues on improvement of quality of education. The outflow from private schools to public schools witnessed when free primary education was introduced in 2003 seems to be taking a different route with parents preferring the private schools for primary education. Indeed, available statistics indicate that the bulk of students in National Secondary Schools are from private primary school - a trend that should be worrying the Ministry of Education.

104. In order to bridge the digital divide in the country through the education system, Kshs.1.3 billion has been allocated to purchase 300 computers in each constituency and make ICT a reality in rural schools. Even though this initiative may be better than the proposal in 2009 where the Ministry intended to implement the computer Bus Programme/project, it may not be feasible to implement due to lack of electricity connections in most rural areas. In this case, the Ministry should go ahead and budget for alternative power sources including solar and generators. Issues of running costs in terms of repairs and maintenance should also be considered.

105. In order to introduce pupils to environmental conservation at an early stage, the minister allocated funds for the establishment of tree nurseries in schools. This initiative has been further supported by allocating Kshs.30,000 each for 50 schools in every constituency towards the purchase of seedlings to empower children to actively participate in conservation of their environment in order to mitigate climate change variability. Even though this initiative is welcome, difficulties in choosing the schools to benefit might arise leading to skewed considerations. Further, the rigid and congested school curriculum may make it difficult to get the pupils to find time to engage in such activities. Couldn't it have been better to channel this towards *'Kazi Kwa Vijana' programme?*

106. In line with Vision 2030, the government planned to integrate the early childhood development and education into the primary education and as such, enrolment and number of teachers in Early Childhood Development (ECD) increased. The pre-primary enrolment rose from 1.7 million in 2008 to 1.9 million in 2009. Similarly the number of teachers increased significantly by 18.8% from 78,230 in 2008 to 92,955 in 2009. The number of ECD trained teachers increased by 23.5 % from 57,976 in 2008 to 71,580 in 2009. This was attributed to increased ECD teacher training colleges. This item has been allocated funds totalling Kshs.52 million up from Kshs.51 million funds for development for the 2009/10 and 2010/11 financial years respectively.

107. As the economy expands, demand for professionals and technicians in firms increases. An educated and trained labor force is able to adapt and utilize new technologies in the production of goods and services. The ratio of technologists to technicians to artisans in Kenya of 1:3:15 as at 2003[3]. Such an imbalance of professionals in the labor force affects negatively efficiency, research and development, which are crucial elements in firm productivity and competitiveness.

108. Generally although the expenditure in education has been rising over the years, basic education continues to receive a bigger portion of the total allocation for education sector. Though, the percentage of total funds allocated to the Higher Education Science and Technology increased from 17.41 % (27,214.96 million) in the 2009/10 FY to 25.88% (49,233.33 million) in the 2010/11 FY, the increment is to among other things cover salary increment offered to the academic staff. Though there has been a considerable improvement in the student enrolment in tertiary education and training institutions, enrollment has been significantly higher in Arts related courses. There is therefore need to allocate more resources to technical and other tertiary levels to be able to reap from the growth potential of productive sectors.

109. Although there has been an improvement in the education performance in recent years, Kenya still ranks poorly in basic and advanced human capital compared to other countries it aspires to emulate. On basic human capital, it ranks ahead of South Africa but lags behind Korea, Malaysia, Mauritius and Indonesia.

Health Sector

110. **Health sector is one of the key components in addressing equity under the social pillar in vision 2030.** In the 2010/11 FY budget speech; the Minister for Finance underscored the importance of the health sector in attaining the high levels of growth and accelerating private sector investment. The health sector is one of the key sectors expected to drive the economy to the projected 5.1% economic growth.

111. Kenya being a signatory to Abuja declaration is expected to spend at least 15% of the national budget on health expenditure. The total resources allocated to expenditure on health increased from Kshs.46,707.07 million in 2009/10 FY to Kshs.55,155.5 million in the 2010/11 FY which accounts for 5.38% and 5.53% of the total budget for the 2009/10 and 2010/11 FYs respectively. This is still far below the recommended allocation. Nevertheless, the allocations for development and recurrent increased for both ministries in this sector. In consideration to challenges faced by Kenyans the

[3] There is no currently available data

2009/10 budget, earmarked funds for expansion of health care facilities, recruitment of nurses and provision of medical kits in each constituency were factored under the Economic Stimulus Program. **In the 2010/11 FY an additional Kshs.1 billion has been allocated for recruitment of 15 additional nurses and 5 public health technicians in each constituency.** Overall, the **development expenditure on promotive and preventive health increased from** Kshs.1.89 billion to Kshs.2.74 billion. This hopefully will address the regional imbalances in the distribution of health personnel, but more needs to be done with regard to marginalized areas. There are concerns on whether the employment of nurses through allocations in the development budget is being considered under recurrent for future sustainability.

