International Bank for Reconstruction and Development

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KE 91-3

FROM: Deputy Secretary

CONSULTATIVE GROUP FOR KENYA
Paris, November 25 and 26, 1991
CHAIRMAN’S REPORT OF PROCEEDINGS

1. Attached is the Chairman’s Report of Proceedings of the Meeting of the Consultative Group held in Paris, November 25 and 26, 1991. The following Annexes are attached to this Report:

- Annex A - List of Participants
- Annex B - Agenda
- Annex C - Opening Statement by the Vice-President and Minister for Finance
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Consultative Group for Kenya
Paris, November 25 and 26, 1991
Chairman's Report of Proceedings

Background

1. A Consultative Group meeting for Kenya was held at the Park Avenue Hotel in Paris on November 25th and 26th, under the Chairmanship of Mr. Callisto Madavo, Director of the Eastern Africa Department of the World Bank. Representatives of Canada, Denmark, Finland, France, Germany, Italy, Japan, the Netherlands, Sweden, Switzerland, the United Kingdom, and the United States attended the meeting. Also present were representatives of the African Development Bank, the Commission of the European Communities, the European Investment Bank, the International Monetary Fund, and the United Nations Development Program. Belgium, Saudi Arabia and the Organization for Economic Cooperation and Development attended as observers.

2. The World Bank Draft Report No. KE 91-2, "Kenya - Economic Developments and Public Sector Reform" was distributed prior to the meeting.

Chairman's Opening Statement

3. In his opening remarks the Chairman outlined those areas which would constitute the core agenda for the meeting. In addition to reviewing Kenya's economic performance and prospects, the focus will be on two related topics: public sector management and human resources. The Chairman explained that while Kenya has made progress in structural adjustment, this will not be sustained unless the performance of the public sector is substantially improved. For this reason, one of the sessions will be devoted to reform of the public sector, including parastatals, the civil service, and expenditure rationalization. He noted the importance of these issues to the overall effectiveness of development programs supported by donors. Also, there is a need to follow-up on last year's intensive discussion of human resource development. The Government has prepared some concrete proposals for addressing unemployment, and the Bank is making an attempt to strengthen its capacity for addressing these issues in East Africa. This year's session on human resource development will explore some of these proposals.

4. The Chairman noted that this meeting is being held at a time of widely publicized donor concerns. He called on participants to share their concerns with the Government, and to constructively outline those key areas which need to be addressed. By doing so, the Chairman expressed the hope that the meeting would build upon Kenya's economic and social progress, and would assist the Government in moving into the next phase of its development efforts.

Opening Statement of the Vice President and Minister for Finance

5. The Vice President and Minister for Finance, Professor George Saitoti, noted (see Annex C) that Kenya's development strategy for the nineties continues to be guided by the overall policy framework articulated in Sessional Paper No. 1 of 1986 on Economic Management for Renewed
Growth. This policy framework, which identifies the measures to be implemented to deal with Kenya's growing employment needs and to achieve a faster rate of economic growth, has been and will continue to be the basis for a series of adjustment programs. As a result of the effective implementation of these adjustment measures in a number of critical sectors, the Kenyan economy withstood the impact of several international events in the late eighties and maintained a sustained growth of over 5% per annum.

6. Although Kenya's economic adjustment and sector reform programs have been on track, economic performance last year was adversely affected by exogenous factors. The Gulf crisis had a devastating effect on the economy, mainly through increased petroleum prices, a sudden drop in tourism, and a decline in the demand for Kenya's exports in the region. These factors, together with a further fall in coffee prices, contributed to a growth rate of about 4% in 1991. Also, increased producer and consumer prices of basic food items, salary increases for the lower job groups in the public sector, and the depreciation of the Kenya shilling contributed, along with the Gulf crisis, to an increase in the inflation rate from 10.5% in 1989 to 12.6% in 1990.

7. Fiscal performance in 1990/91 was also affected by domestic factors including a revenue shortfall and the depreciation of the Kenya shilling. The latter resulted in a number of State Corporations being unable to meet the shilling contributions needed for their debt servicing, and the Government having to honor its guarantees. The Government attacked the fiscal management problems in several ways. Several drastic measures were initiated in the State Corporation sector, both from a short and a medium-term point of view. The restructuring of the Kenya Airways Board and the steps taken to review the activities of the Kenya Posts and Telecommunications Corporation (KPTC), leading to privatization of many of them, are some of the short term measures. Simultaneously, the Government began implementation of the State Corporation privatization program, the fiscal effect of which will be felt in the medium term.

8. The Vice President noted an improved current account deficit on the balance of payments, mainly as a result of a decline in the rate of growth of imports and an increase of over 22% in export volume coming from tea, petroleum products exported to neighboring countries and horticultural produce.

9. In discussing Kenya's immediate prospects, the Vice President stated that the growth of GDP is expected to pick up by 1992, in line with the end of recession in industrial economies. Other factors such as the recovery of coffee prices, strong growth of tourism, a fall in the rate of inflation and further realization of benefits of structural adjustment measures will assist in the process of recovery. Although the Government anticipates that the adverse balance of payment situation will continue for the next two years, the Government remains committed to continuing the tempo of trade policy reform and to maintaining the growth in private sector imports. The Vice President stated that additional resources of a substantial magnitude are needed not only to sustain the trade liberalization program, but also to fill the resource gaps during the critical transition years, until such time Kenya's exports pick up momentum.

10. The medium-term expenditure program visualizes a gradual reduction of the budget deficit from above 5.0% of the GDP in fiscal 1990/91 to about 2.0% in fiscal 1991/92 and maintaining it at this level for the next three years. Government expenditures, including grant financed
expenditures, as a percentage of the GDP are expected to fall from about 32% in 1990/91 to 28.2% by 1994/95.

11. The main elements of fiscal policy in the medium-term will be (a) further enhancement of domestic resources available to the Government; (b) a gradual reduction in the share of education and health sectors in the total budget; (c) reforms in the State Corporations sector; (d) improvements to the public investment program (PIP) to improve the productivity of public expenditures and (e) a much stricter control over expenditure over-runs and commitments.

12. The Vice President restated the Government’s commitment to political reform and the eradication of corruption. However, the pace of political reform would be determined by Kenyans, without foreign influence. On corruption, he noted that recent changes in the Government were aimed at ensuring greater accountability and transparency in decision-making. The Government has also introduced an anti-corruption bill in Parliament.

Statement by the World Bank

13. Mr. Ian Bannon, Senior Country Economist for Kenya, presented a statement on the economy’s short and medium term outlook (Annex D). He stated that the Kenyan economy has faced a difficult period during 1990 and 1991, as a result of adverse external and domestic developments. In late 1990, as the Gulf crisis unfolded and Kenya’s external terms of trade deteriorated sharply, the Government raised domestic oil prices between 30 and 49 percent, and revised its fiscal targets for 1990/91 in line with a tighter fiscal and monetary stance. Nevertheless, the budget deficit and money supply increased substantially, far exceeding the Government’s revised targets. Although affected by adverse terms of trade, the current account deficit on Kenya’s balance of payments fell from 7.4 percent of GDP in 1989 to 5.3 percent in 1990. A sharp reduction in net capital inflows, however, lowered foreign exchange reserves to only 1.4 months of imports by the end of 1990.

14. Since it began a series of sectoral adjustment programs in late 1986, the Government has implemented a number of measures to broaden the role of market signals and align relative prices more closely with those prevailing in world markets. In agriculture, producer prices have been improved, fertilizer imports and prices have been liberalized, and meat prices have been decontrolled. In industry and trade, the exchange rate has been managed flexibly, price controls have been substantially reduced, the marginal company tax rate has been lowered from 45 percent to 37.5 percent, the import licensing system has been liberalized, quantitative restrictions on imports have been practically eliminated, the level and dispersion of tariff rates have been lowered substantially, export incentives are being improved, a private sector export processing zone has begun operations, a new Value Added Tax has been introduced, and a number of trade licensing requirements have been streamlined. In the financial sector, interest rates have been fully liberalized, a number of troubled financial institutions are being restructured, the auction system for treasury bills has been opened up, the Banking Act has been strengthened and the Stock Exchange is being improved. These reforms enabled Kenya to withstand a major external shock with only a moderate slowdown in economic growth.
Despite this credible growth performance, there is a growing sense of unease over Kenya's current economic situation and its longer-term prospects. These concerns center around four major areas: first, as recent experience shows, failure to control the level of public spending continues to be a major threat to economic stability and sustained economic growth. The lack of progress in containing the public sector wage bill, overspending by a number of key ministries, and the poor performance of a number of large parastatals have been major contributors to recent expansionary fiscal policies. Second, although output has responded to the Government's reform measures, as shown by the sustained recovery in GDP growth over the past five years, this improved performance has not been matched by a recovery in private investment. In fact, real private fixed investment, which stagnated in 1988, fell by almost 3 percent in 1989 and dropped a further 10 percent in 1990. Third, while the improved balance of payments performance in 1990 was a welcome outcome, the presently precarious foreign exchange reserve position suggests that Kenya's economy remains highly vulnerable to adverse external developments and highly dependent on the level of aid inflows. The need to ensure external viability is critical if the Government's trade liberalization reforms are to be sustained. Fourth, in recent years there has been a growing perception that over-regulation of the economy and the lack of transparency in the enforcement of regulations and controls, are deterring private investment, creating inefficiencies in the allocation of resources, and weakening confidence in the sustainability of recent reform efforts.

The reform effort now needs to increasingly target not just policies and the structure of incentives and relative prices, but focus more explicitly on institutions and effective implementation across the whole spectrum of government functions. There are a number of facets to this process. Chief among them is the need to reform the public sector itself, including the civil service, and the transparency and accountability of its various components. A more direct effort is also required to promote private sector activity and remove the discretionary elements of government policies where they are found to contribute to an uncertain investment climate.

Mr. Bannon concluded by noting that over the past three decades Kenya has clearly been one of the economic front-runners in Sub-Saharan Africa. Following stagnation in the early eighties, in recent years a number of major policy reforms have produced a welcome spurt of economic growth. As the Kenyan economy enters the nineties, however, there are worrying signs that this lead is eroding.

Statement by the IMF

In his statement (Annex E), Mr. Peter Heller, Division Chief for the East Africa Division, provided an assessment of Kenya's performance under the IMF supported Enhanced Structural Adjustment Facility (ESAF) which began in 1989. He stated that under the present ESAF arrangement, the Kenyan authorities adopted a strong policy program, combining tight macroeconomic policies with continuing structural reforms in such areas as trade and financial liberalization, budget restructuring, parastatal reform, social sector reform, and price decontrol. The 1991/92 budget calls for a sharp reduction in the overall deficit from about seven percent of GDP to about two percent of GDP, with a correspondingly tight monetary policy. Non-concessional borrowing is to sharply contract in 1991 and 1992, relative to that of 1990. The program seeks to reduce the external current account deficit (excluding official transfers) to 6.3 percent of GDP in
1991/92 and 5.5 percent in 1992. Provided that the remaining external financing requirement of about SDR 100 million can be met, gross reserves should rise to the equivalent of 1.6 months of imports by June 1992 and to about two months of imports by end-1992 (from about one month of imports in mid-1991). Although real GDP growth is expected to fall to four percent in 1991, growth should be able to recover to five percent in 1992, primarily reflecting a recovery of agricultural production and a rise in investment activity. Inflation is now higher than anticipated, increasing to eighteen percent at end-September, as measured under the old CPI basket, and about twenty-two percent under the newly developed CIP basket. Thus, it will be critically important to adhere to the monetary targets of the program to begin to decelerate inflation by end-1991 and to reduce it substantially in 1992.

19. Mr. Heller noted that the significant reduction targeted for the 1991/92 budget deficit is an important condition for the achievement of these macroeconomic policy objectives. The principal task ahead is to ensure the realization of the full budgetary adjustment envisaged in the program. This will require continuing vigilance in budget monitoring and execution. Particular attention must be paid to preventing overruns in expenditure and a recurrence of last year’s recourse by large parastatals to government financing of their debt service beyond the amount budgeted.

20. In this regard, the considerably higher than envisaged budgetary deficit of seven percent of GDP at the end of fiscal year 1990/91 was disturbing, as well as the resulting larger than targeted growth in liquidity. Equally worrisome, at end-September, the preliminary data suggest that while revenue collections are broadly on track, overall deficit financing appears significantly larger than would have been expected. Some of the larger state corporations have contributed significantly both to a drain on the budget and to expansionary pressures on the balance of payments. Mr. Heller noted that, from the Fund’s perspective, policy and management reforms in the larger parastatals which are not intended for divestiture are at least as important for macroeconomic adjustment as the impact from divestiture of nonstrategic firms.

21. To ensure the effective implementation of monetary policy, it will be important to restrain overall credit expansion sufficiently to a rate consistent with the inflation reduction and reserve accumulation targets, while allowing an adequate expansion in credit to the private sector. The recent introduction of convertible bearer foreign exchange certificates to encourage the surrender of foreign exchange increases the urgency of ensuring that supporting fiscal and monetary policies are sufficiently tight, with due consideration being given to the monetary implications of the new certificates. The financial liberalization program continues to progress as targeted with the recent de jure removal of all ceilings on interest rates. With treasury bill yields effectively market determined, open market operations commenced in June; this should reduce the need for direct credit controls and reinforce the role of indirect monetary policy instruments. Also in the financial area, it will be necessary to take steps to address the weaknesses of some financial institutions.

22. In the external area, the ESAF arrangement calls for continuing actions to reduce anti-export biases in the economy. In this connection, the final phase of the import liberalization program was completed in June 1991 with the shifting from quotas to tariffs on almost all remaining restricted items. Average tariffs on already liberalized imports were reduced further, with the intention to continue tariff reductions beyond the ESAF period. Exchange rate policy over the last two years has largely restored Kenya’s competitiveness in exports, and the authorities intend to monitor
developments in domestic competitiveness so as to maintain this position. To further enhance efficiency, during 1991/92 the General Price Control Order will be abolished, and a significant number of items under the Specific Order will be decontrolled, while taking care to consider the impact on the more vulnerable groups.

23. Mr. Heller noted that one area of continuing concern is that recent structural reforms in the trade, financial, and pricing policy environment have been insufficient to induce significant new inflows of foreign private investment capital. This suggests the need to create a conducive environment for such investments, including transparency in the implementation of existing regulations and the assurance of an effective one-stop investment approval process, and a progressive easing of restrictions on outward transfers of profits and dividends.

24. Mr. Heller concluded with the observation that the policy package should be strengthened even further as the need arises, with the objective of achieving a viable external position. To facilitate such a determined implementation of the adjustment effort, Kenya’s access under the third annual ESAF arrangement was augmented by SDR 20 million. He urged donors to support Kenya with similar additional efforts.

Discussions

25. Generally, donors expressed strong concern about slow progress in the implementation of the economic reform program, poor governance, and alleged corruption in high places. On the economic side, participants acknowledged Kenya’s historical economic lead in the region. They also acknowledged the Government’s success in sustaining economic growth throughout the second half of the 1980’s, in implementing important structural reforms in trade and the financial sector, and in avoiding debt rescheduling. However, they expressed concern that Kenya was consuming its lead as a result of slippages in program implementation and eroding business confidence in the country. The latter was reflected in capital flight and the rapidly declining levels of private investment. They attributed these to the strain exerted on the economy by the large and inefficient parastatal sector, the expanding civil service, and continuing problems in the management of public expenditures, despite earlier reforms in this area. Delegates also expressed disappointment that despite previous Government promises to move decisively to address these problems, very little had been done. Hence, there was a need for tangible results rather than statements of intent.

26. The delegates argued that the deficiencies in the public sector were linked to weaknesses in governance, including the lack of transparency and accountability in the Government. More generally, some speakers also observed that there was a strong link between economic liberalization and political reform. Those speakers called for the Government to respect individual rights, including international standards of freedom of speech and assembly. In this regard, many speakers expressed concerns over the recent arrests of political demonstrators, and observed that little progress could be made unless the political system was opened up. Delegates also called upon the Government to take decisive actions to substantially reduce corruption.

