NATIONAL ASSEMBLY

OFFICIAL REPORT

Thursday, 15th June, 2000

The House met at 2.30 p.m.

[Mr. Speaker in the Chair]

PRAYERS

ARRIVAL OF HIS EXCELLENCY THE PRESIDENT

(Mr. Speaker announced the arrival of His Excellency the President, the hon. Daniel Toroitich arap Moi, M.P.)

(Hon. Members rose in their places while His Excellency the President took his seat in the Chair of State)

COMMITTEE OF WAYS AND MEANS

MOTION

THAT, MR. SPEAKER DO NOW LEAVE THE CHAIR

The Minister for Finance (Mr. Okemo): Mr. Speaker, Sir, I beg to move that Mr. Speaker do now leave the Chair.

PAPERS LAID

The Following papers were laid on the Table:-

2000/2001-Estimates of Revenue of the Government of Kenya for the year ending 30th June, 2001. Financial Statement for 2000/2001 (Budget).

(By the Minister for Finance)

The Minister for Finance (Mr. Okemo): Mr. Speaker, Sir, over recent years our economy slowed down to an unacceptably low growth rate. This has led to increased unemployment and poverty. Recognising the need for bold steps to reverse the situation, His Excellency the President took action to introduce greater effectiveness in the management of the economic affairs of the country by announcing in July 1999, major public sector reform initiatives. I wish to take this opportunity to sincerely congratulate His Excellency the President for that foresighted action which has started to bear fruit, to which my speech will bear testimony. I also wish to thank all the hon. Members of this House; the Cabinet and the parliamentary committees for their support which has facilitated my work over the past year.

INTRODUCTION

The most critical economic challenge facing Kenya today is the achievement of a broad-based sustainable improvement in the standard of living and welfare of all Kenyans. Today, about 52 per cent of Kenyans live below the poverty line. Living conditions of a large proportion of Kenyans both in rural as well as urban areas have either stagnated or worsened. Many have no access to basic amenities such as clean water and adequate shelter. Our problems have been compounded by the heavy toll taken by the HIV/AIDS epidemic and the high rise in crime and security. More recently, these problems have been worsened by an emerging drought which has decimated food supplies, caused water shortages and drastically reduced our hydro-electricity supply. Clearly, this situation is not tenable and must be reversed as a matter of urgency. The Government is taking actions to deal effectively and comprehensively with the drought related emergencies while at the same time implementing policy measures and programmes to initiate a sustainable economic recovery. The Government is putting in place the conditions needed to achieve sustainable rapid economic growth which is essential to experience a significant reduction in poverty and unemployment.

The theme of the budget this year is poverty reduction through sustainable economic growth. It focuses on achieving sustainable improvements in the performance of the economy and in the quality of life of all Kenyans. To realise this objectives we have adopted a longer term approach to our budget process that better links the budget to achieving our national development objectives. The 2000/2001 Budget is the first which is prepared under the Medium Term Expenditure Framework, shortly referred to as MTEF. This is a new approach to planning and budgeting. It emphasises full stakeholder participation in setting national priorities, expenditure prioritisation and transparency and accountability in public expenditures with the goal of achieving enhanced service delivery.

The MTEF will ensure that the Government spends taxpayers money well by radically changing the way it allocates and manages public resources. While revenue collection efforts have been efficient over the years, the delivery of services has deteriorated. The MTEF will restore credibility, predictability and effectiveness to the budget and the actual delivery of the public services to Kenyans. This MTEF is a three-year rolling plan covering the fiscal year 2000/2001 to 2002/2003, based on a realistic assessment of resource availability.

Planning and budgeting are first developed to meet sectoral priorities and then translated into ministerial budgets. The first year of the planning period has been translated into the detailed annual estimates. With this new budgetary system, Government ministries will be able to undertake their planned activities with greater predictability while Permanent Secretaries will be given greater autonomy to manage their resources, but will also be expected to be directly accountable for performance and results while adhering to the hard budget ceilings.

I now want to turn to the economic environment in which we are developing our budget framework. On the international front there are some brighter prospects. Stronger growth is expected in the OECD countries as well as many of the newly industrialised countries. Commodity prices are starting to recover from the Asian economic crisis. New opportunities are also presenting themselves. The passage of the United States Trade and Development Act offers new trade options particularly in sectors such as clothing and textiles which Kenya intends to pursue vigorously. The recent steep rise in world oil prices, however, has become a major burden for oil importing countries such as Kenya. The impact in the coming years will be even more adverse as we will be forced to increase our oil product imports to power generation to make up the shortfall in hydro-electricity supply.

The economic environment in sub-saharan Africa is a mixed one. Military conflicts and political instability are still disrupting economic development in our region and elsewhere. Drought has emerged as a major adverse factor in the near term in the EGAD region. On the bright side the prospects for expanded trade and development within the COMESA and East African Co-operation still remain attractive. Turning to the domestic economy, in 1999, the economic growth rate of 1.4 per cent was the lowest in six years. This is significantly below our population growth rate currently estimated at 2.4 per cent. The resultant fall in per capita incomes has led to a deterioration in the social and economic welfare of our population which is reflected in increased unemployment and worsening poverty.

The poor performance of the economy is linked to low levels of investment. Gross fixed capital formation has dropped from 21.4 per cent of GDP in 1995 to 15.1 per cent in 1999. The decline in investment can be attributed mainly to high domestic interest rates, poor physical infrastructure, particularly roads, telecommunications and electric power, adverse weather conditions, corruption and poor enforcement of the rule of law, escalating insecurity in the country and increased oil prices.

The financial sector which experienced turbulence in 1998 has stabilised as a result of timely introduction of reforms and improvement of banking supervision. Broad money supply increased by about 2.8 per cent in 1999, compared to 3.3 per cent in 1998. Inflation rates improved from 6.6 per cent in 1998 to 3.5 per cent in 1999, the lowest in the last four years. Interest rates on Treasury Bills which had declined from a high 27 per cent in April 1998, to 8.9 per cent in March 1999, rose again sharply to 20.3 per cent by January 2000. Prudent economic management has brought them down again into the 10 per cent to 12 per cent range. Our exchange rates depreciated by 20 per cent from Kshs62 to the US dollar in December 1998, to Kshs74 to the US dollar in December 1999 and further to over Kshs76 to the US dollar in recent weeks, partly due to the decline in earnings from commodity exports and partly due to net outflows of capital.

The depreciation of the shilling however, has helped our local industries competing with imports and increased earnings over export industries. Overall, our net balance of payments position remained in surplus in 1999, and gross official reserves as at the end of 1999 were enough to cover 3.2 months worth of imports. The most significant factor in the domestic economy has only emerged over the recent weeks as it became evident that the long rains were failing to materialise and Kenya was facing a serious drought situation. This drought will have major impacts on the agricultural sector output, food, water and hydro-electricity supply. The Government is putting together a comprehensive response to this emergency in co-operation with our development partners and NGOs.

Mr. Speaker, Sir, the planning and preparation of this Budget started back in late 1999 and was virtually completed by the time the full extent of the drought became evident. Nevertheless, some measures to respond to this crisis have already been included in this Budget Statement. Already, His Excellency the President has declared the drought situation a national disaster and the suspended duties on imported maize have been removed to facilitate private and donor-sponsored inputs to alleviate the food shortage. Even as I present this Statement, work is under way with the assistance of our development partners to assess the full extent of these emergency, design and appropriate responses and arrange the financing that will be needed for food relief and emergency power supply. Estimates of the ultimate impact on the economy will depend upon the effectiveness of the responses we put in place and on the generosity of the support that we can mobilise from our development partners. The Government will keep the public informed on a regular basis of actions being taken to combat the adverse effects of the drought and electricity shortage.

Mr. Speaker, Sir, faster economic growth requires increased investments and higher productivity. The MTEF for the three-year period, 2000/2001 to 2002/2003, therefore, addresses both the needs to provide consistent macro-economic management and to improve the effectiveness and efficiency with which public resources are used. The macro-economic framework for the MTEF period aims to progressively increase real per capita GDP growth to at least three per cent a year on a sustainable basis. In order to achieve this, we need, one, to create a stable and efficient macro-economic environment which will attract both domestic and foreign investment, and two, to improve public sector performance by concentrating public resources on a focused range of activities which will contribute to a poverty-reducing growth strategy.

Achieving this goal involves, first, that the share of the total Government expenditure relative to the GDP will be reduced from 27.5 per cent in 1998/1999 to 24 per cent in 2002/2003 while ensuring that expenditure is properly targeted at national development objectives, and that those objectives are achieved in an efficient manner. Second, the total Government revenue will be maintained at a maximum of 24 per cent of GDP. Third, domestic debt will be reduced systematically over the MTEF period. Fourth, sound monetary policy will be followed to keep inflation at below five per cent. Fifth, foreign exchange reserve will be increased gradually to provide four months of import cover, and maintain the current account deficit at sustainable level to minimize speculation in the foreign exchange market.

