KENYA

TRADE SUMMARY

In 2001, the U.S. goods trade surplus with Kenya was $449 million, an increase of $321 million from 2000. U.S. exports to Kenya were $577 million, a $340 million increase from 2000. Kenya was the United States' 62nd largest export market in 2001. U.S. imports from Kenya were $129 million, an increase of $19 million from 2000. The stock of U.S. direct investment in Kenya was $136 million in 2000, an increase of 3.9 percent from 1999.

OVERVIEW

In 2001 Kenya's GDP growth rate was approximately one percent – an improvement over the negative 0.3 percent growth rate in 2000. However, Kenya continues to experience reduced foreign investment as a result of corruption, poor infrastructure, high power costs and other factors. The return of the International Financial Institutions (IFIs) in mid-2000 was expected to improve investor confidence, but the Government of Kenya (GOK) has failed to met IFI conditionalities, and investment outflows have continued. The December 2000 Supreme Court decision disbanding the Kenya Anti-Corruption Authority (KACA), together with Parliamentary setbacks on economic governance legislation, harmed GOK reform efforts. To replace the KACA, the GOK formed an Anti-Corruption Unit under the Police Department to handle corruption cases in August 2001.

Despite the downturn in investment, Kenya has continued to play an increasingly important role in the region. Kenya is a member of the re-established East African Community (EAC) and remains an active member of the Intergovernmental Authority on Development (IGAD), the Common Market for Eastern and Southern Africa (COMESA), and the World Trade Organization (WTO). Although initially slow to honor its WTO commitments, Kenya has now implemented the WTO Customs Valuation Agreement and the Financial Services Agreement, and has passed legislation designed to implement the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS).

IMPORT POLICIES

The GOK continues to liberalize trade and restructure many of its important sectors. Kenya continues to rely on tariffs as the primary instrument of trade policy. The GOK usually announces changes in its annual budget speech. In June 2001, the GOK declared import duties on all primary raw material imports would be waived to allow local manufacturers to compete with imports of finished goods from the 20 COMESA Free Trade Area countries. Other raw material and capital goods tariffs were reduced from 5 percent to 3 percent. The government also imposed a 35 percent duty on imported fabrics (up from 25 percent to 30 percent) in order to protect the local textile industry. The tariff on fiber used in textile factories is zero while the duty on yarn is 20 percent.

The budget also imposed a 35 percent duty on imported foodstuffs that compete directly with goods produced in Kenya. These include meat and meat products, dairy products, poultry and poultry products. The GOK continues to carefully control imports of seed corn by subjecting hybrid varieties to a certification process that effectively restricts trade. Until a seed variety is fully registered (a process that can take 3-4 years), the Ministry of Agriculture and Rural Development restricts cereal seed imports by setting quantitative ceilings. However, once a variety is certified, the quantitative restrictions are lifted. Firms operating in Export-Processing Zones (EPZs) are able to purchase tariff-free fuel.

Customs Procedures

Under the WTO Customs Valuation Agreement, implemented in early 2000, Kenya must use the transaction value in valuing goods imported from other WTO signatories. Kenya continues to maintain its pre-shipment inspection (PSI) regime. COTECNA Inspection, S.A., and Intertek Testing Services International provide PSI services under a two-year contract, which is expected to end in February 2003. The companies' mandates include ensuring that up-to-date customs valuation and risk assessment methods are applied.

STANDARDS, TESTING, LABELING AND CERTIFICATION

The Kenya Bureau of Standards (KBS), a regulatory body under the Ministry of Trade and Industry, inspects imports to ensure conformity with International Standardization Organization (ISO) and other products standards. The body also conducts product testing and certification for individual product categories. Goods that do not meet KBS standards are withdrawn from the market and the importer is prosecuted. KBS has regular meetings with local manufacturers to address problems arising from the importation of illegal, counterfeit, and substandard goods.

Certain imported agricultural goods are subject to further inspection by the Kenya Plant Health Inspectorate Service (KEPHIS). KEPHIS regulates the importation and exportation of plant materials and trade in bio-safety control organisms (organisms that require special handling to ensure they are not accidentally released into the environment) in accordance with the International Plant Protection Convention (IPPC). KEPHIS also evaluates commercial hybrid grain seeds for a period of three years before the seeds can be released in the market. This certification process is sometimes tedious and restrictive, and the three-year period needed for the government to approve or reject a variety can be burdensome.

GOVERNMENT PROCUREMENT

According to government regulations, goods worth more than Ksh. 10,000 (about $127) and less than Ksh. 200,000 (about $2,548) must have three competitive quotations and be adjudicated by three responsible officers. Goods and services valued at over Ksh. 200,000 and less than Ksh. 5,000,000 (about $63,694) must be purchased through an open tender process adjudicated by the Ministerial Tender Board (MTB). The Central Tender Board (CTB) must also approve goods and services worth in excess of Ksh. 5,000,000, in addition to the requirement of going through the MTB. GOK reform measures over the last two years have resulted in wider publicity to government tenders, established an appeals committee, and appointed people from the private sector to the CTB, the main decision-making agency for large-scale government purchases.

