



REPUBLIC OF KENYA

COUNTY GOVERNMENT OF NYERI

COUNTY TREASURY

**MEDIUM TERM DEBT MANAGEMENT
STRATEGY PAPER**

2018/19-2020/21

FEBRUARY, 2018

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FOREWORD

The 2018/2019-2020/2021 Medium Term Debt Management Strategy is prepared in accordance with section 123 of the Public Finance Management (PFM) Act 2012 and is consistent with county government development policies and strategies. The main objective of MTDMS is to ensure that the county government financial needs and payment obligations are met at the lowest possible cost in the market, which is consistent with a prudent degree of risk, while ensuring that the overall level of public debt is sustainable.

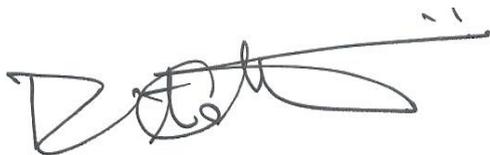
The sustainability of debt is a key fiscal responsibility principle and this, among other issues, will be dealt with in this document. Through a resolution of the Nyeri County Assembly as required under the PFM Act section 107 (2) (e) and section 107 (4) that deal with sustainability of debt, an annual borrowing limit has been set for any future requirements.

The County Treasury shall ensure that the medium-term debt management strategy is aligned to the broad strategic priorities and policy goals set out in the County Fiscal Strategy Paper. The Policy goals and strategic priorities are geared towards unlocking the potential of our people through a robust social-economic investment in line with the CFSP, 2018.

The county government inherited a huge debt from the four defunct local authorities i.e. Nyeri County Council, Nyeri Municipal Council, Karatina Municipal Council and Othaya Town Council. The inherited debt will continue to increase the county debt burden and to ensure sustainability the MTDMS has proposed measures to be undertaken to reduce the debts to a manageable level.

Considering the current level of debt, both inherited and county pending bills, the 2018/2019-2020/2021 MTDMS largely proposes strategies on how to reduce the current debts level and how to manage future debts if they will ever occur. The county will endeavor to ensure that both the burden of and benefit from public borrowing is shared equitably between the current and future generation as stipulated under Article 201 of the Constitution.

Further, the county government will form a debt management committee, within the County Treasury, and build its capacity in terms of staffing and training to ensure that it is in a position to handle all matters relating to borrowing and servicing of debt. Effective linkages will be established with the National Treasury to facilitate the management of the inherited debts, future borrowing and provision of technical advice.



Robert Thuo Mwangi,
C.E.C.M - FINANCE AND ECONOMIC PLANNING

ACKNOWLEDGEMENT

The 2018/2019-2020/2021 MTDMS is intended to ensure accountability and transparency in management of the county public debt. The review and preparation of the medium term debt management strategy is done annually in accordance with section 123 of the PFM Act, 2012. A public debt is a charge on the County Revenue Fund, though an Act of the County Assembly may provide for charging all or part of the public debt to other established public funds.

In the year 2014, the county government, in conjunction with the Transition Authority compiled a report on the Assets and liabilities inherited from defunct local authorities and verification process has been concluded but are yet to be officially handed over to County Government. The previous BPS, envisaged the transfer to be concluded by March 31st, 2017 but this was never actualized.

To enhance debt management in the county, the County Treasury will endeavor to establish a debt management committee that will be mandated to prepare the debt management strategy and to give comprehensive, accurate and timely information. The establishment of the committee will lay the ground for future borrowing to finance the budget and servicing of outstanding debt. Despite the establishment of the committee the overall control and accountability remains with the C.E.C.M - Finance and Economic Planning.

The MTDMS will formally be submitted to the Commission on Revenue Allocation (CRA) and the Intergovernmental Budget and Economic Council as per PFM Act 2012. In addition, MTDMS strategy will be published and made available at the county website, www.nyeri.go.ke, to ensure wide circulation as envisaged under the PFM Act, 2012.

Let me take this opportunity to acknowledge the C.E.C.M – Finance and Economic Planning for his overall leadership, Chief Officer Finance and Accounting for the support during the preparation of MTDMS, the entire staff of the department of Finance and Economic Planning for spending substantial amount of time putting together this MTDMS and ensure it was produced on time while maintaining the expected standards.



