THE IMPACT OF TAX INCENTIVES ON FOREIGN DIRECT INVESTMENTS INFLOWS OF FIRMS LISTED AT THE NAIROBI SECURITIES EXCHANGE

BY

GITHAIGA, ISAIAH WAHOME

D61/75192/2009

A Research Project Report Submitted in Partial Fulfillment of the Requirement for the Degree in Master of Business Administration, University of Nairobi

NOVEMBER 2013
DECLARATION

STUDENT

I, the undersigned, declare that this is my own original work and has not been submitted to any other university or institution for academic credit.

Signature……………………………….….. Date…………………………...

Isaiah Wahome Githaiga

D61/75192/2009

SUPERVISOR

This Research Project has been submitted for examination with my approval as the University Supervisor.

Signed……………………………………… Date……………………………

Dr. Kisaka Sifunjo

Lecturer, Department of Finance and Accounting School of Business

University of Nairobi
DEDICATION

I dedicate this research paper to my spouse Mercy Wambui and my daughter Cecile Wambui for their love and support during the research period.
ACKNOWLEDGEMENT

I thank the almighty God for the blessings through the Master of Business Administration program. It has been a long journey full of challenges but God has given me the endurance that I needed to succeed.

I am truly indebted to my supervisor Dr. Kisaka Sifunjo for his critique that has enabled me produce a quality paper. I also thank University of Nairobi School of business faculty for passing on their knowledge that has added value to the process.

My thanks also go to my parents Cecilia Githaiga and the late Richard Githaiga and my siblings Ann, Grace, Jane, Lucy, Patrick and Rose for their encouragement and financial support during my studies. I cannot forget to thank my uncle, Francis Wahome for funding the research project and his helpful career advice he has given to me.

Finally I thank David Godsell, a third year PhD candidate at Queen’s university Canada, who gave me the necessary exposure that I needed in data analysis and presentation through his research and consultancy projects.
TABLE OF CONTENTS

DECLARATION ........................................................................................................... ii
DEDICATION .............................................................................................................. iii
ACKNOWLEDGEMENT ........................................................................................... iv
LIST OF TABLES ..................................................................................................... viii
LIST OF FIGURES ..................................................................................................... ix
LIST OF EQUATIONS ................................................................................................ x
LIST OF ABBREVIATIONS ...................................................................................... xi
ABSTRACT ................................................................................................................. xii
CHAPTER ONE ............................................................................................................ 1
INTRODUCTION ......................................................................................................... 1
  1.1 Background to the Study ...................................................................................... 1
    1.1.1 Tax Incentives ................................................................................................ 1
    1.1.2 Foreign Direct Investments ......................................................................... 2
    1.1.3 Impacts of Tax Incentives on Foreign Direct Investments ......................... 2
    1.1.4 Nairobi Securities Exchange .................................................................... 4
  1.2 Research Problem ............................................................................................... 4
  1.3 Objective of the Study ....................................................................................... 6
  1.4 Value of the Study ............................................................................................. 6
CHAPTER TWO .......................................................................................................... 8
LITERATURE REVIEW ............................................................................................. 8
  2.1 Introduction ...................................................................................................... 8
  2.2 Theoretical Literature ..................................................................................... 8
LIST OF TABLES

Table 1.0: Distribution by Industry ................................................................. 22
Table 2.0: Percentage Change in tax allowance claims ............................. 25
Table 3.0: Average return on investment ..................................................... 25
Table 4.0: Descriptive statistics ................................................................. 28
Table 5.0: Pearson Correlations ................................................................. 28
Table 6.0: t test values .............................................................................. 29
Table 7.0: ANOVA table for testing hypothesis ........................................ 29
Table 8.0: R square table for testing hypothesis ....................................... 29
LIST OF FIGURES

Figure 1.0: Distribution by industry .................................................................................. 23

Figure 2.0: Tax incentives available at Nairobi securities exchange ................................ 23

Figure 3.0: Percentage change in the level of FDI inflows .............................................. 24

Figure 4.0: Average return on investment ........................................................................ 26

Figure 5.0: Extent of tax incentives contribution towards FDI inflows .......................... 27
LIST OF EQUATIONS

Equation 1.0: Conceptual model equation................................................................. 19

Equation 2.0: Analytical model equation................................................................. 20
# LIST OF ABBREVIATIONS

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Full Form</th>
</tr>
</thead>
<tbody>
<tr>
<td>EPZ</td>
<td>Export Processing Zone</td>
</tr>
<tr>
<td>FDI</td>
<td>Foreign Direct Investments</td>
</tr>
<tr>
<td>AAI</td>
<td>Action Aid International</td>
</tr>
<tr>
<td>TJN-A</td>
<td>Tax Justice Network - Africa</td>
</tr>
<tr>
<td>KRA</td>
<td>Kenya Revenue Authority</td>
</tr>
<tr>
<td>GDP</td>
<td>Growth Domestic Product</td>
</tr>
<tr>
<td>UNCTAD</td>
<td>United Nations Conference on Trade and Development</td>
</tr>
<tr>
<td>IEA</td>
<td>Institute of Economic Affairs</td>
</tr>
<tr>
<td>OECD</td>
<td>Organization for Economic Cooperation and Development</td>
</tr>
<tr>
<td>ROI</td>
<td>Return on Investments</td>
</tr>
<tr>
<td>PSC</td>
<td>Parliamentary Service Commission</td>
</tr>
<tr>
<td>USA</td>
<td>United States of America</td>
</tr>
<tr>
<td>NSE</td>
<td>Nairobi Securities Exchange</td>
</tr>
<tr>
<td>CMA</td>
<td>Capital Market Authority</td>
</tr>
<tr>
<td>KNBS</td>
<td>Kenya National Bureau of Statistics</td>
</tr>
<tr>
<td>EU</td>
<td>European Union</td>
</tr>
</tbody>
</table>
ABSTRACT

The main objective of this study was to establish the impact of tax incentives on FDI inflows of firms listed at the NSE. It is assumed that tax incentives play a major role in attracting FDI inflows especially in developing countries. The same has been proven empirically in developed countries. However, in developing countries the research is at its infancy stage. This study focused on the impacts of Wear And Tear Allowances; Investment Deductions and Industrial Building Deductions, towards attracting FDI inflows to firms listed at the NSE.

The study involved collection of a time series data on investments and tax incentives from a sample of 10 firms listed at the NSE between years 2008 – 2011. The data was mainly from secondary sources, most attention being focused on annual reports and audited financial statements of the sampled firms. Correlation analysis was carried out on FDI inflows and tax incentives variables to establish whether there was any relationship. The results were then analyzed to arrive at a conclusion on whether tax incentives have any impact in attracting FDI inflows in firms operating at the NSE.

The results of the study revealed a strong relationship between wear and tear allowances and FDI inflows. Industrial Building Deductions and Investments Deductions had no significant relationship with FDI inflows. Despite strong relationship between Wear and tear allowances and FDI, further analysis on percentage change in FDI inflows across the study period shows that the Impact of tax incentives on FDI inflows is insignificant.
CHAPTER ONE

INTRODUCTION

1.1 Background to the Study

1.1.1 Tax Incentives

Tax incentive can be defined as a deduction, exclusion or exemption from tax liability offered as an enticement to engage in a specified investment activity (Mutua, 2011). The most dominant tax incentives in Kenya take the form of investment allowances, tax credit, special economic zones, reduced tax rates and tax exemption. Specific tax incentives offered include Capital allowances, capital market incentives, EPZ benefits and tax remissions for exports.

