FINANCING TECHNOLOGY ENTREPRENEURS & SMES IN DEVELOPING COUNTRIES: CHALLENGES AND OPPORTUNITIES

KENYA
Country Study

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# TABLE OF CONTENTS

Executive Summary  1  
I. Introduction  3  
II. The Country Background  5  
   II.2  The ICT/ICTE Sector  5  
   II.2  Policy and Institutional Framework  6  
   II.3  The Financial Sector  7  
III. Issues in the Financing of ICT/ICTE Small Business  9  
   III.1  SME Financing Needs – The “Demand Side”  9  
   III.2  Issues in Accessing Financing – The “Supply Side”  9  
   III.3  Financing Gap – Nature and Severity  11  
IV. Conclusions and Recommendations  13  
   IV.1  Measures Aimed at Facilitating Access to Equity Financing  13  
   IV.2  Measures Aimed at Facilitating Access to Bank Financing  14  

ANNEXES  15  
Annex A – The ICT/ICTE Sector  17  
   A.1  Telecoms  17  
   A.2  Internet Services  18  
   A.3  ICT/ICTE Activities  19  
   A.4  Call Centers and BPO Services  20  
Annex B – The Institutional Setting  21  
   B.1  Public Entities  21  
   B.2  Private Entities  21
Annex C – The Financial Sector 23
   C.1 Banking and Related Activities 23
   C.2 Venture Capital 24
   C.3 Other Financing Schemes 35
Annex D – List of Entities Interviewed 27
Annex E – Profiles of SME Financing Organizations 29
Annex F – Profiles of ICT/ICTE SME 33
Annex G – Selected Sources 37
# Abbreviations and Acronyms

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Full Form</th>
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<tbody>
<tr>
<td>AEAF</td>
<td>Aureos East Africa Fund</td>
<td>ICT</td>
<td>Information and Communication Technology</td>
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<td>AfrISPA</td>
<td>African Internet Service Provider's Association</td>
<td>ICTE</td>
<td>ICT Enabled</td>
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<td>BPI</td>
<td>Business Partner International</td>
<td>IFC</td>
<td>International Finance Corporation</td>
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<td>BPO</td>
<td>Business process outsourcing</td>
<td>IFI</td>
<td>International Financial Institutions</td>
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<td>CBA</td>
<td>Commercial Bank of Africa</td>
<td>IXP</td>
<td>Internet Exchange Point</td>
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<td>CCK</td>
<td>Communication Commission of Kenya (Kenya)</td>
<td>MIC</td>
<td>Ministry of Information and Communications</td>
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<td>CRM</td>
<td>Customer Relations Management</td>
<td>MFI</td>
<td>Micro-finance Institutions</td>
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<td>DFI</td>
<td>Development Finance Institutions (Kenya)</td>
<td>NCS</td>
<td>National Communications Secretariat</td>
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<td>EACP</td>
<td>East Africa Capital Partner</td>
<td>NSE</td>
<td>Nairobi Stock Exchange</td>
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<td>EASSY</td>
<td>East Africa Submarine System</td>
<td>PDNO</td>
<td>Public Data Network Operator</td>
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<td>EC</td>
<td>European Commission</td>
<td>SME</td>
<td>Small and Medium Enterprise</td>
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<td>EIB</td>
<td>European Investment Bank</td>
<td>TESPOK</td>
<td>Telecommunication Service Provider’s Association of Kenya</td>
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<td>EPZ</td>
<td>Export Processing Zone</td>
<td>TKL</td>
<td>Telkom Kenya Ltd.</td>
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<td>ERP</td>
<td>Enterprise resource planning</td>
<td>TOR</td>
<td>Terms of Reference</td>
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<td>EU</td>
<td>European Union</td>
<td>UNDP</td>
<td>United Nations Development Program</td>
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<td>GMPCS</td>
<td>Global mobile for personnel communication system</td>
<td>UNIDO</td>
<td>United Nations Industrial Development Organization</td>
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<td>KDN</td>
<td>Kenya Data Networks</td>
<td>USAID</td>
<td>United States Agency for International Development</td>
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<td>KeKoBI</td>
<td>Kenya Kountry Business Incubator</td>
<td>VSAT</td>
<td>Very small aperture terminal</td>
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<td>KEPSA</td>
<td>Kenya Private Sector Alliance</td>
<td>WTO</td>
<td>World Trade Organization</td>
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**Exchange Rates**

- US$ 1 = KES 75.724 (average 2005)
- EUR 1 = KES 94.347 (average 2005)
EXECUTIVE SUMMARY

Kenya is home to a modest ICT/ICTE industry, most of which has emerged after the recent liberalization of the telecom sector. Leaving aside the vast group of distributors and resellers of IT equipment, which in some cases can hardly be included in the category, the Kenyan ICT/ICTE sector is mainly comprised of small enterprises active in fields such as software customization, web design, ICT value-added services and IT consultancy. Typically, the services provided are very basic. In addition, some hardware assembling activity was set up after the government lifted the import duty on parts, but the amount is still very limited. The export of services—in the form of outsourced processes—is also very limited. There are only a handful of active BPO firms and call centers. The National ICT Strategy issued by the government in 2006, places particular emphasis on the enormous potential of this industry. Nevertheless, Kenya has yet to overcome the persistent weaknesses of its telecom infrastructures, and its lack of a reliable and cost-effective international connectivity.

A few large foreign-owned commercial banks and other state-controlled entities dominate Kenya’s financial sector. The total amount of outstanding loans is increasing year by year, and financial indicators suggest that performances of banking sector are improving. Commercial banks’ lending activities have traditionally concentrated on large enterprises and consumer credit, with very little involvement in SME financing. However, signs of a slight change in attitude were evident from direct contacts with local bankers. Private equity firms account for a tiny share of the financial market. This industry exists since more than a decade, but the consolidated volume of operations has remained small-scaled. Recently, some new facilities have been opened and few more are in the pipeline, which will specifically address the demand coming from small enterprises. Microfinance is rapidly gaining ground thanks to the refinancing schemes put in by donors and IFIs, and to recent improvements in the regulatory framework. In other words, although access to financing for SMEs is today fairly difficult, some significant progresses are expected from current developments. As regards ICT/ICTE SMEs, the situation is somewhat different: this sector is regarded with greater caution by both institutional lenders and private investors, and the availability of financing is smaller than for other types of business. In summary, the Study has verified the existence of a financing gap which affects in particular ICT/ICTE enterprises seeking for US$50,000 to 500,000. The factors that concur to determine this gap are as follows:

- **Financing Policies.** Banks are wary of lending to SMEs. Loans have to be heavily securitized with personal assets, and start-ups are normally excluded from credit. Interest rates are hardly affordable. The majority of enterprises are too small for VCs to consider, and the sector is largely viewed as immature and scarcely profitable for the moment. Microfinance mostly focuses on sectors other than ICT/ICTE;

- **Limited Diffusion of Alternatives.** Credit guarantee schemes operate mostly in agribusiness sector and alike, and normally ICT/ICTE firms do not have access to them. Business Angels’ operations are almost inexistient;

- **Constraints on the Demand Side.** High degree of informality of SMEs, which are also often unwilling to disclose information on their financial status. Entrepreneurs are scarcely familiar with the equity financing instruments;

- **Understanding of ICT.** ICT/ICTE is a novelty in the Kenyan business landscape, and bankers are not entirely comfortable in dealing with these new business models;

- **Business Environment Constraints.** Monopoly persists in some key areas of telecommunication sector. Credit information system is practically inexistient.

Over the past few years, the issue of SME financing has been repeatedly indicated by public authorities and donors community as a major obstacle for country’s development. As a consequence, a number of initiatives have been designed and implemented in this field both at the policy/
regulative level and through concrete facilities. It must be said that these initiatives mainly have a generalist approach, and, albeit relevant, they are unlikely to have a significant impact on the ICT/ICTE sector, which requires specific instruments. Possible additional measures have been then identified, which could prove beneficial in facilitating the access of ICT/ICTE SMEs to bank lending and VC financing alike. As regards to private equity financing, the possible interventions that have been identified fall within two categories: (i) measures to facilitate equity investment in ICT/ICTE, like assistance to the design of a dedicated facility based on the matching funds model, and (ii) support to the strengthening and diffusion of business angel's operations in the ICT/ICTE field. At the same time, some relevant initiatives in the field of access to bank financing could be envisaged. Basically, this includes the promotion of and assistance to the establishment of credit guarantee schemes accessible to ICT/ICTE enterprises, and the provision of direct assistance to ICT/ICTE promoters to upgrade their ability in dealing with commercial banks.
I. INTRODUCTION

This report (the “Report”) has been prepared by Economisti Associati (the “Consultant”) within the framework of the assignment on “Scaling up Innovation and Entrepreneurship in Developing Countries: The Role of Private Sector Finance” (the “Assignment” or the “Study”). The overall objective of the Assignment is to analyze issues in the financing of small and medium enterprises (SME) in developing and emerging countries, with special reference to small businesses active in the information and communication technology (ICT) sector as well as in ICT-enabled (ICTE) activities.

This Report is part of Phase 2 of the Assignment and reviews recent developments in the ICT/ICTE sector in Kenya, with special emphasis on current conditions for the financing of ICT/ICTE small enterprises. The Report is based on the results of a field mission in Kenya (April 9–14, 2006) as well as on the analysis of a variety of secondary sources.

The Report is structured as follows:

- Section II presents a country overview including the ICT/ICTE industry, the relevant policy and institutional framework, and the financial system;
- Section III analyzes the main issues related to the financing of small ICT/ICTE enterprises;
- Section IV offers some conclusions and recommendations.

The Study also includes a series of Annexes, providing additional information and supporting evidence for the elements presented in the main text. In particular:

- Annex A provides additional information on the ICT/ICTE sector;
- Annex B illustrates the institutional setting for the ICT/ICTE sector;
- Annex C reviews the Kenya’s financial system;
- Annex D provides the list of entities and persons met during field work;
- Annex E presents the profiles of some SME financing organizations;
- Annex F presents the profiles of small ICT/ICTE enterprises interviewed during field work;
- Annex G provides a list of selected sources.
II. THE COUNTRY BACKGROUND

II.1 THE ICT/ICTE SECTOR

Overview. The development of the ICT/ICTE industry in Kenya is recent. It occurred with some delay compared with other African countries, mainly due to impediments of regulatory and institutional nature. Precise data are not available, but the total turnover of this sector is unlikely exceeding US$ 1.0 billion, with telecoms accounting for more than 90%. Overall, the total employment can be tentatively estimated around 20,000 and 30,000 people with again the vast majority working in telecoms. The ICT/ICTE industry comprises some 200–250 enterprises, most of which are small or micro sized. In addition to that, an estimated 500 cyber cafés are currently active in the main urban areas. The industry is little diversified and sophisticated. Most of the enterprises are basically resellers and installers of hardware and software, and IT-consultancy firms. The software development and IT services sub-sector includes some 50 enterprises, mainly involved in web design, system planning, and customization of branded application. Call centers and BPO represent a marginal share, with export of services presently accounting to not more than 10% of ICT/ICTE industry income.

