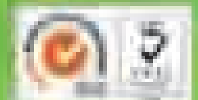
Transformative Institutions for delivering Kenya Vision 2030

KENYA ECONOMIC REPORT 2011

KENYA INSTITUTE FOR PUBLIC POLICY RESEARCH AND ANALYSIS



Kenya Economic Report 2011

Transformative Institutions for Delivering Kenya Vision 2030

Nairobi, Kenya
2011

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ISBN 9966 777 93 8

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Foreword

The Kenya Economic Report 2011 is prepared by the Kenya Institute for Public Policy Research and Analysis (KIPPRA) pursuant to the KIPPRA Act No. 15 of 2006. This report analyses economic developments in Kenya in 2010/11 and provides medium-term prospects for the next three years. The report aims at deepening understanding of the underlying factors affecting Kenya's economic performance and the prospects thereof. It provides critical input and contribution to economic policy debate as well as prescriptions aimed at informing the design and formulation of the national development agenda. This report comes at a critical juncture as the country steadily pursues implementation of the Constitution of Kenya 2010 promulgated on 4 August 2010 and proclaimed on 27 August 2010 as the supreme law of the land.

In 2010, the Kenyan economy grew by about 5.6 per cent. This reflects a strong recovery relative to the growth of 2.6 per cent recorded in 2009. However, due to shocks including drought, high international oil prices and a slowdown in the global economy, growth is expected to slow down to about 4.5 per cent in 2011. This performance remains below the medium-term plan targets.

In order to realize its medium-term development targets, there is need to achieve coherence and focus in the execution of programmes and projects, especially the Vision 2030 flagship projects. Implementation of the Constitution of Kenya 2010 provides an opportunity of institutionalizing rule of law, respect of property rights, removing inhibiting formal and informal constraints to doing business, and generally engendering predictability and certainty in the formulation and implementation of social and economic development policy.

The theme of the Kenya Economic Report (KER) 2011, *Transformative Institutions for Delivering Vision 2030*, recognizes the fact that as the country engages in the massive social re-engineering scheme that is the national development agenda, benefits will be measured by how effectively it supports improvements in the welfare of citizens at all levels.

As the country goes where the eagles dare, it will be important to focus on implementation of the Constitution of Kenya 2010 in a manner that ensures equitable sharing of the national cake and baking a larger and more nutritious cake to be shared. It is critical to recognize that the imperatives of growth will remain the same. Macroeconomic stability will have to be jealously preserved, while at the same time ensuring that a business and investment climate attractive to both domestic and foreign investors is created. The national government and county governments must be configured in a manner that allows them to effectively respond to the mandates

of the Constitution of Kenya 2010, the high expectations of the citizenry as well as the imperatives of effective management of public resources. A key issue that must be addressed in the design and reform of existing institutions should be the focus on dealing with the 'deficit of trust' that could easily contribute to raising transaction costs and limit the ability of the country to respond to a rapidly evolving domestic, regional and global environment. This has potentially adverse implications for the cost of government and ultimately the competitiveness of Kenya as an investment destination. Another concern will be the imperative of engendering cordial and consultative relations between the national government and county governments at all levels. These matters will require a targeted and sustained effort to build the capacity of the national government and county governments. Capacity requirements will be determined by a clear understanding and conceptualization of the assignment of functions between the two levels of government. In this regard, the structuring and organization of government as implementation of the Constitution of Kenya 2010 gathers pace should be seen as a means through which Kenya is able to rid itself of conflicts in mandates, with a clear goal of building and sustaining technical and operational competency. One of the greatest anxieties of business is that county governments might become a bastion of rent-seeking activity, and they will not be able to attract the level of skills required for them to deliver on their constitutional mandates. This concern must be faced and dealt with firmly through adoption of facilitative policy, legal and regulatory arrangements.

Hon. Wycliffe Ambetsa Oparanya, EGH, MP
Minister of State for Planning, National Development and Vision 2030

Preface

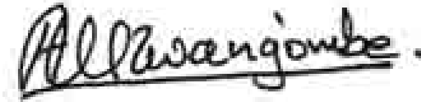
The Kenya Economic Report (KER) 2011 is the third in a series of annual reports on the Kenyan economy prepared by the Kenya Institute for Public Policy Research and Analysis (KIPPRA) pursuant to the KIPPRA Act No. 15 of 2006. The report is prepared in consultation with the Ministry of State for Planning, National Development and Vision 2030; Ministry of Finance; and the Central Bank of Kenya.

Improvements in Kenya's economic outlook in 2010 need to be looked at in the context of looming dangers arising from rising global energy prices, food security challenges, and a burgeoning current account balance. These circumstances will have implications on not only the ability to achieve Vision 2030 targets but also the effectiveness with which to implement the Constitution. Part I of KER 2011 provides an analysis of the macroeconomic and socio-economic performance of the country and provides policy recommendations aimed at enhancing economic growth and reducing poverty. Part II reviews sectoral performance and makes recommendations for changes in light of the ongoing constitutional and administrative reforms. It looks at the medium-term prospects of the various sectors and makes recommendations for reforms to ensure that these prospects are achievable. Part III discusses the transformative institutions for delivering Vision 2030. It benchmarks Kenya's institutions in the context of Kenya's development imperatives and the need to pursue smart and inclusive growth, while pursuing global competitiveness. It selectively reviews macroeconomic management, human resource development, and tourism, and reflects on the institutional change imperatives. Part IV focuses on conclusions and makes broad recommendations on the goals and mechanics of institutional reform in Kenya, which will ensure achievement of smart, inclusive and broad-based growth as envisioned by the Constitution of Kenya 2010.

The overall message of the Kenya Economic Report 2011 is that the Constitution of Kenya 2010 is pregnant with promise, but fraught with challenges. It provides a golden opportunity to deal with the 'deficit of trust' that pervades our existing institutional and organizational structures. In the promise lies the opportunity to redesign and reform institutions to be more responsive to the country's aspirations. It is a major building block in the long-desired effort of securing a prosperous nation, at peace

with itself and with the world. The efforts of rebuilding the institutions must not lose sight of the fact that we still must grow our economy, even as we share. This means that we must build and nurture those development agents who will facilitate investment and growth. It will be important that a sharp focus on reducing the cost of doing business is maintained by both the national government and county governments.

Dr. Eric A. Aligula
Ag. Executive Director
KIPPRA



Prof. Agnes W. Mwang'ombe
Chair, Board of Directors
KIPPRA

Acknowledgments

This Kenya Economic Report 2011 has been prepared by the staff of the Kenya Institute for Public Policy Research and Analysis (KIPPRA). The work was undertaken under the overall guidance of the immediate former Executive Director of the Institute, Dr Moses Ikiara and the Acting Executive Director, Dr Eric Aligula. The core team that prepared the report comprised the dedicated staff in all the research divisions comprising Macroeconomics Division, Productive Sector Division, Social Sector Division, Infrastructure and Economic Services Division, Trade and Foreign Policy Division, and Governance Division. The advisory team comprised Dr John Omiti, Dr Dickson Khainga, Prof Joseph Kieyah and Mrs Eldah Onsomu.

In accordance with the KIPPRA Act No. 15 of 2006, there was consultation with the Office of the Prime Minister, Ministry of State for Planning, National Development and Vision 2030, Ministry of Finance and the Central Bank of Kenya who provided critical comment and support. We acknowledge, with thanks, the support from these institutions and their continued collaboration in the development process.

The Kenya Economic Report 2011 benefitted from many useful comments and suggestions received from the KIPPRA Board of Directors. KIPPRA Associates, including Prof Michael Chege and Prof Germano Mwabu were also instrumental in shaping this report.

We remain grateful to the KIPPRA editorial production team in the Knowledge Management and Communications Division, the Finance and Investment team as well as the Human Resources and Administration team, without whom this work would have been much harder to realize.

Further, KIPPRA acknowledges, with thanks, the generous financial support received from the Government of Kenya, the African Capacity Building Foundation and the Think Tank Initiative of IDRC.

To all of you, thank you, and we look forward to your continued engagement and support as we continue together and separately to lay the building blocks for a healthy, strong and prosperous Kenya.

God Bless You All.

Abbreviations and Acronyms

ACFCI	Assembly of French Chambers of Commerce and Industry
ADC	Agricultural Development Corporation
AFC	Agricultural Finance Corporation
AfDB	African Development Bank
AFIT	The French Agency for Tourism Engineering
A-I-A	Appropriations-in-Aid
AIBK	Association of Insurance Brokers of Kenya
AKI	Association of Kenya Insurers
AMR	Adult Mortality Rate
APRM	African Peer Review Mechanism
ARI	Agricultural Research Intensity
ASALs	Arid and Semi Arid Lands
BICs	Business Information Centres
BMI	Business Monitor International
BoK	Bomas of Kenya
BPAP	Business Process Association of the Philippines
BPO	Business Process Outsourcing
BRRU	Business Regulatory Reforms Unit
CBK	Central Bank of Kenya
CBR	Central Bank Rate
CCA	Controller of Certifying Authorities
CCK	Communications Commission of Kenya
CDF	Constituency Development Funds
CIGs	Common Interest Groups
CIPRO	Companies and Intellectual Property Registration Office
CMA	Capital Markets Authority
CMP	Common Market Protocol
CoK	Constitution of Kenya
COMESA	Common Market for Eastern and and Southern Africa
CPD	Continuing Professional Development
CPIA	Country Policy and Institutional Assessment
CPR	Contraceptive Prevalence Rate
CRA	Commission on Revenue Allocation
CTDLT	Catering and Tourism Development Levy Trustees
DAT	Directorate of Applied Technology
DFCK	Development Finance Company of Kenya
DFZ	Disease Free Zoning
DIT	Department of Information Technology

DJLB	District Joint Loans Boards
DTM	Deposit Taking Microfinances
EAC	East African Community
ECS	Electronic and Computer Software
EEC	European Economic Community
EFT	Electronic Funds Transfers
EMCA	Environmental Management and Coordination Act
EPAs	Economic Partnership Agreements
EPC	Export Promotion Council
EPZA	Export Processing Zones Authority
ESP	Economic Stimulus Programme
EU	European Union
FCB	First Community Bank
FDI	Foreign Direct Investment
FP	Family Planning
FRS	Famine Relief Stocks
GCI	Global Competitiveness Index
GDP	Gross Domestic Product
GPI	Gender Inequality Index
GWCs	General Waste Collectors
HRA	Hotel and Restaurants Authority
HRH	Human Resource for Health
IATA	International Air Transport Association
ICASA	Independent Communications Authority of South Africa
ICDC	Industrial and Commercial Development Corporation
ICPD	International Conference on Population and Development
ICT	Information, Communication and Technology
IDA	International Development Association
IDB	Industrial Development Bank
IDB	International Data Base
IFMIS	Integrated Financial Management Information System
IFPRI	International Food Policy Research Institute
ILRI	International Livestock Research Institute
IMCI	Integrated Management of Childhood Illness
IMR	Infant Mortality Rate
IPOs	Initial Public Offers
IRA	Insurance Regulatory Authority
ISPs	Internet Service Providers
IST	In-Service Training
IT	Information Technology
ITIDA	Information Technology Industry Development Agency
JLB	Joint Loans Board
KAAO	Kenya Association of Air Operators
KAHC	Kenya Association of Hotelkeepers and Caterers
KATA	Kenya Association of Travel Agents
KATO	Kenya Association of Tour Operators
KBPOCCS	Kenya Business Process Outsourcing and Contact Centre Society
KDB	Kenya Dairy Board
KENAO	Kenya National Audit Office
KEPSA	Kenya Private Sector Alliance
KEPSS	Kenya Electronic Payment and Settlement System
KFA	Kenya Farmers Association
KFMP	Kenya Forestry Master Plan
KIBT	Kenya Institute of Business Training
KICC	Kenyatta International Conference Centre
KIE	Kenya Industrial Estates
KLBO	Kenya Livestock Breeders Organization
KMC	Kenya Meat Commission
KNBS	Kenya National Bureau of Statistics
KNTC	Kenya National Trading Corporation
KSC	Kenya Seed Company
KTB	Kenya Tourist Board
KTDC	Kenya Tourist Development Corporation
KTF	Kenya Tourism Federation
KTMM	KIPPRA-Treasury Macro Model
KUC	Kenya Utalii College
KWS	Kenya Wildlife Service

MCIT	Ministry of Communication and Information Technology
MDeC	Multimedia Development Corporation
MDGs	Millennium Development Goals
MEMR	Ministry of Environment and Mineral Resources
MFIs	Micro Financial Institutions
MICE	Meetings, Incentives, Conferences and Exhibition
MIPs	Medical Insurance Providers
MMR	Maternal Mortality Rate
MoE	Ministry of Education
MoHEST	Ministry of Higher Education, Science and Technology
MPER	Ministerial Public Expenditure Review Report
MRTTAT	Ministry of Research, Technical Training and Applied Technology
MSC	Multimedia Super Corridor
MSEP	Micro and Small Enterprises Programme
MSMEs	Micro, Small and Medium Enterprises
MTEF	Medium Term Expenditure Framework
MTEP	Medium Term Expenditure Plan
MTP	Medium Term Plan
NAAIAP	National Accelerated Agriculture Input Access Programme
NALEP	National Agriculture Livestock Extension Programme
NASEP Policy	National Agricultural Sector Extension
NASI	Nairobi All Share Index
NASSCOM	National Association of Software and Services Companies
NCAPD	National Coordinating Agency on Population and Development
NCCRS	National Climate Change Response Strategy
NCCU	National Contact Centre Union
NCPB	National Cereals and Produce Board
NCPD	National Council for Population and Development
NCSE	National Council for Small Enterprises
NESC	National Economic and Social Council
NGO	Non-Governmental Organization
NKCC	New Kenya Cooperative Creameries
NPLs	Non-Performing Loans
NPPSD	National Population Policy for Sustainable Development
NRP	National waste Recycling Programme
NSE	Nairobi Stock Exchange
NSSF	National Social Security Fund
NTRA	National Telecommunication Regulatory Authority
PBGs	Producer Business Groups
PCK	Productivity Centre of Kenya
PEFA	Public Expenditure and Financial Accountability Assessment Framework
PEM	Public Expenditure Management
PER	Public Expenditure Review
PO	Public Offer
PPP	Public-Private Partnership
PST	Pre-Service Training
PWCs	Public Waste Collectors
R&D	Research and Development
RBA	Retirement Benefits Authority
RH	Reproductive Health
RTGS	Real Time Gross Settlement
SACCOs	Savings and Credit Cooperative Societies
SAFEX	South African Futures Exchange
SASRA	Sacco Societies Regulatory Authority
SBKenya	Stud Book (K)
SCAC	State Corporations Advisory Committee
SEZ	Special Economic Zones
SGR	Strategic Grain Reserves
SA	South Africa
SSA	Sub-Sahara Africa
STABEX	Stabilization of Export Earnings
STEs	State Trading Enterprises
STF	Skills Task Force
T&T	Travel and Tourism
TEAMS	The East African Marine System
TEUs	Twenty-foot Equivalent Units

TNA	Training Needs Assessment
TOE	Tonnes of Oil Equivalent
TSVs	Tourist Service Vehicles
TTCI	Travel and Tourism Competitiveness Index
TTF	Tourism Trust Fund
UAE	United Arab Emirates
UMR	Under-5 Mortality Rate
UNDP	United Nations Development Programme
URA	Urban Redevelopment Authority
WEF	World Economic Forum
WRMA	Water Resources Management Authority
WSBs	Water Service Boards
WSRB	Water Services Regulatory Board
YEDF	Youth Enterprise Development Fund

Executive Summary

Macroeconomic Performance

The Kenyan economy grew by 5.6 per cent in 2010, representing a marked improvement from the 2.6 per cent and 1.6 per cent growth rates recorded in 2009 and 2008, respectively. The registered growth indicates that by 2010, the economy was on a steady path to full recovery following subdued growth in 2008/09 due to the post-election violence, drought, global financial crisis, and high international oil and food prices. Various factors explain the improved economic performance recorded in 2010. Firstly, the weather conditions were favourable, which contributed to improved agricultural output. Secondly, the effects of the economic stimulus package started to take effect across the various sectors of the economy. Apart from the fiscal stimulus of about Ksh 22 billion, the Central Bank of Kenya sustained monetary policy support by consistently reducing the Central Bank rate in 2010. Thirdly, improved liquidity in the economy, prudent macroeconomic management and recovery in the global economy contributed to better economic outlook in 2010.

At the sectoral level, there was improved growth from all sectors of the economy in 2010. Financial intermediation recorded a growth of 8.8 per cent in 2010, up from 4.6 and 2.7 per cent in 2009 and 2008, respectively. Agriculture recorded improved growth by 6.3 per cent in 2010 compared to the corresponding period in 2009. The tourism sector rebounded from the effects of the post-election violence with an impressive growth of 17.9 per cent. The manufacturing sector, on the other hand, grew by 4.4 per cent in 2010 compared to a growth of 1.3 per cent in 2009, boosted by improved electricity and water supply, and recovery in the agricultural sector that supported agro-based industries. Electricity and water sub-sectors grew by 9.9 per cent in 2010. The share of industry in total Gross Domestic Product (GDP) stood at 17.4 per cent, with mining and quarrying at 0.7 per cent, manufacturing at 10 per cent, and the construction industry at 4.3 per cent. The service sector had the highest contribution to GDP of about 48.07 per cent, with wholesale and retail trade having 10.3 per cent share in total GDP, hotels and restaurants 1.7 per cent, transport and communications 9.8 per cent, and financial intermediation 5.6 per cent.

Real GDP per capita increased from Ksh 35,470 in 2009 to Ksh 36,419 in 2010 after a slight slowdown in 2008 and 2009, following the 2008 shocks (post-election violence, global financial crisis and drought). Going into 2011, GDP growth is expected to slow down due to high oil prices and slow global economic recovery. With the dim projection of GDP for the year 2011, real GDP per capita is also expected to slow down.

The key objective of monetary policy in Kenya is to ensure price stability. Vision 2030 envisages a monetary policy that will achieve less than 5 per cent, annual inflation rate. However, the rate of inflation has remained above the target of 5 per cent except during 2002, 2007 and 2010. Inflation declined from 9.2 per cent in 2009 to 4.1 per cent in 2010, largely due to a prudent monetary policy and better agricultural performance. The two most important contributors to overall inflation in Kenya are food and non-alcoholic drinks, and fuel and power prices. Lower income household groups residing in urban centres experienced higher incidence of inflation compared to other groups, since expenditure on food represents a large share of their household expenses estimated at about 48.3 per cent, compared to upper income households that spend only about 10.5 per cent on food.

Supply shocks have played a major role in explaining inflation in Kenya. In addition, poor infrastructure network contributes to escalating agricultural commodity prices due to difficulties in accessing markets. Reliance on rain-fed agriculture makes the country vulnerable to extreme weather conditions. On the demand side, expansionary monetary and fiscal policy poses the challenge of accelerating aggregate demand. There is need to improve wage and productivity in the country; to transform the agricultural sector to produce sufficient affordable food; to expand and utilize national grain stores to provide adequate buffer stock of readily available food in order to create price stability; and to ensure prudent macroeconomic management necessary to support economic stability.

Kenya is facing an increasing investment-savings gap. While investments grew from 17 per cent of GDP in 2005 to 19.3 per cent in 2010, savings declined from 16 per cent in 2008 to 12.2 per cent in 2010. Vision 2030 identifies savings and investments as critical channels through which Kenya can achieve high economic growth prospects that can lead to the attainment of economic development. The promotion of both local and foreign direct investments and savings culture will accelerate the pace of economic growth and development in Kenya. The regulatory environment still remains a hurdle both for local and foreign investments. Effective implementation of the Constitution will lead to the creation of strong institutions, including the Judiciary that is critical in investment dispute resolutions.

One of the major instruments expected to enable the economy achieve macroeconomic stability is fiscal policy. The fiscal strategy outlined in Vision 2030 and in the Medium Term Plan 2008-2012 envisages overall fiscal deficit to decline from 5.2 per cent of GDP in 2007/08 to 3.6 per cent of GDP in 2012/13. The overall fiscal deficit was 7.04 per cent of GDP in 2009/2010. Kenya has undertaken fiscal policy measures to mitigate the adverse effects of both domestic (e.g. drought) and external (high oil and fertilizer prices, the global economic downturn) shocks that the economy experienced between 2008 and 2010.

Tax revenues have maintained a consistently upward trend over the 2005/06–2009/10 period, with tax revenues almost doubling from Ksh 256 billion to Ksh 476 billion. This trend is consistent with the policy shift by the government to enhance local capacity to finance the budget and depend less on external borrowing. The ratio of domestic debt to GDP still remains higher than the MTP target of a domestic debt of 21-22 per cent of GDP. Comparing globally, the country's external debt stock (at 26.6% of GDP in 2010 or 5.03% of exports of goods, services and income) is still high and remains an issue of serious policy concern. The current account deficit as a percentage of GDP increased from 5.5 per cent in 2009 to 7.8 per cent in 2010. This is an issue of policy concern in terms of sustainability of the external account.

Economic recovery is expected to continue and remain above the 2008/09 performance. In the medium term, the economy is projected to grow at 4.5 per cent, 5.2 per cent, 5.8 per cent and 6.6 per

cent in 2011, 2012, 2013 and 2014, respectively. In the projections, it is assumed that stability in international oil prices, prudent fiscal and monetary policies and favourable weather conditions are expected to yield single-digit inflation levels of about 7 per cent in the medium term and a stable exchange rate. Overall, it is expected that commitment to reform will remain strong, especially maintaining macroeconomic stability, deepening structural reforms and strengthening key institutions such as the Judiciary and security. This will provide a good background for investor confidence and thus support stability and an improved investment climate.

Strengthening Public Expenditure Management

The implementation of the Constitution of Kenya (CoK) 2010 offers opportunities as well as challenges to the government's reform effort towards strengthening expenditure and macroeconomic management. The CoK 2010 provides a window for reform and establishment of new institutional and governance structures. These have important implications for public expenditure and macroeconomic management in Kenya, including devolution, which leads to creation of county governments, county revenue funds and distribution of functions between the national government and county governments; and principles of public finance enshrined in the Constitution (Chapter 12) including openness and accountability, public participation and equitable development. Establishing appropriate institutions and reforms that support these constitutional principles requires immediate policy attention. Other structures include Equalization Fund, Judiciary Fund, Commission on Revenue Allocation (CRA), Controller of Budget, Salaries and Remuneration Commission and an independent Central Bank of Kenya.

Recent reforms in Public Expenditure Management (PEM) have aimed at enhancing the link between policy planning and budgeting, strengthening transparency and accountability, combating corruption in PEM and improving operational efficiency through introduction of results-based management in the public service. The key reforms include: introduction and strengthening of Medium Term Expenditure Framework (MTEF), introduction of Integrated Financial Management Information System (IFMIS), and strengthening of the legal framework for PEM by enacting relevant legislation such as the Government Financial Management Act 2004, Public Audit Act 2003, Public Procurement and Disposal of Assets Act 2005, and the Fiscal Management Act 2009. Other reforms include establishment of a National Integrated M&E system, and various amendments to the Central Bank Act to enhance operational effectiveness, including the establishment of a Monetary Policy Committee responsible for monetary policy formulation.

Until now, sub-national level participation in the MTEF has been hampered by lack of an appropriate legal framework. Although there have been reforms on the MTEF to enhance outcomes, participation at the sub-national level has been limited. Article 225 provides for the establishment of a national treasury, while Article 220(2) provides for preparation of County Development Plans and the form and manner of consultations between the national government and county governments in the process of preparing plans and budgets. The establishment of a national treasury might also necessitate a review of the current organization of the Ministry of Finance, with a view to aligning the functions to reflect the responsibilities and functions that take into account devolution and establishment of new constitutional offices such as the Commission on Revenue Allocation, and Controller of Budget.

The Fourth Schedule provides the distribution of functions between the national government and county governments. The Constitution introduces new institutions and requires participation of stakeholders. A framework needs to be developed that plainly defines the timetable for budget preparation, clearly indicating the roles of different stakeholders and a framework for participation.

Introduction of devolved governments has the potential of increasing transaction costs and calls for a proper framework of coordination between the 47 county governments. It is important that the design of the devolved public financial management system supports macroeconomic stability.

Population Dynamics and Socio-economic Performance

According to the 2009 Population and Housing Census, Kenya's population was 38.6 million in 2009 with a sex ratio of about 1:1 and an intercensal growth rate of 2.6 per cent. The population distribution shows that 53.6 per cent of the population is aged 15-64 years (constituting the working age population); 43 per cent is aged below 15 years and 3.4 per cent is above 64 years. The population is further projected to increase to 54 million in the year 2030. The country is currently undergoing demographic transition (shift from a high fertility and high mortality equilibrium to a low mortality and fertility equilibrium). Life expectancy in Kenya is on the rise (projected to increase to 68 years by 2050) with decline in HIV prevalence and mortality rates. Birth rates have also declined as a result of late marriage, urbanization, industrialization and other factors that have brought about major demographic transitions.

Thus, as fertility declines and Kenyans live longer, there is likely to be a dramatic improvement in the dependency ratio by 2020. Given these scenarios associated with an upward trend in population, the government, together with various stakeholders, endeavours to manage population growth through several efforts. A draft National Population Policy (2011) has been prepared to guide Kenya's population and development agenda over the next decade.

However, despite various achievements made through programme interventions, several challenges impede effective management of population growth, including: under-funding of reproductive health (RH) and family planning (FP); heavy dependence on the public sector, which places a burden on government and donor revenues; poverty levels that reduce the affordability of contraceptives offered by other agents other than the government; provincial-level inequities in availability of contraceptive methods; lack of equipment and supplies for FP and RH; lack of basic FP services, knowledge and refresher training; stock outs of FP commodities; husbands' disapproval of FP; religious and cultural barriers to FP; prohibitive costs of FP campaigns; and lifestyles that promote risky sexual behaviour among the youth.

The size and quality of a country's labour force can potentially affect economic growth since human capital is a vital component in the production process. Kenya's working-age population (persons aged 15-64 years) was estimated at 19.8 million persons in 2005-2006. In the same period, the labour force participation rate (ratio of total labour force to the working-age population) was 73 per cent. The relatively low overall open unemployment rate of 12.7 per cent in 2005-06 masks high open unemployment rates among the youth, attributed to such factors as skill mismatch and information asymmetries in the labour market. According to annual employment estimates, the number of employed persons increased from 8 million in 2004 to 10.4 million in 2009. Most jobs created annually are in the informal sector, whose share rose steadily to about 80 per cent of all jobs in 2009.

Kenya remains weak in a number of indicators that would greatly undermine creation of formal jobs. These include: perceptions that the total tax rate is high; high number of procedures required to start a business; and high burden of customs procedures. Other areas posing a challenge fall under the ambit of the institutional pillar, including corruption, burden of government regulation, business costs of crime and violence, organized crime, and ethical behaviour of firms. Clearly, expanding formal sector jobs and overall employment creation will require

improvements in these measures of institutional effectiveness.

Poverty has remained a top priority in Kenya's development agenda since independence. It manifests itself through various deprivations and associated low living standards. It is mainly concentrated in the rural areas, where the bulk of the population (75%) resides. According to recent poverty surveys, the poor constitute about 45.9 per cent of the total population. Vision 2030 targets to reduce poverty to a range of between 30 to 35 per cent by 2012. The year 2010 recorded slight improvement in the poverty headcount, attributed to improved economic growth and re-distribution policies, which are linked to various reforms.

Some of the reforms include the implementation of the Constituency Development Fund (CDF), which provides individuals at the grassroots the opportunity to make expenditure choices that maximize their welfare in line with their needs and preferences; introduction of free primary education in 2003; the school feeding programme; the introduction of direct transfer of education funds to schools, and provision of learning materials; and the recently introduced subsidized secondary education for poor families. Moreover, the government also plans to implement other poverty reduction-related reforms, including: land reforms, judicial reforms, public sector reforms, and a social protection framework to provide support to the poor to help them access services and income-generating opportunities.

Health

The health sector is one of the key components of the social pillar of Vision 2030. Good health is recognized as a critical pillar in ensuring individual, household, community and country prosperity. In pursuit of population health, the health sector continues to redirect resources towards preventive and promotive health care, cost effectiveness and efficiency in resource allocation and use, enhancement of public health regulations, strengthening of health institutions and fostering partnerships in health care provision and financing.

Although most health outcome indicators improved during the review period, mortality rates are still below the MDG targets. There have been remarkable declines in under-5 and infant mortality rates after 2005 (from 93 to 74 in 2008 and 85 in 2010, and from 61 to 55 in 2010, respectively). These gains were probably largely due to: increases in immunization rates, increased use of mosquito nets, and positive rate of per capita economic growth. Life expectancy rose to 54 years in 2007, but stagnated there in 2008 due to unfavourable effects of the post-election violence and drought. Regarding burden of disease, nationally, Malaria was the leading cause of death followed by Pneumonia and AIDS.

The key issue that needs to be addressed in the health sector is unsustainable financing, which is characterized by low public spending and high donor dependence. The country is lagging behind in relation to the requirements set by UN MDGs, WHO and the Abuja Declaration for health funding. Much remains to be done to lift the health sector in Kenya to the standards envisioned in Vision 2030. Increased health financing may be addressed through increased government allocations to the health sector up to 15 per cent of GDP (government allocation is 4.3% of GDP); finding new sources of funds – this could be done by encouraging and supporting community health insurance schemes and micro insurance; earmarked funds and taxes going directly to funding the health sector or specific interventions in the health sector such as strengthening public-private partnerships; and promoting corporate social responsibilities targeting the health sector.

Education

Provision and sustainable financing of quality education and training are fundamental in the attainment of the objectives in the Kenya Vision 2030, through development of requisite human

capital. Efforts towards this include substantial expansion of the sector over time. In 2009, for example, there were 38,247 ECDE centres, 26,667 primary schools, 6,971 secondary schools, 105 primary teacher training colleges and 31 universities in the country. In 2007/08, the total education expenditure as a percentage of GDP was 6.2 per cent and 7.4 per cent in 2009/10.

Despite the substantial resources that the government spends on education and training, there are inequalities in access to education at all levels, and low access to post-primary education. Access to post-primary education is low and levels of performance vary across regions, gender and income groups. The marginalized areas and urban informal settlements have low education participation rates, while higher income groups benefit more from post-primary education relative to the low income groups. The Gender Inequality Index, which captures equity across gender in human resource development, shows that the male population is more advantaged relative to their female counterparts.

Key interventions required to improve performance in the education sector include: integrating ICT in learning processes and innovation; enhancing uptake of science and technology disciplines; increasing equity and access for the poor to educational resources and facilities – continuing to implement free primary education and free day secondary education; increasing access to post-primary education (ensuring every Kenyan child has access to basic education and remains in school until they attain the age of 17 years); and improving quality of basic education and effectiveness of management of learning institutions at county level.

Infrastructure and Economic Services

Infrastructure refers to the technical structures that support a society, such as roads, water supply, sewers, power grids and telecommunications. Infrastructure, therefore, facilitates the production of goods and services. The growth of infrastructure lies in having strong institutions, the right policies, increased funding, greater efficiency and a responsible private sector. Inadequate infrastructure can deter foreign investors. Research shows that inadequate public infrastructure tends to drive away foreign investment more so than quality infrastructure attracts private investment. Apart from boosting productivity, modern infrastructure also creates employment opportunities and attracts skilled knowledge workers, increasing the country's growth and competitiveness.

Infrastructure contribution to GDP rose from 21.2 per cent to 21.3 per cent in 2007 to 2010. The sector has been faced with inefficiencies and inadequate resource allocations over the years. However, the government scaled up investments in key infrastructure facilities covering road network, energy supply, transport system and port services in 2010 by allocating Ksh 182 billion, which was 20.1 per cent higher than the amount allocated in 2009/10. Road transport is still the main artery of transport in Kenya and the region. The proportion of Kenya's paved road network was approximately 12 per cent by the year 2011, which is still far below a country such as Egypt (87%).

Maritime transport is critical to Kenya's export-led growth strategy and linking the region to the rest of the world. This mode of transport is, however, faced with many challenges, including high cost of transporting containers within the East African region; congestion at the ports; inadequate container capacity against the high proportion of containerized cargo; and trans-shipment functions that are performing below par. To decongest the port of Mombasa, a new container terminal is under construction, capable of handling 1.2 million twenty-foot equivalent units (TEUs) per annum and is scheduled for completion by 2013.

The total energy consumption increased marginally from 3,627.0 Tonnes of Oil Equivalent (TOE) in 2007 to 4,250.7 TOE in 2010. Among the

outstanding challenges and policy issues in the energy sector include: long and cumbersome procedures and licensing requirements for private investors in alternative and cheaper energy; lack of connectivity to facilitate trade and commerce and expansion of economic opportunities; and limited sources of energy and low affordability of power, resulting in inadequate energy to meet the demand. A critical policy issue is the need to address the volatility in the cost of energy. Although the Energy Regulatory Commission (ERC) has reviewed the current formula for determining electricity tariffs with a view to making movements in the cost of power predictable, this remains a short-term intervention.

While enormous effort and resources have gone into improving the energy sector, there is still significant scope for intervention. Measures to improve the sector include: strengthening regulatory institutions; enhancing private sector participation in the provision of infrastructure and economic services; integrating ICT into the infrastructure resource allocation and management framework; providing a mechanism for sharing information and improving mechanisms for effective citizen participation; cost-reduction measures to address the huge development budget deficit and unmet demand in the energy and housing sub-sectors; embracing cheap renewable energy alternatives that offer decentralized solutions to the spatially-spread rural populations; strengthening the capacity of local research/learning institutions to deliver effectively on low-cost building materials and technologies; and providing incentives and a conducive environment to attract FDI and technology transfer into the sector.

Tourism

Tourism is an important sector of the Kenyan economy and operates within a liberalized economic environment characterized by partnership between the government and the private sector. While the public sector plays an important role in policy implementation and regulation, the private sector is mainly involved in the provision of accommodation, transport and entertainment through ownership and management of hotels, lodges, camp sites and other tourist facilities, tour companies, and travel agents. The sector contributes about 11 per cent of the country's Gross Domestic Product.

Following the crisis associated with the post-election violence in the country in early 2008 and the global financial crisis the following year, Kenya's tourism sector is returning to commendable levels of growth as a result of policy, institutional and market responses to the crisis. International tourist arrivals to Kenya grew by about 8 per cent in 2010 to reach 1,609,100 while revenue grew by 17.9 per cent to reach Ksh 73.68 billion. The revenue performance represented a 26.3 per cent shortfall of the ministry's projection of Ksh 100 billion. While the arrivals performance in 2010 was about 11.4 per cent less than the best ever performance achieved in 2007, tourism earnings in 2010 were the best ever for the country. Beach tourism registered a 16 per cent decline, which was attributed to deterioration of the product quality.

This performance has been achieved following aggressive marketing campaigns by the Kenya Tourist Board (KTB), targeting domestic and international tourists; enhanced partnerships with international travel and leisure organizations; as well as global advertising on international media and airlines to build a strong image for Kenya as a niche tourist destination. It was also enhanced by investment on market-specific advertising, market missions, joint marketing with tourism trade partners, public relations activities and participation in travel and tourism exhibitions. In addition, KTB opened representation offices in new and emerging markets such as India, China, United Arab Emirates, Japan, Poland and Turkey, and a new venture into Russia.

Although it has great potential to generate revenue, tourism is highly susceptible to shocks in domestic

and international environments. Such shocks include political and macroeconomic uncertainty, and insecurity associated with terrorism risks. With Kenya's porous borders and constant threat from terrorism, the security situation in the country remains one of the most significant hindrance to further development of tourism. The government has stepped up internal security operations against terrorist groups along the border with Somalia and the coastline in order to reassure inbound tourists that the country is still a safe haven to visit.

Despite the importance of tourism in foreign exchange generation and the relative high government spending, funding to the sector is very low relative to the resources required for effective implementation of some of the crucial programmes and flagship projects envisaged in the current Medium Term Expenditure Plan (MTEP). To implement various objectives and activities outlined in the ministry's Strategic Plan for fiscal years 2008/09–2012/13, an estimated Ksh 115 billion in financial resources is required. Innovative financing through public-private partnerships and incentives to private investors in the sector is necessary.

There is need to fast-track implementation of the recently-enacted Tourism Act 2011 and tourism policy through formation of key tourism-sector institutions responsible for regulation; development and marketing; tourist protection services; research; financing of tourism infrastructural development; and dispute resolution amongst stakeholders in the tourism sector. It is envisaged that this will also lead to development of unique tourism products, improved service delivery and competitiveness in the sector. Continued implementation of the Constitution of Kenya 2010 and Vision 2030 will have a big positive impact on the business environment for tourism. There is need to review the regulatory framework, to repeal numerous permits and licences that have made doing business cumbersome and costly; and put in place legislation that takes into account the potential in the informal tourism sector.

Agriculture

The agriculture sector has recorded positive growth since 2009 compared to previous years. In 2010, agriculture grew by 6.3 per cent. Due to heavy reliance on rainfall, the agriculture sector is considerably vulnerable to weather-related shocks. These shocks have a multiplier effect on other sectors of the economy (such as agro-processing, exports and food prices) that rely on the agriculture sector. As a result, there needs to be a paradigm shift in the strategies that are employed in addressing the agricultural development of the country.

A large segment of the population continues to predictably suffer from chronic food shortages; it is estimated that 39.9 per cent of the population lives on less than US$ 2 a day. Kenya's per capita agricultural production has been on the decline since 2007, attributed in part to drought and the post-election violence. Generally, close to 50 per cent of rural and urban poor households are net buyers of food and they spend between 50-70 per cent of income on food. Interventions should include increased access to food and strengthening of social protection programmes. The devolved system of government will create opportunities for investments in value addition for agricultural products so as to increase the amount of marketable produce from the different county governments. This is expected to spur production of raw materials and increase adoption of technologies so as to meet the demand from this market niche.

Regarding policy issues, there is need to review and harmonize the legal, regulatory and institutional framework governing the agriculture sector by fast-tracking the ongoing consolidation of agriculture policy and legal frameworks in line with the Constitution of Kenya 2010. This will ensure a conducive environment for competitive agricultural production and marketing as well as collaborations and partnerships in the sector. Efforts are being made to strengthen institutional capacity by focusing on restructuring the sector and its institutions for improved coordination. In addition to this,

there is need to develop an integrated information management system and to enhance efficient planning and management.

There is need for targeted efforts to improve and increase agricultural output per unit area. Focus should go to promotion and implementation of existing technology, knowledge and best practices, and ensuring adequate linkages between different actors at different stages along the chain. Specifically, investment should be focused towards removing crippling bottlenecks at the different stages. Biotechnology offers an avenue of improving food security and reducing pressures on the environment. However, widespread use will depend on if food safety, environmental concerns and socio-cultural perceptions/concerns can be adequately addressed.

Under the devolved government, the issue of resource allocation, management and reorganization will affect how much funds the sector gets. Emphasis should be put on the development budget so that the necessary infrastructure can be put in place to cater for and anticipate future agricultural production needs. The sector is expected to undergo institutional reforms in order to fit in a devolved government structure. Increased access to financial services, savings and credit products and transfer services for remittances will go a long way to expand opportunities for producers and other actors in the agricultural value chain.

In addition, it will be necessary to review all relevant legislation relating to fresh and processed farm products in terms of packaging, quality, handling, labelling and health standards with a view to making them relevant, and establish effective and efficient frameworks and mechanisms for surveillance and enforcement.

Wholesale and Retail Trade

The trade sector has been identified as one of the key sectors to play a crucial role towards attainment of national development objectives in Kenya especially under Vision 2030. The sector is also important towards the achievement of the Millennium Development Goal (MDG) Number 1 on 'eradicating extreme poverty and hunger' and Goal Number 8 on 'developing global partnerships for development'. The trade sector provides an evolving link between producers and consumers and contributes significantly to the national economy. The trade sector comprises five economic areas, namely: distribution and wholesale trade, retail trade, international trade, informal trade, and trade in services and electronic trade (e-commerce).

Under the current Constitution of Kenya (CoK, 2010), international trade is a function of the national government, while domestic trade will be managed under the county governments. The Fourth Schedule of the Constitution Part 2 points that the county governments will be in charge of trade development and regulation, including markets, trade licences (excluding regulations of professions), fair trading practices, local tourism and cooperative societies. Wholesale and retail trade is, therefore, one of the key sub-sectors in the economic development agenda of Kenya, which is expected to expand substantially as the economy moves towards a 10 per cent growth target.

Over the last three years, the wholesale and retail sub-sector registered improved performance; it was valued at Ksh 154,558 million in 2010 up from Ksh 131,754 million in 2007. As a share of GDP, it contributed 9.7 per cent in 2007 compared with a contribution of 10.3 per cent in 2010. However, the sub-sector's performance slowed down drastically from a peak growth rate of 11.6 per cent in 2006 to 7.8 per cent in 2010. The drop was mainly attributed to poor economic performance following the effects of the 2007 post-election violence, drought and the global financial crunch.

The phenomenal growth of the ICT sector, especially the rising subscription and penetration of mobile telephony and internet services, is likely to spur the growth of the retail of ICT-related

products and consumer goods in general. Sustained competition in the sector is expected to drive down average tariffs and further increase use and coverage. Besides, the rapid growth of urbanization in Kenya and the associated rural-urban migration is expected to fuel demand for consumer goods and services in the medium to long term.

Further, the envisioned devolved system of government portrays basic features of 'a free trade regime', in which county governments will, by and large, be 'open economies' allowing relatively free mobility of goods, persons and capital within and across their jurisdictions. In this regard, there is need to fast-track ongoing regulatory reforms relating to streamlining registration and licensing as well as other factors affecting the operations of wholesale and retail trade. For instance, licensing is currently under the Ministry of Local Government, whose main focus is revenue collection. The Ministry of Trade, through the Department of Domestic Trade, needs to play a more strategic role in streamlining operations of wholesale and retail trade.

Finally, the domestic market of about 40 million people is becoming closely integrated with the EAC (regional) following the coming into force of the EAC Common Market Protocol and steady progress towards a Monetary Union. The EAC integration boasts of a single market with an estimated population of 130 million persons and GDP of US$ 72 billion. Thus, there are prospects for expanding exports of processed and semi-processed products including food, beverages, cement and refined petroleum through locally-incorporated retail outlets. There is need for Kenya to push for the reduction of non-tariff barriers in both COMESA and EAC regions so that Kenyan wholesale and retail outlets can increase their operations and presence in the region and take advantage of the expanded market.

Micro and Small Enterprises

The Micro and Small Enterprise (MSE) sector is one of the most dynamic and fastest growing sectors of the Kenyan economy. Although the sector is prolific in terms of job creation, there are concerns that employment in the sector is not decent. Micro enterprises employ 10 or fewer workers, while small enterprises employ 11-50 workers and can either operate formally or informally. Given the wide coverage and magnitude of the sector, it has been identified as a key agent in stimulating economic growth and enhancing equitable income distribution.

The MSE sector accounted for 74.7 per cent of all formal establishments in Kenya. The number of formal MSEs in the country increased by 11.88 per cent to 35,165 in 2010, contributing to 42.2 per cent of total formal employment. Majority of MSEs operate in the service sector, of which 36 per cent are in wholesale and retail trade, restaurant and hotels; 23 per cent in community, social and government services; and 10.6 per cent in manufacturing. MSEs have potential to create productive employment opportunities to bridge the job deficit in the country.

Over the years, different ministries have been responsible for different MSE-related activities and roles, hence complicating coordination of MSEs. Recent reforms in the financing of MSEs include the establishment of the Youth Enterprise Development Fund and the Women Enterprise Fund. During the 2010/11 Budget Speech, the Minister for Finance created a Ksh 3 million small and medium enterprises (SMEs) revolving fund. This fund received a further Ksh 1 million following the 2011/12 Budget Speech. However, the utilization of this fund has been slow due to disagreements between MSEs and the relevant ministry regarding the conditions set for accessing the funds. In October 2011, a Micro and Small Enterprise Bill was introduced in Parliament as a private member's Bill, which provides for a MSE Authority with roles similar to the proposed National Council for Small Enterprises (NCSE). The MSE sector has not previously had any law regulating or promoting it.

In order to improve coordination in the MSE sector, there is need to fast-track the enactment of the MSE Bill, which provides for the establishment of a MSE Authority. Similarly, efforts should be made to ensure that laws and regulations addressing the MSE sector are harmonized to ensure proper coordination. The definitions provided in the Public Procurement and Disposal Act (Act No. 3 of 2005), the Income Tax Act (CAP 470), the MSE Bill 2011 and other relevant statutes should, therefore, be uniform.

Strengthening organization and advancing unification will provide the answer to problems of fragmentation and lack of a shared vision. There is need to educate the MSE operators about the need and benefits for a unified MSE sector in an emerging political and economic integration and in a global environment. The MSE sector should, by consensus, form an umbrella association at the national level, which should develop from constituency, ward and county levels. Building stronger associations implies that the government and the private sector will assist in the reinforcement of association structures at sub-regional and sub-national levels.

The government should also provide incentives to MSEs (to encourage them to formalize) such as tax rebates, access to government procurement of goods and services, one-stop shop for registering, licensing, and providing technical support to MSEs. Since the government is depending on the MSE sector to meet most of the targets set in Vision 2030, including employment, MSE parks, Special Economic Zones (SEZs), wholesale and retail hubs, the commercialization of agriculture and the MSE national survey should be prioritized. MSE data needs to be updated since the last national survey on MSEs was conducted in 1999. The survey should include modules to capture the size and nature of the informal sector, which have not been included in previous surveys. The results of which will assist in policy and strategy formulation and implementation.

Manufacturing Sector

The contribution of the manufacturing sector to the economy has remained at about 10 per cent over the years, contributing 9 and 10 per cent in 2009 and 2010, respectively. The near-stagnant sector contribution to Gross Domestic Product stems from policy setup under which the sector has operated since independence. The employment growth averaged 1.43 per cent per annum over the 2005-2009 period and, overall, the sector contributed to 13.0 per cent of all formal employees nationally in 2010. The improved sector growth and output in 2010 has been attributed to declining interest rates, which attracted new investment in the sector, low inflationary trend (4.1% in 2010) that boosted local consumption, availability of raw materials (mainly agricultural output) and reliable power supplies.

Constraints that hinder manufacturing competitiveness in Kenya include low value addition and diversification, low productivity, slow investment growth, low research and development, narrow export base, influx of counterfeits and substandard goods, high production costs associated with poor physical infrastructure, and high costs of energy. The period 2008-2010 has experienced renewed government commitment for reforms to facilitate industrial development in Kenya. Such efforts include the enactment of the Anti-Counterfeit Act 2008, ongoing MSME competitive project to improve growth and competitiveness of MSMEs in Kenya through increase in access to finance, strengthening enterprise skills and market linkages, and improving the business environment. However, there is need for more institutional reforms for the manufacturing sector to overcome teething challenges that impede its growth.

Kenya's manufacturing sector is still largely based on agro-processing and production of consumer products. Strategic transformation of the manufacturing sector requires planning and implementation of well-defined strategies. Overall, the South East Asian countries have had a remarkable industrial growth, adopted industrialization

strategies that were oriented to changes in the global environment and market requirements while at same time, they have been sensitive to national goals. Kenya needs to formulate an industrialization policy to guide the manufacturing sector to meet the ever-changing demands of consumers within a global context. While providing incentives to attract local and foreign direct investment, the industry policy should create a level playing field for competing firms. In addition, there is need for a more participatory planning process with firms and interest groups to ensure implementation of the Anti-Counterfeit Act 2008.

To promote creation and growth of small firms, efforts are required to put the MSE clusters in the global value chain, as this enhances possibilities of new market avenues as well as benching indigenous market innovative efforts to international standards. Low productivity in manufacturing is partly attributable to weak linkages with other sectors and within sub-sectors of the manufacturing establishments. Many enterprises are discouraged by high cost of capital and energy, and bureaucratic and inefficient provision of public services. To address these setbacks, the National Economic and Social Council (NESC) has recommended a cluster development strategy to create related and supporting industries. For instance, ICT can potentially contribute more to the manufacturing sector by reducing transaction costs.

Business Process Outsourcing/Off-shoring

The Business Process Outsourcing (BPO) sector has significant potential in making important contributions to the country's economy. The Vision 2030 target is to create at least 7,500 direct jobs in the sector and increasing GDP contribution by Ksh 10 billion by 2012. Currently, the sector provides employment to 1,000 workers, accounting for less than 0.01 per cent of GDP. Unlike India, the BPO sector in Kenya is young, small and largely under-developed.

The BPO sector relies heavily on Information Technology (IT) infrastructure. In 2010, data and internet revenue peaked at Ksh 148,033 million, while data and internet investment was valued at Ksh 29,361 million. The improved internet access and increased internet investment can be attributed to the landing of the undersea cables in 2009-2010, which contributed to increase in international internet bandwidth at lower access costs. Kenya now has three undersea cables: EASSy, TEAMS and SEACOM. The latter two account for 98 per cent of total international internet bandwidth. Kenya has also experienced growth in mobile data/internet subscription provided by the different mobile service providers, which accounts for 98 per cent of total internet subscriptions.

Based on the best practices reviewed, some priority areas should be addressed. Firstly, the legal and policy framework should be strengthened to promote the ICT and BPO sector. Secondly, in order to improve the business environment, the government should introduce a one-stop shop, which would assist investors in obtaining all the necessary business registration and licensing requirements. Thirdly, additional training and capacity building is required for personnel to equip them with soft skills and specialized writing skills, telephone etiquette, internet marketing, and customer service in order to increase their productivity in the BPO sector.

Kenya needs to develop and market its niche markets in the areas of human resource, accounting, software development, design, and travel and tourism. These niches should be developed from ready skills, whereby companies already offering such services locally are source clienteles from overseas. Such companies can utilize the power of 'internet marketing' to increase their visibility in the global market place. The role of the government in respect to this is, therefore, to provide such businesses with investment grants, capacity building support and to institutionalize such skills training into tertiary education.

Finally, in the development of the Konza Technology City, the following key factors should be considered: ensuring the local communities benefit from the development; putting in place safeguards to manage electronic waste; appropriate public-private partnership (PPP) regulations for the technopolis, in line with the ongoing development of the PPP Bill; and a one-stop shop modality to make business start-up and operation procedures easier. Lastly, the technopolis development should provide incentives to attract local and foreign investors and provide support to local investors.

Financial Services

Financial institutions are the main intermediation channels between savings and investment in the economy and are, therefore, critical for attaining broad-based economic growth as envisaged in Vision 2030. As at 31 December 2010, there were 43 commercial banks (both local and foreign owned) with 1,063 branches, 1 mortgage finance company, 5 deposit-taking microfinance institutions, 126 foreign exchange bureaus and 3,280 active SACCOs. In the same period, there were 46 licensed insurance companies and two locally-incorporated reinsurance companies. As at December 2010, 15 million Kenyans were enjoying mobile financial services. Although the financial sector expanded by 8.8 per cent in 2010, its contribution to GDP increased marginally to 5.6 per cent from 5.5 per cent in 2009.

With regard to cost of credit, high interest rate spread (currently at 8.5%) is a key challenge and an impediment to financial intermediation growth goals. In 2010, the NSE 20 share index increased by 36.5 per cent to close at 4,432.6 points from 3,247 points in 2009. However, compared to aspirator countries, as a percentage of GDP, market capitalization for Kenya is below 50 per cent while proportions for countries such as Korea, Chile, Malaysia, South Africa and Singapore are 100 per cent and above.

In order to expand financial access and address the cost of financial services in Kenya, there is need to embrace financial literacy–to contribute to transparency, competition and reduction in information asymmetries. Moreover, as the complexity of financial products increases, consumers need to be empowered so that they can assess inherent risks, emerging markets and products. This would protect consumers and foster stability of financial systems. Public-private sector collaboration can be an efficient way of realizing financial literacy. The Central Bank of Kenya should take the lead towards this goal.

Enforcing the recently enacted Competition Act would also help to reduce the cost of credit in the country, since its enforcement will protect consumers from unfair and misleading market conduct. The Competition Authority should be fully facilitated to enable it perform its mandate effectively. Further, putting in place an integrated property information system would remove the information asymmetry problem in the credit market, as well as solve the existing collateral issues. Ensuring a stable macroeconomic environment, including achieving low levels of inflation, is important in lowering interest rates and interest positive spread.

There is also need to restore confidence in the stock market. As evidenced by over-subscription in the recent issues of bonds, investors are willing to invest where returns are assured. Efforts to continue strengthening the supervisory role of the Capital Markets Authority (CMA) need to be sustained, coupled with effective enforcement of the Capital Markets Act to stem vices of poor governance in the industry. Further, CMA needs to enhance the education campaign on capital markets and also sensitize the public on reforms undertaken, in order to boost their confidence.

To enhance the uptake of insurance services, it is important to strengthen governance in the insurance industry. To complement the supervisory role of the Insurance Regulatory Authority, there is need

to legally recognize the role of the Association of Kenya Insurers (AKI), the Association of Insurance Brokers of Kenya (AIBK) and the Insurance Institute of Kenya under the Insurance Act. Such a move will be crucial in stemming out vices such as poor corporate governance and money laundering, to which the industry is potentially vulnerable.

Environment and Natural Resources

Approximately 80 per cent of Kenyans depend on natural resources (such as land, forests, water, fisheries, wildlife and air) for their livelihoods and household income. Appropriate government policy and sustainable exploitation and management of the key natural resources for the country is critical towards realization of economic growth and poverty reduction coupled with better livelihoods for all Kenyans. Kenya's challenge is to devise sustainable environmental policies that incorporate an appropriate mix of economic incentives and suitable institutional arrangements based on clear specification of property rights. Although the ongoing comprehensive institutional, legal and policy reforms in the sector are still at an early stage, notable achievements so far include the success of the new legislation on stopping excisions and efforts in barring settlements in the Mau forest complex.

With its natural endowment of renewable freshwater but only 647 cubic metres per capita per annum under normal circumstances, Kenya is classified as a water scarce country. Interventions proposed for the sub-sector include alignment of the Water Policy with other sectoral policies including irrigation, land reclamation, environmental sanitation and hygiene policies, among others; clear classification and adoption of water companies as private or public with guidelines on their formation and operation; prioritizing demand management so as to promote water use efficiency; and putting in place a water management information system to collect accurate data on water resources in terms of quantity and quality.

The freshwater and marine fisheries sub-sector employs about 35,000 and 8,000 fishers, respectively. The country earns about Ksh 4 billion in foreign exchange and the fishers over Ksh 7 billion, thus contributing to poverty alleviation in rural Kenya. The government has launched its first-ever National Oceans and Fisheries Policy, which is envisioned to increase income from fisheries to around Ksh 10 billion annually by the year 2014. In order to boost the performance of the fisheries sub-sector, proposed interventions include integrating the sub-sector into the country's agricultural sector to improve food security; developing and improving infrastructure to facilitate increased fisheries production and export; and developing a clear strategy for implementation of the comprehensive fisheries policy.

Kenya's wildlife biodiversity provides the base for the tourism industry, research and education. The country's wildlife is found in an area of 4,403,595 hectares (about 8% of land area), gazetted by the government for wildlife conservation. There are 4 marine national parks, 6 marine national reserves, 23 terrestrial national parks, 26 terrestrial national reserves and 5 national sanctuaries representing key ecosystems in the country and home to 30 per cent of total wildlife. The rest is found in 17 community sanctuaries and private conservancies. The major concern in wildlife is the rapid decline in population, both in and outside protected areas. The Wildlife Bill, which is currently underway, is a great opportunity for the country to put things right.

At least 70-80 per cent of mining activities are dominated by small-scale artisan miners, mainly involved in exploiting non-metallic minerals. Lack of clear mineral exploitation policies hinders the maximum exploitation of minerals in the lucrative industry. According to estimates, mineral production was valued at US$ 106.6 million in 2003. As part of reforms in the sector, the Mining and Minerals Bill 2011 was recently tabled in Parliament, which will repeal the Mining Act Cap. 306 of the Laws of Kenya enacted in 1940. The proposed legislation is expected to address regulation, sustainable

utilization of mineral resources; equitable access and benefit sharing, considering interests of communities affected by mining activities, alternative mine closures and development of new mine sites; and value addition to raw minerals before export.

Pollution and solid waste are some of the leading environmental health problems in the country affecting both rural and urban populations. While the focus of solid waste management (SWM) in the country has been disposal, this is an end-of-pipe solution which, if not handled properly, can only worsen the waste problem. In order of priority, several measures should be institutionalized in SWM in the country, including reduction of waste, reusing of products, recycling/composting the products, recovering energy by incineration, disposing products using landfills, and enacting a comprehensive policy and legislative framework.

Transformative Institutions for Delivering Kenya Vision 2030

Data shows that the Kenyan economy, while it has been steadily improving, has not kept pace with the growing population in a manner that would see a sustained long-term improvement in the welfare of the population. This population has been growing rapidly, is youthful, comparatively educated and increasingly urbanizing. The natural environment within which it is growing is deteriorating as manifested in Kenya's water availability classification, frequent recurrence of droughts and the increasing occurrence of communal clashes over the same. All this is taking place in a regional and global environment that is increasingly uncertain, with potentially adverse consequences for Kenya. It is within this environment that Kenya must create welfare improvement opportunities for its citizenry.

Kenya is in the midst of a major shift in the management of its affairs as it seeks to make a shift to the next level. This shift is anticipated in Kenya Vision 2030, hence the need to put in place institutions with operative capacity to create growth and development in all pillars stipulated in Vision 2030. Key questions that are pertinent in Kenya's reform experiment include: How can government reinvent itself to solve the problems that face us today or those that have been caused by it? Has the problem of governance aligned itself to the challenges we face today? Why do institutions fail us and how do we fix them? Smart, sustainable and inclusive growth thrives on strong fundamentals. Institutions, policies and factors that enhance resource-use efficiency and innovation determine the level of productivity of a country, hence a country's competitiveness on the global scene.

As the country implements the Constitution of Kenya 2010, there is need to respond to these questions in designing key institutions. The challenges Kenya faces are largely predictable. Broadly speaking, the following three emerging policy issues can be considered to be the threshold that would be the focus of determining the success or failure of the various institutions operating within the country: Macroeconomic management; human resource development; and infrastructure and economic services. The Constitution is a critical determinant for the nature, mandate and operations of the various institutions in the country. One of the key issues that the Constitution brings forth is the apparent tension between the strong constitutional protections for individual property rights and community rights. The design and operationalization of the various institutions should respond to these policy concerns.

Enhancing efficiency in governance and achieving equity in regional development are key features of the Constitution of Kenya 2010. Strong public and private institutions are indispensable in the pursuit of these crucial public policy goals. Strong institutions contribute immensely to national development since they instil into the system the following key strengths, among others: reduced economic costs of doing business through an enabling environment free of over-regulation, bureaucracy and red tape, corruption and corporate scandals; independence of

the Judiciary; ethical and transparent public-private sector dealings; protection of property rights; sound management of public finance; strong auditing and reporting standards; and a level playing field that attracts high investor and consumer confidence.

One of the key challenges that will have to be faced in the structuring and organizing of government will be the need to proactively have a government that will, over the medium to longer term, lead to increased trust in government by citizens. Literature shows that when citizens or governments do not trust governance institutions, they increasingly seek to control them and the processes therein. One of the key adverse consequences of this is seen in increased transaction costs in terms of governance institutions to be built and the processes requiring participation. The ongoing administrative and sectoral reforms, therefore, must immediately do a stock take and account for the implications of the Constitution of Kenya 2010.

With regard to capacity building, even under the previous constitutional dispensation, capacity (human resource, facilities and equipment) has been a challenge. Implementation of the Constitution will exacerbate this challenge if not well managed. There is need to define institutions early and their resource requirements determined *vis a vis* available capacities. Experiences in countries that have decentralized, almost all on a much smaller scale than Kenya, show that some failed because of lack of adequate capacity.

Moreover, there is need to strengthen coordination of the institutions in each sector (both public and private sector institutions), for example, through participation in regular consultative meetings; enhancing sectoral policy research to inform planning processes; conducting audits of existing institutions (before forming new ones) in order to determine their resource needs; enhancing private sector participation through Public-Private Partnerships; and revising the entire budgetary process in order to provide adequate funds to key public productive sector institutions.

PART I

Macroeconomic and Socio-economic Performance

This part provides an analysis of the recent macroeconomic and socio-economic performance in Kenya. It reviews the achievements and challenges, and provides policy recommendations aimed at improving economic growth and reducing poverty. Besides the chapter on macroeconomic performance, there are chapters on strengthening public expenditure management; and population dynamics and socio-economic performance. These chapters provide an in-depth analysis and identify the main challenges in these policy areas, and make policy recommendations which, if well implemented, would improve the quality of life of citizens.

Chapter 1

Macroeconomic Performance

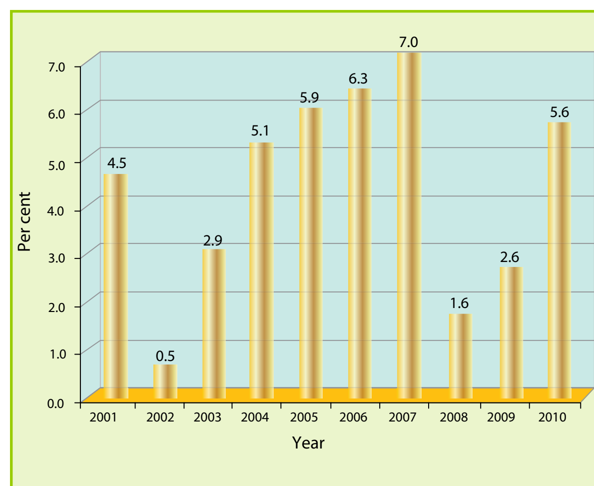
1.1 Kenya's Economic Growth

The Kenyan economy grew by 5.6 per cent in 2010, representing a marked improvement from the 2.6 per cent and 1.6 per cent growth rates recorded in 2009 and 2008, respectively (Figure 1.1). The fourth quarter of 2010 recorded the highest quarterly growth rate of 6.9 per cent compared to a growth rate of 3.3 and zero (0) per cent in the same quarters in 2009 and 2008, respectively. The third quarter of 2010 recorded GDP growth of 6.1 per cent compared to a growth of 0.5 per cent in 2009 and 2.7 per cent in 2008. The second quarter of 2010 recorded GDP growth of 5.3 per cent compared to growth rates in the same quarter of 0.9 per cent and 2.4 per cent in 2009 and 2008, respectively. The first quarter of 2010 recorded the slowest growth in 2010, on a quarterly basis.

Various factors explain the improved economic performance in 2010. Firstly, is favourable weather conditions, which contributed to improved agricultural output. Secondly, the effects of the economic stimulus package started to take effect across the various sectors of the economy. The Central Bank of Kenya sustained monetary policy support by consistently reducing the Central Bank Rate (CBR). Other factors that contributed to the impressive economic growth over the last three quarters were improved liquidity in the economy, prudent macroeconomic management, and recovery in the global economy.

Financial intermediation recorded a growth of 8.8 per cent in 2010, up from 4.6 and 2.7 per cent in 2009 and 2008, respectively. This is attributed to increased lending following increased liquidity in the money markets. Agriculture recorded improved growth in 2010 compared to the corresponding period in 2009. The sector grew by 6.3 per cent, up from a contraction of -2.6 and -4.1 per cent in 2009 and 2008, respectively. The performance reflected recovery from the effects of the 2008 post-election violence and drought conditions during

Figure 1.1: Kenya's GDP growth (2001-2010)



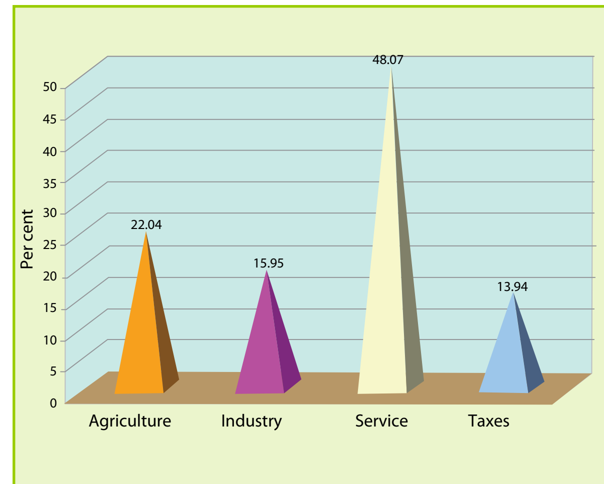
Source: Government of Kenya (2010a; 2010b). *The value for 2010 is provisional.

the same period. The improved performance of the agricultural sector might also have been supported through the provision of subsidized farm inputs such as fertilizer and seeds by the government. The tourism sector also appears to have fully recovered from the effects of the post-election violence with an impressive growth of 17.9 per cent recorded in 2010. Improved growth in the sector could be explained by improved political stability in the country, the promulgation of the new Constitution in August 2010, and efforts to promote Kenya as a tourist destination. The manufacturing sector grew by 4.4 per cent in 2010 compared to a growth of 1.3 per cent in 2009. Growth in the sector was boosted by improved electricity and water supply, and recovery in the agricultural sector that supported agro-based industries. Electricity and water sub-sectors grew by 9.9 per cent in 2010.

A comparison of the sectoral shares in total GDP given in Figure 1.2 shows the service sector had the highest contribution to GDP of about 48.07 per cent, agriculture 22.04 per cent, and industry 15.95 in 2010. Wholesale and retail trade contributed 10.3 per cent share in total GDP, hotels and restaurants 1.7 per cent, transport and communications 9.8 per cent, and financial intermediation 5.6 per cent. Mining and quarrying stood at 0.70 per cent, manufacturing 10 per cent, electricity and water 2.4 per cent and the construction industry at 4.3 per cent.

Going into 2011, GDP growth is expected to slow down due to high oil prices and slow global economic recovery. Near-term weather outlook indicates that drought conditions might affect food security and thus increase inflationary pressure, leading to a negative impact on real household disposable incomes and consumption.

Figure 1.2: Sectoral shares in total GDP in 2010



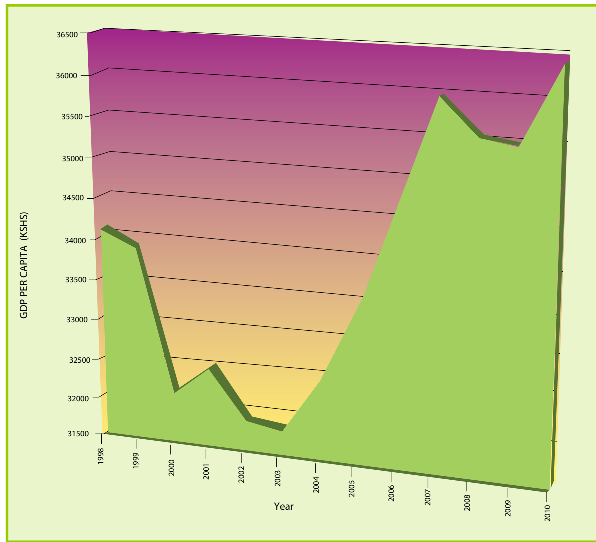
Source: Government of Kenya (2011) and author's own computations

1.2 Per Capita Income

Real GDP per capita increased from Ksh 35,470 in 2009 to Ksh 36,419 in 2010 after a slight slowdown in 2008 and 2009, following the 2008 shocks (post-election violence, global financial crisis and drought). Kenya's real GDP per capita, as shown in Figure 1.3, recorded a marked decline from the 1990s to around 2003. After 2003, real GDP per capita was on the rise until the year 2007 and then dampened again thereafter.

The slowdown in real GDP per capita in the 1990s and early 2000s could be attributed to the general slowdown in economic growth in the country around that time. As economic growth picked up in the year 2003, peaking at 7.0 per cent in the year 2007, real GDP per capita was on the rise. The dampening in the year 2008 afterwards was as a result of the slowdown in economic activity brought about by the multiple effects of the post-election violence, the global economic crisis of 2008 and drought in the country, which reduced agricultural output. With the dim projection of GDP for the year 2011, real GDP per capita is also expected to slow down.

Figure 1.3: Real GDP per capita



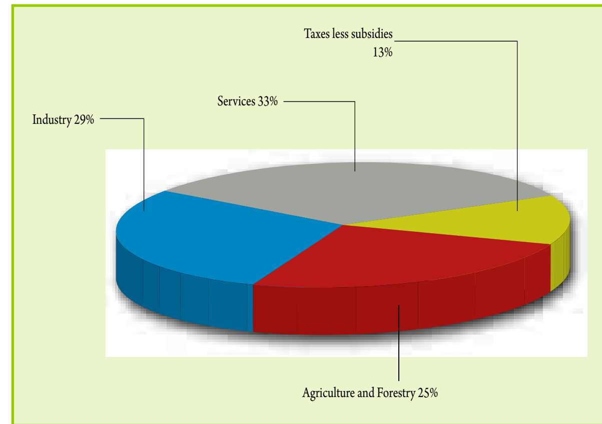
Source: Government of Kenya (Various), Economic Surveys

1.3 Sources of Growth

In 2010, agriculture accounted for about 24.5 per cent of GDP growth. This is an improvement from a contribution of -22.9 per cent in 2009 and a contribution of -64.0 per cent in 2008 (Government of Kenya, 2011). The manufacturing sector, which performed dismally in 2009 with its contribution to GDP growth standing at 4.7 per cent down from 22.6 per cent in 2008, recorded an improved contribution to GDP growth of 7.8 per cent in 2010. This also points to the recovery of the main sectors after the post-election violence.

The services sector in general made the highest contribution to GDP growth in 2010. The main sub-sectors that contributed most to GDP growth in 2010 just like it was in 2009 remained transport and communications sub-sector, with transport and communications contributing 13.0 per cent to growth, transport and storage contributing 8.9 per cent, and post and telecommunications contributing 4.1 per cent.

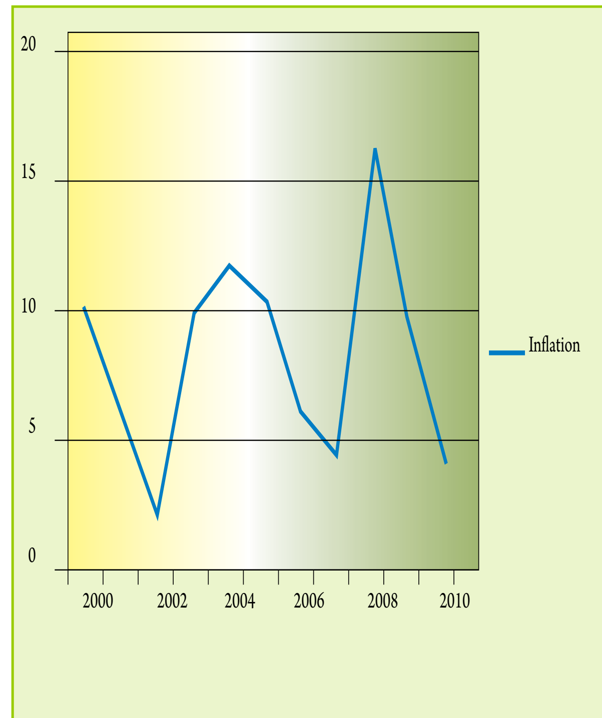
Figure 1.4: Sectoral contribution to total GDP growth in 2010



1.4 Inflation

The key objective of monetary policy in Kenya is to ensure price stability. Vision 2030 envisages a monetary policy that will achieve less than 5 per cent annual inflation rate. However, the rate of inflation has remained above the target of 5 per cent, except during 2002, 2007 and 2010.

Figure 1.5: Trends in inflation



Source: Government of Kenya (Various), Economic Surveys, and Central Bank of Kenya (Various) reports

Table 1.1:Inflation rate by commodity group (2005-2009)

Commodity/Year	2005	2006	2007	2008	2009
Food and non-alcoholic drinks	12.5	20.9	12.3	35.3	12.6
Alcohol and tobacco	7.0	8.5	7.7	14.6	8.7
Clothing and footwear	4.6	2.5	3.3	5.3	4.3
Housing costs	5.9	4.6	6.9	6.3	7.6
Fuel and power	21.6	12.7	8.4	21.5	-3.8
Household goods and services	6.8	3.6	5.7	9.4	6.1
Health and personal care	5.0	4.0	4.3	10.7	9.2
Transport and communication	6.0	7.4	5.5	18.1	2.4
Recreation and education	4.0	2.4	3.1	6.6	5.2
Personal goods and services	3.9	2.4	3.4	7.5	9.1
Kenya inflation rate	10.3	6.0	4.27	16.2	9.2

Source: Government of Kenya (Various), Economic Surveys

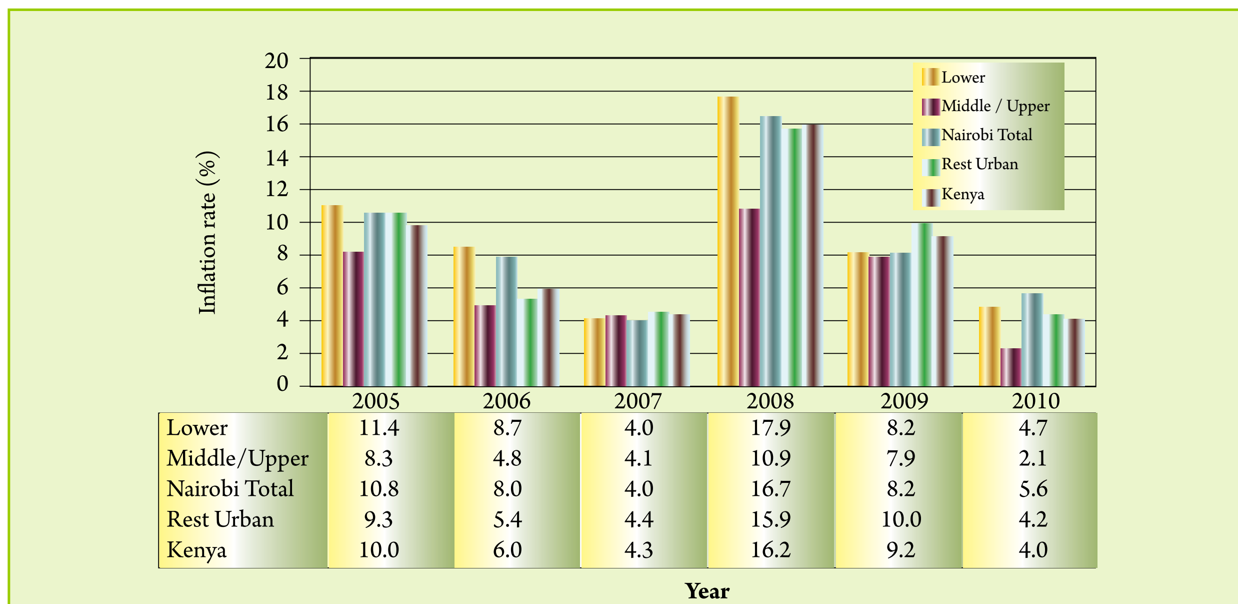
The two most important contributors to overall inflation in Kenya are food and non-alcoholic drinks, and fuel and power prices (Tables 1.1 and 1.2). The high inflation rate in 2008 is largely explained by the effects of the post-election violence that disrupted economic activity, drought and high global oil prices. In 2009 and 2010, Kenya recorded declining inflation pressures largely due to a prudent monetary policy and better agricultural performance. Inflation declined from 9.2 per cent in 2009 to 4.1 per cent in 2010.

Table 1.2: Inflation rate by commodity group (2010)

Commodity/Year	2010
Food and non-alcoholic beverages	5.9
Alcohol beverages, tobacco and narcotics	7.5
Clothing and footwear	3.4
Housing, water, electricity, gas and other fuels	3.2
Furnishings, household equipment and routine house maintenance	3.2
Health	4.4
Transport	5.3
Communication	-10.3
Recreation and culture	1.2
Education	1.4
Restaurant and hotels	4.0
Miscellaneous goods and services	2.2
Kenya inflation rate	4.1

Source: Government of Kenya (Various), Economic Surveys

Figure 1.6: Inflation rate by income group



	2005	2006	2007	2008	2009	2010
Lower	11.4	8.7	4.0	17.9	8.2	4.7
Middle/Upper	8.3	4.8	4.1	10.9	7.9	2.1
Nairobi Total	10.8	8.0	4.0	16.7	8.2	5.6
Rest Urban	9.3	5.4	4.4	15.9	10.0	4.2
Kenya	10.0	6.0	4.3	16.2	9.2	4.0

Source: Government of Kenya (Various) Economic Surveys

Analysis of inflation by income group reveals that the lower income group households residing in Nairobi experienced higher incidence of inflation compared to other groups. This is because expenditure on food represents a large share of the low income group household's expenses, estimated at about 48.3 per cent, compared to upper income households that spend only about 10.5 per cent on food.

The levels of inflation in other countries are important in gauging the regional macroeconomic environment and competitiveness. Figure 1.7 shows inflation trends for selected countries. Within the region, Uganda and Tanzania have had relatively low inflationary pressures.

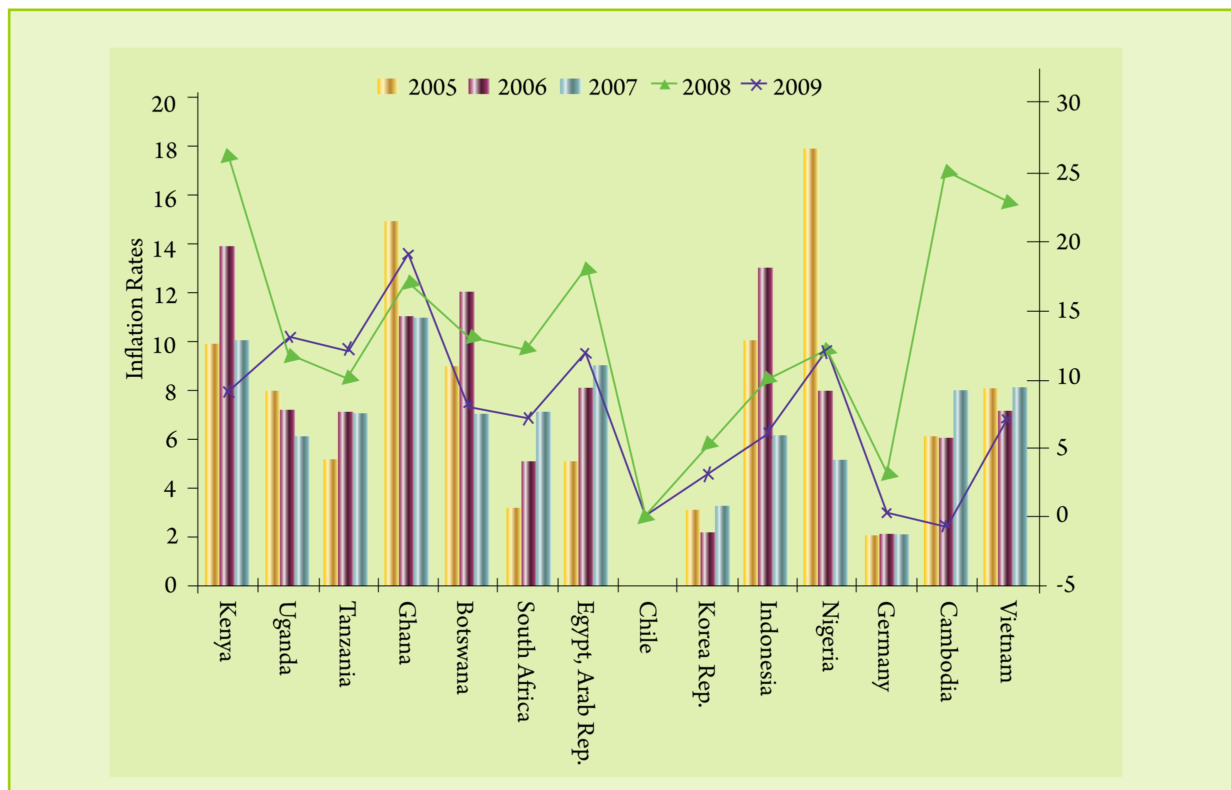
Supply shocks have played a major role in explaining inflation in Kenya. In addition, poor infrastructure network contributes to escalating agricultural commodity prices due to difficulties in accessing markets. Reliance on rain-fed agriculture makes the country vulnerable to extreme weather conditions. On the demand side, expansionary monetary and fiscal policy poses the challenge of accelerating aggregate demand.

1.4.1 Recommendations

i. Improve productivity in the country. There is need to strengthen the Productivity Centre of Kenya (PCK) so that it plays an effective role in improvement of productivity levels in Kenya. PCK offers a forum where the government, the private sector and labour unions ensure that wage and productivity growth lowers inflation levels.

ii. Transform the agricultural sector to produce sufficient affordable food. The government needs to expand and utilize national grain reserves to stabilize food prices during periods of shortages occasioned by supply shocks.

Figure 1.7: Comparison of inflation (2005-2009)



Source: World Bank (2010)

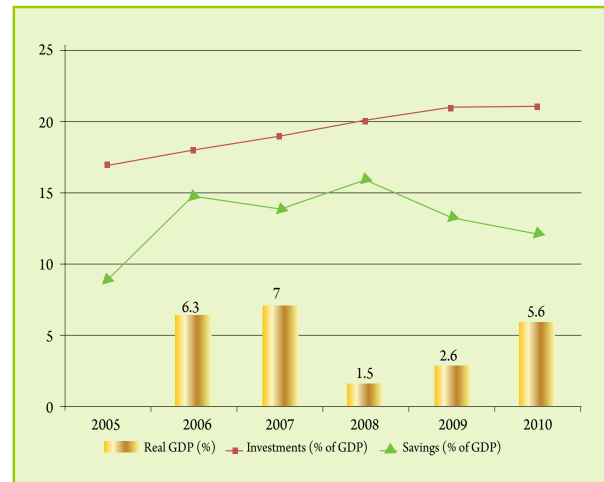
iii. Prudent macroeconomic management is necessary to support economic stability.

1.5 Investment and Savings

1.5.1 Investment-Savings Gap

Kenya is facing an increasing investment-savings gap. The level of savings is low and a large component of capital formation is imported in terms of transport equipment and other machinery. Vision 2030 identifies savings and investment as critical channels through which Kenya can achieve high economic growth prospects that can lead to the attainment of economic development. The MTP (2008-2012) provides a roadmap to enhance investment and savings in the medium term. The promotion of both local and foreign direct investment and savings culture will accelerate the pace of economic growth and development in Kenya.

Figure 1.8: GDP, investment and savings flows

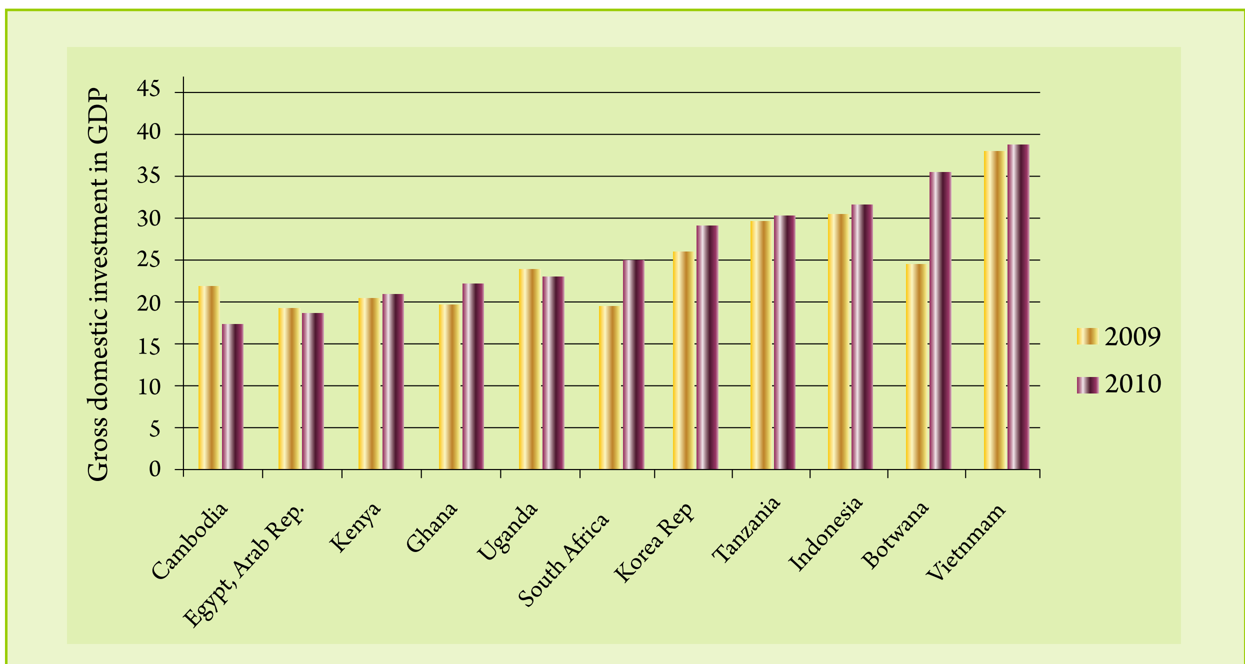


Source: World Bank (2010) and Government of Kenya (2011)

While investment grew from 17 per cent of GDP in 2005 to 19.3 per cent in 2010, savings declined from 16 per cent in 2008 to 12.2 per cent in 2010 (Figure 1.8). Kenya's savings rate is still low and the declining trend should be a matter of serious policy concern.

Kenya's rate of investment and savings remains comparatively low (Figures 1.8 and 1.9). In recent

Figure 1.9: Cross-country investment performance



Source: World Bank (2010)

years, Vietnam has been able to sustain high levels of savings and investment. Other best performing countries include Botswana, Indonesia, Tanzania, and Republic of Korea, which have relatively higher rates of savings.

Kenya is making important efforts to improve the investment environment. The Kenya Investment Authority (KenInvest) was revitalized as a one-stop shop for investment. The regulatory reforms for investment include the review of 1,325 licences and the resultant elimination of 424 licences, rationalization of 694 licences, and simplification of 607 licences. In addition, a Business Regulatory Reforms Unit (BRRU) was established in 2007 to coordinate regulatory reforms. An E-registry of all licences in Kenya has also been operationalized with a view to controlling illegal licensing processes and streamlining the licensing process. Effective implementation of the Constitution will lead to the creation of strong institutions, including the Judiciary, which are critical in investment dispute resolution.

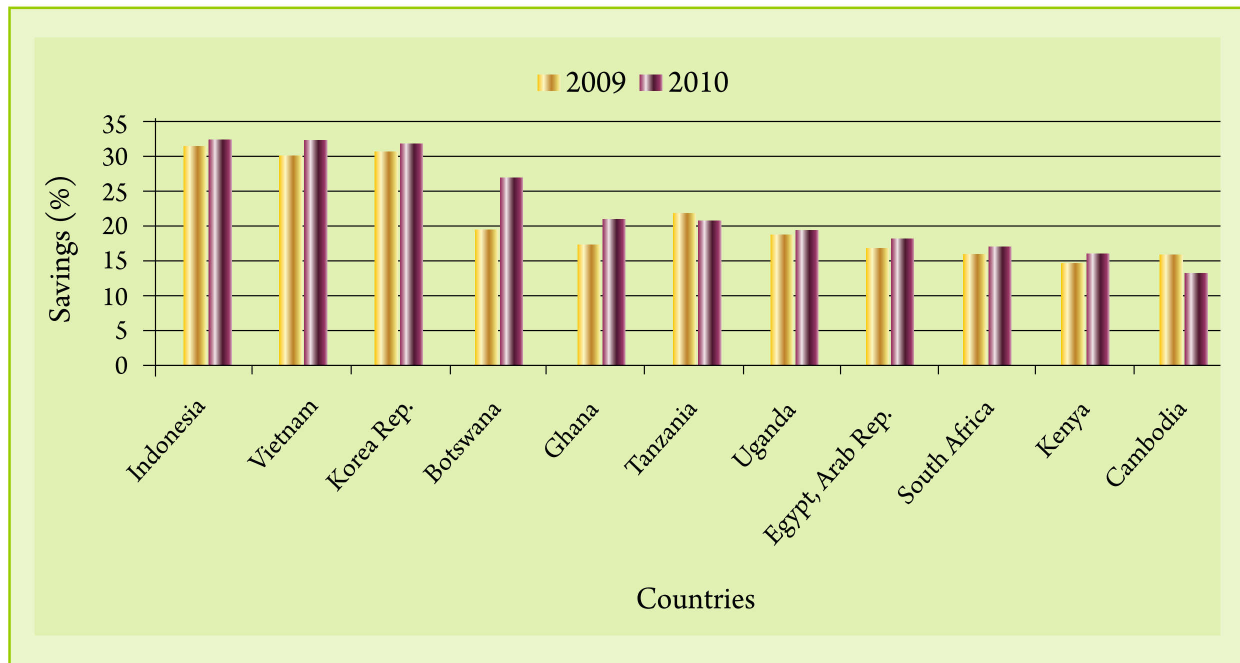
1.5.2 Challenges

The main challenge for investment and savings is poor investment environment. The regulatory environment still remains a hurdle both for local and foreign investment. The weak infrastructure network also adds to the cost of doing business in Kenya. In addition, the lack of a long-term savings culture in Kenya is another challenge. Structural reforms aimed at strengthening governance, especially addressing corruption and improved public service delivery, are critical for the investment environment. There is also need to maintain macroeconomic stability.

1.5.3 Recommendations

For a double-digit economic growth rate to be achieved, improvement of physical and human infrastructure is needed. Priority public investments in infrastructure to facilitate investment and savings identified by Vision 2030 are roads, railways, airways, special economic zones, the port of Mombasa, Information and Communications Technology (ICT), Science, Technology and Innovation (STI),

Figure 1.10: Cross-country savings performance



Source: World Bank (2010)

water and sanitation. Infrastructure development cannot be achieved through public investments only due largely to the huge financial resources required. There is, therefore, need to deepen the public-private partnerships (PPP) policy and legal framework to facilitate private sector participation in infrastructure development. The improvement

Table 1.3: Fiscal performance (Ksh billion)

	2005/06	2006/07	2007/08	2008/09*	2009/10**
TOTAL REVENUE	311.3	373.0	432.2	487.9	586.4
Ordinary revenue[1]	283.4	340	396.5	455.8	538.8
Appropriation-in-Aid[2]	27.8	33.0	35.7	32.1	47.5
EXPENDITURE AND NET LENDING	382.8	419.6	534.8	595.7	791.8
Recurrent	306.5	306.8	403.4	435.5	536.4
Development and net lending	67.7	80.4	131.5	160.2	255.4
Drought development expenditures	1.0	1.5	-	-	-
DEFICIT EXCLUDING GRANTS (Commitment basis)	(71.6)	(46.5)	(102.6)	(107.8)	(205.5)
Grants[3]	20.1	15.5	25.4	18.1	31.2
DEFICIT INCLUDING GRANTS (commitment basis)	(51.5)	30.7	77.2	89.8	174.3
Adjustment to cash basis	15.0	(5.6)	84.7	(27.3)	-
DEFICIT INCLUDING GRANTS (Cash basis)	(36.5)	(36.3)	7.6	(117)	(174.3)
FINANCING	36.5	36.3	(7.6)	117	174.3
Foreign financing (Ksh)[4]	1.2	2.4	6.3	41.1	48.2
Domestic financing (Ksh)[5]	35.3	38.7	13.9	75.9	126.1
Memo items (as % of GDP)					
Total revenue	20.5	21.6	22.0	21.8	23.7
Ordinary revenue	18.7	19.7	20.2	20.3	21.8
Tax revenue	16.9	17.7	18.5	18.6	19.4
Non-tax revenue	1.8	2.0	1.7	1.7	2.4
Appropriations-in-Aid	1.8	2.0	1.8	1.4	1.9
Grants	1.3	0.9	1.3	0.8	1.3
Financing	2.4	2.1	0.39	5.22	7.0

* Indicates preliminary results

** Indicates revised estimates

Source: Ministry of Finance (2010)

of the quality and quantity of health and education infrastructure would also enhance investment and savings. Development of a strong financial system to mobilize resources is critical, and this should include the National Social Security and Pension System, Insurance and Banking, Savings and Credit Cooperative Societies (SACCOs) and the Capital Markets. Only about 19 per cent of Kenyans have access to formal financial services. The target groups for financial access improvement include informal businesses, micro, small and medium enterprises (MSMEs), youths, women groups and entrepreneurs.

