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Review

Industrial policy, institutions and foreign direct investment: The Kenyan context

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The importance of industrial policy, institutions and FDI in industrialisation is one of the most widely debated issues in the economic discourse. As a contribution to the debate, this paper examines the importance of industrial policy and institutions in Kenya's industrial development. The paper also examines FDI focusing on positive spillovers, capability development and performance. FDI had a positive role on industrial development through spillover benefits. Nevertheless, the paper argues that FDI's role in industrialisation can be enhanced by stimulating a strong science, technology and innovation culture. Although institutions established portrayed a positive impact, they were severely constrained in terms of operational capacity making them inefficient. It is therefore recommended that the government continues to provide support to such institutions in earnest to particularly enhance their capacity such as co-ordination, finance and human capital. Lastly, consistent and carefully formulated industrial policies are advocated for as they allow firms long term planning horizons.

Key words: FDI, institutions, spillovers, industrial policy, industrialisation and Kenya.

INTRODUCTION

The importance of industrial policy, institutions and foreign direct investment (FDI) in industrialisation, for economic growth and development, is one of the most widely debated issues in the economic discourse. Starting with the latter, many contend that FDI can have positive effects which range from direct capital financing to positive externalities (spillovers) via technology and innovation transfer to host economies (Caves, 1982; Dunning, 1993). Many governments especially those of the developing economies have now been forced to offer a wide range of incentives such as investment allowances and tax holidays to attract FDI. With regard to industrial policy, the newly industrialized countries (NICs) have provided international evidence purporting that a country cannot industrialise without a prudent industrial policy in place (Lall, 1987; 1996). A sound industrial policy enables a country to identify and address industrial constraints impeding economic growth and development. Accordingly, countries are now involved than ever before, in developing road maps or master plans envisioned at achieving industrialisation within specified time frames. Similarly, institutions (organisations) are fundamental to achieving industrialisation through their intermediation role such as provision of finance capital, technical support or strengthening network cohesion (Aoki, 2001; Doner, 2001). This is articulated succinctly by North (1992) when he stated that "institutions and the way they evolve shape economic performance."

In Sub Saharan Africa, Kenya serves as a good laboratory for a case study analysis to examine the above issues. As will be shown, the Kenyan manufacturing started with establishment of a few manufacturing industries during the colonial era, all foreign owned (Leys, 1975; Swainson, 1978). All of them were located mainly in agro-based industries performing simple and basic manufacturing activities characterised by limited value added. As a result of foreign capital investment in manufacturing received from Britain during the colonial period, it is claimed that Kenyan manufacturing enjoyed an early colonial manufacturing experience from British firms (Swainson, 1978, 1980; Kaplinsky, 1978). In addition, the country continued to enjoy most of the infrastructure and a vast of revenue earning primary sectors (such as tea, sisal and coffee estates) all developed in the same period. In cognizance of these developments and in light of subsequent changes with time, a historical backdrop coupled with institutional analysis become relevant if we are to understand the origin of FDI, its evolution and perceived impact on industrial development.

Similarly, institutions created and industrial policies adopted after independence are believed to have had tremendous influence on industrial development. Existing institutions also had an influence on FDI including FDI flow and their subsequent impact in manufacturing. For example, at independence; institutions erected and policies enacted helped attract more foreign investment, mainly European, into the country. Since then, a relatively large FDI stock has been accumulated in Kenya's manufacturing. Due to their participation in manufacturing after independence; that is capital investment, contribution in exports, value added, employment and revenue generation to the economy etc the country is over time believed to have benefited tremendous manufacturing experience in the form of technological spillovers from foreign investments. This is more so with the facilitation and coordination role undertaken by institutions established.

The direct consequence of this is that FDI plays a positive role in industrial capability development. However, this is still a contentious issue since to date no concrete studies on FDI have been conducted in the country to confirm technological spillovers, their form, and mode of occurrence or perceived impact on domestic firms. This not withstanding, the role of supporting institutions in FDI, spillover and industrial capability development has not been critically addressed either. Occurrence of technological spillovers in the industry is usually a complex phenomena due to the tacit and non-codifiable nature, which takes place through interactions between domestic firms, FDI and host country institutions. Institutions in this context are taken as organisations – economic agents whose systemic embeddedness in the National System of Innovation stimulates spillovers occurrence, firms' technological capability, innovation and performance.

Following from the above, this paper will seek to answer the following issues: Which industrial policies were pursued and how effective were they in supporting industrial development through initiatives such as promotion of FDI and institution formation? What has been the role of FDI and institutions in Kenya's industrialisation process? In broad terms, has there been any positive spillover occurrence? If yes what have been their consequences on industrial capability development and productivity performance? Lastly, which institutions were established and how effective were their roles in supporting industrialisation?

This paper is divided into six sections. Section 2 presents an overview of industrial policy, FDI and institutional setting. Section 3 examines the role of FDI in industrial capability development and seeks to understand the role of institutions established during the colonial period as well as during the early decades of import substitution. Section 4 provides a review of the structural adjustments period. Section 5 examines the role of FDI in industrial capability development and seeks to understand the role of institutions established during the export promotion period. In section 6, the recent performance and effort towards industrialisation is examined while the last section presents summary, conclusion and policy recommendation.

INDUSTRIAL POLICY, FDI AND INSTITUTIONAL SETTING

Kenya's industrial policy can be classified into two main categories; the import substitution (I-S) and the export orientation (E-O). I-S industrialisation, which was the main mode of industrialisation during the colonial days, continued to be encouraged until mid 1980s when it was gradually replaced with export-oriented industrialisation dawning the era of liberalisation measures also advocated as part of World Bank structural adjustment programme (SAPs). I - S was initiated in Kenya before her independence; hence an analysis of industrial policies in Kenya without a backdrop to I - S policies pursued during the colonial period would be incomplete. I-S pursued influenced the inflow and kind of FDI as well as facilitating institutions including those established to support industrialisation.

This section therefore starts by examining the industrial policies before Kenya's independence, during the colonial days, and their influence on FDI and broad industrial capability development. Since industrial policies followed after independence kept changing at different time periods, this would have direct and/or indirect consequences on FDI and hence their effect on manufacturing industry. Consequently, for a comprehensive examination of industrial policies pursued and their influence on FDI, our analysis will be done in three distinct phases. The early decades of I-S will be examined first followed by the era of structural adjustments and liberalisation and export promotion, and finally the recent performance and effort towards industrialisation in Kenya.

Pre-independence: The colonial period

The history of Kenyan manufacturing industry dates back to the colonial period from which the existing manufacturing characteristics including those depicted by FDI are likely to have taken their bearing. To appreciate this observation, an examination of industrial policies during the entire colonial period, would have to be examined. Various modes of capital investment would also have to be examined with particular emphasis to thekind of manufacturing industries established and their ownership structure. The analysis is presented in two phases – the period before 1945 and the period 1945 - 1963. The choice of the two time periods is not arbitrary. The period before 1945 can be regarded as the pre-war period (That is, First and Second World War) while the period after 1945 can be considered as the post war period. The period 1945 – 1963 differs significantly from the period before 1945 in that during the period 1945 - 1963 there was a radical transformation towards industrial development in the British colonies. In the later period, Britain encouraged its MNCs to invest in Kenya – as it did in its other colonies. Thus while the former period was characterised by little industrial development activity, the latter period was marked by an improved effort to promote manufacturing industry in Kenya with significant participation by British MNCs.

The Period Before 1945: Kenya was founded as a British Colony in 1890s and converted into a Crown colony in 1920. Existing literature on colonial history reiterates that several factors induced the formation of colonies in the nineteenth and twentieth centuries. Firstly, the rush for colonial expansion during this period was to develop and control sources of strategic primary goods, raw materials and foodstuffs. Secondly, it was assumed that by controlling the activities undertaken in the colonies, the colonial territories would provide an export market 'protected markets' for the colonial manufactured products. As a British colony, Kenya's role was reduced to that of raw material production to supply the British manufacturing industries. It was also clear that Kenya would serve as a growing market for British manufactured products - once these products are manufactured in Britain they would then be exported back to the Kenyan market including those of other British colonies in the region. This had a negative implication in that it would not stimulate strong domestic manufacturing capability development.

In order to achieve the colonial objectives, several things were put in place; first, the British Government provided funds for infrastructure development, which included roads and railway to facilitate transportation of primary goods - food crops and raw materials from the mainland. The funds availed facilitated the building of the Kenya Uganda railway in the period (1895-1901). Port facilities were also developed and export–import warehouses established to facilitate export of primary goods and import of consumer goods. Second, the British Government encouraged European settlers to settle in Kenya and participate in commercial agriculture directed towards exporting. The commercial agricultural activities were undertaken in the so-called 'white highlands' in Kenya with labour supplied by indigenous Africans (Pearson, 1969).

Since commercial agriculture turned out to be the main mode through which raw materials were generated and exported to Britain, the European settlement was further encouraged in 1920 when Kenya was declared a Crown Colony in 1920 making the number of European settlers in early 1920s reach about 20,000. Formation of a Crown colony in 1920 was the official sanctioning of settler dominance in Kenya (Swainson, 1980). Examples of major MNCs from UK, which made their investment during this period, included James Finlay (1924) in tea production; Brooke Bond (1924) in tea and coffee production; Mitchell Cotts (1936) in sisal production (Kaplinsky, 1978; Swainson, 1978; 1980) (Table 1). By participating in raw material generation, the European settlers would enable the British Government to recover the costs incurred in the construction of the Kenya-Uganda railway line. Finally, in order to encourage and support production for exports by European settlers, import protection and export incentives were offered.

