President Ruto presents Memorandum of Referral as he declines to assent the Finance Bill 2024

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President William Ruto declined to assent into law the Finance Bill 2024 against the backdrop of widespread protests in Kenya against the Bill in recent days. Through the Presidential Memorandum of Referral, President Ruto recommended a deletion of all clauses in the Finance Bill 2024. Technically, withdrawal of a Bill after it has been passed by Members of Parliament (on Tuesday's sitting session) is impractical necessitating the Presidential Memorandum of Referral. Nevertheless, the National Assembly proceeded on recess after yesterday's session prior to the President's announcement, but we anticipate a special sitting for the National Assembly to officially vote on the Presidential Memorandum of Referral.

Highlights of President Ruto's speech

- The President emphasized the outsized impact of debt servicing (interest and amortization) on revenue with 61.0% of revenue going towards meeting debt obligations. The outstanding USD 567.0mn KENINT 2024 was settled on Monday this week, following the buyback of USD 1,443.0mn from the net proceeds of KENINT 2031 in February this year.
- The FY25 budget has been revised lower from KES 4,188.0bn in the 2024 Budget Policy Statement to KES 4,006.0bn tabled by the National Treasury Cabinet Secretary.
- Following the vibrant public participation on the Finance Bill 2024, the Finance Committee made some concessions and dropped some of the contentious tax proposals that included imposition of 2.5% motor vehicle circulation tax, standard rating VAT on bread at 16.0% and imposition of Eco Levy on specified goods. With the costing of the Finance Bill 2024 as initially proposed pegged at KES 346.0bn, President Ruto stated that the concessions have led to a downward revision in the expected tax yield to KES 200.0bn.
- The President further directed austerity measures to reduce FY25 expenditure, more so for non-core recurrent spending, essentially blunting the impact of his refusal to assent the Finance Bill 2024.

Our views:

Impact of Finance Bill 2024 hit slightly overamplified

- Costings of Finance Bills are never publicized by the National Treasury, although the Finance Committee initially pegged it at KES 302.0bn. Subsequently, the costings seem to have increased to KES 346.7bn. However, this amount includes the revenue yield to be generated from Import Duty. As Import Duty is expected to generate an additional KES 45.0bn, we estimate the actual costing of the Finance Bill 2024 at KES 301.7bn (1.7% of GDP).
- That said, the performance of Finance Act 2023 has been disappointing. Against expected yield of KES 215.0bn in the FY24 budget, the actual outturn in the first 11-months has been 61.0% of the overall FY24 target. This amplifies the two-pronged approach of tightening administrative measures over and above the tax proposals that are contained in the Finance Bill to ensure the targeted revenue yield are achieved.
- Nevertheless, the start of the FY25 budget year will continue based on the main existing tax laws of Income Tax Act, Value Added Tax and Excise Duty Act.

Likelihood of a Special Sitting to formally approve the Presidential Memorandum of Referral

- The Presidential Memorandum of Referral was publicized after the National Assembly commenced its short recess following the adjournment of yesterday's sitting, and are expected to resume regular sittings on July 26. Under Kenyan law, a Bill passed in Parliament effectively becomes a Law after 21 days if the President does not assent the Bill. We thus see the likelihood that the National Assembly is called for a Special sitting to deliberate on the Presidential Memorandum, at the very earliest, next week at the start of the FY25 budget year.
- Furthermore, we noted that the President remained silent on the Appropriations Bill 2024, which was also passed on Tuesday by Members of Parliament. With the start of FY25 budget year imminent, the President is likely to assent the Appropriations Bill 2024 that effectively authorizes withdrawal of monies from the Consolidated Fund to finance the approved expenditure. With the President proposing further austerity measures to blunt the impact of his Presidential Memorandum, these tees the odds of a Supplementary Budget, rather than a revision in the spending Bill.

We see higher fiscal deficit from the 3.3% baseline in FY25

- Although the President has called for further tightening in expenditure, we see less wiggle room. Interest payment accounts for 25.0% of the FY25 budget, whereas recurrent spending is approximately 41.0%. The President hinted of broad-based cuts in the operational budget such as travel expense, hospitality and purchase of motor vehicles, renovations and other expenditures, that fall under recurrent expenditure. Going by recent Supplementary budgets, negative adjustments have been on development spending, as opposed to recurrent spending, and we are of the view this will be the base case with the upcoming FY25 Supplementary Budget I.
- Amidst a lack of prioritizing the domestic arrears which closed 1Q2024 at KES 486.9bn, 2.7% of GDP, the authorities will have a tight balancing act accommodating further tightening in the FY25 budget. Notably, the FY25 budget has been reviewed lower by 4.3% from the estimates tabled in the February 2024 Budget Policy Statement and the estimates presented at the FY25 budget statement by the National Treasury Cabinet Secretary.
- We expect the fiscal deficit to widen to 5.0% from the baseline of 3.3% in FY25, with domestic financing doing the heavy lifting. In nominal terms, we estimate domestic borrowing target in FY24 post Supplementary Budget II at KES 723.9bn (4.5%) and the FY25 budget as tabled indicated domestic borrowing at KES 277.6bn (1.5%). As such, the authorities may be inclined towards more domestic financing if the envisaged budget cuts are less significant.

Approval of the IMF 7th review in limbo with eyes on the imminent legislative process

- In a short statement on 26th June 2024 on Kenya, the IMF indicated its concern about the negative spillovers of the recent protests that have rocked Kenyan towns. The IMF also reiterated its *"main goal in supporting Kenya to overcome the difficult economic challenges it faces and improve its economic prospects". The* recent developments with the President's memorandum on the Finance Bill casts a long shadow on fiscal reforms under the ongoing programme, and the approval of the disbursement following the seventh review with the Executive Board meeting slated for July 12. We are of the view that the next hurdle would be the speed in approving a FY25 Supplementary Budget, following the formal MPs' approval of the President's memorandum. With FY24 tax revenue adjusted by KES 250.0bn, and which will be one of the quantitative performance criteria for the next 8th review, the IMF may take a wait-and-see approach as it monitors the legislative process of the requisite FY25 budget adjustments.

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