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February 2, 1983

To: Members of the Executive Board

From: The Secretary

Subject: Kenya - Staff Report for the 1982 Article IV Consultation

Attached for consideration by the Executive Directors is the staff report for the 1982 Article IV consultation with Kenya. A draft decision appears on page 24.

This subject will be brought to the agenda for discussion on a date to be announced.

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INTERNATIONAL MONETARY FUND

KENYA

Staff Report for the 1982 Article IV Consultation

Prepared by the Staff Representatives for the 1982 Consultation with Kenya

Approved by J.B. Zulu and W.A. Beveridge

February 1, 1983

I. Introduction

The 1982 Article IV consultation discussions with Kenya, together with a review of the recently expired stand-by arrangement were initiated by two missions which visited Nairobi on June 27-July 9, and September 26-October 7, 1982. 1/ Discussions were completed in the period November 28-December 11, when a new stand-by arrangement was also discussed and its principal elements agreed. 2/3/ The missions met with the financial and economic officials in the Treasury, the Ministry of Economic Planning and Development, and other government departments, as well as with Central Bank officials. The second mission was received by His Excellency, Daniel Arap Moi, President of the Republic.

Kenya continues to avail itself of the transitional arrangement of Article XIV. The latest stand-by arrangement expired on January 7, 1983.

II. Background

Following several years of rapid economic growth and strong balance of payments, largely related to a substantial improvement in the terms of trade, there was a marked deterioration in the general economic environment in Kenya beginning with 1979. In part the difficult situation resulted from exogenous factors, such as an extensive drought, which had a major impact on agricultural output and required the importation of foodstuffs on an emergency basis, and a rapid reversal of the very favorable terms of trade that existed in the earlier period. However, it is also clear that

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1/ The first two missions comprised Messrs. J.M. Jiménez (head-AFR), J. Simpson (AFR), and L. Doe (FAD), and Ms. S. Eken (ETR), Ms. Y. Coker (secretary-AFR) and Miss M. Simpson (secretary-AFR).

2/ The last mission consisted of Messrs. J.M. Jiménez (head-AFR), J. Simpson (AFR), L. Doe (FAD), and D. Lipton (ETR) and Miss A. Greasley (secretary-SEC). Mr. Makalou (AFR) participated in some of the discussions.

3/ The paper requesting the new stand-by arrangement will be issued shortly.

other fundamental factors played an important role in the deterioration of Kenya's economic and financial situation. The slowdown in economic activity and the weakening of the balance of payments, which characterized the post-1979 period, was also influenced by the import substitution policies pursued in the 1960s and 1970s, which led to a continued fall in the competitiveness of the export sector and increased reliance of domestic industries on import protection. The pressures generated by a continued high population growth on limited resources also became evident. The pursuance of expansionary fiscal and monetary policies, even after the balance of payments had weakened, was also important in the deterioration which occurred. In FY 1979/80 (July/June) the budgetary deficit was equivalent to 5.7 per cent of GDP (6.3 per cent excluding grants) but rose to 9.5 per cent of GDP (10.4 per cent excluding grants) in 1980/81. During this period net domestic bank credit also expanded rapidly (Table 1).

In both 1979 and 1980 the agricultural sector contracted, while the expansion in the industrial sector fell significantly from the high levels recorded in the 1976-78 period. Construction and the trade sectors also suffered major reductions in their growth rates. As a result of these developments, the rate of growth of real GDP fell to an average of about 4.0 per cent in 1979-80, compared with an average of over 8 per cent in the years 1977-78.

The balance of payments registered major strains beginning in 1978, when the current account deficit rose to the equivalent of 12.4 per cent of GDP, and an overall deficit of SDR 161 million, or 3.8 per cent of GDP was recorded. The large overall deficit was easily financed by the authorities, given the substantial accumulation in net reserves which had taken place in the previous two years. Through a combination of temporarily tightened financial policies, import restraint, including advance import deposits, and additional foreign borrowing, the current account deficit was reduced to 8.2 per cent of GDP and an overall surplus generated in 1979. However, with the relaxation of financial policies once more and the removal of most of the advance import deposit requirements in 1980, the balance of payments improvement was quickly reversed and the current account deficit widened to 12.6 per cent of GDP and an overall deficit of 2.6 per cent of GDP was recorded. This outturn focused attention on the basic problems which continued to plague the Kenyan economy and emphasized the need for a more adequate and consistent policy stance.

A one-year stand-by arrangement was approved in August 1979 and followed by a two-year stand-by arrangement in October 1980. Under neither arrangement were all of the contemplated purchases carried out, as some of the performance criteria were not observed.

Table 1. Kenya: Selected Economic and Financial Indicators, 1979-82

	1979	1980	1981	1982 Original indicative program targets	1982 Revised program targets	1982 Estimate
	(Annual per cent changes, unless otherwise specified)					
National income and prices						
GDP at constant prices	4.1	4.3	4.1	4.0	4.2	4.5
GDP deflator	6.3	10.9	9.7	11.4	15.4	14.4
Consumer prices	9.4	12.8	20.0	8.0	14.0	14.4
External sector (on the basis of SDRs)						
Exports, f.o.b.	4.3	19.5	-3.2	17.1	11.3	-0.8
Imports, c.i.f.	-5.5	42.6	-8.2	1.1	0.4	-13.1
Non-oil imports, c.i.f.	-11.4	31.2	-17.1	5.5	2.1	-15.1
Export volume	-1.9	3.0	--	6.7	6.0	-1.2
Import volume	-18.4	9.1	-27.5	-4.7	-3.0	-13.5
Terms of trade (deterioration -	-8.3	-8.0	-18.5	1.8	1.0	1.4
Nominal effective exchange rate (depreciation -)	-3.2	-2.6	-14.5	--	...	3.0
Real effective exchange rate (depreciation -)	-7.2	-0.8	- 6.7	--	...	--
Government budget 1/						
Revenue and grants	7.3	19.4	21.3	13.0	10.1	12.4
Total expenditure	18.6	12.9	29.7	5.9	4.9	3.8
Money and credit 1/						
Domestic credit	21.9	14.8	24.2	19.9	25.2	33.0
Government	94.1	-2.1	83.4	34.0	50.3	65.5
Private sector	8.5	18.0	9.5	15.3	15.3	16.0
Money and quasi-money (M_2)	10.5	9.4	7.1	11.0	7.5	9.1
Velocity (GDP relative to M_2) 3/			3.23	3.45	3.68	3.55
Interest rate (annual rate) 3/						
Savings deposit	5.0	6.0	10.00 5/	10.00	...	12.50
Average time deposit	5.13 to 5.86	6.35 to 7.00	10.75 to 12.50	10.75 to 12.50	...	13.75 to 15.50
Maximum lending rate	...	...	14.00	14.00	...	16.00
			(In per cent of GDP)			
Central government current account surplus/deficit (-)	0.9	1.2	-0.2	2.8	2.5	1.1
Central government overall budget deficit	7.4	5.7	9.5	6.0	6.4	6.5
Domestic bank financing	2.5	—	2.8	0.5	1.6	2.6
Foreign financing	3.5	4.1	4.9	4.2	2.6	1.7
Gross domestic investment	22.7	29.2	23.0	25.0	22.0	22.0
Gross domestic savings	16.7	17.2	16.2	16.2	16.4	16.4
Current account deficit 6/	8.2	12.6	10.2*	7.4*	8.0*	7.1*
External debt	28.5	30.6	34.4	43.7	37.6	34.1
inclusive of use of Fund credit:						
External debt	31.6	34.2	38.3	45.5	39.4	39.0
Debt service ratio 7/	11.8	11.7	20.6	15.0	14.9	22.1
Interest payments 7/	4.6	5.8	8.4	6.1	7.9	10.7
	(In millions of SDRs, unless otherwise specified)					
Overall balance of payments 8/	154.0	-142.0	-198.0**	-32.0**	-169.0**	-146.0**
Gross official reserves (months of imports)	4.2	2.3	1.4	2.0	1.5	1.7
External payments arrears	--	--	--	--	--	--

