Democratic Transition: Economic Development and the Role of the Private Sector
A Case Study of Kenya
by Caroline Kariuki, CEO Kenya Private Sector Alliance (KEPSA)
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History shows that democratic development and economic progress are fundamentally linked. It also shows that a well-functioning economy is a prerequisite to achieving broad-based prosperity, which is crucial if a government is to achieve legitimacy among its population. There is a direct relationship between democratic development and economic prosperity, yet the importance of this link is often relegated to an afterthought when considering political and institutional reform. Countries in transition towards democracy, or, as in the case of Kenya, towards greater democratic stability, must not overlook the vital importance of economic reform.

The African continent has experienced numerous transitions since the end of the colonial era. Few immediate transitions following this period were successful, but over the past two decades the number of African democracies has soared as part of the ‘third wave’ of democratisation. With increased democratisation come widening economic opportunities, which must be seized to ensure democratic legitimacy in the long term.

In Kenya, economic reform—in this case a transition to a market-based system—has proven essential to democratic consolidation. Since the post-election turmoil in 2007–08, Kenya has made significant progress towards a stable democratic outcome. From here, progress can only be sustained by rising living standards and increased opportunity, which require long-term growth, stability, and investment. This paper looks at Kenya’s example of bringing in the private sector to achieve democratic progress, and what lessons may be offered to other transitioning countries in Africa and around the world.
Democratic Transitions

Recently, we have witnessed a number of democratic transitions taking place across the globe. Millions of people in countries once ruled by autocrats are struggling to realise freedom and shared opportunity. A number of African countries, such as Liberia and Sierra Leone, are striving to consolidate democratic transitions and usher in a brighter future. However, financial instability, internal inefficiencies, and lack of opportunities are major barriers to achieving this.

As the 2011 events in Tunisia demonstrate, economic factors will often be the spark for political transition and regime-change. Over the past three decades, many African transitions have been triggered by unsustainable authoritarian economic policies that inflicted unacceptable costs on citizens, rupturing the ‘authoritarian bargain’. For example in Egypt, a winter drought in China led to severe wheat shortages and skyrocketing bread prices, causing Egyptians to take to the streets waving bread as a protest symbol. Clearly the ‘authoritarian bargain’ can expire if basic needs are not met.

Here we turn to good governance and legitimate institutions, for which a growing middle class, demanding accountability and neutrality, and resisting the pull of an authoritarian backslide, is essential. As Kenya undergoes this process, an important role of the private sector and of the Kenya Private Sector Alliance (KEPSA) is to continue to strengthen this middle class, creating the prosperity under which good and accountable governance can become deeply embedded, positioning the country for long-term stable economic growth.

Kenya’s Democratic Transition and Economic Reforms

The promise of political freedom raises people’s expectations for economic and social opportunities. The success of emerging democracies depends fundamentally on whether political transitions and democratisation can deliver shared opportunity and inclusive growth to materially improve people’s wellbeing. Each country begins the process of democratic transition from a unique position based on its own political and economic development. Thus an evaluation of the initial circumstances plays a critical role in understanding the transition.

Kenya has gone through a protracted political transition starting in 1992 when the first multiparty elections were held. The 2002 Presidential Election saw the end of the 40-year reign of the Kenya African National Union (KANU), which was defeated by an opposition coalition. The disputed general elections in 2007 triggered ethnic violence that led to a push for a new constitution, which was formally adopted in 2010. This new constitution marked a critical juncture in the nation’s history and encompassed a dramatic transformation of the Kenyan state through new accountable and transparent institutions, inclusive approaches to government, and a firm focus on equitable service delivery for all Kenyans through decentralisation. During this process, the establishment of 47 county governments was essential for government efficiency, providing functions and services at a more localised level and creating conditions for growth. Following this establishment
of county governments, there has been greater focus on facilitating private-sector activity and supporting businesses, as greater economic activity is expected to shift to the counties. Kenya’s future economic development will rely heavily on private-sector investments with the public sector playing a supporting role. The Kenya Vision 2030, a long-term initiative to achieve durable growth, which is discussed in detail in the next section, recognises this fact and places emphasis on private-public partnerships.