Telecom. The liberalization of fixed-line market was decreed in 1999, but the former national incumbent Telkom Kenya Ltd (TKL) held exclusivity rights until 2004. As of today, no other operator has been licensed, with the exception of a local carrier active only in certain areas of the country. TKL is partly privatized but the control share is still in State’s hands. There are about 300,000 fixed-line subscribers, demonstrating a very low penetration rate, below 1%. The number of fixed-lines clients has remained almost stable since 1999. A different story is that of mobile telephony whose diffusion soared over the past few years. The number of mobile subscribers have risen from less than 1.0 million in 2002 to 6.5 million in 2006, and the mobile tele-density has grown from 3% to nearly 20%. The mobile market is presently shared between two main operators, but the Kenyan regulator announced the issuance of new licenses in this area.

Internet Services. The penetration of Internet in Kenya was hampered by delays in the build up of communication infrastructures and the adoption of a favorable legislation. The asymmetries and restrictions which characterized the telecom sector had a negative impact also in the emerging of private sector businesses in the Internet segment. Recently, the overall framework has changed significantly and important infrastructural projects are in course. But for the moment the Internet market is still lagging due to high costs and lack of connectivity in vast areas of the country. The supply side includes some 16 ISPs, but their number is declining, as the scarce profitability induces operators to merge or discontinue activities.

ICT/ICTE Activities. Kenya hosts a small and poorly diversified ICT/ICTE industry. Most of the enterprises in this field are in fact simple resellers of IT equipment and off-the-shelf software, sometimes providing installation and basic maintenance services. Another large group of players offers IT-consultancy services, while proper software development and IT services sector is limited to no more than 50 enterprises, which activities concentrate on web-based services design, content management, e-commerce, customization of ERP packages and software localization. A handful of firms provide offshore outsourcing services to foreign clients, like payroll and other administrative services, but a substantial growth of this segment is expected. Call centers are widely considered as a very promising business, though as of today the scaling up of operations is hindered by the lack of an adequate infrastructure and the high costs of broadband connection. In the field of hardware, a national PC

1 Figures are drawn from a variety of sources, including the Communication Commission of Kenya, the TESPOK association and mainly articles appeared in the press and company websites.
assembling industry is fledgling, fuelled by the support received from the State and from major telecom operators.

II.2 POLICY AND INSTITUTIONAL FRAMEWORK

Overview: Until recently, Kenya lacked of comprehensive policies for the development of ICT and the support of private sector enterprises in this field. A full liberalization of telecommunications was achieved only in 2004, while the National ICT Policy was finally released in March 2006. The necessary regulation to implement the ‘Policy’ was drafted in late 2006, but it has not been approved yet. The institutional setting was lately modified to reflect this new attitude toward ICT. The Ministry of Information and Communications (MIC) took over in 2004 from the Ministry of Transport and Communications as the authority responsible for the telecommunications policy and the realization of a national strategy for the ICT sector. A Permanent Secretariat for ICT was recently established under the MIC. This authority is entrusted inter alia for the design and the implementation of measures to support the realization of the National ICT Policy. In addition to that, the set up of an ICT Board is anticipated. The Board, which will comprise representatives of public and private sector alike, will oversee the implementation of the ICT development plans, and adopt concrete initiatives for the promotion overseas of the national ICT industry.

Legislative Framework: The reform process in the telecom sector started formally in 1998 with the issuing of the Kenya Telecommunications Act. Under this Act the former Kenya Postal & Telecommunication Corporation was split into separated entities. Telecommunications went under the control of the state-owned company TKL, while all the regulatory matters were subjected to a new independent body, the Communications Commission of Kenya (CCK). The Act provided also for the establishment of two other institutions: (i) the National Communications Secretariat (NCS)—a policy advisory body; and (ii) the Communications Appeals Tribunal. The concrete effects of the reform became tangible only six years later, when the TKLs monopoly over the key infrastructures formally came to an end and the CCK began licensing new private operators. In 2006, the National ICT Policy was adopted. The strategy lies on four pillars: (i) infrastructure development, (ii) improvement of education and skills of labor force, (iii) increased participation of the private sector in strategic projects, and (iv) the set up of an appropriate legal framework. In late 2006 the MIC has started circulating an ICT bill which is expected to translate the indications contained in the Policy into regulative acts.

Support to Private Sector Development.
Intermediary bodies such as TESPOK and Kenya ICT Federation, were significantly involved in the design of the National ICT Policy. The private sector will also be involved in projects to be implemented under the Policy, and in the prospected ICT Board. Some concrete measures in support of the BPO sector and to attract foreign investments are already in place: ICT companies located within the numerous Free Trade Zones (i) enjoy a 10 year corporate tax holiday, and (ii) are duty and VAT exempted on various items.

Cooperation with donors. The donor community is supporting ICT and the development of small-scale entrepreneurship through various initiatives. A summary description of a sample of these projects is provided below:

- In 2003, the IFC opened the SME Solution Center, a facility that provides support to SMEs. Its services include technical assistance, trainings, business information, and access to financing. The Ministry of Trade and Industry is planning to co-invest in the facility some US$4.0 million.
- Within the above-mentioned SME Solution Center is hosted the KeKoBI business incubator. This is an initiative sponsored by the infoDev Program and supported by the Ministry of Trade and Industry and the Ministry of Information and Communications.
- The World Bank is currently implementing a project specifically addressed to the SMEs denominated “Micro, Small, and Medium Enterprise (MSMEs) Competitiveness Project”. The project aims at increasing productivity, and employment in the targeted enterprises improving the overall business environment and reducing the financial gap. Recently the World

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2 For more information, the full text of the national ICT policy is available from the MIC’s website, www.information.go.ke
3 For more information see Box 1 in Annex C. See also www.ssc.co.ke
Bank has also committed US$6 million to finance the establishment of multi-level e-centers in the country.

- DFID is involved in several projects for the financing and diffusion of ICT in Kenya. It is worth mentioning, for instance, the initiative co-financed by Vodafone aimed at enabling with cellular infrastructures, financial sector institutions located in remote areas of the country.

**Regional Cooperation.** The Government of Kenya co-operates with neighboring countries in a number of regional ICT projects including:

- **The East Africa Submarine System (EASSy)** project, whose aim is installing a 9,900 km long submarine cable from South Africa to Sudan;
- **The East African Digital Transmission System (EADTS)**, that is conceived to link the major cities in the hinterland with the EASSY cable;
- **The Regional African Satellite Communications (RASCOM)**, aimed at promoting satellite telecommunications in East Africa;
- **The East African Regulators, Postal and Telecommunications Operators Forum**, which *inter alia* promotes the interconnection of the various East African Internet Exchange Points (IXP).

**II.3 THE FINANCIAL SECTOR**

**Banking Sector:** As of June 2006, total assets of banking system were about US$ 9.2 billions, two-thirds of which controlled by the six main institutions. Banks’ credit to private sector amounted to some US$ 4.8 billion, with 23% represented by non-performing loan, decreased by 7% over 2005. The Kenyan banking industry is doing well, the system is fairly liquid and the gross profit margins are increasing. Also the overall reliability has improved overtime, especially after the Central Bank’s issuance of the new guidelines on corporate governance and risk management. However, some observe that the overall capitalization is still not sufficient to protect banks from possible negative shocks. The banking industry includes 42 commercial banks. The two largest institutes are local subsidiaries of foreign banks, while two other major banks are State-controlled. Some banks offer directly or via subsidiaries other financing instruments such as leasing and factoring which are particularly appreciated by SMEs.

**Venture Capital:** Kenya is home of some venture capital operations, sometimes with a regional scope. The debut of private equity industry in the country dates back to mid nineties, with the establishment of the Acacia Fund. This was a regional scheme of US$ 20 million, which invested in some 20 deals over a period of 10 years, with substantial positive results. The Acacia’s ‘model’ is currently being replicated by the Aureos East Africa Fund (AEAF) which started operation in 2003. In addition to AEAF, two more VCs schemes have been set up between 2005 and 2006, in one case addressing early stage financing while in the other case focusing on large-scale transactions in the field of ICT. A specific regulation for Venture Capital was published by the Capital Markets Authority only in 2006. Before that date, the legal framework was largely unclear and partially restrictive, thus determining a significant delay in the diffusion of institutional VCs in the country. In addition to private VCs, equity financing is also provided by the Industrial and Commercial Development Corporation (ICDC), which is a State-owned institution with a significant share of operations in the SME segment. As for the near future, the East Africa Development Bank is reported to be setting up a private equity fund for SMEs operating in Kenya, Tanzania and Uganda.

**Business Angels:** Angel investing is quite a novelty in Kenya. The concept is currently being developed by IFC, which started in 2005 to work around the idea of a Business Angel Group (BAG). The project is still in its initial stage and so far, the activities have concentrated on the identification of possible participants and the analysis of the relevant legal framework. In summary, the model puts forward by BAG would combine three aspects: (i) investments, with possible deal-size: US$10,000 to 70,000; (ii) mentoring; and (iii) technical assistance. The first company presentation was held in March 2006, with the presence of 4 promoters and some 15 BAG’s members.

**Micro-lending and Government Schemes:** Various micro-lending schemes are offered by banks, micro finance institutions (MFI), credit cooperatives and alike. The total amount of outstanding loans in this segment is of about US$0.5 billion. These schemes are often supported by IFIs and other donors’
programs. The micro finance industry comprises 130 MFIs of various nature and about 4000 savings and credit cooperatives. The main MFIs are grouped under the umbrella of the Association of Microfinance Institutions (AMFI). As of the end of 2006, the AMFI’s members had consolidated outstanding loans for about US$210 million. In the public sector, the main development finance institutions dealing with SMEs is the already mentioned ICDC, whose activities include debt and equity schemes. Since its establishment, some 40 years ago, ICDC has reportedly assisted some 15,000 SMEs.
III. ISSUES IN THE FINANCING OF ICT/ICTE SMALL BUSINESS

III.1 SME FINANCING NEEDS – THE DEMAND SIDE

ICT/ICTE Companies: The financing needs voiced by Kenyan ICT/ICTE enterprises reflect the weaknesses of a fledgling industry which includes at a large extent young micro enterprises and very few established operators. The amounts sought by ICT/ICTE companies vary according to the business models, but tend to remain relatively low. Startups typically content themselves with sums in the order of US$10,000 to 50,000, while for expanding businesses financing needs are unlikely to exceed half million dollars. The rationale for these needs is also varied, with prevalence of R&D, product development, capacity building, marketing etc. Table 1 below summarizes the salient features of financing needs voiced by ICT/ICTE firms across the different stages of development.

Considerations on Specific Sub-Sectors: The above considerations do not apply to all type of ICT/ICTE companies. In particular some specifications are required with respect to call centers, which normally display different investment patterns. The initial investment to set up a call centers is definitely more sizeable than for any other ICT/ICTE enterprise. This is mainly due to a couple of factors: (i) at least some 30–40 seats are necessary since the very beginning; (ii) high costs for trainings personnel, must be taken into account because of the frequent turnover of employees. In later stage, call centers normally evolve in one main direction that is the scaling up of their capacity, through an increased number of seats available. Once maturity is reached, in some cases a slight diversification is observed, with the introduction of new outsourced services. However, apparently none of the Kenyan call centers has reached this stage.

