FOREIGN DIRECT INVESTMENT DESTINATION IN KENYA: BENCHMARKING THE CAUSAL FACTORS

By

Benson A. Ateng', Senior Lecturer

Department of Economics and Resource Management, The Technical University of Kenya

Kenneth W. Aduda, Senior Research Fellow

Jaramogi Oginga Odinga University of Science and Technology

Florence Nelima, Lecturer

Department of Economics and Resource Management, The Technical University of Kenya

Abstract

The main objectives of this paper are to determine key factors that explain why Kenya is lagging behind selected African and Asian countries in attracting foreign direct investment (FDI) inflows and what the country needs to do to improve its competitiveness.

We conducted benchmarking analysis of Kenya with selected African and Asian countries in attracting FDIs in order to explain why Kenya is lagging behind some of these countries.

Several reforms have been undertaken to attract FDI; however, inflows into Kenya have been erratic and way below the country's potential. Varied challenges are identified -- quality of infrastructure; macroeconomic policies; low levels of income; institutional framework; democracy and corruption; domestic savings and investments; and low factor productivity.

Comparison economies are a good indication of how well countries are doing against the competition, while comparisons with better performing economies can show where to head in the future. The paper makes recommendations that once implemented will go a long way in streamlining institutional, legal and administrative framework for attracting FDI and also in contributing to the achievement of Vision 2030 and Sustainable Development goals.

Keywords: Benchmarking, FDI, corruption, infrastructure, competitiveness indexes

1.1 Introduction

Kenya's long term development strategy is captured in Vision 2030 (Republic of Kenya, 2007), which aims at transforming the country into a rapidly industrializing middle income nation by 2030. The Vision is being implemented through five-year rolling plans called medium term plans (MTPs). The first MTP ended in mid-2013 while the second MTP runs from July 2013 to June 2017. The Vision's major thrust is the implementation of flag-ship projects which will require substantial resource inputs from both the private and public sectors. In this respect, foreign as well as domestic direct investments are expected to play a major role in financing the projects in the form of equity and debt; indeed in excess of 70% of the funding needs of these projects.

Foreign Direct Investment (FDI) is considered to be important in promoting economic growth in developing countries by providing capital, technology, improvement of skills, efficiency and trade; and by providing domestic small and medium-sized enterprises with linkages and markets for the supply of goods and services. However, despite the fact that several reforms have been undertaken by the Government of Kenya to attract more FDI, these efforts have not led to significant success in FDI inflows.

Mwega and Ngugi (2007) argue that FDI inflows to Kenya are largely equity and reinvested earnings. Intra-company loans flowing into Kenya are low, depicting the limited level of offshore financing in the country. Reinvested earnings of course depend on the performance of the economy and the profitability of multinational corporations. Available data shows a clear increase in reinvested earnings during 1975–1980 and 1985–1990, periods of fairly rapid economic growth fuelled by "coffee booms" as well as economic reforms in the latter period. There also seems to be a negative correlation between equity and reinvested earnings, with the country relying on new inflows during periods of poor economic performance and reinvested earnings during periods of good economic performance.

The main objectives of this paper are to determine the key factors that explain why Kenya is lagging behind selected African and Asian countries in attracting FDI inflows and what the country needs to do to improve its competitiveness.

1.2 Methodology

We employed descriptive statistics to conduct benchmarking analysis of Kenya against twelve selected African and Asian countries to determine why Kenya is trailing some of these countries.[1]Benchmarking is an evaluation of criteria that compares and contrasts performance among a group of competitors, and in doing so, develops measurements that result in a standard for "best practices" in the given field or area. It is used across a wide range of organizational disciplines, including site selection and expansion. It has evolved from its roots as a method for purely quantitative, "boilerplate" comparison, to a highly

[1]The 12 countries included Malaysia and South Korea from South Asia; Tanzania, Uganda and Rwanda from the East African Community; Ghana and Nigeria from West Africa; South Africa and Mozambique from Southern Africa; Morocco from North Africa; and Ethiopia and Mauritius from the rest of Africa.

customizable mechanism that emphasizes and reinforces strategic objectives, and identifies opportunities to gain added competitive advantage (Gagaya and Lipimile, 2008).

Benchmarking is particularly adaptable to the complex, high-stakes world of foreign direct investment. Through the collection of timely, "on-the-ground" information, benchmarking reduces a variety of risk factors for investors, which in turn, helps to foster increased FDI flow. In particular, the information that is compiled and quantified during a benchmarking study often relates to five categories of issues that are important to investors. According to the World Bank (2007), the five categories are the country's business climate and government policy; specific industry factors; investment promotion services; infrastructure, such as land and building space, power and telecommunications; and labour.

In doing the comparative analysis, we used different indexes of competiveness. World Economic Forum (2014) defines competitiveness as the set of institutions, policies, and factors that determine the level of productivity of a country, which is one of the central determinants of its return on investment. Return on investment is one of the key factors that foreign investors -- like any private investor -- consider when they decide where to invest their resources. A more competitive economy is one that is likely to grow faster and attract more FDI over time.

