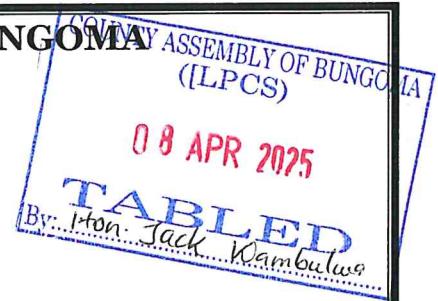
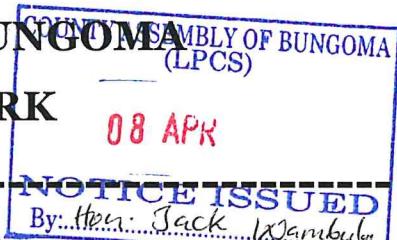


COUNTY GOVERNMENT OF BUNGOMA



COUNTY ASSEMBLY OF BUNGOMA

OFFICE OF THE CLERK



THIRD ASSEMBLY FOURTH SESSION

BUDGET AND APPROPRIATIONS COMMITTEE

**MEDIUM TERM DEBT MANAGEMENT STRATEGY
PAPER FOR THE PERIOD FY 2025/26 - 2027/28**

**Clerks Chambers
County Assembly Buildings
P.O BOX 1886 - 50200
BUNGOMA, KENYA**

MARCH 2025

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CHAPTER ONE

1.0 Preamble

Mr. Speaker Sir, it is my pleasure to present the report on the Medium Term Debt Management Strategy Paper for the period of three years 2025/26 to 2027/28 which was tabled on 4th March, 2025 and committed to Budget and Appropriations Committee for consideration.

1.1 The Mandate of the Committee

Mr. Speaker Sir, Budget and Appropriations Committee is established under Standing Order 210 of the County Assembly of Bungoma and is mandated to:

- a) Discuss and review the estimates and make recommendation to the County Assembly;
- b) Examine the County Fiscal Strategy Paper presented to the County Assembly;
- c) Examine the County Debt Management Strategy Paper presented to the County Assembly;
- d) Examine Bills related to the County Budget, including Appropriations Bills; and
- e) Evaluate tax estimates, economic and budgetary policies and programmes with direct budget outlays.

1.2 Committee Membership

Mr. Speaker Sir, the Committee on Budget and Appropriation as currently constituted comprises of the following Members:-

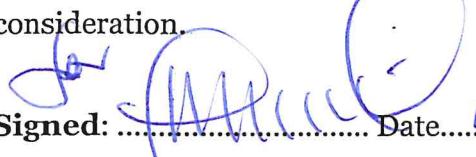
1. Hon. Jack Wambulwa	Chairperson
2. Hon. Charles Nangulu	Vice chairperson
3. Hon. Anthony Lusenaka	Member
4. Hon. Joan Kirong	Member
5. Hon. Meshack Simiyu	Member
6. Hon. Sudi Busolo	Member
7. Hon. Milliah Masungo	Member
8. Hon. Ali Machani	Member
9. Hon. Grace Sundukwa	Member
10. Hon. Polycarp Wandabusi	Member
11. Hon. Caleb Wanjala	Member

1.4 Acknowledgment

Mr. Speaker Sir,

The Committee appreciates the Offices of the Speaker and that of the Clerk of the County Assembly for making this undertaking a success through facilitation and other logistics offered during report writing. The Committee also register its gratitude to the members of the Committee and the secretariat for successfully compiling this report.

Mr. Speaker Sir, it is therefore my pleasant duty and privilege, on behalf of the Budget and Appropriations Committee, to table this report and recommend it to the House for consideration.

