REGULATION OF FOREIGN INVESTMENT IN KENYA 1963-81: An Empirical Study

by

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ABBREVIATIONS

AC	Appeal Cases
CAE	Certificate of Approved Enterprise
CBK	Central Bank of Kenya
CBU	Complete Built Unit
CIC	Capital Issues Committee
CKD	Complete Knock Down
DFCK	Development Finance Company of Kenya.
EA	East African Law Reports
EALJ	East African Law Journal
EALR	East African Law Review
EAPH	East African Publishing House
EAPLR	East African Protectorate Law Reports
ECA	Exchange Control Act
ECN	Exchange Control Notices
ECOSOC	UN Council for Economic and Social Affairs
FIPA	Foreign Investment Protection Act
GSC	General Superitendence Company
HCCC	High Court Civil Case
IBRD	International Bank for Reconstruction and Development
ICDC	Industrial and Commercial Development Corporation
ICJ	International Court of Justice
ICLQ	International and Comparative Law Quarterly
IDB	Industrial Development Bank
IDR	Institute For Development Research
IDRC	International Development Research Centre
IDS	Institute For Development Studies
ILO	International Labour Organisation
ILW	Investment Laws of The World
ISPC	Industrial Survey and Promotion Centre
JMAS	Journal of Modern African Studies
JWTL	Journal of World Trade Law
KANU	Kenya African National Union
KENATCO	Kenya National Transport Company
MCI	Ministry of Commerce and Industry
MNC	Multinational Corporation
NCCK	National Christian Council of Kenya
NKP	New Kenya Party
NPC	New Projects Committee
OUP	Oxford University Press
PFI	Private Foreign Investment
PIMA	Project Implementation and Management Agreement
RAPE	Review of African Political Economy
SP 10/65	Sessional Paper No. 10 of 1965
TEA	Technical Engineering Agreement
TS & MA	Technical Service and Management Agreement
UN	United Nations Organisation
UNCTC	UN Centre For Transnational Corporation
UNCTAD	UN Cenference on Trade and Development
UNIDO	UN Industrial Development Organisation
WP	Working Paper
PS	Permanent Secretary

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ABSTRACT

Kenya was a British dependence since 1897 in more ways than just the political fact of colonial government. Even after independence in 1963, the capitalist ideology and economic structure pursued by the colonial regime has been maintained with the well to do African bourgeoisie taking over political power from the non-Africans. Private Foreign Investment was one of the economic mainstays particularly in Industry, at independence. It still is a dominant factor in the present Economy.

Although the government of independent Kenya has not used legislation much in regulating PFI, it has nevertheless, sought to impose some form of regulation on such investment. This study argues that despite such attempts, the active encouragement of PFI has meant that the government has been less than enthusiastic in pursuing its regulation with vigour and that, on the whole, PFI has been able to establish and operate in Kenya with minimal and often insignificant regulatory constraints. The study examines the government's three-pronged main thrust at regulation of PFI viz. the PFI approval process prior to establishment; the attempt to acquire corporate control over investment through Africanization of equity and management; and use of financial and fiscal measures. The study argues that these measures are undermined by the policy environment that often runs counter to their intended objectives. It calls for a review of the broad economic and social policies pursued by the government in order to remove the policy-induced distortions that afflict the attempts to regulate PFI thus rendering them largely ineffective.

INTRODUCTION

Private Foreign Investment (PFI) in underdeveloped countries (UDCs) has been on the increase in the period following the second world war. Such investment has played a major role in the shaping of many of these countries' economies. In Africa, such investment became prevalent after the 1950s following independence of many of these countries. Many of the newly independent African countries viewed PFI as the panacea to the solution of their economic problems. For many years after independence they sought to attract PFI in the belief that such investment was necessary in order to obtain capital, technology and skilled manpower. The concern was with the quantity rather than with the quality of the investment that flowed into their economies from abroad. PFI was viewed as a neutral ally in the pursuit of economic goals. It was not, in general, associated with exploitation or economic dominance over their economies to their detriment. Nyerere graphically describes the blissful ignorance the ruling regimes of the newly independent states displayed on the issue of economic 'colonisation.' He writes

> During our political struggle, some of us thought that independence would be the end of the process of liberation ... We were now beginning to discover that political independence, alas, is not enough. You have to have economic independence, and it is vital that the problems and areas of economic domination should be politically perceived before we can push the process of liberation to its logical conclusion ... We perceived the problems of colonisation in its correct perspective. We saw colonisation as a wrong. That wrong was perceived politically by the leaders of the nationalist movements.

> Not all of us realized that we were also economically colonised. That wrong was not politically perceived ... There was an underlying belief that political liberation would take care of economic independence too.[1]

Foreign investment has been, and still is, an extremely important medium for the perpetuation of economic domination by external economic interests. Many third world countries are now beginning to realize that PFI is not synonymous with economic development. The simplistic and naive perception of PFI as a neutral ally in the struggle for economic independence has undergone some significant change in the last ten years or so and continues to change in the light of UDCs' experience of such investment.[2]

The need for UDCs to control their economies has received a great deal of attention in the rhetoric of many spokesmen for these countries in national and international fora.[3] Again, Nyerere neatly summarises the theme of the rhetoric. He argues that

> The question is not whether nations should control their economy but how they do so. The real ideological choice is between controlling the economy through domestic private enterprise or doing so through some state or other collective institution.[4]

One thing that seems to be accepted in all UDCs is that regulation of PFI is a necessary condition to their serving the interests of national economies. However, the divergence of views on the degree, nature and objectives of such regulation is almost as diverse as the number of countries involved.

Some of the UDCs have increasingly pursued a more regulatory approach towards PFI while others have reluctantly imposed some form of regulation in response to specific crises e.g. foreign exchange scarcity.[5] A further distinction is in the form of the regulation exercised on the establishment of such investment. The Andean group of countries for example have a fairly specialised formal institutional machinery for regulating the aspects of foreign capital they deem necessary to regulate, while Kenya has only ad hoc machinery for the most part. In each case, the form and extent of regulation chosen corresponds to the general economic policy pursued by each state. In the majority of cases, there exists a striking discrepancy between government rhetoric and the reality as exemplified by its actual practice.[6] This work is an empirical study of the nature and efficacy of some key regulatory instruments over PFI in Kenya.

The declaration of a protectorate in June 1897 over most of what is now known as Kenya marked the beginning of a 70 years rule under British colonisation.[7] In December 1963, the country became independent after a long bitter and bloody struggle for independence. A year later, the country became a republic. Political independence did not, however, mean or lead to a complete break with the past. Kenya's economic system and policies, as well as her political ideology, have to a considerable degree been influenced by circumstances and institutions whose origins are traceable to her colonial past.[8]

Economically, the country is predominantly agricultural. The basic structure of the economy is one that was largely inherited from colonial times. Britain's colonial economic policy brought Kenya into the orbit of the capitalist world economy. Much of the first half of the colonial period's economic policy revolved around the need to extract the country's resources for the benefit of the metropolitan economy. The economy was a settler based one growing cash crops and breeding animals for export to the metropolis. The consumption needs of the European settlers and bureaucratic community were largely met by imports from the metropolis.

After the second world war, Britain intensified the extraction of resources from her colonies to help rebuild her war-battered economy. In an attempt to reduce her huge dollar deficit accumulated during the war years, she sought to increase the export of primary products from her colonies to dollar areas and to encourage the manufacture and processing of consumer goods in the colonies to avoid importing them from outside the sterling area. This was the beginning of the development of the import substitution industrial policy that has been pursued by independent Kenya with some remarkable vigour. In the 1950s, the colonial administration in Kenya began to adopt specifically protective investment policies in its economic policy. This led to foreign firms establishing production facilities behind these protective measures primarily to protect their markets. Nearly all the

production facilities established were heavily dependent on the metropolis.

Kenya's foreign investment policy and her regulation of such investment are greatly influenced by her political ideology. To the ruling regime, capitalism is the Kenyan ideology while all other ideologies, notably socialism and communism, are 'foreign' and therefore 'dangerous and subversive'.[9] The system lays heavy emphasis on private enterprise which is in control of basic economic activities particularly in industry. The role of the state was perceived as one of identifying possible investment opportunities and acting as the guardian of private enterprise. Until the 1970s, the state concentrated on creating the necessary infrastructure and political environment in which private enterprise would operate. Its control of the economy was not expected to emanate from its active participation, but from what the government referred to as a breed of 'sensitive controls' which would supposedly secure equity without interfering with the operation of the so-called 'free enterprise'.[10]

Having opted for a private enterprise based economy, the government was faced with a situation in which the dominant sector of this economy was largely foreign owned and controlled. To have got rid of foreign capital or discouraged it would have left the regime with little private capital and entrepreneurship to fulfil its plan targets. Thus, since independence, the country has pinned her hopes for

rapid economic growth on foreign capital.[11] The government therefore, adopted a very liberal policy on foreign investment. The foreign capital, on its part, responded to the government policy on industrial growth based on import substitution by increasingly setting up production facilities in the country that were virtually assured of lucrative returns due to the protection and other incentives given to such ventures. This trend has helped a great deal in perpetuating the dominance of foreign capital over the Kenya economy.

By the mid-1970s, the government had begun to run out of soft economic options based on import substitution industrialisation. The easy phase of this programme had been achieved largely through PFI. Despite this achievement, its real benefits to the long term economic development of Kenya remains doubtful. The Kenya regime has failed to capitalise on the potential offered by such investment. Given the incentives the country offers to PFI, this failure is a costly affair. In 1975, the IBRD warned the government that

> The issue of how much foreign investment to have is, in the last resort, a political one ... The more immediate question is how to get the greatest possible benefit from such investment, because of its enormous importance to Kenya, and because of the considerable incentives which are now offered to overseas investors. Unfortunately, in many respects, the present environment provides an abject lesson in how not to get much advantage from it all. 12

This study looks at some key policy strategies adopted by the government since independence to regulate and control foreign investment operations in Kenya. It examines the overall regulatory and control environment under which PFI operate in the country and its response to the same. It seeks to identify and trace the development of government attempts to regulate PFI since independence. The analysis lays emphasis on the political and economic foundations and determinants of the regulatory policies and measures identified. It seeks to demonstrate that the regulation of foreign investment in Kenya has been, and still is, conditioned by an interplay of political and economic factors that are at times, conflicting, inconsistent and misguided in their application to Kenyan circumstances.

Chapter one looks at the historical foundations of the present economic system and many of the policies that have contributed to its evolution. It is not in any way intended to be an exhaustive coverage of the economic policies pursued by the colonial administration. Its objective is to provide an idea of some of the historical factors that have influenced or shaped the formulation of current economic policies in the country. It is for this reason that great attention is given to some of the strategies adopted to ensure the survival of capitalist relations of production and to retain Kenya within the orbit of the world capitalist market.

In chapter two, government policy on private investment and in particular, PFI, is discussed in some detail . An analysis of some of the basic legal framework in existence for the safeguarding of the economic and political interests of PFI is included as an indication of the government's commitment to welcoming it to the country. In addition, the government's explicit policy on regulation of PFI is outlined. The objective of this chapter is to provide a picture of the economic policy environment in which PFI operates in the country. The assumption underlying this objective is that any regulatory measures undertaken towards PFI will reflect, and be conditioned by, the nature of government economic thinking which may be a significant constraint to their effective application. The liberal open door policy towards PFI adopted by the government since independence is a major contributory factor to the lack of a comprehensive policy on its regulation and to the inefficacy of the existing rudiments of regulatory framework that tend to respond to individual crises and also to personal or group interests as opposed to national ones.

Chapter three discusses the ad hoc regulation governing the establishment of PFI in the country. With the exception of the 1964 Foreign Investment Protection Act,[13] there is no other legislation in the country specifically designed to regulate specific or general aspects of PFI operations. This Act is not, and was not intended to be, used for regulation purposes. Despite this lack of specific

legislative machinery for the regulation of the establishment of PFI, other forms of regulation do exist. All business ventures in the country have to register with the office of the Registrar General in accordance with the relevant legislation governing the type of business involved.[14] These statutes provide for certain procedural regulation for the registration of establishing business as well as for some substantive, though for the most part technical, regulation for operation of registered businesses.[15] However, the chapter is not concerned with these technical legal aspects of business establishment, but with the regulatory policies applied to prospective PFI independently of the registration system. I have referred to this type of regulation as the investment approval process. Using empirical data, the chapter outlines and analyses the approval process with the object of establishing its efficacy or otherwise and the factors underlying the same.

In chapter four, the thorny issue of Africanization of business and personnel is considered. For political and personal reasons the predominance of non-Kenyans in the ownership and management of business in the country was unpalatable to a government that had come to power on a nationalist platform. Having rejected public ownership as the ultimate objective of government economic policy, the government chose Africanization as the alternative in taking over business from foreign and non-African hands. The emphasis was on facilitating African ownwership of equity in private enterprise and engaging African personnel in

management positions. The former is premised on the notion that owners of property have the right, power and the ability to exercise effective control over their property. The basic theme of the chapter is that this notion is not supported by the reality in Kenyan projects associated with foreign capital. The chapter outlines the objectives and the process of the Africanization programme since independence. Using empirical data, it is shown that Africanization as a regulatory and control strategy has not succeeded in dislodging foreign capital from its dominant position in the operation of projects involving local equity participation. The key reasons behind this failure are considered in the chapter. This approach was considered necessary due to the fact that the Kenyan regime has all along regarded the programme as the linch-pin in the attainment of economic independence. Although not all aspects of the programme and foreign capital's counter-strategies, have been considered, the chapter clearly shows that without a radical transformation of the programmes' strategies, there is clear danger that the economy is likely to be increasingly characterised by what Berle and Means referred to as

> Ownership of wealth without appreciable control and control of wealth without appreciable ownership. [16]

In order to concentrate on empirical evidence of the failure of the programme as a regulatory and control measure over PFI, the chapter does not deal with the technical legal niceties on the powers of shareholders to exercise control

over their investments. This topic is adequately covered in existing literature.[17]

Chapter five deals with government financial and fiscal regulation over foreign capital. It discusses exchanage control and taxation measures. A brief discussion of the industrial training levy scheme is included to demonstrate the futility of haphazardly developed legislative measures in terms of goal achievement. Exchange control and taxation are probably what most foreign investors in Kenya regard as the most far-reaching regulation undertaken by the government. The discussion in this chapter shows that this is really not the case in the light of available evidence. It shows that the present regulatory framework has been substantially inadequate to deal with the problems posed by the strategies adopted by PFI to circumvent the intended control. A great deal of this inadequacy is a direct consequence of the government's open door policy on PFI and its ambivalence over the issue of its regulation. After outlining the key measures adopted, the discussion concentrates on the analysis of their shortcomings within the Kenyan circumstances. Again the emphasis is on empirical factors rather than on mere enumeration of legal provisions.

Chapter six concludes the study. It considers whether the existing regulation system is properly equipped to deal with the very complex problems raised by PFI in the country and discusses the conclusions drawn from the overall analysis

in the study. The concluding remarks and observations in the chapter deal with broad issues affecting regulation of PFI rather than the detailed regulatory measures which are adequately covered in the rest of the study. These argue that since regulation is only a means to an end, the end must be clearly perceived before any regulatory measures are imposed. The underlying theme of these observations is that it is not regulation that determines the economic, social and political policies and goals of a country, but rather that the latter determine the nature and extent of the former. The basis of an effective regulatory system is, therefore, the existence of coherent and rational economic policies intended to achieve specific objectives in society. In addition, the discussion in the chapter goes on to argue that political will is a key element in the formulation and enforcement of any regulation of PFI. Political will is necessary to reverse the present trend where private interests appear to have been substantially pursued instead of, or at the expense of, public ones. The chapter also advances a case for institutional reorganisation as well as that of the decision making process in matters involving PFI.

RESEARCH AND METHODOLOGY

In the course of the preparation of this study, the question of the scope of coverage arose. There was a choice of adopting a legalistic approach to regulation which would have meant concentrating on provisions of legal instruments

and the case law founded upon such provisions. This would have led to the exclusion of those measures of control and regulation not expressed in legal instruments e.g. the Africanization programme. This approach was rejected for two main reasons. First, it would have ignored the real issues involved in the task of regulating PFI by concentrating on the form and legal theory of regulation rather than the substance and reality involved in such a politically charged exercise. Second, this type of regulation is well documented elsewhere in readily available sources.[18] Having rejected this approach, an empirical approach to the problem was adopted. Furthermore, the study is not placed within any particular or general legal theory or theoretical framework on regulation of PFI. This is because the study is intended to be a fairly comprehensive analysis of the Kenyan scene approaching the subject from a legal as well as an economic and political standpoint. This seeks to avoid the all too familiar approach to the subject in which most studies limit themselves to one facet of the topic such as the right of the state to regulate PFI, nationalisation of foreign assets, dispute settlements, choice of law in international contracts, regulation of technology transfer, limitation on foreign equity holding etc.

In choosing such an area of coverage, the guiding principle was the potential role that effective implementation

of pertinent regulation over such areas would play in the formulation of a comprehensive overall economic policy in a an environment in which PFI is already heavily involved. This called for an investigation of the actual practice in operation of the existing regulatory machinery.

The collection of data for this study was done during the second half of 1978 and that of 1980 as well as in the third quarter of 1981. The study covered a random sample of thirty eight projects in which PFI is involved. Out of this initial number, only twenty five projects provided enough data upon which some form of analysis could be based. The areas covered by the available data included the following:

- identification of investment areas;
- pre-investment studies;
- participants;
- negotiations between foreign and local parties;
- relations between government and projects;
- application of regulations to projects;
- PFI's strategies in response to regulation;
- institutional machinery for regulating foreign investment;
- policy formulation on PFI and decision making in matters concerning the same;
- the role of the Kenyan partners and personnel in the operation of projects involving PFI; and
- agreements between Kenyan firms and foreign firms as well as those between the Kenya government and other governments or foreign institutions relating to specific investments.

Not all data collected are used in this work. However, the selection of data for use was based on their representative character of the subject area or areas they cover .

The data collected are both primary and secondary. They were collected within and without Kenya. The bulk of the research data was obtained through interviews with project and government officials. In conducting the interviews, efforts were made in each case, to obtain documentary evidence to corroborate the interviewees' responses. Owing to the informal nature of the interviews, this was largely successful. Thus in nearly all cases in this work where the source is given as 'interview', documentary evidence where it existed to back this was either shown, or made available to the author. However, even where it was available, its open use in this study would have involved a breach of an undertaking given by the author not to make direct references to it. Some tabulated data and other information was obtained from existing studies by other researchers in similar fields. Nevertheless, even where use of such tabulated data was made, the raw data upon which such tabulation was based was available to the author independently of the existing work in nearly all cases.

The services of a research assistant were used in obtaining data from the office of the registrar general and to conduct several interviews with four company officials. Eighty two interviews were carried out, excluding numerous

repeat interviews, with business and government officials between 1978 and 1982.[19] In addition, there were two interviews with officials of a Swiss company in Geneva conducted in 1981 and four with representatives of foreign firms operating in Kenya which took place in Stratford-Upon-Avon in April 1981. All the interviews, except the Geneva ones, were conducted on an informal basis and all the questions were of an open ended type. No questionnares were used in this study.

Library research was carried out in Kenya newspaper, parastatal and public libraries as well as in the university library. In two important cases, I was able to informally make use of government registries. Outside Kenya, the resources of the following institutions were made use of:

- the British Overseas Trade Board Library, London
- the Foreign and Commonwealth Office Library, London
- the Institute of Advanced Legal Studies Library, London
- SOAS, University of London, Library, London
- Company Registry, London
- Bodleian Library, Oxford
- IDS Library, Sussex University
- Warwick University, Coventry, and
- IDR, Copenhagen.

NOTES

1. Nyerere, 1979, 20

2. For example, foreign firms in the copper industry in Chile made a profit of 4b. dollars in 42 years on an initial investment of a mere 30m. dollars. Again, in just one year, American firms withdrew profits from the third world that represented net transfers in their favour of 1.723b. dollars of which 280m. dollars came from Africa. (see Salvador Allende's speech to the UN., 4/12/72 reproduced in Hugo Radice, ed., 1975, at pp.236 and 242).

3. See for example The UN Charter Of Economic Rights And Duties Of States, 1974.

4. Nyerere, 1968, 264.

5. Examples of the first are India and South Korea while Kenya and Sudan are good examples of the latter.

6. Tanzania is a case in point. Its rhetoric has emphasised self-reliance while the practice has been more and more dependence on foreign, in particular aid, resources. Ivory Coast, Philippines, Nigeria, and Kenya are also good examples to name just a few.

7. See G.K. Kamau, 1975

8. See Leys, 1975; Hazlewood, 1979; ILO, 1972.

9. See for example, Parliamentary Debates, March 1982.

10. Sessional Paper No.10 of 1965, 10.

11. See Deepak Lal, 1975

12. IBRD, 1975, 309 (emphasis added)

13. Cap. 518, Laws of Kenya

14. The main ones are: The Companies Act, The Registration of Business Names Act, The Banking Act, The Insurance Business Act, The Building Societies Act, and The Partnership Act.

15. For example, The Companies Act provides for extensive regulation over matters concerning the issue of share capital by companies registered under the Act. See Part III of the Act.

16. Berle and Means, 1932, 4.

17. See for example, P Sargant Florence, 1970, 1961, 1947; Penrose, 1946; B. Gower, 1955-6; R.A. Gordon, ed., 1961; M. De Vroey, 1975; Theo Nichols, 1969; M. Gilbert, ed., 1972; and Osunbor, 1981.

18. See for example, O.C. Eze, 1975; J.W. Katende, 1969; Nwogugu, 1965; Friedman, 1953; Scwazenberger, 1969. etc.

19. Many of these were carried out in 1978 and 1979, before the formal commencement of this study in September, 1979.

CHAPTER ONE

SOME ASPECTS OF POST WORLD WAR II ECONOMIC POLICY IN KENYA

A : A BRIEF HISTORICAL SUMMARY

(a) Pre-War Period

When Britain declared Kenya a protectorate in 1895, she set about consolidating her imperial rule over the country that was to last for nearly 70 years. In 1920, she formally annexed the territory with the exception of a 10 mile coastal strip.[1] The creation of a "whiteman's country"[2] in which the native Africans were to be second class citizens in their own country was the major theme of the first half of the 20th Century. Their assigned role was expected to be that of suppliers of cheap, and at times, unpaid labour at the whims of the colonial rulers. The "whiteman's" country was expected to be created "with a flow of white people mainly from Europe.[3]

1902 marked the real beginning of a deliberate policy of white settlement to the detriment of the native population. That year saw the enactment of the Crown Lands Ordinance.[4] It provided for the alienation of native lands to white settlers on 99 year leases. This Ordinance marked the beginning of a series of legislation designed to economically subjugate the native population to the whims and dictates of an alien community. The Crown Lands Ordinance

of 1915 declared all land to be Crown land thus disinheriting the natives from their ancestral rights to land. The Ordinance formed the legal basis of a racially determined land policy that the colonial authority was to pursue with much vigour in the next 50 years. A colonial judge, well schooled in his racial prejudice, had no doubts at all regarding the consequences of this ordinance to the land rights of native peoples. Among other things, he said, it was meant to vest land reserved for the use of natives in the crown and in consequence all native rights in such lands had disappeared and the natives in occupation therein had become tenants at will of the Crown.[5]

For most of the colonial period, the economy of the country was based almost entirely on agriculture. It was for this reason that the colonial administration encouraged white settlement in the highlands. Its legally sanctioned racial policies aimed at basing the creation of a monetary agricultural economy on such settlement to the exclusion of non-whites. Thus, for example, Sir Charles Elliot forbade Asians, on racial grounds, from owning land in the highlands, an administrative measure that was sanctioned by the Colonial Office in 1906 and 1908.[6] The Privy Council, it too not unfamiliar with racial prejudice, sanctioned this racial discrimination decreeing that imposition of racially discriminative conditions of land sales were within the powers of the Commissioner for Lands under the 1915 Ordinance.[7] The emphasis on settler agriculture led to a situation in

which the settlers' interest dominated the politics and the formulation of economic policies.[8] The main interest of the colonial power was to develop the colony into a supplier of raw materials, mainly agricultural, for British industries as well as a market for these industries. The settler economy met this need sufficiently by supplying such products as cotton, sisal, hides and skins, meat etc. to British industry. Thus only a handful of international firms were operating in Kenya prior to 1945 and most of them were in agriculture related enterprises, mining and the provision of basic infrastructure. The colonial office which wanted to develop Kenya into a market for British industrial goods viewed colonial industries as a threat to British products in the home market as well as in other colonial markets. In her study of foreign corporations in Kenya, Swainson convincingly argues that the British colonial policy towards the extraction of raw materials from the colonies involved the positive discouragement of colonial industrial development, with the exception of such industries as were linked to the agricultural sector of the economy.[9] Given such an attitude to the establishment of local industries coupled with the dominance of settler interests before the second world war, foreign investment in Kenya remained low and was largely concentrated in primary industries, that were mainly of an extractive nature.[10] Table 1 shows the principal foreign based firms in Kenya before 1945.

Table 1 The Principal Foreign-based Companies in Kenya before 1945

Date	*Name of Firm*	*Type of Business*	*Parent Company and Country of Origin*
Agriculture and Estates			
1924	African Highlands Produce Co.	Tea	James Finlay, U.K.
1924	Kenya Tea Co.	Tea and Coffee	Brooke Bond, U.K.
1931	Anglo-French Sisal Co.	Sisal Plantations	British/French
1907	East African Tobacco Co.	Tobacco Trading, Tobacco and Cigarette Manufacture (1934)	British American Tobacco, U.K.
1932	East African Tanning and Extract Co.	Wattle Bark and Extract	Natal Tanning and Extract, S.A. Forestal Land and Timber, U.K.
1936	E.A. Sisal Estates, Ltd.	Sisal Production	Mitchell Cotts, U.K.
1906	British East Africa Corporation	Agents, Exporters of Primary Produce	Mitchell Cotts, U.K.
Trading			
1920	Bird and Co., (Africa) Ltd.	Merchants, Transporters, Shipping, Freight, Warehousing	Bird and Co., U.K.
1920	Gibson and Co.	Agents, Exporters of Primary Produce	Gibson and Co., U.K.
1934	Holland Africa Line	Shipping and Warehousing	Netherlands
1924	Gailey and Roberts	Import and Distribution of Agricultural Machinery, etc.	United Africa Co., U.K. (after 1937 Unilever)
Manufacturing and Minerals			
1911	Magadi Soda Co., Ltd.	Extraction of Soda	E African Syndicate (taken over by I.C.I. in 1923), U.K.
1922	East African Power and Lighting	Generation of Electrical Power	Power Securities, Balfour Beatty Co. U.K.
1920	East African Breweries	Beer	Ind Coope, U.K.
1933	East African Portland Cement	Cement Clinker Grinding	Associated Portland Cement, U.K.
1935	Leibig	Meat Processing	Leibig. U.K.

Source: Kaplinsky, 1978, p.51

(b) Post War change in Economic Policy

The second world war brought about a significant change in economic policy relating to industrialization. During the war, the colonial office emphasised the need to exploit colonial resources for the benefit of the war-battered British economy.[11] The secretary of state for the colonies, for instance, sent out a circular on economic policy stressing the need for increasing the flow of colonial supplies to help Britain meet its war requirements.[12] Thus a new colonial economic policy was prompted by the changed position of Britain in the world economy after the war.[13] Increased production of raw materials and import-substitution manufacture of products hitherto imported from Britain became a pressing priority to help earn dollars to offset the rising dollar deficit of the "mother country".[14] It became imperative, then, for the colonies to either produce manufactured goods to meet their own demand, or to import them from Britain rather than from outside the sterling area. This policy meant that the economy of Kenya, by being developed into a supplier of primary products to the mother country and an importer of the latter's industrial goods, was geared to fulfilling the economic needs of her colonial power. The pattern of foreign investment that followed reflected this phenomenon.

The existence of a non-African population, both as producers and consumers provided the initial stimulus for the development of manufacturing and processing in Kenya by

foreign capital. This population coupled with the slowly rising purchasing capacity of the non-white population provided a significant market for a range of industrial consumer goods. This relatively larger home market than that available to its neighbours, put Kenya in a favourable position to capture the neighbours' market thus creating an enlarged market for foreign capital. In addition, official colonial policy favoured Kenya as an administrative headquarters for the region. This favouritism was partly in response to the settler pressure on the colonial power to put in more emphasis on Kenya than on her two neighbours whose white population was only a small proportion of the Kenyan one. By the late 1950s, Kenya had become the industrial centre for the whole of East Africa. With an increasingly favourable policy on industrial development, foreign capital was bound to be a growing and dominant sector of the colony's economy.[15]

A rapid expansion of industrial development followed increased supportive government intervention policies in the post-war years. By 1954, the geographical net income attributable to manufacturing industry had exceeded that of settler agriculture for the first time in the colony's history.[16] Competition from non-British sources led to a system of protection that encouraged many British firms to set up production facilities within Kenya. Following this trend, a Royal East Africa Commission Report of 1955 outlined two measures of promoting economic development.

The first measure was, inter alia, the provision of suitable infrastructure and removal of restrictive regulation on investments. The second aimed particularly at overseas capital which would be increased

> ... if there should be a climate of opinion that is not obviously well disposed to a continued inflow of external capital and enterprise.[17]

In addition to the Royal Commission's recommendations, a 1955 government report on "Economic Assistance For Primary and Secondary Industries," concluded that existing protection fell far short of being adequate to attract capital into investment. It argued that:

> appropriate assistance to an industry should be granted to the industry as a whole ... and this should be provided for by a special amendment to the customs tariff ... In a country where the setting up of a new industry is still a venture carrying considerable risks, it is doubtful whether a fair return on capital employment is enough to induce owners of capital to face the risks.[18]

It was foreign capital that led the way in exerting pressure upon the government to provide protection against competition as an inducement to the investment of capital in Kenyan production facilities. They usually insisted on specific protection measures prior to setting up such facilities in the colony.[19] Foreign firms were in a better position to pressurise the local colonial administration to adopt a more protective policy than before for two main reasons. First, they could invest their capital elsewhere if their

Table 2 *Tariff Protection to Foreign-Based Industrial Firms 1958–62*

Product	Company	Year Began Production	Duty Imposed	Year	Previous Duty
Industrial Ink	Coates Bros	1960	22%	1958	11%
Bicycle Inner Tubes	Bata Shoes	1958	90 cents per lb	1958	55 cents per lb
	Avon Tyre Remoulding Co.	1958	90 cents per lb	1958	55 cents per lb
Paints	Sadolins	1959	25%	1961	11%
	Leyland Paint Co.	1958	33⅓%	1963	11%
	East African Paints	1960	33⅓%		
	Walpamur	1961	33⅓%		
Vehicle Tyres	Michelin (Tanzania)	1962	S. 1/25 per lb	1968	90 cents per lb
	GI Tyre (Tanzania)	1969	S. 1/50 per lb	1968	90 cents per lb
	Firestone	1969	S. 1/50 per lb	1968	90 cents per lb

Source: Swainson, 1980, p.133

demands were not substantially met. The local administration felt the country needed such investment sufficiently to warrant susbstantial concessions to the foreign capital. Second such firms which were overwhelmingly British at that time, could apply direct pressure on the colonial government in London. Eglin suggests that the ultimate introduction of a comprehensive system of protective tariffs corresponds with the date of the establishment of foreign investment.[20] The pattern of protective tariffs introduced after 1958 lends support to this argument. Table 2 shows a sample of tariff protection introduced after 1958. By 1958 protection of domestic industries, a majority of which were foreign-owned, had received a major boost through the introduction of a comprehensive custom tariffs system.

In addition to the institution of a comprehensive scheme of import duties, 1958 also saw the introduction of a comprehensive system of import licensing under the Imports, Export And Essential Supplies Ordinance of that year.[21] The Ordinance empowered the governor to appoint a director of trade to issue licences for the importation or exportation of goods subject to licensing thereunder.[22] S.4(1) of the ordinance gave the minister such wide powers that:

> Whenever from time to time it appears to the minister, after consultation with such persons as appear to represent commercial and industrial interest in Kenya, to be necessary

> in the public interest ... he may by order either prohibit absolutely or restrict, by means of such conditions and limitations as may be specific in the order, the ... importation of any specified goods ... either generally ... or from any specific country ... (emphasis added)

This enabled the authorities to protect domestic industries either by regulating the category of goods imported or the source of such goods. This power was extensively used to protect domestic industries from external competition in particular from Japan.[23] Table 3 shows a sample of products that were subject to licensing in terms of both their category and source. Products such as cement, rubber products and textiles in which Japan offered very stiff competition were high up on the list of regulated imports.

Financial support was another approach the colonial administration adopted to encourage industrial development. The Industrial Development Council Ordinance of 1954[24] created the Industrial Development Council to assist enterprises in the colony. The IDC was designed to

> ... facilitate the industrial and economic development of the colony by initiating, assisting or expanding industrial, commercial and other undertakings in the colony.[25]

This body was to form the foundation of the system of partnerships between state and private capital up to the present day. In addition to the creation of a local financing body, Britain provided financial support or prepared ground for the entry of international capital into the colony.

Table 3

Sample of Products subject to Lincensing on the basis of both category and source.

Product	Country of Origin
Wax-based boot and shoe polish	All countries
Rubber bicycle tyres	Japan
Rubber bicylce tubes	Japan
Cement-Building	Japan
Stocking and hose	Japan
Vests and Singlets	Japan
Underpants	Japan
Slippers and house footwear of all materials except rubber	Japan
Footwear wholly or mainly of leather	Japan
Footwear wholly or chiefly of textile	Japan
Rubber footwear	Japan

Source: Imports, Exports and Essential Supplies (Import) Order 1961, THIRD SCHEDULE.

The Overseas Resources Development Act of 1948, for example, created two financial bodies to support investment by private capital in the colonies. The two were the Commonwealth Development Corporation (CDC) and the Overseas Food Corporation (OFC). Each had a capital of £50 million. They were intended to promote industrial investment by British private capital by financing necessary infrastructure and subsidising such investment.[26] Grants in aid were also significantly increased to help finance the development of infrastructure conducive to investment by private capital.[27]

By the mid-1950s, it was clear that the colonial government was committed in its support of an economic system founded on private capital. An overwhelming proportion of this capital was foreign owned or was heavily associated with the settler community in as far as it had any local content. At the same time, it had become increasingly clear that the struggle for independence had gained such momentum that its defeat through military means would, at best, be prolonged, costly and not conducive to the exploitation of the nation's resources for the benefit of metropolitan industry. By 1958, some far-sighted settler groups, closely associated with the colonial administration had began to realize that independence for the African majority population was just a matter of time. They saw their most immediate challenge as that of ensuring that the system of private enterprise developed so far survived

a takeover of power by the African nationalists.[28] They advocated measures that would lay the basis for a continuation of an economic system formulated during the colonial days that rested upon the foundation of private capital. The colonial power was receptive to such ideas as they would ensure the continuance of the benefits to metropolitan industries. The existing economic system had to be sold to the new African ruling elite as a viable system that would be worth retaining without radical structural changes after independence. How this objective was achieved is the subject of discussion in the remaining part of this chapter.

B : MEASURES TO PREEMPT RADICAL ANTI-PRIVATE ENTERPRISE POLICIES AFTER INDEPENDENCE

The first major issue the colonialists had to address themselves to was the deep resentment among the native population against its racial policy. Its policy of racial discrimination was epitomised by the administration's policy on land ownership in the highlands. Non-Europeans were prohibited from owning land in the highlands where a small number of white settlers held 7.5 million acres of land, or 31% of the country's best land suitable for agriculture and intensive animal husbandry, and employed the native population at low rates of pay.[29] In addition, following the same racial policy, the administration forbade Africans to grow cash crops in their so called reserves which were

in fact little else but concentration camps. Until the mid-1950s legislation and administrative practice fostered the development of settler production to the detriment of the non-Europeans. As Ghai and McAuslan pointed out

> Since the Europeans had an overwhelming say in the direction of government policy, ... economic and political development was looked at from a European perspective, and legislation was designed to further that development with little or no regard to the economic or social effects that such furtherance would have on Africans.[30]

This approach to economic policy had to change if the potential future African leaders were to be persuaded that the system of private enterprise set up under colonial rule could benefit them. It was, therefore, decided in 1959, that the racial allocation of land should be abandoned. This was legally implemented by a 1960 Order In Council that abolished racially based division of the country into scheduled and non-scheduled areas.[31] This decision paved the way for the inevitable ownership of land in the highlands by Africans. The lifting of legal racial barriers in many aspects of social and economic life constituted the first measure by the colonial rulers aimed at making the existing economic system and policies acceptable to the emerging African elites destined to rule over the nation in a few years time.

The second measure was to get the support of the African designated ruling elite for the colonial economic

system with minor modifications that would leave the basic structure substantially unchanged. This, they hoped would guarantee a continuity of economic policies after colonial political rule ceased. To achieve this objective, the colonial administration set about incorporating the future African ruling elites into the mainstream of the country's class of the privileged few. This was seen as a means of creating a vested interest in the maintenance of the system by the African leadership. It was also expected to help import western capitalist values to the African leadership which would help them aspire to a capitalist way of life thus opting for a capitalist economy. Blundell had no doubt that

> ... the real challenge to us [colonizers] is how we can give the Africans enough conviction and force to carry forward our own ideas and our own civilization ... Unless we can do that, unless the African himself can carry forward conviction that what we have to offer him is a real way of life, something really to work for, then I believe we have lost the battle for the continent of Africa.[32]

If the future African leaders could be thus convinced, then they could be expected to defend the private enterprise centred economy provided they obtained sufficient tangible benefits from it. This would make it possible for a post-independence government to endorse the economic system that not only rested on private capital, but largely on foreign capital at that. The economic interests of the metropolis would, therefore, be safeguarded without having to

retain a large force in the country.

As early as 1959 a new 'multi-racial' policy was being propounded - in particular by the New Kenya Group[33] led by Sir Michael Blundell. This group suggested a basis of collaboration between European and African interests in making a transition to political independence without any radical change in the existing economic structure.[34] Its fundamental axioms emphasised that

> The social and political tenets of the free world shall apply ... The rights of private property and the sanctity of contracts shall be respected.[35]

They saw economic factors as a major obstacle in the process of integrating the African leadership into the existing capitalist structure of the economy. They advocated that

> ... the only solution, in our view is vigorously to tackle the basic problem of low living standards, so that there <u>may rapidly emerge from the poorer majority, people with the same interests and similar ideals to those economically more advanced</u>.[36]

This view was not a novel one. It was in line with the earlier recommendations by the E.A. Royal Commission and the Swynnerton Plan.[37] These had been accepted by the administration as a basis for preparing the economic reforms to adopt the system to a changing political environment. Clearly the improvement of the African lot was not seen as an end in itself, but rather as a means to an end. The end was the continuation after independence of an economic system

established in colonial times in which foreign and ex-settler capital had a substantial share. It is also clear that reforms were not intended to affect the whole African population, but a few who would emerge from the poor majority to join hands with the economically more advanced. There was no doubt at this stage who were more economically advanced - they were largely the Europeans who had set up the then existing economic system. This would obviously produce a stratified African population with a few economically well endowed Africans taking the helm and forming an alliance with the existing capitalist class.

To achieve the goal of creating an African political elite with a vested interest in the existing economic system, the colonial administration set about to implement two sets of economic reforms that would, and were expected to, have stratifying effects upon the African population. These were the land tenure reform in the non-scheduled areas and the partial Africanization of the 'white highlands' - the scheduled areas. Both of these measures had been advocated by the E.A. Royal Commission

> ... the analysis and recommendations of which had been described by The Economist newspaper as 'Adam Smith in Africa.'[38]

The mother-country's economic system, adapted to colonial circumstances, was to be adopted in Kenya.

The land tenure reform in the non-scheduled areas aimed at the commercialization of African-occupied land in line with capitalist legal principles of property ownwership. It took the form of land adjudication, consolidation and registration.[39] Its immediate effect was the destruction of customary basis of land holdings. By conferring land ownership titles upon individuals, it became possible to deal with land as a commercial property upon which the aspiring African capitalists would base their accumulation of wealth. The reform was spelled out in the Swynnerton Plan. Its main political objective was to create wealthy capitalist farmers, tied to and dependent for their accumulation on, capitalist values, as a buffer between the existing economic system and the landless masses. As Swynnerton perceived it

> In future, if these recommendations are accepted former government policy will be reversed and able, energetic rich Africans will be able to acquire more land and bad or poor farmers, less, creating a landed and landless class.[40]

A capitalist orientation of African agricultural economy par excellence.

The partial Africanization of the hitherto 'white highlands' envisaged the transfer to Africans of 3.5 million of the 7.5 million acres in the scheduled areas suitable for agriculture and intensive animal husbandry. The Africans who were to own land in the highlands under this programme

were divided into two main categories: The first one comprised of some landless Africans and the second the emerging African middle class. The land was to be bought off the settlers on a willing seller willing buyer basis. The political history of the programme suggests that it was a colonial administration's insurance policy against too radical a change from existing economic policies following the transfer of political power to the Africans. Its main attraction was that it offered the African elite, poised to take over political power, a chance to step into the shoes of the former white elites. However, given the willing seller, willing buyer basis accepted by the African leadership,[41] the programme would need some massive financial aid from Britain. This gave Britain a negotiating card for the African leadership was keen to replace the colonial rulers and a programme that offered them some breathing space to organise was welcome. For those who sought the perpetuation of the economic system (shorn of its legally based racism) they had no doubt about how the programme ought to help. It was their view, that

> It must encourage the evolution of a responsible, contented middle class African who may be a bulwark of the emergent African state.[42]

This programme, like its counterpart the land tenure reform one, was intended to form the basis of accummulation for an aspiring African capitalist bourgeoisie. These two programmes incorporated the African elite into the monetary

agricultural sector which was at that time the backbone of the economy.[43]

Having designed the Africanization of the scheduled areas to meet political objectives, Britain agreed to finance the programme with a large aid package in the f of both loans and grants.[44] The future African rulers accepted this 'aid' with pleasure. They saw it as a means of keeping the lid on the kettle of the popular demand for re-distribution of land.[45] In addition, the 'aid' benefitted, almost without exception, all members of the small group of African elite that was to take over power after independence and hold tightly on to it thereafter. They got large tracts of the best land in the country all financed by the aid funds.[46] This aid, indebted the new African government to the 'generosity' of the former mother country who intimated that there would be more where that came from as long as the African government kept to course. And so there was.[47] The independent Kenya government was to toe the line. As Leys aptly points out, the education and climate of opinion in which the African leaders had moved since school

> ... had in most cases been premised on the acceptance of private property and the highly regulated monopolistic, private enterprise system established under colonialism.[48]

The thought of radically transforming the system, as experience was to reveal later, hardly ever crossed their minds. The worst they had in mind, it would appear, was the

encouragement of African businessmen of a similar orientation. Barely two months before independence in 1963, the Minister of Finance (designate), James Gichuru, was telling the Nairobi Chamber of Commerce (dominated by foreign interests)

> You do not have to go far in Nairobi today to become aware of people in our society, with new tastes, frequently with the money to satisfy them, and themselves creating a new demand amongst their fellows for better things of life ... At the same time I hear too frequently of the inadequacy of our distribution system, or the cost of reaching much of this potential market, and incidentally stimulating consumer demands and setting in train the urge 'to keep up with the Joneses' which can contribute so much to our productivity. I suggest that the way of making good these deficiencies is through the African businessman.[49]

The African businessman was, therefore, not perceived as an agent for transforming the structural foundations of the existing economy, but of spreading demand for its western tastes and products.