1/ Fiscal year ending June 30.
2/ Refers to stand-by program approved on October 15, 1980 and canceled on January 8, 1982.
3/ Level in per cent.
4/ The program did not specifically indicate level, only upward direction.
5/ Rate introduced in September 1981.
6/ Asterisk * reflects severe constraint on foreign exchange availability.
7/ In per cent of exports of goods and services.
8/ Double asterisk ** reflects severe constraint on foreign exchange availability.

III. Performance Under the 1982 Stand-By Arrangement

In view of the difficult economic situation, in 1981 the Kenyan authorities felt that a reorientation of policy was required. To this end an economic and financial program was adopted for FY 1981/82, which was supported in January 1982 by a one-year stand-by arrangement of SDR 151.5 million, representing 146.4 per cent of Kenya's quota, and the previous two-year arrangement was canceled. The program aimed at a better distribution of resources, through improved incentives particularly, in the export sector, which would promote growth and redress the balance of payments position in the medium term. The program also sought to strengthen the budgetary situation and to adopt more cautious financial policies.

To aid the shift of resources to the export sector, and to restrain import demand, the authorities devalued the Kenya shilling by 15 per cent in terms of the SDR on September 21, 1981, following an earlier depreciation of 5 per cent in February 1981. Moreover, a reform of the import system aimed at simplifying import procedures by reducing official discretion and quantitative restrictions was pushed forward. Imports were classified into three schedules. Schedule 1 included items such as food, raw materials, industrial spare parts, capital goods, and pharmaceutical products not produced domestically. Goods classified in this schedule were made freely importable. The importation of items in the remaining two schedules (2A and 2B) was made subject to quotas. The new system significantly simplified the complicated procedures utilized previously and reduced the number of ad hoc decisions which could be taken by the licensing authorities, thereby improving planning possibilities in the private sector. To permit the transfer of an important number of items into Schedule I, import tariffs on some items were increased with the 1981/82 budget, following increases already put into place in the previous two fiscal years. In addition, producer prices were reviewed and some increases put into effect.

In the fiscal area the program called for a reduction in the overall budgetary deficit from the equivalent of 9.6 per cent of GDP (10.4 per cent excluding grants) in 1980/81 to 6.4 per cent (7.8 per cent excluding grants) in 1981/82, largely through a sharp reduction in public expenditure. Net domestic bank financing of the budget was to be limited to the equivalent of about 6 per cent of the stock of money and quasi-money at the start of the fiscal year, compared to about 12 per cent in the previous fiscal year. 1/ The growth of total domestic bank credit was expected to remain at about the previous fiscal year's level of 24 per cent. Thus, the private sector would receive a larger amount of credit than previously. Interest rates were raised by about 2 percentage points, resulting in an increase of between 5 and 6 percentage points in the period June 1980 and September 21, 1981. The lending rates reached a level of 14 per cent,

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1/ The definition utilized in the stand-by arrangement allowed for a larger increase because it included the counterpart of Eurocurrency borrowing.

minimum time deposit rates ranged between 10.75 to 12.0 per cent, and the minimum savings rate rose to 10 per cent.

As a consequence of these measures, the current account deficit of the balance of payments in 1982 was expected to decline by 2.2 percentage points of GDP to 8.0 per cent (9.0 per cent excluding grants) in 1982. This improvement was expected in part from a better export performance, reflecting higher export prices and further volume increase in major products. Imports were expected to fall in real and in SDR terms.

Kenya drew SDR 60 million after the approval of the stand-by arrangement (Table 2). The performance criteria for end-January 1982 were met by substantial margins and a further SDR 30 million were drawn in June 1982 (Table 3). The first of two reviews agreed in the program was completed by the Executive Board on June 6, 1982. During this review exchange and interest rates and fiscal policies were examined and the performance criteria applicable for end-June 1982 were fixed. The second review, involving import policy and the setting of the remaining credit ceilings, was to be held prior to August 1, 1982. The review could not be completed as expected because the budgetary policies for 1982/83 were not fully constituted at the time of the mission's visit. An attempted coup in early August precluded further discussions and generated additional financial problems which needed to be reviewed before the arrangement could be reinstituted. Nonetheless, in accordance with the requirement of the program, the Kenyan authorities transferred 20 per cent of the items in the restricted categories (Schedule 2A and 2B) to the unrestricted category (Schedule 1), in June. The items transferred accounted for 5 per cent of total imports and 8 per cent of non-oil imports in 1981, a year of tight import controls. However, with respect to 1978, the last year of a relatively free import system, the items tranferred accounted for 19 per cent of total imports and 22 per cent of non-oil imports. Thus, the shift represented a meaningful attempt to liberalize the import system. The export compensation scheme was also suspended in June 1982.

Provisional data for FY 1981/82 indicate that total expenditures reached K Sh 20.9 billion, slightly above the revised program target of K Sh 20.6 billion. The expenditure outcome involved a reduction in real government outlays of 10 per cent during the year. Revenues and grants at K Sh 16.6 billion were also slightly higher than the revised target of K Sh 16.4 billion. Consequently, the overall deficit, at K Sh 4.3 billion (6.5 per cent of GDP), was marginally above the K Sh 4.2 billion forecast made during the review of the program; the program's original indicative target had been K Sh 4.0 billion (Table 4).

Although the efforts to limit overall government expenditure to the targeted level and keep the overall deficit in line with the program were successful, Kenya faced considerable difficulties in obtaining the level of net foreign financing expected in the program for fiscal year 1981/82.

Table 2. Kenya: Schedule of Purchases and Repurchases under Expired Stand-By Arrangement, and Fund Holdings of Kenya Shillings, 1982

(In millions of SDRs)

	Original phasing of purchases	Actual purchases	Actual repurchases	Fund holdings 1/	
				Total	Per cent of quota (At end of period)
January	60.0	60.0	0.6	261.6	252.8
February	--	--	--	261.6	252.8
March	--	--	--	261.6	252.8
April	30.0	--	--	261.6	252.8
May	--	--	--	261.6	252.8
June	--	30.0	--	291.6	281.8
July	--	--	0.6	291.0	281.2
August	30.0	--	--	291.0	281.2
September	--	--	--	291.0	281.2
October	--	--	--	291.0	281.2
November	31.5	--	--	291.0	281.2
December	--	--	--	291.0	281.2

Sources: Phasing in the stand-by arrangement; and data provided by the Treasurer's Department.

