Kenya - European Community

Country Strategy Paper

for the period 2003-2007

The Government of the Republic of Kenya

The European Commission

GENERAL PROVISIONS

The Government of the Republic of Kenya and the European Commission hereby agree as follows:

(1) The Government of the Republic of Kenya, (represented by Hon. David Mwiraria, Minister for Finance, and the European Commission, (represented by Mr Gary Quince, Head of Delegation,) hereinafter referred to as the Parties, have held discussions in Nairobi with a view to determining the general orientations for co-operation for the period 2003 – 2007.

During these discussions, the Country Strategy Paper and an Indicative Programme of Community Aid in favour of the Republic of Kenya were drawn up in accordance with the provisions of Articles 2 and 4 of Annex IV to the ACP-EU Partnership Agreement, signed in Cotonou on 23 June 2000. These discussions complete the programming process in the Republic of Kenya.

The Country Strategy Paper and the Indicative Programme are annexed to the present document.

(2) As regards the indicative programmable financial resources which the Community envisages to make available to the Republic of Kenya for the period 2003-2007, an amount of € 170 million is foreseen for the allocation referred to in Article 3.2 (a) of Annex IV of the ACP-EU Partnership Agreement (A-allocation) and of € 55 million for the allocation referred to in Article 3.2 (b) (B-allocation). These allocations are not entitlements and may be revised by the Community, following the completion of mid-term and end-of-term reviews, in accordance with Article 5.7 of annex IV of the ACP-EU Partnership Agreement.

(3) The A-allocation is destined to cover macroeconomic support, sectoral policies, programmes and projects in support of the focal or non-focal areas of Community Assistance. The indicative programme under chapter 6 concerns the resources of the A-allocation as well as uncommitted balances of former EDFs, for which no projects and programmes have been identified under the respective National Indicative Programmes. It also takes into consideration financing from which the Republic of Kenya benefits or could benefit under other Community resources. It does not pre-empt financing decisions by the Commission.

(4) The B-allocation is destined to cover unforeseen needs such as emergency assistance where such support cannot be financed from the EU budget, contributions to internationally agreed debt relief initiatives and support to mitigate adverse effects of instability in export earnings. The B-allocation shall be triggered according to specific mechanisms and procedures and does therefore not yet constitute a part of the indicative programme.

(5) The European Investment Bank may contribute to the implementation of the present Country Strategy Paper by operations financed from the Investment Facility and/or from its own resources, in accordance with Articles 3 (a) and 4 of the Financial Protocol of the ACP-EU Partnership Agreement *(see Annex 7 for further details).*

(6) In accordance with Article 5 of Annex IV to the ACP-EU Partnership Agreement, the National

Authorising Officer and the Head of Delegation shall annually undertake an operational review of the Indicative Programme and undertake a mid-term review and an end-of-term review of the Country Support Strategy and the Indicative Programme in light of current needs and performance.

The mid-term review shall be undertaken within two years and the end-of-term review shall be undertaken within four years from the date of signature of the Country Support Strategy and the National Indicative Programme. Following the completion of the mid- and end-of-term reviews, the Community may revise the resource allocation in light of current needs and performance.

(7) The agreement of the two parties on this Country Strategy Paper and the National Indicative Programme will be regarded as definitive within eight weeks of the date of the signature, unless either party communicates the contrary before the end of this period.

Signatures

For the Government of the Republic of Kenya

For the European Commission

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PART A - COUNTRY STRATEGY

EXECUTIVE SUMMARY

Kenya's economic performance in the last ten years has declined. This has been due to stop-go macroeconomic policies, the slow pace of institutional reforms and governance problems, exacerbated by the effects of drought/floods, decline in external resources and low commodity prices. As a result, the slow down in economic growth, coupled with an increasing population, has lead to a decline in per capita income.

Despite the decline in economic performance and recent downturn in fiscal and monetary indicators, Kenya has maintained a certain degree of macroeconomic stability as reflected in low and stable inflation rate, declining interest rate and a relatively stable exchange rate.

Poverty has increased in recent years: about 56 per cent of Kenyans live below the poverty line, of which three-quarters live in the rural areas, but with the numbers of urban poor also rising. Most social indicators show a deteriorating trend. The challenge now facing Kenya is to achieve sustainable economic growth and reduce poverty. The Government's programme to address this challenge is spelt out in the Poverty Reduction Strategy Paper (PRSP) officially introduced by GoK in June 2001. The PRSP outlines the priorities and measures necessary to achieve economic growth and poverty reduction. It is the product of a broad-based consultative process amongst key stakeholders, including the poor.

Following the elections of December 2002, which were described by the EU as an example for other countries in the region, the newly elected Government has committed itself to reconstruct the economy and achieve sustainable development. The Government is finalising an Economic Recovery Strategy which will bring together the Poverty Reduction Strategy Paper launched in June 2001 and its election manifesto.

The objective of this Country Strategy Paper (CSP) is to support the Government in its efforts to achieve higher and sustained economic growth and to reduce the high incidence of poverty. The CSP reviews the Government of Kenya (GoK) priorities and development strategy and proposes the specific contribution that the EC can provide.

On this basis, EC support will be concentrated in two focal sectors identified as priorities in the PRSP: agriculture and rural development, and physical infrastructure with focus on roads. In addition, support will be given in appropriate circumstances to macro-economic and public sector reforms as well as budget support reflecting the PRSP priorities.

1. EC CO-OPERATION OBJECTIVES

In accordance with Article 177 of the Treaty Establishing the European Community, Community policy in the sphere of development co-operation shall foster:

- The sustainable economic and social development of the developing countries and, more particularly, the most disadvantaged among them;

- The smooth and gradual integration of the developing countries into the world economy;

- The campaign against poverty in the developing countries.

These objectives have been confirmed and reinforced in Article 1 of the ACP-EC Partnership Agreement, signed in Cotonou on 23 June 2000, which puts main emphasis on the objective of reducing and eventually eradicating poverty. Co-operation between the Community and Kenya shall pursue these objectives, taking into account the fundamental principles laid down in Article 2 of the Agreement - especially the principle of encouragement of the development strategies by the countries and populations concerned - and essential and fundamental elements as defined in Article 9.

In their Statement of the European Community's Development Policy of 10 November 2000, the Council of the European Union and the European Commission determined a limited number of areas selected on the basis of their contribution towards reducing poverty and for which the Community action provides added value: link between trade and development; support for regional integration and co-operation; support for macro-economic policies; transport; food security and sustainable rural development; institutional capacity-building, particularly in the area of good governance and the rule of law. The Statement also specifies that, in line with the macro-economic framework, the Community must also continue its support on the social sectors (health and education), through the form of sectoral programmes, particularly with a view to ensuring equitable access to social services.

The Treaty establishing the European Community foresees that the Community and the Member States shall co-ordinate their policies on development co-operation and shall consult each other on their aid programmes, including in international organisations and during international conferences. Efforts must be made to ensure that Community development policy objectives are taken into account in the formulation and implementation of other policies affecting the developing countries. Furthermore, as laid down in Article 20 of the Agreement, systematic account shall be taken in mainstreaming into all areas of co-operation the following thematic or cross-cutting themes: gender, environmental and institutional development and capacity-building issues.

The end of the year 2000 marked an era spanning 25 years of EU – Kenya cooperation under the Lomé Convention. It was a partnership that witnessed the evolution of global and domestic developmental challenges which have become increasingly complex. With the coming into force of the new Partnership Agreement in June of the same year, the major challenge is to identify appropriate instruments that will improve the responses of the European Commission's country programme to make them relevant to Kenya's reform framework and maintain consistency with the main policy objectives of poverty reduction and sustainable economic growth.

The above objectives and principles and the national policy agenda presented in the next chapter constitute the starting point for the formulation of the present Country Strategy Paper, in accordance with the principle of national ownership of development priorities.

2. KENYA'S POLICY AGENDA

2.1 Priorities of the New Government

In December 2002, the general elections resulted in the election of a new Government. According to its election manifesto, the new Government's prime goal is to bring about comprehensive political and economic changes in Kenya by :

- Ensuring the completion of the constitutional review process,
- Rehabilitating the national economy,

- Restoring the rule of law,
- Reducing poverty on a sustainable basis,
- Empowering the electorate to make and execute the decisions that affect their lives,
- Promoting a sense of inclusiveness of all citizens of Kenya, and
- Nurturing a sense of nationhood and resistance to divisions based on ethnicity, social class, race or any other consideration.

At the time of writing, the new Government is preparing an Economic Recovery Strategy which will bring together the PRSP and its election manifesto. The following analysis is based upon the priorities of the PRSP as published in June 2001.

The broad agenda of the Kenya Government which is reflected in a series of policy documents aims at addressing the challenges of Poverty Reduction and Sustainable Economic Growth. The Poverty Reduction Strategy Paper (PRSP) is at the centre of the long-term vision outlined in the National Poverty Eradication Plan (NPEP). The NPEP proposes a fifteen (15) year time horizon to fight poverty in the country. The PRSP implements the NPEP in three years rolling plans. In between the PRSP and NPEP is the National Development Plan, which offers a 7-year horizon of development stipulating policies of a broader nature to be implemented in the medium-term.

The adoption of the Medium Term Expenditure Framework (MTEF) provides the linking of policy, planning and budgeting and it aims at improving the quality of expenditure and the shifting of resources towards pro-poor activities and programmes.

2.2 Overall objectives of the PRSP

The guiding principles of the PRSP are:
- Giving voice to the poor,
- Participation and ownership,
- Transparency, openness and accountability,
- Equitable distribution of natural resources and development initiatives.

The objectives of the PRSP are:
- Linking policy, planning and budgeting
- Identifying national development objectives and priorities
- Quality expenditures leading to efficiency gains
- Harmonisation of Financing framework, and
- Monitoring and evaluation.

Within the above objectives, in the next three years GoK aims to:

- ***Implement a sound macro-economic policy through an appropriate fiscal strategy*** outlined in the PRSP and in subsequent fiscal strategy papers.

- ***Increase food security, rural productivity and raise income opportunities for the poor*** by targeted interventions to make national growth more evenly spread across all sectors of the economy and all members of society, e.g. improving extension services to agricultural smallholders; supporting private agricultural marketing systems; promoting rural employment; protection of natural resources, rehabilitation of physical infrastructure, including electricity supply and labour intensive road schemes.

- ***Increase real per capita GDP growth*** to 3.3% p.a. by 2004, increase foreign exchange reserves, and maintain the current account deficit at sustainable levels, through better allocation of public resources, prudent fiscal and monetary policy and a pro-active role in facilitating the expansion of the private sector.

- ***Improve Governance*** by focusing on enhancing accountability and transparency of public financial management, strengthening oversight bodies and budget planning and execution, and the fight against corruption.

- ***Improve the quality of life*** by focussing resources on improvements in basic social services that are most needed by the poor, in particular education, health and water supply, housing, and access to markets, in particular through rural roads.

- ***Improve equity and participation*** by ensuring that there is a more equitable distribution of income between citizens and of economic activity among regions.

2.3. PRSP sectoral priorities

The Government of Kenya has carried out a countrywide stakeholder consultation in the process of preparing the PRSP. The objective of the consultative process was to identify the constraints/problems affecting the stakeholders and to identify their priorities. The following sectoral priority list is the outcome of a comprehensive national consultative process involving public debates and national stakeholders' fora in all districts of Kenya, including donor participation.

- Agriculture and Rural development,
- Human Resource development,
- Physical Infrastructure (in particular roads, water & energy),
- Trade, Tourism and Industry,
- Public Safety, Law and order,
- Public Administration
- Macroeconomic policy.

