The State of Kenya’s Private Sector

Recommendations for Government, Development Partners and the Private Sector
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A thriving private sector is central to achieving the objectives of Kenya’s Vision 2030. In fact the success of Vision 2030 is largely premised on the role of the private sector in achieving the country’s growth objectives and, thereby, creating greater wealth and employment opportunities.

Six priority sectors were targeted in Vision 2030 to raise the national GDP growth up to 10% by 2012. These sectors are: Tourism; Agriculture, Livestock and Fishing; Wholesale, Retail and International Trade; Manufacturing; Business Process Outsourcing; and Financial Services. In addition, the Government prepared a Private Sector Development Strategy (PSDS) 2006-2010 and Private Sector Development Strategy Implementation Plan (PIP) 2007-2012 to support the development of the private sector. The PSDS and PIP were focused, primarily, on addressing the poor business environment, and improving the competitiveness and productivity of the private sector (especially micro, small and medium enterprises).

The purpose of this report is to measure the private sector’s actual contribution to the Kenyan economy and, as a result, the progress and success of the aforementioned policies. This is done by providing an in-depth profile of the private sector and how it has evolved over the last five or so years, as well as a detailed assessment of the current business environment for private sector growth in Kenya. Given the new constitution and a new system of devolved government, a section is also dedicated to understanding what this might mean for private sector activities.

Ultimately, we hope the insights and recommendations in this report are instructive in guiding Kenyan policy makers as they formulate a new approach to developing the private sector going forward and, thereby, enhancing its role as the primary driver of the economy. In addition, the report also draws insights and recommendations for development partner’s active in this space, as well as the private sector themselves and the options they have to enhance their contribution to the economy.

The African Development Bank has recently adopted a Ten Year Strategy (2013-2022), which is designed to place the Bank at the center of Africa’s transformation. One key priority of this strategy is private sector development. Through this report and the Bank’s continued support to Kenya, we hope to play our role in building an even stronger, more dynamic and inclusive private sector.

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This briefing note accompanies a fuller report on the state of the private sector in Kenya\(^1\). It captures recommendations for the Government of Kenya, development partners and the private sector itself, to develop the private sector faster and further.

The research and analysis was undertaken by development consultants Genesis Analytics (South Africa and India), in association with Integral Advisory (Kenya).

**Methodology**

The purpose of the study was to map the size, nature and health of the Kenyan private sector. The data gathering process consisted of three stages. The first reviewed all available data on Kenya’s private sector, including data kindly made available by the Kenya National Bureau of Statistics (KNBS) and the World Bank, UNCTAD, business associations, government policy papers and sector studies, as well as all literature from 2007 to 2012 describing the state of the business environment.

Next, fifty face-to-face interviews were held with interested parties, including government officials, development partners, business associations and captains of industry.

Lastly, workshops were held with members of business associations - KAM, KENFAP, KFC, KATO, KAHC, KNCCI, the informal sector and Jua Kali - and others.

The interim findings were presented for validation to representatives of government, development partners and the private sector.

A draft report, including recommendations, was circulated for comment, before the report was finalised.

The overall finding of the report is that the private sector in Kenya is vibrant and in good health. Kenya is a promising place to do business, with growing markets and good opportunities. Importantly, there is a widespread intellectual appreciation amongst Kenyans, including government officials, that the private sector is important and will be the main driver of growth and employment, rather than the state. Positively, the business climate has improved over the last decade; frustratingly it is the same recurrent challenges that prevent the private sector from reaching its full potential: political uncertainty, corruption, infrastructural deficits, and an untapped informal sector.

This report explores seven characteristics of the private sector:

1. **Importance and size**: The private sector is well developed and large by sub-Saharan and regional standards and plays the leading part in the Kenyan economy. The health of the economy and benefits to citizens are directly correlated to the health of the private sector.

2. **Growth**: The private sector has been growing and continues to grow, impressively at times, though on balance remains below full potential. A number of infrastructure, regulatory, security and political challenges persist in restraining private sector growth.

3. **Structure**: The private sector is noticeably split into two parts: a formal, large business sector which is relatively healthy and productive, and a massive, informal small business sector that is poorly understood and supported, yet which employs almost nine out of ten workers. Links between the formal and informal sectors are very weak – and initiatives that bridge the gap should be a priority.

4. **Diversification**: The formal private sector is well diversified across primary, secondary and tertiary activities, and the tertiary sector is impressive for a developing country. Exports, however, are dominated by a handful of globally competitive agricultural products, with limited value addition.

5. **Sectors**: Agriculture, manufacturing, trade, tourism, transport and communication, and financial services account for over 80% of the private sector’s contribution to total GDP. Agriculture remains the most important sector in terms of contribution to private sector GDP and employment, though the importance of agriculture in terms of its contribution to GDP is declining relative to other sectors, while that of manufacturing remains relatively stagnant. Growth in the private sector is increasingly driven by trade, transport, ICT and financial services.