The rationale behind granting of tax incentives is to exploit investments opportunities, where tax system is seen as an obstacle. They are also used to improve social welfare of the community for example, granting incentives related to health, education or savings for future use. On the other hand they can also be used to discourage certain activities like overproduction of agricultural produce resulting to instability in prices (Klemm, 2009).

In Kenya tax incentives for investments have not been effective in promoting GDP growth. The current structure have been associated with disincentives that have contributed to massive revenue losses by the government in terms of tax holidays, tax exemptions and reduced tax rates. According to KRA statistics (2009), it is estimated that Kshs 220.8 billion was lost between the years 2003 -2009.
1.1.2 Foreign Direct Investments

According to the US model of Bilateral Investment Treaty (2004), investments refer to any asset held with expectations of profit in the future. Investment level in a country can be measured using FDI inflows and private gross capital formation (Klemm and Parys, 2009). FDI can be defined as investment by Multinational Corporation. It consists of investment through equity or debt and reinvested earnings (Mooij and Ederven, 2001).

In Kenya, the key sectors with a lot of investment potential include Agriculture, tourism and mining. Tax incentives alone cannot lead to increase in level of FDI inflows to these sectors. Factors such as political stability, infrastructure and cost of doing business play a major role in determining the level of investments in a developing economy (AAI and TJN-A, 2012). To prospective investors, tax rate and tax base also play a major role in making investment decision (Thuronyi, 1998). Kenya being a developing country in the sub Saharan Africa, it is necessary to address issues hindering investment growth and formulate a good policy framework. This can help tap the potential of the unexploited sector of the economy especially mining and agriculture.

1.1.3 Impacts of Tax Incentives on Foreign Direct Investments

The role of tax incentives in attracting FDI inflows have not been clearly established in Kenya. Previous Studies have shown that there have been success and failures in effectiveness of various tax incentives. The main issues that can be attributed to the failure are expectations of the investors and tax competition (UNCTAD, 2000). The incentives are available to resident companies targeting agriculture, tourism, and mining
sectors, which are the key pillars of Kenyan economy as articulated under the in vision 2030.

Potential investors carry out evaluation before committing time and resources to invest in a given country. They carry out a background check based on countries’ certain economic factors necessary for successful investments. Their expectations are that the country has good infrastructure, politically stable and secure (AAI and TJN-A, 2012). If these conditions are not met, the investor will turn down any offer to invest. Tax incentives are not given preference in making their decision to invest in a developing country.

Another key issue contributing to failure of tax incentives is tax competition. Governments compete to have the best tax policies to attract and retain FDI. If tax competition is not put to check, it can be lead to tax losses (IEA, 2012). In East Africa, disparities in tax rates has led to illicit trade and complicated business processes (AAI and TJN-A, 2012). Mitchell (2004) however, argues that tax competition from economic point of view, can lead to increased purchasing power of individuals and thus should be encouraged. This debate is still at its infancy stage and more empirical research is needed to distinguish between good and bad tax competition (Wildasin and Wilson, 2001).

Tax incentives play a vital role in attracting FDI in developed countries. However, in developing countries caution should be taken since they lead to loss of much needed revenue by the government (AAI and TJN-A, 2012). For tax incentive to be justifiable, the benefits derived from any tax incentives should be significantly higher than the cost of administering them.
1.1.4 Nairobi Securities Exchange

The NSE has three investment market segments. These include Main investment market segment (MIMS); Alternative investment market segment (AIMS) and Fixed income securities market segment. The issuer of securities in any segment must satisfy its eligibility requirements as specified in the capital market regulations (NSE listing manual, 2013).

For an investment to qualify as FDI at the NSE, the foreign investor must own at least 10% of the stock invested. This includes investment in affiliates or subsidiaries (Mooij and Ederveen, 2001).

1.2 Research Problem

The government of Kenya has continued offering tax incentives to various sectors of the economy despite slow growth in GDP within the last four years. Lack of evaluation on the performance in relation to contribution to development has resulted to major loss of income which could have otherwise been used in social welfare of Kenyan citizens. This study is focused on establishing whether reforming tax incentives structure in Kenya would aid in exploiting the full potential of the key economic sectors.

Studies have been done on tax incentives and investments and their results have been different depending on the countries where they have been carried out and methodology adopted. Klemm and Parys (2009) conducted an empirical research to address the question on how effective tax incentives are in attracting investments. Data was collected in over 40 Latin American, Caribbean and African countries between 1984 and 2004. The
results showed that lower corporate income tax rates and longer tax holidays are effective in attracting FDI, but not in boosting gross private fixed capital formation or growth.

Sebastian (2009) made an analysis on how tax incentives may or may not be used to attract investments especially in developing countries. The analysis was based on research done using micro economic data collected from OECD countries. Micro economic data provides little information on tax policies effects on investments (Hassett and Hubbard, 2002). The analysis reached to the conclusion that tax incentives alone have little effects on investments. Good investment climate is also necessary to attract investments.

Musyoka (2012) conducted a study with the objective of correlating tax incentives and foreign direct investments in Kenya. Data for investments incentives, trade related incentives, import duty exemption and foreign direct investments inflows for the recent 10 years was collected. Measures of central tendency were conducted to measure dispersion while correlation and regression analysis was carried out to establish relationship between the dependent and independent variables. The results of the test were used in arriving at the conclusion that there was no significant improvement in FDI as a result of implementing tax incentives in Kenya. A part from this unpublished research, no other study has been carried out in Kenya to measure the impact of tax incentives on FDI inflows at the NSE. This study focused on filling this research gap.

Lack of adequate empirical literature in Kenya and inconsistency in the results of previous studies on exact position of tax incentives impacts on FDI inflows necessitates further research to be conducted. The research answers the following question: Do tax
incentives have any impact on foreign direct investments inflows at Nairobi securities exchange?

1.3 Objective of the Study

To establish the impact of tax incentives on Foreign Direct Investments inflows of firms listed at the Nairobi Securities Exchange.

1.4 Value of the Study

This study is of great value to the Government, researchers and corporate tax payers. It forms the basis of reviewing the tax policies and carrying out an evaluation on their effectiveness. A review of the current tax policies can aid in carrying out a cost benefit analysis and scrapping off the incentives that have little benefits. This can help in formulating fiscal policies aimed at reducing external borrowing and also enhance investments and employment creation. This research has provided the government with empirical evidence on performance of current tax incentives and hence makes informed decision in improving the status quo.

The research has provided the corporate tax payers with an insight on available tax incentives and how to utilize them in order to increase their savings for future investments. Rise in level of investments in the country is likely to result to rise in level of revenue for the government through taxation. However a favourable climate for investment should be established otherwise the revenues are likely to be eroded by factors such as political instability and unfair tax policies that tend to favor certain sectors only.
The researchers have a basis for further research by adopting different research methodology or extending the period of analysis. The report forms a reference for future studies.
CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

This chapter reviews work done by other researchers who have carried research on this field. It is organized as follows: Section 2.2 discusses theoretical literature, section 2.3 presents empirical literature, section 2.4 reviews the local research on this topic and finally section 2.5 give a summary and critique of the key results.