The conclusion of the PRSP consultations is that **Agriculture and Rural Development** is the top ranked national priority. Eighty per cent (80%) of Kenyans live in rural areas which are characterized by low agricultural productivity, low incomes, poor access to credit, limited employment opportunities and poor economic and social infrastructure. The performance of agriculture is constrained by declining household share of productive land as a result of land subdivision, limited utilization of the Arid and Semi-Arid Lands (ASALs) and the absence of appropriate dry-land farming technological packages

The Government aims to increase agriculture sector growth to 6% p.a. The Government recognizes that the agriculture sector is the engine of growth and will concentrate its efforts on investing in public goods and in creating an enabling policy environment for private sector operations. Priority actions will cover two broad areas (i) creating opportunities for rural communities and the private sector to operate and (ii) accelerating policy and institutional reforms, including decentralisation to local government, local authorities and stakeholder/farming institutions.

Investment in **Human Resource Development** will improve Kenyans' capacity to participate more effectively in development. In Education, the Government's priority is to ensure affordable and equitable access and free primary education. The objective for the Health sector is similar, to enhance equity, quality accessibility and affordability of health care. Health resources will be shifted towards preventive/promotive/rural health services.

Without doubt, **HIV/AIDS** presents a major threat to Kenya's economic and social development. HIV/AIDS prevalence rate stands at 13% of the population, mainly in the 15-49 age bracket. It is estimated that about 700 persons die every day from AIDS related diseases. An additional and even more serious practical problem precipitated by the pandemic is catering for an increased number of orphans given the widespread collapse of traditional extended family options. Government policy in this area emphasises the promotion of safe sex, prevention of mother to child transmission, blood screening and strengthened national capacity to respond to the epidemic through improved funding, training, sensitisation and awareness. The Government has established a task force to develop a strategy and new legislation to introduce Social Health Insurance to address equity healthcare for poor people in the country.

The provision of quality **Infrastructure** is essential if poverty reduction and economic growth targets are to be met. The Government's immediate focus is on the maintenance, rehabilitation and reconstruction of existing infrastructure especially to facilitate delivery of inputs, marketing of produce and general trade. In the long term, the enhancement of competition and involvement of private capital will also be promoted.

The **Trade, Tourism and Industry** sector makes a significant contribution through employment creation and foreign exchange earnings. The Government's role in this sector is to improve an enabling environment for the private sector to operate effectively.

Public Safety, Law and Order has a direct correlation with investment and growth and thus with the incidence of poverty. Within the framework of the PRSP, the Government targets to establish an improved regulatory framework for the legal sector maintenance of law and order, the administration of justice and enhancement of security.

Efficient and effective **Public Administration** is also critical for economic growth and development. The Government will therefore accelerate ongoing reforms of the public service including the privatization programme, improving the governance/management of quasi-public institutions/cooperatives including measures to deal with corruption.

In terms of Pro-Poor growth policies, GoK policy will focus on promoting access to markets and market opportunities for the poor; improving the effectiveness of public resources geared towards poverty reduction; enhancing the security of the poor; allocating increased resources on human development.

3. AN ANALYSIS OF THE POLITICAL, ECONOMIC AND SOCIAL SITUATION

3.1. Political situation

Democratic participation: The General Elections of 2002 demonstrated a notable and peaceful democratic process in Kenya based on principle of universal suffrage, free vote, a multi-party system and freedom of access to political activities. Nevertheless, there is widespread agreement that the current constitution is deficient in a number of respects. Government and opposition parties, as well as civil society, have agreed that the constitution needs to be revised to meet future challenges. Following the enactment of the Constitutional Review Act and establishment of the Constitutional Review. Commission, the constitutional review was well advanced by the time of the general elections. The new government has given assurances to complete this process by June-July 2003.

In addition, civil society in Kenya has developed rapidly, and is now vibrant while there is also a well-developed private sector as well as an extensive network of economic and social partners contributing to the reinforcement of the democratic system.

Good Governance : Corruption, nepotism and lack of accountability have been major constraints to sustainable and equitable development. The previous administration had publicly committed itself to a policy of "zero tolerance" to corruption but initiatives taken to address this problem have derailed by important set backs and no real progress was made.

The new Kenyan administration has immediately placed good governance and, in particular, the fight against corruption as its central priority. First measures taken include the establishment of an office for Governance and Ethics directly under the Office of the President whilst a programme to re-evaluate various public projects and initiatives has been launched. In parallel, key Bills[2] aiming to implementing an independent anti-graft authority and to providing a legal frame against economic crimes and corruption were published. The passage of these Bills by Parliament is important to enable the GoK's programmes with the IMF and major donors to get back on track.

Human Rights: Significant efforts have been made to maintain respect for human rights and freedom of speech in Kenya despite some shortcomings. The constitution provides for all the basic rights, but with certain limitations. Legislative gaps are being addressed through the recently enacted Children's Act, presentation of the National Commission of Gender and Development Bill to Parliament, the passage of the National Commission on Human Rights Bill by Parliament in June 2002, and the on-going preparation of the National Action Plan for the Promotion and Protection of Human Rights. With the re-establishment of a multi-party system, restrictions on political meetings have been lifted and there is a free press.

Rule of Law and Internal Security: Under the present constitution, the Head of State appoints the Chief Justice, whilst the appointment of Judges of the Court of Appeal and High Court are made by the Head of State on the recommendation of the Judicial Services Commission. The constitution further accords these officers security of tenure. However, the effective administration and delivery of justice is

[2] The Constitution of Kenya (Amendment) Bill will, among other things, lead to the setting up of the new anti-Corruption Authority after the constitutional problems met by previous KACA (Kenya Anti-Corruption Authority). The Anti-Corruption and Economic Crimes Bill will set, inter alia, the rules under which the Anti-Corruption Authority will work and the Public Officer Ethics Bill will bring further accountability to public workers conduct.

hampered by poor facilities, unattractive conditions of service, and corruption. The NARC government has placed judicial and police reforms among its main concerns.

Such reforms will also contribute to tackle internal security issues which increasingly affect Kenya. Other contributing factors for the raising crime rate include growing poverty, influx of refugees arising from conflicts in the neighbouring countries, and inflow of small arms and their use in the Kenya.

Regional dimension of conflicts: In contrast to many of its neighbouring countries which have been afflicted by internal or external armed conflict, Kenya enjoys relative stability and is seen as a regional stabilising factor. It is also host to a large number of refugees from the sub-region. Kenya has been at the forefront of recent efforts to resolve the conflicts in Sudan and Somalia through the regional initiatives undertaken by the Inter-Governmental Authority on Development (IGAD) and is willing to further contribute to the region's political and economic stabilisation.

Political dialogue: the EU and GoK are engaged in a political dialogue which covering areas of mutual interest within the scope of the Cotonou Agreement, including such issues as democratic principles, human rights, constitutional review, economic and structural reform, governance, environment, security and regional affairs. The dialogue got underway in February 2002 and it is the intention of both partners to enlarge and systematise such regular exchange of views.

3.2. Economic and social situation and poverty in Kenya ([3])

- **Economic situation, structure and performance**

Economic growth averaged 6% p.a. during the 1960s and 1970s, but more recently, economic growth has declined from 4.6% in 1996 to -0.2% in 2000, 1.2% in 2001 and a similar level in 2002. Although some improvement is expected for 2003 and 2004, GDP growth will probably fall short of the official target (3.3%). Despite an expected better performance in key sectors (agriculture, tourism) and an improvement of net transfers, Kenyan expectations in social areas will add extra pressure on public expenditure. To face the challenge, economic reforms including the fight against corruption will be crucial to increase public revenue and re-establish economic operators and donors' confidence.

The trend of decline in economic performance has been due to stop-go macroeconomic policies, slow pace of institutional reforms, and governance problems, exacerbated by recurrent droughts/floods, low commodity prices, high population growth and the impact of the large refugee population due to regional insecurity. Additional factors associated with the more recent decline include net capital outflows, reduced inflows of concessional aid and declining levels of investment and productivity. As a result, Kenya has been unable to maintain basic public infrastructure and services which it developed over past decades.

In terms of economic structure and sectoral contribution to the GDP in 2001, Agriculture remains the major contributor, with 24.1%, followed by Manufacturing 13.0%; Building and Construction 2.4%; Trade, Restaurants and Hotels 12.7%; Transport, Storage and Communications 6.2%; Financial Services 10.6%; Government Services 14.7%; Other Sectors 16.5%.

Kenya thus has a reasonably diversified economy. Its export earnings are spread across several agricultural crops, both traditional and new, together with manufactured goods and tourism. There is

(3) Selected social and economic indicators are set out at Annex 2

certainly potential for export led growth. For example, although the overall trade deficit increased during 1990-99, the value of exports to the EU rose by over 50% over the same period. Ninety per cent (90%) of Kenya's exports to the EU consist of horticultural products (flowers, vegetables, fruit), tea and coffee. Kenya is one of the world's largest exporters of cut flowers, pyrethrum and the third largest exporter of tea.

Restructuring and liberalization of the tea industry has been successfully undertaken. Liberalization and development of appropriate policies for other traditional exports (coffee, livestock, cotton, sisal, and pyrethrum) are at an advanced stage. However, these sectors are still hampered by poor price structures.

The 1999/2000 drought led to shortages in electricity and low agricultural production. This also led to increased cost of inputs which further weakened the manufacturing and services sectors, with negative ripple effects on overall economic activity. The droughts of the past decade were a recurrent event, for which Kenya was not fully prepared, and thus for which an emergency response was required. This highlighted Kenya's weaknesses in disaster preparedness and inadequate food security policy.

According to the PRSP consultation process, another major factor in declining economic performance and rising poverty in Kenya is the poor condition of the road network, which makes access to markets, hospitals, schools, etc, very difficult or even impassable.

To achieve benchmarks agreed with the IMF and the donor community, the new Kenyan administration has committed itself to deliver on improvements in the regulatory and institutional framework and on sustainable public sector reforms, which are crucial for improving economic activity and restoring growth.

- **Social development and poverty in Kenya**

During the 1970s and 80s Kenya had one of the fastest growing populations in the world averaging 3.8%, although the current population growth rate has declined to around 2.1% p.a. The population has grown from 8.6 million at Independence in 1963 to about 31 million today.

Over this period, the performance of the economy has been particularly inadequate in generating new jobs, which has resulted in **rising levels of poverty**: around 56% of the population now live below the poverty line, compared to 45% in the mid 1990s, and 30% in the early 1970s. Whilst most of the poor reside in rural areas, urban poverty is intensifying with the growth of slums/informal settlements, urban unemployment and increasing social problems such as crime and insecurity, street children, prostitution, drug abuse, disease etc.

According to the PRSP consultations, local communities invariably indicate the following as the main causes of poverty: low agricultural productivity and marketing, insecurity, poor governance, poor or lack of roads, the cost of health and education, HIV/AIDS, the gender imbalance and disability (see Annex 1).

Kenya faces a multiple **land problems,** many of which are aggravated by **poor environmental practices.** This further impacts in the poverty situation: Eighty per cent (80%) of Kenya's land area is arid or semi arid and supports 25% of the population. In addition to the scarcity of arable land, issues related to land tenure, misuse of natural resources including water, low productivity arising from land subdivision and deteriorating soil due to cultivation methods.

Kenya experiences **inadequate supply of water** to sustain human, livestock, crops, wildlife and individual demand. This is primarily due to high population pressure and inadequate management of existing water resources coupled with limited water resources and poor policy implementation practices.

Kenya had built a relatively well-developed **health sector** during the 1970s, and some of the country's health indicators were amongst the best in Sub-Saharan Africa. However, the health sector has experienced a decline in performance since the 1980s, both in terms of the services provided and the health status of the population. For instance the maternal mortality rate, under 5 mortality rate and infant mortality rate have all shown significant increases since 1989. Life expectancy has also declined from 59 years in 1991 to 49 by 1999. These changes have in most cases been due to the rapid increase in cases of HIV/AIDS, the overstretching of the health services by the rapidly increasing population and refugees and the impact of the sectoral reforms in the sector, as changes occurred requiring cost recovery at a time when poverty levels were increasing.

