

Doing Business in KENYA

FINANCIAL TIMES SPECIAL REPORT | Thursday November 25 2010

Inside
The country's reputation for innovation in the area of software and ICT is growing, writes Parselelo Kantai
Page 6



www.ft.com/kenya-2010 | twitter.com/ftreports

Political reform boosts hopes of change

A new constitution has helped east Africa's leading economy move back into gear, write **William Wallis** and **Parselelo Kantai**

It would be premature to suggest Kenya has a clear run to recovery, given the hurdles that remain before it. But in the three months following the adoption of a new constitution by referendum, east Africa's leading economy has at least made a start.

The politics have been shaken up and the economy is rebounding faster than expected from the triple shock of political turmoil, drought and the global downturn. In Nairobi's bars and shopping centres, consumption, heralded as the mark of an expanding middle class, is returning to boom levels not seen since disputed election results tipped Kenya into crisis in 2008.

The first cracks are emerging, too, in a long-standing culture of impunity. On a near daily basis, top officials are exposed for alleged corruption and in several cases have been forced to step aside, as inquiries in parliament and by the Kenya Anti-Corruption Commission take their course.

Investigations by the International Criminal Court in The Hague converge with this trend. ICC prosecutor Luis Moreno-Ocampo last week announced his intention to charge six leading figures before the end of the year for allegedly fuelling the post-election violence, in which 1,200 died.

Revelations about senior officials partly serve to underscore the scale of the rot. If Kenya's aggressive media is to be believed, almost nothing government touches is clean, from the sale of foreign embassy buildings to primary education, which the World Bank and Britain have ceased funding because of graft. Moreover, numerous putative clean-ups have fizzled out. Yet amid the first real signs of movement since international pressure halted Kenya's descent into civil war and imposed a power-sharing entente between feuding politicians, the public mood is shifting from one of anxiety and cynicism to impatience and expectation. After the constitutional referendum went off peacefully, some three-quarters of Kenyans polled expressed optimism about the country's economic future.

"This is a moment of hope. That's genuine," says John Githongo, the former government whistleblower back in Kenya after a period in exile. But it is early days, he warns, and the underlying dynamics have yet to change.

Kenya retains its position as east and central Africa's dominant economy, its main financial, diplomatic and aid agency centre, and a growing entrepot in a region where demand for goods and services outstrips supply.

Should moves towards east African integration consolidate and big regional infrastructure projects get under way, Kenya is in prime position to benefit. Nairobi's mix of financial capital, technological savvy and entrepreneurial flair is already driving businesses past bureaucratic hurdles and across borders.

Yet there can be little doubt, given the depth of frustration exposed in 2008, that the country faces a precarious future, should reforms lose momentum. Kofi Annan, the former secretary-general of the United Nations who brokered the coalition



Popular pressure: voters backing the 'Yes' vote during a rally in a Nairobi park in August

development aid and funding for much-needed infrastructure, including roads, railways and power plants.

A slew of projects is already on the table or under way. These should help tap into regional growth from Uganda, soon to be an oil producer, and the Democratic Republic of Congo and south Sudan.

Constitutions, however, have a mixed record in aiding progress in Africa, partly because autocrats, coup-makers and political conspirators have found it all too easy to ignore them, tear them up or adapt them.

Kenya's constitution, inherited from colonial times, was tinkered with to consolidate power in the presidency and centralise the state. The effect was to minimise accountability and heighten competition for the spoils of office since the reintroduction of multi-party politics in 1991.

The new draft clips presidential powers, reinforces those of the national assembly, and dilutes executive control of provincial government. The representatives of 47 newly created counties will now be elected and receive a statutory share of some 15 per cent of the national budget.

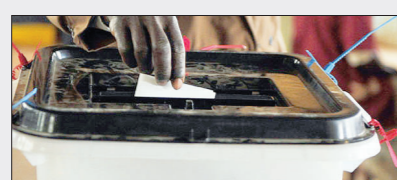
It takes a leap of faith to believe such changes offer renewal in themselves and among Kenya's human rights and civil society activists scepticism abounds. Taken to logical ends, the current clean-up would "leave few cabinet members standing" says Mwalimu Mati, who runs Mars Kenya, a campaigning website. He says only sustained public pressure will keep the governing classes on their toes.

Yet the case for change and popular pressure to achieve it have rarely been stronger or more urgent. As the dominant economy in a region attracting interest from diverse investors, including emerging powers such as China, Kenya has everything to gain.

agreement, warned as much this month, cautioning that the hard bits are still to come.

Demographics tell part of the story. Two-thirds of the population is aged under 30. A paucity of arable land is driving young Kenyans to cities and slums in unprecedented numbers, with more than 500,000 people entering the job market each year to chase barely a 10th as many formal sector jobs.

Economic growth, which peaked in 2007 at 7.1 per cent and is picking up to a forecast 5 per cent this year (driven mainly by services, construc-



Inside this issue

Constitutional reform Ethnic divisions remain a source of instability, writes Parselelo Kantai **Page 2**

Economy Much work is needed improving infrastructure, although mobile telephony is booming, reports William Wallis **Page 3**

Regional focus Land hunger and community strife mean tensions are high, despite new political arrangements, says Michela Wrong **Page 4**

Investment The country is being used as a beach head for FDI, says Andrea Bohnstedt **Page 6**

tion and tourism), has yet to dent the pervasive poverty. According to the UN human development index, an estimated 38 per cent of national wealth is in the hands of 10 per cent of the population, with the poorest 10th controlling only 1.8 per cent. Such inequities stoke crime and exacerbate historic ethnic grievances over land and income distribution.

Similar challenges beset other poor and rapidly changing societies, and in some respects they are less severe in Kenya than elsewhere in the region. What makes the mix so combustible, says David Ndi, an influential economist who contributed to drafting the new constitution, is the willingness of politicians to exploit it, especially at election time. Fixing the political system is a large part of the battle.

Early this year, when political progress was slow, a group of businesspeople sought to chivy government along after a sustained period of infighting and inaction.

During meetings with both President Mwai Kibaki and his former election rival Prime Minister Raila Odinga, they laid out a stark choice of futures. In one, ethnic vigilante groups manned by underemployed youth expand their reach into organised crime and Kenya's parallel worlds of affluence and poverty increasingly collide.

Another future beckons, however, in which improved governance, investment in power and transport infrastructure produce economic expansion closer to double figures, levels at which real inroads can be made in job creation. Some of those present at the meetings date a change of tempo at the top from this time.

Leaving behind recalcitrant lieutenants, Mr Kibaki and Mr Odinga exhibited a rare display of unity when cam-

paigning for the constitution. Should they continue to use the new national law, which on paper strengthens anti-corruption statutes to dismantle the rent-seeking architecture that has

underpinned the postcolonial state – and their own positions – the upside could be great.

Kenya would probably benefit from increased foreign investment flows,

Kenya's First is Africa's Finest.



AFRICAN BUSINESS AWARDS 2010
Telecoms Company of the Year

Thanks to all our subscribers, staff and partners for helping us to be recognized as Telecoms Company of the Year at the 2010 African Business Awards.

www.safaricom.co.ke

Safaricom

Enthusiasm for EAC not matched by results

Integration

Officials finally catch up with their people's fluid view of borders, writes **William Wallis**

Regional integration is fashionable in Africa these days, and politicians, civil servants and foreign donor organisations are adopting it as a cause.

But spend time near any border on the continent, or indeed among businesses and banks, and it is clear that officialdom, far from setting the pace, is merely catching up.

African populations have long treated the porous and artificial borders that were bequeathed by colonial powers with contempt, and wherever possible slipped

back and forth across them undetected with their wares. After a decade of sustained economic growth in much of Africa, big businesses and financial institutions are following the informal sector, looking across borders for expansion.

Until recently the continent's bureaucracies put obstacles in the way. The launch last July of an east African common market should be changing that.

In theory the common market joining the five members of the revived East Africa Community – Kenya, Tanzania and Uganda, Rwanda and Burundi – facilitates the free movement of labour and capital, building on a customs union with common external tariffs in place since 2005.

