KENYA ASSOCIATION OF MANUFACTURERS
Driving Global Competitiveness

60+ Years OF ADDING VALUE

MANUFACTURING MANIFESTO 2022-2027

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Abbreviations

BRICS	Brazil, Russia, India, China, and South Africa
CoG	Council of Governors
CIDPS	County Integrated Development Plans
CIP	Competitiveness Industrial Performance
CPI	Consumer Price Index
DPC	Document Processing Centre
EBITDA	Earnings Before Interest, Taxes, Depreciation and Amortization
FDI	Foreign Direct Investment
GDP	Growth Domestic Product
ICD(N)	Inland Container Depot (Nairobi)
IEA	Institute of Economic Affairs
JKIA	Jomo Kenyatta International Airport
KAM	Kenya Association of Manufacturers
KEPROBA	Kenya Export Promotion and Branding Agency
KNBS	Kenya National Bureau of Statistics
KRA	Kenya Revenue Authority
LAC	Latin America and the Caribbean
LEADS	Logistics Ease Across Different States
NEDPS	The National Export Development and Promotion Strategy
OECD	Organisation for Economic Co-operation and Development
SGR	Standard Gauge Railway
STEM	Science, Technology, Engineering, Maths
UNIDO	United Nations Industrial Development Organization
VAT	Value Added Tax

Foreword

Kenya Association of Manufacturers (KAM) is one of Kenya's leading Business Member Organizations (BMOs) with a sharp focus on articulating issues affecting the manufacturing sector.

Securing the future of industry is at the heart of our advocacy. This is why KAM continues to engage partners and stakeholders on the broader national goal and ambitions of Vision 2030 - to become a middle-income country with a manufacturing sector that contributes over 15% to GDP. It is in this spirit that the Association actively participates in policymaking, and during the election period, engages political parties and actors.

Majority of KAM Members run Kenyan owned businesses and come to this conversation with a sense of patriotism and a long-term interest in the future and prosperity of our nation. As manufacturers, we have a unique view of the issues borne out of years of experience in the market and engagement with stakeholders. Our insights add positively to the conversation based on real and measurable contribution to the economy, made in the last 60 years, as evidence of our capability, commitment, and tenacity.

Although Kenya has made strides in manufacturing output, other economic sectors have grown faster than manufacturing, in the last one and half decade. This has seen manufacturing sector contribution to GDP shrink over the years - currently, contribution to GDP stands at 7.6%. In addition, the sector faces real challenges in the wake of COVID-19 pandemic, globalization and digitization. This calls for the country to be resolute in branding and positioning herself on the global map, as a serious industrial centre that drives the competitiveness of value-add goods.

Manufacturing is known world over for generating sustainable, well remunerating decent jobs, improving foreign exchange income, and driving the country's overall wealth and well-being. The Industrial Revolution, two centuries ago, and the East Asian Miracle of the last three decades have demonstrated the ability of manufacturing to grow incomes, reduce poverty and change the trajectory of nations.

The Association, through this Manifesto, aims at contributing to the national conversation on the economic choices that will face any incoming government and proposes solutions that will benefit the sector and the nation at large.

KAM remains committed to working with all other stakeholders in developing sound public policies and frameworks to boost industrial growth. We will continue to provide thought leadership and strategic advocacy to support our country's ambition of transformation into a regional industrial hub.

Mucai Kunyiha
KAM Board Chairperson

Executive Summary

Kenya's Constitution (2010) lays out a calendar for the conduct of elections at all levels of government. This provides ample opportunity for KAM to reflect on the policy priorities and present an "Agenda for Manufacturing".

The Manifesto presents the Association's policy proposals, to enable the new administration at all levels of leadership, to ensure Kenya's economic and social goals are attained. It is divided into three sections:

- The background, containing the national development and policy context in Kenya. We have identified five key issues that summarize the state of the national economy. These include falling share of manufacturing as a share of the total economic output (GDP), debt-driven economic growth, high spending on infrastructure without commensurate contribution to growth and revenues, elevated levels of fiscal distress and undeniable rise in cost of living.
- The second section isolates the priority issues which the new administration must address to restore growth, enable private sector vitality and create balance in Kenya's fiscal affairs. Among these proposed priority issues are creating jobs in manufacturing, expanding exports, reducing the regulatory burden on businesses, robust investment in the provision of public goods and creation and implementation of a coherent taxation policy.
- The final section captures the solutions matrix, that highlights the specific policy and administrative priority areas that would enhance the realization of our socio-economic goals, upon implementation.

The Manifesto shall guide our engagements with aspiring political leaders, with a focus on economic policy challenges and the need to create a competitive manufacturing sector in Kenya.

Phyllis Wakiaga
KAM Chief Executive

Acknowledgment

The development of the Manufacturing Manifesto, 2022-2027, has been made possible through the participation of KAM Board led by the Chairman, Mucai Kunyiha, KAM Chief Executive - Phyllis Wakiaga and the lead consultant and Institute of Economic Affairs (IEA) Chief Executive – Kwame Owino. Our gratitude goes to them for providing continued strategic guidance on the Manifesto.

Oversight of the development of the content for the Manifesto was provided by KAM Head of Policy Research & Advocacy - Job Wanjohi and KAM Research & Fiscal Policy Manager - Dr. Simon Githuku. Further assistance was provided by Legal & Regulatory, Sectors, Trade & Policy and Chapter teams.

SectionONE>>

State of Play

1.| Background

Kenya has demonstrated weak and uneven signs of recovery, with the country recording poor economic performance in 2020 and 2021. This is attributed to various factors, key among them being the low expansion of employment in the formal sector despite Kenya having one of the highest growth rates in the continent.

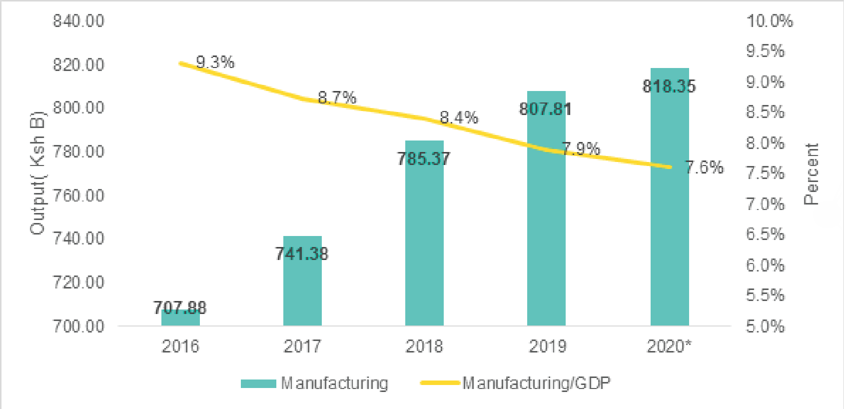
While growth has been moderately strong in the last five years, the overall employment picture has shifted more strongly towards informal sector employment. The first implication of this is that Kenya's growth pattern is neither solving nor meeting the demand for formal and decent employment.