6. **Local versus foreign ownership**: The private sector is relatively closed and concentrated – dominated by domestic companies and attracting less FDI than much smaller neighbouring countries, in both absolute and relative terms. Early indications are that this FDI underperformance may be changing, possibly related to the discovery of oil.

7. **Stability**: The performance of the private sector is volatile primarily because business must operate in a politically charged environment. Political disruption and uncertainty is the most obvious brake on consistent private sector (and economic) growth. Also, the private sector is structurally exposed to shocks – tourism to demand shocks, agriculture to supply shocks and the whole economy to import inflation, especially from fuel imports, make stable and consistent growth harder to achieve.

Figure 1: The dualistic structure of the Kenyan economy is apparent, with a poorly quantified informal sector.

![Output](KSh 1.3 trillion?)

Formal sector

Informal sector

Employment

2 million

9 million

Note: agriculture is not included in the measure for informal sector employment, as KNBS observes the ILO definition of the informal sector, which excludes primary activities. KNBS calculations suggest that most people working in the informal sector (approximately 60%) are traders in the wholesale and retail trade sector.

KNBS only captures data for ‘hotels and restaurants’, which is used as a proxy for tourism. In 2007, Vision 2030 estimated that tourism accounts for 10% of Kenya’s GDP, whereas in 2009, KIPPRA estimated a 5% GDP contribution.
Figure 2:
Relative employment creation, average growth rate, and % contribution to GDP (2011) for Kenya’s main sectors

Source: Genesis Analytics 2012 (adapted from KNBS Economic Survey 2012 and Statistical Abstract 2011)
3. Strengths, Challenges and Opportunities

Below is a summary of the main strengths and challenges of the Kenyan private sector and the environment in which it operates; followed by a selection of emerging opportunities that, if capitalised upon, would contribute to stronger private sector growth and development.

3.1. Strengths

The diversified nature of the Kenyan private sector bolsters its ability to weather external shocks (although still vulnerable) and bodes well for future resilience in a competitive global market. It is clear that the private sector drives growth and employment in the economy.

The private sector is vibrant and it benefits from a well-educated and entrepreneurial workforce. The private sector is more developed, in terms of scale and sophistication, relative to Kenya’s neighbours. This has contributed to Kenya’s status as a net exporter to all other East African Community (EAC) countries. In the global market, the private sector is competitive in a variety of export products, especially tea, cut flowers, leguminous vegetables and cements.

Government has invested, and continues to invest, in the improvement of transport infrastructure. Kenya’s infrastructure advantage, relative to its neighbours, combined with its strategic geographic position, affords the country the status of a regional trade and transport hub. The tertiary sector is growing in importance as a value adder and employer. Notably, Kenya has an innovative and fast-developing ICT industry that also enables the financial services sector (e.g. M-Pesa), which in turn is growing rapidly.

Finally, it appears that there is widespread intellectual appreciation within the Government of Kenya that the private sector is important and should be developed, as well as a genuine commitment to dialogue and partnership. This augurs well for positive, collaborative outcomes in private sector development.

3.2. Challenges

Kenya has a disruptive political cycle, with a mediocre, but improving, business climate. Political uncertainty, especially around elections, and the associated volatility is arguably the main handbrake on sustained private sector investment and growth. Without long periods of stability and peaceful transitions of government, private sector performance will continue to underperform against its long-term potential.

There is widespread perception of corruption, political interference and patronage in business, which hinders small businesses in particular.

Macro-economic volatility has been cited as a challenge to doing business. The cost of capital is high and a variable exchange and inflation rate is challenging to business operations and planning. The macro-economy has been more stable in recent years. Critical enabling infrastructure remains below par: Transport infrastructure and logistics systems (including customs, goods clearance and weighbridge processes) are persistently weak for a regional trade and transport hub. High energy costs and weak and interrupted supply of power are crippling to business, especially manufacturing businesses.

A possible outcome of the aforementioned political uncertainty, macroeconomic volatility and high costs of doing business is a low level of foreign direct investment (FDI) - an anomaly for a pre-eminent regional market. This FDI status quo could also be a function of company and land ownership restrictions, a closed and protective political economy with strong local vested interests and anticompetitive behaviour by dominant firms. However, early indications are that FDI might be increasing, primarily driven by opportunities in oil.

