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# The Developmental Impact of Asian Drivers on Kenya with Emphasis on Textiles and Clothing Manufacturing

*Paul Kamau*[1], *with Dorothy McCormick*[1] *and Nicolas Pinaud*[2]

[1]*Institute for Development Studies, University of Nairobi, and* [2]*OECD Development Centre, France*

## 1. INTRODUCTION

RESEARCH on the impact of Asian Drivers on Africa is fairly recent, with most studies having been undertaken no earlier than 2005. Furthermore, most of these studies have focused on the wider African region by examining impacts on several countries. However, there is consensus that individual African countries are affected differently by the growth of China and India (Jenkins and Edwards, 2005; Broadman et al., 2006; McCormick, 2006; Kaplinsky et al., 2007). Therefore, as the body of research grows, there is a need for country- and sector-specific studies (see Alemayehu, 2006; Goldstein et al., 2006; McCormick, 2006; Stevens and Kennan, 2006). As a response to this research gap, this paper is designed to examine the impact of Asian Drivers on Kenyan textile and clothing manufacturing. The paper utilises four main vectors: trade flows, financial flows, foreign aid and human resource flows.

This paper adds to the literature in the following ways. First, it is a contribution to the young body of literature that examines the impact of the rise of China and India on developing countries. Second, with the exception of McCormick et al. (2006), it is the only other country-specific study that examines the impact of Asian Drivers on clothing and textile manufacturing in Kenya. Third, this paper examines the opportunities and the threats in the

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sector arising from the ascendancy of Asian Drivers through trade, investment, foreign aid and human resource channels.

The paper is organised into six sections. Section 2 examines trade flows between Kenya and the Asian Drivers. Section 3 enumerates the patterns of FDI from Asian Drivers in Kenya and the effects of drastic growth of FDI in the Asian Drivers on Kenya. Section 4 discusses the recent evolution of development aid and the role being played by the Asian Drivers. Section 5 examines political–economic issues between Kenya and the Asian Drivers as well as the concerns about human resource flows. Finally, Section 6 concludes the paper and provides some policy recommendations.

## 2. KENYA'S TRADE FLOWS AND THE EFFECT OF CHINA AND INDIA

Trade between the Asian Drivers and Africa has significantly grown during the last decade, although the impact varies among different countries depending on the relations and commodities involved (Jenkins and Edwards, 2005; Broadman et al., 2006; Kaplinsky and Morris, 2006). While the natural resource-rich countries have gained out of the Asian Drivers' economic surge, the natural resource-poor (particularly those relying on export of textile and clothing) are losing (Zafar, 2007, pp. 10–12). Unfortunately, Kenya is in the latter category: its manufactured products face stiff competition from Asian Drivers in both the domestic and the export markets.

### *a. Kenya's Exports and Imports*

Table 1 shows Kenya's top-10 trading partners in both the export and import trade in 2005. On the export side, the top-10 trading partners accounted for nearly 60 per cent of total exports in 2005; while on the import side, the top-10 trading partners accounted for 68 per cent of total imports. This illustrates how Kenya's international trade is concentrated in just a few countries. Uganda and Tanzania combined account for more than 25 per cent of Kenya's exports in 2005. Notably, the Kenyan exports to these two countries constituted agro-based and industrial manufactured products. The next major export destination is the UK, which absorbed close to 10 per cent of Kenya's exports in 2005. Other developed countries that feature in the list of the 10 major export destinations include the Netherlands, France and the US, and accounted for close to 10 per cent of Kenya's export. With the exception of the US, Kenya's exports to developed countries consist of raw agricultural materials including cut flowers in the Dutch Flower Auction. The US market is different from other OECD markets as close to 90 per cent of Kenya's exports to the US constituted clothing products.

TABLE 1
Top-10 Kenyan Trading Partners in 2005 (Kshs million and % of total exports)

| *Exports by Destination* | | | | *Imports by Country of Origin* | | | |
|---|---|---|---|---|---|---|---|
| | *Country* | *Value* | *% of total* | | *Country* | *Value* | *% of total* |
| 1 | Uganda | 42,545 | 17.1 | 1 | United Arab Emirates | 62,130 | 14.4 |
| 2 | United Kingdom | 23,371 | 9.4 | 2 | USA | 42,493 | 9.9 |
| 3 | Tanzania | 19,887 | 8.0 | 3 | South Africa | 42,305 | 9.8 |
| 4 | Netherlands | 18,316 | 7.4 | 4 | Saudi Arabia | 27,580 | 6.4 |
| 5 | Pakistan | 14,072 | 5.7 | 5 | United Kingdom | 26,134 | 6.1 |
| 6 | Egypt | 8,839 | ***3.6*** | ***6*** | *India* | *24,236* | *5.6* |
| 7 | Rwanda | 7,273 | 2.9 | 7 | Japan | 23,021 | 5.3 |
| 8 | France | 5,086 | ***2.1*** | ***8*** | *China* | *19,764* | *4.6* |
| 9 | USA | 4,518 | 1.8 | 9 | Germany | 15,761 | 3.7 |
| 10 | *India* | *4,000* | 1.6 | 10 | France | 13,883 | 3.2 |
| | **Total Exports in 2005** | **248,198** | **100** | | **Total Imports in 2005** | **430,740** | **100** |

Source: Kenya (2006).

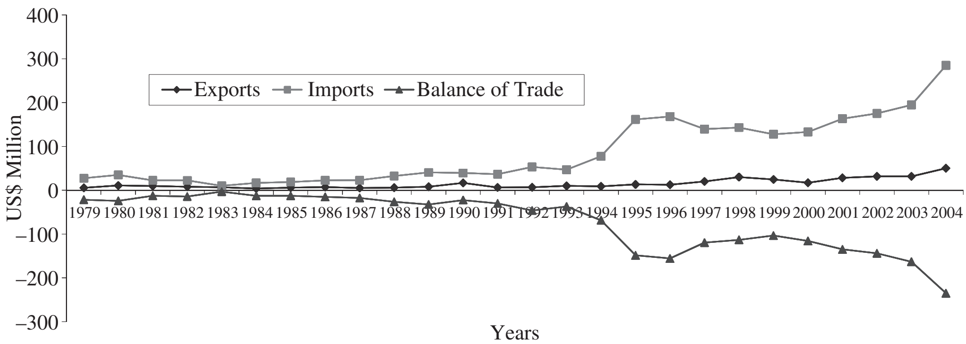
With regard to the Asian Drivers, India absorbs more of the Kenyan exports than China. For instance, in 2001, India and China accounted for 1.601 per cent and 0.016 per cent, respectively; while in 2005, India accounted for 1.638 per cent and China 0.518 per cent[1] (Kenya, 2006). Further observation reveals that in 2005, food and beverages (raw and processed) products accounted for 47 per cent of exports, while industrial products accounted for around 26 per cent (Kenya, 2006). In addition, the share of consumer goods was 21 per cent, while textiles and clothing exports accounted for only 1 per cent of the total Kenyan exports.

On the import side, the picture is somewhat different as both India and China feature in the sixth and eighth positions, accounting for 5.6 per cent and 4.6 per cent of Kenya's imports, respectively. Both China and India appear to have increased their exports to Kenya between 2001 and 2005. In 2001, India accounted for 4.4 per cent, while China accounted for 2.3 per cent of total imports in Kenya. This growth points to the fact that trade between Kenya and the Asian Drivers grew between 2001 and 2005. The prominence of trade between Kenya and the OECD countries is also clear. Five out of the 10 leading countries that Kenya imported from in 2005 were OECD countries, which jointly accounted for nearly 30 per cent of total imports.[2]

[1] In 2001, Kenya's exports were valued at Kshs.147,590 million while in 2005 total exports were Kshs.244,198 million.

