REPUBLIC OF KENYA **GOVERNMENT of MAKUENI COUNTY**

COUNTY TREASURY

2021 County Debt Management Strategy Paper

FY 2021/2022 – 2023/24 MEDIUM TERM EXPENDITURE FRAMEWORK

FOREWORD

The Medium Term Debt Strategy Paper is prepared annually on a three year rolling basis and guides the County Governments' public debt management and borrowing to ensure sustainability for each fiscal year and the over the Medium term.

Public Debt Management is the process of establishing and executing a strategy for managing the Government's debt. This is done in order to raise the required amount of funding to meet any arising budget deficit necessary to realize the objectives set by government.

The Debt Strategy Paper seeks to act as a guideline for debt management practices of the County Government including the issuance process, management of the debt portfolio, and adherence to various laws and Regulations governing debt contracting and management. It guides in pursuing the desired structure of the public debt portfolio which reflects its choice on cost and risk tradeoffs.

The Makueni County development blue print 'Vision 2025' aims at achieving accelerated and inclusive economic growth and development; improved access to quality water and health services, access to quality education, increased job creation increased household incomes and sustainable food security. Over the years, the Government has implemented programs within the available fiscal space. In the medium term, as the Government seeks to realize the agenda for socio economic transformation, it will be seeking to enhance its resource mobilization strategies and expand the available fiscal space through enhancing own source revenue and engaging development partners, initiating PPPs and seeking loans.

The County Government of Makueni has no plans of incurring debt in the financial year 2021/2022. The County's Budget will be balanced with the resource envelope available hence, there will be no anticipated need for deficit financing. However, the Government will continuously manage its cash flow through short term lending from commercial banks to offset delays in equitable share disbursements and own source revenue mobilization.

MARY K. KIMANZI
COUNTY EXECUTIVE COMMITTEE MEMBER - FINANCE AND SOCIO ECONOMIC PLANNING

ACKNOWLEDGEMENT

The Medium Term Debt Management Strategy (MTDS) 2021 is prepared by the County Government under the requirement of the PFM Act 2012. It sets out the debt management strategy for the Government of Makueni County in the fiscal year 2021/22 and over the Medium Term.

The Makueni Debt Management strategy will play a major role in guiding on the optimal process of procuring debts/loans and management of the same in a way that optimizes benefits and minimizes costs and risks.

The paper is informed by a fiscal policy supportive of the macro-economic stability and growth. The Strategy highlight strategies to be explored in seeking funding for the enormous financial needs from either internal or external sources to deliver the programmes in the Vision 2025. As at now, the County Government's public debt is nil.

I would like to acknowledge the overall guidance provided by ECM Finance Mrs. Mary K. Kimanzi throughout the preparation period of this debt management strategy. The Budget, Revenue and Planning team spent a significant amount of time to put together the report. In this regard, I'm grateful for their technical input and commitment to the success of the process. Thank you all for the excellent support and work.

ELIUD NGELA
CHIEF OFFICER - BUDGET, PLANNING AND REVENUE
MAKUENI COUNTY

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EXECUTIVE SUMMARY

The Medium Term Debt Management Strategy (MTDS) is published every year and guides County Government borrowing in the medium term while providing a path for sustainable level of debt over the same period. The Debt management policy act as a guide for public debt and borrowing practices of the County Government, including the issuance process and management of the debt portfolio. It also emphasizes the need to adhere to the laws and regulations governing public debt management.

The Paper is prepared pursuant to PFM Act Section 123 and incorporates the principles of public finance as expounded in the constitution of Kenya 2010. The document lays out plans for Makueni County debt management for the fiscal year 2021/22 and over the Medium Term.

The MTDS provides guidance on raising resources through borrowing to finance the development objectives of the Government and managing the public debt portfolio. This will ensure any sought debt is affordable and sustainable and any new borrowing is for a good purpose and that the costs and risks of borrowing are minimized. It evaluates both costs, risks of various debt management strategies, and recommends an optimal debt management strategy for implementation in the future.

The Medium Term Debt Strategy is based on the medium-term macroeconomic framework as provided in the 2021 County Fiscal Strategy Paper which is focusing on investing in productive sectors. This will be geared toward achieving the theme for increased household income for sustainable livelihoods. The priority interventions will be on; Increasing investments in county productive sector; and Strengthening the capacity of the community to drive development at local level.

The paper details a statement setting out the debt management strategy of the county government over the medium term with regard to its intention to seek loans to advance the agenda for socio economic transformation.

The constitution and the PFM Act gives County Government powers to borrow money through issuing county treasury bonds and by loan or credit evidenced by instruments in writing. This must be guaranteed by the National government. In Guaranteeing the loans, the National Government shall ensure the loans financing needs and payment obligations are met at the lowest possible cost in the market which is consistent with a prudent degree of risk while ensuring that the overall level of public debt is sustainable.

Section 140 of the PFM Act, authorizes the County Executive Committee member for finance to raise a loan on behalf of the County Government only if the terms and conditions for the loan are set out in writing and are in accordance with;

i. Article 212 of the constitution
ii. Sections 58 and 142 of the PFM Act
iii. Regulations to the PFM Act 2012
iv. Fiscal responsibility principles and the financial objectives of the County Government set out in the most recent County Fiscal Strategy Paper
v. The debt management strategy of the County Government over he medium term.