2.2 Theoretical Literature

Glaeser et al (2001) classified tax incentive economic theories into five categories, namely: consumer and producer surplus; agglomeration economics; ex-post appropriation; tax discrimination and finally corruption and influence. The study was a review of literature to ascertain why tax incentives occur and whether they should occur in USA cities.

2.2.1 Consumer and Producer Surplus Theory

Consumer and producer surplus theory implies that government lure firms to invest in their countries to create employment and create outputs for the local market. They evaluate potential investors based on their ability to improve quality of life for their citizens (Glaeser et al, 2001).

FDI involvement with local market for inputs and outputs contributes to economic growth of the host country. In most cases the governments’ demands employment of
local citizens to the industries. An upward slope on the labour demand curve means the presence of the firm is beneficial to the community. A downward slope on the consumer demand curve means that consumers are benefiting from the firm's goods and services (Glaeser et al., 2001).

When making a decision on tax incentive to offer, the government should consider benefits created by presence of the investor. The magnitude of the tax incentive should be equal to consumer or producer surplus generated. This is determined by elasticity of demand and supply. When labor supply to the firm is elastic there will be little local surplus. The government should not offer tax incentives, unless labor supply is inelastic (Glaeser et al., 2001).

On the other hand highly elastic demand generates little consumer surplus. However, an inelastic demand to the firm products generates higher surpluses and government should offer tax incentives. Another factor that can generate consumer surplus is that, if the firm has large fixed costs and prices of its products are set close to marginal costs then the surplus goes to the consumer (Glaeser et al., 2001).

2.2.2 Agglomeration of Economies Theory

Mila and McGuire (2001) argued that agglomeration of economies lead to increase in production as a result exchange of ideas. When firms in related industries come together, they enjoy economies of scale through networking. They also attract more suppliers and customers (Glaeser et al., 2001).

According to this theory governments will tend to give higher tax incentives to firms that will lead to agglomeration of economies as they will benefit from spillovers. They are
interested much in firms that will attract related industries to the economy and hence
development (Glaeser et al, 2001).

This theory argues that countries with more skilled labour tend to offer higher tax
incentives in order to create employment opportunities. It also argues that cities with
many small firms grow faster than the ones with few big firms. Attractiveness of
Agglomeration based tax incentives increase with the ability of the potential investors to
attract more economic activities within a country (Glaeser et al, 2001).

2.2.3 Ex-Post Appropriation Theory
Ex-post appropriation theory assumes that new firms are target of exploitation by the
government, especially where their resources are immobile. Hence they tend to demand
for compensation in advance. In most cases they demand compensation in terms of tax
break (Glaeser et al, 2001).

Firms with immobile resources will tend to demand for more attractive tax breaks in
order to recover their entry costs. However the tax incentive cannot be higher than the
total NPV of future tax payments of providing the firm with essential services it requires
to remain in operation (Glaeser et al, 2001).

2.2.4 Tax Discrimination Theory
Tax discrimination theory asserts that government charge different tax rates based on
regions. Tax rate is determined by demand for firms to locate in a particular location. In
Kenya investment deduction rates differ with regions to enhance development in
underdeveloped areas (Glaeser et al, 2001).
Tax discrimination is applied by the government with an aim of encouraging development in the rural areas. Low tax rates and tax holidays are given to investors who are willing to locate their business outside major towns and cities. However, there has been a lot of criticism on tax holidays whereby some firms relocate to other countries after the end of the term (Glaeser et al, 2001).

For tax discrimination to apply effectively, the government is charged with the task of ensuring basic infrastructure is available in the rural areas. These include good road network for transporting the final output, telecommunication network, and availability of labour force to work in the firms (Glaeser et al, 2001).

2.2.5 Corruption and Influence Theory

Corruption and influence theory states that tax incentives occur because of corruption and influence. Firms with greater political influence get higher tax incentives. For instance in Kenya, the cabinet secretary to the finance ministry can introduce or discontinue a tax policy. This is a loophole that can be utilized by firms or individuals with great political influence (Glaeser et al, 2001).

In developing countries, corrupt practices are prominent in designing and implementing tax incentives. It is influenced by low salaries for tax officials, protection of prominent personalities, poor monitoring, high tax rates, and lack of information (Asher, 2001).

For tax incentives to be successful, the government should foresee challenges brought about by corruption and design checks and balances to counter their negative effects. These include regular audits procedures to ensure tax targets are achieved and money spent in development projects.
2.3 Empirical Evidence on Impacts of Tax Incentives on Investments

Hartman (1984) used after tax ROI for foreign investors in US and gross ROI for investments in US to explain the effect of tax policy on level of foreign investments in the US between 1965 and 1967. The result implied that tax rate elasticity for retained earnings is significant. Boskin and Gale (1987) extended Hartman analysis to cover the period between 1956 -1984. Their experiments proved Hartman main findings. Young (1988) extended Hartman research to cover from 1953 -1984. His results also confirmed Hartman’s results. Newlon (1987) casted doubt on Hartman’s work; he argued that the study used wrong data for the ROI. To deal with this he used alternative data in his study. However, his study still confirmed Hartman’s results.

Slemrod (1990) criticized Hartman research to lack of a perfectly specified model, unreliable data, and measure for tax rate and variables. He made modifications to correct Hartman’s model. His findings concluded that retained earnings are not responsive to US taxes. This was different from Hartman results which shows tax rates affected retained earning significantly. His qualification made researchers reluctant to continue using Hartmann’s model. Swenson (1994) aggregated FDI inflows in the US for 1979 – 1991 using 18 different industries. She conducted a regression of FDI log to the average tax rates. Swenson concluded that higher effective tax rates will raise FDI from investors in tax credit countries. Cassou (1997) repeated Slemrod’s work using data from individual countries investing in the US between 1970 - 1989. The results were insignificant.

Grubert and Mutti (2000) used 500 tax returns from the US to compute average effective tax rates and investment in plant and equipment by US multinationals in 60 different
locations. The results reported significantly negative elasticity. Auerbach and Hassett (1993) argued that there is need to breakdown the components of FDI since each is likely to respond differently to tax rates. Data on investments in property plant and equipment is viewed as the most appropriate measure of FDI inflows as it relates to real investment. Swenson (2001) distinguished 6 main components of FDI: New plants, plant expansions, mergers and acquisition, joint ventures, equity increases and other FDI. The results of the study revealed negative tax elasticity for new plants and plant expansions, positive tax elasticity for mergers and acquisition.

Mooij and Ederveen (2001) carried an empirical review of literature on impact of tax on FDI in EU countries. The study compared outcome of 25 empirical studies using tax elasticity under uniform definition. The results gave a mean tax elasticity of approximately 3.3%. This was interpreted as a 1% reduction in host country tax rate led to a 3.3% increase in FDI. Another study carried out by OECD (2001) had similar results. However there exist substantial variations across studies.

