RESEARCH NOTES

Missing the GO in AGOA? Growth and constraints of foreign direct investment in the Kenyan clothing industry

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This research note presents findings from a small-scale survey of foreign affiliates in the Kenyan clothing industry. While a sizeable clothing manufacturing industry has re-emerged in Kenya as a result of the African Growth and Opportunity Act of the United States, the findings highlight the constraints on the growth of the industry and the development of local backward linkages. Despite the diverse growth aspirations expressed by the foreign-owned clothing manufacturers in Kenya, "growth and opportunity" appear to be missing in the industry. The characteristics of the parent transnational corporations and the shortcomings of the government in Kenya have constrained the generation of significant benefits from foreign direct investment in this industry.

1. Introduction

The opportunities for industrial upgrading and local economic development in Sub-Sahara African (SSA) nations may conceivably have expanded markedly with the enactment of the African Growth and Opportunity Act (AGOA) of the United States, which, under certain conditions, allows preferential United States market access to SSA producers. In this research note, we assess the growth and development impacts of the recent foreign participation in the clothing industry in Kenya. After the decline of Kenya's largely indigenous and local-market oriented clothing industry that had developed before the 1980s, the industry has recently re-emerged as an export-oriented, foreign-owned industry as a direct result of the AGOA. Despite a sizeable industry, which employed 37,000 workers at its high point in 2003 (McCormick et al., 2006), the opportunities for industry growth, upgrading and wider economic development impacts in Kenya remain elusive.

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Although there have been a number of studies on FDI in Kenya – notably Langdon (1981) and UNCTAD (2006) – the subject remains relatively under-researched. For the clothing industry in Kenya, a number of studies have been undertaken following its re-birth in recent years (Ikiara and Ndirangu, 2003; McCormick et al., 2006). The findings presented here add to these studies by considering more explicitly the FDI component of the industry and its wider impacts.

The (re-)growth of the clothing industry in Kenya with the advent of the AGOA is an interesting case to study when exploring the developmental impacts of FDI. The AGOA is a non-reciprocal trade agreement between the United States and 38 SSA countries, which covers around 7,000 product lines. The original agreement ran from 2000 to 2008 and was subsequently extended to 2015 (Office of the United States Trade Representative, 2007). SSA countries seeking to benefit from export to the United States market under the AGOA are obliged to make progress towards market reform, protection of property rights, maintenance of the rule of law, removal of impediments to United States trade and investment, reducing poverty, policies to combating corruption, and compliance with international standards covering workers rights (McCormick *et al*., 2006). Twenty-six of the 38 countries in the region are eligible for market access benefits related to clothing manufacture and 17 for hand-made clothing items.

At first glance, FDI in the Kenyan clothing industry presents some *a priori* grounds for optimism with regard to its positive effects on the local economy through participation in global commodity chains (GCCs). Kenya has traditionally been a hub for the East African region (Kaplinsky, 1978, p. 4) in terms of flows of people, goods, services and investment – although a great deal of complacency on the part of the national government has seen Kenya and Nairobi's role challenged somewhat in recent times in terms of FDI flows (UNCTAD, 2006; Phelps et al., 2007). Moreover, the country has been host to a sizeable clothing industry, the seeds of which were sown by foreign investment under British colonial rule prior to the Second World War. The industry flourished under the import substitution regime instituted with independence. The protected, import substitution-based clothing industry reached its peak in term of employment in the early 1980s. Just as significantly, by this time, a cotton-textile supply industry had developed. The industry subsequently collapsed, but one might expect that the industrial experience and institutional infrastructure from the period offer some advantages in the re-emergence of the clothing industry stimulated by the AGOA. However, the sizeable FDI in the

Kenyan clothing industry in recent years has failed to generate wider economic impacts. It is a story that underlines some of the difficulties SSA nations face in participating in the international economy.

In this paper, we trace the missing "GO" (growth and opportunity) in AGOA in the Kenyan clothing industry to the parent company, customer relationship, the uncertainties associated with the AGOA itself, and both general and industry-specific failings of government and associated institutions in Kenya. Significant constraints upon the growth of the Kenyan clothing industry and the development of local supply chains become apparent from the findings.

This paper is organized as follows. In the next section, we provide a brief resume of the theoretical issues motivating the study of FDI in the Kenyan clothing industry. We outline the research method used in section 3. Then, we present empirical findings from our questionnaire survey and interviews. The description of the companies interviewed are reported in section 4 and their plans for further expansion in section 5. Section 6 draws inferences on the constraints the industry faces, and section 7 discusses the absence of backward linkages. Section 8 concludes.

2. Growth and growth constraints of FDI

The contribution of FDI to a host economy partly depends on the evolution of the foreign affiliates over time within their parent organizations. In keeping with early studies documenting the negative aspects of host economies' dependency on the foreign-owned sector, early analyses of the contribution of FDI to host economies treated employment change at foreign affiliates in terms of growth being "allocated" from the parent companies, perhaps on the basis of product life-cycle considerations (Firn, 1975). In contrast, more recent work within the international business and economic geography literature has concentrated on differences among TNCs according to their resources and capabilities. Along with this perspective has come something of a celebration of the varied contribution of individual affiliates to parent TNCs' performance. Recognition of the role an affiliate plays (Young et al., 1988) implies different mechanisms of allocation by parent companies and/or competition among affiliates as well as ultimately distinct evolutionary trajectories of individual affiliates (Birkinshaw, 1997, 1999; Fuller and Phelps, 2004; Phelps and Fuller, 2000). The emphasis within this literature is less upon numerical changes in employment and more upon *qualitative* changes at affiliates, as reflected in their acquisition or loss of broader capabilities.

The perspective of "allocated growth" that prevailed in the 1970s and early 1980s can be captured and analysed through conventional employment changes associated with the foreign-owned sector (e.g., Stone and Peck, 1996). However, the number of employees alone reveals little about the *qualitative* dimension of employment change. The issues that have become central to the capability perspective of the TNC and its affiliates are more adequately captured through the examination of its growth and constraints. Working in the context of the widespread industrial decline in the United Kingdom, the pioneering work by Massey and Meegan (1982) classified employment change into the categories of "rationalization", "technological change" and "intensification". To these categories, Turok (1989) later added "extensive growth", "stagnation" and "product development".[1] Four of these categories imply some growth in output although not necessarily in employment, drawing attention to qualitative changes in the nature of activity at manufacturing establishments. Although we do not use these categories of employment change, the research presented below draws on this work when seeking to understand the growth and constraints associated with FDI in the Kenyan clothing industry.

Furthermore, there has been a renewed interest in the specific contributions that host environments make to the possible acquisition (or loss) of capabilities at individual TNC affiliates. Consideration of the host environment's contribution to affiliates' position within the parent organization has extended beyond "conventional" location advantages, such as labour costs and accessibility, to identify a role for the broader supporting institutional environment provided by universities, technical institutes and even specific programmes for supplier development or after care that impact positively on affiliates' capabilities. However, the precise contribution of such host economies' "institutional capacity" is still open to debate (Fuller and Phelps, 2004). Moreover, questions remain

[1] Turok (1989, p. 5) defines these components in the following ways. Rationalization involves "a straightforward cut-back in production capacity and may involve complete plant closure". Technological change involves "changes designed to increase labour productivity with a major new investment and substantial reorganization of production techniques". Intensification implies "changes intended to increase labour productivity but without large scale new investment or major reorganization of production techniques". Extensive growth is "the expansion of production through the provision of additional production capacity of the same type as existing techniques". Product development is the "designing and development of new commodities and the identification of new markets". Stagnation is a situation "where output and employment are broadly unchanged".

over the manner in which such host economy locational advantages and institutional capacities are structured by elements of the international trade and investment regulatory environment such as the AGOA, which forms the context to our discussion in this research note (see also Phelps et al., forthcoming). In the research findings that we present below, we discuss these considerations regarding the contribution of the host environment to the growth and constraints facing FDI in the clothing industry in Kenya.

3. Methodology

This research note draws upon original research carried out in 2004 focusing on the volume manufacture of clothes in Kenya, which has been the preserve of foreign affiliates.[2] The research as a whole was designed to examine the economic impacts of FDI in the clothing industry in Kenya in terms of the characteristics of manufacturing establishments, patterns of assistance received by these establishments from customers, parent companies and agents, local purchasing linkages, other linkages to local institutions (findings on which are reported in Phelps et al., forthcoming) and the plans for growth and constraints identified by foreign-owned establishments which we discuss here.

