# KENYA

## ECONOMIC REFORMS FOR 1996 - 1998

### The Policy Framework Paper

Prepared by the Government of Kenya

in collaboration with the International Monetary Fund and the World Bank

*February 16, 1996*

# ECONOMIC REFORMS FOR 1996 - 1998

## The Policy Framework Paper

**KENYA**
**ECONOMIC REFORMS FOR 1996-1998:**
The Policy Framework Paper
Prepared by the Government of Kenya in collaboration with the IMF and the World Bank
February 16, 1996

---

# I. INTRODUCTION

1. Kenya faces a major challenge in reducing unemployment and poverty. The number of people unemployed is currently more than two million and at least ten million people are living in poverty. In addition, around one-half million people will enter the labor force each year over the next decade. To achieve significant reductions in unemployment and poverty, the economy will require to grow on average by over 6 percent a year for several years. It will also be imperative that the Government places increased emphasis on social services and adequately targeted interventions in favour of the poor.

2. The Government is determined to meet this challenge and has in this respect initiated a number of reforms in the last three years. The specific reforms which have been implemented so far include: decontrol of prices; removal of import licensing; removal of exchange controls; liberalisation

of pricing and movement of maize; liberalisation of the petroleum market; and reform of the civil service.

3. This reform framework incorporates the policies and programmes that the Government is committed to pursue over the next three years in order to deepen the reform process. This will create the conditions necessary to achieve the desired rapid and sustainable economic growth.

# II. ECONOMIC PERFORMANCE

## Macroeconomic and Structural Policies

4. Sustained effort by the Government to tighten fiscal and monetary policies since mid-l993 has been effective in stabilizing the economy and contributing to the revival of economic growth. Gross domestic product (GDP) grew by about 3 percent in 1994 and by an estimated 5 percent in 1995. The fiscal deficit has been sharply reduced from over 11 percent of GDP in 1992/93 to 2.6 percent in 1994/95. Expansion in money supply, though still high, has also been reduced substantially. Inflation has been reduced substantially. Annual inflation (month over month) declined steadily from a peak of 62 percent in January 1994 to 6.9 percent in December 1995. However, after a small surplus in 1993, the current account balance (excluding official transfers) deteriorated to a deficit of 0.4 percent of GDP in 1994, and further to an estimated 4.2 percent in 1995.

5. The tight control on the budget was accompanied by tax reforms aimed at reducing the tax rates and broadening the tax base. Expenditures have also been reoriented with more resources allocated to non-wage recurrent outlays and development expenditures. Progress in controlling expenditure has, however, been slow and some ministries have continued to spend in excess of their authorized limits.

6. With respect to structural reforms, the Government has, since mid-l993, made significant strides. It has eliminated exchange controls including restrictions on inward portfolio investments and removed all trade restrictions, except for a short list of a few products controlled for health, security and environmental reasons. The number of non-zero tariff rates has been reduced from seven to five, and the maximum tariff reduced from 62 percent in 1993/94 to 40 percent in 1995/96. With the liberalisation of the maize market in December 1993 and the petroleum market in October 1994, all price controls have been abolished. Steps were also taken to strengthen the financial system, including enhanced prudential supervision of commercial banks, the closure of financially unsound banks, and strict enforcement of statutory requirements of nonbank financial institutions (NBFIs), some of which were either transformed into banks or merged with existing banks. Firm actions were also taken to deal with the hitherto widespread mismanagement and corruption in the financial system involving access to credit from the Central Bank and budgetary resources.

7. The Government has since 1992 been implementing a major civil service reform programme aimed at reducing the overall size of the civil service and achieving cost containment, and rendering the civil service more efficient by improving working conditions. To this end, the civil service has been trimmed by over 33,000 since July 1993.

8. Privatisation of 211 non-strategic public enterprises has started, with the Government divesting its holdings in over 100 firms (including 43 tea factories in which it turned over the bulk of its shareholdings to farmers) by the end of 1995. In addition, it has reduced its holdings in another six enterprises, including Kenya Airways, Kenya Commercial Bank and the National Bank of Kenya. The Government is also making progress in parastatal reform. Initial steps to restructure key public enterprises like the Kenya Ports Authority (KPA), Kenya Railways (KR), Kenya Power and Lighting Company (KPLC) and Kenya Posts and Telecommunications Corporation (KPTC), have begun. However, further steps will need to be taken in order to accelerate progress in this area and thereby improve on the low investment efficiency that limits economic growth.

## Social Policies

9. The Government has given clear priority to education and health, and has taken a pragmatic approach in respect to private provision of these services. To date, Kenya has achieved an average life expectancy of 58 and an infant mortality rate of 61 per thousand live births. Many challenges, however, remain. Secondary school enrolment is only 29 percent of the relevant age-group. Child nutrition, after showing improvement during 1982-87, stagnated, and even deteriorated in some areas. It is also estimated that thirty-four percent of the population under five is currently stunted. Child status indicators show significant differences according to the education of the mother, which is also a proxy for income differences. While there is no indication of major discrimination against females in access to basic education and health services, the completion rate for primary school education is lower for females, and in times of economic difficulty, female students are more likely to drop out of primary school. Girls from poor rural families typically do not attend secondary school. Moreover, female-headed households, i.e., those with no male support, experience high rates of severe poverty.

10. The lack of sustained economic growth has become the primary constraint to social improvement in Kenya. In particular, economic growth has not been sufficient to generate productive employment opportunities to absorb the rapidly growing labour force. Unemployment in urban areas is

currently around 25 percent. About half of the rural population is living in poverty, and have no access to the minimum requirement of food and essential non-food commodities.

## III. POLICY OBJECTIVES AND STRATEGIES FOR 1996-98

11. The key development challenge facing the Government over the next three years will be to create the conditions for rapid and sustained growth at a level which will result in a significant reduction in unemployment and poverty. The Government's strategy to meet this challenge will be to: (a) maintain macroeconomic stability by strengthening monetary and public sector finance management, and by consolidating fiscal discipline; (b) improve the efficiency of the public sector by accelerating and streamlining reform in the civil service and public enterprises, and improving the delivery of infrastructural services; (c) enhance external and domestic competitiveness of the economy through further liberalisation of markets; (d) address the social aspects of development particularly through targeted poverty interventions and increased access of the poor to social services; and (e) eliminate corruption. The Government intends to move further away from direct participation in economic activity, and toward the provision of an enabling environment for private sector development with emphasis on policies which are environmentally friendly and which encourage labour-using growth.

## Macroeconomic Objectives

12. The Government's first priority is to maintain a stable macroeconomic framework while continuing with structural reforms necessary to accelerate economic growth. The key macroeconomic objectives for 1996-98 include: (a) achieving higher real GDP growth rising from an estimated 5 percent in 1995 to nearly 6 percent in 1998; (b) limiting the annual rate of inflation (end of period) to no more than 5 percent in 1996 and thereafter, close to the rate of inflation projected for Kenya's major trading partners; and (c) strengthening the external current account position (excluding official transfers) from a deficit of about 4.2 percent of GDP in 1995 to a deficit of about 1.4 percent of GDP in 1996 and to 0.8 percent by 1998. Gross official reserves are targeted to rise to the equivalent of 4.3 months of imports at end-l 998, up from 2.1 months at the end of 1995.

13. Stable macroeconomic conditions, liberalised markets, and more efficient operations of the strategic public enterprises are expected to enhance the level and the efficiency of private investment, and result in increased income and job creation. To achieve these objectives, Kenya will require an increase in gross fixed capital formation from 21.7 percent of GDP in 1995 to 23.2 percent in 1998. The investment recovery will be financed out of national saving, which is projected to increase from about 20 percent of GDP in 1995 to 24.5 percent in 1998.

14. Over the period 1996-98, the agricultural sector is projected to grow slightly above 4 percent per annum, with a slight decline in its share as percent of GDP by 1998. Government policies will seek to ensure that broad based rural development is promoted through appropriate investment in rural infrastructure and agricultural research and extension. The manufacturing and the service sectors are projected to grow at around 7 percent per annum, reaching 18.2 and 36.6 percent of GDP by 1998, respectively.

## Monetary and Financial Sector Reforms

15. The primary objective of monetary policy will be to maintain price stability. To achieve this objective, the Central Bank of Kenya (CBK) will seek to ensure that money supply expands at rates consistent with the growth of economic activities. The Bank will continue to rely mainly on Open Market Operations (OMO) to manage the supply of money and credit to the economy. Interest rates in such operations will be allowed to vary, as necessary, to achieve this goal. Credit to the financial institutions from the CBK will be kept low. Foreign exchange intervention by the CBK will be limited to smoothing out short-term fluctuations in the exchange rate.

16. A number of measures will be taken to strengthen monetary policy management. Accordingly, the Government will submit a Bill to Parliament by June 1996 to amend the

CBK Act and to give the Central Bank more autonomy. The Government considers this to be critical to sustain price stability. The Bill will define clearly the purposes of the Central Bank and grant it sufficient powers to discharge its responsibilities more effectively. In addition, the CBK will seek to improve its capabilities to forecast accurately and on a timely basis the movements in reserve money. The Bank will also strive to improve its intervention techniques in the money and foreign exchange markets.