1.6 Fiscal Policy and Performance

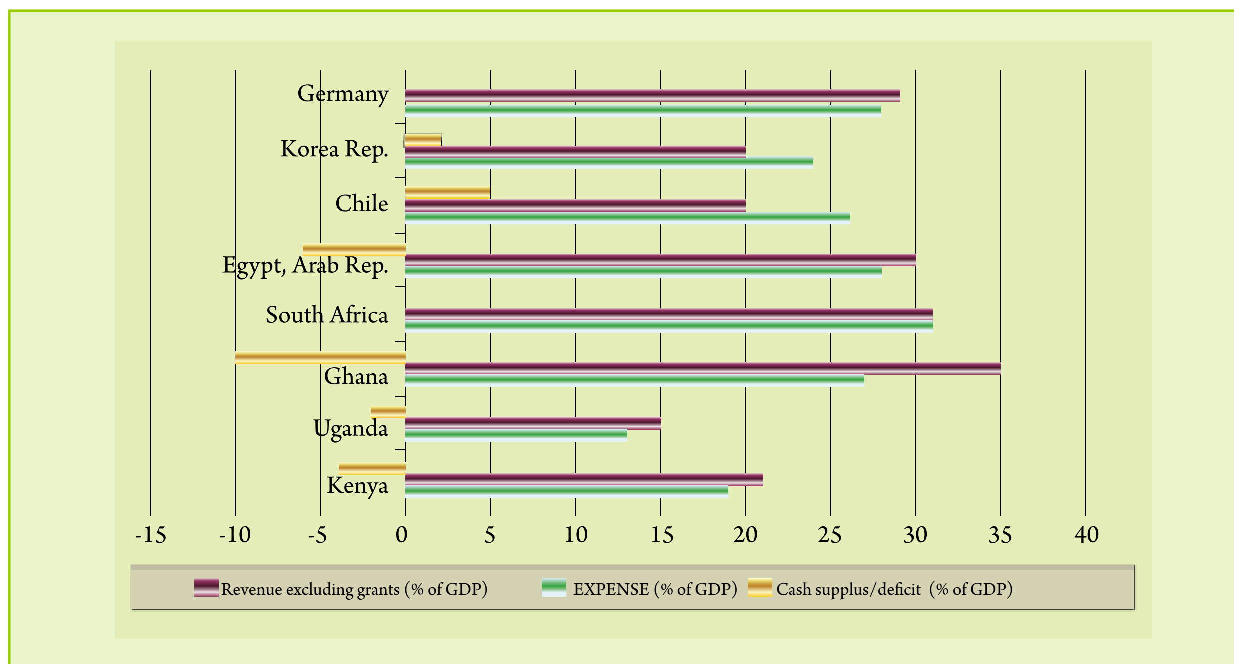
One of the major instruments expected to enable the economy achieve macroeconomic stability is fiscal policy. The fiscal strategy outlined in the Medium Term Plan 2008-2012 envisages the overall fiscal deficit to decline from 5.2 per cent of GDP in 2007/08, to 3.6 per cent of GDP in 2012/13. Other medium-term targets include a domestic debt to GDP ratio of 21-22 per cent, revenue to GDP ratio of 20-22 per cent, public development spending of 9.5 per cent of GDP and decline of public sector wage bill to 6 per cent of GDP.

Kenya has undertaken fiscal policy measures to mitigate the adverse effects of both domestic (post-election disturbances and drought) and external (high oil and fertilizer prices, the global economic and financial crisis) shocks that the economy experienced between 2008 and 2010.

The overall fiscal deficit (on a commitment basis and including grants) was Ksh 174.3 billion (7.04% of GDP) in 2009/2010 (Table 1.3). This figure was above the targeted deficit of Ksh 71.8 billion (2.9% of GDP). In the same year, total revenues were 23.7 per cent of GDP, above the targeted levels by 2.4 percentage points. Similarly, total expenditure and net lending (Ksh 791.8 billion) was 32 per cent of GDP and stayed above the targeted amount by 6.3 percentage points.

Table 1.3 shows that government spending continued to grow faster than revenue collection. Between 2005/06 and 2009/10, recurrent

Figure 1.11: Fiscal indicators, selected countries, 2008



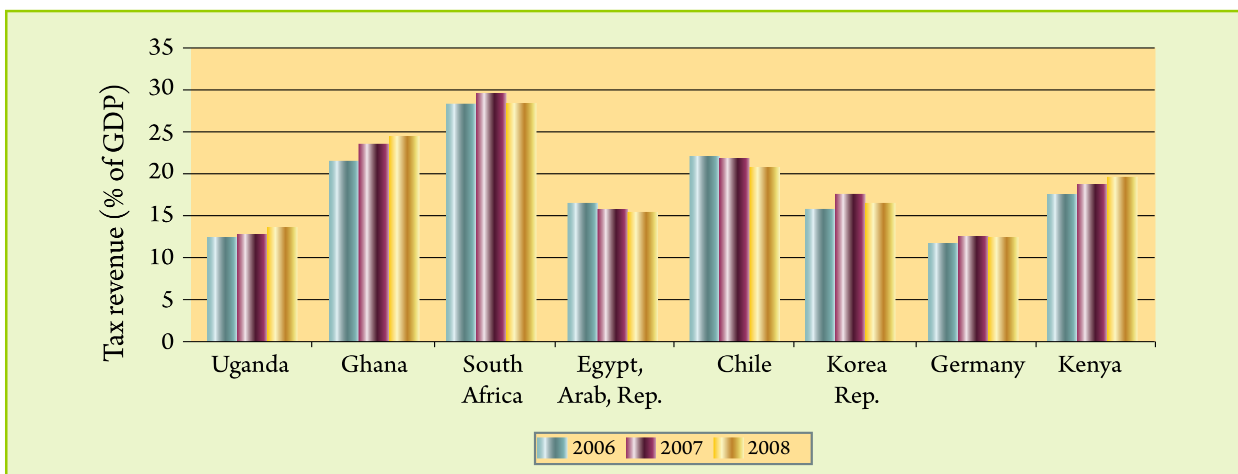
Source: World Bank (2010)

expenditure increased by 75 per cent whereas development expenditure and net lending grew by 277 per cent. The high growth in spending is attributed mainly to the efforts put in place as a result of the MTP target to increase public development spending from about 4.7 per cent in 2006/07 to 9.5 per cent of GDP in 2012/2013. From the table, it is evident that this target was exceeded in 2009/10, since development expenditure and net lending as a share of GDP was 10.3 per cent. The approved sectoral ceilings provided in the Budget Outlook Paper for 2011/12 – 2013/14 show that in 2009/10, the sectors that received the largest share of budgetary resources are human resource development (25.1%); physical infrastructure (21.8%); and governance, justice, law and order (12.4%). The increase in spending is mainly attributed to the government's focus on supporting critical infrastructure in order to lower the costs of doing business, voter registration, costs related to the constitutional referendum, and economic stimulus programmes. In particular, the economic stimulus programmes were initiated to spur economic growth, create livelihood opportunities and help to bridge the equity gap that has been systemic in the country.

Between 2005/06 and 2009/10, taxes have remained the main source of government budget. This implies that taxation is a key instrument at the disposal of the government in achieving the distribution function (through progressive taxation), allocation function (high excise taxes on demerit goods) and stabilization (through enhanced tax elasticity). Tax revenues have maintained a consistently upward trend over the 2005/06–2009/10 period. Over this period, tax revenues almost doubled, rising from Ksh 256 billion to Ksh 476 billion. This trend is consistent with the policy shift by the government towards enhancing local capacity to finance the budget and depend less on external borrowing. The main elements of tax revenue in Kenya are income tax, VAT, customs duties and excise duties. Income tax is the most important component of tax revenues. In 2009/10, the share of income tax in total tax revenue was 43.9 per cent. The second most important source of tax revenue is VAT, with its tax share averaging 30.1 per cent in 2009/10. A comparison between taxes on income and profits and taxes on goods and services shows that the latter are more important in Kenya's revenue structure.

Figure 1.12 shows that Kenya's tax ratio is much lower than that of South Africa, Chile or Ghana but higher than Uganda, Germany, Korea or Egypt. It can be concluded that Kenya has an average tax effort, indicating scope to widen the tax revenue base as a way of increasing tax revenues.

Figure 1.12: Tax ratio, selected countries



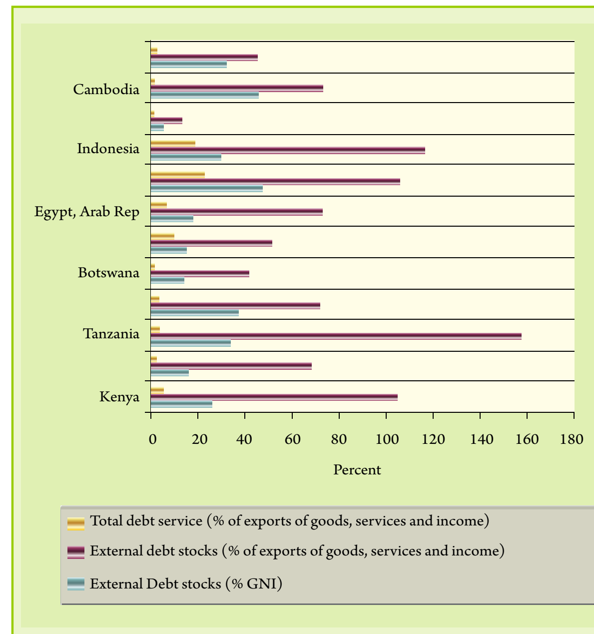
Source: World Bank (2010)

1.7 Public Debt

In June 2010, the gross public debt stock in Kenya was Ksh 1,225.1 billion or 49.5 per cent of GDP. External debt stood at Ksh 565.5 billion, whereas domestic debt was Ksh 659.6 billion (or 26.6% of GDP). This ratio of domestic debt to GDP is higher than the MTP target of domestic debt of 21-22 per cent of GDP. Domestic debt was held by the Central Bank of Kenya (7%), commercial banks (53.2%) and the non-banking sector (39.2%), whereas external debt was held by bilateral lenders (34.7%), multilateral lenders (61.7%), and export credit (3.6%). The main multi-lateral creditors are the International Development Association (IDA), African Development Bank (AfDB), and European Economic Community (EEC), while the main bilateral creditors are Japan, France and Germany. The government mainly issues its debt through sale of treasury bills and fixed rate treasury bonds.

Analysis of Kenya's public debt position reveals the following trends. First, whereas the share of public debt in GDP has fallen from 58.81 per cent in 2004 to 44.84 per cent in 2009, the debt per capita has increased from Ksh 21,912 to Ksh 25,846 over the same period. Second, between 2004 and 2009, the share of domestic debt in total debt increased from 41.0 per cent to 50.1 per cent whereas the share of foreign debt has reduced from 59.0 per cent to 49.9 per cent. Third, the public debt stock has grown from Ksh 749.4 billion in 2004 to Ksh 1,018.3 billion in 2009, an increase of 36.0 per cent. Fourth, the share of annual debt servicing charges for external debt is generally lower than is the case for domestic debt. Fifth, the composition of domestic debt has changed from short maturity to longer term profile; in 2007, the respective shares over the period 2003 to 2007 were 21 per cent and 79 per cent, respectively. However, a comparison of Kenya's debt figures with selected countries reveals that the country's external debt stock (as a % of exports of goods, services and income) is relatively high (Figure 1.13). However, in terms of debt service (as a % of goods, services and income), Kenya's ratio of 5.03 per cent is relatively low. This indicator combined with the high debt to exports of goods and services ratio indicates that Kenya has low export base and low external debt payments. Therefore, Kenyan policy makers should be seriously concerned about expanding the country's export base and competitiveness.

Figure 1.13: Selected indicators of debt burden, 2009



Source: World Bank (2010)

1.8 External Sector Performance

1.8.1 Balance of Payments

Kenya's external sector performance deteriorated in 2010 (Table 1.4). The current account deficit as a percentage of GDP increased from 5.5 per cent in 2009 to 7.8 per cent in 2010.

Table 1.4: External sector performance (% of GDP)

	2009	2010
Current account balance as percentage of GDP	-5.5	-7.8
Merchandize	-16.2	-19.6
Services	10.8	11.8
Capital and financial account	8.5	7.3

The increase in the current account deficit is largely explained by a rapid increase in imports relative to exports. Imports increased by about 24.4 per cent

compared to an increase of about 18.8 per cent in exports. The services account has remained positive mainly due to strong performance in transport and tourism sectors. The capital and financial account registered a slightly lower surplus in 2010. The continued growth in the current account deficit should be an issue of policy concern in terms of sustainability of the external account.

1.8.2 Terms of Trade

Terms of trade refer to the ratio of export price index to import price index. Terms of trade for all items and non-oil items improved by 3.7 per cent and 11 per cent, respectively, to stand at 85 and 110 per cent, respectively, in 2009. This came as a result of faster growth in prices of Kenya's key commodity exports and exchange rate movements (Table 1.5).

Table 1.5: Terms of trade (1982=100)

Description	2005	2006	2007	2008	2009	2010
All items	72	72	70	77	82	85
Non-oil items	84	90	88	94	99	110

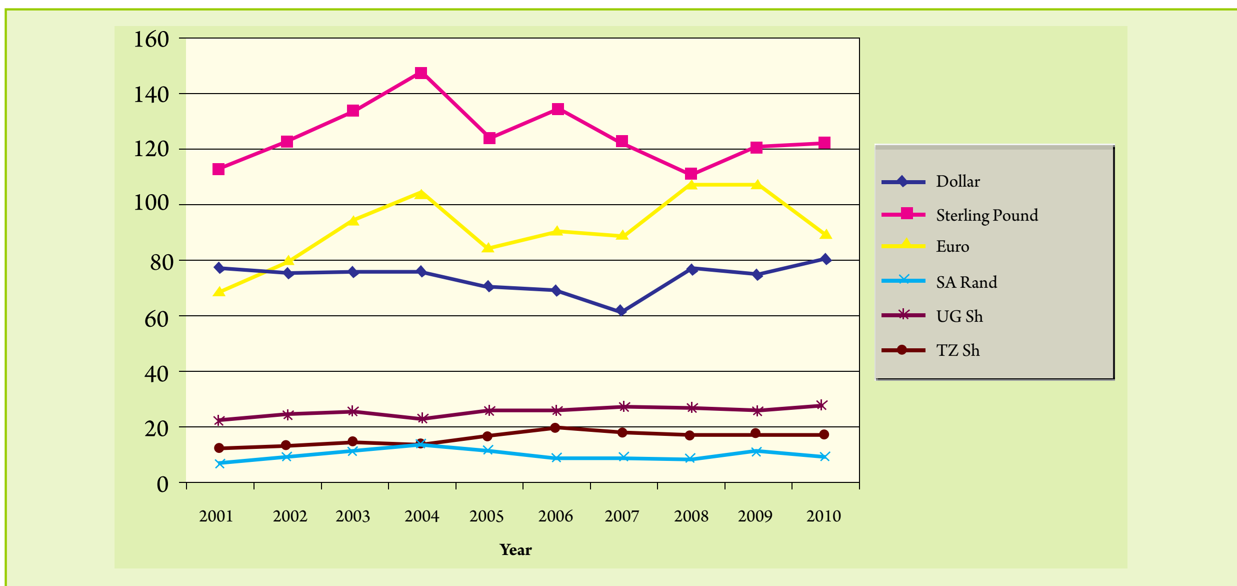
Source: Government of Kenya (2011)

1.8.3 Foreign Exchange Rate

The exchange rate remained stable against the US dollar for the greater part of the period 2003-2007, with some tendency towards appreciation. This reflected a strong Balance of Payments position. Between the periods 2008 to 2010, the Kenya shilling depreciated gradually against the US dollar to exchange at an average of 81.0 in 2010 compared to 77.9 per US dollar in 2009, Ksh 69.18 per dollar in 2008 and Ksh 67 per US dollar in 2007. Overall, the Kenya shilling depreciated marginally against major world currencies as reflected by the trade weighted exchange rate index, which rose to 718.19 as at December 2009. The trade weighted exchange rate stood at 735.13, reflecting a further real depreciation.

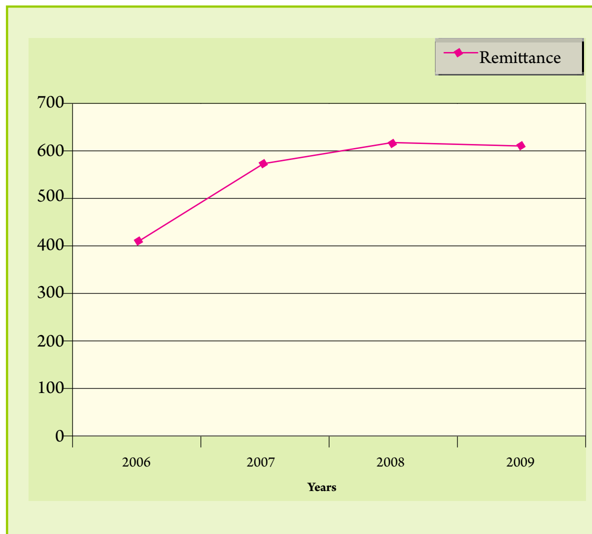
Kenya pursues a flexible exchange rate policy regime where market forces and economic fundamentals play a major role in determining movements in exchange rate. Sound fiscal and monetary policy is, therefore, expected to support a stable exchange rate.

Figure 1.14: Selected end period mean Kenya shilling exchange rate



Source: Central Bank of Kenya (Various)

Figure 1.15: Diaspora remittances to Kenya (US$ millions)



Source: Government of Kenya (2010a)

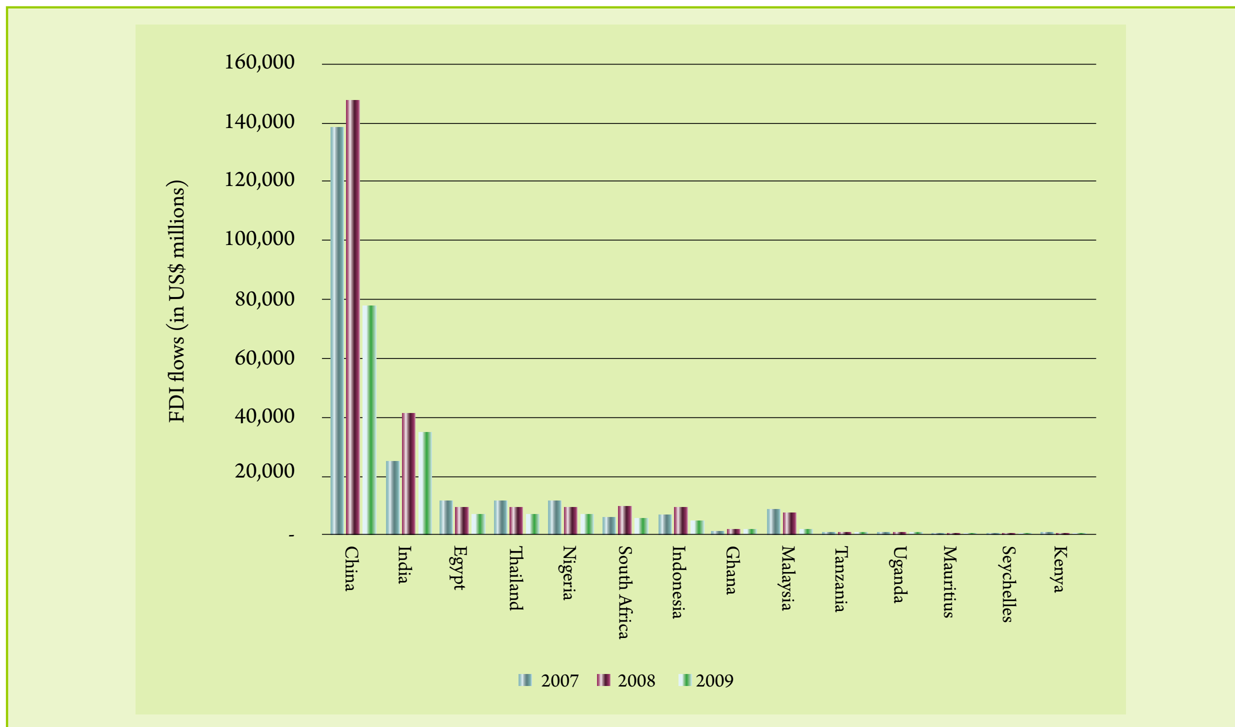
1.8.4 Foreign Remittances

The source markets for remittances have, on average, maintained the same shares with North America contributing 53 per cent and Europe 26 per cent of total remittances to Kenya in November 2010. Remittances have grown strongly since 2006 (Figure 1.15). Most of the remittances improve household disposable income and, therefore, increase consumption.

1.8.5 Foreign Direct Investment

Foreign Direct Investment (FDI) more than doubled between 2008 and 2009 (Table 1.6). However, Kenya is still among the countries that received the lowest FDI in both Africa and among other developing countries. The low level of FDI in 2008 could have been a result of the post-election violence that erupted immediately after the 2007 elections. However, the economy did well to rebound in 2009, and the country should be able to continue optimizing its capability of attracting more FDI. Among the factors that affect FDI flows include the macroeconomic environment as well as institutional factors such as observance of law and order, political stability, and corruption. Thus, more effort is needed in ensuring macroeconomic stability, political stability, security and law and order

Figure 1.16: FDI flows (in US$ millions)



Source: World Bank (2010)

in order for the country to improve its attractiveness as a destination for FDI.

Table 1.6: Foreign direct investment flows (US$ millions)

	2007	2008	2009
China	138,413.00	147,791.00	78,192.73
India	25,127.16	41,168.61	34,577.00
Egypt	11,578.10	9,494.60	6,711.60
Thailand	11,323.99	8,570.12	5,955.60
Nigeria	6,033.00	4,876.44	5,786.68
South Africa	5,736.93	9,644.83	5,628.09
Indonesia	6,928.48	9,318.45	4,877.37
Ghana	970.38	2,111.59	1,684.74
Malaysia	8,453.77	7,375.91	1,609.31
Tanzania	646.97	744.02	645.00
Uganda	792.31	728.86	603.75
Mauritius	340.76	377.72	256.68
Seychelles	249.31	241.44	248.57
Kenya	729.04	95.59	140.52

Source: World Bank (2010)

1.9 Medium Term Prospects

1.9.1 Macroeconomic Prospects

As is the case with the world economy, the Kenyan economy was on a recovery path in 2010, recording an impressive growth rate of 5.6 per cent. There were severe multiple shocks in 2008 whose impact was slightly muted in 2009, with an economic performance of 2.6 per cent being recorded. This economic recovery is expected to continue and remain above the 2008/09 performance. However, the final outcome will depend on both domestic and external factors, and the policy response by the government. The implementation of the new Constitution, political reforms that include the 2013 general elections, macroeconomic stability and the effective implementation of the Medium-Term Plan (MTP) of Vision 2030 are part of the key domestic factors. Weather conditions remain an important determinant of agricultural performance and inflationary outlook. The relevant external factors include the pace and composition of the global economic recovery and growth, trends in crude oil prices and stability in the neighbouring countries.

1.9.2 Recent Economic Performance and Estimates for 2011

The economic recovery that started in 2009 continued in year 2010 with a growth rate of 5.6 per cent. The four quarters in 2010 recorded impressive growth rates with the first quarter having 4.5 per cent, second quarter at 4.6 per cent, third at 5.7 per cent and the fourth quarter with the highest at 7.2 per cent. The first three quarters of 2011 have shown a continued recovery though at a lower speed than expected. The first quarter had 4.9 per cent, the second had 4.3 per cent and in the third quarter, a paltry 3.6 per cent growth was registered. The fourth quarter is expected to register a relatively strong performance due to better short rains. The average growth for the three quarters is 4.3 per cent. Given the expected good performance in the fourth quarter, the overall annual growth for 2011 is estimated at around 4.5 per cent, which is, however, lower than the growth recorded in 2010.

All the sectors performed quite well and registered positive growth rates for all the three quarters in 2011. However, some sectors recorded low growth rates in the third quarter, such as the manufacturing sector, which registered 1.1 per cent growth, public administration had 1.1 per cent and wholesale and retail trade recorded 1.3 per cent growth.

The sectors that recorded strong growth over the third quarter of 2011 include construction, mining and quarrying, financial intermediation, fishing, and agriculture and forestry with growth rates of 6.9, 6.4, 6.0, 4.9 and 4.8 per cent, respectively. The growth in value addition in financial intermediation was supported by the modern technology of money transfers through mobile phones and increased lending, as a result of the easing monetary policy to support growth.

The overall average inflation rate for 2011 is estimated at 14.0 per cent, reflecting high inflationary pressures during the year. This performance is attributed to drought during half of the year, high oil prices, depreciation of the shilling and high domestic demand as the government continued to pursue a loose monetary and fiscal policy.

1.9.3 Medium Term Outlook

The medium term outlook hinges on smooth implementation of the Constitution and effective implementation of the MTP 2008-2012. It is also critical that the government restores and maintains macroeconomic stability. The MTP and Vision 2030 targets include real GDP growth of 10 per cent by 2012/13 and supported by robust sectoral growth performance. Implementation of Vision 2030 flagship projects is expected to continue.

The economic recovery is expected to continue in the medium term but below the MTP targets. In the medium-term, the economy is projected to grow at 4.5 per cent, 5.2 per cent, 5.8 per cent and 6.6 per cent in 2011, 2012, 2013 and 2014, respectively. This recovery is pegged on favourable international environment, effective implementation of the medium term policy agenda and favourable weather conditions. In the projections, it is assumed that international oil prices will remain stable in the medium term.

Table 1.7 summarizes the key macroeconomic variables for the years 2009, 2010, 2011 and three-year forecasts.

Table 1.7: Optimistic scenario – macroeconomic projections for 2012-2014

Variable	2009	2010	2011	2012	2013	2014
GDP growth	2.6	5.6	4.5	5.2	5.8	6.6
Inflation overall	9.0	4.0	14.0	10.0	7.0	5.0
Private consumption growth	5.0	1.0	0.8	4.0	6.0	7.0
Private investments growth	1.0	4.0	3.0	6.0	10.0	13.0
Government consumption growth	6.0	10.0	7.0	8.0	7.0	8.0
Government investment growth	8.2	5.0	9.0	12.0	9.0	10.0
Exports of goods and services	-9.1	16.0	16.0	8.0	7.0	9.0
Imports of goods and services	0.4	4.0	6.0	8.0	10.0	12.0
Financial deficit as % of GDP	-5.4	-6.5	-6.4	-6.4	-5.8	-5.7
Public expenditure as % of GDP	31.0	33.9	33.0	31.8	30.6	30.2

Source: Projections based on KIPPRA-Treasury Macro Model (KTMM)

The average overall inflation for 2011 is 14.0 per cent as compared to 4.1 per cent recorded in 2010. Stability in international oil prices and prudent fiscal and monetary policies are expected to yield single digit inflation levels of about 7.0 per cent in the medium term. Improved food production and favourable weather conditions are crucial for any future overall price stability, since food commodities account for a big share in the consumer basket.

The assumptions underlying the fiscal framework are consistent with the Budget Strategy Paper and adjustments to reflect actual budget implementation. Public expenditure as a percentage of GDP is still high at 33 per cent in 2011. In terms of real growth in government expenditure, consumption and investment for 2011 are expected to average about 7 per cent and 9 per cent, respectively. Similarly, investment is expected to be high due to increased construction activities especially on infrastructure and as implementation of the planned development programmes as contained in the Medium Term Expenditure Framework gain momentum. In the years 2012, 2013 and 2014, both consumption and investment are expected to stabilize but at high

levels supported by a relatively strong economic environment.

The tourism sector is expected to stabilize and continue to grow at an annual average of 12 per cent. This growth is expected to be supported by vigorous marketing of Kenya as best tourist destination, and political and economic stability at home. This is expected to boost exports in the medium term and support economic growth outcomes. Imports are expected to expand with the economic growth. The projected positive growth for Sub-Saharan Africa at 5.5 per cent for 2011 and 5.8 per cent for 2012 is expected to provide an impetus to private investments for the recovery process.

With the expansion of the economy expected in the medium term, imports growth is expected to continue and is projected to grow at 6 per cent, 8 per cent, 10 per cent and 12 per cent for 2011, 2012, 2013 and 2014, respectively. The import volume growth will be occasioned by the need to complement domestic production, purchase of intermediate and capital goods and purchase of oil and oil-related products.

However, it is expected that commitment to reform will remain strong, especially in maintaining macroeconomic stability, deepening structural reforms and strengthening key institutions such as the Judiciary and security. This will provide a good background for investor confidence and thus support stability and an improved investment climate. However, there are some challenges and uncertainties that might strongly impact medium term prospects, key ones being weather conditions, slow implementation of the Constitution, any occurrences in the international economy, and regional stability. An alternative scenario is, therefore, presented in Table 1.8, showing projected GDP growth of 4.7 per cent in 2012 and a moderate rate expansion in 2013 to 2014. The forecasts are based on the assumptions that high inflation rate continues in 2012 due to supply constraints, weakening of the Kenya shilling against the US dollar, and slowdown in the global economy. Investors might also take a 'wait and see' stance during the election year. As a result, some potential investors may fail to take advantage of the investment opportunities that exist in the country.

Table 1.8: Economic projections for 2012-2014 (Alternative scenario)

Variable	2009	2010	2011	2012	2013	2014
GDP growth	2.6	5.6	4.5	4.7	4.9	5.1
Inflation overall	9.0	4.0	14.0	12.0	9.0	9.0
Private consumption growth	5.0	1.0	0.8	3.0	5.0	5.0
Private investments growth	1.0	4.0	3.0	5.0	11.0	13.0
Government consumption growth	6.0	10.0	7.0	8.0	7.0	8.0
Government investment growth	8.2	5.0	9.0	14.0	12.0	14.0
Exports of goods and services	-9.1	16.0	16.0	10.0	6.0	9.0
Imports of goods and services	0.4	4.0	6.0	9.0	11.0	13.0
Financial deficit as % of GDP	-5.4	-6.5	-6.4	-6.6	-6.1	-6.4
Public expenditure as % of GDP	31.0	33.9	33.0	31.8	30.8	30.6

Source: KIPPRA Staff Estimates based on the KIPPRA-Treasury Macro Model (KTMM)

Slow uptake of the public-private partnership (PPP) initiative in the implementation of MTP strategies may lead to a slower rate of economic expansion than envisaged in Vision 2030. Also, the weak implementation of the budget can adversely

affect growth in the medium term. Table 1.8 shows economic projections reflecting downside risks.

ENDNOTES

1. **Ordinary revenue** is composed of both tax and non-tax revenue. Taxes are compulsory payments collected by the government to finance its operations, while non-tax revenue includes rent from buildings, fees, fines and operating surpluses from public enterprises.

2. **Appropriations-in-Aid (A-I-A)** encompasses funds that do not go through the exchequer and may include some loans, grants and internally generated revenue by state agencies.

3. **Grants** are voluntary payments made by foreign governments, international organizations and individuals. They may take the form of cash grants, programme grants or Appropriations-in-Aid. Grants are, therefore, the transfer of financial resources to Kenya's Treasury by other countries or agencies, following mutual agreement but without any conditions for repayment. Grants differ from revenue since grants are neither predictable nor sustainable.

4. Includes disbursements (programme cash loans, project cash loans, A-I-A), rescheduling, change in arrears, repayment of arrears, less repayment due.

5. Includes domestic borrowing, privatization proceeds, bank restructuring costs and financing.

Chapter 2

Strengthening Public Expenditure Management

2.1 Introduction and Background

The implementation of the Constitution of Kenya 2010 offers opportunities as well as challenges in strengthening expenditure and macroeconomic management. The Constitution of Kenya 2010 provides for wide-ranging reforms and establishment of new institutional and governance structures. These have important implications for public expenditure and macroeconomic management in Kenya. They include:

1. Devolution, which leads to creation of county governments, county revenue funds and distribution of functions between the national and county governments.

2. Principles of public finance enshrined in the Constitution (Chapter 12), which include openness and accountability, public participation and equitable development. Establishing appropriate institutions and reforms that support these constitutional principles requires immediate policy attention.

3. Other structures such as Equalization Fund, Judiciary Fund, Commission on Revenue Allocation (CRA), Controller of Budget, Salaries and Remuneration Commission and an independent Central Bank of Kenya.

This chapter reviews Kenya's public expenditure and macroeconomic framework within the context of the Constitution of Kenya 2010. Public expenditure management is concerned with the determination of the needs and aspirations of the society and the deployment of resources (manpower, money, materials and institutional arrangements) for meeting those needs and goals. The key aspects include expenditure planning (translation of policies into budgetary

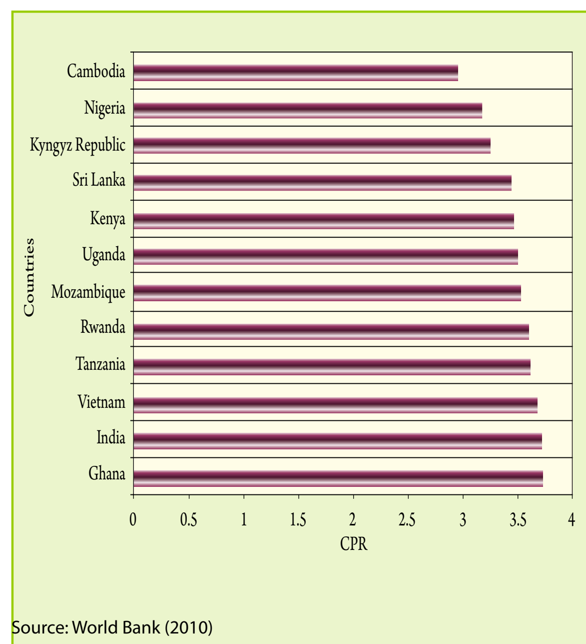
decisions), budget execution, external oversight and design and implementation of policies that support the achievement of public expenditure management goals. The three broad objectives of public expenditure management are to ensure macroeconomic stability through enhanced overall expenditure discipline and control, allocation of resources towards the nation's priorities, and ensuring 'value for money' or operational efficiency. The quality of the macroeconomic framework and public expenditure institutions should support stability, equity and economic growth.

2.2 Review of Recent Institutional Reforms in Public Expenditure Management and Performance

Recent reforms in public expenditure management (PEM) have aimed at enhancing the link between policy planning and budgeting, strengthening transparency and accountability, combating corruption in PEM and improving operational efficiency through introduction of results-based management in the public service. The key reforms include: introduction and strengthening of the Medium Term Expenditure Framework (MTEF), introduction of Integrated Financial Management Information System (IFMIS), and strengthening of the legal framework for PEM by enacting relevant pieces of legislation such as the Government Financial Management Act 2004, Public Audit Act 2003, Public Procurement and Disposal of Assets Act 2005 and the Fiscal Management Act 2009. The government launched the Strategy for the Revitalization of Public Financial Management System in Kenya (2006-2011) to guide reforms in financial management. Other reforms include establishment of a National Integrated M&E system, and various amendments to the Central Bank Act to enhance operational effectiveness, including the establishment of a Monetary Policy Committee responsible for monetary policy formulation.

While Kenya has made commendable progress in strengthening institutions for public expenditure management, its rating on Country Policy and Institutional Assessment (CPIA)[1] reveals that there is substantial scope for improvement. Based on the most recent published data, the country performance rating for Kenya in 2009 was moderately low. The CPIA shows that Kenya performed moderately high on the economic management (4.2) and structural policies (4.0), compared to moderately low performance on policies for social inclusion and equity (3.5), and public sector management and institutions (3.3).

Figure 2.1: IDA country performance ratings (CPR), 2009



Source: World Bank (2010)

Certain countries outperform Kenya, including East African Community members (Uganda, Tanzania and Rwanda) and others such as India and Vietnam. There is, therefore, a case for strengthening Kenyan institutions to enhance public service delivery and create a conducive environment for private investment and growth.

2.3 Review of Current Policy Formulation

While various institutions and stakeholders are involved in policy formulation, three institutions, namely: Ministries of Finance; Planning, National Development and Vision 2030; and the Central Bank of Kenya (CBK), play a leading role in macroeconomic policy formulation and management. The Ministry of State for Planning, National Development and Vision 2030 is incharge of medium and long-term planning as well as monitoring and evaluation of national development. The Constitution, Government Financial Management Act 2004, and the Fiscal Management Act 2009, provide the Treasury with the authority to formulate and implement fiscal policy. The CBK, through the Central Bank Act, has operational independence in the formulation and implementation of monetary policy. Besides, there are 42 ministries responsible for coordinating and implementing sectoral policies.

Kenya's long-term development goals are outlined in Vision 2030, whose aim is to transform Kenya into a newly-industrializing middle income country by 2030. The Vision is being implemented through five-year medium term plans. The first Medium Term Plan (MTP) covers the period 2008-2012. The MTP is in turn implemented through three (3) year Medium Term Expenditure Framework (MTEF) budget. In addition, there are Vision 2030 Sector Plans and Ministerial Strategic Plans that inform planning and budgeting for national development goals (Table 2.1). At the sub-national level, District Development Plans have been the basis for planning and linking or ensuring consistency between national and sub-national planning.

The planning framework is faced with various challenges, key among them the weak links between the MTP and the MTEF, and weak sub-national planning frameworks. Sub-national level participation in the MTEF is hampered by lack of an appropriate legal framework.

Table 2.1: Kenya's planning framework

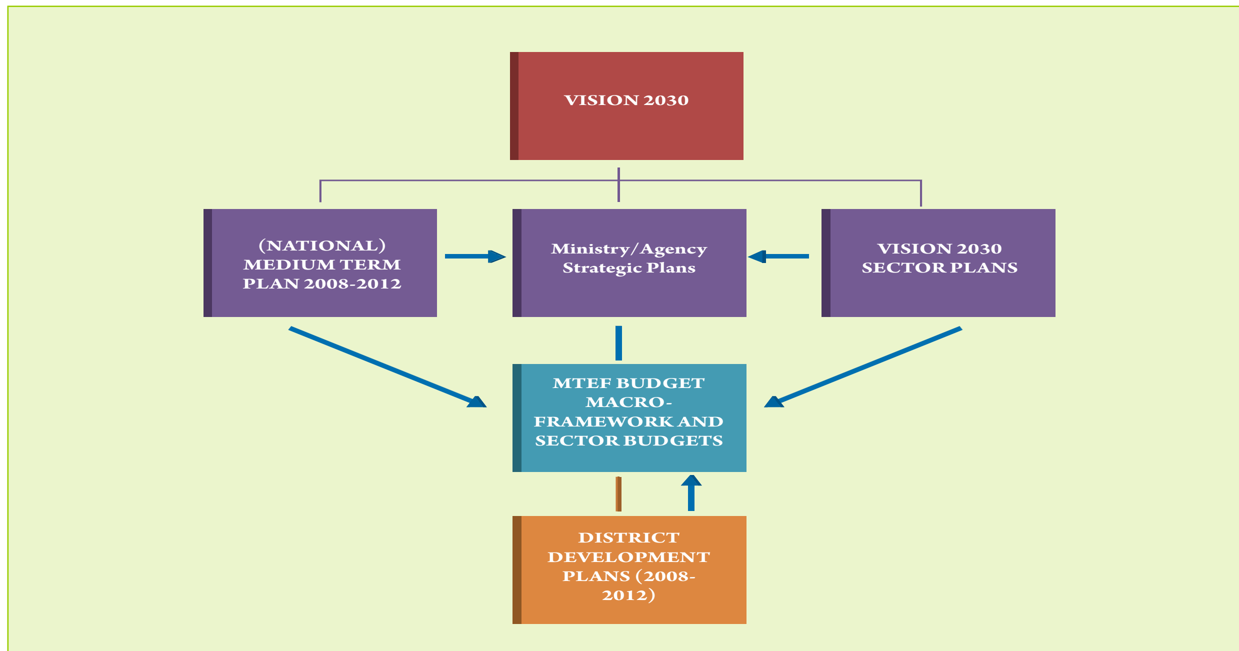
National Level	Key Elements
Kenya Vision 2030	Framework for long-term development to transform Kenya into a middle income country by 2030
Medium Term Plan	Implement Vision 2030 through 5-year rolling plans (1st Plan covers period 2008-2012)
Vision 2030 Sector Plans	Detailed Vision 2030 sector requirements, including flagship projects
MTEF	Comprises of a macroeconomic policy framework (Budget Outlook/Strategy) and MTEF sector reports that link policy to budget expenditure and management decisions

The adoption in 2000 of the Medium Term Expenditure Framework (MTEF) was an important step towards strengthening the link between budget, policy and planning. The Kenyan MTEF model includes a public expenditure review process, a macroeconomic spending framework, sector policy prioritization, and public sector hearings that enhance stakeholder participation. Although there have been reforms on the MTEF to enhance outcomes, participation at the sub-national level has been limited.

The budget formulation process begins with the issuance of a Treasury circular to all accounting officers. The circular provides guidelines for the preparation process and the time frame. Public Expenditure Review (PER) is now part of the budget process. PER involves a diagnostic review of the structure of expenditure and composition that supports policy.

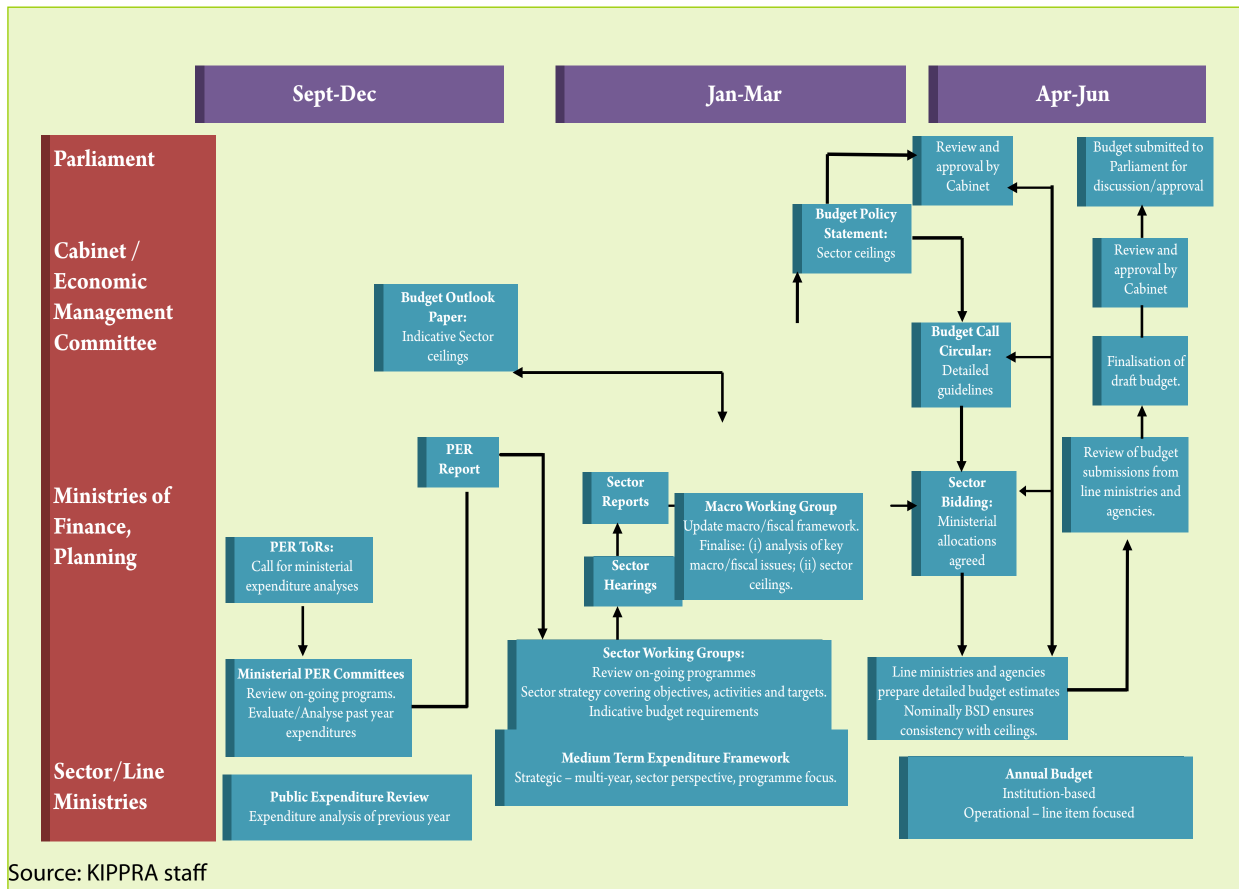
Table 2.2 summarizes public financial management performance for Kenya based on the Public Expenditure and Financial Accountability Assessment Framework (PEFA) in areas that did not show much improvement in the intervening periods.

Figure 2.2: Linkages between various national planning processes



Source: KIPPRA staff

Figure 2.3: The PER, MTEF and budget preparation cycle in Kenya



Source: KIPPRA staff

Table 2.2: Kenya's public financial management (PFM) performance

	Summary of PFM performance scoring	Score 2006	Score 2008
A	*Credibility of the Budget*		
1.	Composition of expenditure outturn compared to original approved budget	A	B
2.	Stock and monitoring of expenditure payment arrears	B	B
B	*Comprehensiveness and Transparency*		
3.	Classification of the budget	C	C
4.	Comprehensiveness of the information included in the budget documentation	B	B
5.	Extent of unreported government operations	D+	D
6.	Transparency of inter-governmental fiscal relations	B	B
7.	Oversight of aggregate fiscal risk from other public sector entities	C	C
8.	Public access to key fiscal information	B	B
C	*Budget Cycle*		
C(i)	*Policy-based Budgeting*		
9.	Orderliness and participation in the annual budget process	B	C+
10.	Multi-year perspective in fiscal planning, expenditure policy and budgeting	C	C+
C(ii)	*Predictability and Control in Budget Execution*		
11.	Effectiveness in collection of tax payments	D+	D+
12.	Predictability in the availability of funds for commitment of expenditures	B+	B+
13.	Recording and management of cash balances, debt and guarantees	B	B
14.	Competition, value for money and controls in procurement	B	B
15.	Effectiveness of internal controls for non-salary expenditure	C	C
C(iii)	*Accounting, Recording and Reporting*		
16.	Timeliness and regularity of accounts reconciliation	C	C+
17.	Availability of information on resources received by service delivery units	B	D
18.	Quality and timeliness of in-year budget reports	C+	C+
19.	Quality and timeliness of annual financial statements	D+	D+
C(iv)	*External Scrutiny and Audit*		
20.	Legislative scrutiny of annual budget law	D+	D+
D	*Donor Practices*		
D-1	*Predictability of direct budget support*	*D*	
D-3	*Proportion of aid that is managed by use of national procedures*	*D*	

Source: PEFA (2009)

2.4 Implications of the CoK 2010

Article 220(2) of the Constitution of Kenya 2010 requires that 'National Legislation shall prescribe (a) the structure of the development plans and budgets of counties'...(c) the form and manner of consultations between the national government and county governments in the process of preparing plans and budgets. It is, therefore, expected that such legislation will provide a framework for county governments to prepare plans or strategies consistent with medium term plans and/or Vision 2030 goals.

Article 225 provides for the establishment of a national treasury. The Ministries of Finance and Planning play a critical role in coordination of inter-ministerial policy formulation, implementation and evaluation. In the envisaged reorganization of the government, Article 152 (1) d provides three options that could be considered: namely, forming a super ministry responsible for both budget and planning; retaining the two ministries separately but with enhanced coordination through formal mechanisms such as committees and taskforces created by law or administrative orders sanctioned at the cabinet level; or creating a planning commission. It is important to note that in the past, mere merging

of the two ministries without changes in the basic rules and procedures did not help enhance policy formulation and coordination.

In the third option, the Ministry of Planning could be replaced with a Planning Commission that will support and coordinate the planning function at the national and county government levels towards the goals of Vision 2030.

The establishment of a national treasury might also necessitate a review of the current organization of the Ministry of Finance with a view to aligning the functions to reflect the responsibilities and functions that take into account devolution and establishment of new constitutional offices, such as the Commission on Revenue Allocation, and Controller of Budget.

According to Article 152 (1) d, the cabinet shall consist 'not fewer than fourteen and not more than twenty-two Cabinet Secretaries'. The dominant principle in establishing ministries or departments together with other supporting units is functionality (e.g. Health, Defence, Education) with various functions grouped together based on criteria such as non-fragmentation and non-overlap. The other principles used include area principle (e.g. Ministry of State for Northern Kenya), client principle (e.g. Ministry for Youth Affairs), and process principle (e.g. Ministry of Public Works staffed with engineers). In addition to the above principles, ministries may be established to reflect new policy thrusts. These criteria will be useful during the reorganization of government as envisaged under Article 152 (1) d so as to facilitate effective policy formulation and coordination. A systematic review of the functions and organization of the grand coalition government may be advisable.

Article 220(2) provides for preparation of County Development Plans. During the month of May 2011, the government released a medium-term review of the MTP. A review of the district development planning has not been undertaken. It is recommended that such a review be undertaken as a first step towards development of County Development Plans as stipulated in Article 220(2).

According to Article 173(3), the Chief Registrar 'shall prepare estimates of expenditure for the following year, and submit them to the National Assembly for approval'. The general practice has been that the Judiciary has been submitting the budget to Treasury. This new arrangement enhances the autonomy of the Judiciary. However, if not well managed, it could entail potential risks to aggregate expenditure control and macroeconomic stability. In this regard, it would be useful to establish a framework for budget negotiations and formulation involving Treasury so that the Judiciary budget is within limits that are consistent with a stable macroeconomic environment, and is subjected to sufficient prioritization and public participation.

The Fourth Schedule provides the distribution of functions between the national and county governments. In designing grant transfer systems, it will be critical to examine and explore the use of the grant in filling fiscal gaps, reducing regional disparities, setting/meeting minimum national standards and influencing local priorities, especially in areas of high national but low local priorities.

Budget Cycle: According to the PEFA assessment in 2009 (Table 2.2), practices in budget preparation had not improved especially with regard to orderliness and participation in the annual budget process. The Constitution introduces new institutions and requires participation of stakeholders. A framework, therefore, needs to be developed that plainly defines the timetable for budget preparation, clearly indicating the roles of different stakeholders and a framework for participation.

Budget Coverage: A key principle in public finance in the Constitution is transparency. Effective reporting on public expenditure allocations and utilization is supportive of transparency and accountability. While budget coverage has focussed

more on the Central government, it is now critical that coverage is enhanced and extended to the general government (including state agencies and sub-national governments). This will ensure sufficient oversight of fiscal risks and realization of the goals of public expenditure management. Reporting should include functional, economic and geographical classification. This will facilitate effective analysis of county and central government expenditure. County governments will need a sound estimate of the available resources before they can prepare their budgets. The PFM assessment appears to suggest that there are weaknesses especially with regard to unreported government financial operations.

The PEFA assessment reported earlier indicates that the PFM systems are weak, especially with regard to donor practices. Introduction of devolved governments has the potential for increasing transaction costs and undermining alignment and harmonization, if donors are to start working directly with 47 county governments without a proper framework of coordination.

Devolution and Stability: It is important that the design of the devolved public financial management systems should support macroeconomic stability. Consequently, matters related to borrowing and creation of fiscal deficits, including sufficient oversight over fiscal operations is critical. While the Auditor General has reduced the audit backlog for the Local Authorities, more needs to be done to clear the remaining audit backlogs ahead of the operationalization of county governments. Besides, it is important to establish the assets currently held by Local Authorities and Central government in the various counties, so that this does not create challenges for inter-governmental relationships and new PEM systems.

ENDNOTES

[1] The World Bank's CPIA rates countries on four broad areas, namely, economic management, structural policies, policies for social inclusion/equity and governance.

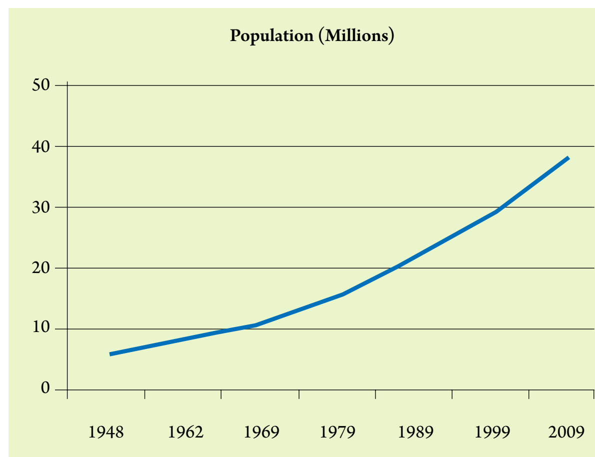
Chapter 3

Population Dynamics and Socio-economic Performance

3.1 Population Growth

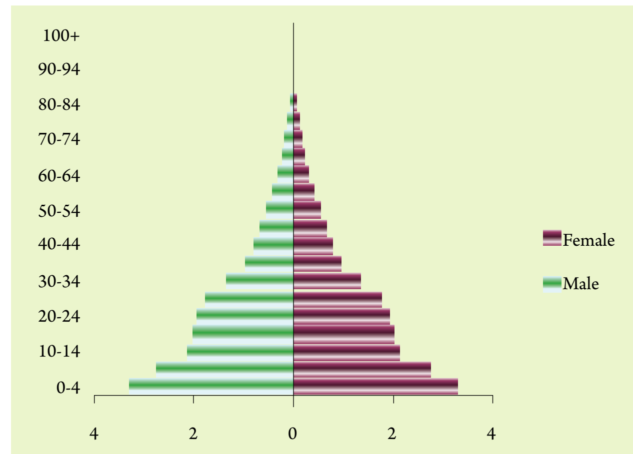
Kenya has had a sustained increase in its population since independence. According to the 2009 Population and Housing Census, Kenya's population was 38.6 million in 2009 with a sex ratio of about 1:1 and an intercensal growth rate of 2.6 per cent. The population distribution shows that 53.6 per cent of the total population is aged 15-64 years; 43 per cent is aged below 15 years and 3.4 per cent is above 64 years (Figures 3.1 and 3.2). The population is further projected to increase to 54 million in the year 2030 (US Census Bureau, 2010).

Figure 3.1: Trends in Kenya's population, 1948-2009



Source: Government of Kenya (Various), Economic Surveys

Figure 3.2: National population pyramid



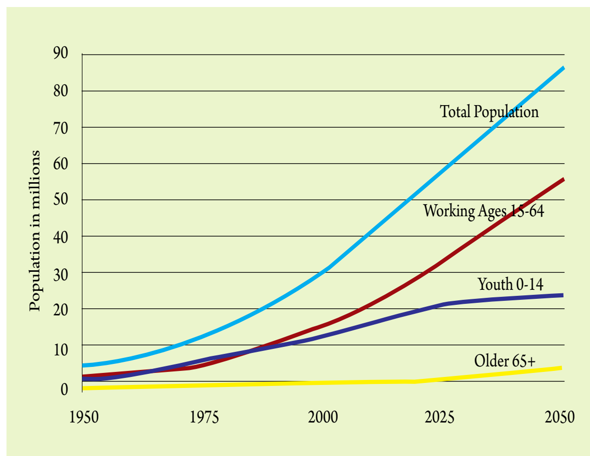
Source: Census Report (2010)

3.2 Demographic Transition

Demographic transition refers to the shift from a high fertility and high mortality equilibrium to a low mortality and fertility equilibrium. Life expectancy in Kenya is on the rise with decline in HIV prevalence rate and mortality rates. Birth rates have also declined as a result of late marriage, urbanization, industrialization, rising aspirations and other factors. These factors have brought about major demographic transitions.

With a population of 38.6 million people as per the 2009 Population and Housing Census, Kenya's rapid population growth appears to be very steady. The growth could be explained by increasing numbers of children due to high fertility rates until 2000. However, since 2000, the number of children per family has fallen sharply, from 8.1 children in 1978 to 4.6 children in 2008, and it is projected to reach 2.4 children by 2050 (United Nations, 2009). According to Fengler (2010), two reasons explain the changes in population growth. First, high fertility in previous decades has contributed to increase in formation of families in the country. Therefore, even though families are smaller, the total number of children continues to grow. Second, Kenyans are living longer. Life expectancy has been rising over time and is projected to increase to 68 years by 2050. As a result of these trends, the fastest growing population groups in Kenya are 15 to 64 years, and this constitutes the working age population (United Nations, 2009).

Figure 3.3: Kenya's demographic transition



Source: World Bank computations based on United Nations (2009)

Thus, as fertility declines and Kenyans live longer, there is likely to be a dramatic improvement in the dependency ratio; that is, the proportion of the working-age population will grow much faster than the young and elderly population groups that depend on them. This implies that Kenya is in a position to benefit from a "demographic dividend" (Fengler, 2010), especially by 2020 when this gap starts to widen (Figure 3.3).

Rapid population growth and the even more rapid urbanization that is associated with it are likely to affect Kenya's development prospects. Firstly, high urbanization is good for development. No country has ever reached high income levels with low urbanization. Secondly, population growth increases density and, together with rural-urban migration, creates higher urbanization, which is critical for achieving sustained growth.

Large urban centres have two distinct economic advantages. First, as more people interact, there is more scope for innovation. Young people need jobs, but they also create jobs. Kenya has an educated workforce and a dynamic service industry, which typically has lower barriers of entry than agriculture or manufacturing, and provides opportunities for young entrepreneurs.

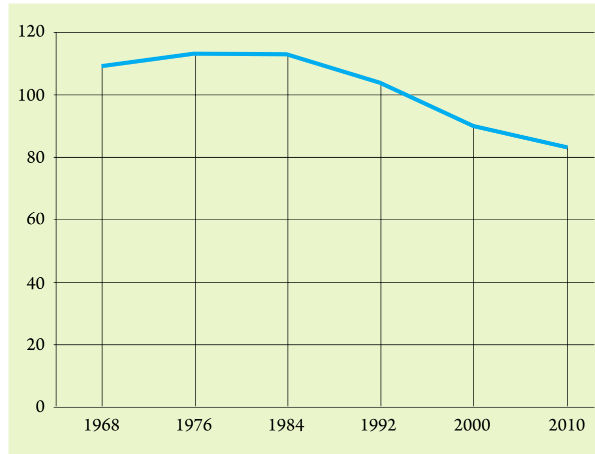
Second, larger groups of the population living in close proximity allow for economies of scale. Companies can produce goods in larger numbers and more cheaply, serving a larger number of low-income customers (Fengler, 2010). Over the past decade, Kenya has seen the emergence of a number of companies, such as in the telecommunication industry that have successfully targeted the large numbers of lower and lower-middle income groups, the "bottom of the pyramid". Their business model is viable because they can serve a multi-million customer base.

3.2.1 Dependency Ratio

The most recent human development reports (UNDP, 2010; 2011) indicate that Kenya's dependency ratio for 2010 stood at 83.3 per cent down from 106.8 per cent in 1990. Age dependency ratio is the ratio of dependent-persons aged less than 15 years or 64 years or more to the working-age population (persons aged 15-64). Figure 3.4 shows historical data for age dependency ratio or

a proportion of dependents per 100 working-age population.

Figure 3.4: Historical age dependency ratio in Kenya



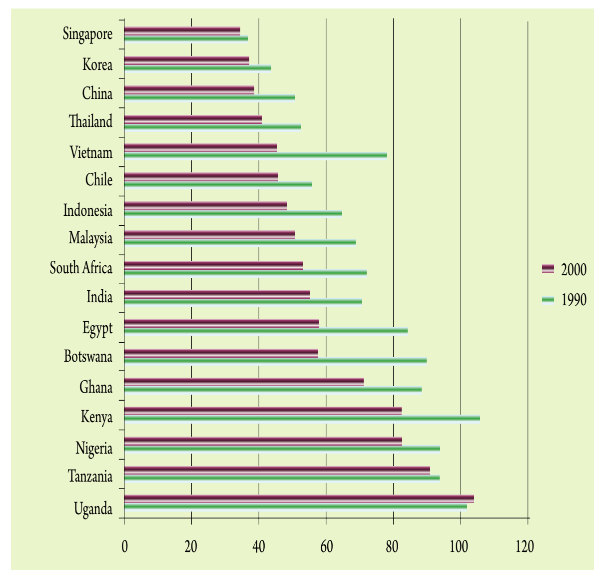
Source: World Bank (2010)

Between 1968 up to about 1990, the dependency ratio was almost constant and well above 100. However, from 1990, the dependency ratio depicted a declining trend and is now at 83. Although this is high, at least there has been good progress in this area and there are good prospects for further improvement.

However, as shown in Figure 3.5, cross-country comparisons show that Kenya's dependency ratio is among the highest in the world, despite being the lowest among the East African countries. Uganda has the highest dependency ratio, which seems to have risen since 1990. The implication of a high dependency ratio is that there is a high proportion of the population dependent on a low proportion of working population for provision of food, education, health care and other basic services.

The upward trend in population growth calls for efforts to manage it, given the pressure a high population would exert on national resources. The government together with various stakeholders has endeavoured to manage population growth through several efforts. Sessional Paper No. 10 of 1965 on African Socialism and its Application to Planning in Kenya highlighted several important issues on population. It recognized that a link existed between the country's population growth rate and its impact on socio-economic development. This awareness prompted the government to adopt an official population policy in 1967, which culminated in formation of national family planning action programmes under the auspices of the Ministry of Health. The programmes laid great emphasis on the reduction of family size and spacing of children, which was expected to contribute to reducing the population growth rate.

Figure 3.5: Dependency ratios for selected countries



Source: UNDP (2010) Initiatives for Management of Population Growth

The government established the National Council for Population and Development (NCPD) in 1982 to advise on matters pertaining to population and development. NCPD's role and mandate was contained in Sessional Paper No. 4 of 1984 on Population Policy Guidelines.

The National Coordinating Agency on Population and Development (NCAPD) was established in 2004. Under the coordinating role of NCAPD's predecessor, NCPD, Kenya's population programme registered considerable achievements that could be viewed from the two broad perspectives of policy and programme. NCPD spearheaded the updating of the 1967 National Family Planning

Policy and formulated Sessional Paper No. 4 of 1984 on Population Policy Guidelines. It subsequently reviewed Sessional Paper No. 4 of 1984 to incorporate the recommendations of the International Conference on Population and Development (ICPD) Programme of Action and came up with Sessional Paper No. 1 of 2000 on National Population Policy for Sustainable Development (NPPSD). There is also a draft National Population Policy (2011), which is expected to guide Kenya's population and development agenda over the next decade. NCPD also developed the National Plan of Action to implement the NPPSD; developed district-specific plans to implement NPPSD; and facilitated the development of national policies on adolescent reproductive health, the youth, and gender and elderly persons.

On the programme front, NCAPD attributes the attainment of the following targets to its activities: decline of population growth rate from 3.8 per cent per annum in 1979 to 3.3 per cent in 1989 and to 2.5 per cent in 1999; decline in total fertility rate from 7.7 children in 1979 to 6.7 in 1989, 5.4 in 1993 and 4.9 in 2003; and decline in ideal family size among married women from 4.4 children to 3.8 in 1998 and 3.7 in 2003. Furthermore, the maternal mortality rate declined from 590 in 1998 to 414 in 2000, but remains relatively high. The contraceptive prevalence rate (CPR) increased from 27 per cent (1989) to 33 per cent (1993) and then to 39 per cent (1998) for all married women.

Other significant developments include:

i. Development and dissemination of the National Population Policy for Sustainable Development in 1996.

ii. Revision of policy guidelines for family planning service providers to reflect the broader concept of reproductive health and family planning and standards for service providers were released in 1997.

iii. Development of the National Reproductive Health Implementation Plan for the years 1999-2003.

iv. Ensuring strengthened reproductive health service delivery systems at all levels to improve efficiency, including doubling of the numbers of community-based distributors.

v. Creating sustained demand for family planning and ensuring contraceptive commodities' security by involving all stakeholders including the community.

vi. Promoting participation of communities and the private sector in provision and financing of FP services.

vii. Increase in availability of a range of contraceptive technologies and the concomitant increase in contraceptive usage.

However, the measures for the management of population growth have centred mainly on family planning. For instance, the 1990s saw a steady increase in the use of family planning, attributed to some of the aforementioned factors. The reason for a robust population management policy centres on the fact that a rapid increase in the population may lead to unemployment problems, where the rate of population increase is much higher than the rate of job creation. As young people move up the age cohorts, and enter the labour markets, the majority end up not being economically active. This is accentuated by the fact that the age dependency ratio stands at 86.5 per cent, yet the labour markets cannot provide for the existing labour force, leading to a high percentage of Kenyans living below the poverty line.

3.2.2 Challenges of Institutional Effectiveness

There are some challenges that impede effective management of population growth, including:

i. Under-funding of reproductive health (RH) and family planning (FP);

ii. Heavy dependence on the public sector, in terms of distribution and sales, placing a burden on government and donor revenues;

iii. Poverty levels that reduce the affordability of most contraceptives offered by other agents other than the government;

iv. Large regional level inequities in availability of contraceptive methods;

v. Lack of equipment and supplies for FP and RH;

vi. Lack of basic FP services and refresher training;

vii. Stock outs of FP commodities;

viii. Lack of FP and RH knowledge;

ix. Problems of access to and availability of FP and RH services;

x. Husbands' disapproval of FP;

xi. Religious and cultural barriers to FP;

xii. Prohibitive costs of FP campaigns; and

xiii. Lifestyles that promote risky sexual behaviour among the youth.

3.3 Labour Market

This section focuses on recent labour market performance in Kenya relative to selected comparator countries. It analyzes challenges and required actions to ensure increased job creation and labour force participation in a decent work environment. Specifically, the section analyzes key aspects of the labour market, including employment and unemployment profiles, labour market developments and related institutional issues.

3.3.1 Labour Market Performance and Development

Labour force and labour participation

The size and quality of a country's labour force can potentially affect economic growth, since human capital is a vital component in the production process. Kenya's working-age population, which is made up of persons aged 15-64 years, was estimated at 19.8 million persons in 2005-2006. In the same period, the labour force participation rate, which is the ratio of total labour force to the working-age population, was 73 per cent (Table 3.1).

Table 3.1: Labour force participation and unemployment in Kenya by sex and age (%) (2005/06)

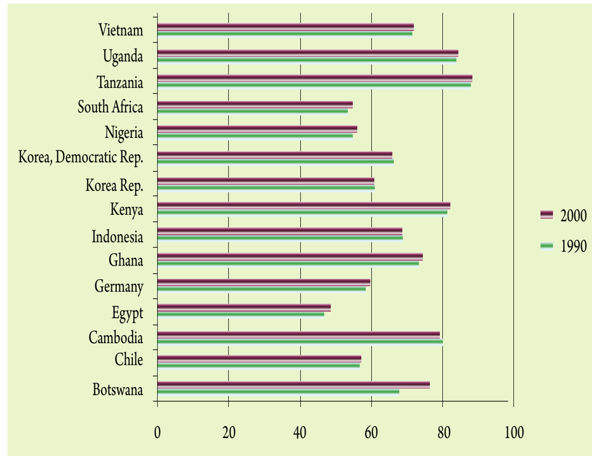
Age	Labour force participation 2005/06 (%)			Unemployment 2005/06 (%)
	Male	Female	Total	
15 – 19	30	30	30	**25.0**
20 – 24	73	68	70	**24.2**
25 – 29	93	82	87	**15.7**
30 – 34	97	86	91	**7.5**
35 – 39	98	90	94	**7.6**
40 – 44	98	90	94	**6.4**
45 – 49	96	89	92	**5.7**
50 – 54	93	85	89	**4.7**
55 – 59	92	82	87	**4.0**
60 – 64	89	76	82	**2.5**
Total	**76**	**70**	**73**	**12.7**

Source: Government of Kenya (2008)

Kenya's labour force participation rate increased to 82 per cent in 2009 (ILO, 2010) and continues to exhibit a divergent trend in its components with that of the males (88%) being higher than that of the females (76.3%). However, increases in female participation rates are expected given continuing changes in the social acceptance of female workers and the greater availability of childcare services. Among the East African countries, Tanzania has the highest labour force participation rates (88%), followed by Uganda (84%) and Kenya (82%). The East African labour force participation rates

are among the highest, relative to the comparator countries (Figure 3.6).

Figure 3.6: Labour force participation rates across countries (%) 2008-09



Source: ILO (2010) and World Bank (2010) World Development Indicators

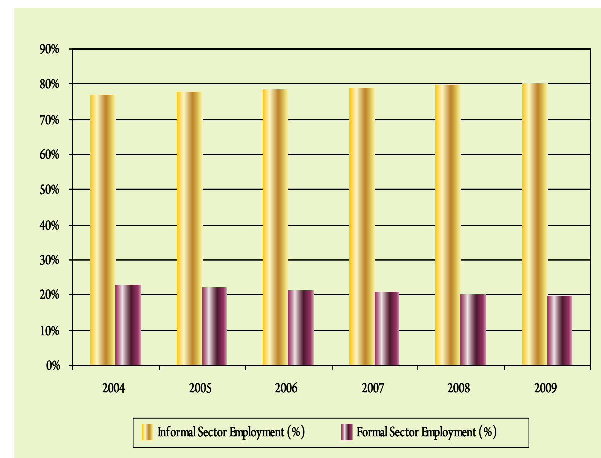
Unemployment and underemployment

The relatively low overall open unemployment rate of 12.7 per cent in 2005-06 masks high open unemployment rates for some groups, particularly the youth. The open unemployment rate among the youth aged 15-24 was nearly 25 per cent in 2005-06, about double the overall open unemployment rate (Government of Kenya, 2008). The unemployment rates among the youth can be attributed to such factors as skill mismatch and information asymmetries in the labour market. Due to information problems, individuals may acquire skills that are not demanded in the labour market. In addition to open unemployment, underemployment, which measures the percentage of workers working less than 28 hours per week, has been on the rise. In 2005-06, about one fifth of the employed persons were underemployed, while only about one in twenty was underemployed in 1999 (Government of Kenya, 2008).

Employment

According to annual employment estimates, the number of employed persons increased from 8 million in 2004 to 10.4 million in 2009. However, in 2008, there was a slowdown in employment expansion. The economy created 493,000 jobs in 2008 compared to 712,000 jobs the previous year (Government of Kenya, 2010). Among the factors contributing to the decline were the post-election violence and the global economic crisis, which stifled economic growth. Another observable trend is that most jobs created are in the informal sector. Figure 3.7 shows that the share of informal sector employment rose steadily to about 80 per cent of all jobs in 2009.

Figure 3.7: Sectoral shares in total employment (%) (2004-2009)



Source: Government of Kenya (Various), Economic Surveys

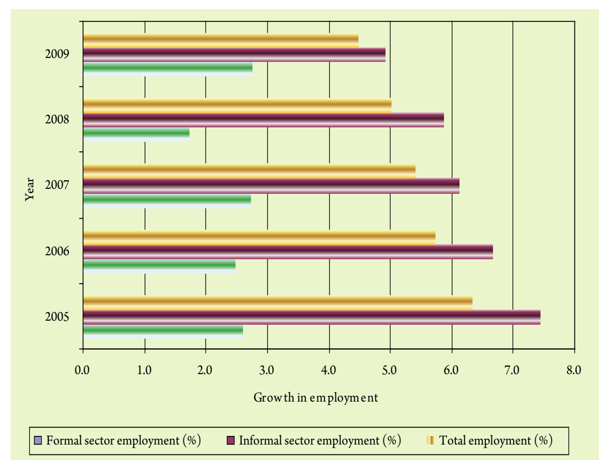
Informal sector employment

It is estimated that about 8.3 million persons were engaged in the informal sector in 2009, up from 6.2 million in 2004 (Government of Kenya, Various Economic Surveys). Informal sector employment is highest in the wholesale and retail trade and hotels and restaurants industry, which absorbed 59.1 per cent of persons employed in the informal sector in 2009, followed by manufacturing (21.1%). The expansion is a response to an institutional framework that imposes high costs to formality (Government of Kenya, 2010c). Such costs include burdensome business registration and licensing procedures and complex tax procedures. The sector has also expanded due to its potential to absorb the excess

labour supply occasioned by the failure of formal wage employment to expand at a pace that would absorb the expanding labour force.

For instance, in 2009, about 445,900 new jobs were created, out of which 88 per cent were in the informal sector. In 2005, about 506,500 new jobs were created, out of which 91 per cent were in the informal sector. This implies that in 2009, only two jobs out of every ten jobs created were in the formal sector, while the rest, about eight out of ten, were in the informal sector. Between 2005 and 2009, the informal sector grew at about 35.1 per cent while the formal sector grew at about 12.9 per cent, indicating the declining capacity of the modern economy to create employment.

Figure 3.8: Growth in formal and informal sector employment (%)



Source: Government of Kenya (Various), Economic Surveys

There are clear regional disparities in informal sector employment, with a high concentration of informal sector activities in rural areas. In 2009, 62.2 per cent of the informal activities were in the rural areas and 37.3 per cent in urban areas (Government of Kenya, Various Economic Surveys). However, these activities were concentrated in Nairobi (24.3%), Rift Valley (18.9 %) and Central Province (15.8%).

3.3.2 Labour Market Institutions

There is no single tight definition of what labour market institutions encompass. International Labour Organization–ILO (2008) considers labour market institutions to range from formal labour market regulations and policies to informal values and norms, as well as labour markets as institutions in themselves. Common specific examples of labour market institutions include: minimum wages and wages in general, unions and collective bargaining, and employment laws and regulations. Other examples of institutions are: temporary employment contracts, social dialogue, apprenticeship programmes, and equal employment legislation and so on.

Recent developments and performance

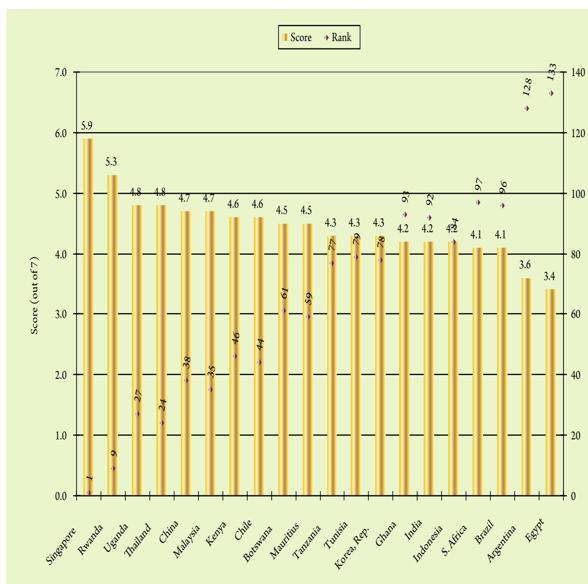
Minimum wages have been in operation in Kenya for a long time and are aimed at compensating workers for increases in the cost of living. Minimum wages in Kenya cover formal sector workers but, as seen above, most workers are in the informal sector. In addition to low coverage, evidence of low compliance implies that minimum wages are unlikely to hinder job creation in Kenya. Currently, the aim of the government is to move towards use of productivity to anchor wages. The task of establishing productivity levels and linking them to wages was given to the newly-established Productivity Centre of Kenya.

Employment laws form another important institution in the labour market. Rigid employment laws and regulations can generate labour market inefficiency. Kenya enacted new labour laws recently. These are (i) The Labour Institutions Act, 2007; (ii) The Employment Act, 2007; (iii) The Labour Relations Act, 2007; (iv) The Work Injury Benefits Act, 2007; and (v) The Occupational Health and Safety Act, 2007. It is too early to make an assessment of the new labour laws given that the laws are yet to be fully implemented. However, the implementation of these laws faces a number of challenges. First, a balance between the need for economic efficiency and the need for worker protection is not easy to strike. Second, the Ministry of Labour does not have

adequate capacity to make the laws operational. For example, there are not enough inspectors to conduct inspections envisaged in the Occupational Health and Safety Act. These challenges must be dealt with to ensure that the laws do not erode Kenya's competitiveness.

The Global Competitiveness Index (GCI) (2010-11) has labour market efficiency as one of its 12 pillars. The GCI (2010-11) indicates that Kenya's labour market is relatively efficient with a score of 4.6 out of 7 for labour market efficiency and a rank of 46 out of 139 countries. Ten sub-indices are used to generate the labour market efficiency index and some of these include: cooperation in labour-employer relations, flexibility in wage determination, hiring and firing practices, redundancy costs and the extent to which pay relates to productivity. In the previous 2009-10 report, Kenya ranked 40th out of 132 countries with respect to labour market efficiency, which was an improvement from a rank of 60 in 2007.

Figure 3.9: Labour market efficiency score and rank across countries



Source: Global Competitiveness Report (2010)

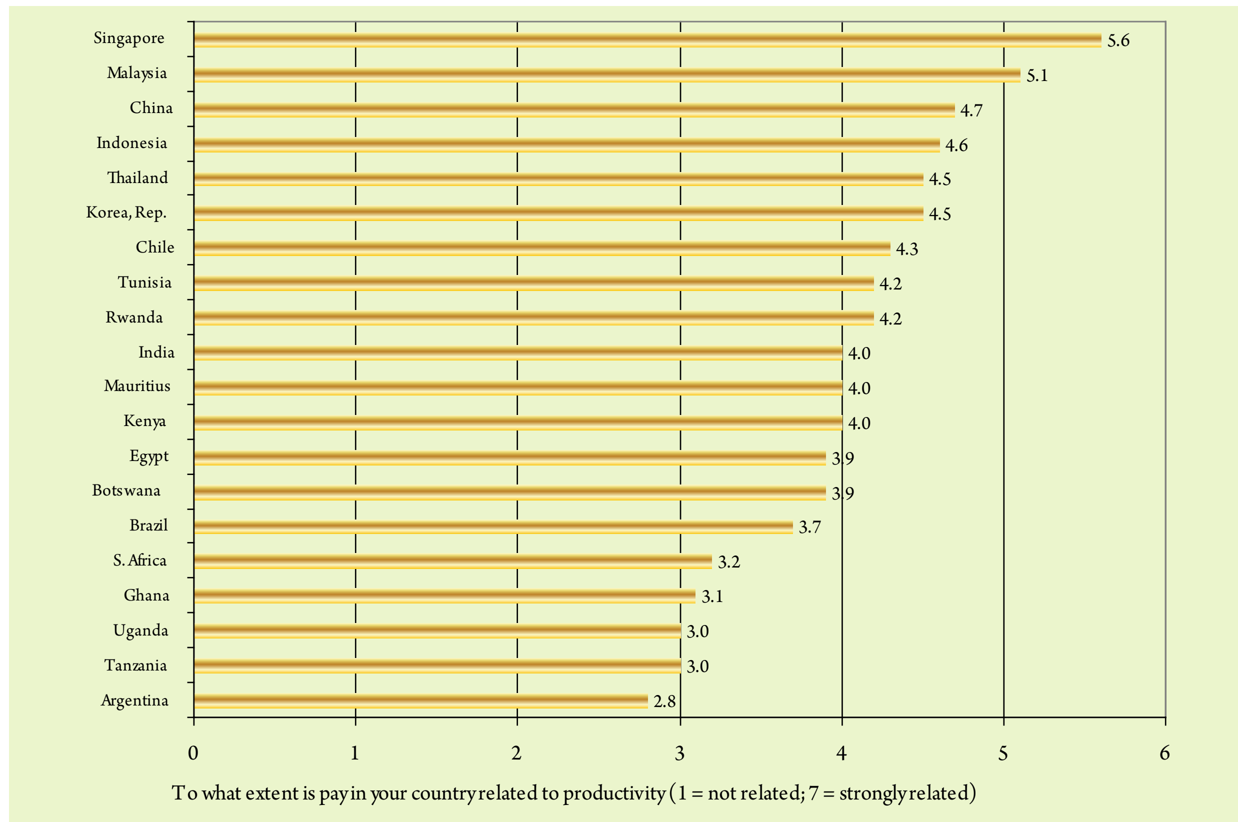
As already noted, minimum wages and wages in general are key institutions in the labour market. Specifically, the cost of labour and minimum wages has been advanced as an explanation of rising unemployment in Kenya. Minimum wages combined with job security regulations are thought to constrain employment growth by imposing excessive labour costs that discourage businesses from hiring more workers. However, as indicated in Figure 3.10, the GCI (2010-11) indicates that Kenyan executives perceive that pay is fairly related to productivity and may not support the notion that formal sector wages are too high. Kenya ranks 37 in the rigidity of employment index, indicating that labour market regulations are less rigid than in most comparator countries. In addition, Kenya fares relatively well in hiring and firing practices (12th), indicating that hiring and firing of workers is impeded little by regulations. Thus, job security regulations relating to hiring and firing are perceived as minor impediments to job creation.

Labour unions and their activities is an institution that may affect employment growth. Labour unions in Kenya have a relatively small size of union membership relative to total employment. The unions are, therefore, unlikely to be a major barrier to employment creation. Kenya's rank of 83 out of 139 in cooperation in labour-employer relations in the World Economic Forum (WEF) Executive Opinion Survey (2009/10) suggests that there is need to improve on aspects of labour-employer relations and social dialogue.

From the foregoing discussions on performance of the labour market, Kenya's labour market faces a number of challenges including: high rates of unemployment and underemployment and relatively inadequate growth in formal sector jobs. The latter is problematic since the increasing number of fresh university graduates target formal sector employment opportunities. When formal sector jobs are not forthcoming, these job seekers may resort to queue for better jobs, thus worsening the unemployment situation. The informal sector is also plagued by low productivity, hence low wages.

One of the avenues that have been proposed to circumvent the growing informal sector is the need

Figure 3.10: Pay and productivity



Source: World Economic Forum (2010)

to formalize the informal sector jobs partly by reducing the costs of formalization. As indicated, Kenya's labour market is perceived as relatively efficient in a number of areas including: flexibility in wage determination, hiring and firing practices, redundancy costs and the extent to which pay relates to productivity. Even so, Kenya remains weak in a number of indicators that would greatly undermine creation of formal jobs. These include: perceptions that the total tax rate is high, high number of procedures required to start a business and a high burden of customs procedures.

Other areas posing a challenge fall under the ambit of the institutional pillar. Important sub-indices (and rank by the GCI 2010-11) include: irregular payments of bribes (134), burden of government regulation (106), business costs of crime and violence (124), organized crime (123), and ethical behaviour of firms (117). Clearly, expanding formal sector jobs and overall employment creation will require improvements in these measures of institutional effectiveness.

3.4 Poverty and Inequality

Poverty has remained a top priority in Kenya's development agenda since independence. It manifests itself through various deprivations and associated low living standards. This section analyzes the poverty prevalence in Kenya. It focuses on various indicators, including poverty incidence and inequalities. Comparative analysis is also undertaken using a multidimensional measure of poverty, which is the most recent measure of poverty capturing both food poverty and other dimensions of deprivations.

3.4.1 Poverty Prevalence

Poverty is pervasive in Kenya. The poor in Kenya are identified as: the landless, the elderly and those with special needs, those without formal education,

orphans and vulnerable children, among others. Similarly, poverty is associated with landlessness, lack of education, prevalence of sickness and vulnerability. Poverty is also described as a rural phenomenon. It is mainly concentrated in the rural areas, where the bulk of the population (75%) resides. According to Geda *et al.* (2001), poverty is mainly found in the agricultural sector, and further findings suggest that focusing on education in general and primary education in rural areas in particular and raising income opportunities for the poor would be essential for poverty reduction.

The most recent poverty analysis based on the survey data for the KIHBS 2005/06 finds that the poor constitute about 45.9 per cent of the total population. Analysis based on the poverty projection model (Mwabu *et al.*, 2003) shows that poverty rates increased to 50.9 per cent in 2008 and declined to 49.4 per cent by the year 2010. The methodology, which is based on borrowed coefficients and growth and inequality estimates, is the basis for predicted poverty numbers in this report (Table 3.2). The most recent survey, the Kenya Integrated Household Budget Survey 2005/06 puts the national income poverty incidence at 45.9 per cent. This means that about 45.9 per cent of the 30 million people were living below the poverty line in 2005/06. While the total population increased to 38.6 million by 2009, the total number of poor people also increased significantly (19.4 million). Vision 2030 targets to reduce poverty from 46 per cent to a range of between 30 and 35 per cent by 2012.

Similarly, the trend in Table 3.2 shows that poverty remains a rural phenomenon. In 2007, rural poverty increased by 4.6 percentage points, while national poverty increased by 3.2 percentage points. In 2008, the number of poor people increased by a further 2.1 percentage points from the previous year. However, the year 2010 recorded slight improvement in the poverty headcount. The improvement is associated with improved economic growth and re-distribution policies, which are linked to various reforms.

Table 3.2: Predicted poverty headcount index, 2005-2010

Year	National	Rural	Urban
2005/06*	45.9	49.1	33.7
2005/06	46.1	50.5	29.7
2007	48.8	53.7	34.9
2008	50.9	56.5	36.2
2009	50.5	56.0	36.0
2010	49.4	54.5	35.3

** Actual poverty estimate based on survey data (KIHBS).*

Source: Poverty Projections Using KIHBS 2005/06 data

Table 3.3: Income and non-income poverty headcount, 2000-2008

Country	Income poverty headcount	Multidimensional poverty headcount
Kenya	-	60.4
South Africa	3.1	22.0
Egypt	6.4	16.7
Ghana	28.5	30.1
Uganda	31.1	-
Tanzania	35.7	65.3
Thailand	1.7	-
India	28.6	55.4
China	2.8	12.5
Brazil	21.5	8.5

Source: UNDP (2010)

The pervasive nature of poverty is a common phenomenon in most developing countries. Apart from income poverty measures, poverty could also be described as multidimensional in nature and it differs from one country to another. In terms of non-income poverty, Sub-Saharan Africa has the highest incidence of multidimensional poverty. This varies from a low of 3 per cent in South Africa to a massive 93 per cent in Niger. In Guinea, Mali and Niger, more than half of the population is poor and has experienced a child death. In addition, Burkina Faso, Burundi, Ethiopia and Mozambique have more than half of their populations poor and live in a household where no one has completed primary school. Other African countries range between 45 per cent and 69 per cent. In Kenya, non-income poverty is worse in North Eastern Province.

Nearly half of the world's multidimensional poor live in South Asia (844 million people), while more than a quarter (458 million) live in Africa (UNDP, 2010). Poverty of both income and non-income indicators has a negative effect on the overall human development index. This index is made up of measures of health, education and living standards. Despite attempts to eradicate poverty, it remains a key development challenge for most governments in developing countries, especially in Africa.

Inequality is another aspect that negatively affects both poverty and growth. This negative relationship extends to human development indicators as measured by health, education and living standards. In developed countries, public cash transfers through pensions, housing and family cash benefits, and disability and unemployment benefits supplement household income. On average, according to the Human Development Report for 2010, inequality has worsened in most countries over the years. In Sub-Saharan Africa, inequality increased substantially during the 1980s and improved during the growth period of the late 1990s and 2000s (UNDP, 2010). A few countries have begun to tackle this inequality through progressive policies such as targeted social policies. For instance, some Latin American countries, and more recently other diverse countries in Sub-Saharan Africa (Malawi, Ghana, Uganda, Tanzania and Kenya), have introduced targeted micro-based interventions such as conditional and unconditional cash transfers. While targeted transfers have proved effective in reducing poverty, they are not the only ways to tackle poverty and inequality. The processes for budget allocation and monitoring are also important. In Kenya, the recent decentralization policies have provided an opportunity for communities to be engaged in the process. There are also efforts to address underlying disparities such as regional and gender disparities.

According to the Human Development Report (UNDP, 2010), the global trend estimates for global income inequality are both mixed and controversial. One estimate shows a significant decline in income inequality, with the world Gini coefficient falling from 0.68 to 0.61 over 1970-2006, while a different study with different time frames shows that the world Gini coefficient has worsened since 1998 and now stands at 0.71. However, both schools of thought agree that income inequality in the world's population is generally very high. On the other hand, data on trends in inequality in non-income dimensions are scant, but general patterns emerge.

In health, the overall gaps between the high and low-income groups tend to be large, especially in developing countries. For instance, infant mortality is more frequent among the poorest households across all regions. In Indonesia and Nicaragua, infant deaths are more than three times more common in the poorest fifth than in the richest. In developing countries, improvements in education have increased access to education. In Egypt, between 1995 and 2000, school participation increased by 18 percentage points for girls in the poorest fifth of the income distribution.

Table 3.4: Income Gini coefficient 2000-2010

Country	Income Gini coefficient
Kenya	47.7
South Africa	57.8
Egypt	32.1
Ghana	42.8
Uganda	42.6
Tanzania	34.6
Korea, Rep.	31.6
Singapore	42.5
Malaysia	37.9
Thailand	42.5
India	36.8
China	41.5
Chile	52.0
Brazil	55.0
Argentina	48.8
United States	40.8
Japan	24.9
United Kingdom	36.0

Source: UNDP (2010)

3.4.2 Poverty Trends and Institutional Arrangements and Reforms

The human development sector has continued to receive considerable attention from most governments. In September 2000, world leaders committed the global community to halving by 2015 the proportions of the poor and hungry. They also pledged to achieve other Millennium Development Goals. Following these commitments, individual governments took it upon themselves to put in place policies and institutional reforms that would be necessary in the achievement of the MDGs.

In Kenya, despite the failure of some poverty reduction efforts, the government has continued to spearhead the fight against poverty. The current guiding policy document is Vision 2030, which articulates the various policies and reforms. The institutions encompass the formal and informal rules and customs within which individuals and firms operate; policies, on the other hand, refer to various strategies and measures a government adopts to achieve its goals and objectives within a country's institutional framework. Some of the institutions and reforms that are necessary for the achievement of Vision 2030 goals have already been implemented.

For instance, the implementation of the social protection programmes since 2003 has helped relieve the severe vulnerability that many households face. The social protection programmes, which range from giving cash to households to public works programmes, such as giving food for work, have been shown to reduce short-term poverty. However, the effects of the programmes on headcount poverty are likely to be insignificant if the programmes target the very poor with very low benefit transfer amounts. However, the impact on poverty depth and poverty severity could still be substantial even when the transfer benefits are low. The effects of these programmes are also long term and their magnitudes are linked to performance of sectors such as education and health, which are critical in eliminating long-term poverty.

In order to institutionalize this process, the government has made commendable efforts in drafting a social protection policy to guide the whole process. The main objective of the proposed policy is to create a social protection framework that benefits all citizens, and in particular, to provide support to the poor to help them access services and income-generating opportunities.

The Constituency Development Fund (CDF) is also a key institutional reform established through the Constituency Development Fund Act of 2003. The fund is an annual budgetary allocation by the central government to each of the country's parliamentary jurisdictions. In essence, the CDF provides individuals at the grassroots the opportunity to make expenditure choices that maximize their welfare in line with their needs and preferences. Since the community is better informed about their priority needs, the choices made can be expected to be more aligned to their circumstances. Nevertheless, there are increasing concerns on issues of efficiency and equity in the utilization of the funds.

The introduction of free primary education in 2003 has also seen many poor families send their children to school. Coupled with this is the school feeding programme, which benefits those schools in drought-prone regions. The programme offers meals in the schools in order to keep the children in school. Along with the free primary education is the introduction of direct transfer of education funds to schools, and provision of learning materials. Recently, the government introduced subsidized secondary education, which has enabled many poor families to take their children to school.

Despite the ongoing reforms, the government also envisages to implement many other reforms in other sectors that have direct relevance to the poverty reduction effort. These include land reforms, judicial reforms, public sector reforms, among others. The details of these reforms have been reviewed elsewhere in this report.

3.4.3 Institutional Reform Priorities over the Next Three Years

There are several reform agendas that have been identified as pathways to poverty reduction. These priorities cut across all sectors of the economy. However, priorities specific to the social pillar as outlined in Vision 2030 include increased levels of income made possible by interventions that reduce gender and regional inequalities in access to education, health and social services. The target is to raise the human development index for Kenya to about 0.6-0.7 by the year 2012 from its current level of 0.47. In addition, special welfare programmes would be provided to meet the needs of the most disadvantaged individuals and communities, in order to increase their overall welfare. The education and health sectors would also play a significant role in attaining gender and regional parity. The programme targets a primary school net enrolment rate of 95 per cent and secondary school transition rate of 80 per cent.

Similarly, a poverty reduction and reduced income disparities initiative would reduce inequalities in access to public services and income opportunities across gender, social status and regions. The target would be to reduce the national poverty index from 46 per cent to a range of between 30-35 per cent by the year 2012. The six growth sectors (tourism, agriculture, financial services, wholesale and retail trade, manufacturing, and business process offshoring) would play a key role in providing income-earning opportunities for disadvantaged groups and regions.

Another initiative is to empower local communities through increased efficiency in the use of devolved funds. The goal for 2012 is to increase the amount of devolved funds by a percentage consistent with the annual growth in government revenue. This would be achieved by increasing the amount, efficiency and impact of devolved funds and by increasing public participation and voice of the poorest members of local communities.

3.5 Health

The health sector is one of the key components of the social pillar of Vision 2030. Good health is recognized as a critical pillar in ensuring individual, household, community and country prosperity. In pursuit of population health, the government continues to give priority to access to basic health services with strong emphasis on reaching the poor. The health sector continues to emphasize the importance of re-directing resources towards preventive and promotive health care, cost effectiveness and efficiency in resource allocation and use, enhancement of public health regulations, strengthening of health institutions and fostering partnerships in health care provision and financing.

Health sector performance is presented in terms of trends in health indicators such as life expectancy and mortality, and the direct causes of morbidity and mortality, including the various disease burdens in the population. In this respect, the role played by interventions to improve reproductive and child health services are analyzed, as well as trends in health inputs in relation to health outcomes. The health inputs considered include health expenditures, health infrastructure and human resources.

3.5.1 Health Indicators

Impact indicators are a good measure of trends in the overall health of the population. The most commonly used health indicators relate to life expectancy, adult mortality rate (AMR), maternal mortality rate (MMR), under-5 mortality rate (UMR), infant mortality rate (IMR), and neonatal mortality rate (NMR). These indicators are defined as follows:

- Adult Mortality Rate (AMR): Number of deaths per 1000 adults;
- Maternal Mortality Rate (MMR): Number of women who die during pregnancy and childbirth, per 100,000 live births;

- Neonatal Mortality Rate (NMR): The probability of an infant dying within the first 28 days;

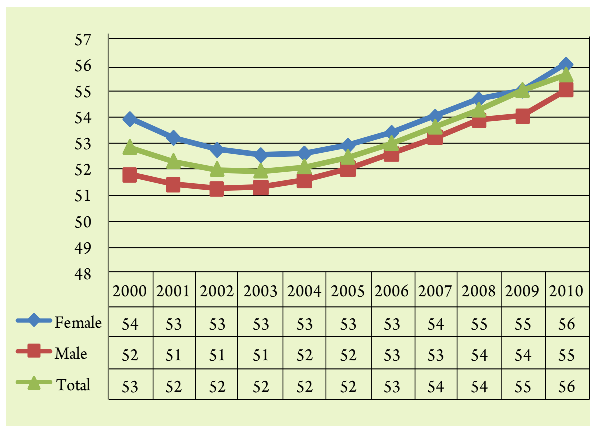
- Infant mortality rate (IMR): The probability of dying before the first birthday;

- Under-five mortality rate (UMR): The probability of dying between birth and the fifth birthday.

