COUNTY GOVERNMENT OF KILIFI

THE TREASURY

COUNTY BUDGET REVIEW AND OUTLOOK PAPER

SEPTEMBER 2017

LEGAL BASIS FOR THE PUBLICATION OF THE COUNTY BUDGET REVIEW AND OUTLOOK PAPER (CBROP)

The County Budget Review and Outlook Paper, 2017 is prepared in accordance with Section 118 of the Public Finance Management Act, 2012. The Act states that:

1. A County Treasury shall —
   a) Prepare a County Budget Review and Outlook Paper in respect of the county for each financial year; and
   b) Submit the paper to the County Executive Committee by the 30th September of that year.
2. In preparing its County Budget Review and Outlook Paper, the County Treasury shall specify—
   a) The details of the actual fiscal performance in the previous year compared to the budget appropriation for that year;
   b) The updated economic and financial forecasts with sufficient information to show changes from the forecasts in the most recent County Fiscal Strategy Paper;
   c) Information on—
      i. Any changes in the forecasts compared with the County Fiscal Strategy Paper; or
      ii. How actual financial performance for the previous financial year may have affected compliance with the fiscal responsibility principles, or the financial objectives in the County Fiscal Strategy Paper for that financial year; and
   d) Reasons for any deviation from the financial objectives in the County Fiscal Strategy Paper together with proposals to address the deviation and the time estimated for doing so.
3. The County Executive Committee shall consider the County Budget Review and Outlook Paper with a view to approving it, with or without amendments, within fourteen days after its submission.
4. Not later than seven days after the County Budget Review and Outlook Paper is approved by the County Executive Committee, the County Treasury shall—
   a. Arrange for the Paper to be laid before the County Assembly; and
   b. As soon as practicable after having done so, publish and publicise the Paper.

FISCAL RESPONSIBILITY PRINCIPLES IN THE PUBLIC FINANCE MANAGEMENT ACT, 2012

Section 107 of the Public Finance Management (PFM) Act, 2012 sets out the following fiscal responsibility principles to ensure prudence and transparency in the management of public resources:

(i) The county government's recurrent expenditures shall not exceed the county government's total revenue;

(ii) Over the medium term, a minimum of thirty percent of the county government budget shall be allocated to the development expenditures;

(iii) The county governments' expenditures on wages and benefits for its public officers shall not exceed a percentage of the county government's total revenue as prescribed by the County Executive member for finance in regulations and approved by the County Assembly;

(iv) Over the medium term the government borrowing shall be used only for the purpose of financing development expenditure and not recurrent expenditure;

(v) The county debt shall be maintained at sustainable level as approved by county assembly;

(vi) The fiscal risks shall be maintained prudently; and

(vii) A reasonable degree of predictability with respect to the level of tax rates and tax bases shall be maintained taking into account any reforms that may be made in the future.

FOREWORD

This Paper reviews the county fiscal performance in FY 2016/17, analyzing the challenges and emerging issues that hindered attainment of fiscal objectives set for that year and updates the economic and fiscal forecasts upon which financial objectives for FY 2018/19 will be set. It also provides the basis for revision of the FY 2017/18 budget in the context of Supplementary Estimates.

County actual revenue performance in FY 2016/17 exceeded the 2016 County Fiscal Strategy Paper's (CFSP) forecasts on account of midstream adjustments in conditional grants. Actual revenue received was Kshs. 9,287,583,089 against the projected Kshs. 13,332,803,333; representing 70 percent of the targeted revenue. Projected at 12 percent of total county revenue, own source revenue collection fell short the target by 61 percent, while conditional grants from national government attained a 72 percent level against the target. Budget absorption rate increased from 75 percent in FY 2015/16 FY to 81 percent in FY 2016/17. Pending bills, however, continued growing at a very high rate and were estimated to be above Ksh. 2 billion.

Based on the theme of enhancing economic transformation for a shared prosperity, FY 2016/17 budget was predicated upon Kenya's strong macroeconomic performance. This prospect did not hold, however, as the global outlook became more subdued for advanced economies following what is popularly known as Brexit and weaker than expected growth in the United States of America (USA). There was a weakened growth in Sub-Saharan Africa on account of subdued global demand on commodity-exports, particularly fuel exports, and other non-macroeconomic shocks such as conflicts and difficult security situations, droughts and natural disasters, which exacerbated already weak macroeconomic conditions. The unpredictable and drastic change in climatic conditions during this period undercut the projected growth prospects for Kenya in 2016 and 2017. The prolonged drought in the arid and semi-arid areas of the country, including a large area of Kilifi County, not only lowered agricultural productivity but also reached disastrous levels that forced diversion of development resources to relief and emergency operations up to FY2017/18. It is against this backdrop that the national economic outlook for 2017 has been revised downwards to 5.1 percent from 5.5 percent as earlier projected in the 2017 Budget Policy Statement (BPS). Other factors that exerted pressure on the economic outlook included the prolonged electioneering period leading to the 2017 general elections and a subdued credit growth caused by interest rate capping.

In the medium term, however, Kenya's macroeconomic outlook remains favourable though risks remain. The economy is projected to grow at 6.5 percent in FY 2018/19 and 7.1 percent over the medium term. This likely translates to increased transfers to county governments, projected at 3.3 percent of GDP in FY 2018/19. The projected growth is also likely to boost economic activities in Kilifi County and result in improved own source revenue especially if the ongoing recovery of tourism is taken into consideration. This has informed the resource allocation framework and sector ceilings which will be firmed up and rationalized to meet the financial objectives to be set in the County Fiscal Strategy Paper, 2018. Once the sector ceilings are set, departments will be called upon to adhere to these ceilings and allocate resources to programmes with least cost but highest beneficial impact to residents of Kilifi County.