Easson and Zolt (2002) argued that tax incentives are both bad in theory and bad in practice in developing countries since they distort investment decisions. They are prone to corruption and thus their objectives are hard to meet. To improve chance of success they recommended that the government should set clear objectives; minimize chances of attracting corruption and evaluate effectiveness from time to time.

Klemm and Parys (2009) conducted an empirical study to investigate how effective tax incentives are in attracting investments. Data was collected from over 40 Latin American, Caribbean and African counties between 1984 and 2004. FDI and private gross fixed
capital formation were used as the dependent investment variables and tax as the independent variable. Their result revealed a significantly positive relationship between tax incentives and FDI.

Sebastian (2009) in his analysis of tax incentives effects on investments in OECD countries concluded that tax incentives alone cannot lead to increased investments. The analysis was based on existing literature and case studies from developed countries. Its key results showed that every tax incentive has costs and benefits. The benefits are as a result of increased investments and costs are due to revenue losses by the government. It therefore recommended that government should prepare expenditure statements to monitor costs and benefits of tax incentives.

2.4 Review of Local Research on Tax Incentives Impact on Investments

There is little research that has been conducted in Kenya to measure effectiveness of tax incentives in attracting FDI inflows. KRA conducted a time analysis of revenue lost by the government through tax incentives for a period of six years starting from 2003/2004-2008/2009. The losses amounted to an average 1.7% of GDP. UNCTAD (2011) comparative analysis on FDI inflows in Kenya, Uganda and Tanzania revealed that Uganda attracted more FDI despite offering fewer incentives than Kenya. Tax incentives are not always effective since they are likely to lead to tax competition among neighboring countries. It further states that no cost and benefit study has ever been undertaken to ascertain the net benefit of tax incentives. The government is put to task in developing effective tax policies whose benefits will outweigh their costs.
Musyoka (2012) conducted a study to establish the relationship between tax incentives and foreign direct investments. He used data for investments incentives, trade related incentives, import duty exemption and FDI inflows for a ten years period. Mean, mode and median were calculated to measure dispersion while correlation and regression analysis to establish relationship between the dependent and independent variables. The results concluded that tax incentives lead to revenue losses by the government.

According to PSC (2012), tax incentives have not achieved the following economic variables: increased investments; employment generation; technological upgrades and exports. The reports argued that tax incentives play a major economic role in promoting the above variables; however, they deprive the government much needed income in short term especially where they are prone to abuse. The Government should shift efforts from offering tax incentives to encouraging domestic savings to increase formal sector employment (Attiya et al, 2009).

2.5 Summary

A great number of recent studies carried on impacts of tax incentives on investments take a case study approach instead of empirical approach. Most of the studies have been carried out in developed countries mainly USA and Europe. Using time series analysis of FDI data and ROI as a percentage of GDP, the results of the studies have shown that tax incentives contributed to growth in FDIs. However, the few studies from developing countries have proofed otherwise. The results have shown that tax incentives in developing countries deprive the government much needed revenue for development.
This calls for further research to be carried out especially in developing countries in order to come up with a conclusive answer.

A good tax system should be fair to all and encourage wealth distribution through projects that aim to improve quality of life for the citizens. Tax Administration costs should be minimized and excessive borrowing should be discouraged. The more the number of tax incentives the greater the tax administration costs.
CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter describes how the research was carried out. It is organized as follows: Section 3.2 covers research design, 3.3 population and sample, 3.4 data and data collection instruments, 3.5 data analysis and 3.6 data validity and reliability.

3.2 Research Design

A good research design allows researcher to draw valid inferences that can advance scientific knowledge. Valid inferences lead to theories that explain phenomenon (Plumper 2008).

This study adopted a quantitative and descriptive approach to evaluate available tax incentives based on their impact towards attracting FDI inflows. Data collection forms were used to collect quantifiable data for analysis. The study focused on 61 firms listed on NSE. The researcher selected this area since all the main sectors of the economy are well represented. These include agricultural, commercial services, telecommunication, automobile, banking, insurance, investment, manufacturing, construction and energy.

A time series data on investments and tax incentives for period 2008 - 2011 was collected. Correlation analysis was carried out on FDI inflows and tax incentives variables to establish whether there was any relationship. Analysis of the result was done to arrive on a conclusion and recommendations on whether tax incentives have any impact in attracting investments in firms operating on Nairobi stock exchange.
3.3 Population and Sample

Population consists of every element in the area of study. A sample is a random selection of element of a population for which inferences are drawn to represent the entire population (Moore et al, 2012).

The unit of analysis in this research was 60 firms listed at NSE. These firms are fairly uniform in terms of capital structure since a standard criterion is adopted by CMA during listing. Therefore a simple random sampling was used to draw a representative sample of 10 out of the 60 firms listed on NSE. Data relating to investments and tax incentives was collected from the sample; this covered year 2008 -2011.

3.4 Data and Data Collection Instruments

The study used secondary data for analysis. A time series data covering period 2008-2011 was collected. This included percentage changes in FDI inflows; total revenue lost by the government through tax incentives during the sample period. A comprehensive data collection method was used to capture relevant information.

Designing a good data collection instrument leads to accurate and quality results. Data collection methods include: Household survey, diaries/logs, direct observation and questionnaires (Glewwe and Grosh, 2000). Secondary data was collected from financial statements of sampled firms, KNBS and KRA reports and previous studies both published and unpublished. A predesigned data collection form was used to aid in this process. The data was be used to analyze investments trends and revenue losses by the government through tax incentives.
3.5 Data Analysis

Data analysis is a scientific fact finding process used to test hypothesis and draw inferences that later contribute to a theory. It simplifies a rather complicated process and makes it usefully to users of the information (Macintosh, 1996).

This study involved qualitative and quantitative data analysis with the aid of conceptual model and analytical model. Measures of central tendency were calculated and thereafter dependent and independent variables correlated to establish the relationship. The data was analyzed using Microsoft excel spreadsheet and Statistical package for social sciences (SPSS) computer package.

3.5.1 Conceptual Model

Dependent variable for this model was percentage change in FDI inflows expressed as a function of percentage changes in tax incentives.

Equation 1.0: Conceptual model equation

\[ y = f(x_1, x_2, x_3, x_4, x_5, x_6) \]

In this model \( y \) represented percentage change in FDI inflows, while \( x \) represented percentage change in tax incentives. Investments variable were measured using ROI ratios of sampled firms while tax incentives variable were be measured using actual allowances deducted during the year. Theoretically in a developing country, change in FDI inflows is triggered by Political stability; good Infrastructure; cost of doing business and investment incentives (AAI and TJN-A, 2012).
3.5.2 Analytical Model

After tabulating and analyzing data collected, analytical model were estimated. Percentage changes in dependent variable was multiplied by respective correlation coefficients and then summed up together with the error term and the constant term to arrive at percentage change in FDI inflows. The analytical model used in the study is explained below.