Our case study makes use of both extensive and intensive research methods (see Sayer and Morgan, 1985). A survey of establishments was conducted, mainly through face-to-face interviews and, in a few instances, through telephone and fax. A survey of all volume clothing manufacturing establishments was thought necessary in order to give a balanced picture of the aggregate economic impacts, growth aspirations and growth constraints facing the industry. The intensive method consisted of a series of tape recorded face-to-face interviews, which, while eliciting information for the above factual survey, also sought to gain greater explanatory insight into these aggregate trends. Quotations from respondents in these interviews are used to illustrate the key findings.

First, extensive empirical research by means of a questionnaire survey was undertaken to gather data on direct and indirect impacts of clothing manufacturing establishments, the ownership and markets, and upstream and downstream relationships, and finally the growth and

[2] From the Kenyan perspective, craft based indigenous clothing manufacturing, rather than volume manufacturing, may represent a better strategic opportunity for exploiting the opportunities presented through the AGOA (McCormick et al., 2006).

constraints anticipated by the management at these establishments. A survey of 23(66%) of the 35 identified clothing firms operating in the industry just after its recent high-water mark of 2003 was conducted. The list of 35 clothing manufacturing companies was derived primarily from the Export Processing Zone Authority (EPZA) of Kenya and cross-checked with other available business directories and on location. Some discrepancies between the figures for overseas equity participation in the industry provided by the EPZA and those obtained at interview were noted. Nevertheless, all but two appeared to have substantial equity participation from overseas companies or individuals and hence could be classed as foreign affiliates (see table 1 and further discussion below). Most of these responses were obtained at face-to-face meetings, which, for practical reasons, were therefore skewed towards those establishments operating in and around Nairobi and Mombasa. We can only presume that the general constraints on growth reported here will have been more severe elsewhere than in the two largest and most developed city/region economies of Kenya.

Second, semi-structured interviews with these 23 firms and 25 interviews with government ministries, the investment promotion agency, development banks, industry representative bodies, international organizations and others provided expert opinions on the development impacts of the clothing industry in Kenya. The positions of the interviewees and those who provided factual information as part of the survey varied, although all interviewees were in a senior management position such as general manager, financial director or purchasing director.

In the remainder of this research note. we report on the most relevant part of these interviews.

4. Activities, employment, ownership and markets

Before considering the constraints on the growth and linkage development of the Kenyan clothing industry, we present a description of FDI in the industry.

4.1 Employment

The establishments we surveyed covered 23 of the 35 known establishments and 26,642 of the estimated 32,000 employees in 2004 (McCormick et al., 2006). As such, the survey covered a good part of the known private sector actors in the industry at the time (table 1).

Table 1. Ownership, age and employment of clothing manufacturing companies in Kenya

Company	Ownership	Date established	Direct production employees 2004	Total employees 2004
Rising Sun EPZ Ltd	Sri Lanka	2002	1,400	1,460
Upan Wasana EPZ Ltd	Sri Lanka	2001	1,650	1,690
Indigo Garments EPZ Ltd	India	2001	1,500	1,580
United Aryan Resources EPZ Ltd	India	2003	2,300	2,350
Storm Apparels (MUB)	Kenya	2004	735	785
Falcon Apparels (MUB)	Kenya	2003	200	225
Protex Kenya EPZ	Taiwan Province of China (90%)/Kenya	2001	1,150	1,200
Apex Apparels	India /Bangladesh	2003	2,156	2,342
Sahara Stitch EPZ	United Arab Emirates (60%) / Kenya	2001	835	850
Sinolink Kenya EPZ	China	2001	1,016	1,100
Ashton Apparels	India (located in the United Arab Emirates)	2001	2,700	2,800
KAPRIC1 Apparels	Hong Kong (China)	2001	1,820	2,000
Birch Investments (Kapric2)	Hong Kong (China)	2001	900	900
Shin Ace Garments	Taiwan Province of China	2003	789	800
Blue-Bird Garments	India (located in the United Arab Emirates)	2002	575	600
Senior Best Garments	China	2002	820	850
Kenya Knit Garments	China /Taiwan Province of china	2001	1,905	1,920
Ancheneyar EPZ	Sri Lanka	2004	500	513
Chandhu EPZ	Kenya/foreign	2004	188	217
Mirage EPZ	India	2002	1,175	1,200
MRC (Nairobi) EPZ Ltd	Sri Lanka	2001	1,270	1,300
Rolex Garments EPZ Ltd	India	2002	897	950
Asia Resources EPZ Ltd	Sri Lanka	2004	683	700
Totals			27,164	28,332

One initial observation that can be made from table 1 is that these factories are large in size, employing several thousand workers. All but two operations employed over 500 people. Our survey also sought the breakdown of the total employment figure into management and direct production components. The numbers of direct production workers are also reported in table 1. The vast majority (96%) of the workers are involved in direct production. Despite the labour intensive nature of the industry, there is a sizeable number of white collar workers. However, interviews confirm that many of the key positions are held by expatriates from the home country of the parent TNC.

The majority of direct employment created in these large factories follows a pattern that is also quite familiar in older industrial regions of developed countries. The majority of direct production employees in these large factories are on casual or temporary contracts (see also MIGA, 2006) – with resultant implications not just for the job security for them but also labour relations and the generation of skills in the industry.

4.2 Products

A wide range of goods were produced by the companies surveyed, including sports clothes, shorts, t-shirts, woollen knits, track suits, pyjamas, ladies' tops and trousers – the latter two items being the most common. Two factories visited appeared to have become specialized as they produced denim jeans exclusively. All the respondents noted that the choice of products was dictated by the buying agents, the dealers or the parent companies with the product mix influenced by seasonal demand.

4.3 Activities

Within the wider clothing GCC, there are several distinct stages of production: conception, manufacture and delivery to the consumers. The research sought to identify not only the characteristics of FDI within the Kenyan clothing industry as nodes of activity but also wider upstream and downstream connections within a GCC. The questionnaire solicited information in relations to five stages: design, textile manufacture, garment manufacture, sales and marketing, and eventual packaging. Interviews and site visits provided additional details on important sub-stages involved.

Design of garments

Eighty-three per cent of the respondents did not carry out any garment design at their site. Instead, the end customer, the agent or buyers would specify the designs for the factory to produce a prototype. This would be sent to the customer for approval, after which an order would be placed for the factory to produce in a certain quantity. The remaining 17% carried out some design activity but only on a small scale, and these respondents were not significant players in the Kenyan clothing industry.

Garment manufacture

None of the companies surveyed were involved in textile manufacture – they externally procured all the necessary fabrics, mostly imported, either from a buyer-nominated supplier or from the parent company. The majority of these textile suppliers were located in the home economies of the parent TNCs – namely China, Hong Kong (China), Pakistan, Sri Lanka and Taiwan Province of China. The respondents confirmed that imported fabrics was often cheaper than locally-made fabrics.[3]

Two types of manufacturing can be identified. In the first type, companies do not purchase the fabrics; everything is provided for, either by the buyer/agent or the parent company. Their only task is to cut and make (C&M). These companies do not carry out any overseas marketing and have no direct links with their customers. In the second type, companies purchase all the fabrics and negotiate the prices with the customer. They then make the products and ship them to the customer. This is free on board (FOB) manufacture.[4] The profit margins attainable under different types of production vary as do the risks to producers.

Cutting, sewing and finishing

Within clothing manufacture, 100% of the companies carried out cutting, sewing and finishing. Cutting involves laying-out and measuring the fabrics into suitable sizes and then separating these into smaller cloth pieces to be joined up. In the small and medium-sized firms, all cutting appeared to be done manually with virtually no machinery involved. The larger enterprises had some automated operations. A company like Ashton Apparels had several such machines (straight knife cutters, band

[3] During interviews, company representatives noted that the overriding factor was not the cost, as the orders often came with conditions that fabric must be sourced from a supplier who had been quality certified by the buyer or customer. There are significant risks of an entire order being rejected should a company choose to source its own fabric later found to be sub-standard.

[4] Free on board manufacture – this is an international trade term where the seller is held responsible for delivering goods to a certain port, clearing through export control and loading these onto the ship. Once loaded they become the responsibility of the buyer.

knife cutters and end-cutter machines). They also employed a spreading machine and a mechanized marker-plotter.

Once cut, the fabrics are passed to the sewing floor. Here, the workers were organized into production lines comprising benches holding sewing machines. The majority of the sewing machines used were standard industrial models, with each factory having a range of single-needle, double-needle and multi-needle machines for different tasks. The most common brands used were Juki and Kansai models imported from Asian manufacturers.

The next stage involves fitting cuffs and collars, making button holes, over-locking, and adding snaps and bar tacks. Some tasks require use of additional machinery and staff training. The more customized garments undergo additional work, such as embroidery and sandblasting. Only about a quarter of the firms surveyed had the machinery to complete complex embroidery work, and some often had to sub-contract this task to other firms.

