UNIVERSITY OF NAIROBI

THE CHALLENGES OF IMPLEMENTING ECONOMIC REFORM PROGRAMMES IN DEVELOPING COUNTRIES: A CASE STUDY OF THE BRETTON WOODS INSTITUTIONS POLICIES IN KENYA 1983-2005

BY

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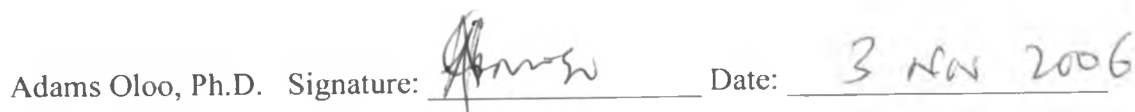
DECLARATION

This dissertation is my original work and has not been presented for a degree in any other University.

George K Shiundu (Signature) ______________ Date: 3 Nov 2006

This dissertation has been submitted for examination with my approval as a University Supervisor.



Adams Oloo, Ph.D. Signature: ______________ Date: 3 Nov 2006

ABSTRACT

Economic development is not a phenomenon. The policies of governments and the international economic environment are decisive influences. It is worth identifying the factors that can create a climate conducive to economic takeoff. The challenges facing developing nations and the factors that are critical to overcoming these challenges must be addressed by both the governments of the developing countries and other international stakeholders.

Although Kenya has made some economic and social progress, this has not been sufficient to eradicate corruption and bad governance. To fight corruption, the government must invest in people particularly in education, health and infrastructure. Second, regional integration is imperative if large markets are to be created that can attract investment. It is important that the private sector as an engine of growth is enhanced to avoid the dependency syndrome that makes IMF impose donor conditionalities.

The policies enacted by the Government of Kenya immediately after independence largely emphasized the role of the public sector. In the process, the private sector was marginalized. As a result of these policies, private sectors were poorly developed and do not have the capacity to produce wealth that is needed to meet rising obligations. Public sector led growth, has been disappointing for Kenya. It is now well accepted that durable economic growth requires a well-established private sector. The role of the private sector in economic development provides an enabling environment in the development of the private sector. Kenya should undertake deliberate efforts to ensure that it has a viable private sector.

Economic growth requires a productive labour force. While Kenya is endowed with immense natural resources, its ability to convert these resources to valuable commodities is limited. The primary reason for this outcome is low productivity of the labour force. The low productivity can be explained by the fact that Kenya has extremely low levels of human capital. For Kenya to meet the challenges of the 21st century, it must invest heavily in her people. The key is for Kenya to strive to have an educated and healthy labour force, which naturally requires deliberate population control policies and higher public investment in health, education and infrastructure.

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ABBREVIATIONS

ACECA	Anti- Corruption and Economic Crimes Act
AIDS	Acquired Immune Deficiency Syndrome
ATM	Automated Teller Machine
CBK	Central Bank of Kenya
CDC	Commonwealth Development Co-operation
CIS	Commonwealth of Independent States
DANIDA	Danish International Development Assistance
EPZ	Export Processing Zone
ERS	Economic Recovery Strategy for Employment and Wealth Creation
EU	European Union
FISS	Farm Input Supply Scheme
GDP	Gross Domestic Project
GoK	Government of Kenya
HIPC	Highly Indebted Poor Countries
HIV	Human Immunodeficiency Virus
IADP	Integrated Agricultural Development Project
IBRD	International Bank for Reconstruction and Development
IMF	International Monetary Fund
KACC	Kenya Anti-Corruption Commission
KAM	Kenya Association of Manufacturers
KANU	Kenya African National Union
KenGen	Kenya Energy Generating Company
KPLC	Kenya Power Lighting Company
LDC	Less Developed Countries
MDGs	Millennium Development Goals
MOJCA	Ministry of Justice and Constitutional Affairs
MNC(s)	Multi-National Corporation(s)
MP	Member of Parliament
MTEF	Medium Term Expenditure Framework
MUB	Manufacturing Under Bond
NARC	National Rainbow Coalition
NCPB	National Cereals and Produce Board
NGO	Non-Governmental Organization
NHIF	National Hospital Insurance Fund
NICs	Newly Industrialized Countries
PFI	Private Foreign Investment
POEA	Public Officer Ethics Act
PRSP	Poverty Reduction Strategy Paper
SAL	Structural Adjustment Loan
SAPs	Structural Adjustment Programmes
SCIP	Smallholder Coffee Improvement Project
SU	Soviet Union
Telkom	Kenya Telecommunications Corporation

TI	Transparency International
TRJC	Truth, Justice and Reconciliation Commission
UN	United Nations
UNDP	United Nations Development Project
USA	United States of America
USAID	US Agency for International Development
USD	United States Dollars
VSAT	Very Short Aperture Transmission
WB	World Bank
WTO	World Trade Organization

CHAPTER ONE

FRAMEWORK OF THE STUDY

Introduction

I believe that it is critically important for us to empower ourselves, to ensure that we have the wit and the wherewithal to decide our own destiny. But it is not easy in a world where the large majority of the countries of the developing world are already debt-enslaved, or under International Monetary Fund (IMF) rule of massive World Bank (WB) conditionalities, or is dependent on foreign aid from the developed countries. For most of these developing countries, who can no longer decide what they can do for their peoples, my warning, my urgings, and my predictions are much too late. But as history has shown, the tide can be turned.[1]

The geographical and ecological environment of Kenya is somehow harsh. Kenya is an enormous country with the amount of good arable land severely limited. The productive areas are found within the highlands regions while the rest consists of semi arid land. Kenya's continuing economic crisis presents an extra–ordinary challenge to the development of the community to both intellectuals and policy makers. In their response to this challenge, the IMF has issued a series of reports on Kenya. They have increasingly concentrated on measures needed to set Kenya's economy on the path to recovery.[2]

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[1] Mahathir Mohamed: *Globalisation and the New Realities*, (Putrajaya, Pelanduk, 2003) pp.86-87
[2] Central Bank of Kenya, *Kenya Land of Opportunity* (Nairobi,1991) p.48

The IMF and the International Bank for Reconstruction and Development (IBRD) popularly known as World Bank were the two financial institutions established in 1946, following plans agreed upon in July, 1944, by experts from 44 nations meeting in Breton Woods, New Hampshire. The purpose for which these institutions were established points to their role in resource mobilization for development. With such massive destruction worldwide, immediately after the Second World War it was necessary that a framework be established to channel funds for reconstruction and development. The WB was established to promote and supplement the international flow of long-term funds for construction and development by selling its own bonds in the principal money centers and lending the proceeds and guaranteeing loans made by others.[3]

Clearly no single group can claim to have done full justice to the diversity of Kenya's economy, the complexity of the problem it confronts and the driving views of how best to tackle them. No one should pretend to have solutions to Kenya's economic problems, but the goal should shift carefully through the evidence to listen to many view points and to set forth Kenya's best assessment of the policies and measures needed for Kenya to achieve a sustained and sustainable improvement in welfare.[4] The IMF has many purposes of which the provision of financial aid to member countries needing assistance to meet actual or threatened deficits in their balance of payments is the most important. The Fund provides for short-term loans to enable the countries meet their budget deficits to be paid within three to five years. The Fund has established a system of free multilateral payments and reduction of other barriers to trade and payments. In addition

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[3] Mahatir Mohammed op.cit p.152

[4] Government of Kenya, Central Bureau of Statistics, *Geographic Dimensions of Well-being in Kenya*, Ministry of Planning and National Development, Vol 1 2003 p.9

it provides an orderly system and altering exchange rates. All these were as a result of Second World War when the exchange rate fluctuated widely.[5]

The root cause of Kenya's weak economic performance in the past has been the failure of public institutions, private sector initiative and market mechanisms to promote Kenya's economic growth. But these requirements must go hand in hand with good governance, a public service that is efficient, a judicial system that is reliable and an administration that is accountable to its public. In addition, a better balance is needed between the government and the governed so as to promote economic growth and eradicate donor dependency. The difficulties facing Kenya are formidable. The margin for manoeuvre is slim indeed. The risks of failures are devastating in human terms. Hence the need for concerted action among all partners in development be it the government or multi-lateral institutions, the private sector and the donors, official and non-governmental are of great importance. Once these parameters are taken care of, then Kenya will register economic growth and surpass the best level ever reached in its history.[6]

Background to the problem

Why is it that so many rich countries, despite all their globalisation and liberalisation rhetoric, will not remove the barriers on those products such as textiles, clothing and footwear in which the poor countries are world-beaters? Why is there instead tariff escalation on all those important products where the developing world is able to develop

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[5] Mahatir Mohammed op.cit p. 153

[6] Government of Kenya, Central Bureau of Statistics, Vol 1 2003 op.cit p.9

awesome global competitiveness?[7] Maybe the third world has over relied on agriculture. The Kenyan economy is basically agriculture-driven. The country has a population of about 30 million and at least 80 per cent of the employed population is found in this sector. The main cash crops grown are coffee, tea, pyrethrum and horticulture especially flowers. Other agro-based products include maize, wheat, sugar cane, cotton and livestock. Closely following is the manufacturing sector, the tourist and the general services sector.

Since independence, Kenya's economy has experienced a number of cycles of growth following down turns and stagnations. Immediately after independence between 1964 and 1971, the economy registered a GDP growth averaging 6.5 per cent. The oil shocks of the early 1970s, the collapse of East African Community in 1977 and other external factors caused a marked slowdown in growth in this decade. However, the 'coffee-boom' induced growth in 1976-1977 but only on a temporary basis.[8] The debt crisis of the early 1980s turned Kenya into a highly indebted nation. The debt problem was exacerbated by macroeconomic mismanagement in the 1990s, leading to a reduction of donor inflows. The government has thus resorted to occasional debt rescheduling and expensive short-term domestic borrowing to finance its expenditures. Debts induce uncertainty and affects private investment via high interest rates and the development of the financial sector. High interest rates dictate that a large proportion of expenditure must

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[7] Mahathir Mohamed, op.cit p.77
[8] The Treaty of the Establishment of the East African Community p.1

be allocated to interest payments. Debt distorts the economy and complicates macroeconomic management.[9]

In Kenya debt service has crowded out funding for capital and social expenditures. After debt servicing and salaries, there is little left for core functions of the government, basic infrastructure, education, health and other essential services, to create an enabling environment for the private sector. Kenya's economy stabilized in the 1980s with a GDP growth around 5 per cent being recorded except in the 1984 drought year. In 1989, growth started to decline as a result of poor weather, regional conflicts, influx of refugees and global recession lowered demand for Kenya's traditional exports namely coffee, tea and pyrethrum. The short-term dislocation caused by structural adjustment, inadequate macroeconomic management and political uncertainty were other contributing factors towards the decline of the country's economy. A combination of improved weather, the favourable impact of economic liberalization and the emergence of global economy from recession led to a much improved GDP of 3 per cent in 1994 and 4.9 per cent in 1995.[10]

Kenya's economy has continued to depend largely on donors. Faced with increased poverty and severe budgetary constraints the government resorted to borrowing from the development partners and international financial institutions notably the IMF and the World Bank. The IMF and the World Bank have been imposing non-economic conditions and withholding budget support on the basis of poor governance, corruption and coercing the government to hasten its privatisation program. As it unfolds, the aid that is finally

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[9] Kenya Land of Opportunity, op.cit p.76

[10] Government of Kenya, *Poverty Reduction Strategy Paper for Period 2001-2004*, Ministry of Planning and National Development p.32

given is not well managed as targeted and this has contributed to low or negative economic growth.[11]

Kenya's economy has continued to experience poor performance. Economic growth over the last five years averaged 2 per cent per annum, with the worst performance experienced in 2000 at negative 0.3 per cent due to poor weather, leading to electricity power rationing and the continued impasse in external resources flows. [12] The economy is however at a turning point and the steps taken over the past several years may bear fruits in terms of economic growth. The pro-poor growth strategies proposed in the 2002-2008 National Development Plan have a target and gradual recovery process, to realize an annual average of 4 per cent growth in GDP over the next several years[13].

Problem Statement

In Kenya, the early 1980s were characterized by high budget deficits, high inflation and unsustainable current account deficits. These financial imbalances were triggered by, among other things, the erosion of fiscal disciplines following an expansionary fiscal policy implemented after the coffee boom of 1977-78 and severe external shocks (oil shocks). During this period, the ratio of public expenditure to GDP increased from 24 per cent in 1973-74 to over 31 per cent in 1979-80 while the deficit increased from 3 per cent to 10 per cent of GDP. Kenya's problems were typical with those of other developing countries. For instance, when the economy was growing fast, it was possible

[11] Ibid p.33
[12] GoK, *Kenya National Development Plan 1997-2000*,Ministry of Planning and National Development p1
[13] GoK, *Kenya National Development Plan 2002-2008*,Ministry of Planning and National Development p6

for the government to fund new priorities while retaining the old ones but once growth stagnated and donor funding petered out, resource allocation became fixed and priorities failed to change in line with circumstances.[14]

Once foreign aid has been received, its role in economic development becomes extremely controversial. Thus some schools argue that foreign aid is indispensable in economic development of poor countries while the other group emphasizes that foreign aid abstracts economic development in poor countries. Thus with the continued debates on donor conditionalities and with the IMF denying that it had improved conditions on aid resumption to Kenya, it is difficult to see Kenya registering an economic growth.[15]

The basic factors that need to be adjusted are structures of production and consumption, science and technology, management, ownership, distribution and marketing channels. In order to do this, one requires the participation of the visible hand of government rather that the invisible hand of market forces. If you insist that market forces become the dominant feature in an improvement and modernisation of these structures it will definitely lead to increased trade liberalisation. That is very dangerous since if it takes such a direction, it means that anybody will be allowed to import anything he or she likes into the country as imports will be all those things bought by the scarce dollars. This will lead to more economic difficulties and I can compromise with the IMF on other things but not on this one.[16]

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[14] Government of Kenya, (2000) *Second Report on Poverty*, Ministry of Finance and Planning
[15] Ibid
[16] Yoweri K Museveni: *What is Africa's problem?* (Kampala. NRM Publication 1992) p.175

The problem is whether policy interventions by the World Bank and IMF since the 1980s have been sustainable. This problem arises from the fear that the neo-liberal paradigm casts the IMF and World Bank in the role of advocates of free economy, and hence they are unlikely to induce policies that are genuine. The key research question for this study therefore is: Why is it a challenge to implement the IMF and World Bank conditionalities in Kenya?

Purpose of the Study

Since independence, Kenya has continued to rely on foreign aid from the donor countries. Foreign aid to Kenya exists in either private or foreign sources. Private capital can either be direct or indirect sources of investment. Direct investment refers to a situation where the investing countries or company controls all the asset liabilities that have been generated. Indirect investment is where the investing capital allows for some share holding from locals, which is normally the minority. Foreign aid can be received from the following sources: -

a. Bilateral hard cash, which is between governments and is given in cash.
b. Bilateral soft loans (grants), which is also between governments but comes either through project assistance or food gains. It can also incorporate personnel with some skills in implementation of projects agreed.
c. Multi-lateral sources, which include agencies, like UNDP. The loans secured through multi-lateral sources are normally for research and development with a view to making recommendations to development plans or priorities.

It is difficult to quantify the sacrifice ratio involved in meeting conditionalities such as retrenchment and expenditure cuts by the government of Kenya. In Kenya, civil service and parastatal sector reforms have led to unemployment and increasing poverty, as the economy is unable to create jobs and redeploy the retrenched labour force. It is sad that Kenya is unfairly grouped with countries that are referred to as 'reluctant adjusters' or 'mixed reforms' yet the government set in motion implementation of fundamental policy changes that have been designed elsewhere. Some of these conditions were not necessarily negative, but there was need to rethink on how, when and where they were imposed. It therefore follows that the government of Kenya should be allowed to identify its priorities itself and have careful consideration in implementing, as implications seem to be far reaching than what meets the eye. Some of the donor conditionalities include reduction of the civil service, privatization of state enterprises, economic liberalization, reduction of corruption and introduction of political pluralism and democratization.[17]

The purpose of the study is to analyse the challenges of implementing economic reform programmes in developing countries and show the implications of the IMF policies on Kenya from 1983-2005.

Objectives of the Study

The primary objectives of this study is to analyse the challenges of implementing IMF economic reform programmes and clearly show

a. The causes and nature of the reform programmes

b. The rationale of IMF in providing aid to Kenya

[17] Government of Kenya (1998) *First Report on Poverty*, Ministry of Finance and Planning

c. The impact of the challenges of donor conditionalities on Kenya

d. The opportunities created by the reform programmes to strengthen Kenya 's economy

Justification of the Study

Investments and interests in Kenya have taken a heavy toll on the citizens as a whole. The study seeks to critically examine the facts and find out whether conditionalities benefit the populace or have a negative impact in other areas. Notably, the role of Bretton Woods institutions in Kenya's policy process has received very little attention. Analysts of Kenya's political economy and public policy process such as Anyang' Nyong'o, Joel D Barkan and Raphael Kaplinski tend to ignore international lending institutions.

In addition the scanty literature on the impact of the donor induced policies were done mainly by none Kenyans and in some cases by and for the donors. For example in 1997 two non-Kenyans, Michio Watanabe and Motoki Takahashi did a study and prepared a paper entitled, *Effectiveness of Donor Aid in Kenya's Health Sector.* Thus the introduction of macroeconomic reform measures, including user fees in the late 1980's as a way to improve allocation, adversely affected the access and affordability of government health services to the poor.[18]

On the other hand, if the IMF plans were followed in spirit by the government of Kenya, the long-term prospects for Kenya would improve. However one has to question the

[18] George Saitoti: *The Challenges of Economic and Institutional Reforms in Africa* (Aldershot, Ashgate 2002) p.212

efficiency of the IMF reforms if the government is still corrupt from the top to down. In Kenya, domestic borrowing has two major impacts: crowding out the private sector; and secondly bidding up interest rates, a disincentive to investment. Between 1996 and May 1997, real interest rates on the 91 day treasury bills and overdrafts by commercial banks averaged 13.5 per cent and 21.2 per cent respectively thus making the cost of capital relatively high. It was hoped that these rates would decline with the improvement of the government's fiscal position. About 72 per cent of Kenya's debt is the balance in domestic debt of short maturity.[19]

It is hoped that this study will be useful in closing the literature gaps on the implementation of economic reforms particularly with regard to the conditionalities imposed by the Bretton Woods institution on Kenya.. The findings of this study will also provide a basis for making recommendations on how to identify policy gaps and suggest remedial measures on how to implement responsible management to enhance economic development.

Literature Review

Successive policies of the government have been aimed towards improving the standard of living of its people. This aspiration has been reflected in various Government documents such as Sessional papers, Development plans, Policy Framework papers, the Poverty Reduction Strategy Paper (PRSP) and lately, the Economic Recovery Strategy for Wealth and Employment Creation. The Sessional Paper No. 10 of 1965 on "African

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[19] Government of Kenya, (2000) *Second Report on Poverty*, Ministry of Finance and Planning, op.cit

Socialism and its Application to planning in Kenya" was among the first Government policy documents on the vision and the needs of the Kenyan people.[20] The paper recognized the elimination of poverty, ignorance and disease as key priorities. Consequently, the country's major development objectives have been founded on the principles of reducing poverty through achieving high and growing incomes that are equitably distributed among Kenyans.

