INSTITUTE OF ECONOMIC AFFAIRS

THE BUDGET FOCUS

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FIRST QUARTER ANALYSIS OF THE 1999/2000 BUDGET

Inside this issue:

In this second issue of the Budget Focus, we undertake an analysis of the first quarter of the 1999/2000 financial year, focussing on first quarter allocation and exspenditure trends in seven ministries—all considered critical to poverty eradication. The report attempts to determine whether allocations made correspond with expenditure incurred. The ministries examined are Office of the President (OP), Agriculture and Rural Development, Education, Health, Energy, Environment and Natural Resources, Roads and Public Works.

FROM BUDGETING TO DISBURSEMENT: THE PROCESSES

The collection of data on national accounts, updating of the inter-industry input-output coefficients, conducting economic surveys, preparation of Sessional Papers ((SPs), preparation of the 5-year National Development Plan (NDP) all constitute important stages in the allocation of resources. This process continues with the preparation of the 3-year Public Investment Programme (PIP), the 3-year Forward Budget and, finally, the Annual Budget or Printed Estimates. Whereas the preparation of the SPs and NDPs lays the policy basis for long term public finance allocation the PIP translates some of these policy intentions into costed programmes over the next three years. The Printed Estimates annualises these projections which are presented as the annual budget.

Perhaps the Report of the CAG should be in two parts; the first part constituting the financial audit (budget) and the second comprising policy and performance audit (programme and project).

By enacting the Finance and appropriation Bills into law, Parliament grants to government the legal authority for taxation and expenditure respectively. Whereas it is the Appropriations Act that signals government expenditures, Sec. 101 of the Constitution allows the National Assembly to authorise withdrawals from the Consolidated Fund (CF) before the Appropriation Act is passed for purposes of meeting expenditure necessary to carry on the services of the Government of Kenya during that year until such a time as the Appropriation Act comes into operation.

The Appropriation Act grants money from the CF to meet the costs of providing the services and development programmes specified in the Act. It gives statutory sanction for the issue by the Treasury out of the CF to meet expenses as outlined in the recurrent and development expenditure votes.

Before the Minister of Finance makes withdrawals from the CF and as specified in the Appropriation Act, he has to obtain authorisation from the President who issues a Presidential Warrant that permits that expenditure to be charged against the appropriation. Subsequently, the Treasury applies to the CAG for credit on the exchequer account to meet the charges likely to be incurred by the accounting officers. If satisfied that this applications conforms to the law, the CAG authorises Central Bank of Kenya to issue some from the exchequer's account. This is the control function of the CAG.

Once the Treasury obtains the Presidential Warrant, it issues the Treasury Warrants (Annual Estimates Warrant) which authorises accounting officers (Permanent Secretaries) to incur expenditures in respect of votes for which they are responsible. In making the issues, Treasury acts through the Paymaster General (Financial Secretary) on statutory office established under Cap. 413 of the Laws of Kenya. The Acts issued to ministries by the Paymaster General must be made not later than 15th July of each year and upon receipt of the AIEs, ministries are required to enter them as a commitment in their vote books.

Information on the allocation side of national accounts (the Gross National Product -GDP) is normally printed in such documents as Sessional Papers (SP1 of 1986 and 1994), National and District Development Plans, Public Investment Program (PIP), 3 year rolling Forward Budget, Annual Budget /Printed Estimates (PE) and various circulars.

On the expenditure side, the only documents that attempt to determine whether the allocated resources were spent as per the PE is the Controller and Auditor General's (CAG) Report to the Parliamentary Public Accounts Committee (PAC). The CAG is a constitutional office established under Section 105 of the constitution and tasked with the control and audit function of government funds. However, this office is undermined by various factors which include a two-year audit lapse, under-staffing, under--funding, reporting through the Executive which it is auditing, lack of prosecutorial powers, lack of security of tenure to junior officers.

