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## A scoping study on China-Africa economic relations: The case of Kenya

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# A Scoping Study on China- Africa Economic Relations: The Case of Kenya

Revised Final Report

By

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## 1.0 Introduction

There is a lack of disaggregated and detailed data that could be of some help for the analysis of the nature and contribution of China's Trade, FDI and Aid in Africa. In order to illuminate these concerns, this study was designed to analyse the extent of China's Trade, FDI and Aid in Kenya. The specific objectives of this study are to determine the size;

- a) Composition and significance of Kenya's exports to China and the SITC classification of exports, as well as the identification of key stakeholders and classification of such stakeholders into gainer or loser groups.
- b) Composition and significance of imports of Kenya from China and the SITC classification of such stakeholders into gainer or loser groups.
- c) Composition and significance of Chinese investment in Kenya and the ISIC classification of recipient sectors, as well as identification of key stakeholders and classification of such stakeholders into gainer or loser groups.
- d) Features (types, purpose, conditions including the extent to which the aid is tied and purpose) and the significance of Chinese aid to Kenya and the ISIC classification of the recipient sectors, as well as the identification of key stakeholders and classification of such stakeholders into gainer or loser groups.

The general approach to this study entailed investigating the extent to which existing data in Kenya support the thesis that the China-Kenya relations (Trade, FDI, and Aid) has expanded in recent years, resulting in losers and gainers. The primary sources of data included interviews and published information i.e. from International Sources, Government Printers, Kenya National Bureau of Statistics, Ministry of Trade and Industry, Investment Promotion Centre, Kenya Revenue Authority - Customs. The interviews targeted Chinese Embassy/Mission, Kenya Association of Manufacturers (KAM) Ministry of Planning and National Development, Ministry of Trade and Industry and other government departments (Export Promotion Centre, Investment Promotion Centre, Kenya Revenue Authority-Customs Department).

## 2.0 A Review of Cooperation Arrangements between China and Kenya

The current diplomatic cooperation arrangement between Kenya and China covers several areas. The People's Republic of China established the diplomatic relations with the Republic of Kenya on the day of December 14, 1963. In the initial days of the establishment the relations between the two countries it saw a fair development. After 1965, the relation of the two countries was lowered to be at the chargé d'affaires level and towards the beginning of 1970s it gradually returned to the normal. In 1978, when President Daniel Arap Moi came in power, the relation of the two countries gained a fast development. With frequent mutual visits at high level the friendly cooperation witnessed outstanding achievements in many fields. By the end of 2002 when a new government was formed after Mwai Kibaki was elected President of the country he expressed to hold a great account of the relations with China, willing to further deepen and expand the friendly cooperation between the two countries.

Kenya and China trade diplomatic relations have significant historical dimensions, starting with the Ming Dynasty<sup>1</sup>. Although China embraced communism and Kenya at independence adopted a capitalist system, their relations have largely remained cordial. China was the fourth country to recognise Kenya's independence in 1963 when the two countries exchanged diplomatic representations<sup>2</sup> (Kamau, 2007). The Chinese embassy in Kenya is arguably their largest embassy in Africa both in terms of size and employees (*interview a Chinese embassy official in Nairobi*). It is strategically located in a relatively high-security area near the Defence Headquarters, Kenya Army Barracks, and closer to the Kenya's State House. Similarly, Kenya has an embassy in Beijing which serves China and a few countries in the neighbourhood. Kenya, like other countries with diplomatic relations with China, subscribes to the 'One China Policy' which states that "*there is only one China in the world and*

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<sup>1</sup> A story is told of how through royal orders, Zheng commanded seven expeditions to the western oceans in the early 15<sup>th</sup> Century. Navigating by a compass and astronomical readings, Zheng's fleet visited many African islands in the Eastern Africa region, including Lamu and Mombasa now in Kenya and that some sailors may have settled on the Kenyan coast after a shipwreck (*Business in Africa*, 2006).

<sup>2</sup> The first country to recognise Kenya's independence was Germany (then West Germany), then Russia, Ethiopia and then China. This order of recognition is still reflected in the diplomatic number given to the embassies of these countries which are 1-CD, 2-CD, 3-CD, and 4-CD respectively.

*that Chinese Taipei is one part (a Province) of China*". This means that Kenya does not support Chinese Taipei's calls for independence and reiterates that it is an inalienable part of Chinese territory. The Sino-Kenya relationship, first established in 1964 was centred on promoting trade between the two countries. The trade component of this relation was further reinforced in 1978, when under the leadership of Deng Xiaoping, China started implementing trade reforms and outward oriented programmes. Since the China-Africa Forum was established in 2000, Kenya has remained an active member of the forum. Different Ministers have represented the Kenyan government in all the Ministerial Conferences of the China-Africa Forum.

The exchange of official visits at the high levels of head of states, ministers, senior government officials and business delegations has strengthened relations between China and Kenya. Kenya's first high profile delegation to China was in 1964 led by the then Vice-President Jaramogi Oginga Odinga. In 1980, the then Kenyan President Daniel arap Moi led another high profile delegation to China, followed by others in 1988 and 1994. In August 2005, President Mwai Kibaki led a Kenyan delegation to China which resulted in the signing of several bilateral agreements. In May 1996, the former President of China Jiang Zemin made a state visit to Kenya, which marked the first ever visit to Africa by a Chinese President. In November 2004, Wu Bangguo paid a visit to Kenya heading a Chinese delegation. In April 2006, the Chinese President, Hu Jintao visited Kenya in his tour of five African countries as the head of state. In the past five years, over fifteen Kenyan ministers have visited China since 2002. Similarly, many other government officials have also made official trips to China (Kenya, 2006).

The entry of people of Chinese origin in Kenya is fairly recent and their population is still low. It is only in the last decade or so that the presence of a Chinese community in Kenya became noticeable. The small number of Chinese people and their separation from the rest of the people has, however, contributed to the Chinese community being less visible. Even those Chinese people engaged in the clothing industry avoid dealing directly with the local people. They tactfully employ local human resource managers and accountants to handle local matters. Anecdotally, it is currently estimated that there are approximately 8,000 Chinese people living in Kenya (Kamau, 2007). However, there are no official statistics. The

people of Chinese origin living in Nairobi have settled in the neighbourhood of the Chinese embassy. Similarly, most of the Chinese companies with operations in Kenya have their national head office closer to the Chinese embassy and arguably closer to the other Chinese people.

Most of the Chinese people in Kenya are engaged in trading and manufacturing activities. They are involved in the importation of various products from China which they either distribute to retailers or through outlets they have opened to sell their products to the public. Since the year 2000, they have been actively involved in the manufacturing of apparel. More recently, a number of them have ventured into the motor vehicle industry whereby they are involved in the importation of auto-spare parts from Asian countries.

Since the establishment of the diplomatic relations between China and Kenya, leaders of importance who visited China from Kenya include: Daniel Arap Moi, President of Kenya (September 1980, October 1988 and May 1994), David Okiki Amayo, President of the Kenya African National Union (September 1986), Wilson Ndolo Ayah, Minister of foreign affairs (August 1991), Bonaya Godana, Minister of foreign affairs (April 1999), Francis Ole Kaparo, Speaker of the Kenyan National Assembly (April 2000), and in October 2000 B. Godana, the Kenyan Foreign Minister headed a delegation to attend the "Beijing Ministerial Meeting 2000 of the Sino-African Cooperation Forum". Over 15 Kenyan Ministers have visited China since 2002 including the Minister for Finance, Minister for Communication, Minister for Roads and Public Works, Minister for Tourism, Minister for Foreign Affairs, Ministry of Cooperatives and Marketing Development.

Chinese leaders and officials who visited Kenya mainly include: Ji Pengfei, Vice-premier of the State Council (August 1980), Zhao Ziyang, Premier of the State Council (January 1983), Tian Jiyun, Vice-premier (November 1985), Gu Mu, member of the State Council (April 1987), Wu Xueqian, member of the State Council and concurrently minister of foreign affairs (May 1987), Sun Qimeng, Vice-chairman of the NPC (November 1991), Qian Qichen, Vice-premier and concurrently foreign minister (January 1991 in the name of foreign minister, January 1994), Chen Muhua, Vice-chairwoman of the NPC (April 1992), Jiang Zemin, President of the PRC (May 1996), Qian Zhengying, Vice-chairperson of the

NPPCC (June 1997), Tang Jiaxuan, Minister of Foreign Affairs (January 1999), Peng Peiyun, Vice-chairwoman of the NPC and chairwoman of All China Women's Federation (November 1999), Li Peng, Chairman of the NPC (November, 1999), Dai Bingguo, Minister of the International Liaison Department of the CPC Central Committee (April 2000), Wang Zhongyu, Member and Secretary-general of the State Council (May 2000), Li Tieying, member of the political bureau of the CPC Central Committee (2001) and Zhu Rongji, Premier of the State Council (April 2002). In April 28, 2006, Chinese President Hu Jintao held talks with his Kenyan counterpart Mwai Kibaki in Nairobi. Both sides expressed willingness to jointly commit to developing bilateral friendly cooperative relations of long-term stability and mutual benefits and continue to deepen friendly cooperation in all areas (Kenya, 2006).

Bilateral relations have been developing smoothly with the traditional friendship continuously deepened and friendly cooperation in all areas increasingly expanded. Bilateral economic and trade relations have scored new progress and both sides have made rapid headway in cooperation in the areas of electric power, communications, investment and project contract, achieved new results in humanities exchanges and maintained close consultations and cooperation in international affairs. The bilateral economy and trade agreements signed between China and Kenya include: "Agreement on Economic and Technological Cooperation between the People's Republic of China and the Republic of Kenya", "Agreement on Trade between the People's Republic of China and the Republic of Kenya" (1978) and the agreement on promotion and protection of investments in 2001. The two countries have signed a total of 12 bilateral accords over the past three years which have covered a variety of fields including the economy, technology, energy, tourism, health, aviation, the press, archaeology and education (Kenya, 2006).

In 2006, Kenya and China signed six agreements signaling closer economic and technical cooperation between the two countries during a meeting held at the Great Hall of the People in Beijing between President Kibaki and his host President Hu Jintao. The signed agreements included Economic and Technical Cooperation, agreement on the provision of the concessional loan by China to Kenya and the Air Services Agreement which grants Kenya Airways landing rights in several cities in China. Also signed were agreements on



Radio Cooperation between the State Administration of Radio, Film and Television of China and the Ministry of Information and Communications of Kenya and a collaborative agreement between General Administration of Quality Supervision Inspection and Quarantine of China and Kenya's Bureau of Standards. Appendix A provides a detailed account of the agreements signed.

In view of the above developments, Kenya Airways has begun operating scheduled flights to China. The Guangzhou City route was introduced due to the increased popularity of China as a business destination. The airline flies to Guangzhou three days a week (The China Monitor, November, 2005: p.17).