In order to achieve these objectives, the country needed to grow at an annual rate of 7 per cent sustained over a period of at least ten years. Other subsequent policy documents such as the Sessional Paper No. 1 of 1986 on "Economic Management for Renewed Growth",[21] Sessional Papers on "Economic Recovery and Sustainable Development to the year 2010"[22] and "Industrial Transformation by the year 2020" emphasizes more or less on the same principles of tackling the country's economic objectives.[23] From traditional quantitative measures of poverty, as used in the first and second reports on poverty in Kenya, the overall poverty line has been calculated by summing the food expenditure level.[24]

During the first sixteen years of independence, the country's rate of annual economic growth averaged 6.1 percent. The next sixteen years saw the average rate of growth fall

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[20] Government of Kenya, (1965), Sessional paper No.10 of 1965 on *African Socialism and its Application to Planning in Kenya.*
[21] Government of Kenya (1986) Sessional Paper No.1 of 1986 on *Economic Management of Renewed Growth,* Ministry of Finance and Planning
[22] Government of Kenya (2000) *Second Report on Poverty in Kenya* Ministry of Finance and Planning, Nairobi, op.cit
[23] Sessional Paper No 1 of 1986, op.cit
[24] Government of Kenya (1998) *First Report on Poverty in Kenya* Ministry of Finance and Planning, Nairobi, op.cit

to 3.4 per cent. The rate of growth since 1995 has fallen to 1.4 per cent. The government has consulted and collaborated with development partners, to address the decline in economic growth with little success.[25] From December 2002, the NARC Government put in motion a bold initiative towards poverty alleviation and economic development through the "Economic Recovery Strategy for Wealth and Employment Creation (2003-2007)." It identifies key policy measures and programmes that the government is committed to pursue over a period of five years starting from 2003. When implemented, the measures are expected to create the necessary conditions for achieving the desired economic growth, wealth, employment and reduced poverty in the Kenyan society.[26]

By mid 1970's many third world countries were heavily in debt. In 1977 the IMF set up an emergency fund.[27] Since mid-1983, the government of Kenya has made progress in tackling corruption and improving governance, and the IMF has acted as an advisor in the area of governance drawing from the experience of its membership. To bolster progress in this key area of reform, the IMF programme has included two structural benchmarks, the first pertaining to a bill including an ethics code for public officials and the second to an Anti-Corruption and Economic Crimes bill.[28] These are important elements in an IMF programme, and reflect the institution's concern with improving governance, of which the beneficiary is meant to be Kenya's population at large. However, as with many other IMF programmes, the Kenyan one requires that legislation be enacted in parliament so as to legalise some of these conditionalities set by the IMF.

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[25] Mule H., D. Ndii and C. Opon, (2003)
[26] Government of Kenya (2003) *Participatory impact Monitoring Ministry of Planning and National Development*/ GTZ Social Policy Advisory Services, Nairobi, Kenya.
[27] Norman Lowe: *Mastering Modern World History*, (London, Macmillan,1997) p.177
[28] Kenya enacts Graft bursting Law; *Mail and Guardian*, 17 April 2003

Several features of the Kenyan programme are similar to those found in other IMF-supported programs. Provision of daily balance-sheet information is required to the Kenyan program. Likewise, the release of funds in bunches after periodic reviews are a standard feature of IMF programmes. Kenya's programme is distinguished by an unusually long list of conditions attached to the loan. And, in any event, the majority of these conditionalities pertain to one of the IMF's core areas of responsibility, namely fiscal reforms. However, many other issues also seem relevant to the issues that its programmes seek to address. A challenge for the IMF in future is to retain a sound financial and economic basis for its operations while also responding to relevant social and political issues. In addition, as a member-based organization, the IMF only has relevance and utility if member countries view it as an institution whose policy advice is appropriate and worth implementing.[29]

Many borrower countries believe that IMF policies are too narrow and lack sufficient appreciation for the real needs and the limits of their political and economic situations. As developing countries are the primary recipients of IMF assistance and policy advice, divergence between lenders and creditors has grown, with protests against the IMF in general and specific IMF programmes.[30] A sizeable number of the public in both the developed and developing countries have strong negative views of IMF. This tends to encourage and hinder the process of reform by intensifying, polarizing and complicating

[29] Joel D Barkan: *Beyond Capitalism vs Socialism in Kenya and Tanzania* , (Nairobi, EAEP, 1995) p.39
[30] Ibid p.2

public and official discussion of these issues. Fundamentally, the IMF is an economic and financial institution.

Politicians and scholars both inside and outside IMF are currently debating whether the policy tools and methods used by IMF are appropriate for current world conditions. As yet, no consensus has developed for an alternative model, which is likely to be more effective in promoting stabilization and development in poor countries. At least, no alternatives have been proposed that do not require some type of long-term budget support and subsidies from richer countries. Few developed countries seem willing to make long-term unrestricted financial transfers of this sort.[31] In the meantime, controversy and debate about IMF's basic principles and its scope of operations will remain an ongoing concern to developing countries like Kenya.

Success in economic and development growth depends on the policies that a country has adopted and institutional framework put in place to implement those policies. Thus after evaluating the growth of Kenya's economy that is agro – based and given that the arable agricultural land has continued to shrink the need to diversify and industrialize was hatched by the government of Kenya. It was expected that the country would join the newly industrialized countries by 2020.[32] The base for take off was expected to be the large manufacturing and industrial sectors whose gross domestic product (GDP) has been on slight increase.

[31] Christopher Clapham: *Africa and the International System* (Cambridge, University of Cambridge,1998) p. 94

[32] Government of Kenya, Sessional Paper No 2 of 1996 on Industrial Transformation to the year 2020 p.87

On the same vein, USAID undertook to finance healthcare in Kenya in August 1989, on two conditions. First, the government was to introduce user charge fees for all outpatient and inpatient services in public health facilities, except dispensaries. Secondly, the National Hospital Insurance Fund (NHIF) was to be reformed. The two conditions were implemented in December 1989 and July 1990 respectively. To enhance revenue collection and improve services quality, each health facility was to retain 75 per cent of revenue generated through user charges. The remaining 25 per cent was to be allocated by the respective health management boards. The policy provided for free family planning, maternity, child health care services and payment waivers for those who could not afford the fees. It was hoped that once the health institutions were able to generate sufficient revenue from user charges, they would not need funding from the Ministry of Health. However, the policy was not without pitfalls. First, different health institutions inconsistently applied user charges. Secondly, the waiver system was corruptly administered. Thirdly, there was a drastic attendance decline in health institutions charging the fee. [33]

The declining economic growth and increased social and regional inequalities, led to a revision of economic and rural development policies in the 1970s. The implementation of the policy raised public outcry, forcing the government to halt user charges in August 1990. However, this step was taken without consulting the World Bank and USAID who were threatened to stop supporting the health sector reforms. The government had to reconcile public demand for improved health services, with donor pressure for expenditure reduction. Obviously the pressure for expenditure reduction was driven by

[33] George Saitoti op.cit pp.213-214

the need for Kenya to raise surplus to repay outstanding debt. This confirms the hypothesis that donor interests rather than the interest of recipients motivate donor aid.[34]

From the early 1980s, Kenya, faced severe economic crisis, characterized by balance of payment, high inflation, slow economic growth and unemployment. Infact, its GDP growth slowed from 6.7 per cent in 1978 to 3.1 per cent in 1979. These macroeconomic problems were attributed to her weak policy and institutional framework for economic growth. To redress this, Kenya accommodated the Bretton Woods-fronted Structural Adjustment Programmes (SAPs). The term *Structural Adjustment* was coined by the then World Bank president, Robert McNamara during the bank's board of governors meeting in Belgrade in October 1979. Its goal was to reduce spending and direct economic involvement by the state, move towards market allocation of resources and provide an enabling environment for private enterprise.[35]

SAPs had four major policy prescriptions. First, for macroeconomic stability, Kenya was required to control budget deficit, liberalize foreign exchange, and devalue currency. Secondly, state monopoly over purchase of agricultural produce was to be eradicated and private enterprises allowed to compete for better producer prices, while money guzzling, loss-ridden parastals were to be privatized. Thirdly, SAPs called for price deregulation and recommended that consumers should meet at least part of the cost of social services like education and health, previously provided freely by the state. Lastly, SAPs proposed public expenditure and budget deficit reduction through balanced budgeting and civil

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[34] George Saitoti op.cit pp.219-220

[35] Rolph van der Hoeven and Fred van der Kraaij, *Structural Adjustment and Beyond* (London, Heinemann 1994) p.4

service reform. It was to replace traditional mechanisms of financing budgets like borrowing or increasing money supply. In any case, domestic credit crowds out investment, external credit exacerbate debt crisis, while increased money supply breed inflation.[36]

Despite implementation of SAP policies, Third World debt rose from US$650 billion in 1980 to US$ 15,000 billion in 1992. Infact "the level of debt for many countries has become so high that a large slice of government budget and an even larger portion of foreign exchange must go into servicing debts rather than into urgent economic initiatives and welfare projects".[37] Kenya's initial resistance to SAPs was softened by the fact that the much needed donor funding was to be pegged on the adoption of the reforms. Around the same time, the East, Central and Southern Africa countries passed the *Gaborane Declaration of 1984,* which dedicated the decade 1985-1995 to co-operative development in the region. As a result, Kenya embraced SAPs, and incorporated it into the *Sessional Paper No.1 of 1986 on Economic Management for Renewed Growth.*

Turner and Hulme (1997) noted that during the cold war era, foreign aid greatly influenced domestic policy-making in Africa. Donors focused almost exclusively on disbursing aid through public projects. This practice diverted policy-makers from policy formulation to implementation, and monitoring of specific projects. It was in this context

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[36] Ibid p.26

[37] Mark M Turner, David Hulme and David Hulmes, D. *Governance, Administration and Development: Making the State Work* (New Delhi Kumarian Press, 1997) p.31

that the World Bank initiated the Integrated Agricultural Development Project (IADP) in 1976 to assist subsistence farmers to join the cash economy. During the 1980/81 fiscal year, the Bank gave Ksh 9.4 million to 13 co-operative societies to support cash crop development. Similarly, the Bank in collaboration with the Commonwealth Development Corporation (CDC) initiated the Smallholder Coffee Improvement Project (SCIP), which provided funds to farmers for the rehabilitation and improvement of coffee processing factories. During 1980/81 fiscal year, a total of Kshs. 28 million was loaned to 76 coffee factories, while another Kshs. 6.8 million was loaned to small- scale farmers. DANIDA also helped to set up the Farm Input Supply Scheme (FISS) in 1976 to support weak unions create input merchandise stores and grant credit to farmers through co-operatives. By 1980, about Kshs. 41 million had been loaned to some 107 co-operatives.[38]

Theoretical Framework

The contemporary relationship between the North and South is best described as one of asymmetric interdependence.[39] The developing countries can be found in Africa, Latin America, Asia and the Middle East. The problems facing them are in many ways more difficult than during the struggle for independence. This is essentially so because the third world is not dealing with one common external enemy; but because of vested interests both local and foreign. The developing countries should have a strategy for development, reduction of unequal access to productivity such as land, and provision of basic needs such as education, health, food and water. These strategies should go beyond simply increasing economic growth to the existing social, economic, political and cultural

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[38] Fassil G Kiros: *Challenging Rural Poverty: Experience in Institutional Building and Popular Participation for Rural development in East Afric*a (New Jersey Africa World Publishers) p.18

[39] Steven L Spiegel: *World Politics in a New Era*, , (Orlando, Harcourt Brace 1985). p.236

environment which has remained the basis for the argument on economic development by the North for a long time.[40]

Unfortunately for most third world countries, their argument has been centered on the reception of handout from the developed nations. This made third world economies to be forced to liberalise by the developed economies. Liberalism is an ideology, philosophical view, and political tradition which holds that liberty is the primary political value. Broadly speaking, liberalism seeks a society characterized by freedom of thought for individuals especially of government and religion, the rule of law, the free exchange of ideas, a market economy that supports relatively free private enterprise, and a transparent system of government in which the rights of minorities are guaranteed. In modern society, liberals favour a liberal democracy with open and fair elections, where all citizens have equal rights by law and an equal opportunity to succeed in whatever development project an individual undertakes. In the context of economics, the term "liberalism" refers to economic liberalism, which is associated with the political ideology of liberalism itself.[41]

The word "liberal" is derived from the Latin *liber* ("free"), from which the term "liberty" also comes. Largely dormant during the Middle Ages, the struggle for freedom began again during the Italian Renaissance, in the conflict between the supporters of free city states and the supporters of the Pope as the head of the Church. Nicolo Machiavelli, in his *Discourses on Livy*, laid down the principles of republican government. John Locke in

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[40] P Mosley and L Smith, *Structural Adjustment and Agricultural Performance in sub-Sahara Africa 1980-1987,* Journal of International Development Vol 3 pp.321-325
[41] Ken Booth and Steve Smith: *International Relations Theory Today*, (Cambridge, Polity Pree,1997) p.171

England and the thinkers of the French Enlightenment articulated the struggle for freedom in terms of the Rights of Man. All these were meant to guarantee and favour liberal democracy[42]

For the purposes of this paper, I will use "political liberalism" for the support of democracy; "cultural liberalism" for the support of individual liberty over laws limiting liberty for patriotic or religious reasons; "economic liberalism" for the support of private property, over government regulation; and "social liberalism" for the support of equality, and over inequalities of opportunity. Modern liberalism has a mixture of these forms and the principles that liberals generally agree upon are political, cultural, economic and social liberalism.[43]

Political liberalism is the belief that individuals are the basis of law and society. It also emphasizes that the society and its institutions exist to further the ends of individuals, without showing favour to those of higher social rank. Political liberalism stresses the social contract, under which citizens make the laws and agree to abide by those laws. It is based on the belief that individuals know what is best for them. Political liberalism enfranchises all adult citizens regardless of sex, race, or economic status. Political liberalism emphasizes the rule of law and supports liberal democracy[44].

Cultural liberalism focuses on the rights of individuals pertaining to conscience and lifestyle, including such issues as sexual freedom, religious freedom, cognitive freedom, and protection from government intrusion into private life. John Stuart Mill aptly

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[42] Robert Gilpin: *The Political Economy of International Relations*, (New Jersey, Princeton 1987) p. 11
[43] Ibid p.14
[44] Robert Gilpin op cit p.13

expressed cultural liberalism in his essay "On Liberty" and hence cultural liberalism generally opposes government regulation of any controls.[45]

Economic liberalism is an ideology which supports the individual rights of property and freedom of contract. The watchword of this form of liberalism is "free enterprise". It advocates laissez-faire capitalism, meaning the removal of legal barriers to trade and cessation of government-bestowed privilege such as subsidy and monopoly. Economic liberals want little or no government regulation of the market. Some economic liberals would accept government restrictions of monopolies and cartels. Others argue that monopolies and cartels are caused by state action. Economic liberalism holds that the value of goods and services should be set by the unfettered choices of individuals, that is, of market forces.[46]

Social liberalism, also known as new liberalism (not to be confused with 'neo-liberalism') and reform liberalism, arose in the late 19th century in many developed countries, and was influenced by the utilitarianism of Jeremy Bentham and John Stuart Mill. As explained by John Dewey and Mortimer Adler, in social liberalism, individuals are the basis of society; all individuals should have access to basic necessities of fulfillment, such as education, economic opportunity, and protection from harmful macro-events beyond their control. To social liberals, these benefits are rights.[47]

In all these forms of liberalism there is a general belief that there should be a balance between government and private responsibilities, and that the government should be

[45] Robert Gilpin op. cit p.13
[46] Robert Gilpin op.cit p.12
[47] Robert Gilpin op cit p.13

limited to those tasks which cannot be carried out best by the private sector. All forms of liberalism claim to protect the fundamental dignity and autonomy of the individual under law; all claim that freedom of individual action promotes the best society.[48] Liberalism is so widespread in the modern world that most nations at least pay lip service to individual liberty as the basis for society. A main contributing group of thinkers whose work would become considered part of liberalism are those associated with the "Scottish Enlightenment", including the writers David Hume and Adam Smith, and the German enlightenment philosopher Immanuel Kant.[49]

The impact of liberalism in the modern world is profound. The ideas of individual liberties, personal dignity, free expression, religious tolerance, private property, universal human rights, transparency of government, limitations on government power, popular sovereignty, national self-determination, privacy, enlightened and rational policy, the rule of law, fundamental equality, a free market of economy, and free trade were all radical notions some two hundred and fifty years ago. Economic liberals today stress the importance of a free market and free trade, and seek to limit government intervention in both the domestic economy and foreign trade. [50]

Modern liberal movements often agree in principle with the idea of free trade, but maintain some skepticism, seeing unrestricted trade as leading to the growth of multi-national corporations (MNCs) and the concentration of wealth and power in the hands of the few who are more privileged. Liberals agree that a high quality of health care and education should be available for all citizens, but differ in their views on the degree to

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[48] S P Varma: *Modern Political Theory* (New Delhi, Vikas Publishing house, 2003) p. 84
[49] Robert Gilpin op. cit p. 12
[50] Robert Gilpin op .cit p.15

which governments should supply these benefits. Since poverty is a threat to personal liberty, liberalism seeks a balance between individual responsibility and community responsibility. In particular, liberals favour special protection for the handicapped, the sick, the disabled, and the aged all over the world.[51]

Liberalism turned back to more laissez-faire policies in the 1980's and 1990's, and supported privitisation and liberalisation in health care and public sectors. The liberal consensus appears to involve a belief that economies should be decentralized. In general, contemporary liberals do not believe that the governments should directly control any industrial production through state owned enterprises.[52] The IMF and the World Bank enforce this new arrangement through conditioned reforms in the developing world. It is in this context that the IMF and the World Bank introduced SAPs aimed at reducing public expenditure, raise budget surplus and facilitate loan repayment to the West.

What then emerges is a theoretical debate that has gone full circle between state-led and market-led economic development. The IMF and the World Bank lending terms are designed within the context of neo-liberalism, and therefore seek to push the state away from the arena of development. However, the resultant free market is not a panacea since it has adverse effects on the welfare of the vulnerable groups in the society. Under neo-liberalism therefore, it is only institutions like co-operatives that can fill the void created by the state, and intervene to cushion poor co-operator from adverse effects of free and unrestricted competition through subsidies and other forms of support for the cooperators.

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[51] Tony Cleaver, *Understanding The World Economy* (London , Routledge,2001) p.9
[52] Ibid p.95

The foregoing discussion raises a paradox. On the one hand, the World Bank and IMF are cast in the role of neo-liberal institutions that support and protect free market The fundamental question, which constitutes our entry point in this theoretical debate therefore, is: - To *what extent can the same free-market inclined agents of neo-liberalism, like the IMF and the World Bank, include policies in the developing world which strengthen local organizations like co-operatives whose mission is to intervene in the operations of a free market economy?*

The key assumptions drawn from the theory to guide this study are:-

a. State has different interests and different degrees of autonomy with respect to policy-making. Some are weak and hence less autonomous and perpetually loose out to the interests of domestic non-state actors and the external actors.

b. In the struggle for supremacy over the policy process, all the actors are rational, opportunity maximizers and self-interest driven. It is often the narrow interests of the actors and not public interest that dominates the process.

Hypothesis

The IMF's mandate has not changed over the last sixty years. Their chief goal remains promoting global financial stability and thereby laying the groundwork for sustained growth. What has changed is the approach to achieving this goal, which has been significantly and continuously adapted in response to global developments. The breakdown of the Bretton Woods system, the emergence of Africa as a continent of independent nations, the oil shocks of the 1970s and the collapse of communism in the

former Soviet Union (SU) have all brought different economic challenges to the third world countries. [53] Most recently, the IMF has been grappling with the growth in size and sophistication of International Capital Market. We may therefore draw the following hypotheses:

a. Kenya needs to implement the economic reform conditions so as to enhance its economic development.
b. The implementation of IMF economic reform programmes may not enhance economic development in Kenya.
c. Kenya should look for other avenues for development other than depending on IMF.