Mr. Speaker, Sir, I expect interest rates to decline and stabilise at lower levels over the next year as a result of the on-going reforms, the resumption of financial assistance by our development partners and increased investor confidence. This will help the economy to recover and grow at higher and sustainable growth rates over the MTEF period. The macro-economic framework has been based on focused real growth of 2.65 per cent in the year 2000/2001, 3.5 per cent in the year 2001/2002 and 5 per cent in the year 2002/2003. It is recognised that the current drought and electricity crises will have a negative impact on the growth rate over the coming year, depending upon the structure and financing of the emergency programme currently being devised. In the medium-term, however, the combination of the fiscal restructuring, enhanced governance and service delivery will still provide a sound platform for a solid economic recovery. While sound macro-economic management is one essential pre-condition for faster economic growth and poverty reduction, it is equally important that the Government sets clear development goals, targets priority activities and improves the efficiency in the use of the scarce national resources. We have, therefore, prepared, following broad consultations with various stakeholders within and outside the Government, an Interim Poverty Reduction Strategy Paper (IPRSP) which incorporates the broad consensus on Kenya's development vision, national objectives, priority policies, programmes and projects. This Paper forms the basis of our negotiations with the Bretton Woods institutions on the new Poverty Reduction and Growth Facility. These two institutions and our other development partners have reviewed the Paper and concurred with our strategy. I wish to thank all those who have made an input into the preparation of Kenya's IPRSP.

Our next aim is to ensure that a final comprehensive Poverty Reduction Strategy Paper (PRSP) is completed and issued by May, 2001. The intervening period will be used for conducting more comprehensive and elaborate consultations down to the grassroots level to ensure that our national programmes have full ownership by all stakeholders. We invite all Kenyans to participate in these consultations. Copies of the IPRSP have been provided to Members of this House. The Paper contains three important annexes. One, contains the governance measures that the Government shall be implementing over the next three years, and the second one, is the implementation matrix that gives a work plan of all the sectoral reforms including the objectives, strategies and activities to be undertaken. The third one is the participation plan that will be adopted to obtain broad-based stakeholders' input into the final PRSP over the next 10 months.

Mr. Speaker, Sir, relations with our development partners have improved tremendously in the last Financial Year. We have continued to hold constructive discussions with the World Bank, the IMF and other development partners over the performance and prospects of economic growth in the country. A joint World Bank and IMF mission visited the country in April and in May to review our economic performance; to assess our progress in preparation of the IPRSP and to negotiate resumption of financial support. Following this visit, we now have strong indications that a new IMF programme under the Poverty Reduction and Growth Facility will be in place by July, 2000, together with the new programme loan from the World Bank. In addition, discussions have already commenced with the World Bank and other donors on modalities of assessing and mobilising assistance to deal with the drought and electrical power shortages.

Mr. Speaker, Sir, corruption has in the past deterred investment and undermined the rule of law. We are making good progress in our fight against corruption. The Kenya Anti-Corruption Authority (KACA) is now fully operational, and a number of cases have been brought before the court for prosecution and many more are currently under investigation. We are taking a multi-disciplinary approach in tackling corruption. This involves: sensitizing the public about the disastrous effects it has on the economy and the need for zero-tolerance for corruption; making the briber just as accountable as the bribed person; and making sanctions so punitive as to discourage potential participants completely.

During the Fiscal Year, 2000/2001, the Government will strengthen the KACA by providing additional resources to enable the recruitment of additional staff and enhancement of systems. The powers of KACA will also be broadened to enable it to investigate and prosecute effectively. During this session of Parliament, this House will debate and enact the Anti-Corruption and Economic Crimes Bill which will be introduced in the House by the Attorney-General. It will also debate a Bill on the code of conduct for all public officers, including a proposal for declaration of assets and liabilities by such officers.

(Applause)

In the Public Sector, we have enhanced transparency by involving the private sector and the civil society in the public sector operations. The following measures have been taken:

(i) The Central Tender Board is now chaired by a reputable representative of the private sector and includes two additional private sector members. Tenders and awards are now widely published and a private-sector-led Procurement Appeals Board for aggrieved parties is in place. The Procurement Reform Project was completed early this year with the assistance of the World Bank and will be implemented effective in July, this year. Procurement regulations will be promulgated for universal application within the Central Government, local authorities, statutory authorities and parastatals. They will provide stringent sanctions for non-compliance on both the officers of the procurement institutions and the suppliers or the contractors.

(ii) A Roads Board has been legislated to oversee the development of the road network in Kenya. Apart from a number of Permanent Secretaries, the Roads Board will have eight members from the private sector organisations. This will no doubt improve transparency and accountability in the sector which has been riddled with corruption.

The Local Authorities Transfer Fund is now being overseen by a Board, comprising private and public sector representatives. This Board reviews the disbursement criteria for allocation of funds to local authorities, as well as the performance of the Fund.

Mr. Speaker, Sir, a taskforce has been established to review the Exchequer and Audit Act and other financial regulations and procedures, with a view to improving timely flow of funds to the district level. A taskforce has also been set up to implement assets register systems in Government. Asset management units will be established in all Ministries to control and manage Government assets. In addition, Ministerial Audit Committees will be established and charged with the mandate of following up and acting upon audit reports and Public Accounts Committee (PAC) recommendations.

I would now like to comment on the sectoral policies and programmes which the Government intends to implement in the first year of the Medium Term Expenditure Framework (MTEF) period. It should be noted that even though the Budget is being presented on the basis of Ministerial portfolio allocations, these comments relate to six sectors which have been adopted under the MTEF approach. The top Budget priorities are expenditures that support economic growth and reduce poverty. The MTEF process and consultations on the final PRSP over the next year will help intensify the focus on these priorities and strengthen the delivery of benefits to the poor.

In this Budget, significant increases have been made in the allocations to the known wage expenditures on primary health and education, through provisions for items such as schools textbooks and equipment and basic drugs. In the 2001/2002 Budget and beyond, to satisfy the need to deliver basic preventive health, primary education and other basic social services to the poor, expenditure allocations to these areas will receive top priority and an increasing share of the Budget.

Mr. Speaker, Sir, public safety is a fundamental concern that, impacts directly on economic growth and poverty. Breakdown of security leads to breakdown of law and order, making it impossible or costly to undertake any meaningful economic activity. Africa, unfortunately contains too many examples of the disastrous economic and social consequences of national and civil insecurity. The rise in insecurity in Kenya has, therefore, become a disturbing development in our society today.

The escalation of crime on our streets and incidents of ethnic tension has eroded investor confidence, reduced economic activities, increased unemployment and the cost of doing business. The capacity of the disciplined forces to combat crime will be enhanced by improving the terms and conditions of service, including appropriate training, housing and upgrading their facilities and equipment, including motor vehicles and higher Budgetary provisions to enhance their mobility and improve their response time to tackling crime.

(Applause)

Hon. Members will notice in the Printed Estimates a substantially higher allocation to this sector, including the national defence and intelligence services. This is a deliberate effort by the Government to provide a secure enabling environment for the effective delivery of public service, and for private sector business activity. Given the current state of deteriorating security, these expenditures on security will assist the effectiveness of social spending and should not be viewed as distracting from our social programme. In the context of developing the final PRSP, however, careful consideration will be given to the relative importance of different security programme elements to supporting the social programmes. In addition, over the medium term, the incremental expenditures funded out of the savings from the retrenchment of excess staff, will be targeted at social and co-poverty programme.

Mr. Speaker, Sir, to promote the impartial administration of justice and the rule of law, the Government will, therefore, take a number of reform actions aimed at increasing transparency in and accessibility to the dispensing of justice and ensuring that the rule of law is upheld. These include accelerating the on-going comprehensive reform process for the legal sector and the implementation of the recommendations of the 1998 Committee on the Administration of Justice. Additional funds have been set aside for restructuring the high court by creating specialist divisions and creation of arbitration and other alternative dispute settlement mechanisms. Penal Code procedures will also be revised for speedier delivery of justice while measures to improve access to legal aid, particularly by the disadvantaged groups, will be put in place. Additional Budgetary allocations have been made for infrastructure for the judiciary, including court rooms, and to the office of the Attorney-General, to enable the strengthening of their capacity to support administration of justice.

Mr. Speaker, Sir, the deteriorating physical infrastructure in the country has been a major factor leading to the decline in investment and economic activities. The restoration and development of physical infrastructure will constitute a primary objective. The Government will implement the roads strategic plan and give priority to the routine maintenance of the main trunk roads, as well as improvements in feeder roads that have not been bituminsied

In this Fiscal Year, Kshs7.8 billion has been raised through the Fuel Levy and was used to rehabilitate roads, both under the central and local Governments. However, compared to the massive damage caused by *El Nino* rains, estimated at Kshs48 billion, the rehabilitation process has not proceeded with the necessary speed. The Government recognises that factors contributing to the poor road network include corruption in awarding of contracts, construction of poor quality roads and lack of routine maintenance. The Government is determined to root out these malpractices and stern measures will be taken against corrupt contractors and Government officials who compromise on the quality and standard of work. Already, we have blacklisted a number of contractors who have done shoddy jobs. Measures are being undertaken to restore transparency, professionalism and accountability in undertaking road works by enforcing professional standards and eliminating corruption in procurement of contractor services.

Use of economic-project appraisal methods will be strictly enforced, while auditing and accounting for roads maintenance funds will be improved. Blacklisting of defaulters and non-performing contractors will also be stepped up. Steps have been taken to limit the number of projects a single contractor can handle at any given time.

(Applause)

The provisions of the Kenya Roads Act which was enacted by Parliament in February, 2000, will be operationalised to enable the Board co-ordinate and oversee the management of the entire national road network from July, 2000. Forty per cent of the funds under the Roads Board will go to the districts and will be administered by District Road Committees chaired by elected leaders. A positive impact of these measures should be through improved agricultural activity as rural access roads are rehabilitated.