As the region most advanced on the path to

economic integration, east Africa can provide the continent with a model that responds to an agenda long recognised as central to development prospects.

If African countries traded more among each other, spoke with one voice and strengthened regional co-operation in keeping peace, they would go a long way towards overcoming the political frailties and economic fragmentation associated with their inherited borders.

Member states still have to adapt their national laws to allow full implementation of areas such as immigration, labour and customs. However, trade and business within the region is already growing steadily, with Kenya benefiting most so far.

Kenya is among the top sources of foreign direct investment to Uganda with



Halt: a Kenyan border post

27 licensed investment projects worth \$158m. Kenya is the second-biggest investor in Tanzania, with 270 companies providing more than 100,000 jobs.

The EAC's goal is to have a common currency by 2012 and a political federation in place by 2015. Although few believe such an ambitious timetable can be met, the region's leaders have at least recognised that the larger market provided by integration should attract more investment and spur economic growth.

Continued on Page 2

Doing Business in Kenya

Questions of power

As Kenya recovers from the 2009 economic downturn, the demand for electricity will continue to rise.

Electricity is expensive and not reliable. A transmission network in need of an overhaul creates regular disruptions, while demand, at an estimated 1,334 megawatts, is so close to output that there is not much of a safety margin.

About two-thirds of the country's energy supplies are derived from hydropower, which makes for a good renewable energy balance, but can become a problem. When the rains fail, so do power supplies.

In past years, Kenya had to supplement regular energy generation with expensive emergency thermal generation, which feeds through to power bills and raises business costs. In 2009, power rationing was temporarily reintroduced. Large corporates routinely have back-up generators, but this is a precaution many small-scale companies and entrepreneurs cannot afford.

However, there are several initiatives to diversify power sources.

The government recently reversed an announcement that it would cut back on expensive thermal emergency power generation and formed the Geothermal Development Company to accelerate exploitation of the country's geothermal potential.

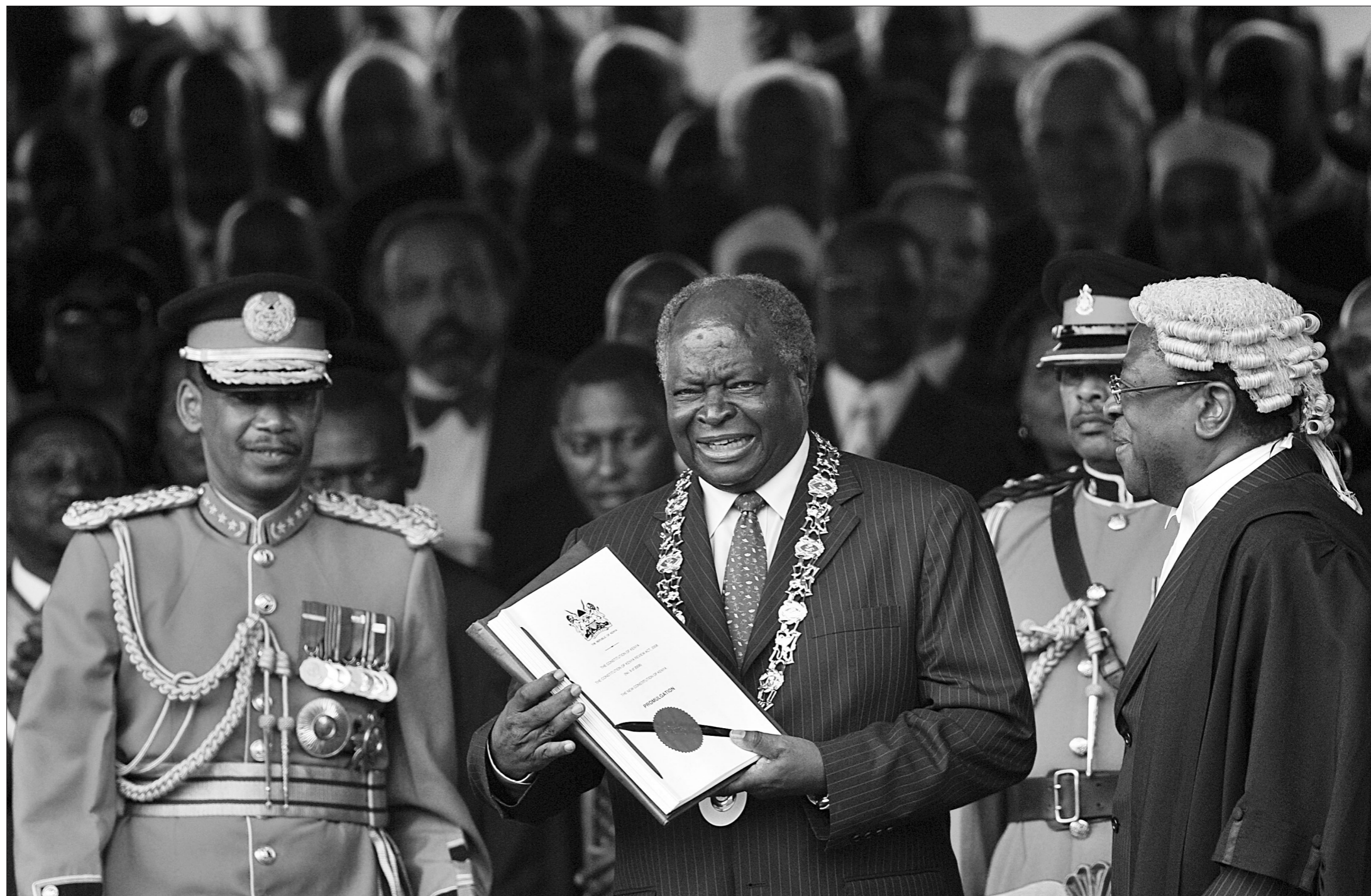
So far, KenGen, the national energy generation company, has built the 45MW Olkaria I and the 65MW Olkaria II plant, while the 48MW Olkaria III is privately operated.

Because of rising demand, the sector has become interesting for investors. Lake Turkana Wind Power, for example, is a venture located in north Kenya and is designed to generate 300MW once fully onstream. At full capacity, this would equal the amount currently derived from thermal emergency power, but it still needs to reach the grid from its remote location. There is no transmission line and negotiating the infrastructure financing has led to delays.

The Ngong Hills Wind Farm, about 22km from Nairobi, is a smaller venture, with six turbines capable of generating 5.1MW. Mumias Sugar Company has installed capacity of 34MW from burning bagasse, a sugar byproduct, and sells about two-thirds of its supply to the national grid.

The government is in principle keen to see more private-sector involvement in the energy sector. But corruption is a deterrent and often the government lacks the technical capacity to deal with such complex agreements speedily, causing delays for investors.

Andrea Bohnstedt



Capital ceremony: Mwai Kibaki, Kenya's president, smiles after being handed the new constitution by Amos Wako, attorney-general, right, during a ceremony in Nairobi in August

Getty

Ethnic divide still a cause of unease

Constitution

The counter-reformist lobby is still seeking to cause upsets, writes Parselelo Kantai

The term "watermelon" came into Kenyan political parlance ahead of this year's referendum on the adoption of a new constitution. A play on the colours of the opposing 'Yes' and 'No' camps – green for the former, red for the latter – a watermelon, being green on the outside and red on the inside, referred to people in the 'No' camp, who privately opposed the draft. Because the most powerful oppo-

nents of the draft held high office they were in positions to frustrate its successful passage at the polls.

A number of incidents, such as the insertion of a national security interests clause in the bill of rights while the draft was at the government printer, threw suspicion on members of the security – a powerful cabal close to President Mwai Kibaki composed of senior members of the cabinet, the civil service and the intelligence service.

Had it been printed with this last-minute amendment, the bill of rights, a liberal innovation that seeks to draw the curtain on decades of citizen abuse at the hands of state authorities, would have been a victory for the conservative counter-reformists.

Investigations were promised. If they were ever conducted they have shed not revealed the perpetrators.