HIV/AIDS has become a development crisis in Kenya. The prevalence rate rose from 11% in 1997 to 13.9% in 1999 before declining to 13% in 2001. If this scenario continues, the number of people infected with HIV/AIDS in Kenya will reach 3 million by 2010, and another 3 million will already have died. Given that 80% of these deaths are expected to occur among the population aged 15-49, it has been estimated that GDP in 2015 could be 15% lower as a result of HIV/AIDS and per capita incomes 10% lower.

Kenya has achieved a significant progress in the **family planning** programme. In the period between the 1970s and 1998 the fertility rate has fallen from 7.9 to 4.7 children per woman and the contraceptive prevalence rate has increased from 7% to 39%. The challenge now is to sustain these gains.

A major area of concern is the **labour** market, given the low level of employment creation and existing under employment. This, coupled with the need to improve productivity, require to be addressed.

Kenya has had one of the best **education systems** in sub-Saharan Africa. However today, the Kenyan education system faces serious challenges, characterized by declining enrolment rates, poor quality, and inefficiency. These problems arise from a combination of (i) Kenya's deteriorating economic situation and (ii) low budgetary provisions for learning and teaching materials, as well as inadequate institutional management capacity at the school level. One of the first measures introduced by the new Government in January 2003 was free primary education, which has resulted in thousands of additional children returning to school.

Women continue to suffer disproportionately from poverty. Cultural and traditional practices often inhibit equal access to resources, including land. This contributes to the higher incidence of poverty in female-headed households as they have limited access to productive resources. The lower status of women also has a negative impact on the vulnerability of children, for whom women are the main providers and carers.

- **Structure of public sector finance**

The Government expects economic growth to increase from the low rates of the previous two years due to efficient allocation of resources, rising investment and improved export earnings. The fiscal strategy reflects a more conservative revenue outlook than in past years especially after the reform and liberalisation of key sectors and the inclusion of other service providers who take up some of the service delivery. However the projected revenue flows especially concerning privatisation proceeds and the availability of external financing are low. Revenues are expected to increase, however, as a result of the improved administration of taxation and enhanced public financial management.

Nevertheless, development and operating expenditure (i.e. non-wage and non-debt commitments) will be under political pressure. The GoK faces a major challenge to downturn the rising public deficit which will be higher than the initially budgeted 4% of GDP for 2002-2003. In addition, the persisting problem of pending bills is further cause for concern.

3.3. External environment including regional cooperation agreements

- **External debt**

Kenya's external debt, remains high at US$ 4.8 billion or 38% of GDP while the debt service ratio is 19%.

- **Trade** ([6])

Kenya's trade position has been worsening: the trade deficit rose from US$ 1,124 million in 1995 to US$ 1,814 million in 2001. (Exports: US$ 1,879 million; Imports US$ 3,693 million).

The market-destination of Kenya's exports is narrow, with over 30% of total exports going to Tanzania and Uganda and 30% to the European Union. Despite that the EU is an important trading partner, with Kenya's exports totalling € 907 million in 2001, and imports of € 960 million, there is a significant trade imbalance in favour of the EU. New WTO-compatible trade arrangements must now be established under the Cotonou Agreement. This implies the end of non-reciprocal trade preferences by 2008 which will have important consequences for the Kenyan economy and exports.

- **Regional Cooperation Agreements** ([7])

Kenya has entered into multilateral, regional and bilateral trade agreements and is a signatory to the ACP-EU Partnership Agreement. It is a member of the East African Community (EAC), of COMESA, the Inter-Governmental Authority on Development (IGAD) and of WTO.

3.4. Assessing the process of reform, the sustainability of current policies and medium-term challenges

- **Economic and public sector reform programme and the PRSP**

On **macroeconomic policies**, the Kenyan authorities have maintained stability despite the 2002 downturn in public finances, but against a background of low real economic growth. However, disbursement under the IMF reform programme has been suspended since 2001[8]. This has been followed

([6]) Provisional figures provided by the Economic Survey 2002, page 104.

(7) see Annex 4 for more details

8 Following the general election of December 2002 and the measures taken by the new Kenyan administration, dialogue resumed with the IBW and the international community in general with a view to re-establish co-operation in areas where it had been suspended, including general budget support.

by a decline in external financing and a corresponding increase in domestic borrowing to finance the budget deficit, putting pressure on interest rates and reducing credit available for the private sector.

Key to future development in Kenya is the successful implementation of the economic and public sector reform programme, notably measures to **improve efficiency and public accountability**. The disbandment of the Kenya Anti-Corruption Authority (KACA) after a successful court challenge has put back this process. However, the new Kenyan administration is in the process of re-establishing an independent Corruption Control Authority. To this respect key anti-corruption Bills have been tabled in Parliament. The Anti-Corruption and Economic Crimes Bill that will set the rules under which the Anti-Corruption Commission will work and the Public Officer Ethics Bill aiming to bring further accountability to public workers.

Accelerated progress in **public sector reform** is essential if more resources are to be made available for core poverty programmes. A key structural reform achievement during this period was the first phase of civil service retrenchment (23,000 persons retrenched) with donor support. The second phase of the process has been delayed. Public sector reform also has an important role to play in creating a more favourable environment for private sector activity. The Government's actions in this area are guided by the **'**Strategy for Performance Improvement in the Public Service' (SPIPS), published in March 2002. The strategy was elaborated with EC technical assistance and provides a framework for a comprehensive reform programme across the entire range of the public sector.

The SPIPS incorporates a detailed Action Plan covering civil service reform, including further ministerial and parastatal rationalisation, retrenchment, pay and benefits reform, training and capacity building, and results oriented management. In addition, the strategy includes a programme for Public Financial Management reform, including the deepening of the MTEF process, reform of the key internal audit bodies and the introduction of an Integrated Financial Management System.

The SPIPS also highlights the need to build on recent reforms under the Local Government Reform Programme which has introduced the Local Authority Transfer Fund (LATF) and the associated Local Authority Service Delivery Action Plan (LASDAP). The LATF transfers 5% of total income tax revenues as grants to local authorities for development purposes. As a condition of LATF payment, local authorities are required to elaborate their LASDAP in close consultation with their local communities. This process provides opportunities for promoting greater community involvement in the local planning process and is the cornerstone of the Government's evolving policy on decentralisation

- **Assessing the PRSP:**

The strongest asset of the PRSP is that it is the product of a broad-based and an all inclusive process of national district and community consultations. On January 2003 a mission of IMF to Kenya has announced a possible revision of some PRSP objectives and their rescheduling in order to take into consideration, inter alia, some macro-economic shortcomings due to the 2002 electoral year. Nevertheless, the basic principles, objectives and sectoral priorities all reflect the outcome of these consultations and remain an appropriate framework for Kenyan long term development strategy.

In assessing the success of PRSP, three particular issues are of concern to the European Commission:

- Economic growth: there can be no reduction in poverty nor significant job creation without sustained economic growth at rates of up to 7% p.a. This in return will require major efforts by GoK not only to achieve long-term macroeconomic stability, but to create an enabling environment for private sector activity by accelerating public sector reforms, promoting privatisation and deregulation of markets, establishing a transparent, regulatory framework conducive to private sector investment, thus reducing transaction costs and improving incentive structures.

- Sectoral strategies: the PRSP appropriately focuses on poverty reduction strategies in identified key sectors. The PRSP Action Plan is addressing these issues in greater detail. It will be essential for the credibility of the PRSP that the Government takes the lead by more clearly reflecting the PRSP priorities in its Medium Term Expenditure Framework.
- Governance: the PRSP correctly recognizes the critical importance of improving governance and the Government has now set out a programme to address governance issues. It is essential that the enactment of the legislation is quickly followed by the establishment of effective institutional structures.

a) Sustainability of current sectoral policies:

The following sections assess the sustainability of policies within the priority sectors as identified by the PRSP***:***

(i) Rural development policy:

The PRSP targets a long-term growth rate of 6% for the agriculture sector as being the basis for rural poverty reduction. The GoK's specific role in the strategy therefore focuses on providing the enabling environment for private sector growth. Essentially, this concerns providing the framework for an appropriate level of provision of public goods and services. In this context, the PRSP consultation process identified a number of factors as being major constraints to rural development, including:

- Inadequate extension services
- Poor state of rural infrastructure
- Poor marketing and distributions systems
- Limited Water supply
- Inadequate animal health services
- Environmental management
- Quality and standards enforcement
- Lack of a land use Policy and poor land tenure systems in some areas,
- Lack of a fully developed rural industrialization to provide alternative employment for rural people,

In addition, the PRSP clearly recognizes the decline in service delivery, as being a significant factor in contributing to poverty Kenya. The PRSP consultation process also revealed that communities are insufficiently involved in the local development planning and coordination process. Moreover, the consultations attributed this to the effective 'dis-empowerment' of local government by central government. Against this background, the PRSP resolves to strengthen t community participation in local development planning and implementation.

The final draft of the Kenya Rural Development Strategy (KRDS) ([9]) recently developed by the rural sector ministries further elaborates on the PRSP and proposes the following broad categories of policy actions and interventions (see Annex 5 for more details):

- Empowerment of rural communities; ([10])

([9]) Final KRDS draft awaits GoK's formal adoption.
(10) Immediate priority will be given to the rehabilitation of rural infrastructure, starting with access roads repair and maintenance, provision of electricity to markets and market centres and construction and maintenance of water supply and dams, using locally raised funds and grants from Central Government

- Undertake further policy and institutional reforms and promote stakeholder participation in the identification, planning, implementation and maintenance of development initiatives;
- Further decentralisation of rural service delivery with the emphasis on an enhanced role for Local Authorities in rural development planning;
- Enhanced public security and an effective response to droughts.

The above will entail implementation of measures to:

(i) Increase Rural sector production and productivity for food security, raw materials for industrialization, protection of the environment and wildlife, increase employment opportunities

(ii) Improve policy, institutional and legal framework that supports the participation of all stakeholders

(iii) Improve rural sector physical and social infrastructure to facilitate delivery of input to the farming community and exports to markets, trade, tourism, education, health and the role of women

(iv) Improve governance and management of the farmers institutions, public security and the rule of law

(v) Establish a mechanism for rapid flow of development financing for rural development.

The KRDS also recognises the need to continue with the liberalisation of key agricultural sub-sectors and, in this context, identifies a wide-ranging programme of policy, legislative and institutional reforms to be undertaken. This reflects the policy of gradual government withdrawal from much of the trading/production or direct participation and regulatory responsibilities now devolved to the respective commodity boards e.g. Coffee and Sugar Boards. More fundamental liberalization will, however, require the development of stakeholder capacity to manage the liberalized functions and their participation in the regulatory model based on self- regulation. Progress in this area is likely to be constrained, however, by the reform capacity of the various ministries involved in the policy development, legislative process and inadequate financing due to the sheer size of the workload.

The PRSP also recognises the role of land reform policies in enhancing Rural Development. Fundamental reforms will be initiated during the PRSP period to provide for improved land administration, management and ownership.

The National Policy on Water Resources Management and Development was passed by Parliament on 29th April 1999. It recognises the need for active participation of private sector in water supply development and management. It encourages the local communities to play a more active role in managing rural water resources and supplies. The policy also encourages local authorities to prepare to take over urban water supplies under their jurisdiction.

Two strategy papers have been prepared in order to operationalise the above policy:-

(a) Water supply services strategy paper proposes that water supply operations be under Water Service Boards mandated to appoint service providers in private companies, Local Authorities, Institutions etc.

(b) Integrated Water Resources Management Strategy Paper.

The revised Water Act incorporates the policy and the two Water Strategy Papers.

The revised forestry policy must also be brought into effective operation. It recognises promotion of various stakeholders: Government agencies, NGOs, research institutions, local communities in the sector management and development. The new Government has already taken steps to stop illegal encroachment of forest areas.

