COMPETITIVENESS OF KENYAN TEXTILE INDUSTRY AT THE INTERNATIONAL MARKETS UNDER THE AFRICA GROWTH AND OPPORTUNITY ACT (AGOA)

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A Research Project submitted in partial fulfillment of the Degree of Masters of Arts in International Studies
DECLARATION

I declare that this research project is my original work and has not been presented for a degree in any other university.

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This research project has been submitted for examination with my approval as university supervisor.

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MR. IKIARA

Sign: ................................. Date: ..............................
DEDICATION

I dedicate this project to my late father. Thank you for everything.
ACKNOWLEDGEMENT

I would like to thank God for giving me the grace for my project. To thank my family for their love, encouragement and support. To my late father thank you for everything.

To my supervisor Mr. Ikiara thank you for your support and guidance.
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ABSTRACT

One of the main advantages of textile and apparel industry was contribution to income generation in by means of providing a market for cotton growers in rural areas. During the post-independence period textile industry grew rapidly in the immediate due to the protection offered to firms under the import substitution strategy. The main objective of the study is to examine the competitiveness of Kenyan textile industry at the international markets under the Africa Growth and Opportunity Act (AGOA). The study adopts a descriptive survey design. This research design is appropriate since the study seek to describe the competitiveness of Kenyan textile industry at the international markets under the Africa Growth and Opportunity Act (AGOA). The target population for the study comprises of official at the Ministry of Foreign Affairs and International Trade and owners of textile companies under the Export Processing Zones (EPZs) and officials at Export Processing Zones. From the findings, . Through AGOA the governments, civil society and the private sector work together in building trade capability and expanding business links amid Africa and the US. Trade capacity increase encompasses technical assistance on world trade rules, customs reform and modernization. It is further driven by industry standards and regulations development, enforcement of intellectual property rights and infrastructure transformation. After successful recovery of Kenya’s garment sector under AGOA, the cotton-to-textile/garment sector is far from realizing its true potential. However, the Kenyan cotton-to-textile/garment market structure has the capability of competing with international markets such as china if well managed. Importation of fabrics by the Kenya garment and apparel sector still remains a big obstacle to the realization of its full potential and producing the right quantities. The study recommends additional investments in infrastructure with a view to benchmarking subsequent rates to international rates; enhance the efficiency of the transport and relate service sectors of the ports, sustain technical skills trainings in order to increase productivity, and sustain reforms in the business environment and business climate including exploring the option of commercial representation in the US market. Further, the cotton-textile chain has to be developed in a wholesome way.
CHAPTER ONE
INTRODUCTION

1.0 Introduction

This chapter introduces the study whose main objective is to examine the competitiveness of Kenyan textile industry at the international markets under the Africa Growth and Opportunity Act (AGOA). The chapter entails: the background of the study, Statement of the Research Problem, objectives of the study, justification of the study, literature review, theoretical framework, hypotheses and the research methodology.

1.1 Background of the study

The garment and textile industry in Kenya has been in existence for a long time. By the year 1954 there were a total of 74 enterprises in Kenya with 2,477 workers\(^1\). Growth of textile industry after independence saw the local availability of fibers such as cotton, wool and sisal while synthetic fibers (nylon, polyester, acrylics) jute and linen as well as dyes, chemicals, and resins were imported.\(^2\) Major textile firms were: Kenya Textile Mills (in Thika), Rift Valley Textiles (RIVATEX), Mountex (in Nanyuki) and Kisumu Cotton Mills (KICOMI). Production stagnated from mid-80 and fell sharply after liberalization in the early 90’s.\(^3\) It was in the year 1984 when policy reform in the Kenyan textile industry started resulting to change of policy to export led industrialization as confined in national development plan of 1984-88. The policy encouraged export promotion creating schemes such as Export Processing Zones (EPZ’s), Manufacturing under Bond (MUB) and Export Compensation Schemes. Markets were

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liberalized through abolition of quantities restrictions and lowering of tariffs to enable exportation of their products.

In 1993, liberalization of the Kenyan Economy enhanced Competition in Kenyan textile industry.\textsuperscript{4} The country saw an increase in the importation of secondhand clothes referred to as “\textit{mitumba}”. These clothes were preferred to locally manufactured clothes since they are high quality and are cheap.\textsuperscript{5} The disparity led to low sales and financial difficulties by the local producers expediting closure of textile firms for instance Heritage Woolen Mills, KICOMI, and Allied Industries Limited.

During the post-independence period textile industry grew rapidly in the immediate due to the protection offered to firms under the import substitution strategy. Government investment in the industry through its parastatal - Industrial and Commercial Development Corporation (ICDC) also facilitated the growth of the garment and textile industry by locating them in major towns in the country. It also had significant shares in textile firms such as Kenya Textile Mills (Thika), KICOMI (Kisumu), Rivatex (Eldoret) and Mountex (Nanyuki).

There were also privately owned garment firms which grew and flourished in the import substitution era. They included among others Yuken, Thika Cloth Mills, United Textile Mills, Sunflag, Spinners & Spinners and Raymonds. Like other manufacturing, garment firms generally benefited from the protectionist policies which were there up to the mid-1980s. As is observed in

\textsuperscript{5} ibid
other manufacturing sectors, the garment and textile industry failure to create strong vertical and horizontal linkages with other sectors left it vulnerable when the protectionist policies were abandoned.\(^6\)

One of the garment and textile industries, EPZ, provides an incentive regime for exporting firms in Kenya with a 10-year tax holiday, unobstructed foreign ownership and employment in addition to freedom of repatriating unlimited amount of earnings. The firms are correspondingly exempt from observing some core labor laws and regulations for instance until 2003, there were no organizations of workers in the EPZ firms by trade unions. Under the US-led African Growth Opportunity Act (AGOA) and the African, Caribbean and Pacific-European Union (ACP-EU) Cotonou Agreement the EPZs enjoys an enormous market prospects presented by the tariff and quota advantages granted.\(^7\) The EPZ factories dominant occupational divisions which are machining, ironing, cutting, packaging, cleaning, quality control, finishing and maintenance.

Africa Growth and Opportunity Act (AGOA) liberalize trade between 38 designated Sub-Saharan African (SSA) countries, Kenya being one of them. The Act was amendment in July 2004 further extending AGOA to 2015 although it originally covered an 8-year period from October 2000 to 2008. Being one of the first SSA countries, Kenya qualified for the AGOA wearing Apparel provision in January 2001.\(^8\) The act helped in exporting textiles and apparel goods considered the country’s dominant export category to the US. \(^9\) The exports which were


US$ 64.4 in the year 2001 rose gradually to US$ 277.2 in the year 2004. AGOA further contributed to increase in the number of manufacturing firms, the value of exports as well as number of employees.

Nevertheless, the advantage to the African countries was hampered by the surge in textile imports from Asia following the end of a global quota system in year 2005. The textile industry was further affected by the removal of the quota restrictions under the World Trade Organization (WTO), 30-year old Multi-Fiber Agreement (MFA) as it exposed the poor African producers from protection stiff competition from Asian mass producers. Further lifting of the quotas in January 2005 meant that Asian countries would enjoy unlimited access to the duty-free market hence rapidly increasing Asia’s textile and apparel exports to Kenya. China which had a total share of 10% in the Kenyan market increased to 33.5% in year 2008. A decline in Kenya’s exports from US$ 270.6 to US$ 248.2 to the US was noted between 2005 and 2007 resulting to Kenya’s EPZ shading jobs as many investors pulled out in October year 2004.

Textile products and especially garments elevate employment and export in many developing countries. Liberalization of the country’s economy in the early 90’s resulted in great competition from imported clothing leading to closure of some textile industries hence affecting the Kenyan textile industry which was one the most important contributors to industrial development. Escalation of volume of exports from Asia threatened firms that were exporting under the

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African Growth and Opportunity Act (AGOA). Kenya’s textile industry’s development which had contributed to 20.7% of total African attire exports to the US was hampered by manpower underdevelopment, high cost of production, competition both in the local and international markets, consumer preference for imported textiles and corruption. This study therefore seeks to examine the competitiveness of Kenyan textile industry in the international trading blocs.

1.2 Statement of the Research Problem

One of the main advantages of textile and apparel industry was contribution to income generation in by means of providing a market for cotton growers in rural areas. The cotton sub-sector has a number of significant connections. Other than it having close touch with the rural farmers, it also has links with manufacturing industries such as textile processing and manufacturing industry, soaps and detergents industry, animal feeds manufacturers, chemicals producers and fats and oils factories. These direct linkages with the textile and apparel processing and manufacturing firms are particularly important for the exploitation of the market opportunities presented by Africa Growth and Opportunity Act (AGOA).

The cotton-to-textile/garment market structure has lacked the kind of market and institutional dynamics required to remain competitive with global players like China, or even with regional competitors such as South Africa and Lesotho. This is after the government of Kenya adopted market liberalization in 1991. The Kenya’s garment sector got it revival in 1994 after the

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United States banned several products asserting transshipping goods from Asia. It has however far from realizing its true potential.

Several studies have been carried out in Kenya regarding the textile industry. Kinyanjui, Lugulu and McCormic\textsuperscript{15} examined the policy and research concerns on clothing and footwear in Kenya, Ikiara and Ndirangu\textsuperscript{16} examined the prospects for Kenya clothing exports under AGOA; Nyang’or\textsuperscript{17} studied the factors influencing consumer’s selection of imported over local clothing among women in Nairobi, Kenya, Elungata\textsuperscript{18} investigated factors influencing the business viability of local Apparel Traders within a liberalized market, Bosibori\textsuperscript{19} examined the training needs of quality control and production managers in clothing industries in Nairobi and, Rael, Maiyo and Beatrice\textsuperscript{20} analyzed the performance and challenges of the Kenyan textile industry in a liberalized economy. However, none of the studies carried out has analyzed the contributions that trade agreements have made in enhancing competitiveness of the Kenyan textile industry. This presents a knowledge gap which this study seeks to bridge by examining the competitiveness of Kenyan textile industry at the international markets under the Africa Growth and Opportunity Act (AGOA).

1.3 Objectives of the Study

The main objective of the study is to examine the competitiveness of Kenyan textile industry at the international markets under the Africa Growth and Opportunity Act (AGOA).

The study will be guided by the following specific objectives:

i. To establish the role played by Africa Growth and Opportunity Act in promoting growth of local textile trade in Kenya in the international markets

ii. To analyses the competitive advantages that Kenyan textile industry has gained in the international markets under Africa Growth and Opportunity Act.

iii. To establish the challenges that Kenyan textile industry has encountered in the international markets under Africa Growth and Opportunity Act.

iv. To recommend policy adjustments that will enhance the competitiveness of Kenyan textile industry at the international markets under the Africa Growth and Opportunity Act.

1.4 Justification and Significance of the Study

The textiles and apparel industry occupy a prominent economic position, in terms of trade, employment and foreign investment, in the economic development of Kenya. However, the combination of international pressures arising from globalization as well as international commercial policies, including tariff and nontariff barrier reduction on the one hand, and national policies on the other, have brought enormous challenges to the contribution of the industry to economic development. The success of the Kenyan textile industry in the global market lies with its access to the European Union (EU), United States of America (USA), and COMESA as well as East African Community (EAC) markets.
It will be vital also to make policy recommendations on how to cushion local manufactures in textile and clothing how to diversify and value addition to compete competitively with new clothes from other countries. To the local firms it is vital to know how to discern opportunities so as to remain relevant in local textile industry and international market. This research project hence contributes to knowledge on international trade.

1.5 Literature Review

This section presents review of empirical literature. The chapter entails Competitiveness of an industry, Factors affecting competitiveness in the Kenyan textile industry, Building an Export Oriented Textile and Clothing Industry through EPZs, Africa Growth and Opportunity Act (AGOA) and Kenyan Textile industry.

1.5.1 Competitiveness of an industry

Existence of a competitive advantage occurs when a firm is able to deliver similar benefits as those presented by competitors although at a low cost (cost advantage), or convey benefits exceeding those of competitors products (differentiation advantage). A competitive advantage enables creation of superior value for the firm’s customers and higher profits for itself. Cost and differentiation advantage describe the firm’s position in the industry or a leader in either cost or differentiation hence referred as positional advantage. Resources and capabilities assist in making competitive advantage in order to achieve either a lower cost structure or a differentiation product. Through a choice of low cost or differentiation a firm places itself in its industry a decision which is a central component of the firm’s competitive strategy.