Once finished, the garments are laundered prior to packing. Most of the companies surveyed had in-house laundry facilities, which involved large, industrial washing machines, tumble driers, water extractors and drying equipment. The garments are then pressed to remove creases and checked for defects prior to bagging and packaging.

Packing

Once passed for quality, the garments are labelled, bagged and packed into boxes, stamped for traceability. By this stage, the products are usually ready to go straight to the shelves of the end customer, some of which are labelled and price tags attached. Once approved and verified by the customs representatives, export authorization is granted and the products are loaded onto ships at Mombasa port bound for the United States.

Sales and marketing

The bulk of the work carried out within Kenyan clothing factories is C&M; for the majority of enterprises, the sales and marketing functions are not conducted within the country. Only two companies reported having a marketing or buying office which directly sought orders overseas. For most firms, sales and marketing was done through their parent company in the home country or arranged by agents or brokers who liaised with the end customer.

4.4 Age

As table 1 confirms, all of the companies surveyed indicated that they had been established after the enactment of the AGOA in 2000. Only one clothing company surveyed indicated that they had existed prior to the AGOA. All of the companies surveyed were involved in clothing manufacture for which the AGOA represented major new export opportunities so that the re-birth of the clothing industry in Kenya has also been one of clothing manufacture rather than textile manufacture. Although as many as 35 textile mills continue to exist in Kenya according to one recent report (MIGA, 2006), these are moribund and uncompetitive as a local source of fabrics.

4.5 Ownership and the nature of investments from developing country TNCs

There exists a long history of Asian involvement in the East African economies and Kenya in particular. The roots of Asian involvement in business activities stem from labourers brought in from India to build the Kenya-Uganda railway under British colonial rule in the 1880s. These workers later set up small trade operations which evolved over time into dominant Kenyan enterprises (Himbara, 1993). These Kenyan-Asians have maintained relationships with their country of origin in Asia over generations, and with the recent industrialization of these Asian countries, the relationship has strengthened as it leveraged upon new and expanded corporate networks. Textile manufacturing was one of the earliest modern forms of manufacturing in Kenya, with the first textile plant being set up in the early 1930s by Indian investors. These early efforts were followed by similar investments and, post-1945, Asian merchant capital played a significant role in the diversification of the economy into manufacturing (Swainson, 1978, p. 40). The concentration of new Asian investment into SSA clothing industries, as facilitated by the AGOA, reflects some of these long-standing trade and investment interests as well as the global competitiveness of Asian clothing companies. It is part of a broader engagement of Asia as a major driver of trade and FDI with SSA (Jenkins and Edwards, 2006).

The home economies of the parent TNCs reflect these distinctive Asian trade and investment connections with the ultimate ownership residing in Bangladesh (8%), Hong Kong (China) (4%), India (17%), Singapore (4%), Sri Lanka (13%), Taiwan Province of China (17%) and the United Arab Emirates (17%). The ownership listed above and in table 1 is inferred from the authors' research, but the ultimate ownership of those companies is not always clear. Some of the difficulties in establishing the precise ownership status of Kenya-based clothing companies is a reflection of the obscure ownership structure of these firms and the marginal and transient nature of industrialization prompted by the AGOA.[5] The level of foreign equity participation varies. The various secondary sources available in Kenya indicated differing proportions of Kenyan ownership.

Three of the establishments surveyed indicated that they were independently owned (i.e. wholly Kenyan-owned single operation) but noted at interview that they had "sister companies" or related factories operating in various parts of Asia with whom they shared orders, ownership and management links. Here, their identity was given as Kenyan even though they had significant foreign equity participation. These sometimes obscure relations of ownership and control also appear to be partly due to differential tax and incentives status open to domestic and foreign companies.[6] This appears to be indicative of the "paper" rather than real nature of such joint ventures (Bräutigam, 2003, p. 460). It also highlights the contradiction between the expectations of developing countries regarding the potential benefits to be gained from FDI, and the potentially fluid nature of FDI stimulated through international trade and investment agreements.

With few exceptions, most of the new investment in the industry originates from Asian economies such as Hong Kong (China), Singapore and Taiwan Province of China, which might be regarded as the "semi-periphery" of the international economy (Henderson, 1989) by virtue of their role as "first tier" coordinators of GCCs in clothing (Gereffi, 1999). However, the expectations and cultural values these parent companies bring with them from their home countries appear to preclude

[5] Companies responded to this matter from different perspectives. Some respondents viewed this question as one questioning whether they owned their factories or whether these were owned by a separate, larger company. Yet others viewed the question in terms of their company's legal position in the country; whether they were registered as a Kenyan or as a foreign company, with the relevant legal liabilities assumed. Other respondents took the question to be one of control; whether they were stable, entities capable of making independent decisions or whether they were a subsidiary controlled through a head office.

[6] In Kenya capital tax rates for resident companies are 30% and 37.5% for subsidiaries of foreign owned companies. There is an incentive here for nominal local business participation to confer lower domestic rates of tax upon what ostensibly is FDI. Against this must be set the incentives offered to FDI such that domestic companies may establish and finance separate firms masquerading under a foreign identity [Interview FDI 12].

important indirect economic benefits, such as technology transfer (see also Lall, 2005, p. 1007). The nature of FDI by these TNCs appears to be efficiency-seeking in labour-intensive GCCs (UNCTAD, 2007, p. 160).

Other Asian TNCs (from countries such as Bangladesh and India) participating in the Kenyan clothing industry are newly internationalized on the basis of being "second tier" locations within clothing GCCs. Whilst these late-comer Asian TNCs have apparently attained the capacity to remain internationally competitive in the longer term (US-ITC, 2004 cited in Lall, 2005, p. 1015), their FDI in Kenya represents an initial, tentative step towards internationalization, rather than investment that constitutes part of a well-developed internationalization strategy. In a number of cases, the new Kenyan enterprises are run as branch-plants for capacity sub-contracting, with the parent company directly providing all the inputs and materials and managing both the sourcing and marketing ends of the production process. In this regard, it is doubtful that the Kenya-based affiliates could operate profitably without the ownership advantages derived from the parent company's networks. Instead, there is a case for arguing that the re-birth of the Kenyan clothing industry is a product of the recent expiration of the Multi-Fibre Agreement (MFA) and the preferential treatment granted as part of the AGOA (UNCTAD, 2006, p. 98).

The case of Apex Apparels located in the Athi River EPZ is typical of the vulnerability of the Kenyan clothing industry. Apex Apparels EPZ Ltd. is located within the Athi River EPZ and is one of the larger enterprises in the zone. At the time of the survey in 2004, it employed over 2,000 people. Apex Apparels has its parent company located in Dhaka, Bangladesh. It is one of six factories run by the parent company with the other five being located in the home country. The Kenyan operation is the newest of them, but its orders and marketing of products are handled through the home country. Partly as a result of this pattern, it is 100% reliant on the orders channelled through a particular buyer known to the parent company and sister factories in Bangladesh. The factory forms part of a relatively low-risk strategy of limited internationalization that augments capacity and profits of the parent company. The factory's existence is highly contingent upon the AGOA agreement and its renegotiation, with an interviewee suggesting that any major deleterious change in this respect would most probably result in complete closure [Interview FDI 8].

The extent to which the Kenyan clothing enterprises are an integral part of their parent companies' strategic direction is therefore questionable. These establishments can hardly be regarded as examples of strategic autonomy and capability sometimes developed at foreign affiliates of TNCs (Birkinshaw, 1999; Phelps and Fuller, 2000), nor are they territorially embedded. Their relationship to the parent company coupled with the terms of the AGOA and the low barriers to entry into the clothing industry mean that these investments are likely to be highly transient [Interview INST 10]. The marginal nature of the Kenyan clothing industry has been confirmed in a more recent study: McCormick et al. (2006) reported that just 22 enterprises remained in the Kenyan clothing industry in 2005.

4.6 Markets

All of the companies produced entirely for the United States retail market. Of the companies that agreed to provide information on their end customers, over 50% were producing for Walmart Stores, the largest retailer in the United States. Other customers for whom the factories were making products included JC Penney, Calvin Klein, Kmart, Target, Levis and Gloria Vanderbilt. These patterns are to be expected given the growth of the industry in connection with the AGOA, however, the strong focus on the United States market, to the exclusion of other destinations, such as the European Union or countries in the regional grouping, COMESA (Common Market for Eastern and Southern Africa), highlights the failure of the industry to diversify its market.

4.7 Dependency

Respondents at the surveyed companies were asked what proportion of their sales was accounted for by their single largest customer. The findings from the 20 companies which responded indicated a very high level of dependency: on average, 64% of sales were destined for the largest customer. Over half of the sales of almost all companies were taken by the largest customer.