A series of foreign missions reinforced the African leaders' willingness to retain the existing economic structure by emphasising the need, indeed indispensability, to Kenya of improving conditions for private enterprise including foreign capital if she were to attain any credible rate of economic growth. Of particular importance was the IBRD Economic Mission to Kenya of 1962 undertaken "at the request of Kenya and the United Kingdom." At this time, Kenya was still a British colony and there is little doubt that Britain

requested the mission to endorse the modified (largely in racial terms) economic system formulated in Kenya between 1956 and 1962. A positive approval by an "independent" body such as IBRD would convince the skeptics, if any, among the African leadership of the value of retaining and strengthening the existing system. The mission duly gave its unmitigated approval. Its task was to

> ... undertake a general review of the economic potential of Kenya and to make recommendations designed to assist the government in the development planning for the period up to 1967, and in formulating policies which would further expand and stimulate the economy and so raise the standard of living of the people.50

The Mission assembled in Washington in September 1961, was in Kenya from mid-September to mid-December the same year, and commenced the preparation of its report in Washington in 1962. Thus in just three months, it managed, in between cocktail parties, wildlife trips and a visit to the Coastal beaches, to gather enough official and settler organisations' reports to compile its seemingly "authoritative" report. If speed were the only measure of efficiency, then the Mission was indeed the very epitomy of efficiency.

In its report, the Mission faithfully emphasised the need for not making any fundamental changes in basic economic policies. It warned that rocking of the boat was likely to lead to the collapse of the economy. It left no doubt of its conviction that Kenya's only hope of a stable economy

lay in her adherence to a capitalist economic system. It was emphatic that during the "next four years"

> ... a first requirement would be the adoption of and firm adherence to, policies likely to establish economic conditions to promote development.[51]

It recommended that such policies be formulated forthwith and reflect four main factors one of which was

(d) The promotion of the maintenance and further development of production in private hands to be assisted by:-

(i) A clear statement of policy towards private investment. This might include re-assurances about interference by the state with private undertakings. External investors will be concerned about freedom to transfer earnings and repatriate original capital.

(ii) Conditions in which private financial institutions can continue to operate and confidence in the currency preserved.

(iii) The opportunity to make reasonable profits.[52]

The other factors were on fiscal solvency, the maintenance of efficiency in all branches, and the maintenance of law and order. The Mission went on to rationalise that pursuit of these policies would have beneficial effects beyond the private sector. Such an approach, it felt, should encourage other governments and institutions

> ... <u>to look more favourably on Kenya's requests for external assistance</u>.[53]

As the Mission had already expressed its opinion to the effect that the economic growth of Kenya would "depend for

some time to come on funds from abroad,"[54] this was clearly a thinly veiled warning that availability of external aid depended on conformity to economic policies acceptable to potential donors.[55] On the role of the government in economic matters, the Mission was of the view that it should remain unchanged.

> Generally we do not think that the extension of the role of government in production would be beneficial during the next few years. In advancing up a suggested program, we therefore assumed that the scope of government intervention in economic life will be largely unchanged.[56]

Hitherto, the role of the government had been to support private capital mainly from abroad in its exploitation of Kenyan resources. It certainly had shown no intention whatsoever of transforming the inequitable capitalist oriented economic system into a more equitable socialist oriented one.

The analysis and recommendations of the IBRD Mission clearly represented the colonial administration's views formed from around 1955 to 1962 as well as those of some of the so-called liberal settlers organised under the New Kenya Party. There was neither objectivity nor originality in the Mission's report. Its recommendations on land, restoration of the confidence of private investors, need for continuity in economic policies, for example, had all been well documented in official and other records.[57] It is not surprising that the Mission's report should have

turned out to be merely a compilation of economic analysis and recommendations by the colonial administration and pressure groups such as the New Kenya Party. This, it is submitted with respect to the Mission, was precisely why it was called in. It had neither the mandate nor the intention of conducting an objective enquiry into the economic potential of Kenya with its peoples' welfare as the fundamental point of reference. It is doubtful whether it had any other mandate apart from giving a mark of legitimacy and respectability to an economic structure which had been fashioned by a colonial administration largely in response to interests of non-Africans , both individual and corporate.

C : CONCLUSION

This chapter has examined, albeit very sketchily, some relevant aspects of the colonial administration's policy. We have seen that the administration adopted racial policies in furtherance of its economic and political endeavours to create a colony modelled upon the British capitalist model to serve the economic interests of the mother country. Before the second world war, Britain's economic policy towards its colonies was based on the conception that the latter were merely suppliers of raw materials to be used by British industry, as well as a ready market for her industrial products. The economic hardships resulting from the war changed Britain's attitude towards the development of industries in the colony. Thus by the late 1950s, the

administration had begun to adopt a policy of increasing protection and encouragement of investment in the colony, the bulk of which were British in origin.

At the same time that the colonial authorities began encouraging domestic industries, they also finally realized that independence for the colony was just a matter of time. They were keen that a future African government should adopt their economic policies. So they set about to create the conditions suitable for the survival of the capitalist oriented economy after independence. They sought to do this by incorporating the future African leaders into the stream of the private system existing in the country. The land reform and abolition of racial policy in land ownership in the highlands saw to this while the IBRD economic mission to Kenya in 1962 provided the incoming leadership with an acceptable economic policy. The first two major economic policy documents[58] produced by foreign advisors under the auspices of the independent African government left no doubt that the measures taken by the colonial government had successfully been adopted and continuity of economic policy, at any rate a capitalist oriented one, ensured.

NOTES

1 See the Kenya (Annexation) Order in Council, 1920

2 See Blundell, 1964, 21

3 Ibid.

4 Ordinance No. 21 of 1902

5 As per Barth C.J., in Wainaina v. Murito 9 EAPLR 102.

6 See Sorrenson, 1968 chapter 10 and G.K. Kamau, 1975

7 Commissioner for Local Government, Lands and Settlement v. Kaderbhai, 1931 AC, 652

8 Sir John Campbell, financial and economic adviser to the secretary of state summed up the position as follows: "... The root of the problems seems to be political ... the constitutional position is such that the settlers' interests are overepresented by the sheer nature of things. Under the existing conditions the policy of the country is constantly bent towards the furtherance of their interests. As a body they are neither easy to deal with nor farseeing. The Government has not in practice a free hand ... I have seen how political exigencies have forced the Government time and again to do things which it was reluctant to do and which would have been better left undone." (Colonial Office Minutes. Quoted in Swainson, 1980, 24).

9 She cites the performance of some colonial agencies in support of this policy. The Empire Marketing Board, for example, gave no assistance to any forms of manufacturing limiting itself to the marketing of empire food. In theory, The Colonial Development Advisory Committee placed no limit on its sphere of activity, but in practice it totally ignored the industrial sector in the colonies. By 1939, it had allocated just under £8m. of which only £151,000 was for industrial projects and of this amount only £23,000 or 0.3% of the total allocations had been disbursed. (see Ibid. at p.26 also pp.33-34 for details). For colonial policy on the textile industries in Kenya, see Eglin, 1978.

10 See Swainson, 1980

11 During the war, Britain had accumulated a dollar deficit estimated at £311m. by 1948.

12 Lee, J.M. 1967, p.47

13 For details, see Swainson, 1980

14 Ibid.

15 Oil refining and Cement manufacture are good examples. Before 1969, British multinationals dominated the scene.

16 E.A. Royal Commission Report, 1955, 83

17 Ibid, 77

18 Economic Assistance For Primary and Secondary Industries, 1955, 8

19 A good example is the consistent refusal by a British Cement manufacturing firm to set up a plant in the country without protection against competition by cement imports. (see Swainson, Chapter II).

20 See Eglin, 1978

21 Cap 502 Laws of Kenya. Now styled 'Act'.

22 Ibid. ss 3(1) and 6(1)

23 See for example, The Imports, Exports and Essential Supplies (Imports) Order, 1961.

24 No.63 of 1954. The IDC succeeded the wartime Industrial Management Board.

25 MCI memo, KNA 16/3/52. quoted in Swainson, 1980, 121.

26 The East Africa Industries Ltd. was the most significant project promoted by the CDC and later turned over to international capital in the form of Unilever.

27 See Swainson, 1980 chapter 3

28 This was the loud and clear message in a document entitled "A Consideration of the White Highlands: Underwriting and Resettlement, Five Premises and The Five Points of a Kenya Highlands Charter, 1960" Ref. No. 33/C5B/Amended. (The only copy of this document known to the author is in the Standard Library, Nairobi).

29 In this area there were 3,600 settler farms varying in size from 26 to over 50,000 acres. By 1948, approximately 17,500 whites lived in rural areas.

30 Ghai & McAuslan, 1970, 96

31 s.14 of The Kenya (Lands) Order in Council of 1960 LN No.589 of 1960. This Order, which repealed the Highland and Native Areas Orders in Council, 1939, declared racially restrictive covenants and similar provisions void, and empowered the governor to make regulations providing for the conversion of estates from leasehold to freehold.

32 Speech by Blundell during the Legislative Council's debate on Sessional Paper No.10 of 1958/9.

33 This was a group of far-sighted settlers who sensed which side of their toasts would be buttered in the future. The post-independence experience of their leader, Michael Blundell, indicates they played their cards extremely well.

34 Leys, 1975, 43

35 Ibid.

36 The Challenge of the New Kenya, manifesto of the NKP, 1959 (emphasis added)

37 These were contained in R.J.M. Swynnerton 1955

38 Hazlewood, 1979, 9

39 Now carried out under The Land Adjudication Act, 1968 and the Registered Land Act, 1963

40 Swynnerton Plan, 10. (emphasis added)

41 See SP 10/65

42 Highlands Charter, 1960, 3. (emphasis added)

43 The Success of these programmes is portrayed by the consistent refusal by the independence government to place a ceiling on land ownership.

44 One third of all foreign debt incurred from 1961 to 1969 was made up of loans under the programme. (see Dept. of Settlement, Annual Report 1968/69, 13)

45 For a glimpse of a freedom fighters disappointment, see account in Leys 1975, 57

46 Many of these loans have not been repaid (see Auditor Generals Report, 1978)

47 For details see Holtham and Hazlewood, 1976.

48 Leys, 1975, 60

49 Speech to Nairobi C of C on 28/10/62. Quoted in Leys, 1975, 61-2 (emphasis added)

50 IBRD, 1963, (vii)

51 Ibid. 43

52 Ibid. 44

53 Ibid. 45

54 Ibid. 1

55 This seems to have been a position emphasised by potential aid donors. For example, in December 1960, the Director of Trade and Supplies reported to his minister that he had just learned that a proposed West German mission "will base its consideration of financial aid to Kenya not only on pure economic considerations, but also on the wider political aspects of the future of Africa. It will have regard particularly to steps which it might be able to take to counter communist infiltration." (quoted in Leys, 1975, 60-1).

56 IBRD, 1963, 45

57 In documents such as the Swynnerton Plan, E.A. Royal Commission Report, the 'Highlands' Charter, the New Kenya Party manifesto etc.

58 The 1964-70 Development Plan and Sessional Paper No.10 of 1965

CHAPTER TWO

GOVERNMENT POLICY ON THE TREATMENT OF PRIVATE FOREIGN INVESTMENT, 1963-81

A. GOVERNMENT POLICY POSITION ON PRIVATE ENTERPRISE

In the last chapter, I discussed the colonial administation's efforts and strategies to bequeath independent Kenya an economic system designed in the twilight days of colonial rule. This system rested on the pillars of private enterprise dominated by external capital. These efforts paid dividends as the independent government expressly accepted the inherited basic economic framework. It declared at the outset that the base

> ... from which the economy must grow during the plan period is the one established during the 1954-64 period. The resources now available for future growth have been inherited from that period and the present structure of industry, commerce and agriculture, and the composition of output are the products of that period.[1]

Although economic growth has proceeded at a rapid pace since independence[2], it has, nevertheless, continued on the lines set by the earlier colonial structure. This is not to say that there have been no changes. There have been many changes in the economy. Kenyanisation, for example, has radically changed the racial composition of the group of people in the centre of power, but these have not radically changed the basic structure of the economy.[3] For over 70 years of colonial rule, Kenya had been subjected to a system of

private enterprise. Independent Kenya government's policy has been consistently one of encouraging, supporting and defending this same basic private enterprise economic system.

In 1965, the government issued a major policy statement - AFRICAN SOCIALISM AND ITS APPLICATION TO PLANNING IN KENYA[4] - which has come to be regarded as independent Kenya's economic blueprint.[5] Despite the inclusion of the word 'socialism' in the statement, it ruled out collective ownership of means of production as the ultimate objective of the government's economic policies. The key principle embodied in the statement was the inviolability of property rights as long as the nation's productive assets were used "in the interest of society and its members".[6] The government committed itself to an economic system of various forms of ownership.[7]

A major cause of concern to the government at independence had been the fear entertained by a large section of the capitalists in the country that their property would be expropriated. In an attempt to assuage these fears the Prime Minister, Kenyatta, assured them that the government of Kenya

> ... will not deprive them of their property or rights of ownership. We will encourage investors in various projects to come to Kenya and carry on their business in order to bring prosperity.[8]

This assurance, also embodied in the 1965 policy statement, has become entrenched in the government's economic policy throughout the last eighteen years. It has been restated and re-emphasised in all later policy documents.[9]

After independence, the targets established for increased investment in industry were left to be implemented primarily by private enterprise, fostered by what was termed as a government policy

> ... characterised by encouragement and support where needed, in order to secure a maximum rate of economic growth and the structure and location of industry which will benefit the country most.[10]

Under this policy 86% of investment in manufacturing was expected to come from the private sector which was foreign dominated.[11] The government then argued that state ownership is not necessary to ensure that industry operates in the national interest and that increased state ownership might, to the contrary, have a detrimental effect on industrial development by

(a) discouraging overseas private investment and government aid;

(b) syphoning off public funds into compensation payments to investors whose investments are expropriated; and

(c) blunting the edge of the incentives for aspiring local capitalist entrepreneurs.[11]

Even as early as 1964, before the 1965 policy statement rejected nationalisation as an instrument of economic policy, the Prime Minister had emphatically stated that "the government considered that nationalisation will not serve to advance the cause of African Socialism".[12] However, if public control of any economic operation were necessary, nationalisation would be undertaken regardless of its cost. This would occur only if other less costly controls are unavailable or ineffective. Thus the overriding criterion for the nationalisation of private property was set as the necessity of public control. According to government expectations, such a necessity would arise in instances:-

(a) when the assets in private hands threaten the security or undermine the integrity of the nation; or
(b) when productive resources are being wasted; or
(c) when the operation of an industry by private concerns has a serious detrimental effect on the public interest.[13]

Should such a measure become necessary, the 1965 policy statement made it clear that it would apply to both Africans and non-Africans owning productive resources in any industry involved.[14] The commitment to non-nationalisation of private enterprise has been strictly adhered to by the government since independence. The incidences of outright nationalisation have been few.

In 1964, the government nationalised the then Kenya Broadcasting Corporation. This was to be the only case involving 100% outright nationalisation of a private business operation. In April 1970, the government purchased 51% of the shares of the East African Power and Lighting Company. Later it purchased the rest of the shares with the exception of a few belonging to 83 shareholders who refused to sell out and their shares were transferred from London to the Nairobi register. In 1970, the government purchased 60% of the shares of 78 domestic branches of the then National and Grindlays Bank Ltd.[15] Following this purchase a new corporation was created known as Grindlays International in which the government held 40% of equity with National and Grindlays holding 60%. This new corporation was formed out of the three remaining branches of National and Grindlays and was to engage essentially in international banking and related services conducted by National and Grindlays. In 1971, the government purchased 50% of the shares in the Mombasa Oil Refinery. In each of these cases, handsome compensation was paid to the expropriated owners.[16] In most other cases in which the government took over shares in private business, it did so because it was invited by the enterprises in order to provide funds or to save an enterprise from liquidation.[17] In new investment projects, particularly those involving foreign investors, the government has been steadily increasing its participation. This increased public ownership of productive resources is, however, not aimed at displacing private

enterprise. Its objective is primarily to attract foreign capital into the country. It is worthwhile noting here that these enterprises do not exactly fall into the category covered by the government's explicit criteria for nationalisation outlined above.

B POLICY ON PRIVATE FOREIGN INVESTMENT

"It is the policy of the Government to welcome private foreign investment."[18]

Private foreign investment constitute a substantial proportion of total private investment in Kenya. It occupies a dominant position in large scale industries that rely on relatively advanced technology. At independence in 1963, there was a general feeling of insecurity in private foreign investment circles. They were not sure whether or not the government of independent Kenya would really welcome or adopt a hostile attitude towards them. The government wasted no time in assuring them a warm welcome and a bright future. It declared the prime need of the country to be rapid economic growth in which private foreign investment would play a key role. It expected such investment "to be a growing sector rather than a shrinking one".[19] Indeed, as Kenya expanded its industrial sector after independence, its reliance on private foreign investment increased. This

reliance is reflected in the role assigned to such investment in national economic development. For example, private foreign investment was expected to contribute 52% of the foreign exchange requirements for financing the 1970-74 five year development plan.[20] In the 1974-78 plan it was expected to contribute over 10% of the country's entire capital formation.[21] In manufacturing, over 50% of expected new investment for 1967-73 was in eight projects all managed and controlled by foreign firms.[22] Table 4 shows the estimated book value of private foreign investment in 1972, the latest year for which such tabulated statistic is available to the author.

The heavy presence of foreign firms in Kenya is not restricted to the industrial sector alone. It is also a significant feature in the tertiary and primary sectors of the economy. In banking for example, Barclays and the Standard Bank, both foreign-owned, together handled over 50% of banking business in 1977.[23] In agriculture, the mainstay of Kenya's economy, foreign capital is still present though not as dominant as it was at independence. It has coffee, tea, pineapple etc. estates and processes agricultural products. It also dominates in the supply of agricultural inputs. The three main inputs in agriculture - fertilizers, agricultural chemicals and fuel, are all supplied almost exclusively by subsidiaries of foreign firms. These three inputs alone accounted for 55.8% of all material inputs into agriculture in 1972.[24]

Table 4 Estimated Book Value of Foreign Investment in Kenya in 1972

Country	K£m.	% of Total
UK	87	67
USA	26	20
Germany	6	5
France	5	4
Japan	1	2
Total	130	100

Source: S. Langdon, 1976 p.136

The prominence of foreign firms in such major sectors of the Kenya economy is in response to Kenya's open door policy towards foreign investment. It has been the policy of the government to encourage foreign investors to set up business in Kenya. The attraction of foreign investment is seen as an essential factor in the country's economic development. For example, the 1970-74 Development Plan emphasised the need to attract more private foreign investment than the country had done so far.

> ... the success of the plan will also depend in part also on the ability of the country to attract private overseas capital ... so as to cover the remaining balance of payments gap. Overseas investment in the private sector must be significantly higher in the next 5 years than it has been in the past 5 years.[25]

The 1979-83 plan promises foreign investors that

> ... Government will continue to maintain that open door policy to foreign capital. Foreign investment will be encouraged particularly in priority industries....[26]

The Vice President and Minister for Finance recently assured firms that

> ... Kenya would continue to be a haven for foreign investment...[27]

He summarised the government's past and present strategy for industrial development as having

> ... been based primarily on import substitution and on the need to attract foreign capital and technology.....[28]

In the 1979-83 Development Plan, the government outlines its industrial development policy.[29] It comprises of three industrial policies one of which is stated thus

> 7.24 Encouragement of Foreign Investment
>
> As in the past, the Government will continue to welcome foreign investment and to provide adequate measures to safeguard such investments.[30]

It is clear that encouragement of private foreign investment has been and continues to be a significant factor in the formulation of the government's economic policies. This desire to attract foreign investments promoted the government to formulate legal safeguards for private foreign investment in addition to those contained in the constitution.

C SAFEGUARDING THE INTERESTS OF PFI

Foreign investors are usually concerned with three major aspects of host countries' investment policy. Viz. the potential for making adequate or even excessive profits; expropriation of private and in particular, foreign investment; and the limitation placed on repatriation of funds abroad. Kenya has provided adequate opportunity and potential for profit making through its economic policies as well as adequate legal safeguards against non-economic risks to private foreign investors. It is to a consideration of these that I now turn.

(1) Potential for making adequate profit

A primary objective of private foreign investment is to make adequate profit from their operations. Unless they have the chance of making profits, no amount of legal or other safeguards would induce them to venture into the country. The profitability of any economic operation depends on various factors which include its productivity, marketing skill, available effective demand for its products, the level of taxation, the degree of competition etc. All these and many others can be affected by government economic policies. Since independence, the government has pursued three major incentive policies that have so far ensured foreign investors good chances of making profit. The first is the creation of a general environment conducive to profit earning by private investors be they local or foreign. The second is to give all investors in similar circumstances standard incentives. These include a 20% investment allowance plus depreciation allowances given to all investors, local or foreign, under the provisions of the Income Tax Act,[31] a 20% export compensation for certain specified exports given under the Local Manufacture Export Compensation Act.[32] These reduce the cost of production in the case of the investment allowances and operate as subsidies in the case of the export compensation scheme.

The third and perhaps the most important policy to foreign investment is the tendency by the government to provide

certain valued privileges to individual firms. These privileges may involve protective measures and or exemptions from certain statutory obligations. The key factor about these privileges is that they are granted by the government on an individual basis following individual negotiations. This means that it is up to the individual investor to negotiate for privileges he feels are to his best advantage with a view to maximising his profits. These privileges are incorporated in agreements with the foreign investors as terms of contracts. The following are some of the privileges that have been obtained from the government by various foreign investors through such negotiations.

- duty-free imports of machinery, industrial inputs etc.
- exclusive licence to produce certain products for a period ranging from seven to twenty five years.
- exemption from price controls.
- sole manufacturing and/or importing rights.
- exclusive rights to supply all government's departments.
- provision of essential infrastructure at no cost.
- permission for extensive use of expatriate personnel.
- exclusive management and technical services supply.
- Operation of external accounts.

To the foreign investor, this individual approach means that he can insist on being granted the privileges that suit his objectives and strategies best. For example,

to one who has a good opportunity of engaging in transfer-pricing, an exemption from import-duties, an exclusive right to supply machinery and services, and an exclusive export marketing right, would immensely improve his chances of making excessive (undeclared) profits through transfer-accounting. Thus a foreign investor's ability to bargain for concessions may determine his potential for making profits - declared and hidden. There is also the added advantage that should any privileges obtained not prove sufficient to guarantee adequate profits, the foreign investor can always go back to the government and negotiate for more privileges. These may be entirely new ones or improvements on existing ones. Thus the textile industry, for example, led by a leading firm has been able to obtain both new and improved privileges from the government. When such a system is in operation and the government itself admitting to being too eager to grant concessions to foreign investors,[33] the prospects for making handsome profits could hardly be better assured. Recent government rhetoric contained in both the 1979-83 Plan and Sessional Paper No. 4 of 1980 suggests that the government intends to do away with the case by case approach. However, this strategic policy shift appears, as far as the author is aware and as of December 1981, not to have been implemented.

(2) Legal Safeguards Against Non-economic Risks

Legal provisions for the protection of foreign investment, although by themselves not very useful unless backed by government willingness and ability to adhere to them, are usually a good index of government attitude towards such investment. It is primarily to demonstrate their welcime for foreign investment that many host countries have enacted laws intended to protect such investors.[34]

Private foreign investors are not only concerned with the existence of laws guaranteeing them the inviolability of their property rights, but also with laws that govern the regulation of business operations in general. Such laws include, for example, customs laws, industrial licensing laws etc. In Kenya, however, the application of such business regulation laws is at the discretion of the government which has proved itself willing to grant exemption on an individual basis.

There are three main legal instruments that guarantee the rights and interest of private enterprise to operate its business without undue government interventions. First, there is The Constitution[35] which guarantees the principle of inviolability of private property. This covers both domestic and foreign capital. Second, there is the Foreign Investment Protection Act[36] which deals specifically with foreign investments. Finally, there exists a regime of bilateral investment guaranty treaties between Kenya and capital exporting countries. These too deal exclusively with foreign investment. In the discussion of these three regimes of legal protection, I consider the guarantee they offer in matters concerning expropriation and repatriation of funds abroad. These are the two main components of non-economic risks faced by foreign investment.

(i) The Constitution

In the late 1950s, two important political facts became clear to the foreign community in Kenya and the British colonial regime. The first was that the people of Kenya, even after the murder by the British of their leading freedom fighter,[37] would never settle for anything less than full political independence from British colonialism. The second was that the British military machine would not hold out for ever against the peoples' assault on this bastion of the colonial power. Having realised that political independence was imminent, the foreign community was gripped by fear that an independent Kenya Government would expropriate their property, most of which they had expropriated from the native peoples of Kenya anyway. The colonial government which had presided over and provided the firepower for the robbery, euphemistically referred to as alienation, from the native people of their rights and interest[38] over the country's natural resources also shared the foreign community's fears. Its response to this fear was the inclusion, in the country's independence constitution,[39] of an extensive chapter on fundamental rights. This chapter is a manifestation of both the settler individualistic philosophy that dominated Kenya politics in the colonial era[40] and the fears about their future in Kenya. Commenting on these fears, Professor S. A. De Smith observed that

> ... the acute anxiety that many members of the European community ... feel for their future in Kenya is reflected in the unusual tightness and scope of the constitutional provisions in that country.[41]

The end result, as far as private property is concerned, was a constitutional guarantee of the sanctity of private property with few very stringent exceptions. It is ironical that the colonial power should have insisted on such legal guarantees when her 70 odd years rule over the country was based on the denial of even the most basic of human rights to the non-European peoples of Kenya.[42]

The Constitution declares one of the fundamental rights every person is entitled to as being

> ... protection ... from deprivation of property without compensation.[43]

The section "refers to every person in Kenya" and the term 'person' includes any body of persons, corporate or unincorporate.[44] This would seem to grant equal protection against expropriation without compensation to all property owners including non-citizens. It is important to note that the Constitution refers to 'deprivation of property without compensation'. It is, therefore, not an absolute guarantee against expropriation although it provides an absolute guarantee (legally) of compensation. It would appear that its drafters envisaged the possibilities of situations where retention of some private property cannot or would not be guaranteed. The substantive section on this subject narrowly

circumscribes such situations[45] and the government has been very wary of using the exceptions to the rule that encroach on, albeit legally, the sanctity of private property.

Section 75 (1) of the Constitution makes expropriation of private property conditional upon the fulfilment of three mandatory requirements. First, the expropriation must be necessary in the interest of one or more factors such as defence, public safety, public morality, public health etc. or the development or utilisation of any property in such manner as to promote the public benefit. Second, the necessity of such an expropriation should be such as to afford reasonable justification for the causing of any hardship that may result to any person having an interest in or over the property. Third, provision must be made by the law authorising an expropriation for the prompt payment of full compensation. These three conditions are cumulative. In addition, the section provides two other safeguards to the owners of expropriated property. It prohibits any barring of

> ... any person who is entitled to compensation ... from remitting within a reasonable time after he has received any payment of that compensation ... to any country of his choice.[46]

Such remission has to be allowed free from any deduction, charge or tax made or levied in respect of its remission. This provision is of great interest to foreign investors for

it in effect requires any compensation to be effective by virtue of being made repatriable. If it has to be repatriable, it must, therefore, be in convertible currency. Finally, the constitution grants the owner of expropriated property a right of direct access to the High Court. The High Court is empowered to determine such person's interests or rights, the legality of the taking of possession or acquisition of the same and the amount of compensation payable. Such access is also available to obtain prompt payment of agreed compensation.

On the face of it these provisions would seem to confer adequate protection to owners of private property. However, on closer examination of the provisions, the protection by them appears to be, at best, uncertain until tested in the courts. The protection they afford would depend, to a large extent, on statutory interpretation of some vague terms such as 'public benefit', 'reasonable justification' 'necessary' etc. The term 'public benefit', for example, would appear to be sufficiently wide to cover a wide variety of expropriations. Would it not be to the 'public benefit', for instance, if the government expropriates land belonging to a private company for distribution to landless masses in order to forestall social and political upheavals? Would it not be to the 'public benefit' to expropriate a foreign company in order to save or even earn foreign exchange and/or to earn revenue with which to provide basic services such as health facilities to the public?

The author would readily argue that it would be unreasonable and illogical for any court to hold that a measure that benefits the public financially, materially or even one that provides intangible benefits is not to the public benefit.

In relation to foreign investment in particular, it is arguable that the attainment of the government's stated objective of attaining economic independence[47] is in the public interest and therefore a public benefit. Any argument to the contrary would, it is submitted, find it hard going proving that foreign economic domination of a nation is in its own interest. Such issues will have to await determination by the courts in Kenya should they ever arise.

In the only case brought and determined under the provision of S.75 of the Constitution since independence,[48] none of these issues arose for consideration. However, Chanan Singh, J. while outlining the provisions of S.75 (1) observed that

> ... No special attempt has been made to show that acquisition was for development or utilisation for "public benefit" but it seems to be accepted that the acquisition of land for the purpose of settling squatters on it would be for public benefit.[49]

This appears to be a reasonable interpretation and one that may have wide support among the mass of landless Kenyans.

(ii) The Foreign Investment Protection Act (FIPA)

This Act was enacted in 1964 "to give protection to certain approved foreign investments".[50] It is the only legislation, in the history of independent Kenya, aimed exclusively at foreign investment. Its enactment was prompted by two main factors. The first of these factors was the need to improve "the climate of confidence so necessary to attract new private capital".[51] The uncertainties prevailing in the private sector at independence had led to a fall in the flow of private foreign investment and an increase in the outflow of capital. Table 5 shows the trend in the balance of payments over the years 1957 - 1968. The government was anxious to assure foreign investors that their investment was not in jeopardy and therefore improve their confidence. The primary method it chose was the enactment of FIPA. Its aims were to attract more foreign capital and to reduce the level of capital outflow from the country. The second of the factors that led to the enactment of FIPA was the pressure from the World Bank for the government to manifest its policy of welcoming foreign investors. The Bank's mission to Kenya in 1962 had emphasised that

> ... It is clearly to the benefit of Kenya that foreign investment should be encouraged in the future and the mission considers that demonstration of a favourable attitude on the part of the independent Government of Kenya towards overseas capital would be an appropriate and necessary measure to attract funds.[52]

Table 5 Net Inflows of Long-term Capital and Net Outflows of Investment Income 1957-68

K£'000

	Net inflow of capital	Net outflow of income	Retained earnings after tax, foreign investment	Total net inflow
1957	1,119	5,360	-	-4,241
1958	650	5,450	-	-4,800
1959	375	7,016	-	-6,641
1960	5,642	7,283	-	-1,821
1961	-5,133	5,341	-	-10,474
1962	-2,696	4,845	-	-7,541
1963	9,800	9,843	3,514	-43
1964	10,800	8,665	3,546	2,135
1965	8,800	8,731	3,019	69
1966	2,100	8,750	2,800	-6,650
1967	4,100	9,170	4,400	-5,070
1968	9,000	9,590	5,000	-590

Source: Lal, 1975, P.183

Notes: (a) net increase in long-term liabilities (represented by equity capital, loan and debenture capital, and retained profits after tax)

(b) net outflows of dividends and interest, and retained earnings after tax.

The mission felt that Kenya would continue to depend on external assistance for some time after independence and, therefore, strongly recommended that the Government issue a clear statement of policy towards private investment. It suggested that

> ... This might include reassurances about interference by the state with private undertakings. External investors will be concerned about freedom to transfer earnings and repatriate original capital. [53]

It is possible too that the British government which was to supply most of the overseas aid to Kenya may have put some pressure on the Kenyan government to follow the World Bank Mission's recommendations. At that time, the major foreign investment projects in the country were almost entirely British. The Act offers assurances to foreign investors in matters concerning repatriation of fund and expropriation of property.

Under the Act, a foreign national who proposes to invest foreign assets in Kenya may apply to the Minister for Finance for a certificate declaring the enterprise in which the assets are proposed to be invested, or have been invested, an approved enterprise.[54] The issuance of the certificate, referred to in the Act as Certificate of Approved Enterprise (CAE), depends upon the discretion of the Minister. Before exercising his discretion in favour of granting the CAE, the Minister has to satisfy himself that the enterprise would further the economic development

of Kenya or would be to the benefit of Kenya.[55] In considering an application for a CAE, he consults one or more of five specified ministries depending on the type of project involved.[56] The term "economic benefit" has been interpreted to mean any investment that would

- Lead either to an earning or saving of foreign exchange;
- result in a gain of technical and skills to the country;
- result in an increasing in the economic wealth and the social stability of the country by raising the national income or promoting the diversification of the economy.[57]

If a foreign investor's project meets these conditions, the CAE issued to him brings him under the provisions of FIPA.

A CAE entitles its holders to two types of protection afforded by the Act in relation to repatriation of funds and expropriation of capital. The Act guarantees a holder of CAE permission to transfer out of Kenya, in approved foreign currency and at the official exchange rate, the following:

(a) The profits, after taxation, arising from or out of his investment of foreign assets

(b) The capital specified in the CAE or representing and being deemed to be the fixed amount of the equity of its holder in the enterprise for the purposes of the Act: and

(c) The principal and interest of any loan specified in CAE[58]

Prior to 1976, it was not clear whether or not capital gains were profits for the purposes of the Act. The Capital Issues Committee, which approves such transfers, had treated them as as qualifying for repatriation under S.7 (a) in certain cases and refused to allow this in others. However, the Act was amended and now capital gains are deemed not to be profits arising from or out of the investment for the purpose of the Act.[59] They are therefore not remittable as of right. Their remission schedule has to be negotiated for with the Central Bank. This amendment was aimed at conserving foreign exchange by limiting remission of funds arising from speculative dealings on the stock exchange, and also to encourage re-investment of such capital gains. The Central Bank argued that this was consistent with the original guarantees offered by FIPA on repatriation of funds.

The freedom to transfer funds abroad granted under the Act is available to holders of CAE "notwithstanding the provisions of any other law for the time being in force".[60] This is no doubt with reference to the Exchange Control Act[61] which imposes some strict restrictions on the remission of funds abroad. However, all dealings in foreign currency are subject to approval and supervision by the exchange control authorities.

The protection against compulsory acquisition is a re-iteration of S.75 of the Constitution the Act simply providing that

> No approved enterprise or any property belonging thereto shall be compulsorily taken except in accordance with the provisions of the Constitution.[62]

S.75 of the Constitution is incorporated into the Act as a schedule thereto.

The government considers FIPA as "the major instrument for the protection of foreign investment in Kenya".[63] So too do the foreign investors interviewed by the author and also some major financial institutions.[64] Clearly the Act provides some very vital freedom in repatriation of funds which the constitution is silent about. As of today, it symbolises the very favourable investment policy on foreign investment that has prevailed in Kenya since independence.[65]

(iii) Investment guaranty agreements

In addition to the protection offered to foreign investors under national law i.e. the Constitution and FIPA, the Kenya government has entered into several bilateral treaties with capital exporting countries[66] aimed at further reassuring foreign investment. These treaties deal with matters such as standard of treatment, guarantees on property rights, currency restrictions, settlement of disputes etc. Under the terms of such treaties the capital exporting country acquires a right to guarantee any investment by its nationals in Kenya provided such investment has been approved by the Kenya government. The effect of such treaties is to impose treaty obligations on the host country

undertaking to abide by the terms of the treaty in its treatment of investments covered by any guarantee by the capital exporting country. The USA/Kenya treaty, for example, provides that

> The Government of the US shall not guaranty any investment in Kenya unless the Government of Kenya approves the activity to which the investment relates and recognises that the Government of the US may guaranty such investment.[67]

Once Kenya has issued an investor with a CAE, he receives a certificate for presentation to his own government for purposes of obtaining a guarantee from that government in accordance with the treaty provisions.[68] Kenya is then bound to recognise the rights of that other state (against her) as guarantor to the investment. The treaties give full subrogation rights to the guarantor to the claim of the foreign investor against the Kenyan government once he has fulfilled his guarantee obligations. The subrogation clause in the West Germany/Kenya treaty, for example provides that

> If either contracting party makes payment to any of its nationals or companies under guarantee it has assumed in respect of an investment in the territory of the other contracting party, the latter contracting party shall ... recognise the assignment, whether under a law or pursuant to a legal transaction, of any right or claim from such national or company to the former contracting party as well as the subrogation of that ... party to any such right or claim, which that ... party shall be entitled to assert to the same extent as its predecessor.[69]

Notice the deceptive expression of mutual obligations as if the flow of investment were into and from both countries.

The treaties also provide for national treatment of the investors of the signatories within their boundaries.[70] However, the Kenya Government has reserved the right to depart from its obligation to accord national treatment to the other party's investors where this is necessary to correct historical imbalances caused by the colonial regime's discriminatory economic policies against Kenyan native nationals.[71] They also provide for protection against expropriation. Usually it is stipulated that the investments by nationals of either party are not to be expropriated except for public benefit and then only with adequate, prompt and effective compensation. The terms usually repeat the guarantees in the Constitution discussed earlier in this chapter.[72] In effect, where such treaties exist, the protection offered to foreign investors is governed not only by national laws but also by the treaties.

The protection offered by such treaties may be of some vital importance in case of a change in national laws. Both the Constitution of Kenya and FIPA can be amended by the government with ease should it want to do so.[73] Thus the protection offered by national law is to a large extent at the discretion of the government. Its treaty obligations, on the other hand, are not as easy to shake off without some

form of repercussions.[74] Again these treaties confer rights vis - a - vis the Kenya government from which it cannot easily withdraw while the constitutional guarantees may be regarded as privileges to foreign nationals that could rightly be withdrawn. Indeed, it is possible that the government holds such a view. While discussing the government's policy on Kenyanisation, the 1970-74 plan seems to take the view that while constitutional guarantees are a right to citizens, they are privileges to non-citizens. Thus it states

> The Constitution of Kenya guarantees equal rights to all citizens and the KANU Manifesto states that citizens will have the right to follow the profession and trade of their choosing and to own property .. When these same perquisites are extended to non-citizens, however, they become privileges and not rights. The government may grant privileges to non-citizens, but always with the understanding that they may be withdrawn should it be found necessary or useful in terms of national interest.[75]

When the host government appears to hold such views, protection given by means that are in its exclusive discretion to change may not be said to be founded on very solid ground.

The treaties provide an important procedural advantage to foreign investors covered by them in matters concerning compensation. It is a settled rule of international law that a state may not take up a claim on behalf of its national against a foreign state, unless that national has exhausted all local remedies available to him under the

municipal law of that foreign state.[76] Under these treaties, a foreign investor does not have to fulfil this procedural requirement as all he has to do is to recover indemnity against his government or its agent for his losses under the term of the guarantee. There is no provision in the treaties requiring the foreign government to exhaust local remedies. Once the guarantor government has made good the loss of the insured private investor, it then steps into his shoes and claims reparation for any damages in its own right on a government basis.[77] Also, the effectiveness of any remedy available through the investor's municipal courts may be severely limited by the defence of sovereign immunity[78] or the act of state doctrine. Thus in Banco Nacional de Cuba v Sabbatino[79] the US Supreme Court held that in the absence of a treaty or other agreement, American courts would not question the taking of property within its own territory by a sovereign government recognised by the U.S.

D POLICY ON THE CONTROL AND REGULATION OF PRIVATE FOREIGN INVESTMENT

Although the government actively encourages private enterprise, both domestic and foreign owned, it has nevertheless reserved the right to regulate the nation's economic activities. Thus the 1966-70 plan declares that

> The plan envisages that various forms of ownership will be permitted and encouraged but in all cases the state retains the right to plan and control the uses of resources and to limit the excessive accumulation of wealth. Indeed, the planning and control of resource use are the principal tools for managing the nation's economy.[80]

The 1974-78 Plan restates this position and gives an indication of the possible form such controls may take. It states that

> The ultimate power to guide and control the use of all resources is declared to belong to the state. The range of control is wide and can take either direct or indirect form .. Even when ownership is entirely private, some Government controls or intervention may be appropriate.[81]

Private foreign investment, being part of the economy is clearly subject to the government's powers of control and regulation. The question is what approach the government takes in the regulation of foreign investment. Here I am concerned with broad policies and not specific measures in response to particular incidents. On the whole, the government has rejected the idea of formulating a comprehensive system of legislation on the regulation of foreign investment setting out terms and conditions for operating such investment in the country. It has chosen to try and accommodate foreign investment within the framework of the nation's private enterprise. Its attitude towards this is that

> There are ... no rigid or doctrinaire views for ... the degree of Government control

> that ought to be exercised on private enterprise. The approach being followed is both flexible and pragmatic.[82]

There are three main approaches that the government has adopted in what it sees as its 'flexible and pragmatic' regulation of foreign investment. Viz

(i) an ad hoc system of project approval prior to their establishment;

(ii) A Kenyanization process; and

(iii) Financial and fiscal regulation.

These approaches are considered in detail in the next three chapters and, therefore, I need not say any more about them here.

E CONCLUSION

In this chapter I have discussed private foreign investment within the overall framework of private enterprise in general. This approach has been necessitated by the fact that government policy on foreign investment has developed from that on private enterprise. The encouragement of private foreign investment has become imperative because the government had ruled out public ownership as the only basis of economic development. Having chosen to rely, rather heavily, on private enterprise to achieve the targets set out in its development plans, the government had little choice but to allow in and even actively attract private foreign investment.

There simply was not enough domestic private capital to help attain the ambitious goals set for economic growth.

