



Another One Bites the Dust

Taxpayers absorb yet another round of fiscal pressures

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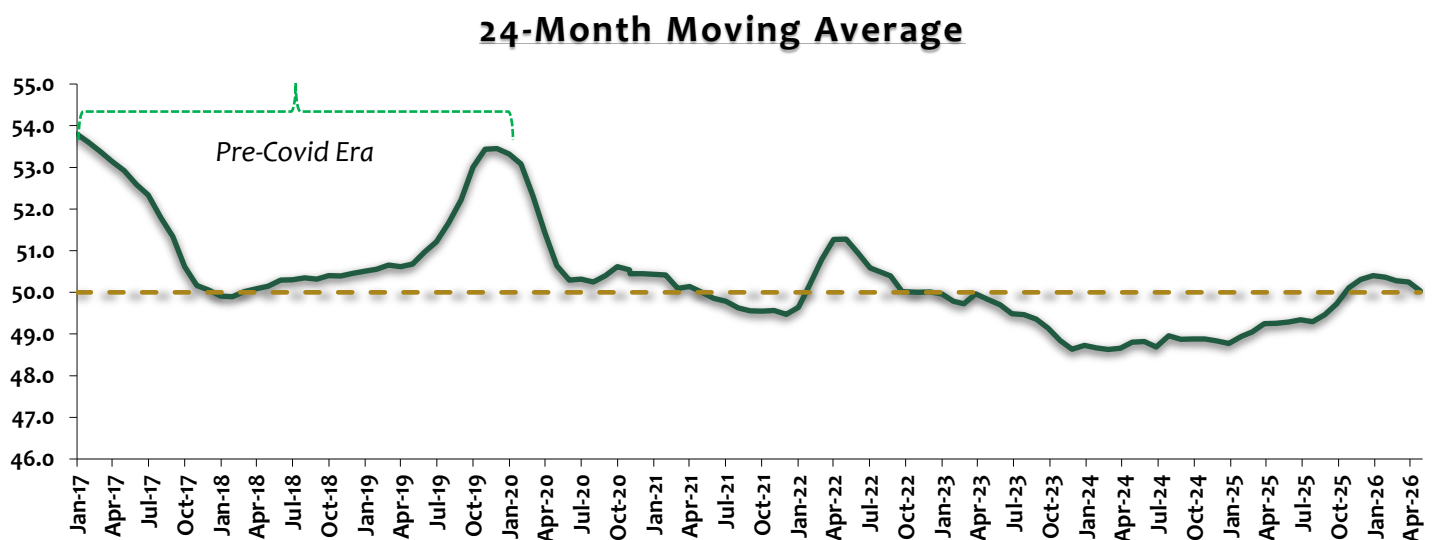
Reading the Tea Leaves

We want to start from a broader perspective and eventually show why this starting point matters. The chronology of events is important.

Our assessment indicates that the private sector has been in a prolonged healing phase since the COVID era. While activity showed signs of improvement in late 2025 and early 2026, the recovery remained shallow, with business activity only marginally above the expansion threshold. Although much has happened over the past few years, several key events stand out for their significant impact on the business environment:

- i. COVID-19 (2020–2021): Demand shock and widespread business disruptions.
- ii. 2022–2024: Inflation shock, drought effects, currency depreciation, higher interest rates, and tax measures weighed on business activity.
- iii. 2025–2026: Easing inflation and lower interest rates began supporting activity, but the recovery remained fragile.

The chart below highlights the 24-month average, providing a clearer view of the underlying trends in the business environment;



Source: Stanbic Bank Kenya, KSL Estimates | Chart: KSL

COVID-19 was an unprecedented occurrence that cannot solely be attributed to policy failures, and at the time, the priority for businesses and governments alike was survival. We therefore begin our analysis from 2022.

The period between 2022 and 2024 was particularly challenging for the business environment and, by extension, the Kenyan economy. While several factors were at play, our focus is on the fiscal side of the story, alongside developments in the interest rate environment and the depreciation of the Kenyan shilling.

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Our assessment points to persistent fiscal indiscipline, characterized by large fiscal deficits and the inefficient use of borrowed funds, culminating in a growing debt burden with limited transformative impact on the economy. During this period, the Kenyan shilling depreciated significantly amid concerns over Kenya's ability to meet its obligations on the debut Eurobond. The depreciation triggered intense imported inflation, which in turn contributed to higher interest rates both locally and globally.