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Competitive advantage is classified into five categories: product advantage, knowledge advantage, cost advantage, relationship advantage and structural advantage. Creating a superior product of higher value than competitors aids an enterprise in gaining product advantage. For those in the service sector this may be considered a service advantage. Cost advantage is gained if an enterprise cumulative operating costs are lower than competitors further allowing the enterprise to offer products or services at a lower price, take control of its cost and capacity utilization, access unique and cheaper sources of input, gain economies of scale and advance experience curve economies.

Competitive strategy encompasses identification of sources of competition in the continually changing environment before developing strategies that match organizational capabilities to the environmental changes. A firm’s conduct and performance is critically impacted by the environment in which it operates on which could be local, national, regional and/or international subject on the firm’s scope of activities. The environment is constituted of the numerous formal and informal institutions, individually and or interactions with each other. Therefore, local, regional, national, and/or international institutions impact on firm performance, as do firm level institutions (for example management styles and employer-employee relations), market

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institutions (for instance inter-firm relations, supplier and customer relations), and society-level institutions (such as education, the state and others).\textsuperscript{26}

The potential or capability of a firm to survive and grow is represented by the competitiveness at firm level, considering the competition of other firms in the same market and for the same profits.\textsuperscript{27} The competition of firms for markets and resources is reflected in either market shares or in the creation and accumulation rate of comparative advantages, such as innovative products, processes among others dependent on both its performance as well as direct entrepreneurial environment in which it operates and acts. Competitive advantage is also dependent on entrepreneurial competencies exhibited facilitating the much needed thrust. Enterprises must understand the sources of such advantages and utilize them effectively and efficiently so that competitive advantage can be developed and sustained.\textsuperscript{28}

According to Owiye\textsuperscript{29} competitive strategies is important to a firm while developing its fundamental approach to attaining competitive advantage (low price, differentiation, niche), the size or market position it plans to achieve, and its focus and method for growth (sales or profit margins, internally or by acquisition). Profit potential and competitive attractiveness is dependent on the intensity of competition in an industry.\textsuperscript{30} Competitive strategy will succor a firm in retorting to the competitive forces in these markets (from suppliers, new entrants, rivals,

\textsuperscript{26} Whitley (1992), cited in McCormick et al. (2001) , for details regarding this categorization of institutions.
\textsuperscript{28} ibid
\textsuperscript{29} Owiye, P. O. (1999). Why Kenyan Firms are Failing to Compete Effectively Within the Liberalized Trading Environment in Kenya: The Case of Government Owned Sugar Firms, Unpublished MBA Project University of Nairobi.
substitute products and customers). Competitive strategy permits a firm to define its business today and in future, as well as determine the industries or markets to compete with.\textsuperscript{31}

If Enterprises are able to sustain competitive advantage by establishing protections against competitors’ replications or creating cost barriers for competitors then they consequently strengthen their long-term competitive position.\textsuperscript{32} Competitive strategy is intended to give the business a competitive advantage which is a relative competitive position that an enterprise establishes and implements by offering superior value to customers. It also endures its competitive edge in the long run by encouraging barriers to duplications. Corporations create unique competitiveness as a result of fluctuations in business phenomenon and competitive situations.\textsuperscript{33}

\textbf{1.5.2 Factors affecting competitiveness in the Kenyan textile industry}

Kenya’s trade and finance is hampered by corruption and reliance upon several primary goods with dwindling prices.\textsuperscript{34} Other problems facing the industry are high cost of production, unskilled labor, managerial hitches, competition and lack of government support.

\begin{itemize}
\item \textsuperscript{33} \textit{ibid}
\item \textsuperscript{34} Tralaac. (2005). AGOA-Kenya http://www.Agoainfo. com
\end{itemize}
1.5.2.1 High Cost of Production

High cost of production is experienced in industry due to high cost of electricity, technological changes, poor infrastructure, high interest rates and unskilled labor.\(^{35}\) Similar findings are reported by Ikiara & Ndirangu’s\(^ {36}\) study among spinning fabric and garment manufacturing firms in Nairobi, Mombasa, Nakuru, Nanyuki and Athi River. Also, the hardware technology used in the industry comprises of old and obsolete technology. Only a few firms have been able to change this technology since installation because of lack of finance as well as due to high interest rates in addition to the fact that these firms are not allowed importation of duty-free machinery contending the need of new technologies appropriate and critically important in the sector for processing. Ikiara et al.\(^ {37}\) found out that garment producers have newer machinery hence newer technology than yarn fiber manufacturers. Additionally, though threat from China is real as acknowledged EPZ officials the sector continues to witness issues such as delays in port clearance, poor transport and communication systems, high power costs. These issues contribute towards making Kenyan exports competitive.\(^ {38}\) Notably, the cost of electricity in Kenya is five times higher than in South Africa and nearly three times more than in China.\(^ {39}\)


1.5.2.2 Unskilled Labor and Lack of Trained Managers

Poor quality and inadequate supply of labor forced local companies to hire highly paid expatriates is a hindrance in the garment industry.\textsuperscript{40} The recommended training of an average textile worker should be about five years in order to attain the skills and productivity level equivalent to a worker in China a task that Kenyan firms cannot afford since the industry lacks unambiguous human resource development plan.\textsuperscript{41} As reported by the United Nations and the Directorate of Industrial Training the mainstream academic institutions offering courses in the field of textiles have not adequately catered for the industry indicating that the Kenyan University training lack a link to the industries. Retraining of recruits for up to two years is another cost that most employers have to endure in order to equip them with skill.\textsuperscript{42}

1.5.2.3 Competition, Lack of Government Support and Corruption

Competition is experienced in both the import and export markets for yarn, fabric and garment manufacturers.\textsuperscript{43} Elung’ata’s\textsuperscript{44} study among apparel traders in Nairobi found that consumers’ preference affected the type of apparel sold thus requiring importation of apparel as locally made ones hardly met their needs in terms of quality and variety. Apparel traders mainly sold Custom-tailored followed by new-imported then the second-hand apparel. Most locally manufactured apparel that was highly sold were uniforms for schools and work though

\textsuperscript{44} ibid
comprising the least sold apparel in the country. The traders highlighted competition and lack of government support as problems facing them.

According to Ikiara et al.,

competition is both in the import and export markets for yarn, fabric and garment manufacturers. Counterfeit textile products, imports that evade duty and uncontrolled imports of second-hand clothes bring unfair competition in the import market. These firms receive little support from the government. They are also weighed down by trade policies such as payment of import declaration fee which are nonexistent in other competing countries, taxation of second-hand items based on weight rather than value and corruption and delays by Kenya Revenue Authority at entry points. The above problems have all contributed to uncompetitive Kenyan textile products both in the import and export markets.

Among the major factors behind the success of Asian, Caribbean, and South American exporters to the USA are availability of raw materials, high quality products, abundant low and high-skilled labor and good marketing or management. Sufficient numbers of high-skilled workers are needed to spearhead apparel design, equipment maintenance and production and marketing. Most African countries however lack high-skilled workers unlike Asian producers who have special training programs guaranteeing steady supply of middle and high-level management for their textiles and clothing. China on the other hand has the Textiles University of Shanghai.


1.5.3 Building an Export Oriented Textile and Clothing Industry through EPZs

The emergence of Export Processing Zones (EPZs) has accompanied by the shift from an inward to an outward oriented development strategy in Kenya. Implementation of the EPZ programme in Kenya started in the year 1990 and is covered under the Export Processing Zones Act, (Chapter 517) Laws of Kenya. The Act defines EPZs as “…a designated part of Kenya where any goods introduced are generally regarded, insofar as import duties are concerned, as being outside the customs territory but are duly restricted by controlled access…” The objective of the programme is to promote exports, foreign exchange earnings, transfer of technology and skills, employment creation and enhancement of industrialization.47

Other than providing exporting firms with a 10-year tax holiday, giving unrestricted foreign ownership and employment and freedom to repatriate unlimited amount of earnings the EPZ incentive regime is also exempt from observing some core labour laws and regulations. Under EPZ incentive regime, trade unions are not allowed to organize workers in the EPZ firms. However the Factories Act (Chapter 514) is not being enforced in the zones. The EPZs have had massive market prospects as presented by the tariff and quota advantages granted under the agreement by the US-led African Growth Opportunity Act (AGOA) and the African, Caribbean and Pacific-European Union (ACP-EU) Cotonou.48

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The garment and apparel sub-sector have been the fastest growing exports to the US under the program.\footnote{Kelly, K. J. and Munaita, P. (2005). Kibaki Moves to Protest 40000 jobs over threat from China. East African Standard. Retrieved on 3 May 2005 from http://www.allArca.com} The act played has assisted exports of textiles and apparel goods which became the country’s dominant export category to the US.\footnote{Tralaac. (2005). AGOA-Kenya http://www.Agoainfo.com} The number of manufacturing firms, the value of exports and also the number of employees have increased thanks to the facilitation by AGOA.\footnote{ibid} This advantage to the African countries however came under threat from year 2005 as a result of gush in textile imports from Asia.\footnote{Mugambi K. (2005). 2000 Jobs lost in Textile Industry. Daily Nation. Retrieved on June 3, 2005 from http://www.allAfrica.com} Lifting of quotas in January 2005 led to Asian countries enjoying unlimited access to the duty-free market setting the stage for a rapid increase in Asia’s textile and apparel exports to the US. China which had a total share of 10% in the US market raised to 33.5% in 2008.\footnote{Rael, C. Maiyo and Beatrice, E. (2012) Imo The Kenyan Textile Industry in a Liberalized Economy: An Analysis of Performance and Challenges, Journal of Emerging Trends in Economics and Management Sciences (JETEMS) 3 (1): 111-115} A decline in Kenya’s exports to the US was noted as it decreased from US$ 270.6 in 2005 to US$ 248.2 in 2007.

\subsection*{1.5.4 Africa Growth and Opportunity Act (AGOA)}

The African Growth and Opportunity Act (AGOA) is a unilateral trade programme that significantly augments U.S. market access to (currently) 41 Sub-Saharan African (SSA) countries. The Act initially covered an 8-year period from October 2000 to September 2008. It was later amended to further extend AGOA to 2015.\footnote{African Cotton & Textile Industries Federation (ACTIF) (2010). Impact of A goa the Textile and Apparel Industry of Kenya. Available at http://www.competeaf rica.org/Files/ACTIF_report_on_the_Impact_of_AG OA_in_Kenya_on_CTA.pdf} Key changes to AGOA were signed into law on 20 December 2006, extending the garment provisions to 2012. A revised textile
certificate of origin was published to give effect to the "abundant supply" provisions contained in the most recent legislative changes in June 2007 and repealed in 2009.

