

**FOR  
AGENDA**

SM/08/276  
Correction 1

September 9, 2008

To: Members of the Executive Board

From: The Secretary

Subject: **Kenya—Staff Report for the 2008 Article IV Consultation**

The attached corrections to SM/08/276 (8/20/08) have been provided by the staff.

**Factual Errors Not Affecting the Presentation of Staff's Analysis or Views**

**Page 1, text box, line 3:** after "... assisted the mission." insert "Mr. Gakunu and Ms. Gesami from the Executive Director's office participated in the policy discussions."

**Page 4, text table, row 1, cols. 3-4:** for "5.1" read "5.4", and for "10.6" read "11.2"

**Page 5, lines 1-2:** for "in the early summer" read "in mid-2008"

**Page 15, Table 1, line 9, footnote 2:** removed

**Page 18, row 7:** for "Commercial banks (net REPOS)" read "Commercial banks (net)"

Questions may be referred to Mr. Yang (ext. 34339) and Ms. Masha (ext. 35939) in AFR.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

Att: (5)

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## INTERNATIONAL MONETARY FUND

## KENYA

**Staff Report for the 2008 Article IV Consultation**

Prepared by the African Department  
(In consultation with other departments)

Approved by Saul Lizondo and Anthony R. Boote

August 20, 2008

<b>Mission Date and Team</b>	June 23–July 2, 2008. Messrs. Krueger (head), Atingi Ego, and Yang, Ms. Masha (all AFR), Ms. Everaert (FAD), and Mr. John (PDR). Mr. Rogers (Senior Resident Representative) assisted the mission. Mr. Gakunu and Ms. Gesami from the Executive Director's office participated in the policy discussions. The mission met with Prime Minister Raila Odinga, Finance Minister Amos Kimunya, Central Bank Governor Njuguna Ndung'u, other senior government officials as well as representatives of the business community, labor unions, civil society, and Kenya's development partners. The mission overlapped with a June 23–25 visit by Mr. Horton (FAD) to discuss the <i>Ex Post</i> Assessment of Kenya's Longer-Term Program Engagement with the Fund.
<b>Background Papers</b>	<i>Public Debt Thresholds for Kenya</i> and <i>Assessing Kenya's External Stability and Competitiveness</i> , which were discussed at a seminar with government officials.
<b>Exchange Rate Regime</b>	Kenya has accepted the obligations of Article VIII, Section 2, 3, and 4 and maintains an exchange system free of restrictions on payments and transfers for current international transactions.
<b>Economic Statistics</b>	Broadly adequate for surveillance purposes, but weaknesses in some areas hinder policy assessments, especially with respect to data on consumer prices, national accounts, and balance of payments (Information Annex).
<b>Last Article IV Consultation</b>	In concluding the 2006 consultation, Executive Directors commended the authorities for sound macroeconomic management and progress with structural reforms. They encouraged maintaining fiscal prudence, centering monetary policy around reserve money targets, and advancing structural and governance reforms. Policies (supported through November 2007 by a PRGF arrangement) were broadly in line with this advice, although there were at times slippages in meeting reserve money targets and advancing structural reforms.

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## EXECUTIVE SUMMARY

### **The Article IV discussions focused on the policy agenda of the new grand coalition government.**

In light of the disruptions that followed the December 2007 elections, the discussions centered around policies to strengthen growth and address some of the social issues that emerged from the crisis, while preserving macroeconomic stability. There was broad agreement on key, but not all, policy issues and on economic prospects:

- **Economic prospects:** after a contraction in the first quarter of 2008, an economic rebound is underway. Notwithstanding considerable risks, staff expected that GDP growth would exceed 7 percent in 2008/09 (July/June); the authorities were somewhat more optimistic than staff that this rapid growth would continue over the medium term.
- **External stability:** the real exchange rate has appreciated considerably and the external current account widened. However, there was broad agreement that this seemed to reflect foremost fundamental factors, and exports, capital inflows, and foreign reserves remain robust.
- **Fiscal policy:** fiscal policy in 2008/09 needs to provide adequate resources for infrastructure and social objectives while preserving macroeconomic stability. With this in mind, staff saw merit in reducing the fiscal deficit to around 4½ percent of GDP—not least in light of expected high growth and inflationary pressures. The authorities’ budget envisaged a higher deficit of about 5½ percent of GDP, and they emphasized infrastructure needs. The authorities were considering staff’s proposal to move to a fiscal anchor of total public debt (including domestic and external), in light of increased external borrowing opportunities. Concerning a planned sovereign bond issue, the authorities agreed that its size, costs, and maturity profile needed to be carefully evaluated in order to mitigate potential risks.
- **Monetary policy:** recent measures to tighten monetary policy were in the right direction in the face of high money growth and inflationary pressures—and more steps are urgently needed to prevent second-round effects of higher food and fuel prices.
- **Structural reforms and Vision 2030:** the government’s Vision 2030 aims for Kenya to reach middle-income status by 2030. There was agreement that for the private sector to play its envisaged lead role, substantial infrastructure investment as well as structural reforms would be required, including in the financial sector and on public financial management, governance, and trade policy.

The authorities agreed with the main findings of the *Ex-Post Assessment* and suggested several steps for a more effective and balanced partnership in the future.