III.2 ISSUES IN ACCESSING FINANCING – THE SUPPLY SIDE

Issues in Accessing Bank Financing: Kenya is commonly not classified as an economy with severe obstacles in access to credit. In the Doing Business ‘getting credit’ ranking, Kenya occupies the 33rd place, ahead of many OECD countries, while according to the Enterprise Surveys nearly one-third of enterprises’ investments are financed by banks—which is 14 points above the regional average. Nevertheless, evidence from the fieldwork showed that borrowing from commercial banks is far from being easy for SMEs, and especially when operating in the ICT/ICTE sector. Firstly, this is due to the conservative attitude of the majority of banks. Conditions applied are usually very stringent. The value of collateral normally requested is 30 points above the regional average, amounting to some 172% of the sum borrowed, and it can easily approach 200% in the case of SME. This is particularly affecting software developers and IT service providers as these businesses notoriously rely on ‘immaterial’ assets rather than on tangible features. Reportedly, the only bank practicing, to a certain extent, a policy of unsecuritized lending is the Barclay’s Bank. Furthermore, Kenyan banks pay much attention to the business history of the applicants. For instance, Kenya Commercial Bank (KCB) commonly request to monitor the financial

4 More details on the firms mentioned in this section are provided in Annex F.
statements of would-be borrowers for a three-year period before extending a loan to a SME. Finally, most of banks concentrate on overdraft lending and contract financing, while medium and long-term loans— which are typically asked by SMEs at early stage of development—are hardly available. The situation does not change significantly in the microfinance sector, where loans, with a tenure above three years, are very rare. The level of interest rates is viewed as an additional obstacle. Normally, rates range from 13% to 15% p.a., but in the case of micro-lending they can easily climb to 19–20%. ‘Subsidized’ rates will be applied to entrepreneurs borrowing from the “Youth Enterprise Development Fund” (see Annex C), that will be operational in 2007. At the same time the difficulties in dealing with banks can be also ascribed to would-be borrowers’ approach. SMEs are often informally, and promoters are typically unable to provide reliable financial statements and accurate business plans as requested by bank officers. In addition to that, Kenyan entrepreneurs are reported to be particularly bank-averse, and field contacts confirmed that in many cases this attitude is not based on direct experience but on a sort of a priori basis. In late 2006, the Kenyan Parliament passed some amendments to the Banking Act in order to have an impact on access to credit. The new provisions enhance the functioning of the credit information system.

### TABLE 1. Summary Presentation of ICT/ICTE Financing Needs

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<th>Lifecycle</th>
<th>Amount Sought</th>
<th>Rationale</th>
<th>Examples from fieldwork</th>
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<tr>
<td>Early Stage</td>
<td>US$10,000 to 50,000</td>
<td>The initial stage goes from the conception of the business idea to its commercialization. In the case of Kenya, the field interviews showed that, at these stage of development, financing needs are very limited, as most of startups focus on business models which require little physical assets in their fixed-cost structure, like: webdesign, e-content, and alike. The bulk of the investment at this stage relate to typical ‘seed’ activities, R&amp;D and initial development of the business concept, as well as to purchase of equipments and licenses, product development, and initial marketing efforts.</td>
<td>E-Mart Solution – Web-based solutions, e-commerce (KeKoBi incubatee)</td>
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<td>Development</td>
<td>US$50,000 to 150,000</td>
<td>This phase corresponds to the proper “formalization” of the business and the actual commercialization of the products/services developed in the initial stage. Financing requirements typically refer to the need of supporting market development, with the creation of adequate “production capacity” (i.e. the hiring of software engineers and technicians) and the build up of working capital. In the case of Kenya, financing needs at this stage range remains however quite low, for the relatively simple nature of most of ICT businesses.</td>
<td>Spreading Wings – software dev., IT services (KeKoBi incubatee)</td>
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<td>First Expansion</td>
<td>US$150,000 to 500,000</td>
<td>The first expansion phase is often associated with the launch of a new, upgraded version of the original product, which incorporates and systematizes the improvements gradually introduced during the first commercialization phase. In other cases, the expansion phase involves some degree of diversification, with the introduction of new products/services which build upon the technical expertise acquired and/or on the connections established with certain clients. This phase also characterizes small retail businesses opening subsidiaries in other areas. Depending on the nature of the business, financing needs can vary considerably.</td>
<td>Rivotech – software dev., localization services (KeKoBi incubatee)</td>
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<tr>
<td>Second Expansion</td>
<td>More than US$0.5 million</td>
<td>This stage of development is associated with a major change in the scale of operations, often associated with the scaling up of international operations. In this case, financing requirements relate to the establishment of commercial subsidiaries and/or technical assistance centers abroad, as well as to a host of other internationalization-related expenses. In the case of Kenya very few examples of firms at this stage can be identified.</td>
<td>Easy Surf – Cyber cafe</td>
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<td>ISP Kenya – internet provision and value-added services</td>
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8 Other banks apply even more stringent rules: an entrepreneur met during the fieldwork reported that despite his five-year successful business history his bank was unwilling to lend, and eventually he had to ‘alter’ the financial statements to obtain a loan.

9 As of June 2006 the Central Bank reported that the average lending rate was at 13.79%.
through the definition of nature and mandate of credit bureaus, and streamlining the procedure for the exchange of information between banks and bureaus, and more generally. As far as more SMEs will be progressively included in the system, a major improvement in the access to bank financing is expected.

**Issues in Accessing Equity Financing**: The ICT/ICTE sector has been historically neglected by Kenyan private equity firms. The Acacia Fund—and afterwards AEAF—has invested in 21 firms so far, but none of which was an ICT/ICTE enterprises. Other recently established facilities appear more inclined to invest in this sector, but the overall conditions are still not conducive for a large deployment of venture capital in ICT/ICTE industry. Some hampering factors can be summarized as follows:

- As of today, this sector comprises few ‘genuine’ IT enterprises diluted in a multitude of substantially speculative operations. In few years most of the latter are destined to disappear and the valid business ideas will emerge more clearly. Hence, some investors deem premature to venture in this arena at this stage, and rather wait for the situation to evolve;
- Today, most of ICT/ICTE enterprises active in Kenya are startups. This means that they require an intensive financial effort for a period of at least 2–3 years before becoming really profitable. With an usual investment duration of 5–6 years, it is therefore uneconomic for a VC to consider businesses at this stage of maturity;
- The Kenyan final market for ICT/ICTE is thin, and any business in this field is unlikely to generate important earnings, unless maybe large operations in telecom or infrastructures.

**Government and Donors Schemes**: Kenyan SMEs employ some 3.5 million people, accounting for about 18% of county’s GDP. The development of SMEs is increasingly regarded by the Kenyan Government as an important instrument to improve the employment rate and to achieve a more balance distribution of wealth among the regions. In Kenya, the economic power is traditionally held by few large public and private firms, while SMEs operate in an environment that often lacks adequate technical and financial support. In this sense, some measures have been recently taken at the regulatory level to upgrade the institutional framework for SME lending activities. In addition to that, a direct lending scheme at a subsidized rate, is envisaged (YEDF), but it will seemingly target only enterprises at the seed stage. The efforts deployed by donors and IFIs in this line appear somewhat more consistent. As seen in previous sections, some interesting pilot projects for SME development are already running, while few more initiatives are in the pipeline. In particular, the financing facility attached to the SME Solution Center (see Box 1 – Annex C) will help cover one of the most problematic areas of financing represented by projects in the US$50,000 to 500,000 range. In the near future, this area will also be covered by another SME-dedicated private equity fund. This is an EADB’s scheme, which will provide financing from US$100,000 to 1.0 million to SMEs active in various sectors (including ICT) and operating in the East Africa region.

### III.3 Financing Gap – Nature and Severity

**Overview**: Although somewhat mitigated by State’s and donors’ initiatives described above, it is undeniable the existence of a financing gap for ICT/ICTE SMEs. Most of the schemes discussed will be fully operational over the next few years and a proper assessment of their efficiency and ability in reducing the gap will be possible only at that time. As of today, access to financing is severely tackling the development and expansion of various SMEs in ICT/ICTE sector, as diagrammatically illustrated in Figure 3 below.

As indicated in the figure above, financing constraints faced by ICT companies appear comparatively more severe in the development and first expansion phases, while the situation is more nuanced in other phases. In particular:

- In the *early stage* financing needs are very limited, usually in the order of US$10,000–30,000. These amounts are compatible with the recourse to entrepreneur’s personal savings and other informal channels. Similar amounts can also be borrowed from micro-lending facilities, e.g. K-Rep Bank, Equity Bank, Cooperative Bank. Business incubators play an important role at
At this stage in assisting the entrepreneur in various ways, such as the assessment of the real financial needs, the identification of the most suitable source of financing, and the preparation of the relevant documentation. The prospected YEDF, which will become operational in 2007, will also likely cover this area of need.

The problem area starts above the US$50,000 mark. The development and first expansion are critical phases in the SME’s life cycle. At these stages, products and services have been developed and commercialization has begun, though at a limited scale. Some commercial banks manage SME-lending schemes, but startups are generally excluded. Furthermore, ICT/ICTE is typically regarded as a very volatile sector. In addition to that, the level of interest rates is often not affordable for many of these entrepreneurs. As for equity financing, deals at these stages are usually too small for institutional VCs. For instance, AEAF considers transactions only above the US$0.5 million threshold, and EACP even larger. In principle, the amounts sought could be compatible with ICDC equity schemes, but de facto no ICT/ICTE firms have ever managed to tap into this source. The establishment of the SME Solution Center, with the attached BPI’s fund represents an important opportunity for SMEs to have access to private equity capital. In the near future, this scheme is expected to be of substantial help in bridging the financing gap existing at this stage.

If and when an enterprise manages to reach the second expansion stage, then conditions for access to financing improve significantly. At this stage, banks are more willing to concede loans and the business becomes interesting for venture capitalists as well. However, due to the recent development of ICT/ICTE industry in Kenya, only a handful of enterprises have possibly reached this stage.
IV. CONCLUSIONS AND RECOMMENDATIONS

Introduction. The Kenya’s ICT/ICTE sector is small but rapidly growing. Many new businesses have mushroomed in recent years, fueled by liberalization and a renovated policy framework. However, most of the operations established thus far are very small and simple, and it is too early to decide if this is the initial phase of a fledging industry or just a wave of speculation destined to soon dry up. In Kenya, the financial sector situation is not particularly difficult compared with other Sub-Saharan countries: the overall system is liquid and stable, and banks’ credit to private sector is increasing. However, access to financing remains difficult for SMEs, because of risk-averse policies applied by most of commercial banks, and the heavy securitization required. The study demonstrates that ICT/ICTE enterprises are particularly affected by this financing gap, which emerges most often when enterprises seek financing in the US$50,000 to US$500,000 range. The problem is somewhat mitigated by the presence of various micro-finance schemes and other donor or government supported facilities dedicated to SMEs. The likely establishment of few more facilities of this kind is expected to further contribute toward bridging the gap.

In this section, some possible additional initiatives aimed at tackling the financing gap for ICT/ICTE enterprises are briefly displayed. These measures fall into two categories: (i) measures aimed at facilitating access to equity financing; and (ii) measures aimed at facilitating access to debt financing.

