



# Trade Notes

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## EAST OR WEST?

### Comparing China, US and EU Policy, Trade and Investment Relations With Kenya

*By Trade Programme Team*

#### 1.0 Background

Kenya developed a single reference document containing her foreign policy in 2009. The vision direction of the foreign policy is 'a peaceful and prosperous Kenya effectively contributing to the realization of a stable continent and better international understanding' and the mission, is "to advance the interests of Kenya through innovative diplomacy'. There are five foreign policy pillars, these are: economic, peace, environmental, cultural and 'diaspora'. The main strategy to be used to achieve this economic goal in increased market access; capital in-flows and enhanced technological advancement. Kenya's foreign policy is guided by the pursuit of national interest, which is hinged on national security and economic prosperity. Kenya has had strong diplomatic relations - 74 resident ambassadors/ high commissioners, 29 non-resident ambassadors/ high commissioners, 7 charges d'affaires, 20 general/honorary consuls and 24 United Nations agencies, (GOK, 2014).

Kenya has had a long-standing development cooperation relationship with the European Union (EU). This is evidenced in the Yaoundé I and Yaoundé- II agreements, the successive

Lomé conventions: Lomé I: 1976-1980; Lomé II: 1981-1984; Lomé III: 1985-1990 and Lomé IV: 1991-2000, and subsequently in the Cotonou Partnership Agreement. The Lomé Conventions focused on international trade. The Cotonou Partnership agreement between the African, Caribbean and Pacific and the EU countries took effect in 2000 and encompassed three pillars: political, development and economic and trade cooperation. The Cotonou Agreement forms the basis for Kenya's interaction with development partners from the EU. Kenya signed a country joint assistance strategy with 17 partners in 2005, including the European Commission and the United States among others, in order to intensify collaboration that would significantly improve harnessing the opportunities for sustained growth. The main objective of this strategy is to ensure that development cooperation supports the achievement of Kenya's Government set goals. The EU is trading with Kenya under the Economic Partnership Agreement (EPA).

Kenya has also been a beneficiary of the US African Growth Opportunity Act (AGOA) that was signed into law in 2000. AGOA offers incentives for African countries to open up their economies and build free markets. The US government has given Kenya various incentives under the Africa growth and Opportunity Act (AGOA) initiative, which seeks to give African products market in



the US. AGOA has been through a series of reviews to make it more effective in addressing emerging technical issues as well as addressing the extension details of the apparel provision in accordance with the Acts terms and conditions.

- AGOA II amendment was to allow for an expansion of preferential access for imports from beneficiary Sub Saharan Africa countries in order to increase their utilization capacity.
- AGOA III extended third country fabric provision (TCFP) from September 2004 until September 2007
- AGOA IV extended the TCFP from 2007 to September 2015
- In June 29, 2015, President Obama renewed AGOA for another 10 years.

China's accession to the WTO in March 2001 has seen its integration to the global economy resulting in wider geographical pattern of trade and investment. There has been increased trade and investment between China and Africa resulting in China emerging as a potential development partner. China –Africa trade and economic relations are anchored under the framework of the Forum for the China Africa Cooperation (FOCAC). The main objective is to “to deepen the China –Africa strategic relationship in advancing trade and economic cooperation and actively exploring common development paths, that reflect the realities in China and Africa”. FOCAC is centered on:

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- i. Promoting sustainable trade through capitalizing on the complementary nature of the Africa-China relations;
  - ii. Support for enterprise and financial institutions in order to increase investment in Africa in the energy and mineral, manufacturing, services, and agriculture sectors;
  - iii. Agricultural cooperation in order to improve food security; Infrastructure support for improving ease of doing business
  - iv. Providing support and capacity building initiatives.

