

# Contracting of External Loans For Public Development Project by The National Treasury

Presentation By SAI-KENYA

# Background

- Bulk of borrowing is to cover fiscal deficit. (Audit of Public Debt Management Handbook for Supreme Audit Institutions, August 2020).
- This act of borrowing where government considers and negotiates the terms and conditions offered by different potential lenders, and formulates these binding agreements, defines Loan Contracting (Public Debt and Borrowing Policy, 2020).
- Growth of Deficit vis a vis Borrowing External Loans .
- Legal and Institutional Framework

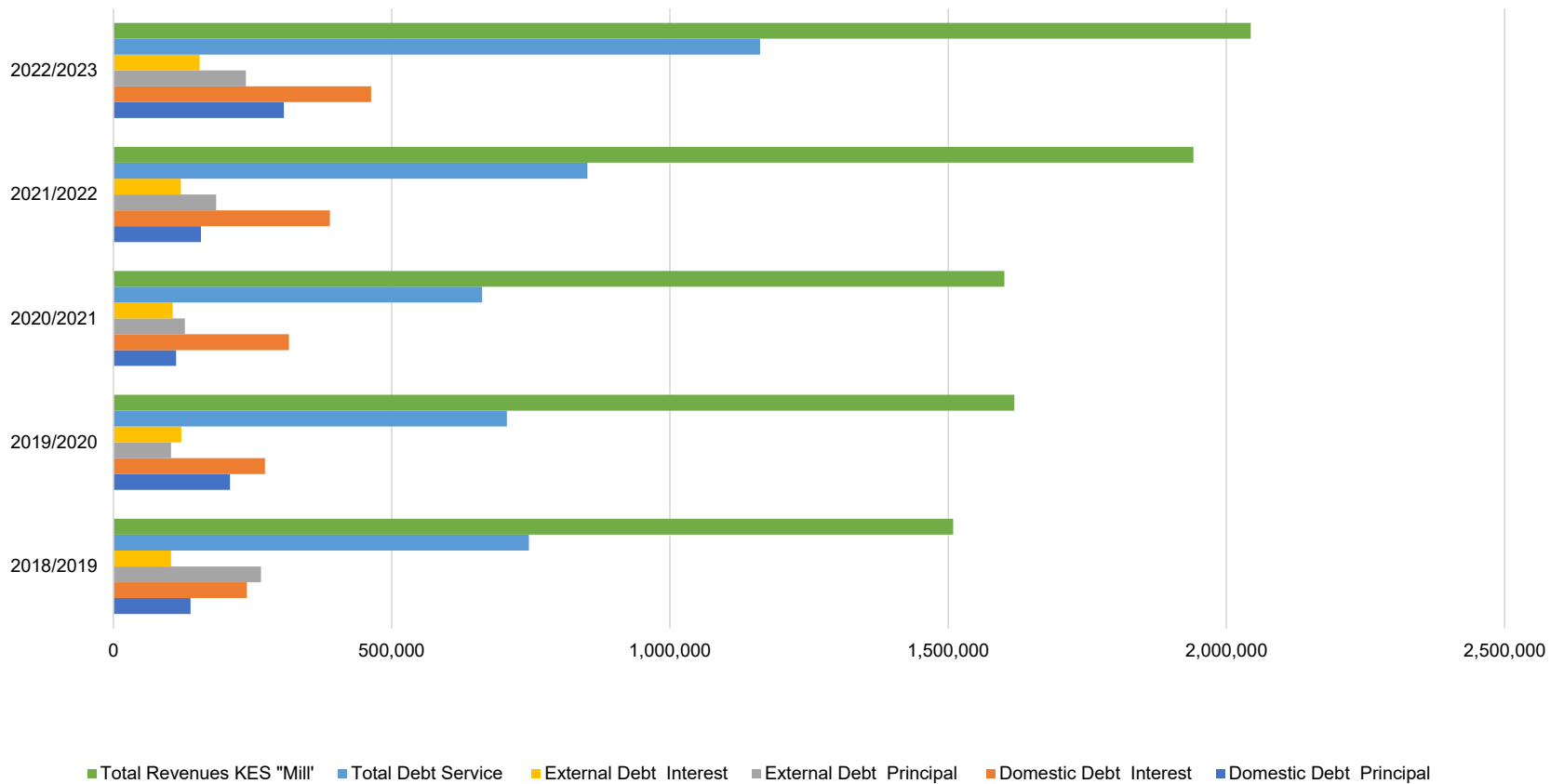
# Risks/Motivation



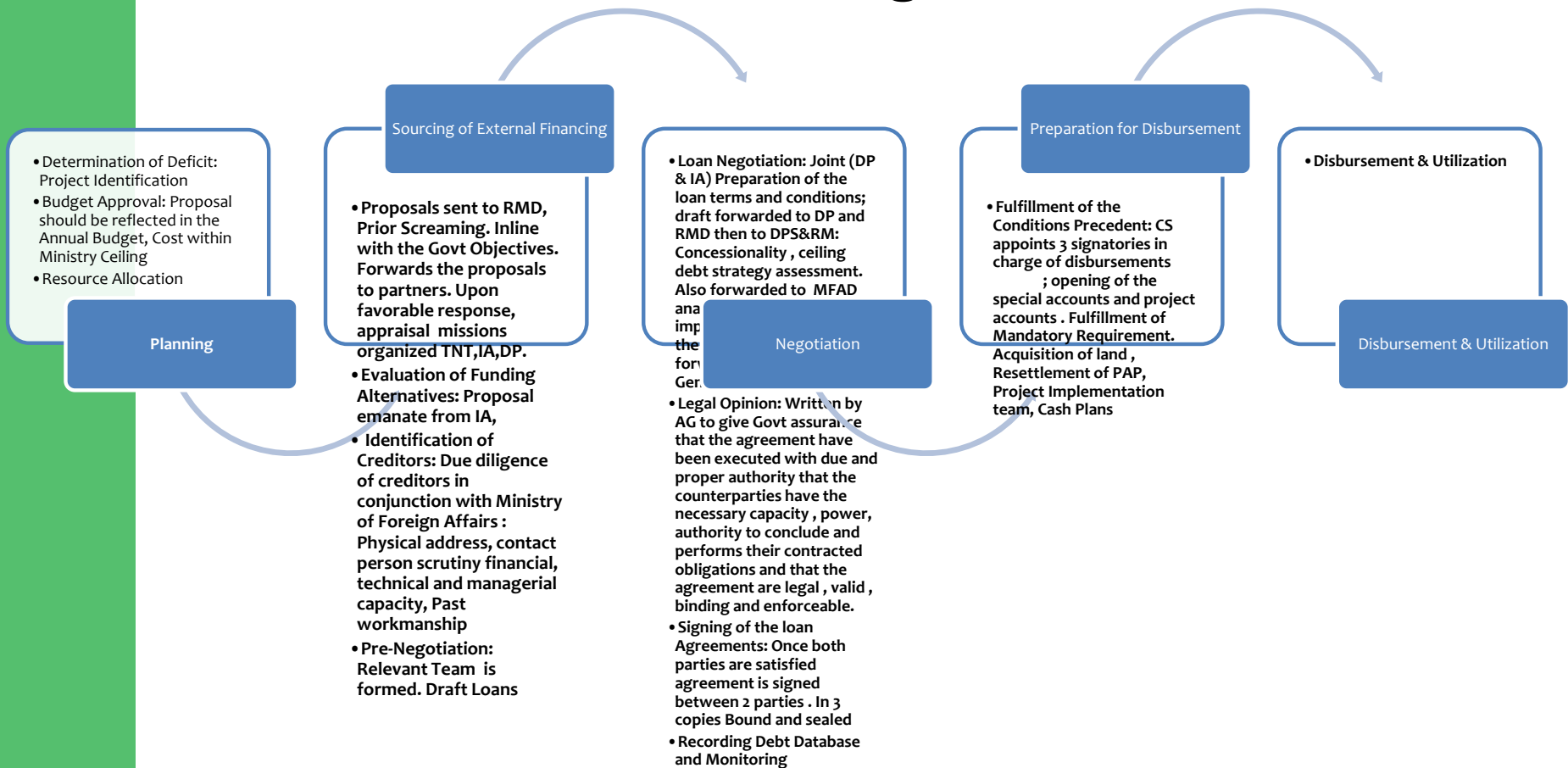
- Excessive levels of external debt + poor debt management can hamper a country's ability to invest in their economic future as external debt is usually denominated in the currency of the lender's country, not the borrower. This means if the currency in the borrowing country weakens, it becomes much harder to service those debts.
- Financing for Sustainable Development Report identifies a “great finance divide” – the inability of poorer countries to raise sufficient resources and borrow affordably for investment - UN Sustainable Development Report, 2020. Thus there is need to address financing gaps, rising costs of borrowing and heightened debt risks.
- GoK Paid commitment fees of Kshs.5,357,470,000 in the three years on undisbursed external loans payment (Annual Public Debt Reports for the financial years 2019/2020 to 2021/2022).
- Therefore there is need to address financing gaps, rising costs of borrowing and heightened debt risks.

