AFRICAN DEVELOPMENT BANK GROUP
GROUPE DE LA BANQUE AFRICAINE DE DÉVELOPPEMENT

Country Focus Report 2025

Kenya



Making Kenya's Capital Work Better for its Development

Country Focus Report 2025
Kenya

Making Kenya's Capital Work Better for its Development

AFRICAN DEVELOPMENT BANK GROUP
GROUPE DE LA BANQUE AFRICAINE DE DÉVELOPPEMENT

The opinions expressed and arguments employed herein do not necessarily reflect the official views of the African Development Bank, its Boards of Directors, or the countries they represent. This document, as well as any data and maps included, are without prejudice to the status of or sovereignty over any territory, to the delimitation of international frontiers and boundaries, and to the name of any territory, city, or area.

© African Development Bank 2025

You may copy, download, or print this material for your own use, and you may include excerpts from this publication in your own documents, presentations, blogs, websites, and teaching materials, as long as the African Development Bank is suitably acknowledged as the source and copyright owner.

ACKNOWLEDGEMENTS

The Country Focus Report (CFR) 2025 for the Republic of Kenya (Kenya) was prepared in the Chief Economist and Vice-Presidency for Economic Governance and Knowledge Management Complex, under the general direction and supervision of Prof Kevin C. Urama, Chief Economist and Vice-President, with support from Adamon Mukasa (Principal Research Economist), and Amah Marie-Aude Ezanin (Executive Assistant).

The preparation of the report was led by Désiré Vencatachellum (Senior Director, Country Economics Department – ECCE). With Marcellin Ndong Ntah (Lead Economist, ECCE) as Technical Coordinator of the process, Abir Bdioui (Consultant, ECCE) for IT support, Tricia Effe Baidoo (Knowledge Product Management Specialist, ECCE) for the monitoring of copy editing and design, and Eugenia Grant (Team Assistant, ECCE) for administrative support. The CFR 2025 for Kenya was prepared by Caroline Bernice Akishule Ntumwa (Principal Country Economist) under the supervision of George Auma Kararach (Lead Economist, ECCE.2 East Africa Regional Development and Business Delivery Office (RDGE)).

Our thanks go to (i) Hervé Lohoues, Division Manager for South, Eastern and Nigeria ECCE.2 (ii) the Kenya country team led by Alex M. Mubiru (Director General, RDGE and Country Manager, Kenya) (iii) the Department of Macroeconomic Policy, Forecasting and Research (ECMR) led by Anthony Simpasa (Director); (iv) the Department of Transition States (RDTS) led by Yero Baldeh (Director); (v) the African Centre for Natural Resources (ECNR) led by Solomane Koné (Director); and the Economic Research Consortium for Africa (AERC) led by Prof. Victor Murinde (Executive Director); for their contributions.

The Bank would like to thank the heads of government entities for hosting and organizing the mission to prepare the CFR 2025 for Kenya and the quality of the discussions. It also thanks the representatives of the private sector, and technical and financial partners for their availability and the quality of the discussions during the meetings held with the mission.

The data in this Report were compiled by the Department of Statistics - ECST headed by Samson Babatunde Omotosho (Director) with the participation of Koua Louis Kouakou, Head of the Economic and Social Statistics Division, and Anouar Chaouch (Senior Statistician, Economic and Social Statistics Division, ECST).

Comments made during the peer review were received from: Walter Owuor Odero (Principal Country Economist, ECCE.2), and Maria Saguti Marealle (Chief Land Officer, ECNR). Dr. Joseph Atta-Mensah, Senior Fellow African Center for Economic Transformation – Ghana, and Dr. Ahmed H. Ahmed, University of Loughborough, UK – an Expert from the African Economic Research Consortium, contributed as external reviewers.

The cover of the report is based on a general design by Laetitia Yattien- Amiguet and Justin Kabasele of the Bank's External Relations and Communications. Copy-editing was done by the Annes Mcgoogan and layout was done by Eighth Wonder Company Limited.

TABLE OF CONTENTS

ACKNOWLEDGEMENTS III
TABLE OF CONTENTS IV
ABBREVIATIONS AND ACRONYMS VI
EXECUTIVE SUMMARY VII
GENERAL INTRODUCTION IX

1. MACROECONOMIC PERFORMANCE AND OUTLOOK 1
1.1 Introduction 1
1.2 Growth performance 1
1.3 Other recent macroeconomic and social developments
1.3.1 Monetary policy, inflation and exchange rate 2
1.3.2 Financial sector 2
1.3.3 Fiscal policy and public debt 2
1.3.4 External position and external financial flows 3
1.3.5 Social developments 3
1.4 Macroeconomic outlook and risks 3
1.4.1 Outlook 3
1.4.2 Risks 4
1.5 Policy options to accelerate Kenya's economic development 4

2. BOOSTING DOMESTIC CAPITAL MOBILIZATION AND EFFICIENT UTILIZATION 7
2.1 Introduction 7
2.2 Fiscal Resource Mobilisation 7
2.2.1 Kenya's financing needs 7
2.2.2 Tax revenue 8
2.2.3 Non-tax revenue 8
2.2.4 Expenditure efficiency and mobilizing domestic fiscal resources 8
2.3 Natural Capital 8
2.3.1 Overview of Kenya's natural capital 8
2.3.2 Economic contribution of Kenya's natural capital 9
2.3.3 Estimates and Dynamics of natural capital 9
2.3.4 Challenges of leveraging Kenya's natural capital 10
2.4 Business Capital 11
2.4.1 Setting the stage 11
2.4.2 Indicators of business capital 11
2.4.3 Challenges and opportunities for enhancing business capital in Kenya 11
2.5 Human Capital 12
2.5.1 Current state of human capital in Kenya 12
2.5.2 Major barriers to human capital development in Kenya 12
2.5.3 Investing in education and skills development 13
2.5.4 Health as a pillar of human capital development 13
2.6 Financial Capital 13
2.6.1 Domestic capital and financial markets 13
2.6.2 State of financial development in Kenya 14

2.6.3 Mobilizing financial resources for Kenya's development 15
2.6.4 Off-shore-linked financial resources for Kenya's development 15
2.6.5 Innovative finance 15
2.7 Policy Recommendations 16

3. HARNESSING KENYA'S CAPITAL POTENTIAL FOR DEVELOPMENT 17
3.1 Introduction 17
3.2 Institutional arrangements for the management and utilization of the various forms of capital for resource mobilisation 18
3.3 Governance challenges in the management and utilization of the various forms of capital for resource mobilisation 19
3.4 The rule of law, management and utilization of the various forms of capital 20
3.5 A Pan-African approach to strengthening the rule of law, institutions and governance for harnessing Kenya's capital 21

REFERENCES 23

LIST OF FIGURES

Figure 1: Trends in the fiscal balance and public debt in Kenya

LIST OF TABLES

Table 1: Key macroeconomic indicators 3
Table 2: Decomposition of Kenya's natural capital 9
Table 3: Challenges facing carbon sequestration-adjusted GDP of Kenya 10
Table 4: Key indicators of education, health, and workforce in Kenya 12

LIST OF BOXES

Box 1: Domestic Resource Mobilization Efforts and the Development Finance Gap 4
Box 2: Potential Impact of Recent Changes of the United States Foreign Policy on the Kenya Economy 4
Box 3: Reforms and Investments in Education that Have Worked Well in Kenya 13
Box 4: Capital Markets Landscape in Kenya 14
Box 5: CBK's Efforts to Strengthen Kenya's Financial Systems for Inclusive Growth 14

ABBREVIATIONS AND ACRONYMS

AEO	African Economic Outlook
AfCFTA	African Continental Free Trade Area
AfDB	African Development Bank
AGOA	African Growth and Opportunity Act
CFR	Country Focus Report
EAC	East African Community
EU	European Union
FDI	Foreign direct investment
GDP	Gross domestic product
GHG	Greenhouse gas
GNI	Gross National Income
ICT	Information and communications technology
iTax	Web-based system introduced by KRA to shorten time taken to file tax returns
IMF	International Monetary Fund
KRA	Kenyan Revenue Authority
MW	Megawatt
MSMEs	Micro, Small and Medium Enterprises
NCA	Natural Capital Accounting
NEPAD	The New Partnership for Africa's Development
STEM	Science, Technology, Engineering and Mathematics
S&P	Standard and Poor's
PPPs	Public-Private Partnerships
SEZ	Special Economic Zone
TVET	Technical and Vocational Education and Training
UN	United Nations
USD	United States dollar

EXECUTIVE SUMMARY

Kenya's economy grew by 4.6% in 2024, a slowdown from 5.6% in 2023, due to weak industrial activity, low investment, and climate-related shocks. Growth was supported by agriculture and fintech-driven services. Inflation dropped to 4.5%, and a stronger shilling allowed for monetary easing. Fiscal consolidation reduced the deficit to 5.4% of GDP and lowered public debt to 65.7%, while the current account deficit narrowed to 3.7%, aided by rising exports and remittances. Despite these gains, structural issues persist, including high poverty, inequality, and youth unemployment, requiring better mobilization of Kenya's development capital. While there have been advances in infrastructure, financial innovation, and basic services, capital quality and depth remain weak. Fiscal capital is strained by debt and inefficiencies, innovation in business capital is limited, financial capital is unevenly accessible, natural capital is eroding, and human capital suffers from poor learning outcomes and skills mismatches. Governance gaps, corruption, and regulatory inefficiencies hinder progress. A coordinated, inclusive, and sustainable capital strategy, anchored in tax reform, public-private partnerships, and institutional strengthening, is essential for Kenya's equitable long-term development.