SAMUEL KOMBE NZAI
COUNTY EXECUTIVE COMMITTEE MEMBER,
FINANCE AND ECONOMIC PLANNING

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CHAPTER ONE: INTRODUCTION

Overview

1. Preparation of this County Budget Review and Outlook Paper (CBROP), 2017 complies with Section 118 of the Public Finance Management (PFM) Act, 2012. This section of the law provides for the preparation of this critical document within which planning, budgeting and execution of programmes is managed and specifies the contents therein. In view of the foregoing therefore, this CBROP reviews recent economic developments and actual fiscal performance of the FY 2016/17 against corresponding budget appropriation. It also highlights how the actual performance of FY 2016/17 complied with fiscal responsibility principles under the PFM Act, 2012 and PFM (County Government) Regulations, 2015. Finally, this paper provides the basis for revision of FY 2017/18 budget in the context of Supplementary Budget and the broad fiscal parameters underpinning FY 2018/19 budget and the medium term.

2. In the past four-and-a-half years, the County Government laid the transformative foundation to make greater leaps forward into the second phase of devolved government. This was achieved through implementation of the first County Integrated Development Plan (CIDP), 2013-2017. The successful implementation of the County's development agenda transformed the development trajectory and improved prospects for prosperity in the medium term. It remains desirable for the County to take stock of key achievements, programme implementation challenges, applicable lessons and best practice in order to consolidate these gains for a leap forward into FY 2018/19 and beyond.

Objectives of the CBROP

3. The objectives of the CBROP, 2017 are to:
    - (i) Review the actual fiscal performance compared to the budget appropriation for FY 2016/17;
    - (ii) Update economic and financial forecasts with sufficient information to show changes from the forecasts in the County Fiscal Strategy Paper (CFSP), 2017;

(iii) Provide information on how actual financial performance for the FY 2016/17 may have affected compliance with the fiscal responsibility principles, or the financial objectives in the CFSP, 2016; and

(iv) Provide reasons for any deviation from the financial objectives in the CFSP, 2017 together with proposals to address the deviation and the time estimated for doing so.

Structure of the CBROP

4. This CBROP is organized as follows:

(i) Objectives and structure of the CBROP are provided in Chapter One;

(ii) Review of the fiscal performance in FY 2016/17 and its implications on the financial objectives set out in the CFSP, 2017 is presented in Chapter Two;

(iii) Recent economic developments and updated macroeconomic outlook is highlighted in Chapter Three;

(iv) Resource allocation framework is set out in Chapter Four; and

(v) Conclusion is in Chapter Five.

CHAPTER TWO: REVIEW OF COUNTY FISCAL PERFORMANCE

Overview

5. This chapter presents the County's fiscal performance focusing on deviations between actual and budgeted expenditure and revenue in the FY 2016/17 combined with an analysis of the ways in which this performance affected the financial objectives set in the County Fiscal Strategy Paper (CFSP), 2016. Overall, the County recovered from initial budget implementation challenges occasioned by delays in approval of the budget by the County Assembly and lags in disbursement of funds by the National Government to record an improved fiscal performance in FY 2016/17 compared with FY 2015/16.

Overall Fiscal Performance

6. The County's actual revenue grew by 8 percent in FY 2016/17 on account of increased equitable share of revenue raised nationally and conditional grants. The equitable share of revenue raised nationally allocated to the County Government increased to Kshs. 8,029,167,703 in FY 2016/17 from Kshs. 7,441,216,645 in FY 2015/16, representing a 7-percent increase while conditional grants increased to Kshs. 638,321,809, up from Kshs. 475,525,125 in FY 2015/16. The increase in conditional grants is attributable to the conditional grants to doctors and nurses allowances – this being a return to work negotiated agreement after their strike. Own source revenue collection, including facility improvement fund marginally dropped by 4 percent to Kshs. 620,093,577 in FY 2016/17 from Kshs. 646,871,556 in FY 2015/16. This drop is attributable to the decreased Facility Improvement Fund (FIF) collection mainly due to protracted industrial action by medical staff which kept patients unattended. On the expenditure side, the County Government recorded 26 percent increase to Kshs. 10,843,121,165 in FY 2016/17 from Ksh. 8,587,382,016 in FY 2015/16. The County expenditure has still maintained a steady growth in both recurrent and development classifications.

7. Table 1 below presents the overall fiscal performance from FY 2014/15 to FY 2016/17. The variation between total revenue and total expenditure arises from unmet commitments resulting to pending bills and arrears.

Table 1: Overall Fiscal Performance for FY 2014/15 - FY 2016/17

ITEM DESCRIPTION	PERFORMANCE FY 2014/15	PERFORMANCE FY 2015/16	PERFORMANCE FY 2016/17		
	ACTUAL	ACTUAL	BUDGET	ACTUAL	% GROWTH FROM FY 2015/16
Revenue					
Equitable Share	6,492,284,172	7,441,216,645	8,029,167,703	8,029,167,703	7%
Conditional Grants	105,150,000	475,525,125	886,163,682	638,321,809	26%
Own Revenue	550,816,703	519,075,625	1,385,881,577	554,484,876	6%
Facility Improvement Fund (FIF)	48,512,266	127,795,931	200,000,000	65,608,701	-95%
Re-voted Revenue (B/F)	-	-	2,831,590,371	-	-
Total	**7,196,763,141**	**8,563,613,326**	**13,332,803,333**	**9,287,583,089**	**8%**
Expenditure					
Compensation to employees	1,771,746,404	2,547,026,468	2,909,546,946	2,788,470,274	9%
Use of goods and services	1,307,255,549	2,334,936,424	1,766,719,615	1,336,606,221	-75%
Other recurrent	1,456,870,012	119,553,894	1,191,377,952	-	-
Development	2,976,901,139	3,585,865,230	6,830,750,524	4,979,212,535	28%
Total	**7,512,773,104**	**8,587,382,016**	**11,858,199,604**	**9,104,289,030**	**6%**