AGOA builds on prevailing U.S. trade programs through expanding the (duty-free) benefits formerly available only under the Generalized System of Preferences (GSP) program. Under the combined AGOA/GSP program duty-free access to the U.S. market stands at approximately 7,000 product tariff lines, together with the roughly 1,800 product tariff lines added to the GSP by the AGOA legislation. Items such as apparel and footwear, certain motor vehicle components, a variety of agricultural products, wine, chemicals, steel and others are included. The major beneficiary sector since the passing of the AGOA has been the textile sector until January 1, 2005 when textile quotas were phased out. This has been in exception of a few SSA countries endowed with oil and minerals. The SSA AGOA beneficiary countries have faced substantive competition from the more well-organized Far East countries of Asia and China.55

1.5.5 Africa Growth and Opportunity Act (AGOA) and Kenyan Textile industry

The restoration of the textile and apparel industry in Kenya was expedited by the enactment of AGOA which opened up the opportunity for growth. AGOA market assurances fastened the investments in textile and apparel industry in Kenya.56 This short term extensions although welcome don’t give adequate confidence to the private investors. The ongoing liberalization, globalization, and technological advancements albeit simplifying sourcing arrangements give no confidence. The gains of AGOA in the Kenyan textile and apparel sector were reversed after the

expiry of Multi Fibre Agreement (MFA) in 2005. Despite the Kenya Textiles and Apparels Sector having great potential to spur economic growth, the textile sector has been declining over the years from a high of 40 firms to 26 from 2003 to January 2010 causing to decrease in the number of people employed by 5.6%. Investment was also affected as it declined from 8.6 billion shillings in 2004 to 7.6 billion shillings in 2008 which is an average annual decline of 3.04%. A decline by 2.8% and 2.2% of exports of finished goods and imports of raw materials respectively was also reported.\textsuperscript{57}

The extinction of the textile and apparel industry in SSA is likely to further erode the AGOA benefits if AGOA provisions are not protected and extended on a more permanent basis. This will halt the revitalization of the cotton-textile to garment chain which had started taking shape. Extending AGOA on short term basis such as 5 years will intensify the current decline with eventual impact of textile trade thus remaining minimal meaning very little investment in textile manufacture will take place. It can further result to disruption of the cotton-textile chain. Also to be affected by such changes will be the complementary (banking, logistics) as well as related sectors in the value chain (cotton growing, ginning, spinning, and weaving). It is essential therefore to have a more decisive arrangement where AGOA is extended on a more permanent basis. Failure to extend AGOA will confound the textile and apparel contribution to the manufacturing sector in Kenya, thus devastating the Vision 2030 which prioritized textile and apparel in the manufacturing sector in propelling the economy to a 10 per cent growth rate and support the country’s economic growth.\textsuperscript{58} For that reason therefore this study analyzes the

\textsuperscript{57} ibid

competitiveness of Kenyan textile industry at the international markets under the Africa Growth and Opportunity Act (AGOA).

1.6 Theoretical framework

This section presents the theories behind the study. The theories include Adam Smith’s Theory of International Trade; Theory of Absolute and Comparative Advantage and Ansoff Product-Market growth matrix.

1.6.1 Adam Smith’s Theory of International Trade

According to Smith, international trade has the same underlying cause as all kinds of trade. In the wealth of nations, trade is the consequence of the human “propensity to truck, barter, and exchange one thing for another." That however does not imply that there isn’t selfish motive in trade. In contrast, people pursue their own interests whenever they trade with each other. They must benefit from trade or else they would not pursue it. For this matter therefore merchants carry on commerce internationally as from it they earn profits. However, Smith endeavors to show that the society as a whole benefits from international trade and not an individual merchants.

From Smith’s thoughts on the division of labor constitute the basis for his theory of international trade is formed. According to him the greatest improvement in the productive powers of labor are as a result of division of labor. Due to more advanced division of labour, more output with the same amount of labour can be produced. Division of labor produces an increase of the

60 ibid
quantity of work which the same number of people is capable of performing. The division of labor leads to quantitative and qualitative production improvements indicating that output is increased, technological development is stimulated, and workers’ skills and productivity are enhanced. Consequently, economic growth is endorsed while national wealth is increased therefore the more specialization, the more growth.61

As spelt out by Smith, international trade is beneficial for nations for it gives a value to their accompaniments, by exchanging them for something else satisfying a part of their wants, and increasing their delights. The narrowness of the home market hinders not the division of labour in any particular branch of art or manufacture from being carried to the highest perfection. Home consumption may be exceed the by opening a more extensive market for whatever part of the produce of their labour may as it encourages them to improve its productive powers. It further helps to augment its annual produce to the utmost thereby increasing the real revenue and wealth of the society.62

International trade is connected to his ideas of the division of labour63. He argues that, establishment of trade with another nation facilitates an extension of the division of labour making it possible as the international market is bigger than the domestic market alone. International trade has enhanced division of labour thus advantageous to a nation because it leads to a growth of the exchangeable value of the annual produce of the land and labour of the country. Accordingly the real wealth of the nation and its population rises. The quantitative and

qualitative benefits of an extended division of labour are exploited by International trade for it leads to an increase in specialization that raises productivity through technical and organizational innovations. Thus, more goods can be produced overall with the same amount of labour. Activating the resources and encouraging the industry boosts economic development.\textsuperscript{64}

The gains from international trade are reinforced by the increased competition that which confronts domestic producers. Since international trade decreases the likelihood of domestic monopolies International trade is at an advantage. As argued by Smith\textsuperscript{65} free competition is always beneficial to the public though frequently not in the interest of the producers. He also mentions an additional beneficial aspect of international trade such as knowledge and technology transfers between different nations. Productivity growth, economic development and an increase in wealth is as a result of adoption and use of new production techniques. For a big nation these gains can even be more important other than access to a wider market. International trade is therefore beneficial to both the individual nations and the world as a whole. Smith says that it is always more advantageous to trade with a more developed nation that has a more mature economy, as it is more developed and has generally bigger market enabling a more advanced division of labour.


1.6.2 Theory of Absolute and Comparative Advantage

The trade theory of absolute advantage was developed by Smith a Scottish economist\textsuperscript{66}. From his argument greater output of a good or service are produced by a country that has an absolute advantage as opposed to other countries still having the same amount of resources. He suggested that tariffs and quotas should be allowed to flow according to market forces but should not restrict international trade. Smith argued that a country should concentrate on production of goods in which it holds an absolute advantage. Countries with no absolute advantage in the production of any goods or services are not considered by this theory as they lack benefit of trade existence of trade itself.

Ricardo\textsuperscript{67} in regards to Comparative Advantage contends that a country should produce and specialize in goods and service it produces most efficiently then purchase those that it produces less efficiently making comparative advantage proposition incredibly counterintuitive. Less developed country have an option of engaging in mutually beneficial trade that lacks an absolute advantage in any good, while an advanced country with more efficient domestic industries than those in any other country may benefit from trade whilst some of its industries face intense import competition.\textsuperscript{68}

This study adopts theory of absolute advantage as a basis for competitiveness of Kenya textile industry. With reference to the theory of absolute advantage, the Kenya textile industry can gain


an absolute advantage over other counties by implementing appropriate marketing strategies. On
the other hand the study uses the theory of comparative advantage to argue that Kenya textile
industry can specialize on efficient utilization of locally produced raw materials to gain absolute
advantage over counties who do not produce the same raw materials.

1.6.3 Ansoff Product-Market growth matrix
Igor Ansoff created Ansoff Product-Market growth matrix which is a marketing tool.\textsuperscript{69} Used in
new or existing markets the matrix permits firms in considering the growth of new or existing
products. It consists of four strategies: Market penetration, product development, market
development and product diversification. Through Market penetration strategy sales volume
already on the market are increased. The strategic objective consists of obtaining a market share
or the position of market leader. Sales are increased by Product development strategy through
improvement of an existing product or by creation of a new product fitting demands of the
market. Market development strategy increases sales by improving an existing product via
penetration of new markets by geographical expansion. Product diversification strategy extends
business portfolio by use of technology and new distribution channels to add new product.

Market penetration strategy also termed as concentrated growth strategy since a firm thoroughly
develops and exploits their knowledge and expertise in a specific market with known products.\textsuperscript{70}
One of its goals is increasing the present customers’ rate of use through growing the size of the
purchase, maximizing the rate of product obsolescence, finding new users for your product,
advertising other uses besides offering incentives for increased use. Attracting competitors’

\textsuperscript{70} ibid
customers by establishing differentiation from them, increasing advertising efforts or reducing on your prices is yet another goal. Another goal is to attract new users to buy your products which can be achieved by showing trial uses of products, adjusting the price while promoting other uses aimed at attracting the customers.

Due to changes in advances in technology, increasing competition and consumer preferences, then Product development flourishes. Other than covering never introduced products in the market and product innovations on new products it also covers existing products which have been modified and improved. Leveraging these three internal elements i.e. technical advantage and experience, marketing savvy and better understanding of the customer results in successful product development strategies. The option open are divided into two basic strategic paths, either the introduction of products similar to current offerings known as “line extension” or new products in the market. Line extensions can be further sub-divided into four extensions: low-end products, new generation products, breakthrough products and high end products.\textsuperscript{71}

Market development strategy for a current product is achieved through new users in new geographic segments, new demographic segments, new institutional segments or new psychographic segments. The target customer which is the starting point influences all subsequent elements of the strategy statement as the compelling reason to buy explains the buyer motivation therefore the source of demand. Partners and allies are obligated in providing parts of the whole product. The distribution channel acts as a function of both the solution and marketing complexity that delivers the whole product. Determining the pricing and revenue model is a

function associated with the target customer’s perceived value. Analyzing potential competition for the target market reference requires economic competition to be put into consideration. Positioning must discover your product as more attractive as compared with the competition’s in the target market.\textsuperscript{72}

1.7 Hypothesis

The study will test the following null hypotheses

$H_{01}$: Africa Growth and Opportunity Act has not played a major role in promoting growth of local textile trade in Kenya in the international markets

$H_{02}$: The Kenyan textile industry has not gained competitive advantages in the international markets under Africa Growth and Opportunity Act

$H_{03}$: The Kenyan textile industry has not encountered challenges in the international markets under Africa Growth and Opportunity Act

1.8 Research Methodology

1.8.1 Research Design

The study adopts a descriptive survey design. This research design is appropriate since the study seek to describe the competitiveness of Kenyan textile industry at the international markets under the Africa Growth and Opportunity Act (AGOA).

\textsuperscript{72} ibid
1.8.2 Scope of the Study

The study is restricted to the application of Africa Growth and Opportunity Act in the Kenyan textile industry.

1.8.3 Target Population

The target population for the study comprises of official at the Ministry of Foreign Affairs and International Trade and owners of textile companies under the Export Processing Zones (EPZs) and officials at Export Processing Zones.

1.8.4 Data Collection Instruments and Procedure

This study will draw from both primary and secondary sources of information. Primary data will be derived from interactive interviews with official at the Ministry of Foreign Affairs and International Trade and owners of textile companies under the Export Processing Zones (EPZs) and officials at Export Processing Zones. Secondary data will be sourced from a collection and review of published and unpublished material, journals, academic papers and periodicals. These are taken through intensive and critical analysis.

1.8.5 Data Analysis

The study will collect qualitative data which will be analyzed though content analysis. Content analysis involves systematic and objective identification of special characteristics of a message gathered from written documents and transcriptions of verbal communications.

1.8.6 Limitation of the Research

The main limitation of the study will be difficulty in generalization of study findings because Kenyan textile industry is affects by other trade policies, treaties and trade agreements than the
Africa Growth and Opportunity Act (AGOA) on which the study has focused. However, the study will overcome the limitation by comparing the study findings with other empirical studies on Kenyan textile industry and other trade agreements.

1.9 Chapter Outline

Chapter one presents the introduction to the study which includes: the background of the study, Statement of the Research Problem, objectives of the study, justification of the study, literature review, theoretical framework, hypotheses and the research methodology.

Chapter two will present a discussion on the role played by Africa Growth and Opportunity Act in promoting growth of local textile trade in Kenya in the international markets.

Chapter three will discuss the competitive advantages that Kenyan textile industry has gained in the international markets under Africa Growth and Opportunity Act.

Chapter four will discuss the challenges that Kenyan textile industry has encountered in the international markets under Africa Growth and Opportunity Act.

Chapter five will discuss the study findings on the competitiveness of Kenyan textile industry at the international markets under the Africa Growth and Opportunity Act.