IV.1 MEASURES AIMED AT FACILITATING ACCESS TO EQUITY FINANCING

Venture capitalists are generally better equipped than banks to understand the viability of business ideas in innovative fields, and they have played a crucial role in the development of ICT/ICTE clusters in several countries. In Kenya, the contribution of institutional VCs to this sector is still marginal. Hence, some concrete measure should be envisaged to mobilize more resources to encourage the deployment of equity capital in this field. In particular, it could prove beneficial to concentrate efforts in two directions: (i) facilitating the allocation of existing and planned private equity capital to ICT/ICTE sector; and (ii) supporting the development of business angels.

Facilitate Equity Investments in ICT/ICTE. The Kenyan Government has recently placed strong emphasis on the ICT/ICTE industry, in particular on Call Centers and BPO, as a key driver of country’s economic development. While concrete measures in the field of regulatory and institutional framework are already in the pipeline, it is not clear if and how the public sector intends to assist enterprises through financial instruments. So far, ICDC has represented the State’s financial arm in the private sector. As such, ICDC has invested through equity and debt instruments in a number of enterprises of various sizes, but apparently no ICT/ICTE business has ever tapped from this facility. Possibly, assistance could be provided to create the conditions for increasing the flow of development capital from the public sector to the ICT/ICTE industry. Assistance could simply include technical advisory support, or combine expertise with funding through a ‘matching fund’-like model. To this end, it could be also worth exploring the possibility of teaming up with the prospective equity fund planned by EADB, which will be launched in 2007.
Support to Business Angels. Business Angels’ investments fit particularly with startups, as they represent the ideal link from a status of financial self-reliance to institutional equity operations typical of later stages. Angels do not provide clients with capital only, but also with expertise and useful contacts. In an emerging industry like Kenyan ICT/ICTE, the contribution of Angels could also have a cultural significance, such as instructing entrepreneurs on the fundamentals of equity financing and preparing the ground to larger VC operations. As discussed, IFC is presently involved in setting up a business angels group, but the ICT/ICTE sector appears marginally concerned. Efforts to promote angels’ investing in this sector could therefore serve the two-fold purpose of reducing ‘techno-preneurs’ dependence from bank financing and facilitating the creation of an enabling environment where genuine business ideas could nurture and grow. To this end, an active involvement of the business incubators and the ICT sector associations would prove beneficial.

IV.2 MEASURES AIMED AT FACILITATING ACCESS TO BANK FINANCING

Commercial banks dominate the Kenyan financial sector, and despite discouraging lending conditions and prohibitive financing costs, they still represent the main, and often, sole option available for SMEs. In order to reduce the financing gap, it is crucial to devise ways to facilitate the access to banks’ lending, in particular for software developers and IT services providers. Two possible areas of intervention can be identified: (i) support to the establishment of credit guarantee facilities, and (ii) assistance to ICT/ICTE promoters in dealing with commercial banks.

Assistance to the Establishment of Credit Guarantee Facilities: Credit guarantee schemes (CGS) aim at facilitating access to bank financing through the provision of a loan repayment guarantee that replaces to a variable extent the need for collateral. Several examples of facilities of this kind can be observed in various European countries, where they play an important role in helping SMEs to access credit. More recently, CGS are spreading in a number of emerging countries, from North Africa to East Asia and Pacific, sometimes with the support of donors and/or local governments. In Kenya, some cooperative banks and MFIs participate to a USAID’s credit guarantee facility, which provides partial coverage to loans extended to SMEs. This facility, though, operates exclusively in agribusiness, farming and related field. Apart from that, no other example of CGS is reported in the country. Therefore, an intervention in this area should initially focus on assessing the feasibility of a CGS open to ICT/ICTE SMEs and possibly providing technical assistance in the design of such a scheme.

Provision of Direct Assistance to ICT/ICTE Promoters. Evidence from the fieldwork indicates that problems in accessing loan financing cannot be blamed entirely upon banks. Small entrepreneurs are often unable or unwilling to prepare business plans of sound quality, and to discuss them in an effective way with bank officers. Provided that the Kenyan financial system is fairly stable and liquid and that the difficulties in obtaining loans are not imputable to ‘exogenous factors’, the entrepreneurs’ skills in dealing with financial affairs and presenting their projects to banks must be addressed. The existing business incubator and SME-dedicated facilities are strongly involved in this field and offer a range of advisory and technical services to their clients/incubatees. This is an important task, though the present outreach of these recently-established facilities is perhaps too small to serve the needs of a vast SMEs base. Therefore, further interventions in this field could prove particularly beneficial, especially if they are focused on ICT/ICTE entrepreneurs.
ANNEX A – THE ICT/ICTE SECTOR

A.1 TELECOMS

The telecom sub-sector includes one national fixed line operators, two mobile operators, and some specialized operators (such as VSAT and GMPCS operators). All these operators are subject to the issuance of licenses from the telecom regulators, the Communication Commission of Kenya (CCK). The telecom market has been formally liberalized in 1999. The former Kenya Post & Telecommunication Corporation was split into parts and the telecom sector was put under the rule of the newly established Telkom Kenya Ltd. (TKL). At the same time, TKL was granted 5 year of exclusivity in operating the land line national network, in order to restructure and prepare for privatization and full market liberalization. The monopoly terminated in June 2004, but a first attempt to issue a second license recently failed, and TKL remains de facto the only land line operator. In mid 2006 the CCK officially announced a new tender for the awarding of a multiple license for telephony. The license include fixed-line, mobile, international voice gateway, commercial VSAT and Internet backbone. The privatization of TKL is expected to take place in 2007 through the sale of almost 60% of State’s participation. The plan, announced by the Government in February 2006, was to sell 36% of its shares to the Nairobi Stock Exchange (NES), while another 24% to a single strategic investor. Before the sale of stocks begins an important company restructuring is expected, as TKL is presenting operating at losses. In particular, a significant reduction of personnel is anticipated, from the current 18,000, to 6,000.

At the local level, alternative operators in land line telephony are already emerging. In March 2005, TKL signed an interconnection agreement with Bell Western Telecommunication Ltd. (BWTL) enabling the latter to provide fixed-line connections in the north-east region of the county.

The mobile telephony market is dominated by two operators. The largest one—Safaricom—is publicly controlled through the 60% of shares held by the TKL, while the remaining 40% is owned by the British Vodafone. Government is currently arranging to sell another 9% to Vodafone, in order to raise the funds necessary to finance the social costs of TKL restructuring. The second GSM license is operated by Celtel Kenya who acquired it from Kencell Telecommunication in November 2004. Celtel Kenya is an affiliate of Celtel International—the leading pan-African mobile communication group that has been recently acquired by the Kuwaiti MTC. A third provider (Econet Wireless) has been licensed in 2004 but it has never started operations.

The salient features of main telecom operators are provided in Table 1 below.

The Kenyan mobile telephony market is growing at a very quick pace. The level of subscription rose from 2.2 million, in mid 2004, to nearly 6.5 million within two years, while the penetration rate has recently hit the 20% mark. In contrast, fixed telephony registered a slight downward trend in the number of subscribers, declining from 313,000 in 2000 to less than 300,000 in mid 2006, with a mere 0.9% rate of tele density. Pay phones, installed throughout the country amount to 8,900.

Since the liberalization in 1999, the telecommunication sector witnessed a proliferation of new entrants in the various sub-sector of the market, from public data network operators (PDNO), to value-added services providers (VAS), to local loop providers, whose clients recently topped 4,000. The Table 2 below summarizes the evolution of the market over the past six years.
restrictive environment inhibited the emergence of a real competitive market in Internet service provision because all operators had to purchase Internet access from the same monopoly, which at the same time sold its own services at lower prices.

In 2002, the Telecommunication Service Provider’s Association of Kenya (TESPOK) obtained a license to set up a domestic Internet Exchange Point (IXP). The establishment of a local IXP has been a turning point for Kenyan ISPs. This made it possible to significantly cut back on peering costs for internal traffic. Another milestone was the end of the monopoly on physical networks.

### TABLE 1. Main Telecom Operators

<table>
<thead>
<tr>
<th>Operator</th>
<th>Line of Business (subscribers)</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Telkom Kenya Ltd</td>
<td>Fixed telephony (some 287,000 subscribers in February 2006)</td>
<td>Telkom Kenya is currently 100% State-owned; a partial liberalization is expected by end 2006. It currently employs some 18,000 people that will likely be reduced to 6,000 after restructuring. The annual turnover is about US$290 millions.</td>
</tr>
<tr>
<td>Safaricom Ltd.</td>
<td>Mobile telephony (3.1m subscribers in February 2006)</td>
<td>TKL’s share in Safaricom is 60%, the remaining 40% is held by the British Vodafone. It has 600–700 employees. In 2005 Safaricom has generated a turnover of some US$355 millions.</td>
</tr>
<tr>
<td>Celtel Kenya Ltd.</td>
<td>Mobile telephony (some 2.6m subscribers in February 2006)</td>
<td>Celtel Kenya is a subsidiary of Celtel International (formerly known as MSI Cellular Investment), a mobile phone operator active in 15 African countries. Celtel Kenya employs some 600 staff and in 2005 posted a US$140 millions turnover.</td>
</tr>
</tbody>
</table>

### TABLE 2. The Telecommunication Sub-sector Composition

<table>
<thead>
<tr>
<th></th>
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<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Internet Service Providers</td>
<td>43</td>
<td>66</td>
<td>72</td>
<td>76</td>
<td>78</td>
<td>72</td>
</tr>
<tr>
<td>Internet Exchange Point Providers</td>
<td>—</td>
<td>—</td>
<td>1</td>
<td>2</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Paging Service Providers</td>
<td>12</td>
<td>16</td>
<td>12</td>
<td>12</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>Value Added Service Providers</td>
<td>—</td>
<td>1</td>
<td>1</td>
<td>3</td>
<td>17</td>
<td>24</td>
</tr>
<tr>
<td>Public Data Network Operators</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>4</td>
<td>6</td>
<td>14</td>
</tr>
<tr>
<td>Public Switched Network Operators</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Commercial VSAT Hub Operators</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>2</td>
<td>2</td>
<td>6</td>
</tr>
<tr>
<td>Regional Telecoms Operators</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>Internet backbone &amp; Gateway Operators</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>Local Loop Providers</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>2</td>
<td>4</td>
<td>13</td>
</tr>
<tr>
<td>Call centers</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>—</td>
<td>1</td>
<td>2</td>
</tr>
</tbody>
</table>

### A.2 INTERNET SERVICES

The total number of Internet hosts is above 13,000, nearly 5 times higher than in 2001. The estimated number of Kenyan Internet users is above 1.5 million, with a penetration rate of 4.63%. Internet users are concentrated in Nairobi and few other large cities, while the rest of the country is severely lagging behind. The penetration of the Internet into Kenya has been quite slow compared to other African countries. This is mainly due to the lack of infrastructure, the comparatively high prices charged, and an inadequate regulatory framework. Prior to 2004, TKL retained a monopoly on the Internet backbone and on the international gateway through its subsidiary Jambonet. This restrictive environment inhibited the emergence of a real competitive market in Internet service provision because all operators had to purchase Internet access from the same monopoly, which at the same time sold its own services at lower prices. In 2002, the Telecommunication Service Provider’s Association of Kenya (TESPOK) obtained a license to set up a domestic Internet Exchange Point (IXP). The establishment of a local IXP has been a turning point for Kenyan ISPs. This made it possible to significantly cut back on peering costs for internal traffic. Another milestone was the end of the monopoly on physical networks, and the

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10 Source: Communication Commission of Kenya (CCK). Figures include only licensed operators.
entrance of several private operators into the various segments. Two operators are currently laying down optical fiber cables along the main axis of the country, while projects for broadband international connectivity are in the pipelines\(^{11}\). This would help in the near future with the improvement of Internet connection and the lowering of bandwidth prices that are currently 20–30 times higher than the world average.