#### *Economic cooperation*

Kenya and China signed a Trade Agreement in 1964 and revised it in 1978. The Ministry of Trade has begun consultations to review this agreement to take in changes in the international economic arena and the phenomenal growth of the Chinese economy. To actively implement already-signed bilateral cooperation agreements, China encourages its businesses to import Kenyan goods, expand investment in Kenya, participate in its infrastructure construction and energy & resources exploitation and expand cooperation with Kenya in processing industries and agriculture. China will continue offering economic aid within its available resources and strengthen assistance for Kenya's human resources development.

The government of the People's Republic of China has set up a special fund to encourage Chinese companies to import some Kenyan products, including coffee beans, rose seeds, black tea and sisal all of which are exported in raw form. Efforts being made at bridging bi-lateral trade should focus on value addition before export. The Third Economic and Trade Committee meeting between Kenya and China took place on 25<sup>th</sup> April 2006. The meeting addressed various issues of interest to both countries, including ways of bridging the balance of trade, which remains heavily in favour of China (Kenya, 2006).

### *Cultural cooperation*

In order to expand cooperation in the fields of culture, education, health, tourism, journalism, environmental protection and sport and further build up mutual understanding and friendship between both peoples, a number of initiatives are on-going:

- In order to stimulate Chinese investment in the tourism sector as well as resulting in direct flight connections between China and Kenya (and a number of African destinations), Kenya and other individual African countries have been granted “Approved Destination Status”. Chinese tourism abroad is strongly regulated. The popular tourist destinations of Egypt and South Africa were the first countries to be granted such status. Following FOCAC’s Addis Ababa Action Plan, China gave an additional eight countries (Ethiopia, Kenya, Tanzania, Zambia, Mauritius, Seychelles, Zimbabwe and Tunisia) such status.
- China and Kenya signed a memorandum for setting up the website "Kenya-China Economic and Trade Cooperation" in June 2006.
- The two sides agreed that China will import more coffee from Kenya and at the same time offered Kenya the most advanced coffee processing equipment.
- China’s influence is not limited to raw materials. Kenyan universities are developing Chinese language programmes (University of Nairobi), Technical Scientific Cooperation (Egerton University), while Ministry of Information officials attend exchange schemes.

### *Motivation for Cooperation*

China views Kenya as a gateway to the region and it has become a key focus of China’s trade and economic strategy in Africa. Being a war-free country with stable political situation has made Kenya an ideal regional base for Chinese investors to expand their business in Africa. Currently China offers favorable loans to Kenya, builds hospitals and schools for less-developed areas, sets up malaria prevention and control centers as well as sends volunteers to train the locals.

### *Gains and Losses*

The Kenya Airways has been granted landing rights in several cities in China and is now operating direct flights to Hong Kong (China) and Guangzhou in southern China from Nairobi. Furthermore, since Kenya was granted Preferred Tourist Destination in 2004, arrivals from China have more than doubled and are expected to grow even more (Kaplinsky R. et al, 2007). These initiatives are likely to boost the Kenyan economy by enhancing not just the earnings of the Airlines but also earnings for the tourism sector which has become a leading foreign exchange earner for Kenya. Moreover, these operations are likely to facilitate the movement of Chinese business persons to Kenya, leading to increased foreign direct investment in Kenya from China.

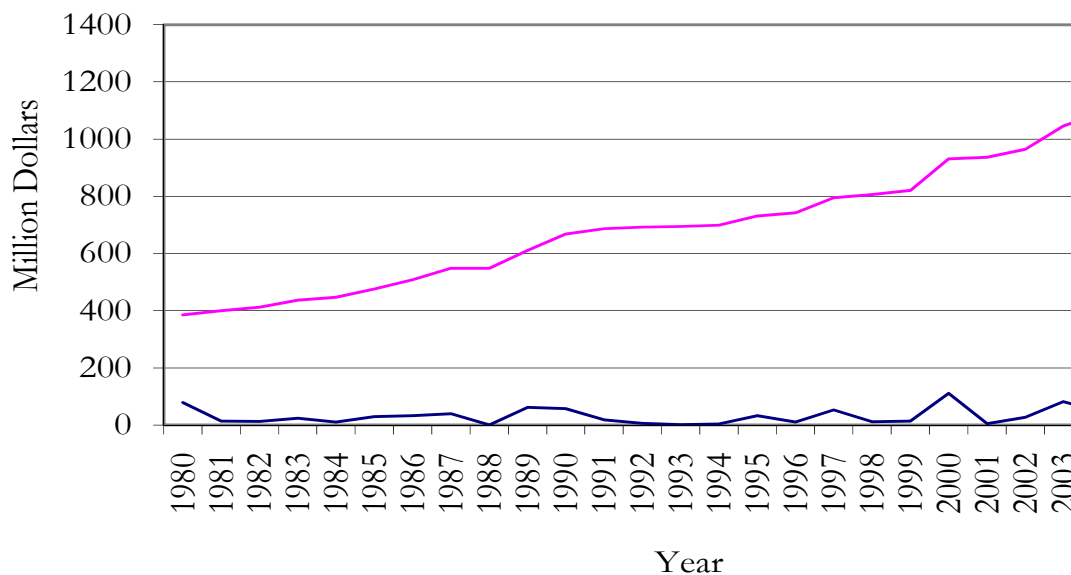
### **3.0 China-Kenya Investments**

Foreign direct investment (FDI) in Kenya is defined as investment in foreign assets, such as foreign currency, credits, rights, benefits or property, undertaken by a foreign national for the purpose of production of goods and services, which are to be sold either in the domestic market or exported overseas (Investment Promotion Center Act, Chapter 518). The Central Bank of Kenya keeps records of FDI transactions.

Kenya like most of other African countries has recently liberalised the investment environment. Until 1995, all foreign investments flowing into the country were subject to approval by the Central bank. The Investment Promotion Act of 2004 clearly spells out the government commitment to attracting FDI in Kenya. This was necessitated by the realisation that FDI in Kenya was declining during the last decade, while it rose in other countries in the region (Kenya, 2006). In addition, increased competition among African countries in the global FDI also necessitated Kenya to address the domestic impediments to foreign investments. According to the Investment Act of 2004, foreign ownership is only restricted for insurance industry, telecommunication industry, and companies listed on the Nairobi Stock Exchange, to seventy-seven, seventy and seventy-five per cent, respectively.

Kenya's FDI flows and stocks are shown in figure 1. These stocks have been increasing gradually over the years. However, the FDI inflows have been subject of fluctuations particularly in the last decade (see Figure 1). Analysis over the last decade to 2001 shows that Kenya has lost its competitiveness in attracting investment. Kenya has also lost in terms of retaining the stock of investment. The loss in Kenya's investment competitiveness is the result of many inter-connected factors such as negative perception by investors about political instability, poor governance, corruption, inadequate infrastructure, insecurity, crime, theft, and policy instability. Private investment which was growing at an average of 10% between 1985 and 1989, only grew by 0.4% between 1997 and 2001 (Central Bank of Kenya, 2006).

Figure 1: FDI Inflows and Stocks in Kenya, 1980-2006



### Foreign Direct Investment by China

Chinese investment projects in Kenya currently number about 96 with a workforce of about 6,700 Kenyans and an investment capital of 52.6 million US dollars. Based on data from Kenya Investment Authority (KIA), the value of FDI from China between 2000 and 2005 is presented in Table 1. Between 2000 and 2005, total FDI was US\$446 million, of which, US\$ 32 million originated from China, representing 7.2 per cent. China had a total of fifty-seven projects during the period. Using this information, we compute the average size of Chinese projects in Kenya. Although this measure is crude given the incompleteness of data, on average, an FDI project from China is US\$ 0.56 million.

Table 1: FDI from China in Kenya 2000-2006

Year	Total FDI US\$ Mn	China		
		No. of Projects	Capital US\$ Mn	Employment
2000	110.9	9	4.08	787
2001	5.3	12	2.79	1313

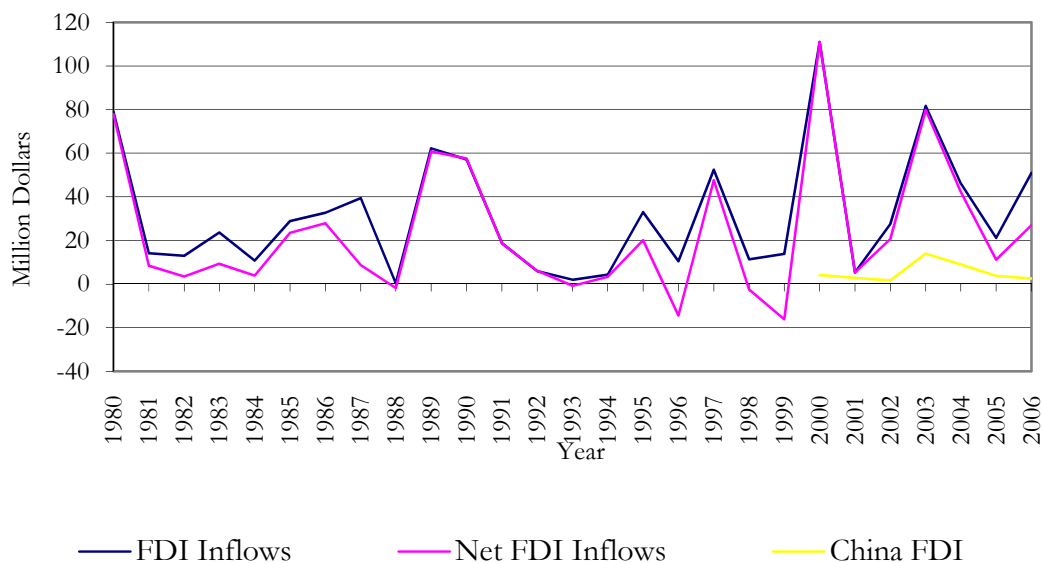
<b>2002</b>	27.6	6	1.67	170
<b>2003</b>	81.7	11	13.95	493
<b>2004</b>	46.1	12	9.03	1414
<b>2005</b>	21.2	12	3.74	239
<b>2006</b>	51	8	2.51	681

Source: Own Calculations based on the Investment Promotion Centre, and Kenya Investment Authority Data Sets

Most FDI from China is by companies that in China are either wholly or partially state-owned even though in Kenya they operate as private companies.

Until the year 2000, the FDI from China remained very low. The flows from China became remarkable in the last three years (see Figure 2).

Figure 2: Kenya: FDI Flows, China FDI, 1980-2006



#### *The size, composition and significance of Chinese investment and the recipient sectors*

In this section, we examine the size and composition of Chinese investments in Kenya between the year 2000-2006. In the year 2000 most of the investments established were in manufacturing (90%) and services (10%) (see Table 2a). The capital costs was entirely foreign, ranging from US\$ 46,000-95,000. Most of the capital was invested in manufacturing. Employment in these firms was mainly local, constituting 96%, while foreign employment

was only 4%. The average employee per firm was 87 i.e. average for local employees was 83 while that on foreign employees was 4 persons.