[2] The fact that the United Arab Emirates (UAE) accounted for the highest share of Kenya's imports (14.4 per cent) raises questions because the UAE is known to be more of a trading centre than a production centre. Therefore, imports from the UAE could in actual fact be originating from China, India or other Asian countries. This figure therefore needs further investigation.

FIGURE 1
Balance of Trade between Kenya and China, 1979–2004




Source: Government of Kenya, *Statistical Abstracts* (various issues).

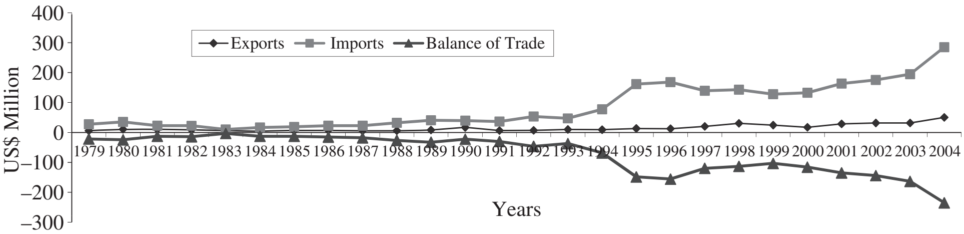
Analysis of trade between Kenya on one hand and China and India on the other shows a growing deficit in favour of the Asian Drivers. Figures 1 and 2 show trade between Kenya and the Asian Drivers during the period 1979–2004. It is clear from these statistics that the trade grew more rapidly during the period 1995–2004.

Kenya's major exports to China include hides and skins, sisal, fibre, coffee, tea, fishery products, horticultural products and scrap metals; while imports from China include textiles, ready-made clothes, shoes, electronics, computer accessories, machinery and equipment, glassware, pottery, iron and steel wire, tubes and pipe fittings. In comparison to other African countries, trade between Kenya and China is small (see Broadman et al., 2006), because Kenya does not have either the oil or minerals that appear to propel trade between China and some other African countries. However, the recent entry of China into the oil exploration and titanium mining industry is a clear indication of the direction of China's trade interests.[3]

Kenya's major exports to India include cashew nuts, dyeing and tanning materials, hides and skins, scrap metal and precious stones, whereas imports from India include drugs, pharmaceuticals, chemicals, machineries, farm tools and implements, textiles, plastics and linoleum products, manufactured metal and steel, transport equipment and accessories, software, electronics, and processed and agro-based products.

[3] In April 2006, during the state visit to Kenya by H. E. Hu Jintao, Kenya and China signed an 'Oil and Gas Exploration Agreement' which gave China National Offshore Oil Corporation (CNOOC) rights to prospect for oil and gas in six offshore blocs in Northern and Southern Kenya. Again on 28 April 2006, a Chinese company, Jichuan Group Ltd, bought about 10 per cent of Tiomin's common shares, injecting Kshs.460 million into the capital of Tiomin, which is involved in the mining of titanium in Coast Province, Kenya (*Daily Nation*, 28 April 2006).

FIGURE 2
Balance of Trade between Kenya and India, 1979–2004



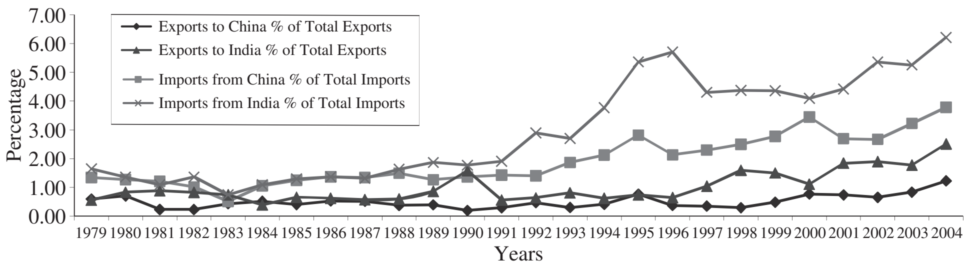

Source: Government of Kenya, *Statistical Abstracts* (various issues).

China and India are more important as sources of imports for Kenya than as market destinations (Figure 3). Between 1990 and 1995, for instance, imports from Asian Drivers increased steadily while Kenyan exports to these markets stagnated. As proportion of Kenya's imports China and India combined accounted for 10.2 per cent in 2005 (Table 1). India ranks sixth as a major source of imports, while China ranks eighth.

Many studies conclude that the rapid growth in China and India has resulted in increased demand for commodities that these countries need to sustain their growth. Therefore, exporters around the world find new market opportunities in China and India (Jenkins and Edwards, 2005; Broadman et al., 2006; Razmi, 2006). The increased demand for commodities by the Asian Drivers results in higher commodity prices and subsequently creates improvement in terms of trade for exporting countries (Goldstein et al., 2006). However, countries which rely on export of commodities which do not have high demand in China and India mostly experience erosion in their terms of trade. This is even more severe for countries competing with China and India in third-country markets. The export share in China's and India's markets indicates the extent to which a country has participated in the growth process and to a large extent the expected benefits. Table 2 shows these shares for different countries based on 2003 data.

From Table 2, one observes that Sudan is among the countries that have potential for a rise in terms of trade because approximately 43.9 per cent of its exports are directed to China and India. The other country is Nigeria with about 10 per cent, followed by South Africa with 8.8 per cent. Apparently for Kenya, the export share to China and India is only 0.3 per cent and 1.4 per cent, respectively. In total, the Asian Drivers account for only 1.7 per cent of Kenya's total exports. Even if prices for Kenyan exports were to rise, the impact in terms of trade in Kenya would remain insignificant. The situation is even worse for countries like Lesotho and Botswana whose export shares to the Asian Drivers are close to zero.

FIGURE 3
Percentage Share of Asian Drivers' Trade in Kenya, 1979–2004




Source: Government of Kenya, *Statistical Abstracts* (various issues).

### *b. Competition between the Asian Drivers and Kenya*

Undoubtedly, the Asian Drivers, which are more competitive and technologically advanced, pose stiff competition to those countries that rely on similar export products as those exported by the Asian Drivers. This is more visible in the case of labour-intensive manufactured goods such as footwear, furniture, and textiles and clothing (Jenkins and Edwards, 2005; Kaplinsky and Morris, 2006). As the Asian Drivers gradually increase their supply of manufactured products in the world market, they are likely to crowd-out less competitive countries (Razmi, 2006). Table 3 shows the export similarity index (ESI) between the Asian Drivers and selected African countries.[4]

TABLE 2
Share of China and India in Exports of Selected African Countries, 2003 (%)

| *Country* | *China* | *India* | *Total* |
|---|---|---|---|
| Botswana | 0.1 | 0.0 | 0.1 |
| Cameroon | 4.4 | 0.3 | 4.7 |
| Ethiopia | 0.7 | 1.2 | 1.9 |
| Ghana | 1.6 | 1.3 | 2.9 |
| ***Kenya*** | ***0.3*** | ***1.0*** | ***1.7*** |
| Lesotho | 0.0 | 0.0 | 0.0 |
| Namibia | 2.9 | 0.1 | 3.0 |
| Nigeria | 0.5 | 9.9 | 10.4 |
| South Africa | 4.6 | 4.2 | 8.8 |
| Sudan | 40.9 | 3.0 | 43.9 |
| Tanzania | 2.6 | 9.9 | 12.5 |
| Uganda | 0.2 | 0.2 | 0.4 |

Source: Adapted from Jenkins and Edwards (2005).

[4] Normally, an ESI is expressed as a percentage ranging between 0 and 100 per cent. A low index implies that the two countries in consideration do not have export structures that are similar, while a high index implies that export structures are similar. In this case, a high ESI implies that the African country may face competition from the Asian Drivers.

