12/3/19

Paper laid on 12/3/19 @ 2-30pm

for Clerk CASS
12/3/19

GOVERNMENT OF NAIROBI CITY COUNTY

THE NAIROBI CITY COUNTY ASSEMBLY

OFFICE OF THE CLERK

SECOND ASSEMBLY-THIRD SESSION

NBI CA. PLC. 2019 / (024) 12th February, 2019

PAPER LAID

Pursuant to Section 123 of the Public Finance Management Act, 2012, I beg to lay the following Paper on the Table of the Assembly, today Tuesday 12th March, 2019.

THE MEDIUM TERM DEBT MANAGEMENT STRATEGY FY 2019/2020.

(The Leader of Majority Party)

Copies to:
The Speaker
The Clerk
Hansard Editor
Hansard Reporters
The Press

NAIROBI CITY COUNTY

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City Hall
P .o. box 30075-00100
Nairobi
Kenya

FINANCE AND ECONOMIC PLANNING

NNC/FIN/DDM/023/2019 **28TH FEBRUARY 2019**

The Clerk

Nairobi City County Assembly

City Hall Building-2nd Floor

P.O.Box 458844-00100

NAIROBI

RE: MEDIUM TERM DEBT STRATEGY PAPER 2019

Forwarded herewith is the Medium Term Debt Strategy Paper 2019 for your noting and action.

ALLAN IGAMBI
CECM-FINANCE AND ECONOMIC PLANNING

NAIROBI CITY COUNTY ASSEMBLY
CLERK'S CHAMBER
1 MAR 2019
RECEIVED
Sign:
P.O. Box 30075-00100, NAIROBI

Rongo Snr/C.A
Table & refer to budget committee
CA
04/3/19

CA - Austin
Pls deal.
Snr clerk for
4/3/19

NAIROBI CITY COUNTY

Medium Term
Debt Management Strategy

2019/2020

Enquiries covering this Debt Strategy Paper may be addressed to;

Allan Igambi
County Executive Member-Finance & Economic Planning,
P.O. Box 30075,
Nairobi.

Telephone: +254 2022221349
Website: www.nairobi.go.ke

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FORWARD

The preparation of the County medium term debt management strategy (MTDMS), is guided by the Public Finance Management Act of 2012 and the PFM County Regulations of 2015.These provide the requisite framework to ensure the county continues with prudent debt management. The PFMA has laid strict procedures, accountability and reporting requirements for counties.

The Medium Term Debt Management Strategy (MTDS) is one of the important deliverables of the County Treasury as provided for under the PFMA. It provides the guidance to the county on the amount, type of borrowing to undertake over the medium term. It evaluates the costs and risks of various scenarios and recommends an optimal strategy for implementation. The 2019 /2020, MTDS is in line with the broad strategic priorities and policy goals set out in the County Fiscal Strategy Paper 2019, which shall be tabled in the County Assembly on or before 28th February 2019.

The MTDMS aims to ensure sustainability of the county debt, having undertaken an analysis of the existing level of debt, associated risks and strategies to address management of the debt. There is need for fiscal prudence in management of county's resources and emphasis of operational efficiency, to ensure that the county government financing needs and payment obligations are met at the lowest possible cost in the market that is consistent with a prudent degree of risk, while ensuring that the overall level of public debt is sustainable. This will further cushion the county from a situation of debt overhang.

Considering the current level of debt both inherited and pending bills arising from county government, the MTDMS 2019 will reinforce measures geared towards reduction of county debt. In addition, the county government will continue to build capacity of the newly established Debt Management Department in terms of staffing and training to ensure that it is in position to handle all matters relating to borrowing and servicing of debt.
The county treasury will continue to maintain effective linkages with the National Treasury for effective debt administration and provision of technical advice

Allan Igambi
CEC MEMBER FOR FINANCE

ACKNOWLEDGEMENT

The Medium Term Debt Management Strategy (MTDMS) paper has been prepared as per the requirement of Public Finance Management (PFM) Act, 2012.The MTDMS sets out the debt management strategy of the County Government over the medium term with respect to actual and potential liabilities.

As required by the PFMA the MTDMS will be formally tabled to the County Assembly on or before 28th February 2019, and will be published and publicized.

To ensure circulation of the MTDS, it is available in the County website. www.nairobi.go.ke.

I also take this opportunity to acknowledge the staff of the County Treasury who were involved in the preparation of the 2019/2020 MTDS. Specifically, I wish to thank the Debt Management Department for their commitment in compilation, editing and finalization of the Debt Management Strategy Paper on time.

WINFRED GATHAGU
AG.CHIEF OFFICER -FINANCE

List of Abbreviations

B.	Billion
CBA	Collective Bargaining Agreement
CBK	Central Bank of Kenya
CBR	Central Bank Rate
DMD	Debt Management Department
DMO	Debt Management Office
FY	Financial Year
GOK	Government of Kenya
MTDS	Medium Term Debt Strategy
MTEF	Medium Term Expenditure Framework
PFMA/PFM	Public Finance Management Act, 2012

EXECUTIVE SUMMARY

The accumulation of government expenditure arrears is one of the most common problems in public financial management (PFM). Government debts are financial obligations incurred by any level of the public sector for which remain unpaid when due. Payments may be overdue based on a particular legal obligation (such as payment of social security benefits, or salaries), a specific contractual commitment (such as payment for construction of a road), or a continuing service arrangement (such as payment for electricity supply).
Debt remains one of the major economic policy issues facing County Governments. Nairobi County Government (and its predecessor the defunct City Council of Nairobi) has been heavily in debt for decades.