Trends in life expectancy

Life expectancy at birth measures the overall quality of life in a country. It can also be thought of as indicating the potential return on investment in human capital. As can be seen from Figure 3.11, life expectancy was 53 years in 2000 and fell to 52 years in 2001 where it stagnated until 2005. It then improved slightly in 2006, probably due to steady economic growth and improvement in infant and maternal mortality rates. Life expectancy rose to 54 years in 2007, but stagnated there in 2008 due to unfavourable effects of the post-election violence and drought.

Figure 3.11: Life expectancy at birth



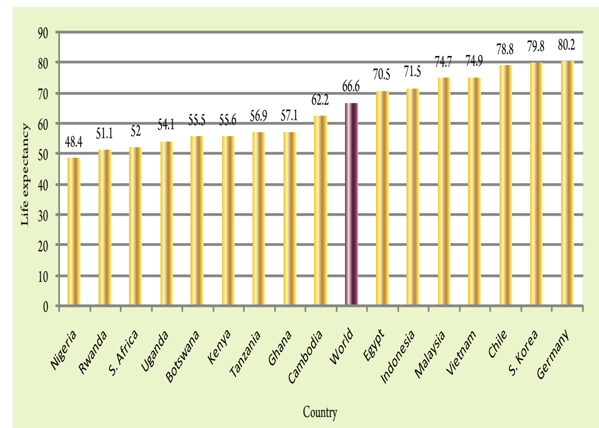
	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
Female	54	53	53	53	53	53	53	54	55	55	56
Male	52	51	51	51	52	52	53	53	54	54	55
Total	53	52	52	52	52	52	53	54	54	55	56

Source: World Bank (2010)

A closer look at life expectancy by gender reveals that the life expectancy of females has consistently been above that of males save the year 2006 when life expectancy for both males and females was at par.

A comparison is also conducted of life expectancy in Kenya with comparator countries. As of 2010, South Korea, Chile, Malaysia, Egypt, Indonesia, Germany and Vietnam had life expectancy of more than 70 years, which is more than the world average of 66.6 years. The country with the lowest life expectancy is Nigeria at just 48.4 years (World Bank, 2010). Most Sub-Saharan African countries including Kenya, saw life expectancies of their populations fall below the world average during this time. As can be seen from Figure 3.12, life expectancy in Kenya compares favourably with life expectancies in Sub-Saharan Africa and other world regions.

Figure 3.12: Life expectancy for selected countries, 2010

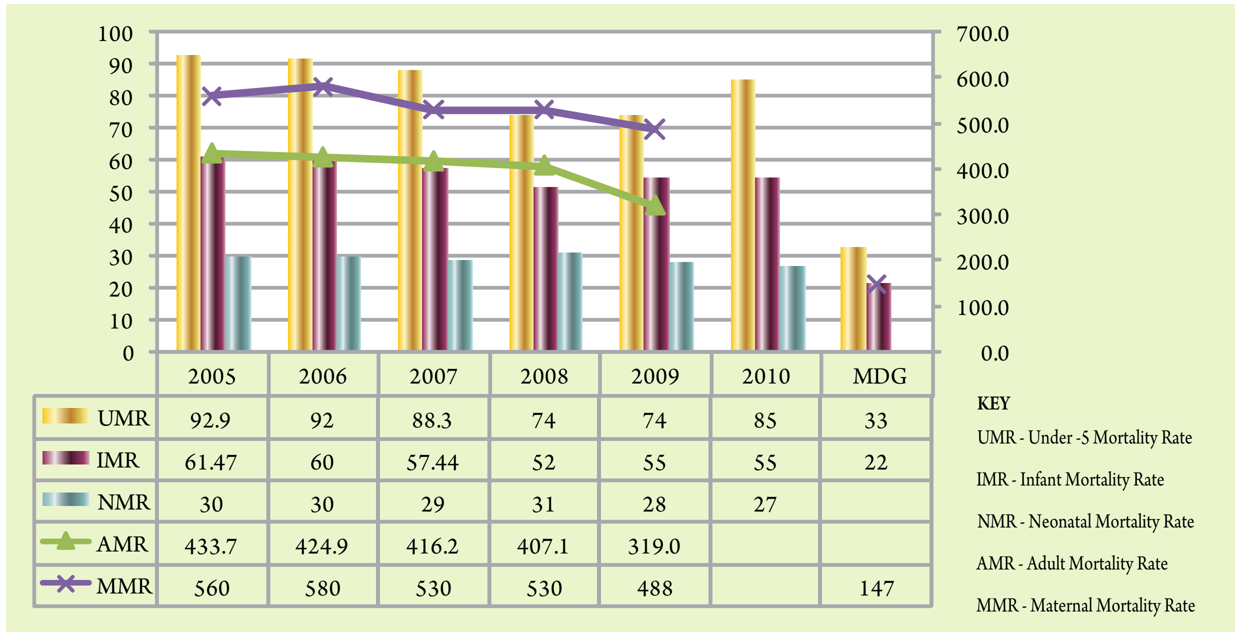


Source: UNDP (2010)

Trends in mortality rates

There have been remarkable declines in under-5 and infant mortality rates after 2005 (from 93 to 74 in 2008 and 85 in 2010, and from 61 to 55 in 2010, respectively). These gains were probably largely due to: (i) increases in immunization rates; (ii) the increased use of mosquito nets; and (iii) the positive rate of per capita economic growth in that period. Data on maternal mortality rates is elusive and non-existent in many African countries. There is no trend data on maternal mortality reported by health institutions because of poor reporting rates by these institutions. However, data available from public health facilities show that some progress has been made in reducing maternal and child mortality rates (Figure 3.13).

Figure 3.13: Trends of mortality rates

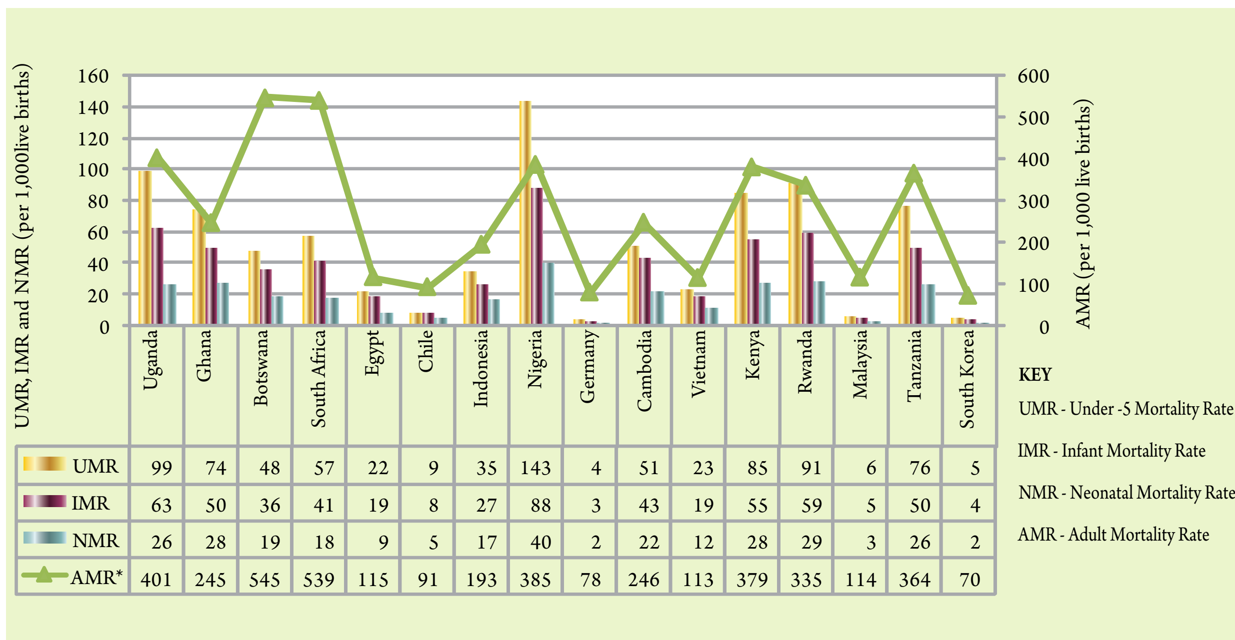


	2005	2006	2007	2008	2009	2010	MDG
UMR	92.9	92	88.3	74	74	85	33
IMR	61.47	60	57.44	52	55	55	22
NMR	30	30	29	31	28	27	
AMR	433.7	424.9	416.2	407.1	319.0		
MMR	560	580	530	530	488		147

Source: KNBS (2010) and World Bank (2011)

Figure 3.14 gives a comparison of Kenya's mortality rates in relation to selected countries in sub-Saharan Africa and elsewhere. Nigeria seems to fare the worst in all health indicators, except for the adult mortality rate where Botswana fares the worst, with 545 deaths per 1,000 adults aged between 15 and 60 years. On the other hand, Germany has experienced the most impressive reductions in mortality rates, as all mortality rates are single digits, apart from the adult mortality rate of 78 deaths per 1,000 adults.

Figure 3.14: Mortality rates for some selected countries, 2010



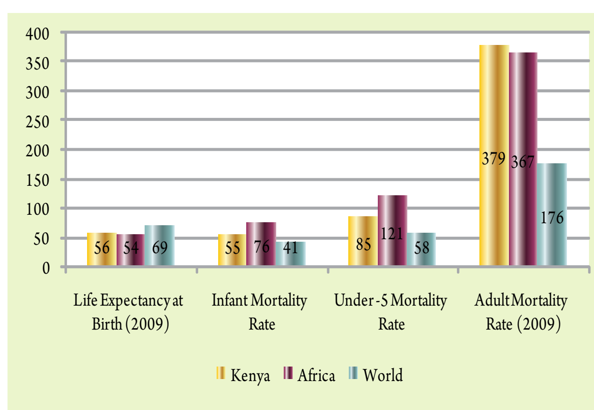
	Uganda	Ghana	Botswana	South Africa	Egypt	Chile	Indonesia	Nigeria	Germany	Cambodia	Vietnam	Kenya	Rwanda	Malaysia	Tanzania	South Korea
UMR	99	74	48	57	22	9	35	143	4	51	23	85	91	6	76	5
IMR	63	50	36	41	19	8	27	88	3	43	19	55	59	5	50	4
NMR	26	28	19	18	9	5	17	40	2	22	12	28	29	3	26	2
AMR*	401	245	545	539	115	91	193	385	78	246	113	379	335	114	364	70

**Data for AMR is for 2009*

Source: World Health Organization (2011)

Figure 3.15 compares Kenya's health indicators with those of Africa and the rest of the world. Generally, Kenya is at par with other African countries on average, but far below the world average on all the indicators for which data is available.

Figure 3.15: Health impact indicators for Kenya, Africa and the world, 2010



Source: World Health Organization (2011)

3.5.2 Burden of Disease

This section describes trends in the burden of disease in Kenya in terms of mortality and morbidity trends. The morbidity and mortality rates in the country are driven by the underlying social and economic determinants such as household and individual characteristics, the environment, and the health system. Individual level factors include low level of maternal education (74% female literacy, compared to 85% for males); poor nutritional status (34.7% of children stunted); and large gender inequalities in favour of men (WHO, 2008). The environmental determinants of health include poor access to clean water, inadequate sanitation, soil degradation, and a variety of disease vectors that thrive in certain ecological systems (WHO, 2008).

Mortality trends

Table 3.5 shows the ten major killer diseases in the country by province for the year 2010. Nationally, Malaria was the leading cause of death followed by Pneumonia and AIDS. Tuberculosis and cancer follow closely with significant deaths. In Nairobi, Central and Rift Valley provinces, Pneumonia is the leading cause of death, and Malaria is the leading cause of death in all the other provinces.

Morbidity trends

Over time, Malaria and diseases of the respiratory system have been the leading cause of inpatient morbidity nationally. As shown in Table 3.6, Malaria has had a clear lead over the years and, unfortunately, it is on the rise. Diseases of the respiratory system have almost been stable, though they increased slightly in 2009 and 2010.

Table 3.5: Causes of death by province, 2010

Cause of death	Nairobi	Central	Western	Coast	Nyanza	Eastern	Rift Valley	North Eastern	Total
Malaria	983	1,663	8,481	1,694	8,565	4,621	2,497	156	28660
Pneumonia	2,131	3,750	2,169	1,095	3,046	3,605	3,653	59	19508
AIDS	911	1,482	1,813	946	2,253	2,163	2,141	7	11716
Tuberculosis	1,391	1,304	1,523	866	2,799	1,696	1,158	52	10789
Cancer	1,070	1,644	1,796	567	1,832	1,526	1,614	64	10113
Anaemia	543	972	1,509	865	1,538	1,118	884	51	7480
Heart disease	616	1,262	448	198	600	603	854	24	4605
Other accidents	1,656	522	166	225	425	568	857	16	4435
Meningitis	823	431	380	289	902	433	897	10	4165
Road accidents	904	648	167	293	478	504	1,074	8	4076

Source: Government of Kenya (2011a), Economic Survey

Table 3.6: Leading causes of in-patient morbidity in Kenya, 2005-2010

Disease	2005	2006	2007	2008	2009	2010*
Malaria	27.6	28.6	30.8	32.8	31	29.7
Diseases of the respiratory system	24	22.4	24.5	24.1	25	25.5
Disease of the skin	5.9	5.8	6.1	7	7	7.1
Diarrhoeal diseases	4.2	4.4	4.7	4.9	5	4.8
Intestinal worms	4.7	4.1	4.3	1.2	1	1.1
Pneumonia	2.3	2.8	3	3.5	3	2.8
Accidents	2.4	2.2	2.4	2	2	1.9
Rheumatism, joint pains, etc	1.7	1.7	1.9	1.7	2	1.7
Urinary tract infections	1.5	1.6	1.8	2.3	2	1.7
Eye infections	1.5	1.5	1.6	1.7	2	1.7
All other diseases	24.3	24.9	18.5	18.8	21	22.1

Provisional

Source: Government of Kenya (2011b), Statistical Abstract

Table 3.7 shows that Malaria and diseases of the respiratory system together accounted for almost half of all outpatient morbidity over this period. The trends in both of these conditions have remained fairly stable over time. Other leading causes of morbidity such as skin diseases, diarrhoeal diseases and intestinal worms have also shown a stable trend over time. Over 60 per cent of all outpatient morbidity has been due to infectious diseases, while accidents have accounted for no more than 3.1 per cent of out-patient diagnoses over the period analyzed.

Table 3.7: Leading causes of outpatient morbidity in Kenya 2000–2010

Disease	2005	2006	2007	2008	2009	2010*
Malaria	33.2	28.6	30.8	32.0	32.0	49.7
Disease of the respiratory system	25	22.4	24.5	24.7	24.8	43.3
Diseases of the skin (including ulcers)	6.4	5.8	6.1	6.9	6.5	11.8
Diarrhoeal diseases	4.8	4.4	4.7	5.1	5.2	7.6
Intestinal worms	4.6	4.1	4.3	3.5	3.3	5.7
Accidents (including fractures, burns, etc)	2.6	2.2	2.4	2.2	1.8	3.1
Pneumonia	2.8	2.8	3.4	3.5	3.2	4.8
Urinary tract infections	1.7	1.5	1.6	1.6	1.6	2.9
Eye infections	1.6	1.5	1.8	1.8	1.7	2.9
Rheumatism, joint pains, etc	1.9	1.7	1.9	2.3	2.6	4.3

** Provisional*

Source: Government of Kenya (2011a)

3.5.3 Key Intervention Areas

Key interventions to improve population health are recommended in areas of reproductive health and child health.

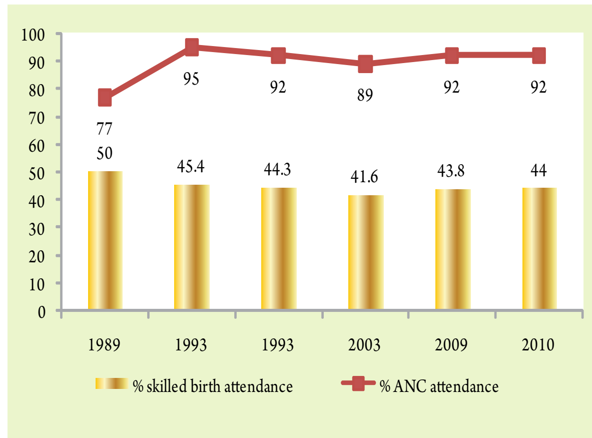
Reproductive health

Antenatal care and skilled birth attendance

Attendance of antenatal care services was already high in the early 1990s and continues to be high with nine out of ten women attending clinic at least once. However, for skilled birth attendance, only 50 per cent of the deliveries were attended by a skilled professional in 1989, but fell to 44 per cent in 2010.

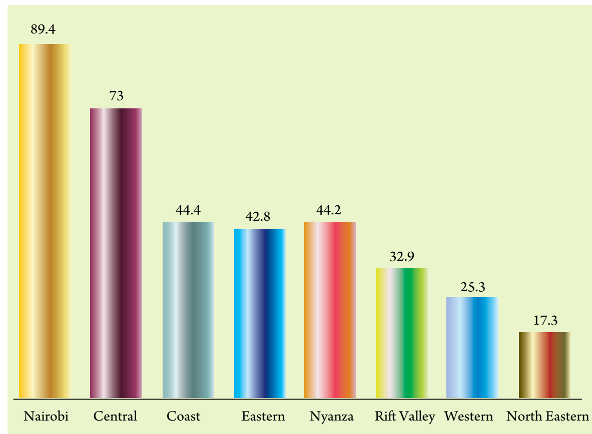
The place of delivery is highly correlated with the skilled birth attendance, as very few deliveries at home are attended by doctors or nurses. There are marked differences in the country in this respect between the provinces, with Central Province and Nairobi having institutional delivery rates that are twice as high as in all other provinces.

Figure 3.16: Trends in ANC coverage and skilled birth attendance



Source: World Bank (2011) and World Health Organization (2011)

Figure 3.17: Delivery in a health facility by province, 2008[1]



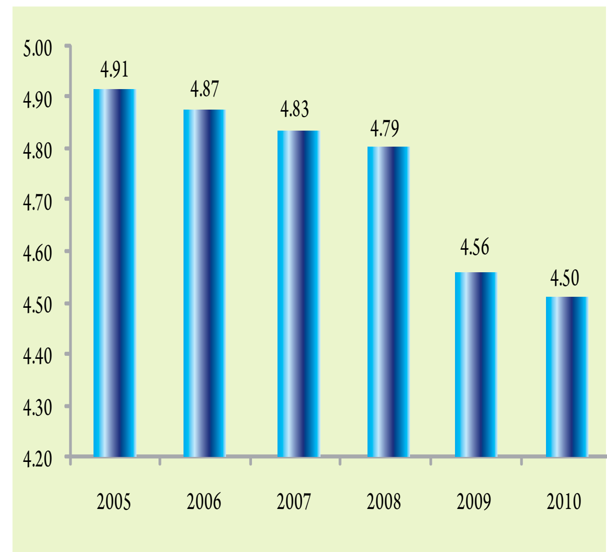
Source: KNBS (2010)

Fertility

Total fertility rate is the average number of children that would be born per woman if all women lived to the end of their childbearing years and bore children according to a given fertility rate at each age. The total fertility rate (TFR) is a more direct measure of the level of fertility than the crude birth rate, since it refers to births per woman. This indicator shows the potential for population change in the country. A rate of two children per woman is considered the replacement rate for a population, resulting in relative stability in terms of total population numbers. Rates above two children indicate populations growing in size and whose median age is declining. Higher rates may also indicate difficulties for families in feeding and educating their children, and in enabling adult female members to enter the labour force. Rates below two children indicate decreasing and ageing populations.

Figure 3.18 shows trends in total fertility rates in Kenya between 2005 and 2010. The data shows that fertility rates have been on the decline over the years, but is yet to reach the optimal rate of two children per woman.

Figure 3.18: Trends in total fertility rate in Kenya

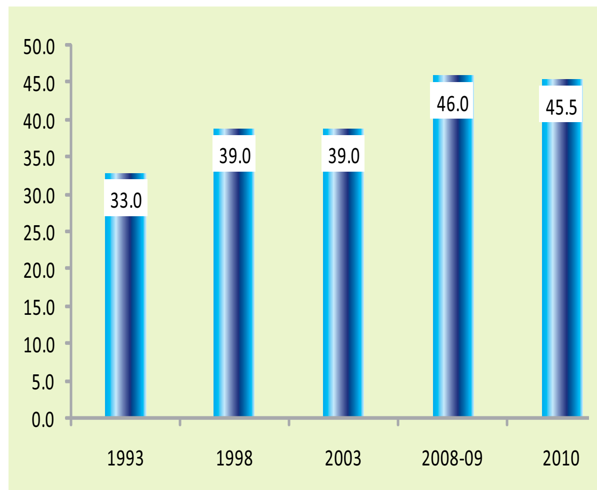


Source: World Bank (2011)

Contraceptive use

Data on contraceptive use is drawn from the KDHS (KNBS, 2010) and World Health Statistics (World Health Organization, 2011). The overall contraceptive prevalence rate among all married women 15-49 increased gradually over the period, with 46 per cent of this group using any method in 2008-09 (Figure 3.19). The rate seems to have dropped slightly in 2010.

Figure 3.19: Contraceptive use rate among married women (any method)



Source: KNBS (2010) and World Health Organization (2011)

Figure 3.20 shows distribution of contraceptive use by married women aged 15-49 years old by province. Married women in Central Province have the highest contraceptive prevalence rate for any method (67%) and 63 per cent for modern method, followed by Nairobi (53%) and 49 per cent for modern method and Eastern Province (52%) and 44 per cent for modern method. The lowest level of family planning use is recorded in North Eastern Province at 4 per cent, which also has the highest percentage of non-use of any method. A whole 54.5 per cent of currently married women of reproductive age in Kenya are not using any method of family planning.

Child health

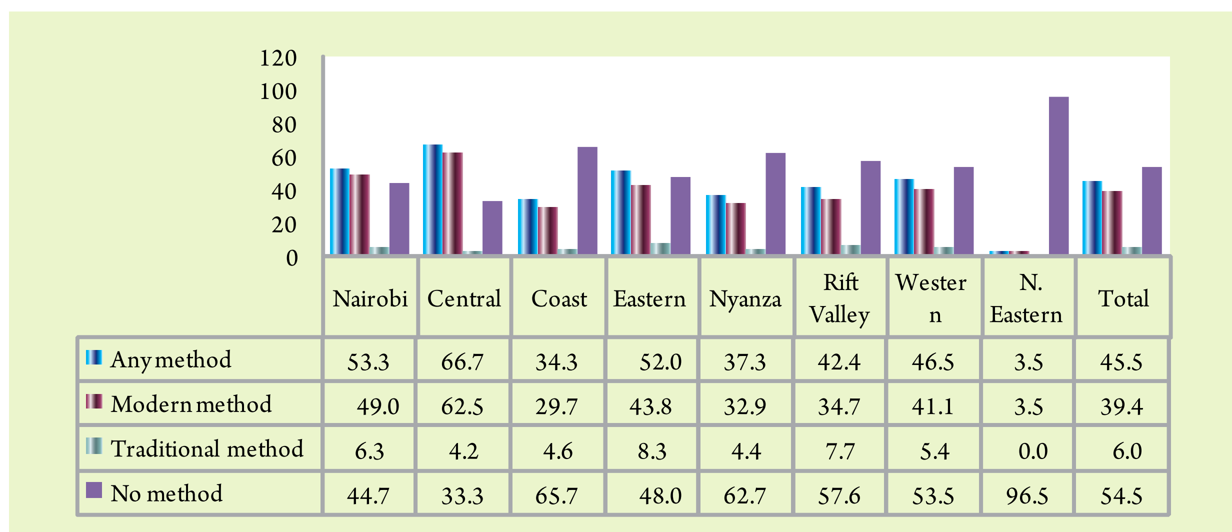
Kenya's child health strategy includes a range of interventions in early childhood, neonatal health care, school health services and adolescent health. Integrated Management of Childhood Illness (IMCI) for children under five years of age was introduced in selected districts in the late 1990s and expanded during the following decade.

Immunization

Annual trends in immunization coverage are derived from the World Bank database (World Bank, 2011). These are shown in Figure 3.21. DPT immunization coverage reached a peak of over 85 per cent in 2008 and has been on the decline since then. A similar trend is observed for measles immunization.

The provincial differences for BCG, measles[3] and fully immunized are shown in Figure 3.22 based

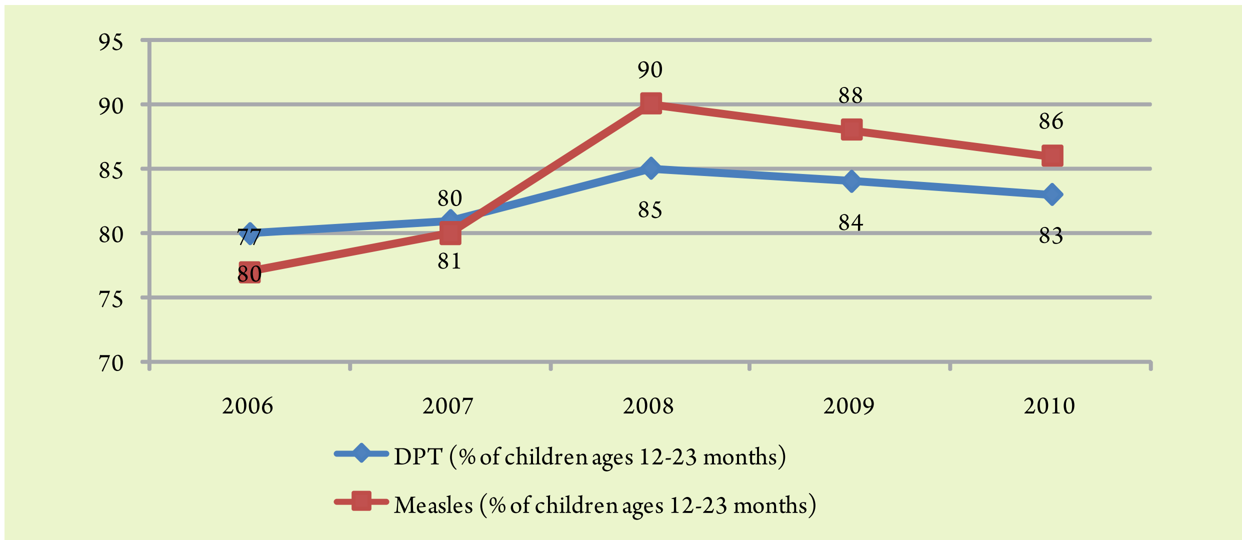
Figure 3.20: Distribution of contraceptive use by married women by province, 2008[2]



	Nairobi	Central	Coast	Eastern	Nyanza	Rift Valley	Western	N. Eastern	Total
Any method	53.3	66.7	34.3	52.0	37.3	42.4	46.5	3.5	45.5
Modern method	49.0	62.5	29.7	43.8	32.9	34.7	41.1	3.5	39.4
Traditional method	6.3	4.2	4.6	8.3	4.4	7.7	5.4	0.0	6.0
No method	44.7	33.3	65.7	48.0	62.7	57.6	53.5	96.5	54.5

Source: KNBS (2008)

Figure 3.21: DPT and Measles immunization coverage (%) 2000-2010

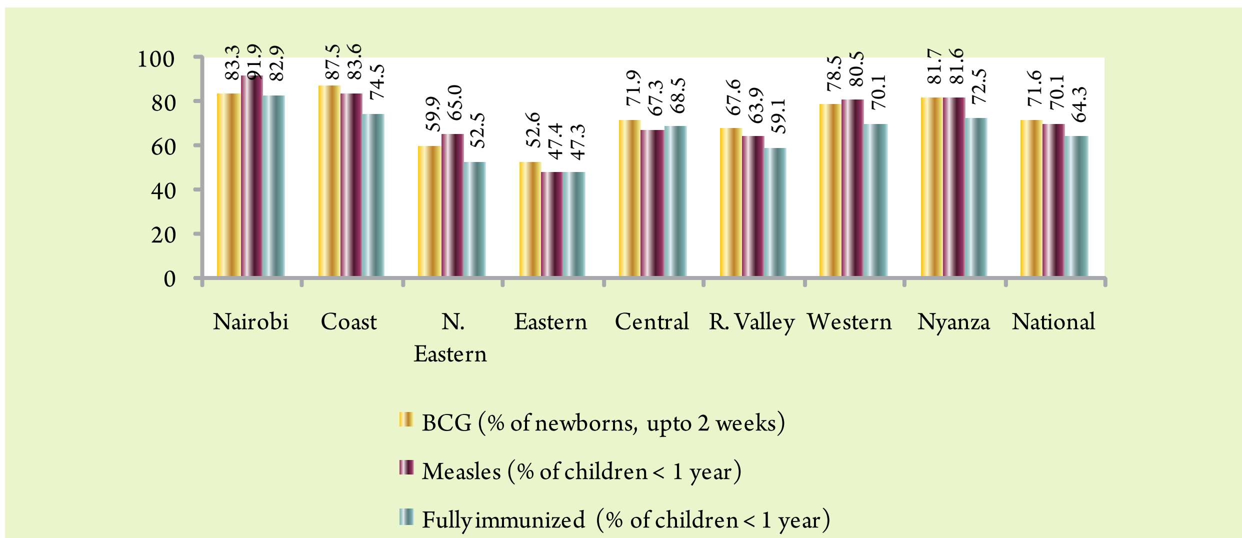


Source: World Bank (2011)

on data from the HMIS 2010/2011 financial year. Overall, BCG coverage was 71.6 per cent, measles 70.1 per cent and fully immunized 64.3 per cent. Eastern Province had the lowest coverage for all the three types of immunization followed by North Eastern Province. Central, Eastern and Rift Valley provinces had similar pattern of coverage in all the three areas (BCG, measles and fully immunized).

Trends in full immunization coverage for children under one year old by province between 2005 and 2010 are shown in Table 3.8. Nairobi and Central provinces have the highest coverage, while North Eastern Province has the lowest coverage.

Figure 3.22: BCG, measles and fully immunized children below one year



Source: Government of Kenya (2011a)

Table 3.8: Full immunization coverage for under-ones by province

	2005	2006	2007	2008	2009	2010*
Nairobi	75	76	78	74	83	103
Central	93	88	85	86	92	102
Coast	61	74	78	75	71	87
Eastern	67	78	78	64	80	83
North Eastern	48	72	81	89	67	64
Nyanza	53	66	66	75	79	79
Rift Valley	57	67	70	64	71	72
Western	57	59	68	66	85	90
National	63	71	73	71	78	83

*Provisional

Source: Government of Kenya (2011b)

On the international scene, a comparison is made of Kenya and other countries for measles and DPT3 for 2010. For measles, Kenya compares well with her peers, though far below countries such as Malaysia, South Korea, Germany, among others.

3.5.4 Health Inputs

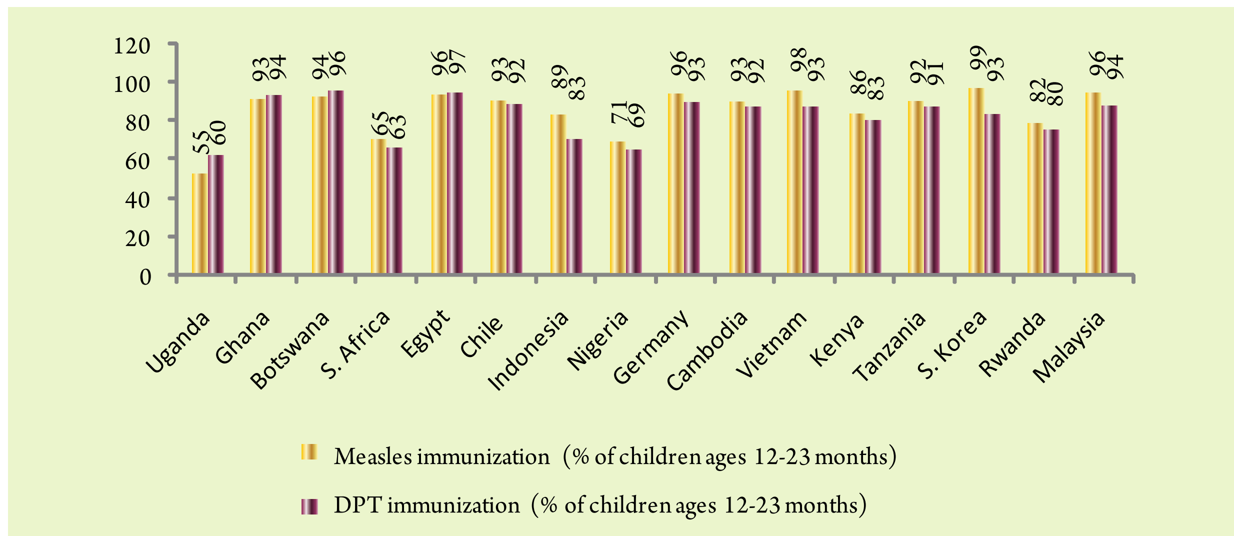
These refer to the inputs that are needed to deliver the health services, and they include human resources for health, health infrastructure and operational finances. This section analyzes overall health expenditures, followed by human resources for health and health infrastructure.

Health expenditures

There are three main sources of finances for health in Kenya, namely, public (government), private (household out of pocket payments or cost sharing) and donors. Government contribution to total healthcare financing is 29 per cent, donors 31 per cent and private 36 per cent and others (private companies and local foundations) 4 per cent. The total health expenditure per capita trends, total health expenditure as a percentage of GDP, and government health allocations as a percentage of total government allocations are shown in Figure 3.24.

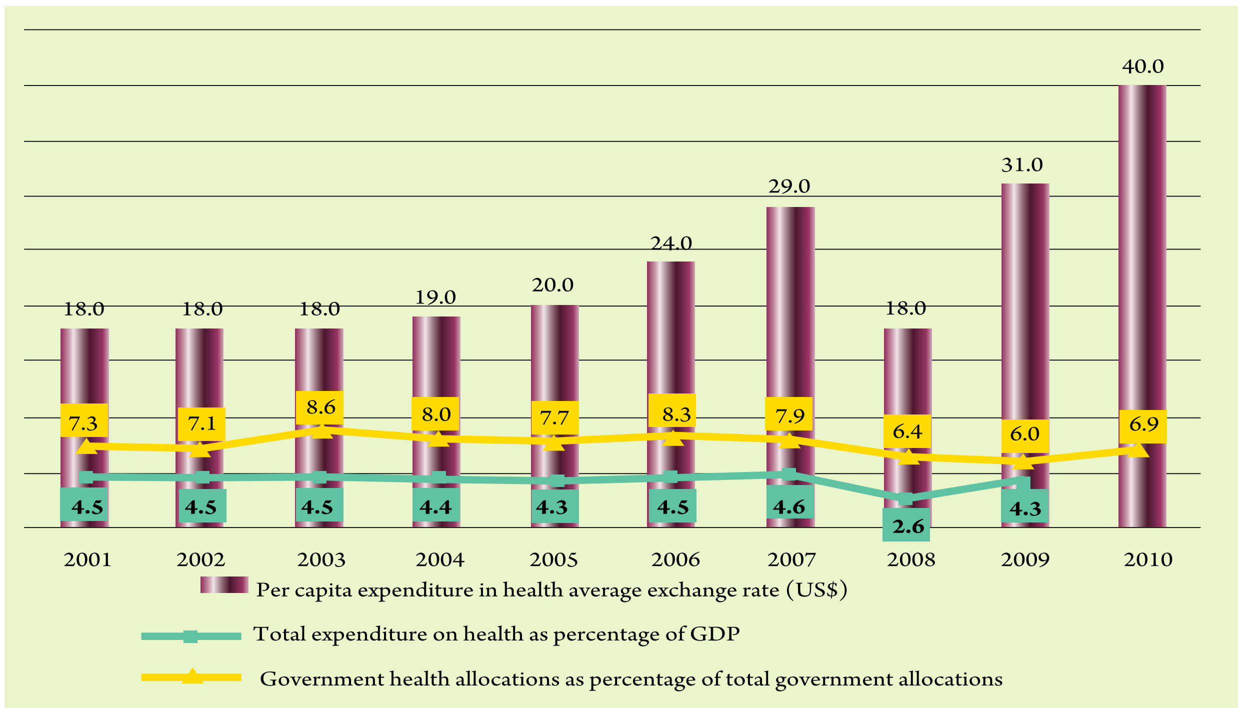
The overall financing available, in real terms, has been increasing over time, from an estimated total health expenditure of US$ 17.7 per capita in 2001, to an estimated US$ 40 per capita in 2010. The reduction in 2008 is a reflection of the peculiar situation in that year, with reduced funding due to the post-election crisis then. However, looking at total health expenditure as a share of GDP, there is no increase; values remain within 4.3-4.6 per cent of GDP being spent on health. This suggests that the increase in health funding is an absolute increase, not a real increase.

Figure 3.23: Measles and DPT immunization coverage for selected countries, 2010



Source: World Bank (2011)

Figure 3.24: Total health expenditure trends (US$)

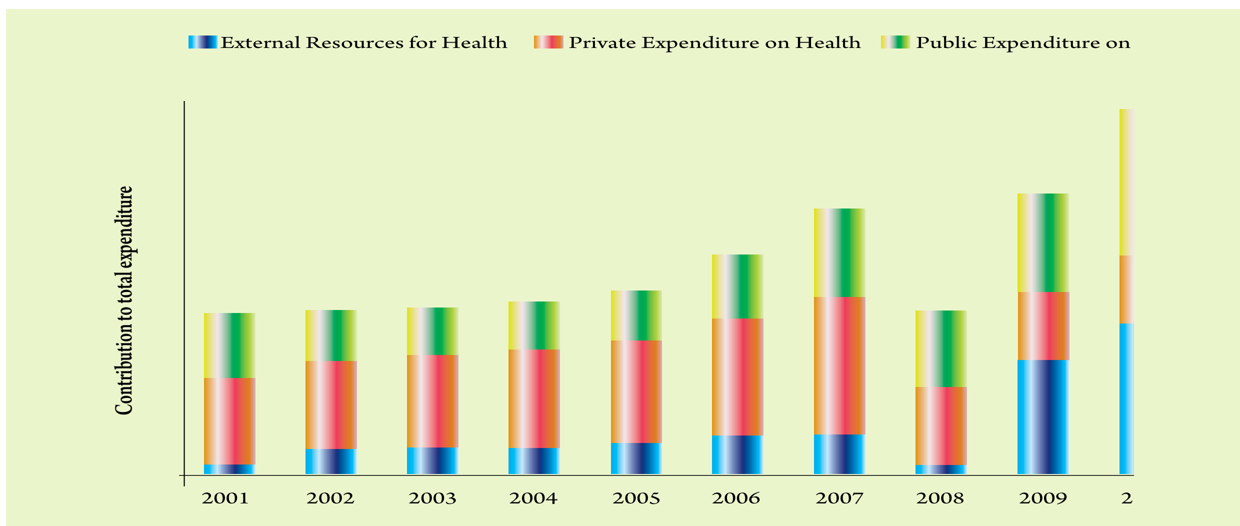


Sources: Government of Kenya (n.d; 2009) and WHO (2010; 2011)

As can be seen from Figure 3.25, the absolute increases are from government and external sources, with private spending having reduced. External sources represent some of the most unsustainable sources of financing. This is well seen in the level of funding during 2008, the year of the post-election crisis, when external financing had the most significant drop as compared to all the other sources of financing.

Out of pocket financing for health has been increasing over the years, in absolute terms. This has, however, been reducing as a portion of total health expenditure from 51 per cent in 1999/2000, to 35.9

Figure 3.25: Contribution to total expenditure (US$)



Sources: Government of Kenya (n.d; 2009) and WHO (2010; 2011)

per cent in 2005/06 (Government of Kenya, 2009a). The further increases in total health expenditure due to increasing government and donor financing should further reduce this portion of financing.

Total expenditure on health as a per cent of GDP for different countries (Figure 3.26) shows that Kenya is amongst the lowest spenders on health as a per cent of GDP. Countries with lower per capita income, such as Uganda and Tanzania, have higher allocations to health as a per cent of GDP than Kenya. This could be explained by the fact that these countries have a lot of donor support compared to Kenya, and the fact that they qualified for Heavily Indebted Poor Countries (HIPC) Initiative (which Kenya did not) and as a result, they have to allocate the debt forgiven to health and education.

Human resources

For health goals to be achieved, adequate numbers of health workers with the appropriate training must be available. The health workforce includes those directly providing health services as well as health administrators and engineers working in the health field who do so indirectly.

Trends in human resources

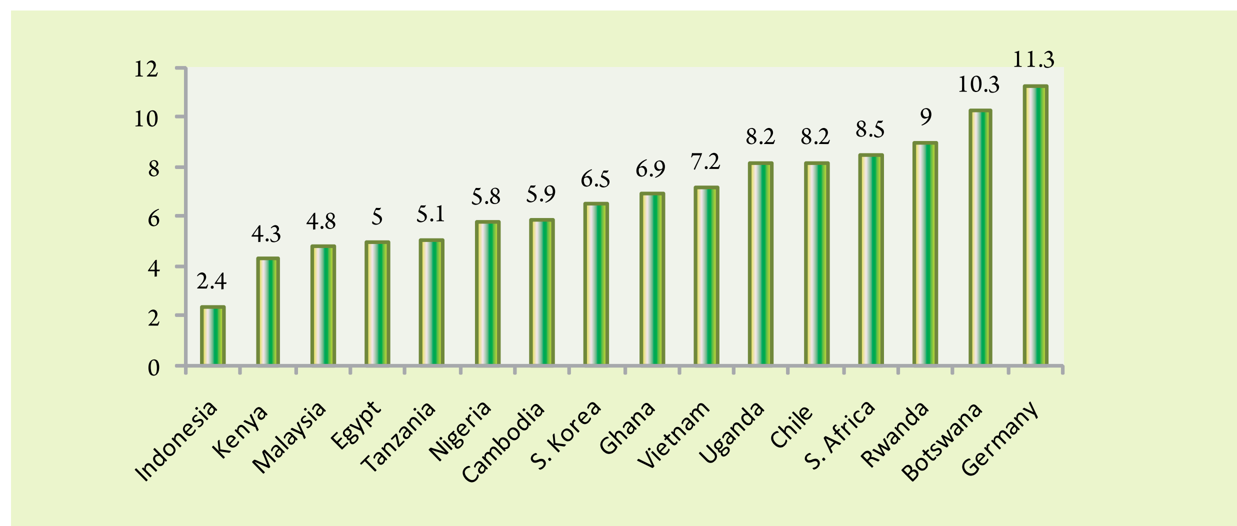
In absolute terms, the health workforce has been increasing over time. However, the number of enrolled nurses has remained the same for about three years, while the number of clinical officers declined in 2008 from 5,797 in 2007 to 5,035. However, health workers/10,000 population has remained the same for all cadres, except for nursing officers, which has been on the rise, and enrolled nurses and clinical officers, whose number has been on the decline for the three year period (Table 3.9).

In all provinces (Figure 3.27), a general decline is evident in the number of health workers per 10,000 population over the period analyzed. In Nairobi, however, this trend is reversed in 2008-2009. Also, there is no significant difference amongst the provinces in terms of health workers/10,000 population, though North Eastern Province is clearly lagging behind and Central Province has a clear lead in all the years except 2009, when Nairobi Province is leading.

Kenya compares relatively well with other African peer countries regarding availability of public health workers. It has a fairly good availability of public health workers for a number of cadres, when compared even with the global picture. This is shown in Figure 3.28.

Comparison with selected countries using latest available data for nurses (2000-2010) shows the

Figure 3.26: Total expenditure on health as a % of GDP, 2009



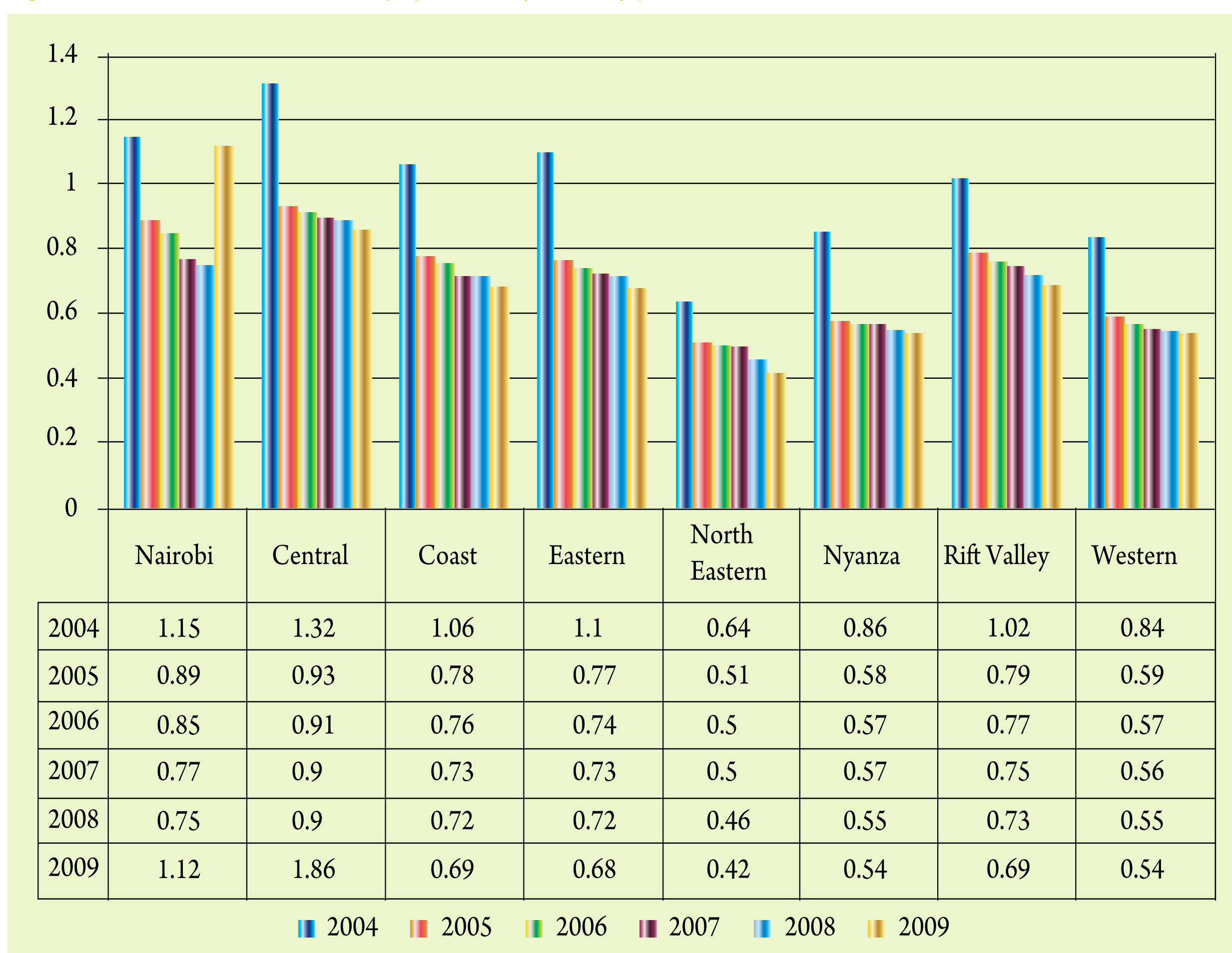
Source: World Health Organization (2011)

Table 3.9:Health workers/10,000 population by cadre

Type of Health Personnel	2007		2008		2009		2010*	
	Number	No / 100,000	Number	No / 100,000	Number	No / 100,000	Number	No / 100,000
Doctors	6,271	17	6,623	17	6,800	18	7,129	18
Dentists	931	3	974	3	859	2	898	2
Pharmacists	2,775	7	2,860	7	2,921	8	3,097	8
Pharmaceutical technologist	1,680	5	1,851	5	1,950	5	2,233	6
Nursing officers	12,198	33	14,073	37	26,988	70	29,678	75
Enrolled nurses	31,917	86	31,917	83	34,032	88	34,282	86
Clinical officers	5,797	16	5,035	13	7,816	20	8,598	22

Source: Government of Kenya (2011b)

Figure 3.27: Health workers/10,000 population by cadre by province



	Nairobi	Central	Coast	Eastern	North Eastern	Nyanza	Rift Valley	Western
2004	1.15	1.32	1.06	1.1	0.64	0.86	1.02	0.84
2005	0.89	0.93	0.78	0.77	0.51	0.58	0.79	0.59
2006	0.85	0.91	0.76	0.74	0.5	0.57	0.77	0.57
2007	0.77	0.9	0.73	0.73	0.5	0.57	0.75	0.56
2008	0.75	0.9	0.72	0.72	0.46	0.55	0.73	0.55
2009	1.12	1.86	0.69	0.68	0.42	0.54	0.69	0.54

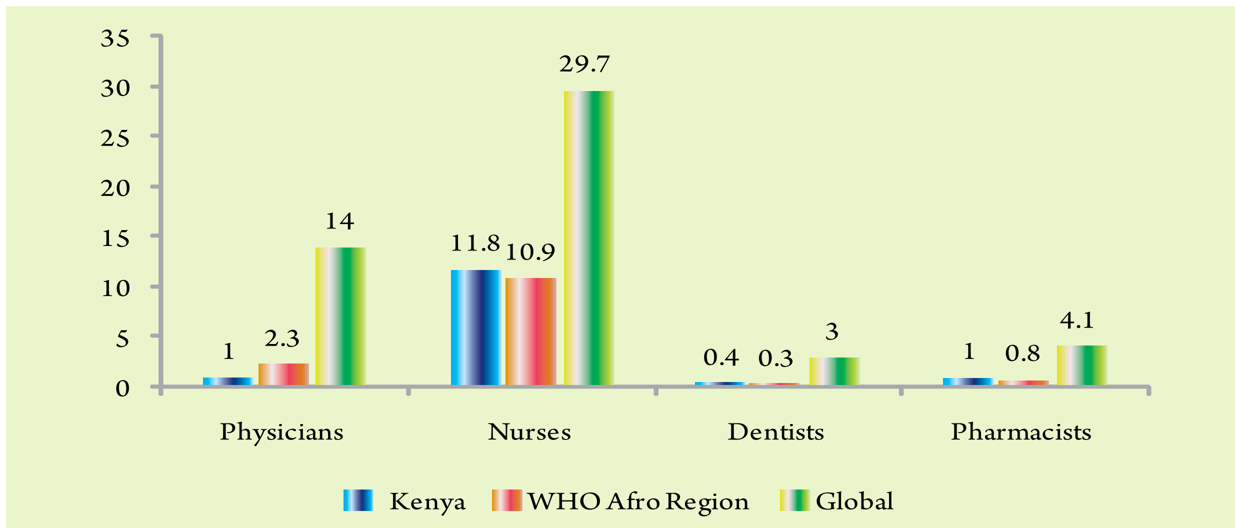
Sources: Government of Kenya (2010a)

country is performing relatively well within the region compared to Tanzania, Rwanda and Ghana (Figure 3.29).

Physical infrastructure

The number of health facilities is a proxy to the quantity of health infrastructure investment within the country. Health facilities in Kenya can be

Figure 3.28: Benchmarking of selected staff cadres, 2000-2010



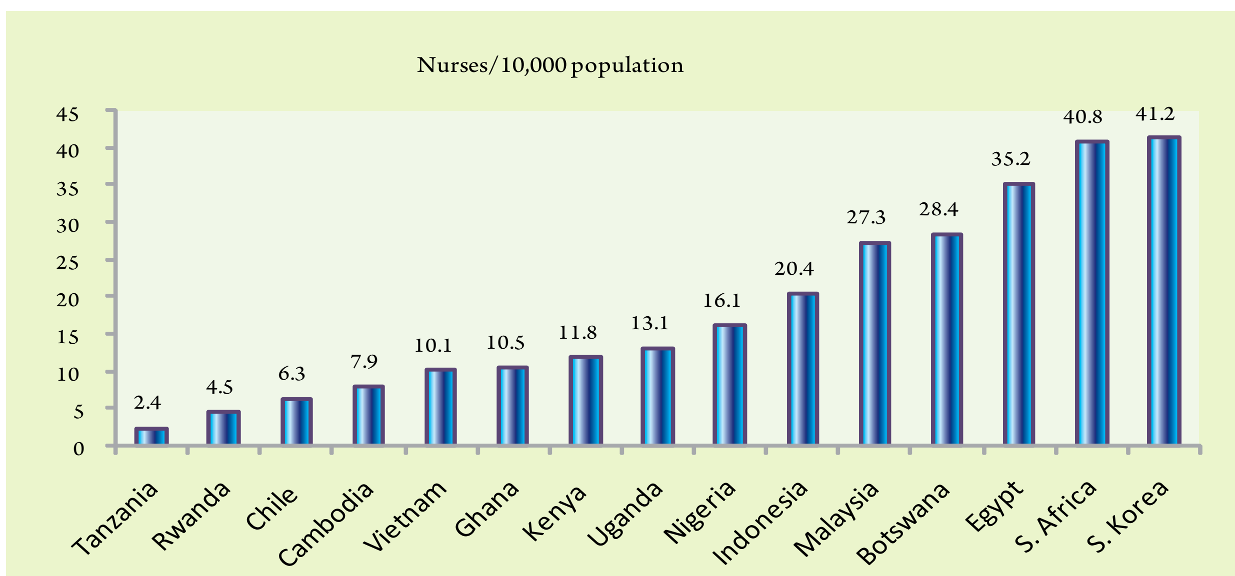
Source: World Health Organization (2011)

classified according to ownership. Hence, we have public facilities (owned by the Government of Kenya), those owned by Faith-Based Organizations (FBOs), Non-Governmental Organizations (NGOs), and those that are wholly private.

Trends and distribution of physical facilities

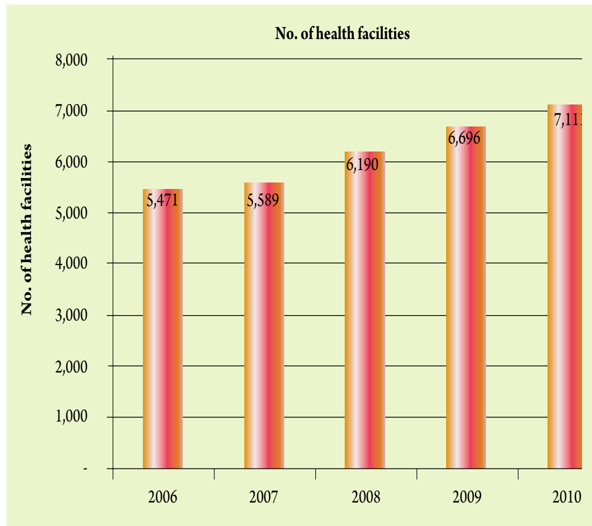
The number of health facilities has been increasing over time in the period 2006-2010. This is depicted in Figure 3.30. Between 2006 and 2007, the facilities only increased by 118 facilities but rose by 601 the following year and 506 between 2008 and 2009. This abrupt increase between 2007 and 2009 could be attributed to the Constituency Development Fund (CDF) facilities.

Figure 3.29: Benchmarking of nurses/10,000 population 2000-2010



Source: World Health Organization (2011)

Figure 3.30: Trends in total numbers of physical facilities



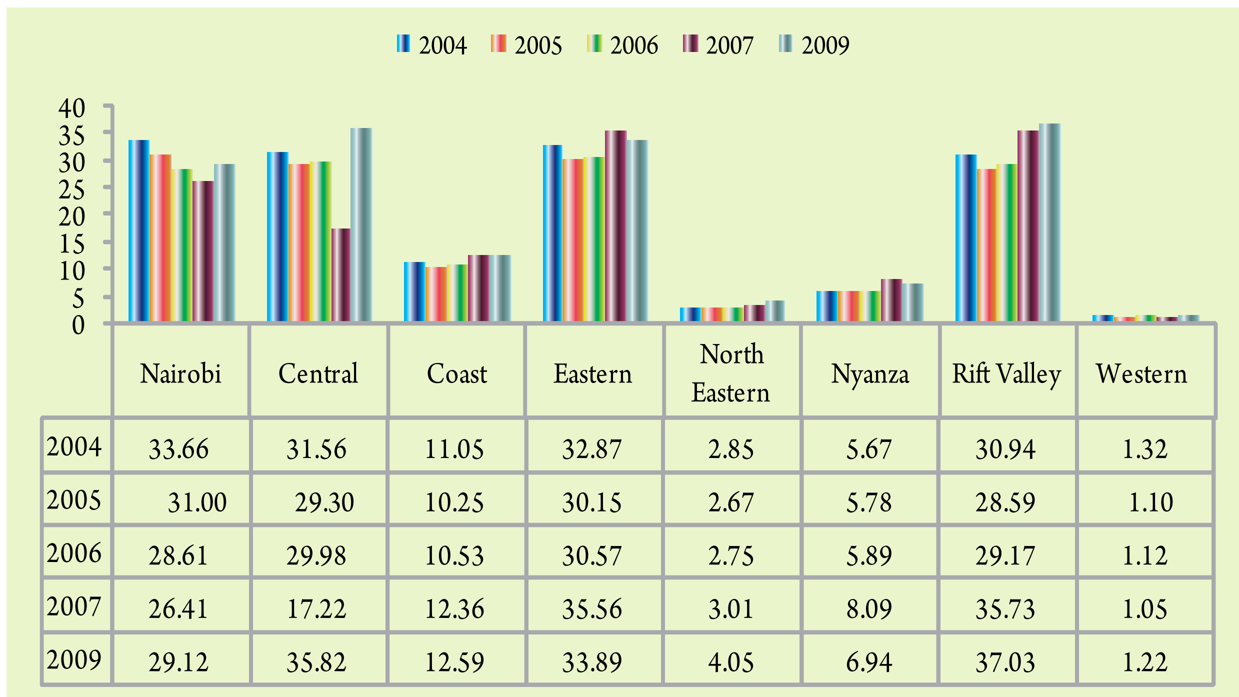
Source: Government of Kenya (2011a)

By province, the number of health facilities has also been growing over time though at different rates. Nairobi, Western and North Eastern provinces have had very small growth rates in health facilities compared to Rift Valley, Central and Nyanza provinces. Rift Valley Province has the highest number of health facilities, followed by Central Province, while North Eastern Province has had the least number of facilities over time. Figure 3.31 shows the trend in health facilities by province.

Health facilities per 100,000 persons (Figure 3.32) have not shown remarkable increase over time since, as the facilities increase, the population is also increasing. The increase between 2007 and 2009 could be attributed to the CDF health facilities.

We use the number of hospital beds per 10,000 persons as the variable to benchmark the country performance (Figure 3.33). From the WHO statistics (World Health Organization, 2011), Kenya is doing better in number of hospital beds per 10,000 persons than Uganda, Nigeria, Ghana and Tanzania, but lagging far behind the developed countries.

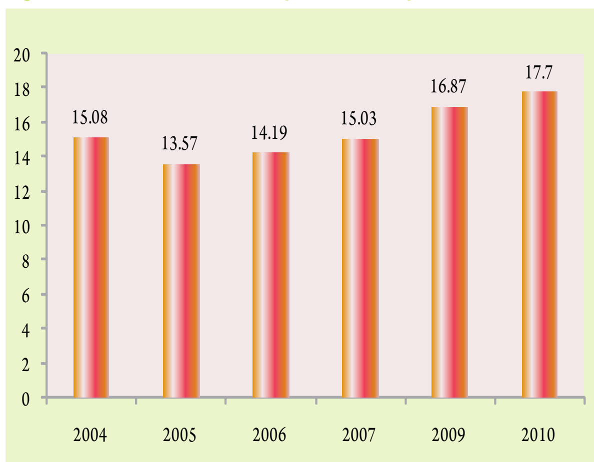
Figure 3.31: Trends in health facilities by province, 2005–2009



	Nairobi	Central	Coast	Eastern	North Eastern	Nyanza	Rift Valley	Western
2004	33.66	31.56	11.05	32.87	2.85	5.67	30.94	1.32
2005	31.00	29.30	10.25	30.15	2.67	5.78	28.59	1.10
2006	28.61	29.98	10.53	30.57	2.75	5.89	29.17	1.12
2007	26.41	17.22	12.36	35.56	3.01	8.09	35.73	1.05
2009	29.12	35.82	12.59	33.89	4.05	6.94	37.03	1.22

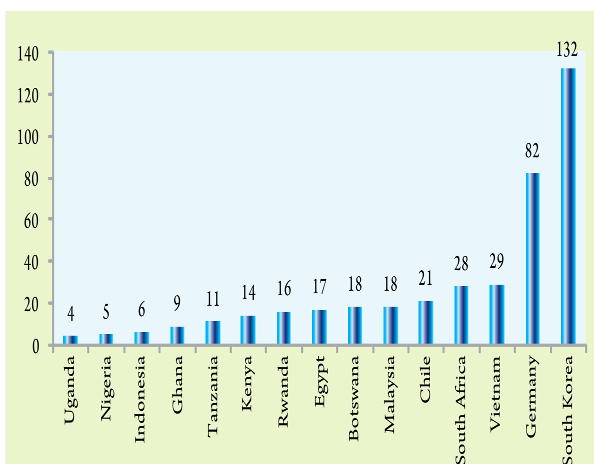
Source: Government of Kenya (2011)

Figure 3.32: Health facilities per 100,000 persons



Source: Government of Kenya (2010c)

Figure 3.33: Number of hospital beds per 10,000 persons, 2009



Source: World Health Organization (2011)

3.6 Education

Provision and sustainable financing of quality education and training are fundamental in the attainment of objectives in the Kenya Vision 2030 through development of requisite human capital (Government of Kenya, 2007b; 2008c). Efforts towards this include substantial expansion of the sector over time. In 2009, for example, there were 38,247 Early Childhood Development Education (ECDE) centres; 26,667 primary schools, 6,971 secondary schools, 105 primary teacher training colleges and 31 universities in the country (Government of Kenya, 2010a). During the same period, the enrolment was 1.91 million children in ECDE centres; 8.8 million pupils in primary schools (9.4 million in 2010); 1.5 million students in secondary schools (1.7 million in 2010); 177,735 students in universities; 163,340 students in non-formal schools; 189,000 adult education learners; about 26,324 trainees in teacher training institutions and 71,513 students in technical education institutions. On the other hand, the education sector receives a substantial proportion of public funds. For instance, in 2007/08, the total education expenditure as a percentage of GDP was 6.2 per cent and 7.4 per cent in 2009/10 (Government of Kenya Appropriation Accounts and Economic Survey, Various).

Despite the substantial resources that the government spends on education and training, the sector faces various challenges with regard to quality, equity in access and financing. All these issues are related to the management of learning institutions. In effect, this section examines issues and trends directly related to public spending on education, access, quality and internal efficiency, equity, and issues of institutional management of education and training in Kenya. These factors have direct impact on the processes and strategies for improving educational attainment and educational objectives as articulated in both Vision 2030 and the Constitution of Kenya (2010). Issues on the current status of institutional frameworks are also discussed. Further, the section discusses the country's education sector performance relative to selected comparator and aspirator countries.

3.6.1 Financing of Education and Training

Public spending on education and training increased from 6.2 per cent of GDP in 2007/08 to about 7.4 per cent in 2009/10. This represents about 25 per cent of total government expenditure. In 2009/10, about 88.5 per cent of the total education expenditure was recurrent, down from 91.9 per cent in 2007/08. Increasing the level of development

expenditure is partly due to the economic stimulus spending mainly towards expansion of school infrastructure and improvement of learning facilities in most marginalized areas (Table 3.10).

Table 3.10: Education spending as percentage of GDP and government outlays, 2007/08-2009/10

	2007/08	2008/09	2009/10
Education expenditure as % of GDP	6.2	6.5	7.4
Education expenditure as % government outlays	23.2	21.9	24.8
Education recurrent expenditure as % government recurrent outlays	30.8	29.8	32.9
Education development expenditure as % government development utlays	6.1	5.9	8.6
Ministry of Education recurrent expenditure as % of expenditure	91.9	91.0	88.5
Ministry of Education development expenditure as % of expenditure	8.1	9.0	11.5

Source: Government of Kenya (Various), Appropriation Accounts, and Government of Kenya (Various), Economic Surveys

Table 3.11 shows the allocation of the total education budget across the education sub-sectors. Despite the observed decline in the proportion of primary education as a percentage of total education expenditure, the primary education sub-sector has received the highest allocation across all the education sectors over the years. For instance, in 2009/10, the primary school sub-sector received the highest share of government expenditure on education (44%). Secondary and university sub-sectors received 25 per cent and 13 per cent of the total education budget, respectively. The substantial allocation to primary education is a deliberate effort towards attainment of the Millennium Development Goals (MDGs) and Education for All (EFA) goals on attaining Net Enrolment Rate (NER) and completion rate of 100 per cent at primary education level by 2015.

Table 3.11: Public spending on education by level, 2007/08-2009/10 (%)

	2007/08	2008/09	2009/10
General Administration and Planning	9.85	7.38	12.46
Primary Education	52.01	49.81	44.18
Teacher Education	0.36	0.29	0.16
Special Education	0.35	0.43	0.06
Early Childhood Education	0.05	0.18	0.16
Secondary Education	22.97	24.67	24.59
Technical Education	3.46	4.85	5.89
University Education	10.94	12.39	12.50
Total Education Expenditure (Ksh billion)	121.13	136.89	159.21

Source: Government of Kenya (Various) Appropriation Accounts and Economic Surveys

The secondary education sub-sector receives the second highest share in the total education budget. As shown in Table 3.11, government allocation to the secondary education sub-sector increased marginally from about 23 per cent in 2007/08 to nearly 25 per cent in 2009/10. The increase could be attributed to the introduction of the Free Day Secondary Education programme. The funds for this programme are mainly spent on teaching and learning materials and other operational costs; bursary allocation for bright students from poor households and vulnerable groups; and development grants allocation and infrastructure across provinces.

Data provided in Table 3.12 shows estimated government (recurrent) spending per student enrolled in the respective levels of education. The per capita public primary education spending increased from Ksh 7,457 in 2007 to Ksh 7,978 in 2009 at current prices. The unit spending for secondary education (Ksh 27,574) was 3.5 times that of primary education in 2009, and 48 per cent of Gross Domestic Product (GDP) per capita. University

and technical education public unit spending (Ksh 83,761 and 113,779) were 10.5 times and 14 times that of primary education, respectively.

Table 3.12: Per capita expenditure on education by level, 2007-2009 (Ksh)

	2007	2008	2009
Unit public spending (Ksh)			
Primary	7,457	7,781	7,978
Secondary	29,485	29,484	27,574
Technical	43,474	55,318	83,761
University	138,417	137,707	113,779
As ratio to primary education			
Secondary	4.0	3.8	3.5
Technical	5.8	7.1	10.5
University	18.6	17.7	14.3
GDP per capita*	49,204	54,371	57,887
As % GDP per capita			
Primary	15.16	14.31	13.78
Secondary	59.92	54.23	47.63
Technical	88.35	101.74	144.70
University	281.31	253.27	196.55

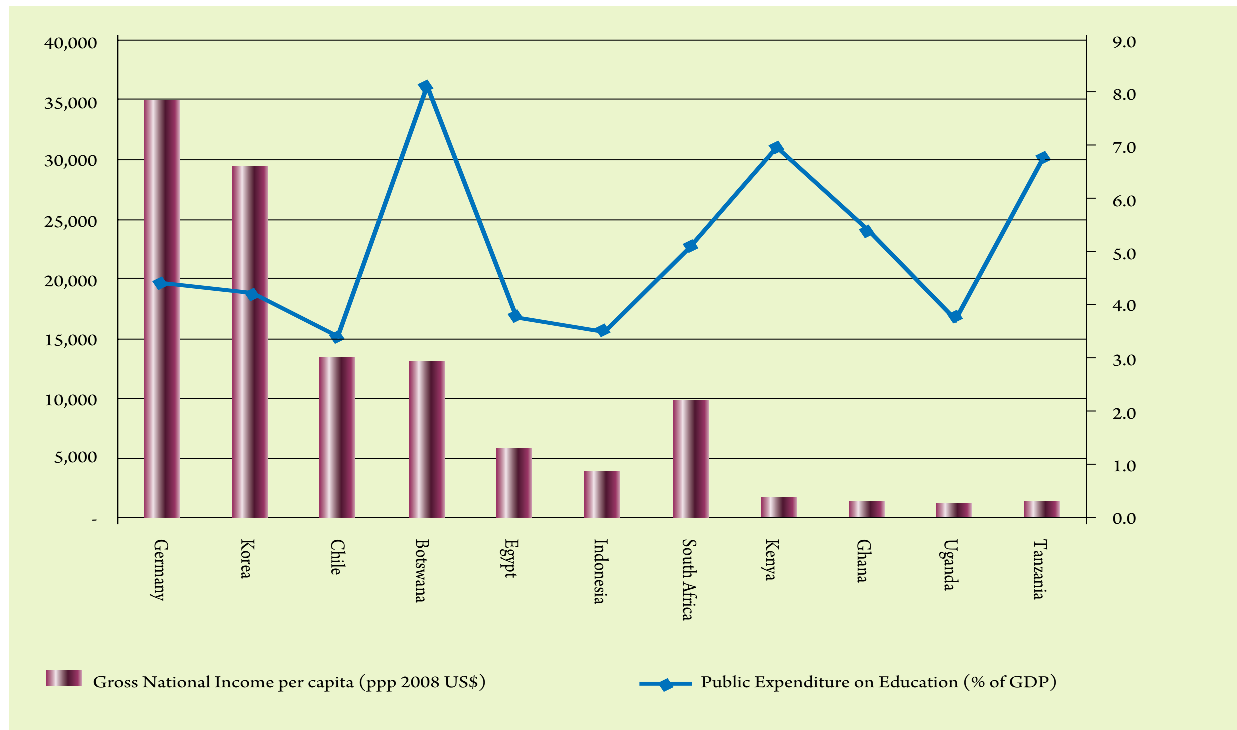
Source: *Government of Kenya (Various) Economic Surveys and authors' computations

In 2010, total public expenditure on education as a percentage of GDP was relatively high (7.4%) for Kenya compared to South Africa (5.1%), which had a relatively higher GNI per capita (US$ 9,812). Public spending on education as percentage of GDP was, however, close to Botswana's level of spending (8.1%). Kenya's GNI per capita at the time was estimated US$ 1,628, while that of Botswana was US$ 13,204.

Table 3.13: Gross Enrolment Rate (GER) and Net Enrolment Rate (NER), 2007-2010

			2007	2008	2009	2010
Primary	Gross Enrolment Rate	Male	111.8	112.2	112.8	109.8
		Female	106.0	107.3	107.2	109.9

Figure 3.34: Public spending on education as % of GDP and GNI, 2010



Source: UNDP (2010)

			2007	2008	2009	2010
		Total	108.9	109.8	110.0	109.8
	Net Enrol-ment Rate	Male	94.1	94.6	93.6	90.6
		Fe-male	89.0	90.5	92.1	92.3
		Total	91.6	92.5	92.9	91.4
Sec-ond-ary	Gross Enrol-ment Rate	Male	41.4	46.3	49.0	50.9
		Fe-male	34.6	38.8	41.8	46.3
		Total	38.0	42.5	45.3	47.8
	Net Enrol-ment Rate	Male	25.2	29.8	36.5	38.0
		Fe-male	23.2	27.9	35.1	38.9
		Total	24.2	28.9	35.8	32.0

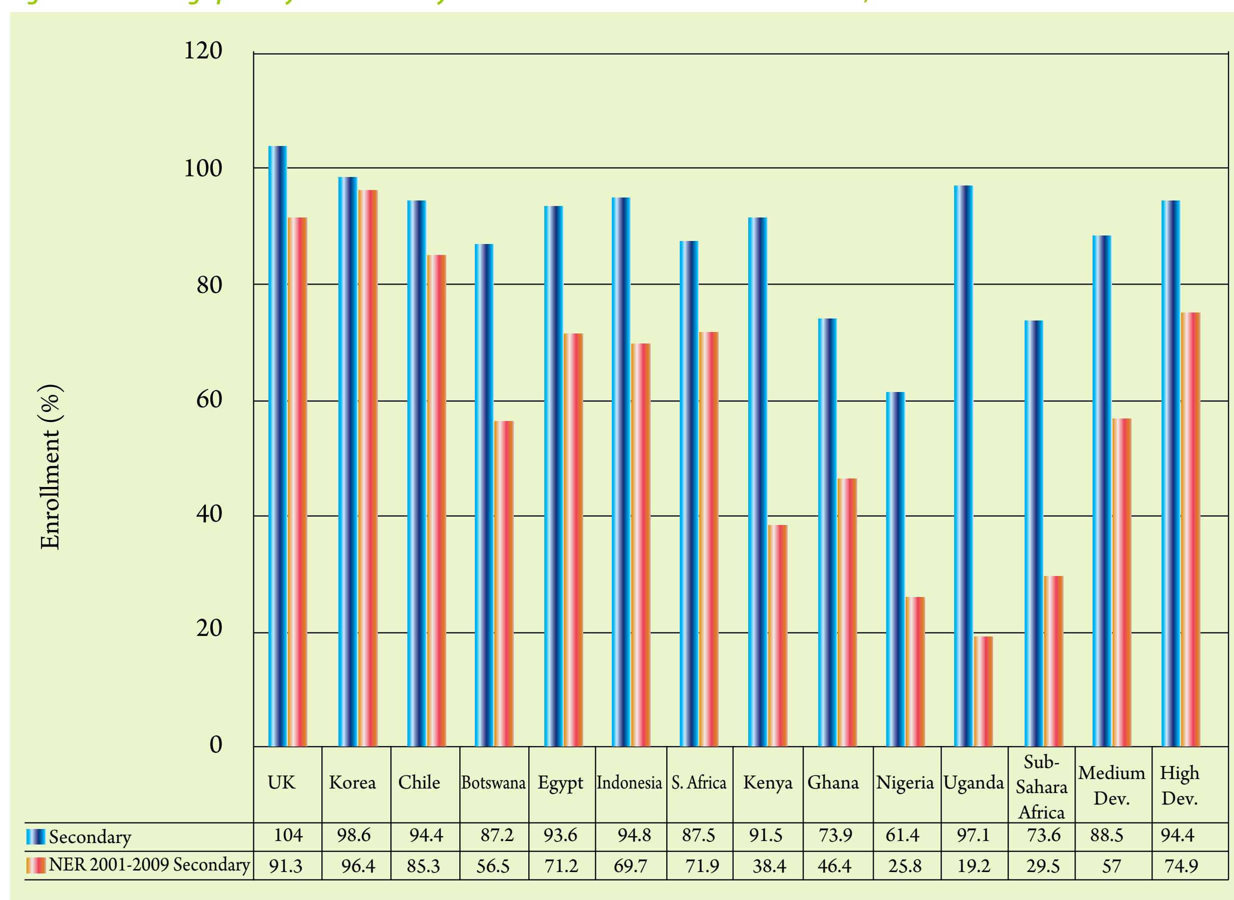
Source: Government of Kenya (2010b)

3.6.2 Performance of the Education Sector

Access and participation

Overall primary gross and net enrolment rates increased from 108.9 per cent and 91.6 per cent in 2007 to 109.8 per cent and 91.4 per cent in 2010. Gross and net enrolment rates in ECDE were 60.6 per cent and 49 per cent in 2009 and 2010, respectively. Secondary gross enrolment rate increased from 38 per cent in 2007 to 47.8 per cent in 2010, while net

Figure 3.35: Average primary and secondary net enrolment rates for selected countries, 2001-2009



	UK	Korea	Chile	Botswana	Egypt	Indonesia	S. Africa	Kenya	Ghana	Nigeria	Uganda	Sub-Sahara Africa	Medium Dev.	High Dev.
Secondary	104	98.6	94.4	87.2	93.6	94.8	87.5	91.5	73.9	61.4	97.1	73.6	88.5	94.4
NER 2001-2009 Secondary	91.3	96.4	85.3	56.5	71.2	69.7	71.9	38.4	46.4	25.8	19.2	29.5	57	74.9

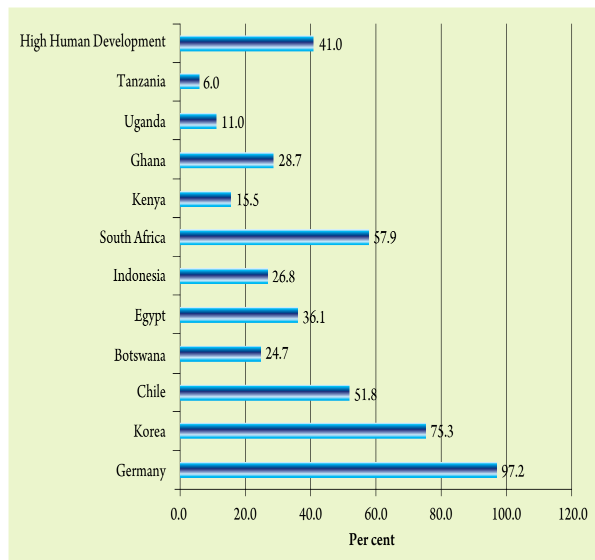
Source: UNDP (2010)

enrolment rate rose from 24.2 per cent in 2007 to 32 per cent in 2010.

Cross-country data as shown in Figure 3.35 indicates that Kenya's NER at the primary and secondary levels are above the Sub-Sahara Africa averages of 74 per cent and 29.5 per cent, respectively. However, Kenya's secondary school NER of 32 per cent in 2010 was lower than for Korea (96.4%) and South Africa (71.9%). The average for medium human development countries was 57 per cent (Figure 3.35). It is evident that although there is considerable progress in primary education participation levels, there is need for enhanced access to post-secondary education.

In 2010, for instance, only 15.5 per cent of Kenya's population aged 25 years and above had attained at least secondary education. This was relatively low when compared with the levels attained by comparable countries such as South Africa (57.9%) and Botswana (24.7%) (Figure 3.36).

Figure 3.36: Population with at least secondary education (% ages 25 and older), 2010



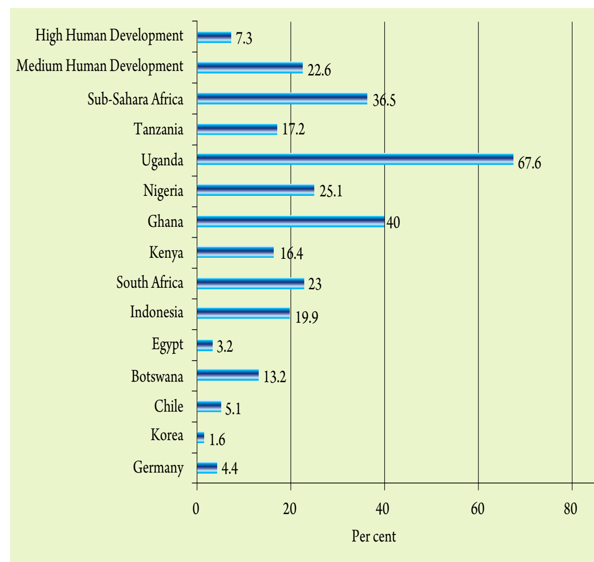
Source: UNDP (2010)

Internal efficiency

Drop-out rate

Dropout rate is a measure of internal efficiency of any education system. It constitutes the percentage of students to total enrolment who exit the system at any given level. It is also assumed that transfer into is equal to transfer out of education and/or the effect, if any, is negligible. During the period between 2005-2008, Kenya's dropout rate was estimated at 16.4 per cent and was relatively higher than for Korea (1.6%), but lower than the Sub-Saharan average of 36.5 per cent (Figure 3.37). Although it is not possible to estimate the direct cost associated with dropping out of school, the indicator depicts wastage in the learning process and it leads to lower class sizes and under-utilization of available physical and human resources in learning institutions. Further, pupils who drop out before completing the school cycle do not also attain the requisite skills for sustainable development.

Figure 3.37: Average primary dropout rate (% of primary school cohort), 2005-2008



Source: UNDP (2010)

Repetition rate

Grade repetition in primary schools is a common phenomenon in most countries, Kenya included

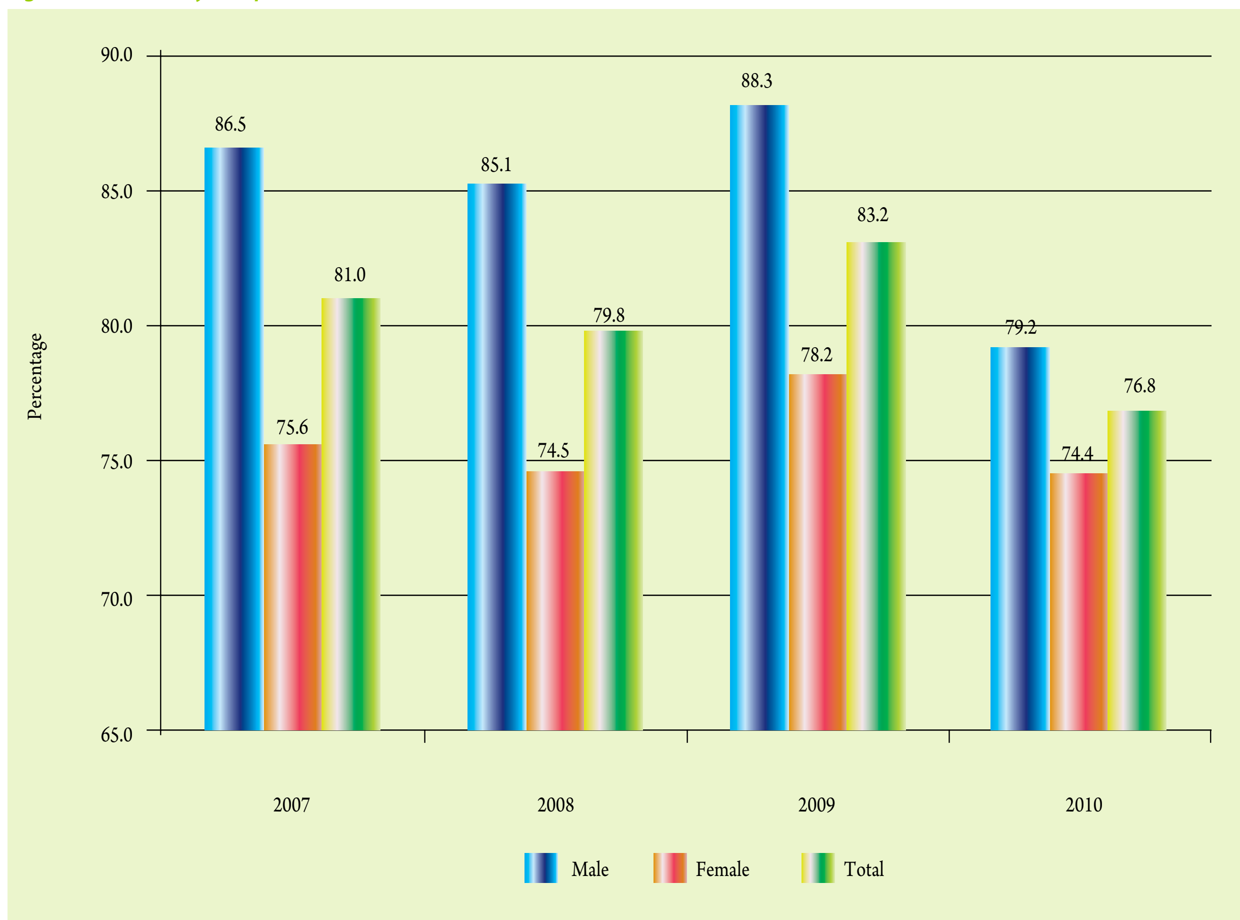
(Figure 3.38). The main motive of repetition is to improve performance in student test scores. Although there is a government policy of non-repetition, an average of about 5.8 per cent of primary school children was observed to have repeated a class between 2005-2008.

Repetition rates were relatively low for Egypt and Chile; but medium human development countries recorded a high of 6.5 per cent despite their level of human resource development. Given that the Government of Kenya through FPE allocates US$ 14.6 per student per year in Kenya, the repetition rate translates into an annual total loss of US$ 7.9 million to cater for over 544,110 repeaters per year.

Primary completion rate

Primary completion rate was estimated at 76.8 per cent in 2010, having declined from 81 per cent in 2007 (Figure 3.39). This implies that despite the improvement in access to schooling, the number of pupils who completed grade (class) 8 as a proportion of the total population aged 13 years declined during the review period. This issue requires further

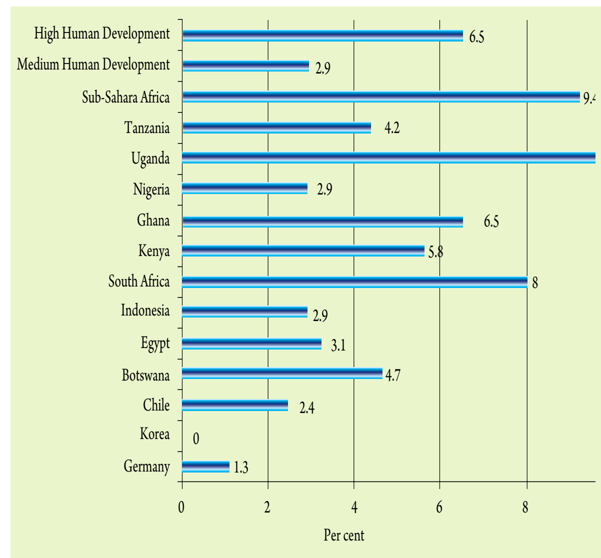
Figure 3.38: Primary completion rate, 2007-2010 (%)



Source: Ministry of Education, Education Management Information System (EMIS)

investigation, given its implications on education policy targets.

Figure 3.39: Primary repetition rate (% of primary school cohort), 2005-2008

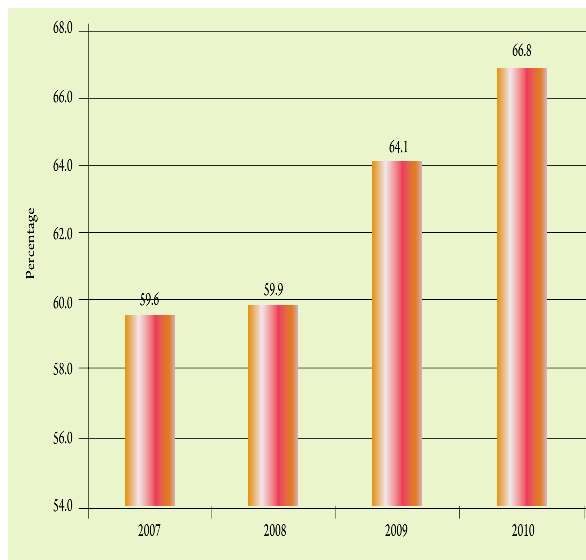


Source: UNDP (2010)

Transition rates

Transition rate between Standard 8 and Form I was about 59.6 per cent in 2007 and 66.8 per cent in 2010 (Figure 3.40). Transition is affected to some extent by lack of capacity and low educational attainments among those who complete Standard 8, which means that some students have not met the minimum requirements to join secondary education. Transition from secondary to university education is relatively low compared to transition from primary to secondary education. The highest rate achieved recently was a transition rate of 6.5 per cent in 2008.

Figure 3.40: Transition to secondary education, 2007-2010 (%)

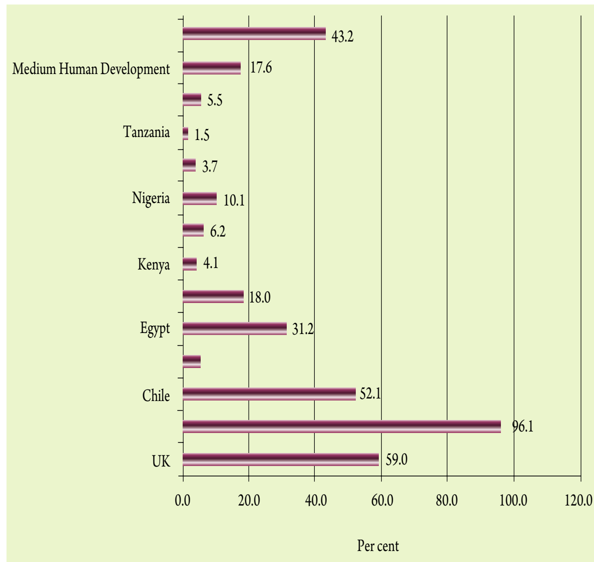


Source: Ministry of Education, Education Management Information System (EMIS)

Access to tertiary education

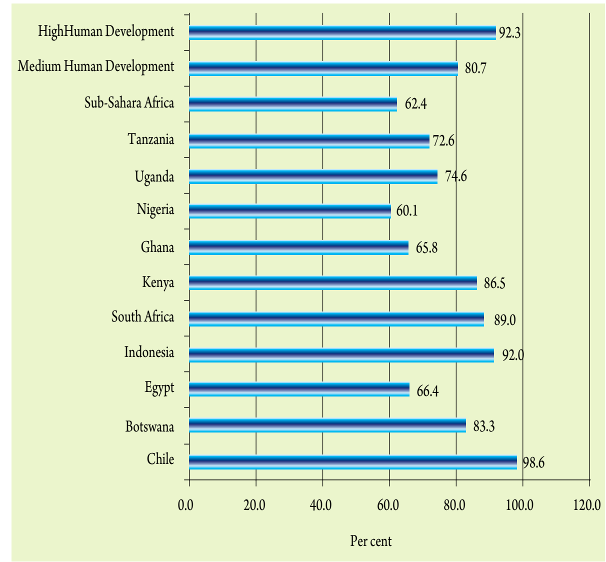
The tertiary education GER for Kenya was 4.1 per cent in 2007-2010 and was lower than that of South Africa (5.5%), Egypt (31.2%) and the Republic of Korea (96.1%) (Figure 3.41). A related challenge that can be observed from the analysis is the relatively lower percentage of females enrolled in Kenya's tertiary education institutions (36% in 2010). The implication of the low access rates at secondary and tertiary levels of education is that interventions to boost access to post-secondary education would form a key strategy to improve supply of skilled human resource for key development sectors in the economy.

Figure 3.41: Average tertiary gross enrolment rate (% of tertiary school age population), 2007-2010



Source: UNDP (2010)

Figure 3.42: Adult literacy rates for selected countries, 2005-2008

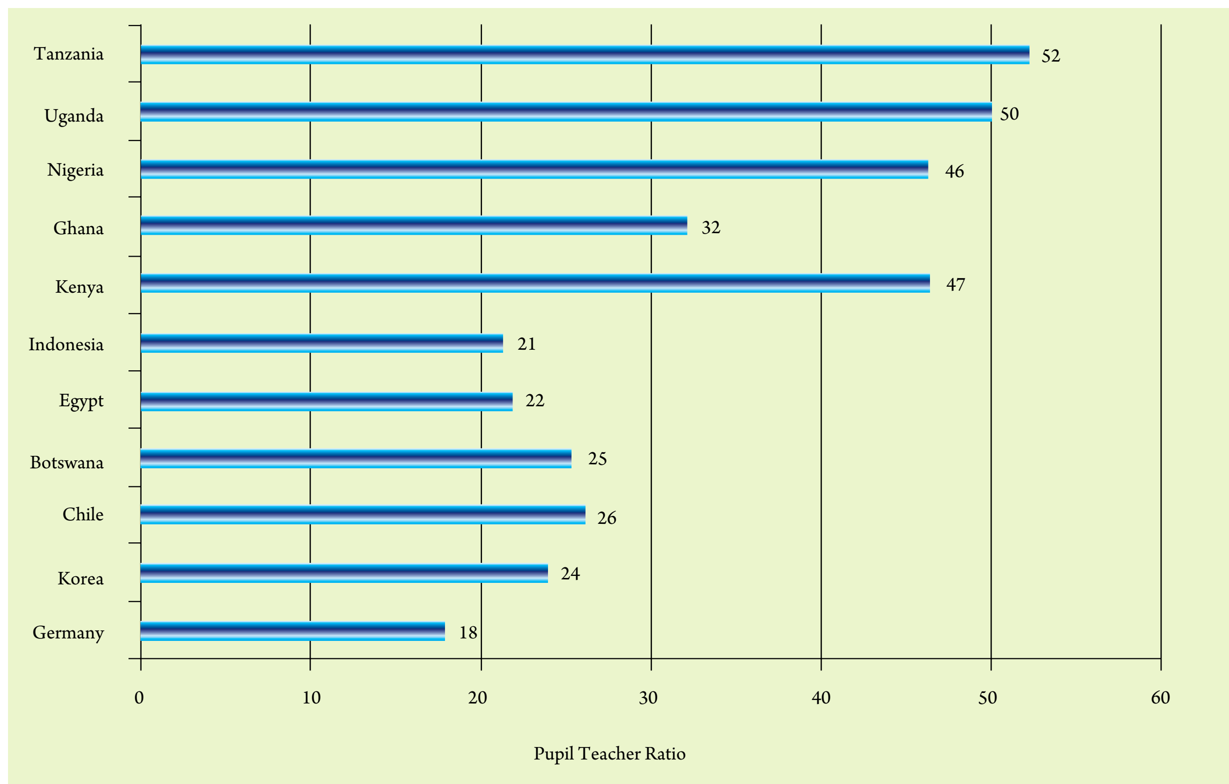


Source: UNDP (2010)

Figure 3.43: Average and expected years of schooling, 2010

Source: UNDP (2010)

Figure 3.44: Mean primary pupil teacher ratio, 2005-2008



Source: UNDP (2010)

Adult literacy levels

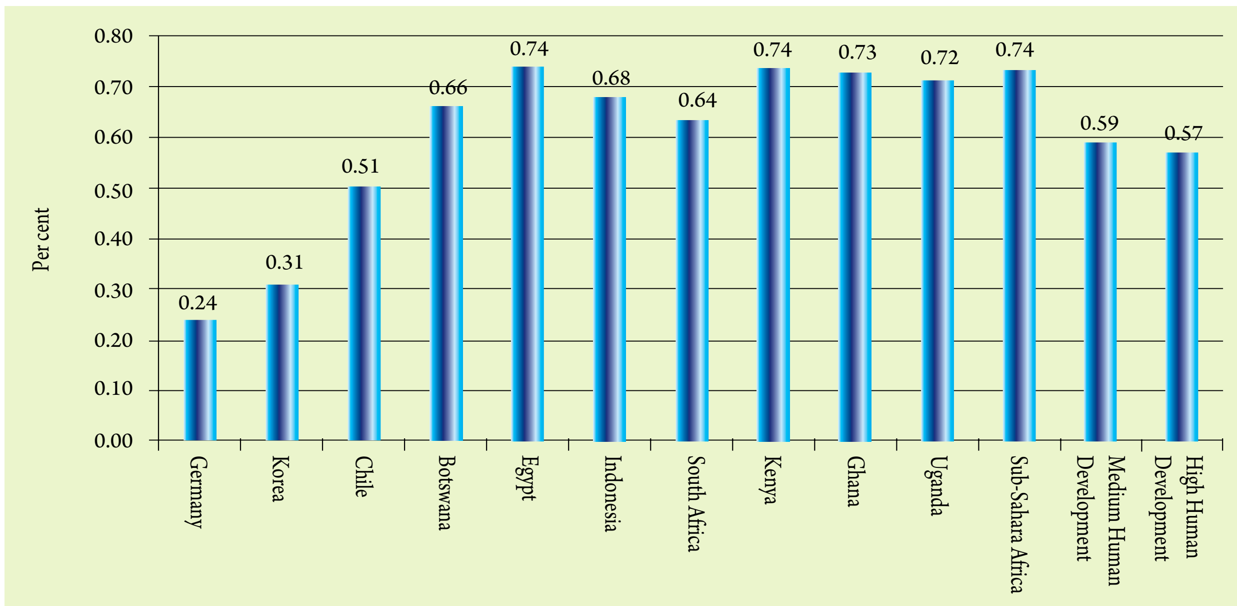
Using 2005-08 data for selected countries, it can be seen that the adult literacy rate was 86.5 per cent for Kenya compared to 98.6 per cent for Chile and an average of 92.3 per cent for countries with high human development indices. However, the adult literacy rate is still low in relation to the comparator countries such as South Africa (89%) and Indonesia (92 per cent). This translates to an illiteracy rate of 13.5 per cent for Kenya. Perhaps, this is due to the low access and participation rate at post-primary education and regional inequalities in education service delivery observed in the preceding sections of this report.

