THE DETERMINANTS OF FOREIGN DIRECT INVESTMENT IN THE MANUFACTURING SECTOR IN KENYA

BY

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2012
DECLARATION

I declare that this is my own original work and to the best of my knowledge it has not been submitted for a degree award in any other University or institution of higher learning.

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This research project has been submitted to the University of Nairobi with my approval as University Supervisor

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DEDICATION

This research proposal is dedicated to my dear parents Helen and Moses, my guardian Charity, sisters Purity, Ann and Damaris, Brothers, Elias, Elvis and Oki for their love and support during my studies. May God bless you mightily
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I am indebted to many individuals for their support and contributions towards the successful and timely completion of this research project.

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ABBREVIATION

AGOA-African Growth and Opportunity Act

EPZ -Export Processing Zones

ERS -Economic Recovery Strategy

FDI -Foreign Direct Investment

GDP -Gross Domestic Product

ICRG -International Country Research Guide

IMF -International Monetary Fund

KIPPRA- Kenya Institute for Public Policy Research & Analysis

M&A -Merger and Acquisition

MNE -Multi-National Enterprises

SAPs -Structural Adjustment Program

SSA -Sub-Saharan Africa

TNCs - Trans-National Corporations

UNCTAD- United Nations Centre for Trade and Development

US - United States
ABSTRACT

In this era of increasingly globalized world economy, FDI is a particularly significant driving force behind the interdependence of national economies. Even though most of the FDI flows have always concentrated in the developed countries, its importance is undeniable for developing countries as well. Through private direct investments, developing countries are participating more than ever before in the global production network.

It is widely acknowledged that FDI has potential benefits that can accrue to developing countries. This view is based on the theories that suggest that FDI is important for economic growth as it provides the much needed capital for investment, increases competition in host countries economies, and aids local firms to become more productive by adopting more efficient technology or by investing in human or physical capital. Theories and studies conducted on FDI determinants have different approaches and do not necessarily replace each other but explain different aspects of the same phenomenon.

This paper provides fresh evidence on the determinants of FDI inflows on the manufacturing sector in Kenya based on a survey of foreign firms in Kenya as at 2011. Results from this study show that Kenya needs to improve its macroeconomic environment i.e. economic growth and stability and strengthen its institutional base which affect political environment and regulatory policies. The government should put a lot of resources to curb crime and restore law and order, embrace positive democratic practices, maintain stability and embrace zero-tolerance on corruption in order to gain substantially in investment growth and FDI flows.
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CHAPTER ONE

INTRODUCTION

1.1 Background on the Study
Promoting foreign direct investment (FDI) has always been a primary concern for economic growth, especially in developing countries. In this era of increasingly globalized world economy, FDI is a particularly significant driving force behind the interdependence of national economies. Even though most of the FDI flows have always concentrated in the developed countries, its importance is undeniable for developing countries as well. Through private direct investments, developing countries are participating more than ever before in the global production network, (Sun, 2002).

Foreign direct investment (FDI) can potentially benefit domestic manufacturing firms. The benefits arise from foreign firms demonstrating new technologies, providing technological assistance to their local suppliers and customers, and training workers who may subsequently move to local firms in both service and manufacturing sector. Local firms can also learn by watching. Moreover, the very presence of foreign owned firms in an economy increases competition in the domestic market. The competitive pressure may spur local firms to operate more efficiently and introduce new technologies earlier than would otherwise have been the case, (Kokko, 1994)

The importance attached to foreign direct investment in the growth and development process has led a number of African countries to put in place various measures apart from improving their investment environment that they hope will attract foreign direct investment to their economies. Many countries have put in place different incentives to ensure that resources are directed to areas and sectors where they are badly needed to deal with the issues of employment generation and poverty elimination. Indeed, in some cases, there is the risk of “racing to the bottom” as countries compete for FDI.
1.1.2 Meaning and Rationale of FDI

According to the International Monetary Fund, foreign direct investment, commonly known as FDI refers to an investment made to acquire lasting or long-term interest in enterprises operating outside of the economy of the investor. The investment is direct because the investor, which could be a foreign person, company or group of entities, seeking to control, manage, or have significant influence over the foreign enterprise. A direct investor may be a firm, a multinational company, or a government. Where funds to set up a newly entity abroad are raised from the direct investors of the home country, an FDI is referred to as Greenfield investment. FDI may also be described as cross-border or international merger and acquisition (M&A) where there is a transfer of a local ownership of local productive activity and assets from a domestic to a foreign entity (United Nations, 1998). A country is poised to reap more immediate benefits in the case of a green field investment as it directly impacts on job creation and capital injection.

FDI is a major source of external finance which means that countries with limited amounts of capital can receive finance beyond national borders from wealthier countries. According to the World Bank, FDI and small business growth are the two critical elements in developing the private sector in lower-income economies and reducing poverty. It is now widely acknowledged that FDI has potential benefits that can accrue to developing countries. This view is mainly based on the neo liberal and development economists. They suggest that FDI is important for economic growth as it provides the much needed capital for investment, increases competition in host countries’ economies, and aids local firms to become more productive by adopting more efficient technology or by investing in human or physical capital. FDI is also said to contribute to growth in a substantive manner because it’s more stable than other forms of capital flows.

1.1.3 FDI and Manufacturing Sector in Kenya

Rweyemamu, (1987) notes that, foreign investment has been of considerable significance in financing development in Kenya not only in the manufacturing but also in the primary and tertiary sectors. Before independence in 1963, bulk of it went to primary production and plantations. The few manufacturing industries established up to World War II were mainly for basic processing of agricultural exports and the processing of food for the local market until after the war when British manufacturing firms begun to invest directly in the manufacturing. This
was so because of the competition from non-British trading firms, which threatened Britain's share in the Kenyan market.

After land resettlement between 1962 and 1964, the Kenyan government prevented foreign firms from purchasing more land and as a result foreign ownership in agriculture was greatly reduced. In commerce and industry by contrast, virtually all the expansion which took place, that is a 50 per cent increase in output between 1964 and 1970 and 100 per cent increase in the annual level of investment, was foreign owned. At first much of it involved capital transfer out of agriculture, especially following the introduction of exchange controls in 1965. But two years later after the initial period of uncertainty as to the government development strategy, a substantial inflow of foreign direct investment and its diversification to other sectors occurred, (Gachino 2006). In addition the government set up institutions which would assist in the development of the manufacturing sector. During this period Kenya had pursued import substitution from as early as 1950s. This industrial policy advocated for a large role of the public sector participation and protection of the infant manufacturing industries. The government used a combination of tariffs and quotas supplemented by foreign allocation measures including overvaluing exchange rates to maintain import costs low, favourable credit and interest rate policies intended to subsidize the manufacturing consumer goods (Rweyemanu, 1987).

FDI levels in Kenya at this period were reasonably high in comparison to other East African countries. This was partly attributed to the fact that Kenya had maintained a favourable investment climate. Obrien and Ryan (2002) note that Kenya was for many years a relatively attractive locale for foreign investment. However, Bradshaw (1988) observes that although that was case, there were already concerns by both scholars and government planners that, because of Kenya's liberal repatriation policies, more international investment income left Kenya in the form of profit remittances than flows into the country. As a result the government instituted measures to encourage reinvestment of their profits in the country. From 1974, firms with high repatriation rate had their local borrowing rights restricted by the Central Bank. The government also attempted to cut down on the level of management remittances and technical fees by imposing a 14 per cent withholding tax. These efforts discouraged foreign investors.
Since then, FDI in Kenya has not only been volatile but also low. This led to the stagnation of the manufacturing sector which was largely been dominated by the foreign firms. This decline was blamed on the inward oriented strategy as well as the collapse of the East Africa Community in 1977. Ensuing economic distortions resulted in severe structural constraints and macro-economic imbalances and firms failed to develop competitive capabilities to penetrate the international markets. The inward looking policies pursued at the time under import substitution made it difficult to effectively participate and compete keenly in the export markets. As a result the manufacturing industry failed to play a more dynamic role enough to function as an engine of county's growth and did not contributed significantly to foreign exchange (Kenya Government 1994).

Further, the economic stagnation in the mid-1980s and 1990s affected Kenya’s industrialization with consequent effects on labour productivity. Political instability in neighbouring countries particularly Uganda also drew away markets and investment in Kenya. Macro-economic constraints arising from a collapse in the IMF’s Structural Adjustment Program (SAPs) in 1986, massive destruction of infrastructure due to El Nino rains and weak institutions had all contributed to economic stagnation. Hence, although Kenya introduced a number of instruments to promote FDI and export oriented industrialization during this period, these efforts did not yield much, (Kinuthia 2010).

After the 1990s when economic stagnation was seen, Kenya resumed the path to rapid economic growth in 2002 through the implementation of the Economic Recovery Strategy paper which was replaced by vision 2030 after it expired in 2007. During this period the government embarked on establishment of free trade zones, improvement of business climate, infrastructure, and development of incentives among initiatives. These efforts are aimed at building a momentum that can sustain economic growth and promote development. At the centre of these efforts is a commitment to attract foreign direct investment which was hoped would assist in the industrialization process, (Kinuthia 2010).
1.2 Statement of the problem

FDI is considered less prone to crisis because direct investors, typically, have a longer-term perspective when engaging in a host country. In addition to the risk-sharing properties of FDI, it is widely believed that FDI provides a stronger stimulus to economic growth in host countries than other types of capital inflows. Yet, economists know surprisingly little about the driving forces and the economic effects of FDI, (KIPPRA/World Bank, 2004). The relevance of earlier findings on the determinants of FDI is debatable. The relative importance of traditional determinants may have declined in the process of economic globalization and the economic effects of FDI do not allow for easy generalizations.

The recent high demand of FDIs has brought interest to various disciplines to empirically investigate the fundamental factors that drive the FDI behavior for example, Kinaro (2006) using time series analysis to determine FDI competitiveness finds out that FDI in Kenya is determined by economic openness, human capital, real exchange rate, inflation, and FDI in the previous periods. Opolot et al (2008) find using panel data for Sub Saharan African Countries, Kenya included that market potential, openness to trade, infrastructure, urbanization, and rate of return on investment positively affect foreign direct investment inflows to Sub-Saharan Africa, while macroeconomic instability is a disincentive to foreign direct investment. Other variables such as government consumption, financial development, natural resources, wage and political rights are found to be insignificant. Mtega and Rose (2007) using panel data of 43 countries with a Kenyan dummy find that Kenya is not different from other countries and that FDI is determined by growth rates, terms of trade shocks, external debt ratio and quality of institutions. Ngugi & Nyangoro (2005), in their study on FDI and institutional factors find out that infrastructure, cost of doing business and return on capital is a major determinant for FDI inflows in Kenya.