When, during the promulgation of the new constitution, adopted by a resounding 67 per cent, Sudan's President Omar el-Bashir showed up, putting a stain on what was supposed to be the dawn of a new democratic order in Kenya, fingers were again pointed at the watermelons.

Such signs, analysts point out, suggest Kenya may not be out of the woods yet and that behind the scenes some of the same divisions which fuelled post election violence in 2008 continue to play out.

The country's political future, says Duncan Okello, executive director of the Society for International Development, an economic rights non-governmental organisation, is predicated on whether Mr Kibaki can rise above his ethnic coterie and embrace real change.

The power-sharing arrangement between Mr Kibaki and Prime Minister Raila Odinga – agreed under international pressure in a bid to curtail the violence that raged after both men claimed victory in the 2007 polls – seems to have settled into a harmoni-

ous working relationship. But the sense of ethnic grievance that existed before the botched elections is alive and well.

Public appointments skewed in favour of Mr Kibaki's Kikuyu community, the largest single ethnic group in the country, continue to stoke the fires of ethnic grievance.

And with only 20 months left before Mr Kibaki is due to stand down, after serving two elected terms, lingering perceptions that he is still in the clutches of an ethnic coterie could cost him the opportunity to cement a legacy as a Kenyan leader rather than a tribal one.

"There's a sense in which the Kibaki inner elite does not appreciate

'They are caught in a bind. The regime is leaving and has to pay ethnic debts'

Duncan Okello
Society for International
Development

the resentment against pro-Kikuyu public appointments. It was this that almost brought the country to its knees after the 2007 election," says Mr Okello. However pro-Kibaki forces charge that within the coalition government everybody has been given to ethnic favouritism.

"But they are caught in a bind," says Mr Okello. "The regime is leaving and has to pay ethnic debts."

On the other hand, says Mr Okello, the president's Party of National Unity has a narrow recruitment base, with only its central and eastern Kenya ethnic constituencies to pick from. "I'm not surprised that this is going on, also because this elite seems to have a much bigger sense of country."

The National Cohesion and Integration Commission, a creature of the

deal that restored peace to the country in 2008, has promised to release the results of an ethnic audit of the public sector. Even as the public awaits this, little is being done to reform public sector appointments along the lines of the new constitution, which contains clauses outlawing discrimination and ethnic favouritism in appointments.

"There's no question that Kenya is on an irreversible course to a new era," says Gitobu Imanyara, a member of parliament and a veteran of the struggle for constitutional reform.

"But what will delay the onset of this new order are the so-called watermelons. They are looking for any opportunity to frustrate change."

Mr Imanyara reserves his harshest criticism for Mr Kibaki. "The president remains hostage to ethnic interests. While the president has publicly expressed his commitment to the new constitution, he appears privately to support the anti-reformers," Mr Imanyara says. "Fortunately for us, the new constitution is crafted and worded with self-perpetuating mechanisms which will make it very difficult for these forces to succeed."

The way the country's politics are being reshaped by the new constitution is perhaps best seen in regions such as the Rift Valley. Long a flash-point during elections, it was the tensions between the ethnic Kalenjin elite and the Kikuyu community that settled there which have stoked the worst electoral violence since the return of multiparty politics.

After the abolition of the old appointed provincial administration, the region's warring ethnic groups are separated into counties that will be governed by elected officials, each with their own ethnic support base.

Mr Imanyara says: "The Rift Valley has changed and changed forever. It no longer exists in the way we knew it. More than anything else, that will influence the direction of politics."

Business in Africa?

.... Then join the Associations for business in Eastern, West and Southern Africa



The Eastern Africa Association (EAA), the Business Council for Africa, West & Southern (BCA W&S) represent the interests of members and foreign investors, by assisting them in the conduct of their businesses in their respective Regions. When brought together these Associations form the Business Council for Africa (BCA UK). Benefits include regular business reports, specialist meetings, briefings by Ministers, African and British Ambassadors and High Commissioners and practical advice and assistance from local representatives on the ground. Economic policy is influenced through our local Associations in the Regions and in UK to improve the general business environment whilst providing networking opportunities between business people with common interests. Through BCA UK's membership of the Brussels-based European Business Council for Africa & the Mediterranean (EBCAM), the Associations have a voice within the European Commission and with other EU Africa business organisations.

Forthcoming Events include:

EAA	EVENT	LOCATION
8 December	Members' Lunch Meeting	EAA Nairobi
19 January	Members' Breakfast Meeting	EAA Nairobi
24 February	Members' Evening Meeting	EAA Dar-es-Salaam
1 March	Members' Meeting	EAA Kigali
4 March	Members' Meeting	EAA Kampala
9 March	Members' Lunch Meeting	EAA Nairobi
20 April	Members' Lunch Meeting	EAA Nairobi
8 June	Members' Breakfast Meeting	EAA Nairobi
9 June	Members' Meeting	EAA Kigali
10 June	Members' Meeting	EAA Kampala
10 June	Members' Meeting	EAA Dar-es-Salaam
14 June	AGM	London
27 July	Members' Lunch Meeting	EAA Nairobi
26 August	Members' Meeting	EAA Dar-es-Salaam
2 September	Members' Meeting	EAA Kampala
14 September	Members' Breakfast Meeting	EAA Nairobi
18 October	Members' Meeting	EAA Addis Ababa
21 October	Members' Meeting	EAA Kigali
26 October	Regional Meeting	EAA Nairobi
4 November	Members' Meeting	EAA Dar-es-Salaam
7 December	Members' Lunch Meeting	EAA Nairobi
BCA W&S		
26 January 2011*	VIP Briefing with HE Mr Omer Pionkaki, Ambassador, Embassy of the Gabonese Republic	Venue *
22 Feb 2011 *	VIP Brief on Nigeria by Peter Stephenson Director of Trade & Industry, BHC Lagos	Venue: Old Trafford Stadium, Manchester.
BCA UK		
15 December	BCA UK Annual Christmas Review with Patrick Smith, Editor of Africa Confidential	Stephenson Harwood LLP One St Paul's Churchyard London. To Register: www.eventelephant.com/review

*TBC

For further information on membership and the above events contact:
2 Vincent Street, London SW1P 4LD

EAA/BCA UK Tel: 0207 828 5511. E-mail: jcsmall@eaa-lon.co.uk www.eaa-lon.co.uk
BCA W&S Tel: 0207 828 5544. E-mail: info@bcAfrica.co.uk www.bcAfrica.co.uk

Contributors

William Wallis
Africa Editor

Parselelo Kantai
East Africa correspondent

Andrea Bohnstedt
Publisher of Ratio
magazine and independent
Africa risk analyst

Michela Wrong
Journalist and author of
"It's Our Turn to Eat. The
Story of a Kenyan
Whistleblower"

Adam Jezard
Commissioning Editor

Steven Bird
Designer

Andy Mears
Picture Editor

For advertising contact:
Mark Carwardine +44
(0)20 7873 4880, email:
mark.carwardine@ft.com,
or Larry Kenney on +44
(0)20 7873 4835, email:
larry.kenney@ft.com

All FT Reports are
available on FT.com.
Go to: ft.com/reports
Follow us on twitter at
twitter.com/ft.reports

EAC enthusiasm lags results

Continued from Page 1

The EAC has a population of 126m and gross domestic of some \$75bn. In practice, however, the common market has yet to live up to its billing.

According to businesspeople in Nairobi, special interest groups across the region, from second-hand car importers in Uganda, to cloth importers in Tanzania, are undermining progress by winning exemptions on the common external tariff that continues to distort trade within the bloc.

"It will take time, but there is a lot of political momentum," says a European Union donor official involved in efforts to support the process.

Ironically, economic integration in east Africa under British administration half a century ago was well in advance of that taking shape in Europe at the time. In the original EAC linking Kenya, Tanzania and Uganda, external trade, fiscal and monetary policy

and university education operated under one umbrella. There was even a jointly run airline, post office and railway network.

However, the politics of the union ran ahead of economic reality and the EAC collapsed in 1977. Cold war ideological differences and fears that Kenya, with its more advanced economy, would dominate the other two were partly to blame. The region's economies and labour markets complement each other better today. Governments now follow broadly similar economic policy.

