REPUBLIC OF KENYA
THE NATIONAL TREASURY & PLANNING

PRESS STATEMENT

Thursday, 8th July, 2021.

FOR IMMEDIATE RELEASE

UPDATE ON REFORMS OF STATE CORPORATIONS

The National Treasury wishes to announce its ongoing efforts towards developing a national strategy to improve the governance and financial oversight, as well as address the debt vulnerabilities, of State Corporations (SCs), as outlined in the 2013 *Presidential Taskforce Report on Parastatal Reforms*.

Kenya has approximately 260 SCs which play an important role in the economic and social development of the country, by providing essential social services and achieving strategic commercial objectives on behalf of the Government and for the benefit of the citizens.

However, the financial performance and operational efficiency of many SCs have been deteriorating in recent years, weighing heavily on public finances, by increasingly relying on budgetary support from the government in the form of grants, subsidies, government loans and debt guarantees. These Government transfers to SCs are no longer proportional to the social and economic benefits gained from these corporations, in effect limiting public resources available for investment in other critical areas of national development.

Consequently, the National Treasury selected eighteen (18)[1] major State Corporations based on the size of their activities, strategic importance and financial risks, to undertake an in-depth financial evaluation and fiscal risk analysis.

Financial Evaluation
The State Corporations were grouped into three broad categories for the financial evaluation and analysis as follows: - (See Table below):

[1] Kenya Airways (KQ) where the Government of Kenya has a 48.9% shareholding is not included in the financial evaluation and analysis, as it has retained an international aviation consultant to undertake a forward-looking evaluation, which is still ongoing.

- Large Service Providers (profitable and unprofitable);
- Social Service Providers (such as hospitals and universities); and
- Insolvent or Loss-making Government-Owned Enterprises.

Category	State Corporation (SC)	Earnings Rating	Characteristics
Large Service Providers	1. Kenya Ports Authority (KPA) 2. Kenya Pipeline Company Ltd. (KPC) 3. Kenya Airports Authority (KAA) 4. Kenya Electricity Generating Company PLC. (KenGen)	Profitable	Regularly pay dividends and taxes and are the main revenue earners and profit makers in the State Owned Enterprises sector.
	5. Kenya Power & Lighting Company PLC. (KPLC) 6. Kenya Railways Corporation (KRC)	Unprofitable	Highly indebted with on lent loans, hold large liabilities and have acute liquidity challenges.
Insolvent or Loss-making wholly or majority Government-Owned Enterprises	7. Kenya Broadcasting Corporation (KBC) 8. East African Portland Cement Company PLC. (EAPCC) 9. Postal Corporation of Kenya (PCK) 10. Kenya Post Office Savings Bank (KPOSB)	Loss making	Have lost market share to effectively compete and have generated large tax and social security arrears.
Social Service Providers	11. Kenyatta National Hospital (KNH) 12. Kenya National Examinations Council (KNEC) 13. Athi Water Works Development Agency (AWWDA) 14. Kenya Wildlife Service (KWS) 15. University of Nairobi (UoN) 16. Jomo Kenyatta University of Agriculture & Technology (JKUAT) 17. Moi University (MU) 18. Kenyatta University	Operating below cost recovery	Have strong social mandates to deliver core services that are affecting cost recovery, resulting in the accumulation of arrears, and are heavily dependent on government transfers.

Table: *Typology of 18 State Corporations (SCs)*

The evaluation broadly assessed agencies' projected cash-flows for the period FY2021/2022 - 2024/2025 incorporating *market/sales outlook* and *liability structure* including *contingent liabilities*, which have the potential to migrate to and crystallize in the national budget.

From the eighteen (18) sampled State Corporations for the financial evaluation, the estimated liquidity gap over the next five (5)-year period is KES. 382 billion. This calculation is based on a set of conservative assumptions, which presupposes that the entities' financials will in FY2021-22 be affected by the COVID-19 pandemic to the same degree as they were in FY2020-21 and that their financial health is fully restored during the 5-year evaluation period, with no extraordinary budget support and no borrowing to fill unmet liquidity needs. The estimated liquidity gap reflects the sizable financial woes in the State Corporations Sector. If these challenges are not addressed, they may crystalize into significant fiscal risks to Kenya's economy.