**Equation 2.0: Analytical model equation**

\[ y = \beta_0 + \beta_1 x_1 + \beta_2 x_2 + \beta_3 x_3 + \beta_4 x_4 + \beta_5 x_5 + \beta_6 x_6 + \varepsilon \]

\( y = \) Percentage Change in FDI inflows

\( \beta_0 = \) Constant Term

\( \beta = \) Correlation Coefficients

\( \varepsilon = \) Error Term

\( x_1 = \) Percentage Change in Wear and Tear Allowances

\( x_2 = \) Percentage Change in Industrial Building Allowances

\( x_3 = \) Percentage Change in Tax Exemptions

\( x_4 = \) Percentage Change in Corporate Tax Rates

\( x_5 = \) Percentage Change in EPZ Allowances

\( x_6 = \) Percentage Change in Investment Deductions

The t-test was computed to test hypothesis that tax incentives have little impact on FDI inflows at NSE and results to revenue losses by the government. In addition to t test, R
square test and ANOVA test of hypothesis was also computed. The tests were conducted on tax incentives and FDI variables across year 2008 - 2011. This gave a statistical strength on the relationship between FDI inflows and tax incentives. The decision to reject or accept the null hypothesis was at 95% confidence level.

3.6 Data Validity and Reliability

To control for data validity and reliability, the study used data collection forms targeting for specific information required for the study. The forms consist of two sections; section A and B. Section A covered company profile while section B sought to establish the impact of tax incentives on FDI inflows at NSE. The target information was data on ROI, tax incentives claimed and investments in property plant and equipment. Data collected was then counterchecked for consistency and accuracy. The data was obtained from audited financial statements; reports from KNBS, KRA, IMF, OECD, World Bank and previous research on this topic both published and unpublished.
CHAPTER FOUR
DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter presents data analysis, results and discussion. It is organized as follows: section 4.2 presents summary of the statistics from data collected, section 4.3 presents impacts of tax incentives on foreign direct incentives, section 4.4 discusses the results and finally section 4.5 gives a summary of the chapter.

4.2 Summary of Statistics

This section analyzes the summary of statistics used to make an inference on the impacts of tax incentives on foreign direct investments at NSE.

Table 1.0: Distribution by Industry

<table>
<thead>
<tr>
<th>Sector</th>
<th>Frequency</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Agricultural</td>
<td>1</td>
<td>10%</td>
</tr>
<tr>
<td>Commercial and services</td>
<td>1</td>
<td>10%</td>
</tr>
<tr>
<td>Automobiles and accessories</td>
<td>1</td>
<td>10%</td>
</tr>
<tr>
<td>Banking</td>
<td>1</td>
<td>10%</td>
</tr>
<tr>
<td>Investment</td>
<td>1</td>
<td>10%</td>
</tr>
<tr>
<td>Insurance</td>
<td>1</td>
<td>10%</td>
</tr>
<tr>
<td>Manufacturing and allied</td>
<td>4</td>
<td>40%</td>
</tr>
<tr>
<td>Total</td>
<td>10</td>
<td>100%</td>
</tr>
</tbody>
</table>

Source: Author computation

Table 1.1 represents various sectors from which data was collected. More weight has been given to manufacturing and allied sector since major investment based tax
allowances are biased towards this sector. The same has also been presented below in form of a pie chart on figure 1.1.

**Figure 1.0: Distribution by industry**

![Distribution by industry chart]

Source: Author computation

**Figure 2.0: Tax incentives available at Nairobi securities exchange**

![Tax incentives chart]

Source: Author computation
Figure 2.0 above reveals that 80% of firms studied claimed investments deductions with a 100% of the firms claiming industrial building deductions and wear and tear allowances. No observations were made on manufacturing under bond, mining allowance and export processing zone allowances.

**Figure 3.0: Percentage change in the level of FDI inflows**

![Graph showing percentage change in FDI inflows from 2008 to 2011](image)

Source: Author computation

Figure 3.0 above shows insignificant change in the level of foreign direct investments between years 2008-2011, the range is -0.01% to 0.51%. There was a fall in FDI inflow level in 2008 to 2009, and then there is a sharp rise between years 2009 to year 2010, which then starts to fall later in the year. It is observed that there is no uniform trend in FDI inflows during the period of study.
Table 2.0: Percentage Change in tax allowance claims

<table>
<thead>
<tr>
<th>Tax allowances</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wear and tear allowance</td>
<td>0.0000%</td>
<td>-0.5005%</td>
<td>3.0034%</td>
<td>0.1211%</td>
</tr>
<tr>
<td>Industrial building allowances</td>
<td>0.0000%</td>
<td>1.4916%</td>
<td>1.5233%</td>
<td>0.1759%</td>
</tr>
<tr>
<td>Investment deductions</td>
<td>0.0000%</td>
<td>-0.9911%</td>
<td>1.4800%</td>
<td>0.2970%</td>
</tr>
<tr>
<td>Manufacturing under Bond</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
</tr>
<tr>
<td>Mining allowance</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
</tr>
<tr>
<td>Export processing zones</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
</tr>
<tr>
<td>Mean</td>
<td><strong>0.0000%</strong></td>
<td><strong>0.0000%</strong></td>
<td><strong>0.0000%</strong></td>
<td><strong>0.0000%</strong></td>
</tr>
</tbody>
</table>

Source: Author computation

Table 2.0 above reveals a zero percent average change in tax allowances between years 2008 to 2011. This is mainly because capital allowances are claimed at a fixed rate throughout the life of an asset. This depicts that there was no significant change in the level of investment among the firms studied.

Table 3.0: Average return on investment

<table>
<thead>
<tr>
<th>Year</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Mean</td>
<td>6.8293%</td>
<td>5.5646%</td>
<td>6.1069%</td>
<td>5.4370%</td>
</tr>
</tbody>
</table>

Source: Author computation

Return on investments is the firm’s profit after tax expressed as percentage of total assets of the firm. Table 3.0 above reveals that there was insignificant level of investment between years 2008 to 2011. Investments over this period would have resulted to increase in total assets of firms studied and hence and reduction in profit after tax as a result of increase tax allowances. This could have in turn affected the average return on
investment rate across the period. However, there is possibility of compensating error whereby there could be uniform additional investments across the firms and thus lender this observation irrelevant. Figure 4.0 below depicts average return on investment movement in a graphical form; the range is between 5% and 7%.

Figure 4.0: Average return on investment
Figure 5.0: Extent of tax incentives contribution towards FDI inflows

Source: Author computation

Figure 5.0 above reveals that based on analysis of data collected export processing zone allowances, mining allowances and manufacturing under bond allowances has not contributed to attracting FDI inflows. Investment deduction, wear and tear allowances and industrial building deductions have contributed either by moderate or less extent towards attracting FDI inflows.

4.3 Estimated Model for Impacts of Tax Incentives on FDI Inflows

To measure the impacts of tax incentives on foreign direct investment an empirical model was estimated. The model used data on percentage change in wear and tear allowances; industrial building allowances; tax exemptions; corporate tax rates; EPZ allowances and investment deductions. The percentage change in tax incentives were multiplied by the
respective correlation coefficient and summed up together with an error term and a constant term to arrive at a percentage change in FDI inflows. Table 4.0 to table 8.0 below summarizes key statistics used in the model.