*Table 2a: Chinese Direct Investments in 2000*

CO_NAME	ACTIVITY	CAPCO STF US\$ (000)	CAPCO STL US\$ (000)	EMP F	EMP L
Victory River Company Ltd	Import & export of goods	462	0	3	18
Crown Sea Enterprises Ltd	Shoe production	923	0	1	55
Kenya Fulu Industrial Ltd	Importation of T.V, solar panels	231	0	4	45
Neo Smart suppliers Co Ltd	Manufacturing of PU shoes	246	0	4	470
Penguin Grain & Oil Processing Machinery	Import & selling milling machinery	231	0	4	70
Hgy International Co. Limited	Import & Export of chinese goods	246	0	6	14
Chinese Huangpai Grain Processing Equi..	Processing maize, wheat and rice oil	924	0	6	22
Tisco Kenya Ltd	Bicycle plant	769	0	3	50
Sun Yu Enterprises Ltd	Diesel/petrol ext.from plastic waste	52	0	4	8
CAPCOSTF=capital cost (foreign); CAPCOSTL=capital cost (local); EMPF=employment (foreign); EMPL=employment (local)					
<i>Source: Investment Promotion Centre (IPC), Kenya Investment Authority (KIA) Data sets</i>					

In the year 2001 and 2002, there were 17 Chinese investments started in Kenya. Again most of these were in manufacturing and services. Most of the capital was invested in services. The average employment in these firms was 82 persons, i.e. average for local was 78 and foreign 4 persons per firm (this translates to 95% local and 5% foreign). The capital costs was both local (30%) and foreign (70%), averaging US\$ 66,000, local US\$ 20,000 and foreign US\$ 46,000.

*Table 2b: Chinese Direct Investments in 2001 and 2002*

CO_NAME	ACTIVITY	CAPCO STF US\$ (000)	CAPCO STL US\$ (000)	EMP F	EMP L
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East Hegeyoy Trade Co	Import & export of Chinese goods	216	0	3	15
Dong Fang Dev. Ltd	Import & export of goods	177	0	2	7
China Victory King Stone Material Co.	Making ballast	106	0	6	32
Thai Star Restaurant Ltd	Chinese Restaurant	62	0	2	11
Tabasa food Company	Making sausages	47	0	1	64
Newland Industries Ltd	Manufacture of candles from wax	708	0	2	800
Chinese Centre for Promotion of Trade	Trade and investment Promotion	216	240		22
Newland Industries ltd	Manufacturing of Candles	708		2	2
Laibao (K) import&Exports Dev. Ltd	Spare parts VCO& Radio Assembly	83	0	3	45
An- Ning Holding Ltd	Production/Distr. Of Textile	246	0	4	168
Famonar pharmaceuticals	Manufacture of intravenous Fluids	924	0	5	24
Famonar Ltd	Manufacture of Cigaretes	216	113	14	73
*China- Flying Dragon (K) Ltd	Import of Chinese Furniture	177	0	8	2
Chang Sheng International Ltd	Growing & Exporting Mushrooms	246	0	7	11
Nantong Yuanxt Co Ltd	Import and export Business	246	0	6	11
Double Leopard enterprises	Manu. OF Motor cycles	853	0	6	90
Peng & Huo Medical Company	Chinese clinic	20	0	3	6
Youngstar International Ltd	Manufacturing of Mosquito nets	126	0	0	20
CAPCOSTF=capital cost (foreign); CAPCOSTL=capital cost (local); EMPF=employment (foreign); EMPL=employment (local)					
<i>Source: Investment Promotion Centre (IPC), Kenya Investment Authority (KIA) Data sets</i>					

In the year 2003, 11 Chinese firms were started, fully owned by the Chinese, mostly in services sub-sector i.e. 82 % of the firms while the rest were in manufacturing (see Table 2c). Capital investments in these firms were entirely foreign, averaging US\$ 1.3 million per firm. Most of the capital was invested in services sector. Employment in the firms averaged 45 persons, with local employment averaging 37 (82%), while foreign averaging 8 (18%) persons per firm.

*Table 2c: Chinese Direct Investments in 2003*



CO_NAME	ACTIVITY	CAPCO STF US\$ (000)	CAPCO STL US\$ (000)	EMP F	EMP L
China Farm Products	Importing& Process of farm products	154	0	3	27
Henan Company (K) Ltd	Export of Coffee	154	0	0	16
For You Chinese Restaurant	Restaurant	170	0	0	14
Baus Optical Co Ltd	Manufacturing of optical lenses	413	0	0	100
China San Yuan( Kenya) Ltd	Processing of Farm Products	154	0	6	25
China Agricultural Technology Co	Imports	154	0	5	32
Horizon Ivato Supermarket Ltd	Supermarket (Wholesale and Retail)	11,154	0	0	50
Phoenipaper Ltd	Production of Paper products	62	0	3	43
Changhong Electronics (E.A) Ltd	Assembly& Production of electronic goods	1,231	0	70	46
Super Beauty Parlour ltd	Beauty Parlour	154	0	0	21
Tianchi Health Products	Multi- Level Marketing of food prod	154	0	0	32

CAPCOSTF=capital cost (foreign); CAPCOSTL=capital cost (local); EMPF=employment (foreign); EMPL=employment (local)
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<i>Source: Investment Promotion Centre (IPC), Kenya Investment Authority (KIA) Data sets</i>
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### *Chinese Direct Investments in 2004*

By 2004 there were about 60 Chinese companies such as Jiangsu International Economic and Technological Cooperation Co., Sichuan International Economic and Technological Cooperation Co. Ltd. and China Road Bridge Construction (Group) Corporation and China Import and Export (Group) Corporation for Complete Sets of Equipment and so on doing their businesses in Kenya.

In 2004 at least 12 firms established their activities in Kenya. These were mainly in the manufacturing and services sector as shown in Table 2d below. Most of the capital was invested in services sector. The firms established were mainly fully owned by the Chinese with capital costs averaging US\$ 775,000 per firm. Employment was mainly local (97%), averaging 114 per firm and foreign (3%), averaging 4 persons per firm.

*Table 2d: China's Foreign Direct Investment to Kenya in 2004*

ISIC	CO_NAME	ACTIVITY	CAPC OSTF US\$ (000)	CAPC OSTL US\$ (000)	EMP F	EMP L
AGRI	Beinparts Ltd	Coffee growing	7,539	0	0	180
MANU	Aucma Technology Ltd	Digital Manufacture of Tvs,Dvd,Vcd	31	0	4	12
MANU	Kenya Manufacturing industry	Xianghui & assembling of motor car batteries	310	0	4	24
MANU	Crystal Bull Kenya Ltd	Glass Manufacture	462	0	3	90
MANU	Future Industry & Trade Corporation Ltd	Manufacture of glass and Alluminium	170	0	5	15
MANU	Aucma Technology Ltd	Digital Manufacture of Tvs,Dvd,Vcd	31	0	4	12
MANU	Kenya Manufacturing industry	Xianghui & assembling of motor car batteries	310	0	4	24
MANU	Wu yi Kenya Company Ltd	Civil Structural engineering contracts	65	0	10	1020
SERV	Stuttafords International Fashion Co Ltd	Clothing retail	124	0	3	5
SERV	Geo-Net Communications Ltd	Telecommunications	0	0	0	6
SERV	Go Africa travel Limited	Travelling Promotions	108	0	3	5
SERV	China King Restaurant	Chinese Restaurant	154	0	4	77
CAPCOSTF=capital cost (foreign); CAPCOSTL=capital cost (local); EMPF=employment (foreign); EMPL=employment (local)						
<i>Source: Investment Promotion Centre (IPC), Kenya Investment Authority (KIA) Data sets</i>						

### *Chinese Direct Investments in 2005*

In 2005, 12 Chinese firms commenced their operations in Kenya. These were distributed in manufacturing (58%) and services (42%) (see Table 2e). Most of the capital was invested in services sector. The capital costs averaged US\$336,000 but were mainly foreign (93%). Employment averaged 20 persons per firm, dominated by locals (86%).

*Table 2e: Chinese foreign direct investment in Kenya 2005*

ISIC	CO_NAME	ACTIVITY	CAP COST F US\$ (000)	CAPCOSTL US\$ (000)	EMP F	EMP L
MANU	Kenya AA Electric Crane Company	Manufacture of electric machines and construction	524	0	3	10

MANU	Newstar Ltd	Manufacture of mattresses	54	0	1	4
MANU	Blue Wave Group of Companies Ltd	Manufacture of fruit juice, water & milk processing	570	0	3	14
MANU	Focus Motorcycle Manufacturing Co Ltd	Manufacture of Motorcycle	62	293	0	19
MANU	Kenplastics Limited	Recycling to protect environment	77	0	3	5
MANU	Lulu Development Co. Ltd	Textile manufacturing	208	0	0	13
MANU	Afri-China International Co Ltd	Recycling Plastics	570	0	4	59
SERV	Mabokoni Ostrich Investment Ltd	Rearing breeding ostrich	77	0	3	5
SERV	Health Action International Africa	Charitable org	62	0	3	17
SERV	Transafrika Motors Limited	Motor vehicle assembly	570	0	4	59
SERV	Global Entrepreneurs Africa Ltd	International export	616	0	3	33
SERV	Xin Yuna Construction Investment Ltd	Import & export of all kinds of granite	284	0	3	10
SERV	Greatland Pharmaceutical Ltd	Pharmaceutical and Surgical Wholesaler	62	0	3	17
CAPCOSTF=capital cost (foreign); CAPCOSTL=capital cost (local); EMPF=employment (foreign); EMPL=employment (local)						
<i>Source: Investment Promotion Centre (IPC), Kenya Investment Authority (KIA) Data sets</i>						

A Chinese company called Dong Song opened East Africa's first concrete pole factory, for 3 million dollars. It represents the biggest single investment by a Chinese company in Kenya. Most of the firms were in the manufacturing and services sub-sectors as seen in Table 2c. At least two of the firms established in 2005 were joint ventures between Kenyan and Chinese firms.

#### *Chinese Direct Investments in 2006*

Eight (8) Chinese firms were established in Kenya in 2006, again mostly in the services (63%) and manufacturing (37%) sub-sectors. Most of the capital was invested in services sector. The average capital investment was US\$ 636,000, most of the capital going into services investment. Employment averaged 85 persons per firm for locals and 8 persons per

firm for foreigners.