17. Steps will be taken by the CBK to develop secondary markets in Treasury bills to increase the effectiveness of financial markets. Preparatory work on the legal and technical infrastructure for the introduction of Repurchase Agreement instruments (REPOs) will be undertaken in 1996. The Capital Markets Authority will also encourage the private sector to establish a central depository for Treasury bills, which would ensure an efficient delivery and payment system for the bills. An expanded role for the Nairobi Stock Exchange is envisaged, particularly through a widening of the range of financial instruments traded on the exchange and assistance in the privatisation of public enterprises.

18. To strengthen the broader financial system, the National Social Security Fund (NSSF) will be converted into an autonomous pension fund and necessary legislation will be

presented to Parliament by end-December 1996. The legislation will stipulate, *inter-alia,* that members of the Board be elected by pensioners, and that the Board members elect the chairman. The conversion will be carried out with the assistance of the World Bank and other donor agencies and will include, *inter alia*, strengthening of information technology as well as an actuarial study by an external auditor. Meanwhile, the NSSF has been instructed to invest its revenue in government securities only, except for deposits in sound and stable financial institutions which will be limited to 15 percent of NSSF's total assets. An external audit of the financially troubled Kenya National Assurance (KNA) has been completed and specific recommendations have been made for its restructuring by end-June 1996. The general insurance business of KNA will be liquidated and the life insurance business will be operated as a closed fund. This means that no new insurance will be issued and most of the existing staff will be retrenched. Any financial impact will be reflected in the 1996/97 budget. To consolidate the soundness of the banking system, no new banking licenses will be issued before end-1996 except for large new entrants, i.e., banks with capital larger than K Sh 1 billion who are judged to offer credible competition to the existing large banks. Moreover, all prudential regulations will continue to be strictly enforced.

## Budgetary and Public Expenditure Policies

19. Fiscal policy will continue to be significantly tightened with the objective of lowering domestic debt and thereby facilitating the reduction of interest rates. The overall budget deficit (on a commitment basis and excluding grants) is targeted to decline gradually from its 1994/95 level of 2.6 percent of GDP to 1.9 percent of GDP in 1995/96 and further to 1.5 percent of GDP by 1997/98. In the process, overall revenue will slightly decrease from 31.7 percent of GDP in 1994/95 to 30.9 percent in 1997/98. On the expenditure side, the programme will focus on improving the quality and the sectoral allocation of public spending, as well as strengthening of budgetary control and management. Development expenditure would be increased over the period to help rehabilitate infrastructure, while recurrent expenditure will be markedly reduced so that total expenditure would decline from 34.3 percent of GDP in 1994/95 to 32.3 per cent in 1997/98. With the projected availability of grants and external financing and assuming budgetary support from programme financing, this level of deficit will allow domestic debt to be reduced from 28.1 percent of GDP in 1994/95 to 18.4 percent in 1997/98. The retirement of domestic debt is essential to allow more credit to the private sector and a reduction in real interest rates.

20. **Tax Reform.** Steps will be taken to deepen the tax reform which is aimed at reducing the tax burden and broadening the tax base. Maximum import duties will be lowered further by July 1997, while income tax and VAT rates will be lowered to the extent compatible with the deficit target. The tax base will be broadened by eliminating many of the exemptions from taxes and reducing the scope for tax evasion. In particular, the Government will take immediate steps to do away with all discretionary import duty exemptions.

Improving tax administration will continue to be an important element of the tax reform programme. In this respect, the Government will ensure the proper functioning of the newly established Kenya Revenue Authority by improving remuneration and funding its other operations and by empowering the Authority to freely hire and dismiss staff in order to encourage diligence, honesty, and performance. To enhance controls on customs revenues, the Government has begun a systematic ex-post reconciliation of actual receipts of customs duties and those calculated by the Pre-shipment Inspection (PSI) firms.

21. **Public Expenditure Reform.** Further steps will be taken on expenditure reform involving strengthening budgetary controls and rationalising expenditures. Budgetary controls will be reinforced through increased transparency and accountability. To this end, the Government will not enter into any commitments which have not been included in the Budget and approved by Parliament. It will strictly enforce and, where necessary, strengthen procedures for the granting of public procurement contracts and for external and domestic borrowing. In this respect, no exemption will be granted in the requirement for the public tender of all contracts exceeding K Sh 10 million. Expenditures will be closely monitored on a monthly basis by the recently established unit at the Treasury, and the sanctions of the financial orders and regulations will be strictly applied to Accounting Officers in ministries and departments that violate established recurrent and development ceilings without explicit and prior written approval of the Treasury. Consistent with this, the Government will publish on a quarterly basis, the preliminary budgetary outturn. The Government will also take steps to ensure that local government expenditure processes are on a sound footing, particularly given the increased resources made available to them through the authorization of a 50 percent increase in the service rates on businesses.

22. The rationalisation of public expenditures will involve a shift in the allocation of public funds toward the Government's basic functions of maintaining law and order

and administering justice, financing broad-based education and health services, providing economic infrastructure, supporting agricultural research and extension, and protecting the environment. While recurrent expenditures will continue to be constrained, limits on the overall growth of the wage bill through civil service rationalisation, improvements in the collection of appropriations-in-aid by ministries, and the shedding of non-essential government services, will permit significant real increases in non-wage operations and maintenance expenditures, particularly for the basic functions. To this end, the Government will initiate, with assistance from the World Bank, a wide-ranging review of public expenditures during the first half of 1996. This review will be the basis for specific spending decisions in the 1996/97 to 1998/99 budgets.

23. Development expenditures (including net lending) will be increased from their current level of just over 7 percent of GDP. Full annual funding will be provided for all “core” projects and allocations to core functional areas will account for at least 75 percent of the development budget over the next three years. Shortfalls in funding will be met by reallocating funding from non-core to core projects. The Government will improve the project selection criteria to ensure that all new projects are vetted before they are introduced into the Public Investment Programme (PIP) in order to ensure consistency with likely available resources, and that no project will be included in the budget which is not contained in the PIP.

## Civil Service Reform

24. The first of three phases of the seven-year programme of the Civil Service Reform Programme, which is intended to increase the efficiency of the Service and to improve management capacity, is now underway. As indicated earlier, in order to improve the efficiency of the Service, the programme involves the reduction of positions and staff, implementation of staffing norms for all cadres, improved establishment control, rationalisation of selected ministries and pay reform. These actions will be taken consistent with budgetary resource availability. In line with the Government's previous commitments, staff reduction measures and the corresponding positions are to be reduced by 16,000 per year over 1995/96 and 1996/97, through natural attrition, voluntary retirement and position rationalisation. During the period January 1996 to June 1997, the Government will limit new hires to 3,000 per year maximum, i.e., no more than 1500 between January and June 1996 and 3000 between July 1996 and June 1997. This will imply net reductions in civil service of 20,180 over the period January 1996-June 1997.

25. In light of emerging staff shortages in certain areas, the Government will ring-fence some of the most critical and well-trained but scarce junior staff. During 1996, the Government intends to carry out staff analysis and establish staffing norms for key cadres. This, together with the results of the ministerial

staff rationalisation programmes, will enable the Government to develop a coherent programme of Civil Service rationalisation for the period 1997/98 and beyond. This program will be developed by June 1997 taking account of the medium term budgetary outlook.

26. To increase personnel control, the Government is committed to the introduction of an Integrated Personnel and Payroll Database (IPPD) system in the Service. By mid-1997, the Government will have completed the first Phase of this introduction. Similarly, by the end of 1996, modalities will have been worked out for the introduction of and implementation of performance-related pay for identified critical cadres. In addition, and as part of its effort to improve efficiency, the Government will identify key indicators for Civil Service Operations and Maintenance (O&M) requirements and give them priority in the recurrent budget expenditures beginning in 1996/97.

27. In the area of ministerial rationalisation, work has already been initiated in the ministries of Health (MOH), Finance (MOF), Lands and Settlements (MOLS), Public Works and Housing (MOPWH), Land Reclamation, Regional and Water Development (MLRRWD) and Agriculture, Livestock Development and Marketing (MOALDM). For MOH and MOALDM, implementation of these plans is underway and is expected to be completed by the end of 1996. The rationalisation of the other four ministries is expected to

be completed by July 1997. The Government intends to identify by July 1996, six additional ministries for rationalisation with emphasis on the development of staffing norms which can be applied to determine optimal staffing levels. It is envisaged that the process of ministerial rationalisation will be complete by the end of 1998.

28. During the period 1996-98, increased attention will be paid to training and human resource development in the Civil Service. Training will be geared toward the development of special skills in key areas, based on the results of the staffing norms and ministerial rationalisation. Towards this end, the Government will seek to improve physical facilities in the existing training institutions. Before the end of 1996, it is expected that all critical training needs will have been identified and prioritised.

## Public Enterprise Reform

**29.** The Government considers the private sector as the only basis for sustainable long term economic growth. Accordingly, it will progressively reduce the role of the public sector in the economy through rationalisation of public sector firms and an accelerated programme of privatisation.