Francis Maranga Kirira
C.O. - ECONOMIC PLANNING

Abbreviations and Acronyms

BPS	Budget Policy Statement
CBROP	County Budget Review and Outlook Paper
CFSP	County Fiscal Strategy Paper
CRA	Commission on Revenue Allocation
Kshs.	Kenya Shilling
LAPFUND	Local Authority Provident Fund
LAPTRUST	Local Authority Pension Trust
LGLA	Local Government Loans Authority
MTDS	Medium Term Debt Management Strategy
NSSF	National Social Security Fund
PFM	Public Finance Management
TA	Transition Authority
MTDMS	Medium Term Debt Management Strategy
CECM	County Executive Committee Member
IGRTC	Intergovernmental Relations Technical Committee
NHIF	National Hospital Insurance Fund
VAT	Value Addition Tax
PAYE	Pay As You Earn
NHC	National Housing Corporation

**LEGAL BASIS FOR PUBLICATION OF MEDIUM TERM DEBT MANAGEMENT
STRATEGY PAPER**

The debt management strategy is published in accordance with section 123 of the Public Financial Management (PFM) Act, 2012. The law states that:

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

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

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

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

(c) The principal risks associated with those loans;

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

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

As soon as practicable after the statement has been submitted to the county assembly under this section, the County Executive Committee member for finance shall publish and publicize the statement and submit a copy to the Commission on Revenue Allocation and the Intergovernmental Budget and Economic Council.

EXECUTIVE SUMMARY

The 2018/2019-2020/21 Medium Term Debt Strategy Paper has been prepared in accordance with PFM Act, 2012. The preparation of the strategy is in line with fiscal responsibility principles and is interlinked with other budget documents such as departmental reports, county budget review and outlook paper, annual financial statements and county fiscal strategy paper.

The county government inherited approximately Kshs 592,807,561.54 from defunct local authorities i.e. Nyeri County Council, Nyeri Municipal council, Karatina Municipal council and Othaya Town Council; and Kshs 28,464,516.32 from Devolved ministries/departments. In dealing with inherited debts, the county treasury through the help of the Transition Authority has been verifying liabilities inherited from these former local authorities.

The inherited debt together with pending bills arising from county government ministries has caused a sharp rise in debt since the county government assumed power. As at 30th June, 2016 the county debt was Kshs. 690,016,852.54 comprising of inherited debt of Kshs. 592,807,561 and pending bills from county government departments amounting to Kshs 712,444,170.13.

To reduce the county debt to manageable levels sufficient funds, as budgetary reserves, will be allocated in the budget to cater for debt repayment especially the pending bills from the last financial year. The County Treasury requires Kshs. 712 million to settle pending bills during the financial year 2017/18, however only Kshs. 516 Million have been allocated as per the approved supplementary budget for FY 2017-2018. In dealing with the other substantial liability inherited, once they are handed over, the county government will negotiate with creditors to spread the debt burden for a few year since the fiscal space may not accommodate all the payments in one year.

To reduce future pending bills from the departments, all county entities will be required to reprioritize their projects and programs and align their expenditure to availability of funds and cash flow forecast. In addition, procurement in the fourth quarter of the year should be discouraged to avoid huge pending bills. The pending bills will be cleared as a first charge in the approved budget, to avoid accumulation, as provided for under section 41(2) of the Public Finance Management (County Governments) Regulations, 2015.

The County Treasury will create and strengthen a debt management committee to handle matters relating to borrowing and management of county debt. The County Treasury will also continue to work closely with the National Treasury to enhance the capacity building of staff and also offer technical expertise in issues relating to borrowing and repayment of debts especially those inherited from the defunct local authorities.

1 INTRODUCTION

1.1 Background

The debt management strategy is prepared in accordance with section 123 of PFM Act, 2012 which requires the County Treasury to submit to the County Assembly a statement setting out the debt management strategy of the county government over the medium term with regard to its actual liability and potential liability and its plans for dealing with those liabilities. The statement should, among other information, contain:

- (a) The total stock of debt as at the date of the statement;
- (b) The sources of loans made to the county government;
- (c) The principal risks associated with those loans;
- (d) The assumptions underlying the debt management strategy; and
- (e) An analysis of the sustainability of the amount of debt, both actual and potential.

There are other section of PFM Act that guides the management of county debt, this include PFM Act sections 107, 140,141,142,143 and 144. Other documents that guide the preparation of debt management strategy are county fiscal strategy paper (CFSP) and county budget review and outlook paper (CBROP).