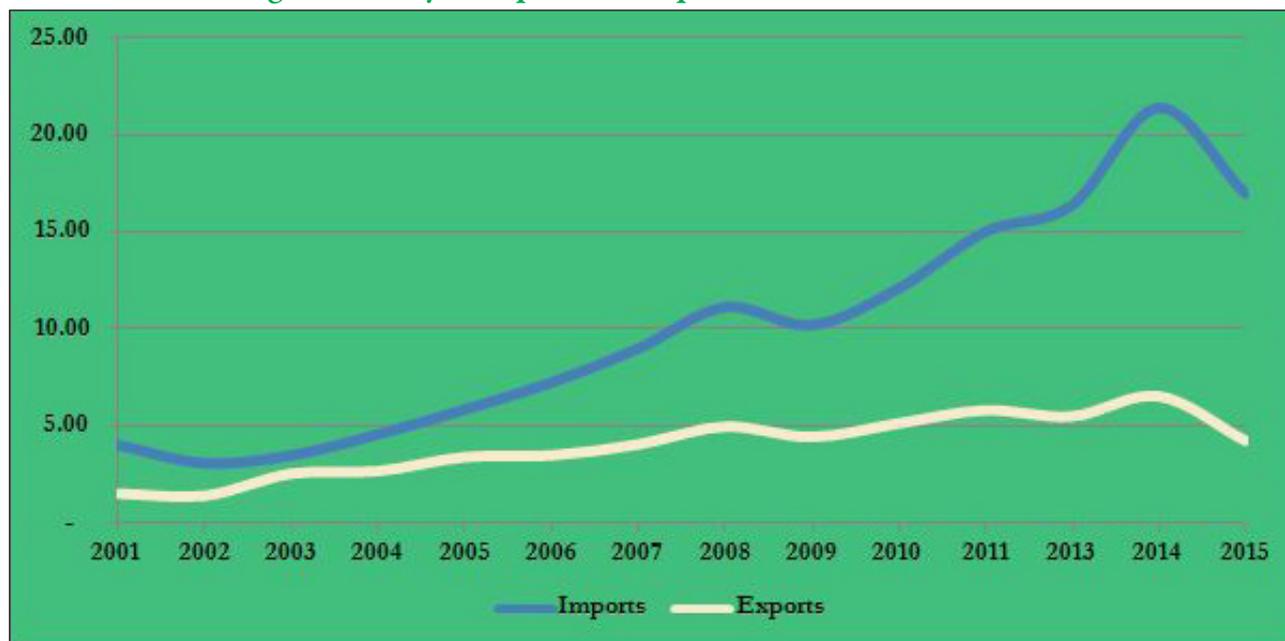
In terms of infrastructure development, in the recent past beginning in the year 2000, China has significantly increased her support for infrastructure development in Africa as a whole. In Kenya there are various projects that are the brainchild of the Chinese government in collaboration with the Kenya government, spearheaded by various agencies and government ministries, and funded by Export-Import (EXIM) Bank of China.

There has been a growing debate over the role of China in Kenya as compared to the traditional development partners such as the EU and the US. This debate has culminated into political statements such as 'looking east'. The IEA has taken the initial steps of holding discussion whether looking east is the only option for Kenya. As a starting point, the IEA reviewed the trade and investment trends between Kenya and the EU, US and China in order to establish whether this debates really holds.

## 2.0 Key Features of Kenya's Trade with China, EU and US

Kenya's imports from the rest of the world increased from USD 3.48 billion in 2003 to 21 billion in 2014, on the average imports has been increasing by 26 percent annually. The top imports include: mineral fuels and oils, vehicles, plastic articles, electrical equipment and machinery. Exports from the rest of the world increased from USD 2.6 billion in 2003 to USD 4.3 billion in 2014, on the average, exports increased by 4.4 percent annually. The main export products are live tree, coffee and tea, edible vegetables, mineral fuels apparels and accessories.

