The KENYA INSTITUTE for PUBLIC POLICY RESEARCH and ANALYSIS

Policy Brief

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Thinking Policy Together

Building Resilience and Sustainable Economic Development in Kenya

Overview

This Policy Brief is based on the Kenya Economic Report 2022, themed "Building Resilience and Sustainable Economic Development in Kenya". The Report analyses the contexts, policies and institutional frameworks that support sustainable development by building resilience across various sectors of the economy. The report covers a review of recent macroeconomic performance and discusses the Kenya's medium-term prospects. It focuses on building resilience for manufacturing, trade, livestock in arid and semi-arid lands, and creative economy. It also covers digital economy, national values, governance, and science, technology and innovation as key drivers in building resilience. As such, the scope of the report interphases the pillars of economic resilience (macroeconomic stability, social-economic development, institutions/good governance), the pillars of the Kenya Vision 2030 (economic, social and political), and the targets of the Sustainable Development Goals that seek to build resilience and nurture the required transformations through science, technology and innovation, and the digital economy.

Recent Macroeconomic Developments and Medium-Term Economic Prospects

Kenya's economy rebounded in 2021 with a growth rate of 7.5 per cent. The services sector expanded by 15.4 per cent, industrial activity by 9.2 per cent while the agriculture sector contracted by 0.2 per cent due to drought conditions across the country. Total employment grew by 5.6 per cent while inflation remained within the government target range. These developments were supported by targeted fiscal interventions, accommodative monetary policy that ensured adequate liquidity in the market while anchoring inflation, and mass vaccination drive that saw mobility restrictions vacated.

Government revenue bounced back in the first half of fiscal year 2021/22, with virtually all tax heads recording above target collections. At the end of 2020/21, fiscal deficit stood at 8.4 per cent of Gross Domestic Product (GDP) compared to 7.4 per cent in 2019/20 and 7.5 per cent projected for 2021/22. Public debt increased to 66.2 per cent of GDP but was within the sustainability threshold. Current account deficit stood at 5.5 per cent of GDP in 2021 compared to 4.8 per cent of GDP in 2020. The secondary income account, especially receipts from diaspora remittances and international travel remained resilient.

While growth prospects over the medium-term are positive, the country faces downside risks, including dynamics and uncertainty on the COVID-19 pandemic, weather-related shocks, political uncertainty with the August 2022 general elections, and a surge in commodity prices compounded by the geo-political tension between Russia and Ukraine. Nevertheless, the country is leveraging on mass COVID-19 vaccination drive and digitalization to sustain economic recovery.

To maintain macroeconomic stability, which is a key enabler for sustainable development:

1. A growth-oriented fiscal policy is preferred, with targeted fiscal support to the services, industrial and agriculture sectors, for accelerated and sustainable economic recovery. This is to be complemented with accommodative monetary policy to support recovery by ensuring there is adequate liquidity in the market, and inflation is well anchored. Furthermore, fast-tracking a system-wide implementation of risk-based pricing will enhance conversion of liquidity into credit to support private sector activity. In addition, expanding irrigated agriculture will ensure adequate food supply throughout the year, muting food inflationary pressures.
2. Fiscal stability is a priority. This is to be achieved through revenue enhancement measures such as expansion of the tax base and curbing tax evasion, increased efficiency in public spending and strict adherence to medium-term fiscal consolidation plan. Further, it is important to secure the gains made in the health sector during the COVID-19 period and further prioritize

investments to strengthen the health systems in enhancing human capital development.

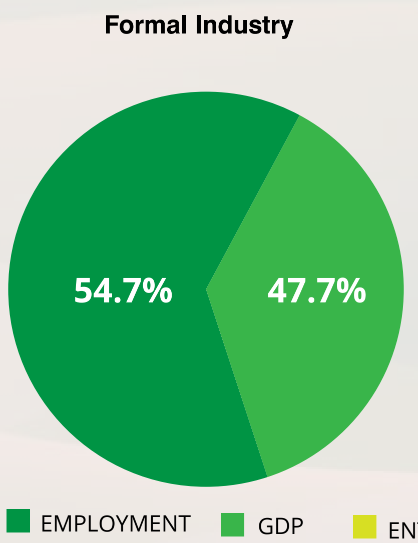
Building a Resilient Manufacturing Sector for Sustainable Development