The GOK has increased transparency in bidding by removing from its tenders the clause that reads, "the government reserves the right to accept or reject any bid and is not obliged to give any reasons for its decisions." With the removal of the clause, CTB now publishes its decisions and, if the bidder asks, provides reasons for rejecting certain bids. However, tenders are still frequently awarded to noncompetitive firms in which government officials have a significant interest, and conflict-of-interest regulations are rarely enforced. Kenya is not a signatory to the WTO Agreement on Government Procurement.

EXPORT SUBSIDIES

Firms in Export-Processing Zones (EPZs) are allowed to purchase imported inputs tax-free. The firms are allowed to sell up to 20 percent of their output on the domestic market. However, Ministry of Trade and Industry officials state that these products are usually of

second quality. In order to discourage the practice, EPZ firms are liable for all taxes plus a 2.5 percent penalty on goods sold locally. There is no general system of preferential financing although sectoral government development agencies in areas such as tourism and tea are supposed to provide funds at below-market rates to promote investment and exports by Kenyans.

INTELLECTUAL PROPERTY RIGHTS (IPR) PROTECTION

Kenya is a member of, or signatory to, most major international and regional intellectual property conventions, including the World Intellectual Property Organization (WIPO), the African Regional Industrial Property Organization, the Paris Convention on the Protection of Industrial Property, and the Berne Convention on the Protection of Literary and Artistic Works. Although a unified system for the registration of trademarks and patents for Anglophone Africa was signed in 1976, the effort has remained dormant due to the lack of cooperative procedures among the signatory states. A future prospect for patent, trademark and copyright protection is embodied in the African Intellectual Property Organization, although its enforcement and cooperation procedures are as yet untested.

To comply with its WTO obligations, the Kenyan Parliament passed an amended version of the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) in August 2001 as part of the Kenya Industrial Property Act (KIPA). The KIPA became law after President Moi’s assent. However, it is still unpublished in final form and, therefore, has not been implemented. In the meantime, November 2001 estimates indicate that the Kenyan manufacturing sector lost over Ksh. 20 billion (over $254 million) in direct sales and the Treasury over Ksh. 1.3 billion (over $16.5 million) in taxes last year due to the sale of counterfeit goods. The Kenya Association of Manufacturers (KAM) has called on the GOK to raise fines imposed against counterfeiters from the current Ksh. 20,000 shillings ($255) to Ksh. 500,000 ($6,370) and to introduce stiffer jail penalties and the right to seize and destroy counterfeit goods.

Patents, trademarks and trade secrets are the responsibility of the Kenya Industrial Property Office (KIPO) under the Ministry of Trade and Industry. Copyright protection is the responsibility of the Attorney General's office. A new Copyright Bill superceding the previous Copyright Act was passed into law in November 2001. Computer programs, literary, musical, artistic and audiovisual works, sound recordings, and broadcasts are protected under the bill. The bill created the Kenya Copyright Board, which has the authority to inspect, seize and detain suspect articles and to prosecute offenses. New criminal penalties include fines up to Ksh. 800,000 ($10,192) and a maximum of 10 years in jail, or both, up from previous levels of Ksh. 200,000 (about $2,548) and 5 years. Historically, however, penalties for copyright infringement have been low and enforcement and the understanding of the importance of intellectual property are poor. There is widespread sale of pirated music and videotapes produced in neighboring countries on the Kenyan market.

SERVICES BARRIERS

In general, service providers are accorded the same treatment, whether local or foreign. However, foreign firms in the construction, engineering, and architecture trades may face discrimination on tenders for public projects. An exchange authorization is required from the Ministry of Finance, and there is a high level of government discretion. In addition, new foreign investors with expatriate staff are required to submit plans for the gradual elimination of non-Kenyan employees. The Kenyan bar admits foreign lawyers for a maximum duration of 12

years. Medical personnel (doctors) must serve a one-year "induction" in public hospitals and sit for exams before they are considered for registration in the country.

The privatizations of note since 1995 are the sale of state-owned tourist facilities, the flotation of shares of state-owned financial institutions on the Nairobi Stock Exchange, and the divesting of government shares in Mumias Sugar Company. The government is reviewing the bids from six companies for the Kenya Reinsurance Corporation. However, since February 2001 no actions have been taken towards the sale of the 35 percent government stake in Kenya Commercial Bank (KCB).