The 2021 Makueni County Debt Strategy Paper is prepared taking account the following;

a. The borrowing needs of the county government
b. Fiscal responsibility principles as set out in section 107 of the PFM Act and regulation 25 of the PFM Act
c. Prevailing macro-economic conditions
d. Prevailing conditions of the financial markets.

1.0 LEGAL FRAMEWORK FOR PREPARING A MTDS

The PFM Act section 123 mandates the county to develop a medium-term debt management strategy paper; Sec 123 states **- (1) "**On or before the 28th February in each year, the County Treasury shall submit to county assembly a statement setting out the debt management strategy of the county government over the medium term with respect to its actual liability and potential liability in respect of loans and guarantees and its plans for dealing with those liabilities.

(2) The County Treasury shall include the following information in the statement-

- The total stock of debt as at the date of the statement
- The sources of loans made to the county government
- The principal risks associated with those loans
- The assumptions underlying the debt management strategy; and
- An analysis of the sustainability of the amount of debt, both actual and potential

(3) As soon as practicable after the statement has been submitted to the County Assembly under this section, the County Executive Committee Member for Finance shall publish and publicize the statement and submit a copy to the Commission on Revenue Allocation and the Intergovernmental Budget and Economic Council.

2.0 INTRODUCTION

Makueni County Integrated Development Plan (CIDP 2018-2012) aims at achieving increased household income for sustainable livelihoods. This will be realized through; Increasing agricultural productivity, value addition and commercialization; Increasing availability and access to water; Enhancing quality health care for all; Youth, women and PWD economic empowerment and ensuring Secure land tenure and urbanization.

To implement this agenda, the County requires an estimated Kshs 82,588,976,106.63 for the period 2018-2022. Based on actual revenues realized from FY 2017/18 – 2019/20 and the revised projected revenues for FY 2020/21 and FY 2021/22, the projected revenue gap has increased by 21 percent from Kshs 30,319,854,883.95 to Kshs 44,843,718,748.33. Consequently, for the County to realize its envisaged socio economic transformation in the CIDP, the resource mobilization strategy needs to be restructured and enhanced.

The County Government has developed a strategy that seeks to seek funding both internally (on source revenues) and externally. The external strategy shifts the attention towards engaging external partners to finance implementation of the prioritized programs. This will involve deepening engagement with bilateral and multilateral agencies, public private partnerships, private foundations, seeking loans and diaspora engagement (fundraising).

Table 1; CIDP 2018-2022 Funding and Projected Revenues

Item	Targeted	Actuals
Total required funding - CIDP - 2018-2022	82,588,976,106.63	82,588,976,106.63
Revenues - (Fy 2017/18 - FY 2021/22)	45542043245	37,745,257,358.30
Deficit	**(37,046,932,861.23)**	**(44,843,718,748.33)**

Funding through PPPs and loans will be restricted to high impact projects focusing on the productive sectors of the economy. This will be expected to stimulate the growth of the county economy and enhance our Gross County Product. This in effect will result to increased business activities and more revenues. The increased revenues will enhance the credit rating for the County that will facilitate high access to loans.

3.0 PUBLIC DEBT MANAGEMENT AND ITS OBJECTIVES

Public Debt; is defined by Constitution Article.214.(2) as all financial obligations relating to loans raised or guaranteed and securities issued or guaranteed by the national government.

Public Debt Management -is the process of establishing and executing a strategy for **managing** the government's **debt** in order to; raise the required amount of funding, achieve its risk and cost objectives, and to meet any other objectives set by government.
Deficit is the financing gap created when projected expenditure exceeds available revenues. To finance this gap government's resort to borrowing and debt is created.

The 2021/2022 – 2023/24 Debt Management Strategy will guide County Government debt management operations in the Medium Term. The Strategy seeks to balance cost and risk of county debt while taking into account the county government financing needs. In addition, the strategy incorporates initiatives to seek new funding sources, manage the cash flow and support the County Government priorities for socio economic transformation while ensuring debt sustainability. The strategy is on a three year rolling basis with an aim to ensure that debt levels stay affordable and sustainable.

The main objectives of the strategy include;

i. Ensuring that the government financing needs and its payment obligations are met at the lowest possible cost over the medium to long run, consistent with a prudent degree of risk;
ii. Ensuring public debt remains sustainable and that it does not place unbearable burden on its current and future generation. In this regard, management of public debt will seek to safeguard County Government's ability to service debt without compromising the fiscal capability to fund provision of services and development projects;

Responsibilities of County Treasury in Matters of Debt

Pursuant to PFM ACT Section 107 (2) The County Treasury is mandated to manage its public finances in accordance with the principles of fiscal responsibility. In managing the county government's public finances, the County Treasury shall ensure; over the medium term, the government's long term borrowings shall be used only for the purpose of financing development expenditure and the county debt shall be maintained at a sustainable level as approved by the county assembly.

Section 140 (1) of the PFM Act, authorizes the County Executive Committee member for Finance, to raise loans to implement Government programs, only if the loan and the terms and conditions for the loan are set out in writing and are in accordance with—

a) Article 212 of the Constitution; - A county government may borrow only— (i) if the national government guarantees the loan; and (ii) with the approval of the county government's assembly

b) Section 58 of the PFM Act; Mandates the cabinet Secretary (National Treasury) to guarantee loans for county governments or any other borrower on behalf of the national government with approval by Parliament.

c) Section 142 of PFM Act; the County Assembly may authorize short term borrowing by county government entities for cash management purposes only. However such borrowing shall not exceed five per cent of the most recent audited revenues of the county. The borrowing should be repaid within a year from the date on which it was borrowed.

d) The fiscal responsibility principles and the financial objectives of the county government set out in its most recent County Fiscal Strategy Paper; and

e) The debt management strategy of the county government over the medium term.