Source: County Treasury

County Own Source Revenue Performance

8. In FY 2016/17, own source revenue collection, including Facility Improvement Fund (FIF) stood at Kshs. 620,093,577 comparing with a target of Kshs. 1,585,881,557, representing a deviation of 61 percent from the target. The collected amount was also lower than Kshs. 646,871,556 collected in FY 2015/16. Analysis of own source revenue collection by stream shows immense potential on plot ground rent which consistently grew from Kshs. 4,541,843 in FY 2014/15 to Kshs.4,903,549 in FY 2015/16, and to Kshs. 6,466,287 in FY 2016/17. Revenue collection from land rates and other land

revenue was also impressive having recorded an increase from Kshs. 150,728,560 in FY 2014/15 to Kshs. 222,904,581 in FY 2016/17 though there was a decline to Kshs. 138,348,379 in FY 2015/16. The increase in collection of land rates and other land revenue in FY 2016/17 is explained by the waiver on penalties to rate payers, a campaign that ran for the better part of the fiscal year. Cess on natural resources recorded an increase in 2015/16 at Ksh. 205,501,826 up from Ksh. 148,724,039 in the year 2014/15, although it further decreased in the year 2016/17 to Kshs. 128,366,720. Further analysis shows mixed performance on other own source revenue streams. These include Sales of Tender Documents which was at Kshs. 4,788,000 in FY 2014/15 but dropped to Kshs. 652,000 in FY 2016/17 due to the policy stance not to sale tender documents. Similarly, Food and Hygiene fees consistently dropped to Kshs. 1,193,090 in FY 2016/17 from Kshs. 1,704,700 in FY 2015/16 and Kshs. 4,985,425 in FY 2014/15. On the contrary, House rent dropped from Kshs. 4,268,168 in FY 2014/15 to Kshs. 1,500,000 in FY 2015/16 before increasing to Kshs. 2,047,815 in FY 2016/17.

9. The County Government has drawn applicable lessons from the deviations between targeted and actual own source revenue collection. In this regard, projections of own source revenue collection will continually be adjusted to realistic levels while strategies to increase collection will be regularly reviewed and corrective measures implemented to ensure collection of own source revenue is optimized.

Table 2: County Own Revenue Collection for FY 2014/15 - FY 2016/17

Revenue Stream	Actual Revenue Collection	Actual Revenue Collection	Annual Revenue Estimates	Actual Revenue Collection	% Deviation from Target FY 2016/17
	FY 2014/15	FY 2015/16	FY 2016/17	FY 2016/17	
Facility Improvement Fund	48,512,266	127,795,931	85,881,577	65,608,701	-24%
Land Rates and other Land Revenue	150,728,560	118,874,085	384,775,645	222,904,581	-42%
Cess on natural resources	148,724,039	205,501,826	529,192,453	128,366,720	-76%
Business Permits	96,474,071	76,760,495	246,718,009	67,414,245	-73%
Parking Fees	47,255,581	19,740,023	87,051,981	22,415,974	-74%
Market Fees	26,352,393	15,059,945	64,952,583	15,917,455	-75%

Revenue Stream	Actual Revenue Collection	Actual Revenue Collection	Annual Revenue Estimates	Actual Revenue Collection	% Deviation from Target FY 2016/17
	FY 2014/15	FY 2015/16	FY 2016/17	FY 2016/17	
Bill Boards and signage	20,128,072	14,333,944	47,072,894	17,321,882	-63%
Building Plan approval and Inspection	16,290,903	5,874,115	20,549,385	8,452,043	-59%
Rent/Stall rents		5,480,380	17,944,487	7,193,960	-60%
Survey fees and plot rents		72,000	6,861,938	2,407,280	-65%
Sale of Tender Documents	4,788,000	631,500	2,067,729	652,000	-68%
Plot ground rent	4,541,843	4,903,549	15,511,682	6,466,287	-58%
House rent	4,268,168	1,500,100	7,269,306	2,047,815	-72%
Refuse Collection		836,243	3,474,516	588,127	-83%
Food Hygiene Fees	4,985,425	1,704,700	6,232,658	1,193,090	-81%
Slaughter House and Livestock sale Yards		932,215	3,052,365	2,178,932	-29%
Others	26,279,648	46,870,505	57,272,369	48,964,485	-15%
Total	**599,328,969**	**646,871,556**	**1,585,881,577**	**620,093,577**	**-61%**

Source: County Treasury

County Expenditure Performance for FY 2016/17

10. In FY 2016/17, the County's actual expenditure amounted to Kshs.10,843,121,165 against a target of Kshs.13,322,803,334 representing an absorption rate 81 percent of the approved budget. The department of Health and County Public Service Board had the highest absorption rate of 88 percent and 87 percent having spent Kshs. 2,619,834,538 and Kshs. 58,150,447 respectively. The department of Devolution, Public Service and Disaster Management and County Executive, both recorded an absorption rate of 86 percent having spent Kshs. 668,897,155 and Kshs. 324,910,944 respectively. The department of Trade, Cooperatives, Industrialization, Tourism and Wildlife and ICT, Culture and Social Services had the lowest absorption rates of 52 percent and 69 percent having spent Kshs. 226,179,216 and Kshs. 181,460,850 respectively. These were closely followed by the County Assembly and Lands, Energy, Housing, Physical Planning and Urban Development which had absorption rates of 71

percent and 76 percent having spent Kshs. 846,382,702 and Kshs. 379,265,228 respectively.

11. In FY 2016/17, recurrent expenditure was Kshs. 5,863,908,630representing a 90 percent uptake of the total recurrent budget of Kshs. 6,502,052,809. A detailed analysis of recurrent expenditure in FY 2016/17 shows that Trade, Cooperatives, Industrialization Tourism and Wildlife recorded the lowest absorption of recurrent budget at 76 percent having spent Kshs. 59,987,795out of Kshs 79,122,071. The department of ICT, Culture and Social Services had a recurrent absorption rate of 77 percent having spent Kshs. 93,701,423out of Kshs. 121,648,918.

12. In FY 2016/17, the actual development expenditure was Kshs. 4,979,212,535 representing 73 percent of the development budget of Kshs. 6,830,750,525. The department of Water, Environment and Solid Waste Management had the highest absorption rate of 83 percent having spent Kshs. 1,074,208,594 out of Kshs. 1,296,445,953; followed by the department of Roads, Transport and Public Works with absorption rate of 82 percent having spent Kshs. 1,474,684,308 out of Kshs. 1,800,278,950. The County Assembly had the lowest absorption rate of 40 percent having spent Kshs. 167,334,342 out of Kshs. 415,144,013; followed by Trade, Cooperatives, Industrialization Tourism and Wildlife with 46 percent having spent Kshs. 166,191,421 out of Kshs. 357,549,746. The table below presents the county expenditure performance for FY 2016/17.

