

# Kisumu

Invest in Kenya: **Focus Kisumu** July 2007



MILLENNIUM CITIES INITIATIVE (MCI)  
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# Invest in Kenya: Focus Kisumu

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July 2007



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## pr eface

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Kenya, along with 189 other countries, adopted the Millennium Declaration in 2000, which set out the millennium development goals (MDG) to be achieved by 2015. The MDG implementation process was initiated by the Government of Kenya in September 2002. The process is spearheaded by the Ministry of Planning and National Development in partnership with UNDP-Kenya and the Government of Finland, through a project titled 'Mainstreaming MDGs in Kenya's Development Process'. One component of the project is support to Kisumu city to review its city development strategy and profile investment opportunities to attract private investment from within and outside the country. For more on the MDG project in Kenya, see Box I.1 in Chapter I.

This Guide is part of the work supported by the project just described. It was prepared by the Millennium Cities Initiative (MCI), which is an initiative of the Earth Institute at Columbia University, undertaken in cooperation with the MDG Support Team at the United Nations Development Programme and the Columbia Program on International Investment. The MCI is guided by Jeffrey D. Sachs and co-directed by Susan Blaustein and Karl P. Sauvant. Its initial effort focuses on helping seven cities in six African countries attract more foreign direct investment (FDI). The cities are: Kisumu, Kenya; Blantyre, Malawi; Kumasi, Ghana; Akure, Nigeria; Bamako–Segou, Mali; and Louga, Senegal. For more on the MCI, see the MCI website: <http://www.earthinstitute.columbia.edu/mci/>.

The millennium cities were chosen in part for their proximity to the millennium *villages* (<http://www.earth.columbia.edu/millenniumvillages/>). In the case of Kisumu, the first millennium city to have an investors' guide prepared for it, the millennium village is Sauri, in the neighbouring Siaya district in western Kenya.

The idea behind this Guide is to offer the reader a brief description of investment opportunities in the Kisumu area, supplemented by a description of the investment climate and of the broader context of Kenya and East Africa. The MCI does not believe that serious investors can be attracted to an area through a purely 'promotional' approach, one that promotes the positive while hiding the negative. So the Guide is written to be credible. The challenges that potential investors would face are described along with the opportunities they may be missing if they ignore Kisumu.

The Guide is intended to make Kisumu and what Kisumu has to offer better known to investors. Although we have had the foreign investor primarily in mind, we believe that the Guide will be of use to domestic investors in other parts of Kenya as well. While by no means the sole driver of growth and development, foreign direct investment does have a distinctive contribution to make. Not only does it bring scarce capital, it also brings know-how, technology and access to foreign markets. Furthermore, it helps improve the competitiveness of *domestic* enterprises, which must be the foundation of all growth.

We hope that our investor readers find the Guide a useful practical tool.



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# Acknowledgements

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Our thanks are owed to the companies and government agencies that participated in the workshop in Kisumu, as well as to the government agencies that participated in a feedback meeting in Nairobi hosted by the Kenya Investment Authority. Among those who provided substantial inputs to the Guide or the workshop, we should particularly like to thank Jit Bhurji, Susan Blaustein, Calvin Burgess, Leon D'Souza, Munira and Salima Gilani, Heikki Haili, Ghulam Abbas Hirani, Peter Jones, Susan Kikwai, Shirish Limaye, Saida Mäki-Penttilä, Gideon Mailu,

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The preparation of the Guide was undertaken in parallel with three other related efforts, all focussing on investment opportunities in Kisumu and the regulatory framework governing it, by KPMG, UNIDO, and Cravath, Swaine & Moore LLP. These are still ongoing. Their results will be available in due course, and will complement and deepen the information provided by the Guide. We thank the Corporate Council on Africa and the European Business Council for Africa and the Mediterranean for their cooperation in this project.

Photographs for the Guide were provided by the Kenya Investment Authority, the Municipal Council of Kisumu and Vishwas P. Govitrikar. Administrative assistance in Kisumu was provided by Susan Siaji. Nelson Vigneault designed the Guide.

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Investment opportunities are abundant in Kisumu, from agriculture to construction and manufacturing. The city also offers an attractive and safe living environment. Investment in Kenya generally, and in Kisumu particularly, would grow and thrive even more if governments at all levels were more proactive in its cause and concentrated on creating a more enabling environment for investors.

Sailesh Shah, Director, Swan Industries



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## Executive summary

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Kisumu is an attractive city in Kenya on the eastern shore of Lake Victoria, one of the Great Lakes of Africa. Established as Port Florence, the lakeside terminus of the Uganda Railway, over a hundred years ago, it grew into a trade and transport hub for East Africa over the following fifty. Its prosperity continued into the first decades after independence, which came to Kenya in 1963. In 1977 occurred the first setback in Kisumu's fortunes, as the then East African Community (EAC) collapsed and long-established transport and other links were severed. Kenya, and Kisumu with it, then went through a long period of relative decline, caused by poor governance, deteriorating security and neglected infrastructure.

In the new millennium, the trend has changed, as witness the steady increase in Kenya's GDP growth rate, which was 6.1 per cent in 2006. External conditions have changed as well, with the EAC re-emerging in 2000 and moving towards both economic and political integration. Kisumu is thus poised to regain its former status as a regional hub. The present Guide is meant to alert investors to its potential and to provide an overview of the investment conditions it offers.

The principal opportunities in Kisumu are to be found in agriculture and agro-processing, dairy, and aquaculture. Western Kenya has long been known for some major crops, such as cane, cotton, groundnuts and rice. There is a domestic market for some of these crops (e.g., rice) and products made from them (e.g., peanut butter) and a regional or overseas market for others (e.g., potable alcohol made from sugarcane). Aquaculture again has both domestic and foreign markets for its products, in particular for tilapia. Other opportunities may be found in service sectors. Kisumu has a serious prospect for conference and leisure tourism from the East African region. Water transport on Lake Victoria, for cargo in particular, also

offers opportunities. There may be opportunities in construction as well, as there is a real shortage of low-cost housing.

A number of regional and international trade agreements enhance Kenya's access to foreign markets. The EAC Customs Union Protocol is already in place in the three founding members of the EAC (Kenya, Tanzania and Uganda) and will soon be extended to the two new members, Burundi and Rwanda. Kenya is also a member of the Common Market for Eastern and Southern Africa (COMESA) and one of the 11 (out of 20) countries that belong to its free-trade area.

Overseas, Kenya was the first country to qualify under the apparel provision of the African Growth and Opportunity Act (AGOA) of the United States. (In 2006, Kenya's garment exports to the US were worth USD 273 million.) It is also a member of the ACP agreement with the European Union and is eligible for GSP preferences, which give it preferential access not only to the EU market but also to other rich markets such as Japan.

It is only fair to add that the investment climate is not without its challenges. Transport infrastructure linking Kisumu to its customers and suppliers is not all that it should be. Although the road *network* in Kenya is more extensive than in its neighbours, road *conditions* are often very poor. The railway from Mombasa to Kisumu is not in much better shape, although improvement is expected since the concessioning of Kenya Railways to a South African firm in 2006. The regulatory framework offers its own challenges, in the form of cumbersome licensing and customs procedures, although the licensing system is being cut back and simplified. Against these challenges, however, one needs to put the attractions of Kisumu: its safety, its climate and its workforce. Any investor interested in Africa needs at least to consider this lakeside city in the heart of East Africa.





Map No. 494, 1988 © ICAO  
 Area 100

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 Geographic Section

## Kenya in brief

- Official name:** Republic of Kenya
- Capital:** Nairobi
- Form of government:** Multi-party democracy
- Head of state and of government:** President Mwai Kibaki
- Location:** East Africa (see map), with an Indian Ocean coastline of 536 km.
- Surface area:** 582,646 sq. km, of which water 11,230 sq. km and national parks 25,334 sq. km.
- Climate:** Hot and humid on the coast, temperate inland and very dry in the north and northeast. Two periods of rainfall: the long rains between March and June, and the short rains between October and December.
- Population:** 34 million (estimate)
- Religions:** Christian (78%), Muslim (10%), indigenous African and other (12%).
- Languages:** English is the official language and Kiswahili the national language. Many of Kenya's over 40 ethnic groups have their own languages.
- GDP:** USD 17.4 billion – at purchasing power parity, USD 40.8 billion (2005).
- GDP per capita:** USD 470 – at purchasing power parity, USD 1,100 (2005).
- Currency:** Kenyan shilling (KSh)
- Exchange rate:** USD 1 = KSh 67 in mid-2007.

## Kisumu in brief

- Location:** On the eastern shore of Lake Victoria, Nyanza Province, western Kenya.
- Notable natural feature:** Lake Victoria, the second largest freshwater lake in the world, with a surface area of 69,000 sq. km<sup>2</sup>, of which 4,113 sq. km<sup>2</sup> belongs to Kenya and the rest roughly equally to Tanzania and Uganda.
- Climate:** Moderate tropical, 17° to 29° Celsius round the year.
- Population:** Kisumu district 565,000 and Kisumu city 375,000 (estimates)
- Religion:** Mainly Christian, with a significant Muslim minority
- Languages:** English, Kiswahili and Dholuo, one of the languages in the Luo family. The main ethnic group in the area is Luo.
- Economic activity:** Sugar, fishery, agriculture, some tourism, large informal economy

Spectre International is a team effort by Kenyan and Canadian investors, to revive an industrial plant that politics had made idle for twenty years. Our aim is two-fold, to do profitable business and to contribute to Kisumu's development. We are very pleased with our progress over the past three years and would like to see other investors join us in Kisumu.

Ruth Odinga, Director, Spectre International Ltd



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## i. the broader context

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### 1. A sketch of Kenya and East Africa

#### The country

Kenya is a sizable country in East Africa, almost twice the size of Italy. The Indian Ocean provides it with a 536 km coastline on the east. Tanzania shares its border to the south, Uganda to the west, and Sudan, Ethiopia and Somalia to the north. To the southwest lies Lake Victoria, the second largest freshwater lake in the world and the source of the White Nile (which joins the Blue Nile at Khartoum to form the Nile proper). Some six per cent of the lake belongs to Kenya; the rest in roughly equal proportions to Tanzania and Uganda.



The population of Kenya was around 34 million in 2006, nearly 80 per cent of it rural. The three largest cities are Nairobi (about 3 million), Mombasa (about 900,000) and Kisumu (about 375,000), the last the focus of this guide. Although there is some uncertainty about religious affiliations, the overwhelming majority is Christian, with significant minorities of Muslims and practitioners of traditional African faiths. There are said to be over 40 ethnic groups in Kenya but the principal ones are the Kikuyu, the Luhya, the Luo (who predominate in Kisumu), the Kalenjin and the Kamba.

Kenya is the economic hub of East Africa and has been so for a long time, even though, in the 44 years since it became an independent country in 1963, the economy has known some serious ups and downs. The good years were the 60s and the 70s, when import substitution reigned and a diversifying economy grew at an average of 6.5%. Growth faltered in the 80s and per capita incomes actually fell through the 90s. Recovery seemed to begin with the election of a new government in the new millennium.

Expectations were high when the National Rainbow Coalition (NARC) took power in December 2002 and there were a number of positive signs at first. (Kenya had long been a one-party state, *de facto* at first and then *de jure*, until multi-party democracy came to stay in 1992.) Corruption, for instance, long a bane of the Kenyan economy, seemed to decline in the first year or two of the new regime. But apparently it did not last, according to the Kenya Bribery Index of 2006.<sup>1</sup> Two other issues of concern to all investors, whether domestic or foreign, have been infrastructure and security. The difficulties in these areas have eased somewhat, but not dramatically so.

<sup>1</sup> Published by the Kenya Chapter of Transparency International, on the basis of a survey of 2,405 respondents in all eight provinces.

Nonetheless, there are a number of positive signs as the NARC government approaches the end of its first mandate. (Elections must be held by December 2007.) The most obviously encouraging of these is the *resumption of growth* (Figures I.1 and I.2). Another is the *steady increase in exports* (Figure I.4 below), although imports have gone up as well, as the price of petroleum has risen, and the trade deficit has increased. Beyond these numbers are the various policy and legal measures taken by the government. A *new Investment Act* was passed in 2004 and amended in 2006 to remove some of the obstacles to foreign direct investment (FDI). (See the discussion of the investment framework in Chapter III below.) The *Privatization Bill*, which had stalled, became law in 2005 and provided for the setting up of a Privatization Commission, expected in 2007. The management of

the Kenya Railways Corporation, along with that of its Ugandan counterpart, was privatized in 2006 through a 25-year concession.<sup>2</sup> The government sold 30% of KenGen, the electricity-generating company, in a hugely successful IPO in 2006 and is planning to sell a further 19% this year.

<sup>2</sup> To Rift Valley Railways of South Africa.

Privatization remains one of the Government's priorities. Other economic priorities are embodied in the Economic Recovery Strategy for Wealth and Employment Creation, the Investment Climate Action Plan, the Private Sector Development Strategy (PSDS) and the National Export Strategy. All of these are meant to create a more enabling environment for business and to lead to economic growth and poverty reduction. From them have followed various measures to enhance security, strengthen infrastructure, streamline procedures and simplify regulations.

#### Box I.1. Millennium Development Goals in Kenya

Kenya, along with 189 other countries, adopted the Millennium Declaration of the United Nations in 2000, which set out the Millennium Development Goals (MDG) to be achieved by the year 2015. Today, Kenya is one of four African countries implementing the Millennium Project, a United Nations initiative undertaken to support member countries in assessing their investment requirements for the promotion of equity, the reduction of poverty levels, and thus the achievement of the MDG. The MDG process in Kenya is spearheaded by the Ministry of Planning and National Development, in partnership with UNDP Kenya and the Government of Finland, through a project titled 'Mainstreaming MDGs in Kenya's Development Process'.

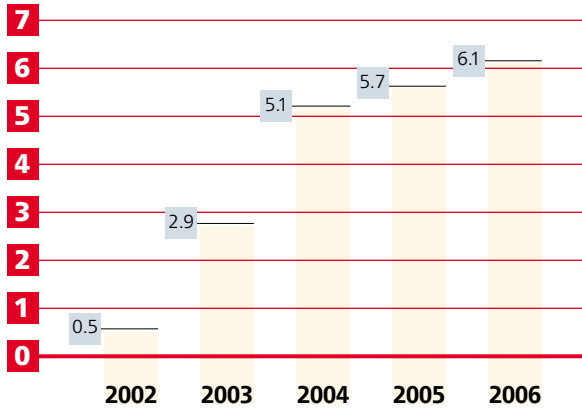
The MDG project in Kenya aims to mainstream MDGs into Kenya's national policy formulation through MDG-based planning, budgeting, monitoring and reporting processes. While targeting the poor, the project also involves the Government, Civil Society Organisations (CSOs), and various development partners through such activities as a) building the capacity of key public sectors for MDG mainstreaming in policy formulation and planning processes and of non-state actors to participate in the process; b) undertaking MDG campaigns and awareness-raising; c) developing a National MDG-based Long-term Framework for Action; and d) undertaking comprehensive MDG tracking and reporting.

In addition, the MDG project in Kenya has produced MDG Needs Assessment Reports, launched by the Minister for Planning and National Development, the Honourable Henry Obwocha. These reports highlight the requirements necessary to achieve the MDGs in Kenya by 2015, as well as the cost estimates to fulfill those requirements. In order to achieve the MDGs in Kenya by the year 2015, the Government of Kenya has, through its budget Strategy Papers, shifted the allocation of resources to Kenya's core poverty sectors of agriculture, health, infrastructure and the environment. Finally, another component of the MDG project in Kenya is supporting Kisumu's city development strategy and the profiling of investment opportunities in the Kisumu area to attract private investment from within and outside the country.

**Source:** Millennium Cities Initiative, drawing on information provided by the Ministry of Planning and National Development, UNDP Kenya and the Government of Finland.

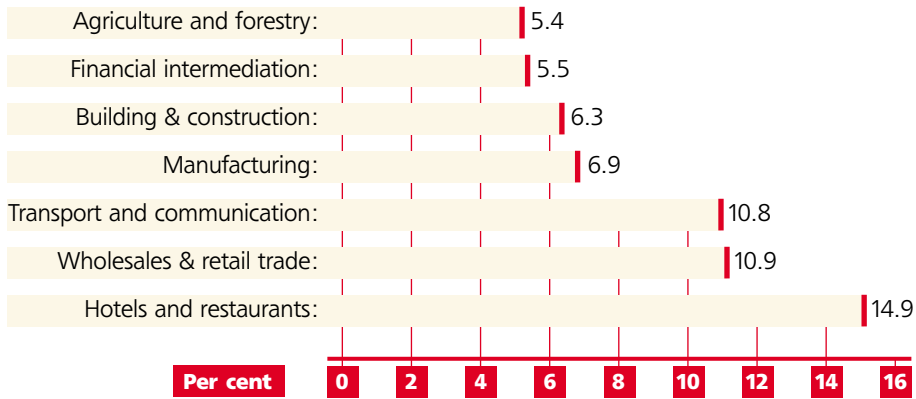


**FIGURE I.1. Real GDP growth at market prices, 2002-2006**



Source: National Bureau of Statistics, *Economic Survey 2007*, launch presentation.

**FIGURE I. 2. Sectoral growth rates in 2006**



Source: National Bureau of Statistics, *Economic Survey 2007*, launch presentation.