Pursuant to PFM regulations 177(2) a county government may from time to time borrow within and outside Kenya such sums of money in such amount and on such terms and conditions as to interest, repayment, disbursement or otherwise as the County Executive Committee Member may think fit, in any of the following ways—

(a) By issuing County Treasury bonds;
(b) By bank overdraft facility from the Central Bank of Kenya; and
(c) By any other loan or credit evidenced by instruments in writing.

Borrowing through Issuance County Treasury bonds and any other loan or credit evidenced by instruments in writing shall require a national government guarantee pursuant to section 58 of the PFM Act.
Borrowing through overdraft facility from CBK will be guided by PFM Act Section 142. This is restricted to short term borrowing at a maximum of 5 percent of the most recent audited equitable share and has to be approved by the County Assembly.

Principles of Public Finance

The Constitution of Kenya (Article 201) stipulates the following principles to guide all aspects of public finance management. The principles will apply to public borrowing and debt management.

a. There will be openness and accountability in borrowing and management of public debt;
b. Public debt management will promote an equitable society;
c. The burdens and benefits of the use of resources and public borrowing will be shared equitably between present and future generations;
d. Public money will be used in a prudent and responsible way; and
e. Borrowing and management of public debt will be responsible and fiscal reporting will be clear.

Audit of Public Debt and Borrowing

The office of the Auditor General will audit all public debt management activities annually in accordance with the Public Audit Act and the Public Finance Management Act, with the aim of promoting value for money and accountability of public funds.

Control of Loan Proceeds and Payments

The Controller of Budget will authorize withdrawal of funds for debt management operations – receipts and payments – and prepare reports on public debt and borrowing in accordance with the law.

Settlement of Debt Service Obligations

The County Government undertakes to timely honor all public debt obligations entered into directly with the aim to minimize fiscal cost and risks that may arise out of undue defaults. The County Government commits to ensuring that all laws governing public debt management are honored.

Proceeds of Borrowing

All loan proceeds will be credited into the County Exchequer Account or any other account as provided by law.

Disclosures

Public debt and borrowing processes will be conducted in a transparent and open manner. In enhancing fiscal transparency, the County Treasury will: -

a. Publish and publicize debt reports and information as guided by the relevant laws;
b. Set-up and avail relevant information on the County Government website;
c. Be responsive to the public on debt management issues;
d. Engage as needed with the potential lenders, creditors/investors in Government securities and media; and
e. Undertake any other necessary measures to achieve this objective.

4.0 PRINCIPLS AND GUIDELINES FOR PUBLIC DEBT MANAGEMENT

In the Medium Term, the Government will raise resources through long term and short term borrowing to finance the programs in the budget. This will be done while ensuring the debt levels are maintained at sustainable levels. The management of public debt will be in accordance with the constitution and the PFM Act.

4.1 purpose for borrowing

The County Government borrowings will be for the following purposes;

i. Financing government budget deficits;
ii. For cash management;
iii. To finance development projects including on-lending to approved entities;
iv. To mitigate against adverse effects caused by urgent and unforeseen events. in cases where the emergency fund is depleted;
v. Meeting any other development policy objectives that the County Executive Committee Member for Finance shall deem necessary, consistent with the law and as Cabinet and County Assembly may approve

The County Executive Committee Member for Finance will ensure that the level of fiscal deficits set out in the County Fiscal Strategy paper is consistent with the principles of public finance as set out in the Constitution of Kenya and the objectives of Medium Term Debt Strategy Paper.

4.2 Managing Costs and Risks

The Debt Strategy paper will guide public borrowing taking into account the cost and risks associated with the various borrowing options. Borrowing decisions will be taken after a critical and comprehensive cost benefit analysis of the debt involved, its purpose, amount, repayment terms, currency of contract, and any other risks associated with the loan.

Short-term borrowings will be for management of temporary cash flow fluctuations during the financial year and will be limited for a period of twelve months. Development/capital expenditures will be financed through long-term borrowing to maximize the benefits of long repayment periods of these type of loans.

The County Government will maximize borrowing loans whose benefits have a potential for self-liquidating i.e. where the use of loan funds will generate proceeds that directly or indirectly repay the loan. This implies that the social and economic returns on borrowed funds exceed the cost of such capital. In this regard, a cost benefit analysis will be undertaken for all projects before a loan is accepted.

In order to ensure sustainability of loan repayment, the following guidelines will be applied:

i. Commercial borrowing will not be used to finance social projects;
ii. The social internal rate of return of loan funded projects should be high enough to justify the cost of the loan; and effort should be made to objectively quantify this measure);
iii. The gestation period of the candidate project – i.e. the time it takes for the project to start producing its outputs, outcome, or impact – should be shorter than or equal to the grace period of the loan; and
iv. Short-term loans should be limited to commercial or revenue generating projects as well as for financing projects of strategic value.