Xavier Sala-i-Martín, *et al* (World Economic Forum, 2014) make a detailed presentation of 12 pillars of global competitiveness which they group into three categories of indicators – **basic requirements**(institutions, infrastructure, macroeconomic environment, and health and primary education);**efficiency enhancers**(higher education and training, goods market efficiency, labour market efficiency, financial market development, technological readiness, and market size); and **innovation and sophistication factors**(business sophistication and innovation) – with weighted average indicators of 60%, 35%, and 5%, respectively. We considered Kenya's performance in these areas compared to its share in FDI inflows.

A number of indexes (FDI competitiveness index, inward FDI potential index, inward FDI performance index, and global competitiveness index)exist that measure a country's potential in attracting FDI.

FDI Competitiveness Index (FDICI) provides the possibility of conducting detailed analyses of strengths and weaknesses for countries and regions. These analyses provide support to policymakers to improve the country's attraction for receiving inward FDI. They also enhance the discussion of why FDI flows still remain concentrated in other economies and, additionally, about the areas in which emerging and developing countries have to improve in order to narrow the gaps. In addition, FDICI assists the location decisions of prospective investors as well as policymakers in their efforts to promote FDI-led economic development.

Inward FDI Potential Index is based on FDI inflows and structural economic factors (UNCTAD, 2011). It is the average of the scores on eight variables for each country. The eight variables are: (i) GDP per capita; (ii) real GDP growth; (iii) exports; (iv) number of telephone lines per 1,000; (v) commercial energy use per capita; (vi) R&D expenditure as

a percentage of Gross National Income; (vii) students in tertiary education as a percentage of the total population; and (viii) country risk. The Inward FDI Potential Index ranking is based on the simple average of a country's percentile rank in each of the economic determinants areas. A country's ranking within each group of determinants is based on the simple average of the country's percentile rank of each variable included in the group. World Development Report provides information on the variables used in constructing this index (UNCTAD, World Investment Report 2012).

The Inward FDI Performance Index is the ratio of a country's share in global FDI flows to its share in global GDP (UNCTAD 2005). Countries with an index value of one receive FDI exactly in line with their relative GDP. Countries with an index value greater than one attract more FDI than may be expected on the basis of relative GDP.

Countries with an index value greater than one may have the following characteristics: exceptionally welcoming regulatory regimes, very well-managed in macroeconomic terms or efficient/low cost business environments. These countries may also offer other competitive attractions such as good growth prospects, ample skilled labour, natural resources, good R&D capabilities, advanced infrastructure, efficient financial support or well-developed supplier clusters. In addition, they could have privileged access to large markets, or serve as entrepot base or tax havens, etc. On the other hand, countries with index values less than one may suffer from instability, poor policy design and implementation or competitive weaknesses in their economies.

Economies are ranked on their **ease of doing business**, from 1 – n, where n is the number of countries in the sample (World Bank, 2013). A high ranking on the ease of doing business index means the regulatory environment is more conducive to the starting and operation of a local firm. Often, improvements on the *Doing Business* indicators proxy for broader reforms, which affect more than the procedures, time and cost to comply with business regulation and the ease of access to credit. This index averages the country's percentile rankings on 10 topics, made up of a variety of indicators, giving equal weight to each topic.