Research Methodology and Data Collection

The thesis will utilize primary and secondary sources of data. People who have worked in the Ministries of Finance and Planning and National Development will be interviewed. On the other hand, the IMF and World Bank representatives working in Kenya may also be interviewed so as to enrich this paper. Meanwhile, the research methodology and data collection will involve:

a. Primary Sources. Interviews on researchers, professionals, practitioners, representatives of international organizations such as the IMF and the World Bank officials working in Kenya.
b. Secondary Sources: Written materials from books, reports, papers, research papers and journals.

Musalia Mudavadi, *Rethinking Development in Africa in the 21st Century* (Nairobi EAEP 2002) p.17

Brief Outline of the Proposal Thesis

CHAPTER 1: Framework of the Study

Introduction; Background to the Problem; Problem Statement; Purpose of the Study; Objectives of the Study; Justification of the Study; Literature Review; Theoretical Framework; Hypothesis; Research Methodology, Chapter Outline

CHAPTER 2: The Kenyan Economy in Perspective

Introduction; Post Independence Period (1963-1974); The period of Economic Decline (1974-1990); Lack of Economic Growth (1990-2002); Structural Weaknesses in Kenya

CHAPTER 3: Foreign Aid and its Impact in Kenya

Introduction; **Foreign Direct Investment**; The role of Agriculture in Kenya development; Food Crisis in Kenya; Ways of managing Food crisis in Kenya; Lack of subsidy in Agriculture; Industrialisation in Kenya; MNCs and the Culture of Consumerism; Debt crisis in the South; Solutions to Debt crisis; **Structural Adjustment Programmes (SAPs);** Reduction of Government Spending; Liberalisation of Markets; Export promotion; Privatisation of public sector Utilities; **IMF Policies;** Liberal Economic Reforms; Capitalist Economic Globalisation; Problems with Economic Globalisation in Kenya; Global Political Transformation

CHAPTER 4: Implementation of IMF programmes in Kenya and its Impact

Introduction; Implementing reform measures; Economic recovery through good governance; Dealing with the past; Asset Recovery; The Kenyan Experience; The Goldenberg affair; Loss of Political will; Adoption of Legislative measures to combat corruption; Transparency and accountability in the management of public affairs; Administrative reforms and codes of good practice; Public participation and accountability; Legislation on lending and borrowing in Kenya; MTEF Budgetary Process in Kenya.

CHAPTER 5: Conclusion and Recommendations

Conclusion; **Recommendations;** Implementation of Monetary and Fiscal Policies; Foreign Trade in Economic Development; Developing the Manufacturing and Industrial Sectors; The labour market; The capital market; Fiscal policy and public expenditure; Infrastructure Development; Quality controls and enforcement of standards.

CHAPTER TWO

THE KENYAN ECONOMY IN PERSPECTIVE

Introduction

Kenya's first policy objectives were produced and are documented in Sessional Paper No. 1 of 1963 entitled Observations on the Report of an Economic Survey Mission from the International Bank for Reconstruction and Development, which came out shortly after independence on 12 December 1963.[54] The International Bank for Reconstruction and Development, (IBRD) was later to be known as the World Bank. The main policy objectives were to fight poverty, ignorance and disease. More than four decades later, Kenya has not achieved these objectives. Among the three, poverty if reduced substantially will have some bearing towards the fight on the other two. According to the Welfare Monitoring Survey III conducted in 1997, more than half of Kenya's population lives in abject poverty, earning less than a dollar per person per day.[55]

Post Independence Period (1963-1974)

After independence, Kenya promoted rapid economic growth through public investment, encouragement of smallholder agricultural production and incentives for private (often foreign) industrial investment. Gross domestic product (GDP) grew at an annual average of 6.6 per cent from the 1963 to 1973. Agricultural production grew by 4.7 per cent annually during the same period, stimulated by redistributing estates, diffusing new crop

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[54] Government of Kenya (1963) Sessional Paper No.1 of 1963 *on Observations on the Report of an Economic Survey Mission from the International Bank for Reconstruction and Development.*
[55] Central Bureau of Statistics (1997), Welfare *Monitoring Survey III*, Ministry of Finance and Planning(Nairobi 1997) p. 16

strains and opening new areas to cultivate.[56] The Sessional Paper No. 10 of 1965 on "African Socialism and its Application to planning in Kenya" was among the first of the Government's policy documents on the vision and the needs of the Kenyan people.[57] The paper recognized the elimination of poverty, ignorance and disease as some of the key priorities. Consequently, the country's major development objectives have been founded on the principles of reducing poverty through achieving high and growing incomes that are equitably distributed among Kenyans.

During the early years after independence, Kenya financed most of its investments from domestic saving. For instance in 1964 domestic savings were 18 per cent of the gross domestic product while the gross ratio was 14 per cent reflecting a surplus in the external current account. By the end of 1980 the domestic savings ratio was 17 per cent while investment was about 25 per cent. The financing gap was largely as a result of the ambitious investment programme that the country undertook during the period.[58] The value of output can be measured by its cost which is equal to the total value of inputs in the productive process. According to the classification scheme employed in the United Nations system of national accounts, the cost of gross domestic product is divided compensation of employees, consumption if fixed capital, indirect taxes less subsidies and operating surplus.[59]

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[56] Ibid p.17

[57] Government of Kenya (1965) Sessional paper No.10 of 1965 on ***African Socialism and its Application to Planning in Kenya*** op.cit

[58] Central Bank of Kenya (1991) Kenya Land Of Opportunity op.cit p. 68

[59] United Nations (1968) A System of National Accounts, New York p.19

Despite the impressive performance of Kenya's economy since independence, various structural weaknesses have been evident in the macro economic framework. In recognition to this, the government of Kenya began to implement structural policy reforms in the mid-1980's with the launching of the Sessional Paper No1 of 1986.[60] Among these were trade liberalisation, reduction in tariffs, deregulation of prices and interest rates, simplification of investment approval procedures, reforms of foreign investment protection legislation, establishment of the manufacturing under bond (MUB), export processing zone facilities and liberalisation of marketing procedures and improvements in the payments systems for the major agricultural crops. [61]

The Period of Economic Decline (1974-1990)

Between 1974 and 1990, Kenya's economic performance declined. Inappropriate agricultural policies, in adequate credit and poor international terms to trade contributed to the decline in agriculture. Kenya's inward–looking policy of import substitution and rising world oil prices made Kenya's manufacturing sector uncompetitive. The government began a massive intrusion in the private sector by creating many parastatals with a view to enhance its economic growth to no avail. This happened due to lack of export incentives, tight import controls and foreign exchange controls which made the domestic environment for investment even less attractive.

The argument above can be summarized by the fact that valuation changes are a potential source of apparent economic growth rather than real differences between the changes in

[60] Central Bank of Kenya (1991) Kenya Land of Opportunity op.cit p. 69
[61] Joel D Barkan and John I Okumu, *Politics and Public Policies in Kenya and Tanzania*, (New York Prager, 1984) p.4

net foreign assets as recorded in the balance of payments and the corresponding stocks of net foreign assets in the monetary survey. For example, a revaluation of foreign assets due to exchange rate changes or a change in the valuation of monetary gold will change the value of net foreign assets of the monetary authorities in the monetary survey with a corresponding change being entered in other items.[62] In Kenya, the early 1980s were characterized by high budget deficits, high inflation and unattainable current account deficits. These financial imbalances were triggered by among other things the erosion of fiscal disciplines following an expansionary fiscal policy implemented after the coffee boom of 1977-78 and several external shocks (oil shocks). During this period, the ratio of public expenditures to GDP increased from 24 per cent in 1973-74 to over 31 per cent in 1979-80 while the deficit increased from 3 per cent to 10 per cent of the GDP.[63]

Kenya's problems are typical. When the economy was growing fast, it was possible for the government to fund new priorities while retaining the old ones but once growth stagnated and donor funding petered out, resource allocation became fixed and priorities failed to change in line with circumstances. The high deficits were financed by a combination of domestic and foreign borrowing. By 1981 debt to GDP ratio stood at 13.2 per cent, up from 4 per cent in 1977. Clearly this trend of expenditure was not sustainable and in 1982 Kenya had to turn to the IMF for a Structural Adjustment Loan (SAL). However, the policy changes stipulated in the lending arrangement were not backed by

[62] International Monetary Fund (1977) Balance of Payment Manual p.152
[63] Ibid p. 153

true commitment to change and lack of compliance led to failure. Kenya received nineteen structural adjustment loans during the reform period.[64]

In Kenya twenty years of reforms have not achieved the expected results. The macroeconomic environment has not created the conditions necessary to achieve sustained growth at the levels that had been attained in the 1970s and 1980s. Though some reforms like market liberalization have been successfully implemented, other critical structural and institutional reforms are yet to be finalized. The failure to achieve institutional reforms has resulted in a reduction of donor inflows to finance the government budget. This includes uncertainty in the economy and a reluctance to invest in the sector, thus a declining trend in private investment observed in the economy.[65]

The aid conditionality arrangements pertaining to maize market reforms commenced in the late 1980s with the Agricultural Sector Adjustment Operation of the World Bank and the central sector reform programme of the European Union (EU). The reform programme was marked by increased political interference in the decisions of key co-operative and joint-venture market organizations. Thus in the maize sector, the state owned marketing board National Cereals and Produce Board (NCPB) has continued to support maize prices in certain areas[66].

On the other hand, the oil crisis and the rise in international interest rates in the 1980s, Kenya like other developing countries was not in a position to service its debt and turned

[64] International Monetary Fund (1977) op.cit p.154
[65] Musalia Mudavadi op. cit p.19
[66] Musalia Mudavadi, op.cit p. 47

to Bretton Woods institutions to be bailed out. Assistance was conditional on implementing Structural Adjustment Programmes (SAPs). This meant that Kenya was to undertake ambitious programmes on market liberalization, privatsation, currency devaluation and reduction of public expenditure all of which worsened poverty. In line with Sessional Paper No. 1 of 1986 on economic management for renewed growth, the government strived to increase domestic savings in order to reduce external indebtedness. To this end interest rates were decontrolled in July 1991 to supplement other policies and incentives to promote domestic savings.[67]

The implementation of SAPs saw a significant reduction in the deficits incurred in early 1990s. After a period of chronic deficits reaching unprecedented level of 9.65 per cent of GDP in 1992-93 the fiscal deficits gradually declined to 0.25 per cent of GDP in 1996-97. The reduction was achieved through cuts in public investment and the provision for operations and maintenance. Through the introduction of cost sharing in the education and health, the government also reduced its involvement in the provision of the basic services in the related sectors.[68] Due to budgetary constraints the government recognized that it could not continue to absorb the labour force at the same rate as it did in the first two decades after independence. Since the early 1980's the government has been implementing structural adjustment policies, which were intended to stimulate agriculture and industry, thereby generating employment opportunities in these sectors.[69]

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[67] Government of Kenya (1986) Sessional paper No.1 of 1986 *on Economic Management for Renewed Growth,* op.cit

[68] Musalia Mudavadi op. cit pp.3-4
[69] Central Bank of Kenya (1991) Kenya Land of Opportunity op. cit p.72

Lack of Economic Growth (1990-2002)

The government's strategy in the 1990's was aimed at maintaining a stable macro-economic environment coupled with carefully designed sector programmes to deepen structural adjustments and enhance production in both agricultural and industrial sectors. This was meant to provide a favourable macro-economic environment to facilitate private sector activities in order to achieve and sustain non-inflating growth that is higher than the population growth rate.

As a result, public infrastructure has been decaying and has witnessed little expansion. Both health and education standards have been declining, consistent with high poverty levels and the posture trends achieved in its first decade after independence have reversed. The Structural Adjustment Programme was characterized by high demand management and this seems to have compromised investment and growth and it would appear that the fiscal contraction was high to be contained by a developing economy such as that of Kenya. It can thus be observed that the implementation of SAPs proved to be beyond the capacity of most third world governments, Kenya included, though it was acknowledged that reforms were needed. At the same time, it must be agreed that even well formulated reform programmes can be thrown overboard by adverse shocks that would be least accommodative. [70]

Kenya was among the first African countries to launch a Structural Adjustment Programme in 1980. Little liberalization of foreign trade took place from 1980 to 1992, and it was for only two years, 1992 to 1994, that little progress could be noted.

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[70] Joel D Barkan and John I Okumu (1984) op.cit p.15

Liberalisation of the financial markets was undertaken in a situation where macroeconomic stability, fiscal discipline and containment of inflation were lacking. Thus, as a result, it failed to make the rate of interest rise to a market-determined level. In the financial year 2004/05 the reforms led to the growth of Kenya's economy to the tune of 4.2 per cent.[71]

Initial strategy advocated for heavy government involvement in the economy as the private sector had limited capacity to stimulate economic growth. In the early years, the economy achieved an annual growth rate of 6.6 per cent until the 1970s.[72] This growth momentum was lost and the economy declined with an average growth rate of 5.2 per cent per annum between 1974 – 1979; 4.1 per cent in 1980 – 1985; 2.5 per cent between 1990-1995 and eventually declined to negative 0.3 in 2000.[73]

From 1991 to 1993, Kenya had its worst economic performance since independence. Growth in GDP stagnated and agricultural production shrank at an annual rate of 3.9 per cent. Inflation reached 100 per cent in August 1993 and the government's budget deficit was over 10 per cent GDP. As a result of these combined problems, bilateral and multilateral donors suspended their programmes on aid to Kenya in 1991. The allocation of resources, both by economic category and by sector, contributed to the poor performance of the public expenditure. During the period 1991/92 to 1999/2000, interest payments and wages and salaries averaged 54 per cent of the total expenditure and 66 per

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[71] Mats Lundhl, *From Crisis to Growth in Africa*,(London Routledge 2001), p.8
[72] *Towards linking Agriculture, Poverty and Policy in Kenya*; Vol. 8, issue No.4, 2002, in http://www.ipar.or.ke/pb4.%2002.pdf
[73] Ibid.

cent of recurrent expenditure. Thus, Kenya is a typical example where fiscal adjustment was an illusion. The success in deficit reduction was a result of reduced spending in operations and maintenance, resulting in a rapid depreciation of public capital stock, and of crowding out new public investment.[74]

Fiscal indiscipline, typified rapid expansion of the public sector and large deficits left most developing countries with huge debt obligations; inadequate evaluation of expenditure implied that the budget carried the burden of past policy budgetary and legislative decisions left little room for manoeuvre. The overwhelming majority of resources must be allocated to existing programmes and projects leaving little or no scope for funding new policies and priorities. Thus since the Kenyan government proved inefficient, public sector wages were low and much public expenditure was absorbed by dead weight administrative costs and the government robbed of resources needed for critical social development.[75]

Several factors have been identified as being responsible for mismanagement of the economy and for the resultant budget deficits over the recent years. Trade deficit resulted from a rise in both import volumes and prices thus much higher value of imports. The trade deficit rose from KSh.83 million in 1999 to KSh.113 million in 2000. Whereas the poor performance of the agricultural sector has been blamed on insufficient rainfall, other factors included poor world commodity prices. Fish quantities harvested declined in

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[74]Towards Linking Agriculture, Poverty and Policy in Kenya op cit

[75]Government of Kenya (2001) Report of the Sector working Group on Physical Infrastructure, Ministry of Finance and Planning p.31

1999 by 1.6 per cent compared to the previous year mainly as a result of the total ban in fishing at Lake Naivasha, which was needed to preserve dwindling stocks.[76]

The prevailing conditions and circumstances limited the range of executive and legislative discretion. Thus the resource allocation process and implementation was flawed as a result of the following:

a. Frequent policy reversals have undermined government credibility.

b. The productivity of investment fell sharply and was estimated at 50 per cent over the last three decades.

c. Both public investment and savings were well below the levels required to generate growth and enhanced the impact on poverty.

d. Kenya achieved a successful record on investment in education and health but these gains were threatened by the lack of private investment through which the social investments would achieve growth and equality divided.

e. The main constraints on poverty reducing growth rate relate to weak governance, corruption in government, poorly coordinated and prioritised government actions.

f. The poor record of fiscal management and the inefficiency of much of the public expenditure have curtailed the scope for effective government investment.

g. Public finance strategies have been characterised by an expansion of short term domestic debt which has crowded out the private sector and increased the

[76] Ibid p. vii

proportion of debt service obligations in the government budget, subsequently, shrinking the proportion available for social expenditure.[77]

Structural Weaknesses in Kenya

Thus Kenya's problems and structural weaknesses have been well analysed and documented in various policy papers dating as far back as the 1990s but the development strategy has not addressed them. It is difficult to improve from the past but the macroeconomic strategy aims at reducing the debt burden through revenues from privatisation, concessional foreign borrowing and a medium term reduction of government share in GDP. Debt clearly emerges as a major pre-occupation in growth and poverty reduction in the medium term.[78]

Coupled with the problem of inadequate political systems in Kenya is the problem of economic underdevelopment. Underdevelopment is in itself not enough to lead to conflict but it is exacerbated by inadequacies of the political systems. In a situation where the economy is insufficient, the resulting competition often leads to politics being ethnic as power becomes the only avenue to state resources. Once in power, the elite mismanage and loot available resources before they are removed by others who also try their turn to "eat" by clamoring for political power. Often the elite try to propagate and maintain their hold on power and its economic benefits by resorting to coercive means.[79]

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[77] GoK (2001) *Report of the Sector Working Group on Physical Infrastructure* op.cit pp.33-37
[78] GoK (2001) *Report of the Sector working Group on Physical Infrastructure*, op.cit p.32
[79] S Burchill, *Theories of International Relations*, (New York, Palgrave 1996) p.50

The liberals' solutions to the above, is a greater push towards democracy. This push is led by actors in the international system; both state and non-state actors. The collapse of the cold war and the resultant push for liberal democracy in Africa, led by the USA being the main proponent and the IMF as well as the World Bank was as a result of liberal thinking. For instance in Kenya, the suspension of aid by the Paris Club in November 1991 led the monolithically Kenya National African Union (KANU government to liberalize the political system by succumbing to multiparty political system. This averted a political head-on collision between the regime and the forces opposed to it.[80]

However, it is doubtful whether this intervention transformed Kenya into a democracy as had been envisaged. In 1992 and 1997 there erupted tribal clashes, as a result of the multiparty drive, as the regime in power tried to forestall its eventual removal through elections. Through out the conflict (1992-1997), the international community only condemned and watched. These half way measures illustrated the shortcoming of the liberal theory, that the state, though some of its sovereignty may have been reduced, still retains some of it, such as monopoly over the instruments of coercion within its territory.

