Ubiquity Consulting Ltd

KENYA

BUDGET HIGHLIGHTS

2019-2020

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ECONOMIC OVERVIEW

Sub-Saharan Africa

The Sub-Saharan Africa regional economy is projected to expand 3.3% in 2019, down 0.1 %age points from last month's forecast. For 2020, the region is forecast to expand 3.7%.
Elevated global trade tensions, commodity-price volatility, adverse weather shocks and policy uncertainty represent key downside risks to the outlook.
Inflation in Sub-Saharan Africa rose to 8.6% in March (February: 8.3%). Higher fuel prices in South Africa and accelerating inflation in Zimbabwe primarily drove the uptick. Price pressures are expected to ease going forward, in large part due to more stable exchange rates. A preliminary estimate for April indicates that inflation climbed to 9.0%.

India

According to IMF estimates, India's economy grew 7.1% in FY19 and is expected to accelerate to 7.3% growth this fiscal and to 7.5% in FY21. All the estimates are 0.2 %age points less than its previous assessment in January. Private-sector PMI data in April hinted at potentially quicker economic growth going forward despite easing to the lowest reading since September 2018, as businesses were optimistic that economic conditions would improve once the political dust settles. Despite softer growth, the Indian economy remains one of the fastest growing and possibly the least affected by global turmoil.

Middle East and North Africa

Growth prospects for the Middle East and North Africa are deteriorating on the back of elevated geopolitical risks, weak global demand and severe oil production cuts. Moreover, escalating trade tensions between China and the United States threaten to hit global economic growth, which could, in turn, reduce demand for the black gold.

UK

Britain's economy strengthened in the first three months of the year, with growth of 0.5% helped by unprecedented stockpiling by manufacturers fearful of the impact from a no-deal Brexit.

It was an improvement on 0.2% growth in the previous three months and was bolstered by the strongest quarterly performance for manufacturers since 1988, with factory output up 2.2%, according to the figures from the Office for National Statistics. The slow-burn impact of Brexit on the British economy will be a drag on growth for the rest of 2019, blocking the Bank of England from raising interest rates, a leading economics forecaster has warned.

Eurozone

Flash estimates revealed that growth surpassed expectations in the first quarter of the year, reviving after last year's sharp slowdown.

- solid household spending likely supported the result as consumers benefitted from a tightening labor market.
- a relatively mild winter may have bolstered the construction sector,

Downside risks loom from an escalation of trade tensions, a slowdown in China, market volatility and lingering weakness in the manufacturing sector. Our panel left the Eurozone's outlook unchanged this month after six downgrades, taking a wait-and-see approach after the positive Q1 outturn. Growth is seen at 1.2% in 2019 and 1.4% in 2020.

USA

The U.S. economic outlook is healthy according to the key economic indicators. The most critical indicator is the gross domestic product, which measures the nation's production output. The GDP growth rate is expected to remain between the 2% to 3% ideal range. Unemployment is forecast to continue at the natural rate.

Growth will slow this year, with higher interest rates, fading fiscal stimulus and lower global growth weighing on activity. However, a strong labor market and solid wage gains should support private spending. An all-out escalation of the trade war with China is by far the largest downside risk, with trade uncertainty likely to persist even if a deal is reached going forward.