The port of Mombasa is important not only as the main gateway for goods in this country, but also as a transit point for goods destined to our neighbouring countries. The port, however, has suffered from inefficiencies caused by bad management, old equipments and inadequate port facilities. I wish to report to this House that there has been a marked improvement in services, especially at the container terminal since the new management took over. New equipment has now been installed and rehabilitation of the container terminal has been tendered for. The port has for the first time in many years made a profit.

During the next year, the on-going activities of improving availability and reliability of container handling equipment through refurbishment and replenishment of equipment and tug masters will be hastened. In order to eliminate corruption and theft of goods and services, and to facilitate the flow of goods through the port, action will be taken to rationalise administrative procedures and remove bottlenecks. Plans for privatisation of port operations through awarding concessions for the container terminal and other non-core services will be accelerated.

Railways

Mr. Speaker, Sir, the use of out-dated and inefficient locomotives and an old railway line has resulted in high maintenance costs, unprofitable operations and poor service delivery by the Kenya Railways. The Government will address this by providing additional funding for improving Kenya Railway's telecommunications system, increasing wagon availability, rehabilitating locomotives and re-laying 60 kilometres of the Nakuru-Kisumu branch line in the financial year. This will increase the capacity of the Railways to haul more traffic and capture the lucrative traffic destined for North Western Tanzania, Uganda and Rwanda.

Telecommunications

Efficient telecommunication is an essential prerequisite to increased trade and economic activities, and to international competitiveness. During the last fiscal year, two cellular telephone licences were issued opening up the area to competition, which will bring down prices, improve the services and bring more users within the subscriber base. In the new financial year, Telkom will reduce international tariffs by 18 per cent. This will bring down the cost of doing business, and enhance he attractiveness of Kenya as an investment destination. Plans are also underway to provide additional payphones in all urban areas and rural centres as part of the poverty reduction strategy. Within the next financial year, Telkom will upgrade the existing telecommunications infrastructure. Digital equipment has already been secured for the Industrial Area, Parklands and Embakasi areas under this modernisation programme. The sale of a 49 per cent share of Telkom to a strategic partner will be effected in order to upgrade its access to technology and capital.

Energy

Normally, hydro-power stations supply roughly 77 per cent of the 750 megawatts (MW) of peak power and 70 per cent of the energy demand. The balance of 30 per cent is supplied by geothermal, thermal and diesel plants and imports from Uganda. The power situation has been severely affected by failure of rains in the hydro catchment areas in the latter parts of last year and the first half of this year that has depleted the reservoirs at Masinga, Kiambere and Turkwell. This situation initially led to power rationing for six hours a day in order to load shed about 100 megawatts of power. Power rationing has since been intensified to 12 hours a day due to the extremely low water levels in the dams. The effect of power shortages in the economy have been serious with economic activities slowing down and industries operating below their installed capacities. Urgent measures are therefore necessary to reverse this sad state of affairs.

Mr. Speaker, Sir, emergency measures are being put in place to expand power supply by 180 megawatts to alleviate the rationing. First, I will be announcing tax measures to encourage private sector participation in power generation and to reduce the costs that will arise from the additional use of oil-based electrical power generation. The Ministry of Energy, Kenya Power and Lighting (KPLC) and Kenya Revenue Authority (KRA) will be working with companies and institutions with generators over 100 KVA to make arrangements for them to receive duty rebates on fuel usage and compensation payments for the extra costs of supplying themselves in place of using grid power. This will save some 20 megawatts of grid power.

Secondly, KENGEN and KPLC will work to re-locate idle standby generators owned by the Government or parastatals to critical institutions such as universities. KPLC is also investigating the potential for sugar factories to supply their excess power to the grid. Third, KENGEN will rehabilitate a moth balled boiler and turbine at Kipevu to provide an additional 30 megawatts by September 2000. Fourth, arrangements have been made with Uganda to import increased amounts of power from July onwards as new power plants come on stream in Uganda. Fifth, the Government is already working with our development partners on the modalities and financing to bring in emergency power generators over the next three months. To supply the remaining 130 megawatts, a combination of power generation sets rented from international suppliers for 6 to 12 months, an incremental generating capacity installed on an emergency basis by KenGen and the existing independent power producers are being investigated.

Mr. Speaker, Sir, the Government will also take measures to ensure capacity is enhanced over the medium-term to stabilise the power supply. KenGen has drawn up a detailed energy balanced plan which includes conservation of water in the reservoirs and commissioning of Kipevu power plant, Gitaru Hydro Power Station. Medium-term generation programmes include progressive commissioning of several power plants up to the year 2004. The Government with support from development partners, will also embark on a project to reduce power losses. Possibilities of sourcing additional power from Uganda and the SADC region are also being actively explored. We expect that beyond July 2001, the power situation in the country will be healthy and there will be adequate reserve capacity to meet peak demands and energy requirement even under drought conditions.

Mr. Speaker, Sir, KPLC will through the Rural Electrification Programme, invest over Kshs1 billion during the next financial year for extension of transmission lines in rural areas. Market centres, public facilities and social amenities will be targeted with the aim of supporting business creation and income generation.

Agriculture and Rural Development

Mr. Speaker, Sir, the agricultural sector has suffered greatly due to persistent drought and high dependence on rain-fed agriculture and high costs of inputs. The decrease in agricultural productivity has impacted negatively on economic growth rates and led to increased poverty in the rural areas. The growth in the sector slowed down to 1.2 per cent in 1999 compared to 1.5 per cent in 1998, mainly due to poor prices offered for agricultural commodities, inadequate rainfall in major food growing areas and increased prices of farm inputs. In order to arrest the decline in productivity and to realise the full potential of the agricultural sector, the Government will undertake a number of measures: The promotion of food security through establishing a strategic reserve to protect the most needy will be a key policy intervention in the medium-term. Given current food shortages, Kshs1.5 billion has been allocated to food relief. The promotion of income and employment generating crops and the development of ASAL areas will also be key priorities. The Government has already taken action to begin restructuring institutional arrangements for marketing coffee and tea, which together account for about a third of exports. The tea sector is also in the process of being liberalised to allow individual tea factories to operate independently. The Government has also held wide consultations among stakeholders on a sugar sector reform policy. A Sugar Bill will be presented to Parliament in the course of the year. Other measures will include: provision of water, ensuring that early warning system is functional in drought-prone areas, the improvement of inspection and quality control of farm inputs through the revision of legislation, control of crop and livestock pests and diseases and rationalisation of funding of research and technology development and transfer to farmers. Increased funding has also been provided for boreholes in rural areas. Emphasis will be on removing silt from and rehabilitating existing boreholes in readiness for the short rains.

The Government will also address other structural and physical constraints of the sector which have decreased yields and reduced the areas under cultivation. These include the dilapidated infrastructure and poor management of major agricultural marketing organisations. We expect that these measures will lead to sustained growth in agricultural production of about 4 to 6 per cent in the medium term which will make a meaningful impact on overall economic growth.

4. Human Resource Development

Mr. Speaker, Sir, the Government will in the next financial year focus resources on improving the provision of and access to basic social services, particularly basic education and primary health care. In all of these activities, the Government will seek a closer working relationship with development NGOs, religious organisations and other private service providers to increase the range and quality of provision.

Education

Mr. Speaker, Sir, the fall in enrolment rates experienced at all levels of education is attributed to the rising costs that are borne by parents at this time of increasing poverty. The Government remains committed to the goal of Universal Primary Education (UPE) by the year 2015 and will pursue this target by lowering costs to parents. Specific measures include:

1. Collaborating with development partners and NGOs to significantly increase funding for the purchase of textbooks.

2. Revising the curriculum to ensure quality and relevance of subjects.

3. Increasing funds for the purchase of essential equipment in schools;

4. Improving and expanding the school feeding programme.

In order to bring more children into the school system, the bursary programme will be expanded while at the tertiary level, the Higher Education Loans Board will be facilitated to provide more loans efficiently and effectively. At the same time, scholarships will be provided for outstanding students from poor households targeted to specific degree programmes which are of high demand by the economy.

Mr. Speaker, Sir, the priority for health care will be to increase the availability of affordable quality health services to all Kenyans. More resources will be given to district and rural health facilities, and allocations for communicable and vector borne diseases and family planning and maternal and child care have been more than doubled. The waiver system will be enforced and charges for certain diseases dropped in Government hospitals. We will also develop a transparent and accountable drug procurement system, to ensure that drugs are available in hospitals at reasonable cost. The emphasis in the next financial year will be on shifting greater resources from curative to primary and preventive health care and rural health services.

Mr. Speaker, Sir, HIV\AIDS has had a devastating effect in Kenya, with about 2.2 million people currently infected; including 106,000 children under the age of five. On average, close to 500 people die every day because of AIDS related infections. In order to deal with this disease effectively, the Government has declared AIDS a national disaster and established the National AIDS Control Council to co-ordinate a multi-sectoral response to deal with all aspects of the epidemic. Adequate funding will be provided for the activities of the Council, while AIDs control units will be established in all Ministries. Our objectives will be to reduce the HIV prevalence rate, increase access to care and support to people infected and affected by the epidemic, and strengthen the capacity at national, district and community level, to respond to the epidemic.