30. **Rationalisation of Major Parastatals.** The Government intends to implement major rationalisation and divestiture programmes for each of the key parastatals. In so

doing, the Government will seek to increase the role of the private sector through direct participation as well as through divestiture of non-core activities. Furthermore, tight budgetary controls will be enforced on the parastatals. This will be achieved by charging market rents for use of lands held by the Government, applying a 2 percent fee to any new loan guarantees provided by the Government, requiring parastatals to be current on their financial obligations, and eliminating any existing arrears within the next three years.

31. **National Cereals and Produce Board.** The Government will by end-1996 transform the National Cereals and Produce Board (NCPB) into a commercially viable entity free to make independent commercial decisions. Experts will be engaged for this purpose. The experts are expected to begin work by June 1996, based on terms of reference agreed with the World Bank. Principles governing this commercialisation, including expanding the private sector role in maize marketing, and the interim operating rules for NCPB have been finalised.

32. **Kenya Ports Authority.** To improve the efficiency of Kenya Ports Authority (KPA), the Government has requested Singapore Port Authority (SPA) to manage and operate the container terminal at the port of Mombasa. SPA has agreed in principle, and the necessary contract will be signed before the end of March 1996. KPA will also at that time have completed the re-negotiation for the two ten-year equipment

maintenance contracts it entered into in 1994, limiting the duration of these contracts to five years and establishing performance guarantees and penalties. A performance contract between the Government and KPA will be completed before April 1996. The contract will include arrangements to implement the recommendations of the ongoing staff rationalisation study.

33. **Kenya Railways Corporation. A** programme for the restructuring of Kenya Railways (KR) which has already been initiated will be accelerated early in 1996, based on the paper to be considered by Cabinet in February 1996. It will include the separation of passenger and freight services, the discontinuation of loss-making services, the contracting out of locomotive maintenance, the divestiture of marine services, and staff reductions. The maintenance contracts will be signed by August 1996 and staff numbers will be reduced to 14,500 by the end of **1996.** A performance contract will be entered into before the end of May 1996.

34. Kenya **Posts and Telecommunications Corporation.** The Government will issue, early in 1996, a policy statement spelling out the privatisation programme for Kenya Posts and Telecommunications Corporation (KPTC). Legislation will be presented to Parliament in March 1996 seeking to split KPTC into three separate entities: posts, telecommunications, and a regulatory authority. If approved, the three entities will be established by December **1996.** The Government will open

to outside investors at least 30 percent of the capital of the new telecommunications entity through the participation of a strategic investor and through public flotation. The entity will also engage in joint ventures with private investors in activities such as cellular telephones. As part of this process, KPTC has recently liberalised telecommunication services beginning with pay phones and Very Small Aperture Terminals (VSAT) for private operators. KPTC will also divest its non-essential services including workshops and buildings by September 1996.

35. **Power Sector Companies.** Legislation is now being prepared to separate the regulatory and commercial functions of the power sector, facilitate restructuring of the sector and promote private investment. This will be presented to the Parliament by the middle of 1996. An action plan is also being formulated which will provide for the commencement of the separation of generation, transmission and distribution, and articulate the reforms in the organisation, management and financial structure of the *Kenya Power and Lighting Company* (KPLC) and other power companies. The implementation of the action plan will commence in June 1996. Performance contracts for all power sector parastatals will be entered into for implementation commencing before the fourth quarter of 1996. Early in 1996, bids will be invited for investment by independent private producers in power generation.

36. **Institutional Arrangements. To increase** managerial autonomy in public enterprises, a Government Order will be issued early in 1996 exempting key parastatals (excluding Kenya Railways, which is already exempted, but including Kenya Airports Authority) from provisions of the State Corporations Act. The Ministry of Finance has also begun filling its staff positions charged with monitoring the reform programme.

## Privatisation

37. The Government aims to complete by the end of 1997 the divestiture of [1] all remaining (96 entities) "non-strategic" enterprises . This will be done in two roughly equal installments. In addition, in 1996 work will be initiated on the divestiture of three formerly strategic enterprises: Kenya Pipeline Corporation, Kenya Petroleum Refineries and Nyayo Bus Corporation. The Government is progressively reducing its holdings to a modest minority shareholding in the National Bank of Kenya and Kenya Commercial Bank.

38. The Government will take steps to ensure access for a wide spectrum of Kenyans in the ownership of enterprises to be divested. In order to build and maintain public confidence in the programme, the Government is committed to ensuring

*'Privatisation" is understood to mean that the Government (including its various departments, ministries, holding companies, agencies, etc.) has divested its holdings in the firm to 30 percent or below the blocking share as stipulated in the firms' articles of agreement.*

the utmost possible transparency in the implementation of divestitures. To achieve this, where shareholders do not hold clearly established pre-emptive rights, the Government will employ competitive bidding using transparent procedures: (i) firms (or their assets) to be sold will be widely publicized in advance; (ii) pre-qualification criteria and ranking methodology will be clearly publicized with the call for bids; (iii) bids will be opened publicly; and (iv) results will be published at the conclusion of each sale listing the terms of sale, the offers received, and the price at which the sale took place. Quarterly reports will be prepared and published on the implementation of the privatisation programme and on the privatisation proceeds and their uses. Semi-annual audits on the privatisation proceeds and uses will also be prepared and made public.

## Market Liberalisation

**39. Trade Reform.** The Government will continue with the following process of trade and investment liberalisation. Import tariffs will be further realigned, with the aim of achieving by July 1997 no more than three non-zero rates, and a lower trade weighted average tariff. The discriminatory elements of the supplementary levy on sugar will be eliminated by December 1996. The suspended duty on petroleum imports, introduced in November 1994 to give temporary protection to Kenya Petroleum Refineries Limited following the petroleum market liberalisation, will be eliminated by October 1996, contingent on the completion of the LPG import unloading pipeline (see para 54). Specific duties on cereal imports will be abolished by end-l996. By that time anti-dumping legislation consistent with the World Trade Organisation (WTO) rules will be presented to Parliament, and anti-dumping duties on cereal imports will be imposed in accordance with the law. The Government will also work with Uganda and Tanzania, under the framework of the Permanent Tripartite Commission for East African Cooperation, toward an eventual goal of an East African common external tariff and harmonized investment regulations, as well as a more active use of regional currencies.

40. Given its commitment to export-oriented growth, the Government intends to implement a strategy for industrial development that is intended to develop and diversify Kenya's industrial exports . The strategy will focus on creating the conditions to encourage private investment in activities where Kenya could be competitive. Underpinning this strategy will be a broad based effort, through appropriate training and incentives, to make all relevant Government agencies active promoters of investment and trade. The policy instruments to enable such growth will include simplification of licensing and tax regulations and procedures, and provision of improved infrastructure services. Effective enforcement of the low and simple tariff structure will reduce uncertainty and promote investment in areas where Kenya has a comparative advantage.

41. **Domestic Market Liberalisation.** The Government will undertake further reforms to ease restrictions on business entry and operations while putting in place appropriate safeguards against anti-competitive behavior. This will be achieved by rationalisation and a reduction in the number of national and local fees and licenses required for new businesses, and through minimising restrictions on retail and wholesale trade and investment under various legislation. Actions on this front will be taken within the context of reforms of the fiscal base of local authorities. The Government is also committed to taking corrective measures to ensure that farmers, consumers and traders benefit from a liberalised market. In this respect, the liberalisation of maize marketing and the establishment of a competitive seed industry will be crucial. To speed up resolution of commercial cases, the Government intends to introduce additional courts in major towns.

## Sectoral Policies and Programmes

42. **Agriculture.** The main aim of agricultural sector policy will be to accelerate agricultural growth, increase small-holder productivity, and expand rural employment. With the substantial deregulation of the domestic markets for all agricultural commodities, this objective will be pursued under a liberalised system where the private sector plays the key role in production, marketing and processing. The

Government has already liberalised the seed subsector; additional measures will be taken to strengthen the subsector, including the establishment of financially sustainable breeder and foundation seed units at the research centers of KARI, and the improvement of plant health, quality and quarantine services and facilities through the operationalisation of the Kenya Plant Health and Inspectorate Services (KEPHIS).

43. The Government is also taking steps to improve the operations of Kenya Cooperative Creameries (KCC), with a view to improving its financial viability and enhancing the farmers' role in the management of the affairs of the organization.

44. Consistent with these changes is the proposed restructuring of MOALDM which will be completed by the end of 1996. This will reorient the role and strategic functions of the Ministry so as to effectively facilitate private sector initiatives, with emphasis on providing strengthened research, extension and other essential services to farmers. A number of services, such as tractor hire and some veterinary services, will be privatised and cost recovery introduced for others. KARI, which plays an important role in the generation and dissemination of knowledge and related technology, will also be restructured durin g 1996/97 within the context of the joint donor financed Second National Agricultural Research Project (NARP II). This restructuring will include the review and

streamlining of user charges in order to reflect acceptable cost-sharing and cost-recovery in the financing of research. To strengthen the application of science and technology to agricultural development, the existing legislative framework will be reviewed; in this respect, a review of the Science and Technology Act (Cap.250 ) has already been initiated.

45. Food security is of paramount concern to the Government. To this objective, the Government will maintain a strategic maize reserve stock of up to 3 million 90-kilogram bags and will develop rules governing its management. While it is expected that the actions of private traders will serve to stabilize the maize market in most years, under exceptional situations, the Government will supplement these private efforts to reduce uncertainty and ensure food security by financing purchases and sales of maize.

