Stable Growth

An examination of the oft-overlooked link between political stability and economic growth, with special attention to the Kenyan experience

Benjamin Sawatzky

ABSTRACT

This paper examines the link between political stability and growth, and uses the Kenyan experience as a case study. It also looks into education and agriculture as two sectors that can be used to create a virtuous cycle of political stability and economic g rowth.

When considering economic development, the focus is usually on economic variables, the idea being that the growth of these variables leads to the realization of economic development. At first glance, this would seem to make sense. However, one could easily make the argument that economic development is not actually possible without the political conditions that enable economic action to be effectively implemented. This leads to the hypothesis that economic development requires not only a focus on economic variables, but also on social and political factors. As a first step towards showing that, this paper examines the relationship between political stability and growth, using Kenya as a case study. Political instability is defined here as corruption, irregular regime change, violent internal or external conflict, or popular unrest. Growth is defined as high levels of key economic variables, in particular: GDP growth, per capita GDP, or foreign direct investment. Kenya makes an ideal case study, as for a developing country it has remained generally stable and experienced generally good economic performance, but has had periods of political instability which allow us to see how the economy reacts. This paper will also examine education and rural development as two sectors that promote a virtuous cycle of political stability and growth, and show how Kenya has successfully included them in its development path.

Kenyan Political Stability and Growth

Kenya became a state in 1963, when it was granted independence by the British Government. In 1964, Jomo Kenyatta of the KANU party was elected

president. Despite some negative expectations, Kenyatta ruled even-handedly, including disparate groups in the decision-making process and developing a free-market economy open to foreign investment (HistoryWorld). He died in 1978, leaving a country viewed by many as a model of political stability and economic progress. The country's stability found its roots first of all in Kenyatta's fair and effective rule, but also in two other aspects. Kenyatta focused heavily on education for the Kenyan people, increasing the number of primary schools from 6058 in 1963 to 9243 upon his death in 1978, and enrolment increased from 891,553 to 2,994,991 in that same period (Eshiwani, 1993). The number of secondary schools in the country also rose dramatically from 51 in 1963 to 1,773 in 1978 (Eshiwani, 1993). He also initiated Kenya's focus on rural development, starting the Special Rural Development Program in 1966 (Ergas, 1982).

Economic performance during Kenyatta's tenure was unquestionably positive. Kenya saw a steady increase in per capita GDP, going from $195 in 1970 to 455$ in 1978 (United Nations, 2009). There were also high levels of GDP growth, averaging around 5.4% during the 1970s until his death (United Nations, 2009). This was accompanied by an equally large increase in foreign direct investment in Kenya. FDI in 1970 amounted to $14 million, and by the time of Kenyatta's death it had risen to $57 million (World Bank, 2009). During this period Kenya also saw high growth rates in the economic value-added by such activities as utilities, mining, and manufacturing (United Nations, 2009). However, during this period there were

highly erratic periods of growth and decline of GDP by expenditure in each of the different categories (United Nations, 2009). This would imply that it was not just one aspect of the economy which lead to this rapid economic growth, but rather that it was due to some overarching trend in the system of political economy as a whole.

After Kenyatta's death in 1978, Daniel Moi assumed the presidency. At the beginning of his tenure economic indicators stayed high, but this was not to last. While Moi did assume office peacefully, his presidency soon began to give off an aura of corruption and instability. In 1981 there was a military coup against Moi's leadership (Crawfurd.dk, 2009), and although it was not successful the economy went into a tailspin. Per capita GDP began to fall, and fell steadily through to 1985, when it recovered briefly (United Nations, 2009). GDP growth averaged between 1% and 3% through first half of the '80s, although it too recovered in the second half of the decade, ranging from 4% to 7% (United Nations, 2009). Foreign direct investment also dropped precipitously, from $79 million in 1980 to $14 million in 1981 (World Bank, 2009). This trend also reversed itself in the second half of the 1980s, with FDI ranging around $50 million (World Bank, 2009). However, in the early 1990s this period of grace ended dramatically. 1990 saw protests beginning against Moi's rule, and in 1991 an opposition party was formed (Crawfurd.dk, 2009). Moi soon banned it, and jailed several of its leaders (Crawfurd.dk, 2009). This sparked protests against the Moi government's repression and human rights abuses, as well as its history of corruption. Elections were held in 1992, and were widely