Mr. Speaker, Sir, it is now recognised that the mandate structure and operation of the public service needs to be re-shaped in a manner that will raise productivity, so that it can more effectively, facilitate private sector activities. Reforms in this area initiated in 1993 produced little impact on the levels of efficiency and productivity in the public service. The Government, therefore, has approved a new strategic plan for public sector reforms, which is more comprehensive and integrated. The programme has four elements namely:-

(i) The Public Management Programme.

(ii) Legal Sector and Judicial Reforms.

(iii) Enhanced Integrity and Accountability.

(iv) Interaction with Civil Society.

Mr. Speaker, Sir, the pubic service management reform component covers the entire public service. The Ministerial and Departmental rationalisation exercise has been completed and restructuring and retrenchment can now be implemented. Ministries and Departments have identified their optimal staffing levels for carrying out their core functions. The extra staff are targeted for retrenchment over the next two years. During this financial year, a total of 25,783 civil servants, 195 Kenya Revenue Authority staff, 4,883 University staff, 1,500 Kenya Agricultural Research Institute staff and 300 Catering Training Levy Trustee staff will be retrenched at a cost of Kshs7.8 billion, generating on-going annual wage savings of Kshs3 billion. The average termination package for each retrenched public servant is expected to be about Kshs240,000. But substantial savings in salaries and associated personnel costs mean that this initiative should achieve pay-back within three years. It is planned that 25,783 civil servants due for retrenchment during the year 2000 and 2001 will proceed on leave between July and August. Their retirement package will be paid to them in October to enable them to settle into their retirement. The Government is grateful to several donor agencies for their participation in the design and financing of the programme.

Mr. Speaker, Sir, the Kipkulei Commission on harmonisation of terms and conditions of service in the pubic service has presented its Report to the Government. Recommendations for the improvement of pay and benefits will be implemented. Kshs6.8 billion has been set aside this financial year to implement the first phase of proposals. Further adjustments will be made over the following years. Further adequate funding has also been set aside for capacity building and training in order to re-equip the public service with skills to fulfil its new mandate. In this way, the culture of efficient service delivery, integrity and professionalism should be restored in the public sector.

Mr. Speaker, Sir, the Parastatal Reform Programme, which has been on-going since 1992 will be re-defined this financial year. Its scope will be widened and the process made more transparent, open and competitive. The immediate focus will be to divest the large infrastructure and service enterprises, specifically, Kenya Railways, Kenya Ports Authority and Kenya Pipeline. During this financial year, the strategy for the privatisation of the Kenya Railways, through a unitary concession, to a private operator of the rail infrastructure, including passenger and cargo operations, will be implemented, and, at least, two concessions will be let for the operation of the container facilities at Mombasa. Necessary regulatory agencies will be established in both cases. The strategic partner will be sought to take over the running of the Kenya Pipeline Company.

In the financial sector, the Government is committed to selling its shares in the Kenya Commercial Bank (KCB) during the course of the next financial year. Restructuring the KCB in preparation for further privatisation has already begun with the appointment of a new management team. The restructuring of the National Bank of Kenya (NBK), including intensification of efforts to collect all restructure outstanding debts will be accelerated in preparation for future privatisation. Plans to privatise the Kenya Reinsurance Company are already at an advanced stage.

Mr. Speaker, Sir, successful implementation of poverty reduction measures, through the better delivery of public services will depend highly on strengthening the capacity of Local Governments, to deliver key local services in a more responsive manner to local demands. Over the medium term, this will require the revolution of greater responsibility for local services, to more autonomous Local Authorities. To achieve this, the Government will develop a decentralisation strategy and reform the Local Government Act accordingly. At the same time, it will continue the efforts to strengthen the governance and service delivery capacities of Local Authorities. Two key mechanisms are being used for local capacity development; namely, the Local Authority Transfer Fund (LATF) and the Financial Control Management Boards. The LATF aims simultaneously to increase the resource base of Local Authorities and also to enhance their governance capacities, through a number of conditions imposed on their financial management performance. The LATF became operational from January this financial year, and two per cent of the Income Tax collections have been transferred to Local Authorities. During 2000/2001 the LATF will transfer 5 per cent of Income Tax collections. This will include a transitional amount to compensate for the full phase out of the Local Authority Service Charge effective 1st January, 2001, which was announced in the Budget last year. The LATF Secretariat is being strengthened with specific funds set aside to ensure that all Local Authorities are well informed of the LATF requirements. That, on-sight monitoring is conducted and programme performance is reported.

Mr. Speaker, Sir, the Nairobi City Council is in a state of chronic financial distress. It has been spending beyond its means, and it has debt payments arrears that exceed its annual income, before even taking into account its large future debt repayment obligations.

Accordingly, following the findings of an Extraordinary investigation, His Excellency the President acted expeditiously to appoint an Interim Oversight Board to assume control of the Nairobi City Council finances, under the direction of an Inter-Ministerial Committee. Funding has now been raised from development partners such that, this Board will start its work to systematically reform the City Council finances; starting with a full external audit. In addition, the Government will bring to Parliament legislations to underpin the future operations of the boards to impose financial controls on all authorities suffering from chronic financial distress and at the same time, to assist them restructure their operations to enhance their revenues, rationalise their budgets and expenditures and improve the efficiency of their service delivery. Such boards will provide an objective private sector-driven approach and employ professional staff to reform the financial management of the larger local authorities.

Mr. Speaker, Sir, productivity in our manufacturing industry has suffered substantial decline as a result of increased costs of doing business. Poor infrastructure, particularly, poor roads, erratic and unpredictably electric power supply, inefficient seaports and railways, high interest rates and high input cost, have all contributed towards increased costs of production.

In addition, with further reductions in the COMESA tariff, the threat of greater competition from other COMESA countries has increased. Our strategy of reviving the manufacturing sector will, therefore, entail addressing the factors which act as constraints and contribute towards high cost of production. The speedy rehabilitation of all infrastructures; improvement in security and improvement in the delivery of public services, will be the cornerstone of this strategy. In order to rejuvenate local industries, the Government will also significantly reduce tariff rates on a large of raw materials not produced in the country, and remove a number of minor import inspection fees, as a way of reducing costs of production and levelling the playing field with other COMESA countries.

(Applause)

Mr. Speaker, Sir, this is a very significant step, and I call upon industries to take full advantage of the reduction of tariff rates to expand their production. The COMESA preferential rates will now be on a reciprocal basis.

The *Jua Kali* Sector has emerged as an important industry for the creation of employment and poverty alleviation. Informal sector employment, as a share of total employment, as expanded from 53 per cent, in 1967, to 64 per cent in 1994. However, despite this important contribution, micro-enterprises continue to suffer from weak marketing, inadequate property rights, excessive regulations, both formally and informally through corrupt officials, poor access to economic services and poor access to formal bank credit.

Mr. Speaker, Sir, in recognition of the potential of the micro-enterprises in creating jobs and alleviating poverty, the Government will develop an appropriate policy and legal framework to promote a system of viable and sustainable micro-financing in the country. The Central Bank of Kenya is already assisting the newly-formed Association of Micro-Finance Institutions in streamlining legal and regulatory framework and accounting standards. Within the course of this financial year, the Bank will establish a fully fledged micro-finance unit to regulate micro-finance organisations.

Mr. Speaker, Sir, tourism remains an important source of foreign exchange. In 1999, the sector showed signs of recovery. The number of visitors went up 8 per cent, to stand at Kshs970,000 compared with a decline of 10 per cent in 1998. Tourism earnings also increased by 22 per cent, to stand at Kshs21 billion. The objective in the year 2000/2001, will be to increase our share of the world tourism market, by aggressively marketing Kenya as an attractive and safe destination. This will be done through joint-public-private-sector initiative, in areas of security, infrastructure and marketing.

Mr. Speaker, Sir, experience has shown that, countries which do not integrate themselves into the regional and global economy do not reap the benefits of improved resource allocations and wider markets. Our commitment to regional integration is borne out of this realisation, and Kenya has continued to play a pivotal role in COMESA and the East African Co-operation. It was particularly gratifying to witness the signing of the Treaty establishing the East African Co-operation in Arusha, by the Heads of States of the three East African countries. The Treaty ushers in a new commitment to a common in East Africa, guaranteeing the free movement of goods, capital and people, as well as the removal of all tariffs and non-tariff barriers.

We also recognise that the success of both COMESA and East African Co-operation will depend on the commitment and contribution of every member in the organisation. For this reason, we endeavour to faithfully implement the programmes of the organisation and continue to urge other member countries to abide by the timetable agreed upon for integration. By October this year, we will be going to zero-tariffs for inter-regional trade, according to the COMESA programme.

Mr. Speaker, Sir, a healthy and vibrant financial sector is key to the achievement of higher economic growth rates. Unfortunately, our banking sector is still characterised by a large number of small unstable banks and a huge portfolio of non-performing advances. The latter has been increasing over the years and currently stands at 36 per cent of the total gross advances. Consequently, a number of banks have been placed under statutory management and a range of regulatory measures have been implemented during this year. It is encouraging to note that two banks under statutory management have been successfully restructured and have re-opened during the current year.

Further measures will be implemented in the next Financial Year to address the problem of non-performing advances and to enhance financial stability. A legislative framework will be introduced into the Banking Act for the establishment of credit reference bureaus, confidentiality requirements governing the relationship between banks and their customers will be safeguarded.