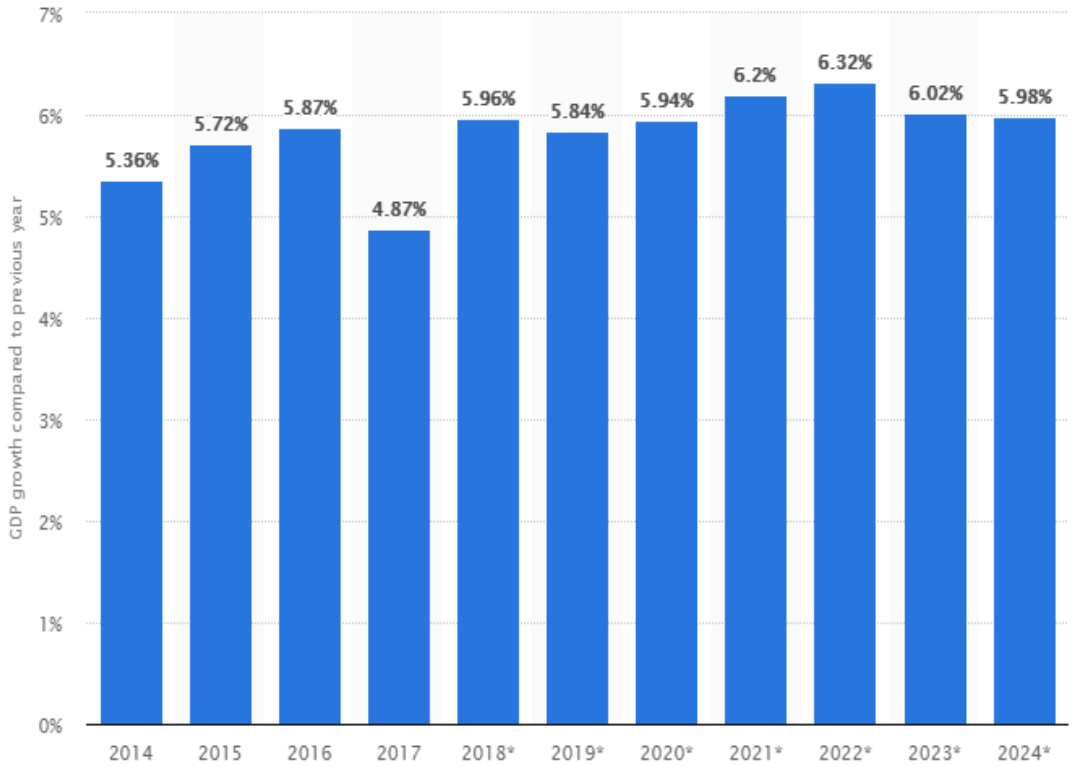
U.S. GDP growth will slow to 2.1% in 2019 from 3% in 2018. It will be 1.9% in 2020 and 1.8% in 2021.

China

China's economy, despite sizeable challenges such as trade tensions and the unfinished deleveraging campaign, will see its GDP grow at a respectable rate of around 6.2 %. So far in 2019, the Renminbi has performed strongly, as a result of the ongoing trade talks. Even a temporary suspension of conflict would improve the rather subdued sentiment in China and the region, triggering equity rallies and bolstering battered regional currencies

Kenya Economic Outlook

Kenya's real gross domestic product is projected to grow by 5.7% in 2019, a slight decrease from the estimated 5.8% growth experienced in 2018. Growth in 2018 was driven by favorable harvests, a resilient services sector, positive investor confidence and a stable macroeconomic environment. So far in 2019, a strong pick-up in economic activity was underway for Q1 of 2019 as reflected by real growth in consumer spending and stronger investor sentiment.
Dry weather conditions, owing to a delay in the advent of the rainy season, has curbed agricultural output, causing a marginal fall in overall activity. Many firms have also highlighted problems with money circulation in the economy impeding activity.



GDP Annual Growth Rate

The Gross Domestic Product (GDP) in Kenya expanded 1.50 % in the fourth quarter of 2018 over the previous quarter. GDP Growth Rate in Kenya averaged 1.34 % from 2005 until 2018, reaching an all time high of 3.80 % in the third quarter of 2010 and a record low of -2.40 % in the first quarter of 2008.