Table 3: County Expenditure Performance for FY 2016/17

DEPARTMENT	RECURRENT		DEVELOPMENT		TOTAL		AR*
	BUDGET	ACTUAL	BUDGET	ACTUAL	BUDGET	ACTUAL	
COUNTY ASSEMBLY	774,923,317	679,048,360	415,144,013	167,334,342	1,190,067,330	846,382,702	71%
COUNTY EXECUTIVE	376,227,098	324,910,944			376,227,098	324,910,944	86%
FINANCE & ECONOMIC PLANNING	502,639,675	411,106,061	40,063,063	24,827,190	542,702,738	435,933,251	80%
AGRICULTURE, LIVESTOCK AND FISHERIES	300,267,057	287,650,990	478,824,535	345,986,361	779,091,592	633,637,351	81%
WATER, ENVIRONMENT AND SOLID WASTER MANAGEMENT	199,000,282	195,843,449	1,296,445,953	1,074,208,594	1,495,446,235	1,270,052,043	85%

DEPARTMENT	RECURRENT		DEVELOPMENT		TOTAL		AR*
	BUDGET	ACTUAL	BUDGET	ACTUAL	BUDGET	ACTUAL	
EDUCATION AND YOUTH AFFAIRS AND SPORTS	685,032,276	662,044,696	1,085,976,859	712,219,706	1,771,009,135	1,374,264,402	78%
HEALTH SERVICES	2,186,718,544	1,988,249,328	775,290,527	631,585,210	2,962,009,071	2,619,834,538	88%
ROADS, TRANSPORT AND PUBLIC WORKS	367,913,248	349,468,730	1,800,278,950	1,474,684,308	2,168,192,198	1,824,153,038	84%
LANDS, ENERGY, HOUSING,PHYSICAL PLANNING AND URBAN DEVELOPMENT	214,038,281	187,508,096	285,911,881	191,757,132	499,950,162	379,265,228	76%
ICT, CULTURE AND SOCIAL SERVICES	121,648,918	93,701,423	141,776,049	87,759,427	263,424,967	181,460,850	69%
TRADE, COOPERATIVES, INDUSTIRALIZATIO N TOURISM AND WILDLIFE	79,122,071	59,987,795	357,549,746	166,191,421	436,671,817	226,179,216	52%
COUNTY PUBLIC SERVICE BOARD	67,027,670	58,150,447			67,027,670	58,150,447	87%
DEVOLUTION PUBLIC SERVICE AND DISASTER MANAGEMENT	627,494,372	566,238,311	153,488,949	102,658,844	780,983,321	668,897,155	86%
TOTAL	**6,502,052,809**	**5,863,908,630**	**6,830,750,525**	**4,979,212,535**	**13,332,803,334**	**10,843,121,165**	**81%**

Source: County Treasury

AR – Absorption rate

Overall Balance and Financing

13. In FY 2016/17, the overall fiscal balance on a commitment basis amounted to a fiscal deficit of Kshs. 1,555,538,076 which is an improvement from that of Kshs.1,689,581,056 in FY 2015/16 as shown below.

Table 4: Fiscal Balance on a Commitment Basis for FY 2014/15 to 2016/17

Item Description	Performance FY 2014/15	Performance FY 2015/16	Performance FY 2016/17	
	Actual		Budget	Actual
Total Revenue	**9,024,446,027**	**8,563,613,326**	**13,332,803,333**	**9,287,583,089**
Equitable Share	6,492,284,172	7,441,216,645	8,029,167,703	8,029,167,703
Conditional Grants	105,150,000	475,525,125	886,163,682	638,321,809
Local Revenue	550,816,703	519,075,625	1,385,881,577	554,484,876
Facility Improvement Fund (FIF)	-	127,795,931	200,000,000	65,608,701
Re-voted Revenue	1,876,195,152		2,831,590,371	-

Total Expenditure	**8,695,370,923**	**10,196,810,162**	**13,332,803,333**	**10,843,121,165**
Recurrent	4,987,723,862	5,436,684,743	6,502,052,808	5,863,908,630
Development	3,707,647,061	4,760,125,419	6,830,750,525	4,979,212,535
Fiscal Balance	**329,075,104**	**(1,633,196,836)**	**-**	**(1,555,538,076)**

Source: County Treasury

CHAPTER THREE: RECENT ECONOMIC DEVELOPMENTS AND OUTLOOK

Overview

14. The performance of the national economy is a key determinant to allocation and utilization of resources in the country. Thus, macroeconomic management and performance of sectors in the national economy affects transfers to county governments much the same way as it affects own source revenue collection within the County.