(ii) Human resource development policies

- Health Sector Policy:

The declining trends in most health indicators and scarcity of resources to cater for the ever increasing demand for health services underscore the need for health sector reforms, including organizational reforms in the health sector. The long term vision of the Ministry of Health (MoH) as set out in the "Health Policy Framework 1994", aims at achieving improvements in the health status of all Kenyans through the implementation of six key objectives : (i) equitable allocation of government resources to reduce disparities in health status; (ii) increased cost effectiveness; (iii) continued management of population growth; (iv) enhanced regulatory role of Government; (v) creation of an enabling environment for increased private sector and community involvement; (vi) increased and diversified per capita financial flows to the health sector.

This has been restated in 1999 in the five-year National Health Sector Strategy Plan (NHSSP) (1999-2004) to address the reform needs of the entire health sector in the context of the wider economic and public sector reform process. The NHSSP sets out a reform agenda for providing quality curative, preventive, and rehabilitative health care with major emphasis on the six essential packages([12]). A multi-donor (including EC) Health Sector Reform Programme is now under implementation.

The implementation of NHSSP is on-going and requires further financial support focused on increased budgetary allocation and targeting of funds to core activities.

A major concern, which is being addressed on a multi-sectoral basis, is the increasing impact/incidence of HIV/AIDS. A National Aids Control Council was established in 2000 and developed the National HIV/AIDS Strategic Plan 2000-2005. Budget resources for preventive and curative health interventions are insufficient. Donors, including the EC, contribute in the provision of scarce essential drugs and on aids prevention/awareness rising. A joint AIDS programme review to assess progress made towards delivering the Strategic Plan and to identify main priorities and milestones of achievement for the 2002-2003 financial year has been carried out with development partners. However, given the size of the pandemic, GoK's budget for HIV/AIDS activities is unlikely to increase sustainability in the medium term.

- Education policy:

The new Government stresses the importance of education as part of its overall poverty reduction strategy. The PRSP sets out the following targets for the sector:

- increased primary school enrolment to achieve education for all by 2015.
- improved transition rate from primary to secondary education.
- improved retention, promotion and completion rate through reduced drop out and repeat rates, particularly at primary level.
- improved equity in education, with particular emphasis on less developed areas, girls and learners with special needs.

The new Government's decision to reintroduce free primary education from January 2003 has resulted in a large increase in primary school enrolment. This shift in the cost burden from households to the public

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(12) The six health priority packages are (1) Reproductive Health (2) HIV/AIDS & TB (3) Malaria (4) Integrated Management of Childhood Illnesses (IMCI) (5) Expanded Programme on Immunization EPI (6) Communicable Disease Control (CDC) e.g Typhoid and Cholera).

sector, together with the need to improve education quality, will require significantly increased public expenditure on education, together with improved public spending efficiency.

Already, public expenditure on education represents one-third of the Government Budget and 6.5% of GDP. Most expenditure is, however devoted to teachers' salaries, leaving little for school operations and maintenance. Comparison with other African countries suggest that Kenya's education system operates at high unit costs and that efforts need to be made to improve efficiency of public spending.

(iii) Physical Infrastructure policy:

In recent surveys, including the PRSP consultations, farmers, traders, processors, large and small manufacturers consistently cite infrastructure, in particular transport deficiencies as a major factor contributing to Kenya's lost productivity and a major obstacle to economic recovery and sustainable development. In the absence of a comprehensive transport policy, GoK is addressing some shortcomings on a sub-sector basis **(Annex 4**). With the reform programme under the Change Initiative started in 1999, privatisation of parastatals in charge of telecommunication, ports, airports, as well as the establishment of an independent Roads Board are envisaged as major activities. The Water Act was debated in Parliament and was passed in June 2002. The passing of the act will stimulate development, management and provision of water supplies and sanitation in the country by bringing on board greater private sector participation in the sub sector. After floating bids for privatisation of Telkom Kenya, the Government could not secure a suitable investor to take over the management and operations of the parastatal hence the delays in completing the transaction. The Government has drafted a privatisation Bill aimed at streamlining and accelerating the implementation of the privatisation programme. Under the Bill the Government will ensure that the objectives of the programme are clearly defined, prior to commencement of each transaction.

- Roads:

There is now a road maintenance/rehabilitation backlog which will require substantial donor funding. The rural/district road network is particularly poor and the PRSP consultations identified this as a major constraint to agriculture and rural development generally.

In recent years, Kenya has assembled many of the building blocks necessary to develop sustainability in the road sector, notably:

- A Strategic Plan for the Sector
- An appropriate strategy for rehabilitation and maintenance of the rural road network
- Axle load and weight restrictions enforced with a reasonable level of compliance and a substantial reduction in overloading
- Annual road maintenance funding progressively increased to more than US$ 100 million p.a in 2001through the introduction of a Road Maintenance Levy Fund ([13])
- An executive Roads Board to oversee the road network and coordinate its development, rehabilitation and maintenance
- A well established domestic road construction industry and substantial engineering capacity

Despite these measures the road sector is increasingly identified as a primary constraint to development. Given the size of the network, its condition has been deteriorating over the years due to inadequate

(13) Funded by a levy on fuel, previously administered by the Treasury and implemented through allocations to the Roads Department and Local Government, this fund will be under the authority of the Kenya Roads Board (KRB) created by law on 1.7.2000 to oversee the development, rehabilitation and maintenance of Kenya's road network through the Kenya Roads Board Fund.

funding, despite the fact that an average of Kshs 8.6 billion p.a. is collected through the fuel levy to maintain trunk roads.

Efforts by GoK will be required to adopt a coherent, sustainable transport sector policy and strategy to effectively contribute to national and regional development. Government needs to bring the Kenya Roads Board into full and effective operation; establish efficient autonomous Road Agencies in addition to strengthening their capacities.

- Road Safety:

The Government in May 1982 established the National Roads Safety Council. It was mandated to formulate Road Safety improvement policies and programmes and coordinate road safety activities undertaken by various organisations and departments. The Government intends to reactivate the National Roads Safety Council, in the medium term, to oversee Road safety matters while, in the long term, GoK intends to establish a Kenya Roads Safety Authority to oversee safety matters pertaining to road transport services, introduce new generation Smart Card Driving Licenses, provide technical assistance to Traffic Police and the Director of Vehicle Inspection and train personnel working on road safety related programmes. Also, to eliminate unworthy vehicles on the roads, GoK intends to introduce compulsory inspections for all types of vehicles by private operators. The Government has already published the Traffic (Amendment) Bill 2001, which is expected to address most of these matters.

- Kenya Railways (KR):

Railway transport is the second most important mode of transport after road transport for both freight and passenger services. The Government has been undertaking various reforms to ensure that the rail service plays its rightful role in the economic development of the country. These reform measures have included staff rationalization, privatisation of catering services, contracting out locomotive maintenance and installation of a rail tracker system for monitoring movement and performance of trains. Despite these efforts, Kenya Railways is still faced with various challenges and problems such as insufficient investment, the use of outdated and inefficient rolling stock, old rail track and lack of maintenance/renewal of old railway lines, outdated communication systems and poor management in the past. These have led to progressive decline of railway transport services. However, it is worth acknowledging that drastic management changes, focusing on improved service delivery and other measures introduced such as operation of block trains between Mombasa and Kampala, resulted in improved performance (with freight transport increasing by 40% in 2000) and a reduction of turnaround time from 28 days to 10 days and transit time between Mombassa and Kampala from 14 days to 4 days.

Continuing efforts concentrate in particular on improving operations, decreasing costs and improving earnings. This will increase capacity and capture the lucrative traffic for North West Tanzania, Rwanda and Uganda. The medium-term strategy is to privatise KR through unitary concessioning.

- Ports:

Marine transport is cost effective for transportation of heavy/bulky agricultural and other products. The port of Mombasa is important not only for Kenya, but also for transit cargo to its landlocked neighbours: Uganda; Burundi; Rwanda and the Democratic Republic of Congo. The performance of the port has not been optimal due to inadequate facilities, outdated equipment and inefficient management. Traffic through the container terminal has already exceeded its design capacity of 250,000 TEUs per annum.

GoK has introduced various measures aimed at improving the performance of the port including appointment of new management, streamlining and centralising of clearing procedures and replacing many of the old equipment. The Government medium term strategy is to privatise the port of Mombasa.

- Air Transport:

This is the major transport mode for tourists, for high value exports and perishable goods and acts as a lever for regional integration. The privatisation of Kenya Airways (KLM as important share-holder), the fleet expansion strategy and focused marketing have achieved good results on local, regional and international routes. With the opening of the new Air Cargo Centre, Nairobi has greatly enhanced ground operations and storage of perishable export products and general cargo. All three international airports (Nairobi, Mombasa and Eldoret) have sufficient spare capacity to handle increased volumes but need to be more focused on maintenance and service-orientation.

Kenya Airport Authority (KAA) which manages the airports aims to improve airport facilities and landing strips through maintenance and equipment so as to enhance the quality of air services. The GoK will de-link the Directorate of Civil Aviation (DCA) from the central Government into a Civil Aviation Authority and already the Attorney General has published a bill to this effect which has been forwarded to the Parliament.

- Energy:

Energy has a direct impact on the general growth of the economy. Therefore, sustainable cost-effective energy supplies used in the most technically efficient manner are pre-requisite for achievement of development goals. In order to achieve the above policy objective, expansion of electricity generation capacity need to be undertaken on least cost basis in order to meet the growing electricity demand which is envisaged to increase from 843 MW to 1202 MW by 2008. In addition, the power sub sector is being restructured and organised to mobilise financial resources and attract private investment with the view to improving operational efficiency and reliability of electrical supply.

Petroleum Exploration: The Government continues to play a major role in stimulating petroleum exploration activities by attracting international oil companies through the production sharing contracts to explore the hydrocarbon resources with the ultimate aim of striking commercially exploitable deposits.

Promotion of wood fuel supplies and management are encouraged through programmes aimed at the widespread on-farm energy production and use of efficient stoves in order to make the resource available on a sustainable way. Further use of alternative sources of energy such as solar, wind, power alcohol and biogas are being promoted to supplement and conserve energy where appropriate.

(iv) Private Sector Development, Policy on Trade, Tourism and Industry

- **Private sector development**

GoK has committed itself to relinquish its direct involvement in commercial activities and focus on the provision of an appropriate regulatory framework for private sector activities. The implementation of the **Privatisation Strategy** under the economic reform programme has been on-going, and, so far, 168 parastatals have been privatised and further ones are in the process of being privatised.

The informal sector contributes in a significant way to domestic manufacturing, particularly in the areas of household goods, motor vehicle parts and farming implements, and accounts for double the employment of the formal sector (2.5 million). In terms of potential income and employment-generation, it is a key component in the fight against poverty.

The Government's attention to the high potential of poverty reduction and income generation of the informal sector is now increasing. To this end, GoK is working with the private sector to support the informal sector.

- Trade policy:

Since 1993, steps have been made to liberalise Kenya's trade regime with the abolition of import licensing, the elimination of tariffs in countries participating at the COMESA free-trade area in October 2000, and the removal of quantitative restrictions.

Domestic industry had been protected by a wall of high tariffs levied on competing imported products prior to the era of tariff reforms, but today the maximum tariff rate stands at 35% for a few selected items and the number of bands has been reduced.

Regional integration is an important driving force for internal and structural change by increasing competition, economies of scales, regional investment opportunities and by prompting collaboration on economic policies.