The County Government debt portfolio comprises of both short and long-term debts. These include historical on-lent water loans taken to finance water infrastructure in the 1970's and a guaranty (government guaranteed loans) taken in the 1980's to finance construction of Umoja II housing project, owing's to various contractors and suppliers of goods and services, utility companies, statutory bodies, loans to commercial banks and unpaid personnel emoluments.

Further, the County's debt portfolio worsened over the years due to a growing wage bill and high-compounded interest/ penalties charged by the statutory creditors. This has made servicing of the debts quite a challenge and the result is an ever-growing debt portfolio.

CHAPTER ONE

MEDIUM TERM DEBT MANAGEMENT STRATEGY 2019/20

1. Introduction

The PFMA Act, 2012 section 107(2e) requires that Nairobi City County debt be maintained within a sustainable level, as approved by the County Assembly, section 107(3) requires that short term borrowing be restricted to management of cash flows and not exceed 5% of recent audited government revenue. In complying with this, the Nairobi City County will only issue debt when necessary to fund projects.

Long-term borrowing will only be used to finance development projects as approved in the County Integrated Development Plan (to a limit of 5% of the recently audited financial statements) and projects funded by debt will only be funded for their expected useful life. Operations and management expenditure will not be funded through debt. To maintain debt at sustainable levels, the Nairobi City County's borrowing per the debt management strategy will be capped at 15% of total revenues. The Nairobi City County has introduced initiatives to manage its current debt levels:

Debt rescheduling/renegotiation - the Nairobi City County will seek to reschedule current bank loans with a view to obtaining favourable terms for a longer period. This is aimed at releasing scarce resources to service delivery by easing pressure on cash flows;

- Large infrastructure projects will be financed through external borrowing as this is concessional and requires longer period of time than what commercial banks normally offer;
- The Nairobi City County may look into money and capital markets through the issuing of bonds;
- Negotiations will be undertaken with various creditors with a view to effect debt/asset swaps; and
- Negotiations will be entered with the National Government with an aim of writing off debts that were guaranteed by the Central Government to the defunct Local Authority.

This is aimed at cleaning the balance sheet and improving the Nairobi City County's credit worthiness.

1.1 Background

The Medium Term Debt Management Strategy Paper is published in accordance with Section 123 of the Public Finance Management Act, 2012. The law states that:

- **The County treasury shall submit to the county assembly on or before 28th February in each year ,a statement setting out the debt management strategy of the county government over the medium term with regard to its actual liability and potential liability in respect of loans and its plans for dealing with those loans.**

The information to be included in the MTDS includes:

a) **The total stock of debt as at the statement date**

b) **Sources of the loans made to the county government**

c) **Principal risks associated with those loans.**

d) **The assumptions underlying the debt management strategy**

e) **An analysis of the sustainability of the amount of debt, both actual and potential**

As soon as practicable after the debt management strategy has been submitted to the assembly the County Executive Member for Finance shall publish the statement and submit a copy to commission for revenue allocation and the Intergovernmental Budget and Economic Council.

The Debt Management Department falls under Finance and Economic planning Sector, which was established in 2018 and currently understaff; needing an establishment of 20 staff as per the proposed structure.

The principal objective of the County Government debt management is to meet the County Governments financing requirements at the least cost possible with a prudent degree of risk. The secondary objective is to service and retire the existing debt portfolio in order to release resources to service delivery.

The 2019, MTDS will guide the County Government operations in 2019/2020. The strategy seeks to balance cost and risk of public debt while taking into account the financing needs of the county and to develop initiatives for new funding sources.

The Nairobi County Government Medium-Term Debt Management Strategy (MTDS is developed within the context of the Fiscal Responsibility Framework and guided by the Public Debt Management Act 2012 section 107(2e). The MTDS for FY2019/20 examines the costs and risks to the debt portfolio relative to established targets. Further, it considers alternative financing strategies, geared toward meeting the following broad strategic debt management objectives of Nairobi County Government:

- Raising adequate funding to satisfy County Government is financing needs, at the lowest possible costs and at prudent levels of risk
- Minimizing exposure to and managing the main risks inherent in the public debt portfolio
- Maintaining and encouraging further development of an efficient debt Portfolio for county government securities; and
- Broadening the County Government's investor base and diversifying funding sources.

There are improvements in key risk indicators as reflected in lower exposure to Interest rate and refinancing risks. The accommodative monetary policy of the Central Bank of Kenya during this review period contributes to marginally lower annualized interest cost for the debt portfolio. The general reduction in exposure to market and refinancing risks coupled with marginally lower annualized interest costs highlights the key successes of the County Government over the review period.