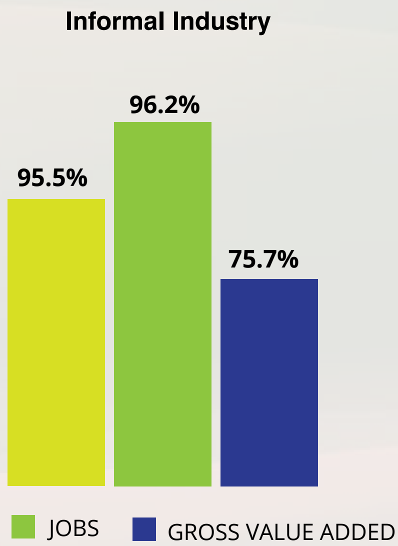
The manufacturing sector supports economic development through its forward and backward linkages with other sectors in the economy. Manufacturing accounts for 47.7 per cent and 54.7 per cent of the formal industrial GDP and employment, respectively. Further, manufacturing accounts for 95.5 per cent of enterprises, 96.2 per cent of jobs and 75.4 per cent of gross value added in the informal industrial activities. Manufacturing contracted by 0.1 per cent in 2020, rebounding to record a growth rate of 6.9 per cent in 2021. Despite its potential to contribute to economic development, manufacturing contribution to national GDP remains below the 15 per cent target. The sector faces significant downside risks, including droughts, election cycles, global recessions, and increase in global oil prices. Further, the resilience of manufacturing is weakened by high concentration of informal Micro and Small Enterprises (MSEs), dominance of low technology manufacturing, weak innovation ecosystem and technology adoption, skills deficits for technological upgrading, and limited access to affordable financing and quality infrastructure. Notwithstanding the various challenges, the COVID-19 pandemic revealed latent opportunities in diversifying manufacturing in Kenya.

To build a resilient manufacturing sector for sustainable development:

1. It is important to incentivize diversification of manufacturing into medium and high technology activities using fiscal incentives, especially on financing of Research and Development (R&D) investments. The private sector can increase financing of R&D by leveraging on the Second Schedule of the Income Tax Act Cap. 470 that provides for tax deductibility of expenditures on scientific research and contributions to universities and research institutes that undertake scientific research related to the line business. Further, it is important to support the adoption of industry 4.0 with supportive infrastructure and skills development, particularly those related to Science, Technology, Engineering and Mathematics (STEM) courses. Measures to promote financing of transition to industry 4.0, such as Internet of Things (IoT), Artificial Intelligence (AI), advanced robotics, and big data analytics are also imperative. A gradual shift to industry 4.0 through these supportive measures would aid a gradual shift for overcoming incompatibility between the old and new technology.

2. For the MSEs that dominate enterprises in manufacturing, and which are disproportionately affected by shocks and stressors, it is imperative to mainstream disaster risks management in the policy documents. Further, there is need to fast-track implementation of the Sessional Paper No. 5 of 2020 on MSEs Policy, as it provides for measures in skills upgrading, infrastructure, financing, technology and innovation, which





is essential for building resilience. Support accelerated innovation with market incentives such as public procurement preferences and export markets promotion, and fiscal incentives that compensate investors for risks assumed investing in innovation within frontier high technology manufacturing.

Building a Resilient Economy Through Trade

Trade is indispensable in building economic resilience, given its linkages to other sectors such as agriculture, manufacturing and services. For Kenya to achieve the potential of the trade sector, there is need to mitigate the existing obstacles that hold back the sector. First is to finalize the implementation of the Medium-Term Plans (MTP's) I-III proposed trade flagship projects that are still lagging, including the construction of one tier markets that are yet to be completed. Second, is the under-utilization of existing Generalized System of Trade (GSP) arrangements under trade agreements such as the Economic Partnership with the United Kingdom, which holds back the potential of the trade sector as Kenya has only utilized 2 per cent between 2018 and 2021. Third, the concentration of goods and services to a few varieties and export markets limits the sectors performance. Fourth, trade performance remains sensitive to negative shocks such as increase in crude oil prices, droughts, and the COVID-19 pandemic.