Signed:  Date..... 1st April 2025

HON. JACK WAMBULWA, MCA KIMAETI WARD

CHAIRPERSON, BUDGET AND APPROPRIATIONS COMMITTEE

CHAPTER TWO

2.0 GUIDING PRINCIPLES IN THE EXAMINATION OF THE DEBT MANAGEMENT STRATEGY

2.1 Legal Framework

Mr. Speaker Sir, the Debt Management Strategy Paper has been developed in accordance with Section 123 of the Public Finance Management Act, 2012 which provides as follows:

“(1) On or before the 28th February in each year, the County Treasury shall submit to the County Assembly a statement setting out the debt management strategy of the county government over the medium term with regard to its actual liability and potential liability in respect of loans and its plans for dealing with those liabilities.

(2) The County Treasury shall include the following information in the statement –

(a) The total stock of debt as at the date of the statement;

(b) The sources of loans made to the county government;

(c) The principal risks associated with those loans;

(d) The assumptions underlying the debt management strategy; and

(e) An analysis of the sustainability of the amount of debt, both actual and potential.

(3) As soon as practicable after the statement has been submitted to the County Assembly under this section, the County Executive Committee Member for Finance shall publish and publicize the statement and submit a copy to the Commission on Revenue Allocation and the Intergovernmental Budget and Economic Council.

Further, Article 212 of the Constitution of Kenya provides for borrowing powers by Counties on guarantee by the National Government.”

Regulation 182(2) (d) of the Public Finance Management (County Governments) Regulations 2015 requires the preparation of the County Medium Term Debt Strategy to be consistent with the County Fiscal Strategy Paper.

Further **Section 140(1) (c) (d) of the Public Finance Management Act 2012** provides that

(1) A County Executive Committee Member for Finance may, on behalf of the county government, raise a loan for that Government's purposes, only if the loan and the terms and conditions for the loan are set out in writing and are in accordance with—

(a) Article 212 of the Constitution;

(b) Sections 58 and 142 of this Act;

(c) The fiscal responsibility principles and the financial objectives of the county government set out in its most recent County Fiscal Strategy Paper; and

(d) The Debt Management Strategy Paper of the county government over the medium term.

(2) A loan may be raised either within Kenya or outside Kenya.

Article 212 provides that “A county government may borrow only—

a) If the national government guarantees the loan; and

(b) With the approval of the county government's assembly

Section 142 of Public Finance Management Act 2012 states that:

1) The County Assembly may authorize short term borrowing by county government entities for cash management purposes only.

(2) Any borrowing under sub-section (1) may not exceed five percent of the most recent audited revenues of the entity.

(3) A county government entity that has any such borrowing shall ensure that the money borrowed is repaid within a year from the date on which it was borrowed.

Mr. Speaker Sir, it is worth noting that the linkage between the County Fiscal Strategy Paper (CFSP) and Medium Term Debt Management Strategy Paper (MTDMSP) cannot be overlooked and this explains why the two documents are tabled on the same day.

It should be understood that approving the Medium Term Debt Management Strategy Paper does not in itself authorize the County Government to borrow but it only gives a framework and an additional strategy which the County Government can pursue to fund deficit in its budget.

The National Government is guarantor for all debts accrued by the County Governments therefore County government can borrow only if and when the National Government approves. These powers are vested in the Cabinet Secretary for Finance who guarantees the loans by County Governments and this is approved by Parliament.

However, the County loans will be guaranteed by the National Government only if the following Fiscal Responsibility Principles are adhered to:

1. Over the medium term a minimum of thirty percent of the County Government shall be allocated to the development expenditure.
2. The County Government expenditures on wages and benefits for its public officers shall not exceed 35% of the County Government total revenue.
3. Over the medium term the County Government's borrowing shall be used only for the purposes of financing development expenditure and not for recurrent expenditure.
4. The County debt shall be sustained at 20% of the most recently audited revenues and the cost of debt shall not exceed 15%.
5. A reasonable degree of predictability with respect to the level of tax rates and tax bases shall be maintained taking into account any tax reforms that may be made in the future.