46. Environment. The National Environmental Action Plan (NEAP), which was formally adopted by the Government in June 1994, sets the framework for dealing with the crucial urban, rural and coastal environmental problems which need to be urgently addressed. Since its completion, the challenge has been to translate NEAP's broad concerns about environmental management into an operation programme of effective policy, legislative and institutional action. The Government will soon be presenting to Parliament, as a Sessional Paper, a comprehensive environmental programme.

An action plan to operationalise this programme, including the establishment of an institutional framework, will be initiated before the middle of 1996. The Government is currently preparing an environmental legislation which, after broad-based consultation, will be presented to Parliament by the end of the third quarter of 1996. It is the Government's intention to establish a Land Use Commission to address land tenure and land use policy issues, with a view to improving sustainable agricultural productivity and the food security situation, as well as in ensuring that biodiversity considerations are properly considered in land-use decisions.

47. The Government is particularly concerned about the state of the woodlands. The decline in areas of indigenous high forests and the degradation of biodiversity and forest product resources within them has reached critical levels. The use of woodlands in arid and semi-arid lands as grazing areas and wood fuel continues to accelerate. Industrial plantations have been inadequately restocked and lack production-oriented management. The Government's Forestry Policy Statement addresses these various concerns, particularly inadequate restocking which is addressed by requiring loggers to replant clear-felled plantations. The Policy Statement will be presented as a Sessional Paper to Parliament in March 1996. Necessary supportive amendments to the Forest Act will be presented to Parliament in September 1996.

48. The Government is in the process of updating the policy on wildlife conservation and management (as contained in Sessional Paper No. 3 of 1975) and the Wildlife Conservation and Management (Amendment) Act of 1989 to respond to changing conditions and objectives of wildlife and biodiversity conservation. The new policy framework centers on three main goals: (i) conserving of biological diversity and representative indigenous ecosystems; (ii) promoting environmentally sustainable tourism; and (iii) promoting compatible land use in priority biodiversity areas, and channeling the benefits thereof to the local communities. A revised policy and legislation will delineate the roles and responsibilities of the Kenya Wildlife Service and of other Government and non-Government stakeholders in the implementation of this participatory approach. The draft policy is being prepared by the Kenya Wildlife Service and is expected to be approved by the middle of 1996, with the revised legislation to be presented to Parliament by the end of 1996.

49. **Road Transport.** The Government recognizes that inadequate maintenance over many years has led to a significant deterioration in the road network. The introduction of a special levy on motor fuels in 1994 to be earmarked for road development and maintenance was a major step to deal with this problem. The activities to be financed by the fund are contained in the relevant Act. The Government will also

ensure that at least 50 percent of the funds required for routine and periodic road maintenance (including urban areas) will be provided in the budgetary allocations in 1995/96. This level will be progressively raised to fully finance routine and periodic road maintenance by the turn of the century.

50. A strategic plan for the road sector is now being prepared for approval by the Government in June 1996, and outlines the framework for: (i) capacity building and increased use of the private sector in both roads maintenance and construction; (ii) plans for provision of adequate and sustainable funding for road maintenance; (iii) provide guidelines for transparent management and use of the fund; and (iv) setting priorities for roads investments.

51. **Water.** Draft legislation amending the Water Act will be presented to Parliament to address concerns regarding national water resources management and planning. A National Water Policy Paper is also being prepared for Government approval. A comprehensive investment plan for the rehabilitation and extension of existing water supply schemes, many of which are in poor condition as a result of inadequate maintenance by financially weak operating agencies, has also been recently prepared and is now being implemented. The low level of cost recovery has been a major factor contributing to inadequate maintenance. To address this, the Government will progressively implement its policy

of charging urban consumers water tariffs sufficient to cover capital amortization and O&M costs, while setting rural tariffs to cover O&M costs only.

52. **Energy.** The implementation of a sound policy framework and an appropriate investment programme to address the increasingly serious shortfalls in power supply is of high priority to the Government. The Government has, therefore, prepared a rolling five-year least cost investment programme comprising urgent investments in power generation, transmission and distribution as well as investments to facilitate importation of liquid petroleum gas (LPG) and the transportation of other petroleum products. Construction of five power stations, two of which will be developed and operated by the private sector, will add a total of 338 MW to existing capacity at the turn of the century. The Government attaches great importance to rural electrification and is therefore also reviewing cost-effective options for providing electricity to the rural areas, including policies to encourage the use of renewable energy resources (e.g. wood fuels, photo-voltaics and windmills).

53. To mobilize resources required to supplement external borrowing in financing the power sector investment programme and to encourage economic consumption of electricity, tariffs will be adjusted to ultimately cover long-run marginal costs (LRMC). As an interim measure, tariffs

will be raised to 75 percent of LRMC by the beginning of June 1996 following resolution of outstanding administrative/ legal issues. An update of the November 1993 Tariff Study, to be completed in the third quarter of 1996, will provide the basis for the Government to establish the magnitude and phasing of further adjustments required to achieve LRMC after taking due consideration of the cost of power from independent power producers and the sector's overall financing requirements.

54. Deregulation of the procurement, distribution and pricing of petroleum products was announced in October 1994. The objective of the deregulation was to create a more competitive environment which would improve the availability of petroleum products and lower prices in the long-term. Because of the lack of import facilities for LPG, temporary (two year) arrangements were made for: (i) the annual processing of about 1.6 million tons of crude oil by the refinery to ensure production of about 250,000 tons of the current annual demand for LPG; and (ii) protection of the refinery by levying duties on imported products. To achieve the full benefits of deregulation, removal of the following existing constraints to competition is required: (a) urgent construction of LPG import facilities comprising pipeline connection between the Shimanzi Oil Terminal and the new storage tanks and rail/road loading facilities to be constructed at Mombasa; (b) review and implementation of options for continued use

of the petroleum products pipeline as a common carrier; and (c) installation of a product testing laboratory in Mombasa. Part of the LPG import facilities, to be constructed on a priority basis, include the LPG unloading pipeline from Shimanzi Oil Terminal to Mombasa Refinery Compound wall and the vapour return line from that point. As indicated in paragraph 39, suspended duties on petroleum imports will be completely removed by October 1996, contingent on completion of the LPG import unloading pipeline.

55. **Population.** Kenya has been pursuing an active population policy. While there has been remarkable success in reducing fertility over the last decade, the population of Kenya is still growing at a high rate of around 3 percent per annum. Continued emphasis will thus be placed on family planning service delivery to achieve higher contraceptive use and on the promotion of programmes such as social marketing and community-based delivery to address demand for these services. To ensure better coverage of the population in the delivery of these services, greater reliance will be placed on private and other non-government entities. To reflect this, the Government is in the process of restructuring the National Council for Population and Development (NCPD) to de-emphasize its role in service delivery and to turn it into a policy-making, coordinating and advocacy entity. Over the longer run, following the U.N. Cairo Conference on Population, Kenya will emphasize the integration of

population policy into the overall policy framework. This will include specific interventions in primary education and reproductive health, particularly for disadvantaged families.

56. **Health.** The Government is firmly committed to major reforms in the health sector. The recently prepared Health Policy Framework sets out a comprehensive approach to improve the quality and availability of health services, including specific measures to be undertaken over the next three years, namely, (i) the adoption of a strategy to reduce the prevalence of disease among the population; (ii) the decentralization of financial and administrative authority to districts, beginning in the first half of 1996; (iii) the shifting of a larger share of the financial burden of curative care from the Ministry of Health's (MOH) budget to insurance schemes of the National Hospital Insurance Fund (NHIF) [1] and competing private financial entities; (iv) an increase in resources devoted to the completion, maintenance and repair of existing facilities and equipment; (v) the strengthening of key health management information systems at the district level; and (vi) the restructuring of the MOH to support these reforms. The budget of the MOH will continue to reflect the shift to preventive health care away from hospital care, particularly Kenyatta National Hospital where efforts are underway to improve its efficiency and financial autonomy. The Government is committed to limit the share of MOH's

*'The Government is currently reviewing the scope for expanded enrollment and coverage in the NHIF The new draft Bill of the NHIF reflects an intention to include self-employed and the Jua Kali (Informal) sector.*

budget to the hospital to 12 percent beginning 1996/97, subject to adequate progress being made in ensuring other facilities are in place to serve the Nairobi area. Efforts to improve the quality of health services under constrained budgetary conditions requires that funds be mobilised through increased user charges. The contribution of user charges will therefore have to be raised from their current level of 12 percent of MOH's non-wage recurrent budget to about 18 percent in 1997/98.

57. To address the problem of AIDS and other sexually transmitted diseases, the Government is implementing a National AIDS and Sexually Transmitted Disease Control Programme (NASCP), and has prioritized capacity building at national and district levels to integrate AIDS into the development plans. Steps are also being taken to minimize the socio-economic impact of HIV/AIDS and to strengthen HIV/AIDS epidemiological surveillance. A Policy Paper on AIDS is being finalised, which includes appropriate institutional arrangements to coordinate the implementation of the NASCP. As part of a pilot project supported by donors, non-governmental organisations (NGOs) are beginning to play a key role in control and prevention of sexually transmitted infections. All annual district health plans include funds earmarked for NGO activities, and the authority to incur expenditures has been delegated to the District Medical Officer for ten districts and municipalities.