Three companies indicated that they were entirely dependent upon a single customer. These companies are among the smallest operations surveyed, but even the largest and most technologically sophisticated of the clothing operations were highly dependent on their largest customer, as the case of Ashton Apparels indicates.

Ashton Apparels Ltd. is one of the largest garment manufacturing firms in Kenya. It is located in Mombasa's Jomu area where it runs three factories. The company has a regional head office in Dubai, the United

Arab Emirates, and strong links to the ultimate parent company in India. Ashton is one of the very few globally competitive operations in the Kenyan clothing industry. However, despite its size and sophistication, Ashton was, at the time of interview, dependent on orders from a single customer for 60% of the value of its sales [Interview FDI 11].[7]

The entrenched nature of the problems of dependency on a very limited number of customers for orders is an important constraint on the companies' further growth and wider economic development. These foreign affiliates in Kenya are caught between the parent TNC on the upstream side and the powerful customers in the West on the downstream. In the following section, we highlight the lack of spillover effects commonly thought to flow from both upstream and downstream sources.

5. Plans for growth

The questionnaire survey asked the companies to outline their future plans for the business in the medium term (3–5 years) with regard to the forms of possible expansion. Table 2 summarizes the results which indicate that the majority of respondents are seeking to expand in more than one way.

Table 2. Companies planning future business development

Forms of expansion being considered	Number of respondents (%)
Expansion of output	18 (78)
Installation of new equipment	14 (60)
Producing more expensive garments	12 (52)
Acquire /strengthen design capability	9 (39)
Improve worker skills	19 (82)
Diversify /expand customer base	17 (74)

Source: Authors' survey in 2004.

Since the clothing industry is widely recognized as labour intensive and low technology in nature, it is not surprising that a large proportion (72%) of establishments surveyed should be considering an expansion of output, as this can be achieved through "capital widening" – a quantitative increase using the same production processes, technology and labour skills. It is this form of expansion that has turned out to be the most significant effect of the AGOA on the clothing industry in Kenya.

[7] Nevertheless, it was reported in 2005 that new investment doubled employment at the factory to 5,000 (EPZA, 2005a, p. 17).

The AGOA provided significant opportunities for expansion through duty-free access into the lucrative United States clothing market. Initially, this expansion in output has come from the opening of new factories but once established an important form of growth has come from the addition of "more of the same" production processes. Thus, Mirage EPZ planned to add two new production lines utilizing similar machinery [Interview FDI 20]. Kenya Knit garments planned to establish another plant [Interview FDI 21].

More surprising is the large proportion of firms looking to make what might be regarded as forms of expansion which imply "capital deepening" – a *qualitative* change in production processes, technology and skills. Thus, high proportions of surveyed establishments seek to diversify their customer base (74%) and worker skills (82%). To the extent that establishments are seeking to make such qualitative enhancements to their business operations, the figures in table 2 provide grounds for optimism over the future development of the clothing industry in Kenya.

Sixty per cent of surveyed establishments suggested that they wished to introduce new equipment during the period 2004–2009. This is higher, but broadly in line with a figure of 43% of firms surveyed by KIPPRA in 2001 that had changed their machinery since the initial installation (Ikiara and Ndirangu, 2003, p. 62). The prevailing view was that the Kenyan clothing industry was not employing much new technology [Interview INST 22] with the KIPPRA report arguing that "the level of technology upgrading in the T&C sector in the country is low" (Ikiara and Ndirangu, 2003, p. 62). The figure of 60% found in this survey in the relatively short time-scale (3–5 years) involved indicates some further development in the capacity of the sector for technological upgrading. Several companies therefore planned to acquire more advanced technology, such as boilers and specialized embroidery machines [Interview FDI 15], washing facility for woollens [Interview FDI 18], an industrial laundry machine, embroidery machine and sandblasting equipment [Interview FDI 3]. The larger companies which already owned such equipment [Interviews FDI 11 and 14] represented this as a competitive advantage when tendering for orders, as it confirmed their technical competence in fulfilling intricate and detailed orders.

Smaller proportions of surveyed establishments were seeking to make more expensive or sophisticated garments (52%), introduce new equipment (60%) or improve their design capabilities (39%) – something that may be largely beyond their reach, given the importance of end customers to this process.

Improving workers skills emerged as a key concern among the firms, with 82% of respondents looking to develop their workers' capabilities. Some of the expected benefits from FDI include transfer of skills and management know-how, which is seen to benefit recipient countries through improved processes, superior standards and the diffusion of knowledge into the domestic economy (Blomstrom and Kokko, 1999). While many companies expressed their intention to raise the skill level, there has been little evidence of this occurring in the industry to date, which raises questions regarding the categories of skills companies intend to develop. The absence of knowledge transfer on the ground may indicate that this was more of an aspiration than a specific target. It also highlights the underlying complexities involved in effecting knowledge transfer. Complex relationships exist between the improvement of skills, on the one hand, and the issues of wages, industrial relations, the expectations of parent companies and the performance of their overseas affiliates in cultural settings quite different from those of their home country, on the other.

Some limited evidence of skills upgrading in the industry does exist. Certainly, there have been changes in the nature of jobs performed by local workers, with more of them moving into supervisory roles than was previously the case. As indicated by one ministry official, "there is some training occurring and skills development here; there is some evidence that Kenyans are moving up these companies' hierarchies" [Interview INST 4]. In companies like Protex EPZ**,** Kenyan workers held senior management roles, such as general managers, human resources managers [Interviews FDI 2]. Several companies had Kenyan personnel as their spokespersons, liaising with the press and unions. The majority, however, maintained expatriate staff in senior management and technical roles, especially those of quality inspection, merchandising, finance and some supervisory roles. As one interviewee explained, "the supervisory jobs are done by Asians here, even though locals can do this job at a cheaper rate … we must have Asian technical supervisors as they are internationally recognized" [Interview FDI 15].

Some basic training programmes take place at the EPZs. According to one company manager, these are organized jointly at cost to the companies involved [Interview FDI 12]. The existence of a labour pool with basic skills can be explained in part by the legacy of the clothing industry under the import substitution policy in the 1980s and the existence of a significant number of micro-enterprises. Other training institutions exist, such as the Kenya Textile Training College, Kenya Technical Training Institute and numerous city and village polytechnics, though there is little evidence of direct engagement of the companies with these institutions. More specific skills shortages cited were the lack of skilled workers to maintain machinery and technical specialists [Interview FDI 16].

Some companies have in-house designers (e.g. Upan Wasana), but the ability to come up with new designs independently in the prevailing mode of manufacture to customer designs may be less relevant than the ability to reproduce pre-set designs to exacting standards. The issue of design capability is, in reality, closely linked with the types of garments these companies manufacture. Currently, the products these companies manufacture remain fairly straightforward (t-shirts, trousers, sportswear) and tend to be low priced items in the United States market, although the companies interviewed did express a desire to produce garments that had more specifications, style, sophistication and fashion content as these paid more and improved the investors' margins [Interviews FDI 17 and FDI 2].

The growth aspirations among foreign affiliates in the volume manufacture of clothing in Kenya are broadly formed by two factors. First, the provisions in the AGOA have created opportunities for the Kenyan clothing industry in two rather separate industry segments. A second factor noted earlier is the potentially constraining role of parent companies and customers which have been passive with regard to enabling qualitative forms of growth in the Kenyan clothing industry. This is an issue we report at greater length in Phelps et al. (forthcoming).

6. Constraints on the growth of foreign-owned establishments

Companies were asked to indicate the three major constraints as they saw them affecting their intended plans. To aid analysis, the responses are categorized into broad issues and summarized in table 3.[8]

[8] Eighteen companies responded to this question, with over half the companies providing more than four responses on the challenges they felt they faced. The responses were not ranked in any order of importance by the companies but they all featured as the most significant challenges their firms were confronted within the medium term.

Table 3. Constraints on business growth

Constraint	Respondents	Percentage
High costs of production	12	67
AGOA uncertainty	11	61
Bureaucracy & inefficiencies	8	44
Industrial unrest	8	44
Poor Infrastructure	7	39
Lack of government support	6	33
Lack of credit /access to finance	6	33
Labour productivity and skills	6	33
Negative media publicity	5	28
Access to global markets /orders	4	22
Lack of local inputs	2	11

Source: Authors' survey in 2004.

6.1 High production costs

Concern over high production costs is widespread across the whole of the manufacturing sector in Kenya and not just within the clothing industry. Numerous representations to the government by industry bodies confirm that the issue of high production costs remains a chronic challenge for the industry, which the government recognizes as affecting national competitiveness (KEPSA, undated). In our survey, 67% of the firms identified production costs as their main challenge, specifically the cost of electricity, water and labour costs.