Table 2f: China's Foreign direct investment to Kenya 2006

ISIC	CO_NAME	ACTIVITY	CAP COST F US\$ (000)	CAPCOS TL US\$ (000)	EMP F	EMP L
MANU	Hua Long Auto Repairs Co Ltd	Manufacture of motor vehicles bodies	385	0	9	23
MANU	Hua Long Auto Repairs Co.Ltd	manufacture of motor vehicle bodies	385	0	9	23
MANU	Gold Lida Ltd	Manufacture of PVC products	154	0	9	90
MANU	Dong Fang Auto Assembly Co. Ltd	Manufacture & Assembly of motor vehicle bodies	385	0	9	23
SERV	Zenith Rubber Roller (E.A) Ltd	Re- rubberizing of rubber rollers	131	0	1	6
SERV	Afri-China International Co Ltd	Recycling Plastics	222	0	8	50
SERV	Fasr Track Kenya Ltd	Air transport agencies	519	0	2	10
SERV	Datang Optical Company	Glazing and assembling of spectacles	333	0	2	327
SERV	Ando Roofing Products (k) Ltd	Importing & selling of roofing tiles & paints	954	0	3	56
SERV	Proparco Ltd	E.Africa Grain handling	554	0	10	57
CAPCOSTF=capital cost (foreign); CAPCOSTL=capital cost (local); EMPF=employment (foreign); EMPL=employment (local)						
<i>Source: Investment Promotion Centre (IPC), Kenya Investment Authority (KIA) Data sets</i>						

Besides the above activities in 2006:

- An offshore exploration deal was signed between Kenya Government and China, allowing CNOOC to explore in six blocks covering 44 500 sq miles in the north and south of the country. Kenya gave six key oil blocks to Chinese companies (CNOOC) to the detriment of potential European competitors. Companies such as Cepsa of Spain and Swedish Lundin International lodged complaints on this perceived favouritism.
- Chinese drug firm, one of China's largest pharmaceutical companies, Beijing Holley-

Cotec Pharmaceuticals, opened a drug distribution centre and an East Africa Logistics Centre, in Nairobi to serve the East and Central African region. The company's top managers committed themselves to distribute anti-malarial drugs in the African continent. The company has been in the African market since 1993 with offices in Tanzania, Nigeria and Uganda. The centre distributes anti-malarial medicine to the private and public sectors at less than current market prices.

#### *Chinese Direct Investments in 2007*

In 2007, China's Jinchuan gave \$9.34m to Canadian Tiomin's Titanium project Canadian mining company. Tiomin Resources Incorporation signed a Memorandum of Understanding with Chinese mining company Jinchuan Group, China's largest producer of nickel, cobalt and platinum with an output of nickel and platinum of 88% and 90% respectively, of the total Chinese production. The joint venture of the two companies aims to finance and expedite the development of the Kwale mineral sands project in Kenya.

#### *Overview of ownership structure, size, and distribution of Chinese investment*

In Kenya Chinese are in the manufacturing and service sector. Recently they are moving to mining and minerals exploration. Chinese companies operating in Kenya are not based on joint venture. The firms established so far are most fully owned by the Chinese companies. The companies are mostly privately owned by Chinese companies that are dominant in Kenya. There is very limited joint ownership or local capital. Furthermore, the employment level in such firms is very low for both Kenya and China. Even though the initial interest of Chinese investors was in manufacturing, there is a rapid shift in the later years towards services sub-sector. Most of the capital investment also appears to be placed in the services sub-sector. Increasingly also, the structure of employment is gradually changing, with an increasing proportion of Chinese employees.

#### ***The Importance of China's Foreign Direct Investment in Kenya***

The FDI inflows from China have become important in recent years. This position can be explained by two factors (see Figure 3 on FDI flows):

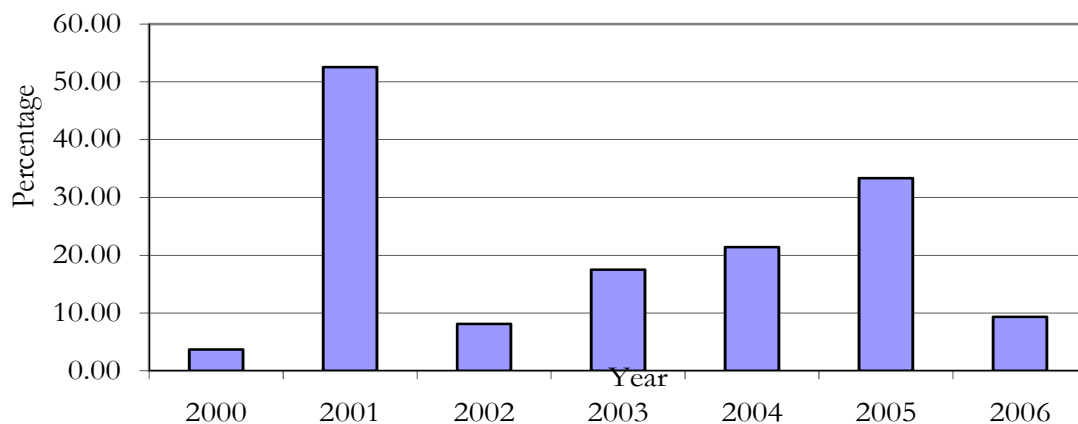
1. The loss in Kenya's competitiveness to attract direct foreign investment has meant

that any FDI flows from China have constituted an important proportion of the Net FDI flows in Kenya.

2. China has adopted a new policy to Kenya, aimed at closer ties in economic cooperation. There is therefore increased presence of Chinese enterprises.

But the importance of China's FDI flows to Kenya is much more in terms of capital investment rather than the quality of activities. This is because of the firms established have tended to engage in services such as trade with very few firms participating in manufacturing. The FDI flows from China have assumed significant proportions even though they remain low i.e. ranging from US\$ 1-3 million in the last 6 years.

*Figure 3: China's FDI as % of Net FDI flows in Kenya, 2000-2006*



### *Major beneficiaries and losers arising from Chinese investment in the relevant sectors*

#### *a) Spillover Effects*

The Chinese FDI inflow in Kenya compared to neighboring countries may be largely determined not only by macropolitical and macroeconomic factors, but by the quality of the underlying domestic business climate and institutional conditions, both within Kenya and on a regional level. In addition, and equally important from the perspective of furthering economic development and growth within Kenya, the linkages between FDI and trade

among Chinese firms involved in Kenya create the possibility for positive “spillovers” in Kenya through the attraction of investment of infrastructure and related services development and through the transfer of advances in technology and managerial skills, which are often the intangible assets that accompany FDI (Broadman, 2007:292).

*b) Diversification in FDI*

Greater diversification in FDI has been occurring increasingly falling into several investment sectors. Significant Chinese investments in Kenya have been made in retail ventures, tourism, transport, construction, power plants, and telecommunications, among others. To cite and example, Huawei, a major Chinese telecommunications firm, has won a huge contract to provide cell phone service in Kenya. Thus China is pursuing commercial strategies with Kenya that are about more than resources.

*c) Possibility of New Trade Patters*

In light of the significant heterogeneity among Chinese FDI firms in Kenya, one would expect to observe significant differences in the emerging trade patterns between Kenya and regional states and the rest of the world. In particular, the increased presence in the services such as imports, exports, might suggest that China’s motive is to use Kenya as an entry point as a trading platform in the region.

*c) Participation in International Trade*

Worldwide, the presence of foreign firms usually has a profound effect on a host country’s participation in international trade, because FDI is often associated with an increase in both exports and imports (Broadman, 2007:324). An important potential by-product of this process in China-Kenya relations is that Kenyan firms might become exposed to transfer of advances in technology or enhanced skills. Such exposure could engender positive spillover effects on the efficiency and competitiveness of Kenyan firms.

*d) Technology transfer*

On technology transfer, most of the Kenyan EPZ firms recruited people without experience in the garment industry who were then trained within the factory (Fukunishi *et al.*, 2006). In this case, the EPZ firms do not compete directly with the local firms. Equally, some former EPZ employees leave formal employment to start their own small-scale garment firms using the training and experience they got while working in the EPZ garment firm. More importantly, some production expatriate workers left EPZ firms to team up with local investors to establish garment factories.

There are some locally-owned (non-EPZ) firms specialised in high value activities such as embroidery, sand-blasting, stone-washing and printing, and that they get regular subcontracts from EPZ firms. In this way local firms are able to participate in the global apparel value chain indirectly. Local garment firms are increasingly purchasing machinery from EPZ firms either when the EPZ firms upgrade their machinery inventory or at times when they close down. The cheap and appropriate capital goods has resulted in local firms using relatively modern technology in their production activities (Kamau, 2007).

In Kenya, there appears to be the growth of small-scale entrepreneurial investment from China, often presaged by the construction of specialised shopping malls retailing Chinese goods. Prospects of technology transfer are real, but along with these emerging trends, here is displacement of existing and potential local producers; less spin-off to local economy than other foreign contractors; while increased Chinese FDI could lead to disinvestment and relocation by other foreign investors (for example, clothing and furniture) (Kaplisnky et al, 2007).

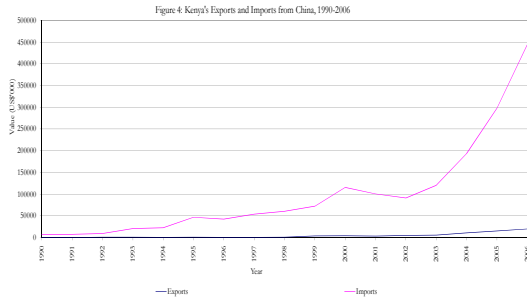
#### *e) Labour Conditions*

China labour conditions have generated intense interest among international policymakers, labour movement activists, and development agencies (Winters Alan and Shahid Yusuf (ed.), 2007). The extent to which such labour conditions could be imported into Kenya through FDI is a cause for concern, especially in the EPZs where already protests have been encountered due to poor working conditions.



#### 4.0 Trade between China and Kenya

The volume and value of Kenya's exports has been growing with time. This trend is evident from Figure 4 below. The rate of export growth has particularly been very high in the last three years.



Analysis of trade between Kenya and China shows a growing deficit in favour of China. Total trade between the two countries grew more rapidly during the period 1995-2004, than during the period 1979-1994 (Figure 4). Nonetheless, the growth of trade between during the period 1995-2004 is associated with an increased deficit (Figure 5): imports indeed grew at a higher rate than the exports over the period.

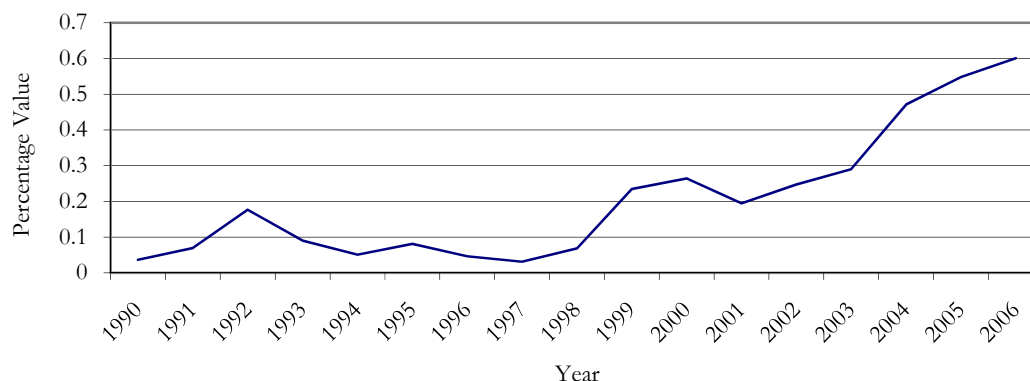
As a proportion of Kenya's total exports, China accounted for 0.43 per cent on average between 1979 and 1994; while it accounted for 1.42 per cent of total imports during the same period. During the period 1995-2004, exports to China as a proportion of total exports

on average increased to 0.63 per cent, while imports as proportion of total imports doubled to 2.85 per cent (Figure 5).