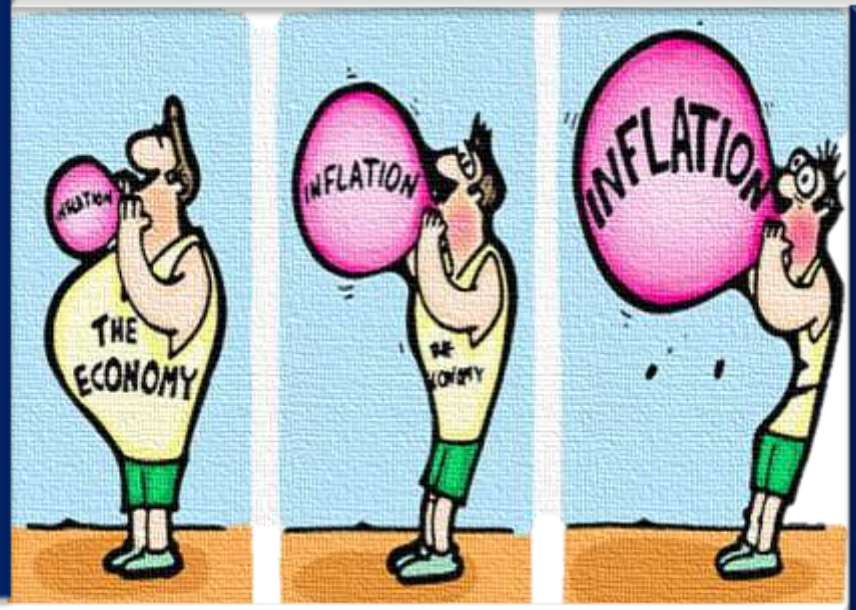
Inflation

Consumer prices fell 0.07% over the previous month in May, contrasting a 3.51% month-on-month upturn in April. Lower prices for food and non-alcoholic beverages, along with alcoholic beverages, tobacco and narcotics were behind the decline. Improved weather conditions likely boosted agricultural production and helped push down food prices.

Inflation slid to 5.5% in May from 6.6% in April, which had marked a 19-month high. Thus, inflation moved closer to the mid-point of the Central Bank's 2.5%–7.5% target range. Lastly, annual average inflation inched up to 5.0% in May from 4.9% in April.

Interest Rates

Monetary Policy Committee (MPC) of Kenya's Central Bank held the benchmark lending rate at 9.00%, where it has been since July 2018. The Bank opted to keep the rate stable despite a surge in price pressures in April, as inflation remained within the 2.5%–7.5% target band and is projected to fall in the near-term. Weather conditions are seen improving and pushing down food prices, while reduced usage of costly power services should ease electricity expenses.



Foreign Exchange Market

The Kenyan shilling (KES) shot up in value against the U.S. dollar amid renewed political stability, which has led to a resurgence in strong capital inflows. The foreign exchange market has remained relatively stable supported by increased tea and horticultural exports, strong diaspora remittances, and a continued recovery in tourism.

Balance of Trade

Kenya's Trade Balance recorded a deficit of 719.2 USD million in Mar 2019, compared with a deficit of 901.4 USD million in the previous month. Kenya's Total Exports reached 525.0 USD million in Mar 2019, an increase of 3.3 % year on year. Total Imports recorded 1.2 USD billion in Mar 2019, a decrease of 17.9 % year on year. The researchers project that Kenya's current account deficit will narrow in 2019 due to lower levels of imports and higher income from the tourism industry as well as rising diaspora remittances.

Sectorial Highlights

Tourism

In 2018, Travel and Tourism grew 5.6 % to contribute KShs.790 billion and 1.1 million jobs to the Kenyan economy.

This rate of growth is faster than the global average of 3.9% and the Sub-Saharan Africa average of 3.3%.

Kenya is counting on increased air connectivity within Africa to grow tourism numbers in 2019. The Tourism ministry projects the sector to register a 16% growth riding on the visa-on-arrival policy for Africans and the United States direct flights.

Major brands that that have announced Kenya expansion plans include Marriott International which will open at AVIC International's building in Westlands, Nairobi, and Hilton Hotel, which will open at The Pinnacle in Upper Hill.

Real Estate

The real estate market in 2018 was dynamic thanks to low-interest rates. However, the country has seen high mortgage rates of 12% to 15% on average and demand for affordable housing. Real estate continued its rise in 2018 but it was more contrasted. In fact, prices rose by + 3.8% on average, with spectacular increases in some cities such as Loresho (8.9%), Kitusuru (4.6%), Gigiri (4.6%), Spring Valley (2.6%), Langata (7.6%), Nyari (6.5%), Karen (2.1%).