The government continues to liberalize the telecommunications sector. After dissolving the Kenya Posts and Telecommunications Corporation (KPTC) when the Kenya Communications Act of 1998 became effective in July 1999, three separate entities were formed: Telkom Kenya (telecommunications); the Communications Commission of Kenya (CCK), the regulatory body; and the Postal Corporation of Kenya (postal services). Telkom Kenya is permitted to maintain its monopoly in segments of the telecommunications market for five years (1999 - 2004). The CCK licensed two firms, Safaricom (a joint venture of Telkom and Vodafone) and Kencell (a joint venture of Vivendi and Sameer Investments), to provide mobile cellular telecommunications. As of December 2001, these two companies had over 540,000 subscribers combined, almost double the 320,000 landlines provided by Telkom. In August 2001, the government announced that three Kenyan firms had succeeded in acquiring the rights to operate eight regional licenses in competition with Telkom Kenya. Telair Communications acquired five of the eight licenses for a reported $23 million. Safitel acquired two regional licenses for $9 million and Bell-Western acquired the remaining regional license for $25,000. However, these regional entities have yet to begin operations. And after more than one year of negotiations to sell the 49 percent GOK stake in Telkom Kenya, the government cancelled the sale in late 2001. Failure by the GOK to privatize Telkom Kenya has cast doubts on the willingness of the government to privatize other parastatals such as the Kenya Ports Authority and Kenya Railways Corporation.

INVESTMENT BARRIERS

Tight fiscal policies have brought inflation under control. The financial system has been restructured and measures taken to increase the role of the private sector and establish greater accountability and transparency with respect to financial infractions. A managed floating exchange rate regime has been adopted and companies may now retain foreign exchange earnings and repatriate capital and profits without certification. The government has identified more than 200 parastatals for privatization and another 33 for restructuring. The 2001 Donde Banking Bill proposed caps on lending rates and minimum rates of return on deposits, which may have decreased the number of loans available to the private sector and higher risk ventures. However, in January 2002 parts of the bill were declared unconstitutional and it is unclear whether similar legislation will be passed in 2002.

The GOK has placed a number of restrictions on foreign ownership for publicly traded companies – particularly in the areas of financial services and telecommunications. Foreign ownership of firms listed on the Nairobi Stock Exchange (NSE) cannot exceed 40 percent for corporations and 5 percent for individuals. Where foreign ownership in a company exceeds 40 percent at the time of listing on the NSE, the foreign owner is allowed to maintain (or reduce) but not to increase that

share. Foreign brokerage companies and fund management firms must be locally registered companies, in which case fund management firms must be at least 30 percent Kenyan-owned and brokerage firms 51 percent Kenyan-owned.

Internet Service Providers (ISPs) operate in the main towns, but have to rely on Telkom Kenya for bulk Internet services. For telecommunications companies, foreign ownership of an ISP is restricted to 40 percent. Although there are about 90 licensed ISPs, the Communications Commission of Kenya (CCK) restricts the number of ISPs and prohibits them and other carriers from establishing switches, international gateways, or direct satellite links. This has forced continued dependency on Telkom Kenya and inhibited competition and improvements in customer service. The CCK specifically prohibits ISPs from providing the following services: voice telephony, uploading of telecommunications traffic by satellite, and the use of wireless communications. In fact, ISPs must agree, in writing, not to provide Internet protocol telephony through their networks (paging services are excluded from this requirement). ISPs must also provide the CCK with information on what they charge for all services, as well as the names and addresses of their clients. CCK must also type-approve equipment that ISPs provide to clients. These regulatory practices make investing in this area considerably less attractive than it might otherwise be. The CCK regulates telecommunications and radio communications in the country as well as postal services.

The Kenyan legal system protects and facilitates acquisition and disposition of all property rights – including for land, buildings and mortgages. However, the process of securing the title deed is cumbersome and not transparent, and this is one of the most serious impediments to new investment. The fact that many of the 99-year government leases covering much of Kenya's urban land are expiring is another extenuating factor, since original lessees are choosing not to sublet, but rather to "sell" the leases as the expiration dates approach to avoid potential future complications. The courts are a factor as well because they have generally been unwilling to permit mortgage holders to sell off land to collect unpaid mortgage debt.

Technology transfer requirements and foreign exchange controls have been abolished. Local partners are encouraged but not required. Kenyan partners are no longer required for small-scale commercial enterprises.

Infrastructure

The GOK has been hesitant to open public infrastructure to competition because the state-owned companies that control infrastructure are considered "strategic" enterprises. For this reason, the reform and partial privatization of telecommunications, power, and rail has fallen behind schedule.

In the late 1990s, the GOK split Kenya Power and Lighting Company (KPLC) into three entities: a power generator (KenGen), a distributor (KPLC), and a regulator, the Electricity Regulatory Board (ERB) to regulate retail tariffs and approve power purchase contracts between KPLC and producers. The government also licensed two Independent Power Producers (IPPS) to sell electricity to the grid. Although KenGen appears to be a model of technical expertise and energy generation, non-payment of bills/accounts by the GOK and KPLC have adversely affected operations of all entities, particularly KPLC. In late 2001 the ERB commissioned a study to review electricity tariff policy. The draft report presented in January 2002 recommended an upward adjustment to electricity tariffs to make the struggling KPLC profitable. If the proposed increase in the electricity tariff is implemented, it will further dampen the investment environment in Kenya due to the already

expensive price of power compared to its regional competitors.

The Kenya Railways Corporation has contracted the maintenance of some of its locomotives to General Electric. The corporation has restructured its operations and recruited senior management from the private sector in the hope of turning the loss making company into a profitable entity. However, the company is yet to be privatized as intended.