.

GENERAL INTRODUCTION

The Republic of Kenya is a lower middle-income, coastal country in East Africa, covering an area of 582,646 square kilometres. With a population of 52.4 million (mid-2024 projection), Kenya has a relatively young demographic profile where, in 2019, 36% of the population was aged between 15-34. Over the past three decades, Kenya has recorded steady per capita income growth (USD 2,110 billion in 2023, from USD 280 in 1993) and notable macroeconomic improvements, supported by political stability, resilient services (notably fintech), and ongoing structural reforms. However, rising poverty alongside high unemployment and inequality highlights that Kenya's economic growth has not been fully inclusive. The economy remains vulnerable to climate shocks and external risks and faces structural challenges such as high business costs, limited industrial competitiveness, and uneven social outcomes. Kenya's growth is driven by services and agriculture, with manufacturing and extractives playing a smaller role, limiting deeper structural transformation. Despite improvements in fiscal consolidation and macroeconomic management, financing gaps and weak capital mobilization have slowed progress toward sustainable development. The Bottom-Up Economic Transformation Agenda (BETA) seeks to address these gaps through inclusive growth, job creation, and investment in human capital and productivity-enhancing sectors.

The Country Focus Report (CFR) 2025 for Kenya, seeks to replicate at the country level the thematic analysis conducted in the African Development Bank's 2025 African Economic Outlook (AEO). It was informed by desk research and reviews as well as consultations with the government and the private sector. The report is structured as follows: Chapter I examines Kenya's recent macroeconomic performance and outlook; Chapter II examines the effectiveness and potential of domestic capital mobilization in Kenya to address the financing gaps for sustainable development; and Chapter III explores how institutions, governance, and the rule of law can support harnessing Kenya's capital for development. Each chapter offers policy recommendations.

1 MACROECONOMIC PERFORMANCE AND OUTLOOK

KEY MESSAGES

- Kenya's economy grew by 4.6% in 2024, driven by fintech and agriculture, despite challenges in the mining and construction sectors. The Central Bank of Kenya maintained an accommodative monetary policy, supporting growth and lowering lending rates. Fiscal consolidation focused on expanding the tax base and enhancing revenue collection through digitization.

- Kenya faces a financing gap, with a projected FY2025/26 budget deficit of 5% of Gross Domestic Product (GDP). Key initiatives include broadening the tax base, modernizing tax systems, and investing in natural capital and digital infrastructure to support inclusive growth.

1.1 Introduction

This chapter analyzes Kenya's economic performance in 2024 and projects growth for 2025–2026 (Table 1). It examines trends in key macroeconomic indicators, touching on the links between Kenya's current domestic resource mobilization efforts and its development financing gap. The chapter also discusses the main upside and downside risks to the growth outlook and outlines policy options to foster high resilient growth. The recommendations aim to support Kenya's macroeconomic stability, advance its economic transformation, and enhance the country's capacity to manage ongoing and future economic shocks.

1.2 Growth performance

Kenya is a lower-middle-income[1] country with a gross national income (GNI) per capita of USD 2,110 in 2023 (up from USD 280 in 1993). The diversified economy faces several challenges. Real GDP growth slowed to 4.6% in 2024 from 5.6% in 2023, largely due to lower mining and construction output, and investment. While the economy remained resilient, supported by a robust services sector, particularly fintech and mobile money, and improved agricultural performance, it remains vulnerable to climate shocks and external trade pressures. Quarterly GDP growth in 2024 decelerated from 5.0% in Q1 to 4.0% in Q3, mainly due to heavy rains and floods that disrupted agriculture and damaged infrastructure. The mining sector contracted sharply following the closure of Base Titanium, a Kenyan mining company that operated the Kwale Mineral Sands Project, Kenya's largest mining operation, while industrial growth was subdued by reduced construction and lower electricity generation. The industrial sector grew by just 0.8%. Weak household consumption, sluggish private sector lending, and poor external trade further dampened aggregate demand, contributing to the economic slowdown.

[1] GNI per capita between USD 1,146 and USD 4,515 in 2025 – World Bank classification.

1.3 Other recent macroeconomic and social developments

1.3.1 Monetary policy, inflation and exchange rate

The Central Bank of Kenya (CBK) aims for price stability. At 4.5%, 2024 overall inflation was within the medium-term objective range of 2.5-7.5%, having slowed from 7.7% in 2022, aided by increased food supply from good weather, a shilling appreciation of 16.0% to KES 129.8/USD end-December 2024, and falling global oil prices. The CBK maintained an accommodative monetary policy stance to support economic growth, lowering its policy rate to 10.0% in March 2025 from 10.75% in February, and by 175 basis points between June and December 2024. Subsequently, lending rates dropped to 15.8% in March from 16.4% in February 2025 and 17.2% in November 2024.

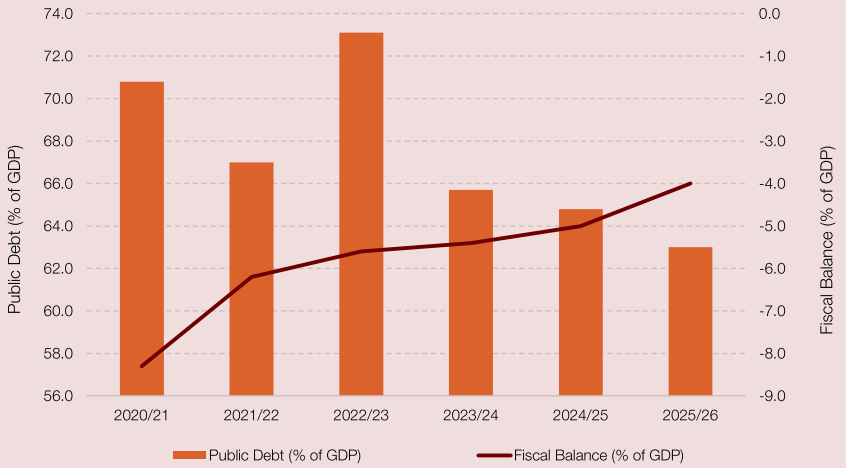
1.3.2 Financial sector

Kenya's banking sector remains well-capitalized, with a capital adequacy ratio of 19.1% in 2023, well above the 14.5% prudential minimum. However, asset quality deteriorated, as the non-performing loan ratio rose to 17.2% by February 2025 from 16.4% in December 2024, and from 10.4% in 2023, reflecting the lagged effects of earlier interest rate hikes. Commercial bank lending to the private sector declined to 4% by June 2024, from 13.9% in early 2023, before contracting by 1.1% in November 2024, driven by a stronger shilling and elevated interest rates. As interest rates fell in response to monetary policy easing, lending showed early signs of recovery, growing by 0.2% in March 2025.

1.3.3 Fiscal policy and public debt

Kenya's 2024 fiscal deficit narrowed to 5.4% of GDP from 5.6% in 2023 (Figure 1), reflecting ongoing fiscal consolidation efforts. This progress was supported by measures to expand the tax base, enhance tax efficiency, and reduce revenue leaks, combined with more rationalized spending that safeguarded priority social and development programs. However, the withdrawal of the 2024 Finance Bill amid widespread protests raised doubts about the sustainability of these reforms. Although the July 2024 supplementary budget introduced expenditure cuts to offset fiscal gaps, high borrowing costs and ongoing debt service pressures persisted. Public debt (49.7% external) declined to 65.7% of the GDP by mid-2024, from 73.1% in 2023 (Figure 1), supported by an appreciating currency and improved liability management operations. However, while sustainable, debt remains at high risk of debt distress with solvency and liquidity challenges. Moody's, Fitch, and S&P downgraded Kenya's credit ratings in 2024, citing deteriorating debt dynamics, though S&P retained a stable outlook. The government, through the 2025 Budget Policy Statement, reaffirmed its commitment to fiscal discipline and structural reforms to restore confidence.

