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**Review of Kenyan  
Export Processing Zones  
Programme**

**October 1995**

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The objective of this project is to:-

- (i) Review progress to date on the Kenyan EPZ Programme.
- (ii) Identify the technical assistance needs of the EPZ Authority, which is responsible for the overall management of the programme; and
- (iii) Prepare a project document which can be presented to various donor agencies for financial support.

The basic approach in this project is to:-

- (i) Survey selected aspects of the international EPZ situation which are relevant in analysing the Kenyan EPZ performance (these issues are covered in Appendix 1).
- (ii) Analyse the changing economic, trading and investment environment in which the EPZ programme operates, and the likely impact of this environment on EPZ development (see Chapter 2).
- (iii) Examine the EPZ development to date, identifying the strong and weak points and make proposals for improving the operation of the programme (covered in Chapter 3).
- (iv) Identify the technical assistance needs of the Authority in order to realise fully the development potential of the EPZ programme. These technical assistance needs should cover staff training, technical consulting and equipment. These needs are identified in Chapter 3.
- (v) Prepare a project document in line with standard UNIDO guidelines (see Appendix 2).

Field work for the project was carried out in the first 3 weeks of October 1995.

## **CHAPTER 2      THE ECONOMIC ENVIRONMENT**

### **2.1      A General Review**

The Kenyan economy is more advanced than any other in East Africa. It has achieved a reasonable growth rate over the years since independence. Throughout most of the 1980's the growth rate average is about 4% a year. A combination of factors including droughts resulted in very low growth rates in the early part of this decade. In 1994 the growth rate recovered to 3% and the expectations for 1995 and 1996 are for even higher growth rates.

Kenya has a relatively well developed manufacturing sector, accounting for around 10% of GNP. Development of the economy and the manufacturing sector in particular was similar to that of many developing countries. In the years following independence there was a rapid expansion of the manufacturing sector, based on the production of a wide range of consumer goods and products for the domestic market. As the limits of that policy were reached in the 1980's, the emphasis shifted to export production and trade liberalisation.

Since 1986 there has been a gradual rationalisation of the customs tariff and steady reduction in tariff rates. Quantitative restrictions and import controls have been eliminated. In addition to trade liberalisation, other economic controls have also been dispensed with. All price controls have been abolished. The currency is allowed to float and restrictions on current account transactions have been removed.

In a liberal economic climate a number of manufacturing sectors which developed in a protected environment to service the domestic market are likely to contract or disappear. This point has been recognised by the government. The Minister for Commerce and Industry noted in October last year that liberalisation "may lead to many inefficient domestic firms to go under".

In the current economic climate, the main way in which the economy and the industrial sector in particular can expand is via exports. To develop a successful export manufacturing sector is not a simple task. Not all domestic manufacturers have the capital or expertise to succeed in export markets. It is necessary in most countries (including Kenya) to attract new, mobile foreign investors with technology and market expertise to develop a successful export manufacturing sector.

### **2.2      Trading Environment**

Trade liberalisation has been a feature not only of the Kenyan economy but also of the economy of all the neighbouring states in East Africa. The opening of the neighbouring economies presents obvious opportunities for Kenyan traders and manufacturers. Over the last couple of years they have moved to exploit these opportunities. The

results are reflected forcefully in the export statistics. In 1994 for the first time, Kenyan exports to the PTA region exceeded those to the European Union. The most important markets for Kenya PTA trade are Uganda, Tanzania, Rwanda, Somalia and Ethiopia. The export/import ratio was 11 to 1 in 1994, up from 3 to 1 in 1990. Kenya's exports to the PTA have grown by 700% since 1990 compared with an overall growth of about 250%. The strong growth in PTA exports is based on:-

- (i) a recovery in the economies of neighbouring States and a liberalisation in their trade regimes; and
- (ii) the relative strength of the manufacturing and trading sectors in Kenya.

Moves to improve further trade co-operation between the neighbouring States should enhance the prospects for Kenyan exports, including EPZ exports.

Whether or not plans to further economic co-operation between the neighbouring States leads in the medium or longer term to the establishment of some form of free trade area or customs union is difficult to predict. At a global level, there is a very definite move towards the establishment of free trade areas within economic regions. The economic forces in East Africa seem to be pressing in a similar direction.

If a free trade area or customs union is established in East Africa, in the medium or longer term it will have significant implications for the operation of the EPZs, and particularly for those firms within the EPZ supplying regional markets. The issue of free zones and customs unions or free trade areas is covered in Appendix 1.

EPZ companies selling a significant (in most cases 30% or more) percentage of their total output in regional markets will in the event of moves to establish a free trade area or customs union want to:

- (i) pay duty only on the imported raw material content of the products sold in the regional market; or
- (ii) opt out of the EPZ regime.

### **2.3 Export Oriented Investors**

Attracting export investment is a difficult task, especially in Africa. There is no tradition of export oriented investors coming to Africa. All of the investment in Africa to date has been in the development or extraction of raw materials or processing goods for the domestic market. Raw material or domestic market producers will often suffer poor infrastructure and difficult bureaucratic conditions to gain access to materials or markets (where there are often monopoly producers). Such investors do not respond to incentives (such as tax holidays) or marketing efforts by investment promotion agencies. Market conditions (e.g. large market or monopolistic conditions) and valuable raw materials are the key attractions or determinants. Such investors are often large multinationals with considerable experience of difficult operating environments.

Export oriented investors are influenced by different considerations. Good infrastructure and operating conditions are necessary. Export investors are often small or medium scale international investors with limited knowledge of operating conditions or incentives in overseas locations. Most importantly they can very often choose between many different locations. They can be and are strongly influenced by good

promotional and marketing efforts, as well as good operating conditions within the host country.

In a country starting to attract export investors, it is often difficult to create a good physical and administrative operating environment on a countrywide basis in which

- (i) export investors are attracted; and more importantly;
- (ii) where such investors can succeed without encountering too many difficulties.

## **2.4 Kenyan Investment Climate**

Kenya in the 1980's was a difficult environment for new foreign investors. Suitable buildings were not easy to find. In addition, investors would encounter serious problems and delays with bureaucracy. In recent years there has been a streamlining of administrative procedures and the elimination of some of the permits required by investors. Nevertheless, the investment climate remains difficult. The flow of direct investment into the country has declined in the 1990's according to IMF estimates. The volume of export oriented manufacturing investment is very small.

However, there is no evidence to suggest that the Kenyan investment climate was any worse than that in the neighbouring countries (although this situation seems to be changing), or in other parts of Africa. This point is acknowledged by commentators with a close knowledge of Kenya and Africa. The existence of a large number of overseas journalists in Nairobi is one reason why Kenya is often featured in the international press stories (usually in a negative context).

Kenya is a major destination in Africa for tourists. Despite the adverse investment climate, tourists numbers have remained high in recent years. In 1994 tourist numbers were up on the previous year. Export oriented investment is not flowing into other parts of Africa no less than into Kenya.

Many of the facilities required by export investors are better in Kenya than elsewhere in Africa e.g. international transport services, hotel facilities and commercial support services.

It should be noted however that in recent years investment conditions in Tanzania and Uganda have improved considerably as well as their image overseas. The Uganda Investment Authority is developing a reputation as a very efficient promotion agency with strong government backing. Up to 1500 projects have been approved in recent years. A number of people interviewed in relation to this project have contrasted the Ugandan government's very explicit and strong support for investors and investment, and the apparent ambivalent attitude of the Kenyan government.

## **2.5 Promoting Investment**

In an effort to encourage and facilitate investors coming to Kenya, the government established the Investment Promotion Centre in 1986. The task of the Centre is to assist investors in all sectors of the economy including those in tourism, agriculture and horticulture. The main role of the Centre is the approval of investment projects and assist approved projects in securing the necessary permits and licences. The ability of



the centre to promote investment in Kenya and assist investors in establishing businesses in limited by the availability of resources and a number of changes in personnel over recent years. At present the Centre has about 35 staff. Because of resource constraints, the Centre has not been able to identify selected or targeted groups of investors and persuade them through intensive promotion efforts to establish in Kenya.

In addition to the Investment Centre, the government in 1986 also established a manufacturing under bond (MUB) programme to encourage investors to manufacture for export. To date about 40 investors have been approved under the scheme. Applications under the scheme are processed by the Investment Promotion Centre. Most of the approved investors are of Kenyan origin and in the garment business. Most of the output is destined for the United States market. A number of MUB's have ceased to operate. Many others are experiencing trading difficulties at present and have temporarily stopped production, or are operating at low levels due to difficulties in the American market and competition from other countries. Most MUB investors are producing "at the lower end of the market" in restricted physical conditions which do not always facilitate production efficiency.

In another move to attract export investors the Kenyan government in 1990 established an export processing zones programme.

### 3.1 Role of EPZs in Kenya

The EPZ formula has been acknowledged by the World Bank and other international development agencies "as very effective in the early stages of an export drive as a means of attracting foreign (and domestic) investors in demonstrating a country's export potential, especially in less developed countries that lack the critical elements needed to initiate an outward development strategy. However, to succeed the development of infrastructure, the formulation of appropriate incentives and other elements of the working environment must be well managed".