1/ Excluding oil facility and compensatory financing facility.

Table 3. Kenya: Quantitative Performance Criteria

(In millions of Kenya shillings)

	1981/82 Program		
	June 1981	Jan. 1982	June 1982
Total domestic bank credit 1/			
Ceiling		20,800	21,304
Actual	17,016	20,551	22,623
Net bank credit to Government 2/			
Ceiling		6,550	6,241
Actual	4,153	5,707	6,871
New external borrowing contracted or guaranteed by the Government (cumulative) 3/			
1-12 years' maturity			
Ceiling	--	160	160
Actual		145	145
1-5 years' maturity			
Ceiling	--	--	-

Sources: Data provided by the Kenyan authorities, Letter of Intent and Policy Memorandum, December 3, 1981; and Letter of Intent, May 28, 1982.

1/ The definition of domestic bank credit differs from that of the monetary survey in that the former includes the domestic currency counterpart of drawings on Eurocurrency loans.

2/ The definition of net bank credit to the Government differs from that of the monetary survey in that the former includes the domestic currency counterpart of drawings on Eurocurrency loans and excludes the operations of the Cereals and Sugar Finance Corporation (CSFC). This agency maintains its general account with the Treasury, rather than with a commercial bank; therefore, its operations influence the Government's net position with the banking system, reducing net government credit when the CSFC receives payments, and increasing net government credit when it purchases cereals. Consequently, it is necessary to exclude these operations in order to isolate developments in net government credit due solely to budgetary operations. However, the bank credit utilized by the CSFC is captured in the overall credit ceiling, where this adjustment is not made.

3/ In millions of U.S. dollars.

Table 4. Kenya: Central Government Finances, 1979/80-1982/83

	1979/80	1980/81	1981/82		1982/83	
			Revised program	Provisional outturn	Revised budget	Program
	(In billions of Kenya shillings)					
Total revenue and grants	12.3	14.8	16.4	16.6	19.4	19.5
Total revenue	12.0	14.3	15.9	15.7	17.6	18.0
Grants	0.3	0.5	0.5	0.9	1.8	1.5
Total expenditure	15.1	20.2	20.6	20.9	23.4	23.2
Recurrent expenditure	11.4	14.0	14.2	15.0	16.1	16.4
Development expenditure	4.4	5.7	6.4	6.4	7.3	6.8
Adjustment (net expenditure (-)) 1/	0.7	-0.5	--	0.5	--	--
Overall deficit	-2.8	-5.4	-4.2	-4.3	-4.0	-3.7
(In per cent of GDP)	(-5.7)	(-9.6)	(-6.4)	(-6.5)	(...)	(-4.7)
Financing	2.8	5.4	4.2	4.3	4.0	3.7
Foreign (net)	2.0	2.8	1.7	1.1	2.2	1.9
Drawings (gross)	(2.4)	(3.5)	(3.0)	(2.2)	(3.8)2/	(3.5)3/
Repayments	(-0.8)	(-0.7)	(-1.3)	(-1.1)	(-1.6)	(-1.6)
Domestic (net)	0.8	2.6	2.5	3.2	1.8	1.8
Nonbank	(0.8)	(1.0)	(1.5)	(1.5)	(0.8)	(0.8)
Bank and CSFC 4/	(--)	(1.6)	(1.0)	(1.7)	(1.0)	(1.0)
Overall deficit excluding grants	-3.1	-5.9	-4.7	-5.2	-5.8	-5.2
Total GDP at current market prices	49.0	56.5	65.3	66.4	...	77.9
	(In per cent of GDP)					
Memorandum items:						
Total revenue	24.5	25.3	24.4	23.6	...	23.1
Of which: tax revenue	(21.2)	(22.0)	(...)	(20.8)	(...)	(...)
Total expenditure	30.8	35.8	31.6	31.5	...	29.8
Overall deficit excluding grants	-6.3	-10.4	-7.2	-7.8	...	-6.7
Bank and CSFC	--	2.8	1.5	2.6	...	1.3

Source: Based on information provided by the Kenyan authorities.

1/ Reflects the fact that the revenue and expenditure data are not strictly on a cash basi A negative adjustment item is treated as expenditure, whereas a positive item is treated as revenue.

2/ Includes the full IBRD SAL.

3/ Includes only the first tranche of the IBRD SAL.

4/ Does not correspond to stand-by definition because it excludes counterpart of Eurocurrency drawings.

At its inception the stand-by arrangement envisaged net foreign financing of K Sh 2.8 billion. This level was adjusted downward during the review to K Sh 1.7 billion to take account of the delay in the release of the structural adjustment loan and other credits. Actual receipts, however, totaled only K Sh 1.1 billion. Consequently, the necessary level of domestic financing for the budget rose from an initial estimate of K Sh 1.2 billion to K Sh 2.5 billion at the time of the June review to the present provisional estimate of K Sh 3.2 billion. Faced with the difficulties of stopping ongoing projects and in the expectation that the delayed foreign resources would be received shortly, the Kenyan authorities did not curtail expenditures, but instead sought to make up for the shortfall in foreign resources through increased nonbank financing and made a special effort to keep expenditures to the budgeted level. The monetary authorities enforced the liquidity requirement of nonbanks, which calls for half of the requirements to be met by Treasury bills, more rigorously. In addition, the interest rate on Treasury bills was progressively increased from about 6 per cent at the beginning of the fiscal year to about 13 per cent at the close of the fiscal year. Despite the tight expenditure policy and the additional financing from nonbanks, the shortfall in foreign financing could not be met. Consequently, the performance criteria for end-June 1982 on net bank credit to the Government and on net domestic bank credit were exceeded. The ceiling on net credit to the Government had been fixed at K Sh 6.2 billion and the actual outturn was K Sh 6.9 billion, while the ceiling on net domestic credit had been set at K Sh 21.3 billion and the actual outturn was K Sh 22.6 billion. Only about half the excess over the ceiling in the net domestic credit ceiling resulted from net bank credit to the Government. Apart from developments in the budget, the breaching of the overall ceiling on net domestic credit at the end of June was also affected by a greater increase in credit to the private sector than earlier assumed, largely resulting from the rise in agricultural output generated by improved weather conditions in 1982. Private sector credit rose by 15.8 per cent in the 12 months ended June 1982 compared to the indicative target in the program of 15.3 per cent.

With regard to the balance of payments, the revised program called for an adjustment in the current account deficit equivalent to 2.2 percentage points of GDP to about 8.0 per cent of GDP in the course of 1982. However, it was also recognized that the capital account had weakened and it appeared that the overall balance deficit would be SDR 169 million, compared with the program's original indicative target of a surplus of SDR 32 million. This turnaround reflected the reduced flow of foreign resources to the budget, including a delay in the release of the structural adjustment resources expected from the IBRD. Moreover, the original program counted on an additional Eurocurrency loan, which the Government decided not to contract. There was also an unexpected shortfall in the net inflow of capital to the private sector.