The other key institution on the expenditure side is the Auditor-General Corporations which was created in 1985 through an amendment to the Exchequer and Audit Act. The AGC is tasked with the responsibility of auditing state corporations established under the State Corporations Act and submits its report to the Parliamentary Public Investment Committee (PIC). This office is also greatly handicapped by various factors. First it is unconstitutional since all the audit powers of government funds are vested in the CAG. Thus for the ACG to purport to audit any section of public funds is untenable in constitutional law. Second the AGC operates as a department of Treasury which it is supposed to audit. It derives its staff from the Public Service Commission and this places it at the mercy of the Executive. Further it is grossly under-funded which inhibits its capacity to move around to visit parastatals strewn all over the country.

The economist in treasury and other ministries and budget officers, do not produce a report or monitor sectoral expenditures as they are taking place in-order to determine whether those expenditures trends will enable the economy attain her objectives. In other words, there does not exist sufficient mechanism to continuously monitor the budget as these audit processes are largely post-mortem in character.

This therefore means that it is difficult to track short-term expenditures to determine whether they are related to key policy objectives, annual budgets and the likely impact on the GDP.

Once the Government budget for the financial year has gone through all the above mentioned stages including approval of the Finance Bill by parliament, the permanent secretaries or the accounting officers disburse funds to various expenditure points from their various Paymaster General (PMG) accounts. Again details of this information on disbursement is not readily available for public consumption. It is the Controller and Auditor General who will report to Parliament the accounting perspective of expenditure after about 1 to 2 years of the budget period. Thus, the corresponding impact of the budget by policy is largely undetermined.

WHAT DO THE TRENDS SHOW: LEVELS OF DISBURSEMENT OF FIRST QUARTER FUNDS BY MINISTRY

During the first quarter of 1999/2000 Financial Year (FY), disbursement of both recurrent and development exceeded the first quarter ceilings. Whereas the first quarter ceilings stood at about 15.7 billion, by end of the quarter expenditure was at the 18.6 billion mark representing an excess of 3 billion. However this burst of the ceilings is attributed to more by the recurrent rather than the development expenditures. Indeed the expenditure on development was actually 83 million less the first ceiling allocations while recurrent was 3 billion more than the quarter ceilings. Disbursement of development funds (the GOK component excluding donors) to development activities/ projects for the seven ministries was the lowest averaging to about 5% of the 1999/2000 PE allocations.

Disbursement of recurrent funds is 7 times higher than development for all the seven ministries. This implies that huge sums of public funds are either spent on payment of salaries and allowances or on maintenance of old equipment. This expenditure may not have a direct impact of eradicating poverty or industrialization since the corresponding expenditure on development activities is 7 times lower.

The figures show that all the ministries with the exception of Energy and Environment burst their recurrent expenditure ceilings by an average of 22%. The leading culprit is Health (41%), followed by Education (25%), Public Works (19%), Agriculture (15%) and OP (8%). Interestingly the ministries which exercise some discipline in managing recurrent expenditures, seem to be unable to maintain that standards with regard to development expenditures. Thus Energy which has the best record in recurrent has the worst with development as it has exceeded the quarter allocations by a whooping 155%. It is followed by the Ministry of Environment at 71%, and OP at 17%. Whereas Energy figures can be explained in terms of long term single capital investment, the OP and Environment are a bit mysterious. The Ministry of Health with the highest recurrent expenditure ceiling burst is the poorest in absorbing development funds – 32%. It is followed by Public Works (40%), Agriculture (52%), Education (67%).

Table 4 shows that Office of the President received 22% of annual recurrent allocations in the first 3 months of the financial year while only a low 6% for development activities. Assuming that that trend will continue into the second third and forth quarters, OOP shall have received 88% of recurrent expenditure and only 24% for investment activities. The table also shoes that the Ministry of Public Works has already exceeded total annual recurrent allocation in the printed estimates in the first quarter. Where is it going to get the monies to meet these expenses in the next three quarters. What the table shows is that we invest about 5% of allocations made foe development. At this rate it becomes difficult to eradicate poverty besides having ambitions to industrialise.