Figure 1: Kenya's Import and Export Patterns in US\$ Billions



Source: Trade map database



## China

- Kenya's trade with China has been on the rise, between 2011 and 2015, the average growth of exports from China to Kenya has been 27 percent.
- Kenya's exports to China for the same period were up by 34% from \$32 Million to \$43 Million whereas imports skyrocketed 69% from \$0.96 Million in 2009 to \$1.6 Million in 2011 (GoK, 2011).
- Chinese exports to Kenya constitute approximately 35 percent of Kenya's total imports. The rise in imports from China reveals that there are opportunities that have been identified in the Kenyan market and which have been exploited to the maximum by manufacturers, producers and exporters in China.
- Currently Kenya has a negative trade balance with China worth USD 5.8 billion.
- China is ranked the top world exporter with a share of 14 percent in the total world exports

## United States (US)

- Kenya's export trade with the USA has grown by 30% to a volume of \$293 Million in 2011, up from \$226 Million in 2009,
- Imports within the same period reduced by 22% from a high of \$649 Million in 2009 to a low of \$508 Million in 2011.
- The average export growth for exports from the United States to Kenya has averaged 28 percent between the periods 2011-2014.
- The exports from the US to Kenya constitute approximately 6 percent of Kenya's import.
- Kenya's trade balance with the US is USD 3.5 million (in 2011).
- The United States is ranked second world exporter with a share of 9.2 percent in total world exports

## European Union

Within the EU, Kenya's top trade partners were UK, Germany, Netherlands, Italy and France.

- Kenya's import from the EU increased from USD 1,887million in 2009 to USD 2,395 million in 2013, this amounted to a 27 percent increase.
- The average import growth for imports from the EU averaged 5.4 percent.
- Kenya's exports to the EU increased from USD 1,183 million in 2009 to USD 1,215 million in 2013, this translated to approximately 3 percent increase, or an annual average increase of 0.6 percent.
- Kenya has a negative trade balance with the EU of USD -1,181million in 2013

**Table 1: Top Products Exported /Imported by Kenya From...**

Category	Exports to ...	Imports from...
<b>China</b>	Coconut; Oil seeds and oleaginous fruits; Tea; Dried leguminous vegetables; Citrus fruit, fresh or dried  Waste and scrap, of copper; Tanned or crust hides and skins; Manganese ores and concentrates; Petroleum oils and oils obtained from bituminous minerals; Waste and scrap, of aluminum	Onions, shallots, garlic, leeks; Tomatoes, prepared or preserved; Seeds, fruits and spores, for sowing; Cinnamon and cinnamon-tree flowers; Vegetable saps and extracts.  Diodes, transistors and similar semiconductor devices; Tanks and other armoured fighting vehicles; Refrigerators, freezers and other refrigerating or freezing equipment; Tubes, pipes and hollow profiles, seamless, of iron or ; New pneumatic tyres, of rubber
<b>US</b>	Coffee; Coconuts, Brazil nuts and cashew nuts; Cut flowers and flower buds; Fruit juices; Vegetable waxes, beeswax, other insect waxes and spermaceti.  Women's or girls' suits, ensembles, jackets, blazers, dresses, skirts, divided skirts, trousers; Mineral fuels, mineral oils and products; Line fishing tackle; Telephone sets, Coloring matter of vegetable or animal origin; Extracted oleoresins	Grain sorghum; Dried leguminous vegetables; Margarine; Seeds, fruits and spores, for sowing  Machines and mechanical appliances having individual functions; Telephone sets, ; Parts of aircraft and spacecraft ; Surveying, incl. photogrammetric surveying, hydrographic, oceanographic, hydrological, meteorological ; Travel sets for personal toilet, sewing or shoe
<b>EU</b>	Cut flowers and flower buds ; Tea; Leguminous vegetables; Fruits, nuts and other edible parts of plants; Dates, figs, pineapples, avocados, guavas, mangoes;  Tanned or crust hides and skins ; Unmanufactured tobacco; Vermiculite, perlite and other mineral substances; Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral; Articles and equipment for general physical exercise, gymnastics, athletics, other sports.	Chocolate and other food; Live plants; Cane or beet sugar; Olive oil  Instruments, apparatus and models designed for demonstrational purposes, e.g. in education; Plastics and articles ; Printed circuits; Parts and accessories; Reaction initiators, reaction accelerators and catalytic preparations.