Kenya has a diverse economy, a sophisticated financial sector and the largest manufacturing base in the region. Tanzania and Uganda both have abundant fertile land and natural resources. The discovery of oil in Uganda and gas in Tanzania means that the region will soon have its own fuel supplies.

The need for closer co-operation on infrastructure development is also becoming urgent. The main port

servicing the region, Mombasa in Kenya, has reached capacity, the railways are dilapidated and roads need upgrading.

Fears of Kenyan dominance in the region are, however, an ever-present factor.

"In practice, 80 per cent of Kenyan manufacturers are not able yet to export duty-free to member states," says Bill Lay, who runs General Motors in the region and whose ambitions of selling the buses and trucks his company assembles across borders have so far been stymied.

Mr Lay, who also runs the Amercian Chamber of Commerce in Nairobi, says he knows of up to \$100m in investment from the Americas that is awaiting further progress on the ground towards achieving the common market reality.

"With enough time, the concept of a market of 126m customers for durable goods should be really good," he says. But it is the businesspeople not the bureaucrats who are in a hurry.

Growth that demands more than just talk

Economy

A telecoms price war has provided a fillip, but infrastructure still needs much work, says William Wallis

The economy this year has received a stimulus from an unexpected quarter: India. In an attempt to gain greater market share, Bharti Airtel, the Indian telecoms company, which bought its way into the country through its acquisition of Zain's Pan-African cellular operation, launched a price war.

The result has been a 50 per cent drop in airtime prices. When multiplied by the time Kenya's 20m subscribers talk, the cash liberated each month for other purposes equals \$66m or more.

"This is the most democratic kind of stimulus," says Aly Khan Satchu, a Nairobi-based investment banker. It is playing a part in spurring recovery from two years in the doldrums.

Hit by political crisis, drought and the global downturn, Kenya's economy slowed in 2008 to 1.7 per cent, picking up only gradually in 2009.

The accelerating rebound – to some 5 per cent this year – is partly the result of a return in confidence following the adoption in August of a new constitution. In contrast to the flawed 2007 elections, which unleashed a wave of ethnic violence, the referendum was conducted peacefully, without rigging.

Favourable weather has also been a boon – spurring a recovery in agriculture. Tourism has rebounded to pre-crisis levels, with more than 1m visitors expected this year, and the broader excitement among investors about Africa's potential has buoyed the Nairobi stock exchange.

Kenya is an essential bridge to a fast growing if volatile region, attracting unprecedented interest, as China, India and other emerging powers tap into the continent's frontier markets and store of natural resources to stimulate growth at

home. For all the diversity of its economy, however, Kenya has yet to achieve the transformational growth that might break down the gulf between affluent urban elites and scruffy, impoverished hinterlands.

Over the past decade, the economy has averaged relatively modest 3.7 per cent growth a year. Nairobi's position as a transport and aviation hub is part of this. But telecommunications during the period have played the largest role, growing 20 per cent a year.

"Without telecoms, Kenya would not have grown on a per-capita basis," says a senior donor official. Safaricom, the dominant mobile phone company, is the largest tax contributor, and is inadvertently providing the fiscal stimulus that the state has laboured to engineer.

Telecoms have also unleashed innovative capacity. The ven-

No other country at a comparable stage of development has achieved the kind of financial depth that Kenya has

ture capital, technical savvy and business flair housed in Nairobi office blocks, such as the one Mr Satchu looks out from, is harnessing technology and tailoring it to Kenya's specific needs.

No other country at a comparable stage of development has achieved the kind of financial depth Kenya has, as a result of the development of mobile telephones for banking, says the donor official.

"For the first time, Kenya is exporting innovation rather than the other way round," he says. Yet, as consumption and services have grown, other sectors of the economy have been shrinking, and exports as a proportion of GDP are in decline.

This change taking place is illustrated by plans for one of the continent's most ambitious property developments – a \$5bn residential complex to house 62,000 people harnessing Russian and Kenyan capital. The proposed town will be built on

an old coffee plantation outside Nairobi.

To some extent Kenya's horticulture sector has made up for losses in traditional exports such as tea and coffee. But if there is one thing that has shored up the shilling and saved the current account from falling into deficit it is the diaspora.

Research by the World Bank this year nearly doubled estimates of remittance flows to \$1.9bn a year, making them the country's largest source of foreign exchange.

This is flowing into small enterprises and construction, and along with a surge in money from the large and dynamic Somali trading community, account for liquidity that is palpable, especially in Nairobi.

To harness Kenya's potential, however, will require more solid building blocks. And as growing numbers of young and relatively well-educated Kenyans migrate from rural areas to urban slums, the need for faster employment creation has become acute.

Unlike services, manufacturing, which could provide the jobs, has been flat. The chief executive of one Indian trading conglomerate that supplies upmarket household products says it is 15 per cent cheaper to manufacture in Malaysia and Indonesia, even when transport it taken into account. Higher fuel and electricity costs are part of the reason.

Kenya's infrastructure is another. The port at Mombasa, the power plants, and road and rail connections to neighbouring states are dilapidated and inadequate and require multibillion dollar investments.

The government prides itself in being relatively independent of foreign donors, with a tax base that accounts for 22 per cent of GDP.

But much of the budget is spent financing a bloated civil service and greedy political system. To modernise infrastructure and reduce the costs of production, will require significant inflows of private investment and development aid from abroad.

For this, foreign donors are pressing government to show stronger commitment to reform.



Coming up roses: Kenya's horticulture sector has helped to make up for losses in traditional exports such as tea and coffee

Bloomberg

Mobile phone users present new business opportunities

Banking

Safaricom enjoys a big lead, writes Andrea Bohnstedt

Banking by mobile phone has taken off in Kenya as lenders compete to sign up customers.

"We are talking to all mobile operators – banks really don't have a choice any more," says Martin Oduor Otieno, the group chief executive of Kenya Commercial Bank (KCB).

Among the five heavyweights in the banking sector, KCB, Barclays, Standard Chartered, CFC Stanbic and Equity Bank, competition is intense, he says. In the retail market, there are two turfs to fight over: mortgage financing – and mobile money.

The local Safaricom mobile network operator pulled off a global first with its mobile money service M-Pesa (*pesa* is Swahili for money) and since its launch in 2007 it has accumulated more than 13.5m customers, or 81 per cent of Safaricom's customer base.

The concept is straightforward. Safaricom subscribers need to sign up for the service with an ID card – this ticks off the Know Your Customer requirements. They can then pay cash into their M-Pesa account with any agent, transfer it, or simply keep it in the account and take it out again when they need it.

This was a game changer in an economy where an estimated 30 per cent of people have no access to formal or even informal financial services: the physical distance is too great or the fees and minimum balances are too high, or both.

Having a secure place to keep money, and to send it to relatives, suppliers and business partners safely and in seconds rather than give it to a bus or courier company and hope for the best has made an enormous difference.

But M-Pesa was not just hugely popular with unbanked mobile users who have no alternatives. Many subscribers with bank accounts, credit cards and internet banking also use it to pay household staff, to send money to relatives in rural areas, or to pay a mechanic.

Safaricom's popularity initially triggered much speculation about whether the mobile company would take on banks directly: No, argued Safaricom – we are not a financial institution, and in any case, our target clientele are too small for banks.

Given the enthusiastic uptake of mobile money services across different income groups, the latter argument has become irrelevant, and M-Pesa acknowledges this with an ever widening range of services.

Subscribers can now pay utility bills or renew their television subscription, buy airline tickets from Kenya Airways and pay for their groceries at selected supermarket chains. At the moment, Safaricom has 400 bill payment partners and is clearly no longer just a service for the unbanked.

The relationship with the banking sector has developed on several levels, and from the beginning, there were opportunities for

banks. Since Safaricom is not a licensed financial institution, it does not touch any of the money sent back and forth, but merely provides the data platform. The funds are held in a trust account with Commercial Bank of Africa (CBA).

In May 2010, Safaricom took the collaborative route a step further. Together with Equity Bank, one of the big five banks, Safaricom launched the M-Kesho

Safaricom does not touch any of the money sent back and forth, but merely provides the data platform

service (*kesho* being Swahili for tomorrow). This allows M-Pesa customers to access Equity bank accounts directly.