4.3 Borrowing Limits

Pursuant to PFM regulation 25; the county public debt shall never exceed twenty (20%) per cent of the county governments total revenue at any one time. At any time, the annual debt service cost of a county government shall not exceed fifteen (15%) per cent of the most recent audited revenue of that county government, as approved by county assembly (PFM Act regulation 179 (2).

Based on the Credit rating report Makueni County qualifies for any loan below Kshs 2 billion, however based on the audited revenues for FY 2019/20, Makueni County can qualify for a loan to a maximum of Kshs 1,792,425,973.87. as outlined in table 2 below.

Table 2; Projected county possible loan amounts and expenditure limits

Revenue source	FY 2019/20 Actual Revenues	FY 2020/21 - Revenues	FY 2021/22 Projected Revenues	FY 2022/23 Projected Revenues	FY 2023/24 Projected Revenues
Own source revenue	465,939,455.75	1,093,000,000.00	575,000,000.00	835,000,000.00	885,000,000.00
Shareable revenue	7,406,100,000.00	7,464,930,000.00	8,047,189,800.00	8,132,000,000.78	8,132,000,000.78
Conditional allocations, loans and grants	1,090,090,413.60	1,179,498,668.00	665,918,285.00	800,000,000.00	900,000,000.00
Total	**8,962,129,869.35**	**9,737,428,668.00**	**9,288,108,085.00**	**9,767,000,000.78**	**9,917,000,000.78**
Maximum loan (20%)	**1,792,425,973.87**	**1,947,485,733.60**	**1,857,621,617.00**	**1,953,400,000.16**	**1,983,400,000.16**
Maximum annual repayment amounts (15% of revenues) (without Interest)					
			1,293,328,470.00	**1,345,050,000.12**	**1,352,550,000.12**
Years	**Repayment options**	**Annual repayments – based on annual maximum loan amounts**			
2	896,212,986.94	973,742,866.80	928,810,808.50	976,700,000.08	991,700,000.08
5	358,485,194.77	389,497,146.72	371,524,323.40	390,680,000.03	396,680,000.03
10	179,242,597.39	194,748,573.36	185,762,161.70	195,340,000.02	198,340,000.02
15	119,495,064.92	129,832,382.24	123,841,441.13	130,226,666.68	132,226,666.68

Source; county treasury

The annual repayments for the loan are sustainable over the medium term based on the projected inflows from equitable share and own source revenues.

4.4 Process of seeking loans;

For a project to be financed, it should support the achievement and meet the objectives of Government socio economic transformation agenda and must be included the Medium Term Debt Strategy. In order to be able to process any loan, Departments and entities should;

i. Present a feasibility study report informing the project economic viability, costing and design and social and environmental risks mitigation plans,
ii. Confirm on availability of land and wayleave acquisition for the project where necessary.

iii. Confirm on availability of adequate human resources capacity for project implementation. Where there is a shortfall, the Departments, must commit to develop a strategy to fill the gap;

iv. Demonstrate prioritization and commitment of the counterpart funding by the respective department where necessary. This should not be less than 15 percent of the total project cost. Funding, including but not limited to land and wayleave compensations among others that from part of counterpart funding must be prioritized under the department's allocation through the normal Medium Term Expenditure Framework(MTEF) budgeting process in accordance with the requirements of the loan agreement.

v. Present a due diligence report to ascertain the financial, technical and legal competency for the frim procured competitively to undertake the project implementation.

vi. Present any other requirements depending on either Bilateral or Multilateral Framework Agreement with the respective Development Partner;

All project proposals should be forwarded to County Treasury. The County Debt Management Unit will review all documents and independently assess the cost/benefits analysis submitted and evaluate the sources of financing. The implementing units shall work with County Treasury to ensure Conditions Precedent (CPs) are met first or done in parallel before signing of the financing agreements.

Analysis of Debt Sustainability

In deciding whether or not to contract new debt in the medium term, emphasis will be placed on monitoring the level of total public debt, and to assess the potential cost and risk of new debt measured against the available fiscal space and the vitality of the economy to ensure that future borrowing will maintain outstanding debt within sustainable levels. The ratios to be monitored include solvency and liquidity indicators. These ratios include:

a. Debt to GCP;
b. Debt service to GCP;
c. Debt Service to County Revenues
d. Interest payments to County Revenues
e. Interest payments to GCP;

Debt Management Strategies

In the event, the county seeks debt to finance its operations; the following shall be adhered to;

Debt shall be Sustained at Affordable Levels; To realize this, the county will ensure it pursues grant funding and budget support and where grants are unavailable, or where a loan element of grant funding for priority development projects is mandatory, limited concessional borrowing will be sought.

Concessional loans; Borrowing will be limited to concessional loans from multi- or bilateral donors or development partners

Loan purpose; Any new borrowing shall follow fiscal responsibility guidelines for a fit purpose; from an allowable source and with acceptable terms and conditions.

Any borrowing sought by the County will be for;

a. Managing county cash flow.
b. Investing in the productive sectors of Makueni County;
c. Funding priority core infrastructure and development initiatives as identified in CIDP 2018-2022 and Vision 2025; and
d. Specific purpose projects identified as a high priority in the county Vision 2025; Preference shall be given to projects that have the chance to stimulate growth and development of all other sectors and no borrowing will be done to fund shortfalls in recurrent expenditure.