Findings & Recommendations

The following are the findings and recommendations from the evaluation of the 18 SCs:

- **State Corporations are facing financial shortfalls or liquidity gaps** – the 18 SCs have an estimated cumulative financial shortfall of about KES 70 billion annually [2] over the next five-year period. This requires multi-faceted efforts by all stakeholders to address the financial challenges facing SCs, including, but not limited to possible reforms and restructuring, through expenditure rationalization, revenue enhancing measures and sealing of revenue leakages to minimize financial support from the Exchequer.

- **Unprofitable State Corporations pose high fiscal risks to the Government** because of the large debts they owe the National Treasury and the associated repayment risks, as well as unsustainable pending bills/arrears.

- **Restructuring of insolvent or loss-making government-owned enterprises is expected to have limited costs for the Exchequer**, given their limited direct and indirect financial linkages with the national budget.

- **Entities supporting social welfare have suffered losses in recent years mainly due to their constrained revenues** and are more likely to require

[2] This does not include any potential financial support to Kenya Airways (KQ) which has already received KES 28 billion from the Exchequer in the Supplementary Budget 2020/21 to help it meet its liquidity needs and debt obligations.

government support to address their liquidity challenges, because of their critical social mandates.

- **The State Corporations have considerable scope to implement measures that would improve their financial performance and efficiency**, through diversification of revenue sources, better management of payroll and other operating costs, sale of non-profitable assets and ventures, review of capital investment plans, as well as leveraging ICT in service delivery, among other measures.

Next Steps
The following next steps will be undertaken:

1. **The National Treasury, working closely with individual State Corporations, will continue to gain a deeper understanding in the coming months, of the scope for increased revenue generation and/or cost-saving efforts at these firms, with a view to minimizing or eliminating their dependence on Exchequer support.**

   The estimated liquidity gaps will serve as major inputs in this process, and closing the gaps will require one or more of the following liquidity management choices:

   - Reform measures/initiatives, to boost revenues and rationalize spending;
   - New concessional borrowing;
   - Deferred payment for on-lent loans;
   - A debt-to-equity swap;
   - Additional transfers from the Government, or
   - A combination of the preceding measures.

   Furthermore, the National Treasury is reviewing the business models and operating environments of these SCs, with the possibility of proposing solutions such as a combination of new borrowings and expenditure rationalization for Large Service Providers, that recently experienced significant financial shortfalls.

   Decisions on least-cost strategies and additional government support beyond what is already proposed in the FY21/22 budget will be made in the coming months, in consultation with SCs. Proposals for the restructuring of a number of SCs have already been submitted and received by the National Treasury for consideration.

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In closing the financial shortfalls of SCs, they will be expected to prioritize reforms that improve their financial situation, with any potential financial support from the Exchequer being temporary and only as a last resort.

2. **The National Treasury will continue to apply a staged approach to its State Corporations reform strategy** in the coming months to:

- strengthen the legal framework and institutional structures of SCs;
- improve performance monitoring;
- enhance controls and transparency; and
- bolster the relationship between SCs and the National Government.

The aforementioned reforms are expected to reinforce public accountability for delivering value for money in the State Corporations' portfolio and mitigate fiscal risks to the Exchequer. Efficient and better-managed SCs will significantly contribute to stronger and more inclusive growth, by providing better services as well as help create the much-needed fiscal space for development spending by the National Government.

IMF Support

The evaluation of State Corporations was initiated by the Government in response to the existing structural issues in the financial performance of SCs which were further deepened by the COVID-19 pandemic. It has been carried out with the technical support of the International Monetary Fund (IMF) experts and is part of the 38-month programme between Kenya and the IMF.

The National Treasury will continue to address and improve the country's fiscal vulnerabilities drawing from the technical expertise, broad experience and global best practices of the IMF and greatly values this partnership.

Hon. (Amb.) Ukur Yatani, EGH
Cabinet Secretary, The National Treasury & Planning

NAIROBI, 8th July, 2021.

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