In this MTDMS more emphasis has been put in ensuring the sustainability of the current debt and establishment of necessary structures to facilitate future borrowing. The County Fiscal Strategy Paper, 2017 does not envisage any borrowing to finance the budget and therefore the MTDM strategy will be geared toward servicing of existing debt. With the current level of debt the county government may not be able to accommodate additional borrowing to finance it expenditure therefore over the medium term the government will put more emphasis on servicing of existing debts namely those inherited from the defunct local authorities and the pending bills.

The County Treasury will form a debt management committee to verify all liabilities inherited from the defunct local authorities once the handing over is conclude by the National Treasury, and the pending bills. The main goal of this exercise will be to establish the debt position of County Government of Nyeri and ascertain the borrowing power available.

The debt management committee will be expected to undertake the following;

- a) Compile list of all creditors both statutory and sundry.
- b) Establish whether the claims are genuine or not.
- c) Establish whether all procedures were followed in incurring the debts.
- d) Establish whether all supporting documents are available.
- e) Prioritize the debt.

The establishment of the committee is the first step in ensuring that the county government is in a position to handle its current debt and is ready to undertake future borrowing to finance the budget within the legal framework.

1.2 Objective of debt management

The following are the main objectives of debt management in the county;

- a) To ensure the financial needs and payment obligations of county government are met at the lowest possible cost in the market and is consistent with a prudent degree of risk.
- b) To ensure that the overall level of public debt is sustainable and debt shall never exceed twenty (20%) percent of the county governments total revenue at any one time as stipulated in the Public Finance Management (County Government) Regulations section 25 (1)(d).
- c) To ensure that both the burden of and benefit from public borrowing is shared equitably between the current and future generation as stipulated under Article 201 of the constitution.

1.3 Scope of Medium Term Debt Management Strategy

The Medium Term Debt Management Strategy (MTDMS) covers actual and potential liability i.e. it covers all loans and other debt, whether inherited or created by the county government, that require payment of principal with or without interest by the county government to the creditor at a date or dates in future. The MTDMS is prepared for financial year 2018/19 but also makes projection for year 2019/20 and 2020/21.

2 REVIEW OF NYERI COUNTY PUBLIC DEBTS

2.1 Stock of debt

The total stock of debt as at 30th June 2016 stood at Kshs. 1,305,251,731.67. This comprises of both inherited debt, though unverified, of Kshs. 592,807,561.54 and county government pending bills amounting to Kshs. 712,444,170.13. This was a great difference as compared to the pending bills of Kshs 97,209,291 in the financial year 2015/2016. This can be attributed to the late disbursement of funds by the National Treasury and effects emerging from the electioneering period for the general election.

However the county debt from pending bills is projected to be approximately 600 million by 30th June, 2018 since most of the development activities are being implemented in the second half of the financial year 2017/18 after the lengthy electioneering period and subsequent supplementary budget making and approval process.

2.2 Source of loans/debts made to the county government

The source of debt to the county government will be categorized into two namely;

1. Pending bills arising from works done and not paid during the financial year 2016/2017.
2. Inherited debt from defunct local authorities

2.2.1 Pending bills from the County Departments.

The county government accumulated huge pending bills from departments during the financial year ending 30th June, 2017 amounting to Kshs. 712,444,170.13. This was attributed to late disbursement of the last tranche of equitable share from the national treasury and therefore the county exchequer was received on 30th June, 2017.

Further, failure by the county government to achieve its local revenue target by a total of Kshs. 451,961,847 could have led a huge deficit if contracts signed during the financial year 2016/2017 were executed during the year. Further, some activities suffered from the pre-election dynamics especially towards the end of the financial year. It is important to note that the process of procurement in the IFMIS system was stopped in May, 2017 that no further commitment was allowed after contributing majorly to the high amount of pending bills.