**58. Nutrition.** Recent evidence points to high rates of infant mortality and some deterioration in already adverse child nutritional status indicators. Anaemia and malnourishment among women are also significant, although the precise extent is unknown. To reverse these trends, the Government will review all nutritional interventions to shift its financing to more cost-effective programmes targeted at infants, pre-school children and pregnant women, particularly in rural areas, with selected interventions for older children in poor districts. This will include examining the role of communities in financing the school feeding programme to ensure its sustainability, assessing and monitoring the nutritional situation, preventing specific micro-nutrient deficiency, improving young children feeding, and caring for socially and economically deprived nutritional vulnerable groups.

59. Education. The Government's principal objectives in this sector over the next three years will be to reverse the recent declines in primary and secondary enrolment and completion rates, particularly of girls from poor households, and to improve the quality of education at all levels. This will involve a reallocation of public expenditures from university education toward disadvantaged students in primary and secondary education, and an increase in the effectiveness of these expenditures. Means-tested bursary programmes to secondary schools will be expanded in 1996/97. The Government will also work out arrangements and plan to introduce a bursary programme directed at girls in primary schools--especially

those at the upper primary level in rural and slum areas. Initiatives for pre-primary education and early childhood development will also be strengthened. To improve the quality of education, the Government will maintain its policy of not recruiting new untrained teachers at the primary level.

60. The Government has in place policies to encourage the participation of the private sector in the establishment and. operations of educational institutions. The Government is also encouraging the sector to enhance its participation in the production of all educational materials. To this end, the capacity of the Kenya Institute of Education (KIE) will be strengthened and a review of policies on publishing educational materials prepared by the Institute will be carried out, with the aim of enabling the private sector to participate effectively with the two parastatals publishing educational books, that is, Jomo Kenyatta Foundation (JKF) and Kenya Literature Bureau (KLB).

61. Enhancing the efficiency and responsiveness of educational institutions through the decentralisation of decision-making will be an important objective. This will be achieved by increasing the capacity, responsibility and accountability of local authorities and of boards and committees of educational institutions for funding arrangements and management performance. In this context, the Government is establishing Provincial Education Boards,

strengthening District Educational Boards and reviewing and rationalising the responsibilities of the Teachers Service Commission (TSC). Changes at TSC will involve decentralising its functions more appropriately at the school or local level and strengthening TSC's capacity to manage more appropriately those handled centrally. In addition, the Education Acts and regulations are being reviewed and a plan of action prepared to decentralise management and financial decision-making, permitting councils and boards of educational institutions to determine fees from 1996/97.

62. Consistent with the decentralisation strategy, determination of fees to supplement Government grants to meet especially the actual cost of tuition, accommodation and catering, will be fully devolved to University Councils for the 1996/97 academic year. Reforms have also been recently undertaken in the administration of Student Loan Schemes. The Higher Education Loans Board (HELB), which has now taken over the functions of the former Student Loan Scheme Unit from the Ministry of Education (MOE), will make full use of its enhanced legal powers for loan recovery. The Board intends to progressively increase the role of commercial banks in lending to students, initially as contractors for loan disbursements and recovery, with the long-term aim of encouraging them to accept some portion of the repayment risk.

63. In the area of skills training, the Government, through the Ministry of Research, Technical Training and Technology (MRTT&T) aims at improving the capacity of Kenya's technical training institutions. This will be done through the updating of equipment in the training institutions as well as the improvement of their management. In addition to these efforts, the Government, through the MRTT&T, plans to develop a national Skills Training Strategy through a process involving all key stakeholders.

## Women in Development

64. The Government will continue its efforts to ensure that women participate and benefit equally from the development process through their integration into mainstream activities. Recent studies show that women are not grossly discriminated against in Kenya, but there are subtle differences which have a cumulative effect on the welfare of women, such as drop-out rates of primary education, and low enrollment and completion rates for secondary and higher levels of education. Women are also disadvantaged in their access to land, and are particularly vulnerable in the event of divorce, separation or being widowed.

65. Efforts to improve opportunities for women will continue to focus on increasing their access to education and health. Given the increasingly important role played by

women in the rural sector, the Government will also step up its efforts to redesign agricultural extension services to provide information directly relevant and accessible to rural women. The budget-neutral recruitment of women as extension staff, use of women's groups to disseminate technical information, and integration of home economic messages and information on appropriate labor-saving technologies are important components of the latter. The Government will initiate ways and means to improve access of women to productive resources such as agricultural inputs, water, fuel wood, credit and skills. Towards this goal the Government will support rural water supply systems that feature community participation and NGO involvement, and that can significantly improve the quality of life of women and the community as a whole. In addition, the Government will ensure that women in the small and medium enterprise sectors have access to existing skills upgrading training of the Jua Kali (Informal Sector) programme so as to address their specific needs.

## Youth in Development

66. About 15.5 million people or 60 percent of Kenya's population are young people below twenty-five years of age. Of this total, around 5 million are below 6 years, over 5 million are in primary schools, about 600,000 in secondary schools and about 50,000 are in local and overseas universities. There are also well over 4 million youths outside the school system, either as unemployed or undertaking small-scale income generating activities, in both rural and urban areas.

67. The Government recognises that the most important resource is its people. It is necessary therefore that steps are taken to give the youth correct guidance so that they may grow into useful citizens and leaders of tomorrow. More importantly, steps must be taken to harness the energies and talents of the youth by directing them into productive activities. Towards this objective, the Government will in the period 1996-98, strive to develop appropriate programmes tailored in particular to help alleviate the unemployment problem among the youth. This will involve designing and funding of youth development programmes and projects through Youth Self-Help Groups which already exist in both rural and urban areas. The District Development Committee (DDC) mechanism will play an important role in this regard.

## Targeted Poverty Interventions

**68.** While the policies in support of growth and the social sectors are designed to ensure that the benefits of development reach the poor, targeted interventions will be required to provide income support to those who cannot wait until the growth process gathers full steam as well as those who cannot readily participate in it because of special handicaps, such as geographical isolation. The most important targeted interventions will be in rural areas where the need for wage employment is most acute. In this respect, the Government will allocate funds to expand its intensive rehabilitation and maintenance of minor roads, given the importance of these roads and their current state of disrepair. Flexibility will be built into the scheme to enhance it during drought years. The Government will also develop community-based modalities for providing support to the rehabilitation and maintenance of water projects, including boreholes, water pans and dams, and will seek to establish a pilot water fund in 1997. Special attention is being given to the poor in arid areas through programmes designed to meet their basic needs and to increase their integration with the rest of the economy, Special emphasis will be placed on the rehabilitation of stock routes on a selective basis, improvements in drought management and relief, and on the immunisation and school health and feeding programs.

69. Sanitation and safe water needs of the urban poor requires urgent attention. The Government will take steps to deal with these needs by licensing a larger number of kiosks and by supporting, financially and technically, community-based initiatives in waste removal and sanitation. To help alleviate the related shelter problem in urban areas, access to low-cost housing will be encouraged through cooperative societies.

70. The informal sector is the main source of income for about a quarter of rural households and possibly more in urban areas, and energising the sector is an effective means of reducing poverty. It is, however, constrained by limited access to formal credit and laws and regulations which often lead to

harassment. To help alleviate the credit constraint, the Government will encourage the expansion by donors of micro-enterprise schemes, and will seek to ensure that women groups in both urban and rural areas are specifically targeted. In order to address sector needs, the Government has mounted a national Jua Kali programme aimed at addressing issues related to safe working sites, skills upgrading, access to power and water, access roads, land allocation, and marketing. This programme has helped many artisans gain access to these services although it has been constrained by financial limitations. The Government aims at expanding and intensifying the programme which, as well as emphasizing addressing the above issues, will seek support of donors to expand and improve delivery systems of micro-enterprise lending schemes and involve a review of laws and regulations inhibiting the sector and undertaking appropriate amendments.

## IV. DATA REPORTING AND STATISTICAL ISSUES

71. The quality of economic data base is generally satisfactory in Kenya. In the medium term, the Government will: (i) strengthen the Central Bureau of Statistics and allocate sufficient financial resources to construct a quarterly composite index of economic activity, re-base constant price national accounts data, and compile a producer price index; (ii) take measures to improve the timeliness of the recording of reliable economic statistics, especially those relating to

balance of payments and external financing of the government expenditure and the real sector.

## V. EXTERNAL FINANCING REQUIREMENTS

72. The current account balance, excluding official transfers, is projected to show a cumulative deficit of about US$310 million over the period 1996-98 (Table 2). Together with the scheduled amortization payments and the targeted build-up of international reserves, Kenya's external financing requirement is estimated at about US$2.4 billion over the three-year period. It is expected that private capital inflows, mainly from foreign direct investments and short-term trade credits, would amount to around US$300 million. Potential project financing of US$1.5 billion is identified from bilateral and multilateral donor agencies, in the form of grants (US$O.4 billion) and concessional loans (US$ 1.1 billion) subject to confirmation at the Consultative Group meeting. After taking into account already identified external financing, a financing gap of about US$550 million remains for the period 1996-98. The gap for 1996 is estimated at US$224 million. It is expected that the gap will be closed by disbursements under a World Bank Structural Adjustment Credit (SAC) and associated International Development Association (IDA) reflow, disbursements under the IMF Enhanced Structural Adjustment Facility (ESAF) and commitments made at the March 1996 Consultative Group meeting.