Notwithstanding the improvements in the cost and risk profile of the public debt portfolio, foreign currency and refinancing risks remain significant concerns for the National Government. Accordingly, the MTDS for FY2019/20 - FY2022/23, which will include the Annual Borrowing Plan and Issuance Calendar, will continue to operationalize the strategy of borrowing mainly in the domestic market, at fixed-rates across the yield curve.

In addition to the fiscal responsibility principles set out in section 107 of the Act, the following fiscal responsibility principles shall apply in the management of public finances—

Fiscal responsibility principles.

(a) The County Executive Committee Member with the approval of the County Assembly shall set a limit on the county government's expenditure on wages and benefits for its public officers pursuant to section 107(2) of the Act;

(b) The limit set under paragraph (a) above, shall not exceed thirty five (35) percent of the county government's total revenue;

(c) For the avoidance of doubt, the revenue referred to in paragraph (b) shall not include revenues that accrue from extractive natural resources including gas, oil and coal;

(d) The county public debt shall never exceed twenty (20%) percent of the county governments total revenue at any one time;

(e) The county annual fiscal primary balance shall be consistent with the debt target in paragraph (d);

(f) The approved expenditures of a county assembly shall not exceed seven per cent of the total revenues of the county government or twice the personnel emoluments of that county assembly, whichever is lower;

(g) Pursuant to section 107(5) of the Act, the county government actual expenditure on development shall be at least thirty percent in conformity with the requirement under section 107(2)(a) of the Act;

(h) If the county government does not achieve the requirement of regulation 25(1)(f) above at the end of the financial year, the county executive committee member for finance shall submit a responsibility statement to county assembly explaining the reasons for the deviation and provide a plan on how to ensure annual actual expenditure outtu as well as medium term allocation comply with the provisions of Section 107 (2) (a) of the Act and these regulations in the subsequent years; and

(i) The compliance plan above shall be binding and the county executive committee member for finance shall ensure implementation

CHAPTER TWO

PUBLIC DEBT STOCK IN THE COUNTY

2.0 Key Highlights on the debt

The overall debt consists of statutory debt, owing to suppliers of goods and services, legal creditors, personnel emoluments, loans and contingent liabilities.

The total debt portfolio stood at Kshs.66.57B as at 30th June, 2018 , an increase of 10.07 B compared to Kshs.56.5B as at 30th June, 2017.

The County Debt as at 31st December 2018 stood at Kshs.70.20B

The stock of debt is mainly composed of unpaid statutory deductions Kshs.30.13B. unpaid suppliers and contractors and litigations of Kshs.10.63B, Utilities of Kshs.0.64B. owed to Kenya Power, benefits owed to retired and deceased staff of Ksh 0.134B and a bank loan of Kshs.3.02B.

In addition, the County inherited a large debt portfolio from the defunct City Council of Nairobi, part of this debt are long-term loans amounting to Kshs.19.14B.from taken from development partners for the expansion of water infrastructure in the 70's by the defunct Council and housing guaranteed by the National Treasury. The debts remained in the books of the former City Council of Nairobi until the 2013 when the County Government took over. Further, the County also inherited debts owed to various statutory creditors and merchants. The County also inherited Kshs.5 B. commercial bank loan, which the defunct City Council of Nairobi had taken to finance payment of statutory debts.

Stock of Debts

2.1 Table I: Summary of Outstanding Debts as at 30th, June 2018 in billions (B.)

	SUMMARY NAIROBI CITY COUNTY LIABILITIES		
		30.06.2017	**30.06.2018**
1	Statutory creditors	23,018,436,066	30,132,956,202
2	Suppliers/Contractors	3,787,610,031	5,197,897,213
3	Legal Creditors	2,339,264,112	544,2127,207
4	Utilities	487,276,629	875,716,686
5	Loan	4,973,231,829	3,024,371,706
6	Contingent Liabilities	21,768,297,573	21,768,297,573
7	Employee benefits-Retirees/ Deceased	142,249,068	134,647,551
	TOTAL	**56,516,365,308**	**66,576,014,140**

The debt has risen to Kshs. 70.20B by the end of second quarter, 31st December 2018

Debt Management

The PFMA 2012 section 107(2e) requires that City County debt be maintained within a sustainable level, as approved by the County Assembly, section 107(3) requires that short term borrowing be restricted to management of cash flows and not exceed 5% of recent audited government revenue. In complying with this, the City County will only issue debt when necessary to fund projects.

Long-term borrowing will only be used to finance development projects as approved in the CIDP (to a limit of 5% of the recently audited financial statements) and projects funded by debt will only be funded for their expected useful life. Operations and management expenditure will not be funded through debt. To maintain debt at sustainable levels, the City County's borrowing per the debt management strategy will be capped at 15% of total revenues.

The City County has introduced initiatives to manage its current debt levels:

- Debt rescheduling/renegotiation - the City County will seek to reschedule current bank loans with a view to obtaining favourable terms for a longer period. This is aimed at releasing scarce resources to service delivery by easing pressure on cash flows;
- Large infrastructure projects will be financed through external borrowing as this is concessional and requires longer periods of time than what commercial banks normally offer;
- The City County may look into money and capital markets through the issuing of bonds;
- Negotiations will be undertaken with various creditors with a view to effect debt/asset swaps; and
- Negotiations will be entered with the National Government with an aim of writing off debts that were guaranteed by the Central Government to the defunct Local Authority.