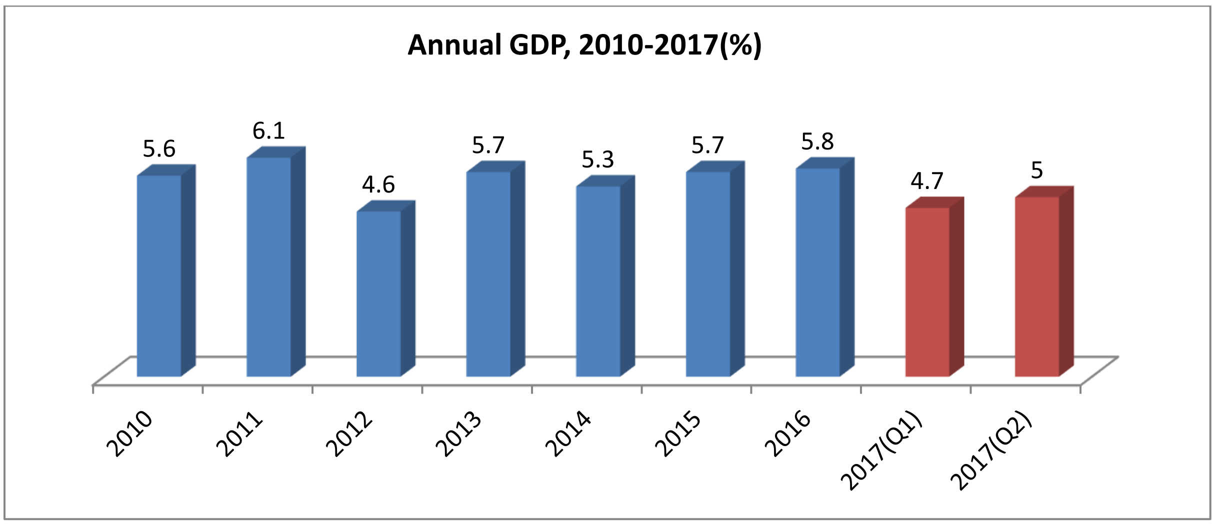
15. Recent economic developments have had a negative impact to the national economy in 2017 leading to a downward revision of economic growth from 5.5 percent to 5.1 percent. The severe drought that started in 2016, the prolonged electioneering period leading to the August 2017 and October 2017 general and presidential elections respectively, and the subdued credit growth to the private sector attributable to interest rate capping will slow economic growth prospects in 2017. This chapter highlights the performance of key macroeconomic variables such as Gross Domestic Product (GDP), inflation rate, interest rates, and exchange rates; and links their performance to resource allocation and utilization in the County. Further, the chapter presents the Medium Term Fiscal Framework and risks to the outlook to describe the county policy intentions to manage the budget and envisaged risks over the medium term period.

Gross Domestic Product

16. Kenya's economy is estimated to have expanded by 5.8 percent in 2016 compared to a revised growth of 5.7 percent in 2015. The sectors that recorded significant growth were accommodation and food services, information and communication, real estate, and transport and storage. This growth was hampered by persistent drought in 2016 that negatively impacted agriculture and electricity supply. Economic growth is estimated to have decelerated to 4.7 percent during the first quarter of 2017 before gaining to 5.0 percent in the second quarter ***(refer to Figure 1)***. The economic outlook for 2017 has been revised downwards to 5.1 percent from 5.9 percent as earlier projected in the 2017 Budget Policy Statement (BPS). This is a result of developments

related to severe drought that started in 2016, prolonged electioneering period due to the 2017 General elections and subdued credit growth due to interest rate capping. The economy is projected to grow at 6.5 percent in FY 2018/19 and 7.1 percent over the medium term. This translates to increased transfers to county governments which is projected at 3.3 percent of GDP in FY 2018/19. The projected growth will also boost economic activities in the County and improve own source revenue especially when the ongoing recovery of tourism is taken into consideration.

Figure 1: GDP Growth Rates for 2010-2017 (%)

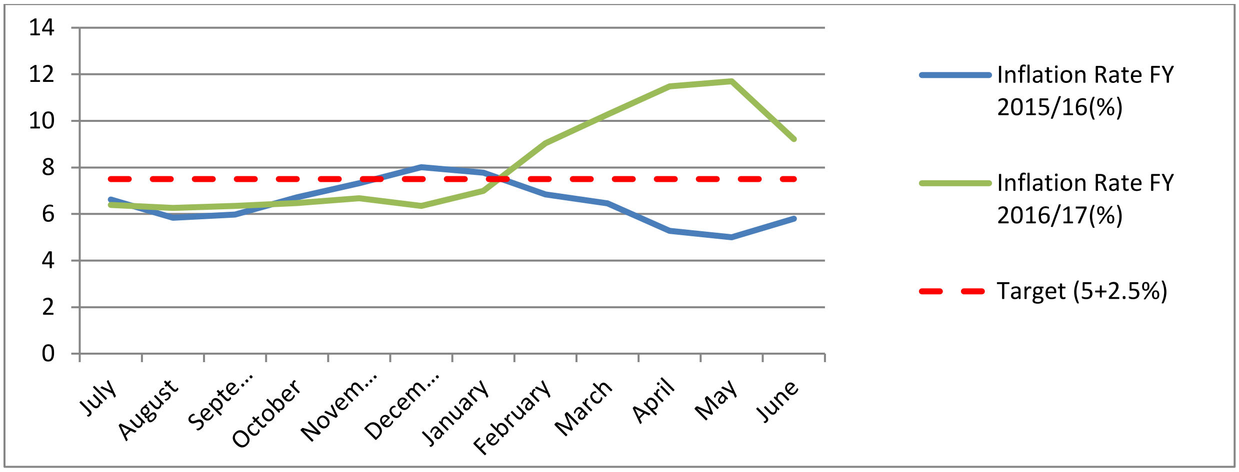


Source: Kenya National Bureau of Statistics

Inflation rate

17. In the first half of FY 2016/17 the rate of inflation remained within target range of between 2.5 and 7.5 percent. There was run-away inflation in the second half of FY 2016/17 due to surge in food prices that was evidenced by comparably high wholesale prices on key food crops. This was largely attributable to adverse weather conditions that prevailed for the better part of the fiscal year and prompted government action to temporarily exempt import on maize, sugar and powdered milk in order to contain demand-driven inflationary pressures. It is expected that inflation will decline and fall within the target range in FY 2017/18 ***(refer to Figure 2).***