**Table 4.0: Descriptive statistics**

<table>
<thead>
<tr>
<th>Variables</th>
<th>Mean</th>
<th>Standard Deviation</th>
<th>N</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI</td>
<td>5.7455</td>
<td>3.6272</td>
<td>4</td>
</tr>
<tr>
<td>Wear and tear allowance</td>
<td>0.6560</td>
<td>1.5879</td>
<td>4</td>
</tr>
<tr>
<td>Industrial building allowances</td>
<td>0.0360</td>
<td>1.2344</td>
<td>4</td>
</tr>
<tr>
<td>Investment deductions</td>
<td>-0.6920</td>
<td>0.6697</td>
<td>4</td>
</tr>
<tr>
<td>Manufacturing under Bond</td>
<td>0.0000</td>
<td>0.0000</td>
<td>4</td>
</tr>
<tr>
<td>Mining allowance</td>
<td>0.0000</td>
<td>0.0000</td>
<td>4</td>
</tr>
<tr>
<td>Export processing zones</td>
<td>0.0000</td>
<td>0.0000</td>
<td>4</td>
</tr>
</tbody>
</table>

Source: Author computations

**Table 5.0: Pearson Correlations**

<table>
<thead>
<tr>
<th>Pearson Correlations</th>
<th>FDI</th>
<th>Wear and tear allowances</th>
<th>Industrial building allowances</th>
<th>Investment deductions</th>
</tr>
</thead>
<tbody>
<tr>
<td>FDI</td>
<td>1.0000</td>
<td>-0.9620</td>
<td>-0.5700</td>
<td></td>
</tr>
<tr>
<td>Wear and tear allowances</td>
<td>0.9880</td>
<td>1.0000</td>
<td>-0.9170</td>
<td>-0.6800</td>
</tr>
<tr>
<td>Industrial building allowances</td>
<td>-0.9620</td>
<td>-0.9170</td>
<td>1.0000</td>
<td>0.3320</td>
</tr>
<tr>
<td>Investment deductions</td>
<td>-0.5700</td>
<td>-0.6800</td>
<td>0.3320</td>
<td>1.0000</td>
</tr>
</tbody>
</table>

Source: Author computations
Table 6.0: t test values

<table>
<thead>
<tr>
<th>Tax incentive</th>
<th>t</th>
<th>df</th>
<th>Sig. (2 Tailed)</th>
<th>Mean difference</th>
<th>95% Confidence interval of the difference</th>
<th>Lower</th>
<th>Upper</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wear and tear</td>
<td>0.8260</td>
<td>3</td>
<td>0.4690</td>
<td>0.6560</td>
<td>-1.8707 - 3.1827</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industrial building</td>
<td>0.0580</td>
<td>3</td>
<td>0.9570</td>
<td>0.3065</td>
<td>-1.9281 - 2.0002</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment deductions</td>
<td>-2.0670</td>
<td>3</td>
<td>0.1310</td>
<td>-0.6920</td>
<td>-1.7576 - 0.3735</td>
<td></td>
<td></td>
</tr>
<tr>
<td>FDI</td>
<td>3.1660</td>
<td>3</td>
<td>0.0510</td>
<td>0.0510</td>
<td>-0.0262 - 11.5172</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Author computations

Table 7.0: ANOVA table for testing hypothesis

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of squares</th>
<th>df</th>
<th>Mean square</th>
<th>F</th>
<th>Sig</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>39.3330</td>
<td>2</td>
<td>19.6670</td>
<td>143.1200</td>
<td>0.5900</td>
</tr>
<tr>
<td>Residual</td>
<td>0.1370</td>
<td>1</td>
<td>0.1370</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>39.4710</td>
<td>3</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: Author computations

Table 8.0: R square table for testing hypothesis

<table>
<thead>
<tr>
<th>R</th>
<th>R Square</th>
<th>Adjusted R square</th>
<th>Std Error of the estimate</th>
<th>R square Change</th>
<th>F change</th>
<th>df1</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.998</td>
<td>0.997</td>
<td>0.99</td>
<td>0.37069</td>
<td>0.997</td>
<td>143.12</td>
<td>2</td>
</tr>
</tbody>
</table>

Source: Author computations
4.4 Discussion of Results

This section discusses the variables explained in the estimated model. These include: wear and tear allowance; industrial building allowance; investment deductions; mining allowances; export processing zones and foreign direct investments variables.

4.4.1 Wear and Tear Allowance

Analysis of the results shows a positive relationship between Wear and tear allowances and FDI inflows. This means that between years 2008 - 2011 wear and tear allowances attracted FDI inflows at firms operating at the NSE; a correlation coefficient of 0.988 which is almost equal to perfect correlation. A test on hypothesis that wear and tear allowance has little effect on attracting FDI inflows gives a t value of 0.826 which falls with the lower and upper limit at 95% confidence level. Therefore the null hypothesis is rejected.

The results also reveal that 100% of the firms studied claims wear and tear allowances. Wear and tear allowance is easier to qualify for claim as it is at commissioners of income tax specified rates and one only need to proof the asset is used for commercial purposes only. The rest of the tax allowances have to meet specified criteria in order to be allowed as a deduction to tax payable.

4.4.2 Industrial Building Allowances

There is a negative correlation between industrial building allowances and FDI inflows at NSE. The correlation coefficient of -0.9620 can be interpreted to mean that the two variables have no significant relationship.
The results of data analysis give industrial building allowance variable a t value of 0.058 which falls within the lower and upper boundary at 95% confidence level. Therefore the null hypothesis that industrial building deduction has little effect on FDI inflows at NSE is rejected.

4.4.3 Investment Deductions

There is no relationship between investment deductions and FDI inflows at the NSE. A correlation coefficient of -0.5700 reveals that the two variables have no direct association.

The t value for investment deduction is -2.067 which falls outside the 95% confidence interval level. Therefore the null hypothesis that an investment deduction has little effect on FDI inflows at NSE is accepted.

4.4.4 Mining Allowances

There was no significant information from the sample studied that could be used to measure the impact of mining allowances on FDI inflows at NSE. This could be because there are few mining companies listed at NSE.

4.4.5 Export Processing Zones

There was no significant information from the sample studied that could be used to measure the impact of EPZ allowances on FDI inflows at NSE. This can be attributed to few firms operating at EPZ zones and are not listed at the NSE.
4.5.6 Foreign Direct Investments Inflows

The t value for FDI inflows is at 3.166 and it falls within the 95% confidence interval level and thus depicting that tax incentives indeed has an impact of FDI inflows in overall. The null hypothesis that a tax incentive has little impact on FDI inflows is therefore rejected. The ANOVA test and R square test results were also consistent with this observation.

4.5 Summary

The results show a strong relationship between wear and tear allowances and FDI inflows and a negative relationship between Investment deductions, industrial building deductions against FDI inflows. This is because a majority of firms studied (100%) claim wear and tear allowances compared to Investment deductions and industrial building allowance.

It is evident from the study that tax incentives have an impact of FDI inflows at NSE. However analysis of percentage change in FDI inflows between years 2008 – 2011 suggests otherwise. The observed range was - 0.01% to 0.51%, which is an insignificant. This implies that there are other factors that contribute to foreign direct investments inflows apart from tax incentives. These could be social, security and political stability of the investment destination.
CHAPTER FIVE

SUMMARY AND CONCLUSION

5.1 Introduction

This chapter presents summary and conclusion of the research findings. It is organized as follows: Section 5.2 gives a summary of the study; section 5.3 gives a conclusion; section 5.4 presents the limitation of the study and finally section 5.5 gives a recommendation for further study.

