



**Challenges, opportunities, and prospects for Kenyan private sector in the manufacturing sector**

**National Training Workshop on Fostering Productive Capacities in Kenya for Industrialization, Export Diversification, and Inclusive Growth**

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# Outline of the presentation

- ❖ About KAM
- ❖ A highlight of key macroeconomic variables with implications on manufacturing sector
- ❖ State of manufacturing industry in Kenya
- ❖ A highlight of challenges derived from the Manufacturing Priority Agenda (MPA) 2022
- ❖ Opportunities in manufacturing
- ❖ Conclusion

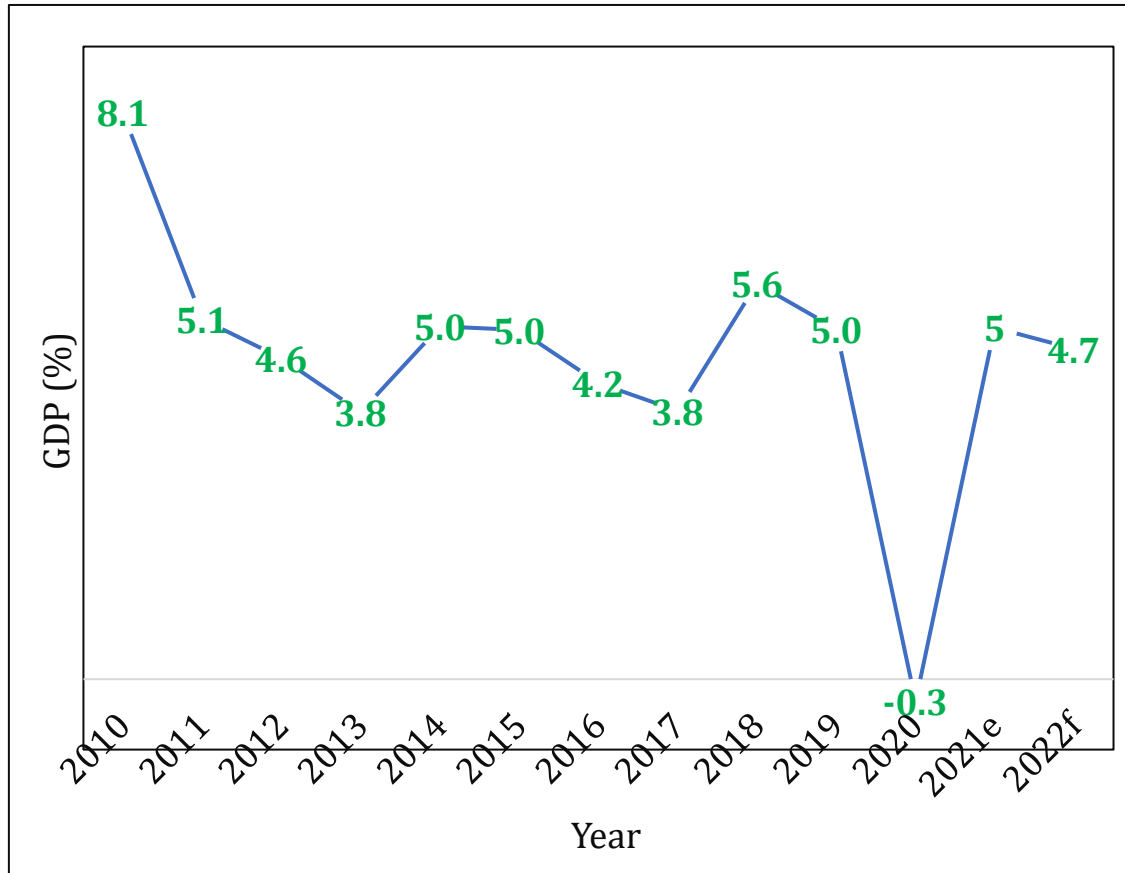
# About KAM



- ❖ KAM is the representative organization for manufacturing value-add industries in Kenya, comprising of more than 1000 members, cut across 14 sectors
- ❖ Established in 1959
- ❖ Carries out fact-based policy advocacy
- ❖ KAM promotes trade and investment, upholds standards, encourages the formulation, enactment and administration of sound policies
- ❖ Mission-to promote competitive and sustainable local manufacturing