(a) Falling GDP share of manufacturing sector

Government spending has played a dominant role in accounting for growth in the last 8 years. This fiscal policy and growth model affected corresponding shares of various sectors of the economy. In particular, the composition of GDP changed through the expansion in agriculture output in comparison to the manufacturing and services sectors.

The share of agriculture in the GDP grew while that of manufacturing has seen a proportionate reduction from 9.3% in 2016 to 7.6% in 2020. While government's spending plans are in line with the Medium-Term Plan III (MTP III) that guided the pursuit of the Vision 2030, the effect of execution is not causing sectoral changes in the desired direction. It would be expected that changes geared towards expanding agro-processing would be consistent with growth in the share of manufacturing in the overall economy.

Chart 1: Performance of the manufacturing sector (2016-2020)



Source: Kenya National Bureau of Statistics (KNBS) Economic Survey 2021

(b) Spending on infrastructure

Investments in infrastructure funded by the Government through public debt have not yielded a positive impact on either cost base or the efficiency of manufacturing enterprises. Judged by the share of manufactured goods in Kenya's export basket, the overall competitiveness of manufacturing firms did not change.

Tied to the large fiscal deficit is the trade deficit, with exports comprising only one third of all forms of trade. The widening of the trade and fiscal deficits is commonly referred to as Kenya's "twin deficits". The fiscal deficit is the direct result of an agreement by the Legislature and the Executive branches of government to expand public spending. On the other hand, the trade deficit is the result of domestic demand for imports without a corresponding growth in external demand for goods manufactured in Kenya.

Since 2014, the Government of Kenya prioritised large infrastructure investments that included the two completed phases of the SGR, the Last Mile Power Project, construction of 3 berths at the Lamu Port, refurbishment of the Kenya oil pipeline and more than 5000 kilometers of roads of different surface qualities. By the end of 2022, it is expected that the public infrastructure will include the Nairobi Expressway, a 28-kilometer highway connecting Jomo Kenyatta International Airport (JKIA) to Westlands in Nairobi. There is no shortage of examples of the enormous expenditure that the government has dedicated to investments in infrastructure. A summation of the investments shows that the declared cost of investments exceeds a nominal value of KSh. 700 billion[1].

Chart 2: Infrastructure investments

	2016/17	2017/18	2018/19	2019/20	2020/21
Energy, Infrastructure & ICT (Kshs Billion)	529.16	426.96	418.8	480.87	335.81

Source: Budget Policy Statement (various issues)

In each of the years in which these enormous infrastructure investments were being conducted, the overall budget deficit stayed above 5.5% of the GDP. This shows that construction was funded primarily using public debt. In the same period, the cumulative public debt as a share of annual output rose from below 50% in 2014 to 68.1% by June 2021[2]. While the declaration of the share of debt to GDP is made by the

National Treasury, it is most likely an understated value because the contingent liabilities of the public sector are not comprehensively reported on. Additionally, there is a substantial backlog of payments for services rendered by private firms to departments and state corporations for which payments are long overdue.

(c) Economic growth and growing deficits

Kenya's growth trajectory had been positive for 10 years before interruption by the COVID-19 pandemic. However, this impressive growth did not translate to formal sector growth, attributed to the rise in fiscal deficits financed through debt.

Public data shows that overall economic productivity has been falling despite GDP growth rates. Public sector investments in infrastructure projects have been significant, even allowing for fiscal leakages and admittedly, high levels of corruption. Public sector spending was the major force behind economic growth recorded in the last five years in Kenya, which was brought to a stop by the pandemic in 2020.

Chart 3: Trends in public debt stock

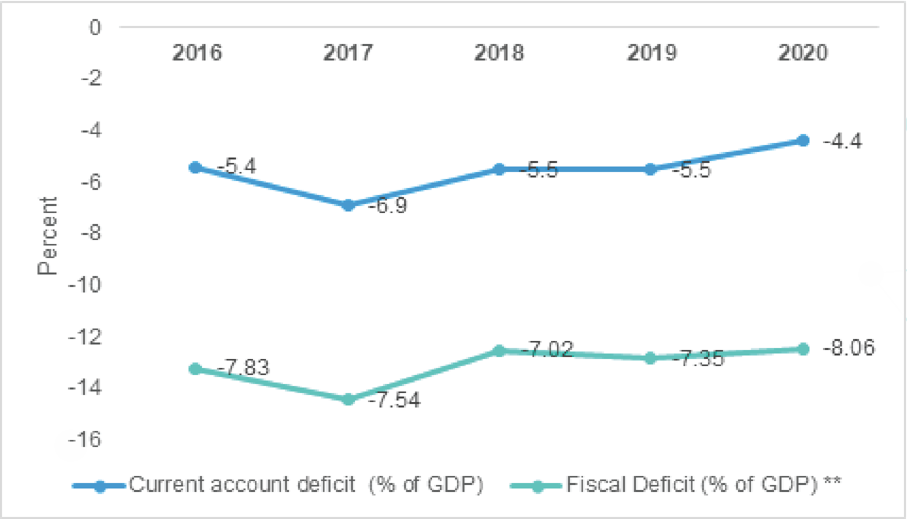
Source: PBO Budget Options for 2021/2022 and the Medium Term

(d) Fiscal distress

Public spending in Kenya has grown at a higher rate than public revenues, with the cumulative fiscal deficit creating debt distress.

Kenya's recent growth pattern is characterized by positive change in the GDP, without corresponding tax revenues. While Kenya Revenue Authority (KRA) has continued to raise its collections, the tax take as a share of the GDP has been falling, owing to the rebasing of the GDP measurement and inadequate expansion in formal employment.