## The region

Kenya is one of the three founding members of the East African Community (EAC), along with Tanzania and Uganda, a region with an area of 1,768,812 sq. km and a population of just over 100 million. In November 2006, the heads-of-state summit of the EAC agreed to admit two new members, Burundi and Rwanda, with the admission to take effect from 1 July 2007. The new five-member EAC will have a population of about 120 million. The EAC shares its boundaries with seven countries: the Democratic Republic of the Congo (DRC) to the west; Sudan, Ethiopia and Somalia to the north; and Malawi, Mozambique and Zambia to the South. The notable physical features of the EAC area include the two highest mountains in Africa, Kilimanjaro and Kenya, the Great Rift Valley and, of course, Lake Victoria. The EAC also has remarkable natural assets in its diversity of minerals and mammals, both significant attractions for investors, in mining and tourism respectively.

The Community has a long history of regional cooperation<sup>3</sup> and it actually had a predecessor that dissolved in 1977. The cultural and economic ties were too strong, however, to let separation last and the EAC began to reconstitute itself in the early 90s. The objectives of the Community, finally established by treaty in 2000, are to widen and deepen integration among the partner states, including economic integration but going beyond that. In fact, it is of some consequence to note that the EAC is not just yet another preferential trade area. It is a relatively compact and homogeneous group – unlike, say, COMESA or ECOWAS – and it has a rather firm grip on where it wants to end up and when. The ultimate objective is political federation and, if the schedule of the EAC's fast-tracking committee is followed, it would happen by 2013 (Figure I.3 below). Although there have been some inevitable delays in implementing these steps, the schedule as a whole is more or less on track.

<sup>3</sup> See Chapter I of UNCTAD's *An Investment Guide to the East African Community*, 2005.

**FIGURE I.3. EAC integration schedule, as recommended by the Fast-tracking Committee**



Source: As in fn. 3 above.

## 2. The economy

### Markets for investors

Despite a poor-to-fair performance in the 80s and 90s, Kenya remains easily the strongest economy in the region, just as it was in the early post-independence years 40 years ago. It is the most diversified, with a small but significant manufacturing sector, has the best-regarded workforce in the region – perhaps the best between Egypt and South Africa – and the strongest domestic private sector. Nairobi is the air traffic hub of the region, with the privatized Kenya Airways among the top airlines in the continent, and Mombasa is the region's main seaport.

The Kenyan market is relatively small, though not insignificant, but an investor in Kenya has access to other markets as well, the nearest of course being the now five-member EAC, a market of nearly 120 million consumers (Table I.1 below). Beyond the EAC, there is the

Common Market for Eastern and Southern Africa (COMESA), which contains some 400 million consumers in 20 countries. Within COMESA, 11 countries including Kenya have formed a free-trade area (FTA).<sup>4</sup> At its recent (May 2007) 12<sup>th</sup> Summit in Nairobi, COMESA members agreed that a customs union would come into effect as of December 2008, with the Common External Tariff (CET) to be set at 0% for raw materials and capital goods, 10% for intermediate goods, and 25% for finished goods, with a provision for flexibility on policy space. The EAC Customs Union Protocol, which came into force in January 2005, has adopted a three-band CET that is almost identical. The EAC protocol further binds the members to institute full free trade within five years, i.e., by 2010. Until then, there will be a declining asymmetrical tariff on Kenyan exports to Tanzania and Uganda, in recognition of the fact that EAC trade is mostly one-way, Kenya exporting to its partners but importing relatively little in turn.<sup>5</sup>

**4** The other 10 countries are Burundi, Djibouti, Egypt, Madagascar, Malawi, Mauritius, Rwanda, Sudan, Zambia and Zimbabwe. Of the five EAC members, Uganda is a member of COMESA but not of the FTA, while Tanzania is not a member of COMESA at all but instead of the Southern African Development Community (SADC). These overlapping memberships can create inconsistencies that the EAC needs to address.

**5** It should be noted that the EAC has a list of 'sensitive products' that carry much higher tariffs than the CET specifies. The sensitive products include wheat and maize flour, milk and cream, tobacco, rice, fabrics of various sorts, sacks and bags, etc. For a list, see Appendix 1 to UNCTAD's 2005 EAC guide; for discussion, see Heinz-Michael Stahl, 2005.

**TABLE I.1. The East African market, 2005**

Country	Population Million	GDP <sup>a</sup> USD <sup>billion</sup>	GDP, PPP <sup>b</sup> USD <sup>billion</sup>	GDP per capita <sup>c</sup> USD	GDP per capita, <sup>d</sup> USD
Burundi	8	1	5	105	699
<b>Kenya</b>	34	19	42	442	1240
Rwanda	9	2	11	260	1206
Tanzania	38	12	29	330	744
Uganda	29	9	42	270	1454

**Source:** Adapted from the World Bank, *World Development Indicators*, 2007.

<sup>a</sup> At current USD. <sup>b</sup> At current international USD. ('PPP' is purchasing power parity.)

<sup>c</sup> At constant 2000 USD. <sup>d</sup> At current international USD.





Beyond its neighbourhood, Kenya has access to two key markets: the European Union and the United States. (New markets are being developed in the Middle East and India.) Although Kenya does not qualify for the EU's 'Everything But Arms' initiative – since it is not what the United Nations calls a 'least developed country',<sup>6</sup> unlike the other members of the EAC – it does qualify under the EU's agreement with the African, Caribbean and Pacific States (ACP) and also under the Generalised System of Preferences (GSP), which latter gives Kenya preferential access not only to the EU but to many other rich markets (e.g., Japan) as well. As far as the US market is concerned, what is relevant is the African Growth and Opportunity Act (AGOA) – see Box I.2 below.

<sup>6</sup> Broadly speaking, 'LDCs' are not only poor but have little economic diversification and low levels of skills. Most countries in sub-Saharan Africa are LDCs. Kenya is among the few that are not. If income were the only criterion, it would be.



#### Box I.2. AGOA

The African Growth and Opportunity Act (AGOA) was signed into law on 18 May 2000. It is meant to encourage market forces in African countries by offering them the best access to the US market available outside of free-trade agreements. The Act covers some 6,400 items, including textiles and apparel. The AGOA Acceleration Act, signed into law on 12 July 2004 and known as AGOA III, extends this preferential access until 30 September 2015.

Eligibility for AGOA benefits is determined annually on the basis of a review by a committee chaired by the United States Trade Representative (USTR). The criteria require that the country have established, or be making progress towards establishing, a market economy, the rule of law, policies to reduce poverty, and a system to combat corruption. Currently, 38 sub-Saharan countries qualify as eligible, including Kenya.

Ready-made garments have been of particular interest to Kenya, as the Act provides duty-free and quota-free treatment for eligible apparel articles made in qualifying sub-Saharan African countries through 2015. Kenya's textile exports to the US increased from USD 39.5 million in 1999 to USD 273 million in 2006. Total investment in the sector, mainly in the export-processing zones (EPZs), stood at KSh 10,317 billion in 2006, while employment stood at 31,813. (For restrictions on apparel exports under AGOA, see Box III.6 in UNCTAD's 2005 Kenya guide.)

**Sources:** AGOA website: [www.agoa.gov/index.html](http://www.agoa.gov/index.html); EPZA sector profile of the apparel and textile industry: <http://www.epzak-kenya.com/UserFiles/File/ApparelTextile.pdf>; and UNCTAD, 2006.

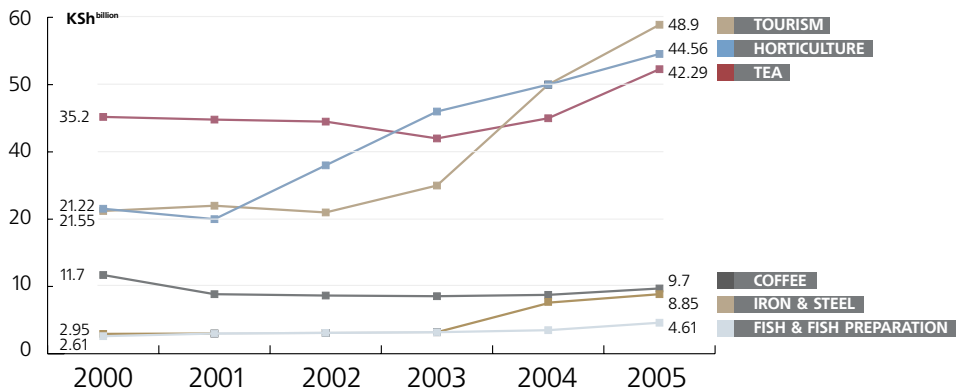
## Exports and imports

Exports are the great Kenyan success story of recent years. As Figure I.4 shows, the top three export products retain their collective lead, though not their individual positions. Tea yielded the top spot to horticulture a while ago, and tourism replaced horticulture in 2005. Coffee, in decline for many years because of global competition among other things, also picked up a bit in 2005. These remain Kenya's principal exports, along with ready-made clothing, which does not appear in Figure I.4 but would rank immediately after tea if it did (see box on AGOA above).

Other exports include fish, plastic goods and pharmaceuticals.

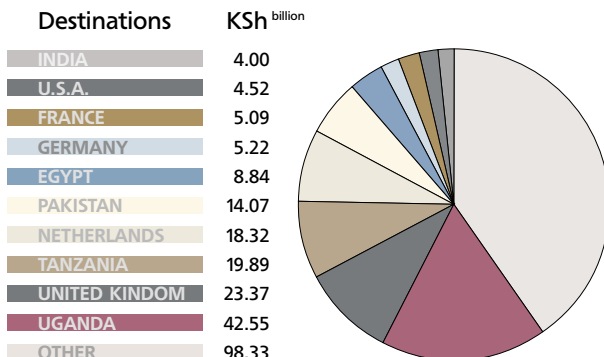
The pie chart below (Figure I.5) shows the chief destinations of Kenya's exports in 2005. The top five destinations – Uganda, the UK, Tanzania, the Netherlands and Pakistan – have been the top five for a decade, though not always in that order. Between 1998 and 2000, Pakistan took in substantially more of Kenya's exports than did the Netherlands. The main export to Pakistan has been tea, while to the Netherlands it has been flowers, and floriculture really took off in the new millennium.

**FIGURE I.4. Selected exports by value, 2000-2005, in KSh billion**



Source: Adapted from the *Economic Survey 2006* by the Export Promotion Council.

**FIGURE I.5. Selected export destinations, 2005, in KSh billion**



Source: Adapted from the *Economic Survey 2006* by the Export Promotion Council.

It is obvious from Figure I.5 that Kenya's exports to the region, in particular to Uganda and Tanzania, are substantial. Petroleum re-exports are a major part of the exports to Uganda but Kenya exports many other things to the EAC. In fact, most of its merchandise exports other than horticulture, garments and tea (which go to the EU, the US and a few other countries overseas) are destined for the region – hence the asymmetrical tariff on them until 2010. Incidentally, it should be noted that not all trade within the EAC shows up in the official figures, as a good deal of it is informal.

The top ten imports and the top ten sources of imports appear in Table I.2. Petroleum and petroleum products together account for over 20% of Kenya's import bill. Industrial machinery and motor vehicles follow. It is noteworthy that no EAC or COMESA member appears among the top ten sources. Indeed, no African country other than South Africa makes the list. Nonetheless, Kenya does have regional imports, including tobacco, beverages and cereals from the EAC and sugar and chemicals from COMESA.<sup>7</sup>

<sup>7</sup> On sugar from COMESA, see more in Chapter II below.

**TABLE I.2. Top 10 import products & import sources in 2005, with values**

	Product	KSh <sup>billion</sup>	Country	KSh <sup>billion</sup>
<b>1</b>	Crude petroleum	51.53	United Arab Emirates	62.13
<b>2</b>	Industrial machinery	48.06	United States	42.49
<b>3</b>	Petroleum products	46.07	South Africa	42.31
<b>4</b>	Road motor vehicles	25.24	Saudi Arabia	27.58
<b>5</b>	Plastics in primary & non-primary forms	17.64	United Kingdom	26.13
<b>6</b>	Animal & vegetable fats	14.01	India	24.24
<b>7</b>	Medicines & pharmaceuticals	12.51	Japan	23.02
<b>8</b>	Chemical fertilizers	10.65	China	19.76
<b>9</b>	Wheat unmilled	7.96	Germany	15.76
<b>10</b>	Organic & inorganic chemicals	7.62	France	13.88

**Source:** Adapted from the *Economic Survey 2006* by the Export Promotion Council.

**Note:** The list of products and the list of countries are unrelated to each other. Total imports in 2005 were valued at KSh 430.74 billion.



## Foreign direct investment

Kenya has long been a surprising laggard in East Africa when it comes to foreign direct investment (FDI). Just as FDI flows to developing countries began to surge in the early 90s, Kenya's inflows began to fall. In the late 90s Kenya was averaging USD 40 million a year when Tanzania and Uganda were averaging over USD 200 million. FDI seemed to pick up a bit in 2003 but has languished again since.

However, over the past several years, the government has been pursuing a variety of measures to create a more appealing environment for potential investors. These include the passage of the bills on investment and privatization mentioned earlier, a simplification of licensing and other procedures and a variety of incentives in export-processing zones (EPZs). For further discussion, see Chapters II and III below.

## Debt, reserves, etc<sup>8</sup>

Kenya's external debt in February 2007 was USD 5.41 billion, 61% of it owed to multilateral creditors and 35% to bilateral ones. Foreign-exchange reserves were USD 3.57 billion in April 2007, providing 3.7 months' import cover. The underlying inflation rate was under 5%, while the overall inflation rate was just under 11%. Remittances by Kenyans abroad amounted to about USD 1 billion in 2006.

<sup>8</sup> These figures are mainly from the Central Bank of Kenya's Monthly Economic Review, April 2007.



**Table I.3. Foreign Direct Investment in East Africa, inflows in USD million**

Country	2003	2004	2005
Burundi	..	-2	-1
Kenya	82	46	21
Rwanda	5	8	8
Tanzania	527	470	473
Uganda	202	222	258

Source: UNCTAD, *World Investment Report 2006*, Annex Table B.1.





Kisumu is Kenya's third biggest city. With its strategic location, hardworking people and agreeable climate, it remains an ideal place to invest in today's Africa. A metropolitan attitude without the hassles of a big city makes for higher productivity in business. With good governance and sound investment, Kisumu can realize its potential for greatness.

Munira Gilani, Director, Peche Foods



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## ii. Investing in Kisumu

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### 1. Introduction

Kisumu, on the eastern shore of Lake Victoria, is Kenya's third largest city, after Nairobi and Mombasa. It is the capital of Nyanza province and the administrative centre of Kisumu district. The population of Kisumu district was projected to be around 565,000 in 2007, with perhaps two-thirds of that (375,000) being the city population. The climate is warm and humid, moderated somewhat by the elevation of over 1,100 metres. The annual rainfall, during the long and short rains in March-June and October-December respectively, is 1,245 mm.

(The reader should note that, in speaking of Kisumu as a location for investment, this guide intends to include both the city proper and the area of which it is the commercial and administrative centre. The map that appears at the beginning of this guide, showing towns and districts within a 60-km radius of Kisumu, is a good approximation of what is intended.)

The modern city of Kisumu began life as Port Florence, the lakeside terminus of the Uganda Railway, which reached Kisumu (from Mombasa) in 1901. Further transport to Uganda was provided by ferry. The rail link with Mombasa on the Kenyan coast and the water transport links with Port Bell, Entebbe and Jinja in Uganda and with Bukoba and Mwanza in Tanzania were the foundation of Kisumu's rise to prominence as an East African trading hub.

The railway from Mombasa still reaches Kisumu, *via* Nairobi, but has suffered greatly from a lack of investment and poor maintenance. Rift Valley Railways (RVR) of South Africa now has a 25-year concession to rehabilitate and run the railway, but the transfer to private management, completed in 2006, is still too new to have made a difference. Kenya Airways offers two daily flights between Nairobi and Kisumu and other airlines offer another half a dozen. There have been some discussions about upgrading Kisumu airport to international status, which would be a substantial attraction to export industries, but this is thought unlikely to happen soon.

Economically, the good years in Kisumu were the same as in Kenya generally, the 60s and the 70s. Since then, the economy of the city has tended to stagnate. One explanation sometimes offered is trade liberalization, which is said to have damaged the traditional industries of cotton and sugar. Another is that the sugar industry in particular has been dominated by parastatals and has suffered from the usual problems of underinvestment and poor



management that characterize the state-owned sector. This has been compounded by the neglect of infrastructure, both within the city and in its external links, thus raising production costs and reducing market access. A further difficulty has been damage to the enormous natural resources represented by Lake Victoria, through pollution, overfishing and the growth of water hyacinth.

Nonetheless, Kisumu is a vital city. The Municipal Council of Kisumu<sup>9</sup> has recently outlined a development strategy that places investment and public-private partnership at its very centre. Kisumu is the headquarters of both the Lake Basin Development Authority (LBDA) of Kenya and the Lake Victoria Basin Commission (LVBC) of the East African Community. (For some investment opportunities identified by the LBDA, see section 2 below.) A number of educational institutions are based in or near Kisumu. These include Maseno University, Kisumu Polytechnic, Tom Mboya Labour College and the Great Lakes University of Kisumu (formerly the Tropical Institute of Community Health and Development). Other related institutions are the Centre for Disease Control and the Kenya Medical Research Institute. The city also offers a well-regarded workforce, both skilled and unskilled.