A major challenge facing Kenya in her trade relations with the EU is the negotiations of an Economic Partnership Agreement (EPA) as foreseen in the Cotonou Agreement. The EPA, which will promote regional integration in Eastern Africa and will be WTO compatible, will replace the current trade arrangements from 2008. The EPA negotiations will address the gradual establishment of an FTA with a high degree of asymmetry and flexibility, and will include arrangements in the area of services and in trade related areas, such as sanitary and phytosanitary measures, technical regulations and standards, competition and investment. EPA negotiations started on an all-ACP level in September 2002. Negotiations on a regional level are foreseen from September 2003."

- Tourism policy:

Tourism remains one of most important foreign exchange earners to the country. While the sector has suffered during recent years it recorded improvement in 2000, showing a 20% increase in tourist arrivals. However, over the last decade, Kenya has been facing strong competition in the segment of quality tourism, which is the highest foreign exchange earner within the sector. In order to increase the market share at the upper end of the tourism-market and fulfil the objective to move towards quality tourism, increased efforts in modernisation and upgrading of facilities, marketing and diversification of tourism products will be required to provide a competitive value-for-money rate for consumers. There is also need to promote investment on alternative products like eco-tourism which demonstrated significant growth even at times where the sector was in crises.

- Industry:

The Government's policy on industrialisation is detailed in the "Sessional Paper No 2 of 1996 on Industrial Transformation to the Year 2020" which aims at laying the foundation for structural transformation of the country into a Newly Industrialised Country (NIC) by the year 2020. The just ended 8th National Development Plan also focused its attention on industrialisation as a strategy for achieving rapid and sustained economic growth.

Kenya has a strong industrial base and the manufacturing sub-sector accounts for 13% of GDP. The sector has however experienced declining growth in the past, arising from several constraints including, among others, high cost of electricity, poor infrastructure, unfair competition, cheaper imports, and high interest rates. The public and the private sector through the Joint Industrial and Commercial Consultative Council (JICCC) are addressing these constraints.

In addition, GoK is under the current 9th National Development Plan (2002-2008) committed to improving the sector's performance through: revitalisation of industrial growth; maintain quality control and standards; enhance research and technology advancement; and undertake industrial skills and private sector development.

b) Medium term development challenges:

In the recent past Kenya has made progress towards improving the framework for the implementation of its poverty reduction strategy.

While the **policy orientations** have been in the right direction, the pace of implementation has been slow and irregular. The new Government is, however, committed to put in place the enabling environment for policy implementation, although the pace of implementation is hampered by inadequate resources.

The Government has declared and adopted a "zero tolerance to corruption", and has taken steps to strengthen the legal and institutional framework to improve **governance** and eliminate **corruption**.

It is imperative that the commitment to reforms is maintained and reinforced. The successful implementation of these reform initiatives will be decisive for the ultimate sustainability of the PRSP.

In addition, flooding/droughts/insecurity and **HIV/AIDS pandemic** remain major challenges to Kenya's efforts in returning to the path of sustainable development. The large **refugee** population continues to exert pressure on natural resources as well as on government resources/service delivery and an upsurge of **insecurity** through the **proliferation of small arms**.

The attainment of **food security** also remains an important medium-term challenge.

The Government's **institutional capacity** to manage and implement policies for achieving the PRSP objectives continues to remain a challenge. The Government recognises the need to enhance institutional capacity building with the view to improve performance and efficiency in public service delivery. This is being addressed through the on-going Public Sector Reform initiative.

In order to implement the PRSP priorities, mobilisation of the country's internal resources together with external support, requires **Government commitment** as well as **involvement of the private sector and civil society**. An important challenge for those leading the change process is to maintain public support and manage expectations. The PRSP consultative process is highly positive and should help in this respect in building national consensus. Monitoring and evaluation of the PRSP implementation will be a continuous exercise involving all the stakeholders.

It is also evident that the Government would require **substantial resources to sustain its economic and public sector reforms**.

Furthermore, the importance of **asylum and migration** has been underlined by the Commission in its Communication of 3 December 2002. Issues such as discussions on the root causes of migration, better integration of legal migrants living and working in the EU and combating illegal migration, trafficking and smuggling of human beings should become an integral part of existing dialogue and contracting frameworks with Kenya. The potential dynamics between migration and development policies need to be explored and efforts should be made to strengthen the capacity of Kenya to manage migration.

4. AN ASSESSMENT OF PAST AND ONGOING EC COOPERATION.

4.1. Programme Overview

The EC is currently Kenya's second-largest cooperation partner, after the World Bank. Annual EC aid finances over 10% of GoK's development budget. EC assistance, under the 6th, 7th and 8th EDFs has totalled €920 million, covering programmable (€412 m) and non-programmable aid (€508 m). The latter comprises STABEX, EIB loans, structural adjustment and emergency aid. In addition, Kenya has received support under EDF Regional Programmes and from the Community Budget, mainly NGO programmes and food aid. The current active EC programme portfolio comprises programmes and projects totalling approximately €350 million, of which STABEX resources (transfer years 1990-1993 and 1999 plus accrued interest) comprise around €110 million.

Until 1995, EC cooperation with Kenya was highly concentrated on the cereals sector (50% of programmable resources and 100% of STABEX). The programme was re-oriented away from the cereals sector, towards supporting policy and institutional reforms and on greater effectiveness through management improvements. EDF resources were shifted towards strengthening the productive sector, together with programmes to support the development of the human, economic and natural assets. The use of STABEX resources was also entirely re-structured, to focus on the coffee sector and economic diversification.

- **Productive Sector Strengthening:** (53% of EC country portfolio)

  (i) Support to agriculture and rural development (10%)

  EC support has mainly been provided towards institutional and management capacity, but also through specific projects. The Commission has particular experience in four agricultural sub-sectors**:** livestock (and in particular animal health), coffee, fisheries and agricultural research. These are also some of the key sub-sectors identified under PRSP for support in the poverty eradication program.

  On-going EC programmes are consistent with the key elements of the Kenya Rural Development Strategy (KRDS), notably relating to increasing rural/agricultural productivity, food security, promoting community and private sector participation, efficiency in service delivery, continuing the reforms and support for the Arid and Semi-Arid Lands.

  Experience in the sector has highlighted the need to support the management capacity, identified as an essential area of weakness. A support programme in this area is now under appraisal.

  One particularly successful programme is the Community Development Programme (27 M€). This supports small self-help programmes throughout Kenya. It has shown the value of decentralised management structures and the potential of working directly with civil society through community based self-help programmes in alleviating poverty in both rural and urban areas.

  The EC has also supported rural income diversification, rational land use and conservation through its support under its Community Wildlife Initiatives and Biodiversity Conservation Programme. At the same time, support to environmental management has been given through the launching of stakeholder consultations on impact assessment. This culminated in the elaboration and eventual promulgation of the Government's Environmental Impact Assessment guidelines institutionalised through the Environment Management and Coordination Act, which came into force in 14th January 2000 and the establishment of the National Environmental Management Authority. It has also supported rural water supplies e.g. in 1997 it supported rehabilitation of small dams in ASAL districts in the country.

(ii) Roads sector: (43%)

The EC has been one of the major donors to the roads sector in Kenya, covering institutional reforms and rehabilitation of trunk and rural roads. It was on the recommendations of an EC-financed institutional reform study that the GoK decided to establish an independent Roads Board (KRB) to take over the management of the Road Maintenance Fund. The next challenge is to assist the KRB to become fully efficient in its operations. Another positive development has been the reduction of overloading of trucks through axle-load monitoring financed by the EC. The future privatisation of axle-load control will be the subject of a "best-option" study being launched with EC financing.

The implementation of the EDF-financed Northern Corridor Rehabilitation Programme has encountered major delays after tender cancellation following leakages of confidential information. The works contract for phase 1 was finally signed in December 2002, with construction beginning in April 2003. Experience with the "Roads 2000" ([14]) programme, which focuses on maintenance and improvement of rural roads, shows the need to decentralise planning and management to district levels, with the involvement of local communities. Experience on this programme also supports the PRSP proposals to expand the programme through labour-based small contractors.

- **Public Sector Reforms, institutional capacity development and governance:** (15%)

This is a recent area for EC support and has been provided to the comprehensive public sector reform programme launched by GoK in 1999 (budget support plus TA). In parallel, the EC is providing support to public service institutions for the improvement of their efficiency, effectiveness and standards of governance.

(i) Budget support for Public Sector Reforms (PRBS)

Following resumption of WB/IMF support to Kenya in 2000, an EC Poverty Reduction Budget Support Programme (PRBS)([15]) was approved to support the strengthening of Public Service efficiency totalling M€ 50. Linked to the reform programme set out in the PRSP, PRBS provides for the re-imbursement of the costs of civil service retrenchment.

PRBS is providing targeted budget support for the Public Sector Reform Programme and thus the first EC resumption of "quick disbursement" aid to Kenya. The majority of the first tranche of this programme (€23 million out of €26 million) has been disbursed. The second tranche is linked to the implementation of the BWI programmes and has now expired.

(ii) Institutional capacity development support

EC support to public sector reforms and economic management includes strengthening institutional capacity by supporting institutions such as the Kenya Institute for Public Policy Analysis

(14) Co-financed by EC, DANIDA, SIDA.

(15) PRBS also provides for technical assistance to the general economic and poverty reduction reform programme.

(KIPPRA), which is active in policy formulation and analysis in support of the on-going reforms and to provide longer term perspectives.

Institutional Support to the NAO comprises technical assistance, logistics and training to increase institutional capacity in EDF programme management.

(iii) Good Governance

An EC support programme on good governance and democracy (8th EDF) was approved in November 2000. It aims to strengthen governance institutions such as the parliament, the judiciary and civil society. A call for proposals is being launched in 2003.

- **Support to human resource development** (16%)

(i) Health Sector support

In response to the Government's Health Strategic Plan NHSSP, the EC - in consultation with other donors – has developed a District Health Services and Systems Development (DHS&SD) Programme, which was signed in May 2002, and follows earlier EC support for the Kenya Family Health Programme. These programmes aim at strengthening the quality of and access to health services delivered by public and non-public providers and respond to community needs.

(ii) Education support operations:

In the education sector, support has been limited to specific institutions e.g. Strathmore University and Eldoret Polytechnic. Many classrooms have also been constructed under the Community Development Programme.

(iii) Research and S&T capacity building:

Kenya plays an important role as partner in the EC led North-South research co-operation. The country has traditionally benefited from EC support, in particular in the field of agricultural research. It is expected that the country will be closely associated with the European Developing Countries Clinical Trials Programme on new interventions, drugs and vaccines against HIV/malaria and tuberculosis and its specific efforts on trial capacity building in Africa. Further initiatives should be considered in support of the mainstreaming research and S&T capacity building in line with ACP wide co-ordination in support of R&D for sustainable development.

- **Support for Private Sector Development, Trade and Tourism:** (11%)

(i) Enterprise promotion and Trade support

The main interventions revolve around the Micro-enterprises Support Programme (MESP), leading to the establishment of a Micro-Credit Trust Fund. MESP has been successful with an outreach of around 8000 beneficiaries, thus constituting a major element in poverty reduction activities.

Concerning Trade, the EC is providing GoK with support to strengthen its institutional negotiation capacity with a view to the negotiations of new Economic Partnership Agreements.

(ii) Tourism

A Tourism Development Programme is underway for an amount of 24 M€ to support marketing, product diversification (including eco-tourism/community-based tourism) and improvement of the regulatory framework. A Tourism Trust Fund was established in May 2002. Tourism has a significant potential to make a direct impact on poverty reduction, community participation in development and on sustainable economic growth in Kenya.

- **Other support areas:** (5%)

  EC also supports some important activities in sectors such as natural resources conservation and cultural heritage.