At present, there are 72 ISPs licensed, but only 16 of them are active: Africa Online, ISP Kenya, Jambo Telkom, Kenyavews, NairobiNet, Net two thousand / Bidii dot com, Postal Corporation of Kenya, Sahannet, Swift Global, Today’s Online, UUNet and Wananchi Online. The profitability of the Internet market is rapidly decreasing, and the sector is undergoing a process of consolidation and diversification. At the retail level, Internet access is provided by a vast network of cybercafés. The 90 licensed cybercafés represent only a small portion of a phenomenon that includes, to a large extent, informal economy operators. Although precise figures are not available, it is estimated that 500 cybercafés are active. These figures include about 200 E-touch centers that were set up by Africa Online, mostly in Nairobi. These are quasi-business centers offering the following integrated services: e-mail, Internet, fax, and telecommunication. Reportedly, the E-Touch centers are quite successful, although they are so expensive that only small number of Kenyans can afford their services.

### A.3 ICT/ICTE ACTIVITIES

Kenya is a regional hub for many IT industry world leaders, including HP, IBM, Microsoft, Oracle, SAP, Sybase, and Samsung. There are also a few medium-sized local IT firms, such as Symphony, Fintech Kenya, and ICL East Africa, which are mainly locally incorporated affiliates of larger international IT firms. The bulk of ICT enterprises are small companies with less than 10 employees. They are principally involved in IT assistance and maintenance, web designing, development of basic applications, and software “localization”.

**Sale and Installation of Hardware and Software** is probably the largest sub-sector, with an estimated 100–150 active players. Local assembly of PCs and peripherals is almost non-existing. This is partly due to the fact that until recently the import of computer parts was charged 15%, while the import of complete units was duty-exempt. Some small-scale computer assembly activity is performed within the Export Processing Zone (EPZ)\(^{12}\), but mainly destined to export. Three local universities co-ordinated by the Kenya College of Communication Technology (KCCT), are planning to spin-off a business project for the local assembling and trading of PCs. The four institutions have signed an agreement in early 2007, and have received a US$ 270,000 seed financing from CCK and Safaricom Foundation.

With a share of about 80%, the off-the-shelf packages predominate the business of software applications. However, major brands report of serious problems related to the wide-spreading of software piracy. In particular, Microsoft estimates that 70–80% of Kenyan PCs in Kenya are running pirated version of its operative systems. The Business Software Alliance estimated that illegal software business accounted in 2003 for some US$ 12.4 million.

**Software development** is a small but growing business. There are some 30–50 players active on the market, mainly developing applications for accounting and financial services, health care, and database management. Web-based businesses are also on the rise, with an increasing number of SMEs active in web-design, e-content development, e-commerce etc. Although limited in absolute terms, the penetration rate of open-source software in Kenya is non-negligible. Some 4–5% of users have opted for Linux and open applications, while the presence of IT firms specialized on this segment is reported. An enabling factor is likely represented by the presence in Nairobi of the secretariat of the Free and Open Source Software Foundation of Africa (FOSSFA).

A summary presentation of some selected ICT/ICTE firms is provided in Table 3 below.

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\(^{11}\) Reportedly, Telkom have agreed with Etisalat of Dubai on the construction of an undersea cable connecting the two countries. The value of the project is estimated at some US$100 million.
\(^{12}\) For more information, please refer to the EPZ’s website, www.epzkenya.com

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A. CALL CENTERS AND BPO SERVICES

The business of call centers is expanding in Africa as well. Wages and other costs are as competitive as in India or the Philippines, and the continent abounds with well-educated workforce who speaks English. At present, the telemarketing accounts for almost the totality of the activities outsourced to Africa, while more profitable businesses, such as customer care services, are still performed in countries with a longer tradition. In Anglophone Africa, the leading country is by far South Africa, where some 54,000 people are employed in the 500 existing call centers. But Kenya, along with Ghana, is considered by many as one of the most promising economies for this type of business, due to political stability, pro-western attitude, and the presence of a skilled workforce. As of today, the Kenyan call center industry is still in its infancy. The main reasons being on the one hand the lack of an adequate infrastructure and the related high costs of connectivity, on the other hand the inadequateness of the regulatory framework prevalent mid-2004, which inhibited an earlier growth. The first Kenyan call center—KenCall EPZ—started operating in November 2004. Subsequently, two other companies have been licensed by the CCK, but operations have not taken off yet.

The National ICT Strategy issued by the government of Kenya in January 2006, underline the key role of call centers and business process outsourcing services (BPO) to achieve the strategy’s goal of “making Kenya the ICT capital of Africa”. According to the plan, outsourcing can contribute to create some 30,000 jobs in the near future. The National ICT Strategy has been adopted by ICTPark, a consortium of local, regional, and global organizations working together for the development of ICT sector in Kenya. The consortium focuses on facilitating the development of BPO and call centers in Kenya by working in close relation with facility owners, business operators and outsourcing clients.

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**TABLE 3. Selected ICT / ICTE Companies**

<table>
<thead>
<tr>
<th>Company</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Kenya Data Networks</strong></td>
<td>Kenya Data Networks (KDN) is a member of Sameer Group. Licensed in 2003 as a Public Data Network Operator, KDN is among the largest and most innovative IT firms in Kenya. The company has inaugurated in March 2006 a fiber-optic connection between Mombasa and Nairobi and is currently planning to extend it to other major cities. KDN is also involved as private investors in international broadband connectivity projects.</td>
</tr>
<tr>
<td><strong>KenCall EPZ</strong></td>
<td>Established by a pool of U.S. IT firms with an investment of US$1.3 million. KenCall EPZ is a remote service and sales support provider. The company operates the first Kenyan call center with some 70 workstations with about 200 employees.</td>
</tr>
<tr>
<td>ICL East Africa</td>
<td>ICL East Africa is a leader in the provision of IT systems in the East African region. ICL is controlled by the South African-based company, Dimension Data. ICL’s clients include banks, telecoms, and local subsidiaries of large MNCs. It employs 60 staff.</td>
</tr>
<tr>
<td><strong>Wananchi Online Ltd</strong></td>
<td>Established in 2000, the company is the larger ISP of Kenya. Wananchi also provides a wide range of value-added services such as web-hosting, multimedia contents provision, instant messaging etc. Its clients include Chase Bank, Nairobi Stock exchange, and several governmental bodies.</td>
</tr>
<tr>
<td><strong>ISP Africa</strong></td>
<td>ISP Kenya started operating in 1999, and at present it is the second largest ISP and value-added service provider. Services offered include: domain registration, web hosting, and customized email services. The company has a staff of 30 employees. In 2005, it generated a turnover of US$ 1.5 million. Currently, ISP Kenya is in process of merging with another Kenyan leading Internet company—Wananchi Online, thus creating the largest Internet business of Kenya.</td>
</tr>
<tr>
<td><strong>Easy Surf</strong></td>
<td>Easy Surf manages a relatively large network of cyber café in Nairobi. The first facility was opened in 2001, and currently, Easy Surf operates four branches in different areas of the city. The company is planning to open new branches in other major cities of Kenya. Easy surf has a workforce of 13 employees and posts a turnover of US$ 130,000.</td>
</tr>
</tbody>
</table>
ANNEX B – THE INSTITUTIONAL SETTING

B.1 PUBLIC ENTITIES

Ministry of Information and Communication\textsuperscript{13}. The Ministry of Information and Communications (MIC) was created in July 2004. Previously, the competences on ICT sector where fragmented under several departments of various Ministries. The National Communication Secretariat, charged of advising the government on ICT matters, operates under the responsibilities of MIC. Another relevant body, recently instituted by the MIC, is the Permanent Secretary who is directly involved in the definition of a Master Plan for the realization of the National ICT Policy.

Communications Commission of Kenya\textsuperscript{14}. Established in February 1999 by the Kenya Communications Act, the Communications Commission of Kenya (CCK) is the body responsible for the regulation of telecommunications, radio communication, and postal services. Its mandate covers a broad range of activities, from issuing licenses to telecoms and postal/courier operators, to setting tariffs for monopoly areas, and to establish interconnection principles among operators to approve communications equipment. CCK is also responsible for the obligation deriving from the Universal Service for both postal and telecommunication services. Each year the CCK issue a report that outlines the statistics for the telecommunication sector. In particular, the annual report contains updated indicators of the accessibility trends, the price indexes, the market competitiveness and the measures adopted to support the growth of the sector.

B.2 PRIVATE ENTITIES

Telecommunications Service Providers Association of Kenya\textsuperscript{15}. The Telecommunications Service Providers Association of Kenya (TESPOK) was established in 1999, as an organization representing the interests of ISPs and other telecommunication service providers. Originally, the association had 25 members including ISPs and PDNOs. Presently, TESPOK is planning to enlarge membership to include other kind of operators. TESPOK is run by an elected Board of Directors, made up of representatives from member companies. TESPOK’s commitment was determinant to obtain the establishment of Kenya Internet Exchange Point. TESPOK has been also involved in important campaigns, such as the introduction of free competition in international gateway market, and participated to the design of the Kenya National ICT strategy. At present, the association is trying to be assigned the management of the Kenyan domain name “.ke”.

Kenya Private Sector Alliance\textsuperscript{16}. Established in 2003, as the umbrella body of the private sector, the Kenya Private Sector Alliance (KEPSA) is the largest business association in the country. KEPSA’s primary members are 25 sector federations and multi-sectoral organization who represents the various industries and categories of Kenyan economy, while associated members includes 150 enterprises and industry associations. KEPSA has three main activities: (i) implementing sector-wide programs, which are sponsored by the government and/or international donors; (ii) advising the Government on regulatory issues; and (iii) implementing capacity building programs for enterprises and business associations.

The Kenya ICT Federation\textsuperscript{17}. The Kenya ICT Federation (KIF) is the evolution of the ICT Board,

\textsuperscript{13} For more information, please refer to the MIC’s website www.information.go.ke
\textsuperscript{14} For more information, please refer to the CCK’s website www.cck.go.ke
\textsuperscript{15} For more information, please refer to the TESPOK’s website, www.tespok.co.ke
\textsuperscript{16} For more information, please refer to the KEPSA’s website, www.kepsa.or.ke
\textsuperscript{17} For more information, please refer to the KIF’s website, www.kif.or.ke
which was originally established within the *Kenya Private Sector Alliance* (KEPSA). KIF was established in April 2004, and it comprises several ICT organizations. These include the following:

- TESPOK (see above);
- The *Cyber café Owners Association of Kenya*;
- The *Kenya Information Society* (KIS);
- The *Kenya Network Information Centre*;
- The *E-Commerce Association of Kenya*;
- The *Office Equipment Association of Kenya*;
- The *Export Services Association of Kenya*;
- The *Institute of Electronic and Electrical Engineers* (IEEE);
- The *International Systems Audit Control Association* (ISACA);
- The *Information Technology Standards Association*.