The rising real estate prices have impacted the purchasing power of Kenya. The year 2019 will be marked by several regulatory changes and in particular the implementation of the current construction codes into Euro codes by January 2021.

For 2019 the property market outlook will be dominated by the

- economic developments,
- the effect of property demolitions
- the fragile legal environment over ownership rights.

Information and communications technology

In 2018, the ICT sector expanded by 12.9% to KShs.390.2 billion supported mainly by growth in the digital economy which includes mobile telephony, uptake of e-commerce and penetration of internet .

Mobile money transfers grew by 9.5% from KShs.3.6 trillion in 2017 to KShs.3.9 trillion in 2018 and is on course to cross the KShs.4 trillion mark in the fourth quarter of the 2018/2019 financial year.

The value of investment by the telecommunication operators increased by 7.3 % to KShs.41.5 billion, while that of Internet service providers increased by 73.3 % to KShs.2.6 billion.

Huawei Technology has renewed their long-trusted partnership with the Kenyan government. This will work to improve the provision of ICT skills, build capacity as well as infrastructure and IT Services.

Building and Construction

Construction experienced decelerated growth of 6.6 % in 2018 compared to 8.5% in 2017. The Kenyan construction industry is set to grow steadily for the next decade attributed to an increased number of projects being carried out in the country. The total number of projects in East Africa has risen by a substantial 96% between 2017 and 2018 with an equally substantial increase of 167% in the total US dollar value of projects, a new report has shown. BMI Research shows that the local industry will grow by 8.7% this year and remain steady up to until 2026 with an annual growth of 6.2% which will see Kenya outperforming all sub-Saharan countries.

BMI pegs this on the government's' huge spending on infrastructure development such as the SGR and the Lamu port , South Sudan Ethiopia Transport (LAPPSET) corridor being key drivers of local economic growth.

Energy

The energy sector in Kenya is largely dominated by petroleum and electricity, with wood fuel providing the basic energy needs of the rural communities, urban poor, and the informal sector. An analysis of the national energy shows heavy dependency on wood fuel and other biomass that account for 68% of the total energy consumption (petroleum 22%, electricity 9%, others account for 1%).

Electricity access in Kenya is low despite the government's ambitious target to increase electricity connectivity from the current 15% to at least 65% by the year 2022.

President Uhuru Kenyatta assented to the Energy Bill 2017 and Petroleum Bill 2017, which stakeholders say offers a sound regulatory regime for the development of the sectors, particularly in relation to upstream development of oil and gas.

Kenya also moved to protect infrastructure in the sector with the imposition of penalties of up to $100,000 or a jail term of 15 years for sabotage. This will ensure facilities like pipelines are protected as the country gears up for commercial production of crude in Turkana County.

United States Acumen Capital Partners a subsidiary of Acumen recently announced a $70 million funding for KawiSafi ventures aimed at driving energy access across East Africa in a bid to scale the clean energy sector. KawiSafi is a nearly $70 million venture capital fund that invests in fast-growing companies leading the new energy revolution.