#### *Size, Composition and Significance of Kenyan Exports to China*

Kenya is ranked third among the 24 southern and eastern African countries that trade with China. Trade between Kenya and China has been steadily rising since the two countries established diplomatic ties in 1963. In 2000, the volume of bilateral trade hit a record of over 136 million dollars, compared with about 26 million dollars in 1991. From January to May 2001, the trade volume between the two countries reached over 55 million dollars, up 23 percent compared to the same period in 2000 with Kenyan exports to China jumping nearly 47 percent. The volume of bilateral trade between the two countries reached 475 million dollars in 2005, an increase of nearly 30 per cent over the previous year, and Kenyan exports rose four percent to 17.6 million dollars. The bilateral trade volume between China and Kenya in 2006 reached US\$650 million , up by 36.1% , among which China's export to Kenya was US\$620 million , up by 36.0% , while China's import from Kenya was US\$20 million , up by 38.3%. China's trade surplus with Kenya stood at US\$600 million. Growth in Kenya's export to China is well illustrated in Figure 2 below. This growth was more rapid in the last three years. As a percentage of Kenya's total export value, the exports to China are still very low, below 1 percent. Growth in the value of Kenya's export to China has been gradual but the rapid been growth has been encountered in the last three years as evident in Figure 2 below.

Figure 5: Kenya's Exports to China as % of Total Exports



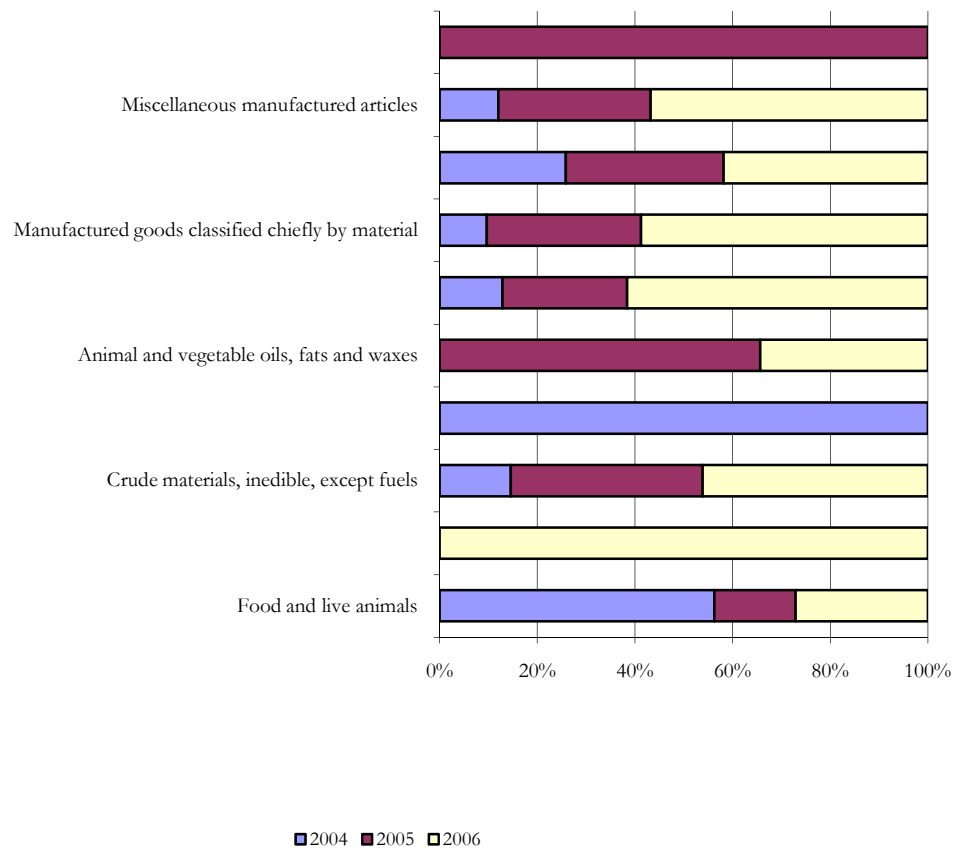
A summary of the exports by value in the last three years is provided in Table 4 below. The highest export values are in article 2-crude materials, inedible (69%), followed by article 6-manufactured goods classified chiefly by material (15%). The other important export is 0-food and live animals which constitute 14 percent of the export value to China.

Table 4: Computation of China's % share of Exports by Commodity Groups (2004-2006)

ARTICLE	SHORT DESCRIPTION	VALUE (US\$) 2004	% of Total	VALUE (US\$) 2005	% of Total	VALUE (US\$) 2006	% of Total
0	Food and live animals	6,887,593	53.53	2,036,354	11.13	3,306,550	13.82
1	Beverages and tobacco		0.00	0	0.00	149	0.00
2	Crude materials, inedible, except fuels	5,190,404	40.34	13,994,223	76.46	16,441,102	68.74
3	Mineral fuels, lubricants and related materials	24,125	0.19	0	0.00	0	0.00
4	Animal and vegetable oils, fats and waxes		0.00	15,743	0.09	8,220	0.03
5	Chemicals and related products	68,901	0.54	136,597	0.75	329,496	1.38
6	Manufactured goods classified chiefly by material	585,612	4.55	1,914,161	10.46	3,553,685	14.86
7	Machinery and transport equipment	79,635	0.62	99,475	0.54	128,618	0.54
8	Miscellaneous manufactured articles	31,711	0.25	82,442	0.45	150,027	0.63
9	Commodities and transactions not classified elsewhere in the s.i.t.c.		0.00	24,285	0.13	0	0.00
	<b>TOTAL EXPORTS</b>	<b>12,867,982</b>		<b>18,303,280</b>		<b>23,917,847</b>	

Changes in the patterns of exports to China by value are analysed in Figure 6 below. Exports in crude materials, inedible, and exports in manufactured goods classified chiefly by material have grown steadily in the last three years. The value of exports in Food and live animals has nevertheless been shrinking. The other export that has also declined is that of mineral fuels which was exported in 2004 and not in the subsequent years. Exports of Beverage and Tobacco have emerged in the last one year.

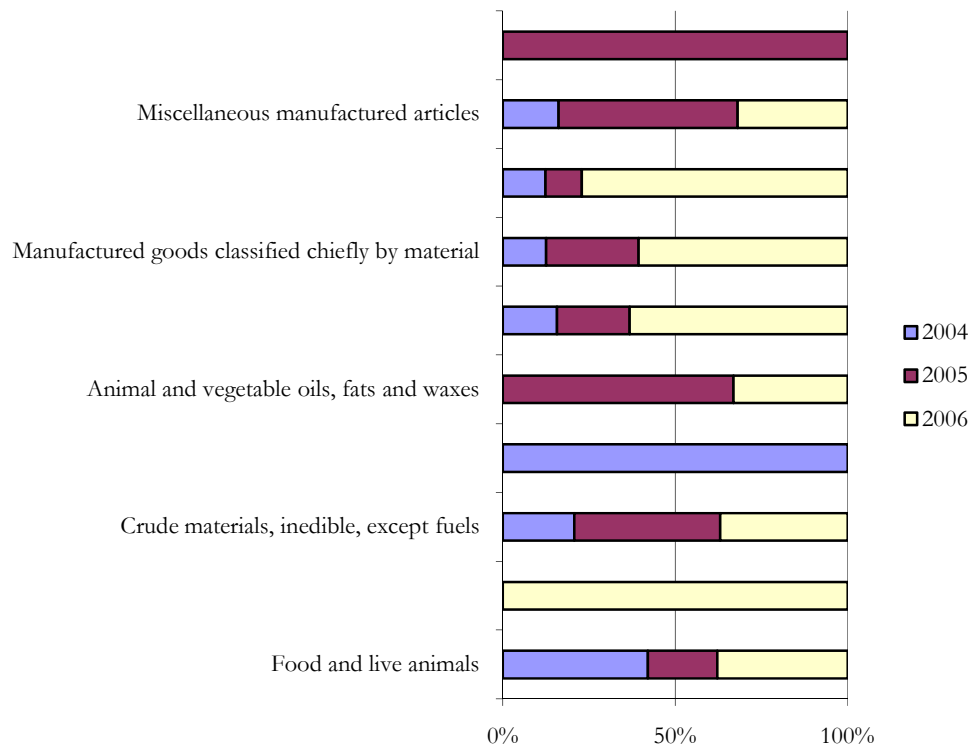
Figure 6: The Value of Kenya's Exports to China, 2004-06



In terms of export quantities, Figure 7 below suggest that the quantities exported has maintained their proportions as the values, suggesting that there has not been any major shift in the prices of goods exported to China in the last three years.

The major exports to China are hides and skins, sisal, fibre, coffee, tea, fishery products, horticultural products and scrap metals. In comparison to other African countries, trade between Kenya and China is small (Broadman *et al.*, 2006). However, the recent entry of China into the oil exploration and titanium mining is a clear indication of the direction of China's trade interests<sup>3</sup>.

Figure 7: Quantities of Kenya's Exports to China, 2004/6

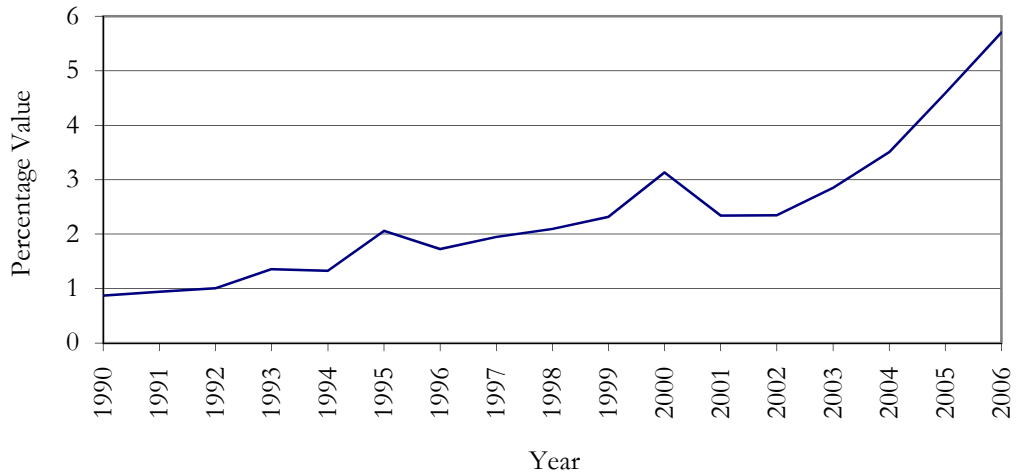


<sup>3</sup> In April 2006, during the state visit to Kenya by H.E. Hu Jintao, Kenya and China signed an “Oil and Gas Exploration Agreement” which gave China National Offshore Oil Corporation (CNOOC) rights to prospect for oil and gas in six offshore blocks in the Northern and Southern Kenya. Again on 28<sup>th</sup> April 2006, a Chinese company Jichuan Group Ltd bought about ten per cent of Tiomin’s common shares, injecting Kshs. 460 million into the capital of Tiomin, which is involved in the mining of Titanium in Coast Province – Kenya (*Daily Nation*, 28<sup>th</sup> April, 2006).