In 1990 there was a strong justification for initiating an EPZ programme in Kenya. The country had one of the most developed manufacturing sectors in the continent. The support services for export industry were reasonably good. The potential for further development based on import substitution was very limited. The overall administrative and operating conditions in the domestic economy were difficult. If Kenya wanted to develop an export industry sector based in part at least on foreign investment, an EPZ type environment was essential.

In the last 5 years a number of changes have taken place in the economy. In particular there has been considerable deregulation and a liberalisation in relation to:

- (i) establishing businesses;
- (ii) trading; and
- (iii) foreign currency payments.

Nevertheless, many of the problems facing export investors in 1990 - bureaucratic delays with shipments and inadequate infrastructure and buildings, as well as security problems still remain. The arguments for EPZ development in 1990 are for the most part still valid in 1995. There is still a great need for an EPZ, providing a good secure, physical and administrative environment. Over the last 5 years very few (if any) foreign export manufacturing projects have established in the domestic economy. In the last four years 48 foreign and domestic export projects have been approved by the Authority - 22 are in operation and 13 are waiting to start.

### 3.2 Review of Progress

The Kenyan EPZ programme began in 1990 when the government passed a law providing for the establishment of an EPZ Authority. The first EPZ, The Sameer Industrial Park covering 16.5 hectares and a site of 339 hectares at Athi River were gazetted on November 23 1990. Since then 11 other EPZ sites have been gazetted. The first EPZ investors were licensed in February 1992. Up to August 1995 a total of 48 investor licences were issued. Tables 2 and 3 provide an analysis of the licensed investors.

A problem in evaluating the progress of the programme is that there are no precedents in Sub-Saharan Africa which might be used as a yardstick or guideline against which progress can be measured. Making comparisons with zones in Asia, North Africa or Central America is not valid. Zones in these regions are:

(i) much closer to major centres of outward investment than Kenya:

**TABLE 1 - EMPLOYMENT**

December 1992	534
December 1993	1653
December 1994	2720
June 1995	2911

Male/Female ratio - Dec 1994 (based on sample of 12 firms)

Male%	Female	Total
1056 (51.6%)	992	2048

Job approvals v actual employment

December 1994	2801 -	2720
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Source : Kenyan EPZ Authority.

**TABLE 2 - EPZ PROJECTS AND JOB APPROVALS  
ANALYSIS BY YEAR AND STATUS (OCTOBER 1995)**

	Never Started	Closed	Waiting to start	In Operation	Total
<b>1992</b>					
Projects	4	6	-	7	17
Jobs	259	110	-	776	1145
%	22.6%	9.6%	-	67.8%	100%
<b>1993</b>					
Projects	-	1	1	3	5
Jobs	-	186	253	849	1288
%	-	14.4%	19.6%	66.0%	100%
<b>1994</b>					
Projects	2	-	8	10	20
Jobs	61	-	1051	2939	4051
%	1.5%	-	25.9%	72.6%	100%
<b>1995 (Oct.)</b>					
Projects	-	-	4	2	6
Jobs	-	-	291	299	591
%	-	-	49.3%	50.7%	100%
<b>Total</b>					
Projects	6	7	13	22	48
%	12.5%	14.5%	27%	46%	100%
Jobs	320	296	1595	4863	7074
%	4.5%	4%	22.5%	69%	100%
Source:	Kenya EPZA.				

**TABLE 3 - EPZ PROJECTS AND JOB APPROVALS  
ANALYSIS BY SECTOR AND STATUS (OCTOBER 1995)**

	Never Started	Closed	Waiting to start	Operational	Total	% of Total
<b><u>Clothing</u></b>						
Projects	-	1	4	8	13	27.1%
Jobs	-	186	861	2898	3945	55.8%
<b><u>Raw Material Processing</u></b>						
Projects	2	1	3	5	11	22.9%
Jobs	89	18	407	1057	1571	22.2%
<b><u>Pharmaceuticals</u></b>						
Projects	1	1	-	2	4	8.3%
Jobs	50	-	-	684	734	10.4%
<b><u>Electronics</u></b>						
Projects	2	-	1	2	5	10.4%
Jobs	115	-	15	21	151	2.1%
<b><u>Other</u></b>						
Projects	1	4	5	5	15	31.3%
Jobs	66	92	312	203	673	9.5%
<b><u>Total</u></b>						
Projects	6	7	13	22	48	100%
Jobs	320	296	1595	4863	7074	100%

Source : Kenya EPZA

- (ii) closer to final destination markets; and
- (iii) have strong ethnic and cultural links with major investing countries.

Proximity to centres of outward investment does make a significant difference to investment flows. Mexico has a long border with the United States and as a result was a major recipient of US investment over the years (about 500,000 jobs were created in the Maquiladora industry over the last 30 years). A second problem in evaluating progress is that it is less than four years since the first group of investors were approved. During those years the Authority has encountered some difficulties with the availability of sites and buildings. The first zone at Sameer was fully occupied in late 1992. There were no buildings available in 1993 - Athi River was under construction. More recently the Authority has encountered difficulties with the completion of buildings in the Athi River zone, thus delaying the implementation of a number of approved projects. New private zones are now nearing completion in Nairobi and Mombasa and developed sites are available at Athi River.

Throughout the 1980s the most successful zones around the world, apart from Mexico, averaged about 7000 jobs a year. However, most zones in Central America and the Caribbean averaged around 1000 to 3000 jobs a year.

The Kenyan EPZ programme has averaged about 750 jobs a year since 1992. The prospects in the coming years for continued employment growth are good, as a number of major investment projects are commencing operation. The quality of the investment in Kenya compares favourably with that of other zones. The male/female employment ratio is around 50%. In many zones up to 85% of the workforce are women engaged in assembly work.

A total of 7074 jobs have been approved to date in 48 projects. The low level of project approvals in 1993 and 1995 are noteworthy, as are the high levels in 1992 and 1994. The low levels in 1993 and 1995 reflect in part at least the non availability of buildings. The level of enquiries at present is strong. However, with the increased availability of sites and buildings, the need for a very intensive focus promotion campaign is evident.

What is not evident in the figures is that a number of good quality projects are in the process of implementation. These projects are being closely watched by other investors. Successful implementation will lead to additional projects. The number of approved projects which have failed to start is quite small compared with other countries. In a number of countries over 30% of approved projects have failed to materialise. In Kenya the figure is 12.5% in terms of projects approved, and 4.5% in terms of jobs approved. The failure rate is reasonable - only 10% of projects accounting for 4% of approved jobs have ceased to operate.

The dependence on the clothing sector is lower than in many zones. About 56% in terms of job approval and 27% in terms of project numbers are clothing projects. The number of EPZ firms processing domestic or regional raw materials is relatively high. The pharmaceutical sector is well represented at present with two good quality investors.

### 3.3 Availability of Sites and Buildings

The situation with regard to the availability of sites and buildings for EPZ investors has improved considerably in recent times. There are upwards of 50 hectares of good quality industrial sites available at Athi River with infrastructure which would suit almost all EPZ investors. There are over 25,000 sq. metres of buildings under construction by the Nagoya EPZ company at Changamwe in Mombasa and in Embakasi in Nairobi. These buildings will become available in the early part of 1996. There is about 5000 sq. metres of space available at the Coast Industrial Park in Mombasa. There are limitations on the type of investor which can be accommodated at Changamwe because of infrastructure restrictions (no sewerage connections). The fact that buildings are all constructed means that flexibility in accommodating investor needs is limited. At present the developer does not have a final cost for the Changamwe or Embakasi sites. Consequently, he could not provide an indication of the least cost of the buildings.

Future EPZ development would benefit from a more flexible approach to design and layout and some pre project test marketing suggestions from potential investors.

### 3.4 Investor Reaction

A satisfied customer base is a major factor in attracting further investors. During the course of the study interviews were conducted with a number of investors. The Authority has developed a good rapport with investors. Most complaints centred on the difficulties of the port of Mombasa, customs delays and the cost of transshipping goods from Mombasa to Nairobi. Resolution of these difficulties would be a decided advantage in zone promotion. The Authority is developing some initiatives at present which hopefully will alleviate and resolve these problems. Other complaints centred on the availability of buildings and delays in securing immigration and labour permits. There were some labour difficulties which in part at least stem from cultural misunderstandings. These have been largely resolved. Such problems are not unusual in the early stages of a zone development.

It is important that the Authority regularly reviews the services it provides for investors to ensure a good standard of service and anticipate problems. A potential problem at Athi River relates to the cost and logistics of transporting people from Nairobi to work in the zone. With two new major projects starting up at present the numbers of commuters from Nairobi could increase considerably in the coming years. This issue was already raised by investors and is one which the Authority needs to consider.

### 3.5 Customs Administration

An EPZ is about moving goods quickly into and out of a zone to export markets. This requires a Customs Administration with a positive attitude towards the movement of goods, together with suitable procedures and operating guidelines. Ideally, EPZ imports (and other imports for use in export products) should benefit from a separate fast track procedure which permits clearance within 24 hours.