## I. POLITICAL CONTEXT

1. **A political crisis followed the December 2007 elections, resulting in major economic disruptions.** During the crisis, over 1,000 people were killed and more than 350,000 (about 1 percent of the population) displaced. The disruptions affected also neighboring countries dependent on transport links through Kenya.
2. **Following an internationally intermediated power-sharing agreement, a grand coalition government assumed office in April 2008.** Under the agreement, President Kibaki remained in office and Mr. Raila Odinga assumed the newly-created position of Prime Minister. Constitutional and land reforms are among the challenging political tasks of the new government. On the economic front, the government submitted the 2008/09 budget and launched Vision 2030, a long-term vision for Kenya. However, there have also been challenges, and the Minister of Finance stepped aside in July to allow investigation of alleged misconduct related to a property sale, with allegations also leveled against the Governor of the Central Bank of Kenya (CBK).

## II. ECONOMIC CONTEXT

3. **After a long period of stagnation, growth rebounded strongly over the 5-year period preceding the recent crisis.** Important, if uneven, progress in addressing long-standing weaknesses—including in the areas of financial management, governance, and the business climate—underpinned the gains in recent years, combined with strong global growth. Kenya's GDP growth of 7 percent in 2007 was its highest in over two decades and caught up with growth in the rest of the East African Community (EAC).

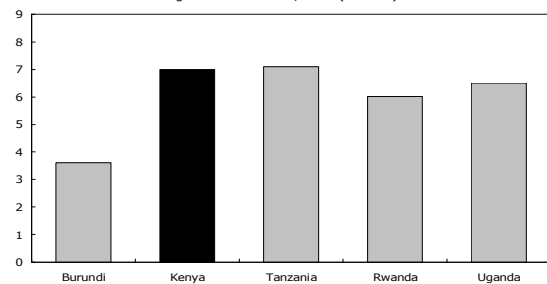
4. **Political instability took a toll on economic activity and exacerbated inflationary pressures in early 2008.** First quarter GDP contracted by 1.3 percent (year-on-year), with tourist arrivals down by over 50 percent and most sectors hampered by disruptions to supply chains and displacement of productive resources. The resulting shortages compounded inflation pressures arising from an earlier accommodative monetary policy as well as from rising international fuel and food prices. Inflation for the official headline consumer price index (CPI) was 26.5 percent in July (year-on-year); and even if the index appears to overstate inflation

Kenya: Comparative Macroeconomic Indicators  
(Annual percentage change)

	1990-2002		2003-2007	
	Real GDP Growth	Inflation	Real GDP Growth	Inflation
Kenya	2.1	14.2	5.4	11.2
Uganda	6.2	13.9	5.7	6.6
Tanzania	3.8	17.8	6.5	4.3
SSA - LIC <sup>1</sup>	3.7	14.3	6.1	8.8
All Low Income	4.0	41.1	7.6	8.9

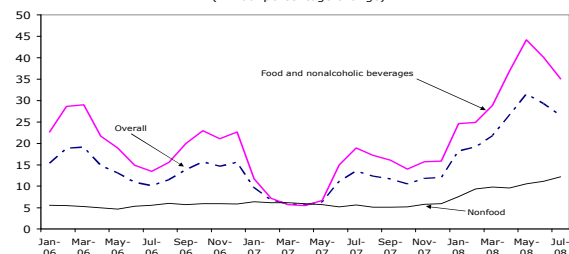
Sources: Country authorities; and IMF staff estimates.

<sup>1</sup> Sub-Saharan Africa Low-Income Countries.  
Regional GDP Growth, 2007 (Percent)



Sources: Country authorities; and IMF staff estimates.

Kenya: Official Consumer Price Indices  
(Annual percentage change)



Source: Kenya National Bureau of Statistics.

due to some methodological issues (see Box 1), correcting for the overstatement still left estimated inflation at around 15 percent in mid-2008—well above the authorities' target of 5 percent.

### Box 1. Upward Bias in the CPI Inflation Rate

Kenya's official CPI imparts an upward bias to "true" inflation. This mainly reflects the chain-linked Carli index used to aggregate individual prices. The Carli index is not "transitive" (if a price increase in one period is reversed in the next, the index would still show an overall increase) and, especially in its chain-linked form, it creates a substantial upward bias, particularly when prices are volatile. For this reason, the International Labor Organization's CPI Manual (2004) strongly advises against using it for compiling the CPI.

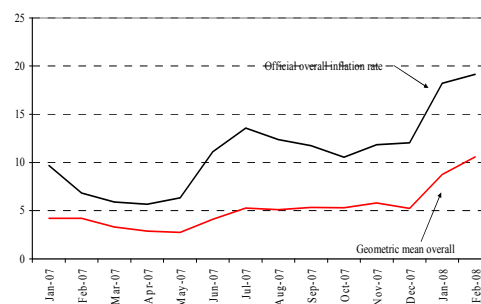
To provide a rough sense of the magnitude of the bias, staff applied one of the recommended methodologies (the so-called Jevons index). The results suggest that the overall CPI was overestimated over the past 1½ years by a factor of about 2. In line with the recommendations of a recent STA mission, the Kenya National Bureau of Statistics plans to switch to a formula consistent with international best practices later in 2008, together with a rebasing and reweighing of the CPI basket.

Illustration of Upward Bias in the Carli Index

	May	June	June/May
Price	(Shillings)	(Shillings)	(Ratio)
Item A	20	25	1.25
Item B	25	20	0.8
<b>Mean of prices</b>	(Shillings)	(Shillings)	(Ratio)
Arithmetic	22.5	22.5	1.0
Geometric	22.4	22.4	1.0
<b>Derived indices</b>	(May = 100)	(May = 100)	(% change)
Carli	100	102.5	2.5
Dutot	100	100	0.0
Jevons	100	100	0.0

Source: IMF staff calculations.