This is aimed at cleaning the balance sheet and improve the City County's credit worthiness.

Financial Sustainability
To ensure long-term financial sustainability, sound financial principles must be applied. The Nairobi City County follows the principles of public finance in financial management as outlined in Article 226 of the Constitution of Kenya and Public Finance Management Act 2012.

Revenue and Expenditure
The City County expenditure and revenues for the financial years 2016/2017 to 2017/2018 are shown in the figure (1) below. Financial deficits were experienced in the financial years 2010/2011 and 2011/2012, however current projections indicate financial surplus will arise in the financial years 2019/20 and 200/2021.

The intergovernmental Relations Technical Committee (IGRTC) took over the residual functions of the Transition Authority (now defunct) pursuant to Section 12 (b) of the Intergovernmental Relations Act, 2012. IGRTC vide a legal notice no. 858 published in the Kenya Gazette on 27th January, 2017 is mandated in consultation with the relevant stakeholders to develop guidelines and liquidation options for settlement of the liabilities of the defunct local authorities. Negotiations are ongoing to obtain more information on those debts for ease of settlement.

With the increased appetite, for funding of large capital projects there is need to be cautious on the level of debt accumulation. Domestic borrowing and revenue raised are used to service public debt and little resources are freed for development expenditure. The Public Finance Management Act (PFMA 2012) Section 107 (2e) requires the debt to be maintained at a sustainable level as approved by County Assembly. Section 107 (3) requires that the
short term borrowing is restricted to management of cash flows and not exceed 5% of the recent audited County Government revenue (CIDP, 2014).

Budgeting and Funding
Over 50% of the budget is currently funded by the National Government making the City County heavily dependent on state funding. To satisfy the increasing funding needs, the Development of New Capital Financing Strategies has been initiated such as public private partnerships, lease financing, labour trade off platforms, constituency-county project financing and government financial arrangements. The City County is leveraging on external funding for resource mobilization as stipulated in the CIDP.

The City County is also using technology and innovation to widen the tax base and reduce lost revenue. These include the introduction of waivers to encourage payment of accrued fees, as well as a graduated rate scale for business licenses and land valuation among others. There is however, need to further

develop and implement financial strategies that will put the City County in a financial position to fund all planned projects.

Capital Prioritization

It is imperative to note that during the budgeting process, projects are prioritized in a manner that objectively balances risk, capital limitations and regulatory requirements. The Finance and Economic Planning sector is responsible for providing consultation on budgeting matters such as the budget reviews, the fiscal strategy paper and outlook papers.

Projects and the corresponding capital requirements of the sectors are not always aligned to the budget. This has contributed to a low capital expenditure rate within the sectors and delayed implementation of planned projects. The current financial management processes is being reviewed for effective service delivery to the public. This is mainly due to the manual nature of the financial process and the disempowerment of the spending units. All approvals are done at the Treasury causing lengthy delays in the procurement and payment process. Thus the cause of current big debt portfolio.

CHAPTER THREE

3.0 COST AND RISK ANALYSIS (SITUATIONAL ANALYSIS)

Paramount to the effective management of the public debt is ensuring an appropriate balance between the relative costs and risks in the public debt portfolio. The MTDS provides a diagnostic framework through which cost and risk assessments of alternative financing strategies are conducted. While cognizant of the varied risks to the debt portfolio, the MTDS focuses on the quantification and management of market and refinancing risks.
Market risks relate to changes in macroeconomic or financial variables that impact the debt portfolio, either through valuation effects or debt service costs.

In line with prudent management of risks envisioned in section 107 (2)(f) of the PFM Act, 2012 the County Executive Committee Member shall in the County Fiscal Strategy Paper include a statement of fiscal risks outlining the potential policy decisions and key areas of uncertainty that may have a material effect on the fiscal outlook and the statement shall include—

(a) Potential policy decisions affecting revenue, taxpayer behavioral responses and court decisions that are likely to affect revenue bases and overall tax and revenue collections and government income, including tax concessions (or tax expenditures), increase in tax rates, tax minimization and avoidance by tax and rates payers;

(b) Potential policy decisions that could increase or decrease expenses depending on decisions taken, and which constitute risks to the fiscal forecasts only to the extent that they cannot be managed within existing baselines or budget allowances;

(c) Potential capital decisions that are risks to the fiscal forecasts only to the extent that they cannot be managed within existing county government balance sheet;

(d) Matters dependent on external factors such as the outcome of negotiations or international obligations; and

(e) A list of contingent liability including debt guarantees.

3.1 Market Analysis

The main market risks are exchange rate, interest rate, and inflation risks. The public debt portfolio continues to be significantly exposed to foreign currency risk. Given the current trajectory of interest rates in the external and domestic markets and considering the monetary policy dynamics at play, there are potential upside risks to interest costs over the medium-term. Inflation risks are subdued due to low exposure and low and stable inflation expectations over the medium-term.

Interest Analysis

Interest rate risk measures the portfolio's exposure to changes in market interest rates.

Adverse movements in interest rates can increase debt service costs for variable-rate debt and will have implications for the cost of rolling over near-to-maturity fixed-rate debt.