It was not possible during the course of the study to examine in any detail the existing customs procedures. From brief discussions with investors and customs personnel, it seems that there is a need for improved procedures and operating instructions, in addition to possibly a new management structure and increased staffing to service the growing volume of EPZ (and other export related) business.

**Because customs administration is a central part of the operation of any EPZ programme, the whole issue should be reviewed in some depth by the Customs Administration and the EPZ Authority.** To assist in this review there should be a customs officer with considerable world-wide experience of EPZ procedures and practices.

### 3.6 The Planning/Environmental Framework

EPZ planning operates on two levels. The first is what might be termed economic planning which:

- (i) relates EPZ development to overall national development plans and policies;
- (ii) involves projections of EPZ growth based on historical experience, market demand and future prospects; and
- (iii) establishes the type and location of space and infrastructural requirements based on these projections.

Under the present national plan, employment growth in the manufacturing sector is forecast to be about 6000 annually. If the EPZ sector could make a significant percentage contribution to this target (say 2000 to 3000 jobs annually) it would be a considerable achievement. Based on a discussion with the Authority about investment prospects over the next year or two, a target of 2000 to 3000 jobs is achievable. The space and infrastructure implications of this growth need to be examined. If all existing plans were implemented there would most likely be excessive space available. A mix of 10,000 to 15,000 sq. metres of buildings and 4 to 5 hectares of site should be adequate in most situations to cater for this type of target.

In the light of:

- (i) recent proposals by the private sector to provide EPZ sites and buildings; and
- (ii) an analysis of EPZ growth potential in the next 3-5 years based on recent experience and proposed promotion programmes, the Authority should undertake

**a supply/demand analysis for EPZ facilities and review existing proposals for developing EPZ sites.**

A second area of planning relates to the planning, design, and layout of sites and buildings. EPZ sites (and particularly large sites) need to be developed within an overall urban and planning framework. Most EPZ sites are in the 40 to 100 hectare range. Larger sites when developed can place a lot of strain on transport infrastructure. The Athi River site is an exceptionally large one. **A potential problem in Athi River is congestion on the Nairobi/Mombasa road as the zone develops, unless the road is upgraded and widened.**

The planning, design, management and control of industrial parks is a relatively new activity in Kenya. There is a limited amount of experience on this issue. Good planning and design can:

- (i) reduce development costs and the amount of unused or wasted space;
- (ii) result in a wide range of investors being accommodated; and
- (iii) reduce or eliminate environmental damage.

Good lease agreements can protect both the Park users and the Park developer. In the coming years, the Kenyan EPZs will be developed largely by the private sector. Many of these developers could use advice on all aspects of zone development and management. The Authority is responsible for the overall development of the EPZ programme including:

- (i) encouraging private sector developers;
- (ii) evaluating plans; and
- (iii) making recommendations in relation to the issue of developer's permits.

The Authority needs to develop its expertise in all aspects of Park development including planning, design, control and management to:

- (i) advise developers;
- (ii) evaluate proposals; and
- (iii) supervise developments.

The areas in which the Authority needs to develop its expertise include:-

- (i) the technical aspects of industrial park planning, design and control with particular emphasis on environmental controls; and
- (ii) the practices and procedures involved in the management of private industrial parks and EPZs in particular.

Important issues would include lease agreements and procedures for terminating leases (and operating licences issued by the Authority). The requirements in terms of technical assistance include :

- (i) A review of existing plans and procedures from an engineering or technical viewpoint, and an evaluation of the capacity of the Authority to evaluate or review such plans by a specialist in industrial park design and planning;
- (ii) A study by the Authority staff (and its legal adviser) on procedures and practices in relation to lease agreements and Park management, as well as the technical aspects of industrial park design in selected EPZs; and
- (iii) A seminar to impart the knowledge gained during the review by the Industrial Park specialist and the study tours to potential private sector park developers.

### **3.7 Linkages and Technology Transfer**

An important objective of many development programme (including an EPZ programme) is the transfer of skills and technology on a permanent basis to the developing economy (in this case Kenya). Technology is not transferred automatically from foreign investors to Kenya. It must be planned. The transfer occurs when:

- (i) Foreign investors with the assistance of the Authority identify opportunities for sourcing materials and components from domestic suppliers. The overseas investor in such circumstances will often work with the domestic supplier to achieve the desired quality standards and delivery schedules.
- (ii) Foreign investors with appropriate technologies are encouraged through the efforts of the Investment Promotion Division to locate in Kenya.



The Authority needs to support investors in their attempts to source materials within the domestic economy. A person is being recruited for this purpose at present. He should be enabled to examine how other zones in similar organisations manage linkage programmes.

### 3.8 Promoting EPZs

The importance of EPZ promotion has already been stressed in this document. An important point in EPZ promotion is the fact that about one third of investors are of domestic origin and another one third are domestic/foreign joint ventures. There are already a number of Kenyan investors involved in zone projects. There is a tendency on the part of some of the zone authorities to ignore domestic investors in their promotion campaigns on the assumption that they (the domestic investors) are fully aware of the advantages which the EPZs have to offer. This is a dangerous assumption in any context.

The Kenyan Zone Authority has already made a number of presentations to business groups within the economy. However, there is still a lot of work to be done before all the potential domestic investors are fully aware of the advantages of the EPZ. A lot of this type of promotion is best undertaken with smaller groups. The image projected in the domestic media of the EPZ programme can help influence potential investors. Much of the publicity in the daily media at present is negative or neutral in character. The Authority should examine ways and means of improving its media image by using

- (i) positive photographic opportunities e.g. visits by various dignitaries to EPZs, factory openings; and
- (ii) announcing "good news" stories such as project approvals and the results of promotion trips etc. (The Authority is recruiting a media consultant at present).

An important objective of any zone development is the development of linkages with the rest of the economy and the transfer of technology. Some industries and companies are better from this point of view than others. The Authority should take a pro-active approach to promotion by targeting sectors and companies which best fit the needs of the Kenyan economy.

Identifying suitable sectors and companies within those sectors and developing suitable focus presentation material, including project proposals, is an important task from the point of view of the long-term security of the EPZ programme. This is a very specialised promotion activity which involves:-

- (i) access to a wide range of industry specific information; and
- (ii) expertise and a good knowledge of selected industry sectors.

Another advantage of this promotion approach is that it permits the Authority to go direct to investors and make the case for investing in Kenya and the Kenyan EPZ programme directly to them, thereby neutralising or reducing the effect of any general adverse publicity about Kenya. To undertake this task effectively, the Authority needs the support of specialists in selected industry sectors (3 people for 2 months each) to assist in developing a methodology and presentation material. The Authority also needs up to date information systems for accessing the necessary study information and making contact with investors. To determine the nature of the Authority's

information and technology requirements, it needs the assistance of an information technology specialist. In addition the Authority will need equipment and staff with the necessary training in the use of this equipment.

Responsibility for investment promotion to date has rested mainly with the EPZ Authority. So long as the Authority is held responsible by the government for the success of the EPZ programme it will have to promote the concept. However, the private sector will have to take an increased responsibility (including financial responsibility) for promotion activity. To date the promotion and marketing efforts of the private sector have been limited and largely uncoordinated.

The Authority should reach agreement with the private sector on sharing promotion costs and ways and means of co-ordinating promotion activity to avoid waste and misunderstandings.

### 3.9 The EPZ Authority

Over the past five years the Authority has built up a considerable body of experience and expertise in developing and managing an EPZ programme. The relatively low failure rate and the small number of projects which failed to go ahead is a reflection of the Authority's ability to evaluate projects.

In developing its expertise the Authority has benefited from a two year technical assistance project funded by the United Nations Development Programme and executed by UNCTAD. The emphasis was very much on capacity building. Two international experts were recruited for 24 months each to work with Authority staff on all aspects of EPZ development. Twelve fellowships were provided to allow Authority staff to travel overseas for training

The result of this support, plus experience, is an EPZ Authority whose staff have a good understanding of the main issues involved in EPZ development and who have managed the EPZ programme in an effective manner to date.

The Authority is however, lacking expertise in some areas notably in

- (i) selecting and targeting suitable industry sectors and companies within those sectors in order to maximise the gains from EPZ development; and
- (ii) the technical aspects of planning, developing and managing EPZ industrial parks, including environmental protection so that the Authority can advise private developers on all aspects of industrial park planning, development, evaluate developers proposals and supervise the operation of various parks, as the Authority with responsibility for such matters

## CHAPTER 4

### CONCLUSIONS AND RECOMMENDATIONS

#### 4.1 Conclusions

1. In the current economic climate in Kenya economic expansion and in particular industrial expansion will depend largely on exports.
2. The trading environment for exporters in Kenya is improving with the growth and liberalisation in neighbouring economies. PTA exports exceeded exports to the European Union for the first time in 1994.
3. If or when Kenya becomes a member of a customs union or free trade area, EPZ investors selling a significant percentage (in most cases over 30%) in the customs union market will either:
  - (i) pay duty only on the imported raw material content of the product; or
  - (ii) opt out of the EPZ.
4. Attracting export investment is always a difficult task because of the intense competition for such investment among countries. The difficulty is even greater in Africa because:
  - (i) there is no tradition of such investment in Africa, and
  - (ii) Africa is far removed from the main centres of outward investment.
5. Export investors are strongly influenced by:
  - (i) promotion efforts -unlike domestic market investors,
  - (ii) a good secure physical environment with support infrastructure and services, and
  - (iii) "bureaucracy free" operating conditions.
6. These conditions were lacking in Kenya in the past where the investment climate was perceived as difficult -although no more so than other parts of Africa. (It should be noted that the reputation of Uganda and Tanzania as investment locations is improving rapidly and there is some anecdotal evidence to suggest that some investment is flowing from Kenya to these countries).
7. In an effort to promote export growth the Kenyan government has over the past ten years taken a number of initiatives including; the establishment of an Investment Promotion Centre, the introduction of a manufacturing under bond scheme, and the development of an Export Processing Zone (EPZ) programme.
8. The EPZ has been acknowledged by international development agencies as a very useful formula for attracting foreign and domestic investors in the early stages of a country's efforts to develop an export manufacturing sector.  
Note: One third of EPZ investors are of domestic origin and another third are foreign/domestic joint ventures.