# Key macroeconomic variables

## Kenya's economic outlook (GDP growth (%))

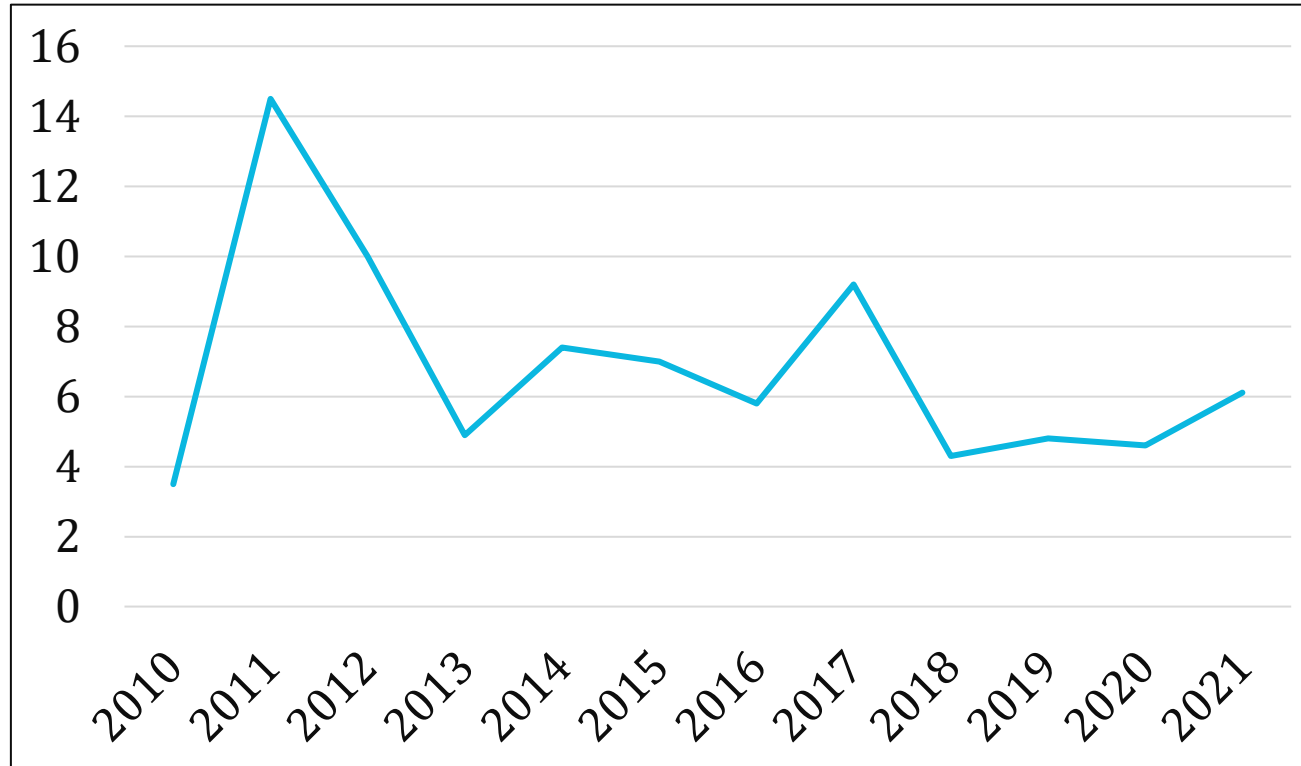


Data source: Economic Surveys (various) &  
World Bank's Global Economic Prospects 2022

- ❖ Kenya economy contracted by 0.3% in 2020 because of COVID-19 pandemic and is projected to grow by 4.7% in 2022 (World Bank estimates)
- ❖ A Key feature of Kenya's GDP growth is that it is episodic
  - ❖ East Asian growth miracle has proved that a robust manufacturing industry ensures long-term and sustainable economic growth