- **Operations of the European Investment Bank (EIB)**
  The EIB is very active in Kenya. This reflects the importance of the manufacturing and productive sectors in the country. During the Lomé IV period, the EIB has provided € 133 million in own resource loans and € 83 million in risk capital operations. The major part of this financing has been made within the framework of the Global Private Enterprise (GPE) scheme whereby the EIB makes funds available to the Central Bank of Kenya which are then tapped on a competitive basis by commercial banks and financing institutions to finance small and medium-scale investments in the agro-industrial, horticultural, manufacturing sectors, tourism and associated services (about 250 firms have been supported in this manner, with unit amounts of between € 10.000 and € 1.5 M). The Government and the EIB have agreed to include health and education in the GPE scheme. The Bank has also been active in financing larger scale private sector projects (steel, plant propagation) and in the energy sector ([16]).

- **Humanitarian aid and the link between relief, rehabilitation and development (LRRD)**

  Often as a result of insufficient disaster preparedness in the country, ECHO had to intervene several times to deal with the consequences of drought and conflict, providing support for refugee assistance and drought relief. The overall amount of ECHO funding was more than 10 million € over the last 3 years. Appropriate disaster preparedness and LRRD measures should be envisaged to increase the overall efficiency of Community action, in line with EC development policy and taking into account the potential of complementarity.

- **Other Financing Instruments**

  In response to the 1999/2000 droughts, the EC contributed 45,000 tonnes of cereals to the GoK/WFP relief programme. A further 6,800 tonnes of food aid was provided via NGOs. In addition, two long-term household food security programmes have been financed. Support has also been provided under the NGO co-financing budget line. Since 1997, some 30 projects have been financed for an amount of € 10 million. These projects have focussed on health, micro-finance for women, child rights and education for street children.

4.2. Consistency and Relevance of EC-Programmes

The ongoing EC Country Programme is relevant to Kenya's reform framework and consistent with the main policy objective of poverty reduction of both the Government and the EC. The sectoral breakdown is also broadly consistent with the sectoral priorities defined in the PRSP. Recent project evaluations

(16) Mabati Galvanising Plant (€ 9 million), and cofinancing of Olkaaria Geothermal Plant (€ 41 million)

(SPIM, MESP, TDP, Family Health, CDP([17]) have all confirmed the positive trend in project relevance, implementation and impact.

The major weaknesses of ongoing EC-cooperation, however, is that (i) it is spread across too many projects, which are difficult to manage, (ii) implementing agencies have not always performed satisfactorily, and (iii) in the absence of sector-wide policy reforms, the sustainability of some programmes may be difficult to achieve.

Although rapidly improving, disbursement rates under the 8th EDF remain behind schedule: around 32% (stabex excluded) as at end 2002, reflecting the fact that EC cooperation with Kenya was almost entirely refocused in 1995 and has subsequently largely been designed on a project basis.

4.3. Lessons learnt

Currently, EC-Kenya cooperation can be judged as broadly positive, certainly when compared with the difficulties experienced during the first half of the 1990s. Room for further improvement remains, however, requiring action by both partners.

The following lessons learned have been fed into the proposed 9th EDF response strategy:

- NAO-Delegation relationship: the close working relationship between the NAO's office and the EC Delegation has been a key element in the recent improved performance of Kenya-EC cooperation. More intensive cooperation will be required under the 9th EDF, with greater emphasis on continuous dialogue.

- Organisational support: linked with the above, experience has shown that the work of the NAO's office benefits from organizational support. This is being provided through technical assistance and support for short term studies. For its part, the EC Delegation in Kenya is one of the first that received new powers and responsibilities under the de-concentration exercise being implemented by the EC worldwide. This will enable more decisions to be taken on the spot and contribute to speeding up programme implementation.

- Decentralised programme management: a major success of the 7th/8th EDF programmes has been the implementation of programmes through trust funds managed by boards of trustees which bring together key stakeholders and expertise. This has already been successfully applied in the Community Development and Biodiversity programmes and is being extended to Tourism and will be extended to Microfinance. These programmes have generally been implemented more rapidly and have reached their final beneficiaries more effectively than more traditional management approaches. Possibilities to further extend the decentralized management approach will be explored under the 9th EDF, particularly within the framework of greater involvement for non-state actors. At the same time, it is intended to build on the success of these community-driven development approaches in order to further support government's efforts in local government reform and rural service delivery.

- Community/Private Sector involvement: linked to the above, there is already a strong involvement of non-state actors in programme implementation, particularly in the areas of community development, health and microfinance. This provides an excellent springboard for

(17) SPIM – Strengthening Public Investment Management
MESP – Micro Enterprises Support Programme
TDP – Trade Development Programme
CDP – Community Development Programme

their further involvement under the 9th EDF, including earmarking a specific allocation for non-state actors.

- Good governance has been acknowledged as a prerequisite to successful poverty reduction efforts and sustainable economic development. It will therefore be important to identify areas of support under EDF 9 to sustain continued progress in governance and other reforms.

- In the past emergency aid interventions have been used extensively to respond to recurrent/seasonal disasters such as drought. Such needs are in general better addressed through development assistance, as underlined in the Commission Disaster Preparedness and Prevention Policy. Emergency assistance should only be required in case of serious economic and social difficulties of an exceptional nature.

4.4. Programmes of EU-Member States and other donors

Net ODA from all donors has been steadily declining during the 1990s to stabilize in recent years around 3% of GDP. However an important number of donors remain active in Kenya including many of EU Member States. In terms of magnitude of funding the major multilateral donors to Kenya in recent years have been the World Bank, EC and the World Food Programme (WFP) while Germany, Japan, UK and US have traditionally played an important role amongst bilateral donors.

Moreover, in the area of emergency/disaster preparedness, the World Bank is finalising the appraisal of a 6 year programme[18] (Arid lands resource management Project) aimed at improving the Kenyan administration capacity in disaster management, including drought, in critical areas of the country.

Although there is a growing concern from many donors to concentrate aid on a limited number of sector interventions, the wide distribution of donor support in various sectors is still significant. A donor matrix illustrating expected donors' contributions by sector for 2002-2003 is also shown in annex 6.

4.5. Export –oriented sub-sector assistance

In accordance with the provisions of the Lome IV Convention, Kenya has qualified for a transfer under the STABEX system for loss of earnings in coffee and tea for the year of application 1999. The total amount of the transfer was EURO 47,841,888 (plus interest). These funds were utilised in targeted budget support benefiting areas were export losses were originated. Previous Stabex transfers have been allocated for the development of key foreign exchange earning-productive agricultural sub-sectors, diversification and improvement of the general economic environment. Existing balances non yet allocated will be used in line with the general objectives of Stabex and according to the priorities defined in the CSP.

5. GoK - EC RESPONSE STRATEGY

- **Indicative Resources**

  Under the 9th EDF, the indicative allocation of resources to Kenya is as follows:
  "A" allocation: M€170, which may cover macro-economic support, sectoral policies, and programmes and projects.

[18] estimated financing envelope (2004-2010): 68.4 million USD

“B” allocation: €55million, covering unforeseen needs such as emergency assistance, contribution to debt relief initiatives as well as support to mitigate adverse effects of instability in export earnings.

In addition, there remain approximately €45million uncommitted from previous EDFs. These funds together with STABEX uncommitted and/or undisbursed resources will be utilised in accordance with the response strategy agreed upon by GoK and EC.

- **GoK - EC Response Strategy**

The response strategy outlined below is based upon the following considerations:

-the analysis of the economic, social and political situation in Kenya and its prospects
-the priorities identified during the PRSP consultation process and financing requirements
-EC development policy priorities([19])
-lessons learnt from past/ongoing EC programmes and an assessment of comparative advantage
-complementarity with EU Member States and other donors active in Kenya.

It should be recognised that measurable improvements in **governance** are fundamental to sustainable economic growth and poverty reduction in Kenya. The response strategy and other donor programmes must be implemented within an acceptable timeframe, policy environment and institutional framework.

The EC is ready to support this process through further programmes in the areas of public sector reform and governance. Resumption of macroeconomic budget support by BWI will depend upon measures taken by GoK to address the governance issues by improving Public Finance Management and enactment of anti-corruption legislation.

Agriculture and rural development was identified as the highest sectoral priority during the PRSP consultation process. The sector significantly contributes both directly and indirectly to about 80% of employment and 60% of natural income. About 80% of the population live in the rural areas, of which 75% are poor. Consequently, significant improvements in the agricultural and rural development sector are prerequisites to addressing economic growth and poverty reduction in Kenya.

In addition, the KRDS initiative aims at addressing policy and institutional reforms in the sector. The KRDS has been the subject of extensive consultations with stakeholders (with EC support) and is now being finalised for adoption. The KRDS places particular emphasis on the empowerment of rural communities and the need to strengthen the capacity of local authorities in the delivery of rural services and infrastructures. It also focuses on food security and more effective response to droughts which could be a base for a more comprehensive disaster preparedness strategy, particularly in areas of past recurrent EC emergency interventions. An effective disaster preparedness element within rural development will make an important contribution to reduce the need for such emergency interventions within the overall Commission strategy of improving linkages and coherence between relief, rehabilitation and development.

All these initiatives are relevant and fit well with the EC’s development policy priorities in Kenya and the EC is committed to supporting the sector.

(19) Identified areas in the EC Communication on Community Development Policy (04/2000) are: trade and development; regional integration and cooperation; support for macro-economic policies; transport; sustainable rural development and food security, institutional capacity building, particularly in the area of good governance and the rule of law

The PRSP consultative process identified roads as the top priority within the physical infrastructure sector. However, the poor state of infrastructure acts as a constraint to rural development. Rural roads are in poor condition which affects production, transportation and marketing of agricultural produce. Other infrastructure constraints, such as water supplies, lack of electricity, marketing and storage facilities and telecommunications were also identified as constraints to the development of the sector.

The PRSP National Stakeholders Forum also identified the poor sector of the road network as a major constraint on economic growth and poverty reduction as it contributes to the high cost of doing business.

Continued EC support to **Roads Sector** would also constitute a logical continuation of past and ongoing EC support. Such support is essential if the policy and institutional reform of the sector is to be sustained and the Kenya Roads Board fully established as the effective and operational custodian of the road network and the prime policy adviser to Government.

Furthermore, Government will only be able to raise a small fraction of the road sector's financing requirements (estimated at about US$ 1 billion p.a.). The EC's financial resources and comparative advantage all point to the importance of continued EC support to this sector.

Human resource development was also identified as a priority in the PRSP process. The needs of the health sector are certainly important, and there are already a number of donors active in this sector including World Bank, UK, Denmark, Sweden, Germany, US as well as the EC under ongoing programmes. Within the Education sector, the immediate requirements are additional budgetary resources to meet the cost of free primary education together with a comprehensive policy review to address the efficiency of public expenditure. EC support to both these sectors could best be provided from targeted budget support and from non-EDF resources (e.g. HIV/AIDS funds).

All sectors in Kenya need a supportive macroeconomic framework within which to operate. The PRSP recognises the critical challenges now facing the country: how to revamp growth, raise productivity, encourage private investment, reduce unemployment and poverty. The Government has underlined its commitment to implement the necessary macroeconomic and institutional reform measures within the PRSP cycle. These reform measures will encompass public expenditure management, the fiscal strategy, pro-poor growth policies, public sector reform, privatisation, trade liberalisation, regional integration and measurable improvements in the standards of governance.

Within this context, resumed **EC Macroeconomic Budget Support** would be an important complement to GoK core poverty reducing expenditure on the one hand and to EC's own support to the focal sectors on the other. The provision of budget support requires, in principle that Kenya gets back on track with the IMF to enable such support to be resumed.

Finally, it is proposed that an allocation within the A-envelope be reserved for other programmes, in particular support for private sector, civil society, regional initiatives including trade and environment, and preparatory and/or complementary actions to EC projects and programmes.

- **Involvement of Non-State Actors**

The PRSP-preparation was based upon an extensive consultation process, which has involved a series of national workshops with civil society, including the poor in which the Delegation participated. Furthermore, the draft KRDS has been extensively discussed with key stakeholders, including non-state actors, in workshops supported and attended by the EC Delegation

At the same time, EC involvement in the Community Development Trust Fund has given it a close insight into the priority needs of local communities throughout Kenya. The ongoing rural roads programme is being reoriented to involve local communities in the selection and implementation of road rehabilitation, to ensure a participatory approach and local ownership.