27. In response, Professor Saitoti outlined the Government’s plans for reform of the public sector, including public enterprises, as well as its intent to open up the political process, citing
President Moi’s recent statement that Kenya will undertake political reform in due course. He emphasized that to keep peace and stability, which have been fundamental to Kenya’s economic success since independence, any political change would have to be orderly and carried out in accordance with the laws. He also stated that the Government’s resolve to eradicate corruption was evidenced by the recent Cabinet reshuffle, changes in the leadership of the civil service, and by the proposed establishment of an anti-corruption unit.

Concerning public enterprises, the Vice President stated the Government’s determination to proceed with reforms in a systematic and transparent manner. He provided details of a number of tangible steps which have already been undertaken to complete divestiture actions that have been pending for some time. These include the President’s recent appointment of a high-powered committee with the mandate and capacity to guide and oversee implementation of the privatization component of the Government’s parastatal reform program. He also noted that the Government, through the Capital Markets Authority, had announced the privatization of 139 parastatals, and that the sheer number and diversity of institutions attest to the enormity of the Government’s task.

Public Sector Management

The Chairman noted that many of the issues to be addressed during this session were in fact dealt with during the extended discussion of the Vice President’s opening statement, and in the Vice President’s response to the concerns raised by donors. The Vice President agreed that his statement on public sector management issues was in fact incorporated into the previous discussion, and therefore volunteered to waive his presentation all together (The Vice President’s formal statement is attached as Annex F). The Chairman then called upon Bank staff to present an abbreviated statement on public sector management.

Statement by the World Bank

In his presentation (Annex G), Mr. Colin Bruce, Country Economist for Kenya, noted that there are at least two compelling and related arguments why parastatal reform should be undertaken in Kenya. First, the parastatal sector is a net drain on the Government’s budget. In FY91, the net outflows were equivalent to at least one percent of GDP. Second, data recently put together show that the parastatal sector is using labor and capital so inefficiently that if these resources were transferred to the private sector, the economy could grow faster by about 2 percentage points a year. Mr. Bruce stated that although privatization is an important component of a parastatal reform program, it should be viewed as part of a broader effort to promote production efficiency, strengthen competitive forces in the economy, and support entrepreneurial development. Experience indicates that divestiture programs that are accompanied by regulatory and institutional reforms have shown better results than programs undertaken in isolation from such reforms.

Mr. Bruce also spoke about the need for civil service reform stemming from the expansion of the government machinery which has made effective coordination difficult, has created duplication, and has fostered jurisdictional disputes between ministries. In addition, the Government has become fragmented and multi-layered, and staff numbers and the wage bill have increased.
significantly. He argued that civil service reform should give the highest priority to: (i) streamlining the functions and organizational structure of Government to avoid duplication and redundancies, and achieve better organizational synergy; (ii) downsizing staff in line with the rationalized functions and organizational structure; and (iii) reforming the pay structure and personnel procedures so as to achieve an appropriate mix of staff at all levels, who are motivated and equipped to function effectively and efficiently. He noted that while other issues such as improving training, accountability, and capacity utilization are important, independently none of these would address the immediate and longer-term need to both generate budgetary savings and improve productivity.

32. Mr. Bruce concluded that while some improvements in the process of expenditure allocation have been achieved through the Budget Rationalization Program and the Public Investment Program, the underlying structural factors which drive the fiscal deficit and constrain public sector productivity remain intact. Specifically, reform is urgently needed to redefine and restructure the organizational structure of the civil service, downsize its staff, and provide adequate levels of non-wage O&M. Also, the Government needs to install transparent mechanisms for divestiture while expanding the implementation of the parastatal program to include regulatory and institutional reforms.

Discussions

33. In a brief discussion, delegates agreed that vigorous action is urgently needed to reduce the share of the wage bill in Government expenditure, thus releasing resources for operation and maintenance, and to improve the productivity of the civil service. Delegates welcomed the Government's intention to proceed with a program of civil service reform, with donor support. They also welcomed the Government's stated intention to ensure transparency in the divestiture of public enterprises along the lines presented in the Government's parastatal reform strategy paper, while underlining the importance of accelerated and decisive implementation.

Human Resource Issues

Statement by the Minister for Planning and National Development

34. In his statement (Annex H), the Minister for Planning and National Development, Dr. Zachary Onyonka, commented on recent developments in population, education, health, the labor force, and women. He noted that a few years ago Kenya had the world's highest population growth rate, and that this had placed a tremendous burden on social infrastructure. However, today the situation has changed: population and fertility rates have declined, and contraceptive use has increased significantly. He attributed these achievements to large investments in education and the expansion of school enrollment, the effective implementation of the Government's family planning policy, the rapid decline in infant mortality in the 1980s, and, more generally, to the impact of social programs which have succeeded in changing attitudes towards family size.

35. In education, the Minister noted the need to rationalize Government expenditure in the sector while expanding enrollment at primary and secondary levels especially in the arid and semi-arid areas. These dual objectives will be attained by capping the number of primary and secondary school teachers, and through an increase in the ratio of pupils to teachers, and the expansion of boarding facilities while exploring alternative delivery systems in the arid and semi-arid areas. He
also noted the Government's ongoing attempts to rationalize the use of resources at the universities. The Government is introducing measures which include a levy of 6,000 shillings per year from all students. Also, loans will only be available to students in need and will not exceed 17,500 shillings per student, and in order to ensure access to outstanding students from low income families, bursaries will be made available for roughly 20 per cent of all students.

36. In health, the Government is considering the introduction of an adjustment program for the sector. The aims will be to improve the management of the sector while increasing the budgetary allocations for primary health care. The Minister noted that user fees were introduced, but are being reviewed to ensure access to the poor.

37. The Minister outlined the Government's approach to employment creation: the stimulation of agricultural smallholder growth and the promotion of small-scale enterprises and informal sector business. He noted that Sessional Paper No.2 on Small Enterprises and Jua Kali Development will soon be published. In this paper, the Government's role is defined as that of providing the enabling environment in which entrepreneurs can emerge. The Minister also noted that a recent Presidential Committee on Employment made several recommendations for reducing unemployment, including the creation of a rural infrastructure program that would benefit agriculture and small scale enterprises in the rural areas.

38. The Minister stated that despite the progress made to increase women's opportunities, a lot remains to be done. Some of the measures to remove the disadvantages include the development of indicators to enable planners to address gender issues in the preparation of programs, and increased technical training opportunities for girls. Public agencies which provide loans to farmers will be alerted to the need for special measures aimed at increasing greater access to credit by rural women.

39. The Minister concluded by noting that reforms of the civil service and parastatals will have short term adverse effects on employment, and therefore the attainment of the objectives of growth and development will require the understanding and support of the donor community.

Statement by the World Bank

40. Mr. Nicholas Burnett, Senior Economist, presented a statement by the Bank on Human Resources (see Annex I). He stated that unless the Government tackles some of the economic problems highlighted by previous speakers, Kenya's record of economic growth as well as its impressive set of human resource achievements will be threatened. He noted that despite apparently entering a demographic transition, characterized by fertility reduction, Kenya's population is continuing to grow very rapidly. This has implications for employment, the provision of social services, and for poverty alleviation. Failure to accelerate economic growth will result in growing unemployment, and thus he welcomed the finalization of the report of the Presidential Committee on Development and Employment, whose very production is a recognition of the employment problem.

41. Mr. Burnett noted the difficulty of the Government's task. Not only must it maintain and even accelerate economic growth to permit social progress, but at the same time, some of the very
steps necessary to maintain growth have short term implications for social progress. A first issue is the provision of appropriate resources in a very tight fiscal situation, requiring hard choices on efficiency, cost sharing and equity. A second, particularly complex, issue that the Government will have to face as it takes steps to reduce the drag of the public sector on the economy, will be the addition of retrenched public employees to the ranks of the unemployed, unless the reform of the public sector is handled very carefully and appropriate transitional safety nets are put in place.

42. Mr. Burnett welcomed the steps taken by the Government to contain the growth of the education sector recurrent budget, and a Cabinet decision to reintroduce outpatient consultation charges at public sector health facilities to complement those already in place for inpatients. Finally, the Government has sustained its efforts to encourage fertility reduction. These steps have been difficult. They are only a beginning, however, and will require extension in the coming years. Employment is now on the Government’s agenda and women also should be. Social policy, human resources and medium term objectives must not be forgotten in the natural tendency to focus on the immediate economic issues. There is also a need to gather better information on regional and income disparities, and on the impact of the adjustment reforms on Kenya’s population, particularly the poorest households. The Household Welfare Monitoring System that the Government is now putting in place is thus particularly urgent and deserves donor attention to fill its unmet financing gap.

43. Mr. Burnett noted that although the social sector ministries are by far the largest ministerial employers, once all teachers and health workers are included, they are among the weakest ministries in terms of internal management and suffer from a combined lack of reliable data and analytical capacity. Weak service delivery programs also need attention; an important example is nutrition where responsibility straddles several ministries, including Planning, Health and Agriculture, and none takes appropriate overall responsibility. As noted earlier, programs are also urgently needed to deal with renewed and new problems like malaria and AIDS.

44. He stated that these issues are not unique to Kenya, and other countries in Eastern Africa face many of them, to differing degrees and without the advantages Kenya has of past progress and a record of economic growth. Their common elements have prompted the Bank’s Eastern Africa Department to take a look at how it does business with regard to poverty and social policy, and to decide to establish a Poverty and Social Policy Unit in its Nairobi office to meet the needs of Kenya and its neighbors in the Eastern Africa Department.

Discussions

45. In a brief discussion, delegates acknowledged Kenya’s solid achievements in this area, as well as the policy reforms recently announced by the Government. These included the introduction of student fees at the universities, and the decision to reintroduce outpatient treatment charges at Kenya’s public-sector health facilities; in both cases including mechanisms to protect the poor. However, there were concerns about the perceived gap between intent and practice, and delegations urged the Government to follow-through on the implementation of the policy reforms.
External Finance Requirements
Statement by the World Bank

46. Mr. Michael Carter, Division Chief, presented the Bank’s statement on its strategy for Kenya (see Annex J). He stated that the levels of support provided by IDA to its developing country members is based on an assessment of Government efforts to reduce poverty through sustained economic growth and broad access to basic social services. Progress towards this overall goal is predicated on sound macroeconomic management and usually requires strongly implemented reforms to address structural obstacles to growth and development in key sectors. Without a stable economic environment, sectoral reforms will neither pay off nor be sustainable. Sound macroeconomic management is therefore a precondition for the Bank’s ability to sustain current level of activity, and in particular, to provide quick disbursing support to structural reforms. However, recent economic developments have raised concerns about Kenya’s macroeconomic management. Provided macroeconomic management is adequate, a substantial although declining share of Bank lending can be quick disbursing. The amount of such financing depends on progress in implementation of structural reforms in key sectors; delays in these reforms imply a reduction in the lending program.

47. Mr. Carter expressed concern about the slow progress in undertaking reforms of parastatals and in the energy sector. In both cases, policy reforms could be supported with adjustment operations, as soon as strong reforms are underway. There is also an urgent need for structural reforms to improve the efficiency of Government expenditure, including civil service reform. Here too, the Bank is willing to provide appropriate support.

48. The Bank is placing increased emphasis on the Government’s efforts to reduce poverty, and this is the main rationale for support to human resource development, and the Government’s welfare monitoring system. The provision of safety nets for those affected by the Government’s planned adjustment measures would be integral components of any IDA support to parastatal and civil service reform. In addition, the Bank’s next economic report will provide an overview of poverty and employment issues in Kenya as the basis for designing further Bank support in this area.

Statement by Participants

49. Many delegations were unable to indicate the level of financial support, particularly of the quick-disbursing kind, that they would be willing to commit for 1992 and beyond, while a few suggested large cuts in their aid programs to Kenya. Donors emphasized that there is growing competition for increasingly scarce donor resources, and that aid programs are being reexamined with a view to ensuring the most effective use of these resources in helping to improve human welfare. While not walking away from Kenya, most of the donors emphasized that they wanted to see actions rather than further statements of intent in both economic and political spheres. Specifically, delegates called for: better governance, particularly with respect to corruption and human rights including freedom of expression; expenditure control; civil service reform; and the rapid implementation of parastatal reform.

50. Delegates emphasized the strong connection between the quality of governance and economic progress. In this regard, they emphasized that capital flight and the decline in private investment are
symptoms of eroding confidence in Kenya, and they stated that the underlying causes are corruption
and, relatedly, the lack of accountability on the part of those entrusted with safeguarding public
resources. Many speakers observed that consequently, there is an urgent need for political reform
to enhance accountability, and to guarantee basic freedoms of speech, assembly and association.

51. Many speakers thought that a specific financial pledge during the CG would be meaningless,
and that it would be more constructive to focus on the economic and social reforms required for
continued external assistance. Some delegates called for another round of consultations in about six
months to review progress in these areas, and as a basis for indications of further external assistance
to Kenya.

Closing Remarks by the Kenyan Delegation

52. In his closing statement, Vice-President Saitoti expressed his gratitude for the frank and
constructive discussion of economic and social issues. He emphasized that the Government is
committed to addressing those concerns raised during the meeting: the need for civil service reform,
the need for the transparent and vigorous implementation of a divestiture program, and the need to
reduce the budget deficit. He noted that many delegates had expressed the view that Kenya must
maintain its economic lead in East Africa. He agreed that there is a need for even stronger
adjustment measures to restore investor’s confidence and attract foreign investment. The Vice
President also welcomed the discussion of social issues and donors’ acknowledgment of past and
ongoing progress in this area. However, he noted that there was a need to focus more sharply on
Kenya’s most vulnerable, and to expand access to basic social services to all.

53. The Vice President restated the Government’s commitment to political reform, but
emphasized that this must be undertaken in an orderly manner and in accordance with the rule of
law. He also restated his Government’s strong commitment to the eradication of corrupt practices.

54. In concluding, the Vice President noted that the meeting had witnessed a convergence of
views between the Government and donors on an agenda for reform. He expressed his gratitude for
the breadth and frankness of the views discussed, and therefore considered the meeting to have been
highly successful.

Closing Statement by the Chairman

55. In his closing remarks, the Chairman thanked the delegations for their constructive statements
made during the course of the meeting. He also expressed his appreciation to the Kenyan delegation
for their candor and willingness to openly discuss the complex and difficult economic and political
issues raised during the meeting. He observed that this was a particularly difficult Consultative
Group meeting, but that all participants can be proud of its outcome. The conclusion is proof that
the CG process is sufficiently robust to enable the frank discussion of difficult issues.

56. In summarizing the discussion, the Chairman noted that there was agreement that Kenya has
enjoyed a marked degree of economic success. Hence, the focus of the meeting was on defining
those areas which need to be addressed if economic success is to be sustained. The two broad areas of concern raised throughout the meeting were on governance issues and on the scope and pace of economic reform.

57. He stated that there was general agreement that the actions proposed by the Government’s delegation, when implemented, will quickly restore the enabling environment for sustained economic development. These actions include: (i) addressing current macroeconomic imbalances by reducing the budget deficit; (ii) redefining the role of the Government through comprehensive civil service and parastatal reform programs aimed at improving the efficiency of public expenditures and at creating an environment supportive of private investment initiative; and (iii) wider access to social services building on Kenya’s credible record in this area. Hence, donors were encouraged that the Government is well aware of what needs to be done, and welcomed the Government’s stated intention to act on these proposals. However, the Chairman noted that delegates expected the Government to translate these statements of intent into concrete actions.

58. The Chairman observed that donors were not walking away from Kenya, but, to the contrary, were intent on continuing the partnership in Kenya’s economic development. He noted that, as suggested by a number of donors, there was a need to meet in the near future, perhaps within six months, to review the Government’s progress in the areas of concern raised during this meeting, and to explore what donors can do to continue to support Kenya’s development efforts.