Chapter six will present conclusion and recommendations of the study.
CHAPTER TWO

THE ROLE PLAYED BY AFRICA GROWTH AND OPPORTUNITY ACT IN
PROMOTING GROWTH OF LOCAL TEXTILE TRADE IN KENYA IN THE
INTERNATIONAL MARKETS

2.0 Introduction


2.1 AGOA’S Main Provisions on apparel trade

Sub-Saharan African countries had access to the U.S. market (essentially paying a zero tariff subject to certain conditions) for a range of exports under the Generalized System of Preferences (GSP) before the introduction of AGOA.73 Out of Africa’s total exports of US$23 billion, the GSP covered about US$4 billion in the year 2000. The margin of preference which is the advantage enjoyed by African exporters in comparison to other most-favored nation (MFN) suppliers was about 5 percent (the average MFN tariff rate). AGOA represents two advances

over the GSP scheme: first, the existing preferential access enjoyed by Sub-Saharan African (SSA) countries under the GSP scheme has been extended in time; and second, increasing the range of products for which preferential access is granted that include: petroleum products; apparel products, and a range of other agricultural and industrial products which previously enjoyed quotas.\footnote{ibid}

The really important incremental benefits provided by AGOA relate to the two non-petroleum categories in the lightly shaded panel. The first comprises exports of apparel products and the second a whole range of non-apparel products such as footwear, agricultural products, watches etc. Although a number of items in the latter category subject to tariff rate quotas, with out-of-quota tariffs (average and peak) are exceptionally high in numerous cases. In both these categories, potential benefits are large because average protection is high even if current exports are low. The actual protection is considerably higher owing to the quotas on exporters under the MFA. Elimination of this protection would result to a substantial increase in exports. A key determinant of these benefits however will be the rule of origin to be met by African exporters in an effort to qualify for the duty free treatment.\footnote{Mattoo, A., Roy, D., and Subramanian, A. (2002). The Africa Growth and Opportunity Act and Its Rules of Origin: Generosity Undermined? World Bank Policy Research Working Paper 2908, October 2002.}

The crucial rules of origin that African exporters have to meet include the extension of access to apparel and other products and the benefits of the incremental coverage under AGOA. These rules vary across these two categories of exports. Provisions on rules of origin relating to apparel
by AGOA’s are:76 products with unrestricted access include apparel assembled from U.S. formed and cut fabric from U.S. yarn, apparel assembled and further processed from U.S. formed and cut fabric from U.S. yarn, apparel cut and assembled from U.S. fabric from U.S. yarn and thread, cashmere sweaters, merino wool sweaters, knit to shape, with fibers 18.5 microns or finer. Apparel assembled from regional fabric from U.S. or African yarn attract tariff rate quota that grows from a cap of 1.5 to 3.5 percent of total U.S. apparel imports which have recently been doubled. The provision also sees unrestricting of four years for apparel assembled in a lesser developed country by use of foreign fabric or yarn nonetheless exports counted against the 1.5 to 3.5 percent caps.

According to AGOA’s provisions on rules of origin relating to apparel it essentially requires that apparel be assembled in eligible sub-Saharan African countries in addition to the yarn and fabric being made in either the United States or in other African countries. However, apparel imports made with regional (African) fabric and yarn are subject to a cap of 1.5 percent of overall U.S. imports, which has grown to 3.5 percent of overall imports over an 8-year period. To receive the apparel and textile benefits of AGOA, a USTR-chaired inter-agency committee must determine, inter alia, that countries have an effective visa system and enforcement procedures to prevent unlawful transshipment and the use of counterfeit documents.

In 2002, the AGOA law was amended to further increase market access for products from sub-Saharan Africa this being one of the many amendments that have been carried out since 2000. In 2004, Congress passed legislation to extend AGOA benefits beyond the original deadline and to

clarify certain provisions. Others on legislation list were directives to the President regarding investment initiatives and technical assistance. Congress passed legislation in 2006 to further amend AGOA, and extend certain provisions concerning textile and apparel imports to 2012. This provision was recently extended through September 2015.77

AGOA provisions allow for duty-free and quota-free treatment for —qualifying articles, which include: apparel made of United States yarns and fabrics; apparel made of sub-Saharan African yarns and fabrics (subject to a cap); apparel made of yarns and fabrics not produced in commercial quantities in the United States; textile or textile articles originating entirely in one or more lesser-developed beneficiary sub-Saharan Africa countries; certain cashmere and merino wool sweaters; and eligible hand loomed, handmade, or folklore articles, and ethnic printed fabrics.78

Third-country fabric (TCF) provision, also known as the Special Rule for Apparel, is the root of the AGOA apparel program which allows only least developed AGOA beneficiaries to incorporate yarn and fabric from all over the world including India or China. However, countries that do not enjoy extended preferences available under the TCF provision are those with a per capita gross national product (GNP) of over $1,500 as from 1998.79 This is to mean that those countries that fall outside the TCF provision only use fabric inputs from other AGOA

79 AGOA Apparel Provisions (Eligible Countries – AGOA Preferences Chart). Countries that fall outside of the TCF provision include, for example, Gabon, Seychelles, and South Afric
beneficiaries. AGOA‘s TCF provision has for the matter of fact helped generate hundreds of thousands of jobs in sub-Saharan Africa, while at the same time assisted American retailers in reducing their costs, diversifying their supply chains and provided greater low-cost apparel options for their consumers.80

2.2 Kenyan Textile Industry under African Growth and Opportunity Act

As conveyed by KIPPRA report, the textile sector noted its peak performance in 1984, when the supply cotton production to the domestic textile industry was over 70,000 bales, with 52 textiles mills employing over 42,000 people.81 It also facilitated the textile and clothing industry to being the second largest employer after the civil service. Since then domestic spinning and weaving capacities have considerably reduced from approximately 52 mills in 1984 to only 15 main textile mills that are under capacity. Global Economic Reforms under the Structural Adjacent Programme’s (SAP) and Trade Liberalization of the 1980s/90s led to the collapse of the industry. Another contributing factor to the collapse of the industry was corruption and mismanagement at the defunct Cotton Board of Kenya.

There has been however intermittent recovery and good performance within the context of some regional and international initiatives considerably having a positive effect to the textile industry. With the inclusion of the 3rd country fabric provision that allows the sector to utilize imported fabric from Asia, the garment sector is now performing relatively well under the African Growth and Opportunity Act (AGOA) provision. The garment sector in Kenya has been principally

driven by exports to the US under the AGOA initiative. Unfortunately, the success of the garment industry profits the foreign affiliation while having no direct effect on the existing textile mills in Kenya. No correlated growth of the local mills has been recorded with the main excuse being failure fabric supply to the garment factories exporting to US under AGOA. Fabric sourcing as raw material is an significant factor in textile manufacturing and therefore with no local sourcing of fabric for export manufacturing, there remains seriously broken value chain and disjointed between garment / made ups and other sections of the chain. There has not been any trickle effect to the cotton growing in the country as a result of these impositions. Since Kenya is an agricultural country, an in-depth evaluation of the value chain is needed in order to detect segments of potential economic growth with highest returns so as to strengthen the backward and forward integration linkages.\(^\text{82}\)

Cotton being a basis for industrial transformation the world over for many centuries and also being a strategic crop in Kenya, Vision 2030 and the Government’s medium-term plan 2008 – 2012 identified the cotton industry as an important sector in employment creation, poverty reduction and food security. Other than being suitable to varied agro-ecological zones in the country cotton crop is also a source of raw material to many industries. NESC through the then Office of the Prime Minister worked with a number of sector players in formulating relevant policies and strategies to revive the cotton sector (GOK, 2012). Consequently, in addition to prioritizing cotton/textile industry, the Agricultural Sector Development Strategy (ASDS) 2010-\(^\text{82}\)African Cotton & Textile Industries Federation (ACTIF, 2013). Policy Research on the Kenyan Textile Industry Findings and Recommendations. Charmy Investments Limited, Kenya.
2020 (2009) undertook among other initiatives rehabilitating the irrigation schemes so as to revive irrigated production of various crops cotton being one of them.83

The cotton/textile industry has a potential of contributing over Kshs.4 billion to the gross national income due to the possibility of long value chain ranging from cotton production to finished products. Policy gaps and institutional limitations have hindered full exploitation of this enormous potential. In particular, the lack of a favorable policy environment to stimulate farmers and other stakeholders in promoting production, processing, utilization and marketing makes Kenya cotton/textile products uncompetitive in both local and international markets. The Kenyan government currently does not provide subsidy to the cotton sector in form of: growing cotton, price support for producers, ginning or marketing. It has nevertheless continued to provide funding to the smallholder farmers in form of provision of planting seeds as a food security measure and free advisory service, extension service and research.84

2.3 Depth of AGOA preference - Preference margins

The benefits provided by AGOA, is considered by three studies (all high quality) - Van Grasstek,85 Brenton and Ikezuki86 and Dean and Wainio87 confirming that AGOA preference margins on apparel products are relatively high. This explains the strong import response in the

83 ibid
sector. The average preference margins on agricultural products are also small and there has been little increase in agricultural exports under AGOA.

Brenton and Ikezuki\textsuperscript{88} make a comparison on the margins of preference of the products covered by AGOA to the margins of preference on those covered by GSP. Generally, they find that preferences to products with higher duties are extended by AGOA than those covered by the GSP. For LDCs, the average MFN duty (i.e. preference margin) on the additional agricultural products covered by AGOA is 7.7\% while those covered by the GSP for agricultural products receive 5.2\%. The products excluded from AGOA and GSP are high duty products which could potentially confer very high preference margins if they were included in AGOA. The average duty on excluded agricultural products is 31\% for LDCs and 30.7\% for non-LDCs, with peak rates being extremely high for some products of particular interest to SSA producers. The average duty on products covered by the GSP is 3.8 \%, while those covered by the basic AGOA provisions are subject to an average duty of 6.1\% for manufactured products. Clothing products receive an average duty 12\% on products included in AGOA. So AGOA does reduce the number of tariff peaks facing African exporters to the U.S, particularly so on apparel products.

Two studies (all high quality) - Brenton and Hoppe\textsuperscript{89} and Dean and Wainio\textsuperscript{90} - empirically measure the actual value of AGOA preferences to beneficiary countries. The studies show some

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indication on the extent of preference erosion that might occur if DFQF was permitted in other LDCs, indicating the countries which would be most affected. The study estimate the value of AGOA preferences on a country by country basis for the 37 AGOA eligible countries in 2005 based on their non-oil exports in that year.\textsuperscript{91} The value of preferences is the sum across exported products i.e. for each country getting and using preferences under AGOA multiplied by the preference margin (i.e. the normal MFN rate) for that product.

2.4 Security of Access

Other than establishing a series of eligibility criteria to be met by countries in the programme, AGOA also provides for the removal of noncompliant countries with the requirements. At present 48 countries in SSA are eligible for AGOA, and 27 among these countries are entitled to apparel benefits.\textsuperscript{92} In order to be granted and maintain eligibility, countries need to show that they have established or are making continual progress towards: market-based economies; the rule of law and political pluralism; elimination of barriers to US trade and investment; protection of intellectual property; efforts to combat corruption; policies to reduce poverty, increasing availability of health care and educational opportunities; elimination of certain child labour practices and protection of human rights and worker rights.

Each country’s eligibility is required to be reviewed on an annual basis as recommended by AGOA who directs the President on denying benefits to any country failing to satisfy these


conditions. In December 2009 for example, the US President removed Guinea, Madagascar and Niger from the list of AGOA-eligible countries because of political mayhem in these countries, Mauritania was on the other hand was readmitted to the scheme. Eligibility may also be reconsidered if AGOA threatens U.S industries for instance; domestic import competing sectors in the US may foyer the government to remove preferences from countries that have utilized them effectively to increase exports to the US.93

There is uncertainty around the current and future eligibility status of all AGOA beneficiaries due to AGOA unilateral nature in its agreement, its timeframe and the evident political and commercial conditionality attached to it. Mueller,94 for example, comments on these issues by suggesting that inclusion of both economic and political conditions raises the risk and uncertainty confronted by producers and investors in these countries. Brenton and Ikezuki95 emphasizes investment response to the agreement is constrained by the temporary and relatively short statutory period of AGOA constrains the. Yet no substantive and empirical evidence was found in the literature on how the limited duration and conditionality attached to eligibility have impacted on the effectiveness of AGOA.

2.5 Distribution of preferential tariff rents

Though it is possible that some AGOA beneficiaries may lose the full value of the preference, there are a number of factors which may serve to overstate the value of the preference to the

94 ibid
exporting country (and may therefore reduce the actual cost of preference erosion). It is unlikely however for exporters to receive the full value or rent provided by the preference, and so this rent is shared between exporters, middlemen and/or the US importer.