Another problem with liberal theories is the emphasis on the roles of international regimes, such as the World Trade Organization (WTO), WB and the IMF. Through a process of globalization, these organizations have advocated for liberalisation of the economy (laissez-faire). However, this has created problems in African countries, especially the Structural Adjustment Programmes (SAPs), which have deepened the gap between the rich and the poor. Devaluation, de-subsidization, de-nationalization and de-

[80] Ibid p.51

regulation, have led to the internal social-economic inequalities, often a security problem for African elites, who are seen to be more concerned with the west than their own people's welfare. The situation was best illustrated in 1985 in Sudan when the then President Jaffar Numeiry was ousted by a popular uprising occasioned by his accession to the World Bank demands of de-subsidization. The irony is that, as the West spends $300 billion on subsidies per annum, they expect others not to do so and this is "imperialism of free trade".[81]

[81] S. Burchill, op.cit p. 51

CHAPTER THREE

FOREIGN AID AND ITS IMPACT IN KENYA

Introduction

Private capital can either be direct or indirect source of investment. Direct investments refer to a situation where the investing country or company control all the assets and liabilities that have been generated. Indirect or portfolio investment is where the investing capital allows for some share holding from locals which is normally the minority Most poor countries (Kenya included) avoid the private source of capital due to the fact that the financial needs of these poor countries are so massive that the private sources may not easily satisfy. The private capital seeks quick profit to the extent that they may not invest in low yielding and slow yielding activities such as education, health, roads and infrastructure which are in serious demand in developing countries like Kenya.[82]

The periods of repayment in the private capital is much shorter and cannot be integrated into the development plans of poor countries. Private capital also encourages non-fixed interest rates which are driven by market forces. This makes it very unpredictable and a risky source of capital. In general, Foreign Aid can be received from the following sources

a. Bilateral cash which is between governments and is given in cash

b. Bilateral soft loan (grants) which is also between governments but comes either through project assistance or food grains. It can also incorporate personnel with some skills in implementation of the projects agreed.

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[82] James H Mittelman, *Globalisation, Critical Reflections*, (London, Lynne Rienner, 1997) p. 74

c. Multilateral sources which include agencies like UNDP, World Bank among others. The loans are normally for research and development with a view to making recommendations on plans or priorities.

Once foreign aid has been received, its role in economic development becomes extremely controversial. One school of thought argues that foreign aid is indispensable in economic development of poor countries. However the other school of thought emphasises that foreign aid abstracts economic development in poor countries.[83]

FOREIGN DIRECT INVESTMENT

Most poor countries including Kenya are not poor by choice. Moreover, even governments lack the capacity to accumulate sufficient capital through tax systems. This is because majority of the population is unemployed and only a few pay taxes. Against this background, Third World population growth stands at 2.5 per cent per annum. It is therefore implied that governments must provide service extensively. In addition; third world countries are technologically backward. This makes it difficult for them to add value to their raw products. Yet foreign aid not only makes capital available but also provides the much needed technologies.[84] Foreign aid can easily make available competent personnel in project management's financial organization and market information. Ideally, third world countries earn little income from their export which may not enable them acquire imported machinery which are expensive. When the value of

[83] Musalia Mudavadi op. cit pp.10-14
[84] Tony Cleaver; *Understanding the World Economy* (London, Routledge, 2002) p. 203

export is lower than that of imports, then a deficit gap emerges. It is only through foreign aid that balance of payment deficits may be bridged.

Virtually most of Kenya's foreign assistance has come from Western industrialized countries and multilateral institutions closely tied to them such as the European Union (EU), World Bank, and IMF. Kenya has, however, diversified her aid resources among the industrialized countries. Britain continues to be an important source of aid, but in the period since the middle 1970s has lost her predominant role. Between 1970 and 1974, Britain supplied 30 percent of the bilateral assistance to Kenya. From 1978 to 1981 the figure dropped to 17 per cent. West Germany, in the same period, virtually equaled Britain's assistance level. The most important trend in Kenya's foreign assistance, however, is the emergence of the United States of America (USA) in the early 1980s as the largest single source of Kenya's foreign assistance. [85]

Overhead capital investments require massive resource that poor countries may not manage projects such as hydro electrical power stations, bridges and infrastructure development. Many see foreign aid assistance in quickening development indirectly and governments may not readily invest in them. In addition risky investment like mining or oil exploration is marked by heavy pioneering losses that poor countries like Kenya cannot afford. It is only through foreign aid that such activities may be undertaken. Thus, poor countries are unable to start large industries given the capital demands. They can only succeed through foreign aid. Furthermore, foreign aid wideness employment opportunities in recipient countries since through such funds labour could be engaged.

[85] Joel D Barkan: *Politics and Public Policies in Kenya and Tanzania* (New York, Praeger 1984) p.309

Foreign aid politicizes life in the recipient countries to the extent that all activities are calculated with foreign aid in mind. Foreign aid perpetuates dependency and increased external control in an economy. This has been evident with projects such as construction of infrastructure. Foreign aid conditions always give loses to the recipient countries to the extent that original priorities are heavily altered to suit the interests of the lending institutions. Moreover, acquisition of raw materials may be external even if there could be local alternatives as was the case of constructing the Nyali Bridge in Mombasa where building material was imported from Japan.

Contrary to the view that foreign aid makes available advanced technologies, the reality is that this technology is not only inappropriate to the condition of poor countries but it also undermines their comparative advantage (labour). This is due to its capital incentives. Hence foreign aid does not solve the balance of payment but aggravates the situations. This makes poor countries lack capacity to take advantage of foreign aid.[86] They either invest in luxuries and wasteful activities that bring with it unnecessary cost like security and maintenance cost as has been the case with Moi International Sports Complex in Kasarani in the outskirts of Nairobi.

Despite the above arguments, Professor Bauer was amazed that countries which were initially poor, managed to develop without foreign aid while others that received huge amounts of foreign aid remained poor. His answers were that an economy must develop main springs of development such as its labour resources and how factors of production

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[86] Ibid p. 204

and production itself develop. Without this, economy cannot overcome poverty even if foreign aid doubled.[87]

The Millennium Declaration called on the donor community to support developing countries through increased Foreign Direct Investment (FDI), debt cancellation, improved market access as well as transfer of technology yet to date there are no significant improvements to honour this call. As at November 2004, Kenya's public debt was Kshs. 752.49 billion which is 63per cent of the GDP. Out of this, the domestic was at Kshs.301.54 billion while the external debt stock stood at Kshs. 449.95 billion. Servicing of this debt means committing a huge chunk of resources from the national resources leaving inadequate funds to implement the MDGs. For instance, between 2002 and 2003, Kenya committed Kshs 29,261.5 and 32,256.2 millions as external debt service charges annually. This gave adverse effects on the growth of the economy.[88]

The experience in Kenya is that the debt does not leave sufficient resources to implement the MDGs. Consequently, it is impossible to achieve any MDGs, without addressing the debt burden and the unfair trading practices. Without debt cancellation the government will continue channeling towards servicing the previous debt. Therefore with the international community's call to achieve the MDGs by 2015, debt sustainability criteria need to be redefined to focus on the MDGs and not merely on exports, as is the case in

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[87] Robert Gilpin op.cit p. 267.

[88] GoK (2005) *Millenium Development Goals Status Report for Kenya,* Ministry Of Planning And National Development p.30

the Highly Indebted Poor Countries (HIPC). In this regard debt should be said to be sustainable if it leaves enough resources to meet the MDGs.[89]

The Role of Agriculture in Kenya's Development

The role of agriculture is important because Kenya's economy was based on production of raw materials and mining. There was no emphasis on industrialization but on agriculture. Thus, Kenya adopted an agricultural led economy. Emphases were on production of agricultural products, export them and use proceeds to industrialize. Some industries were to be established. Thus agriculture was the backbone of all economic development. The decline in agriculture meant decline in manufacturing since a big percentage of population live in rural areas and use subsistence agriculture. Kenya was thought of as the leading light and was said to be moving ahead because of tea and coffee production. Yet the response of opposition politics to the structural causes of the agrarian crisis in Kenya has been quite disappointing.[90]

Agriculture is also important for production of food security. This has been a great weakness as Kenya failed to produce food for domestic consumption. The colonial legacy made the sector less mechanized for the indigenous farmer since modern technology was not available. Fluctuations in the world market also made Kenya dependent. Kenya has no voice at the WTO and its agricultural products do not march the market forces of global institutions. Notably Kenya fetched good prices in agricultural products until the

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[89] GoK (2005) Achieving *Millennium Development Goals in Kenya A Needs Assessment And costing Report.* Ministry of Planning and National Development p.31
[90] James H Mittelman op. cit p.158

fall in 1970's where similar products were produced for instance Kenya, Uganda and Tanzania all produced coffee hence competition was high.[91]

Alternative products have also been developed at the expense of Kenya's agricultural produce. For example cotton, had high prices in 1960's but when synthetic fabrics came up, cotton lost market. Thus policy framework is not favourable because there is lack of political will since some government officials allow importation of products which are found locally such as sugar and enhances poor terms of trade both at domestic and international levels. Notably, the Kenyan farmer requires many incentives so as to make meaningful production such as credit and exemption from certain taxes. But the Kenyan government relies on other financiers to assist farmers. In addition, mismanagement in agricultural institutions has been evident. Unfortunately, agriculture has not been emphasised in the school curriculum and does not have good ranking.[92]

Agriculture is not linked to industrialization and its graduates do not get jobs easily. This has been coupled by land ownership and tenure policies.[93] This is ill defined in Kenya since these policies discriminate and the big farmer is usually favoured thus encouraging idle land, where people own them purely for speculation such as the areas of Kitale and Molo in the Rift Valley province. There is a poor marketing strategy and competition from foreign goods and MNCs out wit local agricultural goods. The adoption of genetically modified food has led to lack of diversification in the agricultural sector. In addition the impact of SAPs on agriculture created competition and the government could

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[91] Ben Crow, Mary Thorpe (et al): *Survival and Change in the Third World* (nNw York, OUP, 1990) p.143
[92] Ibid p. 144
[93] Ben Crow, Mary Thorpe (et al) op .cit p. 187

not give subsidies such as fertilizers and farmers became vulnerable to the competition. Thus liberalization brought about competition between local and international textile products which led to the collapse cotton industry.[94]

Food Crisis in Kenya

Kenya has suffered serious decline in terms of agricultural food production. This has occurred against a background of rapid population growth. The drought of 1984 complicated the scenario because a lot of food production in Kenya relies on rain fed resources. A number of arguments have been raised in trying to answer the food paradox. A big percentage of the country is not arable due to natural constraints.[95] This has increased peasantry as a formidable political force which determines its own productive systems based on its needs and desires. Peasants are self- employed who cultivate land by hand. The key characteristics defining peasantry include family labour as the unit of production, and use of simple tools as the motive of production (subsistence). The persistence of peasantry as a mode of production has undermined economic development. The reality is that peasantry production has been declining and even food security has become a problem.[96]

Agricultural production in Kenya relies on international trade system yet the economy lack scientific capacity to add value. This has led to neglect of domestic market and declining return from international trade. Kenya was largely a colonial creation and so was its agriculture. Colonialism gave agriculture a top- down orientation that is a supplier

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[94] Joel D Barkan op. cit pp. 133-134
[95] Musalia Mudavadi op .cit p. 136
[96] Colin Leys op .cit p. 141

of raw materials and largely an extractive sector. It did not receive the value chain hierarchy that sucks such subjects as medicine. It was to be a support system which largely undermined relevant industrial set up. Agriculture, particularly food production suffered from lack of scientific personnel. Technical capacity in food production never occurred hence agriculture meant cash crop production. Innovative scientific knowledge and new inputs were controlled in cash crop production. The pricing system favour cash crop production at the expense of food production.

Ways of managing food crises in Kenya

Since Kenya's food production is reliant on the weather, there is need to invest in adequate reliable mechanisms of weather management. Food production has not received specialized efforts in what is necessary to provide the relevant seed crops based on an area resource endowment. Areas that are dry must use drought resistant crops and areas with rainfall and poor soils must utilize yielding crops in order to take advantage of the environment.[97] There is need to balance on modern foods stuff and the rich nutritious traditional foodstuffs. The new foodstuffs have taken Kenya by storm yet the better alternatives that are more energy providing are being neglected.

There is need to improve storage facilities and encourage incentives that enable farmers to produce food stuffs in excess of subsistence. This can then be distributed within the domestic markets. Food production must be treated in a similar manner as the cash crops if not better. This would entail improved extension services provisions, adequate infrastructure, new inputs such as high yielding crops and soil conservation. There must

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[97] Thomas D Lairson and David Skidmore op. cit p. 428

be requisite (corresponding) attempt to contain the rapid population growth. This is because rapid population growth threatens the land acreage available for production and also unchecked population growth may permanently stifle the capacity to expand food production. Food crisis in Kenya can only be solved when the government de-politicizes it since food crisis, has been used as regime survival strategy in terms of influencing decision making. Food production must enjoy special funds similar to the stabilization funds for export. There is need for the government to direct investments in food related sectors. This would enhance investment in different areas of food production and create vibrancy in the sector.[98]

Lack of subsidy in Agriculture

Policies like liberalization have undermined the capacity of local food production because of the intense competition from other cheaper agricultural commodities. This has made markets flooded and local goods have faired poorly. The removal of government support has made food production decline tremendously. The WTO regime view government subsidies as unnecessary and this has undermined efficient food production that heavily on government support

Use of fertilizers and chemicals approved by IMF has had serious consequences on food production. This is because these chemicals ravage the soil texture and changing to food production can only succeed after years of soil rehabilitation which is very expensive. There is a deliberate policy prescription to undermine the capacity of Kenya to add value

[98] Thomas D Lairson and David Skidmore op .cit p. 429

to their production. Any value added attracts high taxes yet the developed world would like Kenya to continue to supply raw materials that are zero rated according to the integration regimes. This has increased commodity production devoid of any value.[99]

Industrialisation in Kenya

Industrialisation provide capital goals and increases investment in the growth of industry with the objectives of converting raw materials into manufactured goods and this involves value addition for higher returns.[100] This has been lacking in Kenya due to colonial legacy. Ideally, colonial economy was pegged at fulfilling the colonial interest at home. The idea was not to develop industries in colonies but little processing was done to make them exportable to Europe. More emphasis was on agriculture but less emphasis on industrialization. Dependence on imported technology and capital goods brought about the negative accounts of payments, trade deficits, and external indebtedness was high because resources were spent on importing capital goods.

Lack of linkage between educational curriculum and industrialization brought about lack of appropriate skills. Thus the adopted agriculture led economy lacked capital machinery and input for industrialization. This led to establishment of foreign direct investment through MNCs. The major focus was to find out whether MNCs contributed to industrial or agricultural development. The roles of foreign investment were to promote foreign investment and liberalise the economy. There was technology transfer from north to south but the kind of technology transferred was inappropriate that led to the creation of

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[99] Thomas D Lairson and David Skidmore op. cit p. 433

[100] Ben Crow, Mary Thorpe (et al) op. cit p. 193

white elephants. The top cadre positions were held by foreigners, while the unskilled labour was given to locals and this created lay offs and retrenchment. [101]

The introduction of Automated Teller Machines (ATM's) renders people jobless hence I cannot credit MNCs with provision of employment. Performance of economic development is measured by employment. Foreign investment undermines local industries negating the policy of using indigenous people to build their economy. MNCs out-compete the local industries because they operate trans-nationally and make losses and profits differently. MNCs concentrate in profitable areas, with existing infrastructure. This is contrary to the development policy in most African countries.[102] They concentrate in urban centers with infrastructure because they want to make quick profit. MNCs accelerate class inequalities and this has caused underdevelopment in Kenya.

Environmental degradation through which resources leave the third world countries must be guarded. Programmes agreed between the IMF, World Bank and the countries are designed by World Bank and IMF. By 1980, high inflation, high indebted depleting infrastructure, balance of payment problems budget deficit in Kenya could not make ends meet. Thus in the 1980's when Kenya requested for loan they argued that the economy was maladjusted and hence Kenya needed to put it in order first.[103] Hence policies were put in place in order to qualify for these loans but the loans were never forthcoming.

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[101] Joel D Barkan op. cit pp.201-202
[102] Musalia Mudavadi op.cit p. 58
[103] The SAPRI Report (2004) *The Policy* Roots *of Economic Crisis and* inequality

MNCs and the culture of Consumerism

The spread of MNCs globally is an aspect of globalization. With globalization, MNC's dominate the economic activities of third world countries. A critical analysis of their operations shows that they have both positive and negative implications. The MNCs have been instrumental in upgrading personnel welfare in third world countries. They have great incentives to employees including local personnel in response to the shortage of the trained personnel. Many of them have developed programmes with universities and technical colleges in the third world countries. They have created employment opportunities for people in developing countries. They earn third world countries foreign money and improve their economies. Some MNCs are instrumental in developing infrastructure and bring technological relocation including work place facilities which tend to be more adequate compared to local industries.

These corporations exploit cheap labour in third world countries compared to workers in the developed world. In this respect, there is reduction in cost of production yet they pay workers peanuts. In some third world countries MNCs have been referred to as "runway plants" because they cause job insecurity.[104] Despite the overwhelming role of labour in wealth creation, it is imperative that sufficient capital must be available to sustain and boast production to execute specific tasks since labour wage motivates labour.

[104] Thomas Oately op .cit pp. 177-179

Debt crisis in the South

Debt crisis is one of the most prevalent structural problem that, countries of the south face. The developing countries during the period 1963-1973 registered a growth of 7.8 per cent and from 1973-1979 they registered a manufacturing output of 5.6 per cent. These growths were largely achieved because of the widening middle and working class in south. State of policies was also favourable and activities of MNCs were fairly positive. After 1975-1979 period, the mode of development in the south relied largely on accessing capital from developed countries through moderate interest rates. This was a common trend within the development of the south.[105]

Unfortunately after sometime, stagnating economies of the north and the recession of 1980 had a direct impact on the interest rate, of previously borrowed funds. This saw a sharp increase in the interest rates in the north to reduce inflation and the debt service ratio began to climb. By 1979 it was 19 per cent and climbed as high as 50 per cent in 1984. The scenario worsened by 1984 due to deep depression and increased protection of markets in the north. However, most investment to the south went to the Newly Industrialised Countries (NICs) that led to a situation of mainly consumer goods in the north. The collapse of former SU was a big blow to the developing countries, because economic assistance previously received in the East–South relations which by 1984 had amounted to 60 billion dollars reduced because Soviet Union focused in developing the economy of the Commonwealth of Independent States (CIS).[106]

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[105] Robert Gilpin; *Global Political Economy: Understanding the International Economic Order* (Oxford, Princeton Press,2001) p. 315
[106] Ibid p. 317

The operations of MNCs changed with their realization that most of the policy proposals would not hold. They began dumping old machineries, producing for protected market, repatriating profit and undermining local capacity in industrial process as was the case with Del Monte in Kenya. These changes made the south particularly from 1980 to 1990 to register a slow growth of an average of 0.9 per cent of GDP and 2.6 per cent manufacturing output. Similarly the south's capacity was further weakened by poor terms of trade, whereby primary products declined steadily, yet these economies were expected to repay their debts.[107]

Equally debt crisis have been complicated by internal structures in developing countries. Most of the capital is directed to capital benefit at the expense of society. A big percentage is mismanaged either through corruption or repatriated to overseas accounts as individual capital. By 1986 the south had transferred 250 billion dollars to the north compared to the Marshall plan for Europe which was only 13 billion dollars. From 1984 to 1989, Latin American countries paid Northern creditors 153 billion dollars as interest on borrowed capital. The implication of this transfer of wealth from the south had critical consequences. Average annual per capital GNP growth in sub- Saharan Africa for the 1980's was 2.2 per cent and Latin American was – 0.6 per cent. Only countries of the South East Asia region recorded growth.

