The South African Institute
of International Affairs

## Business in Africa Research Project

# East Africa's Hub

# The Experience of South African Firms Doing Business in Kenya

Judi Hudson

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# About the Author

Based in Johannesburg, Judi Hudson consults to the FinMark Trust and Technoserve and lectures to MBA students at the Milpark Business School. When she was policy manager at the Small Business Project, Judi focused on the regulatory constraints facing private sector development in South Africa, paying particular attention to small and medium–sized enterprises, viewed in an international context. Judi was a senior research fellow at Kings' College, London University, and senior research co-ordinator at the Centre for Development and Enterprise. She was awarded a master's degree in Political Science from the University of Natal, and subsequently became a lecturer in that department.

## About the SAIIA Business in Africa project

This is the eighth country case study in a comprehensive examination of business conditions prevailing in Africa, conducted by SAIIA's Business in Africa project. The report forms part of a series of country and sectoral studies undertaken with a view to extrapolating specific policy recommendations for African governments on how to create a more supportive business environment in Africa.

The New Partnership for Africa's Development (Nepad) initiative emphasises the critical importance of the private sector to the continent's economic development. South Africa's expanding track record as a significant and, even more important, a fellow African investor is a notable indicator of business confidence in the future of the continent. It is also paving the way for the private sector to play a stronger role in Africa's advancement.

Although it is generally assumed that South African investors are less averse than others to taking risks, in view of their knowledge of, and proximity to, the African market in terms of appropriate technology and products, the SAIIA Business in Africa project aims to establish whether this is indeed the case. Moreover, an aim of this research is to identify critical areas in which reform is essential if Africa's private sector is to contribute to growth.

The Business in Africa project is headed by Neuma Grobbelaar, the Director of Studies at SAIIA.

The following reports have been published by the project thus far.

Games D, *A Preliminary Survey: The Experience of South African Business in Africa*, Business in Africa Report 1, SAIIA, 2003.

Grobbelaar N, '*Every Continent Needs an America': The Experience of South African Firms doing Business in Mozambique*, Business in Africa Report 2, SAIIA, 2004.

Games D, *An Oil Giant Reforms: The Experience of South African Firms doing Business in Nigeria*, Business in Africa Report 3, SAIIA, 2004.

Besada H, *Glimpse of Hope in West Africa: The Experience of South African Firms doing Business in Ghana*, Business in Africa Report 4, SAIIA, 2005.

Grobbelaar N & K Tsotetsi, *Africa's first Welfare State: The Experience of South African Firms doing Business in Botswana*, Business in Africa Report 5, SAIIA, 2005.

Sayagues M, *Golden road to Timbuktu: The Experience of South African Firms doing Business in Mali*, Business in Africa Report 6, SAIIA, 2005.

Besada H, *Meeting the Sphinx: The Experience of South African Firms doing Business in Egypt*, Business in Africa Report 7, SAIIA, 2006.

Games D, A *Nation in Turmoil: The Experience of South African Firms Doing Business in Zimbabwe*, Business in Africa Report 8, SAIIA, 2006.

# Methodology and Rationale

The World Development Report 2005 defines *the investment climate* as 'the many location specific factors that shape the opportunities and incentives for firms to invest productively, create jobs and expand'. Within this context, the experiences of companies become pivotal to an understanding of the investment opportunities and challenges and the related government policies and actions of a country. This view is taken as the point of departure for the report.

The researcher's findings are based on in-depth interviews with representatives of 21 South African companies that are currently doing business in Kenya, or contemplating it, or have recently closed down their operations in that country. The objective of the interviews was to elicit information on their experiences of the Kenyan business environment. Follow-up interviews were also conducted in South Africa with some businesspeople working in the head offices of those subsidiaries. The interviews, which lasted approximately an hour each, were based on a semi-structured questionnaire that had been designed in consultation with the management team at the South African Institute of International Affairs (SAIIA).

