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Strengthening Cooperatives for Greater Economic Development in Kenya

KEY MESSAGES

- Cooperatives continue to play an important role in employment, income generation and poverty reduction in the country.
- Important constraints hampering cooperatives from realizing their potential include both governance and management challenges at all levels, as well as political interference.
- Agricultural cooperatives (e.g., coffee, cotton, pyrethrum, sugarcane) suffer from low supply of outputs and high costs due to inadequate inputs, extension services and credit.
- Cooperatives have also faced policy and institutional constraints including legal and regulatory challenges since the liberalization of the sector.
- Revamping of cooperatives is urgently needed in order to overcome existing constraints, improve the legal and regulatory framework, strengthen coordination and facilitate the contribution of the cooperative sector to the Government's Big Four Agenda.
- More resources for the sector must be found and utilized efficiently.

The Government has made serious and commendable efforts to promote cooperative development over the years as reflected in five-year development plans, sessional papers and more recently in Kenya Vision 2030 and the Big Four Agenda. This policy brief presents some ideas about what might be done to ensure that the country continues to promote and support the cooperative movement in order to contribute to both the short and long-term goals outlined in Kenya Vision 2030 and the Government's Big Four Agenda.

1. Introduction

After Independence in 1963, the cooperative movement was vibrant and well supported through various institutions including the ministry responsible for Cooperative Development and umbrella bodies – the Kenya Federation of Cooperatives Union for promotion and advocacy (now the Cooperative Alliance of Kenya), Kenya Planters Co-operative Union (KPCU) for coffee milling (Baka, 2013), presently in receivership, the Kenya Farmers Association (KFA), which later was renamed the Kenya Grain Growers Co-operative Union (KGGCU) before reverting to KFA, for supply of inputs, and many district cooperative unions which handled inputs supply and distribution, banking and bookkeeping services and, to a small extent, extension and advisory services.

In addition, there was significant donor support bringing in significant resources.¹ The Co operative Bank of Kenya had also been establishment to provide, among other things, credit for cooperative production and for long-term cooperative investment. On the whole, the cooperative movement was floated as an important instrument of mass participation in national development. Despite many challenges, some successes were achieved in the provision of access to inputs and services, income generation in initial subsectors especially in the agricultural marketing cooperative societies (coffee, milk, cotton, and pyrethrum), land purchases and housing cooperatives. The shortage of qualified and experienced personnel, especially for accounting and management functions, was and is a serious constraint, then and now. Following the adoption of Structural Adjustment Programmes (SAPs), liberal-ization and legal reforms were implemented that led to the liberalization of coffee marketing and the establishment of private coffee mills, and the separation of district cooperative unions and coffee cooperative societies. This led to declining support from the development partners, which resulted in reduced support to the cooperative sub-sector and challenges to and constraints for the promotion of cooperatives

¹ Important donors included the Scandinavian countries: Danish International Development Agency (DANIDA); Finnish International Development Agency (FINNIDA), Norwegian International Development Agency (NORAD) and Swedish International Development Agency (SIDA).

development (Develtere et.al., 2008). Support to agricultural extension for farmers was also severely affected by reduced funding.

In addition, there has been a major decline in crop production (coffee, cotton, pyrethrum) accompanied by the break-up of cooperatives and unions into smaller units (especially for coffee), raising the per-unit cost of processing. Also significant is the emergence of cartels² in the marketing of products and inputs which has not augured well for farmers' returns. In addition, the licensing of larger producers among the coffee cooperatives to process and market their own coffee has further undermined coffee cooperatives. In the recent past, however, we have also witnessed cooperative societies that are milling their own coffee, as well as increased production by and improved performance of dairy cooperative societies.

2. Agricultural cooperatives

An important constraint on the performance of agricultural cooperatives is the low level of output (at the farm level) that is channeled through marketing cooperatives. There has been a major decline in the production of coffee, cotton and pyrethrum; this can be attributed to poor producer prices, inappropriate technology on small-scale farms and the decline in coordinated agricultural extension, advisory and information services. The decline in output has further undermined processing facilities with low throughput, thereby raising unit production and processing costs.