Following the exchange rate action in September 1981, the prices of a large number of price controlled items were adjusted upward and producer

prices were raised. These adjustments, in addition to the inherent price pressures produced by the devaluation and the impact of the increase in excise duties in April, have been responsible for a significant proportion of the increase in the price index. The composite consumer price index went up by a little over 14 per cent in 1982, an increase larger than that recorded by Kenya's major trading partners, but in line with the program's expectations. Moreover, the Kenya shilling is pegged to the SDR, which appreciated in nominal terms with respect to the currencies of many of Kenya's trading partners. Consequently, the trade weighted real exchange rates of the Kenya shilling appreciated by about 14 per cent through October 1982.

The earlier liberalization of the import licensing scheme, including the further adjustments carried out in June, the real appreciation of the exchange rate, and the shortfalls in foreign financing contributed to the pressures brought to bear on the balance of payments in the second half of 1982. With these events and the coup attempt in August, foreign exchange availability failed to match import demand and a substantial tightening of the licensing process became necessary. The most recent projections of the 1982 balance of payments indicate that the current account deficit is likely to reach the equivalent of 7.1 per cent of GDP, involving a downward adjustment of over 3 percentage points. In order to meet this objective, however, the level of imports was kept at a lower level than targeted in the program, largely through restrictions. Exports performed less well than expected, and a shortfall is also estimated under net services and transfers, reflecting greater external interest payments and smaller net tourist earnings. As projected during the mid-term review, the net capital inflow fell considerably below the original estimates. The overall deficit is now estimated at SDR 173 million, of which the net use of Fund resources is estimated at SDR 133 million and the remainder to be financed out of reserves (Table 5). Kenya's gross foreign assets were the equivalent of 1.3 months of imports at the end of 1982, a level considered inadequate by the authorities.

The most recent developments in export and invisible earnings, although partly related to a worse world economic outlook scenario than originally forecast, and the need to tighten the import licensing procedures made it unlikely that Kenya, without taking additional meaningful and convincing measures, would be able to reach a sustainable balance of payments position by 1985, while maintaining a reasonable growth rate. Moreover, the delay in formulating a realistic budget at the start of fiscal year 1982/83, the weakening of the revenue base from the fall in dutiable imports, and the losses suffered during the coup attempt led to the deterioration of the budgetary position in the early months of the current fiscal year, despite the authorities' success in limiting expenditures, highlighting the need to reinforce the adjustment program.

Table 5. Kenya: Balance of Payments Summary, 1979-82

(In millions of SDRs)

	1979	1980	1981 Prov.	1982 Program 1/	1982 Prov.	1983 Proj.
Current account	-386	-686	-586	-470	-424	-352
Trade balance	-620	-1,068	-933	-878	-696	-639
Imports, c.i.f.	(-1,418)	(-2,022)	(-1,856)	(-1,870)	(-1,612)	(1,625)
Exports, f.o.b.	(798)	(954)	(923)	(992)	(916)	(986)
Invisibles and transfers (net)	234	382	347	408	272	287
Capital account	539	543	388	301	251	243
Private long-term capital	160	147	139	124	112	94
Official long-term capital	234	303	175	177	129	116
Short-term capital 2/	138	85	67	--	10	33
Allocation of SDRs	7	7	7	--	--	--
Unfinanced gap	--	--	--	--	--	91
Overall balance	154	-142	-198	-169	-173	-18
Financing (increase in assets -)	-154	142	198	169	173	18
Gross official reserves	-213	104	176	-26	40	-16
Use of Fund credit	56	44	23	195	133	34
Other liabilities	3	-6	-1	--	--	--
Memorandum items:						
Current account/GDP	-8.2	-12.6	-10.2	-8.0	-7.1	-5.9

Sources: Data provided by the Kenyan authorities; and staff estimates.

1/ As revised in EBS/82/91.
2/ Including errors and omissions and valuation adjustments.

IV. Report on the Discussions

The consultation discussions began at a time when the Kenyan authorities had not yet fully reviewed the events of the 1981/82 fiscal year, and the policies for 1982/83 had not been fully determined. The authorities recognized that economic conditions had deteriorated: the balance of payments constraint had tightened, budgetary pressures were once again emerging, the inflation rate remained stubbornly high, and the outlook for growth was uncertain. The need to reinforce the policies in place during 1981/82 in order to meet the medium term adjustment objectives of the Government had become evident. Yet the Government was also contending with social and political pressures to loosen economic and financial restraints. The attempted coup in early August, and its aftermath clearly worsened the outlook for the economy, stressing the need for convincing additional policies, but also making the political and social situation more precarious.

Apart from reviewing recent economic developments, the discussions centered on the progress made in implementing the structural adjustment required to promote more rapid economic growth in the medium term, within the constraints set by the balance of payments and Kenya's foreign borrowing capacity. Special consideration was given to strengthening these endeavors and there were discussions on the type and magnitude of the new measures which were needed.

1. Development policies and the allocation of resources

The Kenyan representatives pointed out that substantial progress had been made in the course of 1981/82 in implementing the adjustment program. They recognized that further progress was required in the coming years, but felt that the continuing pressures on the balance of payments were to an important degree the result of a continued weak international economy and Kenya's inability to utilize more of the available foreign aid given the shortage of counterpart funds brought about by the fiscal adjustment.

The Kenyan representatives indicated that Sessional Paper No. 4 of 1980, on which their present adjustment efforts are based, attaches great importance to the implementation of a new industrial strategy, which, in addition to improving the efficiency and competitiveness of the sector, would create the conditions for launching major export oriented expansion. The exchange action undertaken in 1981, together with the reform of the import system, was designed to facilitate this objective. The Kenyan representatives pointed out that despite the recently established incentives Kenyan industrialists were continuing to have difficulties in expanding nontraditional exports. This resulted from the weaknesses in the economies of neighboring countries, which had traditionally provided important markets for Kenyan industrial products, and also from the continued recessionary conditions in major industrialized partner countries. In addition, increasing exports to markets like the Middle East, which were still

growing, had become difficult as a result of limited transportation links between Kenya and these countries. Given the institutional and structural issues involved, the Kenyan representatives felt that specific measures to overcome these problems were needed rather than continued reliance on generalized macroeconomic tools. Certainly, in their view, an improvement of the world economy would go a long way toward ameliorating their situation. The Kenyan representatives pointed out that the Government was committed to expedite a study of export incentives. A comprehensive incentive package had not yet been prepared, but the authorities hoped to receive technical assistance from the IBRD in completing their proposals which they hoped would be made public during the present fiscal year. The Kenyan representatives said that the impact of the suspension of the export compensation scheme in June 1982 had been considerably more negative than estimated, with some affected firms curtailing operations. This had led to an appreciable increase in urban unemployment, particularly as supplier firms had also been affected. Consequently, on September 21, 1982, a revised compensation scheme was reintroduced retroactive to June 18, 1982. Exporters of nontraditional products would now be entitled to a compensation payment of 10 per cent of the export value compared to 20 per cent under the old arrangement. In addition, the increase in exports over a year earlier would be entitled to a compensation payment of 25 per cent. In fiscal year 1982/83 the scheme was expected to cost about SDR 15 million or the equivalent of 1.5 per cent of estimated 1983 exports with payments concentrated in a limited number of firms.

Although the Kenyan representatives stressed the need for more specific incentives targeted on the nontraditional exports, they also recognized the need for maintaining a competitive exchange rate. Consequently, in recognition of the relative price developments in Kenya during 1982, the Kenya shilling was cumulatively devalued by 15 per cent with respect to the SDR (foreign currency terms) between December 10, 1982 and early January, 1983. Moreover, a flexible exchange rate policy will be pursued henceforth aimed at keeping the real effective exchange rate at about its present level.