Figure 1: Trends in the fiscal balance and public debt in Kenya



Source: Data from domestic authorities; estimates (e) and prediction (p) based on AfDB calculations; AfDB Statistics Department, May 2025

1.3.4 External position and external financial flows

Kenya's current account deficit narrowed to 3.7% of GDP in 2024 from 4.0% in 2023, reflecting improved exports and remittance inflows. The deficit narrowed further to 3.1% of GDP in the 12 months to February 2025 from 3.3% the previous year, supported by a 13.1% rise in goods exports, mainly agricultural and re-exports, alongside strong diaspora remittances, which rose by 14.5%. The Kenya National Bureau of Statistics (KNBS) revised re-export and travel receipt data. Services receipts also improved, driven by higher travel and transport earnings. The 2024 deficit was partly financed by financial account inflows. Foreign exchange reserves increased to USD 10.1 billion (5.1 months of import cover) in December 2024, up from USD 7.34 billion (3.9 months) in December 2023, buffering against short-term shocks. By March 2025, reserves stood at USD 9.93 billion (4.4 months of import cover).

Table 1: Key macroeconomic indicators

	2020	2021	2022	2023	2024(e)	2025(p)	2026(p)
Real GDP growth (%)	-0.3	7.6	4.9	5.6	4.6	5.0	4.8
Real GDP growth per capita	-2.3	5.6	3.0	3.7	2.6	3.0	2.8
CPI inflation	5.4	6.1	7.6	7.7	4.5	3.9	4.5
Overall fiscal balance, including grants (% of GDP)*	-7.0	-8.3	-6.2	-5.6	-5.4	-5.0	-4.0
Current account balance (% of GDP)	-3.7	-5.1	-5.1	-4.0	-3.7	-3.0	-3.4

Source: Data from domestic authorities; estimates (e) and prediction (p) based on AfDB calculations. AfDB Statistics Department, May 2025. Data in fiscal year 1 July (n-1)/ 30 June (n).

1.3.5 Social developments

Kenya's economic growth (see 1.2) has not been inclusive. At 39.8% (2022), poverty increased from 38.6% (2021) with unemployment at 13.9% driven by 13.4% youth unemployment (2022), contributing to income inequality (38.9% 2021 Gini coefficient). The Human Development Index is at 0.598 (2022), and the 2024 Sustainable Development Goals (SDG) Index ranked Kenya 123 out of 166 countries, with a 62.1% achievement of the 17 SDGs, a rank deterioration from 118/163, but a score improvement from 61.0% in 2021.

1.4 Macroeconomic outlook and risks

1.4.1 Outlook

Kenya's macroeconomic outlook for 2025 is positive, with real GDP growth projected at 5.0%, supported by stronger agriculture and key services. The fiscal deficit is expected to narrow to 5.0% of GDP (Box 1), while public debt is projected to decline toward the 55.0% anchor under continued fiscal consolidation. With lower global oil prices, inflation and the current account deficit are forecast to decline to 3.9% and 3.0% respectively. The CBK sees room for further monetary policy easing to boost private sector lending, support economic activity, and maintain exchange rate stability.

Box 1: Domestic Resource Mobilization Efforts and the Development Finance Gap

Kenya's 2025 Budget Policy Statement outlines key domestic resource mobilization measures to address its FY2025/2026 KES 831 billion budget gap. These include implementing the Medium-Term Revenue Strategy to raise tax revenues to 20% of GDP, strengthening tax administration through improved compliance and reduced leakages, and digitizing revenue collection via systems like the Integrated Tax Management System (iTax) and Integrated Customs Management System (iCMS). The government plans to broaden the tax base, especially in the informal sector, and rationalize tax incentives. However, challenges with tax compliance remain.

Source: 2025 Budget Policy Statement

1.4.2 Risks

Kenya's 2025 outlook faces upside risks from stable weather, improved macroeconomic conditions, lower lending rates, reduced global oil prices, and the full implementation of fiscal consolidation reforms to enhance development spending, broaden the tax base, and boost growth. Kenya faces several downside risks, including potential declines in global aid and escalating trade tensions (Box 2); regional geopolitical instability, particularly spillovers from Ethiopia and Somalia that could adversely impact trade and security; fiscal slippages due to possible reversals on tax reforms and ongoing debt vulnerabilities; climate-related pressures such as food price increases caused by recurring droughts and floods that disrupt agriculture and infrastructure; and high business costs that may hamper productivity, especially in the industrial and agricultural sectors. However, effective implementation of the BETA strategy, which focuses on inclusive growth and resilience could help mitigate these risks and support economic stability and growth in the medium term.

Box 2: Potential Impact of Recent Changes of the United States Foreign Policy on the Kenya Economy

In the short term, suspended aid programs like the President's Emergency Plan for AIDS Relief have disrupted health services, causing layoffs and funding shortfalls. Tariffs threaten exports under the AGOA, risking jobs in Export Processing Zones, while . US-China tensions weakening global demand for Kenyan exports and straining supply chains. However, falling oil prices have eased Kenya's import bill and inflation, offering short-term relief. Long-term risks include the possible September 2025 expiry of the AGOA, which could undermine export competitiveness and deter foreign investment. Prolonged trade frictions may slow Chinese foreign direct investment (FDI), remittances, and manufacturing, while sustained aid cuts could destabilize social programs. For resilience, Kenya is diversifying trade through the African Continental Free Trade Area (AfCFTA), boosting domestic manufacturing, implementing revenue reforms, attracting private capital through public-private partnerships (PPPs), and investing in digital infrastructure. Kenya is pursuing new partnerships with China on infrastructure, security, and technology. Key policy priorities include building fiscal buffers from oil savings, leveraging diaspora financing, and expanding renewable energy to reduce oil dependency and enhance long-term economic stability.

Source: Author's research from online sources such as Reuters, Financial Times, AP News.

1.5 Policy options to accelerate Kenya's economic development

- **Monetary Policy:** Kenya's monetary policy is focused on enhancing credit access for Micro, Small and Medium Enterprises (MSMEs) through an accommodative stance and improved interbank efficiency, aided by a narrower policy rate corridor (±75 bps). Disciplined forex reserve management and stabilization of diaspora remittances are key to cushioning external shocks and supporting the current account.

- **Fiscal Policy:** Kenya has made visible progress, but its high debt burden restricts its ability to replace external aid with domestic resources in the short term. Fiscal consolidation is supported by KRA's digitization (iTax, eTIMS) and integration with key government databases (NTSA, Lands Registry, Business Registration Services). Formalizing MSMEs via mobile-based tax filing, cutting non-priority spending, and refinancing costly debt with longer-term concessional loans are key steps. Protecting BETA's pro-poor programs remains critical. Domestic debt management is improving through tools like the liability management operations and market engagement programs.

- **Structural Reforms:** Kenya can boost trade through AfCFTA, EU, and regional ties; improve arid agriculture via irrigation and climate-smart inputs; and prioritize gender inclusion, MSME finance, digital infrastructure, value chains, PPPs, and diaspora bonds. A revised 2014 External Resources Policy will enhance resource mobilization and governance, with stronger debt transparency and citizen engagement aligning with Vision 2030 and the SDGs. Strengthening debt transparency and governance, through timely publication of debt reports and increased citizen engagement, will be central to these reforms.

2 BOOSTING DOMESTIC CAPITAL MOBILIZATION AND EFFICIENT UTILIZATION

KEY MESSAGES

- Kenya needs to mobilize diverse capital sources to achieve the SDGs: Realizing Kenya's Vision 2030 and SDGs will require strategic mobilization of multiple forms of capital - fiscal, natural, human, business, and financial. Despite the progress made, capital utilization remains fragmented, and better alignment of public and private resources is essential for sustained, inclusive development.

- Financial development is advancing but remains uneven. Kenya has made notable gains in financial inclusion (83.6% of the total population) through fintech and mobile money. However, capital markets remain underdeveloped, and insurance and pension sectors are not fully tapped for long-term development financing. This uneven progress constrains investment in infrastructure, MSMEs, and climate adaptation.

- Strategic reforms are crucial for unlocking capital. Kenya must strengthen tax policy, digitize revenue collection, and formalize the informal sector to expand fiscal space. It should also deepen financial markets, incentivize innovation through blended and green finance, and align education and skills with growth sectors. Enhancing institutional capacity, transparency, and public-private collaboration is vital to fully unlock sustainable development financing.