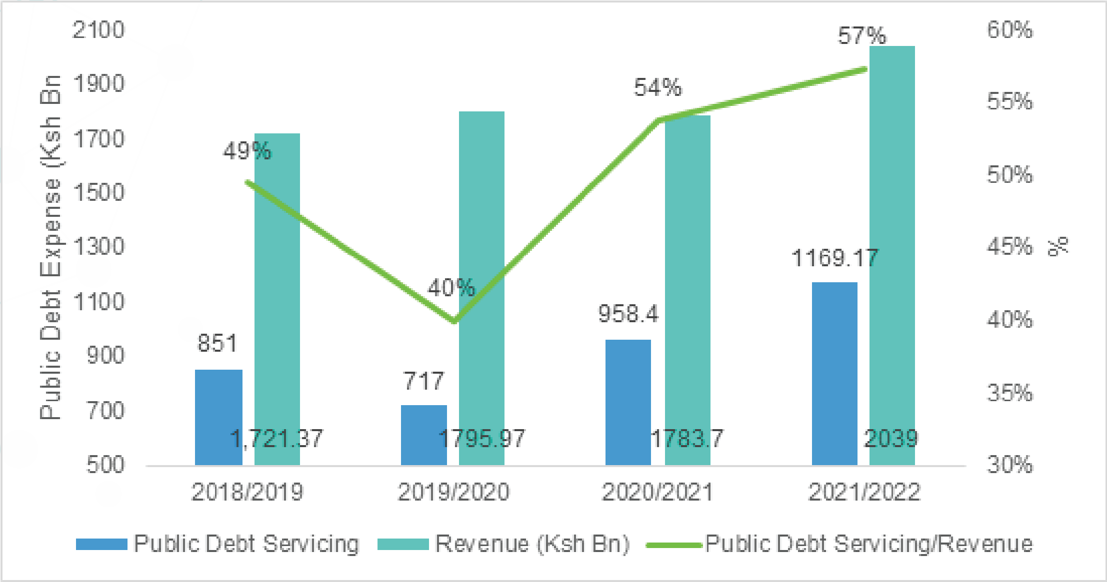
Chart 4: Twin deficits



Source: KNBS Economic Survey (Various issues) ** Fiscal Year

While the direction of cumulative debt has recently shifted towards a longer tenure, the overall debt burden has increased with a substantial shortening of the tenure. The immediate fiscal effect of this confluence of large deficits and short tenure is that the public sector faces the pressure of making prompt payments in addition to paying for regular services. As a result, the proportion of public revenues being dedicated to debt servicing has reduced discretionary public sector spending. Here, the fraction of revenues dedicated to debt servicing has moved by 18 percentage points from 40% to 58% as at the end of 2020. Estimates of revenue that were approved in the financial year that started in July 2021, the share of revenues required to service the public debt commitments and other consolidated fund commitments for the year stands at 65%.

Chart 5: Fiscal distress (Ksh Billion)



Source: National Treasury's Program Based Budget (Various Issues)

To close the persistent fiscal deficit, the National Treasury has persuaded the Legislature to pass numerous laws geared towards raising revenue. These laws primarily introduce new taxes, increase tax rates and mandate more aggressive interpretation of the tax laws. This is seen in the annual adjustment of excise tax and the introduction of new taxes such as the 1% Minimum Tax. This is in addition to giving the KRA Commissioner General the discretion to adjust excise tax. Kenya's fiscal policy is, therefore dominated by increased efforts to raise taxes from all existing tax heads.

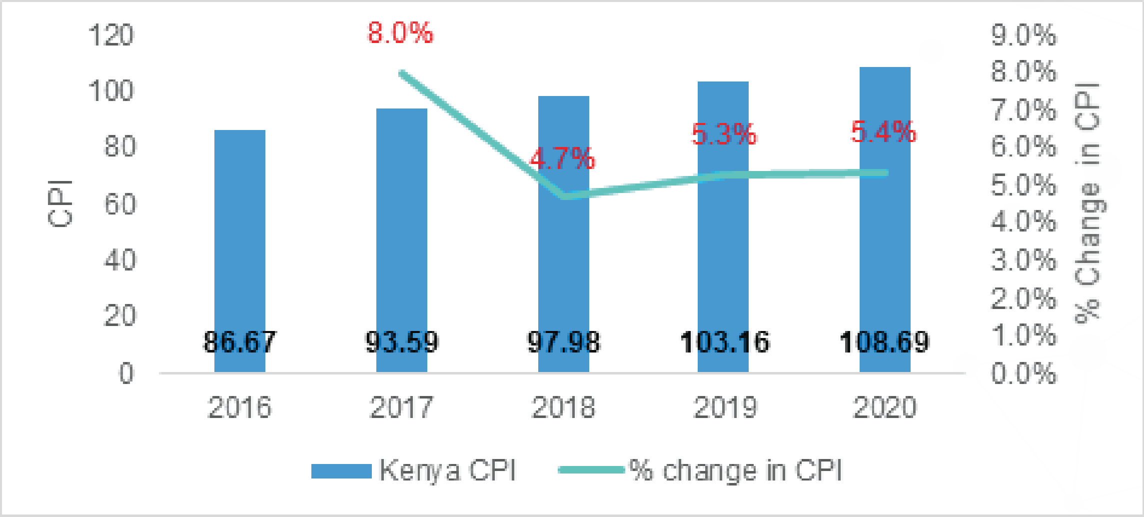
The fragility of the Kenyan economy in 2021 has immediate implications on the manufacturing sector. Undoubtedly, the economy will be on a delicate recovery path to restore growth levels and ensure debt resolution in the medium-term. This situation suggests that the economic policy priorities for the incoming governments must focus on restoring economic balance and ensuring frugal public spending without triggering debt default.

Besides the commitment to lower the costs of debt by lengthening the maturity of the loans and directing lending towards a 60:40 ratio for external and internal debt respectively, the government must also provide an impetus for growth in employment.

(e) Rising cost of living

The rapid increase in the cost of living disproportionately affects Kenyan households. Kenya's Consumer Price Index (CPI) has increased in the last five years from 86.67 in 2016 to 108.69 in 2020. This represents a 25.4% increase in the consumer price index that rose sharply in 2017 by 8% on account of economic dynamics which included drought.

Chart 6: Kenya Consumer Price Index (Annual)



Source: KNBS Economic Survey 2021

Section TWO>>

Big Ticket Items

2.| The Priority Issues

Because of the imperative to secure growth that creates jobs for Kenyans, the manufacturing sector must be at the center of policy discourse. In particular, the promise of Vision 2030 means that the idle labour in form of unemployment is not only undesirable, but also a barrier to making Kenya a real middle-class economy. Job creation is essential, but the nature of the jobs suggests that they should be in modern sectors with higher labour productivity and income.

Issue 1: Creating jobs in manufacturing

Unemployment is the leading challenge in economic policy management in Kenya and the manufacturing sector is central to providing a solution. It is essential for all political formations and party leaders to prioritize job creation. This will not only enable economic prosperity but also improve social welfare of all citizens.

Kenya's manufacturing sector is faced with a double conundrum - while the nominal value of output is growing, the sectoral contribution to the overall GDP is falling. Secondly, the share of formal employment in the manufacturing sector is stagnant. On the other hand, the growth in average wages of manufacturing firms has grown consistently at a rate of 10% per annum for five years before falling to 5% in 2020.

Growing the quantum of manufacturing jobs is important because it provides an avenue for decent wages in addition to ensuring that labour productivity is raised. Granted that the Kenyan economy has sufficient labour reserves, the priority for the manufacturing sector and the country converges in expanding jobs in the sector.

Chart 7: Economic growth and job creation

	2016	2017	2018	2019	2020
Annual GDP Growth Rates	4.2	3.8	5.6	5	-0.3
Total formal sector jobs ('000)	2,683.20	2,792.60	2,859.80	2,928.40	2,741.10
New Job Creation ('000)		109.40	67.20	68.60	(187.30)
Annual GDP Growth Rates		3.8	5.6	5	-0.3
Jobs per GDP Point		28.79	12.00	13.72	624.33

Source: Data from KNBS Economic Surveys (Various Issues), Authors own Calculations.