1.3 Findings

1.3.1 Trends in FDI inflows

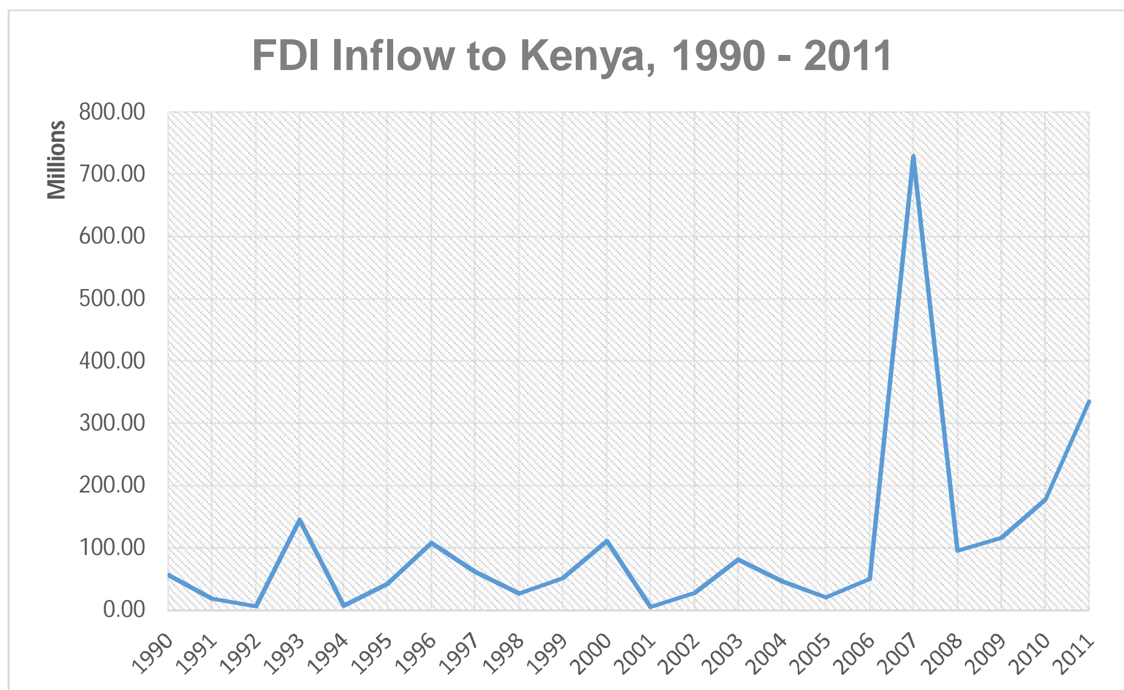
1.3.1.1 Sources and amounts of FDI

The United Kingdom, Germany and the Netherlands have been the leading sources of FDI inflows to Kenya since independence. However, the latest economic data shows that China, South Africa, India and South Korea have risen to stand among the top five sources of FDI for Kenya, knocking off the UK, Germany and the Netherlands (UNCTAD, 2013). The change in FDI pecking order deepened in the past five years as the majority of developed countries – under the shockwaves of debt crises – cut back on foreign investment while emerging economies scaled up their search for new business opportunities in frontier markets. In the first six months of 2011, China, South Africa, India and South Korea invested a total of Sh4.4 billion to make four out of five top sources of FDI for Kenya (UNCTAD, 2013). Most of that investment went into manufacturing, energy, tourism and construction sectors. China has become Kenya's leading source of FDI after

it pumped Sh2.5 billion into the economy, seeking to consolidate its new-found economic clout in the country. The Chinese broke into Kenya's list of leading FDI sources in 2011 with a total investment of Sh40.2 billion. Developed economies, including Israel, Canada, Germany and Italy lost clout after each invested less than Sh500 million in Kenya in 2012.

Some of the factors of attraction were: relatively high level of development, good infrastructure, market size, growth and openness to FDI at a time when other countries in the region had relatively closed regimes which made the transnational corporations choose Kenya as their regional hub. FDI started at a low level of around U$10 million a year in the early 1970s before peaking at US$80 million in 1979-1980. However, the deterioration in economic performance, together with growing problems of corruption and governance, inconsistency in economic policies and structural reforms, and the deterioration of public services and infrastructure generated a long period of low FDI that started in the early 1980s and continues to date. Figure 1 shows the trend in FDI inflows to Kenya during the period 1990-2011. The sharp rise noted in 2007 was due to the Initial Public Offerings in the ICT sector.

Figure1: Annual FDI Inflows to Kenya 1990 - 2011



Adapted from World Development Indicators, The World Bank

1.3.1.2 Kenya vis-à-vis selected countries

The efforts by Kenya to attract foreign direct investments and to strengthen private sector investments can be traced a few decades ago. However, the efforts have come with challenges which have made some of the anticipated and expected results unattainable. FDI grew steadily through the 1970s as Kenya remained as the prime choice for foreign investors seeking to establish a presence in Eastern and Southern Africa.

Inflows of FDI in the period 1981-1999 averaged only US$22 million a year. Although the sale of mobile phone licenses to Kenyan-foreign joint ventures pushed FDI to over US$100 million in 2000, inflows fell again to around their average of the 1980s and 1990s, before rising again in 2003 on the back of textile investments in export processing zones that may not prove sustainable.

Although Kenya was the lead destination of FDI to the East African Community in the 1970s and 1980s, the relative level of inflows was never high by developing countries' standards, since it was only 7.5 per cent of GDP in 2003, compared with 25.3 per cent for Africa as a whole and 31.5 per cent for developing countries(World Bank, 2012 and 2013).

Table 1 shows FDI inflows for selected countries for the period 2006 to 2011. Table 2 presents a summary of FDI inflows into Sub-Sahara Africa, East African Community, Kenya, Tanzania and Uganda from 2000 to 2010. FDIs into Sub-Sahara Africa have been showing significant changes in terms of their destinations. The bulk of the cumulative FDIs in the East Africa region were predominantly in Kenya up to the last decade. However, in recent years, Kenya's neighbours, Uganda and Tanzania, have been increasingly taking up more of the share of FDIs into the region.

Kenya's regional leadership in attracting FDI disappeared as soon as Tanzania and Uganda started reforming their economies and opening up to foreign investors in the early 1990s, at a time when Kenya itself was suffering from economic stagnation. The end of apartheid in South Africa in 1994 also increased competition in the attraction of large transnational companies seeking a single production or headquarters centre in English-speaking Africa.

Some of the FDI inflows to the EAC member states are from Kenya. Some Kenyan companies have expanded their operations in these countries to diversify their operations. The head offices are still in Kenya.