Olareeaga and Ozden⁹⁶ decompose the increase in prices (what they call the tariff preference rent) on apparel exports to the US under AGOA and measure the proportion of this price increase that actually goes to the beneficiary country. They based their analysis on the exports of the seven leading AGOA apparel exporters to the US in 2002 which are Kenya, Lesotho, Madagascar, Malawi, Mauritius South Africa, and Swaziland. Competition among competing firms in theory should influence an increase in the prices received by exporting firms by the amount of the normal MFN tariff on the product receiving the preference. Their results however show that the average export price rise for apparel products benefitting from AGOA preferences is around 6%, whereas that of MFN tariff on the same products is 20% indicating that exporters receive less than one third of the tariff preference rent.

Their results also indicate substantial variation in the share of the preference rent accruing to exporters across countries, with the LDCs taking a lower portion. An example is Malawi which receives just less than one seventh of the potential preference rent available while Lesotho takes less than a quarter. From the authors perspective the primary reason for this occurrence is due to the high level of concentration and market power amongst importers in the US enabling them to negotiate prices and capture most of the preference rents. The preference rent that is retained by the beneficiary country is therefore dependent upon the negotiating skills, the extent of reliance

on US market and experience of the exporter from SSA. As a result Mauritius and South Africa have strong trade experience since they export to a diversified number of countries thereby capturing over fifty percent of the preference rent.

2.6 Benefits from AGOA

AGOA has had a positive impact on the African continent including a 500% increase in African exports ($8.51 billion in 2001 to $53.8 billion in 2011) as noted by its supporters. Other impacts include creation of as many as 1.3 million jobs thus benefitting 10 million people in the Africa region. United States economy has also profited from AGOA as more than 100,000 jobs in the United States through exports to Africa have been generated. AGOA has resultanty created more than 30,000 jobs through revival of previously idle capacity for textile and clothing manufacturing in Kenya.

According to some people AGOA is one of the best opportunities for economic engagement between Africa and the US. A report by United States Senator Coons of Delaware, Chair of the Senate Foreign Relations Subcommittee on African Affairs, recommended quick reauthorization of AGOA well before its scheduled expiration date of September 2015. The report noted that AGOA was enacted to offer trade preferences and assist African countries in building free

markets and opening the economies. The report pointed out that AGOA has supported a growing African middle class, reduced dependence on development assistance while further opening African markets to American companies.\textsuperscript{100}

2.7 Development of Value Chains through AGOA

AGOA in conjunction with Africa’s regional economic communities i.e., Southern African Development Community (SADC), East African Community (EAC), Common Market for Eastern and Southern Africa (COMESA), and Economic Organization for West African States (ECOWAS), provide enormous potential to develop value chains for many products. This potential has not been realized yet. AGOA export growth in Kenya sharply contrasts the performance at lower levels of the value chain an example being cotton production which falls below 10\% of demand.\textsuperscript{101}

Limited regional trade in raw materials and other inputs has additionally been noted resulting to use of more than 90 percent non-originating raw materials in the Kenyan textile industry.\textsuperscript{102} In Lesotho the overall effect of nascent textile sector is limited to local communities since all


\textsuperscript{102} ibid
AGOA exports are manufactured using multinational (primarily Asian) inputs.\textsuperscript{103} AGOA’s stringent rules of origin requirements have served to stymie export growth potential in South Africa where the TCF provision does not apply, clothing exports are not eligible for AGOA preferences as producers find it cheaper to import fabrics from China.\textsuperscript{104}

\textbf{2.8 AGOA contribution to Foreign Direct Investment (FDI) Diversion}

It was a requirement for domestic and foreign investors seeking to take advantage of AGOA to attract a heave of investments from the United States as African producers sought to expand production in an effort to increase their market share although it has not materialized. Kenya being one of the major AGOA beneficiaries has increased its clothing exports to the U.S 24 by a 400\% rise from a minimal pre-AGOA base where the vast majority of companies involved were recent entrants, and non-nationals setting up shop in EPZs.\textsuperscript{105} AGOA has arguably resulted in allowing profits to be extracted from Africa via FDI although its initial intention was to help alleviate poverty.\textsuperscript{106} Foreign owned factories in the textile and garment industries can quickly dismantle once foreign entrepreneurs are unable to take advantage of the trade preference scheme as they are very mobile. An example being the Caribbean textile industries, which


\textsuperscript{104} ibid

\textsuperscript{105} ibid

experienced a dismantling in the face of NAFTA and Chinese competition after benefiting from the Caribbean Basin Initiative.

In Kenya, out of a total of eighteen apparel producers only one is Kenyan owned.107 The initial AGOA-related investors in Kenya’s were all foreigners. 500% growth in employment occurred due to the textile industry boom while at the same time advancing manufacturing technologies and practices, which when introduced trained the workers accordingly. Flying investors were however among these investors who are known for traveling across the world in search of short-term trade breaks and afterwards leave when such opportunities are exhausted. Kenya which had fallen prey, suffered economically after the United States opened its market in 2005 after it had become a major AGOA beneficiary and banked heavily on its textile industry. Sales, profits, and the workforce plunged since clothing producers could no longer compete.108

2.9 Impact of AGOA on manufactured/apparel exports

53.1% of the increase in apparel exports in the post AGOA that is in between 2000 to 2006 period can be directly attributed to AGOA.109 From Fayissa and Tadesse110 findings, AGOA has been responsible for 43 percent of the increase in apparel exports in the post AGOA period.

Collier and Venables\textsuperscript{111} compare apparel exports under AGOA with those under the EU preferential access program using a triple difference in differences model, Everything But Arms (EBA). Their findings indicate a positive and very substantial effect on apparel exports by AGOA raising apparel exports to the US by almost a factor of seven. This number is much higher compared to estimate by Frazer and Van Biesebroeck as Collier and Venables are able to control better the effects of AGOA through comparing its influence to the EU preferences. Seyoum\textsuperscript{112} through his model test the impact of AGOA on three sectors – energy, minerals and apparel. His results indicate that AGOA-induced statistically significant gains only on apparel exports.

Nouve\textsuperscript{113} model provides a different perspective on AGOA apparel exports as he finds that AGOA apparel exports have a negative effect on overall SSA exports to the US. This contests the earlier views which show the main benefit of AGOA being the rise in apparel exports. He argues that there may have been a reallocation of resources far from other exports so as to sustain AGOA induced increases in apparel exports. Nouve therefore suggests that it is inappropriate to proclaim a positive impact on a given SSA country by concentrating wholly on increased apparel exports. He suggests that it is important to evaluate the impact of the agreement on the entire economy as gains in some sectors could potentially come at the cost of others.

2.10 Local economic impact of AGOA apparel sectors

Broader economic losses outside the export sector concerned can accrue from preference erosion. In the case of AGOA, the actual scale of such economic losses may be less than projected, basically because exporters are not fully integrated into the local economies of many AGOA-qualifying countries. Phelps et al.,114 Rolfe and Woodward115 and Lall116 provide evidence of the limited impact that AGOA has had on local economic development in three country case studies (all high quality) and especially so in the apparel sector.

Phelps et al.117 examine the AGOA-orientated apparel sector in Kenya through a survey and interviews with 23 (of an estimated 35) of its apparel manufacturers. They find very limited evidence of wider local economic benefits. Although considerable direct employment has been created in the sector, this is mostly of an unskilled nature. The industry in Kenya is primarily foreign-owned, with the majority of the new post-AGOA investment in the sector coming from Asian multinational enterprises, mainly from Hong Kong, Singapore and Taiwan. Most of the skilled white collar workers in the sector were expatriates. Moreover, a negligible amount of textiles are sourced locally – again textiles and fabrics are imported from affiliates in their home countries.

Rolfe and Woodward\textsuperscript{118} come to a similar conclusion in their analysis of the Kenyan apparel sector. Using data from the local Export Processing Zone (EPZ) authority in Kenya (data on imports, local components and local salaries) they empirically measure the local value added being generated by this industry. They too find weak linkages with the local economy – the value of local Kenyan components in apparel exports is just three percent of sales value and none of these companies use local textiles and fabrics. In addition, there is little evidence of skills transfer and upgrading in the sector, with most production requiring marginal skills and minimal value added.

The story is little different in Lesotho, the largest beneficiary of AGOA apparel preferences. Lall\textsuperscript{119} finds that the sector is almost entirely owned by East Asian firms, primarily Taiwanese. The majority of these firms had been in place prior to AGOA and this strong base enabled Lesotho to move quickly to take advantage of AGOA apparel preferences. While the sector has created large scale employment, linkages with the local economy and skills transfer is minimal. The author notes that apparel firms make little effort to impart more advanced skills, with training limited to basic production requirements. Most supervisory, technical and managerial jobs remain with expatriates, even within firms that have been in Lesotho for a decade or more. The author also finds little evidence of backward linkages with the local economy, with almost no local firms competing with, supplying, or subcontracting with the foreign firms.

2.11 Conclusion

Even though cotton no longer stands among Kenya’s leading cash crops, such as tea, horticulture, sugar cane and coffee, it was once an important source of income for rural communities’ low agricultural potential areas in addition to being a key source of raw material for a thriving national textile industry. Despite the sector’s decline in recent years, cotton is still considered one of the few cash crops which has actual potential for aggregating employment opportunities and availability of food via income generation in the Arid and Semi-Arid Lands (ASALs) of Kenya (CODA, 2008). Thus, revitalizing the cotton sector is one of the government’s key development and industrialization initiatives to be implemented mainly in the ASAL regions, but also on other high potential areas for this crop, under Kenya’s Vision 2030 strategic plan and it’s Medium Term Plan, 2008-2012.\textsuperscript{120} Contrary to the situation in neighboring cotton producing countries, Kenya is endowed with a well-developed textile industry that requires a constant supply of cotton lint. However, this industry has been operating below capacity, partly due to the low supply of domestic cotton lint.

In 2000, a preferential trade agreement under the African Growth Opportunity Act was signed with the U.S. Government eliminating all duties and quotas that were imposed on Kenyan textile exports to the U.S. market. As a result, Kenya’s textile exports to the U.S. have increased significantly over the past decade.\textsuperscript{121} Despite this growth in exports, very few benefits have been realized by local cotton producers due to the fact that Kenya’s textile industry continues to


import most of its factory inputs rather than purchase domestic cotton lint. As stipulated by the World Bank\textsuperscript{122} and the Cotton Development Authority (CODA),\textsuperscript{123} of the key factors causing poor performance in the cotton sectors include: periodic drought, volatile producer prices, the high cost of pesticides, delayed payments to farmers and lack of access to quality seeds. Other factors are competition over scarce resources with other farm enterprises, downfall of former state-owned textile firms and co-operative societies along with competition from synthetic fiber substitutes and importation of new and second-hand clothes which are cheap.


CHAPTER THREE

THE COMPETITIVE ADVANTAGES GAINED BY KENYAN TEXTILE INDUSTRY IN THE INTERNATIONAL MARKETS UNDER AFRICA GROWTH AND OPPORTUNITY ACT

3.0 Introduction

The chapter discusses the competitive advantages gained by Kenyan textile industry in the international markets under Africa Growth and Opportunity Act. The chapter is structured into The Relevance of AGOA for Textile and Apparel Industry in Kenya, Trade patterns between AGOA-eligible countries (including Kenya) and the United State of America, The socio economic effects of AGOA, and a Case for Moving AGOA beyond Preferential Trade.

3.1 The Relevance of AGOA for Textile and Apparel Industry in Kenya

The third country fabric provision currently extends until 2015 thus explaining why large garment exporters (e.g. from Asia) wish to invest in Kenyan EPZs. This is because their production in Kenya gives them access to the United States market which they might otherwise not have owing to the expiry of Asian importers Multi Fibre Agreement that set their quota. Kenya faces pressure at the moment from garment companies threatening to relocate as the specific advantage Kenya could offer, in relation to the MFA, is vanishing. Moreover, the US is pushing African countries and regions to give extensive opening and BIT-like protection measures to US investments and including it as a condition under AGOA.\textsuperscript{124}

Opportunity for growth and revival of the textile and apparel industry in Kenya were opened up by the enactment of AGOA expanding bilateral trade between Kenya and USA. Kenya is among the main beneficiaries of export textiles to the US under AGOA which constitute all sub-Saharan African countries. AGOA preferences creation of market access for Kenyan textiles made foreign buyers get their supplies at competitive prices from Kenya and were able to place orders as long as AGOA was in operation. Concurrently, competitiveness was also enhanced with decline in unit cost of apparent products. More employees benefitted from the textile value chain as well as complementary services like transportation, banking among others.