The President's Big Four Agenda has the ambition of raising the contribution of the manufacturing industry to 15% of GDP by 2022. This growth is ambitious but achievable. Based on the prevailing circumstances, the Agenda would increase employment in the sector from 293,000 to a minimum of 500,000 employees. The creation of linkages to other sectors is demonstrable and Kenya is well-placed to create manufacturing jobs since agricultural products would be inputs in the manufacturing industry. It is without a doubt that manufacturing creates high value jobs whose earnings play an important role in expanding the tax base. Additionally, employees working in the manufacturing sector would be part of the group considered high savers.

Chart 8: Trends in manufacturing employment as share of total employment (2016-2020)

	2016	2017	2018	2019	2020*
Manufacturing employment	315,100	317,500	321,300	329,000	293,800
Formal sector Employment	2,683,200	2,792,600	2,859,800	2,928,400	2,741,100
Manufacturing Employment/ Formal Sector Employment	11.7%	11.4%	11.2%		
Scenario Manufacturing Jobs (at 15% growth)	362,365	416,720	479,228	551,112	633,779

Source: KNBS Economic Survey 2021

As per the scenario: provided in Chart 8 above, manufacturing jobs would have doubled in size if the sector's growth stood at 15%, as envisioned in our development goals. Full scale economic recovery after the overwhelming economic shock caused by the confluence of debt distress and a global pandemic is not guaranteed unless the jobs that were lost in all sectors, including manufacturing, are restored. Kenya needs to recover from the first economic contraction in a generation (-0.3% in 2020)[3] and to regain the growth momentum. However, this must be accompanied by investments and job creation.

Creating a stable economy cannot happen without a viable and sufficiently large middle class in Kenya. Historically, middle class incomes tend to be created from modern economic activities which create stability of work, good conditions, and opportunities to drive consumption and allow for domestic savings. KAM commits to work with the public sector to explore and create a national level jobs creation plan with responsibilities accorded to both the public and private sectors. Our participation would be to create a coherent economic and social policy structure that would enable hiring, training, and deployment of workers in all sectors of the economy. Specifically, KAM shall draft a practical plan for the expansion of jobs in Kenya's manufacturing sector.

Issue 2: Raising export quantity and the intensity of Kenyan manufacturing

Kenya's export quantities are below what both the economic structure and income levels would predict. Therefore, expanding the value and volume of exports of Kenya's manufactured goods is both a medium and long-term goal.

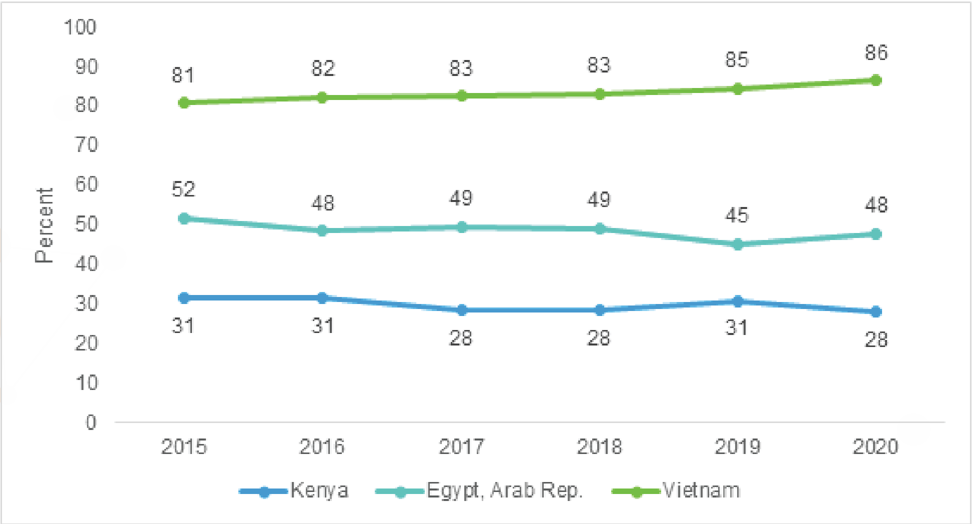
A focus on export markets is welcome and is aligned to the government's leadership in regional, bilateral and multilateral trade arrangements. Efficient manufacturing is possible in Kenya – some manufacturers under the KAM membership base are considered regional and even global leaders in select manufactured products. It is a shared responsibility of government and private sector firms to use export markets to build high productivity through competition in regional and global markets.

Raising the quantity of manufactured exports is dependent on a trade policy that allows for the importation of raw materials and intermediate goods for finishing or partial processing in areas where Kenya does not have comparative advantages. In areas where comparative advantage is sufficient, backward and forward integration, coupled with sound and competitive policies, is key to expanding manufacturing and ancillary jobs along supply and value chains. For example, agribusiness to manufacturing to export markets.

Needless to state, the effects of COVID-19 have adversely affected supply chains. Among the effects that are felt in Kenya are delays in supply of raw materials, intermediate goods, industrial machineries, and spare parts for domestic production. Consequently, this affected the export quantum in addition to the complexity of products that are sold outside Kenya. At the same time, the ranking of Kenya in Export Intensity shows that the country "underperforms" in respect to its share of exports, relative to its share of global imports. This gap can only be closed with an expansion of manufactured exports.

In the chart below, we compare manufacturing exports against all merchandise exports for Kenya, Egypt, and Vietnam. Manufacturing exports as a share of all merchandise exports for Vietnam rose from 81% in 2015 to 86% and averaged 84% within the period surveyed. For Egypt, the manufacturing exports as a share of all merchandise exports ranged between 52-48% and averaged 50% within the surveyed period. Kenya's performance on manufacturing exports as a share of all merchandise exports averaged 30%. The performance stagnated between 2015 and 2019 and declined between 2019 and 2020 from 31% to 28%. Relative to peers, Kenya's manufacturing exports are one-third of Vietnam's and half of Egypt.

Chart 9: Manufacturing exports as % of merchandise exports (2015-2020)



Source: World Development Indicators

There is great scope for embedding Kenyan manufacturing firms into regional and global value chains. This objective would ensure that Kenyan firms have access to the best possible opportunities by participating in value chains that generate higher value per worker and return on investments with more products available for export. The diversification of exports for Kenya is also a sound goal that can be met by allowing manufacturing firms to explore export maps for the region and other parts of the world in the search for new markets.

Data/rankings on Competitiveness Industrial Performance (CIP) index, produced biennially by the United Nations Industrial Development Organization (UNIDO), can give indication about the competitiveness of

Kenya's manufactured exports. Industrial competitiveness refers to a country's capacity to increase its presence in international and domestic markets while developing industrial sectors and activities with higher value added and technological content. Chart 10 gives comparative statistics for Kenya, South Korea, Tanzania, and Uganda. According to the chart, Kenya's major weakness lies in the inability to produce medium and high-tech manufactured goods, and this should be addressed.