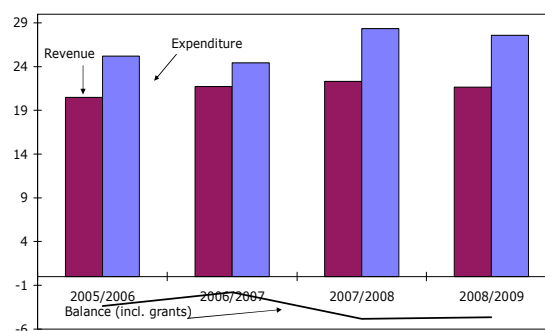
Comparison of CPIs: Official Series and Geometric Mean Estimates  
(Annual percentage change)



Sources: KNBS for official series, and IMF staff for geometric mean estimates.

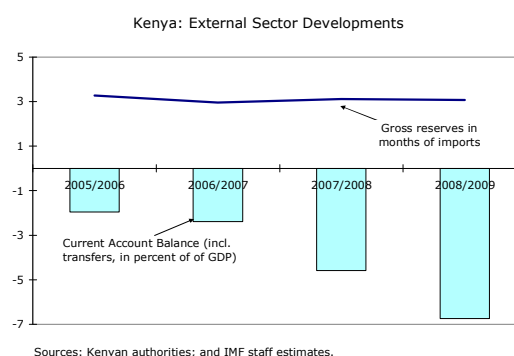
5. **The fiscal deficit (including grants) reached 4.8 percent of GDP for 2007/08 (July/June)—below the original budget target but more than twice the deficit of the previous year.** The lower-than-budgeted deficit reflected mainly a shortfall in foreign-financed development spending, which had been anticipated under the now expired PRGF program (Table 2). Strong revenue performance benefited from continued tax administration improvements, a buoyant economy through end-2007, which boosted particularly income tax collections, and a 0.3 percent of GDP one-off transfer of collected road fees. Privatization receipts increased sharply to almost 4 percent of GDP. As a result, domestic financing declined and public debt fell below 40 percent of GDP.

Kenya: Fiscal Developments (In percent of GDP)



Sources: Kenyan authorities; and IMF staff estimates.

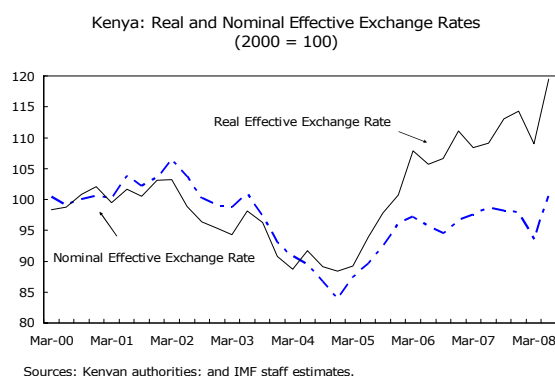
6. **The external current account deficit almost doubled in 2007/08 to 4½ percent of GDP.** The widening deficit largely reflected the impact of higher oil prices, while exports held up well despite a strong shilling (see below). Strong capital inflows resumed after the crisis—partly driven by a heavily oversubscribed initial public offering (IPO) of Safaricom—and gross reserves increased.



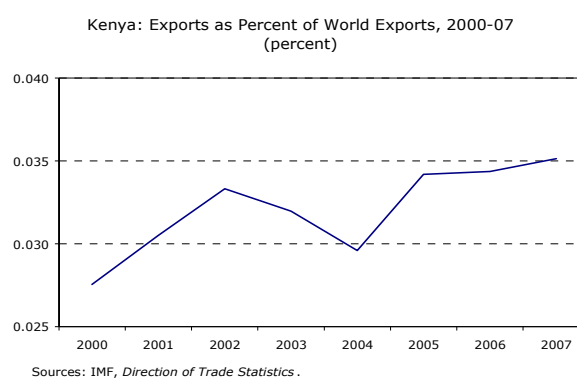
### III. POLICY DISCUSSIONS

#### A. External Stability

7. **Indicators of external performance provide mixed signals.** The shilling appreciated by almost 32 percent in real effective terms since end 2004 (based on a corrected CPI series), a period over which the terms of trade deteriorated markedly and the current account deficit increased. However, export values have expanded somewhat faster than global exports, financial and FDI inflows have increased, external debt has declined and is fairly low, and reserves are at historically high levels.



8. **Overall, the authorities agreed with staff that the exchange rate level appeared broadly appropriate (Box 2).** The shilling's real appreciation since 2005 was likely driven by improving fundamentals, including rising tea and coffee prices, a strengthening net foreign asset position, and improved productivity—all of which helped attract large private financial inflows. Even so, there was agreement that the widening current account deficit entailed risks, and that developments in competitiveness and financial flows needed to be monitored carefully.