Table 1: FDI Inflows for Selected Countries 2006-2011 (million US $)

Country	2006	2007	2008	2009	2010	2011
Malaysia	6,060	8,595	7,172	1,453	9,103	11,966.01
Nigeria	4,898	6,087	8,249	8,650	6,099	8,915.00
South Korea	4,881	2,628	8,409	7,501	8,511	4,660.90
Morocco	2,449	2,805	2,487	1,952	1,574	2,519.11
Uganda	644	792	729	842	544	792.26
Ghana	636	855	1,220	1,685	2,527	3222.25
Ethiopia	545	222	109	221	288	206.09
South Africa	527	5,695	9,006	5,365	1,228	5,807.36
Republic of Tanzania	403	582	1,247	953	1,023	1,095.40
Mozambique	154	427	592	893	989	2,093.47
Mauritius	105	339	383	248	430	273.39
Kenya	51	729	96	116	178	335.25
Rwanda	31	82	103	119	42	106.00

Source: Adapted from UNCTAD World Investment Report 2012.

By the end of 2010, only 12.9 percent of FDI positions in the East African region were placed in Kenya compared to 30.2 percent and 56.9 percent in Tanzania and Uganda, respectively, in the same period. Relatively low share of the FDI in Kenya as compared to those of Tanzania and Uganda is the result of diminishing share of Kenyan economy in the stream of inflows during recent years. In 2000, the share of FDIs inflow into Kenya was 1.6 percent of the total FDI inflows into Sub-Sahara Africa. This was reduced to 0.7 percent by the year 2010. However, Tanzania's share of FDIs dropped from 6.9 to 1.6 percent while Uganda's share went up from 2.4 to 3.0 percent of the total FDIs into the Sub-Saharan Africa region during the same period. These trends show that in recent times, Kenya has been losing more FDIs.

Table2: FDI Inflows *(millions US$)*

Region/Economy	2000	2001	2002	2003	2005	2010
Sub-Sahara Africa	6,731	14,910	11,477	14,328	19,490	27,153
East Africa Community	733	544	607	647	1,335	1,435
Kenya	110	5	27	81	21	185
Tanzania	463	388	396	364	935	433
Uganda	160	151	184	202	379	817

Source: World Bank Data Website **http://www.data.worldbank.org/**

1.3.2 A Comparative analysis of Kenya and selected comparators

1.3.2.1 FDI competitiveness index

Table 3 compares Kenya's competitiveness index in four areas (economic activity, economic freedom, business environment, and infrastructure) with those of selected countries. The two Asian countries are ranked much higher than Kenya. Mauritius and Rwanda are also ranked better than Kenya. Except for infrastructure, Ghana too is placed above Kenya.

Table 3: FDI Competitiveness Index 2011

Country/Economy	Determinants groupings					
	Economic Activity (GDP per Capita in US$)1*	Economic Freedom (2011)2**		Business Environment	Infrastructure 3***	
		Index	Rank/144	Rank	Score	Rank
S. Korea	22,424	7.48	33	9	5.94	9
Malaysia	9,977	6.97	68	13	5.22	26
Mauritius	8,755	7.93	8	20	3.33	54
S. Africa	8,070	6.72	85	40	4.02	62
Morocco	3,054	6.42	102	98	3.95	69
Ghana	1,570	6.96	70	65	2.84	110
Nigeria	1,502	6.04	119	131	2.21	135
Kenya	808	6.85	77	122	3.10	103
Rwanda	583	7.30	48	53	3.20	101
Mozambique	533	5.41	133	134	2.57	123
Tanzania	532	6.37	105	146	2.41	130

Uganda	487	7.24	52	121	2.49	128
Ethiopia	357	5.65	129	128	2.64	120

Source: 1* World Bank, 2011; 2 ** Economic Freedom Data; 3*** World Competitiveness Report 2012; **http://www.freetheworld.com/datasets_efw.html**

1.3.2.2 Inward FDI potential index

Table 4 shows Kenya's ranking in four economic determinants groupings (market attractiveness, availability of low-cost labour and skills, enabling infrastructure, and presence of natural resources) vis-à-vis selected countries. Overall, Kenya was ranked 98th out of 183 countries, beating only Mozambique, Mauritius, Ethiopia, Uganda, and Rwanda.

Table 4: Inward FDI Potential Index 2011

Selected Country Rankings by Inward FDI Potential Index, 2011					
	Economic determinants groupings				
Country/Economy	**Market attractiveness**	**Availability of low-cost labour and skills**	**Enabling infrastructure**	**Presence of natural resources**	**Overall rank out of 183**
S. Korea	10	5	13	28	4
Malaysia	19	15	53	33	26
S. Africa	54	30	76	15	34
Nigeria	46	-	127	18	53
Morocco	73	55	85	39	69
Ghana	60	42	119	66	73
Tanzania	86	45	150	63	91
Kenya	104	40	142	82	98
Mozambique	116	-	144	59	103
Mauritius	87	75	41	157	110
Ethiopia	78	29	175	115	112
Uganda	98	-	157	107	132
Rwanda	111	-	151	139	144

Source: Adapted from UNCTAD (www.unctad.org/fdistatistics), Web table 32a.

