UNIVERSITY OF NAIROBI

SCHOOL OF LAW

A RESEARCH SUBMITED TO THE UNIVERSITY OF NAIROBI IN PARTIAL FULFILMENT OF THE REQUIREMENT FOR THE MASTERS DEGREE OF LAWS (LLM)

COURSE TITLE: RESEARCH PAPER

COURSE: GPR 699

SUPERVISOR: DR. JACKSON BETT.

TITLE:

LEGAL REFORMS ON EXTERNAL PUBLIC DEBT LAW IN KENYA

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G62/11408/2018

DECLARATION

I, **Paul Wilkinson Waga**, declare that this research which I submit for the Masters of Law at The University of Nairobi is my original work except where indicated by special reference in the text. This research has not been presented in any other university for the award of Masters Degree award in Kenya or anywhere else in the World.

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Signed……………………………………………..

Date………………………………………………..

This thesis has been submitted to the University of Nairobi School for examination with the approval of Dr. Jackson Bett as the Supervisor.

Supervisor: Dr. Jackson Bett

Signed……………………………………………..

Date……………………………………………….

DEDICATION

To my Saviour Jesus Christ who gave his life for me that I may live and attain eternal life. His mercies endure forever more.

I can do all things through Christ which strengtheneth me. Philippians 4:3

To my parents, Dismas Bundara Waga and Pamela Waga, who denied themselves to ensure my siblings and I received education but most importantly for raising us in the way of the Lord. I have nothing to repay you but may God reward you always.

To my cheerleader and lovely wife Terian Oloo Burure, who has always been on my side and helped me during this rigorous period, and always prayed for me and our family. My God bless you my best friend.

And to my siblings, Waindi, Bundara, Osara, Asole, Aguko, Oria, Grace: May we continue to trust in the Lord.

ACKNOWLEDGEMENT

In the course of writing, I benefited immensely from a number of people.

First, I wish to acknowledge and thank my supervisor, Dr. Jackson Bett, who worked with me tirelessly and whose guidance I so greatly cherish. His wisdom on Public finance matters is unrivaled. It was a great privilege to be supervised by him.

My defence panel and specifically Dr. Munyi who timeously led me through the corrections. I thank you so much and may God reward you for your labours.

I would also like to acknowledge my father, Dismas Bundara Waga, mother Pamela Waga, Brothers, Don, Frank, Winnestone, Bolton, Oria, Aguko, Grace, Faridah and my extended family members. They constantly pushed me to finalize this long overdue project.

I would also like to acknowledge my many friends who are also undergoing this process as me, Kirunga, Joan, Kojo and all others of class 2018.

Table of Statutes
Kenyan statutes

1) The Constitution of Kenya.
2) Public Finance Management Act.
3) Finance Act
4) The Central Bank of Kenya Act.
5) Public Finance Management (National Government) Regulations 2015
6) Public Finance Management (County Governments) Regulations 2015

Nigerian Statutes

7) The Constitution of Federal Republic of Nigeria.
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ABSTRACT

External Public debt remains to be one of the sources of government revenue in most economies, Kenya included. However external public debt has metamorphosed into problem to many economies. This phenomenon has greatly impacted on most developing countries, where most of them find themselves locked in a public external debt burden and negative effects on economic growth. This research therefore takes a look at the Kenyan legislation with regards to public domestic debt and in specific foreign debts and whether the laws are sufficient to put an end to the runaway borrowing practices by the country and the changes (if necessary) to the current regulations on public debt and in specific to better manage the public debt.

CHAPTER ONE

1.0 BACK GROUND OF THE STUDY.

Debt is defined to mean a sum due by contract.[1]While foreign or external debts is defined by the World Bank to mean, sums owed by a country to foreign individuals, foreign institutions or another country.[2] This research aligns itself with the definitions offered by the World Bank and International Monetary Fund and refers to external debts as debts incurred by a country from without its borders.

Many developing countries rely heavily on debts to finance their budgets and various projects and as a result they experience difficulties in her huge pilling up external public debts.[3] Foreign debt has remained one of the sources of government revenue for most economies. This phenomenon has greatly impacted on developing countries where most countries find themselves locked in external public debt burden with dire consequences for example losing their key assets just as Sri-Lanka did lose its port to china.[4]

It seems incontestable that given the structural weaknesses of most developing economies, their low income, low savings and low investments, the current high levels of debt would militate against rapid economic development and at the same time burdening the countries with huge debts to offset. Thus necessitating this research for us to know and try to implement the necessary legal reforms to enable better acquisition and management of public debt.

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[1] Bryan A. Garner, 'Black's Law Dictionary,' West 8[th]ed (2009)9780314199492.

[2]http://www.documents.worldbank.org/curated/en/1930614872370806/external-debt-definition-statistical-coverage-and-methodology (accessed on 13/12/2018)

[3] Edwin Mutai, 'IMF warns over kenya's new debts, wants rate cap abolished,' Business daily, Thursday 22 February 2018

[4] http://www.nytimes.com/2018/06/25/world/asia/china-sri-lanka-port.html. (accessed on 11/11/2018)

1.2 HISTORICAL BACKGROUND

In Kenya, foreign debt has been increasing from time immemorial.[5]The relatively high level of Kenya's external debt and the continuous rising debt has caused alarm even in the international circles leading to a warning that the Kenya's debt is approaching the unsustainable levels and authorities being encouraged to take substantive steps to reduce the fiscal deficit to address Kenya's rising public external debt. [6]

In 2014 the Parliament of Kenya increased public domestic borrowing ceiling from 1.3 trillion to 2.5 trillion but in 2015 the Public Finance management Act was amended and the parliamentary oversight role was removed, giving leeway for increased borrowing which now stands at over 5 trillion.[7] It is no longer a question of when, but the impact of huge debts in the country is already being felt in the country as taxes are now being levied on all petroleum at 8% by implementation of Act No. 38 of 2016 also referred to as the Finance Act of 2016, leading to outcry in the general public.[8] This is in a bid to raise more revenue to pay maturing debts and fund government expenditure.

Kenya has a population of about 51 million people and if the Kenyan public debt was to be paid by individuals then it would mean that each person would be required to pay about Kenyan shillings 100,000/- not forgetting the projection that by 2022 the total debt of the country will be at 7 trillion Kenya shillings. Thus leading to the question, whether our public debt is sustainable?[9]

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[5] Joseph Onjala, 'China's developmemt loans and threat of debt crisis in Kenya,' Institute of Development studies, University of Nairobi (2017).

[6]IMF Country Report Number 18/295, October 2018.

[7] http://af.reuters.com/article/investingnews/idAFKBNOJ0OGH2014120 (accessed on 13/11/2018)

[8] Karen Kandie, 'The star: Viability of VAT on petroleum products, 2018. (accessed on 13/11/2018)

[9] Ibid n 6.

Unsustainable debt levels can be harmful because huge portion of government revenues are taken away from essential services and used instead to service debts. In the worst case scenario, countries have been forced to cede control of its strategic national assets to foreign creditors as in the case of Sri Lanka which had to hand over its strategic port to China.[10]

The significance of this study lies in the fact that the Kenyan debt burden presents a gruesome picture of hopelessness and how legal reform on foreign debt is necessary to enable the country and developing countries in debt management, and guidance on good borrowing going forward.

1.3 PROBLEM STATEMENT.

The issue of Kenya's public debt has caused a stir in the public domain with many people trying to figure out whether the public debt as it is currently has a good or adverse effect on the economy. Kenya's current public debt is approximately 5.7 trillion Kenya Shillings.[11] This translates to 57.10% of the country's Gross Domestic product.[12] This means that the Country owes more than half of the value of its economic output. International Monetary Fund recommends that ratios of public debt to Gross Domestic Products for most developing economies should be at 40% and anything above that should be considered risky.[13] Kenya's Public debt is projected to increase to 6.09 Trillion Kenya Shillings by June 2020.[14] While as at August 2018 Kenya's external debt approximately amounted to (USD $ 26.9 Billion).[15]

[10]Supra n. 4
[11] Supra n.3
[12] https://www.centralbank.go.ke/publicdebt accessed on 13/02/2019
[13] Indermit Gill and Kenan Karakulah, 'Sounding the Alarm on Africa's Debt,' Future Developing, 2018 accessed at https://www.brookings.edu/blog/future-development/2018/04106/sounding-the-alarm-on-africa's-debt. accessed on 13/02/2019.
[14] The National Treasury, New annual Public Debt Management report 2018/2019.
[15] National Treasury on external debt.

The Constitution of Kenya gives the parliament the mandate to legislate and prescribe the terms on which the national government may borrow and impose reporting requirements.[16] It is through this mandate that the parliament passed the Public Finance Management Act of 2012. Under section 12(1) (b), (d) and (2)(K) the National treasury is mandated to manage the level and composition of national debt, national guarantees and other financial obligations of national government and develop a framework for sustainable debt control, mobilize domestic and external resources for financing national and county government budgetary requirements and likewise issue guidelines on financial matters.

Section 15 (4) of the Public Finance Management Act provides that the national treasury shall ensure that the level debt does not exceed the level specified annually in the medium term national government debt management strategy submitted in parliament and that the cabinet secretary of the ministry of finance shall submit report to parliament stating the loans balance brought forward, carried down, drawings and amortization on new loans obtained from outside Kenya or denominated in foreign currency and such other information as maybe prescribed by regulations.

Section 49(2) of the said Act gives the cabinet secretary of finance the authority of raising loans from within and outside Kenya on behalf of the national government. However, Section 50 (2), (3) and (5) provide that the National government may borrow money in accordance with the Act or any other legislation and shall not exceed a limit set by parliament and that only for the budget approved by parliament and the allocations for loans approved by parliament and finally that the

[16] Article 211(1)(a) of the Constitution of Kenya,

parliament shall provide for threshold for borrowing entitlements of national government and county government and other entities.

This is backed by Legal Notice number 34 of 2012, Public Finance Management (National Government) Regulations 2015, in regulation 26(1) (c) which provides that the national public debt shall not exceed 50% of the Gross domestic Product in net present value. This is equally buttressed by regulation 196 (1) which provided that pursuant to section 50 (2) of the Act, the debt limit at any given time shall not exceed the present value of the public debt that is determined in accordance with fiscal responsibility principles under regulations 26(1)(c) of these regulations. This was however amended by a motion of parliament moved by Hon Aden Duale seeking to increase the government of Kenya's external borrowing ceiling from 1.3 trillion to 2.5 trillion.[17] Subsequently in 2015, the Public Finance Management Act was amended parliamentary oversight role with regards to borrowing was removed giving lee way to increased external borrowing.[18]

Clearly there is a problem and a gap between the law and the application of the law since despite all these laws and provisions there is a ballooning public debt which is likely to soon put the country in debt distress.

1.4 RESEARCH QUESTIONS

a) What is the legal framework governing public debt acquisition and management in Kenya and whether it is efficient to deal with the phenomenon of the rising external debts?

b) What are the legal challenges attributed to the legal framework on external public debt in Kenya?

[17] Info.mzalendo.com/hansard/sitting/national-assembly/2014-12-09-14-30-00. Accessed on 25/02/2019

[18] Wanjohi Githae, Bill seeks to Curb Kenya's big appetite for borrowing,' Daily Nation, August 31 2018

c) What is the best practices in public debt acquisition and management in other jurisdictions?

d) What are the legal reforms required in acquisition and having sustainable public debts?

1.5 OBJECTIVES.

a) To examine the legal framework governing external public debt acquisition and management in Kenya.

b) To investigate the effectiveness of the current legal structure on external public debt in Kenya.

c) To draw the best practice in debt acquisition and management in other countries.

d) To propose legal reforms necessary in acquisition and management of debts.

1.6 HYPOTHESIS

This research is undertaken with the background that unsustainable borrowing in Kenya has been occasioned by:

a) Lack of adequate regulation to curb the runaway external public debt.

b) The failure in implementation and enforcement of the existing laws thus leading to the looming debt crisis.

1.7 THEORETICAL FRAMEWORK

This paper is based on three main theories: Virtue Ethics theory, sociological theory and legal positivism.

Virtue Ethics theory as propagated by Aristotle that human beings should lead flourishing lives.[19] It argues that it is the duty of legislation to ensure that citizens lead flourishing lives. Aristotle the

[19] P Koller, 'Law, Morality and Virtue' in Rebecca L Walker and Philip J (eds), 'Working virtue: virtue ethics and contemporary moral problems' (Oxford press 2007)191,192.

originator of virtue ethics, considered the achievement of human flourishing as the function of the law and government.[20]

Given that the current legal structure seems to have failed in the acquisition and management of foreign debt then the situation will definitely lead to misery to the citizens of the state as unstable debts lead to debt crises for countries. A country spending most of its revenue on paying off debts rather than development over burdens its tax payers leading to increased poverty levels. This thus inhibits the citizens of such a country from leading flourishing lives which is the main propagation of virtue ethics theory.

To this extent virtue ethics offer a theoretical underpinning for debt relief or legislative reform for sovereign debtors that are unable to meet their debt burdens thus enabling them to overcome their debt crisis.

Legal positivism as propounded by both Thomas Hobbes and John Austin which provide that states is perceived as creator and enforcer of the law and is equally vested with the power to punish for the disregard of law.[21] To this end the government is therefore mandated to come up with laws which would help to better public debt management and this laws should equally be backed by sanctions and incase of contravention then the government should be in a position to punish the contravener of the law and in this way the government may successfully overturn the looming debt crisis envisaged in our country.

This theory equally addresses the issue of laws having sanctions so as to ensure compliance by the citizens, to this end it is necessary that the laws on public debt should have clear definition on

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[20] CF Cimino, 'virtue and contract law,' L.Rev 88 (2009) 703,605.
[21] Michael Freeman FBA, 'Lloyd's Introduction to Jurisprudence,' 9th ed, Thomson Reuters, Legal td, London, 2014 pg 715-721.

offences under the act for example borrowing past the limits set by the law and equally outline the punishment for contravening the legislation.[22]

Lastly this paper is based on sociological theory of law, as propounded by Roscoe Pound that the law should change to meet the societal social needs and as such the law should change from time to time to handle the changes that have occurred in the society.[23] In our study it is clear that the law does not adequately address the twin issues of debt acquisition and management, thus leading to public debt distress and eventually public debt crisis. It is therefore necessary for legal reforms to be enacted to enable the laws to adequately address the crisis at hand thus the law playing its role of giving solutions to the problems of the society.

