



REPUBLIC OF KENYA

THE NATIONAL TREASURY AND PLANNING

DRAFT KENYA SOVEREIGN WEALTH FUND POLICY

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TABLE OF CONTENTS

INTRODUCTION.....	2
POLICY OBJECTIVES.....	4
SCOPE	4
LEGAL AND REGULATORY FRAMEWORK.....	4
GUIDING PRINCIPLES	5
INSTITUTIONAL FRAMEWORK.....	7
RESPONSIBILITY AND ACCOUNTABILITY.....	7
POLICY REVIEW	7

INTRODUCTION

Background

As countries continue to discover natural resources within their territories, management of revenues from such resources become a pressing challenge to policymakers. In particular, countries are faced with three competing options namely; saving the revenues, using the funds for stabilization or development of the economy. Further, the question of who should directly benefit from the resources between the current and the future generations also arises given the fact that the resources will at one point be exhausted. The paradox becomes even more pronounced when one considers the effect of windfall revenue from the natural resources. This has sparked an interest in policy solutions to deal with the possible unfavorable effects of resource abundance.

A number of resource rich countries have established sovereign wealth funds to effectively manage revenues generated from extraction of resources. This has enabled the countries to prudently utilize the funds while at the same time investing excess funds to generate more income and save for future generations. For instance, Norway is one of the success stories in the management of resource revenues through the sovereign wealth fund. This has inspired developing countries such as Libya, Algeria, Angola, Nigeria, Botswana, Senegal and Ghana to establish sovereign wealth funds for the management of their natural resource revenues.

A sovereign wealth fund comprises pools of money derived from a country's reserves set aside for investment to benefit the country's economy and citizens. The funding for a sovereign wealth fund can come from central bank reserves that accumulate because of budget and trade surpluses, and revenue generated from exploiting natural resources.

Case for the Fund

Sovereign Wealth Funds are used to build a savings base for purposes of national development, facilitate the stabilization of the economy and enhance intergenerational equity.

With the discovery of mineral and petroleum deposits in Kenya, coupled with the enhanced exploration efforts by the Government, it is expected that the national government is going to get additional revenue from exploitation of these resources. Considering that natural resources are exhaustible, there is need for a clear framework to guide the usage of the proceeds and to effectively manage the wealth from these resources. It is against this backdrop that the National Treasury developed a framework for establishment of Kenya Sovereign Wealth Fund.

The Fund will be financed by resource revenues and returns from investments of these revenues. Currently, revenues from minerals in Kenya are paid into the Consolidated Fund and utilized through budgetary allocation. With the discovery of more minerals and petroleum deposits, resource revenues may increase beyond the economy's absorption capacity. Considering that the flow of these revenues is volatile due to various factors, it is important to establish a Fund through which the revenues will be managed effectively for the present and future generations. The Fund will be used to convert natural resource revenues into long-lasting assets in furtherance of a country's strategic, economic, or social priorities.

Guided by fiscal rules, it is envisaged that the Sovereign Wealth Fund will work as a counter cyclical stabilizer by cushioning the economy against unforeseen macroeconomic shocks. Similarly, the Fund will insulate the government budget against revenue fluctuations by creating precautionary buffers that will deal with commodity price volatility. Further, a portion of revenues from the resources may

be saved when revenues are high and drawn down when revenues decline in order to prevent “boom-bust” spending cycles.

Moreover, the Fund will finance infrastructure projects in line with Government development priorities. Finally, the Fund is expected to address issues of intergenerational equity by saving and investing resource revenue for use by future generations.

POLICY OBJECTIVES

The overall objective of the policy is to guide the establishment of the Fund for effective administration and efficient management of minerals and petroleum revenues. The specific objectives include:

1. Guide utilization of natural resource income for inclusive growth and development; and
2. Secure income from current resources for future generation.

SCOPE

The policy covers revenues from the petroleum and mining sources payable to the national Government. It will guide on matters relating to the establishment, objectives, and management of the Fund.

LEGAL AND REGULATORY FRAMEWORK

This policy is guided by the following statutes:

1. The Constitution of Kenya

The Kenya Constitution, 2010 pays special attention to management of natural resources. More specifically, Article 69 requires the State to ensure sustainable exploitation, utilization, management and conservation of the environment and

natural resources for the benefit of the people of Kenya. Further, Article 201 provides that: the burdens and benefits of the use of resources and public borrowing shall be shared equitably between present and future generations; public money shall be used in a prudent and responsible way; and financial management shall be responsible, and fiscal reporting shall be clear.

2. The Public Finance Management Act

The Act provides for allocation of resources to priority needs, overall fiscal discipline and institutional structure for effective and efficient management of public resources.

3. The Petroleum (Exploration and Production) Act

The Act provides a framework for contracting, exploration, development and production of petroleum. Further, the Act provides for the categories of revenue payable to the national Government which forms part of the sources of the monies to the Fund.

4. Mining Act

The Act provides a legal framework that regulates on prospecting, mining, processing, refining, treatment and transport of minerals. Further, the Act provides for the categories of revenue payable to the national Government which also forms part of the sources of the monies to the Fund.

GUIDING PRINCIPLES

In order to ensure predictability and consistency in the management and utilization of petroleum and mining resources, the Fund shall be established through an Act of Parliament.

The Fund shall be divided into three components geared to: promote infrastructure development priorities for fostering strong and inclusive growth; insulate budget expenditures from revenue fluctuations and cushion against unexpected shocks; and build a savings base for future generations.

1. Monies for the Fund

The monies for the Fund shall consist of national Government share of resource revenues from minerals and petroleum and any other approved sources including returns from the investments of the Fund that shall be deposited into a holding account. The holding account of the Fund shall be at the Central Bank of Kenya.

The monies shall be shared among the components taking into account government expenditure priorities. Upon depletion of mineral and petroleum resources, all components shall cease to exist and the monies shall be consolidated into one account of the Fund.

2. Fiscal responsibility principles

The administration and management of the Fund shall be in accordance with the fiscal responsibility principles provided in the Public Finance Management Act and the Act establishing the Fund.

3. Investment of the Fund

The funds that may not be immediately needed for the budget shall be invested in instruments to be specified by an Act of Parliament establishing the Fund. The investment of the funds shall be done without prejudice to the objectives of the Fund. The Cabinet Secretary shall approve investment policies, risk management framework that will guide investment of the Fund.

INSTITUTIONAL FRAMEWORK

The Fund shall be managed by a Board which shall be a body corporate. The Board shall be answerable to the Cabinet Secretary responsible for finance on the management of the Fund.

The Board may delegate some of its functions to investment fund manager, senior management of the Fund or any other person as may be necessary.

The Cabinet Secretary may appoint the Central Bank of Kenya as the administrator of the Fund before incorporation of the Board.

RESPONSIBILITY AND ACCOUNTABILITY

The Board shall be responsible and accountable for the performance and the management of the Fund.

The Fund shall be audited by the Auditor General in line with the Constitution and Public Finance Management Act.

The Board shall prepare financial statements of the Fund and submit to the Auditor General for audit in accordance with the Public Finance Management Act.

The Board shall also prepare annual performance reports of the Fund and submit to the Cabinet Secretary.

POLICY REVIEW

This Policy will be reviewed from time to time on need basis. The Ministry responsible for finance may involve other stakeholders in the review of the Policy.

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