[107] Robert Gilpin op .cit p. 282

Growth by real per capita GDP by period

Region	1965- 1973	1973- 1980	1980- 1989
Sub- Saharan Africa	3.2.	0.1	-2.2.
Latin America	3.7	2.6	- 0.6
East Asia	5.1	4.7	6.7
South Asia	1.2	1.7	3.2
Middle East of North Africa	5.5.	2.1	0.8

Source: World Development Report 1990 pg 11

South East Asian countries did well because of manufacturing and focused leadership. The above statistics were further made severe with very rapid population growth against diminishing capital. In order for the developing countries to service their debts, they accepted new policy prescriptions. The south has been forced to de-nationalize their economies, dismantle the import barriers, de-regulate the financial market and privatize state owned enterprises.

Solutions to debt crisis

There have been calls for total debt cancellation in the south because they were brought into contract that they did not understand. A global framework is needed to incorporate all players with a view of making available debt relief by converting such debts to specific programmes of development in the south. Through the World Bank a debt reduction facility was established targeting low income countries that suffer the natural constraints but would still be in accession to soft loans. Thus, developing countries must

strengthen their absorptive capacity and identify key areas of growth such as food production, population control, energy resources, security and environmental conservation.[108]

There is need to introduce a comprehensive regime for foreign investment that would establish a code of conduct on MNCs and how their operations can benefit developing economies. Previously loans were not subjected to high interest rates. International mechanism should be put in place to check the vitality of exchange rates of the principal world currencies. Incases where rates have gone up, then the developing economy should be insulated from the effects of excessive high charges. The south must be insured against unexpected shortfall in foreign exchange earnings and protectionism in the north must be removed because the same north advocated for free trade. The north fears the emergence of a strong unified aggressive south to the extent that the debt crisis among other instruments is used to condition, regulate, divide and weaken the south. Debt crisis has assumed a life of its own as a new weapon to achieve obedience and compliance to specific policies that cannot be achieved through International Trade Agreements.[109]

STRUCTURAL ADJUSTMENT PROGRAMMES (SAPS)

Structural Adjustment Programmes (SAPs) are an aspect of globalization. They were meant improve the economies of third world countries by enabling them pay their debts as well as achieve sustainable economic development. The 1980's was described as a lost

[108] Joan Edelman Spero: *The Politics of International Economics Relations*, (London, Routledge, 1990) p. 182
[109] Ibid pp. 183-185

decade for Africa.[110] This was a decade characterized by poor performance of economies and an increase in external debts. The performance of Kenya's economy during this period provided justification for introduction of policies that would enhance development. Kenya got many problems which affected its economic development. Kenya has been faced with very many natural calamities such as floods, drought and famine. Man-made disasters, dictatorship, political unrest, poor governance as well as lack of political will were a concern for the developed world. In addition, population explosion brought unfavourable international terms of trade. The economy was narrow based and cultural practices that hamper development were witnessed.

During the 1980's many third world countries defaulted in servicing their loans. This created fear all over the capitalist world. Western countries led by USA impressed on the IMF and World Bank to improve on debt collection from third world countries. To enhance this, the IMF and World Bank attached certain conditionalities to loans given to these countries. These conditionalities came as Structural Adjustment Programmes (SAPS).[111] These conditionalities would lead to sustainable economic growth and help them solve economic problems. A critical analysis of these conditionalities shows that there were other motives. Among the conditions were reductions in government spending, liberalization, export promotion, privatization of public sector activities only but to mention a few.

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[110] James H Mittelman op cit p. 148
[111] James H Mittelman op cit p. 2

Reduction of government spending

The official aim of this conditionality was to reduce excessive demand of limited government resources. This was a way of ensuring that governments have enough resources to repay loans. Due to this, governments in the third world countries including Kenya reduced spending in health, agriculture, education and even carried out retrenchment. In the health sector there was the introduction of cost sharing in hospitals creating inability to expand the health sector. There has been no improvement in pay of health personnel. There has also been the inability to increase health staff. Many people are dying of preventable health problems. It is also becoming difficult to manage endemic health programmes such as malaria, HIV/AIDS, giving an increase in mortality and morbidity while the poor have been cut from accessing quality health service.[112]

Critics argue that the impact of SAPs on health have a gender perspective. Women tend to be affected more by health problems because of their reproductive roles. Women tend to have lower income compared to men hence may not access health facilities. Women have concentrated in rural areas where there is no increase in health services. Women also take care of the sick in the rural areas and engage in agriculture. Reproduction in spending in agriculture has affected food production and therefore led to famine in some countries. It is argued that many women are involved in agriculture than men especially in food crop production. This has impacted negatively on food production.[113]

[112] Musalia Mudavadi op. cit p. 78
[113] Ben Crow, Mary Thorpe (et al) op .cit p. 140

Retrenchment (commonly known as reduction of civil service staff) was also carried out as a condition of IMF. This contributed to unemployment and worsened poverty. It affected women in the third world countries because they occupy lower level jobs in the civil service. Women are more likely to be less skilled compared to men and women are affected by reproductive roles. The social services and infrastructure sectors such as housing, water, electricity and road, were also affected. The government of Kenya reduced spending since this conditionality had a noble objective. Its implementation has produced negative results.[114] The IMF condition on education became too expensive for the poor. In some countries there was reduction in enrollment, poor remuneration of teaches and illiteracy went up. This also reduced investments in other areas. Women have been affected more because of cultural values that tend to enhance the chances of education of male children compared to the female ones.[115]

Liberalisation of markets

The official aim of this conditionality was to increase international competitiveness and efficiency. Competition would bring improvement in quality and efficiency. The implication of this conditionality has had some negative implications. It continues to undermine local industries such as textile and sugar. Local industries are unable to compete favourably with goods from other markets. This has led to unemployment because some industries have closed down.[116] It has also meant that multi-nationals dominate economies of third world countries and they have been accused of exploitation

[114]Joel D Barkan op. cit p.52
[115] Joel D Barkan op. cit p.53
[116]Thomas Oatley: *International Political Economy, Interests and Institutions in the Global Economy*, (London, Longman, 2006) p. 19

of cheap labour and destruction of environment. Liberalisation devalued national currencies and removed government from protecting the economy. The government was to sell out parastals to enhance reduction of state control of economy because governments are not good in business since they were eating into national revenue.[117]

Export promotion

The aim of the export promotion conditionality was to earn foreign exchange for debt repayment. This had negative implications. In Kenya there was replacement of food crops by cash crops creating food insecurity. The establishment of export processing zones (EPZ) led to exploitation of cheap labour and bad terms of payment. It increased dependence on foreign markets and damaged the environment. Earnings in this sector went to debt repayment and not investment. Thus, African countries among them Kenya did not have control the kind of exports they specialized in.[118]

Privatization of public sector utilities

This conditionality was to reduce public expenditure and increase efficiency. The argument was that governments are bad in giving transport, postal and electricity services. However turning over public utilities to the private sector where profitability over rides social welfare was likely to exclude the performance of certain basic services. There has been the problem of ownership where the public utility being sold end up into foreign hands. Thus in June 1982, the government appointed a working party on

[117] Oyugi Aseto, Jasper A Okello: *Privatization in Kenya* (Nairobi, Basic Books 1997) p.139
[118] Ben Crow, Mary Thorpe (et al) op cit p. 292

Government Expenditures chaired by Philip Ndegwa to address the issue of privatization of the public sector utilities.[119]

The social cost of SAPs has been enormous and critics argue that SAPs have succeeded in entrenching African economies into the world capitalist system. These conditionalities may have developed to serve the interest of western capitalist world. The conditions may have been used to serve political interest because by propagating capitalism, they were leading to align themselves with the west. The impacts of SAPs in Kenya kept labour cost low and deepened dependency since there was repartition of money, sale of parastals to foreigners and hence no value addition to the indigenous people. The removal of government subsidies in agriculture, education and health made the government to stop issuing inputs to farmers at low cost such as fertilizer and in education it meant that even university students paid fees. The net effect was widening class. In medical, free health care in rural areas was done away with and cost sharing was introduced. SAPs also stopped the government from regulating prices of basic commodities. In Kenya this was left to market forces. Retrenchment helped lower expenditure. There was no money for investment and it denied leaders a chance to buy loyalty. This led to urban crime.[120]

The political implication is that free political activities and free market economy reinforced capitalist ideology, eroded sovereignty, and opened up political systems. Economically, SAPs deepened dependency, increased debt, as more emphasis were on

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[119] Republic of Kenya, *Report on the Working Party on Government Expenditure,* (Nairobi, Government Printer,1982)

[120] Joel D Barkan op .cit p.113

exports targeting EPZ to undermine local industry and marginalize the poor countries due to the failure of government to effectively interact with them.

IMF POLICIES

Liberal Economic Reforms

Economists and political scientists have argued and continue to argue whether there is anything like free trade. If free trade could be loosely taken to mean market driven exchange without government involvement then there are strong beliefs that free trade is superior of trade protections. They contend that open economic stand gain considerably from cheaper imports. Despite this argument trade protection has not disappeared from the world economy whereby restricted trade has been a feature of world economy. Thus with liberalization of economies the third world countries find it difficult to cope with the demands of free trade.[121]

According to Paul Bainch, free trade has been historically the exception and the protection of the developed nations. This is because nations take advantage of 'foreign' markets but are unwilling to open up their markets. The fear is that free trade may hurt some specific class interests and undermine reactive prices in the pattern and distribution of gains from trade. Over the years, international trade has been regarded either as an international public good "forum" which everyone benefits or as a battle ground in which there are winners and losers. Even though the argument for free trade is powerful,

[121] Robert Gilpin op .cit p. 265

protection continuously raises tension and continues to rise between, trade liberalization and professionalism and the future of free trade remains "precarious".[122]

Trade protection has been internationally promoted as one of the first steps in which the economies generate revenue. This is done by creating high tariffs regimes to imports so that local goods are cheaper in the market. As a matter of fact the developed nations through IMF have continued to reinforce this so as to antagonize young nations such as Kenya. But through careful trade protection, weak economies can boost their domestic entrepreneurs into manufacturing and take advantage of environment.

Trade protection is a good way of domesticating industry to the extent that local ideas and resources are used in the production process. Trade protection ensures an economy does not become a mirror of another economy since that is what free trade promotes although situations differ greatly. Trade protection allows an economy to realistically access its potential through comparative advantage such that goods can be produced cheaply and also find out where it does not enjoy such advantages. Once this is done then an economy can develop strategically to fill the void.[123]

In the same line, trade restriction enables an economy to promote desires and wants that are realistic to their situation. But security concerns may militate against free trade since some industries that are sensitive require state protection such as food security, communication industries and arms industries. In addition, environment protection may

[122] Tony Cleaver op.cit p. 103
[123] James Mittelman op. cit p. 53

necessitate some elements of trade restriction. Thus the role that the environment plays in economic achievements can not be overemphasised. Trade restriction may also be influenced by human rights concerns such as child labour and workers welfare.

Of least concern is that trade is no longer a purely economic matter but it is embedded on nature, state and sovereignty. Although import restriction had been admired, a number of people argue that it overburdens an economy and creates monopoly, rent seeking and cartelism. On the contrary the liberal doctrine of free trade is based on the principles of the market systems as formulated by classical economists.[124] Adam Smith and David Ricardo argued that the removal of restriction on trade and service would enhance speculation and optimal utilization of the world's scarce resources. The trade liberalization would led to efficient pattern of trade as anchored by comparative advantage of the relative factors of production which include land, capital and labour.

Kenya needs to adopt a comparative cost in production which would strengthen its economic growth within the global economy. Underlying this conception is that Kenya should research on free trade and see how it builds economic activities so as to maximize economic growth. Free Trade enhances international competition because it undermines anti-competitive practice thereby increasing both domestic and international wealth. It also promotes comparative advantages while at the same time ensures trade complimentarily. Free trade builds international co-operation among nation states. However, a number of people have pointed out that trade benefits developed economies and lead to dependency in the less developed ones. Proponents of trade protection reject

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[124] Tony Cleaver op. cit p. 256

free trade and other forms of globalization as threat to jobs, wages and domestic social welfare. They point out that free trade undermines the weak. It is important that the state should guide and shape the overall industrial and technological structures of the society through careful and selective trade protection, industrial policy and supervision.[125]

Despite the above arguments it is impossible to find a purely free trade environment or a purely protected economy. What is there is a hybrid whereby protective measure tends to enforce tree trade. It is prudent for a developing economy to mature into sustainable position and have industries that are able to compete. In summary the issues on the implantation of free trade were some of Kenya's challenges in coming to terms with the IMF conditions although as Charles Lindborn argues, free trade rarely exists. The politics of market is concerned with economic competence of Liberal theory.[126]

Capitalist Economic Globalization

The other major challenge for Kenya was accepting capitalistic economic globalization. As it has been argued, 'imperialism began a process in which the colonies with the pre-capitalist modes of production were undermined and destroyed. The subsistence economies were rudely interpreted and Kenya was not spared from this either. According to Lenin V.I, imperialism can be summarized as the off-spring of monopoly of capital, exploitation of capital and the development of spheres of economic influence.[127] In order for imperialists who were Kenya's colonial masters, to maximize their intended economic exploitation, other aspects of the society were also to be shaped so that a proper

[125] Robert Gilpin op. cit p.71
[126] Robert Gilpin op. cit p.27
[127] Robert Gilpin op .cit p.39

environment was created. This is why the political and social elements within the colonies, were transformed. This meant that for capitalism to thrive certain obstacles were to be removed during the implementation of economic reform programmes.'

According to Karl Marx, capitalism is synonymous to class struggle. The owners of the means of production, as a class are always pitied against the labourers. The struggle is built on the fact that despite their efforts, the labourers loose out because their wages do not match what the bourgeois obtains from the market. Such a reform would make Kenya just to survive and ensure that there is a constant labour supply for the production of goods for the developed nations.[128] Economic globalization can be defined as a situation in which activities and events in one part of the world have a series of effects in other entities elsewhere. Similar decisive, policies and advances made in specific areas have a spill over effect in distant countries. [129] For example the events of 11 September 2001 in the USA were felt all over the world. The major reasons for the rapid economic globalisation will be discussed further in subsequent paragraphs.

International trade reproduction and consumption require that large markets are established outside a state boundary. The end of the cold war and particularly the death of communist Soviet Union (SU) gave capitalism a new lease of life as it triumphed as the new force in global trade. This led to opening up of the closed markets and even Cuba which had a stronger socialist ideology went for selective international trade. The end of socialist conglomeration strengthened the movements of capitalist dominance as an

[128] Robert Gilpin op cit p.40
[129] James H Mittelman op cit p.64

enduring mode of production and young nations like Kenya had no option but to agree to the demands of the capitalist economic globalization.[130]

The movement and expansion of MNCs with their headquarters based in their parent countries captured mainly exclusion to established subsidiary. The main motive of creating subsidiaries in other economies by MNCs was to take advantage of their situation and create strict regulation and high cost of labour was avoided so that other states without strict rules bear the burden of MNCs operations under the disguise of economic globalisation. Kenya too suffered the wrath of MNCs as they continued to dominate its economic activities.

Problems with Economic Globalisation on Kenya

The problem of economic globalisation is that Kenya was integrated into the international economy forcefully to the extent that a number of distortions are present to date. These distortions denied Kenya the natural movement from pre-capitalist to capitalist based on their own internal logic. It made Kenya a commodity producer and neglected manufacturing. Its economy continues to evolve within the economic globe as a supplier of raw materials without manufacturing content. This limits resources that Kenya receives because capital respects value and Kenya's goods do not have value addition.[131]

Kenya's economy was shaped to produce cash crops for external markets. Fertile lands were exclusively reserved for export production which, undermined food production and

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[130] Jonathan Michie And John Grieve Smith: *Globalisation, Growth and Governance* (Nairobi, OUP 1998) p.5

[131] Colin Leys: *The Rise and Fall of Development Theory*, (Nairobi, EAEP 1996) p.143

brought total neglect to domestic market. The production within the international trade is one whereby if sources of capital are from external resources then to produce goods for external markets becomes very expensive. Thus, economic globalisation has undermined Kenya's state sovereignty in the sense that territorial boundaries do not matter because of free movement of goods and services.[132]

Economic globalization brought with it immense structural reformations in Kenya. SAPs prescribed that the state must be removed from economic activities. The state was accused of corruption, lack of transparency and inefficiency. The liberals recommended the market forces as a suitable replacement. This was intended to strengthen capitalism particularly it's exploitative and domineering virtues. SAPs called for privatisation of public enterprise. Yet Kenya's local capital capacity could not buy such enterprises but sell them to foreigners with capital. Partial privatisation was encouraged, where top management had the reserve for exports which were treated differently. The SAPs introduced cost sharing in public utilities to the annoyance of the citizens who were used to free services. This created tension and political instability in Kenya.[133]

Economic globalization also brought in a new lease of life where it controlled political activities. In order to receive foreign assistance, Kenya was forced to adopt multi-party democracy. Thus Kenya's democratic policy system was ridiculed as undemocratic to the extent that local forces in the opposition were fully funded and encouraged to oppose the government of the day. Moreover, Non-Governmental Organisations (NGO's) emerged

[132] Ibid p. 144

[133] Musalia Mudavadi op. cit p. 9

as new alternatives to the state. They were seen as transparent, connected to the people, less bureaucratic and thought as new partners of development. Unfortunately NGO's did not make any significant contributions. A lot of resources were wasted in conferences and accusations between the so-called stakeholders denying the government of Kenya an opportunity to strengthen its resource capacity.[134]

Economic globalisation opened Kenya to international telecommunication systems. However, global telecommunications encouraged money laundering where terrorist activities and dissemination of inappropriate values are accessed very easily. Despite its negative implication, economy globalization has made communications easy and facilitated exchange among people. It has strengthened the competitive value of Kenyan goods in the global market and has made learning and exposure to ideas immediate where at the luxury of ones sitting room, one can access and join classes in Europe or North America. This is a diversifying source of opportunities. [135]

It has made people interact frequently and improve their leadership. It has made the movement of capital easy from the developed world. One can argue that economic globalisation can be benefiting and marginalizing but as of now, Kenya's economy has been marginalized due to lack of capital and technological capacity. The owners of capital embrace economic globalisation and the way forward is for Kenya to embrace regional economic integration; so that they can approach the global market as a region.

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[134] Thomas D Lairson and David Skidmore: *International Political Economy, The Struggle for Power and Wealth,* (London, Thomas Wadsworth,2003) p.409
[135] Ibid p. 410

Global Political Transformation

Geopolitical shift and the post cold war political system removed one super power that had balanced the other. During the cold war, most countries of the south benefited through technological support, economic programmes, educational opportunities and military hardware. The geo-political shift made the developing countries very weak with reduced assistance and was forced to re-assess their policies. A lot of governments were either over thrown or replaced.

The paradigm shift and post cold war political economy saw the emergence of neo-liberalism in which the market forces were to be the determining factor in production. The state was no longer seen as suited to social transformations. Policies on privatization, liberalization and free trade were a hallmark of international relations. Unfortunately Kenya could not easily absorb and implement these realities because it was consolidating its activities particularly on the allocation and distribution of resources. SAPs were meant to restrict what was perceived as structural problems of Kenya. The state was not accountable, it lacked transparency, was inefficient, corrupt, lethargic and largely arbitrary. Thus, the state suffocated the market which contributed to the burden of market forces which erupted and only cooled after finding their bearing.[136]

The loss of sovereignty continued pursuit of favorable access to new technologies, markets and improved commodity pricing. The north created the agenda for the developing countries. Human rights, corruption, gender equity, good governance, child rights and democracy were on the agenda. The south simply played by the rules and did

[136] Tony Cleaver op. cit p.139

not determine what constituted the agenda. Universal institutions such as the United Nations (UN) were not spared because vested interests took over. Unilateralism emerged and the developing countries were major causalities because either they supported unilateralism or opposed it to their detriment.