To enhance trade performance and achieve economic resilience it is imperative to:

1. Strategize in taking advantage of the opportunities brought by operationalization of the African Continental Free Trade Area (AfCFTA) and other trade agreements. This includes mapping out all the products exported to and imported from African countries to increase trade performance. The current export to only 28 per cent of African countries signals existence of a huge market that has potential to enhance trade revenue. The mapping out of these products will help improve export promotion strategies in Africa for Kenya. Review the National Trade Policy (NTP) of 2016 to capture the trade dynamics arising from the AfCFTA and other trade agreements that have been signed by Kenya. In addition, pursue free trade agreements with focus on products that offer Kenya high returns for exports and imports. This also calls for collaboration between the Ministry of Industrialization, Trade and Enterprise Development and other agencies such as Export Promotion Council, Kenya Association of Manufacturers and the private sector to help develop export promotion strategies and increase trade revenue.

2. Take deliberate efforts to boost efficiency and scale of domestic trade. This includes deepening information on products that utilize Customer to Government (C2G) and Customer to Business (C2B) mobile money services by mapping of government services and ministries that use online services and providing this information to all mobile money outlets and government offices. Further, it is important for the government in collaboration with the private sector to set up a development fund that advances financial support to traders in agriculture and services sectors at affordable interest rate. The financial support provided to these two sectors will improve the quality and competitiveness of goods and services.

Enhancing a Resilient and Sustainable Livestock Industry in Kenya

The livestock sub-sector plays a significant role in steering economic growth in Kenya and serves as a cornerstone for millions of livelihoods, particularly in ASALs. The potential of the livestock production in ASALs and the related value chains is, however, curtailed by recurrent shocks and stressors in the form of extreme weather hazards, desert locust invasions and livestock diseases, conflicts/insecurity, and market/economic shocks. The shocks and stressors, which have increased in frequency and intensity over the years, threaten food security, welfare of communities and economic stability of ASALs with consequent ripple effects across the country. Despite the significant response action to mitigate the effects of shocks and stressors in ASALs' ecosystems, there are gaps in the sub-sector's ability to anticipate, prepare for, reduce the impact, and retain function through the disturbances, and the capacity for learning and adaption to deal with changing circumstances.

To enhance resilience and sustainability of the livestock industry:

1. Enhance livestock production system by exploring climate smart measures such as silvopastoral system (the practice of integrating trees, forage, and the grazing of livestock in a mutually beneficial way), which entails intensification of livestock production based on sustainable natural processes. Climate smart approaches present an opportunity to respond to climate change and sustainable utilization of ASALs. Encourage partnerships to adequately finance investments in the sector and integrate pastoralists into the livestock value chain by building their capacities to improve the quality of livestock and livestock products and fully implement the various strategies and programmes currently being developed. Further, enhance access to support services to include adequate extension services and significant affordable livestock credit and insurance through partnerships. This can be achieved effectively and efficiently by strengthening the livestock producer organizations in ASALs for more organized service delivery.

2. Adopt a rural development strategy for ASALs that integrates both economic and social activities. This includes development of well-equipped local processing centres; mobile service delivery programmes, water and market infrastructure; livestock trekking/migratory corridors; and grazing reserves. Further, encourage cultural heritage activities to minimize social polarization that can escalate intercommunal conflicts between pastoral communities or between pastoral and non-pastoral communities. All these should be supported by an efficient and effective data management system in planning, decision making, monitoring and evaluation processes.

Building Resilience through the Digital Economy

The digital economy is not only important in supporting economic growth and development but also in building a resilient economy. The digital economy is important for building economic resilience with evidence showing that a 10 percentage point increase in broadband Internet penetration accelerates economic growth by 1.35 percentage points in developing countries. Internet enabled digitization helps to mitigate the economic disruption brought on by shocks and emergency situations such as a pandemic. The Kenya Digital Economy Blueprint (2019) defines the digital economy as "the entirety of sectors that operate using digitally-enabled communications and networks leveraging Internet, mobile and other technologies" irrespective of industry. Digital economy is also defined as composed of the firms providing digital goods and services, either for final or intermediate consumption.