There is a reported mismatch of skills of those leaving the education sector and those attractive to the private sector, particularly in new and fast-paced industries such as ICT.
The private sector is bifurcated between the formal sector and mostly informal MSE sector with weak linkages between the two. The informal sector is poorly understood and documented, and is not supported by coherent government action. There is limited empirical evidence for the factors that give rise to a large, fragmented and delinked informal sector in Kenya. Anecdotal evidence suggests that the main barriers to growth and formalisation include low skills and access to technology; high effective tax rates; an unfriendly regulatory environment for small business (e.g. trading restrictions and minimum wage regime); inadequate access to financial services; and a poor collective voice of small business, particularly in policy decisions.

There is a lack of comprehensive and consistent economic data for the tourism and ICT (including Business Process Outsourcing (BPO)) sectors, as well as FDI, which inhibits evidence-based policy decisions. There is a perception by business that the pace of government reform is too slow and the administration is characterised by fragmentation and duplication of effort, compounded by unnecessary bureaucracy and red tape (e.g. the burden of inefficiencies within the tax system).

Finally, the impact on business of devolved government is still unclear but may be mildly negative overall, at least during the transition period. The ability to maximise county-level opportunities and foster a business friendly environment will greatly depend on the vision and capability of county leadership, which is still untested.

3.3. Opportunities

The Constitution is likely to be a positive force for the private sector, if it is upheld and if constitutional institutions are properly empowered. It should promote a more transparent and stable economic environment in which the private sector can confidently invest.

Much of the vision for a more inclusive, growing and wealth-creating private sector depends on the government’s ability to implement stated policies and plans in a timely fashion. That said, it is also incumbent on the private sector to leverage the opportunities within the country and region, and to play a role in holding government to account and bridging the gap between the formal and informal sectors.

Opportunities include an increasingly attractive domestic market, with improving appeal to foreign investors, particularly in the ICT, manufacturing and financial services sectors, and a rapidly urbanising Kenyan population, which may present further opportunities in sectors such as retail trade, construction and real estate.

The technological innovations emerging from the ICT industry, such as those that improve access to, and functionality of, mobile phone and internet services have the potential to catalyse growth and improve efficiencies.

Government’s intention to increase public-private partnerships (PPPs), particularly in large infrastructural projects presents an opportunity for private sector involvement in national development, and the multiplier effects of these developments will improve growth across the economy. Infrastructural developments will also assist in the facilitation of increased regional trade in goods and services resulting from increased access to the EAC common market.

Government actions emerging from the Micro and Small Enterprises (MSE) Act will present opportunities for the inclusion of small enterprises in the formal economy.

Possibilities for growth exist in Kenya’s “budding sectors”, namely oil & gas and real estate. The discovery of oil in the Lake Turkana region can play a transformative role in the economy, accelerating the growth trajectory of the private sector and providing a boost to the fiscus. If handled poorly it may also bring the attendant problems of “Dutch disease” and escalate the extent and magnitude of corrupt activity and civil unrest.
A number of insights and recommendations emerge for developing the private sector further and faster, the responsibility for which are shared by policy makers (Government of Kenya), development partners, and the private sector itself. The recommendations are grouped around six topics:

- Improving the business and investment climate;
- Understanding and supporting MSEs and the informal sector;
- Mitigating possible negative consequences of devolved government, and upholding the Constitution;
- Encouraging further public/private co-operation;
- Supporting sector growth and competitiveness; and
- Improving the collection of economic data relating to the private sector.

Below are the detailed recommendations per topic area, differentiated by stakeholder.

### 4.1. Improving the Business and Investment Climate

#### 4.1.1. Eliminate Corruption and Political Patronage in Government Decision Making

Corruption has long been a challenge for private sector development in Kenya. Corrupt behaviour from both private and public representatives (especially in public procurement, licensing and land administration) increases the cost of doing business, creates unfair competition, favours inefficient and larger firms to the detriment of smaller players, and generally impedes private sector investment.

Recommended actions for the Government of Kenya are:

- Fast-track the computerisation of government processes (relating for example to fees, tax and procurement) to increase transparency and close avenues for corrupt behaviour.
- Fully implement the existing ethics policy and strengthen other policies on declaring interests transparently and managing conflicts of interest in relation to politician/public servant participation in business.

Recommended actions for development partners are:

- Provide strategic support in the form of technical capability and systems capacity building to the Public Procurement Oversight Authority, Ethics and Anti-Corruption Commission and Land Commission.
- Share global best practice on policies and associated implementation around declaring interests transparently and managing conflicts of interest in relation to politician/public servant participation in business; and whistle-blower protection mechanisms.

Recommended actions for the private sector are:

- Actively monitor the work of the Public Procurement Oversight Authority, Ethics and Anti-Corruption Commission and Land Commission.
- Finalise, activate and monitor adherence with the Kenyan Private Sector Alliance (KEPSA)-led private sector Code of Conduct, to tackle private sector participation in corrupt behaviour.
- Create and support a non-aligned private sector-funded non-governmental organisation (NGO) “Corruption Watch” entity, which has the resources to investigate and publish instances of both private and public sector corruption.