The studies conducted on FDI determinants have different approaches and do not necessarily replace each other but explain different aspects of the same phenomenon. The question is do these determinants have the same influence on the manufacturing sector in Kenya? Given the growing importance of FDI in manufacturing industry, but weak performance, it is therefore valuable to explore the determinants of FDI inflows into Kenyan manufacturing industries. Furthermore, the relative importance of FDI determinants may change over time, e.g. due to
ongoing globalization, (Mwega & Rose 2007). This study therefore intends to find out the determinants of FDI inflows in the Kenyan manufacturing industry. Thereby answering the question what are determinants of foreign direct investment in the manufacturing sector in Kenya?

1.3 Objective of the study
To establish the determinants of foreign direct investment in the manufacturing sector in Kenya

1.4 Significance of the study
This study will be useful to Policy makers in Kenya. A number of factors come into play to determine the growth and development determinants of FDI in a country. Often policymakers rush into FDI liberalization policies without considering the pros and cons of the policies and without any definite strategies. It can be extremely useful for emerging economies if the determinants influencing FDI’s are well known and used strategically. This is because FDI, however, does not depend solely on domestic determinants. There may be external factors influencing FDI flows, which are beyond the control of an individual developing country.

The findings will raise international awareness on many of foreign investors who have entered developing countries seeking high returns and portfolio diversification. Investors are most satisfied with investment experiences when they are free to realize returns from their investments without government interference. When investors consider investing in a country, they give much weight to the independence of regulatory processes from government interference. Foreign investors are more interested in ensuring the long-term viability of investments than in maximizing short-term returns. In many cases they are willing to stay the course and do what is needed to turn around the financial and technical performance of the assets in which they have invested—as long as governments ensure that the conditions they consider priorities are in place. In planning for FDI, foreign investors need to understand what will maximize or limit their returns and help achieve their goals in a given country, hence the need for this study

The study will also be significant to scholars and researchers as it will provide contribution to existing body of knowledge on the determinants of foreign direct investment in the manufacturing sector in Kenya and provide a foundation for further research
CHAPTER TWO

LITERATURE REVIEW

2.0 Introduction
This chapter reviews the information from other researchers who have carried out their research in the same field of the study. Specific emphasis has been put on the major determinants of foreign direct investment in a country. The specific areas covered here are the theoretical orientation and the determinants of FDI in manufacturing sector empirical review

2.1 Theoretical Review
There is a variety of theoretical models explaining FDI and a wide range of factors that can be experimented within empirical studies in order to find the determinants of FDI. They include Neoclassical trade theory, Portfolio Theory (PT) Models, ownership advantages theory and internalization theory framework (Oli Framework).

2.1.1 Neoclassical Trade Theory
Turning to the early theoretical models, the first theoretical attempt to explain FDI was based on the Heckscher–Ohlin model of the neoclassical trade theory where FDI was seen as part of international capital trade. The economic intuition behind the Heckscher–Ohlin model was based on the further assumption that commodities differ in relative factor intensities and countries differ in relative factor endowments, leading to international factor price differentials. Hence, a relatively capital-abundant country would either export the capital-intensive good to foreign or – in the absence of commodity trade – move capital to foreign where returns on capital are higher and returns on labor lower until factor price equalization is achieved, MacDougall (1960). However, countries could manipulate capital returns and capital flows by imposing taxes on internationally mobile capital to enhance their welfare. Aliber (1970) expanded the view that capital moves due to a difference in capital returns, but claimed that this difference was due to a difference in capital endowments and currency risks, as interest rates include a premium that is charged according to the expected currency depreciation.
Firms from countries with ‘harder’ currencies, i.e. currencies with less fluctuation in value, could borrow money in countries with ‘softer’ currencies at a lower interest rate than host country firms due to their lower risk structure. Foreign firms could therefore capitalize the same stream
of expected earnings at a higher rate than host country firms, giving them a reason to invest in the host country. Allowing for the possibility of the world being a unified currency area (without currency risk), it was argued that FDI could still take place, though it was then explained in terms of the financial side of location, for instance as investment between different societies areas.

2.2.2 Portfolio Theory (PT)
Under the Portfolio Theory (PT), investors consider the returns and risk in selecting their portfolio. The risks in international portfolio investment are mainly from unfavorable changes in exchange and interest rates, and regulatory environments. Apart from the inherent risks, institutional constraints might also limit the potential for international portfolio investments, for example constraints due to taxation, exchange controls, capital market regulations and transaction costs, Dunning (1996). In this case, element of uncertainty is taken into account. It is based on the observation that fluctuations in rates of return on capital within and between countries are not perfectly correlated, such that risks might be reduced by a diversification of portfolios. In such a case, having a mix of both domestic and foreign portfolios can lead to a reduction in risk

2.2.3 Ownership Advantages Theory
Hymer (1976) and Kindleberger (1969) were among the first to criticize the neoclassical approach for its limited ability to explain FDI flows. They argued that the assumption of perfect competition in neoclassical theory could not explain FDI, which – in their view – needed structural market imperfections to flourish. FDI was assumed to be linked to the theory of MNEs, which are, by definition, large companies with control or market power. Both authors focused on the concept of ‘monopolistic advantage’ to explain why firms enter foreign markets. They argued that foreign firms needed ownership advantages such as product differentiation (imperfect good markets), managerial expertise, new technology or patents (imperfect factor markets), the existence of internal or external economies of scale or government interference to balance out the disadvantages of entering a foreign market (including higher risk, less information, more uncertainty, physical distance and differences in culture, business ethics, the legal system and other regulations) in order to compete with local firms. Caves (1974) focused on product differentiation as a monopolistic advantage, claiming
that imperfect competition encouraged MNEs to differentiate products and engage in horizontal FDI. FDI was preferred over exporting or licensing if knowledge was employed in product differentiation rather than in managerial skills.

2.2.4 Internalization theory Framework (Oli Framework)

Dunning (1996) brought together internalization theory and traditional financial economics to create the extensive paradigm of FDI, synthesizing the reasons for firms to operate internationally (advantages) and the mode of entry (FDI, export and licensing).

In the MNE theory, FDI was explained by identifying three types of special advantages that MNEs have: ownership, location and internalization advantages. Ownership advantages referred to the MNE’s production process, ensuring a competitive advantage over domestic firms, and include patents, technical knowledge, management skills and reputation. Location advantages were motives for producing abroad including the access to protected markets, favorable tax treatments, lower production and transport costs, lower risk and favorable structure of competition. Internalization occurred due to the public good nature of ownership advantages and – compared with licensing or exporting – had the advantage of lowering transaction costs, minimizing technology imitation and maintaining the firm’s reputation through effective management and quality control. Based on these assumptions, the degree of foreign ownership in an industry should be higher, the more research-, technology- or marketing-intensive products are. The OLI framework can further be related to country-, industry- and firm-specific structural variables.

With the above theories, FDI is grouped into three different types: natural resource-securing type, market-securing type, and cost-saving type. The market-securing type or market-seeking type of FDI is driven by the size and growth of the host market. This is also referred to as horizontal FDI as it involves building duplicate plants in a foreign location to supply the market there. The idea is to reduce the cost involved in supplying the market, such as the tariffs and transport costs, or to become more competitive in other ways, such as through proximity to the market and being able to respond to the changing local circumstances and preferences. The cost-saving type or production cost minimizing FDI is also referred to as vertical FDI as it involves slicing the vertical chain of production and relocating part of the chain in a low cost location. This type of FDI also encompasses the raw material seeking FDI, as the inexpensive input could
be primary commodities or raw materials in a specific location. Other inexpensive input that may attract such FDI is the cost of labor, intermediate goods and even access to certain externalities.

2.2. Trend of the FDI in the Manufacturing Sector in Kenya

In the 1970’s, Kenya was a prime choice for foreign investors seeking to establish presence in Eastern and Southern Africa that led to a steady growth of Foreign Direct Investment (FDI). The country had a relatively high level of development, good infrastructure, market size, growth and FDI openness compared to other countries in the region that had relatively closed regimes. The level of FDI in the 1970’s was about $10 million a year peaking to approximately $80 million in 1979-1980. However, the early 1980’s saw a decline in FDI as a result of numerous factors such as the deterioration in economic performance, stop-go nature of economic reforms, political instability, rising costs of services and doing business, mediocre growth performance, corruption, poor governance, deterioration of public services and infrastructure.

It was estimated that Kenya’s FDI inflows in 1996-2003 averaged $39 million a year, which is very little compared to inflows to Tanzania and Uganda that surged to $280 million and $220 million, respectively, from negligible levels in the 1980s. Around this time, the average inflow to African countries was six fold. Although developing countries as a whole attracted an annual average of $41 of FDI per capita in 1996-2003, Kenya only drew average inflows of $1.3 per capita. In fact, UNCTAD's FDI performance index ranked Kenya 125th (out of 140 countries) in 2003, (UNCTAD (2005).

Foreign firms in Kenya since the 1970s have invested in a wide range of sectors. Most notably they played a major role in floriculture and horticulture, with close to 90 per cent of flowers being controlled by foreign affiliates. In the Manufacturing sector FDI has concentrated on the consumer goods sector, such as food and beverage industries. This has changed in the recent years with the growth of the garment sector because of African Growth and Opportunities Act (AGOA). Of the 34 companies involved in AGOA 28 are foreign most of them concentrated in the Export Processing Zones (EPZs), 55 per cent of the foreign firms are concentrated in Nairobi while Mombasa accounts for about 23 per cent, thus Nairobi and Mombasa account for over 78 per cent of FDI in Kenya. The main form of FDI establishment has been through the form of green fields establishments and Kenya has in total more than 200 multinational corporations. The
main traditional sources of foreign investments are Britain, US and Germany, South Africa, Netherlands, Switzerland and of late China and India (UNCTAD, 2005).

Recent trends in Kenyan sectoral composition of FDI are in horticulture, floriculture, garments, and tourism. While interest in horticulture and floriculture has been in response to favorable local conditions linked to climate and transport infrastructure, Garment investment has been in response to the U.S. granting preferential access to its market under AGOA. Manufacturing FDI has concentrated on consumer goods sectors, such as the food and beverage industry. Most foreign investment in manufacturing since 2001 has been in the (EPZs), with the majority in AGOA-related textiles. There were 55 foreign or joint-venture enterprises operating in EPZs in 2003. EPZs have expanded from their initial textiles focus to also produce a number of other goods. The largest single investment is the De La Rue currency printing operation with a value of $48 million, (UNCTAD (2005).