The development strategy mentioned above has a vision of Kisumu as a leading transport, communication and commercial hub in the Great Lakes<sup>10</sup> Region, offering great tourism and agro-investment opportunities. As the closest municipality to the Millennium Village Cluster, the integrated rural development project of the Earth Institute and the World Agroforestry Centre (ICRAF) located in the neighbouring Siaya District, Kisumu is the logical manufacturing, processing and marketing centre for the increased and diversified agro-production expected to issue from the Millennium Villages over the coming months.

## 2. Opportunities for investors<sup>11</sup>

### Main areas of interest to potential investors

#### *Sugar and ethanol*

Sugar has long been the major industry in western Kenya and several million people are thought to be supported directly and indirectly by the industry. There are some 200,000 smallholders who grow cane and seven operating sugar mills, as well as transporters and distributors. The smallholder farms are typically small, of less than 1 ha, and the cane yield per ha is low, 50-60 tonnes per ha, as against nearly 100 tonnes per ha in Tanzania. The variety of cane commonly grown also has a long maturity period and a low sugar yield.

Of the seven sugar mills – Mumias Sugar Company Ltd., West Kenya Sugar Company Ltd., SOIN Sugar Company Ltd., Muhoroni Sugar Company Ltd., Nzoia Sugar Company Ltd., Chemelil Sugar Company Ltd., and South Nyanza Sugar Company Ltd. (SONY) – four are state-owned, along with a fifth that ceased operation in 2001.<sup>12</sup> Mumias, West Kenya and SOIN are private enterprises. Mumias is the largest and accounts for nearly half of Kenya's total production. It is also the most efficient. The state-owned companies are both inefficient and deeply in debt.

The chief impending problem for the mostly uncompetitive sugar industry is that its protection against much cheaper imports from its COMESA partners, mainly Egypt and Swaziland, is set to disappear in early 2008. There is a possibility that the safeguard agreement that provides this protection could be extended for another two years, until 2010. The agreement currently restricts imports to 200,000 tonnes, which is about a third of the total Kenyan demand. The seven Kenyan sugar factories produce the remaining 500,000 tonnes.

<sup>9</sup> Kisumu City Development Strategies (2004-2009), no date.

<sup>10</sup> The largest of the Great Lakes of Africa are all in East Africa: Lake Victoria, Lake Tanganyika and Lake Malawi (also known as Lake Nyasa), in that order.

<sup>11</sup> A team from Columbia University's School of International and Public Affairs carried out a substantial study of investment opportunities in Kisumu in 2006-2007 for the Millennium Cities Initiative. The present section draws extensively on this study. Although the study had a broader development mandate than simply identifying commercially profitable prospects, its assessments keep commercial viability very much at the front and centre, and are thus of direct relevance to investors. See Aguilo, et al., 2007, in **Sources consulted** at the end.

<sup>12</sup> The fifth is Miwani, the oldest sugar factory in Kenya, set up in 1922.

What keeps the domestic firms afloat is the high domestic price. The average retail price for a kilo of mill white domestic sugar in 2006 was KSh 64, while the average ex-factory cost for the industry as a whole was KSh 53.54/kg. At the same time, the average landed price for mill white imported sugar was KSh 29.05/kg. Figure II.1 shows the difference in prices per tonne over a 10-year period.

Under these circumstances, many believe that only Mumias could survive the full liberalization of imports.<sup>13</sup> If the state-owned enterprises are to survive, they would need to be privatized.

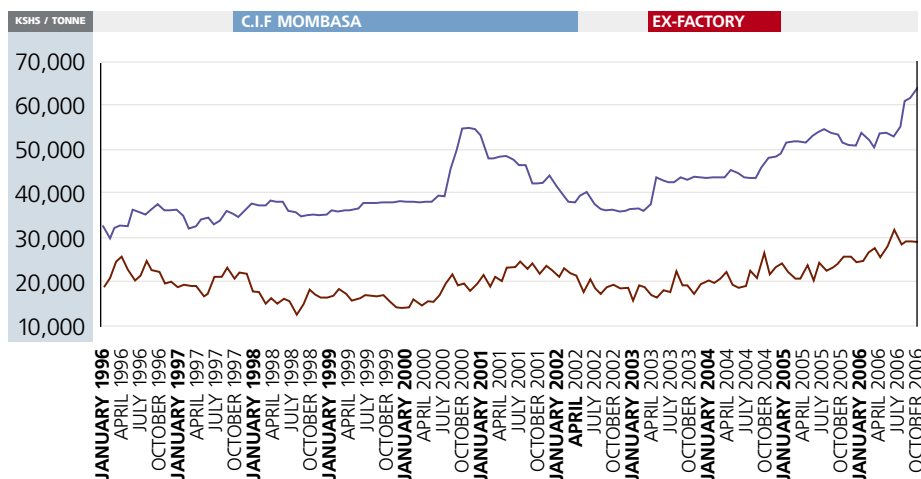
This, then, is one opportunity for investors, to invest in the existing private companies and to invest in the state-owned ones when privatized. Mumias demonstrates that sugar *can* be produced competitively in Kenya and there *is* substantial domestic demand to be met at competitive prices.

It is unclear how quickly the privatization of the SOEs could occur. The Privatization Bill is now law and a Privatization Commission is to start operating this year. On the other hand, the SOEs would need to go through a restructuring process to deal with their substantial debts. The government does regard privatizing these firms as a priority, however, and Muhoroni and Miwani are said to be ready for privatization.

The other major opportunity is in using sugarcane to produce ethanol rather than sugar. Ethanol is produced for consumption, for industrial purposes such as solvents, and above all for fuel. It can be derived from juice squeezed from sugarcane, molasses produced as a by-product of sugar production, or sugar crystals. A common strategy is to link an ethanol distillery to a sugar mill, limiting transport and energy costs, and allowing the producer to shift back and forth between sugar and ethanol as their relative prices fluctuate.

<sup>13</sup> Aguilo, et al., 2007.

**FIGURE II.1. Sugar prices, ex-factory Kenya & cif imports, 1996-2006**



Source; Aguilo, et al., 2007.



There are several distilleries currently in place in and around Kisumu, producing industrial or potable alcohol. One of them belongs to Spectre International, which has rehabilitated the abandoned facility of the Kenya Chemical and Food Corporation (KCFC) on the outskirts of Kisumu – see Box II.1 below.

An investment in fuel ethanol production could take the form of a greenfield operation, with a stand-alone distillery producing ethanol from feedstock drawn from nearby smallholders or from the nucleus estates of SOEs closed in the wake of an import surge. It could also take the form of investment in a distillery attached to an existing sugar mill.

A government mandate requiring the addition of ethanol to fuel oil in a 10:90 ratio, an E10 mandate, is a possibility. Certainly, Kenya would gain from reducing its very large fuel import bill. The availability of feedstock is another incentive, especially if the demand for cane to produce sugar declines substantially in a post-2010 world of liberalized sugar imports. Kenyan ethanol may also have substantial export prospects, given the fuel needs of large and fast-growing economies like those of China and India.

#### Box II.1. Investment story: Spirits and yeast

Spectre International is a joint venture by Canadian and Kenyan investors that produces alcohol from molasses. The Canadian investor is Energem Resources Inc., a natural resources company listed on the Toronto Stock Exchange and engaged in 13 African countries in long-term energy and mining projects. Energem owns 55% of Spectre and has thus far invested around USD 12 million. The company has 200 permanent employees and an additional 200 casual or contract employees. Three of the permanent employees are expatriates.

Spectre International was set up in 2003, when it acquired the abandoned facility of the Kenya Chemical and Food Corporation (KCFC) on the outskirts of Kisumu. The KCFC began in the mid-1970s as a visionary state project responding to the oil crises of the 70s. The aim was to produce fuel ethanol from molasses. However, after a large investment was made and the plant was built, the project stagnated on account of financial as well as political problems. Spectre's reasons for locating near Kisumu, beyond the presence of the KCFC facility, included the proximity of Lake Victoria as a source of water and the availability of the necessary raw material, molasses, in the area.

The company's intended products fall in three categories: industrial ethanol for blending with liquid fuels (bio-fuels), alcohol for beverages and chemical industries, and yeast. At the moment, it is not producing fuel ethanol. It is producing various grades of alcohol: neutral spirits for use in the manufacture and blending of products like vodka and brandy, rectified spirit for use as industrial solvent, and methylated spirits for use in a variety of industrial products and processes. It is also producing yeast of different sorts for use in baking. Spectre's markets are both in Kenya and in the region. At the moment, about 70% of the spirits the company produces are exported. Current production is around 60,000 litres a day (or 1.2 million litres a month). This could easily be doubled, with marginal investment, if sufficient feedstock were available.

Ruth Odinga, a director of Spectre, identifies taxation as the major challenge the company has faced. The Kenya Revenue Authority (KRA), according to Ms Odinga, seldom consults with stakeholders before issuing its directives. According to one recent KRA directive, spirit producers are required to pay what amounts to 400% of the product price in taxes up front. The effect of this sort of taxation, motivated by little except the desire to meet pre-set tax revenue targets, is to encourage regional buyers of Kenyan spirits to look for other and cheaper sources.

Nonetheless, Ms Odinga thinks there are opportunities in the Kisumu area which are well worth exploring. There are also tax advantages in locating outside Nairobi. Although the licensing regime is much criticized by investors, it is improving and a number of licenses are being abolished. Spectre itself is committed to Kisumu and would like to see more investors come to the area.

**Source:** Millennium Cities Initiative, drawing on information provided by Spectre International.

### *Groundnuts (peanuts)*

Nyanza province produces the majority of Kenya's groundnuts. Nearly 60% of Kenyan land under groundnuts in 2003 was in Nyanza, producing 7.2 million kg valued at KSh 444 million. This is basically a subsistence crop, so the use of fertilizers and pesticides is minimal, and yields are low. The nuts are sold unprocessed in small quantities by informal vendors. There is some processing in Nairobi, which produces either roasted and seasoned nuts or peanut butter. The processed products are sold to high-end supermarkets or to commercial users such as boarding schools. Peanut oil does not appear to be produced, at least on a large scale, and it is currently too expensive for most Kenyan consumers.

There is a definite opportunity in setting up a groundnut-processing plant in Kisumu, as 30 to 40 per cent of the provincial crop passes through Kisumu markets on its way elsewhere. Such a plant would be able to buy nuts at a lower cost than a plant in Nairobi and to sell its product at a lower cost. An investor in such a plant would also be able to supply inputs to outgrowers and to raise yields per ha from between 400 and 480 kgs to anything up to 1,000 kgs or more.

The plant could produce peanut butter or peanut oil. Peanut butter is an established product in Kenya and the market for it is growing at about 18% p.a.<sup>14</sup> A 300g container of peanut butter produced in Kenya sells for about KSh 100; imported brands from South Africa and the U.S. sell for about twice that price. Peanut oil may also be a viable product. Even if it cannot be sold domestically for cooking purposes, it can be sold for use in processed foods, cosmetics, and paints and finishes. The process of oil extraction also produces oil-cake as a byproduct, which can be sold as animal feed or fertilizer. In the long run, peanut oil, widely used in Asian cooking,

may have significant export prospects. (Its import-substitution value is also considerable, as animal and vegetable fats are a major import in Kenya, valued at over KSh 14 billion or USD 200 million in 2005 – see Table I.2 in Chapter I above.)

### *Aquaculture*

One would expect the largest Kenyan city on the shores of Lake Victoria to offer serious opportunities for investors in fisheries. Unhappily, this does not seem to be the case. Although Lake Victoria has traditionally accounted for well over 90% of the fish landed in Kenya, fish stocks have been in sharp decline in recent years. In 1999, the Lake Victoria fish catch was 200,159 tonnes; in 2005, it was 124,625 tonnes.<sup>15</sup> Part of this is due to pollution; part of it the unfortunate consequences of the introduction of an alien species, the Nile perch, into the lake in the 50s; and the third damaging element is the spread of water hyacinth, a weed that threatens fish through de-oxygenation, offers a hospitable site for malarial mosquitoes, and interferes with water transport.

On the other hand, there are serious opportunities in *aquaculture*. Although aquaculture has thus far played a marginal role in the Kenyan economy (less than 1% of the total catch), it has a long history in the country, having been introduced in the 20s to support sport fishing. Most existing aquaculture is small-scale, with something over 7,000 ponds farmed by nearly 5,000 fish farmers. There is commercial potential to be developed, however, and the Department of Fisheries is taking a number of initiatives to expand and promote it.

Kenya's varied climate makes it suitable for farming a variety of fish including tilapia, African catfish, the common carp and rainbow trout. Of these, tilapia is the preferred species for cultivation as it does not require sophisticated feeds, can withstand low oxygen levels and poor water quality, and

<sup>14</sup> According to Truefoods Ltd, a Kenyan producer of peanut butter, as reported in Aguilo et al., 2007.

<sup>15</sup> This was actually a recovery from the 2003 figure of 105,866 tonnes. Table 8 in Government of Kenya, Ministry of Environment and Natural Resources, March 2007.

does best in the warm waters found in the Lake Basin region. The rainbow trout is more demanding but fetches higher prices. A number of swamps amenable to aquaculture have been identified, including Sondu Swamp, Yala Swamp and Nyando Swamp.

An example of commercial aquaculture on a large scale is about to be provided by Dominion Farms – see box below. According to both local observers and the Department of Fisheries, the Dominion model may be replicable, as the demand for fish is substantial and much of the Lake Basin wetlands unutilized.<sup>16</sup> Tilapia, catfish fingerlings, or both (in a process known as polyculture) offer opportunities. As the fish of choice within Kenya and a fish with increasing international demand, tilapia can serve both domestic and foreign markets. Given its proximity to Europe, an investor in Kenya would have an advantage over its Asian competitors in exporting fresh tilapia fillets to the EU.

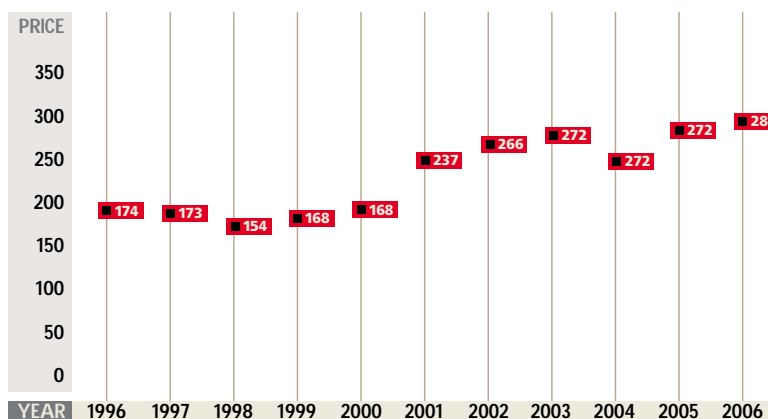
Catfish production can serve the Kenyan market and provide fingerlings to be used as bait. The availability of fingerlings, immature fish acting as “seedlings” for fish farms or baitfish for long-line fishermen in Lake Victoria, is currently low. As reported in a USAID call for proposals to develop of catfish fingerling production clusters, the Kenyan demand is between 5,000 and 50,000 catfish fingerlings per day, or an annual demand exceeding 15 million fingerlings.<sup>17</sup> Considering that polyculture systems combining catfish and tilapia are common, the sale of catfish fingerlings, either as seedlings or baitfish, presents a natural source of supplementary income for an investor interested in a tilapia farm.

Another opportunity is represented by fish feeds. About two tonnes of feed are needed to produce a tonne of fish. The fact that a major constituent of fish feeds is sunflower seed or cottonseed oil cake underscores the suitability of Nyanza province as a location for a fish feed plant. Production of feeds from other locally produced oil sources such as groundnuts may also be feasible.

<sup>16</sup> As reported in Aguilo, et al. One should note, however, that the wetlands are ecologically important. The Lake Basin Development Authority's decision to award 17,000 acres of wetlands in Yala Swamp to Dominion Farms was opposed by local conservationists. The possible constraints imposed by conservation regulations such as the Nile Basin Treaty would also need to be looked into. (The treaty, signed in 1929, in effect guarantees that water flow to Egypt would not be reduced by the actions of the other nine signatories – most of whom are dissatisfied with the treaty as it stands.)

<sup>17</sup> Aguilo et al., 2007.

**FIGURE II.2. Prices of fish exports, 1996-2006, in KSh per kg<sup>a</sup>**



**Source:** Peche Foods, Kisumu, 2007 and EPZA, Fishery Industry in Kenya, 2005 ([www.epzakenya.com/userfiles/file/fishkenya.pdf](http://www.epzakenya.com/userfiles/file/fishkenya.pdf)).

<sup>a</sup> Prices for all years except the year 2000 are from Peche Foods and for Nile Perch. The price for 2000 is from the EPZA sectoral profile and is mainly for Nile Perch, said to account for more than 80% of Kenya's fish exports.



#### Box II.2. Investment story: Aquaculture and rice-farming

Dominion Farms is part of the Dominion Group of Companies, founded and owned by Calvin Burgess of Guthrie, Oklahoma. The Group's main business in the United States is in land and real estate development. Dominion Farms in Kenya is the Group's first agricultural venture, which began in 2003 and currently has over 400 permanent employees, including 5 expatriates. The company also employs up to 1,000 casual workers when required. The business mission is to produce and sell rice and other cereal grains in the Kenyan and East African markets, and tilapia fish in the Kenyan and European markets.

As of now, the Kenyan operation is still largely in a building stage, although substantial investment has already been made (USD 15 million) and the project's ambitions are considerable. The company expects to produce 100,000 tonnes of rice when fully operational by 2010. Also scheduled for completion in 2008 is an aquaculture operation capable of producing 20,000 tonnes of tilapia per annum. The aquaculture farm will be complemented by a feed mill and a fish-processing plant.