#### 4.1.2. Accelerate Investment in Critical, Enabling Infrastructure

This infrastructure deficit particularly relates to energy and transportation. Lagging infrastructure increases the cost of doing business, and lowers the country’s private investment appeal and competitiveness.
Recommended actions for the Government of Kenya are:

- Continue government’s infrastructure investment programme in energy, telecoms, roads, ports, rail, airports and associated mass transit services (goods and passenger).
- Accelerate implementation of infrastructure plans by activating public-private partnerships (PPPs), ideally starting with small/medium-sized projects to build experience and confidence. Proactively improve understanding within government of the benefits of PPPs, and a clear understanding of their complexity, long-term nature and cost and risk implications.
- Fast-track the finalisation of a policy to promote and regulate competition in the electricity market.
- Review procurement policies and regulations for government infrastructure projects to identify and remove bottlenecks.

Recommended actions for development partners are:

- Continue co-financing of government’s infrastructure investment programme in energy, telecoms, roads, ports, rail, airports and associated mass transit services (goods and passenger).
- Build government capacity to initialise and manage public-private partnerships (PPPs), including the structuring and negotiating of deals, ideally starting with small/medium-sized projects to build experience and confidence. Codify and share with government and the private sector the benefits of PPPs, as well as their complexity, long-term nature and cost and risk implications.

4.1.3. Investigate and remediate anti-competitive behaviour

Abusive firm-level behaviour creates barriers to entry for competitors and leads to business inefficiencies. If anti-competitive behaviour occurs in a major input sector, higher prices than necessary are pushed throughout the economy.

Recommended actions for the Government of Kenya are:

- Finalise and implement the planned privatisation of state-owned enterprises, especially in cement, sugar and hotels.
- Revise the role of marketing boards to remove bottlenecks and address instances of market failure, for example, in pyrethrum, coffee, cereals and produce.
- Instruct the Competition Authority of Kenya (CAK) to investigate and resolve potential competition problems in a timely fashion, prioritising major input sectors and those sectors with strong linkages to multiple sectors. Industries for possible review include: cement, trucking, banking, petroleum, beer, maize, fertiliser, sugar, pay TV, and domestic air passenger transport.
- Require private sector participants in government infrastructure projects to disclose in tender submissions that there was no hard core cartel conduct, collusive tendering or bid rigging in preparing the tender.

Recommended actions for development partners are:

- Commission an assessment of the role of marketing boards, with a view to remove bottlenecks and address instances of market failure, for example, in pyrethrum, coffee, cereals and produce.
- Provide strategic capacity building and support to ensure that the CAK executes investigations and market enquiries with minimum political interference and maximum cooperation.

4.1.4. Address mismatch of skills between education sector and private sector

A supply-demand skills mismatch affects new and fast-paced industries, resulting in extra investment training of new recruits or the ‘importing’ of skills, and thus higher labour costs.
Recommended actions for the Government of Kenya are:

- Establish effective mechanisms for dialogue between the public and private sector to ensure that skills development is demand-driven – rather than driven by the educational institutions.
- Undertake joint public-private sector planning to improve effectiveness in the use of training levies (for example, industrial and tourism training levies) to improve skills.
- Formulate as a PPP a framework for interaction between teaching professionals and the private sector, to ensure the currency and relevance of skills and knowledge of educationalists.

Recommended actions for development partners are:

- Share global best practice in creating the feedback mechanisms between the public and private sector to better match the supply and demand of skills.
- Commission a review of the funding and operating model of the National Industrial Training Authority (NITA) and Utalii College to improve their effectiveness.
- Provide funding to a) support dialogue between the public and private sector to ensure that skills development is demand-driven; and b) implement a PPP framework that supports interaction between teaching professionals and the private sector.

4.1.5. Foster a Business-Friendly Regulatory Environment

Challenges in the regulatory environment relate primarily to outdated company legislation, business permit procedures and local ownership requirements in selected industries. Furthermore, by not including Regulatory Impact Assessments (RIA) into the legislative process to ensure regulatory rigour and consistency across national and county government, the result may be the “Balkanisation” of business regulation across 47 counties. This perpetuates investment uncertainty and increases the complexity and cost of doing business.

Recommended actions for the Government of Kenya are:

- Prioritise the revision and passing of the Business Regulation Bill, Statutory Instruments Bill (RIA legislation) and various new companies’ legislation e.g. Companies Bill, Insolvency Bill, Partnerships Bill that seek to coordinate and reduce the red tape in doing business.
- Drive the wholesale replacement of various local level business permits with a Single Business Permit.