9. **The authorities considered that the managed float exchange rate system had served Kenya well.** Interventions in the foreign exchange market have been largely limited to meeting foreign reserve and monetary targets and reducing exchange rate volatility, with the *de facto* and *de jure* exchange rate regimes classified as a managed float. The authorities noted that further structural reforms would be important to keep the current account deficit at a sustainable level. The projected



Table 1. Kenya: Selected Economic Indicators, 2005/06-2012/2013

	2005/06	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
	Estimate			Projection				
(Annual percentage change, unless otherwise indicated)								
<b>National accounts and prices</b>								
Real GDP growth (market prices)	6.1	6.7	3.9	7.2	6.0	6.6	6.5	6.5
GDP deflator (average) <sup>1</sup>	6.4	5.5	12.0	11.6	4.8	5.1	5.1	5.1
Consumer price index (annual average) <sup>1</sup>	11.1	10.4	18.5	14.5	5.0	5.0	5.0	5.0
Consumer price index (end of period) <sup>1</sup>	10.9	11.1	29.3	8.0	5.0	5.0	5.0	5.0
Export volume, goods and services	6.4	4.7	3.7	6.3	10.2	9.6	9.7	9.5
Import volume, goods and services	16.7	15.2	3.5	1.1	7.8	9.6	9.8	9.4
Terms of trade, goods	-5.8	-3.0	-11.9	-7.6	-2.3	0.3	0.3	1.1
Ksh per US \$ exchange rate (end of period)	69.3	62.6	64.6	...	...	...	...	...
Nominal effective exchange rate (- depreciation; end of period)	4.0	5.9	3.0	...	...	...	...	...
Real effective exchange rate (- depreciation; end of period)	11.8	14.2	7.8	...	...	...	...	...
<b>Money and credit</b>								
M3 (broad money, end of period)	18.0	16.0	18.3	21.8	17.2	16.2	16.1	16.1
M3X (broad money and foreign currency deposits, end period)	14.9	18.9	19.4	17.3	16.0	15.2	15.2	15.2
Reserve money (end of period)	14.0	17.5	19.6	15.0	14.6	14.1	14.1	14.1
(In percent of GDP, unless otherwise indicated)								
<b>Investment and saving</b>								
Investment	18.0	19.1	20.0	22.0	22.1	22.4	23.1	23.6
Central government	4.2	4.6	6.7	7.4	7.3	7.4	7.8	7.8
Other	13.8	14.5	13.3	14.6	14.8	15.0	15.3	15.8
Gross national saving	16.0	16.7	15.4	15.3	16.6	17.2	17.9	18.3
Central government	0.0	2.0	1.2	1.8	2.3	2.4	2.3	2.1
Other	16.0	14.8	14.3	13.5	14.3	14.8	15.6	16.2
<b>Central government budget</b>								
Total revenue	20.5	21.7	22.3	21.6	21.6	21.6	21.6	21.6
Total expenditure and net lending	25.2	24.4	28.3	27.6	26.7	26.7	27.3	27.5
Overall balance (commitment basis) excluding grants	-4.7	-2.7	-6.0	-5.9	-5.2	-5.2	-5.7	-5.9
Overall balance (commitment basis) including grants	-3.4	-1.8	-4.8	-4.6	-3.8	-3.8	-4.2	-4.3
Net domestic borrowing	1.9	2.0	1.1	2.2	2.5	2.5	2.6	2.7
Total donor support (grants & loans)	1.9	1.5	2.5	2.6	2.8	2.9	3.3	3.3
<b>Balance of payments</b>								
Exports value, goods and services	26.6	25.5	24.9	25.2	25.1	25.2	25.4	26.9
Imports value, goods and services	35.9	35.2	36.6	39.2	37.6	37.1	36.9	38.6
Current external balance, including official transfers	-2.0	-2.4	-4.6	-6.7	-5.4	-5.2	-5.2	-5.3
Current external balance, excluding official transfers	-2.3	-2.4	-4.8	-6.7	-5.4	-5.2	-5.2	-5.3
Gross international reserve coverage								
in months of next year imports (end of period)	3.3	2.9	3.1	3.1	3.1	3.1	3.1	3.2
<b>Public Debt</b>								
Total government debt (end of period)	45.1	42.3	38.8	38.0	38.6	38.6	38.7	39.6
of which: external debt	26.7	22.8	20.3	20.3	20.2	19.6	19.2	19.4
NPV of central government debt (end of period)	37.9	35.6	32.5	31.9	32.8	32.9	33.2	34.0
of which: NPV of external debt	19.5	16.1	14.0	14.2	14.3	14.0	13.7	13.8

Sources: Kenyan authorities; and IMF staff estimates and projections.

<sup>1</sup> Up to 2007/08, GDP Deflator and Consumer Price Index are overestimated (see Box 1).

Table 2a. Kenya: Central Government Financial Operations, 2005/06-2012/13 <sup>1/</sup>