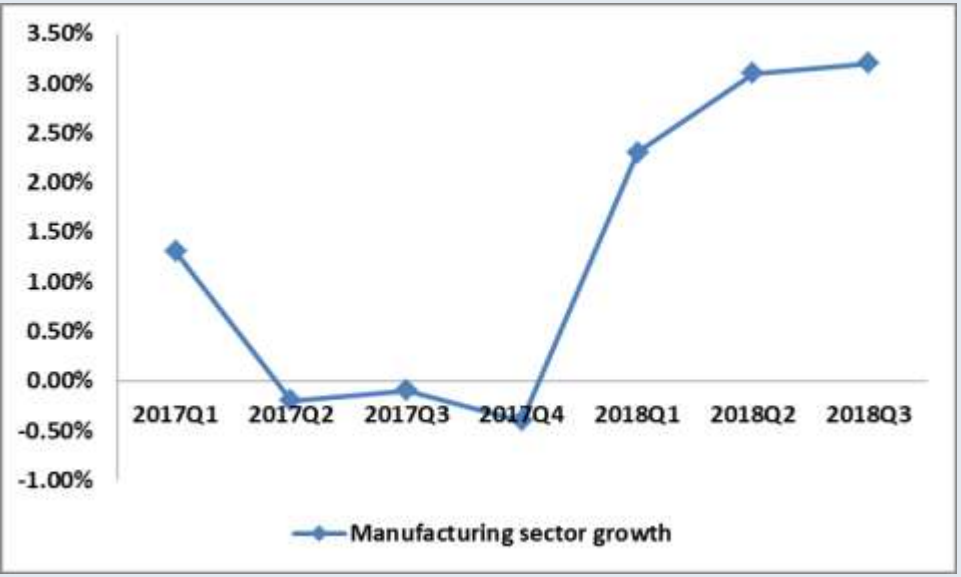
Banking

Growth in the Kenyan banking industry will remain stunted and will lag behind the wider economy which has been tipped to grow 5.8% in 2019.

Kenyan banks have been unwilling to lend to the private sector, preferring the government through risk-free Treasury-bills and bonds. Monetary Policy Committee (MPC) of Kenya's Central Bank held the benchmark lending rate at 9.00%, where it has been since July 2018.

The rate capping has seen several bank mergers & acquisition since it's introduction in 2016. In what is set to be the largest merger to date between KCB and NBK creating a bank with the largest asset base of KShs.1trillion.

Manufacturing



In last years annual budget, the government has declared manufacturing as a top priority investment area for the country to drive economic growth. Historically, manufacturing sector's contribution to the economy in Kenya has stagnated at around 10% of the gross domestic product (GDP) and was about 8.4% in 2017. There is renewed interest in the manufacturing sector through the Big 4 Agenda which seeks to increase the GDP contribution of the sector to 15% by 2022. Hence, the need to promote the competitiveness of local industries should be prioritized in the rejuvenated endeavor to focus on the manufacturing sector as a country. Food products sub-sector is the biggest ,contributing about 43% to the overall manufacturing sector contribution to GDP. Under the category of "others", we have sub-sector such as leather, wood and furniture, transport equipment, and Machinery.

Agriculture

Agriculture grew by 6.4% in 2018, driven mainly by a bumper produce and export of fresh fruits , tea and coffee. Growth in East Africa has historically been driven by growth in agriculture due to its major contribution to GDP and employment in most countries. GDP growth in the agriculture sector is about four times more effective in poverty reduction than GDP growth from other sectors. Kenya risks falling behind its regional peers in food and industrial production, largely due to inadequate credit to farmers and manufacturers. Agriculture accounts for only 1% of total loan accounts despite being the backbone of the economy. Without adequate credit, farmers are constrained to finance inputs and capital investments. Growth in 2018 was driven by favorable harvests, a resilient services sector, positive investor confidence and a stable macroeconomic environment.

Delays in the long rain season in 2019 and a growing need for emergency interventions to deal with food shortages is a reminder of the outstanding challenges in managing agricultural risks in Kenya.

- ‘‘Treasury Secretary Henry Rotich has presented this year’s budget, mentioning the KShs.3.02 trillion spend plans which includes new tax measures.’’
- The government is expected to borrow more in the next financial year to bridge the budget deficit of about KShs.607.8 billion That's KShs.45 billion higher than the deficit for the current year, KShs.562 billion. The government is likely to borrow more in the next fiscal year to bridge the deficit as Kenya Revenue Authority (KRA) is expected to miss this year’s revenue collection target by KShs.118 billion.
- This year’s budget focuses on the Big Four Agenda which has been funded to the tune of KShs.450 billion
- In the coming financial year, we expect revenue including Appropriations in Aid of KShs.2.1 trillion. Expenditure and net lending are projected at KShs.2.8 trillion.
- CS Rotich says this will help create more jobs as it transforms the lives of Kenyans. He further predicted growth in the medium term saying the country has witnessed a 6.3% growth in 8 years.