Chart 10: Comparative CIP data for Kenya, South Korea, Tanzania and Uganda

Sector	South Korea	Kenya	Tanzania	Uganda
CIP rank	5	112	116	131
Medium- and high-tech manufactured exports share in total manufactured exports	0.74	0.24	0.38	0.2
Manufactured exports share in total exports	0.97	0.52	0.84	0.36
Share in world manufacturing exports index	0.22	0	0	0
Share of medium and high-tech activities in Manufacturing Export Index	0.9	0.29	0.46	0.24
Share of medium and high-tech activities in total MVA Index	0.75	0.14	0.07	0.13
Industrialization intensity index	0.79	0.2	0.16	0.19

Data source: https://stat.unido.org/database/CIP%202021

Because Kenya has a large and growing trade deficit, it is essential that we raise the quantum of exports and export intensity for manufacturing to fill this shortfall. Together with a review of the achievements of the Big Four Agenda, KAM calls on the new administration to re-energize Kenya Export Promotion and Branding Agency (KEPROBA) and revise Kenya's National Export Development and Promotion Strategy (NEDPS) to align it to the aforementioned employment strategy. A major commitment of this strategy is to raise the share of Kenyan manufacturing firms that generate exports sales from 6%, as identified by World Bank's Enterprise Survey of 2018, to 20% by 2028[4].

Issue 3: Reducing the regulatory burden on manufacturing

In a widely regarded economic paper, Economist and Nobel Laureate George Stigler theorizes the need for government regulation and recognizes that state regulations can either be a potential resource or threat to every industry[5]. This means that regulations can benefit society or be considered a burden. Regulatory burdens can be defined as the increase in complexity of rules and regulations that require firms to comply without adding value to the companies, households or the long-term objective of government policymakers.

The success of industrial policy requires that governments and firms work to reduce the inefficiencies in the allocation of resources. Rodrik (2004)[6], and Hausmann and Rodrik (2006)[7] explain that the industrial policy is more appropriately conceived as a process whereby the state and the private sector jointly arrive at diagnoses about the sources of blockage in new economic activities and propose solutions to them[8]. Rodrik (2007) adds that an industrial policy requires the government to take an ex-ante stand neither on the activities to be promoted nor on the instruments to be deployed. It simply requires it to build the public-private institutional arrangements whereby information on profitable activities and useful instruments of intervention can be elicited[9].

The main aim of economic regulation should be to induce competition, increase efficiency in resource allocation, and allow firms to expand the product space. Economies grow by upgrading the products they produce and export. The technology, capital, institutions, and skills needed to make newer products are more easily adapted from some products than from others[10]. A joint study between World Bank and Competition Authority of Kenya in 2015, found that there is a relatively high level of government intervention in markets where the private sector is already present, and significant, non-justifiable regulatory requirements to enter new markets[11] .

Based on this section, we identify regulatory burdens that have adversely affected Kenya's manufacturing sector including lengthy and manual processes of obtaining regulatory permits.

i. Lengthy and manual processes for obtaining regulatory permits

An analysis by Product Market Regulation Index revealed that Kenya is one of the countries with the most significant barriers to entrepreneurship. From the analysis, these barriers are a result of burdensome entry regulations that are not as common globally, and an uncontrolled system of license and permit requirements at the national and sub-national levels[12]. The KAM Regulatory Audit, 2020 identified the following immediate issues on regulatory permits related to manufacturing[13].

- Manual renewal of licenses, which is inefficient, increases the cost of doing business and creates loopholes for corruption and fraud. Approval processes for construction are bureaucratic, leading to the stalling of projects. There are no fixed timelines for each of the approval stages.
- The process of starting a business is long, cumbersome, and expensive, as a result of various requirements. These requirements include registration of the business, registration for taxes, and fragmentation of licenses that are required by various county departments.

The table below shows the summary of the number of charges.

Chart 11: Summary of cost of license across sectors

Sector	Number of Charges
Chemical and Allied	33
Metal and Allied	22
Paper and Paper Board	27
Plastics and Rubber	16
Building, Construction and Mining	23
Pharmaceutical	15
Automotive and Accessories	15
Timber, Wood and Furniture	12
Food and Beverage	41
Leather and Footwear	19
Salt Sector	12

Source: KAM Regulatory Survey 2020

The next administration needs to reduce the number of regulations, bring down the cost and time spent on compliance and consolidate regulators.

Issue 4: Raising investment in the manufacturing sector

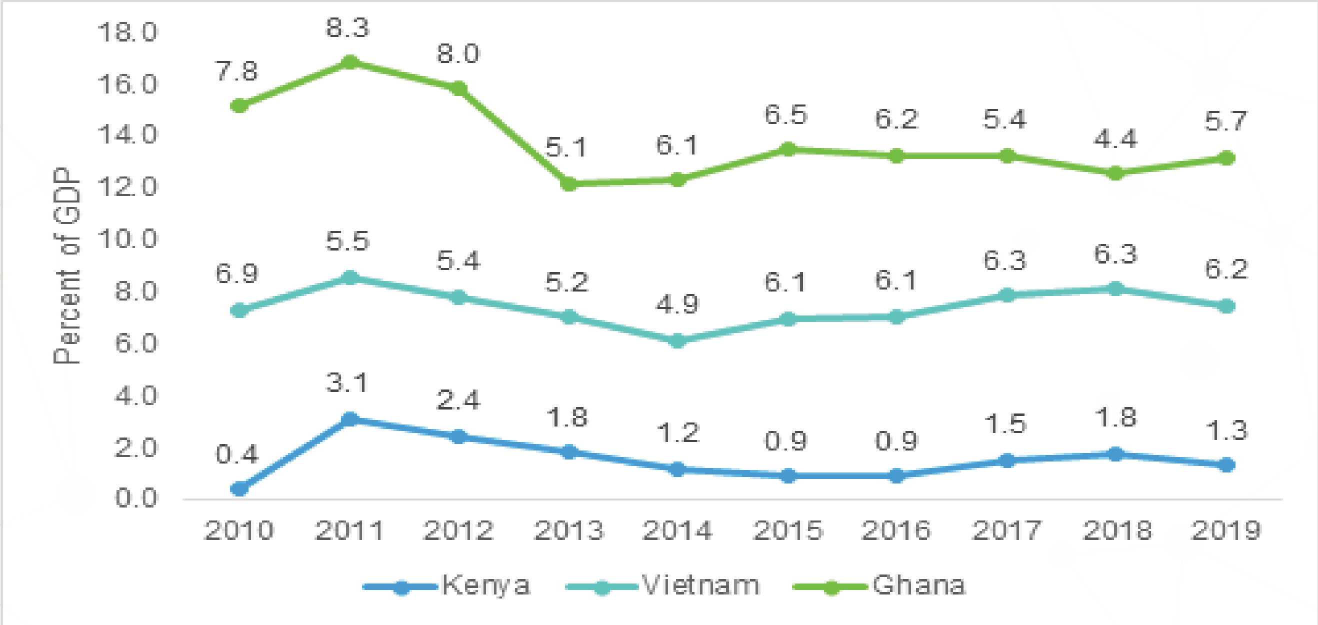
Raising investment, local and foreign, is imperative in boosting the efficient growth of manufacturing and the entire Kenyan economy.