Recommended actions for development partners are:

- Undertake a study to evaluate the impact of local ownership requirements in relevant industries; and share information on the global experience of indigenisation policies.

4.1.6. Improve the National Logistics System

A poorly developed and maintained national logistics system increases the cost of doing business, diminishes a natural advantage in the region as a central trade hub, and impinges on Kenyan business’ ability to maximise EAC common market opportunities.

Recommended actions for the Government of Kenya are:

- Drive continuous improvement in the Single National Window to harmonise ministry processes and create electronic systems in import/export; and ports efficiency and goods clearance procedures.
- Accelerate the replication of the Malaba border pilot one-stop goods clearance programme.
- Drive the removal of all remaining non-tariff barriers (NTBs) with the EAC e.g. cumbersome weigh-bridge processes and police road blocks.

Recommended actions for development partners are:
• Continue supporting ongoing improvement in the Single National Window to harmonise ministry processes and create electronic systems in import/export; and ports efficiency and goods clearance procedures.
• Assist by financing the systematic roll-out of one-stop goods clearance border posts.

4.2. Understanding the Informal Sector; Linking MSEs with Bigger Business

4.2.1. Define, Understand and Address the Large Informal Sector

Large-scale informal sector activity leaves families without formal protection from job loss, ill-health and natural calamity, creates a drag on productivity and growth, and erodes the functioning and legitimacy of market- and equity-enhancing institutions. Furthermore, a large informal sector presents an overly large burden on the formal sector by unfairly reducing the tax base.

A poor understanding of the informal sector limits the ability of government to design and implement appropriate and effective policies.

Recommended actions for the Government of Kenya are:
• Clearly define what constitutes formal and informal enterprise in Kenyan terms.
• Support the Kenyan National Bureau of Statistics’ (KNBS) planned implementation of an MSE survey.
• Implement the MSE Act, ensuring that those responsible for its implementation have the necessary authority and resources. Create a clear avenue for informal enterprises to register with the proposed MSE Registrar so that such enterprises can formalise and access business development benefits afforded to formal MSEs.

Recommended actions for development partners are:
• Support KNBS in going beyond enumeration in its upcoming MSE survey, explicitly seeking to understand the drivers of informality in Kenya and the barriers to small business of becoming formal.
• Support the successful implementation of the MSE Act by sharing global best practice in targeted government support for MSEs.

4.2.2. Create Programmes to Link MSEs with Government Business and Large Private Sector Business

A bifurcated private sector with poor links between major buyers (government and large business) and suppliers (MSEs) means lower and less inclusive private sector growth.

Recommended actions for the Government of Kenya are:
• Provide government support to corporate business linkage efforts by better directing government finance and business development services to MSEs that are actively competing for or executing corporate business.
• Design and implement a programme to support government’s intent to procure 25% of goods and services from MSEs, without compromising value for money, independence of procurement decisions and eroding local content.

Recommended actions for development partners are:
• Understand barriers to successful business linkages by assessing and sharing the experience, or consolidating the assessed experience, of donor linkage initiatives (e.g. USAID, UNIDO SPX and DANIDA) and existing/historical corporate linkage initiatives (e.g. GM, EABL, Unilever and KTDA).
• Support government and business associations (BMOs) to develop effective business linkage programmes.
• Commission an evaluation of the funding and operating

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4 World Bank, 2007. The Informal Sector: What Is It, Why Do We Care, and How Do We Measure It?
model of existing government-led business development agencies (e.g. Kenya Institute of Business Training and the Productivity Centre of Kenya) to improve their effectiveness.

Recommended actions for the private sector are:

- Commit to tangible plans (e.g. design and fund business linkage programmes) and targets to create and grow business linkages with MSEs.
- Business associations (BMOs) to provide members with best practice tools and knowledge in developing business linkages.
- Adopt a Financial Sector Charter to encourage formal lending institutions to improve access to financial services for MSEs, building on the work of Financial Sector Deepening (FSD) Kenya.

4.3. Manage Impact of Devolved Government and the Constitution

4.3.1. Foster Business Confidence Around the Impact of Devolved Government

Uncertainty around the implementation of the highly complex devolution process may result in a slowing of private sector investment as investors take a “wait and see” approach. To mitigate this risk and maximise a positive outcome, recommended actions revolve around supporting government entities charged with the implementation of devolution:

Recommended actions for the Government of Kenya are:

- Deliver a systematic campaign to educate county politicians and government officials on key areas of potential weakness or controversy e.g. county cooperation in provision of services; local revenue raising; rural vs urban spending; and business regulation.
- Create a forum for communication of upcoming business opportunities to the private sector in order for business to prepare and compete fairly at a county-level. This should be closely monitored, for example through a transparent database that lists contracts awarded.
- Assure effective implementation of anti-corruption efforts at the county level, for example, produce a transparent database that lists contracts awarded.