Encouraging private foreign investors to set up businesses in the country has been a prime object of government economic policy. To achieve the objective of attracting more private foreign capital into the country, the government has adopted an open door policy towards such investment. This policy has entailed the granting of vital privileges to foreign investors on an individual basis and the provision of rather favourable legal machinery for the protection of such investments. The government has been very liberal in its dealings with foreign capital.[83]

This chapter has outlined the major legal protection offered to foreign investors. It has argued that protection against economic risks has been achieved through the ad hoc individual treatment and that the legal protection machinery is aimed primarily at what are generally referred to as political risks. It has been shown that the Constitution, FIPA and bilateral treaties with capital exporting countries may possibly have certain shortcomings owing to possible difficulties in the interpretation of certain terms. In addition, the government may change the relevant legislation at its discretion.[84] All this would seem to suggest that the guarantees offered by these national legislations may not be watertight. While this may be so from a legal point of view, it has not been so in reality. The existence of

foreign investment in the last eighteen years and its increase over the period would seem to suggest that foreign investment is satisfied with these guarantees. Even more important, to take advantage of the loopholes afforded by the laws involved, the government would have first to discard its policy of attracting foreign investment. As long as the government is committed to attracting foreign investment and to a non-nationalization policy, there is little likelihood that it would take advantage of any available legal loopholes if such a move would alarm foreign investors.

The government recognises the need to regulate private enterprise both domestic and foreign. With regard to foreign investment, this regulation must take into account the need to achieve the government's stated objective of economic independence on the one hand and that of attracting supposedly needed foreign investment. As the government is fully committed to an economy in which private enterprise plays a major role, then the objective of economic independence must of necessity mean independence from foreign domination. It has been stated that

> The heavy dependence of development in Kenya on sources of foreign capital is a matter of legitimate concern.[85]

It would thus be naive for the government not to take into account this concern in the formulation of its regulatory policies. How the government has sought to regulate the

activities of private foreign investment within the scope of its stated policy of encouraging such investment is the subject of consideration in the following three chapters.

N O T E S

1 1966 - 70 Development Plan, 13

2 The G D P grew at a cummulative rate of 6.8% over the period 1964 to 1972. In absolute terms this was 69%. Capital formation rose by 150% in absolute terms over the same period. (Source 1974-78 Plan, 43 and 47).

3 Various Kenya studies have arrived at this same conclusion. These include: I L O, 1972, 11 and 85; Colin Leys, 1975, 60, chapters 3 and 4; A Hazlewood, 1979, 13; Kaplinsky, 1978, 2.1; G Wasserman, 1973, 148 where he observes that "The Kenya political economy was altered only so as to facilitate its transition. The question of transformation of the colonial system was answered by never being posed".

4 Sessional Paper No. 10 of 1965 (SP 10/65).

5 Every subsequent plan, policy statement etc. has re-iterated and re-emphasised its commitment to the principles laid down in this paper.

6 SP 10/65, 17

7 Ibid, 16

8 Kenyatta, 1968, 147

9 e.g. In the 1974-78 and 1979-83 Development Plans, 279 and 79 respectively.

10 1966-70 Plan, 235-6

11 See SP 10/65, 26

12 A Seidman , 1972, 91

13 SP 10/65, 27

14 Ibid

15 The government purchased the remaining 40% in 1976.

16 See C Lubar, 1971, 119-120

17 An example of the first type is the E. A. Portland Cement Co, Ltd. while of the second type is KENATCO Ltd.

18 1979-83, Plan, 30

19 SP 10/65 p.14. Notice also that this was in conformity with the IBRD Mission's recommendation that "emphasis should be placed on measures likely to improve production rather than welfare projects".

20 1970-74 Plan pp 101 - 102

21 1974-78 Plan p 159

22 See 1970-74 Plan pp 308 - 340

23 Steven Langdon, 1976, 85. Since then several new foreign banks have been established in Kenya while an agreement between the government on the one hand and Barclays and Standard banks on the other, to merge the two with the government holding 50% of the shares of the resulting merger has yet to materialize.

24 Economic Survey, 1974. This figure has most likely increased since then owing to inflation and the devaluations of the Kenya Shillings as well as increased modernisation in farming methods.

25 1970-74 Plan p 17

26 1979-83 Plan p 335

27 Speech by V-P and Minister for Finance during an inauguration ceremony of the extension of the cement works by the E. A. Portland Cement Co. Ltd., a joint venture by the Kenya government with foreign capital. The Weekly Review 28.3.80 p 23

28 Budget Speech 19.6.80 p 4 See also 1979-83 pp (iii), 30, 96, 332 and 343 for example.

29 1979-83 Plan p 332

30 Ibid. The other two are: developing a mixed economy and encouraging geographical dispersion of industries.

31 Cap. 470, Laws of Kenya - 2nd Schedule. A special 40% allowance, known as a shipping investment allowance, is given for purchases of new ships in excess of 495 tons.

32 Cap. 482, Laws of Kenya

33 See for example, Budget Speeches, 1972, 4; 1973, 7 and 8; 1980, 4, 6 and 7; 1981, 6 and 8 and Development Plan 1979-83, 28

34 See for example Burundi, Investment Code 6.8.63; Ethiopia, Investment Code, 1963; Uganda, Foreign Investment Protection Act, 1964; Tanzania, Foreign Investment Protection Act, 1965; Liberia, Investment Incentive Code, 1966 etc.

35 Act No 5 of 1969

36 Cap. 518, Laws of Kenya

37 Field Marshall Dedan Kimathi.

38 Cf. Chapter 1

39. Kenya Independence Order in Council, 1963

40 These seem to have been successfully inherited by the ruling oligarch of post-independent Kenya.

41 De Smith, S. A., 1964, 195

42 The lie to the apparent guarantees such as the Devonshire White Paper, 1923; The Native Lands Trust Ordinance; The Masai Treaties, 1904 and 1911 etc., is starkly exposed in a letter written by a Governor of Kenya, Charles Elliots, to the Colonial Secretary in which he states

> "No doubt on platforms and in reports we declare we have no intention of depriving natives of their land, but this has never prevented us from taking whatever land we want - Your Lordship - I think it is well that in confidential correspondence at least, we should face the undoubted issue viz white mates black in few moves". (Quoted in G. K. Kamau "Kenya Land Policy and Land Control Act, 1967". University of Nairobi (Memio), 160). (emphasis added)

43 S. 70

44 SS. 70 and 123 (1) respectively.

45 S. 75

46 S. 75 (4)

47 See for example 1974-78 Plan p 34 where it is stated that "The fundamental objective of the KANU Government is to achieve economic independence for Kenya". See also S P 10/65,

48 New Munyu Sisal Estates Ltd v A. G. H.C.C.C. No 320 of 1969

49 Ibid, 1.

50 Preamble to the Act

51 1964 Economic Survey, 11

52 IBRD, Economic Development of Kenya 1962, 38.

53 Ibid p 44

54 FIPA S. 3(1)

55 Ibid. S. 3(2)

56 Rules of Procedure made under S. 9 of the Act, Rules (a) 1 - 4.

57 C G Lubar 1971, 168. See also Tom Mboya, 1969, where he says that

> "The benefit that a country derives from private foreign investment must be judged by the contribution of such investment to output, employment, supply of skills and other scarce resources such as foreign exchange, and the generation of training opportunities and experience for citizens. Foreign investment in the form of an enclave that does not affect the incomes and skills of Kenyans, cannot be accepted.. the overriding criterion in assessing the benefits from foreign investment should be the magnitude of gains accruing to Kenyans". (at p 201). Mboya was the Minister for Planning and Economic Development under whose jurisdiction foreign economic advisors formulated much of the economic policies adopted by the government at independence.

58 FIPA S. 7

59 See Act No 7 of 1976

60 FIPA S. 7.

61 Cap. 113 Laws of Kenya

62 FIPA S. 8

63 1979-83 Plan, 335

64 See for example, Lloyds Bank's Overseas Department Economic Reports, the Kenya series.

65 This is the view expressed by two senior government officials and one parastatal official during interviews with the author. See also IBRD, 1975, 308

66 These include the USA, UK, Netherlands and West Germany.

67 Agreement between the US and Kenya: Guaranty of Private Investments, signed March 19, 1964. ILW II: 4A - 5 1

68 See rule (f), FIPA Rules

69 Treaty between W. Germany and Kenya Concerning The Reciprocal encouragement and Reciprocal Protection of Investment signed December 4, 1964. ILW: 4B - 5.1

70 Ibid Clauses (a) and (b)

71 See for example, Ibid, Clause (7)

72 See for example, Ibid, Clause (b)

73 Only a simple majority of those present and voting is required to amend any provision of FIPA while ammendment of the constitution requires a 2/3 majority. It is not a difficult task for the government to obtain the relevant 2/3 majority in a parliament that is composed of 100% KANU members and that refers to itself as a KANU government. In addition, 54% of the parliament is made up of Ministers and their assistants who are therefore supposed to back up the government. Despite the ability of the government to amend the constitution, private foreign investment can take heart from the fact that so far the government has used this ability almost exclusively to oust from parliament and government opponents of private enterprise and in particular foreign capital. It has also used its powers under The Preservation of Public Security Act, to incarcerate the most vocal critics of its economic policies.

74 Kenya is heavily reliant on aid from these countries: See Holtham and Hazlewood, 1976.

75 P. 10 (emphasis added)

76 See Zouhair A. Kronfol, 1972, 124

77 The agreement with the US for example, provides that any such claim is to be the subject of negotiations between the two governments and is to be settled in so far as is possible in such negotiations. See also Nwogugu, 1965, 107: Corfu Channel Case, (1949) ICJ Reports, 4.

78 See Chemical Natural Resources v Republic of Venezuela 1966 South Atlantic Reporter Vol. 215, 84. Also The Underhill Case US 168, 250.

79 US 376, 398.

80 Introduction by Minister for Economic Planning and Development P.ix (emphasis added)

81 P.6 (emphasis added). The use of the words "is declared to belong to the state" would appear to be in reference to SP 10/65 which states that "Under African Socialism the power to control resource use resides with the State". (p.11)

82 1974-78 Plan, 7

83 See Deepak Lal, 1975; S. Langdon, 1976; ILO, 1972 J Carlsen, 1973 etc.

84 The 1976 amendment of FIPA declaring capital gains not to be profits for the purposes of the Act would seem to underscore the ability of the government in these matters.

85 1966-70 Plan 14

CHAPTER THREE

REGULATION OF THE ESTABLISHMENT OF FOREIGN INVESTMENT

The regulation of the establishment of foreign investment in Kenya does not lend itself to easy examination or classification. Anyone looking for legislation that specifically applies to the establishment of such enterprises in the country is bound to be struck by its scarcity. The basic business legislation in the country such as the Companies Act, the Banking Act[1] etc. do not apply to the establishment of any specific type of enterprise, domestic or foreign, but to the establishment of enterprises in general. Even where they deal specifically with foreign enterprises it is in the form of formal or procedural details e.g. the definition of a foreign company.[2] Such formal regulation usually applies only in situations where a foreign enterprise enters Kenya and establishes an entity in the form of a company or a place of business.[3] This chapter is not concerned with such formal requirements, but with regulations that deal with substantive aspects of foreign investment. Such regulation may define the areas - sectoral and/or geographical - in which such investment should establish as well as laying down the terms and conditions for admitting the investment. The terms and conditions laid down for any particular investment should (in theory) largely depend

on and reflect the government's economic development policy and the specific objectives of the particular project in question.

It was not easy to differentiate merely administrative from regulatory machinery. The machinery selected from the myriads of bureaucratic procedures was that which the author felt had potential or actual regulatory effect or was likely to be a foundation for any regulation contemplated by the government. Two main stages of the regulation of the establishment of foreign investment in Kenya are discussed in this chapter. These are the project (or proposal) evaluation and the negotiation stages. Before proceeding to the discussion of each of these stages, it is important to point out that the establishment of foreign investment in the country is considered by the authorities on a case by case basis. There is no rigid system of apriori 'dos and don'ts' that have been laid down by the government as conditions for admitting them into the country. Virtually every aspect involved in the participation by foreign investors in economic activities is negotiable on a case by case basis. The hallmark of the entry regulation system is its ad hoc and discretionary characteristics arising from the case by case approach. As stated earlier, recent government rhetoric suggesting an abandonment of such an approach has yet to be translated into practice.

A : PROJECT EVALUATION

1. The Machinery

Prior to 1968, no institutional machinery existed for the evaluation of project proposals submitted by foreign investors. Such proposals received little, if any, scrutiny from the government. In that year, the government created an *ad hoc* interministerial committee to evaluate such proposals and negotiate with the investor. This committee is known as the New Projects Committee (NPC). It is composed of representatives from Treasury, Industry and the ministry under whose jurisdiction a proposed project falls. If any of the parastatal bodies is expected to participate in a project, then it is represented in the committee. Little is said or published about the activities of the NPC. In the 1974-78 Development Plan, it was envisaged that it would be

> the main technical organ through which the Government will administer legislation to regulate the establishment of industrial capacity.[5]

In view of this enhanced role, the NPC was to be given legal status.[6] However, the proposed legislation to require firms to obtain government approval to increase capacity for manufacturing[7] was never enacted and NPC's status remained unchanged. It remained an *ad hoc* committee with neither any clear mandate nor legislation

to enforce or implement. The 1974/75 Plan Implementation Report of the Treasury reported that:

> Enactment of legislation to control productive capacity has not been undertaken. The New Projects Committee does not provide an adequate mechanism for controlling new investments.[8]

Despite the admission of the inadequacy of the existing machinery, nothing has been done about it so far.

The role of the NPC as an evaluation and negotiation body seems to be enhanced in the latest plan which states that:

> The New Projects Committee will co-ordinate the evaluation of all industrial projects. The establishment of new projects as well as the importation of machinery and equipment will be undertaken only on the recommendation of this committee. The New Projects Committee will be gazetted as the agency to approve all new projects. Projects not approved by the New Projects Committee will not be provided the Approved Enterprise Status under The Foreign Investment Protection, nor will they be entitled to any concessions or investment allowance.[9]

If this had happened the NPC would have acquired a legal status vesting it with the authority to vet foreign investment. However, as in the case of the changes envisaged in the previous plan, nothing has come out of the current plan and there is little chance of anything materializing. The approval of non-industrial projects is ultimately the responsibility of the Treasury.[10]

In addition to the NPC the government set up, in 1971, an Industrial Survey and Promotion Centre (ISPC), under the then Ministry of Commerce and Industry whose role includes "evaluation of project studies prepared by the private sector".[11] However, owing to severe budgetary and technical manpower constraints, the Centre has been unable to fulfill this role satisfactorily. In the current plan period - 1979/83 - the government had envisaged the development of the Centre "into the principal instrument for providing consultancy services in industrial development."[12] Its proposed functions under the plan include:

- Continuous study and analysis of the manufacturing sector in order to identify new investment opportunities and prepare programmes to assist in planning the development of the sector.
- Conducting regional studies to help plan for greater geographical distribution for industries.
- Identification of areas for industrial research and subsequent commercialization of research results, and
- Preparation of pre-feasibility and feasibility studies.[13]

It is not clear whether or not the ISPC would conduct such studies in all proposed new projects. Should this be so and the Centre performs its role successfully, this would provide valuable information for use in negotiating with foreign investors where projects have been approved.

2. The Process

Although the NPC has been described as a "a forum for evaluation and approval of industrial projects,"[14] it usually does no more than peruse the investment proposals submitted to it. Where it detects patent shortcomings in a proposal it sends back the proposal to the applicants with instructions to correct these. Where it finds the information in the proposal inadequate to base a judgement on, it sends it back with a request for further information or clarification.[15] Sometimes when it has more than one proposal it compares the two or more proposals although this does not seem to have a great bearing at times on the eventual outcome. The essential feature of NPC's project 'evaluation' is its heavy reliance on information and data supplied by applicants. It has little access to any independent source of information.

Unlike the NPC, the ISPC is not an ad hoc body. It is an established department of the Ministry of Industry with a core of permanent technical staff. This makes it possible for it to carry out a less superficial technical evaluation of the proposals referred to it. This places it in a position of being the only government source of technical analysis of project proposals to the NPC. The ISPC too does rely heavily on the information contained in the proposals in its evaluation.

Not all investment projects have gone through the NPC. Even less are the projects that have been referred to the ISPC. Some projects have been established by foreign investors in Kenya without going through all the established administrative procedures. This is a direct result of the ad hoc and discretionary nature of the system. We shall have more to say on this later. In practice, the evaluation process is hardly ever separate from the negotiation process. Since very little evaluation of any significance takes place outside the negotiation stage, the primary role of the NPC has been in negotiations. What evaluation that has been noted in the projects studied will be discussed under negotiations.

B : THE NEGOTIATIONS

As stated earlier, the establishment of new foreign enterprise in Kenya is considered on a case by case basis. So also is the expansion of existing establishments where such expansion involves injection of new capital from abroad. The NPC is, in theory, the organ that is supposed to conduct the negotiations and approve the projects. However, the NPC hardly ever negotiates or evaluates projects that involve no government participation either directly or through one or more of several parastatal bodies.[16] The 1979-83 Plan does, in fact, clearly recognise this practice for it declares that foreign investors meeting

the specified criteria [17]

> ... and seeking no government participation or special concessions will be free to establish enterprises in Kenya subject to meeting normal regulations.[18]

Normal regulations refer to the legal process applicable to all entities carrying out economic operations in the country[19] as well as the formal application to the Treasury for a CAE. This leaves the NPC to consider mainly the projects that require special concessions or government participation. Special concessions include tax exemptions, duty exemptions, protection through import controls etc. In practice, this apparent limitation is meaningless for virtually all incoming investments require one or both (special concessions or government participation). More often than not it is both.

Negotiations with foreign investors is carried on simultaneously with the consideration of their applications for CAE under FIPA. This also constitutes what is referred to as project evaluation. In reality then the combined processes of negotiation and evaluation are nothing more than a consideration of the investors' applications for a CAE and concessions from the government. Referring to the pre-1975 period, the government admitted that

> ... such projects as were submitted were reviewed by the Government to determine their profitability and their eligibility for certain forms of incentive and protection.[20]

The primary purpose of the reviews or negotiations was, therefore, to consider applications as submitted and recommend means and levels of protection to achieve profitability acceptable to the foreign parties. They had no interest in imposing terms of entry that would produce results consistent with the government's stated overall economic objectives. The government appears to have recognised that such a micro approach to the evaluation of new investment proposals may not necessarily be in the interest of the national economy. It indicated that its role in promoting new industries would undergo a significant change and that in receiving proposed new industrial projects

> ... greater attention will be given to evaluation of projects from the standpoint of their benefit to the national economy.[21]

There is little evidence that this admirable rhetoric has been followed in practice.

Negotiation with a foreign investor is put into motion by an application by such an investor for a CAE. Details of the information to be provided by the applicant are fairly comprehensive.[22] For purposes of this study the author considered the treatment of some of the main categories of project details by the Kenyan evaluators and negotiators. These categories are those that concern project description, project sponsors, project capital cost and structure, project profitability, marketing arrangements, machinery and

technical processes, concessions, and other miscellaneous aspects of projects involved. The performance of the Kenyans in their evaluation of and negotiations over these aspects of investment projects is considered here in the light of the final agreements reached.

1. Project description

The manner in which a project is described in a proposal may make the difference between its appearing as an attractive project and its appearing unattractive to its recipient. It is important for any project evaluator to scrutinise the description of a project for possible omissions or exaggerations in its presentation. The final decision makers, in approving projects' have tended to rely almost entirely on the description provided by applicants in their proposals while ignoring the findings of the NPC, ISPC and other independent sources where such have been critical of some elements of proposals submitted. This has led to the acceptance at face value of projects that have had little chance of success. Some of the projects in which the decisions heavily depended on the description supplied include Ken-Ren Chemicals and Fertilizers Ltd., Kenya Chemical and Food Company Ltd and Pan African Vegetable Products Ltd.

Ken-Ren was a joint venture between the Kenya government and N-Ren Corporation, a US company to set up a fertilizer plant in Kenya. In 1975, N-Ren submitted a financial and technical proposal for an agrochemical complex. The proposal was described in "brief and general terms" and mainly concerned financial aspects of the project.[23] It glossed over vital technical issues and painted a rosy picture of the proposed project. Its description of the benefits of the projects in terms of foreign exchange saving was indeed an insult to the intelligence of the Kenya negotiators.[24] In its technical description it included an additional stage of ammonia manufacture rather than importing the required nitrogen. This alternative had been rejected by all the other eight major applicants and an Italian government mission as non-viable and therefore a non-starter.[25] N-Ren also omitted in its proposals any consideration of the problems and costs related to the substantial amount of effluent - 15 tons per day of fertilizer dust alone - plus other noxious stuff.[26] The ISPC felt that the technical evaluation of the N-Ren proposal as described

> ... depends therefore to a large extent on obtaining confirmation of the performance of such small PFP ammonia plants, particularly in developing countries.[27]

No such confirmation ever materialised and the proposal therefore was to stand or fall on the basis of its own description that left a lot to be desired. It stood as it was for powerful forces in the Kenyan bereaucracy were only too willing to accept the project as described.

The KCFC Ltd. is a joint venture between the government and four foreign companies, two of which are subsidiaries of a Kenya resident magnate. The four foreign companies are the sponsors of the project with the government a holder of 51% of equity. In 1976, the magnate, through the so-called foreign sponsors, submitted to the government a proposal for the establishment of a molasses utilization complex in Kenya. With the proposal he submitted a feasibility study of the same and details of the proposed arrangements for the management of the project.[28] The government, at the decision-making level, accepted all these without question and committed huge amounts of funds to the project. In the description of the project, the very vital issue of raw materials was glossed over and given little prominence, but leaving the government with the contractual obligation of seeing to it that the supply of raw materials was available. In the end the agreement provided that:

> GOK undertakes to arrange the supply to the company of adequate supplies of molasses at reasonable prices and all other local supplies necessary for the company's business.[29]

The government thus was committed to virtually guaranteeing the supply of the raw materials without ever being given a detailed description of the raw materials significance in the project. Although the project is still being constructed, the issue of raw materials is still unsettled and it appears that there may not be enough of them.[30] Also related to the raw material issue, the proposal envisaged the supply

of molasses at 160/= per ton at a time when Kenya molasses sold on the export market for 600/= per ton.[31] Although in this case the proposal's description indicated that it would not be viable without a heavy subsidy in the price of the raw material, the government did not pay adequate attention to this factor.[32] Another very vital factor that was omitted from the project description was the intended end use of the major product - alcohol. No details of its blending with gasoline were given although the joint venture agreement stipulates that

> ... Further, GOK shall procure that the outlets of alcohol sales within Kenya to petroleum companies respectively (sic) end-users shall be arranged.

The use of alcohol for blending with gasoline in Kenya will be dependent entirely on the government enacting legislation to compel the oil companies to blend their gasoline with alcohol. The construction of a blending plant, its location, its cost, the savings in foreign exchange involved (if any) etc. was never raised. The future of the project hangs in the balance and it may never get off the ground.[33]

PVP is a joint venture between two Kenyan parastatals, two foreign firms and an international financial institution in a vegetable processing plant. The present company was set up in 1972.[34] In that year a company known as INHA International Est. (E.A.) Ltd. is said to have

> ... got interested in the project not for any other reason than the commission they would get for selling some equipment for manufacturers.[35]

INHA was then commissioned to look for outsiders interested in financial participation in April 1972. On 19 September 1972, they wrote to the Ministry of Agiculture apologising for the delay in the submission of a proposal adding that:

> ... When all information were (sic!) put together we found that an improvement in the viability of the project was required and consequently have gone back to the suppliers and other parties in order to re-examine the proposal before submission.[36]

A committee set up in 1977 to review the running of the project had this to say about this stated reason for the delay in submission of a proposal:

> We would like to stress the significance of the statement by INHA that an improvement in the viability of the project was required.
>
> ... what we read or understood from this statement is that when they had gathered all available information the project was <u>not very attractive but because they were keen to sell to Kenya a project that was only viable on paper they had to re-examine their figures, cook some of them where necessary, omit information as required just to make the project look viable</u>.[37]

It is significant that this observation was made in the light of the investigation that had been carried out by the committee. What it reveals is that the project proposed by the foreign parties was only viable in its description. As it turned out, the proposal glossed over and

misrepesented vital issues such as availability of raw materials and costing.[38] Again the project was approved as described. In 21 of the projects studies, available information suggests that the project description by the foreign parties involved may have been accepted without any fundamental amandements.

2. Evaluation of Sponsors

The Kenyan evaluation/negotiating team has displayed some laxity in establishing the credentials of the foreign investors who propose to establish projects in the country. Although the Kenya government in its rhetoric insists on having dealings with firms of 'international repute'[39] its attempts to establish the reputation of such firms have left a lot to be desired. The government's view of what is a firm of international repute appears to have nothing to do with the appropriateness of any firm's establishment in Kenya, but rather in reference to its reputed commercial success elsewhere. In general, the NPC and the bureaucracy have tended to take the applicants' account of their credentials without much questioning. Even where information that would cast a shadow over an applicant's self acclaimed credentials is available, the Kenyans appear to have paid little regard to such information. This lack of interest in the credentials of foreign applicants , particularly as to their capacity and ability to deliver the required goods and also their motives for making the investment has had

drastic consequences in the past. Three projects established in Kenya in the 1970s provide telling examples. Two of them have already been mentioned, Ken-Ren and KCFC, and the third is Interfood (Kenya) Ltd.

In May 1974, the government advertised for tenders to set up a fertilizer plant that would cater for domestic and some export markets. By November of the same year a number of proposals had been received and evaluated by the ISPC. By the end of the year, the NPC had studied these proposals and their evaluation reports from the ISPC and also short-listed four of the applicants for further consideration. Up to this stage, N-Ren Corporation had not tendered for the project and apparently the tenders had been closed.[40] In December 1974, a representative of N-Ren International S.A. (N-Ren's Belgium subsidiary) visited the Ministry of Commerce and Industry. He proposed that N-Ren send a team to prepare a proposal by end of January 1975. This it did and the proposal was evaluated by ISPC, considered by NPC and by April 1975, the principal agreement had been signed and was ratified by the Ministry of Agriculture on behalf of the Kenya government in August of the same year. Did the Kenyan authorities really know the applicant they had approved while totally ignoring the others? The answer appears to be no for almost three years later, when the project had cost the taxpayer a fortune, the government announced that it had been conned by "Chicago conmen ". This was in an attempt to, itself, 'con' the public that

The choice of N-Ren was outwardly unimpeachable. But was the choice unimpeachable? The answer appears to be clearly, No.

There was enough information available to cast a doubt on the integrity and ability of N-Ren to deliver its part of the bargain. The decision-makers involved were, however, not concerned with establishing the credentials of the applicant. They relied on N-Ren's information about its credentials. This was in itself very unconvincing. To begin with, N-Ren provided no information on its financial standing. The ISPC report on N-Ren's proposal stated that:

> ... Reports and accounts are not yet available to the sub-committee so that the company's financial standing is not known.
>
> Reserves ..... no information
> Sales (Group) turnover .... no information
> Profits after tax ..... no information
> Shareholders ..... no information.[41]

In view of this, the Centre recommended that:

> In the absence of information on N-Ren, it would be prudent to examine its reports and accounts and to assess the company's financial standing in relation to the offer to supply a fertilizer plant for $55.9m.[42]

This advise was not given the priority it deserved and at the end of the day, it was an N-Ren whose financial standing nobody seemed sure about that triumphed.

In response to a request for information on N-Ren by the Kenya government, the US Embassy in Kenya forwarded a telegram from Washington. It appears that N-Ren had made similar proposals to Gabon and Liberia in 1974, but the telegram gave no more details on these. It went on to state that:

> ... No significant information about N-Ren was obtained,

except that it was established in 1973; owned 8% of St. Pauls Ammonia Products, a public company which distributed and manufactured fertilizers which was affiliated by merger since December 1973 with Miami Delta Inc. and two other companies; that these companies 'were reportedly producing and marketing in excess of one million tons of nitrogen products' and; that it owned a 50% interest in a "successful operation" in Mauritius.[43] Despite the lack of any 'significant information' on N-Ren the telegram concluded by stating that:

> ... no reason why Embassy should not recommend GOK to give serious consideration to N-Ren proposal.[44]

On the contrary, the telegram contained very significant information on N-Ren in the light of its claim that it produced and marketed in excess of one million tons of fertilizer in the US. The telegram did reveal that N-Ren held a very minor - 8% - share of one of the firms that did this and therefore its claim was a big exaggeration that to all

intents and purposes amounted to a clear 'lie' on the part of N-Ren. Also an ICDC mission to Mauritius had reported that the project there was far behind schedule and had suffered great losses owing to a fault in technical designs that were a responsibility of N-Ren. The fault appeared to have occurred not because of the complexities of the technical work involved, but due to a simple error in the choice of some inputs. This error, it would appear occurred as a result of attempts by N-Ren to cut corners thus using cast iron in place of steel in parts of the project .[45]

Meanwhile some ICDC officials who had become skeptical of the proposal carried out some investigation on N-Ren. The results were far from being encouraging which may account for ICDC'c refusal to invest in the project. An ICDC official observed that N-Ren "seem to be making a lot of noise at present - some say a little too much."[46] A commercial contact in New York informed ICDC that N-Ren had sold out its operating company to Bechtel Corporation and warned that:

> The question arises as to whether N-Ren still retains adequate expertise following the sale of its operating company to Bechtel.[47]

Another contact brought information to the effect that N-Ren's headquarters were in fact in Cincinnati, Ohio and not in Bermuda as claimed in their proposal. As to N-Ren's

claim that it produced small standardised packaged units for manufacturing ammonia with capacities of about 100 tons per day, the source warned that;

> Plants of this small size are not ordinarily built in the USA except for special occasions. We know of no such installation by N-Ren.[48]

It suggested that the Kenya government would do well to obtain fron N-Ren a listing of companies where they had built nitrogen plants and then contact these firms either directly of through a fertilizer consultant for details as to how buyers are satisfied with N-Ren's plant and performance. This advice, had it been heeded, would have probably been enough to save the country the huge losses it incurred in the project. A foreign technical adviser to ICDC could not find, through his contacts, any trace of N-Ren in Senegal where it had claimed to have erected a similar plant. He was, as he put it,

> More and more surprised that our Ministry of Agriculture jumped into this project without even knowing who their future partners will be.[49]

And that is the way it was. The government did not really know much about N-Ren and its representatives had displayed remarkable indifference to the necessity of establishing the credentials of the foreign applicant.

In the case of KCFC project, which appears not to have gone through the ISPC or the NPC, the government similarly failed to establish the credentials of its foreign partners.

Some of these so called 'foreign' partners are in fact a local magnate who has incorporated companies in some offshore investment localities. It would appear that the prime object of such a roundabout way of investing is to repatriate funds from Kenya. To date, all that the Kenyan partners know about one of these 'foreign' firms is its collecting agent's address in London. The agents are a firm of law agents. No attempt whatsoever was made at the start of the project to establish whether or not the foreign partners were capable of delivering their part of the bargain or who they were. As it turned out, they just played the role of middlemen and the plant is being constructed by sub-contractors.[50] Meanwhile project overrun costs are running at nearly 300% with little signs of the rate subsiding unless the project is completed, and there are doubts as to this happening.

Interfood (Kenya) Ltd., is yet another example of the failure of the Kenyan machinery for evaluating project proposals submitted by foreign firms. It was a joint venture between ICDC, IDB, ADC and Apeninn A.G., a company registered in Liechtenstein. The proposal to establish a project to manufacture freeze dried meat and coffee products for export to Europe had been submitted to the

Kenya government, ICDC and IDB by an Italian national in 1975.[51] The proposal was accepted and thus Interfood came into being in 1977. The joint venture agreement committed the project to enter into a technical service and management agreement with a company known as Technopatent A.G., and into an exclusive purchasing and marketing agreement with a company known as Foodsimport A.G. These two companies were also registered in Liechtenstein. At this stage, nothing was known about Apeninn except that it had procured the incorporation in Kenya of Interfood (K) Ltd., with a nominal share capital of Kenya shillings 2,000/= with two Italian nationals holding the requisite two shares as nominees for Apeninn. The Kenyan parties were then asked to subscribe for shares in the company.

As for Technopatent A.G., Apeninn had described it to the Kenyan shareholders as:

> Apeninn's branch company that provides know-how, engineering, chief supplier of management in the realization of freeze drying turnkey projects.[52]

Apeninn gave three examples of the plants it claimed Technopatent had implemented "during the last three years".[53] Two IDB officials visited Italy in November 1976 to inspect a plant equipped with freeze drying equipment supposedly supplied by Technopatent. What they saw was far from any clear proof of Technopatent's expertise.

> They saw a project in Sicily where equipment for freeze drying juices was being installed but did not visit any freeze drying plant for meat or coffee either being installed or operational.[54]

Indeed what they saw had absolutely nothing to do with Technopatent.[55] Even after this rather unconvincing tour, the Kenyans signed a TS&M agreement with Technopatent in which the latter describes itself (the agreement was drawn by Apeninn, its parent company) thus

WHEREAS

> A. The managers have considerable knowledge and experience in planning, design, engineering, construction, staffing and operation of plants for the manufacture and production of freeze dried coffee and meat and other products...

There is no doubt that the Kenyans who evaluated the project and those who negotiated with Apeninn relied on this description of Technopatent's experience without any resort to independent corroboration. In addition to all this, the president of Apeninn had claimed that:

> Foodsimport engaged in marketing and distribution of freeze dried products and had a turnover of $20m. per annum.[56]

Once again the Kenyans accepted this claim without bothering to verify it from an independent source.

In 1979, Technopatent defaulted and the truth at last came out. The Kenyans had been duped. They found out, inter alia, that

- Technopatent had been formed in 1975 specifically to enter into the TS&M agreement with Interfood (K) Ltd.
- Technopatent did not previously have a bank account in Switzerland and opened one in 1976 specifically to conduct the major transaction with Interfood - i.e. to receive the 30% of total plant cost down payment plus an irrevocable letter of credit from Interfood for an amount that was 40% of total plant cost - as per the provision of TS&M agreement.
- Foodsimport had been formed in 1975 to specifically enter into a purchasing and marketing agreement with Interfood and thus completing a neat looking investment package.

The project eventually collapsed and the local shareholders formed a re-constituted firm out of the ruins.[57]

It is clear then that in these instances the Kenyan negotiating team proceeded to negotiate draft agreements submitted by foreign parties without questioning the ability and capacity of the foreigners to perform their contractual obligations. Even where independent evaluation, as in Ken-Ren, was available it seems to have been totally ignored. Four other projects in the sample displayed similar characteristics while in the case of nine other projects, the question was not whether they had the ability and capacity to deliver, but whether they intended and were willing to deliver at reasonable terms and conditions; at what cost;

and most important, what exactly did they contract to deliver? Many of these questions were never raised and the foreigners were, therefore, able to chart their operations virtually unhindered. For these firms, the Kenyans ought to have considered, not their capacity and ability but their appropriateness as well as that of their proposed projects to the Kenyan circumstances.

3. Financial Matters

We include, under this heading a discussion of issues on capital cost and structure and the profitability forecasts of proposed projects. These are very vital aspects of all projects for they bear on other important economic considerations such as creation of employment, saving and earning of foreign exchange etc. Prior to the approval of any project, they should have a potential for contributing towards such wider economic objectives in a positive way. The NPC and other government departments involved should, therefore, subject all proposals submitted to a thorough financial analysis and should stick to a policy of evaluating projects in the light of their contribution to the economy at large. Sadly, this appears not to have been the case so far. In their consideration of a project financial proposals the Kenyans have made little effort to analyse these in a realistic way. Two of the cases discussed above illustrate this lack of effort on the Kenyans' part to negotiate for reasonable financial arrangements in projects

involving foreign investors. These are once again, Ken-Ren and KCFC.

The Ken-Ren financial plan provided for the cost of supply of equipment from overseas and its construction only. It did not provide for the cost of import duties and sales tax on these items. As a result of this omission, the real costs were likely to be significantly higher than shown in the proposal. In the preparation of the proposal, N-Ren had also assumed that the government would pay for substantial infrastructure investment including that of laying two pipelines to convey naptha and fuel oil from the oil refinery at Mombasa to the fertilizer factory. They therefore omitted these costs in their costing of the project. These factors were pointed out to the permanent secretaries in the Treasury and in Commerce and Industry by an expatriate adviser to the government who observed that:

> It is quite impossible to assess the project at all unless it is costed taking into account all factors. The financial plan should then be drawn up on the basis of that complete costing ... The full cost of the project should be taken into account and viability measured on the basis of that costing.[58]

Nobody in the government departments involved, it seems, took any notice of this advice.

It appears that not only were important cost elements omitted in N-Ren's proposal, but that even some

of those that were included were deliberately understated. This flaw in the proposal was brought to the attention of the Kenyan negotiatiors,via ICDC, by the latter's two man mission to Mauritius to study N-Ren's project there.[59] Noting that the Kenyan project was twice the capacity of the Mauritius one, they commented:

> It appears that the Mauritius plant experienced a gross capital overrun which arose out of understatement and hidden cost. Between 31.6.74 and 31.1.75 it was found necessary to revise the cost of the project by around $4.6m. The Kenyan project is to cost $57m. and only some $5m. has been set aside for preliminary expenses and capital. Considering that it will have a turnover of $52m. per annum it is felt that the working capital is grossly underestimated.[60] (emphasis added)

A provision for overrun costs had been estimated at £1m. This too was questioned.[61] There was no provision for inflation or contingencies in the plan and it was, therefore, almost certain that £1m. would be insufficient.

Regarding the capital structure proposed, the ISPC felt that this would change considerably as actual costs exceeded the estimated ones. But even assuming that the estimated cost would not be exceeded, the equity to loan ratio would be 25% rather than that given by N-Ren i.e. 30%. Under this structure N-Ren's equity participation of £1.66m. would represent 7.6% of the total investment with the government bearing the risk on the remaining 92.4% including its guarantee on the loan.[62]

The government risk burden was heavy compared to that borne by N-Ren and some people felt that N-Ren should be asked to increase its equity participation. A government adviser felt that:

> one of the few safeguards we have is to require N-Ren to take a meaningful equity stake in the new company which I would define as being at least 50% and if possible, more.[63]

In the end, the N-Ren financial proposal was accepted intact. The very pertinent misgivings outlined above and several others appear to have been totally ignored.

In the case of KCFC, the deal that was approved also underestimated costs by about 300%. It committed the government to supply free electricity and water. The initial gearing ratio was 30%, but taking into account the project overrun resulting from the gross underestimation of various items, this now stands close to 40%. The government holds 51% of equity and has also guaranteed all the loans to the project, both foreign and local. Another project, Kenya Fibre Corporation involving the same foreign parties has also reached project overruns in excess of 200%. A special audit report commissioned by Treasury in 1979 to examine the project's financial affairs identifies the main cause of project overrun as being a severe underestimation of working capital and the omissions altogether of some important cost elements. The cost of buildings for example was underestimated by as much as 175%.

Yet these projects went through the approval stage without alteration in any significant way. These were not the only projects which exhibited these characteristics. Fourteen other projects in the sample exhibited similar characteristics in varying degrees. No information was available on three projects while in the remaining six the financial arrangements on paper, appear to have received sufficient attention.

4. Protection and Other Incentives Offered

In negotiating for the protection and other privileges to be accorded to an applicant for a CAE, the Kenyan system presents a really sad picture. The Kenyans have accorded protection and other privileges asked for almost as a matter of course. The rhetoric of the government has increasingly been in favour of less protected and therefore more internationally competitive projects,[64] but this has been matched by a practice that has favoured highly protected industries that are non-viable at not only internationally competitive prices but also at nationally semi-competitive prices. The NPC, wherever a project is referred to it, and the bureaucracy in all other cases have served as fora for dispensing extremely liberal privileges to foreign applicants. In dispensing these privileges, the Kenyans have, on the whole, asked for little reciprocity. Instead of being a mechanism for ensuring that foreign firms are admitted only on terms favourable and conducive to the achievement of Kenya's

Table 6

MAJOR ISSUES RAISED IN ENTRY NEGOTIATIONS INVOLVING

19 KENYAN SUBSIDIARIES, 1965-1973

Issues raised by Subsidiaries/ Government	Pct. of 19 Subs Involved	Pct. of these requests in which subsidiary/Govt. achieves object
A: By Subsidiaries		
1. Seek import protection via tariffs or restrictions.	53%	90%
2. Seek right to import machinery and/or inputs duty free.	32%	100%
3. Seek Government Finance in project.	16%	67%
4. Seek guarantee against domestic competition for period.	11%	100%
5. Seek long-term status-quo clause.	11%	100%
6. Seek guarantees on work permits. *	11%	100%
7. Seek approval for generous fee agreements.	11%	100%
Total Issues by Subsidiaries - 32		
B: By Government		
1. Seek better Foreign Exchange Cash Flow via higher capital invested, lower planned dividends, etc.	26%	100%
2. Seek assurance subsidiary take on African partners, plan Africanization of managers or distributors.	21%	100%
3. Seek location outside Nairobi and Mombasa	11%	50%
4. Seek higher government equity participation	5%	100%
5. Seek control over subsidiary pricing formula.	5%	----
Total Issues raised by Government - 16		

* This table covers all 19 interview cases in which subsidiaries negotiated with government over substantive points to obtain a Certificate of Approved Enterprise, during the period 1965-73.

Source: Langdon, 1976 P. 125.

economic objectives the approval machinery has played a very different role. Several other studies on Kenya have also concluded that the protection and incentives offered to foreign investors are extremely liberal.

Langdon, for example, argues that the oligopoly perspectives of multinational companies suggest that they seek market security and protection from competition for their investment and that available evidence shows that this has been their primary objective in negotiating entry into African countries.[65] He further argues that even when negotiation takes place in Kenya, the effect is not necessarily to constrain the MnC sector, but that empirical evidence

> ... suggests that the NPC is primarily a channel by which subsidiaries obtain economic privileges, particularly freedom from external (and sometimes internal) competition and from duties on their imported machinery and inputs.[66]

Table 6 summarises his research findings on issues raised in entry negotiations in support of this argument. Other studies by Kaplinsky, Swainson, Deepak Lal, Eglin, ILO and IBRD fully support this argument.[67] Evidence from over 25 agreements involving foreign investors in Kenya examined by the present author, but not presented here, support this argument. As examples, a detailed account of privileges granted to Firestone is produced below and those granted to KCFC in the joint venture agreement appear in Appendix 1 The privileges Firestone, USA demanded and obtained

through the NPC included:

- An undertaking binding the government to discourage "establishment in Kenya by any individual, firm ... other than the New Company (Firestone (E.A.) Ltd.) of any activity ... within the scope of the project. In particular ... the government undertakes that no such establishment shall be approved under FIPA ... or the Exchange Control Act, or under any comparable legislation" for seven years from start of production.[68]

- A quota restriction of tyre imports from outside E.A. in accordance with a formula stipulated by Firestone USA.[69]

- A total ban on imports of tyres Firestone would from time to time notify the government of its intention to produce in Kenya.[70]

- Unrestricted import licences (including the availability of necessary foreign exchange) to the extent that, and for so long as, its requirements for construction materials, equipment, machinery, spare parts, or raw materials.... [71]

- Exemptions from import and customs duties and from any other tax for and with regards to items imported by the company.[72]

- Unrestricted export licences and total exemption from export duties.[73]

- Freedom to use its own pricing formula in the sales of its protected products.[74]

- A commitment by the government to ensure that its departments, including the armed forces purchase tyres from Firestone (E.A.) Ltd. and also ensure that the firm secured monopoly rights to supply its tyre products to any enterprise established in Kenya for the assembly of motor vehicles.[75]

- A 20% investment deduction under the Income Tax Act for capital expenditure which deduction would not be reduced below that figure even if the law wereto be subsequently amended reducing the deduction allowable to below 20% or abolishing it all together.[76]

This provision applies to Firestone E.A's future capital investments.