6. The fiscal risk shall be managed prudently.

2.2 Procedure for borrowing by the County Government

Mr. Speaker Sir, pursuant to Section 58 PFMA, the following procedure will apply when County Government wants to borrow especially long term borrowing:

- a) The County Executive Committee Member for Finance shall submit the borrowing proposal to the County Executive Committee for approval of the borrowing including its terms and conditions;
- b) After approval by the County Executive Committee, the County Executive Committee Member for Finance shall submit the signed loan agreement and a sessional paper to the County Assembly for approval of the borrowing, including its broad terms and conditions;
- c) After obtaining the approval of the County Assembly, the County Executive Committee Member for Finance shall submit the final draft loan financing agreement and the approval of the County Assembly to the Cabinet Secretary requesting for the guarantee of the final loan financing agreement;
- d) The Cabinet Secretary, after receiving the request from the county government, shall seek the recommendations of the Inter-governmental Budget and Economic Council;
- e) The Cabinet Secretary to the National Treasury, after receiving recommendations of the Inter-governmental Budget and Economic Council, shall seek the recommendations of the Attorney-General;
- f) The Cabinet Secretary may, upon taking into account the recommendations of the Intergovernmental Budget and Economic Council and the Attorney-General, approve or reject the request;
- g) The Cabinet Secretary shall reject a request for loan guarantee with reasons and communicate the same to the concerned County Executive Committee Member for Finance.
- h) Upon approval of a loan guarantee request, the cabinet secretary shall submit a sessional paper to parliament with recommendations seeking its approval;

- i) The Cabinet Secretary shall communicate the decision of Parliament on the draft loan guarantee to the respective County Executive Committee Member for Finance; and
- j) Upon approval by the parliament the Cabinet Secretary shall issue a loan guarantee.
- k) After receiving the communication of the decision of the Parliament on the draft loan guarantee, the County Executive Committee Member shall report to the County Assembly of the decision.

CHAPTER THREE

3.0 SCRUTINY OF THE MEDIUM TERM DEBT MANAGEMENT STRATEGY PAPER FOR FY 2025/26 TO FY 2027/28

3.1 Introduction

Mr. Speaker Sir, the Medium Term Debt Strategy Paper FY 2025/26 to FY 2027/28 is the 7th prepared by the County Government and the third under CIDP 2023-2027. It sets out the debt management strategy of the County Government over the medium term with an aim of guiding prudent debt management and minimizing high cost associated with excess borrowing.

The County MTEF budget for FY 2026/27 and the medium term projections shows an enlarging financing gap thus justifying the need for this strategy paper. The required budget based on CIDP 2023-2027 is Kshs. 81.6 billion for the FY 2025/26 to 2027/28 while revenue projections are Kshs. 50 million implying that only 61.30% of the budget requirement can be financed leaving a financing gap of Kshs. 31.5 million representing 38.70%. In order to finance budget deficit and bridge the gap between resource requirements and allocation with National Government guarantees, Bungoma intends to initiate borrowing domestically and externally.

This paper has also highlighted the magnitude outstanding financial obligations resulting from the accounts payable across the departments totalling to Kshs. 3.66 billion.

The County government has a short-term arrangement with the Kenya Commercial Bank, Bungoma Branch, to facilitate salary payments in the event of delays in the exchequer releases.

3.2 Goals and Objectives

Mr. Speaker Sir, the Debt Management Strategy covers three years with provisions for annual review. The main objectives of the Medium Term Debt Management Strategy Paper are as follows:

- a) To provide appropriate guideline and direction to assist in making sound debt management decisions with strong financial management practices for posterity.

- b) To meet the County Governments financing requirements at the least cost with a manageable degree of risk.
- c) To guide county government debt management operations in the FY 2025/26 and in the medium term.
- d) To balance cost and risk of county debt while taking into account the County Government financing needs by incorporating initiatives to seek new funding sources, support the County Government development priorities and achieve debt sustainability.
- e) To diversify the governments funding sources and their investment portfolio.
- f) To advance measures to maintain and develop an efficient domestic debt market.