59. The Chairman concluded by noting that this would be his last Consultative Group meeting for Kenya before assuming his new responsibilities as Director of the East Asia Department. He thanked all delegates for their cooperation and thoughtful participation in the Consultative Groups, and called upon Mr. Francis Colaço, his replacement as Director of the Eastern Africa Department, to formally adjourn the meeting.
MEETING OF THE CONSULTATIVE GROUP FOR KENYA

Paris, Monday-Tuesday, November 25-26, 1991

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MEETING OF THE CONSULTATIVE GROUP FOR KENYA
November 25 and 26, 1991
Proposed Agenda

Morning Session 10:30 am to 1:00 pm
1. Chairman's Opening Statement
2. Statement on the Economy by the Vice President and Minister for Finance
3. Statement on the Economy by the World Bank
4. Statement on the Economy by the IMF
5. Discussion

Buffet-Lunch hosted by World Bank at Park Avenue Hotel

Afternoon Session (2:30 pm to 5:30 pm)
6. Statement by the Government on Public Sector Management Issues
7. Statement by the Bank on Public Sector Management Issues (Civil Service Reform, Parastatal Reform and the PIP)

Coffee Break
8. Discussion

Reception hosted by Kenya for all at Park Avenue Hotel at 7 p.m.

Tuesday, November 26, 1991

Morning Session (9:30 am to 1:00 pm)
9. Statement by the Government on Human Resources Issues
10. Statement by the Bank on Human Resources Issues
11. Discussion

Coffee Break
12. Statement on Financing Requirements by the World Bank
13. Statement by Delegations on their Assistance Programs

Afternoon Session (2:30 pm to 4:00 pm)
14. Concluding Statement by the Vice President and Minister for Finance
15. Chairman's Closing Statement.

Mr Chairman, Your Excellencies, ladies and gentlemen:

Welcome

On behalf of the Government of Kenya and on my own behalf, I extend a very hearty welcome to all of you attending this meeting of the Consultative Group. We very much appreciate this opportunity to have yet another round of useful discussions with all of you. We are very thankful to the World Bank for hosting and organizing this meeting.

At the outset, I would like to put on record the valuable and timely assistance, we have received from the international donor community, not only in financial terms, but also and perhaps more important by the friendly advice and suggestions on a number of national economic and social issues. The financial assistance has been substantial and timely, coming as it did in the context of a major liberalization of our trade policy, and has helped us in maintaining import levels, despite the very large deficits in our balance of payments. The people of Kenya are indeed grateful to your countries and organizations for this assistance.

For the Government delegation this meeting is a very important forum, not only for putting forth our policies, programmes, points of view and constraints, but also to understand and appreciate your thinking and approach on several issues of mutual concern.

Development Strategies

Kenya’s development strategy for the nineties continues to be guided by the overall policy framework articulated in our Sessional Paper No. 1 of 1986 on Economic Management for Renewed Growth. This policy framework, which identifies the measures to
be implemented to deal with the growing employment needs and to achieve a faster rate of growth of the economy, has been and will continue to be the basis on which we designed and implemented a series of economic adjustment programmes. Here, we would like to put on record the valuable assistance that we received from the World Bank and the IMF in the design of these programmes within our policy framework and in coordinating the flow of resources to sustain their implementation. In this regard, I am carrying a document on the outcome of our reforms, which was available too late for distribution in Nairobi.

In retrospect, I can say with confidence, and I am sure that most of you will agree with me, that but for the effective implementation of these adjustment measures in a number of critical sectors, the Kenyan economy would not have withstood the impact of several international events in the late eighties and still maintained a sustained growth of over 5% per annum, during the last five years. I am referring to the collapse of the coffee market, the volatile and speculative currency fluctuations, the growing recessionary tendencies in industrial countries, and more recently, the Gulf crisis.

**Implementation of Sector Adjustment Programmes**

The adjustment programme we have been implementing, starting with the agricultural sector reform of 1986, are well known. However it is worth recapitulating briefly the actual achievements so far, to provide a background for today's discussions.

**Agriculture Sector Reforms**

In line with the strategies identified in Sessional Paper No. 1 of 1986, we started with a phased reform of the sector, to overcome some of the major constraints through improvements in incentives. Prices of several items of concern were decontrolled: starting with insecticides in 1986, all categories of meat in 1987, farm machinery and spares in 1988, animal feed and animal salt in 1989, and fertilizers, UHT Milk, agricultural chemicals and barbed wire in 1990. Again, to improve input markets, small packaging for fertilizers and a cost sharing programme to improve the delivery of veterinary services were introduced.
On the marketing side, payment systems have been streamlined to assure timely payments to maize, coffee, cotton and pyrethrum farmers and major marketing boards have been restructured to make them more efficient and competitive. Further restructuring of the cotton and cereals boards is also under way, and with the liberalization of maize marketing, the private sector is now playing a much larger role in the marketing of this commodity. In the livestock sector also, private companies have been allowed to market fresh milk and other products. We have also simplified export procedures and increased the availability of packing material to promote horticultural exports. Indeed, I would like to take this opportunity to reiterate our commitment to continue with the liberalization measures in the sector to assure a much larger role for the farmers and the private sector.

Kenya's agriculture is indeed very dependent on the seasonal variations in rainfall. However, it is worth noting that the sector has performed significantly better in the latter half of the eighties, as a result of the policy reforms, I just described. Overall agricultural production which increased by 2.5% per year between 1979 and 1985, maintained 4.0% per annum on average between 1985 and 1990. Also during this period, investments in agriculture increased rapidly at an average annual rate of K£ 64 million in real terms.

As a result of the better marketing arrangements put in place, the value of pyrethrum increased from K£1.9 million in 1984 to K£12 million in 1990, and horticultural exports increased from K£11.3 million in 1980 to K£159.9 million in 1990. In fact the value of horticultural exports increased by 32% and livestock production by 9.0% in 1990. We also have evidence from a study of grain marketing that the liberalization of grain movement has led to a significant lowering of maize prices in the deficit areas by as much as 20%, whereas farmers in surplus areas have been increasing their take home collections by more than 10%. We are confident that these trends will continue.

**Trade and Industry Reform**

We have made substantial progress since 1988 in trade reform and in enhancing incentives for investment. The specific measures
implemented include, (a) the reduction in tariff bands from 25 to 12 and the removal of the top ten bands leaving a maximum of tariff of 70% now instead of 170%, and a weighted average tariff of below 40%, (b) the removal of quantitative restrictions, which now cover less than 1% of all items and (c) the implementation of a system that ensures the accelerated processing of import applications and release of foreign exchange, from six months in the past to an average of less than a fortnight.

Again, to create conditions for increased competition and efficiency, significant progress has also been made since 1986 in decontrolling prices. With the removal of all categories of goods except six in the General Price Control Order and 43 of the items in the Specific Control Order, the prices of some 76 product categories have been decontrolled. The Government is committed to move further in this direction and fully decontrol all goods under the General Price Control Order and maintain only a very few items under the Specific Price Control Order.

We have also implemented several institutional and legal changes to promote investments, such as changes in the Foreign Investment Protection Act to remove discrimination on equity participation, the legislative measures carried out in regard to restrictive practices and price controls and the establishment of the Investment Promotion Center, as a one step clearing centre.

Export Promotion

Government recognizes the fact that the long-term potential for more rapid growth is critically dependent on our capacity to increase exports. Towards this end, several measures have already been implemented, including a reduction of the level of effective protection, to which I just referred, improvements in export incentives, provision of trade finance and improved services for exporters, and a further easing of the domestic regulatory framework affecting investment, trade and exports.

Again, with a view to reduce the anti-export bias, exporters have been enabled access to inputs at international prices, through the
manufacturing-under-bond (MUB) and a duty/VAT exemption scheme. The MUB programme has recently been improved by simplifying bonding requirements, allowing firms to sell rejects in the domestic market and extending the MUB to three new urban centers. Also, the number of eligible products under the exemption scheme will be broadened gradually with the aim of adopting a negative list during 1991/92.

Legislation was enacted last year to facilitate the functioning of public and private Export Processing Zones (EPZs) and a small private sector funded and operated EPZ began operations in January 1991. Kenya's EPZ legislation provides a package of strong incentives, competitive with other locations around the world. With assistance from IDA the construction of an EPZ in Athi River, Nairobi is expected to begin in December 1991 and completed within fifteen months. A pre-shipment export finance scheme has also been implemented permitting commercial banks to rediscount export bills at Treasury Bill rates. Government has also completed a preliminary design of a scheme to provide firm level assistance and the scheme is expected to commence by December, 1991.

Several measures have already been taken on the regulatory framework, such as the elimination of the licensing requirement for individual export consignments, reducing the number of products requiring licensing from 38 to 19 and consolidation of licenses required under the Trade Licensing Act into three types. The Government is also considering further reforms in this direction which will result in the consolidation of separate registrations currently required under various legislation into one, simplification of the license renewal process and retention of only a minimum set of approvals for all new investments.

**Exchange Rate Policy**

In order to support the measures that I have just described, the Government is committed to continue to pursue an appropriate exchange rate policy which will also ensure that the recent gains in domestic relative prices for tradable goods production are maintained. In this connection, I must also bring to your attention some important and recent decisions of the Government to issue
foreign exchange bearer certificates, as a flexible and innovative new window to encourage the freer flow of resources into the economy coupled with the removal of foreign exchange declaration forms. These measures are indeed a major steps towards the further liberalization of the exchange rate regime, which will also encourage investments within the economy.

Performance of Industry and Exports

Again, as in the case of the agricultural sector we are beginning to observe very important trends in the economy, which indicate the beneficial results of the reform programme. Throughout the reform period, the contribution of the manufacturing sector to real GDP has grown consistently faster than GDP in general and has averaged 5.7%. From the recession period of early eighties, investment in manufacturing in real terms has been growing at a very high 11.5% per year, in contrast with 3.3% rate of growth of investment for the economy as a whole. On the export front, manufactured exports have increased in real terms by 70% since 1986, against a mere 7% for overall exports. Furthermore, there is strong evidence of a substantial diversification of the Kenyan economy, namely that the value of non-traditional exports has increased from 25% of the total before the reform to over 40% now.

Financial Sector Reforms

In the financial sector, the powers of supervision of the Central Bank over financial institutions have been strengthened and a Deposit Protection Fund has been established to enhance confidence in the sector. A major restructuring of some ten weak financial institutions has also been carried out, leading to the establishment of the Consolidated Bank of Kenya last year.

Simultaneously with these institutional strengthening, interest rates have now been completely de-regulated effective July, 1991 and several new instruments have been developed, including the system of auctioning of Treasury Bills and issuance of bearer bonds to deepen the financial sector, to promote secondary markets and national savings.
Capital Markets Authority and DFI's

Perhaps the most important development in the financial sector is the establishment of the Capital Markets Authority in 1990 to promote the development of long-term capital markets and to facilitate access to organized markets by companies in the private sector which are now obtaining finance from informal sources. Further progress is being made in this direction through the issuance of shares by a number of public sector institutions and in ensuring that the price of public issues of domestic corporate securities will be determined by market forces.

The Government has also taken firm measures, again with assistance from the World Bank, for the financial and organizational restructuring of two of the leading development finance institutions in the public sector, namely the Industrial Development Bank and the Industrial and Commercial Development Corporation. This will ensure that profitability and financial sustainability are emphasized and these institutions are able to enhance their role as providers of venture capital and financial advisory services.

Population Trends

Finally, let me place before you an important aspect of our economy, namely the recent trends being noticed on the rate of growth of population. We have witnessed a marked reduction in the rate of growth which has by 1989 slowed down to 3.6% with major falls in both rural and urban and in the total fertility rates. Thanks to the effective implementation of family planning programmes for nearly two decades and the huge investments in primary and secondary education, we are beginning to witness important indicators of fundamental behavioral changes. These are, an increase in contraceptive use from 17% to 27%, a substantial decline in the desired family size, a considerable increase in the number of married women who desire fewer children and an increase in female enrolment in primary and secondary schools. In order to consolidate what appears to be the beginnings of a demographic transition, the Government is committed to strengthen the programme and the delivery of family planning and rural health services.
Recent Economic Performance

Factors Contributing to a Slowdown in 1990

Whereas our economic adjustment and sector reform programmes have so far been on track, as I have just described, our performance last year was very much subject to factors beyond our control. The Gulf crisis had a devastating effect on our economy mainly through the 30% to 49% increase in the domestic prices of petroleum products in September, 1990, combined with a sudden drop in tourism, and a decline in the demand for Kenya’s exports in the region. These factors, together with a further fall in coffee prices, contributed to a slow down in the economy and, for the first time in four years, Kenya registered a rate of growth of less than 5%.

It is very important to appreciate that the Gulf crisis introduced a major set of constraints to our efforts to restructure the economy and to maintain stability. The increase in prices of petroleum products, which I just referred to, had its effects in the manufacturing and transportation sectors. Added to this, the increase in the producer and consumer prices of basic food items, salary increases for the lower job groups in the public sector and the depreciation of the Kenya Shillings, contributed to inflationary pressures in the economy and inflation as measured by the Nairobi existing consumer price index, increased to 12.6% in 1990, compared to 10.5% the previous year.

Reasons for Poor Fiscal Performance

On the fiscal side we faced a series of unanticipated problems in 1990/91, partly as a result of the Gulf crisis and partly due to domestic constraints. A major contributing factor, resulting in our fiscal performance falling short of our own expectations, was once again the depreciation of the Kenya Shillings, which resulted in a number of State Corporations being unable to meet the Shilling contributions needed for their debt servicing. Consequently, Government had to honour its guarantees, as any default would have placed a black mark in our otherwise enviable and long record of servicing our obligations. Under these conditions, the long term implications of defaulting in our debt service obligations would have been far more adverse, than missing ESAF targets.
Another major factor which contributed to our less than optimal fiscal performance under these conditions, was the shortfall we had to encounter in the realization of targeted revenues. When we put together the 1990/91 estimates, we did not in fact visualize a slow down of this magnitude in our economy, which I referred to earlier. The decline in the growth rate did lead to a decline in the realization of revenues, particularly from the coffee sector. In addition, we did experience considerable administrative difficulties in enforcing the collections of the newly introduced VAT. These together with some adjustments we had to make for the advanced receipt of some revenues for 1990/91 in 1989/90 and a decline in import revenues as a result of the slowdown in imports, led to a substantial decline in revenues, contributing to the fiscal problems.

Ladies and Gentlemen, in this regard I would also like to draw your attention to the austerity measures we discussed in this very forum last year. In fact, but for the timely implementation of these measures, we would have found it extremely difficult to remain within reasonable limits on expenditures. However, I must admit that there were some slip-pages in expenditures contributed mainly by some unavoidable needs on internal and regional security and the doubling of in-take of students in universities.

It is also important to recognize that we did attack the root causes of the problem in fiscal management in several ways. First, although revenues were less than anticipated, they still grew by over 18% in 1990/91 compared to 1989/90 and amounted to 22.3% of the GDP. On the other side, several drastic measures were initiated in the State Corporation sector, both from a short and a medium-term point of view. The restructuring of the Kenya Airways Board and the steps taken to review KPTC's activities leading to privatization of many of them are some of the short term measures, which will have a good impact on the fiscal situation. Simultaneously, we developed an started implementing in right earnest, the State Corporation privatization programme, the fiscal effect of which will be felt in the medium term.

Thus, the larger than anticipated budget deficit of 5.8% in 1990/91 should be viewed not only in the context of these serious constraints, but also keeping in view the substantial progress that has been made on all other aspects of the adjustment programme,
which I described earlier, and the specific measures initiated, which will attack the basic structural problems in the budget.

**Balance of Payments Out-turn in 1990**

On the balance of payments, our current account deficit declined to 5.4% in 1990, compared to 7.0% in 1989, mainly as a result of a decline in the rate of growth of imports and an increase of over 22% in our export volume coming from tea, petroleum products to neighbouring countries and horticultural produce. It is important to note that while commercial imports grew by 14.3% in 1990, imports by the public sector as a proportion of total imports did not exceed 6.5%.