The Kenyan representatives pointed out that significant progress had been made in 1981-82 in simplifying the import system. Letters of no objection (a system by which local manufacturers had to declare their concurrence before import licenses were granted for imports competing with their production) were eliminated, new import schedules were drawn up and put into effect, and wide ranging increases in import tariffs were implemented in the 1980/81 and 1981/82 budgets. In June 1982 20 per cent of the items still on the restrictive schedules were transferred to the unrestricted schedule. The Kenyan representatives said that all these measures had been put into effect at a time when the balance of payments continued to be under pressure and that the pace of reform turned out to be too fast given the low level of gross international reserves. Consequently, following the attemped coup, import approvals, which had already been administratively delayed, were further controlled to ascertain that there would be

adequate foreign exchange to meet debt service obligations, pending the Government's attempt to obtain additional foreign exchange. The Kenyan representatives emphasized that the Government was committed to return to a freer import system and to remove the remaining quantitative restrictions over the next few years. However, they cautioned that, without the support of an adequate level of international reserves, they had to proceed cautiously.

The Kenyan representatives pointed out that the improvement in weather conditions together with the maintenance of adequate producer prices had resulted in a bountiful harvest in 1982. They indicated that the increased availability of foodstuffs should play an important role in decelerating the inflationary pressures evident earlier in 1982. However, the increased output had resulted in a larger need than programed for financing the rebuilding of Kenya's emergency maize stocks, which had been drawn down during the drought years. Moreover, output had exceeded Kenya's consumption and storage capabilities, and there would be a need to export maize and beans. Given the established pricing policies, such transactions will be carried out at a loss and will need budgetary support. However, this is not expected to be a recurring problem.

Despite the progress recorded in 1981/82, the Kenyan representatives felt that further improvements in the agricultural sector were needed. Kenya's population is growing at one of the highest growth rates (3.8 per cent) in the world, and Kenya possesses less than ample agricultural resources (only 20 per cent of the land is arable). The strategy in the agricultural sector included the maintenance of reasonable producer prices and export incentives, and increased development outlays in the agricultural sector, including the priority status of agriculture in credit guidelines. They added that the thrust of these policies was aimed at keeping Kenya self-sufficient in foodstuffs and also permitting a larger export of agricultural products.

The Kenyan representatives explained that the implementation of the Fourth National Development Plan (1979-1983) had lagged, largely as a result of the unexpected weaknesses in the balance of payments and the need to adjust the budget. A new development plan, which will emphasize the continued adjustment of the economy, is in preparation. They cautioned that the continued difficulties in the budgetary field, particularly the need to reduce the overall budgetary deficit further, would remain the main stumbling block in the implementation of a larger development plan.

The Kenyan representatives indicated that in the past government policy had been to only allow wage increases which compensated for part of the increases in prices. They added that they would continue to follow this policy, particularly at this time of strong price pressures.

2. Budgetary policies

The Kenyan representatives said that there had been an important improvement in expenditure control in 1981/82. They explained that the support which the tight expenditure policy had received from the Cabinet had been a key element in its attainment. Moreover, the expenditure monitoring procedures, for which technical assistance had been received from the Fund, had allowed the Government to track expenditure trends better. In 1981/82 the growth of total expenditures had been kept to 3 per cent, representing a substantial decline in real terms. In terms of GDP, total expenditures fell from 35.8 per cent in 1980/81 to 31.5 per cent in 1981/82. Although total expenditures had been kept at the programed level, total recurrent expenditures had been slightly higher, while development expenditures had been somewhat smaller. The Kenyan representatives explained that the containment of government expenditures had not been without its drawbacks. With regard to current expenditures, it had meant that the productivity of many ministries had been adversely affected. With respect to development expenditures, various projects were held back, canceled, or spread over a longer period of time, with an adverse effect on Kenya's development efforts. Nevertheless, they realized the overriding importance of correcting the destabilizing effect of large budgetary deficits, and were satisfied with the progress made in 1981/82 in this regard.

The Kenyan representatives explained that the 1982/83 budget initially announced in June 1982 needed to be revised as a result of the coup attempt in August and other factors. In framing the original and the revised versions of the budget, one of the main objectives was to continue the adjustment process by means of a further, meaningful reduction in the overall deficit. Moreover, the report of the Working Party on Government Expenditure, which has been finalized and accepted by the Government, calls for a reduction of the involvement of Government in the economy, including the sale or closure of some public enterprises. It also highlights the need for improved management in the public sector to raise efficiency and limit expenditure.

Given the findings of the Working Party, the revised 1982/83 budget seeks to further restrict the growth of government expenditure. Consequently, the 1982/83 budget as revised and taking into account the most recent exchange rate action, calls for an increase of only 11.0 per cent in total expenditure and a further reduction in the ratio of expenditure to GDP to about 29.6 per cent from 31.5 per cent in 1981/82.

In the first quarter of the fiscal year, revenue collections were lower than expected due to the reduced level of imports and were expected to continue to be depressed for a few more months. Consequently, on December 3, 1982 new discretionary measures expected to yield about K Sh 0.4 billion in the remainder of the fiscal year were introduced. Given these measures, revenues are now forecast to reach K Sh 18.0 billion in fiscal year 1982/83, representing an increase of about 15 per cent from

the previous fiscal year. Additional foreign grants have been obtained this year, following a special appeal made by Kenya after the attempted coup. Consequently, grants are expected to total K Sh 1.5 billion, compared to K Sh 0.9 billion in 1981/82, with total revenues and grants estimated at K Sh 19.5 billion, an increase of about 17.5 per cent from the previous fiscal year.

Unlike the previous year, the budget includes estimates of possible supplementaries and takes account of the subsidies required by the National Cereals and Produce Board (NCPB) for the export of surplus agricultural production estimated at K Sh 240 million. Taking into account these elements, the revised budget incorporates a further decline in the ratio of the overall deficit to GDP to about 4.7 per cent. The Kenyan representatives explained that the foreign financing of the budget had been carefully reviewed, with the inclusion only of resources which are assured, and represents a more realistic estimate than those made in the past. Thus, for example, the second tranche of the World Bank's Structural Adjustment Loan (SAL) has been excluded to take account of possible delays. Net foreign financing is estimated at K Sh 1.9 billion, leaving K Sh 1.8 billion to be financed domestically, of which K Sh 1.0 billion will come from net banking system credit, a sum equivalent to 5.5 per cent of the stock of money and quasi-money at the start of the fiscal year, compared to 14.6 per cent in the previous fiscal year. With the reduction in the deficit which will be continued in 1983/84, the budgetary imbalances will have been reduced to the equivalent of about 4.5-4.0 per cent of GDP, and more effort will be directed toward improving the structure of government expenditure.

The continued implementation of the recommendations of the report of the Working Party on Government Expenditure is expected to lead to further expenditure savings and the trimming down of the government sector. With the approval of the State Corporation Act expected in 1983, a central monitoring of public enterprises will be established and improved management will result. Also, it will lead to the transfer of ownership of some enterprises to the private sector and the closure of others.

