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COMPETITION POLICY AND THE INFORMAL ECONOMY

Contribution from Kenya

-- Session II --

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COMPETITION POLICY AND THE INFORMAL ECONOMY IN KENYA¹

--Kenya--

1. Introduction

1. A 1972 landmark ILO study in Kenya confirmed the existence of this parallel economy dominated by small and micro businesses that absorb a large number of persons that would otherwise be recorded as unemployed by Economic Surveys. This sector that has been referred to as the informal sector to distinguish it from the modern sector is described as consisting of "... all small-scale activities that are normally semi-organised and unregulated, and use simple labour-intensive technology... undertaken by artisans, traders and operators in work-sites such as open yards, market stalls, undeveloped plots, residential houses and street pavements. They are not registered with the Registrar of Companies and may or may not have licenses from local authorities for carrying out a variety of businesses." The informal sector has been efficient at utilizing waste materials such as old tires, scrap metal, etc. to produce goods and provide services that otherwise would have been imported or would be too expensive for low income sectors.

2. These small businesses are often started by individuals with little capital and with virtually no support from the government or Non Governmental Organisations. A government report attributes the notable growth of the informal sector to "... ease of entry into and exit from the sector and little capital investment... absence of registration and other legal formalities, and gradual shift of labour from subsistence farming to informal sector as the economy increasingly becomes market oriented". Unemployment and underemployment is another particularly strong reason to go into self-employment in the informal sector.

3. While the government and the NGOs have been satisfied at the ability of the informal sector to absorb excess labour force in the country, there has been concern regarding how most of these enterprises stagnate at the bottom and do not show signs of growing into medium and large scale enterprises. Some of the difficulties that small and informal businesses face are associated with the country's legal structure; unavailability of capital to develop businesses, while others are related to the lack of appropriate business skills.

4. The concept of an informal economy, micro and small enterprises (MSEs) and Jua Kali² are often used interchangeably. The sector is a major source of employment and income as it accounts for 72% of total wage employment and 81% of private sector employment. Its' contribution is therefore greater than that of the medium and large manufacturing sector.

5. A majority of MSEs are micro-enterprises with fewer than 10 employees, while 70% of them are one person, own account workers. This infers that majority of MSE enterprises are operating at the bottom of the economy, with a significant percentage falling among the 53% of Kenyans living below the poverty line.

¹ The views expressed herein are those of Mr. Francis W. Kariuki, the Acting Commissioner/CEO of the Monopolies and Prices Commission of Kenya and Ms. Beldine Omolo, Head of Enforcement. They do not necessarily represent the position of the Commission.

² Jua Kali means hot sun. It depicts operations by informal businesses in the open, sometimes under the scorching sun.

2. The Dairy sector: A case study of milk vendors

6. The informal dairy sector of Kenya is one of the most dynamic sectors in the economy, creating more jobs than the formal dairy sector. In cognisance of the above, new research has been conducted with the aim of demystifying the myth that milk sold through informal channels pose public health risks. The Government has been urged to recognise the existence of the informal sector and license its players. About 55% of all milk marketed by some 600,000 small-scale farmers is actually sold directly by farmers to neighbouring consumers and institutions. Raw milk traders are estimated to handle about 1/3 of the total marketed milk, with only 8% sold directly to processors.

7. Because the informal milk sector is creating employment in the often-forgotten rural areas, as well as urban areas, the implication of this research is that the government should redesign the rules of the game to enable the sector to create even more jobs. The jobs are being created in the mobile milk trace (bicycle delivery – exclusively for young men mostly of age 20-35), in milk bars, shops/kiosks and small processors.

8. Issues of public health in the informal milk markets came to the fore after a study conducted by the Ministry of Agriculture and Livestock Development, Kenya Agriculture Research Institute (KARI) and the International Livestock Research Institute (ILRI) in 2000. The findings showed that up to 96% of households in Kenya boil milk prior to its consumption, which when likened to pasteurisation, ensures that all harmful bacteria are destroyed hence making the milk safe for consumption.

