REPUBLIC OF KENYA
THE NATIONAL TREASURY & PLANNING

STATEMENT ON BORROWING AND PUBLIC DEBT MANAGEMENT BY THE CABINET SECRETARY/NATIONAL TREASURY AND PLANNING TO THE DEPARTMENTAL COMMITTEE ON FINANCE AND NATIONAL PLANNING ON 1ST DECEMBER 2020

I. REPORTS ON NEW BORROWINGS

Honourable Chairman, the total amount of **new external loans** signed between **1st February, 2017 and 31st August, 2020** is **Ksh. 1.87 trillion submitted to Parliament as per the law**

The loans were contracted to **finance capital expenditures and refinance public debt obligations** dues.

II. THE SIZE OF PUBLIC DEBT

1. The *Public Finance Management Act (PFM) 2012* sets the **public debt ceiling** currently at **Kshs 9 trillion**.
2. Of this amount, the **disbursed and outstanding public debt stock** *(including guaranteed debt)* stood at **Kshs 7.12 trillion** .

3. The structure of the disbursed public debt is as follows:

   - **External debt**: **Ksh 3.66 trillion** or 51 per cent of total debt.
   - **Domestic debt**: **Ksh 3.46 trillion** or 49 per cent.

4. **Honourable Chairman,** the objective of the *2020 Medium Term Debt Strategy (which is approved by Parliament and a copy is attached hereto and is also available in www.treasury.go.ke)* is to **mobilize resources through borrowing to finance the budget at minimum risk and cost**.

5. The **current public debt portfolio mix of 51:49 ratio** of external to domestic debt is in line with the medium term debt strategy.

Highlights on domestic debt.

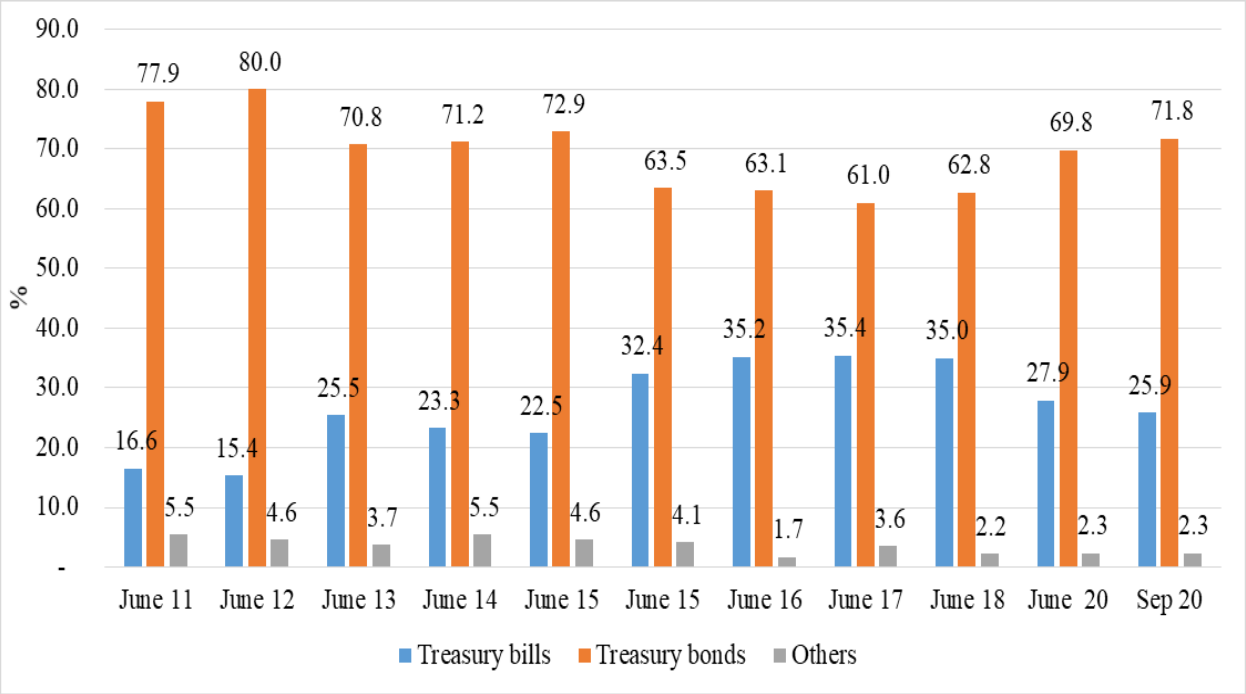
a. Domestic debt

6. Domestic debt attracts an average interest rate of **11 percent per annum**. **The interest rate on domestic debt is market determined.**

7. **The goal is to hold over 70 percent of domestic debt in Treasury Bonds** to lengthen the maturity structure of debt to minimize *settlement and rollover risk*.