2.1 Coffee

Liberalization of marketing and the reduced role of the ministry in charge of cooperatives led to break-up of some societies resulting in higher overhead costs. Lack of credit for critical inputs such as fertilizers and pesticide chemicals for disease and pest control led to a decline in the quality of smallholder coffee. Individual farmer production, processing and direct marketing abroad has also been a major challenge. The loss of the larger and better off farmers to pursue their own initiatives in this regard, together with breaking up of coffee cooperatives into smaller societies with higher overhead costs, is a significant problem. There is a case for some amalgamation of societies and rehabilitation of coffee factories (for wet processing). In addition, centralized marketing vis-a-vis private marketing/treaties needs to be revisited, although it may not be possible in a liberalized market. It is commendable that there is a presidential taskforce which has been working on the coffee subsector. The major issues in production of coffee include supply of inputs, farm credit, processing in coffee factories, drying, milling, grading and marketing. There is a need for a detailed socio-economic analysis of costs and benefits. Opportunities that exist in the coffee sub-sector include adoption of new

breeds of coffee that require less spraying, such Ruiru II and Batian. In the last three years, good quality coffee has been fetching fairly good prices.

2.2 Pyrethrum

Until 1992, Kenya was the major supplier of pyrethrum in the world market. Smallholder cooperatives used to run driers and delivered the dried flowers to the Pyrethrum Marketing Board (PMB) in Nakuru. Pyrethrum production then suffered a major decline in output due to lower demand resulting from the introduction of chemical substitutes. The demand for the natural insecticide – pyrethrin – is now buoyant, given environmental concerns of the use of chemical substitutes, and on the path to recovery. To revive the industry there is a need for the PMB to distribute improved planting materials (with higher pyrethrin content) to farmers and to reinvestigate research and extension in order to raise production levels. In addition, a major effort to revive pyrethrum cooperatives must be mounted in order to improve the efficiency and performance of producers.

2.3 Cotton

Cotton cooperatives relied on output of smallholders. Cotton is attractive because of its lint and also the cotton seed which is processed into oil and cottonseed cake for animal feeds. Cotton production has nearly collapsed in the country. The small output (28,000 bales) is marketed through private traders and smallholder cooperatives. If promoted and supported, the cotton industry could provide a good opportunity for industrialization and the export of textiles and clothing under the African Growth and Opportunity Act (AGOA). The chain from production of seed cotton to ginning and weaving of lint and processing of cottonseed can generate many jobs. The new biotech (genetically modified) cotton provides the option of higher yields and lower production costs due to reduced spraying costs.

2.4 Sugar cane cooperative societies

Sugar cane cooperative societies have met with significant challenges on two fronts. On the marketing side, the sugar mills (Chemelil, Muhoroni, Sony, Mumias and Nzoia) had various management challenges and some-times have not been able to pay for the cane. Further, the mills have been unable to compete against cheap sugar imports from COMESA, Brazil, etc. On the production front, critical inputs are needed such as seed and fertilizer, which require affordable credit, which in better days was provided to the out growers by the sugar mills through farmer cooperatives. The cane varieties also take an inordinately long time to mature compared to those used in competitor countries, where the norm is 12 months compared to 18 months domestically.

² A Cartel is an association of manufacturers or suppliers with the purpose of maintaining prices at a high level and restricting competition or a coalition or cooperative arrangement between political parties intended to promote a mutual interest.

3. Cooperatives dealing with animal products

3.1 Dairy cooperatives

Dairy cooperative societies are at the moment the most vibrant in the country. Milk is the major product handled by dairy cooperatives. Milk involves collection and assembly, cooling and delivery to processing plants – New KCC, Brookside, and others. Some cooperatives own dairy processing plants where they process (pasteurize, homogenize and pack) the milk (e.g., Meru, Githunguri and Bungoma). Other cooperatives may wish to follow the trend but will need to conduct feasibility studies. Marketing in the wet season, when there is a milk surplus, would have to be addressed.

3.2 Fishing cooperatives

These operate at the coast and Lake Victoria, dealing with the handling, storage, transport and marketing of fish, which can cause problems. Other problems relate to fishing equipment (costs), lack of credit and non-existent extension services. The high-priority official attention to the blue economy has regenerated interest in the development of this subsector.