This was a business project motivated by philanthropy, by a desire to make a difference through an operation that would eventually become self-sustaining, creating employment and reducing poverty, while at the same time earning a reasonable return on the investment. There was no specific reason why Dominion began the project in Kenya, except that an opportunity was presented which looked like a challenge, and at the same time showed a promise of profitability. The company is fully foreign-owned and has no local partner.

Mr Burgess, the CEO, assesses the investor's environment as poor, with infrastructure the main culprit. Port and customs services and the regulatory burden of a complicated licensing system have added to the company's difficulties. These are judgments shared by most investors in the area. Dominion Farms has also faced some unique challenges of its own, in the form of opposition by NGOs concerned with the environment, land rights and the like. Over time, the criticisms of the project, which the company sees as misrepresenting its intentions and accomplishments, have been diffused.

The urgent task for the government, in the company's view (again a view shared by the investor community generally), is to repair or replace the inadequate infrastructure, so that producers can get their goods to market. There have been some improvements in infrastructure (in roads, telecommunications, power supply, etc.) but much more needs to be done. Dominion Farms sees itself as in for the long haul and would like to encourage other investors to come in with a similar long-term perspective. Without such a perspective, an investor is unlikely to succeed in the Kisumu area, since the area is as rich in difficulties as it is in opportunities. The company plans to expand into other East African countries in due course.

**Source:** Millennium Cities Initiative, drawing on information provided by Dominion Farms.

**Other areas of interest to potential investors**

*Rice*

Rice is a staple food in Kenya, with consumption estimated at 250,000 tonnes a year and growth at 12% p.a., and it was once a major agricultural crop in western Kenya. However, it has suffered from a variety of problems, including a lack of seeds and fertilizer, little research support, inadequate irrigation and so forth. These have made it hard for domestic growers to compete with rice imported from Asia, in particular Pakistan, in a liberalized trade environment. So only about a fifth of the total demand is met domestically.

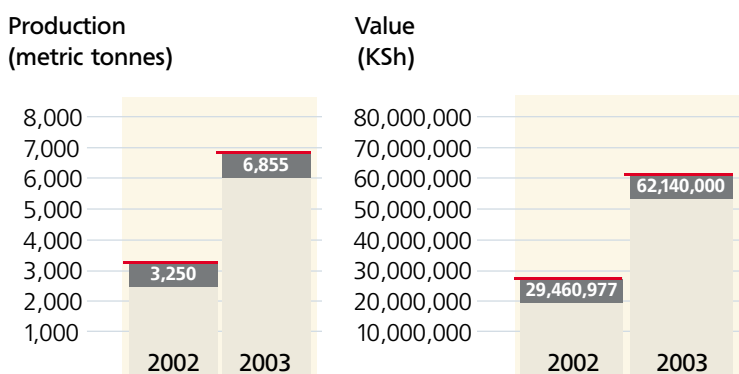
Many of the constraints on rice production could be dealt with by an investor prepared to make a significant investment. Kenya has the potential not only to meet its own demand for rice but also to supply the region. Nyanza Province’s proximity to Lake Victoria and its wetland composition make it an ideal site for irrigated rice production in Kenya. Dominion Farms again offers an example. It expects to have 5,600 ha under rice, producing twice as much rice as currently produced in the country as a whole.<sup>18</sup>

The Lake Basin Development Authority (LBDA) has built a rice mill at Kibos, in Kisumu district, capable of milling and packaging 3.5 tonnes an hour and storing 17,000 tonnes in six godowns. In 2005, the LBDA listed the Kibos mill, one of the largest in East and Central Africa, as a joint-venture opportunity in need of partners to run it on a commercial basis. As of March 2007, three potential partners had been identified: Uchumi supermarkets, United Millers, and an unidentified American firm.

**18** Note that the concerns about conservation and the Nile Basin Treaty mentioned in fn. 16 above might be relevant here as well. There may also be land issues. On land generally, see Chapter III below.



**Figure II.3 Rice production in Nyanza province, in metric tonnes & KSh**



Source: EPZA, Grain Production in Kenya, 2005 (www.epzakenya.com/userfile/filegrainreport.pdf).

## Horticulture

As noted earlier (in Chapter I), horticulture exports are one of the great success stories of the Kenyan economy in recent years. They have earned foreign exchange, created employment and increased the incomes of outgrowers. A number of fruits and vegetables are produced in and around Kisumu (Table II.1 below) and many of them are sold elsewhere in Kenya in significant quantities. (The Millennium Village farmers in neighboring Siaya District have begun to diversify from their staple maize crop into readily grown onions, tissue culture bananas, soy and fruit trees, with domestic, regional and international markets in mind.) Some Kisumu area produce is also exported; for example, passion fruit is exported by East African Growers in Nairobi. A number of large companies, foreign and domestic, have expressed an interest in horticultural products from the area. Unilever is interested in sunflowers as a source of oil and is interested also in sourcing unrefined sunflower oil, chillies, fennel and rosemary from the area. Tetra Pak, a Swiss/Swedish processing, packaging and distributing multinational, has expressed an interest in the processing of tomatoes.

A constraint to note, when it comes to exporting, is transport and cold storage facilities. See section on *Air transport* in 4. The business environment below.



**Table II.1. Horticultural production, Nyanza province, 2005**

	Area planted <sup>(ha)</sup>	Quantity produced <sup>(tonnes)</sup>	Value <sup>(KSh million)</sup>
bananas	22,334	504,336	5,262
sweet potato	...	271,514	2,000
tomatoes	6,132	120,283	2,569
onions	1,931	20,439	553
avocadoes	1,485	21,061	245
passion fruits	1,109	4,127	190
sunflower	708	434	7
soy	241	1,405 <sup>bags</sup>	5
chillies	32.5	238.5	17

**Source:** Aguilo, et al., 2007, drawing on Ministry of Agriculture, 2005 Annual Report.



## Dairy

Little formal dairy production currently occurs in the greater Kisumu area. Most processed milk and other dairy products are produced in central Kenya. (But see Box II.4 below for a new milk-processing venture in Kericho.) In 2006, demand for milk in Kisumu district was 40 million litres, while production was just over 14 million litres. The province as a whole also has a large deficit in milk production.

On the other hand, dairy farms in the area appear to be doing well. Mukumu Farm near Kakamega, one of the largest in the area, operates on 65 acres with 50 mature milk cows and 40 young cows. It sells all of its milk locally and unprocessed for KSh 35 per litre, compared to a price of over KSh 50 for processed milk. The manager

of the farm believes that he would have no trouble selling more milk if he had additional production capacity and that his profits would be higher if he were using Friesian cows, which produce 50% more milk than Guernseys.<sup>19</sup> The demand for high-quality dairy cows with well-kept records is very high, according to those interviewed by the Columbia University team. Such cows are not available in the area and can cost KSh 50,000-120,000 in central Kenya. Large numbers of cows would have to be bought abroad.

Opportunities thus exist for large-scale producers and processors in this field, as well as for cattle breeders. The demand for milk is growing, and the red clay soil and rain conditions in the area are thought to be good for cattle-raising and cattle feed production.

<sup>19</sup> As reported in Aguiló et al., 2007.



## Tourism

Kenya has long been the leading international tourist destination in East Africa, as is clear from Table II. 2 below.<sup>20</sup> This does not, however, seem to have helped Kisumu. The tourists go to Mombasa for the beaches and to Masai Mara for wildlife. Although Kisumu is somewhat closer to the Masai Mara than Nairobi, the roads are not the easiest to drive on, especially when it rains. The chief local attraction, Lake Victoria, is less of a draw than it might be because of pollution and water hyacinth.

However, the government of Kenya has prioritized the western circuit in its current national development strategy and the LBDA is working on a plan for the western circuit that markets eco-tourism to

American tourists. UN Habitat is also developing a plan involving the creation of a tourist information office and the inclusion of Kisumu in the Kenyan tourist circuit. The city has several tourist sites close by, such as the Ruma National Park (four hours from Kisumu) to the south, Ndere Island (one hour from Kisumu) to the north and Kakamega forest (one and a half hours from Kisumu) to the east. These are all relatively small sites and are more abundant in birds than in large mammals. (The wildlife draw in East Africa is the big five: lion, leopard, elephant, rhino and buffalo.)

The majority of current tourists are business people from other parts of Kenya, employees of international bodies and NGOs, and people with family links in or around Kisumu. There are currently eight

**20** It does better, however, on arrivals than on receipts, especially as compared to Tanzania. This is mainly because much of the tourism in Kenya is relatively inexpensive beach tourism, as against Tanzania's mostly high-end safari tourism.

**Table II.2. International tourism in East Africa, 2001 and 2005**

Country	Number of arrivals in thousands		Receipts in USD million	
	2001	2005	2001	2005
Burundi	36	148	1	2
Kenya	841	1,199 <sup>a</sup>	536	969
Rwanda	113	--	29	--
Tanzania	501	566 <sup>a</sup>	626	836
Uganda	205	468	187	357

**Source:** Adapted from the World Bank, *World Development Indicators*, 2007.

<sup>a</sup>Figure for 2004.





to ten daily flights to Kisumu from Nairobi, and one opportunity for investors lies in low to mid-range hotels, of which there is a clear shortage. There may also be an opportunity in creating a conference centre, with associated facilities. The LBDA is building a new headquarters complex, in which it invites investment partners. The complex is to be a 12-storey multi-use office block, shopping and conference centre, and restaurant, located on 9.3 ha of land about 6 km from the city centre. The ground floor and basement were built a few years ago but the project stalled for want of funds. Office space is in short supply in Kisumu and conference facilities could be particularly useful, given Kisumu's central location in the East African Community. The estimated cost of completing the project is KSh 500-600 million.

At this point, domestic and regional tourism probably offers the best prospects. The increasing importance of the EAC can be expected to contribute to this.



**Box II.3. Investment story: Food and hospitality**

Mayfair Holdings is a locally owned business in Kisumu. The Gilani family has been in East Africa since the early 1900s, like a number of other business families of Indian origins. The main business activities are baking, fish-processing and hospitality. The oldest operation is the Mayfair Bakery, set up by S. M. Gilani in 1966. The bakery was upgraded to an automated plant in 1986. Just a year earlier, in 1985, the firm had begun to diversify by building the Imperial Hotel, which remains to this day the most highly regarded hotel in Kisumu.

The most recent Gilani venture (1994) is Peche Foods, a fish-processing plant that exports both frozen and fresh Nile Perch, Lake Victoria's best-known export product, to Europe, Japan, the Middle East and the United States. The reason for this last investment was the proximity of Lake Victoria. Although several other towns in Kenya's neighbours, Tanzania and Uganda, are also on the lake shore, there were no fish-processing factories outside Kenya in the mid-1990s. Today, there are 7 in Tanzania and 15 in Uganda. Of the four Kisumu factories, Peche foods is the smallest, exporting about 1,000 tonnes a year.

Mayfair is a fully family-owned business with 280 employees, 200 of them core employees and the remainder part-time and casual. The company has no expatriates working for it.

Munira Gilani, who runs Peche Foods, assesses the investor's environment as tough, especially for newcomers, but full of opportunities. There is a shortage of hotel rooms in Kisumu, for example. (Mrs Gilani is not particularly worried about competition for the Imperial Hotel.) The progressive integration of the East African Community is something the family sees as highly desirable. The free flow of goods and services in the region would be helpful for all the companies in the Mayfair group.

The main problems for investors in Kisumu are the poor infrastructure, especially the road to Nairobi; an excess of bureaucracy, as witness the number of licenses businesses need to operate; and corruption. For Peche Foods, there has also been another problem: the security of transport. Periodically, a truck carrying fish to Nairobi gets hijacked. (Other investors in Kisumu have also experienced this problem, although its severity varies according to the goods being transported.)

Mrs Gilani believes that what the government needs most urgently to attend to are the twin problems of infrastructure and bureaucracy. If these were addressed, there are plenty of opportunities to be exploited. Mayfair Holdings is committed to Kisumu and plans to stay, to improve and to expand. The people and the climate of Kisumu are major assets for all investors.

**Source:** Millennium Cities Initiative, drawing on information provided by Mayfair Holdings.

## Cotton

Cotton-growing and related industries (ginning, spinning, weaving and garment-making) flourished under the import-substitution policies Kenya adopted in the 60s and 70s. Twenty-five years ago, textiles were the leading manufacturing sub-sector in Kenya, employing nearly one-third of the industrial workforce. Several factors, including easier imports of second-hand clothing and progressive trade liberalization in the 90s, led to the decline of the textile industry and a sharp reduction in the production of raw cotton.

Cotton-growing is mostly a small-farm, rain-fed activity in many parts of Kenya. In 2003, there were an estimated 140,000 cotton farmers with about 25,000 ha under the crop in all of Kenya. On the other hand, 370,000 ha of land is thought to be suitable for cotton-growing just in the Nyanza and Western provinces.<sup>21</sup> Many ginneries, textile mills and garment-making factories have closed since the 90s and in others there is significant under-utilization of capacity.

The one positive development of recent years is the growth of garment exports to the United States under AGOA (see Box I.2 in Chapter I). Most of the fabric used for these garments is imported, mainly from Asia. Although some doubt that Kenya's domestic textile sector can produce the quality and quantity of fabric required for AGOA exports, at a competitive price, this may be precisely where FDI could be most helpful, whether as greenfield investment or in joint ventures with domestic partners. Kisumu Cotton Mills (Kicomi) is one example of a (now privately owned) Kenyan textile firm that has had its ups and downs over the past decade and a half, but is now being revived. It needs to improve its spinning technology and do more value addition, and would be interested in strategic tie-ups with foreign companies that could help it benefit from the AGOA and ACP arrangements.<sup>22</sup>

<sup>21</sup> EPZA, Kenya's Apparel and Textile Industry, Sector Profiles, <http://www.epzak-kenya.com/sector.php?sub=44&cat=12>.

<sup>22</sup> As reported in a preliminary UNIDO note on Kisumu company profiles.



### *Miscellaneous opportunities*

Investment opportunities in the Kisumu area arising from *privatization* are mainly to be found in the sugar industry. These have been mentioned under *Sugar and ethanol* above. Foreign investors may participate in privatization with no restrictions other than the few mentioned in Table III.3 in Chapter III below, under **Restrictions on equity**.

There is said to be considerable demand for *water transport* on Lake Victoria. As indicated in section 4 on the **Business environment** below, a number of ferries are currently in operation. But there is room for more. Potentially, there may also be a demand for passenger service. At the moment, there are no direct air links with Kampala in Uganda or Mwanza in Tanzania. One needs to go through Nairobi, which is time-consuming. The steamers that once plied the waters of the lake could be resuscitated as a profitable venture.

Other opportunities include *construction*. There is a need for low-cost housing in Kisumu, which has grown in a haphazard fashion over the past several decades. (Other construction opportunities have been mentioned under *Tourism* above.) There may also be an opportunity in *cement* production. In Koru and Songhor, there is a limestone deposit of approximately 85 million tonnes, which may be suitable for cement manufacturing.

### *FDI and linkages*

The benefits of many FDI ventures, both to the investor and to the host economy, often depend upon the way these ventures are integrated into the community in which they are located. This is not simply, or even primarily, a matter of 'corporate social responsibility' as it is often understood. It is a matter rather of productive economic relations between the foreign investor and local actors – above all, small and medium-sized local enterprises (SMEs). In this context, a successful recent initiative in one of Kenya's neighbours, Tanzania, is worth noting. (Box II.5 below)



#### Box II.4. Investment story: Confectionary and transport

The Swan Industries Group is a locally owned business conglomerate in Kisumu. Like many Indian businesses in East Africa, the group began as a small retail operation in consumer goods in the 1950s. In 1972, it moved into food-processing in a small way, converting coarse salt into table salt, and into packaging. In 1978, after the current director of Swan Industries, Sailesh Shah, had completed training in confectionary manufacturing in Germany, the group began the manufacturing of sweets. In the same year, it also began a small transport operation, with two trucks. (Today, there are 160 trucks.) In 1982, the group set up a flour mill, which it sold in 2006. In 2007, it has just set up a milk-processing plant in Kericho district, not too far from Kisumu. This venture has been undertaken with Tetra Pak, the Swedish multinational, as the supplier of packaging products.

Although the group has non-family shareholders, management control rests with the Shah family. The annual turnover of the group is around KSh 700 million and it is growing at around 5% p.a. There are 800 employees, most full-time and salaried, of whom 7 are expatriates, all in the transport business.

Mr Sailesh Shah assesses the investor's environment as not very conducive to investment. One factor in this, according to Mr Shah, has been the way the policy shift from import substitution to trade liberalization was carried out. The government did not engage in any serious dialogue with investors about this change, nor did it provide advice and support during the transition phase. In addition, the government could do much more to create an enabling environment of the sort that would help enhance the competitiveness of Kenyan businesses in the global market. As things stand, the regulatory system makes investment difficult, in particular the tax regime and the licensing requirements.

In spite of these criticisms, Mr Shah sees the trend in a number of critical areas, including infrastructure, as positive. Kisumu offers a variety of assets – including its workforce, its climate, a safe environment and a strategic location in East Africa – that could help create a more dynamic economy. It also offers a large number of opportunities for investment, e.g., opportunities in low-cost housing. But all this potential can only be realized if the government, at all levels, displays great vision. The role of the city council is critical in this context, in Mr Shah's view, in promoting Kisumu as a destination for investment. It needs to realize that Kisumu is only one among many destinations competing for investment in an increasingly mobile world.