The summary of pending bills for the county by departments, as reported, is shown in the table below;

N O.	DEPARTMENT	RECURRENT		DEVELOPMENT	TOTAL	REMARKS
		Compensation to employees	Use of goods and services	KSHS	KSHS	
1.	Office of the Governor	0	2,301,701.00	0	2,301,701.00	
2.	Office of the County Secretary	0	84,906	7,400,000.00	7,484,906.00	
	Unpaid Legal Fees, Court Awards and Interest	0	25,483,540		25,483,540	County cases
3.	Finance and Economic Planning	0	2,560,468.70	1,862,183.00	4,422,651.70	
4.	Lands, Housing and Physical Planning	0	1,250,000	27,595,604.00	28,845,604.00	
5.	Health Service and Sanitation	5,085,374.40 *	54,330,865	0	59,416,239.40	*Payment for casuals
6.	Special Programmes Youth and Sports	0	2,037,975	0	2,037,975.00	
7.	Public Administration, Information and Communication	0	10,327,682.70	3,152,695.60	13,480,378.30	
8.	Agriculture, Livestock, Fisheries and Cooperative Development	0	13,079,940.80	1,268,825.00	14,348,765.80	
9.	Education ICT, Trade and Industrialization, Tourism and Culture	0	4,258,252.29	50,718,274.52	54,976,526.81	
10.	Water, Irrigation, environment and Natural Resources	0	309,672.00	106,285,152.84	106,594,824.84	
11.	County Public Service Board	0	1,458,215.00	0	1,458,215.00	
12.	Roads and Infrastructure	0	5,037,416.72	385,779,125.56	390,816,542.28	8 KM and affirmative action Roads Programme
13.	Energy	0	776,300.00	0	776,300.00	
	Total	5,085,374.40	123,296,935.21	584,061,860.52	712,444,170.13	

Source: County Treasury, 2017

While pending bills are considered as those payment vouchers which had reached the treasury and not settled, there were other contracts which had been signed but not executed by the end of the financial year, 2016/2017, which can easily lead to accumulation of debts if not considered in the supplementary budget for the financial year 2017/2018.

2.2.2 Inherited debt from defunct local authorities

The Budget Policy Statement, 2017, indicated that to finalize the transfer of assets and liabilities from the defunct LAs to the County Governments, a Legal Notice Vol. CXIX-No.13 was prepared and published on 27th January 2017 to facilitate this transfer process. Among assets and liabilities of the defunct LAs covered in this process are:

- i) pending bills;
- ii) Tax arrears;
- iii) Statutory deductions relating to the National Hospital Insurance Fund (NHIF), National Social Security Fund (NSSF), Pension Funds, VAT and PAYE.

In this context, County Assets and Liabilities committees were formed to identify, verify, and validate the assets and liabilities of the defunct LAs as at 27th March 2013. This exercise has been concluded, and Intergovernmental Relations Technical Committee (IGRTC) is currently leading an exercise to validate the report as a basis to implementing its recommendations.

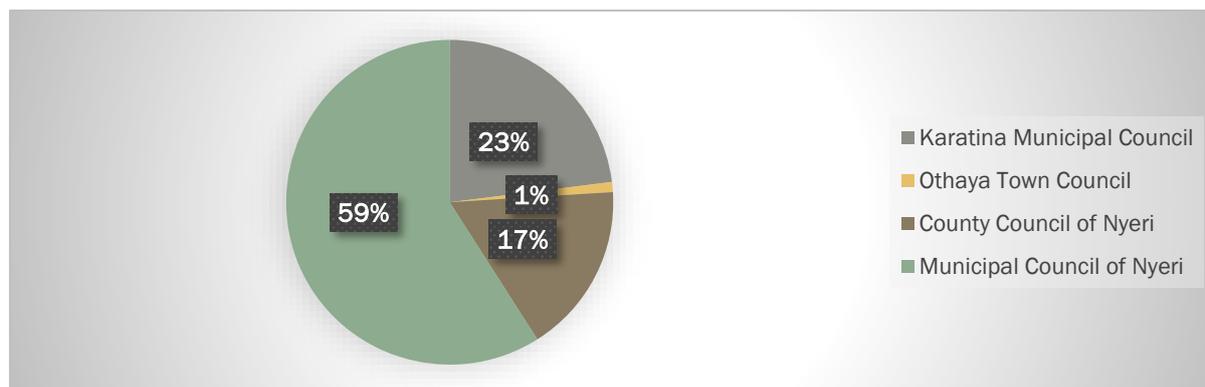
The inherited debt as reported by all defunct local authorities is shown in the table below;

Defunct local authority	Outstanding Debt as at 30th June 2013
Karatina Municipal Council	137,505,036.75
Othaya County Council	5,262,092.09
County council of Nyeri	100,917,404.70
Municipal Council of Nyeri	349,123,028.00
Total	592,807,561.54

Source: Nyeri County Assets and liability report, 2014

Most of the debt were inherited from defunct municipal council of Nyeri with 59% of the total debt inherited, followed by Municipal council of Karatina with 23%. County council of Nyeri had 17% while Othaya Town Council had the least debt inherited with only 1% of the total debt.