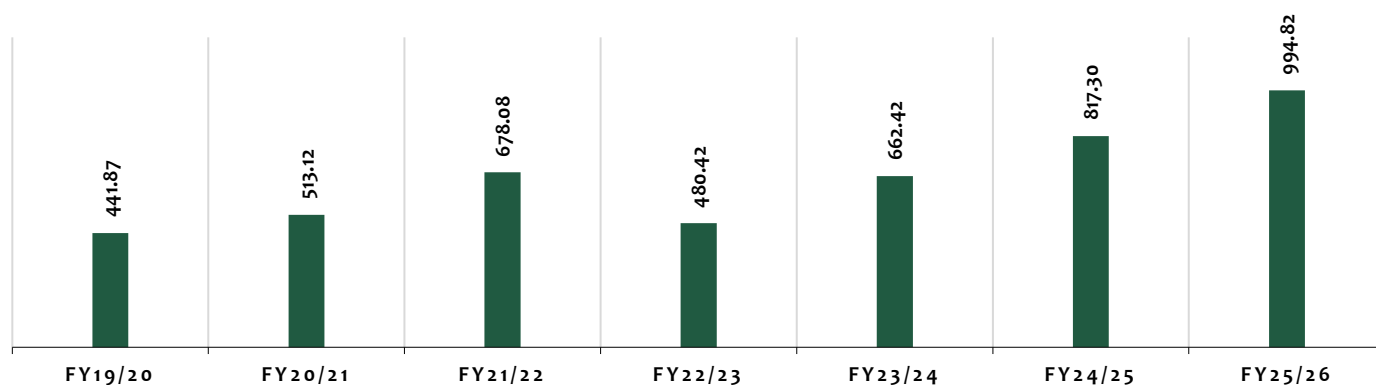
At the same time, rising expenditure needs and a constrained business environment placed pressure on government revenues, necessitating more aggressive tax collection measures. This ultimately gave rise to the Finance Act 2023, which introduced a raft of tax measures that reduced disposable income for formal sector workers and increased the cost of doing business.

Fast forward to FY2026/27, and the economy faces a fresh set of challenges. The fiscal year comes against a backdrop of renewed supply chain disruptions and immediately precedes an electioneering period. Historically, such periods tend to be associated with infrastructure-heavy spending programmes, particularly those with high public visibility.

The likely outcome is increased borrowing as debt service remains a first charge on government revenues, while recurrent expenditure obligations cannot simply be paused. A review of recent fiscal trends shows that domestic borrowing has increasingly borne the burden of financing the fiscal deficit. This signals a growing preference among lenders to extend credit to the government rather than the private sector, potentially crowding out private sector investment.

Moreover, domestic borrowing has generally proved more expensive than external financing. As a result, debt servicing is likely to continue exerting significant pressure on government revenues for the foreseeable future. The chart below illustrates the evolution of domestic borrowing targets over time;

NET DOMESTIC BORROWING TARGETS - KES BN



Source: National Treasury | Chart: KSL

Nonetheless, the government has consistently advanced an austerity narrative over the past few years, but the reality on the ground appears somewhat different. There are several fiscal adjustment paths through which austerity can manifest, including:

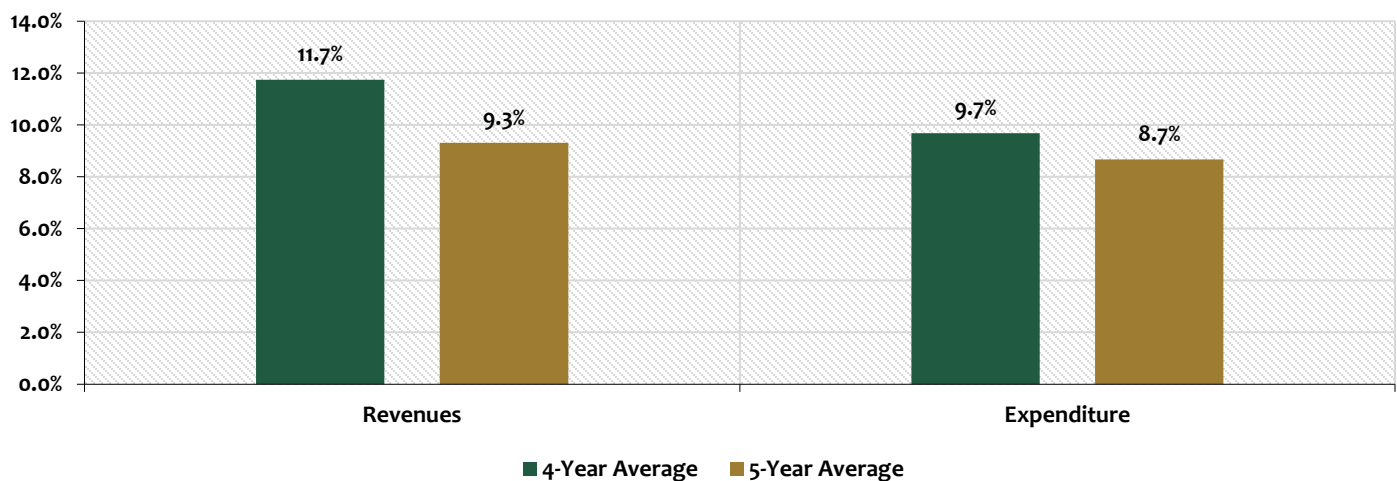
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- Slower growth in expenditure than revenue (relative austerity)
- Stagnant expenditure and growing revenue (passive consolidation)
- Reducing expenditure and stagnant revenue (hard austerity through spending cuts)
- Reducing expenditure and growing revenue (full consolidation or aggressive austerity)

In practice, however, Kenya does not appear to have meaningfully pursued any of the latter three paths. Over the last five years, expenditure has largely grown in tandem with revenues, albeit at a slightly slower pace over the last four years. While this may qualify as a mild form of fiscal consolidation, it falls short of the more aggressive expenditure restraint typically associated with austerity.