Recommended actions for development partners are:

- Assist government with developing materials and designing a systematic campaign to educate county politicians and government officials on the importance of:
  - County cooperation in crucial economic development initiatives that transcend county boundaries and achieving economies of scale in county services;
  - Being guided by business-sensitive principles in the levying of county taxes, user charges and license fees;
  - Avoiding a rural allocation bias that fails to stimulate and support sustainable private sector growth i.e. low recognition of the benefits to agglomeration;
  - Avoiding a ‘Balkanisation’ of the business environment through variable rules and procedures, adding complexity and cost to doing business, by ensuring regulatory rigour and consistency across national and county government – as well as policy making that is based on due assessment of costs and benefits, intended and unintended.

Recommended actions for the private sector are:

- Work together with development partners to initiate and maintain an equivalent “Doing Business” ranking of counties and recognise top achievers.

4.3.2. Support Implementing the Constitution

Adherence to the letter and spirit of the Constitution may be constrained by the ingrained behaviour in politicians
and public servants, and in the manner that constitu-
tional provisions are interpreted and translated into law. For
example, the Constitution stipulates that a body corporate
only be classed as a citizen if its entire shareholding is held by Kenyans, while land ownership is to be restricted to Kenyan citizens. This may have unintended consequences for instance negatively influencing investment flows and the transparency of shareholdings.

Recommended actions for development partners are:

- Commission a study on the likelihood of unintended negative consequences pertaining to constitutional provisions, especially those restricting landholding and what measures could be taken to mitigate them.
- Build up the capacity and strength of key Constitution-supporting entities, such as the Public Procurement Oversight Authority, Ethics and Anti-Corruption Commission and Land Commission.

Recommended actions for private sector are:

- Create a private sector-funded legal “war chest” for business associations to defend the Constitution in the Constitutional Court in test cases, and hold officials and politicians to account.

4.4. Public-Private Cooperation and Dialogue

4.4.1. Streamline Public and Private Sector Interaction and Hasten Decision-Making and Action

Inefficient interaction, unnecessary bureaucracy and red tape increases transaction costs for both the public and private sector. Fragmentation of private sector representation also results in partial representation of the private sector in policy discussions.

Recommended actions for the Government of Kenya are:

- Drive continuous improvement in the functioning of Sector Working Groups; revise and refresh the Prime Minister’s Roundtable in the context of the new government structures.
- Strengthen and maintain momentum on performance-based contracting and rapid results initiatives in the public service.
- Continue and update the Private Sector Development Strategy (PSDS), but restructure the implementation for better results:
  - Increase both the profile of the PSDS Secretariat and strategy, providing the PSDS’ institutional home and leadership with the necessary authority.
  - Build capacity of, and secure strong leadership that is proactive and attuned to the private sector.
  - Ensure that PSDS activities are relevant to, and within the control of PSDS Goal Managers; followed by deep integration of the PSDS activities with those of the Goal Managers.
  - Simplify complex management structures and clearly prioritise activities.
  - Establish and implement a monitoring and evaluation framework to effectively track progress and inform future implementation revisions.

Recommended actions for development partners are:

- Provide technical assistance to support the execution of the planned consolidation of ministries and public entities (e.g. entities listed in the Agriculture, Livestock and Food Authority (ALFA) Act; all investment climate entities; various ministries’ “MSE desks”).
- Assist business associations to increase capacity for more strategic and focused interaction with government and to deliver value-adding member services, e.g. DANNIDA support to KEPSA.
• Provide funding support for the implementation of the PSDS (particularly for monitoring and evaluation).

Recommended actions for the private sector are:

• Drive continuous improvement in the functioning of Sector Working Groups; revise and refresh the Prime Minister’s Roundtable in the context of the new government structures and consider establishing county-level roundtables
• Ensure broader representation of business associations (BMOs) in public-private dialogue.
• Facilitate the creation of a public-private sector platform to resolve ongoing issues around VAT refunds and the tax burden (taxes and fees additional to company income tax).
• Rationalise and improve MSE representation through the mechanisms of the MSE Act.

4.5. Sector Growth and Competitiveness

4.5.1. Improve Competitiveness, Increase Value Addition and Export Diversification

In order to improve Kenya’s trade balance, drive sustainable economic growth and create a level playing field, certain general actions should be taken across the Kenyan private sector (note- this is not a sector specific study, thus detailed sector recommendations have not been included).

Recommended actions for the Government of Kenya are:

• The Competition Authority of Kenya to investigate and resolve potential competition problems, prioritising major input sectors and those sectors with strong linkages to other sectors. Industries for possible review include: cement, trucking, banking, petroleum, beer, maize, fertilizer, sugar, pay TV, and domestic air passenger transport.