9. The report acknowledges that although there is some degree of adulteration of milk supplied through the informal channels, there was no obvious link between milk quality and the type of market agent, and there may not be serious harmful effects in the milk that eventually reaches the consumers. “Adulteration of milk through addition of water may introduce chemical and microbial health hazards as well as reduce the nutritional quality, palatability and market value of milk,” says the report. Overall, only 10 percent of all milk tested was found to be adulterated, most cases occurring in the dry season when there is milk shortage.

10. Another major health risk is the large number (up to 15%) of both pasteurised and raw milk samples that contain antibiotic residues. The negative implications of this are that over time, there is the possibility of patients developing of drug resistance, which then would call for more expensive antibiotics and place a strain on the national budget. This requires training particularly of dairy farmers and veterinary assistants as well as drug suppliers. Training of all milk traders in quality control, including use of proven hygienic handling methods, is the main pre-condition for licensing.

11. The formal and the informal dairy sector relies to a very large extent on marketed surplus from the smallholder dairy producers which in 1997 was estimated at 1,093 million litres, says the report. Of this amount only 12 percent passed through pasteurisation and “formal” marketing while the remainder – about 88 per cent – was sold raw through direct sales to consumers and hotels through co-operatives, self-help groups and small traders.

12. The small-scale market agents include milk bars, shop/kiosks and mobile/itinerant traders, sold, on average sell 50-120 litres a day. The agents pay farmers prices that are 7 to 65% higher than those paid by the processors and charge the consumers 20-50 % less per litre for raw milk compared to what consumers of packaged milk pay.

13. The consumer preference for raw milk is reflected in Nairobi as well as other urban centres. This trend is spurred by the inefficiencies associated with the formal milk processors. Even when the sector was under the monopoly of Kenya Co-operative Creameries, the organisation accounted for only 25 per cent of

the marketed milk. The formal dairy sector is less vibrant because of stringent regulations on quality control and packaging. There is also the large capital outlay needed to set up processing and cooling plants. The informal dairy sector also thrives on the fact that vendors make prompt payments for milk at the farm gate and they also sell at competitive prices.

3. Public Transport- the case of Matatu Transport Providers

14. Public transport in urban Kenya is dominated by Matatu vehicles. The term Matatu, which means “thirty cents” in local vernacular, was a standard charge for every trip made in the early 1960s. In 1973, the Government in response to lobbying from Matatu operators declared that Matatus were a legal mode of transport and could operate without obtaining Public Service Vehicles (PSV) licenses except to comply with existing insurance and traffic regulations. Initially, the Kenya Bus Service- which was jointly owned by the United Transport Overseas Ltd (75%) and the Nairobi City Council (25%) - existed since 1934 as the sole legal provider of public transport services in the five major towns. It was, however, not able to cope with the increase in demand for transport services and this encouraged the growth of the Matatus from 17,600 in 1990 to 40,000 in 2003. The vehicles comprise mini-buses with sitting capacities ranging from 14 to 40 passengers. They provide employment and generate revenue for the Government in the form of license charges, duty, VAT and other taxes. In addition, the industry plays a leading part in transportation of both persons and goods in rural and urban areas.

15. Unfortunately, the industry’s vast growth has been accompanied by increasing road traffic accidents which are caused by among other factors, reckless driving, unroad worthy vehicles, poor road conditions, laxity of law enforcement, vested interests, poor driving skills and poor working conditions. Road accidents are the third leading cause of death after malaria and HIV/AIDS and are at present a major public health problem in terms of morbidity, disability and associated health care costs.

16. The Matatu sector has 4 trade associations each furthering different interests of its members. The Matatu Vehicle Owners Association (MVOA) or MOA was formed in 1973 to allow owners the control of operations of the sector. The formation of the Matatu Welfare Association (MWA) in 2001 and the Matatu Stage Welfare Association serve the interests of drivers, conductors and other stage workers. Route-based Savings and Credit Cooperative Societies (Saccos) serve as welfare organisations that pool resources and redistribute them through credit schemes, organise route operations and address members’ welfare concerns. Most of these Saccos were affiliated to larger organisations like MWA and MOA. The route-based organisations are generally stronger than the national bodies like MWA and MOA in articulating the concerns of the industry.