The chart below illustrates the evolution of expenditure relative to revenues over the period;

Revenue vs. Expenditure Growth



Source: National Treasury | Chart: KSL

For FY2026/27, ordinary revenues are projected to grow by 12.9%, while expenditure is expected to increase at a much slower pace of 3.0%. On paper, this resembles the relative austerity path discussed earlier. However, in our view, the revenue projections once again appear quite ambitious.

The Finance Bill is expected to raise an additional Kes 98.9Bn, leaving approximately Kes 241.6Bn of the projected revenue growth dependent on economic activity and improved collections. History offers reason for caution. In recent years, revenue targets have been revised downward while expenditure has been adjusted upward, ultimately forcing the government to increase borrowing. The consequence has been a heavier debt burden, increased debt servicing costs, and a greater strain on the business environment and, by extension, taxpayers. As such, while the fiscal framework points to restraint on the expenditure side, the risks remain tilted towards higher borrowing should revenues fall short of target.

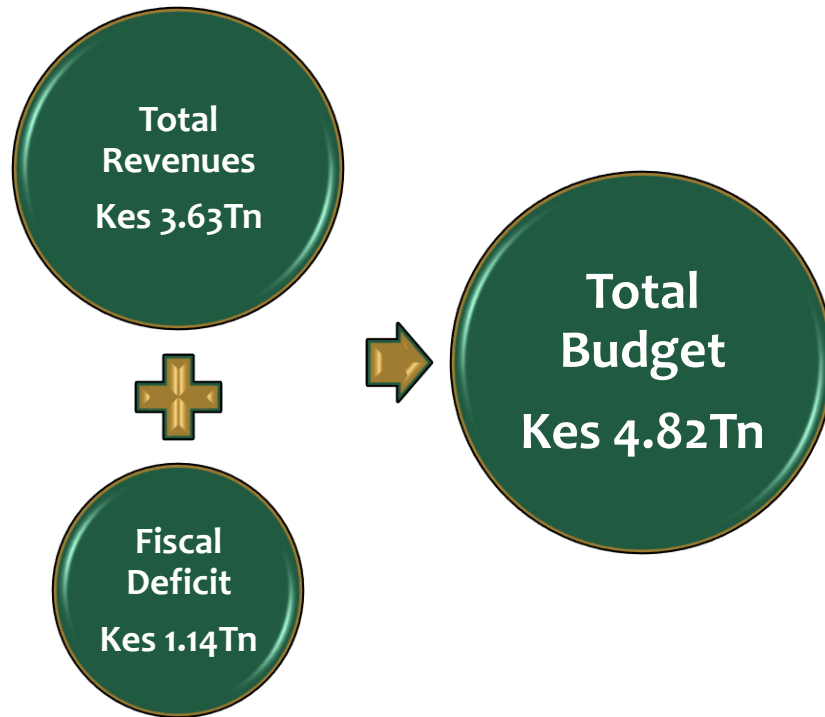
So yes, another one bites the dust. Expenditure continues to rise, and debt service remains a significant claim on government revenues.

Below, we analyze the FY2026/27 budget numbers in greater detail.

KINGDOM SECURITIES

FY2026/27 Budget in a Nutshell

As has been the case for the longest, the FY26/27 budget is heavily skewed towards education and infrastructure. In total, we are looking at Kes 4.82Tn in total expenditure as shown below:



Education is set to gobble a whopping 27% of the national government budget, followed by the energy, infrastructure & ICT category.

	FY25/26	FY26/27
Education	25.9%	27.0%
Energy, Infrastructure & ICT	20.9%	18.5%
Public Administration & International Relations	13.0%	12.6%
Governance, Justice, Law & Order	11.2%	12.2%
National Security	9.9%	10.6%
Health	5.7%	6.1%
Environmental, Water & Natural Resources	3.9%	3.9%
Agriculture, Rural & Urban Development	4.0%	3.7%
Social Protection, Culture & Recreation	3.1%	3.4%
General Economic & Commercial Affairs	2.4%	2.1%