2.1 Introduction

Kenya's total nominal wealth is estimated at USD 480.6 billion (2020), composed of produced capital (5%), human capital (78%), and natural capital (17%). This section highlights Kenya's efforts on domestic resource mobilization, expenditure efficiency and debt sustainability. It explores key domestic capital categories relevant to Kenya, including fiscal resources, natural resources, business resources, human resources, and financial resources. It identifies their status, inefficiencies, and strategies for mobilization and utilization to facilitate the country's future growth, structural transformation, and sustainable development.

2.2 Fiscal Resource Mobilisation

2.2.1 Kenya's financing needs

Kenya has a projected financing gap of USD12.5 billion (11.6% of GDP) by 2030 to meet key SDGs, with major needs in

roads (55%), education (22%), energy (20%), and research and development (9%). The government plans to raise its tax revenue-to-GDP ratio from 13% to 25%, aligning with the African average and peers like South Africa. Despite improved collections, tax efficiency remains low. The Medium-Term Revenue Strategy focuses on expanding the tax base, integrating the informal sector, reducing tax expenditures, and strengthening tax administration and compliance mechanisms.

2.2.2 Tax revenue

Kenya's tax revenue constitutes 85% of government income, 60% of which is spent on debt servicing. The tax structure is dominated by income tax (47%), Value-added tax (VAT; 24%), excise duties (15%), and other taxes (14%). Kenya's personal income tax rate of 35% is higher than Tanzania and Rwanda (30%) but lower than Uganda and the DRC (40%). Corporate tax is 30% across most countries, except Rwanda's slightly lower rate of 28%.

2.2.3 Non-tax revenue

Kenya's non-tax revenue (NTR) to GDP ratio is about 2.3%, well below the African average of 5.8%. Countries like Botswana and Lesotho outperform due to natural resources and revenue-sharing systems. Kenya's NTR mainly comes from service fees, dividends, fines, property income, and royalties. To boost NTR, the government is enhancing the capacity of ministries, departments, and agencies to generate revenue, and expanding the e-Citizen digital platform which provides access to over 16,000 government services. It is also enforcing compliance to ensure surplus funds from state agencies are remitted to the Treasury for improved efficiency and transparency.

2.2.4 Expenditure efficiency and mobilizing domestic fiscal resources

In FY2025/26, Kenya's public expenditure is set to rise to 22.5% of GDP, with recurrent at 16.0% and development at 4.2%. However, inefficiencies (infrastructure funding) cost up to 5% of GDP annually. High wage bills, losses from State-Owned Enterprises, energy subsidies, and poorly targeted tax incentives (costing KES 100 billion annually) strain fiscal resources. To enhance domestic revenue and spending efficiency, the 2025 Budget Policy Statement prioritizes expanding the tax base, reducing tax expenditures, strengthening tax administration, and digitizing tax systems to improve compliance and reduce leakages.

2.3 Natural Capital

2.3.1 Overview of Kenya's natural capital

Kenya's natural capital (Table 2) includes renewable resources such as arable land, forests, wildlife, and renewable energy, as well as non-renewables like minerals and rare earth elements. Agriculture contributes 22% to GDP but faces 30% post-harvest losses. Forest cover has reached 8.8%, targeting 10% by 2030. Renewable energy, led by geothermal at 48%, provides 90% of electricity. Minerals (gold, titanium) and rare earth elements remain underexploited, contributing under 1% of GDP, though rare minerals offer strong potential for the country's clean energy transition.

Table 2: **Decomposition of Kenya's natural capital**

Natural Capital Category	Quantified Contribution / Description	Year of Data	Estimated Economic Value (USD)	Notes
Forests & Tree Cover	8.83% forest cover; 12.13% tree cover	2021	Not directly quantified	Slightly above the 10.0% constitutional requirement
Mineral Resources	Contributes 0.8% of GDP; expected to reach 10% by 2030	Current (2022-2023)	Approx. USD 200M per year (mineral sand and soda ash)	Key minerals include titanium, niobium, soda ash
Petroleum (Crude Oil & Gas)	22% of primary energy consumption	2018	Value depends on production; exploration ongoing	63 petroleum blocks identified; Turkana oil field potential
Water Resources	Approx. 20.2 billion m^3/year renewable freshwater	Estimated (2022)	Approx. USD 0.20–0.50 per m^3 = USUSD 4 billion-10 billion per year	Used in agriculture, industry, and households
Energy (Renewables)	Installed capacity: 3,601 MW; 89.57% renewable	2022	Not directly valued in atlas	Geothermal accounts for 45.5% of installed capacity
Marine & Blue Economy	Fish potential: Exclusive Economic Zone 150,000–300,000 tons; Lake Turkana 30,000 tons	Estimated (2021–2022)	Potentially Approx. USD 500 million per year	Vital for coastal livelihoods, food security
Soils & Land	About 48% of land used for agriculture	Estimated (2020)	Indirect: Agriculture is Approx. 22.4% of GDP	Degradation poses a threat to productivity
Biodiversity Resources	High biodiversity zones incl. Mau Forest, Mt. Kenya, Kakamega Forest	Current (2022–2023)	Not quantified in monetary terms	Ecosystems host elephants, rhinos, birds, endemic flora

Source: Kenya Natural Resources Atlas, 2023

2.3.2 Economic contribution of Kenya's natural capital

Kenya's renewable energy sector contributed 2.5% to GDP and non-renewable 0.5% in 2023, underscoring renewables' key role. Agriculture contributed 21.8% to GDP and 45.0% to fiscal revenues. Natural resource rents rose from 1.05% of GDP in 2019 to 1.23% in 2021. Mining's 2019 share was 0.7%, with potential to reach 10.0% by 2030 through reforms like the Mining Act review. Natural capital revenues are vulnerable to global price fluctuations, requiring transparent governance and stronger institutions for sustainable management. Renewables attract climate finance and reduce energy import costs, supporting long-term sustainability. Non-renewables generate short to medium-term revenues through exports and taxes, funding infrastructure and social needs. Together, they improve access to development financing.

2.3.3 Estimates and Dynamics of natural capital

Kenya's commitment to natural resource sustainability has preserved key renewable

assets, supporting agriculture and tourism. Efforts include large-scale tree planting, forest protection laws, watershed rehabilitation (Tana River Basin), irrigation projects (Galana-Kulalu), community conservancies, and anti-poaching policies such as the Wildlife Act (2013).

Sustainable farming practices are promoted through the Climate-Smart Agriculture Strategy, while investment in clean energy reduces reliance on biomass.

Despite high natural capital per capita (USD 3.9 billion), produced capital per capita remains low (USUSD 1.2 billion), highlighting the need for balanced strategic infrastructure and resource reforms.

2.3.4 Challenges of leveraging Kenya's natural capital

Illicit financial flows are estimated to have cost Kenya USD 1.5 billion annually through illegal mining, logging, and tax evasion, while trade mis-invoicing led to USD 3.92 billion in lost tax revenue (2002–2011). Weak policies, poor data systems, limited skilled personnel and institutional gaps in governance hinder Natural Capital Accounting (NCA) and the sustainable management of both renewable and extractive resources. Climate threats, outdated resource data, and underdeveloped carbon markets (Table 3) further limit sustainable gains. Despite Kenya's NCA progress, carbon-adjusted GDP remains unavailable. Key challenges include limited expertise, poor institutional capacity, and low private sector involvement.