*Size, Composition and Significance of Kenyan Imports from China*

Trends in Kenya's import trade are given in Table 6. There has been a gradual growth in import value in the last three years. The value of imports from china has also risen sharply in the last three years. As a proportion of Kenya's total import value, the value of imports from China has risen sharply from about 2 percent in 2002 to nearly 6 percent in 2006 (see Figure 8).

*Figure 8: Kenya's Imports from China as % of Total Imports, 1990-2006*



Details of Kenya's imports from China are shown in Table 5 below.

*Table 5: KENYA'S IMPORTS FROM CHINA 2004-06, VALUES IN KSHS*

ARTICLE	SHORT DESCRIPTION	2004		2005		2006	
		VALUE (US\$)	% of Total	VALUE (US\$)	% of Total	VALUE (US\$)	% of Total
0	Food and live animals	6,946,625	3	4,843,586	2	3,440,786	1
1	Beverages and tobacco	177,481		370,303		40	
2	Crude materials, inedible, except fuels	1,129,130	1	1,338,276		1,799,632	
3	Mineral fuels, lubricants and related materials	1,134,536	1	23,737,922	8	1,798,928	
4	Animal and vegetable oils, fats and waxes	199,226		25,335		58,097	
5	Chemicals and related products, n.e.s.	25,063,446	13	34,254,279	12	45,161,264	10
6	Manufactured goods classified chiefly by material	51,197,790	26	87,671,224	29	160,275,765	35
7	Machinery and transport equipment	54,993,236	28	99,750,706	33	181,558,751	40
8	Miscellaneous manufactured articles	58,360,951	29	45,837,353	15	63,156,849	14
9	Commodities and transactions not classified elsewhere in the s.i.t.c.	3,984				60	
	<b>TOTAL IMPORTS</b>	199,206,405	100	297,828,983		457,250,173	

**SOURCE: CUSTOMS DEPARTMENT, KENYA REVENUE AUTHORITY**

The most important imports have been as follows:

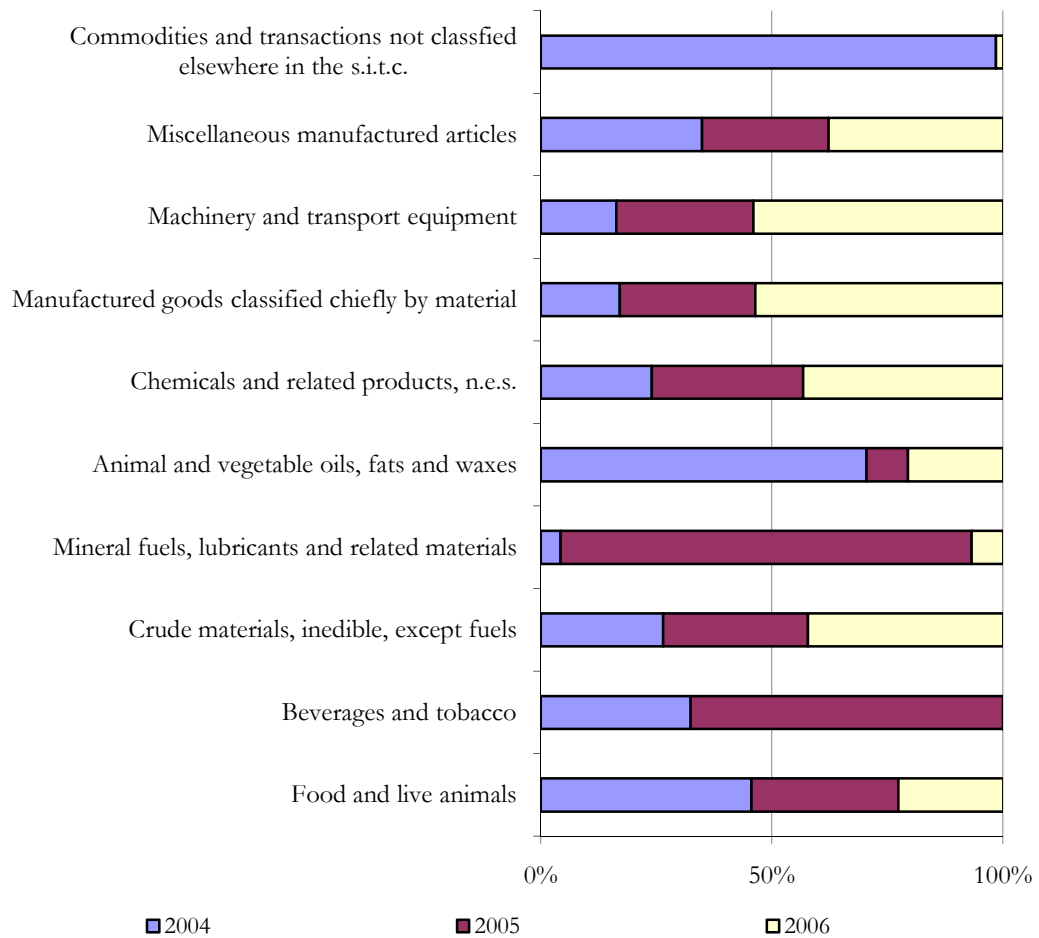
- Machinery and transport equipment constituting 40% of the value of Chinese imports.
- Manufactured goods classified chiefly by material – 35 %.
- Miscellaneous manufactured articles – 14%.
- Chemicals and related products – 10%.

In terms of quantities imported (Figure 9), there has been a gradual decline in the food and live animals (article 0) imported, and animal and vegetable oils (article 4). On the other hand, imports of manufactured goods (article 6), and machinery and transport equipment (article 7) have increased in the last three years.

For Kenya the main imports from China comprise machinery, equipments and parts for specialized industries to China. The imports comprise: medicine , footwear and

headwear , textiles and clothing , batteries , office supplies , household electric appliances, industrial and agricultural tools, textile goods, commodities for daily use, and building materials.

Figure 9: Kenya's Imports from China, 2004/6



China's export to Kenya may have declined for some goods due to pre-shipment inspection carried out by the Kenya Bureau of Standards. China lobbied for acceptance of product certificates issued by Chinese product testing agencies according to the principle of mutual recognition under the WTO Agreement on Technical Barrier to Trade.

***Beneficiary and Loser Groups in Trade***

*Import Gains*



China has been making inroads into African markets, including Kenya, and its influence has been growing year by year. Huge quantities of cheap Chinese products are available in Kenya. Attractive packaging and finishes are the hallmarks of these products.

#### *Import Losses*

The competition from growing Chinese imports in Kenya, due to lower production costs and better technology, has also hurt the textile and other manufacturing sectors. While Kenya's overall share in world regional trade is small, the share in output and employment in Kenya is significant. In recent years, there has been a contraction in the garment sector in Kenya. Chinese factories in Kenya, which had been set up to take advantage of easy African access to the U.S. market under AGOA, have departed overnight. Moreover, since most workers in the textile industry tend to be women, this has had negative implications for gender issues. There is a growing body of empirical evidence documenting job losses (Zafar A., 2007:p.20). According to Kaplinsky, et al (2007), displacement of existing and potential local producers by cheap Chinese products i.e. inputs for industries and cheap consumption goods is rapidly taking place.

#### *Exports Losses*

The Chinese have duplicated the local goods and are trading in them. They are edging locals out of business. Chinese items are made by machines, have a fine finish and are more attractive. Chinese traders are able to show a profit given that their products are sold cheaply. Chinese traders are doing better because they are better "networked". Their goods "are unique and cheap", they sell quickly because of their affordable prices. The goods are available at supermarkets at modest prices. The goods include kitchenware, wall clocks, watches, food containers, electricity-powered torches and shaving equipment. Unease seems to be rising as Chinese businesspeople become significant players and, in some cases, overtake Kenyan locals.

#### *Loss of Regional Trade*

In the East African regional market, the share of Kenya's export of clothing has declined in the recent past. UNECA (2005) estimates that Kenya's export of manufactured products in the region declined by twenty per cent between 1997 and 2003. Moreover, the Centre for Business Information in Kenya (CBIK) estimates that textiles and clothing exports to Uganda and Tanzania declined by fifty-five per cent between 2000 and 2005. Some of domestic firms which previously exported to Uganda and Tanzania had either reduced their sales while others had completely pulled out of these markets. They argued that this was due to imports of relatively cheaper products from China as well as the importation of second-hand clothes (Kamau, 2007). A major consequence of this decline in exports from the AGOA region was the impact on employment and overall economic activity (Kaplinsky et al, 2007).

## 5.0 China's Aid to Kenya

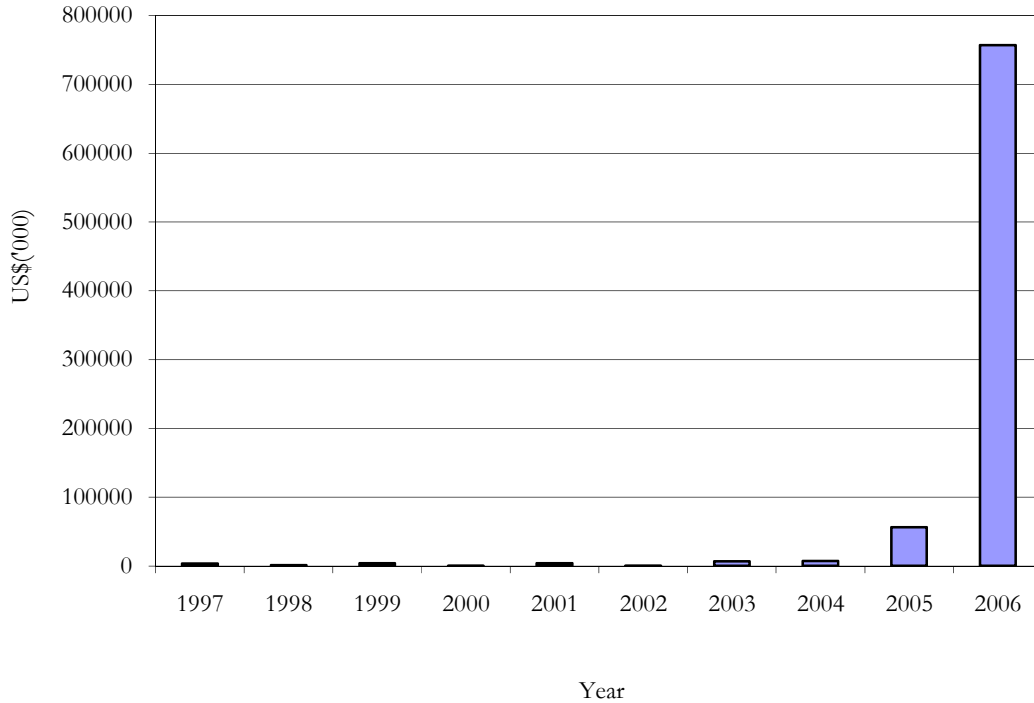
Foreign aid is a broad term describing the help one country gives another through some form of donation. The donors and recipients may be government or non-governmental bodies. Donations may go directly from the donor to the recipient, or they pass through other bodies. The purposes of aid differ, but are commonly grouped into three broad categories: relief, military, and development assistance (McCormick, D. et al, 2007:4). In this study, we track a particular type of aid, official development assistance from Chinese government to Kenya.