FY2026/27 Budget in Detail

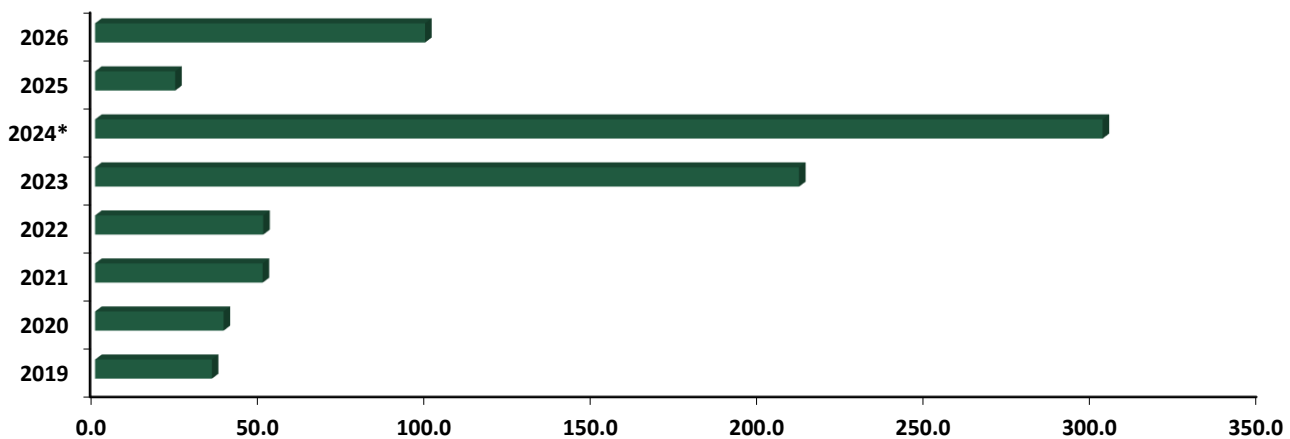
Show me the Revenues

In recent years, the revenue side of the budget has attracted heightened attention and public discourse, largely driven by the Finance Bill, which has become increasingly prominent in policy and market conversations.

As a result, the government has, over the past two years, had limited fiscal headroom to pursue aggressive revenue-raising measures, given the heightened risk of economic disruption. That said, the Finance Bill 2026 introduces a raft of measures which the Finance and Planning Committee projects will generate an additional KES 98.90Bn in revenues.

This estimate is relatively high compared to the 2025 projections, but significantly lower than the 2023 proposals and the subsequently rejected 2024 measures, as shown below;

Revenue Projections from Respective Finance Bills (KES bn)

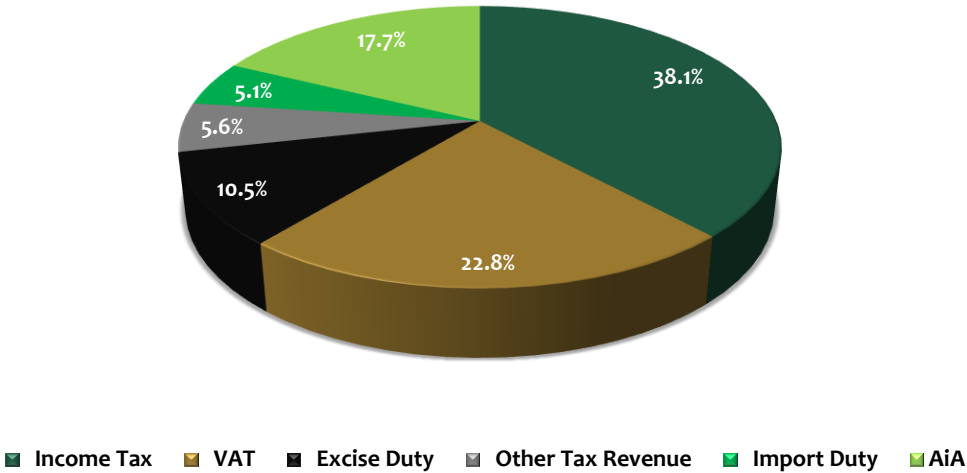


For FY26/27 total revenue is estimated at Kes 3.63Tn, with ordinary revenue projected at Kes 2.98Tn, a marginal jump from Kes 2.78Tn in FY25/26 as summarized below:



As usual, income tax bracket accounts for the highest chunk of ordinary revenues estimated at 38.1%, followed by Value Added Tax at 22.8% and finally excise duty at 10.5%. Appropriations in Aid is expected to contribute 17.7% to the revenue basket as shown below:

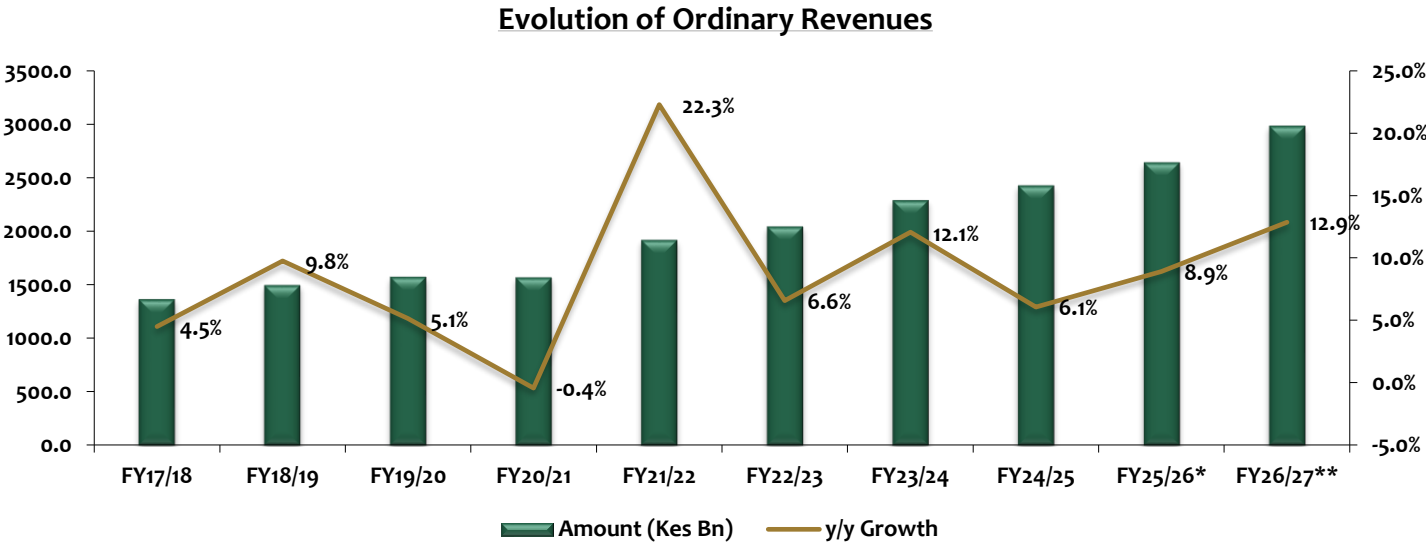
FY26/27 Revenue Breakdown



Evolution of Ordinary Revenues; In the Face of Tax Fatigue, Revenues Continue to Rise

Over the last five years, ordinary revenues have grown at an average rate of 9.3%. It is worth noting that while the revenue-raising measures introduced by the current administration have faced significant resistance, revenue growth has generally outpaced that recorded in the preceding five-year period, save for a few outlier years.

See the chart below for the evolution of Kenya's ordinary revenues:



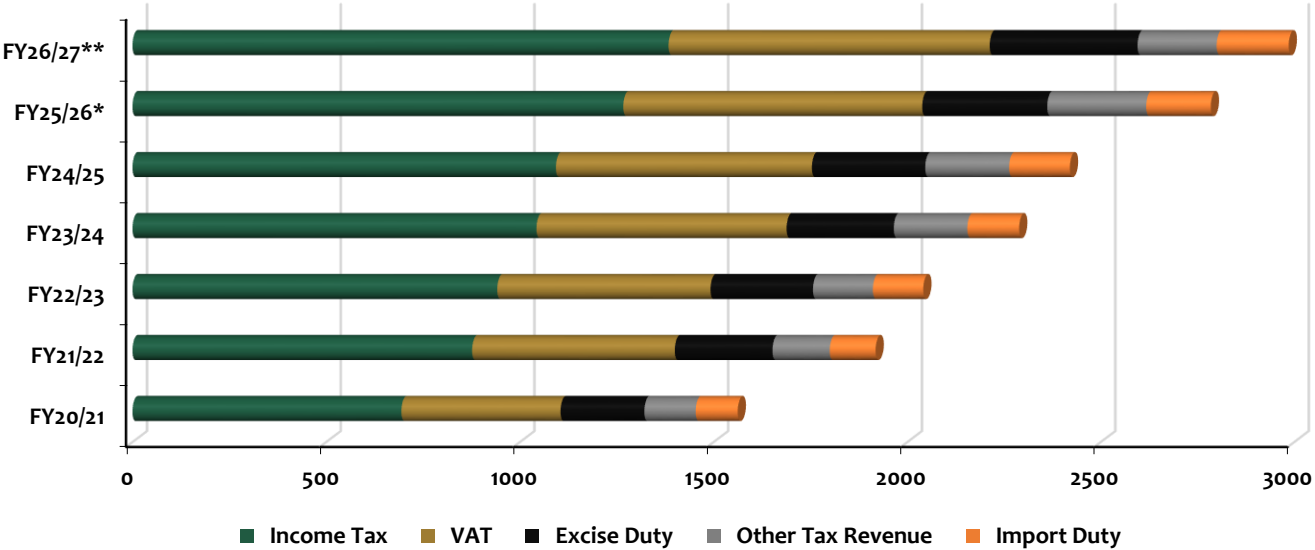
Source: National Treasury, KSL Estimates | Chart: KSL

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In our view, this performance has largely been supported by the reforms introduced through the Finance Act 2023. Since then, subsequent Finance Acts have been relatively lean, aligning more closely with the trend observed prior to 2023, albeit not entirely by choice.