TABLE 3
ESI between African Countries and Asian Drivers

| *Country* | *Year* | *China (%)* | *India (%)* |
|---|---|---|---|
| Botswana | 2001 | 5.8 | 20.1 |
| Cameroon | 2003 | 6.6 | 11.7 |
| Ethiopia | 2003 | 4.3 | 9.3 |
| Ghana | 2000 | 10.6 | 13.0 |
| ***Kenya*** | ***2003*** | ***19.3*** | ***27.9*** |
| Lesotho | 2002 | 17.8 | 13.0 |
| Namibia | 2003 | 18.7 | 29.1 |
| Nigeria | 2003 | 1.7 | 0.8 |
| South Africa | 2003 | 27.7 | 40.2 |
| Sudan | 2003 | 2.6 | 10.1 |
| Tanzania | 2003 | 11.7 | 20.6 |
| Uganda | 2003 | 8.0 | 12.3 |

Source: Adapted from Jenkins and Edwards (2005).

In the case of Kenya, the ESI is 19.3 per cent and 27.9 per cent with China and India, respectively. This clearly indicates that a higher proportion of Kenya's exports face competition from China and India in the world market as opposed to, say, Nigeria and Ethiopia (Alemayehu, 2006). In this case, exports facing competition from Asian Drivers' products in third-country markets are manufactured products in general, and clothing in particular. There is also evidence that about 34 per cent and 25 per cent of exports from Kenya face competition from China and India, respectively (Jenkins and Edwards, 2005). In contrast, Lesotho has about 89 per cent of its exports facing competition from China and 6.8 per cent from India. Similarly, 82.4 per cent and 73.4 per cent of Zambia and Mozambique exports face competition from China. Kenya has also experienced increased imports of manufactured products from China and India lately, which threatens the survival of the local industry. These percentages are much higher than the ESI would suggest. This is because both China and India have much larger economies than their African competitors with the result that even a small percentage of their exports devoted to a particular product can swamp the exports of many African countries. Although from a consumer welfare point of view, entry of cheap manufactured products is beneficial, local producers and workers who lose employment due to increased competition find it harmful. The net welfare effect remains therefore uncertain and actually difficult to measure.

### *c. Impact of Asian Drivers on Trade in the Textiles and Clothing Industry*

The Kenyan clothing industry is quite diverse in terms of size, ownership, technology and market orientation. It consists of micro, small, medium, large and very large firms which form a pyramidal structure with three tiers.[5] The base of the pyramid is formed by the micro and small enterprises (MSEs) that produce mainly for the domestic market. In 2003, it was estimated that there were about 60,000 enterprises in this tier (McCormick et al., 2007). The next tier consisted of firms ranging from medium to fairly large that produce mainly for the domestic market, with some forays into other countries within the region. It was estimated that this tier had approximately 150 firms. The third tier consisted of approximately 45 large and very large firms mostly export-oriented. Most of the firms in this tier were foreign-owned and fairly new having been established between 2000 and 2003. It is well documented that most of these firms were established as a response to the AGOA trade preferences.

Indeed, the development of Kenya's clothing industry has been fostered by the country's eligibility with respect to the African Growth and Opportunity Act (AGOA). The export market for clothing products gained prominence in 2001 following the enactment of the US-AGOA for which Kenya qualified on 18 January 2001. Analysts argue that the AGOA has played a critical role in assisting Kenyan exports of apparel to the US (Kinyanjui et al., 2004). From Table 4, we see that the value of apparel exports increased from US$30 million in 2000 to US$195 million in 2005. In addition, the export of apparel under the AGOA accounted for nearly 90 per cent of Kenya's total export to the US in 2005 (Kenya, 2006). The AGOA is a US programme that builds on an existing General System of Preferences (GSP) programme by expanding the duty-free benefits to about 6,400 product lines including textiles and apparel manufactured from an eligible African country.[6] By 2008, preferential treatment had been extended to 30 September 2015 (www.agoa.gov). The textiles and apparel products – not included in the GSP – benefit from the AGOA but are subject to specific rules of origin and visa requirements. The rule of origin is however waived for 'lesser developed countries' (in effect, most countries in sub-Saharan Africa) allowing them to use fabric from any other (third-country) source.[7] Initially, this special rule of origin for apparel was to expire in September 2004 but it was extended, first to September 2007, and more recently to September 2012. Since Kenya is a beneficiary of this special rule of origin, most of the exporting firms have been dependent on imported raw materials mainly from

[5] The basic size categorisation of Kenyan firms by McCormick et al. (2007) follows the Government's enterprise survey (CBS et al. 1999), which uses the number of workers to classify firms as micro (1–10 workers), small (11–50 workers), medium (51–100 workers) and large (over 100 workers). Given the very low threshold for large firms, they created another category of 'very large' to include firms with 1,000 or more workers.

[6] See also McCormick et al. (2006) and Morris (2006) for more details on the AGOA.

[7] For the purposes of this special rule for apparel, 'lesser developed countries' is based on the World Bank classification in which a country whose GNP per capita was less than US$1,500 in 1998 is considered a less developed country. South Africa, Mauritius, Gabon and the Seychelles do not benefit from the waiver of the rule of origin.

TABLE 4
Performance of the Kenyan EPZ Clothing and Textile Sector, 2000–05

| | *2000* | *2001* | *2002* | *2003* | *2004* | *2005* |
|---|---|---|---|---|---|---|
| Number of Enterprises | 6 | 17 | 30 | 35 | 30 | 22 |
| Employment (number) | 5,565 | 12,002 | 25,288 | 36,348 | 34,614 | 24,234 |
| Expatriates (number) | 235 | 314 | 701 | 912 | 837 | 740 |
| Exports (US$ million) | 30 | 55 | 104 | 146 | 221 | 195 |
| Investment (US$ million) | 16 | 48 | 88 | 128 | 108 | 132 |
| Number of Visas Issued (AGOA) | 983 | 1,060 | 1,986 | 2,979 | 4,185 | 4,867 |
| Average Unit Price (US$) | 4.96 | 4.82 | 4.19 | 4.30 | 4.26 | 3.66 |
| Annual Average Exchange Rate (Kshs./US$) | 76.2 | 78.6 | 78.7 | 75.9 | 79.3 | 75.6 |

Source: Export Processing Zones Authority (2005); McCormick et al. (2006).

China, Chinese Taipei, India and Pakistan. In this sense, China and India play a facilitative role in the Kenyan export of apparel.

The textile and clothing industry in Kenya has its base in the export processing zones (EPZs). Export processing zones were established in 1990 mainly to attract foreign investments in the export-oriented manufacturing activities (Export Processing Zones Authority, 2005; USAID, 2005; Fukunishi et al., 2006). Incentives for firms operating under the EPZ include a 10-year tax holiday, unrestricted foreign ownership, 100 per cent repatriation of profits, duty and VAT exemption on all imported inputs, and an investment allowance on capital equipment. Table 4 shows how the EPZ programme has performed between 2000 and 2005, which is still dominated by foreign-owned firms.[8]

The eligibility of Kenya for the US-AGOA took place when global trade for textiles and clothing was highly regulated through the Multifibre Arrangement (MFA) which allowed major importing countries to set quotas for different producing countries. Therefore, many firms in Asia which were facing stiff competition at home found a window of opportunity to export to the US under the AGOA. In order to qualify for duty-free access, firms based in India, China, Bangladesh, Sri Lanka and Chinese Taipei established subsidiary or independent companies in Kenya mainly under the EPZ programme. To date, most of the apparel EPZ firms are foreign-owned.