- The grant of all government approvals and licences necessary to establish and operate the project.[77] The necessity to be determined by FEA's foreign management.

- The right to capitalize technical and service fees due to Firestone USA. [78]

- A government's undertaking that in connection with any dispute arising out of the investment agreement there would be no plea of sovereign immunity. [79]

- An extremely favourable (to FUSA) process and Licence Agreement to last for 25(!) years from the commencement of production date. [80]

With the exception of the clause on sovereign immunity, such privileges are prevalent in other projects studied that involved foreign firms. Similar, and in some cases even more liberal privileges have been granted to Del Monte International's [81] subsidiary, Kenya Canners Ltd., the Fluorspar Mining Company, Rift Valley Textiles Ltd., Pan African Paper Mills Ltd., and many others. Not one of the firms in the sample included in this study failed to obtain some satisfactory form of protection and/or privileges.

5. Other Factors

In addition to the factors discussed in some detail above, the Kenyan approval machinery have, more often than not, uncritically approved projects with various aspects that may militate against the national interest.

These include approval of projects:

- containing restrictions on exports.
- tied to purchasing embodied and disembodied technology from the foreign party or his appointed suppliers.
- involving high and often duplicated service fees
- involving the vesting of too much discretionary decision-making power to the foreign party.

Such concessions and several others lead, in the final analysis, to the vesting of much of the decision-making power over most vital aspects of projects in the hands of the foreign party. These things are discussed in detail in the next two chapters. The only purpose of referring to them here is to emphasise the point made at the beginning that the approval machinery does not necessarily constitute a significant constraint to foreign investors. It is not merely the fact that they appear in final agreements reached, that casts a shadow of doubt upon the efficacy of the approval machinery as a regulatory measure, but also the fact that they receive virtually no critical review from those involved in the approval machinery.

That the NPC does not raise major critical issues in the negotiations with foreign investors does not necessarily mean that no one else does. In the Ken-Ren case discussed above, for example, it has been shown that there were some public officials who had taken the trouble to analyse

N-Ren's proposal and question the wisdom of approving it. This is not an isolated case. In virtually all the projects studied, issues critical to the well-being of a project or the wisdom of starting it were a common feature. At times they received some attention and at other times they were simply swept under the carpet.[82] The Firestone project [83] is a case in point.

During the negotiations with Firestone International, some public officials outside the NPC raised issues relating to the proposal and made some recommendations. The recommendations that received attention were those that sought to have Firestone International bring in more capital and those that sought to have the company commit itself to appointing certain African personnel at management level as well as awarding its distribution business to African distributors. These were in line with the government's stated objectives of increasing the inflow of capital in the form of foreign exchange and of Africanizing the personnel of companies involving foreign nationals as well as the distribution business. The firm did not resist, and was quite willing and prepared to accept, these relatively easy conditions. However, where the firm dug in its heels, the issues were simply swept under the carpet. One of such casualties was the issue concerning the pricing mechanism of Firestone's product. The Ministry of Commerce and Industry had stated its position on this issue in the following terms:

> ... In particular the most important point was S.6.08 on price mechanism, and in this connection the Firestone representative made it clear that they did not expect the government to control prices of products of the company at any level and further, that any excise duty or other forms of taxes imposed would be passed on to the end consumers. The government proposal on the other hand was that the first clause - i.e. "There shall be no control at any level of the prices at which tyres, tubes and retread materials are sold" - should be deleted .. [84]

The clause was not deleted and appears as clause 6.08 of the investment agreement in verbatim. In addition, the Ministry objected to what is called "the implication" of Firestone's draft clause 6.12 [85] arguing that the Ministry had so far maintained that the government:

> ... Cannot agree to commit itself now such that it would prejudice its chances of exercising of its sovereign prerogative of making and amending laws. This stand seems the only logical one and therefore no valid reason is seen for abandoning it. [86]

Logical as it may have seemed to the Ministry, the stand collapsed in the face of Firestone's adamance. The clause appears verbatim as clause 6.12 of the Investment Agreement. Finally, the Ministry objected to part of clause 8.01 of the draft agreement saying that:

> It is superfluous as we have maintained all along and we should press for its deletion from the section. [87]

The offending part of this clause provided that:

> The Government shall procure that in connection with any dispute arising out

> of this Investment Agreement, there shall be no plea of sovereign immunity.

Once again the Ministry's objection received the, by now familiar response, the clause appears verbatim in the agreement.

Criticisms of the draft agreement from other quarters fared no better. Officials from ICDC and the Ministry of Economic Planning, for example, objected to the quota system of licensing tyre imports that Firestone were proposing and had incorporated into the draft agreement, but to no avail.[88] On the issue of training Kenyan personnel, an ICDC official observed that Firestone's

> so-called training programme for Kenyan citizens smells to me. Furthermore, the Africanization is not their [Firestone International] business and should be left to the government.[89]

He was of the view that too much discretion in training of the recruitment had been left to the foreign managers. Twelve years later, the validity of this observation remains unshaken.[90] The official was also of the view that Firestone's request for an import duty exemption for raw materials for over ten years had not been justified. He suggested that Firestone be asked to specify its production costs so that the committee could determine whether or not Firestone really needed that kind of exemption in order to achieve the forecasted profitability.

As an institution, ICDC was of the view that the protection offered was "a bit too long" and that the attached conditions were "unnecessarily rigid".[91] In addition, it felt that the government "should have power in the agreement to decide whom to give residence permits in connection with the project" rather than the right to merely endorse Firestone's choice. In general, ICDC would have wished the NPC to push for more benefits from Firestone by tougher bargaining. Its executive director summed it all up when he told ICDC'c team on the project:

> I think we should take a very tough line along the lines you have outlined [i.e. reject some of Firestone's demands] ... I do not think the requirements as above are all necessary to induce them in. [92]

As it happened, NPC, under pressure from both Treasury and some highly placed officials in Commerce and Industry, did not take a tough line in its negotiation with Firestone. Indeed none of these criticisms on the terms of the draft agreement was effectively utilised, by the NPC which seemed to have been under pressure from above to approve the Firestone project. There is little evidence to suggest that the NPC made any serious effort to resist this pressure.

C : COMMENTARY

Having examined the approval process for the establishment of foreign enterprise, one may wonder why the machinery seems to perform rather poorly as a means of imposing some form of regulation of such establishment. Indeed the general tenor of all the agreements examined by the present author indicate that the Kenyan approval machinery has granted applicants for CAE far more economic privileges than the concessions it has obtained from them. As a screening process intended to ensure that only viable projects that have a priority by virtue of the benefits they bring to the country, the machinery can hardly be said to be a model of success. The evidence presented herein indicates there are still problems in the selection of projects that have a potential for contributing to the achievement of stated economic goals as well as in imposing, on applicants, terms and conditions aimed at ensuring that they so contribute, as a prerequisite to approval. Since the early 1970s, for example, government policy statements have emphasised the need to encourage a shift to industries that are among other things, local-resource intensive, labour-intensive and export-oriented. The approval machinery has approved some projects that are the exact opposite of these. It has granted exemptions from duties on imported raw materials and other inputs and granted excessively generous protection against competition. This, in turn, has led to a situation in which capital and imported inputs have been

preferred in place of labour and local resources and in which import-substituting industries have been preferred to export-oriented ones. In addition the premium prices resulting from very high effective protection has resulted in inflated costs of locally manufactured intermediates that tax agriculture, the most export-oriented sector of the economy, and pricing out other potential exports.[93] This could hardly be one of the results the approval machinery was intended to achieve. There are two main factors that have contributed to the poor performance of the machinery. For want of a better classification, these may be classified as institutional and substantive factors.

1. Institutional Factors

The institutional framework that exists in Kenya for approving foreign investment is an extremely muddled one. By now the reader will have noticed that having identified the two stages involved in the process - project evaluation and negotiation - the actual discussion hardly follows this pattern. Furthermore, the reader will have also noticed that apparent formal machinery does not feature in some, indeed, most of the examples given. This is primarily because the formal system is very different from the actual practice that prevails. In reality, no institutional process worthy of mention exists. It was emphasised at the beginning that approval is on a case by case basis. This has led to the development of ad hoc committees and very often individuals constituting the sole machinery

for approval. The NPC, for example, is only a committee in name. Except for its Chairman, it has no fixed membership. The committee members seem to be selected on a day to day basis. In several cases where the committee sat in negotiation for two or more days, different personnel sat in the committee each day.[94] At best then, the NPC is no more than a series of ad hoc committees many of them differently constituted.

The lack, in reality, of an institutional set up of the approval machinery affects the effectiveness of the ISPC. Although it is a permanent department of the Ministry of Industry with permanent staff, there is no institutional requirement that all project proposals be referred to it. Thus few projects are referred to it for evaluation. This deprives the only evaluation body with the potential for carrying out project analysis of any significant role in the approval machinery. As the NPC has no technical expertise of its own, the possibility of filling this gap with the use of ISPC technical expertise is greatly hindered by the very frequent side-stepping of the ISPC's machinery.

Even where the formal machinery is partly followed[95] as in the cases of Ken-Ren, and Firestone, its effectiveness is weakened by the fragmentation of the various government bodies, that constitute its membership.

This fragmentation means that the Kenyans hardly speak with one voice and have frequently been in opposition to each other. In Ken-Ren's case, for example, ICDC was not satisfied with N-Ren's proposal (and for good reasons) and thus refused to invest in the project. The permanent secretary in the Ministry of Agriculture on the other hand, fought tooth and nail to have N-Ren's proposal approved despite its patently manifest shortcomings. So too did the Ministry of Commerce and Industry as well as the Treasury.[96] In the case of Firestone, ICDC'c executive director (and therefore ICDC) supported Uniroyal's application while the Ministries of Economic Planning and Commerce and Industry supported Firestone's application. Once again, ICDC found itself pitted against its parent Ministry. Such fragementation enables the foreign applicants to play the Kenyan parties one against the other.

By far the most important weakness of the institutional set up is to be found in its decision-making machinery. Its most glaring feature is its highly discretionary nature. It also contains rather relatively high degree of finality and non-accountability. The decision making power and process is completely divorced from the rest of the approval machinery. Recommendations by the NPC are not binding on whoever makes the decisions. Even if the formal approval machinery were to perform an excellent job in evaluating and imposing conditions on applicants, its effectiveness would be good only to the extent that the decision

makers accept its advice and, even more, resist interfering with the evaluation process. Sadly, the practice has been to the contrary. The decision makers have greatly weakened the effectiveness of the approval machinery by interfering in its running and ignoring its advice. They have interfered in two basic ways. First they have approved projects without referring them to the approval machinery thus depriving the ISPC and the NPC a chance to evaluate the proposals and negotiate with the applicants.[97] These seem to be the projects whose promoters appear to have well placed connections in Kenya's political system. Second, the decision makers frequently interfere by entertaining direct appeals from applicants in the course of negotiations. Such was clearly the case when the NPC was instructed from above to halt its considerations of short-listed applicants for the fertilizer plant to give time to N-Ren to prepare and submit its proposal after the dealine for receiving tenders had long passed.[98] It was also such interference that forced the NPC to drop its pressure on Firestone to reconsider the pricing mechanism for its tyres.[99]

Technically the NPC is the body that ought to evaluate projects and negotiate with the foreign applicants. It is then supposed to advise the government through 'the normal machinery' on whether or not the projects should be allowed and if they should be, on what terms and conditions. The reference to the normal machinery indicates that, decision making power lies with the top level of the civil

service. From the projects the author has studied such decisions were made by no one below the rank of a permanent secretary where such powers were not delegated at all. Where no delegation took place, the decisions were at ministerial level with some decisions being referred to the cabinet for clearance. It is clear then that decision making power lies with those who have little expertise over the type of issues that are raised by such projects. It, therefore, follows that where a minister or the whole cabinet ignore its own experts' advice, it is not on the basis of his or their superior knowledge over the matter, but on the basis of their power to ignore such advice with impunity.

The Treasury, has in theory, the final say for it is its prerogative to issue the CAE under FIPA. However, it is not easy to point out who in Treasury exercises this power. Logically it should be the Minister of finance or an official in Treasury to whom he may have delegated this authority. Even where such authority is delegated to a designated official, one must always bear in mind that there is always the possibility of reversal by higher authority. In a government by civil servants as obtains in Kenya, the decisions of higher authority depends very much on whose advice such authority decides to adopt. In the case of Ken-Ren for example, higher authorities would appear to have adopted the advice of the permanent secretary in the Ministry of Agriculture rather than that of the

experts from ISPC or ICDC.

What must be emphasised is that the NPC has no decision-making powers whatsoever. At times, this observation applies to government ministries and parastatal bodies. Decisions involving major and very profitable concessions from the government may be reached at a high political level even before the projects have been seen or evaluated within the ministry concerned. It is a familiar occurrence for firms with the right political connections to have their glossy agreements and other documents, complete with high-powered approval, land as a fait accompli on the desks of the relevant ministry and or parastatal officials.[100] In such cases, the mechanics of the approval process become irrelevant.

2. Substantive Factors

In addition to the institutional constraints outlined above, several substantive factors contribute to the poor performance of the foreign investment approval machinery. The most important of such factors is the very real shortage of the requisite qualified technical manpower and other resources. The only body with some technical manpower is the ISPC, but even here, the manpower is spread very thin, lacks experience in dealing with multinationals' complex business and investment processes and lacks the necessary financial resources to conduct more than superficial evaluation of project proposals. To confound such

substantial limitations, it may be that the technological and other investment aspects of a given project are just too complex even for the available personnel to tackle adequately. Where such is the case the approval machinery may be operating on rather limited information which would make it even less competent in making any detailed evaluation of such a project. They are left with one of three main choices: vis. to drop the project altogether, to engage an outside consultant, or to accept the applicant's version of the prospects of the project as contained in his proposal. The second alternative is usually mistakenly ruled out as being too expensive and time consuming. The first one may at times prove politically unfeasible leaving the last course as the easier option. The choices are of course only applicable where the projects are channelled through the formal machinery. When they are not, then they constitute political decisions and are established with political backing.

Another possible limiting factor to the effectiveness of the machinery is Kenya's desire to attract private foreign investment. It may be that the overriding consideration is the attraction of such investors by offering them extremely liberal incentives. Some well placed government officials feel that a rigorous application of the approval process might scare away foreign investors. Certainly, the government has been keen to assure the investors that they would be offered adequate protection and other generous incentives.[101] It appears that the approach taken

by the government is to bargain not from its power to permit or reject foreign investors' applications for CAEs, but on the basis of its desire to have investors invest their capital in Kenya. Certainly, Kenya's strong capitalist sentiments have meant that private foreign investors have been accorded much more trust than would otherwise have been in a less capitalist oriented environment.

Finally, there is the very substantial, but difficult to pinpoint, problem of corruption. This is a fact of life whose existence is in virtually every sphere of life in Kenya and is widely accepted in general terms by the government. The government preaches against corruption in general, but has at the same time resisted frequent calls to set up a select committee of parliament to investigate the malady.[102] In corrupting public officials, the interested party would have to aim at decision-makers high up the ladder of political hierarchy, as low level civil servants are not responsible for approval of projects. It is difficult to prove such clandestine dealings when those involved wield enormous political power or they have patrons high up in the government. The dilemma is that:

> ... Whatever your suspicions ... you are unlikely to possess the kind of evidence which can force the government to institute drastic measures in an attempt to expose and punish those guilty of corruption. All the incriminating evidence is usually in the hands of the guilty and there is no reason why they should want to divulge such evidence.[103]

However, the fact that it never comes to the open does not mean it does not exist . Indeed, several officials involved in foreign investment affairs believe that it is fairly common and the reason the government does so little that can be termed positive about it is because many senior personnel are involved either directly or indirectly through a protection racket. [104] Reginald Green has contended that

> Certainly some contracts are determined by bribes both in the sense of being concluded at all and of their specific content. Any frequent negotiator for the African side with TNC's who says he has never been offered a bribe is either a trifle slow on the uptake or a trifle disingenuous. [105]

He should know for he has had the experience as advisor to the Tanzanian government. Many people interviewed in Kenya felt that corruption is a major factor in the relationship with foreign investors. There are many forms that corruption may take ranging from apparently legal offers or gifts to outright cash handouts. Although difficult to pinpoint, it is a safe bet that corruption plays a significant part in weakening the approval machinery in Kenya.

D : CONCLUSION

This chapter has examined the administrative process for approving new foreign investment establishing in Kenya. It has been shown that the approval process is governed, not by legislation, but by some form of administrative process. An underlying assumption of the discusssion in this chapter is that the approval machinery and procedure are part and parcel of the government's regulatory functions and that by processing foreign investment through such machinery or approval, the government intends to regulate the type of investment that is admitted and the conditions of its operation. Such regulation is deemed necessary in order to integrate the investments admitted into the overall economic system in a manner that is conducive to the fulfilment of the objectives for which they were admitted into the country in the first place.

The institutional set up of the approval machinery has been a major constraint to its effective operation. There has been no attempt to lay down even the barest of minimum binding rules either of the procedure to be followed or in the substantive criteria to be applied in the evaluation of projects. This has resulted in a situation where decisions have been made not entirely on the basis of a positive evaluation of projects. Because of the rather unclear decision-making machinery, only limited accountability for decisions taken exists.

The approval machinery has failed as a first stage of a regulatory machinery over the operation of foreign investment in the country. It has proved unable to scrutinise incoming investment in order to ensure that the conditions under which they are admitted into the country are carefully regulated in the national interest. This would be a necessary step towards making foreign investment play the role assigned to it rather than merely pursuing its individual business interests. The project evaluation by the NPC has been inconsistent at times and quite susceptible to political pressure. Lack of a clearly identifiable demarcation of responsibilities, coupled with severe manpower constraints have both substantially contributed to the inadequacy of the machinery. The failure is not inherent in the machinery, but rather has resulted from failure to utilize it constructively; constant subversion of its deliberations by political forces; and a lack of clearly defined and coherent economic and other criteria for admitting foreign investment.

It is now nearly ten years since the government indicated it would pass comprehensive legislation to regulate the establishment of productive capacity in the country. No such legislation has been enacted, and even more telling is the fact that no talk of such legislation has been heard in recent years. Whether such legislation would make any significant difference to the approval process is difficult to tell without seeing it.

What is not in doubt is that legislation or no legislation, the ultimate success of any approval machinery will depend on the willingness and ability of the government to implement it. As of today, the government's willingness to regulate the establishment of foreign investment in a realistic manner lags far behind its limited ability to do so.

A major consequence of the failure of the approval machinery to operate effectively has been the actual and potential limitations placed upon the government's regulatory role by the agreements entered into with the foreign parties. The failure of the machinery operates heavily in favour of the foreign parties who more often than not outbargain the Kenyans. They are able to have their projects approved as described and designed in their proposals and the agreements reached are also tailored to suit their interests in the projects. Thus for example in the case of PVP's approval

> ... many people appear to have been more keen on the implementation of what was contained in the study [proposal by SIFIDA] than trying to find out and be satisfied that the contents of the report was truly viable.[106]

Having had their projects approved as presented, they then draft the agreements in such a way that they are heavily biased to their advantage ensuring that the only way that the government can execute its regulatory role is by committing a breach of the agreements. In the case of

Ken-Ren, for example, it was

> ... Clear that at the moment, the agreements are drawn solely from the point of view of providing N-Ren with maximum advantages. No doubt they do not expect to obtain all they are asking for, but I regard it as essential that the government stick out for much more balanced agreement where the obligations are more clearly shared by both sides.[107]

Yet, N-Ren obtained all it asked for and the government picked up the tabs when the project collapsed.

The government has stuck to the terms of most of its agreements almost to the letter. Where the agreements tie its hands, it has allowed the provisions of these agreements to override its own concerns. Thus for example, when in 1980, the government wanted to introduce sales tax on imported raw materials to meet its overriding industrial restructuring objectives, it was unable to do so in certain cases. The minister of finance expressly admitted that the government's hands were tied saying that

> In view of existing arrangements between the government and a few basic industries, I propose to exempt them from payment of sales tax on their imported raw materials.[108]

There are many instances in the 25 agreements studied where the government has exempted foreign investors from withholding tax, for example, and also granted the foreigners powers in implementing and running the projects that are totally disproportionate to their equity.

This may limit the government's powers to effectively regulate their operations. Some of the limitations on the government's regulatory powers are discussed in chapter five of this study.

NOTES

1. Caps. 486 and 488 respectively.

2. See for instance S.365 of the Companies Act.

3. Where the investment is in a joint verture for example, the Companies Act has no application to foreigners as it merely deals with legal entities and the project would be Kenyan under the Act.

4. See Lloyds Economic Reviews 1971-79 and Langdon, 1978 for example.

5. 1974-8 Plan, 285

6. Ibid.

7. Ibid

8. Ministry of Finance, Plan Implementation Report, 1974/75, III - 36

9. 1979-83 Plan, 334.

10. Ibid, 30

11. 1974-8 Plan 284

12. 1979-83 Plan, 346

13. Ibid

14. 1974-8 Plan, 285

15. This information was obtained from the current chairman of the NPC in August 1978. See also John Ndegwa, 1976.

16. Information obtained through interviews with government and some project officials.

17. 1979-83 Plan, 30

18. Ibid.

19. The most important are the Companies Act and the Registration of Business Names Act for commercial, industrial and agricultural firms; and The Banking Act, and The Insurance Business Act for financial and insurance firms respectively.

20. 1970-74 Plan, 315

21. Ibid.

22. These are contained in an application form entitled "Project Application Form 'A' To the NPC". It is usually accompanied by a booklet entitled "Guidelines For Completion of The Project Application Form 'A' To the NPC."

23. ISPC, Comparative Summary of Fertilizer Proposals, 14/2/75

24. These were summarised in a rather patronising letter from the President of N-Ren, Thomas C. Snyder, to the Ps, agriculture dated 5/3/75

25. See ISPC, 1975

26. See Ibid, where an expatriate adviser in ICDC described this as a "political problem" adding that "As the Shah of Iran once put it: 'We developing countires need pollution at this stage'. This would appear to indicate that such a problem was not for consideration by the NPC. This view is re-inforced by the experience in the cases of the Flourspar Mining Company and that of a Copal factory that followed the same path.

27. Ibid.

28. See Preamble to the Joint Venture Agreement.

29. Ibid. art.IV s.4.04

30. Interview with Agricultural Officer and an Official of KCFC. The government seems reluctant to fulfil this obligation - See Weekly Review 12.2.82

31. Interview with KCFC official.

32. The project appears not to have gone through the NPC, although it appears that it did not support its approval

33. See W.R. 12.2.82, 20-22

34. It was a reconstitution of a financially disastrous venture - Panafoods Ltd.

35. Report of government committee set up to review the problems of PVP and recommend whether or not more public funds should be poured into the company. MCI. 1977, 14

36. Ibid.

37. Ibid at pp 14-15. (Emphasis added). This view is borne out by a synopsis submitted by INHA in a letter to PS, MCI and to ICDC dated 18.1072

38. See Ibid.

39. The guidelines issued by the Ministry of Industry for the application of approval to the NPC state that:

> One of the most important factors for the success of a project is the capability of the investors to carry through the project plan and to successfully implement it. It is therefore important to select partners and/or investors who have the requisite managerial or technical expertise.

40. Jon Ndegwa, 1976

41. ISPC 1975

42. Ibid.

43. Telegram dated 6.5.75 forwarded to the Kenya government by the US Embassy.

44. Ibid.

45. See ICDC mission to Mauritius report on the Mauritius Chemical and Fertilizer Industry Ltd. (MCI), March 1975

46. See ISPC, 1975

47. Ibid.

48. Ibid.

49. Ibid.

50. See WR 5.2.82

51. This Italian was also a director in another joint venture involving an Italian firm whose parent company was involved in a massive transfer pricing operation including the supply of second-hand obsolete equipment and at least one outright illegal transaction involving amounts equal to the parent firm's equity in the joint venture.

52. IDB, "Interfood (Kenya) Ltd.: Sequence of Events to Date", 14.5.79, 3

53. Ibid.

54. Ibid, 1

55. Infact, Technopatent had done no work at all at this stage having been set up specifically for the purposes of this transaction.

56. This claim was made in a letter to the Kenyan parties dated 16.10.76

57. All the contractual safeguards against financial losses were found to be of no use to the Kenyans as none of the foreign companies had any assets that could be attached in satisfaction of any judgment obtained against them. Legal action against the companies was therefore of little practical value and was likely to lead to further losses. Incidentally, to obtain this rather simple advice on the possibilities of legal action, the Kenyans paid a firm of lawyers nearly $18,000. This firm of lawyers had acted as the Kenyan legal advisers in the negotiations, but had not pointed out the futility of legal action at this stage.

58. Internal memo on "Fertiliser Project Draft Agreement" dated 4.3.75 and addressed to an undersecretary in Treasury, 2.

59. The objectives of the mission were "principally to report on the nature of the joint-venture project currently being implemented by the Mauritius Government and N-Ren and to discuss with the Government Officials concerned with the ... project on various aspects and difficulties encountered during the implementation of the project. It was also hoped that the team would clear certain suspicions prevailing during discussions as to the credibility of N-Ren group as a possible partner in the proposed fertilizer plant in Kenya ...." see ICDC, Mauritius MCFI report 1975, 1

60. Ibid.

61. Internal memo on Fertilizer Project, 1975, 3

62. ISPC, 1975

63. Internal memo on Fertilizer Project, 1975, 2.

64. See 1970-74, 1974-78, 1979-83, Plans and Budget Speeches from 1972-81.

65. Langdon, 1976, 249 See also R.S. May, 1965, 12 An executive director of ICDC commenting on the Firestone tyre project had this to say: "We tend to forget that the only reason why Firestone and Dunlop ever came into this project was mainly to protect their own market in this region. For over a year none of these traditional companies had reacted to our requests to sponsor a tyre factory ... until Uniroyal put up its proposal to the government". Memo to PS, MCI and MEPD and General Manager DFCK from executive director ICDC, 21.12.68

66. Langdon, 1976, 122-4

67. See R. Kaplinsky, 1979, 1978 and 1977; N. Swainson, 1980; Lal, 1975; Eglin, 1978; ILO, 1972 and IBRD, 1975 respectively.

68. GOK and Firestone Tire & Rubber Co. - Investment Agreement dated 21.7.69 Art.VI s.6.02

69. Ibid s.6.03 (a) (b) (c) and (d)

70. Ibid (d) (ii)

71. Ibid s.6.05

72. Ibid.

73. Ibid. s.6.07 (a)

74. Ibid. s.6.08

75. Ibid. s.6.09. The original clause in Firestone's draft agreement read: "The New Company shall have the exclusive right to supply tyres, tubes and retread materials to all government departments, agencies, corporations and enterprises, the armed forces and police force, as well as any enterprise established in Kenya for the assembly of automobile vehicles."

76. Ibid. s.6.10 (b)

77. Ibid. s.6. 11 (a)

78. Ibid. s.6.12

79. Ibid. Art.VIII s.8.01. The agreement further provides that in connection with guarantees relating to the project issued by the US government between the two nations, "... nothing herein contained shall be deemed to be a voluntary agreement by Firestone to submit to any exercise by the government of its sovereign rights." - 2.6.13

80. Clause 21 of Process and Licence Agreement.

81. Del Monte was bought by R.J. Reynolds, the cigarette multinational, in 1978.

82. An example of an issue that received attention is the one regarding the location of the project in the cases of PPM, Rivatex and Leyland (K) Ltd. for example. Among those that were swept aside were the viability of the vehicle assembly and KCFC, and also one relating to the terms of a technical services agreement in the cement industry.

83. The Firestone project was set up in 1969 as a joint venture between Firestone Tire & Rubber Co. of USA and the government of Kenya as well as the ICDC, to manufacture various ranges of Firestone tyres in the country.

84. Letter from PS, MCI to various government ministries and parastatal organizations dated 15.4.69. Surprisingly, the attorney-general's office appears to have made no responses to the legal issues raised. The A-G is the principal legal adviser to the government.

85. Clause 6.12 of the JVA reads: "Firestone having provided the government with full details of the project including the financial plan and the government having determined that the project will further the economic development of Kenya, there shall be issued to Firestone and to any other foreign national who, within the meaning of FIPA, 1964, proposes to invest foreign assets in the projects, a CAE with regard to each investment of foreign assets in the projects, including the services performed as contemplated by the Plant Contract and the Process and Licence Agreements. Thereafter, the provisions of the FIPA, shall apply with regard to each such CAE."

86. PS, MCI letter of 15.4.69.

87. See Ibid.

88. ICDC, Note on the Project Committee meeting of 4.3.69.

89. Ibid.

90. A senior African Official with Firestone attributed the "unsatisfactory nature of effective training" to the discretion left to Firestone International on training matters. So did an official of the Kenya Federation of Employers.

91. Internal memo from an official of ICDC to his executive director titled "The Kenya Tyre Factory Agreement", dated 11.3.69. It listed the following as examples of the "unnecessarily rigid" conditions: (a) unrestricted import licenses; (b) complete exemption from import duties for 10 years; (c) Unrestricted import licences, exemptions from export duties, excise and sales taxes; (d) absence of control of prices of tyres by the government; and (e) exclusive right to supply tyres, tubes etc. to all government departments.

92. Reply to Ibid.

93. See for example IBRD, 1975, Langdon, 1976, Phelps and Wasow, 1972 etc.

94. Interviews with government and parastatal officials who have sat on the committee, 1980-81. This was one of the flaws detected in the machinery. The turnover of committee membership was so high that it was likely that it contributed significantly to the inconsistencies noted.

95. The author knows of no case where the formal machinery as well as procedure was followed 100%.

96. Thus putting ICDC at opposite ends with its parent ministry - MCI as well as its financier - Treasury.

97. This appears to be the case in relation to KFC and KCFC for example.

98. Jon Ndegwa, 1976

99. See Langdon, 1976, 130

100. See Hopcraft, 1980, Part II, 16

101. See chapter II of this study.

102. These have usually come from the MP for Butere, M. Shikuku, who was detained in 1977 for alleged subversive activities which have never been revealed, let alone proved, to the present day.

103. Sunday Nation, 20.1.68

104. This emerged in the course of the author's interviews with various government and parastatal officials in 1980 and 1981.

105. R. Green, 1979, 30

106. MCI, PVP Committee Report, 1977, 18.

107. Internal memo on "Fertilizer Project Draft Agreement" 1975, 6.

108. Budget Speech, 1980/81, 8.

CHAPTER FOUR

AFRICANIZATION AS A MEANS OF REGULATING FOREIGN INVESTMENT

At independence, the Kenya government rejected nationalization of the economy as a viable means of control over the country's resources, saying that:

> To imagine ... that the use of resources can only be controlled through their ownership or that appropriate ownership will guarantee the proper use of productive assets are errors of great magnitude.[1]

On the face of it, this would seem to imply that the foreign capital that dominated the economy at independence would remain dominant over all economic aspects of the nation. However, this would have been clearly politically unpalatable to the African petty bourgeoisie who emerged as the new ruling class. The ambition of this small group to amass wealth and live like the whites had been suppressed by the colonial regime and they clearly expected independence to bring an end to this suppression. In the words of their chief spokesman in the gorvernment:

> ... the predominance of non-Kenyans in the ownership, management and control of private enterprise is one of the most glaring defects of the private sector in Kenya. No country can accept the continuance of this kind ... To turn a blind eye to the racial imbalance in the country's economy would be tantamount to inviting racial disharmony and conflicts in the future.[2]

The solution adopted to tackle this 'glaring defect' was the Africanization of the economy and the workforce. Thus

from the beginning, Africanization was viewed as an urgent task which had to be achieved within a relatively short period. The question facing the government was, therefore, not whether to Africanize, but rather 'how to reconcile the urgency of the matter with citizenship guarantees and the desire for rapid economic growth'.[3] In his introduction to Sessional Paper No.10 of 1965, President Kenyatta summed up the government's view of its priorities and their limitations. He said:

> Our entire approach has been dominated by a desire to ensure Africanization of the economy and the public service. Our task remains to try and achieve these two goals without doing harm to the economy itself and within the declared aims of our society.[4]

One of the harms that was feared by the government was the discouragement of the inflow of private capital from overseas.[5]

A : OBJECTIVES OF AFRICANIZATION

1 Political Objectives

The Africanization of the economy and the bureacracy has had two main objectives. The first and immediate objective was a political imperative. This was the government's desire to be seen as actively correcting the imbalance that had been brought about by 70 years of racial discrimination by the British colonials against the Africans in particular. Except by a takeover of economic operations by the state, the only other way to excise these operations from the hands of aliens was through Africanization. Two phases in the process of Africanization since independence are clearly discernible. The first phase involved the most sensitive and politically volatile land question. The expectations of the masses had to be partially met by transferring part of the land to a portion of the landless masses.[6] This phase was largely dictated by the political expediencies of keeping the expectant masses at bay while the next phase was a more selective one. By 1965, the government had already decided to apply brakes on the infant scheme of land settlement for the landless masses. It had decided that in future economic benefits to the country should determine the pattern of Africanization of agriculture. It rationalised that:

> Africanization in agriculture has taken the principal form of land settlement ... This approach has been necessary for political reasons - to ensure that areas formerly closed to Africans were opened to them. These areas are now open to Africans;

> settlement policy should hereafter be based on its economic benefits and on Kenya's wishes and terms instead of those of the United Kingdom as has hitherto been the case. 7

Though the shift anticipated did not take place immediately, the ruling clique had clearly decided that in future, their interests rather than the clamour of the masses (political reasons) were to dominate the Africanization programme. It is interesting to note that the United Kingdom had dictated the terms of this first phase which, in some ways, was more in tune with the demands of the masses than the second phase.

Phase two of the process of Africanization was characterised by the dominance of the interests of the emerging African elite who were in total control of government policy-making, in as far as that was possible in an ex-colony highly dependent on external sources for its economic well-being. First came the policy of transferring intact the best land available in the highlands to individual or groups of rich Africans, while confining the settlement schemes, which catered for the poor, to marginal areas of the highlands. This meant that henceforth the best land in the highlands would go to the political elites who were the only people who had the political clout to obtain huge amounts of finance from the state to purchase the huge tracts of land.[8] Then came the assault on the Asian dominated commercial and distribution sector. This

included the distribution business carried on by foreign firms. The now increasingly economically ambitious African elite was poised to step into the shoes of the non-African commercial group. There was to be no mass participation in this phase and all the rhetoric about co-operatives in Sessional Paper No.10 of 1965 had long been shelved. Greed became the creed and the elites scrambled to take over the distribution and commercial sectors of the economy.[9] In this phase comes the government's participation in projects with foreign capital. A few African tycoons have now started moving into industries, although largely as junior or dormant partners with foreign capital.[10]

2 Control Objectives

In its policy statements the government has presented its Africanization policy as a measure for controlling or influencing the economic activities of private enterprise and, in particular, as an important measure for checking the dominance of foreign capital over the rest of the economy. Thus it warned that:

> ... the foreign ownership and management of productive assets could mean that economic decisions in Kenya might be dominated by foreign rather than domestic considerations. 11

It therefore felt that Africanization would limit such tendencies. Its recommendation was that foreign investors should be prepared to accept "the spirit of mutual social

responsibility" (sic!) by assisting in the process of Africanization.[12] In the view of the government, Africanization is a means of:

> ... establishing Africans in a firm position in the monetary sector by ensuring that a large share of the planned new expansion is African owned and managed. 13.

Given the fact that a substantial portion of the economy that was essential as a basis for new expansion was in foreign hands, it did not take long for the Africanization programme to concentrate on existing economic establishments.

An ad hoc committee of the Ministry of Commerce and Industry was more specific about the intended control functions of Africanization. It emphatically stated that:

> ... The Africanization of commerce and industry is the surest way by which Africans can hope to control the economy of this country. 14

This notion of Africanization as a means of wrenching the control of the economy from foreign capital has become a major part of government economic policy and has been pursued with some vigour.[15] It is this aspect or objective of Africanization that is the subject-matter for consideration in this chapter.

B : THE PROCESS

The process of Africanization falls into two main categories. The first is the Africanization of equity ownership in firms owned by foreign nationals[16] and the second is Africanization of personnel in such firms. In theory, the process is one of Kenyanization, but in reality Africanizing is the dominant theme and it is for this reason that the term Africanization has been chosen for use here. Both legal and administrative measures have been used to secure, or in support of, the Africanization of parts of the economy. In addition, the government has provided financial backing to the programme.

1 Equity

The Africanization of equity in foreign firms has taken four forms. First, those Africans with the means have purchased shares in publicly quoted foreign-owned companies. Second, the government has purchased shares in existing foreign operations or entered into joint ventures with foreign firms in new projects. Third, a few African tycoons have entered into joint ventures with foreign firms. Finally, there have been joint ventures involving foreign firms, the government and some local business and/or political elites. Government participation as used in this study refers to either direct investment by treasury or through any of the public development financial institutions or the two wholly government-owned commercial banks.

Initially, official Africanization policy laid emphasis on inducing foreign firms to 'go public' and thus enable Kenyans to buy shares in such firms. This approach had two main shortcomings. The immediate one was that foreign companies revalued their assets prior to going public. These revalued shares were then sold on the stock market and the proceeds repatriated. In addition, the revaluation resulted in a potential increase in the dividends that could be repatriated without a corresponding inflow of actual foreign assets. This was seen as a set-back on the government's need to conserve foreign exchange.[17] The other, and more important, shortcoming was that it was largely the non-Africans, both citizen and non-citizen residents, who were able to buy the shares offered to the public. Thus the government reduced its emphasis on the offer of shares to the public, but it did not actively discourage it either. With increased levels of accumulation by a few Kenyans partly as a result of the existing unequal distribution of income (see 1979-83 Plan, 5), the government feels that it can now achieve viable Africanization through the stock exchange. Thus it promises that:

> In order to enhance the role of Kenyans in industry, the Government will increase industrial services to small and medium-sized enterprises owned by Kenyans. ... Besides these measures, the Government will ensure that more companies will offer shares to Africans through the stock exchange. [18]

It is worth while noting that the reference is specifically to ensuring sale of shares to Africans. There is no indica-

tion of how the government expects to go about ensuring this. Certainly, no legislation has been enacted to achieve this end. If any pressure has already been applied to foreign firms to sell shares specifically to Africans, it is yet to be made public.

In commercial and transport operations, the government has used largely legislative means to achieve Africanization of these sectors. Owing to the constitutional guarantees to equal treatment for all citizens, the government has relied on the administrative machinery for implementing the legislation to give effect to the bias in favour of Africans. In commercial trading, the operative legislation is The Trade Licensing Act of 1967.[19] S.5(1) of this Act makes all trading business subject to licensing by the Department of Trade and Supplies. Subsection (2) bars any non-citizen from conducting business:

> a) in any place which is not a general business area; or
>
> b) in any specified goods unless his licence specifically authorises him to.

Thus the licensing system bars foreign firms from certain geographical locations and leaves discretion to the authorities on whether or not to bar such firms from trading in certain items. S.11 provides for what are termed as the 'principles of licensing', one of which is that, in issuing licences, a licensing officer shall:

a) be guided by the principle that businesses carried on in any place which is not within a general business area ought, where practicable, to be controlled by citizens of Kenya, and that specified goods ought, where practicable, to be dealt in by citizens of Kenya and, in particular, take into consideration:

   i) Where the activities in respect of which the licence is applied for ought to be and could be carried on by a business conducted by citizens of Kenya.

It is clear that this Act, rigorously implemented, would be a very potent instrument for the Kenyanization of commercial trading in Kenya. With the 'proper' exercise of its discretion, the licensing authority can ensure that, in practice, Africanization of the businesses concerned is achieved. The Act has been utilized a great deal, and its only limitation is whether or not its dictates are practicable. The 1979-83 plan states:

> Since Independence the Government has encouraged Kenyans to enter the commerce sector through various measures ... Notable among these is the 1967 Trade Licensing Act ... Partly as a result of this Act almost all businesses in rural centres have been acquired by Kenyans. In order to complete this programme, the Government henceforth will focus its attention on urban general business areas where non-citizens are still legally free to operate as traders. 20

In other words, the government has the intention of excluding virtually all foreigners from commercial trading in Kenya. It also promises to review the law with the view to closing the loopholes that have enabled non-citizens to survive in such businesses.[21]

In the transport business, the Transport Licensing Act[22] performs a very similar role. It set up a Transport Licensing Board (TLB) to consider applications for licences to engage in any road transport business. It issues licences in such a way that African applicants receive top priority. The regulations confer upon the TLB discretion

> To have regard whether an applicant is a citizen of Kenya, or if an applicant is a company, whether the members and its employees are citizens ... 23

It is this regulation that the TLB relied upon in 1968 when it threatened not to approve the annual renewal of licences for companies that had not sold 50% of their equity to the public. This was in reference to foreign private companies. The threat was sufficient to compel East African Road Services, the largest company owned by foreign capital, to comply.[24]

As far as banks and financial institutions are concerned, the government has not pressed hard for their Africanization. In the early 1970s there seems to have been a policy to Africanize the banking sector, but this seems to have changed. It was at that time that the government took over 60% of the National & Grindlays Bank Ltd., and also negotiated with the other two leading foreign banks for their merger with the government taking 50% of the merged bank. Had this merger between Barclays and The Standard Banks taken place as the government had intended, it would no doubt have spelt the end of the dominance of foreign

banks in the country. The move appears to have been aborted for some unknown reasons. It appears that the government became apprehensive of being seen to follow the Tanzanian approach, thereby deviating from its avowed policy of non-nationalisation of foreign investment. It has also been suggested that the banks had later changed their minds about the merger and, therefore, frustrated it.[25]

Instead, the government established another wholly-owned bank - The National Bank of Kenya - and later took over the remaining 40% in The National & Grindlays Bank Ltd. (now known as Kenya Commercial Bank) to compete with the foreign banks. In the meantime, it allowed the establishment of more foreign banks in the country.[26] There is, however, no doubt that the establishment of the two Kenyan banks has gone some way in Africanizing the banking system. Furthermore, the government has pledged that:

> Every encouragement will, however, be given towards local participation in the ownership of foreign banks operating in this country. 27

If need be, some of this 'encouragement' could be in the form of restrictions imposed on recalcitrant foreign banks.