Amendments will be made to the Banking Act to allow the Central Bank of Kenya to share confidential banking information with other regulatory authorities or other authorities deemed fit by the Central Bank. Amendments to the Building Societies Act, will be brought to Parliament to bring building societies under the regulatory control of the Central Bank. Legislation will be introduced to criminalise cheque-kiting and bouncing. Banks will also be encouraged to modernise their information technology and to pull services, such as, Automated Teller Machines to cut down cost. The Commercial Court's capacity to assist in the collection of loans arrears will be expanded.

Following the amendment of the Banking Act, in 1999, capital requirements banks were progressively increased. To meet the higher capital requirements, institutions are expected to generate increased profits or inject fresh capital, while small banks are encouraged to merge. To facilitate a smooth merger, appropriate, legal and other enabling procedures will be put in place to remove legal impediments in areas like the assignment of assets and liabilities.

The Government will also accelerate its divesture from the financial sector, during the three year period by selling its shareholding in the Kenya Commercial Bank, the National Bank of Kenya, the Development Bank of Kenya, Housing Finance Company of Kenya(HFCK), Consolidated Bank and Industrial Development Bank (IDB).

A number of amendments to the Insurance Act, will be presented to Parliament during the year. Among the more important, will be proposals for the introduction of structured compensation for motor vehicle related accidents to reduce disputes and prevent the escalating cost that are damaging both the insurance and the passenger transport sectors.

Mr. Speaker, Sir, the regulations to the Retirement Benefit Act, have received considerable comments from stakeholders and are going to be gazetted early in the new Financial Year. Thereafter, the Retirement Benefits rules, under the Income Tax Act, will be amended to remove any inconsistencies with the standards required under the Retirement Benefit Act, for the pension scheme. Kenya needs to attract foreign capital to support privatisation and industrial development.

Following a review of the policy governing foreign participation in the securities market, I am proposing to amend the Foreign Investor Regulations under the Capital Markets Act, to introduce a new policy that will guarantee a minimum shareholding reserve for domestic investors and introduce the concept of beneficial interest in domestic companies to gain sharper identification of domestic investors. Strategic sectors will have a higher minimum reserve for domestic participation.

Mr. Speaker, Sir, significant advances have been achieved in improving the regulation of the financial sector. However, those developments have not been co-ordinated, or comprehensive across all financial market subsectors, leaving gaps and inconsistencies in the regulations. Accordingly, I propose to appoint a task force to study and advice on the development of consolidated financial services regulatory framework.

Mr. Speaker, Sir, the restoration of monetary discipline and maintaining price stability remains the primary objective of monetary policy. The further tightening of monetary conditions in the last financial year saw a general reduction in the growth of money supply. The Government will continue to pursue a tight monetary policy with the aim of ensuring that expansion of money remains consistent with the growth of economic activities. The intervention in the market will continue to be via open market operations. The Government is committed to live within its means and employ prudent fiscal policy to support the monetary policy objectives, particularly the maintenance of inflation below 5 per cent.

Mr. Speaker, Sir, the high interest rates have been a disincentive to investment and frustrated efforts to achieve higher economic growth rates. More recently, partly due to tighter expenditure management and the receipt of Kshs5.3 billion from the sale of two cellular phone licences, the proceeds of which have been applied to domestic debt reduction; interest rates on Treasury Bills have fallen to the 10 to 12 per cent range. However, commercial bank lending rates have unfortunately remained high.

Hon. Members: Shame! Shame!

The Minister for Finance (Mr. Okemo): These high lending rates will not trigger the increased private sector borrowing and investment required to spur economic growth. The Government is determined and would play its part to achieve sustained reductions in the stock of domestic debts to bring it down by 6 per cent to 15 per cent of GDP over the next three years. This should lead to consistent lower interest rates on Treasury Bills. In addition, foreign exchange reserves would be gradually increased and the Current Account deficit maintained at sustainable levels, to discourage speculative attacks on the shilling.

The overall investor confidence in economy engendered by the commitment of the Government to a realistic and constructive reform programme with strong backing from our development partners, will also provide the stimulus for a decline in market interest rates. This confidence factor will also allow the Government to lengthen the maturities of its domestic debt portfolio, as the market becomes more willing to buy Treasury bonds.

Mr. Speaker, Sir, in this Financial Year, we aim to limit domestic borrowing by targeting a balanced budget through expenditure reduction measures and improved revenue collection. However, Government revenue fail below budget by Kshs11.2 billion. The majority of this came from a shortfall in income taxes on business activity by Kshs6.3 billion as company profits declined, particularly in the financial sector. Although, we have not achieved a balanced budget, our performance at the end of the Financial Year shows improvement in the management of the Budget. The Budget deficit this year on a commitment basis before grants, is expected to be lower than in the 1998/99 Financial Year.

Mr. Speaker, Sir, under the IMF and related programmes, significant concessional borrowing is being negotiated. This will require external borrowing limits of the Government to be raised. Accordingly, I will be presenting to Parliament, amendments to the External Loans and Credits Act, to raise the external borrowing limit to accommodate the expected new concessional borrowing and to adjust the limit for past devaluations in the Kenya shilling.

Mr. Speaker, Sir, the declining economic growth rate over the past three years has put enormous stress on our revenue collection machinery to meet revenue targets. This makes our task for the coming year doubly difficult. On the one hand, the Government needs the resources to spend on infrastructure development and poverty reduction programmes, and to bring down the debt burden, while on the other hand, the private sector needs incentives to invest and match international competition. The poor need the burden of tax shifted more, to those more capable of bearing it. Therefore, to make up the significant revenue shortfalls that have arisen out of the decline in economic activity and to finance investment and business incentives, two strategies will be followed.

First, Kenya Revenue Authority (KRA) as part of its medium corporate strategy, will be focusing increased efforts on expanding the tax base, enhancing its audit capacity, tightening the policies and procedures for tax exemptions and accelerating collection of tax arrears. This will not only bring in more revenue, but it will shift more, of the tax burden onto those that have been evading tax in the past and thereby enhance equity. Secondly, proposals will be made that will increase the revenue collected out of consumption, so that we can encourage investment that will provide the growth and job creation that this economy urgently needs.

Mr. Speaker, Sir, in the tax proposals laid before the House today, significant reductions are made in customs duties on raw materials and other inputs into manufacturing. Under the Income Tax proposals, personal reliefs and brackets are expanded to ensure that the poor are left out of the tax net.

(Applause)

Measures are also introduced in the Income Tax and VAT to encourage investment. In the area of VAT, proposals are included to widen the tax base and adjust the tax rates to rationalise them with those of the other East African Community member states.

Expenditure policies are targeted towards sectors that will contribute to growth in the economy and thereby lead to poverty reduction. In the short-run, key interventions will be in the following areas:- Security and governance, human resource development, specifically primary health and basic education; upgrading and rehabilitating physical infrastructure, especially roads, water and sanitation. The Government has allocated Kshs20.3 billion for core poverty programmes in an endeavour to improve the welfare of Kenyans. These programmes which are mainly in the social sectors of education, health, water and sanitation will be ring-fenced, so that they will not be subject to budget cuts, should this become necessary.

A listing of the core poverty programmes is provided as an annex to this Speech.

To enhance transparency in allocation of resources, the Ministries of Roads and Public Works, Environment and Natural Resources and Health, are now preparing district annexes which will contain details of provisions made to districts in respect of their programmes. The annexes will be presented to this House when debate on Estimates begin.

Mr. Speaker, Sir, to restore the credibility of the Budget system, the cash management system introduced a few years ago will be enhanced and the Treasury will endeavour to meet the Exchequer issues to Ministries in a predictable manner, so that planned programmes are implemented on schedule. However, Ministries will only be provided with resources if they adhere to set budgets and make timely and accurate expenditure returns on all commitments and payments. In order to eliminate the menace of pending bills, beginning the new Financial Year, no Accounting Officer will be allowed to enter into commitments for any goods or services over and above the set expenditure ceiling for the quota. The Treasury shall also strengthen its capacity to monitor the budget on a continuous basis, to ensure that the overall ceilings for a Ministry or department as well as the sector ceilings are adhered to in order not to distort the priority allocations.

Mr. Speaker, Sir, let me now briefly review the financial out-turn for the 1999/2000 Financial Year. Despite a weak economy below target revenue collection and high external debts, armotisation requirements, we have managed to keep the budget deficit on a commitment basis and before grants to 0.6 per cent of the GDP, or approximately Kshs4.5 billion, down from 0.7 per cent of the GDP or Kshs5.2 billion in the 1998/99 Financial Year. Tight expenditure controls have helped to restrain the domestic borrowing which was largely driven by the need to finance the net repayments of foreign loans of Kshs14.5 billion. This net foreign loan repayments along with the current year deficit, resulted in Government having to borrow an additional Kshs10.3 billion from the domestic market, excluding the Kshs5.1 billion of special bonds issued to clear pending bills.

Mr. Speaker, Sir, originally, ordinary revenues were estimated at Kshs174.6 billion plus Appropriations-In-Aid of Kshs28.9 billion, making a total of Kshs203.5 billion.