9. In 1990 there was a strong justification for an EPZ programme in Kenya. The country had a well developed manufacturing sector with good support services but a difficult bureaucracy and physical environment.(i.e. a lack of well planned and developed industrial sites and buildings).
10. In the last five years the economy has been liberalised and many controls relating to trade and investment have been abolished. However many of the problems facing investors in 1990 still exist-including the lack of well planned industrial parks and bureaucratic delays. The Investment Promotion Centre because of budget limitations, management changes, and limited staff resources is constrained in its ability to provide a "one stop service" to investors. Because of these problems the need for an EPZ programme is as great now as in 1990.
11. **The need for an EPZ programme is in some ways even greater now than in 1990. Competition from neighbouring states is now more intense than before.** A number of people interviewed in relation to this project have commented on the enthusiastic government support for foreign investment in Uganda and Tanzania and contrasted this with the apparent non-committal attitude of the Kenyan government.
12. **The Kenyan EPZ programme has developed successfully over the last four years providing almost 3000 jobs to date. The prospects of additional jobs over the coming months and years are good** as projects currently being implemented reach their full employment potential. A total of 48 projects with an employment potential of 7074 jobs have been approved.
13. The quality of many of the approved projects is good. Dependence on the clothing sector (56% of total jobs approved) is less than in many EPZs where up to 80% of employment is in clothing factories. Projects processing local raw materials account for 22% of jobs approved.
14. The problems with the availability of sites and buildings for investors which limited the Authority's promotion efforts have been largely overcome. There are upwards of 30,000 sq. Metres of building space available or under construction in private EPZs and 50 ha. of developed sites at Athi river.
15. **Promotion. With the increased availability of buildings a major promotion effort is essential if the programme is to maintain its momentum.** The promotion effort should focus on;
- (i) projecting a positive image of the Authority and the EPZs in the national and international press.
  - (ii) promoting the EPZ concept aggressively among selected groups within Kenya e.g. diplomats, bankers, accountants, investment advisors, industry associations, and major investor groups. The need for more aggressive promotion domestically was emphasised in a number of interviews conducted in relation to this project
  - (iii) developing a selective/targeted approach to promotion generally but particularly in foreign markets. This would mean identifying sectors and companies within sectors for intensive promotion, using the full range of

modern information technology-both for research purposes and making contact with investors.

16. Most investors are satisfied with the operation of the EPZs. The relatively low level of approved projects which do not start or close reflect this. The main complaints centre on delays at the port, problems with customs clearance and the cost and difficulty of transshipment from Mombasa to Nairobi.(The Authority is examining ways and means of solving these problems at present). The non availability of buildings at Athi River was a problem for some investors. The private sector will have to play a more prominent role in the promotion effort and the Authority will have to co-ordinate the efforts of the private sector to avoid confusion, duplication and wasteful competition.
17. The Authority should review the services it provides to investors on a regular basis and where possible anticipate problems. Are there any unnecessary delays in approving projects or securing permits or licences?. Potential problems at Athi River include traffic congestion and travel arrangements for workers living in Nairobi. A satisfied group of investors is a major promotion asset.
19. The difficulties with the Customs Administration should be reviewed by a customs officer with significant EPZ experience who could assist the Authority and the Customs Administration with proposals on organisation, procedures, and operating instructions.
20. The transfer of technology and the development of linkages between the EPZs and the domestic economy will depend a lot on:
  - (i) the type of project attracted to the EPZs (which is based to some extent on the sectors targeted in the promotion effort); and
  - (ii) the opportunities for EPZ trained personnel to find employment in the domestic sector or set up in business.
21. The overall EPZ development needs to be placed in a planning framework.(The Authority is preparing a plan at present). EPZ employment targets should be based on past experience, a realistic demand assessment, and related to overall national targets. The current national plan expects the manufacturing sector to provide an additional 6000 jobs annually. If the EPZ programme could provide 2-3000 of this total it would be a significant achievement.
22. Careful monitoring of the supply and demand for EPZ sites and buildings, and a review of existing EPZ development proposals is necessary to avoid unnecessary competition between sites and a waste of resources.
23. The industrial park concept is relatively new in Kenya. Knowledge of industrial park planning, design, management, and control is therefore limited. There is a need for both the Authority and developers to build up expertise in this area to be able to accommodate the requirements of a wide variety of end users and ensure proper environmental controls.

24. All EPZ sites but particularly larger sites (e.g. Athi River) need to be placed within an urban planning framework to avoid infrastructure bottlenecks or difficulties.

#### **4.2 Recommendation**

A second phase technical assistance programme for the EPZ Authority should be supported by UNIDO and UNDP which would build upon the first phase. The programme should focus on

- (i) building up the competence of the Authority in conducting selected or targeted promotion activity by developing skills in relation to industry sector analysis and the preparation of project profiles and material for presentation to individual companies or investor groups.
- (ii) developing the Authority's skills in accessing and using modern electronic information sources and providing the Authority with the necessary equipment.
- (iii) improving the Authority's capability in relation to the planning, design, management, and control of industrial parks and in particular the evaluation of the environmental impact.
- (iv) providing the Authority with the experience and knowledge to develop and manage an effective linkage programme
- (v) evaluating the Authority's overall operations and
- (vi) providing assistance in evaluating the EPZ customs operations and procedures.

#### **Technical Assistance Programme**

The main elements of the programme would be:-

- (i) A Chief Technical Advisor (CTA) for eighteen months with a strong investment promotion background who in consultation with the authority would oversee the programme
- (ii) A number (probably three ) sector specialists for three months each who would undertake sectoral studies in collaboration with Authority staff and prepare project profiles and presentation material. The sectors would be identified by the CTA in consultation with the Authority
- (iii) An information technology specialist for three months who would assess the requirements of the Authority in consultation with the CTA and the Authority, make recommendations in relation to the necessary equipment and staff training.
- (iv) A civil engineer with experience in industrial park design and management to work with Authority staff in reviewing existing EPZ engineering and management operations and developing guidelines for evaluating future projects
- (v) A customs specialist to work for three months in a split mission in developing proposals in relation to customs management, operating procedures, and operating instructions.
- (vi) Study tours for selected staff involved in engineering evaluation, the linkage programme, sectoral studies, and customs administration -a total of eight.
- (vii) Training for a staff member in the use of information technology equipment.

## APPENDIX 1

### REVIEW OF SELECTED EPZ ISSUES

#### 1. Trends and Developments World-wide

The problem with any analysis or comment on free zone development world-wide is the lack of any agreed definition of what constitutes a free zone and the limited availability of statistics and information on zone development. For present purposes a free zone is defined as a limited geographic area where one or more enterprises can:

- (i) import materials and equipment duty free without restrictions;
- (ii) process, warehouse, pack or otherwise handle those materials or use the equipment to provide services; and
- (iii) export those goods and services - or sell those goods and services domestically after paying the appropriate duties and taxes.

The difference between a single factory free zone and a factory manufacturing under bond is minimal. Free zone customs procedures may be somewhat more streamlined.

The free zone in its modern form is a mechanism for promoting manufactured exports and international services, which began in the 1960's and has been adopted as a policy instrument by many countries in Asia, Central America and the Mediterranean region interested in promoting export growth. In the early years the emphasis in most free zones was on manufacturing activity for export. Domestic sales were prohibited or severely restricted and international service activity was not permitted. Over the years restrictions in domestic sales have been eased and international service activity permitted - although manufacturing is still the dominant activity.

The main advantages of a free zone are:

- (i) an industrial park with good infrastructure, developed sites and possibly standard factory buildings available for lease or purchase; and
- (ii) streamlined customs procedures

This concept is particularly suited to export manufacturers who can operate successfully in industrial parks and who require regular (weekly) shipments of imported materials. Free zones are located mainly in developing countries with an unskilled workforce. The main industry sectors which benefit from the particular conditions offered by free zones are clothing and electronic assembly. Other smaller sectors which benefit from free zone conditions include toy manufacture; sports goods; and other light assembly activity, including watch making, plastic products and light engineering.