Figure 2: Overall Inflation Rate (%) for FY2015/16 and FY 2016/17

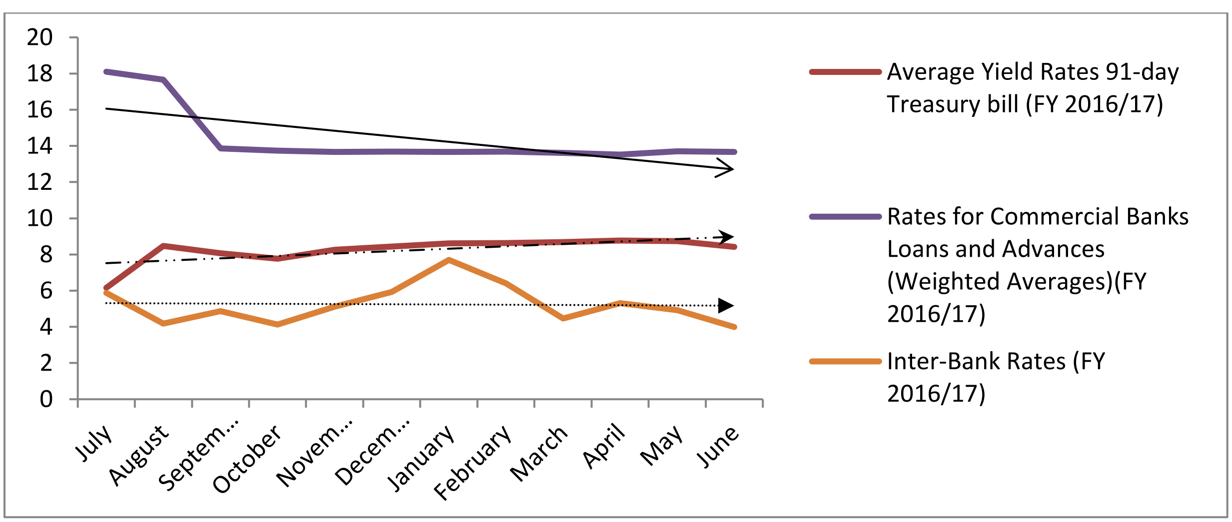


Source: Kenya National Bureau of Statistics

Interest Rates

18. In FY 2016/17, the average yield rate for the 91-day Treasury bills, which is the benchmark for the general trend of interest rates, took an upward trajectory fluctuating from a range of 6.16 percent in July, 2016 to 8.42 percent in June 2017. The rates for commercial banks loans and advances recorded a high rate of 18.1 percent and dipped to 13.52 percent in July 2016 and April 2017 respectively. This general downward trend is attributable to the interest rate cap on lending. Interbank rates in FY 2016/17 were fairly unstable and hit 7.7 percent in January 2017 and a low of 3.99 percent in June, 2017. Figure 3 below analyses the trends in the interest rates.

Figure 3: Analysis of Trends in Interest Rates (%) for FY 2016/17

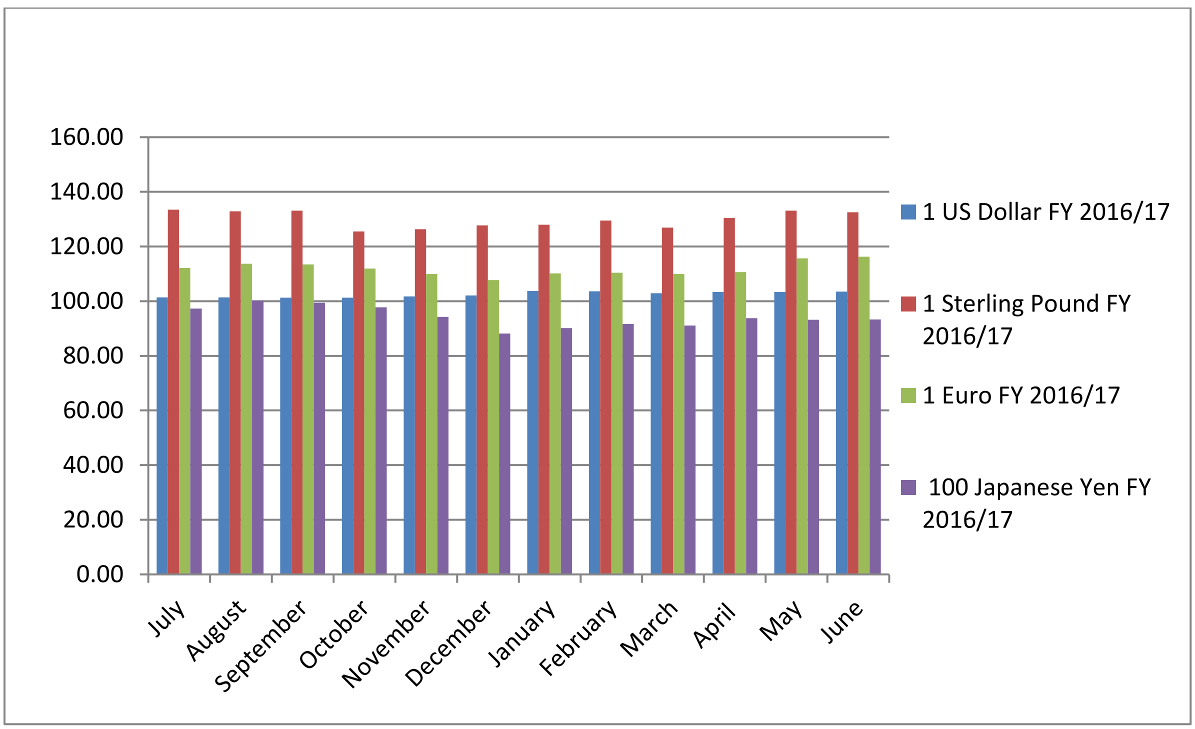


Source: Kenya National Bureau of Statistics

Exchange Rates

19. The exchange rate of the Kenyan shilling to US dollar remained fairly stable in FY 2016/17. The Kenya Shilling exchanged at a low of Kshs.101.27 to the US dollar in September 2016 and a high of Kshs.103.75 in January 2017. The Kenya Shilling to Sterling pound fluctuated from a high of Kshs.133.42 in July 2016 and a low of Kshs.125.47 in September 2016. The Kenya Shilling to the Euro exchanged at a low of Kshs.107.67 in December 2016 and a high of Kshs.116.24 in June 2017. The Kenya Shilling to Japanese Yen slopped downwards in the period under review having exchanged at a high of Kshs.100.24 in August 2016 and a low of Kshs.88.1 in December 2016. Figure 4 presents the exchange rates of these major currencies for FY 2016/17.

Figure 4: Exchange Rates FY 2016/2017



Source: Kenya National Bureau of Statistics

Medium Term Fiscal Framework

20. FY 2017/18 budget was assented in June 19, 2017 courtesy of the revised budget calendar that anticipated challenges because the budget preparation and approval process coincided with the electioneering period for General elections constitutionally scheduled for August, 2017. It is the implementation of FY 2017/18 budget that could not escape the effects of the General election particularly during the first quarter.