Table 3: Challenges facing carbon sequestration-adjusted GDP of Kenya

Issue	Progress	Challenges	Way Forward
Forestry Accounting	Forestry accounts developed; forests contribute 3.6% to GDP	No valuation of carbon sequestration; outdated forest data; lack of inclusion in national accounts	Update forest inventories, quantify carbon sequestration, and integrate into GDP calculations
Ecosystem Services Valuation	Pilot wildlife and biodiversity valuation projects initiated	Lack of standardized methods for valuing carbon sinks and other ecosystem services	Develop and adopt valuation methodologies aligned with UN SEEA framework
Institutional Capacity	KNBS together with Kenya Forest Research Institute leading on NCA; Planned: Water resources account; finalization of the National Plan for Advancement of National Accounting 2025-2028; incorporate NCA in national planning; implement 2025 SNA fully.	Few trained experts; no dedicated NCA units in key ministries; weak integration into fiscal planning	Train professionals, establish NCA units, and embed carbon valuation in budgetary processes
Data and Methodologies	Initial accounts exist for forestry and water basins (Tana, Athi)	Incomplete data; limited geospatial tools; absence of real-time resource monitoring	Improve data collection and invest in GIS and remote sensing for natural capital tracking
Carbon Market Integration	Kenya exploring carbon trading with estimated USD 1 billion potential	Only USD 200 million generated to date; weak regulatory framework; low corporate participation	Strengthen regulations, incentivize carbon credit generation, and engage private sector
GDP Adjustment Integration	Growing policy interest in sustainability accounting	No official GDP adjustment for carbon sequestration due to valuation and reporting constraints	Integrate carbon sequestration into GDP via SEEA-compliant satellite accounts and fiscal tools

Source: Kenya National Bureau of Statistics (KNBS); World Bank WAVES Initiative; Ministry of Environment & Forestry; National Treasury and Planning; UN System of Environmental-Economic Accounting (SEEA) Reports

2.4 Business Capital

2.4.1 Setting the stage

Business capital refers to financial, physical, and intellectual assets that MSMEs like Safaricom, Jumia, and M-Pesa leverage to fund operations, production, and innovation. This type of capital enables businesses to drive growth and create jobs. Access to capital fosters entrepreneurship, boosts productivity, and attracts both local and foreign investment. Opportunities include enhancing mobile banking (M-Shwari), supporting agribusiness through affordable financing, and expanding venture capital for tech startups like Twiga Foods. Increased capital availability can spur innovation in sectors like agriculture, information and communications technology (ICT), and manufacturing, helping Kenya achieve sustainable economic transformation.

2.4.2 Indicators of business capital

75% of Kenya's private sector is composed of MSMEs. These contribute 40.0% of GDP and employ about 14.9 million people. With 120 formal firms per 1,000 people, Kenya's firm density exceeds many developing regions, reflecting a strong private sector. Sub-Saharan Africa's informal firms often have fewer than five workers, underlining Kenya's comparatively higher formal firm density. Key investment opportunities lie in expanding MSME financing in agriculture, manufacturing, ICT, and financial services. Entrepreneurship, indicated by new firm entries, supports sustainable development. In 2024, 130,527 new entities were registered; a 7.6% drop from 2023 due to rising taxes and lending rates. Still, private company registrations rose by 3.2%, underscoring Kenya's dynamic entrepreneurial landscape.

2.4.3 Challenges and opportunities for enhancing business capital in Kenya

Business capital growth is constrained by high informality, costly business registration (15% of GNI per capita), expensive electricity (USD 0.15/kWh), and poor infrastructure. MSMEs face limited access to affordable credit due to high interest rates, collateral demands, low financial literacy, and inadequate rural banking. Widespread mobile banking is insufficient for complex needs. Business capacity is limited by weak financial skills, inadequate Jua Kali spaces, and poor market access. Start-up capital is scarce, and while Uwezo and Hustler Funds offer loans, demand outstrips supply. Table banking supports savings but remains manual. High loan defaults also undermine credit schemes. Key opportunities include expanding affordable financing, digitizing table banking for streamlined financing accounting, enhancing infrastructure, simplifying regulations, lowering service fees, boosting research and development, and increasing awareness of funding options (climate finance, credit guarantees) to unlock MSME growth and strengthen Kenya's business capital.

2.5 Human Capital

2.5.1 Current state of human capital in Kenya

Human capital (skills, knowledge, health, and expertise) is vital to Kenya's economic growth and transformation (Table 4). With an 82.0% literacy rate, the highest in East Africa, Kenya has made significant progress through Free Primary and Secondary Education, and over 600,000 students enrolled in universities in 2023. STEM is promoted via initiatives like the Tunapanda Institute and the New Partnership for Africa's Development (NEPAD) projects.

Ranked third in Africa in human capital development (HCI score: 0.55), Kenya's ICT sector contributes 8% to GDP, fuelling innovation and positioning the country as a tech leader in Silicon Savannah. However, youth unemployment remains high at 39% due to a skills mismatch. Life expectancy has improved to 67 years, supported by Universal Health Coverage though hunger, and malaria (with 70% at risk) continue to pose challenges. Human capital supports industrial growth, with 350,000+ employed in manufacturing aided by TVET expansion. It also fuels entrepreneurship: Kenya's 7.4 million MSMEs employ 15 million people, with government support such as the Hustler Fund improving access to startup capital. Strengthening education, health, and job-market alignment will be key to sustaining growth.

Table 4: Key indicators of education, health, and workforce in Kenya

Indicator	Measurement	Challenges	Way Forward
Education	Adult literacy rate: 82.88% (2022) University enrollment: 600,000+ students (2023) Free Primary and Secondary Education	Skills mismatch with industry demands (e.g., ICT, manufacturing) Unequal access in rural/ marginalized areas (northern Kenya, Coast)	Expand TVET and STEM programs further to target technical skills for green growth Promote digital learning initiatives Align curricula with market needs
Health	Life expectancy: 67.93 years (2025) Universal Health Coverage (UHC) rollout ongoing	Inadequate infrastructure and financing. 70% of the population at risk of malaria. Underfunded rural facilities (e.g., Turkana, Mandera)	Increase health sector budget Strengthen UHC implementation Invest in healthcare workforce development
Workforce	15 million employed in MSMEs ICT contributes 8% to GDP	Youth unemployment: 16% Brain drain (doctors, nurses migrating to UK Gulf). Limited job readiness	Promote entrepreneurship (Hustler Fund) Enhance job training and skilling Expand youth employment initiatives and youth-focused financing tools

Source: World Bank indicators (2022); Macrotrends (2025); Kenya National Bureau of Statistics (2023); World Health Organization (2025)

2.5.2 Major barriers to human capital development in Kenya

These barriers are: (i) Mismatched skills: many graduates lack practical technical and digital skills, especially in ICT and manufacturing, leading to employer-led retraining. (ii) Brain-drain: skilled professionals, including doctors and engineers, increasingly migrate to countries like the UK and the US for better opportunities. (iii) Unequal access to education: rural areas such as northern Kenya and the coast suffer from poor infrastructure, teacher shortages, and limited digital access. (iv) Healthcare constraints: underfunded public health systems, especially in Turkana and Mandera, reduce productivity and stall progress of universal health coverage.

2.5.3 Investing in education and skills development

Investing in education and skills is vital for Kenya's growth. Expanding access needs more funding, digital learning, and better rural infrastructure. Aligning TVETs with green sectors like renewable energy and climate-smart agriculture supports sustainable development. Kenya promotes STEM through initiatives like the Digital Literacy Programme and NEPAD's e-school targeting future workforce demands, with universities increasing STEM enrolment. However, talent retention is a challenge. To tackle brain drain,

Kenya can boost local job opportunities, invest in research, and leverage its skilled diaspora to drive home-grown innovation and entrepreneurship, for long-term skills resilience.

Box 3: Reforms and Investments in Education that Have Worked Well in Kenya

Kenya has made significant strides in education through key reforms and investments. Free Primary and Secondary Education programs boosted enrolment, while the Digital Literacy Programme improved early ICT skills. TVET expansion has increased access to practical training, and the Competency-Based Curriculum emphasizes creativity and problem-solving. The government has strengthened STEM education and raised the education budget to KES 656.6 billion in 2024/25; 27.6% of total spending. School feeding programs now support 2.6 million children, with a goal to reach 10 million by 2027, enhancing learning, retention and well-being.

Source: 2024/2025 Budget highlights; Education Sector Report FY2024/25-2026/27 (2023)

2.5.4 Health as a pillar of human capital development

Challenges affecting workforce productivity include limited access, especially in rural areas, a high disease burden (malaria and non-communicable diseases), low medical staff density (13 doctors per 100,000 people), and 14 hospital beds per 10,000. The National Health Insurance Fund (NHIF) covers 22% of Kenyans, leaving many without financial protection and reducing labour efficiency. Policy options include expanding compulsory NHIF coverage for informal workers, increasing county health budgets, investing in preventive care, digital health solutions, and training more health workers to build a resilient inclusive health system.

2.6 Financial Capital

2.6.1 Domestic capital and financial markets

Kenya's domestic capital and financial markets are central to development financing. The country hosts a diverse financial ecosystem, ranging from 41 commercial banks, 102 fintechs, the Nairobi Securities Exchange (NSE), 56 insurance companies, to real estate, with Nairobi positioned as a regional financial hub, supported by digital infrastructure and regulatory reforms. Overcoming capital flight, tax evasion, underutilized domestic savings, and informality while enhancing financial inclusion, SME access to credit, and digital finance are crucial for full financial capital mobilisation. Remittances have become Kenya's largest foreign exchange source, rising from USD 51 million in 2001 to USD 4.8 billion in 2024, surpassing tea and tourism. Kenya leads the EAC in absolute remittance volumes due to strong diaspora ties and financial infrastructure. However, as a share of GDP, South Sudan (17.5%) leads, followed by Kenya (4.6%), Rwanda (3.9%), and Uganda (2.6%). To maximize remittance impact, Kenya should enhance diaspora engagement, lower transaction costs, and shift remittances toward productive investments. Strengthening capital markets (Box 4) and diversifying pension fund investments also offer sustainable financing for Kenya's long-term growth.