While the AGOA preferential trade access remains important for the Kenyan apparel industry, its benefits have been eroded by the termination of the MFA. We observe that the value of apparel exports to the US declined by 12 per cent between 2004 and 2005. In addition, eight apparel manufacturing firms in the EPZ closed down, resulting in a loss of about 10,000 jobs. Even for those firms

[8] Foreign investors in the EPZ in 2005 were from India, China, Chinese Taipei, Sri Lanka, Bahrain, United Arab Emirates, Qatar, the UK and the USA (Export Processing Zones Authority, 2005).

still in operation, a decline is reported in the capacity utilisation owing to declining orders from US buyers (see also McCormick et al., 2006). Anecdotal evidence suggests that most of the EPZ firms that closed down in Kenya relocated to China and India, while a few relocated to Uganda and Ghana. Our interviews with managers of some EPZ apparel firms indicated that the US buyers are slowly shifting their buying patterns to China and India where firms offer lower prices and shorter lead-times than firms in Kenya.[9] Another impact has to do with the sourcing of apparel raw materials. Before the year 2005, raw materials were readily and cheaply available in China and India, but now they have gradually become less available and more expensive. This is due to increased domestic production in both China and India following the termination of the MFA. Therefore, Kenyan manufacturers are taking longer to source raw materials, resulting in long lead-times. They also allege that the US buyers are pressuring them to lower their prices by approximately 25 per cent if they wish to continue getting orders (McCormick et al., 2006), and they are also being criticised by the buyers over the long lead-times. However, their ability to address these concerns is limited by rising labour costs and the high costs of doing business in Kenya.

Next, we examine the impact of China and India on Kenyan exports of clothing in third-country markets. Considering that the US market accounts for a high share of the apparel exports from the three countries helps us in understanding competition in a third-country market. We also take into account that the three countries export knitted and woven clothing products to the US. Table 5 shows the share of each country in the US clothing market between 2001 and 2006.

Overall, we observe that China and India dominate in the US market for both the knitted and woven clothing products. In 2001, China accounted for about 11 per cent and India 3 per cent. Although market shares for both countries continued to rise, China has recorded more spectacular growth than India. In 2006, the Asian Drivers accounted for more than 30 per cent of the US clothing market. In the case of Kenya, the market share was less than 0.5 per cent between 2001 and 2006. The highest share was registered in 2004 when Kenya accounted for 0.41 per cent, but this declined to 0.36 per cent in 2006. Between 2004 and 2006, we observe that the market share for Kenya in the US declined, while that of China and India increased. Therefore, we can infer that the exports of woven and knitted clothing from Kenya face competition from China and India in the US market and are partly crowded out of the latter.

[9] While the average lead-time for an order in China and India is 30 days, in Kenya the average lead-time is 120 days. In addition, China and India have better infrastructural systems and well-developed value-chain linkages. Wage rates in the Chinese and Indian manufacturing sector are more competitive than in Kenya (see also USAID, 2005; Export Processing Zones Authority, 2006; Kaplinsky et al., 2007).

TABLE 5
Share of Exports to the US Clothing Market, 2001–06 (%)

| *Country* | *Clothing* | *2001* | *2002* | *2003* | *2004* | *2005* | *2006* |
|---|---|---|---|---|---|---|---|
| China | HS61 Knitted or Crocheted | 3.89 | 4.46 | 5.09 | 6.14 | 9.29 | 10.91 |
| | HS62 Woven | 7.09 | 7.63 | 8.73 | 9.89 | 14.45 | 16.15 |
| | Total HS61–62 | 10.98 | 12.09 | 13.82 | 16.03 | 23.74 | 27.06 |
| India | HS61 Knitted or Crocheted | 0.86 | 0.97 | 0.92 | 1.02 | 1.32 | 1.58 |
| | HS62 Woven | 2.18 | 2.36 | 2.35 | 2.38 | 2.99 | 2.83 |
| | Total HS61–62 | 3.04 | 3.33 | 3.27 | 3.40 | 4.31 | 4.41 |
| Kenya | HS61 Knitted or Crocheted | 0.00 | 0.04 | 0.08 | 0.12 | 0.11 | 0.09 |
| | HS62 Woven | 0.11 | 0.16 | 0.22 | 0.29 | 0.28 | 0.27 |
| | Total HS61–62 | 0.11 | 0.20 | 0.30 | 0.41 | 0.39 | 0.36 |

Source: Authors' own calculations based on US import data.

Kenya is also facing competition from China and India clothing products in the East African market which has been a major market (CBIK, 2006).[10]

Finally, we now examine the impact of China and India in the domestic market for clothing, whereby increased imports of manufactured products from China and India have caused both positive and negative effects (see Table 6). On the one hand, the consumers' welfare increases as they in most cases buy these products for lower costs than those supplied by domestic producers. On the other hand, these imports squeeze local producers out of domestic market opportunities. The net benefit of consumer welfare and loss of production determines the long-run impact of this trade.

From Table 6, first, trade in textiles and clothing was much stronger between Kenya and India than it is between Kenya and China from 2000–05. Second, in both cases, trade has been in favour of China and India as Kenya imports more textiles and clothing products from the Asian Drivers than it exports to them. Third, the import of textiles constitutes the largest share of trade in textiles and clothing between Kenya and the Asian Drivers. This is mainly the fabrics for use by EPZ firms to assemble clothing products for the export markets. In 2001, Kenya's trade with India in textile and clothing was almost double with China, Kshs.1,064.4 million and Kshs.622.02 million, respectively. However, by 2005, Kenya's textile and clothing trade with China was more than that of India standing at Kshs.2,511.69 million and Kshs.1,839.1 million respectively (see Table 6). Due to the lack of data on local production of textiles and clothing, we were not able to determine the extent to which imports

[10] Centre for Business Information in Kenya (CBIK) of the Export Promotion Council estimates that textile and clothing exports to Uganda and Tanzania declined by 55 per cent between 2000 and 2005. Interviews with managers of local garment firms also corroborated this allegation as some of the local firms which previously exported to Uganda and Tanzania have experienced drastic reduction in sales, due to imports from China and India as well as second-hand clothes.

TABLE 6
Textile and Clothing Trade between Kenya and the Asian Drivers, 2000–05 (Kshs. million)

| | | *2000* | *2001* | *2002* | *2003* | *2004* | *2005* |
|---|---|---|---|---|---|---|---|
| Exports to China | Textiles | 21.43 | 16.56 | 14.81 | 6.05 | 1.49 | 2.24 |
| | Clothing | 0.34 | – | – | 0.26 | – | 0.19 |
| | Total | 21.77 | 16.56 | 14.81 | 6.32 | 1.49 | 2.43 |
| Imports from China | Textiles | 454.91 | 915.57 | 567.58 | 592.71 | 1,030.23 | 2,125.71 |
| | Clothing | 145.35 | 156.24 | 62.94 | 119.50 | 217.59 | 383.55 |
| | Total | 600.25 | 1,071.81 | 630.63 | 712.21 | 1,247.82 | 2,509.26 |
| Trade Balance | T&C | –578.48 | –1,055.25 | –615.82 | –705.89 | –1,246.33 | –2,506.84 |
| Exports to India | Textiles | 0.55 | 2.69 | 1.70 | 0.60 | 0.32 | 7.59 |
| | Clothing | 4.39 | 0.016 | – | 0.39 | – | 2.29 |
| | Total | 4.95 | 2.71 | 1.70 | 1.00 | 0.32 | 9.88 |
| Imports from India | Textiles | 944.62 | 1,104.19 | 957.84 | 1,068.08 | 1,351.26 | 1,681.51 |
| | Clothing | 114.83 | 79.29 | 90.43 | 81.42 | 142.39 | 147.71 |
| | Total | 1,059.45 | 1,183.48 | 1,048.27 | 1,149.49 | 1,493.25 | 1,829.22 |
| Trade Balance | T&C | –1,054.50 | –1,801.77 | –1,046.56 | –1,148.49 | –1,493.33 | –1,819.34 |