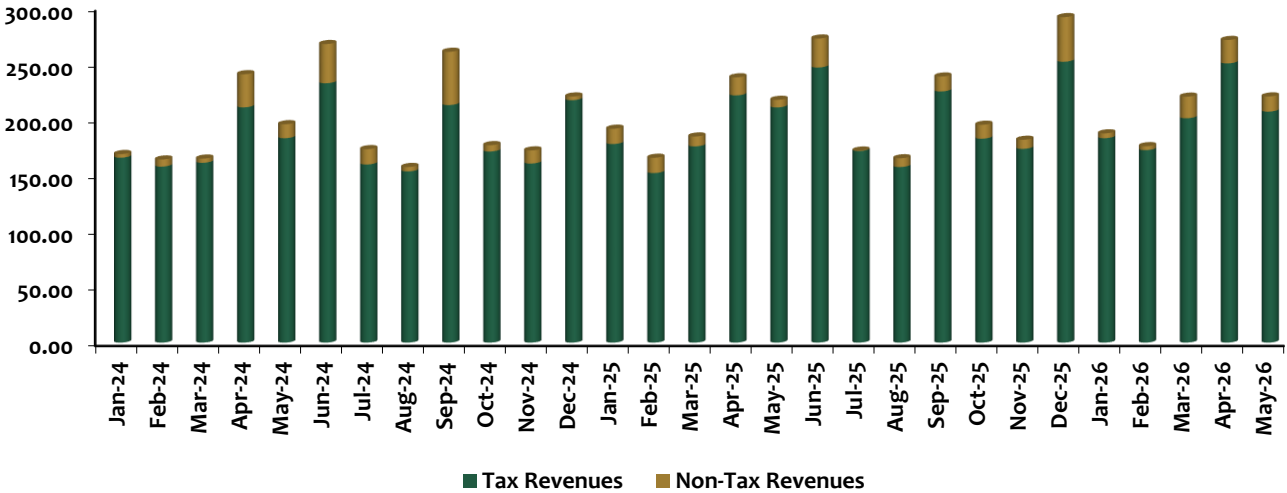
On the specific revenue lines, income tax, and VAT have recorded the fastest growth on average in the last five years.

Kenya's Revenue Breakdown - (Kes Bn)



It is important to note that over the last 29 months, the government has collected an average of Kes 205.11Bn in ordinary revenues per month, representing an average y/y growth of 7.5%. Against this backdrop, the projected 12.9% growth in ordinary revenues for FY2026/27 suggests that the government is confident that the measures contained in the Finance Bill 2026 will support stronger revenue mobilization. See below the trends over the same period;

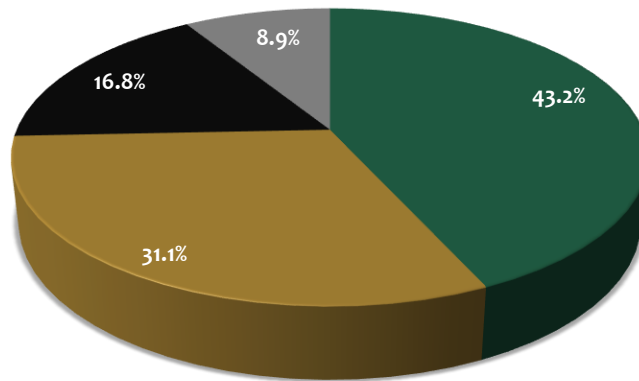
Exchequer Revenues (Kes. Bn)



Follow the Money

The government plans to spend Kes 4.82Tn in FY26/27, with recurrent expenditure (salaries, wages, operating and maintenance) budget accounting for the largest chunk. Of the total budget, the national government budget stands at Kes 2.90Tn with education gobbling a whopping 27.0%. Debt servicing costs and other CFS account for 31.1% of the total expenditure, cementing the continued pressure, debt levies on the country's accounts. See below a breakdown of the expenditure:

FY26/27 Expenditure Breakdown



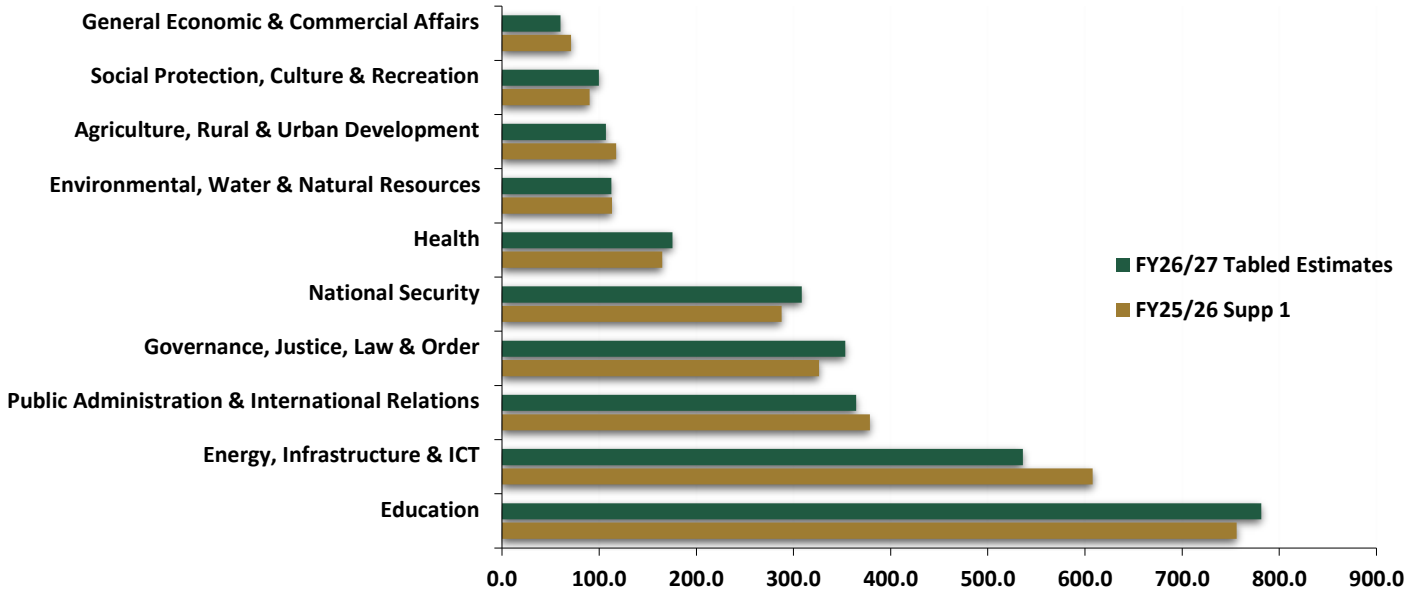
■ Recurrent Expenditure ■ Interest Payments & Other CFS ■ Development & Net Lending ■ County Transfers