17. At the competition level, the Monopolies Department has had few problems with the sector associated mainly with fare fixing and route allocations. Some of their activities e.g. extorting goodwill charges from unsuspecting matatu owners in order to be allocated a route to operate in, are predatory in nature. Most of the players including their Associations have no fixed abode and therefore Department finds it difficult to serve notices on them.

18. The informal matatu business has thrived on the fragmented nature of the institutional and organisational structure of the transport industry. The Kenya Roads Board (KRB) which is the main institution responsible for the national road infrastructure network in Kenya, the Transport Licensing Board (TLB), Motor Vehicle Inspection Unit, Registrar of Motor Vehicles, Driving Test Center, Traffic Police and Local Authorities are under different ministries hence the lack of harmony in policy implementation.

19. In 2002/3, the government undertook two measures to correct the situation. First, it developed the integrated national transport policy and secondly, it introduced reforms in the operation of public service

vehicles. These measures are for the purposes of reducing accidents, enhancing safety of commuters, ensuring responsibility, accountability and competence of drivers and conductors; eliminating illegal drivers, conductors and criminals that had infiltrated the industry; and facilitating the identification of vehicles and restricting their operation to authorised routes. The following provisions were provided:

- installing speed governors to control speed to 80 Kph for vehicles whose weight exceed 3,048 Kilos;
- fitting seat belts on all public, commercial and private vehicles;
- employing drivers and conductors on permanent basis;
- issuing badges and uniforms to PSV drivers and conductors;
- indicating route details and painting of yellow band on Matatus for easy identification;
- re-testing of drivers after every two years;
- prominent display of driver's photograph together with their identity card details;
- regular inspection of motor vehicle for tests and certification.

20. The provisions have not been effective because of:

- lack of proper enforcement by traffic police;
- discriminatory nature of rules which target only Matatus;
- high expenses of institute the safety measures;
- reduction of income for the operators owing to the fact that the seating capacity of the vehicles was reduced from 18 to 14 passengers;
- additional costs owing to inspection charges by the Vehicle Inspection Unit;
- the enhanced regulatory requirements increased the possibility of extortion for bribery by the principal enforcement agencies.

21. However some progress has been noted after the implementation of the reforms:

- most Matatus have been issued with compliance certificates;
- MOTC in collaboration with the National Road Safety Agency has been conducting the National Roads Safety Awareness campaign on radio, TV and newspapers as well as using billboards;
- reduction in accidents by about 73% in the first six months of implementation of the legal notice;
- restoration of sanity and order in the Matatu industry;
- defective vehicles have been eliminated;
- cartels have been eliminated or reduced by disbanding illegal groups and placing management of PSVs in the hands of their owners;
- the government has further directed all local authorities to take over management of bus parks within their areas to help remove cartels from the routes;
- two new insurance companies have started providing insurance cover to Matatus;

- crime rate has reduced owing to the requirement that all PSV drivers and conductors must possess certificates of good conduct from the police. The same requirement has also led to elimination of unqualified drivers who were major causers of accidents;
- interest is now being shown in the sub-sector by NGOs and private sector players such as insurance firms that are sponsoring seminars and workshops in safe driving for owners and workers.

4. Street Trade

22. Street traders are a sub sector of the MSEs that dominate the Kenyan economy. Recent Baseline Survey indicates that there are over 1.3 million MSEs which contribute 18 per cent of Kenya's Gross Domestic Product [GDP]. The survey states that about 64 per cent of the MSEs are in trade, under which street vendors fall. This sub sector is engaged in buying and selling of goods. Income from the trade sub-sector is ranked lowest among the MSE sector, but they are vital to the livelihoods of many urban and rural poor. These micro trade activities are sometimes referred to as 'survivalist' enterprises - they allow entrepreneurs to survive with hardly any savings. The sector is a major source of employment and income and about 48 per cent of the operators are women

23. The Kenya Labour Force Survey Report of 1998/99 indicates that the sector covers all semi organised and unregulated activities that are small scale in terms of employment. The report notes that the activities are largely undertaken by self-employed persons or employees with few workers in the open markets, in market stalls, in both developed and undeveloped premises, in residential houses or on street pavements [Labour Force Survey, 2003].