Inflation Analysis

Inflation-linked debt instruments are attractive to potential investors in a context of high and unpredictable inflation. Upward movements in the inflation rate will increase the nominal value of inflation-linked debt, thereby preserving value for the investor but increasing the costs to the County Government. The extent of the impact will depend on the inflation rate and the portfolio's exposure. Inflation-linked bonds are only in the domestic portfolio.

Debt Vulnerability Indicators

The financial Status over recent years have highlighted the significance of sound debt and liquidity management practices in minimizing the fallout from external shocks. The above assessment of market risks for the debt portfolio does not give an indication of the County's ability to withstand these shocks. Debt service to revenues is an indicator of the County's ability to honour its debt service obligations.

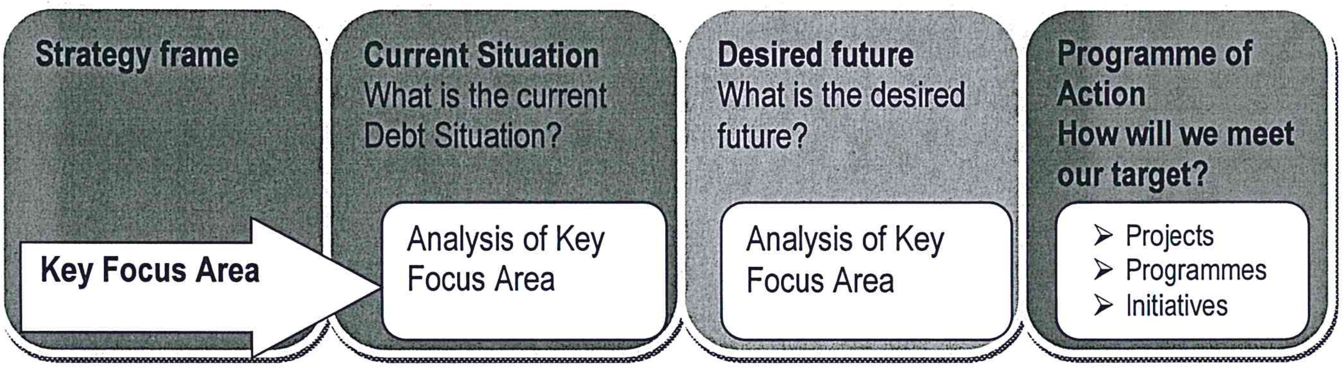
Refinancing risk

Refinancing risk is the probability that debt will have to be refinanced at unfavourable terms, or in extreme cases cannot be refinanced at all. Refinancing risk is measured by assessing: the share of debt maturing in one year or less; the average-time-to-maturity (ATM) of the debt portfolio; and the maturity profile to identify the concentration of debt maturing within a given period. The share of debt maturing in one year or less gives an indication of the immediate refinancing risk in the debt portfolio.

3.2 Gap Analysis and Programme of Action

The programme of action is based on the results of the gap analysis within the County Debt Management Portfolio. Firstly, the 'current state' of each Key Focus Area (KFA) determined during the visioning and strategy workshop with the leadership of the Nairobi City County.

Subsequently, the 'desired future' is outlined. The difference, or gap, between the two situations presents clearly, which actions need to be undertaken to achieve the desired future situation. These actions form the Programme of Action; see Chapter 4 for more information with regards to the implementation of the programme of action and subsequent monitoring of progress.



DEBT MANAGEMENT	
Current Situation ➢ Weak Debt Management System ➢ Under staffed ➢ Weak internal control system	**Desired Future** ➢ A robust automated Debt payment system ➢ Minimize Debt profile ➢ Establish Debt Policy, procedure and Registry
Programme of Action **Projects** ➢ **Automate Debt Payment System** ➢ **Well staffed Debt Department** **Programme** ➢ **Develop and implement Debt Strategy Policy, Procedure and controls**	

- **Review monthly payment status of debtors**
- **Develop and implement debt trucking processes**
-

Initiative

- **Comply with legal requirements**
- **Monitor cash flow management framework**
- **Comply with Accounting Standard Board Standards**
- **Co-ordinate Debts across the sectors**
- **Develop and implement a plan to increase debt collection on rates, licenses, and disembusments**
- **Develop and implement a plan to meet debt set targets**

3.3 DEBT MANAGEMENT STRAGEGIES

Strategies to deal with statutory Debt

1: Debts /Asset Swops
2: Debt rescheduling/renegotiation;
3: Payment of Current Statutory deductions as at when they fall due;

Strategy 1: Debts /Asset Swops;
Where the County owes various statutory creditors/utility firms who also owes us various debts in terms of rates, the County will enter into negotiations with the various creditors with a view to effect debts/assets swops.

To settle the outstanding amounts on the KRA Account the County will approach the National Government and negotiate a debt swap against the amounts owed by the National Government in outstanding rates. In the meantime, the County shall continue to pay monthly deductions of PAYE as and when the salary is paid.

To settle this amount owed to Lap-trust the County in the past has negotiated with the statutory creditor for a property swop to transfer to the scheme one of our prime asset/Estate in respect to accrued debts..

Currently a debt swap negotiated with NSSF is still in force against property rates.