Moreover, three workshops with civil society have already been organized, and a third is planned. A regional seminar in Nairobi of Economic and Social Interest Groups organized by ECOSOC was also used as an opportunity to advance the dialogue with non-state actors.

This process of consultation and involvement of non-state actors will continue and be intensified during the finalisation of the Country Support Strategy and its translation into detailed sectoral programmes. This will, *inter alia*, contribute to determine the criteria and eligibility for direct access by Non-State Actors to EC funding.

- **Policy Coherence**

  It will be essential to ensure coherence between Community support under the response strategy and other Community policies highlighted under Cotonou. To this respect particular attention will be given to the forthcoming regional Economic Partnership Agreements (EPA) to be negotiated with the European Commission. Furthermore, the need to respect EC sanitary and phytosanitary regulations, notably on fish and horticultural exports, must be integrated into efforts to boost exports and appropriate assistance provided.

- **Complementarity and Coordination**

  Thirteen EU Member States are represented in Nairobi and coordination both within the EU and the wider donor community is reasonably well established. In particular, the system of “lead donor” within specific sectors/themes is already being employed e.g. EC is the lead donor in the roads sub-sector, UK for legal sector reforms, WB for disaster preparedness.

  The main forum for donor coordination in Kenya has been the Economic Governance Group, chaired by IMF/World Bank. This has two shortcomings (i) several EU Member States are excluded (ii) it is generally convened on an ad hoc basis, mainly to brief donors on GoK-IMF discussions. The GoK has taken the lead in donor coordination through the recently established Kenya Coordination Group, which brings together a wider range of donors into a forum chaired by the Minister of Finance.

PART B - INDICATIVE PROGRAMME

6. INDICATIVE WORK PROGRAMME

6.1. Introduction

Within the Country Strategy presented in part A, and in accordance with the provisions of Article 4 of Annex IV to the Cotonou Agreement, the indicative programme has been drawn up in a series of tables presenting the intervention frameworks for each focal sector.

6.2. Financial Instruments

Several financial instruments will be used to finance EC co-operation with Kenya. The following is an indication of their mobilisation as presently envisaged.

(i) ***EDF 9 - Envelope A (170 M€).*** This envelope is to cover long-term development operations within the Country Strategy. Although the basic principles, objectives and sectoral priorities of the PRSP remain the guiding framework of Kenya's development strategy, for the new administration economic recovery can be achieved mainly by releasing resources into the budget and tightly monitoring macro-economic performance in key-sectors. The response to this need is reflected in the NIP by a significant allocation to budget support without neglecting other traditional sectors of the Kenyan economy. The indicative allocation of this envelope to the elements of the strategy is proposed as follows:

- Agriculture and Rural Development, 25% - 35%
- Transport/Roads infrastructure sector, 20% - 30%
- Macro-economic support, 40% - 50%
- Other programmes (private sector development, non-state actors, regional initiatives, reserve) 5 - 10% .

(ii) ***EDF 9 - Envelope B (55 M€).*** To cover unforeseen needs as indicated in the Cotonou Agreement, Annex IV, Article 3.2 (b).

Possible use of envelope B will be consistent with the EC development policies. As far as emergency assistance is concerned, possible use of envelope B will be consistent with EC DPP and LRRD policies.

(iii) ***Balances of previous EDFs.*** Approximately €45 million is uncommitted from previous EDFs. These funds will be added to the 9th EDF funds earmarked for macroeconomic budget support. Furthermore, Stabex balances will be allocated along the lines and the priorities established in the NIP.

(iv) ***EC budget lines*** could be used to finance specific operations, particularly to support civil society. Finance from this source will be decided in accordance with the procedures for the budget line concerned and will depend on availability of funds.

Apart from the above-mentioned financial instruments, of which the A-envelope is the main programmable basis for the Indicative Programme, the 9th EDF also includes the "Investment Facility" as a financing instrument managed by the European Investment Bank (annex 7). The Investment Facility does not form part of the Indicative Programme.

6.3 Focal sectors

A. Agriculture and Rural Development

The specific objective of EC intervention in this sector is to support the achievement of the PRSP sectoral growth target of 6% p.a. for Agriculture and Rural Development and thereby contribute to national growth and poverty reduction.

For indicative purposes, approximately 25-35% of envelope A shall be reserved for this sector.

Priority actions will be in support of the two main areas identified in the PRSP:

- empowering rural communities in the local development process and providing the conditions for accelerated private sector economic activity
- support to local service delivery and infrastructure provision through capacity building, policy and institutional reforms, and financial assistance to key public good/service providers/facilitators.

Particular attention will also be paid to crosscutting environmental/biodiversity issues, the role and position of women and, when appropriate, to trade related technical support.

If the sector wide policy and institutional conditions permit, interventions might consist of budget support

The **major accompanying policy measures**, which will be taken by the Government, are as follows:

(i) Further elaboration of the Kenya Rural Development Strategy and provision of a coherent framework for rural investments, including infrastructure, through the MTEF process,

(ii) take measures to give effect to the announced policy of increasing the functional responsibilities of Local Authorities in service delivery and the decentralisation of decision making to local communities

(iii) take steps to improve:

- dissemination of research findings to small scale farmers;
- markets and marketing information;
- improved management of farmer and trade organisations, particularly cooperatives and statutory boards.

(iv) Within the main sub-sectors, the Government will take steps to make progress in the following areas:

- Rural Water: GoK will encourage greater stakeholder involvement in the management of water schemes. GoK will gazette water catchment areas and enforce the Water Act, whilst promoting riverine/riparian afforestration, spring protection and wetland conservation.
- Crops: the Government will take steps to improve the regulatory and tariff environment for the main export crops and domestic staples.
- Livestock Development: the GoK and relevant stakeholders will develop a national policy to control and eradicate livestock diseases, promote the improvement of livestock marketing and livestock extension services.
- Food Security: the GoK and relevant stakeholders will institute a national early warning and food distribution system as a basis for disaster preparedness. In this context the Commission, the GoK and other relevant stakeholders will discuss further the definition of a more comprehensive disaster preparedness strategy.
- Lands and Settlement: the GoK will implement the Environmental Management Coordination Act and other relevant land use policies to encourage sound land use, water and forestry policies more compatible with higher agriculture growth rates.
- Environmental Management: the GoK and other stakeholders will create awareness on environmental costs and benefits and involve communities in environmental conservation activities such as reforestation, develop and enforce environmental standards and sustainability indicators. The GoK will carry out a natural resource inventory with a view to establish a clear environmental profile of the country, also the GoK will institute a national policy on agro-chemicals, industrial emissions and effluents.
- Forestry: the GoK will develop working partnerships with NGO's, the private sector and other stakeholders to expand forest plantations and improve the policy, legal and institutional framework needed to restore Kenya's forest ecosystem. The GoK will control excisions of gazetted forests and carry-out a full forest inventory and the development of a national policy framework through extensive stakeholder participation.
- Fisheries: the GoK will promote private sector activities through improved beach facilities, roads, water supplies and electricity. The GoK will also strengthen the Fish Inspectorate and Quality Control Service.

2. Transport/Roads Sector

The specific objective of EC intervention in this sector is to reduce transport costs and time for users to access economic and social services, thereby increasing accessibility, incomes and employment in the rural areas.

For indicative purposes, approximately 20-30% of Envelope-A shall be reserved for this sector.

Priority actions will be in continuation of support already provided under previous EDFs, i.e.:

(i) Support to develop a coherent transport sector policy and strategy; enhanced institutional support for road sector management reforms, related to road sector institutions, including the Kenya Roads Board; autonomous Road agencies, regulatory authorities; and the devolution of power and resources to district level;

(ii) Reducing the maintenance backlog of the Northern Corridor linking Mombasa port to the Kenyan hinterland, and through to Uganda, Rwanda, Burundi and eastern Congo. The rehabilitation of the road north to Ethiopia will also be examined.

(iii) Rehabilitation and improvement of rural access roads and bridges, particularly through labour-based small contractors and local communities.

The **major policy measures** to be taken by the Government will concern the continuation/finalisation of existing policy reforms, i.e.:

(i) The recently established Kenya Roads Board will be fully operationalised to oversee the maintenance of all major roads, to rehabilitate and upgrade international trunk roads and to facilitate the construction of bypasses to reduce congestion on classified roads.

(ii) The District Roads Committees, also recently established, will be strengthened and given greater devolved responsibilities to enable them to oversee effectively the maintenance, upgrading and construction of rural access roads, footpaths and bridges, as well as linkages between rural access roads and other rural roads and major highways.

(iii) The Government will also:

- direct more budget resources to the Kenya Roads Board Fund, in order to improve road quality and service delivery
- strictly comply with the dispositions of the Kenya Roads Board Act and Fuel Levy Act
- reduce delays in auditing and accounting for road maintenance
- pursue opportunities for privatisation and commercialisation of road construction, maintenance and management
- continue to enforce axle-load controls, including their privatisation/contracting out by 2005
- encourage the participation of the private sector, civil society, and local communities in road construction, maintenance and management
- ensure compliance with tendering and evaluation procedures, in accordance with the Cotonou Agreement
- create a Road Safety Board to harmonise road safety programmes and ensure enforcement of road safety regulations
- develop the capacity to undertake environmental impact assessments as a standard element of all road programmes
- work with its regional partners towards coordinated, harmonised and complementary transport policies and agree on investment priorities at regional level.

6.4 Macro-economic Budget support.

The EC is ready to provide macro-economic support, under appropriate conditions, as a contribution to the public sector reform programme and the PRSP. Special attention would be given to the objective of poverty reduction[20], particularly with a view to ensuring equitable access to social services. At the same time, the sectoral PRSP priorities must be clearly reflected in the MTEF. In this context, close attention will be paid to the monitoring of public expenditure (both in terms of quantity and quality) allocated to the social sectors and other core poverty programmes. The effectiveness of these core poverty

[20] in line with appropriate indicators, including social indicators

programmes will also be the subject of regular monitoring, based on the relevant performance indicators contained in the PRSP Government Action Plan (e.g. net enrolment rate and completion rates in education; immunization coverage and HIV prevalence in health; access to water in rural development etc.). In addition, such support is contingent upon Kenya getting back on track with an IMF-supported macro-economic programme. More general budget support may be considered in the light of improved public finance management.

Macro-economic support shall be delivered, in principle, under a three years' programme. Funds shall be linked to the budgetary cycle of the Government and disbursed on an annual basis in three negotiated tranches. Whereas the first tranche would be fixed, the following two tranches would depend in their total amount/size on the progress achieved on the basis of jointly agreed performance indicators. This progress will be reviewed in the context of the annual review, which should also be part of the annual review of progress in the PRSP implementation.

For indicative purposes, approximately 40-50% of envelope A shall be reserved for this type of support.

The Government will implement the following **economic and institutional reform measures,** if possible within the PRSP cycle and develop measurable indicators for their effective implementation and monitoring:

- Realign budgetary resources in favour of investment and maintenance expenditures (increase share of development budget in total budget);
- Improve Public Financial Management, in particular auditing pending bills and rolling out the Integrated Financial Management and Information System (IFMIS) in key sectoral ministries (i.e. Roads, Agriculture, Health);
- Clear reflection of PRSP priorities in the budget and, in particular, augment the capacity of the MTEF Secretariat;
- Conduct annual PRSP performance reviews in line with the budgetary cycle and a Monitoring and Evaluation framework agreed with key stakeholders, including the development partners.
- In the area of Governance the Government will take concrete measures to deal with corruption, including reform of the public sector and civil service in line with the SPIPS, enactment of anti-corruption legislation, the establishment of a code of ethics for public officials together with reform of the legal and judicial systems. The Government will ensure that all cases of alleged corruption are investigated promptly and, if justified, prosecuted.