In the earlier free zones the emphasis was very much on importing materials for processing and sale in North America and Europe. Notable features in the last 10 years are: an increasing volume of domestic and regional market sales, a growing volume of international service activity, and the processing of domestic raw materials.

There has been very little free zone development in Sub-Saharan Africa, Eastern Europe or South America until recently because the development of an export manufacturing sector was not a priority policy objective in these countries in these regions. However, in the last 5 or 10 years with the switch to what be termed "market economies" , most countries in these regions have shown an interest in free zone

development Many countries have undertaken feasibility studies. A number of countries have passed free zone legislation. However, very few countries have progressed to the stage of actually developing free zone. In Eastern Europe and South America, there are no significant free zone developments. The topic has been discussed in Russia and many other parts of Eastern Europe for a number of years but as yet, with one or two exceptions, there is no free zone legislation in existence. In South America most countries have discussed free zones or export processing zones in recent times. There are free trade zones dating from the early 20th century in a number of countries, but very little of substance in terms of export processing zone development.

## 2. Developments in Africa

Free zones have been developed in North Africa and Mauritius in the 1970's. In terms of numbers, Tunisia and Mauritius have been the most successful. There are upwards of 100,000 people employed in Tunisian free zones and almost 90,000 in Mauritius. Senegal and Liberia also developed export processing zones in the 1970's but were failures. Employment never exceeded 1000 people in either zone. Ghana is often reported in free zone literature as having a free zone since 1978. A free zone law was passed around that time but no free zone was ever declared. The Liberian free zone has ceased to operate due to civil disturbance and attempts are ongoing at present to revive the project in Senegal.

Elsewhere in Africa there has been a lot of discussion on the subject. In West Africa Nigeria, Togo, Cameroon and Ghana have all passed free zone legislation. Togo has attracted 15 or 20 projects in single factory zones in the early 1990's but recent disturbances there have restricted progress. The Cameroon has made some progress. Nigeria has passed a free zone law but there is no progress on attracting investment. In the current political and economic situation, the prospects are not good. Ghana has a free zone law in place and the necessary conditions for successful free zone development. It could have a significant free zone sector within a couple of years. The country has strong donor support, a good investment climate and reasonable infrastructure.

In Southern Africa, Zimbabwe has recently passed a free zone law but the potential for free zone development is limited, especially if Zimbabwe negotiates a free trade agreement with its Southern African neighbours (see discussion on free zones and free trade areas or customs unions in the following sections). Botswana does not have a free zone law. The development, Selibwe Pickwe, is sometimes classed as a free zone development. There are two to three thousand people working in Selibwe Pickwe. The Namibian government has declared free zones in Walvis Bay and Arantis. However, the legal basis for such declarations is uncertain. The country has good infrastructure, a secure operating environment and strong German connections. Most investors coming to Namibia will be attracted by the prospects of duty free access to the Southern African market. Export processing zones will have limited relevance in Namibia. A free port at Walvis Bay may in the longer term prove useful in facilitating transshipment activity if or when the port develops.



The subject of free zones has been discussed in South Africa. Some of the major ports may find a free port concept useful but the EPZ will have limited relevance. There is strong opposition by South African trade unions to the export processing zone concept. Swaziland has considered and rejected the idea. Mozambique is developing a free zone programme at present but progress will be slow until the infrastructure is renewed and investors gain confidence in the country. Madagascar has been promoting free zone activity for a number of years and has been successful in attracting some investment from Mauritius. Malawi has a free zone law in place. It has a reasonable infrastructure and investment climate. However, transport is a major problem and therefore the potential for free zone development will be limited. Zambia has considered the free zone option but as yet does not have a legal framework.

In East Africa there is a free zone in operation in Zanzibar. However, given the small size of the island and the deficiencies in the infrastructure, the development potential is very limited. Tanzania is conducting a free zone feasibility study at present. The idea is being actively considered in Uganda and Ethiopia. Kenya is one of the few Sub Saharan African countries with a free zone programme in operation.

### 3. Employment Structure and Growth Rates

There are about 2 million people employed in free zones around the world excluding China. (The special economic zones in China provide employment for around 3 million people). Asia is the major centre of free zone development, accounting for about half the total employed in free zones (1 million). The employment is spread through 15 countries. There are over 200,000 free zone jobs in Singapore and over 100,000 each in Hong Kong, Malaysia, and Sri Lanka. There are over half a million people employed in Central American free zones, most of whom are in the Mexican Maquiladora, with about 15,000 people in Costa Rica. There are 200,000 jobs in the Caribbean area concentrated in the Dominican Republic (150,000), Bahamas, Barbados and Jamaica. Apart from Tunisia and Mauritius, the main African EPZ centre is Egypt with about 25,000 workers.

Over the 1980's the strongest growth has occurred in Mexico (360,000), the Dominican Republic (100,000), Mauritius (70,000), Tunisia (70,000), and Sri Lanka (70,000). In other countries the growth rate has been more modest. Egyptian free zones added about 20,000 people over the decade and 8000 to 10,000 jobs were created in the Caribbean Islands of Barbados, Bahamas, Jamaica and Costa Rica in Central America.

Electronics and clothing production are the dominant activities in most of the successful free zones. In Madagascar, Mauritius and Tunisia, the most successful African zones, clothing, textiles and leather production account for over 70% of total activity. A similar structure prevails in Sri Lanka, Jamaica, and Bangladesh. In Korea and Malaysia electronics is the dominant activity. In most zones over 80% of the workers are women engaged in assembly activity.

Free zones are often considered enclaves of foreign investment. In most zones however, about one third of investors are foreign, another third are foreign/domestic joint ventures and the remaining third are domestic investors. In zones dominated by the electronics sector, the percentage of foreign investors increases. Most foreign

investors come from neighbouring countries, or countries with whom the zone has ethnic or cultural links. The United States and Canada are major investors in the Caribbean and Central America. Some Far East countries are also using Caribbean and Central American zones to produce products for the United States market. European and Middle East investors are important in many North African zones. France and the United Kingdom are major investors in Mauritius. Japan is the dominant investor in Korea, and Japan and the newly industrialised countries are important investors in many other Asian zones. Australia and New Zealand are significant investors in Fiji.

#### **4 Labour Relations and Conditions**

Working conditions and labour relations in free zones is a controversial subject in many countries. At the early stages of a zone development, labour disputes sometimes arise from misunderstandings between new foreign investors and local workers. This was true in the first zones at Shannon and Korea and subsequently elsewhere. Some zones have laws banning strikes and Union activity which have proved controversial. However, wage levels and working conditions in most zones "tend to be distinctly better" than in the domestic economy, according to World Bank studies on the subject. Other studies also confirm these conclusions. However, these conclusions need to be placed in context. Export processing zones are usually new, high profile buildings with good lighting and ventilation as well as canteens and medical facilities. Living conditions near zones, particularly for migrant workers from the countryside may not match the facilities within the zones. Dormitories can sometimes be overcrowded.

#### **5. Linkages in Technology**

The transfer of technology and the links between the EPZ and the domestic economy are important issues in any EPZ development programme. There was a belief in the 1970's that these linkages in technology transfers would occur automatically. This is not the case. These developments must be planned. The potential for backward linkages depends on a number of factors, the most important of which are:

- (i) the nature of the industry attracted to the zone;
- (ii) the ability of domestic suppliers to meet delivery dates and quality standards for zone producers; and
- (iii) the attitude of zone companies towards sourcing materials and services domestically.

Industries processing domestic raw materials (e.g. agro processing), or sectors using industrial raw materials which are produced domestically, (e.g. cotton yarn produced in Pakistan) will obviously lead to strong domestic linkages. Electronic assembly activities will result in few domestic linkages except where there is a strong domestic electronics industry. In the Korean EPZs, electronic companies source about 30% of their supplies in Korea. In Mexico by contrast without a strong domestic electronics sector, local sourcing is minimal (about 1%). A good domestic packaging or engineering service sector will be able to develop linkages with EPZ companies.

If responsibility for purchasing decisions rests with the EPZ company management rather than on some distant location (e.g. foreign investors home base), the potential for linkage development is substantially improved. This point was highlighted in studies on linkage development in the Mexican Maquiladora. It follows therefore that targeting and attracting companies and sectors which encourage a strong local management team with responsibility for purchasing and marketing, will improve linkage prospects.

Most technology transfer in EPZs occurs through the movement of people trained on the job in EPZ firms into the domestic economy. This will occur only if the business environment in the domestic economy is attractive i.e. domestic firms are willing to pay attractive salaries and offer good career prospects to trained EPZ staff, or conditions exist in the domestic sector where EPZ staff can easily establish new businesses. The contrasting situation of the Mexican Maquiladora and the Taiwanese EPZs highlights this point. In Mexico the annual turnover of Mexican professional staff in Maquiladora was 2.5% versus 23.7% in Taiwan. Most Mexicans (95%) went to other EPZ firms. Most Taiwanese (85%) went to domestic market firms.