4.5 Institutional and Operational Framework

Debt management in the county will be handled by the County Debt Management Unit which will provide secretariat services to the County Debt Management Advisory Committee (DMAC). The functions and responsibilities of the unit shall include:

i. carrying out the government's debt management policy of minimizing cost taking account of risk;
ii. maintaining debt data base for all loans taken by the county government
iii. preparing and updating the annual medium term debt strategy and debt sustainability analysis;
iv. preparing and implementing the county government borrowing plan including servicing of outstanding debts;
v. monitoring and evaluating all borrowing and debt related transactions to ensure that they are within the guidelines and risk parameters of the debt management strategy;
vi. Preparing, updating and executing the annual medium-term debt management strategy including debt sustainability analysis in accordance with Regulations;
vii. Participating in negotiation meetings with government creditors, and provide technical support to the ECM Finance on public debt operations;
viii. Assessing the risks in issuing any guarantees including contingent liabilities inherent in public private partnership projects, and prepare reports on the method used for assessment and the results thereof for the attention of the ECM Finance;
ix. Facilitating the recovery of any payments including interest and other costs incurred by Government due to the honoring of outstanding guarantees;
x. Preparing annual debt management report which shall include outstanding guarantees, outstanding lending and government on-lending by Government;
xi. Monitoring and keeping track of debt levels;
xii. Advise on all debt servicing obligations of Government;
xiii. Preparing and publishing debt statistical bulletins regularly;
xiv. Preparing forecasts on Government debt servicing and disbursements as part of the yearly budget preparation;
xv. Compiling, verifying and reporting on all Government debt arrears and design a strategy for the settlement of those arrears;
xvi. Monitoring that the disbursements of loans raised by Government are in accordance with agreed disbursement schedules;
xvii. Formulating External Resources Policy;
xviii. Assessing, mobilizing, negotiating and allocating all external resources including the consolidation of the donor commitment register in the annual national budget;

xix. Examining and scrutinizing proposals for financing projects of a county government entity from an accounting officer;
xx. Formulating an external resource mobilization strategy to guide the county in external resource mobilization including monitoring;
xxi. Formulating guidelines and procedures for reporting and recording budget estimates and expenditure for external resource;

The County Debt Management Advisory Committee will be responsible for recommending and ranking acceptable proposals to be submitted by the County Executive Committee Member for Finance to the County Executive Committee for considerations and approval. The approved proposals will then be submitted and incorporated as part of the budget approval and appropriation process after signing by the CEC member for finance. Borrowing will not be legal unless it has been signed off by CEC member for finance.

County Debt Management Advisory Committee

The County Debt Management Advisory Committee (DMAC) will be chaired by the Chief Officer in charge of planning, Budget and Revenue with membership of technical officers from County Treasury and Chief Officers from the three pillars of the Vision 2025 i.e. (Economic Pillar (Department of Transport and Infrastructure, Department of Trade, Industry, Tourism and Cooperatives), Social Pillar (Department of water and sanitation ,Health services) and political pillar (Department of Devolution and Public service). The Debt Management Advisory Committee will evaluate borrowing proposals and make recommendations to the CECM for finance as to whether borrowing should or should not proceed.

The County Debt Management Advisory Committee is mandated to assess the volume and risk characteristics of debt to ensure that:

i. Debt is sustainable and affordable;
ii. Debt is below the thresholds established;
iii. Debt is from an acceptable source;
iv. Debt is for a good purpose and the funded project is a high priority in the CIDP 2018-2022 and Vision 2025;
v. The project to be funded has a positive Net Present Value or helps achieve Vision 2025 and the SDGs;
vi. The cost of any contingent liabilities and obligations such as tied procurement are factored into the cost and risk of debt;
vii. Loan terms and conditions are acceptable and achieve the best cost and risk outcome
viii. Borrowing aligns with the CFSP.

County Debt Management Unit

There shall be a County Debt Management Unit (CDMU) under the County Treasury of Makueni county government. The Debt Management Unit will provide secretariat services to the County Debt Management Advisory Committee (DMAC).

The functions and responsibilities of the County Debt Management Unit will include:

i. Making debt payments on time and for the correct amount,
ii. Keeping timely, comprehensive and accurate records of outstanding government debt, guarantees, contingent liabilities and new borrowing in a single debt database;
iii. Publishing, in a timely manner, monthly (and quarterly) reports showing the status of outstanding debt, debt payments, and projected debt payment obligations;
iv. Preparing, reviewing and updating the Debt Strategy;
v. Preparing an annual borrowing plan
vi. Assessing the risks in issuing any guarantees, and prepare reports on the method used for each assessment and the results thereof for the attention of the CEC Member for Finance;
vii. Submitting all debt reports and debt management strategy to DMAC for consideration and recommendation.

4.6 Process for Approving Loan Proposals by the County Government

Pursuant to Section 184 of PFM Regulations the County Executive Committee Member shall undertake the following;

i. Submit the borrowing proposal which will include its terms and conditions to the County Executive Committee for approval of the borrowing; After approval by the County Executive Committee, the County Executive Committee Member for Finance shall submit the signed loan agreement and a sessional paper to the County Assembly for deliberation and approval.
ii. After obtaining the approval of the County Assembly, the County Executive Committed Member for Finance shall submit the final draft loan financing agreement and the 'approval of the County Assembly to the Cabinet Secretary – National Treasury requesting for the guarantee of the final loan financing agreement;
iii. The Cabinet secretary (National Government) shall participate in the negotiations on the contracting of a guaranteed loan by advising the County Government on the best financial terms available and shall sign on behalf of the National Government all agreements on the issuance of a government guarantee.