### *Size, features and the significance of China's Development Aid to Kenya*

Until the mid-1990s much of the Chinese development aid went towards liberation movements in Africa (McCormick, 2006). In fact, Kenya benefited from Chinese development aid in its early years of independence. In 1964, China provided Kenya with military support to counter a Somali invasion but it declined to provide monetary support for the independent government to purchase former colonial farms (*Daily Nation*, 2006). In the 1990s China changed its aid policy from liberation to reduction of debts, promotion of investment and assistance in human resource development.

Kenya is one of the beneficiaries of Chinese aid, but the sources of information do not indicate whether the companies are state owned corporations or private sector firms. China's assistance to Kenya is exclusively project based. Since the establishment of the diplomatic relations, the projects of aid and assistance provided by China to Kenya have been diverse. Projects are mostly part of bigger package deals which include other types of cooperation with Kenya. Aid disbursement trends are shown in Figure 7 below, indicating that until recently, the levels were quite low and stable.

Fig. 10: China's Aid Disbursements to Kenya, 1997-2006



*Based on data from Kenya Development Cooperation Report 2005; Ministry of Finance, Development Estimates 2005/2006; 2007/2008.*

China currently gives both monetary and non-monetary aid to Kenya. Development aid from China supports investment in infrastructure, equipment and plant; academic training; technical training; human relief; and tariff exemptions. Over the last five years China has given Kenya grants and loans for infrastructure, plant and equipment. These were mainly in road construction projects, modernisation of power distribution, rural electrification, water, renovation of international sports centre, medical and drugs for fighting malaria, and construction of a malaria research centre. China has for a long time awarded scholarships to Kenyan students wishing to undertake their studies in China in diverse fields. About 100 scholarships are given by the Chinese government to Kenyans each year, twenty of which are in medical related fields. On technical training, approximately 500 people from the public and private sectors benefit every year. More recently, China has been giving tariff

exemptions to various products originating from Kenya with a hope of promoting trade between the two countries (Kenya, 2006).

*Table 7: Main Types of Aid Given by China to Kenya 2003-2007*  
Amounts (US\$'000)

		2003	2004	2005	2006	2007
<b>Loans</b>	Gambogi Serem Road	3,100.00				
<b>Loans</b>	Kipsigak-Shamkhokho Road	3,000.00				
<b>Grants</b>	Kasarani Sports Ground Maintenance	39.00	3,620.00			43,846.15
<b>Grants</b>	Various Training Courses in China	300.00				
<b>Loans</b>	Purchase of Tractors	66.00				
<b>Grants</b>	Government Office Equipment		120.00			
<b>Grants</b>	Maize Flour Processing Project in Bomet and Drought hit Areas		3,330.00			1,766.00
<b>Grants</b>	Tsunami Relief Kenya			442.00		
<b>Grants</b>	Economic and Technical Cooperation Kenya			10,387.00		
<b>Loans</b>	Rural Telecommunications Development Programme Project			24,500.00		14,583.20
<b>Loans</b>	Kenya Power Distribution System Modernization and Strengthening Project			20,130.00		6,600.00
<b>Grants</b>	Rehabilitation of Nairobi Roads and Street Lighting Project					21,538.46
<b>Grants</b>	Technical Training courses to government officials			548.00		
	<b>Total</b>	<b>6,505.00</b>	<b>7,070.00</b>	<b>56,007.00</b>	<b>0.00</b>	<b>88,333.81</b>

*Sources: Kenya Development Cooperation Report 2005; Ministry of Finance, Development Estimates 2005/2006; 2007/2008.*

Examples of projects supported include (Kenya, 2006):

- China has extended to Kenya, loans and grants for a number of projects including; the Moi International Sports Complex project in Kasarani, supply of medical equipment and drugs, the upgrading of the Moi Referral Hospital in Eldoret, Concessional Loans for construction of various roads, including Kipsigak – Serem – Shamakhoho road, Kima/Emusustwi Road and the Gambogi-Serem road and a Maize Flour Processing Project in Bomet town.
- China grants various scholarships to Kenya every year in the scientific field. Two Chinese postgraduate students are admitted annually to our university. This year (2006), China awarded 20 additional scholarships.

- China has made considerable contribution to capacity building for short term courses in the last few years. Five hundred Kenyans are expected to benefit from these short term courses under the China-Africa Forum Framework Cooperation.

Loans and grants from China became significant in size beginning 2002. Since then, China appears in Kenya national statistics of bilateral donors whereas before then, it was classified in the category of 'Other donors'. As a ratio of total loans and grants in Kenya, China accounted for 1.67 per cent in 2002 and 9.98 per cent in 2005. With the exception of 2004, the grant component of China's loans and grants is relatively high. Kenya was the first African country to receive Chinese financing of educational and cultural exchange programmes through the Confucius Chinese and Language Centre, currently hosted by the University of Nairobi in Kenya and Tia Jin Normal University in China (*Xinhua*, 2005).

According to Kaplinsky R. et al (2007) Chinese aid to SSA can be grouped into six categories. The first is financial assistance for key investments. Linked to this, in recent years, has been a programme of limited debt-relief. The third form of aid provided has been a growing training programme. China's African Human Resources Development Fund has provided training in China. Fourth, China has provided technical assistance to SSA – more than 600 teachers and more than 15,000 Chinese doctors have worked in 52 SSA countries (including Kenya). Fifth, in an initiative announced at the second ministerial meeting of the Sino-African Cooperation Forum held at the end of 2003, China has instituted a programme of tariff exemption for 25 SSA economies, covering 190 products, including food, textiles, minerals and machinery. The policy took effect at the beginning of 2005 (*People's Daily*, 20 October 2005, [www.chinadaily.com.cn](http://www.chinadaily.com.cn), accessed 3 March 2006). These trade references are called for since Chinese tariffs on imports from SSA, although generally lower than Indian tariffs, were significantly higher than those in other Asian economies. We do not have data on the differential tariffs levied by China on imports from SSA compared to tariffs levied by individual SSA countries on imports from China. Finally, China has in very recent years begun to provide military assistance to Kenya.

*The Importance of China's Aid to Kenya*

Even though China's Aid to Kenya has increased substantially in recent years, it still constitutes a very small proportion of the aid received from bilateral, multilateral and the total aid received in Kenya. As shown in Figure 8 below, aid from China was negligible before the year 2005.

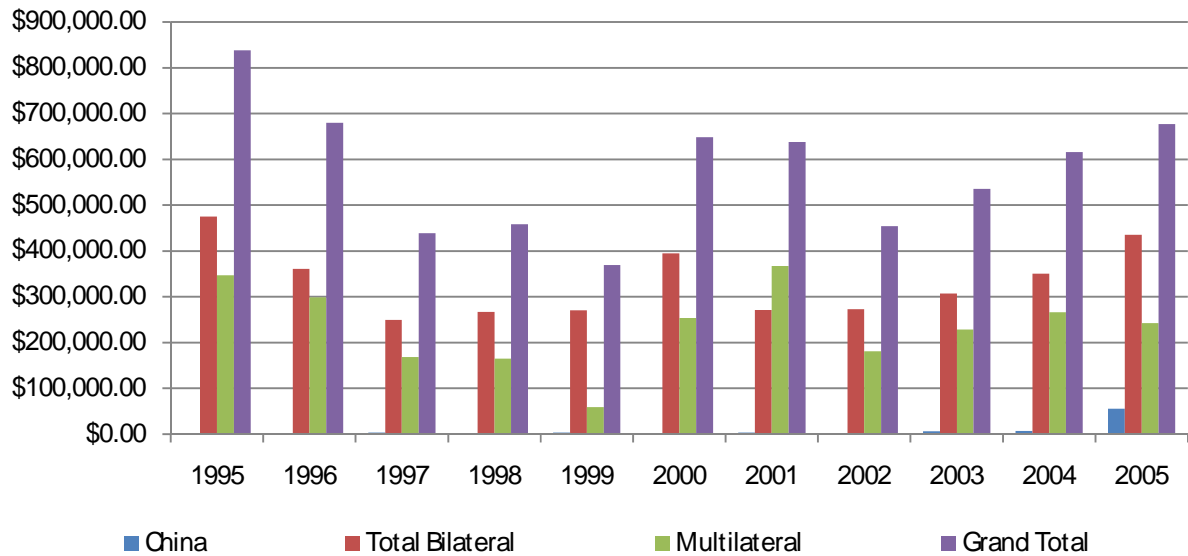
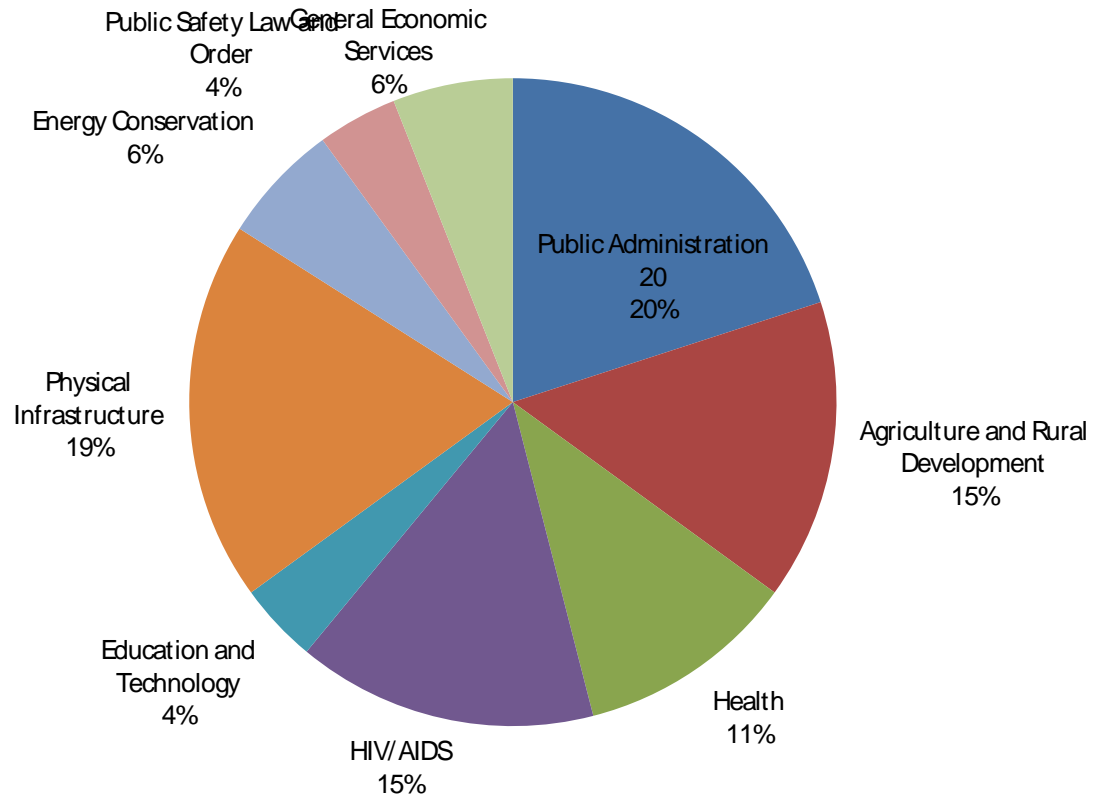


Figure 11: Aid Received from Various Sources in Kenya.