On the other hand, the average years of schooling for Kenya are only 7 years against the expected 9.6 years. Both educational years are lower than for Germany and Korea, which have attained close to 12 years of schooling against the expected 15.6 and 16.8 years, respectively. Unlike Kenya, where the average population has only attained primary education, majority population for developed economies such as Germany (97.2%), Korea (75.3%) and South Africa (57.9%) have attained at least secondary education (Figure 3.36). This has enabled these countries attain high levels of human resource development.

Pupil-teacher ratio

The pupil-teacher ratio (PTR) is used as proxy for quality of education. Currently, the policy target is to attain a pupil-teacher ratio of 40:1 but this could be increased to 45:1 for high potential areas and 25:1 for low potential areas (Government of Kenya, 2010). According to the 2010 data, primary PTR is estimated at 47:1, an indication of large class sizes in some schools across the country (Figure 3.44). The lowest PTR was recorded in developed economies such as Germany (18:1) and Indonesia (21:1). The latter countries also have a high human development index.

Figure 3.45: Gender inequality index, 2010



Source: UNDP (2010)

Inequalities in access to education

Inequality in access to education can be defined in terms of gender, income and locality differences. Gender inequity refers to the extent to which the traditionally disadvantaged gender groups, such as females, have opportunities to access various levels of education, succeed in education and make use of the education and training as an asset for enhancing their chances in life, such as in employment. Income-related inequality focuses on the extent to which the financially disadvantaged groups have access to various levels of education. Under locality-related equity, we present challenges to education opportunities for people living in disadvantaged regions such as marginalized rural areas and income poor, including the hard-to-reach and marginalized areas and urban informal settlements.

Gender equity

The Gender Inequality Index (GII) measures equity across gender in human resource development. It is a composite index capturing loss in achievements in three dimensions of human development, namely, health, empowerment (including attainment at secondary and university education) and labour market participation due to gender differences. The human development report (UNDP, 2010) shows that the Gender Inequality Index for Kenya was estimated at 0.74, meaning the male population is advantaged in terms of the three dimensions mentioned above, relative to their female counterparts. This level was similar to that of Egypt and Sub-Saharan average, but higher than the index for Korea (0.31) and Chile (0.51) (Figure 3.45). Factors contributing to the high gender inequality index for Kenya include the disadvantaged position of women in the access to secondary and tertiary education, and low labour force participation.

Locality-related equity

Estimates on regional, gender and income inequalities in gross enrolment in primary schools using KIHBS 2005/06 show that gross enrolment in rural areas was 120 per cent compared to the urban gross enrolment of 114 per cent (Table 3.14). The low gross enrolment in urban areas relative to rural areas can be attributed to inadequate provision of schooling infrastructure in urban informal settlements, especially in Nairobi and Coast provinces.

The lowest gross enrolment rate of 73 per cent (89% for boys and 55% for girls) was recorded in North Eastern Province, while the highest gross enrolment rate of 127 per cent was recorded in Eastern, Nyanza and Western provinces. The low enrolment rates in North Eastern Province can be associated with such factors as high direct and indirect schooling costs including uniform, poverty, socio-cultural challenges in some places and limited school infrastructure and related long distances that pupils have to cover to school.

Table 3.14: Primary and secondary gross enrolment rates by region, province and wealth quintile, 2005/06 (%)

	Primary			Secondary		
	Male	Female	All	Male	Female	All
Residence						
Urban	115	112	114	59	51	55
Rural	122	119	120	40	36	38
Province						
Nairobi	105	115	110	85	71	79
Central	120	123	122	56	51	53
Coast	121	108	114	26	21	23
Eastern	124	129	127	36	33	35
Nyanza	134	121	127	47	47	47
Rift Valley	117	114	116	43	38	41
Western	127	127	127	41	31	36
North Eastern	89	55	73	20	9	15
Wealth Quintile						
Lowest	117	114	115	16	14	15
Second	131	124	128	30	25	28
Middle	122	119	121	49	39	44
Fourth	119	121	120	59	56	57
Highest	112	108	110	80	72	76
All Kenya	121	118	119	43	38	41

Source: Demery and Gaddis (2009)

Income-related equity

Despite elimination of primary school user fee, some children are out of school at all levels. The degree of out of school children is higher among the low income groups and at secondary school level. Using 2005-06 data, enrolment was also highest among the second lowest wealth quintile (131%) with a surge in primary enrolment recorded among the poorest income group for both boys and girls. Children from poor families are out of school due to direct costs such as uniform as well as indirect costs or the opportunity costs of schooling.

Overall, the lowest income quintile benefits more from primary education, while post-primary education benefits predominantly the high income quintiles. In 2005/06, for instance, 17.4 per cent of the low income group benefitted from overall expenditures on education, compared to 23.7 per cent of the high income group. About 24.7 per cent of the poorest quintile benefitted from primary education, 9.5 per cent from secondary education, and 1.9 per cent from tertiary education. These levels were lower when compared with the benefit incidence for the high income group, which was estimated at 27.2 per cent for secondary and 70 per cent for tertiary education. The benefit incidence was higher for males than for females at all levels of education.

Table 3.15: Gender differences in education sector benefit incidence (% of total subsidies)

Quintile		Poorest Quintile	Quin-tile 2	Quin-tile 3	Quin-tile 4	Richest Quin-tile	Kenya
Pri-mary	Both	24.7	25.2	21.6	18.2	10.2	100
	Male	12.8	12.9	10.8	9.3	5.1	50.9
	Fe-male	11.9	12.3	10.9	9.0	5.1	49.2
Sec-ondary	Both	9.5	5.9	21.9	5.5	27.2	100.0
	Males	4.8	9.2	12.7	12.4	3.6	52.7
	Fe-male	4.7	6.8	9.2	13.1	13.6	47.4
Tertiary	Both	1.9	2.0	7.0	19.1	70.0	100.0
	Male	1.9	1.4	5.8	5.6	76.0	62.3
	Fe-male	-	0.6	1.2	3.5	32.4	37.7
All Edu-cation	Both	17.4	19.3	19.4	20.2	23.7	100.0
	Males	9.1	0.2	0.5	11.0	2.2	53.0
	Fe-male	8.3	9.1	9.0	9.2	11.4	47.0

Source: Demery and Gaddis (2009)

The findings show that higher education is generally accessible to the higher socio-economic groups and that the cost of education is greatest for tertiary education, compared with other levels of education. This means that untargeted education financing might be enforcing the socio-economic advantage of the high income groups, and this might worsen the inequality problems in both higher education and take up of employment opportunities. Besides, although primary and secondary education (day) are by law free from direct school charges, there are unofficial levies that put financial burdens on the income-poor households. Moreover, financial burdens on the poor, which include school fees and opportunity costs, are increasingly high in secondary and higher education levels. All these work to constrain the poor from accessing education opportunities at the various levels.

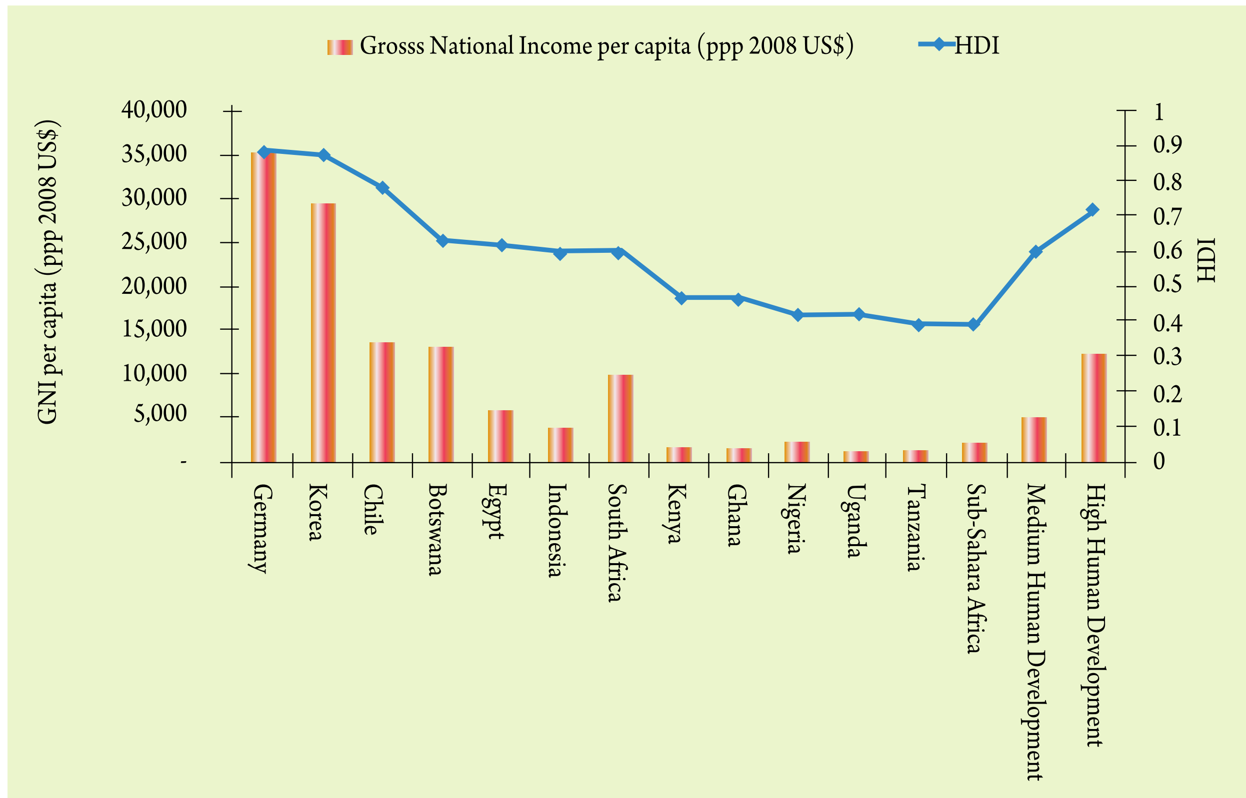
Human Development Index

In 2010, Kenya had a relatively low Human Development Index (HDI) of 0.47 compared to South Africa (0.597), Indonesia (0.60) and Botswana (0.633) (Table 3.16). The respective indices for Korea (0.877), Chile (0.783), Germany (0.885) and overall average for countries with high human development (0.717) are all above 0.70; the Sub-Saharan average was 0.592.

Table 3.16: Human Development Index, 2005-2010

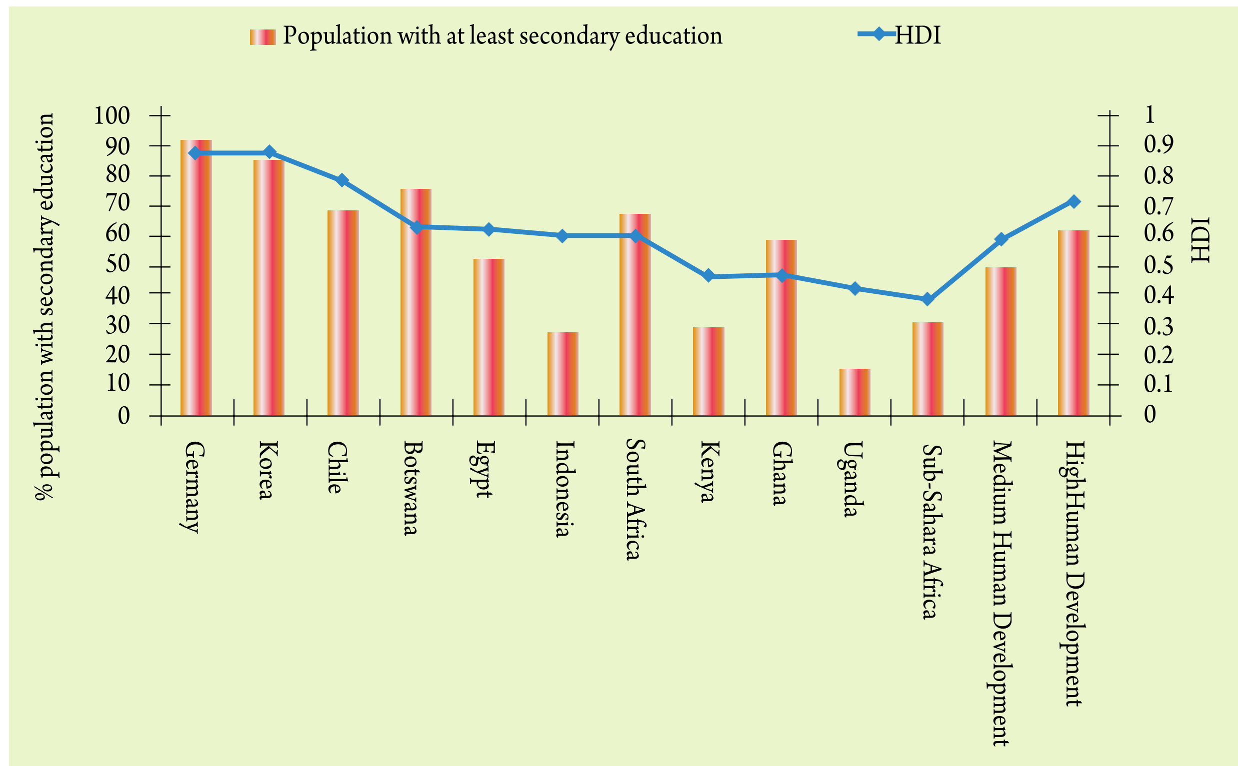
	2005	2009	2010
Germany	0.878	0.883	0.885
Korea	0.851	0.872	0.877
Chile	0.762	0.779	0.783
Botswana	0.593	0.627	0.633
Egypt	0.587	0.614	0.620
Indonesia	0.561	0.593	0.600

Figure 3.46: Gross National Income (GNI) per capita PPP 2008, US$ and HDI



Source: UNDP (2010)

Figure 3.47: Population with at least secondary education (% age 25 and older) and HDI



Source: UNDP (2010)

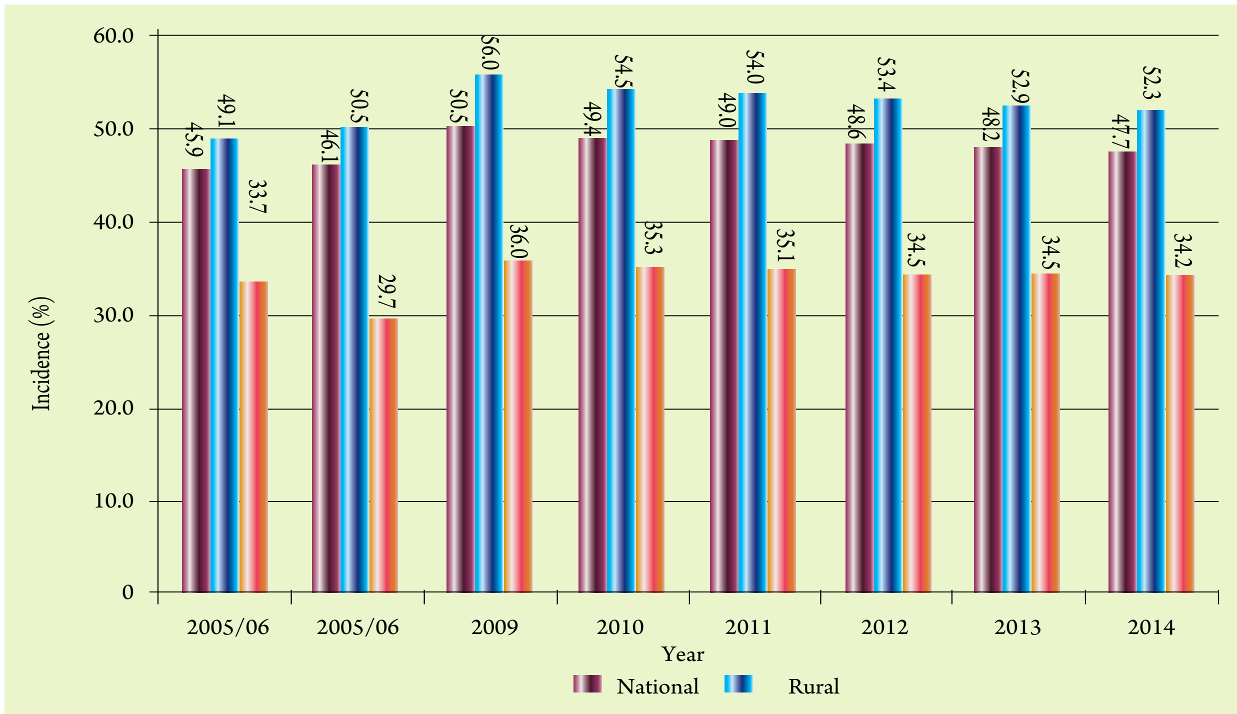
	2005	2009	2010
South Africa	0.587	0.594	0.597
Kenya	0.443	0.464	0.470
Ghana	0.443	0.463	0.467
Nigeria	0.402	0.419	0.423
Uganda	0.380	0.416	0.422
Tanzania	0.370	0.392	0.398
Sub-Saharan Africa	0.366	0.384	0.389
Medium human development	0.555	0.586	0.592
High human development	0.692	0.712	0.717

Source: UNDP (2010)

The high HDI for Botswana relative to Kenya can be attributed to strong institutions and strong economic growth (UNDP, 2010) relative to other countries such as Nigeria that have abundant natural resources but have low economic performance and HDI. Botswana had the third highest growth rate in gross national income per capita over the last 30 years, behind only China and South Korea. This in part was due to mineral resource income (mainly diamond) that enabled high and sustainable financing of infrastructure, education and health; and strong institutions and reforms instituted in early 1990s to curb corruption, which included establishment of an independent Ombudsman's office.

In Figures 3.46 and 3.47, we attempt to assess the correlation between HDI on one hand, and GNI per capita and access to secondary education on the other hand. Indeed, HDI increases with an increase in economic performance of any country as measured by the GNI per capita and purchasing power parity. Countries with low proportions of populations with secondary education also have low human development. Thus, for Kenya to produce the critical mass of human resource required for attainment of Vision 2030, it is important to address factors that are constraining access to post-primary education, besides ensuring sustainable economic growth accompanied with better standards of living.

Figure 3.48: Poverty headcount ratio (%) 2005/06-2014



Source: Predictions using KIHBS 2005/06

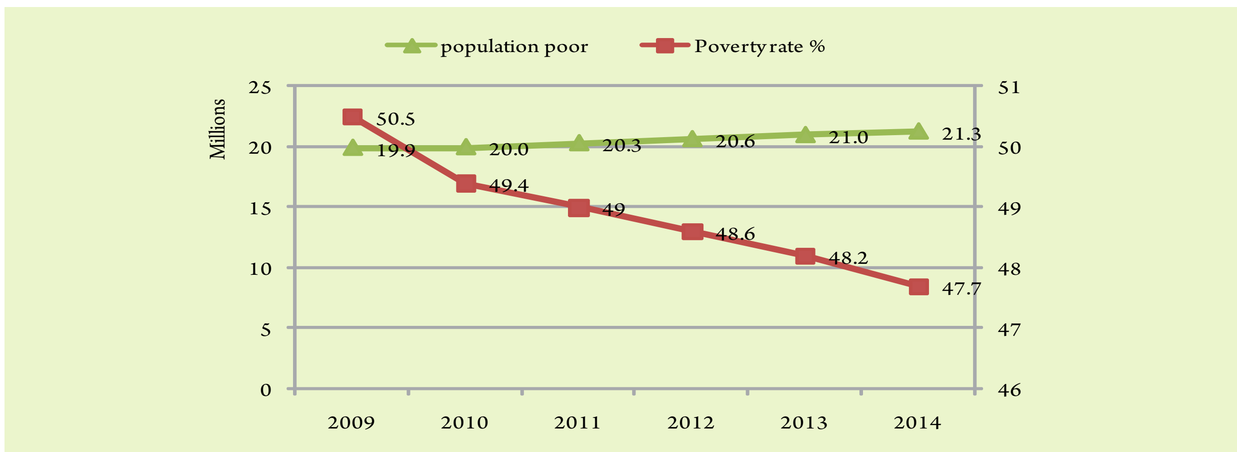
3.7 Medium Term Prospects

This section highlights prospects in areas of poverty reduction, education, and health over the next three years. The related specific reforms and institutional priorities identified in previous sections are also outlined.

3.7.1 Medium Term Prospects for Poverty Reduction

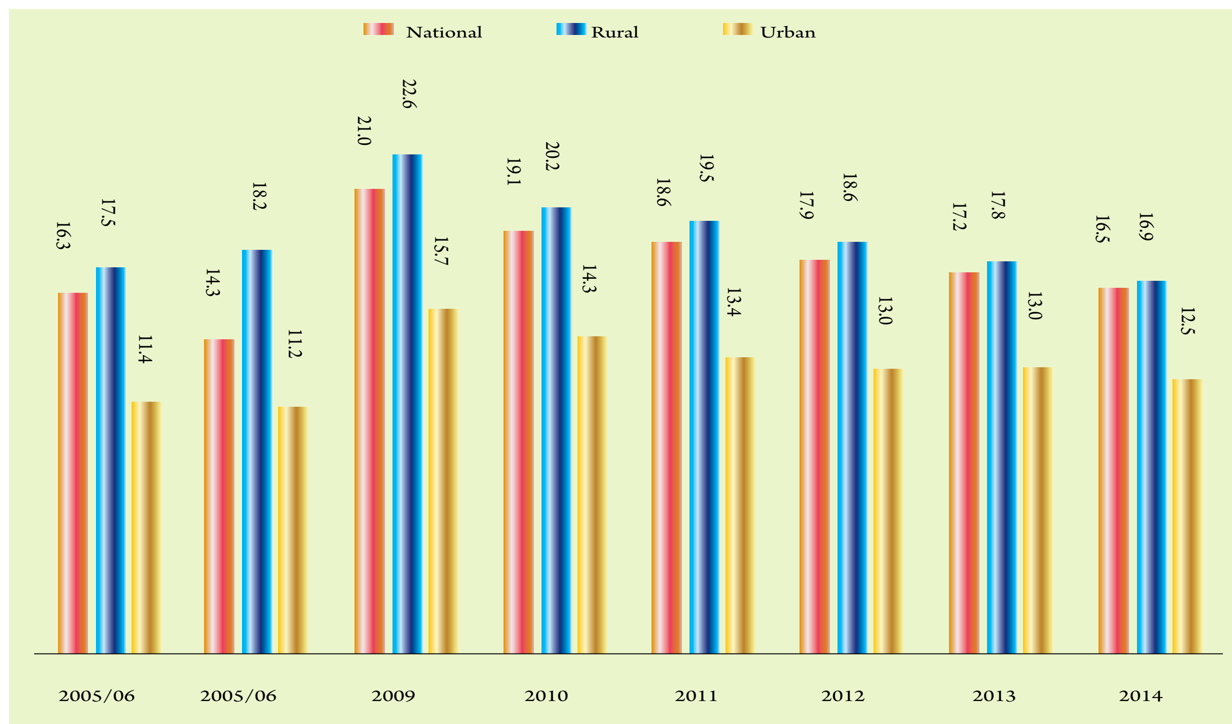
Poverty is dynamic and varies from one region to another. In order to determine the medium term prospects for poverty reduction, the recent household survey would be the best data source to inform the projections. However, it is expensive to collect annual household data at the national level. In Kenya, KIHBS 2005/06 is the most recent household and budget survey available. This report uses a methodology developed by Mwabu

Figure 3.49: Number of poor individuals in the population



Source: Authors' computation using population projections from KTMM

Figure 3.50: Poverty depth (%) 2005/06-2014



Source: Predictions using KIHBS 2005/06

et al. (2003) to make poverty projections using the KIHBS 2005/06. The underlying model asserts that poverty is a function of growth and inequality. The growth projections used here are GDP projections discussed in the macroeconomic section of this report. We assume that the future Gini coefficient is the same as for the previous years, that is about 0.41.

Eradicating poverty remains a challenge that the government cannot ignore (as shown in Figure 3.46). According to the KIHBS 2005/06, the proportion of Kenyans living in poverty in 2005/06 was 46 per cent of approximately 30 million people at the time. Despite moderate economic growth, the gains in poverty reduction have been minimal over the past five years. Between 2005/06 and 2010, the national poverty rate was projected to have increased to 50.5 per cent in 2009, but instead declined minimally to 49.5 per cent in 2010. During this period, rural poverty increased from 49.1 per cent in 2005/06 to 56.0 per cent, the highest ever, but declined slightly to 54.5 per cent in 2010. Unlike the national poverty headcount ratio, urban poverty remained low during the same period.

On the medium term projections, Figure 3.48 shows that rural poverty headcount ratio remains high with very small reductions between 2011 and 2014. Given the projected economic growth rates, it is evident that the number of poor people in the rural population is extremely high compared to the poor population in the urban areas.

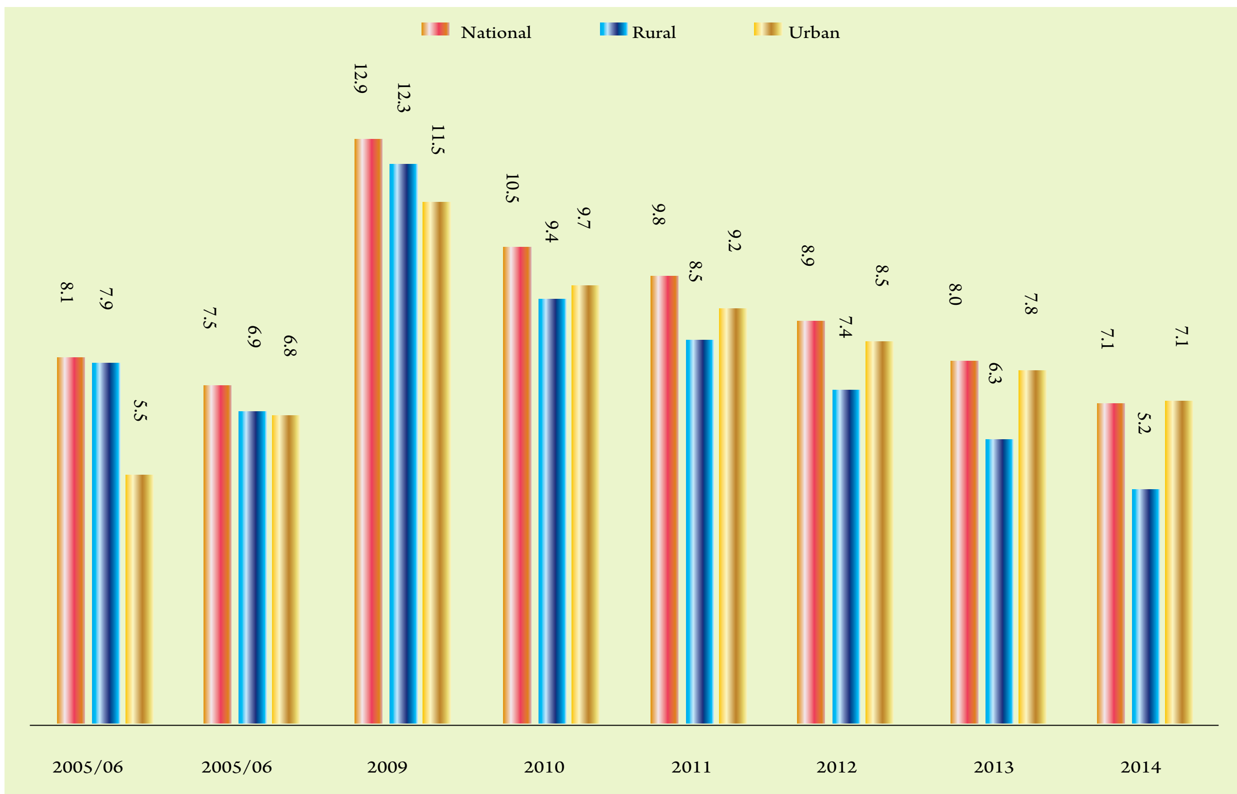
Using population projections from the KTMM, it is envisaged that despite the decline in the percentage of the population living in poverty, the absolute number of the poor in the population will increase marginally. For instance, between 2011 and 2014, the number of poor people will increase from 20.3 million to 21.3 million. This means that an additional one million people will fall into poverty by the year 2014 (Figure 3.49). The exact number of the population below the poverty line would very much depend on the kind of policies and institutions that will prevail in the economy at that time.

While headcount ratio is a good predictor of the overall poverty level in the population, it does not provide any information on how poor the poor are. For this reason, a different poverty indicator is used to reveal the intensity (or depth) of poverty. It is measured as the average income shortfall of the poor person from the poverty line. The larger the poverty gap, the poorer the individual. According to Figure 3.50, the poverty depth increased from 16.3 per cent to 21.0 per cent at the national level, between 2005/06 and 2009. This means that, on average, the poor in 2005/06 had an expenditure shortfall of about 16.3 per cent of the poverty line whereas the poor in 2009 had an expenditure shortfall of 21.0 per cent of the poverty line. According to the projections, poverty depth will decline to 17.9 per cent in 2012 and further decline to 16.5 per cent in 2014. However, the absolute number of the poor population will increase over the years. The rural estimates worsened to peak at 17.5 and 22.6 per cent, respectively, during the same period. The projected reduction in the rural poverty gap during 2011 to 2014 (from 20.2% to 16.9%) implies implementation of policies beneficial to the poor over the period, but such reduction is insufficient to lift them out of poverty. While the urban poverty gap is projected to decline only marginally during the same period, it nonetheless remains relatively low. The per capita cost of eliminating poverty will depend on the absolute poverty line for the respective years.

The above scenario has the implication that the envisaged policies for the medium term should be designed to equitably benefit the poor in rural areas, where the deprivation is most severe.

Another indicator of poverty that is sensitive to income disparities among the poor is poverty severity. It attributes more weight to the poorest of the poor. Between 2009 and 2014, it is projected that poverty severity would decline gradually from a high of 12.9 per cent to 7.1 per cent at the national level (Figure 3.51).

Figure 3.51: Projected poverty severity (%)



Source: Predictions using KIHBS 2005/06

As can be seen from Figure 3.51, the rural poverty severity index is projected to decline from 12.3 to 5.2 per cent over the medium term. These impressive reductions could be interpreted to mean that anti-poverty programmes for the period are strongly pro-poor. Some of these programmes, which have direct impact on the incomes of the poor, include the social protection activities that fall under various ministries within the government. Despite the fact that these programmes target both rural and urban areas, the impact on poverty severity differs across regions. These differences could, to a certain extent, be attributed to prevailing regional differences in resource endowments.

3.7.2 Medium Term Prospects for Education

The education sector has recorded impressive performance in the last decade following the expansion in enrolment across all education levels and improved transition to secondary education. As indicated earlier, in 2010, the country achieved a net enrolment rate of 91.4 per cent and 38.4 per cent for primary and secondary education, respectively. Primary completion rate was 76.8 per cent, while transition rate from primary to secondary education was recorded at 66.8 per cent during the same period. However, the country's policy target is to increase primary net enrolment and completion rates to 100 per cent by 2015; to reduce regional disparities in access to primary education; to increase primary to secondary transition rate to 75 per cent by 2012; and to increase secondary to university transition rate to over 10 per cent by 2015.

Table 3.17: ECDE, primary and secondary enrolment projections, 2009-2014 (millions)

Population	2009 (Actual)	2010	2011	2012	2013	2014
ECDE (4-5 Years)	2.40	2.68	2.75	2.82	2.88	2.95
Primary (6-13 Years)	8.50	8.60	8.78	9.26	9.74	10.22
Secondary (14-17 Years)	3.14	3.20	3.24	3.33	3.43	3.53
ECDE						
Public	1.30	1.37	1.42	1.47	1.52	1.57
Private	0.60	0.63	0.65	0.67	0.70	0.71
Total	1.90	2.00	2.07	2.14	2.22	2.29
GER (%)	74	75	75	76	77	78
Primary Education						
Public	8.11	8.48	8.85	9.21	9.61	10.05
Private	0.83	0.86	0.88	0.90	0.92	0.94
Total	8.94	9.34	9.73	10.11	10.53	10.99
GER (%)	110	109	111	109	108	108
Secondary Education						
Public	1.39	1.58	1.82	2.01	2.11	2.17
Private	0.16	0.16	0.17	0.17	0.17	0.18
Total	1.55	1.75	1.99	2.18	2.28	2.34
GER (%)	45	48	61	65	66	66

Source: KIPPRA Estimates based on the Education Simulation and Financial Projection Model, 2010; 2009 Kenya Population and Housing Census Volume 1C.

Other policy targets include improving quality and internal efficiency across all education levels by reducing dropout and repetition; improving adult literacy; ensuring equitable access to basic and continuing education; improving quality of physical facilities in learning institutions; and quality delivery of science and technology among other higher education programmes. Strengthening of public private partnerships, especially at tertiary education level, is a potential intervention aimed at enabling the country expand access to higher education.

On the other hand, the expansion in this sector will depend on the growth in the school age population over time. For instance, the school age population aged 4-5 years is expected to increase from 2.4 million to about 2.95 million by 2014. Primary school age population is expected to increase from 8.5 million children to 10.22 million children by 2014, while the secondary school age population (14-17 years) is expected to rise from 3.14 million in 2009 to about 3.53 million by 2014.

Table 3.18: Performance of health indicators 2009/10

Medium Term Plan Output/ Outcome	Indicator	Unit	Target 2009/10	Achievement 2009/10	Remarks
Reduced under-five mortality	Under-five mortality rate	Per 1,000	55	74	Not achieved
Reduced maternal mortality	Maternal mortality rate	Per 100,000	254	488	Not achieved
Increased proportion of skilled attendant at birth	Skilled attendant at birth	%	64	43	Not achieved
Immunization coverage	Children under 1 year fully immunized	%	85	77	Not achieved
Reduced HIV prevalence	HIV prevalence rate	%	6.4	6.3	Achieved
Access to HIV health care services	Patients on ARVs	%	60	56.2	Not achieved. Lack of funds to upscale
Reduced Malaria incidence	Proportion of inpatients with malaria	Ratio	17	16	Almost achieved. Challenge: High resistance to Malaria drugs

Source: Ministry of State for Planning, National Development and Vision 2030 (2011)

Taking these policy targets and expected school age population growth into account, ECDE enrolment is projected to increase from 1.9 million in 2009 to 2.3 million in 2014. On the other hand, primary school enrolment is expected to increase from 8.9 million in 2009 to 10.9 million students in 2014. Secondary school enrolment is projected at 2.34 million by 2014, up from 1.55 million in 2009 (Table 3.17).

Gross enrolment rates at ECDE, primary and secondary levels are projected at 78 per cent, 108 per cent and 66 per cent by 2014, respectively, indicating the country is on track towards achieving the national sector targets. However, there is need to address regional disparities in the sector and relatively low transition rates across education levels. Further, the envisaged expansion calls for substantial investment (human resource and physical infrastructure) in

Table 3.19: Kenya's status with respect to the Millennium Development Goals (selected indicators)

MDG Goal No.	Target	MDG Baseline 1990	MDG Goal 2015	Current Estimate
Child health (MDG 4)	Prevalence of underweight children < 5 years (%)	32.5	16.2	11
	Reduce IMR/1000 by 2/3 between 1990 and 2015	67.7	25	52
	Reduce UMR/1000 by 2/3 between 1990 and 2015	98.9	33	74
	Proportion of 1 year olds immunized against Measles (%)	48	90	80
Maternal, - sexual reproductive health (MDG 5)	Reduce MMR/100,000 by 3/4 between 1990 and 2015	590	147	488
	Proportion of births attended by skilled health staff (%)	51	90	47
	Coverage of Basic Emergency Obstetric Care (BEOC)	N/S	100	24
	% WRA receiving family planning commodities	N/S	70	43
Disease control (MDG 6)	Pregnant women/children<5 sleeping under ITNs (%)	N/S	80/80	40/39
	TB case detection rate (%)	NS	60	47
	Treatment completion rates (Smear +ve cases) (%)	75	90	80

Source: WHO Regional Office for Africa (2009)

the sector and improved efficiency in utilization of existing resources.

3.7.3 Medium Term Prospects for Health Outcomes

Despite some good progress in the health indicators over the last five years, Kenya is still far below the MDG targets and other local medium term targets. The targets set in the Medium Term Plan of Kenya Vision 2030 for the financial year 2009/10 and the associated achievements are shown in Table 3.18.

The national under-five mortality rate stood at 74 per 1,000 with regional estimates ranging from 51 per 1,000 in Central Province to 121 per 1,000 in Western and 149 per 1,000 in Nyanza. There has been considerable decline in child mortality rates (infant mortality, neonatal and under-five) despite the disparities. However, the under-five mortality target for 55 per 1,000 live births set by the sector for 2009/10 was not met as shown in Table 3.18.

Likewise, other health indicators such as maternal mortality, skilled birth attendants and immunization coverage did not change as expected. However, the target for HIV prevalence reduction was achieved, whereas targets for access to ARVs and Malaria incidence reduction were missed by about 0.1 and 1.0 percentage points, respectively.

Table 3.19 shows MDG targets against achievements for different health indicators. Kenya is still far below the MDG targets for most of the health indicators. Declines from high initial levels of infant mortality are driven mainly by reductions in the number of post-neonatal deaths (i.e., deaths occurring between the age of one month and twelve months). These deaths are more easily averted by the typical (and relatively inexpensive) child survival interventions, such as child immunizations and oral rehydration therapy. However, as the overall level of infant mortality comes down, further reductions in infant mortality can only be obtained via reductions in neonatal mortality. Averting neonatal deaths typically requires more expensive interventions, such as professionally-attended deliveries, prompt treatment of neonatal infections (such as pneumonia), and availability of emergency obstetric care at lower levels of health-care facilities. Thus, sustained infant mortality reduction becomes increasingly more difficult and expensive. In Kenya, more than three quarters of infant deaths now occur in the first month of life, therefore, future reductions in infant mortality will have to be driven largely by reductions in neonatal mortality, which are considerably more difficult and expensive to attain.

The fifth Millennium Development Goal is to reduce the maternal mortality rate by 75 per cent between 1990 and 2015. The 2008-09 KDHS results show that maternal mortality remains high in Kenya. A strategy essential to reducing the high maternal mortality rates is to ensure that all births are managed by skilled health professionals. Currently, the proportion of births managed by health professionals and the proportion delivered in a health facility are 44 per cent and 43 per cent, respectively.

The prospects of Kenya attaining the health MDGs and other national targets are dimmed by a number of challenges, which include inadequate funding, low health facility deliveries (despite high antenatal care coverage), high poverty levels (which adversely affect health seeking behaviour of the population), inadequate and uneven distribution of health personnel (which hampers service delivery), and inadequate infrastructure.

3.8 Conclusions and Future Considerations

3.8.1 Conclusion and Synthesis of Key Issues

The country is experiencing a major demographic transition. This is evidenced by the rising life expectancy, improvement in dependency ratio, declining HIV prevalence, declining mortality rates

and low birth rates. The demographic transition will have implications on the labour market and location and nature of demand for goods and services.

The labour market has been dynamic as characterized by rapid increase in the working age population. Despite the increase in labour force participation rates, most of the jobs are being created in the informal sector, which is characterized by relatively low productivity and earnings. This has resulted into the emerging challenge of the working poor. Other challenges include: high rates of unemployment and underemployment and skills mismatch.

According to the Global Competitiveness Report (WEF, 2010), Kenya's formal labour market is relatively efficient. This is characterized by high ranking in cooperation in labour-employer relations, flexibility in wage determination, hiring and firing practices, redundancy costs and the extent to which pay relates to productivity in the formal sector. Kenya faces challenges in a number of indicators that would greatly undermine creation of formal jobs. These include perceptions that the total tax rate is high, high number of procedures required to start a business, and a high burden of customs procedures. Other areas posing a challenge include: payment of bribes, burdensome government regulations, business costs of crime and violence, organized crime, and unethical behaviour of firms.

There are inequalities in access to education at all levels and low access to post-primary education. Although the government spends over 7 per cent of GDP on education, the performance indicators are unsatisfactory. Access to post-primary education is low and levels of performance vary across regions, gender and income groups. The marginalized areas and urban informal settlements have low education participation rates, while higher income groups benefit more from post-primary education relative to the low income groups. The Gender Inequality Index (GII), which captures equity across gender in human resource development in terms of the three dimensions of human development (health, empowerment and labour market participation), shows that the male population is more advantaged relative to their female counterparts.

There is a weak balance between increased access to basic education and quality of education service delivery. In addition, the process of monitoring education performance and learning is either weak and/or non-existent at both local and national levels. The low education attainment levels are also associated with the evident low health outcomes, unemployment and high poverty across regions and among the population.

There is low skills development, low integration of ICT in learning processes and low innovation. Tertiary and research institutions are weak in delivering capital intensive and high technology skills and focus on soft skills. Uptake of science and technology disciplines is also low, hence little innovation.

Although most health outcome indicators improved during the review period, the mortality rates are still below the MDG targets. Some of the indicators that recorded a positive trend include life expectancy, skilled birth attendance and HIV prevalence rates. Maternal mortality and under-five mortality rates improved, but the levels are still below the MDG targets.

Health sector financing is unsustainable as characterized by low public spending and high donor dependence. The interventions include: real increases in financial resources for health, additional health workers and health facilities. The country is lagging behind in relation to the requirements set by UN MDGs and the WHO and Abuja Declaration for health funding. Much remains to be done to lift the health sector in Kenya to the standards envisioned in Vision 2030. In order to bring about reasonable improvements and meet local and international targets for the health sector, a number of challenges need to be addressed which include: inadequate funding to support planned and initiated projects,

low health facility deliveries despite high antenatal care (ANC) coverage, high poverty levels (which affect health seeking behaviour of the population), inadequate and uneven distribution of health personnel (which hampers service delivery) and inadequate infrastructure.

Poverty and regional and income inequalities still remain a challenge to long-term development of the economy. In 2010, the poverty incidence was estimated at 49.5 per cent, having worsened from 45.9 per cent in 2005/06. Inequality is another aspect that negatively affects both poverty and growth. This negative relationship extends to human development indicators as measured by health, education and living standards. These call for effective economic growth and redistribution policies for sustainable development.

3.8.2 Recommendations and Future Considerations

Effective management of Kenya's demographic transition

For Kenya to benefit from its demographic transition, there is need to invest in human capital development including health, education and quality job creation, especially for the youth.

There is need to create not only more jobs but also jobs perceived to be of good quality in both the formal and informal sectors. This can be done through further enhancing the role of the private sector, for example, by improving the complex tax compliance procedures. Other interventions include skills development for workers with low education and training levels; addressing unemployment especially among the youth; deepening skills development, and ensuring the creation of good quality jobs in both the formal and informal sectors.

Linking macroeconomic growth targets to redistributive interventions including cluster development, addressing unemployment and social protection programmes targeting the vulnerable groups in society is critical. Policy suggestions towards addressing the labour market, health and education follow:

Labour

i. Creation of good quality jobs in the dynamic labour force calls for accelerated and sustained high rates of economic growth and emphasis on increasing total factor productivity across all production units. This can be achieved by reducing the cost of doing business and keeping political and macroeconomic risks low. Simplifying registration processes, improving governance and physical infrastructure, and curtailing crime should be a top priority for the government.

ii. Given that agriculture is one of the sectors with the largest potential for job creation, there is need for increased investment in irrigation. Improvements in all forms of infrastructure such as supply of energy, rehabilitation of roads, supply of water and provision of other social amenities can lead to increase in agricultural productivity and better investment climate for rural non-farm enterprises. This will create jobs in rural areas and stem rural–urban migration and related urban unemployment issues. Effective implementation of the Constitution has potential to create jobs at the local level.

iii. Financial assistance programmes are popular interventions aimed at empowering the unemployed workforce, especially the youth. The Youth Enterprise Development Fund (YEDF) should consider enhancing systematic and targeted training as a way of complementing the funding function. Other interventions include efficient business support services and monitoring and evaluation framework for job creation interventions. The framework will also enable assessment of the quantity and quality of

jobs being created in all sectors of the economy: public, private, agriculture, and informal sectors. Furthermore, an integrated employment and wealth creation programme for micro and small enterprises should be implemented.

iv. Institutions such as decentralized labour market information system and institutionalization of school-to-work transition mechanisms will improve the design of employment policies and programmes for the youth. This will help assess the relative ease or difficulty of the youth's transition from school to work life. It will also help identify levels of skills needs; perceptions and aspirations in terms of employment; job search processes; barriers to entry into the labour market; and the preference for wage employment versus self-employment and required interventions.

v. The rapid informalization of the labour market and the economy poses a challenge due to low productivity, and hence low earnings in some of the activities. There is need to further reduce the costs of firm formalization to encourage informal firms that wish to become formal to do so if it would enhance their productivity. Increase in casual workforce is another aspect of informalization. Employment safety regulations aimed at protecting workers' welfare as recommended in the new labour laws should be upheld and should cover casual workers while addressing issues of worker exploitation.

Health

The key issue that needs to be addressed in the health sector is financing. Adequate financing will address the other underlying issues of inadequate and demoralized health workers, inadequate health infrastructure and medical supplies. In addition, more resources will be channelled to preventive care, which will help ease the burden of disease by improving water and sanitation, among other preventive measures. If the above issues are addressed, health outcomes will ultimately improve.

Heath financing, therefore, needs to be addressed by:

1. Increasing government allocations to the health sector: As noted from the analysis above, government allocations to the health sector fall far below the Abuja Declaration of 15 per cent of GDP (government allocation is 4.3% of GDP). Countries with much lower per capita incomes than Kenya are allocating more to the health sector.

2. Finding new sources of funds: This could be done by encouraging and supporting community health insurance schemes and micro insurance. This will go a long way in addressing the problem of access to health services.

3. Earmarked funds: The government could introduce earmarked taxes going directly to funding the health sector or specific interventions in the health sector. Taxes such as cigarette and beer taxes (commonly referred to as 'sin taxes') could be channelled directly to financing health sector activities. This is because consumption of these products sometimes ends up adding to the burden of disease, and thereby adding to the financial burden of the health sector.

4. Strengthen partnerships: There is also need to enhance private sector participation in funding of health sector activities. This should be coordinated and channelled to priority areas in the health sector. For instance, many private companies target some activities in the health sector for their corporate social responsibilities. This could be coordinated so that the money is channelled to priority areas in the health sector. Also, more private players should be encouraged to come on board. This could then lead to a collaboration and partnership with the private sector, whose policies and services have

an impact on health outcomes with enhanced joint planning, funding and monitoring arrangements.

Education

1. Increasing equity and access for the poor: Effective government intervention is needed to ensure equitable access to educational resources and facilities. This is critical because the effectiveness of the recent policy reforms in the sector (such as Free Primary Education and Free Day Secondary Education) largely depends on the extent to which the interventions take account of the needs and circumstances of regional disparities, the poor and their involvement in the design and implementation of the programmes. This could include targeted policy effort encouraging poorer households to enrol their children at appropriate levels of schooling.

2. Increase access to post-primary education: There is need for programmes aimed at increasing transition across levels of education and expanding access to post-primary education. These are critical for improvements in human capital development in the country. Specific interventions towards addressing internal efficiency challenges (dropout, repetition and low transition across levels) include enforcing the non-repetition policy in schools, and institutionalizing automatic promotion from primary to secondary education, while ensuring that every Kenyan child has access to basic education and remains in school until they attain the age of 17 years.

3. Improving quality of basic education: Ensuring a balance between increased access to basic education and high quality of education service delivery within the free primary and secondary education schooling programmes is critical. It is also important to note that improvements in schooling quality, efficiency and equity depend on a nexus of teaching and learning factors. Schooling and the general formal teaching and learning environment can also be influenced by resources, and how individual schools translate inputs to expected outputs and outcomes. Enhancing the quality and effectiveness of management of learning institutions is also important.

4. Design technology for assessing and monitoring education quality at the school level: To help monitor and sustain continuous improvement in education, there is need at all levels for innovative intervention within the context of decentralization for participatory decision making. Head teachers, in order to provide leadership and mobilization of community support, should be able to assess and implement corrective measures aimed at improving education quality of their schools and use the information in strengthening school strategic plans.

   For instance, improving quality and efficiency of the teaching and learning processes in classrooms and schools depends on information of the actual and feasible teaching and learning conditions. One approach to building a supporting information base is to develop easily quantifiable, identifiable and monitorable indicators at school level that take into account the teaching and learning processes. The indicators should reflect the government education targets such as adequate facilities, availability and utilization of instructional materials, pupil-teacher ratio, class size and school attendance (teachers and pupils) and school performance and general learning achievements. The performance indicators can then be adapted by counties, school committees, teachers and other local level management organs.

ENDNOTES

[1] 2008 is the latest date for statistics on delivery in a health facility by province from KDHS 2008-09.

[2] Data on contraceptive use by province is available only in KDHS's.

[3] Fully immunized include BCG, Measles, and 3 doses each of DPT and Polio Vaccine (excluding Polio Vaccine given at birth).

PART II

Sectoral Performance

This part provides an analysis of key sectors of the economy, namely: Infrastructure and Economic Services (Chapter 4), Tourism (Chapter 5), Agriculture (Chapter 6), Wholesale and Retail Trade (Chapter 7), Micro and Small Enterprises (Chapter 8), Manufacturing (Chapter 9), Business Process Outsourcing/Offshoring (Chapter 10), Financial Services (Chapter 11), and Environment and Natural Resources (Chapter 12).

Chapter 4

Infrastructure and Economic Services

4.1 Introduction

The term infrastructure refers to the technical structures that support a society, such as roads, water supply, sewers, power grids, telecommunications and so forth. Viewed functionally, infrastructure facilitates the production of goods and services. Successful infrastructure development necessitates appropriate institutional arrangements.

World Concerns indicates that infrastructure is a basic and a necessary requirement for achievement of any of the MDGs. The growth of infrastructure lies in having strong institutions, the right policies, increased funding, greater efficiency and a responsible private sector. Inadequate infrastructure can deter foreign investors. Research shows that inadequate public infrastructure tends to drive away foreign investment, while quality infrastructure attracts private investment. Public infrastructure is also related to productivity. Congestion, for example, takes a major economic toll–it slows movement of goods and impacts productivity. The port of Mombasa is estimated to incur cost of congestion (in terms of lost time and fuel consumption) of 35 metric tonnes per day; waiting period immediately translates to close to US$200,000. Modern infrastructure also creates employment opportunities and attracts skilled knowledge workers, increasing the country's growth and competitiveness.

Table 4.1: Infrastructure contribution to GDP (%)

Infrastructure	2007	2008	2009	2010*
National GDP growth	7.1	1.7	2.6	5.6
Electricity and water	1.5	1.2.1	2.4	2.4
• Electricity	0.8	1.5	1.7	1.7
• Water supply	0.6	0.6	0.6	0.7
Construction	3.8	3.8	4.1	4.3
Transport and communication	10.6	10.2	9.8	9.8
• Transport and storage	7.6	7.5	7.2	7.3
• Post and telecommunications	3.0	2.7	2.6	2.5
Real estate-renting and business services	5.3	5.1	4.9	4.8
• Real estate dwellings, owner-occupied and rented	2.7	2.5	2.5	2.4
• Real estate-renting and business services	2.6	2.6	2.5	2.4
Total infrastructure	21.2	19.1	21.2	21.3

* Provisional figures
Source: Government of Kenya (2011b)

Infrastructure contribution to GDP rose from 21.2 per cent to 21.3 per cent in 2007 to 2010. The largest contribution of GDP from infrastructure came from transport and communication, which stood at a lower value of 9.8 per cent in 2010 down from 10.6 per cent in 2007 (Table 4.1).

Electricity and water performance increased from 1.5 per cent in 2007 to 2.4 per cent in 2010. This was due to increased demand in energy as a result of a stable macroeconomic environment and peace in the country. Conversely, the real estate sub-sector (which includes dwellings, rented and owner-occupied as well as real estate-renting and business services performance) was moderately stable at 2.7 per cent and 2.6 per cent, respectively, in 2007 but went to 2.4 per cent in 2010. The post and telecommunications sub-sector recorded a high contribution of 3 per cent in 2007, but declined slightly to 2.4 per cent in 2010. Water supply and construction stood at 0.7 per cent and 4.3 per cent in 2010 up from 0.6 per cent and 3.8 per cent in 2007. Water supply had the lowest contribution to infrastructure.

4.2 Expenditure Review and Policy Setting

4.2.1 Analysis of Expenditure on Physical Infrastructure Sectors

An extensive and efficient infrastructure is an essential driver for growth, competiveness and overall development of the country. The government scaled up investments in key infrastructure facilities covering road network, energy supply and transport system, and port services. About Ksh 182 billion (representing 20.1% over the amount allocated in 2009/10) was allocated towards financing prioritized infrastructure development countrywide.

Funding of physical infrastructure in the country is mainly from government and with some support from donor-funded programmes. Public expenditure on physical infrastructure has in the past three years increased tremendously. According to the Public Expenditure Review 2009 (Government of Kenya, 2009), both development and recurrent expenditure saw huge increases. The development and recurrent expenditures increased from Ksh 21.84 billion and Ksh 51 billion in 2007/08, respectively, to over Ksh 40 billion and Kshs 90 billion, respectively, in 2009/10. This has mainly been driven by massive investment in road and energy sub-sectors (Table 4.2) and the shift in policy emphasis from recurrent to development expenditure.

With regard to physical infrastructure expenditure by sub-sector, the roads sub-sector realized the highest allocation. Recurrent public expenditure in roads increased from about Ksh 16.5 billion in 2007/08 to Ksh 21.4 billion in 2009/10, an increase of 29.3 per cent. In the same period, development expenditure increased from Ksh 24.6 billion to Ksh 46.4 billion, an increase of 88.7 per cent. This is an indication that more emphasis has been placed on roads construction and long-term infrastructure development than in the earlier years when recurrent expenditure on roads was prominent due to increased maintenance costs. Within the same period, donor-funded roads projects increased from Ksh 25.5 billion to Ksh 26 billion (increased by 1.8%).

Table 4.2: Analysis of expenditure on physical infrastructure sectors (Ksh millions)

Year	2007/08	2008/09*	2009/10*	% Change
Analysis of actual recurrent expenditure				
Sub-sectors				
Roads	16,567	21,159	21,435	29.4
Transport	1,968	3,214	3,363	70.9
Public Works	709	3,443.59	3,384	377.3
Housing	1,294	1,716	1,857	43.5
Energy	290	366	372	28.3
Local Government	973	10,547	11,308	1062.2
Nairobi Metropolitan	37	268	339	816.2

Year	2007/08	2008/09*	2009/10*	% Change
Total	21,838	38,261	40,049	83.4
Analysis of development expenditure				
Sub-sectors				
Roads	24,596	42,353	46,437	88.8
Transport	3,244	4,231	2,481	-23.5
Public Works	1,454	2,597	2,267	55.9
Housing	1,284	2,330	2,066	60.9
Energy	17,704	30,386	31,260	76.6
Local Government	2,796	3,517	3,462	23.8
Nairobi Metropolitan	-	2,050	1,690	-
Total	51,078	88,328	90,449	77.1
Analysis of donor-funded programmes -Physical infrastructure				
Sub-sectors	2007/08	2008/09*	2009/2010*	
Roads	25,543	25,558	26,000	1.8
Transport	4,789	2,739	1,943	-59.4
Public Works	115	80	-	-
Housing	68	179	176	158.8
Energy	6,775	7,816	8,042	18.7
Local Government	101	1,263	1,500	1,385.1
Nairobi Metropolitan	-	50	-	-
Total	37,391	37,685	37,661	0.7
Total	**110,307**	**164,274**	**168,159**	**52.4**

Source: Ministry of Finance (2009)

In the transport sub-sector, development expenditure declined from Ksh 3.2 billion in 2007/08 to Ksh 2.45 billion in 2009/10 (reduced by 23.5%). Development expenditure in the energy sub-sector showed tremendous progress, standing at Ksh 31.2 billion in 2009/10 (76.5% increase) from Ksh 17.7 billion in 2007/08.

From 2007/08 to 2009/10, public works recurrent expenditure increased, while that of development expenditure and donor-funded programmes dropped. The recurrent allocations for housing reduced, while for development expenditure and donor-funded programmes increased. In the same period, local government and Nairobi Metropolitan donor-funded programmes and both recurrent and development expenditure increased.

4.2.2 Analysis of Resource Allocation and Utilization in Infrastructure Sub-sectors

The physical infrastructure sector in Kenya faces major limitations and inefficiencies. The most typical and chronic obstacle has been inadequate resource allocation. This scenario is further complicated by low absorption rates of the financial resources allocated to the sector over the years, a fact that can exact a strong argument against increased budgetary allocations to such a highly deserving but grossly underfunded sector.

Analysis of recent recurrent and development resource requirements and allocation and absorption rates gives a clearer picture of the shortcomings that institutions must effectively address. Under the recurrent resource account, the roads and transport sub-sectors lead with deficits running into several billions; Ksh 5.4 billion for roads and Ksh 2.5 billion for transport in the 2011/12 financial year. The development resource account displays a different picture with the highest deficits ranging from Ksh 8 billion to over Ksh 20 billion in the energy, local government and housing development sub-sectors. These are also the sub-sectors experiencing very high unmet infrastructure demand. Less than 20 per cent of Kenyans have access to electricity and the unmet housing demand exceeds 100,000 units per year. Tables 4.3, 4.4. and 4.5 show the most recent estimates from the Medium Term Expenditure Framework (MTEF).

Table 4.3: Analysis of recurrent resource requirements vs allocation (Ksh millions)

Sub-sector	Estimates 2010/11	Requirements Vs Allocation		
		Requirement-2011/12	Allocation-2011/12	Variance
Roads	25,548	31,040	25,646	-5,394.0
Transport	4,430	6,357	3,816	-2,541.0
Public Works	1,470.72	1,827	1,519.04	-308.0
Housing	977.8	2,170	1,702	-468.0
Energy	2,283.29	2,682.87	2,381	-301.9
Local Govt.	13,201	15,135	14,243	-892.0
Nairobi Metro	319	580	334	-246.0
Total	48,229.81	59,791.87	49,641.04	-10,150.83

Source: Government of Kenya (2011a)

Table 4.4: Analysis of development resource requirements vs allocation (Ksh millions)

Sub-sector	Estimates 2010/11	Requirements Vs Allocation		
		Requirement	Allocation	Variance
		2011/12	2011/12	
Roads	79,194	87,276	81,299	-5,977
Transport	7,213	13,378	9,255	-4,123
Public Works	5,051.9	9,561	6,052	-3,509
Housing	2,982	11,045	2,782	-8,263
Energy	34,072.85	65,448.38	44,880	-20,568
Local Govt	5,799	17,865	4,486	-13,379
Nairobi Metro	1,158	9,132	1,558	-7,574
Total	**135,470.75**	**213,705.38**	**150,312**	**-63,393**

Source: Government of Kenya (2011a)

Analysis of recurrent and development expenditure from 2007/08 to 2009/10 exposes the low level of budget execution, especially in the roads and transport sub-sectors. Underlying these poor results are causes that can be traced back to failures in the institutional environment. There has been general under-utilization of both recurrent and development expenditure, but to a much higher degree under the development vote. Between 2007/08 and 2009/10, the average under-utilization of development expenditure was a significant 28.7 per cent. The approved and actual development expenditure budget on the physical infrastructure sector has been increasing steadily since 2007/08. This improved budgetary allocation is in harmony with the recognition of infrastructure as a critical foundation of Vision 2030. The roads and transport sub-sectors score high absorption rates for recurrent expenditure, but return the lowest absorption rates for development expenditure. The low absorption rates can be linked mainly to procurement challenges, which also affect donor-funded projects. Delayed exchequer releases have also been blamed for the low absorption rates (Government of Kenya, 2011b).

Table 4.5: Analysis of development expenditure (Ksh millions)

Sub-sectors	Approved Estimates			Actual Expenditures			Absorption Rate: Actual/Approved%		Rate
	2007/08	2008/09	2009/10	2007/08	2008/09	2009/10	2007/08	2008/09	2009/10
Roads	33,682	46,437	58,491	24,597	36,279	36,577	73	78	63
Transport	4,789	2,482	5,792	3,324	2,013	3,548	69	81	61
Public Works	1,705	2,287	3,971	1,454	2,137	3,007	85	93	76
Housing	1,364	2,066	2,074	1,284	1,900	2063	94	92	99
Energy	21,075	31,260	33,118	17,704	30,560	32,513	84	98	98
Local Government	2,973	2,375	4,556	2,796	2,057	1,988	94	87	44
Nairobi Metropolitan Development	0	1,650	1,420	0	1,150	1,144	-	70	81
TOTAL	65,588	88,557	109,422	51,159	76,096	80,840	78	86	74

Source: Government of Kenya (2011a)

Legal constraints and conflicts also cause delays and low execution by hindering the acquisition of space for infrastructure development. Cases of expensive and controversial land acquisition and contravention of property rights need to be addressed effectively.

Table 4.6: Analysis of recurrent expenditure for the sector (Ksh millions)

Sub-sectors	Approved Estimates			Actual Expenditures			Absorption Rate: Actual/ Approved%		
	2007/08	2008/09	2009/10	2007/08	2008/09	2009/10	2007/08	2008/09	2009/10
Roads	24,400	21,159	21,852	17,277	20,647	20,969	71	98	96
Transport	4,021	3,214	3,389	3,937	3,191	3,286	98	99	97
Public Works	792	991	1,671	709	929	1232	90	94	74
Housing	1,766	1,715	1,836.50	1,293	1,433	1,515.30	73	84	83
Energy	322	365	409.3	290	348	362	90	95	88
Local Government	1,005	1,296	11,348	963	1,078	11,330	96	83	100
Nairobi Metropolitan Development	42	268	338	39	266	299	93	99	88
TOTAL	32,348	29,008	40,843.80	24,508	27,892	38,993.30	76	96	95

Source: Government of Kenya (2011a)

4.3 Performance Indicators

4.3.1 Transport

Analysis of the transport sector performance reveals that the sum of value of outputs grew from Ksh 383 billion in 2007 to Ksh 550 billion in 2010 (Table 4.7). In 2010, the road transport sub-sector had the highest value of outputs standing at Ksh 331 billion followed by air transport at Ksh 80 billion, then pipeline transport at Ksh 64 billion, water transport at Ksh 21 billion and the least being rail transport at Ksh 2 billion. Services incidental to transport stood at Ksh 49 billion in 2010. The total value of outputs in the transport sector expressed as a per cent of GDP increased from 20.9 per cent in 2007 to 21.6 per cent in 2010. However, there was a decrease in 2009 recording 18.7 per cent of GDP.

Road transport

Road transport is still the main artery of transport in Kenya and the region. Safety of the mode is, however, in question given the high road crash rates in the country and the attendant high transaction costs. The remarkable improvement in road network quality has only worsened Kenya's road crash and fatality records, a paradox that is worrying road users and decision makers alike. The proportion of Kenya's paved road network was approximately 12 per cent by the year 2011, which is still far below a country such as Egypt (87%).

Table 4.7:Value of outputs in the transport sub-sector: 2007-2010 (Ksh millions)

Transport Mode	Year			
	2007	2008	2009	2010
Road	233,224	273,047	285,250	331,948
Rail	4,550	4,449	4,356	2,208
Water	23,233	21,868	21,039	21,488
Air	80,254	83,010	80,519	80,935
Services incidental to transport	33,971	38,823	40,016	49,348
Pipeline	8,736	9,222	11,481	64,463
Total	383,968	430,419	442,661	550,390
Total outputs as per cent of GDP	20.94	20.39	18.71	21.57

Source: Government of Kenya (2011b)

The road transport sub-sector has, over the years, witnessed safety challenges associated with traffic accidents. This has become a major issue of public policy and welfare. The total number of reported traffic accidents fluctuated in the period between 2007 and 2010; the highest recorded values were

observed in 2009 with a total of 12,369 accidents. This figure dropped to 9,771 in 2010, which could be attributed to road safety campaigns by the government and other agencies. Fatalities due to traffic accidents have been on the increase, rising from 2,530 in 2007 to 3,055 in 2010, while those seriously injured and slightly injured decreased from 10,658 and 10,327 in 2007 to 9,327 and 9,739 in 2010, respectively. The rise in fatalities as opposed to the decline in injured persons could be interpreted to mean that the severity of road accidents has increased over the years, which could be attributed to increased travel speeds along improved highways. The analysis of 2010 reveals that approximately 8 people out of 100,000 died as a result of road accidents.

Table 4.8:Road safety indicators: Traffic accidents, 2007-2010

Indicator	Year			
	2007	2008	2009	2010
Total reported traffic accidents	10,225	9,093	12,369	9,771
Persons killed (fatalities)	2,530	2,463	4,072	3,055
Seriously injured	10,658	9,481	10,644	9,327
Slightly injured	10,327	9,476	11,906	9,739
Fatalities per 100,000 population	7	6	11	8

Source: Government of Kenya (2011b)

Maritime and inland waterways transport

Maritime transport (Mombasa Port) is critical to Kenya's export-led growth strategy and linking the region to the rest of the world. This mode of transport is, however, faced with many challenges, which include: high cost of transporting containers within the East African region; congestion at the ports; inadequate container capacity against the high proportion of containerized cargo and trans-shipment functions that are performing below par. The cost of importing a 20-foot container is much higher in the EAC countries (between three and five times as much as in Malaysia, Singapore and Mauritius). The import cost for a 20-foot container excluding tariffs and trade taxes for Kenya and Tanzania in 2009 was US$ 2,190 and US$ 1,475, respectively (World Bank, 2010). Under-utilization of inland waterways is another big setback to closing the logistics infrastructure.

A new container terminal in Mombasa capable of handling 1.2 million twenty-foot equivalent units (TEUs) per annum should be completed by 2013 to accommodate the port's rising throughput. BMI (2011) projected a throughput in excess of the existing capacity of 20 million tonnes to 852,461 TEUs by 2014.

Burden of customs procedures

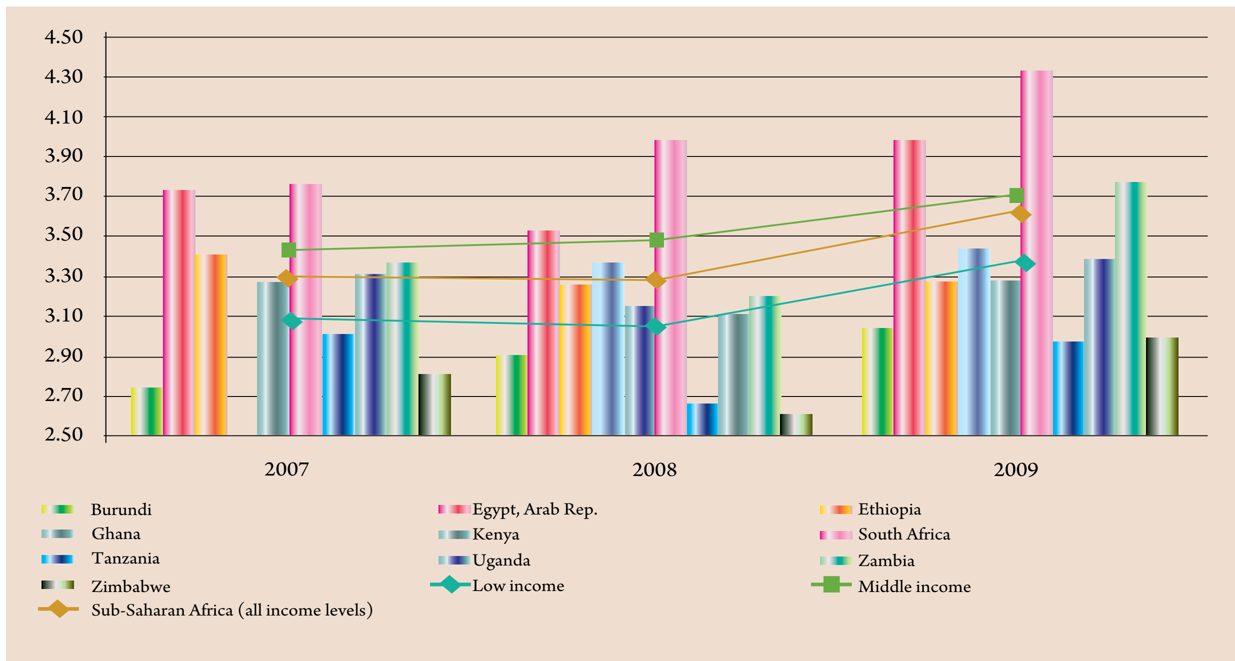
For the period 2007 to 2009, Uganda and Kenya were performing relatively well among the EAC countries in customs procedures. As shown in Figure 4.1, Burundi and Tanzania were trailing in the region (World Bank, 2010).

The Liner Shipping Connectivity Index

The Liner Shipping Connectivity Index captures how well countries are connected to global shipping networks. The index generates a value of 100 for the country with the highest average index in 2004. Kenya and Tanzania are still performing poorly on this indicator, way below South Africa and Egypt. This calls for enhancement of trans-shipment, container-carrying capacity, vessel size and number, as well as the number of shipping companies that are efficient in their scheduled services and coverage.

Improving maritime transport in the region will require keen attention on the following urgent action areas in the medium term in respect of the Port of Mombasa. The Port of Mombasa can only be the EAC's trans-shipment hub after major dredging and a determined focus to improve the performance of the port, including targeted investment in revamping the railway off-take infrastructure. There should be stronger measures aimed at reducing and

Figure 4.1: Burden of customs procedures in the EAC and other African countries



Source: World Bank (2010)

streamlining customs clearance procedures and other non-tariff barriers, as well as further reduction in waiting time at the berths and dwell time of containers by at least 50 per cent.

4.3.2 Construction and Housing

Analysis of the performance of the construction and housing sector reveals a rise in the index of completed buildings. In the private sector, the index of completed building works increased by 88 per cent between 2007 and 2009, while in the public sector the index increased by 68 per cent for the same period.

Figure 4.2: Liner shipping connectivity index

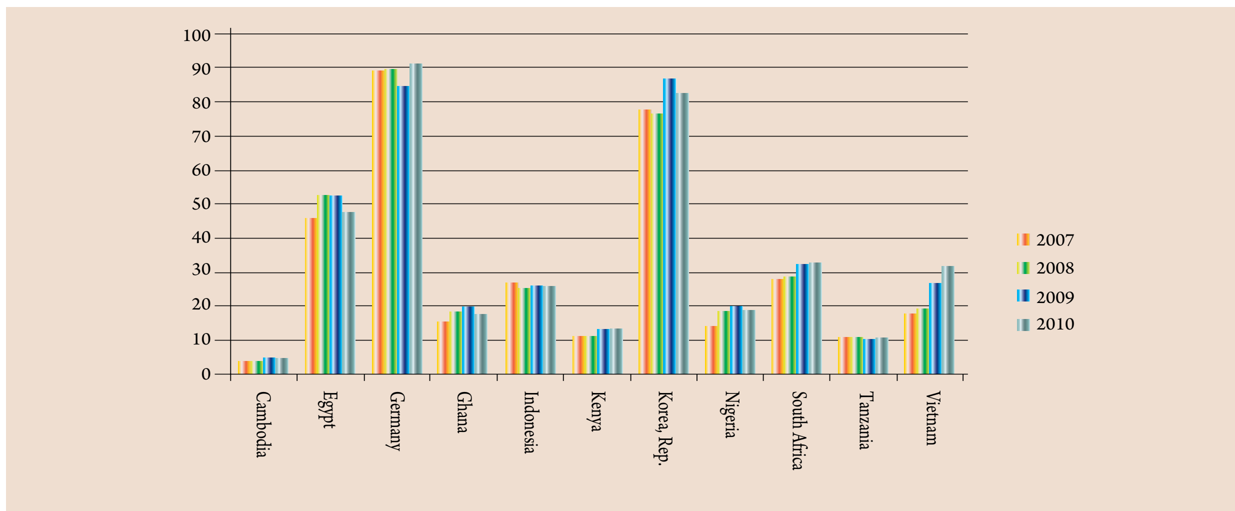


Table 4.9: Performance of the construction and housing sector, 2011

Indicator	2007	2008	2009	2010
Index of completed buildings in main towns (private sector)	108.2	142.2	203.0	
Index of completed buildings in main towns (public sector)	4.5	5.1	7.6	
Index of government expenditure on roads	219.4	223.8	312.9	394.8
Cement consumption ('000 tonnes)	2,061.4	2,205.8	2,671.2	3,104.8
Employment ('000)	81.3	84.8	93.4	101.3
Building materials cost index		7.60	3.10	3.20
Labour cost index		6.1	8.8	6.9
Value of building plans approved: Nairobi (Ksh million)	59,765.1	52,073.0	78,303.7	93,574.8
Value of building plans approved: Other towns (Ksh million)	7,322.7	17,248.7	15,888.4	17,992.9
Total value of building plans approved : % of GDP	3.6	3.3	4.0	4.4

Source: Government of Kenya (2011b)

Government expenditure on roads also witnessed an increase with an index of 219.4 in 2007 and 394.8 in 2010. This is manifested by the current and completed new roads in different parts of the country. Cement consumption went up by 50 per cent, which can be attributed to construction of roads and housing. The construction sector provided 101,300 jobs in 2010, an improvement of the 81,000 jobs provided in 2007. Interestingly, the building materials cost index went down from 7.6 in 2008 to 3.2 in 2010. The labour cost index witnessed fluctuations, recording 6.1 in 2008, 8.8 in 2009 and a drop to 6.9 in 2010. The value of building plans approved in Nairobi went up from 59.7 billion in 2007 to 93.6 billion in 2010; the same upward trend was witnessed in other towns, recording 7.3 billion in 2007 to 17.9 billion in 2010. The total value of building plans approved expressed as a percentage of GDP witnessed an increase, rising from 3.6 per cent in 2007 to 4.4 per cent of GDP in 2010.

4.3.3 Energy

The demand for petroleum products marginally increased from 3,285.7 thousand metric tonnes in 2007 to 3,979 thousand metric tonnes in 2010. On the other hand, power generation has increased from 6,324.6 GWh in 2007 to 6,975.8 GWh in 2010 (Table 4.10). The total energy consumption has marginally increased from 3,627.0 Tonnes of Oil Equivalent (TOE) in 2007 to 4, 250.7 TOE in 2010.

Table 4.10: Status of the energy sector in Kenya

Year	Petroleum demand '000 tonnes	Electricity generated GWh	Total Energy Consumption (TOE)
2007	3,285.7	6,324.6	3, 627.0
2008	3, 302.3	6, 455.6	3, 614.2
2009	3, 803.0	6, 507.2	4, 002.3
2010	3, 979.0	6, 975.8	4, 250.7

Source: Government of Kenya (2011b)

With regard to production, trade and consumption of energy expressed in terms of primary source of energy, in thousand Tonnes of Oil Equivalent (TOE), the energy consumed increased from 3,627.1 TOE in 2007 to 4,250.7 TOE in 2010. Of this consumption, the local energy production declined from 10.9 per cent in 2007 to 8.4 per cent in 2010 of the total energy consumed. This indicates

that Kenya relied heavily on imported energy, and much is needed to secure energy supply in the country. At the same time, per capita consumption in terms of kilogrammes of oil equivalent increased from 97.5 in 2007 to 107.3 in 2010.

Table 4.11: Production, trade and consumption of energy expressed in terms of primary source of energy, 2007-2009, TOE

	2007	2008	2009	2010*
Coal and Coke Consumption	109.5	108.8	94.6	165.2
Imports of Crude Oil	1,598.7	1,773.3	1,627.9	1,551.5
Net Exports of Petroleum	1,836	1902.8	2,565.6	2662.8
Stock Change and Balancing	-312.9	-543.0	-582.7	-492.2
Total Consumption of Liquid Fuels	3,121.8	3,133.1	3,610.8	3722.1
Hydro and Geothermal Energy				
Local Production of Hydropower	308.8	280.9	182.4	269.9
Local Production of Geothermal	85.0	89.3	111.2	90.9
Imports of Hydro	1.9	2.1	3.3	2.6
Total Consumption Hydro and Geothermal	395.7	372.3	296.9	363.4
Total Local Energy Production	393.8	370.2	293.6	357.4
Total Net Imports	-125.9	-18.6	-839.8	-943.5
Total Energy Consumption	3,627.1	3,614.2	4,002.3	4250.7
Local Production as Percentage of Total	10.9	10.2	7.3	8.4
Per capita Consumption in Terms of Kilogrammes of Oil Equivalent	97.5	97.5	94.4	107.3

NB: Modern sector only; fuel wood and charcoal are excluded

Source: Government of Kenya (2011b)

Alternative and nuclear energy (% of total energy use)

Clean energy is non-carbohydrate energy that does not produce carbon dioxide when generated. It includes hydropower and nuclear, geothermal and solar power, among others. Korea and Germany top the list in use of clean energy as shown in Figure 4.3 with 16.9 per cent and 12.8 per cent, respectively. Kenya ranks higher with 6.4 against Egypt, Nigeria and South Africa with 2.1, 0.5 and 4.6 per cent in that order (World Bank, 2009.)

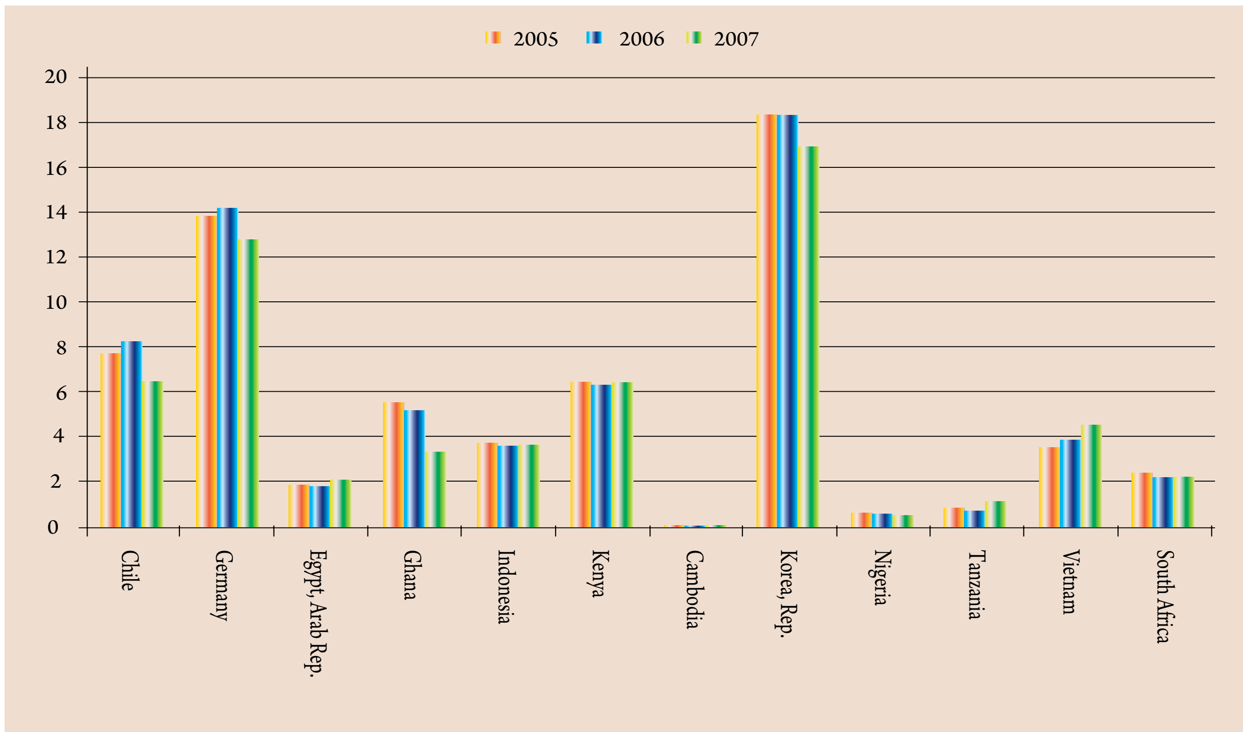
Combustible renewables and waste (% of total energy)

Combustible renewables and waste comprise solid biomass, liquid biomass, biogas, industrial and municipal waste, measured as a percentage of total energy use. Africa is leading in the performance of this sub-sector. Tanzania, Nigeria and Kenya are ranked higher with 88, 80 and 74 per cent, respectively, as shown in Figure 4.4 (World Bank, 2009).

Energy production (kt of oil equivalent)

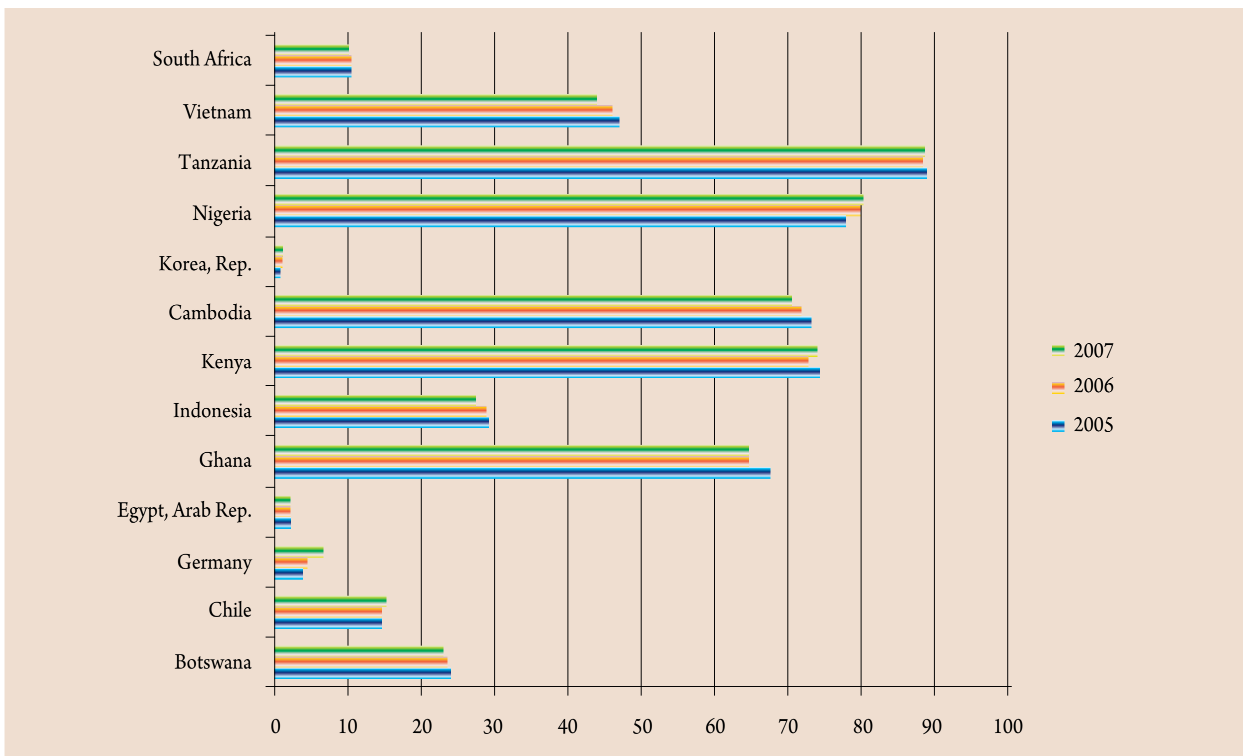
Energy production refers to forms of primary energy – petroleum (crude oil, natural gas liquids and oil from non-conventional sources), natural gas, solid fuels (coal, lignite and other derived fuels) and combustible renewables and waste – and primary electricity, all converted into oil equivalents. Indonesia, Nigeria, South Africa and Germany are highly ranked (World Bank, 2009) compared with Tanzania and Kenya, which had an energy production of 16,902 Kt and 14,725 Kt, respectively, as shown in Figure 4.5.

Figure 4.3: Alternative and nuclear energy (% of total energy use)



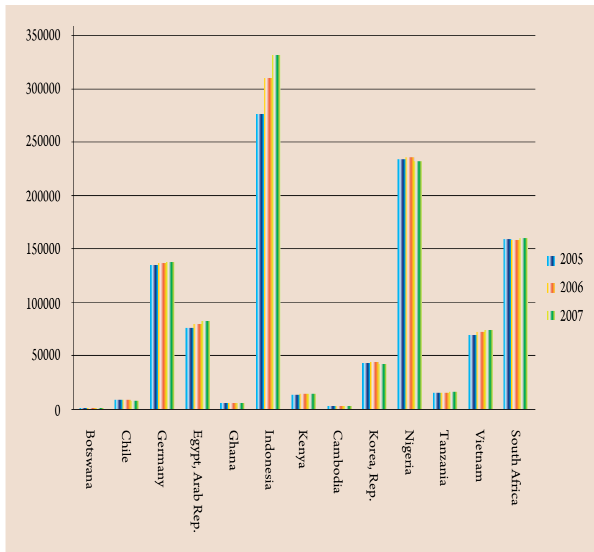
Source: World Bank (2009)

Figure 4.4: Combustible renewables and waste (% of total energy)



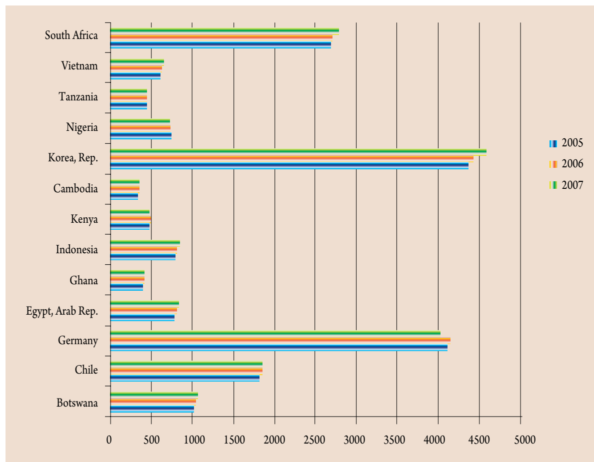
Source: World Bank (2009)

Figure 4.5: Energy production (kt of oil equivalent)



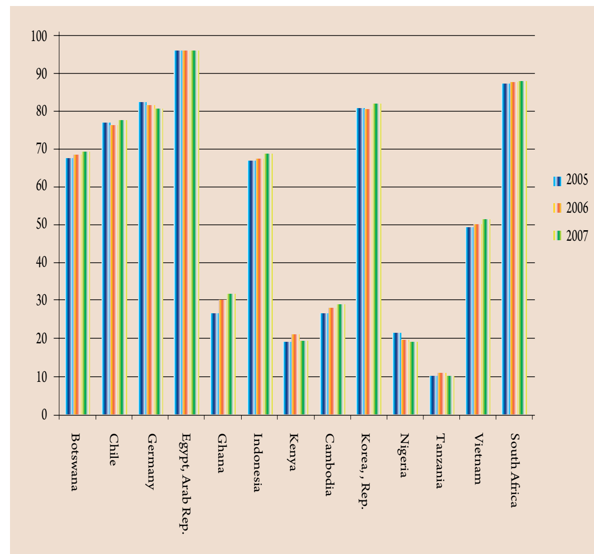
Source: World Bank (2009)

Figure 4.6: Energy use (kg of oil equivalent per capita)



Source: World Bank (2009)

Figure 4.7: Fossil fuel consumption as a percentage of total fuel consumption



Source: World Bank (2009)

Fossil fuel energy consumption (% of total)

Fossil fuel comprises coal, oil, petroleum and natural gas products. According to the World Bank (2009), Egypt (80.8%), South Africa (87.7%), Korea (81.8%) and Indonesia (68.8%) are ranked highly in terms of fossil fuel energy consumption compared to Nigeria, Kenya and Tanzania with 19.3, 19.5 and 10.3 per cent, respectively as shown in Figure 4.7.

Energy sector outstanding challenges and policy issues

The procedures and licensing required to be taken by private investors to invest in alternative energy and cheaper sources such as geothermal, wind, solar and other renewable sources are long and cumbersome. There are issues with lack of connectivity to facilitate trade and commerce and expansion of economic opportunities. There are also issues of limited sources of energy and affordability of power, resulting in inadequate energy to meet the demand arising from expanded production and externalities. There is, therefore, need to expand investments in cheaper and reliable energy sources to ensure affordable power. A critical policy issue is the need to

address the volatility in the cost of energy. Although the Energy Regulation Commission (ERC) has reviewed the current formula for determining electricity tariffs with a view to making movements in the cost of power predictable, this remains a short-term palliative intervention.

4.4 Benchmarked Infrastructure Indicators

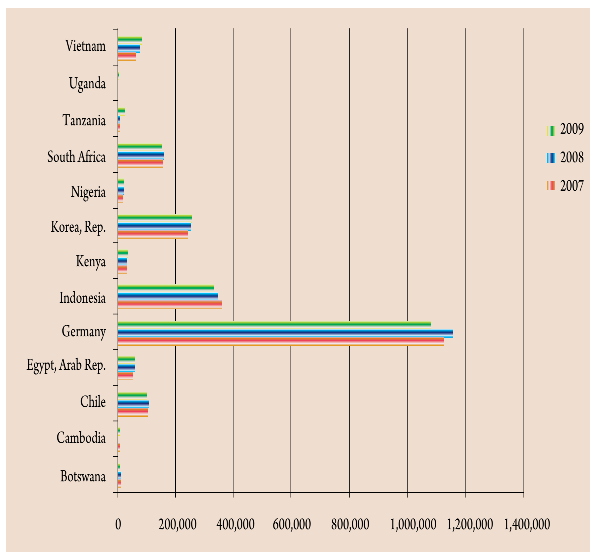
4.4.1 Transport

According to the World Bank (2011), Germany, Indonesia, Korea Republic and South Africa have the highest registered carrier departures worldwide. In 2009, Kenya had 33,593 registered carrier departures worldwide,[1] which was very low compared to Germany with 1,080,993. However, Kenya ranked higher compared to Tanzania, Cambodia and Uganda, which were the least performing as shown in Figure 4.8.

4.4.2 Energy Consumption

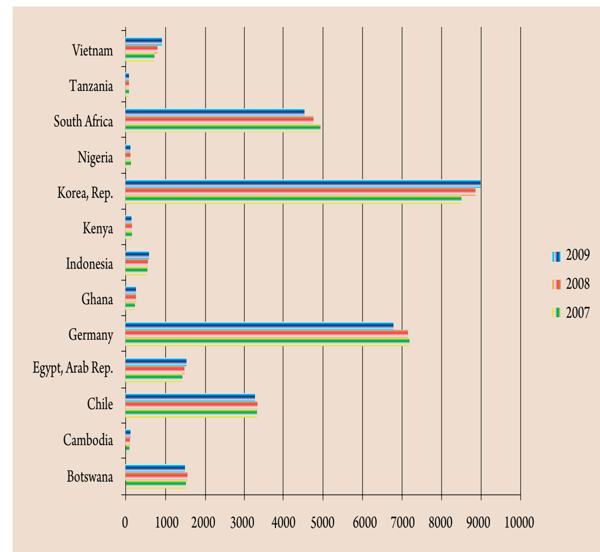
Electric power consumption measures the production of power plants and combined heat and power plants less transmission, distribution and transformation losses and own use by heat and power plants. As shown in Figure 4.9, Korea had the highest electric power consumption in 2009 of 8,980 kWh per capita followed by Germany and South Africa with 6,779 kWh and 4,532 kWh per capita, respectively. In the year 2009, Kenya (with only 147 kWh per capita) together with Nigeria and Tanzania had the lowest electric power consumption (World Bank, 2011).