BUDGET ALLOCATION VERSES EXPENDITURE LEVELS BY MINISTRY

Documents that determine sectoral resource allocations mentioned above indicate that there are huge disparities between 1999/2000 PIP and the PE for 1999/2000 FY. Sources contacted at the treasury could not confirm whether the PIP resource allocation system was subjected to both resource evaluation and simulation using the Kenya Macro Economic Model. This model was last updated in 1994 a partially liberalized economy. It was also confirmed that regional o/district annual annexes and five-year development plans are rarely simulated with respect to national and district/ regional micro, meso and macro economic development potentials. The overall scenario depicts low level of investment hence a low rate of growth of GDP.

This is obviously attributed to also the disparities between levels of resource allocation in PIP and the net GOK allocations in 1999/2000 Printed Development Estimates. Notwithstanding the huge disparities in allocations, the quarterly expenditure levels are also very low despite being above the first quarter ceilings for all 7 ministries.

?? MINISTRY OF ROADS AND PUBLIC WORKS

According to the 1999/2000 Public Investment Program document, the Ministry of Roads and Public Works has the highest number of projects to implement during this FY. The PIP document estimates that about 12 billion Kenya shillings should be invested on roads while the 1999/2000 Printed Estimates has allocated 1.2 billion Kenya shillings. The first Quarter Ceiling is Kshs 151,960,390/=. The data obtained from Treasury indicate that less than half of the Quarterly Allocation has been spent despite the under-allocation of funds to this important sector of the economy. The projects which the money was released were only two. These projects are Nairobi Mombasa Road and Other GOK funded projects.

?? OFFICE OF THE PRESIDENT

Of the 5.8 billion required by the PIP fir investment in the OP the OP received about 4 billion – 1.8 billion less. Of this amount the first quarter ceiling stood at 191 million while the actual issues were 223 million an expenditure that exceeds allocation by about 4 million. Of these issues less than half were spent in the districts (about 91 million). The projects that this money went into include two El Nino infrastructure projects funded by the ADF and the IDA, Construction of Additional Facilities, Micro-Small Training and Technology. What the statistics show is that despite the expensive national spread of the OP about 55% of its first quarter issues were spent at the headquarters.

?? MINISTRY OF ENVIRONMENT AND NATURAL RESOURCES

The first quarter ceilings for this ministry represent about 10% of the allocation in the printed estimates. At 173 million the first quarter issues exceeded the first quarter ceilings by 73 million. From these issues only 1 million was transmitted to the districts which went into the funding of Kiradich dam, Masinga-Kitui Water Supply (Austria/GOK), Coast Water Supply (GOK), Arid and Semi-Arid Forestry (IFAD/GOK), National Environmental Secretariat(UNDP/GOK).

?? MINISTRY OF AGRICULTURE

To make leaps in the agricultural sector the PIP estimated that we need to invest a minimum of 2.3 billion. The Printed Estimates of this FY allocated 2.4 billion to its ministry representing an increase of about 1 billion. However the rate of absorption has been slow in the sector as of the 94 million first quarter ceiling the government managed to issue only 49 million.

For the Ministry of Education the first quarter issues were about 10 million less the ceilings and most of it went into the University Investment Programme and the Curriculum Support Services.

Out of 172 projects reflected in the PIP document, 32 are externally funded with small amounts of GOK contribution. At the time of compiling data for this report, it was not possible to determine expenditures on externally funded projects. However, reliable sources from the ministry of Finance confirmed that the flow of donor funds to projects has not improved as much due to liquidity and improper documentation for expenditures. Although donor funded projects are pre-financed, in most cases the government has to spend her money and thereafter claim reimbursement from the donor special accounts with Central Bank of Kenya. This arrangement has proved to worsen the liquidity situation for most ministries implementing donor funded projects.