**Medium-term Growth Prospects and Strategy**

**Weakened World Economic Situation**

Let me now spend a few minutes on our assessment of the medium-term prospects for the Kenyan economy, which are interlinked to the projected economic performance of OECD countries. The world economy is going through a difficult period, as can be witnessed from the fact that the rate of growth of GNP for all OECD countries, who are Kenya's major trading partners declined from 3.8% in 1989 to 2.8% in 1990. Again, the rate of growth of world trade declined from 7% in 1989 to 5.1% in 1990, and is projected to improve marginally to 5.2% in 1991. These developments and projections imply that the next two to three years will indeed be difficult for the Kenyan economy, calling for an even more vigorous implementation of adjustment measures we have been pursuing since the late eighties. Apart from the weakening world economic activities which has serious implications for our export growth, there is also an increasing competition for available resources as a result of the political developments in Europe and USSR.

**Prospects for Kenyan Economy**

We therefore cannot expect any major growth in our exports in the medium-term. It is however possible that both the volume and nominal value for Kenya's tea and coffee exports could pick up
momentum on account of higher prices. Again, horticulture exports have witnessed a strong growth in the first six months of 1991 and could register a significant growth in volume and value. However, the high retail price of petroleum products and the high rate of inflation, coupled with a slow down in the rate of growth of public expenditures is likely to depress domestic demand, resulting in some further slowing down of growth in the economy.

Thus the growth of GDP is expected to slow down further to about 4% in 1991, progressively picking up towards the end of the year. We also believe that the rate of growth will pick up by 1992, with the end of recession in industrial economies. Again, other factors such as the recovery of coffee prices, strong growth of tourism, fall in the rate of inflation and further realization of benefits of structural adjustment measures, will assist in this process of recovery.

**Balance of Payments**

However we do anticipate that the adverse balance of payments situation will continue for the next two years. The details of our projections for the medium-term are given in the paper circulated for this conference and it is not necessary for me to go into them at this stage. In spite of this we are committed to continue the tempo of reform in trade policy and maintain the growth in the level of private sector imports.

**Need for Resources**

In the context of what I have just stated, a critical factor for Kenya’s rapid economic recovery will indeed be the inflow of resources into the economy. Additional resources of a substantial magnitude are therefore needed not only to sustain the trade liberalization programme, but also to fill the resource gaps during the critical transition years, till such time Kenya’s exports pick up momentum. In fact, as I had already stated before, at this critical juncture of our economy and in the context of fundamental social changes taking place, assuring the continued flow of resources is the best insurance for the continued and even more vigorous implementation of effective measures for maintaining stability.
**Medium-term Strategy**

The basic elements of our medium-term strategy are described in the discussion papers for this meeting and I do not intend to go into the details at this stage, except to emphasize on a few very important aspects.

The first of these will be aimed at ensuring macro economic stability through the implementation of a series of measures to reduce fiscal deficits and domestic bank borrowings to sustainable levels.

Second vigorous measures will be continued to be implemented to improve substantially our external position through various export promotion initiatives combined with the continued maintenance of an appropriately valued exchange rate.

Third, Government will give the highest priority to ensure a favourable macroeconomic environment to achieve a sustained non-inflationary real GDP growth rate that is higher than the population growth rate.

Fourth, measure will be implemented that will rationalize public enterprises, improve the productivity of public expenditures and generate productive employment opportunities for the rapidly growing labour force.

Having briefly outlined the broad elements of our medium-term economic strategy, I shall now briefly refer to some of the more important issues in it, mainly to provide a background for to-day’s discussions.

**Fiscal Policy Issues**

The Government is committed to ensure a very careful management of fiscal policy so that it functions as the central tool for economic stabilization and growth. Maintaining the budget deficit at a sustainable level and ensuring a non-inflationary financing of the
same, will be the critical element in our fiscal policy. Therefore, the medium-term expenditure programme visualizes a gradual reduction of the budget deficit from above 5.0% of the GDP in fiscal 1990/91 to about 2.0% in fiscal 1991/92 and maintaining it at this level for the next three years. Government expenditures, including grant financed expenditures, as a percentage of the GDP are expected to fall from about 32% in 1990/91 to 28.2% by 1994/95.

In order that these projected levels are realized, the main elements of fiscal policy in the medium-term will be (a) further enhancement of domestic resources available to the Government; (b) a gradual reduction in the share of education and health sectors in the total budget, (iii) reforms in the State Corporations sector, (iv) the implementation of the public investment programme (PIP) to improve the productivity of public expenditures and (v) a much stricter control over expenditure over-runs and commitments.

**Resource Mobilization**

The Government has already implemented several measures to ensure that revenues as a proportion of the GDP, increase from about 22.3% in 1990/91 to above 23% by 1994/95. This is being achieved through a combination of expanded bases and rationalized tax structures and through a more effective and efficient administration. I have already referred to some of the major changes, we have implemented in the tax structure. I must also mention here the steps taken in the last budget to expand the VAT tax base and to reduce the number of rates from 15 to 8, both of which will contribute to a substantial increase in revenues. In order to move as planned in this direction, a Tax Policy Unit has been established in the Treasury and a Tax Modernization Programme is being implemented. Several measures have already been implemented with the twin objectives of increasing revenues and enhancing the incentive structure.

**Reforms in Education and Health Sectors**

One of the main forces behind the increase in the rate of growth of public expenditures is the introduction of the 8-4-4 system of
education as a means of ensuring a more relevant system, taking into account the changing needs of the economy. This together with the expansion of university education, has been contributing to the increased absorption of budgetary resources by this sector. Similarly in the case of the health sector, the rapid growth in rural areas of the delivery of health services, combined with increases in the provision of curative services, has resulted in a much larger share of this sector in the total budget, than was the case a decade ago.

The Government has already implemented far reaching adjustment measures in the education sector which will have, among other improvements, the effect of gradually reducing the rate of growth of the education budget to a level commensurate with the overall expenditure targets and ensure greater efficiency in public expenditures.

With the active support from the World Bank, the programme will ensure a strict control of the growth of primary and secondary school teachers through increasing the student teacher ratio in primary education and reducing the intake of Primary Teacher Training Colleges. The major policy measures already implemented in university education, include the levy of Shillings 6,000 per year from all students as direct tuition, limiting the student loan amount to qualifying students to Shillings 17,500, reducing drastically the intake of future university students to no more than 10,000 in 1991 (compared to 21,448 in 1990) and limiting its growth to no more than 3% per annum.

A similar adjustment programme is also being implemented in the health sector, which will gradually increase the resources available to the delivery of services, particularly curative services in the urban centers and rural areas.

**State Corporation Sector Reforms**

The reforms being implemented in the State Corporations Sector, which have been documented in detail in our discussion paper, will also greatly assist the Government in reducing the rate of growth of
public expenditures. In addition to the rationalization of the State Corporations, emphasis will be placed on ensuring that the debt service obligations of such of those State Corporations experiencing cash constraints are closely monitored and advance action is taken to ensure that these are systematically discharged.

Public Investment Programme

Perhaps the most important institutional change that will enhance the productivity of public expenditures is the Public Investment Programme, the details of which have already been described in the discussion paper circulated for this meeting. This system will help the Government to achieve much greater selectivity in the inclusion of projects for funding not only in Ministry budgets but also in State Corporations. Although the first PIP covered ten major non-financial State Corporations, during this year’s exercises this coverage has been increased to 20, thus providing the Government with an effective tool for review of projects financed within this sector. Over a period of two to three years, the PIP Task Force in the Treasury will increase the coverage and will eventually extend it to all strategic State Corporations that will remain in the public sector.

In order to improve the quality of the PIP exercises an important role has been assigned to the Ministry of Planning and National Development to further improve the procedures whereby projects are formulated, appraised and approved for inclusion in the PIP as well as for assisting the sector Ministries in the review of their on-going project portfolio. The 1992/93 - 1994/95 PIP is currently being prepared as an integral part of the on-going forward budget exercises and it is expected that this document will be published in January, 1992 and will be the basis for the annual estimates for 1992/93.

During this exercise, the Treasury together with the Ministry of Planning and National Development is reviewing and assessing the relative merits of all new projects, whose total cost exceeds K£ 100,000 in selected sectors. It is also the intention of the Government to extend such a close scrutiny to the health, energy and transportation sectors during 1991/92. The project level information already compiled on project financial data is also being
used extensively to guide in the allocation of resources to projects in an advanced stage of completion and to the core and high priority projects.

**Budget Monitoring**

In regard to the achievement of fiscal targets on the expenditure side, we have taken into account the lessons of last year and have already implemented several measures that will ensure that the current fiscal year’s targets are met and no slippages are allowed. For this purpose, the Government has already put in place a system to review macro level revenue and expenditure trends on a monthly basis and to initiate appropriate corrective action to ensure that budget implementation proceeds as planned and that unanticipated changes during the year are minimized.

The macro-level monitoring has enabled us to review all aspects of budget management, such as the realization of revenues and programme finance, Ministry expenditures, debt service payments and the domestic financing of the deficit, all simultaneously, so that any constraints observed in implementing the budget as originally planned are quickly identified. As a result of these macro-level monitoring initiatives, we have already taken a series of steps to improve the actual realization of revenues and to enforce strict controls on Ministry expenditures and commitments. The monitoring system has also led to Government-wide action in regard to State Corporations, which is expected to ensure that their debt service obligations are properly discharged.

**Expenditure Monitoring System**

To support this macro-level monitoring with more detailed data, the Treasury has established an Expenditure Monitoring System to monitor on a quarterly basis the actual expenditures and commitments being incurred by the Ministries and districts, against budgeted provisions. This system will facilitate tracking of expenditures and commitments to ensure that the budgetary ceilings are being adhered to and to identify corrective action on potential expenditure over-runs in sector Ministries. The system will
also assist the Treasury in monitoring commitments on all items of expenditure, particularly Government of Kenya financed development projects, so that they do not accumulate to excessive levels and are controlled within the allocations in the annual budget.

**Government Employment**

The Government has also taken strong action to reduce the rate of growth of employment particularly at the lower job groups. As a result of the effective freezing of new recruitment to these job groups, prohibiting the filling of vacancies on other job groups, and an effective removal of the practice of providing guaranteed employment to school leavers and graduates, there has been a distinct slow down in the rate of growth of expenditures on salaries and allowances during 1990/91. The Government is committed to implement further measures to rationalize public sector employment policies and benefit packages, so that the productivity of the civil service is increased.

I am therefore confident that these institutional measures and policy reforms will strengthen the ability of the Treasury to effectively plan and implement expenditure control measures and to reach the deficit targets in the medium-term programme.

**Financing of Deficits**

In financing the proposed public expenditure programme for the next three years, Government will continue to ensure that domestic borrowings do not crowd out the private sector from the credit market. Therefore a two-pronged approach will be followed which will ensure that (a) a major part of the budget deficits is financed by concessionary borrowings from abroad in the form of project and programme assistance and (b) a major part of the resultant domestic borrowings are financed from non-bank sources.

**Foreign Financing**

In this regard, considerable attention is being given, while
formulating development expenditure proposals, to restrict severely the expenditures on 100% Government financed projects and to confine them to complete very high priority on-going projects. This will enable the Government to increase the absorption of loan financed projects in various sectors, within the overall expenditure levels. This approach will increase the financing of the deficit through external concessionary loans and is based on the actual level of donor commitments we have so far received for projects in various sectors.

The above pattern of financing of the budget deficits is indeed directly related to the net inflow of resources from abroad. As you might have noticed from the document circulated, the share of this form of financing of the development budget is projected to increase from about K£ 330.5 million this year to about K£ 400 million by the year 1994/95.

**Domestic Financing**

The domestic financing of the budget deficit is expected to be around 40% of the total deficit in the next three years. However, this could be reduced further to the extent further assistance through non-project loans and grants are mobilized. Even within a reduced proportion of domestic financing of the deficit, the Government will ensure that most of the domestic borrowings are resorted to from non-bank sources, particularly through the intense use of the new instruments developed recently and through a more aggressive selling of Treasury Bonds. The Government is therefore confident that the planned financing of the central Government budget deficit will be non-inflationary and will release sufficient resources for the private sector, particularly for export promotion activities.

**Sector Adjustment Programmes and Other Policy Initiatives**

As I said earlier, we have a good record of implementing several difficult adjustment measures in a number of sectors since the mid-eighties. Our approach for the medium-term is therefore to deepen the structural reforms in the key sectors of the economy
and supplementing such reforms with much stronger measures for maintaining macroeconomic stability, and for enabling the private sector to grow at a faster pace than before through promotion of exports.

ASAO II

The second phase of the agricultural sector adjustment operation which is now being implemented will result in the further liberalization of maize marketing, improvement of producer incentives, more efficient supply of inputs and a better management of the resources in the sector. This programme is also linked with the implementation of the market development project financed by the USAID, so that infrastructure improvements are put in place simultaneously.

Energy and Transportation Sector Programmes

With the assistance from the World Bank, the Government will soon start implementing a major adjustment programme in the health sector. This programme will lead to implementation of strategic reform measures in this sector and to an improved delivery of health services. In addition, the Government is also keen to develop sector adjustment measures in the energy and transportation sectors, both of which have very important implications for promoting private sector development.

State Corporation Sector Programme and Safety Network

The Government is also keen that the measures being implemented in the State Corporation sector be coordinated through the development of a sector lending operation. In this regard, as has already been stated in the discussion paper, the Government is seeking additional financial and technical assistance for putting in place a safety network mechanism for such of those employees of State Corporations, who may be rendered surplus during the implementation of the programme.
Priorities for External Assistance

As I said earlier, additional flow of resources into the economy is critical at this stage of our development for achieving a more rapid growth of the economy, in the light of the balance of payments problems we will be facing in the medium-term. Till such time Kenya’s exports pick up momentum, the financing of a minimum level of imports needed for the private sector could become a major constraint in the process. We are therefore seeking your active cooperation in many ways. The relevant areas are already covered in the paper we have circulated for this meeting. I shall however briefly mention two of the more important areas for joint action.

Balance of Payment Support

Perhaps the most important need for the next three years is balance of payment support without which the economy cannot grow in the direction which all of us here want it to go. In the distributed document we had assessed a financing gap of 353 million SDR’s for the three year period. Our more recent assessment of the financing gap is of the order of 416 million SDR’s million for the three year period 1991 - 1993; Although the current projections are based on a number of assumptions, we know that the magnitude of our requirement is indeed large.

As in the past, this support can take several forms such as policy oriented programme grants and soft-loans, commodity aid or import support. We are indeed grateful to the donor community for the significant commitments on the pipe line, but I would like to take this opportunity to plead with you for substantial additional commitments, so that we can close the financing gap in our balance of payments. Such additional commitments can in fact be considered through the co-financing of the export promotion, agriculture, health and education sector lending operations which have been developed with the initiative of the World Bank.
The Government is also seeking a substantial increase in project based assistance both through grants and soft loans to implement a much more rationalized portfolio of investment projects that is being developed under the Public Investment Programme. As I mentioned earlier, we have put in place overall financial plans which will facilitate an increased absorption of project loans for high priority investments in the critical sectors.

The priorities for project assistance will indeed be reflected in our Public Investment Programme. However, I would like to take this opportunity to mention the need for increased investments in the transportation sector, which could include programmes for major and access roads, and to improve rural and urban water supply.

Concluding Remarks

Finally, we are aware that this meeting is taking place at a time, when Kenya is facing considerable international criticism on a number of issues. I want to emphasize that we are indeed listening very carefully to these reactions and are in fact concerned that Kenya does not lose the good reputation, for which all of us here have worked very hard for many years to build and maintain. We are also aware that this will require on the part of the Government, some extremely difficult but necessary action.

Let me therefore take this opportunity to brief you on the current political environment in Kenya, starting with the issue of governance, which has been repeatedly mentioned in a number of places.