# Key macroeconomic variables...

## Annual average inflation rate (%)



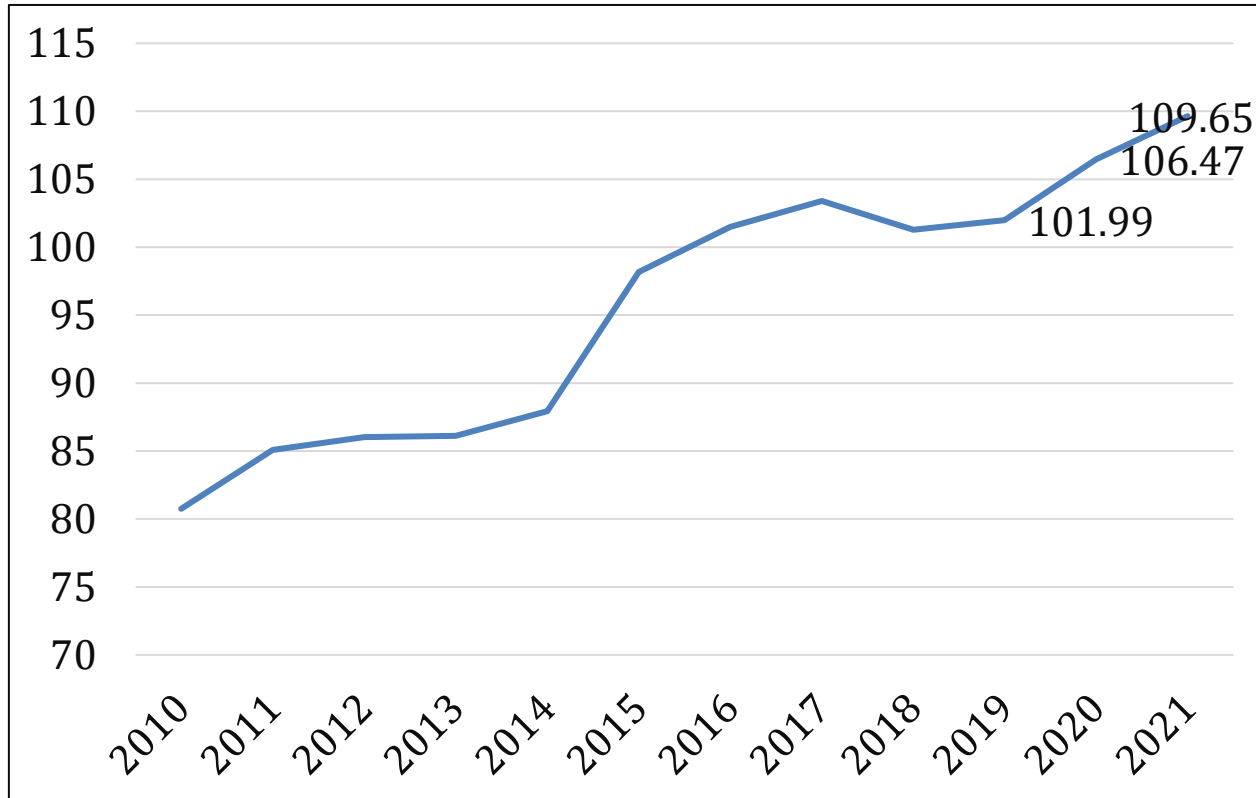
*Data source: Economic Surveys (various)*

*Note: 2021 data was averaged from KNBS's monthly CPI and inflation rates reports*

❖ Inflation has implications on the purchasing power

# Key macroeconomic variables...

## Exchange rate (Ksh/US\$)



*Data source: Economic Surveys (various)*  
*Note: 2021 was averaged using CBK data*

❖ Ksh. depreciated by about 7.51% against the US\$ between 2019 and 2021

❖ Depreciation of Ksh. negatively impacts the manufacturing sector because of its heavy reliance on imported raw materials and intermediate inputs for processing and capital goods for investment