The effort by the settlers to have full control and dominate in all social and economic activities reflected a clear emerging pattern of de-indigenisation. Jorgensen (1975) offered a luminous illustration of how the de-indigenisation process of the Kenyan economy took place during the colonial days. He examined the role of MNCs in the de-indigenisation process using a three-level analytical framework that constituted structure of the economy, control over individual production and the distribution of firms, and the racial division of labour within firms. Jorgensen showed how Kenya entered into the vertical international division of labour during the colonial period by participating in international trade suited to the colonial masters. By so doing the "structure of the domestic economy was transformed to produce agricultural goods needed by the external economy and to import consumer goods and machinery from the external economy." De-indigenisation at the second level took place in the form of ownership of farms, firms and other commercial entities. Africans were not supposed to participate in either the interior or external trade with the rest of the world. These were left exclusively in the hands of non-indigenous Europeans and Asians. Africans were also denied control over units of production and over production itself. At the third level, division of labour within firms, Africans were forced to become labourers. Under pressure from European settlers, Jorgensen (1975) noted that the colonial regime relegated the African population to a subservient role as labourers meant to produce largely for export to satisfy needs of non-Africans. They were not allowed to participate in production of trade goods except peasant production of foodstuffs for consumption within their native reserves (Jorgensen, 1975). Asians participated in production but were restricted to light small scale manufacturing, characterised by low capital and thus value added. The phrase below explains it all:

> "Europeans controlled the colonial administration apparatus, financial institutions, the larger import-export firms, shipping, mining (gold and soda ash), plantations, large farms, large scale food processing firms (breweries, bacon factories, co-operative creameries and canneries), and the larger commercial firms in urban areas. Asians controlled smallerimport-export firms, most of the retail shops in cities and towns, financial institutions serving the Asian community, and small-scale manufacturing (alumi-num pots, soap, vegetable oils, and sawmills). In addition, Asians filled most of the positions of

Table 1. Principal foreign-based firms in Kenya before 1945.

Estates	Firm	Business	Country of origin/parent
Estates and primary processing			
1906	British East Africa Co.	Exporters of primary produce, manufacturing agents	BEA, Mitchell Cotts (after 1945).
1907	East African Tobacco Co.	Trading and growing tobacco products	British Imperial Tobacco Co. (UK) (later British American Tobacco Co.).
1922	East African Breweries.	Beer manufacture	Ind Coope Ltd (UK).
1924	African Highlands Produce Co.	Tea manufacture	James Finlay (UK).
1931	Anglo-French Sisal Co.	Sisal growing	Anglo-French Sisal Co. (Paris).
1924	Kenya Tea Co.	Tea and coffee processing	Brooke Bond (UK).
1932	East African Tanning & Extract Co.	Wattle bark and extract manufacture	1 Natal Tanning and Extract Co. 2Forestal Land & Timber (UK).
1935	East African Meat Co.	Meat processing	Liebigs (UK) (1969 Brooke Bond, Liebig).
Trading			
1920	Bird & Co.	Merchants, transport shipping, warehousing	Bird & Co. (UK).
1920	Gibson & Co.	Manufacture gents, export of primary produce	Gibson & Co. (UK).
1924	Gailey and Roberts	Import and servicing of machinery	United Africa Co. (Unilever Ltd, UK).
1934	Holland Soda Co.	Shipping agents and warehousing	Holland Africa Line (Holland).
Manufacture and minerals			
1911	Magadi Soda Co.	Soda extraction and processing	1 East African Syndicate. 2 Imperial Chemicals Inc. (ICI) UK.
1922	East African power	Power generation	Balfour Beatty (UK) and Power Securities (UK).
1933	East African Portland Cement	Cement-processing, clinker-grinding	Associated Portland Cement (UK).

Source: Adopted from Swainson (1980) with minor changes.

> artisans and clerks in European and Asian firms and in the colonial administration. Africans controlled petty trade, subsistence farming and subsistence pastoral agriculture within the Native Reserves or worked as labourers for Europeans and Asians (Jorgensen, 1975)".

Based on the colonial setting laid out in Kenya, it is clear that from the outset of British colonial rule emerged a policy of simple primary production without any substantive and immediate policies towards industrial development. Lack of an industrial policy demonstrated unwillingness and lack of effort by the British Government towards the development of a manufacturing industry in Kenya. Hence the manufacturing industry remained nascent characterised by low technological capability development and thus low value added manufacturing activities. The existing policies were in favour of investment in commercial agriculture and a few mercantile activities strictly dominated by foreign and non-indigenous firms - Asians firms. Existing literature on Kenya's industrialisation explicitly articulate lack of political will from the British colony in support of manufacturing industry that is, Swainson (1980) puts it succintly:

> "During this time it is not surprising that the colonial office were indifferent and often hostile to colonial attempts to develop manufacturing industry. The work of the so-called development agencies before 1939 illustrates the general unwillingness on the part of the British Government to encourage colonial industries. The Empire Marketing Board, for instance, gave no assistance to any forms of manufacturing and colonial development advisory committee in theory placed no limit on its spheres of activity, but in practice it totally ignored the industrial sector (Swainson, 1980)".

Analysis done indicates that very few manufacturing industries were established in the early colonial days and most of the agricultural commodities (78%) were exported to Britain in their raw and unprocessed form (Vaitsos, 1991). As Swainson (1980) frames it '… the settler bourgeoisie in Kenya was involved in a process of primitive accumulation of capital' (Swainson, 1980). The processing was undertaken under strong tariff wall and trade policies that only allowed processing of a few agricultural commodities for local consumption. It is important to emphasise at this point that a few investments were also made outside the agro-based industries by subsidiaries of major MNCs to supply certain essential services and goods e.g. cement, salt, power and lighting (Table 1). Such subsidiaries of British MNCs included; Magadi Soda Co. Ltd (1911) for the extraction of soda ash; East African Power and Lighting Co. Ltd (1922) for electrical power generation; Gailey and Roberts (1924) for import and distribution of agricultural machinery and East African Portland Cement (1933) for cement clinker grinding.

Since imports were protected, generally no imports from other countries were allowed into the Kenyan market during this period as the source of external products remained United Kingdom to a large extent. As mentioned earlier, no strong manufacturing promotion would be encouraged since Kenya was supposed to serve as a protected market for the British manufactured goods and as such emergence of strong manufacturing firms was bound to create competition for the British manufactured goods in the country and other neighbour-ing colonies. However, during the Second World War, the European settlers in East Africa were unable to get their imports from Britain by sea culminating in a severe shortage of consumer goods (Munene and Wandibba, 1989). Due to intense pressure by the settlers, there was a slight change in the imperial policy in 1940 allowing selective kind of processing for I-S and only by foreign and settlers firms (Swainson, 1980). Nonetheless, no concrete policy was formulated in favour of industry which still reflected lack of colonial will, commitment and effort to establish a dynamic manufacturing base in the country.

In sum, the discussion held for the period before 1945 indicates that a few things are important to take into consideration when examining FDI in relation to Kenya's industrialisation process and policy. The first one is that extremely few and simple manufacturing activities were undertaken during this period. Only products meant to substitute imports, that were scarce during the war period, could be manufactured under high tariff wall. No policy existed in support of an industrial development - one characterised by a strong entrepreneurship culture - hence low technological capability development. Secondly, despite the simplicity of the manufacturing undertaken, it was fully controlled by the British settlers and FDI from other countries with no involvement of indigenous locals - the indigenous firms remained absent. Thirdly, the British settlers and other foreign investors also dominated commercial agriculture strictly excluding Asians and the indigenous Africans. The investment done was concentrated on estate-based export commodities such as tea, coffee, wattle and sisal which were exported in their raw form. Forthly, while a few settlers showed interest and actually moved into construction and real estate, foreign firms went into large scale trading where they became dominant. Fifth, Asian firms were concentrated in small trading activities. However, some of the Asian-owned firms originally in the mercantile trade branched gradually into light manufacturing, which formed the basis for their initial capital accumulation in Kenya (Leys, 1975, 1996; Kaplinsky, 1978; Swainson, 1980; Himbara, 1994).

The period between 1945 and 1963: The period after the Second World War was characterised by major changes in the international capital movement (Dunning, 1972; 1993). There was free movement of capital across national boundaries with MNCs serving as the main conduit of capital flow across national and international boundaries. This culminated in stiff international competition to expand international capital with United States taking a dominant position. United States had assumed a dominant position as a result of increased domestic investment in technology, extensive capital accumulation and great transformation of its industrial organisation with tremendous increases in labour productivity. It is argued that, the huge advance by the United States in 1940s was the main cause of upheavals witnessed in technology, organisation of labour and relations of production in the world after the Second World War. There was a change in the pattern of international capital when United States industrial capital started turning outward in search of new global markets (Dunning, 1972).

The dominance of the United States capital in the international market had long-term effects to Britain's political and economic levels (Louis, 1977). The increased international competition to expand capital globally made Britain feel threatened over its colonial territories. Economically, Britain was at a disadvantage in that it had just incurred huge expenses during the war resulting in increased foreign aid and dependence on the US. There was also the looming danger of severe unemployment in Britain if production slowed down to match available materials and foreign exchange (Cowen, 1980 p. 145). To take care of these constraints, the British Government had no option than to try and channel more government resources into primary and industrial production. In addition, the British Government encouraged the British MNC firms to invest in colonial territories–both in the production sector and in the manufacturing industry. The British Government, therefore, implemented a radical policy change from'extraction of raw materials and restriction of industrialisation' to promotion of industrialisation alongside agricultural production. An industrial development policy was therefore designed after 1945 to promote development of secondary industries in addition to agricultural production (Lee, 1967).

In response to this policy change, FDI initially concentrated in the field of commercial farming and raw material extraction began to change in favour of foreign investment in manufacturing industry, albeit gradually (Swainson, 1980). Many British manufacturing firms went to Kenya after 1945 to manufacture goods previously imported under protected conditions - quota restriction and high tariff walls. Available statistics show that by mid 1960, approximately 78.8% of FDI in Kenya was British owned (Vaitsos, 1991). Nevertheless, there was also intensified penetration of foreign firms and an inflow of predominantly industrial capital from other countries such as: United States, Germany, Denmark and Canada among others (Eglin, 1978; Swainson, 1980). Examples of such MNCs include Del-Monte (1950), Pepsi Cola (1953) and Coca-Cola (1956) all from USA; Jensen and Nicholson (1959) from Denmark and Bata Shoe Company (1958) from Canada (Table 2). The period after the Second World War in 1945, therefore, marked a significant point of departure in the history of Kenya's manufacturing industry with dynamics of I-S and participation of FDI in manufacturing becoming more apparent.