Over the last decade, Kenya’s macroeconomic indicators have maintained a positive average trend, resulting in moderate economic growth. Kenya’s GDP was about US$17.39 billion in 2004 and per-capita GDP averaged more than US$450 annually. Adjusted in purchasing power parity (PPP) terms, per-capita GDP was approximately US$1,200. The country’s real GDP growth picked up to 2.3 percent in early 2004 and to nearly 6 percent in 2005 and 2006, compared with a sluggish 1.4 percent in previous years (1997–2002). Kenya’s economy witnessed an annual real GDP growth rate of 4.6 in 2012, as compared to an annual real GDP growth rate of 4.4 percent in 2011 and 5.8 percent in 2010. Kenya’s GDP growth rate for 2013 is projected to be over 5 percent. Unlike some countries in sub-Saharan Africa, which experienced above-average economic growth, either due to natural resource extraction or starting from an initially low level of economic development, Kenya’s growth relied largely on reforms that allowed market forces to govern private-sector growth. These reforms created substantial opportunities, particularly in the services industry and infrastructure development, as well as facilitating economic efficiency, increased competition, and foreign investment.

FIGURE 1: KENYA GDP (CURRENT US$ BILLION)
Kenya’s GDP is expected to continue to improve, largely driven by growth in tourism, telecommunications, transport, and construction, and a recovery in agriculture. The government has implemented economic reforms to cultivate these markets, such as the deregulation of telecommunications. The World Bank estimates that mobile phones have added 1 percent a year to Kenya’s GDP growth since 2000. Kenya is also very competitive in terms of human capital, with an adult literacy rate of 87 percent and a strong emphasis on education. Kenya shows the highest public expenditure on education in East Africa at 17.7 percent between 2008-2009 and 2011-2012.

Kenya’s economy also serves as an anchor in the region, contributing to the progressive development of the East African Community. Its geographic location, in the centre of Africa’s east coast, makes it an ideal gateway for exports and imports to the continent. Additionally, Kenya has emerged as a regional technology hub. IBM recently set up its first African research lab in Nairobi, joining other global tech giants headquartered there, such as Google, Intel, and Microsoft.

Kenya’s growth is expected to increase with the exploitation of the newly discovered resources of oil and gas as well as other minerals. The oil and gas discoveries in the Rift Valley could have a potentially transformative effect, placing Kenya in the top tier of oil-producing countries on the continent. Resisting the negative effect of the resource curse, where rising revenues result in corruption, rent-seeking, and the possibility to undermine other sectors of the economy, will be one of the greatest challenges Kenya faces over the next few years.

The importance of turning Kenya’s oil into a blessing and not a curse is all the more pressing given the number of challenging social and economic indicators. For example, demand for electricity is growing at a rate of 14 percent annually, while debt at 1.96 trillion shillings, or 53.3 percent of Kenya’s annual output, is stable but significant. Most worrying is Kenya’s youth unemployment. According to the World Bank, “of the 800,000 Kenyans who reach working age each year, only about 50,000 are likely to find a ‘modern wage job’, securing a stable source of income.” For Kenya to continue on a positive track, it will need to provide jobs and create the growth that its citizens have come to expect.
The Role of the Private Sector in Kenya’s Transitions Process

The private sector has a significant role to play in Kenya’s transition—from job-creation, innovation, and growth to good governance and social cohesion. The private sector offers valuable insight into the formulation and implementation of pro-growth policies that enhance Kenya’s competitiveness, encourage domestic and foreign investments, and pursue regional and international economic opportunities.