## **6. Free Zones and Customs Unions or Free Trade Areas**

There are few examples of EPZs operating in free trade areas or customs unions. The main example to date is the European Union. The issue is especially relevant to investors who establish a base in a free zone to supply a regional market and that market subsequently becomes a free trade area or customs union. EPZ investors operating in customs unions are faced with two options:

- (i) the EPZ is extra territorial from a Customs point of view and EPZ investors pay duty on the finished product going into the customs union or free trade area; or
- (ii) EPZ investors are treated on par with domestic investors and pay duty only on the imported or third country raw material content of products sold in customs union or free trade area markets.

If the first option prevails (duty on the full value of the finished product), EPZ investors with significant (in most cases 30% or more) customs union market sales will opt out of the EPZ and choose a domestic market location. If the second option prevails, investors with significant customs union markets will remain in the EPZ provided that there are no quantitative restrictions on customs union sales. In the second scenario domestic market producers will obviously seek conditions similar to EPZ producers.

The second scenario prevails in the European Union. Here EPZ producers pay duty on the third country or imported raw materials used in the finished products sold in the European Union. In addition, EPZ producers are subject to the same operating conditions and incentives as non EPZ producers, to ensure "free and fair competition" i.e. EPZ producers pay duty on imported (non EU) machinery and equipment, and pay the same taxes as non EPZ firms.

## **7. Zone Lifespan**

An EPZ is a limited area where suitable physical and administrative conditions are created in which export oriented foreign and domestic investors can operate

successfully. The need for EPZs arise because suitable conditions cannot be created easily or quickly on a countrywide basis. The need for EPZs diminishes as conditions in the domestic economy improve. If an EPZ programme is successful it should provide a stimulus and example to improving conditions in the domestic economy. A number of commentators have suggested that a fall in demand for EPZ facilities (as the gap between the EPZ and the rest of the economy is reduced and eliminated) and the eventual disappearance of EPZs is an indication of the success of an EPZ programme i.e. helping to create suitable conditions countrywide for export industry development. In some countries the spillover effect from the EPZ to the rest of the economy never happens. Linkages between the zones and the domestic economy are minimal. This is the case in some Caribbean and Central American zones. In other countries, notably a number of the East Asian countries, the demonstration effects of EPZ development is fully absorbed inside the decade and the need for EPZs thereafter diminishes and disappears.

#### 8. Size and Specification

Most EPZ sites are in the 40 to 80 hectare range. The Grupo Bermudez in Mexico which has developed 10 industrial parks for Maquiladora industry, believes that parks in the 50 to 70 hectare range are ideal. Larger zones can cause a lot of congestion - particularly if the employment density in the zone is high. There are significant economies of scale in the development of industrial parks up to about 50 hectares. After that the gains from internal economies of scale are usually offset by external diseconomies.

The ideal site should be gently sloping (one in fifteen is ideal) for drainage with good ground bearing conditions and support infrastructure, including good road access and a reliable water supply (40,000 litres per hectare per day is regarded as a minimum in most situations).

A square site is ideal from the point of view of space utilisation. The site should be developed in phases in line with demand. The first phase should be based on conservative demand projections and be fully developed and occupied within three years. In most cases a 10 to 20 hectare first phase development is more than adequate. Large areas of developed land unused for years means capital lying idle, producing no financial returns, leading to a difficult financial situation, reduced maintenance budgets, and a gradual and steady deterioration in the whole standard of infrastructure over time. If demand exceeds expectations, the second phase development can always be accelerated. However, the reverse is not possible.

**A. CONTEXT****1. Description of Subsector**

The Kenyan EPZ law was passed in 1990 and the EPZ Authority established. This initiative by the government was designed to create a physical and administrative environment in which the private sector could establish export business. The private sector, apart from establishing businesses within the export processing zones is an important partner in developing and managing a number of zones. The first zone to be gazetted under the EPZ programme was the privately sponsored Sameer zone in Nairobi. The second zone (339 hectares at Athi River) was developed by the Zone Authority with World Bank funding. The first phase development of 90 hectares includes administrative buildings and 12 factory units is completed at Athi River.

A total of thirteen EPZs have been gazetted by the Authority and the government to date. They include seven in Nairobi, five in Mombasa and one in Nakuru. Six zones are operational of which two are single factory EPZs and four will accommodate a range of investors. A seventh zone, the Coast Industrial Park, is ready to receive investors. Construction activity is under way in two further zones - one in Mombasa at Changamwe and Magoywe EPZ at Embakasi in Nairobi.

The EPZ Authority has approved forty eight projects involving 7074 jobs. These include thirteen clothing manufacturers, eleven raw material processors, four pharmaceutical companies, five electronics companies and fifteen other projects. The clothing sector accounts for 56% of the approved jobs, followed by the raw material process group with 22% and pharmaceuticals with 10%. So far six projects involving 4% of approved employment have withdrawn without starting. Seven small projects accounting for another 4% of job approvals have closed. There are 22 projects in operation with a job potential of 4863 and thirteen projects waiting to start. There are about 3000 people currently employed in EPZ projects, about 50% of whom are men.

**2. Host Country Strategy**

Since 1986 Kenya has been placing a growing reliance on export manufacturing as a means of stimulating the economy. That year the Investment Promotion Centre was established. Its main function is to approve investment projects and assist investors in securing the necessary permits and licences. The ability of the Centre to assist investors has been constrained by a lack of resources and changes in senior personnel over the years. In addition to the Centre, the government in 1986 also established a manufacturing under bond programme to encourage investors to manufacture for export. To date about 40 projects have been approved under the MUB scheme. A number of these projects have since ceased production and many other are operating at levels way below their capacity in a restricted physical environment (unsuitable buildings). Most MUB investors are of Kenyan origin.

In another move to attract export investors, the Kenyan government in 1990 established an EPZ programme. The details of progress to date have already been

outlined. The EPZ programme has succeeded in attracting a significant number of export oriented foreign investors. There are few (if any) export oriented foreign manufacturing investors operating outside the EPZ sector.

The EPZ formula is considered an ideal initiative by international development agencies for countries embarking on an export manufacturing development strategy - especially where the necessary conditions are absent on a countrywide basis. Within an EPZ a good physical and bureaucracy free environment can be created, which export investors find attractive. In 1990 there was strong justification for initiating an EPZ programme in Kenya. The country had one of the most developed manufacturing sectors on the continent. The support services for export industry were reasonably good. The potential for further development based on import substitution was very limited. Nevertheless, the overall administrative and operating conditions in the domestic economy were difficult. If Kenya wanted to develop an export industry sector based in part at least on foreign investment, an EPZ type environment was essential.

In the last five years a number of changes have taken place in the economy. In particular there has been considerable deregulation and liberalisation in relation to :

- (i) establishing businesses;
- (ii) trading; and
- (iii) foreign currency payments.

Nevertheless, many of the problems facing export investors in 1990 - bureaucratic delays with shipments and inadequate infrastructure and buildings, as well as security problems, still remain. The arguments for EPZ development in 1990 are for the most part still valid in 1995. There is still a need to provide within an EPZ framework a good secure physical and administrative environment for export investors.

### 3. Prior Assistance

The EPZ Authority has already benefited from a capacity building project funded by the UNDP with the United Nation's input of 662000\$ (Ken/91/009/A/01/40). The purpose of the project was to strengthen and consolidate the function of the EPZ Authority through the provision of on the job training and overseas training for its professional staff. The main elements of the assistance were:

- (i) the provision of two experts for two years each to act as advisors to the Authority; and
- (ii) training fellowships to send 12 Authority staff for overseas training;
- (iii) study tours; and
- (iv) 40,000\$ to purchase equipment.

This project has been completed satisfactorily. The progress made in developing a number of zones, the low level of non starters among approved projects, and the low level of project failures is a reflection of the success of the programme in developing the technical and management capacity of the Authority.

The World Bank has provided substantial funding for the development of the Athi River zone which began in 1992. The responsibility for developing and operating the zone rests with the EPZ Authority. In line with its ongoing divestiture programme, the

Kenyan government intends to examine all the alternatives for privatising the operation of the Athi River zone. The World Bank is funding two consultancies through a technical assistance credit (IDA Credit No. 2440-KE) to:

- (i) develop and evaluate options for privatising the EPZ, prepare the necessary documentation for the preferred option, and administer the privatisation transaction in a transparent manner; and
- (ii) in relation to offsite facilities (water supply, sewerage plant, approach roads, electricity transformers and telecommunications connections), to assess the capacity of the suppliers to manage the facilities, evaluate options for the operation and maintenance of offsite facilities, and identify the method for contracting the operation and maintenance of each infrastructure service.

The African Development Bank (ADB) fund feasibility studies for the development of two EPZ sites in Mombasa - one of 35 hectares in Kipevu, and one at Kokatoni of 400 hectares. An ADB mission in December 1993 visited Kenya, prepared an aide memoire recommending the financing of the development of both sites - 35 hectares in Kipevu and a first phase development of 80 hectares in Kokatoni. The total cost of the project in June 1993 prices was estimated at 12.803 million units of account. A decision on the funding from the ADB is still awaited.

#### 4. Institutional Framework

There are three public sector agencies involved in the promotion and develop of exports and investment in Kenya. These are the Investment Promotion Centre (IPC), the Export Promotion council (EPC) and the Export Processing Zones Authority. Each organisation has a different focus, although there are occasional overlapping responsibilities.