3. Monetary developments and policies

The Kenyan representatives said that during 1981/82 significant progress was made in more closely coordinating monetary and fiscal policies. The overall government deficit was reduced substantially, and, although the net utilization of bank credit by the Government was above the estimates made earlier, efforts were made to link these developments with the overall level of domestic credit. The Kenyan representatives pointed out that the better-than-expected performance of the economy, particularly in the agricultural sector, had generated a larger demand for domestic bank credit than originally foreseen. During the fiscal year private sector credit expanded by 16.0 per cent, compared to 9.5 per cent the previous year. Demand for credit had been larger than the credit granted, and the Central Bank had to take special care to limit the growth of private sector credit

by keeping the banking system's liquidity tight. However, despite these efforts, private sector credit expanded more rapidly than expected by the authorities and its growth rate contributed to the nonobservance of the performance criteria established for end-June 1982. The Kenyan representatives expressed the view that given the large number of financial institutions and the sizable amount of freedom they enjoyed in the Kenyan context, it was difficult for the Central Bank to fine tune the expansion of credit, particularly as commercial banks tended not to use the rediscount facilities of the Central Bank. However, in order to prevent difficulties in the future, monitoring of commercial bank activities would be improved in 1983.

The Kenyan representatives said that, given the external difficulties and domestic price pressures, it was extremely important to continue with cautious financial policies in 1983. Consequently, they were aiming for a lower increase in domestic credit than estimated for 1982, so that money and quasi-money growth would be below the estimated expansion in nominal income. This objective would be made possible because of the reduction in net credit expected to be absorbed by the budget. Therefore, private sector credit was targeted to expand only slightly less than in 1982.

The Kenyan representatives explained that nonbank financial intermediaries continued to grow more rapidly than commercial banks in 1982, when they accounted for about 25 per cent of total financial system deposits at the end of September compared to 19 per cent at the end of 1977. During 1981 the Kenyan authorities moved further to control the activities of nonbanks. Although nonbanks continued to be allowed to offer higher rates for deposits than commercial banks, the margin is better regulated now and there is a stricter enforcement of credit allocation policies by the Central Bank, including the requirement for a minimum allocation of credit to agriculture. During the year the Central Bank moved to enforce the liquidity ratio of nonbanks strictly, with a salutary effect on their purchases of Treasury bills. However, the large number of nonbanks makes it difficult for the Central Bank to exercise continued strict control of this sector, given its available human resources.

The Kenyan representatives explained that interest rates had been increased by about 5-6 percentage points between June 1980 and September 1981. They felt that the resulting level of domestic interest rates had been a hindrance for domestic companies, limiting their expansion plans and their profit margins. Particularly hard hit had been exporters of agricultural products whose profit margins had also been affected by low commodity prices. According to the Kenyan representatives, too frequent changes in the interest rate structure were disruptive of the flow of business activity. However, the Kenyan representatives also felt that, given the continued high level of domestic inflation and balance of payments difficulties, interest rates needed to be kept under continuous review and adjusted from time to time. They said that the domestic inflation rate would begin to fall in the second half of 1982 and that

interest rates should be adjusted when a clearer indication was available on the trend in prices.

On December 10, 1982 the Central Bank of Kenya announced an increase in the minimum savings rate of 2.5 percentage points. This will have an upward effect on other rates, specially time deposit rates, which will go up by no less than 3 percentage points. Consequently, the minimum savings rate is now 12.5 per cent, while time deposit rates range between 13.75 per cent and 15.50 per cent. The maximum lending rate was also raised by 2 percentage points to 16 per cent. Given that the increase in consumer prices in 1982 was 14 per cent, most time deposit rates and the lending rates are now positive in real terms, while the savings rates are only marginally negative.

4. External policies and developments

As noted above, the current account deficit was estimated to have fallen by about 3 percentage points to around 7 per cent of GDP (about 8 per cent excluding grants), a larger amount than expected earlier. The Kenyan representatives recognized that further adjustment efforts were needed in each of the next two years in order to achieve a sustainable balance of payments position in the medium term. In this regard they felt that the measures recently adopted with respect to exchange and interest rates and budgetary policy should help to bring this about. The Kenyan representatives said that such an adjustment would be made easier through an expansion of exports. However, given the present conditions in the international market, particularly in neighboring countries, which are Kenya's traditional markets, a resurgence of export growth could not be expected in the short run. Therefore, while the Government would continue to provide adequate incentives to the export sector, through the exchange system and in other ways, in the short term the brunt of the adjustment would be on imports. The Kenyan representatives, however, were worried that too severe a reduction would have a substantial negative impact on the real economy, with difficult social and political results.

The Kenyan representatives pointed out that in 1982 imports had been reduced by 13 per cent in SDR terms, to a level of only 80 per cent of 1980 imports. A further reduction would be necessary in 1983, pending a more resurgent export performance. The Kenyan representatives explained that they expected the current account deficit to be reduced to less than 6 per cent of GDP in 1983, with exports rising by about 6.5 per cent in SDR terms and imports falling slightly. However, even this target of the current account was not yet fully financed. At the present time, the current account deficit was estimated at SDR 352 million, compared to SDR 429 million in 1982. It was expected to be covered with SDR 93 million in government long-term capital and SDR 150 million in private sector capital, leaving a gap of about SDR 109 million, plus SDR 43 million in repurchases to the Fund. The Government of Kenya had asked its major donors for special assistance in filling the remaining gap and some positive responses have already been received.

The Kenyan representatives explained that the current program is viewed as a fundamental step in an ongoing effort to reach a sustainable balance of payments position in 1985. The objectives envisaged for 1985 include a reduction of quantitative restrictions on imports, a current account deficit of about 5 per cent of GDP, or to the level financed by the medium- and long-term capital flows normally expected by Kenya, a reserve position with gross official reserves representing at least six weeks of imports, and an improvement in the growth of industry and agriculture. To attain these goals, additional adjustment will be necessary, including the reduction of the budget deficit to about 4 per cent (including grants), or a level largely financed by medium- and long-term foreign development assistance, the adequate financing of private sector activity, and the maintenance of satisfactory export and production incentives through an appropriate exchange rate and realistic producer prices.

Kenya's public and publicly guaranteed external debt has traditionally been low but has grown to be more of a burden in recent years and stood at about US$2.6 billion (39 per cent of GDP) in 1982, of which only about one-third is on commercial terms. The Kenyan representatives indicated that although additional financing is required in the future, such borrowing will be carefully reviewed, so that the debt service ratio does not rise beyond a manageable level. The debt service ratio has risen from 12 per cent in 1980 to an estimated 22 per cent in 1982. Including the anticipated borrowings for the upcoming years, this ratio is expected to rise to 23 per cent in 1984 and stabilize thereafter (Table 6).

The Kenyan representatives explained that the advance import deposit scheme put into effect in 1979 had been reduced in steps and would be abolished by January 31, 1983. They expressed regret that the tight foreign exchange situation has necessitated the retention of restrictions on dividend remittances and the continuation of foreign exchange rationing. They said that there were no payment arrears with respect to these outlays and that the current policy is that companies will be permitted to remit dividends as soon as adequate foreign exchange is available for this purpose. Although an effort has been made in this regard, some delays still exist. The practice of requiring fees for the purchase of foreign exchange to buy airline tickets was abolished during 1982.