3.3 Debt Management Strategy Finance Principles

The following principles should be adhered to;

- i. The debt must be for capital projects
- ii. The debt must be guaranteed by National Government
- iii. The debt must be contracted to support expenditure in identified County priority areas that are transformative
- iv. Prudence must be observed when contracting debt taking into account the cost and risk implications
- v. Financing must be pegged on debt sustainability over the long term

3.4 Bungoma County Liabilities

Mr. Speaker Sir,

The County accumulated accounts payable amount to Kshs. 3,665,142,229 as at June 2024. The County formed a pending bill committee to address the issue and based on its recommendations, the cabinet approved that 30% of the Bills to be paid each year for three years as per the below schedule for account payable payment;

SNO	YEAR	AMOUNT
1	2024-2025	1,215,752,788
2	2025-2026	1,157,133,263
3	2026-2027	1,292,256,178

The County Government projects to borrow Kshs. 2,399,727,879 which is 20% of actual revenue arising from last audited accounts at a negotiated interest rate of 11.25 p.a on reducing balance. The debt is to be serviced in 15 years with an annual repayment of Kshs. 338,336,759.

3.5 Strategies for management on Debt in the Medium Term

Mr. Speaker Sir,

The County Debt Management Strategy presents three main strategies that County Government of Bungoma will explore in the next three years in debt management. These strategies include: -

Strategy 1: External Financing (Semi and concessional) and some domestic bond financing.

Mr. Speaker Sir, External debt refers to loans that a country or entity borrows from foreign lenders, which can include foreign commercial banks, foreign governments, and international financial institutions such as the International Monetary Fund (IMF) or the World Bank. One key characteristic of external debt is that all payments, including interest and principal repayments, must be made in the currency in which the debt was issued. This means that if a country borrows in US dollars, for example, it must repay the loan and interest in US dollars, which can expose it to currency exchange rate risks.

This strategy evaluates the cost and risk aspects of a continuation of current borrowing practices for Bungoma County which will form a benchmark for examining different approaches. This strategy is based on current practice of external and domestic borrowing and therefore does not best address the priority issues of foreign exchange risk, liquidity and repayment risk, creditor concentration risk and refinancing risk.

Mr. Speaker Sir, the following are the risks associated with this strategy:

- a) **Affects economic growth:** Economic growth occurs when governments and companies incur capital expenditures that boost production and increase output

and income levels. If large amounts of external debt need to be repaid, then there is less money left for investment purposes. It hampers future economic growth.

- b) **Long gestation period:** Gestation period is the interim period between the initial investment in a project and the time the project becomes productive. When external debt is used to fund infrastructure projects, it takes a few years for the project to start giving a return on the investment. However, the debt will need to be repaid, along with interest, within a provided time of receiving the loan. Thus, government will face the pressure of repaying the loan even before the project starts yielding a stable return.
- c) **Unexpected devaluation of domestic currency:** If the currency of the borrowing country depreciates with respect to that of the lending country, then the real value of interest (as denominated in the domestic currency) will rise.
- d) **The Vicious Cycle of Debt:** The most crucial disadvantage of external debt is that it often leads to a vicious cycle of debt. The debt cycle refers to the cycle of continuous borrowing, accumulating payment burden, and eventual default. When a government's expenditure exceeds how much it earns in a year, it faces a fiscal deficit. In order to finance the adverse gap, the government borrows money from another country. In the next year, with the additional expense of interest payment and loan repayment, the government might face a deficit again and be forced to take another external loan. In subsequent years, there might be a situation where it borrows money in order to repay its previous loans.

Strategy 2: Negotiated domestic borrowing and utilization of securities market

Mr. Speaker Sir, domestic borrowing refers to a government raising funds within its own country's financial markets. This is typically done through the issuance of various securities such as treasury bills and treasury bonds. Treasury bills are short-term debt instruments with maturities ranging from 91 days to 364 days, while treasury bonds have longer maturity periods, typically exceeding one year. These securities are used by

governments to meet short-term funding needs (treasury bills) or to finance long-term projects and expenditures (treasury bonds).