The Export Promotion Council was established in August 1992 with the primary objective of assisting exporters and producers of export goods and services (including tourism) to overcome bottlenecks and difficulties facing them in order to increase the level of performance of the export sector. The EPC's main task largely compliments that of the EPZ Authority. The Authority's main focus is the creation of a physical and administrative environment within EPZs in which investors are attracted and within which export manufacturers and service companies can operate efficiently and compete in external markets. In so far as the EPC succeeds in overcoming obstacles and bottlenecks for exporters generally, including EPZ exporters, the task of the Authority is made easier.

The IPC's task is to market Kenya as a location which is attractive for a wide range of investors including domestic and export manufacturers and tourism investors. The main target of the EPZ Authority is export manufacturers. There is obviously some potential overlapping of activity between the IPC and the EPZ Authority. This is recognized by both agencies. As a result there has been a high degree of co-operation between them to avoid wasteful effort. Both agencies have participated in joint investment conferences and any EPZ type enquiries are always passed on by the Investment Promotion Centre to the Authority.

## B. PROJECT JUSTIFICATION

The justification for supporting the EPZ Authority is that:

- (i) There is still a very definite need for EPZs to stimulate a flow of export oriented manufacturing investment into Kenya. Despite the improvements arising from economic liberalisation, export investors are faced with many physical and bureaucratic obstacles in the domestic economy. (To date almost all the new export oriented manufacturing investment is being concentrated in the EPZs).
- (ii) The EPZ Authority has benefited considerably from previous technical assistance. This is evident by the fact that the EPZ programme is well managed and that the number of approved projects which failed to materialise, or ceased to operate is relatively small.
- (iii) The Authority needs to review its operations after 5 years.
- (iv) The EPZ Authority still needs to develop expertise in strategic areas including targeting sectors for promotion and companies within those sectors; the development, planning, management and control (including environmental control) of industrial parks; the refinement of customs organisation procedures and the management of a linkage development programme.

### 1. Problems to be Addressed

There are 6 problems to be addressed.

1. The Authority has been in operation for 5 years. A general review of its activities and policies is appropriate. In particular there is a need to examine:
  - a. the range of support services it provides to investors to ensure that no issues are being ignored and that existing services are being delivered to the satisfaction of the investors. A satisfied group of investors is a major factor in attracting new investors.
  - b. the way in which the Authority conducts its press and public relations activities within Kenya and overseas to ensure that the image of the Authority projected in the media is a positive one which appeals to investors.
  - c. the resources and methods used to promote the EPZ concept among established investors in Kenya and other groups within the country who are in regular contact with or who advise investors. The Authority has made contact with many such groups. Nevertheless, there are large numbers of people in Kenya unaware of the benefits and advantages of an EPZ location. A related issue is the responsibility of the private sector to share the costs and participate in the overall promotion effort.
  - d. the supply/demand situation for EPZ sites and buildings. This issue needs to be monitored closely to ensure that there is an adequate range of sites and buildings available to meet most investor requirements. Nevertheless, there is a need to ensure that there is no unnecessary competition between different EPZ sites or the resources are wasted as developed sites and buildings lie idle for long periods.
2. Targeted Promotion. The Authority needs to develop its expertise in identifying and targeting selected industry sectors and companies within those sectors in



order to attract investors who best meet the needs of the EPZ programme and the Kenyan economy. For this the Authority needs some specialized industry sector personnel to work with the Authority promotion and planning and research staff in analysing and evaluating the suitability of particular sectors. The industry specialists will work with the Authority in developing suitable promotion material including project profiles for presentation to selected companies and groups. The expected end result of their focused promotion activity would be a group of projects with potential for developing strong linkages with the rest of the economy.

3. **Linkage Programme.** The development of linkages between the EPZ and the Kenyan economy does not happen automatically. These links need to be planned, rotated and encouraged. The Authority needs to encourage a flow of information between the EPZ investors and the domestic economic sector. This is a logical consequence of the targeted promotion approach. The Authority is in the process of appointing a person with technical qualifications to develop and manage a linkage programme. This person needs to examine the methods and approaches used elsewhere in developing and managing linkage programmes. There are valuable lessons to be learned for Far East zones in this context. A study tour of selected countries (possibly Malaysia, Singapore and Taiwan) would prove very useful.
4. **Information Technology.** In order to effectively undertake the analysis related to its targeted promotion programme, the Authority needs access to an extensive up to date data base dealing with sectoral trends and developments across a range of industries. The Authority should also be able to make use of modern information technology to make contact with potential investors.
5. **Industrial Park Planning, Design, and Management.** There is a need to develop a range of skills related to industrial park planning and management. Good flexible planning and design will reduce development costs and enable developers to cater for the requirements of a wide range of investors. Good planning and design can also reduce or eliminate any adverse effects on the environment by introducing adequate pollution control standards and treatment facilities at an early stage. A well planned industrial park gives investors a feeling of confidence in the future. Good management also includes lease agreements which give developers power to control investors behaviour in so far as it adversely affects other tenants. The industrial park concept is new in Kenya. Both the EPZ Authority, as the organisation responsible for encouraging private developers and evaluating and approving their plans, and private developers need to build up expertise in this area. This can be done by recruiting an expert in industrial park planning and management to:
  - (a) examine the existing procedures and guidelines which the Authority uses in approving industrial park plans and where necessary advise changes; and
  - (b) review the planning and management practices of the private sector and advise on changes and modifications which would lead to improvements.Study tours by Authority staff to examine practices and procedures in other countries would be useful. Finally, a seminar following the study tours and

expert review for private developers and others involved in the development and management of industrial parks would be valuable.

6. **Customs Administration.** Good customs procedures which allow goods to be cleared in normal circumstances in 24 hours or less is an important attraction for zone investors world-wide. Many investors have expressed dissatisfaction with the service provided by the Customs Administration to date. There is a need to review the EPZ customs operations, including management, procedures and operating instructions. This should be done by a Customs expert with a detailed knowledge of EPZ systems in consultation with the Kenyan Customs Administration and EPZ Authority.

## 2. Expected Output

At the end of the project which will last for 18 months, the EPZ Authority will have the capacity to:-

- (i) Undertake sophisticated and targeted promotion activities, using new information technology systems.
- (ii) Advise developers on all aspects of industrial park design and management and evaluate development plans and proposals, especially in relation to the environment.
- (iii) Plan and manage a linkage development programme.

In addition, the Authority will have reviewed and improved its economic planning capacity; its approach to Press and Public Relations issues and its domestic promotion efforts. The role of the private sector in the promotion process and the contribution expected from the private sector will have been clarified. The EPZ Customs Administration will have been improved. Most importantly, there should be an increased flow of investors attracted to the EPZ programme and those investors should match the requirements of the Kenyan economy.

## 3. Target Beneficiaries

The most obvious direct beneficiaries will be the EPZ Authority in that its capacity to promote, manage and supervise the EPZ programme will have been improved. The private park developers will benefit directly in that ;

- (i) the capacity of the Authority to advise on industrial park development would be improved; and
- (ii) the information available to park developers on planning, designing and management of industrial parks will be improved. Everybody associated with the EPZ programme, but particularly investors and traders, would benefit from improved customs procedures. The Kenyan domestic economy would benefit from improved targeting of investors by the Authority and the efforts of the Authority to promote linkages with the domestic economic sector.

#### 4. Project Strategy

The strategy in this project is to recruit a Chief Technical Adviser (CTA) for a period of 18 months, who would work closely with the Authority in the implementation of the project, including the supervision of the work of a number of short-term consultants and arranging in consultation with the Authority, study tours and a seminar towards the end of the project. The CTA would in addition to project supervision undertake a number of consultancy tasks, mainly in the area of investment promotion, investment support and economic planning.

The short-term consultants would include:-

- (i) 3 industry specialists who would examine in-depth the potential for development of selected sectors under the EPZ programme.
- (ii) An industrial park planner and management specialist.
- (iii) A customs specialist.

Each short-term specialist would work for 3 months in a split mission. Two months would be spent reviewing options and developing proposals. Following a time lapse (of around 6 months) during which the Authority will implement the proposals in consultation with the CPA, the short-term specialists will return to review the implementation and where necessary make adjustment proposals.

The consultancy activity will be supplemented by new information technology equipment (and training in the use of the equipment), study tours for selected zone Authority personnel, and a seminar for the private developers, consulting engineers and others involved in the development and management of industrial parks and EPZs.

The targeted promotion activity and industrial park planning activity should be initiated at the start of the consultancy as these are priority areas and major tasks.

#### C. DEVELOPMENT OBJECTIVE

The main development objective is to strengthen the export manufacturing sector and especially the EPZ sector and the capability of the private sector in relation to the provision of industrial parks.

##### 1. Immediate Objective

The project has a number of immediate objectives. These include:-

- (i) The strengthening and development of the overall capacity of the EPZ Authority to manage and supervise the EPZ programme and in particular target selected industrial sectors; and
- (ii) Improve the Authority's capacity to advise developers, evaluate plans and supervise the management and operation of EPZ industrial parks, and the ability of private developers to plan, design, develop and manage such parks.