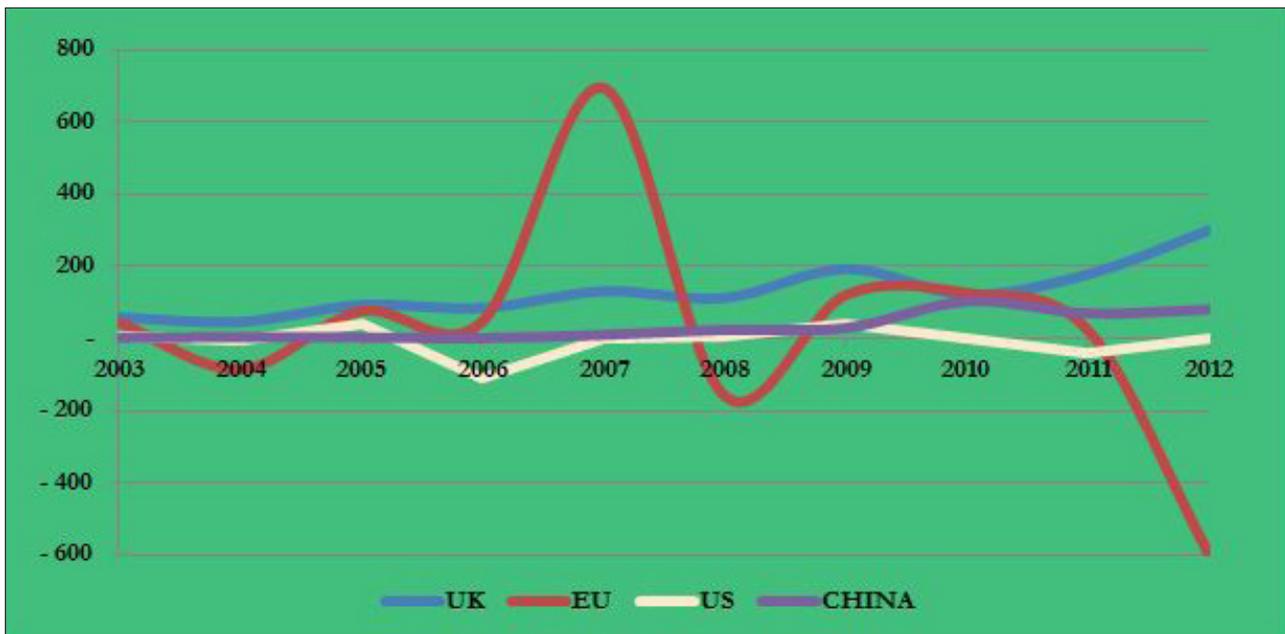
The value of products that Kenya is exporting to the EU and China vis-a-vis the imports explain the negative trade balances (Table 1). Of concern is the fact that vegetables and live plants are being imported from China despite these products being available within Kenya's borders.

### 3.0 Investment Trends

In order to understand the investment trends, it is important to distinguish what FDI inflows or FDI stocks mean. FDI inflows are the values of inwards direct investments made by non-resident individuals in a country. The net investment flows are obtained when the liabilities are netted out of the assets invested. FDI stocks measures the level of total direct investments, using equity and net loans. In the case of outward FDI stock, this is the value of resident investors' equity in and net loans of enterprises in foreign countries. Inward FDI stock is the value of foreign investor equity in and net loans to enterprises for residents in the reporting country.