In the six months since its launch, M-Kesho has gathered 613,000 subscribers. For Equity Bank – which targets clients in the lower-income population – the co-operation created access to a sizeable national agent network of about 20,000 agents, vastly bigger than Equity's already extensive branch network.

M-Pesa's success became apparent quite quickly, prompting Safaricom's then chief executive Michael Joseph to predict that mobile operators across the continent would copy it within the next 12 to 18 months. This has not happened and it may be that the skewed structure of Kenya's mobile telecommunications market – although it is a concern to the regulator and competitors – has helped to make M-Pesa so successful.

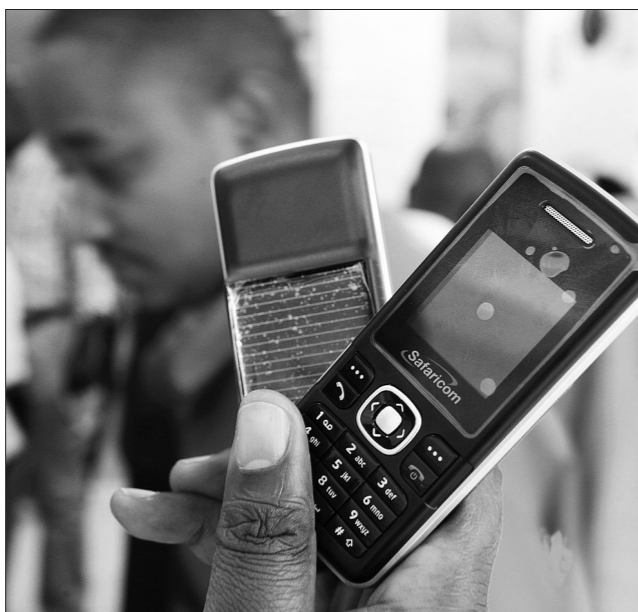
Safaricom's ubiquitous frog green logo is a reflection of its extensive agent network throughout the country. This means it is easy for subscribers to retrieve their cash anywhere. And while Safaricom does not actually handle any cash, Mr Joseph has argued that in the perception of most clients, they give their money to a company that they trust to handle it safely.

Safaricom's competitors also offer mobile money services: Airtel (which bought Zain) through Zap, Essar's Yu through Yu-Cash, and Telkom Orange finally launched its Orange Money service in November 2010, also in co-operation with Equity Bank. For Kenya's innovative developers, this is an opportunity.

Several companies have developed payment systems that connect mobile payments, banks and card payments for merchants, schools and others who need to process large numbers of transactions.

But whether any of the other mobile money services will become a serious competitor to M-Pesa is still open. Safaricom now co-operates with seven commercial banks and two non-bank financial institutions, Housing Finance and Post Bank, whereas Orange is tied to one bank.

Subscriber figures alone will bolster M-Pesa's dominance. Between banks and mobile money services, co-operation is still the modus operandi – but with a clear warning: "You're either with us or against us."



Cash call: mobile telephone banking is a success story Getty

Financial Times: Africa Reports 2011

In 2011 the Financial Times will publish worldwide a significant programme of Country, Industry, and Pan-regional reports relating to Africa.

These highly anticipated reports will provide unique insights into the economy, politics, key industries and issues unique to the region. This provides companies with the opportunity to align their brand with the FT and use these reports to highlight their own activities in an editorially relevant environment.

For more information about the 2011 Nigeria Report and the range of African Reports being scheduled please contact:

Mark Carwardine or Larry Kenney
mark.carwardine@ft.com or
larry.kenney@ft.com
 +44 (0)207 873 4835

We live in FINANCIAL TIMES®

EuroCave®

For more than 25 years the world's leading supplier of wine storage display and serving equipment, EuroCave has the solution.

Wine Cabinets

To have 50 to 250 bottles always at hand – the wine cabinet inventor in 1976, EuroCave now offers more than 250 models to provide ideal conditions for wines to be preserved and matured.

The Vin Au Verre

Preserve, present and serve wine...by the glass – this is an exclusive system enabling fine wines to be served by the glass with no loss of quality with up to eight open bottles.

Cellar Conditions

Turn any room into a real wine cellar – EuroCave air conditioners enable you to mature and preserve your wines just about anywhere, in ideal conditions to reach maturity.

Storage Systems

Optimised your wine storage – EuroCave has developed two unique storage systems, modular to fit in with your premises and your requirements. An exclusive concept for the storage, presentation and service of your best 'crus'.

Available now in KENYA

contact: **Semfeb Limited**

email: g@iconnect.co.ke

tel: +254 20 2716340, +245 20 2724551

Doing Business in Kenya

Lack of clarity over port plan raises concerns

Infrastructure

Lamu residents fear their voices will go unheeded, writes Parselelo Kantai

Omari Musa's last regular job was at the cotton ginny, separating seeds, seed cases and other objects from cotton fibres, in the seventh-century Swahili settlement of Lamu on Kenya's northern coast. That was in 1998.

Since the cotton ginny, the district's last factory, closed Mr Musa has taken on whatever work he can find. He worked on a dhow transporting grain between Lamu and other coastal towns. A few years ago, he became a porter and tour guide, befriending tourists at Lamu's tiny airport and showing them round the old town, famed for its Byzantine alleys and ancient, narrow buildings.

In a month, he earns anything between \$50 and \$100. It is enough to pay for food and school fees for his daughter, who is in kindergarten.

Mr Musa perks up at the mention of the proposed Lamu port. "It could be good for us," he says. "There are no jobs here for the youth. Even if I don't get a job at the port, maybe some of my relatives will."

For all its seaside panoramas and its reputation as the repository of old Swahili culture – Lamu has been designated by Unesco as a World Heritage Site – this is one of Kenya's poorest regions, and among its most marginalised.

The majority of the population is illiterate; most people depend on fishing and the petty earnings from backpacker tourism. Less than 1 per cent of the indigenous population have title to their lands, effectively meaning they are squatters on their ancestral lands.

Now the government is embarking on perhaps the most ambitious infrastructure modernisation project since the construction of the colonial Kenya-Uganda railway more than a century ago.

The \$20bn project, including a \$4bn port, an oil refinery, railway and a highway linking Lamu to south Sudan and Ethiopia will transform the town from a sleepy settlement to the epicentre of the region's modernisation.

Work on the Lamu Port-Southern Sudan-Ethiopia Transport Corridor is in its planning stages. Briefing papers have been drafted and rewritten; the government has courted potential investors, including the Chinese and the Qataris, and contracted Japan Port Consultants to conduct a feasibility study.

Nobody argues seriously with the need for the project. The region's economies have expanded significantly in the past decade. The port at Mombasa, which serves Kenya,

Uganda, Rwanda and eastern Congo, can handle only 25m tonnes of cargo a year. With the inclusion of an independent south Sudan, a possibility for the region's planners, annual cargo handling demands will rise upwards of 35m tonnes.

The Mombasa port, says a Ministry of Transport paper, does not have sufficient room for expansion. Lamu, on the other hand, is perfect for a port in line with the region's expanding needs. Manda Bay, where the port will be located, has a 3.5 kilometre entrance, wide enough for seven ships, wider than Mombasa's port. There is also land available for future expansion, and for the construction of an oil refinery and an airport, with some left over for a tourist resort.

But construction is already months behind schedule, though it is unclear why. In fact, aside from JPC's feasibility study, little seems to be happening.

This lack of information has led to fears that locals will be robbed of their livelihoods. There has also been no indication that a statutory environmental impact assessment has been carried out. Letters from environmental groups to the National Environment Management Authority have gone unanswered.

"We are concerned the Lamu port project will be a cultural, social and environmental catastrophe," says Mohammed Ali Baddi, a former councillor and one of the leaders of the Lamu Environmental Protection and Conservation Group.

Mr Baddi says there are more than 25,000 fishermen in Manda Bay. A fragile marine environment, a spawning ground for prawns and crabs, the bay is ringed by mangrove forest that is likely to be cut down.