112. **To further enhance the coverage of preventive healthcare in the rural areas, Kshs.265 million has been allocated towards the purchase of additional motorcycles, operations and maintenance expenses, employment of 10 health community workers and provision of medical supplies in each constituency.** Consequently, the increase in budget allocation for acquisition of additional tools and equipment required by health workers serves to improve their working environment service delivery.

113. In the 2009/10 FY funds were provided for the construction and equipping of a maternal and child care ward in every constituency and the construction of these facilities is ongoing. In the FY 2010/11, a total of Kshs.5 million for each constituency toward expanding health care facilities to include wards for children and adults. Similarly to ensure that critical patients receive timely medical attention throughout the country, 300 ambulances have been provided for in the 2010/11 budget for use in the healthcare facilities.

114. High population growth rate and its implication on socio-economic sphere has been a major concern to the Government since independence. However, development allocation for the family planning maternal and child health dropped from 1.29 billion to 1.11 billion. This was to a large extent occasioned by a drop in the allocation for expenditure on specialised materials and supplies whose expenditure dropped from Kshs1.18 billion to Kshs.1 billion. The recurrent expenditure on specialised materials and supplies remained constant at Kshs.0.1 million.

115. Similarly, a total of Kshs.4.4 billion for the purchase of drugs for curative purposes and another Kshs.900 million for ARVS to make the important life savings drugs available in the health facilities. There was a deliberate move to strengthen the management of medical supplies chain through deepening reforms in the health sector including strengthening KEMSA's procurement capacity and accountability.

116. Though the Government financing of the health sector has been progressive over the years, the health sector still faces many challenges. The 2010/11 FY budget has not adequately addressed the issue of operational autonomy to level 4 and 5 (district and provincial) hospitals and to establish functional referral systems at all levels aimed at decongesting the two national referral hospitals in Kenya.

V. APPENDICES

Appendix 1

Tax proposals and the implication in the economy

i) Customs Duties

<table>
<tr><th>No</th><th>Proposal</th><th>Implications</th></tr>
<tr><td>1</td><td>Lowering import duty on wheat grain from 35% to 10%</td><td rowspan="2">• Even though the measures are proposed for only 1 year, they are anti development and promotion of agriculture and rural development in Kenya.
• The minister should have put measures to fast track reforms in the rice and wheat sub-sector for increased production of these products locally. This would go a long way in creating more employment in the farms and enhancing the productivity in the country.</td></tr>
<tr><td>2</td><td>Lowering import duty on imported rice from 75% (or $200 per tone) to 35%</td></tr>
<tr><td>3</td><td>Exemption of parent stock for chicken breeding from import duty</td><td>• May be good news for local poultry farmers. However, the best strategy should have been that of promoting local production of the parent stock for chicken.</td></tr>
<tr><td>4</td><td>Increasing import duty on Aluminum Conductors and Cables products from 10% to 25%</td><td>• Making imported pieces expensive to discourage imports and increase the market for locally produced pieces as well as promoting local manufacturers.</td></tr>
<tr><td>5</td><td>Scrapping import duty on flat rolled products of iron or non alloy steel coated or plated with tin(inputs in the iron and steel industries)</td><td rowspan="2">• The measure is necessary to spur iron and steel which are important for construction industry</td></tr>
<tr><td>6</td><td>Scrapping import duty on flat rolled products of iron or non alloy steel which are used for the manufacture of filters and bottle tops.</td></tr>
</table>

7	Scrapping of import duty on petroleum coke; a raw material for production of cement	• The measures are good for promotion of construction sub-sector. The issue is whether the reduced cost will be passed on to the Kenyan consumers or not
8	Scrapping of import duty on prepared driers and pigments which are used for the manufacture of paints	
9	Granting duty remission on all inputs used in the manufacture of goods which are duty free	• The measures are good for promotion of competitiveness. However, the administration involved in the remission process may frustrate the realization of the intended benefit. Also, the determination of inputs for use to manufacture duty free goods could present another cause of dispute between the tax authority and the manufacturers.
10	Scrapping of import duty on lamps and bulbs using Light Emitting Diode (LED) technology	• The measure may enhancement the use of energy saving bulbs. But what mechanism will the government use to ensure that the reduced price is passed on to the consumers?

ii) Excise duties

No	Proposal	Implications
1	Increase in duty rate by 20.4% for malt beer from Kshs.54 per litre to Kshs.65; and non-malt beer by 22.2% from Ksh.45 per litre to Ksh.55 per litre. The goal being to raise additional Kshs.2.5 billion from beer.	• The immediate effect of this is that the brewers would increase the prices of their beer products to pass on the additional costs to the final consumers. • More Kenyans who cannot afford the increased cost of beer would fall down to the consumption of cheap alternatives including illegal illicit liquor like *'changaa'* among others. • The minister should have spelt out some intervention measures with the brewers to forestall any negative repercussions due to increased drinking of illicit liquor.

iii) Value Added Tax (VAT)