In guaranteeing the loans, the County must demonstrate the following;

a. That the project could not be financed on reasonable terms and conditions without a government loan
b. The County has adopted a unified approach in project cycle management that includes the preparation, appraisal and management of public investment projects
c. Conditions precedent for the implementation of the project have been met including
    a. Land acquisition, compensation and resettlement of persons affected and stakeholder management

b. Detail designs have been completed and relevant approvals obtained where applicable;
c. Necessary regulatory approvals vane been granted
d. Detailed resource requirement including sources of funding and personnel to operationalize the project have been planned for
e. Project details have been captured in the pipeline of Public Management Information System

d. Provide the projected cash flow clearly setting out the projected disbursement schedule and repayment plan
e. Contribute a substantial portion of project funds from the own county resources not less than 15 percent
f. Demonstrate that the proposed feasible project(s) have been approved by the County Government as required by county legislation

iv. While the cabinet secretary is guaranteeing the loans, He/she shall take into account the recommendation of the Intergovernmental Budget and Economic Council IBEC in respect of any guarantee. This is in line with section 58(2) of the PFMA, 2012.
v. The Cabinet Secretary after receiving recommendations of the IBEC shall then seek the recommendations of the Attorney General
vi. The Cabinet secretary to the National Treasury upon taking into account the recommendations of IBEC, the cabinet and the Attorney General may recommend for approval or rejection of the request
vii. Upon rejection of a loan request, the cabinet secretary shall give reasons and communicate the same to the county executive committee member for finance.
viii. Upon approval of a loan guarantee request, the Cabinet Secretary shall submit a sessional paper to Parliament with recommendations seeking its approval;
ix. The Cabinet Secretary shall communicate the decision of Parliament on the draft loan guarantee to the respective County Executive Committee Member for finance; and
x. upon approval by Parliament the Cabinet Secretary shall issue a loan guarantee.
xi. After receiving the communication of the decision of Parliament on the draft loan guarantee, the County Executive Committee member shall report to the County Assembly of the decision

Procedure for submission of County Treasury Bonds guarantee request.

While seeking funding through treasury bonds, the CEC Finance shall follow the following process;

i. The County Executive Committee Member for finance shall develop and submit the cash plan, indicating the borrowing requirements to the County Executive Committee for approval of the borrowing including its terms and conditions;

ii. After approval by the County Executive Committee, the County Executive Committee Member shall submit the cash plan referred to above to the County Assembly for approval of the borrowing including its terms and conditions;

iii. upon approval by the County Assembly, the County Executive Committee Member shall submit the final cash plan and the approval of the County Assembly to the Cabinet Secretary requesting for the guarantee of the Treasury Bond and their inclusion in the issuance calendar;
iv. the Cabinet Secretary to the National Treasury, after receiving the request from the county government, shall seek the recommendations of the Intergovernmental Budget and Economic Council in fulfillment of the requirements of section 58(2)(i) of the Act;
v. the Cabinet Secretary to the National Treasury may, upon taking into account the recommendations of the Intergovernmental Budget and Economic Council and the Attorney General may approve or reject the request;
vi. the Cabinet Secretary shall reject a request for loan guarantee with reasons and communicate the same to the concerned County Executive Member ;
vii. upon approval of a loan guarantee request, the Cabinet Secretary to the National Treasury shall submit the request to Parliament with recommendations seeking its approval;
viii. the Cabinet Secretary to the National Treasury shall communicate the decision of Parliament on the draft loan guarantee to the respective County Executive Committee Member for finance;
ix. upon approval by Parliament, the Cabinet Secretary shall include such authorized Treasury Bonds in the overall national issuance calendar.
x. once the issuance calendar is known, when the national governments advertises its bond issuance for a specific month it shall also incorporate those to be issued on behalf of county governments;
xi. on the issuance day, the county whose bond is being issued, shall be represented in the auction committee meeting by the County Executive Committee Member or his or her representative; and
xii. after the National Treasury and the county government sign an on-lending agreement, the National Treasury shall transfer the proceeds of the Treasury Bond to the Revenue Fund of that county government and such on-lending transactions shall attract a fee to be determined by the National Treasury

5.0 FY 2021/22 – FY 2022/23 DEBT OUTLOOK

5.1 National Debt Outlook

Kenya’s public debt has gradually risen to Ksh 7.2 Trillion as of end of December 2020, split broadly equally between external and domestic debt, and the structure continues to evolve with economic transformation of the country. Public debt is primarily driven by fiscal deficit as the country resorts to borrowing to fill the budgetary resource gap to finance development needs of the two levels of government.

The costs and risks characteristics of the public debt portfolio have significantly changed over time due in part to increase in stock and its components, and due to decline in grants from development partners. Consequently, debt service obligations have risen and fiscal consolidation to stem expenditure pressures need to be sustained to avoid undesirable outcomes.