The risks associated with this strategy are as listed;

- a) Domestic borrowing could lead to pressure on institutional investors and banks to absorb “too much” government debt and this may have a negative effect on financial stability.
- b) Expanding the market for domestic government bonds may have the risk that the public sector may crowd out private issuers.
- c) Finally, there are political economy reasons that may make domestic debt more difficult to restructure. In fact, a few highly indebted countries which were able to use debt relief initiatives to address their external debt problems are still burdened with high levels of domestic debt.

Strategy 3: External financing and some domestic bond financing

Mr. Speaker Sir, this is where the County combines both external and domestic financing in order to take advantage of the medium to high risk mainly due to the foreign exchange factor and low to medium cost in relation to County revenues. With gradual development of the domestic market this would provide a more balance composition of the public debt with less external debt and more domestic debt.

Bungoma County intends to use this third option which allows the county to source funding from both External and Internal sources of funding but with emphasis on Domestic borrowing in order to minimize the risks associated with external borrowing.

3.6 General Risks associated with Debts

Mr. Speaker Sir,

There are many inherent risks in any debt portfolio. The County Government of Bungoma should employ measures to mitigate these risks and to minimize the impact of various exogenous shocks on the debt portfolio.

Creditor Concentration Risk: This refers to risks associated with most of the debt portfolio being held by one or two creditors. Those who hold a large proportion of debt could have a vested interest in the course of a county's affairs and could potentially have an undue influence in policy development hence the investor base should be diversified and expanded.

Credit Risk of on-lent and guaranteed loans: When the level of outstanding on-lent loans from County Government of Bungoma is high, there is an implicit exposure to default and non-payment of obligations even when the loans are guaranteed. Deeper analysis and oversight required on these transaction.

Operational Risk: This arise from a small staff size and limited capacity. The difficulty in establishing the Debt Management office is a risk for Treasury and the County Government of Bungoma in general.

Strategic Risk: Strategic risk is the risk that decisions made about management of the debt portfolio have a high opportunity cost. If the CGoB decides not to borrow, then it could miss out on grant funding. If decisions to borrow for particular projects do not match expectations, then this money could have been better spent elsewhere on more beneficial projects. Money spent on servicing debt might be better spent on providing essential services.

Financial Risk: In this case, CGoB's portfolio management is so poor that it creates a source of instability for the private sector, less money is available for servicing the county's basic needs which could undermine development. A build-up of debt arrears might negatively influence investor confidence, weakening private sector activity, leading

to a withdrawal of investment in the county, a decline in growth prospects and a further increase in debt to revenue ratios. This is an extreme risk.

Market Risk: Refers to the risks associated with changes in market prices, such as interest rates, exchange rates, commodity prices, on the cost of the government's debt servicing.

Rollover Risk: The risk that debt will have to be rolled over at an unusually high cost or, in extreme cases, cannot be rolled over at all. To the extent that rollover risk is limited to the risk that debt might have to be rolled over at higher interest rates, including changes in credit spreads, it may be considered a type of market risk.

Liquidity Risk: This refers to a situation where the volume of liquid assets can diminish quickly in the face of unanticipated cash flow obligations and/or a possible difficulty in raising cash through borrowing in a short period of time.

Credit Risk: The risk of non-performance by borrowers on loans or other financial assets or by a counterparty on financial contracts.

Settlement Risk: Refers to the potential loss that the government, as a counterparty, could suffer as a result of failure to settle, for whatever reason other than default, by another counterparty.

CHAPTER FOUR

4.0 COMMITTEE'S OBSERVATIONS AND RECOMMENDATIONS:

4.1 Committee Observations

Mr. Speaker Sir, the Committee after analyzing the Debt Management Strategy Paper made the following observations;

