

**PROPERTY RIGHTS, REGULATORY RISK
AND PRIVATE INVESTMENT
IN KENYA'S TELECOMMUNICATIONS SECTOR**

A THESIS

SUBMITTED TO THE

STANFORD PROGRAM IN INTERNATIONAL LEGAL STUDIES

AT THE STANFORD LAW SCHOOL

STANFORD UNIVERSITY

IN PARTIAL FULFILMENT OF THE REQUIREMENTS

FOR THE DEGREE OF JURIDICAL SCIENCES MASTER

BY

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MAY 2000

ABSTRACT

Many countries have instituted regulatory reform programs, seeking to stimulate private investment in their public telecommunications network. Effective regulation encompasses two components: the formal regulatory incentives and the regulatory governance structure. Although the regulatory governance – the institutional endowment underlying the regulatory scheme – determines the impact of the incentive, it is often overlooked in regulatory design initiatives.

The potential impact of the regulatory governance structure is examined through a case study of the reform program currently underway in Kenya's telecommunications sector. For more than a century, that sector has operated under public control and in the shadow of an administrative process that was corrupted in colonial times and offered fresh opportunities for distortion under post-independence governments. Furthermore, the sector continues to operate in the same predatory arena of distributive politics that contributed substantially to its decline.

The performance of Kenya's telecommunications sector continues to be constrained by its history and, although the formal structure has changed, the institutional underpinnings of the sector – the regulatory governance structure – remain largely unaltered. This legacy dilutes the security of property rights and creates scope for administrative expropriation in several ways. The government and regulator can change the regulatory scheme easily and are not effectively restrained from violating contractual commitments to private parties. In addition, local mechanisms enforcing restraints on the regulator and government are weak or non-existent. Property rights in Kenya, therefore, remain uncertain, forcing investors to adopt strategies to manage, deflect or re-allocate the regulatory risk posed by Kenya's weak domestic institutions. While these strategies are useful, most of them have costs that render them sub-optimal if the sector is to be efficient in the long term.

To consolidate the gains made in the reform efforts so far, attention should now be paid to strengthening the regulatory governance structure that supports the definition and enforcement of property rights. Evidence from other countries shows that, unless this is done, privatization programs will not stimulate an optimal level of the telecommunications investment that is so badly needed for Kenya's economic growth.

PREFACE AND ACKNOWLEDGEMENTS

To gain an understanding of institutional evolution and regulatory design in the Kenyan telecommunications sector, I have drawn repeatedly on the analytical framework and supporting evidence developed by Brian Levy, Pablo Spiller and their team. I have also relied extensively on field research on the Kenyan telecommunications sector performed by Michael Tyler, Charles Jonscher, Janice Hughes, and Helena Renfrew.

I would also like to express my appreciation to the people that made this research possible. My colleagues in the Stanford Program in International Legal Studies, particularly Eric Jensen, Sophie Pirie, Lawrence Friedman and Rogelio Perez-Perdomo offered invaluable input and guidance on the substance, methodology and framework of this thesis.

Teri Adams of the Disability Resource Center and Darren J. Luvaas of the Assistive Computer Technology Center at Stanford University offered moral and practical support.

The generosity of two anonymous funding sources allowed me to enroll in the Stanford Program in International Legal Studies.

Editorial assistance from Mugo Kibati and Sandra Macharia is also greatly appreciated. All the inadequacies and errors in this paper, however, remain entirely mine.

Finally, I would like to thank my family and friends. Annie Kameri-Mbote provided her mentoring throughout this process. Winnie Ouko, Njeri Gakonyo, other SPILS fellows and colleagues at the Global Fund for Women offered cheerful support. Finally, Mugo Kibati and my family (Helen, David, Chris and Sandra Macharia) showed remarkable interest and patience, offering encouragement at every stage of the project.

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