**Source:** Millennium Cities Initiative, drawing on information provided by Swan Industries.

#### Box II.5. Business linkages in Tanzania

The business environment of many developing countries suffers from the problem of the "missing middle" - there are a few large (often foreign) corporations on the one hand and a very large informal sector with very limited capacities on the other. The Private Sector Initiative Tanzania, known as Psi Tanzania, addresses this problem. It began when BP Tanzania approached SBP, a research and private-sector development organization based in South Africa, to help create an enterprise development programme. Psi Tanzania was formally launched in mid-2002. The programme has been a boon to both large companies - who can carry less stock, reduce import hassles and minimize transaction costs - and local SMEs - who develop their capacities and find new business.

The initiative was launched by eight charter members: BP Tanzania, Kahama Mining, Kilombero Sugar, National Microfinance Bank, Sumaria Group, Tanga Cement, Tanzania Breweries and Tanzania Cigarette Company. By 2005, the membership had grown to 17, with the following additional members: Celtel, Coca-Cola Kwanza, CRDB Bank, Geita Gold, Mac Group, Mobitel, Placer Dome, Resolute Tanzania and Standard Chartered Bank. Psi has a database of local SMEs which its members use for import substitution. There is no formal secretariat. Psi members select one of their own to chair the Initiative for a year and this company in effect acts as a secretariat. This informally organized exercise has been a very substantial success, with USD 51 million spent by its members on local sourcing from SMEs in its first two years of operation.

**Source:** UNCTAD, *An Investment Guide to the East African Community*, 2005.

### 3. Incentives, EPZs and related matters

#### Incentives in Kenya

Investment incentives in Kenya are primarily associated with export-processing zones (EPZs). There were 39 EPZs in Kenya in 2006, of which 37 were privately developed and operated. They hosted 71 firms, of which 83% were partially or fully foreign-owned.<sup>23</sup> They accounted for nearly KSh 23 billion in exports (roughly 10% of Kenya's total merchandise exports), about KSh 15 billion of which were garment exports destined for the United States under the preferential treatment granted by AGOA (box in Chapter I above).

The total investment in EPZs was just over KSh 20 billion and the total Kenyan employment close to 37,000. The total expenditure by EPZ firms on goods and services sourced from the domestic market in 2006 was just over Ksh 9 billion.

There is at present no EPZ in Kisumu. However, the EPZ Authority would be very happy to see one developed. Information about the requirements and procedures is available from the EPZA website, which is notably informative and user-friendly. Full contact details for the EPZA are provided in the **Appendix**.

Incentives currently available to EPZ enterprises are summarized in Table II.3 below.

<sup>23</sup> Note that a number of the EPZs are single-firm operations.

**Table II.3. EPZ incentives in Kenya, 2007**

Category	Incentive
Corporate tax	<ul style="list-style-type: none"> <li>• 10-year exemption from corporate income tax; 25% maximum rate for next 10 years (not applicable to EPZ commercial licenses)</li> <li>• 10-year exemption from withholding tax on dividends &amp; other remittances to non-residents (not applicable to EPZ commercial licenses)</li> <li>• 100% investment deduction on buildings and machinery investment over 20 years</li> </ul>
Other taxes	<ul style="list-style-type: none"> <li>• No stamp duty on legal instruments</li> <li>• Full VAT exemption (except on motor vehicles and petroleum fuels)</li> <li>• Exemption of Customs Duty on all inputs (except motor vehicles, motor vehicle spare parts and petroleum fuels)</li> </ul>
Accelerated depreciation	<ul style="list-style-type: none"> <li>• 100% depreciation in first year on investment in buildings, machinery and equipment</li> </ul>
Imports	<ul style="list-style-type: none"> <li>• Perpetual duty &amp; VAT exemption on all imports</li> </ul>
Sales to domestic market	<ul style="list-style-type: none"> <li>• EPZ firms can sell a maximum of 20% of their annual turnover to the domestic market</li> <li>• EPZ service enterprises can sell services to the domestic market with the approval of the Minister for Trade and Industry</li> <li>• No domestic sales for commercial enterprises</li> </ul>
Other	<ul style="list-style-type: none"> <li>• On-site customs inspection</li> <li>• Single license granted by EPZA, except for special permits related to certain sectors (e.g., pharmaceuticals) and to environment, health and public safety concerns</li> <li>• Maximum 30-day investment approval, one-stop shop facilitation</li> <li>• No exchange controls: liberal repatriation of dividends, profits &amp; capital</li> <li>• Serviced land &amp; buildings with full infrastructure (power, water, etc.)</li> </ul>

**Source:** Millennium Cities Initiative, based on information provided by the Export Processing Zones Authority.



There are no city-specific investment incentives available in Kisumu. However, investors in manufacturing and in hotel services anywhere *outside* Nairobi and Mombasa are eligible for an investment allowance of 85% on plant, machinery, buildings, and equipment. In addition, Kisumu is one of the seven designated locations in Kenya for the manufacturing-under-bond scheme, intended to encourage exports. Under this scheme, the investment allowance on plant, machinery, buildings, and equipment is 100% and investors are also exempted from customs duties and VAT on machinery, equipment and raw materials.

### Investment and tax treaties

Kenya's trade treaties have already been mentioned in Chapter I, under **Markets for investors**. The country has also signed a number of bilateral investment treaties and treaties for the avoidance of double taxation.<sup>24</sup> These are listed in Table II.4 below.

<sup>24</sup> On taxation, see Chapter III.



**Table II.4. Kenya's bilateral investment treaties (BITs) and double taxation treaties (DTTs), with signing dates where available**

BITs <sup>a</sup>		DTTs <sup>b</sup>	
China	16 July 2001	Canada	--
Germany	3 May 1996	Denmark	--
Italy	16 September 1996	Germany	--
Netherlands	11 September 1970	India	--
Switzerland	2006	Norway	--
United Kingdom	13 September 1999	Sweden	--
		United Kingdom	--
		Zambia	--

**Source:** UNCTAD, Country-specific lists of BITs, <http://www.unctad.org/Templates/Page.asp?intItemID=2344&lang=1>, and Kenya Investment Authority.

<sup>a</sup> Note that the BITs with China and the UK may not yet be in force.

<sup>b</sup> The eight countries listed here are the ones with which DTTs have so far been *concluded* by Kenya. Note, however, that some of these DTTs may be due for review and renegotiation. A number of other DTTs are currently in the *process* of negotiation. Finally, although Kenya, Tanzania and Uganda signed the East African double taxation treaty in 1997, only Kenya and Tanzania have thus far ratified the treaty. For further information on investment and tax treaties, readers should contact the Kenya Investment Authority (contact details in **Appendix**.)



## 4. The business environment

### Infrastructure

As noted earlier, Kisumu had emerged as a trade and transport hub in East Africa by the time Kenya became independent in 1963. Over the following four decades, conditions changed and, for both political and economic reasons, most infrastructure *within* the city and transport infrastructure *connecting* the city with other parts of Kenya and East Africa suffered badly. Some of these negative trends are now being slowly reversed.

Kisumu's infrastructure problems are complicated by the patterns of land use.<sup>25</sup> The central business district (CBD), the colonial as well as post-colonial heart of Kisumu's economy, has now become encircled by uncontrolled informal settlement neighbourhoods. Since the 70s, these neighbourhoods have been incorporated into the city but they remain for the most part without the kinds of services (water, power, waste collection) available in the CBD.

### Electricity

Electricity is provided by the Kenya Power and Light Company (KPLC). The relatively high installation and use charges mean that less than 25% of the city residents have access to electricity. In addition, there has been an increase in illegal 'subletting' or 'sub-distributing' off of KPLC power lines in the informal settlements, leading to fires and electrocutions and causing a huge financial strain on KPLC. Recently, KPLC has been working on a sub-contracting model that would allow local business leaders to monitor one connection and subcontract out the electricity at an affordable rate. Some NGOs and donors are also funding the installation of transformers in schools and public buildings, which would then make electricity much more accessible to nearby residents,

who can set up individual connections for only KSh 4,000 (approx. USD 60). Despite all this, power remains much too expensive for the majority of the city's residents.

### Water

Since the passage of the Water Act in 2002, water has been provided by the Kisumu Water and Sewerage Company (KIWASCO) and the numbers of those supplied has risen from 95,000 to 159,000. Revenue collection has also risen, from 67% to 95%, and water production has increased by nearly 6,000 m<sup>3</sup>/day. Some old pipes have been repaired and service has become more customer-friendly and efficient. Problems remain, however, with the supply of water at just over 30% of the total demand. Again, a sub-contracting initiative as in power is helping reduce cost and increase supply, as are the efforts of donors and NGOs.

### Air transport

Kenya Airways and East African Air have offered four or five daily flights from and to Nairobi for some time. There are now two additional carriers, Jet Link and 540, flying to Kisumu, bringing the total number of flights to between eight and ten a day. This added competition may bring fares down further and help increase tourist travel to the region. The Kenya Airports Authority (KAA) is also planning an upgrade of the Kisumu airport.<sup>26</sup> The first phase of the upgrade involves building a new passenger terminal, to be ready by mid-2009. This terminal will remain domestic for the moment. At the same time, the runway would be expanded from its existing dimensions of 2000 x 30 m to 3000 x 45 m, with a view to accommodating larger planes like the Boeing 737. The expansion is expected to cost USD 35 million and the funds have been budgeted. Also planned is a further expansion of the runway to accommodate still larger planes, like the Boeing 767.

<sup>25</sup> The discussion of infrastructure within Kisumu that follows draws upon a report on Kisumu's infrastructure submitted to the Millennium Cities Initiative in 2007 – see Sweeney, 2007.

<sup>26</sup> What follows is based on interviews with David Matole, Manager of Planning, Research & Budgeting at the KAA, carried out by Ashley Hufft, the MCI representative in Kenya, in April and June 2007.

There are no plans at present to expand to cover long-haul passenger flights from, say, Europe, as it is unclear that there is enough demand to justify such an expansion. New regional routes to Entebbe, Arusha, Mwanza and Juba are more likely but there are no firm plans for such flights yet. International cargo flights are a stronger prospect, although, until the runway can accommodate 767s, cargo will only be flown to *regional* destinations. Once the new terminal is operational, the KAA intends to convert the existing terminal into a cargo terminal with refrigeration facilities – which would be of interest to exporters in the fish-processing industry as well as to those in horticulture.

### Railways

Kenya Railways once offered twice-a-day passenger service to Nairobi (*via* Nakuru) and daily passenger service to Butere. The collapse of the first East African Community in 1977<sup>27</sup> led to a collapse of regional trade and a severing of the transport links that both supported trade and profited from it. At the same time, road traffic increased and so did air traffic, leading to further neglect of the rail links. As things stand, investors complain of long delays in the freight service from Nakuru to Kisumu, although the new rail operator (see below) denies this.<sup>28</sup>

Privatization of the railways in East Africa had been on the agenda for some time and the first plan was for Kenya, Tanzania and Uganda to do it jointly. That was dropped when Tanzania decided against it in 2003.<sup>29</sup> Kenya and Uganda went ahead with a joint concessioning and Rift Valley Railways (RVR) of South Africa now operates Kenya Railways under a management contract. The contract requires RVR Kenya to run the rail network and maintain the infrastructure as well as the rolling stock for a period of 25 years, after which the railway either reverts back to the government or is conceded again to another independent party.

According to RVR, there are plans by the Kenyan government to expand the rail network into Juba in southern Sudan. Also anticipated is the upgrading of the rail line from Molo to Kisumu (again by the government) from the current 60-pound gauge to 90-pound gauge in order to accommodate heavier locomotives that can haul more load per trip. As for RVR itself, it is currently refurbishing passenger coaches in order to attract more customers to this service.

### Water transport

Kisumu once offered Uganda and parts of Tanzania the main connection to the port of Mombasa and it did so by means of the steamers that connected the inland ports on Lake Victoria. This lasted until the 70s, with the first EAC operating several steamers that linked Kisumu with Port Bell, Jinja and Mwanza.<sup>30</sup> This small fleet of steamers has since disappeared. At the moment, only the Government of Tanzania operates a ferry (MV Umoja), with a cargo capacity of 1,200 tonnes, which links the three countries. Its Kenyan and Ugandan counterparts, which have the same capacity, are currently docked. There are also private cargo carriers, such as those operated by MOIL, a Tanzanian company. Kisumu Port is managed by Kenya Railways (not by RVR) and is apparently in poor condition. Given the progressive integration of the EAC, it is difficult to envision a future for Kisumu that does not include a revitalization of lake transport, at least of cargo transport.

### Roads

Investors in Kenya have for some time held the poor condition of the road network to be the principal obstacle to further investment.<sup>31</sup> The road from Kisumu to Nairobi, especially the part closest to Kisumu, is a case in point. In a way, the present condition of the roads is a consequence of earlier improvements. As road links increased and improved in the 50s and 60s, traffic

<sup>27</sup> The present (second) EAC dates from 2000.

<sup>28</sup> Information attributed to Rift Valley Railways in this section is derived from conversations and correspondence with Christine Tatua of RVR in Kisumu.

<sup>29</sup> For more on railways in East Africa, see UNCTAD's 2005 guide to the EAC.

<sup>30</sup> The first two in Uganda and the third in Tanzania.

<sup>31</sup> See the chapter on investor perceptions in UNCTAD's 2005 Kenya guide and Section IV.1 below.



switched from the railways. Unfortunately, the roads were not built to carry the loads they have since carried and the economic difficulties of the 80s and 90s meant that there was little maintenance or new construction.

The Ministry of Transport, in cooperation with the Ministry of Roads and Public Works, is just beginning construction on a bypass express route around Kisumu. Trucks, buses and cars headed for somewhere other than Kisumu would no longer need to drive through the central business district. This will reduce congestion in the CBD and protect municipal roads from heavy traffic. It will also protect parts of the main roads closest to the city. The project is part of the Northern Corridor Infrastructure Project and is meant to protect and enhance the major roadways through northwestern Kenya.

A recent World Bank report<sup>32</sup> commented on logistics in Kenya. After noting that Kenya's logistical performance was viewed negatively by international logistics operators,<sup>33</sup> it mentioned a number of recent improvements. These included improvement of road infrastructure backed by a consistent maintenance policy; customs reform and modernization; the concessioning of the railway; and a modernization programme for the port at Mombasa. It also observed that the reform programme was being pushed by a proactive private sector and considerable donor support. In a box on 'Issues in Trade Logistics in Kisumu and Nyandarua', the report noted that among "the problems along the supply chain that limit farmers' market power or their ability to access export markets are a lack of cold-storage facilities for horticulture and milk products."

### Telecommunications

This was one area of infrastructure in Kenya in which the investors consulted by UNCTAD agreed there had been progress.<sup>34</sup>

Fixed-line telecommunication has traditionally been a monopoly of Telkom Kenya, which has been on the privatization list for some time. An IPO is now expected by December 2007. But the improvements in telecoms have more to do with mobile telephony. As Table II.5 shows, Kenya is far ahead of its EAC partners in mobile tele-density – and in Internet use.

### The financial sector

There were 45 financial institutions in Kenya in 2007.<sup>35</sup> The leading foreign banks were Barclays, Citibank, Stanbic and Standard Chartered; the leading domestic bank was Kenya Commercial. Non-performing loans, which had accounted for 30% of all loans in 2002, had fallen to a little over 20% by 2007. The spread between average lending rates (a little under 14%) and average deposit rates (a little over 4%) remains large and credit remains difficult to access for SMEs.

In the insurance field, there were some 40 registered companies. The penetration ratio of life insurance (premiums as a percentage of GDP) is very low at less than 1%. The industry is mostly focussed on non-life insurance. On trade and investment insurance, see Box II.6 on ATI below.

### Human resources

Kenya has one of the best educated workforces in sub-Saharan Africa. As Table II.6 shows clearly, its adult literacy rate is the highest in the neighbourhood and its secondary school enrolment figures strikingly higher than those of its EAC partner states. Perhaps more important than any data on formal qualifications is the assessment of investors. UNCTAD's discussions with investors in 2005 revealed that foreign investors in particular held the Kenyan workforce in high regard, seeing it as able, enterprising and motivated.<sup>36</sup> Lastly, it is also an English-speaking workforce.

<sup>32</sup> Kenya: *Unleashing the Potential for Trade and Growth*, February 2007.

<sup>33</sup> The report cited the Logistics Perception Index compiled by the Turku School of Economics and Business Administration in Finland in 2004.

<sup>34</sup> See chapter on private-sector perceptions in *An Investment Guide to Kenya*.

<sup>35</sup> Central Bank of Kenya, *Monthly Economic Review*, April 2007.

<sup>36</sup> *An Investment Guide to Kenya*, 2005

**Table II.5. Telecommunications in East Africa, 2005**

Country	Fixed telephone subscribers	Mobile cellular subscribers		Internet indicators	
	Telephone lines per 100 people	Per 100 inhabitants	As % of total telephone subscribers	Internet users per 100 inhabitants	PCs per 100 inhabitants
Burundi	0.39	2.03	78.4	0.53	0.48
Kenya	0.82	13.46	94.2	3.24	0.95
Rwanda	0.27	3.21	85.8	0.55	--
Tanzania	0.40	8.84	95.6	0.89	0.74
Uganda	0.30	4.56	93.8	1.74	1.04

Source: Adapted from the International Telecommunication Union, <http://www.itu.int/ITU-/ict/e/Indicators/Indicators.aspx#>, 2007.