Box 4: Capital Markets Landscape in Kenya

Kenya's capital markets have seen significant reforms, with growth in collective investment schemes, improved governance, and expanded Islamic finance. The bond market is active, investor compensation limits have risen, and Kenya is re-engaging with the East African Capital Markets Infrastructure (CMI) project. The 2014–2023 Capital Markets Master Plan was 74% implemented, advancing market access and investor participation. However, challenges remain, including no new IPOs, stalled privatization, low corporate bond issuance, and high market concentration. Integration with the CMI faces technical and financial hurdles, while legal and governance issues limit private sector access. To advance, Kenya should finalize the privatization framework, reduce competition for capital between public and private sectors, and legislate virtual assets. A second Capital Markets Master Plan should prioritize impact-driven strategies, strong governance, responsive regulation, and structured funding. Fast-tracking regional integration, reforming commodity exchanges, and promoting inclusive, sustainable finance will be key to long-term market development.

Source: April 15 2025 discussions with officials of the Capital Markets Authority

2.6.2 State of financial development in Kenya

Kenya shows relative strength in financial institutions (FIs) but persistent weaknesses in financial markets (FMs), according to the IMF's Financial Development (FD) Index. The overall FD score slightly declined from 0.18 (2012–2016) to 0.17 (2017–2021), ranking Kenya above many Sub-Saharan peers but behind emerging markets like South Africa (0.61). FI performance held steady at 0.28, with improved efficiency (0.60) driven by digital finance gains. However, depth (0.18) and access (0.09) declined slightly, reflecting slow growth in credit, pensions, and insurance. FM performance deteriorated, with the index falling from 0.07 to 0.05 due to sharp declines in depth (0.08), access (0.01), and efficiency (0.06). This reflects reduced listings, low liquidity, and weak capital mobilization. Broader challenges include a low tax-to-GDP ratio (13%) and savings at 17% of GDP. Reforms should prioritize revitalizing FMs by incentivizing listings, streamlining regulation to attract more firms, promoting green/SME bonds, and improving market infrastructure. CBK is leading in these reforms (Box 5). Expanding access to credit, supporting pensions and insurance, and deepening financial inclusion beyond mobile money through inclusive banking are also critical. There are ongoing reforms to streamline the microfinance law for improved governance.

Box 5: CBK's Efforts to Strengthen Kenya's Financial Systems for Inclusive Growth

CBK has taken bold steps to modernize the financial system and promote inclusive growth. It upgraded the Kenya Electronic Payment and Settlement System (KEPSS) to support 24/7 real-time settlements using ISO 20022 standards and championed full interoperability among mobile money operators, allowing seamless transactions across platforms like M-PESA and Airtel Money. To support MSMEs, CBK expanded credit information sharing to include digital lenders and SACCOs, enabling informal businesses to build credit profiles. It also promoted risk-based lending using digital transaction data and encouraged banks to offer tailored mobile-based loans to MSMEs. Beyond this, CBK ensures price stability through data-driven monetary policy, supervises financial institutions under a risk-based framework, and advances financial inclusion via agent and mobile banking. The Bank is also pioneering green finance initiatives, strengthening anti-counterfeit measures with new banknotes, and supporting regional integration through harmonized regulations and cross-border payment systems like the East African Payment System.

Source: April 2025 discussions with officials of the Central Bank of Kenya

2.6.3 Mobilizing financial resources for Kenya's development

Kenya's traditional financial sector plays a pivotal role in development financing. Equity and bond markets support long-term capital mobilization, though equity participation remains low and corporate bond issuance has slowed due to past defaults and listing constraints. Insurance mobilizes long-term savings through life and pension products, but its full potential remains untapped due to low coverage, limited product offerings, and regulatory barriers. Unlocking insurance's role requires product innovation, infrastructure investment, and public awareness. Pension funds, with over KES 1.5 trillion in assets, are key institutional investors but remain overexposed to government securities. Greater diversification into clean energy, affordable housing, and regional markets is vital. Alternative finance—including private equity, venture capital, fintech, crowdfunding, and diaspora bonds—offers new capital channels, though scale and regulatory support remain challenges. PPPs and project finance contribute to infrastructure development, hindered by bankability issues and legal risks. Illicit Financial Flows (IFFs), estimated at 3–5% of GDP, undermine capital retention. Curbing IFFs, expanding financial integration in the EAC, and leveraging blended and green finance can enhance Kenya's capacity to finance inclusive, sustainable development.

2.6.4 Off-shore-linked financial resources for Kenya's development

Offshore-linked financial resources are a vital component of Kenya's development finance landscape, encompassing foreign direct investment (FDI), external debt, portfolio flows, remittances, offshore banking, and aid. In 2022, FDI reached USUSD 1.3 billion, focused on telecom, energy, and infrastructure, often routed through offshore hubs like Mauritius and Dubai. Diaspora remittances, mainly from the US, UK, and Gulf states, reached USD 4.94 billion in 2024, supporting households and micro, small, and medium enterprises (MSMEs). Special Economic Zones (SEZs) are drawing offshore-linked investment in value-added sectors. However, rising Eurobond dependence and exchange rate volatility threaten debt sustainability, while portfolio flows are susceptible to capital flight. IFFs, tax evasion, and opaque offshore holdings further erode Kenya's tax base. To mitigate risks, Kenya should strengthen transparency via beneficial ownership registries, align with Financial Action Task Force (FATF) guidelines, including separating anti-money laundering and counter-terrorist financing (AML/CFT) functions from prudential oversight, and improve virtual asset supervision. Reformed tax treaties, trade mispricing oversight, and blended finance strategies can help channel offshore capital into climate adaptation, green infrastructure, and agriculture, ensuring long-term, sustainable financing.

2.6.5 Innovative finance

Kenya is increasingly turning to innovative finance mechanisms, such as blended and green finance, to bridge its development funding gaps. Blended finance, which combines public and private capital, has attracted over 95 impact investors managing more than 136 capital vehicles in Kenya, channelling funds into climate-resilient infrastructure, renewable energy, and SME development. Green finance is also gaining traction, with frameworks like the Green Bond Programme and the Green Fiscal Incentives Framework supporting climate-aligned investments. Kenya's dynamic FinTech ecosystem, comprising over 385 startups, plays a crucial role in mobilizing domestic savings and extending credit. Platforms such as M-Pesa, M-Shwari, and Fuliza have revolutionized financial inclusion, enabling broader

access to financial services. These digital solutions are instrumental in channelling funds into productive sectors like agriculture and clean energy, aligning with Kenya's Vision 2030 goals. To maximize the potential of innovative finance, Kenya should continue to strengthen its regulatory frameworks, enhance transparency, and foster partnerships between the public and private sectors. Such efforts will ensure that financial innovations become a sustained source of alternative financing for Kenya's development.

2.7 Policy Recommendations

Unlocking Kenya's development potential requires coordinated action across local and global stakeholders.

- **Fiscal Capital:** The government can expand the tax base by formalizing the informal sector, accelerating compliance through digital education and tax administration, and eliminating inefficient tax incentives. Development partners and Multilateral Development Banks (MDBs) can support fiscal reforms, tax capacity building, and performance-based budgeting.
  Recent support to Kenya include AfDB investments in energy, transport, and skills development (about USD1.2 billion over 2023-2025), World Bank's 2024 USD1.5 billion Development Policy Operation to support governance and fiscal reforms, IMF's Extended Fund Facility/Extended Credit Facility USD2.34 billion program, and EU Euro250 million budget support and green transition funding commitment over 2023-2025.
- **Natural Capital:** Kenya can scale up value addition in agriculture, mining, and renewables. Development Finance Institutions (DFIs) and donors can finance green value chains, natural capital accounting, and enforcement against IFFs.
- **Business Capital:** Kenya can expand credit guarantee schemes with seed money from the current KES 100 million to KES 5 billion, and simplify business regulations for MSMEs, while partners support venture capital and fintech infrastructure. In terms of capacity, the Kenya Institute of Business and Kenya Private Sector Alliance provides MSMEs with bookkeeping skills and absorbs 70% of the youth in digital upskilling programs.
- **Financial Capital:** Deepen capital markets through green and SME bonds, with diversified pension and insurance fund investments. MDBs can offer de-risking tools. Leverage fintech to mobilize savings and expand credit access; increase blended finance for climate-resilient investments. Strengthened governance, data systems, and public-private partnerships are essential to ensure sustainable capital mobilization.
- **Human Capital:** Expand STEM and TVET aligned with green growth sectors; scale up digital and health infrastructure for productivity.