Figure 4.8: Air transport, registered carrier departures worldwide



Source: World Bank (2011)

Figure 4.9: Electric power consumption (kWh per capita)

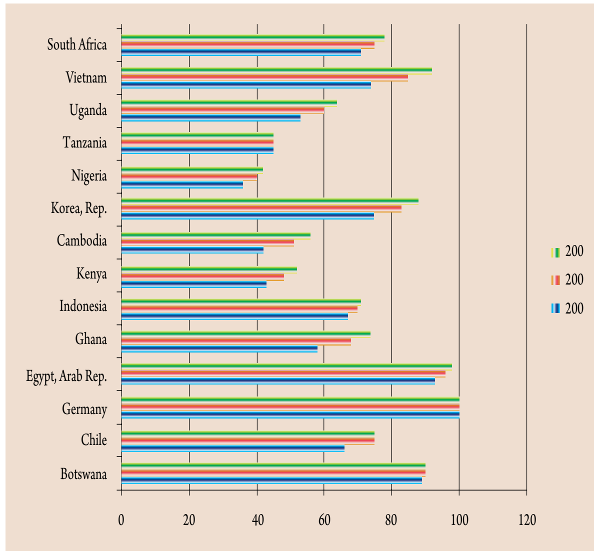


Source: World Bank (2011)

4.4.3 Water and Sanitation

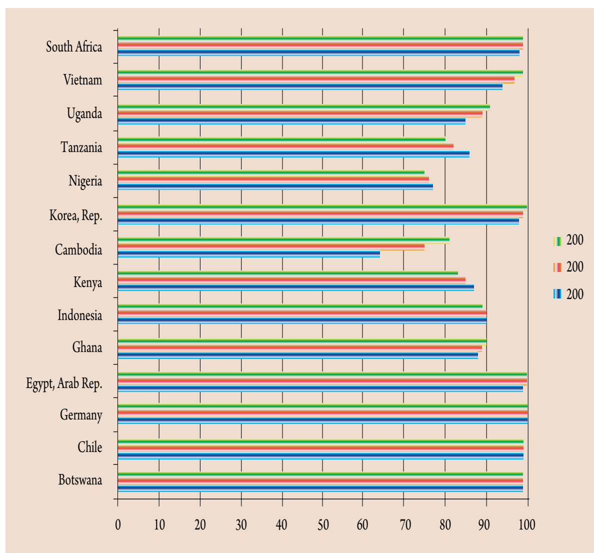
Access to an improved water source refers to the percentage of the population with reasonable access to an adequate amount of water from an improved source, such as a household connection, public standpipe, borehole, protected well or spring and rainwater collection. Unimproved sources include vendors, tanker trucks and unprotected wells and springs. Reasonable access is defined as the availability of at least 20 litres of water per person per day from a source within one kilometre of one's dwelling. World Bank (2008) ranks Germany and Egypt highly in terms of improved water source for rural areas at 100 per cent and 98 per cent, respectively. Uganda had 64 per cent, doing better than Kenya (52%) as shown in Figure 4.10.

Figure 4.10: Improved water source, rural (% of rural population with access)



Source: World Bank (2010)

Figure 4.11: Improved water source, urban (% of urban population with access)



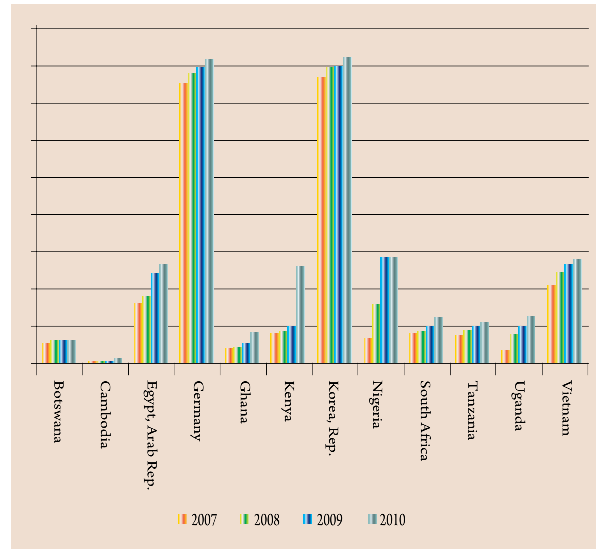
Source: World Bank (2010)

The same report still ranks Germany and Egypt highly in terms of improved water source for urban areas, with Uganda still outperforming Kenya with 91 per cent and 83 per cent, respectively, as indicated in Figure 4.11.

4.4.4 Internet Utilization

Internet users are people with access to the worldwide network. As shown in Figure 4.12, Korea and Germany had the best performance in 2010, with the percentage of internet users standing at 82.5 per cent. In 2010, Kenya had a higher percentage of 25.9 per cent compared to Uganda at 12.5 per cent and Tanzania at 11 percent (World Bank, 2011).

Figure 4.12: Internet users



Source: World Bank (2010)

4.5 Medium Term Prospects for Infrastructure and Economic Services

The infrastructure and economic services sector is a critical pillar for realization of Kenya Vision 2030 as well as the objectives of the Constitution of Kenya 2010. The current challenging economic environment locally as well as globally presents severe challenges to the financing of the sector. It is, therefore, necessary that a major focus for the sector should be to enhance productivity of existing investment levels and leverage linkages with other sectors to enhance development outcomes.

4.6 Conclusions and Emerging Policy Issues

The infrastructure and economic services sector is a key enabler for all the other sectors. Its operation and efficacy are key elements in building an investment

environment that is attractive not only to foreign but also domestic investors. While enormous effort and resources have been applied to enhance the sector, there is still significant scope for improvement. The Ministry of Finance, in its Budget Policy Statement of 2011, notes the following as key objectives for the sector:

- Accelerating ongoing infrastructure development;
- Focusing on quality, aesthetics and functionality of infrastructure services developed;
- Supporting identified flagship projects to ensure contribution to economic growth and social equity goals;
- Improving efficiency and effectiveness of the infrastructure development process at all levels of planning, contracting and construction;
- Protecting the environment as a national asset and conserving it for the benefit of future generations; and
- Providing a utility sector that is modern, customer-oriented and technologically-enabled to provide efficient and cost-effective quality services to all citizens.

These are high-minded and noble goals that, given the current performance of the sector, will need a reset of the institutional framework for the provision of infrastructure and economic services. It is important to observe that implementation of the Constitution of Kenya 2010 will significantly challenge the mechanisms for delivery of infrastructure and the services thereof.

The level of efficiency of resource use by this sector needs to improve. Raising levels of resource-use efficiency given the poor absorption rates and of technological innovation in the sector are key elements to be targeted by institutional transformation in the infrastructure sectors.

Other measures to improve the sector are:

- Streamline institutions to strengthen the role of government regulation, even as private sector participation in the provision of infrastructure and economic services is enhanced. The key issues to note include streamlining of processes and clear identification of obligations for all the players in furtherance of constitutional and other legal provisions.
- Integrate ICT into the infrastructure resource allocation and management framework, as well as provide a mechanism for sharing of and access to information, and improving mechanisms for effective citizen participation.
- Cost-reduction measures to address the huge development budget deficit and unmet demand in the energy and housing infrastructure.
- Provision of cheap renewable energy alternatives that offer decentralized solutions to the local needs of the spatially-spread rural populations without expensive transmission lines (which are also associated with high distribution losses). The Geothermal Development Company only addresses geothermal power, but other suitable renewables such as wind and solar energy also have high upfront costs that should be addressed, including development of solar and wind development institutes to provide technical training for local people in maintenance of the necessary devices.
- Research institutions including university departments dealing with engineering and building sciences should strengthen research capacity and collaborate to deliver effectively on low-cost building materials and technologies.
- Local capacity constraints require that strong institutions should be in place to encourage investor security and market stability for infrastructure services (feed-in tariff policy, FDI

and technology transfer, Design Build Operate and Transfer).

- Securing access to land is a critical element for ensuring that infrastructure plays its rightful role. Fast-tracking of reforms in the land sector are key in this regard. A modern land policy and national spatial plan is critical to infrastructure development.

ENDNOTES

1. Registered carrier departures worldwide are domestic takeoffs and takeoffs abroad of air carriers registered in the country.

Chapter 5

Tourism

5.1 Introduction

Tourism is an important sector of the Kenyan economy and operates within a liberalized economic environment characterized by partnership between the government and the private sector. While the public sector plays an important role in policy implementation and regulation, the private sector is mainly involved in the provision of accommodation, transport and entertainment through ownership and management of hotels, lodges, camp sites and other tourist facilities, tour companies, and travel agents. The sector contributes about 11 per cent of the country's Gross Domestic Product (GDP).

In Kenya's Vision 2030 and its first five-year Medium Term Plan (2008-2012), tourism is one of the six sectors earmarked to accelerate the growth of the Kenyan economy to the average annual rate of 10 per cent between 2012 and 2030. The overall target of the sector between 2008 and 2012 is to treble national tourism earnings from Ksh 52.7 billion (in 2008) to over Ksh 200 billion (in 2012). The other sector goals for the period include raising the number of international visitors from 1.8 million (in 2007) to 3 million; raising the average spending per visitor from Ksh 40,000 to at least Ksh 70,000; increasing hotel beds from 40,000 to about 65,000; and developing niche products as well as business and conference tourism (Government of Kenya, 2010).

Although it has great potential to generate revenue, tourism is highly susceptible to shocks in domestic and international environments. Such shocks include political and macroeconomic uncertainty, and insecurity associated with terrorism risks.

Following the crisis associated with the post-election violence in the country in early 2008 and the global financial crisis the following year, Kenya's tourism sector is returning to commendable levels of growth as a result of policy, institutional and market responses to the crisis. Current demand issues, which can be addressed for increased performance include: ease, frequency and price of transport to Kenya; comparative price or value of tourism offerings in times of financial uncertainty; improving institutional effectiveness; and safety, security, and health considerations as perceived by tourists (World Bank, 2010).

This chapter assesses the performance of the tourism sector to date, and projected performance for the next three years, while identifying institutional bottlenecks that must be addressed in order to improve effectiveness in service delivery and achieve the ambitious targets set in Vision 2030.

5.2 Tourism Sector Performance

5.2.1 Tourism Arrivals and Revenue

International tourist arrivals to Kenya grew by about 8 per cent in 2010 to reach 1,609,100, while revenue

grew by 17.9 per cent to reach Ksh 73.68 billion (Table 5.1). The revenue performance represented a 26.3 per cent shortfall of the Ministry's projection of Ksh 100 billion (Ministry of Tourism, 2010).

Table 5.1: Tourist arrivals and revenue, 2007-2010

Performance Indicator	2007	2008	2009	2010
International arrivals, no. millions	1.82	1.20	1.49	1.61
Growth in arrivals (%)	13.49	-33.79	23.86	7.99
Tourism earnings, Ksh. billions	65.20	52.70	62.50	73.68
Growth in earnings (%)	16.01	-19.17	18.60	17.89

Source: Government of Kenya (Various) Statistical Abstracts; Government of Kenya (2009); Ministry of Tourism (2011)

While the arrivals performance in 2010 was about 11.4 per cent less than the best ever performance achieved in 2007, tourism earnings in 2010 were the best ever for the country.

In terms of market share, the UK and US led Kenya's traditional source markets with 10.82 per cent and 6.70 per cent of arrivals, respectively. Moreover, the share of business travellers increased significantly during the year under review (Ministry of Tourism, 2011a). Beach tourism registered a 16 per cent decline, which was attributed to harassment of tourists by beach boys as well as deterioration of the product quality (Ministry of Tourism, 2011b).

This performance has been achieved following aggressive marketing campaigns by the Kenya Tourist Board (KTB), targeting domestic and international tourists; enhanced partnerships with international travel and leisure organizations, as well as global advertising (on CNN, BBC and Euro news media) and airlines to build a strong image for Kenya as a niche tourist destination. This campaign was a first for Kenya and provided massive visibility of the destination. It was also enhanced by investment on market-specific advertising, market missions, joint marketing with tourism trade partners, public relations activity and participation in travel and tourism exhibitions. In addition, KTB opened representation offices in new and emerging markets such as India, China, United Arab Emirates, Japan, Poland and Turkey (Ministry of Tourism, 2010).

The Ministry/KTB are also venturing into Russia, which is a source market for high-spending tourists, and targets at least 10 per cent of the 1.3 million Russians who visit Egypt annually. Kenya might benefit from the current political turmoil in North Africa if tourists consider the country as an alternative destination to Egypt and Libya.

5.2.2 Visitors to Parks and Museums

Wildlife tourism in Kenya is currently concentrated in only 7 parks, which receive 80 per cent of the total number of visitors (Ministry of Tourism, 2010). Due to improved volume of local and international tourist arrivals, the number of visitors to museums, snake parks and historical sites expanded by 23.67 per cent in 2010, while visitors to game parks and reserves increased by 15.67 per cent (Figure 5.1).

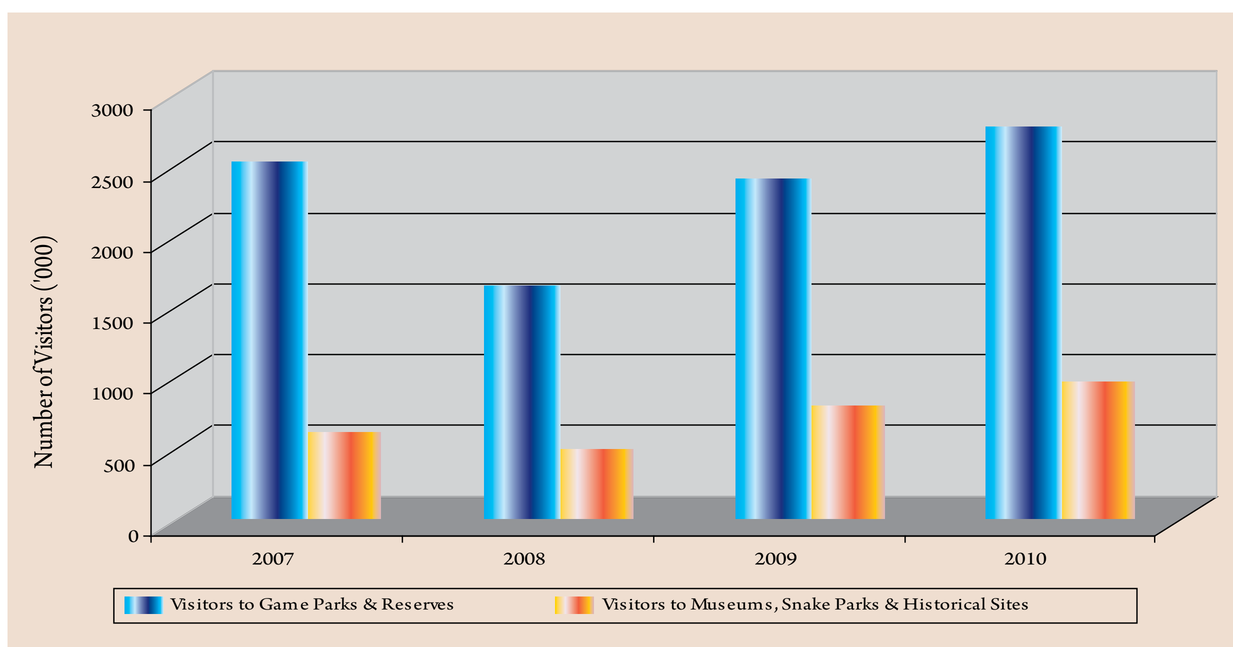
5.2.3 Conferences

In 2010, the number of international conferences and delegates decreased by 25.0 per cent and 24.2 per cent, respectively, while domestic conferences held and delegates attended increased by 30.8 per cent and 84.8 per cent, respectively (Table 5.2). Government ministries conducted the highest number of meetings, 31.2 per cent of the total, while corporates accounted for the largest share (36.8%) of the total number of delegates.

5.2.4 Average Length of Stay

One of the key determinants of per capita spending is the length of stay or number of nights spent in the destination. Over the last decade, the average length of stay has increased from 8.5 days during the first 4 years of the decade (2000-2003) to 11.9 days during the last 4 years (2007-2010) (Figure 5.2), which is a 40 per cent improvement. Moreover, the highest ever length of stay in the country (13.4 days) was achieved in 2010. The strategies employed to achieve this transformation should be sustained and

Figure 5.1: Visitors to game parks and reserves, 2007-2010



Source: Calculations from Government of Kenya (Various) Statistical Abstracts and Government of Kenya (Various) Economic Surveys (2007-2011); National Museums of Kenya (2011)

enhanced for the tourism sector to achieve the high targets set in Vision 2030.

Length of stay varies considerably among source markets, with a tourist from China having spent 28 nights on average in Kenya in 2009, compared to only 4 spent by a tourist from the Middle East. This should be always considered when decisions are being made on the source markets to target with the limited promotion and marketing resources available.

5.2.5 Hotel Bed Nights and Occupancy Rates

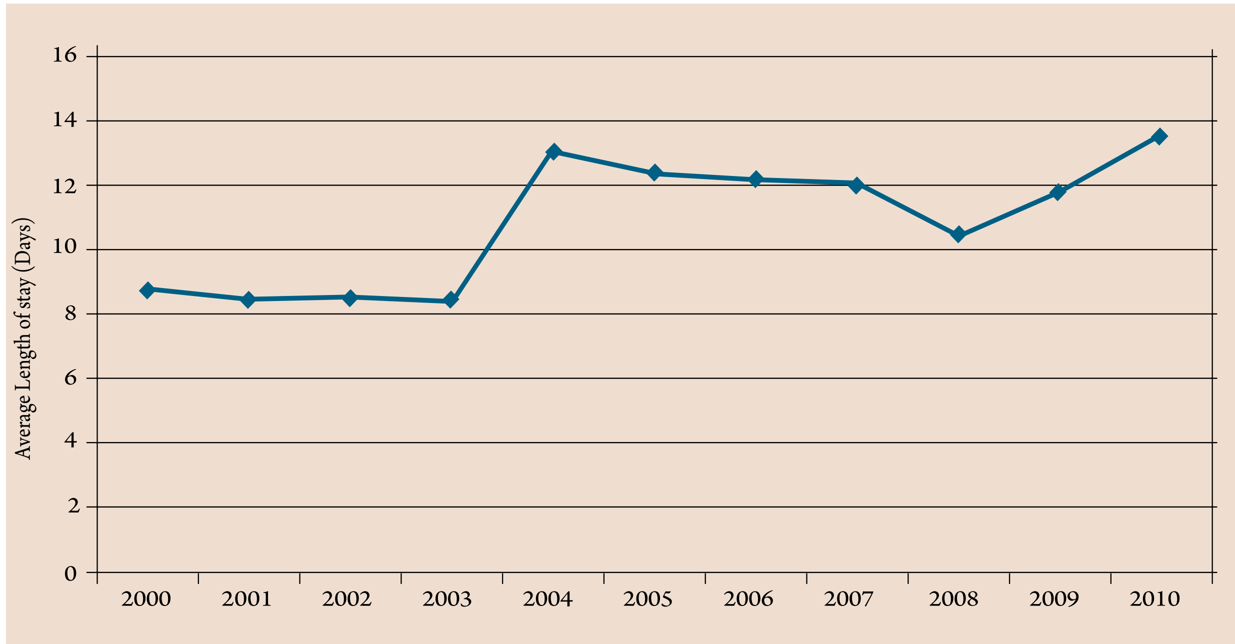
In 2010, bed night occupancy improved to 38.8 per cent from 36.5 per cent the previous year, but failed to return to the pre-crisis level of 47.2 per cent in

Table 5.2: Conference tourism – number of events and delegates, 2007-2010

Type of Meeting / Event	2007		2008		2009		2010	
	Events	Delegates	Events	Delegates	Events	Delegates	Events	Delegates
International conferences	8	10,800	13	10,210	20	19,695	15	14,937
Domestic / National conferences	15	18,000	8	6,650	13	6,250	17	11,550
Trade fairs	9	-	7	275	10	1,670	8	1,442
Exhibitions	13	-	16	2,214	28	4,334	27	1,111
Corporates	84	58,015	164	85,577	74	70,910	69	83,352
NGO & Special	76	47,170	83	20,640	64	15,554	60	21,004
Ministries	170	29,910	344	44,180	178	42,375	149	49,888
Parastatals	62	34,600	76*	18,742	91	18,525	102	22,609
Banquets	22	19,280	35	14,804	34	20,920	30	20,607
Total	459	217,775	746	203,292	512	200,233	477	226,500

Source: 2007-2009 data: Ministry of Tourism (2011); and KICC (2011); " * " implies estimated

Figure 5.2: Trend in average length of stay (days) for international visitors, 2000-2010



Source: Government of Kenya (Various) Statistical Abstracts

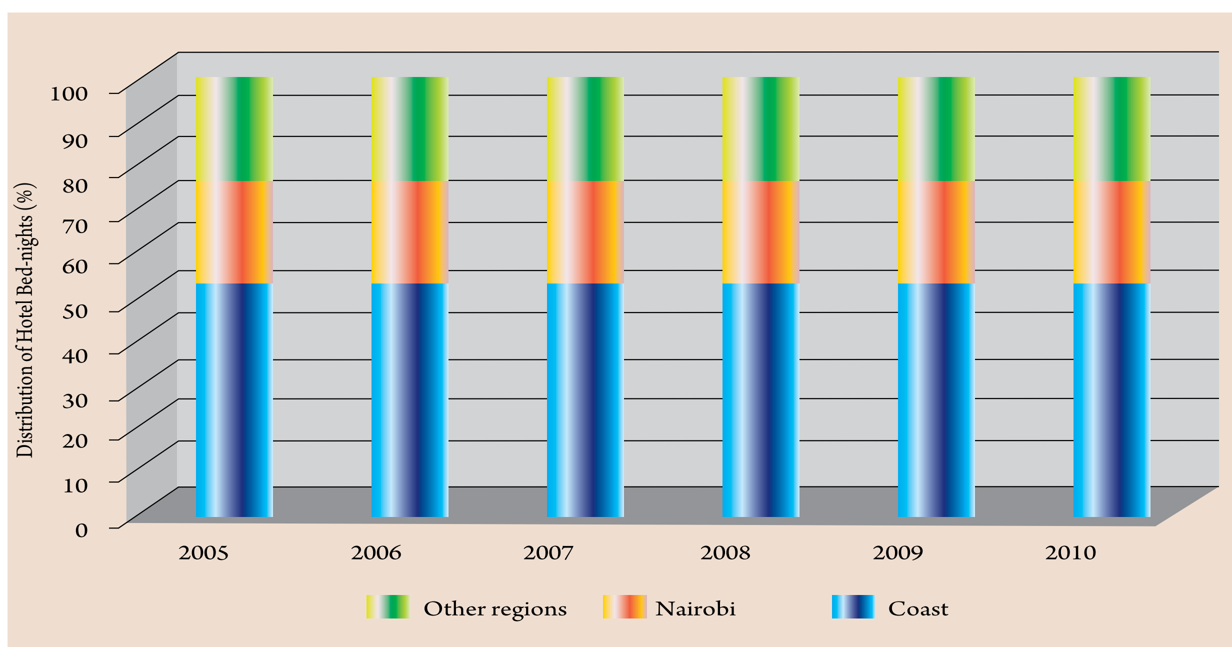
2007 (Government of Kenya, 2011). This was partly due to improved tourist arrivals and average length of stay. The distribution of bed nights is still skewed, being largely concentrated at the Coast. However, the share for the Coast decreased by 2.44 per cent over the previous year (to 52.74%), while that for Nairobi decreased by 13.52 per cent (to 23.03%). In contrast, the share of other regions increased by 25.41 per cent (Figure 5.3). This is a significant improvement in regional dispersion of tourism, and should be enhanced. Vision 2030 proposes the development of 3 resort cities (at Isiolo, Kilifi and Diani) which, upon completion, will expand the accommodation capacity and also spread tourism benefits to less-visited areas (Ministry of Tourism, 2009).

Table 5.3 shows the average hotel occupancy rate for a few selected countries, including Kenya. The greatest reduction in hotel occupancy among the selected countries in 2008 was in Kenya (by 42.9%, followed by China). Although Kenya's occupancy rate improved by 35.7 per cent in 2009 to 36.5 per cent – the highest among the selected countries – this momentum decreased in 2010, achieving a growth of 6.3 per cent over the previous year; and is yet to recover to the 2007 level. China, Singapore and Malaysia were the best performers among the countries in the sample, owing to state-of-the-art developments in their tourism, transport and communications infrastructure (see Box 1 for highlights on Singapore).

Domestic tourists accounted for 35 per cent of all bed nights occupied in the country in 2010, followed by the United Kingdom (15%), Germany (11%) and Italy (7%) (Table 5.4). There is potential for growth in domestic tourism through development of tourism facilities and products that are affordable and attractive to low-medium income Kenyans.

Visitors from the UK, Germany, France, Switzerland, Italy and other European countries generally prefer spending more nights at the Coast (Table 5.4); in contrast, those from USA, Canada, India, Middle East, China and other Asian countries prefer more nights in accommodation facilities at Nairobi, lodges, game reserves and parks. This pattern of choice of accommodation is useful in informing the type of products that should be provided in different parts of the country, in line with expected growth in arrivals from specific source markets.

Figure 5.3: Distribution of hotel bed nights in Kenya by region, 2005–2010, percentage



Source: Computed from Government of Kenya (Various), Statistical Abstract and Government of Kenya (Various), Economic Surveys (2006–2010)

Table 5.3: Hotel occupancy rates for selected countries, 2007–2010

Country	2007 (%)	2008 (%)	2009 (%)	2010 (%)	Mean (2007 – 2010)	% Change (2009 – 2010)
Kenya	47.1	26.0	36.5	38.8	37.1	6.3
South Africa	60.1	59.9	52.5	47.5	55.0	-9.5
China	66.1	56.0	57.4	78.6*	64.5	36.9
Thailand	47.6	44.4	50.0	53.0	48.8	6.0
Singapore	87.0	81.0	75.8	86.0	82.5	13.5
Indonesia	66.9	73.7	62.0	50.3	63.2	-18.9
Malaysia	70.0	66.3	60.7	78.0*	68.8	28.5
India	75.1	73.0	62.0	64.1	68.6	3.4
Mauritius	76.0	68.0	62.5	68.8	68.8	10.1
Egypt	63.0	70.0	80.0	75.0	72.0	-6.3

Source: KNBS and various country websites ; " * " implies estimated

Box 1: Singapore

Singapore has succeeded in promoting its cruise tourism product, with cruise passenger throughput rising steadily at an average annual growth rate of 12% in the last five years. In 2009, the country registered a 20% growth in cruise arrivals, welcoming its one millionth cruise passenger.

Most visibly, one of the most drammatic changes to the tourism landscape is the opening of the two Integrated Resorts that have bolstered Singapore's appeal worldwide as a must-visit destination.

The "YourSingapore" brand represents a bold step in destination marketing and it invites visitors to immerse themselves in the adventure of discovering Singapore and to experience the city their way. Cumulative tourism receipts were estimated at S$12.8 billion (US$ 9.1 billion) in 2009. Visitor arrivals to Singapore reached 9.7 million in 2008.

With regard to hotel infrastructural enhancements, an additional 2,740 rooms in 2009 increased total hotel room inventory to more than 41,000, with 76% occupancy rate. Overall average room rate (ARR) reached S$189 (US$ 135), a decline of 23 per cent. Approximately 29 new hotels with 10,700 rooms are expected to open in Singapore by 2012; and 13 additional hotels with 4,300 rooms by 2015. By 2015, Singapore will have a total of 15.1 million new room-nights, an increase of nearly 50% over the 2009 figures.

Singapore's massive investment in tourism infrastructure in the form of the two Integrated Resorts will help to generate significant additional demand for the expanded hotel room capacity by 2015, along with improved business and consumer taste and preferences. The Singapore Tourism Board has also worked with major international airlines, tours and travel firms to promote discount flights.

Table 5.4: Hotel guest nights by area and country of residence for selected source markets (2009-2010), percentage

	2009				2010			
Country	Nairobi	Coast	Other	Total	Nairobi	Coast	Other	Total
Kenya	33.2	22.6	62.3	34.5	31.6	23.8	63.6	35.3
Uganda	3.8	0.8	1.0	1.6	2.4	0.6	0.5	1.0
Tanzania	2.7	0.6	0.4	1.1	2.5	0.5	0.3	0.9
Other Africa	2.3	0.6	0.5	1.1	2.4	0.6	0.4	1.0
United Kingdom	7.2	21.9	6.8	14.6	7.4	21.4	6.2	14.5
Germany	2.5	18.6	4.0	11.0	2.1	13.9	2.7	8.5
France	2.3	4.4	3.8	3.7	2.3	4.1	2.7	3.3
Switzerland	1.0	3.3	0.5	2.0	0.7	1.8	0.5	1.2
Italy	0.8	10.8	1.9	6.1	0.8	17.9	0.7	9.8
Other Europe	4.1	7.5	4.0	5.8	5.2	6.4	3.6	5.5
US	7.8	1.3	4.4	3.7	8.3	1.1	5.4	3.8
Canada	2.2	0.4	0.7	0.9	2.2	0.3	0.9	0.9
Japan	1.1	0.1	1.1	0.6	1.1	0.1	1.3	0.6
India	2.5	0.9	1.0	1.3	3.0	0.5	1.6	1.4
Middle East	1.6	0.2	0.2	0.6	1.4	0.2	0.5	0.6
China	1.1	0.1	0.7	0.5	1.4	0.1	1.5	0.8
Other Asia	1.5	0.3	0.4	0.7	1.7	0.2	0.7	0.6
Australia & N. Zealand	1.4	0.7	0.7	0.9	1.8	0.5	1.0	0.9

Other innovative products include:

- Food, cultural and arts festival outreach;
- Promotion of prime retail shopping (branding, through tax incentives, encouraging foreign investors to establish internationally-recognized shopping outlets and brands/concepts, entertainment centres, hotel chains, etc);
- Promotion of exchange visits (e.g., for university students and media organizations);
- Promotion of medical tourism (Singapore is reputed as Asia's leading medical hub, having the best healthcare infrastructure in Asia and fourth best in the world. Over 570,000 visitors went to Singapore as medical travellers in 2009, generating S$1.3 billion (or US$ 0.9 billion) in tourism receipts.
- Sports tourism (e.g., Formula 1 Singapore Grand Prix; Volvo ocean race; youth games);
- Promotion of Meetings, Incentives, Conferences and Exhibitions (MICE) tourism, which generates up to 30% of the country's total tourism revenue.

Source: Singapore Tourism Board Annual Report 2009/2010

Development of proposed tourist resort cities will generate significant demand for hotel rooms and related facilities over the next decade (e.g., conference facilities, shopping and entertainment facilities and other value added products such as spa and medical tourism), hence the need to enhance the investment climate in Kenya for development/expansion of tourism infrastructure.

5.2.6 Competitiveness of the Kenya Travel and Tourism Industry

In 2010, Kenya was ranked 11th in Africa and 103rd overall out of 139 countries in the Travel and Tourism Competitiveness Index (TTCI)[1] (Table 5.5). The overall ranking for Kenya has hardly improved since 2008. Moreover, the ranking with respect to two of the three variable categories (regulatory framework, business environment and infrastructure) deteriorated over the period. The deterioration with respect to regulatory framework (from rank 93 to 113 between 2009 and 2010) was particularly large.

Regarding regulatory framework, tourism is a priority sector within the country (with Kenya ranked 18th overall on this pillar), with high government spending on the sector and effective destination marketing campaigns. In addition, there is a strong focus on environmental sustainability in the country (ranked 26th), which is particularly important for Kenya given the sector's dependence on the natural environment.

On the downside, the policy environment has not been sufficiently conducive to the development of the sector (ranked 103rd), with bilateral Air Service Agreements that are not open, insufficiently protected property rights, a lengthy and expensive process of starting a business and policy rules related to visa requirements for visitors. In addition, infrastructure remains underdeveloped and health and hygiene levels require improvement. Key institutions that

Table 5.5: Travel and tourism competitiveness index for selected African countries, 2008 -2010

Country	Overall rank (Africa)			Overall rank (World)			T&T regulatory framework			T&T business environment and infrastructure			T&T human, cultural and natural resources		
	2008	2009	2010	2008	2009	2010	2008	2009	2010	2008	2009	2010	2008	2009	2010
Tunisia	1	2	1	39	44	47	25	31	31	49	49	54	57	56	59
Mauritius	2	1	2	41	40	53	29	24	28	44	44	48	76	69	79
South Africa	3	3	3	60	61	66	70	82	82	51	52	62	52	49	49
Egypt	4	4	4	66	64	75	58	52	70	69	65	74	70	73	71
Morocco	5	5	5	67	75	78	55	64	69	75	78	77	72	83	73
Namibia	9	7	6	93	82	84	92	71	83	74	77	67	113	94	109
Cape Verde	-	-	7	-	-	89	-	-	85	-	-	73	-	-	114
Botswana	7	6	8	87	79	91	82	66	86	76	76	85	103	95	98
Gambia, The	6	8	9	84	87	92	67	65	76	87	90	90	97	98	117
Rwanda	-	-	10	-	-	102	-	-	75	-	-	120	-	-	110
Kenya	10	9	11	101	97	103	100	93	113	102	100	106	77	72	72
Senegal	14	12	12	108	101	104	94	101	111	104	108	108	108	82	82
Ghana	-	13	13	-	110	108	-	105	115	-	102	105	-	104	104
Tanzania	8	10	14	88	98	110	89	102	121	117	118	127	48	50	56
Zambia	13	11	15	107	100	111	91	87	104	118	115	131	90	85	95

Note: Ranking for 2007–2009 is out of 133 countries, while for 2010 is out of 139 countries

Source: World Economic Forum (2007, 2008, 2009, 2011)

require strengthening include the Tourism Police Unit, health sector institutions, immigration and air transport regulatory institutions.

With Kenya's porous borders and constant threat from terrorism, the security situation in the country remains the most significant hindrance to further development of tourism. The country was ranked last among all 139 countries on this indicator. The recent threats of terrorist attacks by the *Al-Shabaab*[2] rebel group from Somalia have contributed to this dismal position. The low ranking on safety and security is attributable to high business costs of terrorism, high business costs of crime and violence, and low reliability of police services. The government has stepped up internal security operations against the terrorist groups along the border with Somalia, in order to reassure inbound tourists that the country is still a safe haven to visit.

As part of measures to remedy this state of affairs, the government enacted the Tourism Act 2011, which paved way for formation of key tourism-sector institutions responsible for regulation; development and marketing; tourist protection services; research; financing of tourism infrastructural development; and dispute resolution amongst stakeholders in the tourism sector.

According to the World Bank (2010), current demand issues that can be addressed for increased performance include: ease, frequency and price of transport to Kenya; comparative price or value of tourism offerings in times of financial uncertainty; improving institutional effectiveness; and safety, security and health considerations as perceived by tourists.

5.2.7 Government Expenditure in the Tourism Sector

Through its constituent institutions,[3] the Ministry of Tourism runs six sub-programmes, namely: International Tourism Promotion and Marketing; Domestic Tourism Promotion and Marketing; Conference Tourism Development; Cultural

Tourism Development; Product Standardization and Classification; and Tourism Infrastructure Development.

In order to implement various strategies and projects outlined in the Ministry's Strategic Plan for fiscal years 2008/09–2012/13, the Ministry estimated that Ksh 115 billion would be required over the plan period (Table 5.6). The largest share of the total estimated budget (53.2%) goes to developing new products and diversification of source markets as follows: developing 3 resort cities (90.61%), establishing and licensing high quality home stays (6.53%), enhancing tourism products (2.45%), venturing into viable emerging markets (0.24%), and carrying out a market study on emerging markets (0.17%). The second highest share of the estimated total budget (32.6%) has been planned for increasing tourism revenue from Ksh 65 billion (in 2007) to Ksh 200 billion (in 2012) as follows: increasing the number of quality tourist facilities (0.03%); increasing MICE (Meetings, Incentives, Conferences and Exhibitions) facilities and KICC upgrade (45.13%), increasing accessibility to Kenya and source markets by air and sea transport (0.04%), increasing promotional campaigns in traditional and emerging markets (45.08%), and intensifying domestic tourism promotion campaigns (9.72%).

Despite the importance of the tourism sector in foreign exchange generation, funding levels have remained very low over the last 3 years, hampering effective implementation of some of the crucial programmes and flagship projects envisaged in the current Medium Term Expenditure Plan (MTEP). In 2008/09 and 2009/10 financial years, the ministry received Ksh 1.9 billion and Ksh 2.3 billion, respectively (Table 5.7), against its requirements of Ksh 19.5 billion and Ksh 18.6 billion, respectively, as indicated in the current Strategic Plan (Table 5.6) (Ministry of Tourism, 2008/09). In 2009/10, the Ministry allocated more resources to development expenditure and as a result the development index improved from 11.3 per cent in 2007/08 to 22.3 per cent in 2008/09 and 34 per cent in 2009/10. However, the target of 50 per cent was not realized and the ministry needs to focus on achieving this (Table 5.7).

Disaggregated total expenditure by the programme (Table 5.8) shows that although actual expenditure in tourism promotion and marketing has increased by 35.3 per cent from Ksh 829 million in 2007/08 to Ksh 1,121.58 million in 2009/10, this allocation as a ratio of the total budget of the Ministry of Tourism has declined by 27.3 per cent from 74.7 per cent to 48.1 per cent. This is partly attributed to increased allocation to the tourism infrastructural development budget (Ministry of Tourism, Strategic Plan 2008-2012).

Looking at projected funds for 2010/11–2013/14 (Table 5.9), it is evident that the funding status is still way below the anticipated resource requirement. Thus, given the enormous transformation required in the sector, there is need to establish a sustainable funding mechanism for tourism to support product development and facilities.

Since allocation of more funding to tourism public sector institutions may not be feasible in the short-to-medium term, considering lessons from France, Singapore and Malaysia among other successful tourist destinations, Kenya should initiate active partnership with the private sector (through public-private-partnerships) and provide investment incentives (e.g. tax relief/holiday) to investors in the tourism sector. France, for instance, has succeeded in coming up with innovative fundraising initiatives to encourage investors to operate tourism enterprises in the rural areas, and has put in place institutions that finance investors in the tourism industry.

5.3 Medium Term Prospects for the Tourism Sector

In assessing the medium term prospects for the tourism sector, we assume that the macroeconomic environment will remain stable during the period and that, although Kenya will participate in a general election in 2012/13, this will not affect

Table 5.6: Budgetary requirements for each objective, 2008/09–2012/13 (Ksh millions)

Broad Objectives / Planned Activities	2008/09	2009/10	2010/11	2011/12	2012/13	Total
Develop new products and diversify source markets	13,164.0	11,500.0	11,620.0	11,780.0	13,140.0	61,254.0
Increase tourism revenue from Ksh 65 billion (in 2007) to Ksh 200 billion (in 2012)	4,124.8	4,603.5	9,231.3	9,483.0	10,050.8	37,493.3
Reduce tourism resource conflicts	1,105.0	1,105.0	1,105.0	1,105.0	1,105.0	5,525.0
Formulate and implement an appropriate policy and legal framework for the development of the tourism sector	855.0	868.0	1,300.0	1,150.0	1,100.0	5,273.0
Enhance and sustain the financial resources for the tourism sector	3.9	13.8	2,013.5	3.9	4.2	2,039.4
Enhance safety and security of tourists	114.0	412.0	507.0	502.0	502.0	2,037.0
Offer and maintain internationally-accepted standards of tourist service	90.0	95.0	100.0	105.0	110.0	500.0
Enhance tourism information management and research capacity	63.0	229.0	230.0	182.0	194.0	898.0
Attract, develop and retain competent and motivated ministry staff	28.8	32.8	34.8	32.8	32.8	162.0
Estimated Total Cost of Planned Activities	19,548.5	18,859.1	26,141.6	24,343.7	26,238.8	115,131.7

Source: Ministry of Tourism (2009; 2010)

performance in the tourism sector negatively due to the institutional and legislative reforms that have been made in the Judiciary, police and political parties, among others.

Tourist Arrivals: In the baseline scenario, we envisage that in 2011, the country will achieve the average growth rate in arrivals of 11 per cent experienced during the pre-crisis period 2005-2007,

Table 5.7: Analysis of total expenditure by economic classification, 2007/08–2009/10

Development and Recurrent Budget Items		Approved Estimates (Ksh M)			Actual Expenditure (Ksh M)		
		2007/08	2008/09	2009/10	2007/08	2008/09	2009/10
Recurrent budget	Compensation to employees	110.3	116.5	124	108.4	109.4	124
	Use of goods and services	275.5	359.2	453	273.5	339.7	414
	Grants, transfers and subsidies	588.9	1,000.5	1,002	588.5	999.95	992
	Acquisition of non-financial assets	16.96	30.7	17.8	15.1	25.2	10
	Sub-Total	991.7	1,506.9	1,596.8	984.5	1,474.3	1,540
Development budget	Compensation to employees	-	-	-	-	-	-
	Use of goods and services	-	10	-	-	9.9	-
	Grants, transfers and subsidies	40	388	712	40	388	712
	Acquisition of non-financial assets	80	40.5	92	85.8	24.5	78
	Sub-Total	120	438.5	804	125.8	422.5	790
Total Expenditure		1,111.7	1,945.4	2,400.8	1,110.4	1,896.8	2,330.0
Recurrent as % of Total		89.2	77.5	66.3	88.7	77.7	66.1
Development as % of Total		10.8	22.5	33.4	11.3	22.3	33.9

Source: Ministry of Tourism (2009; 2010)

Table 5.8: Analysis of total expenditure by programmes, 2007/08–2009/10

Budget		Approved Estimates (Ksh M)			Actual Expenditure (Ksh M)		
		2007/08	2008/09	2009/10	2007/08	2008/09	2009/10
Tourism promotion and marketing	International	732.7	1,074.5	940.5	725.0	1,069.1	977.3
	Domestic	95.3	166.7	42.8	104.0	146.5	144.3
Conference tourism development		-	287.1	-	-	286.9	-
Cultural tourism development		183.9	255.1	279	188.0	254.6	286.5
Product standardization and classification		74.2	102.0	235	69.4	92.0	261
Tourism infrastructure development		25.6	60.0	903.5*	25.0	47.7	660.9*
Total budget		1,111.7	1,945.4	2,400.8	1,110.4	1,896.8	2,330.0
Promotion and marketing as a % of total		74.5	63.8	41.0	74.7	64.1	48.1

Source: Ministry of Tourism (2011); * Implies provisional data

and maintain it through 2012-2014 (Table 5.10). If the exchange rate remains stable and close to the current levels, this might also accelerate earnings in the forecast period. Given the recent unrest in Egypt and Libya, the North African states may take the next two to three years to stabilize and this may boost arrivals in Kenya in the optimistic scenario. Under this scenario, all factors remaining the same, tourism arrivals are predicted to reach the 2 million mark in 2012/2013.

Tourism Earnings: Throughout the pre-crisis period of 2005–2007, tourism earnings grew at about 18.7 per cent on average per year. In 2010, the tourism sector earnings exceeded the record set in 2007 by 12.7 per cent. We use the pre-crisis average growth rate to forecast the earnings for the medium term.

Value Added in Hotels and Restaurants: Using year 2001 constant prices, in the baseline scenario, the value added for hotels and restaurants for the period 2011 to 2014 is projected using the average annual growth rate in value added for the period 2005 to 2007 of 14.8 per cent.

Major Source Markets: The above forecasted arrivals and earnings for year 2012 are much lower than the Ministry of Tourism's target of 3 million arrivals and Ksh 200 billion in revenue (Ministry of Tourism, 2009). We envisage this may be achieved after 2014, and will depend on availability of more funding to the sector, implementation of flagship projects, improvement of the quality of tourism facilities, tourism promotion and marketing in key source markets, transformation of various institutions in the sector, peaceful elections in 2013

Table 5.9: Projected resource requirements by sub-programmes, 2010/11–2013/14 (Ksh millions)

Budget Items		2010/11	2011/12	2012/13	2013/14
Tourism promotion and marketing	International	721	1,970	2,575	3,762
	Domestic	71	161	171	203
Conference tourism development		0	630	426.2	63
Cultural tourism development		326	406	358	410
Product standardization and classification		505	899	1,029	787
Tourism infrastructure development		67	747	180	206
Wildlife conservation and management		408	2,518	1,535	1,565.5
General planning and administration		281	502	546.6	599
Total Budget		**2,379**	**7,833**	**6,818**	**7,596**
Promotion and marketing as a % of total		33.3	27.2	40.3	52.2

Source: Government of Kenya (2011)

and reduced risk of terrorist attacks. Stability of the exchange rate is also likely to have a significant impact on the tourism sector.

Due to the global financial crisis of 2008/09 and the recent Euro-zone debt crisis, some of Kenya's traditional markets will register decline in real GDP growth over the period 2009-2016 (Table 5.11) but will rebound by 2016. However, figures for arrivals and earnings in 2009 and 2010 (Table 5.10) show that the crisis has not significantly reduced incentive by tourists from source markets to travel to Kenya. This explains our optimistic forecasts for 2011.

The prospects for inbound tourists are derived using departures by country of residence. In the baseline scenario, it is assumed that the pre-2008 departure levels are reached in 2010, and thereafter grow at the average growth rates experienced over the period 2005-2007, which are used to forecast for the 2011-2014 period (Table 5.12). All factors held constant, the highest growth rates in arrivals over the forecast period are expected from Canada, Tanzania, Australia and New Zealand (Oceania), USA and India.

5.4 Conclusion and Policy Implications

Following a period of decline in activity, Kenya's tourism sector is returning to commendable levels of growth. In 2010, the tourism sector achieved the highest receipts ever in the history of the sector, following aggressive marketing campaigns by the Kenya Tourist Board (KTB), targeting domestic and international tourists, venturing into new/emerging markets, enhanced partnerships with international travel and leisure organizations as well as global advertising (on CNN, BBC and Euro news media) and airlines to build a strong image for Kenya as a niche tourist destination.

Tourism is a recognized priority within the country, with effective destination marketing campaigns and a strong focus on environmental sustainability. However, infrastructure remains underdeveloped and health and hygiene levels require improvement. With Kenya's porous borders and constant threat from terrorism, the security situation in the country remains a significant hindrance to further development of the sector.

Despite the importance of the tourism sector in foreign exchange generation and the relative high

Table 5.10: Projected tourist arrivals, earnings and value added in hotel and restaurants

	Pre-crisis Period				Post-crisis Period					
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Arrivals										
Number	1,479,000	1,600,541	1,816,957	1,203,200	1,490,000	1,609,100	1,786,101	1,982,572	2,200,655	2,442,727
Growth (%)	8.7	8.2	13.5	- 33.8	23.8	8.0	11.0	11.0	11.0	11.0
Earnings										
Ksh billions	48.90	56.20	65.40	52.71	62.50	73.68	87.46	103.81	123.23	146.27
Growth (%)	24.7	14.9	16.4	- 19.4	18.6	17.9	18.7	18.7	18.7	18.7
Value Added in Hotels and Restaurants										
2001 Constant prices (Ksh million)	15,572.0	17,894.0	20,814.0	13,298.0	18,993.0	19,796.0	22,725.8	26,089.2	29,950.4	34,383.1
Growth (%)	13.3	14.9	16.3	-36.1	42.8	4.2	14.8	14.8	14.8	14.8

Source: Calculated from Government of Kenya (Various), Economic Surveys (2007–2011)

government spending, funding to the sector is very low relative to the resources required for effective implementation of some of the crucial programmes and flagship projects envisaged in the current Medium Term Expenditure Plan (MTEP). To implement various objectives and activities outlined in the Ministry's Strategic Plan for fiscal years 2008/09–2012/13, an estimated Ksh 115 billion in financial resources is required. Innovative financing through public-private partnerships and incentives to private investors in the sector is required.

Regarding the business environment, there is need to urgently implement the Tourism Act 2011 and the tourism policy. Continued implementation of the Constitution of Kenya 2010 and Vision 2030 will have a big positive impact on the business environment for tourism. There is need to review the regulatory framework, and to repeal numerous permits and licences that have made doing business cumbersome and costly. There is also need for legislation that will take into account the potential in the informal tourism sector, where majority of the poor earn their living.

Table 5.11: Real GDP growth for selected tourism source countries, 2007-2016

	Actual (%)				Projections (%)			Direction of growth (2010 – 2012)
	2007	2008	2009	2010	2011	2012	2016	
USA	1.9	-0.3	-3.5	3.0	1.5	1.8	3.4	Negative
Canada	2.2	0.7	-2.8	3.2	2.1	1.9	2.2	Negative
UK	2.7	-0.1	-4.9	1.4	1.1	1.6	2.7	Positive
Germany	3.4	0.8	-5.1	3.6	2.7	1.3	1.3	Negative
France	2.2	-0.2	-2.6	1.4	1.7	1.4	2.1	Positive
Italy	1.5	-1.3	-5.2	1.3	0.6	0.3	1.2	Negative
Spain	3.6	0.9	-3.7	-0.1	0.8	1.1	1.8	Positive
Portugal	2.4	0.0	-2.5	1.3	-2.2	-1.8	2.0	Negative
Greece	4.3	1.0	-2.3	-4.4	-5.0	-2.0	3.3	Negative
Netherlands	3.9	1.8	-3.5	1.6	1.6	1.3	1.8	Negative
Belgium	2.8	0.8	-2.7	2.1	2.4	1.5	1.8	Positive
Austria	3.7	2.2	-3.9	2.1	3.3	1.6	1.8	Positive
Finland	5.3	1.0	-8.2	3.6	3.5	2.2	2.0	Negative
Ireland	5.2	-3.0	-7.0	-0.4	0.4	1.5	3.3	Positive
Luxembourg	6.6	1.4	-3.6	3.5	3.6	2.7	3.1	Positive
Sweden	3.3	-0.6	-5.3	5.7	4.4	3.8	2.5	Negative
Switzerland	3.6	2.1	-1.9	2.7	2.1	1.4	1.8	Negative
Denmark	1.6	-1.1	-5.2	1.7	1.5	1.5	1.9	Negative
Singapore	8.8	1.5	-0.8	14.5	5.3	4.3	4.0	Negative
Japan	2.4	-1.2	-6.3	4.0	-0.5	2.3	1.3	Negative
Australia	4.6	2.6	1.4	2.7	1.8	3.3	3.3	Positive
New Zealand	2.8	-0.1	-2.0	1.7	2.0	3.8	2.3	Positive
Russia	8.5	5.2	-7.8	4.0	4.3	4.1	3.8	Positive
China	14.2	9.6	9.2	10.3	9.5	9.0	9.5	Positive

Source: IMF (2011) World Economic Outlook – Slowing Growth and Rising Risks

Table 5.12: Projected departures by country of residence (baseline status), '000

	Pre-crisis Period			2005 – 2007 mean growth rate (%)		Post-Crisis Period					
	2005	2006	2007		2008	2009	2010	2011	2012	2013	2014
UK	248.20	272.00	313.60	12.44	216.70	245.90	247.10	277.84	312.40	351.27	394.96
Germany	237.60	248.90	263.20	5.26	137.30	149.70	154.80	162.94	171.51	180.53	190.03
Italy	123.10	129.90	146.60	9.19	80.20	112.10	112.60	122.95	134.25	146.58	160.06
France	71.30	76.20	84.70	9.01	43.10	51.30	52.00	56.69	61.79	67.36	73.43
Switzerland	58.00	60.30	60.50	2.15	37.70	43.10	44.10	45.05	46.02	47.01	48.02
USA	78.70	91.90	116.80	21.93	89.40	127.20	131.50	160.34	195.50	238.37	290.65
Canada	15.30	22.10	27.40	34.21	18.90	28.10	28.90	38.79	52.06	69.86	93.76
India	26.20	35.70	37.10	20.09	35.30	38.20	41.20	49.48	59.42	71.35	85.69
Japan	22.20	21.50	22.00	2.74	14.20	18.80	20.10	20.65	21.22	21.80	22.40
Tanzania	16.80	25.80	27.60	30.28	23.20	46.10	46.60	60.71	79.09	103.04	134.24
Uganda	15.30	19.80	20.90	17.49	22.80	42.70	43.40	50.99	59.91	70.39	82.70
Oceania**	18.70	24.00	28.70	23.96	19.20	22.80	24.00	29.75	36.88	45.71	56.67

Source: Government of Kenya (Various) Economic Surveys (2007-2011); and authors' calculations; Oceania** = Australia and New Zealand

ENDNOTES

1. TTCI is published by the World Economic Forum (WEF) in collaboration with International Air Transport Association (IATA), the United Nations World Tourism Organization (UNWTO) and the WTTC among other tourism-related bodies. It measures how different countries compare in terms of the attractiveness of factors and policies that are important for development of the travel and tourism (T&T) sector. It is based on three broad categories of variables:

   Travel and Tourism Regulatory Framework – Policy rules and regulations, environmental sustainability, safety and security, health and hygiene and prioritization of travel and tourism;

   Travel and Tourism Business Environment and Infrastructure – Air and ground transport infrastructure, tourism infrastructure, ICT infrastructure and price competitiveness;

   Travel and Tourism Human, Natural and Cultural Elements – Human resource, education and training, availability of qualified labour, affinity for travel and tourism, natural and cultural resources.

   These variables are important indicators of institutional effectiveness of Kenya's tourism sector, especially those engaged in policy design/implementation, training, security, hygiene/sanitation, tourism pricing and overall tourism sector infrastructure.

2. Al Shabaab, which means "the youth" in Arabic, is an organized, but shifting, Islamist group in Somalia. It is frequently referred to as a terrorist group in the media. However, it may also be understood as a political party, a militia and a movement. Al Shabab controls much of southern Somalia and has been fighting interim government forces and the 8,000 African Union troops for control of Mogadishu in recent months.

   Source: http://terrorism.about.com/od/groupsleader1/p/Al-Shabab.htm ; http://hornofafrica-abdikarim.blogspot.com/2011/03/somalia-government-captures-al-shabab.html ; http://www.markacadeey.com/march2011/20110329_3e.htm

3. Kenya Tourist Development Corporation; Kenya Tourist Board; Catering and Tourism Development Levy Trustees; Kenya Utalii College; Kenyatta International Conference Centre; Bomas of Kenya; Hotel and Restaurants Authority; and Tourism Trust Fund.

Chapter 6

Agriculture

6.1 Overview of Agriculture and Rural Development

The agriculture sector has recorded positive growth since 2009 compared to previous years. In 2010, agriculture grew by 6.3 per cent. Due to heavy reliance on rainfall, the agriculture sector is considerably vulnerable to weather-related shocks (e.g. drought and floods). These shocks have a multiplier effect on other sectors of the economy (such as agro-processing, exports and food prices) that rely on the agriculture sector. As a result, there needs to be a paradigm shift in the strategies that are employed in addressing agricultural development of the country.

A large segment of the population continues to predictably suffer from chronic food shortages; it is estimated that 39.9 per cent of the population lives on less than US$ 2 a day. Depending on the weather, transitory demand for food continues to increase with the increasing population growth. Generally, close to 50 per cent of rural and urban poor households are net buyers of food; they spend between 50-70 per cent of their budget on food (FAO, 2011). Interventions should include increased access to food, and development/strengthening of social protection programmes.

Diets in many developing countries are changing as per capita disposable incomes rise especially in urban areas. The share of staples such as cereals, roots and tubers, is declining, while that of meat, dairy products and oil crops is rising. In the last 40 years, per capita meat consumption in developing countries rose by 150 per cent and that of milk and dairy products by 60 per cent. By 2030, per capita consumption of livestock products could rise by a further 44 per cent, the so called livestock revolution (World Bank, 2007). For Kenya, there is potential for livestock trade within the region and beyond, and this would improve household income and thus access to food.

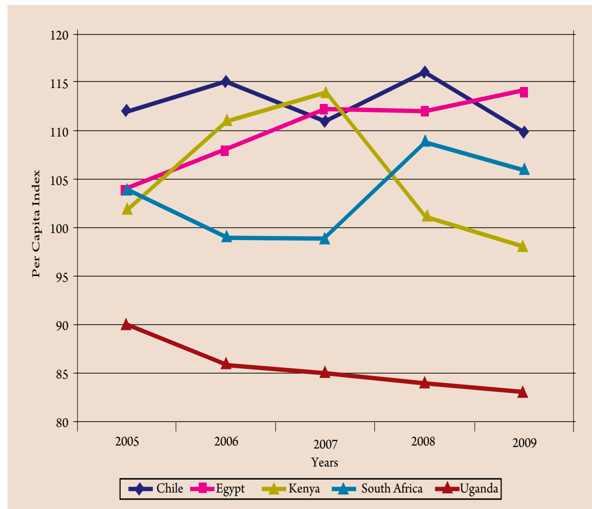
Broadly, supply-driven growth will be as a result of programmes that increase cropping frequency and higher yields as a result of irrigation and increased cultivated land. Due to high population pressure in the highlands, investments in irrigation will bring some land in semi-arid areas into cultivation. In livestock production, increased supply will be as a result of breeding and improved/fortified feed lots, while in fisheries, aquaculture will be central to increased production. There is evidence under the Economic Stimulus Programme that two cropping seasons can be achieved in irrigation schemes.

6.2 Overall Performance of the Sector

6.2.1 Agricultural Production

One of the central objectives of agricultural production is to produce enough food to feed the population. Kenya's per capita agricultural production has been on the decline since 2007 (Figure 6.1). This can be attributed in part to drought and the post-election violence. Worldwide, the same period (2007-2008) saw the increase in world food prices, leading to political and social unrest. Some of the reasons attributed to the increased food prices include: falling world food stock, drought, rising oil prices and increasing demand for a more varied diet especially from the transitional economies (IFPRI, 2011). The agricultural growth trends in per capita for some comparator countries (Figure 6.1) show that in 2009, Chile, South Africa and Uganda also recorded declined growth; on the other hand, Egypt has maintained increased growth.

Figure 6.1: Growth trends in per capita agricultural production index, base year 1999-2001

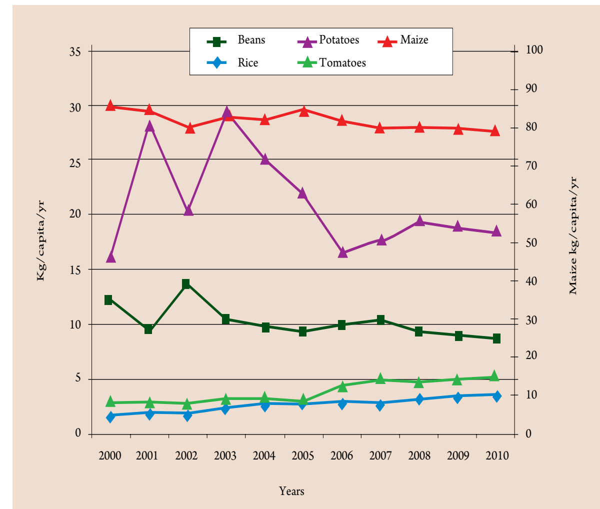


Source: FAO (2011)

6.2.2 Food Production

Maize accounted for 27.142 million bags; this was attributed to the increased access to subsidized fertilizers and utilization of certified seed. Indigenous crops are contributing a significant portion of the total crop produced annually. For instance, in 2009, cassava production was at 0.9 million tonnes and sweet potatoes at 1.03 million tonnes. Figure 6.2 shows that the trends in food supply since the year 2000 have been declining with the exception of rice and tomatoes, which are usually grown under irrigation. On average, annually, the maize available from production is about 81kg per capita, while rice is about 7kg and potatoes about 21kg per capita. Cassava is about 13kg and sweet potatoes at 15kgs; these root tubers can be used to complement maize supply. Pulses supply annually is at 5kg per capita and sorghum is at 2kg. This shows that there needs to be continued concerted efforts to increase crop yields and acreage so as to increase food supply.

Figure 6.2: Food supply kg/per capita/yr 2000-2010[1]



Source: FAO (2011)

The need to increase the food available for consumption is emphasized further when the level of hunger is taken into account as measured by the Global Hunger Index. In 2010, Kenya recorded a rating of 19.8, an improvement from the 2009 rating of 20.3 (IFPRI, 2011). Despite this marginal improvement, indications are that about 20 per cent of the population does not attain the minimum dietary requirements to sustain a healthy and productive life. This means that more energy is spent on activities that focus around meeting

immediate food requirements, instead of the long-term initiatives that are sustainable.

Figure 6.3 shows that there has been positive growth in population and food consumption from 1990. However, the change in growth has not been as high as was in the 1990s. The last decade has experienced lower rate of growth. Food availability per person has been steadily declining, implying that supply does not match population growth.

Figure 6.3: Percentage change in food consumption and population growth

Source: FAO (2011)

6.2.3 Industrial and Horticultural Crop Production

Under industrial crops, tea and coffee are highlighted. They are the country's leading agricultural export earners. In 2009, tea, horticulture, coffee and articles of apparels and clothing accessories accounted for 50.5 per cent of total domestic exports. Tea was the leading foreign exchange earner, recording increased prices per kilo to Ksh 212 and resulting in improved export earnings by 11 per cent from Ksh 62 billion in 2008 to Ksh 69 billion. Coffee production increased from 43,462MT in 2008 to 54,020MT in 2009, while its price per kilo rose from Ksh 177.2 to Ksh 195.75 (Government of Kenya, 2010).

Horticulture was the second leading foreign exchange earner. Table 6.1 shows the contribution of the different sub-sectors in horticulture in terms of volume and value. Only 4 per cent of horticultural produce is exported with the other 96 per cent consumed locally (Ministry of Agriculture, 2011).

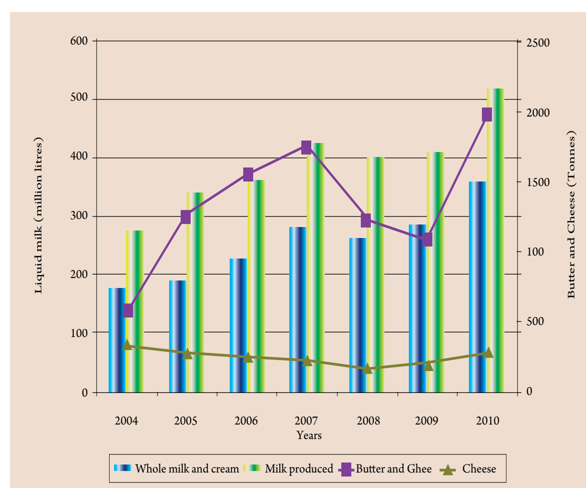
Table 6.1: Volume and value of horticultural exports, 2008-2010

Year	Volume (MT)			Value (billions)		
	2008	2009	2010	2008	2009	2010
Flowers	124.91	87.0	51.03	39.91	30.81	17.53
Vegetables	123.48	21.22	16.52	23.97	2.28	1.61
Fruits	145.26	72.49	44.19	8.67	16.25	10.95

Source: Horticultural Crops Development (2011)

There is a sharp contrast between the institutions that have propelled growth in these sub-sectors. The tea and coffee sub-sectors in the formative years have benefitted greatly from government interventions (e.g. research, extension services, and quasi-public organizations in procurement of inputs, seeds and fertilizer). The tea sub-sector continues to benefit from this background, while the coffee sub-sector is currently undergoing reform and is partially incorporating private actors into the marketing chain. On the other hand, the horticulture sub-sector is largely privately-driven, with the government basically playing a peripheral regulatory role.

Figure 6.4: Milk production and milk products in Kenya, 2007-2010



Source: Government of Kenya (2011) Economic Survey

6.2.4 Livestock Production

In 2000, the annual per capita milk consumption was 78 litres and production was 70 litres. The latest statistics available (2007) show that there has been an increase in production, and the average annual per capita consumption of milk is 87 litres, while per capita production is at 92 litres (Government of Kenya, 2011). Over time, milk production has substantially increased. In 2009/10 (Figure 6.4), there were substantial surpluses, causing farmer distress due to the limited avenues for disposal even after the milk industry was liberalized.

Kenya could borrow a leaf from New Zealand, where the dairy industry is a vertically integrated coordinated global supplier industry. The dairy farms are strongly tied to their respective food marketing and processing chains. This industry is the country's biggest export earner with annual exports estimated at US$ 11 billion. Although the country accounts for less than 2 per cent of the global milk supply, its dairy products account for one-third of the international dairy trade. Livestock farming in New Zealand is a low-input, low-cost model of production, which relies on year-round grazing of animals in open pasture, using clover as the primary nitrogen source. However, the prospects of prolonged drought in Kenya may negate any past gains within the sub-sector.

Table 6.2:Livestock census of 2009

Livestock	No.
Cattle	17,467,774
Sheep	17,129,606
Goats	27,740,153
Camels	2,971,111
Donkeys	1,832,519
Pigs	334,689
Indigenous chicken	25,756,487
Commercial chicken	6,071,042
Beehives	1,842,496

Source: Government of Kenya (2011)

6.2.5 Livestock Census

Even though there was counting of livestock during the national population census, there is need for more data and information on breeds, numbers, locality, production systems and the management skills of stockowners, breeders and producers. Reliable data and information are needed to assess the current status of animal genetic resources in the country, to facilitate more effective and strategic planning and management at all levels. The livestock data should be stored in a national databank as part of a national livestock census programme.

Beef production

The ASAL support over 6 million beef cattle and account for about 70 per cent of total beef consumed in the country. The average annual beef production is about 320,000 metric tonnes with a great export potential to the emerging markets in Eastern and Central Africa. The future production of red meat depends on effective disease control to restore production for exports, better market information and improved livestock infrastructure.

Camel production

There is high potential for camel rearing especially in the ASALs. Camel is important in addressing food security due to its ability to tolerate and continue being productive under drought conditions. Additionally, camel milk, despite its nutritious value, has limited market outlets due to traditional consumption preferences in the country. Therefore, to improve the livelihoods of ASAL communities, there is need to popularize camel milk and meat consumption to other regions.

Fish production

Fish farming has a potential to contribute 50 per cent of total fishery output; the current contribution is 2.5 per cent. The harvest from fisheries (from lakes) has decreased from about 128,000MT in 2007 to about 123,000MT in 2010. Fish farming, on the

other hand, has increased from 4,000MT in 2007 to 12,153MT in 2010 (Table 6.3).

Table 6.3: Volume of fish production (metric tonnes), 2007-2010

Year	Fish farming	Fisheries	Marine fish
2007	4,245	128,888	6,355
2008	4,452	126,672	7,561
2009	4,897	136,529	7,811
2010	12,153	123,631	7,600

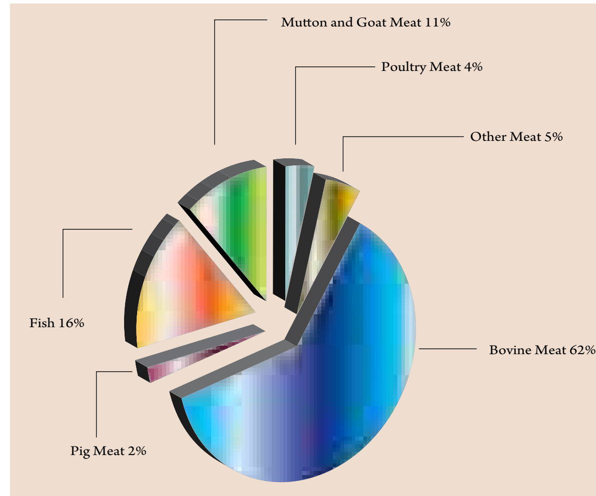
Source: Ministry of Fisheries Development

The government, through the Economic Stimulus Programme, has invested Ksh1.12 billion to promote fish farming (i.e. aquaculture). Initial reports (2010) show that a total of 26,559 ponds were constructed in 140 constituencies. This means that in 2011, there may be a surplus in fresh fish. There is enormous potential in the number of species that can be produced such as oysters, salmon, mussels, carp, trout and shrimps, which increase supply to specific market niches.

6.2.6 Livestock and Fishery Consumption

Figure 6.5 shows that per capita meat consumption is still heavily skewed towards beef, with only 4 per cent of the population consuming poultry. Fish consumption is currently estimated at 16 per cent although this is expected to change with the increase in production from fish farms, which is a positive contribution to the dietary needs of the population.

Figure 6.5: Proportion of meat consumption per capita in 2010



Source: Government of Kenya (2011)

6.2.7 Water and Agriculture

Water is critical for viable agricultural production. The total actual renewable water resource for Kenya stands at 31km^3/yr, with a dependency ratio of 33 per cent. Per capita availability is 840m^3/yr (2006) (AQUASTAT, 2009). Food security has continued to be a concern for the country since independence, mainly because of the reliance on renewable water resources that are declining at a rate of 9 per cent according to the MDG water indicator. It is with this backdrop that it is important to look at agriculture as an integrated multiple use system within an agro-ecosystem.

Access to water for agricultural purposes needs to be improved through water rights and investments in water storage, technology and delivery infrastructure including promotion of sustainable agricultural practices so that the ecosystem is able to cope with other competing needs for water. For instance, in the highlands, focus should be on storage, while in the semi-arid and arid areas, focus should be on water harvesting technologies and water-efficient technologies for production.

Kenya is struggling with frequent dry spells and declining land productivity. One immediate solution that will increase agricultural output and reduce dependence on rainfall will be to develop irrigation infrastructure. The National Irrigation and Drainage Policy identifies irrigation and drainage development as key to increasing cropped area and crop yields. The country's irrigation potential is estimated to be 495,626 Ha, which is distributed in the following basins: Lake Victoria (45%), Tana River (26%) and Rift Valley (18%) (Government of Kenya, 2009). The development of irrigated agriculture will not be without challenges; some of

the immediate ones include issues of quantity, cost and quality of water available for irrigation. It is critical to develop systems that are innovative and based on low water requirement. At the same time, the systems should be economically productive to compete with industrial and domestic uses. In Israel, for instance, the country has developed policies to anticipate the future needs for water, food security and agricultural production. The emphasis is on integrated water management that accounts for both conventional and non-conventional sources of water. The country has utilized most of the available renewable potential and is now focusing on the marginal resources such as improvement of field efficiency, modifying cropping patterns and reclaimed municipal waste water.

Table 6.4:Irrigated land as a percentage of agricultural land

Country/Year	2005	2006	2007
Uganda	0.1	0.1	0.1
Ethiopia	0.5	0.4	0.5
Kenya	1.6	1.6	1.8
Japan	36.3	36.1	35.9
Korea	52.1	51.4	51.6
Egypt	100.0	100.0	98.5

Source: World Bank (2011)

Table 6.4 shows a country comparison of the percentage of irrigated land as a share of total agricultural land. Kenya lags behind in comparison to the Asian economies and Egypt.

6.2.8 Agricultural Sector Institutional Performance

Resource allocation and expenditure review

Resource allocation to the agriculture and rural development (ARD) sector averages at about 4 per cent per annum of national expenditure for the last four years. Spending increased between 2006/07 and 2009/10 from Ksh 16.9 billion to Ksh 23.9 billion (Ministry of Finance, 2011). Table 6.5 shows that most of the ministries are able to absorb their recurrent budgets. However, there is increasing concern about the inability to absorb the development budgets. The ministry that is least able to absorb its development budget is that of livestock development. The Ministry of Lands' budget in 2009/10 was higher than the allocated, but more than double this can be accounted for by the accelerated programmes that were put in place after the post-election violence in 2007/08.

Table 6.5: Budget absorption capacity (%) in the agricultural sector

Ministries	Recurrent budget			Development budget		
	2007/08	2008/09	2009/10	2007/08	2008/09	2009/10
Agriculture	134	96	101	110	106	84
Cooperatives and marketing	99	97	71	80	59	57
Fisheries	93	96	93	91	53	83
Lands	109	101	96	77	54	232
Livestock	111	96	86	40	48	59
Overall	117	97	94	82	84	92

Source: Ministry of Finance (2011)

Resource allocation is obviously not up to the level it ought to be. However, absorption of the development budget is a major concern, especially in the Ministry of Livestock. Logically, one may argue that even if there is increased investment, the sector may not have the "spending capacity".

Overview of selected projects in the sector

There are a number of development programmes in the sector aimed at transforming the face of agriculture within the broad aspirations of Vision 2030 and Agricultural Sector Development Strategy - ASDS (2010-2020). These programmes include flagships projects, facilitation services (research, extension) and public-private partnerships (financial services). A few are highlighted (Ministry of Agriculture, 2010) below:

National Extension Services

The national extension services are guided by the National Agriculture Sector Extension Policy (NASEP) and are delivered through the National Agriculture Livestock Extension Programme (NALEP). Notable achievements include:

i. Accelerated uptake of farming technologies (such as poultry vaccination, improved soil fertility management, dairy feeding, cattle dipping and goat keeping) from 6 per cent to 23 per cent. The general uptake of agricultural credit remained low at 22.6 per cent, mainly due to lack of information on where to get credit and fear of inability to repay.

ii. Enhanced farm productivity, consequently contributing to an increase from 2 per cent to 6 per cent in the proportion of farmers having marketable surplus of maize, sorghum, beans and animal products and a reduction in cases of nutritional deficiencies (Kwashiorkor and Marasmus) within the households.

iii. Formation of Common Interest Groups (CIGs) that has enhanced commercialization of diverse agricultural enterprises.

iv. Increased income for 69 per cent of the farmers from farm production. However, most households (67%) are still unable to satisfy their household needs solely from farm incomes because of low agricultural productivity levels and reliance on rain-fed production.

v. Capacity building for most of the extension staff was achieved (73%); however, the sector is still male-dominated.

National Accelerated Agriculture Input Access Programme (NAAIAP)

The focus is to improve access and use of farm inputs, and provide supporting services. So far, the project has increased the productivity of maize from 3bags/acre to 22kg/acre. There has been an increase in fertilizer and certified maize use from 10 per cent to 15 per cent in the district covered by the project. Farm business credit has been provided through Equity Bank, amounting to Ksh 993.9 million as shown in Table 6.6 (Ministry of Agriculture, 2010).

Table 6.6:Credit from Equity Bank

Recipients Category	Amount Ksh (millions)	No. of Beneficiaries
Small-scale farmers	735.7	27,742
Stockists	66.2	228
Large-scale farmers	191.9	589
Total	993.8	28,559

Source: Ministry of Agriculture (2010)

Community Agricultural Development Project in Semi-Arid Lands

The objective was to increase agricultural production in a sustainable manner in Keiyo and Marakwet districts. The project has achieved several outputs including: capacity building for farmers and frontline extension staff, provided technical support to service providers, verified farmer-friendly technologies such as water harvesting, crop husbandry, and developed guidelines for community agricultural development.

Small Dairy Research and Development Project

This is a collaborative project between the Ministry of Agriculture, International Livestock Research Institute (ILRI) and KARI. Achievements include a pro-poor advocacy campaign based on empirical evidence on the importance of the informal milk sellers in the country's economy and poor population. Together with stakeholders in the dairy sub-sector, it contributed to policy debate and provided information and analysis to support the policy making process. Extension and training materials on fodder preparation and milk preservation were developed in English, Swahili and some local languages.

Cross-cutting Challenges

A general synthesis of the challenges affecting most of the projects and programmes in the sector highlights the following:

i. Inadequate technical staff capacity.

ii. Weak linkage between stakeholders in the projects and, therefore, no clear strategy for replication of initiatives.

iii. Delayed disbursement of funds.

iv. Inadequate promotion of public-private partnerships.

v. Inadequate market linkages.

Administrative capacity to generate and implement programmes/ projects

Staffing levels for technical departments are short of the recommended levels, especially when the decentralized government system is taken into account. Table 6.7 shows the staffing levels for the sector ministries. The Ministry of Livestock Development (MLD) has the highest deficiency of technical staff of about 66 per cent and 60 per cent for veterinary services and livestock production, respectively.

Table 6.7:Sector human resources

Ministry	Department	Approved Establishment	In-Post	Variance (%)
Ministry of Agriculture	Support staff	2,272	2,298	-1.1
	Technical	5,316	2,298	36.8
	Total	7,588	4,596	
Ministry of Livestock Development	Support staff	365	229	37.3
	Veterinary services	9,347	3,150	66.3
	Livestock production	5,675	2,292	59.9
	Total	15,387	5,671	
MCD&M	Support staff	935	626	33
	Cooperative Dept.	681	476	30.1
	Total	**1616**	**1102**	
MoL	Total	6,748	3266	51.6

Source: Strategic Plans (2008-12)

With devolution and county governments, this challenge is going to be more evident; recruitment has not matched the creation of more administrative units in the past. As an initial stop-gap measure, the government could seek public-private partnerships to assist in providing extension services. At the same time, it should encourage the counties, districts and divisions to tap into devolved funds and seek partnerships to facilitate the provision of public services.

Functions of the sector ministries

The agricultural and rural development sector has five different ministries, each with specific mandates to run their sub-sectors. However, some of the functions of the sector ministries tend to overlap, are duplicated, or underperformed by the ministry. The Ministry of Fisheries has been used as an example to highlight some of these discrepancies (KIPPRA, 2011).

Some of the areas that are duplicated include:

i. Regulation of fisheries activities in reserve areas such as game parks, reserves and marine parks; where Kenya Wildlife Service is responsible for the parks and reserves, and the Ministry of

Forestry Development provides the licences for fishing.

ii. Fish export licensing and provision of export levies.

iii. Monitoring and surveillance of the fishing areas.

Some functions that could be better performed by other agencies are:

i. Development and management of beach infrastructure.

ii. Community awareness and empowerment.

iii. Production of fingerlings.

iv. Manufacture of fishing gear.

v. Conservation of the fisheries ecosystems.

Some functions that would be better performed by the fisheries ministry are:

i. Enforcement of fisheries standards and quality assurance.

ii. Monitoring and surveillance of beaches.

iii. Registration of fish farmers.

iv. Pilot development of value added fish products in partnership with the private sector.

Agricultural marketing institutions

As market exchange grows increasingly complex, both formal and informal institutions have evolved to minimize transaction costs. This enforces contracts that build trust and promote reputation and social capital and institutions have emerged in various contexts to facilitate trade. There are several market institutions in the sector. An overview is given for selected sub-sectors for crop and livestock production:

Horticulture

The sub-sector has public and private market institutions, with the latter playing a more dominant role in the development of the sector and the former playing a regulatory role. The factors that have led to the success of the institutions include:

- The involvement of a highly-driven and professional private sector.
- Access to both local capital and Foreign Direct Investment (FDI).
- Development of good relationships with the major importers in the European Union (EU).
- Development of formal joint ventures to attract investment from abroad.
- Access to high level pre- and post-harvest export skills.
- Access to information/knowledge on market niches and customer requirements/dynamics.

The main challenge affecting horticultural marketing institutions is the missing link between production and marketing systems for export commodities and the production and market systems for the domestic market. Also, there are no strong linkages between the export-focused value chains and the domestic ones.

Industrial crops

Coffee and tea are expected to continue being the country's leading agricultural export earners among the traditional export crops.

Tea

The marketing institutions involved include tea processing factories, the Kenya Tea Development Authority (KTDA), the Tea Board of Kenya (TBK) and the East African Tea Trade Association (EATTA). These institutions have been successful largely because Kenyan tea is competitive in the world market due to its unique quality, and there are only a few actors involved in the value chain. Another critical success factor is that its production and marketing has been clustered to meet the different needs of stakeholders.

Some challenges include the over-reliance on a few export markets, which in the recent past are becoming prone to political unrest, especially in the Arab markets. In the smallholder clusters, there has been an increase in marketing inefficiencies due to high transaction costs.

Coffee

Coffee marketing has had several challenges in the recent past. Top on the list is the outstanding loan portfolios, especially among the farmers' cooperatives and the near-collapse of the Kenya Planters Cooperative Union (KPCU). This has resulted in herding behaviour among coffee marketers, which has not been successful due to market inefficiencies and inadequate supply. The government in 2006 set up the Coffee Development Fund to provide credit to the sub-sector so as to increase supply. Four years down the line, the fund's size has grown to Ksh 1 billion, having lent out Ksh 483 million by the end of the 2008/09 financial year with 7,000 coffee farmers having benefitted from the fund.

Grain markets

The National Cereals and Produce Board of Kenya (NCPB) is mandated to regulate and control the marketing and processing of grains. The board has functions that include buying and maintaining grain on behalf of the Strategic Grain Reserves (SGR), buying, maintaining and distribution of Famine Relief Stocks (FRS), distribution of farm inputs and logistics support services. There are institutional gaps in grain trade and food distribution including lack of properly organized storage facilities for farmers. There are inadequate institutional mechanisms to set up prices and manage risks. Since liberalization, NCPB can be considered to be a buyer of last resort, which is unable to meet its financial commitments to producers on time.

Some suggestions

Market reforms have been ongoing in the sector since the adoption of market liberalization. However, market development in the sector is still wanting. Several issues still affect the sector; top on the list is price. Commodity prices have remained unstable, while production has more or less stagnated. This affects both the producers who need to stay in production and the consumers who need to purchase food at favourable costs. There is high variability of price within the production seasons and between successive market years, making price stabilization critical. Some of the possible interventions that can be put in place in an attempt to address the incompleteness of the market structure include:

i) Use of international futures and options markets

The use of hedging and "synthetic storage" has been tried and has worked to stabilize maize prices in Malawi and Zambia. This option was sold on the South African Futures Exchange (SAFEX). This strategy involves buying futures contracts, with a view to evening out the supply of grain because of the assured prices in both the seasons of bountiful or lean harvests.

ii) Facilitate warehouse receipt systems

By contracting private warehouse operators to store grain for a fee, public sector agencies can reduce cost for both warehouse construction and operations costs (staff, chemicals, etc). The warehouse operator

takes care of all physical handling and is held responsible for delivering specified weight and grade of commodity. The government will have achieved two goals with this intervention. Firstly, it will assure that the prices are within bounds that allow surplus production to continue, and secondly, it will have met the food security concerns of consumers.

iv) Promote on-farm storage

Post-harvest losses increase due to several factors, including poor storage. Lack of proper storage at farm level necessitates the farmers to sell in order to avoid losses, and this tends to accelerate intra-seasonal price instability.

v) Provide incentives for the private sector to invest in storage

Livestock legal and market institutions

A number of legislations affect livestock marketing. These include: the Animal Diseases Act; Hides and Skins Act; Stock and Produce Theft Act; Stock Traders Licensing Act; Pig Industry Act; Dairy Industry Act; Co-operatives Act; Hatchery Rules; Kenya Meat Commission Act, and Veterinary Surgeons and Veterinary Para-professional Act. A few of these are highlighted:

Veterinary Surgeons and Veterinary Para-professional Act

The Sessional Paper on National Livestock Policy acknowledges that the existing legal and regulatory framework is inadequate to address current and future challenges in the sector. In response, some of the old Acts such as the Veterinary and Surgeons Act Cap 366 have been reviewed, awaiting parliamentary approval. This new Act accommodates the operations of para-veterinarians who play an important role in livestock disease and pest control.

Disease Free Zoning (DFZ)

Increasing market access is key in developing the livestock sub-sector. The DFZ programme addresses the main challenges in the livestock sub-sector performance, which has high prevalence of trade-sensitive diseases, and the resultant failure to access high-value markets. The programme is consistent with the government policies of mainstreaming the development of ASALs in the economic framework of the country, as some of the areas targeted are located in these high potential lands. Even though the DFZ is not currently anchored in law, the Animal Diseases Act, Cap 364, can be effectively used to support its operations.

Kenya Meat Commission (KMC)

KMC has since been revived with assistance from the government. However, it is yet to reach its optimal operational capacity due to a myriad of constraints, including obsolete machinery. Before its collapse, KMC was a buyer of last resort, especially in times of drought, and provided services for drought management and disease control. The institution had holding grounds in various parts of the country, which helped facilitate these objectives. It is interesting to note that despite there being a marketing gap, the private sector has not been able to take up the role of KMC effectively; there is always a crisis in times of drought and the government is forced to step in.

Currently, there are a number of community-based organizations, associations, non-governmental organizations (NGOs), professional associations, cooperative societies, input suppliers and development partners who play a significant role in marketing. They collectively bring together farmers to pool their resources and efforts, in order to maximize their returns and facilitate access to inputs, credit, markets, market information, production, education, information and advocacy for their members.

Kenya Livestock Marketing Council

The Council is a private entity, with membership open to all livestock traders. The structure of the Council begins at community level reporting to the District Councils. The Districts Councils report to the National Council. So far, 10 District Councils have been formed in predominantly pastoral areas. The Council objectives include: advocating for the rights of traders; promoting livestock and livestock products, while marketing from pastoral areas; identifying market gaps locally, regionally and internationally; enhancing the dissemination of market information to both producers and traders; liaison with pastoralists at grassroot level; support the exportation of live animals to alleviate poverty; support the entrepreneurs investing in slaughterhouses, cold storages, and other premises; improve livestock marketing; undertake extension services in liaison with the government; and fund solicitation for credit facilities and offering group guarantees.

Some suggestions:

i. The legal framework that governs the industry should be updated and harmonized in order to facilitate and promote trade.

ii. There needs to be concerted effort by the stakeholders to develop livestock market centres that offer minimum infrastructure in livestock production areas in the country.

iii. There is need to promote and empower livestock traders' cooperatives, which will facilitate the development of processing plants and slaughter houses/abattoirs in the affected counties.

Livestock breeding

The Ministry of Livestock has a major responsibility of creating and facilitating a better environment for players in the breeding industry. This can be achieved through: the technical Departments of Livestock Production and Veterinary Services, and two regulatory boards, i.e. the Kenya Dairy Board (KDB) and the Kenya Veterinary Board (KVB). Currently, the Agricultural Development Cooperation (ADC) and private large-scale farms are the custodians of stud herds/flocks and the main source of breeding stock for the local and export markets. The Kenya Agricultural Research Institute (KARI), through its various livestock stations, conducts research on beef, poultry, dairy, sheep and goats. However, livestock breeding services in the country are currently fragmented and weakly coordinated among the institutions involved.

The Breed Societies have been promoting various breeds by setting breed standards and inspections for purposes of registration. The Kenya Livestock Breeders Organization (KLBO), for example, has been promoting the grading-up scheme and the pedigree registration of various breeds for breed improvement, while the Kenya Stud Book (KSB) has been involved in maintaining authentic ancestral and identification records of livestock in the country. The inadequate coordination and harmonization of activities carried out by various breeding organizations has adversely affected the implementation of national breeding programmes. Further, lack of guidelines, expertise and planned recruitment of breeding stock for the local and export market has led to the export of non-registered animals as well as depletion of the national genetic resource.

Agricultural credit

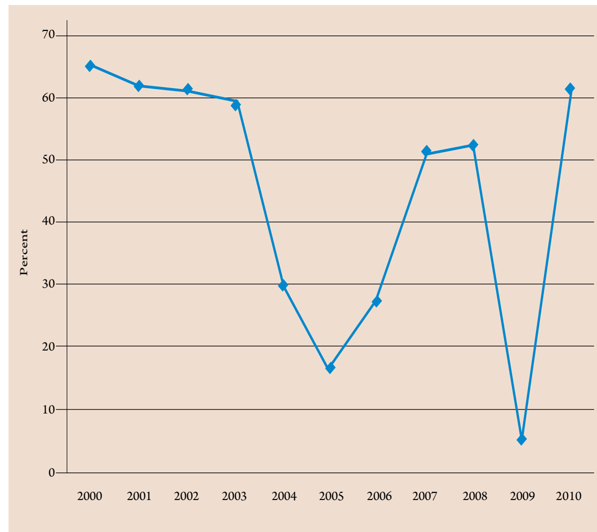
The financing of agriculture continues to be a challenge despite the progress made in access to credit. The sector is characterized by seasonal cash flows, rural bias, widely dispersed producers, and marketing risks. The sector's demand for credit is enormous, especially with the recurrent drought spells increasing the need to cushion farmers to enable them to stay in production.

Since adoption of market liberalization, seasonal input credit is mainly provided by commercial

banks, microfinance institutions and private agricultural marketing companies. The cooperatives and government agencies that offered seasonal credit have since taken a smaller portion of the credit market. The economic reforms in the country have provided fertile ground for commercial banks to provide credit, which has become more accessible.

The government, through the Agricultural Finance Corporation (AFC), has been advancing credit to farmers, though limited because of financial constraints. Over the years, AFC has accumulated non-performing loans, which the government, from time to time, has written off on behalf of farmers. However, such write-off initiatives have been met with scepticism due to the possible effect on the credibility of the institution. As at 2010, the performing loan portfolio was at Ksh 3.8 billion and non-performing loans were Ksh 2.4 billion (AFC, 2011). Figure 6.6 shows the trend of performing loans as a percentage of the total loan portfolio where it is clear that weather and political-related shocks affect the repayment of loans.

Figure 6.6: The percentage of performing loans in comparison to the total loan portfolio



Source: Agricultural Finance Corporation (2011)

Micro-credit Finance Institutions (MFIs) have responded to the credit gaps by working with community-based organizations and groups to provide collateral for monies borrowed. In 2009, the country had 62 registered micro-finance NGOs; they are based on the concepts of mutual guarantees, unsecured and character-based lending (Ministry of Agriculture, 2009).

Contract farming is the other avenue that has been used by agricultural marketing companies to stimulate production by providing credit, technology and inputs while assuring and linking farmers to markets. The requirement of quality assurance and traceability, especially for exports to Europe, has driven the development of contract farming in horticulture. It is becoming a viable means of assuring agricultural product supply to markets even where missing markets or imperfect markets exist (World Bank, 2007). Structured functioning contractual arrangements can be the main solution to production, marketing and institutional problems.

Cooperatives

Cooperative development promotion efforts started soon after independence to facilitate commercialization of the smallholder farm sector. Savings and Credit Cooperatives (SACCOS) have played an increasingly important role in the socio-economic development of the country. According to a recent survey conducted by the Kenya National Bureau of Statistics, 11.9 per cent of the population borrows from SACCOs compared to about 4.0 per cent and 3.6 per cent levels for commercial banks and micro finance institutions, respectively.

Based on the historical bias, most agricultural commodities such as maize, wheat, tea, coffee, horticulture and dairy have had marketing institutions that enjoyed monopoly to market these outputs before the adoption of the market liberalization policy in 1993. Since then, with the exception of tea, most of the other commodity-based marketing institutions have lost their roles and now play secondary marketing agency roles.

Cooperatives continue to provide access to credit, and promote value addition and trade within the agricultural sector. The government has put in place a new cooperatives development policy and a cooperatives investment policy, in addition to the formation of the SACCO Regulatory Authority governed by the SACCO Regulatory Act. All these efforts will have a positive impact on the growth of the sub-sector.

Investment in agricultural research

According to the World Bank (2008), investment in agricultural science resulted in an average rate of return of 43 per cent in 700 development projects evaluated in developing countries. The capacity of the country to invest in laboratories and analytical services and strategic research capacity increases the effectiveness of both applied and adaptive research, thus in the long-run meet the country's food security needs. To be able to produce more food will largely depend on increasing crop yields and not farming more land.

A comparative analysis of spending in research provided by the Agricultural Research Intensity (ARI) ratios and the latest global statistics from 2000 show that in developed countries, public spending on agricultural research is about 2.4 per cent of Agricultural GDP. This is almost five times that of developing countries, which is estimated at 0.62 per cent. The global average is 1.04 per cent, while that of Sub-Saharan Africa is 0.79 per cent. The World Bank in the 1980s had given a preferred intensity ratio of 2 per cent; however, 1 per cent was found to be more realistic. Nonetheless, most countries in Sub-Saharan Africa have not achieved this target (Beintema and Stads, 2010). This data may be dated but it gives a realistic indication that would still apply today to the investments in agriculture.

KARI accounts for almost half of the researchers and spending on agricultural R&D in the country. Public agricultural research and development (R&D) expenditures vary from year to year, largely because funding is mainly provided by the government and donors contribute an estimated one third of the budget. The government has also established a national research fund under the National Council for Science and Technology, where research institutes, universities and other agencies may submit proposals for funding.

6.3 Medium Term Prospects for Agriculture

The sector is expected to record positive growth experienced in 2010 despite the poor weather conditions in the last quarter of 2010. The underlying assumptions are that the investment made in 2009/10/11 to revive the irrigation schemes under the Economic Stimulus programme, and programmes such as the National Accelerated Agriculture Input Access Programme (NAAIAP) will continue to bear positive results.

Based on KTMM estimates, GDP growth will be 7.5 per cent in 2012, 8.6 per cent and 9.8 per cent in 2013 and 2014, respectively. It is safe to assume that given the favourable weather conditions, the agriculture sector will also grow since the economy is agriculture-based. This growth will be pegged on increased access to physical markets and market information, increased production from the irrigation schemes and crop yields from increased use of inputs.

As the country prepares for the devolved system of government, it is expected that there will be increased investments in value addition for agricultural products, so as to increase the amount of marketable produce from the different county governments. This is expected to spur production of raw materials and increase adoption of technologies to meet the demand from this market niche.

6.4 Policy Directions

6.4.1 Review and Harmonization of the Legal, Regulatory and Institutional Framework

- To ensure a conducive environment for competitive agricultural production and marketing as well as collaborations and partnerships in the sector, there is need to fast-track the ongoing consolidation of agricultural policy and legal frameworks in line with the Constitution of Kenya 2010.

- Efforts are being made to strengthen institutional capacity by focusing on restructuring of the sub-sector and its institutions for improved coordination. This can be achieved by developing an integrated information management system and providing for an efficient planning and management system.

6.4.2 Production

There is need for targeted efforts to improve and increase agricultural output per unit area. Focus should go to promotion and implementation of existing technology, knowledge and best practices along the value chain. This will ensure that there are adequate linkages between and with the different actors at stages along the chain. Specifically, investment should be focused towards how to remove crippling bottlenecks at the different stages.