From the discussion undertaken for the period 1945 - 1963, the following things have emerged. First, it can be argued that the first major drive towards industrialisation in Kenya started in the period 1945 - 1963. This period can be regarded as the starting point of actual manufacturing in Kenya with policy support from the authorities, in this case the British Government. However, at this early stage, industrial capabilities and their development remained rather weak. Also, with the exception of Asians of the Kenyan origin, the indigenous Africans had not ventured into the manufacturing - thus entrepreneurship capability on their side was extremely weak or altogether missing. Secondly, that the mode of industrialisation adopted at this time was I-S supported largely by the state. This mode of industrialisation was implemented to a large extent under strong tariff wall and trade barriers. Thirdly, that in comparison to the period before 1945 when investment was largely concentrated in commercial farming and mercantile, there was a significant increase in foreign investment into manufacturing Industry in the period after 1945, which was reflected in a major shift in the sectoral pattern of investment by FDI. The fourth point is that comparing settlers' capital to that of the incoming MNCs, the settlers' capital remained weak after their failure to take it into manufacturing industries. In actual fact, the incoming MNCs and the Kenyan Asians ended up acquiring most firms that had previously been owned by local settlers making the incoming MNCs and a few Asian firms become dominant in the large manufacturing category especially in the period 1945 -1955. Although Asians had ventured into manufacturing before 1945, they were only a few “due to the constraints of capital and lack of credit facilities from European banks" (Swainson, 1978).

Post-independence: The early decades of import substitution

At independence, Kenya inherited I-S industrialisation pursued during the colonial days. Adoption of I-S appeared to be the trend world-wide in that during the period 1950s - 1960s, I-S industrialisation strategy appeared to be the norm in most developing countries (Van Arkadie, 1964; Bruton, 1998). In the Kenyan contex, the I-S framework mainly advocated for a large role of public sector participation and protection of infant manufacturing industries. Broad based economic controls in favour of industrial sector were implemented such as: combination of tariffs and quotas supplemented by foreign exchange allocation measures; use of overvalued exchange rates to maintain import costs low; favourable credit and interest rate policies intended to subsidise manufacturing of consumer goods. As a result of high increase in overall demand for consumer products in the domestic market, the implementation of I-S framework encouraged production for domestic market shielded from imports and international competition (Van Arkadie, 1964; Mekkelsen, 1986; Nyong'o, 1988; Coughlin and Ikiara, 1988). Under I-S, the economy was characterised by rapid economic growth - in the Kenyan economic history this period is usually referred to as the "golden economic period" due to the high GDP growth levels recorded. The GDP growth rate averaged above 7% in the period 1965 - 1972 (Gachino, 1998), while manufacturing value added grew by over 10% in the period 1964 - 1971.

At independence, Kenya was ambitious to diversify her foreign investment by attracting FDI from different countries in the world. Unfortunately, during this period of transition to independence, the country was faced with capital disinvestment problem; severe outflow of foreign capital was taking place following the eroding confidence among foreign investment resulting from the intended indigenisation of economic activities contained in the 'Kenyanisation' policy. In order to revert this process and to attract more diverse foreign investment, the Kenyan Government decided to enact the Foreign Investment Protection Act (FIPA) in 1964, which guaranteed foreign investors the right to transfer profits, dividends and capital out of the country. Under FIPA Act, foreign investors were supposed to apply for a "Certificate of Approved Enterprise" from the Ministry of Finance. The determining criterion was the firm's participation on the economy and thus only foreign enterprises viewed as capable to participate in Kenya's economic development would be granted this certificate. These investors would also be assured that their firms would not be compulsorily acquired under the indigenisation policy, which was launched upon independence (Langdon, 1978). This was also supported by sessional paper no. 10 of 1965 entitled: African Socialism and Its Application to Planning in Kenya. The sessional paper reaffirmed the government's commitment towards attracting more foreign firms with no nationalisation unless state intervention was deemed necessary to prevent wastage of raw materials (Langdon, 1978; Nyong'o, 1988).

Continued effort to attract investment and to reduce capital outflow seemed to gather momentum with time. A New Projects Committee (NPC) was set up in 1968 to review more vigorously the foreign applications interested in making investment in Kenya. This committee which

Table 2. Major foreign investments 1945 - 1963.

Code	Company	Date	Product	Owned by
Food products and beverages				
Np	Schweppes (EA) Ltd	1954	Soda drinks	Allsops & Schweppes
Ext	Allsops East Africa	1954	Beer	Allsops (UK)
Np	Pepsi Cola	1953	Soda drinks	Pepsi Cola (USA)
Np	Fitzgerald Baynes	1953	Soda drinks	Canada Dry (UK)
Np	7-Up Bottling Co.	1954	Soda drinks	7-UP Company (USA)
Np	Kenya Canners	1950	Canned fruits and vegetables	pickering & West (UK) Del Monte (USA)
To	Associated Packers	1956	Fruit squashes, puddings, juices, jellies	Mitchell Cotts (UK)
To	ABC Foods	1954	Animal feeds	Baumann & Co. and Steel Bros (UK)
To	Lyons Maid	1959	Ice cream	Lyons (UK)
Np	Coca Cola Mid Africa	1956	Soft soda drinks	Coca Cola (USA)
Np	EA Tobacco	1954	Manufacture tobacco and cigarettes	British American Tobacco (BAT) (UK)
To	Kenya Orchards	1948	Canned fruits and vegetables	Marshalls Ltd (UK)
Ext	EA Breweries	1952	beer	Ind Coope (UK)
Non-food manufacturing				
Np	Carbacid Manufacturing Co.	1954	Carbon dioxide	Carbacid (USA)
Np	Robbialac Paints	1956	Paints and Varnishes	Robbialac (UK)
Np	Leyland Paints EA	1954	Paints and Varnishes	Baumann & Co. and Leyland Paints (UK)
Np	Cassmann Brown	1953	Roofing felts	Cassmann (UK)
Np	Sadolins Paints	1959	Paints and Varnishes	Sadolins
Np	Jensen & Nicholson	1959	Paints and Varnishes	Jensen & Nicholson (Denmark)
Np	East African Oxygen	1949	Oxygen	British Oxygen (UK)
Np	Bamburi Portland Cement		Cement	Amalgamated Road-Stone Corp. (UK) Cementia Holdings AG
Ext	EA Portland Cement	1956	Cement	Assoc. Portland Cement
Np	Avon Tyre	1958	Bicycle inner tubes	Avon Tyres (UK)
Ext	EA Bata Shoe Co.	1940 1958	Bicycle inner tubes Leather and shoes	Bata Shoe Co. (Canada)
Np	EA Stationary Manufacturers	1949	stationary	Dickinson Co. (UK)
Np	Metal Box EA	1948	Metal containers	Metal Box (UK)
Np	Crown Cork Co. EA	1948	seals	Crown seals (UK)
Np	Van Leer Containers EA	1952	Steel drums, pails	Van Leer Containers (Holland)
Np	Shell Chemical	1952	Industrial Chemicals	Shell-BP (UK)
Np	Sterling Winthrop	1953	chemicals	Sterling Winthrop (USA)
Np	Finlay Industries Ltd	1952	Brushes, wooden articles	James Finlay (Scotland, UK)
Np	EA Oil Refinery	1959	Refining of crude oil	Shell-BP (UK)
Np	Walparmur EA Ltd	1961	Paints and Vanishes	Walpamur (UK)

Source: Adopted from Swainson (1980) with minor changes.
Key: Ext - extension of existing plant; To takeover of existing firm and Np - formation of new plant.

drew representatives from various institutions and government ministries acted as the negotiation team on all issues pertaining to investment ranging from level of tariff protection, shareholding, and management among others (Langdon, 1978). Capital Issues Committee (CIC) was set up in 1971 to cut down continued capital outflow from Kenya following the perpetual fever at the time that foreign investment in the country would be forced to go public and allow Kenyans to become shareholders. The aim of CIC was therefore to revert this trend by approving all future issues and capitalisations of reserves in firms with majority foreign interest (Leys, 1974: Swainson, 1980). On the international front, Kenya became a member of Multilateral Investor Guarantee Agency (MIGA), which issues guarantees against non-commercial risk to enterprises that invest in member countries. Kenya also became a member of International Center for the Settlement of Investment Disputes (ICSID), and of Africa Trade Insurance Agency (ATIA). As a result, Kenya attracted a substantial amount of FDI in the period 1960s - 1970s - where in most cases the investors were subsidiaries of wholly owned MNCs and occasionally joint participation between MNCs and the state. A large share of this investment went into import-substituting industries (Kaplinsky, 1978; Swainson, 1980; Nyong'o, 1988).

Compared to the period before independence there was a drastic change in this period with foreign firms showing a clear dominance in Kenya's manufacturing industry. Available statistics show that by 1967, about 33% of the FDI stock in Kenya was in manufacturing (Hveem, 1975). From the Census of Industrial Production undertaken in Kenya in 1967 and covering 607 establishments, it was noted that 433 of these establishments with 50 or more employees were mainly or wholly foreign owned by non-citizens. Detailed analysis of the Census of Industrial Production data further revealed that these enterprises accounted for 71% of the value added and 72% of the total sales for manufacturing firms employing 50 people and above, which in turn, generated more than 82% of the gross manufacturing product (Eglin, 1978). This clearly demonstrated the significance of foreign investment in the early decades of Kenya's independence and as noted by Vaitsos (1991) on the Kenya's development plan for 1970 - 1974:

> "…. long-term capital inflows, especially by TNCs, strongly influenced the evolution and growth of modern manufacturing and services during the first decade after independence as confirmed by macro, sectoral and sub-sectoral evidence (Vaitsos, 1991)."

Besides the fact that most foreign companies saw potential market opportunity in the East African region, the region was also richly endowed with raw materials and cheap labour. An analysis of FDI inflows to Kenya in comparison with other developing countries in Africa revealed that while 32.4% of FDI in Kenya went into manufacturing by 1967 the average for the whole of Africa that went into manufacturing was only 18.8%. FDI going to commercial agriculture in Kenya was also relatively high at 21.4% in comparison to 7.5% for the whole of Africa. The average for FDI in Africa going into trading activities was 19.4% which was slightly higher than FDI going into trading activities in Kenya which was 16.9%. Finally, there was almost negligible foreign investment in petroleum and mining in Kenya while the average investment for Africa was 19.4 and 29.6% respectively (Kaplinsky, 1978).