Electricity

Industrial energy needs in Kenya are met mainly through electricity and industrial oil. Kenya's electricity problems stem from the fact that nearly 60% of total electricity output comes from hydroelectricity; a supply highly vulnerable to weather conditions. The bulk of hydro-electricity is generated through five hydroelectric plants along the Tana River basin at the Kindaruma, Gitaru, Masinga, Kiambere and Kamburu dams, which produce over 400 MW. Another source, geothermal power, is tapped from the Rift Valley, with three plants located at Ol-Karia. In addition to the relatively high costs, electricity supply is often unreliable, resulting in a loss of production and damages to equipment (KEPSA, undated). One recent report estimated that disruptions to power supplies cost Kenyan-based enterprises the equivalent of 10% of their annual sales (World Bank, 2004, p. 63).

Within the clothing industry, the high costs of electricity places companies at a distinct global disadvantage. According to industry groups, electricity contributes as much as 67% of the cost of an export-oriented finished garment (KEPSA, undated, p. 5).

Kenya's costs of electricity for industry compare poorly with its neighbours, let alone some of its competitor countries in the clothing industry (UNCTAD, 2006). A kilowatt-hour (KW/h) in Kenya costs \$0.10–0.15, compared to \$0.04 in South Africa and \$0.08–0.10 in China. The costs are lower still in other countries: \$0.025 in Egypt, \$0.007 in Malaysia, \$0.02 in Zambia and \$0.023 in Malawi (EPZA Kenya, 2004, KEPSA, undated).

Transport costs

High transportation costs were also noted by the companies surveyed. The transport costs of inputs and finished products comprise a significant part of total production costs, especially for firms located in Nairobi, Athi River and Ruaraka. Their finished products are destined for export through the port of Mombasa located over 400 kilometres away. The majority of inputs are imported. Transportation is mainly along the Nairobi-Mombasa highway, which is in a poor state and there are major delays due to congestion at weighbridges and security problems along certain sections of the road.

The transport infrastructure within the country has been dilapidated through years of neglect (World Bank, 2004; Ikiara and Ndirangu, 2003). The poor state of road and rail infrastructure has been a common concern for industries. In general, the industry perception of transportation infrastructure compares poorly with those in neighbouring East African countries and major competitors in the clothing industry, such as China (World Bank, 2004, p. 60)

Just as importantly, the air and sea port administration and infrastructure are also in a very poor state. No direct flights from Nairobi to the United States are permitted since Jomo Kenyatta airport has not been certified by the United States Federal Air Administration (Office of United States Trade Representative, 2005). As a result, shipment by air has to be routed via third countries. The main sea port in Mombasa has been plagued by congestion and delays in customs administration. The outdated equipment also means that there is a limited capacity to handle cargo for neighbouring inland countries.

Labour costs

Interviews with firms in the clothing industry confirm that labour costs make up significant components of production costs. The industry lobby group, Kenya Apparel Manufacturers and Exporters Association (KAMEA), part of Kenya Association of Manufacturers (KAM), has identified labour costs as the single most important cost factor in the industry, although it is still the case that the main attraction of Kenya for overseas investors has been comparatively cheap labour [Interview INST 10].

In interviews with firm representatives, concern was raised over the rising labour costs relative to other locations [Interviews FDI 12, FDI 16 and FDI 19]; the firms felt they were paying too much for the workers involved in garment assembly compared to labour costs in their home economies in Asia. These costs are further increased through ad hoc annual decisions on minimum wage levels made by the Government for the entire economy in traditional announcements by the Ministry of Labour during annual national Labour Day celebrations. These, of course, are not productivity-related and have been criticised by the Federation of Kenyan Employers (Omolo and Omitti, 2004). The firms' views on labour costs is strongly contested by local and international NGOs which have led high-profile campaigns against the EPZ sector for poor wages, in addition to poor working conditions, inadequate labour rights and harassment of workers. The labour and human rights activists accuse the EPZ firms of exploitation and sweatshop conditions. These conflicts have led to industrial unrest and mutual suspicion in the sector.

A recent survey of FDI in SSA countries indicated that the garment industry's wages were the lowest among the region's industries (UNIDO, 2006, p. 72). Furthermore, Kenyan labour costs, with the exception of Indonesia, are the lowest of any apparel exporter to the United States (ECATRADE, 2005). Low labour costs have been a key factor in attracting investment to the industry; however, this significant competitive advantage is offset by comparatively low efficiency and productivity levels, as indicated in a recent report on the impacts of the AGOA (Office of United States Trade Representative, 2005, p. 52) with labour productivity having remained stagnant despite wage increases in recent years (World Bank, 2004, p. iv). In Kenya, the clothing industry lacks qualified staff in more technical and skilled positions, such as managers, machine operators, designers and engineers (ECATRADE, 2005, Ikiara and Ndirangu 2003, p. 57) with the poor provision for production and technical training to meet industry requirements being a concern (World Bank, 2004, p. iv).

Other costs

The provision of water has not been uniform for industry and is a problem for clothing companies located in Mombasa and Athi River. Various problems identified by the Kenyan private sector include lack of water billing, corruption at water treatment and rates payment, illegal water connections, poor management and destruction or abandonment of generation equipment. Thirty-four per cent of local manufacturers have dug their own boreholes to address the problem, compared to 16% in China and 13% in Uganda (KEPSA, undated).

In interviews, companies identified the cost of water provision as another high cost factor. Firms located in Athi River, for example, experience this problem fairly regularly, as the responsibility for water provision lies with the Mavoko County Council, rather than the EPZA. One firm, Upan Wasana EPZ, had constructed its own boreholes and was located on its own site away from the EPZ zones [Interview FDI 11].

6.2 Uncertainty over the renegotiation of the AGOA

The general uncertainty facing investors in Kenya has had a bearing on industry development in the country. As a recent World Bank investment climate survey reported "uncertainty in the policy regime has … resulted in outdated plant and equipment, low investment levels, and poor training" (World Bank, 2004, p. 71). A recent UNIDO survey of overseas investor perceptions placed Kenya among a group of countries in which both the value of anticipated investment as well as the share of past investment were among the lowest of SSA nations (UNIDO, 2006, p. 84).

Beyond this, the survey results revealed the more specific but pervasive influence that the AGOA had on the revival and future development of the clothing industry in Kenya. Kenya qualified for AGOA access in January 2001 and experienced a dramatic increase FDI and associated exports in the clothing industry [Interview INST 4].

Under the AGOA Apparel Provision, qualifying countries can export to the United States eligible apparel items made in the SSA countries, produced either from United States yarns and fabrics or from regional yarns and fabrics. But in addition, under the Special Rule, yarns and fabrics may be sourced from a designated least developed country, subject to quantitative limits. This third-country sourcing is of particular significance to FDI in the Kenyan clothing industry, as third country fabrics are the main input used. The Special Rule was scheduled to run out in September 2004, but has since been extended.[9]

At the time this field work was carried out, in 2004, negotiations over the extension of the special rule on fabric sourcing were still ongoing, and the outcome was very uncertain. This uncertainty over the policy situation appeared to be stalling any further investment in the industry as stakeholders adopted a "wait and see" position. It was widely agreed that Kenya did not have the capacity to produce enough domestic fabrics to meet the needs of the industry, without further investment or incentives for cotton growing and textile mills [Interviews INST 4 and INST 12]. Sixty-one per cent of the respondents identified the uncertainty over the AGOA's third country fabrics provision as a major concern to them and a constraint on expansion. Firms interviewed signalled their intention to cease production or relocate their operations to different countries if the provision was not extended [Interviews FDI 12, FDI 4 and FDI 2]. A widely held view was that the lack of timely action by the Government in resolving this situation meant any measures taken would be "too little, too late" [Interviews INST 1, INST 4 and FDI 12].

The investors' concern over the AGOA's extension was echoed by government representatives, who explicitly acknowledged that not enough had been done to prepare the industry for the AGOA requirement on domestic inputs. According to the representative at the AGOA desk, "we, the Government, were too relaxed and we have realized too late the need to substitute for third country imports of materials" [Interview INST 4]. It is interesting that while 61% of firm representatives ranked the AGOA and third country fabric sourcing as very significant to their future operations, only two firms specifically highlighted the issue of local inputs as of particular concern. The inconsistency in these results has possible pointers for the poor prospects of upstream linkages with textile mills and cotton ginneries, possibly signalling the short to medium term horizons of footloose capital. This issue of the AGOA overlapped with the concern regarding the end of the MFA in January 2005. China's expected dominance of the global textile industry in

[9] Duty-free access to the United States market for clothing produced in lesser developed SSA countries (which includes Kenya) and made from third country yarns was extended until 2012 and limited to 3.5% of all AGOA apparel imports (Office of the United States Trade Representative, 2007) .

quota-free environment raised serious concerns over the future of SSA exports and the viability of the industry in Kenya.