2.3 Determinants of Foreign Direct Investment

2.3.1 Economic stability and growth rate
According to Lipsey, (2000) and Salvatore, (2001), FDI flows to where fast economic growth has been recorded. A virtuous circle is observed here that FDI contributes significantly to economic growth, faster economic growth attracts more FDI because it increases foreign investors’ confidence in the economy, which in turn pushes the growth rate even higher. In the least developed countries, studies have shown that FDI in fact follows, not proceeds, some initial growth or at least the promise of growth. A country’s overall macroeconomic performance, such as low inflation rate and balanced fiscal account, is a consistently significant factor in shaping the decision making of foreign investors when assessing investment locations. Because macroeconomic instability makes it difficult for investors to evaluate the true costs and returns of their investments, only in rare cases would FDI flows to places where there is hyperinflation or severe imbalances in their internal and external positions.

FDI flows in an economy driven by economic growth can be seen in two ways; market seeking FDI, made by multinational firm with two or more branches in different countries, is induced by market accesses to host countries for efficient utilization of resources and exploitation of
economies of scale (Markusen et al., 1996). Export oriented FDI is motivated by factor-price differentials (e.g. cheap labor in host countries) along with human capital and infrastructure conditions (Zhang and Markusen, 1999). Rapid economic growth leads to aggregate demand for demand for investments including FDI. Moreover, better economic performances in host countries provide a better infrastructural facilities and greater opportunities for making profits, and so greater incentive for FDI. With regards to FDI, infrastructure encompasses both physical (e.g. roads and power) and social (e.g. health and education) concepts. It has been repeatedly shown around the world that a well-developed infrastructure network and a well-trained labor force are major elements of attractiveness to foreign investors. This is especially true where high quality FDI (e.g. long-term transfer of advanced technology) is concerned.

2.3.2 Political stability
Quite understandably, incidences of political coups, assassinations, riots, or armed conflicts may exert a dominant negative influence on foreign companies’ investment decisions. Indeed, frequent changes of governments and the resultant policy changes can reduce an investor’s assets to zero overnight. In the absence of significant reserves of non-renewable natural resources (e.g. oil), rarely would any foreign investors accept serious political risks or frequent policy reversals.

2.3.3 Market demand/ Size
The flows of FDI are positively influenced by the size of a country’s market demand as measured by GDP per capita. This confirms the casual observation that most FDI flows to affluent countries and it is particularly true with market-seeking type of FDI. Even in developing countries, where FDI inflows tend to be more resource-seeking, a country’s overall development level still has a strong bearing on how much FDI it attracts. Scarparlanda and Mauer (1969) studying the determinants of US direct investments in the European Economic Community (EAC), found that size of EEC as the only significant variable after many simulations.

2.3.4 Regulatory environment
It is increasingly recognized that the administrative and regulatory environment of a country can have a significant influence on the level of FDI flows. While large and powerful investors may be able to endure cumbersome and costly procedures, they may prove fatal to the entry and growth of small and medium enterprises. Business environment of a host country such as legal restrictions related to business activities including various taxes, regulation on trade, investment
and incentive policy to attract inward FDI might be considered as a potential FDI determinant. Since regulations of various kinds restrict free business activities, they’ve negative effects on FDI inflows. Moreover, arbitrary, discriminatory, and non-transparent regulations often lead to corruption, which has been shown to be a fatal deterrent to FDI. Red tape and particularly corruption present the biggest disincentive to investment in Kenya. The government has moved to reverse this trend. In 2003, the government passed the anti-corruption and Economic Crimes Act, settling the rules for accountability and transparency, and defining graft and abuse of office among other measures.

2.3.5 Investment promotion
Once a country has established a reasonably appealing investment climate, how much FDI it gets depends also on its marketing efforts to attract foreign investment. Granted, no amount of promotion can substitute for a truly investment-friendly environment, but when other factors are similar – as it true in economies having attained a certain level of development – promotion efforts do make a difference. In this context, mention should be made to the fiscal incentive schemes that host governments often feel obliged to offer in order to attract FDI. There have indeed been examples of such “tax heavens” which are highly successful with mobile multinational companies. Most economic studies and surveys of international investors, however, have repeatedly shown that these incentives are not nearly as influential in the location decisions of foreign investors as it is usually believed. That is, even though all investors would seek the lowest tax liabilities when it is possible – just like they would prefer low factor costs when all other conditions are equal.

2.3.6 Infrastructure
More FDI is likely to occur in countries with good physical infrastructure such as bridges, ports, highways, etc. It also seems likely that there are some diminishing returns in infrastructure, at least in infrastructure of a specified type. Therefore, especially for countries with poor infrastructure, investing in improvements in infrastructure may be important for attracting FDI. Nonetheless, some countries with poor infrastructure may be unattractive hosts for FDI for a variety of other reasons, and even substantial investments in infrastructure might not bring FDI pouring in. But all else equal, a country with more infrastructure would be expected to attract more FDI (as well as more domestic investment).
In developing countries, an essential requirement for economic growth and sustainable development is the provision of efficient, reliable and affordable infrastructure services, such as water and sanitation, power, transport and telecommunications. The availability of efficient infrastructure services is an important determinant of the pace of market development and output growth, and, in addition, access to affordable infrastructure services for consumption purposes serves to improve household welfare, particularly among the poor. In most countries, however, the potential contribution of infrastructure to economic growth and poverty reduction has not been fully realized, and existing infrastructure stock and services fall far short of the requirements.

2.3.7 Cost of doing business
Among the factors taken into consideration by firms before they put their investment in place is the cost of doing business in a country. This has implication on the production costs either through increased costs of operation or through higher costs of inputs. To enforce a contract in Kenya is more costly and takes longer than enforcing the same contract in other countries. Such a long duration opens up chances for corruption and, therefore, more costs to investors. The high costs (as a percentage of GNI per capita) imply that firms have to spend more to get their contracts enforced, which is a disincentive for their investments. Accessing financial capital (especially credit) is less difficult in Kenya as compared to Uganda and Tanzania where there are no private credit bureau coverage. However, the proportion of private credit available in Kenya is much less, about 26% of GDP, as compared to South Africa, about 72%. The intermediation cost is relatively higher in Kenya (with an interest rate spread of about 13%, which is second to that of Tanzania of about 15%), as compared to South Africa with a spread of about 5%, Mwega F.M and R.W. Ngugi (2007). The major problem with investments in Kenya is that once the firms are established, it takes even longer (about five years) for firms that want to relocate to other regions to close their business as compared to an average of about two years for the other economies. However, the actual cost as a proportion of the entire estate is higher in Uganda than in other economies. The longer duration taken to close a business may make foreign firms to avoid such economies in the wake of risk, though most FDI are not reversible.
2.4 Review of Empirical Studies

Over time a number of studies have been carried out to examine/analyze the various determinants of FDI. Feenstra and Hanson (1997) consider a total of 49 manufacturing companies for the period 1994-2002 in the US point out that low labor costs have large impact on US-owned assembly plants and US electronic assembly manufacturers. In their study using the Human Development Index (HDI) to capture the aspects of human capital development in Japan, Biswas (2002) find marginal negative effects of wages on investment, suggesting that low wages are not necessarily a crucial factor for investment. However, Mody et al. (1998) find labor costs not to be an attractor of Japanese FDI, although labor quality is. Similarly, Fung et al. (2000) reflect average wage costs to be insignificant but the labor quality significant for US and Japanese FDI in China. Globerman and Shapiro (2002) note that the absence of educated and healthy workers can be a deterrent to foreign entry, and that as increasing amounts of FDI becomes skill and efficiency-seeking, access to an educated and skilled workforce becomes essential.

Gustanaga et al (1998) consider a total of 49 countries, only 6 of which are in sub-Saharan Africa (SSA); while Schneider and Fry (1985) consider 51 countries of which 13 are in SSA. In Edwards (1990), about half of the 51 countries are in SSA. In their econometric analysis of the determinants of FDI using panel data, Edwards,(1990) argue that while market size is relatively unimportant in explaining FDI flows to Africa, economic growth is an important determinant. They however find that a depreciation of the real effective exchange rate, an increase in a country’s openness to trade, and the expansionary effects of fiscal balance have positive impacts on FDI. It is also shown that an improvement in removing restrictions and providing good conditions for private initiative have important bearing on FDI inflows, while the number of political upheavals has a negative bearing. Terms of trade shocks and the level of schooling are found to have little impact on FDI into Africa. Incidents of war and African regional integration arrangements are found to have limited impacts on FDI flows.

Busse (2003) using cross-sectional and panel data analysis to look at democracy as a determinant of FDI in a country found that on average, investments by multinationals are significantly higher in democratic countries. Democracy is proxied by political rights and civil liberties indicators.
Political rights enable people to participate freely in the political process, while civil liberties include the freedom to develop views, institutions, and personal autonomy without reference to the state. Rodrik (1996) regresses an indicator for democracy (and a number of control variables) on the value of investment by majority-owned US affiliates abroad, while Harms and Ursprung (2002) focuses on developing emerging market economies. Both studies have found out that MNEs are more likely to be attracted by countries in which democracy is respected, concluding that there is little evidence that weak democracies provide a haven for foreign investors.

Smarzynska and Wei (2000) analyze the implications of host country corruption on foreign investor’s choice of entry mode, arguing that in an environment where corruption exists, there is a trade-off in using local partners. This is because corruption makes local bureaucracy less transparent and increases the value of using a local partner to cut through the bureaucratic maze. On the other hand, corruption decreases the effective protection of investor’s intangible assets and lowers the probability that disputes between foreign and domestic partners will be adjudicated fairly, therefore reducing the value of having a local partner. They argue that corruption makes dealing with government officials less transparent and more costly, particularly for foreign investors. Globerman and Shapiro (2002) also point to governance as a major factor influencing the flow of FDI. Basing their argument on the “Eclectic” theory of FDI, they suggest that one factor contributing to a location’s attractiveness for FDI is its national political infrastructure (where national political infrastructure consists of the political, institutional and legal environment). The study shows that national political infrastructure is an important determinant of FDI inflows and outflows. The results suggest that investment in governance infrastructure attracts capital and creates conditions under which domestic MNEs emerge and invest abroad.

Blomstrom and Kokko (2003) indicate that among the factors that potential investors look up for include the rule of law, strong and clearly defined property rights, degree of corruption, regulation and local bureaucracy and political stability. Similarly, Balasubramanyam (2001) indicates that the efficiency of legal institution is important not only in ensuring that there is proper enforcement of contracts, but also in maintenance of law and order to ensure security of people and property. A well-functioning legal system also provides protection of intellectual
property rights, which gives a competitive edge to most foreign direct investors, forming a capacity of providing credible commitment on the part of the state. In a situation where there are high risks of insecurity, a firm may operate in incremental steps by starting with a smaller investment and hold out the prospect of additional investments in the future if the government agrees to maintain a certain level of security. Further, Biswas (2002) uses the law and order and the expropriation indices as proxies for the security of property and contract rights and finds a positive and significant relationship at 1% level. This suggests that institutions that protect property rights are important to investment.