This supported empirically the thesis that after independence foreign capital, FDI, in Kenya was not concentrated in primary production but rather in manufacturing and services following increasingly high inflow especially into the two sectors and especially manufacturing industry. It is therefore argued that this trend of foreign investment flow into the manufacturing industry affected significantly the evolution of I-S strategy at the time. For instance in 1977, imports of consumer goods dropped sharply to just 15% of the total imports while imports of intermediate goods rose to about 67% of the total imports (Vaitsos, 1991). This seemed to indicate success in the pursuance of the I-S mode of industrialisation. More so, it also indicated transfer of technology to be used in their production processes - although participation by domestic firms was still minuscule, this is important as it would result in demonstration effects, training of the local labour, learning by performing and in turn all these would serve to stimulate broad industrial capability development.

Apart from availability of raw materials and cheap labour, Kenya was also favourable for among other factors; stable political climate and macroeconomic conditions, a rapid economic growth rate, a large and growing market encompassing countries of the then East African Community and high tariff protection. Given their keen interest on the protection level, MNCs wanted and in fact sought involvement even in the determination of the extent and structure of protection to be granted (Swainson, 1978, 1980; Eglin, 1978; Vaitsos, 1991). As an example, protection from imports was a key pre-investment negotiation issue at the time: effective rates of protection were therefore very substantial, particularly for consumer goods industries. In about 90% of the cases studied by Langdon and Godfrey (1973), it was observed that the type and range of existing protection was largely influenced by the MNCs' bargaining strength and position. Most MNC firms therefore enjoyed a virtual monopoly, which ensured their profits (Eglin, 1978). The inflow of equity capital in the 1960s -1970s was mainly in the agro-based industries with textile taking a clear lead (Leys, 1975, 1996; Eglin, 1978; Langdon, 1978; Kaplinsky, 1978).

At independence, the Kenya's economy and in particular manufacturing ownership structure was dominated by the European and Asian firms. MNCs from United Kingdom dominated in the European firm's category, which were engaged in heavy manufacturing processes while Asian firms dominated in the light manufacturing industries almost sharing the entire cake with no portion of it left for the indigenous locals (Kaplinsky, 1978; Swainson, 1980; Himbara, 1994; Leys, 1996). Although by this time Kenyan manufacturing industry was relatively the most advanced in comparison to those of the other countries in the region. There was a need to integrate the Africans into the mainstream of the economy despite their low entrepreneurship skills, lack of experience and finance.

As a preamble to the indigenisation policy; it is recalled that during the colonial days, Africans served as labourers in the commercial firms owned by the foreigners and were not allowed to participate in any form of trade or manufacturing activities - this denied them a chance to become entrepreneurs from early on. Africans could not obtain any form of loan or financial credits to support and nurture their ambition into either trade or entrepreneurship. Incidentally, they had no collateral since at the time, they were not even allowed to acquire and/or own land title deeds, which could serve as collateral with existing financial institutions. This notwithstanding, the existing Banks viewed Africans as depositors but not as potential borrowers claiming that Africans had a different mentality on repaying loans as they failed to see it as an obligation. The banking style relied to a large extent on social interaction with British banks funding British firms, Asian banks funding Asians and since there were no African banks, no one had the will to extend loans to indigenous African firms (Jorgensen, 1975).

As a result of this disequilibrium in the economic setting, there was a need to indigenise commerce and manufacturing industry at independence. The Kenyan Government established a Kenyanisation of Personnel Bureau (KPB) with an aim to Africanise senior positions in the civil service including parastatals and to also regulate the number of foreign workers in the private sector by introducing work permits. In addition to encouraging MNCs, the Trade Licensing Act of 1967 was enacted, to help Africans venture into commerce and trade. To this effect, foreigners were excluded from trading in certain locations and from dealing with certain kinds of goods. Such goods included basic foodstuffs and clothing and a few other items such as cigarettes, soft drinks, farming implements and basic hardware which were all produced or processed locally under MNCs I-S industries (Leys, 1974). Since the Asians were restricted from joining retail and wholesale trade, this forced them to venture into light manufacturing.

The greatest effort by the government towards indigenisation took place in the creation of support institutions such as Industrial and Commercial Development Corporation (ICDC), Industrial Development Bank (IDB) and Kenya Industrial Estates (KIE) etc. Some of these institutions allowed joint partnership with MNCs as well as providing soft loans and technical support to the Africans who were by then being encouraged to become entrepreneurs. Some institutions encouraged establishment of linkages between indigenous firms and foreign firms. This was the first significant attempt to integrate indigenous firms into the manufacturing industries. An interesting scenario that emerged from the intended indigenisation policies was that of Asians in Kenya. After being restricted from participating in trade and commerce, the Kenya Asians ventured into light and medium manufacturing using own finance, and from which they were able to entrench themselves, have developed some manufacturing capabilities and have dominated ever since (Pearson, 1969; Swainson, 1980; Himbara, 1994).

Nevertheless, despite the spirited effort by the government to implement indigenisation policy especially in the manufacturing industry not much progress has been achieved. The nature and characteristics of manufacturing industry has virtually remained the same as it was in the early decades of Kenya's independence. Taking as an example, the ownership structure by race in 1990, we note that according to Himbara (1994), in a sample of 100 large scale manufacturing firms; Asians accounted for 75%; Foreign and JVs 11%; Kenya Africans 5%; Publicly held 4%; State firms 4%; African/Indian 1%. Although these percentages do not represent performance, they somewhat support the critique that indigenisation policy had not succeeded as the disequilibrium was still widely reflected in Himbara's study. It is common knowledge that the country has not succeeded in transforming its manufacturing industry, which is still dependent on foreign technology as domestic industrial capability remains weak and manufactured export goods with little value added. Jorgensen (1975) offered a strong critique of the Kenyan indigenisation process which still seems to hold regarding it as lacking in credibility. He argued that, "since independence the process would have required integration of the various sectors and subsectors of the economy to increase self-reliance and decrease dependence on the import of foreign technology, foreign machinery, foreign intermediate goods and components, and foreign consumption patterns on the one hand and decreased dependence on the export of agricultural raw materials and of minerals on the other" (Jorgensen, 1975 p. 156). This has however not been the case and African indigenous firms remained small in size and both technically and financially weak.

Following her ambitious plan for industrialisation in 1960s - 1970s, Kenya enacted and implemented several industrial promotion policies within I-S framework particularly meant to stimulate and strengthen the industrial base and especially within manufacturing sector, which was at the time characterised by weak technological capabilities, weak supporting institutions and lack of finance for business expansion. Several development finance and industrial promotion institutions intended to cater for small and large scale firms were established. Ideally, these institutions were supposed to play a facilitation role in industrial development by advancing indigenous manufacturing technology; assisting in technology transfer; offer industrial training, promote Industries that exploit locally available raw materials; promote linkage (e.g. between locally owned firms and MNCs); offering financing capital, enhance production of goods that are competitive for exports. Such institutions included Industrial and Commercial Development Corporation

(ICDC); Development Finance Company of Kenya (DFCK); Industrial Development Bank (IDB); Kenya Industrial Estates (KIE); Kenya Bureau of Standards (KEBS); Kenya Industrial Research and Development Institute (KIRDI). Others included Kenya Industrial Training Institute (KITI); National Council for science and Technology (NCST) and Universities and Polytechnics. A brief discussion on the role played by some selected institutions in line with their objectives is presented in the next section.

FDI AND INDUSTRIAL CAPABILITY DEVELOPMENT: THE ROLE OF INSTITUTIONS ESTABLISHED DURING THE IMPORT SUBSTITUTION PERIOD

In the section above, we have shown that at independence, Kenya inherited a manufacturing industry characterised by relatively weak indigenous industrial capability with low value added activities and productivity performance. There was however increased FDI inflow and participation in the manufacturing. At that time, supportive institutions were missing while new ones were getting established and still grappling with learning to perform. In such a context, where institutions are missing or weak in performance, then their role in systemic coordination becomes equally weak. This results in weakened role for instance in financing, knowledge generation and diffusion and consequently low levels of industrial capability development. Given this background, this section examines the type and specific role played by institutions during the I-S period.

Industrial and commercial development corporation: Industrial and Commercial Development Corporation (ICDC) was first established in 1954 by the colonial government. At inception, it was established as the Industrial Development Corporation (IDC) to promote the colonial industrial development but after independence in 1963, IDC's mandate was expanded and diversified in the economy to provide project and commercial finance to enterprises. Consequently, IDC was changed to Industrial and commercial Development Corporation (ICDC) mandated to promulgate industrial capabilities by promoting participation of indigenous Kenyans in industrial and commercial development, encouragement of Industries with capacity to earn foreign exchange, facilitate rural development, increase use of locally available raw materials, create job opportunities and enhance diversifycation of the economy. The industrial and commercial development was facilitated through: venture capital finance; export financing; management, support and consultancy services and administration of funds on social-economic programmes at agreed terms.

ICDC has co-invested in various leading commercial and industrial ventures in Kenya that are either local firms or MNC subsidiaries. This is important as it harnesses the resources and expertise of MNCs in the promotion and financing of joint venture (JV) projects. Projects financed included some of the established local companies as well as MNC subsidiaries in Kenya among them the General Motors Kenya (GMK) Limited which boasts of significant linkages in the auto industry with domestic firms including body builders. ICDC is an important shareholder in two main industrial financing institutions; Industrial Development Bank Ltd. and Development Bank of Kenya Ltd. This kind of coordination and establishment of financial linkages is important for the support of firms in an industry for their capability development and eventual growth, innovation and performance.