1.3.2.3 Inward FDI performance index

Kenya's ranking vis-à-vis selected countries is shown in Table 5.Due to problems in comparing FDI inflow data, care should be exercised in treating Inward FDI Performance Index as an indicator of countries inward FDI positions. Tax havens will tend to show massive inflows in relation to the size of their economies. Some countries could also have lumpy inflows for short periods, say because of newly discovered resources, mega mergers and acquisitions involving foreign investors or large privatizations. Economies that have been relatively isolated from international capital flows and have recently opened up may also get a substantial wave of FDI inflows. Even countries with steady FDI inflows may change ranks if their share in global GDP changes.

Table 5: Inward FDI Performance Index 2011

Country	World FDI Performance Index Ranking	GDP (billion US $)	FDI Inward Stock (million US $)	FDI Outflows (million US $)	FDI Inflows (million US $)
Ghana	11	32.1748*	9,098	7.86	3222.25
Mozambique	19	9.2094*	5,489	-3.38	2,093.47
Uganda	41	17.1974*	5,853	00	792.26
Malaysia	46	246.8210*	101,339	15,257.52	11,966.01
Tanzania	59	22.9150*	9,966	00	1,095.40
Nigeria	61	228.6379*	60,327	-824.00	8,915.00
Morocco	101	90.8029*	2,023	247.47	2,519.11
Rwanda	118	5.6245*	435	00	106.00
Ethiopia	120	26.5753*	4,102		206.09
Mauritius	121	9.7057*	592	88.55	273.39
S. Korea	122	1,014,890*	127,047	20,354.90	4,660.90
South Africa	128	363.5232*	132,396	-634.89	5,807.36
Kenya	129	32.1982*	2,262	9.43	335.25

Source: Adapted from UNCTAD (www.unctad.org/fdistatistics), July, 2011, Global Finance-2013, * World Bank Estimates, 2010.

A comparison of Tables 4 and 5 shows that Inward FDI performance index for Kenya was less than the country's Inward potential index in 2011. Out of 183 countries, Kenya was ranked number 98 and 129 with respect to its Inward FDI potential index and Inward FDI performance index, respectively. Thus, Kenya was unable to attract as much FDI as her actual potential would suggest.

1.3.2.4 Global competitiveness index

According to the Global Competiveness Report (2012-2013 and 2013-2014) Kenya was ranked 96th with a score of 3.85 in 2013-2014 compared to 106th with a score of 3.75 in 2012-2013 and 102nd with a score of 3.82 in 2011-2012, showing a relatively steady poor performance (Tables 6a and 6b).

In the 2012 – 2013 GCI report, Kenya's strengths were found in the more complex but less important areas measured by the GCI. Kenya's innovative capacity was ranked an impressive 50th, with high company spending on R&D and good scientific research institutions that collaborate well with the business sector in research activities. Supporting this innovative potential is an educational system that -- although educating a relatively small proportion of the population compared with most other countries -- got relatively good marks for quality (37th) as well as for on-the-job training (62nd). The economy is also supported by financial markets that are well developed by international standards (24th) and a relatively efficient labour market (39th). On the other hand, Kenya's overall competitiveness was held back by a number of factors. Health was an area of serious concern (115th), with a high prevalence of communicable diseases contributing to the low life expectancy of less than 57 years and reducing the productivity of the workforce. The security situation in the country was also worrisome (125th) (Global Economic Report, 2013).

Table 6a: The Global Competitiveness Index Data for Kenya, Mauritius and Malaysia (2012/13)

	Kenya		Mauritius	Malaysia
Summary	Rank / 144	Score / 7	Score / 7	Score / 7
GCI 2012–2013	106	3.75	(54) 4.4	(25) 5.1
GCI 2011–2012 (out of 142)	102	3.82	(54) 4.3	(21) 5.1
GCI 2010–2011 (out of 139)	106	3.6	(55) 4.3	(26) 4.9
Indicators				
Basic requirements (60.0%)	**123**	**3.6**	**4.35**	**5.06**
Institutions	106	3.4	4.59	4.94
Infrastructure	103	3.1	4.32	5.09
Macroeconomic environment	133	3.4	4.41	5.34
Health and primary education	115	4.6	5.85	6.16
Efficiency enhancers (35.0%)	**76**	**4.0**	**4.14**	**4.89**
Higher education and training	100	3.6	4.29	4.83
Goods market efficiency	93	4.1	4.80	5.16
Labour market efficiency	39	4.6	4.38	4.82
Financial market development	24	4.7	4.65	5.44
Technological readiness	101	3.3	3.98	4.31
Market size	75	3.5	2.74	4.78
Innovation and sophistication factors (5.0%)	**56**	**3.7**	**3.63**	**4.70**
Business sophistication	67	4.0	4.30	5.02
Innovation	50	3.4	2.95	4.38

Adapted from: The Global Competitiveness Report 2012-2013

Tables 6a and 6b show data on global competitiveness indices for Kenya, Mauritius, and Malaysia in the 2012/2013 and 2013/2014,respectively.These two countries have better indices than Kenya. They also attract more FDIs than Kenya (Table 1).