4. Infrastructure cooperatives

4.1 Housing cooperatives

Housing cooperatives can make a significant contribution to increased supply of affordable houses, which forms one of the pillars of the Government's Big Four Agenda on affordable housing. Many housing cooperatives own land. Such cooperatives can be facilitated through the subdivision and provision of individual land titles for the land that is cooperatively owned which could then be used as collateral for housing loans. Housing loans would be useful to members who may want to construct their own houses. Provision of housing through the cooperative framework has been used with some success in some societies in Kenya. Support is initially needed in planning and development of feasible housing schemes. Also associated with housing are branch markets and small-scale brick-making factories.

There are many saving and credit cooperative societies (SACCOs) and housing cooperatives that are mobilizing resources from members for onward lending to their members for housing development. The Government could adopt similar models for improving access to affordable housing by working with the current SACCOs and housing cooperatives by improving their capitalization so that they can reach more members. Secondly, the Government could work with the county governments to develop and build capacity of new societies for housing. This has the advantage in that the Government would provide funds additional to the SACCO's own funds, which would then be

lent to SACCO members. The advantage is that members would not view the funds as public funds but as loans from the SACCO's funds which have to be repaid as any other SACCO or cooperative loans. Thirdly, it encourages savings and not just borrowing.

5. Handicrafts cooperatives/small-scale industries (SMES)

Among handicrafts cooperatives are wood carving and soapstone societies. Assistance is provided by the national handicraft marketing union. Effective product planning and quality control procedures are still a challenge. Imparting skills is critical in product development and the training of artisans.

Among the small-scale industries are those that fabricate farm equipment, furniture, appliances, clothing, leather goods, footwear and household utensils. Marketing of products is highly regimented, which is a challenge. Much effort will need to be mounted to address many of the constraints in this sub sector.

6. Transport cooperatives

The transport cooperative societies, which are erroneously referred to as SACCOs, mainly deal with the provision of public transport services in form of matatus/and or taxis. It is clear that such cooperative societies do not strictly play within cooperative rules in accordance with the Rochdale Principles. There is a lack of a clear urban transport policy to cover urban/rural transport problems. Many of the SACCOs operate transport services for travelers moving from rural to urban areas and back. Some of the cooperative societies are too small, with many routes having more than one SACCO (Mitullah and Onsate, 2013). There are other numerous challenges facing these cooperatives.

7. Water cooperatives

Under the Ministry of Water and Sanitation, a section has always existed with the remit of coordinating efforts in developing, operating and maintaining self-help/cooperative water schemes in the country. Important considerations are development, operation and maintenance of such schemes and the training of operators. This being one of the devolved functions, challenges are emerging with respect to autonomy of water cooperatives from control by County Governments, with some of these governments seeking total control/nationalization or take-over.

8. SACCOs

SACCOs have played and continue to play an important role in the mobilization of savings among members in regular

wage employment in urban areas and to some extent co-operators in productive activities in the rural and urban areas. SACCOs are one of the most important and often visible types of cooperatives in Kenya. Their distinguishing and unique characteristic is the object and purpose for which they are incorporated, which is to transact the business of the mobilization of savings and advancement of credit facilities to their members. The provision of savings and credit facilities is part and parcel of the financial services sector and, consequently, SACCOs are also often referred to as financial cooperatives, and are clustered as such together with other financial intermediating cooperatives like investment and housing cooperatives.

The SACCO subsector is legally divided into two segments, principally defined or differentiated by the nature of savings and deposits that they mobilize from their membership. The first segment consists of the deposit-taking SACCOs (DT-SACCOs), while the second segment consists of the non-deposit-taking SACCOs (non-DT-SACCOs). The Sacco Societies Regulatory Authority (SASRA) plays an important role in the regulation of DT-SACCOs.

These funds mobilized by SACCOs are on-lent to members of the SACCO. Many SACCOs have provided affordable credit and financial services for productive income-generating activities and financial education among other activities. An important challenge is efficient management to meet their objectives. A number of SACCOs have been plagued by corruption. It should, however, be stated that there are some extremely successful member-controlled SACCOs in the country that have served their members very well.