Asiedu (2002, 2004). Using a cross-section data on 71 developing countries, attempts to find out on what factors drive FDI to developing countries, if these factors are equally relevant for FDI to SSA, if SSA attracted FDI and if so why has SSA been relatively unsuccessful in attracting FDI despite policy reform. The analysis is focused on only three main variables – the return on investment, infrastructure availability and openness to trade and does not take into account natural resource availability, which is an important determinant of FDI to Africa. The result indicates that Countries in SSA have on average received less FDI than countries in other regions by virtue of their geographical location. From various studies however we find that policy matters very much in attracting FDI to Africa. The roles of policy in affecting the levels and composition of FDI have been reviewed extensively by Balasubramayam and Salisu (2001) and further evidence can be found in Pigato (2000), Morrisset (2000) and Asiedu (2002).

Employing panel data on 22 African countries for the period 1984-2000, Asiedu (2003), empirically examines the impact of several variables including natural resource endowment, macroeconomic instability, FDI regulatory framework, corruption, effectiveness of the legal system and political instability on FDI flows. The paper debunks the notion that FDI in Africa is solely driven by natural resource availability and concludes that natural resource endowment, large markets, good infrastructure and an efficient legal framework promotes FDI while macroeconomic instability, corruption, political instability and investment restrictions deter investment flows. The result implies that government in the region can play major roles in promoting FDI to the region through appropriate policy framework, and that FDI to Africa is not solely driven by natural resources endowment but also by other factors. In the short and medium
term, government can increase their FDI by streamlining their investment regulatory framework, implementing policies, which promote macroeconomic stability and improve infrastructure. In the long run, more FDI can be achieved by curbing corruption, developing a more efficient legal framework and reducing political instability.

Morisset (2000) focuses exclusively on Africa and controls for resource natural resource availability. He identified which African countries have been able to attract FDI by improving their business climate. Evidence from the countries show that pro-active policies and re-oriented governments can generate FDI interest. Morisset makes the point that African countries can also be successful in attracting FDI that is not based on natural resources or aimed at the local market but rather on regional and global markets by implementing policy reforms. Using panel data for 29 countries over the period 1990-97, he finds that GDP growth rate and trade openness have been positively and significantly correlated with the investment climate in Africa. On the other hand, the illiteracy rate, the number of telephone lines and the share of the urban population (measure of agglomeration) are major determinants in the business climate for FDI in the region. Also the political and financial risk as measured by (International Country Risk guide (ICRG) and the International Investors (II) ratings did not appear significant in the regression. One of the major deterrents to FDI flows in the literature is uncertainty. Uncertainty is also a known factor plaguing Africa’s development strategy. Empirical relationship between FDI and uncertainty in developing countries are very few.

There are the studies by Lehmann (1999) for developing countries. These studies conclude that a negative relationship exists between uncertainty and FDI in developing countries. Only a few studies address the connection between uncertainty and FDI in Africa. While studies by Abekah (1998), Nnadozie (2000), Bennell (1995) and Pigato (2000) highlighted the roles played by uncertainty, none of them formally address the impact of both economic and political uncertainty in African countries. The study by Lemi et al (2001) examines how uncertainty affects FDI flows to African economies. Analyzed in the study are total U.S. FDI flows, U.S. manufacturing FDI and U.S. non-manufacturing FDI flow to sampled host countries in Africa. Using a generalized autoregressive heteroscedastic model, the study concludes that the impact of uncertainty on the flow of FDI from all sources is insignificant, for aggregate U.S. FDI, economic and political
uncertainties are not major concerns, for U.S manufacturing FDI, only political instability and government policy commitment are important factors, whereas for U.S. non-manufacturing FDI, economic uncertainties are the major impediments only when coupled with political instability and debt burden of host countries and other economic factors such as labor, trade connection, size of export sector, external debt, and market size are also significant in affecting FDI flow to Africa.

In Kenya few studies have been conducted on FDI determinants Kinuthia (2010) finds that FDI in Kenya is determined by economic openness, human capital, real exchange rate, inflation, and FDI in the previous periods. Opolot et al (2008) find using panel data for Sub Saharan African Countries, Kenya included that market potential, openness to trade, infrastructure, urbanization, and rate of return on investment positively affect foreign direct investment inflows to Sub-Saharan Africa, while macroeconomic instability is a disincentive to foreign direct investment. Other variables such as government consumption, financial development, natural resources, wage and political rights are found to be insignificant. Mwega & Rose (2007) using panel data of 43 countries with a Kenyan dummy find that Kenya is not different from other countries and that FDI is determined by growth rates, terms of trade shocks, external debt ratio and quality of institutions.

UNCTAD (2005) argue that Kenya's inability to attract FDI is due to growing problems of corruption and governance, inconsistencies in economic policies and structural reforms, deteriorating public service and poor infrastructure. Todd et al (2005) argues that Kenya officially encourages and grants national treatment to foreigners but that the problem is Kenya's political elites who resent FDI perceiving it to lead to dependency. Himbara (1994) shares similar sentiments. Kareithi (1991) concerned with the impact of foreign-owned media upon the body politic of Kenya argues that foreign ownership undermines both national sovereignty and even the rudiments of political freedom.
2.5. Summary

The literature review has given an overview of theoretical models attempting to explain the determinants of FDI inflows in a country. These theories include; Neo-classical trade theory, Portfolio theory, Ownership advantages theory, and Internalization theory framework. There is no one single theory of FDI but a variety of theoretical models attempting to explain FDI location determinants. The different approaches therefore do not necessarily replace each other but explain different aspects of the same phenomenon. From each of the theories mentioned, there is no unanimously accepted single factor determining the flow of investment in a country.

It is also clear that the determinants of FDI that have been successful in other regions may not be equally successful in Kenya. The determinants considered in this study include; economic growth and stability, Political stability, Regulatory environment, Cost of doing business, Infrastructure and Market size. The findings of various studies on the determinants of FDI in Africa have been contradictory in many cases. Furthermore there seems to be a dearth of empirical work that is solely concentrated on African countries and especially in Kenya on the determinants of FDI inflows in the manufacturing sector.

It shows therefore that the literature is replete with information on the full range of factors that are likely to induce the flow of foreign direct investment in general anywhere, but not specifically on the manufacturing sector in Kenya. The study therefore tries to fill the research gap that exists by carrying out a survey on the determinants of the FDI inflows in the manufacturing sector in Kenya.
CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter will represent the research design and methodology that was used to carry out research. The chapter also presents the research design, the population, sample size and sampling procedure, data collection and data analysis.

3.2 Research design

According to Creswell (1994), research design provides answers for all questions such as; what techniques will be used to gather data, what kind of sampling strategies, tools used and how will time and constraints be dealt with. The study will adopt descriptive research design. A descriptive research design determines and reports the way things are (Mugenda and Mugenda, 2003). Creswell (2003) observes that a descriptive research design is used when data are collected to describe persons, organizations, settings or phenomena.

For the purpose of this study, survey research design was adopted. This was applicable in this case because the population of FDI manufacturing firms is big and so representative sample was meaningful (Mugenda and Mugenda, 2003). The collection of qualitative and quantitative data enabled the study establish the determinants of FDI in the Manufacturing sector in Kenya.

3.3 Population

Target population is that population to which a researcher wants to generalize the results of a study. The target population in a research study comprises all those potential participants that could make up a study group (Mugenda and Mugenda). In this study the survey was conducted from all manufacturing companies in Kenya as at 2011 a total number of 812 firms’ obtained for the year 2001 to year 2010, data that has been compiled from several lists obtained from the Kenya Investment Authority (KIA), KIPPRA, Kenya Private Sector Alliance (KEPSA) and Kenya Industrial Research and Development Institute (KIRDI).
3.4 Sample and Sampling Procedure

Sampling means selecting a given number of subjects from a defined population. The selected items together are assumed to be a representative of that population, (Mugenda& Mugenda). The number of FDI manufacturing firms in Kenya is large and therefore a sample of 30 foreign firms was drawn, (appendix 2) this because they were considered the ones to give sufficient information on the determinants of foreign direct investment in the manufacturing sector in Kenya. Therefore data was gathered from the list of the identified institutes based on the manufacturing sectors and availability of address e.g. exact location, telephone number, and country of origin. Simple random sampling was applicable in this study since it gives an element in the population an equal chance of being selected.

3.5 Data Collection Procedures and instruments

The study used primary to collect both quantitative and qualitative information. Primary data was collected using semi-structured questionnaires, which contain A 5 point Likert scale questions. Close-ended or structured questions will give a respondent limited and pre-determined response to choose from. The advantage of structured questions is that they were easy to analyze and they leave no room for further responses. The questionnaires were dropped through a drop and pick method to the investment/Finance managers of the sampled firms.

3.6 Validity and reliability

Piloting was carried out to test the validity and reliability of the instruments. Validity indicates the degree to which the instrument measures the constructs under investigation (Mugenda and Mugenda, 2003). There are three types of validity test which include content, criterion, and related construct validity. This study will use content validity because it will measure the degree to which the sample of the items represents the content that the test was designed to measure.

A pilot study was conducted by the researcher taking some questionnaires to the respondents which was filled by some respondents at random. From this pilot study the researcher was able to detect questions that need editing and those that are ambiguous. The final questionnaire will then be printed and used to collect data to be used for analysis.
3.7 Data Analysis and Reporting

After having gathered data, it was edited, classified, coded and tabulated to analyze both and qualitative and quantitative data using Statistical Package for Social Science (SPSS Version 17). Tables and charts were used for further representation for easy understanding and analyzes.

\[ Y = \alpha + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + \beta_6 X_6 + \beta_7 X_7 + e \]

Where:

- \( Y \) = FDI inflows in Manufacturing Sector
- \( \alpha \) = Constant Term
- \( \beta_1 \) = Beta Coefficient
- \( X_1 \) = Market size
- \( X_2 \) = Political stability
- \( X_3 \) = Economic stability
- \( X_4 \) = Regulatory policies
- \( X_5 \) = Investment promotions
- \( X_6 \) = Infrastructure
- \( X_7 \) = Cost of doing business
- \( E \) = Error Term

From the data collected it will be measured from the key indicators as shown below and then a relationship between FDI inflows and the various determinants will be developed.

From the data collected it was measured from the key indicators as shown below and then a relationship between FDI inflows and the various determinants were developed.

