This year over KES 330 billion has been allocated for infrastructure projects which accounts for about 15% of the Consolidated National Government Budget.

The rate of budget absorption by infrastructure related ministries has been about 60%.

Infrastructure… Are all the ingredients in place?

Government continues to invest towards Vision 2030 projects. The delivery of infrastructure projects will depend on how well resources are utilised.

Ambitious allocation of funds for infrastructure projects

The allocations to infrastructure are a good measure to ensure sustained economic growth as well as to spur employment creation.

Focus on flagship projects
Kenya's Medium Term Plan II (2013-17) identifies Energy and Infrastructure as key enablers for sustained economic growth, development and poverty reduction. By focusing on this, Kenya will lower its cost of doing business and improve its global competitiveness. In staying with this agenda, in the National budget estimates 2015/16, the Cabinet Secretary (CS) to The National Treasury has apportioned over KES 330bn to capital projects, infrastructure and energy.

Funding will be geared towards improving the transport network, energy generation, water conservation and irrigation. The standard gauge railway will be fast-tracked for completion by end of year 2017, earning a budgetary allocation of KES 143.9bn. Further allocation of KES 40bn will go to enhancing access to energy and absorption of the 280MW generated from the target of 5,000MW. New road infrastructure and maintenance of existing infrastructure will cost KES 132bn. To improve our harbors and ports, the Lamu port will be a priority and will be financed through Public Private Partnerships (PPPs). An allocation of KES 1.3b will go to finance new ferries.

The generation of additional energy capacity has already borne results with reduction of the cost of energy. This will improve the cost of production and manufacturing.

The allocations to infrastructure are a good measure to ensure sustained economic growth as well as spur employment creation. The government policy to ensure 40% of the inputs to these projects are procured locally will also create a multiplier effect on the economy, thereby sustaining the projections of a 7% economic growth rate. However, there are also concerns as to whether the budgetary allocations are sufficient to meet the Medium Term Plans (MTP) II priorities. Some of the projects that seem to have lower visibility include the LAPSET corridor projects, which will be financed under the PPP arrangements. Other than Lamu Port, there was no mention of the related projects.

In addition, the low absorption capacity of the Government especially on infrastructure projects may impede the timely completion of major flagship projects and envisioned key drivers of economic growth.
The budget has also outlined monetrary policy measures to safeguard the Kenya shilling against the strengthening of the US dollar. The exchange rate losses on the capital projects and infrastructure could be quite significant since approximately 60% of inputs will be imported. It remains to be seen if the current safeguards will be sufficient to hedge against foreign currency exposure given most of our revenue is in local currency compared to the loans repayments in US Dollars and Euros.

Financing

In his speech, the Cabinet Secretary (CS) acknowledged that public sector resources are insufficient to close the existing infrastructure financing gap. The CS left options open for raising additional funds from local and international sources.

Government plans to rely on Private Public Partnership (PPPs) to implement some of the projects.

One of the models which the Government continues to explore in order to address infrastructure bottlenecks and funding constraints is the potential of PPPs.

The key projects earmarked for PPPs highlighted in the 2015/16 Budget include:

- road projects,
- generation of 5000 MW of electricity and
- the construction of university hostels.

In emerging markets that are planning to undertake PPP projects, the risk is whether the private sector is able to respond to the projects brought to the market by the public sector, or the cost of responding is high, undermining the business case and rationale for the PPPs.

It is important to come up with the right structure, payment mechanism and risk transfer and assess the capacity of the private sector to respond. This requires assessing the following:

- What is the structure and capacity of the local industry and if they will be able to bid or support the bidders planning to bid for concession; will the international bidders be willing to come into a new market and what will be the key risk factors that they will consider as 'no-go'?
- Are there local and international infrastructure developers that will be interested to bid and what will be their key investment criteria and key risk factors and how are they likely to view the transactions?
- Is there a local / regional funding market (bank, capital markets / bond and others) that can provide funding to the project and on what terms – long term / pricing and key terms?
- Are the proposed terms 'bankable' whilst at the same time ensuring the public sector receives value for money?

Other funding sources

All these projects are meant to spur economic growth and encourage Foreign Direct Investment into Kenya once completed.

The CS has adopted a raft of measures to ensure the projects are completed within the stipulated time by ensuring there is adequate funding. Some of the measures are:

- Taxation
- Domestic and External financing
- The precautionary Stand-by Arrangement and a Stand-by Credit arrangement with the IMF for an amount of US$ 688.3 million. However, this facility is to be drawn only in the event of an exogenous domestic or external shock.

Given the above the government has ambitious projects which require large capital outlay. Therefore the sourcing of funds and the implications need to be considered in tandem.

Constraints to budget absorption

Procurement

In the budget speech, the CS for The National Treasury recognises that in the past procurement has been a bottleneck in the delivery of infrastructure projects. The CS indicated that Ministries Department and Agencies (MDAs) will be required to use the eProcurement Module of the IFIMIS system. Other measures to make procurement more beneficial are the requirement that 40% content of all procurement for infrastructure projects should be Kenyan and also that 'buy Kenya build Kenya' will be built into all public procurement. These are commendable measures to streamline procurement short of overhauling the procurement law.

Financial disbursements

Some of the infrastructure projects are financed by development partners. More often, project implementation is slowed by the conditions put on disbursements and different procurement regulations. As implementing MDAs cope with the conditions, payments are delayed and projects may stall. This will need to be addressed as it may be a cause of slow implementation of the infrastructure projects that are planned to disburse over KES 330bn in 12 months.

Capacity of implementing MDAs

Procurement process may be complete and financial disbursements may be efficient but there is still the question of the capacity of the implementing MDAs to deliver, such as in financial management. This should have been addressed in the speech and measures outlined to ensure remedial capacity building for MDAs that may have history of inadequate implementation capacity.