However, the critics of this theory are of the view that it is not the purpose of the law to try and fit within the social context of the society but it is the law that should guide on the social context of the society.[24] Also from a Marxist and Feminist point of view, the law is viewed as an instrument to bring balance and deal with injustices and not to provide gratification for societal social changes.[25] It is important to note that this theory borrows heavily from Socrates' ideology.[26] For example it equally believes on the idea of the law achieving practical results for the greater well of the society with happiness and good lifestyle being the determining factor in human choices.[27]

[22] Ibid
[23] Ibid
[24] Lepaulle Pierre, "The function of comparative law with a critique of sociological jurisprudence," Havard Law Review, Vol 1 35 no.7, (1992) pg 838-858
[25] Haris J.W, "Legal Philosophies (2nd Edition)London,": Lexis Nexis Butterworths, 1997
[26] Ibid no. 23
[27] Ibid

1.8 LITERATURE REVIEW.

Over the years, there have been legal reforms in Kenya with regards to public debt acquisition and management and numerous literatures have been published on the public debt of Africa and developing countries. Most of these literatures have looked at the public debt mainly in terms of acquisition and management of public debt from an economic point of view.

Maana, Owino and Mutai in their article Domestic Debt and its impact on the economy analyze the issue of development in public domestic debt in Kenya and its impact on the economy and gives recommendation on how to improve on domestic debt management in Kenya.[28] This paper mainly deals with domestic debt, which is the loan that acquires from institutions within its borders as such this book does not provide much insight with regards to foreign debts. However, it does not cover on the aspects of external debt as part of the public debt thus there is the gap with regards to research on external debt thus necessitating this research.

While other writers such as Missale Alessandro has researched on public debt management giving attention to the theories and evidence on public debt composition and debt returns.[29] He also brings out the effects of debt managements on financial markets, risk sharing, policy credibility, interest cost and taxation and evaluating them through a theoretical framework.[30] The analysis clarifies the tradeoff involved in policy decisions and shows how to use theory and evidence to answer to practical policy problems.[31] This research mainly focuses on how theories can be used in answering policy issues in public debts and how theories can be useful in managing public debts.

[28] Isaya Maana, Raphael Owino and Nahashon Mutai, 'Domestic Debt and its impact on the economy' 2011.
[29] Missale Alessandro, 'Public Debt Management,' Oxford University Press, (1999)9780198290858.
[30] Ibid
[31] Ibid

It however, does not focus on the legal reforms necessary in external debt in developing countries and in specific Kenya thus the need for this research to fill the information gap.

Bua, Pradelli and Presbitero also researched on public debt in low income countries.[32] They characterized the recent trends regarding low income countries domestic public debts and explored the relevance of different arguments put forward on the benefits and costs of government borrowing in local public markets.[33] Like other writers, this paper also focused mainly on the domestic debts and its effect on the low income countries, this research is closer to this current research only that it focuses on the domestic dept as opposed to the foreign debt which is our main focus and thus the reason for this research.

Trampusch in her research focused on the financialisation of sovereign debt through an in depth study of institutional changes in German debt management, conceptualizing these changes as institutional innovation.[34] She insists that the ministry of finance played a leading role in the reform process.[35] Through her research we get to understand necessary institutional changes necessary in public debt management but her research can hardly apply to our intended research area considering that German is a developed country and therefore her strong and well established financial institutions and debts cannot be compared to those of a developing countries for example Kenya. This research on the other hand is concerned with the legal infrastructure and the necessary reforms in Kenya which is a developing country which is not covered in trampusch's research.

[32] Giovanna Bua, Juan Pradelli, Andrea F. Presbitero, 'Domestic Public Debts in Low Income Countries: Trends and Structure.' Review of Development Finance 4 (2014)1-19
[33] Ibid
[34] Christine Trampusch, 'the Financialisation of sovereign debt: an institutional Analysis of the Reforms in Germany Public Debt Management' (2010) German politics, 24:2, 119-136.
[35] Ibid.

Carmen and Rogoff on the other hand did a research on how countries can have economical growth in time of debt.[36] In their book they have mainly concentrated on how developed countries more specifically USA can achieve economical growth despite their debts.[37] This does not apply to developing countries which find it very difficult to repay their huge debts and grow economically at the same time. Thus this research deals with Kenya which is a developing country and in particular our research is concerned with the necessary legal reforms to enable better management of external debt.

Montiel also did a research on public debt management and macroeconomic stability, linking public debt to macroeconomic.[38] In his research he explains on how to maintain public debt without affecting the Macroeconomic sector which he expounds that can easily be affected by public debt management. This article is not closely related to this current research as it majors on different aspect of public debt management. This current research, on the other hand seeks to contribute on the legal solutions on external debt as opposed to this montiel's research which is concerned with public debt and micro economics.

The Article on Public debt sustainability by Abbas is closer to our research as it analyses the condition of sub Saharan Africa.[39] In this article he majors on the role of domestic debt in sub Saharan African economy where he explains that most countries should now focus to domestic borrowing as a way of avoiding foreign debts but should balance the same so as to avoid negative

[36] Reinhart Carmen and Kenneth S. Rogoff, 'Growth in a Time of Debt,' American Economic Review (2010) 100(2)573-578.
[37] Ibid.
[38] Montiel J. P, 'Public Debt Management and Macroeconomic stability: An overview,' Oxford University Press journal (2005) 20:259-281.
[39] Abbas A.S.M, 'Public Debt Sustainability and Growth in Subsaharan Africa: The role of Domestic Debt.' GND Projects on Macroeconomics of Low Income Countries (2015).

effect on the economy.[40] The said Article does not focus on the same issues raised by our research which focuses on legal reforms in foreign debts in developing countries and in specific Kenya thus our research is important as it deals with a different aspect of public debt.

Panizza in his article discusses the relation between domestic and external public debt and how they affect the economy.[41] In this article one gets to understand the relation and balance between domestic and public debt in developing countries without one affecting the other.[42] The focus of this article is not close to what this research focuses on but it can guide on how to manage debts generally. Our research on the other hand deals with the legal reforms necessary to better public debt, this is a part not covered panniza's article.

Another article on public debt is the one by Presbitero which focuses on the public debt visa vis growth in developing countries.[43] It focuses mainly on how developing countries can maintain development while managing their debt and discusses the impact of debt on development and economy on developing countries. However, this research does not endeavor to handle the legal perspective of public debt and in particular external debts as envisaged in our research.

Lucia, Bulir and Rodriguez on the other hand have researched on the implication of debt relief on low income countries.[44] This article tackles debt relief in low income countries and how incentives lead to accumulated debt, boost consumption and reduce investment overtime.[45] The research

[40] Ibid n 28.
[41] Panizza U, 'Domestic and External Public Debt in Developing Countries' UNCTAD Discussion paper 188, United Nations Conference on Trade and Development 2008.
[42] Ibid
[43] Presbitero A, 'Total Public Debt and Growth in Developing Countries,' European Journal of Development Research (2012) 24 (4)606-626.
[44] Alma Lucia R, Ales Bulir and Jose Daniel Rodriguez, 'The Dynamic Implication of Debt Relief For Low Income Countries,' Review of Development Finance (2015) Vol 5 issue 1,p1-12.
[45] Ibid.

shows the effect of debt relief on the economy. However, it does not try to look into the external debt which is equally a major problem in many developing countries as such our research is necessary as deals with the legal reforms necessary for developing countries to better manage their public debt.

An article by Fosu explores the impact of a binding external debt servicing constraint on the sectoral composition of government expenditures in the economies of Africa.[46] The paper establishes that debt service burden adversely affects the share of public spending in social sector with similar impact on development.[47] It is different from this current research paper as it focuses on the impact of debt repayment on the economy of developing countries. This paper basically focuses on the economical perspective of public debt while our research concentrates on the legal aspects of external debt.

Lastly is an article by Onjala which discuses the link between external loans and debt challenges in Kenya.[48] This article examines the external debt situation in Kenya and how Chinese loans are likely to precipitate a crisis of sustainability.[49] This research basically gives the dire situation facing the Kenyan economy with regards to external debts, as opposed to our research which is concerned with the legal solution to the external debt problem in Kenya and other developing countries.

From the above discussed literatures, it is clear that most writers look at the economical effect of public debt but fail to pay attention to the legal reforms necessary in acquisition and management

[46] Fosu, Augustin Kwasi, 'The External Debt Servicing Constraint and Public Expenditure Composition: Evidence from African Economies,' Wider Research Paper (2007)36
[47] Ibid.
[48] Ibid n 5.
[49] Ibid.

of external debts thus necessitating this research which focuses on the legal angle of public debt and in particular the necessary legal reforms required.

1.9 JUSTIFICATION OF THE STUDY

It is without doubt that the issue of public debt is a major problem to most developing economies in the world. Most writers have looked at the issue of public debt from the sociological and economical angle. It is therefore necessary to look at the public debt challenge from a legal perspective and come up with the necessary reforms required in acquisition and management of public debt.

This research would equally look into and give a recommendation as to whether the nine trillion carping of the public debt is good or detrimental to the country.

The following institutions may benefit from this research, the government of Kenya, the policy makers, Ministry of finance, future research in this area.

1.10 LIMITATIONS.

This research is basically qualitative as it is based on existing materials and does not base its findings on quantitative data.

This research does not equally bring out the relationship between governance and the external public debt. It is mainly concerned with the role legislation plays in the external public debt this leaving out the governance angle which would have delved into issues such as corruption which has equally helped in compounding the external debt problem.

1.11 METHODOLOGY

This research undertakes a mixed research approach of doctrinal analysis of core, subsidiary and related legislation on external public debt and primarily relies on qualitative analysis and looking at best practices in other jurisdictions.

It will particularly focus on opinion based data and recommendation of previous researchers. This is important to our research which focuses on the existing legislation and secondary sources to come up with an appropriate solution in our research problem.

Data will be collected from both primary and secondary source. And the secondary sources will include review of literature from other authors, World Bank reports, international monetary fund reports and previous research studies related to this topic. Existing international and national laws and declarations will also be used.

1.13 CHAPTER BREAKDOWN

Chapter 1 gives an introductory background to the study and presents the problem surrounding the public debt in Kenya and highlights the laws affecting external public debt in Kenya. This chapter also lays the theoretical framework behind the study and reviews literature from various sources to provide an insight into the external public debt menace.

Chapter 2 gives an insight on the historical development of external public debt in the world perspective and then narrows down Africa and lastly to Kenya, It equally brings out the changes in terms of Kenya’s debt composition from colonial era to date.

Chapter 3 looks at Kenya’s Legal Framework and its institutional framework on public debt and in particular external public debt and literature on sound debt acquisition and management. It equally gives the weaknesses of the legal and institutional framework.

Chapter 4 looks at a best practices Kenya, may borrow from Nigeria and New Zealand with regards to their legal and institutional framework on external debt.

Chapter 5 deals with findings from the research and equally gives conclusions and key recommendations from the study.

CHAPTER TWO

2.0 EXTERNAL PUBLIC DEBT AND ITS HISTORICAL DEVELOPMENT IN THE WORLD AND KENYA

This chapter brings out the concept of external public debt and narrows down to foreign debts, its historical development and the general legal framework on foreign debt.

2.1 Historical Development of Foreign debt in general.

There are three possible definitions that can be used to define foreign debt. The first focuses on the currency in which the debt is issued, the second focuses on the residence of the creditor and the third focuses the place of issuance and the legislation that regulates the debt contract.[50] However the first definition of foreign debt has been ruled out to be inappropriate because several countries issue foreign currency denominated debt in the domestic market, moreover, this definition is problematic for countries that adopt the currency of another country[51] a good example is South Sudan using the dollars currency. The definition of foreign debt that is preferred in the world over is the second and third which focuses on the residence of the creditor and the laws governing the debt contract.[52]

It should be noted that borrowing from both foreign and domestic sources; tax and grants and withdrawal from current cash balances are the major sources of the government funding. The concept of external borrowing to fund its projects and expenses is not a new concept in the world and dates back to the ancient days.

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[50] Panizza Ugo G., 'Domestic and External Public Debt in Developing Countries,' United Nations Conference on Trade and Development Discussion (March 2008) paper No. 188. Accessed at https://ssrn.com/abstarct=1147669 accessed on 13th May 2019.

[51] Ibid.

[52] The External Debt Statistics: Guide for Compilers and Users jointly Published by the BIS, Eurostat, IMF, OECD, Paris Club, UNCTAD and the World Bank.

From the religious perspective borrowing of any kind was condemned as it involved interest which is condemned by the Bible and the Quran teaching that no one should lend expecting anything in return.[53] Public borrowing was equally seen as unnecessary and evil by the early philosophers for example Thomas acquinas who condemned debt as sinful and wasteful[54] and that a government should finance its expenditure without borrowing. As such public borrowing was difficult at this time.

It should be noted that foreign debts in the ancient times were different from the current form of borrowing, it involved the borrowing in form of commodities, was mostly short term and was used to fund wars,[55]for example the ancient Greece would borrow from temples to finance wars.[56]It was not until the 12th century that public borrowing which was secured by future interest was introduced in Italian cities.

The first recorded instance of discernible foreign borrowing was when Athens' interim government borrowed 100 talents from the victorious Spartans, following the Peloponnesian war and when Athens democratic government assumed power, it owned the debt incurred by the interim government and repaid Spartans in full.[57] Prior to this loan Athens had borrowed from the first Delian league and the amount borrowed accounted for 40% of the public spending but Athens

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[53] Aaron Krischenbaum, 'Jewish and Christian Theories of Usury in the Middle Ages,' Jewish Quarterly Review 270 (1985)58.