# Kenya's Debt servicing trends

Debt Servicing Expenditures Vs Total Revenues (KES "Mill")



# Loan Contracting Process.



# Objective



To assess if measures put in place by The National Treasury (TNT) ensures that external loan contracting is done effectively to minimize cost and risk of borrowing.

## **The specific audit sub-questions :**

- Are there adequate measures in place for guiding identification, planning and approvals of projects before loan signing?
- Does the measures put in place by TNT ensures adequate assessment of credit terms and conditions before signing of the loan agreements?
- Do the measures put in place by TNT ensure all conditions precedent are met on time and funds are disbursed as per agreed schedules?
- Does the monitoring and evaluation mechanisms put in place by TNT ensures that project funds are utilized accordingly as per the project loan requirements?

# SCOPE

- The audit team examined the external loan contracting processes in SAI Kenya as conducted by The National Treasury and as guided by the PIM Guidelines, 2020
- The team carried out field verification on inspection of sampled projects in six (6) counties.

# Results

## Legal and Structural Arrangement

- Inadequate operationalization of PIM Guidelines 2020: Proposal scrutiny and preparation in the loan uptake and monitoring of the project
- Reorganization from External Resource Department to Resource Department,
- Inadequate Alignment, Revision, Policies & Draft Manuals.

## Project Identification and Preparation

- No involvement in the intended beneficiaries during project identification. Top bottom approach . highly centralized and has disconnect from grassroots beneficiaries
- Delays in Fulfilment of Mandatory Loan Requirements/Precedent Loan Conditions
- Limited leadership, ownership, social accountability and sustainability.

## Inadequate Creditor Assessment

- Limited Credit Comparisons.
- Framework Agreements already with identified creditors and in some cases, the creditor has already financed a feasibility study.
- Inadequate Evaluation of Credit Terms: Only concessionality dome
- Analysis i.e. currency, penalty fees and other charges, disbursement and maturity profile and impact on existing debt service profile left out . This was attributed to inadequate staff and skills in the Debt, Policy, Strategy and Risk Management Department

## Inadequate Monitoring and Evaluation of Contracted Loans

- Inadequate governance & structure: Inter-Agency coordination,
- Inadequate enforcement of implementation of the National Treasury Circular



# Recommendation



The National Treasury should strengthen its external loan contracting processes to minimize borrowing costs and risks. This can be achieved by:

- Implementing stricter measures to ensure thorough project identification, planning, and approvals before finalizing loans.
- Enhancing the assessment of credit terms and conditions to avoid unfavorable loan agreements.
- Establishing clear mechanisms to guarantee timely fulfillment of all conditions precedent for loan disbursement and avoid unnecessary commitment fees.
- Developing robust monitoring and evaluation frameworks to ensure project funds are used efficiently and exclusively for their intended purposes

# Conclusion



- The National Treasury's efforts to guide loan contracting processes through policies and checklists have not been sufficient to ensure efficient and cost-effective borrowing.
- The audit identified weaknesses in project identification, planning, loan term assessment, disbursement conditions, and project fund monitoring.
- These weaknesses have led to project delays, feasibility study redesigns, potentially unfavorable loan terms, and potential misuse of funds.

**THE END**