73. At end-1995, the external debt of Kenya's public sector amounted to about US$6.4 billion, or about 80 percent of GDP. Kenya borrowed extensively on non-concessional terms in the second half of the 1980s; since that time, new borrowings have been on concessional terms. In present value terms, in 1995 the external debt amounted to 191 percent of exports and the external public debt service was equivalent to 24.9 percent of exports of goods and services. Consistent with the lower current account deficits associated with the medium term balance of payments scenario described above, the external debt will decline as a percentage of GDP. In addition, as the older non-concessional debt is being repaid and new financing is provided on concessional terms, the overall concessionality of the external debt is expected to increase over the medium term. As a result of these two factors, the present value of the debt will decline to 83 percent of exports by 2005 along with the ratio of debt service payments to exports of goods and services which would fall to less than 10 percent.

## POLICY MATRIX
## SUMMARY AND TIMETABLE OF POLICY ACTIONS, 1996-1998

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| Overall objective of poverty reduction via maintaining a stable, low inflation macro-economy, while continuing with structural reforms necessary to revive GDP growth to 5-6 percent per annum in 1996-1998. | Policies that encourage environmentally sustainable, labor intensive growth supplemented by public expenditure programmes focused on the financing of basic social services targeted at the poor. | 1996-1998 |
| Monetary & Financial Sector Policies | | |
| Monetary policy to maintain price stability | 1. NDA to be reduced substantially with limited foreign exchange market intervention. Broad money to grow in line with nominal income; sharply curtail net credit to the Government. | 1996 |
| | 2. Present the Bill amending the CBK Act to Parliament. | June 1996 |
| Financial sector reform | 3. Submit legislation to Parliament converting the National Social Security Fund (NSSF) into a pension fund. | Dec 1996 |
| | 4. Limit the level of deposits in sound and stable financial institutions to 15 per cent of NSSF's total assets. | Jan. 1996 onwards |
| | 5. Instruct NSSF to invest its ftmds in Government. securities only until pension fund is established. | Jan 1996 onwards |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| | 6. Develop secondary markets in Treasury bills. | 1996 |
| | 7. Encourage establishment of a central depository for Treasury bills by the private sector. | 1996 |
| | 8. Facilitate an increase in the range of financial instruments traded at the NSE. | 1996 |
| | 9. Improve CBK's technical capacity to intervene in domestic money and foreign exchange markets. | 1996 |
| | 10. Institute restructuring of KNA | June 1996 |
| **Budgetary and Public Expenditure Policies** | | |
| Fiscal policy will be significantly tightened, thereby allowing substantial lowering of domestic interest rates to spur economic activity. | 1. Reduce the overall budget deficit (on a commitment basis but before grants) to 1.9 percent of GDP in 1995/96. The budget deficit will be reduced further to 1.5 percent of GDP by 1997/98. | 1995/96<br>1997/98 |
| Broadening of tax base and reduction of rates and efficient tax collection. | 2. Strengthen the management of the Kenya Revenue Authority. | Continuous |
| Safeguard customs revenue. | 3. Treasury to ensure receipt of ex post reconciliation reports of PSI agencies. | Immediately and continuous |
| Tighter expenditure control. | 4. Sanction Accounting Officers in ministries that violate established recurrent and development ceilings without explicit, prior written (PS/Treasury) approval. | 1996-98 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| | 5. All expenditures to be included in the budget and approved by Parliament. No exceptions to be granted to requirement for public tendering of all contracts exceeding K Sh 10 million. | 1996-1998 |
| | 6. Local government expenditure processes to be strengthened and rationalised. | 1996-1998 |
| Rationalize public expenditure to maximize impact on economic growth and poverty reduction. | 7. Increase expenditure on O&M, especially on areas covering the basic functions of Government, by restraining personnel expenses, improving collection of recurrent appropriations in aid, and eliminating non-essential Government services as identified in the Public Expenditure Review (PER). | 1996-1998 |
| | 8. Increase regular development expenditures from current level of roughly 7 percent of GDP. | 1996-1998 |
| | 9. Provide full ammal funding allocation for all "core" projects with at least 75 percent of the development budget for spending in core functional areas. | 1996/97 onwards |
| | 10. Initiate detailed PER with World Bank support | Feb., 1996 |
| | 11. Introduce project approval authority in Ministry of Finance and Planning to ensure that Public Investment Programme (PIP) is consistent with availability of budgetary resources. | From 1997-98 budget cycle |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| **Civil Service Reform** | | |
| Undertake civil service reforms to increase the efficiency of the service and to improve public sector management capacity. | 1. Reduce staff levels and their corresponding positions by a further 16,000 a year. New hiring to be restricted to no more than 1500 during January - June 1996 and 3000 during July 1996 - June 1997. | 1995/96 -- 1996/97 |
| | 2. Finalise a rationalisation programme with new targets for civil service reductions for 1997/98 and beyond. | June 1997 |
| | 3. Introduce first phase of IPPD System for Civil Service | June 1997 |
| | 4. Complete implementation of rationalisation plans for Ministry of Health (MOH) and Ministry of Agriculture, Livestock Development and Marketing (MOALDM). | Dec. 1996 |
| | 5. Complete rationalisation of the Ministries of finance (MOF), Lands and Settlements (MOLS), Public Works and 'Housing (MOPWH), and Land Reclamation, Regional and Water Development (MLRRWD) . | July 1997 |
| | 6. Identify six (6) additional ministries for rationalisation. | July 1996 |
| | 7. Complete rationalisation of the six additional ministries. | Dec. 1998 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| **Public Enterprises** | | |
| Achieve commercially viable operation of strategic public enterprises with. Government and management relationship based on arms-length, monitorable performance criteria. | 1. Exempt KAA, KPA, NCPB, KPTC and KPLC from provision of the State Corporations Act to enhance managerial autonomy. | March 1996 |
| | 2. Eliminate indirect subsidies to parastatals by: applying 2 percent guarantee fee to all new guarantees provided by the Government and charging parastatals market rents on use of land leased from Government. | June 1996 |
| | 3. Commence implementation of action plan to eliminate parastatal cross debts and parastatal debts to Treasury. | June 1996 |
| Complete divestiture of parastatals, while ensuring that public confidence is maintained by transparency in the process of privatisation. | 4. Complete divestiture of remaining parastatals from original list in two roughly equal tranches. | Dec. 1997 |
| | 5. Complete divestiture proceedings for Nyayo Bus Corporation. | Dec. 1996 |
| | 6. Institute divestiture procedures for Kenya Pipeline Corp. and Kenya Petroleum Refineries. | June 1996 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| | 7. Reduce Government's position in National Bank of Kenya to below 25 percent. | June 1996 |
| | 8. Reduce Government's position in Kenya Commercial Bank to less than 50 percent. | Dec. 1996 |
| | 9. Commence publication of: (i) regular quarterly reports on the implementation of the privatisation process; (ii) quarterly reports on use of privatisation proceeds; (iii) semi-annual audits on use of privatisationproceeds (June 1996; and (iv) sales notices on completion of sales. | March 1996 |
| | 10. Adopt competitive bidding for all divestitures with fully transparent procedures. | March 1996 |
| **External Policies** | | |
| To achieve a sustainable external current account position over the medium-term. | 1. Progressively reduce import tariff to no more than three non-zero rates, and a lower trade-weighted average tariff. | July 1997 |
| | 2. Eliminate suspended duty on petroleum imports introduced in November 1994. | October 1996 |
| | 3. Abolish specific duties on cereal imports. Present to Parliament anti-dumping legislation consistent with WTO rules and impose anti-dumping duties on cereal imports in accordance with the law. | Dec. 1996 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| **Domestic Market Liberalization** | | |
| Ease restrictions on business entry and operations. | 1. Reduce number of national and local fees and licenses for new start-ups and minimize restrictions on retail and wholesale trade under Trade Licensing Act. | 1996-1998 |
| **Agricultural Policies** | | |
| To accelerate agriculture growth, increase smallholder productivity and expand rural off-farm employment as well as improve food security. | 1. Complete rationalisation programme for KARI. | June 1997 |
| | 2. Submit to Parliament revisions to the Cooperative Act defining new and more independent role of cooperatives in a liberalised agricultural sector. | March 1996 |
| Establish competitive seed industry. | 3. Implement actions to improve operations of KCC. | March 1996 |
| | 4. Issue policy statement related to the liberalisation of the seed market. | March 1996 |
| | 5. Establish financially self-sustaining breeder and foundation seed units at KARI's research centers and improve public plant quarantine facilities to enable import and export of seed. | 1996 |
| Ensure longer term sustainability of liberalised maize market. | 1. Issue letter of invitation for proposals for provision of services to undertake commercialisation of NCPB. | March 1996 |
| | 2. Experts in place to prepare and implement commercialisation program of NCPB. | June 1996 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| | 3. Establish NCPB as a commercial entity, free to make independent commercial decisions. | Dec. 1996 |
| | 4. Establish modalities for maintenance of strategic maize reserve stock and market interventions. | Dec. 1996 |
| | 5. Implement agreed operating rules for NCPB during transition period. | 1996 |
| **Environment** Government to focus on implementation of the NEAP. | 1. Initiate the implementation of an action plan to operationalise environmental policies articulated in the Comprehensive Environmental Policy Sectoral Paper. | June 1996 |
| | 2. Present to Parliament necessary environmental legislation, following broad-based consultations. | Sept. 1996 |
| | 3. Present Forestry Policy Paper to Parliament | March 1996 |
| | 4. Present to Parliament legislative amendments to Forest Act based on GOK approved Forest Policy Statement. | Sept. 1996 |
| | 5. Complete and begin implementation of Kenya Wildlife Service's land use policy study. | June **1996** |
| | **6.** Present to Parliament revised wildlife legislation. | Dec. 1996 |
| | 7. Establish Land Use Commission. | Dec. 1997 |