[54] Ibid

[55] Richard M Salsman, 'A Brief History of Public Debt' in Nicholas J Theocarakis, 'The History of the Political Economy of Public Debt,' (4th ESHET Latin America conference, Belo Horizonte- Brazil,19-21, 2014)

[56] Nicholas J Theocarakis, 'The History of the Political Economy of the Public Debt,' (4th ESHET Latin America conference, Belo Horizonte- Brazil,19-21, 2014)

[57] Thad A. Titze, 'We're all Ancient Greeks Now When it Comes to debt,' History News Network, The George Washington University Press (2007). Accessed at https://historynetwork.org/article/150063. Accessed on 14/5/2019

defaulted during the devastating pelonnesian war which strained both tax and silver mining revenues while simultaneously necessitated increased spending.[58]

On the other hand Roman republic lived on the spoils of war and a tax system with low levels of direct taxation, the Romans avoided public debt and instead accrued surpluses during relatively peaceful times to finance impending war but this died with the empires and public borrowing re-emerged in the medieval times.[59]

Foreign debt in modern state and public finance originated in the 17th century during the financial revolution and the enlighten age. Issuance of debts equally led to cases of default by the borrowing countries for example during the American Revolution, the new state government repudiated the bills of credit issued by the former colonial government and defaulted in many credit obligations.[60] At four periods during the last two centuries, over 40% countries were in default or debt rescheduling, thus leading to the creation of International Monetary Fund in 1944 to buoy foreign lending and development, however it should be noted that since the emergence of IMF foreign debt continues to swell in many countries.[61]

More recently Argentina defaulted on its $82 billion debt in 2001, Ecuador defaulted on a $ 3.2 billion in 2008, Jamaica defaulted on a debt of $7.9 billion in February 2010 while Greece recorded the largest sovereign debt default in history of up to $ 138 billion in March 2012,[62] and Kenya may

[58] Ibid.
[59] Ibid.
[60] Supra n. 73
[61] IMF, Sovereign Debt Restructuring Recent Developments and Implication for the Legal and Policy Framework 6, (2014). Accessed at https://www.imf.org/external/np/pp/eng/2013/042613.pdf accessed on 14/5/2019
[62] Ibid.

soon join the defaulters list if it does not take appropriate measures to ensure that it curbs the runaway borrowing tendencies it has been engaging in.

In history debt defaulters were treated harshly, it was considered morally and legally indefensible to default on one's debts and such a debtor was considered a thief,[63] this may have informed the drafting of Section 40 of the Civil Procedure Act.[64] Creditors to sovereign debtors employed military force to demand payment on the loans extended.[65] The military forces was not limited to blockading, invasion and cannonading of default nations a good example being in 1902 when a number of European states employed naval blockades and gunboats in order to force Venezuela to pay up its debts.[66]

Another instance when military force was used was in reference to the United States president Theodore Roosevelt's interventionist policy that aimed at policing other states so as to protect European investors.[67] It did this by leveraging on its regional power so as to ensure that sovereign debts owed to European investors by countries in Central America and the Caribbean were honored, this was referred to as the Monroe doctrine.[68] However, the use of the military force to enforce sovereign debts gradually wore off after Latin American states began claiming sovereignty and equality of states in international law, a principle that demanded non intervention, this led to

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[63] L H White, 'Bankruptcy as an Economic Intervention,' Journal of Libertarians Studies 281, 282 (1997)
[64] Cap 21 Laws of Kenya.
[65] As Hershey, The Calvo and Drago Doctrines,' The American Journal of International Law 40 (1907). Accessed at https://www.jstor.org/stable/pdf/2186283.pdf?=1459135969251 accessed on 14/5/2019
[66] DG Munro, ' Intervention and Dollar Diplomacy in the Caribbean 1900-1921,' Princenton University Press 67
[67] K J Mitchener and M Weidenmier, ' Empire Public Goods and the Roosevelt Corollary,' The Journal Of Economic History 658 (2005). Accessed at https://www.jstor.org/stable/pdf/3875013.pdf?=1459138417999 accessed on 14/5/2019
[68] Ibid

the signing of the Hague peace conference treaty of 1907 by creditor states which signaled the end of use gunboat diplomacy and other military measures in debt enforcement.[69]

More recently creditor countries have resorted to taking and running debtor countries assets for a period of time where there is default in payment of loans a good example being Sri Lanka that handed over its Port to be managed by China for a period of 90 years because it Sri Lanka defaulted on its loan obligations.[70] These are some of the dangers Kenya stands to go through if they fail to avert the ever impending debt crisis it faces.

Equally Africa's international indebtedness has grown dramatically from independence, by 1970 most countries in Africa had attained freedom and by the end of the said year, the total African external debts were US$ 6 billion; the lowest estimate for 1985 would suggest a continental total external debt of US$ 82 billion.[71] In relation to GDP Africa's debts are the heaviest in the world. The Estimates of the level of African indebtedness have continued to rise and by 2000, Africa's debt was estimated to be over US$600 billion.[72]

Africa's rising debt has been a subject of heated debate in both local and international circles, and both in the policy and academic spheres. Already, multilateral financiers such as the World Bank and the International Monetary Fund have sounded alarm bells that the continent is hurtling towards the abyss with its growing debt burden.[73] Concerns about the current debt situation in Africa, it would seem, are in part informed by Africa's past debt overhang problems. Between the

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[69] F C Hicks, 'The Equality of states and the Hague Conference,' The American Journal of International Law 530 (1908) 2(3). Accessed at https://www.jstor.org/stable/pdf/2186330pdf accessed on 14/5/2019
[70] Supra n. 4
[71] Trevor W. Parfitt and Stephen P. Riley, 'The African Debt Crisis,' Routledge Library Edition: Development (2013)
[72] Ibid
[73] Njuguna Ndung'u, 'Rising debt to GDP Ratio In Africa: Cause for concern or a non Issue?' African Economic Research Consortium, December 2018.

1980s and early 2000s, many African countries accumulated large amounts of debt, which resulted in a debt burden that negatively impacted on economic growth, exacerbating poverty and underdevelopment among these countries.[74] This experience created the impetus for the Highly Indebted Poor Country and Multilateral Debt Relief initiatives through which the creditors forgave the debt owed by these countries.[75] Most of the countries then on the road to debt forgiveness swore never again to be such a position. It is largely through this lens that the current debt situation in Africa is being monitored and assessed.[76] However, that has not been the case and developing countries such as Kenya have continued to borrow heavily and continue to put their countries in precarious situations with regards to external debt as such there is even stronger need of having sound public debt management system.

2.2 Historical Development of External Debt in Kenya

Kenya's external debt can be traced back to post independence period in the beginning of the settlement schemes when the whites were being compensated for their lands they were leaving after Kenya had gained independence. By middle of 1969 the settlement programme had cost over £29 million of which £ 14million was borrowed abroad provided by the Britain government, the commonwealth development corporation and the World Bank.[77] By 1969, £12.5 million had been paid to the Europeans for the purchase of the land but still more debt was owed to the colonialists for the lands. By 1970 the total outstanding interest towards the settlement scheme was £ 3.1 million a sum equivalent to roughly a third of the settlers total original debt of the time.[78]

[74] Ibid
[75] Supra n 90
[76] Ibid
[77] Colin Leys, 'Under Development in Kenya, The Political Economy of Neo- Colonialism 1964-1971,' University of California Press Berkley and Los Angeles (1975)
[78] Ibid

British government on sensing that Kenya may fail to repay the loan advanced to it, sponsored the stamp mission in 1965 led by Van Arkadie to find out the financial viability of the re-buying of land project and whether the country would pay up the debt owing to the British government.[79] After their investigation one of their recommendations was that the common wealth development corporation and the World Bank should be rescheduled to allow the actual rate of repayment by settlers' arrears should be accepted without strain by the Kenyan government and that the interest from the loan, however, by 1970, the recommendations had not been implemented and Kenya still owed debt arising from the settlement scheme project.

Another loan received by the government of Kenya was used to facilitate registration of land, the government of Britain issued a loan of £ 3.4 million to facilitate the registration process and this was to help enable the registered people to access loans from banks using their land as collateral.[80]

As at 1990 Kenya had and external debt of $ 6.8 billion of which 70% was long term credit to the public sector or publicly guaranteed credit to quasi-public institutions.[81] During the 1990s Kenya's economy fell into recession leading to shortage of foreign exchange and the government for the first debt crisis.[82]In 1993, the public debt to the GDP was at 131.8%.[83]

By the end of 2002 Kenya's outstanding stock of external debt, including arrears amounted to US$ 5.1 billion being 49% of the GDP, of which US$ 3.9 billion was on concessional terms. The

[79] Supra n 88
[80] Ibid
[81] Benno J. Ndulu and Francis W. Mwenga, 'Economic Adjustment Policies (1994) in Joel D. Barkan, 'Beyond Capitalism Vs. Socialism in Kenya and Tanzania,' Lynne Rienner Publishers (1994)
[82] Kenya Debt Relief Network (KDRN), 'Kenya's Public Debt Crisis: An Overview of the Current Status, Insight
[83]Ibid

external debt comprised of 57.5% owed to official multilateral creditors, while debt to official bilateral and commercial creditors accounted for 32.2% and 8.5% respectively.[84]

External debt for Kenya has shown an upward trend ever since from the first debt. Recently external debt has increased from 21.7% of the GDP in 2007 to 29.8% in 29.8% in 2017 and in the same breadth, the bilateral debt category increased from Kshs 141 billion (35.3% of the total external debt in 2007) to Kshs 670 billion (38.9% of the external debt) in 2017.[85]

Kenya's lending countries with leading outstanding national debts as at 2017 were China, Japan and France wit Kshs 478.6 billion, Kshs 91.5 billion and Kshs 63.3 billion respectively, this translated to 66.2%, 12.7% and 8.8% of the total bilateral debts, however, this is a change from 2007 when the leading bilateral creditors were Japan at Kshs 66.2 billion, 46.7% of the bilateral debt; followed closely by France at Kshs 18.9 billion, 13.3% of total bilateral debt and then Germany at Kshs 13.5 billion, 9.5% of the total bilateral debt while Kenya owed China Kshs 3.1 billion, 2.2% of total bilateral debt in 2007.[86] The stock of debt from china started rising steadily in 2011 and has grown over time due to continued bilateral agreements in infrastructural developments in Kenya.

As early as 1987, Kenya was receiving support from china for example the loan that was used to construct the Moi International sports Complex approximately Kshs 1.16 billion.[87] In 2006 china extended to Kenya concessional loans and grants under the agreement on economic and technical cooperation which included the northern and eastern by pass road projects for Kshs 8.5 billion

[84]Anupam Basu and Anthony R. Boote, IMF, Staff Country Reports, December 2003. No 03/400.
[85] Policy Monitor, Supporting Sustainable Development Through Research and Capacity Building (July- September 2018) Issue 10 No. 1
[86] Ibid
[87] Supra no. 5

and Kshs 2.16 billion respectively.[88] The funding was from external import bank of China (chexim) while the implementing contractor was the china road and bridge corporation (CRBC).[89] China also extended loan to Kenya for building of the Standard Gauge Railway from Mombasa to Nairobi but recently declined to give another loan to extend the standard gauge railway from Nairobi to Naivasha[90]

The fear has been that Chinese debt poses a threat to Kenya because the loan agreements are not transparent, projects are not well prioritized, accounting procedures are weak and it is not clear what the projects are costing.[91] On top of that, most Chinese loans are conditional on Kenya's acceptance of Chinese contractors, this limits the loan's development impact through potential technology transfer which could improve the country's productive capabilities and in turn its future ability to comfortably absorb the debt burden.[92]

The bilateral loans between Kenya and China have led to the concern on whether Mombasa port was used as collateral in securing loans from China.[93] This was however, disputed by the President, Uhuru Kenyatta while addressing a round table interview on the state of the nation in December 2018.

The commercial loans in external debt has risen from Kshs 574 million representing 0.1% of total external debts stock to Kshs 634 billion in 2017 representing 29.4% of total external debt.[94]

[88] Supra n 104
[89] Ibid
[90] Aggrey Mutambo, "Why China refused to Finance railway it initially Backed,' Daily Nation News Paper, April 27, 2019
[91] Supra n. 5.
[92] Ibid.
[93] George Omondi, 'Mombasa port at risk as audit finds it was used to secure SGR loan,' The East African, December 20 2018. Accessed at https://www.theeastafrican.co.ke/business/mombasa-port-sgr-default-china/2560-4903360 accessed on 14/2/2019
[94] Ibid

Likewise multilateral debt increased from Kshs 240 billion in 2007 to Kshs 840 billion in 2017, as at 2007 multilateral debt accounted for 61% of total external debt, this reduced to 31% in 2017.[95]

Borrowing through syndicated loans and issuance of Eurobond has increased the share of commercial loans in Kenya's external debt mix.[96] In 2014, Kenya issued her first Eurobond in London stock exchange and raised Kshs 202 billion, the second Eurobond was issued in February 2018 and raised Kshs 203 billion[97] to be paid in two tranches but the said amount would earn an interest of Kshs 323 billion as interest.[98] And recently in 2019 Kenya issued another Eurobond for Kshs 210 billion to repay its debts.[99] It is a short term loan which is slightly more expensive than the other two Eurobond loans. The loan is to be paid in two tranches of 7 percent for the portion of the loan whose repayment will start in 2023 and 8 percent for the other half that matures starting 2028.[100] Part of the Eurobond loan will be used to pay $750 million plus a final interest of Kshs 2.2 billion will be paid to the lenders of the 2014 debut Eurobond.[101] This means that the proceeds from the debt were not earmarked for a specific capital project thus the fears that part of the loan is to offset other due loans.[102]

This year alone Kenya will pay close to Kshs 100 billion in interest payments on foreign loans while clearing maturity debts estimated at Kshs 380 billion.[103] If a country uses loans to repay its due debts, no wealth is created and it might struggle to repay debts in future. This leads to falling

[95] Supra n 102
[96] Ibid
[97] Supra n. 16
[98] Ibid
[99] Moses Michira, 'A third of Kshs 210 billion Eurobond to repay debt,' The standard Newspaper, May 17, 2019
[100] Ibid
[101] Ibid
[102] Ibid
[103] James Anyanzwa, 'Bleak 2019 For Tax Payers as Kenya Begins Repaying Loans,' The East African, January 7 2019 accessed at https:www.theeastafrican.co.ke.business/bleak-2019-for-taxpayers-as-kenya-begins-repaying-loans/2560-4923632 Accessed on 14/2/2019.

of its credit rating, lenders and investors would then demand a higher interest rate to compensate for the risk that they will lose their money, this makes it costly to repay new debts which might be what Kenya is facing if the rates charged on the 2018 Eurobond is to go by.[104]It should also be noted that the interest rates charged by investors are higher for sovereign bonds issued by governments in Sub-Saharan Africa. The unexplained 'Africa Premium' is about 2.9% this is after considering the relevant facts like period of issue, the credit ratings of issuers and macroeconomic fundamentals.[105] Thus by resorting to international markets Kenyans are paying dearly for their loans.

Another issue is that huge foreign government debts are in foreign currency thus increasing the risk to the country. Principal and interest repayments on external debts are made in foreign currency.[106] This depletes the country's foreign exchange reserves and may devalue the domestic currency.[107] In short term, a weak domestic currency makes a country's exports more competitive, however, a weak currency can lead to high inflation rates in the long term because it costs the country more to import what it needs for consumption, this inflationary effect is bad for a country like Kenya which imports more goods and services than it exports.[108]

In 2017, the World Bank stated that Kenya's economic growth was decelerating and recommended that credit access could be supported by reducing public sector borrowing and transactions cost for accessing credit through better credit reporting.[109] As if this is not enough in 2018, International

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104 Supra n.18.