Recommended actions for development partners are:

• Provide focused support to increase value addition, especially in agribusiness (e.g. UNIDO standards and market access programme).

4.5.2. Effectively Manage “Budding Sectors”

The discovery of oil in the Lake Turkana region, if managed well, could play a massive transformation role in the Kenyan economy, accelerating the growth trajectory of the private sector and providing a boost to the fiscus. If handled poorly it may bring the attendant problems of “Dutch disease” and escalate the extent and magnitude of corrupt activity. Deliberate and careful thought and action is needed to promote sustainable, shared benefit from oil extraction, distribution and refining, including transparency and stewardship.

The construction and real estate sector is expected to grow steadily boosted by government’s increased spending on infrastructural development and Kenya’s rapid urbanisation. However, the sector is faced by regulation and supervision challenges, including quality assurance and the lack of a reliable title registry.

Recommended actions for the Government of Kenya are:

• Sign the global Extractive Industries Transparency Initiative (EITI); and create and strengthen government institutions tasked with managing oil resources and revenues in highly transparent manner.
• Remove key construction bottlenecks, for example, reducing delays in property transactions by reforming and digitising the title registry and increasing capacity at land registry offices to speed up land valuations and processing capability.

Recommended actions for development partners are:

• Provide technical assistance to those government institutions tasked with managing oil resources and revenues; and global best practice policies and strategies to mitigate the possible ill-effects of a resource boom.
• Support the design and implementation of market linkage programmes between oil companies and local MSEs.
• Provide capacity building support to local government agencies responsible for development planning, building approvals and construction supervision, especially in view of the new county dispensation.

Recommended actions for the private sector are:

• Demand government participation in the global Extractive Industries Transparency Initiative (EITI).
• Relevant industry bodies to commit to stronger industry self-regulation measures in construction.

4.6. Improving Economic Data

4.6.1. Generate Comprehensive and Consistent National Economic Data on Private Sector Output and Investment

While KNBS collects comprehensive national statistics, there are gaps that make it difficult to fully understand the private sector and therefore to design evidenced-based policy-making around private sector development and the best allocation of public resources, good private sector development policy. There are data gaps for two of Kenya's most important sectors, tourism and ICT, as well as very limited information on the informal sector. There is also contradictory data on levels of foreign direct investment.

Recommended actions for the Government of Kenya are:

• Provide KNBS with the necessary financial and human resources to modernise and streamline data collection methodologies and statistical accounts, to capture comprehensive tourism data (e.g. create Tourism Satellite Accounts), disaggregate Transport and Communications data, and improve the veracity and granularity of FDI data.
• Coordinate data collection efforts of KNBS, Central Bank of Kenya, the ICT Board, KenInvest, the proposed MSE Registrar and the Ministry of Tourism and Ministry of Planning to assure complementarity and address data discrepancies.

Recommended actions for development partners are:

• Provide KNBS with technical assistance to modernise and streamline data collection methodologies and statistical accounts (e.g. create Tourism Satellite Accounts) and advise KNBS on global best practice in managing data collection efforts of multiple government agencies.
• Commission a study to fully understand the state and nature of MSEs and the informal sector, as well as barriers to formalisation (see earlier recommendation on KNBS MSE survey).

5 The FDI values obtained from World Bank data differ from those made available by KNBS (Foreign Investment Survey, 2011) and also from those obtained from KenInvest Computations (which estimate substantially higher FDI inflows, based on investment approvals as opposed to actual investments).
5. Matrix of priority recommendations

Given the large number of aforementioned recommendations, a priority list would look as follows. This is based on a rough estimation of the degree of impact on private sector development and extent to which these recommendations are achievable in the next 18 months.