Whatever benefits that would come with the port are offset by a painful past. For more than a century, Lamu's communities have been subjected to an almost continuous process of land dispossession, first by the British colonial administration and by successive post-independence governments.

Starting with the Kenyatta government, thousands of ethnic Kikuyu were settled on what the state regarded as government land, but what locals see as ancestral property.

"These resettlement projects have brought 40,000 upcountry people into our area," says Mr Baddi. "We are now minorities in our home region."

While land reforms in the constitution offer some relief for Lamu's indigenous communities, a rash of land speculation has seen prices rocket. Indications are that Lamu is about to see history repeat itself.

"We need this project, no doubt," says Mr Ali Baddi. "But we want a good, clean port that will benefit the indigenous community as much as anybody else."



Centre of unrest: Daniel arap Moi, former president, seen campaigning for the 'No' vote against constitutional reform in the troubled town of Nakuru in June

Getty

Unrest runs deep in Rift Valley

Regional focus

Michela Wrong on an area stained with a bloody history and still threatened by ethnic turmoil and violence

The Rift Valley lake town of Nakuru, north of Nairobi, has many claims to fame, most of them invisible to the tourists who drive there to view the flamingos in their pink and honking splendour.

It was here, just before independence from Britain in 1963, that Jomo Kenyatta reassured white settlers they still had a future in his country, preventing a disastrous haemorrhage of investment and confidence. It was here that Kenya's founding father came to watch the dancing troupes, rewarding favourites with stretches of local land.

And it is here, analysts warn, that violence risks breaking out in coming years, the result of land hunger and ethnic hostilities left festering for too long.

"Nairobi's business and investment community doesn't see the Rift Valley as an immediate issue.

There's a feeling that if you can get the economy to expand and the infrastructure built, you can grow your way out of crisis," says David Anderson, a British historian on Kenya. "But this is not over. The problem is deeply entrenched."

The Rift Valley was the scene of some of the most shocking violence to explode in the wake of the rigged 2007 elections, when local Kalenjin ethnically cleansed farmers from the Kikuyu tribe, Kenya's largest, seen as "foreigners", in spite of their having been settled in the area since the 1960s and 1970s.

In one incident, Kikuyu women and children were burnt to death in a church in Eldoret, home town of Kalenjin former president Daniel arap Moi.

In Nakuru and the town of Naivasha further south, the slums later became battlefields as militiamen, trucked in by politicians to boost Kikuyu numbers retaliated by castrating and beheading members of rival ethnic groups.

The new constitution was approved by a majority of Kenyans partly in the hope it would prevent a repeat of such horrors. In theory the devolution of central power, the redrawing of provincial boundaries to cut across

already blurred tribal lines, and the creation of local assemblies will finally draw Kenya's ethnic poison. But most members of the Kalenjin community voted against this historic document.

Chauvinistic local leaders angrily predict the new arrangement will do nothing to mend the wounds left by what they see as

"Who are... the leaders here? This is our heartland and we are not about to surrender it to other people"

decades of land appropriation, which began when British farmers brought Kikuyu labourers in to work on what were known before independence as the "White Highlands".

Pastor Peter Chemaswet says: "We rejected the constitution 100 per cent because we knew it would just open up our land to further appropriation. Nakuru is the Jerusalem of Rift Valley. Who are supposed to be the leaders here? This is our heartland and we are not about to surrender it to other people."

Kalenjin bitterness is exacer-

bated by the awareness that when the new constituencies stipulated under the constitution are delineated, the local assembly in Nakuru, the central town in the Rift Valley region, will not be controlled by the Kalenjin.

The influx of Kikuyu and other groups – as a result of ethnic cleansing in the early 1990s and the 2008 violence – has altered the ethnic make-up. New housing scheduled for construction on a stretch of scrub land on the town outskirts will undoubtedly reflect this new reality.

"In the old days, it was 'if this is Rift Valley, it has to be Kalenjin'," says Joseph Omondi, who works for Bunge La Mwananchi, a non-governmental organisation trying to encourage reconciliation and social change. "Now those who were born here are outnumbered three to one."

The resentment of local Kalenjin is only equalled by that felt by poor Kikuyu farmers expelled from farms in Molo, Eldoret and other parts of the Rift Valley, most recently following the disputed elections in 2008.

Although the government announced in July that Kenya had no more internally displaced people, thousands of Kikuyu families still live under tattered tarpaulin, too frightened to return to aban-

doned farmland yet aware they are unwelcome in their new location. At Pipeline IDP camp, located down a muddy track off the main highway to Nakuru, 6,500 Kikuyu ejected from Kericho, Nandi, Molo and Rongai are anxious to show visitors the inadequate size of plots bought with government start-up money.

"You see? These are barely the size of a house," says Paul Thiongo, camp chairman. As the rain starts, he points with disgust at a row of 21ft by 27ft allotments planted with maize and beans. "Not enough to survive on."

Human rights workers warn that the camps, whose funding by Nairobi's central government is the target of a current investigation by the Kenya Anti-Corruption Commission, are ripe areas for recruiting by ethnic militias, which are regularly whipped into existence and sent in to do battle at times of political tension.

They also warn that the widespread availability of weaponry in Kenya – much of it filtering in from Somalia – means any new conflict will involve not the clubs, axes and machetes of the past, but AK47s. "The Rift Valley is now tooled up," says Mr Anderson, seeing analogies with the former Yugoslavia. "And the mood reminds me of Kosovo."

Drive to combat corruption fosters scepticism and hope

Political reform

Could the country be on the cusp of genuine change? Michela Wrong investigates

A foreign minister and his permanent secretary forced to step down; an education minister suspended; an industry minister humiliatingly questioned; the mayor of Nairobi hauled into court. When it comes to high-profile anti-corruption probes, Kenya has never seen the like.

A flurry of recent high-profile investigations by the Kenya Anti-Corruption Commission under its new director Patrick Lumumba has left many wondering whether a country whose politics are indelibly associated with sleaze might finally be on the cusp of genuine reform.

Coming soon after anti-corruption group Transparency International announced Kenya's ranking in its yearly global Corruption Perceptions Index to be a predictable 154 out of 178, the flood of KACC announcements is triggering both hardened scepticism and tentative hope.

Mr Lumumba's burst of activity has reminded a public already embittered by a two-and-a-half-year series of scandals that has sent fuel and maize prices soaring and prompted a donor freeze on support for primary education just how

far and deep sleaze extends throughout the Kenyan body politic.

To date, the probes embrace the suspect sales of embassies abroad, shadowy land deals, the irregular issuing of citizenship papers and questionable car imports.

But these appear to be the tip of an iceberg. Mr Lumumba has at least four further cabinet ministers and 45 para-statal chiefs in his sights and has also bravely announced his intention to probe past regimes' scams.

"Everyone has got dirt in their backgrounds," says Mwalimu Mati, head of the anti-corruption Mars Group Kenya. "Back in 2008, when the coalition government was formed, we said that 24 out of the 44 ministers were ineligible for appointment on the grounds of suspected corruption or human rights violations."

But the reminder of the size of the "eating" or corruption – routinely justified, in a nation obsessed by tribal affiliation, on the grounds of ethnic solidarity – is overshadowed by the fundamental question of whether the KACC can deliver. Past efforts have been a depressing litany of setbacks, retreats, stalemates and betrayals.

In the mid 1990s, the International Monetary Fund set the establishment of Kenya's first anti-corruption agency as a condition for aid. Donors were exasperated by the damage cynicism was doing to the

economy, in particular the Goldenberg scam, which began with fictitious gold exports but ended up swamping Kenya's entire financial system.

Grudgingly established by Daniel arap Moi, the then president, the institution did not last long. Its director was suspended after six months and it was then declared unconstitutional by the High Court.

In 2002, a coalition of opposition groups led by Mwai Kibaki won a massive election victory on an anti-corruption platform.

The new government signalled its seriousness by appointing John Githongo, a young anti-corruption campaigner, as special presidential adviser and relaunching the KACC

"The investigations will land at the president's door... I don't know how long Kibaki will retain enthusiasm"

under the directorship of Aaron Ringera, a respected judge. An inquiry into Goldenberg was launched and Kroll Associates, the international risk consultancy, hired to track down the whereabouts of stolen funds.