In addition to participation in the banking business, the government has made several amendments in the rules and legislation governing banking business. One of these amendments introduces a discriminatory element between locally incorporated banks and those incorporated abroad. No

locally incorporated bank may be licensed to conduct business unless its paid up capital is KShs.10m.or more (up from KShs.3m). The corresponding figure for foreign incorporated banks is KShs.50m. (up from KShs.10m.). In addition, foreign banks are now required to keep within Kenya an assigned capital of not less than KShs.10m.[28] While merely incorporating locally does not make a foreign bank Kenyan (except in law), the requirement is designed to have the foreign banks incorporated locally as public companies so that local elites and public financial institutions can purchase part of the shares on the market. It is part of the 'encouragement' for local participation in the ownership of foreign banks.

A similar approach has been followed in the case of the insurance industry. The government has established the Kenya National Assurance Company to compete in the business while ICDC acquired 51% of the Minet Insurance Group to form Minet ICDC Ltd. There also exists local participation in other insurance firms. In addition to this, the government has used legislative means to take over part of the re-insurance business. In 1970, parliament passed the State Re-insurance Corporation of Kenya Act,[29] establishing the State Re-insurance Corporation, to which it gave a degree of statutory monopoly for the re-insurance of certain types of policies. Section 3 of the Act provides that:

> Every insurer shall re-insure with the corporation in such proportion as the minister may, by notice in the Gazette, prescribe of

> each policy, other than a policy of re-insurance, issued or renewed in Kenya by the insurer.

Under this provision, the Minister of Finance has required that every insurer re-insure with the corporation 30% of every fire and accident insurance policy issued in Kenya.[30] The scope and potential of utilizing this legislation to fully Africanize the re-insurance business is virtually unlimited. Its only limitations are the corporation's ability to cope and the government willingness to Africanize.[31]

In the case of industry, the government has so far not utilized legislative means to achieve Africanization, but has concentrated its efforts on administrative and political means as well as government equity participation to achieve its goal of Africanization. Unlike in countries such as India and Nigeria, Kenya has no legislation designating the levels of equity holding foreign firms are permitted to have in specified industry. However, this absence of legislative means does not mean Africanization has not taken place. A considerable degree of Africanization has been achieved since independence. The government has pursued Africanization of this sector mainly through direct treasury participation and through parastatal organizations.[32] The leading conduit for the government's Africanization of industrial capacity is the Industrial and Commercial Development Corporation.[33] It participates in joint ventures with foreign investors both in existing and new industrial capacity. Its participation was intended to

promote African ownership of businesses rather than public ownership and control of the same. Its 1965/66 Annual Report, for example, describes its functions as including:

> ... help to African industrialists and traders to expand their operations, and the promotion of overall Africanization of industry and commerce.

Five years later, this was still its major objective and the corporation claimed to have:

> ... relentlessly pursued its promotional role as an effective mechanism for the implementation of the Africanization of trade and industry in furtherance of government policy. 34

In pursuance of this policy, ICDC has bought equity in several existing private companies and entered into joint ventures with others in new projects. Thus, for example, as of June 1977, it had invested a total of K.Shs. 167,601,470/= in equity in 61 companies, only five of which were its wholly-owned subsidiaries. Of this investment, K.Shs.126,605,160/=, or 76%, was invested in just nine projects managed and controlled (regardless of equity holding) by foreign capital.[35] ICDC's total overall equity in these nine companies was 44%. Other parastatal institutions have made similar, though smaller, investments.[36]

Although the original intention was for ICDC to resell its equity to individual Africans, no such sale has taken place yet. However, in most of its agreements with foreign capital, ICDC's right to sell all or any of its

shares to the public (usually through its subsidiary company) without giving priority to its partners is expressly recognised.[37] In view of this, it may be that ICDC will in future divest itself of such equity by selling them to its publicly quoted subsidiary - the ICDC Investment Company Ltd. Some such sale has taken place, but the bulk of ICDC's equity in joint ventures with foreign capital is still held by the corporation.

A few individual African entrepreneurs have bought significant amount of shares in existing foreign firms and/or entered into partnership with such firms in new projects. However, this figure is still relatively small. No firm data exists except an unpublished study by Kaplinsky undertaken for the NCCK. This study of some 2,000 large-scale manufacturing firms shows that individual African entrepreneurs have as yet to seriously challenge foreign equity holding in industry.[38] In the words of the government:

> Whereas improvements in efficiency will open up more opportunities for Kenyans to engage in industrial activities, the Government recognizes (sic.) that the share of <u>industrial output contributed by Kenyan-owned industry is still very small</u>. 39

2 <u>Personnel</u>

The Africanization of personnel in foreign firms as well as in all employment sectors has been a major policy objective of the government since independence.[40] Indeed, the government had 1982 in mind as the target date for a

complete Kenyanization of employment in the 1974-8 Plan; it observed that:

> The Kenyanization programme deserves special mention in the employment context for two reasons. First, the Government has made significant progress towards the achievement of its target of complete Kenyanization by 1982. In 1967, only 59 per cent of all posts and middle level manpower posts were held by citizens. By 1972, 74 per cent of all posts in those categories had been Kenyanized; only 25,000 non-citizens remain in such jobs. 41

The major legislative instrument used by the government to pursue the Africanization of personnel has been the Immigration Act of 1968. The Act makes the employment of non-citizens subject to government regulation by requiring that they obtain a work-permit from the Department of Immigration. Section 18 of the Act makes it illegal for any employer in the country to engage a non-citizen without a work permit, while Section 19 makes it illegal for a non-citizen to be employed without a permit. The stated government policy has all along been that work permits should not be issued to non-citizens for jobs for which qualified Kenyans are available. Here too the Africans have received priority and policy has, in practice, largely been one of Africanization. The permits are issued for short durations of approximately one to three years, thus giving the government a chance to replace non-citizens with Africans as soon as the latter become available.

To speed up the programme, the government set up the

Kenyanization of Personnel Bureau in 1967, under the Ministry of Labour, to advise the Immigration Department on the availability of local personnel for jobs in the country. The Bureau, which was abolished in 1981, built up a manpower register of citizens available for all types of jobs falling vacant in the economy. The intention was to keep the Department of Immigration well informed to enable it to decide in which cases to renew and those to refuse to renew the permits of those non-citizens that have expired or to fill up new posts. The Bureau's role was only advisory in nature, but it did exert some pressure behind the scenes on foreign firms to Africanize their management. Swainson states that the Bureau was consulted on the question of training and personnel in the preparation for management contracts.[42] This is, in fact, not the case in as far as the present author has been able to gather in the cases studied. In most cases, the foreign managers include a list of the posts they need to fill with expatriates and demand that the government issue work permits for them.[43] Indeed, neither the Bureau nor the Ministry of Labour was ever represented in the NPC or any other body negotiating management agreements. Contrary to Swainson's argument, none of the more than twenty agreements containing provisions for training of manpower has any schedules that can be termed 'strict' for the provision of training schemes for local personnel. In fact, the training provisions in the relevant agreement of the major concerns mentioned in Swainson's work do not contain any specific training schedules.[44] Most of the

training provisions are ambiguous with the manner, type, extent, duration and even cost of any training conducted being left largely to the discretion of the foreign manager or technical collaborator.[45] However, even with the agreements being weighed against a vigorous enforcement of the training obligations of the foreigners, the Bureau did exert some informal pressure on firms to Africanize and to expedite their training programmes.

The government has also used its equity holding to expedite Africanization of management in ventures involving foreign capital. Where the government has no equity holding, some form of political pressure may be exerted in achieving a certain amount of Africanization. Largely because of the government's Africanization of personnel policy, the employment of Kenyans grew at a rate of 5.2% as compared to an average annual growth rate of 4.5% in total employment between 1968 and 1977. Over the same period, the employment of non-citizens was being reduced at an average annual rate of 10.7%. While in 1968, non-citizens comprised 7% of total modern sector employment, this proportion had fallen to 1.7% in 1977.[46]

Despite the success in Africanizing a substantial proportion of equity and personnel in operations involving foreign investment, its effective regulation and control has proved rather elusive. Students of the Kenya economy are agreed on the view that Africanization per se has not led

to significant levels of effective regulation over foreign investment.[47] Both the 1971 ILO and the 1974 IBRD missions to Kenya are also agreed on this point. So does the government, which observes that:

> Control over the nation's resources and institutions has progressively passed into Kenyan hands ... But as progress is made on the Kenyanization of assets, the need to examine the functions of the institutions coming under Kenyan control assumes greater importance. Many of those institutions were initially established to serve foreign rather than domestic interests ... to channel savings abroad instead of domestic investments ... The functions of these institutions must now be redefined to serve Kenyans rather than expatriates and to serve all Kenyans rather than the few. [48]

The considerable Africanization so far achieved has, therefore, not been very successful in effecting structural changes in the operation of the businesses involved to radically alter their pattern of behaviour. The notion of Africanization as a method of regulating and controlling foreign investors is based on the traditional assumption that owners of capital exercise control over their investments either directly or indirectly through their representatives on the boards of directors.[49] This assumption has been questioned and sufficiently shown that it does not necessarily apply in the twentieth century business environment.[50] However, the Kenya government believes that:

> Government participation also provides an opportunity to influence the direction of

> company policy in accordance with general industrial strategy. 51

This view is predicated upon the premise that boards of directors effectively execute their legal role as the policy-formulating bodies in companies. In Kenya this is rarely the case where foreign investors are involved. There are three major reasons for the failure of Africanization as a means of regulating and controlling foreign investment. These are: the use by the foreign parties of non-equity means of exercising effective control; the incompetence of the Africanized boards of directors; and an alliance between local capital and political elites, on the one hand, and foreign capital on the other. The remaining part of this chapter is devoted to an examination of these three items.

C : EFFECTIVE CONTROL THROUGH NON-EQUITY PARTICIPATION

There is no denying that it may be a lot easier to exercise control over a 100% owned subsidiary than a 50% owned one. Where such complete ownership is politically unfeasible, or even unwise, foreign investors have increasingly come to learn and appreciate that local majority equity ownership is not necessarily a bar to their exercising effective control. It has been observed that:

> ... although a number of foreign investors ... feel that voting and technical control should always be linked, a majority of them consider their technical superiority an

> adequate means of exercising a lasting *de facto* control over the foreign joint ventures where they are in a minority position. 52

Foreign investors in Kenya and other underdeveloped countries have been able to sufficiently alienate powers of control from boards of directors by playing upon the notion of the indispensibility of their supposedly superior management , technical and marketing skills.

1 Management Control

The device of a management contract between joint venture projects (or even wholly-owned Kenyan ones) and foreign parties is one of the most frequent channels for alienating much of the control over a project from the boards. In most cases the managers are also equity holders in the project. There seems, in government circles, a rather credulous belief that the interests of the foreign parties as managers and their interests as owners can be and are reconcilable. This assumed neutrality of managers is, however, not supported by empirical evidence. Indeed, such empirical evidence as is available suggests that foreign parties use their role as managers as a strong counteracting force to the potential exercise of control by local equity holders. To the foreign investor, a management contract is an important instrument for retaining control over an enterprise in which it may have lost majority shareholding.[53] The most significant feature of all the 25 management agreements studied in Kenya is the

alienation from the boards by management, under the terms of the agreements, of effective control over the affairs of projects. The foreigners regard such contracts as so vital to their interests that they insist on their appointment, or that of their nominee, as managers of the projects irrespective of whether they hold minority or majority equity. They make their appointment as managers a condition precedent to their equity participation.[54] In two of the cases studied, it is revealing to note that the foreigners had specifically insisted on EITHER MAJORITY equity or a minority equity with EXCLUSIVE management rights and powers. While some of the agreements stipulate the foreigners' exclusive rights to management, others stipulate their exclusive rights to hold specific positions in the management of the project for as long as they remain equity holders in the projects.[55] One of them, for example, stipulates that:

> KRKA shall provide DA with their experts to assist DA in modern type of business organization. Their experts will be as managing director and marketing manager, and will remain in their posts for so long as KRKA is a shareholder in DA (emphasis added).

Unless their equity is taken over, the foreigner's control of what they take to be the key positions to suit their interests in this particular project would appear to be aimed at being perpetual.

The foreigners do not only insist on being appointed

managers, but in addition insist on management being given virtually unfettered powers to manage. They draft the agreements in such a way that they give themselves wide discretionary powers in running the project while limiting the boards' effective supervisory powers over them.[56] These powers comprise both general rights and specific prerogatives of management. The managers are, in all cases, said to be solely responsible for day-to-day management for which they enjoy an immense degree of autonomy from the boards under the agreements. In the 25 management agreements studied, day-to-day management is said to include sole responsibility for

- training of Kenyan personnel (25)
- hiring and firing management personnel (18)
- preparation and implementation of production programmes (25)
- formulation of management and financial control systems (19)
- preparing financial budgets (23)
- negotiations and conclusions of all contracts with third parties (14)
- marketing (8)
- selection of engineering and technical consultants (14)
- selection of machinery and equipment suppliers (17)
- purchase of raw materials (20)
- preparation of feasibility, market and other studies (9)

It is clear that the agreements deal with all the important

issues falling to be decided in the projects. The only limitation is the stipulation that the managers are to operate within the framework of the general overall policy and consistent with the directions and instructions which may from time to time be given and subject to the control and supervision of the board of directors. In the Kenyan circumstances, as we shall see later in this chapter, the supervisory role of the boards is largely illusory.

There is little doubt that the rights and powers given to managers under such agreements play a very vital role in the shaping of the balance of power between Kenyan and foreign partners. I asked one of the representatives of the foreign managers why they insisted on the management agreement that gave them so much discretion in managing the firm. He answered without the slightest hesitation that this was to 'safeguard' their investment, adding that:

> we are a minority shareholder as you may be aware; we have no hope of influencing or shaping company policies using our voting power. The majority shareholder is the government. If voting power were to be used to appoint managers, we would be outvoted. This would not matter very much if the management were efficient, but if it was not, we would be the uncompensated losers ... so we insist on managing the firm to ensure efficient management for our own good and that of the Kenya government.

Shorn of its rationalisation element, this is an admission that management has a vital role to play in 'safeguarding' sectoral interests. In this particular case, the government has consistently been the loser while the managers

(whose two affiliated companies are equity holders in the project) have dictated the course of events in the project over the last four years. A government-commissioned audit of the firm concluded that the management and its affiliates were the only beneficiaries of the project so far, with the board having played ball all along. From the point of view of effective control, management agreements would appear to put the Kenyan partners at a significantly disadvantaged position right from the start, by leaving key decisions to the discretion of the foreign management.

2 Control over Technical Matters

Like in the case of management, technical agreements play a crucial role in the determination of the balance of power in exercising control over any project between the local and the foreign partners. They are an integral part of foreign investors' arsenal of non-equity means of exercising control over investment projects. As in management, foreign investors usually insist on their, or their nominee's, appointment as the technical collaborator in projects. In 16 of the 25 projects studied, one or more of the agreements (investment, promotion, technical, etc.) stipulated such an appointment as a condition precedent of their equity participation. One such agreement provided:

> CIC agreed to invest K.Shs.42.5m. in the venture upon condition (inter alia) that PEC shall enter into a Technical Engineering Agreement (TEA) substantially in the form set forth in Annex I hereto ...

In this example, the foreign party has also made the acceptance of his draft TEA as a condition precedent to investing in equity. The terms in the TEA agreement are heavily biased in favour of the foreigner, through PEC, exercising control over the project that is disproportionate to his 34% equity holding.[57] In the remaining nine projects, the foreign party or his nominee has been appointed technical collaborator although the appointment apparently appears not to have been a condition precedent. In seven of those cases, the appointments are on exclusive basis, while one of the last two agreements is silent on the issue of exclusivity. The agreement in the last provides interesting reading. On the one hand it provides for the appointment of the foreign party as technical consultants, provided:

> ... the said appointment in relation to Art. 6 [optional services] shall not be exclusive ... BUT PROVIDED FURTHER that EAPC will give BCI one month's notice in writing of its intention to appoint or enter into any agreement with any other technical organization ... in respect of the duties covered by the said article. (emphasis added)

The said Art.6 provides that at the request of EAPC, BCI would 'be prepared' to provide the relevant optional services. From this, one may deduce that the notice provision is, in effect, a requirement that EAPC give BCI first option to provide the services. Should BCI exercise this option, then the 'powers' of appointing other consultant organizations by EAPC would be more apparent than real. This seems to be the case in practice.[58]

The terms of the technical agreement studied give wide powers to the foreign collaborators including those of:

- training of technical personnel (23)
- choice of technology input, including where to obtain and who to supply the technology (24)
- determining size of production unit (25)
- choice of products (11)

In all these very vital aspects of any investment, the Kenyan projects are entirely reliant on the foreigners' technical and technological resources. By making the supply of such resources exclusively the right of one or more designated foreign firms, the agreements greatly reduce the range of choice available to the Kenyan projects in related matters. For example, Firestone's exclusive Process and Licensing agreement's terms meant that the Kenya tyre plant could not utilize Goodyear, Michelin, Uniroyal, etc. resources, even if they could prove cheaper and of a better quality than those Firestone International offers in Kenya. The ability of the Kenyan boards of directors to exercise control in determining the type of technology input is therefore nullified by the terms of the agreements right at the outset. Tie-in provisions and export restriction clauses in technical agreements are two specific examples of outright nullification of the boards' power of control over company affairs.

Tie-in provisions compel Kenyan firms to acquire

from their foreign technical collaborator or from sources specified by him either one, a given combination, or all of the following items: raw materials, machinery and equipment, intermediate inputs, process and/or product technology, technical and/or managerial knowhow, other accessories such as packaging materials, brand names, etc., and any other relevant purchases to be made in relation to a particular business. Such tie-in provisions are either explicitly or implicitly included in technical agreements. In 19 of the 25 agreements studied in Kenya, the tie-in is stipulated in express terms. An example is to be found in a Technical Assistance Agreement in one of the motor assembly projects. It requires that:

> FARAGHA Kenya, within three years from the date of this agreement, will assemble one or more of the motor vehicle models ... from CKD component packs which it will purchase from MRIJA MKUU.

The foreign party also had an exclusive right to supply machinery and equipment. Even in personnel training, the agreement ties the Kenyan firm to the foreign technical collaborator. The remaining six agreements do not explicitly tie the Kenyan firms to purchasing items from the foreign collaborator, but they nevertheless do so implicitly. This is cleverly done by giving the foreigner exclusive right and responsibility for providing plant design and specifications for machinery and equipment as well as for the purchase of the same.[59] Such provisions do not provide the foreigner with a contractual right to supply

anything, but they give him (not the board) the right to determine who supplies what. In the absence of a provision excluding the foreigner from designating himself or his affiliate as the supplier, he is free to so designate himself. The important factor here is that a traditional power of a board is nullified by contractual terms and granted to the technical collaborator.

Export-restriction provisions nullify a board's power to mark out its marketing strategy and the geographical scope of its application. They are a common feature in technical and trade mark agreements. The policy of allocating markets to those they can exert control over is a long-standing practice of virtually all foreign investors.[60] Vaitsos, for example, found the practice very prevalent in Colombia, while O'Brien observed the same practice in Spain.[61] In the Kenyan case, export-restriction provisions occurred in varying degrees of strictness in all the 25 agreements examined. They all prohibited, either absolutely or without the permission of the foreign technical collaborator, the production or sale by the Kenyan firms of the products produced utilizing the foreigner's technical assistance outside the geographical limits specified in the agreements. In one extreme example involving Coca Cola, the sale of the products was restricted to within a radius of 30 kilometres.[62] Thus the power to formulate an export policy is, under all the agreements, either taken away from the boards or severely limited. It is difficult to see how

the Africanization of the 25 firms involved in this study can assist in the achievement of the government's commendable new economic thinking to the effect that:

> Future industrial growth must be based increasingly on the penetration of export markets. This plan period will be used to effect the transition from an industrial sector primarily serving the domestic market to one that is actively and competitively engaged in export sales. This will require substantial increase in productive efficiency, appropriate export incentives and aggressive export-oriented management. 63

Without the removal of the pervasive export restrictions or their being legally outlawed, such export-stimulating strategies are likely to lead only to increased exporting capacity without export markets.

3 Marketing Control

Marketing is a vitally important phase of any business. It comprises the promotional and sales operations of a firm. The promotional aspects of marketing involves bringing to the attention of buyers of a given commodity as well as persuading them to buy one's product in preference to those offered by competitors (if any). This is done chiefly through advertising. Product promotion is particularly intense, and therefore very important, in branded products where several competing substitutes exist, as in the case of toiletries or soft drinks. The foreign parties utilize trade-marks and/or trade names agreements to exercise control over domestic marketing. In export markets,

the foreigners usually utilize marketing agreements to reserve marketing decisions to the virtual exclusion of the boards. The most extensive and far-reaching of domestic marketing control by the foreign investors is so far in matters related to promotional activities. Fourteen trademarks and/or trade names agreements were examined in this study. They all contained elaborate provisions for the rights and powers of the licensor to literally dictate marketing procedures and strategy to the Kenyan projects. These mandatory provisions give extensive powers to the foreigners to determine the advertising campaigns, including minimum costs to be incurred,[64] product packaging and labelling,[65] pricing, etc.[66] In one case, for example, the agreement requires the licensee:

> To submit to the owner of trademark for approval, prior to the use thereof, all packaging, labels, advertising and other material on which the said trademark appear and to amend to the satisfaction of the owner any such packaging, labels, advertising and other material.

It is very doubtful whether the board of such a firm has any powers left to it in marketing matters independent of the foreigner who is a minority shareholder, but has effective veto power.[67]

The creation of goodwill for the foreign trademarked goods is given high priority to the extent of expressly prohibiting the Kenyan licensee from selling products under its own brand names. Four of the fourteen

agreements include such express prohibition clauses.[68] Again, in such cases the board can hardly be said to be in control of product diversification through product differentiation. The trademark laws in the country granting firms rights to differentiate their products is thus clearly rendered of no practical use to the Kenyan firms except in so far as the foreigners approve. And they do this to suit their interests. In addition to prohibiting use of independent brand names, some trademark agreements also include express tie-in and export-restriction provisions as well as quality control provisions designed to strengthen the foreigners' control over domestic marketing.[69]

In export marketing the agreements simply grant a monopoly of such marketing to the foreigner in all cases. Four such agreements were examined, all of them in what is usually referred to as the export sector. The philosophy underlying this grant of exclusive export marketing rights to foreigners appears to be the belief that the services of an 'established' international firm is an indispensible key to success.[70] Thus in one of the cases, for example, notwithstanding ICDC's reservations about the services offered by the foreign parties, "in particular as to whether it was desirable for B to be the exclusive marketing agent",[71] the agreement appointed the foreigners:

> ... to act as exclusive agents export for the marketing of all of the products produced at the plant ...

The reason for granting such monopoly marketing rights despite the serious misgivings expressed about the foreigners appears to be the belief of the indispensibility of their services in the marketing of the products abroad.[72] Indeed, they were, in this case, the only market, as they were to buy all the Kenyan firm's export produce.

In all the four agreements the marketing agents had total and exclusive control over the marketing of the products abroad. The Kenyan majority owned firms who produce the products have no say at all, under the agreement, in this matter. The boards' powers over export marketing had effectively been ceded to the foreigners and Africanization was therefore of no consequence in this matter. Not a single one of these agreements provided for the effective supervision of the agents in their execution of their marketing obligations. In one celebrated case, Kenya Canners Ltd., the foreigners went much farther than utilizing their marketing skills and rights to alienate export marketing powers from the board. They used them to de-Kenyanise the firm.[73]

D : INCOMPETENCE OF BOARDS

The imcompetence of many of the boards appointed to projects involving local capital is a significant contributory factor to the failure of Africanization as an effective means of regulating and controlling foreign investments. There are several factors that account for the

boards' ineffectual exercise of control. Some of these also affect the ability to exercise control through the Africanization of management personnel. The incompetence observed in boards has little to do with inherent incompetence of the individuals involved, but is largely the function of the environment in which they operate. As we have already noticed, many key issues in business operation have been taken away from the jurisdiction of the boards or the African management personnel and given to the foreign parties. Such contractual terms render the boards, as well as African managers, short of acting in breach of the agreements, legally incompetent to exercise any control over such matters. In addition, even where the board has the legal power to act, the power of the majority shareholders so to act in key issues may be nullified by a stipulation that such decisions require not a majority vote, but a unanimous vote of the board.[74] This, in effect, gives the minority foreign shareholders a power of veto over such issues. In such a case, the only effective Africanizstion is a 100% equity takeover. In two other joint ventures in which the government holds a 51% and 60% equity, a much more subtle approach was adopted by the foreign parties. The two projects have common managers and technical collaborators and their joint venture and other agreements are virtually identical. The management has no equity in any of the projects. However, the joint venture agreement in each case gives it the right to be represented on the board. The agreements provide for the right of the government to

have three directors on the board and the two foreign parties two. In addition, the management is entitled to have a representative director. Thus, in reality, in spite of being the minority equity holders, the foreign parties have managed to obtain equal representation on the board by having the subsidiary of one of them as the management with a right of representation. The required quorum is five, three of whom must be the foreign parties.[75]

The sometimes complex technical and financial nature of projects may render boards incompetent in as far as the ability of the members to absorb and critically analyse the myriad technical and financial aspects of a given project is limited. This is confounded by the fact that the day-to-day management of projects rests with the foreign parties or their affiliates under management contracts. So also do the technical details for which the foreigners are usually responsible under the relevant technical agreements. This means that the boards must, of necessity, rely on information, data and recommendations of the foreigners. Although the boards are legally responsible for the formulation of overall policy, this is in fact no more than a line of action based on the analysis of aggregate day-to-day factors over a period of time for which the board must rely on the foreigners. For a board to be effectively in control of the policies of a company, it would need to have access to all the correct relevant data and other information, as well as its membership being

able to make critical analysis of the same and reaching intelligent conclusions. In the majority of cases studied the Kenyan directors are simply unqualified as entrepreneurs in the fields to which they are appointed. Most of them have no experience whatsoever in the line of business they are involved in. They hold their directorships in the companies by virtue of either their jobs in the civil service, political connections, wealth or a combination of these. For example, in 1975/76, the local directors of the East African Oil Refineries included an MP, two permanent secretaries and a government official, none of whom had any experience in the oil industry, and all owed their appointment to the board to their positions in the political system. Many such boards are, therefore, more likely than not to accept the management's version of issues and to adopt the latter's recommendations. By contrast, the foreigners' representatives on the boards are usually always technically qualified and well-seasoned in the line of business in which they are appointed. It is virtually impossible for Kenyan directors to utilize their positions on the boards to formulate policy and exercise control over business operations about which they know next to nothing. In addition to their lack of experience and technical qualifications, most of them are simply overloaded and, therefore, severely handicapped by their other commitments. A handful of local businesses and political elites are repeatedly involved in a number of projects because the government has been reluctant to appoint representatives

from without the mainstream of the bureaucracy. This leaves the Kenyan representatives spread too thin to pay the detailed attention to the affairs of their projects which is required to ensure effective control. In Rivatex, for example, by 1979 the nine Kenyan representatives (including alternatives) on the board simultaneously held between them 125 'other' directorships, while the seven foreign representatives held between them only 14 'other' directorships. One Kenyan, for example, held in 1978 sixty-one directorships, over 70% of which were in joint venture with foreign companies and covered a very wide range of business activities.[76] If one adds the lack of technical qualification and business experience to such an overloaded system of directorships, it becomes easy to appreciate why Kenyan directorships on boards have hardly had any significant effect on joint venture company operations. The views of one public institution official deputising for his boss as an alternative are revealing; he thinks that:

> There is little Kenyan directors can do to control the management. The managers are professionals in their fields and so are the directors of the foreign companies sitting on the boards. Kenyan directors on the other hand hardly have any business experience. They are appointed by virtue of their positions in the civil service or in these public institutions. Quite frankly many boards sit to rubber stamp the managers' suggestions. 77

E : ALLIANCE WITH FOREIGN CAPITAL

In 1965, the Kenyan government gave unsolicited advice to foreign investors on how to survive in an independent Kenya. It advised them that:

> Foreigners have no vote in Kenya and can only have a political voice now that independence has been achieved by enlisting the support of Kenya citizens. 78

This was a clear invitation to the foreign investors to enlist the support of key political figures to help them feather their nests. The foreigners were quick to adopt this advice, as they have done in other countries. The relative success of the government's Africanization programme is, in many cases, a result of the foreign investors heeding this rather frank advice. In an administered economy as exists in Kenya, political support by persons or groups with influence over the powers that be has become a 'commodity' much sought after by foreign investors. Empirical evidence gathered by recent students of the Kenyan economic system suggest that foreign capital has had substantial success in obtaining such relatively unqualified support.[79]

While to the government Africanization represents an instrument of control, to the foreign investors it has served as a useful instrument of decontrol. They have, therefore, supported the programme and in most cases insisted on domestic participation. This has led to the

forging of quite a strong alliance between foreign capital and powerful local political forces.[80] Foreign capital has long realized that while it might be much easier to exercise control over a wholly-owned subsidiary, domestic participation in their ventures offers a useful and reliable insurance against political risks.[81] This is true not only in Kenya but also in other countries. Thus, for example, in the wake of the Zambian nationalization of the copper industry in 1969, the Economist was quick to point out that:

> The shrewdest businessmen in that part of the world [Africa] have argued for some time that 40 per cent stake in a business whose success is underwritten by government participation may be more valuable than 100 per cent of a concern exposed to all the wind that blows. Companies that have anticipated the direction of events and invited the government into partnership have no reason to regret Zambian investment. 82

In Kenya, many foreign investors have not been unwilling Africanizers. Rather they have strongly pressed for domestic participation[83] and actively Africanized their management with Africans sympathetic to their cause. The alliance forged between foreign capital and the powers that be through the Africanization programme has provided the former with a workable insurance policy against unfavourable government interference, as well as providing one for government interference favourable to their cause. One recent study has observed that:

> By making available relatively large sums as both equity and loan finance, by a record of minimal interference in the workings of the firms, and by substantially reducing the

> firms' risk by providing vital contacts and a powerful ally in the firms' negotiations with the government, parastatal investments make attractive investment partners. 84

For such foreign firms, Africanization is a "painless and antiseptic" way of responding to government control[85] or for pressuring the government to grant further concessions whenever needed. Thus, for example, in one case where one such company wanted the government to block a competitor from establishing production facilities as well as importing the product, the firm applied for such protection. It sent a copy of its application to its parastatal partner with a request for the parastatal to pressurise the Ministry of Industry to grant such protection. The parastatal immediately responded with a letter to the director of industries pointing out that:

> As you are aware we have financed up to 40% of ... a company that has been producing a range of ... for the last 9 months. The installed capacity is enough to supply the local market with all types of ... As a condition of disbursing our loan we received some indication that the government was going to give the required protection by way of referring all applications for importation of ... to messrs ... for letters of no objection, ... We would appreciate very much if this company is accorded the requisite protection. 86

The company got what it wanted; a veto power over the importation of competing products, as well as blocking the establishment of a competing plant.[87] In another case, a company applied for the following protection:

- a ban on all import of all refined salt for two years.

- a decrease in duty on coarse salt, which must be considered as an industrial raw material, from 30% to 15%. 88

- increase in duty on refined and vacuum salt from 30% to 60% after the expiration of the two-year ban.

In its letter to the government containing those demands, it argued thus:

> First of all we wish to point out that the majority of the equity of our company is owned by ... two parastatals

The two parastatals duly supported the demand formulated by the foreign managers of the firm who were also the minority equity holders and the exclusive suppliers of coarse salt to the Kenyan firm. The use by the foreigners of local partners or personnel as channels for obtaining privileges and concessions from the government was found to be extensive as well as frequent in the present study.[89] In some cases the 'lobbyist' role of the domestic partner was expressed in contractual terms. Appendices 1/2 contain extracts from two joint venture agreements showing the 'lobbyist' role assigned to the domestic equity holder.

The alliance between foreign capital and the powers that be is cemented by the incorporation of key figures from the political mainstream or the civil service into the foreign managed business operations. This is achieved through offers of executive management posts as well as passing on increasingly large crumbs of the profits from the excessive profits derived from the business. Many senior

government officials and other political heavyweights have either a few shares in such companies or have lucrative contracts for the supply of local inputs to the foreign-managed firms or for the distribution of their products. The selection of the personalities to be incorporated is carefully done on the criteria of their potential abilities to deliver the necessary influence over the powers that be. A poignant example of the cementing of such alliance occurred in 1976, when a prominent multinational company operating in Kenya decided to issue one million shares to the public. The company valued the shares at 15/= on the basis of its 1975 profitability, but intended to sell them at 13/=. However, the book value of the shares in 1975 was 8/65. In a confidential circular to selected prominent Kenyans occupying key decision-making posts, the company offered blocks of 2,000 shares to each of the selected few at the par value of 5/=.[90]

In the Africanization of personnel, the foreign investors find another channel for cementing their alliance with the local bourgeoisie who wield political power. Appointment to the very senior executive posts are usually offered to Africans with close personal relationship with those in positions of authority.[91] As for the rest of the management and technical personnel, the new personnel becomes increasingly company oriented in their thinking rather than defenders of national interests. They therefore absorb and adopt the foreign parties' management philosophies and

styles while seeking to make little change of any significant consequence to the operation of the companies in whose management they participate. A major factor in producing loyalty to the company first rather than to the nation is the material benefits that go with appointment to managerial positions in foreign-managed firms. Conformity to company views and policies as espoused by the dominant foreign parties is an overriding prerequisite to reaching the top level of management in such firms. Thus one gets appointed to such posts not because of his exhibited potential to assert local shareholders' control over the foreign managers, but because of those that exhibit his loyalty to the company as run by the foreigners. This is one of the reasons why the foreign management have sought and obtained wide discretionary powers in matters relating to the appointment, promotion and training of personnel.[92] The financial returns that go with such appointments are so high compared with those available in any other sector that the price of opposition to company policies can be financially very high indeed. As the ambition of a lot of those joining the ranks is to acquire the affluence enjoyed by their foreign counterparts, the high financial returns constitute enough attraction to stifle any nationalistic feelings they may entertain. One African marketing manager of a Swiss-managed company in Kenya told me that he would only consider accepting another job if it offered him a monthly net income of 20,000/=. He explained that:

> I earn over 12,000/= a month; I have a fully maintained company luxury car, my three children have their fees paid for by the company in exclusive schools, I have a company house, I get a good bonus every end of year. Where else would I get such incentives? In any case, even if I would, would I not have to conform to my superiors' policies? If I have to serve under patronage, I would rather serve here, where the returns are better.

There are many Kenyans who feel like that and who aspire to such positions and the financial returns.[93] Their controlling role is thus obviously limited by their pecuniary interests. In his 1975 path-breaking work on the Kenyan political economy, Colin Leys observed that:

> After talking to a number of leading foreign companies' senior personnel, one became conscious that external control was really less important than the socialization of the new African executives into their roles as foreign-company managers. None of the managers I talked to, African or expatriate, thought that complete Africanization of top management would entail any significant change in company policies ... In retrospect, what strikes one as significant is that in the course of many discussions no senior African executive mentioned this issue, of control over fundamental company policies <u>and in general it was the identity of views of African and expatriate executives that was remarkable, not the differences</u>.[94]

Years later, the present author found little evidence to suggest the contrary. Even in 1982, African personnel are still being appointed and socialized in foreign-managed firms.

F : CONCLUSION

This chapter has discussed the government's Africanization programme as an instrument of regulation and control over foreign investors. I have shown that the government believes that Africanization would give Kenyans a greater say in running the sections of the economy hitherto dominated by foreign investors. This view is not shared by independent observers, including the ILO 1971 mission to Kenya.[95] Having outlined the pattern the Africanization programme has assumed, I have endeavoured to show that though it has no doubt reduced the volume of foreign ownership to a level below which it would otherwise have been without the programme, it has nevertheless not resulted in the achievement of effective control over foreign investment. It is clear that foreign investors have increasingly come to rely on non-equity channels of exercising control with enviable success.

Another factor discussed in this chapter is the use which foreign investors have made of the Africanization programme to feather their nests in Kenya. It is clear that they have achieved considerable success in their use of Africanization to ward off possible control by the government and as a medium of extracting vital concessions from the government. Those African representatives of domestic owners have consisted of the elite group in the society and have proved, at times, unresponsive to national priorities

or even government objectives, either because they were or had been rendered incompetent to exercise any significant control or because their pecuniary interests have compromised them into an alliance with foreign capital.[96] Where local participation takes the form of subscribing for shares on the stock exchange, the dispersal of a majority local ownership among a number of equity holders has created a passive non-unified group, a factor that has assisted minority foreign interest to perpetuate its control position with ease.

In the context of Kenya's discretionary and ad hoc system of regulatory mechanisms and interventions, Africanization has provided foreign capital with useful allies in pressurising the government to exercise this discretion in favour of projects they manage and control in the country. This guarantees their profitability, which is their primary objective in investing their funds in Kenya.

N O T E S

1. SP 10/65 p.11
2. T. Mboya, 1969, pp.202-3
3. SP 10/65, 27
4. Ibid. Introduction by Kenyatta.
5. See for example Ibid at p.14
6. For more details see C. Leys, 1975; A. Hazlewood, 1979; J.B. Harbeson, 1966; V. Vinnai, 1973; Gachuki, 1976.
7. SP 10/65. 28
8. For details see A. Njonjo, 1978
9. 'Elitinisation' would better describe this phase. The small shop-owners in rural areas and those in urban slum areas escape this elitinisation because of their relatively low returns.
10. For details see Kaplinsky's works; Langdon, 1976; Swainson 1980; Leys 1975; Marris and Somerset, 1971.
11. SP 10/65, 13
12. Ibid.
13. Ibid. at p.30
14. Ministry of Commerce and Industry, Report of an ad hoc Committee, 1970
15. See for example 1970-74 plan pp.9 and 316; 1974-8 plan pp. (i), 2, and 41; 1979-83 plan pp.6, 27; etc.
16. Some operations owned by Kenyan citizens of non-African origin were also taken.
17. For a useful example of the Canadian subsidiary E.A. Packaging Co. Ltd., see Leys, 1975 p.129
18. 1979-83 Plan, 29. (emphasis added)
19. Act 33 of 1967
20. 1979-83 plan p.375

21. Ibid. at p.376. The major loophole appears to be s.2(2) (b) of the Trade Licensing Act which defines a citizen corporation thus "a corporation is a citizen of Kenya if more than ½ of its capital is held by or on behalf of persons who are citizens of Kenya."

22. Cap.404, Laws of Kenya.

23. Transport Licensing Regulation 15(3). L.N.264/1968. Although the regulation refers to 'citizens', the TLB has always sought to use it as a basis for executing the government's Africanization policy in the transport business. In one case, for example, the board made a distinction between citizens of different origins and, therefore, refused a licence to those of non-African origin because this would be in contravention of its avowed Africanization aim. Certiorari went from the High Court to quash the decision, the Court holding that the refusal was unconstitutional. (Shah Vershi Devshi & Co. v. TLB) (1971) EA 289.

24. See Leys, 1975, 128

25. The first of these two possible reasons for the failure to effect this arrangement was suggested to me by Steve Langdon in his comments on the first draft of this work. This is the impression he got from his interviews with government officials in his 1971/73 survey on multinational corporation in Kenya. The second was given to me by a senior African manager in one of the two foreign banks involved. He expressed the view that the banks may have pressurised the government to abort the plan.

26. No less than 8 new foreign banks have set up business in the country since 1972.

27. 1979-83 plan p.72

28. See 1980 Budget Speech, at p.10

29. Act 20 of 1970

30. LN 233/1970 abd LN 265/1971. The initial percentage was 20%

31. The indications are that the squeeze on insurers will continue See 1979-83 plan p.71

32. Examples of the former are KCFC, KFC, and Mumias Sugar Co. ICDC and IDB, between them, hold 30.5% of the issued capital of the 23 biggest industrial firms established in Kenya since independence (see their 1979 Annual Reports)

33. It was set up in 1954 by the Industrial Development Ordinance of that year. Its present statutory form was provided for in the 1967 Industrial Development (Amendment) Act which also expanded its interests to cover the commercial sector.

34. ICDC 1970/71 Annual Report.

35. ICDC 1976/77 Annual Report. The nine were:

Fluospar Co. of Kenya Ltd	51% ...	Kshs21,942,280/=
General Motors of Kenya Ltd ..	51% ...	Kshs12,535,000/=
E.A. Fine Spiners Ltd	65% ...	Kshs15,330,360/=
Kenya Minning Industires Ltd..	51% ...	Kshs 7,650,000/=
Firestone E.A. Ltd	20% ...	Kshs 8,435,860/=
Brollo Kenya Ltd	40% ...	Kshs 6,666,660/=
PVP Ltd	37% ...	Kshs 6,345,000/=
Rivatex	36% ...	Kshs31,000,000/=
African Synthetic Fibres Ltd..	49% ...	Kshs14.700,000/=

36 These are IDB, DFCK, AFC, KCB and NBK

37. For example clause 1(2) of the Joint Venture agreement in Salt Manufacturers Ltd.,; Clause 9 of the promotion Agreement in Dawa Pharmaceutical. Also the Investment Agreement in Kenya Furfural Ltd.

38. See Kaplinsky, 1980 for statistical details in support of this contention.

39. 1979-83 Plan, 29 (emphasis added)

40. See for example, SP 10/65 pp.13 and 57; 1966-70 plan

41. P.93. The term Kenyanization has been substituted for Africanization in recent years.

42. N. Swainson, 1980 p.237.

43. Examples are KCFC's and KFC's Project Implementation and Management Agreements; Interfood's Technical Services and Management Agreement; PVP's and Kenya Furfural's Management Agreements.

44. These include Kenya Canners Ltd., Firestone EA Ltd.; AVA, Leyland Kenya Ltd.; GM Kenya Ltd.; and EAPC Ltd.

45. Examples are in EAPC, KCFC, KFC, etc.

46. 1979-83 Plan, 5.

47. See Langdon, 1976; Kaplinsky 1976, 1978 and 1979; Eglin, 1978; Swainson 1980; Hopcraft 1979; Deepak Lal, 1975; Leys, 1975

48. 1979-83 plan p.6

49. See E.S. Herman, 1981 at p.4

50. See Baran & Sweezy, 1966; E.S. Herman, 1981; J.K. Galbraith, 1967.

51. 1970-74 plan p.316

52. Quoted in Lewis D. Solomon, 1978 p.109

53. Studies in other countries have reached similar conclusions. Examples are A. Richter, 1980 and C. Vaitsos, 1974.

54. Examples inlcude KFC, KCFC, Interfood Kenya Ltd. Furfural, GM, Leyland, Dawa Pharmaceutical, and Salt Manufacturers K. Ltd.