105 Michael Olabisi and Michael Howard Stein, 'Sovereign Bond Issue: Do African Countries pay more to borrow?' Journal of African Trade, Vol 2 Issue 1-2, December 2015. Pgs 87-109. Accessed at https:www.sciencedirect.com/science/article/pii/522148515000079 accessed on 14/2/2019.

106 Supra n.22

107 Ibid

108 Ibid.

109 World Bank, 'Kenya's Economic Outlook to dip in 2017,' Press Release, 12 April 2017. Accessed at https://www.worldbank.org/en/news/press-release/2017/04/12/kenya's-economic-outlook-to-dip-in-2017.

Monetary Fund representatives before the National Assembly's budget and appropriations committee informed the committee that the Kenyan public debt was worrying and if no caution was heeded the public debt would reach unsustainable heights.[110] Private financial experts have equally had their say in this matter, for example cytonn investments has indicated that Kenya's public debt will hit a crisis if the country fails to invest in projects with high returns to enable the government repay its debts.[111]

Recently in 2018 Moodys investor services downgraded Kenya's credit score to B2 from B1 but assigned a stable outlook, implying that the probability of the governments defaulting on its loan obligations is increasing and that new loans would attract higher risk premium.[112] To exacerbate matters, recently the International Monetary Fund withdrew Kshs 100 billion standby facility that was available to the country in case the shilling depreciated.[113] Though the Central Bank of Kenya argues that the shilling does not IMF guarantee to be strong but the ripple effect of withdrawal of the standby facility cannot be down played as it will go a long way into affecting the interests on loans acquired by the country.[114]

Reckless borrowing by different government entities marred with corruption in different sectors in the government leading to loss of money led to the issuance of different circulars giving directions on how money should be spent on projects. The first of such circulars was issued in 2018 that the Treasury had the mandate to mobilize external resources which include loans and grants and that all negotiations for external resources must be held under the guidance of the

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[110] Supra n. 35
[111] Cytonn investments, 'Kenya's Public debt, should we be concerned?' Nairobi commercial office Report, February 12 2018.
[112] https:www.moodys.com/credit-ratings/kenya-government-of-credit-rating-806356852 accessed on 15/2/2019.
[113] Brian Ngugi, 'CBK now says shilling does not need IMF guarantee,' Business Daily, Tuesday 31,2018.
[114] Ibid.

National Treasury.[115] The said circular also provided checklist of mandatory requirements that must be provided before seeking external financial support which are that; feasibility study report must be inspected and approved by the relevant government entity informing the project's viability, cost and design; confirmation of the land and way leave acquisition for the project and the resettlement Action plan should be presented if necessary; commitment to relocate public utilities like electricity line, sewer line among others where necessary; confirmation of adequate human resources for project implementation and where there is shortfall, the implementing ministries , department agencies and county governments must commit to develop a strategy to fill the gap; prioritization and commitment of the counterpart funding by all ministries, departments and agencies and county governments where necessary; due diligence report to ascertain the financial, technical and legal competency for the firm procured competitively to undertake the project implementation.[116] These were to ensure that money is not wasted through projects which are not economical and to try and curb on rising corruption in government projects.

To curb on borrowings by other local entities without approval by the national treasury another circular was issued providing that all memorandum of understanding and commercial contracts which local and foreign parties are to receive the concurrence of the respective cabinet secretary and approval of cabinet prior to execution. The commercial contracts and memorandum of understandings must also receive concurrence from the national treasury and the office of the Attorney General and department of justice on tax exemption and legal clearance respectively.[117]

[115] Treasury Circular No. 12/2018 of October 29, 2018
[116] Ibid
[117] Cabinet circular by the Head of the Public Service Ref. OP/CAB.39/1 of March 1, 2018.

It is critically important that our development agenda be funded in a coordinated manner and within the constitution and stipulated laws.

2.3 Conclusion

It is clear that there has been switch from concessional to non-concessional sources, including bilateral and commercial creditors as well as international bond markets which have generally worsened the debt situation. The rate at which the government is borrowing has raised public outrage and fears that the country is moving towards unsustainable path. It is equally clear that debt is necessary in any economy for example in the Kenyan economy, the debt raised has been used for funding different development projects which are necessary in the country.

It is also evident that borrowing is a necessary evil that any society must have, however, it is important for Kenya to have sound legislation to curb the runaway borrowing experienced in the country and to equally manage public debt with an aim of reducing the public debt to healthy levels.

CHAPTER 3

3.0 LEGISLATIVE FRAMEWORK AND INSTITUTIONAL FRAMEWORK ON FOREIGN DEBT IN KENYA

3.1 Introduction

In Kenya the laws governing public debt are the constitution, the Public Finance Management Act, The Public Finance Management (National Government) Regulations 2013 and Public Finance Management (County Governments) Regulations 2015. Various institutions have also been established to manage debt management including foreign debts. This Chapter gives insight on the legislative and institutional framework on foreign debts.

3.2 Legislative framework

In this part we will discuss into details the Constitution, the Public Finance Management Act and the general rules and regulation on foreign debt in Kenya and their relation to the current ballooning Public debt in Kenya.

3.2.1 Constitution of Kenya

The Constitution of Kenya is the supreme land and gives the guidelines with regards to foreign debt. The Constitution provides for two levels of governments; the national governments and the devolved government. Article 211(1) gives guidelines on how the parliament through legislation, prescribe the terms on which the national government may acquire loans.

The devolved government has no power to borrow unless the loan is guaranteed by the national government and with the approval of the county government's assembly. Article 214 of the Constitution defines public debt to mean all financial obligations attendant to loans raised or guaranteed by the national government, this includes foreign debt. The public debt is a charge on the consolidated fund but it may be charged to other public funds.

The Constitution of Kenya also establishes the judiciary, executive and legislature each with a role to pay in Public finance. It equally establishes the national government and devolved level of governments each with specific powers with regards to public borrowing and including foreign borrowing.

The legislature has power over public finance such as exercising oversight over revenue and its expenditure and enacting of legislation. The challenge has been how to balance between the roles of the executive and legislature to avoid friction in the management of public debt.[118]

The Constitution also establishes institutions such as the Central bank of Kenya, controller of budget and auditor general.[119] They are established to provide guidelines on public debt. The controller of budget has the role of overseeing the implementation of the budgets of the national and county governments by authorizing withdrawals from public funds, the auditor general has the mandate to audit and report within six months of financial year public debt, confirm whether or not public funds have been properly used and the central bank has many roles including monetary policy, promoting price stability and performing other tasks conferred to it by the Act of parliament.

It is important to note that the guidelines provided have not been adequate to curb ballooning debt in Kenya if the news on the media all over the world is anything to go by. However, we should not forget that the constitution is a document with many dimensions and it is only important for giving guidelines but the detailed provisions on public debt should be done by specific legislation.

[118] Ally Jamah, 'Parliament has failed to check growing public debt,' Standard Digital, November 18, 2017. Accessed at https://www.standardmedia.co.ke/article/2001260504/parliament-has-failed-to-check-growing-public-debt accessed on 20/05/2019

[119] Articles 231,228 and 229 of the Constitution of Kenya.

3.2.2 The Public Finance Management Act

This is the main legislation that deals with public debt both in the national and the devolved government. The Act is supported by the Public Finance Management (National Government) Regulations and Public Finance management (County Governments) regulations.

The Public Finance Management Act establishes the National treasury pursuant to Article 225 of the Constitution.[120] The National treasury is mandated to formulate, implement and monitor macro-economic policies involving expenditure and revenue; manage the level and composition of national public debt, national guarantees and other financial obligations of national government and develop a framework for sustainable debt control; mobilize domestic and external resources for financing national and county government budgetary requirements; design and prescribe an efficient financial management system for the national and county governments to ensure transparent financial management and standard financial reporting and that the National Treasury shall prescribe regulations that ensure that operations of a system under this paragraph respect and promote the distinctiveness of the national and county levels of government; monitor the financial aspects of risk management strategies and governance structures for the national government and national government entities; issue guidelines to national government entities with respect to financial matters and monitoring their implementation and compliance.[121]

The national treasury shall manage the national government's public finances in accordance with the constitution and the principles of fiscal responsibility principles which include, that the public debt and obligations shall be maintained at a sustainable level as approved by Parliament for the national government and the county assembly for county government; over the medium term, the

[120] Section 11 of the Public Finance management Act.
[121] Section 12 (1), (2) of the Public Finance Management Act

national government's borrowings shall be used only for the purpose of financing development expenditure and not for recurrent expenditure; the National Treasury shall ensure that the level of National Debt does not exceed the level specified annually in the medium term national government debt management strategy submitted to Parliament; short term borrowing shall be restricted to management of cash flows and in case of a bank overdraft facility it shall not exceed five per cent of the most recent audited national government revenue.[122]

Section 49 (1) (2) of the said Act gives the cabinet secretary of finance the authority of raising loans from within and outside Kenya on behalf of the national government. The national government may from time to time borrow within and outside Kenya such sums of money in such amount and on such terms and conditions as to interest, repayment, disbursement or otherwise as the Cabinet Secretary may think fit and the cabinet secretary can borrow; by issuing external government securities; by issuing treasury Bills or treasury Bond or stock; by advances from Central Bank of Kenya; by bank overdraft on exchequer account or any other public account and by any other loan or credit evidenced by instruments in writing.[123]

However, Section 50 (2), (3) and (5) provide that the National government may borrow money in accordance with the Act or any other legislation and shall not exceed a limit set by parliament and that only for the budget approved by parliament and the allocations for loans approved by parliament and finally that the parliament shall provide for threshold for borrowing entitlements of national government and county government and other entities. This is backed by Legal Notice number 34 of 2012 and that the national public debt shall not exceed 50% of the Gross domestic

[122] Section 15 of the Public Finance Management Act
[123] Rule 187 (1), (2) of the Public Finance Management (National Government) Regulations 2015

Product in net present value.[124] This is equally buttressed by regulation 196 (1) which provided that pursuant to section 50 (2) of the Act, the debt limit at any given time shall not exceed the present value of the public debt that is determined in accordance with fiscal responsibility principles under regulations 26(1)(c) of the regulation.

The Parliament is entitled to approve for the thresholds for borrowing entitlements of the national government, county governments and their entities and this is in line with the relevant regulations.[125] The Public debt incurred by the national government is a charge on the consolidated fund or other pubic fund.[126] The Cabinet Secretary in charge of national treasury is also to ensure that the proceed of any loan raised are paid into the consolidated fund or into any other public fund established by the national government or any of its entities as the Cabinet Secretary may determine in accordance with the regulations approved by government.[127]

The Act equally gives option for the national government entities to borrow loans. Such entities are required to seek the approval of the cabinet secretary in charge of national treasury, for its intended program of borrowing, refinancing and repayment of loans. The national entities are also required to obtain the cabinet secretary's approval before making changes to its program for borrowing, refinancing and repayment during a financial year.[128]

Under section 51 (1) of the Act, the cabinet Secretary in charge of national treasury is authorized to execute loan documents for borrowing by the National government or a person designated by the Cabinet secretary. The Public Finance Management Act was recently amended to give the

[124]Rule 26 (1)(c) of the Public Finance Management (National Government) Regulations 2015
[125] Section 50 of the Public Finance Management Act
[126] Supra n 124
[127] Ibid
[128] Section 51 of the Public Finance Management Act

cabinet secretary the discretion to raise loans and issue external government securities in such a manner as he may determine but it has to be within the borrowing limit set by the Parliament.[129]

The authority to raise loans by the Cabinet secretary in charge of national treasury includes authority to raising external government loans and the external loan documents can be executed by the cabinet secretary in charge of treasury, a delegate appointed by the cabinet secretary in writing and a borrowing agent appointed in accordance with section 50(9) of this Act.[130]

The Act establishes the office of the public debt management office within the national treasury mandated to; carrying out the government's debt management policy of minimising its financing cost over the long-term taking account of risk; maintaining a reliable debt data base for all loans taken by the national government, county governments and their entities including other loans guaranteed by the national government; prepare and update the annual medium-term debt management strategy including debt sustainability analysis; monitor and evaluate all borrowing and debt-related transactions to ensure that they are within the guidelines and risk parameters of the debt management strategy; transact in derivative financial instruments in accordance with best international practices benchmarked to the debt management offices of other governments that are internationally respected for their practices; prepare and implement the national government borrowing plan including servicing of outstanding debts and many more roles as will be discussed while discussing institutional framework.[131]

The government is also authorized to lend money but only in accordance with terms and conditions prescribed by the regulations approved by Parliament.[132] A national government entity may lend

[129] Section 53A (2)(3) of the Public Finance Management Act
[130] Section 53A (5)(6) of the Public Finance Management Act
[131] Section62 and 64 of the Public Finance Management Act
[132] Section 57 of the Public Finance Management Act

money only if authorized to do so by an Act of Parliament and in accordance with terms and conditions prescribed in regulations.[133] Money loaned under this section is payable only from an appropriation for development expenditure or from some other authority approved by Parliament for the purpose for which the loan is made.[134] The Cabinet Secretary is to ensure that a security given in respect of a loan under this section is given in the name of the national government.[135]

The Cabinet Secretary may on behalf of the national government carry out any of the responsibilities and exercise any of the powers of the national government with respect to securing a loan granted by the national government.[136]

3.2.3 Public Finance Management (National Government) Regulations 2015

This is the set of regulations that give the details on how National Public debt is carried out, including external debt. The regulation provides that the fiscal responsibility principles that helps in management of public finances include, the national public debt shall not exceed 50 percent of Gross Domestic Product in net present value terms; the annual fiscal primary balance shall be consistent with the debt target.[137]

The regulations provide that the borrowing by the government shall be guided by the principles that, promotion of inter-generational equity in the sharing of burdens and benefits of public borrowing; need to ensure stability of domestic financial markets; determination of thresholds of borrowing rights for both levels of government; use of objective criteria for evaluating national

[133] Ibid
[134] Ibid
[135] Ibid
[136] Supra n.135
[137] Regulation 26(1) of the Public Finance Management (National Government) Regulations of 2015

government entities or county government eligibility for national government debt guarantee; and prudence and equity in setting limits for debt stock levels for each county government.[138]

The regulations also provide for policy frameworks in the public debt management and it shall comprise of the medium term debt management strategy.[139] All loans incurred by the national government shall be informed by the medium term debt management strategy which shall be reviewed annually, prepared and executed by the public debt management office in accordance with the delegated authority by the cabinet secretary in charge of national treasury.[140] The medium term debt management strategy shall be formulated annually on a three year rolling basis and the strategy shall be approved by the cabinet.[141]

The medium term debt management strategy shall be prepared taking into account, the borrowing needs of the republic of Kenya; prevailing macro- economic conditions; prevailing conditions of the financial markets; and shall entail minimizing borrowing costs with a prudent degree risk.[142]

The regulations also provide that the negotiations with foreign governments and agencies for external loans shall be formalized into a recognized instrument for example a loan agreement; exchange of letters that constitute an agreement; subscription agreements in regard to external government securities; or a national government guarantee.[143] Regulation 192 provides that the national government may borrow for the purpose of, financing national government budget deficits; borrowing for purposes of cash management; honouring obligations under outstanding

[138] Regulation 183 of the Public Finance Management (National Government) Regulations of 2015
[139] Regulations 184 and 185 of the Public Finance Management (National Government) Regulations of 2015
[140] Ibid
[141] Ibid
[142] Ibid
[143] Regulation 189 of the Public Finance Management (National Government) Regulations of 2015

national government guarantees; refinancing outstanding debt or repaying a loan prior to its date of repayment; mitigation against adverse effects caused by an urgent and unforeseen event in cases where the contingency fund has been depleted; mitigation against significant balance of payment imbalances; and meeting any other development policy objectives that the Cabinet Secretary shall deem necessary, consistent with the law, and as Parliament may approve.