However, despite a relatively good performance in ICDC, it has been criticized for failing to meet one of its major objectives to reach the small entrepreneurs. The security required for ICDC's loans has tended to favour the already established entrepreneurs and to those already owning other enterprises. The implication of this is that firms owned by indigenous Africans would not qualify for financial support. ICDC officials interviewed felt that ICDC was not playing its role of promoting participation of indigenous Kenyans in industrial and commercial development effectively. Performance in venture capital and export finance had declined. ICDC was severely constrained in that they have to rely on the government for finance making its capacity limited. This was happening at a time when government was beginning to withdraw support.

Development finance company of Kenya: Development Bank Company of Kenya (DFCK), a financial institution, was incorporated as an investment company in 1963 to promote industrialisation after independence. The government was the main shareholder alongside other shareholders which included foreign financial institutions. DFCK priority was accorded to economically viable projects deemed to have the necessary capacity to contribute to economic development effort such as employment creation, increase foreign exchange earning as well as use of locally available raw materials. It was indicated that DFCK performed well in the early days.

Nevertheless, DFCK has been faced by several constraints. As noted above, the financial institutions were funded primarily through loans and grants received from multilateral and bilateral development institutions, as well as from the Kenyan Government. The government allocations of development finance institutions have been virtually eliminated following a government policy to stop funding parastatals. At the same time, the government was gradually rescinding its role as an active guarantor to loans obtained by development finance institutions from other financial institutions most of which are foreign (KIPPRA, 2001). Nonetheless, the government continues to be a key shareholder in these development finance institutions (DFIs); a situation that makes willing lenders and shareholders shy off from lending their funds to DFI.

Without privatization, foreign lenders are reluctant to continue their participation. To get round this problem, the DFIs have adopted universal banking policy which has already resulted in the conversion of DFCK into a bank. This has worsened the situation as the interest rates remain relatively high and hence not favourable of industrial promotion. Firms will shy off from taking loans at such high interest rates implying that they no longer afford to acquire new machinery and technology using loan facilities from DFCK. In the long run this works out to weaken firms' entrepreneurship and capability development and consequently their ability to learn from and compete with the MNCs present in manufacturing.

Industrial development bank: Industrial Development Bank (IDB), another financial institution, was established in 1973. IDB was established for the purpose of furthering industrial and economic development by promoting, establishing, expanding and modernising of the medium and large scale industrial enterprises, including mining, agro-industries, engineering, tourism and transport and shipping. IBD provides the following forms of financial services: medium and long-term finance; working capital, machinery finance and export trade related banking facilities; direct equity investment; guarantees for loans from other sources; underwriting of security issues, shares, stocks and promissory notes.

In addition to the finance obtained from equity and accumulated reserves, the government as the main shareholder is supposed to provide finance to IDB. But due to the balance of payments problems in 1980s, the government role as the chief financier has declined forcing IDB to look for alternative sources of finance. Since the government no longer invests in IDB - given its blanket rule to stop investing in parastatals - IDB then faces financial difficulties in its operations. Recall also from the above that the government no longer guarantees its lines of credits. To overcome these problems, IDB decided to start offering banking services through mobilization of deposits. Nevertheless, this has not been very successful, as customer deposits have remained extremely low. IDB also continued to face severe difficulties in securing credit from foreign financiers, who demand that the government acts as a guarantor or privatises IDB to qualify for funding. As confinded during the interview, all these resulted in a declining industrial role of IDB over time. Introduction of quasi banking activities makes interest rates and other services comparable to those of other commercial banks whose industrial promotion is usually minimal.

Kenya industrial estates: Kenya Industrial Estates Limited (KIE) was established in 1967 to encourage entry of indigenous firms into the manufacturing industry. This was expected to result in indigenous manufacturing capability in the long run. Indigenous firms entering into the manufacturing industry were basically characterised by extremely small scale, they were basically 'start ups' small and medium enterprises (SMEs) faced with severe financial constraints and with weak technical skills. They needed finance for capital investment alongside technical support mainly on how to set enterprises and manage them. KIE was formed as a supportive institution to extend assistance by a way of offering technical and financial support to indigenous firms. KIE targets enterprises ranging from micro enterprises commonly referred to as Jua Kali artisans to modern scale industries. The enterprises must be start-ups or expansions solely owned and managed by indigenous Kenyans and located in the country. Currently, the perception is that KIE is far from achieving its perceived role of spurring industrial development.

Despite the effort made by KIE, its perceived role to promote industrial development has not been achieved. Operations of KIE are still faced by many constraints. Finance being one of them. The government has not been able to provide adequate finance. It was noted that the funding which used to be obtained from donors declined drastically especially in the 1990s when most international financial bodies and donors pulled out of the country. More so most of them refused to show commitment in funding resulting in KIE's due to its poor performance. KIE also lacks adequate capacity to offer effective technological training and supervision. However, the most severe problem is lack of enough working capital required for KIE's recurrent expenditure given the reduced financial support from the government as well as from donors and international funding agencies. This means that KIE was unable to hire and sustain qualified personnel. This leads to the next problem in that KIE lacks the capacity to study the industry and play a more active role in the match making process, which would in turn promote linkage proliferation in the industry. For instance, discussions held with KIE officers revealed that only a few cases existed of linkages formed between SMEs and MNCs as a result of facilitation done by KIE.

Similarly, KIE's role to promote industrial parks/ incubators had not been a success with only a few cases of such parks surviving from bankruptcy and collapse. Although one of KIE's mandates was to pass information, interestingly it does not even have an internet site where information could be placed for easy access by client firms. From the point of client firms, complaints have been launched that interest rates charged by KIE were extremely high. As one can rightly guess, when firms fail to get financing loans in atmosphere of escalating liberalisation under the aegis of structural adjustments, it is then expected that most of them would face stiff competition from MNCs and perhaps exit business. This has actually been the case and when they hang on, most of them remain static in capability development characterised by poor performance. These results in low profitability, reduced working capital and most a times inability to meet debt obligations. The implication of this is that KIE plays a very minimum role in industrial development.

Kenya bureau of standards

The Kenya Bureau of Standards (KEBS) was established by an act of parliament in 1974 to promote and make manufactured goods competitive in both the local and external markets by raising quality. KEBS was therefore formed as a regulatory body mandated to deal with strengthening of manufactured goods and services through the application of standards and by providing technical advice on quality management in Kenya. Enhanced standardisation in an industry can stimulate technology transfer and diffusion. As a technical language needed to communicate industrial and service specifications, it can equally lead to industrial growth and capability development which would come a long as firms and industries strive to achieve minimum set standards or existing international standards. KEBS organises trainings and seminars to promote and develop standardisation mainly in manufacturing and service at all levels. Participants would be drawn from local and MNCs. This way the participants get to interact and share knowledge, ideas, skills etc. This is sometimes extended to include attachments and firm visits by the KEBS officers. In these trainings and seminars, the resource persons are drawn from public and private sector – with MNCs as the dominant contributors.

Nevertheless, despite the achievements made so far, there are still many problems facing KEBS. Inadequate funding to facilitate training, dissemination of information by a way of exhibiting in show grounds and others such as trade exhibitions, seminars and symposia to educate the manufacturers as well as consumers on standardization work and increase their awareness. There is extremely low patronisation by manufacturers blaming it on lack of capacity such as recent metrology techniques coupled with few skills available in terms of professionals required. Although it was indicated that with regard to human resources development some of the research officers had been sent abroad for further training, there is still inadequate capacity to deal with drastic changes in standardisation and metrology. Although KEBS maintains a website providing background information on the institute and the services offered, there is lack of a strong ICT back up from where queries can be launched. Information, say on training placed on the internet site would reach a lager audience. Another problem is that there are few testing centres in the country subjecting manufacturers to unnecessary delays waiting. KEBS also need to strengthen its modalities to come up with a meaningful cooperation between players from both the public and private sectors.

Kenya industrial research and development institute: Kenya Industrial Research and Development Institute (KIRDI) was established in 1979 to promote the national industrial innovation process through the development of a sufficient national capacity in disembodied and embodied industrial technologies for the attainment of self-sustaining industrialisation process. Although services are offered at a specified fee, many firms in the manufacturing industry including small and large firms, locally and foreign owned firms have sought KIRDI's services. Interviews conducted indicated that due to the increased demand in their services from the industry, KIRDI has recently started outsourcing for professional services from the private sector – especially MNCs with higher technological capabilities. This strategy seems successful and is now being extended to include other institutions and universities where experts will be taken on contract or part time bases. This coordination strategy is expected to reduce the time manufacturing firms spend waiting for certain services.

Although relatively good progress has been made at KIRDI, internal constraints have hindered KIRDI from achieving its full potential. For instance, the uni-directional staff mobility running from KIRDI to the private sector or universities makes retention of trained staff difficult. Part of the reasons for this is that the salaries paid are low and thus once they get trained they leave to join private firms or teaching institutions, universities and polytechnics. This is fine since it would indicate that KIRDI generates human capital for the larger industry but because of this aspect, most of the time you find that the core staff constitute young graduates with little experience in research. The effect of these is that the productivity of the institute is reduced in terms of research conducted or services offered to the industry.

With the activities of KIRDI funded by the government, it is obvious that this funding may not be enough as this is usually the case with the institutes funded by the government. Due to lack of working capital, it becomes difficult to purchase adequate machinery and facilities for use in the laboratories or stock and maintain library. Lack of funds also does not permit improvement in remuneration and conditions of service. It becomes also difficult to contract services of qualified professionals from the private sector. With availability of funds such professsionals could be engaged for instance to carry out surveys or experiments or train in management such as ISO. Lack of all these denies Kenya flow of spillovers which are necessary for industrial development. To some extent this has an effect to the weak co-operation between KIRDI and the industrialist as they think KIRDI has little to offer. For its development expenditure, KIRDI relied mainly on foreign donors which was no longer enough or assured.

When the government adopted strict fiscal control, especially with SAPs, the implication was that institutions relying on treasury for grants were forced to reduce their operations drastically. To overcome this problem of funds KIRDI established a National Industrial Research

Programme (NIRP) which would draw funds from government, private sector and donors. NIRP would play a more active role for technology development, identify constraints to linkage formation and information flow and maintain a database for industrial technologies. The body would also actively play the matchmaking role to identify and connect for instance SMEs to MNC firms for technical assistance etc. However, to-date KIRDI has not been able to create a technologically vibrant culture. It has for instance failed to trigger technology and innovation interests in most large firms including MNC in the manufacturing sector. This problem is compounded by the fact that there is no attempt from the government to link and co-ordinate the research institutions in the country. Lack of such intermediation reduces spillovers in an industry and thus learning and capability building.

