

KENYA

COUNTRY PARTNERSHIP STRATEGY

FY2014-2018

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Photo: KPLC

Executive summary

1 Kenya can be one of Africa's success stories.

It holds great potential including from its growing and youthful population; dynamic private sector; a platform for change laid down by the new Constitution and recent peaceful elections; and its pivotal role within East Africa and further afield. Yet poverty remains high with 4 out of 10 Kenyans living in poverty and the richest 10 percent of the population receiving 40 percent of the nation's income. Governance concerns persist; and growth, while solid, has been constrained by low investment and low firm-level productivity and has yet to take off at the rapid, sustained rates needed to transform the lives of ordinary citizens.

Progress and prospects: Diagnostic review of the country context and development agenda

2 This strategy is based on a systematic review of evidence to identify the key challenges and opportunities for Kenya to accelerate progress toward the twin goals. The poverty rate

fell from 47 percent in 2005 to 39 percent based on best estimates in 2012. Some social indicators have improved notably, yet inequality is high (Gini of 47.4); there are significant differences in opportunities and outcomes between women and men, for those living in the remote and most underdeveloped regions, and ethnicity remains an important factor in societal development. Looking ahead, ending extreme poverty by 2030 would imply a cut in the poverty rate of 2 percentage points each year, likely requiring the economic growth rate to double and inequality to halve. To unlock rapid and uninterrupted growth that is sustainable and inclusive, Kenya must address the key binding constraints of low investment and low firm-level productivity. Faster growth needs significant policy reform to redirect public spending to meet growing infrastructure needs. It also needs an improved business environment that encourages private sector expansion and carefully manages the tax burden on business.

Vision: Government priorities and medium-term strategy

3 Kenya wants to be a globally competitive and prosperous nation with a high quality of life.

“Vision 2030”, a broad-based agenda straddling the current and previous administration, rests on three pillars: economic, social, and political. The economic pillar envisages moving up the value chain in key areas, including agriculture and financial services, to consistently deliver 10 percent annual growth. The social pillar focuses on investing in people, including in education, health, and housing, and with a focus on women, youth, and vulnerable communities. The political pillar seeks to “move to the future as one nation,” including improving the rule of law, transparency, and accountability. Vision 2030 is operationalized by the second Medium-Term Plan (MTP2, 2013-17), and this national agenda is entirely consistent with the Bank Group’s global timeline targeting an end to extreme poverty. This, together with stakeholder input gathered in extensive consultations, provides a good anchor for this Country Partnership Strategy (CPS).

Development challenges and opportunities

4 Against this backdrop, achieving rapid and uninterrupted growth over a decade or more is the foundational challenge.

The Government’s second Medium-Term Plan calls for huge investments in infrastructure. A key opportunity here is to leverage private sector resources through innovative public-private partnerships (PPPs), which are currently underdeveloped. To underpin a sound macroeconomic framework, a renewed effort is merited to help stabilize the wage bill. A more forceful initiative is needed to improve the business environment, including tackling some of the deficiencies pinpointed in World Bank Group

(WBG) analytical work. Much of this change agenda will only be possible when relevant, accurate, and timely statistics are produced to inform policies and help evaluate programs.

5 Placing a premium on human development is essential from several vantage points.

Growth must be inclusive so that prosperity can be shared by all. From an equity perspective it cannot be right that maternal mortality is among Africa’s highest at 488 deaths per 100,000 live births; and many lack access to food security, clean water, good healthcare, and proper housing. Youth unemployment at 21 percent is double the adult average. Equipping young people with a modern education and job opportunities is essential to make the most of their talents. Cities must not only generate economic activity but also provide basic services for those who dwell in them. And the cohesiveness of Kenyan society calls for renewed efforts to include the marginalized and disadvantaged. To curb poverty, growth must take place in sectors where the majority of the poor live. Investment must be redirected to projects closer to the poor, including improving agricultural productivity in rural areas, expanding and targeting unified social protection programs that keep people from slipping into poverty, attracting private sector investment and participation into education, and improving service delivery in health at the local level.

