FUNDAMENTALS

KENYA FY26 BUDGET UPDATE

CLARITY NEEDED

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IN BRIEF

- The Cabinet Secretary (CS) for the National Treasury John Mbadi is expected to table in Parliament the FY26 Budget statement. This will be CS Mbadi's maiden budget speech, having been appointed in August 2024. In line with the PFM Act, this event is coming at the tail end of the budget making process with the FY26 fiscal framework already patched up.
- From our estimates, the total FY26 budget excluding debt amortization amounts to KES 4,291.9bn and within the ceilings approved by Parliament in its consideration of the 2025 Budget Policy Statement (BPS). This notwithstanding, there has been a slight uptick to the spending plan from the estimates tabled at the end of April 2025 by the National Treasury.
- From our assessment of BAC report that was publicized last week, there were KES 235.6bn additional requests that remained unfunded, including KES 33.9bn hole arising from the US funding aid freeze that is affecting the health sector. Furthermore, the potential carryovers from this fiscal year on weak revenue outturn, and the unfunded requests are likely to push upwards the spending plan and trigger a Supplementary budget at the front end of executing FY26 budget.
- Disaggregating the KES 176.0bn targeted ordinary revenue increase, Finance Bill 2025 is targeting to raise KES 40.0bn, whereas the Tax Laws (Amendment) Act 2024 and Tax Procedures (Amendment) Act 2024 that were passed in late December 2024 to yield KES 70.0bn this fiscal year. Absent ramped up tax administrative measures, there should be a funding gap of at least KES 66.0bn in FY26 budget. The possibility of a follow-up Tax Laws (Amendment) Bill 2025 later in the year could be a mitigating wild card, in our view.
- We applaud the authorities' efforts in recognizing the need to settle the domestic arrears, colloquially pending bills, that comprise outstanding payments to contractors and suppliers, and outstanding unremitted pension contributions. There's a proposal to increase the per/litre Road Maintenance Levy amount from the initial KES 7/litre to KES 12/litre to settle roads sector domestic arrears. Outside this proposed securitization, there is the proposed privatization that is targeting to yield KES 149.0bn in FY26 budget year. Nevertheless, there is less clarity on the route of privatization, whether direct asset sales or Initial primary offers (primary and/or secondary), which we hope the FY26 budget statement should clarify.

Budget Day

The Cabinet Secretary (CS) for the National Treasury John Mbadi is expected to table in Parliament the FY26 Budget statement. This will be CS Mbadi's maiden budget speech, having been appointed in August 2024. In line with the PFM Act, this event is coming at the tail end of the budget making process with the FY26 fiscal framework already patched up. On the spending side, the National Assembly approved the spending plan to the national government while the non-discretionary spending under the Consolidated Fund Services (CFS) will be approved prior to the FY26 Budget statement. In any case, the CFS expenditures are priority items on the budget, so the approval will be a formality. On the financing side, the Finance Committee is at the tail end of incorporating the public input of the Finance Bill 2025 prior to tabling its report with recommendations. Overall, the budget statement speech, albeit pronouncing largely what is in the public domain, will also be an opportunity to get some clarity on some outstanding issues.

This note is an update on our previous Kenya FY26 Budget note here and highlights our three top emerging issues in the upcoming fiscal year.

Vulnerabilities to the fiscal consolidation efforts

From our estimates, the total FY26 budget excluding debt amortization amounts to KES 4,291.9bn and within the ceilings approved by Parliament in its consideration of the 2025 Budget Policy Statement (BPS). This notwithstanding, there has been a slight uptick to the spending plan from the estimates tabled at the end of April 2025 by the National Treasury. This amplifies the rigidities in the budget formulation, even as the National Treasury pursues a fiscal consolidation path. Notably, the CFS expenditures are largely non-discretionary and comprises of interest payments of KES 1.1tn, and pension and salaries to Constitutional office holders to the tune of KES 239.6bn. The other contentious budget item is the equitable revenue share to counties that was proposed at KES 405.1bn in the Division of Revenue Bill 2025 and that was approved by the National Assembly. This notwithstanding, the Senate proposed a higher KES 465.0bn and thus mediation between these two Houses of the bicameral Parliament is expected to midwife a figure somewhere in between these amounts; essentially some upward bias to the FY26 budget plan.

Shifting attention to the discretionary budget items, spending by the National government, the Budget and Appropriations Committee (BAC) proposed an additional KES 33.0bn that was approved last week and on Tuesday this week, an additional KES 11.0bn was approved during the Committee of Supply stage as Parliament approved the spending votes by the national government. From our assessment of BAC report that was publicized last week, there were KES 235.6bn additional requests that remained unfunded, including KES 33.9bn hole arising from the US funding aid freeze that is affecting the health sector. The lobbying by spending units to their respective Departmental Committees and which necessitated the increase to the spending plan by the BAC is a major headwind to the fiscal consolidation efforts. Furthermore, the potential carryovers from this fiscal year on weak revenue outturn, and the unfunded requests are likely to push upwards the spending plan and trigger a Supplementary budget at the front end of executing FY26 budget.