Smallholder cotton farmers, ginners, textile and spinners, and garment and apparel manufacturers are the main sectors in the Kenyan textile industry. The textile and apparel produce a large variety of products in the country for instance the Spinning firms produce yarn and sewing thread while integrated mills produce yarn, knitted garments, fabrics (knitted and woven), canvas, uniforms, school and traveling bags, blankets, sweaters, shawls, baby nappies and towels. Garment manufacturers on the other hand, produce various types of men’s’ wears or garments both for export and for the local market. Other products are woven chemise and robes, knitted and woven garments, pants and Kaunda suits (for men).

The textile and apparel industry has made a generous contribution to income generation in rural areas through provision of market for cotton growers. Other than to its close touch with the rural farmers, the industry has linkages with the textile processing and manufacturing industry, animal feeds, chemicals, fats and oils and manufacturers of soaps and detergents. The
direct linkages with the textile and apparel processing and manufacturing firms are particularly imperative for the exploitation of the AGOA market opportunities. The effect of AGOA on textile and apparel industry may be fragmented into yarn and thread production; apparel manufacture; production and manufacturing of cotton growing and ginning and fabric manufacture.

The textile industry influence other industries such as banking Industry and logistics Industry. The banking sector facilitates all the transactions by textile export sector. It also institutionalizes links of local banking industry with external global networks, thus the financial sector benefits with added capacity development benchmarked. For that reason capacity and networks stand to gain with increased textile export to the US. Further, the inland and shipping industry has gained from AGOA.

3.2 Trade patterns between AGOA-eligible countries (including Kenya) and the United State of America

There is a U.S. trade programs been built by AGOA through expansion of duty-free access earlier available to developing countries under GSP program. The highest trade barriers by the United States tend to apply to goods that developing countries export thou it generally maintains relatively low average trade barriers. The U.S. grants preferential duty-free access to 127 developing countries around the world for 4,975 products under the GSP, distinct by the
Harmonized Tariff Schedule.\textsuperscript{125} The program however reduced tariffs by $742 million in 2012.\textsuperscript{126}

An additional 1,827 goods previously not covered in the GSP are given duty-free treatment by AGOA.\textsuperscript{127} Particularly, AGOA provides duty-free access to all clothing exports from countries that qualify under the Act’s ‘wearing apparel provisions’, on condition that the Rules of Origin (RoO) are met.\textsuperscript{128} Eligible sub-Saharan African countries can export approximately 6,800 goods to the U.S. duty-free that is between the GSP and AGOA.

The primary purpose of AGOA is to increase trade and boost the development of eligible countries through preferential access to the U.S. market. The proposition being that the preferential access minimizes export costs to the U.S. market making African exports more competitive. It further spurs trade-related investment in AGOA-eligible countries, and in so doing creates jobs and contribute to economic growth and development. The data from Foreign Trade Division, U.S. Census Bureau show that AGOA has led to an increase in two-way trade since its commencement in the year 2000. Below is the data on US imports and export on textile products under AGOA.

\textsuperscript{125} Office of the U.S. Trade Representative, “GSP by the Numbers,” April 16, 2013, http://www.ustr.gov/sites/default/files/GSP%20by%20the%20numbers_0.pdf
\textsuperscript{126} Ibid
\textsuperscript{128} AGOA.info, “New GSP Products Added Under AGOA,” http://agoa.info/about-agoa/products.html
Table 1: US imports and export on textile products under AGOA

<table>
<thead>
<tr>
<th>Year</th>
<th>Import (billion USD)</th>
<th>Export (billion USD)</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>Apparel Manufacturing Products</td>
<td>Textiles &amp; Fabrics</td>
</tr>
<tr>
<td>2005</td>
<td>74.57</td>
<td>7.48</td>
</tr>
<tr>
<td>2006</td>
<td>77.09</td>
<td>7.39</td>
</tr>
<tr>
<td>2007</td>
<td>79.03</td>
<td>7.47</td>
</tr>
<tr>
<td>2008</td>
<td>76.27</td>
<td>6.96</td>
</tr>
<tr>
<td>2009</td>
<td>66.88</td>
<td>5.29</td>
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<tr>
<td>2010</td>
<td>75.64</td>
<td>6.53</td>
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<tr>
<td>2011</td>
<td>82.07</td>
<td>7.5</td>
</tr>
<tr>
<td>2012</td>
<td>81.25</td>
<td>7.7</td>
</tr>
<tr>
<td>2013</td>
<td>84.4</td>
<td>8.04</td>
</tr>
</tbody>
</table>


Figures 1, 2 and 3 show the trends in textile trades between USA and AGOA-eligible countries (including Kenya) under AGOA.

**Figure 1: Imports and Exports of Apparel Manufacturing Products under AGOA (2005-2013)**

![Graph showing trends in imports and exports of apparel manufacturing products](http://tse.export.gov/TSE/TSEHome.aspx)

As shown in Figure 1, U.S. import of apparel manufacturing products from AGOA-eligible countries (including Kenya) increased from $74.57 billion in 2005 to $84.4 billion in 2013, as measured in constant 2013 dollars. Despite the considerable variance in the year 2008/2009, the export of apparel manufacturing products to AGOA-eligible countries increased from $4.9 billion in 2005 to $5.44 billion in 2013. The variance in the year 2008/2009 is attributed to the global financial crisis and post-election violence in the Kenyan context.

Figure 2: Imports and Exports of Textiles and Fabrics under AGOA (2005-2013)

Source: Foreign Trade Division, U.S. Census Bureau (2014),
http://tse.export.gov/TSE/TSEHome.aspx
Study findings in Figure 2 shows that U.S. import of textiles and fabrics from AGOA-eligible countries increased from $7.48 billion in 2005 to $8.04 billion in 2013. The export of textiles and fabrics to AGOA-eligible countries increased from $8.76 billion in 2005 to $9.64 billion in 2013.

Figure 3: Imports and Exports of textile mills products under AGOA (2005-2013)

Source: Foreign Trade Division, U.S. Census Bureau (2014),
http://tse.export.gov/TSE/TSEHome.aspx

Study findings in Figure 3 shows that U.S. import of textile mills products from AGOA-eligible countries increased from $13.51 billion in 2005 to $18.86 billion in 2013. The export of textile mills products to AGOA-eligible countries increased from $2.54 billion in 2005 to $3.25 billion in 2013.
3.3 The socio economic effects of AGOA

The direct jobs generated by AGOA in Sub-Saharan Africa are about 350,000 while indirect jobs are 1,000,000 and about 100,000 jobs in the US.129 As of 2012 the top five AGOA-beneficiary countries in were Angola, Chad, Gabon, Kenya, Nigeria and South Africa. Others are Cameroon Lesotho, Mauritius and the Republic of Congo.130

Gender-wise women are key beneficiaries of AGOA. The African Women Entrepreneurship Program (AWEP) is a network of women-led businesses that has been exporting to the United States under AGOA and which was started by the U.S. State Department in 2010. It has 152 members in the 48 countries under AGOA. AWEP companies trading under AGOA can be found in textiles, agribusiness, home décor, food processing and other sectors and therefore plays a critical role in ensuring that gender issues are deliberated under AGOA.

AGOA also provides incentives for African countries to improve their investment climates, reduce corruption, respect human rights and the rule of law, improve infrastructure and harmonize trade standards through supporting regional economic integration in order to help them become more competitive globally. The requirement of democratization and respect for human rights which is anchored on continued eligibility of AGOA has to a large extent served to undertake requisite political, economic and social developments. Additionally given that trans-shipments lead to discontinuation of AGOA the private sector accountability has

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been enhanced. The trade and investment incentives of AGOA are also intended to press African governments in improving their political and economic governance as sound policy is vital economic growth sustenance as well as broad-based development.¹³¹

For this matter therefore, sub-Saharan African countries do not automatically qualify for AGOA benefits. The U.S. President must designate eligible countries based on their progress in areas such as establishing market-based economies, representative government, eliminating barriers to U.S. trade and investment, safeguarding intellectual property, reducing poverty, combating corruption, expanding health care and educational opportunities, strengthening the rule of law, and protecting human rights.¹³²

3.4 A Case for Moving AGOA beyond Preferential Trade

Textile goods from eligible countries without the GSP and AGOA would face major tariff-related costs that would make African textile exports less competitive and also hinder trade and trade-related economic activity between the U.S. and sub-Saharan African countries. Kenya and countries interested in advancing economic growth and development in sub-Saharan Africa support the renewal of both the GSP and AGOA.

Ample benefits from trade however remain unrealized under AGOA, as it is largely one-sided trade preference arrangement rather than a Free Trade Agreement (FTA). Furthermore, AGOA

retains tariffs and quotas on a few key products. If the U.S. were to grant duty-free and quota-free treatment to all imports from AGOA-eligible countries, exports from those countries to the U.S. would rise by more than $105 million whereas U.S. production of those goods would fall by only $9.6 million. These gains would be small compared to actions that African governments could undertake on their own. Implementing five regional economic communities in sub-Saharan Africa would increase intra-African trade by $8 billion and a continental free trade area would boost intra-African trade by $37.5 billion. This is according to a recent study by Brookings Institution.

The U.S. trading relationship with Kenya and sub-Saharan Africa is based on a regional perspective which is increasingly not precise and so AGOA was established to provide a hand up to a region in need of economic assistance. Much of the region remains poor thus considerably becoming more dynamic and integrated into the global trading arena as from 2000. In spite of a number of setbacks caused by political tumult in some countries, the overall trade and investment policy has steadily improved and contributed to increased living standards and resultant economic growth.

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135 ibid
An annual data-driven economic policy analysis by The Heritage Foundation and The Wall Street Journal\textsuperscript{136} states that sub-Saharan African economies as a group have gradually moved toward greater economic freedom ever since the year 2000. Mauritius has become the world’s eighth freest economy, while Rwanda, Cape Verde, Angola, and Botswana have over the years made notable improvements. Advancing economic freedom yields higher economic growth rates in AGOA eligible countries. 38 AGOA-eligible counties (including Kenya) were examined by Miller \textit{et al.},\textsuperscript{137} and the observations and analysis made is as presented in Figure 4.

\textbf{Figure 4: The effect of advancing economic freedom on economic growth rates in AGOA eligible countries (including Kenya)}

![Graph showing the effect of advancing economic freedom on economic growth rates in AGOA eligible countries (including Kenya).](image)

Source: Miller, Holmes and Fuelner (2013), \url{http://www.heritage.org/index}.


\textsuperscript{137} Ibid
Trade facilitation and other regulatory reforms strongly contribute to advancing economic freedom in these countries, enhancing competitiveness and the general entrepreneurial environment.\textsuperscript{138} Actually, 24 of the 38 AGOA-eligible countries in exclusion of South Sudan have moved toward greater economic freedom since 2000. The policy reforms coincide with high economic growth over the same duration. African countries have on average registered consistent growth rates of around 5 percent, which were only temporarily interrupted by the global economic recession.\textsuperscript{139}

The economies of about one-fourth of African countries grew at 7 percent or higher in 2012.\textsuperscript{140} Net private capital flows to the region improved by 3.3\% recording $54.5 billion in 2012 while FDI into the region increased by 5.5\% to $37.7 billion in the same year. Economic growth is still expected to remain strong.\textsuperscript{141} A declination in the overall Kenyan and African poverty has been noted. The entrepreneurship encouraged by greater economic freedom leads to innovation, economic expansion, and overall improvement in human development and living standards.\textsuperscript{142} Improved policy environments and a rich resource endowment have made Kenya and many economies in the region to become more attractive trading partners worldwide. The EU is currently pressuring African countries to enter into economic partnership agreements that would

\textsuperscript{142} ibid
make preferential access to EU markets contingent on reciprocal preferential access to markets in Africa.\footnote{Bloomberg View, “Obama’s Opportunity to Improve U.S. Investment in Africa,” July 7, 2013, \url{http://www.bloomberg.com/news/2013-07-07/obama-s-opportunity-to-improve-u-s-investment-in-africa.html}} The U.S., which used to be Africa’s largest trading partner in 2009, has been overtaken by China’s, whose trade with Africa exceeds $160 billion. Other emerging partners such as Brazil, India, and South Korea have increased their continent’s merchandise trade from 23% to around 40% in a span of 10 years.\footnote{Bloomberg View, “Obama’s Opportunity to Improve U.S. Investment in Africa,” July 7, 2013, \url{http://www.bloomberg.com/news/2013-07-07/obama-s-opportunity-to-improve-u-s-investment-in-africa.html}}
CHAPTER FOUR

FACTORS INFLUENCING COMPETIVENESS OF KENYAN TEXTILE INDUSTRY IN THE INTERNATIONAL MARKETS UNDER AFRICA GROWTH AND OPPORTUNITY ACT

4.0 Introduction

This chapter discusses factors influencing competiveness of Kenyan textile industry in the international markets under Africa Growth and Opportunity Act. The chapter is structured into Factors contributing to Competitiveness of the Kenyan Textile and Apparel Industry, Kenyan business environment and business climate, factors contributing to non-Competitiveness of the Kenyan Textile and Apparel Industry and incentives and support to the textile and garment industry.

