

Public Sector Reform and Institutional Capacity Building:

Joint Statement by Development Partners at the Kenya Consultative Group Meeting

24th – 25th November 2003, Nairobi, Kenya

Introduction

This statement covers the key issues associated with public sector reform and capacity building. As noted in the Economic Recovery Strategy for Wealth and Employment Creation (ERSWEC) paper, the public sector is both large and relatively inefficient. The ERSWEC Investment Programme Financing Framework takes a three-pronged approach to increasing the funding available for implementation: (1) increasing donor resources, (2) reducing the wage bill, and (3) privatisation.

The Government of Kenya is to be commended for articulating a bold vision in the ERSWEC paper. This vision embraces a public-private partnership as each party does what they do best with the Government becoming a leaner, more efficient provider of policy frameworks and services that will facilitate the private sector as an engine of growth.

Recent developments:

Civil Service Reforms

The Government has been carrying out civil service reforms over the past decade by downsizing the core civil service, harmonising pay and benefits and putting in place interventions to enhance civil service efficiency. Indeed, the civil service has declined from 272,000 in 1991 to 193,000 in 2002. In spite of this reduction, the wage bill as a percentage of Government revenue is currently around US\$40 in Kenya as compared to 30-33% in other countries within the sub-region.

The Government is strongly commended for its announced commitment to accelerating the Public Service Reform to create a leaner, efficient, motivated and more productive institution that concentrates public finance and human resources on the delivery of core government services.

Local Authorities Reforms

Throughout the world, the consensus is that governance and service delivery are improved when managed as close to the beneficiary as possible to better respond to his/her needs. In addition,

businesses generally choose to locate in those areas where essential services are delivered in a reliable and low-cost way.

To date the most significant reform implemented is the Local Authority Transfer Fund (LATF) and associated measure to strengthen local authorities' capacity to manage their finances and improve service delivery.

Public Enterprise Reforms

One of the principal findings of the 2003 Public Expenditure Review was the inordinate level of funding which was transferred from core Government services to cover the debt incurred by loss-making parastatals involved in economic activities that are generally more efficiently managed by the private sector. Therefore, the Government statement that it "remains fully committed to moving away from commercial activities that can be performed more efficiently and effectively by the private sector" is welcomed by the donor community, investors, and Kenyan consumers.

In the ERSWEC, the Government has presented an overview of its plans to:

- Further liberalise the telecommunication sector;
- Prepare Kenya Railways Corporation for concessioning;
- Transform the Kenya Ports Authority into a landlord port by June 2004;
- Prepare a specific time-bound action plan to realise the objectives:
 - reducing the Government's direct equity in Kenya Power and Lighting Company,
 - implementing reforms to strengthen the regulatory function of the Electricity Regulatory Board (ERB),
 - restructuring of the Kenya Electricity Generating Company (KenGen) to enable a Public Private Partnership necessary to mobilise the investment needed for expanding generation capacity;
- Establish the necessary institutions to facilitate policy formulation, service delivery and regulation of the water sector;
- Implement the concession for the management and maintenance of the Northern Corridor dual-carriageway;
- Put in place a time-bound action plan for the privatisation of Chemelil Sugar Company; and
- Prepare a Privatisation Bill to be tabled before Parliament and develop a clear privatisation strategy and programme with an implementation plan and timetable for the remaining list of public enterprises.

In addition to these efforts, the Government has committed itself to restructuring and privatisation of the National Bank of Kenya and the Kenya Commercial Bank.

Key challenges:

As discussed above, the Government must be commended. The Economic Recovery Strategy for Wealth and Employment Creation is the articulation of the bold and comprehensive approach it has adopted to public sector reform as a means to economic recovery. The challenge facing Kenya now is to accelerate the implementation and results delivery of the reforms. However, the capacity to achieve the desired results is often fragile. In this respect, the development of capacity, especially implementation capacity, in both the public and private sectors, that will enable Kenya to transform its economy will be critical. It is essential that the public sector scale-down its size, become more efficient and effective. The public sector must facilitate private sector investment by providing the necessary policy framework and delivering necessary social and infrastructural services. It is equally essential that the private sector develop the capacity to respond to emerging opportunities and challenges within a competitive market framework that allocates scarce resources efficiently and furthers the national welfare.

One of the key challenges in public sector reform, especially the privatisation of public enterprises is to gauge the pace of reform in such a way that the private sector is able to assume the responsibilities previously undertaken by the public sector. This is a delicate balancing act. If privatisation is undertaken too quickly, without adequate institutional capacity within the private sector, one runs the risk of incurring market failure and social distraction. If, on the other hand, privatisation is too slow, one risks declining investor confidence and economic stagnation. Given the Government deficit and the magnitude of resources needed within the social sector for the provision of education and health services, it is essential to find the middle ground, monitor private sector actions, and undertake privatisation as quickly as feasible without risking market failure of vital services. It will be essential for the Government to develop the capacity for effective regulation to ensure that privatised enterprises fulfill public policy objectives.

A further challenge will be to expand the privatisation efforts to include agricultural and livestock marketing parastatals that represent a significant drain on public resources. In this regard, public intervention should be undertaken with clear objectives and a clear and definite exit strategy based on the outcome of interventions.

A final challenge will be to find an acceptable balance between short-term (often politically motivated), fixes to an industry and more sustainable, longer-term responses that will contribute to the achievement of national objectives. This challenge is especially relevant in the context of a nation that has a history of public sector market interventions and the political incentive for Government to demonstrate that it is improving the immediate well-being of the people.

Priority actions:

The objectives of the Public Sector Reform and Capacity Building exercise are to enable the Government to reduce the budget deficit, direct scarce resources to priority needs especially in the social sectors and establish an environment that is conducive to both domestic and foreign investment. To achieve these goals movement on several fronts will be required.

At a minimum it is our hope and expectation that the Government will:

1. Stay the course on privatisation/private sector participation in the commercial activities of public enterprises including, inter alia,
 - Concessioning of railways at an accelerated pace and taking prior actions in preparation for concessioning;
 - Continue with telecommunication sector liberalisation;
 - Implement the decision of converting Kenya Ports Authority (KPA) to a landlord port;
 - Implement the PSP schemes in Nairobi and Mombasa;
2. Develop a policy choice or preferred option to reduce the wage bill within the macroeconomic framework and improve productive with a time-bound action plan to be implemented and the institutionalisation of performance-based management systems in the public sector;
3. Privatisation: the development and approval of legislation and time-bound action plan taking into consideration the capacity of the private-sector to respond to opportunities and challenges;
4. Commitment by Government to minimise any new public investment in utilities or the financial sector to the minimum required for making them attractive to private sector participation; and
5. An examination and policy determination of the role of Government in its support of agricultural marketing parastatals in light of the ongoing strategic planning exercise.