On this issue, somehow or other an impression is there in many places that the present Government in Kenya does not want any change. The truth of the matter is far from it. What our people have said time and again, is that we do want change - but we will embrace it in our own time and in our own way. We certainly do not want change, just for the sake of it or for purely ideological
reasons. Each society is the best judge to decide when to change and how to bring about that change. In fact we have never been static. Our ideas and concepts keep changing, as we gain more experience of developmental issues and we are constantly adapting to changes in the environment.

Our system is not at all opposed to divergent political view or the free expression of ideas and opinions, as you can see from reading of our local newspapers. The Government and indeed our President is on record, saying time and again that Kenya is not opposed to pluralism, but its introduction requires the people’s mandate, without foreign influence and through the amendment of the appropriate laws of the land in an orderly and peaceful manner.

Second, let me also refer briefly to the issue of corruption. We are very conscious that corruption undermines the enabling environment which we are trying to establish for promoting investments and exports, through several measures for liberalizing the economy. Therefore we are very much concerned about this issue and are going to take very strong action in this area. Already there has been major changes in Government, which are indeed aimed directly at establishing conditions for ensuring greater accountability and transparency in decision-making and in giving the right signals within the economy. We have also introduced an anti-corruption bill in our parliament, which strengthens the mechanism and the penalties and which will assist greatly in enhancing the public awareness of this issue. In this process, we are sure that a far better environment will be established for enforcing transparency and accountability in decision-making, covering both political leaders or administrators.

**Conclusion**

Ladies and gentlemen, what I have just outlined before you requires your careful review and understanding, so that we could discuss the possible channels for the transfer of resources in the pursuit of our common goals. As I said earlier we are very keen to listen to your own assessment of the Kenyan economy and your suggestions and comments for improving the growth prospects.
1. The Kenyan economy has faced a difficult period during 1990 and 1991, as a result of adverse external and domestic developments. When we last met here a year ago, it was clear that economic growth would slow somewhat as a result of the Gulf crisis and that in order to respond to adverse external factors stabilization measures, especially fiscal policy, needed to be strengthened. In the event, economic growth in 1990 slowed to 4.5 percent, after averaging over 5 percent during the previous five years, and is expected to slow further to about 4 percent in 1991.

2. In late 1990, as the Gulf crisis unfolded and Kenya's external terms of trade deteriorated sharply, the Government faced the need to adjust domestic energy prices and restrain the growth in aggregate demand to cushion the impact of these external factors on the economy. In September 1990, the Government raised domestic oil prices between 30 and 49 percent to bring them in line with international prices. In order to contain aggregate demand pressures, the Government revised its fiscal targets for 1990/91 in line with a tighter fiscal and monetary stance. However, as discussed in the IMF statement to follow, efforts to control the budget deficit and credit expansion during 1990/91 were inadequate. The budget deficit and money supply increased substantially, far exceeding the Government's revised targets. As a result, the Kenyan economy remains subject to major macroeconomic imbalances.
3. Although affected by adverse terms of trade, Kenya's balance of payments improved—the current account deficit fell from 7.4 percent of GDP in 1989 to 5.3 percent in 1990. This improved performance was assisted by Government efforts to cancel or postpone non-essential imports, as well as high growth in horticulture exports, tourism revenues and some non-traditional exports. A sharp reduction in net capital inflows, however, lowered foreign exchange reserves to only 1.4 months of imports by the end of 1990.

4. Since it began a series of sectoral adjustment programs in late 1986, the Government has implemented a number of measures to broaden the role of market signals and align relative prices more closely with those prevailing in world markets. Although there has been real progress in structural adjustment, the problems currently facing Kenya's economy suggest a large unfinished agenda—both in terms of deepening existing adjustment programs as well as expanding policy and institutional reforms in complementary areas.

5. In agriculture, producer prices have been improved, fertilizer imports and prices have been liberalized, and meat prices have been decontrolled. In industry and trade, the exchange rate has been managed flexibly, price controls have been substantially reduced, the marginal company tax rate has been lowered from 45 percent to 37.5 percent, the import licensing system has been liberalized, quantitative restrictions on imports have been practically eliminated, the level and dispersion of tariff rates have been lowered substantially, export incentives are being improved, a private sector export processing zone has begun operations, a new Value Added Tax has been introduced, and a number of trade licensing requirements have been streamlined. In the financial sector, interest rates have been fully liberalized, a number of troubled financial institutions are being restructured, the auction system for treasury bills has been opened up, the Banking Act has been strengthened and the Stock Exchange is being improved.
6. Two reform areas in particular, Mr. Chairman, deserve to be highlighted—trade reform and interest rate liberalization. Over the past four years, there has been a gradual but sustained liberalization of Kenya’s trade regime. In 1987/88, quantitative restrictions covered 24 percent of all import items—in 1991/92 they cover less than one percent. Maximum tariffs have been reduced from 170 percent to 70 percent, while the number of tariff rates has been reduced from 24 to 12 over the same period. This has helped to reduce considerably the average tariff in recent years. This is not to say, however, that the process of trade reform is complete. Future reforms should focus more explicitly on removing the import licensing system—preferably as fiscal performance improves—further reducing the dispersion of tariff rates, and intensifying measures to reduce anti-export bias in the economy. The substantial import liberalization that has taken place over the past four years, however, is a good illustration of how a well-designed and gradual reform process can be successfully implemented when there is sustained commitment on the part of the Government.

7. Another example is interest rate liberalization. Since the mid-eighties, through frequent adjustments to nominal rates, the Government ensured that interest rates remained positive in real terms. Partial interest rate liberalization was introduced in 1990 with the removal of the requirement that the ceiling on lending rates be inclusive of lending fees and charges. The process was completed in mid 1991, with the full liberalization of interest rates. This is a major achievement which should considerably enhance the efficiency of financial markets and the allocation of financial resources. At the same time, to capitalize on the efficiency gains from a liberalized financial system, it is even more critical to ensure that the Government pursue prudent fiscal and monetary policies.

8. The fact that Kenya was able to withstand a major external shock with only a moderate slowdown in economic growth would appear to suggest that the economy today is more resilient than during the early
eighties. Yet, despite this credible growth performance, there is a
growing sense of unease over Kenya's current economic situation and its
longer-term prospects. These concerns, Mr. Chairman, center around
four major areas.

9. First, as recent experience shows, failure to control the level
of public spending continues to be a major threat to economic stability
and sustained economic growth. The lack of progress in containing the
public sector wage bill, overspending by a number of key ministries,
and the poor performance of a number of large parastatals have been
major contributors to recent expansionary fiscal policies. In turn,
increased public spending and domestic borrowing by the public sector
have made the task of reducing inflation increasingly difficult.

10. Second, although output has responded to the Government's reform
measures, as shown by the sustained recovery in GDP growth over the
past five years, this improved performance has not been matched by a
recovery in private investment. In fact, real private fixed
investment, which stagnated in 1988, fell by almost 3 percent in 1989
and dropped a further 10 percent in 1990. Moreover, real private
investment in 1990 was 15 percent below the level achieved in 1980.
Unless this trend can be quickly reversed, it is doubtful that the
economy can continue to sustain recent GDP growth rates over the longer
run.

11. Third, while the improved balance of payments performance in 1990
was a welcome outcome, the presently precarious foreign exchange
reserve position suggests that Kenya's economy remains highly
vulnerable to adverse external developments and highly dependent on the
level of aid inflows. Although a number of key exports have recorded
high growth in recent years, especially horticulture and tourism, the
economy's export base remains narrow. The need to ensure external
viability is critical if the Government's trade liberalization reforms
are to be sustained.
12. Fourth, in recent years there has been a growing perception that over-regulation of the economy and the lack of transparency in the enforcement of regulations and controls, are deterring private investment, creating inefficiencies in the allocation of resources, and weakening confidence in the sustainability of recent reform efforts. This concern manifests itself in a number of different ways. Foreign investors cite long delays in repatriating profits and dividends, as well as excessive regulations and their arbitrary enforcement, as major obstacles to investment in Kenya. There are some indications that capital flight has increased in recent years. Even allowing for some possible imperfections in the data, the trend and magnitude of capital flight may be indicative of a lack of confidence in Kenya's economic policies and prospects. A lack of accountability on the part of some large parastatals and other quasi-public bodies frequently leads to mismanagement and large financial losses, inappropriate and non-transparent investment decisions, and inefficiency in service delivery. Despite repeated attempts to chart a more prudent fiscal course, budget discipline has been difficult to enforce in a number of key ministries.

13. These issues are linked. Macroeconomic imbalances, both domestic and external, are being driven largely by an expansionary fiscal stance. Difficulties in containing the growth of public spending result from structural constraints in the public sector itself. As we will discuss in a later session, these constraints impinge directly not only on the efficiency and transparency of the public sector, be it the civil service or parastatals but, as importantly, on the ability of the private sector to respond to improved incentives and market signals. A streamlined and efficient public sector is an essential prerequisite not only for a prudent and sustainable fiscal policy, it is also a key component of an appropriate enabling environment for the private sector. Without increased accountability in public sector bodies, greater transparency and uniformity in the enforcement of a streamlined regulatory framework, and a redrawing of the boundary between the public and private sectors, the important policy reforms being implemented by the Government will, of themselves, be insufficient to
support a dynamic economy capable of growing in line with the full potential of its considerable human and physical resources.

14. In a sense, over the past five years the Government has tackled many of the first-order constraints on the development of key economic sectors. However, as the Government seeks to sustain momentum in the reform process, the challenge becomes more difficult but no less critical. The reform effort now needs to increasingly target not just policies and the structure of incentives and relative prices, but focus more explicitly on institutions and effective implementation across the whole spectrum of government functions. There are a number of facets to this process. Chief among them is the need to reform the public sector itself, including the civil service, and the transparency and accountability of its various components. A more direct effort is also required to promote private sector activity and remove the discretionary elements of government policies where they are found to contribute to an uncertain investment climate. Clearly, these reforms will be more difficult to implement and will require strong commitment on the part of the Government, as they will inevitably threaten entrenched interests and rent-seeking opportunities.

15. Mr. Chairman, within the past three decades Kenya has clearly been one of the economic front-runners in Sub-Saharan Africa. Following stagnation in the early eighties, in recent years a number of major policy reforms have produced a welcome spurt of economic growth. As the Kenyan economy enters the nineties, however, there are worrying signs that this lead is eroding. In an international climate characterized by tightening foreign aid budgets and increasing competition for limited foreign investment resources, Kenya cannot afford to lag behind. Kenya has made impressive strides since independence and, as most of us here today would no doubt agree, continues to have enormous potential. This potential cannot and should not be wasted.

16. Thank you Mr. Chairman.
On behalf of the staff of the International Monetary Fund, I am pleased to attend this meeting of the Consultative Group for Kenya. You will recall that in 1989, Kenya began a three-year structural adjustment effort supported initially by an arrangement under the Structural Adjustment Facility, and followed by successive arrangements under the Enhanced Structural Adjustment Facility (ESAF), with total access under the latter of SDR 241.4 million. During the first two years under the ESAF arrangement, Kenya received four disbursements totaling SDR 180.9 million. In August 1991, the Executive Board of the Fund approved the third annual arrangement under the ESAF and taken note of a policy framework paper for the period 1991/92-93/94. A Fund staff mission is expected to visit Nairobi shortly to review recent economic developments and policy implementation under the program supported by this arrangement.

In the framework of the present ESAF arrangement, the Kenyan authorities adopted a strong policy program involving a number of up-front measures, combining tight macroeconomic policies with continuing structural reforms in such areas as trade and financial liberalization, budget restructuring, parastatal reform, social sector reform, and price decontrol. The 1991/92 budget calls for a sharp reduction in the overall deficit from about 7 percent of GDP to about 2 percent of GDP, with a correspondingly tight
monetary policy. Nonconcessional borrowing is to sharply contract in 1991 and 1992, relative to that of 1990. The program seeks to reduce the external current account deficit (excluding official transfers) to 6.3 percent of GDP in 1991/92 and 5.5 percent in 1992. Provided that the remaining external financing requirement of about SDR 100 million can be met, gross reserves should rise to the equivalent of 1.6 months of imports by June 1992 and to about two months of imports by end-1992 (from about one month of imports in mid-1991). Although real GDP growth is expected to fall to 4 percent in 1991, growth should be able to recover to 5 percent in 1992, primarily reflecting a recovery of agricultural production and a rise in investment activity. Inflation is now higher than anticipated, increasing to 18 percent at end-September, as measured under the old CPI basket, and about 22 percent under the newly developed CPI basket. Thus, it will be critically important to adhere to the monetary targets of the program to begin to decelerate inflation by end-1991 and to reduce it substantially in 1992.

The significant reduction targeted for the 1991/92 budget deficit is clearly an important condition for the achievement of these macroeconomic policy objectives. Revenue measures announced either before or at the time of the budget included a strengthening of the value-added tax, increased taxation of petroleum products, and a reduction in import duty exemptions. Significant real cutbacks were budgeted for recurrent outlays on defense, security, and public administration (including the Office of the President). In the context of a recent sectoral credit with the World Bank, policies were formulated to stanch the significant pressures for expansion in the
education sector's budget. On the development side, virtually no new projects wholly financed by the Government were to commence in 1991/92. A senior Budgetary Review Committee was established within the Treasury to review monthly fiscal developments and to recommend any corrective policies necessary to keep the fiscal program on track.

In proceeding with the ESAF, we felt that these policy commitments and the prior actions taken in July were necessary and important first steps for achieving the required degree of fiscal adjustment. However, as stressed to our Executive Board in August, the principal task ahead is to ensure the realization of the full budgetary adjustment envisaged in the program. This will require continuing vigilance in budget monitoring and execution. A continuing lack of fiscal adjustment would make the achievement of external viability very difficult and compromise what has already been achieved in the structural reform process. Particular attention must be paid to preventing overruns in expenditure and a recurrence of last year's recourse by large parastatals to government financing of their debt service beyond the amount budgeted.

In this regard, the considerably higher than envisaged budgetary deficit of 7 percent of GDP at the end of fiscal year 1990/91 were disturbing, as well as the resulting larger than targeted growth in liquidity. Equally worrisome, at end-September, the preliminary data suggests that while revenue collections are broadly on track, overall deficit financing appears significantly larger than would have been expected. I know that our Kenyan colleagues are actively assessing these developments and have indicated their intention to address any slippages forcefully and quickly so as
to be consistent with the intentions of the program. Obviously, these issues, particularly the necessary strengthening of policies will be examined in greater depth during the forthcoming mission.

Some of the larger state corporations have contributed significantly both to a drain on the budget and to expansionary pressures on the balance of payments. Indeed, from the Fund's perspective, policy and management reforms in the larger parastatals which are not intended for divestiture are at least as important for macroeconomic adjustment as the impact from divestiture of nonstrategic firms. The ESAF arrangement focused particular attention on the need to resolve the financial difficulties of Kenya Airways and the Kenya Posts and Telecommunications Corporation (KPTC). Recent actions to strengthen the management of Kenya Airways, and the announcement of the Government's intention to privatize the airline over the medium term are positive developments. As regards KPTC, based on an assessment of the macroeconomic effects of KPTC's operations, and taking account of the views of the World Bank, we have strongly supported the authorities' decision to freeze KPTC's external borrowing and put a hold on any new investment projects. At the same time, we believe that a strengthening of management systems, development of a plan for rationalization of KPTC's staffing, and improved revenue collection efforts are absolutely necessary if the corporation's financial position is to be improved over the medium term. In this respect, the pace of reform efforts to date has not been encouraging and must be accelerated. With the assistance of the World Bank, we will continue to monitor policies and developments with respect to these two
corporations. Reforms should also be accelerated in other key strategic parastatals, especially in the energy and agricultural sectors.