Biotechnology offers an avenue of improving food security and reducing pressures on the environment. However, widespread use will depend on whether food safety, environmental concerns and socio-cultural perceptions/concerns are adequately addressed. A safeguard mechanism to manage risk could be through implementation of a virtual reserve backed up by a financial fund to calm markets under speculative situations.

6.4.3 Agricultural Finance and Credit

Agricultural financing and credit is critical for the development of the sector, moreso in the light of the Constitution. Since the issue of resource allocation, management and reorganization will affect how much budget the sector gets, emphasis should be put on the development budget so that the necessary infrastructure can be put in place to cater and anticipate future agricultural production needs. The sector is expected to undergo institutional reforms towards devolved government structure. Therefore, it will require the concerted efforts of all the stakeholders to ensure that the process does not impact the programmes negatively. Fundraising and participation of the private sector will be critical in ensuring that programmes are able to meet their medium-term objectives.

Increased access to financial services, savings and credit products and transfer services for remittances will go a long way to expand opportunities for producers to be more efficient in technology adoption and resource allocation.

6.4.4 Marketing and Value Addition

The importance of marketing and value addition cannot be overemphasized in agricultural production. Focus should be on empowering the producers, facilitating market linkages and expanding/developing agricultural market information systems. These should include initiatives such as building the capacities of district councils and local communities to sustainably manage their marketing infrastructure and building and/or rehabilitating identified marketing infrastructure.

In addition, it will be necessary to review all relevant legislation relating to fresh and processed farm products in terms of packaging, quality, handling, labelling and health standards with a view to making them relevant, and establishing effective and efficient frameworks and mechanisms for surveillance and enforcement.

ENDNOTES

1 2008 -2010 are estimated, FAOSTAT does not provide the data.

Chapter 7

Wholesale and Retail Trade

7.1 Introduction

The trade sector is one of the key sectors to play a crucial role towards attainment of national development objectives in Kenya, especially under Vision 2030, towards the achievement of the Millennium Development Goals (MDGs) Number 1 on Eradicating Extreme Poverty and Hunger and Number 8 on Developing Global Partnerships for Development. In Kenya, the trade sector provides an evolving link between producers and consumers, and contributes significantly to the national economy.

The trade sector comprises five economic areas, namely: distribution and wholesale trade, retail trade, international trade, informal trade, trade in services and electronic trade (e-commerce). The trade sector can be divided into two broad categories: domestic and international trade. Wholesale and retail trade falls within domestic trade. Wholesale and retail trade is one of the key sub-sectors in the economic development agenda of Kenya, which is expected to expand substantially as the economy moves towards a 10 per cent growth target. It is because of its contribution to GDP and employment that Vision 2030 has identified and earmarked it as one of the key sectors to spearhead rapid growth and development. This sub-sector also has strong backward and forward linkages with other sectors of the economy. For instance, it provides a link between production and consumption, both of which are expected to expand substantially with economic growth. Wholesale and retail trade has been one of the most rapidly-expanding sub-sectors of the economy since the introduction of trade liberalization in the 1990s by way of employment creation.

The wholesale and retail trade sub-sector has great potential for employment creation. However, the sub-sector faces a number of challenges that need to be addressed for it to thrive. For instance, most of the employment in the wholesale and retail trade tends to be found in the informal sector, with a few jobs in the formal sector. The other challenge facing this sub-sector relates to inefficiencies along the supply chain, from the producer to consumer and from the importer to the final buyer. On informality in employment, the policy concern has been on how to mainstream the informality of the sector into the formal economy. Some of the proposed interventions include provision of secure business location, credit, training and access to markets. Such efforts will bring the informal segment of the sector closer to the formal sector, and ultimately gain entry into the regional and global markets. There have also been suggestions for improving efficiency and productivity in the sub-sector. It is argued that wholesale and retail trade has great potential to benefit both producers and consumers and to

improve the distribution of local and imported goods. Ultimately, if well streamlined, wholesale and retail trade has the potential to lower the cost to consumers and to immediate producers. Kenya's commitment to regional integration undoubtedly has an implication on the performance of this sector. On one hand, regional integration is expanding the market for wholesale and retail traders who can access the growing market. On the other hand, integration may create competition in Kenya's domestic market.

In the Vision 2030 Medium Term Plan 2008-2012, the flagship projects that are expected to contribute to the growth of the trade sector were identified as follows:

1. Develop a free trade port in Mombasa.

2. Create at least 10 hubs and 1,000-1,500 Producer Business Groups.

3. Build at least 10 tier one market with a pilot project in Athi River.

4. Construct wholesale, retail and hawkers' markets.

5. Develop Business Process Outsourcing/off-shoring parks.

6. Business linkages and sub-contracting programme sources.

This chapter reviews the performance of the wholesale and retail sub-sector for the period 2007-2010 and examines the role of institutions in the sub-sector performance. Specific objectives are to:

a. Compare performance of the sub-sector with the targets set in various policy documents.

b. Examine the extent to which performance gaps can be explained by institutions in this sub-sector in the context of Vision 2030 and the Constitution of Kenya 2010.

c. Analyze effectiveness of selected institutions in this sub-sector.

d. Suggest policies for institutional reforms in the sub-sector.

Under the Constitution of Kenya 2010, international trade is a function of the national government, while domestic trade is managed under the county governments. The 4th Schedule of the Constitution, Part 2, points that the county governments will be in charge of trade development and regulation, including markets, trade licences (excluding regulations of professions), fair trading practices, local tourism and cooperative societies (Government of Kenya, 2010).

7.2 Overview of Wholesale and Retail Trade

The supply chain for household goods begins with both domestic and overseas manufacturers and agricultural producers who produce goods for consumption. Goods reach wholesalers and retailers with the assistance of transport and logistics companies, which make use of road, air and sea modes of transport. Both domestic and overseas manufacturers as well as agricultural producers supply household goods for the domestic market. Often, overseas goods will compete with locally-produced ones.

The wholesale and retail sub-sector in Kenya is highly fragmented, consisting predominantly of many informal players, a large number of medium-scale retailers and a few large supermarkets mainly located in urban areas. The informal retail sector is dominated by trade in agricultural perishable goods, which are primarily produced by smallholders throughout the country. Kenya's traditional retail system comprises formal constructed public markets, small shops and street hawkers. It is characterized by fragmentation,

single units rather than chains, market power with wholesalers, long channels, direct payment to suppliers, a strong presence of women traders, little quality control, little grading, few standards and small inventories. Retailers acquire their products in three different ways:

i. Import from overseas;

ii. Directly from local manufacturers or primary producers; or

iii. From local wholesalers.

Retailers operate in urban areas and rural areas in accessible and remote locations throughout the country.

These distinct geographical regions pose a number of difficulties for retail businesses, impact upon retail supply chains, and have implications on the range and price of food and other products available in these distinct geographical zones.

On one hand, wholesalers primarily engage in selling merchandise to retailers dealing in industrial, commercial and institutional goods, farm inputs, construction materials, or acting as agents or brokers in buying or selling. They act as middlemen between the producers/manufacturers and the retailers, although in a few cases they supply merchandise directly to final consumers. On the other hand, the retail trade sub-sector comprises enterprises generally engaged in retailing goods and services without transforming the physical nature of the product, except bulk breaking. These enterprises fall into various categories, which include the general retail shop or specialized retailers such as food, beverages and tobacco; butcheries; oil and petrol/ gas dealers; building materials, timber, and domestic hardware. Others deal in textiles, soft furnishings, clothing and shoes; photography; pharmaceutical goods; restaurants, cafes and other eating and drinking, and lodging places.

Since the mid-1990s, the sector has experienced rapid transformation with the emergence of self-service stores (mainly supermarkets) increasingly re-shaping consumers' shopping behaviour and in the process expanding domestic market shares. The modern retail industry, though at a nascent stage, has exploded the wholesale and retail scene and developed different store formats to reach different customer segments. Modern retailers include hypermarkets, supermarkets, shopping and "exhibition" malls, which are springing up in major urban centres. Currently, supermarkets control approximately 35 per cent of the retail sub-sector business. It is estimated that Kenya has about 300 registered supermarkets spread in various parts of the country. Hypermarkets cover about 2,250m^2 (24,460 square feet) and large parking areas in major cities such as Nairobi, Mombasa and Kisumu. These attract high and middle income shoppers. The three clear market leaders in supermarket trade in Kenya are Nakumatt, Uchumi and Tuskys. Nakumatt and Uchumi have outlets spread across major towns in Kenya. Nakumatt Holdings currently has 29 stores spread across Kenya, Uganda and Rwanda, making it the largest retail chain in the region, while Uchumi currently employs over 1,000 people and operates 15 branches – 11 in Nairobi, 3 up country (Karatina, Meru and Eldoret) and 1 in Kampala, Uganda. The second tier of supermarkets cover about 150m^2 (1,625square feet) and target middle to low income urban consumers (Government of Kenya, 2011). These include, among others, Tuskys, Ukwala, Metro and Naivas supermarkets. The third and largest tier comprises smaller self-service shops, including mini-supermarkets and convenience stores.

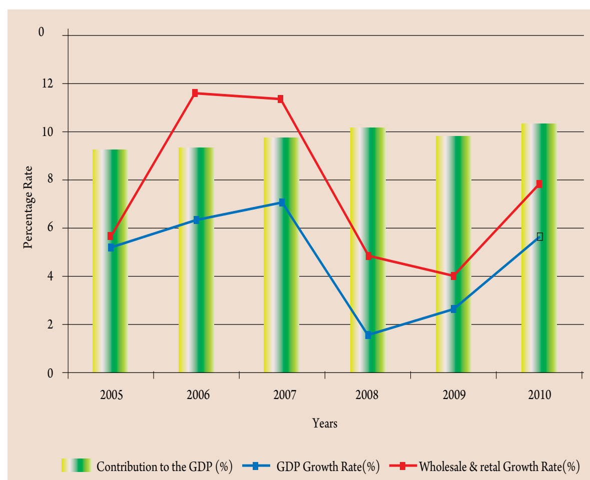
The rise of supermarket retail has transformed the traditional supply chain and influenced the conditions and structure of the agri-food system. For instance, they control their supply chains through introduction of standards, contracts, distribution centres and information technology systems. Direct sourcing facilitates a shift from brokers to dealing with producers directly to control quality, supply reliability and price stability.

7.3 Performance of Wholesale and Retail Trade

Over the last three years, the wholesale and retail sub-sector registered improved performance; the sector was valued at Ksh 154,558 million in 2010 up from Ksh 131,754 million in 2007. As a share of the GDP, it contributed 9.7 per cent in 2007 compared with a contribution of 10.3 per cent of GDP in 2010. However, the sector performance slowed down drastically from a peak growth rate of 11.6 per cent in 2006 to 7.8 per cent in 2010 as shown in Figure 7.1. The drop was mainly attributed to poor economic performance following the effects of the 2007 post-election violence, drought and the global financial crunch. However, the contribution of the sector to GDP has remained relatively stable at about 10 per cent over the years (Figure 7.1).

Like elsewhere in the world, the performance of the sector is pegged to GDP growth. Therefore, the higher the growth prospects for the Kenyan economy, the higher will be the expansion of the wholesale and retail trade sub-sector.

Figure 7.1: Performance indicators for wholesale and retail trade in Kenya



Source: Government of Kenya (2011)

7.4 Institutional and Regulatory Frameworks in Wholesale and Retail Trade

Prior to liberalization, the government had a policy that provided guidance on how distribution of both locally manufactured and imported goods was to be undertaken. The policy prohibited manufacturers from engaging in distribution, wholesale or retail trade. Similarly, an importer of bulky common user goods could not be licensed to engage in retail trade. The government had also established State Trading Enterprises (STEs) to deal with distribution of bulky commodities that were considered essential for the welfare of Kenyans.

Some of these State Trading Enterprises are the Kenya National Trading Corporation (KNTC), the National Cereals and Produce Board (NCPB), the Kenya Farmers Association (KFA), the Kenya Meat Commission (KMC), the Kenya Seed Company (KSC), the New Kenya Co-operative Creameries (NKCC), the National Oil Corporation, among others. These enterprises were established to enhance the efficiency of the distributive trade. However, due to poor management, these State Trading Enterprises became inefficient.

With the liberalization of the economy, the role of these State Trading Enterprises was minimized as the implementation of the policy was relaxed. This led to some manufacturers engaging in distribution of their own manufactured products as well as importers of bulky common user goods engaging in wholesale and retail trade, thus being in direct competition with retailers and wholesalers. Currently, some of the business firms whose core business is basically retail (supermarkets) are also undertaking distribution and wholesale, thus posing a big challenge to the small-scale distributors and wholesalers.

The current policy regime on distribution and wholesale is aimed at improving the business environment by removing regulations that are not

based on health, security and environment, and the government desisting from taking intervention measures except when there are market imperfections in the sub-sector. Overall, regulation of the wholesale and retail sub-sector involves a complex web of rules, laws and regulations administered by various ministries and other government agencies.

7.4.1 Business Registration and Licensing

The licensing of wholesale and retail businesses in Kenya is done by the Ministry of Local Government through issuance of single business permits under Section 163 of Cap 265 of the Local Government Act. The single business permit is normally issued by local authorities and allows for distribution of goods and services within the area of any other local authority. The latter permits the conduct of businesses or trade including profession or occupation within the area of local authorities. Such activities allowed by the permit include general trade, wholesale, retail, shops and services: distributors, traders, wholesalers, hypermarkets, department stores, supermarkets, show rooms, boutiques, retail shops and stores, personal service providers, kiosks, etc. Business licence fees range from Ksh 2,000 to Ksh 80,000 per annum depending on the category and size of business. The challenge to government is to rationalize the licensing regime and reduce the tax burden without compromising the provision of public amenities that are necessary for the growth and development of business enterprises in the country. Towards this, the Business Regulatory Reform Unit (BRRU) was set up in the Ministry of Finance to liaise with regulators in ensuring that licensing and regulations are carried out in line with international best practice.

7.4.2 Promotion and Business Development

According to the Presidential Circular No. 1/2008 of 30th May 2008, the Ministry of Trade is responsible for the promotion of retail and wholesale markets, development of micro and small businesses as well as fair trade practices and consumer protection. The Ministry is responsible for promotion of businesses through a number of programmes and activities including:

a. Provision of credit to small-scale traders under the Joint Loans Board (JLB);

b. Training and capacity building of business persons;

c. Improving the business environment;

d. Development of retail and wholesale hubs; and

e. Establishment of producer business groups.

7.4.3 Fair Competition and Consumer Welfare

Competition is currently guided by the Restrictive Trade Practices, Monopolies and Price Control Act, Cap 504. This is an Act of Parliament to encourage competition in the economy by prohibiting restrictive trade practices, controlling monopolies, concentration of economic power and prices. The Monopolies and Prices Commission of Kenya is a Department of the Ministry of Finance whose mandate is to enforce competition principles and rules in accordance with the provisions of the Restrictive Trade Practices, Monopolies and Price Control Act, Cap 504 of the Laws of Kenya. The role of the Monopolies and Prices Commission is that of economic regulation and entrenchment of the culture of competition through advocacy and other pedagogical issues. The Commission is mandated to encourage competition in the economy by prohibiting restrictive trade practices, controlling monopolies, and concentrating economic power and related activities in accordance with the provisions of Cap 504.

Competition in the wholesale and retail sub-sector is bi-polar, with highly competitive markets

in urban areas and minimal competition in rural areas. The competition in urban areas seems to be driven by the number of competing wholesalers and retailers carrying similar product lines. Wholesale businesses compete on terms of trade offered to customers, prices and services. The dominant role in domestic trade is acquired by large monopolies, which appear in specific organizational forms such as chain and branch systems, multi-unit systems and large department stores. The predominance of the monopolies is the basis for their receiving monopolistic commercial profits both through high prices on goods sold and through low prices on products bought from small producers. Monopolies captured the wholesale trade area first of all, and then spread their influence increasingly to retail trade by use of such forms of trade as shopping centres and self-service stores. Monopolistic tendencies in retail and wholesale trade, although not prominent in the Kenyan market, are slowly developing as the five main supermarkets spread to the countryside. Therefore, proper regulatory mechanisms should be put in place by the Ministry of Trade to ensure healthy competition.

7.4.4 Combating Counterfeits

The Anti-Counterfeit Act No. 13 of 2008 provides for prohibition of counterfeit goods in Kenya. The Act provides for the establishment of an agency, the Kenya Bureau of Standards, to undertake the following:

a. Enlighten and inform the public on matters relating to counterfeiting;

b. Combat counterfeiting trade and other dealings in counterfeit goods in Kenya in accordance with this Act;

c. Devise and promote training programmes on combating counterfeiting; and

d. Co-ordinate with national, regional or international organizations involved in combating counterfeiting.

Following the integration of regional markets under the EAC and COMESA trade regimes, there has been increased cases of illegal replication of known brand names and designs on packages and labels, flooding the domestic market with cheaper and substandard versions of locally-available products. Among the most imitated products include: dry cell batteries, alcoholic beverages and fruit juices, shoe polish, toothpastes/toothbrushes, soaps and detergents, ballpoint pens, books, electrical and electronic items. Others are perfumes, clothing, footwear, cosmetics, pharmaceuticals, automotive spare parts, computer software and hardware, audio and video tapes and CDs.

7.4.5 Health Standards and Quarantines

All business premises are subject to health inspection under the Public Health Act, Cap 242 of the Laws of Kenya. This is done in order to ensure practicable measures for preventing the occurrence or dealing with any outbreak or prevalence of any infectious, communicable or preventable disease, and to safeguard and promote public health. Besides, inspection of health standards is designed to provide consumers with a level of security regarding the safety of the food that they consume, and to provide businesses with guidelines on how to handle food. Breaches of food safety standards can harm the reputation of businesses and whole industries, hurting overall economic performance.

7.4.6 Labour Standards

The wholesale and retail sector constitutes one of the single biggest employment creators in Kenya. The Labour Relations Act No. 14 of 2007 provides for the registration, regulation, management and democratization of trade unions and employers' organizations or federations, promotion of sound

labour relations through protection and promotion of freedom of association, encouragement of effective collective bargaining, and promotion of orderly and expeditious dispute settlement conducive to social justice and economic development. Minimum staff welfare requirements, such as minimum wage levels and work place conditions, exist to protect employees who individually have limited bargaining power with employers. These minimum labour standards also help prevent exploitation and encourage citizens to find employment in the formal sector. The incentive for wholesalers and retailers to ignore these standards is the avoided cost of compliance.

7.4.7 E-commerce

E-commerce is the use of electronic communications and digital information processing technologies in business transactions. The growth of e-commerce is highly related to the growth of Internet usage. In 2007, Kenya's internet usage penetration was 3.2 per cent of the population, and this is expected to increase to 20 per cent by the year 2012. This target is premised on the basis of the world's internet penetration and usage of 17.6 per cent, which would provide Kenya with an opportunity to compete favourably with other countries trading under e-commerce. Currently, ICT issues are covered under various legislations in the Ministry of Information and Communications.

The rapid growth of the ICT sector has witnessed an increase in e-commerce. This type of trading is rapidly spreading in major stores and retail outlets across the country. However, it remains a major challenge in understanding and measuring the value of e-commerce in Kenya, due to the escalating e-commerce in various components of the economy.

E-commerce in Kenya is hampered by low levels of ICT usage among the Kenyan population, relatively high internet costs, limited use of credit cards and a nationwide credit rating system and lack of clear policies to support development of e-commerce. There is lack of legal and regulatory framework for e-commerce, and there is poor telecommunication infrastructure and internet connectivity. There are also instances where consumers are defrauded off their monies by unscrupulous traders. In order to improve e-commerce in Kenya, there is need to finalize the installation of the fibre optic cables across the country, liberalize network infrastructure and promote broadband competition, and establish a legal and regulatory framework to support e-commerce.

7.5 Effectiveness of Institutions in Wholesale and Retail Trade

7.5.1 Registration and Licensing

Despite efforts to streamline the regulatory framework for businesses, the number of licences affecting wholesale and retail trade is still large, in excess of 20. The number of licences is likely to increase when counties become functional as they seek to generate more revenue. So far, the Single Business Permit, which was intended to replace multiple licences and fees remains largely focused on revenue generation for local authorities, thereby burdensome to traders. Besides, the local authorities arbitrarily determine the licensing fees for businesses based on a very wide range of categories, hence giving scope for abuse. The lack of an appropriate inventory system for licensing further makes it difficult to collect and share regulatory-related information necessary for evaluation and strategic regulation of the wholesale and retail sub-sector. Besides, the multiplicity of government agencies with regulatory functions within the sector undermines effective regulation.

7.5.2 Competition and Consumer Welfare

The existing Competition Act No. 12 of 2010 aims to promote and safeguard competition in the national economy; to protect consumers from unfair

and misleading market conduct; and to provide for the establishment, powers and functions of the Competition Tribunal. It was designed to replace the Restrictive Trade Practices, Monopolies and Price Control Act, Cap 504, which was seen as being weak and lacking legal, institutional and technical enforcement capacity. The Competition Act was assented to on 30th December 2010, awaiting enforcement through a gazette notice by the Minister. Meanwhile, there have also been attempts by Parliament to enact legislation to control prices of essential commodities through the Price Control (Essential Goods) Bill, 2009, to further protect consumers (KIPPRA, 2010; Government of Kenya, 2009). The Bill, which has now been enacted, intends to fix the maximum retail and wholesale prices for essential goods, including maize, maize flour, cooking fat or oil, sugar, paraffin, diesel and petrol to check against unfair price increases.

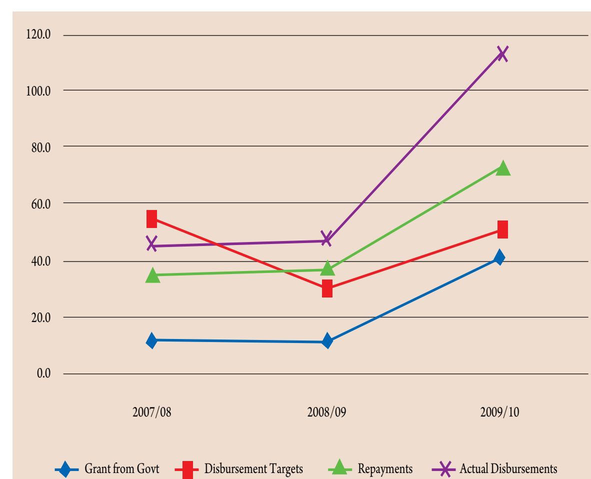
7.5.3 Funds Absorption Rates

Ministry of Trade

There was a general increase in budgetary allocation to the trade sector from Ksh 5.22 billion in 2007/08 to Ksh 10.70 billion in 2009/10. Overall, the absorption rates for the financial years 2007/08, 2008/09 and 2009/10 were 83.1, 96.8 and 94.0 per cent, respectively. Both recurrent and development budget absorption rates declined during 2009/10 as indicated in Table 7.1 .

With respect to the Joint Loans Board (JLB), which is the Ministry's key project for promoting domestic trade, there have been improvements in loan disbursements arising from both increased allocations by government and loan repayments as can be depicted from Figure 7.2. Over the review period, the actual number of beneficiaries increased from 1,163 during the period 2007/08 to 2,023 during 2009/10.

Figure 7.2: JLB performance (Ksh millions)



Source: Authors' own computations based on Department of Internal Trade Statistics

Ministry of Local Government

In Vision 2030, the physical infrastructure sector is recognized as one of the key drivers for rapid and sustainable economic growth and development. Within the wholesale and retail trade sub-sector, construction of wholesale and fresh-produce markets is one of the activities under the Economic Stimulus Programme (ESP). In 2007/08-2009/10, the government allocated Ksh 1.8 billion for the construction of prototype fresh-produce and wholesale markets in 180 constituencies to be implemented by the Ministry of Local Government.

Table 7.1:Analysis of recurrent and development expenditure for the Ministry of Trade (Ksh millions)

Recurrent Expenditure								
Approved Figures			Actual Figures			Absorption Rate (%)		
2007/08	2008/09	2009/10	2007/08	2008/09	2009/10	2007/08	2008/09	2009/10
1,231	1,521	1,922	1,135	1,451	1,806	92.2	95.4	93.9
Development Expenditure								
204	395	426	158	403	402	77.5	102.1	94.4

Source: Ministry of Trade (2011); Authors' computation

The overall approved estimates for the Ministry of Local Government's development expenditure in 2009/10 were Ksh 4.5 billion. However, the actual expenditure in that year was Ksh 1.9 billion. This means that more than a half of the approved estimates for development were not utilized. The under-utilization of funds allocated to the Ministry of Local Government might have contributed to disbursement of inadequate funds for construction of these markets. However, it has been acknowledged by the government that the Ministry of Local Government has been grossly underfunded.

Ministry of Labour: Micro and Small Enterprises (MSEs)

The Micro and Small Enterprises Programme (MSEP) is aimed at creating employment opportunities as a means of reducing poverty. The programme is anchored on Sessional Paper No. 2 of 2005 on the Development of Micro and Small Enterprises, Vision 2030 and the Ministry of Labour Strategic Plan 2008-2012. The Ministry of Labour aims to enhance the performance and competitiveness of the MSEs and the Jua Kali Sector as outlined in the Ministry's Strategic Plan 2008-2012. It is expected that effective MSEs will create productive and sustainable employment opportunities, promote economic growth and reduce poverty.

There was a modest increase of allocation of resources to the Ministry of Labour for recurrent expenditure from Ksh 968.8 million in 2007/08 to Ksh 1.19 billion in 2009/10. The actual expenditure was Ksh 932.57 million for 2007/08, Ksh 961.62 million for 2008/09 and Ksh 1,132.3 million for 2009/10. The absorption rates were 96.3, 96.2 and 94.6 per cent in 2007/08, 2008/09 and 2009/10, respectively.

Table 7.2: Analysis of recurrent expenditure for the Ministry of Labour (Ksh millions)

Approved Estimates			Actual Expenditures		
2007/8	2008/9	2009/10	2007/8	2008/09	2009/10
968.88	999.55	1197.32	932.57	961.62	1132.38

Source: Ministry of Labour (2011)

The Micro and Small Enterprise Programme was allocated Ksh 77.3 million in 2007/08, Ksh 74.8 million in 2008/09 and Ksh 75 million in 2009/10 for recurrent expenditure. The actual expenditure for MSEP was Ksh 81.4 million in 2007/08, Ksh 75.2 million in 2008/09 and Ksh 76.8 million in 2009/10. Actual expenditure for MSEs was slightly higher than the funds allocated. The absorption rates for 2007/08, 2008/09 and 2009/10 were 105.3 per cent, 100.3 per cent and 102.4 per cent, respectively.

Table 7.3:Analysis of recurrent expenditure for MSEs (Ksh millions)

Approved Estimates			Actual Expenditures		
2007/08	2008/08	2009/10	2007/08	2008/08	2009/10
77.33	74.86	75.05	81.45	75.25	76.84

Source: Ministry of Labour (2011)

The Ministry of Labour was allocated Ksh 414.3 million, Ksh 399.71 million and Ksh 479.59 million for 2007/08, 2008/09 and 2009/10, respectively, for development expenditure. The actual expenditure for the period under review was Ksh 347.78 million, Ksh 309.39 million and Ksh 266.32 million, respectively. The absorption rates were 83.9, 77.4 and 55.5 per cent for 2007/08, 2008/09 and 2009/10, respectively.

Table 7.4:Analysis of development expenditure for the Ministry of Labour (Ksh millions)

Approved Estimates			Actual Expenditure		
2007/08	2008/09	2009/10	2007/08	2008/09	2009/10
414.3	399.71	479.59	347.78	309.39	266.32

Source: Ministry of Labour (2011)

Table 7.5: Analysis of development expenditure for MSEs in Kenya (Ksh millions)

Approved Estimates			Actual Expenditure		
2007/08	2008/09	2009/10	2007/08	2008/09	2009/10
107.51	73.55	106.10	101.87	73.16	95.30

Source: Ministry of Labour (2011)

The Micro and Small Enterprises Programme was allocated Ksh 107.51 million, Ksh 73.55 million and Ksh 106.1 million for 2007/08, 2008/09 and 2009/10, respectively. During this period, the actual expenditure was Ksh 101.87 million, Ksh 73.16 million and Ksh 95.30 million. The absorption rates were 94.8, 99.5 and 89.8 per cent for 2007/08, 2008/09 and 2009/10, respectively.

7.6 Programme Implementation and Completion

7.6.1 Provision of Credit to Small-scale Traders under the Joint Loans Board

This is a revolving fund loan scheme run and managed by trade officers in trade offices spread throughout the country. The scheme is meant to enable small-scale traders to access affordable credit to expand their businesses. Currently, there are 47 trade offices in the country and 8 provincial trade offices managed by the Department of Internal Trade. The department had targeted to open five trade offices in 2009/10 and they were able to open all of them, representing a 100 per cent success. There are plans to open four new trade offices during 2010/11. The ministry has also completed profiling of business producer groups in the country to link them to the supply chain as required under Vision 2030.

7.6.2 Construction of Wholesale and Retail Markets

During the period 2007-2010, the Ministry of Local Government planned to carry out feasibility studies for 10 wholesale market hubs and was to construct 10 wholesale markets, 43 retail markets, four hawker markets and 210 economic stimulus markets. A little progress was made during the review period, as only three feasibility studies were done for the wholesale market hubs. In addition, construction of five wholesale markets and 210 economic stimulus markets were commenced while construction of 14 retail markets and one hawker market was accomplished in various parts of the country. It was observed that inadequate funds slowed down the intended output (MTEF Sector Report, 2011). For instance, whereas the ministry projected estimates for markets development was Ksh 8 billion, it was allocated only Ksh 2 billion.

Table 7.6: Market development by the Ministry of Local Government

Intended Output	Output Achieved	Remarks
Carry out feasibility studies for 10 wholesale market hubs	3 feasibility studies done	Inadequate funds
Construction of 10 wholesale markets	Construction of five (5) commenced	Inadequate funds
Construction of 43 retail markets	14 completed	Inadequate funds
Construction of 4 hawkers markets	1 completed and 1 under construction	Inadequate funds
Construction of 210 economic stimulus markets	Construction of 210 ec. stim. markets commenced	Validation of CDF tender award

Source: Ministry of Local Government (2011)

In the Medium Term Expenditure Framework (MTEF) period 2011/12-2013/14, the Ministry of Local Government plans to construct 6 wholesale hubs, 12 wholesale markets, 210 livestock markets and 2,000 modern kiosks in 10 major towns. Resource requirements for market development are estimated at Ksh 2.8 billion (2010/11), Ksh 8 billion (2011/12), Ksh 8.5 billion (2012/13) and Ksh 9 billion (2013/14). While the Ministry of Local Government budgeted for Ksh 8 billion for markets development in 2010/11, the Treasury allocated only Ksh 2 billion for the sub-sector. This is likely to impede development of markets.

Table 7.7: Resource requirements for market development (Ksh millions)

Estimates	Estimates	Projected Estimates	
2010/11	2011/12	2012/13	2013/14
2,810	8,000	8,500	9,000

Source: Ministry of Local Government (2011)

7.6.3 Training and Capacity Building of Business Persons

Through the Kenya Institute of Business Training (KIBT), the sub-sector conducted entrepreneurial and management training of SMEs operators.

Table 7.8:Entrepreneurial and management skills performance indicators

Performance Indicators	2007/08	2008/09	2009/10
No. of SMEs operators trained	1,206	2,107	1,837
No. of SMEs counselled	2,697	3,782	5,984
No. of past trainees followed-up	308	278	1,324

Source: Ministry of Trade (2011)

In addition, trade exhibitions were organized at the Busia border post to sensitize MSMEs on available goods for cross-border trade. Under the programme of promoting women in business and investment, some 300 women operating MSMEs were trained on entrepreneurship skills. Eight district business solution centres were established in Murang'a, Siaya, Bungoma, Kitale, Nakuru, Eldoret, Kisumu and Bondo.

7.6.4 Development of Retail and Wholesale Hubs

No retail and wholesale hubs have actually been established under this programme so far, but a steering committee that comprises members from both the public and private sector has been set up. An indicative concept paper for the wholesale and retail hubs was developed for use by the steering committee. In addition, the sub-sector requested the Ministries of Land and Local Government to provide suitable land for construction of the wholesale and retail hubs/markets in the identified areas.

7.6.5 Establishment of Producer Business Groups

The sub-sector carried out a situation analysis of the Producer Business Groups (PBGs) in Central and Eastern provinces. The needs of one hundred (100) PBGs were identified with a view to addressing the problem of a fragmented supply chain in the wholesale and retail sub-sector.

7.6.6 Assistance to Micro and Small Enterprises Programme (ASMEP)

The ASMEP was commissioned by the European Union (EU) in October 2007, to be implemented over a period of five years until 2012 and another two-year closure phase until 2014. It aims at supporting the development of Micro and Small Enterprises (MSEs) in Kenya. The programme has three components for intervention: Institutional and Capacity Building of Private Sector Organizations, Private-sector related Non-Governmental Organizations (NGOs) and Micro Finance Institutions (MFIs); Information dissemination through support to Business Information Centres (BICs) targeted at MSEs; and Business Development Services through support to Agro-Processing technologies and value addition with particular reference to horticulture and fisheries sectors. According to the 2010/2011 Medium Term Review, the programme is 70 per cent complete.

7.6.7 KEPLOTRADE II

This was a successor to KEPLOTRADE I, and is aimed at facilitating timely establishment and effective early implementation of Economic Partnership Agreements (EPAs) between Kenya and the EU in the context of the East African Community (EAC) and the Common Market for

Table 7.9: Staff establishment in the Ministry of Trade in 2009

Department / Unit	Professional Staff			Support Staff		
	Current Establishment	Proposed Establishment	Variation (%)	Current Establishment	Proposed Establishment	Variation (%)
General Administration	47	40	117.5	104	73	142.5
Human Resource	14	17	82.4	51	37	137.8
Internal Trade	148	304	48.7	297	573	51.8
External Trade	82	171	47.9	42	47	89.4
CPPMU	23	23	100.0	25	25	100.0
Weights and Measures	92	230	40.0	270	357	75.6
Business Premises Rent Tribunal	1	5	20.0	21	39	53.8
Kenya Institute of Business Training	42	203	20.1	37	378	9.8
Accounts Division	13	17	76.5	52	37	140.5
	462	1,010	45.7	899	1,577	57.0

Source: Ministry of Trade Strategic Plan (2008-2012)

East and Southern Africa (COMESA) regional integration agenda. The value of the programme is €4.25 million under the EU's Stabilization of Export Earnings (STABEX) fund, for a three-year period effective from 1st July 2007 until 2010. The programme has since been completed.

7.7 Administrative Capacity

Generally, there are significant variations in current and proposed staff establishment in the Ministry of Trade, according to the Strategic Plan 2008-2012. For instance, the current staff establishment for professional and support staff stands at 45.7 per cent and 57 per cent, respectively. Apparently, there are significant shortages of staff in the categories directly involved in the promotion of domestic trade. Notable among these are Departments of Internal Trade (48.7%), Weights and Measures (40%), Business Premises Rent Tribunal (20%) and Kenya Institute of Business Training (20.1%) as shown in Table 7.9. Ironically, there is over-establishment in the General Administration in both professional and support staff, which stands at 117.5 per cent and 142.5 per cent, respectively.

7.8 Comparative Analysis and Best Practices in Wholesale and Retail

7.8.1 Global Overview

Internationalization of retailing has emerged in the recent past as modern retailers from developed countries turn to new markets. Previous studies show that retail sales growth of companies that have ventured into foreign markets has been faster than those that have confined themselves to home markets (Mathew *et al.*, 2008). For instance, the five South African retailers in the top 250 retailers in the world conducted business in an average of 9 countries, particularly in the African continent in 2005-2006. Unlike the developed countries, unorganized retail and wholesale trade dominates business in developing countries as evident in Table 7.10. For instance, the share of organized retail varies widely from just 1 per cent in Pakistan and 4 per cent in India to 36 per cent in Brazil and 55 per cent in Malaysia.

Table 7.10: Share of organized retail in selected countries, 2006

Country	Total Retail Sales US$	Share of Organized Retail (%)
USA	2,983	85
Japan	1,182	66
China	785	20
United Kingdom	475	80
Brazil	284	36
India	322	4
Pakistan	67	1
Thailand	68	20
Malaysia	34	55

Source: Mathew *et al*. (2008)

The global retail sector continued to endure consequences of recession in 2009, and more than one-third of the top 250 global retailers suffered declining sales. Overall, US retailers maintained the lead as they accounted for the biggest share of retailers and retail sales, i.e. 33.6 per cent and 42.1 per cent, respectively. Wal-Mart from the US has maintained the market lead among the top 250 retailers (Table 7.11). From the African continent, only South African firms made it to the list of top global retail firms; that is, 7 retail firms led by Shoprite Holdings made it to the list in 2009. The extent to which the largest retailers have expanded can be seen by the extent and coverage of their operations beyond their countries of origin.

According to Deloitte (2010), world retailing looks more promising in emerging markets, especially those with strong growth prospects and good demographics. Global retailers are increasingly looking at Africa, which failed to have significant growth for much of the last half century, but is now experiencing good growth as a result of rising commodity prices and better governance. This also follows the argument that strong economic growth that enhances consumer spending triggers investments in modern retailing.

Apparently, regulatory restrictions are more stringent in developed than in developing countries. This is due to the fact that in developed countries, governments have become more sensitive to the demands of small traditional retailers and non-mobile consumers. As noted by Reardon and Hopkins (2006), there are four types of policy regulations that can be seen in

Table 7.11: Top 250 global retailers, 2009

Rank	Company	Country of Origin	Retail Sales 2009 (US$ million)	Operational Format	No. of Countries in Operation
1	Wal-Mart	US	405,046	Hypermarket/supercentre/superstores	16
2	Carrefour S.A.	France	119,887	Hypermarket/supercentre/superstores	36
3	Metro AG	Germany	90,850	Cash and Carry/Warehouse	33
4	Tesco Pic	UK	90,435	Hypermarket/supercentre/superstores	13
95	Shoprite Holdings	South Africa	8,825	Supermarket	16
130	Pick n pay	South Africa	6,810	Supermarket	6
138	Massmart	South Africa	6,274	Cash and Carry/Warehouse	13
206	MigrosTicaret	Turkey	3,691	Supermarket	5
211	Spar	The Netherlands	3,627	Supermarket	3
245	Metcash	Australia	3,105	Cash and Carry/Warehouse	5
248	Woolworths	South Africa	3,093	Department stores	18
NA	Nakumatt	Kenya		Supermarket	3
NA	Uchumi	Kenya		Supermarket	2
NA	Tuskys	Kenya		Supermarket	1

Source: Deloitte (2010), Government of Kenya (2011)

countries that have experienced advanced retail expansion. They are:

- Competition policy that limits concentration and collusion.
- Zoning and hours regulations to limit the diffusion, market penetration and convenience of organized retail.
- Pricing regulations that prevent modern retail companies from pricing below cost and prompt payment regulations to secure speedy payment to suppliers.
- Policies to strengthen traditional retailers and suppliers through technology and practice upgrading, enhancing organizational capacity and financial access.

These regulations were put in place in different countries, basically with a view to balance the conflict of interests between modern retail, on one hand, and the traditional retailers and suppliers to the modern retail, on the other. Southeast Asia (Malaysia, Indonesia and Thailand) imposed restrictions on the growth of large retail companies particularly the transitional companies, in contrast to the fairly liberal approach to the retail sector, followed until the late 1990s.

7.8.2 Country Experiences

South Africa

South Africa offers the full spectrum of retail outlets: neighbourhood convenience stores; small general dealers; specialty stores handling a single product line (such as clothing, electronics, or furniture); exclusive boutiques; chain stores (groceries, clothing, toiletries, household goods); department stores; cash and carry wholesale-retail outlets; and co-operative stores serving rural areas. About 90 per cent of the consumer trade inventories of these stores are domestically sourced. A major phenomenon in South Africa has been the evolution of supermarkets or hypermarkets, which sell large quantities of almost all consumer goods on a self-serve basis. The hypermarkets, located in sub-urban shopping centres, have disrupted the traditional distribution chain by purchasing directly from manufacturers and bypassing the wholesaler, with low margins, achieving high turnover and thereby placing price pressure on all competing outlets.

Singapore

Singapore's retail sector has evolved through time, adjusting and adapting to forces of urban change. Before the 1960s, retail facilities were concentrated in the central business district. In the 1960s, large-scale sub-urbanization of retail trade was triggered by the planned housing and development board centres built around housing estates. From the late 1970s, urban renewal and market forces led to the rapid development of planned integrated multi-storeyed shopping centres, hotels, cinemas and other entertainment facilities. Planned modern retail and entertainment facilities spread to high-income residential areas.

The retail market is highly cosmopolitan and sophisticated as reflected by the wide variety of international brands and retailers. Retail sales area totals 3.2 million square metrs, with retail space in prime shopping districts. The distribution channels for food and beverages retailing are hypermarkets, supermarkets, convenience stores, mini-mart stores and market stores. On the other hand, non-food retail channels are mainly department and specialty stores. The latter prefer a more exclusive and cosy shopping atmosphere as compared to department stores.

Singapore's retail regulatory regime is both direct and indirect in nature. For instance, commercial and retail space is directly regulated by the Urban Redevelopment Authority (URA). URA enforces property and real estate regulations, and facilitates a land sale programme for private sector development.

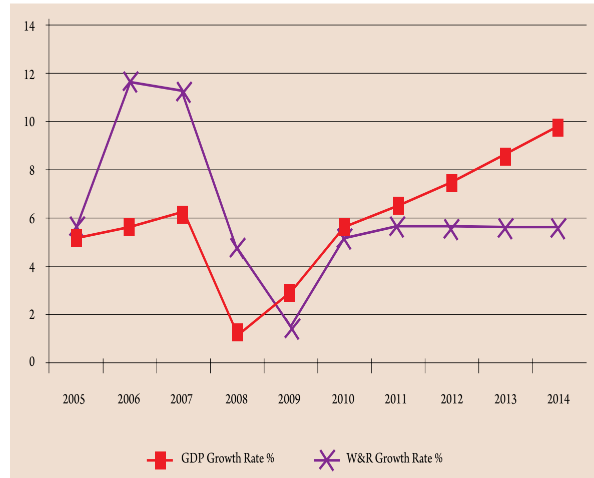
There also exists the Competition Act 2004 to safeguard against anti-competitive activities. In addition, there are tax incentives and investment allowances for new businesses, including retail stores, all of which directly affect retail activities. On the other hand, a key indirect regulatory measure is the "planned shopping centre model". This model was adopted to accommodate the changing pattern of retail activities. The planned shopping centre is designed to accommodate many stores within one building, thereby providing economies of scale for both retailers and shoppers. While retailers hope to benefit from agglomeration or clustering effects, consumers can save on time by shopping from a single destination. This form of retailing has considerable influence on entrepreneurial and consumer behaviour.

Rapid economic growth, rising populations and incomes, greater mobility, influx of tourists and new merchandizing techniques (self-services and check-out facilities) have all contributed to changing the retail scene in the country. These factors have fostered growth in retail facilities, promoted construction of new forms of retail outlets, caused shifts in their location, and changes in the retail structure. Many of Singapore's earliest ultra-modern, multi-storeyed shopping centres were sited in the central area. Over time, sub-urban shopping centres have sprung up, reflecting the efforts by public and private bodies to meet the increasing demand for goods and services.

7.9 Medium Term Prospects

Going forward, the outlook for wholesale and retail trade is promising taking into consideration the positive prospects for economic growth, the global economic recovery, opportunities in the expanded regional markets especially in the EAC and COMESA, a new constitutional dispensation and improved tourist activity.

Figure 7.3: Medium term projections for wholesale and retail trade



Source: KIPPRA Projections (2011) using KTMM

The wholesale and retail trade sub-sector is projected to grow at a rate of 5.4 per cent in 2010 and to sustained growth rate of 5.6 per cent between 2011 and 2014. This growth (pegged on the upswing of major business activities in agricultural products, manufactures, ICT products, motor vehicles and associated spare parts and repairs, construction, chemicals, petroleum and petroleum products) is rising and expected to support household retailing for final consumption. The phenomenal growth of the ICT sector, especially the rising subscription and penetration of mobile telephony and internet services, is likely to spur growth of the retail of ICT-related products and consumer goods in general. Sustained competition in the sector is expected to drive down average tariffs and further increase use and coverage. Besides, the rapid growth of urbanization in Kenya and the associated rural-urban migration is expected to fuel demand for consumer goods and services in the medium to long term.

Further, the envisioned devolved system of government portrays basic features of "a free trade regime" in which county governments will, by and large, be "open economies" allowing relatively free mobility of goods, persons and capital within and across their jurisdictions. This will particularly be the case for the counties that will adopt friendly trade policies, for example, by offering incentives to mobile

capital, subsidies to certain industries, professionals, sports teams, and infrastructure development. It is also expected to address governance issues, improve the business environment and enhance competitiveness among county governments.

Finally, the domestic market of about 40 million people is becoming closely integrated with the EAC (regional) following the coming into force of the EAC Common Market Protocol and steady progress towards a Monetary Union. The EAC integration boasts of a single market with an estimated population of 130 million persons and GDP of US$ 72 billion. The EAC common market regime strives to open new opportunities for business in the region by making free movement of labour, capital, services and the right of establishment a reality in the EAC region within the next five years. In the context of a single market, the free flow of economic factors envisions greater prosperity of the states and their citizens. Thus, there are prospects for expanding exports for processed and semi-processed products, including food, beverages, cement and refined petroleum through locally-incorporated retail outlets.

7.10 Policy Recommendations

Wholesale and retail trade plays a significant role in Kenya's development discourse and more importantly in the achievement of Vision 2030 goals. In the context of the devolved governance under the new constitutional dispensation, institutional restructuring is paramount.

In this regard, there is need to fast-track on-going regulatory reforms relating to streamlining registration and licensing as well as other factors affecting operations of wholesale and retail trade. For instance, licensing is currently under the Ministry of Local Government, whose main focus is revenue collection. The Ministry of Trade is not actively involved in this process. The Ministry of Trade, through the Department of Domestic Trade, needs to play a more strategic role in streamlining operations of wholesale and retail trade.

The construction of wholesale and retail markets as envisaged in Vision 2030 is critical in enhancing the development of both wholesale and retail trade. Markets development has the potential of facilitating trade, commerce and rural enterprise development. However, there is need to streamline the lead agencies involved in development of markets. Currently, there is fragmentation of the roles played by the Ministry of Trade and the Ministry of Local Government in terms of the development of markets, yet these markets are supposed to promote domestic trade.

Finally, there is need for Kenya to push for the reduction of non-tariff barriers in both the COMESA and EAC regions so that Kenyan wholesale and retail outlets can increase their operations in the region and take advantage of the expanded market.

Chapter 8

Micro and Small Enterprises

8.1 Introduction

The Micro and Small Enterprise (MSE) sector is one of the most dynamic and fastest growing sectors of the Kenyan economy. Although the sector is prolific in terms of job creation, there are concerns that employment in the sector is not decent. The sector employs 9 out of every 10 people employed in Kenya. Every 9 out of every 10 new jobs are created in the informal sector. Given the wide coverage and magnitude of the sector, it has been identified in Kenya's main policy frameworks as a key agent in stimulating economic growth, enhancing equitable income distribution, allowing more productive and efficient use of scarce resources, enhancing regional dispersion of industries and developing a vibrant private sector. In addition, MSEs create employment at low levels of investment per job, absorb surplus labour in the economy, use mainly local resources, promote local invention and innovation, and provide skills training at a low cost to society. However, for this to happen, the institutional impediments that have kept most entrepreneurs in the informal sector will have to be identified and removed. Institutional impediments can come from the state, the market and the private sector.

In Kenya, MSEs are defined more generally as those enterprises, whether formal or informal, that employ 1-50 people. Micro enterprises are those that employ 10 or fewer workers, while small enterprises employ 11-50 workers and can either operate formally or informally. For purposes of this chapter, the terms MSEs, Jua Kali and informal sector are used interchangeably although in actual usage, they are slightly different.

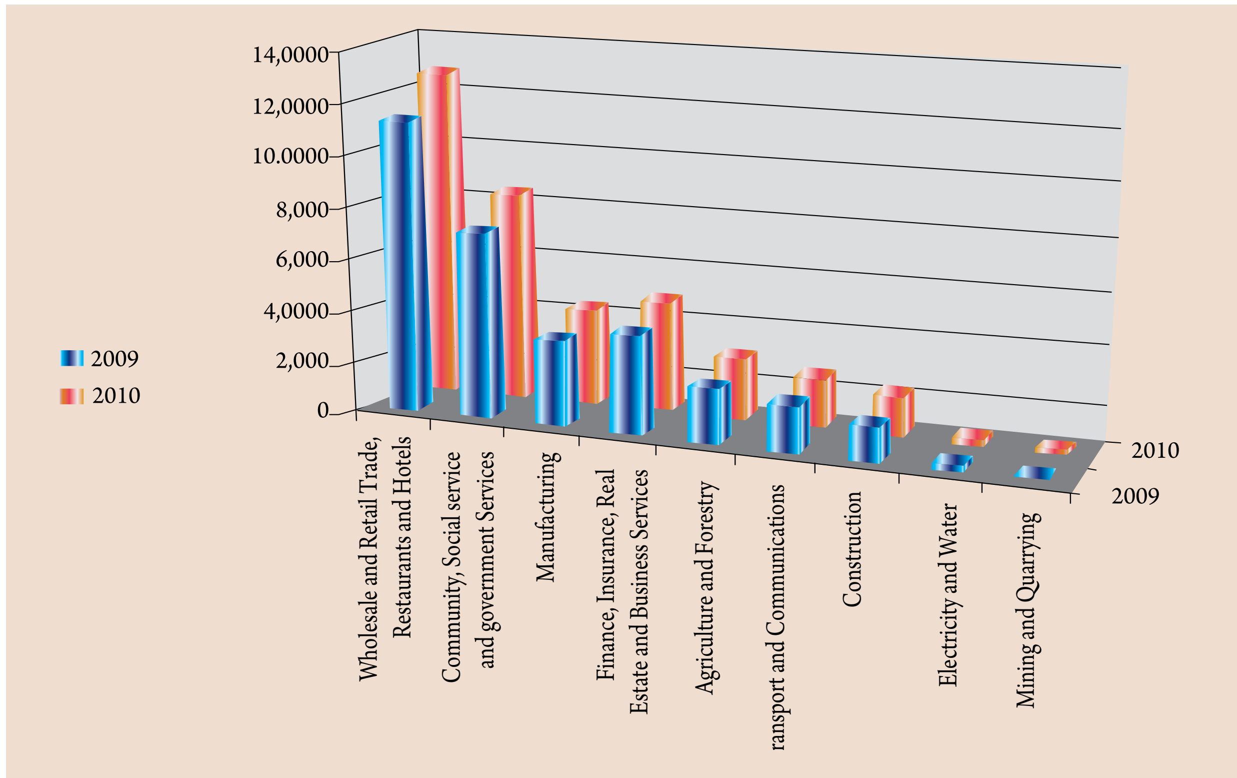
8.2 Recent Performance[1]

Number of Establishments

The MSE sector accounted for 74.7 per cent of all formal establishments in Kenya. The number of formal MSEs in the country increased by 11.88 per cent from 31,430 in 2009 to 35,165 in 2010. Interestingly, large enterprises also experienced similar growth (11.98%) over the same period. Majority of MSEs operate in the service sector as illustrated in Figure 8.1, which reveals that 36 per cent of MSEs are involved in wholesale and retail trade, restaurant and hotels; and 23 per cent in community, social and government services. As is the case in previous years, only 10.6 per cent of MSEs participate in manufacturing, a sector identified in Kenya Vision 2030 as one of the drivers of economic growth.

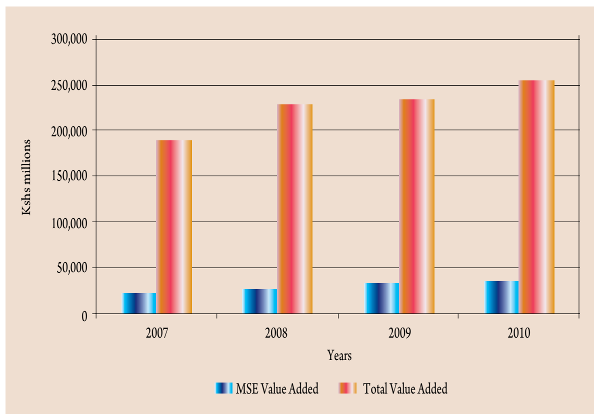
Despite the fact that the number of formal MSEs involved in manufacturing does not change much, the contribution of total value added in manufacturing has been increasing over the years, from 12 per cent between 2004 and 2008 to 13.8 per cent and 13.7 per cent in 2009 and 2010, respectively.

Figure 8.1: Distribution of MSEs by industry



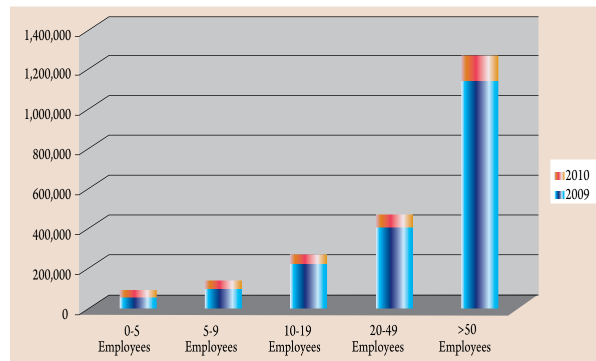
Source: Government of Kenya (2010a ; 2011b)

Figure 8.2: Manufacturing value added



Source: Government of Kenya (2010a ; 2011b)

Figure 8.3: Employment figures in formal micro and small enterprises



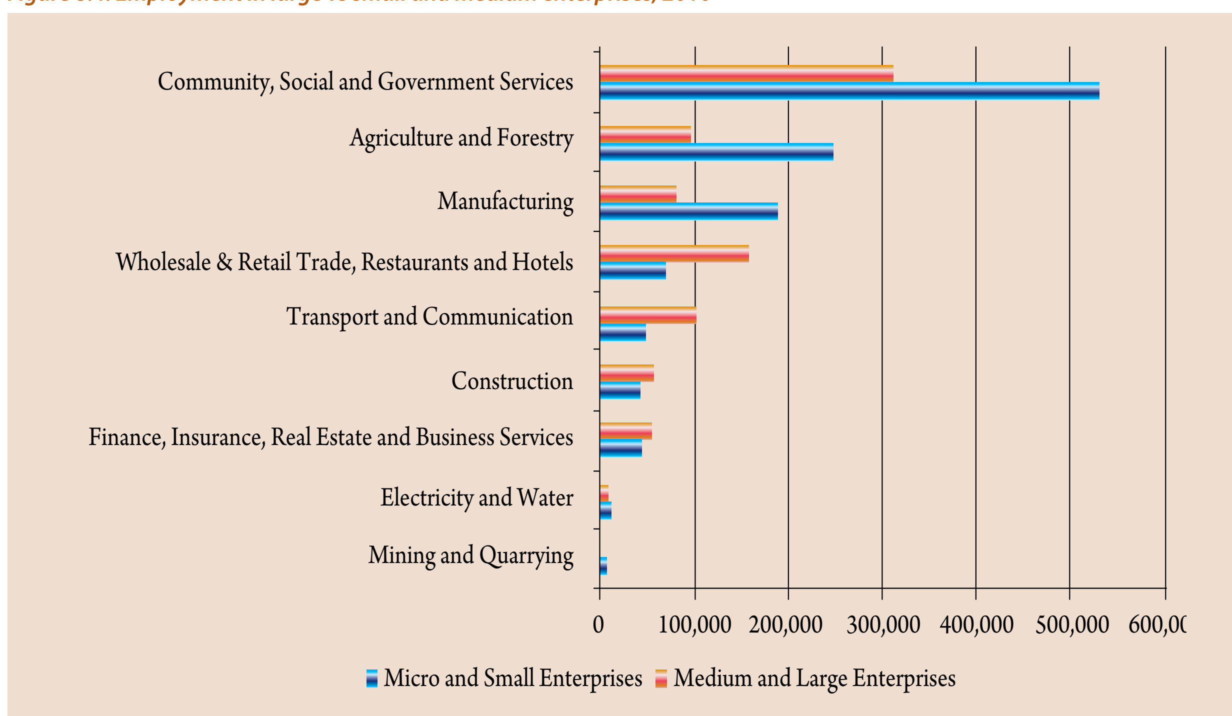
Source: Government of Kenya (2010)

Employment

The formal MSE sector experienced an increase in employment in 2010, but only marginally compared to 2009 as illustrated in Figure 8.3. The sector contributed 42.2 per cent of total formal employment representing a slight decline from 42.6 per cent in 2009.

The MSE sector, however, dominates some sectors such as community, social and government services, agriculture and forestry, manufacturing, electricity, water, and mining and quarrying as illustrated in Figure 8.4.

Figure 8.4: Employment in large vs small and medium enterprises, 2010



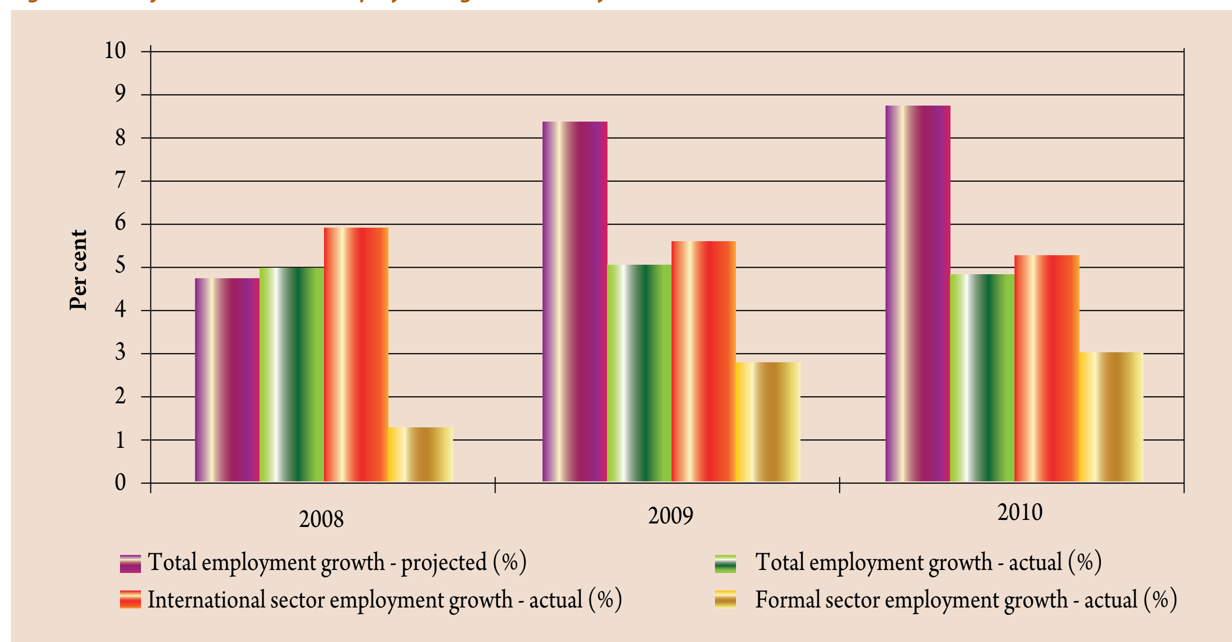
Source: Government of Kenya (2011b)

8.3 Performance Gap and Medium Term Prospects

The most serious challenge facing Kenya today is the creation of productive employment opportunities. The MSE sector holds the greatest potential in bridging the job deficit in the country. However, according to statistics, majority of MSEs in Kenya operate informally.[2] Available statistics show that between 2007 and 2010, the informal sector contributed 70 per cent to 80 per cent of total employment. During the same period, out of every 10 new jobs created, 9 jobs were created in the informal sector. Similarly, employment growth in the informal sector continued to outpace formal sector employment growth. Average annual employment growth in the informal sector was 5.6 per cent compared against 2.4 per cent for the formal sector. These statistics suggest that job creation in Kenya is heavily driven by expansion in the informal sector. This trend is not sustainable and requires a structural shift that will lead to rapid formalization of the informal sector.

According to the Medium Term Plan (MTP) 2008-2012, the Kenyan economy was expected to create 425,000 new jobs in 2008, 759,000 in 2009 and 787,000 in 2010. Similarly, employment growth was projected at 4.7 per cent in 2008, 8.4 per cent in 2009 and 8.7 per cent in 2010. Actual employment numbers show that the MTP target of 425,000 was surpassed by 41,000 jobs in 2008. However, the economy failed to meet the MTP targets in 2009 and 2010. New jobs created in 2009 and 2010 were 503,000 per year. These shortfalls in job creation in 2009 and 2010 are largely attributed to weak economic growth and the lagged effects of the 2007/08 post-election violence. A comparison of employment growth targets and actual employment reveals that the economy failed to meet the target in 2009 and 2010 when employment growth was 5.1 per cent and 4.8 per cent, respectively. It is important to note that employment growth in the informal sector in 2008, 2009 and 2010 was 5.9, 5.6 and 5.3 per cent, respectively. However, employment growth in the formal sector lagged behind that of the informal sector. Formal sector employment grew

Figure 8.5: Projected and actual employment growth in Kenya



Source: KIPPRA projections based on employment data (Government of Kenya Economic Surveys)

by 1.3, 2.8 and 3 per cent in 2008, 2009 and 2010, respectively.

KIPPRA projections for 2011 and 2012 based on employment data from 1991 to 2010 show that the informal sector will increasingly contribute to job creation in Kenya. In 2012, the informal sector will contribute 82.2 per cent of total employment.[3] The number of new jobs will fall from 503,000 in 2010 to 457,000 in 2012. Out of the 457,000 jobs, the informal sector will create 427,000 jobs or 93.4 per cent of new jobs created. Overall, there are no indications that the economy will meet the projected 823,000 jobs in 2011 and 904,000 jobs in 2012.

8.4 MSE Institutions

Post-independence policy as stipulated in Sessional Paper No. 1 of 1965 on African Socialism and its Application to Planning in Kenya was geared at encouraging the growth and development of indigenous but formal enterprises with the overall aim of spurring industrial development. This policy encouraged African entrepreneurs, including civil servants, to establish local enterprises. The policy established specialized parastatals to cater for financial and business development services. These parastatals included the Development Finance Company of Kenya (DFCK), the Kenya Industrial Estates (KIE) and the Industrial Development Bank (IDB). The legislation in place during this period, including the Trade Licensing Act and Land Control Act was also aimed at indigenizing the economy.

The informal sector received official recognition in Kenya in 1972 following an ILO employment mission report.[4] Though the recognition of the informal sector started in 1972, the institutional framework of the sector lagged behind. Additionally, MSE policy coordination lacked a focal point and it was not clear which government ministry was in charge of MSE sector activities. In 1992, the Sessional Paper No. 2 of 1992 established the Directorate of Applied Technology (DAT) as the key institution dealing with MSEs under the then Ministry of Research, Technical Training and Applied Technology (MRTTAT). During this time, the Ministry of Planning and National Development was also running parallel programmes for the MSE sector. The Deregulation Section, for instance, commenced work in May 1996 with the overall

mandate of reviewing and identifying legal and regulatory impediments to the growth of MSEs.

In 1998, the Directorate of Applied Technology was moved to the Office of the President. In the following year, the Presidential Circular No. 1 of 1999 on "Organization of the Government of the Republic of Kenya" directed that all activities and programmes that deal with MSEs and informal sector be moved to the then newly-created Ministry of Labour and Human Resource Development. Thus, the ministry was established by merging the then Ministry of Labour and the Ministry of Manpower and Development. In 2000, the Division of Small Scale and Jua Kali Enterprises and the Directorate of Applied Technology were merged to form the Department of Micro and Small Enterprise Development (DMSED). The Presidential Circular No. 3 of July 2003 reiterated that the Ministry of Labour and Human Resource Development was responsible for informal, micro and small scale enterprise development. The role of DMSED was strengthened following the Sessional Paper No. 2 of 2005 to include coordinating and monitoring the roles and activities of the various stakeholders.

Over the years, however, different ministries have been responsible for different MSE-related activities and roles. The Presidential Circular No. 1 of 2007 on the "Organization of the Government of the Republic of Kenya", for example, specified the responsibilities of the different ministries. According to the Circular, the Ministry of Trade and Industry was responsible for the development of micro and small enterprises, while the promotion of self-employment in micro and small enterprises is the responsibility of the Ministry of Labour and Human Resource Development. A Presidential Circular No. 1 of 2008 assigned the role of developing micro and small businesses to the Office of the Deputy Prime Minister and Ministry of Trade, while the role of supporting the development of micro and small industries and the Micro Enterprise Support Project (MESP) fell under the Ministry of Industrialization.

As illustrated above, the responsibility for the sector has moved from one government ministry to another and from one department to another over time. Apart from the changes in responsibility of the MSE sector from one government agency to another, there are certain functions of the MSE sector that have been scattered across several ministries. For instance, the Ministry of Trade and Industry has been responsible for the Kenya Industrial Estates (KIE) and Industrial and Commercial Development Corporation (ICDC) since their establishment in the 1950-60s to 2007. In 2008, the Ministry was split into the Ministry of Industrialization, which is now responsible for KIE and the Ministry of Trade under which ICDC now falls. Both KIE and ICDC were established to support and promote small indigenous enterprises.

Some reforms in the financing of SMEs include the establishment of the Youth Enterprise Development Fund and the Women Enterprise Fund. The Youth Enterprise Development Fund was gazetted in 2006 and was later transformed into a state corporation in May 2007 under the Ministry of Youth Affairs and Sports. The Youth Enterprise Development Fund aims to encourage the youth to engage in entrepreneurial activities. Shortly afterwards, the Women Enterprise Development Fund was established under the Ministry of Gender, Children and Social Development with the aim of providing affordable credit to support women entrepreneurs. During the 2010/11 Budget Speech, the Minister for Finance created a Ksh 3 million SME's Revolving Fund, a credit facility for small and medium enterprises (SMEs). This fund received a further Ksh 1 million following the 2011/12 Budget Speech. However, the utilization of this fund has been slow due to disagreements between MSEs and the Ministry of Finance regarding the conditions set for accessing the funds.

Several policy papers have, over the years, expressed the need to improve the coordination, implementation and monitoring of MSE policies and activities in response to this problem. The

most relevant policy paper for MSEs, for instance the Sessional Paper No. 2 of 2005 proposed the establishment of a National Council for Small Enterprises (NCSE) to monitor policy and programme implementation and advise the government on the appropriate action to be taken and assist with the mobilization of resources. The proposed Council will comprise of key MSE stakeholders and will complement activities of the National Economic and Social Council (NESC). The Sessional Paper also prescribed the formulation and enactment of the MSE Act, which would support the growth and development of the sector and also formalize the National Council for Small Enterprises. In October 2011, a Micro and Small Enterprise Bill was introduced in Parliament as a private member's Bill. It went through the first reading in November 2011. The Bill provides for a MSE Authority with roles similar to the proposed NCSE. The MSE sector has not previously had any law regulating and promoting it.

8.5 Recent Institutional Reforms

Vision 2030 addresses other MSE institutions in different sectors such as manufacturing, wholesale and retail trade, and agriculture, thus introducing a number of reforms, some of them described below.

The Public Procurement and Disposal (Preference and Reservations) Regulations, 2011 (Legal Notice 58): These regulations were gazetted in June 2011. They are regulations for public procurement from micro and small enterprises, amongst other groups. According to the regulations, MSEs wishing to participate in public procurement are to register with the Ministry of Finance. Such enterprises will then be entitled to preference and reservation scheme benefits for a period of five years, which can be renewed once. The regulations also provide procurement officers with a working definition of micro and small enterprises.[5]

SME Revolving Fund for Capacity Building: In line with Vision 2030, the government allocated Ksh 800,000 to an SME Revolving Fund for Capacity Building. Additionally, a needs assessment survey and capacity building was carried out for youth and women entrepreneurs.

Construction of Wholesale and Retail Markets: At the end of 2010, construction work had commenced on 5 wholesale markets, 14 retail markets and1 hawkers' market. This, however, represents only 35 per cent of the intended output. One of the flagship projects identified in Vision 2030 was the establishment of wholesale or retail hubs. So far, none has been developed. However, a steering committee was formed to coordinate the process.

Business Process Outsourcing (BPO): As at 2010, there were 30 licensed BPOs in Kenya. The government has provided support in form of bandwidth subsidy provided by the ICT Board, where 10 BPO companies benefitted before the end of the programme in February 2010. The government has also made significant investments in internet aimed at improving internet access and costs. The government is also developing a technolopolis that would house a BPO Park.

Special Economic Zones and SME Parks: According to Vision 2030 Medium Term Plan, one of the flagship projects for 2008-2012 is the Special Economic Cluster (SEC) in Mombasa and Kisumu. Towards this end, the government has developed a Memorandum of Understanding (MoU) with Singapore for the establishment of the Mombasa SEZ and SME Parks. Additionally, a Special Economic Zone policy and Bill have been drafted. The SEC and the five planned SME Parks are, however, yet to be started. It is hoped that progress will be made once the MoU is implemented and once the SEZ policy and Bill are finalized.

The government has prioritized the development of Constituency Industrial Development Centres. Under the Economic Stimulus Programme (ESP), each of the 210 constituencies received Ksh 2.5 million. Construction of approximately 179 sheds has commenced.

Fish Farming Ponds: Also under ESP, Ksh 1.1 billion was allocated to 140 constituencies countrywide for the construction of 200 fish farming ponds and 28,000 fish farms nationally. This programme is also aimed at creating employment for over 120,000 people and targets micro and small-scale operators. According to the *Progress Report on Fish Farming Enterprise Productivity Programme,*[6] as at January 2011, there were 26,781 fish ponds constructed and another 1,121 under construction or pending. According to the Economic Survey (Government of Kenya, 2011), production from fish farming increased by almost 250 per cent in 2010 compared to 2009.

Institutional Issues in the Sector

A review of the main institutions in the MSE sector above has revealed a number of challenges that the sector still faces. These challenges include:

a. Weak coordination mechanism: Policy coordination of MSE issues is weak – creating confusion, overlaps and duplication of activities and wastage of resources. The current institutional framework has multiple government ministries, departments and agencies that deal with the MSE sector. Responsibility for MSE policies is often dispersed across different ministries. There is no clear focal point, structure or institution for coordinating all MSE issues. However, mechanisms for consultation on MSE policy between the government and the private sector, in policy deliberations, are largely *ad hoc* and limited. Although there are Ministerial Stakeholder Forums (initiated at the behest of KEPSA), these are not properly institutionalized and integrated with other departments and divisions in government ministries.

b. Over-extended informal sector: Kenya's private sector is predominantly informal. This implies that a large proportion of the enterprises operate outside the scope of existing legislation, regulations and policies and, therefore, may not receive the incentives, benefits and protection thereof.

c. Weak business associations: The MSE sector remains uncoordinated, and the capacity of MSE associations to lobby for the implementation of MSE policies remains weak. Whereas MSE associations are expected to play a pivotal role in organizing MSEs and enhancing their participation in policy formulation, implementation, monitoring and evaluation, the institutional capacities of MSEs fall below the levels required to meet the challenges posed by these expectations. The sector lacks a unified platform for lobbying and policy advocacy. Representation of the sector is characterized by power struggles among association leaders. This fragmentation, weak bargaining power and low policy advocacy capacity has been partly linked to the weak leadership of MSE associations. Most association leaders lack the mandate of their members, since elections are rarely held. The disunity has led to duplication of efforts and the MSE sector lacks a strong voice to influence the country's policy agenda.

d. Mapping the sector: The last national survey on MSEs was conducted in 1999. This implies that the current size, composition and contribution of the MSE sector in Kenya is unknown, thus making planning and programming for the sector difficult.

8.6 Conclusions and Recommendations

Coordination: To improve coordination in the MSE sector, we recommend the enactment of the MSE Bill, which provides for the establishment of an MSE Authority. Similarly, efforts should be made to ensure that laws and regulations addressing the MSE sector are harmonized to ensure proper coordination. The definitions provided in the Public Procurement and Disposal Act (Act No. 3 of 2005),[7] the Income Tax Act (Cap 470),[8] the MSE Bill 2011

and other relevant statutes should, therefore, be uniform.

Formalization of MSEs: One way of ensuring that MSEs formalize is by reducing the costs involved in starting, registering and licensing a business. This can be achieved through introduction of a 'one-stop shop' concept where all statutory procedures regarding registering a business, obtaining licences and registering for taxes are provided within one single location as opposed to multiple different ones as is the case today. In this way, entrepreneurs can access all relevant agencies and obtain the relevant licensing and statutory services from a single location. Similarly, MSEs can be accorded incentives to encourage them to formalize. Such incentives may take the form of tax rebates and access to government procurement of goods and services. In this case, MSEs that register within a specified period of time can access certain types of tenders they qualify for.

Strengthening organization and unification: Strengthening organization and advancing unification will provide the answer to problems of fragmentation and lack of a shared vision. There is need to educate the MSE operators about the need and benefits for a unified MSE sector in an emerging political and economic integration and in a global environment. Following the example of the formation of the Kenya Private Sector Alliance, the entrepreneurs in the MSE sector should, by consensus, form an umbrella association at the national level. This national association should, however, develop from the lower levels including county, constituency and ward structures. Building stronger associations implies that the government and the private sector (through the Kenya Private Sector Alliance) will assist in the reinforcement of association structures at sub-regional and sub-national levels.

MSE National Survey: Since the government is depending on the MSE sector to meet most of the targets set in Vision 2030, including employment, SME parks, Special Economic Zones (SEZs), wholesale and retail hubs, the commercialization of agriculture, etc, conducting a national MSE survey should be prioritized. MSE data needs to be updated. The survey should include modules to capture the size and nature of the informal sector, which have not been included in previous surveys. The results of the survey would assist in policy and strategy formulation and implementation.

ENDNOTES

1. The definition of MSEs used in this section is drawn from KNBS, which provides data for all establishments operating formally, disaggregated by number of employees. The data, however, excludes informal sector enterprises, very small non-agricultural rural establishments, small holdings that are outside 'Scheduled Areas' and, therefore, may not be very representative of MSEs given that majority of MSEs operate informally.
2. The 2007 survey by KIPPRA and Ernst and Young revealed that only 28 per cent of Micro, Small and Medium Enterprises (MSMEs) surveyed had some form of business registration while, according to the 1999 National MSE Baseline Survey Report, only 11.4 per cent of Small and Medium Enterprises (SMEs) had any form of business registration.
3. According to the data in the 2011 Economic Survey, (Government of Kenya, 2011), the informal sector represents 80.56 per cent of total employment.
4. "Employment, Incomes and Equity: A Strategy for Increasing Productive Employment in Kenya" (ILO, 1972).
5. Micro enterprises are those with less than ten employees and annual turnover or investment not exceeding Ksh 500,000, while small enterprises are those with between 11 and 50 employees and annual turnover or investment not exceeding Ksh 5 million.
6. Accessed in May 2011 from http://www.economicstimulus.go.ke
7. Specifically, Public Procurement and Disposal (Preference and Reservations) Regulations, 2011.
8. Specifically for small businesses that do not quality for VAT based on the Income Tax (Turnover Tax) Rules, 2007 and Section 12c of the Income Tax Act (Cap 470).

Chapter 9

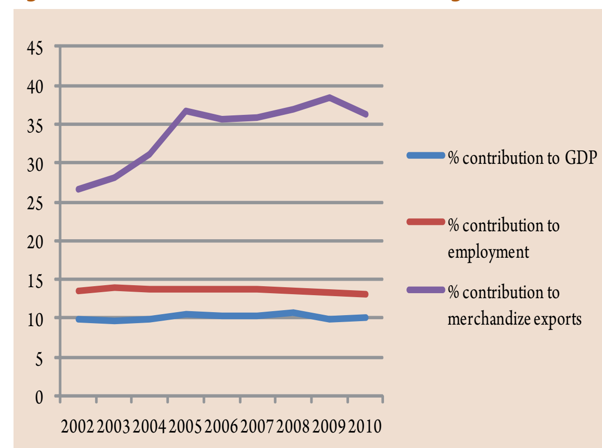
Manufacturing

9.1 Overall Macro Performance

The contribution of the manufacturing sector to the economy has remained at about 10 per cent over the years, contributing 9 and 10.0 per cent in 2009 and 2010, respectively (Figure 9.1). As explained in KIPPRA (2009), the near-stagnant sector contribution to Gross Domestic Product stems from policy setup under which the sector has operated since independence. A poorly implemented import substitution strategy was hampered by limited local demand and operational inefficiency from 1963 to the mid 1980s. The industrial establishments (mainly in food and textile industries) that resulted from import substitution strategy were uncompetitive and unsustainable in the wake of structural adjustment programmes of the 1980s, which led to government divestment from the industry. For instance, the textile industry was the leading sub-sector in manufacturing till the mid-1980s but, thereafter, economic liberalization saw the influx of textile goods and second-hand clothes into the Kenyan market, resulting to the near-collapse of the local textile industry in the early 1990s. The sector further experienced depressed growth in the mid-1990s in the wake of macro mismanagement that gripped the country during the period, which also resulted in spiral inflation that negatively impacted on both demand and supply conditions.

Since 2004, the performance of the manufacturing sector steadily grew until 2007 when negative political shocks, precipitated by the disputed presidential elections, slowed the sector's growth. In the period 2004-2006, the sector grew by 4.5 per cent on average, before reaching a high of 6.5 per cent in 2007, but its growth slowed down to 3.6 per cent in 2008. The onset of the global financial crisis in 2008 further worsened the performance of the sector. The sector was at its lowest ebb in 2009 when it recorded a growth of 1.3 per cent. Manufacturing performance improved in 2010 to record a 4.4 per cent growth (Government of Kenya, 2011b).

Figure 9.1: Performance of the manufacturing sector



Source: Compiled from Government of Kenya (2011b); Government of Kenya (2011a), World Bank (2010a), World Bank (2010b).

The contribution of the manufacturing sector to overall merchandise exports has been increasing since 2003, though some marginal decline was experienced in 2010. Manufacturing exports contributed 36.2 per cent of total merchandise exports in 2010 compared to 38.4 per cent in 2009. In employment creation, the manufacturing industry has not been robust. The employment growth in the manufacturing industry averaged at 1.43 per cent per annum over the 2005-2009 period. The average annual growth rate declined from 3.34 per cent in 2007 to -0.75 per cent in 2008. This was followed by a growth rate of 0.44 per cent in 2009. With improved performance in 2010, the sector recorded a 0.6 per cent growth in formal employment, largely driven by employment under the African Growth and Opportunities Act, which grew by 26.5 per cent. In terms of the sector's contribution to overall employment, 13.3 per cent and 13.0 per cent of all formal employees were engaged in manufacturing in 2009 and 2010, respectively.

The improved sector growth in 2010 has been attributed to declining interest rates (which attracted new investment in the sector), low inflationary trend (inflation fell from 16.2% in 2008 to 4.1% in 2010) that boosted local consumption, availability of raw materials, and reliable power supplies (which resulted in high industrial production). The strong rains in early 2010 led to increase in agricultural output of various commodities, including the staples – maize and beans – lowering prices of food items in addition to contributing to better performance in agro-based industries.

The rebounding of manufacturing growth in 2010 is unlikely to be sustained in 2011 if the severe drought experienced in the months of January and February continues into the mid-months of the year. Food scarcity is already being reported in dry areas of the country and the possibility of a national food crisis will drive up inflation. With high dependence on hydroelectric and thermal power, energy costs will continue to rise. This is further being compounded by high international prices of oil. Consequently, dwindling consumer demand and higher production costs will result in slow growth of the sector. Further, the political environment in Kenya is unpredictable and shaky, and may compound the economic challenges due to negative signals that may arise.

With limited employment capacity in traditional agriculture, and stagnant or declining employment opportunities in the public sector, the importance of the manufacturing sector as a catalyst for economic growth cannot be over emphasized. Indeed, Vision 2030 expects the manufacturing sector to play a critical role in creating employment, generating foreign exchange, and attracting foreign investment.

9.2 Manufacturing Performance

Though the manufacturing sector in Kenya is diversified in terms of manufacturing activities, processing of food and other agricultural goods still contributes the largest share of manufacturing GDP. Table 9.1 shows that food manufacturing contributes about 21 per cent of manufacturing value added, followed by production of non-metallic refining minerals and petroleum products at about 15 per cent and 11 per cent, respectively. Lack of industrial transformation has negative implication on the overall growth of the manufacturing sector and the economy. Some sub-sectors in manufacturing also absorb the largest shares of about 13 per cent manufacturing contribution to overall formal employment. For instance, of the total wage employment in the manufacturing sector in 2009, the food sub-sector contributed 31 per cent whereas textiles contributed 17 per cent (KIPPRA, 2010). The percentage contribution of each sub-sector to overall employment has remained fairly constant over the last six years, an indication of lack of major transformation shift within the sector.

As Figure 9.2 shows, food, beverage and tobacco manufacturing sub-sectors actually recorded negative growth in 2008 and 2009 but picked up to achieve a growth rate of 10.76 per cent in 2010

Table 9.1 Percentage share of total manufacturing value added by sub-sectors

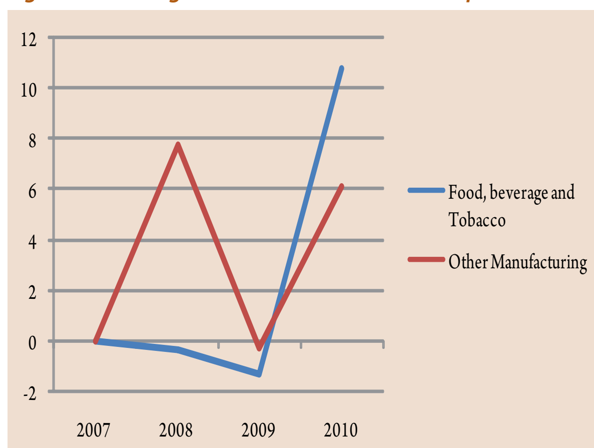
GDP product by manufacturing activity	2005	2006	2007	2008	2009	2010
Total food manufacturing	20.60	20.37	20.93	19.34	22.57	21.81
Tobacco and beverages	8.37	9.04	9.45	9.19	9.68	10.06
Textiles and clothing	3.14	3.25	3.1	2.73	2.18	2.16
Leather and footwear	1.76	1.75	1.83	1.67	1.55	1.88
Wood and furniture	1.69	1.39	1.39	1.43	1.57	1.77
Paper and printing	7.28	6.51	6.5	6.4	5.15	4.75
Industrial chemicals, paint and soap	1.43	1.42	1.4	1.38	1.5	1.59
Petroleum refineries: oils, vaseline	15.87	15.38	15.32	17.4	10.61	10.62
Rubber products	1.32	1.34	1.24	1	1.12	1.05
Plastic products	1.98	1.93	1.78	1.39	1.61	1.52
Clay and glass products	1.61	1.46	1.51	1.76	2.07	2.04
Metal products	4.23	4.58	4.6	4.07	4.2	4.15
Non-metallic mineral products	9.81	11.08	11.41	13.37	15.67	15.46
Transport equipment	1.50	1.76	1.61	1.53	1.61	2.02
Micro and small enterprises*	11.94	12.01	11.66	11.91	13.82	13.66
Export Processing Zones*	4.05	3.79	3.93	3.48	2.90	3.17

* The categories are not really product-specific sub-sectors as is the case with other sub-sectors but listed for purposes of identifying their contribution to GDP.

Source: Computations based on Government of Kenya (2010; 2011a)

as good rains increased agricultural produce and stabilized power supply.

Figure 9.2: Change in value added at constant prices



Source: Government of Kenya (Various) Economic Surveys

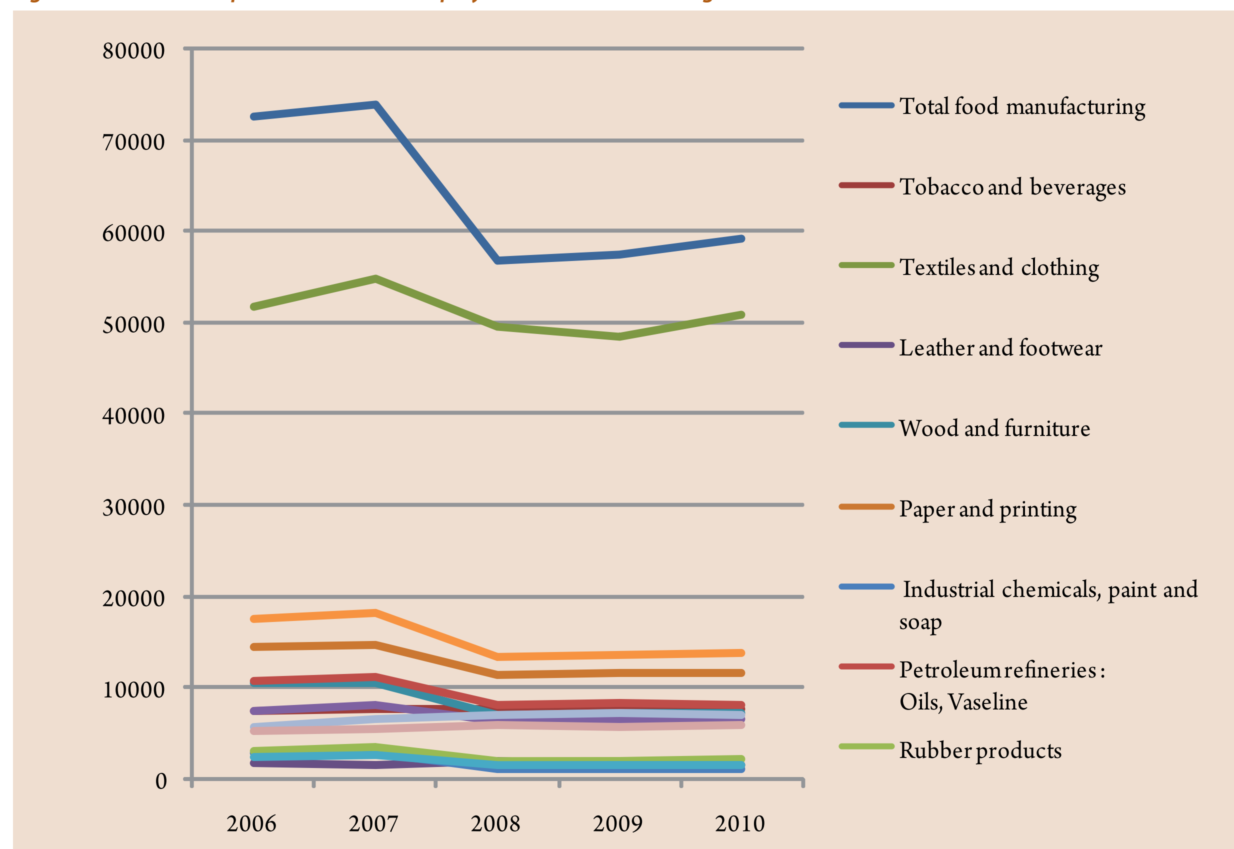
The growth of 'other manufacturing' was not as volatile, though it registered a negative growth in 2009. This relative resilience of 'other manufacturing' could be attributed to import orientation of the inputs as opposed to the food, beverage and tobacco sub-sector processing, which is agro-based in inputs, hence inward sourcing. The food, beverage and tobacco sub-sector was significantly affected by the post-election violence and dry weather in 2009.

Notably, even as the food, beverage and tobacco manufacturing sub-sector actually recorded negative growth in the 2008/09 period, the performance of 'other manufacturing' was not only positive but increased in 2008. This may be a pointer to low linkages between the two sub-sectors, meaning that the two sub-sectors neither support nor reinforce each other.

Though Vision 2030 expects the manufacturing sector to play a significant role in employment creation, the number of people engaged in various sectors has generally been declining (Figure 9.3).

There are a number of possibilities for this development. Declining employment may result if firms are increasingly experiencing poor

Figure 9.3: Number of persons in formal employment in manufacturing sub-sectors



Source: Computed from Government of Kenya (2011a)

performance (and hence curtail employment) or are divesting and possibly relocating to other countries.

There is the possibility of automating a number of operations (and hence less use of labour) or firms may opt to engage employees on casual or short-term contract basis to limit their statutory responsibilities related to having employees on permanent contractual terms.

These possibilities raise policy issues in relation to technology choice, nature of contractual engagement of employees (whether casual or formal employment), level of new investment in manufacturing and the growth of industrial establishments in Kenya. On the whole, as Table 9.2 shows, labour productivity across sub-sectors has been increasing, raising the possibility of reduced labour engagement.

*Table 9.2: Labour productivity across manufacturing sub-sectors**

Year	2006	2007	2008	2009	2010
Total food manufacturing	2.12	2.31	2.45	2.99	3.35
Tobacco and beverages	4.10	5.52	5.59	6.47	7.28
Textiles and clothing	0.32	0.33	0.32	0.32	0.29
Leather and footwear	6.06	8.84	3.60	4.58	7.65
Wood and furniture	0.28	0.37	0.50	0.50	0.64
Paper and printing	2.57	2.47	3.67	2.63	2.55
Industrial chemicals	1.98	2.07	3.88	4.49	5.43
Petroleum refineries	7.95	6.51	10.67	7.09	10.11
Rubber products	2.25	2.10	2.00	2.34	2.36

Year	2006	2007	2008	2009	2010
Plastic products	1.17	1.26	1.20	1.38	1.47
Clay and glass products	1.40	1.30	2.77	3.34	3.99
Metal products	0.90	1.03	1.06	1.15	1.24
Non-metallic minerals	4.62	4.71	5.43	6.41	6.94
Transport equipment	2.12	2.31	2.45	2.99	3.35

*For large-scale firms and establishments

Source: Computed from Government of Kenya (2011)

Comparing the value of output relative to number of employees engaged in the sub-sector, leather and footwear, and tobacco and beverages recorded the highest labour productivity in 2010. This finding suggests that either employees in these sub-sectors are more productive than in other sub-sectors, or the sub-sectors are relatively more capital intensive. Indeed, firm size matters in labour productivity, as recent work on Kenya manufacturing suggests positive correlation between size of establishment and labour productivity (Chege and Kimuyu, 2011). Large firms generally tend to be more capital intensive than relatively smaller farms.

9.3 Sector Performance within the International Context

Kenya aspires to become a globally competitive and prosperous nation with a high quality of life by the year 2030, a development level akin to that of newly-industrialized countries. The manufacturing sector has been pivotal in growth of the economies of South East Asian countries. Indeed, a high performing manufacturing sector is associated with a strong export performance in newly-industrialized countries such as China and Malaysia. As Table 9.3 indicates, manufacturing contribution to GDP in Kenya is substantially low compared to that of middle level economies such as Korea, Malaysia and China. Kenyan manufactured goods contributed just about a third of merchandise exports in 2008. The Kenyan manufacturing sector is still much in agro-processing and production of consumer products. The sector will have to be re-structurally diversified so as to hasten its growth and contribution to GDP.

Table 9.3: International comparison of sector's performance (merchandise exports, 2008)

Country	Sector's Growth	% Contribution to GDP	% Contribution to Exports
Brazil	3.2	16.0	45.0
China	10.5	34.4	93.0
Egypt	8.0	16.9	37.0
India	-	16.0	63.0
Kenya	3.6	12.0	37.0
Korea	3.1	28.1	89.0
Malaysia	-	28.0	54.0
Singapore	-4.1	20.8	70.0
South Africa	5.5	18.5	52.0
Thailand	-	35.0	74.0

Source: World B ank (2010b)

For Kenya to achieve accelerated growth in the future, the issue of low export share of manufactured goods must be addressed. This primarily calls for value addition in traditional exports in addition to technological transformation to enhance quality to international standards. An examination of the types of manufactured goods from most of the newly-industrialized countries suggests that the technological structure of manufacturing in South East Asia has been largely upgraded in line with mature industrial countries such as Japan.

Literature on evolution of industries in South East Asia indicates that the structure of manufacturing shifted from resource-based (1957-1963) and low technology activities to medium (1960s-70s) and high technology ones (1980s-90s). Since 2000, industrial production in these countries has mainly been knowledge-based, with emphasis on higher value addition. Thus, manufacturing production in newly-industrialized economies has experienced rapid technical transformation, shifting the structure of manufacturing towards more complex technology and skill-intensive activities.

Apart from inefficient policy focus, the inability of the manufacturing sector in Kenya to transform and grow is mainly attributed to weak fundamental conditions. Not only is the domestic market in Kenya too small to drive industrial development but also the business environment has been imposing high production costs to manufacturers.

9.4 Outstanding Challenges and Policy Options: An Institutional Approach

Constraints that hinder manufacturing competitiveness in Kenya are well outlined in various government publications. These include low value addition and diversification, low productivity, slow investment growth, low research and development, narrow export base, influx of counterfeits and substandard goods, high production costs associated with poor physical infrastructure and high costs of energy.

The challenge to the government is to develop a model of industrial growth that addresses the various facets of industrial challenges. The period 2008-2010 has experienced renewed government commitment for reforms to facilitate industrial development in Kenya. Such efforts include the enactment of the Anti-Counterfeit Act 2008 to reduce substantial losses borne by manufacturers, and losses in tax revenue occasioned by counterfeits in Kenya. Further, an MSME competitive project is underway to improve growth and competitiveness of MSMEs in Kenya through increase in access to finance, strengthening enterprise skills and market linkages, and improving the business environment. However, there is need for more institutional reforms for the manufacturing sector to overcome teething challenges that impede its growth.