# Key macroeconomic variables...

## Fiscal deficit inclusive of grants as a % of GDP

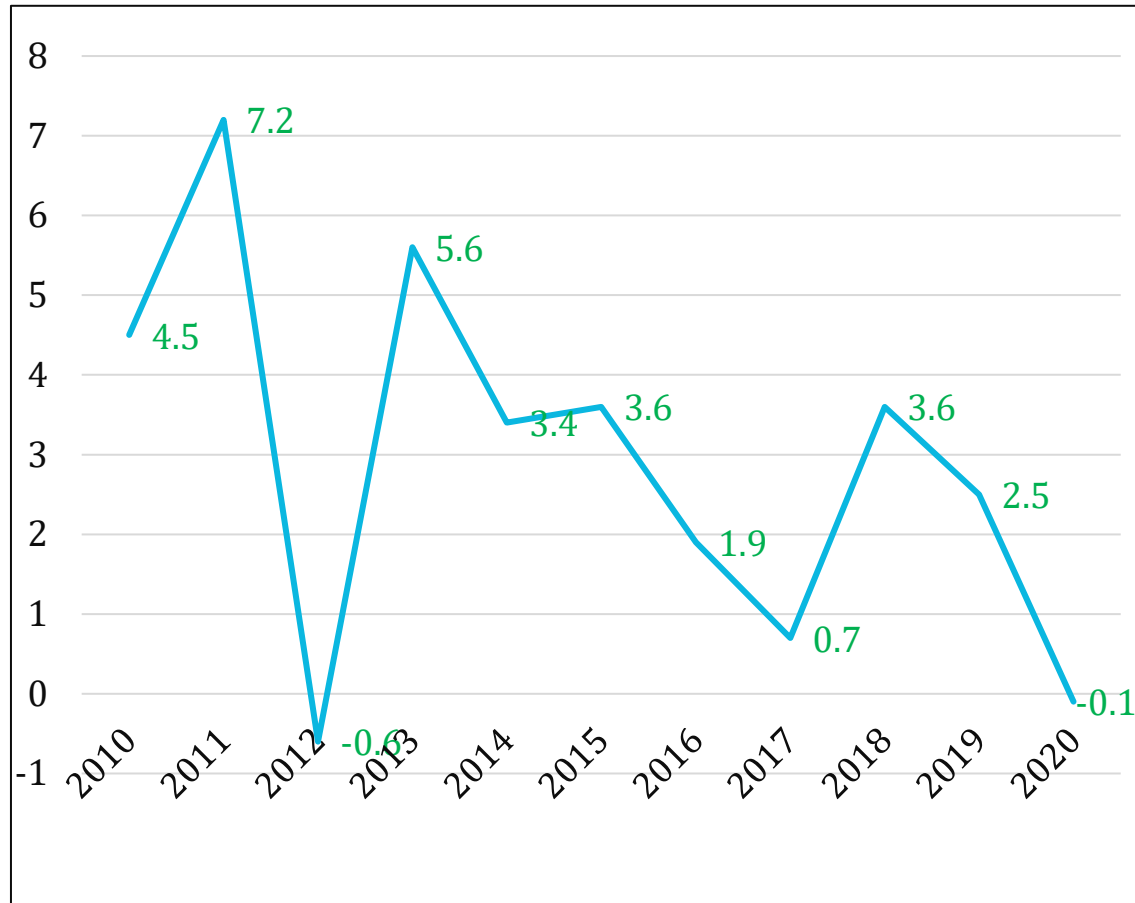
2016/17	2017/18	2018/19	2019/20	2020/21	2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
Actual	Target	Actual	Target	Actual	Target	Actual	Target	Actual	Target	Target
(8.9)	(10.9)	(6.8)	(7.2)	(7.7)	(7.6)	(8)	(9)	(8.6)	(9.4)	(7.7)

*Data source: Budget Review and Outlook Paper*

- ❖ Fiscal deficit as a % of GDP is usually used as a proxy for fiscal discipline of a country
- ❖ 7.7% is the fiscal deficit target for 2021/22
- ❖ Large fiscal deficits have the potential to disrupt the general macroeconomic environment
- ❖ Fiscal deficit and its effect on the overall stock of public debt (Ksh. 7.71 trillion by June 2021) matter to the private sector:
  - ❖ Likely to lead to increased taxation-evidenced by reduction of fiscal incentives (tax expenditure)
  - ❖ Increased domestic borrowing by the government crowding out the private sector
  - ❖ It can be inflationary if the government prints money to fund the deficit