6.3 Bureaucratic inefficiency and corruption

In Kenya, the term "bureaucracy" has become synonymous with red tape, inefficiency and officious obstruction within public service organizations. Various aspects of bureaucratic inefficiency have been identified in recent surveys as major problems facing the private sector in Kenya (EABC, 2005; World Bank, 2004). These general findings are confirmed in our survey with 44% of company representatives in the survey cited bureaucracy as a significant challenge facing their operations – excessive "red tape" and the widespread incidence of corruption being the main aspects mentioned by the respondents. Additionally, 33% considered the lack of government support as a constraint on their business growth.

The perceived severity of corruption varies depending on the ethnicity and nationality of the businesses involved. In this respect, one recent survey suggests that Asian businesses were seemingly subject to some of the highest costs associated with rent seeking behaviour in Kenya (World Bank, 2004, p. 57). Given the high participation of Asian businesses in the Kenyan clothing industry, it is hardly surprising that our interviews suggested that bureaucratic costs were evident in several areas, such as excessive delays at the port in clearing imports and exports, the amount of red tape involved in obtaining licences and clearances from various authorities, long delays in issuing work permits, and demands for monetary inducements in order to speed up these processes [Interviews FDI 1 and FDI 6]. Additional points identified were inefficient procedures including paper-based port clearance processes and an obstructive attitude from various government officials in dealings with day-to-day issues, such as the problems of water, telephones and security [Interview 12].

For clothing companies, the area where bureaucracy-related problems were experienced most frequently was customs clearance [Interviews FDI 7 and FDI 17]. Frequent delays were experienced at the ports; these mainly resulted from a requirement by the Kenya Revenue Authority for textiles and inputs to undergo 100% verification at the ports. Prior to January 2004, goods destined for EPZ companies were released directly and verifications completed within the EPZ zones. Checks have been re-introduced with resultant delays; a shipment takes up to two weeks to be cleared at the port, with an added cost of $75 and $150 for a 20-foot and 40-foot container's verification respectively (EPZA, 2004, p. 2). The extra costs as well as added delays placed the firms at a disadvantage in view of the geographical distance from key markets.

In Kenya, the issue of bureaucracy is closely interlinked with that of corruption. Kenya's performance in this area has deteriorated steadily; the country continues to rank high among the most corrupt places to do business in the Transparency International Survey.[10]

Recently, efforts have been made by the government to reduce some of the excessive bureaucracy. According to one recent investment climate assessment, the range of business licenses required has reduced from a high of 1,347 licenses to 195 (World Bank, 2006). Additionally, the Kenya Revenue Authority introduced an electronic clearing system – Simba – at the Mombasa port to reduce delays and reduce corruption. It is too early to judge the effect of these changes.

6.4 Industrial unrest and negative media coverage

Kenya's apparel industry has been characterized by intense industrial unrest; the EPZ factories regularly experience labour disputes. In 2003 and 2004, the firms underwent a series of acrimonious and unplanned strikes, mainly over low wages and disputed working conditions. The unrest was sometimes accompanied by violence, destruction of property at the factories and riots which required the police and anti-riot personnel to move into the EPZ zone factories to control the situation.

These disputes were widely covered in the national and local press and served to focus attention on specific firms. Local and international human rights activists have led high profile campaigns against poor practices in the industry, such as low pay, forced overtime, harassment and sexual exploitation, denial of union representation (KHRC, 2004). Various campaigns were directed at the end customer companies, such as Walmart and Sears in the United States, for complicity in human and labour rights abuse at their subcontractor factories (for example, the

[10] Government departments clothing industry firms need to deal with include Immigration (for work permits), Customs, which is under the Kenya Revenue Authority (for taxes, duties and clearances), the Kenya Police, and various state corporations such as the investment promotion authorities, and the local authorities (for various licenses, water provision).

clean-clothes campaign, sweatshop alert). The campaigners demanded that the retailers who hold significant power over these firms put pressure on them to improve working conditions and withhold the placing of orders until improvements are made.

6.5 Labour skills and productivity

The overall view expressed by the management of several firms was that Kenyan workers were not as productive as those in China, which dominates the global clothing industry. This view is echoed in an earlier study which claimed that the average Kenyan worker required five years of extra training before attaining the productivity level in China (Ikiara and Ndirangu, 2003, p. 57). Workers' productivity also lags behind that of workers in several other Asian home countries of parent TNCs with FDI in the Kenyan clothing industry. To reinforce this point, one respondent from a clothing company noted that in Bombay, one person can make two shirts but in Kenya it requires two people to make two shirts [Interview FDI 12]. Another respondent suggested that while Kenyan workers were second only to those in Mauritius in the East African regional context, they were only two-thirds as efficient as those in Bangladesh, India, Pakistan and Sri Lanka [Interview FDI 4].

It is in respect of labour skills and productivity that differences in industry cultures between the home countries of TNCs and Kenya are most pronounced. Arguably, the unmet expectations of TNCs in this respect have further contributed to the potentially transient nature of FDI in the clothing industry.

6.6 Other constraints

The other constraints mentioned by respondents to the survey were few but focused upon financial matters. The ability of firms to raise credit locally, especially for working capital, was constrained by various factors. The most often cited concern was the local interest rates being significantly higher than those available in international markets; local rates range from 17 to 22%, compared to international rates of 5 to 10% [Interviews FDI 1, FDI 3 and FDI 11]. One interviewee noted how "... these rates are too high. Outside, we can get it at 5–6% but here, the rate is 21%. I would not want to borrow any money here ..." [Interview FDI 3].

In general, the bulk of the initial set-up costs and financing requirements were arranged through their parent companies or own funds, while supplementary financing, mainly for working capital and local costs, were arranged through local loans. However, some companies reported raising a significant portion of all their financing locally through Kenyan banks. Upan Wasana EPZ raised 100% of its loans locally, Sahara Stitch EPZ between 40–60%, MRC EPZ 60% and United Aryan EPZ raised 10% [Interviews FDI 11, FDI 4, FDI 5 and FDI 16].

High interest rates had a direct impact on the capacity of the firms and the type of orders they could accept; the higher the interest rates, the fewer the number of FOB orders a firm could accept, which meant lower returns and reduced capacity for expansion [Interview FDI 14]. Firms therefore had to accept higher amounts of C&M orders, which had narrower margins, but also entailed less financial risk to the firm. For smaller export processing firms, the issue of access to local finance was a key challenge as it significantly constrained their ability to progress from the sub-contracting stage to direct order processing [Interview FDI 15].

In sum, there are a host of factors that contribute to the high costs facing foreign affiliates in the Kenyan clothing industry. By the same token, it is apparent that there is considerable scope for reducing these costs. Thus, were production costs to come down significantly, the industry would have a good chance of surviving in the competitive post-MFA era; the industry is thought to be able to hold on to its global market share if production costs were reduced by between 20% and 30% to make up for the loss of its quota advantages (World Bank, 2006)

7. The absence of local backward integration

7.1 Backward linkages to local cotton textiles suppliers

The clothing establishments surveyed were asked to estimate the percentage of their total expenditure on textile materials and business services from Kenyan suppliers. Many of the responses actually distinguished between textile materials and other materials, as reported in table 4. The table reports the number of firms, grouped according to the level of local sourcing.

A number of empirical studies have reported the tendency for foreign affiliates in both developed and developing country settings to be associated with generally low levels of local sourcing of materials and services (Helleiner, 1973; Phelps, 1993). In the few previous studies of FDI in Kenya, similar tendencies for companies to import materials were apparent (Langdon, 1981, p. 34). As such, the figures in table 4 are to be expected. They reflect important constraints on local sourcing by overseas investors and the generally low levels of local sourcing found across foreign affiliates in SSA (UNIDO, 2003, p. 63).

Table 4. Percentage of materials and business services purchased from Kenyan suppliers

	0%	1-5%	6-25%	26-50%	51-100%	Average
Textiles	18 (90%)	1 (5%)	1 (5%)	0 (0%)	0 (0%)	0.6%
Other Materials	2 (10%)	11 (55%)	2 (10%)	1 (5%)	4 (20%)	25.05%
Business services	8 (40%)	3 (15%)	3 (15%)	2 (10%)	4 (20%)	25.25%

Source: Authors' survey in 2004.

The first observation that can be made from table 4 is that negligible amounts of textile materials were sourced locally. Only two companies purchased textile materials from Kenyan suppliers, with one company indicating this was mainly for materials for pockets sown into the garments. This underlines some of the paradoxical effects of the AGOA. The AGOA is designed to stimulate investment and industrial upgrading among SSA countries. However, exemptions granted to allow certain countries to source fabrics and materials from third countries has stimulated the growth of a largely foreign-owned clothing industry which is not linked to the local economy.