Brief summary of emerging issues based on the role of institutions examined

The institutions established after independence played a substantial role in supporting industrial development by facilitating formation of JVs between MNCs and local firms; offering finance for start up firms or for expansion; advance indigenous manufacturing technology; assist in technology transfer; promote industries that use locally available raw materials and stimulate linkage formation. All these factors were in favour of industrial capability development. They were also in favour of spillover occurrence from FDI into the local firms. However, as time went by some of the institutions were faced with severe constraints such as lack of capital to finance R and D, acquisitions of technology and machinery, training to develop required and adequate human capital to support industrial capability development. As such, some of the industrial development financing institutions were transforming and re-orienting some of their services to include banking services through mobilisation of public deposits. They were therefore forced to charge high interest rates similar to those charged by commercial banks implying declined supportive role to industrialisation - as firms will shy from taking loans for development purposes which would result in capability building. This meant a reduction in their role of nurturing indigenous industrial capability promotion.

One consequence of the above was that the indigenisation process launched to nationalise jobs, encourage and support Africans to venture into trade and manufacturing did not turn out very successful. The policy was intended to implant and nurture an entrepreneurship culture to the indigenous, a process expected to result in capability development inspired by the existing FDI in manufacturing. However, weak or declined role of the institutions were not the only things to blame; there was also slackened commitment from the government side and by the end of the first two decades a clear distribution pattern in the structure of the manufacturing emerged greatly skewed in favour of MNCs and the Asians. The large manufacturing industries in the country were dominated by either MNCs or parastatals; Asians dominated small and medium enterprises while Africans dominated the micro and firms in the informal sector. Although Kenyan Asian and Africa firms benefited from FDI, spillover occurrence, it is impossible to quantify that in this paper.

STRUCTURAL ADJUSTMENTS: THE ERA OF LIBERATION AND EXPORT-PROMOTION

So far we have examined the role of FDI in industrial capability development during the colonial period and during the early decades of I-S. The institutions established to encourage foreign investment and support indigenous capability development were also examined. In this section, the analysis will be done in the context of structural adjustments. The section is divided into several sections starting with economic crises of 1980s which served as the stimulus to the adoption of SAPs. We also examine the economic adjustments with the commencement of SAPs and export promotion. Finally, we relate that to FDI and discuss how policies adopted affected FDI, spillover and broad industrial capability development.

The economic crises of 1980s: Stimulus for structural adjustments

Contrary to the high level of economic growth witnessed until late 1970s, in the period 1981 – 1985, the GDP growth rate declined to about (3.6%) from a growth rate of (6.2%) witnessed in the period (1977 - 1980). The rateof growth in manufacturing output slowed down from (10.3%) in the period 1977 - 1980 to (3.8%) in the period 1981 - 1985. Similarly both agriculture and service sectors recorded substantial declines in the same periods. The breakdown of GDP and sectoral growth rates is provided in Table 3. As a result of the economic stagnation, the manufacturing industries recorded a corresponding decline in manufactured exports. As noted in Glenday and Ndii (2000), merchandise export earnings as a percentage of GDP declined from (19.6%) in the 1970s, to (16.97%) over the period 1980 - 1984 and a further (13.6%) over the period 1985 - 1989 reaching an all time low of (11.5%) in 1987. Compared to the other main sectors of the Kenyan industry, manufacturing share in GDP stagnated at (13%) in the period 1981 - 1985 while agriculture and services in GDP stood at (33%) and (47%) respectively in the same period (Table 4). As will be shown this had some negative ramifications for FDI in terms of inflow and performance.

This decline in economic performance was blamed on

Table 3. Sectoral and GDP annual average growth rates, Kenya, 1972 – 2002.

Sector	72 - 76	77- 80	81 - 85	86 - 90	91 - 94	95 - 00	01	02
Agriculture	3.1	4.2	2.8	4.2	-1.1	1.9	1.3	0.7
Manufacturing	9.6	10.3	3.8	5.7	2.2	1.8	0.8	1.2
Services	3.7	6.4	4.4	5.4	3.0	3.0	2.6	2.3
GDP	3.6	6.2	3.6	5.0	1.5	2.46	1.2	1.1

Source: Sessional paper No. 2 of 1997, economic survey and statistical abstract various issues.

Table 4. Average sectoral share of GDP, Kenya, 1972 - 2002.

Sector	72 - 76	77 - 80	81 - 85	86 - 90	91 - 94	95 - 00	01	02
Agriculture	35	34	33	31	28	27	27	26
Manufacturing	10	12	13	13	14	13	13	13
Services	47	47	47	50	52	54	55	55
Others	5	7	7	6	6	6	5	6
GDP	100	100	100	100	100	100	100	100

Source: Sessional paper No. 2 of 1997, economic survey and statistical abstract various issues.

the inward-oriented strategy stipulated in the I-S strategy. Of course other factors such as break up of the EAC in 1977 had their toll as well. Ensuring economic distortions resulted in severe structural constraints and macroeconomic imbalances - problem of technology upgrading, lack of information on technology sources, lack of managerial and technical skills and financial constraints. Firms failed to develop competitive capabilities to penetrate international markets (Lall, 2001; Wangwe, 1995). The efficacy and efficiency of the institutions formed at independence was declining with little co-ordination among them and lack of finance (Lall and Pietrobelli, 2002). Admittedly, inward looking policies pursued at the time under I-S made it difficult to effectively participate and compete keenly in the export markets. Participation in the domestic and immediate regional market seemed to have had negative implications for Kenya's manufacturing in that by so doing Kenya lost its global competitiveness, which would have cumulatively resulted from participation in the international market - path towards accumulation of export and marketing capabilities. It was believed that following the I-S path, Kenyan exports would never compete internationally and especially at a time when the global market was becoming increasingly competitive and production for exports highly innovation based.

As noted in most studies, high levels of protection seemed to have distorted resource allocation, constricted foreign competition and restricted technology inflows from abroad. There were very few incentives to build technological capabilities and upgrade imported technologies. Not much emphasis was put on things like cost reduction, productivity improvement, quality control, inventory control among others (see Wignaraja and Ikiara, 1999). The I-S industrial strategy was not achieving its perceived industrial and subsequently overall economic development agenda. As a result, the manufacturing industry failed to play a more dynamic role enough to function as "an engine of country's growth" and had not contributed significantly to foreign exchange (Kenya Government, 1994).

Towards structural adjustments programme and export orientation

In light of the above developments, there was a need to pursue an outward-oriented industrial policy in order to re-orient industrial production in favour of exports. Faced with economic stagnation and increasing debt, the government had no alternative than to adopt the structural changes, which were at this time being recommended in the SAPs and economic stabilisation programs advocated by World Bank and IMF receptively (see Logan and Kidane, 1993). Hence, in the second half of 1980s, there was a change in public policy and the government started implementing SAPs. One of the major objectives of SAPs was restoration of internal and external balances through a strong policy of export promotion coupled with drastic reduction in public spending and expenditure switching. There was a strong recommendation towards institutional reforms - for the purpose of encouraging FDI inflow, exports and industrial capability development. New FDI was being encouraged following increased openness to local and foreign investment. Price controls were eliminated and trade protection relaxed. There was free entry into production, services and trade (Mwamazingo, 1999; Glenday and Ndii, 2000). This culminated in a slight recovery in the economic performance in the subsequent years, the GDP grew by

Table 5. FDI inflow and stock, Kenya, 1977 - 2001.

Year	77 - 80	81 - 85	86 - 90	91 - 94	95	96	97	98	99	00	01
Kenya											
FDI Inflows	60	40	31	8	35	13	40	42	42	127	50.4
FDI (% GFCF)	5	1	2	1	2	1	1	1	3	8	3
FDI Stock	344	434	668	694	732	745	785	827	869	996	1047
FDI Stock (% GDP)										9.5	9.2

Note: FDI inflows and FDI stock are in million of dollars.
Source: Kenya, Central Bank; UNCTAD, World Investment Report Various Issues; World Bank, World Development Indicators CD-ROM.

(5.0%) in the period 1986 – 1990 (Table 3). The growth rate in manufacturing suddenly rose to (5.7%) in the same period (1986 - 1990), agriculture (4.2%) and services (5.4%) (Table 4). Available figures on merchant-dise exports indicated that merchandise exports as a percentage of GDP jumped to (13%) between 1978 and 1992 (Glenday and Ndii, 2000).

However, despite the observed improvement in economic performance, the rewards were short lived. Part of the blame was put on the government failure to show serious commitment to the reforms it was undertaking. For instance, the liberalisation measures introduced in mid 1980s were being reverted; some were getting halted or applied intermittently (Mwamazingo, 1999; Ronge and Nyangito, 2000). The economy once again seemed to have been headed for another doomsday as reflected by the figures in Table 3 for the interval (1991 - 94). The government, however, started showing keen commitment in the first half of 1990s. So by 1993, the government undertook far reaching structural reforms to reverse the declining trend in Kenya's economic activities: removal of price controls, removal of import licenses, tariff reducetions, liberalisation of foreign exchange markets, and privitisation of public enterprises. Reforms aimed at packaging more attractive investment incentives, streamlining public enterprises and strengthening financial institutions were made.

Deeper economic crises under structural adjustments and the consequences on FDI

Despite the introduction of SAPs, in the 1980s and introduction of new reforms by early 1990s, the initial in Kenya escalate. However, in the last couple of years, inward FDI has risen fairly rapidly relative to the past years reaching US $ 42 and US $ 127 million in 1999 and 2000 respectively. The FDI stock has remained on an upward trend; increasing from US $ 344 million in 1977-80 to US $ 732 million in 1995 and US $ 1,047 million in 2000. FDI stock had an average growth rate of 12.7% (in current terms) for the period 1977 - 2001 and a GDP average share of 9.4% for the period (2000 - 2001). Despite this increase in the period, Kenya still lies behind years prior to 1990s recorded very low economic growth than any other period before. During the period 1991 - 1994, the economy recorded a GDP growth averaging below 2.0%. The manufacturing sector growth rate continued to decline tremendously. It declined from (5.7%) in the period 1986 - 1990 to (2.2%) in the period 1991 - 1994 (Table 3). Major monetary indicators such as inflation, real interest rates and exchange rates all shot up during the period 1991-94. This scenario presents a weak and un-conducive learning atmosphere hence reduced effort towards industrial capability development in the period.