	2005/06	2006/07	2007/08		2008/09		2009/10	2010/11	2011/12	2012/13
	Actual	Actual	EBS/07/124	Staff	Budget	Staff	Projection			
			Projection		Projection					
(In billions of Kenyan shillings, unless otherwise indicated)										
Revenue	311.3	373.0	427.2	442.2	512.7	513.7	569.3	637.6	715.8	801.5
Income tax	113.9	131.5	151.8	165.1	194.0	190.5	211.8	237.1	265.3	296.8
Import duty (net)	20.5	27.5	32.3	32.9	36.5	38.6	42.0	46.6	53.2	60.4
Excise duty	50.3	56.4	65.6	61.9	72.9	72.4	80.9	91.2	102.8	114.7
Value-added tax	76.3	96.3	112.2	111.9	133.9	135.4	149.8	167.6	188.2	210.6
Investment income	2.2	6.6	2.7	3.1	5.7	5.7	6.3	7.1	7.9	8.8
Other	25.2	28.4	30.6	29.8	34.7	35.9	39.9	44.8	50.1	56.1
Ministerial and Departmental Fees (AIA)	22.8	26.4	32.0	37.4	35.1	35.1	38.6	43.2	48.4	54.1
Expenditure and net lending	382.8	419.5	557.3	562.0	673.0	654.5	705.6	790.5	903.4	1,019.6
Recurrent expenditure	315.1	339.2	403.8	422.1	471.7	472.0	508.2	566.7	641.0	724.4
Interest payments	41.2	42.5	49.7	47.9	56.7	57.0	61.7	72.0	87.4	98.9
Domestic interest	31.4	36.9	44.0	42.2	49.4	49.4	54.3	62.4	76.3	85.5
Foreign interest due	9.8	5.7	5.7	5.7	7.2	7.6	7.4	9.6	11.1	13.4
Wages and benefits (civil service)	112.3	127.3	144.0	146.4	162.0	162.0	174.7	195.8	219.1	245.3
Civil service reform	1.3	1.4	0.5	0.8	0.2	0.2	0.2	0.2	0.2	0.2
Pensions, etc.	19.8	20.4	24.4	24.3	27.1	27.1	31.6	36.7	42.2	48.6
Other	111.8	119.0	139.6	157.1	171.4	171.4	187.7	209.1	232.8	265.2
Defense and NSIS 2/	29.3	28.7	45.7	45.8	50.8	50.8	52.3	52.9	59.2	66.3
Pending bills	-0.5	-0.1	0.0	-0.2	3.6	3.6	0.0	0.0	0.0	0.0
Development and net lending	67.7	80.3	147.8	140.0	198.3	179.4	194.3	220.6	259.0	291.7
Domestically financed	40.5	53.5	81.1	87.8	113.3	113.3	118.1	132.3	148.1	165.8
Foreign financed	23.1	26.1	60.3	45.8	81.2	62.4	74.2	86.2	108.9	123.8
Net lending	1.0	1.4	2.4	2.4	2.1	2.1	2.0	2.0	2.0	2.0
Pending bills	-1.0	-0.7	0.0	0.0	1.6	1.6	0.0	0.0	0.0	0.0
Drought Development Expenditure	4.0	0.0	4.0	4.0	0.0	0.0	0.0	0.0	0.0	0.0
Civil Contingency Fund	0.0	0.0	2.0	0.0	2.0	2.0	2.0	2.0	2.0	2.0
Drought expenditures	0.0	0.0	3.7	0.0	1.0	1.0	1.1	1.2	1.4	1.6
Balance (commitment basis, excluding grants)	-71.6	-46.5	-130.1	-119.8	-160.2	-140.8	-136.4	-152.9	-187.6	-218.1
Grants	20.1	15.5	30.7	24.2	33.8	30.4	35.1	39.5	48.3	58.3
Food/debt relief grants 3/	0.0	0.0	0.4	0.4	0.0	0.5	0.5	0.5	0.5	0.5
Project grants	15.7	15.5	26.5	20.3	33.8	30.0	34.6	39.1	47.9	57.8
Program grants	4.4	0.0	3.7	3.4	0.0	0.0	0.0	0.0	0.0	0.0
Balance (commitment basis, including grants)	-51.5	-31.0	-99.4	-95.7	-126.4	-110.4	-101.3	-113.4	-139.3	-159.8
Adjustments to cash basis	14.2	1.6	0.4	0.4	-0.4	0.0	0.0	0.0	0.0	0.0
Balance (cash basis, including grants)	-37.2	-29.4	-99.0	-95.3	-126.9	-110.4	-101.3	-113.4	-139.3	-159.8
Financing	35.0	35.5	99.0	99.2	126.9	110.4	101.3	113.4	139.3	159.8
Net foreign financing	-0.2	-3.1	29.0	9.9	58.8	43.4	34.1	40.7	53.8	58.2
Project loans	7.4	10.6	33.4	25.1	47.4	32.0	39.1	46.7	60.6	65.6
Program loans	1.6	0.0	1.3	1.3	0.0	0.0	0.0	0.0	0.0	0.0
Commercial (incl. security refinancing) 4/	0.0	0.0	20.2	0.0	33.6	35.1	13.9	13.9	13.9	14.6
Repayments due	-27.5	-16.7	-17.1	-15.7	-16.6	-17.3	-18.9	-19.8	-20.7	-22.0
Change in arrears	12.7	0.7	-8.8	-0.7	-6.1	-6.4	0.0	0.0	0.0	0.0
Rescheduling	5.6	2.2	0.0	0.0	0.5	0.0	0.0	0.0	0.0	0.0
Privatization proceeds and other 5/	7.0	4.0	44.9	76.4	13.7	13.7	0.0	0.0	0.0	0.0
Bank restructuring costs 6/	0.0	-20.0	-1.1	-1.1	0.0	0.0	0.0	0.0	0.0	0.0
Expenditure arrears securitization costs	0.0	0.0	-0.1	-0.1	-0.1	-0.1	0.0	0.0	0.0	0.0
Telkom restructuring costs (cash) 7/	...	...	-8.8	-8.8	0.0	0.0	0.0	0.0	0.0	0.0
Telkom restructuring costs (bond) 8/	...	...	-11.5	-9.0	0.0	0.0	0.0	0.0	0.0	0.0
Telkom restructuring costs (tax arrears) 9/	...	...	-15.0	-19.0	0.0	0.0	0.0	0.0	0.0	0.0
Bank restructuring financing 6/	...	20.0	1.1	1.1	0.0	0.0	0.0	0.0	0.0	0.0
Expenditure arrears securitization financing	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Telkom restructuring financing 8/	...	...	11.5	9.0	0.0	0.0	0.0	0.0	0.0	0.0
Telkom restructuring financing (tax arrears) 9/	...	...	15.0	19.0	0.0	0.0	0.0	0.0	0.0	0.0
Net domestic financing	28.3	34.7	34.0	21.8	54.5	53.3	67.2	72.7	85.5	101.7
Financing gap (stat. discrepancy for outturns)	2.2	-6.2	0.0	-3.9	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:										
Nominal GDP	1,519.4	1,717.5	2,077.8	1,983.3	2,393.2	2,373.8	2,637.9	2,955.5	3,308.6	3,703.1
Primary budget balance	4.0	13.2	-49.3	-47.4	-70.2	-53.4	-39.6	-41.4	-51.9	-61.0
Stock of domestic debt, net (end of period)	280.1	334.7	381.3	366.5	421.0	419.8	487.0	559.6	645.1	746.8
NPV of total public debt	576.0	611.9	...	643.7	...	756.4	864.9	972.6	1,097.5	1,257.7
Total public debt	686.0	725.8	...	768.9	...	901.0	1,018.6	1,140.3	1,281.1	1,465.4