This is all the more frustrating in the case of Kenya because, as interviewees highlighted, some local suppliers exist as a result of the earlier growth of the cotton and clothing industries under the import substitution strategy [Interviews INST 3 and INST 12]. In 2005, there were 24 registered cotton ginneries in Kenya but only ten of these were operational, producing at about 14% of installed capacity (EPZA, 2005b, p. 5).

Investment gaps in the chain

It was evident from the interviews that policy-makers recognized the desirability of developing the clothing commodity chain further upstream to revive the moribund cotton ginning and textile industry. An interviewee at the EPZA, for example, commented how he wanted "to have the full value chain as it would bring multiplier effects". In this regard, he notes that his organization, "the EPZA has gone out to try and attract spinning and weaving companies" [Interview INST 9]. However, progress in developing the chain backwards from garment manufacture into textile manufacture and cotton growing has been slow and uncoordinated as confirmed by another interviewee who commented that "local linkages need to be developed, and it is only coming up very slowly" [Interview INST 17].

However, obstacles exist to the revival of textile manufacturing in Kenya. While there is some cotton cultivation and ginning surviving from the previous period of growth of Kenya's clothing industry, there is a major problem in attracting both indigenous and foreign investment, specially in textile manufacturing. Referring specifically to the risks associated with the financing of projects involved with textile manufacture in East Africa, an interviewee from the PTA investment bank based in Nairobi observed that "you find, as you go further down the chain, going into the textile industry is a little tricky" [Interview INST 7]. From this representative's point of view, the attraction and support of investment into spinning and weaving has been problematic. The same interviewee went on to observe that, from experience, investing in this industry was risky, noting specifically that "the PTA bank itself has had problems in other countries with spinning and weaving companies that went into receivership. We're not sure about the prospects for investment in this" [Interview INST 7].

Institutional/government failures

The apparent lack of local backward linkages can also be attributed to institutional and government failures in the regulation of the industry. The clothing industry in Kenya lost its coordinating structures along with the collapse of the industry in the 1980s (Ikiara and Ndirangu, 2003, p. 3). Among the sources of institutional failures are those "manifested by lack of strong producer associations; weak or inefficient mechanisms for overseeing issues such as production and distribution of quality seed, provision of input to producers on credit, and the quality of inputs such as pesticides; and the virtual collapse of extension services" (Ikiara and Ndirangu, 2003, p. 3).

There is a recognition of the desirability of coordinating garment production with backward segments of the chain, especially cotton growing and ginning, within the government circles. As a representative of the Ministry of Trade and Industry noted on the relationship between government bodies and other stakeholders, "for the whole chain to work, we must work together" [Interview INST 4]. Another interviewee noted how “in order to attract investment, we need to restructure the cotton industry. The structure of incentives is wrong at the moment” [Interview INST 1].

Some of these failures stem from the lack of an effective apex institution to coordinate the cotton and clothing industries in Kenya (Ikiara and Ndirangu, 2003) [Interview INST 12]. The Cotton Board of Kenya, which enjoyed some success, such as the introduction of the post-independence import substitution strategy, and could still assume such a role, has been ineffective since the industry’s decline prior to the AGOA. It is due to be replaced under new legislation which has progressed only very slowly through the Kenyan parliament due to the vested interests within the Cotton Board itself [Interview INST 4].

Parent companies and customers and local sourcing

The government’s failings to assist with the development of the industry are also exacerbated by the attitudes of manufacturing enterprises themselves. The same interviewee went on to observe that the clothing companies were not searching for local suppliers of raw materials, possibly in light of the marginal and transient nature of the businesses concerned and the lack of long-term commitment to manufacturing in the country [Interview INST 4].

The specific nature of both the parent companies and customers involved have shaped the characteristics of foreign affiliates in the Kenyan clothing industry. By the same token, the influence of customers and parent companies can shape the wider economic impacts in the form of local purchases of materials and services. Interviewed companies identified a range of constraints on their local sourcing, with several respondents recognizing that the lack of adequate supply, stemming from the collapse of the local cotton and clothing industry was a factor. The cheaper cost and wider variety of imported inputs available helped them address this challenge. In addition, the process of acquiring local raw materials was no easier than importing materials, as it involved the same bureaucratic process [Interview FDI 19].

The economic liberalization affecting the clothing industry and the AGOA itself may have come at a wrong time for the cotton industry (Ikiara and Ndirangu, 2003, p. 13). With the collapse of the local ginneries and textile mills, the industry lost its capacity and key position in relation to the clothing industry that has re-emerged so that shortfalls in raw materials are routinely made up through imports.

The potential for cooperation at the East African regional scale

With the collapse of domestic cotton cultivation and the textile industry, there has been recognition of the possibility for wider cross-border links to support the clothing industry. Cotton is already imported into Kenya from Uganda and Tanzania. According to one interviewee, "some of the other sources within SSA are expensive, for example, South Africa and Mauritius are expensive. West Africa, however, has a lot of cotton" [Interview INST 4].

With regard to the efforts to revive regional integration and the collapsed East African Cooperation, views were expressed on the desirability of regional supply linkages between Kenya, Tanzania and Uganda. Several interviewees noted the possibility for the clothing industry to work across East Africa on the basis of comparative advantage [Interviews INST 7 and INST 8]. The relatively well-developed Kenyan cotton ginning capacity could be supplied with raw material sourced from Uganda which has a thriving cotton-growing industry. This is echoed by another interviewee who noted that "we are looking at sharing or building more capacity jointly with Uganda, to let them do the cotton side, and then supply to manufacturers in Kenya" [Interview INST 1]. However, concern was also expressed regarding the ability to coordinate such arrangements at the regional level. This is due to the perceived lack of capacity of the governments and industry institutions to deal with the complications inherent in regional negotiations. At least one interviewee with some overview of the matter in East Africa was not optimistic over the prospects of such regional coordination [Interview INST 7].

7.2 The sourcing of other material inputs

A second observation to be made on table 4 is that significant proportions of other material inputs were purchased locally from Kenyan suppliers. Indeed, only two companies surveyed indicated they did not purchase any of these materials locally, while four companies purchased all or virtually all of these materials from Kenyan companies. Overall, one quarter of the expenditures on these other material inputs came from Kenyan suppliers.

While machinery and spare parts are almost exclusively imported, several foreign owned companies have begun to source chemicals, dyes and accessories from local Kenyan suppliers. Nineteen of the twenty-three companies surveyed (83%) purchased some or all of their packaging materials (boxes, poly-bags) locally, while 52% (12 of 23) purchased threads from Kenyan suppliers. Additionally, some companies also purchased zippers, elastic, washing chemicals and dyes locally. These trimmings and embellishments such as laces, thread interlinings, buttons and zip fasteners are not, however, widely available locally to the standard and quality that meet conditions set by buyers.

The sorts of constraints on local sourcing of inputs identified by the companies surveyed reflect the sorts of cost and quality pressures that are felt routinely in most industries. The influence of customer or parent company policies in dictating the sources of purchased inputs is also something that should not be surprising. It has long been understood that parent company strategies place important constraints on the purchasing autonomy of their branch factories. This is well illustrated in the case of Protex EPZ Kenya.

Protex EPZ is located within the Athi River EPZ and is an affiliate of Protex Taiwan, headquartered in Taipei. As of 2004, it imported 100% of all its textile fabric requirement. The sourcing for this imported fabric was arranged via the broker providing the orders for production. This arrangement limited the ability of the Kenyan operations to source fabrics locally, as it required prior approval from the broker. If any orders failed due to the poor quality of materials or deviation from specifications, the retailer may reject the order at significant costs to both the broker and the firm. Protex EPZ Kenya confirmed that it did purchase some inputs locally, which included dyes and packaging. Additionally, the company also contracted out some of its embroidery requirements to local firms. The company noted that there were various obstacles to their increasing local sourcing. In the case of packaging, there are only four package manufacturing firms. Additionally, production costs in Kenya were high, making their imported equivalents cheaper. The quality of local inputs was also viewed as sub-standard and inconsistent, compared to the more established and efficient producers in Asia, from where Protex EPZ sourced through its parent company in Taiwan Province of China [Interview FDI 2].

7.3 Sourcing of business services

Even if the proportions of material inputs being sourced from Kenyan suppliers are low, we might expect greater use of Kenyan suppliers of business service inputs, not least because of Nairobi's role as the investment hub within the East Africa region. Fifty-seven per cent of companies surveyed purchased some business services locally. Also, as table 4 shows, these companies spent, on average, a quarter of their total expenditures on business services with Kenyan suppliers. Financial and business services purchased included the provision of management consulting, auditing and accounting, raising finance, legal as well as banking services. Local auditing and management consulting services were provided by local consultants, including the local offices of internationally recognized firms, such as Deloitte and Touche [Interview FDI 14].