KIF’s mission is to promote the growth of the ICT sector in Kenya, and as such, is particularly involved in the implementation of the National ICT Strategy. KIF has partnership with all the major stakeholders in the public and private sector and it operates in specific areas through dedicated committees.
**C.1 Banking and Related Activities**

**Commercial Banks:** Kenya’s banking system includes 42 commercial banks, with total assets of about US$8.0 billion18. Altogether, they operate 532 branches and local offices installed across the country. Bank credit to the private sector is around 29% of the country’s GDP. Lending interest rates usually range between 10% and 16%. The six largest institutions account for about 67% of all assets of the banking industry. Kenya’s two main banks, the *Barclay’s Bank* and the *Standard Chartered Bank*, are locally incorporated subsidiaries of large foreign financial institutions, with a minor participation of local shareholders. The State controls the other two prominent commercial banks, the *Kenya Commercial Bank Group* and the *National Bank of Kenya*, and holds ownership shares in the other two institutions. Other important players of the banking industry include the *NIC Bank*, the *Commercial Bank of Africa*, and the *K-Rep Ban.*. The latter is a small but very active institution involved in numerous microfinance and development initiatives for SMEs. A summary presentation of some selected main banks is provided in Table 4:

For more information, please refer to the central bank of Kenya website [www.centralbank.go.ke](http://www.centralbank.go.ke)

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**TABLE 4. Salient Features of Selected Main Banks**

<table>
<thead>
<tr>
<th>Bank</th>
<th>Total Assets (US$ Million)</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td><em>Barclay’s Bank</em></td>
<td>1275</td>
<td>Barclay’s Bank is one of the leading banks in Kenya. It is a locally incorporated foreign bank listed at the Nairobi Stock Exchange, and having some 34,000 shareholders. The bank is among the leaders in the retail segment of the market and in corporate banking. Barclay pioneered the concept of unsecured retail lending in Kenya where it currently holds a market share of 30%</td>
</tr>
<tr>
<td><em>Kenya Commercial Bank Group</em></td>
<td>977</td>
<td>The Kenya Commercial Bank Group is the largest State-controlled financial institution of Kenya. KCB operates the largest network of outlets in the country, accounting alone for the 55% of the existing facilities. The Bank offers a wide set of services ranging from guarantees to bill discounting and stock financing facilities. KCB owns a subsidiary in Tanzania.</td>
</tr>
<tr>
<td><em>National Bank of Kenya</em></td>
<td>404</td>
<td>The National Bank Of Kenya Ltd (NBK) was incorporated in 1968. The current shareholding composition stands as follows: National Social Security Fund (NSSF) 48.06%, Kenya Government 22.5%, General Public 29.44%. NBK only recently recovered its leading role after the financial crisis of 1998.</td>
</tr>
<tr>
<td><em>NIC Bank</em></td>
<td>272</td>
<td>NIC Bank—formerly known as National Industrial Credit Bank Limited—is the Kenya’s 5th largest bank. In November 1997, it merged with African Mercantile Bank Ltd (AMBANK). NIC Bank is listed at the Nairobi Stock Exchange and has some 20,000 shareholders.</td>
</tr>
<tr>
<td><em>Commercial Bank of Africa</em></td>
<td>267</td>
<td>The Commercial Bank of Africa is a corporate-oriented bank. CBA offers a wide range of lending, credit and trade finance products covering short term and long term financing needs. CBA commenced business as a subsidiary of a multinational financial society controlled for some times by the Bank of America (BoA). In late 80s the BoA sold all its shares on local market and since then CBA is fully owned by Kenyan private investors.</td>
</tr>
<tr>
<td><em>K-Rep Bank</em></td>
<td>33</td>
<td>K-Rep Bank is a development bank that specializes in microfinance to MSME. It also offers a wide range of banking services. It was established in 1999 by K-Rep Group limited, which is a microfinance development agency. Among the bank’s shareholders there are international organizations such as IFC (16.7%) and the African Development Bank (15.1%).</td>
</tr>
</tbody>
</table>
Leasing and Factoring: Leasing is not a new concept in Kenya. Although there is no statute specifically governing this instrument, the leasing is recognized and regulated by provisions contained in various Acts, such as the VAT Act, the Tax Act. Recently, the issuing of new leasing rules by the Minister of Finance (2002) has improved its attractiveness both to lessors and lessees and the number of transactions has risen. The encouraging new framework has also stimulated some institutions to design new leasing schemes. Factoring is a common but unstructured practice in Kenya. Some financial institutions are reportedly offering financial instruments of this type, but mainly on a case-by-case basis. On the demand side, the SMEs appear to have a weak knowledge of this instrument, and this is likely the major obstacle to the emerging of dedicated schemes.

Credit Guarantees: The only example of credit guarantees in Kenya is the USAID’s supported DCA scheme. This is a facility that provides accredited financial institutions with a 50% risk coverage on loans extended to qualifying borrowers. The local financial partners are cooperative banks and MFIs. The sectors targeted are mainly farming and agribusiness processes. The facility has a capital endowment of US$3.0 million.

C.2 VENTURE CAPITAL

Overview: Kenya’s equity financing industry is not very developed. The first and most famous equity financing scheme, Acacia, was launched in 1996 by Kenya Capital Partners. The Acacia Fund, whose initial capital was US$20 million, operated throughout the whole East African region but was particularly focused on Kenya and Tanzania. In 2003, Aureos Capital follows up on this experience launching the Aureos East Africa Fund (AEAF). The Fund has a capital provision of US$40 million, and the same Acacia’s management. More recently a couple of new players joined in. The first is East Africa Capital Partner, a financing scheme set up by a well-known Kenyan ICT entrepreneur. Established in August 2005, EACP is currently finalizing its first investment. The last institution to enter the Kenyan market is Business Partners International (BPI), a concern of the South African Business Partners equity firm. BPI set up at the beginning of 2006 a risk capital fund in the framework of the IFC’s project denominated SME Solution Center (see box 1 below).

Equity financing is also provided by a public-sector body—the Industrial and Commercial Development Corporation (see section C.3 below). A new venture capital fund is also in the pipeline at the initiative of the East Africa Development Bank—a development institution whose shareholders include the regional governments, some IFIs, and to a lesser extent, some private commercial banks. The prospective fund aims at financing SMEs from Kenya, Uganda and Tanzania, with transactions of about US$100,000 to 1.0 million.

A summary description of the existing Kenyan equity financing operators is provided in Table 5:

BOX 1. The SME Solution Center

The Kenya SME Solutions Centers (SSC) is a three-year pilot project implemented by IFC as a part of its Africa strategy. The facility is addressed to formally registered SMEs (with 5 to 100 employees and an annual turnover between US$80,000 and 1.3M), whose amount is estimated around 22,000.

The SSC assistance to SME is based on four pillars:

i. Access to finance, with the establishment in partnership with BPI of a Risk Capital Fund providing loans, equity and quasi-equity financing for innovative SMEs seeking for US$50,000 to 500,000;

ii. Capacity building programs and technical assistance services;

iii. Access to market information, through a fully fledged information center, an agreement is in the pipeline with Microsoft to create a dedicated portal for SMEs;

iv. An enabling business environment—collaborating with various stakeholders and with regulatory authorities to improve the business environment for SMEs.

The SSC houses also the Kenya Kountry Business Incubator (KeKoBI). Launched in 2005, the KeKoBI is currently incubating four ICT enterprises. KeKoBI has been sponsored by the infoDev Program, and cooperates with various local institutions including the JKUAT University, KEPSA, the Ministry of Trade and Industry and the Ministry of Information and Communications.
Salient Features. The salient features of Kenya’s private equity industry can be summarized as follows:

- **Origin of Funds**: The Kenyan private equity industry is almost completely dependent upon funds provided by international investors, and in particular by international financial institutions, such as the IFC and EIB. Kenyan private investors are, to a minor extent, involved in Aureos East Africa Fund. State equity investments are mainly channeled through ICDC;

- **Investment Policy**: The existing private equity firms have different investment policies, especially with reference to the size of deals targeted. BPI is expected to cover the lower end of the spectrum, with transactions between US$70,000 and 700,000, while AEAFF addresses operations in the US$500,000 to US$4 million range. EACP does not appear to have a specific target, but it appears oriented toward much larger operations;

- **Operating Modalities**: The financing instruments proposed by the surveyed equity schemes typically include equity, quasi equity and debt financing. Interest rates on straight loan are aligned with the rates offered by commercial banks. Investees are normally charged a transaction fee typically ranging from 2% to 3% of the investment, in order to cover the investment appraisal and the management costs.

- **Performance**: It is too early to assess the performances of the various funds. In fact, AEAFF has closed only two deals, while BPI and EACP have no investment yet in their portfolio. The earlier experience of the Acacia Fund was largely positive: in about 10 years of activity, the fund earned from 18 out of the 20 transactions made.

### TABLE 5. Kenyan Equity Financing Operators

<table>
<thead>
<tr>
<th>Fund</th>
<th>Funding (US$ mn)</th>
<th>Deals</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aureos East Africa Fund</td>
<td>40</td>
<td>2</td>
<td>Established in 2003 by Aureos Capital—a joint venture of CDC Capital Partners and the Norwegian Investment Fund for Developing Countries (Norfund)—Aureos East Africa Fund (AEAF) provides finance for expansion, acquisitions and management buy-outs. AEAF typically targets investment whose size range from US$0.5 to US$4 million, without sector preferences. Apart from CDC and Norfund, AEAF’s investors comprise also the European Investment Bank, the Swiss State Secretariat for Economic Affairs (SECO), International Finance Corporation (IFC), Netherlands Development Finance Company and local investors such as PTA Bank and Trans-Century Ltd.</td>
</tr>
<tr>
<td>Business Partners International</td>
<td>15</td>
<td>n.a.</td>
<td>Established in Kenya in 2006, Business Partner International (BPI) is a subsidiary of the South-African Business Partners—a public/private financial institution, providing equity, quasi equity and debt financing to SMEs. BPI plans to invest some US$1.5 million in Kenyan innovative small businesses (i.e. with a turnover below US$1.5 million per year), active in almost all sectors of the economy. The foreseen size of transactions will range from US$70,000 to 700,000.</td>
</tr>
<tr>
<td>East Africa Capital Partner</td>
<td>n.a.</td>
<td>n.a.</td>
<td>East Africa Capital Partner (EACP) is a private equity firm focused on media, technology and telecommunications. Established in 2005, EACP operates raising the investment capital on a case-by-case basis. EACP is currently closing its first deals.</td>
</tr>
</tbody>
</table>

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C.3 OTHER FINANCING SCHEMES

**Industrial & Commercial Development Corporation**

The Industrial and Commercial Development Corporation (ICDC) is the investment arm of the Kenyan Ministry of Finance. ICDC is the largest public financial institution and it provides financial product to the private sector, such as corporate financing, equity investments, loans, and technical assistance. ICDC control 25% of the ICDC Investment Company (ICDCI), an investment...
firms listed at the Nairobi Stock Exchange. Since its establishment in 1967, ICDC invested directly or through ICDCI, in more than 100 companies. Its equity portfolio includes some of the most important Kenyan companies including banks, insurance companies, trade corporations, etc. ICDC is also a key facilitator for SME development, having assisted some 15,000 enterprises in virtually all sectors with an overall financing of approximately US$26 million. ICDC’s equity scheme for SME targets deals with value ranging from US$150,000 to 650,000, and on a 3 to 6 years terms. Industrial loans for SMEs may vary from as little as US$2,500 up to 650,000 while in the case of commercial entities the maximum amount that can be borrowed is about US$50,000.