The range of companies approached included firms in the financial services, retail, franchising, insurance, telecommunications, services and tourism industry sectors. The in-depth discussion covered a wide spectrum of subjects, ranging from general perceptions of the investment climate in Kenya and the types of investment made, to what were perceived as the main constraints in the operating environment, to interviewees' opinions on the major challenges and opportunities connected with doing business there. The interviewees were also asked for general recommendations to both the Kenyan and South African governments on how to boost private sector development in Kenya specifically, and on the continent in general. The respondents were also invited to discuss their perspectives and experiences in terms of South African companies operating in Kenya, and to impart the key lessons learned.

The views of a number of Kenyan policy analysts and business association members were also canvassed, in order to explore their views of South Africa's expansion into Kenya — the strengths, weaknesses and areas of concern. It was also considered necessary to consult important members of the business community and commentators in Kenya whose opinions are not shaped by the South African corporate perspective. These interviews were supplemented by others conducted with a range of representatives of government departments and donors involved in this field. Overall approximately 41 interviews were carried out. The research interviews for this report started in the first half of 2005 and work was completed on this report by mid-2007.

No agency in Kenya has a mandate to collect data on foreign direct investment (FDI), although the Investment Promotion Centre, Central Bank of Kenya and Central Bureau of Statistics can provide some information. Kenya does not keep comprehensive records of the value of FDI by sector and industry, and investors are not required to liaise with the Investment Promotion Centre. As a result, this report is of an exploratory nature.

Additional information was obtained through semi-structured detailed interviews, combined with a literature review. The latter included material provided by the Kenya Institute for Public Policy Research and Analysis (Kippra), Transparency International–Kenya, the Investment Promotion Centre in Kenya, the World Bank's *Investment Climate Assessment*, the

UNCTAD *Investment Policy Review*, and the Economist Intelligence Unit.

The overall objective of the study was to locate some of the challenges and opportunities related to doing business in Kenya for South African companies, to identify some of the mistakes made and to convey the key lessons these firms have learnt. It is also intended to make both the Kenyan and South African governments more cognisant of the nature of the investment environment, and in this way to contribute to improved policies and more active dialogue among the parties concerned.

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# Executive Summary

Few could have predicted the speed with which South Africa has become the largest investor in the rest of Africa, eclipsing even the recent increased interest shown by investors from other continents. This 'rush' to expand into African countries has been described as 'one of the biggest economic phenomena of the last decade'.[1] Once a pariah state, South Africa now 'seems poised to dominate the continent that once shunned its products and leaders'.[2]

The situation is somewhat different in Kenya. In effect, that country has managed to keep the South African business heavyweights at arm's length. The experiences of South African companies doing business in Kenya show us that we cannot separate the successes from the problems of doing business in Africa. Indeed, some Kenyans have perceived some of the efforts at economic penetration made by South African corporations as aggressive. The clash between local and South African firms reached its peak in the widely reported 'beer wars', in which South African Breweries eventually lost out to Kenya Breweries. South Africa's Metro Cash and Carry outlet in Kenya closed its doors in March 2005 after eight years of failing to make a profit. The more than 120 stores Shoprite Checkers has in 15 African countries outside South Africa do business that accounts for only 12% of the group's turnover.[3] But while this chain has registered a company in Kenya, strong levels of competition from established local businesses in a market that is smaller than South Africa's have reportedly

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1 Quoted in Christianson D, 'South Africans doing business in Africa: The new imperialists', *Enterprise*, December 2004, p.78.

2 *New York Times*, 17 February 2002.

3 Quoted in Christianson D, *op. cit.*, and *Business Day*, 25 August 2005.

prevented it from opening any stores there. Again, while MTN International's returns from its operations in Africa overall entered the profit column in 2002, a full two years ahead of schedule,[4] it did not succeed in Kenya.

Despite these setbacks, Kenya remains an attractive investment destination for many South African companies. Interviewees pointed to a range of factors that encourage investment into Kenya. These include saturation in the local market; the desire to 'extend our African footprint'; strategic positioning for further expansion into Africa; and improving brand recognition. Some investors wanted to improve their capacity to serve their South African clients with operations in East Africa; some pointed to a market of an appropriate size for their products in Kenya; others wished to take advantage of the well-established industrial base and high level of skills which make Kenya more attractive than its neighbours.