FIRST QUARTER EXPENDITURE RETURNS BY MINISTRY AND DISTRICT

Information on expenditure returns by item or activity and project is captured in every ministry's monthly ledger. The monthly ledger is purely an accounting document lacking any information on the linkages between expenditure and policy objective. At the time of compiling this report, it was not possible to obtain a monthly ledger for any ministry since all ministries were working on last financial year final accounts.

This information obtainable from the ledgers could be useful in many ways including determining the likely impact or otherwise of expenditures on policies and hence GDP. In order to achieve any meaningful analysis in this direction, perhaps the way to start is to compile information on the following variables:

?? Tabulation of sectoral policies by region/ district, expenditure projections per policy objective
?? Tabulation of inter-industry input output tables or coefficients by national, region/ district and the corresponding investment activities including enabling environment policies

Otherwise, expenditure returns as they exist today do not provide room for quantitative evaluation against specific policy objectives. It is however not known whether the process of PIP preparation includes cross checking expenditures against policy objectives and projects and even conduct a random check of project performance on the ground.

ANNUAL DEVELOPMENT PROJECTS FOR FUNDING BY MINISTRY

Another area this report is focusing on is whether projects that have been funded under the seven ministries ere those initially earmarked for funding in the PIP and PE.

The government variously categorises the projects to be implemented largely on the basis of the source of funds and also on the basis of their coreness or newness in a financial year. According to the PIP the projects that need to be implemented by the various ministries are as follows: OP (76); Agriculture (68); Health (106); Education (109); Roads(172); energy (55); Environment(9). However, in OP there are a total of 9 projects that are not in the PIP but which are Public Investment Total Projects. These are ghost projects.

It is also evident that apart from the Ministry of Agriculture, the projects that are appearing in the Printed Estimates are far much fewer than the ones proposed by the PIP. Thus in the Ministry of Education for example, out of 109 projects only 23 are in the printed estimates. In Roads out of 172 a mere 17 are the ones that appear in the PE. The Ministry of Environment on the other hand has 16 more projects in the PE than was anticipated in the PIP.

What this table shows is that there is a disparity between PIP projects and PE projects. All the projects approved by the PIP document were not funded by 1999/2000 P. E. And in certain instances, such as Ministry of Environment, projects that were never in the PIP have been funded under the PE. What one wants to question is the rationality of these allocations to projects whose identification did not follow the normal procedures.

Whereas on average the PE made allocations for 28 projects for each of the seven ministries at a cost of about 700 million by the end of the firs quarter only 20 projects or all the ministries had received funding totaling about 600 million.

Again the linkage between the list of projects for which funds were released and the PE is not clear. It was not possible to determine whether these are the very projects that appear in the PIP and PE since they do not have codes in the list for funding by ministry. Moreover, the project codes in the PIP are not the same codes adopted by the PE.

THE PACE OF IMPLEMENTATION VERSES EXPENDITURES

On the whole, the pace of implementation of GOK funded projects considered seem to be very slow. Whether the situation may be worse for donor funded projects is not yet determined. The performance of projects is currently determined by the rate of disbursement and final expenditure. Table N0 4 shows that no ministry/project had spent more than 6% of the funds allocated to it in the 1999/2000 Printed estimates during the first 3 months of project implementation. It would be a miracle to spend the remaining 94% of the allocation in just 6 months. This so far is a very low rate compared to the projected 25% of the annual allocation. The question what and where is the problem?

Highlights of Issues Impinging on Allocation Verses Expenditures

With the exception of the Ministry of Agriculture and Rural Development, there is a huge disparity between allocations appearing in the Public Investment document and the voted Printed Estimate of 1999/2000 Financial Year (FY).

At the time of compiling the report, it was established that the PIP allocations, although done by technocrats in various ministries planning units, were neither done according to established technical procedures nor the involvement of the key representatives of the population at the district level.