6.5 Other programmes.

An indicative amount, approximately 5-10% of envelope A, has been reserved for other possible commitments. This includes, inter alia, complementary funding to private sector development, regional projects and programmes including in the area of trade, environment and regional integration, insurance against possible claims, cost increases and contingencies as well as preparatory actions, studies and evaluations. Support to non-state actors will be considered upon agreement of funding eligibility criteria between GoK and the EC

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6.6. Intervention Framework

A) Intervention Framework for Focal Sector: Agriculture and Rural Development

Summary	Indicators	Source of verification	Hypothesis/Assumptions
Aim: ▪ To reduce rural poverty by half by 2015	▪ % living below poverty level	▪ National statistics ▪ PRSP reviews ▪ Welfare Monitoring Survey	Comprehensive PRSP monitoring and evaluation system established
Specific Objective: ▪ To support the achievement of the PRSP growth target of 6% p.a. for the Agriculture and Livestock sector	▪ % growth of agricultural sector > = global growth	▪ Reports by Ministry ▪ National accounts ▪ Employment reports ▪ Export statistics ▪ Special surveys/studies	▪ Kenya Rural Development Strategy is translated into a Sessional Paper, adopted as a Policy document and effectively applied
Expected results: ▪ Reduced role of state in agricultural production and marketing ▪ Institutional reforms and deregulation in selected sub-sectors ▪ Decentralised rural service delivery and infrastructure improved ▪ Capacity in Local Government increased ▪ Food crop production increased ▪ Enhanced quality of Kenyan agricultural export commodities ▪ Vulnerability of poor households reduced/reaction-capacity strengthened ▪ Improved and rationalised use of natural resources	▪ Number of acts and laws reviewed, enacted and effectively applied ▪ % of the population with access to basic services infrastructure ▪ Nutritional scores improved in rural areas ▪ Share of commodities in exports increased ▪ Production of food crops increased ▪ Environmental indicators as appropriate	▪ Reports by Ministry ▪ Assessment reports ▪ Food security surveys ▪ Trade/Exports statistics ▪ Project reports ▪ LATF returns	▪ GoK/MoALD continued commitment to ministerial rationalisation, decentralisation and deregulation and other institutional reforms in the selected sub-sectors ▪ Establishment of the agreed programme management unit in MoALD
Identified Projects/Programmes: ▪ Community Development for Service Delivery ▪ Local Government Capacity Building ▪ Export sector programmes ▪ Community self-help programmes (CDP III) ▪ Livestock marketing study	**Indicative Budget:** ▪ 25-35% from A envelope	▪ Feasibility/Preparatory studies ▪ Presentation of Financing Proposals ▪ % programmes committed	▪ Results of preparatory studies are favourable ▪ Clear linkage to PRSP budgets established

B) Intervention Framework for Priority Sector: Roads Infrastructure

Summary	Indicators	Source of verification	Hypothesis/Assumptions
Aim: ▪ Sustainable contribution by the roads infrastructure sector to poverty reduction, and economic and social development in Kenya	▪ Improvements in socio-economic development including environmental aspects ▪ Improved condition of Kenya's roads/infrastructure	▪ National income, employment, public transport and roads statistics ▪ UNDP report on human development	▪ PRSP policy recommendations are effectively translated into priority actions ▪ Coherent transport sector policy/strategy adopted & implemented
Specific Objective: ▪ To reduce transport costs and time for users to access economic and social services thereby increasing accessibility, income and employment in rural areas	▪ Km of roads rehabilitated/maintained including part through labour based contracts ▪ Road sector institutions are operating efficiently and fully accountable ▪ Sufficient resources allocated for reconstruction and maintenance	▪ Reports by Min of Roads ▪ Annual statistics ▪ Employment reports and special surveys/studies ▪ Annual budget ▪ Income and Expenditure of KRB (Fuel Levy Fund and Coffee+Tea Cess)	▪ Institutional reforms continued ▪ Axle load restrictions are enforced and privatized/contracted out ▪ Tender procedures are respected ▪ Participation of communities ensured ▪ Timely payment of contractors and casual labour
Expected results: ▪ KRB and DRC/s become fully operational and Roads Department replaced by a viable, autonomous Roads Agency ▪ Roads network rehabilitated/maintained ▪ Transport time shortened ▪ Roads safety and their environmental/social impact improved ▪ Privatisation of Axle load enforcement, with overloading progressively stabilized at below 10%	▪ Number of Acts and Laws reviewed, enacted and effectively applied ▪ Maintenance/Rehabilitation programmes effectively implemented ▪ Number of accidents reduced ▪ Monitoring results ▪ Studies	▪ Government Gazette ▪ Independent audits ▪ Assessment reports ▪ Annual budget ▪ Road accident statistics	▪ GoK continued commitment to institutional reforms
Identified Projects/Programmes: ▪ Completion of Northern Corridor Rehabilitation ▪ Rural Roads Programme ▪ Isiolo-Moyale Road study ▪ Support to institutional reforms	**Indicative Budget:** ▪ 20-30% from A envelope	▪ Feasibility/Preparatory Studies ▪ Presentation of financing proposals ▪ % programme committed	▪ Results of preparatory studies are favourable ▪ EDF tender/contract procedures respected

C) Intervention Framework for Macro-Economic Support 2001 -2004

Summary	Indicators	Source of verification	Hypothesis/Assumptions
Aim: ▪ To create the conditions for accelerated, sustainable and equitable economic growth	▪ GDP growth rates ▪ Reduced poverty ratios	▪ National accounts ▪ PRSP reviews ▪ Welfare monitoring survey ▪ National population census	▪ PRSP priorities clearly reflected in MTEF ▪ Available external resources ▪ Appropriate monetary and taxation policies ▪ Governance issues addressed ▪ Tariff harmonisation within EAC/COMESA
Specific objective: ▪ To support improvements in Public Service Delivery; ▪ Increase the investment/budget ratio	▪ Increased quality and coverage of key public services ▪ Investment/budget ratio	▪ National accounts ▪ Budget/MTEF ▪ service delivery surveys ▪ Public expenditure reviews ▪ Statistics	▪ Measurable progress to improve governance and the fight against corruption ▪ Government programme gets back on track with BWI ▪ Donor funding comes forward to support the programme
Expected results: ▪ Core poverty programmes increased ▪ Quality of expenditure improved in line with poverty reduction goals ▪ Coherent Taxation policy, and tariff system streamlined	▪ Core poverty programmes as % of total budget ▪ PRSP GAP impact indicators in social sectors and other core poverty programmes (eg enrolment and immunisation rates, access to water) ▪ Pay as proportion of budget ▪ Simplification of taxation procedures ▪ Other social indicators when appropriate	▪ Budget, ▪ Public Expenditure reviews ▪ Service Delivery surveys ▪ Enterprises professional association reports	
Identified Projects/Programmes: Support contingent upon Kenya getting back on track with IMF/WB	**Indicative budget:** 40-50% of envelope A		

6.7(a) PIPELINE CHRONOGRAMME

	Instrument	%NIP	Amounts (M€uro)			Target dates			
EDF Co-operation Programmes			**Total**	**EDF9**	**EDF Balances**	**Stabex p.m.**	**Identification**	**Appraisal**	**Financing decision**
EDF Co-operation Programmes **FOCAL AREA 1 : Agriculture/Rural Development**									
Rural Service Delivery Programme	PS			34			Mar 03	Jul 03	Nov 03
Community Development for Environmental Management Programme	PS			13			Mar 03	Sep 03	Jan 04
Sub Total 1		**28 %**		**47**					
FOCAL AREA 2 : Transport (Road Transport Sector)									
- Feasibility/Design Studies	PS			2			Jun 03	Sep 03	Oct 03
- Maintenance backlog Northern Corridor	SBS			35			Jul 03	Oct 03	Feb 04
- Rural Roads	SBS					20	Jul 03	Dec 03	Mar 04
Sub Total 2		**22%**		**37**					
FOCAL AREA 3 : Macroeconomic support									
Budget Support Programme	GBS			70	45		Jun 03	Jul 03	Sept 03
Institutional Support	PS			5			Jun 03	Dec 03	Mar 04
Sub Total 3		44%		**75**					
Non Focal Sectors									
MESP II	PS			6.5			Mar 03	Nov 03	Mar 04
NSA support	PS			2			Jun 03	Dec 03	Apr 04
Sub Total 4		5%		**8.5**					
RESERVE		**1 %**		**2.5**					
TOTAL 9th EDF		**100 %**	**215**	**170**	**45**				
P.m. Front Load Budget Support (FY 2002-2003)	SBS					50			
STABEX			**70**			**70**			
T O T A L			**285**						

PS Project Support
SBS Sector Budget Support
GBS General Budget Support
BFS Basket Funding Support

6.7 (b) INDICATIVE TIMETABLE FOR COMMITMENTS AND DISBURSEMENTS - Commitments

All amounts in € million	2003/1	2003/2	2004/1	2004/2	2005/1	2005/2	2006/1	2006/2	Total
1. Agriculture/Rural Development									
♦ Rural services Delivery Programme		34							
♦ Community Development for Environmental Management Programme			13						
2. Support to Transport policy (Road transport sector)									
♦ Feasibility/design studies		2							
♦ Maintenance Backlog Northern Corridor			35						
♦ Rural Roads			20 (1)						
3. Macro-economic Support									
• **Budget Support Programme**		115 (2)							
• **Institutional support**			5						
NON-FOCAL AREAS AND RESERVE									
♦ Micro-Enterprises Support Programme (MESP II)		6.5							
♦ Non-State Actors support			2						
♦ Reserve				**2.5**					
TOTAL 9th EDF		**157.5**	55	2.5					
% NIP 9th EDF + Previous EDF Balances		**73%**	**26%**	**1%**					
% NIP 9th EDF + Previous EDF Balances (Cumulative)		73%	99%	100%					

(1) STABEX

(2) including €45 mio previous EDFs

6.7(c) INDICATIVE TIMETABLE FOR COMMITMENTS AND DISBURSEMENTS – Disbursements

All amounts in € million	2003/2	2004/1	2004/2	2005/1	2005/2	2006/1	2006/2	2007/1	2007/2	2008/1	2008/2	**Total**
1. Agriculture/Rural Development												
♦ Rural services Delivery Programme		2.5	3.5	4.0	4.0	4.0	4.0	4.0	4.0	4.0		**34.0**
♦ Community Development for Environmental Management Programme		1.5	1.5	2.5	2.5	2.5	2.5					**13.0**
2. Support to Transport policy (Road transport sector)												
♦ Maintenance Backlog Northern Corridor			10.0		15.0		10.0					**35.0**
♦ Institutional support, Preparatory Actions and Studies		0.1	0.5	0.5	0.5	0.4						**2.0**
3. Macro-economic Support												
♦ Budget Support Programme		40	40		35							**115(1)**
♦ Institutional		1	2	1	1							**5**
NON-FOCAL AREAS AND RESERVE												
♦ MESP II		0.2	0.8	1.5	1.5	1.5	0.7	0.3				**6.5**
♦ Support to NSA's			0.5	0.5	1.0							**2**
♦ RESERVE				*1.0*	*1.5*							***2.5***
TOTAL		***45.3***	***58.8***	***11.0***	***62.0***	***8.4***	***17.2***	***4.3***	***4.0***	***4.0***		***215***
% NIP 9th EDF + Previous EDF Balances		21.1	27.3	5.1	28.8	3.9	8.0	2.0	1.9	1.9		**100**
% NIP 9th EDF + Previous EDF Balances (Cumulative)		21.1	48.4	53.5	82.3	86.2	94.2	96.2	98.1	100		

(1) of which €45 mio balances is from previous EDFs.