Table 6b: The Global Competitiveness Index Data for Kenya, Mauritius and Malaysia (2013/14)

	Kenya		Mauritius	Malaysia
Summary	Rank /144	Score / 7	Score / 7	Score / 7
GCI 2013–2014	96	3.85	(45) 4.45	(24) 5.03
GCI 2012–2013	106	3.75	(54) 4.4	(25) 5.1
GCI 2011–2012 (out of 142)	102	3.82	(54) 4.3	(21) 5.1
Indicators				
Basic requirements (60.0%)	**121**	**3.76**	**4.97**	**5.37**
Institutions	88	3.62	4.58	4.85
Infrastructure	102	3.24	4.44	5.19
Macroeconomic environment	132	3.64	5.82	5.35
Health and primary education	119	4.52	6.01	6.10
Efficiency enhancers (35.0%)	**73**	**4.0**	**4.18**	**4.86**
Higher education and training	103	3.54	4.32	4.68
Goods market efficiency	80	4.21	4.85	5.23
Labour market efficiency	35	4.62	4.45	4.79
Financial market development	31	4.68	4.73	5.45
Technological readiness	89	3.36	3.90	4.17
Market size	79	3.58	2.80	4.87
Innovation and sophistication factors (5.0%)	**53**	**3.83**	**3.76**	**4.70**
Business sophistication	61	4.09	4.40	5.02
Innovation	46	3.57	3.11	4.39

Adapted from: The Global Competitiveness Report 2013-2014

Once again in the 2013 -2014 GCI report, Kenya's strengths are found in the more complex areas measured by the GCI which account for only 5 percent of the weighting in ranking. Kenya performs relatively poorly in the basic requirement areas such as institutions, infrastructure, macroeconomic environment and health and primary education which account for 60 percent of the weighting.

1.3.2.5 Economy rankings

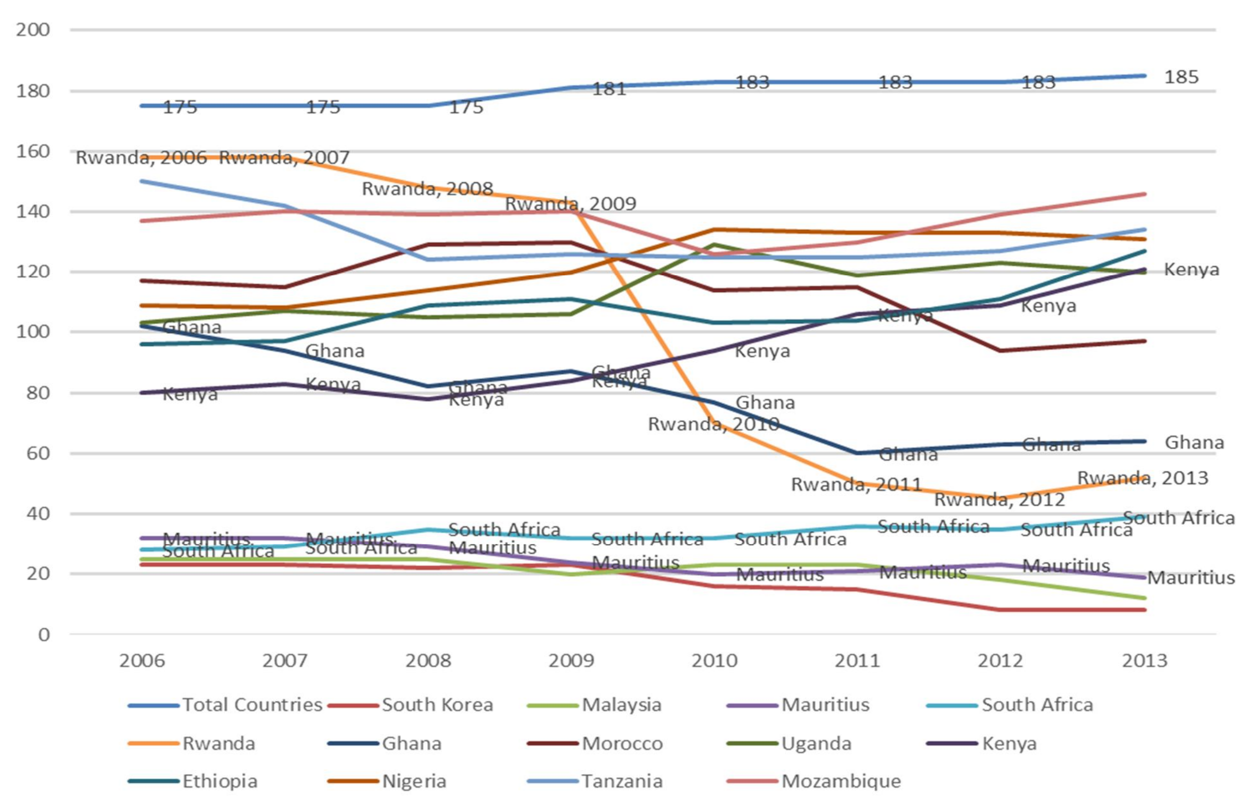
The Figure 2 shows Kenya's rankings in provision of a conducive business environment as ranked by the World Bank using ten parameters for evaluating the ease of business over the period 2006-2013.