<table>
<thead>
<tr>
<th>Variable</th>
<th>Key indicators</th>
<th>Measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market Size</td>
<td>• Trade liberalization and levels of market integration&lt;br&gt;• Great levels of exports&lt;br&gt;• Levels of local consumption&lt;br&gt;• Population&lt;br&gt;• Efficient and market oriented institutional environment</td>
<td>The larger the market size, the more the inflow</td>
</tr>
</tbody>
</table>
| Political Stability | • Stable government  
• Democratic Accountability  
• Political coups  
• Security of people and property  
• Law and order | The lower the risk in political environment, the higher the investment |
|---------------------|-------------------------------------------------|
| Regulatory          | • Transparency and efficiency  
• Reliable, accessible and publicized regulatory policies  
• Legal certainties and corruption  
• Non-discriminatory treatment of investors  
• Consistency and predictability in government policies | The better the regulations in a country are, the higher the level of investment. |
| Investment promotions | • Monopoly rights  
• Availability of sweeter policies e.g. lower taxes for foreign investors and ax holidays  
• Financial incentives e.g. grants and preferential loans  
• Market preferences  
• Anti-competitive regulations | The higher the level of investment promotions, the higher the investment |
| Economic Stability and growth rate | • Price stability  
• Currency Stability  
• Interest rates  
• Levels of GPI | The higher the level of economic instability, the higher the risk premium on investment and the lower the level of investment |
4.1 Introduction
This chapter presents analysis and findings of the study as set out in the research methodology. The study findings are presented on to establish the determinants of foreign direct investment in the manufacturing sector in Kenya. The data was gathered exclusively from the questionnaire as the research instrument. The questionnaire was designed in line with the objectives of the study.

4.2 Data presentation

4.2.1 Company’s profile

Year of firm establishment in Kenya

![bar chart showing years and percentages of firm establishment](image)

**Figure 4.2.1: Year of firm establishment in Kenya**
The study sought to find out the year the firm was established in Kenya. From the findings, 45.8% of the respondents indicated that the firms they worked in were established in Kenya between 1980 and 1989, 29.2% of the respondents indicated that the firms they worked in were established in Kenya between 2000 and 2009 while only 25% of the respondents indicated that the firms they worked in were established in Kenya between 1970 and 1979.
Type of entity ownership

![Bar chart showing the distribution of entity ownership types.]

**Figure 4.2.2: Type of entity ownership**
The study sought to find out how the entities were owned. From the findings, 62.5% of the entities were private companies (limited by shares), 12% of the entities were franchise entities, 12.5% of the entities were partnerships, 8.3% of the entities were public companies (listed) while only 4.2% of the companies were joint ventures.

![Bar chart showing the distribution of sources and locations of information.]

**Figure 4.2.3: Parent company's most valuable sources & location of information**
The study sought to find out the company's most valuable sources & location of information. From the findings, 54.2% of the respondents indicated that the Parent company's most valuable sources were located in Kenya, 25% of the respondents indicated that the Parent company's most valuable sources were the clients, 16% of the respondents indicated that the Parent company's most valuable sources were located in the home country while only 4.2% of the respondents indicated that the Parent company's most valuable sources was the research done by the entity.
4.3 Concept of FDI

4.3.1 Political stability

Table 4.3. 1: Extent that various factors about political stability in Kenya affect levels of investment by firms in Kenya

<table>
<thead>
<tr>
<th>Change in Factor</th>
<th>No extent</th>
<th>Little extent</th>
<th>Moderate extent</th>
<th>Large extent</th>
<th>Very large extent</th>
<th>Mean</th>
<th>Stdv</th>
</tr>
</thead>
<tbody>
<tr>
<td>Changes in government has negative influence on the firms investment</td>
<td>16.7</td>
<td>50.0</td>
<td>8.3</td>
<td>12.5</td>
<td>12.5</td>
<td>2.5</td>
<td>1.3</td>
</tr>
<tr>
<td>There is law and order in Kenya which has made the levels of inflows by you firm increase</td>
<td>12.5</td>
<td>37.5</td>
<td>25.0</td>
<td>25.0</td>
<td>0</td>
<td>2.6</td>
<td>1.0</td>
</tr>
<tr>
<td>Political coups have an influence in the levels of investment in the organization</td>
<td>20.8</td>
<td>37.5</td>
<td>25.0</td>
<td>8.3</td>
<td>8.3</td>
<td>2.5</td>
<td>1.2</td>
</tr>
<tr>
<td>Surety of property security and that of people has encouraged the levels of investment</td>
<td>50.0</td>
<td>25.0</td>
<td>20.8</td>
<td>4.2</td>
<td>0</td>
<td>2.8</td>
<td>0.9</td>
</tr>
<tr>
<td>Democratic accountability has increased the levels of FDI in the country</td>
<td>20.8</td>
<td>33.3</td>
<td>16.7</td>
<td>12.5</td>
<td>16.7</td>
<td>2.7</td>
<td>1.4</td>
</tr>
</tbody>
</table>

The study sought to find out extent that various factors about political stability in Kenya affect levels of investment by firms in Kenya. According to the findings, respondents indicated that Surety of property security and that of people has encouraged the levels of investment to a moderate extent as shown by a mean of 2.8; democratic accountability has increased the levels of FDI in the country to a moderate extent as shown by a mean of 2.7; There is law and order in Kenya which has made the levels of inflows by the firm increase to a moderate extent as shown by a mean of 2.6; Political coups have an influence in the levels of investment in the organization to a moderate extent as shown by a mean of 2.5 and that Changes in government has negative influence on the firms investment to a moderate extent as show by a mean of 2.5.
4.3.2 Regulatory environment

Table 4.3.2: Respondent’s level of agreement with statements about regulatory environment

<table>
<thead>
<tr>
<th>Statement</th>
<th>No extent</th>
<th>Little extent</th>
<th>Moderate extent</th>
<th>Large extent</th>
<th>Very large extent</th>
<th>Mean</th>
<th>Stdev</th>
</tr>
</thead>
<tbody>
<tr>
<td>There is legal certainties and no corruption in the administration environment of FDI</td>
<td>12.5</td>
<td>29.2</td>
<td>20.8</td>
<td>4.2</td>
<td>33.3</td>
<td>3.2</td>
<td>1.5</td>
</tr>
<tr>
<td>There is efficiency and transparency in business licensing</td>
<td>16.7</td>
<td>20.8</td>
<td>37.5</td>
<td>20.8</td>
<td>4.2</td>
<td>2.8</td>
<td>1.1</td>
</tr>
<tr>
<td>Political coups have an influence in the levels of investment in the organization</td>
<td>29.2</td>
<td>29.2</td>
<td>37.5</td>
<td>4.2</td>
<td>.0</td>
<td>2.2</td>
<td>.9</td>
</tr>
<tr>
<td>Surety of property security and that of people has encouraged the levels of investment</td>
<td>8.3</td>
<td>33.3</td>
<td>37.5</td>
<td>16.7</td>
<td>4.2</td>
<td>2.8</td>
<td>1.0</td>
</tr>
<tr>
<td>Democratic accountability has increased the levels of FDI in the country</td>
<td>12.5</td>
<td>33.3</td>
<td>12.5</td>
<td>16.7</td>
<td>25.0</td>
<td>3.1</td>
<td>1.4</td>
</tr>
<tr>
<td>Kenyan investment sector is well regulated to attract foreign investments in Kenya</td>
<td>16.7</td>
<td>37.5</td>
<td>25.0</td>
<td>12.5</td>
<td>8.3</td>
<td>2.6</td>
<td>1.2</td>
</tr>
</tbody>
</table>

The study sought to find out the respondent’s level of agreement with statements about regulatory environment. According to the findings, respondents indicated that there is legal certainties and no corruption in the administration environment of FDI to a moderate extent as shown by a mean of 3.2, democratic accountability has increased the levels of FDI in the country to a moderate extent as shown by a mean of 3.1, there is efficiency and transparency in business licensing to a moderate extent as shown by a mean of 2.8, surety of property security and that of people has encouraged the levels of investment to a moderate extent as shown by a mean of 2.8, Kenyan investment sector is well regulated to attract foreign investments in Kenya to a moderate extent as shown by a mean of 2.6 and that political coups have an influence in the levels of investment in the organization to a little extent as shown by a mean of 2.2.
4.3.3 Investment proportion

Table 4.3. 3: Extent that various investment promotion incentives have favored the firms’ investment in Kenya

<table>
<thead>
<tr>
<th>Incentive</th>
<th>No extent</th>
<th>Little extent</th>
<th>Moderate extent</th>
<th>Large extent</th>
<th>Very large extent</th>
<th>Mean</th>
<th>Stdev</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lower taxes for foreign investors</td>
<td>54.2</td>
<td>12.5</td>
<td>16.7</td>
<td>16.7</td>
<td>0</td>
<td>2.1</td>
<td>1.5</td>
</tr>
<tr>
<td>Giving monopoly rights to foreign companies</td>
<td>33.3</td>
<td>16.7</td>
<td>12.5</td>
<td>12.5</td>
<td>25.0</td>
<td>2.8</td>
<td>1.6</td>
</tr>
<tr>
<td>Availability of sweetener policies e.g. favorable tax heavens and tax holidays</td>
<td>8.3</td>
<td>25.0</td>
<td>41.7</td>
<td>12.5</td>
<td>12.5</td>
<td>3.0</td>
<td>1.1</td>
</tr>
<tr>
<td>Marketing by the country i.e. The initiatives by Kenya to other countries</td>
<td>12.5</td>
<td>45.8</td>
<td>12.5</td>
<td>16.7</td>
<td>12.5</td>
<td>2.7</td>
<td>1.3</td>
</tr>
<tr>
<td>Raising the education levels and labor skills in Kenya</td>
<td>12.5</td>
<td>37.5</td>
<td>25.0</td>
<td>8.3</td>
<td>16.7</td>
<td>2.8</td>
<td>1.3</td>
</tr>
<tr>
<td>There has been investment promotion done by Kenya that has impacted the levels of investment by the firm</td>
<td>16.7</td>
<td>33.3</td>
<td>20.8</td>
<td>25.0</td>
<td>4.2</td>
<td>2.7</td>
<td>1.2</td>
</tr>
</tbody>
</table>

The study sought to find out the extent that various investment promotion incentives have favored the firms' investment in Kenya. According to the findings, availability of sweetener policies e.g. favorable tax heavens and tax holidays favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 3.0, giving monopoly rights to foreign companies favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 2.8, raising the education levels and labor skills in Kenya favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 2.8, there has been investment promotion done by Kenya that has impacted the levels of investment by the firms favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 2.7, marketing by the country i.e. the initiatives by Kenya to other countries favored the firms’ investment in Kenya to a moderate extent as shown...
by a mean of 2.7 and that lower taxes for foreign investors favored the firms’ investment in Kenya to a little extent as shown by a mean of 2.7.