6 The changing institutional landscape is undergoing a tectonic shift with powers and 30 percent of government revenues moving from the national government to the 47 new county administrations.

This transition is truly historic and few countries have attempted anything on this scale. The

forthcoming challenge is to deliver a “devolution dividend” through greater citizen engagement, direction, and oversight of public authorities to fundamentally deliver better services to ordinary people; building new local governmental structures that are responsive and responsible; and fresh inter-governmental relationships, including resource transfers that translate policy priorities into meaningful on-the-ground services.

7 All of these opportunities would be amplified by improved governance and reduced corruption, or undermined by any deterioration in the prevailing environment.

In moving forward the WBG will be firm in its intolerance for corruption and desire for impunity to end, while setting expectations sensibly to make step-by-step progress. There are opportunities to continue improving public financial management, corporate governance standards, openness, transparency, and accountability in government; and to maintain robust safeguards. Such an “institution-building” approach will protect not only the integrity of WBG resources but also Kenya’s internally generated resources that contribute to 90 percent of all public spending.

Strategic options to make the most of the WBG assets

8 To help Kenya address these challenges, this CPS draws on a fruitful country relationship established over several decades and sets out how the combined resources of the Bank, IFC, and MIGA can best help Kenya fulfill its ambitions of becoming a modern economy in which growing prosperity is shared across all communities. The Bank will use a “selectivity test” that deploys a four-pronged benchmark to guide the deployment of scarce resources to

maximize the prospects of success: (a) confirming a credible line of sight to make a sustainable impact on poverty and prosperity; (b) critically reviewing WBG capability and comparative advantage, including assessing opportunities for WBG collaboration; (c) cementing client ownership; and (d) calibrating client capacity and accompanying project design. The selectivity test is used in a cascading fashion to establish the three domains of engagement, the sectors within each of the domains, and to make trade-offs between particular operations and analytical advisory activities (AAA).

9 The first domain of engagement is competitiveness and sustainability.

Improving infrastructure and the business environment, while being responsive to environmental pressures, is the backbone of long-term growth. WBG policy advice will help the authorities create a well-functioning and properly regulated energy market; IDA financing will be used for some publicly merited investments; and IFC and MIGA instruments will help leverage more private resources. More broadly, the Bank Group will redouble its support to public-private partnerships, especially in the water and transport sectors where there is medium-term potential. On transport, the focus of new IDA lending will be on significant rural feeder roads within and between counties to connect communities to emerging economic opportunities. Competitiveness can also be enhanced through improving the business environment, unleashing the potential of specific sectors and geographic locations, and ramping up financing sector and capital market development. The Bank will support the Government’s oversight of the rapidly emerging oil and gas sector. Both IFC and Bank resources will be deployed to help create private sector

jobs and try to make cities livable and sustainable, with a special focus on secondary cities where poverty is proving most stubborn.

10 The second domain of engagement is to protect the vulnerable and help them develop their potential, which is critical to sharing in prosperity. Social protection plays a pivotal role—the Bank’s strong engagement will be maintained. Health is also a pressing priority; in this sector the combined resources of IDA and IFC, alongside global funds and other partners, will be scaled up. Another key to help target support for the poor is to focus on agriculture, a high priority since it has such a direct link with helping families in rural areas where a majority of Kenyans live. Potential IFC investments in infrastructure, agro processing, and financial institutions further support the goal. The burgeoning youth population brings opportunities and challenges for WBG support in education, jobs, and skills. Protecting the poor who are disproportionately impacted by climate variability will also be an area of support. And across the board the gender focus of WBG operations and analytical work will be upgraded, including support for female education, entrepreneurship, and rural women’s groups.