Foreign Direct Investment (FDI) provides the capital required by firms either in their formation, buying new technology, providing expansion, or improving overall productivity. Verhoogen (2021) argues that firms in developing countries benefit from the fact that advanced technologies and products have already been developed in industrialized countries and can simply be adopted through a process often referred to as industrial upgrading[14]. One of the important fixes that FDI can bring to Kenya's Manufacturing sector is industrial upgrading where Kenyan firms will attract additional resources and technology transfer from investors coming into the country.

The Product Market Regulation Index confirms that barriers to trade and investment are higher in Kenya than in the Organisation for Economic Co-operation and Development (OECD), Latin America and the Caribbean (LAC) and Brazil, Russia, India, China, and South Africa (BRICS) countries. The 2015 World Bank study on Unlocking Growth Potential in Kenya by Dismantling Regulatory Obstacles to Competition cites barriers to trade and investment as the limited use of mutual recognition agreements and international standards and certification procedures and relatively higher import tariff rates for agricultural products.

A country of Kenya's economic standing should have the capability of attracting FDI net inflows that are more than 10% of GDP. FDI net inflows measure the capability of a country to attract and retain FDI. This means that the business environment is competitive, compared to other destinations in the long term. The chart below compares Kenya's performance to selected countries (Vietnam and Ghana) in respect to attracting and retaining FDI. In the last decade, Kenya's net inflows averaged 1.82% of GDP while Vietnam and Ghana have attracted an average of 22.98% and 5% of GDP respectively, on an annual basis. Kenya's performance in attracting FDI and retaining it has stagnated in the last decade and is a quarter of Ghana's performance.

Chart 12: Foreign Direct Investment (net inflows) (% of GDP)



Source: World Development Indicators[15]

FDI can be classified into different kinds which include horizontal FDI, conglomerate FDI, vertical FDI and platform FDI as explained by Angel (2020)[16]. Downstream and upstream manufacturing requires diverse forms of FDI. The principle in stimulating FDI is dependent on providing a business environment that stimulates competition and has consistent and sensible rules for businesses. However, the disproportionately high taxes and more complex policies in Kenya as compared to other EAC neighbouring countries provide incentives for contraband trade, hence, reducing Kenya's ability to attract investment in industries afflicted by contraband trade.

Issue 5: Efficient provision of public goods and essential services

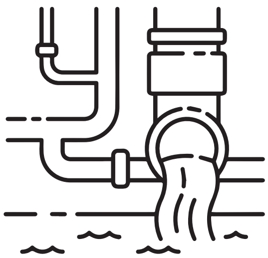
Industrial development is predicated on the availability of essential public goods and services. These goods and services are the responsibility of national and county governments in Kenya. At the national level, there are essential services whose provision, the Constitution (2010), has specifically placed in the hands of the national government. Among other responsibilities, the national government should emphasize dedicated provision of essential services and public goods because they lead to growth in labour productivity.

There are specific public goods whose availability reinforces industrial policy by driving down costs of inputs for all industry players in the manufacturing sector. Public goods that are known to spur industrial growth include public information, infrastructure, law and order, and the targeted wide sector industrial policies.

1. Sector-wide industrial policies

Loayza (2017) shows that the main justification for targeted sector-wide industrial policy is the need to address market imperfections. This involves providing goods that solve the problem of asymmetry of information. By embracing targeted sector-wide industrial policy that makes the business environment better for all businesses, policymakers would be solving the issue of imperfect knowledge on existing constraints, incentives, and opportunities across the economy; and their vulnerability to corruption, manipulation, and rent-seeking[17].

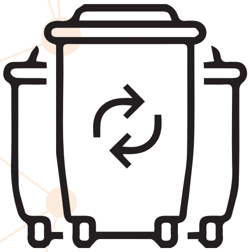
For this part, we classify public goods that can be provided by national and county governments. They can vary between "vertical" policies that favour specific firms or narrow sectors and "horizontal" policies that target broad sectors by improving their business environment. The more "horizontal" these policies are, the more they approach the characteristics of public goods. Improving the business environment can be done at the two levels of government.



2. Water provision

A large part of potential and existing investments in manufacturing in Kenya require the processing of food and agricultural inputs. The adequacy and quality of water provision in urban settlements in the country is woefully inadequate.

Industrial processing of all goods from textiles, food, chemicals, and other sectors require water. Yet, the four largest urban conglomerations in Kenya (Nairobi, Mombasa, Nakuru and Kisumu) fail to meet industrial and domestic water demand. Because county governments have taken it upon themselves to directly provide water services, the national government needs to support this through conditional grants. The use of conditional grants will not only be helpful by expanding access but also provide an incentive for provision of this essential service and collect revenue from it. On the other hand, Council of Governors (CoG) needs to develop metrics for assessing the capacity for the provision of these essential services for each county government.



3. Urban waste management

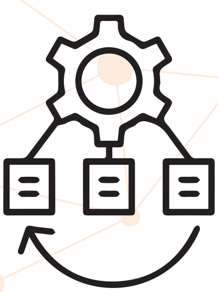
In most of Kenya's industrial zones and dedicated areas, the county and national governments have not provided regular and comprehensive waste collection and management services. This is an omission and neglect of a statutory obligation as well as an imposition of costs on businesses. Most manufacturers require adequate infrastructure for waste disposal. Therefore, inadequate mechanisms for waste disposal imposes a cost on the firms and affects configuration of plants and their overall productivity. It is imperative for the national and county governments to approve a workplace for upgrading waste management facilities in all industrial and population settlements in the country.

4. Efficient judicial resolution

A significant number of business enterprises rely on commercial contracting to supply and create value. It is, therefore, accepted that disputes on commercial performance do arise. Despite the constitutional requirement for it, prompt dispute resolution is still a rare outcome in Kenya. This failure of the formal dispute resolution system imposes significant financial and time costs on the parties. To improve the efficiency of commercial dispute resolution, the three arms of government must commit to provide the resources and monitor the performance of every tribunal and court level for efficiency in dispute resolution.

5. Public information

This will involve full disclosures of all information that is considered public. Public information, in this case, would include general government information and research developed through taxpayers' resources. Economic and transaction data that is in the possession of public sector institutions should be made available because it reduces the cost of business decision making.



6. Infrastructure

The manufacturing-specific infrastructure that is required includes providing an efficient logistical ecosystem and improving the ease of setting up manufacturing facilities. There is evidence that an efficient logistics ecosystem is a catalyst in enhancing the competitiveness of all sectors of the economy and improving supply chain efficiencies[18].