### 4.3.4 Economic growth and stability

**Table 4.3. 4: Respondents level of agreement with statements about economic growth and stability**

<table>
<thead>
<tr>
<th>Statement</th>
<th>No extent</th>
<th>Little extent</th>
<th>Moderate extent</th>
<th>Large extent</th>
<th>Very large extent</th>
<th>Mean</th>
<th>Stddev</th>
</tr>
</thead>
<tbody>
<tr>
<td>There is predictability in Kenya’s inflation rate that can help determine/predict on the levels of production</td>
<td>54.2</td>
<td>25.0</td>
<td>12.5</td>
<td>4.2</td>
<td>4.2</td>
<td>1.8</td>
<td>1.1</td>
</tr>
<tr>
<td>The currency is known to be stable</td>
<td>41.7</td>
<td>25.0</td>
<td>25.0</td>
<td>4.2</td>
<td>4.2</td>
<td>2.0</td>
<td>1.1</td>
</tr>
<tr>
<td>There is price stability in the country</td>
<td>33.3</td>
<td>41.7</td>
<td>12.5</td>
<td>12.5</td>
<td>0.0</td>
<td>2.0</td>
<td>1.0</td>
</tr>
<tr>
<td>Changes in interests are expected to change often</td>
<td>45.8</td>
<td>20.8</td>
<td>29.2</td>
<td>4.2</td>
<td>0.0</td>
<td>1.9</td>
<td>1.0</td>
</tr>
<tr>
<td>There is growth in GPI in Kenya</td>
<td>12.5</td>
<td>29.2</td>
<td>29.2</td>
<td>29.2</td>
<td></td>
<td>2.8</td>
<td>1.0</td>
</tr>
<tr>
<td>Economic growth and stability in Kenya has contributed to the levels of the inflows by the company</td>
<td>20.8</td>
<td>20.8</td>
<td>25.0</td>
<td>25.0</td>
<td>8.3</td>
<td>2.8</td>
<td>1.3</td>
</tr>
</tbody>
</table>

The study sought to find out the extent that various investment promotion incentives have favored the firms’ investment in Kenya. According to the findings, respondents indicated that economic growth and stability in Kenya has contributed to the levels of the inflows by the companies to a moderate extent as shown by a mean of 2.8, raising the education levels and labor skills in Kenya favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 2.8, there is price stability in the country which has favored the firms’ investment in Kenya to a little extent as shown by a mean of 2.0, the currency is known to be stable to a little extent as shown by a mean of 2.0, no currency devaluations are expected often to a little extent as shown by a mean of 1.9, and that there is predictability in Kenya’s inflation rate that can help determine/predict on the levels of production to a little extent as shown by a mean of 1.8.
### 4.3.5 Market size

**Table 4.3. 5: Respondents level of agreement with statements about Market size**

<table>
<thead>
<tr>
<th>Statement</th>
<th>No extent</th>
<th>Little extent</th>
<th>Moderate extent</th>
<th>Large extent</th>
<th>Very large extent</th>
<th>Mean</th>
<th>Stdev</th>
</tr>
</thead>
<tbody>
<tr>
<td>There is trade liberalization and levels of market integration that have brought market for the products</td>
<td>33.3</td>
<td>37.5</td>
<td>8.3</td>
<td>12.5</td>
<td>8.3</td>
<td>2.3</td>
<td>1.3</td>
</tr>
<tr>
<td>The level of exports of the firms product is high</td>
<td>25.0</td>
<td>45.8</td>
<td>16.7</td>
<td>8.3</td>
<td>4.2</td>
<td>2.2</td>
<td>1.1</td>
</tr>
<tr>
<td>Levels of local consumption of the firms product is promising</td>
<td>29.2</td>
<td>29.2</td>
<td>29.2</td>
<td>8.3</td>
<td>4.2</td>
<td>2.3</td>
<td>1.1</td>
</tr>
<tr>
<td>There is efficiency in exports market environment</td>
<td>25.0</td>
<td>33.3</td>
<td>16.7</td>
<td>20.8</td>
<td>4.2</td>
<td>2.5</td>
<td>1.2</td>
</tr>
</tbody>
</table>

The study sought to find out the respondents level of agreement with statements about Market size. According to the findings, respondents agreed that there is efficiency in exports market environment to a moderate extent as shown by a mean of 2.5, levels of local consumption of the firms product is promising to a little extent as shown by a mean of 2.3, there is trade liberalization and levels of market integration that have brought market for the firms’ products to a little extent as shown by a mean of 2.3, and that the level of exports of the firms product is high to a little extent as shown by a mean of 2.2.

### 4.3.6 Cost of doing business

**Table 4.3. 6: Respondents level of agreement with statements about Cost of doing business**

<table>
<thead>
<tr>
<th>Statement</th>
<th>No extent</th>
<th>Little extent</th>
<th>Moderate extent</th>
<th>Large extent</th>
<th>Very large extent</th>
<th>Mean</th>
<th>Stdev</th>
</tr>
</thead>
<tbody>
<tr>
<td>The cost of starting a business in Kenya is reasonable and attractive</td>
<td>20.8</td>
<td>20.8</td>
<td>29.2</td>
<td>16.7</td>
<td>12.5</td>
<td>2.8</td>
<td>1.3</td>
</tr>
<tr>
<td>Availability of credit for expansion of the business in Kenya</td>
<td>16.7</td>
<td>29.2</td>
<td>20.8</td>
<td>16.7</td>
<td>16.7</td>
<td>2.9</td>
<td>1.4</td>
</tr>
<tr>
<td>Cost of closing the business in Kenya in case it does not pick up is reasonable</td>
<td>33.3</td>
<td>25.0</td>
<td>16.7</td>
<td>20.8</td>
<td>4.2</td>
<td>2.4</td>
<td>1.3</td>
</tr>
<tr>
<td>The procedures involved in enforcing contract details for the organization are reasonable and attractive for the investment</td>
<td>12.5</td>
<td>41.7</td>
<td>12.5</td>
<td>20.8</td>
<td>12.5</td>
<td>2.8</td>
<td>1.3</td>
</tr>
</tbody>
</table>
The study sought to find out the respondents level of agreement with statements about Cost of doing business. According to the findings, respondents agreed that there was availability of credit for expansion of the business in Kenya to a moderate extent as shown by a mean of 2.9, the cost of starting a business in Kenya is reasonable and attractive to a moderate extent as shown by a mean of 2.8, the procedures involved in enforcing contract details for the organization are reasonable and attractive for the investment to a moderate extent as shown by a mean of 2.8, the procedures involved in enforcing contract details for the organization are reasonable and attractive for the investment to a moderate extent as shown by a mean of 2.8, the cost of starting a business in Kenya is reasonable and attractive to a moderate extent as shown by a mean of 2.8 and that the cost of closing the business in Kenya in case it does not pick up is reasonable to a little extent as shown by a mean of 2.4.

4.3.7 Infrastructure

**Table 4.3. 7: Respondents level of agreement with statements about infrastructure**

<table>
<thead>
<tr>
<th>Statement</th>
<th>No extent</th>
<th>Little extent</th>
<th>Moderate extent</th>
<th>Large extent</th>
<th>Very large extent</th>
<th>Mean</th>
<th>Stddev</th>
</tr>
</thead>
<tbody>
<tr>
<td>There is availability of transportation network e.g. ports, rails and roads for free movement of the raw materials and finished goods</td>
<td>8.3</td>
<td>20.8</td>
<td>8.3</td>
<td>41.7</td>
<td>20.8</td>
<td>3.5</td>
<td>1.3</td>
</tr>
<tr>
<td>There is power which helps in the manufacturing of the company's products</td>
<td>12.5</td>
<td>12.5</td>
<td>16.7</td>
<td>16.7</td>
<td>41.7</td>
<td>3.6</td>
<td>1.5</td>
</tr>
<tr>
<td>Availability of water and sanitation has enabled the company to do the investment in the country</td>
<td>16.7</td>
<td>25.0</td>
<td>16.7</td>
<td>20.8</td>
<td>20.8</td>
<td>3.0</td>
<td>1.4</td>
</tr>
<tr>
<td>Availability of telecommunication network which assists in the communication</td>
<td>12.5</td>
<td>12.5</td>
<td>29.2</td>
<td>8.3</td>
<td>37.5</td>
<td>3.5</td>
<td>1.4</td>
</tr>
</tbody>
</table>

The study sought to find out the respondents level of agreement with statements about infrastructure in Kenya. According to the findings, respondents agreed that there is power which helps in the manufacturing of the company's products to a very large extent as shown by a mean of 3.6, there is availability of telecommunication network which assists in the communication to a very large extent as shown by a mean of 3.5, there is availability of transportation network e.g. ports, rails and roads for free movement of the raw materials and finished goods to a very large extent as shown by a mean of 3.5.
extent as shown by a mean of 3.5 and that there was availability of water and sanitation which has enabled the company to do the investment in the country to a moderate extent as shown by a mean of 3.0.

4.4 Regression analysis

The study required regression analysis so as to establish the relationship between the independent variables (political stability, regulatory environment, investment proportion, economic growth and stability, market size, cost of doing business and infrastructure) and the dependent variable (foreign direct investment inflows in the manufacturing sector in Kenya).

According to the findings from the data, the following results were established by use of the SPSS (Statistical Package for Social Sciences).

Table 4.4.1: Coefficient of Determination (R²)

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.587 (a)</td>
<td>.345</td>
<td>.203</td>
<td>.125</td>
</tr>
</tbody>
</table>

Source: Researcher, 2012

Predictors: (Constant), political stability, regulatory environment, investment proportion, economic growth and stability, market size, cost of doing business and infrastructure. Coefficient of determination explains the extent to which changes in the dependent variable can be explained by the change in the independent variables or the percentage of variation in the dependent variable (foreign direct investment inflows) that is explained by all the seven independent variables (political stability, regulatory environment, investment proportion, economic growth and stability, market size, cost of doing business and infrastructure.)

Table 4.4.2: Multiple Regression Analysis

| Model | Unstandardized Coefficients | Standardized Coefficients | T | Sig. |
Dependent Variable: Foreign Direct Investment

The researcher conducted a multiple regression analysis so as to determine the relationship between Foreign Direct Investment and the seven independent variables. The regression equation

\[ \text{Foreign Direct Investment} = \alpha + \beta_1 \text{ (Political stability)} + \beta_2 \text{ (Regulatory environment)} + \beta_3 \text{ (Investment proportion)} + \beta_4 \text{ (Economic growth and stability)} + \beta_5 \text{ (Market size)} + \beta_6 \text{ (Cost of doing business)} + \beta_7 \text{ (Infrastructure)} + e \]

now becomes:

\[ \text{Foreign Direct Investment inflows (Y)} = 1.124 + 0.117 \text{ (Political stability)} + 0.018 \text{ (Regulatory environment)} + 0.199 \text{ (Investment promotion)} + 0.169 \text{ (Economic growth and stability)} + 0.164 \text{ (Market size)} + 0.293 \text{ (Cost of doing business)} + 0.037 \text{ (Infrastructure)} + e \]

4.5 Summary and Interpretation of the findings

4.5.1 Political stability

The study sought to find out extent that various factors about political stability in Kenya affect levels of investment by firms in Kenya. According to the findings, respondents indicated that Surety of property security and that of people has encouraged the levels of investment to a
moderate extent as shown by a mean of 2.8; democratic accountability has increased the levels of FDI in the manufacturing levels to a moderate extent as shown by a mean of 2.7; There is law and order in Kenya which has made the levels of inflows by the firm increase to a moderate extent as shown by a mean of 2.6; Political coups have an influence in the levels of investment in the organization to a moderate extent as shown by a mean of 2.5 and that Changes in government has negative influence on the firms’ investment to a moderate extent as show by a mean of 2.5.