With lower than expected economic growth, however, ordinary revenues are now estimated to be 9.4 per cent below target. I now expect a total of about Kshs163.5 billion in ordinary revenues and Kshs22.9 billion in appropriations-in-aid (A-in-A). As indicated in the Supplementary Estimates that were recently approved by this House, expenditures for the year had to be adjusted downwards to off-set shortfalls in revenue. As a result, total expenditures for the year have decreased by Kshs9.7 billion. Initially, growth re-current expenditures for the year were projected at Kshs163.1 billion, including A-in-A of Kshs15 billion and a Consolidated Fund Services (CFS) amount of Kshs36.5 billion. Total growth development expenditures were projected at Kshs54.1 billion of which Kshs38.6 billion was A-in-A. The Supplementary Appropriation Bill adjusted expenditure downwards as follow: The total growth re-current expenditures declined by Kshs2.1 billion, while development expenditures declined from Kshs54.1 billion to Kshs42.4 billion. However, CFS payments increased from Kshs36.5 billion to Kshs38.4 billion, reflecting an additional Kshs1.9 billion over the printed Estimates.

Mr. Speaker, Sir, I will now go to the focus for the 2000/2001 Financial Year. As emphasised above, this Budget has been prepared within the context of the Medium-Term Expenditure Framework (MTEF), based on estimates developed over the last six months. In recent weeks, the extent of the drought and hydro-electricity shortage has become clearer. While policies have already been developed to mitigate the adverse effects of this crisis, many of which are contained within the Budget Statement, and donor assistance is being sought to alleviate its adverse effects, the full economic impact of this crisis is currently being assessed, and its effects on growth and Government revenues estimated. There is no doubt that it will reduce Government revenues, and will require some expenditure re-allocations and cut-backs. The full extent of these expenditure adjustments will be announced as soon as estimates are completed.

The total revenue target for the 2000/2001 Fiscal Year is Kshs203.3 billion, or nearly 24 per cent of Domestic Growth Product (DGP). This is comprised of Kshs182 billion in ordinary revenues and Ksh20.9. in A-in-A. As hon. Members have already noted from their copies of the Printed Estimates, growth re-current expenditures for the 2000/2001 Financial Year will be Kshs190.3 billion. This includes Kshs16.8 billion financed by A-in-A. The CFS payments will take up about Kshs36.9 billion, leaving Kshs151.4 billion for discretionary expenditures. The CFS payments include Kshs21.5 billion for domestic interest, Kshs9.1 billion for foreign interest, Kshs6.3 billion for pensions, salaries and the rest for Constitutional Officers and contributions to international organisations.

Mr. Speaker, Sir, growth development expenditures for the 2000/2001 Financial Year will be Kshs38.4 billion. This will include Kshs23.1 billion financed by A-in-A, including direct project financing of Kshs8 billion in loans and Kshs10.9 billion in grants commitment, and Kshs4.2 billion realised as A-in-A from domestic sources. I have received commitment of project grants of Kshs12.5 billion from both multilateral and bilateral development partners to finance development expenditures. In addition, Kshs11.4 billion has been committed in project loans. As hon. Members are aware, negotiations with the Breton Woods institutions are at an advanced stage with conclusion expected in July, 2000. Based on this new IMF programme, in the 2000/2001 Financial Year, I expect to receive Kshs7.5 billion in programme grants and Kshs14.4 billion in programme loans. Under the programme, the fiscal deficit on a commitment basis and excluding grants will be held to Kshs14.8 billion, or 1.8 per cent of GDP. Within the additional programme loans, and with the planned re-scheduling of Kshs12.6 billion in external debt, I now expect foreign financing to provide a net inflow of Kshs500 million to help reduce the domestic debt. In addition, expected capital receipts from the privatisation of about Kshs10 billion will be used to reduce domestic debts. After allowing for cash payments of pending bills and foreign interest arrears, and excluding the issuance of Kshs3.3 billion in special bonds to pay off the remaining pending bills, I expect to be able to reduce domestic debt by Kshs9.1 billion, or 1.1 per cent of GDP.

Mr. Speaker, Sir, as already mentioned, I plan to raise Kshs203.3 billion in total revenues. Based on an economic growth rate of 2.65 per cent and current taxation structures, revenues will fall short of the total revenue target by Kshs8.6 billion. The rest of my Speech outlines the tax measures I intend to take to raise the revenue to bridge this gap. As already mentioned, I am faced with the difficult task of making up revenue shortfalls in a slow-growth economy and, at the same time, finance poverty reduction programmes and provide growth enhancing investment incentives. To the maximum extent possible, revenue enhancement will be achieved through base broadening and enforcement measures. But, it will also require tax rate increases that will not jeopardise investment or put an unfair burden on the poor. Much of the burden of enhancing revenue collection will be sought from the Kenya Revenue Authority (KRA).

The KRA has established a medium-term corporate strategy that not only seeks greater effectiveness and efficiency in tax administration, but will also make the KRA more supportive of taxpayer compliance through improved taxpayer education and information. In the medium-term, the KRA will become he collector of all Government revenues. Therefore, in this Budget, I will continue the process of shifting revenue administration responsibilities to the KRA to ensure that its expertise and low cost of collection will lead to enhanced revenue receipts. Customs and Excise will be a major target area for strengthening the administrative capacity of the KRA. Part of this capacity development will involve Customs and Excise Department assuming greater responsibility for import valuation and inspection. Over the course of the 2000/2001 Financial Year, the Government will tender for new pre-shipment inspection and import verification contracts that will reduce the role of these agencies through more selective and cost-effective targeting of their services.

(Applause)

Mr. Speaker, Sir, in keeping with tradition, I now request that the remainder of my Speech be regarded as a notice of a Motion to be moved before the Committee of Ways and Means. I will start with the customs measures that have no direct revenue implications. First, to further support the implementation of the General Agreement on Trade and Tariffs (GATT?) rules for customs valuation legislated last year, I propose to establish a tribunal for the resolution of appeals concerning customs values. This will provide a more transparent dispute resolution mechanism. Second, to assist the motor vehicle assemblers, recognising that world-wide sourcing of parts has now become standard practice, provisions will be introduced to allow completely knocked-down kits to be sourced from multiple countries. In addition, it is proposed that longer periods for holding assembled motor vehicles in bonds will be allowed for approved assemblers.

Third, with the expanded use of inland dry ports and transit sheds, proposals are being made to mandate operators to have proper goods handling facilities and bear the costs of disposal of condemned goods under their control. In addition, to cater for the time taken to transport goods to inland dry ports, normal 21 days allowed for entry of goods shall commence from the date of arrival of the goods at the port. Fourth, to discourage the diversion of duty exempt manufactured goods designated for export, particularly vegetable oil products, it is proposed to increase the fines on this offence significantly up to the higher level of Kshs500,000, or three times the value of the goods. In addition, to deter the sale of adulterated refined petroleum products, a new fine of up to Kshs5 million and forfeiture of the goods is proposed. To minimise the red-tape, the responsibility of the Kenya Revenue Authority to approve charitable donations for exemptions is increased by raising their duty exemption limits from Kshs100,000 to Kshs500,000. It is proposed to raise the general fine for offenses under the customs regulation from a maximum of Kshs200,00 to Kshs500,000. To reduce bureaucracy it is further proposed to raise the amount of warehouse rent, interests and penalties at customs commissioner along with interest and penalties that the commissioners of VAT and income tax can waive for deserving cases without reference to the Minister for Finance from Kshs100,000 to Kshs500,000. These commissioners, however, will have to provide quarterly reports of these waivers. To assist the tea industry in verifying tea exports for purposes of the EPPO Programme, tea sold at the Mombasa auction shall be deemed to have been exported.

I now turn to customs measures with direct to revenue consequences. First, the Government recognises that the manufacturing sector has been going through difficult times as their competitive position has been eroded by high domestic costs arising from high interest rates, poor infrastructure particularly transport and energy supply problems. Low world commodity prices in recent years have also lowered product prices. The opening up of trade with COMESA is also posing competitive problems. To assist manufacturers weather this storm and level the playing field with countries in the region, I propose to lower the duty rates on key raw materials and inputs into the manufacturing sector. All items in the 10 per cent tariff ban along with selected inputs in the 15 per cent ban will be lowered to 5 per cent. The range of key primary raw materials currently in the 10 per cent and five per cent tariff bans will be lowered to 2.5 per cent. These raw materials include crude vegetable oils, rubber, basic metals and minerals.

Mr. Speaker, Sir, over the past three years the Asian and South American currency crisis led to the use of suspended duties to provide temporary relief against falling international prices. These led to a complex web of tariff rates which now need to be unravelled into a simpler and more transparent structure. Accordingly, all suspended rates will be combined with regular tariff rates except for the suspended duty on oil products. At the same time the top duty rate will be cut at 40 per cent excluding the rates applicable to the major agricultural commodities. This will reduce the number of tariff bans from 13 to nine excluding tariffs on sugar. Within this structure the duty rates on a limited range of products including footwear, biscuits and soaps will be raised. At the same time the duty rates on a range of paper products not produced in Kenya has been lowered to assist the printing and converting sector.

While high duty rates have afforded manufacturers some added protection in recent years and sustained businesses through difficult times, in the long run high duty rates lead to high domestic costs making Kenyan businesses internationally uncompetitive. Kenya will also be working towards harmonising its tariff structures with those of COMESA and the East African Co-operation trading partners to establish a common external tariff. Accordingly, a review will be undertaken over the coming year on how to reduce further and rationalise tariff structures. Particularly important will be the identification of sectors with the potential for high domestic value added and employment creation to remain the focus of future protection.