2.2.3 Outstanding Debt as at 30th June 2013



Source: Nyeri County Assets and liability report 2014

A detailed analysis on specific debts are shown below per defunct local authority;

(a) Defunct Municipal Council of Nyeri

Item	Debt as at 31st December 2014
Loan from LGLA	320,319,642
Unpaid emoluments	3,544,357
Creditors	25,259,029
TOTAL	349,123,028

(b) Defunct Town Council of Othaya

Item	Debt as at 31st December 2014
LAPTRUST	2,582,956
LAPFUND	267,250.09
Creditors	2,411,886
TOTAL	5,262,092.09

(c) Defunct Municipal Council of Karatina

Item	Debt as at 31st December 2014
Loan from LGLA	38,931,070.20
Loan from NHC	258,929
Unpaid emoluments	7,401,096
LAPTRUST	15,488,531.56
LAPFUND	3,533,102.20
Creditors	71,892,307.79
TOTAL	137,505,036.75

(d) Defunct County Council of Nyeri

Item	Debt as at 31st December 2014
Unpaid emoluments	17,573,065
NSSF	26,927,359

LAPTRUST	3,558,619
LAPFUND	34,510,344.70
Creditors	18,348,017
TOTAL	100,917,404.70

2.3 Assumptions underlying the debt management strategy

The county government will continue to pursue the fiscal responsibility principles and policies outlined in the County Fiscal Strategy Paper. This will help the government to reorient expenditure to priority programmes in roads and infrastructure, water, health, education and agriculture and avoid accumulation of pending bills in the county.

Over the medium term, the aim of the county government is to continue maintaining a balanced budget where total revenue will always equal to total expenditure i.e. the MTDM strategy does not envisage borrowing to finance the budget and over the medium term the focus will be on ensuring the sustainability of current debt. As provided under the PFM Act (County Government) Regulations, 2015, section 177 (2)(b), the county shall consider an overdraft from Central Bank of Kenya in event of cash flow problems.

Revenue growth is expected to be maintained as earlier projected in the budget review and outlook paper (CBROP) i.e. at 10% in each subsequent financial year. This will ensure that sufficient resources are allocated toward debt servicing and ensure that the current levels of debt falls below 10% of the total budget by year 2018/19.

2.4 Sustainability of debt

The sustainability of debt is guided by PFM Act section 107 (2)(e) and section 107 (4). According to section 107 (2)(e) the county debt shall be maintained at a sustainable level as approved by county assembly. Section 107 (4) further states that every county government shall ensure that its level of debt at any particular time does not exceed a percentage of its annual revenue specified in respect of each financial year by resolution of the county assembly. For the case of Nyeri County Government the percentage has been set at five percent but should never exceed twenty per cent.

The National Government is required to maintain public debt at sustainable levels as set out in the Public Finance Management Act 2012, and its regulations. According to BPS, 2018, our national debt ratios compared with internationally recognized thresholds continue to show that our debt level remains sustainable. The baseline public debt path remains consistent with the

EAC convergence ceiling of 50 percent of GDP. External debt sustainability indicators illustrate that Kenya remains within the sustainable bounds. This is attributed to the large portion of debt that is on concessional terms in terms of low costs and long term maturity. This funding continues to play a key role in the development agenda of the National Government and subsequent funding of counties.

The county government recognizes the need to manage debt prudently to avoid unwarranted debt burden. At the County Treasury the debt management committee will be mandated to ensure that there is prudent debt management and that the debt level is sustainable. The County Treasury acknowledges the need to maintain debt at sustainable levels and is closely monitoring spending by departments and other spending units and is working with all entities to cut on possible pending bills.

The current debt (both inherited and pending bills) is about 16.5% of the annual revenue, the County Assembly of Nyeri has set the debt to revenue ratio at 5 percent and thus the burden is considered high in the medium term and thus the level is considered unsustainable due to the requirement that at least 30 per cent of the county budget must be allocated development.