4.5.2 Regulatory environment

The study sought to find out the respondent’s level of agreement with statements about regulatory environment. According to the findings, respondents indicated that there is legal certainties and no corruption in the administration environment of FDI to a moderate extent as shown by a mean of 3.2, democratic accountability has increased the levels of FDI in the country to a moderate extent as shown by a mean of 3.1, there is efficiency and transparency in business licensing to a moderate extent as shown by a mean of 2.8, surety of property security and that of people has encouraged the levels of investment to a moderate extent as shown by a mean of 2.8, Kenyan investment sector is well regulated to attract foreign investments in Kenya to a moderate extent as shown by a mean of 2.6 and that political coups have an influence in the levels of investment in the organization to a little extent as shown by a mean of 2.2.

4.5.3 Investment promotion

The study sought to find out the extent that various investment promotion incentives have favored the firms’ investment in Kenya. According to the findings, availability of sweetener policies e.g. favorable tax heavens and tax holidays favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 3.0, giving monopoly rights to foreign companies favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 2.8, raising the education levels and labor skills in Kenya favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 2.8, there has been investment promotion done by Kenya that has impacted the levels of investment by the firms favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 2.7, marketing by the country i.e. the initiatives by
Kenya to other countries favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 2.7 and that lower taxes for foreign investors favored the firms’ investment in Kenya to a little extent as shown by a mean of 2.7.

4.5.4 Economic growth and stability
The study found out that economic growth and stability in Kenya has contributed to the levels of the inflows by the companies to a moderate extent as shown by a mean of 2.8, raising the education levels and labor skills in Kenya favored the firms’ investment in Kenya to a moderate extent as shown by a mean of 2.8, there is price stability in the country which has favored the firms’ investment in Kenya to a little extent as shown by a mean of 2.0, the currency is known to be stable to a little extent as shown by a mean of 2.0, no currency devaluations are expected often to a little extent as shown by a mean of 1.9, and that there is predictability in Kenya’s inflation rate that can help determine/predict on the levels of production to a little extent as shown by a mean of 1.8.

4.5.5 Market size
The study found out that there is efficiency in exports market environment to a moderate extent as shown by a mean of 2.5, levels of local consumption of the firms product is promising to a little extent as shown by a mean of 2.3, there is trade liberalization and levels of market integration that have brought market for the firms’ products to a little extent as shown by a mean of 2.3, and that the level of exports of the firms product is high to a little extent as shown by a mean of 2.2.

4.5.6 Cost of doing business
The study found out that there was availability of credit for expansion of the business in Kenya to a moderate extent as shown by a mean of 2.9, the cost of starting a business in Kenya is reasonable and attractive to a moderate extent as shown by a mean of 2.8, the procedures involved in enforcing contract details for the organization are reasonable and attractive for the investment to a moderate extent as shown by a mean of 2.8, the cost of starting a business in Kenya is reasonable and attractive to a moderate extent as shown by a mean of 2.8 and that the cost of closing the business in Kenya in case it does not pick up is reasonable to a little extent as shown by a mean of 2.4.
4.5.7 Infrastructure

The study found out that there is power which helps in the manufacturing of the company's products to a very large extent as shown by a mean of 3.6, there is availability of telecommunication network which assists in the communication to a very large extent as shown by a mean of 3.5, there is availability of transportation network e.g. ports, rails and roads for free movement of the raw materials and finished goods to a very large extent as shown by a mean of 3.5 and that there was availability of water and sanitation which has enabled the company to do the investment in the country to a moderate extent as shown by a mean of 3.0.

According to the regression equation established seven independent variables were studied and only represents 58.7% of foreign Direct Investment determinants as represented by the $R^2$. This therefore means the seven independent variables only contribute about 58.7% to foreign Direct Investment while other factors not studied in this research contributes 42.3% of foreign Direct Investment.

Taking all factors (political stability, regulatory environment, investment proportion, economic growth and stability, market size, cost of doing business and infrastructure) and constant at zero, the effect to Foreign Direct Investment will be 1.124. The data findings analyzed also shows that taking all other independent variables at zero, a unit increase in Political stability will lead to a 0.117 increase in Foreign Direct Investment. A unit increase in Regulatory environment will lead to a 0.018 increase in Foreign Direct Investment; a unit increase in Investment proportion will lead to a 0.199 increase in Foreign Direct Investment; a unit increase in Economic growth and stability will lead to a 0.169 increase in Foreign Direct Investment; a unit increase in Market size will lead to a 0.164 increase in Foreign Direct Investment; a unit increase in Cost of doing business will lead to a 0.293 increase in Foreign Direct Investment while a unit increase in Infrastructure will lead to a 0.037 increase in Foreign Direct Investment.
CHAPTER FIVE

SUMMARY OF THE FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 Summary
The study aimed at establishing determinants of foreign direct investment in the manufacturing sector in Kenya. This objective was achieved by analyzing the different variables that were taken into account to establish the determinants of FDI in the manufacturing sector in Kenya. Thirty manufacturing companies were sampled based on the belief that they were a satisfactory number to represent the total manufacturing firms in Kenya. The results regarding overall performance seem to be consistent with the literature review, where the empirical studies show that stability in the economy, political environment and institutions in a country encourage the FDI inflows. In fact, the news about the level of stability in Kenya can depress or encourage the FDI inflows.

The study found out that in political stability, surety of property security and that of people, democratic accountability, law and order in Kenya has made the levels of inflows by the firm to increase while Political coup and changes in government have negative influence on the firm’s investment. The respondents agreed that in the regulatory environment when there are legal certainties, transparency in business licensing and no corruption in the administration environment of FDI increased the levels of FDI in the Kenya.

It was evident from the respondents that investment promotion through the availability of sweetener policies e.g. favorable tax heavens and tax holidays, giving monopoly rights to foreign companies, investment promotions and marketing by the country i.e. the initiatives by Kenya to other countries has favored the firms’ FDI inflows. The economic growth and stability in Kenya has contributed to the levels of the inflows by the companies however there has been difficulty in the prediction of the Kenya’s inflation rate that can help determine/predict future value of currencies hence price instability which has led to decrease in FDI levels.
The study found out that availability of market for manufactured goods especially efficiency in exports market and local consumption increased FDI inflows. There has been trade liberalization and market integration that have brought market for the firms’ products also increasing the levels of FDI inflows in the country. It was evident from the respondents that cost of doing business through the availability of credit for expansion of the business and reasonable and attractive cost of starting a business in Kenya is reasonable and attractive hence encouraging the levels of FDI inflows. Also there is improved infrastructure in the transportation network, telecommunication network and power which has increased the levels of FDI in Kenya.

5.2 Conclusion

Identifying determinants of FDI in manufacturing sector in Kenya is a broad and complex issue. This paper attempted to find out the determinants of FDI in the manufacturing sector in Kenya considering the market size, political stability, infrastructure, cost of doing business, investment promotion and regulatory environment as variables of measure. The results of this study reveal very useful insights in understanding foreign investments in manufacturing sector in Kenya. One of the key factors for FDI investment in Kenya is Cost of doing business. Availability of credit for expansion of the business and reasonable and attractive cost of starting up a business has encouraged the levels of FDI inflows in Kenya. Investment promotion has also contributed a great deal in the levels of FDI inflows through the availability of sweetener policies e.g. favorable tax heavens and tax holidays; giving monopoly rights to foreign companies; raising the education levels and labor skills.

Political stability in Kenya has been uncertain for some time. It is evident that Surety of property security and that of people, democratic accountability, law and order in Kenya has positive influence on the levels of inflows by the firm whereas Political coups and Changes in government have negative influence on the firm’s investment. The role of the government and public agencies in encouraging FDI in Kenya is largely missing. Very few firms seem to have contacted the government for any form of assistance. There appears to be a lose link between the government and its related agencies with the foreign investors. Most foreign investors perceive the government to be unfriendly and hostile to their operations. There is need for a greater government’s appreciation of the importance of FDI through provision for an avenue for
interaction in order to address their concerns. Economic growth and stability has also been a factor of importance whereby predictability in Kenya’s inflation has been uncertain hence price instability and currency devaluations. This has contributed to low levels of FDI inflows in Kenya.

Other variables that were considered include market size where efficiency in exports of the firms’ product is high whereas levels of local consumption of the firms’ product are not as high. From this it shows there is trade liberalization and levels of market integration that have brought market for the firms’ products and levels of exports of the firms’ product to be made high. Infrastructure has been seen to have been developed which has assisted a great deal in the manufacturing companies. This is seen by the availability of telecommunication network which assists in the communication, availability of transportation network i.e. ports, rails and roads which have assisted in free movement of the raw materials and finished goods. Of the Kenyan market this could have potentially led to attraction of other firms in to these segments to take advantage of the abnormal profits enjoyed. This has also led to encouragement of new entrants into these sectors which have helped to enhance healthy competition. The study concludes that in the regulatory environment, there are legal uncertainties and corruption in the administration environment of FDI that discourages FDI inflows hence lack of efficiency and transparency in business licensing of FDI firms.

The above indicates that Kenya is a very important market and investing in Kenya is part of firms’ global strategy. In conclusion, foreign firms do not simply come to Kenya to take the advantage of any single determinant factor, but are more importantly driven by a whole myriad of often conflicting and competing reasons.

5.3 Recommendations

The study recommends the firms to ensure there is surety of property security and that of people as this encourages the levels of investment. The government should ensure that there is law and order in Kenya as changes in government has negative influence on the firm’s investment.
The government should also ensure eradication of corruption in the administration environment; ensure there is democratic accountability, efficiency and transparency in business licensing. Further the Kenyan investment sector should be well regulated to attract foreign investments in Kenya.

The study further recommends that sweetener policies e.g. favorable tax heavens and tax holidays be adopted by the government to increase the level of foreign firms’ investment in Kenya. Further, the foreign firms can be given monopoly rights to favor the firms’ investment in Kenya. In addition investment promotion should be done by the Kenyan government and also lower taxes for foreign investors to improve the level of foreign firms’ investment in the country. The government should ensure there is consistent and sustained economic growth and stability in Kenya, raise the education levels and labor skills ensure there is price stability in the country and also monitor the inflation rate to promote foreign firms’ investment in the country.

Further, there should be efficiency in exports market environment, trade liberalization and market integration to widen the market for the firms’ products.