Micro-finance Institutions Kenya’s micro-finance sector encompasses an articulated and growing set of institutions of different typology. Outside the major cities/towns there are about 4000 Saving and Credit Co-operative Societies (SACCO) providing credit for agriculture mainly, but also to other types of SMEs. In addition, there are about 130 registered micro-finance institutions active in the supply of start-up capital and other financing facilities for SMEs. Several MFIs are members of the Association of Micro-finance institutions (AMFI), which was established in 1999 with the aim of mobilizing resources from the local financial market and donors, and lobbying the government for the improvement of the legal framework for micro finance. Altogether, the MFIs grouped under AMFI serve 100,000 clients country-wide20. In order to provide the micro finance sector with an appropriate legal framework the government has issued in 2006 the Micro-finance Bill.

The Youth Enterprise Development Fund. Established at end 2006, the Youth Enterprise Development Fund (YEDF) is a financing scheme launched by the Ministry of Finance to facilitate access to credit for entrepreneurs under the age of 35. The fund will provide loans at an interest rate below the market average, and money will be channeled through various accredited banks, which will be also responsible for the evaluation of the project proposed and the risk assessment. The YEDF is expected to be operational by early 2007.

20 On Kenyan microfinance industry, see also: George Omino, Regulation and Supervision of Microfinance Institutions, March 2005.
ANNEX D – LIST OF ENTITIES INTERVIEWED

A.1 PUBLIC ENTITIES

Ministry of Information and Communication
- Dr. Bitange Ndemo, Permanent Secretary

Communications Commission of Kenya
- Eng. John N. Waweru, Director General

Ministry of Trade and Industry
- Ms. Margareth C. Rotich, Director of Industries

A.2 PRIVATE ENTITIES, BUSINESS ASSOCIATIONS AND INTERNATIONAL ORGANIZATIONS

SME Solution Center
- Mr. Kiragu Maina, Program Manager
- Mr. Anthony N. Gichini, Business Development Officer

Kenya Private Sector Alliance
- Mr. Samuel M. Waweru, Chief Executive Officer

Kenya Kountry Business Incubator – KeKoBI
- Ms. Atieno Ndede-Amadi, Director

International Finance Corporation
- Nthenya R. Mule, Grassroots Business Initiative

A.3 FINANCIAL INSTITUTIONS

Aureos East Africa Fund
- Mr. Davinder Sikand, Managing Partner
- Mr. Shakir Merali, Partner

Business Partners
- Ms. Sally Gitonga, Chief Investment Officer

East Africa Capital Partners
- Mr. Richard Bell, Managing Director

Kenya Commercial Bank
- Mr. Christopher Migunde, Project Manager

Commercial Bank of Africa
- Mr. Peter M. Kiguru, Assistant General Manager – Corporate Banking
- Ms. Mercy M. Mutua, Manager – Corporate Finance

K-Rep Bank
- Mr. Antone Wambura, Advances Manager
- Mr. Stanley Munyao, Advances Officer

A.4 ICT/ICTE ENTERPRISES

Emart Business Solutions
- Mr. Zack Njunguna, Managing Director
- Mr. Robert Wachira, Director

Spreading Wings
- Mr. Frank Kamau, Director

Rivotek Kenya
- Mr. Patrick Opioyo, Managing Director

Kenya Swahili Institute
- Mr. Nuhu Bahari, Director

ISP Kenya
- Mr. Imran Chaudhrey, Deputy Director

Easy Surf
- Mr. Mburu L. Ndungiu, Branch Director

JKUAT Enterprises
- Prof. H. M. Thairu, Managing Director
Annex E – Profiles of SME Financing Organizations

Profile #1. Aureos West Africa Fund

Salient Features

<table>
<thead>
<tr>
<th>Denomination</th>
<th>Aureos East Africa Fund – AEAF</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nature</td>
<td>AEAF is a generalist private equity fund, focusing on small and medium sized companies. The fund is managed by Aureos Kenya Managers Ltd.</td>
</tr>
<tr>
<td>Location</td>
<td>AEAF’s headquarters is in Nairobi, Kenya, with a local office in Tanzania.</td>
</tr>
<tr>
<td>Geographical Coverage</td>
<td>AEAF operates throughout East Africa region, with particular emphasis on Kenya.</td>
</tr>
<tr>
<td>Establishment</td>
<td>AEAF was established in 2003, following up on the experience of the earlier US$ 20 million Acacia Fund. AEAF is managed by the same team as Acacia’s</td>
</tr>
<tr>
<td>Funding</td>
<td>AEAF’s investors are a group of national and international financial institutions including CDC Capital Partners, the Norwegian Investment Fund for Developing Countries (Norfund), European Investment Bank, the Swiss State Secretariat for Economic Affairs (SECO), International Finance Corporation (IFC), Netherlands Development Finance Company (FMO), and local investors such as PTA Bank and Trans-Century Ltd. The overall capital provision amount to US$ 40 million.</td>
</tr>
<tr>
<td>Investment Policy</td>
<td>AEAF is not oriented to any specific sector. Their preferences are directed to established firms with a solid track record, while start ups and companies at early stages of development are generally not considered. AEAF is characterized by taking active part in the management of the invested companies.</td>
</tr>
<tr>
<td>Operations</td>
<td>AEAF targets investments ranging from US$ 0.5 to 4 millions, combining straight equity instruments with quasi-equity and debt schemes. As a general rule, no more than 15% of the overall capital of the Fund may be invested in one single deal. The maximum duration of AEAF’s investment is five years, but the average is in the order of three years. A management fee of 3% of the amount invested is also applied.</td>
</tr>
</tbody>
</table>

Narrative Description

Aureos Capital was established in 2001 as a joint venture of CDC Capital Partners (“CDC”) and the Norwegian Investment Fund for Developing Countries (Norfund). The first regional fund created by Aureos was the Aureos Central America Fund, who achieved its first closing in 2002. Afterwards, three private equity funds with similar structure have been established in Sub-Saharan Africa, namely the Aureos South Africa Fund, the Aureos East Africa Fund, and the Aureos West Africa Fund. The three funds have the same capital endowment—US$40 million—and similar investment policies.

To date, the AEAF has invested some US$ 5–6 millions in two companies: a packaging manufacturer, and a pharmaceutical company. For the moment, AEAF appears not particularly interested to invest in ICT/ICTE sector.

According to AEAF managers, the Kenyan ICT market is today distorted by various speculative operations and it is hard to identify genuine entrepreneurs with a real potential. Moreover, Kenyan ICT is still in its infancy: hardware manufacturing is almost nonexistent, the software activities are simple customization of existing packages, internet services are undergoing a critical period and outsourcing is still a marginal business. Under these circumstances venturing in ICT today does not offer attractive premiums.

Other Sources

- www.aureos.com
### Profile #2. Business Partners International – Kenya

<table>
<thead>
<tr>
<th><strong>Salient Features</strong></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Denomination</strong></td>
<td>Business Partners International (BPI)</td>
</tr>
<tr>
<td><strong>Nature</strong></td>
<td>BPI is an initiative of the South African private equity firm Business Partners Ltd.</td>
</tr>
<tr>
<td><strong>Location</strong></td>
<td>BPI Kenya is hosted in the IFC’s supported SME Solution Center, in Nairobi</td>
</tr>
<tr>
<td><strong>Geographical Coverage</strong></td>
<td>The BPI is a national scheme covering all Kenya.</td>
</tr>
<tr>
<td><strong>Establishment</strong></td>
<td>BPI Kenya was established in January 2006.</td>
</tr>
<tr>
<td><strong>Funding</strong></td>
<td>BPI Kenya has an initial funding of US$1.5 million.</td>
</tr>
<tr>
<td><strong>Investment Policy</strong></td>
<td>BPI Kenya will invest in small and medium enterprises with a turnover below US$1.5 million per year, active in almost all sectors of the economy. The foreseen size of investments is from US$50,000 to 500,000. Financing instruments include straight equity, quasi-equity and debt at rates aligned to the local market (around 15%). The duration of investments may vary from 3 to 5 years.</td>
</tr>
<tr>
<td><strong>Operations</strong></td>
<td>No operations have been reported yet.</td>
</tr>
</tbody>
</table>

**Narrative Description**

- Based in Johannesburg, Business Partners Ltd is a public–private financial institution, co-owned by Khula Enterprise Finance (controlled by the Department of Trade and Industry), some financial institutions (Nedcor, Sanlam, and others) and several private groups. Business Partners provides equity, quasi equity and debt financing to South African SME. In 2005 the company approved some 550 deals, accounting altogether for some US$100 million, being some US$200,000 each, on average. Financing typically goes along with technical assistance to invested companies.
- BPI Kenya is hosted in the SME Solution Center that is an IFC-sponsored facility aimed at supporting the growth of SME in Kenya, through the provision of a variety of services, including: (i) technical assistance; (ii) mentoring, and (iii) financial support. A similar pilot scheme was launched in Madagascar in 2004.
- BPI targets start-ups as well as existing companies who wish to expand their business. Although the scheme is addressed to enterprises in almost all sectors, a particular inclination toward innovative businesses is reported.

**Other Sources**

- [www.businesspartners.co.za](http://www.businesspartners.co.za)
## Profile #3  East Africa Capital Partner

### Salient Features

<table>
<thead>
<tr>
<th>Denomination</th>
<th>East Africa Capital Partner (EACP)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nature</td>
<td>EACP is a private equity firm focused on media, technology and telecommunications.</td>
</tr>
<tr>
<td>Location</td>
<td>EACP is based in Nairobi.</td>
</tr>
<tr>
<td>Geographical Coverage</td>
<td>EACP is active in East Africa countries with particular emphasis on Kenya.</td>
</tr>
<tr>
<td>Establishment</td>
<td>EACP was established in 2005.</td>
</tr>
<tr>
<td>Funding</td>
<td>EACP does not operate a fund with a determined endowment, but it raises investment capital on a case-by-case basis. Main investors are foreign financial institutions.</td>
</tr>
<tr>
<td>Investment Policy</td>
<td>EACP is a scheme specifically addressed to telecommunication, media and technology. The initial idea was to target operations ranging from US$100,000 to 2 million, but it proved difficult to find investors interested in such small deals, therefore, EACP is today focusing much more sizable investment. EACP applies to its investees a management fee of 2% of total amount.</td>
</tr>
<tr>
<td>Operations</td>
<td>EACP is currently on the way to close its first deal.</td>
</tr>
</tbody>
</table>

### Narrative Description

- EACP is the only private equity firm in Kenya specifically targeting ICT and media sector. This is due to the fact that the managing partner is a former ICT entrepreneur with a profound knowledge of the sector, with specific references to Internet services, and broadband infrastructures.
- Through its manager, EACP is also linked to several industry organizations such as: the Telecommunications Service Providers Associations of Kenya (TESPOK), the Kenya Internet Exchange Point (KIXP), the Kenya Network Information Center (Kenic).
ANNEX F – PROFILES OF ICT/ICTE SME

SPREADING WINGS LIMITED

Operations
Spreading Wings Ltd was incorporated in 1999 as a partnership, and in 2006 became a limited company with a share capital of KES 1 million (approx. US$13,000). Spreading Wings is an enterprise active in the development and implementation of computer software solutions.