Kenya’s debt position remains sustainable, but the risk of debt distress has increased to high level due to the COVID-19 crisis weakening exports and real GDP growth and delaying fiscal consolidation. Kenya’s total public debt has more than doubled to KSh 7.2 Trillion at the end of December 2020 compared to KSh 3.1 Trillion in January 2016. During this period, the amount of external debt rose from KSh 1.654 Trillion to KSh 3.7 Trillion. Kenya’s domestic debt also rose from KSh 1.5 Trillion in January 2016 to KSh 3.5 Trillion as at December 2020. External debt was 52 % of total public debt while 48% was domestic debt as at close of December 2020.

With lower domestic revenue mobilization and elevated budget expenditures before the unwinding of COVID-19 related fiscal stimulus measures, the budget deficit is expected to remain broad and add to Kenya stock of public debt. If Kenya’s fiscal imbalance is not reduced in the coming years, there will be further accumulation of domestic and external public debt, intensifying Kenya’s external debt vulnerabilities, crowding out private sector investment. While Kenya is committed to medium-term fiscal consolidation, this may face challenges, including the 2022 general elections.

5.2 County Debt Outlook

Makueni County Government has no debt. The Government has been operating on a cash basis, expenditure balancing expenditures with the available fiscal space. Despite this, there has been periodic delays in disbursements of equitable share from the National Government negatively affecting service delivery. To address this, in the FY 2021/22, the County will be seeking short term loans from the commercial banks to address projected deficits in cash flows. The County Executive will be submitting quarterly reports to the County Assembly for approvals of these loans. In the FY 2020/21, the County will also evaluate programs and proposals in the CIDP and Vision 2025, appraise and develop proposals for funding through loans.

In the year 2020, Makueni County undertook a rating intended to assess the county capacity to meet its financial commitments. This was aimed at assisting the County Government access financing through capital market for public infrastructure development and service delivery. The credit rating initiative was conducted by Global Credit Rating (GCR) on behalf of the National Treasury, World Bank and Commission on Revenue Allocation (CRA).

The county received an impressive BBB rating for long term loans and a much stronger A3 rating for short term loans, meaning the County is stable enough to repay loans both locally and externally. The ratings reflect the County Government's stable financial profile underpinned by the consistent transfers from National Government, as well as other ongoing operational and institutional support from National Government and the initiatives being implemented to enhance own source revenues.

Over the medium term, Makueni County is considering raising debt to finance development activity to finance the Makueni Vision 2025. The borrowing will be limited to the maximum of 20% of the prior year's audited revenue in line with the PFM Act.

Based on the County's projected revenue and assuming the County raises debt up to this limit, GCR expects that any debt will be below Kshs 2Billion and credit protection metrics will remain comfortable. However, based on the audited revenues for FY 2019/20, Makueni County can qualify for a loan to a maximum of Kshs 1,792,425,973.87.

The potential sources of Loans for Makueni County Government falls under two categories;

a) **Domestic sources of loans;** This will consist of borrowing from financial institutions (banks, pension funds, insurance companies) and non-financial institutions (domestic instruments E.g. T-bills, T-bonds).
b) **External sources of loans;** The main sources will include Loans and grants from multilateral, bilateral organizations. This will be facilitated through the National Treasury

In the FY 2021/22 the Government will be seeking short term loans to manage the County cash flow. This has been occasioned by the inconsistent transfers of equitable share to the County Government affecting service delivery and payment of key obligations. The County Executive will be submitting quarterly requests for approval.

In seeking this loans, the County Government will be guided by PFM Act Section 142 which authorizes borrowing for cash management purposes. The borrowing shall not exceed five percent of the most recent audited revenues of the entity and will be repaid within a year from the date on which it was borrowed.

6.0 MACROECONOMIC ASSUMPTIONS OF THE MEDIUM TERM DEBT MANAGEMENT STRATEGY

This section describes the medium term strategy assumptions considered during preparation and those that are to affect the realization of the proposed management strategies. The assumption is:

i. As the County and National Economy rebounds from the negative effect of COVID 19 pandemic, it's expected that in the medium term, the macroeconomic framework underpinning the strategy will remain stable during the medium term period. Forecasted GCP, GDP growth rates and variables such as inflation rates, interest rates amongst others are expected to remain stable in the medium term.
ii. The macro-economic framework underpinning the 2021/2022-2023/2024 MTDS is consistent with projections included in the 2021 County Fiscal Policy Strategy Paper.
iii. The political, social and economic environment is expected to remain favorable during the implementation of the strategy;
iv. As per the constitution, the national government is expected to guarantee county government loans; and
v. The National Treasury is expected to sustain the efforts towards minimizing the delays in disbursement of equitable share transfers and other factors which might lead to escalation of demand for short-term finance by the counties.

7.0 CONCLUSION

Public debt management forms an integral part of macroeconomic environment in any economy. It has implications on public expenditure and also has a direct bearing on macroeconomic stability.

Public debt management objectives are; to ensure that the county government's financing needs and payment obligations are met at the lowest possible cost over the medium to long term, with a prudent degree of risk, while ensuring the equitable sharing of benefits and burdens of public debt between the current and future generation.

As the county enhances its resource mobilization in the medium term, the county will ensure when funding to programmes is done through debts it will be sustainable and the County will meet its debt obligations in a timely manner. Government borrowing will be guided by the need to lower cost and minimize risks, particularly of foreign exchange, interest rate, refinancing and settlement risks.

The Government will endeavor to implement sound policies and structural reforms to strengthen its credit rating to enhance its access to a wider array of sources of financing at lower cost and risk while maintaining overall debt within sustainable levels.