3 STRATEGIES OF DEALING WITH DEBT

3.2 Debt servicing

The inherited debts must be paid, once the handing over has been concluded, and this may require the county government to set aside sufficient funds in the 2018/19 budget to repay part of them if not all as it will be negotiated with the statutory institutions and other creditors. As indicated earlier the total stock of debt as at 30th June, 2017 was Kshs. 0.712 billion. To reduce this debt to manageable levels a minimum of Kshs 100 million should be set aside in the budget for debt repayment, however, the actual ceiling will be firmed up in County Fiscal Strategy Paper, 2018 after considering all sectors requirement vis a vis the funds available.

3.3 Debt Restructuring

Apart from debt servicing, the county government is exploring the possibility of debt restructuring as one method of dealing with huge debts particularly for bank loans and pension funds inherited from the defunct local authorities once the handing over is concluded. This will spread the debt burden over a period of time since the existing debt cannot be cleared within a year due to budgetary constraints. Restructuring will also help the county to avoid payment of penalties and interest that have accrued and costly legal battles.

3.4 Prioritization of programmes

The pending bills arising from all departments will be cleared as with the funds allocated in the 2017/18 supplementary budget to avoid further accumulation of debts as provided for under section 41(2) of the PFM (County Government) Regulations, 2015. Departments will also be required to prioritize projects/programmes in cognizance of resource constraints. The County Treasury shall prepare a report on cash flow projections in early April, 2018 so as to advice on commitments to avoid pending bills by the end of the financial year as per section 44(5) of the PFM (County Government) Regulations, 2015. This might compromise implementation of some of the critical projects/programmes as well as service delivery but it is a necessary measure in ensuring that the county does not accumulate debts in succeeding years.

4 IMPLEMENTING THE 2018/19-2020/21 MTDMS

Upon the approval of this strategy the Department of Finance and Economic Planning will develop a program for pending bills repayment based on priorities and cash flow forecast.

The debt management committee, which, will be based at the County Treasury will review all pending bills from the departments and make recommendation for payment or otherwise as it deem fit as a new financial year starts. This will ensure that all pending bills approved are settled as a first charge in the budget. The County Assembly has set the ceiling for borrowing at 5 percent of the county revenue and the County Treasury shall provide a budgetary allocation for payment of pending bills. This will not only guide the sustainability of debt but will also lay the ground for future borrowing to finance the budget.

Negotiation with various parties' owed substantial amounts of money will be fast tracked once the handing over of assets and liabilities is concluded. The government will strive to ensure that the negotiations are concluded by the end of June 2017 so that implementation of the agreement(s) can start at the beginning of year 2017/18. Timely conclusion of these agreements will facilitate their inclusion in 2017/18 debt repayment program.

The County Treasury will create and strengthen the proposed debt management committee in terms of staffing, training and provision of working tools and equipment to ensure that the office is in a position to give comprehensive, accurate and timely information on debt. In addition, effective linkages will be established with the National Treasury to facilitate training on debt management techniques and offer guidance and support on future borrowing. The national government is expected to guarantee borrowing by county governments and therefore the National Treasury plays a critical role in ensuring the success of debt management in the county.

5 CONCLUSION

The 2017/2018-2019/2020 Medium Term Debt Management Strategy is a forward looking framework that describe the sustainability of the county debt in the medium Term. Even though the current debt level is high it is sustainable, however it is important that the county government continue to implement prudent debt management practice and policies to avoid unmanageable debt levels. The high debt levels calls for sufficient allocation of funds in the 2018/2019 budget and consecutive budgets in order to improve the debt position and avoid unnecessary cost such as interest and penalties especially from the statutory bodies.

The current stock of debt is in approximately 0.712 billion and 0.592 as pending and inherited debts from the defunct local authorities respectively. However, in the 2017/2018 approved supplementary budget estimates, the government have provided a total of Kshs. 526 million towards payment of pending bills. This clearly illustrates that the county government may not be able to settle all the debts in year 2017/18 and some will have to be schedule to the subsequent years in the medium term.

The county treasury conducted a pending verification exercise to determine authenticity and a report has been produced on their status. This report will guide the settlement of the bills. However, since this MTDMS envisages no borrowing to finance the budget more emphasis has been put on management of current debt. Henceforth, all county departments and other entities are expected to be more conscious while spending and ensure that projects and programmes implementation is in line with the approved budget and availability of fund at the County Treasury.

Procurement processes should be concluded before the end of third quarter to avoid pending bills in subsequent years. Further it is expected that the National Treasury will be releasing the exchequer as per the agreed cash flow schedules.