The Economic Recovery Strategy (ERS) and KEPSA

In 2003, the Kenyan Government developed the ‘Economic Recovery Strategy’ (ERS) which aimed to overhaul and liberalise Kenya’s economy after decades of economic mismanagement, state intervention, and stagnant growth. From 2003 to 2007, this initiative led to strong economic growth. Although this growth collapsed following the global financial crisis, it has since recovered and Kenya has been averaging a growth rate of around 5 percent per year. The founding targets of the ERS were to:

• Reform the state and its operations so that good governance could prevail under democracy and the rule of law, whilst maintaining a sound macroeconomic framework;
• Improve the physical and social infrastructure;
• Revive economic and governance institutions;
• Drive pro-growth policies, e.g. the Micro and Small Enterprises (MSE) Act, and the National Information & Communications Technology (ICT) Policy;
• Provide free primary education to give access to education to all.

To achieve the goals of this plan, the government understood the need to have a focused, organised ‘one-stop-shop’ for the private sector that would allow private enterprise to engage in both the development and implementation of the Economic Recovery Strategy. The government challenged the private sector to form an organisation that would work with the government to deliver the ERS. The private sector was ready to take on a proactive role, as it had suffered from many closings or relocations to other countries due to the unfavourable economic and political climate before 2002. It seized the opportunity to work with the government to revive the economy and invest in Kenya’s prosperity after years of bureaucratic stagnation.

As part of this wider strategy, Kenya’s business leaders came together to form the Kenya Private Sector Alliance (KEPSA) to better facilitate the interaction between the government and the private sector and to help deliver the targets listed above. KEPSA, founded in 2003, operates at the apex of the private sector in Kenya, providing a bridge between the public and private sectors. The collaboration soon showed positive results; by 2005, with constant focus on economic reforms and with a regular engagement between KEPSA and the government, the GDP was about 5.5% from a mere -2% in 2000.
KEPSA’s major strength is its ability to convene the private sector to speak with a unified voice to contribute to positive long-term economic and policy outcomes. In KEPSA’s experience there are five key areas of collaboration and cooperation between the government and the private sector. These include:

- working to improve the investment climate;
- providing a business perspective on state performance and governance;
- developing infrastructure able to support stability and inclusive growth;
- facilitating global and pan-African trade;
- creating strong natural resource management.

Increasing the linkages in these areas has created the conditions for increased dynamism and resilience in the wider economy.

From creating social capital to crisis preparation to facilitating the implementation of pro-growth and investment policies, the private sector is contributing to numerous positive outcomes as Kenya emerges from transition to become a stable middle-income country.

**Vision 2030 and the Medium Term Plans (MTP)**

Like many African countries, Kenya has launched a long-term development plan that targets significant gains within a relatively short period of time. Vision 2030 aims to see Kenya as a middle-income country by 2030. Similarly, Malawi has launched a Vision 2020 plan, while Liberia has also embarked on a Vision 2030 plan.

The long-term plans undertaken by these countries align closely with the UN’s Millennium Development Goals. Taken together, such plans aim to transform a nation’s economy and core state infrastructure and establish accountable political governance. To achieve this progress, it is estimated that Kenya’s GDP must grow by 10% per annum until 2030. This is an aspirational target and demonstrates the sustained, significant private-sector growth that is required to support the wider Vision 2030 process.

An active and flourishing private sector is vital for achieving these goals. As such, KEPSA was highly involved in the consultations and formulation of the Vision 2030 programme through its sector boards that work in partnership with government ministries. KEPSA continues to engage the government on implementing pro-growth policies and regularly presents trade and investment opportunities to both local and foreign businesses in Kenya and abroad. In this process, a particular focus on youth unemployment is vital—38% of the youth are neither in school nor employed (aggregating the rates of unemployment and inactivity). In response, KEPSA has implemented programmes that teach business and entrepreneurship skills, including the Kenya Youth Empowerment Project in partnership with the government and the World Bank. The programmes plan to train approximately 11,000 youths through provision of training and internships over a four-year period (2011–2014). Currently in its 3rd project year, 8,066 youths have successfully been trained, while 5,118 of the total youths trained have successfully completed the internship programme. Approximately 80 percent of the interns have been employed, while the others have gone on to further skills-development.
In addition, KEPSA has contributed greatly to the content and development of other pro-growth policies, such as the Public Private Partnership Act, and trade and industrialisation policies. The role of the private sector here is to carry out functions which the state can support but does not have the capacity to deliver efficiently.