Although Kenya has made significant progress in the digital economy space, there are challenges with limited interoperability of government information systems, absence of a critical mass of people with advanced digital skills, and existence of a digital divide due inadequate broadband internet network coverage.

To build resilience through the digital economy:

1. As a priority, enhance interoperability of government information systems by reviewing and developing a framework for legal, technical, organizational and semantic layers of interoperability. Also, focus on increasing the

Business to Customer (B2C) segment by building the e-commerce capability on the customer (household side) and enhance reach and last mile connectivity in the e-commerce value chain. Further, increase connectivity in underserved areas and make broadband services and devices affordable to address the digital divide.

2. Further, enhance growth and entrenchment of digital skills across the country by reviewing and enhancing existing programmes in the education sector for effectiveness at all levels. In addition, foster growth and development of innovation driven entrepreneurship by building advanced digital skills of entrepreneurs and providing a dynamic policy and regulatory environment that is responsive to the rapidly changing global technologies to ensure global competitiveness.

Leveraging on Science, Technology, and Innovation (ST&I) for Building a Resilient Knowledge-Based Economy

Science, Technology and Innovation (ST&I) is recognized globally as a key driver of sustainable development. ST&I supports in building a resilient knowledge-based economy. The government is implementing education system reforms to develop skills, including introduction of CBC focused on development of skills and their application in real life situation, increasing capacity to offer Science, Technology, Engineering and Mathematics (STEM) courses at the universities and revamping of the Technical and Vocational Education Training (TVET) institutions. However, there is a significant gap of researchers in STEM fields. Also, while there is a significant progress in developing digital, space, energy, medical research, biotechnology, and nanotechnology infrastructures for ST&I, Kenya is yet to harness the enormous benefits from space, biotechnology and nanotechnology economies.

Significant strides in innovation products were witnessed during the COVID-19 pandemic, but innovators and innovation centres in the country are constrained by limited funding, coupled with inadequate framework to support the identification, nurturing, and scaling up of innovations. While the National Research Fund has been established, research funding remains below the targeted 2 per cent of GDP as provided in the ST&I Act 2013.

In addition, absence of techno parks and silo mentality both in the academia and the industry limits strong academia-industry linkages. Further, absence of the envisioned national ST&I policy hampers a coordinated approach in ST&I. To strengthen the role of ST&I in building sustainable and resilient knowledge-based economy, there is need to:

1. Promote Public Private Partnerships to invest in infrastructure, particularly in space, medical research, biotechnology, and nanotechnology and in skills development for anticipation and smart preparedness mainly relating to environmental shocks/stressors. This calls for bringing on board the private sector to participate from the onset in execution of the targeted projects. Further, develop and implement collaborative innovation framework for identifying, nurturing and scaling up various categories of innovations by involving all the key stakeholders, including innovators, government institutions, industries and development partners. The developed framework should create an enabling ecosystem to support identification, nurturing and scaling up of innovations and prepare for shocks/stressor events through establishing accelerator programmes across counties.

2. Fast-track development of a policy framework for adoption of emerging technologies, including Artificial Intelligence, Blockchain, Fifth Generation technology (5G), Internet of Things (IoT), Fourth Industrial Revolution (4IR) and Industry 4.0 technologies that are critical in building economic resilience. Also, adopting best practices and domesticating standards will guide the application of the emerging technologies. Further, fast-track full development and implementation of National ST&I policy to guide the development of the ST&I sector in Kenya. The envisioned policy will be critical for development of the ST&I sector, including the coordination of the ST&I activities and programmes necessary for building economic resilience in the country.

Entrenching a Resilient Creative Economy

The creative economy is essentially a set of knowledge-based economic activities that have strong back and forward linkages with potentially high multiplier effect. Creative economy has tremendous contributions by promoting social cohesion, inclusion and well-being and cultural diversity. Majority in the creative economy are MSEs that use it as a source of livelihood. Given that most of the MSEs are informal, this heightens vulnerability of jobs created due to weak labour protection, low and/or inconsistent earnings. Informal sector players also face challenges associated with ensuring compliance to standards, and contributing to low quality. In addition, there are business risks experienced in the creative ecosystem, which include skills inadequacies; inappropriate infrastructure; limited access to appropriate finance; import constraints; particularly creative economy industries such as fashion, audio visual and new media which rely on imported inputs. Kenya is working to strengthen the policy framework, including the Kenya National Music Policy, Kenya National Culture Policy and the National Film Policy.