55. Eight of the projects studied have one or other of such stipulations.

56. The KCFC joint venture agreement, for example, gives the foreign parties the power of selecting and appointing the technical project manager which is a vitally important post in the project. The agreement provides

> PEC (foreign technical collaborators) shall provide the names of one or more persons who in PEC's opinion are qualified to act as technical project manager ... and subject to the approval of Management (ostensibly foreigners) (which shall not be unreasonably withheld) one of these persons shall be employed by the company and shall report to the management. (emphasis added).

The board has thus no role to play in what should be its funciton.

57. See Appendix 3 for sample clauses of Eximcorp's powers under the KFC's PIMA

58. Information obtained from interview with an official in Treasury, January, 1980.

59. An example of such provision is to be found in KFC's PIMA whose clause 1.1. of Art.1 reads "The company hereby appoints the management to plan, construct, carry out, set up, establish and ensure the completion of the project on behalf of the company ... to the intent that the management shall with land, building, plant and equipment acquired ... in the name of the company, be responsible for providing, establishing and commissioning ... a complete polyester fibre plant ...."

60. See H. Martyn, 1964 p.97

61. See Vaitsos, 1974 and O'brien's Spanish case study respectively.

62. The relevant clause read: "The corporation ... hereby authorises the bottler, and the bottler undertakes upon the terms and conditions following, to prepare and bottle ..., and to distribute and sell the same under the trademark in and throughout, but only in and throughout, the following territory ... The township of Nyeri and an area bounded by a radius of 30 km. from the Nyeri G.P.O." The G.P.O. is located in the centre of the township.

63. 1979-83 plan p.28

64. One agreement, for example, obliges the Kenyan licensee to spend a minimum of 20% of sales revenue in advertising with 25% of this (i.e. 5% of sales revenue) going to the foreign licensor as a marketing service fee.

65. Kenya Canners was obliged to import labels from Del Monte International despite the fact that such labels were available on the local market at comparative quality. A pharmaceutical firm was obliged to import 'green' vials from its foreign licensor although vials of comparable quality were available locally at cheaper prices except they were not green! (See Hopcraft, 1980)

66. The firm referred to in note 62 above, for example, influenced the pricing level of the Kenyan products by setting the extent of trade discounts at 25%. Firestone E.A. Ltd. is another example in which the foreign party determines the price under the terms of the investment agreement. As a result it prices its local tyres at very large premiums above the imported equivalent a factor which led in 1978, for example, to its making a 100% return on its investment.

67. An official of the firm informed this author that this veto has been exercised in the past.

68. One such clause reads: "... licensee shall not manufacture or sell products under its own brand names which may be regarded by 'C' as competitive with the Licensed products. In the event question arises, the licensee shall abide by the decision of C and will withdraw from its lines any products which C deems competitive or label them to conform with C's instructions ..." Of the other 10 agreements, 6 have provisions that give <u>de facto</u> powers over such issues to the foreign parties.

69. All the fourteen agreements included tie-in provisions falling into four main categories. Twelve of the agreements also included export-restriction clauses while all the fourteen included provisions for quality control by the trademark suppliers that were very strict.

70. One marketing agreement states in the preamble that "The company (Kenyan) believes that a continuous marketing of its products in overseas markets on favourable terms can only be undertaken through a well established importer and processor of dehydrated vegetables." In the Kenya Canner's case, it was DFCK that insisted on bringing in a firm like Del Monte with international marketing experience.

71. See PVP Committee Report 1977, p.19

72. For example, in a letter from the General Manager DFCK to the executive director, ICDC dated 27.7.73, on the subject, the former observes that; "If BW is wrong in its appreciation of the raw material supply position (i.e. in its feasibility study) it does not stand to lose much. Its only investment is $154,000 in equity out of a total project cost of $3.46m. Against this BW appears to recover $25,000 for the feasibility study and planning, $10,000 p.a. fixed plus 10% of gross adjusted profits ... However, I share IDB's view that if BW are driven too hard they may lose interest and they appear to be the only large scale user of dehydrates to have shown interest." (emphasis added)

73. Under a 1965 technical agreement, Del Monte was given a right of option to purchase 60% equity. It exercised this right in 1968. As of today, it holds 97% equity.

74. See for example, Cl.9(d) of Interfoods Joint Venture Agreement.

75. See Art.VII of KCFC's and KFC's JOint Venture Agreements.

76. In addition to this, he was the Chairman of a parastatal and had numerous other public roles to play.

77. Interview with a parastatal Senior Project Officer, November 1980.

78. SP 10/65 p.13

79. See studies by Langdon, 1976; Kaplinsky, 1978 and 1979; Swainson, 1980; Hopcraft, 1979; Eglin, 1978 and Leys, 1975.

80. As this study is limited in its scope, the reader is referred to the following work on the debate raging on about the alliance of foreign capital and the indigenous bourgeoisie in Kenya. Swainson 1980;

Langdon 1976 and 1978; Kaplinsky 1975, 1978, 1979 and 1980; Bjorn Beckham 1980; Willy Mutunga 1977 and 1979; A Hazlewood 1979; A Njonjo 1978.

81. See Langdon 1976 and 1978 and P Hopcraft 1979.

82. The Economist 23/8/69 p.56.

83. Of the 25 projects studied, 11 of them insisted on government participation as a condition precedent.

84. P. Hopcraft 1979, Part II p.15

85. See Ibid for examples. In June 1981, the Minister for Finance in his budget prohibited the export of hides and skins. This was aimed at encouraging local leather industry in which Kenya can be competitive on the export market. Three weeks later, after intensive pressure by exporters of hides and skins the majority of who are either foreign owned or managed and controlled, the export ban was lifted by the President in an address to a public rally.

86. Letter from IDB to Director of Industries dated 28.3.78

87. Letter from Ps Commerce & Industry to Import Licensing Office dated 5.7.77.

88. The Italian company involved supplied the coarse salt from Italy although it was available at Mombasa.

89. Such cases were observed in, among others, the motor, tyre, paper, vegetable processing, can and textile industries. Also in the Molasses complex in Kisumu.

90. It is significant that the circular was issued not under the firm's letterheads but those of its African director (then, an MP) who sent out the circular. The same person held directorships in more than a dozen firms involving foreign capital and once made a speech to the Association of African manufacturers in which he said "... I am convinced that unless the African who form more than 95% of Kenyans population feels that he is part and parcel of our ... economy ... it could be difficult to create a stable economy ... He (the ordinary man in the street) must be made to feel that it is truly his industry ... You have a responsibility to assist in the Africanization.. if for nothing else, at least for the preservation of the institution and value of the free enterprise system". Quoted in Leys 1975 p.145 (emphasis added)

91. In the past these have included the President's blood and marriage relatives, his close friends, ex-government ministers, senior government officials, their relatives etc.

92. One PIMA for example provides in Art.III clause 3.5 that "The management shall have the right to appoint all such staff as required by the company ... including but not limited to the General Manager, Chief Accountant, Works Manager and Chief Engineer. All agreements studied gave the foreign parties great opportunity for determining or influencing the selection and appointment as well as the promotion opportunities of senior management staff.

93. A revealing case is that of a former classmate of the author who felt that his American/ICDC Joint Venture employers' project was exploiting Kenya, but was also paying him four times as much as he would be earning in the civil service. He added, "if I had opposed company policies, I probably would not even be here. Why should I wage a war the government has shunned for 16 years at the very probable price of losing my job?"

94. Leys, 1975 p.124 (emphasis added)

95. ILO Report, 1972

96. See Hopcraft 1979, for an example in the pharmaceutical industry.

CHAPTER FIVE

FINANCIAL AND FISCAL REGULATION

Financial and fiscal regulation of business operations has been one of the "range of sensitive controls"[1] the government has used in its attempt to influence the use of human, economic and natural resources by private capital. Such means of economic regulation are a common feature in many capitalist economies both developed and underdeveloped. It can be used by the government to influence the pattern and trend of the economy in response to particular or general economic environment. It is possible for the government to use financial and fiscal measures as a 'stick' or as a 'carrot' or a combination of the two. Used as a 'stick' the measures seek to either discourage certain economic trends pursued by private capital by penalising those who prompt such trends or encouraging certain activities by threatening pecuniary penalties to those who pursue other less desirable activities. Used as a 'carrot' such measures constitute incentive to follow a trend indicated by the government.[2] In a lot of cases, fiscal measures are primarily intended and geared to generate revenue for the exchequer.[3]

Since independence, the Kenya government has increasingly applied financial and fiscal measures primarily for the purpose of conserving foreign exchange and

generating revenue. It has also utilized such measures as incentives to attract capital and recently to try and achieve other objectives such as geographical distribution of industries. This latter approach is a recent phenomenon as we shall see in the following discussion. In this chapter, financial and fiscal regulation is discussed under three main headings. These are regulation by the Central Bank, regulation through taxation measures and that under the Industrial Training Act. This last measure is given special attention not because it has been extensively used or even particularly successful, but because it specifically deals with the vital aspect of manpower training and employment policy. The pre-occupation of the financial and fiscal measures with foreign exchange matters will, it is hoped, become clear from the discussion.

Except where the regulatory measures are specifically stated to apply exclusively to non-resident persons, they apply equally, if not more, to all investments. Our discussion is, however, restricted to the application of these measures to foreign investors.

A : CONTROL BY THE CENTRAL BANK OF KENYA (CBK)

The CBK was established by statute in March 1966 with the responsibility of managing the country's monetary affairs.[4] In particular, it is the sole agency of the government responsible for all dealings in foreign exchange. I shall discuss the regulatory measures by the CBK under two main headings. viz. exchange control and limitation of borrowing rights. These are the two measures that are frequently cited as being among the leading measures in the control of foreign investment.[5]

1 Exchange Control

Like many other underdeveloped countries, Kenya is heavily dependent on imports from the developed countries to maintain the momentum of her economy.[6] Her capacity and ability to earn foreign exchange is far outstripped by her demand for it. The country's five year development plans since independence, have all been based on the assumption that substantial portions of the targets therein would have to be financed from external sources.[7] The current plan, for example, classifies balance of payments as being "the most severe constraint" to the achievement of plan targets.[8] In view of such reliance on scarce foreign exchange, the government has established a comprehensive exchange control system that is viewed as probably the most important government regulatory measure affecting foreign capital in the country.[9]

Section 30 of the CBK Act empowers the CBK to administer any laws relating to exchange control in force in the country. Under the powers conferred to it by this section, the bank regulates all foreign exchange transactions in the country. The legal basis of the current system of exchange control is The Exchange Control Act of 1967.[10] It establishes a system of exchange control whose primary function is conservation of foreign exchange. It operates a regime of exchange restrictions which are determined in quantitative terms by the exchange control authorities. As operated in practice, the system merely regulates the distribution of available foreign exchange to successful applicants rather than regulating its demand. It also supervises foreign exchange receipts and payments in an attempt to ensure that declared earnings in foreign exchange are brought into the country and that foreign exchange payments are made for authorised purposes only. Under the Act, any dealing in foreign exchange whether involving receipts or payment of the same is subject to authorization of exchange control in accordance with its provisions.

In theory, therefore, the CBK has very extensive powers to regulate foreign exchange transactions in the country. However, this apparent power does not operate in a vacuum. It operates in an environment, in as far as foreign investment is concerned, that is far from conducive to an effective regulation of their foreign exchange

transactions. One of the major limitations to the efficacy of CBK's foreign exchange regulation over foreign investors is the Foreign Investment Protection Act (FIPA). This Act places foreign investors covered by its provisions in a specially privileged position as far as exchange control regulation is concerned. It disapplies all but the procedural regulatory measures under the CAE. Once a foreign investor has obtained a CAE under the provisions of FIPA, he is entitled as of right to repatriate the profits, principal and interest and even the capital in accordance with the provisions of the Act. This entitlement applies

> notwithstanding the provisions of any other law for the time being in force.[11]

Thus where foreigners invest funds in Kenya and such funds are covered by a CAE under FIPA, exchange control cannot legally impose any restriction to the remission of the earnings from such funds or the capital itself on its realization. The amount repatriable is not determined by exchange control, but by the terms of the CAE and all exchange control can do is to approve the relevant amounts under the exchange control machinery.[12] The amounts in question, or the formula for calculating the same, are usually predetermined in agreements between the foreign investors and their local partners or subsidiaries. This means that the CBK supervises the remission of funds in accordance with the terms of a CAE in whose formulation it has no say. The Investment Agreement in Firestone, for example, provides that

Table 7

CERTIFICATES OF APPROVED ENTERPRISE

HELD BY 59 PRODUCING SUBSIDIARIES

IN KENYA, 1972/73

Category Subsidiary	N (1)	Number with Certificate (2)	(2) as % of (1) (3)	Negotiated as Specific points to obtain Cert. (4)	(4) as % of (1)	Hold no Certificate	Unclear or N/A
Total	59	51	86%	22	37%	6	2
	A: Divided by Period of Entry						
Pre 1965	31	24	77%	4	13%	6	1
1965 - 1973	28	27	96%	18	64%	-	1
	B: Divided by Orientation of Production						
Export Oriented	10	9	90%	5	50%	1	1
Import Subst. Cons. goods	27	26	93%	10	37%	2	-
I-S intermediate & cap goods	22	17	77%	7	32%	3	2
	C: Divided by Size of Subsidiary						
Capital EMP. £1 million+	21	19	91%	8	38%	2	-
C.E. £300,000 to 1 million	13	9	69%	5	38%	3	1
	25	23	92%	9	36%	1	1

This Table includes all primarily producing subsidiaries interviewed, as noted in Table 8.

A: Subsidiaries are divided on the basis of when the first producing subsidiary began operations in Kenya.
B: See note C in Table 10.
C: See note A in Table 10.

Source: Langdon, 1976, P.123

> ... there shall be issued to Firestone (International) ... a Certificate of Approved Enterprise with regard to each investment of foreign assets, including the services performed as contemplated by the Plant Contract.[13]

The plant contract in Firestone stipulated the amounts to be specified in the CAE and those that were to be subsequently incorporated therein as and when they may be invested in the future. The CBK was not party to the negotiation of any of the four agreements involved in the Firestone tyre project. All the agreements studied in Kenya by the present author have provisions to the same effect and had applied and received CAE's covering their investment as specified in the agreements. In his 1972/73 survey of 59 foreign subsidiaries in Kenya, Steve Langdon found an overwhelming majority of the firms had applied and obtained CAEs. His tabulated results are shown in Table 7.

There are three major channels of remission of funds in foreign exchange by foreign investors that exchange control should be particularly concerned with. These are, remissions as returns to capital invested; fees charged for services rendered and payments made in trading transactions. Available empirical evidence suggests that the exchange control system in force in the country has had little impact on the ability of foreign investors to remit funds through these channels.

(i) Remission as return on capital invested

Remission of funds as return on capital takes two forms. One is dividends (or profits in case of wholly owned subsidiaries) which are returns on equity capital, and the other is in the form of interest which is a return on loan capital. The repatriation of profits by foreign investors is guaranteed under section 7(a) of FIPA where such investors hold a CAE. Exchange control has no legal power to stop or limit such repatriation as long as the investor conforms to the procedural requirements laid down by the CBK under the provisions of CAE. Under those requirements, all such an investor has to do is present a CAE along with an audited balance sheet and profit and loss account with his application for approval to remit profits to exchange control.[14] If these are in order, then exchange control has to approve the remission. Failure to approve it would be a breach of the statutory guarantee offered to holders of CAEs under FIPA. In most cases, where the government is a signatory to a joint venture, investment or any other agreements of a similar nature with a foreign investor, failure to approve the remission would be a breach of a contractual obligation.[15] In addition, where an Investment Guaranty Agreement with the investor's home government is in force, the refusal would be a breach of a treaty obligation.[16] Thus, in strict legal terms, exchange control has little substantive power to regulate remission of profits by foreign investors. However, bureaucratic delays in approving applications for repatriation do occur

in some cases. In addition, the CBK has sometimes deferred remissions abroad due to balance of payments problems. Such remissions are approved, but deferred pending availability of foreign exchange. This is, therefore, not an abrogation of the legal guarantees under FIPA.

In practice, failure to apply for a CAE to cover invested capital has not, in the past, automatically led to refusals to repatriate profits though in such cases the CBK has authority to refuse remission of foreign exchange. In one case, a firm that did not possess a CAE had no difficulty in remitting its profits including remissions of £300,774 in 1975, ten years after FIPA came into force.[18] The firm was allowed to remit its profits in spite of the fact that, according to CBK records, it had been taken over by another firm in January 1969. Yet between 1971 and 1973, it remitted profits amounting to K£6,250 p.a. under its old trading name. Although CBK queried how the firm could have earned profits after being taken over, these remissions were allowed through. In 1974, the firm was allowed to remit dividends of KShs8,749,943 back-dated to the year 1965. The approval was erroneously given by CBK which later sought to withdraw it without success. The successor to the firm sought refuge in its new investment agreement with the government which guaranteed free repatriation of dividends. The CBK appears to have lost the battle for, in January 1976, the funds were remitted. The CBK was not bound to approve any of the firm's dividend remission

from 1965 onwards. Indeed it had legal power to refuse such approval. There is no statutory right of repatriation available to non-holders of a CAE. The only legal obligation on the Kenyan firm would be to pay dividends in Kenyan currency. Indeed even in cases of the expropriation of a non-CAE holder, the state would only be bound to pay compensation in Kenyan currency.[19]

Remission of funds in the form of interest by foreign companies operating in Kenya and holding a CAE is guaranteed under FIPA in similar terms as in the case of profits.[20] In as far as Kenya does not impose any limit on the amount of interest remitted, exchange control is legally obliged to approve remission of interest earned by loan capital covered by a CAE. The only indirect method of limiting the amount of funds remitted as interest is the administrative control over the gearing ratio of firms. A Treasury Capital Issues Committee[21] which operates in close co-operation with the CBK tries to limit the ratio to reasonable levels. According to the government, a 66% gearing is a reasonable level.[22] In practice however, foreign firms operate on much higher gearing than this. Kenya Canners, a subsidiary of Del Monte International, for example, at one time operated on a gearing of 24%.[23] Where the loan capital is from a foreign source, then its interest payments are in foreign exchange and there is little exchange control can do to limit it.

Table 8

Service Fees and Post-Tax Profits for Nine Foreign Subsidiaries (K£)

	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	197
(a) after tax profits										(389)	(14,599	
Service fees										5,413	19,110	
(b) after tax profits	1,915	28,273	26,627	17,455	38,705	22,612	?	46,010	261	10,004	45,501	
Service fees	0	28,273	30,177	21,553	42,455	26,755	?	21,009	5,332	16,559	41,448	
(c) After tax profits							11,755	22,165	(3,130)	(35,525)	(8,693	
Service fees							1,472	8,788	8,953	7,933	7,380	
(d) after tax profits		(29,344)	11,397	12,118	37,995	45,077	50,149	12,407	66,193	(178,054)	(197,084	
Service fees		6,062	17,146	29,015	87,765	103,075	111,240	189,073	120,978	?	170,630	
(e) after tax profits (a)											(167,654	370.3
Service fees											286,350	202.8
(f) After tax profits									(4,269)	(319)	(45,707	
Service fees									18,019	19,522	20,106	
(g) After tax profits									12,216	8,048	?	?
Service fees									?	434,800	474,800	474.8
(h) after tax profits							135,174	173,696	150,034	78,047	180,821	
Service fees							55,339	46,873	70,246	114,423	14,849	
(i) after tax profits (a)						168,126	123,751	?	249,243	152,138	284,287	
Service fees						90,751	65,823	35,216	?	111,566	143,828	

( ) means after tax loss

(a) dividends due to parent company, and not to ICDC who are partners in a joint venture.

Source : Kaplinsky, 1979, Page 20.

(ii) Remissions in the form of service fees and royalties

Service fees and royalty payments are an important channel for remitting funds abroad in many countries. In Kenya, many foreign investors choose to remit their funds in the form of service and royalty fees whenever possible. This channel has several advantages over dividends. First the supplier of any service or technology has an upper hand in the determination of the fee to be charged or the formula for arriving at such a fee. This is usually so because technological, managerial and marketing industrial know-how involved is usually in the possession of the foreign investor.[24] Second, unlike in the case of dividends, where a joint venture with domestic capital is involved, non-equity payments accrue exclusively to the foreigners while profits are shared with the domestic partners. This gives the foreigners involved in joint venture with domestic capital incentive to remit funds in the form of fees. Thus for example, in the Colombia chemical industry, foreign subsidiaries reported royalties that generally amounted to less than 25% of the reported profits. Yet for joint ventures in the same industry the ratio averaged 32.3% for three firms and 142% for three others.[25] Table 8 shows a comparison of after tax profits and service fees of nine Kenyan firms involving foreign investment during the period 1966 to 1977. It is significant that the proportion of service fees is consistently higher than that of profits for seven of the nine companies.[26] A third advantage fees have over dividends is that they are usually not dependent on the firm

making profits. Most agreements providing for payments of fees have fixed minimum fees payable and the foreign party is therefore assured of remission of funds whether or not dividends are declared.[27] Thus for example, between 1975 and 1978, Rivatex remitted abroad management and technical services fees totalling DM3,180,684 while the company consistently made losses over the same period.[28] A fourth major advantage for foreign firms to remit funds in the form of fees rather than dividends is the fact that, in Kenya, fees are taxed at a lower rate than that applicable to dividends.[29] Also they are allowable expenses for purposes of calculating a firm's corporation tax. Where a foreign party has majority equity, as in Kenya Canners Ltd., this reduces the tax burden of such a firm. Furthermore, evidence from projects studied clearly shows that it has been extremely easy for the recipients of the fees to obtain exemption from the applicable tax or to get a re-imbursement from the local partner or licensee of any amount of tax paid. There are other advantages associated with remission of funds through fees rather than dividends but these are sufficient for our purposes.[30]

Clearly the potential advantages of using fees as a channel for remitting funds abroad and the fact that there is ample empirical evidence to show that foreign investors appear to be taking advantage of this,[31] should be reason enough for the CBK to enforce effective regulation over it. However, as in the case of dividends, CBK and the apparently

tight exchange control regulations have had little success in imposing effective regulation (except of procedural formalities) over the remission of service fees by foreign investors. Again the major stumbling block has been FIPA. Under the Act, remission of all income arising from the investment of foreign assets is guaranteed, notwithstanding the provisions of any other law. Foreign assets are defined in s.2(i) as including

> ... rights, benefits or property obtained from... the provision or the use of exploitation of foreign rights, benefits or property.

As the fees payable are covered by FIPA, CBK has found itself frustrated but unable to do much. The major problem is that the fees payable are determined without consultation with the CBK and the agreements are then submitted to it for approval as agreed between the parties. In such cases, should the CBK refuse approval, then it is for the foreign party to decide whether or not to lower the charges. If they decide not to, then the alternative would be to drop the investment altogether. The CBK's attempt to limit the fees payable have as far as we can gather, met with very limited success. Of sixteen cases examined in which the CBK attempted to have the fees payable reduced because they were or would have been too high, only in two did the foreign party agree to a fees reduction or a formula that would lead to a lower fee. Even in the two cases, the CBK had to accept a compromise. In one of them it asked for a fee of 3% of net profits which fee would be subject to withholding tax instead of

the proposed 5% of sale free of withholding tax. The compromise reached was 3% of profits net of withhholding tax with a provision for a minimum net fees. In the other cases, CBK wanted a reduction from 5% of sales net of withhholding tax to a lower percentage with the fees being subject to withholding tax. It got 3% of sales net of withholding tax. Yet in all the sixteen cases, CBK's approval was obtained.[32] Having its legal powers limited by the provisions of FIPA and not being able to substantially influence the determination of the fees payable, the CBK has had little success in regulating payments of fees to foreign parties.[33]

Fees payable to non-resident directors have presented few problems to the CBK. The appointment of a non-resident director is subject to prior approval by exchange control authorities.[34] Under this rule, foreign investors have been pressurised into appointing resident directors,[35] and the CBK has carefully scrutinised payments to non-resident directors. An application to remit director's fees to non-resident directors must conform to and be accompanied by the following:

- the exchange control reference authorising the appointment of a non-resident director; and
- a certified true copy of the director's minutes fixing and authorising the payment of the fees.[36]

The CBK is thus well placed to regulate the payments of such fees in foreign exchange, and so far they have presented few problems. Perhaps the main reason for this state of affairs is the fact that fees form only a tiny fraction of the foreign investor's foreign exchange requirement.

(iii) Trading transactions

Foreign investors in Kenya operate production facilities that are heavily reliant on imported equipment as well as intermediate inputs and raw materials.[37] Exchange control has the responsibility of regulating payments for such imports. In doing this, it cordinates its activities with the department of Trade and Supplies which issues import licenses.[38] As long as foreign exchange is available, then exchange control cannot legally refuse to allocate foreign exchange for licensed imports. In other words, the country's import policy is not determined by exchange control. Other than the purely procedural role of allocating available foreign exchange to competing applicants[39] and supervising the surrender of foreign exchange earned by exporters to authorised dealers, the CBK is responsible for ensuring that the country earns or pays a reasonable amount for its exports and imports respectively. In this section, I am concerned with the regulation of manipulations in trading transactions that result in hidden foreign exchange costs. Such manipulations are commonly referred to as transfer pricing. From the experience of other

underdeveloped countries,[40] regulation of transfer pricing is a difficult task and yet a necessary one to avoid excessive loss of foreign exchange. The two main component parts of transfer pricing involved in trading transactions are the over-pricing of imports and under-pricing of exports.

The legal and administrative machinery for the control of firms' transfer pricing activities in Kenya is largely undeveloped and of doubtful efficacy. Exchange control regulations require that all payments in foreign exchange be approved by the CBK and any payments that do not conform to this requirement are, therefore, illegal.[41] Legally, this provides the CBK with the authority to scrutinise all such payments to ensure that goods imported into the country are worth the money paid for them. In practice, however, the existing exchange approval process under the law merely ensures that only authorised payments are made. Authorised payments are not necessarily fair payments. Until 1972, authorised payments were based on the prices stated by importers of which a certain proportion may well have been accounted for by over-pricing. When an importer who held an import licence applied for a foreign exchange allocation, if his application was formally in order and foreign exchange was available, he got an allocation. This system did not and could not check on over-pricing. It merely compared the total sum of foreign exchange allocated with that claimed to have been used. If these matched, exchange control did no more.

The regulation of over-pricing of imports depends on the ability to determine or ascertain the market prices of imports on the international market. The procedure did not give the CBK the ability to do this. It is for this reason that the CBK entered into an agreement with General Superitendence Company of Switzerland (GSC) in 1972.[42] Under this agreement, GSC is supposed to make pre-shipment quantity, quality and price checks on imports intended for Kenya whose value is K£1,000 or more unless they are exempt from such checks.[43] Under this arrangement, the CBK air-mails an inspection order to the appropriate GSC office for each consignment of more than K£1,000. The GSC or their agents then examine the goods and if satisfied in all three aspects, it issues a "Clean Report of Finding" in relation to the consignment. If not satisfied, it issues a "Non-negotiable Report of Finding" and airmails this to the CBK. If the former has been issued, the CBK gives the necessary foreign exchange to pay for the consignment while it is supposed not to give approval if the latter report has been issued.[44]

While this arrangement may help control the practice of overpricing imports, its effectiveness depends entirely on the ability and willingness of GSC to conduct the checks. Available evidence suggests that it has not been effective. A UNIDO consultant's report to the government found that during the years 1972-77, the estimated foreign exchange saving attributable to GSC was in the region of £2,000,000

excluding the unquantifiable supposedly deterrent effect that GSC claimed was the most important factor in the arrangement. In return for its services GSC received, over the same period, £6,9546,713. The report goes on to document major instances of over-pricing detected in the course of its preparation and concludes that

> In sum, we are led to the conclusion that the real, measurable benefits of GSC's intervention is substantially lower than those claimed by GSC.[45]

The present author confronted a senior official of GSC with these and several other findings of a similar nature and asked him what he thought of it. His answer was that the report had grossly underestimated the value of the deterrent effects of the arrangement. He estimated that GSC had saved Kenya about 2½ times the fees it had received through checking on imports.[46] Using the UNIDO figures, this would amount to a saving of £17,366,782. Asked for substantiation in the form of data showing the pre-GSC check prices and those of post-GSC checks, the official stated they were strictly confidential. He however, stressed that the bulk of these savings resulted from the deterrent effect of the checks. Clearly GSC is not in a position to prove its claim which is rendered rather incredible by several factors all admitted by the GSC's official during the interview.

First, the GSC does not compare the prices of goods with available substitutes of comparable quality.[47]

Thus where a supplier of a branded product supplies it to Kenya, GSC compares the price charged with those of the same product elsewhere. In which case if the supplier adopts a global over-pricing policy, his prices stand. Even more interesting, GSC does not compare the prices of CKD units with those of completely built up units (CBU). Thus for example, in February 1980, a Japanese Suzuki 4-wheel drive CKD unit would have cost Kenya 651,000 yens while a CBU was priced at 578,200 yens.[48] Yet GSC would treat these as two independent categories, arguing that its price checks are not meant to alter company pricing. Second, GSC's past record on available data would leave GSC's claim based entirely on the apparent deterrent factor.[49] Third, the GSC operates under substantial pressure from potential and actual legal threats. In Switzerland, for instance, GSC faces a lot of pressure from the very draconian laws on industrial espionage.[50] The line between legitimate inspection and spying for a foreign firm or country on the affairs of Swiss firms is far from clear. Thus the potential of law suits by individual firms means that GSC cannot pursue its investigations without fear of possible serious financial questions. The company official admitted that they do

receive such threats and gave me a specific example of a case in Nigeria in the cement industry where threat of litigation was expressly made. Nevertheless, he went on to say that they have successfully resisted such pressure. At the same time, he admitted that

> Too much check is considered by the firms concerned as harassment unless there is a clear case of irregularity.

Fourth, a lot of those firms subjected to GSC checks are themselves clients of GSC for the same purposes. The company admits that some of these clients are financially more profitable clients than a small country like Kenya. Even though, while admitting that this is a material factor for consideration, its representative denied that it has ever influenced GSC's decisions. This is impossible to check because the GSC submits only its recommendations to CBK while it holds the data on which it basis such recommendations.[51] Finally, but perhaps most important in relation to foreign investors in Kenya, the company admits that it is very difficult to tell what a fair price is in intra-firm transactions.

In the case of under-pricing of imports, the CBK in conjunction with the customs department has done no more than ensure that the amounts stated in the invoices are brought into Kenya as foreign exchange. Curbing of under-pricing of exports would require a form of machinery for comparing prices of such exports in the foreign markets and political will, to make meaningful use of the findings

obtained from such comparisons. Neither of these exist in sufficient abundance in Kenya today. Indeed, in the celebrated case of Del Monte's transfer pricing practices revealed by a UNIDO consultant and long suspected by CBK, the government has kept mum about the recommendations for action to curb the practice.[52] Political will appears to have been in short supply. African Business saw the government's unwillingness to tackle Del Monte on its malpractices in the following terms

> Tough times on the horizon indicate that Kenya may continue to coddle multinationals ... The interpretation of these events to be that while Kenya Canners [Del Monte's subsidiary] may be making good profits, its value to the economy is such that the government has decided that discretion is the better part of valour. In the light of Kenya's current difficulties, this must be taken as an encouraging sign for MNCs.[53]

It would appear that loss of the ability to regulate the activities of foreign investors is part of the price Kenya has had to pay for its heavy reliance on them.

Like in the case of service payments, CBK's potential to regulate invoice manipulations is greatly whittled down by the terms of the sales agreements entered into between Kenyan parties and foreign firms. These have tended to give the responsibilities of importing and exporting goods to the foreign parties. This has tended to promote a great deal of the foreign firms' intra-company deals which makes it difficult to scrutinise such transactions.[54]

2 Local Borrowing

Until the early 1970s, virtually all commercial banking facilities were owned and controlled by foreign capital. Even by 1977, foreign capital controlled over 60% of all banking business in Kenya.[55] As the rest of the economy was also substantially controlled by foreign capital, there was a tendency for the foreign banks to direct their loans to foreign firms rather than to the African controlled activities. The 1975 IBRD report noted that

> Although adequate statistics were not available it appears that commercial banks direct funds from rural to urban areas, above all, to foreign owned firms in the formal sector. An indication of this is that, by December 1971 loans to Africans ... were only 13% of all loans.[56]

Foreign capital have shown a preference for local over foreign borrowing for two major reasons. One is that borrowing in Kenya is substantially cheap by international standards.[57] And two is that by committing as little as possible of their own capital, foreign firms minimise the risk of loss in case of expropriation, currency fluctuations etc. This tends to encourage very high gearing in capital structure with local savings comprising the major portion of the loan capital. Since foreign banks which dominate the banking sector have shown a preference for lending to foreign firms, unlimited local borrowing by foreign controlled firms would divert funds available for lending from the Africans to foreign capital. In addition, availability of local funds curtailed the volume of foreign assets (exchange) brought

into the country. This last factor was a serious setback to Kenya's policy of attracting foreign investors as a source of foreign exchange. When the 1971 foreign exchange crisis hit the country, it was this consequence of local borrowing that led to the imposition of a limit on overdraft facilities to foreign firms by Kenyan registered banks.

Section 32(4)(a) of ECA provides that except with the permission of the minister, no person resident in Kenya shall lend any money or securities to any body corporate resident in the scheduled territories (E. Africa) which is by any means controlled (whether directly or indirectly) by persons resident outside the scheduled territories. Under the powers of control granted by this section, the CBK issued ECN No. 19 of 1971.[58] This Notice limited overdrafts to 20% of the non-resident investment in the business of the borrower except where a company is a resident controlled one, but with mixed participation of both resident and non-resident shareholders, in which case a maximum overdraft of 40% of the total investment may be advanced. Beyond these limits commercial banks need permission of CBK. It was hoped that this limitation would make foreign firms bring the remainder of their borrowing requirements from abroad. Like the other measures aimed at conservation of foreign exchange, this one too has had only limited success. Its ineffectiveness has resulted from two main factors. These are its limited scope of application and a pattern of granting exemptions from the regulation that has now become the rule rather than the exception.

By restricting the 20% local borrowing limitation to overdrafts only, the bank has unnecessarily narrowed the scope for the application of the rule. In general, non-banking financial institutions do not offer overdrafts. Their lending is mainly of medium and long term range. Thus although the limitation has commonly been referred to as one on 'local borrowing',[59] it does not affect non-overdraft borrowing from non-commercial banking institutions. These institutions include parastatal organisations whose loan advances to firms involving foreign firms far exceeds those by commercial banks in certain cases. Although the CBK may restrict any kind of lending by withholding approval under s.32(4a) of ECA, it is doubful whether this power is exercisable over parastatal organizations whose lending policies are determined directly by the treasury in conjuction with its partners where the organizations are jointly owned as is the case of IDB or the DFCK. It is therefore, clear that the borrowing limitation in force, even if it were to be enforced to the letter, would only affect a very small proportion of the total lending that overdrafts by commercial banks form. However, implementation of this narrow limitation is far from being adequate.

All of the 25 projects studied, had been given, at one time or continuously, exemption from this limitation. Some had over 75% of their foreign assets in local overdrafts. As the power of granting exemption ultimately lies with the Treasury, it appears that it has exercised its

discretion in some cases without consulting the CBK. In one case, Treasury had entered into an agreement with a foreign firm in 1968, in which the firm was given an option to purchase 60% of the Kenyan company's equity and still be able to borrow up to 50% of its capital investment locally. This was apparently done without consultation with CBK. The CBK complained of not being consulted by Treasury on the agreement. This was in spite of s.31 of the CBK Act 1966 which provides that

> The Bank shall administer any payments agreement entered into by Kenya, and the bank shall be consulted by the Government in negotiating any payments agreement.

On interviewing several Treasury and CBK officials, it was clear that they were not aware of this statutory requirement let alone being in the habit of conforming to it. In this particular case, it appears that the authorities were not even sure that the concession was of any use to the country. Determining this was not an easy job as a Senior official of a government institution pointed out in a memo to his boss. He wrote.

> The attached memo ... sets out the consequences of local borrowing concession given when the government entered into an agreement with ... for the latter to purchase majority equity in the above company and to provide management and act as the company's sales agent. An effort will now be made based on the financial statements we can get from the company to see if we can show whether the deal has been of any benefit to this country. An initial difficulty in this exercise will be our inability so far to find another company with comparable export business.

In another interesting case, Treasury informed CBK that a certain company (in which a foreign firm held a controlling though not a majority share but exercised near total control) wanted an overdraft of £1.25 million. CBK immediately objected suggesting that the company obtain a loan from IDB - which would still have been local borrowing but not covered by the relevant limitation. Following intensive pressure from some senior personality in the company, a CBK official advised the bank that although it could reject the application, it would be advisable to pass it despite the objections.

> For the sake of an understanding with treasury that they would not in future involve themselves with an investment project dependent upon local borrowing without appropriate reference to CBK.

The application was granted, but on condition that the company would not declare any dividend until it has reduced its overdraft to below the 20% limit.[60]

No statistics are available that would enable one to calculate how much effect this measure has had in inducing foreign capital to bring more foreign exchange into the country. Nevertheless, judging from the ease with which foreign firms have been able to obtain exemptions from the 20% limit, it is doubtful that it has had any significant effect. Its narrowness in scope leaves out a huge amount of funds available to foreign capital without limitations based on their foreign assets held in Kenya.

Kaplinsky's NCCK study renders support to the conclusion that, for the reasons given above, the limitations of local borrowing by firms involving foreign capital has not been an effective regulatory measure. He observes that

> The major conclusion of interest which emerge from this data [in the study] is the inability of the Central Bank to enforce its admirable policy of tying local credit to increasing local ownership.[61]

Langdon on the other hand, feels that the limitation on local borrowing has provided the CIC, which considers applications for local borrowing in excess of the limit, with a fairly strong leverage against firms wishing to obtain access to additional local credit. He also feels that it is possible that the fact that some firms are able to obtain local credit beyond the limit may indeed be because the CIC has won other concessions from such firms.[62] I readily concede to the possibility of this being the case, but as I have no empirical evidence in support of this contention, it must for the time being remain a matter of conjecture.

The 1979-83 plan introduced a new element in the limitation of local overdraft facilities. It stated that

> ... maximum credit will be based on the monthly or annual wage bill for Kenyan employees. Hence, short-term credit will reflect more closely the finance required for local costs.[63]

This appears to be aimed at pressurising firms involving foreign capital to adopt more labour intensive production methods and to encourage them to Africanise their remaining personnel. The author has found no evidence that this measure has been implemented.

B : REGULATION THROUGH FISCAL MEASURES

In his 1973 budget, the minister of finance declared that

> We must use the tax system to encourage the efficient use of economic resources. For example, our tariffs and taxes should not encourage the excessive use of imported raw materials and capital goods; the system should not discriminate against production for exports; and it should not discourage the use of labour.[64]

This budget marked the beginning of a shift in fiscal policy that was hitherto primarily geared towards the implementation of a strategy for industrial development "based on import substitution and on the need to attract foreign capital and technology"[65] It was therefore, not concerned with positive direction of the pattern of economic development but rather with an increase in the volume of investments. In this budget, the minister set out to change most of that. He found it an uphill and largely an unsuccessful task with his efforts virtually turning into personal efforts with the weight and authority of the rest of the government machinery being brought to bear against him. Thus, few of the fiscal measures contained in the subsequent budgets right through to 1981/82 fiscal year have been implemented.

Those that have been, have nevertheless, been less than enthusiastically implemented.[66] A discussion of Kenya's fiscal policies as it affects foreign capital would fill up a volume on its own which is why the discussion here is restricted to a very brief examination of key fiscal measures that have been adopted. For all the details, the reader is referred to the relevant statutes and government publications cited herein. The fiscal measures are discussed under two headings; income tax and custom tax together with sales tax.

1 Measures Under Income Tax Provisions

Income tax legislation[67] in Kenya provides for two main regulatory measures that affect foreign capital in the country. These are the provisions on investment allowance and those on withholding tax on payments to non-residents. This is not to say that other provisions such as that on corporate tax, do not affect foreign capital. They do in as far as they apply to it, but they are primarily intended for revenue generation rather than a regulatory role.

(i) Investment allowance

Every investor investing funds in the construction of buildings and installation of new machinery is entitled to an allowance known as investment deduction of 20% of his capital cost in the first year of operation.[68] Until 1979, the investment deduction was offered without conditions

as an incentive to attract capital investment. Indeed it was the most often quoted fiscal incentive aimed at attracting foreign capital. The government even boasted that

> Taken together with the usual depreciation allowances, an industrialist can write off 120% of his investment against taxable income over a period of years.[69]

This is in fact, an underestimation in most foreign capital projects. The practice of over-pricing machinery and equipment means that the 20% of the stated cost investment is considerably higher than 20% of the actual market value. As long as the investment deductions were offered for the sole purpose of attracting capital investment, they could not be said to play any regulatory role. Indeed, their offer without conditions had some negative consequences upon some of the declared economic objectives. One of these, is the creation of employment. The system of investment allowance led to the substitution of capital for labour. As early as 1966, the government had realized that this was happening. The revised five year plan stated

> The substitution of capital for labour in recent years seems to have stemmed from three principal causes ... The third factor ... is the system of investment allowances that has been established for tax purposes. While these allowances attract capital to Kenya, they also stimulate substitution of capital for labour by reducing the cost of capital relative to labour.[70]

The 1974-78 and 1979-83 plans make the same observation[71] indicating that although the government was well aware of the problem for the past 12 years it had, nevertheless, felt

that attraction of capital into Kenya ought to take priority over the employment factor.

After 1978, the government finally introduced differential rates of investment allowances aimed at influencing investors to adopt more labour intensive methods as well as locate their investments outside the established major urban areas.

> To promote dispersion of industries, more effective use will be made of investment allowances. To simultaneously promote emplo-ment through the use of labour intensive techniques, account will be taken of the amount of fixed capital involved in every new job opportunity created. The rules pertaining to this concession will be modified by providing differential investment allowances to new enterprises that take into consideration whether they are established in semi-urban or rural areas, and also whether they are labour intensive or capital intensive.[72]

Under this system, enterprises whose fixed investment per every new job created is less than KShs.100,000/= are entitled to the following allowances:

- 10% in urban areas other than Nairobi and Mombasa;
- 15% in semi-urban areas; and
- 20% in rural towns.

For enterprises with a high capital/labour ratio which entail investment exceeding KShs.100,000/= per new job created the applicable allowances are 5%, 10% and 15% respectively for the above stated locations.