Strategy 2 : Debt rescheduling/renegotiation;
The County will seek to renegotiate with various statutory creditors on the debt owed with a view of interest freeze and interest waivers on older amounts owed
.

Strategy 3: Payment of Current Statutory deductions as at when they fall due;
The County treasury intends to pay all statutory deductions as at when salary is paid every month to militate against growth of the debt.

Debt owed to Suppliers of goods and services/ Legal
The County initiated projects whose payments have over-time been rolled over to consecutive financial years. Sectors procure late in the year leading to rollovers and growth in pending bills. This is mainly due to fluctuating revenues, that affect the cash flow projected leading to growth in unpaid merchants at each year-end. The volatility of the economy and government policy affects revenue collection.
Growth in litigations by and against the County has led to an increase in amounts owed to legal creditors.

Strategies to deal with supply of goods and services debt
1: Verification of arrears
2: Increase budgetary allocation on the pending vote and decentralise the same to sectors.
3: Enhance compliance to the legal framework and upscale capacity of the County legal services.

Strategy 1: Verification of arrears
Data on outstanding claims is available but the same needs verification to boost validity and reduce fraudulent claims. The internal audit department of the County, private audit firms or an appointed committee will undertake verification. A Pending Bills Committee was gazetted by H.E. The Governor to scrutinize and verify the pending bills of the county.
The National Governmnet through the Office Of the Audtor General is also undertaking a special audit of the county pending bills.

Strategy 2: Increase budgetary allocation on the pending bills vote and decentralise the same to sectors.
There are proposal to increase budgetary allocations to cater for the growing debt portfolio.Sectors should also factor in their budget proposal aalocations to meet their pending bills.As a matter of principle pending bills and roll over project shoul be given priority in any new financial year or budget allocation.

Strategy 3: Enhance compliance to the legal framework and upscale capacity of the County legal services

No new commitments for supply of goods and services shall be done after 31st May of each year in accordance with the provisions of Section 50(1) of the Public Finance Management (County Governments) Regulations, 2015 except with express authority of the Accounting officer in writing.This will reduce or elimminate roll over of peojects and growth of pending bills at the end of the financial year.
Enhanced compliance to the law in order to reduce litigations against the County while reducing legal cases against other entities will minimise the legal debts,which are mainly legal fees and decretal sums against the county.There is also a need to have a well established and staffed County legal department

Debt owed to Utilities Firms
The debt has accumulated to Ksh 875,716,686 as at the close of the FY 2017/18 This is an accumulation of electricity bills owed to Kenya Power and also the County owes Nairobi Water & Sewerage Company for water consumption to its various entities. The debt accumulated because of withdrawal of the lease rentals by the company.

Strategies to deal utilities Debt

1: Debt swap
2: Verification of arrears
3: Realisting payment plan

Strategy 1: Debt swap
The county is in negotiations with Kenya Power to swop its debt against wayleaves owed to the county.
The county is also pursuing debt swap with Nairobi Water against what the water company owes the county for use of county infrustructure.

2: Verification of arrears
Verification of debts between the county and these utilities companies is paromount in negotiations and plans on way forward to clear the debts.

3: Realisting payment plan
A clear and realistic payment plan must be put in place to ensure this debts are cleared by the county government.This plan must be in line with the realistist cashflow forecast.

Contingent Liabilities
This consists of on lent water loans and government guarantees that date back to the defunct council for construction of water infrastructure, Umoja II housing and historical actuarial deficit, interest and penalties owed to Lap-trust. The loans were obtained years back by the defunct City Council of Nairobi for the development of water infrastructure and construction of Umoja II housing scheme. The loans were obtained from the World Bank, USAID, and Local Government Loans Authority (LGLA).The loans were guaranteed by the National Government and in view of lack of documentation for the loans the County has approached the National Debt Management Office with a view to write off these loans from our books. The guarantee and on-lent water loans have remained un-serviced and static in the books since the era of the defunct council and now in the County.

Strategies to deal with contigent liabilities
1: Debt Renegotiation
2: Debt write offs

Strategy 1: Debt Renegotiation and write offs
In order to clean our balance sheet and improve our credit-worthiness, the County shall enter into negotiations with the GOK with a view to write off debts

that were guaranteed by the National Government to the former City Council of Nairobi.
On the acturial deficit and interest dating back the County intends to renegotiate with the statutory creditors.

Bank Loan
At the close of the financial year 2017/2018 the County had a long-term loan owed to KCB which was inherited from the defunct Council. The Loan is repayable at the rate of 13% per annum for 9 years. The loan is repayable on a quarterly basis at Kshs. 141 Million per quarter and budgeted from our revenue hence the need for re-negotiation of the loan.The current loan balance stands at Ksh 3.2B

Strategies to deal with the loan debt
1: Debt Rescheduling
2: Repayment plan

Strategy 1: Debt Rescheduling
There is need to renegotiate with the banks to reschedule the current bank loan with a view to obtaining favorable terms and for a longer period. Negotiations are underway with various banks for rescheduling of the loan terms.