Source: Authors' own calculations based on CBIK dataset (2006).

from China and India affect the domestic industry either through competitive or complementary impacts.[11]

## 3. FDI IN KENYA AND THE ASIAN DRIVERS

Over the last decade, China and India have emerged as the world's most attractive destinations for foreign direct investment (FDI). Increasingly, China and India have become significant suppliers of FDI, particularly among developing countries. What is of interest to current research is the extent to which FDI flowing to China and India has had a 'crowding-out' effect on other developing countries, as well as the impact of increased FDI from China and India on other countries. A number of studies conclude that the 'crowding-out' effect by FDI to China and India on African countries' FDI is negligible because FDI in Africa is mainly resource-seeking and market-seeking (Eichengreen and Tong, 2005; Jenkins and Edwards, 2005; Kaplinsky and Morris, 2006). However, there could be competition between African countries and Asian Drivers, particularly in the manufacturing sector. Increasingly, there is consensus that in low-technology manufacturing activities such as footwear, textiles and clothing, a crowding-out effect is visible (Goldstein et al., 2006). In the case of textiles and clothing, observers argue that owing to the termination of the MFA,

[11] However, interviews with local producers indicated that they are being pushed out of the market by cheap imports. Further research is necessary to determine the impact of increased imports from China and India on consumer welfare and on domestic clothing and textiles production.

sourcing and investment decisions are no longer based on labour costs alone, but on economic fundamentals such as logistics, infrastructure, investment frameworks and governance (Appelbaum, 2005). In our case, we examine the implications of increased FDI in the Asian Drivers on Kenya.

Data on sector and sources of FDI are critical for examining the extent of competition for FDI in Kenya and the Asian Drivers. Given that these statistics are not available our analysis is somehow limited. However, UNCTAD (2005) analysed FDI projects in Kenya based on registration with the Kenya Investment Authority (KIA) between 1997 and 2004. The analysis found that 27.6 per cent of FDI was in agro processing and 15.4 per cent in energy; 10.7 per cent in tourism; and 9.9 per cent in agricultural activities. Others included 4.4 per cent in petroleum trade; 2.5 per cent in mining; and 2.2 per cent in clothing manufacturing (UNCTAD, 2005). However, given the issue of reliability of data by KIA, these figures should be interpreted with caution. From UNCTAD (2005), FDI in manufacturing activities is almost 35 per cent. Studies have also shown that FDI in China and India is mainly in manufacturing activities (Jenkins and Edwards, 2005; Broadman et al., 2006). We can therefore infer that the increased FDI in manufacturing activities in China and India has a crowding-out effect in Kenya. In 2004, for instance, China alone attracted 17 per cent of global FDI in textiles and clothing (Appelbaum, 2005). In the same year, Kenya experienced a decline of 16 per cent of FDI in the textiles and clothing industry (Export Processing Zones Authority, 2006).

There is an increased presence of FDI from China and India in Kenya. Based on data from the KIA we examine the value of FDI from these two countries between 2000 and 2005: a total of US$446 million in FDI was registered by KIA, of which US$32 million and US$79.4 million originated from China and from India, respectively (see Table 7). In total, China and India represented 7.2 per cent and 17.8 per cent of the FDI in Kenya.[12] Moreover, a total of 57 projects from China and 28 from India were registered by the KIA during the period 2000–05 (Table 7). Using this information, we compute the average size of Chinese and Indian projects in Kenya. Although this measure is crude given the incompleteness of the data, we observe that on average an FDI project from China is US$0.56 million, while a project from India is US$2.82 million. Based on the average size, we can then deduce that Chinese FDI projects in Kenya are comparatively smaller than those from India. Nonetheless, more research is needed given the incompleteness of the data on FDI in Kenya.

[12] In this case, we used data provided by the KIA because of their attempt to disaggregate FDI data by the country of origin. However, the caveat relating to the reliability and accuracy of FDI data still holds.

TABLE 7
FDI from China and India in Kenya, 2000–05

| *Year* | *Total FDI (US$ million)* | *China* | | | *India* | | |
|---|---|---|---|---|---|---|---|
| | | *No. of Projects* | *Capital (US$ million)* | *Employment* | *No. of Projects* | *Capital (US$ million)* | *Employment* |
| 2000 | 127 | 9 | 3.48 | 775 | 4 | 4.97 | 980 |
| 2001 | 50 | 13 | 5.55 | 1,313 | 1 | 0.18 | 364 |
| 2002 | 50 | 6 | 1.33 | 170 | 4 | 1.74 | 395 |
| 2003 | 82 | 11 | 11.95 | 493 | 5 | 11.28 | 1,222 |
| 2004 | 46 | 8 | 7.10 | 1,442 | 6 | 41.28 | 1,185 |
| 2005 | 91 | 10 | 2.61 | 207 | 8 | 19.85 | 1,151 |
| Total | 446 | 57 | 32.01 | | 28 | 79.30 | |

Source: Authors' own calculations based on the KIA dataset (2006).

Our discussion with respondents pointed out that, increasingly, FDI from China is concentrated in construction, telecommunication and resource-extraction activities, while that from India appears to be concentrated in manufacturing, financial services and information technology. In addition, we found that most FDI from China is by companies that in China are either wholly or partially state-owned even though in Kenya they operate as private companies (see also Zafar, 2007 pp. 21–23). In contrast, FDI from India is mainly by private sector companies. One of the outcomes of this kind of ownership is that Chinese companies by and large have access to low-cost capital and can be bailed out by the Chinese government in times of need. In an interview with one of the Chinese companies in Kenya, it was pointed out that, 'since the entry of the firm into the Kenyan market the costs of road construction has gone down, quality of the road construction improved, and completion time adhered to'. Arguably, this was due to the fact that the Chinese company bids in the tendering are lower than most other companies. In addition, this company does a better quality job and in most cases it completes its construction work before the deadline. In that way this company claimed to have helped in setting high standards for government-related construction tenders.

In the case of textiles and clothing, it is the continuation of liberal rules of origin and allowing Kenya to import inputs from cheap suppliers outside AGOA that has attracted FDI from Asian Drivers (Appelbaum, 2005; Brautigam, 2006). In 2005, a total of 24 apparel manufacturing firms were operating in Kenya's EPZ. Out of these, 20 were foreign owned, three were joint ventures between foreign and Kenyan investors, and only one firm (4 per cent) was fully Kenyan.[13] The origin of capital was somewhat diverse, but the dominance of China and India is evident. Of the 24 firms, eight had Indian ownership, while six had Chinese ownership, representing 33 and 25 per cent, respectively. Other countries from which investment originated included two firms from the US; three from Sri Lanka; two from Bangladesh; and one each from Bahrain, Qatar and Kenya. FDI in the clothing industry is fairly recent, as most firms were established between 2001 and 2003. Apart from one firm established in 1997, all the others were established after 2000, seven in 2001, 12 in 2002, and four in 2003. In 2004 and 2005, the Export Processing Zones Authority did not register any new investment in the clothing activities. With regard to textile manufacturing, there is only one firm in the EPZ programme, which was established in 2001, and is a joint venture between Kenya and the UK investors.