# State of manufacturing industry in Kenya

## Manufacturing sector growth (%)



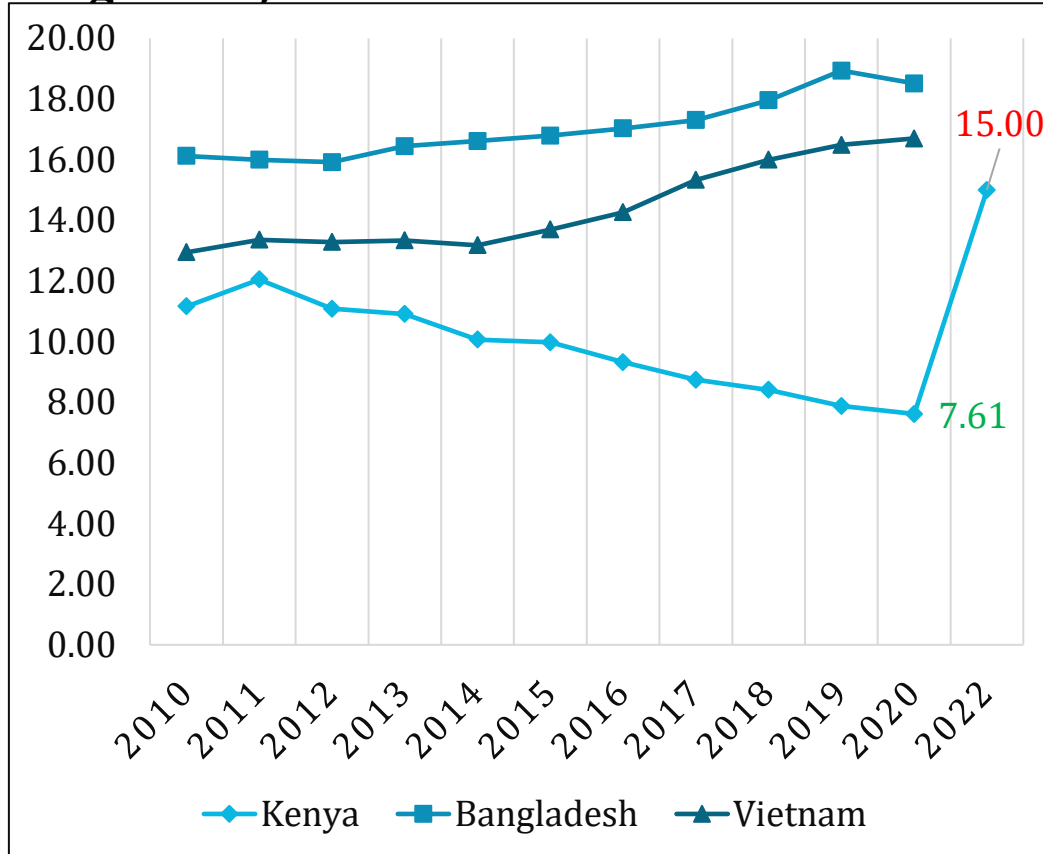
Data source: Economic Surveys (various)

- ❖ Manufacturing sector growth contracted by 0.1% in 2020 because of the impact of COVID-19 pandemic



# State of manufacturing industry in Kenya...

## Manufacturing GDP contribution (%) for Kenya, Bangladesh, and Vietnam



Data source: World Development Indicators

- ❖ Massive growth is required for manufacturing sector GDP contribution to reach 15% as desired under the Big Four Agenda
- ❖ Bangladesh has been hugely successful in producing ready-made garments (RMG) which constitutes about 84% of total exports making it the second largest exporter of RMG after China
- ❖ Smartphone is the leading export commodity for Vietnam and earned US\$45 billion in 2017
- ❖ Even through both Bangladesh and Vietnam have governance challenges and have one-engine driven manufacturing sector, they are a prove that industrialization is possible

# A highlight of challenges

<b>Pillar 1: Competitiveness and level playing field</b>		
<b>Agenda:</b>	<b>Actions</b>	<b>Remarks</b>
Improving regulatory efficiency	<ul style="list-style-type: none"> <li>i. Realignment of existing fees, charges and levies imposed by various government agencies and regulatory bodies.</li> <li>ii. National Government agencies and County Governments create sharing platforms to facilitate compliance and reduce costs for businesses.</li> </ul>	<ul style="list-style-type: none"> <li>❖ Regulations become disruptive when they are many, which in turn increases the cost of compliance</li> <li>❖ A review and alignment of overlapping mandates and roles will reduce the cost of doing business by about 28.9%</li> </ul>
Promote access to quality, affordable and reliable energy for manufacturing	<ul style="list-style-type: none"> <li>i. Implementation of recommendations contained in the Presidential Taskforce Report on electricity costs</li> <li>ii. Fast track finalization of regulations for Energy Act 2019</li> <li>iii. Review pre-conditions for Time of Use Tariff to cover all night consumption and lock in the rate for each facility</li> </ul>	<ul style="list-style-type: none"> <li>❖ Electricity is a major input in the manufacturing process</li> <li>❖ It is estimated that for example in the Metal Sector, electricity accounts for 40-50% of total conversion cost</li> </ul>