Figure 12: The Distribution of Development Assistance by Sector in Kenya



Source: UNDP, Kenya Development Cooperation Report, 2005.

As shown in Figure 12 above, a substantial proportion of the development assistance to Kenya goes to Public Administration (20%), Physical Infrastructure such as roads, water and sanitation (19%). This is followed by Agriculture and Rural Development (15%), HIV/AIDS (15%), and Health (11%). In the table below, we examine the importance of China's Aid to respective sectors. In Physical Infrastructure which covers road construction, the aid increased from about 8% in 2003 to 20% of the development assistance in the subsector. In General Economic services, China's aid increased from 0% in 2003 to 70% of the development assistance in the subsector. Overall, China's aid increased from 1.21% in 2003 to 8.25% of the total development assistance received in Kenya. These trends, shown in Table 8, suggest that Aid from China has become a very strong component of the foreign development assistance received in Kenya.

*Table 8: Development Assistance to Specific Sectors in Kenya  
Amount (US\$'000)*



Sector	2003				2004			2005		
	China		All Others	China		All Others	China		All Others	
	Amount	%	Amount	Amount	%	Amount	Amount	%	Amount	
<b>Physical Infrastructure</b>		8.31	74641		4.67	80064		19.57	125176	
Road Construction	6205			3740						
Information and Communication							24500			
<b>General Economic Services</b>		0.00	46786		6.60	50483		69.45	43941	
Hydro electric power generation							20130			
Social Legislation and Administration							10387			
Industry-Cottage and Medium Industry				3330						
<b>Education and Technology</b>		9.01	36250		0.00	63662		1.80	30412	
Technical and Managerial Education	300						548			
<b>Public Safety Law and Order</b>		0.00	47611		0.00	82610		1.45	30444	
Disaster Management							442			
<b>Total</b>	6505	1.21	536016	7070	3.59	196755	56007	8.25	678829	

Source: Compiled using data from UNDP, 2006.

#### *The main Institutions involved in Development Assistance*

Chinese development assistance processes are complicated with many actors involved. China has no development cooperation agency to coordinate the policies. *The State Council* is the highest executive organ as well as the highest organ of State administration, above the government ministries. *The Ministry of Commerce (MOFCOM)* is the main government body in charge of Chinese aid and coordinates aid policies with foremost the Ministry of Foreign Affairs, but also with other government ministries and bodies involved. *The Ministry of Foreign Affairs* has an advisory role on aid and economic cooperation and is in charge of diplomatic contacts and of coordinating concrete policies in the bilateral undertakings. *The Finance Ministry* is in charge of the budget as well as multi-lateral aid. *The Chinese Embassies* monitor the implementation of projects and report on their progress to the Chinese government. *The Export-Import Bank of China (China Exim Bank)* is in charge of Chinese government

concessional loans. There are also other government ministries involved in channeling aid and banks which play a role in the Chinese government's "going out strategy".

### *China's Aid Policy to Kenya*

Development aid from China in Kenya differs substantially from that originating from Western donors. First, with regard to 'terms and conditions' imposed, and secondly, on the aspect of 'tying'. China is not so much concerned about the issues of internal governance, human rights and democracy in Kenya like the Western donors<sup>4</sup>. Besides subscribing to the 'One China Policy', in the case of China, there is no any other conditionality imposed on the recipient country. China 'ties' its aid to using Chinese companies and procurement of materials in China, but nonetheless, most government officials believe that China is perhaps one of the most price-competitive sources whether its development aid is 'tied' or not. On scholarships and technical training, decisions are made by the relevant Ministry in Kenya. China does not take part in the donor coordination initiatives and instead prefers to operate independently (Kamau, 2006). China is considered much more flexible than the Western donors in accommodating domestic constraints. China does not alter its reporting and accounting procedures like the Western donors once aid has been disbursed.

According to China's African Policy, China will provide assistance "with no political strings attached". The one political condition China does have for the establishment of its relations with African countries is the one China principle, i.e. not to give formal recognition to Taiwan. However, China does give assistance to all 53 African countries, not just the 48 it has formal diplomatic ties with. Albeit China does not push for reforms in recipient countries, tied aid is a type of condition China has, as stated above (CHINAFRICA, 2007).

### *Beneficiary or Loser Groups*

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<sup>4</sup> By offering aid without preconditions, China has presented an attractive alternative to conditional Western aid, and gained valuable diplomatic support to defend its international interests (Tull, 2006).

The types of aid given to Kenya by China have obvious benefits in terms of infrastructural development and market development. The recipient sectors are set to gain, given the quality of China's development. However, if the underlying goal of China's aid is the drive to access raw materials and markets in Kenya, it will hurt Kenya's economy in the long run by undermining the ability of the local firms to exploit the same markets and resources. China's rapid expansion of Aid to Kenya, the lack of aid conditionalities, may lead to overshadowing of the aid from many traditional Western donors. There is a possibility that Chinese aid to Kenya could create productive capacity which competes with regional countries producers and lowers export prices.

The no political strings attached policy has raised much debate and reactions from external actors. Three general motivations for the principle are given by Chinese stakeholders (Embassy Attache, 2007): First, the non-interference policy is deeply rooted in China's historical experience of western interference and China is therefore careful not to interfere in African countries. Second, the Chinese government is careful not to interfere as it sees its political problems in Taiwan and Tibet as internal affairs. Third, the principle is based on China's own experience of being able to develop according to its national context without facing conditionalities.

The lack of political strings provides a risk that the Chinese policy will: 1) strengthen repressive regimes/elites that are not working in the interest of poor people or development at large 2) weaken social and environmental standards and not benefit poor people and the environment 3) weaken efforts to combat corruption and promote good governance in Kenya. Furthermore, according to Kaplinsky, R. et al (2007), the reality of aid conditionalities appears to be different as the aid appears to be very closely linked to strategic and political objectives, perhaps even more so than the aid offered by some European countries and the US. In general, Chinese aid is closely bundled with infrastructural projects, often linked to the extraction and export of minerals and oil to China. These facts indicate that the aid might hurt Kenya in the long-run.

## **6.0 Summary and Conclusions**

The trade, investment and aid figures between Kenya and China are not that big when compared to other trading partners of Kenya such as the European Union (EU) and rest of Africa. Nevertheless, the recent patterns of trade, foreign aid, and diplomatic ties highlight important lessons for policy:

- 1) There is increased proliferation of FDI through manufacturing and service sector in Kenya. Chinese interest in Kenya has also extended to mining and minerals exploration. There is very limited joint ownership or local capital in Chinese investments. Furthermore, the employment level in such firms is very low for both Kenya and China. The initial interest of Chinese investors was in manufacturing. Nevertheless, there is an apparent shift of investments recent years towards services sub-sector. Most of the invested capital is the services sub-sector. Increasingly also, the structure of employment is gradually changing, with an increasing proportion of foreign employees in Chinese enterprises.
  
- 2) The above trends conform with the hypothesis that China views Kenya as a gateway to the Eastern Africa region and it has become a key focus of China's trade and economic strategy in Africa. China's involvement in numerous road construction projects in Kenya attest to this fact. Being a war-free country with stable political situation has made Kenya an ideal regional base for Chinese investors to expand their trading business. Currently China offers favorable loans to Kenya, builds hospitals and schools for less-developed areas, sets up malaria prevention and control centers as well as sends volunteers to train the locals.
  
- 3) The overall impact of China's trade, FDI, and AID to Kenya is mixed. There are both gains and losses. Arising from the low price of imports of both consumer and producer goods, there are gains from the cheap products, quality notwithstanding. On the same scale, local producers are the losers due to competitive pressure although they may get cheaper supply or producer goods. Employees of collapsing firms, which fail to withstand competition, may also lose. The implications of China-Kenya economic relations have intricate dimensions with direct and indirect consequences. Some of the indirect impacts relate to loss of regional markets or loss of opportunity to participate in

international trade. Likewise, the Chinese FDI present an opportunity for technology transfer and possibility of upgrading local enterprises. This is likely to make local firms competitive for the international markets. Given the implication of such impacts for political and social change, this is an area for further research.

## **.Appendix A: Bilateral Agreements Signed between Kenya and China**

The following Agreements were signed during President Mwai Kibaki's State visit to China in August, 2005 (Kenya, 2006):

- a) Agreement on Economic and Technical Cooperation for a grant of 60 million Yuan. 5 million Yuan was earmarked by the Chinese for provision of rice as relief food donation during the Chinese President's visit
- b) Framework Agreement between the Government of People's Republic of China and the Government of the Republic of Kenya on Provision of Concessional Loans of Yuan 400 million (3,54 billion Kenya Shillings). Agreements for the Rural Telecommunication Development Project, and the Power Distribution System and Modernization and Strengthening project, have been signed under these Framework Agreements.
- c) The Bilateral Air Service Agreement.
- d) Collaborative Agreement between the Central Administration of Quality Supervision, Inspection and quarantine of the People's Republic of China and Kenya Bureau of Standards.
- e) Exchange of letters on Radio Cooperation between the State Administration of Radio, Film and Television of the People's Republic of China and the Ministry of Information and Communication of the Republic of Kenya. China Radio International launched the first FM Radio Station (91.9 in Nairobi in January 2006).
- f) A letter of accreditation was signed between Kenya and China on 18<sup>th</sup> July, 2006, marking the final stage of the China Radio International (CRI) project.

The following Agreements were signed during H.E. President Hu Jintao's visit to Kenya in April, 2006

- Agreement on the Economic and Technical Cooperation between the Government of the People's Republic of China and the Government of the Republic of Kenya, for a Grant of 60 million Yuan.
- Agreed Minutes of the 3<sup>rd</sup> Session of the Joint Trade and Economic Commission between the Government of the People's Republic of China and the Government of the Republic of Kenya.
- Exchange of Letters of anti-Malarial Medicine (Grant of RMB 5,000,000).

- Exchange of Letters for Maintenance of the Moi International Sport Center.
- Exchange of letters for donation of rice (Grant of RMB 5,000,000).
- Exchange of letters for a feasibility study on rehabilitation of Nairobi roads and street lighting.
- Renewal of Agreement on Educational Exchanges and Cooperation (2006-2010) between the government of the People's Republic of Kenya.
- Implementation Programme under the Cultural Agreement between the Government of the People's Republic of China and the Government of the Republic of Kenya for the year 2006-2008.
- During President Jintao's visit, H.E. President Mwai Kibaki requested China to consider assisting Kenya in building the railway link between Kenya and Southern Sudan. The Chinese President indicated they would initially be willing to assist in the feasibility study.

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