Sources: Kenyan authorities; and IMF staff estimates and projections.

<sup>1/</sup> Fiscal year ending June 30. Projections from 2009/10 onward are based on the unchanged policy scenario (see text).<sup>2/</sup> Includes a one-time allocation for payment of security-related arrears of Ksh 2 billion in 2007/08 budget.<sup>3/</sup> Includes debt relief from a debt swap deal with Italy.<sup>4/</sup> In 2008/09, this includes a US\$ 500 million sovereign bond, of which some proceeds will be used to clear security related arrears.<sup>5/</sup> In 2008/09, this includes repayment from parastatals of expenditures that are pre-financed during 2008/09 by the central government budget.<sup>6/</sup> Operation consists of recapitalization of National Bank of Kenya and financing this through issuance of a special purpose bond.<sup>7/</sup> Operation consists of recapitalization of Kenya Telkom on account of its pension obligations and restructuring operation and financing this through cash injection.<sup>8/</sup> Operation consists of recapitalization of Kenya Telkom on account of its pension obligations and restructuring operation and financing this through issuance of a special purpose bond.<sup>9/</sup> Operation consists of clearance of tax arrears of Kenya Telkom to KRA and Ministry of Finance.

Table 2b. Kenya: Central Government Financial Operations (percent of GDP), 2005/06-2012/13 <sup>1/</sup>