HARNESSING KENYA'S CAPITAL POTENTIAL FOR DEVELOPMENT

3

KEY MESSAGES

- Kenya has made some progress, but stronger institutions and a transparent rule of law are essential to enhance capital mobilization, maximize the development potential of natural resources, protect rights, and encourage sustainable investment in both renewable and non-renewable capital.

- Improving the ease of doing business will be essential to involving the private sector in the governance of key capital assets for Kenya's development. This will include formalising the informal sector to widen the country's tax base.

- Building capacity for various entities in the context of devolved governance will be instrumental in enhancing both service delivery and resource management.

3.1 Introduction

The chapter explores the impact of institutional quality, governance, and the rule of law on Kenya's capacity to mobilize domestic capital for sustainable development. Despite being rich in natural, human, business, and financial capital, Kenya's progress is hindered by weak institutions, corruption, and capital flight. The chapter emphasizes the government's critical role in resource management and economic advancement, analysing current institutional frameworks, governance issues, and areas for reform. It presents evidence-based, scalable strategies to reduce financial leakages and harness Kenya's capital base to promote structural transformation and inclusive growth.

3.2 Institutional arrangements for the management and utilization of the various forms of capital for resource mobilisation

Institutional quality is critical to Kenya's ability to mobilize, manage, and effectively utilize its natural, human, financial, and business capital for sustainable development and structural transformation. Strong institutions foster governance, transparency, and the rule of law, which build investor confidence, reduce leakages, and improve service delivery. Conversely, weak institutions contribute to capital flight, corruption, and inefficiencies that undermine Kenya's development potential. Kenya has made notable progress in establishing institutional frameworks to support economic growth. Institutions such as the Competition Authority of Kenya (CAK), the Public-Private Partnerships Unit (PPPU), the Public Investment Management (PIM) Unit in the National Treasury, and the Capital Markets Authority (CMA) demonstrate government efforts to improve capital governance. These bodies aim to streamline public investment, deepen capital markets, promote competition, and coordinate infrastructure development. For example, the Public Private Partnerships Act (2013)

enabled private sector participation in large infrastructure projects, while the Public Investment Management Information System (PIMIS) platform helps track and evaluate public investments across national and county governments.

Despite these reforms, institutional weaknesses persist. Transparency International's 2024 Corruption Perception Index (CPI) ranked Kenya 121 out of 180 countries with a score of 32 out of 100, a slight improvement from the previous year's 126 ranking with a score of 31. Kenya's score remains below the global average of 43 and the Sub-Saharan Africa average of 33, signalling persistent challenges in addressing public sector corruption. Illicit International Financial Flows (IIFFs), driven mainly by trade mis-invoicing and tax evasion, cost Kenya billions annually. In the extractives sector, mining contributes less than 1% of GDP despite its potential to add 4–10%, largely due to IFFs and regulatory weaknesses.

Legislation such as the Mining Act (2016), Proceeds of Crime and Anti-Money Laundering Act (2009), and Anti-Corruption and Economic Crimes Act (2003) provide legal frameworks to combat corruption and financial crimes. However, enforcement is weakened by limited political will, under-resourced agencies, and poor inter-agency coordination. In this context, law enforcement agencies and the judiciary play critical roles. Law enforcement bodies should be able to investigate and prosecute corruption, money laundering, and financial crimes independently and free from political interference to ensure accountability. The judiciary, as the ultimate arbiter, enforces the rule of law by adjudicating cases fairly, ensuring due process, and providing legal certainty. An independent judiciary is essential for deterring corruption and ensuring laws are effectively implemented rather than symbolic.

The KRA faces challenges in expanding the tax base due to the dominance of the informal sector (86% of employment), inefficiencies in tax administration, and public resistance to new taxes. Consequently, Kenya's tax-to-GDP ratio remains low at 13%, well below the 20% African target. Public spending inefficiencies, estimated at 5% of GDP, along with revenue leakages and over-generous tax exemptions further restrict fiscal space.

Nonetheless, Kenya has demonstrated institutional innovation. The Micro and Small Enterprises Development Act (2013) has helped formalize informal businesses. The Capital Markets Master Plan (2014–2023) laid the foundation for deeper, more inclusive financial markets, while mobile money and fintech regulation have propelled Kenya to global leadership in digital finance. Kenya's green energy sector, with 90% of grid electricity from renewables, illustrates how policy and regulation can align capital mobilization with sustainability goals.

Moving forward, Kenya should strengthen enforcement of anti-corruption laws by enhancing the capacity and independence of law enforcement agencies, including the Directorate of Criminal Investigations and the Ethics and Anti-Corruption Commission. Expanding institutional capacity in accountability bodies such as parliament, the Auditor General's office, and the judiciary is equally important. Digitizing public financial management and improving inter-agency coordination can reduce leakages and enhance transparency. Improved institutional quality--particularly in natural capital management and enforcement of property and contractual rights by the judiciary --will reduce resource leakages, attract long-term investment, and enable Kenya's capital to drive inclusive sustainable development.

Ultimately, the rule of law, upheld by robust law enforcement and an independent judiciary, remains the foundation for sustained economic growth, social equity, and public trust in governance.

3.3 Governance challenges in the management and utilization of the various forms of capital for resource mobilisation

Governance, comprising clear rules, capable institutions, and inclusive processes, critically shapes how Kenya mobilizes and utilizes capital for development. Kenya's 2010 Constitution created a devolved system to enhance local accountability, established oversight institutions, and strengthened democratic governance. Yet, despite a solid constitutional foundation, weaknesses in implementation have hindered domestic capital mobilization and economic transformation. In the 2024 Ibrahim Index of African Governance, Kenya scored 60.3, ranking 10th in Africa. Yet gaps in tax governance, capital allocation, and Public Financial Management (PFM) continue to hinder domestic resource mobilization.

Kenya's tax system suffers from significant governance challenges that limit revenue mobilization. It relies heavily on a narrow formal sector, while 86% of the population works in the informal economy and contributes little to tax revenues. Although income tax accounts for 45% of total collections, the country's tax-to-GDP ratio has declined over the past decade. The Medium-Term Revenue Strategy (MTRS) 2023/2024 highlights a drop in tax effort and recognizes poor capacity to tax hard-to-reach areas like the digital and informal economies. Inadequate taxation of elite wealth, low rates on sin taxes, and an underdeveloped property tax regime further constrain revenues. In addition, the absence of a clear tax framework for emerging sectors such as online gambling leaves significant revenue potential untapped.

Institutional weaknesses constrain the protection and productive use of Kenya's natural capital. Although the extractive sector holds substantial potential, it contributes less than 1% to GDP due to IFFs, underreporting, and poor enforcement. Kenya has enacted several legal frameworks, including the Mining Act (2016), the Proceeds of Crime and Anti-Money Laundering Act (2009), and the Anti-Corruption and Economic Crimes Act (2003), alongside strategies like the National Action Plan on IFFs. However, enforcement is weak, hampered by poor inter-agency coordination, limited technical capacity, and political interference. Additionally, Kenya's land tenure system presents structural challenges. Insecure land rights and weak enforcement of land laws undermine sustainable resource management. Exploitation often occurs without benefiting local communities, while rapid urbanization and speculation place stress on fragile ecosystems.

Devolution introduced new institutions at county level, but also fragmentation. Counties face several fiscal governance challenges, including underspending or low absorption of development funding, under collection of own source revenues, spending on non-core activities, and inequitable resource distribution. The Public Financial Management Act (2012) governs spending across national and county levels, but inefficiencies remain. Disagreements between county and central governments further disrupt budget execution. These governance weaknesses reduce transparency and accountability, leading to leakages and low public confidence.

The impact of these challenges is severe. Corruption and IFFs cost Kenya up to USD 1.5 billion annually - funds

that could transform health, education, and infrastructure development. Public spending inefficiencies account for 5% of GDP. Tax exemptions and incentives cost an additional USD 0.8 billion annually, limiting fiscal space. Combined, these losses undermine Kenya's capacity to finance its own development and reduce reliance on external aid.