That effort collapsed when Mr Githongo fled to London in 2005 and revealed that new ministers had signed a series of inflated security deals: the

infamous Anglo Leasing scandal. He also revealed that Mr Ringera, far from investigating the suspect contracts, had warned him to stay silent and his attempts to provide evidence had been systematically sabotaged. The KACC stood discredited and when President Mwai Kibaki attempted to reappoint Mr Ringera to another five-year term he was overruled by parliament.

The KACC appears to have been energised by the passing of the new constitution, which could give it powers to prosecute as well as investigate, and by growing public exasperation with a tradition of predatory plundering.

"The constitution is supposed to be a new beginning," says Samuel Kimeu, director of TT's Kenya branch. "Kenyans don't want things to carry on in the same old way. There's an element of legacy for a president whose time in office is coming to an end."

Sceptics argue, however, that an element of political manoeuvring is discernible. The new constitution rules out those under investigation standing for office, so a KACC probe effectively sidelines ambitious players from the 2012 elections.

William Ruto, the suspended education minister, is a turbulent demagogue who has fallen out with Raila Odinga, the prime minister. Moses Wetangula, the sidelined foreign minister, angered some with his presidential ambitions. Cynics point to the nature



Reforming zeal: KACC director Patrick Lumumba

Reuters

of the new appointments as an indication of how much real progress to expect.

The politician taking over Mr Wetangula's post is George Saitoti, who ran the finance ministry during the Goldenberg scandal. Mr Saitoti remains minister for internal security, effectively in charge of the force responsible for investigating corruption.

"You're not going to end corruption by keeping on the same players," says Mr Mati. "The KACC are targeting people who are politically weak already, low-hanging fruit."

Since independence, executive power has become more centralised in State House, which raises doubts over the feasibility of Mr Lumumba's stated intention of investigating the scams that went to the hearts of two presidencies: the \$1bn Goldenberg scandal perpetrated under Mr Moi, and the Anglo Leasing scandal, which erupted during Mr Kibaki's first term.

"If it continues," says Mr Kimeu, "the investigations will land at the president's door. So I don't know how long Kibaki will retain his enthusiasm."

Mr Githongo, who now runs a grassroots organisation, no longer sees much use for anti-corruption agencies, dismissing them as "institutional orphans", doomed to wither from lack of political support.

Nonetheless, he views the KACC's latest moves as an encouraging response to changing times.

He says: "Politics is moving quickly in Kenya and opening up new space for reform. We should take advantage of this before the counter-reform efforts of the tiny elite gather momentum."

But there is a tradition in Kenya of politicians "stepping" aside when under investigation, only to step back once public attention turns elsewhere.

As Michael Ranneberger, US ambassador in Nairobi, says: "Not a single high-profile player has been prosecuted for corruption in the history of Kenya."

Mr Lumumba is likely to have his work cut out if he wants that to change.

Michela Wrong is author of "It's Our Turn to Eat. The Story of a Kenyan Whistleblower"



KESTREL CAPITAL
MEMBER OF NAIROBI STOCK EXCHANGE

The leading broker in Kenya for foreign and local institutional investors, with a strong focus on market and company research.

A foreign client base that spans Europe, the U.S., South America, the Mideast, Asia, Southern and Western Africa.

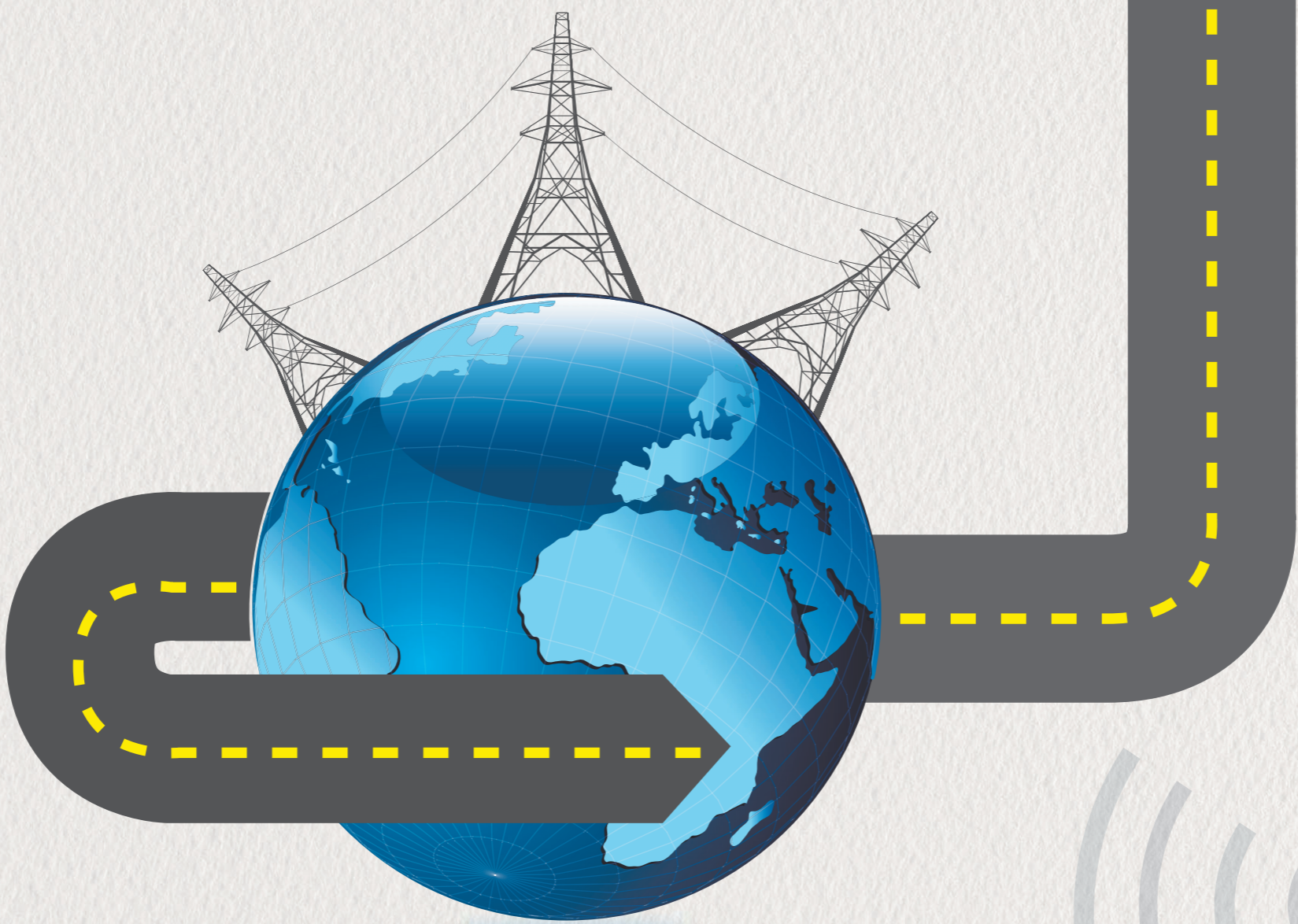
- Company and market research
- Stockbroking and bond trading
- Public offerings and IPOs
- Corporate finance advisory



www.kestrelcapital.com
Nairobi, Kenya

→ Let's be the bank

--- THAT DRIVES ---



KENYA'S DEVELOPMENT

Corporate Investment Banking
We provide transactional and advisory services to corporations that drive development initiatives in Kenya.
Contact us today to find out how together we can power the ideas that will shape Kenya's future.
Call us on +254 20 326 88 88 www.cfcstanbicbank.co.ke
Moving Forward™



Doing Business in Kenya

Fibre-optic backbone strengthens ICT sector

Technology

The country's reputation for innovation is growing, writes Parselelo Kantai

A decade ago Paul Kukubo, head of Kenya's Internet Communications Technology Board, was running an internet start-up, when he was invited to pitch for an outsourcing job with a Swedish television company. It would have changed the company's fortunes.