1. This Medium Term Debt management Strategy Paper (MTDMSP) is the 7th to be prepared by the County Government since devolution and the Assembly notes the absence of an established public debt management unit.
2. The County Government of Bungoma's decision to borrow is vested in the County Assembly of Bungoma as the 1st approver. If the County Assembly is of the opinion that the county government's borrowing carries substantial financial risk, may attract high cost of servicing and is a threat to the County's budgeting and service delivery, then the Assembly can deny approval for the borrowing.
3. The County government has a short-term borrowing arrangement with the Kenya Commercial Bank, for an overdraft facility equivalent to one month's gross staff salaries to be utilized in payment of salaries in the event of delayed in exchequer releases but the limit of borrowing has not been indicated in the report.
4. The Committee notes that the County Government can borrow up-to a maximum of Kshs. 2,399,727,879 for development (Long-term borrowing), which represents 20% of actual revenue from the last audited accounts, to be serviced over 15 years at an interest rate of 11.25% p.a on reducing balance. The actual revenue from last audited account stood at Kshs. 11,998,639,364

4.2 Committee's Recommendations

Mr. Speaker Sir, based on the above observations, the Committee recommends as follows;

1. **THAT**, the County Government should establish a Public Debt Management Unit (PDMU) to enhance the efficiency and effectiveness of debt management. The unit will help in monitoring and coordinating the County's debt portfolio, ensuring

alignment with medium term debt strategy and offering expertise in the assessment of debt sustainability.

2. **THAT**, the County Government of Bungoma adopts Strategy 3; **external financing and some domestic bond financing, which will allow the** county to source for funding from both External and Internal sources of funding but with emphasis on domestic borrowing in order to minimize the risks associated with external borrowing.
3. **THAT**, Pursuant to PFMA Section 107(3), Short term borrowing shall be restricted to management of cash flows and shall not exceed five percent of the most recent audited county government revenue i.e. In this case this Assembly approves a short-term borrowing limit of Kshs. 599,931,968.
4. **THAT**, the County Government should conduct a comprehensive cost-benefit analysis for all proposed development projects to be funded through the long-term borrowing of Kshs. 2,399,727,879. This analysis should prioritize projects with high economic and social returns that will generate sufficient revenue streams to support debt servicing. Additionally, the County Treasury should negotiate for more favorable interest rates below the current 11.25% p.a, potentially through competitive bidding among financial institutions, to reduce the overall debt servicing burden which would amount to approximately Kshs. 5.07 billion over the 15-year period (principal plus interest).

4.3 CONCLUSION

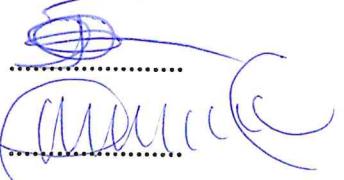
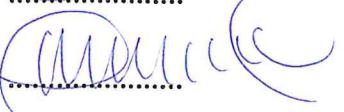
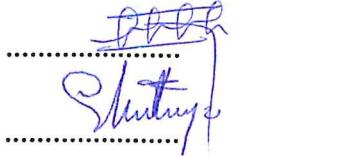
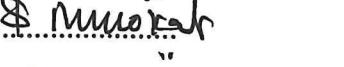
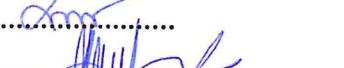
Mr. Speaker, the approval of this Medium Term Debt Management Strategy Paper for FY 2025/26 - 2027/28 by this House will provide the framework for the County Government of Bungoma to pursue for additional funds to finance its budget deficits especially on development expenditures.

5.0 ANNEXURE

Annex I : Adoption schedule

Annex II : The draft Bungoma County Medium Term Management Strategy
Paper for FY 2025/26 –FY 2027/28

Adoption schedule

Name	Title	Sign
1. Hon. Jack Wambulwa	Chairperson	
2. Hon. Charles Nangulu	Vice Chairperson	
3. Hon. Milliah Masungo	Member
4. Hon. Antony Lusenaka	Member	
5. Hon. Meshack Simiyu	Member
6. Hon. Joan Kirong	Member	
7. Hon. Sudi Busolo	Member	
8. Hon. Ali Machani	Member	
9. Hon. Grace Sundukwa	Member	
10. Hon. Polycap Wandabusi	Member	
11. Hon. Caleb Wanjala	Member	