Several reasons were responsible for the poor economic performance: withdrawal of foreign aids, political unrest, and high oil prices during the Gulf war and the world economic recession. However, the major one was the multiparty politics which led to immense political unrest resulting in anxiety and uncertainties of foreign aid, which in turn had negative consequences on the inflow of FDI. This also affected the performance of institutions resulting in reduced effort in their role in industrial capability promotion. FDI inflows in Kenya, which was relatively high in the 1970s, began to decline. Table 5 shows that FDI inflow which averaged US $ 60 million in the period 1977 - 1980, declined to US $ 31 in 1986 - 1990 and had US $ 8 as the lowest ever recorded in 1991-94. During this period, 1991 - 1994, FDI accounted for less than 1% in gross fixed capital formation as it did in the period 1996 - 1998. Investors complained of high taxation and delays in profit and divided repatriation, which had fallen three years in arrears and excessive government regulation (Kimuyu, 1999). During this period, corruption increased and infrastructure deteriorated – making the cost of operating many other countries in Africa as a recipient of FDI but with high levels of FDI (95%) concentrated in manufacturing and services (Wignaraja and Ikiara, 1999).

As an attempt to attract FDI, stimulate external trade and expand exports the government enacted policies towards investment and export promotion. Investment Promotion Council (IPC) was established with a mandate to attract FDI into the country. Export schemes which were introduced in the early 1990s included introduction of Export Processing Zones (EPZ) in 1990 with the

Table 6. Performance of export processing zones, Kenya, 1994 - 2002.

Years	'94	'96	'98	'00	'01	'02	'03	'04	'05
Gazetted Zones	11	14	16	19	23	31	37	41	43
Enterprises Operating	15	22	18	24	39	54	66	74	68
Employment Locals	1,865	2,884	3,645	6,487	13,444	26,447	38,199	37,723	38,051
Employment Expatriates	-	71	74	133	314	701	612	837	800
Total Employment		2,885	3,719	6,620	13,758	27,148	39,111	38,560	38,851
Exports Sales (KShs Mn)	507	1099	1,805	3,635	5,962	9,741	13,812	23,047	20,036
Domestic Sales (KShs Mn)	438	496	649	755	538	932	619	651	3,160
Total Sales (KShs Mn)	945	1,595	2,454	4,390	6,500	11,040	14,817	24,211	23,774
Foreign Imports (KShs Mn)	635	1,009	2,056	2,349	3,990	7,043	9,920	13,029	12,497
Local Purchases (KShs Mn)	192	292	511	1,229	718	1,127	1,176	1,893	2,388
Investment (KShs Mn)	2,097	4,370	5,747	6,107	8,950	12,728	16,716	17,012	18,682

Source: Obtained from Kenya, EPZ Authority and Central Bureau of Statistics; http://www.epzakenya.com/.

enactment of the export processing zones Act to promote export oriented industrial investment. Export Promotion Center (EPC) was established in 1992 to formulate market strategy, promote an export culture and to identify export opportunities regionally and internationally. Manufacturing under Bond (MUB) established in 1986 and administered by the investment promotion council (IPA) was strategised to exempt from duty and VAT those exporters who imported machinery and raw materials in manufactured goods for exports. Finally Export Programmes Office (EPPO) was established in 1992 as a kind of duty draw back scheme administered by the Treasury (Kimuyu, 1999: Glenday and Ndii, 2000). It is believed that this helped jump the Exports from (13%) of GDP in 1992 to over (20%) between the period 1993-96 (Glenday and Ndii, 2000). Nevertheless FDI has remained low in Kenya, albeit high in some selected sectors of the manufacturing industry.

FDI AND INDUSTRIAL CAPABILITY DEVELOPMENT: THE ROLE OF INSTITUTIONS ESTABLISHED DURING THE EXPORT ORIENTATION PERIOD

In the above section we have shown that due to the economic turbulences of 1980s, SAPs were adopted in Kenya by mid 1980s. All the liberal instruments adopted were outlined such as, liberalisation through decreased deregulation, openness to trade and foreign investment. As noted, this did not appear useful to the country as the economy was plunged into deepened crises until 1993 when the government undertook further reforms to revert the crises trend. The reforms included establishment of a number of institutions for promoting exports, FDI, technology transfer, linkage formation, capability building and performance in manufacturing. This section examines the specific role played by institutions during this period focusing on FDI, spillovers, industrial capability and performance.

Export processing zones: The Export Processing Zones (EPZ) program was established through an Act of parliament, in 1990 for the promotion of export industrial investment in the country. An assessment based on available data, Table 6, indicated growth in performance. For instance, the number of gazetted zones had risen from 11 in 1994 to 43 in by 2005 with the number of operating companies increasing from 15 to 68 in the same period. Total turn over for the EPZ companies expanded from Kshs 945 million in 1994 to Kshs 11.0 billion in 2002 and 23.8 billion in 2005 (Table 6). The impetus behind the high growth in performance especially after 2000 came as a result of the enactment of African Growth Opportunity Act (AGOA). As a share of total sales, exports increased from 53.7% in 1994 to 82.8% in 2000 and to 84.3% in 2005. High export performance has been attributed to the opening up of the United States market to textiles and garments under AGOA and also preferential access to the common market for Eastern and Southern Africa (COMESA), as well as European Union markets. Employment in the EPZ rose to 38.1 thousand in 2005 from 1.9 thousand in 1994 depicting an average annual growth rate of 50.9% in the entire period, 1994 - 2005. There was also evidence of deepening linkage system between EPZ and the rest of the economy. Between 2000 and 2005 local purchases increased by more than double from Kshs 1.2 billion to 2.4 billion. Domestic sales also increased by several folds from Kshs 438 million in 1994 to Kshs 3.1 billion to 2005, Table 6.

Despite this performance, some critiques had it that EPZ programme has not lived to its expectations particularly in the area of employment generation and stimulation of industrial growth and development in the country (Chabari, 1999). Another critique was that the EPZ programme had failed to steer the country's industrialisation process (Mireri, 2000). As an example, EPZ had not generated strong linkages both in manufacturing and in the agricultural sector as anticipated which implied less spillover benefits through such linkages. With regard to training, it has been argued that skills employed in those industries are not really sophisticated especially in the textile firms; can be acquired easily by personnel without a university degree. Graduates working in some of these firms were faced with the possibility of de-skilling and low remunerations. Interviews with officers from EPZ indicated that the Kenyan export processing zone follows the traditional assembly-for-export-only pattern. Also, EPZ had failed to single out specific industry groups for specialisation. Additionally, facilities in the zones remained poorly maintained or not promoted to prospective investors' expectations.

Investment promotion authority: The Investment Promotion Authority (IPA) was established in Kenya as a statutory body in 1986 through an Act of parliament to promote private investment in Kenya. The investment centre works closely with all government ministries to facilitate acquisition of relevant approvals, license and permits: IPA encourages investments that are: labour intensive; utilises locally available raw materials; stimulate foreign exchange earning or saving and promote efficient transfer of technology. Although there are no legal requirements in equity ownership levels, IPA highly encourages MNCs to form JVs with locally owned firms. To facilitate this, IPA maintains a database of locally owned firms interested in forming JVs with foreign firms. These firms would then be matched to the incoming foreign investors who are interested in operating JVs with locally owned firms. IPC is supposed to facilitate acquisition of all the required approvals and licences from government ministries.

Nonetheless, in its operations IPA is faced with multiple problems. One of the major constraints is that although IPA is supposed to work closely with government ministry, it does not seem to have much influence. This is explained by the fact that modalities of how to do that have not been laid down properly. IPA lacked the capacity to do that. Staff employed is little against many ministries and their departments and given the normal government salary; their motivation/morale is equally not boosted. In a few cases, they have not received the co-operation they expected from the ministries and have not been able to play its facilitation role of one stop shop effectively. This means that the bureaucracies which are supposed to be eliminated by making IPA one stop shop were still far from being eliminated.

From the interviews conducted with several officers from IPA, it was observed that the centre lacks the necessary capacity to undertake an analysis of incoming investors strategies so that this can be matched with strategies of locally owned firms. In comparison to countries in the East Asia the match making process remains largely unexploited in Kenya. It was also noted that IPA failed to effectively market the country internationally. An explanation to this is that the funding from the government has not been adequate for IPA whose budgets are planned in annual cycles. With adequate funding, IPA in collaboration with Kenyan embassies abroad is supposed to market the country investment opportunities, which would perhaps change the countries tarnished image over corruption and bad governance witnessed during Moi's regime. This would perhaps attract more MNCs targeted especially in areas where Kenya would benefit technological spillovers alongside employment. Another aspect, which ought to be strengthened, is the personnel training as most of them seemed misplaced in the sense that they held totally different qualifications from those required in investment. Staff training ought to become continuous in-house, locally and even in abroad for exposure especially to other countries investment promotion centers. However, according to interviews done significant developments have been undertaken whose achievements will be assessed in the near future. IPA has prepared Kenya's investment code expected to govern and guide all investments in the country.

Export promotion council: The Export Promotion Council (EPC) was established in 1992 to co-ordinate and harmonise export development and promotion activities in Kenya. Working in collaboration with both private and public sectors, EPC identifies new export markets, disseminates export-related information, reviews the country's export performance on a regular basis and advises government on new policy initiatives designed to boost exports.