8. Over the past 5 years, the holdings of Treasury Bills have been declining while that of **Treasury Bonds has been increasing** (see Chart 1) reflecting **successful implementation of the Medium Term Debt Strategy.**

Chart 1: Changing structure of domestic debt since 2010



Source: National Treasury

External debt situation.

b. External debt

9. **Honourable Chairman,** External debt portfolio reflects an **average interest cost of 4.2 per cent per annum.**

10. Guaranteed debt stands at Kshs 169 billion held mainly by *Kenya Airways, Kenya Power & Lighting Company, KenGen, Kenya Railways* and *Kenya Ports Authority*.

11. The **World Bank Group is the leading multi-lateral creditor at 25%** while **China is the top bilateral external creditor at 21%**

12. Current composition of Kenya's external Debt is; multilateral 39% multilateral debt is 39% of total external debt, bilateral debt is 30% while and commercial debt is 31%.

III. COST AND RISK OF DEBT

13. **Honourable Chairman, external debt is highly vulnerable to exchange rate risk**. In order to mitigate against currency fluctuations, the currency mix for external debt should ideally be matched with the country's currency of export earnings. **Nearly 66 % of Kenya's external debt is denominated in US dollars.**

14. The current ***Medium Term Debt Strategy*** is to increase the uptake of **Euro denominated loans**.

15. The goal of the current ***Medium Term Debt Strategy*** is also to **diversify sources** of external debt financing and **seek highly concessional loans** with interest rate of at least 1 percent with long repayment period beyond 20 years. ***This strategy will lower the debt burden.***

IV. PUBLIC DEBT SUSTAINABILITY

16. **Honourable Chairman,** in May 2020, the IMF *Debt Sustainability Analysis* (DSA) report showed that Kenya's debt remains sustainable.

17. **Addressing the Covid crisis** has required a **strong fiscal response** from the Government that has also **increased the budget deficit.**

18. Kenya's external and public debt vulnerabilities **also reflect the high deficits in the past**, partly due to large infrastructure projects.

19. Kenya generally has **enjoyed strong access to the international capital markets,** and our projections assume that existing Eurobonds will be rolled over at reasonable prices when global capital markets reopen to frontier market issuers. **It is expected that the debt indicators will improve as exports rebound after the global shock dissipates.**

20. The analysis highlights the **need for sustained fiscal consolidation to reduce the level of public debt to more prudent levels over the medium term**.

21. Further, the **debt sustainability analysis suggests that Kenya is susceptible to export and market financing shocks and more prolonged and protracted shocks to the economy would present downside risks to the debt outlook.**

V. FISCAL OVERVIEW

22. **Honourable Chairman,** the Government has revised its plans for fiscal consolidation as it responds with measures to mitigate the impacts of the COVID-19 crisis, but well-targeted spending can support prospects for economic recovery.

23. **Due to the adverse effects of COVID-19**, the government has **revised its consolidation plan** for the coming years in order **to support and stimulate the economy.**

Funding the Fiscal Deficit

24. **Honourable Chairman,** Parliament approved a FY 2020/1 Budget with a fiscal deficit of Kshs 841 billion which may change in the upcoming Supplementary budget.

25. The deficit will be financed through **domestic borrowing**, **multilateral and bilateral sources and commercial borrowing.**

VI. FISCAL CONSOLIDATION AND DEBT RESTRUCTURING

a) Continued progression toward fiscal consolidation

26. **Honourable Chairman,** while **debt levels remain elevated as the country manages economic needs during these unprecedented times**, the ***Budget Review and Outlook Paper*** projects **gradual decline in the fiscal deficit** over the medium term

27. The Government is committed to implement the *2020 Medium Term Debt Strategy*. The MTDS is revised annually and tabled in Parliament as part of the documents supporting Budget Estimates. It recommends:

- **A shift towards concessional external borrowing** and **lengthening of maturity structure of the domestic debt.**

- A **<u>scale down</u> on use of commercial debt** contributing to manageable debt service costs as plans for fiscal consolidation continue.

28. **Government will continue to contain growth in non-core recurrent spending** and **enhance efforts in tax revenue mobilisation** to reduce the deficit.

29. The **debt burden is projected to decline over the medium term** in line with the fiscal consolidation plan under implementation.

b) Debt restructuring

30. **Honourable Chairman,** by way of background, the 2020 *Medium Term Debt Strategy*:

- **Is a plan that the government intends to implement** to achieve this desired composition consistent with other macroeconomic policy settings.