| **OBJECTIVES AND POLICIES** | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| Infrastructure, Transport and Communications | | |
| Roads:<br><br>Arrest deterioration of the road network | 1. Adopt strategic plan for the road sector that includes defining activities to be financed by the road maintenance levy to address the maintenance, rehabilitation and upgrading of roads, including procedures for transparent management of the road fund and mechanism to ensure that all the levy funds are used effectively for road maintenance. | June 1996 |
| | 2. Provide budgetary allocations for at least 50 percent of funds required for routine and periodic road maintenance. | 1996/97 |
| | 3. Progressively raise budgetary allocation to finance full routine and periodic road maintenance by 2000. | 1996-2000 |
| Railways: | | |
| Restructure Kenya Railways to improve its efficiency | 1. Present policy paper on restructuring KR for Government approval. | Feb. 1996 |
| | 2. Agree to performance contract between GOK and KR. | May 1996 |
| | 3. Separate service accounts and establish passenger service as an autonomous business. | March 1996 |
| | 4. Bring Gulf Marine Services to the point of sale. | June 1996 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| | 5. KR to contract out full maintenance of locomotives to private contractors. | August 1996 |
| | 6. KR to reduce staff level to 14,500. | Dec. 1996 |
| **Ports:**<br><br>Improve the efficiency of Kenya Ports Authority | 1. KPA to complete renegotiation of the two 10 year equipment maintenance contracts, limiting duration and establishing performance guarantees. | March 1996 |
| | 2. Sign contract for external management and operation of the container terminal. | March 1996 |
| | 3. Complete Performance Contract between GOK and KPA. | April 1996 |
| **Telecommunications:** The extension and efficient delivery of telecommunications services to remove constraint to more rapid economic growth and the long term development of Kenya. | 1. Issue of telecommunications sector policy statement and privatisation programme. | early in 1996 |
| | 2. Divest non-essential services (workshops, buildings). | Sept. 1996 |
| | 3. Present legislation enabling the separation of KPTC into three separate entities to Parliament. | Mar. 1996 |
| | 4. Establish three separate entities for posts, telecommunications and a regulatory authority. | Dec. 1996 |
| | 5. Sale to outside investors at least 30 percent of the new telecommunications after separation. | Mar. 1997 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
| --- | --- | --- |
| | 6. Liberalise telecommunications services beginning with pay phones and VSAT terminals for private operators. | 1995<br>1996 |
| Water:<br><br>Improve management of water resources. | 1. Prepare an operational plan and progressively implement declared government policy of charging urban consumers a water tariff to cover capital amortization and 0 & M costs while setting rural tariffs to cover only O&M. | 1996-<br>1998 |
| | 2. Present to Parliament amendments to Water Act to address concerns regarding national water resources management. | Dec.<br>1996 |
| Energy<br>Implementation of a sound policy framework and an appropriate investment program to address the increasingly serious shortfalls in power supply. | 1, Invite bids for investment hy independent private producers in power development. | March<br>1996 |
| | 2. Present appropriate legislation for separation of regulatory and commercial functions to Parliament. | June 1996 |
| | 3. Complete action plan for reorganization of the power sector, including separation of accounts of power sector companies. | June 1996 |
| | 4. Commence implementation of agreed performance contracts for all power sector parastatals. | Sept. 1996 |
| | 5. Adjust electricity tariffs to 75 percent of LRMC. | June 1996 |
| | 6. Agree with IDA on timing of adjustments of electricity tariffs to cover LRMC. | Oct. 1996 |
| | 7. Remove the temporary import tariff on petroleum products. | Oct. 1996 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| **Human Resource Development** **Population:** Further reduction in population growth rates via continued emphasis on family planning service delivery to achieve higher contraceptive use. | 1. Adopt plan for restructuring NCPD into a policy- making, coordinating and advisory entity. | June 1996 |
| **Health:** Devote relatively more of the Ministry of Health budget to preventive and primary services; increase efficiency and financial autonomy of Kenyatta National Hospital (KNH), and encourage facility-level management and decentralization. | 1. Limit the share of the MOH budget devoted to KNH to 12% (subject to adequate progress being made in reform and rehabilitation of other facilities serving the Nairobi area). | 1996/97 |
| | 2. Give full authority to KNH Board to determine charges at KNH, with the exception of TB, AIDS patients and children under 5. | June 1996 |
| | 3. Increase user charge collections to about 16% of MOH budget in 1996/97 and 18% in 1997/98 (with 25% of this going to primary and preventive health care) | 1997/98 |
| Implementation of major reform measures in the health sector as indicated in the Health Policy Framework. | 4. Decentralise financial and administrative authority to districts, beginning with a phased approach. | 1996 |
| | 5. Complete detailed audits of the NHIF for fiscal years from 1991/92 through 1994/95. | Dec. 1996 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
| --- | --- | --- |
| | 6. Finalise and begin implementation of action plan to shift part of the financial burden of curative care from the Ministry of Health budget to insurance schemes, including the National Hospital Insurance Fund (NHIF) and private providers. | Dec. 1996 |
| | 7. Present legislation to Parliament amending the NHIF Act to allow coverage of the self-employed and workers in the Jua Kali sector. | 1996/97 |
| | 8. Finalise and begin implementation of action plan to consolidate and strengthen key health management information systems to support the policy making role of the Ministry of Health in budgeting, plating and management functions in the districts. | July 1996 |
| AIDS: | Finalise Policy Paper on AIDS. | June 1996 |
| **Nutrition:** Reduction in infant mortality, and improvement in nutritional status of children as well as adult women. | 1. Finalise and begin implementation of an action plans for (i) nutritional interventions with a view to shifting budget financing to more cost-effective programmes targeted at infants, pre-school children, and pregnant and disadvantaged women, with selected interventions for older children in poor districts, the landless and ASAL areas ; and (ii) community financing of the school feeding programme. | Dec. 1996 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| **Education Policies and Reforms:** The Government's key objectives during this PFP period are to increase enrollment rates among girls in poor households, to increase completion rates for primary education, and to improve quality at all levels of the system. The objectives are to be met within the context of a further rationalisation of public expenditures, improved management of education (including decentralization of decision making), and expanded private sector participation. | 1. Make adequate budget allocation to expand means-tested bursary programmes for secondary school students and introduce a means-tested bursary programmes for primary schools, both especially' targeted to girls from poor households. | 1996/97 |
| | 2. Adopt policies to enable the private sector to participate with JKF and KBL for publication of educational materials prepared by KIE. | 1996 |
| | 3. Complete and commence implementation of plan of action to rationalize TSC functions and responsibilities. | June 1996 |
| | 4. Revise Education Acts and regulations and prepare plan of action to decentralise management and financial decision-making, including determination of fees to councils and boards of educational institutions up to university level. | Sept. 1996 |
| | 5. Prepare and implement a plan of action for the HELB to increase progressively the role of the commercial banks in loan recovery. | June 1996 |
| | **6.** Present to Parliament legislation to harmonise the various acts relating to CHE and the public universities. | June 1996 |
| | 7. Prepare, through MRTT&T, a National Skills Training Strategy. | Dec. 1996 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| **Further Targeted Poverty Interventions** | | |
| Provide support to population who cannot wait until the growth accelerates and who cannot readily participate in it because of special handicaps, such as geographic isolation. | 1. Finalise and begin implementation of drought management system which would improve the timeliness and target accuracy of emergency food distribution response. | 1996 |
| | 2. Implement road construction and maintenance schemes to seek to generate employment for the poor at wages defined by existing wage guidelines. | 1996-1998 |
| | 3. License more water kiosks, support community based initiatives in waste removal and sanitation, and encourage access to low cost housing through cooperative societies, | 1996-1998 |
| | 4. Design and commence implementation of a community-based pilot water fund. | Sept. 1997 |
| | 5. Finalise and approve ASAL strategy and action plan which will include programmes designed to provide a safety net to enhance the economic integration of such population groups with the rest of the economy, and to improve the human capital base of the population. | Dec. 1996 |

| OBJECTIVES AND POLICIES | STRATEGIES AND MEASURES | TIMING |
|---|---|---|
| **Technical Assistance** | 1. Develop plan of TA to improve the functioning of money and foreign exchange markets. | 1996 |
| Enhance functioning of financial markets and institutional monitoring capacity. | 2. Place a resident advisor on:<br>(a) expenditure control<br>(b) administering revenue authority | 1996 |
| | 3. Seek TA to build a producer price index and construction of a quarterly index on economic activity. | 1996 |