It was however noted during the interviews that funding from treasury was not enough. Human capital was inadequate and there was urgent need to employ more professionals and to train them continuously extending the training to abroad for exposure. The amount voted for EPC was just enough for staff remunerations and personal emoluments, leaving very little for the actual business of export promotion. Since EPC had come up with a strategic plan covering the period 2004 - 2007 with an aim to improve the council's efficiency in trade promotion and the services it offers to importers, it was interesting to see if the government would increase its EPC's proposed budget. The council also intends to expand its departments to further its role and to offer a support service. The strategic plan proposes the development of export development fund to finance trade development and product diversification. Nevertheless the council hoped to generate funds by providing trade information services through its Centre for Business in Kenya.

Kenya industrial property institute: Kenya Industrial Property Institute (KIPI) was established through an 'Industrial Property Act' in 2001 to administer industrial property rights; provide technological information to the public; promote inventiveness and innovativeness; and provide training on industrial property. However, from the interviews conducted KIPI appeared not to have the expected technical skills to play the role expected of a functional intellectual property office under the new WTO. It is faced with a general shortage of qualified staff: This implies that the institution is not able to meet these training and advisory functions adequately. The fact that KIPI undertakes the advisory role to its clients as well as examining patent applicants means that, it ends up doing too much. There is perhaps a need to separate the two roles or have them placed in different institutions. It comes out clearly that due to low levels of innovation undertaken in the Kenyan industry; KIPI's role in technology promotion is relatively small. Lack of legal skills in intellectual property rights needs to be addressed.

Brief summary of emerging issues based on the role of institutions examined

The analysis has shown that FDI inflows declined making Kenya lie behind most countries in Africa although maintaining relatively high levels of FDI stock in manufacturing. Within the period of SAPs the government policies to promote exports and stimulate FDI resulted in the creation of institutions such as: Investment Promotion Authority to attract FDI, Export Processing Zones to promote export oriented industrial investment and KIPI to administer industrial property rights. As noted, most of these institutions have had a substantial performance. Nevertheless their performance was not as expected due to a multitude of problems ranging from lack of adequate financial support, lack of required skills, physical capital sometimes poor governance and weak co-ordination.

In sum, we note that the period of export promotion under SAPs was characterised by poor and intermittent implementation of liberalisation measures with minimal support and sometimes withdrawal of government support by World Bank and IMF. There was severe institutional failure due to minimal and sometimes lack of support from the government; there was macro-economic instability; widening internal and external imbalances. All these factors worked to reduce the inflow of FDI, industrial capability development and thus general industrial performance in the period.

RECENT PERFORMANCE AND EFFORT TOWARDS INDUSTRIALISATION

On recent economic performance, the economy was still in turmoil and was faced with a multitude of problems ranging from interrupted trade liberalisation process by the onset of stabilisation crises in 1997 - following the collapse of an IMF programme. This resulted in macro-economic instability characterised by low domestic savings. Comparatively, high interest rates, inadequate and high-terrified electricity supply elevated the cost of production. This was compounded by increased transaction costs due to deteriorating institutions, poor infrastructure mainly roads and railway lines all of which undermined competitiveness of exports. These factors eroded the investment climate; there was a decline in investor confidence, leading to a sharp fall in FDI. The fact that SAPs were still being implemented a decade down the road, did not seem to bare meaningful fruits (Kenya Economic Survey; Phillips and Obwana, 2000; Todaro 2000; Soderbom, 2001). In the period 1991 - 2000, the economy recorded the lowest and worst economic growth level since the country's independence with GDP growth rate averaging 1.5 and 2.5% in 1991 - 1994 and 1995 - 2000 respectively. Manufacturing declined from (2.2%) in the period 1991 - 1994 to (1.8%) in the period 1995 - 2000.

In the midst of all these problems the government launched new effort towards industrialisation with an object-tive to transform Kenyan economy into a newly industrialised country by the year 2020. In the wake of multiparty system in Kenya, a new political dispensation emerged in 2002 and which purports the industrialisation process by entrenching the same industrialisation objective. Two main strategies are being considered: Firstly, to consider industry as the leading sector in economic development and second, to earmark specific industries for government support. The proposed Industrialisation strategy outlines some of the measures to be implemented, to industrialise over a two-stage period. In the first phase, the government will selectively encourage labour-intensive, resource-based and light manufacturing industries, where the country enjoys comparative advantage. In the second phase, policy will target intermediate and capital goods industries that are more technology and capital intensive but that must await the removal of infrastructure, technology, and human capital and savings constraints. The policy framework for industrialisation, therefore seeks to provide incentives, improve technological capabilities and provide an appropriate institutional framework that will ensure an industrialisation process led by the private sector (Kenya government, 1997; Ronge and Nyangito, 2000). FDI was expected to play an important role through increased capital investment, technology transfer through formation of linkages in manufacturing industry.

The effort to industrialize the country by 2020 would be pursued alongside industrial policies articulated in the Kenyan Vision 2030. This is the most recent thinking on Kenya's industrial policy. Kenyan Vision 2030 is an economic development plan aimed at accelerating the rate of economic growth. If the vision is realized, Kenya will become a newly industrialized, middle income country by 2030. The vision is skillfully designed taking lessons from developed and advanced developing countries that have their economies highly industrialized. The role of the manufacturing sector in Kenya vision 2030 is to contribute to the social economic development of the country by creating jobs, generating wealth, and encouraging both local and FDI.

Some of the activities to be articulated in these visions pertaining to the industry include: Creation of Special Economic Zones (SEZ). This would include construction of modern, world-class cities with commercial, industrial and residential facilities similar to those of the newly industrialized countries. The anticipated benefits of SEZ include stimulated investment which would result in job creation.

Summary, Conclusion and Policy Recommendation

This paper examined broadly the role of FDI in Kenya's industrialisation process focusing on technological spill-overs, capability development and productivity performance. Also, the paper examined the institutions established with a focus to discern their role on FDI promotion and support for industrialisation.

Since commencement of manufacturing, Kenya pursued two modes of industrialisation starting with import substitution followed by export orientation. Import Substitution was adopted in 1945 when the first major drive towards industrialisation took place in Kenya. This mode of industrialisation was continued until mid 1980s when it was gradually phased out and replaced with export orientation dawning the era of structural adjustments programme in Kenya.

The analysis undertaken revealed that industrialisation was initiated before independence and was dominated by European MNCs. Kenya enjoyed an early colonial manufacturing experience in capital investment from foreign investment particularly British firms as they were the majority. These benefits can be interpreted as spillovers into the manufacturing industry. The country also enjoyed most of the revenue earning primary sectors developed during colonial days as well as infrastructure such as railway line, roads and port facilities.

Under I-S industrialisation, the country was characterised by rapid economic growth with most economic activities witnessing high levels of growth. The institutions established seemed relatively sound and functional. There was increased consumer demand for consumer goods in the domestic market. At the same time external demand for raw materials in Europe was also escalating. The two developments resulted in increased FDI inflow into manufacturing industry particularly in the agro-based industries. From the analysis done, we can contend that in addition to FDI's high capital investment in manufacturing, contribution in exports, value added, employment and revenue generation to the economy, the country benefited manufacturing experience in the form of spillovers.

The analysis showed that economic crises of 1970 - 1980s which were largely blamed on inward looking policies pursued under import substitution resulted in a steady decline in manufacturing growth, value added and exports. It was becoming increasingly difficult to effectively participate and compete in export markets. To change this trend, the I-S policy was dropped in favour of an outward oriented industrial policy in order to re-orient industrial production in favour of exports under liberalisation in aegis of SAPs. New institutions were established to support this porcess. As a result, the country recorded a slight recovery in the economic performance but lasted for only a short time. There was lack of commitment to the reforms being undertaken, hence in 1993, far-reaching structural reforms were undertaken to reverse the declining trend but again without much success.

A further decline in most economic activities, including FDI activities, was noted. For instance, there was a decline in most of the sectoral growths. A few factors were touted for that including world economic recession, multiparty politics which led to political unrest, withdrawal of foreign aids and high oil prices during the Gulf war. The political unrest resulted in anxiety and uncertainties of foreign aid, which in turn had negative ramifications on the inflow of FDI, which could be rated as only modest at the time. Nevertheless, FDI stock in manufacturing remained high and continued to generate highest levels in employment, revenue generation, value added, export performance etc.

In short, E-O under SAPs was characterised by first, economic stagnation due to weak infrastructure, lack of sound institutions and coordination among them, weak technological capabilities, macro-economic imbalances etc. Second, the poor economic performance alongside poor inconsistent policies translated into low levels of domestic investment as well as FDI in the country. The consequence of this was that spillovers which would have occurred, had FDI activities been vibrant, would certainly reduce. Consequently, the capability development process equally slows down. Nonetheless, based on the analysis conducted, we conclude that FDI played a substantial role in the industrial development. Although occurrence of spillovers requires empirical confirmation, the qualitative evidence garnered supports FDI spillover occurrence in the Kenyan manufacturing industry. Also, despite severe constraints, institutions had some important role in promoting FDI vis-à-vis the industrialisation process.

It should however be emphasized that with the new political dispension since 2002 there are signs of recovery although it is still early to make sound conclusion on the basis of FDI process, industrial capability and performace. The positive signs of recovery are as a result of policies enacted. Such initiatives are articulated in the industrialization plan to industrialize by 2020 and in vision 2030. Both of these spell out clearly the specific issues that need to be addressed to industrialise the country. For instance, under EPZ it was recommended that be replaced with special economic zones. Accordingly, Kenya is adopting special economic zones. The country is also deepening the industrial reform process.

This paper has several implications for policy. First is that a sound industrial policy is necessary for economic growth and development. Such a policy should encompass FDI policies (promotion and entrechment) targeted at sectors where MNC presence would be advantageous to the country's industrialisation effort. The government should continue providing support to the institutions particularly to enhace their capacity such as co-ordination, finance and human capital. This would strengthen their intermediary role in supporting industrialisation. Linkage promotion should be done in earnest, possibly, through establishment of an institution with a clear mandate to enchance linkage formation with deepened content. Similary, competation should be regulated in such a way that it spurs learning, capability development and innovation. Partnership among academia, public institutions and business associations should be enhanced focusing on increasing interactions geered at stimulating learning and innovation. R&D should also be encouraged through stimulation of science, technology and innovation culture. Such would ensure that firms maintain clear path-dependence towards capability development that would be followed by industrial development and economic growth.

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