4.1 Factors contributing to Competitiveness of the Kenyan Textile and Apparel Industry

While Kenya remains a high cost production economy, there are a number of resources which makes Kenya attractive for doing business. These include educated and trainable manpower, access through port and air transportation.

4.1.1 Pool of Trained and Trainable Manpower

The textile industry in Kenya has been in existence the past 70-80 years. Staff members laid off with contraction in the industry continues to be available to participate in renewed fabric industry. Even more, majority of Kenyans have attained eight years of education and those looking for work have achieved secondary education. First time employees with no skills have not had any difficulties in short term training.
4.1.2 Linkage with International Shipping Lines

The port of Mombasa has been a gateway for Kenya and hinterland countries of the region with the rest of the world. The ports throughput has increased due to continued investments and modernization of the port thus benefiting the private sector. Another added advantage is the change in transacting majority of businesses online. Mombasa has created connectivity through international shipping lines as it is a hub of marine transportation necessitating both the local and foreign investors and business people in transacting online businesses.

4.1.3 Global and Regional Connectivity

Kenya is linked to the region and the rest of the work through efficient air and road transport. There are many flights per week into/out of Nairobi to USA. Connectivity within Africa and a number of continental airlines makes accessibility much easier. There are elaborate road network though much more needs to be done to improve the quality of roads.

4.2 Kenyan business environment and business climate

4.2.1 Political environment

Kenya has generally been politically stable with the exception of the post-election crisis in 2007. The stability has endeared many investors to locate within Kenya focusing on serving the region, continent plus the global markets. Kenya’s Vision 2030 has three key pillars which are economic, social and political governance pillars. The country’s political governance system transformation is anticipated to take place across six strategic areas: rule of law; electoral and political processes; democracy and public service delivery; transparency and accountability; and security, peace building and conflict management.
Vision 2030 is advocating for adherence to the rule of law applicable to a modern, market-based economy respecting the human rights. Specific strategies involve: aligning the national policy and legal framework with the needs of a market-based economy, national human rights, and gender equity commitments; increasing access and quality of services available to the public and reducing barriers to justice; and streamlining the functional capability of legal and judicial institutions to enhance inter-agency cooperation.

A new era was ushered by the landmark promulgation of a new constitution confidence in government and characterized by strengthening of institutions, decentralization of executive authority and fair distribution of resources. Dual citizenship in addition is legalized in the new constitutional provisions which further entrench property rights, recognition of international treaties in an effort to boost the country’s investment and business.

**4.2.2 Public and Private Sector Profiles**

Significant improvements in the business environment in Kenya within the recent years attributed to the continued collaboration between the Government of Kenya (GoK) and the private sector has been eminent. This goes further to support several business reform initiatives aimed at improving the country’s investment. These improvements have been realized mainly through increased efficiency in the relevant regulatory agencies largely due to the associated Rapid Results Initiatives and the continued implementation of Government Performance Contracting.
The reforms mainly achieved in business regulations in Kenya were informed by the realization that growth and competitiveness of the private sector was being hindered by many inefficient, ineffective and costly permits, certifications and licenses. Other obstacles to new investment and entrepreneur activities to establishing new business entities were long delays and complex and costly procedures. Owing to this, many governments have introduced reforms to quicken and simplify the process of starting a new business so as to remain competitive in attracting and retaining investment by establishing a one-stop shop.

4.2.3 Legal and Regulatory Environment

A number of government initiated polices and efforts are aimed at improving the legal and regulatory business environment and investment climate; particularly targeting the doing business indicators which are opening a business; dealing with construction permits; employing workers; registering property; getting credit; protecting investors; paying taxes; trading across borders; enforcing contracts and closing business.

The Government of Kenya formed a Doing Business Reform Team with specific regards to Doing Business indicators and has been mandated to pay special attention to fast tracking specific reforms in six out of the ten indicators namely: Starting a business, registering property, getting credit, dealing with construction permits, paying taxes and trading across borders.

Performance improvements in these indicators are mainly as a result of the continued elimination and simplification of more licenses, administrative efficiency resulting in time savings, consolidation of procedures and the attendant reduction in administrative costs of compliance. Crosscutting and comprehensive business licensing reforms initiated in 2005 set the pace for the
country’s top performance in Doing Business indicators besides the current implementation of business regulatory reforms.

4.2.4 Trade Policy Environment and Market Access

Kenya’s trade policy takes into consideration the commitments to the bilateral, multilateral and regional agreements. It particularly pays attention to the AGOA, COMESA and regional integration agenda anchored on African Economic Commission (EAC) which goes a long way to influence Kenya’s future trade policies. The theme of the trade policy in line with the country’s Vision 2030, is to develop private sector-led, globally competitive trade through value addition and diversification of goods and services improving Kenyans quality of life. The private sector and civil society further concerns for the country is to remain competitive and institutionalize accountability as stipulated in the trade policy.

The policy additionally prioritizes on policies that benchmark Kenya’s trade development on current international market demands and requirements diversifying into emerging markets. The trade policy is also consistent with that of the EAC partner states, which prioritizes sustainable economic growth and development and further incorporating issues of poverty and unemployment reduction, coherent use of natural resources; more fair income distribution and full integration into the economy of the world.

4.2.5 Investment Climate and Incentives

Investment environment in Kenya is enhanced by engagement of liberal fiscal and monetary policies which includes; goods pricing determined by market forces; removal of exchange control; trade licensing that is rationalized; elimination of discretionary clauses in the tax laws. The investor is also allowed to recover the value of import duties on capital goods contrary to
income tax liability under him. Market-based reforms have been introduced by the GOK in addition to provision of more incentives for investment by both local and foreign private investors.

In 2007 Government of Kenya revised its investment policy and launched a private sector development strategy so as to make the country more attractive to investors. Several reforms have also been enacted by the Kenyan government among them being; abolishment of export and import licensing apart from a few, annulling all export duties and current account constraints, liberating the Kenya shilling’s exchange rate, permitting residents and non-residents to open foreign currency accounts with domestic banks, and getting rid of restrictions on borrowing by foreign and domestic companies.

4.2.6 Physical Infrastructure

Improving the infrastructure is high on the development agenda compelling recent policy actions in transport and communications which includes privatization of Telkom Kenya, contracting-out management and operations of Kenya Railways, strengthening management of ports, modernizing container terminals, port equipment and facilities, and privatizing selected operations of Kenya Ports Authority. The Economic Recovery Strategy for Wealth Creation (ERS) contained proposals for updating road designs and specification, make roads and other civil engineering works more cost effective, deepen the control of the quality of roads during construction, maintenance and rehabilitation, dueling the Mombasa-Malaba highway, use an East African Road Network Project to develop internal roads, improve the quality of rural access roads by implementing the Roads 2000 program and construct by-passes to decongest traffic in the cities of Nairobi and Mombasa.
The government under the ERS sought to upgrade smaller airports to make them capable of accommodating medium range jets, privatize commercial and non-regulatory airport services and modernize the management of air traffic in order to improve air transport. On marine transport, the port of Mombasa is to be transformed to a modern and computerized port with new facilities.

The main recent policy step on energy has been to strengthen of the Rural Electrification Program, and to increase private sector participation in generation, transmission and distribution of energy. Kenya is also furthering the implementation of planned generation plants while further exploring alternative sources of power. Policy proposals targeting telecommunications include the restructuring of Telkom Kenya to improve performance prior to privatization and licensing of internet service providers. Further reforms targeted on improvement of the water and sanitation services and infrastructure.

Skills Level and Their Availability

The Kenyan workforce is relatively well-educated, with high returns to education and workforce in the formal manufacturing firms. Differences in education, experience and industry drives the wide dispersal in earnings by the workforce. Nonetheless, there is low level of quality production and technical training in Kenya. This is partially because of the current training incentive system which does not encourage firms to invest in augmenting production skills. Firms invest more heavily in managerial and professional training than in increasing production skills. Training deficiencies occurs partly due to structural problems in the technical and partly in vocational training system. The current training levy system is troubled financially hence becoming inadequate to firms’ needs for it does not support in-house training in production skills.
4.3 Factors contributing to non-Competitiveness of the Kenyan Textile and Apparel Industry

There remains factors that have been identified as contributing to the lack of competitiveness in the manufacturing sector even with the profusion of comparative advantages, and by extension to the specific sub sectors for instance the textile and clothing industry in Kenya. These broad factors include poor infrastructural conditions and high input prices; low output levels; hostile business environment and inefficient flow of goods and services.

4.3.1 Poor infrastructural conditions and High input costs

Of the many constraints affecting the competitiveness of textile and apparel exports among Kenya producers poor and inadequate infrastructural conditions is one of them. Others include inadequate infrastructure, such as unreliable electricity, poor road quality; limited access to international shipping all which increases production costs and limits speed to market. Consequently, most SSA manufacturers produce lower-value, basic attire products. Extra constraints include geographic distances to major markets, lack of access to affordable capital, and political unsteadiness. Costly and often low-quality raw materials, escalating labor costs, poor infrastructure and inadequate services, such as water and other input supplies, unpredictable and expensive energy have led to high costs of production.

4.3.2 Number of days it takes to clear at port

Since DB 2008 there have been initiatives at the port of Mombasa, international airports and border ports including administrative reforms to make procedures and processes which are more
efficient for importers and exporters involved in international trade as well as trade across borders. An example of this is the National Single Window Community Based Project which is currently under implementation by the GoK.

The system introduced help reduce import cargo delays both at the port of Mombasa and JKIA. This is all thanks to the new program in addition to enhancement of processes such as Enhanced use of X-ray scanners; Customs border control services in line with international standards; Systems interface; RADDEX connectivity to URA and RRA to enable data exchange to facilitate cross border trade in the region; valuation database; and single entry documentation (SED) for both import and export online.

4.3.3 In-country transit transportation and in country border points

In country transit transportation also requires improvement. There is need to reduce the number of road blocks which have turned into toll stations for defrauding the business community. Continued operations of cross border ports of entry even with the introduction of fully operational customs union and Common market, causes delays in the clearance of goods attracting no duty.

4.3.4 Low productivity levels

Compared to regional and global productivity levels capital productivity in the Kenyan manufacturing sector is low. This is occasioned by declining capital investment levels. Gross investment in plants and equipment has been low among the manufacturers as a proportion of replacement value resulting from high levels of uncertainty in the business climate, diminished expected returns on investment, and absence of long-term financing. Although Kenya’s labor
productivity is comparable to that of India and China, there is significant room for improvement, mainly among small- and medium-sized enterprises.

4.3.5 Inefficient Flows of Goods and Services
The ability of local manufacturers to access and be competitive in regional and global markets is greatly hampered by inefficiency in the local transport and logistics sector (e.g. port, rail and road transport services).