Moreover, Kenya was seen as a springboard into the East African region. Especially from an education, skills and labour point of view, Kenya was regarded as the 'natural entry point' to the markets of its landlocked neighbours. Business investors were also attracted by the availability of educated and enterprising people in Kenya. Another advantage was the fact that Kenya had never been through a socialist phase and therefore was not anti-capitalist, but markedly business-friendly. Some interviewees also pointed to Kenya's topographical beauty and climate as factors that have great commercial potential, particularly to investors in the agriculture and tourism sectors.

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[4] Daniel J, Naidoo V & S Naidu, 'The South Africans have arrived: Post-apartheid corporate expansion into Africa', in *State of the Nation: South Africa 2003–2004*, Daniel J, Habib A & R Southall, Human Sciences Research Council, 2003, p.385.

However, Kenya presents a number of logistical challenges that act as constraints on investor enthusiasm. It is important to recognise, however, that not all businesses are affected in the same ways. The type of sector, the size of the firm, how long it has been in operation in the Kenyan environment, whether or not it has a local partner all affect the way a South African enterprise experiences the Kenyan environment. Notwithstanding these differences, the representatives of companies who were consulted during the course of this research study raised the following areas of concern.

- Infrastructure, particularly the poor condition of roads, the inadequacy of the energy supply and the sluggish pace at which goods were processed through the main port, was seen as the most troublesome obstacle to doing business in Kenya. The cost of electricity in Kenya is reportedly four times that of electricity in South Africa.
- The next most common criticisms concerned the high cost of duties and a difficult administrative environment as far as businesses are concerned. The greatest frustrations in the latter were excessive red tape, vague regulations that are open to varying interpretation, and their by-product, corruption.
- Crime had escalated, although not to the same extent as in SA, and had become a cause for concern.
- Apart from the 'hardware' component of the investment climate, there is also the 'software' (the human element). Wrangling in the political arena and political uncertainty (both of which can affect regulatory arrangements) were raised as areas that were troublesome, given that they hamper long-term planning and can alter the viability of projects without warning.

- While the involvement of South Africa's business sector in the Kenyan economy is desirable, and may well assist the private sector to play a more significant role in the continent's economic development, several instances of blatantly anti-South African sentiment were reported. Kenyans resent what they perceive as the excessive volume of South African investment. They have accused South African companies of being patronising, even arrogant, and of not wanting to work with local partners.
- Some South African companies reported having encountered difficulties with Kenyan partners who let them down at the last minute.

On the last two of the above points, while there is the uncomfortable possibility that competitors in Kenya might have been tempted to promote their own interests by exaggerating what South African companies are doing, there may also be room for improvement in the way South African enterprises operate in Kenya, and perhaps elsewhere in the rest of Africa. They need to make a greater effort to understand and accommodate local sensitivities, and take cognisance of local customs and business practices. South Africa could be in danger of acquiring an image similar to that of the 'ugly American' that Uncle Sam continues to project in Latin America and the Caribbean.[5]

As the stronger economy, South Africa has a complex economic role in East Africa, and on the continent as a whole. The experience of South African firms doing business in other African countries raises a number of fundamental questions. To what extent has South Africa become an economic hegemon

[5] See Hudson J, 'Neo-colonialism or development? South Africa's economic role in Africa', article in forthcoming book by the Centre for Conflict Resolution, Cape Town.

in Africa? Are South African companies taking out more than they put into other African countries, dominating markets to the detriment of local industries? How can positive rather than exploitative outcomes of this expansion into the continent be maximised?

There is little strong research-based evidence on which to draw firm conclusions. Evidence is often patchy, contradictory and over-reliant on anecdote and reported 'perceptions'. Nevertheless, sufficient data have been generated to justify the drawing of some tentative conclusions. This report attempts to answer these complicated and far-ranging questions from the perspective of South African firms doing business in Kenya. The findings inform the policy recommendations made in the report to help shape a more positive relationship between South Africa and Kenya, while also proposing key recommendations for improving the business environment in Kenya.