Comparing the net FDI inflows for the three countries: net FDI inflows from China to Kenya increased from USD 68 million in 2011 to 79 million in 2012. For the US, net FDI inflows to Kenya in 2011 were USD -40 million and this went to 0 in 2012. Disaggregating the EU data and having the UK on its own given the imminent exit from the EU, for the United Kingdom, the FDI inflows was USD 101 million in 2011 and decreased to -9 million in 2012. For the rest of the EU, the net FDI inflows increased from USD 17 million in 2011 to USD 45 million in 2012.

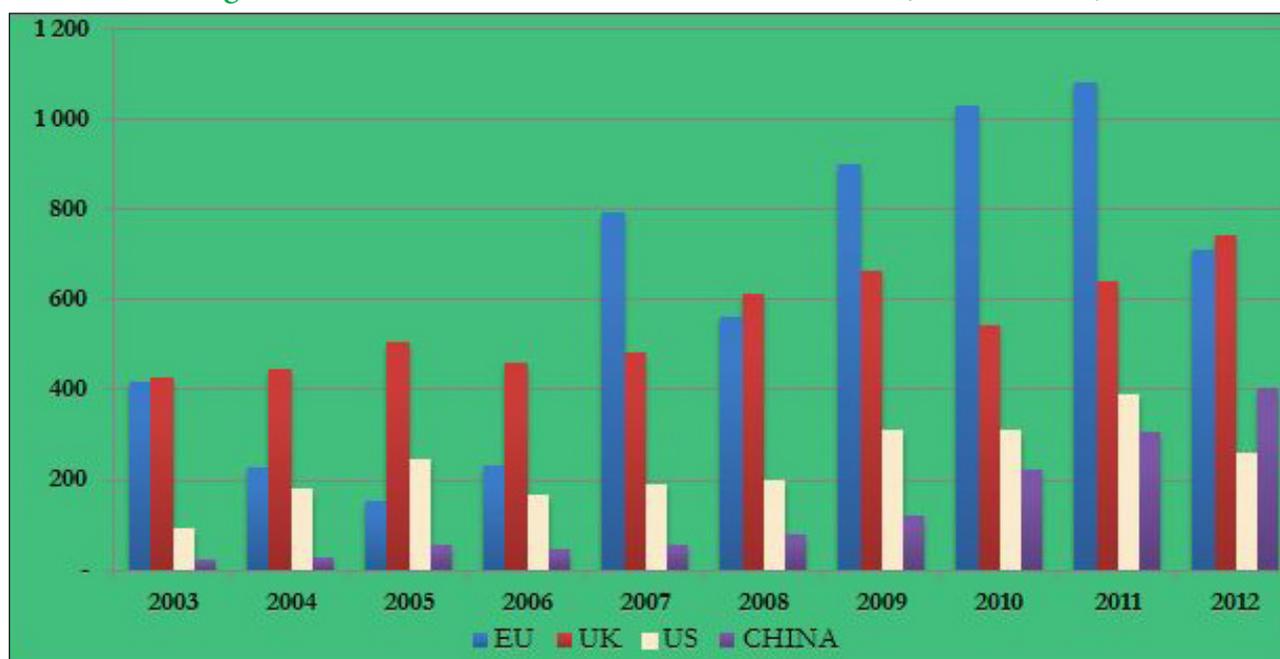
Figure 2: EU, US, China and UK Net FDI Inflow Trends (Million USD)



Source: UNCTAD 2014



Figure 3: EU, US, China and UK FDI Stock Trends (Million USD)



Source: UNCTAD 2014

FDI stock inflows from China in 2012 to Kenya was worth USD 403 million, the United States USD 259 million and for the EU it was worth USD 1.5 billion, of which the United Kingdom has investment stocks worth USD 841 million, France -USD 315 million, Netherlands USD 135 million, Switzerland USD 230 million and Belgium USD 32 million.