# A highlight of challenges ...

## Pillar 1: Competitiveness and level playing field

Agenda:	Actions	Remarks
Reduce transport and logistics costs	<ul style="list-style-type: none"> <li>i. Sustain an efficient and seamless movement of containers at the ports by enhancing the existing collaborative and coordination frameworks with port stakeholders</li> <li>ii. Review the KPA 4 days free clearance period to 6 days in line with average dwell time to reduce cost of clearance</li> <li>iii. Simplify and promote Authorized Economic Operator (AEO) accreditation processes to increase its uptake for enhanced import and export clearance processes</li> <li>iv. Create framework between roads agencies and County Governments to enhance industrial road upgrading and maintenance</li> </ul>	<ul style="list-style-type: none"> <li>❖ There are inefficiencies within the SGR system that increases costs:               <ul style="list-style-type: none"> <li>○ Delayed transfer of containers from Mombasa to Nairobi Inland Container Depot</li> <li>○ High dwell time on account of poor coordination of Government Agencies</li> <li>○ High storage charges, custom warehouse rents, demurrage to shipping lines</li> </ul> </li> <li>❖ The AEO accreditation process by KRA is slow due to:               <ul style="list-style-type: none"> <li>○ Lack mutual recognition of the AEO program by Government Container Intervening agencies</li> <li>○ Lengthy processes and requirements for approval</li> </ul> </li> </ul>

# A highlight of challenges ...

## Pillar 1: Competitiveness and level playing field

Agenda:	Actions	Remarks
Lower the cost of industrial inputs	<ul style="list-style-type: none"> <li>i. Industrial machinery and spare parts of Chapters 84 &amp; 85 to attract Import Declaration Fee (IDF) rate of 1.5%</li> <li>ii. Industrial machinery and spare parts of Chapters 84 &amp; 85 to attract a Railway Development Levy (RDL) rate of 1.5%</li> <li>iii. Allow manufacturers to offset “inputs” as part of the relief that is provided to manufacturers under Section 14 of the Excise Duty Act 2015</li> </ul>	<ul style="list-style-type: none"> <li>❖ Industrial machinery and spare parts of Chapters 84 &amp; 85 attract IDF and RDL rate of 3.5% and 2%, respectively</li> <li>❖ IDF is waived for all manufacturers in the region except Kenya</li> <li>❖ There is no RDL in Tanzania while Uganda has an equivalent infrastructure development levy (IDL) of 1.5% customs value on all imports</li> <li>❖ Clearly, manufacturers in Kenya have a cost disadvantage relative to EAC Partner States</li> <li>❖ The government has been introducing excise duty on inputs used in the manufacturing process e.g., articles of plastics</li> </ul>

# A highlight of challenges ...

<b>Pillar 1: Competitiveness and level playing field</b>		
<b>Agenda:</b>	<b>Actions</b>	<b>Remarks</b>
Sustain the fight against illicit trade	<ul style="list-style-type: none"> <li>i. Advocate for/and harmonize intellectual property rights within the EAC Region for purposes of protection and enforcement against intellectual property rights (IPR) infringement within the region.</li> <li>ii. Enhance inter agency collaboration, co-ordination, accountability, and transparency in the enforcement against illicit trade</li> </ul>	<ul style="list-style-type: none"> <li>❖ Kenya has registered progress in the fight against illicit trade and more can be realized through collaborative efforts between Ministries, Departments, and Agencies</li> <li>❖ The same can be replicated in EAC</li> </ul>
Address multiple county charges, fees, and levies	<ul style="list-style-type: none"> <li>i. Development of County Tariffs and Pricing Policy</li> <li>ii. Reintroduction of County Government Revenue Raising Regulation Process Bill that provides mechanisms for harmonization of county levies, fees, and charges by the County Governments.</li> <li>iii. Development of county competitiveness index</li> </ul>	<ul style="list-style-type: none"> <li>❖ Devolution has made it more expensive to do business as county levies and charges are responsible for 45.8% of all charges</li> <li>❖ Formulation of the Tariffs and Pricing Policy and supporting legislation to guide predictable imposition of levies, fees and charges is a legal requirement under Section 120 of the County Governments Act, 2012</li> <li>❖ The County Own Source Revenue Raising (COSRR) Bill was to create an interagency committee to review County levies, fees, and charges before introducing them in the financial planning and budgeting cycle                             <ul style="list-style-type: none"> <li>❖ The Bill lapsed in December 2019</li> </ul> </li> </ul>