4.3.6 Unfavorable Business Environment
The unfavorable business environment rises from heavy regulations, weak trade agreements, lack of rigorous legal enforcement, incidences of insecurity, as well as limited access to capital. Heavy regulation has led to intricate business and investment registration, affecting both the ease and the cost of doing business in the sector. Weak negotiating proficiency further obstructs the country’s negotiation ability for favorable trade agreements therefore creating barriers against companies in Kenya. Weak enforcement of standards and of tax laws has led to dumping of sub-standard imports and counterfeit goods into the domestic market foiling local competition.

4.3.7 Policy issues and transactional constraints
Policy issues and transactional constraints affect negatively Kenya’s exports to US at the commodity and cross-cutting levels. Also they touch on the procedures of compliance with the US Government determined market accessibility conditions. The Challenges are: Erosion of AGOA benefits with expiry of the Multi Fiber Agreement in 2005 affected textile exports
to the US market where we had comparative advantage because of the quota restrictions imposed on the non AGOA beneficiary countries prior to 2005; Competition from low cost producers, such as China and India, following the expiry of MFA and further liberalization of the international market; The impact of recession for the US economy and financial crisis is expected to affect consumer spending and generally affect demand for imports; Delayed re-establishment of the local/regional integrated textile chains to satisfy the AGOA requirement of local fabric sourcing. Low cotton production, ginning and textile manufacture means that lifting the provision of 3rd country fabric will render existing garment manufacturers idle.

Other challenges include Stringent quality assessments in the US market; Lack of commercial representation in the US market to promote the Kenyan products and link producers with proper marketing chains. Unrelenting reliance on textiles and apparel without exploring value added lines, in order to take advantage of the expansive Market Access opportunity created by AGOA by diversifying the range of products, including value addition; Lack of access to financial support especially for small and medium enterprises; Lack of direct flights from Nairobi to USA which makes Kenya exports expensive compared to its competitors.

The cross-cutting issues include: High cost of production in terms of energy, water and infrastructure. These costs are much lower in South East Asian countries; Lack of an integrated cotton and textile sector to provide raw materials for the garment industry while the South East Asian countries have long traditions in the textile industry; Inadequate financial support for the textile industry from the government while the sector in some countries like India
and Pakistan receives a lot of financial support from the government; South East Asian countries benefit from economies of scale since textile production in their countries is massive. They are therefore able to produce garments at much lower prices than the garment firms in Kenya; Distance to the US from Kenya is also much longer compared to the distance between the US and South East Asian countries; South East Asian countries have huge domestic market.

The EA Customs Management Act provides for hitch of import duty on goods imported for the manufacture of goods which are to be exported transferred to a free port; and transferred to an Export Processing Zone. Though AGOA has clearly played an important role in boosting apparel exports from a relatively small group of Sub-Saharan African (SSA) LDCs to the US market, its broader economic impact has been much more modest. Linkages with the local economy are weak and there has been little transfer of capital or skills in the apparel sector. Most of the rent from apparel preferences also goes to Asian investors and importers in the US.

4.4 Incentives and support to the textile and garment industry

Notwithstanding a long tradition of manufacturing in Kenya there has been a continued deterioration in investment and the overall lack of competitiveness making it difficult for the textile sector to play a bigger role in the economy. Thus, many textile manufacturing companies in Kenya struggle to thrive while some key players have moved their operations to other countries.
Majority of the textile firms are located in EPZ designated areas. Conversely, with entry of AGOA in 2000, a number of textile industries located outside EPZs also enjoyed the same status firms located in EPZs. Other than the fiscal benefits due to tax exemptions and income tax waivers, the textile firms operating within the framework of EPZ also enjoy fast tracking of customs clearance and one stop approvals.

4.4.1 Export Processing Zones (EPZ)

Export Processing Zones (EPZ) program was inaugurated in 1990 as part of the Export Development Program (EDP) undertaken by the Government to transform the economy from import substitution to a path of export led growth in Kenya. The EPZ investors enjoys the following incentives: (i) Fiscal incentives with a 10 year corporate income tax holiday and a 25% tax rate for a further 10 years thereafter; 10 year Withholding Tax holiday on remittance of dividends; Duty and VAT exemption on raw materials, machinery and other inputs; Stamp duty exemption; 100% investment deduction over 20 years on initial investment. (ii) Physical Infrastructure Benefits which include ready factory buildings for rent or purchase, serviced land for construction of buildings, office premises, water, sewerage and electricity supply, landscaping, garbage disposal, street cleaning services, illuminated perimeter fence and 24-hour security and accessible customs offices.

4.4.2 Manufacture under Bond (MUB)

Manufacture under Bond (MUB) was introduced in 1986 as an export drive policy measure. It aims at promoting industrial production for the export market. It allows manufacturers to import plant, machinery, equipment and raw materials tax free, for exclusive use in the manufacture of goods for export. Specific incentives comprise of exemption from customs/excise duty and
VAT on imported plant, machinery, equipment, raw materials and other imported inputs; and 100 percent investment allowance on plant, machinery, equipment and buildings.

**4.4.3 Tax Remission for Exports Office (TREO) Scheme**

TREO scheme objects at encouraging local manufacturers to export their products by way of remitting duty and VAT on raw materials used in the manufacture of export goods. Moreover the scheme provides for tax remission on inputs in order to make defined goods essential for the domestic market. It also emboldens manufacturers to produce goods for export market by giving way remission of import duty on inputs; exemption of IDF fees on inputs other than for payment Kshs. 5,000 processing fee; remission of excise duty on fuel oil and kerosene and remission of VAT on inputs.
CHAPTER FIVE

CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

The objective of the study was to examine the competitiveness of Kenyan textile industry at the international markets under the Africa Growth and Opportunity Act (AGOA). The study established that AGOA has enhanced the competiveness of the Kenyan textile industry. Under AGOA Kenya experienced an increase in exports of textiles and clothing. AGOA promotes economic development and advances while also integrating the economies of Africa countries with the globe. Through AGOA the governments, civil society and the private sector work together in building trade capability and expanding business links amid Africa and the US. Trade capacity increase encompasses technical assistance on world trade rules, customs reform and modernization. It is further driven by industry standards and regulations development, enforcement of intellectual property rights and infrastructure transformation.

The study concludes that AGOA has also helped many African countries, including Kenya, in creating multiple new jobs and boosting international competitiveness. GSP and AGOA offer duty-free treatment for roughly 6,800 products exported from qualified African countries. As a result of this special trade treatment investment opportunities, business formation, job growth, and economic growth have been felt by both the African states as well as by Americans. These gains will however be swept away once the AGOA treaty is terminated.
AGOA has had a positive influence on FDI inflows, predominantly in the Kenyan textile and apparel sector. AGOA beneficiaries have yearned on improving their businesses and investment because of the benefits and entitlement criteria offered to them. In summary, Kenya and African countries should no longer aim for donor fund but gauge themselves as worthwhile economic partners deserving deeper engagement and focused attention.

After successful recovery of Kenya’s garment sector under AGOA, the cotton-to-textile/garment sector is far from realizing its true potential. However, the Kenyan cotton-to-textile/garment market structure has the capability of competing with international markets such as China if well managed. Importation of fabrics by the Kenya garment and apparel sector still remains a big obstacle to the realization of its full potential and producing the right quantities.

China and Asian countries are not only giving stiff competition to the African countries in exporting the products to the US but also taking advantage in selling the fabrics to these countries. Failure to extend the AGOA on long term basis will see a great devastation in the African countries economy Kenya being among them. Private companies especially those that are presently in AGOA beneficiary regions will relocate to Asia and China. Additionally very little investment in textile manufacture shall take place. A disruption of the cotton-textile chain will also occur. The Kenya textile and apparel contribution to the manufacturing sector will be compromised for failure to extend the AGOA. The manufacturing sector which is expected to play a vital role in thrusting the economy to higher growth rate will also be hampered. As per the Vision 2030, the manufacturing sector is anticipated to support the country’s social
development agenda through job creation, foreign exchange generation, and foreign direct investment attraction.

AGOA is at a serious moment as it is set to expire in 2015. As of now the law allows nearly all imports from eligible sub-Saharan countries to enter the U.S. duty-free through 2015. Nevertheless, the existing law disregards substantial potential benefits. Failure by U.S. to advance AGOA past a trade-preference arrangement will see it losing ground to Europe and other nations keen on entering into more stout economic partnerships. Other than just renewing AGOA, legislation should be used by the U.S. to spur African economic integration. The legislation will further transform the trade-preference program into a FTA between the U.S. and African states. Precisely, the AGOA should be renewed through 2025.

There is need urgent visitation of the overall AGOA framework within the context of the global WTO Commitments and proliferations of FTAs if AGOA is to remain the cornerstone of US-Africa economic policy and trade relations. Principally there is need to foyer the US government to: Sustain the original the objective of AGOA of alleviating poverty; maintaining the momentum and motivation picked up in re-building the African Fiber, textile and apparel value chain. To also continue encouraging foreign new investments and the development of attire manufacturing capability of Sub-Saharan Africa.

5.2 Recommendations

5.2.1 Recommendations to the US government

The US should renew AGOA along with provisions so as to encourage regional integration, increase the number of products allowed duty-free access, and abolish quota restraints. Renewal
will further go to providing gradual reciprocal duty-free treatment for American exports in an effort to negotiating a free trade agreement (FTA) between the U.S. and Africa. The renewal of AGOA further offers a timely opportunity to upgrade AGOA from a limited trade arrangement into a trail headed for a free trade and investment partnership which will congeal America and Africa engagement benefiting both.

SSA should call for negotiations with the US government aimed at extending the period of AGOA and AGOA IV beyond 2015 on a permanent basis; prolonging the period of the “third country fabric” provision; extending AGOA to non-sensitive Textile Products; protecting AGOA from being weakened by ongoing USA preference reforms (TPP) and FTA arrangements; reviewing the AGOA eligibility rules; and building the capacity of SSA textile industry.

AGOA’s broader economic impact could be enriched if preferences were extended to all products and fixed for a longer period of time. Equally, the organization should call for liberalization of products that are presently subject to tariff rate quotas. Such measures should go hand in hand with non-restrictive rules of origin giving AGOA exporters the flexibility needed to source inputs across the globe. U.S. should also reauthorize the GSP, endorse regional economic integration; incentivize economic integration and also encourage AGOA-eligible countries in pursuing bigger economic freedom.
5.2.2 Recommendations to the government of Kenya

The study recommends additional investments in infrastructure with a view to benchmarking subsequent rates to international rates; enhance the efficiency of the transport and relate service sectors of the ports, sustain technical skills trainings in order to increase productivity, and sustain reforms in the business environment and business climate including exploring the option of commercial representation in the US market. Further, the cotton-textile chain has to be developed in a wholesome way.

The study recommended the following remedial strategies that are required to be put in place by the Government of Kenya and the private sector: establishing direct relationship between exporters, local garment makers and textile manufacturers; making proper US market survey on quality assessments; having enough stocks that satisfy demand before entering into contractual arrangements; establishing Kenyan distributors in the US; sensitizing the relevant US authorities on AGOA; putting in place urgent policies and measures to boost local production of cotton and high quality fabrics for apparel manufacture and strengthening US/Kenyan textile trade associations links.

Critical solutions to the identified cross cutting constraints hinge upon: ensuring there is direct and cost effective air and sea freight transport from Kenya to USA; and there are no delays and burdensome procedures at the entry ports. Further, the level of awareness of SPS management requirements needs to be increased; the standards testing infrastructure should be improved; trade finance needs to be made accessible with affordable interest rates and
collateral requirements; scaling up attractive features of EPZ and KIA; and developing human capacity for promoting Kenya trade interests in international markets

5.2.3 Recommendation for further research
The study recommends further research on policy alignment between AGOA and other regional trade agreements. The study will give insight into the synergies and barriers to trade caused by differing trade policies between AGOA and other regional trade agreements.
REFERENCES


AGOA Apparel Provisions (Eligible Countries – AGOA Preferences Chart). Countries that fall outside of the TCF provision include, for example, Gabon, Seychelles, and South Africa.


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U.S. Dep‘t of Commerce, Int‘l Trade Admin., Trade Preference Programs - The African Growth and


Whitley (1992), cited in McCormick et al. (2001), for details regarding this categorization of institutions.