To improve capital mobilization, Kenya can enhance institutional capacity, strengthen PFM at both national and county levels, and ensure political independence and adequate resourcing of oversight bodies. The Office of the Controller of Budget plays a key oversight role in controlling, reporting, advising and sensitising in addressing these challenges. Regulatory frameworks must be streamlined and enforced, with tax policy reforms that address equity, emerging sectors, and compliance. Reinforcing inter-agency coordination and digitalizing tax and spending systems will also improve transparency and reduce leakages. Ultimately, stronger governance will unlock Kenya's capital potential.

3.4 The rule of law, management and utilization of the various forms of capital

In Kenya, "state capture," where political elites dominate rule-making and rule-interpreting processes, has significant implications for economic growth, investment, and capital mobilization. This undermines the rule of law, creating an environment of uncertainty, corruption, and weak governance. Such an environment hampers the protection of property rights, enforcement of contracts, and increases the risk of expropriation, which are essential for sustainable development.

Kenya's judicial system, pivotal in economic governance, faces challenges such as judicial corruption, inefficiency in contract enforcement, and slow resolution of disputes, thereby undermining economic stability. Corruption scandals such as Goldenberg and Anglo-Leasing exposed institutional flaws, eroding investor confidence. Investors fear biased rulings, delays, and lack of transparency, increasing operational risks and deterring investment. Protracted legal battles, like the Bidco Africa vs. KRA case, exemplify how lengthy judicial processes drive up business costs and stifle growth. Delayed contract enforcement increases risk premiums, raising the cost of capital and deterring long-term investment. This uncertainty further inhibits investment critical for economic expansion.

Kenya's volatile tax policies add unpredictability. Frequent changes, such as the increase in capital gains tax and new taxes on digital assets, complicate the business environment. These shifts undermine tax regime stability, which is crucial for an investment-friendly climate. Businesses navigating shifting tax laws face greater compliance risks, deterring investors from committing capital.

Weaknesses in enforcing property rights and contracts hinder effective capital utilization. Investors hesitate to invest in regions where legal protections are unreliable, reducing both FDI and local capital mobilization, especially in key sectors like manufacturing, agriculture, and infrastructure. The failure to safeguard investor interests leads to underutilization of resources, stalling economic progress.
To address these issues, Kenya must prioritize strengthening the rule of law by more effective contract enforcement, enhanced property rights protections, and tackling corruption within the judiciary. Judicial reforms that speed up dispute resolution, reduce corruption, and improve transparency will increase investor confidence. Furthermore, the government

should stabilize the tax environment, minimize abrupt policy changes and foster predictability.

While each country's unique context must be acknowledged, successful African nations offer valuable lessons. Rwanda, for instance, has created an enabling environment for investment and growth by prioritizing institutional strengthening and the rule of law. Its efficient judiciary and commitment to transparent governance have significantly boosted foreign direct investment. Similarly, Mauritius has leveraged its stable legal framework and strong adherence to the rule of law to attract both foreign and domestic investment, contributing to robust economic performance.

Strengthening judicial institutions, reducing corruption, ensuring contract enforcement, improving tax compliance, and fostering a predictable legal environment will attract the necessary investments to drive long-term economic growth. By enacting these reforms, Kenya can harness its capital potential, unlock investment opportunities, and position itself as a regional economic leader. Ultimately, this will support the country's broader goals of poverty reduction, job creation, and enhanced living standards for all.

3.5 A Pan-African approach to strengthening the rule of law, institutions and governance for harnessing Kenya's capital

Kenya's potential for cross-border initiatives lies in strengthening regional cooperation through frameworks like the EAC, the African Union, and the Alliance for Financial Inclusion, which align with its constitutional aspirations and commitment to Agenda 2063. Collaborative efforts with the International Criminal Police Organization and the African Union Mechanism for Police Cooperation, along with participation in the Financial Action Task Force (FATF) compliance and regional anti-money laundering actions, aim to curb IFFs. Successful case studies include the African Union's High-Level Panel on IFFs and EAC regulatory harmonization, which help mitigate capital flight, tax avoidance, and ensure effective profit sharing, fostering investment and sustainable development.
Conclusion and policy recommendations

- **Fiscal Capital:** Strengthen tax administration with digital platforms and improve fiscal transparency to ensure effective use of public funds.

- **Natural Capital:** Strengthen land tenure systems for sustainable agriculture investments and implement environmental governance reforms to attract green investments.
- **Human Capital:** Enhance judicial independence to enforce labor rights and invest in education reforms aligned with market demands.

- **Business Capital:** Improve contract enforcement, reduce delays in dispute resolution, and strengthen public-private partnerships for infrastructure.

- **Financial Capital:** Strengthen financial regulations against illicit flows and enhance financial reporting transparency to attract investments.

REFERENCES

African Development Bank (AfDB), 2025. Africa's Macroeconomic Performance and Outlook. January. African Development Bank. Abidjan, Côte d'Ivoire.

African Development Bank. (2023). Country Focus Report 2023, Kenya: Mobilizing Private Sector Financing for Climate and Green Growth. Retrieved from AfDB

Brookings Institution. (2022). Could Africa replace China as the world's source of rare earth elements?. Retrieved from Brookings

Business Daily Africa. (2023). How Kenya can tap power of its rare earth elements. Retrieved from Business Daily Africa

Central Bank of Kenya (CBK), 2023. Annual Report 2023/24. Central Bank of Kenya. Nairobi.

Communications Authority of Kenya (CAK), 2023. Telecommunications and ICT Sector Statistics Report. CAK. Nairobi.

Energy Capital & Power. (2025). African Rare Earth Projects Advance Amid Rising Global Demand. Retrieved from Energy Capital & Power

Government of Kenya, 2010. The Constitution of Kenya. National Council for Law Reporting. Nairobi.

Government of Kenya, 2013. Micro and Small Enterprises Development Act. Government Printer. Nairobi.

Government of Kenya, 2015. Tax Procedures Act. Nairobi.: National Council for Law Reporting.

Government of Kenya, 2016. Mining Act. Government Printer. Nairobi

Government of Kenya, 2019. Kenya Investment Policy (KIP). Nairobi. Ministry of Investment, Trade and Industry.

Heritage Foundation, 2025. Index of Economic Freedom 2025. The Heritage Foundation. Washington, DC.

International Energy Agency. (2021). The Role of Critical Minerals in Clean Energy Transitions. Retrieved from IEA

International Monetary Fund (IMF), 2024. Kenya: Economic Outlook and Fiscal Policies. International Monetary Fund. Washington, DC.

International Renewable Energy Agency. (2022). Critical Materials for the Energy Transition: Rare Earth Elements. Retrieved from IRENA

Kenya National Bureau of Statistics. (2023). Compendium of Environment Statistics 2023. Retrieved from KNBS

Kenya National Bureau of Statistics (KNBS), 2023. Economic Survey 2023. KNBS. Nairobi.

Kenya National Bureau of Statistics (KNBS), 2023. Natural Capital Accounting Report. KNBS. Nairobi.

Kenya Revenue Authority (KRA), 2024. Tax Revenue Performance Report 2023/24. KRA. Nairobi.

Macrotrends. (2025). Kenya Life Expectancy 1950–2025. https://www.macrotrends.net/global-metrics/countries/KEN/kenya/life-expectancy

Oxfam, 2024. Kenya's Taxation System and Revenue Mobilization. London. Oxfam International.

Safaricom PLC, 2023. Annual Report 2023. Nairobi. Safaricom PLC.

Transparency International, 2024. Corruption Perceptions Index 2024. Berlin. Transparency International.

United Nations (UN), 2023. System of Environmental-Economic Accounting (SEEA): Implementation in Kenya. United Nations Statistics Division. New York.

World Bank, 2023. Kenya Economic Update: Enhancing Domestic Revenue Mobilization for Sustainable Growth. World Bank Group.

World Bank, 2023. Wealth Accounting and the Valuation of Ecosystem Services (WAVES) Initiative Report on Kenya. Washington, DC. World Bank Group. Washington, DC.

The EastAfrican. (2013). Kenya's USD 100 billion hidden mineral deposits. Retrieved from The EastAfrican

International Renewable Energy Agency. (2022). Critical Materials for the Energy Transition: Rare Earth Elements. Retrieved from IRENA

World Bank. (2022). Literacy rate, adult total (% of people ages 15 and above) - Kenya. https://data.worldbank.org/indicator/SE.ADT.LITR.ZS?locations=KE

Kenya National Bureau of Statistics (KNBS). (2023). Kenya Facts & Figures. https://www.knbs.or.ke/reports/2023-kenya-facts-figures/

World Health Organization (WHO). (2025). Kenya Health Profile.