Most officers and even accounting officers in technical ministries are not aware of the procedures behind budget ceilings and the infamous budget cuts.

Only a few officers in the Treasury and implementing ministries are aware of procedures and policy details in project documents and financing agreements for externally funded projects. The result has been poor documentation of finances spent on externally funded projects. As a result, the GOK has been unable to claim huge amounts of money from donors.

When setting the budget ceilings, the economists in the treasury review many factors that determine government financial position. The budgeting officers and the officers spending the money tend to ignore these financial constraints or are simply not aware. This scenario has led to low levels of finances earmarked for development.

The technical information utilized in budgeting include:

- ? ? The Kenya Macro Economic Model contains such variables like the level of balance of Payments, sectoral and total GDP, exports and import levels, annual estimated revenue, expenditure levels, deficit levels and its financing procedures, money, credit prices and employment levels of the economy. (the technical procedures include: micro and macro economic projections, meso models for sustainable poverty eradication strategies).
- ? ? Other technical information include: the quantity of money, the market exchange rates, tariff rates and the average rate of compensation of wages to increase in the cost of living in the preceding year.
- ? ? These models are normally utilized to simulate development plans with respect to identified constraints.
- ? ? The micro projections give rise to macro outputs. Key micro projections not utilized in these budgets include the viable length of tarmac and muram roads the economy. Investments in roads have been identified as having the highest multiplier effect in a liberalized economy especially in rural and urban areas.

Other useful variables for budgeting and financial management the report was unable to confirm whether officers in various ministries adhere to include deficit on commitments arising from their ministries' expenditures, grants and loans include:

- ? ? Determining expenditures and net lending coming about as a result of expenditures of their ministries. The information available is aggregated for all the sectors.
- ? ? The weight of their expenditures on GDP

The micro/macro economic model should basically determine the length of additional tarmac road for construction, the length of tarmac road for maintenance during the forthcoming financial year and other physical infrastructure that would facilitate private sector investment. This particular aspect of the budget is lacking in the current estimates of expenditure under the Ministry of roads and Public Works

- ?? The coefficients of the equations of the macro model derived from an input/output table developed in 1976 and modified in 1987, 1989 and 1994. It is composed of 37 interrelated sectors of the economy.

It was not possible to confirm whether in the previous expenditure plans (the budget) this model was utilized. What is clear, however, is that over the years, there has been little utilization of technical procedures of determining suitable projects to invest in. The frequent budget cuts and the little impact public finance management has had on poverty reduction goes to prove that the manner in which projects are identified and implemented is inappropriate. This inappropriateness can be attributed either to the use of wrong instruments or total disregard of the instruments themselves. In the Kenyan context it appears to be both..

Tables 1 and 2 show that there is a low rate of spending against annual allocation by all ministries. This is generally attributed to the fact that important budget activities that complement each other take place at the same time. The time when the Government is collecting the money is the very moment projects are supposed to be implemented. The GoK budget is for one year and closely tied to collection of revenue for all projects funded by donors and GOK. Donors are always demanding of Government to show commitment to implementing agreed projects within the agreed areas. The only method to ensure this commitment is by ensuring that the Government utilize her own money and seek reimbursement from either the special account with the CBK after obtaining clearance from the donor representative or arrange for a direct payment.

In a majority of cases, the GOK is unable to account for the monies and hence reimbursement has been delayed. Whenever money is released from the special account to the ministry account for on-ward transmission to district or projects, there is always a delay in the start of implementation since the procedure takes quite a while.

When ministries receive money for implementing such donor funded projects in the headquarter account, they in-turn send what is referred to as Authority -to-Incur- Expenditure (AIE) to the projects or districts. Meanwhile the actual money is left deposited in the headquarter-ministry's account that is perpetually a bottomless pit. In most cases, the project money is utilized to meet other financial obligations. Thus the project work is stalled and further draw down on the project account will be delayed since replenishing the account is based on past expenditures.