21. The County faced acute shortage of funds arising from delays in disbursement of funds from the national government which was attributed to discrepancies on the disbursement schedule approved by Parliament, in this case the Senate. Other budget implementation bottlenecks include the precautionary quarterly pro-rated upload of FY 2017/18 budget in the Integrated Financial Management Information System (IFMIS) that curtailed expenditure especially on expenses related to drought mitigation. Additional conditions on reports that were hitherto submitted for withdrawal of funds were quickly given prominence and had the effect of limiting expenses to personnel emoluments during the first quarter.

22. On the own revenue front, the 'wait and see' attitude adopted by investors, business community and consumers resulting from uncertainties related to the General elections crippled economic activities in the County. This in turn affected own source revenue collection that has been significantly below target during the first quarter of FY 2017/18. Also, the Finance Bill 2017 which contain own source revenue raising measures is yet to be submitted to the County Assembly for approval. This potentially delays implementation of the measures therein and affects realization of own source revenue targets.

23. The County Treasury will keep an eye on these developments to identify potential budget implementation risks and take appropriate action to mitigate against them in pursuit of improved delivery of public goods and services. The specific fiscal policy objectives underpinning the FY 2017/18 budget and MTEF the County will pursue are:

(i) Enhancing own source revenue collection through automation and sealing revenue loopholes.

(ii) Monitoring performance in own source revenue collection in a bid to arrest accrual of pending bills and arrears.

(iii) Shifting financial resources from recurrent to development expenditures so as to promote sustainable and inclusive growth.

(iv) Extending to outer years, budget allocation for projects in a bid to link project implementation cycle with financial provisions.

Risks to Economic and Fiscal Outlook

24. The macroeconomic and fiscal outlook is replete with risks that the County will closely monitor with a view to take appropriate measures and safeguards should they materialize. The risks include;

(i) Persistent political overtones due to disenfranchisement with the electoral outcome particularly the repeat Presidential elections. This may extend the 'wait and see' attitude held by investors, business community and consumers thereby adversely impact economic activities especially tourism related activities in the County.

(ii) Exposure to adverse weather conditions that instead continue to drain resources towards drought emergencies in the medium term.

(iii) Recurrent expenditure pressures particularly salary increments arising from negotiated agreements from industrial action and the resultant increase in the wage bill that does not necessarily fill critical human resource gaps in the County.

(iv) Accumulation of pending bills and arrears arising from shortfalls in own source revenue collection.

CHAPTER FOUR: RESOURCE ALLOCATION FRAMEWORK

Adjustments to the FY 2017/18 Budget

25. Preparation of FY 2018/19 budget commences when implementation of FY 2017/18 budget is underway albeit with challenges. Apart from the challenges earlier alluded, the budget preparation and approval process in the County was ahead of the approval process of the County Allocation of Revenue Bill, 2017 by Parliament. When this is finally done and County Allocation of Revenue Act (CARA) is in place, then this development will necessitate budget revision to reflect approved funds transfers to the County.

26. Therefore, the revised FY 2017/18 budget will reflect:

(i) Equitable share of revenue allocation provided in the CARA,

(ii) Revision of conditional grants as provided in CARA,

(iii) Revision of unspent revenue balances as at end of FY 2016/17,

(iv) Provisions accommodating pending bills and arrears emanating from FY 2016/17.

(v) Provisions to give priority to on-going projects to secure their completion before new ones commence.

27. These revisions will take into account the fiscal developments during the first quarter of FY 2017/18 as well as ensure continuous provision of key services; implementation of strategic interventions and flagship projects and that in cases of adverse consequences on original planned projects and programmes it is a result of unavoidable logical implication of the trade-offs and reallocations within the available resource envelope.

28. Consequently, the revised budget will affect new projects and distribution to each County Ward; the agreed minimum allocation for projects to each Ward, a practice that

ensures equitable distribution of projects to Wards; and Ward Development Projects (WDP). This is deemed unavoidable because, apparently, the remedial action on some of the issues that the revised budget seeks to address, such as pending bills and on-going projects, cannot be fashioned to satisfy these objectives. The distribution of pending bills and arrears, and on-going projects do not take any particular order.

29. On the revenue front, automation of revenue collection which will be rolled out in the second half of FY 2017/18 will, together with other administrative measures, help in sealing revenue loopholes. The County will also consolidate the gains made on the legislative front by operationalizing laws that enable revenue collection including the Finance Bill, once enacted, so as to boost revenue collection to meet and possibly exceed the set target.

Medium Term Expenditure Framework

30. The medium term fiscal projections take a conservative approach particularly in own source revenue projections and expenditures funded. This is aimed at ensuring more resources coming from enhanced own source revenue collections are directed to development related expenses while curtailing allocation of own source revenue to recurrent spending. This way, the County aims to ensure policy consistency and predictability of spending towards addressing eminent delays in payments over the medium term.

31. The County will fully embrace this stance in the revised budget FY 2017/18 where trade-offs and reallocations will be made to accommodate pending bills and on-going projects without expanding the resource envelope. The process will ensure the County remains on the right pedestal to scrutinize expenditure proposals for efficiency and effectiveness as well as ensure only high impact projects are prioritized and accommodated using the scarce resources. In this regard, allocation to projects that will be traded-off to cater for the on-going projects and those that were not funded in the revised budget FY 2017/18 will be scrutinized for reprioritization and allocation of funds in FY 2018/19.

32. Projection of own source revenue collection in FY 2018/19, is therefore predicated on actual collections in FY 2016/17 in the context of persistent shortfalls from targets in preceding years, known challenges that contributed to these shortfalls, measures put in place to remedy these challenges and the apparent potential for raising more own source revenue. The computation of own source revenue with these variables takes it to the conservative estimate of Kshs. 650,000,000 in FY 2017/18 as shown in table 7 below.