On technology transfer, most of the Kenyan EPZ firms recruit people without experience in the garment industry who are then trained within the factory (Fukunishi et al., 2006). In this case, the EPZ firms do not compete directly with the local firms when recruiting their labour force. Equally, some former EPZ employees leave formal employment to start their own small-scale garment firms using the training and experience they got while working in the EPZ garment firm. Also, some production expatriate workers left EPZ firms to team up with local investors to establish garment factories. There are some locally-owned (non-EPZ) firms specialised in high-value activities such as embroidery, sand-blasting, stone-washing and printing, and they get regular subcontracts from EPZ firms. In this way, local firms are able to participate in the global apparel value chain indirectly. Last but not least, local garment firms are increasingly purchasing machinery from EPZ firms either when the latter upgrade their machinery inventory or at times when they close down. This has resulted in local firms using relatively modern technology in their production activities. The use of an expatriate labour force in Kenya's EPZ programme is minimal and is limited to managerial positions.[14]

In this paper, we did not find evidence of foreign investments by Kenyan companies in either China or India. However, a few Kenyan firms have entered these markets such as Kenya Airways, Copycat, Mabati Rolling Mills and Kenya Tourist Board (Business Africa, 2006). This concurs with other studies which have found that with the exception of South Africa, no other

[13] Data on local production in the textiles and clothing sector are not available from official statistics, which limits our analysis of FDI in the industry to firms operating in the EPZ programme for which data were obtained. However, studies find that in the local production, dominance of Kenyans of Indian origin is evident (Bigsten and Kimuyu, 2002: Kinyanjui et al., 2004; McCormick et al., 2007).

[14] This is in contrast to EPZs in Mauritius and the Philippines where foreign workers are engaged in production activities (Adhikari and Yamamoto, 2006; Brautigam, 2006).

African country has foreign investment in either China or India (Broadman et al., 2006).

## 4. DEVELOPMENT AID IN KENYA AND THE ASIAN DRIVERS

The recent increase in development aid[15] from China and India to other developing countries has triggered a concern about its implications on development. On the one hand, developing countries are slowly shifting their allegiance to the East. As a result, the conventional North–South development aid architecture is becoming weak. On the other hand, critics have been concerned about the role of South–South development aid in governance and human rights issues. China is particularly criticised for giving development aid to countries without any concern about the quality of governance or human rights in the recipient countries, which largely contradicts with Western donors (Business in Africa, 2006; Tull, 2006; Kaplinsky et al., 2007). This section is devoted to examining how development aid from Asian Drivers impacts on Kenya.

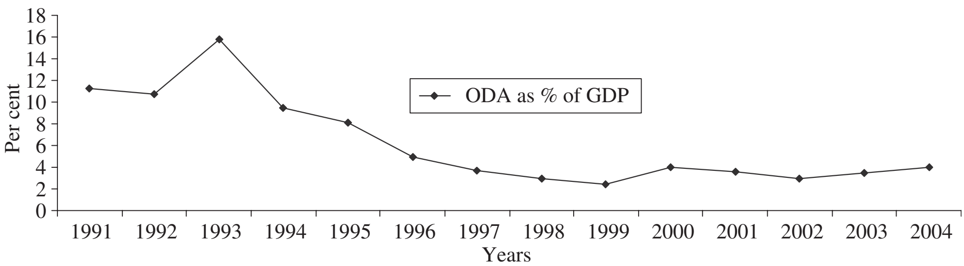
Kenya has a long history of receiving foreign aid. At independence, foreign aid was considered critical to economic reconstruction and over time foreign aid became a significant ingredient for economic development. More recently, foreign aid as a proportion of GDP was low with an annual average of 6.3 per cent between 1990 and 2004. Figure 4 demonstrates the percentage ratio of ODA in GDP for the period 1990–2004. The decline of ODA[16] during the period 1996–2005 is clear from this graph. Unlike countries such as Tanzania and Uganda, which embraced economic reforms ardently, Kenya was moving sluggishly and at times backtracking in the reform process. As a result, Kenya's relationships with the donor community deteriorated in the 1990s. Besides being slow in the reform process, Kenya was also criticised for poor governance, low democratic space, high corruption rates and violation of human rights.

Kenya's utilisation capacity of foreign aid is considered low at about 40 per cent. Government officials argue that pre-disbursement and disbursement 'conditionalities' are some of the major factors behind the low utilisation rate. Moreover, the Kenyan government procurement framework has for a long time been weak, resulting in donors using either their countries' or the World Bank procurement guidelines, oblivious to conflicts between the donors and the

[15] In this section, development aid provided by China and India is not referred to as Official Development Assistance, as the definition of the latter by the OECD Development Assistance Committee (DAC) is very specific (see http://www.oecd.org/glossary/0,2586,en_2649_33721_1965693_1_1_1_1,00.html#1965586). The characteristics of the Asian Drivers' development aid remain partly unknown and do not necessarily fit with the official definition of ODA.

[16] As officially defined by the OECD DAC.

FIGURE 4
ODA as Proportion of GDP, 1990–2004 (%)




Source: OECD (2007); World Bank (2007).

Kenyan government on this issue. Similarly, the 'tying of aid' and stringent accounting procedures (which vary with donors) have adversely affected the effectiveness of foreign aid in Kenya (source: interview with the Ministry of Finance).

China and India have different histories of development and foreign aid to Africa. Until the mid-1990s much of the Chinese development aid went towards liberation movements in Africa (McCormick, 2006). In fact, in 1964, China provided Kenya with military support to counter a Somalian invasion but it declined to provide monetary support for the independent government to purchase former colonial farms (*Daily Nation*, 2006). China currently gives both monetary and non-monetary aid to Kenya while India concentrates on non-monetary aid. Development aid from China takes the form of investment in infrastructure, equipment and plant; academic training; technical training; human relief; and tariff exemptions. India, on the other hand, has a long history of supporting Kenya mainly through human development and technical assistance. India considers itself to be a poor country that is not yet able to give financial assistance to developing countries (Indian Technical and Economic Cooperation, 2007). It therefore limits its aid support to scholarships, technical training and technical assistance. Table 8 summarises areas supported by development aid from Asian Drivers between 2000 and 2005.

Over the last five years China has given Kenya grants and loans for infrastructure, plant and equipment. These were mainly in road construction projects, modernisation of power distribution, rural electrification, water, renovation of an international sports centre, medical equipment and drugs for fighting malaria, as well as construction of a malaria research centre. China also offers scholarships to Kenyan students wishing to undertake their studies in China in diverse fields. Anecdotal sources indicate that about 100 scholarships are given by the Chinese government to Kenyans each year, 20 of which are in medical-related fields. Kenya was the first African country to receive

TABLE 8
Main Types of Development Aid Given by China and India to Kenya, 2000–05

| *Type of Aid* | *Given by* | |
|---|---|---|
| | *China* | *India* |
| General Budget Support | | |
| Grants/Loans for Infrastructure, Plant & Equipment | ✔ | |
| Scholarships for Academic Training | ✔ | ✔ |
| Other Types of Training Opportunities | ✔ | ✔ |
| Technical Assistance | ✔ | ✔ |
| Tariff Exemptions | ✔ | |
| Debt Relief | | |

Source: McCormick (2006).

Chinese financing of educational and cultural exchange programmes through the Confucius Chinese and Language Centre, currently hosted by the University of Nairobi in Kenya and Tia Jin Normal University in China (*Xinhua*, 2005).

Table 9 shows the amount of loans and grants from China between 2002 and 2005. As a ratio of total loans and grants in Kenya, China accounted for 1.67 per cent in 2002 and 9.98 per cent in 2005. With the exception of 2004, the grant component of China's loans and grants is relatively high. In fact, one of our respondents indicated that, "one of the reasons that Kenya is finding Chinese development aid more attractive than the Western one is the high percentage of 'grant component', long grace period of more than 10 years and a long repayment period of more than 25 years".

Development aid from China and India in Kenya differs substantially from that originating from Western donors. First, with regard to 'terms and conditions' imposed, and secondly, on the aspect of 'tying'. China and India are not so much concerned about the issues of internal governance, human rights and democracy in Kenya as are the Western donors.[17] Besides subscribing to the 'One China Policy', in the case of China, there is no other conditionality imposed on the recipient country. China 'ties' its aid to using Chinese companies and procurement of materials in China, but nonetheless, most government officials believe that China is perhaps one of the most price-competitive sources whether its development aid is 'tied' or not.