As part of restructuring of the tariffs and removal of suspended duties, special attention has been paid to the major agricultural commodities to ensure that these key sectors receive adequate and sustainable protection. The current drought conditions however, are necessitating the lowering of duties on maize and milk to ensure domestic supplies are supplemented with imports. Further more, following the declaration by His Excellency the President of the drought situation as a national disaster, the suspended import duties on maize have already been removed to facilitate both the private sector and donor sponsored imports of maize to relieve the domestic shortage. Special attention has been paid to the restructuring of duties on sugar.

A package of policies has been designed to simultaneously enhance support to the domestic sugar industry and also lower costs for the domestic food and beverage processing industries. The duty rate on refined industrial sugar will be set at 70 per cent and that on other sugar at 100 per cent. Domestic manufacturers will be able to get remission of 65 per cent of the duty charged on industrial sugar for production for the domestic market by applying for remission through the EPPO Programme. The bonding and control provisions of the EPPO Programme will afford better control against diversion of such industrial sugar into the domestic market. With the high regular duty rates on sugar imports, the levy charged by the Kenya Sugar Authority on imports will be lowered from 20 per cent on industrial sugar to seven per cent, and from 40 per cent on domestic sugar to seven per cent. This will both remove the previous trade distorting effects of this levy and also lower the costs of food and beverage production making Kenyan businesses more competitive in the regional market.

To help alleviate the costs of the energy crisis and encourage private sector participation in power production, I am proposing a number of measures to support equipment purchase and duty rebates on fuel for emergency power supply. One: All electrical generators and generator sets will be made duty free and VAT exempt. Wind and solar powered generators will be zero rated under the VAT Act. Duty, tax and IDF fee exemptions will be available for the importation of the equipment and parts for rehabilitation of generators for emergency power supply. A special programme will be established in conjunction with KPLC to encourage institutions and companies with generators over 100 KVA in capacity to self-supply rather than use grid power.

Based on meter readings by KPLC of energy self-supply, registered companies will be able to get duty rebates on a prompt basis from KRA and customs as well as compensation from KPLC for the added cost of using their own equipment rather than drawing power from the grid. Approved emergency suppliers of power to the national grid will be able to get duty free fuel supplies. I am also proposing to allow companies manufacturing under bond for export to purchase residual fuel oil free of duty and EPZ enterprises to import duty free fuel for their standby generators.

Oil condensates have recently started to be imported so that a new import category has been created to cater for them with the same duty rate as kerosene. Under COMESA agreements, duties on imports from COMESA countries of origin will be reduced to zero by October 2000. These import duty reductions however, will be applied on a reciprocal basis. Stiff application of the rules of origin will also be applied. To reduce road carnage and entry of unroadworthy used vehicles, I propose to raise the surcharge on large buses and lorries over five tonnes and which are over five years old to the higher of 20 per cent or Kshs100,000. Imports of these types of vehicles which are over eight years old along with used tyres will be prohibited.

To enhance the control over the issuance of import declaration forms, the IDF fee will be divided into two parts: A fixed application fee of Kshs5,000 that will be collected at the time of application and any balance of the *ad valorem* fee at the time of importation.

Mr. Speaker, Sir, eighth, to promote motorcycle rallying as a sport, I propose to allow importation of duty-exempt motor cycles for approved rallies and entrance. To prevent abuse of exemption for motor cars and cycles for rallying, I am proposing that these vehicles become dutiable if they do not participate in the approved rally, or are otherwise disposed of to persons without duty-free privileges.

Finally, I am proposing to continue with the process of reducing non-essential exemptions and tightening their administration. This is necessary, not only for revenue reasons, but also to cut out abuse of these privileges. For the next Financial Year, import exemptions for donated passenger cars and minibuses, goods won in a raffle, films and projectors will be discontinued. While these measures will result in the loss of Kshs955 million from estimated revenues, this cost is considered a worthwhile investment in the economy. These measures will come into effect from midnight tonight.

Under the Excise Duty, first, in order to continue with the rationalisation of duty rates within the East African Community, I propose to reduce the duty rate on malt beer from 90 per cent to 85 per cent. To strengthen the control over undutied cigarettes for retail sale entering either through import smuggling, or through diversion of cigarettes intended for export, I am proposing to introduce excise stamps for all cigarette packages. This will improve the inventory control and allow the easier identification of duty paid, smuggled and diverted cigarettes. To off-set the cost of these stamps to the importer or manufacturer, the Excise Duty rate on tobacco products will be lowered by five per cent points. These measures, in conjunction with stricter administration of excisable goods and higher penalties on improper trading and handling excisable oil products, will increase revenues by Kshs77 million. The changes in the Excise Duty rates will come into effect at midnight tonight.

Regarding VAT measures, first, as already emphasized, the Government is faced with meeting a significant revenue shortfall as well as the need to provide investment incentives to restart economic growth. The VAT has become a broad-based and stable source of revenue. As a tax on consumption expenditures, it also avoids dampening investment incentives. Furthermore, in exempting unprocessed food and other agricultural products, it excludes most of the consumption expenditures of the poor, particularly those in rural areas. Therefore, the VAT has been targeted to bear the burden of meeting the revenue shortfall. The standard VAT rate will be increased by 3 percentage points from 15 per cent to 18 per cent and the rate on hotel and restaurant service will go up from 13 per cent to 16 per cent. These rate increases will bring the Kenyan rate closer to the rates prevailing in the East African region. I will also be proposing increases in the income tax reliefs to offset the effects of the VAT increase on low income workers.

Second, to encourage investment and exports, the provisions for refund of excess input deductions will be amended to hasten refunds. In place of the current practice of only making refunds available to those in a regular refund position, refunds will now be available to all businesses based on their making zero-rated supplies or undertaking major investments in physical category. In the case of investment, once the plant and equipment have been put in place and the excess input deduction exceeds Kshs1 million, the business will be able to apply for a refund. This removes the major cash-flow cost of investment.

Third, currently, services are subject to the VAT if they are included in a schedule of taxable services. In order to expand the VAT base and move to the more standard structure used internationally, I propose to make all services subject to VAT except those appearing on a negative list specifically exempting them. This negative list will include health, education and financial services, amongst others. All services currently subject to the VAT will remain taxable.

The new system will come into effect on 1st of January, 2001 in order to give service providers time to study the exempt services and apply for registration.

Fourth, the switch to a negative list to identify taxable services will effectively result in gaming and betting services becoming subject to the VAT. Accordingly, to avoid doubling the tax burden on this sector, and to simplify the tax system, I am proposing to amend the Betting, Lotteries and Gaming Act to discontinue the taxes on these gambling activities from 1st of January, 2001.

Fifth, to further expand the VAT base, I propose that the tax point for prepared and preserved food items which are already taxable at the manufacturing level and are generally consumed by the higher income group be made taxable through to the retail level. Basic food items, however, will not be taxable at the retail level. By contrast, to cut tax administration costs, I propose to remove zero-rated goods from being taxable at the retail level. These changes will come into effect from 1st of September, 2000.

Sixth, to provide greater certainty about the time of supply of services in the construction sector, I propose to define this tax point in terms of the issuance of the certificates of completion of work by an architect, a consultant engineer, or other appropriate supervisory professional.

Seventh, tax on construction service and building materials are deductible inputs when the newly constructed building is used in the production of taxable supplies, but not otherwise. To expand the tax base and prevent tax evasion, I propose to require that, that these input deductions be repaid when there is a change of use of the building to exempt activities. These VAT measures will increase revenues significantly by Kshs7,369 million and will assist to finance the expenditures on infrastructure and social programmes. The changes in the VAT rates will go into effect from midnight tonight.

Regarding income tax measures, first, my primary concern is to protect the incomes of low income workers from bearing an unfair share of the tax burden. I am, therefore, proposing to raise the personal relief significantly by 20 per cent.

(Applause)

This will increase the minimum monthly taxable income amount from Kshs8,000 a month to Kshs9,440 a month. It will also remove some 200,000 low-income employees from the tax rolls. This measure will be strengthened by the cancellation from 1st of January, 2001 of the payroll component of the Local Authority Service Charge, which is largely a tax on low income workers. These combined measures will shield low income workers from any adverse tax increases from the higher VAT. In addition, to prevent any inflation-induced "bracket creep," I propose to increase the bracket widths by 5 per cent.

Secondly, to encourage investment in industrial buildings, machinery and equipment, including power generators, I am proposing to increase temporarily the investment deduction rate from 60 per cent to 100 per cent through the end of 2001. This measure will be effective for investments put in use by businesses in the financial years starting on or after 1st July, 2000. To accelerate investment expenditures, the investment deduction rate will be reduced back to 60 per cent in steps over the next three years. This measure will encourage investment in physical capital by the private sector, which is key to restarting growth.

Mr. Speaker, Sir, third, to further encourage investment, I am proposing two amendments to the duty offset provisions for large capital investments to make it more effective. The duty offset will become refundable if the company can show that the use of investment deduction resulted in it having insufficient tax against which to offset the duty. Any duty offset claim will be added to the dividend tax account to avoid resulting in any compensating tax being payable.

To encourage savings for retirement and to increase the pool of risk capital available to businesses, I propose to increase the tax deductible contribution limit to registered pension funds by Kshs30,000 to Kshs210,000 per employee per year.

To ease the financial burden on home ownership, I propose to increase the amount of mortgage interest that is deductible from Kshs56,000 to Kshs100,00.

To improve tax compliance by companies and other businesses providing consultancy, agency and contracting services, I am proposing to introduce a two per cent withholding tax on gross payments in excess of Kshs24,000 a month. This will replace the withholding tax that already applies to individual consultants, agents and contractors.