- **Defines the government's desired composition** of debt consistent with its preferences with regard to the **cost-risk trade-off**;

- **Defines necessary institutional, legal and other reforms** needed to remove obstacles that limit development of debt markets and therefore constrain debt management.

- **Medium-term planning horizon** of the government is 3-4 years

31. **Honourable Chairman,** the 2020 *Medium Term Debt Strategy* MTDS identifies key actions to minimize cost and risk:

a. ***Borrow more on concessional terms***;

b. ***Reduce stock of Treasury Bills*** to lower refinancing and rollover risk. The goal is to hold over 70 percent of domestic debt in Treasury Bonds.

c. ***Reduce frequency of issuance of Treasury Bill*** to create fiscal flexibility.

d. ***Identify high cost/risk debts*** for **re-profiling.**

e. **Establishment of a Sinking Fund** to manage debt maturities.

VII. PUBLIC DEBT AND BORROWING POLICY

32. **Honourable Chairman,** the ***Public Debt and Borrowing Policy*** approved by Cabinet in early 2020 will guide management of public debt.

REPUBLIC OF KENYA
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TWELFTH PARLIAMENT (FOURTH SESSION)

RESPONSE TO REQUEST FOR STATEMENT REGARDING PUBLIC DEBT MANAGEMENT

1. **Honourable Speaker,** Section 33 of the Public Finance Management Act of 2012 stipulated that the **Cabinet Secretary of National Treasury submits to Parliament a statement setting out the debt management strategy** of the national government over the medium term with respect to its actual liability and potential liability in respect of loans and guarantees and its plans for dealing with those liabilities.

2. Further that Section 6293) of the Public Finance Management Act of 2012 states that the objective of debt management strategy is to *minimize the cost of public debt management and borrowing over the long-term taking account of risk; promote the development of the market institutions for Government debt securities; and ensure the sharing of the benefits and costs of public debt between the current and future generations*.

3. **Honourable Speaker,** the National Treasury submits reports to National Assembly on new debt every four months. In addition, every year the National Treasury submits the Medium Term Debt Management Strategy (MTDS) latest by 15th February outlining the public debt management strategy of the National Government over the medium Term. **The latest MTDS is in the website of the National Treasury for the general public to refer to.**

4. In addition, the National Treasury submits to Parliament the ***Annual Debt Management Report*** within three months after the end of each financial year. Both the ***MTDS*** and the ***Annual Debt Management Report*** are very detailed in terms of expressing the debt risks and costs characteristics, as well as the fiscal deficits that borrowing seeks to fund.

5. **Honourable Speaker,** it is true that revenue shortfalls due to ongoing pandemic effects and growing public expenditures have generated fiscal deficits funded by public borrowing which led to debt accumulation over the years.

6. **Honourable Speaker,** each year the Cabinet Secretary National Treasury submits annual estimates to the **National Assembly which considers and approves the level of expenditure and the fiscal deficits**. The later determines the quantum of borrowing to finance the deficit.

7. The latest r**eport dated November 3rd, 2020 on Kenya's Debt Sustainability Analysis published by the International Monetary Fund (IMF)** indicates that **Kenya's public debt remains sustainable**.

8. **(**i) On the status of all public debt contracts, **the Government continues to honour all its debt obligations as and when they fall due** in accordance with the provisions of the respective loan agreements.

   (ii) **China extends loans through Export Import Bank of China and China Development Bank**. China is Kenya's leading bi-lateral creditor accounting for 21% of external debt.

   (iii) The National Treasury has **no immediate plans to contract syndicated loans with Trade Development Bank or any other bank.**

   (iv) The National Treasury continues to **deploy debt refinancing techniques to lower the costs and risks in the debt portfolio and create additional fiscal space to lower the fiscal deficit.** This includes **switching Treasury Bills maturities with Treasury Bonds issuance** to lengthen the maturity profile. In addition, **commercial debts will be re-profiled through issuance of longer dated sovereign bonds**.

(v) **The** *2020 Medium Term Debt Strategy* **is to reduce the costs and risks of debt in the medium term.** In the FY 2020/1 Budget**, the budget deficit** of **Ksh. 841.1 billion** will be financed through **net external borrowing of Kshs 346.2 billion** mostly in form of **concessional loans** and **Kshs 494.9 billion** through **net domestic borrowing** in form of Treasury Bonds issuance.

(vi) Kenya has no intentions of defaulting on its debt obligations. **Debt default will limit Kenya's future access to finance from both the domestic and the international financial markets, undermine investor confidence and significantly harm the economy.**

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

1st December, 2020