On technical assistance, India requires that training and consultancy be done by Indian companies. On scholarships and technical training, decisions are made by the relevant Ministry in Kenya. Neither China nor India takes part in the donor coordination initiatives and each of these countries prefers to operate

[17] By offering aid without preconditions, China has presented an attractive alternative to conditional Western aid, and gained valuable diplomatic support to defend its international interests (Tull, 2006).

TABLE 9
Loans and Grants from China, 2002–05 (US$ million)

| | *2002* | *2003* | *2004* | *2005* |
|---|---|---|---|---|
| Loans from China | 3.81 | 11.86 | 9.01 | 50.07 |
| Grants from China | 3.04 | N/A | 0.16 | 27.76 |
| Total Loans and Grants from China | 6.85 | 11.86 | 9.18 | 77.82 |
| Total Foreign Loans Received in Kenya | 208.30 | 194.37 | 260.11 | 397.24 |
| Total Foreign Grants Received in Kenya | 201.61 | 278.03 | 317.36 | 382.64 |
| Total Foreign Loans and Grants Received in Kenya | 409.91 | 472.39 | 577.47 | 779.88 |
| Share of Chinese L&G in Total Foreign L&G (per cent) | 1.67 | 2.51 | 1.59 | 9.98 |

Source: Computed from the Ministry of Finance dataset (2006).

independently. In any case, India does not consider itself a donor country. In terms of accounting, officials in the public sector argued that both China and India are much more flexible than the Western donors in accommodating domestic constraints.

## 5. POLITICAL ECONOMY ISSUES AND HUMAN RESOURCE FLOWS

### *a. The Sino-Kenya Relationship*

Kenya and China trade and diplomatic relations have historical ties, starting with the Ming Dynasty.[18] Although China embraced communism and Kenya at independence adopted a capitalist system, their relations have largely remained cordial. It is important to note that China was the fourth country to recognise Kenya's independence in 1963 when the two countries exchanged diplomatic representations.[19] The Chinese embassy in Kenya is arguably their largest embassy in Africa both in terms of size and employees (source: interview with a Chinese embassy official in Nairobi). It is strategically located in a relatively high-security neighbourhood near the Defence Headquarters, Kenya Army Barracks, and close to Kenya's State House. Kenya subscribes to the 'One China Policy', which states that 'there is only one China in the world and that Chinese Taipei is one part (a Province) of China'. The Sino-Kenya relationship, first established in 1964, was centred on promoting trade between the two

[18] A story is told of how through royal orders Zheng commanded seven expeditions to the western oceans in the early 15th century. Navigating by a compass and astronomical readings, Zheng's fleet visited many African islands in the Eastern Africa region including Lamu and Mombasa, now in Kenya, and that some sailors may have settled on the Kenyan coast after a shipwreck (Business in Africa, 2006).

[19] The first country to recognise Kenya's independence was Germany (then West Germany), then Russia, Ethiopia and then China. This order of recognition is still reflected in the diplomatic numbers given to the embassies of these countries which are 1-CD, 2-CD, 3-CD and 4-CD, respectively.

countries. The trade component of this relation was further reinforced in 1978, when under the leadership of Deng Xiaoping, China started implementing trade reforms and outward-oriented programmes. Since the China–Africa Forum was established in 2000, Kenya has remained an active member of the forum.

The exchange of official visits at the high levels of head of states, ministers, senior government officials and business delegations has strengthened relations between China and Kenya. Kenya's first high-profile delegation to China was in 1964 led by the then Vice-President Jaramogi Oginga Odinga. In 1980, the then Kenyan President Daniel arap Moi led another high-profile delegation to China, followed by others in 1988 and 1994. In August 2005, President Mwai Kibaki led a Kenyan delegation to China which resulted in the signing of several bilateral agreements. In May 1996, the former President of China Jiang Zemin made a state visit to Kenya, which marked the first ever visit to Africa by a Chinese president. In April 2006, the Chinese president, Hu Jintao, visited Kenya in his tour of five African countries as the head of state. Over 15 Kenyan ministers have visited China since 2002.

The Indo-Kenya relationship has a long history due to common past experiences between India and Kenya. For instance, the two countries were British colonies and as such remain members of the Commonwealth of Nations.[20] They are also members of the Non-Allied Movement.[21] The Indo-Kenya relationship dates back to 1963 when Kenya became independent and the two countries exchanged diplomatic representations. The relations between Kenya and India have been strengthened further by several official visits by senior government officials and delegates that have taken place between the two countries. Kenya has a diplomatic mission in New Delhi and has recently opened a consulate in Mumbai. Similarly, India has a diplomatic mission in Nairobi, which also serves the Democratic Republic of Congo and Eritrea.

### *b. The Chinese and Indian Diaspora in Kenya*

Studies on the Chinese and Indian diaspora in Africa in general and Kenya in particular are few (Himbara, 1994; Brautigam, 2006; Dobler, 2006; McCormick, 2006). Generally speaking, the entry of people of Chinese origin in Kenya is fairly recent and their population is still low. It is only in the last decade or so that the presence of a Chinese community in Kenya has become noticeable. In Kenya, the small number of Chinese people and their separation from the rest of the people has contributed to the Chinese community being

[20] The Commonwealth of Nations is a voluntary association of 53 independent sovereign states, almost all of which are former colonies of the United Kingdom.

[21] It is also important to note that as a result of the assistance that India has extended to most of the African countries and the inspiration from Mahatma Gandhi, it has an 'Observer Status' in the African Union.

hardly visible. The majority of people of Chinese origin in Nairobi reside in a small neighbourhood, close to the location of the Chinese Embassy in Kenya and where most of the Chinese companies are located. These people are mainly engaged in importation, trading and manufacturing activities. Most of them live close to one another arguably due to their unique lifestyle and also the fact that their number is small. As a community they meet regularly to share information and business ideas. One respondent reported that ‘‘we Chinese prefer to live exclusively while away from home’’. Interestingly, even those Chinese people engaged in the clothing industry avoid dealing directly with the local workers as they tactfully employ local human resource managers and accountants to handle local labour matters. Anecdotally, it is currently estimated that there are approximately 8,000 Chinese people living in Kenya. However, there are no official statistics of PCO in Kenya.

Kenya’s People of Indian Origin constitute just over 1 per cent of the population. Even though they are many more than the Chinese, they are still a tiny minority. The greatest influx of Indians in Kenya occurred in 1896 when about 31,000 labourers from Punjab and Gujarati were brought in to assist in the construction of the Kenya–Uganda railway (for detailed analysis see Himbara, 1994; Vick, 2000). After the construction of the railway line was completed, some of the people of Indian origin (PIO) were absorbed to work as train drivers, foremen, station-masters, telegraph-workers, mechanics, carpenters or upholsterers. Others were employed by the government as clerks, bookkeepers, health technicians or teachers. Those that were not absorbed by the railway or the government established small retail shops then known as *duka-wallas* in small urban centres that were developing near railway stations (Cowen and Scott, 1996). The aim of these *duka-wallas* was to serve people in the neighbourhood of railway stations and the travellers using the railway line (Himbara, 1994). Due to the fact that the PIO were highly regarded by the colonial government and also they were relatively well-off economically compared to the indigenous population, they remained largely disconnected from the local people (Vick, 2000). Their numbers dropped sharply in the years following independence, and have continued to decline.