#### Box II.6. The African Trade Insurance Agency (ATI)

The African Trade Insurance Agency is a multilateral institution established by African countries in 2001. Its mission is to secure trade and investment in Africa; its vision to transform Africa into a prime trade and investment destination. Through its various products, the Agency increases the financial resources available for trade and investment in Africa and reduces the cost of doing business on the continent by lowering the associated risks.

ATI's foreign direct investment (FDI) insurance covers the investor (or financier) against the loss of equity in a project due to confiscation or broad political risk. The risks covered include the following:

- inability to convert local currency into, or transfer, hard currency
- confiscation, expropriation or nationalization
- breach of concession rights
- forced abandonment or divestiture
- political violence

Any eligible cross-border investment in one of ATI's member states may be protected through FDI insurance against some or all of these risks. Other forms of insurance offered by ATI include short, medium and long term non-payment cover by sovereign, sub-sovereign and commercial obligors. For further information, investors should contact the CEO, Peter Jones (contact details in **Appendix**). Unlike the other well-known multilateral investment insurer, MIGA (a member of the World Bank Group), ATI covers commercial as well as political risk, has no minimum cover period, and can provide cover for stand-alone third-party loans.

Membership in ATI is open to all states, export credit agencies, international financial institutions, regional economic organizations and private corporations.\* ATI's partners in risk syndication are leading players with global operations and include Lloyd's of London Syndicates, MIGA, the Atradius Group, OPIC, EDC, EFIC, AIG, Sovereign Risk, OND Ducreire, and the Zurich Financial Services Group.

Source: Millennium Cities Initiative, drawing on information provided by ATI.

\* ATI members in mid-2007 were: Burundi, DRC, Djibouti, Eritrea, Kenya, Liberia, Madagascar, Malawi, Rwanda, Sudan, Tanzania, Uganda, Zambia, Atradius Group, COMESA, PTA Bank and PTA Reinsurance Company.

The legislation relevant to hiring workers in Kenya is the Employment Act (revised 1984) and the Regulation of Wages and Conditions of Employment Act (revised 1980).<sup>37</sup> Industrial relations in Kenya are on the whole harmonious. EPZ workers may now form unions. Strikes are relatively uncommon. Wages are low, although, adjusted for productivity, labour costs in Africa tend to be higher than in Asia. Tables II.7 and II.8 below indicate the minimum wages payable in agricultural and urban environments respectively.<sup>38</sup>

With regard to the hiring of expatriates, the 2004 Investment Promotion Act provides for three work permits for the employees of a foreign investor holding an investment certificate issued by the Kenya Investment Authority, as well as three additional permits for the investor's partners (shareholders).<sup>39</sup> Beyond this, any investor, whether foreign or domestic, may hire foreign workers after demonstrating that qualified Kenyans are not available to fill given positions. Such a demonstration can be expensive and time-consuming.

<sup>37</sup> Although it is formal employment that most concerns foreign investors, it is worth noting that labour laws have little to do with informal employment, which accounts for a third of the economy.

<sup>38</sup> Note that the urban wage table specifically includes Kisumu.

<sup>39</sup> See further discussion of the Act in Chapter III below.

HIV/AIDS has been a major health issue in much of Africa. It is thus encouraging to note that the East African region was singled out by UNAIDS as a harbinger of hope (Box II.7 below).

**Table II.6. Literacy and education in East Africa**

Country	Literacy rate		School enrolment	
	ADULT TOTAL	YOUTH TOTAL	SECONDARY	TERTIARY
	% of age 15+	% of age 15-24	% gross	% gross
Burundi	59	73	13	2
Kenya	74	80	49	3 <sup>a</sup>
Rwanda	65	78	14	3
Tanzania	69	78	--	--
Uganda	67	77	16	3 <sup>a</sup>
	2006		2005	

**Source:** Adapted from the World Bank, World Development Indicators, 2007. <sup>a</sup>Figure for 2004.

**Box II.7. HIV/AIDS in Kenya**

According to UNAIDS, a decline in adult HIV prevalence is under way in three sub-Saharan African countries: Kenya, Uganda and Zimbabwe. It sees East Africa as providing the most hopeful indications that serious AIDS epidemics can be reversed. The countrywide drop in HIV prevalence among pregnant women seen in Uganda since the mid-1990s is, according to UNAIDS, now being mirrored in the urban parts of Kenya, where infection levels are dropping, in some places quite steeply. HIV prevalence in Kisumu has been fluctuating, with the highest prevalence measured in 2000 (35.0%). According to the population-based study in Kisumu in 1997-1998, young women were more likely to be infected than men of the same age. Among women aged 15-19 years, HIV prevalence was 23.0%, compared to 3.5% among men of the same age. The current prevalence rate is around 11%.<sup>a</sup>

**Source:** <http://www.unaids.org/en/Regions-Countries/Regions/SubSaharanAfrica.asp> and <http://www.unaids.org/en/Regions-Countries/Countries/kenya.asp>.

<sup>a</sup> According to Simon Ochieng, District Development Officer, at a workshop held in connection with this guide in Kisumu in June 2007.

**TABLE II.7. Minimum wages in agriculture<sup>a</sup> in USD<sup>b</sup>**

Unskilled & semi-skilled employees		Monthly <sup>c</sup>	Daily
<b>1</b>	Unskilled employees	37	1.57
<b>2</b>	Stockman, herdsman, watchman	43	1.82
<b>3</b>	House servant or cook	43	1.62
<b>4</b>	Farm foreman	67	2.84
<b>5</b>	Farm clerk	67	2.84
<b>6</b>	Section foreman	44	2.84
<b>7</b>	Farm artisan	44	1.89
<b>8</b>	Tractor driver	45	2.0
<b>9</b>	Combine harvester driver	52	2.21
<b>10</b>	Lorry driver or car driver	55	2.32

**TABLE II.8. Minimum wages in Nairobi, Mombasa and Kisumu<sup>a</sup> in USD<sup>b</sup>**

Occupation			
<b>1</b>	General labourer, including cleaner, sweeper, gardener, children's ayah, house servant, day watchman, messenger	76.40	3.68
<b>2</b>	Miner, stone cutter, turn boy, waiter, cook, logger line cutter	82.51	3.97
<b>3</b>	Night watchman	85.24	4.09
<b>4</b>	Machine attendant, sawmill sawyer, machinist's assistant, mass production machinist, shoe cutter, bakery worker, bakery assistant, tailor's assistant	86.59	4.16
<b>5</b>	Machinist, vehicle service worker (petrol and service stations), bakery plant hand, laundry operator, junior clerk, wheeled tractor driver (light)	98.84	4.76
<b>6</b>	Printing machine operator, shop assistant, machine tool operator, table hand baker or confectioner, typist, driver (car and light vans)	103.12	4.96
<b>7</b>	Pattern designer (draughtsman), garment and dress cutter, general clerk, telephone operator, receptionist, storekeeper	117.68	5.66
<b>8</b>	Tailor, driver (medium-sized vehicle)	129.68	6.24
<b>9</b>	Dyer, crawler tractor driver, salesman	143.16	6.87
<b>10</b>	Caretaker (buildings)	158.44	7.63
<b>11</b>	Cashier, driver (heavy commercial Vehicle)	172.40	8.30
<b>12</b>	Ungraded artisan	103.12	4.96
	Artisan Grade "C"	129.68	6.24
	Artisan Grade "B"	143.16	6.87
	Artisan Grade "A"	172.40	8.30

**Source:** EPZA, drawing on Agricultural sector wage order, Ministry of Labour, May 2006.

<sup>a</sup>These are *minimum* wages. Employers are generally expected to pay above these amounts.

<sup>b</sup>These amounts in US dollars were calculated on the basis of an exchange rate of USD 1 = KSh 68. The rate commonly used in mid-2007 was USD 1 = KSh 65.

<sup>c</sup>Monthly wages here do not include a housing allowance of 15%, which may need to be paid if the employer does not provide housing. Housing and transport allowances can add up to 25% to wages.

## The private sector in Kenya and in Kisumu

Kenya has a large and fairly diverse private sector. There is a very substantial representation of foreign multinationals<sup>40</sup> in the country and there is also a significant domestic private sector, much larger than elsewhere in East Africa. Foreign investment has played a major role in developing Kenya's overseas exports such as tea, horticulture and garments. It is also prominent in tourism. The domestic private sector is concentrated in certain kinds of manufacturing, for example, steel and food-processing, for both the domestic and the regional markets. The domestic private sector is quite substantial in Kisumu as well. Around 30 companies participated in a workshop held in connection with this guide in Kisumu in June 2007, most of them domestic. (See Chapter IV, section 1, below.)

The key private-sector organizations in Kenya include the Eastern Africa Association (an association of foreign

investors in the region), the Kenya Association of Manufacturers (KAM), the Federation of Kenya Employers (FKE), the Kenya Private Sector Alliance (KEPSA) and the East African Business Council (EABC). The National Economic and Social Council (NESCC) is a body set up expressly to provide advice to the government on policy and to improve coordination between the public and private sectors.<sup>41</sup>

## Doing business in Kenya

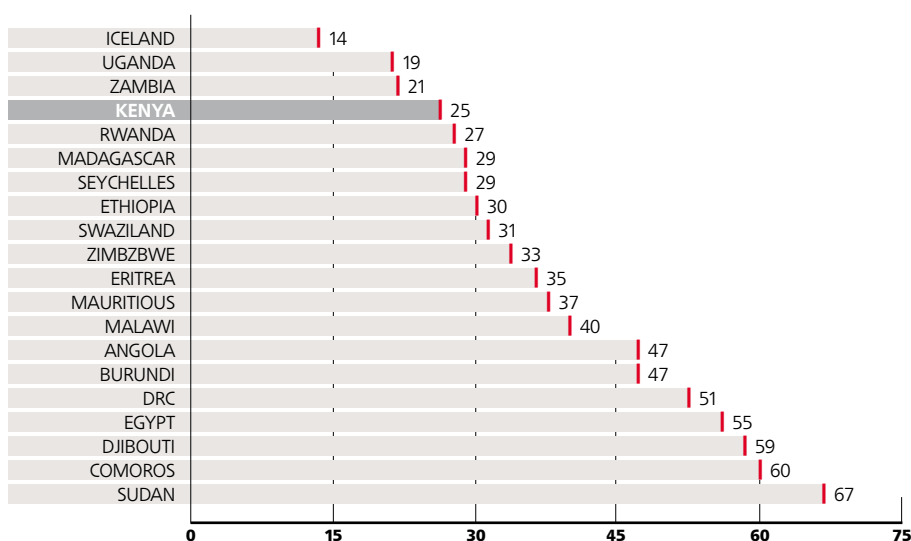
The International Finance Corporation (IFC), the private-sector arm of the World Bank, regularly carries out surveys of the investment climate in most countries of the world, investigating regulations that enhance business activity and those that constrain it. They deal with such topics as starting a business, dealing with licenses, employing workers and registering property. All charts presented below are selected from a recent report by the World Bank and the IFC benchmarking the performance of COMESA members.<sup>42</sup>

<sup>40</sup> For a small sampling, see Chapter IV below.

<sup>41</sup> For more about these organizations, see UNCTAD's 2005 guide to Kenya. For contact details, see Appendix.

<sup>42</sup> *Doing Business 2007: Common Market for Eastern and Southern Africa (COMESA)*, 2006.

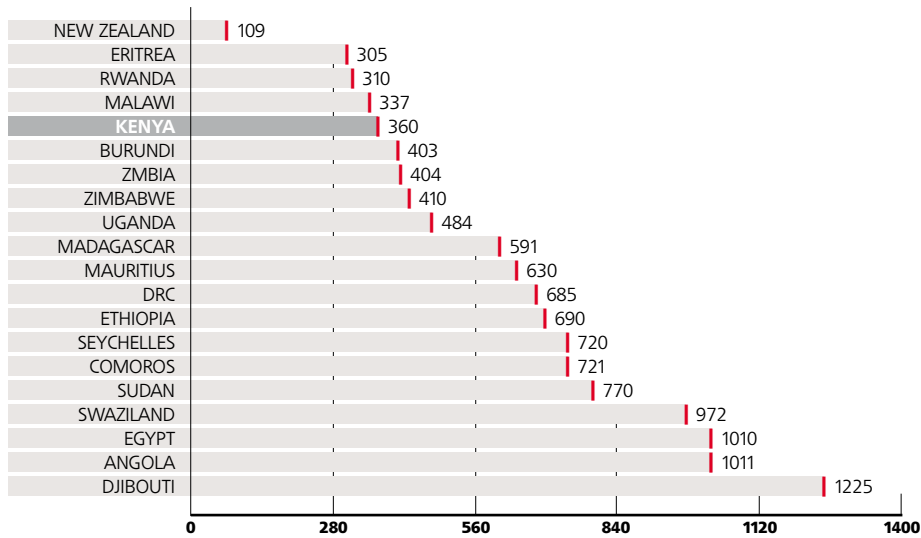
**Table II.4. Procedures to enforce a contract (number)**



<sup>43</sup> Libya does not appear in the charts as it became a full member of COMESA only in June 2006, while the data are as of April 2006.

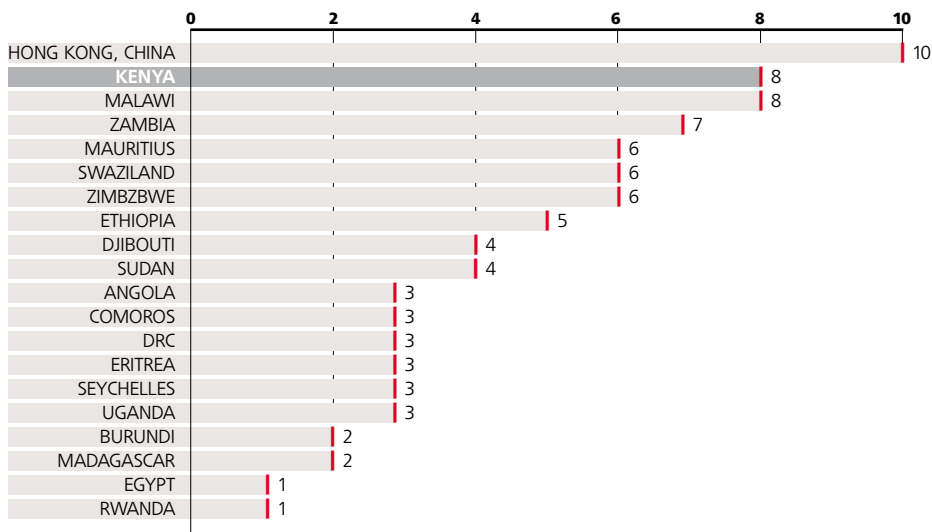
**Note:** Iceland is the global best, with the fewest procedures. Kenya does better than all but two of its 18 fellow members.<sup>43</sup>

**Table II.5. Time to enforce a contract (days)**



**Note:** New Zealand is the global best, with the least time taken to enforce a contract. Kenya's 360 days still put it better than 15 of the other 18 COMESA members.

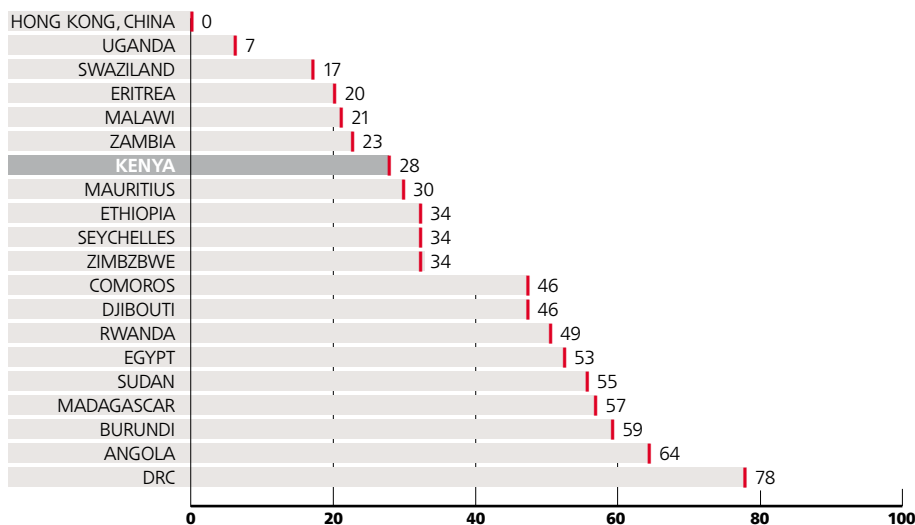
**Table II.6. Legal rights index**



**Note:** Hong Kong is the global best, with the strongest legal rights provided by collateral and bankruptcy laws. Kenya and Malawi lead the COMESA group. (One should note, however, that having the right legislation in place is not enough to ensure that it is effective in practice. In fact, as far as bankruptcy goes, the same study shows Kenya to be slow and expensive.)