24. One outstanding feature of street trade in Kenya is that it is viewed as anti competitive, even predatory because vendors block entrances to shops and sell similar merchandise and at lower prices than the shopkeepers. The low prices are partly attributed to the fact that the vendors do not pay taxes, neither are they obligated to pay rent and other overheads costs that the formal traders incur.

25. The Local Government Reform Programme [LGRP] of 1999 focused on a key policy areas such as reduction of poverty and unemployment, and promoting higher rates of economic growth. The reforms had three components:

- improving local service delivery;
- enhancing economic governance; and
- alleviating poverty through increasing efficiency, accountability, transparency and citizen ownership.

26. Its immediate policy focus is the removal of unnecessary regulatory barriers and the reduction of costs of doing business. In particular, the government initiated two nation-wide reform efforts, namely: the Single Business Permit [SBP] and The Local Authority Transfer Fund [LATF]. The SBP in relation to small businesses is a response to business licensing problems faced by MSEs. Business licensing is aimed at protecting consumers from exploitation, health and safety hazards and control of business activities.

27. Business licensing imposes costs on businesses that are often out of proportion to the benefits delivered. Further, in practice, the regulatory provisions are abused and have become merely income earning opportunities for those charged with enforcing the regulations [Devas and Kelly 2001]. While the move to have a SBP is appreciated, it has largely benefited the small and medium firms and not micro firms where the street traders fall. The micro firms have had ad hoc policy responses from both the central

and local government levels. These responses have included relocation of street traders and affirming government commitment to the sector.

28. On the issue of policies and regulations, most urban authorities in Kenya operate on colonial by-laws that have yet to be reviewed. The policies are deficient and the urban authorities have not only failed to enforce them, but in reality, given their form and coverage, they have not been possible to enforce. While the basic idea is that licensing which is intended to enable entrepreneurs to conduct their businesses productively and profitably, it has become a stumbling block. In spite of the number of people who can be licensed being limited, once the license is given, it is shrouded with many other outdated restrictive requirements relating to public health, building requirements, and other regulations outlined in the Local Government Act. This has resulted in most traders evading licenses, and therefore flouting most regulations laid down by authorities. There is need for local authorities to put in place relevant policy frameworks and reviews of the existing by-laws if they have to conform to government policy of enhancing the performance of MSEs. A few urban councils have reviewed the by-laws relating to street trade. Other councils continue to put emphasis on enforcement without clarity on policies and regulations. The councils have not hit a balance between order, and promoting the activities and performance of informal sector operators such as street traders. Some view street traders as a temporary problem, bound to disappear, although experience has shown the contrary. The inability to address the issues is intensified by lack of effective organisation among street traders, especially in the area of representation and advocacy on issues affecting them.

29. The 2002 - 2008 Kenya Development Plan indicates measures aimed at ensuring control and regulation of hawking within the Central Business District. Most urban local authorities have begun implementing this policy with due to lack of adequate space for all street vendors within the CBD. For instance in the case of the CBD of the capital city of Nairobi, where over fifty thousand street traders operate, the city has only managed to set aside sites that can accommodate about 7,000 traders. This move is positive, although the tenure remains unclear, with the urban authorities viewing the sites as temporary while the vendors view them as permanent. Although the urban authority had a plan to charge some fees, this has not been possible due to a mix up in allocation. There were cases of double allocations, infiltration by those not allocated sites and hostility directed at the City Council Authorities. This has resulted in a stand off situation that can only be solved through dialogue and negotiation. Most of these sites lack infrastructure and services and are congested. The congestion is due in part to infiltration by vendors not allocated sites, and also by vendors allocated unfavourable sites where there is insecurity and fewer customers. These are aspects that should have been taken into consideration before relocation. Past experience of ad hoc street traders relocation indicate that without critical consideration of access to customers and security, relocation efforts will continue to be resisted.

