

## AFRICA RISK CONSULTING

### Country briefing – Kenya

25 September 2013

## Summary

*President Uhuru Kenyatta confirms that security forces have regained control of Westgate Mall following Al Shabaab's attack on Westgate Mall on 21 September. The Westgate attack will hit Kenya's economic growth in the short term but neither this nor the International Criminal Court (ICC) hearings will have long-term impact on the economy. The ICC adjourns the trial of deputy president William Ruto to allow him to return to Nairobi. The ICC had already agreed to stagger his trial with Kenyatta's but a political slow-down is still probable. The Central Bank of Kenya held its key lending rate at 8.5%.*

### 1.1 Al Shabaab attacks Westgate Mall in Nairobi

President **Uhuru Kenyatta** confirmed on 24 September that security forces had seized complete control of the **Westgate Mall** after a three day siege. **Al Shabaab** has claimed responsibility for the armed attack on the mall in **Westlands, Nairobi** which began on 21 September. The attack on a prominent commercial site will jeopardise investor confidence, preclude any withdrawal of Kenyan forces from **Somalia**, and mark a new phase in the strategy of al Shabaab.

The initial assault resulted in 72 deaths, including six security personnel and five militants. Eleven suspects have been arrested. The number of fatalities is likely to rise. The emergency services have begun to sift through rubble as three floors of the building collapsed following a series of explosions during a military operation to dislodge the militants. The attack was sophisticated with al Shabaab fighters armed with AK-47s and grenades separating into two groups, one entering through the heavily-guarded front of the mall, and the other through the basement car park.<sup>1</sup> Kenyatta said that initial intelligence reports indicated that several of the militants were **British** or **United States (US)** nationals. Authorities initially reported the attack as an armed robbery gone wrong. This is highly improbable. The attack bears the hallmarks of an al Shabaab *amniyat* (special cell) operation. There are disputed claims that the gunmen allowed Muslims to escape; **al Qaeda** had previously criticised al Shabaab's willingness to kill Muslim civilians.<sup>2</sup> The taking of

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<sup>1</sup> Standard, 22 September 2013

<sup>2</sup> Daily Nation, 22 September 2013

hostages without the issuing of demands suggests that the seizure was to retain international media attention after the initial attack, rather than leverage to barter an escape as might be expected of a criminal gang.

Al Shabaab issued its claim of responsibility on **Twitter**, claiming that it was in retaliation for Kenya's military intervention in Somalia in October 2011.<sup>3</sup> Kenya's cross-border mission had as objectives to create a buffer zone to secure the porous border with Somalia and to prevent the trafficking of men and arms into Kenya. Despite agreeing to a negotiated withdrawal from **Jubaland** in August,<sup>4</sup> Kenyan forces remain in Somalia notably in control of the commercial and strategic port city of **Kismayo** which the KDF took from al Shabaab in September 2012.

Recent events have increased the probability of an al Shabaab 'spectacular' in either Somalia or Kenya [see *Kenya ARC Briefing February 2013*, *Somalia ARC Briefing July 2013* and *Somalia ARC Briefing September 2013*]. **Sheikh Ahmed Godane (Abu Zubayr)**, the **Somaliland** born emir of the group who favours international jihad over nationalist objectives, launched a bloody internal purge of the group's *shura* (ruling council) in June. Godane ordered the capture and executions of rivals including **Ibrahim Haji Jama Mead (Ibrahim al-Afghani)**, **Sheikh Abdihafid Hashig Olhaye (Maalim Burhaan)** and **Sheik Hassan Dahir Aweys**. Godane's sole leadership means that the group's philosophy will be aligned with his own **Salafi-jihadist** ideology. Aweys, the group's former spiritual leader – detained by federal forces in June – previously tempered Godane's jihadism. Aweys was a committed nationalist and opposed any foreign intervention including not only in Somalia, but also with regard to attacks in Kenya. Godane's leadership will deter many ordinary Somalis from supporting al Shabaab, encouraging the move away from conventional insurgency to terror attacks which began following a series of military defeats in Somalia including the loss of Kismayo. Attacks on international economic targets will help Godane prove his jihadi credentials after Al Afghani complained to al Qaeda leader **Ayman al Zawahri** about his autocratic leadership. The exact role of domestic militants is uncertain. The organisation formerly known as the **Muslim Youth Centre**, now **al Hijra**, is aligned with al Shabaab and supportive of Godane and his jihadi ambitions. It has been involved in the recruitment of Kenyan youth to fight in Somalia, but mainly acts as a forum for low-level provocateurs. Whether it would have the capacity to offer logistical support to such a complex operation is uncertain. The failure of the intelligence services to pick up signals intelligence regarding the planning of the attack suggests al Shabaab kept external communication to a minimum.