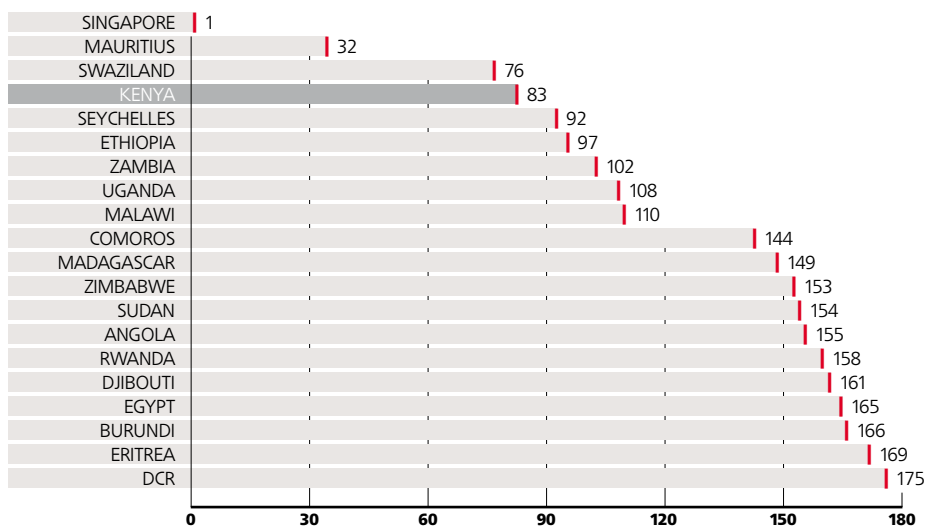


**Table II.7. Rigidity of employment index (90-100)**



**Note:** Hong Kong is again the global best and offers the greatest flexibility in hiring and firing workers and in setting working hours. Kenya is fairly flexible, though not anywhere near as flexible as its EAC partner Uganda.

**Table II.8. Ease of doing business: Aggregate rankings**



**Note:** These are the aggregate rankings that average economy rankings across the 10 topics covered in *Doing Business 2007*. The total number of countries covered is 175. Singapore offers the best environment in the world for doing business. Kenya does better than 92 other countries in the world and better than all but two of its fellow COMESA members. It also does best out of the EAC states – the others being Burundi, Rwanda and Uganda. The remaining EAC member, Tanzania, is not included in the rankings here because it is not a member of COMESA. However, on the aggregate rankings available on the World Bank/IFC Doing Business website,<sup>44</sup> Tanzania ranks 142<sup>nd</sup>.

<sup>44</sup> World Bank and IFC, <http://www.doingbusiness.org/Downloads/>.

**5. Kisumu as an investment location: A summary for investors**

Strengths	Opportunities
<ul style="list-style-type: none"> <li>• Political stability in Kenya</li> <li>• Significant domestic private sector and well-regarded workforce</li> <li>• Strategic location in East Africa</li> <li>• Substantial natural resources in Lake Victoria and the surrounding area</li> </ul>	<ul style="list-style-type: none"> <li>• Sugar and ethanol</li> <li>• Aquaculture</li> <li>• Agricultural products for domestic and foreign markets: groundnuts, rice, fruits and vegetables</li> <li>• Tourism, especially regional and conference tourism, and other services such as water transport and construction</li> <li>• Light manufacturing, especially food-processing, for domestic and regional markets</li> </ul>
Weaknesses	Threats
<ul style="list-style-type: none"> <li>• Poor infrastructure: power, ports, roads, railways, water transport</li> <li>• High transaction costs owing to regulatory and governance problems</li> </ul>	<ul style="list-style-type: none"> <li>• HIV/AIDS prevalence (although declining) in the working-age population</li> </ul>





Our farming and aquaculture venture in Kenya over the past five years has been very challenging but also very satisfying. Doing business in Kenya is not easy but a mix of determination, the right attitude and persistence can overcome most challenges. Although we have only begun our operations, the positive changes in the lives of people on and around the farm have already been meaningful.

Calvin Burgess, CEO, Dominion Farms



## iii. taxes and laws

### 1. Taxation in Kenya

By the standards of many developing countries, especially in sub-Saharan Africa, the Government of Kenya has a high tax yield. According to the Central Bank's most recent figures, tax revenue over the first eight months of fiscal 2007 was nearly KSh 190 billion, i.e., nearly 85% of the total government revenue of nearly KSh 225 billion over the same period<sup>45</sup> or a bit over 20% of the most recent (proportionally adjusted) GDP estimate of KSh 943 billion.<sup>46</sup> By far the largest portion of the tax revenue of KSh 190 billion was income tax (KSh 76 billion), followed by the value-added tax (KSh 60 billion), excise tax (KSh 35 billion) and import duties (KSh 18 billion).

The principal taxes are the ones just mentioned. The income tax splits into the corporate tax on profits and the personal income tax.

#### Corporate tax

The Kenya Revenue authority administers the tax system, on the basis of the Income Tax Act of 1989. Broadly speaking, corporate taxes in Kenya are in line with those in other countries in the region, with one exception: only Kenya has a corporate tax rate for non-resident companies that is 25% higher than resident ones. For Kenyan corporate taxes, see Table III.2 below, which includes VAT; for taxes in the EAC more broadly, see UNCTAD's 2006 guide to Rwanda.

#### Personal income tax

The personal income tax is paid by all Kenyan residents, including foreign workers if they have a permanent home in Kenya or spend more than 183 days working in the country.

#### Excise tax

This is levied on alcohol, tobacco, soft drinks, perfumes, cars and a few other products, whether imported or domestically produced. The rates vary. Excise taxes on tobacco and alcohol were raised in the budget presented on 14 June 2007.

#### Import duties

With progressive trade liberalization, the contribution of import duties to the country's tax revenue has been declining. As indicated above, it currently stands at less than 10%. The coming into force of the EAC's Customs Union Protocol in 2005 has meant that the highest permissible duties on imports from outside the EAC must now be in conformity with the Community's Common External Tariff (CET), which is set at 0% for raw materials and capital goods, 10% for intermediate goods, and 25% for finished goods.<sup>47</sup>

#### Other

For Kenya's double taxation treaties, see Table II.4 in Chapter II above. There have long been complaints by investors about delays in VAT refunds. The budget presented on 14 June 2007 may offer some relief.<sup>48</sup>

<sup>45</sup> Monthly Economic Review, April 2007.

<sup>46</sup> National Bureau of Statistics, Kenya: Facts and figures, 2006 edition.

<sup>47</sup> But see fn. 5 above on the exceptions for 'sensitive goods'.

<sup>48</sup> See KPMG, Budget Brief – Kenya 07.

**Table III.1. Personal income tax**

	Tax bands (KSH P.A.)	Rate (PER CENT)
First*	121,968	10
Next	114,912	15
Next	114,912	20
Next	114, 912	25
Over	466,704	30

Source: KPMG, Tax Data Card, East Africa, 2006.

\*Personal exemption of KSh 13,944 p.a.

## 2. Legal framework for investment

### Investment law

The Investment Promotion Act of 2004, as amended in 2006, provides the legal framework for FDI in Kenya.<sup>49</sup> Some key features of the Act are as follows:

- The Act created the Kenya Investment Authority (KIA), with the mandate to promote and facilitate investment. The KIA replaced the earlier Investment Promotion Centre (IPC). Its functions include advising the Government on improving the investment environment and it is assisted in this function by having a governing body that includes prominent members of the business community, along with government officials. The board appoints the chief executive officer, the Managing Director, of the KIA, currently Susan Kikwai.<sup>50</sup>
- The KIA is authorized to issue investment certificates to qualifying foreign and domestic investors. Initially, these certificates were mandatory for foreign investors and the minimum capital requirement to be eligible for a certificate was set at USD 500,000. In 2006, the Act was amended to make the certificate optional and the minimum capital requirement was reduced to USD 100,000. This change brings FDI requirements in Kenya more in line with those of its neighbours (see Table III.3 below). For domestic investors, the minimum requirement is KSh 1,000,000 or about USD 15,000.
- Among the benefits of acquiring an investment certificate is the automatic entitlement to two-year work permits for three employees and three partners or shareholders.<sup>51</sup> Another benefit is that it entitles the certificate holder to what is in effect a temporary waiver of the licensing requirement, as long as the licenses required are spelt out in

the certificate. At first glance at least, this seems like a major benefit, given the cumbersome nature of Kenya's licensing system.<sup>52</sup>

- The Act directs the KIA to handle requests for certificates with speed – within 25 days, barring special circumstances. If the matter is not resolved quickly, the investor may ask the Minister of Trade and Industry to intervene. The Minister in turn has 15 days in which to communicate his/her decision.

### Incorporation and exit

There are various ways to set up a business in Kenya. They include limited liability companies, a form chosen by most foreign investors who choose to incorporate locally, sole proprietorships, partnerships, and representative offices. Figure III.1 below provides an outline of the steps, time and costs involved in getting an FDI project under way in Kenya as a limited liability company. Exit is straightforward unless it involves bankruptcy. In that case, the procedure is costly and prolonged.<sup>53</sup>

### Priorities and restrictions

The government welcomes FDI in all areas but welcomes it especially in the following:

- Agriculture and agro-processing industries;
- Export-oriented industries including AGOA-oriented ones;
- Physical infrastructure, energy, and information and communication technology;
- Plastics and pharmaceuticals;
- Textiles and apparel; and
- Tourism and related industries.

There has been a shift in priorities with the adoption by the government of its Vision 2030.

<sup>49</sup> For a list of all major laws with a bearing on FDI in Kenya, see Appendix 6 in UNCTAD's 2005 Kenya guide.

<sup>50</sup> For contact details, see Appendix.

<sup>51</sup> Investors seem to feel that this is not working as it should be, that immigration hassles remain and that fees for these permits are high (about USD 1,500 for the shareholder/partner permits and about USD 3,000 for the employee ones).

<sup>52</sup> The number of licenses is in fact being reduced. The KIA reports that, of the 315 licenses slated for elimination, 110 have already been eliminated. In addition, a further 379 are set for 'simplification'.

<sup>53</sup> World Bank and IFC, Doing Business 2007, <http://www.doingbusiness.org/Downloads/>.

**Table III.2. Corporate taxes in Kenya**

<b>Corporate tax rates</b>	<b>in %</b>	
Resident companies	30 <sup>a</sup>	
Non-resident companies/branches	37.5	
<b>Withholding tax rates<sup>b</sup></b>	<b>Resident</b>	<b>Non-resident</b>
Dividends	5	10
Management, technical or professional fees	-	20
Royalties	5	20
Interest:		
• <i>Housing bonds</i>	10	10
• <i>Bearer instrument</i>	25	25
• <i>Others</i>	15	15
Mining companies:		
• <i>Management or technical fees</i>	-	20
• <i>Dividends</i>	-	10
<b>Value-added tax</b>		
Registration threshold (annual)	KShs 3 000 000	
<b>Rates</b>	<b>in %</b>	
• Standard	16	
• Hotel and restaurant services	14	
Penalties (monthly)	2 <sup>c</sup>	
<b>Capital deductions</b>	<b>in %</b>	
Investment deduction		
• <i>Plant/machinery</i>	100	
• <i>Buildings</i>	100	
Industrial building allowance		
• <i>Manufacturing</i>	2.5	
• <i>Hotels</i>	4	
Farmworks allowance <sup>d</sup>	33.33	

**Source:** KPMG, Tax Data Card, East Africa, 2006.

<sup>a</sup> A resident company is one incorporated in Kenya. There are further reductions for companies newly listed on the Nairobi Stock Exchange. There are also tax holidays for companies in EPZs, on which see Incentives, EPZs and related matters in Chapter II.

<sup>b</sup> This table shows only the most common withholding taxes.

<sup>c</sup> 2% per month for late payment and KShs 10,000 or 5% of tax due, whichever is higher, for late returns.

<sup>d</sup> Structures necessary for the proper operation of the farm.





**Table III.3. FDI in East Africa: Entry requirements and restrictions**

	Kenya	Tanzania	Uganda
<b>Entry requirements</b>			
<b>Minimum capital</b>	USD 100,000 for an investment certificate, which is optional.	USD 300,000 to be eligible for a certificate, which is optional.	USD 100,000 for an investment licence, which is optional. There is a new code pending, which reduces the requirement to USD 25,000.
<b>Restrictions on sectors</b>			
<b>Prohibited sectors</b>	Narcotic drugs and psychotropic substances.	Narcotic drugs. Arms and ammunition.	Activities related to national security.
<b>Restricted sectors</b>	Firearms and explosives require special licences.	Sawn timber, veneer, plywood, wood-based products, and utility logs as raw materials are subject to approval from the Ministry of Tourism and Natural Resources.	Activities requiring the ownership of land. (Investors can lease for up to 99 years or participate in joint ventures involving the leasing of land.)
<b>Restrictions on equity</b>			
	Companies listed on the NSE (75%).	Companies listed on the DSE (45%).	None.
	Fishing activities (49%)		
	Insurance (66.7%).		
	Telecommunication (70%)		

**Source:** Adapted with revisions from UNCTAD's 2005 guide to the EAC.

The revised priorities are *agriculture and agro-industries* (with an emphasis on, among other things, reducing the cost of key inputs and expanding primary processing, value addition and branding); *wholesale and retail services* (with an emphasis on, among other things, increasing supermarket share of retail trade from 5 to 10 per cent by 2012 and mobilizing investment to formalize wholesaling through public-private partnerships); *financial services* (with an emphasis on, among other things, introducing more financial products to deepen the financial services outreach and making Nairobi a regional hub for financial services); and *business-process outsourcing* (with an emphasis on, among other things, creating an enabling environment, including BPO policy incentives).

The prohibitions and restrictions are those mentioned in Table III.3 above.

### **Investment protection, investor treatment and dispute settlement**

The Constitution provides a guarantee against expropriation without due process in Section 75. Additional protection is usually available to investors from countries with which Kenya has signed a bilateral investment treaty – see Table II.4. in Chapter II above.

Kenya does not discriminate in principle against foreign investors.

Dispute settlement through arbitration is now encouraged as a matter of policy. Those who choose arbitration are required to make an arbitration agreement and the authority of an arbitrator selected under such an agreement cannot be gainsaid, unless otherwise decided by the High Court. Foreign judgements are enforced by Kenyan courts on a reciprocal basis. Kenya is also a member of the International Centre for the Settlement of Investment Disputes (ICSID), a body

associated with the World Bank that deals with disputes between states and nationals of other states.

### **Land**

In Kenya, there is private land, community land and public land. One may hold land on a freehold basis, i.e., in perpetuity, or may lease it on agreed terms. One may also acquire land through a government allocation.

Land can be a difficult issue in Kenya. On the one hand, the private ownership of land is not prohibited, as it is in some African countries. Nor are foreigners forbidden to own land, unless it is agricultural. And even this restriction may be removed by a presidential waiver. On the other hand, it is unclear how one qualifies for such a waiver. A second issue has to do with titles, which are not always clear. So a foreign investor may acquire land by lease and then the lease may be disputed on the grounds that the lessor had no right to lease it.

Investors in Kisumu believe that local authorities can and should do more to facilitate the provision of land for investment purposes. As things stand, land is hard to come by, in part because some of it is held for speculative reasons. One possible solution might be for the local authorities to set up an industrial estate, perhaps with an EPZ attached to it, which investors could then access on terms similar to those used in EPZs in other parts of Kenya.

As a practical matter, investors are advised not to engage in dealings in land without competent legal assistance.

### **Foreign exchange**

Kenya has a liberal foreign exchange policy and there are no controls over the repatriation of capital, profits or dividends, although a withholding tax may apply.

**FIGURE III. 1. Getting an FDI project started in Kenya: Steps, time & cost**

Steps	Time	Cost to complete
Obtain approval for the company name from the Registrar of Companies.	2 days	USD 1.50 per name reservation
Obtain stamp on the Memorandum and Articles of Association and a Statement of the Nominal Capital at the Lands Office.	7 days	1% of nominal capital + USD 26.50 stamp duty on Memorandum and Articles of Association.
File Declaration of Compliance with the Registrar of Companies as required under the Companies Act.	1 day	USD 3
File deed and details with the Registrar of Companies at the Attorney General's Chambers.	7 days	USD 3
Register with the Tax Department for a Personal Identification Number (PIN).	1 day	no charge
Register with the VAT office.	1 day	no charge
Apply for a business permit at the Nairobi City Council.	1 day	USD 3
Register with the National Social Security Fund (NSSF).	less than 1 hour	no charge
Register with the National Hospital Insurance Fund (NHIF) .	less than 1 hour	no charge
Register for PAYE at the Kenya Revenue Authority.	1 day	no charge
Buy a company seal from the relevant business dealers after a certificate of incorporation has been issued by the Registrar of Companies .	2 days	USD 33

**Source:** Business Licensing and Regulatory Reforms Unit, Treasury, Ministry of Finance.

**Note:** Several of these steps are being streamlined further by consolidation.

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## iv. investors & investment climate

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### 1. Investor assessment of the investment climate

This is a summary of investor opinions of Kisumu as an investment location. It is based mainly on a closed session with the business community held as part of a workshop in Kisumu on 19 June 2007. Some thirty companies, most of them domestic but some either fully or partially foreign-owned, participated in the workshop. In addition, consultations were also carried out with a number of individual investors. What follows should be taken as no more than broadly indicative of investor opinion in Kisumu.

#### Attractions and drawbacks

Investors were asked what they saw as Kisumu's most appealing features as a place to do business in. The clear favourite was *location*. The city lies on the eastern shore of Lake Victoria with a market of some 30 million consumers around it in the catchment area. Although the current transport links with this market are not all that they should be, the potential access to a significant part of the East African market certainly exists. Two features of roughly equal attractiveness that came next were *security* and *natural resources*. *Insecurity* is an issue that weighs much on the minds of investors elsewhere in Kenya. In clear contrast, Kisumu is seen as a safe place to live and work. As for natural resources, there is the great if currently somewhat compromised resource represented by Lake Victoria, both for fishery and for water transport. And there are propitious conditions (soil, sun and water) for a variety of agricultural crops: rice, cotton, sugarcane, groundnuts, fruits and vegetables. Other features mentioned as being of some interest to investors were the climate, which is humid but not unduly so, low start-up costs, and the fact that Kisumu is relatively unsaturated as an investment location.