The regulations equally outlines the main objective of the public debt management is to ensure that the government's financing needs and its payment obligation is met at the lowest possible cost over the medium to long term, with a prudent degree of risk, and to promote development of the domestic debt market while ensuring the equitable sharing of benefits and burdens of public debt between the current and future generation.[144]

Regulation 26 which is in tandem with regulation 196 provides that debt limit at any time shall not exceed the net present value of the total debt that is determined in accordance with fiscal responsibility principles enumerated in this regulation and the debt limit shall specified annually in the budget policy statement and the medium term debt management and strategy. Lastly that the annual new government debt and guarantees shall be consistent with the debt limits set out by the regulation for purpose of monitoring compliance the amount of government debt and government guarantees which are not denominated in shillings shall be recalculated at the prevailing exchange rate of the Central Bank of Kenya.

[144] Regulation 193 of the Public Finance Management (National Government) Regulations of 2015

The cabinet secretary in charge of national treasury is required to submit an annual report to parliament on public debt in the format set out by the cabinet secretary. The information shall include, review of previous year's financing of budget deficit; composition of External debt; publicly guaranteed debt; on-lent loans and contingent liabilities; debt strategy and debt sustainability; outlook for the medium term; and any commitment fees and penalties paid on any undisbursed amounts of a loan.[145]

The national government entities and each county treasury shall submit to the national treasury a report on public debt in a format prescribed by the accounting standards board within two months after the end of the financial year and the report shall the information that, review of previous year's financing of budget deficit; review of previous year's financing of budget deficit; composition of domestic debt; composition of external debt; on-lent loans and contingent liabilities; debt strategy and debt sustainability; outlook for the medium term; and any commitment fees and penalties paid on any undisbursed amounts of a loan.[146]

3.2.4 Public Finance Management (County Governments) Regulations 2015

These regulations are applicable to the county government; county government entities; county public funds established under the Act; and any other person performing any act or doing such thing that is provided for under the Act.[147]

The regulation establishes public finance management standing committee in every county government which is comprised of the Accounting Officer as chairperson of the committee; an

[145] Regulation 200 of the Public Finance Management (National Government) Regulations of 2015
[146] Regulation 199 of the Public Finance Management (National Government) Regulations of 2015
[147]Regulation 3 of the public Finance Management (County Governments) Regulations of 2015

officer designated by the accounting officer as secretary of the committee and who shall be either the head of the finance or accounts units or head of both finance and accounts units of the entity; and heads of departments or administrative units dealing with public finance management matters.[148]

The regulation provides that county government borrowing is guided by the principles that there is need to ensure stability of domestic financial markets; promote inter-generational equity in the sharing of burdens and benefits of public borrowing; determine the thresholds of borrowing rights for both levels of government; use of objective criteria for evaluating county government eligibility for national government debt guarantee; and prudence and equity in setting limits for debt stock levels for each county government.[149]

Regulation 177 invests the power to raise loans for the county government with the county executive committee member and that he may from time to time borrow within and outside Kenya, such sums of money in such amount and on such terms conditions as to interest, repayment, disbursement or as he may think fit. The loans borrowed can be by issuing County Treasury bonds; by bank overdraft facility from the Central Bank of Kenya; and by any other loan or credit evidenced by instruments in writing. In acquiring external loans by the county government then the same is to be guaranteed by the national government as provided for under the Act and the borrowing must be allowed by the national treasury.

[148] Regulation 18 of the public Finance Management (County Governments) Regulations of 2015
[149] Regulation 179 of the public Finance Management (County Governments) Regulations of 2015

The regulations also provide that the purposes for borrowing by the county governments are to finance county government budget deficits; or cash management; or to refinance outstanding debt or repaying a loan prior to its date of repayment; or to mitigate against adverse effects caused by an urgent and unforeseen event in cases where the Emergency Fund has been depleted; or to meet any other development policy objectives that the County Executive Committee Member shall deem necessary, consistent with the law, and as County Assembly may approve.[150]

The regulations equally provide that in line with the Act, a county public debt should not exceed twenty percent of the county government's most recent audited revenues, as approved by the county assembly and that the annual debt service cost of a county should not exceed fifteen percent of the most recent audited revenue of the county government as approved by the county assembly.[151] In line with the above the debt limit at any given time shall not exceed the nominal value of the total county public debt that is determined by county assembly within the limits set under of the Act and in accordance with fiscal responsibility principles under regulation 25 of the these Regulations and it shall be specified annually in the county fiscal strategy paper and the medium term debt management strategy paper.[152] To ensure compliance with the set out debt ceiling the amount of county government debts which are not denominated in Kenya shillings shall be recalculated at the prevailing exchange rate of the Central Bank of Kenya.[153]

A county government can also issue treasury bonds in accordance to section 144 of the Act and the process would involve, before seeking the national government guarantee, the County

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[150] Regulation 178 of the public Finance Management (County Governments) Regulations of 2015
[151] Regulation 179 of the public Finance Management (County Governments) Regulations of 2015
[152] Regulation 180 of the public Finance Management (County Governments) Regulations of 2015
[153] Ibid

Executive Committee Member for finance shall develop and submit the cash plan, indicating the borrowing requirements to the County Executive Committee for approval of the borrowing including its terms and conditions; after approval by the County Executive Committee, the County Executive Committee Member shall submit the cash plan referred to above to the County Assembly for approval of the borrowing including its terms and conditions; upon approval by the County Assembly, the County Executive Committee Member shall submit the final cash plan and the approval of the County Assembly to the Cabinet Secretary requesting for the guarantee of the Treasury Bond and their inclusion in the issuance calendar; the Cabinet Secretary to the National Treasury, after receiving the request from the county government, shall seek the recommendations of the Intergovernmental Budget and Economic Council in fulfillment of the requirements of section 58(2)(i) of the Act; the Cabinet Secretary to the National Treasury may, upon taking into account the recommendations of the Intergovernmental Budget and Economic Council, approve or reject the request; the Cabinet Secretary shall reject a request for loan guarantee with reasons and communicate the same to the concerned County Executive Member; upon approval of a loan guarantee request, the Cabinet Secretary to the National Treasury shall submit the request to Parliament with recommendations seeking its approval; the Cabinet Secretary to the National Treasury shall communicate the decision of Parliament on the draft loan guarantee to the respective County Executive Committee Member for finance.[154]

upon approval by Parliament, the Cabinet Secretary shall include such authorized Treasury Bonds in the overall national issuance calendar; once the issuance calendar is known, when the national governments advertises its bond issuance for a specific month it shall also incorporate those to be issued on behalf of county governments; on the issuance day, the county whose bond is being

[154] Infra note 154

issued, shall be represented in the auction committee meeting by the County Executive Committee Member or his or her representative; and after the National Treasury and the county government sign an on-lending agreement, the National Treasury shall transfer the proceeds of the Treasury Bond to the Revenue Fund of that county government and such on-lending transactions shall attract a fee to be determined by the National Treasury.[155]

Article 212(1) of the Constitution provides that the county governments can only borrow if the loans are guaranteed by the national government. In line with this the regulations provide that with regards to applying for external loans and before a county government requests for the national government to guarantee their external loan then the county government is required to do the following, 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; 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; after obtaining the approval of the County Assembly, the County Executive Committed 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.[156]

the Cabinet Secretary, after receiving the request from the county government, shall seek the recommendations of the Intergovernmental Budget and Economic Council; the Cabinet Secretary to the National Treasury, after receiving recommendations of IBEC, shall seek the

[155] Regulation 183 of the public Finance Management (County Governments) Regulations of 2015

[156] Infra note 156

recommendations of the Attorney-General; 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; the Cabinet Secretary shall reject a request for loan guarantee with reasons and communicate the same to the concerned County Executive Member for finance; upon approval of a loan guarantee request, the Cabinet Secretary shall submit a Sessional paper to Parliament with recommendations seeking its approval; the Cabinet Secretary shall communicate the decision of Parliament on the draft loan guarantee to the respective County Executive Committee Member for finance; and upon approval by parliament the cabinet secretary shall issue a loan guarantee, the County Executive Committee member shall report to the County Assembly of the decision.[157]

The objectives of public debt management are to ensure that the county government's financing needs and payment obligations are met at the lowest possible cost over the medium to long term, with a prudent degree of risk, and to promote development of the domestic debt market while ensuring the equitable sharing of benefits and burdens of public debt between the current and future generation and that any borrowing by the county government is informed by the county government medium term debt management strategy which will set out the framework for the management of county public debt.[158]

The medium term debt management strategy, shall be reviewed annually and will be prepared and executed by the County Treasury and approved by the County Executive Committee. The county medium term debt management strategy shall be prepared considering, the borrowing needs of the

[157] Regulation 184 of the public Finance Management (County Governments) Regulations of 2015
[158] Regulations 186 and 187 of the public Finance Management (County Governments) Regulations of 2015

county governments; fiscal responsibility principles set out in section 107 of the Act and regulation 25 of these Regulations; prevailing macro-economic conditions; prevailing conditions of the financial markets; and any other relevant factors and shall include shall include measures for minimizing borrowing costs with a prudent degree of risks.[159]

The county medium term debt management strategy is implemented through the annual county government borrowing programme for each fiscal year. The annual borrowing programme includes issuance of county government securities, external guaranteed loans and disbursements for the fiscal year and show indicative dates of such issuance and disbursements.[160]

The regulations provide that the negotiation with foreign governments and agencies for external loans shall culminate into and shall be formalized into a recognized instrument in addition to the national government guarantee which maybe loan agreements; or exchange of letters that constitute an agreement; or subscription statement in regard to domestic government securities; or national government guarantee.[161]

In regulation 191 there is provision for credit purchase as a means of loan to the county. The county treasury is to submit to the national treasury a report on county public debt as prescribed in these regulations. Not later than three months after the end of each county financial year the County Executive Committee Member shall prepare and submit an annual report to the county assembly on public debt and the annual public debt report shall be in the format gazette by the Cabinet

[159] Supra n. 150
[160] Regulation 188 of the public Finance Management (County Governments) Regulations of 2015
[161] Regulation 189 of the public Finance Management (County Governments) Regulations of 2015

Secretary and shall include, review of previous years financing of budget deficit; composition of domestic debt; composition of external debt; on-lent loans and contingent liabilities; debt strategy and debt sustainability; nugatory and similar payments, compensation and ex-gratia payments; outlook for the medium term; and any commitment fees and penalties paid on any undisbursed amounts of a loan.[162] The County Treasury shall maintain an inventory of all loans made to the county government and make the record available to the county assembly within seven days of request.[163]

3.3 Institutional Framework

This section gives an insight on institutional framework in Kenya.

3.4 Introduction

This part interrogates the role of institutions involved in public debt acquisition and management in Kenya. Kenya being a devolved government, both the national government and county governments have the power to raise external loans as such there are different institutions cutting across the national and the county governments dealing with public debt. The institutions include the legislature, the executive, central bank of Kenya, public debt management office and county executive committee.

3.5.1 The Legislature

In Kenya the legislature comprises of both the national assembly and the senate. The legislature is mandated to enact laws on public debt which includes external debt. The essence is to promote public debt sustainability by ensuring that the public debt managers abide by the set financial

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[162] Regulations 193- 194 of the public Finance Management (County Governments) Regulations of 2015

[163] Supra n.154

objectives and fiscal responsibilities. The parliament plays check and balances on government's spending.

The parliament oversees the national government's borrowing and expenditure while the county assembly monitors the borrowing of the county governments in conjunction with other institutions. The legislature is required to ensure that the national and county governments and other entities limit their borrowing to the public debt threshold and purpose of borrowing.

The national treasury sets out the government borrowing levels in the medium term debt management strategy which is then approved by the parliament. As earlier discussed the public finance national government's borrowing is limited to50% of the GDP[164] while the county government's borrowing is limited at 20% of the audited revenue for that year.[165]

However, the parliament lacks the power to approve on new borrowings, lack of parliament to approve new borrowings by the government has hindered the parliament's ability to curb the governments appetite for huge loans. There is need for parliament to be granted power to approve new borrowings by the government, which have potential risk on public debt stocks.