Concerning more systemic reform efforts in the public sector, significant progress has been made in developing a strategy paper, an initial action plan, and a timetable for the medium-term restructuring cum divestiture of the state corporation sector. In this sphere, the urgent priority is to move quickly, as envisaged in the ESAF, to operationalize a specialized body with sufficient independence and authority to handle the divestiture of nonstrategic state corporations. Similarly, a safety net for protecting workers who would be laid off by the restructuring of the state corporation sector should also be established as soon as possible. In a similar vein, we attach considerable importance to the Government's commitment under the ESAF to develop, by end-December, an action plan for addressing the excessive size and inadequate remuneration of the civil service. Actions to downsize the civil service are necessary if Kenya is to achieve both meaningful rationalization of the budget and increased productivity over the medium term.

To ensure the effective implementation of monetary policy, it will be important to strengthen fiscal adjustment and eliminate bank financing for the Government as programmed, reduce the imbalances of public enterprises, and allow an adequate expansion in credit to the private sector. Overall credit expansion will need to be restrained sufficiently to contain the growth of broad money to a rate consistent with the inflation reduction and reserve accumulation targets. The recent introduction of convertible bearer foreign exchange certificates to encourage the surrender of foreign exchange
increases the urgency of ensuring that supporting fiscal and monetary policies are sufficiently tight, with due consideration being given to the monetary implications of the new certificates. The financial liberalization program continues to progress as targeted with the recent de jure removal of all ceilings on interest rates. With treasury bill yields effectively market determined, open market operations commenced in June; this should reduce the need for direct credit controls and reinforce the role of indirect monetary policy instruments. Also in the financial area, it will be necessary to take steps to address the weaknesses of some financial institutions.

In the external area, the ESAF arrangement calls for continuing actions to strengthen nontraditional exports through a reduction of antiexport biases in the economy. In this connection, the final phase of the import liberalization program was completed in June 1991 with the shifting from quotas to tariffs on almost all remaining restricted items. Average tariffs on already liberalized imports were reduced further, with the intention to continue tariff reductions beyond the ESAF period. Exchange rate policy over the last two years has largely restored Kenya's competitiveness in exports, and we are confident that the authorities will monitor developments in domestic competitiveness so as to maintain this position. To further enhance efficiency, during 1991/92 the General Price Control Order will be abolished, and a significant number of items under the Specific Order will be decontrolled, while taking care to consider the impact on the more vulnerable groups.
One area of continuing concern is that recent structural reforms in the trade, financial, and pricing policy environment have been insufficient to induce significant new inflows of foreign private investment capital. We believe that the authorities share our view on the importance of a conducive environment for such investments, including transparency in the implementation of existing regulations and the assurance of an effective one-stop investment approval process, and a progressive easing of restrictions on outward transfers of profits and dividends.

We believe that the policy package should be strengthened even further as the need arises, with the objective of achieving a viable external position. To facilitate such a determined implementation of the adjustment effort, Kenya's access under the third annual ESAF arrangement was augmented by SDR 20 million. We are hopeful that a similar additional effort will be forthcoming from other members of the bilateral and multilateral community.

On this important occasion, I would like to extend to the Kenyan authorities our best wishes for success in the implementation of their economic policy program.
Ladies and Gentlemen,

You will recall that this morning I touched on the issues relating to the reform of the Public Sector Management. We acknowledge that there are problems to be addressed in this area and I would like to assure you that we are focusing our attention in this direction to ensure that corrective measures are speedily implemented so that management of public affairs is placed on the right footing.

Equally, the Civil Service reform is a long term programme and we are working on measures to resolve the inherent problems.

The Parastatal Sector occupies an important place in the economy and in view of the magnitude of the difficulties faced therein, I would like to contain the deliberation of this session to the policy and strategy now being undertaken by Government.

Arising from the circulation of the first document on Kenya’s Parastatal Reform Programme and the concern expressed by some of you to the fact that nothing is being done to implement the said programme, I would like to take this opportunity to demonstrate the Government’s determination to proceed with the reform programme in a systematic and transparent manner recognising the reality that the reform process is a field that does not permit dogmatic treatment and that every case must be examined on its own merits.

As a reflection of the Government’s ability to adjust to economic realities, you will observe from the document recently circulated, that a number of tangible actions have already been put in place by taking decisions to complete divestiture actions that have been pending for some time and to initiate additional measures.
The responsibility before us is a challenging assignment. It is for this reason that His Excellency the President has appointed a high-powered Committee with the mandate and capacity to guide and oversee implementation of the privatization component of the Government's Parastatal Reform Programme. The Government through the Capital Markets Authority announced on July 2nd 1991 the privatization of some 139 parastatals. The sheer number and diversity of the institutions attest to the enormity of the challenge before us. Furthermore, there are other institutions that will be added to this list as we go along which will further increase the size and diversity of the challenge. In addition, considerable resources will have to be mobilised to realise the objectives of this programme from both within and outside the country. Needless to say, the Government in implementing this programme will also have to consult even more widely with the private sector on these matters in order to ensure the success of the programme. This will indeed be the largest Government programme in which the networking and interfacing of the mutual interests and energies of these both the public and private sectors will be most pervasive.

The Government's announcement through the Capital Markets Authority was itself a milestone in this process in a number of respects. First, it has put to rest the speculation that the Government may never make a move in the matter of divestiture. Second, it underscored the Government's intention to proceed with privatisation with optimum transparency. Third, it has helped to galvanise the thinking of the would be players towards getting ready to participate in the process and benefit therefrom. And finally, it underscored the Government's determination to proceed with the exercise with as much a measure of fairness and equity as is practically possible. In addition, it will also be important to make every effort to proceed with only the necessary minimum of disruption of the activities of the enterprises in question with respect to management, staffing and operations, and to design such
compensatory mechanisms as may be absolutely essential where such disruptions may be unavoidable.

Your concern about the slowness of action on our part is understandable, but on the other hand the need to tread with caution is equally essential and we should not be rushed into action whereby we lose sight of "transparency of process" and "credibility of intent" in the eyes of the Kenyan public to whom we are accountable.

You will have noted from the Capital Markets Authority's announcement that we are proposing to place for sale our shares in a number of companies already listed in the Nairobi Stock Exchange. However, in accordance with prudent commercial practices it is important that we undertake an assessment of the share pricing as well as the absorptive capacity of the market to respond positively to the offers. An excessively large public offering could prevent available resources and savings to be invested in the creation or expansion of other productive enterprises.

I would like on this occasion to reiterate the Government's determination to ensure that all transactions will be conducted in an open and transparent manner, consistent with normal standards of commercial discretion. At the completion of the sale, all aspects of the transaction will be in the public domain. Specifically, this means that:

(a) a prospectus or offering memorandum will be prepared and publicised for each firm to be sold.

(b) that fair and equitable bidding procedures will be established.

(c) a criteria for ranking bids will be established and publicised.
(d) upon completion of each sale, the PRPC will:
- make public the names of the purchasers, the price paid and the conditions of sale.
- that the valuation of the assets and details of all offers received remain in the public domain.

Furthermore, in conformity with the Government's objective to achieve widespread share ownership or to target certain segments of the investing public, specific mechanisms will need to be introduced to guarantee that these objectives are attained and maintained. An allocation scheme will have to be designed to ensure that preference is given to individuals who purchase a small amount of shares in the event the offer is oversubscribed. Otherwise even a public offering may lead to a given investor or group of investors taking control. The Government also intends to encourage employee participation in ownership through the design of an employee share scheme that permits qualified employees, regardless of seniority or years in service to purchase a set allocation of shares at preferential prices.

Since the rule of law is to be respected throughout the process it is also important that we develop a consulting mechanism in respect of the pre-emptive rights of existing shareholders. The charters of the majority SOEs which were set up as joint-venture companies, contain restrictions on the transferability of all or certain classes of shares and provide for pre-emptive rights of existing shareholders. It is equally important that we also design a pricing process, particularly in respect of private sale, to safeguard a fair valuation of assets and avoid claims that the Government has given away the public patrimony to purchasers who enjoy a windfall gain.

Another aspect that has contributed to the delay has been the need to identify the personnel capacity and constraints of the Government Investment Division (GID) as well as the establishment
and staffing of the Technical Unit needed to generate material for the Parastatal Reform Programme Committee. The World Bank Mission has recently completed a preliminary assessment of both institutions and has identified the additional local staffing needs and technical assistance that will be required to strengthen both GID and the Technical Unit to PRPC. I am now happy to report that the core of the Technical Unit has been established with highly qualified Kenyans and that a proposal for technical assistance will shortly be submitted to the World Bank and Donors for funding.

The Action Plan, which has been circulated for the purpose of this meeting, gives a sense of timing, but it is by no means comprehensive, given the fact that we cannot take action on a number of parastatals without having a "safety net" in place. It is evident that the reform process will lead to redundancies and it is important at this early stage that the Government acknowledges its social responsibility for the affected persons through initiating some relief measures. With specific regard to the time frame of the overall exercise, the Government wishes to ensure orderliness and efficiency as we go along and it is planned that the bulk of the exercise should be completed within the remaining period of the current development Plan.

The pace and ease with which implementation of the parastatal reform process proceeds will be influenced by availability of a safety net for redundancies. Kenya does not have a social security system for unemployed. While the developments of an elaborate social security system for all unemployed is a long-term goal, the mitigation of any potential adverse social consequences directly resulting from the Parastatal Reform Programme requires a safety net to be designed and implemented. The need for a safety net is transitional. Several grounded and under-performing parastatals will employ workers as soon as the private sector rehabilitates them. However, some over-employment in other parastatals may need to be addressed through retrenchment. It is the policy of the
Government to develop, as part of its comprehensive reform programme, a safety net to assist those who are transitionally unemployed as a result of parastatal reform.

Safety nets in other countries pursuing parastatal reform and privatization have included a variety of components ranging from minimum statutory severance payments to special credit, training and employment schemes. The experience from these countries has shown that the use of credit and training schemes and the creation of public works have been largely unsuccessful. High default rates on repaying credit, limited utilization of elaborate training programmes, as well as cumbersome administrative arrangements, are common outcomes. Large scale public works provide only temporary employment and have failed to attract the majority of retrenched workers.

On the basis of the lessons learnt from other countries, the Government is of the view that adequate compensation in the form of a "golden handshake" delivered at the point of retrenchment would be the most economical and socially accepted option. A "golden handshake" is relatively easier to administer, visible as a form of government support, more cost effective, and less subject to abuse.

In order to establish the dimension of the "safety net" fund, it will be necessary to collect baseline information in order to determine the level of funding required. As a starting point, the numbers of parastatal employees, classified by unionizable and non-unionizable staff, will have to be established. This distinction is important because statutory severance pay will vary depending on whether employees are covered by collective wage bargaining agreements or by salary guidelines. On completion of the baseline study, the fund will be established in the Treasury and financed from the Exchequer, Donor contribution, as well as a portion of the proceeds of the sale accruing from the privatised enterprises.
Finally in conformity with the Government's declared policy of encouraging foreign investment, we welcome foreign entrepreneurs who are prepared to bring in foreign exchange and technical expertise.
CONSULTATIVE GROUP FOR KENYA


World Bank Statement on Public Sector Management

1.1 Mr. Chairman, Mr. Vice-President, ladies and gentlemen, last year's World Bank economic report argued that Kenya has the potential to develop and grow more quickly. An important ingredient for achieving this faster pace of development is a significant improvement in the quality of public sector management. On the economic front, this entails a rationalization of what the public sector does, more efficient resource use in doing it, and the generation of public savings. Better public sector management also has to do with issues such as broad-based participation in public policy formulation, decision-making and information flows. This statement focuses on those aspects of public sector management which have a direct bearing on Kenya's macroeconomic performance via the fiscal deficit and the productivity of resources. The discussion of these aspects is organized around three themes: (i) the need to improve the mechanisms for expenditure allocation and programming; (ii) the need to reform the parastatal sector; and (iii) the need to reform the civil service.

1.2 First, the need to improve the mechanisms for expenditure allocation and programming. With this in view, the Government introduced the budget rationalization program (BRP) in 1985. Specifically, the program sought to increase the productivity of Government expenditures, in part, by allocating adequate resources for operations and maintenance (O&M).
1.3 While the BRP has contributed modestly to better financial management and the basic process is sound, it has not succeeded in reallocating funds to non-wage O&M. On the contrary, the ratio of O&M expenditures to personnel expenditures continued to decline even after the BRP was introduced. The reason for this is that existing expenditure commitments of the Government do not leave much discretionary funds for reallocation to non-wage O&M, given the overall expenditure limitations imposed by the need to reduce the budget deficit.

1.4 Another recent reform aimed at improving expenditure allocation and programming is the public investment program (PIP). Ordinarily, the PIP would complement the BRP by improving the quality of strategic forward investment planning and, in a budget constrained environment, would concentrate limited resources on high priority projects. For Kenya, the recently produced PIP represents an important but very modest step in that direction. The work done so far constitutes the first attempt to compile very basic project data (including total cost estimates and cumulative expenditure) for all projects in the development budget and will facilitate better estimates of the expenditures required for project completion. At present, however, there is still scope for improving the basis for prioritizing projects. The absence of meaningful recurrent cost estimates for projects is another major deficiency.

1.5 The Government should continue its efforts to refine the expenditure process through the BRP and the PIP. These efforts should include the development of norms within ministries for O&M expenditures required for increased capacity utilization of Government investments. There should also be better recurrent cost estimates in the PIP.
The Government also needs to apply the principles for project selection which it has articulated on many occasions.

1.6 These steps would improve the expenditure process. However, increasing the productivity of Government expenditures will require freeing up significant amounts of resources for spending on non-wage O&M. To do so, the Government needs—as a matter of considerable urgency—to deal with the underlying structural factors which drive expenditure inefficiencies in public enterprises and in the civil service.

1.7 Let me turn, therefore, to the second theme of this statement, the need for parastatal reform. There are at least two compelling and related arguments why parastatal reform should be undertaken. First, the parastatal sector is a net drain on the Government's budget. In FY91, the net outflows were equivalent to at least one percent of GDP. Second, data recently put together show that the parastatal sector is using labor and capital so inefficiently that if these resources were transferred to the private sector, the economy could grow faster by about 2 percentage points a year!

1.8 When we met one year ago, the Government announced its intention to formulate a comprehensive approach to parastatal reform, including privatization, restructuring, liquidation and regulatory reform. Successful implementation of the reform program and its sustainability will depend on the Government's adherence to guiding principles which have been detailed in the Government's documentation for this meeting. A Parastatal Reform Policy Committee (PRPC) has been established to guide the divestiture process and it has already initiated actions with respect to the liquidation or divestiture of some public sector assets. It has not, however, established detailed and transparent criteria for the disposal of these assets. To date, three key appointments have been made to the Executive Technical Unit which will support the work of the PRPC. Discussions are also on-
going between IDA and the Government on funding for the Unit. While the PRPC's functions, procedures and work program are currently evolving, experience elsewhere suggests that the Committee should be regarded as the political body to devise, guide and oversee implementation of the divestiture component of the Government's parastatal reform. However, it should not be involved directly in the valuation of divestible assets or in negotiations with potential buyers. This should be one of the tasks of the Executive Technical Unit, as outlined in the recent Government document, "Kenya's Reforms: Policies, Plans and Outcomes."

1.9 Although privatization is an important component of a parastatal reform program, it should be viewed as part of a broader effort to promote production efficiency, strengthen competitive forces in the economy, and support entrepreneurial development. Experience indicates that divestiture programs that are accompanied by regulatory and institutional reforms have shown better results than programs undertaken in isolation from such reforms.

1.10 The final theme is the need for civil service reform. At present, the Central Government consisted of 28 ministries, 9 independent non-ministerial departments, 148 functional departments and 550 divisions—considerably more than ten years ago. In fact, not all of this bureaucracy is warranted by the expansion and functional specialization of Government over time. Nor is there evidence that the expansion of government has increased access to and the quality of Government services nationally.

1.11 On the contrary, one consequence of the expansion in the government machinery is that effective coordination is difficult, duplication is extensive, and jurisdictional disputes between ministries occur frequently. In addition, the Government has become fragmented and multi-layered. Another consequence is that staff numbers and the wage bill have increased significantly. For
instance, employment in the civil service (excluding teachers) has grown by 6.5 percent per annum since FY67, faster than either GDP or population.