Under the national government budget, the Governance, Justice, Law & Order sector got the highest increase at Kes 26.9Bn mainly attributed to additional resources provided to the IEBC to support electoral preparedness activities. The enhanced funding is intended to facilitate critical pre-election processes, including voter registration and verification, procurement of electoral materials, logistical planning, civic education, and strengthening of institutional and operational capacity to ensure the timely and credible conduct of the 2027 general elections.

On the other hand, the energy, infrastructure & ICT sector recorded the largest cut in expenditure with critical initiatives, including the Last Mile Electricity Connectivity Project, Electrification in Constituencies Programme, off-grid electrification projects, Street Lighting Programme, and the development of transmission lines, substations, and geothermal energy projects being the most affected.

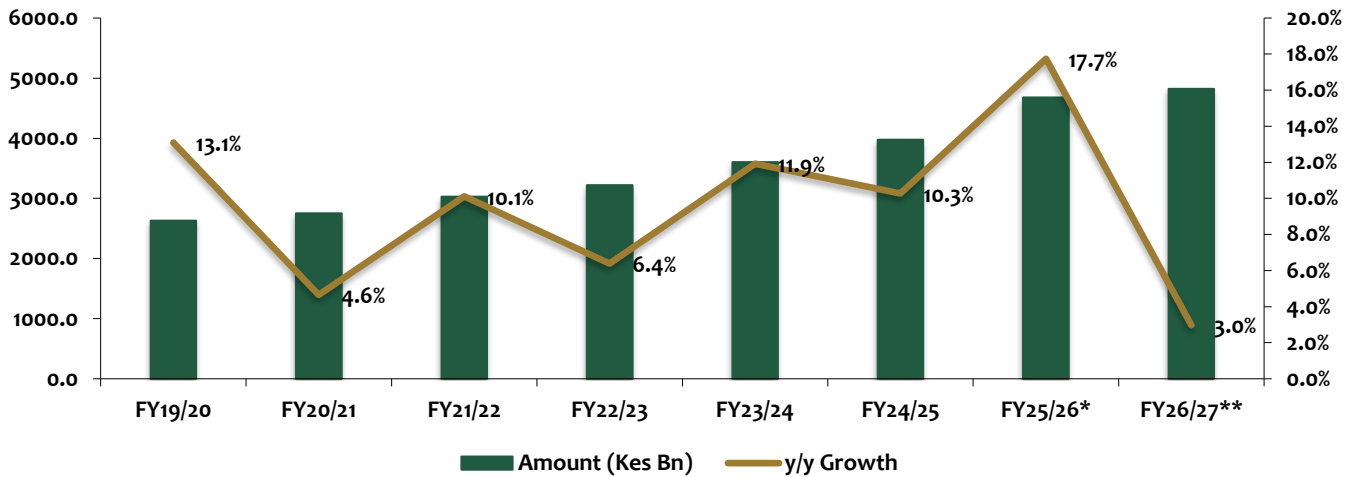
See the chart below for a visual presentation;