Overall, experiences of industrial pathways in newly-developed economies such as China, South Korea and Malaysia show that growth in manufacturing is a result of reform efforts undertaken by the respective governments of these countries. At the onset was the strengthening of institutional governance, with top technocrats in the country assigned enforceable performance targets backed by adequate resources, while at the same time insulating them from political manipulation. More importantly, to inspire investors' confidence, the respective governments worked towards sorting out political uncertainty as safeguards against frequent, unpredictable alteration of the regulatory environment. Meanwhile, the adoption of a new Constitution in Kenya is likely to form the basis for renewed efforts to reduce investor uncertainty, though it needs to be implemented in good time to be effective. Further, Kenya needs to prioritize interventions in the following areas:

9.4.1 Increasing Value Addition in Agro-Processing and Diversification of Manufacturing Output

Kenya's manufacturing sector is still largely based on agro-processing and production of consumer products. The immediate challenge is, therefore, the need to increase value addition in the agro-processing sub-sector. General observations in processing of crops such as coffee and tea indicate that there is excessive regulation, which provides fertile ground for emerging of middlemen and extracting of rents through taxes and licensing by the government. In agro-processing industries where there is substantial value addition, the government's role has been minimal, mainly confined to regulatory and facilitative functions, fostering private sector initiatives and dynamism within the industry. The government should initiate substantial reforms in laws that govern operations in the agro-processing of various crops, allowing the private sector to play a critical role in agro-processing.

9.4.2 Drive for Increased Local and Foreign Direct Investment

Investment is a key factor in providing the basis for economic growth, since it serves as a channel for technological transfer, allowing firms to develop new products or to make existing ones better.

Increasing production also requires expanding plant and machinery, hence the need for investment.

Potentially, fiscal incentives such as quality infrastructure, attractive fiscal packages and minimal regulations promote investments. Thus, the development model of government to create Special Economic Zones as envisioned in Vision 2030 should be structured to attract investments in desirable activities and technology from both local and foreign investors.

Government efforts to support entrepreneurship date back to independence, starting with government-sponsored financial support for micro-enterprises, which were meant to let African entrepreneurs into commerce from which they were previously excluded. Institutions such as the Industrial and Commercial Development Corporation (ICDC), the Kenya Industrial Estates (KIE), District Joint Loans Boards, and Kenya Tourist Development Corporation (KTDC) came from this incentive. However, these initiatives proved expensive and unsustainable. Further, most of these government schemes had governance challenges, making them ineffective in improving financial access.

In recent years, particularly since 2005, the government has renewed support of local investment through the Youth Fund and Women Fund projects, social safety nets such as the 'Kazi kwa Vijana' project as well as the economic stimulus programme introduced in 2009. The economic stimulus programme consists of construction projects in education, health and social sectors, the enhancement of human resource capacity in the form of hiring of nurses and teachers, and in the facilitation of operations of the projects. The aim of the programme is to stimulate economic activity at the local level by creating employment opportunities, spurring entrepreneurial activities and supporting the building blocks that anchor a healthy, educated populace. To promote industrialization, the programme targets to construct one Jua Kali shed in every constituency as well as purchase welding and fabricating machines.

The immediate challenges to the success of the programmes will be how to fast-track them amidst the stringent procurement procedures, limited capacities of implementing ministries as well as domestic borrowing by the government, which creates new pressures on interest rates and prices.

9.4.3 Industry Policy Framework and the Global Trend

Strategic transformation of the manufacturing industry requires planning and implementation of well-defined strategies. Overall, the South East Asian countries have had a remarkable industrial growth, adopted industrialization strategies that were oriented to changes in the global environment and market requirements, at the same time being sensitive to national goals.

Without an industrialization policy in Kenya, it is evident that the country lacks adequate industry policy framework to guide the manufacturing sector to meet the ever-changing demands of consumers within a global context. An industry policy will also be important for creation of a level playing field for competing firms. In addition, there is need for a more participatory planning process with firms and interest groups to ensure implementation of the Anti-Counterfeit Act 2008.

Re-orienting the manufacturing sector to exports calls for diversification of the economy from traditional trade in minerals and primary agricultural commodities to manufactured goods and exportable services. Further, Kenya can use her coastal location and leadership in industrial establishment and support regional cooperation; as domestic firms will exploit their natural comparative advantage, countries that are well regionally-integrated improve their participation in the world economy. The commitment for domestic authorities to full regional integration calls for them to implement politically difficult measures, such as lowering tariffs or instituting wide-ranging reforms of the regulatory and judicial systems. In addition, regional integration

requires regional surveillance and dialogue between the various partners, which help reduce the risks of macroeconomic slippage, resulting in a more stable, predictable environment—clearly an essential factor for the private sector to flourish.

9.4.4 Creation and Growth of Enterprises

Small-firm clusters remain locked in low-quality products and low-income markets with little innovation that can attract foreign demand, yet small enterprises must provide productive employment for an increasing number of job-seekers. Innovation in small enterprises is normally limited to the apprenticeship process and, as such, results in being a dead-end to indigenous technology progress occasioned by market and technology dynamism.

To promote creation and growth of small firms, efforts are required to put the MSE clusters in the global value chain, as this enhances possibilities of new market avenues as well as benchmarking indigenous market innovative efforts to international standards. Exposure of small firms to the global market also encourages formation of networks, which are conduits of skills for quality improvement and valuation of products.

Overall, the government is expected to support innovation and may possibly do so by encouraging sub-contracting of small firms with large firms, through fiscal incentives, in addition to improving the business environment through better infrastructure and efficient regulatory environment.

9.4.5 Improving Productivity through Cluster Development

Any sector growth requires supportive mechanisms to thrive. Low productivity in manufacturing is partly attributable to weak linkages with other sectors and within sub-sectors of the manufacturing establishments. For instance, there are little linkages between R&D institutions and the manufacturing sector. Many enterprises also feel that financial and public support mechanisms are not very favourable. The high cost of capital and bureaucratic and inefficient provision of public services are impediments to rapid growth of the sector. In order to improve competitiveness and productivity, the National Economic and Social Council (NESC) has recommended a cluster development strategy to create related and supporting industries. For instance, the packaging sub-sector, within the manufacturing sector, has general strengths as a supporting industry and can play a significant role in value addition in many products. Similarly, ICT can potentially contribute more to the manufacturing sector by reducing transaction costs.

Chapter 10

Business Process Outsourcing/Offshoring

10.1 Introduction

According to Vision 2030, the Business Process Outsourcing (BPO) sector has significant potential in making important contributions to the country's economy. However, it is a sector that is still in infancy and faces a number of challenges. Unlike countries such as India, the BPO sector in Kenya is young, small and largely under-developed. Like India, however, Kenya has certain advantages, which include low wages and a large educated English-speaking workforce with high academic standards. According to Vision 2030, the sector provides employment to 1,000 workers, accounting for less than 0.01 per cent of GDP. The sector, however, has significant growth potential, especially with the global growing demand for certain BPO services. The Vision's target is to create at least 7,500 direct jobs in the sector and increase GDP contribution by Ksh 10 billion by 2012.

The Kenyan government should continue putting emphasis on encouraging the development of the BPO sector as it has an important role to play in employment creation and overall development of the economy. This is especially because Kenya has a large human resource base that is highly skilled and could take advantage of the sector. Additionally, Kenya has introduced fibre optics infrastructure, which has made the country competitive with respect to improved data transfer rates, bandwidth capacity and overall costs.

Outsourcing is actually not new in Kenya. It has been used by companies that want to focus on their core competencies. Learning institutions and hospitals, for instance, often outsource catering and cleaning services; such institutions also outsource transport services or fleet management. There are companies that provide human resource services and recruitment, which are sometimes outsourced by other companies. Training services, typing and marketing (and market research) can also be outsourced. Developments in the Information, Communication and Technology (ICT) sector have led to the emergence of further BPO opportunities in the sector in Kenya, such as call centres, transcribing services, web design and software development, and data entry.

This chapter aims to identify some medium-term key policy issues that should be properly addressed with the aim of improving Kenya's image as a destination for BPO.

10.2 Recent Performance Indicators

10.2.1 Improved Internet Connectivity and IT Infrastructure

The BPO sector relies heavily on IT infrastructure. There have been several developments in the IT sector over the last few years, which are important for the BPO sector. This includes growth in internet access and internet investments as indicated in Table 10.1 and Figure 10.1.

Table 10.1: Data and internet revenues

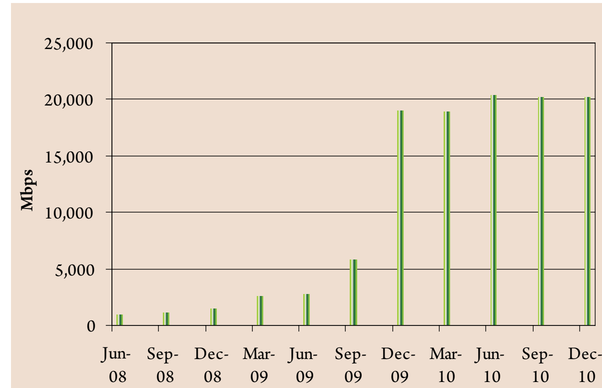
Year	2007	2008	2009	2010
Data and internet revenue (Ksh millions)	7,370	7,595	145,800	148,033
Data and internet investment (Ksh millions)	833	1,171	53,870	29,361

Source: Communications Commission of Kenya (2010)

The improved internet access and increased internet investment illustrated in Table 10.1 can be attributed to the landing of the undersea cables, which contributed to increase in international internet bandwidth. Kenya now has three undersea cables: EASSy which landed in 2010, The East African Marine System (TEAMS) and SEACOM. The latter two landed in 2009 and account for 98 per cent of total international internet bandwidth (Communications Commission of Kenya, 2010; Waema *et al.*, 2010). Kenya has also experienced a growth in mobile data/internet subscription through GPRS/EDGE and 3G provided by the different mobile service providers, which accounts for 98 per cent of total internet subscriptions (Communications Commission of Kenya, 2010). These developments have contributed to cheaper internet access, higher bandwidth capacity, and an increase in international internet connectivity (Figure 10.1). This is important for the BPO sector, which relies on high bandwidth and good connectivity to be effective and competitive.

Over the years, demand for satellite internet bandwidth has been declining due to increased demand for the undersea cables, which are more affordable and available. As of December 2010, 99 per cent of total internet bandwidth was from undersea internet connections.

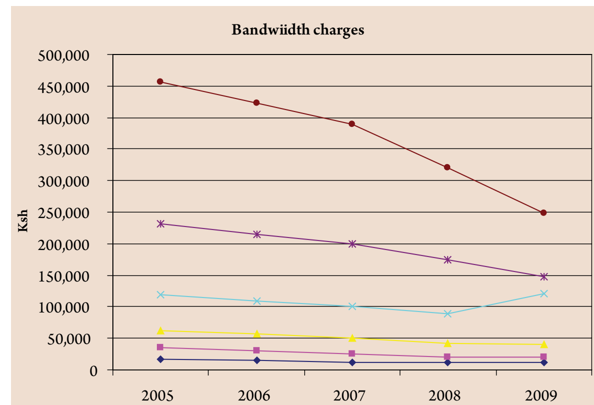
Figure 10.1: Total international internet connectivity bandwidth (2008-2010)



Source: CCK Quarterly Sector Statistics Reports

These developments have also contributed to the reduction of costs charged by internet service providers (ISPs). As indicated in Figure 10.2, bandwidth costs have been declining over the years as the bandwidth was increasing.[1]

Figure 10.2: Bandwidth charges to ISPs



Source: Communications Commission of Kenya (2010)

Businesses that rely on internet connectivity have also been growing over the years due to the increase in reliable and affordable internet access; this is evidenced by the Business Process Outsourcing/IT Enabled Services (BPO/ITES) sector. The first BPO

to be licensed by CCK was in the year 2004; which was a call centre (Communications Commission of Kenya, 2008). Since then, the number of licensed BPOs in the country has been increasing over the years as indicated in Table 10.2. Between 2006/07 and 2007/08, the number of BPOs registered increased by 800 per cent, which may be attributable to the increased policy focus to the sector as the government identified the sector as an important economic pillar and driver of economic growth.

Table 10.2: Number of licensed BPOs in Kenya (2004-2010)

30th June Year	Total No. of BPOs Licensed
2004/05	1
2005/06	1
2006/07	2
2007/08	18
2008/09	20
2009/10	25
31st Dec 2010	30

Source: Communications Commission of Kenya (2010)

10.2.2 Policy Focus

Kenya's Vision 2030 has prioritized the BPO sector as one that the country can benefit from given the growth of the global offshore market and the growing demand. The vision for the BPO sector in Kenya is "to be the top offshoring destination in Africa".

One of the planned activities in Vision 2030 is the establishment of a state of the art BPO Park, which would have superior telecommunications infrastructure, easy access to international transport facilities and affordable and readily available energy. As indicated in the 2008/09 Budget Speech, the ICT sector was allocated Ksh 900 million towards the establishment of a large BPO park in Nairobi. The technopolis (a city built up for technology firms) to host the BPO Park will be on a 5,000 acre piece of land, 60km south of the city of Nairobi in Malili, Konza. Countries such as Egypt, Malaysia and Philippines have similar initiatives as summarized in Table 10.3.

Table 10.3: Technology parks in selected countries

Country	ICT/ Technology Park
Malaysia	Putrajaya forms part of the Multimedia Super Corridor. Putrajaya is, however, the federal administrative capital, which was built on over 5,000 hectors of marshland and former oil palm estate, 25 km from Kuala Lumpur. The residential population in the area as at 2010 is 30,000 and the working population is 34,000. There are modern transport and telecommunication systems and a host of facilities and amenities.
	Cyberjaya also forms the Multimedia Super Corridor 26 km from Kuala Lumpur city centre on 7,000 acres with high class IT infrastructure and amenities and facilities dedicated to multimedia companies. It also houses multinational corporations, universities, etc.
	As at 2009, the Multimedia Super Corridor (MSC) employed almost 100,000 persons and has 2,520 companies.
Philippines	Subic Freeport Zone has 13,800 hectors with more than 610 companies employing over 7,000 workers. It is segmented into the Central Business District, Subic Gateway, the Subic Bay Industrial Park and the Subic Techno Park. There are numerous commercial, recreational and tourist activities. Members also enjoy incentives such as tax and duty exemptions and tax holidays.
	Clark Freeport Zone has 28,000 hectors 400 investors employing over 55,000 workers. Businesses include ICT companies, hotels, restaurants and other recreational activities. Both Subic and Clark were formally US military bases.
Egypt	Smart Village was founded in 2001 to lead and foster the technology cluster. It covers 3 million square metres in Cairo's west suburb, with over 35,000 employees and more than 150 companies as at 2010. Some of the companies located there include Oracle, Vodafone Egypt, Alcatel-Lucent and Microsoft. Smart Village is well equipped with respect to telecom infrastructure including high-speed broadband fibre optic networks.

Source: Presentation made on the Malili Multi-Use Technopolis – The Concept by Bitange Ndemo, Permanent Secretary, Ministry of Information and Communications; http://www.smart-villages.com; http://www.i-putra.com.my; http://www.clarksubicmarketing.com/ and Multimedia Development Corporation (2009)

A BPO/ITES Working Group was established in December 2009 through a Gazette notice with the key aim of guiding and facilitating the development of BPO/ITES activities as envisioned in Vision 2030.[2]

The Konza Technopolis, like the Smart Village in Egypt, will be a public-private partnership. The government has initiated some activities towards realizing this plan as indicated in Table 10.4.

Table 10.4: Achievements, 2008-2010

MTP Outcome/ Output	Cumulative Achievements, 2008-2010
Establishment of ICT Park (Malili Technopolis)	Land registered under government; feasibility study ongoing
	Master plan in place
	Environmental and impact assessment study complete
	Initial concept presentation made in November 2009
	Parliamentary Accounts Committee endorsed the proposal in February 2011
	Konza City Masterplan developed[3]
Market Kenya as a BPO destination	Jobs created through facilitating local BPO operator.
	KenInvest and Brand Kenya have been assisting in this effort
Capacity building	Jomo Kenyatta University of Agriculture and Technology (JKUAT) was awarded the contract as the lead trainer. A certificate course in Business Process Outsourcing was launched in November 2010
	Youth trained in BPO and entrepreneurship skills
Prepare a BPO Incentive Policy	BPO Incentive Policy in place and is being implemented
Regulatory environment	10 BPO operators received bandwidth subsidies

Source: Government of Kenya (2011)

The government is also in the process of developing a framework for the development of Special Economic Zones (SEZ), which will provide for ICT Parks and ICT Towers (ICT Park refers to where IT-related knowledge and service industries will be supported and facilitated, while ICT Towers refers to where ICT service companies will be hosted in well equipped stand-alone multilevel buildings).

10.2.3 ICT Incentives

The sector also benefited from a number of incentives that have been introduced over the years, for example, the 5 per cent allowance on computer software, and an increase of wear and tear allowance on telecommunication equipment from 12.5 per cent to 20 per cent aimed at encouraging investment in telecommunication equipment. These were announced by the Ministry of Finance during the 2009/10 Budget Speech. The Minister also announced the removal of VAT and import duty on televisions, cameras, digital cameras and video cameras to film producers. In 2008/09, import duty on telecommunication equipment and all printers was removed. Computer software now forms part of VAT zero-rated goods as indicated in the VAT Act (2009). New Personal Computers (PCs) and computer parts only attract Import Declaration Fees of 2.25 per cent of cost (CIF).

10.2.4 Innovation in Finance

The banking sector in Kenya has grown over the years and now has 44 commercial banks, most of which are capable of sending and receiving funds overseas through services such as Electronic Funds Transfers (EFT) and Real Time Gross Settlement (RTGS) by Kenya Electronic Payment and Settlement System (KEPSS). This enables people and companies to pay and receive payments on real time basis. Kenya has also introduced several innovations in this area, especially with the introduction of mobile payment solutions, mobile funds transfers and mobile banking. These emerging innovations have built on this platform: M-Pesa from Safaricom and Airtel Money, some of which are summarized in Table 10.5.

Table 10.5: Innovations in finance

Service Provider	Service
iPay; mobile money processing	Mobile money transaction processing system that incorporates M-PESA, Airtel Money and yuCash allowing companies to receive mobile payments electronically, which are then submitted to the company by Electronic Funds Transfer (EFT) or cheque payment.
PesaPal	One can use MPesa, Airtel Money or a credit card to make payments such as school fees, online ticketing, processing donations and generally buying and selling goods and services online. Once the transaction is done, the money is then held in a trust account before disbursing to the merchants/sellers' account.
JamboPay	It is an online payment gateway that enables merchants to allow the buyer/ user to make payment using their website (on partnering with JamboPay) using M-Pesa, Airtel Money, yuCash, credit cards or debit cards.
I&M Bank merchant e-payment service	The online payment service is available to merchants who can accept Visa card payments through their websites.

Source: I&M Bank http://www.imbank.com/KE/inner.asp?pcat=&cat=news&sid=303; JamboPayhttps://www.jambopay.com; PesaPalhttps://www.pesapal.com; iPayhttp://www.intrepidkenya.com

The government has also recently enacted a Payments Systems Act No. 39 of 2011 to regulate payment systems and providers and drafted Regulations for the Provision of Electronic Retail, Transfers and Electronic Money. These are important innovations; however, they largely focus on providing local solutions. The BPO sector would benefit from more developments to assist them in undertaking their international electronic transactions. PayPal, for instance, is an internationally-known payment system, which allows one to make and receive payments online in a number of countries worldwide. One can now receive and send money from Kenya using their PayPal account. However, mechanisms of withdrawing the funds in the account locally are yet to be established. Currently, withdrawals can only be done to a US bank account.

10.3 Regulatory and Institutional Framework

The institutions that address this sector include: The Ministry of Information and Communication, the Communications Commission of Kenya (CCK), the ICT Board, the Export Processing Zones Authority (EPZA), Brand Kenya Board, and KenInvest. CCK is the regulatory body for the communications sector and also issues the relevant licences. CCK provides licences for broadcasting services; electronic certification systems; repositories and administrators of sub-domains of the country's top level domain (.ke); and postal systems and services and operators in the telecommunication sector. Following the amendment of the Kenya Information and Communications Act in 2009 (by the Kenya Communications Amendment Act No. 1 of 2009), CCK is also mandated with additional functions relating to the facilitation and development of electronic transactions and electronic commerce and the control of electronic fraud.

The key mandate of the ICT Board includes: marketing Kenya as an ICT destination; providing advice to the government; providing capacity and funding to stakeholders; and implementing ICT projects. The Export Processing Zones Authority also has a role to play due to the fact that outsourcing is largely an export activity through offshoring. BPOs can, therefore, operate from an Export Processing Zone (EPZ). Currently, there is one BPO in the EPZ located at the Sameer Industrial Park EPZ in Nairobi. It is a call centre with 240 members of staff (as of end of September 2010).[3]

There are two additional institutions that play a role in marketing Kenya as a BPO destination. These are KenInvest and Brand Kenya. KenInvest's (Kenya Investment Authority) main objective is promoting investments in Kenya, while the Brand Kenya Board is mandated to coordinate marketing of the country and creating and/or distinguishing and maintaining Kenyan brands, products, services and concepts.

The main regulatory instruments that govern the ICT sector in Kenya are: the Kenya Information and Communications Act (Cap 411A) and the National ICT Policy (2006). The latter was recently revised through the enactment of the Kenya Communications Amendment Act (2009). Some of the amendments include provision of electronic transactions, which addresses a number of things including electronic records, electronic signatures as well as electronic fraud. The Act also deals with unlawful possession of data, which is complemented by the Constitution of Kenya (2010) that grants everyone a right to the protection of the privacy of their communication. These are important provisions that would give confidence to potential customers.

The Kenya Information and Communications (Electronic Certification and Domain Name Administration) Regulations 2010 provide regulations on digital signature certificates, and certifies service providers and country code top level domains.

Other relevant statutes include the Export Processing Zones Act (Cap 517), the Copyright Act (2001), and the relevant statutes on employment, which include: the Employment Act No. 11 of 2007 and the Occupational Safety and Health Act No. 15 of 2007. The Employment Act (2007) provides information on labour-related activities such as leave, working hours, minimum working age and so on. The Act also gives the Minister responsible for labour matters the mandate of making rules on the intervals for rest and meals. The Occupational Safety and Health Act (2007) deals with the welfare of labourers and has relevant provisions such as overcrowding, ventilation, lighting and other work safety issues.

A summary of the institutional and regulatory framework in Kenya and other comparator countries is summarized in Table 10.6.

10.4 Country Comparisons

Countries such as India, Malaysia, Egypt and South Africa have been selected as comparator countries based on their performance. India, for instance, is said to be commanding 65 per cent of the total BPO industry with revenue of US$ 30 billion as of 2008. South Africa and Egypt are considered as major players in the sector from the region. South Africa, for example, has a well-established domestic outsourcing market and has carved a niche in the financial services sector especially in actuarial and insurance services (Waema *et al.*, 2009). This may be attributed to Johannesburg being an international financial hub in the banking financial services and insurance industry, with a number of call centres. According to Waema *et al.* (2009), South Africa has many large, experienced players with sophisticated products, especially in insurance and banking and common qualification with many client countries. Malaysia is also considered an important player since its conceptualization of the Multimedia Super Corridor (MSC) concept in 1996, which mirrors Kenya's Konza Technopolis concept. Malaysia seems to have introduced relevant laws and institutions to support this concept as illustrated in Table 10.6. The MSC is located south of the Kuala Lumpur Metropolitan area covering an area of 15 km by 50 km.

10.5 Medium Term Prospects

Kenya is making strides towards introducing a large technology park, which would support BPO/ITES services through the establishment of the Konza Technology City.[4] Some of the expected prospects of this would be increased employment; improved technology transfer; further ICT infrastructure developments; and further investments in human capital, all of which are likely to raise overall productivity and also have spillover effects to other related industries. Kenya already hosts a number of prominent international IT companies, and the establishment of the Konza Technology City is expected to attract additional global players.

Table 10.6: Relevant institutions

Country	Sector	Institution	Support and Regulatory Tools
India	ICT related	Department of Information Technology (DIT), Ministry of Communications and Information Technology. In 2004, through a gazetted executive order, DIT appointed INRegistry as the official .IN domain registry	Provides incentives, including: zero duty on imported software; income tax exception on IT software and services; 150% R&D expenditure. Support includes: infrastructure; patent protection in electronics; multiplier grant schemes; the Technology Innovation Promotion Schemes; Technological Incubation and Development of Entrepreneurs (TIDE) schemes; ICT-Intellectual Property Rights Promotion Programme; tax holiday to R&D for up to 10 years with 125 per cent tax concession and IT venture capital fund
		Cyber Appellate Tribunal to deal with disputes and the Controller of Certifying Authorities (CCA) to license and regulate the working of Certifying Authorities (CA) that issue Digital Signature Certificates	Information Technology Act (2008), which recognizes digital signatures, legitimizing contacts made through electronic means and provides for electronic transactions. The Act provides for Digital (Electronic) Signature Certificates and also provides a safeguard against data breaches, unauthorized use of computers and cyber terrorism. It provides penalties for failure to protect data. Companies are legally expected to implement and maintain reasonable security practices and procedures to ensure that there is no wrongful loss or gain to any person
	Technology Parks	Software Technology Parks, Autonomous Society under the DIT setup, manage infrastructure and provide support services	Software Technology Parks Incentives include: income tax benefits; custom duty and central excise duty exemptions; central sales tax reimbursements on indigenous purchases; loan/lease facilities for importing equipment; income tax holidays for 10 years or up to 2010, whichever is earlier (this was extended and expired in March 2011). Data centre providing backup services.
	Copyright	Copyright Office	Copyright Act guards against software piracy of copyrighted material
South Africa	ICT related	Independent Communications Authority of South Africa (ICASA) is the regulatory body that regulates, monitors and licenses the communication sector. Accreditation Authority established to monitor, authenticate and certify products and services used in support of electronic signatures and the za. Domain Name Authority set up to administer and manage the .za domain name; license and regulate	Electronic Communications Act (2005) provides the regulation for electronic communication services and gives the ICASA, which was established by the Independent Communications Authority of South Africa (ICASA) Act, the mandate of introducing measures to protect personal data, privacy and prevent fraud and provides for the Universal Service Agency and Universal Service Fund. Electronic Communications and Transactions Act (2002) focuses on SMEs, provides for electronic transactions; legally recognizes electronic signatures and provides a system for authentication. The Act also develops a national e-strategy; domain name registration and protects against abuse of information and cyber crime and provides for cyber inspectors to monitor and inspect cyber activity and report any unlawful activity to the appropriate authority. It also provides database and data message protection
	ICT/ BPO	Department of Trade and Industry; the Ministry that regulates the ICT and BPO sector, while also proving investment support	Provides investment grants; training support grants; export market and investment assistance; technology industry finance and enterprise development through R&D, capacity building and certification of BPOs and BPO staff. Has a BPO quality assurance framework

Country	Sector	Institution	Support and Regulatory Tools
	Copyright	Companies and Intellectual Property Registration Office (CIPRO), Department of Trade and Industry	Copyright Act No. 98 of 1978 (as amended by 2002); the Act protects original works including literary, music and artistic works and also includes computer programmes and digital data
Egypt	ICT related	Information Technology Industry Development Agency (ITIDA), whose role is to encourage and develop ICT, protects interest of IT activities and provides support services and regulatory	The Law No. 15 of 2004 on e-signature and establishment of Information Technology Industry Development Authority legally recognizes e-signatures and e-writing. It also provides for Digital Certification for them. E-transactions are also recognized and ITIDA is expected to ensure compliance with these laws
		Ministry of Communication and Information Technology (MCIT)	The Ministry provides ICT training, data and Internet centres, a high-tech Smart Village, tax exemptions, and a free zone for international call centres; transit regional Internet traffic and the free Internet initiative
		National Telecommunication Regulatory Authority (NTRA) licenses and promotes competition in the sector	The Law No. 10 of 2003 on the Telecommunications Regulation Law established the NTRA. The Law also provides licensing information for players of the sector. NTRA also provides domain name registration licenses
	Free Zones	General Authority for Investment and Free Zones this is a one-stop-shop facilitating investment in Egypt	According to the Investment Law No. 5 of 1997, the General Authority for Investment and Free Zones can provide incentives for companies in the field of technology and communication
	Copyright	Ministry of Culture is the 'competent authority' dealing with copyrights	Law No. 82 of 2002 on the Protection of Intellectual Property Rights protects the rights of authors of literary and artistic works, which also include computer software and databases
Malaysia	ICT	Ministry of Science, Technology and Innovation; Ministry of Information, Communication and Culture and Malaysian Communication and Multimedia Commission to supervise and regulate communications and multimedia activities	Communications and Multimedia Act 1998 provides for the sector, while Malaysian Communications and Multimedia Commission Act 1998 regulates the sector and provides for the establishment of the Commission; Digital Signatures Act 1997 makes provisions for use of digital signatures Telemedicine Act 1997 provides the regulation of telemedicine E-commerce Act 2006 provides legal recognition of electronic messages in commercial transactions Computer Crimes Act 1997 protects computer data and programmes
		Personal Data Protection Commission; Personal Data Protection Advisory Committee and the Appeal Tribunal	Personal Data Protection Act 2010 to protect data subjects and regulate the processing of personal data
		Multimedia Development Corporation (MDeC) to facilitate the development and provision of MSC Malaysia	MSC Malaysia has Cybercities and Cybercentres for ICT investors/companies. The MSC Malaysia Bill of Guarantees No. 1 is offered to Malaysia status companies and provides a set of incentives, rights and privileges in form of a grant from the Government of Malaysia
	Copyright	Intellectual Property Corporation of Malaysia and Copyright Tribunal	Copyright Act 1987 and Intellectual Property Corporation of Malaysia Act 2002

Country	Sector	Institution	Support and Regulatory Tools
Kenya	ICT	Communications Commission of Kenya (CCK); established in July 1999 after the enactment of the Kenya Communications Act 1998, which establishes it with the aim of regulating the sector. The Act also established an Appeals Tribunal	Kenya Communications Act 1998 (as amended in 2008). The Act addresses electronic transactions, legally recognizes electronic records and signatures and provides that CCK licenses companies providing electronic certification services. The act also addresses issues of cyber crimes, including unauthorized access to computer data; electronic fraud amongst others and establishes the Universal Service Fund to support capacity building and innovation in ICT services. The amended Act also mandates CCK to regulate the .ke domain and sub-domains
		Ministry of Information and Communication	Functions include: formulate and implement the ICT policy and other relevant policies, the ICT Board, the CCK, the Brand Kenya Board, amongst other state corporations and the development of relevant infrastructure
		ICT Board: Established as a state corporation in 2007 to market Kenya as an ICT destination; advising the government; supporting the sector and implementing projects	Support programmes such as: BPO bandwidth capacity support (which ended in February 2009); Software Development Certification Programme (CHIPUKA); Centre of Excellence, which aims to build BPO talent and skills development through collaborations with global BPO providers; and Incubation Programme (the latter two are not yet fully implemented)
	EPZ	Export Processing Zones Authority (EPZA) established by the EPZ Act, Cap 517 in 1990 with the aim of developing and regulating the EPZs	The Export Processing Zones Act (Cap 517) for the promotion and facilitation of export-oriented investment and establishment of EPZs and the EPZA. EPZ incentives include: duty, VAT, stamp duty and withholding tax exemptions; single licence; 10 year tax holiday followed by lower corporate tax of 25 per cent for the next 10 years and 100 per cent investment allowance. Procedural, administrative and infrastructural incentives also available
	Copyright	Kenya Copyright Board	The Copyright Act 2001 protects against copyright infringement of copyrightable works, which include computer programmes

Source: Compiled by author from different sources: Waema *et al.* (2009); Trestle Group Consulting (2010); ICT Board Kenya; http://www.msc.com.my; relevant institution websites and respective Acts/Laws.

Kenya, should, however, not only focus on large scale BPOs but also develop skilled niche markets for specialized business activities that can be outsourced. These activities include: finance (especially with the establishment of a Nairobi International Financial Centre)[5]; accountancy services; human resource management, tourism and marketing; advertising; design; business planning; analysis and reporting, and so on. Such activities are more or less standardized in different regions, unlike activities such as legal services, which are subject to local laws.

It is important for Kenya to develop a sustainable BPO model, which is able to withstand external pressures. Kenya could, for instance, adopt a large-scale centralized BPO strategy, such as the Konza Technopolis and SEZ (which is already underway), but also consider a small-scale BPO strategy. One strategy that Kenya can adopt is to encourage existing companies to expand and also start offering small-scale high-end outsourcing services. Below are some examples:

Professional services such as human resource management can be outsourced: Currently, Kenya already has a number of companies that consult human resource management companies to undertake activities such as job evaluation; development of human resource policies and/or payment strategy and hiring. Such companies could expand their skill levels to be able to serve foreign markets.

Table 10.7: Relevant supporting institutions

Country	Institution
India	National Association of Software and Services Companies (NASSCOM) - a private sector lobby group for the sector.
	Data Security Council - a not-for-profit company set up as an independent self-regulatory organization (SRO) by NASSCOM to promote data protection, and develop security and privacy codes.
	Electronic and Computer Software Export Promotion Council (ESC) - sponsored by the government. Offers services such as market research, media and publicity campaigns and acts as a link between the government, foreign companies and its members.
Philippines	Business Process Association of the Philippines (BPAP) - an umbrella organization for the sector aimed at promoting and supporting the sector.
South Africa	BPO Association (BPeSA) - gets financial support from the government, making it more active and visible.
	National Contact Centre Union (NCCU) - offers support and protection on labour-related issues at the workplace.
Kenya	Kenya Business Process Outsourcing and Contact Centre Society (KBPOCCS).

Source: Authors' compilation from various sources

Creativity and innovation: There are a number of companies in Kenya that provide graphic design, interior design, animation services and advertising, which can also provide an outlet for outsourcing such services.

Tourism: This is another important sector that makes significant contributions to the economy, yet a large number of companies providing relevant services have no web presence and those that do often have a static website. This limits the marketing of tourism services aboard. In fact, a review of companies providing these services reveal that most originate from outside the continent. Locally-based tour agencies can, therefore, diversify into providing a Tourism and Travel BPO, connecting relevant tourist venues, entertainment venues, national parks, car and van hire, airlines and so on. Support for this should be provided by relevant government authorities such as Brand Kenya, Ministry of Tourism (Magical Kenya) and Kenya Tourist Board to develop this sector as a BPO.

Online market places for professional or IT-related services have emerged, whereby small businesses can get short-term jobs or consultancies in various fields from different sources around the world outsourcing certain tasks.[6] An online market can be defined as *"an inter-organizational information system through which multiple buyers and sellers interact to accomplish one or more of the following market-making activities (1) identifying potential trading partners, (2) selecting a specific partner, and (3) executing the transaction"* (Choudhury *et al.*, 1998: 475). These online market places use auction system where buyers start an auction by posting its proposal, which is open to suppliers (Radkevict *et al.*, 2006b). Caution should, however, be used when working with such websites as the auction mechanism encourages competitive bidding, which may attract lower quality suppliers from less professional suppliers, which discourages the buyer (Snir and Hitt, 2003). Additionally, it runs the risk of opportunistic buyers seeking free consultations from bidders (Radkevict *et al.*, 2006a) or buyers contracting a company that later fails to pay for services rendered. Some of these online marketplace websites, however, guard against this by facilitating payments. Most, for instance, hold payments in an account until the work is accomplished and to the buyer's specifications before it is then released to the supplier. According to Radkevict *et al.* (2006b), online marketplaces can provide small businesses with contracting opportunities; easy access to offshore resources may develop institutional trust and reduce transaction costs.

10.6 Performance Gap

In terms of institutions, Kenya is not fairing badly. As indicated in Table 10.6, Kenya has a number of institutions that deal with the ICT and BPO sector just like India, Malaysia, Egypt and South Africa. For instance, all four countries have the following:

- Independent regulatory body to govern the ICT sector.

- There is a key ministry mandated with supporting the sector.

- Protection of intellectual property rights (copyright protection).

- Legal recognition of electronic transactions, including electronic signatures.

Industry support in Kenya is, however, not as strong. Countries such as Egypt, Malaysia, South Africa and India, for instance, have incentives in place to attract investments in the sector. As indicated by Waema *et al.* (2009), there is need to develop a specific BPO policy and BPO-specific incentives in Kenya; the ICT Policy (2006) does not address the sector. Additionally, there are no sector-specific tax incentives. The ICT Board did, however, introduce a bandwidth subsidy programme, which provided 10 BPO companies with subsidies to lower the bandwidth cost. The subsidy programme was provided in three phases between the period July 2007 and February 2010. The programme, therefore, has now lapsed.

Industry support from relevant BPO associations in Kenya is also weak, especially when compared to India and Egypt, which are very strong (Waema *et al.*, 2009).

Labour laws in Kenya do not explicitly state the working hours, meals and rest intervals for employees. This may be necessary to encourage employers within the industry to provide this for their employees to ensure that the BPO workers are not exploited. Additional laws that need to be enhanced include those that deal with data protection, e-commerce and cyber crime, all of which have been addressed by relevant statutes in countries such as India, South Africa and Malaysia as illustrated in Table 10.6.

Another challenge in the sector is long and time-consuming business start-up procedures in Kenya. Investors are faced with cumbersome, time-consuming licensing procedures despite the Regulatory Reform for Business Activity in Kenya, which led to the elimination, simplification and amendment of several licences.[7] It takes approximately 33 days to start a business in Kenya, which is almost four times more than the time required for the same in Egypt, and two times longer than Malaysia.[8] Further, the process in Kenya involves visiting numerous separate institutions such as the Registrar of Companies to register the company; Local Authority for the Single Business Permit; and the CCK for the necessary licence(s).

Electricity is an important input for the BPO sector. However, high cost and unreliable electricity supply is another key challenge for businesses in Kenya.

Table 10.8 and Figure 10.3 depict the situation in Kenya vis a vis other countries such as India, South Africa and Malaysia with established BPO sectors, and neighbouring countries such as Tanzania and Uganda.

Table 10.8: Process of starting a business, 2011

Country	Time (days)	No. of Procedures
Egypt	7	6
Malaysia	17	9
South Africa	22	6
Uganda	25	18
India	29	12
Tanzania	32	7
Kenya	33	11

Source: World Bank (2010)

Countries such as Egypt and Malaysia have adopted one-stop shop models, improving business start-up procedures for investors.[9] Based on Figure 10.3, Malaysia seems to be the best ranking amongst the countries selected with respect to ICT laws. This may be attributed to the fact that the country has placed an emphasis in ICT for several years,

especially following the establishment of the MSC (Table 10.6). The business environment, such as the costs of doing business, reliable electricity supply, and the corporate governance framework of local companies, also appears to be favourable in the countries with well developed BPO/ITES sectors.

Other than a large number of well-educated people who are proficient in English, and the time zone, Kenya does not have a competitive advantage over other countries that are also laying emphasis on the BPO sector. Firstly, Kenyan businesses do not have a strong online presence. A World Bank (2007) Enterprise Survey reveals that in Kenya, only 14 per cent of firms had their own websites, which is low when compared to 38 per cent in Egypt[10] and 36 per cent in South Africa.[11] Secondly, Kenya has not defined and marketed its niche market. Kenya, for instance, has some competitive advantage in a number of small-scale sectors, which had been identified earlier. The government should, therefore, consider a two-pronged approach where incentives and strategies can be developed for both small-scale, highly skilled BPOs as well as large-scale players such as those who will be operating within the Technopolis and Special Economic Zones (SEZ).

10.7 Recommendations

Based on the best practices reviewed, this section identifies five priority areas to be addressed:

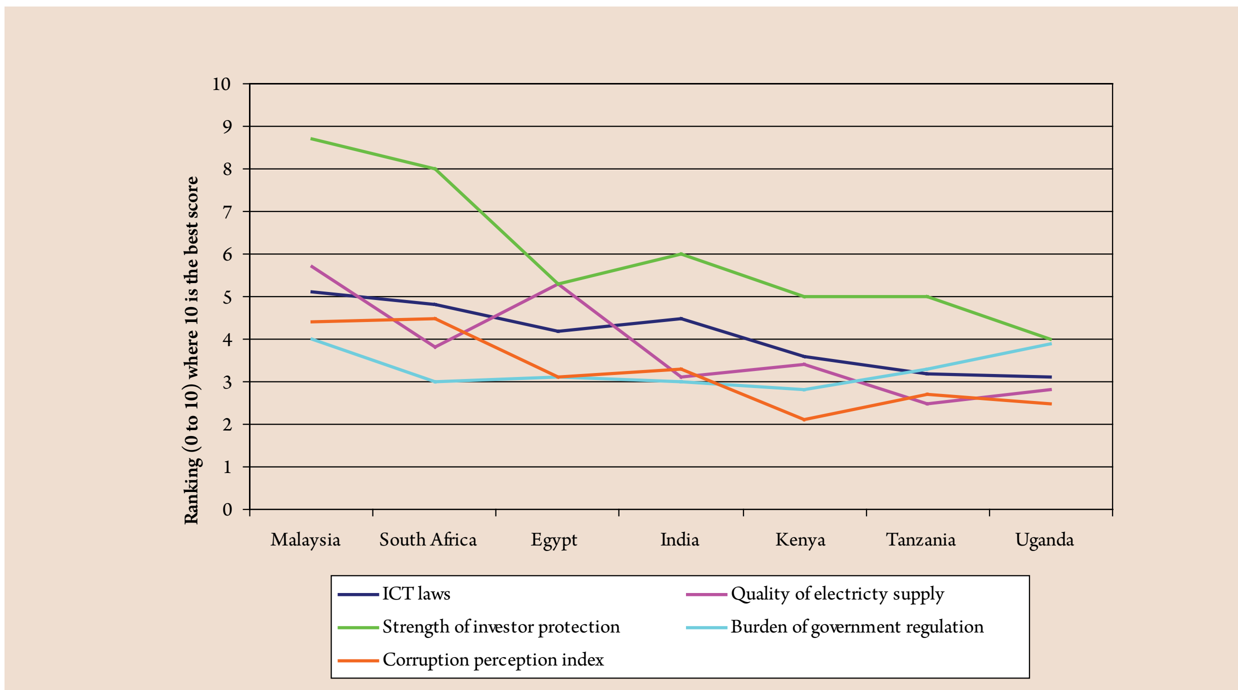
Regulatory Framework: The legal and policy framework should be strengthened to promote the ICT and BPO sector. This can be achieved through the introduction of a BPO sector policy, which addresses BPO incentives, skills and technology development, promotion of local technological capacities by encouraging local purchases, and the promotion of innovation and intellectual property rights.[12] This is to encourage the development of local ICT software, while also improving the uptake of the software locally.

The *Kenya National ICT Policy (2006)* recognizes the importance of establishing an adequate legal framework to deal with network security and cyber crime, and recommends the development of an e-security structure. The policy paper also indicates that e-business should be supported through appropriate legislation such as data protection, as the Copyright Act cannot effectively address this. Kenya provides for electronic fraud in the Kenya Information and Communications Act (Cap 411A). However, the penalty may be considered punitive considering the possible gains from fraud.[13] A strong minimum penalty should, therefore, be provided. The penalties for the unauthorized use of electronic signatures or for unauthorized access to protected systems is stiffer[14] but a minimum is also not provided; it is subject to the courts. There are additional aspects that the law is silent on, such as virus dissemination and network interference (aspects of cyber crime).

The employment law should also address the issue of working and rest hours, which will be applicable to the BPO industry. Currently, the law states that "An employer shall regulate the working hours of each employee in accordance with the provisions of this Act and any other written law" (Employment Act 2007, Section 27). The law goes on to state that the Minister for Labour, after consultation with the National Labour Board, can make rules prescribing for the maximum number of hours during which an employee may be required to work, and the intervals to be allowed to them for meals and rest (Section 91 of the Employment Act 2007). These regulations have, however, not yet been introduced. It would be important to have provisions that specifically address the BPO industry.

The Business Environment: The government should introduce a one-stop shop, which would assist investors in obtaining all the necessary business registration and licensing requirements. As illustrated in Figure 10.3, the business environment must be conducive to the development of the BPO sector, just like any other business. As indicated earlier, investors have to physically visit numerous

Figure 10.3: Business and regulatory environment in selected countries



Source: World Economic Forum (2010; 2011); World Bank (2011) and Transparency International (2010)

regulatory authorities to get the necessary requirements. A study by McKinsey *et al.* (2009) recommends that KenInvest should formalize its role as a one-stop shop. If this recommendation was adopted, it would improve the business environment. Countries such as Egypt and Malaysia have done so successfully. Another option for the government to improve the business environment for BPOs would be to introduce phased out incubation centres for start-up BPO companies for the initial three years (Waema *et al.*, 2009).[15]

Capacity Building: As indicated in several reports and studies, Kenya has a large and educated workforce that is also proficient in English. However, this may not be sufficient from BPO sector perspective. The BPO/KPO Skills Assessment Report for Kenya (2010) established that the industry lacks personnel with soft skills and specialized skills. The Ministry of Information and Communications should support comprehensive capacity building and training that deals with various relevant and emerging areas, such as those identified in the report, and including writing skills, telephone etiquette, Internet marketing and customer service. This is important as Kenya will be dealing with very developed and sophisticated international markets which have mastered the discipline of customer service. A key finding of the study undertaken by Waema *et al.* (2009) is that culture and quality were key aspects that foreign companies that are outsourcing look for. The capacity building programmes should, therefore, lay emphasis on quality customer service experience. The BPO/KPO Skills Assessment Report for Kenya recommended the strengthening of linkages between industry and academia as one mechanism through which BPO/ITES career guidance can be enhanced. To support already existing BPOs to develop their human resource, the government should also provide BPO/ITES training grants.[16] Companies providing BPO services should also be provided with support to develop interactive and dynamic websites.

The presence of strong supportive BPO Associations is important. The government should, therefore,

provide support to the Kenya Business Process Outsourcing and Contact Centre Society, as is the case in South Africa where the government provides the BPO Association with financial support to enable it to effectively support and represent the growing sector.

Development of Skilled Niche Markets: This chapter proposes for Kenya to develop and niche markets offering highly skilled and specialized services in sectors such as finance, human resource, accounting, software development, design and travel and tourism. Comparative advantage is already existing in most of these industries. This means that training should be provided to these calibers of businesses to improve their competency and ability to export their services overseas. One important area that should also be addressed is 'internet marketing'. Companies with online presence would be in a better position to get business contracts even through 'online marketplaces' and online content development. The role of the government is to provide such businesses with investment grants, capacity building support, export market assistance, and institutionalize skills training into tertiary education.

Development of the Technopolis: In the development of the Konza Technology City, the following five key factors should be considered: (i) a clear understanding of the implications that this development will have on the local environment and appropriate safeguards put in place that can also deal with e-waste; (ii) development of appropriate Public Private Partnership (PPP) regulations for the technopolis, which should be considered as the Public Private Partnership Bill is being developed; (iii) a one-stop shop modality adopted to make business start-up and operation procedures easier. An appropriate model that provides the working modalities of regulatory agencies should be established; (iv) a state of the art technology to attract investors and to facilitate development of the BPO/ITES sector in Kenya; and (5) regulations to provide incentives especially to support local investors at the technopolis.

ENDNOTES

1. The increase in bandwidth charges to 256 Khz bandwidth from Ksh 88,526 in 2008 to Ksh 120,000 in 2009 (Figure 10.2) is likely to be due to the increase in demand, as this is the most subscribed bandwidth.
2. The Gazette notice dated 16th December 2009 provided members, the functions and the terms of the BPO/ITES Working Group as two years. However, in a Gazette notice dated 23rd December 2011, the term of the BPO/ITES Working Group was extended by one year.

   Accessible from http://www.konzacity.co.ke/?page_id=2193
3. Information obtained from EPZA.
4. Visit www.konzacity.co.ke
5. One of the goals for the financial sector in Vision 2030 is promoting Nairobi as a regional financial centre. To this end, the Minister for Finance, through a Gazette notice dated 10th December 2010, established a Steering Committee for the Nairobi International Financial Centre (NIFC).
6. They include Elance Online, Rent a Coder, Odesk, Guru.com, eWork, to name a few.
7. See the 2007 report by the Working Committee on Regulatory Reforms for Business Activity in Kenya.
8. Statistics available from World Bank's Doing Business project at http://www.doingbusiness.org/.
9. Egypt has the General Authority for Investment and Free Zone (GAFI) indicated in Table 10.7, where an investor can establish a business and obtain the necessary licences all in one stop, while the Malaysia set up is a one-stop shop hosting company registries, their revenue authority and the pension and social agencies (World Bank, 2009). Additionally, investors in the MSC can get information from the Multimedia Development Corporation MDeC (www.mdec.my).
10. This figure is likely to have improved significantly given the implementation of the Free Internet Initiative launched in 2002.
11. The results are based on firm-level surveys undertaken in 2008 (Egypt) and 2007 (Kenya and South Africa). The data is available from www.enterprisesurveys.org.
12. See policies in place in South Africa and India, summarized in Table 10.7.
13. The Act provides a maximum fine of Ksh 200,000 and/or imprisonment for a term not exceeding three years but does not provide a minimum.

14. The maximum fine is not exceeding Ksh 1 million and imprisonment for a term not exceeding five years.

15. Lessons can be drawn from India's Technical Incubation and Development of Entrepreneurs (TIDE) Schemes.

16. South Africa provides training support grants as illustrated in Table 10.7.

Chapter 11

Financial Services

11.1 Introduction

The financial sector plays an important role in the economic development process in the country. Financial institutions are the main intermediation channels between saving and investment in the economy. A sound and efficient financial system is, therefore, critical for attaining broad-based economic growth as envisaged in Vision 2030. As at 31st December 2010, the sector comprised 43 commercial banks (30 locally owned and 13 foreign owned), one mortgage finance company, 5 deposit-taking microfinance institutions and 126 foreign exchange bureaus. In the same period, there were 46 licensed insurance companies and two locally-incorporated reinsurance companies. 22 insurance companies engaged in non-life insurance business only, 9 engaged in life insurance business only, while 14 were composite (both life and non-life). Other insurance intermediaries and insurance service providers were 163 licensed insurance brokers, 23 medical insurance providers (MIPs) and 4,223 insurance agents. Other insurance players included 120 investigators, 80 motor assessors, 21 loss adjusters, 2 claims-settling agents, 10 risk managers and 26 insurance surveyors. While the Nairobi Securities Exchange continued to be the only stock market, there were 3,280 active SACCOs with total assets worth about Ksh 216 billion.

The financial sector continued playing its intermediation role, recording significant improvements. The sector expanded by 8.8 per cent in 2010 compared to a growth of 4.6 per cent in 2009. However, the sector's contribution to GDP increased marginally to 5.6 per cent from 5.5 per cent in 2009.

11.2 Policy Changes

Several policy changes were witnessed in the sector. To strengthen the regulatory oversight of the financial sector, the Capital Markets Authority (CMA), the Insurance Regulatory Authority (IRA) and the Retirement Benefits Authority (RBA) were legally allowed to share information between themselves. The move is expected to curb risks and shocks within the financial system.

Governance of the insurance industry was enhanced when the functions of the Insurance Regulatory Authority (IRA) were extended to include the issuance of supervisory guidelines and prudential standards from time to time. To improve supervision of the insurance industry in the East African Community, insurance regulators signed a pact. The Memorandum of Understanding (MoU) provides for mutual assistance and exchange of information under member states' respective legislations. The MoU will also protect policy holders; promote the

integrity, stability, efficiency of the industry; and enhance movement of services under the EAC Common Market.

In the capital market, the Capital Markets Authority (CMA) amended the relevant legal framework to facilitate demutualization of the Nairobi Stock Exchange (NSE) by separating ownership and trading rights within 3 years of the passage of the proposed amendment. Demutualization of the NSE is expected to increase efficiency of the market. Further, to boost investor's confidence, CMA also issued guidelines requiring stockbrokers, investment banks and fund managers to publish their balance sheets.

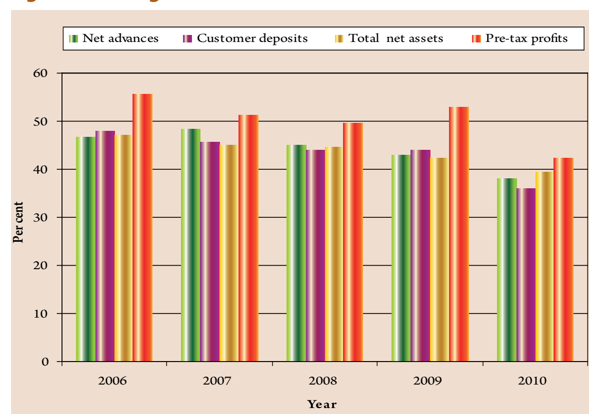
As a step towards agency banking, the Central Bank of Kenya issued new regulations that allow banks to provide a number of services through contracted third parties. Eligible applicants as agents include companies, societies, cooperatives, state corporations, trust funds and public entities. The agency banking model was also extended to deposit-taking microfinance institutions. Introduction of agency banking will lower banking costs and increase access to financial services. Further, the Central Bank of Kenya, in collaboration with the Kenya Bankers Association, rolled out the credit information sharing initiative. Banks can now share credit information on their customers, which is critical in facilitating better assessment of the risks associated with prospective borrowers. The credit information framework will also allow banks to extend credit to customers on the basis of information capital. Finally, the Association of Microfinance Institutions of Kenya (AMFI) adopted rules designed to govern and promote accountability among its members.

11.3 Banking Sector Indicators

11.3.1 Market Share

As at 2010, the banking sector had 43 commercial banks. Figure 11.1 shows the share of the four largest banks on net advances, customer's deposits, total net assets and pre-tax profits. Since 2006, the market share of the four banks on the selected indicators has been declining. The share on pre-tax profits has nose-dived from over 50 per cent in 2006 to about 42 per cent in 2010. This indicates growing competition in the sector as large banks continue to lose their market share. Overall, the sector continued to expand with profitability, total assets and total deposits increasing by 51.9 per cent, 24.4 per cent and 22.8 per cent, respectively, in 2010.

Figure 11.1: Big banks market share



Source: Central Bank of Kenya (2010)

11.3.2 Access to Banking Services

The continued uptake of mobile financial services led to a rapid and massive up-scaling of financial services in Kenya. As at December 2010, 15 million Kenyans were enjoying mobile financial services. Mobile money transfer providers in the same period were four: M-Pesa, Airtel Money, yuCash and Orange Money. Other mobile money solutions include: M-kesho, Mobicash, Elma, Pesa-Pap and Pesa-Connect. Mobile phone money transfer service transactions increased by 100.8 per cent from 125.1 million transactions in the year to June 2009 to 251.2 million transactions in the year to June 2010. Further, the Central Bank of Kenya rolled out the agent banking model for commercial banks and, as at 2010, 8,809 agents had been appointed across the country. This is a boost towards financial inclusion, given that about 32.7 per cent of the population uses no formal or informal financial services, while 26.8 per cent uses informal financial services.

Commercial banks continued expanding their branch networks both nationally and across the East African region. The national branch network expanded from 996 in 2009 to 1,063 in 2010. This was about 7 per cent increase. Population per branch in 1999 and 2010 is shown in Table 11.1. Except for Eastern Province, outreach has declined; meaning that the number of people in a province per branch has increased over time. Nairobi Province has the best outreach, while North Eastern Province continues to have the poorest outreach. However, with the agency banking taking off, outreach is expected to improve. Also, the growth of Islamic banking is expected to increase outreach especially in North Eastern Province. Banks also continued to use ATMs and Internet to expand provision of their services. The number of ATMs grew by 15.3 per cent from 1,717 in 2009 to 1,979 in 2010.

Table 11.1: Branch network and population[1] per branch

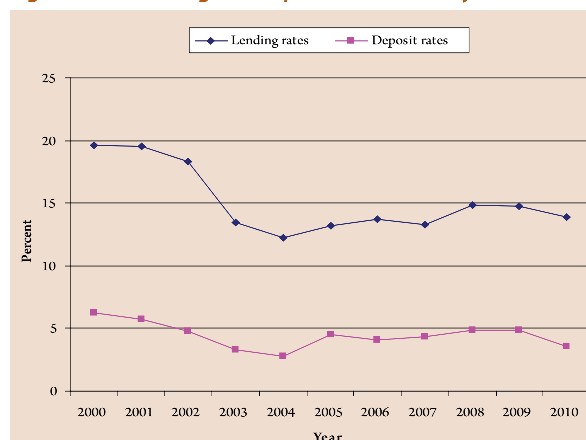
Province	Branches (2010)	Population per Branch (1999)	Population per Branch (2010)	% Change
Central	115	32,458	41,356	27.4
Coast	135	22,580	26,391	16.9
Eastern	91	63,881	62,979	-1.4
Nairobi	411	77,94	7,945	1.9
North Eastern	18	74,400	154,051	107.1
Nyanza	70	53,954	78,880	46.2
Rift Valley	175	37,742	64,146	70.0
Western	48	94,259	111,135	17.9

Source: Central Bank of Kenya, Kenya National Bureau of Statistics and authors' calculations

11.3.3 Cost of Credit

The average lending rates marginally reduced from 14.8 per cent in 2009 to 13.9 per cent in 2010. Average deposit rates also dropped from 4.84 per cent in 2009 to 3.59 per cent in 2010 (Figure 11.2). This implies that commercial banks lower deposit rates when they reduce the lending rates. The motive is to maintain the banks' income levels unchanged since interest income forms a large proportion of their income.

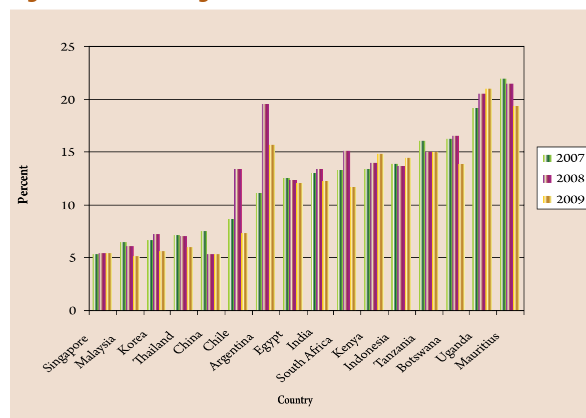
Figure 11.2: Lending and deposits rates in Kenya



Source: Central Bank of Kenya (2010a)

In the period 2007-2009, lending rates in Kenya were higher when compared to middle income countries (Figure 11.3). Kenya's lending rates increased, while in Singapore, Malaysia, Korea, Thailand, Chile, Egypt, India, South Africa, Botswana and Mauritius, the rates declined. Lending rates in Singapore, Malaysia, Korea and China were as low as 5 per cent. However, with the introduction of credit reference bureaus in Kenya, customers with good credit history are likely to benefit from lower lending rates.

Figure 11.3: Lending rates for selected countries



Source: World Bank (2010)

Interest rate spread across selected countries for the period 2006-2007 is shown in Figure 11.4. Countries such as Korea, Chile, Malaysia, China, South Africa, Indonesia, Singapore and Egypt had an interest rate spread of below 6 per cent. Kenya's interest rate spread was higher, averaging 8.5 per

cent. The rate has continued to remain at the same level mainly because commercial banks compensate the reduction in lending rates by also reducing the deposit rate. A high interest rate spread is a pointer of inefficiency in the banking sector and is a key challenge and an impediment to realization of Vision 2030 growth goals.

11.3.4 Credit to the Private Sector

Kenya's commercial banks' credit to the private sector has been on the increase albeit on a slow rate. The credit increased from 38.6 per cent of GDP in 2006 to 40.6 per cent of GDP in 2008. In the period 2006-2008, the credit averaged 39 per cent of GDP. However, this compares unfavourably with countries such as South Africa, China, Thailand and Malaysia, whose credit level is above 100 per cent of GDP (Figure 11.5).

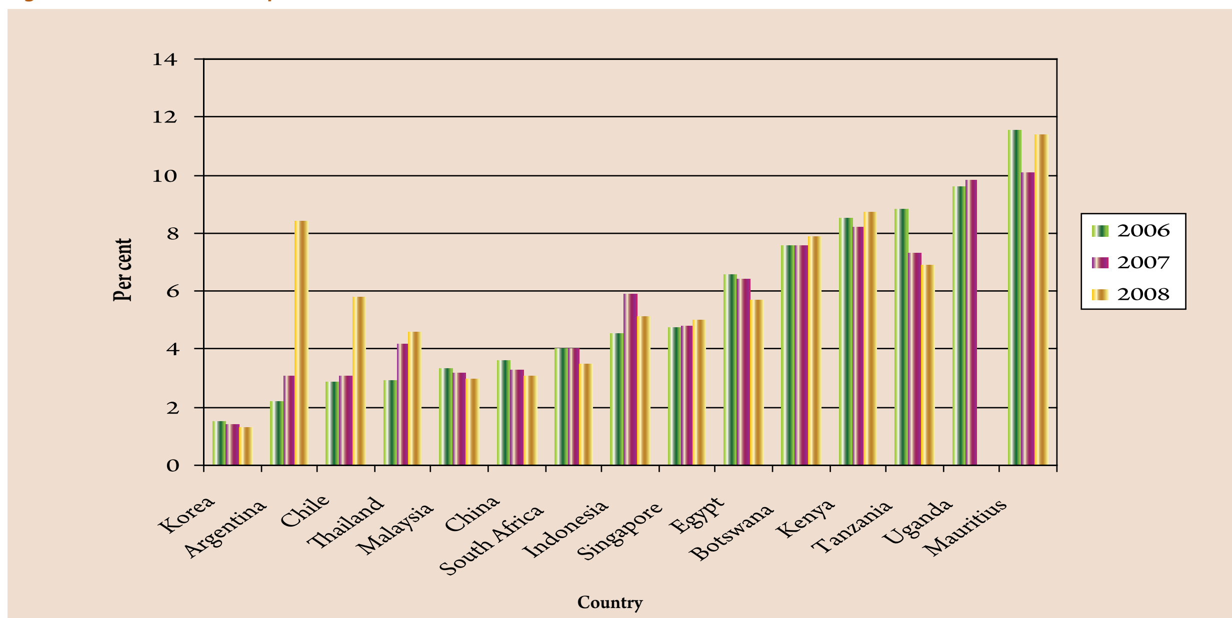
11.3.5 Non-Performing Loans

There has been remarkable improvement in levels of non-performing loans (NPLs) in Kenya. While gross loans increased by 20.7 per cent from Ksh 757.9 billion in 2009 to Ksh 914.9 billion in 2010, the ratio of NPLs to gross loans reduced to 6.3 per cent in 2010 from 8 per cent in 2009. When compared to other selected countries shown in Figure 11.6, Kenya recorded the best improvement in NPLs. Between 2006 and 2008, the NPLs declined from 21.3 per cent to 9 per cent. This trend is expected to continue especially with the credit reference bureaus commencing operations. This is because banks will be able to assess creditworthiness of clients before issuing loans, therefore reducing the associated risk.

11.4 Capital Market Indicators

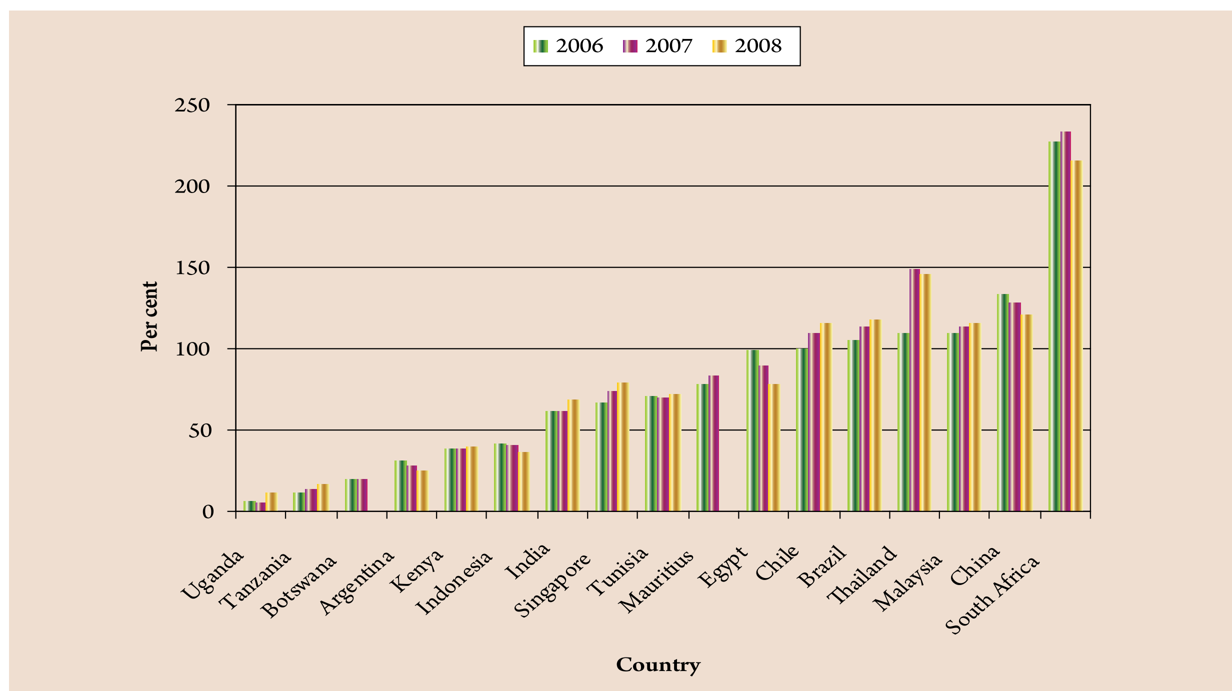
The stock market performance indicators improved in 2010. Though there were no new equity Initial Public Offers (IPOs), lifestyle clothing dealer Deacons Kenya Limited kicked off a Ksh 800 million Public Offer (PO) during the period, raising Ksh 700 million. The company is the first lifestyle brands retailer to raise capital through a PO and is targeting to list at the Nairobi Stock Exchange (NSE). The number of listed companies at NSE continued to be stagnant at 55. Since 2008, this has been the number of listed firms. In 2010, a stock brokerage firm – Ngenye Kariuki Stockbrokers – was placed under

Figure: 11.4: Interest rate spread across selected countries



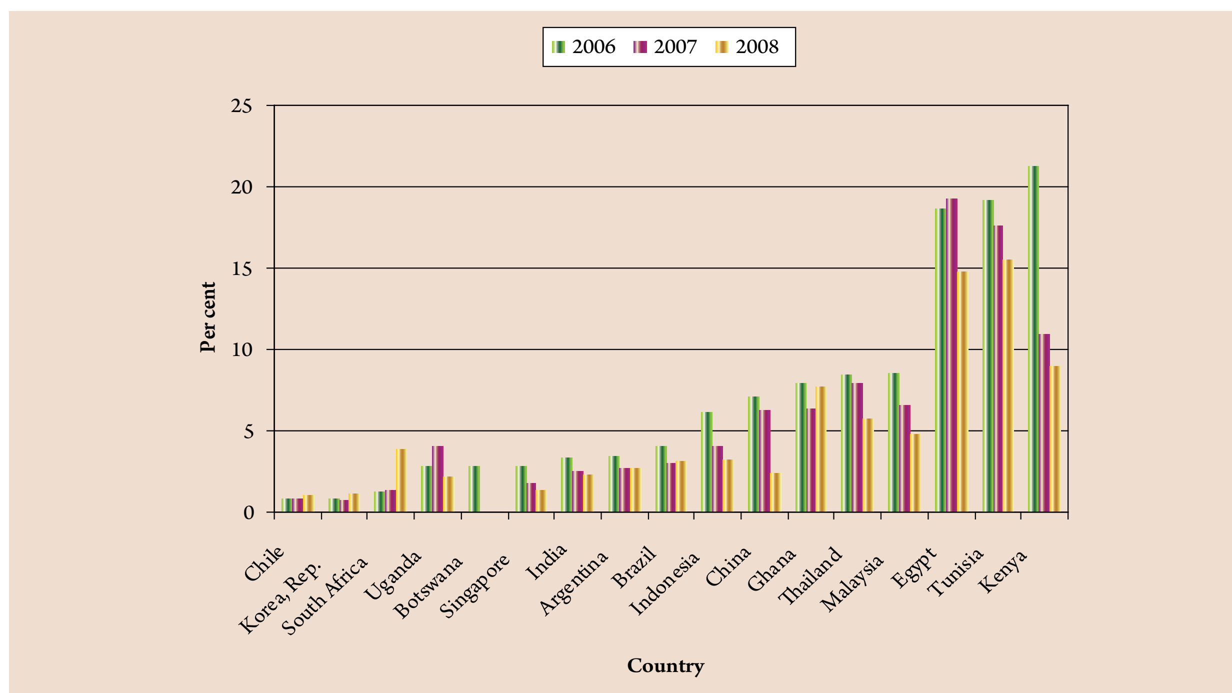
Source: World Bank (2010)

Figure 11.5: Domestic credit to the private sector (% of GDP) for selected countries



Source: World Bank (2010)

Figure 11.6: Non-performing loans for selected countries



Source: World Bank (2010)

statutory management. The firm failed to comply with legal and regulatory provisions of the capital markets. This brings the number of stock brokerage firms troubled so far to four. This continued to erode investors' confidence in the market, and is a critical challenge considering the fact that capital markets are expected to drive mobilization of savings for long-term investments.

11.4.1 Stock Indices

In 2010, the NSE 20 share index increased by 36.5 per cent to close at 4432.6 points from 3,247 points in 2009 (Figure 11.7). This is an indication that the market recovered after a slump in 2008. Similarly, the Nairobi All Share Index (NASI) launched in 2008 increased by the same margin (36.5%) to close at 97.8 points.

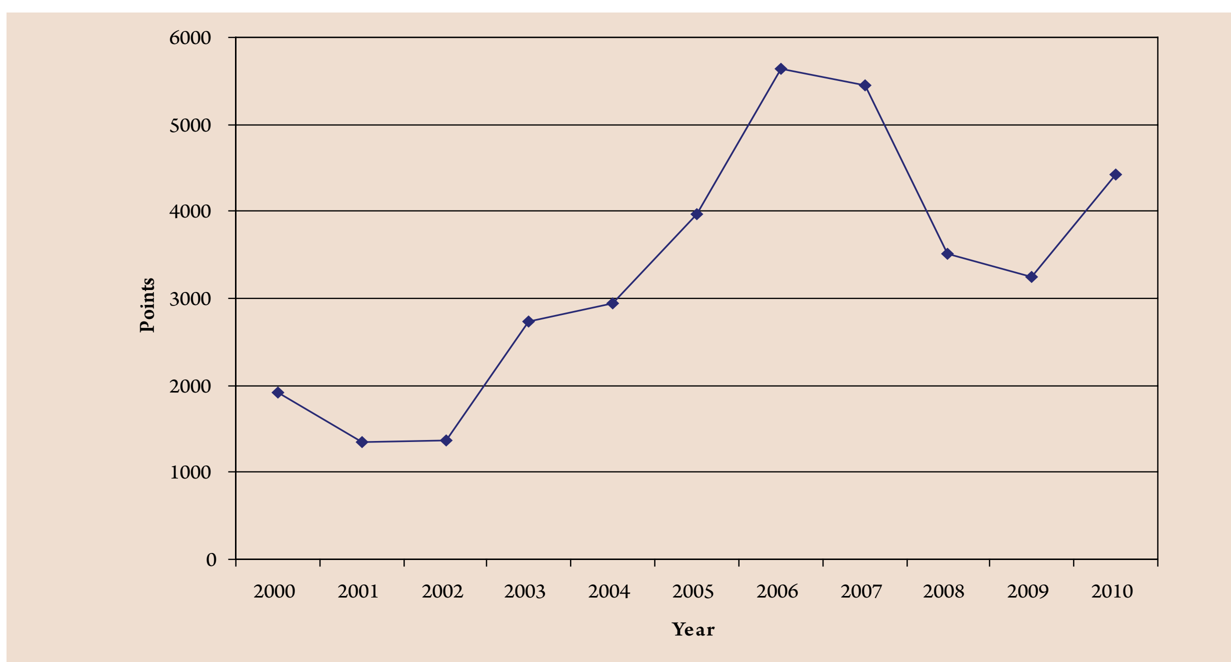
11.4.2 Stock Market Capitalization

The market capitalization also recorded an improvement from Ksh 834.2 billion in December 2009 to Ksh 1,166.992 billion in 2010. This is an increase of 39.9 per cent. However, compared to aspirator countries, Kenya's market capitalization is still small. As a percentage of GDP, market capitalization for Kenya is below 50 per cent while proportions for countries such as Korea, Chile, Malaysia, South Africa and Singapore are 100 per cent and above (Figure 11.8).

11.4.3 Bonds Market

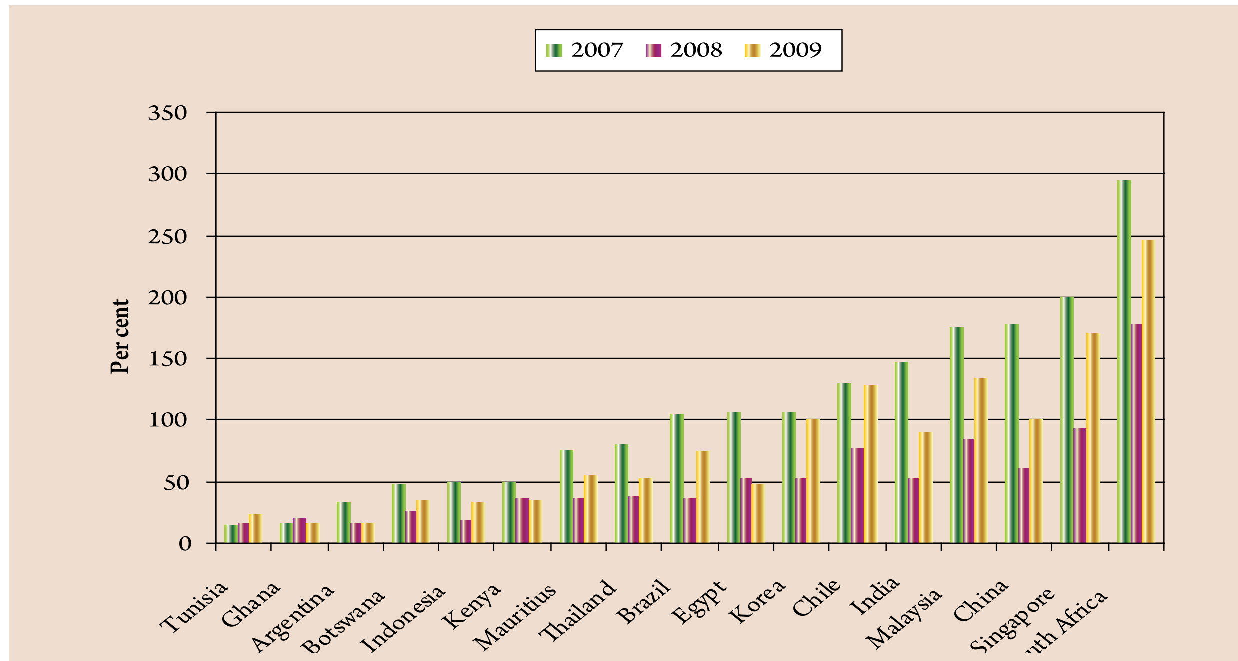
Issuance of infrastructure bonds by the government continued in 2010 when two new bonds worth Ksh 46.1 billion were issued. The corporate bonds market also got a boost when Housing Finance Company issued a Ksh 5 billion bond. The bond had a 41 per cent over-subscription, which raised Ksh 7 billion instead. With approval from the Capital Markets Authority, the Housing Finance Company exercised the green-shoe option, allowing for uptake of more than the target amount. Similarly, the Central Bank of Kenya's 10-year Treasury bond was over-subscribed by 161 per cent, against a target of Ksh 15 billion. This is a sign of the existence of huge potential in the domestic market to raise capital.

Figure 11.7: Nairobi Stock Exchange 20 share index



Source: Government of Kenya (2010b; 2011)

Figure 11.8: Stock market capitalization (%) of selected countries



Source: World Bank (2010)

Following the automation of bonds trading at the Nairobi Stock Exchange, all Treasury and corporate bonds listed on the NSE are now immobilized and traded through the automated trading system. Consequently, the settlement period has reduced from eight days to three days. Liquidity in the debt market is, therefore, expected to increase.

11.4.4 Other Financial Institutions

Microfinance institutions (MFIs) targeting the low-income population continued to complement the efforts of financial access. As at 2010, the Central Bank of Kenya had licensed five MFIs as deposit-taking microfinance (DTM) institutions, namely, Faulu Kenya, Kenya Women Finance Trust, Uwezo, SMEP and Remu. Two of the DTMs had commenced operations with a network of 37 branches. Deposit mobilization by the two institutions was Ksh 6.1 billion, while the total loan portfolio was valued at Ksh 14.2 billion. The total number of active deposit accounts and loan accounts were 1 million and 0.6 million, respectively. More deposit-taking MFIs are expected to be licensed, and this will intensify microfinance outreach in the country.

In the cooperative sector, the Sacco Societies Regulatory Authority (SASRA) became fully operational and commenced the process of licensing SACCOs operating front office services. As at 2010, the Authority had received about 90 licensing applications. Close to 215 SACCOs operating front office services are expected to be licensed. However, the inherent weak governance practices in SACCOs have hampered the speed of compliance to licensing requirements. But once the SACCOs are under the supervision of SASRA, the problem of weak governance is expected to be addressed.

There were 46 licensed insurance companies as at the end of 2010. Twenty two (22) companies wrote non-life insurance business only, 9 wrote life insurance business only, while 14 were composite (both life and non-life). The industry's gross written premium grew by 22.7 per cent from Ksh 64.47 billion in 2009 to Ksh 79.10 billion. Non-life insurance contributed about 66.2 per cent of the total premium. Profit increased by 79.5 per cent from Ksh 4.29 billion in 2009 to Ksh 7.70 billion in 2010. The industry witnessed developments geared

towards increasing penetration. Islamic products by Gulf African and First Community Bank (FCB) were launched. These new Shariah-compliant products and services are expected to cater for the Muslim community, which has hitherto been left out by an industry offering conventional products that do not conform to Muslims religious beliefs. This is expected to intensify competition in the insurance industry. Micro-insurance products covering livestock and crop insurance covers also deepened with the introduction of additional products by insurance companies. This is expected to increase penetration of insurance, which remains low at 3 per cent. Thus, the challenge of enhancing uptake of insurance services continues to exist.

The pensions industry continued to grow, with savings estimated to be about Ksh 451 billion in 2010. The National Social Security Fund (NSSF) accounts for the lion's share of membership (0.9-1.2 million), with savings worth about Ksh 104 billion. To increase penetration, especially in the informal sector, the industry's regulator, the Retirement Benefits Authority (RBA) is adopting mobile phone technology, which is expected to bring onboard millions of people without any savings plan for old age.

11.5 Policy Options

11.5.1 Reduce Cost of Credit

In order to expand financial access and address the cost of financial services in Kenya, there is need to embrace financial literacy. This is an important intervention tool for increasing financial access and consumer protection. Financial literacy can contribute to transparency, competition and access to financial services by reducing information asymmetry. An informed consumer, besides being aware of financial products, is able to compare terms and conditions of suppliers of financial services and shop around, thus giving incentive to competition. Also, as the complexity of financial products increases, it is imperative to empower consumers so that they can assess inherent risks in innovative products. This does not only protect consumers but would also foster stability of financial systems. Public-private sector collaboration can be an efficient way of realizing financial literacy. The Central Bank of Kenya should take the lead towards this goal.

Enforcing the recently-enacted Competition Act will also help reduce the cost of credit in the country. Since the Act is supposed to enhance competitive behaviour, its enforcement will protect consumers from unfair and misleading market conduct. The Competition Authority should be fully facilitated to enable it perform its mandate effectively.

Further, putting in place an integrated property information system will remove the information asymmetry problem in the credit market as well as solve the existing collateral issues.

Ensuring a stable macroeconomic environment, including achieving low level of inflation is also key. Consistently, low inflation leads to lower interest rates and a lower interest positive spread.

11.5.2 Restore Confidence in the Stock Market

There is need to restore confidence in the stock market. As evidenced by over-subscription in the recent issues of bonds, investors are willing to invest where returns are assured. Efforts to continue strengthening the supervisory role of CMA need to be sustained. This should be coupled with effective enforcement of the Capital Markets Act to stem vices of poor governance in the industry. Further, CMA needs to enhance the education campaign on capital markets and also sensitize the public on reforms undertaken in order to boost investor confidence.

11.5.3 Strengthen Governance in the Insurance Industry

To enhance the uptake of insurance services, it is important to strengthen governance in the insurance

industry. To complement the supervisory role of IRA, there is need to legally recognize the role of Association of Kenya Insurers (AKI), Association of Insurance Brokers of Kenya (AIBK) and the Insurance Institute of Kenya under the Insurance Act. Such a move will be crucial to stem out vices of poor corporate governance and money laundering, to which the industry is potentially vulnerable.

ENDNOTES

1. This is based on the 1999 and 2009 population censuses.

Chapter 12

Environment and Natural Resources

12.1 Introduction

The environment has a very significant role and influence on Kenya's social and economic development. Approximately 80 per cent of Kenyans depend on natural resources for their livelihoods and household income. The foundation of the national economy is based on natural resource assets such as land, forests, water, fisheries, wildlife and air. However, evidence demonstrates that these key assets are being degraded at alarming rates. For instance, the rate of deforestation is estimated at 3.2 per cent per annum. At such a rate, in 25 years, no viable forest cover will be available. Sustainable exploitation and management of the key natural resources for the country is critical towards realization of economic growth and poverty reduction, and thus better livelihoods for all Kenyans.

Kenya's long-term blueprint for economic growth and development – Vision 2030 – aims at ambitious targets for economic growth of 10 per cent and poverty reduction across all sectors and socio-economic groups. Such growth rates will immensely assist in meeting the MDGs for Kenyans by 2015. However, the unsustainable use of natural resources and their degradation makes it increasingly difficult to achieve these targets and other national development priorities. Climate change further complicates the pursuit of these national goals and the attainment of MDGs.

Appropriate government policy can enhance the sustainable use and management of natural resources. The inclusion of local communities in the management of natural resources and the environment is also essential for sustainability. Local communities have vested socio-economic interests in the preservation of the environment and the resources upon which they depend for their livelihoods. Involving such local communities in natural and environmental resource management will impart a sense of ownership of such resources in the local community, thus improving their stake in sustainable management.

Kenya's challenge is to find policies that can enhance economic growth, while at the same time preserving the natural resource base. Devising sustainable environmental policies requires an appropriate mix of economic incentives and suitable institutional arrangements based on clear specification of property

rights. Policy makers need to design incentives so that natural resources are priced on an opportunity cost basis; that is, at a level reflecting their replacement costs. That requires, for instance, taking into account the external costs of development projects far more carefully than has been the case in the past, and to translate these costs into realistic market prices.

Reversing the trend of environmental degradation is essential for poverty reduction. The objective of this chapter is to discuss selected environmental resource use trends and challenges with a view to developing strategies and plans towards reversing environmental degradation trends and mitigating the greenhouse gas effect and general ecosystem restoration. The chapter also highlights the key environmental concerns and their economic implications for the country. Where possible, comparisons are made with selected countries in cases where relevant data is available.

12.2 Overview of Sector Performance

Kenya is a mega-biodiversity state with its biodiversity hosted in its various habitats and ecosystems. The latter include forests, grasslands, wetlands, coral reefs and mangroves, among others. However, high rates of population growth and poverty are piling pressure on fisheries, forests, fresh water, and other natural resources that people depend upon for their livelihoods. Additionally, high levels of consumption, waste and environmental mismanagement continue to degrade the country's natural systems and strain the ability to provide crucial environmental services, such as clean air and water to the population.

The country continues to face significant threats of water scarcity, while simultaneously experiencing high levels of population growth. Declining availability of fresh water threatens well-being. Urbanization and freshwater scarcity all pose challenges for policymakers in the country. Urbanization can have both positive and negative effects. As people increasingly move to cities, they have higher incomes, improved access to services and improved living standards. Urban centres produce concentrated amounts of solid waste, sewage and air pollution, as well as increased demand for energy and other resources. The rapid growth in urban areas could overwhelm infrastructure and governments' regulatory mechanisms for dealing with the side effects of growth.

The clearing of forests creates threats to human and ecological health and meeting the needs of a growing population often requires some form of land-use change, such as clearing forests to expand food production. These changes have environmental repercussions. Deforestation, for example, can exacerbate the frequency and severity of floods.

Deteriorating environmental conditions associated with expanding agriculture and deforestation pose threats to human health; for example, deteriorating water quality can contribute to the spread of communicable diseases.

Land

The growing population is increasingly putting pressure on land resources. The increased demand for food and fuel-wood by the population is expected to continue, posing a major threat to existing forest resources. The harvesting of trees for charcoal has moved to more ecologically-fragile areas, especially water catchments and rangelands. As the natural vegetation is destroyed through soil erosion and degradation, the ecological conditions are changed, affecting the livelihoods of people and their survival. The challenge lies in reducing reliance on fuel-wood sources and adopting intensive farming systems. To improve crop production, it is necessary to strengthen environmentally-favourable agricultural practices such as organic farming, environmentally-safe irrigation, horticultural practices and safe use of agro-chemicals. There is also need to assess risks in the application of biotechnologies in the development of crop varieties, livestock breeds for

higher yields, resistance to pests and diseases, as well as drought tolerance.

The rising human population has also put pressure on arable land, leading to encroachment on national parks, causing conflict between people and wildlife. The Kenya Wildlife Service (KWS) is promoting mutual beneficial relations with communities living near parks to reduce human-wildlife conflict.

Energy and Air Pollution

Over 80 per cent of urban household needs for energy are met by charcoal, with Nairobi consuming around 91,000 tonnes annually, equal to 900,000 tonnes of wood. This leads to a lot of air pollution. Other air pollution comes from vehicles, industrial emissions and the open burning of waste. As a result, there are high levels of particles or particulates, which are linked with breathing difficulties and heart problems.

Water Resources

In Kenya, only an estimated 57 per cent of households have access to safe water, while 81 per cent have access to sanitation services. In Nairobi, over 80 per cent of households have access to safe water, but this overides the fact that residents of informal settlements spend an average of eight hours daily searching for water. The urban poor pay 5 to 20 times more than the rich to obtain safe drinking water.

Before the Water Act 2002, the water sector faced many shortfalls that the government is currently reversing. The Act provides a legal framework that separates the management of water resources from water supply and sewerage services.

New Water Supply and Management Strategies

Authority over the water sector has now been decentralized to actors operating at different levels, from the Ministry in charge of water affairs right down to the consumer. Executive authority is also devolved to new institutions: Water supply and sewerage to the Water Services Regulatory Board (WSRB) and water resources to the Water Resources Management Authority (WRMA). The Water Act 2002 further provides for regulation of water provision services, which can only be undertaken under the authority of a licence to service providers.

The WSRB is responsible for regulating water and providing sewerage services, including issuing licences, setting service standards and guidelines for tariffs and prices, and providing mechanisms for handling complaints. Responsibility for the provision of water services is vested in Water Service Boards (WSBs) under the regulation of the WSRB. However, direct provision of water services is undertaken by water services providers that operate as licensees of the water service boards. These service providers may be community groups, non-governmental institutions or autonomous entities formed by local authorities. The WRMA has developed rules to guide the management of water resources in Kenya, with tough penalties for groups that misuse rivers and other water bodies.

The water reforms have, however, faced a number of challenges. The principle of decentralization of water resources management and water provision introduced by the Water Act of 2002 is one major challenge due to lack of adequate capacity at regional and local levels, leading to decreased effectiveness of devolved bodies in some areas (Mumma, 2007). In addition, there is need to determine how these decentralized bodies will work in the new county structure proposed by the Constitution.

The challenge of climate change cuts across all the sectors of the environment, from forestry, water, wildlife, marine ecosystems to mineral resources. The government has recognized climate change as a critical driving factor for major sectors of the economy. This has led to numerous efforts being directed towards dealing with the effects of climate

change. The government has developed the National Climate Change Response Strategy (NCCRS) meant to help the country respond to challenges climate change posses to socio-economic development. NCCRS is the government's 'blue print' document that outlines actions necessary to mitigate and adapt to climate change. The MTP (2013-2017) has also emphasized the need to mainstream climate change across all government programmes.

12.3 Forest Resources

Forest resources play a significant role in the national economy. Forests have a direct role in supplying the country's domestic energy requirements in the form of wood fuel and charcoal. However, this fact is never captured aptly in national economic surveys since petroleum-based products are viewed as the key drivers of the economy (Government of Kenya, 2009). Moreover, forests provide timber, poles (for fencing and power transmission) and a myriad of other non-timber forest products. Their contribution is even more when it is taken into account that they provide direct employment and livelihood opportunities in both rural and urban areas. Indirectly, forests act as carbon sinks, are reservoirs of biodiversity and keep land productive by conserving soil and water, act as water catchment areas, recharging rivers and dams for supplying drinking water and hydro-electric power generation.

Despite the immense contribution of forests, their existence continues to be threatened. Extensive reduction in the forest cover has been witnessed in the country over time (Table 12.1).

Table 12.1: Trends in forest cover

	Area ('000Ha)			
	1990	2000	2005	2010
Indigenous closed canopy	1,240	1,190	1,165	1,140
Indigenous mangroves	80	80	80	80
Open woodlands	2,150	2,100	2,075	2,050
Public plantation forests	170	134	119	107
Private plantation forests	68	78	83	90
Farms with trees	9,420	10,020	10,320	10,385

Source: FAO (2010)

For a long time, the forest sector was constrained by poor governance issues that led to massive destruction of forests and loss of critical biodiversity. Moreover, the increasing population continues to exert more pressure on forests, placing more demand on forest products and services. This pressure has been most severe on the country's five critical water towers covered by natural forests that hold some of the most significant biodiversity in the country. Poor governance was mainly attributed to corruption, policy failures, poor management regimes, low institutional capacity, inadequate community empowerment and devolution of power, poor law enforcement mechanisms, among others.

Attempts to reform the forestry sector date back to 1994 when the Kenya Forestry Master Plan (KFMP) was produced. KFMP is still the most authoritative framework for the forestry sector and the relevant blue print for the sector until today. It calls for an institutional overhaul to pave way for effective management of forest resources in the country. However, political inertia and weak governance have not permitted issues highlighted in the plan to be addressed, though the issues remain pertinent and are echoed in the draft forest policy and the Forest Act 2005.

The government that came into power in 2002 re-energized forest conservation efforts by demonstrating strong political will as evidenced by efforts to give the forestry sector a new legal framework that would include communities in management of forests. To achieve the envisaged inclusion of communities, the new forest policy was completed in 2005 and the new legislation to support its implementation enacted in February 2007. However, the forest policy is yet to be passed by Parliament.

The Forest Act 2005 emphasizes the need to institutionalize the forestry sector. The Act has the following provisions:

- The establishment of a semi-autonomous Kenya Forest Service (KFS) with a broader mandate to cover all forests;
- Increased role and responsibility for local communities and other stakeholders in management of forests;
- Promotion of commercial tree growing (including farm forestry);
- Establishment of a Forest Management and Conservation Fund and drafting of management plans for all forest ecosystems;
- Excision of gazetted forests to require Environmental Impact Assessment and parliamentary approval;
- Management plans for all forests developed by local communities with assistance from KFS; and
- Creation of a professional forestry society, among others.

The reforms in the forestry sector have led to mixed results in as far as the forest cover in Kenya is concerned. While public and community forest lands declined in area, mainly due to excision, private forestry has increased due to increased private sector interest in commercial farming and the expansion of farm forestry in line with the Forest Act 2005 (Table 12.1). With regard to ownership, most forests in Kenya are either in public ownership (managed by KFS and KWS) or owned by local communities (and managed in trust lands by local authorities, Table 12.2).

Table 12.2: Categories of forest ownership in Kenya

Categories of Ownership	Forested Area (1000Ha)			
	1990	2000	2005	2010
Public ownership	1,490	1,404	1,364	1,364
Private ownership	2,218	2,178	2,158	2,103
…of which owned by individuals	1	2	5	10
…of which owned by private business entities and institutions	67	76	78	80
…of which owned by local communities (includes trust land forests managed by local authorities)	2150	2100	2075	2013
Total	**3708**	**3582**	**3522**	**3467**

Source: FAO (2010)

The comprehensive institutional, legal and policy reform processes currently going on in the sector are expected to open up major opportunities to address the challenges of the past and to improve the quality and sustainability of Kenya's forests, trees and woodlands.

Even though most of these reforms are still at an early stage, notable achievements that have already been realized include the success of the new legislation in stopping excisions, and the government's efforts in barring settlements in the Mau Forest complex. There is a lot of optimism that there will be greater morale and incentives to drive the reform agenda forward. On the surface, this may look like a done deal. However, there are challenges that still limit the degree to which this transformation is successful.

12.3.1 Challenges

i. Establishment of farm and private forests is one of the priority areas with the potential to move Kenya from low forest cover to the international recommended standard of 10 per cent. Unfortunately, the country still lacks a clear systematic inventory of private and farm forests.

ii. With demand for timber products being on the rise, forest plantations are going to be the source of timber production for commercial purposes. The success of this initiative will, to a large extent, depend on availability of up-to-date and accurate inventory relating to forest areas, growth and yields and clearly defined modalities of executing the agreements.

iii. Capacity to undertake the reform process: There is the challenge of institutional cultural change from the *modus operandi* to a business culture expected in the new forest legislation. Besides this, the absence of checks and balances and lack of participation by all stakeholders could derail the process.

iv. Absence of clear mechanisms of coordination among different sectors/agencies on management of forest resources. Different pieces of sectoral laws and policies have components relating to management of forests. Poor mechanisms of consolidating and coordinating these legislations are likely to derail the reform agenda for the sector.

v. There are complexities involved in participatory forest management. Already, communities are expecting unconstrained access to and use of forest resources, an attitude that must be tempered through learning, mechanisms to share costs and benefits, feasibility assessments and pilot testing (World Bank, 2007).