Pleasantly surprising in this FY26 budget formulation there has been the failure to implement the recommendations of the Medium-Term Revenue Strategy planned tax proposals. Specifically, the reduction in the Corporate Income Tax from 30.0% to 28.0% had been penciled to be effective in FY26 budget. Understandably, the negative outturn in revenue mobilization in the current fiscal year with shortfall of KES 253.0bn in the first 10 months, July 2024 to April 2025, has lowered the prospect of an introduction to this much-needed accommodative tax proposal. Furthermore, the fiscal authorities adopted a much cautious approach in its Finance Bill 2025 that targets a modest KES 40.0bn on the upper end, markedly lower than the shelved Finance Bill 2024 that was eyeing KES 345.0bn.

Lethargic FY25 revenue outturn; razor sharp focus on FY26 target

Ahead of the FY26 budget statement, the Finance Committee is considering the Finance Bill 2025 and is expected to table its recommendation report next week ahead of the 30 June 2025 deadline. Surprisingly, the BAC report alluded to an increase in total revenue, ordinary revenue plus appropriation-in-aid, to the tune of KES 11.5bn. The budget statement may provide clarity regarding which of the two revenue streams has been revised higher. Should the increase be from ordinary revenue, this should complicate the ongoing mediation between the bicameral Parliament houses, given the necessity to increase equitable revenue share to counties.

The fiscal authorities also alluded to tabling a third Supplementary in this current fiscal year, given the negative revenue outturn. Should this be the case, the projected increase in ordinary revenue from this fiscal year to the next will jump from the baseline KES 176.0bn. Disaggregating this increase, Finance Bill 2025 is targeting to raise KES 40.0bn, whereas the Tax Laws (Amendment) Act 2024 and Tax Procedures (Amendment) Act 2024 that were passed in late December 2024 to yield KES 70.0bn this fiscal year. Absent ramped up tax administrative measures, there should be a funding gap of at least KES 66.0bn in FY26 budget. The possibility of a follow-up Tax Laws (Amendment) Bill 2025 later in the year could be a mitigating wild card, in our view.

Settlement of domestic arrears; securitization and/or privatization

We applaud the authorities' efforts in recognizing the need to settle the domestic arrears, colloquially pending bills, that comprise outstanding payments to contractors and suppliers, and outstanding unremitted pension contributions. Notably, the stock of domestic arrears reduced from KES 539.9bn in December 2024 to KES 421.6bn in March 2025. We understand that the Pending Bills Verification Committee is at the tail end of verifying the authentic domestic arrears. Nevertheless, the outcome of this process, the National Treasury has prioritized settling KES 229.0bn of the domestic arrears as an immediate priority.

Already telegraphed has been c. KES 80.0bn that is towards the roads sector via securitization of the KES 7/litre of the KES 25/litre from the Road Maintenance Levy (RML) utilized towards the instrument that involves the Trade and Development Bank (TDB) as lead arranger and transaction advisor. There's a proposal to increase the per/litre RML amount from the initial KES 7/litre to KES 12/litre towards raising KES 175.0bn to settle domestic arrears in the road sector, and additional KES 125.0bn for road projects in the pipeline. Outside this proposed securitization, there is the proposed privatization which targets KES 149.0bn in FY26 budget year. Nevertheless, there is less clarity on the route of privatization, whether direct asset sales or initial primary offers (primary and/or secondary), which we hope the FY26 budget statement should clarify.

KENYA FISCAL FRAMEWORK

	BUDGET, KES BN'S			% of GDP		
	FY25	FY26 Initial	FY26 Revised	FY25	FY26 Initial	FY26 Revised
National Government	2,346.55	2,497.55	2,549.54	13.5%	13.0%	13.2%
Counties' equitable revenue	418.26	405.07	405.07	2.4%	2.1%	2.1%
Consolidated Fund Services	1,242.74	1,337.32	1,337.32	7.1%	6.9%	6.9%
o/w Interest	*995.77*	*1,097.69*	*1,097.69*			
Expenditure and Net Lending	**4,007.55**	**4,239.94**	**4,291.94**	**23.0%**	**22.0%**	**22.3%**
Total Revenue	3,067.70	3,316.89	3,328.40	17.6%	17.2%	17.3%
Ordinary Revenue	2,580.90	2,756.98	-	14.8%	14.3%	
Appropriations-in-Aid	486.80	559.91	-	2.8%	2.9%	
Grants	52.64	46.94	46.94	0.3%	0.2%	0.2%
Total Revenue and Grants	**3,120.34**	**3,363.83**	**3,375.34**	**17.9%**	**17.5%**	**17.5%**
Fiscal Deficit (Financing)	**887.21**	**876.11**	**916.60**	**5.1%**	**4.5%**	**4.8%**
Net Foreign Financing	281.50	284.20	284.20	1.6%	1.5%	1.5%
Net Domestic Financing	605.71	591.91	632.40	3.5%	3.1%	3.3%
Privatization Proceeds		149.00	149.00			
Payment of part domestic arrears		(149.00)	(149.00)			
NOMINAL GDP				**17,434.50**	**19,272.80**	**19,272.80**

SOURCE: NATIONAL TREASURY

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