The more well-established companies reported that in order to compete and qualify for larger, higher-margin orders from well-known retailers, they had to meet certain criteria, which included providing audited accounts by recognized firms for five years, in addition to the usual capacity criteria. These services were sometimes provided through their parent companies, but in Nairobi, the need was met by local accountants and consultants [Interview FDI 5].

The surveyed firms reported purchasing various technical business services from local suppliers. These included services such as engineering and technical consulting on issues such as structural layout, process engineering and various internal control systems for efficiency. In addition, some companies sourced part of their computing and IT support requirements locally. However, others sourced their computing systems mainly from their home countries, such as India and Taiwan Province of China, where these services were competitive in terms of cost and technology.

7.4 Other linkages to local institutions

All the surveyed companies, with the exception of one, had developed links with other local and national organizations within the country – confirming findings of more developed relationships between foreign affiliates and local organizations in Kenya compared to other SSA countries (UNIDO, 2003, p. 64). In addition, all but one of the companies surveyed were members of the industry body, KAM, which lobbied on issues affecting industry interests.

It was clear from interviews that despite the efforts of these associations, the companies felt that policymakers were not attuned to their concerns and provided little support to investors once they established their affiliates in the country. While industry representations through KAMEA were seen as necessary, they were thought to be weak as a means of effecting the real changes required to strengthen the clothing industry's future prospects in light of the uncertainty over the AGOA and changes in global trading rules after the MFA's demise. This lack of effective public-private sector dialogue on the industry's strategic direction forced companies to play a waiting game, relying on external players, such as international organizations to rescue the industry (McCormick et al., 2006) [Interviews FDI 12 and INST 1] as the case of Kapric Apparels below illustrates.

Kapric is one of the largest TNCs involved in the clothing industry in Kenya. Kapric's view of its relationship with other public and private institutions is typical of the industry's "wait and see" stance. The company is a member of KAM and its industry arm, KAMEA. Through these forums, Kapric has consistently expressed its concerns over the high cost of doing business in Kenya, including issues over labour costs, inadequacies of infrastructure and the high cost of utility services. It has also been vocal on the lack of support for the industry from the government. The interviewee from Kapric was pessimistic about the ability of the Kenyan clothing industry to respond to the imminent threat of competition from Chinese garment manufacturers and compared the Government of China's concerted approach to supporting the expansion of its clothing industry with that of the Government of Kenya. Kapric's "wait and see" stance – resulting in a halt to further expansion of capacity – is a product of the lack of government support and the uncertainty over the AGOA's future prospects. The interviewee at the company noted, "we are lobbying but the government is very slow. We do not wish to keep banging our heads on the wall, if they do not have the sense to listen. They don't even know what this industry is about" [Interview FDI 12].

The incidence of links between the clothing manufacturers and other local organizations was less widespread. Five of the more established enterprises reported the arrangement to collaborate with government technical institutes, such as the Mombasa Institute of Technology and the National Youth Service. One firm, Ashton Apparels, provided industrial apprenticeships in collaboration with the Directorate of Industrial Training, and it also ran its own training centre for skills development. None of the companies surveyed had any research collaborations with universities in Kenya.

The survey also revealed the lack of collaboration with NGOs. Only two enterprises reported having held joint training sessions with an NGO on HIV/AIDS awareness, and even this was organized through the EPZA. This disengagement is perhaps understandable in light of the strained relationship between the industry and NGOs, following the highly vocal role that various NGOs have played against working conditions in the EPZs, and specially in the clothing industry.

8. Conclusions

The re-birth of the clothing industry in Kenya following the enactment of the AGOA has been fuelled almost entirely by FDI. The direct employment created has been substantial although it has declined since the high water mark in 2003. Our survey conducted in 2004 revealed a variety of aspirations for growth among foreign affiliates in the Kenyan clothing industry. However, at the time of the survey reported here, a degree of uncertainty hung over the industry due to the renegotiation of third country sourcing provisions in the AGOA.

The failure of the clothing industry to develop backward linkages and stimulate the growth of competitive local cotton and textile industries has left the industry vulnerable to the terms on which the AGOA grants access to the United States market. This uncertainty has been compounded in the case of Kenya by a general failure of the government to create a competitive environment for the clothing industry. Whilst Kenya may enjoy a measure of macroeconomic and political stability, this masks a range of general bureaucratic inefficiencies, poor infrastructure and limited human resources that impact on the competitiveness of the industry. More worryingly, industry-specific policy to coordinate the development of the industry – especially the development of local backward linkages – has been very slow to develop. Remedying such institutional failures remains a challenge to the successful incorporation of SSA economies into GCCs (Gibbon and Ponte, 2005).

To this end, government action is necessary, given the reluctance of the clothing industry itself to generate such backward linkages. It appears that neither the retail customers in the United States nor the TNCs investing in the Kenyan clothing industry have generated meaningful local indirect employment or spillovers (see also Phelps et al., forthcoming). The findings tend to underline a set of important questions regarding the precise nature of impacts of developing country outward FDI on other developing host nations. Developing country outward FDI does appear to differ from that of outward FDI upon host economies (UNCTAD, 2007). Notably, such outward FDI appears to be less a bearer of technology than of production process efficiencies (UNCTAD, 2007, p. 152). In particular, the impact of TNCs from emergent "first tier" coordinating nations (e.g. Hong Kong (China), Singapore, Taiwan Province of China) and “second tier” source nations (e.g. Bangladesh, China, India and Sri Lanka) within the international division of labour upon “third tier” locations such as SSA nations is a topic ripe for further study.

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APPENDIX

LIST OF INTERVIEW SOURCES

INST 1	Manager, After Care Services, Investment Promotion Centre, 21 May, 2004
INST 2	Senior Promotion Officer, Investment Promotion Centre, Nairobi, 17 May, 2004
INST 3	Senior Manager, Investment Promotion Department, Investment Promotion Centre, Nairobi, 21 May 2004
INST 4	Industrial Development Officer, AGOA Desk, Ministry of Industry, Nairobi, 19 May 2004
INST 5	Dep. Secretary General and Finance/Accountant Kenya Textile and Tailors Union, Nairobi 14 June 2004
INST 7	Portfolio Investment Manager, PTA Bank, Nairobi,
INST 8	Assistant Resident Country Manager, East African Development Bank, Nairobi 25 May 2004
INST 9	Manager, Policy Research and Planning and Procurement Officer, Export Processing Zone Authority, Nairobi, 18 May 2004.
INST 10	Executive Officer, Sector Development Division, Kenya Association of Manufacturers, Nairobi, 21 May 2004
INST 12	Senior Analyst & Programme Coordinator, KIPPRA, Nairobi, 19 May 2004.
INST 17	Research and Information Manager, Investment Promotion Centre, Nairobi, 17 May 2004.
INST 22	Investment Policy Analyst, UNCTAD, Geneva, 28 January 2004
FDI 1	Director, Storm Apparels Manufacturing Ltd., 21 June 2004
FDI 2	General Manager, Protex EPZ Ltd., 17 June 2004

FDI 3	General Manager, BlueBird EPZ Ltd., 19 July 2004
FDI 4	Finance Manager, Sahara Stitch EPZ Ltd., 15 July 2004
FDI 5	Finance Manager, United Aryan EPZ Ltd., 15 July 2004
FDI 6	Directors, Ancheneyar EPZ Kenya Ltd., 14 July 2004
FDI 7	Production Manager, Asia Resources EPZ Ltd., 15 July 2004
FDI 8	Manager, Apex Apparels EPZ Ltd., 15 July 2004
FDI 10	Accountant, Rising Sun EPZ Ltd., 17 June 2004
FDI 11	Finance Manager, Upan Wasana EPZ Ltd., 14 July 2004
FDI 12	Director, KAPRIC and Birch EPZ Ltd., 20 July 2004
FDI 13	Accountant, Chandhu EPZ Ltd., 19 July 2004
FDI 14	General Manager, Ashton Apparels EPZ Ltd., 20 July 2004
FDI 15	Production Manager, Shin Ace Garments, 23 July 2004
FDI 16	MRC (Nairobi) EPZ Ltd., Human resources Manager, 17 June 2004
FDI 17	Directors, Falcon Apparels Ltd., 21 June 2004
FDI 18	Administrator, Senior Best Garments EPZ Ltd., 23 July 2004
FDI 19	Forwarding Manager, Rolex Garments EPZ, Ltd., 17 June 2004
FDI 20	Financial Controller, Mirage Fashionwear EPZ Ltd., 15 June 2004
FDI 21	Manager, Kenya Knit garments EPZ Ltd., 21 July 2004