These differential allowances constitute the first attempt by the government to utilise the investment allowances to achieve goals other than attraction of capital to Kenya. Whether this new fiscal policy will have a marked effect on the geographical dispersion (away from major cities) of industries as well as on the capital/labour ratio of new investments remains to be seen. Its effect may depend very much upon other fiscal and non-fiscal measures such as tariff and quantitative restrictions in protection of local industries which are much more important to investors than the allowances. If these are retained anywhere near the present levels, then their benefits would more than compensate for the loss of the allowances. As for the creation of new jobs, the differential allowances on their own may not be sufficient to affect the choice of factor intensity. In a joint venture where the foreign investor is a minority shareholder, for example, his major interest may be in the supply of machinery and equipment to the project in which case he has more to gain than to lose in not switching over to labour intensive technique.

(ii) Withholding tax

In 1971, the government introduced a withholding tax for all payments to non-residents in the form of dividends, interests, service and royalty fees, rents and pensions.[74] Except for pensions, all the other categories are normally important means for remitting funds abroad by foreign capital. The withholding tax was introduced primarily to limit

the amount of foreign exchange paid out. As Kenya does not have any statutory or effective administrative limit to the amount that may be repatriated in these forms,[75] the Treasury felt that this tax would reduce the foreign exchange payable. It was also aimed at revenue generation. In 1981/82, for example, the revision of withholding tax rates was expected to bring an additional £3 million in revenue.[76] On the basis of this figure, we estimated that total revenue (and therefore an apparent foreign exchange saving) brought in by this tax in 1980/81 to have been approximately K£37 million, assuming that it had a maximum impact.[77]

Although the withholding tax has good potential for conserving foreign exchange by reducing the payments made to non-residents, it has not been properly utilised. In order to have maximum effect, it is necessary that a fixed formula be used to determine these payments and with the exception of dividends, there ought to be fixed rates (or maximum limits) applicable to fees such as management and royalty fees.[78] What is happening today is that foreign investors usually charge their fees net of withholding tax or incorporate a re-imbursement clause in their agreements with their Kenyan projects obliging the Kenyan operation to re-imburse them any withholding tax paid if the fees are not exempt from withhholding tax.[79] This means that both the incidence and impact of the tax falls on the Kenyan operation. The foreign investors simply slap a mark up over

their market charges equivalent to the applicable rate of withholding tax. Given this practice, it is doubtful whether the revenue generated from the withholding tax is in any real sense a savings in foreign exchange. The practice of demanding and obtaining exemption from withholding tax as well as re-imbursement (in case of non-exemption) by foreign investors has greatly reduced the impact of the withholding tax as a regulatory measure for the conservation of foreign exchange. In addition, they have been able to charge such fees as would take into account the existence of tax wherever necessary. In two cases, for example, the foreign investors charged fees at rates dependent on whether or not the fees were exempt from withholding tax.[80]

2 Regulation Under Tariff and Sales Tax Measures

Like investment allowance, tariffs have always been used by the independent government with attraction of foreign capital in mind.[81] Their other major objective has been the raising of revenue. Since independence, they have been the major revenue raising form of taxation. As incentives for attracting foreign capital, they are used to protect domestic economic operations from competition from imports by raising the landed prices of the latter above those of domestically produced products. This has been in line with the government's industrial policy of import substitution, the achievement of which has been the basic aim of trade policy for the first fifteen years of independence.[82]

In the 1970-74 plan, there was no mention of exports among the enumerated targets of manufacturing. Even in the third plan, 1974-78, import-substitution was high up on the priority list of government's economic policy. Tariff protection was seen even then, largely as a measure of protection aimed at encouraging import substitution industries.

> The high rate of growth in manufacturing since independence has been based primarily on import substitution which has been encouraged through tariff protection of consumer goods.[83]

Used in this manner tariffs played little role in regulating foreign investment in the country. They no doubt did influence foreign firms to set up behind the ever rising tariff barriers against their traditional exports to Kenya. Table 9 shows a sample of increases in tariff rates that have coincided with the establishment of local production by foreign capital.

The use of tariff as a means of protecting domestic industry has led to consequences that were not intended.[84] In 1973, the minister of finance warned that

> ... Perhaps the major fault of the existing system is that it has tended to create highly protected inward-looking manufacturing industry in Kenya. Industry has been able to set up behind high tariff walls simply to manufacture products for sale in the restricted East African Common Customs area ... at other times the cost involved in setting up these new projects has been greater than we should reasonably be expected to pay - high cost products, mediocre quality, exclusion of consumer choice, high import content, high repatriation of profits and very little employment content . Is this the economic development we want? I say No![85]

Table 9 Foreign Investment and the Provision of Tariff Protection in Kenya

Product	*Company*	*Year Established or Began Production*	*Duty Imposed*	*Previous Year*	*Duty Imposed*
Bicycle inner tubes	Bata Shoes	1958	90 cts per lb.	1958	55 cts per lb.
	Avon Rubber (Kenya) Ltd.	1958	,,	,,	,,
Industrial ink	Coates Bros. (E.A.)	1960	22%	1958	11%
Paints	Sadolins	1959	25%	1961	11%
	Leyland Paint Company	1958	33⅓%	1963	25%
	Robbialac Paints	1960	,,	,,	,,
	Walpamur	1960	,,	,,	,,
Light diesel oil	Caltex Oil (Kenya) Ltd.	1960	22%	1960	Free
Vehicle tyres	Michelin (Tanzania)	1962	Shs 1/25 per lb.	1962	40 cts per lb.
	General Tyre (Tanzania)	1969	Shs 1/50 per lb.	1968	,,
	Firestone E.A.	1969	,,	,,	,,
Multiwall paper sacks	E.A. Packaging Industries	1963	17½%	1962	12½%
Bicycle tyres	Dunlop (Uganda)	1964	Shs 1/25 per lb.	1963	Free
	Avon Rubber Co.	1964	,,	,,	,,
Glue	John Heffer (Mining) Ltd.	1966	30%	1967	Free
Light bulbs	Philips Electrical Lamps	1965	30%	1966	Free
Radio and T.V. assembly	Sanyo (through ARMCO)	1966	Radio 50% T.V. 50%	1966 1966	37½% Free
Car batteries	Joseph Lucas	1966	30%	1967	Free
Electric cables	East African Cables	1966	15%	1967	Free
Toothpaste	Colgate Palmolive	1966	30%	1967	Free
Brooms and brushes	L.G. Harris	1967	30%	1967	Free
Radio batteries	Union Carbide	1967	30%	1967	22%
Stainless steel tanks	Hall Thermotank Overseas	1967	15%	1967	Free
Chocolate confectionery	Cadbury Schweppes	1970	50%	1968	Free
Fishnets	Kenya Fishnet Industries	1970	20%	1970	12½%

Source: Eglin 1978, P.107

Coming from the person in charge of the economy's finances, this is indeed a rare but revealing admission of the failure of the use of fiscal policy as an instrument for regulating investment, the bulk of which was foreign owned and/or controlled. Other consequences cited as resulting from the use of tariffs for protection purposes include, discouragement of the development of domestic capital and intermediate goods industries, discouragement of the use of local raw materials and encouragement of transfer pricing practices, in particular, over-invoicing of imports.[86] However, the trend of tariff impositions have been upwards since 1972 when the minister began, what became thereafter an annual phenomenon, his castigation of the government's fiscal policy. Indeed, in 1973, for example, he raised the tariff applicable to several products produced domestically by foreign capital. Since then, little has been done to use tariff as a regulatory instrument vis-a-vis foreign investment.

In 1979, the government introduced a 10% duty on imported raw materials and machinery and equipment.[87] The duty on machinery and equipment was raised to 20% in 1981.[88] In addition duty on a few items was reduced to promote exports and to reduce excessive protection.[89] The imposition of duty on raw materials was aimed at regulating the use of imported inputs, and discouraging over-pricing of imports in particular, machinery and equipment. This is the only use of tariff imposition aimed at regulating specific characteristics of investments since independence. In

all its other uses, the tariff has been directed either at the consumer, as in case of luxury goods, or at competitors of domestic producers while the duty-free entry of all raw material and industrial inputs was aimed at benefiting the domestic producers who, in Kenya's import substitution industry, are predominantly foreign. It is very doubtful whether this will have any significant impact on the present pattern of investment for several reasons. First the applicable rate of duty is hopelessly low in view of the fact that the level of protection offered to investors through various protection measures is extremely high in Kenya. The minister of finance in fact points out that, "the effective rate of protection is in some cases as high as 300%"[90] To significantly affect the pattern of behaviour in such industries through tariff measures would require not only imposition of high duties for the inputs but also a drastic reduction in the duties applicable to competing imports. Second, the imposition of duty on capital goods was more than compensated for by the abolition of sales tax on such imports (see below) and the imposition of even higher duties on competing imported goods.[91] Third, but related to the other two is that a 20% duty on machinery and equipment would be hopelessly inadequate to reduce the incentive to over-invoice such sales. It was the view of the government that

> Given the present rate of duty on plant and equipment of 10%, the incentive to over-invoice is great. With the new rate of 20%, this incentive is considerably reduced, and where it occurs, it will now be taxed.[92]

This appears to be a clear case of over-optimism or glossing over an imported economic issue in Kenya today.[93] This is particularly so in cases where foreign investors are in joint venture with local capital.[94]

In 1978, the government introduced sales tax on important capital equipment again to discourage investors adopting capital intensive production techniques. These ranged from between 10 and 30%. However, following intensive lobbying by domestic industries, this tax was abolished in 1981. Indeed, its abolition was aimed at providing importers of such items with a net reduction in their costs (resulting from fiscal policies) of importing them despite the 10% increase in duty payable for such imports. Thus the minister of finance explained that

> Taken together with the changes in rates of customs duty [higher rates for competing imports] ... this change [abolition of sales tax on plant and equipment] will mean that even after the increase in duty on plant and equipment from 10 to 20%, industrialists will benefit by a net reduction in effective taxation of between 8% and 21%.[95]

Fiscal measures intended to influence investors in specific directions appear to have been formulated and implemented in such a way that they end up benefitting the investors of capital even more while not achieving their objectives.

Foreign investors dominate the sectors affected by these fiscal changes.

C : THE INDUSTRIAL TRAINING LEVY

One of the key factors usually cited by proponents of unlimited encouragement of foreign investment is the belief that they bring with them necessary but scarce skills as well as creating employment.[96] Skilled manpower has often been seen as a major constraint to economic development and the government has often expressed, in its economic rhetoric, its determination to remove this constraint.[97] A major problem in training manpower is its expense. To ease this problem, as well as to force the foreign dominated industries to shoulder a proportion of the costs for training industrial manpower, the government amended the 1959 Industrial Training Ordinance to provide for the imposition of an industrial training levy.[98] S.5B of the Act empowers the minister for labour to make a training levy order directed to any employer imposing a training levy on such employer. All monies received in respect of a training levy order are paid into a Training Levy Fund and is disbursed to industries that have training programmes in order to defray part of their training expenses.[99] As a fiscal measure aimed at compelling investors to participate in the active training of local manpower, the Act has not been effective because of three main reasons.

First, the Act has been applied to only a narrow spectrum of the existing economic activities. Initially it only applied to ten subsectors of the economy.[100] There is no reason why the levy should not have been imposed on all industries. However, the government has enlarged the number of sectors covered by the levy and has proposed further coverage.[101] The second main reason for its non-effectiveness is the lack of adequate enforcement even to the narrow scope of industries it applies. The government admits that "collection of the levy have been disappointingly small due to the large number of defaulters." It plans to strengthen the collection mechanisms.[102] The third, and most negative aspects of the Act was the basis on which the levy was calculated. The Act is silent on what the levy should be based on. It would appear that, in some industries, the minister chose to base the levy on the wage bills of the firms to which it applied. This meant that the more labour intensive investments bore the brunt of the levy while those that were capital intensive had a lighter load on their shoulders. By raising the cost of labour in those industries which employ and train more labour, the levy has, in effect, been a tax on jobs. To rectify this shortcoming, the 1979-83 Plan proposed a revision of the Act in accordance with the new stated policy. The new policy was supposed to:-

> ... ensure that the burden of this levy should fall most heavily on those firms that have designed their methods of production to use the least labour. Thus, capital intensive industries will pay a greater share of the cost of training people for other industries where they can be employed.[103]

To achieve this objective, the levy was to be revised so that it would be charged as a tax on depreciation thus basing it on the annual cost of capital rather than on the annual cost of labour.[104] However, as of December 1981, this policy change had not been implemented.

D : CONCLUSION

In this chapter the main features of financial and fiscal policy and regulation have been examined. It has been shown that for the first ten years of independence, the government had pursued a policy that left foreign investors hardly affected in a serious way. Indeed, rather than the financial and fiscal policy being used to regulate the investment patterns and operations of foreign investors, they were primarily used to attract such investors. Their attraction lay in the fact that they left the investors relatively free to tailor their own investment policies. But by the beginning of the 1970s, the consequences of the policy being pursued had been recognised as having actual and potential negative effects on the economy. Even with this realization, the government appears not to be over-enthusiastic to adopt, in practice, changes it so eloquently and frequently promised to bring about in its financial and fiscal policies.[105]

When the government finally adopted some fiscal measures aimed at some form of regulation, its efforts were rather half hearted despite pressure from IBRD to reform its policies in particular those on tariff protection.[106] The inability and unwillingness by the government in imposing effective regulatory financial and fiscal measures is a direct result of the government's broad economic policy. Its basic policy of a private capital based economy has led directly to its heavy reliance on foreign capital. This has in turn meant that it has to sustain its attraction to such capital, a task it feels it cannot execute successfully if it adopts tough and effective regulatory measures. The adoption of an import substitution industrial policy has further weakened the government's regulatory position. Such industries are usually established only on condition they receive high protection and other concessions. Once they are established, to change this basis of their establishment becomes extremely difficult. A major restructuring of financial and fiscal policies in order to make them effective tools of regulation would require, as a condition precedent, the reversal of the policy of attracting foreign investment as well as that of high protection of domestic import substitution industries. This would, in the vast majority of industries, mean a virtual collapse. And this is what the government fears.

As things are today in Kenya, it would be extremely difficult to maintain the economic policy and at the same time

effect financial and fiscal policies that are mainly of a regulatory nature. The two appear to be largely mutually exclusive. High duty on industrial inputs and low or no duty on competing imports, for example, is incompatible with an import substitution industry, such as exists in Kenya. It would appear that a restructuring of the government's economic thinking and policies is a condition precedent to the imposition of effective regulatory financial and fiscal measures.

Although the discussion in this section has concentrated on tariff measures non-tariff measures feature more commonly in government trade policy. Examples of these non-tariff measures are dealt with in chapters three and five.

NOTES

1. SP 10/65, 6
2. For example, export allowance
3. A good example is the airport tax.
4. Established by The Central Bank of Kenya Act 1966.
5. See for example, Lloyds, Barclays, Standard, etc banks' annual reviews on Kenya; Langdon, 1976, Swainson, 1980.
6. Economic Survey, 1972, 58
7. Whenever there is a drastic short-fall in the foreign exchange reserves, some existing development projects are suspended. This happened during the 1974-78 plan period for example. A major revision of the 1979-83 plan which involves the suspension of certain projects was envisaged in Sessional Paper No.4 of 1980.
8. 1979-83 Plan, (iii).
9. See Ibid. Most officials of projects involving foreign capital expressed a similar view.
10. Cap. 113.
11. S.7 of FIPA
12. Ibid. s.6. Such an approval process is merely a procedural formality and its only role is to ensure that the funds applied for are covered under a valid CAE.
13. Art. IV S.6.12. See also the General Motors, Rivatex, Leyland Kenya, K.F.C., K.C.F.C. Investment Agreements for examples.
14. ECN No.31
15. All the agreements studied include provisions to this effect.
16. See for example the USA/Kenya agreement.
17. Interviews with CBK and several companies' officials, held in Kenya during 1980/81

18. The author was informed of at least four other similar cases in the course of field research in Kenya. Each of the firms involved had powerful political personalities backing them.

19. This, it is submitted, is the combined effect of ss.2(4) and 21 of the EC Acts respectively.

20. s.7(c).

21. The CIC was set up in 1971 to consider applications by firms wishing to go public. See Langdon, 1976.

22. Guidelines For Application to the NPC, 1979

23. All firms studied had a gearing ratio of over 33% with eight of them averaging 7.5% See also Kaplinsky, 1980, 102 for details on debt-equity ratios of large scale manufacturing and all tourist firms in 1966-76.

24. See Vaitsos, 1974, 87

25. Ibid.

26. For companies, E, F and G, for example, the fees are 200, 200 and 5,500% of dividends respectively for the five years in which the two sets of figures are available. Eight of these firms were included in the present study. Of the remaining seventeen, eight remitted fees that were, on average, higher than their dividend remissions for the years 1976-79 while six remitted only fees, either because they had made losses or had declared no dividends. No information was available on the remaining three.

27. Twenty-two of the 25 agreements studied had either a fixed minimum fee or an ascertainable formula for fixing such a fee.

28. See willy Mutunga, 1979.

29. See the discussion on income tax measures that follows later in this chapter.

30. See Vaitsos, 1974; Kaplinsky 1978.

31. See Kaplinsky, 1980, 88 Table V

32. An official of the CBK told the author that approval is usually a formality although in some cases the CBK tries to have the fees payable reduced.

33. Kenya's record of permitting repatriation of fees is described as being extremely liberal in comparison with other systems. See ILO, 1972; Deepak Lal 1975 and IBRD 1975.

34. ECN No.31 para. 7

35. In the projects studied, over 70% of the directors or their alternates representing foreign capital were residents. However, several of these were foreign firms registered in Kenya while most of the individuals were non-citizens.

36. ECN No. 31 para.7

37. See 1979-83 plan which states that the manufacturing "sector as a whole still relies to a very great extent on imported intermediate inputs. An analysis of Kenyan imports indicates that about 50% of our import bill is accounted for by capital and intermediate goods imports". p.326-7

38. For details of its operation, see D. Macrae, IDS W. P. No. 90, (undated); Hopcraft 1979; IBRD, 1975.

39. These are contained in ECN No.10

40. For example, Colombia, Greece, India etc.

41. Ss.7 and 8 of CAE.

42. GSC (Societe Generale de Surveillance S. A. - SGS - in French) describes itself as "the world's largest control and inspection company", offering a complete range of quantity and quality checks and related technical services. It is represented in more than 140 countries by 110 affiliated companies. Its headquarters are in Geneva. It has 8,000 specialists working individually or in teams who carry out "any control function from basic quantity checks to testing of complex industrial equipment" in its 57 odd laboratories. It has seven operational divisions: Industrial and Consumer Products; Agricultural; Petroleum and Petrochemical; Mineral, Chemical and Metallurgical; Non Destructive Testing; Industrial; and Laboratory divisions.

43. For items exempted from inspection see UNIDO Consultant Report, 1978, 21

44. However, in some cases it has been given to such imports. (Interview with government official)

45. UNIDO Consultant Report, 1978.

46. Interview with Senior GSC official held at company's headquarters, Geneva on 4/12/81.

47. Ibid.

48. Information from a Sales Manager of a motor trading firm. The CKD kit does not include local components such as tyres, exhaust pipes etc.

49. UNIDO report, 1978. This is supported by Hopcraft, 1979 and also interview with public officials.

50. See Jean Ziegler, Switzerland Exposed, 1976.

51. Interview with GSC official, December 1981.

52. See Kaplinsky, 1979.

53. African Business, November 1979.

54. In one case for example, IDB wished to make a disbursement of a loan to Metal Box Kenya Ltd. It therefore asked MB to make a formal request "which in case of plant and machinery should be supported by copies of the following documents: Suppliers invoice; Bills of lading; Clean report of finding by GSC; Certificate of origin; Machinery Supply Contracts if available; and Evidence of payment." (letter from IDB to MB, 23/1/76). MB replied enclosing what purported to be a list of machinery purchased, against which it wished to make a full withdrawal of KShs.3,000,000/=. It added that "settlement of these invoices is done by means of periodic roundsum payments against the inter-company account with our parent company MB overseas Ltd. and no evidence of payment relating specifically to those invoices is available". (letter from MB to IDB, 5/2/76 - emphasis added).

55. Barclays and Standard Bank, together controlled nearly 50% of banking business in 1976 - Langdon, 1976.

56. IBRD, 1975, 275.

57. The 1974, IBRD mission, for example, questioned whether it is desirable to permit foreign firms to borrow money more cheaply in Nairobi than in London or New York - See IBRD, 1975, 292. See also Budget speech 1980, where the minister states that one of the disadvantages of low interest rates is that "... capital intensive projects are encouraged in preference to the use of labour while foreign investors also prefer to borrow cheap local finance instead of bringing in their own capital." (p.10). A specific example is the E.A. Sugar Industries Ltd. Where a government's loan of 19,000,000/= at 6% provides a 4% subsidy in comparison with loans from other

sources which were at 10%. A government accountant reported that the management (who were also the foreign minority shareholders) "appears to resort to borrowing whenever an issue arises." He recommended that "one may wish to know what the contribution that other shareholders are making to compensate for this (the subsidy). If none is apparent, other than drawing of management fees (sic!), then there is a case for reviewing the rate of interest for this and other projects which are not wholly government owned." (Treasury Internal Report on E.A. Sugar Industries Ltd's accounts up to 31/12/77 dated 17/8/78).

58. Borrowing By Foreign Controlled Companies And By Non-Residents. ECN. No.19 of 1971

59. See for example, ILO, 1972; Deepak Lal 1975: IBRD 1975 1979-83 Plan; Leys, 1975; Swainson, 1980 and Hopcraft 1979.

60. In addition, the company's loans from the government included the following

1976	.....	K£185,908
1977	.....	?
1978	.....	K£750,000
1979	.....	K£750,000

61. Kaplinsky, "The Distribution of Ownership In Industry and Tourism", 20. (in NCCK, 1980)

62. In his comments on the draft to this work, may 1982.

63. 1979-83 Plan, 70

64. Budget Speech 14/6/73, 7

65. See Budget Speech 19/6/80

66. In every budget since 1972, the minister made the same criticisms of government industrial policies and its effect on the economy (see Budget speeches 1972 to 1981). However, most of the solutions he enumerated in the budgets, appear not to have been implemented and others have been reversed within a short period re-instituting the status quo

67. Income Tax Act, 1976 which is a consolidation of past East African Community legislation on the subject.

68. Ibid. Second Schedule, Part IV.

69. 1964-70 Plan, 30. Also in the revised 1966-70 Plan, 239.

70. 1966-70 Plan, 72

71. 1974-78 Plan, 90. and 1979-83 Plan, 8.

72. 1979-83 Plan, 340.

73. Ibid. A rural town is defined as one having a population of less than 10,000; a semi-urban more than 10,000 but less than 30,00; and an urban one with 30,000 and above.

74. At present, the rates are; management, royalty and artist fees at 30%; Rents at 40%; dividens and interests at 20% and pensions at 12½%.

75. The 1980 issue of the Lloyds Bank Economic Report on Kenya states that regulations issued in January 1979 restrict companies with foreign shareholdings to remitting dividends to a maximum of 10% of the foreign equity capital and/or reserves (p.6). The author is not aware of and has been unable to trace any official publication of any such regulation. If CBK did issue such a regulation, then it was clearly in contravention of Section 7 of FIPA and would therefore be challengeable in court as being legally invalid.

76. Budget Speech 19/6/80, 8.

77. The average increase in this tax - amounting to £3 million for all items involved was 8.125%. On the basis of this we estimate the total declared repatriable income from foreign investments in 1981 at £134.18m.

78. As of today, these vary from as low as 2% of net profit to 15% of sales.

79. Twenty three of the twenty-five projects studied had one form or another of such exemption. e.g. Art.VI of Dawa Pharmaceutical's Management and Technical Assistance Agreement with KRKA of Yugoslavia provides that "All duties, impositions, fees or charges of whatsoever nature imposed upon KRKA now or in the future by the government ... arising out of the performance of this agreement ... shall be paid by DAWA and DAWA hereby agrees to indemnify and to hold KRKA harmless in this respect." This effectively shifts KRKA's liability to Kenyan tax on to DAWA. See also Clause 19 of Kenya Furfural Co. Ltd's Management and Marketing Agreement; Union Carbide Kenya Ltd's Integrated Technical Service and Licensing Agreement Art.5 Clause 5.3 to name just a few.

80. In both cases the fees were either 5% of sales subject to withholding tax or 3% of sales net of withholding tax.

81. The main legislation is the Customs Tariff Act, 1978. See Eglin, 1978.

82. IBRD 1975, 264.

83. 1974-8 plan p.19. The plan goes on to say that "Trade and exchange policy since independence has been based on the following principles:-

    (i) Domestic manufactures should substitute for imports; therefore duties on imported manufactured goods have been high.

    (ii) The investment of capital should be encouraged; therefore, duties on imported machinery have been low.

84. See Ibid, 26-7.

85. Budget Speech 14/6/73, 7

86. See for example 1974-8 plan, 280; Budget speech 1980 and 1981; IBRD 1975; and ILO 1972.

87. See Finance Act 1979. Also Budget Speech 1979.

88. Budget Speech 1981, 9. Also Finance Act 1981.

89. Ibid. at p.8

90. Ibid. See also IBRD, 1975, 280

91. Ibid, 8, 9 and 10. For details see Finance Act 1981.

92. Budget Speech 1981, 9

93. See UNIDO consultant report, 1978, 9,for example,where a foreign embassy's commercial attache is quoted as having said "of course most of our firms make their basic profit on transfer pricing - any additional [declared] profit is considered a bonus."

94. See IBRD 1975, 302,where it observes that "... a wholly foreign owned enterprise (with a 40% overseas corporate tax rate and a 47.5% tax rate in Kenya) would find over-invoicing attractive only if the duty were less than 14%, but an enterprise with 50% Kenyan participation would have an incentive to over-invoice any

imports carrying a duty of less 153%. The larger extent of Kenyan participation, the higher the duty would have to be to discourage over-invoicing. If the Kenyan share were 80% of the equity capital, over-invoicing would be attractive at duty levels of over 500%! Thus Kenya's own policy of encouraging local equity participation in foreign companies is a very potent incentive to over-invoicing."

95. See Budget Speech 1981, 10.

96. See for example SP/10/65

97. See for example 1979-83 Plan, 451

98. Ordinance 48 of 1959. This legislation is now styled 'Act'.

99. S.5C.

100. 1979-83 Plan, 331. See also The Industrial Training (Building and Civil Engineering Industry) (Training Levy) Order, para.2. - LN 237 of 1971.

101. See 1979-83 Plan

102. Ibid, 452

103. Ibid, 37

104. Ibid, 67

105. See for example, the 1970-74, 1974-78 and 1979-83 Plans Sessional Papers Nos.5 of 1975 and No.4 of 1980; Budget Speeches 1972 - 1981; and "Policy Towards Private Foreign Investment; A discussion Paper." 1980 (Internal).

106. See IBRD, 1975.

CHAPTER SIX

CONCLUDING REMARKS

This Study has discussed not only some key regulatory measures adopted by the government vis-a-vis PFI, but also the general policy environment in which these measures have been applied. Its primary purpose has been to bring out the discrepancy that exists between explicit government policy (rhetoric) on PFI and the reality as shown in the practice followed since independence. All along, the view that has been held by official sources has been that articulated by the government and PFI.[1] This view has emphasised that the Kenya government welcomes PFI only on condition that it contributes to the achievement of its economic objectives and further that the government exercise strict control over such investment to ensure that they conform to its stated policies. They cite the government's own rhetoric as incontrovertible evidence that the government regulates PFI. In short, official and business views seem concerned with what appears to be rather than what is. They do not evaluate the operation of the regulatory measures applied to determine their efficacy or otherwise. On the other hand, some academic work on the subject of PFI in Kenya has convincingly shown that they operate in the country relatively free from the rigours of the existing regulatory framework.[2] This study has shared this view and contributed empirical evidence in its support.

A : SOME CONCLUSIONS FROM THE STUDY

The main conclusions are grouped here as they are presented in the study. The discussion in chapter one shows that the reliance on private enterprise as the foundation of the economy has its roots in Kenya's colonial history; that this economic system was introduced to Kenya by the colonial authority primarily to serve the interests of non-Kenyan European population and, therefore, the metropolis; and that as independence approached, strenuous but subtle efforts were made to ensure that the basic economic fabric and ideology obtaining in the twilight days of colonialism survived a change in government. By the time independence came, three main factors militated against any radical change in both the economic thinking and structure by the new African political leaders. First the structure of the economy was already well established by East African standards. To orient the economic system away from the colonial pattern would have imposed great demands on the economy and the political leadership. This would have required a selfless leadership motivated by long term national objectives and great political will to undertake the task. Second, the aspirations, education and attitudes of the political leadership had been shaped in such a way that the soft option of continuing the existing system subject to cosmetic changes seemed to offer the best of available alternatives to the leadership. It was relatively easy to carry on if they consolidated their political power by stifling opposition. It also offered them the chance of

accumulating wealth on a scale undreamt of in the colonial days. Third, the World Bank had presented them with a ready-made economic policy which met both their political and private interests.

In addition, the chapter shows that the legal superstructure necessary to facilitate the smooth operation of the economic system and policies chosen was also formulated in the colonial days. This includes the land legislation as well as that on tariff protection, import and export licensing, financial backing etc., all of which were vital to the development of a PFI dominated economy.

In chapter two, the government's policy on private enterprise and in particular PFI was discussed in some detail. In considering government policy on private enterprise, the discussion clearly shows that the strategies of the colonial authority to bequeath independent Kenya a given economic system and policies to run it were largely successful. The discussion in the chapter brings out both the explicit and implicit acceptance of the inherited economic set up by the ruling regime in Kenya. The government's policy position on PFI is shown to be largely a continuation of existing economic policies. Three main conclusions may be reached from the discussion of government's policy on private enterprise, in particular PFI. One is that the government's orientation towards a private enterprise centred economy reflected not only its acceptance of the inherited

economic system, but also the ideological position of the ruling clique. While the government's rejection of public ownership of the means of production as the ultimate economic goal was absolute and unequivocal, its rationalisation of capitalism as 'African Socialism' was clearly a far cry from advocating socialism. As the discussion clearly reveals, the regime has practised unmitigated capitalism all along. The second conclusion derives from the first as well as the economic fact at independence. This is that, having chosen a capitalist path, the regime had pretty much narrowed its choice of available policy on PFI. The government could not have been expected to turn around and throw out PFI or make its existence intolerable. PFI formed the basis of the economy especially the manufacturing sector. Given this fact, the choice of the end, a capitalist economy, determined the means, at least in the foreseeable future. This means was PFI otherwise capitalism was a long way from producing any tangible benefits for there was little private capital and even less, entrepreneurship, in Kenya outside PFI. The third conclusion concerns the possibility of exercising effective control over investment that the government had wooed into the country with the promise of a blank cheque and of virtually unrestricted freedom of operation. Having set out to attract PFI on quantitative rather than qualitative criteria, the government had narrowed its chances of thereafter effectively regulating PFI..

The unwillingness of the government to be seen as imposing unfavourable regulation on PFI is well reflected in the discussion on the measures it took to safeguard the interests of PFI. The economic and legal incentives discussed demonstrate an approach of a government committed to attracting PFI into the country almost at any cost . It is not here being argued that rigorous regulation of PFI for the national interest is necessarily enough to discourage its inflow. The experience of the Andean group of countries, Brazil, South Korea etc. stands out as clear evidence to the contrary. The point being made here is that this appears to be the view held by the government. Fear of discouraging new PFI or scaring away those already in the country would appear to have played a significant role in staying the government's hand in this matter. Thus the government seems to have 'decided that discretion is the better part of valour'.[3] So far, the discretion has been exercised in favour of PFI. The discussions in the three chapters that follow chapter II provide evidence to support this contention.

The failure of the government to exercise effective regulation over PFI is well portrayed in its foreign investment approval process. In theory, this process is supposed to separate the 'chaff from the wheat' in its selection of the PFI that is permitted to establish in the country. The discussion in the third chapter leads up to the conclusion that this process has been far from being effective in doing this in the past and that the prospects for the future

are not bright either unless the system is overhauled. The process takes the form of bargaining between the PFI and the Kenyan partners on the one hand and the authority on the other hand. It is an ad hoc process based on a case by case approach. It may be argued that this approach provides a more flexible set up than apriori terms and conditions to be fulfilled by all PFI. However, this presumed advantage is only realizable where capabilities to bargain with PFI are adequate and properly utilised. In Kenya's case, the existence of these presumptions has not been borne out by experience.

The discussion on the approval process in operation in Kenya leads to several important broad conclusions. The first of these is that the process does not really screen proposed projects, but rather endorses the proposal of whichever investor is selected. The selection is usually arbitrary and often does not involve the stated machinery. The Ken-Ren and Firestone examples discussed in this study provide telling examples of this endorsing role of the approval machinery. As between competing applicants, the process chooses one or more of them (i.e. if given a chance so to choose, which is not always the case) and then proceeds to endorse his proposal. Most projects' preparation and search stage is executed by the interested foreign party. They usually conduct the feasibility studies upon which so much of the evaluation is based by the approval machinery.

The evaluation process rarely prepares its own feasibility studies or even subjects those prepared by the foreign party to serious critical analysis. What this means is that the agenda for the evaluation as well as the information and data necessary to make an informed evaluation are both supplied by the foreign parties. In legal terms, it is like asking a defendant to prepare the evidence upon which the plaintiff will rest his case against him. The second conclusion to emerge from the empirical investigations is that the PFI , so far as is possible to generalise from those studied, appear to have had a field day in their negotiations with the Kenyans. The corollary to this is that the process has, therefore, been of neglible constraint to PFI operating in Kenya. In fact, far from being a constraint, PFI has found the bargaining process to be of great advantage in their favour. Knowing that the regulatory measures applicable to their operations are subject to government discretion as to whom they apply PFI has, more often than not, used with considerable success, the bargaining process to have the government exercise its discretion in their favour. This has involved obtaining exemptions from legal obligations such as payment of some taxes, limitation of local borrowing etc., as well as the government using its powers to stifle competition. In all the cases studied, the process conferred more privileges on PFI establishing in Kenya than the constraint it imposed on them. Strangely enough, the process does not seem sufficiently concerned with the ability and capacity of the chosen PFI to deliver

their part of the bargain. This has led to what, in some of the cases, can only be classified as acceptance of pirate companies. But why has the process performed so badly?

As pointed out earlier, apart from the difficulties posed by the complexities of the issues involved, policy factors have contributed greatly to the failure of the process as a regulatory measure. First, because of the government's concern with attracting PFI, it has failed to establish a viable institutional machinery for evaluating proposals submitted by PFI and developing the requisite capabilities over time. An effective regulatory system would call for minimum rules to be satisfied; clear policy guidelines that provide as precise criteria upon which to evaluate a project as possible; a decision-making process based on objective consideration of the facts rather than on arbitrary exercise of discretionary decision-making power;; a well organised and co-ordinated institutional machinery capable of accumulating evaluation capabilities through learning by doing, as well as collating, analysing and using available data and information to maximum benefit. All these factors are missing in the Kenyan approval process. They are missing not because they are impossible to achieve, but because the government appears not to have been particularly keen on them.

The ad hoc case by case approach to evaluation means that there are no minimum rules to be satisfied because each PFI is likely to negotiate for different terms of entry. Every issue is, therefore, negotiable. The flexibility afforded by this system undermines the bargaining base of the approval process. Such rules usually constitute a bargaining base and leverage not obtainable otherwise. The lack of clear policy guidelines complicates the matter even more. What criteria should take priority? Foreign exchange earning and/or saving prospects? Creation of employment? Generation of technical skills? Creation of export capabilities? The cost of a proposal project? All these or a combination of such issues and many others should be clearly laid out in identifiable policy guidelines. At the end of the day, they determine the value of a project to the nation. No such policy guidelines are available in unequivocal terms to the Kenyan approval process. If any have been made available, their subsequent exclusion by decision makers involved may have rendered them incapable of any rational sense of application.

The ad hoc approval process has also meant that no institution has developed in the country capable of evaluating PFI projects. The New Projects Committee, for example, is itself an ad hoc body whose membership is constantly changing. It has built up little expertise and capabilities or any recognisable evaluation techniques. As the process

operates at present, it allows the fragmentation of the Kenyan parties involved into groups pursuing separate and often opposing interests in the course of approving PFI projects. This fragmentation of the government's organs into separate interest groups has in the past resulted in these groups being pitched against each other. The only party who benefits from this fragmentation is the foreign applicant. In addition to this weak point of the approval process, the empirical investigation in this study reveals the decision-making on who to let in and under what terms, to be highly discretionary and susceptible to political intervention from higher authorities. The decision-making process is virtually divorced from the approval process. The latter, when it comes to decision-making, is not only a toothless puppy, but one without a tongue either. It cannot even as much as bark! Those involved in the approval process have no power to make decisions on the basis of their findings. They cannot even question a decision overruling their recommendations. The views of the Kenyan personnel submitted to the decision-makers do sometimes end up as mere piles of internal memos while the decision reached has little resemblance to the analysis and recommendations contained therein. The discretion of the decision-makers is absolute and because they are located high up in the political hierarchy, they appear not to be accountable for the consequences of their decisions. Because of this highly discretionary decision-making process, exemptions from regulation have become the rule rather than the exception in the arrangement reached with PFI during the approval process. Obviously, such a system is

extremely susceptible to corruption, political interference as well as to demoralising those in the process who see their recommendations sacrificed in preference to personal pecuniary, political or other interests.

A common notion that pervades both capitalist and non-capitalist economic thinking is that ownership of majority or controlling equity constitutes a viable basis for exercising control over investment. This view seems to be firmly held by the Kenya government. It has, therefore, encouraged an Africanization programme partly as a way of regulating and controlling PFI. The discussion in chapter IV shows the programme has not been particularly successful and that, in its present form, is not likely to succeed in wrenching control from PFI in projects it is involved. There are three broad reasons suggested in the discussion for reaching this conclusion. One is that the programme has concentrated on mere acquisition of equity without paying enough attention to the development of indigenous entrepreneurial capabilities. Two is that the programme seems indifferent to the very successful use of non-equity channels of exercising control. This success has no doubt been facilitated by the first reason above. Finally, Africanization of both equity and personnel has, in the majority of cases, led to an alliance between foreign capital and the local bourgeoisie who, in a large measure, have political control over the country.

This study has also shown that despite government rhetoric against direct public participation in the economy, it has nevertheless increasingly participated in equity in areas that do not readily fall under its stated narrow scope in which such ownership would be undertaken.[4] This has forced the government to shift its rhetorical emphasis from that of a private enterprise economy to that of a mixed economy.[5] This shift was clearly necessary because, except in commerce and real estate, there was little private capital investment by the local African bourgeoisie. As this was the one area in which PFI still heavily dominated by the end of the 1960s, the government was under some pressure from this class to pave the way for their entry in industry in partnership with foreign capital. Hence the concentration on the acquisition of equity in foreign controlled enterprises. The objective reality is that the programme as has been in existence so far, has been aimed at, not the displacement of PFI from the country, but participating in the profit sharing with such PFI. As long as the profits continue to flow to the local shareholders, the programme would not concern itself with matters of control. In this sense, the parastatals are simply paving the way for the entrance of local private capital by absorbing the initial losses. At least this was the original intention. The principal goal of Afrinanization is, therefore, not to take over the running of the economy, but to participate in foreign owned enterprises. Nowrojee has aptly described this aspect of Africanization in the following terms:

> ... Africanization is not participation in domestic enterprise, it is participation by domestic capital in foreign private enterprise. Foreign interests are content to have this happen. It ensures their continuance, and diminished profitability is compensated by increased security. Africanization thereby only assists in leaving untouched the neo-colonial process. The implementation of africanization through the parastatals additionally disguises that result. This is because, firstly, the policy has promoted apparent and not real change by putting in african replacements in privilege sharing positions instead of ownership and control; secondly, the parastatals as government bodies carry out the exercise. This allays suspicion and makes it easier to mistake a substantial profit or monetary gain for genuine ownership. When the parastatal shows a profit it is easier to lose sight of the question: Did it gain control? For the price of profit is non-interference. 6

This describes the reality of Africanization in Kenya today as presented in this study. In concentrating on acquisition of equity, the Kenyan authorities have lost sight of the need to master the strategies and instruments of control used by PFI. Africanization has not, in the past, sought to develop local entrepreneurial capabilities, but merely to share the profits from projects totally dependent on foreign entrepreneurship. This explains the abdication of managerial, technical and marketing roles to the foreign parties as outlined in this study.

Far from limiting the abilities of PFI to control economic operations in which it is involved, Africanization has provided a valuable and effective buffer between the government's actual and potential regulation and such

investment. As the study shows, PFI has effectively used its local partners and personnel as a lobby against unwelcome and for welcome interference. Thus for example, ICDC, IDB and DFCK, all major conduits of government participation in partnership with foreign capital, have played a major role in pressurising the government to abolish sales tax on imported machinery which their foreign partners supply; to lower or abolish duty on raw materials imported from their foreign partners; to maintain a quantitative restrictions based protection of industry system which favour PFI operations in the country etc. In addition, local equity participation has greatly reduced the economic risks undertaken by PFI by ensuring them access to otherwise unavailable local risk capital. The interests of the local partners in deriving profits from the partnerships makes them natural allies of PFI in resisting unfavourable government regulation. The African personnel in such projects play a similar role to those of their fellows in equity partnerships. Like the latter, the former's privileged financial positions are invariably tied to the presence and flourishment of PFI.[7] This phenomenon is not unique to Kenya. Writing about Morocco, for example, Pierre Jalee has this to say on the impotence of local equity participation per se as a means of controlling PFI.

> ... foreign capital is often associated with Moroccan private capital or Moroccan public capital or both together. The foreign capital is quite happy to be minority partner and even suggests that it should be, as evidence of the purity of its motives. It goes so far as to

> agree to a Moroccan chairman of the Board of Directors accepting for itself a deputy director, and why should it require more? It knows that the enterprise is viable only on the basis of foreign technical capital. Although in the majority, the indigenous capital is the prisoner of its foreign partner. Mixed investment ... ties up the indigenous capital of the host country and denationalizes it. 8

And so it is in Kenya. Local capital in joint venture with, or leasing technology etc. from, foreign capital has become the prisoner of the latter. It has acquired part, or 100%, ownership in many projects, but foreign capital still calls the tune in the operation of these projects. The present Africanization of equity and personnel, while successful in Africanizing the major economic risks, has left the job of Africanizing effective control unaccomplished. Other means of control have effectively been applied by PFI to shift control to the foreign interests displaced by the Africanization programme.