It should however be noted that the parliament approves the annual budget estimates of the national government and other entities,[166]draft loan guarantees,[167]budget policy statement and deviation from financial objectives in a budget policy statement by the national government or new

[164] Regulations 26 and 196 of the Public Finance Management (National Government) Regulations of 2015
[165] Supra n. 148
[166] Section 39 of the Public Finance Management Act
[167] Regulation 204 of the Public Finance Management (National Government) Regulations of 2015

government.[168]The parliament is equally required where the cabinet secretary in charge of treasury seeks to make payments out of the contingence fund[169] and to establish a public fund. The parliament also has the mandate to ensure that the loans procured are prudently used for the purpose enlisted as provided for under regulations.[170]

Of concern is that despite the parliament's role in putting the country's government external borrowing in check, the parliament has enhanced the government's borrowing by approving budgets with huge deficit thus giving the national treasury the grounds to procure more external debts so as to finance the annual budget, this has equally led to borrowing with the latest loan being Ksh 75 billion from world bank to finance one of the big four agenda.[171]

3.5.2 The Executive

The executive has the power to raise loans from within and outside the country through the treasury. The department of national treasury as established by the constitution and the Public finance management Act[172] deals with the management of the public finance. The national treasury has been mandated to deal with the finances of the country which includes raising loans within and outside the country.[173]

The executive through the national treasury raises loans without any permission from the parliament, however, the national treasury has the responsibility of explaining to the parliament how money raised is spent.[174] All the country's borrowing are initiated by the national government

[168] Section 16 of the Public Finance Management Act
[169] Section 22 of the Public Finance Management Act
[170] Regulation 192 of the Public Finance Management (National Government) Regulations of 2015
[171] The world bank, loans and credit, Kenya inclusive growth and fiscal management development policy operation, may 28, 2019. Accessed at https://www.worldbank.org/en/news/loans-credits/2019/05/28-kenya-inclusive-growth-and-fiscal-management-development-of-policy-operation accessed on 6/6/2019
[172] Article 225(1) of the Constitution as read together with Section 11 of the public finance management Act
[173] Supra n. 121
[174]Supra n. 159

and documents signed by the cabinet secretary in charge of national treasury or an individual assigned by the cabinet secretary.[175]

The cabinet Secretary in charge of national treasury is required to submit to Parliament, every four months, a report of all loans made to the national government, national government entities and county governments, in accordance with Article 211(2) of the Constitution.[176] The cabinet secretary will however, be required submit to Parliament, a report of all loans made to the national government, national government entities, and county governments, not later than seven days after receiving a request to do so from either House of Parliament the parliament is canvassing a matter relating to national debt.[177]

The report tabled to parliament shall state the loan balances brought forward, carried down, drawings and amortizations on new loans obtained from outside Kenya or denominated in foreign currency, and such other information as may be prescribed by regulations, specifying the names of the parties to the loan; the amount of the loan and the currency in which it is expressed and in which it is repayable; the terms and conditions of the loan, including interest and other charges payable and the terms of repayment; the amount of the loan advanced at the time the report is submitted; the purpose for which the loan was used and the perceived benefits of the loan; and such other information as the Cabinet Secretary may consider appropriate.[178]

The cabinet secretary is equally required to submit national government debt management strategy to Parliament annually. This is to happen on or before the 15th February in each year. The report

[175] Supra n. 130
[176] Section 31 of the public finance management Act
[177] Supra n 174
[178] Ibid

shall state the debt management strategy of the national government over the medium term with respect to its actual liability and potential liability in respect of loans and guarantees and its plans for dealing with those liabilities and the information shall include the total stock of debt as at the date of the statement; the sources of loans made to the national government and the nature of guarantees given by the national government; the principal risks associated with those loans and guarantees; the assumptions underlying the debt management strategy; and an analysis of the sustainability of the amount of debt, both actual and potential.[179]Within fourteen days after the debt strategy paper is submitted to Parliament under this section, the Cabinet Secretary shall submit the statement to the Commission on Revenue Allocation and the Intergovernmental Budget and Economic Council and publish and publicize the statement.[180]

3.5.3 The Central Bank

The Central Bank of Kenya is established under Article 231 of the Constitution this equally backed by an Act of parliament.[181] The principal objective of the Bank is to formulate and implement monetary policy directed to achieving and maintaining stability in the general level of prices,[182] other objectives include to formulate and implement foreign exchange policy; hold and manage its foreign exchange reserves; formulate and implement such policies as best promote the establishment, regulation and supervision of efficient and effective payment, clearing and settlement systems; act as banker and advisor to, and as fiscal agent of the Government; issue currency notes and coins; and license and supervise mortgage refinance companies.[183]

[179] Section 33 of the public finance management Act
[180] Ibid
[181] Section 3 of the Central Bank of Kenya Act
[182] Section 4 of the Central Bank of Kenya Act
[183] Section 4A of the Central Bank of Kenya Act

The Central bank is also mandated, at intervals of not more than six months, submit to the minister of finance a monetary policy statement for the next twelve months which shall specify the policies and the means by which the Bank intends to achieve the policy targets; state the reasons for adopting such policies and means; contain a review and assessment of the progress of the implementation by the Bank of monetary policy during the period to which the preceding policy statement relates.[184]

Within the Central bank there is the Monetary Policy Committee, which shall have the responsibility within the Bank for formulating monetary policy.[185] The committee consists of the Governor, who shall be the chairman; the Deputy Governors, who shall be deputies to the chairman; two members appointed by the Governor from among the staff; and four other members who have knowledge, experience and expertise in matters relating to finance, banking, and fiscal and monetary policy, appointed by the Minister; the Permanent Secretary to the Treasury, or his representative, who shall be a non-voting member.[186]

In line with the duty of the Central bank of advising the government with regards to monetary policies, the governor of the central bank has issued statements stating that the country had reached its debt ceiling and more borrowing puts the country at a risk instead the country should think of debt reorganization.[187]

[184] Section 4B of the Central Bank of Kenya Act
[185] Section 4D of the Central Bank of Kenya Act
[186] Ibid
[187] Paul Wafula, Kenya's Debt Problem Creates a Bleak Future, Daily Nation, June 2, 2019. Accessed at https://www.nation.co.ke/news/kenya-debt-problem/1056-5141464-19rdh/index.html

3.5.4 The Public Debt Management Office

The Kenyan legal framework centralizes all the debt functions under the public debt management office. It is an office established within the national treasury.[188] The objective of the office is to minimize the cost of public debt management and borrowing over the long-term taking account of risk; promote the development of the market institutions for Government debt securities; and ensure the sharing of the benefits and costs of public debt between the current and future generations.[189]

The public debt management office has various functions as discussed earlier.[190] The regulation equally provides that the office has other functions including prepare and update an annual medium-term debt management strategy including debt sustainability analysis in accordance with regulations; prepare and review an annual borrowing programme as appropriate including the auction calendar to facilitate auction of government debt securities; participate in negotiation meetings with government creditors, and provide technical support to the Cabinet Secretary on public debt operations; assess the risks in issuing any guarantees including contingent liabilities inherent in public private partnership projects, and prepare reports on the method used for assessment and the results thereof for the attention of the Cabinet Secretary; facilitate the recovery of any payments including interest and other costs incurred by Government due to the honouring of outstanding guarantees; prepare annual debt management report which shall include outstanding guarantees, outstanding lending and government on-lending by Government; monitor and keep track of debt levels; to keep timely, comprehensive and accurate records of outstanding Government debt, guarantees and lending in an appropriate database; advise on all debt servicing

[188] Section 62 of the Public Finance management Act
[189] Ibid
[190] Supra n.131

obligations of Government; prepare and publish debt statistical bulletins regularly; prepare forecasts on Government debt servicing and disbursements as part of the yearly budget preparation; compile, verify and report on all Government debt arrears and design a strategy for the settlement of those arrears; monitor that the disbursements of loans raised by Government are in accordance with agreed disbursement schedules; formulate External Resources Policy; assess, mobilize, negotiate and allocate all external resources including the consolidation of the donor commitment register in the annual national budget; examine and scrutinize proposals for financing projects of a national government entity from an accounting officer; formulate and harmonize policies and coordinate matters relating to employment of Kenyan nationals and appointment of expatriate consultants and technical assistance as experts and consultants in projects supported by development partners; ensure adherence to the accepted guidelines and procedures for procurement involving funds provided under foreign aid; coordinate, review and monitor the utilization of external resources including joint programming, joint work plans, joint visits, joint implementation, and monitoring and evaluation; profile external resources and maintain the accounts thereof; formulate an external resource, mobilization strategy to guide the national and county governments in external resource mobilization including monitoring; liaise for external economic relations with international development agencies; coordinate all international agreements involving financial economic and technical co-operation dealing predominantly with economic and financial issues; programme and manage financing of fellowships, scholarships and foreign training offers from bilateral and multilateral sources; ensure harmonization, alignment and coordination of external resources in line with international conventions of which Kenya is a member state thereof; monitor disbursement and absorption of external resources including reporting of the same by both national and county governments; formulate guidelines and procedures for reporting and recording budget estimates and expenditure for external resource; provide guidance and capacity development to county governments in the assessment, mobilization, negotiation and allocation of all multilateral and bilateral external resources for implementation of development partners; support aid effectiveness initiatives and to use country systems in the management of external resources and where there is need, support in strengthening them rather than avoiding them; perform such other functions as may be determined by the Cabinet Secretary.[191]

The Cabinet secretary in charge of finance is expected to develop the policy and financial framework in accordance with Constitutional principles within which the Public Debt Management Office operates; delegate to the Head of the Public Debt Management Office the operational decisions on borrowing and debt management and the day-to-day management of the Office; ensure that the Public Debt Management Office has the resources and skills to manage the debt and borrowing according to international best practices for liability management; and be accountable to Parliament for the work of the Public Debt Management Office.[192]

The office is required to prepare and submit to the Cabinet Secretary and the Commission on Revenue Allocation reports on the Medium Term Debt Management Strategy consistent with the Budget Policy Statement; the government borrowing plan for the approved Annual Budget; the statistical and analytical reports on debt and borrowing; and the annual performance reports of the Public Debt Management Office.[193] The published copies of the above reports should be sent to

[191] Regulation 194 of the Public Finance Management (National Government) Regulations of 2015
[192] Supra n. 183
[193] Section 64(2) of the public finance management Act

all the counties.[194] The office may appoint agents to provide technical advice or undertake administrative functions for the management of debts provided that control and accountability for these functions remain with the Cabinet Secretary.[195]

At the request of a county treasury, the office may assist the government in its debt management and borrowing, equally at the request of the public debt management office the Treasury shall supply the Office with any information that shall enable it to execute its mandate efficiently.[196]

3.5.5 County Executive Committee

Each county has a county executive committee member for finance who may raise loan on behalf of the county government as per the conditions set out in Article 212 of the constitution and sections 58 and 142 of the Act.[197] The loan should be according to the fiscal responsibility principles and the financial objectives of the county government set out in its most recent County Fiscal Strategy Paper; and the debt management strategy of the county government over the medium term.[198]

A county government may raise loan either within Kenya or outside Kenya by issuing County Treasury bonds, by bank overdraft facility from the Central Bank of Kenya and by any other loan or credit evidenced by instruments in writing.[199]

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[194] Section 64(3) of the public finance management Act
[195] Section 64(4) of the public finance management Act
[196] Section 65 of the public finance management Act
[197] Section 141 of the public finance management Act
[198] Ibid
[199] Regulation 177 of the Public Finance Management (National Government) Regulations of 2015

The County Executive Committee member for finance may appoint advisers, agents and underwriters for the purposes of raising loans and enter into agreements with those advisers, agents and underwriters as to the role to be undertaken by them and the remuneration to be paid to them.[200]

The County Assembly may authorize short term borrowing by county government entities for cash management purposes only.[201] However, the County Executive Committee member for finance or any person designated by the County Executive Committee member for finance in writing is authorized to execute loan documents for borrowing by the county government.[202]

3.6 Effects of the Legislative and Institutional Framework in curbing the increasing Public Debt in Kenya

From the above analysis, it is clear that there are a number of legislation and institutions in Kenya which should be adequate to deal appropriately with the ballooning public debt, however, that is not the case and the important question is why do we still have the problem of increasing public debt and what are the corrections to be done to ensure that the problem is reversed and put in control.

First of all the various legislation discussed above have provided for a way of dealing with the public debt but have not exclusively dealt with the issue of the ballooning public debt and how to reverse the said public debt back within safe levels, to this end the laws have failed to provide for a ceiling for the public debt and left it to be determined annually thus it rises every year without any check. To effectively deal with the problem of the public debt increasing every day without limit, it is important for the law to put an actual level of ceiling for example putting a ceiling in

[200] Ibid n 191
[201] Section 142 of the public finance management Act
[202] Section 143 of the public finance management Act

terms of money which the government cannot borrow beyond i.e putting the public debt ceiling at Kshs 6 trillion.

It is equally clear that according to the legislation, the executive wields all the power to raise loans on behalf of the national government, this also means that the executive does not have to seek for permission from anyone to seek for loans from within or without the country, as was said by John Dalberg that power corrupts and absolute power corrupts absolutely, in this regard the executive has been having a field day borrowing knowing that it will not be held to account for its actions. There is need to amend the law to provide for the parliament to approve any loan proposals by the executive in that if the parliament is not satisfied by the executive on their reasons for raising the loans then the parliament can turn the proposal down and it fails to go materialize. In this manner the parliament will effectively keep watch over the borrowings by the government.

The problem of the ballooning debt has equally been caused by lack of accountability and punishment mechanism. There are no strong accountability mechanisms in place for the treasury and the executive to be held accountable for their unchecked borrowing which ensures that the public debt keeps increasing no matter the consequences. There is need to put in place accountability mechanisms with stringent and punitive punishment for breach of the legislation on public debt. This would go in a long way in keeping the executive in check as individuals would be held accountable for their actions.

There is also the need to have mechanism in place to ascertain whether the public debt being acquired will positively impact on the economical growth. The issue of blindly borrowing from other countries has made Kenya acquire public debts which have created more problems than relief to the country. To this end there is need to have legislation for cost benefit analysis to ascertain whether the debt being acquired will be beneficial to the country, the analysis would help in determining whether the country acquires the debt or not.

Institutions such as the parliament have also failed in helping in curbing the ballooning public debt, this is because the parliament has continually passed budgets with huge deficits thus opening gates to the executive to borrow more to finance the budget. This has ensured that the public debt increases year in year out as the government has to borrow to finance the budgets and other projects.

3.7 Conclusion

From the above it is clear that the public debt ceiling is limited to gross public debt, there is no legal limit on the domestic or foreign borrowing.[203] It should be noted that a proper debt management legal framework should classify the scope of the public debt ceiling, this is most important for external debt, which has serious consequences if it gets out of place, in that regards a sound debt management should provide explicitly a debt ceiling and the consequences of surpassing the public debt ceiling and in particular the foreign debt limit.

It should, however, be noted that Kenya has an obligation under the East African community monetary treaty to ensure that its public debt limit does not exceed 50% of the GDP.[204]

In Kenya public debt limit is set and approved by parliament through the medium term debt management strategies which are made every year. A review of the law on foreign debt should closely focus on the Scope of the foreign debt; objectives and fiscal responsibility principles; legal

[203] Public debt annual report 2015/2016

[204] World Bank, 'Decision Time, Spending More or Spending smart: Kenya Public Expenditure Review, 2014. (Vol 1) 58

authority to borrow loans; borrowing purpose; foreign debt ceiling; contingent liability and the law on the country's lending.