# A highlight of challenges ...

<b>Pillar 2: Enhance market access</b>		
<b>Agenda:</b>	<b>Actions</b>	<b>Remarks</b>
Enhance local market access	<ul style="list-style-type: none"> <li>i. Fasttrack finalization of the local content policy for which an implementation committee was formed</li> <li>ii. Increase Kenya Trade Remedies Agency's capacity to conduct investigations and enforcement of anti-dumping laws</li> <li>iii. Monitor and evaluate the implementation of the local content framework and the BKBK strategy by the various Ministries Departments &amp; Agencies (MDAs) vs the gazetted list of locally manufactured goods by the Ministry of Industrialization</li> </ul>	<ul style="list-style-type: none"> <li>❖ Preferential public procurement is increasingly becoming a popular tool to promote consumption of locally manufactured goods</li> <li>❖ KETRA is operational but requires capacity enhancement to discharge its mandate effectively</li> </ul>
Promote regional market access	<ul style="list-style-type: none"> <li>i. Adopt 35% as the 4th tariff band and ensure conclusion of the comprehensive review of EAC Common External Tariff (CET) by end of June 2022</li> <li>ii. Fast track the finalization and implementation of the EAC NTB Act amendments and development of the regulations</li> <li>iii. Fasttrack finalization of the outstanding issues on the Tripartite Free Trade Area (TFTA) and Continental Free Trade Area (AfCFTA)</li> </ul>	<ul style="list-style-type: none"> <li>❖ 35% as the rate for the 4th tariff band will:</li> <li>❖ Promote industrialization</li> <li>❖ A 10% tariff differential between the 3<sup>rd</sup> and 4<sup>th</sup> tariff band will incentivize industrial investments</li> <li>❖ Only affect 8% of total tariff lines and these are goods abundantly produced in EAC</li> </ul>
Diversify international market access	<ul style="list-style-type: none"> <li>i. In the US Kenya FTA negotiations Kenya to propose for flexible and competitive rules of origin</li> <li>ii. Fastrack implementation of the Kenya EU Economic Partnership Agreement (EPA)</li> </ul>	<ul style="list-style-type: none"> <li>❖ The US is the 4<sup>th</sup> Kenya's export destination especially for apparels and textiles from Export Processing Zones (EPZs)</li> <li>❖ Manufacturers who export to the EU require uninterrupted market access</li> </ul>



# A highlight of challenges ...

## Pillar 3: Pro-industry policy and institutional framework

Agenda:	Actions	Remarks
Ensure certainty and predictability of tax policies to encourage industrial	i. Finalize and implement the proposed National Tax Policy	<ul style="list-style-type: none"> <li>❖ The policy should:                             <ul style="list-style-type: none"> <li>❖ Enhance certainty and predictability-changes to be made after every 5 years to create</li> <li>❖ Reduce the number of taxes</li> <li>❖ Reduce the level of taxation</li> <li>❖ Transition clauses for new taxes</li> </ul> </li> </ul>
	i. Revert Investment Deduction Allowance to 100%/150%	❖ This will promote industrialization in the rural areas
	i. VAT exemption on plant and machinery of Chapter 84 and 85 used for manufacture of goods ii. Limitation of interest deduction to 30% of Earnings Before Interest Tax, Depreciation and Amortization (EBITDA) should be amended	<ul style="list-style-type: none"> <li>❖ Kenya is capital poor and must rely on imports</li> <li>❖ Assume a manufacturer imports a machine worth Ksh. 200 million if you add: 16% VAT; IDF (3.5%); RDL (2%); average exchange rate depreciation for 2021 (3%)                             <ul style="list-style-type: none"> <li>○ This adds up to 24.5% or Ksh. 49 million extra cost excluding and logistics cost to the destination</li> </ul> </li> <li>❖ EBITDA provisions will increase the cost of financing manufacturing investment which is capital intensive</li> <li>❖ Clearly, these tax policies do not encourage manufacturing investment</li> </ul>