Security, Stability, and Growth

Security and stability impact business and growth—and here the private sector also adds great value. This was clear following the 2007 post-election violence. In an effort to manage the crisis, KEPSA mounted a spirited campaign in partnership with the Panel of Eminent African Personalities under the leadership of Kofi Annan, to help mediate between the two warring political factions (the Party of National Unity and the Orange Democratic Movement). This eventually resulted in the formation of the Grand Coalition Government. These efforts also contributed to the formation of the Presidential and the Prime Ministerial Round-Tables as forums for continued engagement between the private sector and the government on both economic and governmental issues.

After the formation of the Grand Coalition Government in 2008, a Committee of Experts (COE) was established to help finalise Kenya’s new constitution. KEPSA engaged the COE to ensure the private-sector voice was included in the process. One key input from KEPSA was advocating a two-tier system of government as opposed to a three-tier system, as the three-tier system would be too costly to the country. KEPSA played a critical role, canvassing its members prior to the referendum. KEPSA then formed a committee mirroring the government committee and worked closely with Parliament. KEPSA continues to actively ensure that constitutional bills are private-sector friendly to allow for continued growth and innovation in the country.

Additionally, following the disruption of business that ensued after the disputed 2007 election, the private sector worked in partnership with civil society, faith-based organisations, media, and development partners to spearhead the MKenya Daima (“Kenyan Forever”) peaceful election campaign, aimed at inspiring peace during and after elections and opening up a dialogue about Kenyan identity and citizenship. This campaign led to over 200 community-building initiatives and contributed to a peaceful election in 2013 and to ensuring stability and business continuity during the process.

A more recent example of the link between economic and national security was the October 2013 terrorist attack on the West Gate shopping mall. Following this tragedy, KEPSA partnered with the government on security measures to mitigate future attacks and on other security issues with economic implications. This included working with the city of New York to gain insights on how to restore Nairobi’s economic vibrancy after the tragic attack.

The Way Forward

As demonstrated in the examples given above, there are many avenues of opportunity for governments in transition to better engage with the private sector. The transition process often takes decades to be fully realised, but this process can be quickened by fast, responsive
governance, inclusive growth policies, and an optimistic outlook. Guided by the National Business Agenda 2013-2018, KEPSA has been part of this process and has played a crucial bridging role between the dynamism and potential of Kenya's private sector and a reform-minded government. This success can perhaps be emulated by countries such as Liberia or Malawi that also look to achieve rapid industrialisation, growth, and prosperity as they look to achieve their economic reform goals.

KEPSA has also played an ambassadorial role, reaching out independently to the international community and developing Kenya’s private sector within global markets. If this process becomes too centralised, the government risks monopolising the productive, globalised areas of the economy while neglecting areas that urgently need attention to grow. Many African countries’ experience of oil wealth has shown exactly this. Wiser deregulation of key industries such as natural resources and agriculture will allow the private sector to be more adaptive in global markets and savvier in trading with more restrictive economic neighbours.

The private sector is at the forefront, not just in terms of providing opportunities for Kenya’s youth and a voice for business, but also in advocating democratic development as an African ideal. However, many challenges lie ahead. For all of Kenya’s dynamism, openness, and bubbling entrepreneurialism it remains a difficult place to do business. Corruption and inefficiency could stifle the promise of democracy and highlight the need to continue positive, pro-business reforms that can combine liberal freedoms and institutional transparency.

A Model in East Africa?