When it came to the major drawbacks of the area, there appeared again to be a consensus – infrastructure and *roads in particular* ranked at the very top. There are infrastructure issues *within* the city but these seem to matter much less to investors than the difficulties of connecting with their markets. The road to Nairobi is in an especially poor condition. Not only does this increase costs, it creates delays that can be damaging for investors dealing in perishable goods, e.g., fresh fruit or fish. It may also contribute to other hazards. A number of investors mentioned the problem of delivery trucks being hijacked on the way to Nairobi (or thence to Mombasa), although there was some disagreement as to how serious the problem was.<sup>54</sup> In any case, the problem is aggravated by the condition of the roads, which leads to more frequent breakdowns for trucks and thus makes them more vulnerable to hijackings. Other areas of concern included problems affecting the lake, in particular the growth of water hyacinth, and the lack of cargo facilities at the airport.

#### The role of government

Although many investors thought that there had been *some* improvement in the past five years in the way the government, at both the national and the local level, dealt with investors, much further room was still available. Licensing requirements were a case in point. The representative of the Kenya Association of Manufacturers at the workshop pointed out that the total number of business licenses in Kenya was over 1,300.<sup>55</sup> Another participant noted that technically he needed a license to advertise his own product on his own truck but mercifully enforcement was weak in Kisumu. Quite apart from the sheer number of licenses and procedures that had to be complied with, investors in Kisumu felt that they had a major additional burden to carry: they could not comply with most of these demands in Kisumu but had to travel to Nairobi to do so.

<sup>54</sup> The frequency of such incidents appears to be related to the nature of the goods being transported. The more easily disposable the goods (e.g., sugar or fish), the more vulnerable the truck.

<sup>55</sup> The KAM's 2006 survey, *Manufacturing in Kenya*, provides a complete list of the 1,323 licenses in an annex. However, see fn. 52 above for improvements.

The Kenya Investment Authority (KIA) was generally well regarded. However, it was seen as an institution that needed much strengthening to be truly effective in facilitating investment. It was also seen as being of more use to new investors than to existing ones. Nonetheless, there seemed to be general agreement that Kisumu would profit from having the KIA present in the city.<sup>56</sup> In general, investors felt that a much greater investment promotion and facilitation effort was required in Kisumu. Apart from the KIA, the Municipal Council of Kisumu (MCK) could be playing a much larger role in this effort than it currently was. The MCK could also do much more to help with the acquisition of land. The existing registry was manual and ineffective. A digital system would help, as would the establishment of an industrial park or estate, along with an export-processing zone.

Dialogue between business and government was by no means missing, with the KAM in particular playing an active role. However, a broader dialogue mechanism that went beyond manufacturers would be helpful (perhaps modeled on the Global Compact Kenya Network). There was a real need to sensitize local authorities to the importance of investment and the needs of investors.



### Some specific points

- The railway from Mombasa to Kisumu was in poor condition. A number of investors seemed to assume that it was dysfunctional and relied only on road transport.
- Feeder roads had seen some improvement but progress had been slow.
- The workforce was generally commendable.
- The tax system was not satisfactory. The tax base was too narrow and VAT refunds continued to be a problem.
- Governance issues (red tape and corruption) continued to be a concern.
- Opportunities in and around Kisumu included rice, organic cotton, low-cost housing, lake transport and health services.

<sup>56</sup> The KIA currently has a regional office in Eldoret, about four hours northeast of Kisumu by road, but not one in Kisumu itself.

### Conclusion

Current investors in Kisumu are upbeat about their city and its potential. Most of them clearly share the MCK's vision of Kisumu as a trade and transport hub in East Africa. They welcome the re-emergence of the East African Community and its progressive integration and see it as enhancing Kisumu's economic prospects. They would like to see the government make transport infrastructure a top priority and would welcome a partnership with the government to promote Kisumu as a location for investment.

## 2. Foreign investors in Kisumu and in Kenya

### Foreign investors in Kisumu

Company name	Major foreign ownership	Nature of business
Agro-Chemical & Food Company Ltd (Mehta Group International)	India	Alcohol from sugarcane and molasses
Barclays Bank of Kenya Ltd (Barclays Bank plc)	United Kingdom	Banking and financial services services
Bata Shoe Company (Kenya) Ltd (Bata Shoe Company)	Switzerland	Footwear
British American Insurance Company Company (Kenya) Ltd (British American Group of Companies)	United Kingdom	Insurance
Dominion Farms Ltd (Dominion Group of Companies)	United States	Rice and other cereal grain production, aquaculture
Group 4 Securicor (Group 4 Securicor)	United Kingdom	Security services
Kenya Shell Ltd (Royal Dutch Shell plc)	The Netherlands	Petroleum
MOIL (Moil Tanzania)	Tanzania	Petroleum shipping, barges
Rift Valley Railways (Sheltam Trade Close Corp.)	South Africa	Transport
Spectre International Ltd (Energem Resources Inc)	Canada	Potable ethanol from sugarcane, molasses, yeast
Standard Chartered Bank Kenya Ltd (Standard Chartered plc)	United kingdom	Banking and financial services



## Foreign investors in Kenya

This is a small sampling of foreign investors in Kenya, grouped by sectors. It does not include any of the companies shown in the Kisumu list above. A more extensive list of foreign companies in Kenya can be found in UNCTAD's 2005 guide to Kenya.

Company name	Major foreign ownership	Nature of business
<b>Agriculture and related activities</b>		
BAT Industries (British American Tobacco plc)	United Kingdom	Tobacco products
Delmonte Kenya Ltd (Cirio Del Monte Foods International Ltd)	United States	Food products
George Williamson Kenya Ltd (Williamson Tea Holdings plc)	United Kingdom	Tea/ Food
Unilever Tea Kenya Ltd (Unilever plc)	Netherlands and United Kingdom	Tea growing and processing
<b>Mining, oil and gas</b>		
BOC Kenya (The BOC Group plc)	United Kingdom	Industrial gases
Caltex Oil (Kenya) Ltd (ChevronTexaco Corporation)	United States	Petroleum
<b>Manufacturing</b>		
Atlas Copco Kenya Ltd (Atlas Copco AB)	Sweden	Industrial equipment
Bamburi Cement (Lafarge)	France	Clay products
BASF (BASF AG)	Germany	Chemicals and plastics
Bayer East Africa (Bayer AG)	Germany	Pharmaceutical
De la Rue Ltd (De la Rue plc)	United Kingdom	Currency and security printing
General Motors (General Motors Corporation)	United States	Motor vehicle assembling

Company name	Major foreign ownership	Nature of business
Glaxosmithkline (Glaxosmithkline plc)	United Kingdom	Pharmaceutical, medical
Mitsubishi Motors (Mitsubishi Corporation)	Japan	Vehicle manufacturing
Nestlé Foods Kenya Ltd (Nestlé SA)	Switzerland	Food products
Siemens Limited (Siemens AG)	Germany	Telecommunication equipment
Tetra Pak Ltd (Tetra Laval International SA)	Switzerland	Packaging materials
<b>Financial services</b>		
Citibank N.A. (Citigroup Inc.)	United States	Banking
Jardine Alexander Forbes Insurance Brokers Kenya Ltd (Alexander Forbes)	South Africa	Financial services
Old Mutual Life Insurance (Old Mutual Plc)	United Kingdom	Insurance
<b>Tourism services</b>		
Abercrombie & Kent Ltd	United Kingdom	Tour operations
Lonrho Hotels (Norfolk Hotel, et al. – John Holt Group Ltd)	United Kingdom	Hotel management
Pollman's Tours and Safaris (Partly TUI Group)	Germany and Mauritius	Tour operations
Tourism Promotion Services Ltd (Serena Hotels – Aga Khan Group)	Switzerland	Hotels & lodges
<b>Business support services</b>		
Ayton Y & R Group Ltd (Young & Rubicam)	United States	Advertising
Cargill Kenya Ltd (Cargill, Inc.)	United States	Tea warehousing, handling, storage, blending, etc.
Maersk Kenya Ltd (A.P. Moller Maersk A/S)	Denmark	Shipping

**Source:** Millennium Cities Initiative, drawing on UNCTAD's 2005 Kenya guide and other sources.

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## appendix

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### Pointers to further information

Kenya Investment Authority  
National Bank Building, 8th Floor  
Harambee Avenue, P.O. Box 55704  
Nairobi, City Square, 00200  
Tel.: 254 20 221 401-4  
Fax: 254 20 243 862  
Website: [www.investmentkenya.com](http://www.investmentkenya.com)

### In Kisumu

Municipal Council of Kisumu  
P.O. Box 105  
Court Road  
Kisumu, Kenya  
Tel & fax: 254 57 202 3812

Lake Basin Development  
Authority (*Kenya*)  
P.O. Box 1516, Kisumu  
Tel. 254-057-2027227  
Fax : 254-057-2027228  
Email: [lake-basinauth@yahoo.com](mailto:lake-basinauth@yahoo.com)

Lake Victoria Basin Commission  
(*East African Community*)  
P.O. Box 1510  
Kisumu, Kenya  
Tel: 254 57 202 6344  
Fax: 254 57 202 6322

Kenya Association of Manufacturers,  
Nyanza/Western Chapter  
Re-Insurance Plaza, 3<sup>rd</sup> Floor Right Wing  
P.O. Box 3605-40100  
Kisumu, Kenya  
Tel & fax: 254 57 202 5757  
E-mail: [kamkisumu@wananchi.com](mailto:kamkisumu@wananchi.com)

Kenya National Chamber of Commerce  
& Industry  
P.O. Box 771  
Kisumu, Kenya  
Tel: 254 57 202 1345  
Fax: 254 57 202 3230  
E-mail: [kncciksm@yahoo.com](mailto:kncciksm@yahoo.com)

### Kenyan public sector

Ministry of Agriculture  
Kilimo Hse, Cathedral Road  
Nairobi  
Tel.: 254 20 271 8870  
Fax: 254 20 272 0586  
Website: [www.agriculture.go.ke](http://www.agriculture.go.ke)

Ministry of Planning  
and National Development  
Treasury Building, Nairobi  
Tel.: 254 20 338 111  
Website: [www.planning.go.ke](http://www.planning.go.ke)  
National Bureau of Statistics



Ministry of Planning  
and National Development  
Tel: 254-20-317-583, 317-586, 317-588,  
Fax: 254-20-315977  
Email: [director@cbs.go.ke](mailto:director@cbs.go.ke)  
Website: <http://www.cbs.go.ke/>

Ministry of Environment  
and Natural Resources  
Maji Hse Ngong Road, Nairobi  
Tel.: 254 20 271 6103  
Website: [www.environment.go.ke](http://www.environment.go.ke)

Ministry of Trade and Industry  
Teleposta Towers, Nairobi  
Tel.: 254 20 315 001-7  
Website: [www.tradeandindustry.go.ke](http://www.tradeandindustry.go.ke)

Ministry of Finance  
Treasury Building, Nairobi  
Tel.: 254 20 338 111  
Website: [www.treasury.go.ke](http://www.treasury.go.ke)

Kenya Revenue Authority  
Times Towers  
Haile Selassie Avenue, Nairobi  
Tel.: 254 20 310 900/315 553

Commissioner of Lands  
Lands Department  
Ardhi House, Ngong Road, Nairobi  
Tel.: 254 20 271 8050

Principal Immigration Officer  
Immigration Department  
Nyayo House, Nairobi  
Tel.: 254 20 333 531

Export Processing Zones Authority  
(EPZA)  
Administration Building,  
Athi River EPZ Viwanda Road,  
Off Nairobi -Namanga Road  
P. O. Box 50563-00200  
Nairobi, Kenya  
Tel: 254 45 26421/6  
Fax: 254 45 26427  
E-mail: [info@epzakenya.com](mailto:info@epzakenya.com),  
Website: [www.epzakenya.com](http://www.epzakenya.com)

### **Kenyan private sector**

Eastern Africa Association  
Jubilee Place, 5<sup>th</sup> Floor  
Mama Ngina Street  
P.O. Box 41272-00100, Nairobi  
Tel.: 254 20 340 341/214 898  
Fax: 254 20 340 341  
E-mail: [aaa@africaonline.co.ke](mailto:aaa@africaonline.co.ke)  
Website: [www.eaa-ion.co.uk](http://www.eaa-ion.co.uk)

Federation of Kenya Employers  
Tel.: 254 20 272 1929  
Fax: 254 20 272 1990  
E-mail: [fke@arcc.or.ke](mailto:fke@arcc.or.ke)

Kenya Association of Manufacturers  
Peponi Road, Westlands  
P.O. Box 30225-00100, Nairobi.  
Tel.: 254 20 374 6005/7  
Fax: 254 20 374 6028/30  
E-mail: [kam@iconnect.co.ke](mailto:kam@iconnect.co.ke)  
Website: [www.kenyamanufacturers.org](http://www.kenyamanufacturers.org)

Kenya Private Sector Alliance  
P.O. Box 3556-00100, Nairobi.  
Tel.: 254 20 273 0371/2  
Fax: 254 20 273 0374  
E-mail: [info@kepsa.or.ke](mailto:info@kepsa.or.ke)  
Website: [www.kepsa.or.ke](http://www.kepsa.or.ke)

### **Other**

African Trade Insurance Agency (ATI)  
Kenya Re Towers, 5th Floor  
Capital Hill Road, Upperhill  
P.O. Box 10620, 00100  
Nairobi, Kenya  
Tel: 254 20 271 9727 / 272 6999  
Fax: 254 20 271 9701

Email: [Info@Africa-ECA.com](mailto:Info@Africa-ECA.com)  
Website: <http://www.africa-eca.com/>

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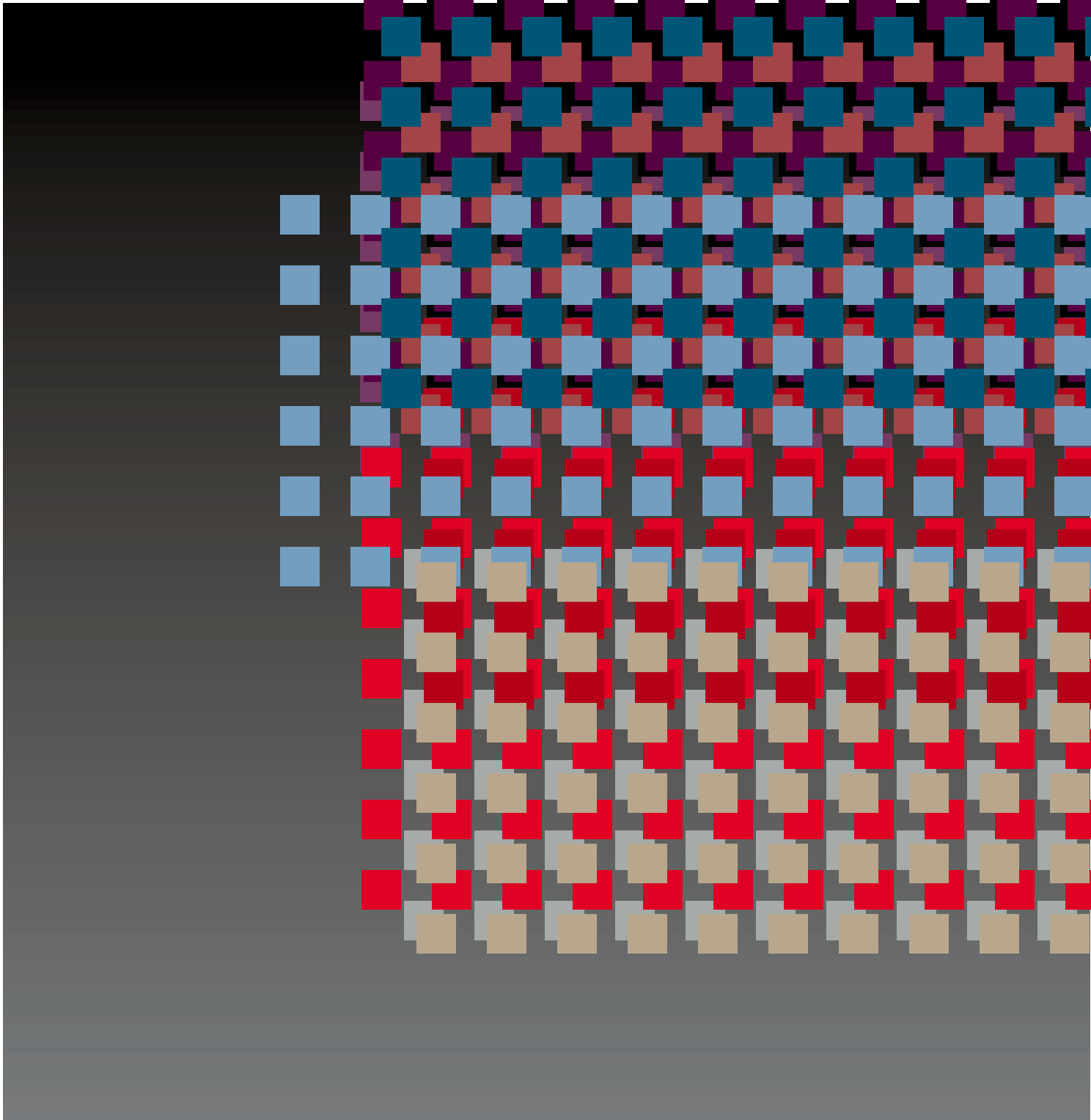
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