To broaden the collection of withholding taxes on management and professional fees paid to non-residents, I propose to widen their definition to include, agency services.

To improve the efficiency of the distraint process for collecting tax arrears, I am amending the distraint rules to allow distraint agent to proceed with the distraint order without the presence of a tax officer.

These measures, in conjunction with enhanced administrative effort, particularly in arrears collection, will raise an additional Kshs1.1 billion.

Turning to the miscellaneous measures, I am proposing the following changes:-

(i) In response to complaints by businesses in manufacturing and other sectors about the proliferation of charges, raising the cost of raw materials, I am proposing to cancel a number of inspection charges on imports and fund these inspection services through appropriations-in-aid out of the import declaration form fee charge, that already funds the pre-shipment inspection and import verification service. Accordingly, the import inspection charge of the Kenya Bureau of Standards (KEBS), the Horticultural Crop Development Authority (HCDA) and the Kenya Plant Health Inspectorate Services will be cancelled.

(ii) Mr. Speaker, Sir, a systematic policy of the Kenya Revenue Authority assuming the responsibility for revenue collections of the Government is being followed in order to lower collection costs and increase accountability. Accordingly, a number of additional revenue items will be collected by the KRA in this Financial Year. These include the standard levy on domestic producers charged by the KEBS, the levy charged by the HCDA on horticultural exports, and the Kenya Sugar Authority levy. Further amendments to the Stamp Duty Act will be brought to the Parliament to facilitate the implementation of stamp duty collections by KRA, which will also commence collection of civil aviation fees as ordinary revenues, early in the new financial year. Finally, financial provisions have been made to assist with the restructuring of the Catering Training Levy Trust to allow the transfer of the collection of the levy to KRA.

(iii) To increase the transparency of tax administration, amendments are proposed to the KRA Act that will require KRA to publicise its annual accounts.

(iv) To remove the double licensing fees on accountants, advocates, doctors, architects and other professionals, I am proposing amendments to their various controlling Acts to cancel the trade licensing fees payable to central Government. They will be required to pay the Single Business Permit to local authorities. In addition, the consequential changes to the Trade Licensing Act are proposed to effect the removal of trade licensing fees for professionals.

(v) To further encourage the use of the Nairobi Stock Exchange (NSE) to raise capital, amendments are proposed to the Stamp Duty Act to provide exemptions from stamp duties for new and expanded listings of stocks and for the transfers involved in the creation of asset-backed securities, such as mortgage backed securities.

(vi) I am proposing two amendments to the Local Government Act.

(a) To discourage delays in payments of the Single Business Permit, a fine of three per cent per month will become chargeable on all late payments.

(b) The Local Authority Transfer Fund requires local authorities to implement their budgets promptly in order to comply with disbursement conditions. This requires the Ministry of Local Government to accelerate their budget reviews and approvals. To ensure this happens, local authority budgets will be approved within sixty days.

(vii) To ensure the proper use of funds disbursed under the Local Authority Transfer Fund, the LATF Act will be amended to allow one-half of one per cent of the funds to be used for operational expenditures relating to dissemination of information to local authorities, monitoring compliance with LATF disbursement conditions and reporting on Fund activities.

(viii) To promote the safe handling and discourage fraudulent dealing in petroleum products, I am proposing amendments to the Petroleum Act that will raise the fine significantly up to Kshs2 million for unlicensed storage, transport, handling of and trading in petroleum products or failure to follow proper procedures or rules for petroleum products.

(ix) To increase the flexibility of the use of Export Processing Zones (EPZ), amendments are proposed to the EPZ Act to licence enterprises for commercial activity to supply goods to other EPZ enterprises or for re-export to other countries, but to limit unfair competition with businesses undertaking similar regional trading business outside the Zones, no income tax breaks will apply to such commercial EPZ enterprises.

(x) Currently, the Airport Passenger Service Charge Act requires payments by passengers in transit forced to leave the airport due to circumstances beyond their control. An exemption will be provided for this anomaly. In addition, to harmonise with international practice, the monthly IATA exchange rate will be used for assessing the charge.

(xi) Mr. Speaker, Sir, while Retirement Benefits Act provides the legal framework for all retirement benefits and supersedes the other laws on this matter, it is important that this Act does not create conflict with banking and revenue laws. Accordingly, I am proposing amendments so that it does not prevail over the Central Bank of Kenya Act and any revenue law. I am also proposing to clarify the definition of an actuary to include all fully qualified actuaries under internationally recognised actuarial professional organisations.

(xii) Under the Insurance Act, a number of limits have not been adjusted for inflation. Therefore, I propose to raise the limits for compensation for the death of a child under ten years, and the right of the Commissioner to arbitrate on small life policies amongst others.

(xiii) Significant amendments were made to the Banking Act last year to ensure the strengths of banks to meet the challenges of the global financial markets and to comply with regional and international standards. I am proposing a number of additional amendments:

(a) When banks are licensed, the integrity and competence of the owners are vetted. Consistent with this policy, any transfer of more than five per cent of the shareholding in a bank, will now require prior approval by the Central Bank of Kenya.

(b) To facilitate the merger of banks, particularly small ones, detailed provisions are proposed covering the modalities of amalgamating institutions and the transfer of assets, liabilities and agreements.

(c) To help the enforcement of prudence in the banking system, clarifications are proposed to the terms "fraudulent" and "reckless" behaviour.

(d) To promote co-ordination of the regulation of financial markets within Kenya and the region, provisions are proposed to allow the exchange of information between the Central Bank of Kenya and other monetary and financial authorities.

(e) Amendments will also be proposed to allow for the establishment of credit reference bureaus to help reduce the incidence of poorly performing loans in the banking sector.

Finally, to further enhance confidence in the financial markets, there is a need to severely discourage the issuance of bouncing cheques. I am, therefore, proposing amendments to the Penal Code to make it a criminal offence the issuing of cheques with insufficient funds or using such cheques to raise loans or misrepresent the financial status of an institution or an individual. In addition, with the development of computerised banking and business operations, I am making proposals to update the Evidence Act to provide for the conditions under which computer print-outs or statements can be admissible documents as evidence.

The miscellaneous tax measures announced above will raise an additional Kshs1.025 billion.

Mr. Speaker, this Budget represents a new beginning for Kenya. First, we have employed new approaches to budgeting. The use of the MTEF and the development of a poverty reduction strategy have allowed Kenyan stakeholders from the public and the private sectors to participate actively and in a systematic fashion in setting objectives and priorities and identifying the policy measures that went into the preparation of this Budget. We can truly say that we have presented the Budget for Kenyans. Second, far-reaching reforms in improving governance have ben implemented this year, and further measures will be implemented in the up-coming year that will improve the capacity, professionalism and integrity of the public sector to ensure that the measures contained in this Budget are efficiently implemented. Kenyans not only want the Budget they deserve, but they also expect to receive the public services that the Budget finances. Third, this Budget also represents the beginning of a new relationship with our development partners. They have provided constructive assistance in the development of the Budget, which incorporates substantial funding commitments from external sources. I look forward to strengthening this productive relationship in the coming year.

The combination of these planning procedures and policy measures will establish a strong platform and provide investors at home and abroad with greater confidence in our economy that will provide a solid basis for economic recovery and poverty reduction.

Mr. Speaker, Sir, it is regrettable that the recent onset of severe drought conditions are going to make the next financial year more difficult than we had originally planned and hoped for. Fortunately, the good relationships we have developed with our Kenyan stakeholders and development partners in the preparation of the Budget and reform programme are already providing a productive working relationship to develop the emergency relief measures to deal with food and electrical power shortages. These measures will be implemented on an urgent basis over the next few months such that the worst effects of the drought can be alleviated. At the same time, we will re-assess the economic and physical situation in order to make adjustments necessary to the Budget to accommodate the physical impacts of the drought and additional donor assistance that we are seeking. As an indication of my deep concern over the drought-induced economic problems and to set the ball rolling in our quest to save our meagre resources, the traditional Budget Party that Ministers of Finance have held following the Budget Statement in past years will not be held today.

(Applause)

I do hope that hon. Members will endorse this decision fully. However, there are fresh refreshments out in the form of sodas and cups of tea which I think befits our emergency situation.

Mr. Speaker, Sir, finally, I will conclude with what has been a traditional appeal by Ministers of Finance for co-operation amongst all Kenyans to pull together in a constructive fashion to achieve our national development objectives. The difference however this year, is the seriousness of the challenges that we currently face. As His Excellency the President has already pointed out, this drought is one of the most severe that the economy has faced. I appeal with all sincerity to all Kenyans to adopt a positive attitude, display commitment and participate fully in our efforts to overcome this emergency and move on to achieve the economic growth that we all seek in order to rid Kenya of the scourge of poverty.

Mr. Speaker, Sir, I beg to move.

Thank you.

The Minister for Education (Mr. Musyoka): seconded.

(Applause)

Mr. Speaker: Order, hon. Members.

(Question proposed)

DEPARTURE OF HIS EXCELLENCY THE PRESIDENT

Mr. Speaker: Hon. Members, it is now the pleasure of His Excellency the President to take his leave. All arise.

(Hon. Members rose in their places while His Excellency the President left the Chamber)

ADJOURNMENT

Mr. Speaker: Hon. Members, it is now time for the interruption of business the House is therefore, adjourned until Tuesday, 20th June, at 2.30 p.m.

The House rose at 4.45 p.m.