The company is hosted within the KeKoBI Business Incubator since its establishment in September 2005. The company is organized in four functional divisions, sales & marketing, production, support and administration, and managed by a board of directors whose members are the respective heads of the divisions. It is active throughout the East Africa region working for both public and private sector entities.

At present, the company is trading two main types of products: (i) insurance brokerage applications; and (ii) financial and accounting software solutions. Another important line of business is the ICT consultancy. As for the future, Spreading Wings envisage to expand their activities to include software solutions for: (i) customer service and support systems; and (ii) database management systems.

Financing
Spreading Wings is currently servicing a loan granted by a commercial bank. The amount borrowed is of about US$60,000, repayable in three years. The procedure to obtain this loan was reportedly quite long and tough, as the company’s financial accounts was accurately monitored by the bank for more than half a year. The amount borrowed was invested in the development of new products, in the purchase of equipments and in the acquisition of patent licenses.

The company’s manager affirms that Spreading Wings is currently ready to take another expansion, but the current cost of financing is discouraging. Seeking for private equity financing has not been taken into consideration so far.

Other
The assistance received from the incubator’s experts has been fundamental to design the company’s structure as it is today, and to upgrade management’s entrepreneurial skills. Other benefits derive from having access to the incubator facilities at a subsidized cost. In addition to that, the director also believes that being located within KeKoBI improves the image of their business vis-à-vis their clients.

ISP KENYA

Operations
ISP Kenya is one of the leading Kenya’s ISP. Established in 1999, ISP Kenya has today 30–35 employees and in 2005 posted a turnover of US$ 1.5M. The company specializes on services for corporate clients, combining straight Internet access (both through land line and satellite) and other value-added services such as domain registration, web hosting, other premium services.

Currently, ISP Kenya is in process of merging with another Kenyan leading Internet company—Wananchi Online, which is more focused on household clients. The merger will create the largest Internet company of Kenya by number of clients.

Financing
The start-up of ISP Kenya was financed with personal resources of the owners. Later on, the company borrowed from commercial banks to
finance its first expansion plan. At present, a further scaling up is in the pipeline, as a consequence of the merger with Wananchi Online. The operation will entail the injection of fresh capital that is expected to be raised through a public sale of stocks through the Nairobi Stock Exchange.

**Other**
The merger of ISP Kenya and Wananchi Online is an example of the consolidation process occurring in the Kenyan Internet market. After an initial boom, in the aftermath of the liberalization, the ISP sector has quickly reached a saturation point and the trend has drastically changed. Price levels are still very high, partly due to the monopoly still insisting on the international up-link gateway. As a consequence, the market growth is very weak and only large ISPs, which have the capacity to offer a wide range of value-added services operate profitably, while most of small ISPs strive to survive.

ISP Kenya has been among the founding members of the Telecommunication Service Providers Association of Kenya (TESPOK)—the ISPs industry association. TESPOK was founded with the aim of promoting the liberalization of telecoms, and stimulating the government to invest in the development of ICT infrastructures.

KENYA SWAHLILI INSTITUTE LTD.

**Operations**
The Kenya Swahili Institute Ltd. (KKI) is operating in the niche sector of translations from and to Swahili language. KKI’s activities include: (i) translations of contents for media and broadcasting; (ii) the set up and administration of web sites in Swahili; and (iii) software localization activities. KKI provides its services to MNCs (e.g. Microsoft), the Kenyan Government, and various media companies. The company has been founded by a team of four Swahili experts coming from the media sector and with an academic background. KKI employs on average a dozen translators and ICT experts.

**Financing**
KKI is a ‘bootstrapping’ business, and its activities are entirely financed with company’s revenue. In this sense, KKI’s managers have never applied for any loan or other financing instruments and have no intention to borrow in the near future. It must be said that activities do not require sizeable investment as mostly based on ‘intellectual’ capital.

In particular, the contract with Microsoft for ‘localization’ services ensures to KKI an adequate cash flow. As regards to the future, KKI’s director recognizes that the potential of their business is not currently exploited at its maximum. The Swahili speakers represent some 100 million based in six different countries, while KKI is presently active only in Kenya and to a lesser extent in Tanzania and Uganda.

**Other**
The KKI’s director is a Swahili radio and TV presenter and writer. In his opinion, the Kenyan ICT environment has improved significantly over the past few years, both in terms of policies and infrastructures. Additional efforts from the Government are however urgent, in order to expand connectivity in rural areas where the Swahili is broadly spoken. Furthermore, in a region particularly affected by the digital divide and with a high rate of illiteracy it is crucial to offer ICT instruments translated into a familiar language, otherwise it would be very difficult to enhance the use of computer.

RIVOTEK KENYA

**Operations**
Rivotek Kenya is a software development firm affiliated to a U.S.-based parent company whose core business is creating various IT solutions for real-time communications. The applications and products are designed to run on mobile devices such as Pocket PC, Palm OS and Blackberry. Rivotek Kenya creates customized versions of these applications and products for the local markets. Other products developed by Rivotek Kenya include: pharmacy management system, software for education institutes, human resources system and the software localization is far more complex than simple translation, it means making technology accessible across languages and cultures. The software localization expert works in team with software developers in order to make the final product full compatible with specific cultural frameworks and attitudes. The importance of software localization is largely recognized by major software developers operating worldwide.
payroll application. The company also offers localization services in partnership with the Kenya Swahili Institute (see above) providing translations of websites and e-marketing materials. The Rivotek Kenya's client portfolio includes various IT firms, factory automation companies, health institutions.

**Financing**
The establishment of Rivotek Kenya has been financed with internal resources. The management did not even try to obtain start up capital from banks or other financial institutions because of the discouraging conditions prevailing. As of today, Rivotek Kenya manages to cope with its financial needs thanks to some substantial contracts which yield a sufficient cash-flow. Though, plans are to raise some US$30,000–50,000 in the near future for the acquisition of patent licenses and to set up a venue for product demonstration.

**Other**
The Managing Director of Rivotek Kenya is a former Microsoft East Africa project manager, and as such he was directly involved in the process of ‘localization’ of Microsoft’s operative system in Swahili. According to him, a big constraint for the development of ICT/ICTE small enterprises is the lack of regulatory provisions to entrust a fixed share of public procurement in ICT to domestic SMEs.

### EMART BUSINESS SOLUTIONS

#### Operations
The company was established in September 2005 and is still in process of incorporating as a limited liability company. Emart Business Solutions (EBS) is mainly active in Web designing, production of e-content, and software development. The company is also the initiator of an innovative portal for e-commerce. EBS currently employs 5 people and is hosted within the KeKoBI incubator. As a subcontractor, EBS is currently involved in setting up the Internet portal for the Ministry of Water and Irrigation. According to the managing director, the EBS’s core business in the near future will deal with e-commerce, as the company is currently engaged in creating the first portal of this kind entirely dedicated to domestic clients.

#### Financing
So far, EBS has not received any external support. In this line of business the financing needs are however quite limited and compatible with personal savings and other informal sources. Recently, they approached a commercial bank to apply for a Ksh 5 million loan (approx. US$65,000). The money was needed to strengthen marketing activities, to conduct further research and development, and to hire new personnel. The bank’s requirements were too stringent and eventually EBS decided to drop the idea. The managers also explored the possibility of entering a lease agreement for the purchase of some equipment, but again it failed as PCs and similar goods are excluded from leasing due to their rapid devaluation. EBS is therefore facing significant difficulties due to the obstacles in accessing financing, as the managers are concerned that this could severely damage the future development of the enterprise.

**Other**
EBS’s director claims to be satisfied of the services offered by the KeKoBI incubator: the rental fee is affordable and sharing the facilities with other enterprises significantly reduces the fixed costs.

### EASY SURF

#### Operations
Easy Surf manages a relatively large network of cyber cafés in Nairobi. The first facility was opened in 2001, and three more branches were opened since then. At present, Easy Surf employs some 13 staff and generates an annual turnover of Ksh 10M. (about US$130,000). The company is 100% owned by Kenyans most of them being very young. In the near future, Easy Surf will open new facilities in Mombasa and other major cities. In addition to that, the company will also diversify its services. In particular, plans are to rent fully equipped and connected office-space to entrepreneurs.

#### Financing
The establishment of the company has been primarily financed through a bank loan of about Ksh 5–6 million (US$70,000–80,000). The loan was extended to the company’s owner who had to 22 The envisaged business model is similar to the one adopted by ‘E-Touch’ centers, as discussed in Annex A.
provide personal properties as a collateral. While access to mainstream sources of financing is reportedly not considered as a severe obstacle, the cost of financing is seen as much too high. For this reason, the company’s management prefers to finance the expansion of activities through the revenue rather than through bank loans or other external sources.

Others

The competition in the cybercafés sector is fierce. Some 200 cybercafés are reported to be active only in Nairobi. The level of prices is quite high, due to the charges imposed by the ISPs, that are among the highest of Africa. According to Easy Surf’s managers the situation could radically change if an industry association grouping the various cyber cafés operators was established. Such an association in fact could manage to negotiate with ISPs better conditions, and this would reflect also in a lowering of prices to customers.
ANNEX G – SELECTED SOURCES

- Communications Commission of Kenya, Annual Report 2005–06
- Export Processing Zones Authority, Kenya’s Information and Communications Technology Sector, 2005
- The International Development Research Center, At the Crossroads: ICT Policymaking in East Africa, 2005
- Ministry of Information and Communications, National Information and Communications technology (ICT) Policy, January 2006
- Spitrack AB, ICT diagnostic study – Kenya, Oct 2004
About infoDev

infoDev is a partnership of international development agencies, coordinated and served by an expert Secretariat housed at the World Bank, one of its key donors and founders. It acts as a neutral convener of dialogue, and as a coordinator of joint action among bilateral and multilateral donors—supporting global sharing of information on ICT for development (ICT4D), and helping to reduce duplication of efforts and investments. infoDev also forms partnerships with public and private-sector organizations who are innovators in the field of ICT4D.

infoDev’s mandate is to help maximize the impact of ICTs in global efforts to achieve the internationally-supported Millennium Development Goals. These include improving education and health services, making public institutions more efficient and transparent, supporting rural livelihoods, and contributing to economic growth by supporting small and medium-sized enterprises that use ICT for their business.

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