The world became more integrated and closer to the extent that it was no longer feasible to talk about the developing countries. This new reality meant that the developing countries had to re-organize their structures within the globe as marginalization was eminent in its attempt to respond to the emerging trends to original agendas of the developing countries. Thus the post cold war era dramatically changed developing countries agenda. This is because globalization demanded that individual states had to re-think their positions on a number of issues. The developing countries agenda lost ground and it was captured by the force of globalization.[137]

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[137] James Petras and Henry Veltmeyer: *Globalisation Unmasked; Imperialism in the 21st Century*, (Halifax NS Fernwood, 2001) p. 32

CHAPTER FOUR

IMPLEMENTATION OF IMF PROGRAMMES IN KENYA AND ITS IMPACT

Introduction

The 2002 elections in Kenya saw a resounding rejection of the Kenya African National Union (KANU) and Daniel arap Moi's legacy of endemic corruption and mismanagement. As the first electoral change of government in independent Kenya, it aroused hopes of the possibility of reform and renewal. Among President Kibaki's first acts was the creation of a new Ministry of Justice and Constitutional Affairs (MoJCA), mandated to coordinate the anti-corruption campaign and spearhead the enactment of laws to facilitate it. The appointment of Transparency International's (TI) John Githongo to the newly created position of Permanent Secretary (PS) in the Office of the President for Governance and Ethics was considered an indication of serious political will to combat the pervasive corruption which had seen Kenya occupying an apparently permanent position near the bottom of TI's annual Corruption Perceptions Index.

By May 2003 two keystone pieces of legislation had been enacted: the Anti-Corruption and Economic Crimes Act (ACECA), which created the Kenya Anti-Corruption Commission (KACC) with responsibility to investigate corruption and economic crimes and conduct public education on corruption; and the Public Officer Ethics Act (POEA), which provides for codes of conduct for all public officers and compels all officers to

declare their wealth, including that of their spouses and dependent children. With these two Acts, Kenya fulfilled long-awaited conditions for the improvement of relations with multilateral institutions after their suspension of cooperation with the Moi government. IMF resumed leading in November 2003. The new government argued that, by submitting to external demands, it was henceforth committing itself to its own conditionalities for the economic recovery of Kenya. However, the attitude of the international community has constituted a large part, whether positively or negatively of the NARC government's preoccupations.

The NARC government had campaigned on the platform of anti-corruption and promised to establish a comprehensive truth commission or similar body to facilitate accountability for past economic crimes and violations of human rights. After taking over power, the NARC government appointed a task force in April 2003 to collect views on the need for and structure of a truth commission. In October 2003, the task force recommended the formation of a truth, justice and reconciliation commission (TJRC) to look into crimes and human rights violations since 1963.

Implementing Reform Measures

It is evident that political governance and corruption influence each other in many ways. The tragedy is that corruption facilitates the diversion of public resources into private hands. For corruption to be effectively addressed Kenya must embark on political and economic reforms. The reforms should promote free and open competition, as in the case of bidding to provide goods and services to government. They should promote

transparency and accountability in the private sector. The reforms should hold the political leadership accountable for their actions. As long as there is no accountability in political leadership, the fight against corruption will not be easy. Civil society has an important role to play in the fight against corruption. This includes monitoring roles as well as advocating and lobbying for the enactment and enforcement of effective legislation to fight corruption, naming and shaming public officials found engaging in corrupt activities.

When one talks of corruption, it is unavoidable not to talk of good governance. Good governance means a system of governance that is free of abuse and corruption and which pays due regard to the rule of law. Various writers have attempted to identify the attributes of good governance. The UN's Commission of human rights took a major step in trying to clarify this concept. In its Resolution 2000/04 it identified eight major characteristics of good governance. These are: -

a. Participation: good governance needs organized and informed participation in public affairs by both men and women.

b. Rule of law: there should be a fair legal framework that is enforced impartially and there should be protection of human rights.

c. Transparency: decisions taken by public bode must be taken and their enforcement carried out in a manner that follows rules and regulations.

d. Responsiveness: Institutions and processes should try to serve all stakeholders within a reasonable time frame.

e. Consensus: good governance requires mediation of the different interests in society to reach a broad consensus.

f. Equity and inclusiveness: all members of a society need to feel that they have a stake in the society.

g. Effectiveness and efficiency: Process and institutions should produce results that meet the needs of society while making the best of resource at their disposal, and

h. Accountability: Government, private sector and civil society must be accountable to the public and to their institutional stakeholders.

Economic recovery through good governance

The overall policy direction of the NARC government is laid down in the Economic Recovery Strategy for Employment and Wealth Creation 2003 (ERS). In keeping with its election manifesto the new government's plans for recovery were firmly predicated on the need for governance reforms and the strengthening of governance institutions. The ERS promised the passage of key laws. In addition to the ACECA and POEA, a public

Procurement and disposal of Public Assets, and a Financial Management and Accountability Bill were promised within the 2003/04 financial year. The government undertook to bring individuals involved in corruption to court. The Attorney General and the Anti-corruption Police Unit, precursor of the KACC, were to produce quarterly progress reports on investigating and prosecuting cases of corruption, the establishment of task forces to review various past misdeeds was also envisaged.

The ERS promised the establishment of a commission to inquire into the Goldenberg Scandal so that proper prosecution and assets recovery could follow. Further measures, including the creation of an ombudsman, were contemplated[138]. Progress against corruption was to be achieved through a strategy whose pillar was political will, dealing with the abuses of the past institutional reform and legal reforms; and coalition-building with non-state actors and the international community. Political will is commonly viewed as essential to the success of any reform programme. The Kenya anti-corruption programme was predicated on the personal commitment of the president, who took every opportunity, in the first year, to reiterate his stance of a 'zero tolerance policy towards corruption. Kenya embarked on ACECA. The act is the successor to the under-enforced colonial Prevention of Corruption Act, 1956. It goes beyond the latter in its definition of what constitutes a corrupt act and in creating a mechanism that enables the government to seize corruptly and criminally acquired assets.

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[138] GoK 2003, *Economic Recovery, Strategy for Wealth and Employment Creation*, www.statehousekenya.go.ke

The Public Officer Ethics Act crafts ethical standards for public officers and creates a legal framework for dealing with conflicts of interest. The occupation of public office in Africa has long been the shortest avenue to great wealth, and Kenya is no exception. Kenyan civil servant's consciousness of what constitutes a conflict of interest has become remarkably blunted over the years following the conclusions of the Ndegwa Commission, which in 1971 recommended that public officers be allowed to conduct private businesses.[139] A series of measures were recommended that ostensibly aimed at mitigating the danger of conflicts of interest. They were ignored as permission to engage in business was enthusiastically embraced by the nascent African bureaucratic elite.

A conflict of interest that irks the Kenyan public today is the exploitation by the senior public servants in particular Members of Parliament (MPs) of their power to determine their wages and allowances, in the absence of a national wage policy, to exorbitant pay scales and profligate expenditure.[140] The wealth declarations submitted under the POEA are not amenable to easy scrutiny since, a part from being strictly confidential, they are available only in hard copy. Attempts led by John Githongo (former Permanent Secretary of Governance and Ethics) to capture the declarations electronically and render them easier to monitor were unsuccessful. While the NARC government's reform strategy is heavily biased towards a lengthy menu of legislative reform, Kenya's parliament, despite the generous salaries and allowances it has approved for itself, is notoriously lethargic. For the larger part of 2003 MPs managed to pass only three laws.

[139] Sunday Standard: *Ministers Conspire to dodge Land Tax*, 16 Jan 05.
[140] H.Mule TCI Ryan and D Ndii: *Public Sector wage Policy study*, Ministry of Finance, Nairobi 2004.

Dealing with the past

Kenyans hoped to uncover, punish and avert repetitions of the abuses of the past. The NARC government chose to investigate and ultimately redress these abuses through a series of specially established commissions of inquiry. The most prominent was the commission of Inquiry into the Goldenberg Scandal, established to look into the infamous and complex scheme of swindles around non-existent exports of gold and diamonds from Kenya in early 1990's which ultimately cost the country an established US$ 650 million.[141] The commission did well to unearth in detail the methods used to defraud the country.

However, after a massive investment of resources, questions whether the commission will adequately fulfill its terms of reference are justified. Kenyans demand that the senior figures involved be brought to book. They crowded to witness the proceedings of the commission, which were reported fully in the electronic and print media. However, if the conduct of the inquiry is any indication, Kenyans may well be disappointed. The report of the commission came out in October 2005, at which time many Kenyans were too preoccupied with the planned constitutional referendum to pay attention to its conclusions. It seems that the government has distanced itself from its original commitment to recover assets.

The Commission of Inquiry into Irregular and Illegal Allocation of Public Lands known as the Ndungu Commission after its chairman, looked into the expropriation of public

[141] Government of Kenya, Gazette Notice No. 1238, 24 Feb 2003

lands to the politically connected. The misappropriation of public land was increasingly adopted under President Daniel arap Moi as a means of accessing resources and dispensing other avenues for corruption were increasingly closed down by advancing economic liberalisation. However, the government's delay in publishing the Ndungu's report overshadowed the commission's work. The NARC government displayed a talent for shooting itself in the foot. The report, with its list of beneficiaries of illicit land transactions, demonstrated clearly the web of complicity that implicates large sections of the Kenyan elite of whatever political colour in plundering the country's resources. According to the report, illegal forests excisions alone amounted to 299,077.5 hectares since independence. Development of a comprehensive land policy remains imperative.[142]

The Pending Bills Verification and Validation Committee sought to unravel valid from invalid claims on the government in the area of construction and recommended that millions of shilling be repaid by construction companies, in some of which public officials had an interest, and that some companies be blacklisted. Pending bills are one of the many imaginative ways in which the exchequer is defrauded. Ministries fail to pay their bills and carry them forward into the following financial year(s). A part from allowing them to fudge their expenditure positions, this is a gross violation of regulations that also represents expenditure incurred without parliamentary approval. Through this mechanism, government ultimately pays for non-performing contracts of fraudulent bills; for instance a batch of 31 companies whose pending bills for Kshs 9 billion were

[142] Ndungu Report

sctrutinised, only about Kshs. 250 million or 3 per cent of the total bills were genuine claims, the committee found.[143]

Asset Recovery

Asset recovery is not an easy task and is fraught with secrecy laws, the complicity of the banks and governments involved, and the navigation of a costly international legal labyrinth. Additionally, recovery attempts are complicated within African countries because those who are mostly implicated in public looting are usually those with the most power and influence.[144] Thus it is an unenviable task for governments, let alone one operating in an environment with few anti-corruption institutions. Yet the potential rewards, in the form of the repartition of money into development starved countries, make asset recovery an attractive undertaking.[145]

Although asset recovery cannot be separated from the broader challenge of the battle against corruption, it does occupy a distinct place in anti-corruption activities with a specific set of concerns. To address these issues I will look at the experience that Kenya has attempted to repatriate some of their lost wealth, and the practical challenges it has faced.[146] A significant element in the asset- looting matrix is foreign aid. In the African context, foreign aid during the cold war was linked to support for either the Western or the Soviet bloc. With global strategic interests at play,[147] donor governments were often more than willing to overlook pillaging of aid and state coffers in return for continued

[143] Daily Nation, 9 September 2003
[144] Commission for Africa, Our Common Interest;*Report of the Commission for Africa,* March 2005 p. 152.
[145] H Goff, The downside of the G8 debt deal, *BBC News* 8 July 2005
[146] Commission for Africa op. cit p.152
[147] G. Mutume, Africa Survives to rebuild its domestic Industries, *Africa Renewal* 18 (3) October 2004 p.1

support from despotic leaders, Mobutu Sese Seko being a classic case. During his three decades in power he received an estimated amount of US$ 2 billion in aid from the USA alone, and the bulk of which ended up in his pocket, for private planes, European chateaux shopping sprees, and other hallmarks of the high life.[148]

Having placed asset looting in its historical context, why should leaders attempt to reclaim their assets now? The answer is related to the broader battle against corruption. In the mid 1990's the detrimental effects of corruption emerged as a chief concern among governments and multilateral institutions around the globe for a number of reasons including the fall of the Soviet Union and the subsequent exposure of a high level of institutionalized corruption.[149] The Kenyan case shares many of the hallmarks of a ruler who enriched himself on the back of his county's poverty; a new leader promising an end to corruption, and a widely popular drive to retrieve the funds stolen by the previous regime, most notably looted in the infamous Goldenberg Affair. Yet the Kenyan case differs in a number of key areas, the most significant being the way that the campaign ran out of political steam before any funds were recovered. To date Kenya has found itself bogged down in stalled inquiries and legal procedures.[150]

When the country received independence from the British in 1963, Kenya's future looked bright. Kenya has a well-resourced state and under liberation leader Jomo Kenyatta

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[148] A Chang, *Get your money's worth, ABC News* 23 December 2002 www.global policy.org/United States/Un policy/gen 2002
[149] J. Brandolino, *The United States and International Anti-Corruption Efforts* 1 January 2002 www.state.gov/g
[150] Kenya to Recover Stolen Money, Mail *& Guardian* 19 March 2002.

maintained a GDP growth of around 8 per cent[151] throughout the 1960's. Although Kenyatta is credited with introducing the seeds or rot into Kenyan institutions, it was only after his death in 1978 that Kenyans began to materially and noticeably deteriorate. President Daniel arap Moi came to power and, as the respected Kenyan anti-corruption expert and former Permanent Secretary John Githongo puts it, he oversaw the systematic destruction of our institutions.[152]

By 2001 Kenya was losing around US$ 1 billion a year to corruption,[153] the economy had stagnated and was shrinking at a rate of 3 per cent a year[154], and unemployment was at 10 per cent. Additionally, International aid had been ceased, owing to rampant corruption.[155] Daniel arap Moi had amassed a massive fortune while his country deteriorated with seven palatial dwelling in Kenya and known associations with thirty Kenyan business firms, his personal wealth has been described simply as fabulous.[156] Of the amount looted during Moi's presidency. Kenya's anti- corruption commission estimates that US$ 3 billion is still hidden in overseas bank accounts,[157] an amount equal to almost 9 per cent of Kenya's 2004 GDP.[158]

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[151] P Goodspeed, Corruption Take US $148B, National Post (Canada*)* 4 July 2005.
[152] G Phombeah, Moi's Legacy to Kenya *BBC News* 5 August 2002.
[153] Corruption Costs Kenya US $ 1 billion a year, *BBC News* 30 May 2003.
[154] Phombea op. cit
[155] Goodspeed op.cit
[156]Phombea op.cit
[157] Goodspeed op.cit
[158] CIA World fact book (online) www.cia.gov/cia/publications/factbook/geos/ke.html

Kibaki and the asset recovery

President Daniel arap Moi hung onto power resolutely and without any serious challenges, even after he allowed nominally multi- party elections to resume in 1992.[159] But this all changed in 2003. Mwai Kibaki was voted into office in a landslide,[160] under the banner of NARC. In the euphoric post Moi mood encapsulated by the NARC slogan "Everything is possible without Moi"[161] Kibaki made rooting out corruption a cornerstone of his administration and all seemed very promising to the Kenyan citizens who thought that the recovery process would be a walk over only to be disappointed. Kibaki set about revamping the 'toothless watchdogs'[162] that had sufficed as anti-corruption agencies under Moi and passed two grafted busting bills[163]. In one fell swoop he fired 6 out of the 12 man Appeal Court, 17 out of 44 High Court judges and 82 of the country's 254 magistrates.[164] Impressed donors resumed aid and the World Bank, IMF and TI pledged their support to help him root out corruption.[165]

As a government official would later comment. "The Narc Government undertook to deal with corruption in the past and with it came 'Asset recovery'".[166] Early investigations into corruption during the Moi regime revealed indications of wide scale looting of the public treasury, and recovery of this money came to feature prominently in anti-corruption efforts. In an attempt to track down some of the country's lost wealth, Kenyan anti-corruption officials hired Kroll Associates, a US- based business investigation and

[159] A Harding: Analysis Kenya's New Democratic Movement, *BBC Analysis*29 December 2002.
[160] Ibid
[161] Kenyans jeer at President's exit, *Mail and Guardian* 17 April 2003.
[162] Creating a toothless watchdog against official corruption, *African Analysis* 402, 31 July 2003 p 46
[163] Kenya Enacts Graft-Bursting law, *Mail and Guardian* 17 April 2003.
[164] Dirt out, Cash in: Kenya Corruption and the IMF, *The Economist* 369 (8352) 29 November P76
[165] Staff Writer: Corruption worth US Billion disclosed in Kenya, Afro *News* 16 December 2003.
[166] P Mwakio, State changes tune on looted billions abroad, The East African Standard 19 May 2005.

risk Consultancy Company.[167] Kroll has a history that includes tracing the illicit accounts of Saddam Hussein and other dictators, and has tracked down the terrorists' funds of Osama bin Laden.[168] Within a few months of its employment Kroll disclosed "illegal transactions by state officials worth more than US$ 1 billion, almost one tenth of GDP.[169] The focus of their investigation was the Goldenberg affair, a giant scandal that emerged in the early nineties and led to severe macro-economic destructions.

The Goldenberg Affair

The Goldenberg Affair and its related schemes ripped out in broadening circle of increasing complexity, spawning scams and insidious rip-offs.[170] That led to the near-collapse[171] of the Kenyan economy. The core scheme began in the early nineties. While the government was running an export compensation scheme to promote export diversification and gain much needed foreign exchange.[172] During this time, a relatively unknown Kenyan businessman named Kamlesh Pattni presented the government with a scheme to provide the country with much – needed foreign revenue.[173]

In return for a monopoly on gold and diamond exports and government compensation of 35 per cent – 15 per cent higher than the capped norm- on his exports, he maintained that he would remit US$ 50 million annually to the Central Bank of Kenya.[174] This was a

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[167] Staff writer, op. cit
[168] The World of Kroll: From Checking out Saddam to Football Managers. *The Guardian* Saturday 31 January 2004.
[169] Staff Writer, op.ct
[170] Fool's Gold, TI-Kenya Reports on Export Compensation Schemes, *TI-Kenya* 24 February 2004 p.8
[171] Kenya Seeks to Unravel Fraud Scandal, *Mail and Guardian* 19 June 2003
[172] Fool's Gold, Op cit p4
[173] P Warutere, The Goldenberg Scandal, *The Nation* 26 February2003
[174] Ibid

strange proposal considering that the legitimate gold industry in Kenya is tiny and informal, and small alluvial deposits in a few areas in the west of the country produce no more than 100kg of gold a year.[175] The proposal was accepted, and what then transpired was an audacious scam that would be farcical, had it not been so effective. Without examining the bureaucratic and financial elements of the scam, Pattni submitted export compensation documents for exports to companies abroad that did not exist to show that Pattni received in export compensation. Yet for all their obvious falsity, each time concerns arose, they appear to have been steam rolled from above, and the compensation[176] claims were honoured. Thus Kamlesh Pattni and complicit government officials made a fortune out of the scheme.