The Way Forward

Cooperatives will continue to play an important role in the economic development of Kenya (Republic of Kenya, 2017). They will contribute to the President's development agenda on, food and nutrition, industrialization, affordable housing, and health, and more specifically in income-generation and employment creation. Some of the challenges that need to be addressed include:

1. Legal and regulatory framework/ governance: the registration of cooperative societies and SACCOs needs to be revisited to improve their performance and productivity, to generate efficiency and economies of scale, and to align them to the national objectives as set out in Vision 2030 and the President's Big Four Agenda, and to reflect the devolved system of governance. According to the State Department of Cooperatives the national Government will facilitate growth and development of cooperatives nationally while the counties shall be responsible for cooperatives in their respective counties, (Republic of Kenya, 2017).
2. In the case of cooperatives related to agriculture, the main challenges revolve around production and marketing issues. Pertaining to production are technological issues – high-yielding varieties, input use, and output and extension services. This particular aspect relates to crops: coffee, cotton, pyrethrum, sugarcane etc. The promotion of production falls under the Ministry of Agriculture, the Kenya Agriculture and Livestock Research Organization (KALRO), and the Ministry of Industry, Trade and Cooperatives. Seeking to increase agricultural productivity is closely related to item 3 below. In order to contribute to industrialization, agricultural output should be increased to feed into agro-processing industries and value addition such as coffee pulping, drying and milling, cotton ginning to produce lint for spinning and textiles, cottonseed cake for oil and feed production, sugarcane factories for sugar production, pyrethrum for pyrethrins and so on.
3. Increasing agricultural output will require affordable credit to provide the cash outlays needed to finance agricultural enterprises. This is a shared responsibility of primary societies, unions and their respective SACCOs, and banks.
4. Management of all types of cooperatives: a lack of qualified and experienced personnel is a major impediment to the good performance of cooperatives. Cooperatives related to agro-processing industries require skilled artisans, technicians, technologists and engineers. In the management of cooperatives, experienced accountants, auditors, and marketers are essential. Skills gaps exist in all four tiers of the cooperative movement and hamper the contribution of cooperatives to industrialization. Good management would also facilitate the adoption of relevant modern technology. Although the cooperative movement has adopted and made serious attempts to implement cooperative principles and values, much remains to be done to improve governance in terms of skills critical for board members and managers. The role of cooperative societies' members and delegates needs greater attention and clarification to ensure a better understanding of their role would contribute to a reduction of rent-seeking by management and corruption.
5. It is critical that the mobilization of funds through programmes and projects designed to strengthen the cooperative movement be developed. Some cooperative programmes, such as for housing, water, and small-scale industries, are constrained by inadequate finance. Despite commendable efforts on the part of co-operators, finances are a critical constraint.
6. SACCOs need to strengthen client/ membership relationships with differentiated product offerings. In order to fight competition, they must strengthen client/ membership relationships by using needs-based segmentation, differentiated coverage, and industry-

specific value propositions. That is to say, SACCOs must be able to show that they understand that dairying is different from coffee, maize, or horticulture and develop specific products that address the needs of each value chain. SACCOs also need to keep in touch with developments in the financial services sector and invest in the development of new skills in order to keep up with the development of the sector. There is a need for SACCOs to advance beyond merely making ad hoc changes to their products so as to develop a more demand-led approach.

7. Another aspect that SACCOs need to look at in order to beat competition is to redefine and refine their product/service offerings. For a long time, SACCOs have offered the same or similar products. In fact, the product offering in a SACCO is replicated in many other SACCOs. There is a need to refine or redefine the SACCO market niches and develop tailor-made products for those niches, especially in the agricultural value chains. The idea is that the product offerings should seamlessly integrate with client value

chains (seasonality, payment times, etc.), offer value-added services and pursue continual improvement.

8. In their efforts to compete, transform, and reach more members/clients, SACCOs will face competitive, technological, and demand dynamics in the market place. They will need organizational agility, an aspirational vision, investments in talent and front-to-back agile delivery, and an intensive member/client value-driven approach. Moreover, they will need to be innovative and promote and establish partnerships with a wide range of financial institutions, models and delivery channels that will support demand-driven approaches that are sustainable and enhance poverty outreach.
9. The SACCO of the future will be more aggressive, responsive and ready to compete. Getting there, however, will require much work. SACCOs will need to reimagine their front, and back offices and develop leadership skills in innovation, risk management, and service delivery.

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