11 The third domain of engagement focuses on building consistency and equity. This is a really long-term drive that has devolution at its core. The Bank’s large-scale capacity-building and AAA program will inform a series of IDA operations to help counties and national agencies to make devolution work. Upon request, the Bank would assemble and manage a Trust Fund framework to maximize donor coherence in this fluid arena. IDA investments will support a more evidence-based approach to policy making, public spending, and public administration reform. The consistency of Kenya’s

development will be buttressed by deepening regional integration with its neighbors; and WBG investments will be made in multi-country projects, including in energy and transport.

12 Individually and collectively the achievement of sustainable development results will only be possible if they are bound together through a connecting platform of garnering good governance, which in some ways has been an Achilles heel in the past. The WBG support has at its heart supply-side capacity building to strengthen oversight institutions, including support for better public financial management and for more effective institutions of accountability, combined with demand-side accountability such as the use of open community meetings for beneficiary engagement. The Bank will continuously review the impact of project-level governance measures that have been put in place, scaling up those that have been effective, including drawing on input from the WBG’s Integrity Vice Presidency (INT) on project safeguards and institutional support to agencies such as the Ethics and Anti-Corruption Commission (EACC). The WBG will deploy “corruption calibration” to its lending program—adjusting areas of focus and/or scaling back resources in the event of issues, which threaten the security of IDA and IFC resource use.

Implementing for results

13 The strategy incorporates a results-focus in this CPS and in specific operations and is flexible in responding to new conditions and information such as updated poverty data in due course. Targeted outcomes have been articulated in a multi-sector fashion, reflecting the interdependence of products across the strategy. The Bank Group’s efforts to manage for

results across the country program are built on country systems and capabilities for measuring and monitoring progress. Collaboration across the Bank Group and with other partners will be purpose driven in specific areas such as business climate, financial sector, public-private partnerships, energy, and agriculture. The selectivity test is already pushing the Bank Group to expand in some fields—such as supporting secondary cities, promoting rural development and devolution—and tapering Bank involvement in others such as highways, natural resource management, and legal reform. This process is dynamic, and the assessment will be continuously updated.

14 The WBG could be providing over US\$1 billion per year to Kenya over the life of this CPS. Careful portfolio management will continue to be an important ingredient of the drive for results—with tailored approaches to suit the particular circumstances of Bank, IFC, and MIGA investments. IFC is targeting portfolio expansion perhaps even beyond the US\$785 million of commitments at mid-FY14 if market conditions permit. MIGA’s current total exposure to Kenya is US\$255 million, and international investors’ interest in infrastructure, power, and agri-business sectors provides potential for this to expand further. The Bank’s annual commitments will be governed by the IDA17 settlement, provisionally assumed at around US\$600 million each year. This will build on the IDA portfolio in Kenya of US\$4.3 billion at mid-FY14, covering 23 national projects (US\$3.5 billion) and 7 regional projects in which Kenya is a partner (US\$0.8 billion). It is important to continue to “move to scale” especially in IDA investments, but also in IFC commitments, by focusing on larger projects and the judicious use of additional finance.

Managing risks

15 Any instability in the macroeconomic environment would probably be the single most damaging factor to overall poverty prospects. The mitigation strategy revolves around the long-term drive to improve competitiveness and exports, combined with a prudent strategy on reserves and international capital access to cope with potential volatility. Disasters and insecurity, natural or man-made, can be expected to occur even though their timing and severity typically cannot be predicted; and the Bank Group and its partners will seek ways to help cope with such risks in the future. Other strategic risks include unexpected changes in political leadership, policy direction and ministerial leads in key sectors, funding priorities of other donors, or a loss of appetite of strategic partners for IFC- and MIGA-supported deals. Each of these would require nimble re-engagement to prevent changes unduly affecting the WBG-supported program. Finally, operational risks include a worsening of the governance and corruption environment, including in new county administrations as their activities expand. The mitigating measures include (a) the thrust of this CPS to help garner good governance, including as part of the devolution process; (b) active cooperation between INT, the Bank, and the authorities in order that preventive measures are built into project design, and allegations when received are handled firmly and decisively; and (c) good communication with stakeholders, including the Board, so due proportionality can be applied in any strategic response needed by the Bank.