Kenya’s approach is often the exception in East Africa, not the rule, with models of state-led development also showing achievements in growth and modernisation. For example, to Kenya’s north in Ethiopia, state-run enterprise has increased exports, and has built 30 universities in 20 years. Despite its high inflation, lack of urbanisation, and heavy reliance on agriculture, Ethiopia’s growth rates have to date been higher than Kenya’s; Ethiopia recently overtook Kenya as Africa’s 5th largest economy. Whether or not this economic success is sustainable in the long term is another matter.

This demonstrates that there are alternatives to the path that Kenya has taken in Africa that other countries may be tempted to follow. The private sector has a significant role to play in proving that decentralisation will lead to better outcomes than an authoritarian core. Democracy across much of the continent is fragile, and aid and loans which would once come from the IMF and World Bank to cement democratic progress now flow from China. Meanwhile, the Chinese economic model looks attractive to many African states, who want to replicate the dramatic strides in living standards which China has achieved in a short period of time.

However, Kenya shows a different, more promising model where an autonomous private sector and a free market position the country for long-term growth, good governance, stability, and investment and innovation opportunities. Whereas the Chinese Government’s heavy hand in enterprise has impeded private-sector development, leading to market inefficiencies and slowing levels of growth—a challenge that led to a reassessment of the relationship between government and markets in China’s Third Plenum in November 2013.
Conclusion

By understanding the trade-offs, sequencing, and critical economic and policy decisions that transitioning countries have faced in the past, policymakers in Africa and Kenya in particular can make wiser choices to improve the chances of successful democratisation today.

Kenya has received praise for following the path of reform. World Bank Executive Director Denny Kalyalya recently stated that “At a time when many countries in Africa were struggling with the idea of the private sector as the engine of growth, Kenya had already embraced this concept.” He concluded that “We [The World Bank] owe a debt of gratitude to Kenya that this proposition, long accepted outside the continent, demonstrated that this was possible in Africa.”

Despite its many challenges, Kenya offers much to be optimistic about. The country is maintaining a course of economic reforms which, if implemented correctly, will lead to growing economic prosperity, giving promise to the Vision 2030 goals and serving as a model for other countries, adding to the stability of the region. Kenya’s experience shows that a vibrant and active private sector has an important role to play in a democratic transition, contributing not only to wealth-creation and stability, but also to overall long-term democratic outcomes.
REFERENCES


2. A situation where a dictator provides public goods for his subjects in order to remain in power.


14. The two-tier system of government consists of the Senate and the National Assembly, making up the Kenyan Parliament.


ABOUT THE AUTHOR

Caroline Kariuki
Caroline Kariuki is CEO of the Kenya Private Sector Alliance (KEPSA), a consortium seeking to create a vibrant business environment in Kenya and East Africa. She was appointed the CEO of KEPSA in 2010 at the age of 35 and has more than 10 years of experience working with governments and the private sector. Prior to her appointment as CEO she had previously worked with Barclays Bank in Kenya and was a research fellow and later an associate at the Sagamore Institute for Public Policy Research in Indianapolis. During this time she initiated and led the Africa Programme. She holds a masters in public administration and international affairs from the Bowling Green State University in Ohio and a bachelor of arts (honours) in economics and sociology from the University of Nairobi.

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Kenya dropped three places, to 116th, in overall prosperity. The Social Capital sub-index increased by eleven places to 73rd, due to an increase in the ability to rely on others, the willingness to help a stranger, and an increase in religious attendance. The Safety & Security sub-index ranks a low 127th, due to an increase in property being stolen, state sponsored violence, and group grievances, and a decrease in the perception of being able to safely walk home alone at night.

"This decline over five years is, in part, due to the addition of 32 new countries in the 2012 Prosperity Index. In this instance, three of these new countries placed above Kenya."

NOTES:

1. Gov. effectiveness: values range from -1.66 to 2.25, higher values indicate higher effectiveness.
2. Human flight: values range from 1 to 10, higher values indicate higher levels of human flight.
3. Civil liberties: values range from 1 to 7, lower values indicate lack of civil liberties.
4. Survey data are taken from Gallup World Poll.