To promote resilience of the creative economy, there is need to:

1. Enhance creative skills and capacity, develop sustainable infrastructure, and promote innovative financial products for creative economy players. A sustainable creative industry infrastructure allows for the expression of creativity, enhances interactions and networks, strengthens innovation capacities, and facilitates digital creation, transmission and promotion of creative products. Capacity at the school level can be enhanced by mainstreaming creativity in school-based and county extra-curriculum activities, and inter-school festivals and awards and strengthening institutes of higher learning to provide relevant capacity building programmes to address the capacity gaps within Kenya's creative ecosystem. Inter-school festivals have taken place in Kenya since the 1950s when they were established by the British Council and later adopted as a government initiative referred to as The Kenya Schools and Colleges Drama and Film Festival and the Kenya National Music Festivals. The festivals are achieved through inter-school competition at local and regional levels, which culminates in a national event. Other than the Kenya National Music Policy (2015), which establishes in-school activities and festivals in music, these festivals have been undertaken in a policy vacuum. This calls for enhanced policy and resource support and further establishment of special programmes and schools for nurturing talent. Capacity can also be enhanced through the promotion of capacity building programmes that nurture creative industries, thus investing in specialized schools and relevant higher education programmes.

2. Identify, preserve and promote museums, cultural sites, cultural centres, theatres, and recreation facilities and institutionalize cultural festivals at the national and county levels as a priority. This calls for the identification and mapping of cultural and heritage assets and initiatives and hastening of relevant policy and regulatory reforms such as the National Addressing System Policy and the Heritage and Museums Bill, 2021. Additionally, is to develop a sector statistics plan, strengthen the intellectual property rights regime, develop an e-commerce policy and expand the local content policy framework to provide for the protection and promotion of creative goods.

Role of National Values in Enhancing Socio-Economic Resilience

The Government has since independence put in place strategies to promote values into the national psyche. These include: the Harambee movement; the working nation (Uhuru na Kazi); and later in the 1980s the Nyayo philosophy of peace, love and unity to rally Kenyans towards peaceful and harmonious coexistence. It was not until the promulgation of the Constitution in 2010 that the same was institutionalized, with establishment of elaborate national policy and legislative frameworks on national values, including the Sessional Paper No. 8 of 2013 on National Values and Principles of Governance, and the Sessional Paper No. 9 of 2013 on National Cohesion and Integration. Further, the Kenya Vision 2030 included National Values and Principles of Governance as a key foundation for economic prosperity. National values have also been mainstreamed in institutional frameworks such as the public sector performance contracting framework and the national education curricula. That said, inculcating national values has faced challenges, which include inadequate monitoring and evaluation, inadequate coordination across Ministries, Counties, Departments and Agencies (MCDAs), inadequate role modelling, weak transformational leadership, non-compliance with policy, legal and institutional provisions, and weak socio-economic status. That

said, there is great potential for the country to nurture national values through the following:

1. Enhancing the role of the annual Presidential Report on measures taken and progress achieved in the realization of national values and principles of governance as a key monitoring tool for promoting and inculcating national values. The Government has since 2014 published annual Presidential Reports where all MCDAs report on Measures Taken and Progress Achieved in the Realization of National Values and Principles of Governance. The same is presented by the President to Parliament in line with Article 132(1)(c) of the Constitution – and debated in Parliament. Its role can be enhanced by: incorporating use of specific indicators that track the progression of specific national values and principles of governance; setting up a clear feedback mechanism clearly outlining areas of improvement for each ministry, county, department and agency; and enhance continuous improvements through periodic institutional analysis of actors in national values and principles of governance using pre-determined frameworks.

2. Cultivating the role of transformational leadership in inculcating national values. This can be achieved through adhering strictly to the provisions of Chapter 6 of the Constitution of Kenya on Leadership and Integrity, which saw development of the Leadership and Integrity Act No. 19 of 2012. The Act specifies various implementers but identifies the Ethics and Anti-Corruption Commission as being responsible for overseeing and enforcing its implementation. The Act envisages that every person has the responsibility of implementing the provisions to the extent required. This suggests that individual responsibility and the use of education programmes becomes key in shaping positive values. With respect to education, actions that can be enhanced include: family values education; enhanced quota system of education that promotes co-mingling among diversities; and continued civic education.