The import licensing scheme has required a license from the Import Quota Allocation Committee (IQAC) and an allocation of foreign exchange from the Central Bank. When the new import system was introduced in late 1981, the two decisions were coordinated. However, to the extent that the licenses issued were restricted, a trade restriction existed. During the last six months of 1982 the level of licenses issued by the IQAC was high in relation to foreign exchange availabilities and the Central Bank found it necessary to delay approving foreign exchange allocations, thereby creating a backlog of licenses waiting for allocations and an exchange restriction. The representatives explained that they plan to eliminate these delays as the licensing backlog is brought under control and plan

to liberalize the licensing and exchange allocation process as quickly as the adjustment in the balance of payments and foreign exchange reserves allows.

Table 6. Kenya: Debt Service Payments on Medium- and Long-Term Public and Publicly Guaranteed Debt, 1982-86

(In millions of SDRs)

	Debt service on:				
	Existing debt, excluding IMF	IMF	Additional financing required 1/	Total debt	Debt service ratio 2/
1982	300	41	--	341	22.1
1983	295	65	15	375	22.4
1984	304	96	27	427	23.2
1985	326	116	35	477	23.5
1986	311	127	45	483	21.6

Sources: Data provided by the Kenyan authorities; IBRD External Debt Division; IMF, Treasurer's Department; and staff estimates.

1/ Under medium-term scenario.
2/ In per cent of exports of goods and nonfactor services.

V. Staff Appraisal

Kenya made significant progress in adjusting its economy in 1981/82, after several years of partial and unsuccessful measures. The disequilibria in the budget and the balance of payments were substantially reduced, although the continued recession in the world economy made Kenya's adjustment needs more difficult. Complete success in attaining the objectives set for 1981/82 was not possible, resulting in the credit ceilings on the one-year stand-by arrangement initiated in January of 1982 being exceeded at the end of June, after drawings of SDR 90 million. Measures to readjust the program were also frustrated by delays in preparing a realistic 1982/83 budget and by a coup attempt which occurred in August, while various domestic policies, such as the exchange and interest rates, were allowed to get out of line and were not promptly corrected. There have also been delays in formulating a coherent export incentive package.

Despite the progress achieved during the year, in order to keep to the objective of attaining a sustainable balance of payments by 1985, it is necessary for the authorities to restrengthen their efforts in 1983. After the political difficulties faced in August, the Government of Kenya asked for extraordinary assistance from its main donor countries to make up for the losses suffered during the coup attempt and to help the economy return to its previous adjustment track. Some of the donors have already replied favorably to Kenya's request, and an important proportion of the required resources has already been agreed. On the basis of the expected assistance, at the end of November 1982 the authorities completed a stabilization package aimed at further reducing the domestic and external disequilibria facing the Kenyan economy.

In November-December of 1982, after a delay of several months, the Kenyan authorities very convincingly implemented a package of measures designed to strengthen their adjustment effort. The staff concurs with the authorities' views that the adjustment path they chose in 1981 remains viable, but that additional measures were required to bring it back on track. The authorities' efforts to transfer resources to the export sector to generate a resurgence of growth and balance of payments adjustment was negatively affected by the appreciation of the real exchange rate during 1982. This has now been corrected by a depreciation of the exchange rate in early December by 13 per cent and a further adjustment of 2 per cent carried out in early January 1983. The staff welcomes the authorities' commitment to follow a more flexible exchange rate policy. The impact of the exchange rate measures on the level of exports will take time to bear fruit, particularly if the world economy continues depressed. However, valuable adjustment will be carried out in reducing import demand. In the past the authorities have limited the level of imports to available foreign exchange resources through use of ad-hoc restrictions. Although these have proven to be effective in reducing overall imports, they have also caused a misallocation of resources and resulted in problems for the private sector in planning correctly for investment and production. The

staff agrees that the recourse to more generalized means of import control such as through the exchange rate and tariffs, is a more adequate tool to deal with these problems. Although the adjustment of the import level through this method may also prove painful, in the end a stronger and more viable production framework will have been established, which will help in improving the economy's growth rate.

Through more rigorous expenditure control measures, the Kenyan authorities were able to reduce the overall budgetary deficit substantially in 1981/82. Although the credit ceilings agreed in the stand-by arrangement with the Fund were exceeded at the end of June, the reduction in the overall deficit in that year, equivalent to three percentage points of GDP, represents a meaningful and significant effort by the Kenyan authorities toward fiscal adjustment. The revised 1982/83 budget, which includes additional revenue and expenditure measures, is a comprehensive and convincing package. The implementation of the budget will require improved monitoring of developments in order to make timely adjustments, as required. The procedures for the timely disbursements of the agreed foreign aid will also be important. Successful execution of the budget would mean an almost 2 percentage point reduction in the ratio of the overall deficit to GDP to a level of about 4.7 per cent of GDP. Thus, over a two-year period Kenya would have adjusted its overall deficit to GDP ratio by 5 percentage points. The required domestic financing of the budget is consistent with the requirements of more judicious allocation of domestic credit resources.

The recent report of the Working Party on Government Expenditure provides the authorities with the basis for bringing a degree of improved management and greater efficiency in the operations of public enterprises. The report has been accepted as government policy and the staff is encouraged that the authorities expect to begin its implementation in 1983.

The staff feels that the degree of caution shown in the stated credit policies for 1983 is essential to promote the containment of price increases while providing needed credit resources for the productive sectors. The recent upward adjustment in interest rates to positive real levels further exemplifies the authorities' commitment toward reducing the domestic disequilibriums. The staff agrees that the authorities should review interest rates on a continuous basis to ascertain that they continue to be appropriate in a rapidly changing environment.

On the basis of the measures already in place, the current account deficit of the balance of payments is expected to be further reduced to the equivalent of less than 6 per cent of GDP in 1983 from over 7 per cent in 1982. Thus, over these two years, there would be an adjustment in this ratio of over 4 percentage points of GDP. This represents a significant accomplishment, although partly influenced by quantitative restrictions, which will go a long way toward allowing the authorities to meet their medium-term goal of reaching a sustainable balance of payments position by 1985. Given the slow growth of exports, largely reflecting deteriorating

terms of trade and a difficult world economic environment, the bulk of the adjustment has involved a reduction of imports of about 20 per cent in SDR terms in the last two years. Despite the major improvements expected on the current account deficit in 1983, an unfinanced gap remains after taking into account the known capital flows as of the end of 1982. On the basis of the expected additional assistance to be received in the near future, the Kenyan authorities would be in a position to finalize their economic and financial program for 1983 and request additional assistance from the Fund in the form of a new stand-by arrangement.