## **D. OUTPUTS AND ACTIVITIES**

### **Output 1**

Develop the capacity of the EPZ Authority to identify industry sectors which are especially suited to Kenyan EPZ's taking account of:

- \* the development objectives of the Kenyan government;
- \* the skills of the workforce;
- \* the resources and special advantages;
- \* the support services available in Kenya;
- \* the market opportunities in East and Southern Africa; and
- \* investment trends and opportunities in various sectors.

### **Activities**

- 1.1. Review in consultation with the EPZ Authority the options on the basis of the criteria outlined and select three industry sectors for detailed analysis.  
Responsibility/timeframe : CTA/EPZ Authority : months 1/2.
- 1.2. Draft Terms of Reference for recruitment of 3 industry specialists.  
Responsibility/timeframe : CTA/EPA Authority : month 2.
- 1.3. Recruitment of industry specialists.  
Responsibility/timeframe : UNIDO : months 3/4.
- 1.4. Analysis by industry specialist of selected industry sectors and preparation of reports and recommendations for action.  
Responsibility/timeframe : Industry Specialist : months 5/8.
- 1.5. Implementation of recommendations in 1.4.  
Responsibility/timeframe : CTA/EPA Authority : months 9/14.
- 1.6. Review of progress and implementing recommendations in 1.5.  
Responsibility/timeframe : Industry Specialists : months 15/17.

### **Output 2**

Improve the capacity of the EPZ Authority to source specialised information and use new information systems to promote the EPZ programme.

### **Activities**

- 2.1. Analyse the information requirements of the EPZ Authority and advise on how to use information systems to contact targeted investors and promote the Kenyan EPZ programme. Develop recommendations on the equipment necessary and the training of Authority staff to use the equipment.  
Responsibility/timeframe : Information technology specialists : months 4/5.
- 2.2. Purchase of equipment.  
Responsibility/timeframe : CTA/UNIDO/EPZ AUTHORITY : months 6/7.
- 2.3. Arrange training for EPZ Authority staff.  
Responsibility/timeframe : CTA/UNIDO/EPZ Authority : months 6/7.
- 2.4. Review the operation of the information system.  
Responsibility/timeframe : CTA/IT Specialist/EPZ Authority : month 12.

### **Output 3**

Improve the capacity of the Authority to:

- (i) advise private developers on industrial park planning, design and management;
- (ii) evaluate private developers proposals; and
- (iii) supervise EPZ development.

### **Activities**

- 3.1 Analyse existing procedures for advising developers and evaluating proposals. Review existing EPZ developments from the point of view of planning, design, control (including effluent control) and management. Identify weaknesses and problems and develop proposals to remedy the situation.  
Responsibility/timeframe: Industrial Park Planner/CTA/EPZ Authority : months 4/5.
- 3.2 Arrange study tours for 2 selected EPZ staff to examine all aspects of industrial park planning and management in suitable countries.  
Responsibility/timeframe : CTA/UNIDO : months 6/7.
- 3.3 Review the implementation of proposals and conduct a seminar for private developers and others involved in the design, planning and development of EPZ industrial parks.  
Responsibility/timeframe: Industrial Park Planner/CTA/EPZ Authority. Month 12.

### **Output 4**

Develop proposals for the improved operation of Customs services in relation to EPZ activity.

- 4.1 Review existing procedures and management structures and operating manuals. Examine the validity of investors complaints, and service standards expected by investors and develop proposals where necessary for improved organisation procedures and operating instructions.  
Responsibility/timeframe : Customs Specialist/CTA/EPZ Authority/Customs Administration: months 6/7.
- 4.2 Arrange study tour for the customs administrator  
Responsibility/time frame: CTA/UNIDO : month 8
- 4.3 Review the implementation of proposals made in 4.1 and where necessary amend the proposals.  
Responsibility/timeframe: Customs Specialist/Customs Administration/EPZ Authority : month 13.

### **Output 5**

Improve the potential for developing linkages between EPZ investors and the domestic economy.

### Activities

- 5.1 Identify potential linkage opportunities, constraints and problems which domestic investors may have in availing of the opportunities. Develop proposals and systems to overcome these difficulties. Establish an information exchange for EPZ investors and domestic suppliers.  
Responsibility/timeframe : CTA/EPZ Authority : months 3-9.
- 5.2 Arrange and undertake a study tour by a responsible EPZ Authority member to examine programmes and systems in operation elsewhere, where successful EPZ linkage programmes have been developed and operated.  
Responsibility/timeframe : CTA/UNIDO : month 8.

### Output 6

Review of selected aspects of EPZ Authority operations.

### Activities

- 6.1 Review the existing Press/Public Relations activities of the EPZ Authority and where necessary develop recommendations for improvement.  
Responsibility/timeframe : CTA/EPZ Authority : month 4.
- 6.2 Examine the extent to which the EPZ Authority promoted the EPZ concept among interested groups in Kenya (investors, advisers, financial institutions, trade associations, foreign industry representatives, diplomats, and others) : outline the potential for further promotion : review the resources devoted by the Authority to such activity: develop recommendations if necessary for additional resources (see 6.3) and more intensive promotion.  
Responsibility/timeframe : CTA/EPZ Authority : month 5.
- 6.3 Review the efforts of the private sector to date to promote investment in the EPZ : examine the practices in other countries. Development recommendations on the appropriate input of the Authority/private sector into the promotion effort in the light of the growing involvement by the private sector in developing and managing EPZs.  
Responsibility/Timeframe: CTA/EPZ Authority/Private Developers : months 6-7.
- 6.4 Examine the planning framework of the Authority for monitoring and forecasting the supply and demand for EPZ sites and buildings. Develop proposals to avoid large amounts of unused buildings or sites or wasteful competition among developers. In this context, existing proposals for the development of additional sites and buildings should be re-examined.  
Responsibility/timeframe : CTA/EPZ Authority : month 8.
- 6.5 Review the procedures and services provided by the Authority to support investors during the establishment and operating phases and where necessary develop recommendations for improvement.  
Responsibility/timeframe : CTA/EPZ Authority : month 9.

**E. INPUTS**

<u>Project Personnel</u>	<u>Duration</u>	<u>Cost</u>
1. Chief Technical Advisor	18 months	225,000\$
3. Industry Sector Specialists	3 x 3 months	120,000\$
1. Industry Park Planner	1 x 3 months	40,000\$
1. Customs Specialist	1 x 3 months	40,000\$
Sub-total :		425,000\$
 <u>Study Tours</u>		
2. Industrial Park Engineers	2 x 1 months	20,000\$
1. Linkage Specialist	1 x 1 month	10,000\$
1. Customs Administrator	1 x 1 month	10,000\$
Sub-total:		40,000\$
 <u>Training</u>		
1. Information Technology Operator	1 month	15,000\$
 <u>Equipment</u>		
Information Technology Equipment		30,000\$
Seminar		20,000\$
 <u>Official Travel</u>		
		10,000\$
 <u>Mission Costs</u>		
		20,000\$
<b>Total</b>		<b>545,000\$</b>

**Appendix 3****List of Meetings**

Monday October 2	Briefing UNDP.
Tuesday October 3	Briefing EPZA.
Wednesday October 4	EPZA
Thursday October 5	9.00 Benjamin C. Chesang EPZA 9.30 First Manufacturing (Ali Osman) 10.30 Tri Star (Bandu Udalagama) 11.00 Norbrook 11.30 Eltex (Grahame Whitehead) 2.00 Sameer Industrial Park
Friday October 6	9.00 UK High Commission (Graeme Gibson 2nd Sec. Commercial) 10.30 Italian Embassy (Fabio Scapigliati) 12.00 Korean Trade Centre (Chang- Byung Yang) 3.00 Investment Promotion Centre (Luke E. Obbenda)
Monday October 9	2.00 Tysons Estate Agents (H.M. Mathu)
Tuesday October 10	Moi Day (Holiday)
Wednesday October 11	Mombasa 8.30 Symon Gaitho EPZA 9.00 Visit Proposed Kokotoni EPZ site 10.00 Birch Investments - Clothing Manufacturers 11.00 Coast Industrial Park 12.00 Changamwe EPZ Park 1.00 View proposed Kipevu EPZ site 1.30 Lunch 2.30 East African Molasses Co. Ltd. 4.30 Depart for airport in Nairobi
Thursday October 12	EPZ Authority
Friday October 13	9.00 Ministry of Commerce and Industry (Laurence M. Ndeeri) 10.00 Customs & Excise (Mr. Thuiya) 2.00 Cotex Clothing Manufacturers



		(M. Gosh)
	3.00	Brother Shirt Manufacturers (Previn Chandura)
Monday October 16	9.00	Mugoya Construction and Engineering Ltd. (Abbey K. Misanvu)
	2.00	Lloyd Masika Ltd. - Valuers/Estate Agents (James W. Ruitha)
Tuesday October 17		EPZA
Wednesday October 18	9.00	Kenya Association of Manufacturers (John W. Kuria, S. Ihinga)
	12.00	Ministry of Planning
Thursday October 19	10.00	Export Promotion Council (Peter W. Muthoka, Zakary E. Gichohi)