Chart Title



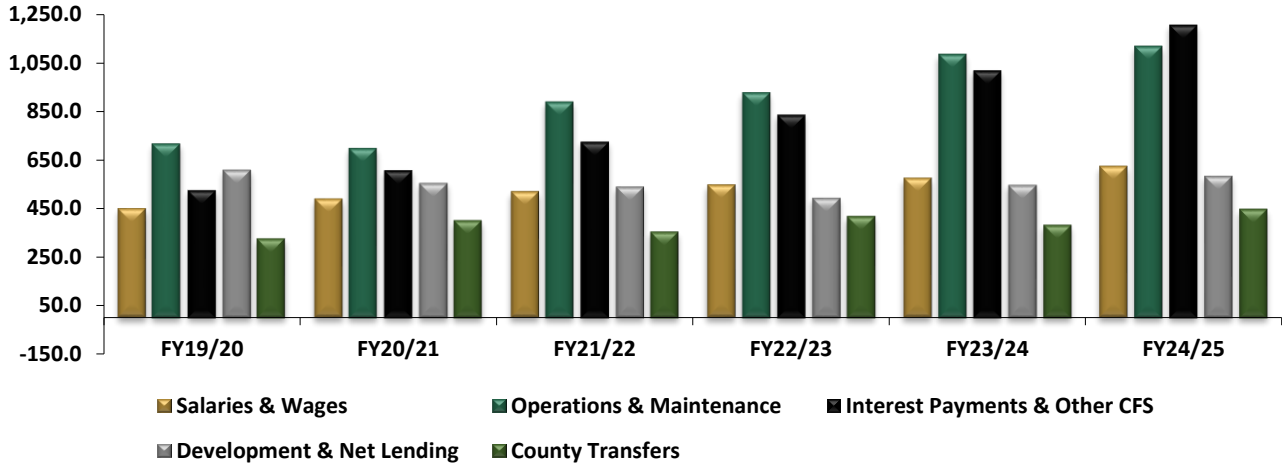
Overall, the FY26/27 budget represents a 3.0% increase from the Kes 4,681.30Tn estimated spend in FY25/26. The figure includes the additions made in the draft supplementary budget II. On average, expenditure has been growing by 9.9% over the last 5 years growing from Kes 3.22Tn, to the projected Kes 4.82Tn for FY26/27.

Evolution of Expenditure - Kes Bn



Notably, debt service, operations & maintenance charges have been the largest expenditure avenues. Between FY19/20 and FY24/25, the two segments have recorded an average growth of 6.8% and 9.8% respectively. On the other hand, interest payments have had a faster growth of 18.0% over the same period with the greatest growth recorded in FY23/24 when Kenya’s debut bond was falling due. The period also coincides with the high interest rate environment which significantly raised the cost of debt. See the breakdown below;

Expenditure Breakdown - Kes Bn

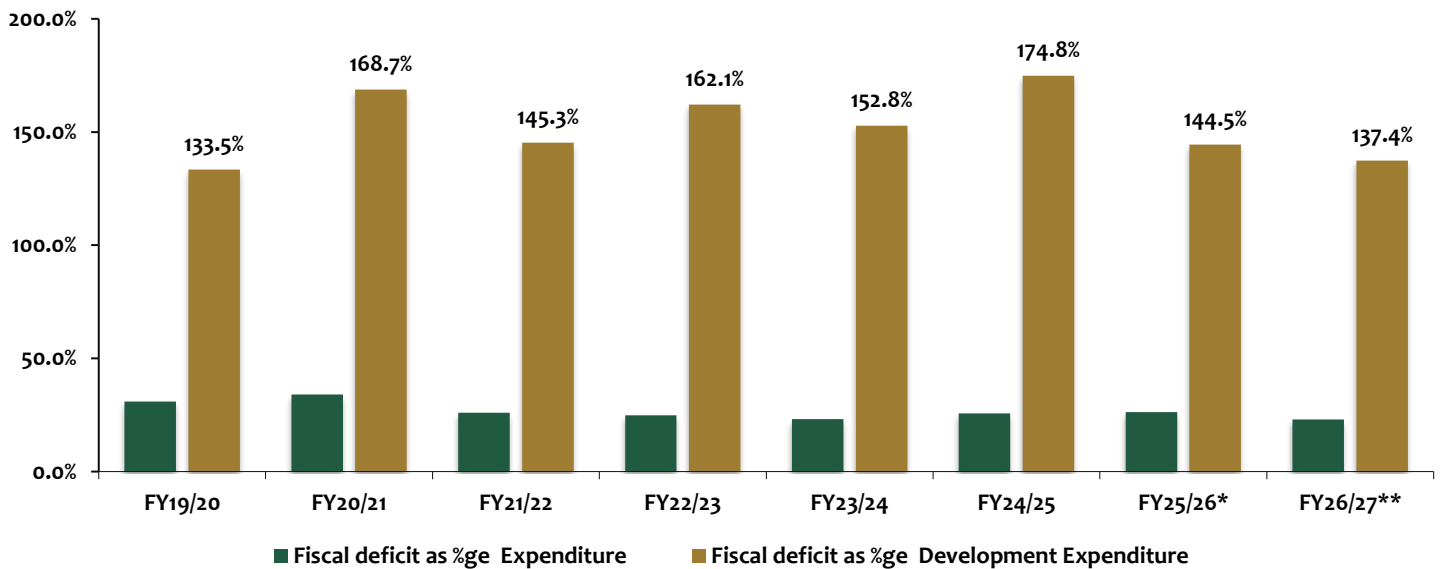


The Making of the Fiscal Deficit

Over time, the fiscal deficit as a percentage of development expenditure has remained stubbornly high. The ratio suggests that, increasingly, government borrowing is being used to finance consumption rather than investment, and this is where the core challenge emerges.

Actual figures between FY2019/20 and FY2024/25 indicate that, on average, more than half of borrowed funds have been directed toward recurrent expenditure. FY2024/25 stands out as the most constrained period, with 74.8% of borrowings effectively financing recurrent spending, as shown below.;

Deficit Burden Relative to Spending



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