

INTERNATIONAL MONETARY FUND
AND
INTERNATIONAL DEVELOPMENT ASSOCIATION

Republic of Kenya

Joint Staff Assessment of the Economic Recovery Strategy

Preparation Status Report

Prepared by the Staff of
the International Monetary Fund and the International Development Association

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Background

1. The Executive Boards of the IMF and the World Bank concluded in August 2000 that the government's interim poverty reduction strategy paper (I-PRSP) provided a sound basis for developing a fully participatory PRSP and for World Bank and IMF concessional assistance. The government produced a draft PRSP in November 2002, which was not submitted formally to the Bank and the Fund on account of the December 2002 elections. The new government of Kenya developed its own Economic Recovery Strategy for Wealth and Employment Creation (ERS), drawing heavily on the PRSP but also reflecting its own priorities. The refinement and augmentation of the ERS now underway is expected to be completed in December 2003.
2. The authorities have prepared a preparation status report on the ERS for presentation to the Boards of the Bank and the Fund in the context of Fund Executive Board consideration of the proposed PRGF program. The report lays out the main activities undertaken to date in developing the ERS and its links to the earlier draft PRSP. It specifies the additional steps being taken to complete the ERS in coordination with civil society and Kenya's development partners, and provides a timetable for completing the ERS. The report also describes how the evolving strategy has addressed the issues raised by the Fund and the World Bank in the joint staff assessment of the I-PRSP. The staffs believe that the broad areas of work listed in the ERS preparation status report are appropriate and respond to the issues raised in the JSA of the I-PRSP.

Assessment and recommendations

3. **Participation and consultation process.** The staffs acknowledge the wide-scale consultations that have taken place both under the previous government in preparing the I-PRSP and draft PRSP, and under the current government in preparing the ERS. The challenge now is on ensuring that the participatory framework remains in place to guide implementation. The staffs welcome plans to establish the National Social and Economic Council, with representatives from all social partners, to provide a forum for a broad range of stakeholders to express their views. The staffs suggest that the participatory process to be used during implementation be described in the final ERS.

4. **Overall strategy.** The staffs generally agree with the government on the priority measures identified to stimulate economic growth and reduce poverty. Creating an improved environment for investment and growth in agriculture, manufacturing, tourism, and in small- and medium-size enterprises is important. Financial sector reform will also be critical to stimulate growth and reduce poverty. In addition, promoting private sector participation in parastatals that provide essential public services to improve efficiency and effectiveness of service delivery is important. The staffs, however, urge the authorities to clearly identify a limited number of key priority actions that will have the greatest impact on growth and poverty reduction, given resource and capacity constraints. The staffs also encourage the government to mention in the ERS plans to undertake poverty and social impact analyses of major structural reforms that could have substantial negative social impacts. The Bank would be prepared to support the government with any such analyses.

5. **Monitoring and evaluation arrangements.** The staffs commend the government's efforts to strengthen its capacity for developing and disseminating statistics, for monitoring and evaluating poverty outcomes against quantitative targets, and for linking outcomes to intermediate output indicators that measure the results of public policy actions, concerns raised in the joint staff assessment of the I-PRSP. The comprehensive logframe matrix, increased capacity, and the plan for monitoring and evaluation to be included in the ERS, will enable Kenya to monitor progress towards achieving the targets of the ERS and the Millennium Development Goals. The Bank and the Fund, in partnership with other donors, will continue to provide support in this area through a variety of programs, including the Bank's Statistical Capacity Building Facility, planned for Board presentation in fiscal 2004.

6. **Poverty diagnostics.** The staffs recognize that Kenya has not carried out a poverty assessment for some time, and that knowledge of the determinants of poverty and its dynamics is therefore weak. The Bank, together with other partners, has been supporting the government in updating knowledge of poverty, including through support for creation of poverty maps. The staffs are pleased that the authorities intend to supplement existing data by drawing upon the emerging knowledge to formulate the ERS. The staffs in particular appreciate the authorities' intentions to gain a deeper understanding of the gender dimensions of poverty and to use this knowledge to enrich the strategy. The staffs however urge the government to draw on information gained

through survey instruments and other sources to deepen their understanding of all key determinants of poverty. The Bank and other partners will support the government in carrying out an integrated household budget survey to be completed in 2004 and in undertaking a comprehensive poverty assessment to be completed in 2005.

7. **Aligning the national budget process with the ERS.** The staffs applaud the government's intentions to align the national budget process with the ERS. Implementation of this commitment will be challenging, as past experience has shown. Aligning the national budget process with the ERS will require a realistic appraisal of available resources, careful costing of programs, and a commitment to significantly reallocate resources both within and between sectors. The staffs recommend that reforms needed to realign expenditures to achieve the pro-poor spending objective be clearly identified in the ERS. These include the difficult but important measures, such as civil service reform that could involve the retrenchment of staff, and parastatal restructuring and privatization.

8. **Medium-term expenditure framework and public expenditure review.** The MTEF and PER are essential tools in aligning the national budget process with the ERS. The staffs welcome the authorities' intentions to strengthen the MTEF as the basic tool for budget formulation. This will provide the means through which expenditure priorities identified in the ERS are translated into ministerial budgets within the resource constraints imposed by the overall macroeconomic framework. The staffs welcome the government's commitment to monitor the efficiency and effectiveness of public expenditures by undertaking annually comprehensive PERs covering expenditures of all ministries. This is important for evaluating budget strategy and performance, in testing and strengthening public expenditure management systems, and in ensuring that budgetary allocations reflect expenditure priorities laid out in the ERS.

9. **Institutional arrangements for coordination.** Proper alignment of the ERS with the budget process will require close coordination of the Ministry of Planning and National Development, the Ministry of Finance, and line ministries. The staffs have noted the institutional arrangements through which coordination will be achieved, including the sector working groups and the thematic groups that will identify the priorities before the start of the budget cycle. The staffs would however like to learn in more detail how greater coordination between the Ministry of Planning and National Development and the Ministry of Finance will be achieved, the nature of the working and thematic groups, how government capacity constraints will be overcome, and how the coordination process will be sustained and strengthened, particularly with regard to improvements in the PER process and mechanisms for donor coordination.

10. **Macroeconomic framework.** The staffs note the authorities' intentions to prepare a comprehensive macroeconomic framework to be presented in the ERS. The government's current macroeconomic framework is consistent with that underpinning the proposed PRGF-supported program. The staffs recommend that any revisions to current plans be incorporated into the framework underpinning the PRGF-supported program. They also suggest that the ERS describe how any additional resources that may become

available to Kenya to support the implementation of the strategy in the near and medium terms would be used, consistent with the growth and macroeconomic stability objectives of the ERS. Finally, they recommend that the ERS specify contingency mechanisms for managing public expenditure in the event of transitory shortfalls in budgetary resources.

11. **Timetable.** The staffs believe that the timetable presented in the preparation status report—with completion of the final ERS in December 2003—is realistic. The staffs agree that the discussions of the Consultative Group (CG) meeting to be held at the end of November 2003 will enrich the strategy, and support the decision to issue the document only after the authorities have had an opportunity to revise the strategy to reflect the comments of the CG. The staffs note that the government has not sought specific technical support to complete the ERS, and the staffs of the Bank and the IMF are working closely with the government to ensure that any needs for technical support are adequately met.

12. **Recommendation.** The staffs of the IDA and the IMF consider that progress on the development of the ERS, as evidenced in the ERS preparation status report, is satisfactory and provides a sound basis for continued access to Fund concessional assistance and to IDA assistance. The staffs recommend that the respective Executive Directors of the World Bank and the IMF reach the same conclusion.