Table 5: Revenue Actuals, Approved and Projections for FY 2016/17- FY 2018/19 Budget

Revenue Stream	Actual Revenue Collection	Approved Revenue Estimates	Projected Revenue Estimates
	FY 2016/17	FY 2017/18	FY 2018/19
Equitable Share	8,029,167,703	9,950,900,000	10,833,000,000
Conditional Grants	638,321,809	1,026,090,396	1,229,707,963
Facility Improvement Fund	65,608,701	208,413,052	100,468,651
Land Rates and other Land Revenue	222,904,581	217,815,688	313,677,194
Cess on natural resources	128,366,720	255,086,204	341,052,835
Business Permits	67,414,245	157,974,770	114,623,556
Parking Fees	22,415,974	41,747,093	21,488,039
Market Fees	15,917,455	7,349,685	15,258,534
Bill Boards and signage	17,321,882	22,917,678	16,604,823
Building Plan approval and Inspection	8,452,043		8,102,161
Rent/Stall rents	7,193,960	593,864	6,896,158
Survey fees and plot rents	2,407,280		2,307,628
Sale of Tender Documents	652,000		625,010
Plot ground rent	6,466,287		6,198,608
House rent			

Revenue Stream	Actual Revenue Collection	Approved Revenue Estimates	Projected Revenue Estimates
	FY 2016/17	FY 2017/18	FY 2018/19
	2,047,815		1,963,043
Refuse Collection	588,127	1,038,631	563,781
Food Hygiene Fees	1,193,090	4,779,771	1,143,701
Slaughter House and Livestock sale Yards	2,178,932	6,194,987	2,088,733
Others	48,964,485	5,751,834	46,937,545
TOTAL	9,287,583,089	11,906,653,653	13,062,707,963

33. The County medium term priorities and strategies will broadly be guided by the Third Medium Term Plan (2018-2022) of the Kenya Vision 2030, the second generation County Integrated Development Plan (2018-2022), Annual Development Plan, 2017 and strategic policy initiatives of the county government's administration. Expenditure composition will focus on productive projects, roads and water infrastructure projects while protecting budgetary allocation to priority commitments including the Kilifi County Health Complex, Scholarship Programme, Free Pre-Primary School Education Programme; School Health and Nutrition through provision of school milk; Mbegu Fund; Cash Transfers to the Elderly; Ward Development Programme; and Car Loans and Mortgage for the County Executive staff.

34. The indicative ceilings for FY 2018/19 take into account the aggregate resource envelope, fiscal responsibility principles, non-discretionary expenditure and expenditure priorities including ring-fencing funds for on-going projects from FY 2016/17 which may not get budgetary provision in FY 2017/18. Where possible, adjustments have been made on identified one-off expenditure in FY 2017/18 while considering the fiscal outturn for FY 2016/17 as the base. These ceilings are provided in table 6 below.

Table 6: Indicative Expenditure Ceilings FY 2018/19 Budget

DEPARTMENT	RECURRENT	DEVELOPMENT	TOTAL

	FY 2017/18	FY 2018/19	FY 2017/18	FY 2018/19	FY 2017/18	FY 2018/19
County Assembly	900,423,148	714,680,971	149,800,000	150,000,000	1,050,223,148	864,680,971
Office of the Governor	563,129,935	345,810,088			563,129,935	345,810,088
Office of the County Attorney		139,258,000			-	139,258,000
Finance & Economic Planning	593,974,614	1,851,093,664	38,000,000	1,568,756,330	631,974,614	3,419,849,994
Agriculture and Crop Husbandry	334,830,052	422,783,323	209,164,804	221,850,995	543,994,856	644,634,318
Livestock Production and Fisheries	35,450,419	36,874,524	155,203,737	112,966,204	190,654,156	149,840,728
Water & Sanitation	207,381,037	190,833,228	781,210,455	301,477,635	988,591,492	492,310,863
Environment, Natural Resources & Wildlife	53,495,000	44,100,000	103,375,000	97,118,000	156,870,000	141,218,000
Education and ICT	913,177,449	722,945,610	532,882,209	616,225,645	1,446,059,658	1,339,171,255
Medical Services	2,261,413,173	2,175,109,194	551,283,127	780,143,917	2,812,696,300	2,955,253,111
Public Health	40,285,273	165,250,124	12,632,000	-	52,917,273	165,250,124
Roads, Transport & Public Works	347,744,314	318,469,214	1,321,119,565	601,959,186	1,668,863,879	920,428,400
Lands, Energy and Housing	271,247,969	178,014,313	76,017,000	92,537,635	347,264,969	270,551,948
Physical Planning and Urban Development	8,640,000	43,500,000		96,040,000	8,640,000	139,540,000
Culture, Social Services and Sports	141,044,963	81,324,266	120,629,269	131,643,185	261,674,232	212,967,451
Trade, Tourism & Cooperative Development	105,365,456	77,124,758	219,550,937	137,846,544	324,916,393	214,971,302
County Public Service Board	90,434,179	61,509,147			90,434,179	61,509,147
Devolution, Public Service and Disaster Management	762,134,166	520,617,912	78,357,950	64,844,351	840,492,116	585,462,263
Gross Total	**7,630,171,147**	**8,089,298,336**	**4,349,226,053**	**4,973,409,627**	**11,979,397,200**	**13,062,707,963**
Budget Threshold	**63.69%**	**61.93%**	**36.31%**	**38.07%**	**100.00%**	**100.00%**

CHAPTER FIVE: CONCLUSION

35. The FY 2018/19 MTEF budget presented in this County Budget Review and Outlook Paper (CBROP) has been developed taking into account moderate growth in overall expenditure, the need to maintain fiscal discipline and adhere to the fiscal responsibility principles outlined in the Public Finance Management Act, 2012.

36. Allocation of resources over the medium term is set to ensure continuity in policy priorities by completing on-going projects, addressing emerging priorities while focusing on implementing priority programmes developed in accordance to the Third Medium Term Plan (2018-2022) of Vision 2030; County Integrated Development Plan (2018-2022); Annual Development Plan, 2017; and strategic policy initiatives of the county government's administration.

37. The set of policies outlined in this CBROP and the Annual Development Plan, 2017 will guide departments in their Sector Working Groups in their bid for resources and preparation of the FY 2018/19 budget. The sector ceilings will be firmed up in the next County Fiscal Strategy Paper by the February 2018 deadline.