1.12 Admittedly, the pressures for generating public sector employment—stemming from rapid population and labor force growth and success in increasing access to education—have been strong. However, this pace of growth has: (i) created overstaffing in the lower ranks of the service; (ii) limited the scope for offering compensation packages which would attract, retain and motivate staff in higher ranks; (iii) destabilized the fiscal deficit; and (iv) because of inadequate O&M, undermined productivity.

1.13 Because the wage bill is a large share of expenditure, reform which involves downsizing of staff would make an important contribution to deficit reduction. But reform is also urgent because of the need to improve the delivery of necessary government services by increasing expenditure on O&M and rationalizing the organizational structure of the civil service. Hence, civil service reform would be necessary even if there was no need to reduce the fiscal deficit.

1.14 It follows that civil service reform should give the highest priority to: (i) streamlining the functions and organizational structure of government to avoid duplication and redundancies, and achieve better organizational synergy; (ii) downsizing staff in line with the rationalized functions and organizational structure; and (iii) reforming the pay structure and personnel procedures so as to achieve an appropriate mix of staff at all levels, who are motivated and equipped to function effectively and efficiently. Other issues such as improving training, accountability, and capacity utilization are important. Independently, however, none of these would address the immediate and longer-term need to both generate budgetary savings and improve productivity.
1.15 The case for reducing the complexity of government, eliminating duplication and discontinuing functions made redundant by reforms elsewhere in the economy is clear. The case for comprehensive pay and employment reform is equally forceful and urgent. Without it, budgetary resources would not be available to significantly improve non-wage O&M expenditures or to provide compensation packages which would attract and retain staff in higher job groups.

1.16 In summary, while some improvements in the process of expenditure allocation have been achieved through the BRP and the PIP, the underlying structural factors which drive the fiscal deficit and constrain public sector productivity remain intact. Specifically, reform is urgently needed to redefine and restructure the organizational structure of the civil service, downsize its staff, and provide adequate levels of non-wage O&M. Also, the Government needs to instal transparent mechanisms for divestiture while expanding the implementation of the parastatal program to include regulatory and institutional reforms.

Thank you Mr. Chairman

November 25, 1991
Mr. Madavo, Executive Director World Bank;
The Honourable George Saitoti, Vice-President of the Republic of
Kenya;
Distinguished Delegates:

Let me thank you for the opportunity to address you on Human
Resource Issues in Kenya. In my presentation I will make a few
comments on the main aspects of human resource development in
Kenya: especially of population dynamics and population growth,
education and health, the labour force in general and women in
Development.

Mr. Chairman, a few years ago, Kenya had "the highest
population growth rate in the world. This had enormous
implications for Government policy and development. At
independence only a small proportion of our children were
attending primary school let alone secondary schools or
university. Health care facilities were grossly inadequate.
Expanding these basic facilities to all Kenyans has been very
high priority to our Government and the people of Kenya. This
high rate of population growth made this task much more
difficult. Rapid population growth together with our limited
amount of arable land has also made it more difficult to achieve
another vital national objective-food security for all our
people. Rapid population growth, according to the document
prepared for this meeting by our friends at the World Bank, means
that Kenya continues to have the highest dependency ratio in the
world. Each working age individual has to support more people
who are below the working age or who are over retirement age than
in any other country.

Mr. Chairman, the outlook has now changed significantly.
The population growth rate has slowed down; it recorded 3.6 per
cent in 1989 and fertility rates have fallen from 6.6 to 4.5 in
urban area and 8.1 to 7.1 in rural areas between 1979 and 1989.
There has been a decline in the number of children women would
like to have. Between 1984 and 1989 contraceptive use has
increased from 17 per cent to 27 per cent. If these trends
continue- if the fertility rate continues to decline- we expect
to bring the average rate of population growth to below 3.0 per
cent in the 1990s and Kenya will be the first country in Sub-
Saharan Africa to begin a demographic transition. I am sure you
are aware that such a transition is prerequisite for sustainable
growth.
Mr. Chairman, there are several reasons for this remarkable change. These include the huge investments in education and expansion in enrollment at the levels of schooling in Kenya, the effective implementation of our family planning policy and the rapid decline in infant mortality in the 1980s. Infant mortality declined by 43 per cent between 1979 and 1989. The Government of Kenya is fully committed to the mix of policies that have made this remarkable improvement possible. To sustain this new development, we will need to maintain and strengthen the policies that have brought us to this important threshold.

Both the family planning programmes that give our people the proper information about birth control and those programmes which make modern methods of birth control available to our people are very important. Our Government will continue to give these programmes the strong support they require.

On Education

Mr. Chairman, equally important are the changes in other social programmes which have changed peoples' attitudes towards family size. Many of these programmes are in the areas of education and health care.

Government spending on education has increased in Kenya because enrollment has increased at all levels. In primary schools for example, we have come close to achieving our objective of universal primary school education. As a result of increased enrollment, recurrent expenditure on education has increased from 30 per cent of total expenditure in fiscal year 1985/1986 to 36 per cent in 1989/1990. There has been much talk in recent years of user costs as the solution to this problem. The phrase "user costs" is new in Kenya but user costs are not. We have had "cost sharing" in Kenya to build social infrastructure for many years. We have usually called it Harambee. Kenyan families have always paid user costs to educate their children even though school fees in Kenya for primary schools were abolished in 1974. However, fees continue for many other costs associated with primary schooling: fees for books, fees to build classrooms and to equip them with desks and blackboards and fees for maintenance. These fees are high relative to the incomes of the families that must pay them.

Our Government continues to feel that access to primary education is a right of every child. Indeed, there is some evidence that primary school intake has reduced in the last few years because of the high share of the costs born by parents. Our Government does not feel it is morally right therefore to add tuition fees to this burden and will continue to bear the full costs of teachers' salaries in primary schools. Instead, we propose to reduce central Government expenditure on primary
education through increasing the student teacher ratio in primary schools from the present level of 31 students for each teacher to 34 by 1993. The total number of primary school teachers will be capped at 175,000 over this period. This solution to our fiscal constraint is less likely to reduce access to education to children of poor families, this solution is more equitable, and I may say, more democratic.

Mr Chairman, it should be noted that some major communities still require further assistance in providing primary schools: those that live in the arid and semi-arid areas. The participation ratios among children in these areas continue to be too low. The Government, therefore, will continue to establish and maintain boarding schools for these children and explore alternative delivery systems.

Despite the rapid expansion of enrollment in Kenya, only 1 child in 4 finds a place at secondary school. Families with children in secondary school also bear a high proportion of the costs for secondary school attendance including school fees. Here too, the Government has decided not to increase fees but to increase the student teacher ratio to achieve our fiscal objectives. The student teacher ratio will be increased from the current 21 students per teacher to 22 by 1993 and the total number of secondary teachers will not exceed 32,000. These changes in both primary and secondary education are being carried out with the active support of IDA under the Education Sector Adjustment operation.

IDA is also negotiating with the Government to rationalize and strengthen the institutional framework for higher education through the Universities Investment Project. In the last few years we have rapidly expanded our university enrollment. Our intake in 1985 was only about 3,000 students. Less than two in a thousand had the opportunity to attend University in this country although others found ways to attend Universities overseas, some in your countries. We have increased this intake rapidly in recent years. On this, the Government is committed to limit intake to 10,000 students in 1991 and thereafter.

Some people have questioned whether the universities can adequately cope with this rapid expansion. They feel that a smaller university system catering to a more elite group of students would be better. I say they are wrong. It is true that this large increase has strained the ability of our universities but the IDA project will greatly assist us in our efforts to rationalize the use of resources at our universities. Moreover, the Government is introducing a set of measures to minimize the
fiscal impact. These measures include a levy of 6,000 shillings per year from all students. Loans will only be available to students who need them and then to a maximum of 17,500 shillings. In order to assure access to outstanding students from low income families, these changes will be accompanied by a bursary for up to 20 per cent of the students.

On Health, Mr. Chairman, the Government is also considering the implementation of a Health Sector Adjustment Programme in consultation with IDA. The objectives are to better manage our health care system increasing the budgetary allocations to primary health care. User fees were introduced in this sector for inpatient and outpatient services. These systems are being reviewed to ensure access to services by the poor and to increase cost sharing for curative services for those than can afford to pay.

Labour Market Issues

Mr. Chairman, much has already been said about labour market issues particularly as they relate to Civil Service reform. Let me therefore concentrate my remarks on other labour force issues. When you say, as you do in this report that 400,000 new jobs per year need to be created to accommodate population growth, you should be cognizant of the fact that the vast majority of these jobs will be created in the small farm agricultural sector. Eighty per cent of our population still live in the rural areas. The Government of Kenya has always strongly supported the agricultural sector. The Agricultural Sector Adjustment Programme currently underway is designed to "stimulate agricultural growth through smallholders". Besides being an agricultural sector Programme, this is also an employment Programme to improve the productivity of most of the new jobs that will be created.

Small enterprises and informal sector

Sessional Paper No. 1 of 1986 on Economic Management for Renewed Growth indicated that after agriculture, most of the employment for our growing labour force would be generated by small scale enterprises, the informal sector, as it was described in that document. The growth rate in employment in small scale enterprises between 1986 and 1990 averaged 11.7 per cent. Not only is the growth rate in small scale enterprises far higher than in all other sectors but the number employed is far higher than all other sectors except agriculture. The promotion of this sector is the second major aspect of employment creation in Kenya.
The Government will soon publish Sessional Paper No. 2 of 1991 on Small Enterprises and Jua Kali Development in Kenya. In this paper Government's role is defined as that of a facilitator, concentrating on providing the infrastructure and enabling environment in which entrepreneurs can emerge, develop and grow.

Several policies and programmes are already in place which will encourage small scale enterprises. The relaxation of quantitative import restrictions will give these entrepreneurs better access to imported materials and tools. It is hoped that the deregulation of interest rates in July of this year will improve their access to credit. The establishment of the District Development Fund in 1987, and the Rural Enterprise Fund in 1989, the construction of Nyayo sheds, and the exemptions from import duty on capital machinery are all programmes created to support small scale enterprises.

The Sessional Paper contains a number of new initiatives to promote the development of small scale enterprises. The Government will encourage local groups of artisans to form associations. This will facilitate the transfer of ideas, new technology and market information to these entrepreneurs. These associations will also be useful in providing collective, cost effective, sources of raw materials and market outlets. The formation of associations can also play an important role in educating and lobbying for the interests and concerns of their members.

Mr. Chairman, the promotion of small enterprises and informal sector business as you can see from above is receiving increased support. Informal sector enterprises are already being promoted through the provision of sheds in central areas of selected towns in most of the districts. A major programme has been initiated to provide limited credit to individuals and groups under a K£ 20 million Rural Enterprise Fund. The programme excludes common farming activities and real estate business. However, the technical and vocational training institutions are revising their training to incorporate training in management and entrepreneurship. The focused training to this important sector, we feel, will create the necessary managerial skill which, coupled with the entrepreneurial spirit of our people, will capture employment generating economic activities.

Industrial land will also be made available to small scale enterprises within designated industrial sites. Small scale entrepreneurs will be able to construct and install their own facilities on these sites.
The Attorney General's Chambers will undertake a comprehensive review to ease the regulatory framework for business. This will include especially licensing arrangements and building codes which hinder small scale enterprises and restructuring clauses of the employment act which restrict access of women in certain industries.

The Government will engage in a number of promotional programmes on behalf of small scale enterprises. Market information will be disseminated and linkages to industry through subcontracting will be encouraged through tax incentives and other means. These include programmes of market surveys, seminars and training for the small scale entrepreneurs and to sensitize lending institutions and other formal sector firms to how they may better work with small scale enterprises. The media will also be used to highlight pertinent issues.

Mr. Chairman, the unemployment rate in the urban areas of Kenya is about 16 per cent. The unemployment rate in rural areas is very low but wages are also very low. A recent Presidential Committee on Employment concluded that much of this unemployment in urban areas was similar to what developed countries describe as "structural unemployment". High unemployment is associated with the large number of young people entering the labour force. Unemployment is very high among young people in many developed countries as well, but we have a much higher proportion of these in our labour force because of rapid population growth and the small number of our young people who attend secondary school.

Kenya also has another structural problem that developed countries do not have which makes reducing the unemployment rate intractable. There are a very large numbers of people in rural areas who would like to move to the urban areas if they could find an appropriate job.

The unemployment rate in Kenya can only be reduced slowly through the process of development. Some measures can be taken to make education more employment orientated and improve information to job seekers but these take time and we will still have the huge number of new entrants and rural migrants seeking jobs. The Committee has made several recommendations in this area. It has also recommended the creation of a rural infrastructure programme that would benefit agriculture and small scale enterprises in the rural areas and also ease the pressure from potential migrants. I would like you to consider this suggestion when you make your review.
Mr. Chairman, it should be observed that, the Committee recognizes as did Sessional Paper No. 1 of 1986 that the most effective and reliable method of reducing unemployment is rapid and sustained economic growth. In this, the private sector must play a leading role.

Sessional Paper No. 1 of 1986 signalled a sharp change in direction to stimulate private sector growth. It envisaged the introduction of reform in nearly every sector that would be implemented by the year 2000. In many of these areas the Government has proceeded more rapidly and gone further in liberalizing the economy than envisaged in the Sessional Paper: price decontrol, financial market development including the decontrol of interest rates, and import liberalization to name but a few.

Mr. Chairman, it will take some time before these measures translate into the more rapid rates of growth of formal private sector employment. But the Government is confident that we are on the right path and these policies will stimulate more rapid growth. The degree of acceptance that these policy changes have received is in large part due to the measured and judicious way they have been implemented.

WOMEN AND DEVELOPMENT

Mr. Chairman, I have talked of human resources in general. I wish at this juncture to bring one particular aspect which we are giving more and more attention. It should be noted that despite the progress made in the country to increase women's opportunities in economic development, a lot remains to be done to further reduce the disadvantages of women in the development of the country. Some of the activities to remove the disadvantages include the development of indicators to enable planners address gender issues in the preparation of programmes and projects and increased technical training opportunities for girls. The Government is to promote and monitor the implementation of the convention on the Elimination of All Forms of Discrimination Against Women. Public agencies which provide loans to farmers are to be alerted to the need for special measures aimed at increasing greater access to credit by rural women. A major share of the new Rural Enterprise Fund is earmarked for women groups. It is hoped that you will continue to support various women programmes both in the NGOs or in Government.
Efforts to involve women fully in the development process will continue to focus on ensuring women participation in mainstream programmes instead of creating special programmes for women. Over the medium term, Government priorities are to increase the productivity of women in farming and business and continued improvement in access to health and family planning services.

Mr. Chairman, in a period of rapid adjustment, there are bound to be some adverse effects. The set of structural adjustments we are now committed to, such as civil service reform and rationalization of the parastatal sector, will have short term adverse effects on unemployment. This is therefore a critical period in terms of achieving the goals of growth and development. Your understanding of this difficult process and support are very welcome.

Thank you, Mr. Chairman, for allowing me to make these few remarks concerning human resource development in Kenya.
CONSULTATIVE GROUP MEETING FOR KENYA


World Bank Statement on Human Resources

1. Mr. Chairman, Mr. Vice-President, delegates, ladies and gentlemen, it is not unusual for there to be a Bank statement on the same topic -- human resources -- at two consecutive Consultative Group meetings. The Bank does so today for three reasons. First, because the overall economic and development policy environment has important linkages to the human resource sector, in particular for Kenya's poorest people and for its record of social achievement. Second, although there are many areas of sectoral importance that require attention, the Government has taken several major policy decisions in the last year. And third, because the Bank wishes to take the occasion of this meeting to announce a new departmental initiative -- the establishment of a Poverty and Social Policy Unit in Nairobi to serve all the countries of the Eastern Africa Department including Kenya.