Policies should also be put in place to ensure there is availability of credit for expansion of the business in Kenya and to review the cost of starting a business in Kenya to ensure that it is reasonable and attractive.

Finally, in addition to availability of water and sanitation, there should be uninterrupted power supply in the manufacturing sector to prevent breakdowns in the process of production. Telecommunication and transportation networks should be well developed for free movement of the raw materials and finished goods to the market.

5.4 Limitations of the study
The number of the manufacturing firms in Kenya is big making it possible only to use a sample. Furthermore the firms are located in different parts of the country and dealing with different manufacturing of products hence a limitation of scope.
Data was not collected hundred percent since not all the respondents were willing to give the information that was requested. Data was analyzed only on seventy percent of the questionnaires that were issued and responded to.

5.5 Suggestions for further studies

The seven independent variables that were studied, explain only 58.7% of foreign Direct Investment as represented by the $R^2$. This therefore means the seven independent variables only contribute about 58.7% to foreign Direct Investment while other factors not studied in this research contributes 42.3% of foreign Direct Investment. Therefore, further research should be conducted to investigate the other factors (42.3%) that affect foreign Direct Investment.

There was also much concentration on the manufacturing sector in Kenya which is resource based but left out service sector which market is seeking. Both of the sectors are important in the growth of the Kenyan economy and this does not mean that what affects the manufacturing sector affects the service sector too, hence leaving a room to explore what are the determinants of FDI inflows in the service industry in Kenya.

The study too concentrated so much on primary data which was interpreted using the regression analysis. This means that further research can be carried out based considering secondary data or both primary and secondary data and interpretation of the results done using a different model to find out if the results would be different to find out the determinants of FDI inflows in a country.
REFERENCES


Kareithi, P.J.M (1991) “Multinational corporations and foreign owned media in developing countries.” *Crime, Law and Social Change*, 16(2);199-212.


MacDougall, G.D.A. (1960). The benefits and costs of private investment from abroad: A


APPENDICES

APPENDIX 1: Letter of Introduction

LETTER OF INTRODUCTION

CAROLYNE KITHINJI

P.O BOX 2924-00200

NAIROBI

Dear Sir/Madam,

RE: RESEARCH ON DETERMINANTS OF FDI IN MANUFACTURING SECTOR IN KENYA

I am a student at University of Nairobi doing a Master’s in Business Administration. I am undertaking the above research project as part of my Academia requirements.

I would be grateful if you could spare some time and fill the questionnaire answering as honestly as possible.

The information that you shall give shall be treated with the utmost confidentiality and will be used solely for the purpose of this research. The findings of this research may be availed to you upon completion of the research.

Upon completion of the questionnaire, kindly enclose in the envelope provided and I will pick it from your offices. In case of any queries don’t hesitate to call me on 0720842990

Thank you for your cooperation.

Yours sincerely,

Carol Kithinji
APPENDIX 2: QUESTIONNAIRE

A.) COMPANY’S PROFILE

1.) What is the name of your firm

2.) Which year was the firm was established in Kenya?
- Before 1970
- 1970-1979
- 1980-1989
- 2000-2009

3.) What type of Ownership is your Entity?
- Franchise
- Private Company (Limited by shares)
- Public Company (publicly listed)
- Joint Venture
- Partnership

4.) What are the Parent company’s most valuable sources & location of information?
- Research done by entity
- Customer/Client
- Kenya
- Home country
- Both Home and Kenya
B.) CONCEPT OF FDI

Please tick where appropriate

Political Stability

To what extent have the following factors in the political stability in Kenya affected the levels of investment by your firm in Kenya?

Use a scale of 1-5 where 1) No extent (2) Little extent (3) Moderate extent (4) large extent (5) Very large extent

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Changes in government has negative influence on your firm’s investment</td>
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<tr>
<td>There is law and order in Kenya which has made the levels of inflows by your firm increase</td>
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<tr>
<td>Political coups have an influence in the levels of investment in your organization</td>
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<tr>
<td>surety of property security and that of people has encouraged the levels of investment</td>
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<tr>
<td>Democratic accountability has increased the levels of FDI in the country</td>
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</tbody>
</table>
**Section C: Regulatory Environment**

Using a scale of 1 to 5 indicate the level of agreement with the following statement in relation to Regulatory Environment

Use a scale of 1-5 where 1 = to a very great extent 2= to a great extent 3= moderate extent 4= to a little extent 5= strongly agree

<table>
<thead>
<tr>
<th>Statement</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>There is legal certainties and no corruption in the Administration environment of FDI</td>
<td></td>
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<tr>
<td>There is efficiency and transparency in business Licensing</td>
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<td></td>
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<tr>
<td>The regulatory policies are reliable, accessible and well publicized</td>
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<tr>
<td>There is non-discriminatory treatment of investors, consistency and predictability in government policies</td>
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<tr>
<td>There is availability of anti-competitive regulations</td>
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<tr>
<td>Kenyan Investment sector is well regulated to attract Foreign Investments in Kenya</td>
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</tbody>
</table>

**SECTION D: Investment Promotion**

To what extent do you think the following investment promotion incentive has favoured your firm investment in Kenya?

Use a scale of 1 to 5 indicate the level of agreement where 1) No extent (2) Little extent (3) Moderate extent (4) large extent (5) Very large extent

<table>
<thead>
<tr>
<th>Incentive</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lower taxes for foreign investors</td>
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<td></td>
</tr>
<tr>
<td>Giving monopoly rights to Foreign companies</td>
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</tr>
</tbody>
</table>
Availability of sweetener policies e.g. Favourable tax heavens and tax holidays

Marketing by the country i.e. the initiatives by Kenya to other countries

Raising the education levels and labour skills in Kenya

There has been investment promotion done by Kenya that has impacted the levels of investment by your firm

SECTION E: Economic Growth and Stability

Using a scale of 1 to 5 indicate the level of agreement with the following statement in relation to Economic Growth and Stability

1) No extent (2) Little extent (3) Moderate extent (4) large extent (5) Very large extent

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>There is predictability in Kenya’s inflation rate that can help determine/predict on the levels of production</td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>The Currency is known to be stable</td>
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</tr>
<tr>
<td>There is price stability in the country</td>
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<td></td>
</tr>
<tr>
<td>No Currency devaluations are expected often</td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Return on Investments are certain or can be predicted</td>
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</tr>
<tr>
<td>Economic Growth and Stability in Kenya has contributed to the levels of the inflows by your company</td>
<td></td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>
SECTION F: Market Size

9). Does Kenya have a market for the goods manufactured in your firm?

   Yes ( )          No ( )

10). Using a scale of 1 to 5 indicate the level of agreement with the following statement in relation to Market Size

1) No extent (2) Little extent (3) Moderate extent (4) large extent (5) Very large extent

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>There is trade liberalization and levels of market integration that have brought market for your products</td>
<td></td>
<td></td>
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<tr>
<td>The levels of exports of the firm’s product is high</td>
<td></td>
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<tr>
<td>Levels of local consumption of the firms product is promising</td>
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</tr>
<tr>
<td>There is efficiency in exports market environment</td>
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</tbody>
</table>
### APPENDIX 3: Sample of FDI Manufacturing Firms in Kenya

<table>
<thead>
<tr>
<th>Company</th>
<th>Ownership</th>
<th>Activity</th>
</tr>
</thead>
<tbody>
<tr>
<td>British American Tobacco (Kenya)</td>
<td>United Kingdom</td>
<td>Tobacco</td>
</tr>
<tr>
<td>Unilever Kenya</td>
<td>United Kingdom</td>
<td>Food</td>
</tr>
<tr>
<td>Brooke Bond Kenya</td>
<td>United Kingdom</td>
<td>Agriculture</td>
</tr>
<tr>
<td>EA Portland Cement Company</td>
<td>France</td>
<td>Non-metallic mineral</td>
</tr>
<tr>
<td>Carnaud Metalbox</td>
<td>United States</td>
<td>Metals</td>
</tr>
<tr>
<td>George Williamson Kenya</td>
<td>United Kingdom</td>
<td>Agriculture (Tea)</td>
</tr>
<tr>
<td>Rhone Poulenc Kenya</td>
<td>France</td>
<td>Pharmaceuticals</td>
</tr>
<tr>
<td>Cadbury Kenya</td>
<td>Netherlands</td>
<td>Food</td>
</tr>
<tr>
<td>Nestle Foods Kenya</td>
<td>Switzerland</td>
<td>Food</td>
</tr>
<tr>
<td>Elida Ponds Kenya</td>
<td>United Kingdom</td>
<td>Pharmaceuticals</td>
</tr>
<tr>
<td>Teita Estate</td>
<td>Greece</td>
<td>Textiles</td>
</tr>
<tr>
<td>Kapchorua Tea Company</td>
<td>United Kingdom</td>
<td>Agriculture</td>
</tr>
<tr>
<td>Henkel Polymer Co</td>
<td>Germany</td>
<td>Chemicals</td>
</tr>
<tr>
<td>PZ Cussons</td>
<td>Britain</td>
<td>Toilettes</td>
</tr>
<tr>
<td>GlaxoSmithKline beecham</td>
<td>United States</td>
<td>Pharmaceuticals</td>
</tr>
<tr>
<td>Birch Investments</td>
<td>Hong-Kong</td>
<td>Garments</td>
</tr>
<tr>
<td>Indigo Garments</td>
<td>India</td>
<td>Garments</td>
</tr>
<tr>
<td>Jar Kenya</td>
<td>USA</td>
<td>Garments</td>
</tr>
<tr>
<td>California Link EPZ (K) Ltd</td>
<td>Sri Lanka</td>
<td>Garments</td>
</tr>
<tr>
<td>Kenya Knit Garments</td>
<td>Taiwan</td>
<td>Garments</td>
</tr>
<tr>
<td>De La Rue Currency and Security</td>
<td>Britain</td>
<td>Currency &amp; security</td>
</tr>
<tr>
<td>Golden Light</td>
<td>China</td>
<td>Torch bulbs</td>
</tr>
<tr>
<td>Indu Farm</td>
<td>Netherlands</td>
<td>Fruits &amp; vegetables</td>
</tr>
<tr>
<td>Iveye Aqua</td>
<td>India</td>
<td>Pharmaceuticals</td>
</tr>
<tr>
<td>Nor brook Africa</td>
<td>UK</td>
<td>Pharmaceuticals</td>
</tr>
<tr>
<td>East-African Breweries</td>
<td>US</td>
<td>Beverage</td>
</tr>
<tr>
<td>Coca-Cola</td>
<td>US</td>
<td>Beverage</td>
</tr>
<tr>
<td>Bamburi Cement</td>
<td>France</td>
<td>Cement</td>
</tr>
<tr>
<td>Johnsons &amp; Johnsons</td>
<td>UK</td>
<td>Toilettes</td>
</tr>
</tbody>
</table>