Kroll was able to trace US$ 1 billion worth of foreign assets directly linked to Goldenberg. This included shares in London hotels and funds generated through foreign exchange transactions at leading international banks, including Citibank and Union Bancaire Privee in Switzerland- both of which were also implicated in the laundering.[177] Rather than go indirectly after the money Kibaki ordered an inquiry into the affair. Kibaki aimed to unravel the scandal and have its findings serve as groundwork for future prosecution against the individuals involved. During the commission, Moi himself was consistently the elephant in the courtroom[178]. Pattni implicated Moi in no uncertain terms, claiming to have taken money to him in briefcase.[179] Additionally Moi's son

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[175] Fools Gold op. cit p.9
[176] Ibid
[177] W Wallis, Kenya: Officials, Banks in $ 1 billion Corruption Probe. *Finance Times* 15 December 2003.
[178] D Taylor, Moi casts a long shadow over Goldenberg Commission *Inter Press Service* 18 February 2005.
[179] Marathon Kenyan Graft Inquiry ends, *Mail and Guardian*, 10th Feb 05.

Gideon and step daughter June were implicated.[180] Moi denied these allegations yet refused to testify to the commission[181].

The Kenyan High Court ordered Moi and other influential Kenyan African National Union (KANU) ministers who were implicated to testify to the commission, yet this was overturned by the Court of Appeal, amid allegations that the courts of appeal judges were not entirely impartial.[182] The commission adjourned indefinitely to decide on the way forward.[183] When it is resumed, its credibility was dented and the message that certain people were still untouchable had already been sent. The commission's report was finalized and released sometime in 2005. It had been delayed numerous times owing to apparent "attempts by interested parties in both past and present governments to influence the findings of the Goldenberg Commission[184] With allegations of tampering even before the report had been released, it would appear that little will be gained from it, least of all the recovery of some of the stolen assets.

Loss of political will

The apparent failure of the Goldenberg Commission was part of a collapsing of the euphoric anti- corruption motivation that surrounded Kibaki's election victory. In the same week in February 2005 that the Goldenberg commission was wrapping up its inquiry, John Githongo the man appointed to lead the anti-corruption battle, resigned. John Githongo was head of TI-Kenya and a member of the TI Board before being

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[180] Ibid
[181] D Taylor op cit
[182] K Ngotho, Waiting for Goldenberg, *The Nation* 26 June 2005.
[183] Kenyan Scam Inquiry Suspended Nairobi, *Mail and Guardian* 30 November 2004.
[184] Ngotho, op. cit

appointed the first permanent secretary for Governance and Ethics in the president's office and leading the campaign to stamp out corruption.[185] Githongo tendered his resignation by fax from London, giving no official reasons for his resignation, which was accepted almost immediately other than stating that he was no longer able to serve the government of Kenya.[186] Gladwell Otieno, who succeeded Githongo at TI-Kenya, added that Githongo was in great personal danger[187] at the time of his resignation.

John Githongo's resignation came on the back of renewed criticism by the British High Commissioner, Edward Clay, who the year before had accused Kenyan officials of 'vomiting on the shoes'[188] of donors. The week before John Githongo's resignation, Clay handed President Mwai Kibaki a dossier with information on twenty corruption scandals that had occurred since the NARC government came to power.[189] Adding to the forbore, Kenyan academic Peter Kagwanja of the International Crisis Group alleged that grand corruption had not only diminished in Kenya, but had increased since Kibaki had come to power.[190] He added that "Githongo was seen as the best person to root out corruption. His exit signifies the government's object failure to do so.[191]

Although the NARC government made some attempts at damage control, it was clear that their credibility was irreparably tarnished. While the anti-corruption campaign has continued in Kenya, it seems that in reality it has failed, and with it all hopes of

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[185] Xan Rice, Anti-bribery chief gives up in land of greased palms, *The* Times UK, 9 February 2005.
[186] Kenya's anti-corruption Tsar quits, *Mail and Guardian*, 8 February 2005,
[187] Rice, op.cit
[188] E Clay, Text of Speech to Kenyan businessmen, 14July 2004 http://news.bbc.co.uk
[189] Kenyan government comes under fire over official corruption, *African Times* 18(4), 15-28 February 2005.
[190] Kenya's anti-corruption tsar quits op cit
[191] Ibid

repatriating Kenya's looted wealth have currently evaporated. As more time passes, it is less likely that money will be traced and funds returned, making the reform and restitution of the Kenyan asset recovery campaign an urgent undertaking.

Adoption of legislative measures to combat corruption

The legislative framework is the starting point in the fight against corruption. The framework is important in that it provides the basis for identifying the constituents' elements of corruption to be proven in a court of law.

a. The enactment and enforcement of criminal laws, which effectively deal with corruption
b. The adoption of legislative mechanisms and procedures for the public to submit complaints related to corruption, including the protection of witnessed and whistleblowers.[192]

Generally Kenya has made good progress with adopting legislative measures to combat corruption. The government under President Kibaki enacted new legislation called the Anti-Corruption and Economic Crimes Act of 2003 to provide for the prevention and punishment of corruption as well as economic crimes development are positive and serve to demonstrate the commitment of a country's combating corruption. The fight against corruption needs more than just a good legislative or criminal justice framework. There should also be strong political will on the part of

[192] George Saitoti op.cit p. 247

the government to ensure that no offender escapes the law regardless of position or status in society.

Unfortunately, the courts tend not to entertain cases of corruption involving high ranking government officials or ruling party officials who have access to state resources and who can influence decisions by virtue of their positions.[193] In Kenya, assessing the political will is not easy, given the relative youthfulness of the ruling coalition that replaced KANU. Yet some of the persons who had in the past been accused of corruption are still in government, which gives the citizenry a sense of hopelessness. The changes that have been made to the legislatives framework, however, suggest that this government has stronger commitment to fight corruption than its predecessor.

Transparency and accountability in the management of public affairs

Transparency leads to predictability of the existence of rules and regulations and public officials' adherence to them, making it possible for the public to know what to expect in any given situation, and thus to know when public officials may have breached their own rules. In includes access to information by the public. Most importantly, accountability requires public entities ultimately to respond to peoples needs and places an obligation on a government to explain to the citizenry the basis upon which decisions are made.[194]

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[193] George Saitoti op.cit p.264

[194] George Saitoti op. cit p.268

Transparency is imperative in the fight against corruption because it makes it possible for the public to monitor the actions of office bearers in relation to rules and regulations. This, therefore, obliges officials to be accountable for whatever actions and decisions they take. To measure accountability, two indicators must be implemented namely:

a. The existence of budgetary and financial management frameworks/ systems as well as adherence thereto.
b. Transparency in producers for public procurement and the procedures and the promotion of this by the government.

Although efforts have been made to address the issue of transparency in Kenya, the country has inherited a unique problem of inadequate technical manpower. There is, therefore, an urgent need for this country to address this problem in order to meet its commitments. While the political regime inspires hope for the country, only time will tell whether the government's promises will be translated into practical policy actions.

Administrative reforms and codes of good practice

Civil service reforms are key to addressing some of the causes of corruption, underpaid, overworked and de-motivated civil servants are breeding grounds for corruption. However, civil services reform goes beyond just the working conditions of civil servants. It includes reforming civil services institutions themselves, with the aim of making them

perform their functions better and more efficiently. [195] The following indicators were used in reviewing administrative reforms and codes of conduct: -

a. The simplification of government systems and procedures
b. The establishment of merit based recruitment and remuneration for employees
c. The establishment of effective revenue collection systems
d. The declaration of assets by public officials.

Public participation and accountability

Kenya called upon to allow the media access to information in cases of corruption and related offences, on condition that the dissemination of such information does not adversely affect the investigation and the right to a fair trial. This recognizes the importance of an independent media used to evaluate the performance of the countries under review in promoting public participation. This can be enhanced by the involvement and participation of civil society in formulating and monitoring anti-corruption strategies. In addition, access to information and the protection of freedom of speech and that of the press is a pre-requisite. It worked slowly to erode humanistic value and impoverished human lives. [196]

Kenya has faced many problems is combating corruption in the past. Since coming to power, the NARC government has reconfirmed its commitment to fighting corruption and improving transparency in the management of financial information and statistics to

[195] George Saitoti op cit p.264
[196] Joel D Barkan and John I Okumu (1984) op. cit p.118

ensure good governance. The new government was also investigating the extent to which acts of corruption perpetrated under president Moi's government had harmed the economic affairs of the state following the announcement by the Minister for Planning that Kenyan had lost more than US$ 9 billion in last decade owing to corruption and the mismanagement of state funds.

The NARC government subsequently constituted teams to investigate the financial management in eight local authorities. All these are good signs of the new government commitment. However, caution should be exercised in praising the government, given the mammoth challenges that lie ahead. A crucial dimension in Kenyan conflict was the aspect of economic injustice. The country witnessed economic mismanagement and mega-corruption that stemmed from government misuse of its institution and political power. Added to this were the repressive legislation and systematic violations of individual rights that provided the broad basis of structural violence to Kenyan society.

Kenya on the other hand, attained its 'independence' from Britain in 1963 and has, in sweeping terms generally avoided overt armed conflict as compared to neighbours such as Somalia, Ethiopia, Uganda and Sudan. The intervening decades after Kenya's independence, however, pointed to a deepening sense of economic and political dilemma. It led to the looting and squandering of the country's resources and the virtual silencing of its people. The Kenyatta and Moi regimes both created government structure that denied citizens their basic democratic rights and kept them perpetually subordinate.

Kenyatta, a charismatic leader, commanded broad respect and loyalty at the time of independence.[197]

Legislation on lending and borrowing in Kenya

External Loans and Credit Act (Cap 422) gives the Minister of Finance power to negotiate the terms and conditions of external loans and credits. The Law requires the Minister for Finance upon conclusion of new borrowing to report to Parliament details on new borrowing. Guaranteed domestic and foreign borrowing is contracted under the Guarantee Loans Act (Cap 461). Parliamentary approval required before guarantee is issued.[198] The Internal Loans Act (Cap 420) governs direct Government borrowing from domestic sources. Government borrowing from the Central Bank of Kenya is governed by the Central Bank of Kenya Act (Cap 491) that pegs the ceiling of such borrowing to 5 per cent of the most recent current audited Government revenue accounts. Currently, the overdraft limit is Shs 9 billion to finance resource gaps: Public debt as at end 2005 stood at Kshs 730 billion. It is composed of External debt at Kshs 428 billion (35per cent of GDP) and Domestic debt at Kshs 302 billion (24per cent of GDP).

Kenya has taken steps to lessen its debt burden in order to release resources for its development programs. It has implemented sound economic and structural reforms and fostered development of well-functioning government securities (Treasury Bills and Bond) market. This will sought debt cancellation on bi-lateral basis. It has also

[197] Joel D Barkan and John I Okumu (1984) op. cit p.117
[198] Jacinta Mwatela, Acting Governor Central Bank of Kenya: Lecture on Roles and Functions of CBK: National Defence College (K) on1 9 May 2006

rescheduled debts through the Paris Club and London Club. The purpose is to close the resource gaps. It is a form of financial assistance without "new money".

Currently implementing Public Debt Reforms to ensure both the level and the rate of growth of Kenya's public debt are fundamentally sustainable over time and can be serviced under a wide range of circumstances at minimum cost and risk. It seeks deeper debt relief on a bi-lateral basis to release resources to pro-poor programs in the Economic Recovery Strategy framework. In projects that cannot be financed by these types of creditors, external borrowing will be contracted from internationally credit rate banks and financial institutions.[199] The debt portfolio will be reviewed and restructured to ensure debt servicing costs are kept at minimum. Domestic borrowing and monetary policies will be closely coordinated so as to ensure that the government raises required resources from the financial market without raising interest rates and crowding out the private sector. New foreign borrowing must have a grant element of at least 35 per cent and will be used to finance pro-poor development programmes.

The Medium Term Expenditure Framework (MTEF) Budgetary Process in Kenya

Links between the development and recurrent budgets tended to be weak or non existent. Budget process therefore lacked credibility and provided little basis or incentive for sound planning. The Government of Kenya in June 2000 introduced the Medium Term Expenditure Framework (MTEF), as an instrument and process to reform its public expenditure management system. The MTEF was introduced in order to link policy-

[199] Jacinta Mwatela, Acting Governor Central Bank of Kenya: Lecture on Roles and Functions of CBK: National Defence College (K) on1 9 May 2006

making to planning and budgeting, maintain sustainable fiscal discipline, facilitate expenditure prioritisation and encourage better use of resources to achieve desired outcomes at the lowest cost possible.

An MTEF process rests on three pillars. First is the top-down approach which consists of defining aggregate resources available, establishing sectoral spending limits that fit government priorities and communicating the spending ceilings to ministries/departments. Second, a bottom-up approach that consists of formulating and costing sectoral spending programmes for the planned period within the given sectoral spending ceilings. Third level consists of top-down resource envelope estimation and a bottom-up estimation of the current and medium-term costs of existing policies. Matching of the two in the context of the annual budget process; and involves rolling over this exercise every year by incorporating policy changes.

If successfully applied, it can improve macroeconomic balance by developing a multi-year resource framework. This will assist in improving resource allocation between and across sectors and improve predictability of funding for line ministries. Based on the overall resource envelope derived from the fiscal framework, the allocation of resources will be based on the ERS priorities. The MTEF sectoral allocation will feature on increasing share of resources destined for the core poverty reducing areas of education, health, agriculture, and physical infrastructure.

CHAPTER FIVE

CONCLUSION AND RECOMMENDATIONS

Conclusion

Infrastructure is key to rapid agricultural development and lack of roads prevents subsistence farmers from accessing markets and also hinders agricultural productivity. Thus, quality infrastructure at reasonable costs contributes to growing and maintaining an economy's reputations as an attractive location for investment will facilitate regional integration [200] Kenya has been trying different approaches to address the failing infrastructure utilities. These include decentralizing to local government, private sector participation, regulatory reforms, and community development. Infrastructure has often been provided by the public sector due to the fact that such developments are often large scale requiring immense amount of capital. They are often natural monopolies and often politically sensitive in that the government is held accountable for prices charged and service outcomes.

Through the 1980's and 1990's various changes were attempted by Kenya to improve efficiency in infrastructure through increase of private sector involvement. It also deregulated the infrastructure sector to make them more open to new entrants and improve their competitive characteristics by introducing specific efficiency incentives and performance targets into parts of infrastructure that are still provided by the public

[200] GoK (2001) *Report of the Sector Working Group on Physical Infrastructure,* Ministry of Planning and National Development p.1

sector enterprises. This included the introduction of pricing policy into infrastructure services.[201]

Kenya's domestic scene has over the years made considerable investment in order to increase the quality and quantity of the existing infrastructure and utilities. However, in the last decade, the quality of some of infrastructure facilities and utilities has fallen below acceptable standards contributing to high cost of doing business in the country. The roads are dilapidated. The main road network is currently in deplorable situation, while the rural road network remains uneconomical for efficient and competitive business ventures. The other supporting modes of transport such as railway and maritime are performing below capacity. This has constrained growth, productivity and profitability margins in production sectors of the Kenyan economy.[202]

In Kenya, significant steps are being undertaken to revitalize and improve efficiency in infrastructure services and to address the deplorable state in service delivery and ensure that the sector plays its role in supporting economic growth. The current government policy on infrastructure spelt out in the Economic Recovery Strategy for Wealth and Employment (2003 -2007) identifies infrastructure as a key pillar in achieving economic recovery and poverty reduction objectives. The overarching objective for the infrastructure sector is to provide efficient, affordable and reliable means for sustainable economic growth through rehabilitation, construction, improvement and effective management of the existing infrastructural facilities. This has led to inadequate funding

[201] Ibid pp.3-4
[202] GoK (2000) *Economic Survey Central Bureau of Statistics*, Ministry of Planning and , National Development Nairobi

for infrastructure development; inadequate budgetary provision for regular maintenance and high cost of infrastructure development.[203]

The government must continue to implement a broad range of policy reforms and other measures aimed at increasing its efficiency and competitiveness. These reforms have included concession, divestiture, commercialisation of management and operations, privatisation, sub-contracting of certain non-core services, introduction of competition, tariff liberalisation in key utilities, financial and management restructuring of state enterprises providing infrastructure services.

Infrastructure remains central to achieving the MDGs. The sector comprises of roads, railway, air, water, pipeline transport and communication. The sector is one of the fast growing in the Kenyan economy. The sector constituted 10.3 per cent of the GDP in 2004. The sector grew by 9.7 per cent in 2004 compared to 4.9 per cent in 2003. Post and telecommunication sub-sector grew by 12.4 per cent in 2004.[204] Kenya has liberalised VSAT services and implemented tax incentives for computer and software. The ongoing privatisation of Telkom Kenya will turn around the performance of the corporation with the infusion of capital for network growth and modernization

Development and maintenance of physical infrastructure on a sustainable basis is a key prerequisite for rapid and sustainable economic growth and poverty reduction as they influence production costs, employment creation, access to markets, and investment.

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[203] GoK (2000) *Economic Survey Central Bureau of statistics*, Ministry of National Development

[204] GoK (2005) *Achieving Millennium Development Goals in Kenya* , Ministry of Planning and National Development p.13

Modern infrastructure and utilities is viewed as critical to lowering the cost of doing business and increase competitiveness of any country's products in the international market. The cost of doing business is to a large extent influenced by the state of infrastructure. Kenya must develop its infrastructure so as to realize economic growth and stop relying on the IMF and World Bank to develop.

The success of the socio-economic and environmental transformation pursued by the government is to a large extent dependent on the performance of the energy sector as an economic infrastructure. There is therefore need to mainstream energy in all national development strategy frameworks including budgeting and utilization of available investment resources which include planning for targeted energy specific MDG interventions. Accessibility and the cost of energy have significant impacts on economic activities in both formal and informal sectors. Consequently, high energy costs impact negatively on employment and wealth creation[205]

RECOMMENDATIONS

The IMF-initiated reforms discussed in this paper address some of the principal critiques of IMF activities. However, some major concerns remain. Prominent among them is the need for the IMF to devise programs, on one hand, which meet the needs of its borrowers, while retaining, on the other hand, the confidence and support of the major countries that provide the hard currencies, which fund its operations. In many cases, the gap between the goals and expectations of the borrower countries and the donor countries is great. For example, many of the major countries, which finance the IMF's operations, subscribe to the basic

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[205] GoK (2005) *MDGs Status Report for Kenya,* op.cit p.11

concepts embodied in the "Washington Consensus," and make them the core policy requirements for IMF assistance.[7] Many borrower countries, by contrast, believe that these policies are too narrow and lack sufficient appreciation for their real needs and the limits of their political and economic situations. As developing countries are now the primary recipient of IMF assistance and policy advice, divergence between lenders and creditors has grown, with increasing protests against the IMF in general and specific IMF loan programmes.

To address these problems, both institutional and policy reforms have been proposed and some have been implemented. The IMF has created two internal groups to conduct research and explore issues in International Capital Markets department and the Capital Markets Consultative Group. Both groups are expected to deepen the Fund's understanding of the international capital markets, the forces driving the supply of capital, and the constraints these capital flows place on economic policy markers.[206]

Kenya should enhance capital formation which means curtailing current consumption needs and increase savings and investment in capital goods. The essence is to increase capital goods now to expand consumable output in the future. Capital formation applies to both accumulation of tangible goods and intangible goods like high standards of education, and break vicious circles through increased investments. Increased investment

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[7] "The Washington Consensus," a term coined by International Institute for Economics Senior Fellow, John Williamson, in 1989, refers to a set of policy reforms including fiscal discipline, tax reform, interest rate liberalization, a competitive exchange rate, trade liberalization, open capital markets, secure property rights, privatization and deregulation. For more information, see: John Williamson, "What should the World Bank Think About the Washington Consensus," available at [http://www.iie.com/papers/williamson0799.htm]

[206] Global Financial Stability Report, March 2002

in capital equipments increases output and creates employment opportunities. Capital formation will lead to technical progress and provide machines, tools and equipments. This will reduce over-reliance on imports of all types through building of import-substitution industries. It will free Kenya from the burden of foreign aid, reduce the burden of foreign debt and make it self-reliant. It will raise the level of national income instead of increasing in the volume of savings through financial and credit institutions.