#### 4.0 Correlating FDI Inflows and Stocks to Kenya's GDP

A rudimentary examination of the correlation between FDI inflows and stocks from the three countries and Kenya's economic growth shows that the Chinese FDI inflows are strongly correlated to Kenya's GDP growth and ranks top, if one compares the US, UK and EU. The EU and US FDI inflows do not positively affect Kenya's GDP growth. A review of the FDI stock shows that the UK and EU's FDI stocks are strongly correlated with Kenya's GDP growth, while the United States and China rank much lower.

Table 1: Top Products Exported /Imported by Kenya From...

Correlation	FDI Inflows	FDI Stock
UK	0.205	0.870
EU	-0.226	0.760
United States	-0.221	0.420
China	0.543	0.425

#### 5.0 Discussion

Given that China is the new entrant in Kenya's development arena, there are more concerns about China as compared to other development partners. From a civil society perspective, some of the factors affecting Africa - Asia trade include:

- Border measures largely grouped into tariffs and Non-Tariff Barriers.

- Behind the border measures which are the prevailing conditions in the domestic markets.
- Trade facilitation, which affect trade between borders.
- Factors to be addressed so as to enhance complementarities between trade and investment

China is viewed by some African countries as a competitor within the country, and is seen to undermine African growth, since it displaces African products from the market. Some view China as the new colonizer, who is harboring a goal to supplant western influence and enforce its geostrategic control. China's activities are seen as primarily extractive in nature and simply repletion of European colonizers' activities. On the contrary, China is seen as less intrusive especially in the area of development financing, they give minimal conditionalities as compared to the EU and US. Others view China as a development partner, whose interactions will result in both parties mutually benefiting. It is however feared that the non-interference policy is likely to hamper political and economic reforms in Africa. Furthermore, China is perceived to sustain undemocratic governance practices coupled with human rights violations.

From a private sector perspective, it is perceived that China is likely to cushion Kenya from the imminent Brexit, there were however concerns that the unmatched increase in Chinese FDI stock could put the country in the risk of a major fall in the FDI stock. The upsurge of low priced products from China could in turn affect Kenya's local industry making Kenya too reliant on Chinese imports. Under governance, Transparency International (TI) has termed China as the second highest country, among 28 countries, likely to bribe host government for tenders, which is contrary to practices in their own country whereby they could be executed for such practices. They have a "free for all" condition outside their country. Employment creation for Chinese projects in Kenya remains questionable. A National investment policy should be updated where investment policies are put in place to manage FDI in the country in a mutually beneficial manner. The Rwanda Government has put in place a sound investment policy, which dictates where foreign investment should be directed in the country with clear guidelines on the same. In drawing valuable lessons, it was suggested that Kenya should develop a local content and investment policy. The role of the Chinese in developing local entrepreneurs is dismal; therefore opportunities for technology transfer should be pegged in the national local content policy.



## 6.0 Conclusion

The East or West question is more of a political debate than an economic one. China, EU and US are development partners with unique opportunities that cannot be easily substituted by other development partners. Each partner has a policy framework from which they operate and pursue economic diplomacy.

Kenya is having a growing negative trade balance with China, however, Chinese FDI inflows have strong correlation with the country's GDP growth. A review of statistics for the last three years shows that the UK FDI inflows to Kenya and the corresponding stocks have been increasing. However, the FDI stock has a stronger correlation with Kenya's GDP growth as compared to the FDI inflows. The US FDI inflows are lower than those of the Chinese and the UK, these inflows are negatively correlated with Kenya's economic growth, and while the FDI stocks positively influence economic growth.

Even though China is becoming a major development partner, there are concerns over whether there will be mutual benefits for both countries in the partnership. Secondly, there is the risk of stagnation in policy reforms especially where the partnership with China is geared towards achieving certain socio-political outcomes that do not have an overall positive effect in the economy. Lastly, there is a major concern for technology transfer amidst the growing Chinese FDI stock in Kenya.

## Trade Notes

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The Trade and Development Programme aims to be an influential actor in Kenya's trade negotiations, policy formulation, reforms and impact assessment.

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