Strategy 2: Repayment plan
The County Treasury intends to come up with a detailed, realistic repayment plan, which can be adopted in servicing the loan. A clear and realistic payment plan must be put in place to ensure this loan is serviced to avoid additional cost in terms of interest and penalties.This plan must be in line with the realistic cashflow forecast.

CHAPTER FOUR

4.0 VISION AND PROGRAMME OF ACTION

4.1 Debt Management Plan

PFM Act, 2012, Regulation 176. County government borrowing shall be guided by the following principles—

(a) need to ensure stability of domestic financial markets;
(b) promotion of inter-generational equity in the sharing of burdens and benefits of public borrowing;
(c) determination of thresholds of borrowing rights for both levels of government;
(d) use of objective criteria for evaluating county government eligibility for national government debt guarantee; and
(e) prudence and equity in setting limits for debt stock levels for each county government.

PFM ACT. 2012, County regulation 177

(1) The County Executive Committee Member derives powers to raise loans for the County Government from section 140 of the PFM Act. 2012

(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 manners—

(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.
(3) Any borrowing by a county government under paragraph (2)
(a) and (c) of this regulation shall require a national government guarantee pursuant to section 58 of the Act.

PFM Act, County 178. The county governments may borrow in pursuant to the requirements of sections 140 of the Act for the purpose of—

(a) financing county government budget deficits; or
(b) cash management; or
(c) refinancing outstanding debt or repaying a loan prior to its date of repayment; or
(d) mitigation against adverse effects caused by an urgent and unforeseen event in cases where the Emergency Fund has been depleted; or

(e) Meeting any other development policy objectives that the County Executive Committee Member shall deem necessary, consistent with the law, and as County Assembly may approve.

Risk Factors

Adverse changes in underlying macroeconomic and market variables can negatively influence the fiscal and debt dynamics. The risk to the portfolio will depend on the likelihood of occurrence and the fiscal or financial impact of the change.

4.2

Fiscal Impact

LOW	Moderate	Major
Government Guaranteed Loans (GGLs): GGLs are a potential fiscal risk to the Government. The impact on the debt will depend on the probability that a GGL will be called or assumed by the value of the guarantee. Consistent with the legislated limits as per the PFM Act 2012, the County has been reducing its exposure to risks from GGLs. Accordingly, the share of GGLs to GDP has been decreasing and is estimated at 5.5 percent at December 2018, only 0.5 percentage point above the legislated target for FY2021/22.	**Fiscal Management:** Weak institutional frameworks in economies precipitate unsustainable and irresponsible fiscal and monetary policies by county governments. This has led to fiscal slippage, economic contractions and ballooning public debt across these countries	**Financial Crises:** Financial crises can have significant negative effects on the economy and the sovereign debt. The financial crisis in county is estimated to have cost upwards of 40 percent of GDP. However the adoption of stronger financial regulations and best practices reduces the likelihood of a reoccurrence.
Public Private Partnerships (PPPs): The use of PPPs as a modality to mobilize investment, particularly in infrastructure development and energy and water generation are common in many developing economies. These types of arrangements impose potentially significant fiscal risks if not properly managed and monitored.	**Shocks in Commodity Prices:** Adverse shocks in commodity prices, especially oil prices, can have major effects on the government's BOP and overall fiscal accounts. Though potentially large on the fiscal, the pass through to the debt portfolio is expected to be more moderate	**Natural Disasters:** Natural disasters pose significant fiscal risks to the County. The adoption of a suite of disaster risk finance instruments including indemnity type insurance coverage and contingent lines of credit will aid in reducing the fiscal impact of natural disasters.

		Low Growth and High Crime Rates: High rates of corruption pose a significant risk to prospects for improvements in productivity and economic growth. Higher corruption related expenditures will also impact the budget directly. Low rates of economic growth (GDP) will impact the fiscal through low revenue generation and potentially higher demand for social spending, which could lead to increases in County Government borrowing. However, an increased focus on corruption fighting and strong and improving macroeconomic fundamentals support projections for economic growth over the medium-term.	**Market Volatility:** Volatility in macroeconomic and market variables can result in higher debt service costs. The adoption of an inflation targeting regime could aid in the stabilization or reduction in the volatility of domestic market rates thereby reducing the risks to the debt portfolio.

4.3 Programme of Action for Debt Management

To realize the programme of action, the projects, programmes and initiatives having been identified within the Finance and Economic Planning Sector under the Debt Management Department for implementation of the identified activities across other sectors within the county based on their debt profile to monitor and evaluate their debt portfolio. Through the system, quarterly and annual targets are monitored to determine the performance of each sector.

Programme of Action How will we achieve this?	**Sector responsible?** Who will be responsible?	**Timeframe** When will it be executed?	**Budget** What is the budget?	**Source of funding** Source of funding?
Project				
Programme				
Initiative				

Other Strategies to deal with the debt under Programme of Action

Public Private Partnerships
The County is considering engaging private partners to develop high investment return projects like multi-storey parking, increasing the parking slots and modernizing stadiums under the Urban-Renewal projects. The county also has plans to build low cost housing in partnership with private investors.

.Enhancing credibility and realism of the budget
One of the first steps in addressing a persistent arrears problem is to strengthen the realism of the annual budget. This will depend on robust assumptions and forecasts in the fiscal framework, which determines the budget. Internal revenues should be realistic and should be in tandem with the expenditure. The County should enhance revenue collection while setting up realistic revenue targets.