The government must focus on agriculture because Kenya's population is mainly rural. About 80 per cent of the population live in the rural area and derive their livelihood largely from agriculture. But more important is the fact that 56 per cent of the population live below poverty line and over 80 per cent of these live in the rural area. Evidently, the growth in the economy is closely correlated with growth in the agriculture sector. In fact in the last two decades; the overall economy barely grew, following a sharp and abrupt decline in agricultural growth. Agriculture is also given prominence because the majority of Kenyans are food insecure (about 50.6 per cent). The incidence and prevalence of food insecurity is even severe in ASALs due to lack of adequate resource endowment as US$ 40-65 million annually go on famine relief.[207]

Implementation of monetary and fiscal policies

Monetary and fiscal policies are important tools for mobilizing resources for economic growth. The twin policies will accelerate the rate of economic growth through fiscal discipline and an appropriate monetary policy. They are regulatory instruments and must

[207] GoK (2004) *Strategy for Revitilaising Agriculture 2004-20014*, Ministry of Agriculture and Ministry of Livestock and Fisheries Development p.15

be applied mainly to ensure macroeconomic stability. Moderate domestic borrowing is to avoid higher interest rates that could crowd out the private sector investments and dampen the growth of the economy. This would provide the fiscal space to facilitate a restructuring of expenditures in favour of priority in social and economic sectors.

Monetary policy should target achieving low rate of inflation and a comfortable level of international reserves. It must provide sufficient credit to the private sector by limiting domestic borrowing and maintain a flexible exchange rate policy to bolster external competitiveness to achieve a sustainable external current account position. This is critical for economic and political development of Kenya. Due to lack of skilled manpower in Kenya, we import finished goods sometimes valued at four times that of the same raw materials sold to developed countries. In Kenya, 1 kg of coffee was valued at US $ 1.2, and when processed was valued at US$ 18. This implies that for 1 kg Kenya exports, we equally donate US$ 16.8 plus the jobs that go with processing of the coffee. This explains why the current debate on international trade is focusing on removing trade imbalances and allowing finished products from Kenya to access markets of developed countries.[208]

Population growth is an asset in countries that are wealthy, with abundant capital and labour scarcity. But in capital-scarce and labour abundant countries like Kenya, population growth will retard investment by diverting more resources to consumption rather than to savings for investments in the future. This strains natural resources leading to environmental degradation, especially where the poor majority competes for arable

[208] Romano Kiome, Permanent Secretary Ministry of Agriculture (Kenya): Lecture on Agriculture and Rural Development: National Defence College (K) on 9 May 2006

land for agriculture. It also strains national budgets leading to low domestic investments due to increased demand for social facilities such as hospitals, water, education, and housing. Standards of living deteriorate and slums emerge as the only housing facilities affordable. In order to strike a balance Kenya must regulate production, distribution and consumption. This can be done through physical, monetary and fiscal controls.[209]

Kenya should maintain an overall framework of minimum budget deficits to ensure that debt/GDP ratio declines significantly in the medium term. This will promote development of efficient and liquid market for government securities. It is recommended that the government sets up a Debt Management Office at the Ministry of Finance to manage public debt according to best practice as per IMF/WB Guidelines for Public Debt Management. It carries out consolidation of debt management functions currently scattered in various departments of Ministry of Finance and Central Bank of Kenya (CBK). This will create capacity building through training and recruitment supported by staff retention policy that will establish comprehensive and reliable Public Debt Database. Development of debt policies and strategies should be consistent with the economic reform programmes; and develop a legal and institutional framework to guide the operations of the Debt Management Office.[210]

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[209] Romano Kiome, Permanent Secretary Ministry of Agriculture (Kenya): Lecture on Agriculture and Rural Development: National Defence College (K) on 9 May 2006

[210] Jacinta Mwatela, Acting Governor Central Bank of Kenya: Lecture on Roles and Functions of CBK: National Defence College (K) on1 9 May 2006

Foreign Trade in Economic Development

Generally, foreign trade promotes economic growth. Kenya will gain through trade and increase national income, which in turn raises the level of output and the growth rate. This will break the vicious circle of poverty and promote economic development. It also widens market and induces investments. Foreign trade will boost demand and enhance the opportunity to produce more products for export. It also boosts employment, domestic savings and investment. The expanded market results in efficient resource allocation and utilization thus increasing employment, reducing underemployment, and boosting both domestic savings and investments. Another method is to treat the aid flow as part of an over-all trade arrangement or finance only those commodities and projects where donor country posses a decided advantage in tendering the specified items. The cost increases when the recipient country is forced to get capital goods.

Developing manufacturing and Industrial sectors

Since the mid-1980s, Kenya has been under increasing pressure to strengthen its industrial competitiveness. The pressure is attributed to a number of factors including the on-going economic globalization, the country's entry into various regional integration arrangements that require opening of the economy to the regional partners, and the general liberalization of the economy to both domestic and external forces. In addition, the Government of Kenya (GoK) declared its vision of becoming a newly industrialized country (NIC) by the year 2020. To achieve this goal, it is imperative to radically increase the country's competitiveness and to expand its export markets.[211]

[211] GoK (1996) Sessional Paper No 2 op. cit

Kenya's industrialization process began at the start of this century under the British colonial rule. The pace of industrialization was quickened after independence in 1963, as the country embraced an important-substitution strategy that was then popular in a number of developing countries. Since then, a number of incentives have been used to encourage manufacturing activities in the country, including protective tariff and non-tariff barriers, tax exemptions and later, special schemes such as export compensation, manufacturing under bond (MUB) and export processing zones (EPZ).[212] These programmes must be encouraged so as to develop the manufacturing sector.

Since the country inherited, one of the strongest industrial bases in the region, the industrial development has been recognized as one of the key sectors in economic development. The policies that were pursued have largely reflected the dominant international viewpoint. Thus, the country's first development plan, 1966-70, laid emphasis on import-substitution as the strategy for the country's industrialization.[213] The strategy was to be implemented mainly through the protection of industries, using tariff and non-tariff barriers, exchange controls and import licensing. Other key elements of the country's industrial policy have been a liberal policy towards foreign investments, the promotion of labour-intensive technologies, greater focus on medium and large industries, and the pursuit of even geographical dispersal of industries, as well as Kenyanization.[214] This would enhance Kenya's industrial capacity so that it does not depend on donor aid.

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[212] GoK (1996) Sessional Paper No 2 op. cit

[213] Government of Kenya (1996) op.cit

[214] Arne Tostensen and John G Scot: Kenya: Country Study and Norwegian Aid Review, (Fantoft, The Chr Michelsen Institute 1991) p.109

Macroeconomic policies also affected industries in several ways. First is economic stability, which is the basis of sound investment decisions. Fiscal and monetary policies, together with trade and exchange rate policies were implemented to achieve high levels of employment and price stability. Price controls were also used extensively up to the mid-1980s as a key policy instrument. It also discouraged domestic firms producing import substitutes from seeking lower-priced or higher-quality inputs in international markets, resulting in high average unit costs. Price controls also had the effect of making producers shift to the production of commodities whose prices were not controlled. These negative effects of the price controls policy on the incentives of the local manufacturers were further exacerbated by exchange controls through import licensing.

In recognition of the burdens imposed on the economy by these policies, the government, in the Sessional Paper No. 1 of 1986, proposed an industrial strategy that was to be driven by the private sector relying more on market-based incentive structure. The policy, among others, emphasized the need to reduce the importance of imports licensing as a protective shield for local manufacturers and to gradually lower tariffs, in order to expose domestic firms to competition for greater efficiency.[215] The 1989-93 National Development Plan, industrial policy continued to emphasize the need to create incentives necessary for the emergence of a successful manufacturing sector, one not based merely on import substitution. The industrial development vision projected in the plan talked of adopting a strategy that would lead to the establishment of iron and steel, tool and die, and a machinery industry, as well as biotechnology and other high technology industries. It is

[215] Government of Kenya (1986) Sessional Paper No 1 op.cit

recommended that these plans are upheld to avoid draw backs that will return Kenya to the dependency syndrome from the Bretton Woods Institutions.

The early 1990s saw the beginning of dramatic liberalization of the economy and an even stronger focus on industrialization. In 1997, the government produced a key document on industrial policy, the Sessional Paper No. 2 of 1999 on the 'Industrial transformation to the Year 2020'. The document highlighted some of the major constraints to industrial expansion and proposed a broad strategy for industrialization. The key elements of the strategy included the promotion of political and social stability, macroeconomic stability to build business confidence, more efficient and diversified primary production as a base for economic growth, increased investment in human resources and rehabilitation of the physical infrastructure. This would foster greater and genuine partnerships, and increase the proportion of resources allocated to technology development and management.[216]

The labour market

The labour force in Kenya, estimated to consist of 14 million in 1998, is rapidly expanding at a rate of close to half a million new entrants per year, due to continued high population growth and an age structure of more than two thirds being less than 40 years old.[217] The levels of unemployment and underemployment have remained high for most of the last two decades. Open unemployment is estimated to be about 25 per cent and underemployment is around 20 per cent.[218] Retrenchment and poor performance of the economy have

[216] Government of Kenya (1996) op.cit
[217] Arne Tostensen and John G Scot: op. cit p.298
[218] Government of Kenya (1996) op.cit

aggravated the employment problem in the country in the 1990s; thus affecting workers in both, the private and public sectors.

Generally, the Kenyan labour market has been characterized by relatively low wages, especially among unskilled and semi-skilled workers. Several factors have contributed to this situation. First, the government purposely pursued a policy of low wages aimed at making the country attractive to foreign investors. Second, the trade union movements in the country has been largely ineffective as an instrument for improving real wages, partly because of the government's close control over the affairs of trade unions, and partly because of high levels of unemployment, which made strikes risky for workers. Third, agriculture tended to subsidize industrial workers though remittances, so that workers were not wholly dependent on their industrial wages.[219]

In the early 1990s, considerable liberalization of the labour market took place, largely as a result of the structural adjustment programme the country was implementing. Some of the reforms that affected the labour market included the relaxation of wage guidelines, which allows trade unions to negotiate for better wages with employer organization largely based on labour productivity and performance of the enterprises. The redundancy laws, had made it difficult to declare workers redundant without having to obtain approval from the Ministry of Labour and Manpower Development. On the whole, these policy reforms are expected to assist the manufacturing industries in gaining competitiveness and must be supported by the Government of Kenya so as to register a positive economic growth.

[219] Arne Tostensen and John G Scot, op .cit p. 291

The capital market

Capital costs are, as the present study shows, decisive factors for competitiveness. In particular, the distortion of the market price, relative to the shadow price, of capital can either cause additional costs or can act as a subsidy. The banking sector has been dominated by two multinational, and two government-owned, banks. The two government-owned banks have been gradually selling an increasing proportion of their shares to public, although the government influence and presence in the two institutions are still strongly felt.[220] The financial and capital markets have undergone considerable reforms in the 1990s, including liberalization of interest rates and foreign exchange markets Due to the problems associated with accessing bank credit facilities, a large proportion of the Kenyan firms rely more on self-financing in terms of retained earnings and supplier credit facilities, which should attract low interest rates and do not require the type of collateral demanded by the banking institutions.[221] The reforms carried out, especially in the last six years, have removed some of the above constraints, notably the shortage of foreign exchange and a host of government controls that were a disincentive to investors. But most of the other constraints continue to be a source of concern for the Kenyan business community.

Control in public expenditure

Inability to control government expenditures has been one of the major weaknesses in Kenya's fiscal management in the last decade. One writer on Kenya's fiscal policy commented that "the heart of Kenya's fiscal problem is its inability to control expenditures,

[220] George Saitoti (2002) op.cit pp.10-11
[221] George Saitoti (2002) op.cit p.13

not its inability to generate sufficient revenues".[222] Consequently, the budget deficit should not be allowed to grow dramatically and this should be financed in part by domestic and in part by external borrowing.

The inability to control expenditures was due in part to the structure and composition of public expenditures and partly due to lack of discipline in expenditure allocation and execution. The main consequences of this failure from the industrial sector and its competitiveness can be seen as two fold: shortage of foreign exchange and its rationing through the licensing system, and the overcrowding out of private investment due to the rising cost of credit. Thus, whereas the overall macroeconomic policy did not have direct effects on the manufacturing sectors, their effects came indirectly through their impact on the balance of payments, the direction of trade policy and the cost of capital.[223] The government should therefore control its expenditure and reinforce existing fiscal policies so as to generate sufficient revenue and avoid depending on donor money.

Infrastructure Development

Several recent studies show that inadequate and poorly maintained infrastructure has emerged as a major impediment to Kenya's industrial growth and other economic activities. A study, which covered more than 200 industrial enterprises in the country's main industrial towns, observes: "The poor state continues to be a serious impediment to business activity and manufacturing".[224] According to the firms interviewed during the study, the state of the country's infrastructure especially with regard to electricity, water,

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[222] Rolph van der Hoeven and Fred van der Kraaij (1994) op.cit p.200
[223] Rolph van der Hoeven and Fred van der Kraaij (1994) op.cit pp201-203
[224] Arne Tostensen and John G Scot, op cit p.161

freight transport, port-handling facilities, telephones, waste disposal and security had deteriorated substantially, compared with a few years earlier. One of the consequences of the government's failure to effectively provide essential infrastructure is that a large proportion of the enterprises have been forced to engage in costly self-provision of various facilities.[225] This self-provision of essential facilities had raised the firms' operational costs, thereby reducing their overall competitiveness.

The analysis reveals that Kenya had a comparative advantage and was internationally competitive in the mid-1980s. This situation has not improved, but seems to have deteriorated, in spite of over ten years of structural adjustment and trade policy changes. If this was only true for profitably and as consequences of decreased protection, then one could consider this as normal for such a transition period. But since it is not even clear that actual protection, as measured by comparison of domestic and international prices, has declined as one would expect, the declining competitiveness must be attributed to increased costs, and we have substantial evidence of this. Competitiveness in the protected domestic market is also weakened due to this cost increases. At present, using the tariff instead of the implicit national report on poverty in about half of the cases, it appears that on average, protection is not reduced in comparison to the mid-1980s.[226]

Given the national goal of transforming Kenya into a Newly Industrial Countries (NIC) by the year 2020, and given the environment of globalization and liberalization trade, it is clear that increased competitiveness must become a major objective and challenge for all

[225] Rolph van der Hoeven and Fred van der Kraaij (1994) op.cit p.204
[226] GoK (1996) Sessional Paper No 2 op.cit

industries. This is true in international as well as in regional markets. The study shows that some of the macroeconomic policies and variables are of crucial importance for the attainment of competitiveness by industries. In particular, low cost of borrowing, a state and well-aligned exchange rate, as well as a sound infrastructure in transport, communications, energy and water supply are a pre-condition for industrial growth.[227]

I recognize the benefits of liberalized trade, but also observe that opening up of the economy is not sufficient to achieve the goals of increased competitiveness and industrial growth. What is needed is a cautious progression of trade liberalization combined with an industrial strategy that recognizes the importance of the pace at which industries can adjust to the changing environment. The study clearly shows that the enactment of liberal trade policy is not sufficient, but must be accompanied by effective enforcement of the trade regime. The recent changes in the trade regime seem to be sufficient to create a level playing field but only if the respective laws are effectively enforced. I observe that several sectors have been adversely affected by the failure to enforce the existing trade policies, which the government has to implement.

The trend of declining Internet rates is a setup in the right direction, but it needs to be further pursued by sound fiscal policies, in order to bring the cost of borrowing to a level that permits industries to make new investments for increased competitiveness. The recent depreciation of the currency has reduced the observed misalignment and often-heard complaint of over-valuation that hurts competitors in international markets. A

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[227] George Saitoti (2002) op.cit p.148

cautious approach to currency depreciation is, however, necessary to prevent new inflationary pressure, which would cancel the gains in competitiveness. Transport and communications are two areas in which industries suffer from substantial extra costs that inhibit their competitive strength. I recognize that some steps are being taken to reduce these problems, but it is urgent to accelerate the pace of such renewal. In addition to improvements in the road infrastructure it seems urgent to further the pace toward privatization of the railways in order to make them again fully functional.

Quality controls and enforcement of standards

There is need for more stringent quality controls and enforcement of standards, in order to ensure that Kenyan producers can compete in exports markets. This is particularly important in the food industries and especially in fish processing, where the ban of exports from East Africa to the European Union has badly hurt the sector. Some sectors require political support as well as regional cooperation in order to allow industries to exploit their natural comparative advantage. Regional integration tends to be successful when intra-industry trade flourishes. Some Kenyan producers may see this as a threat to their traditional export perspectives. But it can also be seen as an opportunity to develop intra-industry trade between the countries of the East Africa region, which would benefit their economic growth.

Currently implementing Public Debt Reforms to ensure both the level and the rate of growth of Kenya's public debt are fundamentally sustainable over time and can be serviced under a wide range of circumstances at minimum cost and risk. It seeks deeper

debt relief on a bi-lateral basis to release resources to pro-poor programs in the Economic Recovery Strategy framework. Government will contract new foreign loans from multilateral and bilateral sources. In projects that cannot be financed by these types of creditors, external borrowing will be contracted from internationally credit rate banks and financial institutions.[228]

It is clear that unless concerted efforts are made by the donor community to meet the resolutions of the Millennium Declaration, then Kenya like any other developing country will not meet the MDGs by the target date. In this regard, Kenya does not expect the donor community to establish a fair and equitable global trading system that is MDGs friendly and more responsive to the development needs of developing countries. Towards this end, Kenya's products should fairly access the developed markets through the removal of non – tariff trade barriers by developed countries. [229]

Sector strategies and priorities as outlined in the Economic Recovery Strategy for Wealth and Employment Creation (ERS) include improvement and strengthening the delivery of existing physical infrastructure facilities. This will promote provision of infrastructure on a cost recovery basis. In addition, there will be investment of financial resources in core and high priority areas that will impact on the poverty reduction. Further, Kenya should facilitate and promote private sector participation. If the above are implemented, Kenya will enhance budgetary provision for completion of viable stalled and on going projects

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[228] George Saitoti (2002) op.cit pp242-243

[229] GoK (2005) *Achieving Millennium Development Goals in Kenya A Needs Assessment And costing Report.* op.cit pp.32-33

as well as clearing pending bills. The sector priorities should include completion of viable on-going and stalled projects and selling of non-viable ones and carry out reconstruction, rehabilitation and maintenance of existing degraded infrastructure, so as to upgrade the levels of service of existing infrastructure. This will provide new infrastructure to disadvantaged areas that have the potential for poverty reduction.

A sizeable number of the public in both the developed and developing countries have strong negative views of the IMF. This tends to encourage and hinder the process of reform by intensifying, polarizing and complicating public and official discussion of these issues. Fundamentally, the IMF is an economic and financial institution. However, many other issues also seem relevant to the issues its programmes seek to address. A challenge for the IMF in future years is to retain a sound financial and economic basis for its operations while also responding to relevant social and political issues. In addition as a member-based organization, the IMF only has relevance and utility if member countries view it as an institution whose policy advice is appropriate and worth implementing.[230]

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[230] George Saitoti (2002) op.cit p.270

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