- **National infrastructure**

  At the national level, important infrastructure for the operating environment includes an extensive broadband network and demand-induced road network. An example of a country that tracks the requirements for a national logistics hub is India, through its Logistics Ease Across Different States (LEADS). The hub tracks specific issues that include infrastructure, services, timeliness, track and trace, competitiveness of pricing, safety of cargo, operating environment, and regulatory processes[19].

- **County infrastructure**

There exists a manufacturing-specific infrastructure that is required to induce competitiveness for manufacturing at the county level. This includes the ease of setting up a warehouse, regulatory approvals and building a manufacturing plant.

Issue 6: Effective and pro-industry national taxation structure

Kenya has a complex and bulky tax code. Full compliance requires that firms employ tax planners, tariff engineers, lawyers, and specific accountants to render professional advice. Large firms can often afford the cost of compliance with the tax code, whereas small scale manufacturing firms often comply at great costs and loss of efficiency. The taxation regime raises three significant concerns:

a. Lack of clear tax policy objectives

The tax policy objectives on legislative proposals to inform changes in taxation are not clear. With every change in the tax code, KAM has identified fundamental tax policy issues that are inconsistent with Kenya's stated economic policy objectives. For example, charging excise tax to financial transactions is contrary to economic literature. This is because excise taxes ought to be charged on goods or services that create negative externalities.

Another concern on tax policy objectives is taxing raw materials and intermediate goods which are brought into Kenya for processing into final goods. Peter Diamond and James Mirrlees (1971), note that an optimal tax structure should not include the taxation of raw materials and intermediate goods, since this would prevent efficiency[20]. This has been demonstrated by other studies and co-opted as a conventional practice. A review of taxation policy shows that Kenya is increasingly subjecting many raw materials and intermediate goods for taxation, thereby harming export competitiveness of Kenya's manufacturing firms.

b. Erratic changes in the tax code

At the firm level, the time required to set up and ensure efficient operations is long and costly. This means that the tax code should be stable to allow for efficiency in compliance and resource planning. Yet, Kenya's tax code changes annually and in very significant ways (through the Finance Bill approved annually by Parliament). Additionally, tax code changes are accompanied by significant requirements for compliance that are brought forward by regulations. These regulations also create additional complexities if not published through a consultative process and in advance of effective date.

c. Multiple taxation at county and national government levels

The KAM Regulatory Audit 2020 identified double taxation in the following areas - transport vehicles branding charges, cold storage charges, cess on agricultural produce and charges on flower products (also charged by Horticulture Crop Directorate at the national level).

Issue 7: County industrial competitiveness

The Constitution of Kenya, in 2010, ushered in a decentralized system of governance comprising a national government and 47 county governments.

The devolved system of government, though viewed by many as a political step to decentralize power, is an economic tool for the country to spur economic development to reap the full benefits of liberalized trade. Kenya's main objective of adopting a devolved system of government was to bring services closer to the people and enhance development through friendly legislation and policies. It was anticipated that with devolution as a key development tool, the country's economy would grow and the cost of doing business would reduce because services would be closer to the people.

Chapter 12 of the Constitution outlines the provisions on public finance issues and gives two core values under which resources are to be shared: Equity in resource sharing between two levels of government and public participation in the budgeting process and exploring financing options by county governments.

Revenue raised nationally shall be shared equitably between the national and county governments (vertical share) and among the county governments (horizontal share) to enable them provide services and perform their functions.

Article 203(2) of the Constitution gives the minimum threshold of the amount of equitable revenue to be allocated to counties as 15% of the latest audited revenues (vertical share).

Article 209 (5) of the Constitution provides that taxation and other revenue-raising powers of a county shall not be exercised in a way that prejudices national economic policies, economic activities across county borders or the national mobility of goods, services, capital or labour.

Section THREE>>

Riding the Storm

3.| Solutions Matrix - KAM Manifesto

Issue	Timelines		
	Short Term	Medium Term	Long Term
1. Macroeconomic issues	**1.1** Both levels of government to adopt best practices in Public Financial Management. This will enable credible budgeting and revenue projections. **1.2** Ensure that all public investments by both levels of government are subject to economic appraisal to guarantee value for public finances. **1.3** Ensure a stable exchange rate regime which balances the fact that Kenya is a net importing country with a narrow export base.	**1.4** The government to aim at reducing the fiscal deficit to 3 percent of GDP in the period 2022-2027 in line with EAC monetary convergence criteria **1.5** Progressively reduce the debt to GDP ratio to a maximum of 50% of the GDP.	**1.6** 10% year on year GDP growth rate driven mainly by private consumption, private investments & export growth.
2. Creating manufacturing jobs	**2.1** The new administration should work with KAM to provide a plan to create a coherent economic and social policy structure that would enable hiring, training and deployment of workers throughout the sectors of the economy. **2.2** KAM and the new administration can work together to create a practical plan for expansion of jobs in the Manufacturing sector. **2.3** Employment tax that does not burden the employer and makes it easy to create employment.	**2.4** Subsidize training in science, technology, engineering, math (STEM)/apprenticeship. **2.5** Increase the number of students in tertiary and midlevel colleges. **2.6** Support the diversification of curriculum by universities.	**2.7** Building working government -industry-university partnerships commonly referred to as the Triple Helix Model. **2.8** Backward integration of manufacturing with other sectors to create ancillary, direct and indirect jobs along the value chain/supply chain.
3. Raising export intensity of Kenyan manufacturing	**3.1** Call upon the new administration to financially re-energize KEPROBA. **3.2** Work with KAM in reviewing and improving NEDPS with a focus on a monitoring target (12-15% of GDP by 2027).	**3.7** Work on strategies to embed Kenyan manufacturing firms into regional and global value chains. A major commitment of this strategy is to raise the share of Kenyan manufacturing firms that	