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>Government of Kenya</th>
<th>Development Partners</th>
<th>Private Sector</th>
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<tbody>
<tr>
<td>Eliminate corruption and political patronage in government decision making</td>
<td>Fast-track the computerisation of government processes (relating for example to fees, tax and procurement) to increase transparency and close avenues for corrupt behaviour. Fully implement the existing ethics policy and strengthen other policies on declaring interests transparently and managing conflicts of interest in relation to politician/public servant participation in business.</td>
<td>Provide strategic support in the form of technical capability and systems capacity building to the Public Procurement Oversight Authority, Ethics and Anti-Corruption Commission and Land Commission. Share global best practice on policies and associated implementation around declaring interests transparently and managing conflicts of interest in relation to politician/public servant participation in business; and whistle-blower protection mechanisms.</td>
<td>Finalise, activate and monitor adherence with the Kenyan Private Sector Alliance (KEPSA)-led private sector Code of Conduct, to tackle private sector participation in corrupt behaviour. Create and support a non-aligned private sector-funded non-governmental organisation (NGO) “Corruption Watch” entity, which has the resources to investigate and publish instances of both private and public sector corruption.</td>
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<td>Accelerate investment in critical, enabling infrastructure</td>
<td>Accelerate implementation of infrastructure plans by activating public-private partnerships (PPPs), ideally starting with small/medium-sized projects to build experience and confidence. Proactively improve understanding within government of the benefits of PPPs, and a clear understanding of their complexity, long-term nature and cost and risk implications.</td>
<td>Build government capacity to initialise and manage public-private partnerships (PPPs), including the structuring and negotiating of deals, ideally starting with small/medium-sized projects to build experience and confidence. Codify and share with government and the private sector the benefits of PPPs, as well as their complexity, long-term nature and cost and risk implications.</td>
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<td>Investigate and remediate anti-competitive behaviour</td>
<td>Instruct the Competition Authority of Kenya (CAK) to investigate and resolve potential competition problems in a timely fashion, pursuant of major input sectors and those sectors with strong linkages to multiple sectors. Industries for possible review include: cement, trucking, petroleum, beer, maize, fertilizer, sugar, pay TV, and domestic air passenger transport. Commission an assessment of the role of marketing boards, with a view to remove bottlenecks and address instances of market failure, for example, in pyrethrum, coffee, cereals and produce. Provide strategic capacity building and support to ensure that the CAK executes investigations and market enquiries with minimum political interference and maximum cooperation.</td>
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<td>Foster a business-friendly regulatory environment</td>
<td>Prioritise the revision and passing of the Business Regulation Bill, Statutory Instruments Bill (RIA legislation) and various new companies’ legislation e.g. Companies Bill, Insolvency Bill, Partnerships Bill that seek to co-ordinate and reduce the red tape in doing business. Drive the wholesale replacement of various local level business permits with a Single Business Permit. Undertake a study to evaluate the impact of local ownership requirements in relevant industries; and share information on the global experience of indigenisation policies.</td>
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<td>Improve the national logistics system</td>
<td>Accelerate the replication of the Malaba border pilot one-stop goods clearance programme. Drive the removal of all remaining non-tariff barriers (NTBs) with the EAC e.g. cumbersome weigh-bridge processes and police road blocks. Continue supporting on-going improvement in the Single National Window to harmonise ministry processes and create electronic systems in import/export; and ports efficiency and goods clearance procedures. Assist by financing the systematic roll-out of one-stop goods clearance border posts.</td>
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<td>Recommendation</td>
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<td>Define, understand and address the large informal sector</td>
<td>Clearly define what constitutes formal and informal enterprise in Kenyan terms.</td>
<td>Support KNBS in going beyond enumeration in its upcoming MSE survey, explicitly seeking to understand the drivers of informality in Kenya and the barriers to small business of becoming formal.</td>
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<td>Support the Kenyan National Bureau of Statistics’ (KNBS) planned implementation of an MSE survey.</td>
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<td>Create programmes to link MSEs with government business and large private sector business</td>
<td>Provide government support to corporate business linkage efforts by better directing government finance and business development services to MSEs that are actively competing for or executing corporate business. Design and implement a programme to support government’s intent to procure 25% of goods and services from MSEs, without compromising value for money, independence of procurement decisions and eroding local content.</td>
<td>Understand barriers to successful business linkages by assessing and sharing the experience, or consolidating the assessed experience, of donor linkage initiatives (e.g. USAID, UNIDO SPX and DANIDA) and existing/historical corporate linkage initiatives (e.g. GM, EABL, Unilever and KTDA). Support government and business associations (BMOs) to develop effective business linkage programmes.</td>
<td>Commit to tangible plans (e.g. design and fund business linkage programmes) and targets to create and grow business linkages with MSEs. Business associations (BMOs) to provide members with best practice tools and knowledge in developing business linkages. Adopt a Financial Sector Charter to encourage formal lending institutions to improve access to financial services for MSEs, building on the work of Financial Sector Deepening (FSD) Kenya.</td>
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<td>Generate comprehensive and consistent national economic data on private sector output and investment</td>
<td>Provide KNBS with the necessary financial and human resources to modernise and streamline data collection methodologies and statistical accounts, to capture comprehensive tourism data (e.g. create Tourism Satellite Accounts), disaggregate Transport and Communications data, and improve the veracity and granularity of FDI data.</td>
<td>Provide KNBS with technical assistance to modernise and streamline data collection methodologies and statistical accounts (e.g. create Tourism Satellite Accounts) and advise KNBS on global best practice in managing data collection efforts of multiple government agencies.</td>
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