5.2 Summary of the Study

The objective of the study was to establish the impact of tax incentives on FDI inflows at NSE and answer the question: Do tax incentives have any impact on foreign direct investments inflows at Nairobi securities exchange?

A quantitative and descriptive approach was used to evaluate available tax incentives based on their impact towards attracting FDI inflows at the NSE. The unit of study was 61 firms listed at NSE, from which a sample of 10 firms was draw using simple random sampling technique. Secondary data was collected with an aid of a data collection form and then analyzed using statistical package for social sciences (SPSS). Measures of central tendency were computed and correlation analysis done to establish the relationship between FDI inflows and tax incentives. To give a statistical strength on the relationship, t test, R square test and ANOVA test statistics were computed.
The analysis of the results from the study has shown that tax incentives have a positive impact in attracting FDI inflows at the NSE. However, the level of significance is also crucial as it has to outweigh the revenue lost by the government in terms of tax exemptions and allowances. The observed range for percentage change in FDI inflows which is -0.01% to 0.51% is insignificant compared to tax allowances claimed within the period of study.

The results are consistent with studies from developed countries which show that tax incentives attract FDI inflows. However, it is clear that tax incentives alone cannot lead to significant FDI inflows. It has to be in combination with other factors such as political stability, security and good infrastructure.

**5.3 Conclusion**

The research findings have proofed a positive relationship between tax incentives and FDI inflows at the NSE. However, the level of significance on average FDI inflows is very low compared to tax allowances advanced to various sectors during the period of the study.

There is need to conduct a cost benefit analysis for tax incentives available to various sectors of the economy. The benefits accrued in terms of increase in level of investments should exceed revenue forgone by the government through tax exemptions and allowances. The government should also ensure that the investment environment is conducive by ensuring security and political stability and also improving on infrastructure.
5.4 Limitations of the Study

The time available was one of the limitations of the study. The research was only able to study a sample of 10 firms listed at the NSE for a time period of four years.

The study focused on quantifiable factors only, these included tax incentives ROI and FDI inflows trends between years 2008 -2011. It is evident from the results of the study that there are other unquantifiable factors that attract FDI inflows.

5.5 Recommendations for Further Research

Research on impacts of tax incentives on FDI inflows in developing countries is at its infant stages. Further research should be conducted by increasing the scope and modifying the model used to include more variables. A measure of social and political factors would be indeed helpful if incorporated in the model.
REFERENCES LIST


36


APPENDICES

APPENDIX I: NSE Listed Companies

1) Eaagads Ltd – Agricultural
2) Kapchorua Tea Co. Ltd – Agricultural
3) Kakuzi – Agricultural
4) Limuru Tea Co. Ltd – Agricultural
5) Rea Vipingo Plantations Ltd – Agricultural
6) Sasini Ltd – Agricultural
7) Williamson Tea Kenya Ltd – Agricultural
8) Express Ltd - Commercial and services
9) Kenya Airways Ltd - Commercial and services
10) Nation Media Group - Commercial and services
11) Standard Group Ltd - Commercial and services
12) TPS Eastern Africa (Serena) Ltd - Commercial and services
13) Scangroup Ltd - Commercial and services
14) Uchumi Supermarket Ltd - Commercial and services
15) Hutchings Biemer Ltd - Commercial and services
16) Longhorn Kenya Ltd - Commercial and services
17) AccessKenya Group Ltd - Telecommunication and technology
18) Safaricom Ltd - Telecommunication and technology
19) Car and General (K) Ltd - Automobiles and accessories
20) CMC Holdings Ltd - Automobiles and accessories
21) Marshalls (E.A.) Ltd - Automobiles and accessories
22) Sameer Africa Ltd - Automobiles and accessories
23) Barclays Bank Ltd – Banking
24) CFC Stanbic Holdings Ltd – Banking
25) Diamond Trust Bank Kenya Ltd – Banking
26) Housing Finance Co Ltd – Banking
27) Kenya Commercial Bank Ltd – Banking
28) National Bank of Kenya Ltd – Banking
29) NIC Bank Ltd – Banking
30) Standard Chartered Bank Ltd – Banking
31) Equity Bank Ltd – Banking
32) The Co-operative Bank of Kenya Ltd – Banking
33) Jubilee Holdings Ltd – Insurance
34) Pan Africa Insurance Holdings Ltd – Insurance
35) Kenya Re-Insurance Corporation Ltd – Insurance
36) CFC Insurance Holdings – Insurance
37) UAP holdings Limited - Insurance
38) British-American Investments Co. (K) Ltd – Insurance
39) CIC Insurance Group Ltd – Insurance
40) City Trust Ltd – Investment
41) Olympia Capital Holdings Ltd – Investment
42) Trans-Century Ltd – Investment
43) Centum Investment Co Ltd – Investment
44) B.O.C Kenya Ltd - Manufacturing and allied
45) British American Tobacco Kenya Ltd - Manufacturing and allied
46) Carbacid Investments Ltd - Manufacturing and allied
47) East African Breweries Ltd - Manufacturing and allied
48) Mumias Sugar Co. Ltd - Manufacturing and allied
49) Unga Group Ltd - Manufacturing and allied
50) Eveready East Africa Ltd - Manufacturing and allied
51) Kenya Orchards Ltd - Manufacturing and allied
52) A.Baumann Co. Ltd - Manufacturing and allied
53) Athi River Mining - Manufacturing and allied
54) Bamburi Cement Ltd - Manufacturing and allied
55) Crown Berger Ltd - Manufacturing and allied
56) E.A.Cables Ltd - Manufacturing and allied
57) E.A.Portland Cement Ltd - Manufacturing and allied
58) KenolKobil Ltd - Manufacturing and allied
59) Total Kenya Ltd - Manufacturing and allied
60) KenGen Ltd - Manufacturing and allied
61) Kenya Power & Lighting Co Ltd - Manufacturing and allied

Source: NSE
APPENDIX II: Data Collection Form

SECTION A: COMPANY PROFILE

1) Date when the company was listed __________

2) In which sector of the economy is the organization operating? (Please tick where appropriate)
   
   - Agricultural [ ]
   - Commercial and services [ ]
   - Telecommunication and technology [ ]
   - Automobiles and accessories [ ]
   - Banking [ ]
   - Insurance [ ]
   - Investment [ ]
   - Manufacturing and allied [ ]

SECTION B: IMPACTS OF TAX INCENTIVES ON FOREIGN DIRECT INVESTMENTS INFLOWS AT NAIROBI SECURITIES EXCHANGE

3) What tax incentives are available for the organization? (Please tick where appropriate)

   - Wear and tear allowance [ ]
   - Industrial building allowances [ ]
   - Investment deductions [ ]
   - Manufacturing under Bond [ ]
   - Mining allowance [ ]
   - Export processing zones [ ]
   - Others (If others please specify) _______________________

iv
4) What was the level of FDI inflows for the organization during years 2008-2011?