- Individuals earning over KShs.9million to be taxed at 35%
- Corporation tax increased to 35% for those with a taxable profit of over KShs.500 million. The effective tax rate after dividends for resident shareholders to increase to 38.25%, while for non-residents to 41.5%.
- Corporate tax rate reduced from 30% to 15% for the first 5 years for any investor operating a plastic recycling plant.
- Re-introduction of turnover tax for businesses whose turnover does not exceed KShs.5 million, however, presumptive tax will still be maintained as minimum tax.
- Capital gains tax (CGT) increased from 5% to 12.5%.
- Transfer of property from non-life to life business to attract CGT.
- Tax exempt dividend threshold from a 12.5% holding to 25% holding.
- The income earned by the NHDF will be exempt.

Withholding Tax(WHT)

- Rent payments subject to 10% WHT.
- WHT of 20% introduced on auction commission and audit residue limits.
- Withholding tax applicable on additional services :
  - Security Services
  - Cleaning and fumigation services
  - Catering services offered outside hotel premises
  - Transportation of goods excluding air transport services
  - Sales promotions
  - Marketing and advertising services
- Demurrage charges to be taxed as income earned by non-resident ship owners.
- WHT is applicable on re-insurance premiums paid to non-resident companies.
- WHT on payments made by a branch to its foreign head office or related party where the double taxation agreements provide for deduction of these expenses

Other Proposals

- Finance Bill 2019 has made a provision that allows for the Commissioner to recover taxes from a person who fails to deduct or withhold tax under the Law.
- Donations to tax exempt organization to be disallowed.
- Restricting the carry forward of the tax losses on business transfers and change of business activity.
- The proposal in the Budget is to streamline the penalties to 5% from the earlier 20% as stipulated in the Tax Procedures Act.

We observe from the budget statement that the government acknowledges the enormous accumulation of VAT refunds arising from delays in the payments. In his budget speech, the CS assures tax payers that validated refunds will be cleared within the next 2 months.

✓ Proposal to zero-rate denatured ethanol.

Exemptions on VAT

- Locally Manufactured Motherboards and all inputs used in their manufacture
- Services offered to Plastic Recycling Plants
- Specialized equipment for the development and generation of solar and wind energy
- Agricultural pest control

VAT REFUNDS-8%

The proposed amendment will ensure that suppliers of zero rated supplies fully recover the input tax related to those supplies.

Removal of VAT Exemption

- Semi-trailers shall now not be covered under exemption.
- securities brokerage services

Clarification of Exported services

- What matters is where the service is provided, who provides the service and the place of use or consumption of the services; the party who pays for the service is irrelevant.
- Proposal to reduce Withholding VAT tax rate from 6% to 2% which has impacted negatively on the cash flow and liquidity of taxpayers.
- suppliers, on whose payment VAT is withheld, are not entitled to VAT refund for the credit arising from VAT withheld.
- Proposal is to bring to tax all supplies made by through a digital market place
- Digital platform will constitute a platform that enables, by electronic means, direct interaction between buyers and sellers of goods and services.

Import duty on iron and steel products and paper and paper products at an ad valorem rate of 25% to be retained for another 1-year period.

It has been proposed to reduce import duty on raw timber from 10% to 0%. Further, a new proposal has been tabled to retain the ad valorem rate of import duty on finished timber products at 25%.

Extension on duty of remission on importation of certain products as below;

- Wheat grain of specified tariffs for one year 10%
- Motor Cycle Kits 10%
- Industrial Sugar 10%
- Input used in manufacture of Roofing tiles coated with acrylic paint for one year 0%
- Raw materials for manufacture of Energy saving stoves for one year 0%
- Inputs and raw materials used in manufacture of leaf springs for one year 0%
- Inputs and raw materials used in manufacture of radiators for one year 0%
- Aerosol Cans 0%

Stay on Application of CET (Common External Tariff) rates on the following items:

- Rice
- Non electric cooking appliances at the rate of 25%
- Liquid Gas cylinders at 25% instead of 0%
- Filing cabinets at 25% or USD 250/MT
- Coated Electrodes at 25% or USD 250/MT
- Leather and footwear items
- Edible oil at 25% or USD 500/MT
- Textiles and Apparel items at 35%
- Skillets, free hinge Lid Packets at 25% instead of 10%
- Road tractors for semi-trailers at 25% instead of 10%
- Safety matches at 25% or USD 1.35/KG
- Styrene Acrylic at 10% instead of 0%
- Polymers of Vinyl Acetate at 0% instead of 10%
- Worn Clothing at 35% or USD 0.2/KG
- Prefabricated Buildings at 35% or USD 250 /MT instead of 25%

EXCISE DUTY

- Proposal to introduce excise duty on betting activities at the rate of 10%.
- Increase in excise duty rate for alcoholic beverages and cigarettes

Items	Proposed Rate of Excise Duty
Cigars, Cheroots, Cigarillos containing tobacco or tobacco substitutes	KShs. 12,098 per KG
Electronic Cigarettes	KShs. 3,629 per unit
Cartridge for use in electronic cigarettes	KShs. 2,420 per unit
Cigarette with filters (Hinge lid and soft cap)	KShs. 3.025 per mile
Cigarette without filters (plain cigarettes)	KShs. 2,177 per mile
Other manufactured tobacco and manufactured tobacco substitutes; "homogenous" and "reconstituted tobacco"; tobacco extracts and essences	KShs. 8,469 per KG
Wines including fortified wines, and other alcoholic beverages obtained by fermentation of fruits	KShs. 181 per litre
Spirits of undenatured ethyl alcohol; spirits liqueurs and other spirituous beverages of alcoholic strength exceeding 10%	KShs. 242 per litre

- Increase in excise duty rate for Motor Vehicles

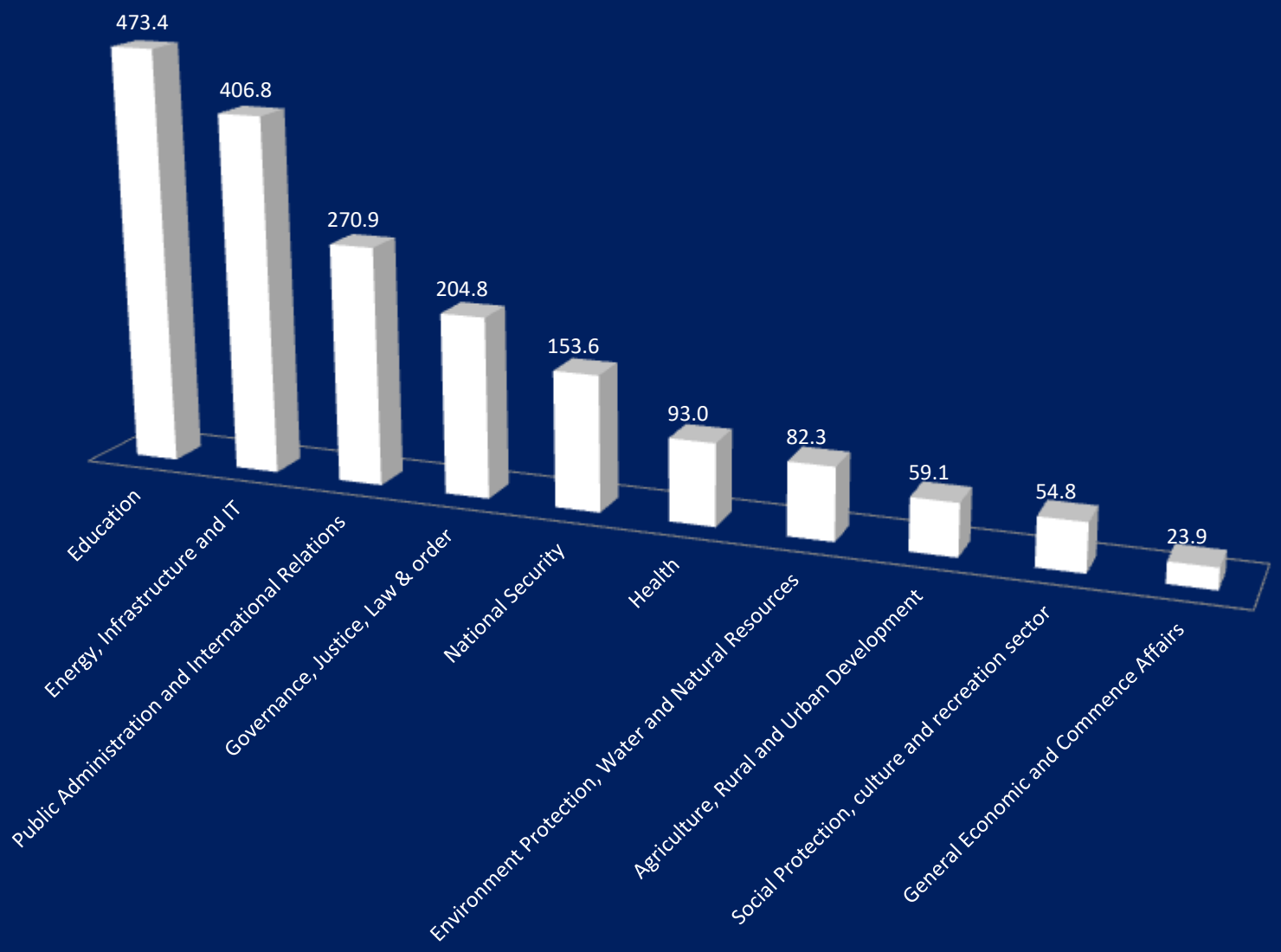
Items	Proposed Rate of Excise Duty
Motor vehicles of tariff heading 87.02, 87.03, and 87.04 excluding: **1. Locally assembled motor vehicles;** **2. School buses for use by public schools;** **3. Motor vehicles of tariff no. 8703.24.90 and 8703.33.90; and** **4. Imported motor vehicles of cylinder capacity exceeding 1500cc**	20%
Imported motor vehicles of cylinder capacity exceeding 1500cc of tariff heading 87.02, 87.03 and 87.04	25%
Motor vehicles of tariff no. 8703.24.90 and 8703.33.90 35%	35%
100% electric powered motor vehicles of tariff no. 8702.40.19, 8702.40.22, 8702.40.29, 8702.40.91, 8702.40.99 and 8702.80.00	10%