It is also clear that despite having various legislations and institutions to deal with public debt and it is obvious that there is need to amend the existing legislation to help in reducing the ever rising Public debt.

4. CHAPTER 4

4.1 BEST PRACTICES FROM OTHER JURISDICTIONS, NIGERIA AND NEW ZEALAND ON THEIR REGULATIONS ON FOREIGN DEBT

This chapter investigates the South Africa and Nigeria's regulations on foreign debts and highlights on the best practices which Kenya can borrow from the two countries.

4.2 Introduction

This chapter analyses the legal framework of Nigeria and New Zealand with regards to foreign debt. The comparative is relevant in terms of population and their debts to GDP ratios of the countries, for example Nigeria has a population of 200,962,417 with a debt to GDP ratio of 27.37%, and New Zealand has a population of 4,783,063 with a debt to GDP ratio of 22.69% while Kenya has a population of 52,214,719 with a debt to GDP ratio of 56.95%.[205]

Our focus will be on the institutions managing debts in the countries, the regulation on foreign debt as compared to Kenya and the best practices to be borrowed from the countries.

4.3 Nigeria

Nigeria has faced changes with its external debt, by the end of 2001, the external debt was at 65% of the GDP while the domestic debt had equally hit an all time high and thus measures and strategies were made to help reduce the public debt and specifically external debt.[206] The rapt of changes included changing the fragile and inadequate economic policy reform, changing weak legal and institutional framework for public resources management, changing inefficient use of public resources and mismanagement and pursuing a domestic economic reforms, limit external

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[205] World Population review of 2019. Accessed at wordpopulationreview.com/countries/countries-by-national-debt accessed on 1/7/2019

[206] Ngozi Okonjo Iwehia, Charles C. SOludo, Mansur Muhtar, "The Debt Trap in Nigeria: Towards a Sustainable Debt Strategy," Africa World Press, Inc 2003

borrowing and mobilize untapped domestic resources, putting systems in place to better manage existing debt and guide future obligations and also participate proactively to address the defects of international financial system,[207] this explains why the country has a debt ratio to GDP of 27.37% as at 2019.[208]

4.4 Legislative framework on foreign debt in Nigeria

This section gives insight on the legislative framework of Nigeria on external debts and the best practices to be borrowed by Kenya on the same.

4.4.1 The Constitution of Federal Republic of Nigeria

The constitution establishes a federation consisting of states and a federal capital territory.[209] The constitution equally establishes the national assembly for the federation which consists of a senate and a house of representatives and given the power to make all laws.[210] With regards to laws on external debts, the parliament has passed different legislations including the debt management office (establishment etc) Act, Investment and Security Act, The government promissory notes Act, The central bank of Nigeria Act, The fiscal responsibility Act and others.

4.4.2 The Debt Management Bureau (establishment etc) Act 2011

The Act is establishes the Debt Management Bureau of Nigeria with the of maintaining a reliable database of all loans taken or guaranteed by the Federal or State Governments or any of their agencies; preparing and submitting to Federal Government a forecast of loan service obligations for each financial year; preparing and implementing a plan for the efficient management of Nigeria's external, domestic and sub-national debt obligations at sustainable levels compatible with

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[207] Ibid
[208] Supra n. 203
[209] Section 2 of the constitution of federal republic of Nigeria
[210] Section 4 of the constitution of federal republic of Nigeria

desired economic activities for growth and development, and participate in negotiations aimed at realizing those objectives; Verifying and servicing all debts guaranteed or directly taken by the Federal Government; verifying and servicing external and other debts taken by State Governments or Local Governments and any of their agencies, where such debts are guaranteed by the Federal Government; setting guidelines for managing Federal Government financial risks and- currency exposure with respect to all loans; advising the Federal Government on their structuring and re-financing of all debt Obligations; advising the Minister on the terms and conditions on which monies, whether in the currency of Nigeria or in any other currency, are to be borrowed; submitting to the Federal Government, for consideration in the annual budget, a forecast of borrowing capacity in local and foreign currencies; establishing and maintaining relationships with international and local financial institutions, creditors and institutional investors in Government debts; collecting, collating, disseminating information, data and forecasts on debt management with the approval of the Board; and undertaking any other duty fit within their powers.[211]

The bureau has also been accorded power to, issue and manage Federal Government debt arising from the issuance of various instruments upon such terms and conditions as may be agreed between the Federal government and the Bureau; develop a debt market for the State Governments, that will allow them have direct access to borrowing through issuance of state bonds, but within the guidelines that will ensure sustain ability; issue from time to time guidelines for the prudent management and smooth operation of the public debt of the Federal Government; issue, from time to time, guidelines on external borrowing, domestic borrowing, federal government guarantees and on-lending to sub-nationals, subject to the approval of the National Assembly; require persons and institutions having access to, at all reasonable times to supply such forms as the Bureau may from

[211] Section 1 of the Debt Management Bureau (Establishment) Act of 2011

time to time direct, information relating to matters affecting borrowing or public debts in the national economy; and do such other things which in the opinion of the Board relate to debt management of Federation.[212]

On external loans, the Act provides that the bureau is to annually advise the Federal Government on the financing gap for the succeeding financial year and the amounts to be borrowed for bridging the gap both internally and externally.[213] And that the advice shall form the basis of borrowing by all levels of government as approved by the national assembly.[214]

The ministry of finance together with the bureau is responsible for negotiating and acquisition of such loans and credit.[215] In section 18 the Act provides that he Federal, State and Local Governments or any of their agencies shall not obtain any external loan except with a guarantee issued by the Minister and where a loan an external loan is obtained without adherence to the laid down law, then the country is not bound by such loans.[216]

The Act allows the federal government to guarantee external loans and such guarantee agreements for external loans are to be executed by the minister of finance on behalf of the federal government.[217]

In section 24 of the Act, the federal government is allowed to issue grants or loans to a foreign government or international body, with the approval of the National Assembly after being submitted before it by the president. The Bureau is then required to negotiate the terms and

[212] Ibid
[213] Section 16 of the Debt Management Bureau (Establishment) Act of 2011
[214] Ibid
[215] Ibid
[216] Sections 17 and 18 of the Debt Management Bureau (Establishment) Act of 2011
[217] Section 20 of the Debt Management Bureau (Establishment) Act of 2011

condition of the loan referred and the resident thereafter submits it to the National Assembly for ratification.[218]

4.4.3 The Government Promissory Notes Act of 2004

This Act provides for the creation and issue of Government Promissory Notes for the purpose of raising loans. If the government raises loans for any purpose as stipulated in any legislation in Nigeria, the minister of finance may do so by issuing securities in the form of government promissory notes.[219]

Section 4 of the Act provides that the principal sums and interest represented or secured by any Government promissory notes are charged upon and are be payable out of the general revenue and assets of the Federation.

The minister of finance is required to ensure the publication in the federal government, each loan raised by the issue of promissory notes detailing, the face value of the notes; the rate of interest payable on the loan; the date of redemption of the notes and if the Minister has reserved an option to redeem the notes at an earlier date, the fact that he has reserved such an option and the terms and conditions on which the option may be exercised.[220]

Section 12 of the Act establishes sinking funds, which the minister of finance after consultation with the governor of the central bank may set up for the purpose of redeeming loans raised by the issue of Government promissory notes, Provided that no sinking fund established is in respect of more than one such loan. After establishing sinking funds, the minister of finance is equally required by issuance of notice in the federal government gazette, state the rate and intervals at

[218] Section 26 of the Debt Management Bureau (Establishment) Act of 2011
[219] Section 3 of the government promissory notes of 2004
[220] Section 5 of the government promissory notes of 2004

which appropriation out of the general revenue and assets of the Federation is to be made as contribution to the sinking fund and the date from which such contributions shall commence.[221]

However, when the funds in the sinking fund are not enough to repay a loan then the deficiency is to be charged on the revenue.[222]

4.4.4 Fiscal Responsibility Act 2007

The Act establishes the Fiscal Responsibility Commission with the powers of compelling any person or government institution to disclose information relating to public revenues and expenditure and causing an investigation into whether any person has violated any of its provisions.[223]

Section 3 provides that the commission is required to monitor and enforce the provisions of the Act and promote the economic objectives; disseminate such standard practices including international good practice that will result in greater efficiency in the allocation and management of public expenditure, revenue collection, debt control and transparency in fiscal matters; undertake fiscal and financial studies, analysis and diagnosis and disseminate the result to the general public; make rules for carrying out its functions under the Act; and perform any other function consistent with the promotion of the objectives under the Act.

The Act provides that the framework for debt management during the financial year shall be based on the rules that the government at all tiers only borrows for capital expenditure and human development provided that such borrowing is on concessional terms with low interest rate and with a reasonable long amortization period subject to the approval of the appropriate legislative body

[221] Section 12 of the government promissory notes of 2004
[222] Section 17 of the government promissory notes of 2004
[223] Section 1 and 2 of the Fiscal Responsibility Act of 2007

where the necessary and that the government ensures that the level of public debt as a proportion of national income is held at a sustainable level as prescribed by the national Assembly from time to time on the advice of the Minister.[224]

Section 42 provides that the president with advice from the minister of finance subject to the approval of national assembly set overall limits for the amounts of consolidated debt of the federal, State governments and the limits and conditions approved by the national assembly is consistent with the Act and the fiscal policy objectives.

The Act equally provides that for the purpose of verifying compliance with the limits specified pursuant to the Act, the Commission is required at the end of each quarter to determine the amount of the consolidated debt of each tier of government.[225] The Commission is also required to publish on a quarterly basis a list of the Governments in the federation that have exceeded the limits of consolidated debt indicating the amount by which the limit was exceeded.[226]

The Act also provides that the violators of the limits specified pursuant to the Act is prohibited from borrowing from internal or external sources, except for the refinancing of existing debts and bring the debt within the established limited by restricting funding commitments accordingly.[227] Where non compliance with the limit specified pursuant to this Act persists after the time limited by subsection of this Act, the affected tier of Government is to be prohibited from receiving grants from any other Government in the Federation.[228]

[224] Section 41 of the Fiscal Responsibility Act of 2007
[225] Ibid
[226] Ibid
[227] Section 42 of the Fiscal Responsibility Act of 2007
[228] Ibid

Section 44 of the Act provides that the states in the federation desirous of borrowing is required to specify the purpose for which borrowing is intended and present a cost-benefit analysis, detailing the economic and social benefits of the purpose to which the intended borrowing is to be applied. All the borrowings made are supposed to be authorized by the appropriate law before being granted and the proceeds from the borrowing are to be applied solely be applied towards long term expenditure.[229]

The borrowings made is supposed to be within the borrowing limits as set out in the law and the fiscal responsibility commission is to verify on a quaterly basis, the compliance with the set limits and conditions for borrowing by each state in the Federation.[230] The law equally requires the Debt Management Office to maintain comprehensive, reliable and current electronic database of internal and external public debts, guaranteeing public access to the information.[231]

The law requires the financial lending institutions to request and obtain proof of compliance with the provisions of the Act before lending to any government in the federation and any lending contravening this part of the Act is unlawful.[232]

The law also gives the minister of finance the power to grant guarantees on behalf of any government in the federation with the approval of the federal executive council.[233] Any guarantee is to be counter guaranteed in an amount equal or higher than the guarantee and a counter guarantee is only accepted from state or local governments.[234] On foreign currency borrowing only federal

[229] Section 44 of the Fiscal Responsibility Act of 2007
[230] Ibid
[231] Ibid
[232] Section 45 of the Fiscal Responsibility Act of 2007
[233] Section 47 of the Fiscal Responsibility Act of 2007
[234] Ibid

government guarantee is required and no state, local government or federal agency can on its own borrow externally.[235]

4.5 Best practices Kenya may borrow from Nigeria

There is need for conducting cost benefit analysis detailing the economic and social benefit on every debt before signing the contracts on loans and all the public loan is to be acquired based on the results of the cost benefit analysis.

There is also need to push for acquisition of concessional loans as opposed to commercial loans which are expensive with regards to interest involved and the overall cost of financing commercial loans.

The law should equally provide for the financial lending institutions to request for proof of compliance with the laws governing debts in Kenya and any lending completed without complying with the laid down regulations should not be binding to the country.

It may be important to establish an independent body from the national treasury to deal with the country's public debt. The bodies would advise on the loans before acquisition and negotiate the terms of the loans.

There is need to provide for public debt restructuring in the Kenya. This would help the country renegotiate on viable and better means of repaying the public debt without adding more pressure to the current debt situation in the country.

[235] Ibid

Kenya can try and enforce the principle of avoiding loans denominated in foreign currency and put in stringent measures and terms for allowing foreign denominated loans both by the national government and the county governments.

There is also need to clearly define financial misconduct more so with regards to public finance management, and clearly outline the offences and penalties for financial misconduct without having to peg financial misconduct claims on other statutes for successful and efficient prosecution of offences.

4.6 New Zealand

New Zealand's struggle with the Public debt can be traced back to the 1930's when there was a recession and the Central government's debt ratio to the GDP was estimated at 150% while the General government's debt ratio to the GDP was around 190%, the First World War spending had pushed the public debt levels in many countries so high.[236]

By 1932, the general government debt had risen to almost 300% of the GDP leading to a sustained loss of ability to roll over maturing foreign debt and by the end of the year New Zealand government had been advised it should not expect to borrow from any of the European countries and they should deal with their debt.[237]

To curb recession and to adequately deal with the high Public debt, New Zealand passed different legislations such as the National Expenditure Adjustment Act and the Debt conversion Act with the main aim of reducing the government's expenditure and converting their existing public debt into equities and long term payment agreement bearing lower interest than the original loan

[236] Michael Reddell, "The New Zealand Debt Conversion Act 1933: A case study in coercive domestic public debt restructuring," March 2012.
[237] Ibid

agreement.[238]The aim of this was to reduce the servicing cost of the public debt and the outcome was that a substantial amount of the debt was subject to conversion thereby lowering the debt levels of the country.

From then on, the public debt has been reducing and is expected to reduce further, as at 2013 the debt ratio to the GDP was at 33.2% and in 2019 this stands at 22.69% because of the measures put in place to ensure that Public debt is kept in low levels which is beneficial to the country's economy.[239]

4.7 Legislative framework on Public debt

This section gives insight on the legislative framework of New Zealand and the impact it has on the Public debt.