While donors work out a budget for a whole project implementation period, the GOK collection and hence budget is for one year.

OVERVIEW OF EXPENDITURE SYSTEMS

Public expenditure reviews have established that centralized public expenditure systems do not augur well with speedy implementation and management of projects for poverty eradication and fast economic growth. A number of weaknesses have been determined, these include:

?? The GOK expenditure system is a top-down model as opposed to bottom-up wish list of development projects from the districts.

?? The ministry technocrats draw money to implement ministry/sector projects from the pool or from the district treasuries that rely on weekly floats of Kshs 3 million from the office of the president.

?? The authority to utilize the money is with the district commissioner who has no legal basis for redress in case of mismanagement.

?? Those who control the money at various points of expenditure in the GOK are in most cases ignorant of various linkages and weights of various technical annual work plans.

?? The recurrent and development expenditure document does not contain the details of an annual work plan.

?? Donor expenditure systems are divided into investment and the cost of implementing the investment project.

?? Implementation and reimbursement are pegged to a detailed annual work plan and budget that are hardly internalized by the administration and accountants at various expenditure points.

Development Expenditure Areas in the PE – The Equivalent of PIP for
Office of the President

During 1999/2000 Financial Year it is assumed that if the Office of the President spends Kshs 4,032,131,000/= on the projects mentioned below, it would contribute some significant percentage (% unknown due to lack of simulation at micro, meso and macro economic levels) towards achieving economic recovery, economic growth, reduction of the incidence of poverty and industrialization.

1 Headquarters
2 Baringo District Development Institute
3 National Drought Recovery Programme
4 SDD –Poverty Eradication Unit
5 State Corporation Relief
6 Arid Land Resource Management Project
7 National Registration of Persons Bureau
8 Kenya Wild Life Services
9 El-Nino Emergency Project

10 Nyayo Tea Zones Development Corporation.
11 Provincial Administration
12 District Administration
13 Administration Police Training College
14 Field Administration Police Services
15 Office of the Government Printer
16 NYS Headquarters Administration Services
17 Training units
18 Production Units
19 Jomo Kenyatta International Airport
20 Moi Airport
21 Border Control Points
22 CID Headquarter Administrative Services
23 Office of the Commissioner of Police
24 Kenya Police College, Kiganjo
25 Divisional and Field Services
26 President Estates
27 Police Dog Unit
28 Training Collage, Embakasi
29 Headquarters Administrative Services
30 Field Services

In the PIP has a total of 85 projects have been proposed for funding under OOP. However, only 30 project appear in the current 1999/2000 PE document under OOP. This trend cuts across all ministries. The allocations appearing in the PIP are more than the project allocations in the PE. It was not possible to determine whether these projects are more of administrative nature or investments aiming at poverty eradication and industrialization.

Region, by including clear estimates for several years, it is easier to track down and monitor government spending and whether these spending are consistent with government policy objectives.

MTEF also allows for clear delineation of responsibility for central agencies and live managers; ensure judgement as to whether output targets have been met; quality and consumable information to MPs and other stakeholders; creation of forums foe consultation and debate (publication of forward estimates provide time and information for debating priorities and funding allocation); holding managers accountable for outputs, publications of about targets provides a benchmark for measuring government performance comprehensive framework for government activity. Thinking medium term targets tax policy debt management and expenditures to meet strategic objectives.

The MTEF stages include:

1. Developing a macro-economic framework and establishing the availability of revenue.
2. Conducting sectors revenue and agreeing on sector objectives, policies, outputs, programme and doing costing. These have been to be prioritised.
3. Hearings between the Ministry of Finance and the sectors on the basis of (1) and (2) above.
4. Ministry of Finance develops detailed expenditure framework and sector review output now available enabling the Ministry of Finance to develop a strategic expenditure framework.
5. Cabinet makes decision on selected resource allocations on the basis of affordability and inter-sectoral priorities. This is done by defining sector resource

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