- Introduction of a general penalty of a fine not exceeding KShs.2Million or a term not exceeding two years, or to both.
- Inflationary adjustments to be made on 1st October from 1st July.

- The CS through the budget speech has sought to reverse the adverse effects of the adulteration levy of KShs.18 per litre of the customs value on illuminating kerosene, by introducing a statute providing for refund of the levy paid by manufacturers of paint and resin.
- Adjustments to RDL and IDF levies:
  - Reduction of IDF on intermediate goods and raw materials from 2% to 1.5%;
  - Increase of IDF on finished goods from 2% to 3.5%; and
  - An increase of RDL for finished products from 1.5% to 2%.

- 10% export levy on tanned and crust hides.
- Treasury is proposing a repeal of the capping of interest rates through an amendment to Section 33B Banking (Amendment) Act.
- A 3-year amnesty for penalties and interest for companies listed on the growth segment of the NSE is proposed.

Budget Expenditure Allocation FY 2019/2020(in Billions)



About Us

Ubiquity Consulting Ltd

Ubiquity Consulting Ltd is a management consulting company that specializes in working across industries to implement, maintain, and improve Quality Management systems. Our team is dedicated to multi-disciplinary approach. We have a particular focus on highly regulated industries where we are able to leverage our knowledge and expertise to assist companies of all sizes.

Ubiquity Consulting Ltd

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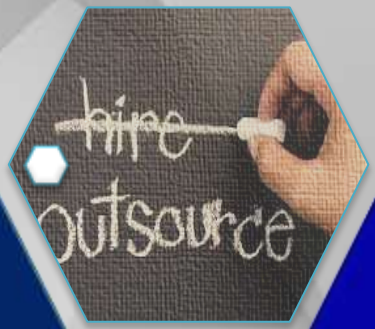

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5. Public Private Partnership
6. Financial Modelling

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4. Transfer Pricing
5. Direct & Indirect Tax

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