Kenya has made significant strides to improve the business environment by making reforms, particularly: streamlining business licensing; abolishing some licenses and introducing single business permits; reducing time to build warehouses; improving access to credit; and improving tax collection (however, tax collection measures have also created additional administrative burdens on the entrepreneurs). Other countries such as Mauritius, South Africa, Rwanda and Ghana have made significant efforts to maintain or improve favourable business environment. Specifically, Rwanda, which until 2009 had lower ranking compared to Kenya, undertook steady reforms and has since 2010 overtaken Kenya in terms of ease of doing business. Doing Business Report (2010) notes that Rwanda has steadily reformed its commercial laws and institutions since 2001.

It is worth noting that despite the efforts made so far, Kenya's business operating environment still fails to offer the necessary and sufficient key safeguards and security needed for lowering the risks to business investments. Furthermore, while the "Single Business Permits" were introduced as a strategy for improving the business environment, reforms in institutional architecture and coordination still lag other reforms and many institutions with regulatory mandates in Kenya still operate in silos.

Kenya's ranking has been sliding over the years. However, this should be viewed in proper context. A close look at the indicators that are used in determining global rankings in terms of ease of doing business shows there are fundamental differences between Kenya and her comparators. It may not be true that Kenya is a non-reformer. She chooses areas in which to reform. For example, Kenya is among the leading countries in the more sophisticated reforms. For instance, it is one of the leading countries in the financial sector reform (Table 7).

Figure 2: Comparison of Selected Countries by Ease of Doing Business 2006-2013



Adapted from: World Bank Doing Business Reports, 2006; 2007; 2008; 2009; 2010; 2011; 2012; 2013

Kenya does well only in getting credit and dealing with construction permits where it is ranked 12th and 45th, respectively. The lowest rankings are in the area of paying taxes, getting electricity, and registering property where the country is ranked number 164th, 162nd, and 161st, respectively, globally. Thus, Kenya is perceived as an expensive location for doing business (bureaucracy, cumbersome regulatory framework, insecurity, weak infrastructure, high energy costs, corruption, multiple taxation regimes, limited access to affordable finance, ICT not fully developed, and high cost of labour not matched with productivity). The country needs to focus on some of the so called soft reform areas if it is to improve its global standing in ease of doing business.

Michael J. Harrison (2011) established that, overall the least-corrupt countries attract a significantly larger amount of FDI inflows compared to the most-corrupt countries. The World Economic Forum and The International Finance Corporation (2008) attribute Kenya's loss of competitiveness in attracting foreign investment to corruption, crime and theft, inadequate infrastructure, inadequate protection of investors, and weak enforcement of contracts amongst others.

Table 7: Kenya's Ranking in Ease of Doing Business Indicators, 2013

Indicator	Global Ranking
Paying Taxes	164
Getting Electricity	162
Registering Property	161
Enforcing Contracts	149
Trading Across Borders	148
Starting a Business	126
Protecting Investors	100
Resolving Insolvency	100
Dealing with Construction Permits	45
Getting Credit	12
Overall Ease of Doing Business	**121**
World Ranking	**122**

Source: World Bank, Doing Business Report, 2013

1.3.3 Why Kenya's global ranking is sliding

There are a number of plausible reasons for this:

a. Perhaps other countries are reforming faster;
b. May be the indicators used do not fully capture areas where Kenya is doing well;
c. Kenya is reforming broadly while others may be focusing on reforms that matter most to potential foreign investors (for example, it takes about a month to incorporate a business in Kenya compared to one day in Rwanda);
d. Kenya has been doing the harder reforms (for example, creating a robust financial system; thinking in terms of a virtual -electronic- one-stop shop instead of a physical a one-stop shop); and
e. Other countries are reforming faster than Kenya.

1.4 Policy Implications

The recommendations for improving the FDI climate include upgrading infrastructure; addressing corruption and governance issues; easing constraints to setting up and doing business; developing human capital; legislating wage policy; ensuring stable macroeconomic and political climate; and improving quality and effectiveness of institutions for promoting FDI.

Infrastructure development - The government should continue with its effort to improve both the quantity and quality of infrastructure in the areas of transport and communication (including ICT) and energy to address the supply-side constraints such as high internal transport and energy costs –factors that have caused some factories to relocate to some neighbouring countries.

Corruption and governance - The government should reduce corruption and poor governance by strengthening the Anti-corruption body with the necessary powers to execute its functions.

Setting up and doing business – The government should cut down red tape; simplify procedures to register a property; reduce stamp duty; eliminate or privatize inspection and valuation of property; reduce the time to declare bankruptcy; and increase recovery rate of closing a business.