30. In the relocation process, associations have not been effectively used, partly due to their fragmentation and weakness. The city authorities opted to use representatives of street traders drawn from different areas of the CBD. The role of these representatives was largely to listen to the packages being offered by the authorities, as opposed to negotiation and dialogue. Their 'listening' role and failure to negotiate for appropriate relocation sites and an efficient allocation process made most street traders feel betrayed. The relocation policy would have been more successful, if the street traders had a unifying body advocating and negotiating on their behalf. Ensuring a dynamic MSE sector requires functioning associations that support entrepreneurs, lobby and dialogue with authorities for enabling MSE policies and programmes. Associations are useful for purchasing raw materials, marketing, bulk transport, sharing tools and equipment, guaranteeing loans, providing market information and linking up with training and business service providers.

5. Sector Reforms

31. The Sessional Paper No. 2 of 1992 notes that the role of Government in the development of the sector will be one of facilitator rather than that of interventionist. This is due to the fact that there has been concern that in attempting to intervene to help it 'grow' its dynamism, ruggedness and innovativeness may be affected. The enabling environment the government has already established or proposes to establish includes investment allowances for starting new factories outside the major cities, duty exemptions for the purchase of capital machinery for small enterprises located in rural areas, support for technological assessment of innovation, developing market incentives to encourage subcontracting to small enterprises and reducing the harassment of the entrepreneurs operating on public land or sites, setting up vocational training centres for apprenticeships etc. Several NGOs and local banks have also attempted to assist small sector entrepreneurs to access credit for start ups and expansion of their businesses

32. Over the years, the Government has continually recognised the role of the informal economy in several policy documents. Under the Development Plan of 2002, various rules and regulations that affect the operation and growth of the sector were reviewed. Other policy responses have included: elimination of trade licensing at Central government level; harmonizing, rationalisation and implementation of Single Business Permit (SBP); and on-going review of labour laws; relaxation of business regulations; broadening access to finance; the enactment of MSE Act; and measures aimed at ensuring control and regulation of hawking within the Central Business Districts of major towns. Under the Economic Strategy for Wealth and Employment Creation (2003-2007), the government committed itself to address factors responsible for the poor performance of productive sectors, which include: high cost of engaging in productive activities, high cost of capital particularly for MSEs and lack of supportive and weak institutions. The initiative was to be achieved by removing *various regulatory impediments that increase the cost of doing business*, promoting MSEs by finalizing and implementing a Sessional paper on the sector, *focusing on employment creation and formalisation of informal activities*.

33. The strategy paper further states that the formal and informal sectors in Kenya are basically the same, and the only difference being size. The latter are however denied essential services as *well as infrastructure as they do not pay taxes*. The Paper proposed to eliminate this dichotomy by providing infrastructure and services, particularly financial, to small and medium enterprises and by *ensuring that they pay taxes*.

34. In the past, the emphasis on the formal private sector has exposed the private informal sector to the vagaries of bad governance, dominated by inefficiency and rent seeking bureaucrats and policy makers. Such officers have been more concerned with rent seeking rather than ensuring the formalisation of adequate policies and efficient implementation of policy provisions. The Policy concern therefore has been how to provide equal opportunities to both the informal and formal sectors of the economy as their integration would lead to one vibrant economy.

35. Under Vision 2030, Kenya' aims to be a newly industrializing "middle income Country providing high quality life for all of its citizens", the government has therefore committed itself to "raise the market share of products sold through *formal* channels (e.g. supermarkets) from the current 5% to 30% by 2012.....this will also contribute an additional Kshs.50 billion to the GDP. At producer level, the plan aims at building "Producer Business Group" (PBGs) which will in turn feed large wholesale hubs principally in the rural areas. These hubs will be "Tier 1" retail markets which will provide the primary producer with better value than at present when markets are heavily fragmented."