	2005/06	2006/07	2007/08		2008/09		2009/10	2010/11	2011/12	2012/13
	Actual	Actual	EBS/07/124	Staff Projection	Budget	Staff Projection	Projection			
(In percent of GDP, unless otherwise indicated)										
<b>Revenue</b>	20.5	21.7	20.6	22.3	21.4	21.6	21.6	21.6	21.6	21.6
Income tax	7.5	7.7	7.3	8.3	8.1	8.0	8.0	8.0	8.0	8.0
Import duty (net)	1.3	1.6	1.6	1.7	1.5	1.6	1.6	1.6	1.6	1.6
Excise duty	3.3	3.3	3.2	3.1	3.0	3.1	3.1	3.1	3.1	3.1
Value-added tax	5.0	5.6	5.4	5.6	5.6	5.7	5.7	5.7	5.7	5.7
Investment income	0.1	0.4	0.1	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Other	1.7	1.7	1.5	1.5	1.4	1.5	1.5	1.5	1.5	1.5
Ministerial and Departmental Fees (AIA)	1.5	1.5	1.5	1.9	1.5	1.5	1.5	1.5	1.5	1.5
<b>Expenditure and net lending</b>	25.2	24.4	26.8	28.3	28.1	27.6	26.7	26.7	27.3	27.5
Recurrent expenditure	20.7	19.8	19.4	21.3	19.7	19.9	19.3	19.2	19.4	19.6
Interest payments	2.7	2.5	2.4	2.4	2.4	2.4	2.3	2.4	2.6	2.7
Domestic interest	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.1	2.3	2.3
Foreign interest due	0.6	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.3	0.4
Wages and benefits (civil service)	7.4	7.4	6.9	7.4	6.8	6.8	6.6	6.6	6.6	6.6
Civil service reform	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Pensions, etc.	1.3	1.2	1.2	1.2	1.1	1.1	1.2	1.2	1.3	1.3
Other	7.4	6.9	6.7	7.9	7.2	7.2	7.1	7.1	7.0	7.2
Defense and NSIS 2/	1.9	1.7	2.2	2.3	2.1	2.1	2.0	1.8	1.8	1.8
Pending bills	0.0	0.0	0.0	0.0	0.2	0.2	0.0	0.0	0.0	0.0
Development and net lending	4.5	4.7	7.1	7.1	8.3	7.6	7.4	7.5	7.8	7.9
Domestically financed	2.7	3.1	3.9	4.4	4.7	4.8	4.5	4.5	4.5	4.5
Foreign financed	1.5	1.5	2.9	2.3	3.4	2.6	2.8	2.9	3.3	3.3
Net lending	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Pending bills	-0.1	0.0	0.0	0.0	0.1	0.1	0.0	0.0	0.0	0.0
Drought Development Expenditure	0.3	0.0	0.2	0.2	0.0	0.0	0.0	0.0	0.0	0.0
Civil Contingency Fund	0.0	0.0	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1
Drought expenditures	0.0	0.0	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Balance (commitment basis, excluding grants)</b>	-4.7	-2.7	-6.3	-6.0	-6.7	-5.9	-5.2	-5.2	-5.7	-5.9
<b>Grants</b>	1.3	0.9	1.5	1.2	1.4	1.3	1.3	1.3	1.5	1.6
Food/debt relief grants 3/	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Project grants	1.0	0.9	1.3	1.0	1.4	1.3	1.3	1.3	1.4	1.6
Program grants	0.3	0.0	0.2	0.2	0.0	0.0	0.0	0.0	0.0	0.0
<b>Balance (commitment basis, including grants)</b>	-3.4	-1.8	-4.8	-4.8	-5.3	-4.6	-3.8	-3.8	-4.2	-4.3
<b>Adjustments to cash basis</b>	0.9	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<b>Balance (cash basis, including grants)</b>	-2.5	-1.7	-4.8	-4.8	-5.3	-4.6	-3.8	-3.8	-4.2	-4.3
<b>Financing</b>	2.3	2.1	4.8	5.0	5.3	4.6	3.8	3.8	4.2	4.3
Net foreign financing	0.0	-0.2	1.4	0.5	2.5	1.8	1.3	1.4	1.6	1.6
Project loans	0.5	0.6	1.6	1.3	2.0	1.3	1.5	1.6	1.8	1.8
Program loans	0.1	0.0	0.1	0.1	0.0	0.0	0	0.0	0.0	0.0
Commercial (incl. security refinancing) 4/	0.0	0.0	1.0	0.0	1.4	1.5	0.5	0.5	0.4	0.4
Repayments due	-1.8	-1.0	-0.8	-0.8	-0.7	-0.7	-0.7	-0.7	-0.6	-0.6
Change in arrears	0.8	0.0	-0.4	0.0	-0.3	-0.3	0.0	0.0	0.0	0.0
Rescheduling	0.4	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Privatization proceeds and other 5/	0.5	0.2	2.2	3.9	0.6	0.6	0.0	0.0	0.0	0.0
Bank restructuring costs 6/	0.0	-1.2	-0.1	-0.1	0.0	0.0	0.0	0.0	0.0	0.0
Expenditure arrears securitization costs	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Telkom restructuring costs (cash) 7/	...	...	-0.4	-0.4	0.0	0.0	0.0	0.0	0.0	0.0
Telkom restructuring costs (bond) 8/	...	...	-0.6	-0.5	0.0	0.0	0.0	0.0	0.0	0.0
Telkom restructuring costs (tax arrears) 9/	...	...	-0.7	-1.0	0.0	0.0	0.0	0.0	0.0	0.0
Bank restructuring financing 6/	...	1.2	0.1	0.1	0.0	0.0	0.0	0.0	0.0	0.0
Expenditure arrears securitization financing	...	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Telkom restructuring financing 8/	...	...	0.6	0.5	0.0	0.0	0.0	0.0	0.0	0.0
Telkom restructuring financing (tax arrears) 9/	...	...	0.7	1.0	0.0	0.0	0.0	0.0	0.0	0.0
Net domestic borrowing	1.9	2.0	1.6	1.1	2.3	2.2	2.5	2.5	2.6	2.7
<b>Financing gap (stat. discrepancy for outturns)</b>	0.1	-0.4	0.0	-0.2	0.0	0.0	0.0	0.0	0.0	0.0
<i>Memorandum items:</i>										
Nominal GDP (billion of Ksh)	1,519.4	1,717.5	2,077.8	1,983.3	2,393.2	2,373.8	2,637.9	2,955.5	3,308.6	3,703.1
Primary budget balance	0.3	0.8	-2.4	-2.4	-2.9	-2.2	-1.5	-1.4	-1.6	-1.6
Stock of domestic debt, net (end of period)	18.4	19.5	18.4	18.5	17.6	17.7	18.5	18.9	19.5	20.2
NPV of total public debt	37.9	35.6	...	32.5	...	31.9	32.8	32.9	33.2	34.0
Total public debt	45.1	42.3	...	38.8	...	38.0	38.6	38.6	38.7	39.6

Sources: Kenyan authorities; and IMF staff estimates and projections.

<sup>1/</sup> Fiscal year ending June 30. Projections from 2009/10 onward are based on the unchanged policy scenario (see text).<sup>2/</sup> Includes a one-time allocation for payment of security-related arrears of Ksh 2 billion in 2007/08 budget.<sup>3/</sup> Includes debt relief from a debt swap deal with Italy.<sup>4/</sup> In 2008/09, this includes a US\$ 500 million sovereign bond, of which some proceeds will be used to clear security related arrears.<sup>5/</sup> In 2008/09, this includes repayment from parastatals of expenditures that are pre-financed during 2008/09 by the central government budget.<sup>6/</sup> Operation consists of recapitalization of National Bank of Kenya and financing this through issuance of a special purpose bond.<sup>7/</sup> Operation consists of recapitalization of Kenya Telkom on account of its pension obligations and restructuring operation and financing this through cash injection.<sup>8/</sup> Operation consists of recapitalization of Kenya Telkom on account of its pension obligations and restructuring operation and financing this through issuance of a special purpose bond.<sup>9/</sup> Operation consists of clearance of tax arrears of Kenya Telkom to KRA and Ministry of Finance.