	3.3 Recognition of Kenya's export champions by government. **3.4** Establish a joint Private-Public Sector Commission to diagnose export-related challenges. **3.5** Seek multiple Free Trade Agreements to boost market diversification. **3.6** Introduce an Exports Incentive Policy.	generate exports sales from 6% as identified by the World Bank's Enterprise Survey of 2018 to an aspirational level of 20% by 2028. **3.8** Increasing labour and total factor productivity in the manufacturing sector. **3.9** Utilize the Privatization Policy to raise FDI. **3.10** Harmonization of EAC domestic taxes and policies that have created trade asymmetry due to growth of contraband.	**3.11** Raise Kenya's exports value-add through export quantum increase & medium/high technology products. **3.12** Make Kenya an African export superpower.
4. Reducing the regulatory burden on manufacturing	**4.1** Assent and enact the Public Participation Bill which is at its 2nd Reading in Parliament. **4.2** All levies and charges by national government agencies and any changes to be made under the Miscellaneous Fees and Levies Act, 2016 to support the predictability of the regulatory environment in Kenya through the following amendments: **Introduce a new Section 4A to read as follows:** *Notwithstanding any provisions of any other law, no levy, fee or charge shall be imposed by a national Government agency unless provided for under this Act* **4.3** Allowing competition between SGR and road transport for goods imported through the Port of Mombasa. **4.4** Ensure efficiency in port operations by establishing a benchmark against the world's best ports in Singapore and Hong Kong. **4.5** Reduce the cost of construction permits and time taken to obtain them to not more than 30 days.	**4.6** Establish an objective monitor on regulatory burden on manufacturing and publish it. **4.7** Privatize port management across all Kenyan ports. **4.8** Introduce Better Regulation Commission to review and reduce regulatory burdens by 50%.	**4.9** Carry out regulatory reforms to address overlaps, duplications, rates for fees and charges amongst regulatory agencies. **4.10** Establish a uniform high level government approval process for any regulatory agency imposing corrective measures touching on business. **4.11** Establish a digitized One-Stop Regulatory Shop bringing together National and county agencies to help in reducing overlaps, duplications and excess fees & charges.

5 Raising investment in manufacturing	**5.1** Increase the use of mutual recognition agreements and the international standards and certification procedures. **5.2** Increase investor certainty and transparency by hastening decision for work permit applications. **5.3** Adjust excise tax for inflation only once every five years to allow for organic growth, reduce incentives to engage in illicit trade and improve Kenya's FDI attractiveness.	**5.4** On FDI related to joint ventures, limit government conditions, and allow Kenyan firms to undertake due diligence. **5.5** Establish a National Investments Council with a sunset clause.	**5.6** Provide a predictable foreign investment strategy
6. Providing public goods for manufacturing	**6.1** Law and Order- Ensure faster case resolution at courts and tribunal levels for commercial disputes.	**6.2** Investing and attracting Investment in Research and Development. **6.3** Develop sector-wide Industrial policies that target broad sectors by improving their business environment. **6.4** Strengthen Kenya's national supply chain to prevent disruptions from COVID-19 or other global shocks and geopolitical risks.	**6.5** Provide required manufacturing specific infrastructure, including provision of an efficient logistical ecosystem and improving the ease of setting up of a manufacturing plant (at county and national levels).
7. County Industrial Competitiveness	**7.1** Develop a County Industrial Competitiveness Index to assess the first two cycles of Devolution and present actionable recommendations fo the third phase. **7.2** Inclusion of manufacturing centric agenda in the third generation County Integrated Development Plans (CIDPs). **7.3** Implement the National Policy on County Governments Own Source Revenue, 2016 and enact the County Government (Tax Regulation) (Draft) Bill, 2016. **7.4** Formulate the Tariffs and Pricing Policy and	**7.5** Develop a model county industrial policy anchored on National Industrial Policy. **7.6** KAM, national Government and the Council of Governors (CoG) to jointly develop a business-led initiative to deliver world class clusters.	**7.7** Operationalize manufacturing-centric county regional economic blocs.

	supporting legislation to guide predictable imposition of levies, fees and charges as a legal requirement under section 120 of the County Governments Act, 2012.		
8. Effective and pro-industry national taxation structure	**8.1** Implement National Taxation Policy aimed at enhancing certainty and predictability, reducing the number of taxes, reducing levels of taxation, reducing reliance on direct taxes, broadening tax base, automating tax collection, increase use of iTax, and introduce transitional clauses for new taxes. **8.2** Revert Investment Deduction Allowance to 100%/150% to spur county industrial agenda. **8.3** Adopt a principle of taxing final goods, rather than taxing raw materials and intermediate goods. **8.4** Ensuring that there are no erratic changes to Kenya's Tax code. **8.5** Remove 16% Value Added Tax (VAT) on plant and machinery. **8.6** Earnings Before Interest, Taxes, Depreciation and Amortization (EBITDA) -Limit interest deductibility to be the greater of: • **30% of EBITDA** • **12% of assets** • **KES 400 million** - Allow excess interest to be carried forward for up to 5 years. - Apply the deductibility limits to net interest, not gross interest. - Apply the deductibility limits only to entities with foreign borrowings **8.7** Abolish double taxation at the county and national government levels for services including vehicle branding, cold storage as well as cess on agriculture		

	and horticulture products **8.8** Limit the use of excise taxes and levies only to goods that damage public health or the environment.		
9. Fully implement existing manufacturing -centric policies **&** **Establish monitoring, evaluation and learning frameworks**	**9.1** Local Content Policy **9.2** Buy Kenya Build Kenya (BKBK) strategy **9.3** National Trade Policy **9.4** Integrated National Export Development & Promotion Strategy **9.5** Automotive Policy **9.6** Draft Public Procurement & Asset Disposal Policy **9.7** Draft National Taxation Policy	**National Industrialization Policy**	

Annex: Types of FDI

Type of FDI	Explanation
Horizontal FDI's - *(This can also be referred to as Joint Ventures.)*	This is the most common type of FDI and it primarily revolves around investing funds in a foreign company belonging to the same industry as that owned or operated by the FDI investor. An illustration of this kind of FDI is where a company invests in another company located in a different country, and both the companies are producing or dealing in similar goods. This is important for manufacturing firms that would get this kind of investment to stretch the comparative advantage that firms already have and expand that kind of manufacturing they are undertaking.
Conglomerate - *(International and in different industries.)*	The conglomerate FDI is defined as when investments are made in two completely different companies of entirely different industries. As such, the FDI is not linked directly to the investors business. For instance, the US retailer Walmart may invest in TATA Motors, the Indian automobile manufacturer.
Vertical (Regional) - *Integrating Value Chains*	A vertical FDI occurs when an investment is made within a typical supply chain in a company, which may or may not necessarily belong to the same industry. This would be an important move for Kenya because it allows for Kenyan firms to expand capacity in specific value chains.
Platform FDI - *(EPZs types)- Pure export focus.*	The platform FDI is where a business expands into a foreign country, but the products manufactured are exported to another, third country. For instance, the French perfume brand Chanel set up a manufacturing plant in the USA and export products to other countries in America, Asia, and other parts of Europe.

Source: (Angel Broking), 2020, Types of FDI.

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Who we are

Established in 1959, Kenya Association of Manufacturers (KAM) is a representative of manufacturing and value-add industries in Kenya. The Association has grown into a dynamic, vibrant, credible Association that unites industrialists and offers a common voice for businesses.

We have been front and centre in driving fact-based policy advocacy towards the formation of industrial policies to strengthen and support the country's economic development. Through fact-based advocacy, KAM partners with Government and its associated agencies to ensure a dynamic and flourishing manufacturing sector in Kenya, to realize a double-digit contribution to GDP.

Our Vision

To be a World Class BMO that effectively delivers services to its members

Our Mission

To promote competitive and sustainable local manufacturing

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