The increase in debt stock strains public service delivery, as resources available for financing other social and development needs are limited. The need to adequately coordinate borrowing activity and establish guidelines to monitor debt levels is crucial in debt management.

The strategies proposed in the MTDS will ensure low cost funding with high returns, thereby promoting socio-economic well-being of the citizens. This is expected to contribute to economic growth both at the county and national level and ensure delivery of Vision 2025 for enhanced socio economic transformation.

8.0 GLOSSARY OF TERMS

Budget	Financial plan that serves as an estimate of future cost, revenues or both.
Capital Expenditure("capex")	Expenditure on long-term assets such as plant, equipment or land, which will form the productive assets of a company.
Cash	Funds that can be readily spent or used to meet current obligations.
Cash Flow	The inflow and outflow of cash and cash equivalents. Such flows arise from operating, investing and financing activities.
Concessionality;	A measure of the softness of a credit reflecting the benefit to the borrower compared to a loan at market rate. Technically, it is calculated as the difference between the nominal value and the present value of the debt service as of the date of disbursement, calculated at a discount rate applicable to the currency of the transaction and expressed as a percentage of the nominal value.
Credit Rating	An opinion regarding the creditworthiness of an entity, a security or financial instrument, or an issuer of securities or financial instruments, using an established and defined ranking system of rating categories.
Debt Service;	The amount of funds used for repayment of principal and interest of a debt.
Debt Sustainability Analysis;	This is conducted in the context of medium-term scenarios. These scenarios are numerical evaluations that take account of expectations of the behaviour of economic variables and other factors to determine the conditions under which debt and other indicators would stabilize at reasonable levels, the major risks to the economy, and the need and scope for policy adjustment. In this analysis, macroeconomic uncertainties, such as the outlook for the current account, and policy uncertainties, such as for fiscal policy, tend to dominate the medium term outlook.
Debt Sustainability;	Sustainable debt is the level of debt that allows a debtor country to meet its current and future debt service obligations in full, without recourse to further debt relief or rescheduling, avoiding accumulation of arrears, while allowing an acceptable level of economic growth.
Disbursement;	The actual transfer of financial resources or of goods or services by the lender to the borrower.
Diversification	Spreading risk by constructing a portfolio that contains different exposures whose returns are relatively uncorrelated. The term also refers to companies which move into markets or products that bear little relation to ones they already operate in.
Domestic Borrowing;	Government borrowing through issuance of local Government securities and direct borrowing from the Central Bank.
Domestic Debt;	Part of the overall debt owed by the Government to creditors domiciled in the economy. The debt includes money owed to commercial banks, non-bank financial institutions, individuals among others. The term domestic

	debt is used in relation to government obligation.
External Borrowing;	Government borrowing from both official (Government or Government agencies) and private institutions domiciled outside the country.
External Debt;	Part of the overall debt owed by the Government to creditors domiciled outside the economy. The debt includes money owed to private commercial banks, other governments, or international financial institutions such as the IMF and World Bank. The term external debt is used in relation to government obligation.
Government Securities;	Financial instruments used by the Government to raise funds from the primary market.
Interest	Scheduled payments made to a creditor in return for the use of borrowed money. The size of the payments will be determined by the interest rate, the amount borrowed or principal and the duration of the loan.
Issuer	The party indebted or the person making repayments for its borrowings.
Leverage	With regard to corporate analysis, leverage (or gearing) refers to the extent to which a company is funded by debt.
Liquidity	The speed at which assets can be converted to cash. It can also refer to the ability of a company to service its debt obligations due to the presence of liquid assets such as cash and its equivalents. Market liquidity refers to the ease with which a security can be bought or sold quickly and in large volumes without substantially affecting the market price.
Loan	A sum of money borrowed by a debtor that is expected to be paid back with interest to the creditor. A debt instrument where immovable property is the collateral for the loan. A mortgage gives the lender a right to take possession of the property if the borrower fails to repay the loan. Registration is a prerequisite for the existence of any mortgage loan. A mortgage can be registered over either a corporeal or incorporeal property, even if it does not belong to the mortgagee. Also called a Mortgage bond.
Own Source Revenue	Own source revenue are those income streams that are directly under the control of the public entity, and may include property rates, business and other licence fees, hospitality fees, fines, or any other charges through which an LRG can generate income.
Present Value;	The present value (PV) is defined as the sum of all future cash flows (interest and principal) discounted at the appropriate market rate. For a loan, whenever the interest rate on a loan is lower than the market rate, the resulting PV is lower than its face value.
Primary Market;	This is a market where financial instruments are originated through initial issuance.
Principal	The total amount borrowed or lent, e.g. the face value of a bond, excluding interest.
Public Debt;	This refers to outstanding financial obligations of the Government arising from past borrowing. It includes Government guaranteed debts to State

	Corporations and Local Authorities.
Secondary Market;	this is a market where already issued financial instruments are traded.
Sovereign/Euro Bond;	A debt security issued by a national government within a given country and denominated in a foreign currency. The foreign currency used will most likely be a hard currency.
Transfers	Income received from a third party, most often a higher level of government or a donor. Includes exchequer releases, income provided by Government Departments, and or external parties such as development finance agencies.
Treasury Bills;	It is a short-term borrowing instrument issued by the Government to finance the budget.
Treasury Bond;	This is a medium to long-term term debt instrument issued by the Government to finance the budget.