"Our work was world-class," he says. "But we couldn't deliver because we didn't have the bandwidth."

The situation is different today. Up to a year ago Kenya, along with the rest of east Africa, was the only region left in the world without a fibre-optic backbone. But the arrival of four undersea cables has increased bandwidth capacity about 100 times, and has been accompanied by a comparable price fall.

"The speeds have substantially increased and the costs have decreased substantially," Mr Kukubo says. "We can take for granted certain things we couldn't before."

Mr Kukubo has become an ambassador for the country's nascent ICT sector and spends much of his time flying between foreign

capitals preaching the message that Kenya has all the conditions to be the next important ICT investment destination.

In the past few years, the country has become known for clever innovations in software development, including M-Pesa (see page 3), a mobile platform that has become the banking system of choice for a population of whom just 5 per cent previously held bank accounts.

There have been other trailblazing innovations. In September Virtual City, a Nairobi-based software development company, won Nokia's \$1m Growth Economy Challenge Fund, a global talent search for innovative applications tailored for mobile phones. The finalists included companies from the more ICT-advanced countries of India, China and Canada.

Virtual City's mobile phone tracking application fed into the buzz within Nairobi's ICT community. The country's software innovations are attracting interest from mobile phone makers such as Samsung and Nokia, venture capitalists and, crucially, the government.

"The Board has a grant of \$3m for local entrepreneurs. In the first series we have committed \$600,000 to 14 entrepreneurs," says Mr Kukubo. Consequently, the Board is registering interest from international investors.

This state support is beginning to change the industry. In the past, year



Hooked up: Nairobi's central business district has been linked to a high-speed network Corbis

the government has turned its attention away from an earlier strategy to promote business process outsourcing – call centres – to focus on software development.

There are plans to establish incubation centres for software development, first within Nairobi and then nationally. Initial studies are complete for the Konza Technology Park, on Nairobi's outskirts, which will house 80,000 software development and BPO workers.

A race among private

'The service economy should surpass agriculture in five years'

Bitange Ndemo
Ministry of Information

telecoms groups has seen a rapid roll-out of infrastructure. Companies such as locally owned Jamii Telkom – which is a minority shareholder in The East African Marine System, the multi-million dollar Teams undersea fibre-optic cable – has embarked on "what we call fibre-on-the-last-mile", according to John Kamau,

chief engineer at Jamii. "We have done fibre in Mombasa and several parts of Nairobi – Umoja, Athi River, Karen and the central business district. We also have fibre in Kisumu, Thika, Nakuru, Eldoret, and we are also moving to smaller towns."

Others, such as East African Capital Partners, are investing in last-mile cable infrastructure and digital content. EACP recently invested \$100m in internet service provider Wananchi. At the same time, it bought equipment from a failing satellite TV firm and has plans to compete with continental satellite TV provider DStv.

For Richard Bell, EACP's chief executive, possibilities for growth lie in a regional rather than national vision. "It's not a Kenya question, it's an East Africa one. That's important because Kenya, Uganda, Tanzania, are 100m people. Combine this with Ethiopia, with its 80m people, and you suddenly have a huge population."

"Each of these countries is identifying ICT as a driver of growth. They all have dedicated ICT ministries, boards of one sort or

another dedicating to driving the growth of the sector. We all have the right policies and fully liberalised telecom sectors, with the exception of Ethiopia."

At the moment, there are only 4m Kenyans with regular internet access. But the numbers will rise sharply with the introduction of 3G mobile phones that can surf the web. Similarly, steep drops in the prices of mobile phones and stiff competition among service providers mean there will be almost universal access to the internet soon.

Bitange Ndemo, permanent secretary in the Ministry of Information, has lofty dreams: "If we can mop up 1m of our youth into ICT and contribute a significant portion of gross domestic product, the service economy should surpass agriculture in five years."

Such dreams are held back by a shortage of local content. Most start-ups are run by software developers with little idea of how to turn ideas into commercial ventures.

"We must incubate those kids," Mr Ndemo says. "We must begin to teach them economics and entrepreneurship."

Africa: the new frontier for private equity firms

Investment

The region needs trailblazers to fund development, writes Andrea Bohnstedt

When Citadel Capital, an Egyptian private equity firm, acquired the shares of the struggling initial leader of Sheltham, the Rift Valley Railways consortium, it went head to head with Kenya's Trans-Century, one of the country's largest private equity firms.

Both parties have since come to an agreement about dividing the company but the Egyptian's willingness to muscle in is an indication of how attractive the investment is.

RVR connects Kenya's Mombasa seaport to Uganda's capital Kampala and the fight for control highlights the consequences of years of mismanagement and underinvestment, as well as the vibrant business in the region and the importance of the discovery of commercial quantities of oil in Uganda. All this means there is strong pressure to modernise the railway.

Infrastructure is as much a disincentive as it is a business and investment opportunity, but it is one of many sectors private equity funds are considering.

Among emerging markets, sub-Saharan Africa is fairly new in attracting such interest, but Kenya is home to several private equity firms. Some, such as Trans-Century, grew out of private investment clubs. Now the country is being used as a beachhead for investment firms, says Milton Lore, chief executive of the Africa Venture Capital Association (AVCA).

The East African Community withstood the global financial crisis remarkably well. With the exception of

Kenya, which struggled with the fall-out of the violent post-election crisis in 2008, member countries generally maintained gross domestic product growth rates of 5 per cent and above in 2009. Driving this resilience was intra-regional trade that also benefited from strong demand in post-conflict border regions such as eastern Democratic Republic of Congo and southern Sudan.

Kenya may have attracted less inward foreign direct investment than its neighbours in 2009, but its companies are the most active regional investors, expanding in financial services, hotels, airlines and agro-processing. This has changed the situation for private equity, says Paul

entry point for Middle Eastern capital seeking new directions. After the financial crisis many family groups pulled out of private equity funds to manage and invest their own funds.

"Africa is the new frontier," Mr Makary says. Arqaam Capital holds several mandates to find acquisition targets in logistics, agriculture and healthcare.

Kenya has attracted funds focusing on small and medium enterprises. TBL Mirror Fund is backed by Dutch private investors who lend their expertise to acquired companies.

It has invested in software, market research, call centres and healthcare. Several SME funds are backed by soft money – cash not invested solely to give a profit – from development finance institutions or social investors such as the Shell Foundation, which sees SMEs as crucial for more equitable growth.

AVCA also tries to engage African pension funds to consider private equity as an asset class. Providing capital to local firms helps nurture the domestic economy while broadening the subscriber base. Institutional investors are often concerned about exiting investments, but AVCA's Mr Lore says Nairobi's Stock Exchange is one of the oldest and largest on the continent and provides such an exit route through public offers.

Though still small in volume terms, venture capitalists have begun to look at Kenya's new economy: a relatively high mobile penetration rate, a mobile money service and improved connectivity through several fibre-optic cables have laid a foundation for digital, e-commerce and mobile ventures.

Tamer Makary, executive director of Arqaam Capital, a Dubai-based investment bank, says Kenya will be an



Tamer Makary: Kenya is the entry point for Middle East capital

Kavuma, chief executive of Catalyst Principal Partners. Kenya's aggressive firms offer exciting private equity opportunities. "The ambitions of local entrepreneurs have grown with regional integration. They no longer just want to be number one in one economy, but have broader ambitions," he says.

"The more forward-looking entrepreneurs want regional scale. This translates into a deeper need for capital that bank financing can't meet. We are looking for trailblazers."

Mr Kavuma and his colleagues are raising \$100m for investments in consumer goods, retail, financial and business services, industrials, manufacturing and value-added processing, technology, telecommunications and infrastructure.

Tamer Makary, executive director of Arqaam Capital, a Dubai-based investment bank, says Kenya will be an



Local knowledge, international expertise





A strong commitment to Kenya

- Afren is an established independent upstream oil and gas company, and has a diversified portfolio of 27 assets spanning the full cycle Exploration and Production value chain, across nine African countries.
- Kenya forms an integral part of the overall exploration portfolio.