Human resource - The government should develop human resource required for investment and should support the creation of culture of science, technology and innovation.

Wage policy and legislation - The government should tighten the wage policy so that the minimum wages for skilled employees are maintained high and in line with comparator countries. It should also revise labour legislation on hiring and firing to favour local skilled employees and assess the appropriate training needs for the various sectors to ensure that training complements employment/maintenance of skilled local employees in FDIs.

Stable macroeconomic and political climate - The Government should pursue sound macro-economic policies to encourage FDI. These include installing flexible and stable exchange rates and maintaining low and stable inflation rates. Additionally, the government should also ensure peace and political stability to attract FDI inflows.

Quality and effectiveness of institutions for promoting FDI - The country should improve degree of property rights protection and bureaucratic efficiency, improve the efficiency and integrity in the civil service, reduce crime rate, and improve efficiency and peace in the dispute resolution and delivery of justice to attract more FDI.

Kenya may need to focus on simpler things/reforms, for example, simplifying procedures/processes for starting a business; business licensing procedures; and procedures required for selling land.

References

1. Basemera, S., *et al* (September 2012). Foreign Direct Investment Inflows to East Africa: Do Institutions Matter? Journal of Business Management and Applied Economics, Issue 5.
2. Gagaya H. and G. Lipimile (2008). The Effects of Anti-competitive Business Practices on Developing Countries and their Development Prospects, New York and Geneva, UNCTAD.
3. Government of the Republic of Kenya (2007). Kenya's Vision 2030, Nairobi, Government Printer.
4. Government of the Republic of Kenya (2008). First Medium Term Plan (2008-2012), Kenya Vision 2030, A Globally Competitive and Prosperous Kenya, Nairobi, Government Printer.
5. Government of the Republic of Kenya (2013). Second Medium Term Plan (2013-2017), Kenya Vision 2030, Transforming Kenya: Pathway to Devolution, Socio-economic Development, Equity and National Unity, Nairobi, Government Printer.
6. Harrison, Michael J. (2011). Can Corrupt Countries Attract Foreign Direct Investment? A Comparison of FDI Inflows between Corrupt and Non-Corrupt Countries, Southern New Hampshire University.
7. Mwega, F. M. and Ngugi. R. W., (2007). "Foreign Direct Investment in Kenya" in Ajayi, S. I. (ed.), Foreign Direct Investment in Sub Saharan Africa: Origins, Targets, Impact and Potential, Africa Economic Research Consortium, Nairobi.
8. Rwanda Development Board: Investor Info Pack, www.rdb.rw
9. The Financial Times, The FDI Report (2013). Global Greenfield Investment Trends, FDI Intelligence.
10. UNCTAD (2005). World Investment Report 2005, Transnational Corporations and Internationalization of R&D, New York and Geneva
11. UNCTAD (2011).World Investment Report 2011, Non-equity Modes of International Production and Development, New York and Geneva.
12. UNCTAD (2012). World Investment Report 2012, Towards a New Generation of Investment Policies, New York and Geneva.
13. UNCTAD, in the World Investment Report (WIR), Geneva, 2012
14. UNCTAD, World Investment Report, New York and Geneva, U.N., 2013.
15. World Bank (2006). Snapshot Africa: Benchmarking FDI Competitiveness in Sub-Saharan African Countries, Washington, DC, World Bank.
16. World Bank (2007). Snapshot Africa – Kenya; Benchmarking FDI Competitiveness, Washington, DC, World Bank.
17. World Bank (2010). Doing Business Report 2011: Making a Difference for Entrepreneurs, Washington, DC, World Bank.
18. World Bank (2011). Doing Business Report 2012: Doing Business in a More Transparent World, Washington, DC, World Bank.
19. World Bank (2012). Doing Business Report 2013, Washington, DC, World Bank.

20. World Bank (2012). Global Investment Promotion Best Practices, Washington, DC, World Bank.
21. World Bank (2013). Reforming Business Registration Tool Kit, Washington, DC, World Bank.
22. World Bank (209). Doing Business Report 2010: Reforming Through Difficult Times, Washington, DC, World Bank.
23. World Bank (2012). Doing Business Report 2013: Smarter Regulations for Small & Medium-Size Enterprises, Washington, DC, World Bank.
24. World Bank (2012). Global Investment Promotion Best Practices, Washington, DC, World Bank.
25. World Bank (various years). World Development Report, Washington, DC, World Bank.
26. World Economic Forum (2013). The Global Competitiveness Report 2012-2013, Geneva, World Economic Forum.
27. World Economic Forum (2014). The Global Competitiveness Report 2013-2014, Geneva, World Economic Forum.
28. World Economic Forum 2012, (September 1, 2012). The Global Competitiveness Index 2012–2013, Geneva, Switzerland.
29. Xavier Sala-i-Martín, *et al* (World Economic Forum, 2014). The Global Competitiveness Report 2013-2014, Geneva, World Economic Forum.