Table 1. Kenya: Selected Economic and Financial Indicators and Medium Term Adjustment Framework, 1991-98

| | 1991 | 1992 | 1993 | 1994 Est. | 1995 Est. | 1996 Proj. | 1997 Proj. | 1998 Proj. |
|---|---|---|---|---|---|---|---|---|
| | (Annual percentage changes, unless otherwise specified) | | | | | | | |
| National income and prices | | | | | | | | |
| GDP (at factor cost and constant prices) | 2.1 | 0.5 | 0.2 | 3.0 | 5.0 | 5.0 | 5.3 | 5.7 |
| GDP (at factor cost and current prices) | 13.9 | 15.2 | 23.0 | 19.3 | 5.5 | 9.0 | 10.7 | 11.2 |
| Consumer price index (dec. to dec.) | 14.5 | 33.7 | 54.7 | 6.6 | 6.9 | 5.0 | 5.0 | 5.0 |
| Consumer price index (period average) | 19.6 | 27.3 | 46.0 | 28.8 | 1.7 | 5.0 | 5.0 | 5.0 |
| External sector (on the basis of US$) | | | | | | | | |
| Exports, f.o.b. | 5.9 | -4.1 | 9.0 | 34.8 | 20.4 | 0.3 | 5.8 | 8.0 |
| Imports, c.i.f. | -15.6 | -4.4 | -13.9 | 27.2 | 27.5 | -5.6 | 6.0 | 6.8 |
| Non-oil imports, c.i.f. | -15.1 | -7.2 | -17.5 | 42.7 | 33.1 | -7.0 | 5.9 | 6.7 |
| Export volume | 6.2 | -6.1 | 11.6 | 7.0 | 15.9 | 4.1 | 4.3 | 6.0 |
| Import volume | -8.2 | -0.4 | -12.2 | 30.6 | 7.7 | -5.2 | 5.2 | 5.9 |
| Terms of trade (deterioration-) | 8.6 | 5.4 | 0.1 | 27.6 | -12.2 | -3.4 | 0.6 | 1.1 |
| Nominal effective exchange rate (depreciation-) | -13.2 | -13.4 | -40.1 | 54.3 | -20.7 | -- | -- | -- |
| Real effective exchange rate (depreciation-) | -7.1 | 11.4 | -20.1 | 47.9 | -20.1 | -- | -- | -- |
| Money and credit (end of period) | | | | | | | | |
| Reserve money | 15.7 | 42.9 | 63.7 | 31.3 | 28.7 | -- | -- | -- |
| Net domestic assets of the CBK 1/ 2/ | 19.9 | 42.6 | 3.2 | 29.3 | 38.8 | -9.8 | -- | -- |
| Broad money (M3) | 13.4 | 29.1 | 22.9 | 26.5 | 14.7 | 2.4 | -- | -- |
| Interest rate | | | | | | | | |
| (90-day Treasury Bills, average rate in percent) | 16.6 | 16.5 | 49.8 | 23.3 | 19.5 | -- | -- | -- |
| | (In percent of GDP, unless otherwise specified) | | | | | | | |
| Gross national saving | 19.4 | 16.0 | 20.1 | 21.6 | 19.8 | 23.2 | 23.6 | 24.5 |
| Central Government 3/ | 2.2 | -0.8 | -1.6 | 3.5 | 7.3 | 7.6 | 7.6 | 8.3 |
| Other | 17.3 | 16.9 | 21.7 | 18.2 | 12.5 | 15.6 | 15.9 | 16.2 |
| Gross Investment | 21.3 | 17.4 | 18.4 | 20.9 | 22.9 | 22.9 | 23.3 | 23.9 |
| Fixed capital formation | 19.3 | 17.1 | 17.7 | 20.4 | 21.7 | 22.2 | 22.6 | 23.2 |
| Central Government 3/ | 6.1 | 5.9 | 6.2 | 6.7 | 7.7 | 7.6 | 7.6 | 8.1 |
| Other | 13.2 | 11.2 | 11.5 | 13.7 | 14.0 | 14.6 | 14.9 | 15.1 |
| Net change in stocks | 2.0 | 0.4 | 0.7 | 0.4 | 1.2 | 0.7 | 0.7 | 0.7 |
| External current account incl. official transfers | -1.8 | -1.4 | 1.8 | 0.7 | -3.1 | 0.3 | 0.3 | 0.6 |
| External current account excl. official transfers | -4.4 | -4.1 | 0.1 | -0.4 | 4.2 | -1.3 | -1.2 | -0.8 |
| Central Government finance 4/ | | | | | | | | |
| Revenue | 24.5 | 24.2 | 29.2 | 31.6 | 34.0 | 31.7 | 30.9 | 30.6 |
| Total Expenditure | 29.5 | 35.6 | 37.2 | 34.3 | 36.0 | 33.3 | 32.3 | 31.9 |
| Overall balance, excluding grants | -4.9 | -11.4 | -8.0 | -2.6 | -1.9 | -1.6 | -1.5 | -1.3 |
| Overall balance, including grants | -3.0 | -10.0 | -6.8 | -1.2 | -0.3 | -0.3 | -0.2 | 0.1 |
| Primary balance, excluding grants | 1.4 | 0.6 | 5.3 | 5.4 | 5.4 | 3.8 | 3.0 | 2.4 |
| Current balance, excluding grants | 0.7 | -5.0 | -1.0 | 5.2 | 6.2 | 6.1 | 6.6 | 7.3 |
| External debt inclusive of Fund credit | 77.3 | 81.2 | 117.3 | 94.3 | 79.9 | 80.6 | 74.7 | 68.1 |
| Debt service ratio 5/ | 32.3 | 3.1 | 28.6 | 26.2 | 24.9 | 23.9 | 21.8 | 19.2 |
| Interest payments 5/ | 11.4 | 10.4 | 8.1 | 8.3 | 8.7 | 7.3 | 6.4 | 5.7 |
| | (In millions of US$, unless otherwise specified) | | | | | | | |
| Overall balance of payments | -313.6 | -237.2 | 281.7 | 99.5 | -138.9 | 113.3 | 116.7 | 148.8 |
| Gross international reserves (end of period) | 184.0 | 182.3 | 474.6 | 625.3 | 457.7 | 595.4 | 803.9 | 997.8 |
| Gross international reserves (in months of imports) | 1.1 | 1.2 | 3.5 | 3.7 | 2.1 | 2.9 | 3.7 | 4.3 |
| Nominal GDP at market prices (in billions of KSh) | 221.2 | 256.1 | 320.1 | 384.5 | 407.5 | 446.6 | 492.7 | 546.0 |
| Exports of goods and nonfactor services (in billions of KSh) | 60.3 | 69.4 | 125.1 | 148.2 | 151.9 | 165.4 | 173.9 | 184.7 |
| Exchange rate (KSh/US$, period average) | 27.5 | 32.2 | 58.0 | 56.1 | 51.4 | 55.0 | 55.0 | 55.0 |

Sources: Data provided by the authorities, and staff estimates and projections.

1/ In percent of beginning-of-period reserve money stock.
2/ For 1996, net domestic assets are calculated as reserve money less net foreign assets at constant exchange rate.
3/ Calendar year basis.
4/ Fiscal year starting July 1 of the calendar year indicated.
5/ In percent of exports of goods and services.

# Table 2. Gross Financing Requirements, 1996 - 1998

(In millions of US dollars)

| | 1995 Act. | 1996 Proj. | 1997 Proj. | 1998 Proj. | 1996-98 Proj. |
|---|---|---|---|---|---|
| EXTERNAL FINANCING REQUIREMENTS | -642 | -875 | -808 | -727 | -2,411 |
| Current Account, excluding official transfers (gross) | -341 | -113 | -114 | -81 | -308 |
| Reduction in arrears | 6 | -95 | -- | -- | -95 |
| Accumulation of international reserves | 172 | -138 | -209 | -194 | -540 |
| Scheduled amortization | -439 | -434 | -412 | -382 | -1,228 |
| IMF Repayment | -39 | -63 | -74 | -70 | -207 |
| Debt Buy-back | -- | -32 | ... | ... | -32 |
| AVAILABLE FINANCE | 529 | 651 | 597 | 612 | 1,860 |
| Private capital flows 1/ | 225 | 117 | 77 | 106 | 299 |
| Rescheduling arrears | -- | 72 | ... | -- | 72 |
| Identified project finance | 303 | 442 | 521 | 506 | 1,469 |
| Official transfers | 95 | 122 | 141 | 139 | 402 |
| Loans 2/ | 209 | 320 | 380 | 367 | 1,067 |
| Identified program finance | 114 | 20 | | -- | 20 |
| FINANCING GAP | -- | 224 | 211 | 115 | 551 |

Source: Data provided by Kenyan authorities; IMF and World Bank staff estimates.

1/ Includes parastatals
2/ Includes defence loans