No	Proposal	Implications
1	VAT Amnesty on remittances prior to 2010	• Would encourage filing of returns by Kenyans in the Diaspora • The concern with this measure is whether it will not open flood gates for remittance of 'questionable' money into the country.
2	Reduction of withholding VAT from constructors by Ministry of Roads from 16% to 8%	• This measure will go a long way to enhance the cash flow of construction companies and could make construction works flow a bit faster. • However, it is not clear whether the reduced withholding tax of 8% will then be final or the balance of 8% will be accounted for by the construction companies themselves – and at what stage

iv) Income tax

No	Proposal	Implications
1	Allowing 100% deduction on capital expenditure incurred by farmers on farm works.	• This is a good policy measure and would promote investment in agriculture towards modernization and mechanization. • However, the measure would only be beneficial to large scale commercial farmers who have the capacity to undertake capital farm investments. The small scale farmers, who are the majority, are likely not to benefit.
2	Scrapping of PSV license for drivers and conductor	• The measure should go a long way to assisting the youth acquire the vital PSV license to work as driver and conductors. • It gives this group a tax break thus allowing them to escape the hassle of paying before being issued with the license. It should be hoped that the measure will ease the procedures of getting the license and that the arising tax savings would be used productively.
3	Amending the tax laws for online filing of tax returns	• The income tax law requires that all income earners, both corporate and individuals file annual returns of their income by 30th June every year. • The proposed e-filling is welcome measure but should be introduced gradually and possibly alongside the manual system so that the small scale income earners who may not have access to the online services are not discriminated against.
4	Extension of double tax treaty networks and operationalization of the same	• These are good measures which would promote investment climate in Kenya by shielding investors from any double taxation and enabling exchange of valuable tax information with treaty partners.

V) Miscellaneous taxes

<table>
<tr><th>No</th><th>Proposal</th><th>Implications</th></tr>
<tr><td></td><td></td><td></td></tr>
<tr><td>1</td><td>Reduction of penalty on stamp duty on instruments from 25% to 5% and capping the penalty to the principal amount of duty</td><td rowspan="3">These measures are welcome and would encourage compliance with stamp duty payments and reduce the payment burden.
The reduction is however is too little and may not translate in any meaningful benefit. The duty should have been scrapped altogether.</td></tr>
<tr><td>2</td><td>Reduction of stamp duty fees on mortgages, charges and debentures from 0.2% to 0.1%</td></tr>
<tr><td>3</td><td>Reduction of stamp duty penalty rate from 2% to 1% on outstanding land rent and capping it to the principal amount of land rent owed</td></tr>
<tr><td>4</td><td>Reduction of days pension schemes are allowed to determine and pay benefits upon a member's retirement from 60 to 30 days</td><td>A welcome measure that should ensure that retirees get their retirement package within a reasonable timeframe. It has been a historical problem that retirees take too long to access their retirement benefits.
The onus would now be on the minister for finance to ensure that the pension schemes comply with this requirement to reduce the agony of pensioners.</td></tr>
</table>

Appendix 2: Compliance to Fiscal Management Act, 2009

	Requirements	Status
1.	Sec. 7(1) provides that the Ministry lays the Budget policy statement not later than 21st March, each year.	The Minister prepared and laid before the National Assembly the Budget Policy Statement before 21st March 2010.
2.	Section 9(1) provides that the Ministry lays the Annual Estimates of revenue and expenditure for the succeeding financial year not later than 20th June 9 each year	The Minister laid the Annual Estimates of revenue and expenditure for the financial year 2010/2011 on 10th June 2010
3.	Section 9(2) provides that the annual estimates laid before the National Assembly under the provisions of sub-sec (1) shall be accompanied by a Treasury Report specifying measures taken by the Government to implement the audit recommendations made by the National Assembly in the previous year	Outstanding
4.	Section 12(1) provides that every public entity shall be required to prepare its budget and submit to its parent Ministry by the 28th February, each year (2) the approved budget by Treasury must be annexed to the annual estimates of expenditure and revenue listed before the National Assembly each year.	The Minister complied with the law and annexed budgets of public entities to the annual estimates laid on the table of the House on 10/6/2010
5.	Section 13(1) provides that within 21 days after end of each month, the Minister shall publish in the Gazette a statement of actual revenues collected by category and net exchequer issues by Ministry.	The Minister has consistently published in the Gazette a statement in actual revenues collected by category and exchequer as prescribed by law.
6.	Section 14(1) provides that the Minister shall, three months after the laying the budget before the National Assembly and every quarter thereafter, lay before the National Assembly, sequentially and cumulatively, a compliance report in such form and of such content as may be prescribed.	The Minister has complied and laid a compliance report every quarter though the report is not in the prescribed form.
7.	Section 15 provides that the first compliance report falling due before one hundred and eighty (180) days and one hundred and twenty (120) days to a general election shall be styled "The Pre-Election Fiscal Report" and shall.	N/A

Appendix 3: List of Contributors

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