Indigenous people felt that the PIO were betraying them by being closer to the colonialists, and as a result their relationship was largely sour. At independence in 1963, people of Indian origin found themselves in a vacuum, as they were not sure whether to align themselves to the former colonialists or indigenous Africans (Himbara, 1994; Cowen and Scott, 1996). Some migrated to Britain while others remained in Kenya where they were given citizenship. Fearing the possible repercussions from the African government, only 10 per cent of the people of Indian origin opted to remain in Kenya. The rest migrated to Britain where they got automatic British citizenship until 1968, when the Immigration Act of 1968 that deprived automatic citizenship was passed (see

Cowen and Scott, 1996; Vick 2000). Although PIO were engaged in trading activities, the Trade Licensing Act of 1967 prohibited the non-indigenous Kenyans from undertaking trade-related activities. This pushed PIO into manufacturing activities where they remain dominant to date. The number of PIO in Kenya is estimated at about 500,000 according to the 1999 population census. Nonetheless, this community has remained distanced from the local populace and they have retained their culture, religions and beliefs. Most of the PIO in Kenya live in areas originally designated for them by the colonial government.

## 6. CONCLUSIONS AND POLICY RECOMMENDATIONS

In this paper we have analysed the impact of the ascendancy of China and India on Kenya based on trade flows, investment, aid and diaspora. Given the central theme of the study, we have mainly focused on textile and clothing manufacturing for which the entry of China and India has had great impacts. In conclusion, we highlight major findings of this study using the four trajectories and at the end we suggest some recommendations.

### *a. Trade*

The study finds that trade between the Asian Drivers and Kenya has increased significantly during the last decade. India ranks higher than China in terms of both exports and imports. Moreover, bilateral trade has remained largely in favour of the Asian Drivers. Kenya's export-basket comprises raw materials which unfortunately are not among the major Kenyan export commodities (with the exception of tea). On the other hand, Kenya imports machinery, manufactured products and medicine from these countries. Thus, Kenya has limited potential to increase its export share in China and India. On the other hand, China and India are likely to export more into the Kenyan market and indeed the world market given their competitiveness. The Kenyan clothing industry (in particular its export-oriented segment) has depended on India and China for supply of inputs. This dependency will continue unless Kenya develops its upstream cotton, yarn and fabric linkages, or a greater clothing and textile synergy is created within the region. Already signs are showing that the dependency on imported inputs is not sustainable in the long run. The Asian Drivers' share of textile and clothing products in the Kenyan market is formidable and it is gradually threatening domestic production. Although this is good for consumers, it is clear that in the long run domestic industry is unlikely to compete. In the export market, China and India are also threatening Kenya. The paper has shown that export share in the US market has declined while that of China and India increased for knitted and woven clothing. The entry of China and India in the global market for textiles and clothing is pushing world prices downwards. This is a threat to less competitive exporters like Kenya where cost of production is comparatively higher than in China or India. In the regional market, Kenya has lost a substantial share of its market as a result of imports from China and India.

*b. Foreign Direct Investment*

The study has demonstrated that FDI from China and India is rapidly increasing in Kenya. A notable feature of these investments is their spread in many sectors of the economy. These investments are in the construction, oil exploration, manufacturing, services and telecommunication sectors. In the case of the textiles and clothing industry, we find that China and India account for more than 60 per cent of FDI. Increasing FDI from China and India in this sector has played a critical role in employment creation, manufactured export promotion and technology transfer, but it is not clear how sustainable these gains are. The labour-intensive nature of the industry combined with the fact that Chinese and Indian FDI has been largely motivated by the desire to exploit preferential markets which are accessible to Kenya make these investments precarious. Investors can easily choose to shift their operations to other destinations when incentives to operate in Kenya wane. Apart from the case of textiles and clothing, however, we find no evidence of diversion of FDI from Kenya to China and India. Finally, lack of consistent, disaggregated and updated statistics on FDI in Kenya seriously limits our analysis. We suggest that more research is needed.

*c. Foreign Aid*

Although foreign aid from Asian Drivers to Kenya is increasing, it is still small compared to total aid. Loans and grants from China increased remarkably between 2002 and 2005. By the year 2005 China alone accounted for nearly 10 per cent of loans and grants received in Kenya. While India limits its development aid to technical assistance, scholarships and technical training, China extends beyond this to cover investments in infrastructure, plant and equipment. The fact that development aid to both China and India has declined substantially in the recent past may imply that more will be available for low-income countries like Kenya. Although the link between aid and development is still unclear, the types of aid given by China and India may in the long run have a positive effect on the economy and by extension on the textiles and clothing industry.

*d. Politics and Diaspora*

As far as Chinese and Indian diasporas are concerned, research and statistics are largely undeveloped. Nonetheless, this paper has documented that the population of both Chinese and Indians in Kenya is rapidly growing, but there are no records to show the rate of growth. Different respondents in our survey gave different figures and rates of population growth of Chinese and Indians in Kenya. Limitation of data constrains our analysis in terms of the activities these diasporas are involved in, but we do show that their presence in the textiles and clothing industry is significant. Given the networks of these diasporas with their respective countries of origin, there is a possibility of utilising it for mutual benefit. A more detailed analysis is required to unravel costs and benefits of these diasporas in Kenya.

*e. Recommendations*

The textiles and clothing industry plays an important role in Kenya. The industry has its fair share of economic growth largely in export revenue, employment creation, industrial development and linking Kenya to the global economy. The most significant impact of the rise of China and India is the increased competition in both domestic and export markets. The only factor that has sustained Kenya in the export market is the preferential treatment in the US market which allows textile and clothing exports duty free. In order for Kenya to continue exporting into this market beyond 2012, there is a need to explore the possibility of developing its upstream cotton, yarn and fabric linkages. While Kenya should pursue trade preferences with other major importers besides the US, it is important to note that there is a need to upgrade production capabilities on an ongoing basis. This is perhaps more urgent for Kenya given that the textiles and clothing industry is characterised by rapid technical change and changing patterns of trade. While China and India are still present in the Kenyan EPZ, there is a need to establish policies that allow more interaction between the exported-oriented and domestic firms. This will facilitate more learning and technology transfer from foreign-owned EPZs to local firms. Currently, EPZ firms wishing to interact with local firms by subcontracting to them find the policy regulations inhibiting as this will require approval from the Ministry of Finance. Increased industrial synergy will be created when local and export-oriented firms are able to learn from each other.

It is unfortunate that Kenya is locked into the lower end of the clothing value chain with most export products being standard type, low-price and low-quality apparel. There is a need to move up the value chain by producing niche products in the medium term. This would reduce the vulnerability of an industry that has focused only on mass-market production. This calls for increased flexibility in order to adapt to the demands of new customers who will often prefer a wider product range, but in smaller quantities. More linkages need to be created between Kenyan producers and high-value buyers in developed countries rather than relying on mass retailers. Similarly, networks that Chinese and Indian investors in Kenya have either in Asia or in importing countries should be strengthened with a view to benefiting the industry.

The investment framework in Kenya needs to be revised on a more regular basis to ensure that the legislation is attractive to new investors and also to retain the existing ones. Laws and incentives should be made more investor- and exporter-friendly. The government should also move to sign bilateral investment treaties and trade agreements with China and India so as to tap increasing investments from these sources. This will also facilitate more trade between Kenya and the Asian Drivers. Infrastructural obstacles such as dilapidated road transport, insecurity, electricity supply and customs clearance which increase the lead-time for Kenya need to be addressed urgently. Low labour costs in Kenya will no longer be the driving force in attracting foreign investors to the industry. Policies aimed at developing the labour force should be designed. There is an insufficient skill level when it comes to the use of new machines and technology in Kenya. Far too little has been spent on training of staff. Better trained staff will lead to increases in production and efficiency and will lower costs. In addition, acquisition of work permits for foreign technical workers in the industry should be made much easier than it is currently. There is a need to utilise foreign aid from Asian Drivers prudently to ensure maximum benefit to the entire economy. Finally, availability of data relating to production, trade, investment and 'diaspora' needs to be developed so as to enable more informed decision making.

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