<table>
<thead>
<tr>
<th>Year</th>
<th>Foreign Direct Investments Inflows (Kshs 000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td></td>
</tr>
<tr>
<td>2010</td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td></td>
</tr>
</tbody>
</table>

5) How much did the organization claim for the following tax incentives, between years 2008-2011?

<table>
<thead>
<tr>
<th>Tax incentive</th>
<th>2008 Kshs (000)</th>
<th>2009 Kshs (000)</th>
<th>2010 Kshs (000)</th>
<th>2011 Kshs (000)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wear and tear allowance</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industrial building allowances</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Investment deductions</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Manufacturing under Bond</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Mining allowance</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Export processing zones allowances</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

6) What was the corporation tax rate for the organization between years 2008 – 2011? (Please tick where appropriate)

25% [ ]

27% [ ]

30% [ ]

Other rate [ ] (If other rate please specify) _____________

7) What was the reported return on investment for the following years?

<table>
<thead>
<tr>
<th>Year</th>
<th>Return on Investment (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2008</td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td></td>
</tr>
<tr>
<td>2010</td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td></td>
</tr>
</tbody>
</table>
8) Based on preliminary analysis using available data to what extent has tax incentives impacted on FDI inflows? (Tick where appropriate along the following scales)

1. Not at all
2. Less extent
3. Moderate extent
4. Large extent
5. Very large extent

<table>
<thead>
<tr>
<th>Tax incentives</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Wear and tear allowance</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2. Industrial building allowances</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>3. Investment deductions</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>4. Manufacturing under Bond</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>5. Mining allowance</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>6. Export processing zones</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

9) Any other comments

________________________________________________________________________
________________________________________________________________________
________________________________________________________________________
APPENDIX III: Raw data

1. Data on return on investments

<table>
<thead>
<tr>
<th>Company</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sasini Ltd</td>
<td>13.7559%</td>
<td>7.0190%</td>
<td>11.5009%</td>
<td>4.7912%</td>
</tr>
<tr>
<td>Kenya Airways Ltd</td>
<td>4.9445%</td>
<td>N/A *</td>
<td>2.7777%</td>
<td>4.4931%</td>
</tr>
<tr>
<td>Car and General (K) Ltd</td>
<td>7.8109%</td>
<td>12.6040%</td>
<td>10.4764%</td>
<td>5.1905%</td>
</tr>
<tr>
<td>Diamond Trust Bank Kenya Ltd</td>
<td>1.8247%</td>
<td>1.8750%</td>
<td>2.7330%</td>
<td>2.4654%</td>
</tr>
<tr>
<td>Trans-Century Ltd</td>
<td>7.4852%</td>
<td>2.6851%</td>
<td>4.1673%</td>
<td>2.8337%</td>
</tr>
<tr>
<td>UAP holdings Limited</td>
<td>3.4662%</td>
<td>2.0327%</td>
<td>5.1183%</td>
<td>6.3381%</td>
</tr>
<tr>
<td>British American Tobacco (K) Ltd</td>
<td>9.6512%</td>
<td>11.1070%</td>
<td>11.2706%</td>
<td>12.4451%</td>
</tr>
<tr>
<td>Mumias Sugar Co. Ltd</td>
<td>8.5768%</td>
<td>9.2126%</td>
<td>8.5757%</td>
<td>8.3413%</td>
</tr>
<tr>
<td>Total Kenya Ltd</td>
<td>4.8455%</td>
<td>1.5306%</td>
<td>3.0162%</td>
<td>N/A *</td>
</tr>
<tr>
<td>KenGen Ltd</td>
<td>5.9320%</td>
<td>2.0158%</td>
<td>1.4325%</td>
<td>1.3891%</td>
</tr>
<tr>
<td><strong>Average</strong></td>
<td>6.8293%</td>
<td>5.5646%</td>
<td>6.1069%</td>
<td>5.4370%</td>
</tr>
</tbody>
</table>

N/A * the firm reported losses during this period.

2. Extent of tax incentives contribution towards FDI inflows

<table>
<thead>
<tr>
<th>Tax incentive</th>
<th>Not at all</th>
<th>Less extent</th>
<th>Moderate extent</th>
<th>Large extent</th>
<th>Very large extent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wear and tear allowance</td>
<td>60%</td>
<td>10%</td>
<td>10%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>Industrial building allowances</td>
<td>60%</td>
<td>10%</td>
<td>10%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>Investment deductions</td>
<td>60%</td>
<td>10%</td>
<td>10%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>Manufacturing under Bond</td>
<td>80%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>Mining allowance</td>
<td>80%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>Export processing zones</td>
<td>80%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
</tr>
</tbody>
</table>
3. Percentage Change in tax allowance claims

<table>
<thead>
<tr>
<th>Percentage Change in tax allowance claims</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wear and tear allowance</td>
<td>0.0000%</td>
<td>-0.5005%</td>
<td>3.0034%</td>
<td>0.1211%</td>
</tr>
<tr>
<td>Industrial building allowances</td>
<td>0.0000%</td>
<td>1.4916%</td>
<td>-1.5233%</td>
<td>0.1759%</td>
</tr>
<tr>
<td>Investment deductions</td>
<td>0.0000%</td>
<td>-0.9911%</td>
<td>-1.4800%</td>
<td>-0.2970%</td>
</tr>
<tr>
<td>Manufacturing under Bond</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
</tr>
<tr>
<td>Mining allowance</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
</tr>
<tr>
<td>Export processing zones</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
</tr>
<tr>
<td>Average</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
<td>0.0000%</td>
</tr>
</tbody>
</table>

4. Tax incentive applied by firms studied

<table>
<thead>
<tr>
<th>Tax incentive</th>
<th>Frequency (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wear and tear allowance</td>
<td>100%</td>
</tr>
<tr>
<td>Industrial building allowances</td>
<td>100%</td>
</tr>
<tr>
<td>Investment deductions</td>
<td>80%</td>
</tr>
<tr>
<td>Manufacturing under Bond</td>
<td>0%</td>
</tr>
<tr>
<td>Mining allowance</td>
<td>0%</td>
</tr>
<tr>
<td>Export processing zones</td>
<td>0%</td>
</tr>
</tbody>
</table>
APPENDIX IV: Time Budget

<table>
<thead>
<tr>
<th>Time budget</th>
<th>Concept paper</th>
<th>Research Proposal supervision</th>
<th>Proposal presentation and Moderation</th>
<th>Data Collection and Analysis</th>
<th>Final Research Project Report</th>
</tr>
</thead>
<tbody>
<tr>
<td>May-13</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>June to July</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Aug-13</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sep-13</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Oct-13</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
## APPENDIX V: Finance budget

<table>
<thead>
<tr>
<th>Item</th>
<th>Budgeted Costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internet</td>
<td>6,000.00</td>
</tr>
<tr>
<td>Typesetting, Printing and Binding</td>
<td>10,000.00</td>
</tr>
<tr>
<td>Data collection and analysis</td>
<td>10,000.00</td>
</tr>
<tr>
<td>Miscellaneous</td>
<td>4,000.00</td>
</tr>
<tr>
<td><strong>Total Budget</strong></td>
<td><strong>30,000.00</strong></td>
</tr>
</tbody>
</table>