Table 3. Kenya: Monetary Survey, 2005-2009

	Jun-05	Jun-06	Jun-07	Jun-08	Sep-08	Dec-08	Mar-09	Jun-09
	Projection							
	(In Billions of Kenya Shillings)							
<b>Central Bank of Kenya (CBK)</b>								
Net foreign assets 1/	95.7	159.5	174.2	213.9	211.6	213.9	216.2	228.9
In Millions of US \$	1,212	2,159	2,357	2,896	3,067	3,078	3,089	3,192
Net domestic assets	-1.2	-51.8	-47.7	-62.7	-58.7	-31.8	-47.6	-55.0
Net domestic credit	1.7	-37.0	-16.8	-21.5	-17.3	11.9	-3.7	-9.8
Government (net)	5.1	-15.8	-3.5	-28.4	-5.6	21.3	7.5	9.5
Private sector credit (CBK staff loans)	2.0	2.2	2.3	2.4	2.4	2.5	2.5	2.5
Commercial banks (net )	-5.3	-23.4	-15.7	4.5	-14.2	-11.9	-13.8	-21.8
Other items (net)	-2.9	-14.8	-30.9	-41.2	-41.3	-43.7	-43.8	-45.2
Reserve money (RM)	94.4	107.7	126.5	151.2	153.0	182.1	168.6	173.9
Currency outside banks	59.3	67.2	78.1	84.0	95.3	115.2	99.9	98.1
Bank reserves	35.1	40.5	48.3	67.2	57.7	66.9	68.7	75.8
Required Reserves 2/	25.9	30.0	35.2	42.2	46.6	49.1	52.4	54.6
Excess Reserves	1.2	1.5	1.5	8.8	3.1	9.8	9.0	9.3
Cash in till	8.0	9.0	11.7	16.2	8.0	8.0	7.3	11.9
<b>Banks</b>								
Net foreign assets 1/	52.8	32.1	65.6	102.1	96.0	93.3	87.6	80.6
Reserves	35.1	40.5	48.3	67.2	57.7	66.9	68.7	75.8
Credit to CBK	5.3	23.4	15.7	-4.5	14.2	11.9	13.8	21.8
Net domestic assets	374.2	442.3	512.0	610.4	609.5	645.8	703.4	731.5
Domestic credit	459.2	535.3	608.3	738.7	696.8	743.8	810.5	852.4
Government (net)	107.2	133.7	160.6	161.1	163.8	164.4	165.1	162.4
Other public sector	10.3	12.2	12.5	10.1	13.0	14.8	16.0	10.4
Private sector	341.7	389.5	435.2	567.6	520.0	564.6	629.4	679.6
Other items (net)	-85.0	-93.0	-96.3	-128.4	-87.3	-98.0	-107.1	-120.9
Total deposits	467.5	538.3	641.7	775.2	777.4	817.9	873.5	909.6
<b>Monetary survey</b>								
Net foreign assets 1/	148.4	191.6	239.8	316.0	307.6	307.2	303.8	309.5
Net domestic assets	378.3	413.9	480.0	543.1	565.0	625.9	669.6	698.3
Domestic credit	466.3	521.7	607.1	712.8	693.6	767.6	820.6	864.4
Government (net)	112.3	117.9	157.2	132.7	158.2	185.7	172.6	171.9
Rest of the economy	354.0	403.8	450.0	580.1	535.4	581.9	647.9	692.5
Other public sector	10.3	12.2	12.5	10.1	13.0	14.8	16.0	10.4
Private	343.7	391.6	437.5	570.0	522.4	567.1	631.9	682.2
Other items (net)	-88.0	-107.8	-127.1	-169.6	-128.6	-141.7	-150.9	-166.2
Money and quasi money (M3)	442.4	522.0	605.5	716.4	745.4	803.4	841.1	872.8
M3 and foreign currency deposits (M3X)	526.8	605.5	719.8	859.2	872.7	933.1	973.5	1,007.8
Currency outside banks	59.3	67.2	78.1	84.0	95.3	115.2	99.9	98.1
Deposits	467.5	538.3	641.7	775.2	777.4	817.9	873.5	909.6
of which: foreign currency deposits	84.4	83.5	114.3	142.8	127.2	129.8	132.4	135.0
Memorandum items:								
	(In Percent of Annual Change)							
Money and quasi money (M3)	8.6	18.0	16.0	18.3	18.1	20.5	20.7	21.8
M3 and foreign currency deposits (M3X)	11.3	14.9	18.9	19.4	17.3	17.0	17.1	17.3
Reserve Money	4.7	14.0	17.5	19.6	16.5	17.0	12.0	15.0
Currency outside banks	6.6	13.3	16.2	7.5	19.0	20.0	17.6	16.9
Net domestic assets of the banking sector	7.0	9.4	16.0	13.2	12.2	18.8	21.0	28.6
Domestic credit	7.8	11.9	16.4	17.4	13.6	14.2	15.9	21.3
Government (net)	-19.3	5.0	33.3	-15.6	-1.4	32.2	5.6	29.6
Rest of the economy	20.6	14.1	11.4	28.9	19.0	9.5	19.1	19.4
Non-bank holdings of government debt, billions of Ksh	137	159.9	175.1	196.4	184.2	170.0	196.4	210.4
Stock of domestic debt, billions of Ksh	249	277.8	332.3	329.1	342.4	355.7	369.0	382.3
Multiplier (M3/RM)	5.7	5.6	5.7	5.7	5.7	5.1	5.8	5.8
Velocity (GDP/M3)	2.6	2.5	2.5	2.4	2.4	2.4	2.4	2.4

Sources: Central Bank of Kenya; and IMF staff projections.

1/ From September 2008, use of program exchange rate stopped.

2/ Calculated as 6% of total deposit excluding those at NBK, up to 2008.