4.7.1 The Constitution Act of 1986

The Constitution Act of New Zealand establishes a Constitutional Monarch, a Unitary State and Parliamentary system. The constitution equally establishes the parliament which consists of Sovereign in right of New Zealand and the House of Representatives.[240] The parliament does many roles including passing legislation governing the country. The Parliament has passed different legislations on Public debt including the Reserve Bank of New Zealand's Act 1989, Public Finance Act 1989 and Fiscal Responsibility Act.

Section 22 of the Constitution Act provides that, it is not lawful for the crown except by or under an Act of parliament to borrow money or to receive money borrowed from any person, this gives footing for the law on public finance as nothing happens outside the law.

[238] Ibid
[239] New Zealand, Economic and Financial Overview,2005.
[240] New Zealand Constitutional Act of 1986

4.7.2 Reserve Bank of New Zealand's Act 1989

The Reserve bank of New Zealand was established as a Central Bank in 1934 but that was changed by the Reserve Bank of New Zealand's Act of 1989 and given the autonomy to implement monetary policy within the framework of the Act.[241]

4.7.3 Public Finance Act 1989

The purpose of the Act is to consolidate and amend the law governing the use of public financial resources including safeguarding public assets by providing statutory authority and control the borrowing by the government.[242]

In Section 5 of the Act, it provides that all the expenses of the Crown should be as approved by the law. Section 26G (i)-(l) equally provides for the principles of responsible fiscal management which at the core is geared towards reducing the Public Net debt to healthy amounts with a long term of reducing the debt to very low levels.

The treasury is equally mandated under this Act to prepare a financial reports giving full account of the assets of the country.[243] The Act equally provides for all the borrowings to be authorized by law.[244] To this end, the minister on behalf of the crown may borrow money from any person within or outside of the country within the law and the minister cannot delegate power to another person but may appoint agents to help in his duties.[245]

The minister on behalf of the crown may borrow money on any terms and conditions that the minister thinks fit.[246] However, the minister may, at any time, vary the terms and conditions of

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[241] New Zealand, Economic and Financial Overview, 2005.
[242] Section 1A(f)(i)
[243] Section 26 of the Public Finance Act
[244] Section 46 of the Public Finance Act
[245] Sections 47-52 of the Public Finance Act
[246]Section 54 of the Public Finance Act

borrowings of the Crown with the consent, if necessary, of the person from whom the money was borrowed.[247]

The minister on behalf of the crown is equally mandated to issue securities but according to the law and the minister also has the authority to vary the terms of the security within the law and the consent of the holder of the security.[248]

The minister on behalf of the crown is also authorized to give loans to organization or other countries within the governing laws.[249]

Sections 76 and 77 of the Act provide for offences against the Act the penalties for the offences respectively.

4.7.4 Fiscal Responsibility Act of 1994

From its enactment, New Zealand's fiscal aggregates have increased with the net government's debt plummeting and the government's net worth increased remarkably.[250] The Act provides a working policy guideline whose objective is to reduce the net public debt to below 20% to the GDP ratio.[251]

The principles of responsible fiscal management are geared towards reducing total Crown debt to prudent levels so as to provide a buffer against factors that may impact adversely on the level of total Crown debt in the future by ensuring that until such levels have been achieved, the total operating expenses of the Crown in each financial year are less than its total operating revenues in

[247] Section 57 of the Public Finance Act
[248] Section 62-65A of the Public Finance Act
[249] Section 65L-65M of the Public Finance Act
[250] Derek Gill and John Yeabsley, "New Zealand Institute of economic research," public discussion paper working paper 2018/1, November 2018 accessed at www//:nzier.org.nz/static/flier-public/id/ie/idie-eclob6/nzier-discussion-paper-2018-no.1-updated.pdf. Accessed on 2/10/19.
[251] Ibid.

the same financial year and once prudent levels of total Crown debt have been achieved, maintaining these levels by ensuring that, on average, over a reasonable period of time, the total operating expenses of the Crown do not exceed its total operating revenues and lastly achieving and maintaining levels of Crown net worth that provide a buffer against factors that may impact adversely on the Crown's net worth in the future.[252]

The Act equally prioritizes government's investment to address the long term financial and sustainability challenge facing New Zealand, the Act was recently amended to include effectiveness and efficiency in management of the government resources.[253]

Section 3 of the Act provides that the Act binds all organs of the crown.

4.8 Institutional Framework of New Zealand with regards to public debt

4.8.1 Parliament

The parliament is made up of the sovereign in right of New Zealand and the House of Representatives. Legislative power is vested with the parliament.[254] The parliament equally controls the government by its power to pass resolution of no confidence or to reject to reject a government proposal made.

4.8.2 Executive

The executive government functions of New Zealand carried out by the executive council. It is made up of the cabinet and the governor general who acts on the advice of the cabinet.[255] While

[252] Section 4 of the Fiscal Responsibility Act
[253] Supra n.243
[254254] Section 14 of the New Zealand Constitutional Act of 1986
[255] Part 6 of the New Zealand Constitutional Act of 1986

the cabinet consists of the prime minister and his/her minister chosen from among the elected members of parliament.[256]

4.8.3 Treasury

The treasury has the key responsibilities for the monitoring, oversight, policy implementation of crown's assets as well as managing the government's borrowing programme.[257] The treasury has in place a regulatory management system which is overseen and administered by the Treasury.

The regulatory quality team within the treasury exercises stewardship over the regulatory management system to maintain and enhance the quality of government initiated regulation.[258] Key responsibility of the quality team include; oversight of the performance of the regulatory management system as a whole and making recommendations to relevant government and parliamentary systems and processes to improve its performance; oversight of cabinet's impact analysis requirement; assessing the significant regulatory proposals against the government standards and the design and delivery of guidance, training and other capability development support for government agencies.[259] These functions complement the treasury's role as the primary economic and fiscal advisor.[260]

Key features of the regulatory management system tend to focus on the development of regulation but system elements also targets the implementation, administration, enforcement, monitoring and review of regulation.[261]The government expects regulatory agencies to adopt a whole of system

[256] Ibid.
[257] Melissa Piscetek, New Zealand Treasury working paper paper 19/01, July 2019
[258]Ibid.
[259] Ibid.
[260] Ibid.
[261] Ibid.

view and take a proactive, collaborative approach to the monitoring and care of regulatory systems within which they have a policy or operational responsibilities.[262]

In the treasury there is the New Zealand Debt management office which manages the government's borrowing programme.

4.9 Best practices Kenya may borrow from New Zealand

There is need to come up with clear cut policies and objectives to ensure that the we sustain our debt levels for example spending within our generated revenue and avoiding having huge budgets which leads to borrowing.

There is also need to clearly define financial misconduct more so with regards to public finance management, and clearly outline the offences and penalties for financial misconduct without having to peg financial misconduct claims on other statutes for successful and efficient prosecution of offences.

The government of Kenya should equally borrow a leaf from New Zealand enact policies which will ensure that the debt levels in the country is reducing and not increasing as is the current trend in Kenya.

Kenya should also come up with legislation on debt restructuring which would enable the country to enter into legal renegotiation of the outstanding debt to come up with a reasonable repayment plan which is less strenuous to the country.

[262] Ibid.

4.10 Conclusion

The above section covered two countries from which Kenya can borrow a leaf on how to deal with public debt and external debt in specific. Kenya can borrow ideas from the other jurisdictions so as to come up with legislation on debt restructuring, have a reasonable public debt ceiling, empower the parliament to question all sources of revenue to finance the budget, come up with a policy to reduce the public debt and provide for financial misconducts and the punishment thereof, however, Kenya should not blindly copy legislation from other countries in a bid to deal with their Public debt problem as their contexts are different and cannot be possibly suffering from the same problem.

CHAPTER 5

5.0 CONCLUSION AND RECOMMENDATIONS

5.1 FINDINGS

Based on the research questions and the research these are the findings that we arrived at. This research found that there are various legislation on public debt in Kenya but there is no attempt made to differentiate between external and internal public debt. However, there is need to make changes to the law to adequately deal with the runaway public debt for example having a reasonable definite debt ceiling for the country and not Kshs 9 trillion as was recently passed.

It also came out from the research that there are various challenges facing the legislative framework on public debt. It is not well equipped to deal with current public debt problem as it does not provide for debt restructuring, it equally fails to provide for financial misconduct and the punishment for the same among other challenges, including failure to provide for a reasonable public debt ceiling.

From the research we realized that there are a number of best practices to borrow from other jurisdictions for example having a debt restructuring legislation, having provision for cost benefit analysis on all loans before they are acquired, empowering the parliament to decide on the revenue to finance the annual budget and equally come up with policy on reducing the public debt to manageable levels.

It is clear that legal reform is necessary to deal with the runaway public debt which includes external public debt. There is the need to incorporate the recommendations of this research in our legislation for example providing for reasonable debt ceiling which will not be a burden to the country. Also have a legislation providing for public debt restructuring and many more changes as suggested in this research.

5.2 Conclusion

In chapter one of this research we have given a back ground of this research and given the objectives of this research. It is our conclusion that there is a problem worth researching on external debt and at the end to come up with solutions to the problem.

Chapter two of the research dealt with the general historical development on external debt and narrowed to Kenya's historical development on external debt to the present day, from this chapter it is our conclusion that there is a looming debt crisis and there is need to address it appropriately, thus leading to chapter 3.

Chapter three of the research deals with the legislative and institutional legal framework in Kenya where we looked into detail, different legislations and institutions. Based on the findings of chapter three it is our conclusion that we have legislation and institutions in place however, there is need to improve on both.

Chapter four of the research dealt with best lessons to be learnt from other jurisdictions in specific Nigeria and New Zealand. It is our conclusion that there are best practices to be learnt by Kenya from other jurisdictions which would assist in making better its legislation and institutions dealing with public debt.

Chapter five deals with the conclusion and recommendations from based on the findings of this research as is hereby exhibited in this chapter.

The hypothesis of this research is based on the premise that there is a looming debt crisis because of lack of adequate legislation on public debt and that there is failure in implementation of the existing laws to help in curbing the ballooning public debt and in particular external debt. From the above research it is clear that Kenya has elaborate regulations on public debt, but it is also clear that minimum attempt is put to draw a distinction between external and internal loans. The laws are generally made to deal with public debt as a whole as opposed to categorizing them into external and locally acquired loans.

It is equally our conclusion that the existing laws do not have the sufficient power to deal conclusively with the ballooning public debt. There is room for improvement on regulations on external debts since they have failed to curb the ever rising public debt and on the same breadth failed to give the way out of the looming debt crisis in Kenya.

A robust legal framework is critical for effective external debt management given the centrality of the law to public debt. While political and economic factors tend to influence debt policies and the quality of debt management practices, a good legal framework helps to promote discipline, transparency and accountability, all of which is critical to achieving sustainable public debt.

5.3 Recommendations

There is urgent need to reduce commercial loans, international bond markets and bilateral loan agreements which are very expensive to furnish and there is need to switch back to concessional debts which are less expensive generally and would not be so expensive to furnish as compared to non concessional loans. This is based on our finding that there is an increase of commercial debt and a reduction in

There is need to curb external borrowing by having a debt ceiling on public debt which essentially determine the maximum amount of debt that government or other public sector entities can carry. In Kenya the ceiling is determined by statutory and ministerial action but this has failed and

Kenya's public debt has continued to swell each year thus there is need for a nominal debt ceiling which are absolute numbers serving as upper limit for debt just as Denmark did.[263] The law should equally be clear on whether the debt ceiling is nominal or relative terms. This should equally apply to county governments. This is in line with the finding that there is no defined debt ceiling which is currently based on the GDP of the country.

There is also need to clearly define financial misconducts, offences and penalties thereof, for example the law should state punishment for borrowing above the ceiling debt set by law which is clearly disregarded in Kenya. As opposed to the current situation where there is no defined financial misconduct in the public finance Act and as such there is need to rely on other out dated laws to combat financial misconduct.

There is need to amend the laws and give power to the parliament to authorize borrowing by the government. The parliament should have the powers to decide on whether a loan facility being acquired by the country is necessary or not and given the powers to decline or approve a loan agreement. As opposed to the current system where the treasury can raise loans without being put in check apart from accounting to the parliament after borrowing.

There is equally the need to conduct a cost benefit analysis on a loan facility before acquiring it and based on the result of the cost benefit analysis the relevant entities will be guided on whether to acquire the loan or reject it, this would save the country from acquiring very expensive loans which at the long run become a burden to the country. Currently that is not the situation currently where loans are acquired without emphasis on cost benefit analysis.

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[263] Elsie Addo Awadzi, "Designing Legal Frameworks For Public Debt Management," IMF Working Paper, July 2015. WP/15/147.

There is also need to improve our legal framework to take into account Islamic financial institutions lending to the country. To this end it is necessary to have compliance with the relevant sharia principles to enable borrowing by the government. The financial loans offered by Islamic financial facilities are not debts in the strict sense of it but are rather trust certificates as such the legal framework should envisage this and open other financial markets for borrowing by the country. Currently such arrangements are not recognized by law and the country can only have conventional loans from conventional banks.

Our country should also not be in a hurry to attain the middle income status if we are not ready this is because the concessional financing from the soft windows of multilateral development banks is likely to be faced out for middle income countries since development partners divert more budgetary resources towards the poorer and more vulnerable countries. Thus meaning that financing loans would be more expensive as there would be over realiance on non- concessional loans.[264]

Kenya may also need to implement the joint World Bank- IMF sustainability framework for low income countries to achieve debt sustainability on the new borrwings from concessional official loans.[265] This would lead to access of sustainable debt and would help in avoiding risks related to debt distress.[266]

There is also need to embrace Public Private Partnerships, essentially for infrastructure developments which are capital instensive, longterm projects. This would help on reducing over

[264] United Nations, Conference on Trade and Development, Economic Development in Africa: Debt Dynamic and Development Finance in Africa, 8th August 2016. Accessed at https://unctad/meetings/en/sessionaldocuments/tdbex63d3-en.pdf. Accessed on 10/6/2019.
[265] Ibid
[266] Ibid.

reliance on commercial loans which are expensive to finance infrastructure. They can also be used to circumvent national or IMF agreed debt limits.

It is important to note that illicit financial flows could become a source of development finance as long as efforts to tackle them at national and international levels are sustained. This is crucial since Africa lost about $ 854 billion in such flows from 1970 to 2008,[267] this sum is nearly equivalent to all official development assistance received during the same period. Recovery initiative should be fully brought on board duplication while leveraging on their experiences and best practices and the vital role of civil society in monitoring transparency should be recognized and used to provide extra vigilance.[268]

It is equally important to notice that this research has not dealt with the role of governance in the external public debt in Kenya, this can form a basis for future research.

[267] Supra n 291.
[268] Ibid.

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