12.3.2 Proposed Interventions

i. Genuine involvement of all stakeholders in management of the forestry sector as stipulated in the Act. Stakeholder involvement is needed in designing clear operational guidelines, objectives and systems to monitor and evaluate impacts. This will ensure buy-in and, therefore, success of the reform agenda.

ii. In spite of the importance of forest and woodland resources, there is no official forest policy in place, and the government must consider it a priority to provide one. This will ensure that genuine partnerships and not self-interest inform participatory forest management approaches, which have been given prominence in the new Act.

iii. Intensive sensitization of stakeholders, especially potential investors, that forestry unlike agriculture, is a long-term proposition will be crucial.

iv. In conformity with the spirit of the Act, KFS in consultation with stakeholders, should prepare guidelines and rules that will ensure true devolvement of certain functions to lower levels of government, that is to the counties.

v. KFS should have proper information and data on the nature and distribution of the various forest types in Kenya. Developing this inventory should be considered a priority.

12.4 Water Resources

Water is an environmental resource for supporting life and sustaining economic activities across different sectors. Kenya faces enormous challenges in the development and management of the limited water resources, and the magnitude and severity of the water crisis cut across most sectors of the economy, making water resources management a high priority that requires urgent attention.

With its natural endowment of renewable freshwater of only 21 billion cubic metres (BCM), which amounts to 647 cubic metres (M^3) per capita per annum under normal circumstances, Kenya is classified as a water scarce[1] country. This compares unfavourably with the neighbouring countries of Uganda and Tanzania, which have per capita levels of 2,940 M^3 and 2,696 M^3, respectively (KIPPRA, 2009). The country's water resources are unevenly

distributed in both time and space in five drainage basins (Table 12.3). Climate change will worsen this already precarious situation as it affects precipitation, thus further altering the spatial and temporal availability of water resources.

Demand for water continues to outstrip the stock of renewable fresh water. The current water supply is inadequate, with only 57 per cent of households using water from sources considered safe. There are disparities in urban water access, with informal settlements recording lower levels. Surface water resources account for 86 per cent while ground water accounts for 14 per cent. Trans-boundary waters constitute 54 per cent of water resources in the country.

There are legal and regulatory frameworks that guide the use of trans-boundary water resources. For instance, the Lake Victoria Tripartite Agreement signed by Kenya, Uganda and Tanzania established the Lake Victoria Environment Project (LVEMP) whose objective is rehabilitation of the Lake Victoria ecosystem. Besides, the Nile Basin Initiative (NBI) provides the basis for cooperation for all riparian countries in the development of water resources of the Basin (NEMA, 2011).

Table 12.3: Major river basins and their potential

Basin Name	Area (M^2)	Mean Annual Rainfall (mm)	Annual Basin Discharge/ BCM
Lake Victoria	46,229	1,368	11.79
Rift Valley	130,452	562	2.91
Athi River	66,837	739	1.29
Tana River	126,000	697	3.89
Ewaso Ng'iro	210,226	411	0.48

Source: NEMA (2011)

Over the last decade, the government has rolled out multiple interventions to address the challenges affecting this sector. Resource allocation to the sector is one positive outcome of such interventions (Table 12.4). Besides resource allocation, the sector is undergoing major institutional reforms. There is a supportive legal and policy framework that is supposed to guide sustainable development of the sector. Vision 2030 and the Constitution of Kenya 2010 have both underscored the importance of water for socio-economic development and spell out strategies to ensure its sustainable utilization, exploitation, management and conservation.

The present legal and institutional framework is anchored on the National Water Policy (1999) and the Water Act 2002. The institutional framework highlights the three-tier pyramidal institutional setup of the water sub-sector, where the Ministry of Water and Irrigation is in charge of coordination, financing and policy formulation, while the Water Services Regulatory Board is the water services regulator. The Water Service Boards are the asset holders and are responsible for efficient service provision in their areas of operation, either through an agent (water service provider company) or directly where there are no agents.

Decision-makers need to be convinced that investment in water, sanitation and sound water resources management drives economic growth, social development and political stability. Water is linked to wider macroeconomic aspects and to the capacity of countries to eradicate poverty and sustain development. Despite this, water's cross-cutting aspects are rarely considered when new policies are developed. There is need for well-balanced decisions in relation to capacity building, institutional development and infrastructure development in the water sector.

12.4.1 Challenges

Renewable fresh water per capita stands at 647 cubic meters and is projected to fall to 235 cubic meters by 2025, if supply does not keep up with population increase. There are also regional imbalances in water availability and utilization that must be addressed.

Provision of water throughout the year presents a major challenge. Inadequate water harvesting is

Table 12.4: Resource allocation for the water sector

Item	2006/07	2007/08	2008/09	2009/10	2010/11*
Water development	3,368.0	4,448.5	9,989.0	13,822.0	21,703.5
Training of water development staff	39.0	40.0	25.0	33.0	26.4
Rural water supplies	814.0	80.0	1,056.7	1,044.8	1,308.7
Miscellaneous and special water programmes	141.5	1,218.0	178.0	216.0	176.7
National Water Conservation and Pipeline Corporation	2,031.5	1,733.5	3,002.2	4,034.2	4,877.0
Irrigation development	442.6	474.4	629.7	487.2	720.9
National Irrigation Board	455.3	420.0	410.0	2,626.7	2,525.7
Total	**7,291.9**	**8,414.4**	**15,290.6**	**22,263.9**	**31,338.9**

Source: Ministry of Water and Irrigation/National Water Conservation and Pipeline Corporation

responsible for regional imbalance in water security, with some parts of the country having a lot of water during rainy seasons and little or no water during dry periods. The challenges are further compounded by extreme climatic changes that cause flooding and immense negative impact on both the social and economic fronts.

The quality of water has deteriorated over time due to increased commercial farming activities, rapid industrialization and laxity in law enforcement. In most cases, effluents and chemical waste from various sources are discharged directly into water bodies. There is also the challenge of infrastructure development; and poor physical planning in urban areas, coupled with the proliferation of unplanned settlements.

According to the MTP 2008-2012, the water sub-sector aims to improve access to safe water and sanitation with the goal of attaining 90 per cent access to safe and reliable water for urban areas and 70 per cent for rural areas and reducing levels of unaccounted-for water to below 30 per cent. It also aims to achieve 70 per cent and 65 per cent access to safe sanitation for urban and rural households, respectively. Given financial, governance and capacity constraints, it will be a tall order to achieve these targets.

There is overwhelming evidence of climate change in Kenya, and one of the apparent signals is the rapid and drastic disappearance of glaciers on Mount Kenya, with scientists projecting that the ice cap on the mountain could disappear by the year 2020. In addition, the country's lakes are experiencing serious declines in water levels. Similar drastic changes have been observed in volumes of river flows. This eminent water scarcity, therefore, poses a serious challenge to the country's economic development, as geothermal power production and its sustainability, for example, is largely dependent on natural water recharge.

12.4.2 Proposed Interventions

Based on the experience gained while implementing the legal and institutional framework, the following interventions are proposed:

- Alignment of the water policy with other sectoral policies, including irrigation, land reclamation, environmental sanitation and hygiene policies, among others.
- Clear classification and adoption of water companies as private or public, with guidelines on their formation and operation developed by the Water Services Regulatory Board and approved by stakeholders.
- Demand management as a priority over supply management so as to promote water use efficiency.

- Need to have a water management information system to collect accurate data on water resources in terms of quantity and quality.

12.5 Fisheries

Kenya has numerous aquatic resources with aquacultural potential. The varied climatic and geographic regions that cover part of the Indian Ocean coastline, a portion of the largest freshwater lake in Africa (Lake Victoria), and several large rivers, swamps, and other wetlands, all support an abundance of native aquatic species. The fisheries sub-sector has the potential to contribute to the national economy through employment creation, foreign exchange earnings, poverty reduction and food security. Lake Victoria produces 90 per cent of the fresh water fish, with the fresh water bodies producing 10 per cent, but production has been decreasing over the years. The fresh water fisheries employs about 35,000 fishers, while marine fisheries employs over 8,000 fishers, with most fisheries coming from Lamu and Kwale. The country earns about Ksh 4 billion (approximately US$50 million) in foreign exchange, and the fishers over Ksh 7 billion, thus contributing to poverty alleviation in rural Kenya.

The government has launched its first ever fisheries policy, which is envisioned to increase income from fisheries to around Ksh 10 billion annually by the year 2014. The National Oceans and Fisheries Policy is currently being implemented.

Challenges

- Degradation of freshwater bodies through waste (chemical, solid, water) that drains into these water bodies. For instance, Lake Naivasha is heavily polluted by effluent from the surrounding flower industries and farming activities upstream.
- Over-reliance on a few fishing sources, mainly in Lake Victoria, leading to over-exploitation and decline in fish stocks.
- Poor infrastructure such as fishing equipment, processing and storage facilities.
- Slow pace of implementation of the recently-launched fisheries policy and lack of stakeholders' involvement in formulating developmental plans that improve the fisheries sector.
- Lack of adequate funding towards the Department of Fisheries by the government to enhance research, production and training in order to improve the sub-sector.
- There is a lot of conflict on various users of fisheries resources especially in Lake Victoria, which is shared among three countries (Kenya, Uganda and Tanzania).

Proposed Intervention

- To integrate the fisheries sector into the country's agriculture sector so as to improve food security.
- To develop and improve infrastructure so as to facilitate increased production and export of fish.
- To develop a clear strategy for implementation of the comprehensive fisheries policy, indicating fisheries as an important sector that needs to be well developed to promote its growth.

12.6 Wildlife Resources

Kenya's wildlife biodiversity provides the base for the tourism industry, research and education. The country's wildlife is found in an area of 4,403,595 hectares (about 8% of land area), gazetted by the

Table 12.5: Quantity of fish produced in metric tonnes, 2006–2010

Quantity in Metric Tonnes	2006	2007	2008	2009	2010
Freshwater fish					
Lake Victoria	143,908	117,231	111,369	108,934	113,041
Lake Turkana	3,097	5,122	8,070	9,445	8,123
Lake Baringo	39	73	225	688	693
Lake Naivasha – Commercial	120	203	262	191	198
Lake Jipe	75	96	109	109	111
Rivers and dams	984	393	1,302	584	596
Fish farming	1,099	4,245	4,452	4,895	12,153
Others	861	313	883	828	869
Total	**151,711**	**127,676**	**126,672**	**125,674**	**135,784**
Marine fish by district					
Lamu	1,309	1,801	2,028	2,181	2,289
Tana River	55	163	89	95	105
Malindi	1,192	1,160	1,345	1,289	1,387
Kilifi	435	729	817	857	859
Mombasa	1,225	680	676	712	700
Kwale	1,750	1,822	2,606	1,890	2,260
Total	**6,023**	**6,355**	**7,561**	**7,024**	**7,600**
Crustaceans by district					
Lamu	23	159	151	97	149
Tana River	97	134	42	27	43
Malindi	0	93	71	57	76
Kilifi	445	29	25	18	13
Mombasa	55	123	192	127	197
Kwale	55	80	97	81	71
Total	**436**	**618**	**578**	**407**	**549**
Other marine fish by district					
Lamu	20	27	16	14	19
Tana River		7	13	13	17
Malindi	185	149	93	57	95
Kilifi	105	97	57	37	59
Mombasa	90	90	59	47	60
Kwale	100	124	359	327	322
Total	**500**	**494**	**597**	**495**	**572**
Grand Total	**158,670**	**135,143**	**135,408**	**133,600**	**144,505**

Source: Government of Kenya (Various) Economic Surveys

government for wildlife conservation. There are 4 marine national parks, 6 marine national reserves, 23 terrestrial national parks, 26 terrestrial national reserves and 5 national sanctuaries representing key ecosystems in the country and home to 30 per cent of total wildlife. The rest is found in other areas where wildlife conservation is designated as the principal land use system. These include 17 community sanctuaries and private conservancies.

Table 12.6: Wildlife population estimates in the Kenya rangelands, 2006–2010

Species	2006	2007	2008	2009	2010
Elephant	17.5	19.7	19.4	20.9	22.6
Buffalo	22.1	20.1	18.1	17.8	16.0
Giraffe	31.7	29.3	27.5	25.4	24.0
Burchell's Zebra	115.4	109.0	107.0	103.4	102.1
Grevy's Zebra	4.1	4.0	3.8	3.8	3.6
Topi	27.3	28.5	27.0	24.0	22.5
Kongoni	9.1	9.7	7.4	8.7	7.0
Wildebeest	291.3	291.5	298.0	295.0	294.6
Oryx	22.4	20.0	18.8	18.8	17.0
Eland	8.0	8.9	7.7	8.5	7.2
H. Hartebeest	0.9	0.9	1.0	0.9	1.0
Waterbuck	4.1	4.4	3.7	3.9	3.0
Kudus	12.1	12.5	11.4	11.2	10.2
Gerenuk	26.5	25.0	23.0	21.0	20.0
Impala	62.5	63.4	63.9	63.8	62.6
Grant's Gazelle	117.5	115.0	114.0	113.3	112.4
Thomson's Gazelle	45.1	45.0	47.4	47.5	47.0
Warthog	15.8	16.0	17.5	18.0	18.7
Ostrich	25.4	26.5	26.9	28.0	28.5

Source: DRSRS

The major concern in wildlife is the rapid decline in population, both in and outside protected areas. Since 1977, the country has lost 60-70 per cent of large wildlife and the annual decline of wildlife is currently estimated at 3 per cent with some species like rhinos, the Hirola antelopes and the dugongs being endangered. The major obstacle for the wildlife sector in Kenya is the lack of an updated legislative framework for managing wildlife resources. The Wildlife Bill, which is currently underway, is a great opportunity for the country to put things right. Stakeholders in this sector are exerting pressure on the government to put in place new wildlife legislation. However, caution is needed to ensure the pressure does not result in enactment of a flawed and disastrous document. The review process on the wildlife legislation must present a chance for the country to enact the most progressive and enlightened legislation.

12.7 Mineral Resources

The government is required to foster the establishment of a thriving mining industry, which will make full contribution to sustainable economic development in the country as envisaged in Vision 2030. This is in recognition of the fact that mining can act as an engine for economic development by diversifying exports, widening the tax base, generating skilled employment, creating demand for local goods and services, contributing to infrastructure development, producing raw materials for local usage and acting as a catalyst for wider investment in the economy. Table 12.7 shows production of different mineral resources between 2006 and 2010.

The mandate of management of mineral resources is currently under the Mines and Geology Department of the Ministry of Environment and Mineral Resources (MEMR). The department carries out mineral surveys on behalf of the government and is responsible for formulation of the legislative framework for the sector. Currently, the government lacks a clear policy and regulatory framework for the sector. Although Kenya is endowed with major mineral resources, the multimillion-dollar industry remains dormant, mainly because the country lacks a clear mining policy to trigger foreign investment in the industry. This is in turn hindering the maximum exploitation of minerals and is likely to jeopardize the mining industry. The ministry has prepared a Mining Policy and Bill, but they are yet to be approved by Parliament. It is expected that the new legislation, once enacted, will provide a framework for harmonizing activities of the different agencies dealing with mining issues so as to ensure improved efficiency and promotion of best mining practices in the country. Presently, the exploration and exploitation of mineral resources in Kenya is governed by the Mining Act, Cap 306 of the Laws of Kenya enacted in 1940.

The need to unlock the potential of the mining sector cannot be overemphasized. But to achieve this, there is need to provide an enabling environment

Table 12.7: Mineral production 2006-2009 (quantity)

	Unit	2006	2007	2008	2009	2010
Soda ash	Tonnes	374,210	386,578	502,846	404,904	473,689
Salt (crude and refined)	Tonnes	35,024	11,596	24,345	24,125	6,194
Flourspar	Tonnes	132,030	85,115	130,100	5,500	40,750
Soda crushed raw	Tonnes	662,939	843,043	865,788	948,076	959,160
Corondum (ruby)	Kgs	4,750	4,800	4,950	5,575	5,450
Carbon dioxide	Tonnes	9,359	11,028	22,030	15,711	16,345
Diatomine	Tonnes	185	201	72	231	224
Garnets (green)	Kgs	850	815	821	965	1,075
Gypsum	Tonnes	5,500	5,000	5,000	5,345	5,500
Vermiculite	Tonnes	350	300	320	315	395
Gold (unwrought)	Kgs	432	3,023	343	1,135	2,035
Gemstones	Tonnes	5	9	21	39	168

Source: Government of Kenya (2011) Economic Survey

for foreign investment. While seeking to encourage investment by mining companies, there is also need to ensure that mining operations are conducted responsibly. As such, the neglect of the environment and harm to local communities as a result of mining operations should not be condoned. The intention, therefore, is to ensure that the country secures the full economic and social benefits that mining development promises.

The new legislative framework is expected to set out principles that will guide the government in reforming the mining industry and trigger investment flows. Specifically, it will address the following issues:

- Sustainable utilization of mineral resources in the country;
- Equitable access to mineral resources and benefit sharing;
- Regulation of common minerals;
- Observation of the social and cultural values of the affected communities in the management of mineral resources;
- Alternative mine closures and development of new mine sites; and
- Value addition to raw minerals before export as a way of increasing returns for the Kenyan people.

12.8 Sanitation and Waste Management

With Kenya pursuing an industrialization path, waste generation is bound to increase significantly. But waste generation is not the problem. Rather, it is the limited assimilative capacity of the environment for wastes that presents a challenge. Entry of too much waste into the environment without reuse or recycling puts the environment under stress. This leads to pollution and resource degradation with obvious consequences of economic damage (Turner, 1995).

Vision 2030, Kenya's new development blue print, aims at transforming the country into a middle-income nation with annual GDP growth of 10 per cent. This implies that citizens will be enjoying higher standards of living on realization of the Vision. The implication of this is that more waste will be generated per capita per day. In this

Table 12.8: Increased density per area – strain to natural resources

Region	Density					Intercensal Growth				Area
	1969	1979	1999	2009	B/rate	69/79	79/89	89/99	99/09	Sq km
Nairobi	746	1,210	3,079	4,515	6.1	4.9	4.7	4.8	3.8	684
Central	127	178	282	333	2.6	3.4	2.8	1.8	1.6	13,173
Coast	11	16	30	40	3.6	3.5	3.1	3.1	2.9	83,040
Eastern	12	17	30	37	3.1	3.6	3.3	2.1	2.0	155,759
N/Eastern	2	2	8	18	9.0	4.2	(0.1)	9.5	8.8	126,902
Nyanza	168	211	350	432	2.6	2.2	2.8	2.3	2.1	12,525
R/Valley	12	19	38	55	4.6	3.8	4.2	3.4	3.6	163,883
Western	161	223	406	522	3.2	3.8	3.4	2.8	2.5	8,196
National	19	27	49	66	3.5	3.4	3.4	2.9	3.0	564,162

regard, it is imperative to put in place innovative methods of waste management, especially in cities, partly because more waste will be generated and partly because poor waste management could kill aesthetics in our cities, compromise health standards and consequently impede tourism and industrial development to the detriment of Vision 2030. Thus, this must be given due attention as a critical building block in all the pillars of the country's development agenda.

The ever-increasing population, improved standards of living and high rural-urban migration will continue to pose a challenge to sanitation and waste management in Kenya. The latter is responsible for the development of densely populated informal settlements in urban and peri-urban areas with poor sanitation facilities. Table 12.8 depicts the population growth and density in Kenya over time.

Development of water supplies has not been matched by a corresponding increase in facilities of sanitary disposal of waste water. As a result, waste water is discharged into mainstream rivers, valley depressions and dams, leading to high pollution levels. In addition, main sewer systems suffer from constant breakages and/or leakages due to increased discharge to fixed systems. Difference in access to adequate sanitation between urban and rural environments still persists, with the formally-planned urban areas being better served than rural areas, and urban informal settlements.

Kenya compares dismally against other countries in terms of access to improved sanitation services (Table 12.9). In 2008, the estimated sanitation coverage in rural areas was 55 per cent. The proportion of urban population with access to improved sanitation facilities in Kenya declined marginally from 48 per cent in 1990 to 46 per cent in 2004. However, there was some increase in the proportion of rural population with access to improved sanitation from 37 per cent in 1990 to 41 per cent in 2004. Kenya's performance is better compared to Ghana but worse off when compared to Uganda (54%). Other countries such as Malaysia, South Africa, Thailand and Singapore have at least over 79 per cent of their urban population having access to improved sanitation facilities. Malaysia has been able to improve sanitation coverage by engaging the private sector in the provision of sewerage services involving 84 local authorities.

The management of wastes generated in Kenya is governed by the Local Government Act Cap 265, Public Health Act Cap 242, and the Environmental Management and Coordination Act (EMCA) No. 8 of 1999. While the Public Health Act prescribes measures of dealing with nuisance such as wastes, EMCA legislates on waste management systems, ranging from generation to disposal. Most Local Authorities, led by the Nairobi City Council, have come up with by-laws on waste management. Some of them engage in periodic updates of their by-laws to better respond to the dynamism in waste

Table 12.9: Access to improved sanitation services

	% Urban	% Rural	% Urban	% Rural				
	1990	2008	1990	2008	1990	2008	1990	2008
Botswana	100	99	88	90	58	74	20	39
Brazil	96	99	65	84	81	87	35	37
Chile	99	99	48	75	91	98	48	83
China	97	98	56	82	48	58	38	52
Egypt	96	100	86	98	91	97	57	92
Ghana	84	90	37	74	11	18	4	7
India	90	96	66	84	49	54	7	21
Indonesia	92	89	62	71	58	67	22	36
Kenya	91	83	32	52	24	27	27	32
Singapore	100	100	…	…	99	100	…	…
South Africa	98	99	66	78	80	84	58	65
Thailand	97	99	89	98	93	95	74	96
Uganda	78	91	39	64	35	38	40	49

Source: World Health Organization and UNICEF (2010)

management. NEMA also developed the EMCA Waste Regulations in 2006, whose purpose was to provide guidelines, procedures and standards for environmental governance to ensure compliance. The lack of a comprehensive waste management policy and framework is the cause of many challenges experienced at present by different Local Authorities. Efforts towards ensuring appropriate policy would lead to improved standards and efficiency in waste management.

12.8.1 International Best Practices in Solid Waste Management

Singapore

Solid Waste Management (SWM) in Singapore is one of the most efficient in the World. In 2007, a total of 5.6 million tonnes of waste were generated. Out of these, 3 million tonnes were recycled while 2.6 million tonnes ended at the incinerators and landfills (MEWR, 2010). About 54 per cent of the waste is recycled, 43 per cent incinerated and only 3 per cent land filled. The country pursues two objectives in SWM: Towards zero landfill, and achieving 60 per cent recycling by 2012.

Public Waste Collectors (PWCs) and General Waste Collectors (GWCs) are licensed by the National Environmental Agency (NEA) to collect solid waste in Singapore. PWCs provide recycling services to residents besides collecting wastes. Waste reduction, waste recycling and minimizing landfill through incineration are top priorities.

To achieve waste reduction, NEA undertakes public education through monthly programmes such as as "Bring Your Own Bag" campaign meant to cut down on the use of plastic bags. In 2007, a voluntary packaging agreement was signed with the food and beverage industry to reduce waste generation at source and to encourage best practices among industry players.

There is a national waste recycling programme (NRP) under which PWCs provide door-to-door collection services for recyclable materials. In 2007, centralized recycling bins were provided for every 5 blocks of flats in residential estates to make it easy for people to undertake recycling.

Incineration plants have been set up to handle incinerable wastes so as to conserve landfill space. Through incineration, the volume of waste ending in

the landfill has been reduced by as much as 90 per cent. At the same time, the heat generated from the incineration process is used to produce electricity, accounting for about 2 per cent of the country's total electricity supply (MEWR, 2010).

Nepal

Waste management is undertaken by municipalities just like in Kenya, and it involves public-private partnership (PPP) in solid waste management, a feature also witnessed in Nairobi.

Initially, the municipality was directly offering door-to-door collection in the core areas of the city and disposing it in a sanitary manner. The municipality had no plan and vision for waste management and was not capable of coping up with the waste generated in the city. A lot of waste was dumped at the bank of Narayani River. Against this backdrop, PPP was initiated in 1999 to manage solid waste.

The Community Development Section for SWM is concerned with cleaning of roadside drains and public toilets, removal of dead animals, training employees involved in SWM, and public education on SWM including the concepts of reduce, reuse and recycle (3Rs). A private contractor has been engaged to take charge of door-to-door collection of waste and collection of waste from unofficial collection points in residential, commercial and industrial areas.

The contractor is able to collect waste from 70 per cent of the areas in the city. Waste reduction at source is encouraged through household composts and segregation of plastic waste. In some areas, residents have installed waste bins particularly for inorganic waste. It is estimated that 15 per cent of municipal solid waste is recycled and 50 per cent of domestic waste and 25 per cent of institutional waste is collected at source each day. A non-governmental organization, Practical Action, distributes compost bins, plastic buckets and suiro hooks throughout the municipality. The municipality also sells compost bins and suiro hooks at affordable rates.

The contractor employs his own staff for collection, transportation and disposal of waste. The municipality provides supervision and support services for the daily operations. The contractor does not collect any fees for waste collection from the residents; instead, he is paid directly by the municipality. The residents, through their organizations, have since agreed to pay NRs. 50 and NRs. 100 per month, respectively, for residential and commercial premises to improve collection and disposal of waste.

Solid waste management has been significantly improved through the PPP with door-to-door collection being effectively executed. Non-governmental organizations (NGOs) have been able to motivate private sector operators to be involved not only in waste collection and disposal but also in waste recycling, leading to creation of significant job opportunities. The municipality has been able to meet its waste management targets with a reduced budget (Practical Action Nepal, 2008).

12.8.2 Challenges

Pollution and solid waste are some of the leading environmental health problems in the country affecting both rural and urban populations. Projects in the mineral development industry, which involve exploration, mining, transportation and processing of minerals and construction materials also contribute to pollution. All mining methods involve some form of disturbance on the surface of the underlying strata, including aquifers. Exploration and pre-development impacts are usually short term and include: surface disturbance; airborne dust, noise and emission from drilling equipment operations, disturbance of soil and vegetation, streams, drainages, wetlands, cultural or historic resources and underground aquifers; and conflict with other land uses.

Both surface and underground mining involve the drainage of the mine area and discharge of mine waters; the removal and storage disposal of large volumes of waste material; and the removal and processing of the ore or construction material.

12.8.3 Proposed Interventions

While the focus of SWM in the country has been disposal, this is an end-of-pipe solution which, if not handled properly, can only worsen the waste problem. In order of priority, the following measures should be institutionalized in SWM in the country:

- Reduction of waste;
- Reuse of products;
- Recycle/compost the product;
- Recover the energy by incineration;
- Disposal of the product using landfill and
- Enactment of a comprehensive policy and legislative framework.

ENDNOTES

1. Water scarcity refers to a situation where a country's water resource availability is less than 1000 M^3 per capita per year as per the United Nations recommended minimum.

PART III

Transformative Institutions for Delivering Kenya Vision 2030

This part of the report discusses the role of transformative institutions in delivering the targets set in Kenya Vision 2030. Kenya is in the midst of a major developmental shift, and hence the need to put in place institutions with operative capacity to create growth and development in all the pillars stipulated in Vision 2030. Though not exhaustive, this part discusses the various challenges in the development of key institutions, and in ensuring that these institutions are well placed to ensure resource-use efficiency and innovation, which determine the level of productivity of a country and its competitiveness on the global scene.

Chapter 13

Transformative Institutions for Delivering Kenya Vision 2030

13.1 Kenya's Development Imperative

13.1.1 Background

The Kenyan economy has been steadily improving but has not kept pace with the growing population in a manner that would see a sustained long-term improvement in the welfare of the population. The population has been growing rapidly, is youthful, comparatively educated and increasingly urbanizing. The natural environment within which it is growing is deteriorating, and this is taking place in a regional and global environment that is increasingly uncertain. It is within this environment that Kenya must create welfare improvement opportunities for its citizenry, with the role of transformative institutions becoming even more important than ever before.

13.1.2 Achieving Smart and Inclusive Growth

Institutions, policies and factors that enhance resource-use efficiency and innovation determine the level of productivity of a country, hence a country's competitiveness on the global scene. To understand the role of institutions in delivering Vision 2030, it is critical to review lessons on the relative performance of world economies and regional economic blocks, based on internationally-accepted pillars of assessing the productive potential of nations worldwide. Comprehensive annual national assessments of global competitiveness conducted by the World Economic Forum using the Global Competitiveness Index (GCI) provide useful information in this context. Within the framework of the Centre for Global Competitiveness and Performance, the World Economic Forum publishes annual Global Competitiveness Reports for countries assessed on the basis of how they score on 12 internationally-accepted pillars of global competitiveness. GCI measures both microeconomic and macroeconomic foundations of national competitiveness.

Remarkably, coming first among the 12 pillars is institutions. The institutions pillar is one of the basic pillars, some of the others being infrastructure, macroeconomic environment, health and education. The efficiency-enhancing pillars are higher

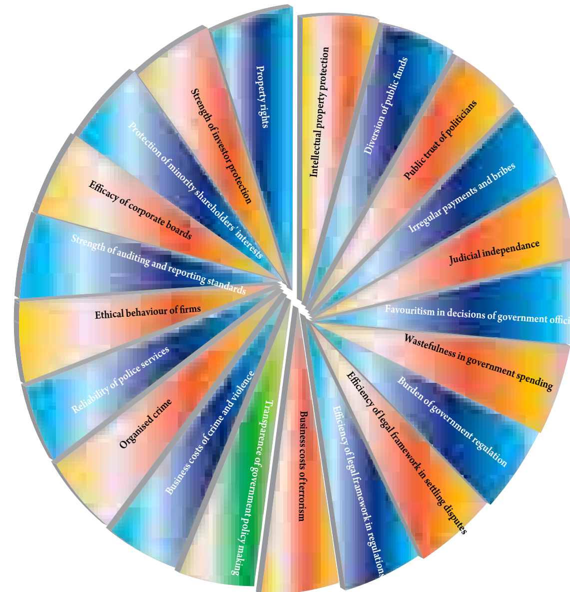
education and training; technological readiness; market size; financial market development; labour market efficiency; and goods market efficiency. The 2010-2011 Global Competitiveness Report of 139 countries shows that countries whose institutions are highly rated also tend to receive high average scores on the basic pillars of global competitiveness; this outcome further leverages their overall Global Competitiveness Index (GCI).

13.1.3 Enhancing National Growth and Competitiveness through Institutions

Enhancing efficiency in governance and achieving equity in regional development are key features of Kenya's new Constitution. Strong public and private institutions are indispensable in the pursuit of these crucial public policy goals. Strong institutions contribute immensely to national development, since they instil into the system the following key strengths, among others (World Economic Forum, 2010):

- Reduced economic costs of doing business through an enabling environment free of over-regulation, excessive bureaucracy and red tape, corruption on all fronts including corporate scandals and political interference with the Judiciary;
- Open, highly ethical and transparent private sector dealings with government, fellow firms and the general public;
- Proper and assured protection of property rights;
- Sound management of public finance and high accountability to the public;
- Strong auditing and reporting standards; and
- A level playing field that attracts high investor and consumer confidence.

Figure 13.1: World Economic Forum indices for assessing national institutional performance, 2010



The central position institutions command in building global competitiveness gives high credit to the legal and administrative environment in which citizens, firms and governments interact to generate income and wealth. Weak institutions are a major impediment to the competitiveness of countries. Weak institutions, for example, contributed immensely to Kenya's poor ranking in 2010-2011, at position 106 overall out of 139 countries (World Economic Forum, 2010).

In response to the important role institutions play in national development, the World Economic Forum has since 2005 established the following comprehensive set of indices for assessing how countries across the world perform on the institutions pillar. These indices provide a useful guideline for a detailed assessment of how Kenya's institutions have been performing over the years, and hence identifying the measures needed to deliver effectively on the valued goals of Vision 2030. As already noted, there are several indices that are used by the World Economic Forum in assessing institutional performance. The indices are weighted and evaluated using executive opinion surveys.[1]

13.2 Global Ranking of the Quality of Kenyan Institutions

Table 13.1 shows Kenya's institutions to be the poorest in the cluster of selected comparator and benchmarking countries. Kenya had its lowest ranked pillar being the one of institutions in GCI 2010-2011, coming 123rd out of 139 countries (with an index score of 3.2 out of a maximum of 7). Inefficient government bureaucracy was mentioned among the top-three hindrances to doing business in the country, with corruption and access to finance being the foremost problems. Singapore demonstrates excellent institutions, with a world-class score that saw it lead in the 2010-2011 GCI ranking. This is contributed by zero tolerance to corruption in Singapore, and efficiency in governance.

Effective and transparent public institutions in countries such as Sweden and Switzerland boost the productive level of economies all over the world. Closer home, Rwanda was ranked 19th in terms of well functioning institutions, Botswana 32nd, and Mauritius 43rd. Institutions in Kenya are weakened by internal and external factors that result in numerous inefficiencies, thus requiring strategies and policies to strengthen the institutions and their linkages for fruitful networking, capacity building and overall competitiveness. Institutional reform is, therefore, a necessary prerequisite for the effective delivery of Vision 2030.

Table 13.1: Rankings on pillars of global competitiveness for Kenya and selected countries, 2010-2011

Country	Rank out of 139 Countries			
	Institu-tions Pillar	Basic Pillars	Innovation and Sophisti-cation Factors	Overall
Singapore	1	3	10	3
Germany	13	6	5	5
Rwanda	19	84	87	80
UAE	20	8	27	25
Chile	28	37	44	30
Botswana	32	76	93	76
Malaysia	42	33	25	26
Mauritius	43	47	59	55
South Africa	47	79	43	54
China	49	30	31	27
India	58	81	42	51
Indonesia	61	60	37	44
Korea	62	23	18	22
Ghana	67	122	100	114
Vietnam	74	74	53	59
Tanzania	83	116	94	113
Cambodia	94	113	106	109
Uganda	104	123	111	118
Nigeria	121	136	83	127
Kenya	123	126	58	106

Source: World Economic Forum (2010)

13.3 Macroeconomic Management and Institutions

Kenya's ranking against other countries on basic requirements is shown in Table 13.2. The basic requirements show a weighted index computed based on the performance of the four pillars of institutions, infrastructure, macroeconomic environment and health and primary education. The country is ranked moderately low on basic requirements.

The responsibility for macroeconomic policy formulation and implementation is shared between the Treasury and the Central Bank of Kenya. The Central Bank Act gives the Central Bank the authority to formulate and implement monetary policy – CBK Act Cap 491 Section 4(1). The core objectives of the Central Bank's monetary policy are price stability and stability of the financial system. Following an amendment to the Act in 2007, subject to realizing price and financial sector stability, the Central Bank is also expected to support the economic policy of the government. Fiscal policy formulation and implementation falls under the purview of the Treasury.

Table 13.2: Global Competitiveness Index 2010-2011 rankings of basic requirements (Macroeconomic environment and Institutions)

Country/Economy	Basic Requirements		Institutions		Macroeconomic Environment	
	Rank	Score	Rank	Score	Rank	Score
Botswana	76	4.37	32	4.84	74	4.52
Cambodia	113	3.72	94	3.56	116	3.81
Chile	37	5.15	28	5.01	27	5.24
Egypt, Arab Rep.	89	4.19	57	4.03	129	3.35
Germany	6	5.89	13	5.50	23	5.32
Ghana	122	3.54	67	3.93	136	3.00
India	81	4.30	58	4.03	73	4.53
Indonesia	60	4.62	61	3.98	35	5.15
Kenya	126	3.50	123	3.16	128	3.48
Korea, Rep.	23	5.42	62	3.98	6	5.76
Kyrgyz Republic	120	3.59	131	3.01	119	3.66
Mozambique	130	3.43	99	3.46	104	4.17
Nigeria	136	3.11	121	3.18	97	4.25
South Africa	79	4.35	47	4.38	43	4.99
Sri Lanka	73	4.42	55	4.06	124	3.60
Tanzania	116	3.66	83	3.74	115	3.87
Uganda	123	3.53	104	3.42	114	3.89
Vietnam	74	4.39	74	3.80	85	4.47

Source: World Economic Forum (2010)

The Constitution and the attendant legal implementation framework provide opportunities for strengthening institutions for public expenditure management (PEM) and macroeconomic management. Some of the implications of the new constitution are:

1. The independence of the Central Bank of Kenya in the formulation of monetary policy and supporting price stability is provided for in the Constitution – Article 231(3). The Central Bank Act, Cap 491 Section 4C gives authority to the Minister "under exceptional circumstances" to give directives to the Central Bank on monetary policy formulation and implementation. To enhance transparency and accountability, a relevant legal framework should require the Governor of the Central Bank to present a report on monetary policy at specified periods within the year, and/or to attend before a committee of the National Assembly, or the Senate when required by the committee, and answer any question concerning monetary policy and price stability in the country;

2. The Constitution provides for devolution. In macroeconomic policy formulation and implementation, an appropriate mechanism for inter-governmental coordination is required to ensure fiscal stability and sustainability. A key area relates to borrowing by county governments, which should be well coordinated so as not to undermine macroeconomic stability. Effective coordination is required to ensure that creation of fiscal deficits and financing does not undermine macroeconomic stability. In addition, there are other important innovations in Kenya's budget that would need to be rolled out to the county governments. These include a Medium Term Expenditure Framework expected to enhance the link between policy-planning and budgeting. The macroeconomic

framework for the central government should explicitly reflect the resources available to counties within a multi-year framework to facilitate effective budget planning. An effective MTEF will enhance predictability and certainty on the timing and flow of inter-governmental resource flows;

3. Performance Contracting System: In 2007, Kenya won the prestigious UN Public Service Award for the performance contracting system. It is important that the country builds on this achievement and rolls out an effective performance contracting system for the county government;

4. The Public Expenditure Review (PER) process is now part of Kenya's budget process. This diagnostic review provides useful information on budget implementation, and serves as a basis for preparation of sector reports. It also informs the budget decision making process. In this regard, the PER process may have to be maintained and rolled out to the county government level.

13.4 Transforming Human Resource Development Institutions

Under Vision 2030, the government recognizes that Kenya's main potential lies in its people. The immediate challenge identified in Kenya's transformation as envisioned in Vision 2030 is how to meet the human resource requirement for a rapidly changing and more diverse economy. This will require not only an improved education and training system, but also a more efficient labour market and health system.

Improvements in the accessibility and quality of education and health services, especially to the poor, can enhance poverty reduction. These improvements in turn depend on the quality of a country's institutions and the nature of inter-relationships among these institutions. Previous research evidence has shown that the quality of institutions impact economic growth, which is a necessary condition for poverty reduction (Acemoglu and Robinson, 2008; Chong and Calderon, 2000). Further, institutions affect how economic benefits are distributed across the various social and political groups in a given society. This partly explains why, despite similar economic performance, poverty reduction differs substantially among nations and across social groups.

13.4.1 Education Service Delivery

Vision 2030, its Medium Term Plan and the Constitution identify education and training as fundamental to: the country's overall sustainable development, poverty reduction, industrial and technological advancement and attaining competitive edge both in local and global economic systems. The Constitution of Kenya provides that the national government, mainly through the ministry in charge of education, will be responsible for education policy, standards, curricula, examinations and the granting of university charters, while the county government will be responsible for pre-primary education, village polytechnics, home craft centres and childcare facilities.

The national government will further be responsible for universities, tertiary educational institutions and other institutions of research and higher learning and primary schools, secondary schools and special education institutions. However, education delivery as a function is better delivered in a decentralized mechanism. For instance, capitation grants are currently being transferred directly to schools and there are systems for quality assurance and education management at local levels; that is, at district and divisional levels. The school committees and board of governors are also charged with the responsibility of managing school operations.

Currently, the management of education and training are under the Ministry of Education and the Ministry of Higher Education, Science and

Technology. Agencies under the MoE involved in service delivery in the education sector include: Teachers Service Commission (TSC); Kenya Institute of Education (KIE); Kenya National Examinations Council (KNEC); Commission for Higher Education (CHE); Higher Education Loans Board (HELB); among others. Further, in the Constitution, the Teachers Service Commission (TSC) is established as one of the constitutional commissions, therefore making it independent. This has far-reaching implications on management of education and service delivery, and more particularly on the relationship between the TSC and the ministry in charge of education and training. It calls for an understanding and reorganization of service delivery patterns at national and county levels, and with other government organs for effective coordination in education service delivery, performance, monitoring and financing.

Institutional constraints and medium term challenges in education

The key challenges identified with respect to education and effective human resource development are: inequalities in access at all levels; low access to education, especially post-primary education; relatively low quality of education, worsened by the need to increase access; weak monitoring of performance; and perceptions of high costs of schooling. Education and training at tertiary levels faces numerous challenges, including curriculum development, revision and implementation that has not kept pace with the rapidly-changing technological environment; weak linkages between industry, training and research institutions and inadequate, obsolete or dilapidated training facilities.

While services for pre-primary education, village polytechnics, home craft centres and childcare facilities are assigned to county level governments, there are various challenges relating to access, quality and equity. Some of them are:

i. Decentralization of education service delivery would help in addressing inequalities in education service delivery. This is likely to be the case in a context characterized by inequities in form of unequal distribution of human and material resources and the existence of both weak and strong regional infrastructure across counties.

ii. Kenya also faces quality-related challenges, which may be more complex in a devolved context. International experience shows that national quality standards are key tools used to ensure that the quality of education is not compromised following distribution of functions to lower levels of governance (Emmanuela di Gropello, 2002). Although Kenya has in place a Directorate of Quality Assurance and Standards, the department is faced with both capacity and financial constraints that hamper its role. Thus, besides establishing national quality standards for all levels of education, there will be need to build additional capacity at both national and sub-national levels to effectively monitor quality standards. In particular, the functions assigned to the counties i.e. pre-primary education, village polytechnics, home craft centres and childcare facilities call for the establishment of national quality standards and the assignment of resources for the effective monitoring of performance.

iii. The quality of education in a decentralized setup can also be enhanced by provision of specific tools to the central ministry/agency in charge of education to guard against the development of significant regional differences in educational quality, its access and cost. Some of the tools commonly used across the globe to ensure uniformity following decentralization include: implementation of redistribution of resources based on population and regional wealth.

Apart from pre-primary education, education and training services will remain largely under the

national government. Even so, the management of the other levels of education, such as primary and secondary education, will nonetheless be affected by the transition to the county system. Kenya, for instance, will require a well-thought out transition from the former system of Provincial Education Officers and District Education Officers to the new governance structure, which has introduced counties. One of the most important actions will be to ensure or facilitate a process that encourages transparent and extensive consultations across stakeholders to avoid national conflict and yield better results. To ensure a smooth transition to the new governance/management structure, there will be need to pay attention to a number of issues. These include:

i. Recognizing that new or restructured institutions, such as some counties, may lack the necessary capacity to take up their new responsibilities immediately. One of the ways to overcome this problem is to put in place transitory arrangements that avoid problems associated with very fast implementation arrangements. There are also existing functions, such as monitoring of standards and productivity enhancement initiatives, which are hampered by capacity and resource challenges.

ii. Accepting that reform of institutions usually results in coordination challenges as roles and responsibilities of players change. An important starting point to promote coordination and avert conflict is to develop a common vision of reform among potentially competing centres of power. A common vision is essential if collaboration, rather than conflict, is to become the dominant force driving actions. To this end, it is important to initiate an open flow of ideas and information among key actors; including the ministry in charge of education (or relevant sector), county leaders, political parties, private sector and communities.

iii. Developing clear policies and well-designed legal and/or administrative instruments that delineate the division of responsibility and authority between the centre and the devolved units. It is important to clarify the assignment of functions, simplify new processes and structures, and provide mechanisms to coordinate and foster a shared understanding of reform at different levels of government, as well as to adjudicate disagreements (King and Guerra, 2005).

iv. Recognizing that, given the governance changes, the role of the central government will change and these changing roles will require new skills to be developed, the national government will need to take up new roles and/ or expand its role in existing functions such as setting and monitoring standards, and the design and implementation of an equalization scheme. Other challenges will relate to the pace of decentralization and capacity building at national and sub-national levels. The country is likely to face more daunting challenges in education access, quality and cost.

Given the above challenges, there is need to:

- Enhance education quality by allocating adequate resources to key processes, including monitoring of education performance.

- Strengthen coordination while giving cognisance of the devolved functions and establishment of constitutional offices. In education, training and labour market sectors, it will be important to merge the functions of the Ministry of Education; Ministry of Higher Education, Science and Technology; and the Ministry of Labour into one ministry, say a new Ministry of Human Resource and Skills Development charged with the comprehensive role of human resource development. The merger should ensure that the various functions are well managed and coordinated, both vertically

(within ministry) and horizontally (between central government and county governments).

- Develop and harmonize national and county government priorities and linkages. Strengthening institutions for effective fiscal decentralization in education (coordination between CDF, LATF, central government financing) is also critical. The role of public-private partnerships at all levels will need to be specified and strengthened across all levels of education. Legislation that is comprehensive enough to clearly define the rights and obligations of the respective entities involved would enhance coordination and reduce conflict.

- Prepare a capacity development plan. The national and sub-national governments and other stakeholders will need to take up new roles and/or expand their roles in existing functions. This will require capacity building, informed by assessment of institutional capacities of the administrative levels that will be given new responsibilities. It will be important to identify both skills requirements and capacity development needs.

- Guide the devolved services, such as pre-primary education, by development of simple and clear decentralization plans and transfer agreements. For the decentralized services, there ought to be devolution of authority, rather than delegation, with experiences across the globe indicating superior performance of models that transfer ownership and authority compared to "shared responsibility models" (King and Guerra, 2005; Emanuela di Gropello, 2004).

Other related interventions that can be pursued to improve education and training, while also improving labour market outcomes and keeping sight of the long-term development objectives include:

- Continuous updates and revision of curricula delivery process to keep pace with the rapidly-changing environment and global trends. This should be informed by regular national manpower surveys, training needs analyses, and benchmarking against international best practices.

- Support linkages between industry on one hand and education, training, and research institutions on the other. Some of the ways to achieve this is through: Teacher placements in businesses/industries during school holidays to sensitize them on the skills their students should acquire; and placing industrialists as members of the boards of educational institutions to provide input into the curricula.

- Establish and institutionalize tripartite arrangements between employers, employees and training and education institutions. To address the skills mismatch problem, a skills gap analysis should be conducted. Modalities should be put in place to expand links between institutions of learning and relevant industries, for example, through attachments for students and instructors. This arrangement should be supported with a well-designed, decentralized and efficient labour management information system.

- There is need to increase the uptake of science and technology disciplines and to expand and upgrade most of the existing training facilities. Some broad proposals include the need to identify and address the bottlenecks facing the uptake of science and technology disciplines; supply, development and retention of good science teachers; and use of out-of-school activities in learning science.

13.4.2 Health Services Delivery

Most physicians in Kenya are trained in public universities, while most nurses graduate from Kenya's

medical training colleges spread across the country. Private and mission hospitals also train nurses. To practise in Kenya, all nurses and physicians must have a "certificate to practise" from the Nursing Council of Kenya and the Kenya Medical Practitioners and Dentists Board, respectively.

Health workers in Kenya are employed by, among others, the Ministry of Health, semi-autonomous government institutions (national hospitals, research institutions and training institutions), NGO health facilities, missionary hospitals, nursing homes and by the private sector. Non-state actors/organizations employing health workers include: NGOs, UN organizations, pharmacies and dispensing chemists. In the public health facilities, health workers are employed through the Public Service Commission, while their salaries are paid from the budget provisions from the Ministry of Finance.

Institutional constraints and medium term challenges

Although a number of reforms have been implemented in the health sector touching on human resources management and development, there are notable weaknesses in implementing these reforms. A key weakness relates to the slow pace towards realization of the set HRH goals within the timelines laid down in the NHSSP II plan.

Shortage of medical personnel is another major impediment to achieving the health millennium development goals (MDGs). The WHO's baseline estimate for achieving health-related MDGs is the need to have at least 23 health workers per 10,000 people. Table 13.3 shows that some of the cadres still fall way below the recommended ratios.

Shortage of medical personnel impacts on staff morale and productivity. Employee satisfaction survey findings (2008) revealed that most staff in the public sector are not taking annual leave due to heavy workload. According to the Human Resource for Health Strategic Plan (2006-2010), the overall staff shortage is 47,247. Shortfalls are mainly in parts of Coast, North Eastern, Rift Valley and Nyanza provinces; areas that have the lowest health indicators (Government of Kenya, 2009). The mushrooming of Constituency Development Fund (CDF) facilities is also causing staffing and facility challenges for the ministry.

Mal-distribution of staff, particularly between urban and rural areas, is a major challenge as identified by the 2006 Human Resource Mapping Survey and the review of the KHPF performance. Government personnel is heavily skewed in favour of hospitals and the better off districts, leaving lower level health facilities to suffer severe shortage of professional health workers. Over half of medical personnel are currently working in district and provincial hospitals (Government of Kenya, 2006). This staffing imbalance accentuates the rural-urban disparities in access to health care, thus working against one of the key stated objectives of Vision 2030 of providing equitable healthcare.

Apart from staff shortages and mal-distribution, high staff turnover and weak HRH development, planning and management systems affect deployment (Government of Kenya, 2008). Health workers are unevenly deployed within the country, with the greatest number being deployed in Nairobi than in hard-to-reach rural areas. The fragmentation and weak coordination of the HR function within the ministry and other service delivery partners contributes to weak and inefficient HR practices and reduces the sector's ability to maintain a strategic HR perspective (Government of Kenya, 2007a).

Despite the shortages of medical staff, there has been no significant progress in regard to human resource development relating to both basic as well as continuing education. In regard to basic education, there has not been any substantive effort in implementing a HRD plan. Training needs assessment (TNA) has not been carried out. Lack of a central information pool on Pre-Service Training (PST), In-Service Training (IST) and Continuing

Professional Development (CPD) hampers HRD planning. This is acknowledged in the JPWF and the HRH component of the AOP 2 , which sets out several activities to address this issue. The current rate of output of registered nurses in nursing training institutions is also low and needs to be increased.

Continuous medical training has been ad hoc and not planned. Lack of pre-training needs assessment further compounds the problem. As an illustration, studies indicated that about 37 per cent of doctors and 74 per cent of enrolled nurses who provide HIV/AIDS patient care and management had not received any specialized training (Government of Kenya, 2006).

A key constraint relates to the issue of decentralization. While NHSSP I, 2001-2004 put emphasis on decentralization of health care delivery through redistribution of health services to rural areas, not much was achieved. To date, there is no national policy on decentralization of health in place. Centralized decision-making has been blamed for, among other things, regional or provincial disparities in distribution of health services, inequities in resource allocation and unequal access to quality health services, with resultant regional or provincial differentials in the indicators of health (Government of Kenya, 2002). The HRM function at the MoH also remains highly centralized, with limited control and/or delegation of authority to provincial and district offices. The District Health Management Boards and the District Health Management Teams that were established through Legal Notice in 1992 still need a legal framework to give the DHMB/DHMT the mandate for a decentralized HR function (Government of Kenya, 2005). Also, there are no available guidelines on the functioning of the DHMTs (Ndavi *et al*., 2009).

Emerging Policy Issues and Recommendations

Kenya's health system faces a number of problems including a variety of human resource-related challenges. Specifically, these include: an overall lack of personnel in key areas, which is worsened by high numbers of trained personnel leaving the health sector to work overseas due to poor morale among health workers. Furthermore, those personnel who remain are inequitably distributed between urban and rural areas. Thus, as in many parts of Africa, the availability of health personnel is one of the major stumbling blocks to the delivery of adequate healthcare. An inadequate health workforce with a high population-to-health worker ratio contributes to the general deterioration of health indicators in Kenya.

Failure to strategically plan for Human Resource for Health (HRH) has led to human resource planning and management weaknesses. Absence of

Table 13.3: Registered key health personnel in Kenya

Type of Health Personnel	2007		2008		2009		2010*	
	Number	No / 100,000	Number	No / 100,000	Number	No / 100,000	Number	No / 100,000
Doctors	6,271	17	6,623	17	6,800	18	7,129	18
Dentists	931	3	974	3	859	2	898	2
Pharmacists	2,775	7	2,860	7	2,921	8	3,097	8
Pharmaceutical technologists	1,680	5	1,851	5	1,950	5	2,233	6
Nursing officers	12,198	33	14,073	37	26,988	70	29,678	75
Enrolled nurses	31,917	86	31,917	83	34,032	88	34,282	86
Clinical Officers	5,797	16	5,035	13	7,816	20	8,598	22

Source: Government of Kenya (2011)

a monitoring and evaluation system for HRH has also made it even more complicated to enhance accountability, to track and even to evaluate progress. Joint planning, funding and monitoring initiatives for HRH would have led to better deployment of resources. There is need for improved stewardship role of the Ministry of Health in regard to HRH so as to achieve the health targets including MDG targets (Government of Kenya, 2007a). The following are some of the proposals put forward to revamp health outcomes:

- There is need to increase training of health personnel and to expand and upgrade the existing training facilities. This will help reduce shortages of health personnel.

- Incentive schemes should be developed and used to attract, recruit and retain health workers in rural areas in general and ASAL districts in particular. Evidence from experiences of other countries suggests a combination of financial and non-financial incentives, but with no specific pointer on what incentives to use. Effective incentives should address wider needs of workers, improve the working environment, and support career paths. Incentives should, thus, be developed consultatively.

- Decentralize human resources management. Decentralization has been a proposal ever since the Health Policy Framework of 1994 but has never been implemented. Employment of health staff in public facilities is done through the Public Service Commission. This needs to be decentralized to the counties. Since the national referral hospitals are the sole responsibility of the national government, recruitment of staff for those facilities could be done at the central government level. However, for the lower level health facilities under the care of the county governments, recruitment could also be done at that level.

- Implement a HRD plan and enhance coordination between OCPD and HRD by developing a central information pool on Pre-Service Training (PST), In-Service Training (IST) and Continuing Professional Development (CPD). This can be preceded by a training needs assessment (TNA) that will guide the design of training programmes. The Ministry of Health should implement the recommendations contained in the JPWF and the HRH components of the AOP 2.

- There is need to institutionalize performance management at facility and individual level – other than adoption at the ministerial level. Individual performance evaluation procedures should be defined and aligned to AOP targets.

- Develop a human resource management information system. Although there is a system for managing the payroll, the personnel function of this is not fully utilized to manage personnel data. This has resulted in many parallel data collection systems and poor coordination. Due to lack of integration of the HR system and current HMIS, there is limited information for workload analysis. An integrated HR system will not only facilitate planning at the national level but also improve administration of human resources.

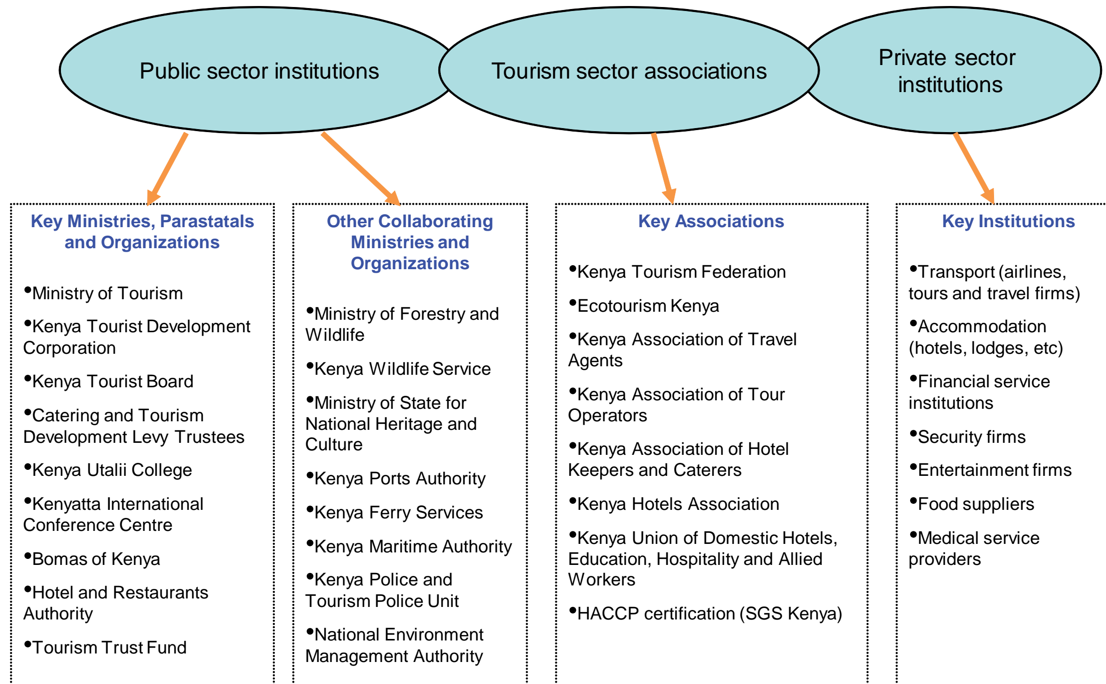
13.5 Transforming Tourism Institutions for Effective Delivery of Vision 2030

13.5.1 Structure of the Tourism Sector

The tourism sector operates within a liberalized economic environment characterized by active partnership between the government and the private sector (Figure 13.2).

The public sector formulates and implements policy, licensing the actors, regulating the industry and maintaining fair practice in the tourism business, developing tourism and supporting tourism sector

Figure 13.2: Basic structure of tourism sector institutions in Kenya



Source: Authors' construct

activities, managing national parks and reserves and other public tourism resources, setting up and maintaining crucial tourism infrastructure and promoting tourism (Ikiara, 2001). More generally, the government is charged with the overall mandate of planning, policy making and coordination; regulation and monitoring; facilitation and implementation; and development and promotion.

The private sector complements the public sector by undertaking most of the investment and capital stock (Elliot, 1997). The private sector is mainly involved in the provision of transport (e.g. tour companies, travel agents, taxi companies), entertainment, accommodation (through ownership and management of hotels, lodges, campsites and other tourist facilities), security companies and other tourism facilities. In the delivery of these services, the private sector is organized into different associations based on the area of activity. These associations play a vital role in linking public and private sector institutions by lobbying for their members' interests and influencing policy making.

At the apex of the sectoral structure is the Ministry of Tourism, whose core functions and services include policy making and planning; overall coordination; investments promotion; facilitating allocation of resources; marketing and promotion; regulation and monitoring; product development and diversification; manpower training and development; and tourist security and safety. Other service delivery obligations include license application and renewal; classification of hotels and restaurants; tourists' security and safety; advice on work permits and handling of complaints.[2]

The ministry discharges its mandate through eight semi-autonomous state corporations and organizations (Figure 13.2) and works with a number of other key government ministries/institutions that influence tourism service delivery.

According to ESCAP (1997), well-functioning institutions will have clear institutional mandates and coordination mechanisms. Ideally, the institutions should have sufficient autonomy to cushion them

from ad hoc political interference. All parastatals under the ministry are semi-autonomous and are responsible to the Minister through the Permanent Secretary.

13.5.2 Institutions in the Tourism Sector

Within the Medium Term Plan 2008-2012, the government has initiated various policy changes including preparation of a draft Tourism Policy, as well as Wildlife and Heritage policies. The Tourism Bill 2010,[3] which provides for development, management, marketing and regulation of sustainable tourism and tourism-related activities and services, proposes the establishment of the following institutions: Tourism regulatory, development and marketing bodies (Directorate of Tourism, Kenya Tourism Regulatory Authority, Kenya Tourism Protection Service, and the Kenya Tourism Board); Kenya Tourism Research Institute; Financial bodies (Kenya Tourism Fund, and Kenya Tourism Finance Corporation); and a Tribunal to handle various disputes arising in the tourism industry.

Of the above-mentioned institutions, establishment of six is pending, namely: Directorate of Tourism, the Kenya Tourism Regulatory Authority, Kenya Tourism Protection Service, Kenya Tourism Research Institute, Kenya Tourism Fund and Tourism Tribunal. Some of the already existing institutions such as KTDC and KTB will be restructured to make them more effective in service delivery (the KTDC will be replaced by a more effective and efficient KTFC), while others will be established. It will be important to review the organizational structure of KTB to make it more effective in 'monitoring standards and performing education' functions. Besides, there is need to expand its funding allocation in order to strengthen the departments of marketing, public relations, and research. In total, the Ministry of Tourism will coordinate 14 institutions (8 old and 6 new ones).

13.5.3 Evaluating Institutional Effectiveness

General Measurement Indicators and Critical Capacity Issues in the Sector

Studies in new institutional economics identify a number of benchmarks of good institutions including: (i) institutional finances – expenditure patterns, revenues, endowments; (ii) institutional strategy; (iii) institutional structure – centralization, professionalism, standardization; (iv) good interaction within and among actors (existence of synergies); (v) compliance; (vi) clear and correct shared objectives (e.g. technical and economic). Clear objectives should cover technical aspects, economic aspects and organizational assignment of responsibilities; (vii) appropriate scale – a right mix of higher and lower level issues vis-à-vis jurisdictional responsibilities; (viii) adaptiveness, and (ix) institutional demographics – gender, unionism, size (Skogan 1997, Cameron 1986, Ostroff and Schmitt, 1993).

In order to measure effectiveness in tourism institutions in Kenya, a structured questionnaire was developed and distributed to 30 institutions. Participants were required to evaluate on a scale of 1 to 10 (where 10 is the highest/best attribute) various indicators of effectiveness in different tourism sector institutions. Average scores were then computed to provide an indicative value of level of effectiveness in the institutions. Twelve (12)senior officers from eleven institutions responded to the questionnaire.

In assessing whether tourism sector institutions are working together effectively towards achievement of medium term targets (for the tourism sector) and Vision 2030, 11 of the institutions interviewed (or 91.7%) indicated a value of 6 (out of 10). About 58 per cent of the participants are of the opinion that the number of institutions in the sector is right in enabling the sector to discharge its mandate.

The Tourism Bill 2010 proposes the establishment of additional institutions and restructuring some of

the current ones. Stakeholders in the sector are fairly optimistic that the Tourism Bill 2010 will ensure effective service delivery in the sector. Ironically, they are doubtful that, although the 14 institutions under the Ministry of Tourism are just right in number, they may not be effective in delivering results for achievement of Vision 2030 (Table 13.4).

Table 13.4: Adequacy of the Tourism Bill 2010

Evaluated Aspect	Sample	Scale (1-10)
Is the Tourism Bill 2010 adequately drafted to ensure effective service delivery in the sector?	9	8
Is the Tourism Bill 2010 adequately drafted to ensure private sector participation in the sector?	9	7
How effective will the additional six institutions be in improving service delivery and efficiency in the sector?	9	7
Given that there will be a total of 14 institutions under the Ministry of Tourism, in your opinion, how effective will they be in delivering an effective and vibrant tourism sector for achievement of Vision 2030?	9	6

There is need to focus on the streamlining of existing organizations with respect to efficiency, effectiveness and follow-up in terms of decisions/ strategies pursued to avoid duplication of roles. There is also need to consolidate resources and roles; the proposed new institutions such as the Tourism Research Institute and the Tourism Regulatory Authority could add value. Better still, tourism research could be outsourced to state corporations other than creating a research institution.

Financing of tourism institutions through industry levies is not a viable option, since the current level of taxation is viewed to be high. In addition, too many institutions will most certainly create conflict unless they are well coordinated, which has been a major weakness.

The new law still recognizes Utalii as the only tourism training institution, whereas a number of public and private sector institutions have been providing training for a number of years. In addition, the country does not have a destination management organization (such as in South Africa) to guide tourism development and marketing. The role is currently played by KTB (destination marketing) and the ministry (destination development).

Table 13.5: Institutions perceived to be redundant

Assessed Institutions	Number of Respondents (out of 11) Perceiving Institution as Redundant
Ministry of Tourism	0
KTDC	4
KTB	0
CTDLT	3
Kenya Utalii College	1
KICC	0
Bomas of Kenya	2
HRA	2
Tourism Trust Fund (TTF)	4

Evaluating how active the main tourism institutions are within the sector, all respondents view the Ministry of Tourism, KTB and KICC as very active. However, 4 out of 11 are of the view that KTDC and TTF are redundant (Table 13.5) and that their roles/mandates should be reviewed. Their presumed ineffectiveness possibly emanates from the low level of funding they receive for onward lending/granting to other public and private tourism institutions. Three (3) out of the 11 respondents, moreover, perceive CTDLT as redundant.

In addition to the above institutions, the Ministry of Tourism works with other key government ministries/institutions that influence tourism service delivery. These include the Ministry of Forestry and Wildlife, Ministry of State for National Heritage and Culture, Kenya Ports Authority, Kenya Ferry Services, Kenya Maritime Authority, Kenya Police and Tourism Police Unit.

However, 11 out of 12 key informants indicated other critical institutions that should play a lead role in service delivery in the tourism sector, but which the Ministry of Tourism is not working optimally with. These include: Ministry of Environment/National Environment Management Authority (NEMA); Ministry of Local Government; Ministry of Transport; Kenya Airports Authority; Kenya Civil Aviation Authority; Ministry of Immigration; Ministry of State for Planning, National Development and Vision 2030; universities/colleges with tourism training programmes; Ministry of Lands; Brand Kenya Board; Kenya Investment Authority; Ministry of East African Community; Ministry of Foreign Affairs; Export Promotion Council; Ministry of Finance; National Disaster Office; Kenya Private Sector Alliance; Kenya Bureau of Standards; and lobby organizations. In addition, the tourism sector should continue working with the public administration sector and to remove cumbersome administrative and licensing procedures and, thus, provide an enabling environment for foreign and domestic investors. An enabling business environment leads to growth of investment, thereby contributing to employment creation and economic growth (Ministry of Tourism, 2010).

Coordination of institutions within the sector

At least 83 per cent of the stakeholders in the tourism sector recognize the Ministry of Tourism as the coordinator for the sector. Other institutions recognized as playing some coordination role include KTF and KTB.

The ministry organizes stakeholders' forums from time to time through circulars, memos, meetings and workshops, and is in charge of formulation, coordination and administration of policy in respect to the sector. The ministry provides overall guidance and policy coordination for the state corporations.

The Kenya Tourism Federation (KTF) is an umbrella organization of tourism associations, and executes decisions through its membership, coordinates private sector institutions, and ensures proper linkage with the Ministry of Tourism and other public sector institutions. KTF is made up of constituent associations (KATO, KATA, KAHC, PERAK, KAAO, EK and MCTA), which are membership-based and take care of different sub-sectors of tourism. The constituent associations take care of membership concerns relating to their specific sub-sectors, while macro issues are cascaded to the federation.

Due to its fragmented nature and widespread linkages, coordination of the tourism sector has been a challenge. Only 4 out of 12 institutions (33.3%) indicated that regular and/or structured meetings are held for all or some of the institutions, with an average of 3 such meetings per institution per year. Half of the respondents also indicated that such meetings would be of great value to the sector.

While the Vision 2030 Delivery Secretariat and the Ministry of Tourism were supposed to form a Vision 2030 Sector Delivery Secretariat to coordinate the entire sector, this has not happened.

Private sector stakeholders are involved in the implementation of decisions, with the tourism associations being instrumental in follow-up and implementation. Executive meetings are chaired by the Minister (ministerial sector forums) and attended by the Heads of Departments and Chief Executive Officers of state corporations. In addition, the Prime Minister's roundtable meetings through KEPSA have attempted to address cross-cutting issues such as infrastructure, taxation and security.

Policy effectiveness

One of the avenues through which the tourism sector seeks to influence policy is through public-private dialogue (e.g., the Prime Minister's roundtable). The private sector has been able to lobby for policy reform (for instance, the Tourism Bill) and policy interventions through tax reforms and regulation

of use of natural assets, such as through restriction of additional establishments in the Masai Mara ecosystem.

Eleven out of 12 key informants (or 91.7%) believe the sector is fairly effective in influencing policy (a scale of 5 out of 10); for instance, with regard to lobbying for higher budgetary allocation from the Treasury. However, some of the proposals submitted to the government by the private sector are ignored, deferred or under-funded. In addition, the sector needs to improve its performance with respect to sharing policy documents with stakeholders for discussion before they are adopted.

The key informants recommended several measures aimed at increasing the policy influence of the sector. These include:

- *Enhancing and demonstrating the actual contribution of the sector to the economy:* In lobbying for higher budgetary allocation, the sector needs to be able to justify its existence beyond the 'contribution to the exchequer' by creating impact at the community level.

- *Strengthening coordination of the institutions in the sector:* The sector (both public and private sector institutions) needs to come together to prioritize their financial requirements and lobby with other government agencies, such as the roads ministry, and to create a Tourism Council that brings together all players for policy advocacy and lobbying. The private sector should be involved in policy setting and planning and not just implementation, through membership in the proposed Council and more regular consultative meetings.

- *Adequate funding of key institutions:* This is critical for institutions, especially those that facilitate investment in the sector.

- *Enhancing tourism policy research:* Proper research and analysis of tourism as an economic activity in Kenya, and its challenges and potential (comparative advantage) is important. Policies and plans should be informed by the evidence emerging from such research.

- *Speedy implementation of the Tourism Act 2011.*

- *Enhancing private sector participation through public-private partnerships.*

- *Revising the entire budgetary process* in order to allocate more financial resources to the productive sectors and the sub-sectors with relatively higher capacity to generate revenue.

Clarity of mandate

The Ministry of Tourism, KTB, KUC and KICC are perceived by 91.7 per cent of stakeholders to have clear mandates, and scored between 70 and 80 per cent in this respect (Table 13.6). All the other institutions in the sector scored 60 per cent.

Table 13.6: Clarity of mandate

Evaluated Institution	Sample	Scale (1-10)
Ministry of Tourism	12	7
Kenya Tourist Development Corporation (KTDC)	11	6
Kenya Tourist Board (KTB)	11	8
Catering and Tourism Development Levy Trustees (CTDLT)	11	6
Kenya Utalii College (KUC)	11	7
Kenyatta International Conference Centre (KICC)	11	7
Bomas of Kenya (BoK)	11	6
Hotel and Restaurants Authority (HRA)	10	6
Tourism Trust Fund (TTF)	11	6

Note: "Sample" implies the number of institutions that responded to the interview question; "Scale" (based on values 1–10, with 10 as the highest) is calculated as an average of the values given by the respondents.

This suggests that the problem of clash of mandates may not be very serious, although further alignment and harmonization could help. In particular, there is need to rationalize activities and mandates of similar institutions in order to avoid fragmentation and duplication of activities and to ensure that funds are concentrated in projects that will create maximum impact.

Strategy planning

Broadly speaking, existence of annual work plans aligned to a strategic plan is indicative of the proper management of an institution and its likelihood of effective service delivery. Although the Ministry of Tourism has a current strategic plan in place (2008-2012) and the Tourism Bill has been enacted into law, the development of various strategies envisaged once the proposed institutions are established is pending (Table 13.7).

Nevertheless, at least 80 per cent of stakeholders perceive key institutions in the sector to be fairly effective in working within their current strategic plans and annual work plans (with most scoring 50-70%), and have been fairly effective in creating opportunities for private sector participation over the last 3-5 years (with most of them scoring 60-80%, Table 13.8). The effectiveness of tourism promotion and marketing in key source markets received a score of only 50 per cent.

Financing

Two key challenges are hindering faster growth of the tourism sector. The first is limited access to credit facilities and financial services. The financial market mainly provides short- and medium-term financial products, while the tourism sector requires long-term financing. The second is lack of a sustainable public funding mechanism to support products and facilities development, refurbish the existing facilities and diversify the sector's products.

Although tourism is a key sector of the Kenyan economy, contributing over 11 per cent of GDP, funding levels for the ministry have remained very low over the last three (3) years. According to the estimate of the Ministry of Tourism, institutions under the ministry require at least Ksh 6 billion annually to discharge their services effectively, yet the current funding is about Ksh 2 billion (Ministry of Tourism, 2010b). Over the last three (3) years, the Ministry of Tourism received about 35.5 per cent of the requested level of funding and absorbed about 92.7 per cent. All stakeholders interviewed felt that the level of government priority to funding flagship projects has been below average over the last 3-5 years, with a score of 30 per cent only.

To implement various objectives and activities outlined in the Ministry of Tourism's Strategic Plan for 2008/9–2012/13, the ministry estimates that Ksh 115 billion is required.

The Tourism Act 2011 provides for improved resource mobilization for the sector through the Kenya Tourism Fund and Tourism Finance Corporation. According to the Act, funding for various statutory institutions will include moneys provided by Parliament; moneys that may accrue to or vest in the institutions in the course of performance of their functions as body corporates (from movable and immovable property, from contracts or other transactions, donations, grants and gifts); and any other moneys that are approved by the Minister for Finance.

For the Kenya Tourism Fund, additional funding sources will include the Tourism Levy and other moneys that may be levied upon tourism activities and services; 5 per cent of the total annual tourism earnings as may be made to the Fund by the Exchequer; income from investments made by the Board of Trustees; and funds generated from partnerships, financing agreements, protocols or memoranda of understanding with development partners. These funding provisions will need to

be reviewed from time to time based on results of monitoring and evaluation.

There is a relationship between size of budgetary allocation to tourism promotional and marketing activities and level of tourism receipts achieved in a particular country (Table 13.9).

Over the period 2007–2010, the government allocated 1.7–3.7 per cent of receipts to the tourism sector (promotional support activities), while institutions in the four comparator countries (South Africa, Malaysia, Singapore and Egypt) received allocations of 1-1.5 per cent of revenue received from the tourism sector. The returns from this relatively higher allocation in terms of relatively faster growth in tourism revenue should be monitored to ensure that the scarce resources are being allocated well and are being applied efficiently.

Adequacy of human resources

At least 50 per cent of the key informants in the tourism sector assert that the lead institutions in the sector are not sufficiently endowed with human resources to function effectively. With exception of HRA and TTF, which are viewed to be performing below average (scoring about 40%), the rest of the institutions are average performers (scoring 50-60%) in terms of human resource endowment (Table 13.10).

The Ministry of Tourism, for example, has a current staff complement of 185 of various cadres, which is about 64.7 per cent of the approved establishment. This has been occasioned mainly by natural attrition and lack of replacements as a result of the freeze on recruitment in the public service (Ministry of Tourism, 2010). There is need to upgrade skills in the workforce, rationalize staff capacity, improve the work environment, and mainstream the public sector integrity programme as planned in the Ministry of Tourism Strategic Plan 2008–2012. In addition, there should be better regulation of the training provided by private institutes to ensure quality, effective partnership and harmonization between the public and private training institutions. An overhaul of the curricula is needed to ensure that training matches the requirements of the modern and increasingly sophisticated tourism industry.

The 2010 constitutional order and tourism institutions

The Constitution of Kenya, promulgated in August 2010, is designed to re-distribute some political and economic power away from Nairobi to the other 46 counties. Under the new system, the national government will provide at least 15 per cent of the revenue collected annually for distribution to the county budgets, with county officials responsible for raising additional revenue from specified sources. The precise share of the national revenue that will go to the county kitty and the formula for sharing the allocated resources among the 47 counties are still being worked out. The devolution will encourage county officials to recruit foreign and domestic investors, thereby creating economic opportunities at the county level.

Regarding tourism, county governments will have a greater say in how tourism revenue is generated and utilized. The Tourism Act 2011 advocates for involvement of the local communities in tourism matters in order to spread tourism benefits.

Eleven out of the 12 key informants interviewed believe[4] that the 2010 Constitution will enhance tourism development in the country, while 75 per cent of them believe that the counties are not well prepared to build effective tourism industries under the new constitutional order (with a score of only 30%).

Devolution of resources and government will lead to more focus on development of local tourism resources and products, including infrastructure, and will enhance accountability and independence of the state actors (i.e., SAGAs) in making sound economic decisions. The devolved units will generate

own revenue and receive county allocations. This will expand local tourism products in the respective counties. In addition, county governments should be given the authority to regulate local tourism but within boundaries or standards set nationally, given the obvious externalities.

Most of the key informants are of the view that regional or county level tourism boards are essential for the country to build a vibrant tourism industry. Other institutions recommended for the same purpose include strong tourism departments or county tourism product development committees, strong regulatory institutions (including environmental protection agencies) at the national and county levels, tourism training institutes and strong county government structures to provide infrastructure and the enabling environment.

In addition, country governments need to address the issue of land availability to develop tourism establishments.

Tourism infrastructure and service delivery

Eleven out of 12 (91.7%) of the respondents in lead tourism institutions assert that Kenya's tourism infrastructure is poorly placed (giving it a score of 40% only) to enable achievement of the target of 3 million arrivals and Ksh 200 billion in revenue and increase average tourist spending from the current Ksh 40,000 to Ksh 70,000 by 2012. Infrastructure that is still inadequate includes roads to and within the game parks, security especially in remote areas neighbouring Somalia, high class accommodation facilities, inadequate facilities such as museums, additional conference facilities especially in Mombasa, among others.

The tourism institutions need to work closely with the physical infrastructure sector to ensure that infrastructural challenges are addressed. It may be imperative to form a special tourism infrastructure taskforce to spearhead collaboration with relevant agencies.

Other pertinent institutional effectiveness issues

Security services

The tourism industry is very sensitive to security, political and macroeconomic stability. The Tourism Act 2011 provides for the development of a Kenya Tourism Protection Service and related institutional structures to guarantee security to all tourists. A Police Unit (Tourist Police Unit) and a cross-sectoral National Tourism Crisis Committee have been constituted to coordinate tourism security concerns (Ministry of Tourism, 2010). There is need to build the capacity of the tourism police in terms of manpower, relevant equipment and more funding. In addition, there is need to fast-track promotion of national cohesion through justice, peace and reconciliation in order to create the image of Kenya as a peaceful tourist destination.

Information technology

The quality of tourism sector data is low and key variables are not regularly monitored. It is envisaged that the proposed Kenya Tourism Research Institute will, in collaboration with relevant lead agencies and stakeholders, establish a comprehensive tourism database for the sector. There is need to ensure that high-speed voice and data technology is accessible at all corners of the country to enable 'business travellers' to keep in touch with their firms while on vacation in Kenya. As a result of little budgetary resources for innovation, research and development, there has been limited innovation in the tourism sector, yet this is crucial for value addition and introduction of new products. With the landing of four (4) fibre optic cables in Kenya over the last couple of years, the quality, speed and cost of telecommunication services have considerably improved. The tourism sector should take advantage of this to innovate and become more competitive.

Environment

Promotion of environmental conservation is one of Kenya's specific strategies required to support the economic pillar flagship projects and achieve the Millennium Development Goals. The increase in human population and climate change among others, are some of the environmental challenges that adversely affect investments, tourism and economic growth. Institutions in the tourism sector need to play a key role in contributing to environmental sustainability by ensuring that new and existing tourism businesses adhere to the best environmental practices. In this regard, because the sector works closely with the environment, water and irrigation sector, there is need to harmonize environment-related laws for better environmental planning and governance.

Regional integration

The signing and ratification of the EAC Common Market Protocol (CMP) provides numerous opportunities for the tourism sector in form of increased market for the sector products, free movement of factors of production, and marketing of the region as one tourist destination. There is need to strengthen the EAC secretariat to promote tourist arrivals from the EAC states – visiting Kenya as leisure or business travellers, conference or sports tourists, or even coming to Kenya to seek medical services. In order to reap these benefits, the EAC secretariat/ministry needs to sensitize partner states within the EAC bloc to eliminate perceived fear of loss of national sovereignty, loss of revenues and unemployment. In addition, there is need to deal with persistent non-tariff barriers to trade in goods and services.

Promotion of domestic tourism

KTB requires more funding to promote domestic tourism and conduct continuous campaigns aimed at changing perceptions of locals to create a culture of tourism as an everyday thing as opposed to seasonal. Players within the tourism industry also need to change their attitudes in order to provide products/services that are affordable to locals. The government could provide incentives to corporate institutions (such as tax relief) in order to encourage stakeholders in the private sector to offer products that are affordable to locals.

Severity of challenges/obstacles in the sector

In all the nine institutions assessed, finance is the severest challenge facing them, with severity scored at 90 per cent (Table 13.11).

The other severe challenges are human resource endowment, lack of autonomy and inadequacy of

Table 13.7: Status of strategic planning of the public tourism sector

Institution	Current / Proposed Strategy	Status of Strategy
Ministry of Tourism	• National Tourism Policy	• 2008-2012 Strategic Plan in use • First National Tourism Policy formulated under Sessional Paper No. 8 of 1969 • Updating of the first version completed in 2006 • Tourism Bill 2010 enacted into law in 2011
KTB	• National Tourism Marketing Strategy	• National Tourism Marketing Strategy pending completion

Institution	Current / Proposed Strategy	Status of Strategy
KICC	• National MICE Strategy in collaboration with KTB	• KICC Strategic Plan 2008-2012 • Strategic Plan 2011-2015 for the National MICE committee and secretariat
Bomas of Kenya	National Cultural Tourism Strategy	Pending
Directorate of Tourism	• National Tourism Strategy • Monitor effectiveness of the implementation of the National Tourism Policy and Act • Integrate tourism development area plans and beach management strategy	Pending
Kenya Tourism Regulatory Authority	• Establish criteria for standardization and classification of tourism facilities and services • A code of practice for the tourism sector • Ensure development and implementation of high quality tourism standards and services	Pending
Kenya Tourism Protection Service	• Formulate policies, in consultation with the national security agencies, regarding the safety and security of visitors and hosts in respect of all tourist destinations in the country	Pending
Kenya Tourism Research Institute	• Strategies and techniques for product development and marketing • Integrated tourism development area plans • Establish a comprehensive tourism database	Pending
Kenya Tourism Fund	• Support the development of tourism products and services • Strategy for financing and marketing of Kenya as a tourist destination through KTB • Develop a National Tourism Information Management System	Pending
Kenya Tourism Finance Corporation	• Strategy for financing development, expansion and maintenance of tourism facilities and services • Provide business advisory services to the tourism sector and • Establish a reserve fund	Currently KTDC
Tourism Tribunal	• A tribunal to settle (hear and determine) disputes arising in the tourism industry	Pending

Table 13.8: Effectiveness of strategy and public-private partnerships

Institution Assessed	Effectiveness of Strategy and Annual Work Plan		Effectiveness in Creating Opportunities for PPPs	
	Sample	Scale (1-10)	Sample	Scale (1-10)
Ministry of Tourism	10	6	12	6
Kenya Tourist Development Corporation (KTDC)	6	5	9	5
Kenya Tourist Board (KTB)	7	6	10	8
Catering and Tourism Development Levy Trustees (CTDLT)	8	7	9	6
Kenya Utalii College (KUC)	6	6	9	6
Kenyatta International Conference Centre (KICC)	6	5	10	6
Bomas of Kenya (BoK)	6	5	9	3
Hotel and Restaurants Authority (HRA)	5	5	8	4
Tourism Trust Fund (TTF)	6	4	9	6

Note: According to the KAHC, the Hotel and Restaurants Authority does not have a strategic plan in place yet.

oversight. These results underline the importance of finding innovative funding solutions for state corporations. In addition, the State Corporations Advisory Committee (SCAC) should study best practices of providing state corporations with the optimal level of autonomy and oversight to enhance effectiveness in the state corporations sector.

13.6 Transforming Institutions for Infrastructure and Economic Services Delivery

The challenges facing the delivery of infrastructure and economic services in a manner that addresses the mandates of the Constitution of Kenya 2010 and Vision 2030 revolve around rationalization and effective coordination of institutional mandates, more efficient utilization of resources, ramping up the building of capacity, and an increased focus on integrated planning and management to ensure better development outcomes.

Rationalization and effective coordination

The existing mandates of various infrastructure and economic services delivery institutions are many times unclear or conflicting. Operationalization of counties, without a review of these, will only make matters worse. Therefore, starting at the national government level, it will be important that mandates of institutions be rationalized with a view to reducing the number of institutions and creating new ones only when mandates have been clearly determined. A clear clarification of and separation of policy, regulatory and service delivery roles should be an imperative.

Enhanced utilization of resources

The utilization of existing resources is a source of concern in terms of whether value for money is actually being achieved. The many documented cases of cost overruns and poor quality of infrastructural facilities has been a running theme on most public projects. One of the key concerns is the clear lack of separation of roles in the sector. This must be achieved as a matter of priority in all the infrastructure service delivery sectors. Also, there is need for an independent institution whose task and mandate would be to provide quality and value for money audits, initially to large scale and critical flagship and other projects and programmes. This can be expanded to other projects as experience is

Table 13.9: Comparison of public sector allocation to tourism sector and revenue for selected countries

Year		Kenya	South Africa	Malaysia	Singapore	Egypt
2007/2008	Tourism Revenue (US$ million)	1,045.71	8,418.00	13,834.80	9,791.70	9,303.00
	Allocation for Sector (US$ million)	17.76	98.52	193.62	133.15	67.45
	Allocation as % of Tourism Revenue	1.70	1.17	1.40	1.36	0.73
	Arrivals (Millions)	1.82	9.09	20.98	10.30	10.61
2008/2009	Tourism Revenue (US$ million)	678.52	9,500.00	14,282.80	10,555.60	11,600.00
	Allocation for Sector (US$ million)	24.42	86.76	155.93	140.15	110.31
	Allocation as % of Tourism Revenue	3.60	0.91	1.09	1.33	0.95
	Arrivals (million)	1.20	9.60	22.05	10.10	13.00
2009/2010	Tourism Revenue (US$ million)	825.75	10,475.00	15,559.10	8,857.10	12,574.00
	Allocation for Sector (US$ million)	30.78	81.69	n.a.	145.88	59.55
	Allocation as % of Tourism Revenue	3.73	0.78	n.a	1.65	0.47
	Arrivals (million)	1.49	9.90	23.60	9.68	n.a

Source: Annual Reports of Tourism Marketing Boards of the respective countries[8]

Table 13.10: Adequacy of human resources

Evaluated Institution	Sample	Scale (1-10)
Ministry of Tourism	7	5
Kenya Tourist Development Corporation (KTDC)	6	5
Kenya Tourist Board (KTB)	6	6
Catering and Tourism Development Levy Trustees (CTDLT)	7	6
Kenya Utalii College (KUC)	6	5
Kenyatta International Conference Centre (KICC)	6	6
Bomas of Kenya (BoK)	5	5
Hotel and Restaurants Authority (HRA)	5	4
Tourism Trust Fund (TTF)	6	4

gained and capacity built. In addition, the Office of the Auditor General should establish a division within it with the requisite capacity.

Integrated planning for effective service delivery

In many instances, the pursuit of development outcomes is not closely linked to the mode of infrastructure service delivery. A simple example would be, if we wanted to improve health outcomes, should we invest in building more health facilities or improve the road network or increase the supply of potable water? The answer to this and other similar questions cannot be a simple one. But it needs to be answered. This requires that there be a stronger focus on integrated development planning linked to resource mobilization efforts.

ENDNOTES

1. See the Global Competitiveness Report by the World Economic Forum for the detailed methodology and tests of robustness.
2. Adapted from: http://www.tourism.go.ke/ministry.nsf/doc/service_charter09.pdf/$file/service_charter09.pdf
3. The Tourism Bill 2010 was published by the Minister for Tourism for introduction to Parliament in the Kenya Gazette Supplement Bills 2010 dated 17th November, 2010. The Bill is a product of several public awareness and participation campaigns. It has been a long wait since Kenya has never had a Tourism Bill since Independence; http://www.tourism.go.ke/ministry.nsf/pages/news_25_11_10?opendocument.
4. However, the 'strength' of this belief is only 60 per cent.

Table 13.11: Severity of challenges facing key tourism institutions

Institution	Human Resources		Finance		Lack of Autonomy		Adequacy of Oversight		Clarity of Mandate		Duplication		Corruption	
	Sample	Scale	Sample	Scale	Sample	Scale	Sample	Scale	Sample	Scale	Sample	Scale	Sample	Scale
Ministry	6	6	6	9	5	5	5	6	5	3	5	3	5	2
KTDC	5	6	5	10	4	5	4	6	4	4	4	2	4	3
KTB	5	6	5	10	4	5	4	5	4	2	4	2	4	3
CTDLT	6	5	6	6	5	4	5	5	5	3	5	3	5	4
KUC	5	5	5	7	4	5	4	7	4	4	4	4	4	5
KICC	5	4	5	8	4	6	4	5	4	6	4	5	4	3
Bomas of Kenya	4	7	5	8	4	6	4	7	4	6	4	5	4	3
HRA	4	9	4	10	4	9	4	8	4	4	4	2	4	3
TTF	5	7	5	9	4	8	4	8	4	4	4	4	4	2
Average	5	6	5	9	4	6	4	6	4	4	4	3	4	3

Note: "Sample" implies the number of institutions that responded to the interview question; "Scale" (based on values 1–10, with 10 as the severest), is calculated as an average of the values given by the institutions in the sample.

PART IV

Conclusions, Policy Issues and Recommendations

This last part provides a brief summary of key conclusions arising from the various policy issues raised in this report and also some major recommendations. More importantly, it outlines specific proposed reforms and institutional priorities identified in Part III .

Chapter 14

Conclusions, Policy Issues and Recommendations

14.1 Introduction

Kenya is in the midst of a major shift in the management of its affairs. The institutions that will arise out of the implementation of the Constitution of Kenya 2010 and the Kenya Vision 2030 will be operative in a context that is manifestly different from the past. Moreover, Kenya is facing serious challenges such as rising youth population, food insecurity, unemployment, frequent occurence of drought and consequent water scarcity, climate change, among others. There is need to ensure that institutions are not only able to identify the challenges the country faces but also to rapidly design responses and marshal the requisite resources to address the challenges identified.

While implementing the Constitution of Kenya 2010 is a critical step in creating confidence about Kenya's progress towards improved governance, this will not be good enough. Given the development challenges, and based on Vision 2030's imperative of "business unusual", institutions will need to be geared for exceptional performance at all levels. Schwab (2011) posits that achieving great transformation requires recognition of four imperatives. The first is an accounting for fundamental power shifts that are taking place and will continue to occur in the political, economic, social and other spheres. Governance processes should be built to accommodate "newcomers", including non-state actors in a manner that recognizes their usefulness and capabilities. A second imperative is that with regionalization and globalization, there is need to acknowledge and leverage diversity. The third imperative relates to recognition of the impact of globalization and the technological innovation it has engendered. These have implications for the nature of economic growth strategies that must imbue shared growth frameworks. The fourth imperative demands recognition of the need to increase firm, regional and national level productivity if the necessary employment opportunities are to be created.

In designing and reforming institutions, the following matters will be critical:

14.2 Principles for Institutional Design

As the Constitution of Kenya 2010 is being operationalized, the design of new institutions must ensure that duplication of mandates is eliminated or minimized. The execution of the mandates must be well coordinated, with clear instruments for conflict resolution and regulation being operationalized. To

achieve this, there must be a clear understanding, conceptualization and operationalization of Schedule 4 of the Constitution of Kenya 2010 and attendant provisions.

14.3 Engendering National and County Government Priorities and Linkages

Creation of a two-tier government under the Constitution of Kenya 2010 has fundamentally shifted the way in which the processes of governance and development in Kenya are executed. It will, therefore, be critical that institutions for effective management of the processes of policy formulation, implementation, review and evaluation are created. This should be done in a manner to enhance coordination and cooperation within, between and across the national government and county government.

14.4 Building Effective Capacity

Available evidence shows that there is very little being done to address the issue of institutional capacity: human resource, facilities, and equipment. Implementation of the Constitution of Kenya 2010 will exacerbate this challenge if not well managed. Experiences in countries that have decentralized, almost all on a much smaller scale than Kenya, have shown that they have all failed because of lack of adequate capacity. This is a pitfall that Kenya could avoid by internalizing the ramifications of Schedule 4 on capacity needs.

14.5 Structure and Organization of Government

The structure and organization of government should be done in a manner that will focus on identifying, seeking and building technical competency. Institutions for managing and harnessing political and other pressures that will emerge from a constitutionally-mandated two-tier government need to be put in place across all sectors. The ongoing administrative and sectoral reforms must immediately do a stock take and account for the implications of the Constitution of Kenya 2010. This is important if public policy formulation and implementation is to be effective within the devolved governance framework. The effectiveness of these institutions will be predicated on capacity at all levels to meaningfully engage.

14.6 Rebuilding Public Trust

Over an extended period of time, Kenya has witnessed a reduction of public trust in institutions of governance, including the ability to shape broad social and economic policy. One of the key adverse consequences of this state of affairs is the manifest desire by citizens to be engaged in making the simplest of administrative decisions. Left unchecked, this will result in increased transaction costs as well as reduced capacity and capability to respond to rapidly changing natural, social and economic environments. There are already murmurs about what the implementation of the Constitution of Kenya 2010 will mean for the cost of government.

Therefore, rebuilding public trust in governance institutions must be imperative while redesigning reform measures. Trust will be key in reducing transaction costs in public affairs, especially in circumstances where relationships between various actors will be inherently asymmetric in the short to medium term. As noted by Blomqvist and Ståhle (2000), this will require a strong focus on ensuring technical competence, engendering goodwill and inculcating the behaviours expected by the Constitution. Focusing on building strong records of good performance by the various institutions and communicating the same is necessary. Implementing these interventions will be critical in dealing robustly with the "deficit of trust". Dealing with this "deficit of trust" should be the cornerstone that helps address the significant challenges emanating from the changing global economic environment, the coming natural resource boom, the demographic transition

underway, and the consequences of climate change, amongst others.

14.7 Strengthening Public Communication

In the brave new world that Kenya is entering, success will depend on better and more focused partnerships between institutions for delivery of developmental outcomes. This means that communication will have to be enhanced at the national and county government level, and between and across government.

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KIPPRA acknowledges generous support from the Government of Kenya (GoK), the African Capacity Building Foundation (ACBF), and the Think Tank Initiative of IDRC.

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