2. Bank statements yesterday drew attention to growing unease over Kenya's current economic situation and its longer-term prospects. Unless the Government tackles some of the problems highlighted yesterday, not only is Kenya's record of economic growth threatened, so also is its impressive set of human resource achievements. There is no need here to go into Kenya's social statistics; we are all aware of the country's record on education, infant mortality, and, as pointed out last year, finally on fertility reduction. Maintaining Kenya's lead in terms of social indicators presents a challenge, however, every bit as great as doing so in terms of economic growth. This is both because of the link to the macroeconomic situation and because there are new human resource problems that require attention and, inevitably, resources.

3. The link to the wider economic questions is simply put. Despite apparently entering a demographic transition, characterized by fertility reduction, Kenya's
population is continuing to grow very rapidly. This has implications for employment, the provision of social services, and for poverty alleviation.

4. Failure to accelerate economic growth will result in growing unemployment; during the 1990s about 400,000 school leavers will join the labor force each year. At present only 100,000 of them are finding jobs in the formal sector. So the Bank welcomes the finalization of the report of the Presidential Committee on Development and Employment, although we have not yet had an opportunity to study its conclusions; the very production of the report recognizes the employment problem.

5. Social services require resources. Accelerated economic growth is essential to enable Kenya -- through both its public and its private and NGO sectors -- to allocate enough resources to provide social services to its people and to continue to improve its social indicators, and hence the quality of life of its people. This is particularly difficult not only because of the concerns over the country's growth prospects but also because there are both unmet areas of need and emerging new problems in the social sectors. Aside from unemployment, these include, but are not limited to, the declining quality of health services at public facilities; the status of women; the resurgence of old diseases such as malaria and the emergence of new ones such as AIDS; the quality of education; and growing regional disparities in terms of education, health and nutrition.

6. In part these disparities can be tackled through targeted interventions. For instance, the Government has recognized that its policy that parents should pay for primary school textbooks may have gone too far for some poor families. In the arid and semi-arid regions, for instance, a policy of public provision of instructional materials may warrant reintroduction. In part, however, disparities in terms of social indicators reflect disparities in income levels. This is again linked to the overall economic situation. Without sustained economic growth, it will not be possible to deal with poverty. Without sustained economic growth, relative poverty cannot be tackled, as
redistribution is politically and socially easier in an atmosphere of rising overall prosperity.

7. The Government does not face an easy task. Not only must it maintain and even accelerate economic growth to permit social progress, but at the same time, some of the very steps necessary to maintain growth have short term implications for social progress. A first issue is the provision of appropriate resources in what is going to have to be a very tight fiscal situation, requiring hard choices on efficiency, cost sharing and equity. A second, particularly complex, issue that the Government will have to face as it takes steps to reduce the drag of the public sector on the economy, will be the addition of retrenched public employees to the ranks of the unemployed, unless the reform of the public sector is handled very carefully and appropriate transitional safety nets are put in place.

8. The Government has started to take these hard choices and deserves appropriate recognition. It has taken steps to contain the growth of the education sector recurrent budget, most notably restricting the growth in the number of teachers on the public payroll, limiting the intake of new students to the universities, modifying the content of the 8-4-4 education system to enhance the quality of learning, and establishing an institutional framework to oversee the development and financing of the universities. It has taken politically difficult steps to increase cost sharing, including the introduction of a direct charge on all university students, revisions to the university student loan scheme, modifications to the National Hospital Insurance Fund, and a Cabinet decision to reintroduce outpatient consultation charges at public sector health facilities to complement those already in place for inpatients. Finally, the Government has sustained its efforts to encourage fertility reduction.

9. These steps have been difficult. They are only a beginning, however, and will require extension in the coming years. Employment is now on the Government's
agenda; women should be. Social policy, human resources and medium term objectives must not be forgotten in the natural tendency to focus on the immediate economic issues. The first action necessary to deal with regional and income disparities is to gather better information on them, and on the impact of the cost sharing reforms — and indeed of other aspects of adjustment — on Kenya's population, particularly the poorest households. The Household Welfare Monitoring System that the Government is now putting in place is thus particularly urgent and deserves donor attention — whatever the macroeconomic situation — to fill its unmet financing gap. Explicit provision is needed for those unable to pay for social services, such as through free provision of school textbooks as already discussed, the bursary scheme now being developed for university students unable to afford the new direct charge, and an effective and fair waiver system for those unable to meet the outpatient charges at health facilities.

10. In the context of public sector management reform, the social sector ministries must not be forgotten. They are by far the largest ministerial employers, once all teachers and health workers are included. Yet, they are among the weakest ministries in terms of internal management and suffer from a combined lack of reliable data and analytical capacity. Particularly urgent is the need to improve the health information system and to build analytical and investment programming capacity in both the Ministries of Education and Health. Weak service delivery programs also need attention; an important example is nutrition where responsibility straddles several ministries, including Planning, Health and Agriculture, and none takes appropriate overall responsibility. As noted earlier, programs are also urgent to deal with renewed and new problems like malaria and AIDS.

11. These issues not unique to Kenya. Other countries in Eastern Africa face many of them, to differing degrees and without the advantages Kenya has of past progress and a record of economic growth. Their common elements include cost sharing, targeting of public resources under fiscal restraint, regional and income disparities, the
employment challenge, safety nets to deal with the social consequences of adjustment, the status of women, the lack of regular and reliable social data, new challenges such as AIDS, and, from the Bank’s perspective, an increasingly important and complex policy dialogue in the social sectors.

12. These circumstances have prompted the Bank’s Eastern Africa Department to take a look at how it does business with regard to poverty and social policy. A lesson from the recent effective dialogues with the Government over education sector reform, over population policy and over cost sharing in health has in major part has been the importance of having key staff in our Nairobi office; successful implementation of policies now adopted will clearly continue to require sustained attention at field level, which we hope to support on a regional basis. Household welfare monitoring schemes are being put in place with Bank support not only in Kenya but also in Uganda. Adjustment programs are rightly being complemented by safety net operations. A Social Fund has been established in Uganda and a pilot is to be introduced in Ethiopia, initially to assist with the reintegration of displaced soldiers, civilians, widows, orphans and refugees and potentially also to assist once a program of structural adjustment is adopted. Measures are going to be necessary in Kenya, Uganda and Ethiopia to handle the employment implications of parastatal and civil service reform. Malnutrition, regional disparities and relative poverty require sustained attention in all the Bank’s client countries in the region. Indeed, experience can usefully be transferred across countries.

13. This is what has led the Bank to decide to establish a Poverty and Social Policy Unit in its Nairobi office, to meet the needs of Kenya and its neighbors in the Eastern Africa Department. The Unit will initially be small and will play the major role in the Bank’s work on poverty in the department, both helping to improve understanding of the dimensions and causes of poverty in Kenya and other countries and working with agencies well-placed to help address the needs of the poor. In this latter context the
Unit will seek not only to improve linkages with social sector ministries but also to establish them with Non-Government Organizations.

14. The Bank hopes that this new Unit will support the efforts of the broader donor community in Eastern Africa. By virtue of having more staff permanently in the field, the Bank hopes that the Unit will play the leading role in enhancing donor coordination at field level in all the areas just discussed. Consistent with this, the Bank invites donors to continue and extend the very successful, but so far limited, experience of funding key individuals to work on human resources in our field offices. We shall shortly be approaching donors in a formal way to seek such extended support but meanwhile welcome informal discussion.

Thank you.
Mr. Chairman, Mr. Vice-President, delegates, ladies and gentlemen, the levels of support provided by IDA to its developing country members is based on an assessment of government efforts to reduce poverty, through sustained economic growth and broad access to basic social services. Progress towards this overall goal is predicated on sound macroeconomic management and usually requires strongly implemented reforms to address structural obstacles to growth and development in key sectors. Kenya's strong performance enabled us to commit considerable resources, in large part through quick disbursement adjustment operations. Recent economic developments are worrying, however.

Without a stable macroeconomic environment, sectoral reforms will neither pay off nor be sustainable. Sound macroeconomic management is therefore a precondition for our ability to sustaining our current level of activity, and in particular to provide quick disbursing support to structural reforms. As you heard yesterday, we have concerns in this area.

Provided macroeconomic management is adequate, a substantial although declining share of our lending can be quick disbursing. However, the amount of such financing depends on progress in implementation of structural reforms in key sectors - delay in these reforms implies a reduction in our lending program.

Let me briefly summarize our approach to structural reforms in key areas, through adjustment and investment lending, and through our economic and sectoral analysis.
First, concerning parastatals, the Government has been slow to move on comprehensive reform. This has been due in part to the difficulty in building commitment, and in part to inadequate technical preparation. The Government's parastatal reform strategy and action plan documents point to a firming of commitment; and a technical assistance credit now under preparation will help to strengthen the ground for the implementation of reform, which we could support with an adjustment operation, as soon as strong reform is underway.

We also regard structural reforms to improve the efficiency of government expenditure as urgent. Some progress has been made in improving budget processes. More needs to be done to improve public investment and operating expenditures, reestablish the discipline and transparency of the project cycle and transform the forward budget into more of a planning instrument. A vigorous start to civil service reform is also needed. We would be happy to provide appropriate support to these efforts.

In parallel with strengthened public sector management, continued high priority must be given to eliminating remaining constraints on the private sector. A major element of our work this year is a Private Sector Assessment Study which would be the analytic foundation for future support from the Bank.

In agriculture, ongoing adjustment lending is supporting reforms in agricultural pricing and marketing. Since the last Consultative Group meeting, the Bank has also approved credits in support of Forestry Development and National Extension programs. The former will enhance the protection and conservation of Kenya's indigenous forests and is a major component of the Bank's environmental program in Kenya. Other environmental projects in the future lending program include the Wildlife Management project, which was negotiated last week, and a project for the protection of the arid and semi-arid regions. We are also helping set up a joint Government-Bank workshop to set in motion preparation of a National Environment Action Plan which would provide an overall strategy for action to protect Kenya's environment.
Mr. Chairman, a solid infrastructural base is crucial to sustained private investment. Our overall goals are to help rationalize investments, strengthen institutions, improve pricing and enhance accountability. We plan lending to support road maintenance, the rehabilitation of the urban transport system, port and railway improvements, and the rehabilitation and expansion of water supply systems. A municipal finance project will be designed to strengthen local governments' ability to finance their infrastructure requirements. We could also provide additional support to improved efficiency in telecommunications.

In the energy sector, progress has been much slower than expected. The sector is obviously of critical importance to Kenya's future development and absorbs substantial investment resources, but efficiency has been severely hampered by investments of questionable priority, with dubious financing arrangements, by inappropriate pricing, by institutional weaknesses, and by barriers to private sector involvement. Future IDA assistance to the sector will require the adoption of an improved institutional and policy framework and sustained commitment to reform. Because numerous other donors have also supported the energy sector in Kenya, we strongly favor the formation of a donor coordinating committee to ensure that aid resources are allocated to the highest priority investments.

Our human resources operations have moved into a new phase. Fertility reduction continues to be at the core, but has now been complemented with an intensive policy dialogue and operational program in education and health, particularly stressing the linkages between the macroeconomy and the social sectors. This will continue, with a health sector operation anticipated to follow the recent education one.
We plan to place increased emphasis on the government's efforts to reduce poverty. This is the main rationale for our support to human resource development and for the Welfare Monitoring System we discussed earlier this morning. The provision of safety nets for those affected by the government's planned adjustment measures would be integral components of any IDA support to parastatal and civil service reform. In addition, our next economic report will provide an overview of poverty and employment issues in Kenya as the basis for designing further Bank support in this area.

Thank you Mr. Chairman
For Immediate Publication

PRESS RELEASE

MEETING OF THE CONSULTATIVE GROUP
FOR KENYA

PARIS, November 26, 1991 — The Consultative Group of donors and multilateral institutions interested in supporting the economic development of Kenya met in Paris on November 25-26 under the chairmanship of Mr. Callisto Madavo, Director of the Eastern Africa Department of the World Bank. The Kenyan delegation, led by the Vice President and Minister for Finance, Professor George Saitoti, included the Minister for Planning and National Development, Dr. Zachary Onyonka, and the Governor of the Central Bank of Kenya, Mr. Eric Kotut.

The meeting reviewed Kenya's current situation and examined the prospects for its future development. Participants acknowledged Kenya's historical economic lead in the region and the Kenyan authorities' success both in implementing important structural reforms, notably in the areas of trade and financial sector liberalisation, and in sustaining economic growth throughout the second half of the 1980s. However, they expressed concern that this economic lead is vulnerable, due to the recent deterioration in the macroeconomic situation, as reflected in the rising public-sector
deficit, inflation, and declining real levels of private investment. They also expressed concern about high unemployment and capital flight. Delegates agreed that these worsening economic trends underlined the importance of greater government commitment to more vigorous and far-reaching structural reform efforts if accelerated economic growth is to be achieved. Delegates also emphasized the need for greater transparency and accountability in decision-making and expressed their concerns over misuse of public funds in certain instances. They welcomed government assurances that determined action will be taken expeditiously to resolve these issues.

In a session devoted to public-sector management issues, delegates recognized the recent improvements in budgetary processes, but emphasized that urgent action is needed to deal with the underlying structural problems which constrain the productivity of the public sector and worsen fiscal imbalances. In this connection, the meeting agreed that vigorous action is urgently needed to reduce the share of the wage bill in government expenditure, thus releasing resources for public saving and operation and maintenance, and to improve civil service discipline and motivation. Delegates therefore welcomed the government's intention to proceed speedily with a programme of civil-service reform, with donor support. They also welcomed the government's intention to ensure transparency in the divestiture of public enterprises, and to accelerate efforts to broaden the scope of parastatal reform to embrace forceful actions to improve efficiency and accountability.

In a session devoted to human resource issues, delegates noted Kenya's achievements in this area, and welcomed the policy reforms recently adopted by the
government. These include the introduction of student fees at the universities, and the decision to reintroduce outpatient treatment charges at Kenya's public sector health facilities, in both cases including mechanisms to protect the poor. However, delegates shared the Government's concern over growing regional disparities in health, nutrition and education. Overcoming these disparities and maintaining the overall progress achieved in human resource development in Kenya also depends heavily on reinforced policies for sustained economic growth.

Participants noted that Kenya's economy has been highly dependent on external assistance, and that continued significant aid inflows are needed to support Kenya's economic development. They emphasized that there was growing competition for increasingly scarce donor resources, and that aid programmes were being reexamined with a view to ensuring the most effective use of these resources in helping improve human welfare.

Delegates underlined that good governance is a prerequisite for equitable economic development and would therefore be a major factor influencing aid allocations. Donors accordingly stressed the need for early implementation of political reform to reinforce the benefits of economic structural change. They also welcomed His Excellency the President's recent statement that Kenya would move in the near future towards greater pluralism, underlined the importance of the rule of law and respect for human rights, notably the basic freedoms of expression and assembly, and called for firm action to deal with issues of corruption.
Delegates made clear their willingness to support Kenya's economic development, but stressed that the levels of aid for Kenya also depend on clear progress in implementing economic and social reforms. All participants agreed on the need for decisive action to correct macroeconomic imbalances; to rationalise public enterprises and improve their financial discipline, accountability and transparency; to launch a substantial civil-service reform effort; to improve the efficiency of public expenditure as a vehicle for providing basic economic and social infrastructure to the people of Kenya; and to provide an environment which is consistently supportive of private investment and initiative.

Participants agreed that there should be further consultations among the members of the Consultative Group in about six month’s time to review progress in these areas, as a basis for indications of external assistance to Kenya.

Members of the Consultative Group attending the meeting were Canada, Denmark, Finland, France, Germany, Italy, Japan, Netherlands, Sweden, Switzerland, the United Kingdom, the United States, the African Development Bank, the Commission of the European Communities, the European Investment Bank, the International Monetary Fund, and the United Nations Development Programme. Belgium, Saudi Arabia and the Organisation for Economic Cooperation and Development attended as Observers.

November 26, 1991