3. Applying the sanction and reward systems more rigorously. MCDAs are expected to promote good governance and integrity by sanctioning members for under-performance and/or complaints within stipulated timelines. MCDAs are also expected to implement sanctions against persons and contractors who have not performed according to professionally regulated procedures or legislation in the procurement for public goods and services. In addition, the Leadership and Integrity Act No. 19 of 2012 empowers the Anti-Corruption Commission to make an application before a High Court judge for appropriate orders of compliance in case a state organ does not ensure compliance with and enforcing Chapter Six of the Constitution. The MCDAs can also enhance the existing reward systems and introduce new ones. An example is the Pupils Reward Scheme (PURES) programme, which is implemented by the Office of the First Lady (since 2015) by hosting students from the 47 counties to enhance national unity and a sense of values-based leadership.

Good Governance in Building Resilience

Kenya has largely complied with its international obligations by ratifying and domesticating the United Nations Convention Against Corruption, 2003 and thereafter enacting national laws that emulate prescribed international standards. It has for example enacted the Anti-Corruption and Economic Crimes Act, 2003, the Public Officer Ethics Act, 2003, the Leadership and Integrity Act, 2012 and the Proceeds of Crime and Anti-Money Laundering Act, 2009; and established such institutions as Ethics and Anti-Corruption Commission (EACC), Asset Recovery Agency (ARA), and Financial Reporting Centre (FRC). Further, the multi-agency taskforce (MAT) brought on board a partnership with anti-corruption institutions (EACC, Office of the Director of Public Prosecutions (ODPP), the Attorney General, ARA and FRC. This has served to improve speedy exchange of information and ease of tracing proceeds of corruption. This notwithstanding, reports by the Ethics and Anti-Corruption Commission (EACC), Asset Recovery Agency (ARA), World Bank, Transparency International, and Kenya National Bureau of Statistics consistently evidence excessive loss of public funds and misappropriation of public resources. To further enhance governance in building resilience for sustainable development, the following is critical.

Re-engineer to focus EACC resources to cases of serious fraud and economic crimes as opposed to cases that require administrative actions and can be reported to other public oversight and regulatory agencies that have a key mandate to handle such cases. This would require review and realignment of the EACC Act, 2011 and other legislations to further streamline the scope of EACC's functions, especially those outlined in Section 11 of the EACC Act, 2011. Also, given the successes and effectiveness of asset recovery mechanisms, it is important that EACC bolsters its asset recovery strategies related to corruption through collaboration with complementary anti-corruption and oversight institutions. Section 11(j) of the EACC Act, 2011 accords EACC the mandate to institute and conduct proceedings in court for purposes of the recovery or protection of public property, or for the freeze or confiscation of proceeds of corruption or related to corruption, or the payment of compensation, or other punitive and disciplinary measures. This is to be distinguished from the mandate of ARA (under Section 54 of the Proceeds of Crime and Anti-Money Laundering Act, 2009), which relates to recovery of proceeds of crime in general while EACC's asset recovery functions and powers are limited to proceeds of corruption.

There is need to review the functions of oversight or disciplinary institutions or commissions with a view to addressing potential duplication and managing incidents of overlapping jurisdiction. Also is the need to engage the private sector in supporting anti-corruption initiatives and promoting their entrenchment within their organizations. Sanctions such as those envisioned in the Bribery Act, 2016 should be reinforced. There is need to deepen the use of social accountability tools spearheaded and supported by citizens and local communities to provide a strong monitoring and reporting system for public officers, and promote use of corruption prevention mechanisms such as systems reviews which are carried out by EACC. EACC can build awareness on the benefits of institutionalizing corruption prevention.

About KIPPRA Policy Briefs

KIPPRA Policy Briefs are aimed at a wide dissemination of the Institute's policy research findings. The findings are expected to stimulate discussion and also build capacity in the public policy making process in Kenya.

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