The last chapter of the main body of this study looks at some financial and fiscal regulations applied to PFI in Kenya. The discussion examines the nature and operation of these measures and suggests that they have been largely ineffective constraints on PFI operating in the country. Four main reasons are suggested as contributory factors to the failure of these measures. First, their potential effectiveness is frustrated by the government's heavy commitment to attracting PFI into the country which, in a bid to

create a hospitable investment climate, leads it to handle such investment with 'velvet' gloves so to speak. This frustration is particularly apparent in the CBK's exchange control role under the ECA whose effectiveness in controlling or regulating repatriation of funds by PFI is greatly hampered by the legal guarantees afforded to such investors under the provisions of FIPA. Second, many of these measures are rendered inapplicable to particular PFI by exemptions and privileges granted to them by the government on establishment. This is a direct result of the government's case by case bargaining approach during which a foreign investor is able to squeeze as many concessions as he can from the government. An example of such concessions and privileges expressed as contractual obligation of the government is reproduced in Appendix 1 of this work. Many of the concessions and privileges exempt the establishing projects from one or more obligations imposed upon it by law or administrative practice. Where such exemptions have been obtained, the financial and, or, fiscal regulation is rendered useless. Third, many of these regulatory instruments are simply inadequate to deal with the complex global operations of MNCs who are the major PFI operating in Kenya. For example, the exchange control regulation, the income tax, the customs etc. machinery established by law seems designed to deal with straightforward, honest transactions by those who are subject to these regulations. They do not take into account the fact that in business, morality (e.g. honesty) takes second place after business interests. PFI have a wide scope

to avoid financial and fiscal regulations through the medium of transfer accounting.[9] The global nature of their operations makes controlling their operations an extremely complex task. Their attitude towards regulation does not simplify the task either. One managing director of an MNC subsidiary is reported to have said

> We would not knowingly break the rules anywhere ... We always employ one set of experts to tell us what they are, and another set to tell us how to get around them.

And another one that

> It is the job of governments to make the rules and ours to find the loopholes.10

Most of the financial and fiscal legislation was not designed for, and has not been adapted to deal with, such complex global operations as are presented by many of the PFI in Kenya. Finally, the machinery of enforcing the regulation lacks both institutional coherence as well as financial and human resources. The blame for institutional incoherence of the machinery as well as the limitations in available resources may, with reasonable justification, be laid at the foot of the government. The study has, for example, shown that there is little coordination between government institutions e.g. the CBK and the income tax department; the customs department ; the ministry of industry etc. Coordination of the relevant government departments in any significant form appears to be absent and little effort seem to have

been spent on rectifying this haphazard organisation of financial and fiscal regulatory machinery. For the last eighteen years since independence, the government has not seen it fit to have a special training programme for personnel specialising in monitoring and regulating the activities of PFI. The bulk of exchange control in the CBK for example, is carried out by ordinary bank clerks without even basic training in the tasks they undertake.[11] The income tax and customs departments have fared no better. Failure to train personnel capable of monitoring and analysing PFI's financial, production and marketing operations in their global context means that even if the legal set up in existence were suitable to deal with MNC's global operations the manpower constraint would greatly hamper its efficiency. The attempt by the CBK to use external expertise in the form of GSC, has clearly not proved effective despite GSC's unverified claims. The cost of engaging GSC, added to the acknowledged but not quantified loss through PFI's financial manipulations,[12] would have been more than adequate to set up a specialised institution staffed with specially trained personnel to monitor and regulate the financial and fiscal aspects of PFI operations in the country. Once again, the government seems to have lacked the political will (not power) to strengthen its capabilities to financially and fiscally regulate PFI in the future.

The discussion and analysis of the empirical investigation in this study have been conditioned by two main

hypothesis. The first is that the overall economic policy pursued by the government determines the nature and extent of the regulation of PFI adopted as well as the political commitment to enforce any regulation that may be imposed, reluctantly or otherwise. The second is that PFI is capable of, and likely to try, countering any regulatory measures imposed by the government with some considerable success. The empirical investigations in this study have shown that government policy-induced factors in conjunction with PFI counter-regulation strategies have led to largely ineffective attempts to regulate and control PFI in Kenya since independence.

B : SOME OBSERVATIONS

From these broad conclusions, we can venture to make the following observations on the current system of regulating PFI in Kenya. First, the government's belief that strict regulation might keep PFI away does not seem to be founded. However, even if it did, it may not necessarily be to the detriment of the national economy. The past experience could be said to be ample evidence for the proposition that PFI needs to be regulated if the country is to rely on it to provide the foundation upon which an independent economy is to be built. It would therefore, be in the interest of the government to formulate a workable regulatory policy that would operate without fear or favour.

As the discussion in this study indicates, the government has yet to formulate a comprehensive policy and strategies towards the long term prospect of PFI. No effective regulation of the same would be possible without clearly defined objectives. The formulation of these is a political matter which the government of the day has to face. The choice of economic ideology has been made in favour of capitalism not so much through a clearly articulated capitalist ideology, but rather by a clear and unequivocal rejection of socialism.[13] In practice the ideology followed has been capitalism pure and simple. This practice has been greatly influenced by the concentration in the country of most of the PFIs operating in East Africa.

Having chosen a capitalist path, the government has to make a choice whether to let the economy remain a dependent peripheral capitalist or an independent one. The choice is important in selecting the regulatory policies to pursue towards PFI. It is upon the choice of policy made that the degree of political will to control and regulate PFI will rest. The more the policies are oriented towards the attainment of economic independence in the long run, the stronger the political will required to enforce the necessary regulation for the achievement of this objective. The choice is between controlling the economy through public ownership or through domestic private capital.

If the control of the economy is to come through domestic private capital, then the Africanization programme will need to be considerably overhauled. In its present form, it produces profit receivers, managers and servicemen for what are still essentially projects controlled by foreign capital with or without equity holding. The challenge of the programme is to produce entrepreneurs capable of running the economy without undue reliance on foreign capital. The present breed of local capitalists is essentially a distributor and consumer class (except in agriculture). Swainson's and Ley's claim of an existing independent local industrial capitalists is as yet to be empirically verified. Indeed, the very personalities they cite as proof of their claim of the existence of such a class are the best examples of the comprador nature of the notable local

capitalist class.[15] Available evidence clearly shows that as the leading local bourgeoisie began to move into industrial activity, they have become more and more dependent on foreign technology, knowhow, management and entrepreneurs.[16] It seems that Swainson and company have equated accumulation of wealth with economic independence. The onus is upon them to prove that this is necessarily so.

If the comprador nature of private capital is to be changed into a more dynamic and independent one, it is necessary that the government change its present industrial policies and strategies. This will not be an easy task. It will involve a review of the role of PFI under whose shadow the domestic entrepreneurship has had to operate for decades. The formulation of appropriate policies will require a detailed review of the operation and effects of the present Africanization policy. We would suggest that in formulating a new policy, the primary objective should be the development of indigenous entrepreneurial, managerial, technical and marketing capabilities rather than mere acquisition of shares in existing or new foreign controlled operations. This would be a medium and long term rather than a short term programme.

In the present Kenyan circumstances, certain reorganisation in the regulatory process appears necessary if PFI is to be used constructively. In the initial stage, the concern should be on utilising PFI to build up a viable

relatively independent domestic economy, be it public or private controlled. Thus any regulation imposed on its establishment or operations in the country should be concerned first and foremost in directing its resources towards the task of developing a viable self-sustaining domestic economy. It is our opinion that a lot of efforts have to be made to orient the present role of PFI in the country towards the development of such an economy. The regulatory framework in existence does not appear to have been designed to significantly alter the role PFI has played in the economy so far. Perhaps it was assumed that participation of domestic capital in PFI operations would lead to the former taking over. While this remains a possibility in years to come, it has to be borne in mind that the interests of domestic capital are not necessarily identical to those of the nation as a whole. This is particularly so where the domestic capital happens to be private capital, or even public capital operating on capitalist economic principles as is the case in Kenya. With this in mind, some active regulation by the state may be a prerequisite to re-orient the role of PFI in the manner described. Here we must register a caveat. In Kenya today, it is difficult to separate the interests of private capital from those of the powerful political elements in government that have a virtually unchallenged control over the affairs of the state. This is so because though state institutions of governing exist in the constitutional set up, the reality is such that institutions derive their power from personalities rather

than vice versa. Thus though parliament is declared to be supreme in the constitution, the practice provides a stark contrast to supremacy. As economic policy has never been subject to unqualified public discussion in independent Kenya, it is these same elements in the government that have determiend the policies adopted towards PFI and its role in the economy. It is therefore their attitude to PFI as well as to the economic structure in which it operates that counts. Ten years ago, the ILO mission to Kenya described these attitudes thus

> Kenyan attitudes and aspirations had perhaps been moulded more than was realised ... by the colonial experience of having to accommodate oneself and to work within the existing structure of the economy rather than to change it. Thus when national independence was achieved the political aim of taking over the economy became merged almost imperceptibly with individual aspirations to take over the jobs, positions and the lifestyles which the economy made possible. 17

It is in changing these attitudes that the present governing regime will need a strong political will. Such a change of attitudes will affect their private interests which as stated above, are essentially one and the same with those of private capital.

Asuming the existence of political will to override the private interests in favour of public ones, three main suggestions regarding regulation of PFI may be made based on the empirical investigations in this study. First, there needs be a moratorium in the establishment of projects

dependent on foreign capital. It is our view that too many such projects have been established in the last fifteen years without due regard to the alternatives available; the short and long term costs and effects of the projects; their relevance and priority in the economy; and above all, the nation's capacity and ability to absorb and utilise them efficiently and to the public good. This has stretched the nation's limited human and financial resources to a level that only casual attention is paid to many of these white elephants. The benefits that have flowed from these projects have not always been without a high price to the nation. In addition they have resulted in to overcapacity in some areas leading to significant capacity under-utilisation, a waste the country can ill-afford. For these two main reasons, a moratorium may be a wise move. The opportunity should be taken during such a moratorium to review, through comprehensive investigative studies, the performance of all major projects involving PFI as well as to determine their contribution or otherwise to the achievement of a viable domestic economy. The investigation should be of a public nature with all findings and recommendations available to the public. Publicity has for so long been kept out of dealings with foreign capital that it has been possible to render the decision-makers in government unaccountable for their actions owing to their secret nature. On the basis of such investigations, the government should then prepare a review of the organisational structure of existing projects, as well as the criteria for admitting new

PFI into the country. The primary criterion for determining the desirability of a project should be its long term positive contribution to the nation's capabilities to achieve meaningful economic independence.

The second suggestion relates to the institutional set up for the regulation of PFI. It is the view of the author that the regulation of PFI should be undertaken by a specialised agency independent from government control. This agency should also undertake the job of monitoring the operations of PFI in the country. The agency would coordinate with all government departments and have access to all records and documentation relating to all PFI operating in the country. Its ultimate objective would be to train and develop manpower and develop technical capability to deal with foreign firms operating in Kenya and to serve as a depository of complete records on the activities of PFI in the country. An important authority the institution should be given is that of being the final authority (excepting a court of law) to determine all matters connected with PFI. No political institution or personalities should be given a veto over the agency's decisions or the power to appoint any of the key personnel of the agency. The agency should preferably be established by statute. Its proceedings should be available to the public and its decisions subject to public debate. Publicity would help reduce the common political pressure such institutions are likely to be subjected to. Once again, the setting up of such an agency

should be seen as a long term undertaking. It would certainly take several years before it is sufficiently operational as well as being manned by well trained local personnel. The cost of setting up such an agency may appear to be prohibitive at first instance, but its benefits in the future can be in no doubt whatsover.

Finally, it is suggested that in its formulation of policy on PFI and its regulation, the government should pay much more attention to economic development and equitable distribution of the nation's wealth than it has done so far. In the past, it has emphasised economic growth above equity issues which has meant that the tangible benefits of PFI have accrued to a very small proportion of the population which have in turn tended to align themselves to it. A system that promotes benefits to a select few instead, or at the expense, of the nation as a whole is likely to promote a comprador bourgeois capitalist class whose interests may be more in line with those of foreign capital than with those of the national economy. It would make the task of achieving a self-sustaining domestic economy independent from foreign capital much more difficult with such a class wielding both economic and political power.

C : A FINAL EMPHASIS

A critical fact that any government seeking to regulate PFI ought to realize is that any form of regulation is only a means to an end. Regulation of PFI must have an objective or even many objectives. Thus the regulation imposed must be carefully planned and firmly enforced with reference to specified objectives. Regulatory responses to incidental or isolated occurences cannot be the basis of a sound and effective regulation of PFI. It is not the legislation that is passed that makes regulation effective and beneficial. Rather it is the soundness and sense of purpose of the policies upon which the regulation is based that make it worthwhile. All over the world, regulation of economic activities conforms to wider social, economic and political policies and strategies. And so is the position in Kenya.

The Kenya government has so far shown an ambivalence in whether or not to secure more control over activities of foreign capital in the country.[18] Such ambivalence must end if significant advances are to be made towards controlling PFI in the country. The intended role of PFI must be specified as clearly as possible and its regulation designed to ensure that it plays this role in a satisfactory manner. It is imperative to understand that the nature and extent of regulation will be determined by the role assigned to PFI in the economy and not vice versa. In turn, the role assigned to PFI will be dependent upon the country's broad social,

economic and political ideology.

Implementation of regulation of PFI is every bit as important as the formulation of the same. It is, however, a much more difficult task than its formulation. While very good policies may be formulated and eloquently articulated in rhetoric, it is their implementation that gives them meaning and distinguishes them from mere hollow rhetoric. Thus for example, while the Kenya government has been prolific in its rhetoric about its commitment to a fair distribution of incomes,[19] in practice it has pursued policies that have achieved the opposite.[20] A strong political will is required to enforce any regulations imposed on PFI operating in the country. In this study, we have seen that lack of political will, as opposed to power, to enforce existing regulations has left PFI very much free to pursue its interests with relative ease. There have been far too many and unnecessary concessions and compromises to PFI from the government to the point that they may now be said to have become the rule rather than the exception. Political will is also necessary to change the attitude of policy formulators towards a much more dynamic drive towards economic independence rather than the present attitude of seeking to work within the existing economic structure. They should be prepared to change or modify their present economic ideology if it stands in the way of the search for economic independence.

This study has not, on the whole, addressed itself to the broader issues of the choice between a socialist or a capitalist economy and also that between a public or a private capital centred one. It has been largely confined to an evaluation of some of the existing regulation on PFI in the present Kenyan economy. It is, however, doubtful whether an independent economic system truly based on private domestic capital in the country is feasible in the near future within the present political and economic environment. At present, private capital involved in production is significantly foreign owned and/or controlled and is likely to remain so for some time to come unless a change in economic policy is made. In addition, even those production operations that appear to be in the hands of domestic private capital are substantially dependent on external resources. and are therefore, not self-sustaining in the absence of such external resources. Few of these have bothered to develop their own capabilities instead of relying on those of foreign suppliers. This has to, a large extent, been a function of government economic policies in particular industrial ones. If the country is to succeed in attaining a viable independent economy that in addition distributes benefits fairly equally throughout the entire population, then it would appear to us that a capitalist oriented economy is not one that is properly equipped or inclined to meet these fundamental goals.[21] In an economic system governed by the ethos of private capital, private interests are likely to take priority over public ones. This likelihood

is even more in a country like Kenya where a substantial portion of the private capital in domestic hands belongs to those few who wield political power. Indeed, this appears to have been the case in Kenya, a fact that the government explicitly admits. Thus the 1979-83 Plan observes that

> The progress achieved since independence [in economic growth] has unfortunately been accompanied by an erosion of the high ethical standards that once were typical of African society. Private interests have too often been placed ahead of the public interests: the social sanctions which controlled such behaviours in the traditional African setting have not yet been successfully emulated in the modern setting of a national economy. 22

Instead, the 'ethical standards' of a capitalist economy have been substituted for those of the 'African tradition'. A substantial proportion of the private interests that have 'unfortunately' overriden public ones, have been associated with PFI.

NOTES

1. See for example, all the Development Plans since 1966; IBRD, 1975; and Business International, 1980.

2. See Langdon, 1976: Leys, 1975; Kaplinsky, 1979; Hopcraft, 1980; Eglin, 1978; and Mutunga, 1979.

3. African Business, November 1979, from where this phrase is taken. It was their analysis of why the Kenya government was doing nothing to bring Del Monte to book for its transfer pricing activities.

4. SP 10/65

5. 1974-78 Plan, 2, 1979-83 Plan, 332

6. Nowrojee, 1975, 160. (emphasis added)

7. For a detailed account of this alliance, see Langdon, 1976, Chapter 3.

8. Quoted in Nowrojee, 1975, 161. (empahis added)

9. For details, see for example, Tugendhat, 1971 and Lall, 1977

10. Both these quotes are taken from Tugendhat, 1971, 163

11. For example, out of about 150 personnel in the CBK's exchange control department, only 10 have some relevant qualifications and some training, but none of these is specially trained in matters dealing with MNC's global operational strategies and techniques.

12. See Budget Speech, 1980; ILO, 1972; IBRD, 1975 and Kaplinsky, 1979 for examples.

13. See SP 10/65

14. Swainson, 1980; Leys, 1978 and 1980

15. These are: Njenga Karume, Udi Gecaga and Ngengi Muigai.

16. This is the case with Gecaga and Muigai in the AVA; Karume in Dawa Pharmaceutical and Kalinga in J. K. Industries, for example .

17. ILO, 1972, 87

18. See IBRD, 1975, 308

19. See SP 10/65 and all the Development Plans since independence.

20. For government's explicit admission of this, see 1979-83 Plan, 5.

21. In addition to the achievement of economic independence, alleviation of poverty is declared to be the central theme of the 1979-83 Plan. Among measures expected to alleviate poverty is the equitable distribution of incomes - see pp. 2 and 5.

22. 1979-83 Plan, 23.

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EXTRACT FROM KCFC's JOINT VENTURE AGREEMENT

ARTICLE IV

UNDERTAKINGS BY GOVERNMENT OF KENYA

SECTION 4.01 GOK shall grant or cause to be granted to the Company, in good time for the purposes of the project, title to and possession of, and GOK shall further procure or cause to be procured the provision to the Company at those favoured rates of such piece or pieces of land as are considered by the Management adequate for this project and its future expansion of an area as shall be accepted by the Company in Kisumu as suitable for the purposes of the project, including the plant and other industrial buildings, offices and residential accommodation.

Such land shall be granted for a leasehold term of at least 99 years, and upon the term and conditions and at a cost no less favourable than those applied to other projects. GOK shall further procure or cause to be procured at no cost to the Company, the provision to the Company of the followingservices or facilities in good time for the purposes of the project:

(a) Electric Power - 6 MVA
(b) Water - 1,000,000 Imperial gallons per diem
(c) Effluent disposal - 225,000 gallons per diem
(d) All facilities such as road, water supply, electricity connection, telephone, rail access, affluent disposal and similar services required for the operation of the Project and all GOK approvals and licenses for the same.
(e) All permits, authorizations, approvals and licenses required for the establishment and the efficient and profitable operation of the Project and the Company in Kenya

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(f) All port facilities necessary for the expe ditious unloading of the materials and equipment required for the establishment and operation of the Project and their transport from the port to Kisumu, and all port facilities necessary for the export of the Factory's products.

SECTION 4.02 GOK undertakes to arrange the supply to the Company of adequate supplies of molasses at reasonable prices and all other local supplies necessary for the operation of the Company's business to enable the Company to meet its own minimum production standards per annum, and to make all such other local arrangements as may be necessary. Furthermore, GOK shall procure that the outlets for power alcohol salers within Kenya to patroleum companies respectively and-users shall be arranged.

SECTION 4.03 During the period from the date hereof until 12 months after the Project Completion Data, GOK shall grant to the Company or (as the case may be) o the contractor employed by it for the construction of the Project, as and when required:-

(a) all import and other licences and permits required for the import into Kenya of all plant machinery, equipment, materials, tools and spare parts which are required:-

i) for the construction and equipping of the Project under this Agreement or under the construction contract for the Project; and

ii) by such contractor for the carrying out of such construction work:

provide that this paragraph (a) shall not apply to furnishing, standard office quipment and non-specialised vehicles for use on roads or excluded from import under, the provisions of the Restricted Imports (Commercial Motor Vehicles) Order 1975 as for the time being in force, which are ordinarily available in Kenya.

(b) exemption from all import duties, other than sales tax, in respect of the items authorised to be imported under paragraph (a) of this Section except:-

i) any goods which shall then be produced and be available in Kenya in appropriate type, quality and quantity and at a competitive price and at the appropriate time ("competitive price" meaning the price of goods produced and available in Kenya compared with the cost of like imported goods when landed, free on rail and duty paid, at Mombasa and "produced" including assemply or processing at any factory in Kenya); and

ii) items of contractors' equipment covered by sub-clause (ii) of paragraph (a) of this section.

All such importation as is mentioned in this Section shall (unless otherwise required by GOK) be subject to surveillance of General Superintendance Company (or other agent appointed by GOK for such purpose) under the present procedures for the import of goods into Kenya (in addition to the usual Customs procedures).

Should GOK determine at any time up to the Project Implementation Data as defined in Section 6.02 that import duties shall thereafter be levied on any or all of the above imported items then the Subscribers hereby agree and shall vote and cause their Directors to vote for an increase of share capital of the Company equal to the amount of said import duties, to be allotted to GOK alone, for which GOK shall subscribe and pay up. GOK shall grant the Company as and when required after the Project Completion Date:

(a) all import or other licences and permits required for the import into Kenya of all raw materials, consumables, equipment, machinery, machines, spare parts and fuel as are required for the proper operation for the Project: Provided that such items or any of them shall not at the relevant time be available for supply in Kenya

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in appropriate type, quality and quantity and at a competitive price (as above defined);

(b) until the Project achieves full capacity as described in Section 2.01 or until the total Overseas Credits specified in Section 2.02 (b) (III) have been repaid, whichever shall first occur, full exemption from all customs duties (other than Sales Tax) on the items imported. under paragraph (a) above; provided that such items shall not then be produced and available in Kenya in appropriate type, quality and quantity and at a competitive price (as above defined) and at the appropriate time.

(c) after the period specified in paragraph (b) above, such exemptions from duties and taxes as shall be determined by GOK from time to time in accordance with its usual discretionary duty remission policies, but so that the Company shall not be treated any less favourably than other manufacturers benefiting from duty remissions in similar undertakings:

SECTION 4.05 GOK hereby undertakes to grant or cause to be granted all approvals and licences subject to normal procedures necessary to establish and to operate the Project and in particular but without derogating from the generality of the foregoing:

(a) As the Project shall have been granted approval in principle under the Exchange Control Act, all Exchange Control approvals required for its completion and operation shall be granted by GOK simultaneously and GOK undertakes that appropriate foreign exchange shall be made available for remittance outside Kenya for:

i) payment for all raw material imports;

ii) payment of commitment fees and prepayment premiums;

iii) repayment of all loans and interest payments thereon;

iv) payment of all dividends to non-residents of Kenya;

v) payment of all fees and charges payable

under the PIMA Agreement and the TEA Agreement for sale of management services, machinery, know-how and engineering services (including per diem);

vi) repatriation of Kenya income and other allowances of expatriate employees of the Company in accordance with the practices prevailing at the date hereof.

(b) overdraft facilities in accordance with the prevailing exchange control regulations but the company will not be treated any less favourably than other companies of similar size and nature. Subject to discretion of Exchange Control, all exchange control consents and approvals required for the remittance outside Kenya of the proceeds of sale in respect of Shares of the Company subscribed by CIC and Advait.

(c) The Company shall be granted permission, during the period from the first subscription of equity under Section 3.01 until the Project Completion Date (as below defined) to maintain and operate banking accounts in Zurich, London and Vienna and such other place or places as the Company may request and GOK agree, for the purpose of receiving moneys from CIC and Advait, being non-residents of Kenya, and of paying the expenses of the Company incurred and payable outside Kenya, provided that the Company shall submit from time to time as required by the Central Bank of Kenya such information as that Bank shall require and the Company shall comply with all controls and directives from time to time established by the said Bank.

(d) Any entry, work or residence permit required by any of the employees or advisers of the Company who are needed and required as designated by Management shall be promptly issued for as long as such qualified personnel are not available from Kenya Citizens.

(f) All necessary trading licences for the Company and export licences in conformity with Section 5.03.

SECTION 4.06 GOK shall ensure that all its own departments and agencies shall extend the same favourable purchasing policy in respect of the Company's products which is generally extended from time to time locally manufactured goods under GOK's and local authorities purchasing policies.

SECTION 4.07 GOK undertakes that exemption from tax shall be granted in respect of any payments arising out of this agreement and the Agreements contemplated hereby and made by the Company to Swissbank, OKAG and/or their sponsored banking institutions or other foreign government or government sponsored lending institutions that shall have entered into such Agreements with the Company and the Company shall not be required to deduct at source any tax in respect of any such payment.

SECTION 4.08 GOK shall guarantee the due payment by the Company of the principal and interest on credits that shall or extended by any foreign government or government sponsored institutions including but not restricted to Swissbank and OKAG sponsored institutions. Where such financial institutions require for whatever reason the participation of other institutions GOK agrees to guarantee those credits extended, by virtue of these requirements, by any such financial institutions.

APPENDIX 2

EXTRACT FROM RIVATEX'S JOINT VENTURE AGREEMENT

NOW IT IS HEREBY AGREED as follows:-

1. *This Agreement will come into force and (subject to the provisions hereof) shall be irrevocably binding upon the parties hereto from the date of signature hereof.*

2. *SEDITEX shall by the Commencement Date enter into firm and binding contracts with suppliers chosen by SEDITEX for the supply and delivery of all machinery and equipment mentioned in the Final Proposals upon the dates according to the specifications at the prices and subject to the conditions of payment mentioned in the Final Proposals.*

3. *ICDC shall by the Commencement Date obtain from the Government a Certificate of Approved Enterprise under the Foreign Investments Protection Act in the name and in favour of SEDITEX in PIVATEX as detailed in the Final Proposals together with all other consents and approvals from Exchange Control and other authorities to assure to SEDITEX's satisfaction the free repatriation (in the currency of original investment) of the total proceeds of realisation of such investment and all deividends and other income accruing therefrom together with the like consents and approvals for the payment to SEDITEX out of Kenya of the remuneration payable to it under the said Technical Services and Supplies Agreement and Managing Agency Agreement.*

4. *ICDC shall obtain from the Government and all relevant local and other authorities assurances satisfactory to SEDITEX and RIVATEX concerning the grant and provision to RIVATEX of title to the plot of land in Nakuru aforesaid already identified by and known to the parties hereto together with all such water, electric power. railway, port and other facilities as mentioned in Article 6 of the said Technical Services and Supplies Agreement so as not to hinder progress or cause any delay in the completion of the Project according to the Realisation Schedule in Appendex I of the Final Proposals.*

5. *ICDC shall obtain from the Government assurances satisfactory to SEDITEX and RIVATEX that imports into Kenya of textiles in general and polyester and polyester blends in particular shall be so rationalised or controlled that such imports shall in no way interfere with or prejudice the production and marketing by RIVATEX of all lines of textiles and other products to be manufactured by the Project upon economical and competitive terms.*

6. *ICDC shall obtain from the Government assurances satisfactory to SEDITEX and RIVATEX to take all such steps as may be necessary and practicable in view of the approved status of the Project and the heavy finance charges and depreciation costs involved therein, to exempt RIVATEX from or minimise the impact upon RIVATEX of Sales Tax and similar impositions upon machinery and raw materials together with the like assurances that the capital machinery necessary for the Project may be imported into Kenya free of any fiscal entry import duty or other like duty or levy· together with the like assurances that Rivatex shall obtain in respect of its importations of machinery and materials at least as advantageous exemptions, remissions or other reliefs as those now or hereafter at any time granted to other overseas investors in similar capital projects, and in any case that any benefits or advantages which RIVATEX may not now be able to obtain shall be conferred upon it in the event of the event of the same being accorded in the future to any other investment in Kenya.*

7. *ICDC shall obtain from the Government assurances satisfactory to SEDITEX and RIVATEX that such Entry Permits as may be applied for under the Immigration Act will be issued (subject to normal Government security requirements) permitting the entry into and employment in Kenya of such expatriate employees as are required from time to time by the Project in accordance with Appendix VIII and Appendix IX of the Final Proposals.*

8. *SEDITEX shall on or before the Commencement Date procure the subscription and payment in cash in foreign currency by it or its nominees of the remaining balance of the foreign promoters' equity of Kenya Shillings Fifty million one hundred forty-nine thousand five hundred (K.Shs 50,149,500/-) upon the "A" Shares becoming available on increase of capital such payment to be remitted in foreign currency to a first-class Bank in Kenya as agreed upon between the parties but the release of such moneys to RIVATEX shall be conditional upon receipt by SEDITEX and RIVATEX of the guarantee referred to in Clause 9 hereof.*

9. *ICDC shall procure the issue to SEDITEX and RIVATEX as soon as possible and in any event not later than the Commencement Date of a guarantee from a first-class Bank in Kenya acceptable to SEDITEX and RIVATEX securing that immediately and automatically upon receipt of the aforementioned equity subscription of K.Shs 50,149,500/- by SEDITEX or its nominees then ICDC or its nominees shall subscribe and pay in full the corresponding balance of Kenya Shillings Forty nine million six hundred fifty thousand five hundred (K.Shs 49,650,500/-) in respect of the "B" Shares in the increased capital.*

10. *ICDC undertakes in favour of SEDITEX and RIVATEX that pending execution and implementation of the Finance Agreement referred to in Clause II hereof it shall provide bridging finance in accordance with the arrangements referred to in Recital G (b) hereof in respect of the funds ultimately to tbe provided and secured under the said Finance Agreement.*

11. *ICDC shall proceed with all speed upon execution hereof in its capacity as a Syndicate Leader and in co-operation with SIFTDA to conclude a Finance Agreement with RIVATEX for the provision to RIVATEX of all loan and credit facilities (excluding suppliers' credits) required for the Project as summarized in Appendix XX of the Final Proposals.*

APPENDIX 3

ARTICLE - I

APPOINTMENT OF THE MANAGEMENT TO IMPLEMENT THE PROJECT

1.1 The Company hereby appoints the Management to plan, construct, carry out, set up, establish and ensure the completion of the Project on behalf of the Company with all possible speed and to the intent that the Management shall with land, building, plant and equipment acquired or to be acquired in the name of the Company, be responsible for providing, establishing and commissioning for the Company a complete polyester fibre plant, and the Management accepts such appointment and the full responsibilities for it as well as the satisfactory execution of all matters relative to such undertaking:

1.2 Without derogating from the general provision of 1.1 above or from any other obligations imposed (expressly or by implication) on the Management by this Agreement or by law or commercial custom the Management shall in the discharge of its duties under 1.1 accept full responsibility for:

1.2.1 Engaging a well known consultancy firm and preparing a market survey report of the local as well as world markets for the fibre to be manufactured by the Company based on the estimate of the demand by standard methods for various end uses;

1.2.2 Carrying out the feasibility study of establishing a plant in Kenya, estimating the profitability of the Project, estimating the funds required for the Project etc. and preparing the report on the same;

1.2.3 Negotiating and concluding an agreement for equity capital participation in the Company from various international agencies, national agencies, private banks and other private parties to meet the equity capital requirements of the Company;

1.2.4 Negotiating with various well known international companies to obtain the requisite know-how for the Project, advising on the selection of the supplier of know-how and obtaining the know-how at terms agreeable to the Company;

1.2.5 Negotiating with various well known international companies to obtain the requisite basic engineering for the Project, advising on the selection of the supplier of basic engineering and obtaining the basic engineering at terms agreeable to the Company;

1.2.6 Obtaining detailed engineering for the Project, and based on the know-how and basic engineering so obtained, calling for bids and selecting detailed engineering contractor at terms acceptable to the Company;

1.2.7 Using its best endeavours to procure the grant to the Company of all authorisations of various Governments and Government Agencies wherever required for the carrying out, completion and operation of the Project;

1.2.8 Planning, and equipping the Project in accordance with the type and capacity of production stipulated in the Joint Venture Agreement and in the Engineering & Technical Services Agreement attached thereto as Annexure II and in accordance

with the terms and conditions contained in said Agreements, and in each of them it being agreed that Management shall be entitled to agree to and approve, on behalf of the Company, any change or modification of the terms contained in such Engineering & Technical Services Agreement which does not materially affect the rights or obligations of the parties thereto and the preparation and implementation of all proposals, projections, specifications, bill of quantities and engineering and other documents required to enable the Project to be carried out and completed with all possible speed, using its best endeavours to achieve economy and avoid wherever possible over-runs in the total cost of the project;

1.2.9 Engaging legal counsel to prepare various material documents such as the Joint Venture Agreement, Know-how Agreement, etc.

1.2.10 Carrying out negotiations and obtaining the required long, medium and short term finances for capital expenditure such as buildings, equipment, etc., as well as working capital requirements from various international and national fiancial and development agencies;

1.2.11 Carrying out all the formalities required under the Laws of Kenya for the issue of the equity capital and managing the issue and subscription of the equity capital of the Company including underwriting arrangements, if any, to be made;

1.2.12 Preparing and submitting to various financial as well as regulating agencies all requisite financial statements, projections, capital budgets, estimates long term profitability statements, cash flow statements, pay back

period statements, repayment schedules, etc., as and when required by them;

1.2.13 Preparing specifications, obtaining quotations and/or tenders for the purchase of various machineries and equipments and coordinating purchases, inspection and testing of equipment;

1.2.14 Making proposals and recommendations to the Company for the most suitable site for the erection of the Project in relation to transport facilities, availability and costs of water, fuel, power, labour, waste disposal facilities and other technical requirements;

1.2.15 Inviting tenders and selecting architects and building contractors for designing and constructing the buildings and utilities for the Project, and negotiating the terms of contracts with such architects and contractors including or excluding the materials to be used;

1.2.16 Arranging for the proper carriage, clearance, reception, transportation, storage and erection of all plant, machinery, equipment and materials required for the purpose of the Project;

1.2.17 Supervising the construction of buildings and erection of machinery and equipment and planning and synchronising work of erectors appointed by all suppliers;

1.2.18 Ensuring that the Project is adequately insured during the period from the starting date to the date of completion as deemed proper by Management;

1.2.19 Dealing on behalf of the Company with all suppliers, contractors and erectors, checking and approving invoices and making all necessary payments;

1.2.20 Negotiating with the suppliers and obtaining from them credit for the payment, negotiating and obtaining deferred term credits from various agencies for the purchase of necessary equipment for the Project;

1.2.21 Ensuring that the effluent from the Project is discharged in such a manner that it can be processed satisfactorily and in accordance with the local and Central Government's requirements, and standards required by the Project;

1.2.22 Establishing all requisite proper safety regulations, procedures and controls;

1.2.23 Supervising the starting up and commissioning of the plant, and preparing a complete plan for the starting of the Project including the purchases of all raw materials and other items necessary for the efficient starting of the Project as well as such test runs as the Management may think proper and necessary for effecting the commissioning of the Project;

1.2.24 Making satisfactory arrangements to ensure the availability promptly at a reasonable cost of all spare parts that the Company may from time to time require for its plant and equipment;

1.2.25 Selecting and recruiting the personnel required for erecting the plant and equipment as well as for the subsequent test runs;

1.2.26 Selecting and recruiting the personnel required for technical and administrative functions of the Company;

1.2.27 Installation and operation of a proper system of financial control and keeping of proper books of accounts and records in connection with carrying out and completion of the Project;

1.2.28 Preparation, revision and updating the system, as necessary, of the detailed estimates and forecasts of the costs of carrying out and completing the Project and the time required therefore and the prompt delivery to the Company of such estimates and forecasts (including all revised and updated estimates and forecasts);

1.2.29 Providing or causing to be provided, all requisite civil, mechanical, electrical, engineering and consulting services including but not limited to site plan and the coordination of the construction of the buildings and shipments, delivery, erection and installation of plant, machinery and equipment as well as for all other above mentioned services;

1.2.30 Ensuring that the cost of erecting and setting up the Project exclusive of know-how and engineering fees, taxes and working capital up to the commissioning date shall not exceed the estimate jointly agreed by Management and the Company;

1.2.31 Completion of all the transactions, operations and services from the date of beginning of construction up to the date of completion within the time limit mutually agreed;

1.2.32 Minimising the effects of the currency fluctuations on the cost of the Project to the extent possible.

ARTICLE - II

APPOINTMENT OF THE MANAGEMENT AS GENERAL MANAGERS OF THE COMPANY

2.1 The Company hereby appoints the Management as its sole and exclusive General Manager in connection with all aspects of the business of the Company for a term commencing as of the date hereof and terminating 10 years after the Project Completion Date as defined in Section 6.02 of the Joint Venture Agreement, and the Management accepts such appointment. Such appointment shall be deemed to be renewed for a further period of five (5) years unless either party shall, within 12 months prior to the end of the first term, give written notice to the other of its intention to terminate the Agreement at the end of said 10 year term. Thereafter, the said appointment shall continue from year to year until terminated by either party by not less than twelve months' previous notice in writing to the other. No person or company other than the Management shall be appointed Co-Managing Director, Co-Managing Agent or Co-General Manager of the Company during the term hereof as extended from time to time.

2.2 Within the framework of the general overall policy and consistent with the directions and instructions which may from time to time be given and subject to the control and supervision of the Board of Directors of the Company, the Management shall be entirely responsible for and shall have full powers relative to the implementation of the Project as described in Article I, the management and operation of the Company, and shall direct all the business and transactions of the Company.

2.3 The Management shall of its own volition as part of its duties under this Article make available to the Company without any specific request from the Company all information known to it which may be useful to the Company in connection with the production and sale of polyester fibre chips and dyed and raw-white polyester texturized filament and provide a full range of services in connection with all aspects of the Company's business, and without derogating from the foregoing or from the general provisions of 2.1 and 2.2 above or from any other obligations imposed (expressly or by implication) on the Management or by Commercial Custom duties, responsibilities and powers of the Management under this Article shall be responsible for:

2.3.1 The preparation and implementation of all planning, management, organization and the financial, technical and administrative control of the Company's business;

2.3.2 The preparation and establishment of production schedules, process, quality and cost control systems, buildings and plant maintenance programmes and all other requisite schedules, systems and programmes;

2.3.3 Recruiting and maintaining at all times the managerial, technical, marketing and administrative staff and the work force required by the Company for the purposes of carrying out the Project and the proper and efficient conduct of its business (including arrangements providing for the allocation of management responsibility for all aspects of the business), organisation charts, staff schedules, job contents, job manuals, instruction schedules, and training programmes for all employees of the Company;

2.3.4 Instituting and arranging for the carrying out in the Company's plant in Kenya or elsewhere of all necessary training programmes and courses for the Company's work force and its executive and administrative staff so as to achieve Kenyanisation of all personnel within 7 years of the successful commissioning of the plant;

2.3.5 Establishing proper and efficient financial control and record system and procedures;

2.3.6 Supplying to the Company full information regarding the main sources of supply, the general levels of prices and the estimated delivery periods from time to time prevailing for any goods that may be required by the Company for the purpose of its business and establishing departments, programmes and arrangements for the direct and prompt acquisition by the Company of raw materials and spare parts at best possible prices and conditions;

2.3.7 Arranging for and carrying through the purchase of raw materials, goods, property and other assets and all plant, machinery, store materials and other things required by the Company;

2.3.8 Negotiating, carrying out and effecting all Kenyan and foreign sales of all production of the Company;

2.3.9 Dispatching, shipping or distributing all production of the Company and effectively insuring the same against such risk of loss or damage thereto as it is by commercial practice usual to insure against;

2.3.10 Ensuring efficient conduct of the Company's business and attending to all engineering and technical aspects of the operations and maintenance of the Company's plant;

2.3.11 Keeping the Company fully informed of all developments and improvements in engineering, production, quality and cost control and maintenance techniques and methods known to the Management which may be of benefit to the Company in the conduct of its business;

2.3.12 Ensuring the maintenance of proper safety regulations, procedures and controls;

2.3.13 Arranging for adequate insurance policy or policies regarding covering all risks which the Company ought to insure against, from the date of starting of the Project and negotiating and obtaining the best bid and most secure terms for such policy or policies as the Management deems fit;

2.3.14 Arranging for the sale, disposal, shipment storage and warehousing of the Company's production, goods, property and assets;

2.3.15 Disclosing or causing to be disclosed to the Board all information matters and documents relating to or having an influence on the property, busines or affairs of the Company which may come to the knowledge of the Management;

2.3.16 Rendering from time to time to the Board as it may require an account or statement of expenditure together with all reasonable details of the disbursements chargeable by the Management against the Company and such information as may be necessary to explain the same or as the Board or the Auditors of the Company shall from time to time reasonably require;

2.3.17 Arranging whenever necessary for a person or persons, being suitably qualified and experienced, to visit the Company's plant to advise on any aspect of the Company's business;

2.3.18 The preparation and conclusion of all contracts and agreements relative to all aspects of the Company's normal business;

2.3.19 Arranging for the preparation of all necessary schemes and plans for the development and operation of the plant of the Company and in connection therewith obtaining all necessary or required specification, drawings and costings;

2.3.20 Negotiating with and obtaining from various agencies further finance as may be required from time to time for working capital as well as fixed assets either for the replacement, balancing or expansion programmes of the Company;

2.3.21 Using its best endeavours to promote the exports of the products of the Company in the world markets;

2.3.22 Using its best endeavours to further increase the import substitution of various items that may be required by the Company;

2.3.23 Carrying out continuous profit improvement programmes from time to time within the framework of the overall policy of the Company;

2.3.24 Promoting, carrying out and reaping the benefits of indigenous research and development programmes in connection with Company's business;

2.3.25 Preparing and carrying out the maintenance and replacement programmes for the various equipment and property of the Company;

2.3.26 Investigating and protecting the use of patents with regard to the Company's products in Kenya;

2.3.27 Using its best endeavours to improve the productivity in the plant of the Company;

2.3.28 Generally carrying out and performing all duties necessary to the efficient conduct of management and control of the Company's business in Kenya;

2.3.29 Implementing any other measures as deemed necessary and useful by the Management including changes in production programmes, modification of selling prices of the Company's products as well as varying the number of personnel, their jobs and salaries.

2.4 The Management may convene Board Meetings of the Company from time to time as may be deemed necessary and in accordance with the Laws of Kenya. The Management shall ensure that the Company submits monthly to the Board of Directors of the Company progress reports and operating results up to the end of the month and for the month, prepares prior to the commencement of each financial year a budget showing the projected capital expenditures together with profit and loss statement and cash flow and prepares annually, prior to the Annual General Meeting of shareholders, a review of the operations of the Company during the preceding year and a statement of recommendations for further improvements in operations.