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<sup>3</sup> Twitter/HSM\_Press

<sup>4</sup> Sabahi, 7 August 2013

The hollowing out of Kenya's security sector facilitated the attack. The 2010 constitution provides for security sector reform, but the privileged position of the military in Kenyan politics means it will take time, money and political will to implement. Meanwhile, corruption and patronage have weakened Kenya's intelligence agencies. Effective intelligence sharing between Kenya and western agencies has prevented similar plans to attack Nairobi<sup>5</sup> and has curbed Islamist militant activity to small-scale gun and improvised explosive device attacks in Nairobi, **Mombasa** and the North Eastern province. However, Western agencies have re-focused their energy, funding and resources on threats emanating from the **Sahel**, notably **al Qaeda in the Islamic Maghreb**.

## 1.2 Deputy president William Ruto appears at The Hague

In response to the Westgate Mall attack, the **International Criminal Court (ICC)** adjourned the trial of deputy president **William Ruto** until 30 September. The trials of Ruto and radio station executive **Joshua arap Sang** began as scheduled on 10 September. Ruto, as expected, pleaded not guilty. The ICC immediately adjourned the trial which resumed on 17 September with the appearance of the first prosecution witness. The adjournment hinted at procedural delays which are likely to mean the cases against Ruto and President **Uhuru Kenyatta** will run for years rather than months.<sup>6</sup> Ruto left **Nairobi** for **The Hague** on 9 September, as the appeals chamber is still to offer a final ruling on whether he will have to attend all hearings in person.<sup>7</sup> However, the ICC agreed to stagger the trials of Ruto and Kenyatta, hearing each during alternative four week periods.<sup>8</sup> This may resolve Kenya's constitutional uncertainty - the constitution does not permit the president and his deputy to be absent from the country at the same time - but not the political. Even with staggered scheduling, the absence of both Kenyatta and Ruto from Nairobi would leave a gap at the heart of Kenyan politics. A procession of law makers wanting to demonstrate their loyalty is expected in The Hague. This will slow government decision-making and policy formation. However,

*"Kenyatta's appointment of a technocratic government with a corporate management style should mean that it is closer to business as usual than you might imagine".<sup>9</sup>*

The trial began amid criticism at the perceived anti-African bias of the ICC. In Kenya, special hearings of the National Assembly and the Senate both passed resolutions calling on the government to withdraw from the ICC. Should Kenya rescind its membership by revoking the Rome Statute, it would be the first member state to do so and a blow to the authority of the court. The significance would be greater to the ICC than to Kenya. Withdrawing from the ICC would not reduce Kenya to pariah status; its role as a key regional

<sup>5</sup> Source, senior western intelligence officer, Nairobi

<sup>6</sup> Source, journalist, Nairobi

<sup>7</sup> <http://www.icc-cpi.int/iccdocs/doc/doc1634623.pdf>

<sup>8</sup> Daily Nation, 9 Sept 2013

<sup>9</sup> Source, businessman, Nairobi

security and economic actor (see below) means that neither **Europe** nor the United States - which is itself not a member of the ICC - can afford to be overly critical. It would not affect the trials of either Ruto or Kenyatta as, once started, legal proceedings are not dependent upon a state's membership status.<sup>10</sup> The parliamentary motion will have little practical impact. Any withdrawal from the Rome Statute that established the ICC requires the submission of a formal request to the **United Nations** secretary general, a process that would take at least a year. Across the continent, Kenyatta has begun to develop a bloc of support against the ICC ahead of an extraordinary summit of the **African Union** in October whose agenda consists solely of Africa's relationship with the ICC. In September:

- A **Ugandan** foreign ministry official said that the government may follow Kenya's example and withdraw from the ICC;<sup>11</sup>
- **South African** deputy foreign minister **Ebrahim Ebrahim** called on the ICC to allow the Kenyan judiciary to try Ruto and Kenyatta under its own jurisdiction;<sup>12</sup>
- On an official visit to **Nairobi**, **Nigerian** president **Goodluck Jonathan** advocated that the United Nations Security Council refer the case back to the Kenyan courts.<sup>13</sup>

Kenyatta continues to manage his response to the hearings carefully. He pre-empted the opening of Ruto's hearings by announcing that the 40,000 still internally displaced people in camps following the 2007-2008 election violence would be rehoused before 20 September.<sup>14</sup> He handed cheques for \$4,500 to families in **Eldoret** and **Nakuru**, some of the worst affected parts of the **Rift Valley**. There is currently no domestic investigation into the post-election violence.

### 1.3 Westgate attack will hit business sector in short-term, but neither the attack nor ICC pose long-term risk

The attack on Kenya's modern economy will hit business confidence in the short-term. Westgate is home to a number of regional and international brands including **Nakumatt**, **Truworths** and **Woolworths**. International firms may defer investment decisions until it is known whether the international business sector and expatriate community were specifically targeted. Tourism, a key source of foreign exchange revenue, is likely to experience a decline before returning to normal levels.

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<sup>10</sup> Reuters, 3 Sept 2013

<sup>11</sup> DPA, 9 Sept 2013

<sup>12</sup> AFP, 6 Sept 2013

<sup>13</sup> The Star, 6 Sept 2013

<sup>14</sup> Daily Nation, 8 Sept 2013

The ICC trials appear to be having little impact on doing business in Kenya. Kenyatta's visit to **China** in August [see *ARC August briefing*] had encouraged perceptions that Kenya was going to favour doing business with those governments critical of the ICC. This was emphasised by Jonathan's criticism of the ICC coming as he led a business delegation including Nigerian industrialist **Aliko Dangote** to Nairobi. The value of the \$5 billion infrastructure contracts that Kenyatta signed with China, including for a standard gauge railway between **Mombasa** and **Malaba** on the **Ugandan** border, will encourage western governments to abandon previous threats of denying Kenyatta foreign investment:

*"European governments that said they would not conduct business with Kenya under a Kenyatta administration are quickly backtracking. There will be contracts signed by the **Spanish** and **Germans** in the energy sector during the next few months and in 2014, each worth over \$100m. General trading continues as always [see below] and tourism levels remain high. There are much bigger issues than the ICC for investors. Growth is slowing and expenditure is increasing as the government tries to fund devolution".<sup>15</sup>*

Political uncertainty caused by the ICC is not having an impact on investor confidence. The **Nairobi Securities Exchange (NSE)** revealed that the bourse's equity turnover reached \$241m in August.<sup>16</sup> According to an NSE statement, turnover increased by 86% compared to figures for July. This was the highest turnover in the NSE's history, and the result of an inflow of foreign investment as firms announced half year results. Foreign investors' participation stood at 52% accounting for shares worth \$172m. The main movers were **Nation Media Group** trading shares worth \$70m and **Safaricom**, \$32m. These figures reveal renewed investor confidence which had previously been hit by the risk of violence and political uncertainty in the run up to the March elections. The government is basing its economic strategy on the calculation that the ICC trials won't deter foreign investment. Treasury secretary **Henry Rotich** announced on 3 September that Kenya may seek as much as \$1.5 billion from its debut Eurobond issue, double the previously stated figure.<sup>17</sup> This would be **sub-Saharan Africa's** largest debt sovereign bond issue. The Eurobond will be a ten year note, to be issued in either November or December. Kenya first considered launching a Eurobond in 2007, but repeatedly delayed the issuance due to the post-election violence and then the global financial crisis.

Government portrayals of the ICC as an international conspiracy increase the probable risk of a political backlash and potential security risks for western companies in Kenya. One source at a **British** company in the oil sector says his company is especially nervous because of Kenyatta's criticism of high commissioner **Christian Turner** in the run up to the election.<sup>18</sup> Kenyatta's electoral victory in March 2013 was predominantly due to his ability to portray the ICC as a colonialist plot against Kenya. If Kenyatta resumes

<sup>15</sup> Source, businessman, Nairobi

<sup>16</sup> Shanghai Daily, 8 September 2013

<sup>17</sup> FT, 4 September 2013

<sup>18</sup> Source, oil sector analyst

such populist rhetoric in a bid to discredit the ICC process, this will increase the probability of anti-western protests with foreign businesses an attractive target.<sup>19</sup>