# A highlight of challenges ...

<b>Pillar 4: SMEs development</b>		
<b>Agenda:</b>	<b>Actions</b>	<b>Remarks</b>
Create a favorable policy environment for SMEs to flourish	i. Fast track the implementation of the MSE policy launched by the government in 2021	<ul style="list-style-type: none"> <li>❖ MSE accounts for 24% of GDP, over 90% of private sector enterprises and 93% of total labour force in the economy</li> <li>❖ MSE policy addresses the main challenges impeding growth of MSEs such as:                             <ul style="list-style-type: none"> <li>○ Access to finance</li> <li>○ Skills and capacity gaps</li> <li>○ Market access</li> <li>○ Facilitation of start-ups</li> <li>○ Formalization</li> </ul> </li> </ul>



# A highlight of challenges ...

## Pillar 5: Industrial sustainability and resilience

<b>Agenda:</b>	<b>Actions</b>	<b>Remarks</b>
Adoption of KAMs industrial manifesto proposals by political parties and both levels of government	<ul style="list-style-type: none"> <li>i. Adoption of KAMs Industrial manifesto proposals by political parties.</li> <li>ii. Adoption of the industrial manifesto by both levels of government</li> </ul>	❖ The creation of the ‘deliberation council’ as a consultative arrangement linking government, business and civil society is credited as one of the institutional factors underlying the remarkable growth in the East Asian miracle economies
Ensure peaceful 2022 general elections and transition	i. Political candidates to embrace issue-based politics as aspired under Vision 2030	❖ Political pillar under Vision 2030 envisages issue-based politics which the Constitution 2010 attempted to create institutional framework to support the realization this goal

# A highlight of challenges ...

## Pillar 5: Industrial sustainability and resilience

<p><b>Agenda:</b> Pro-industry skill development</p>	<ul style="list-style-type: none"> <li>i. Create a policy framework to allow coordinated formation of sector specific Sector skills advisory committees (SSACs) and harmonization of the same</li> <li>ii. Scale up Competency Based Education and Training (CBET) uptake nationally in TVET institutions</li> </ul>	<ul style="list-style-type: none"> <li>❖ SSACs are important in industry engagement for curriculum development, review, and validation, ensuring industry-led standards are incorporated in the curriculum process</li> <li>❖ CBET has been identified as one way to ensure manufacturing sector is able to get relevant skills that in turn increase industry competitiveness</li> </ul>
<p><b>Agenda:</b> Green growth and sustainable development</p>	<ul style="list-style-type: none"> <li>i. Localize and Implement SDGs Goal No. 12 on Responsible Production and Consumption under circular economy</li> <li>ii. Implement KAM's Plastic Action Plan 2019</li> <li>iii. Create a program for greening of Kenyan industries in line with national policies and global commitments</li> </ul>	<ul style="list-style-type: none"> <li>❖ There is global effort towards green growth and production and Kenya should not be</li> </ul>

# Opportunities in manufacturing

- Impact of COVID-19 pandemic has revealed:
  - The risks associated with overreliance on imported goods including industrial inputs
  - Overreliance on China by global economies
- i. Reshoring of global value chains (GVCs):
  - Need to package Kenya as one of the alternative destination
  - There is need to step up investment promotion efforts
- ii. Support to reshoring efforts, specifically, tracking and authentication advancements:
  - To allow visibility across the supply chain
  - Advanced tracking tools can help prevent counterfeits, stolen goods and mishandling of customer information
- iii. Opportunities for near-shore options to shorten supply chains and increase proximity to customers:
  - What are the opportunities? No answer to this question

# Opportunities in manufacturing...

## iv. Developing domestic value chains:

- Agro-industry value chains
- Adding value to minerals already discovered

## v. Component manufacturing:

- Pharmaceuticals and medical equipment
- Electronics
- Automotive

# Conclusion



If Kenya is to realize high, sustained and inclusive economic growth and development, it requires an **industrialization drive** and everything else will fall into place



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