The staff feels that the evolution of the balance of payments in the medium term will be highly influenced by the policies which the authorities follow with respect to the import system, the exchange rate, interest rates, producer prices, and the budget. The prompt correction of any divergencies which may arise will dictate whether the objectives for the medium term can be accomplished. In this regard, the staff feels that it is important to assure that the export incentives are maintained and that impartiality of the import administration be continued. The staff feels that the most recent exchange rate action should provide adequate incentives for a resurgence of export production, and therefore the incentives so far attained should be preserved by a more flexible exchange rate policy allowing the export compensation scheme to be eliminated as soon as possible. Substantial progress had been made in simplifying and liberalizing the import system. Unfortunately, lack of adequate foreign exchange resources forced the authorities to retrench from the progress achieved earlier. The staff feels that, as quickly as foreign exchange resources permit, the authorities should regain the ground which had been attained in 1982. It welcomes the final removal of advance import deposits effective January 31, 1983, which will eliminate Kenya's only remaining multiple currency practice. Kenya still maintains exchange restrictions in the form of foreign exchange quotas on certain imports and restrictions on dividend and rental remittances. All exchange restrictions are subject to approval under Article VIII. In view of significant adjustment measures recently undertaken by the Kenyan authorities and the authorities' declaration that these measures are temporary, it is proposed to extend approval for the retention of the above practices.

VI. Proposed Decision

The following draft decision is proposed for adoption by the Executive Board:

1. The Fund takes this decision relating to Kenya's exchange measures subject to Article VIII, Section 2, and in concluding the 1982 Article XIV Consultation with Kenya, in the light of the 1982 Consultation with Kenya conducted under Decision No. 5329-(77/63), adopted April 29, 1977 (Surveillance over Exchange Rate Policies).

2. Kenya continues to retain restrictions on payments and transfers for current international transactions subject to approval under Article VIII, Section 2, as described in SM/83/___. In view of the budgetary, monetary, and exchange rate measures recently taken, and Kenya's declaration that these measures are temporary, the Fund extends approval for their retention until December 31, 1983.

Kenya: Relations with the Fund 1/

Status:	Article XIV
Date of membership:	February 3, 1964
Quota:	SDR 103.5 million
Fund holdings of currency as per cent of quota:	SDR 412.11 million (398.17 per cent of quota)
Of which: oil facility	SDR 0.39 million (0.37 per cent of quota)
compensatory facility	SDR 120.75 million (116.66 per cent of quota)
credit tranche ordinary resources	SDR 94.11 million (90.93 per cent of quota)
credit tranche supplementary financing	SDR 94.82 million (91.61 per cent of quota)
Holdings of SDRs:	SDR 13.97 million, or 37.8 per cent of net cumulative allocation (SDR 36.99 million)
Loan disbursements under the Trust Fund:	SDR 46.91 million
Direct distribution of profits from gold sales:	US$7.61 million
Gold distribution (four sales):	41,079.961 ounces
Exchange arrangement:	Pegged to the SDR at K Sh 13.963 = SDR 1
Intervention currency and rate:	U.S. dollar; K Sh 12.658 = US$1
Last consultation (Article IV):	April 1981, discussed by the Board August 31, 1981.

1/ As of December 31, 1982.

Financial Relations of the World Bank Group with Kenya 1/

Date of membership, IBRD: February 3, 1964

Capital subscription, IBRD: SDR 40.0 million

	World Bank loans			IDA credits and Third Window loans		
	Committed	Disbursed	Disbursement ratio	Committed	Disbursed	Disbursement ratio
	(In millions of U.S. dollars)					
Agriculture, livestock, and rural development	267.0	98.4	36.9	290.7	105.4	36.3
Education	10.0	3.4	34.0	73.6	22.8	31.0
Energy	144.4	130.5	90.4	--	--	--
Industry	65.0	36.4	56.0	24.5	2.2	9.0
Structural adjustment	60.9	--	--	117.9	55.0	46.7
Telecommunications	64.7	12.2	18.9	--	--	--
Transportation	233.5	100.5	43.0	67.1	67.1	100.0
Utilities	98.3	60.8	61.9	33.0	19.2	58.2
Total	943.8	442.2	46.9	606.8	271.7	44.8
Repayments	57.2	57.2		3.4	3.4	
Debt outstanding (including undisbursed)	886.6	385.0	43.4	603.4	268.3	44.5

IFC operations

Promotion of tourism facilities, capital markets, industrial development (pulp and paper, textiles, cement) and development financing. Total commitments now held by IFC amount to US$43.3 million, of which US$32.8 million have been disbursed.

Source: World Bank.
1/ Through September 30, 1982.

KENYA - Basic Data

Area, population, and GDP per capita

Area	580,000 square kilometers
Population: Total (1982)	17.2 million
Growth rate	3.8 per cent
GDP per capita (1982)	SDR 353

	1978	1979	1980	1981 Prel.	1982 Prel.
GDP (at 1976 market prices)					
Total (in billions of Kenya shillings)	34.1	35.5	37.1	38.6	40.3
Agriculture (per cent of total)	36	35	33	34	34
Manufacturing (per cent of total)	11	11	12	12	12
Government (per cent of total)	12	12	13	13	13
Annual real rate of growth (per cent)	7.2	4.1	4.3	4.1	4.5
Investment as per cent of GDP (at current market prices)	30	23	29	25	25
Prices (per cent change)					
GDP deflator	3	6	11	10	14
Cost of living index	9	15	13	20	14

	1978/79	1979/80	1980/81	1981/82 Estimate	1982/83 Budget
Central government finance 1/	(In billions of Kenya shillings)				
Recurrent revenue	10.0	12.0	14.3	15.7	18.2
Foreign grants	0.3	0.3	0.5	0.9	1.0
Total expenditure	14.0	15.8	19.8	20.9	22.2
Recurrent	9.6	11.4	14.1	14.6	15.1
Development	4.4	4.4	5.7	6.3	7.1
Adjustment	0.5	0.5	-0.8	--	--
Overall deficit (-)	-3.2	-3.0	-5.8	-4.3	-3.0
Foreign loans (net)	1.5	2.0	2.8	1.1	1.8
Domestic borrowing)net)	1.7	1.0	3.0	3.2	1.2
Of which: from banking system	1.1	--	1.6	1.7	0.8

1/ Fiscal year July 1-June 30.

KENYA - Basic Data (concluded)

	1978	1979	1980	1981	1982 Est.
Money and credit			(Per cent change)		
Domestic credit	35	13	13	26	29
Government	78	7	10	79	60
Private sector	37	10	20	11	14
Money and quasi-money	15	14	3	13	13

	1978	1979	1980	1981 Prel.	1982 Prel.
Balance of payments			(In millions of SDRs)		
Exports, f.o.b.	765	798	954	923	916
Imports, c.i.f.	-1,501	-1,418	-2,022	-1,856	-1,612
Trade balance	-736	-620	-1,068	-933	-696
Services and private transfers (net)	147	172	295	281	200
Current account balance	-589	-448	-773	-652	-496
Capital account (net)	428	595	624	447	323
Official	296	298	392	241	201
Private	132	297	232	206	122
Of which: long-term	122	160	147	139	112
Allocation of SDRs	--	7	7	7	--
Overall surplus or deficit (-)	-161	154	-142	-198	-173
Current account deficit as per cent of GDP	-12.4	-8.2	-12.6	-10.2	-7.1
Gross official foreign reserves (end of period)	283	496	392	216	155
In weeks of imports	10	18	10	7	6
External public debt					
Disbursed and outstanding (end of period)	1,121	1,461	1,897	2,203	2,345
Debt service as per cent of exports of goods and non-factor services					
Excluding the Fund	7.7	9.0	10.9	19.4	20
Including the Fund	8.2	11.8	11.7	20.6	22