#### 1.4 Central Bank of Kenya holds key interest rate at 8.5%

The **Central Bank of Kenya (CBK)** held its key lending rate at 8.5% on 3 September.<sup>20</sup> The CBK's monetary policy committee said that the short-term outlook for inflation was stable, although it noted that the new VAT Act that came into effect on 1 September would contribute to inflationary pressures.<sup>21</sup> Inflation, at 6.67% in August up from 6.02% in June, remains within the allowable margin of 2.5% either side of the government's medium term target of 5%.<sup>22</sup> The VAT Act 2013 adds a charge of 16% on consumer goods that were previously exempt including milk and mobile phones.<sup>23</sup> The committee noted that confidence in the economy remains strong, with the NSE index rising from 4,598 in June to 4,698 in August.<sup>24</sup> The committee also raised concerns about risks to its macroeconomic outlook, notably its current account deficit, caused by political instability in the **Middle East** and **North Africa**. This has resulted in higher international oil prices between June and August and could pose a threat to Kenya's tea exports, a key source of foreign exchange earnings for Kenya. The CBK said that the Treasury's borrowing rates were on target and not putting pressure on interest rates.

## 2 Implications

The Kenyan government will cite the mall attack as a reason for maintaining the KDF presence in Jubaland. In the short term, retaliatory attacks on ethnic Somalis particularly in Nairobi's **Eastleigh** district will increase, as will pressure on the government to accelerate the repatriation of Somali refugees. This will be detrimental to already strained relations with the Somali federal government. The attack may provide western governments with an opportunity to rebuild contacts with the Kenyatta government currently damaged by their support for the ICC cases facing Kenyatta and Ruto. Kenyatta has looked to **Russia** and China for diplomatic and economic support during the build up to the ICC hearings, but the attack will remind him that he needs the continued support of the US and **United Kingdom** to address the serious and continuing Islamist extremist terrorist threat to Kenya.

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<sup>19</sup> Source, oil sector analyst

<sup>20</sup> Reuters, 3 Sept 2013

<sup>21</sup> Reuters, 3 Sept 2013

<sup>22</sup> Kenya Bureau of Statistics, 30 Aug 2013

<sup>23</sup> Daily Nation, 3 Sept 2013

<sup>24</sup> Xinhua, 4 Sept 2013

The ICC says the trials of Kenyatta and Ruto are expected to last months. This is highly ambitious; they will rumble on for years. The vote to rescind Kenya's membership of the ICC may not have an impact on the trials, but is symptomatic of a growing frustration in Africa at a body that is perceived as biased and political. Kenyatta has two important allies in Uganda's **Yoweri Museveni** and Nigeria's Goodluck Jonathan, and the ICC may struggle to restore its credibility. Even with staggered scheduling, the absence of both Kenyatta and Ruto from Nairobi will leave a gap at the heart of Kenyan politics. This will slow the government's decision making and policy formation. Young political leaders may see their absence as an opportunity to establish competing claims to their authority as Kenya's political old guard tends to defend its power jealously. Sporadic, low-level instances of violence can be expected in the Rift Valley and outskirts as the case progresses and unearths dormant ethnic grievances.

Any economic weakening from the attack on the Westgate Mall will not be as severe or as sustained as that which followed the 2007-2008 electoral violence. Should this attack prove to be an isolated incident, investors will see it within the wider narrative of Somalia's instability, rather than a bellwether of continued widespread violence in Kenya as was feared following the election. Kenya will remain an attractive destination for foreign investment and subscriptions for the Eurobond debut will remain high. The ICC trials also will not have a detrimental impact on the Kenyan economy, although some foreign investors will delay decisions until they understand the impact any political slowdown will have on Kenya's macroeconomic performance and the NSE. The CBK rate has been constant since May and will remain so until the end of the year in the face of inflationary pressures and a bearish currency. The monetary policy committee's next meeting is in November. The CBK may begin to tighten its monetary policy in 2014. In the shorter term, a spike in inflation is expected at the end of the month as the VAT Act takes effect. It will, however, provide a wider revenue base and therefore greater economic stability. The Eurobond launch reflects Kenyan confidence that the ICC trial will not deter foreign investment.