In the past, one of the causes of increased pending bills has been unrealistic revenue projections that encourage procurement of goods and services beyond the County's ability to finance payments.

Strengthening commitment controls
Commitment controls are part of the internal control system, which should prevent the County from initiating expenditure without available budget and cash. IFMIS as an efficient tool of financial management shall enforce commitment control to ensure that expenditure incurred in a financial year is in tandem with the budget.

Improving cash and debt management

Reliable cash forecasting should ensure that liquidity is available to meet payment obligations as they arise. For effective cash management, the county treasury seeks to develop accurate and timely short-term estimates of cash inflows and outflows.

Regulation 86 (1) of the PFM Act, 2012 advices the County Executive Committee Member for Finance to establish a Cash Management Advisory Committee which is key in improving cash flow management.

The County Treasury shall increase budgetary allocation on debt servicing every year to reduce the debt burden. The county treasury proposes every sector to budget for pending bills. In line with accounting policies the debts should take first charged in every new financial year.

Strengthening legal and regulatory framework

The legal framework or related regulations should define payment terms (and when a payment is in arrears); reporting requirements; controls at the budget authorization, commitment, and payment stages; and the sanctions associated with any breach of those provisions.

In this regard, the County Treasury intends to draft a payments policy that will prioritize payment based on urgency, availability of funds and the age of the payment.

Enhancing revenue collection

Further the County shall also explore ways of enhancing revenue collection in order to liquidate these debts to improve liquidity.

CHAPTER FIVE

5.0 MICROECONOMIC OVERVIEW

Growth in the global economy was moderate during 2018 due to growing geopolitical tensions, a slowdown in international trade, tighter financing conditions and lower rates of investment in both advanced and emerging market economies (EMEs).

Looming uncertainties surrounding the possible escalation of geopolitical tensions and financial market stress stymied investor sentiment and softened growth prospects for 2019.A major risk for emerging market economies (EMEs) in the current financial environment is the increased tightening of credit conditions arising from the acceleration of monetary policy normalization across advanced economies.

During this review period, the tightening of monetary policy in advanced economies triggered capital outflows from EMEs, which will adversely impact on equity prices and currencies, while significantly raising borrowing costs and reducing monetary policy space.

While there is generally more tepid demand for emerging market assets during this review period, country-specific characteristics influenced the performance of individual EM sovereigns in the international capital markets. Continued strengthening of Kenya's macroeconomic environment, supported by sustained improvement in the fiscal accounts and advances in monetary policy effectiveness, contributed to the strong performance of Kenya's global bonds compared to other regional economies. Kenya's economic performance was buoyed by continued macroeconomic stability, anchored by sound fiscal and monetary policy reforms under the International Monetary Fund Precautionary Standby Arrangement (PSBA). It is expected that all quantitative fiscal and monetary performance targets under the PSBA, except for the inflation target, will be met through to December 2019.

Strong revenue performance and more measured expenditure growth contributed to a fiscal surplus of 0.5 percent of GDP in FY2017/18. A fiscal surplus of 0.3 percent of GDP is projected for FY2018/19 with a gradual increase over the medium-term to 2.3 percent in FY2020/21. Strict adherence to a primary balance target of 7.0 percent of GDP over the medium-term will ensure continuance of the downward trajectory in the debt-to-GDP consistent with the legislated target of no more than 60.0 percent by end-March 2024.

5.1 IMPLEMENTATION FRAMEWORK

Item	Action	Responsibility	Timeline	Comments
1.	Comply with legal requirements to access National Government Transfers			
2	Conduct a revenue potential study			
3	Conduct a revenue potential study			
4	Co-ordinate revenue across the sector			

CHAPTER SIX

CONCLUSION

The Medium-term Debt Management Strategy for FY2019/20-FY2022/23 outlines the County Government's strategic priorities for the management of the public debt over the medium-term. It provides an assessment of the relative costs and risks for the debt portfolio and considers alternative financing strategies to meet the broad objectives of raising adequate funding at the lowest possible costs at prudent levels of risk.

During FY2018/19, the Government continued to realize improved fiscal performance and strong macroeconomic fundamentals. This supported improvements in key cost and risk indicators for the debt portfolio as reflected in the improved indicators for interest rate and refinancing risks. Low domestic interest rates offset increases in external interest rates and resulted in a marginal reduction in interest costs over the review period. The nominal value of foreign currency debt decreased over the review period; however, larger net redemptions in the domestic portfolio relative to the external portfolio contributed to a marginal increase in the indicator for the share of foreign currency debt in total debt. Notwithstanding, the improvements in the risk profile of the public debt portfolio, foreign currency, and refinancing risks remain the chief concerns of the County Government.

The financing strategy for FY2019/20 continues to focus on rebalancing the portfolio towards a greater proportion of domestic debt vis-à-vis external debt while at the same time reducing exposure to refinancing and interest rate risks, by borrowing mainly at fixed-rates across the yield curve in the domestic market. An important element of the proposed financing strategy this fiscal year is the increased focus on shorter-tenor issuances.