viewed as having been skewed dramatically by Moi. There were allegations of vote-rigging, and changing the boundaries of districts to support candidates he favoured (Narman, 2003). During the election ethnic clashes erupted, leaving 2000 dead (Crawfurd.dk, 2009). In the end Moi was re-elected president, although he spent massive amounts of state funds in the process (Narman, 2003). In keeping with our trend, the early 90s saw the Kenyan economy plunge in all of its key indicators. GDP growth dropped to 1.4% in 1991, and actually was negative at -0.4% in 1992 (United Nations, 2009). It remained low through to 1994, although it recovered in '95 and '96, hovering around 4% (United Nations, 2009). Per capita GDP dropped from $411 in 1992 to $276 in 1993, although it too recovered to previous levels by 1995 (United Nations, 2009). Foreign direct investment fell to $19 million in 1991 and $2 million in 1993, although it posted a brief recovery in 1995 (World Bank, 2009).

While economic indicators recovered slightly after Kenya regained its stability, this proved to be a fleeting phenomenon. There were more elections in 1997, which were characterized as having been "marred by violence and fraud" (CIA, 2009). The IMF finally suspended loans to Kenya, due mostly to its massive corruption (HistoryWorld). Economic indicators followed the existing trend, dropping precipitously once more during this period. GDP growth dropped to 0.4% in 1997, and remained low throughout the rest of the 1990s and early into the new millennium (United Nations, 2009). Per capita GDP fell as well during this period, reaching its trough of $397 in 2002 (United Nations, 2009). Foreign direct investment fell to $11 million in 1998, and remained low until 2002, with the

exception of a huge spike in 2000 (World Bank, 2009). This trend continued until 2002.

In 2002 the NARC opposition party, led by Mwai Kibaki, gained power in a landmark election victory. While the new administration contained many members from the old regime and was plagued by many of the same problems of corruption, they campaigned heavily on the promise of reform. The IMF resumed loans to Kenya, and economic indicators rose quickly. GDP growth was a low 0.6% in the election year, but rose steadily to 7% in 2007 (United Nations, 2009). Per capita GDP also rose, from a low of $397 in 2002 to $711 in 2007 (United Nations, 2009). Foreign direct investment rose from $5 million in 2001 to $82 million in 2003, and it had jumped to $728 by million in 2007 (World Bank, 2009). As can be seen, Kenyan economic performance directly followed shifts in its political climate. Despite this list of destabilizing events in Kenyan political history, Kenya's population and culture remained quite stable, and it is this stability that this paper claims provides the basis for Kenya's high level of average growth.

Beyond being circumstantially demonstrated in the Kenyan experience, there have been studies done showing the connection between stability and economic growth. Yi Feng's 1997 study "Democracy, Political Stability, and Economic Growth" found that those three variables are all reciprocally related. Democracy in particular was found to have a significant and positive effect on economic growth by inhibiting

regime interruption and enhancing system adjustability (Feng, 1997). The probability of regular government change in a democracy also tends to have a positive effect on growth (Feng, 1997), as the leader is forced to enact policy changes promoting growth or face the possibility of losing the next election. It is regime interruption that is the biggest factor, as "irregular political changes, such as coup d'etats, instill great amounts of uncertainty into the marketplace, slowing down and even reversing economic growth" (Feng, 1997, p. 397). Any sort of political change, such as civil conflict or a disputed election can cause this uncertainty. The data from Feng's survey supports this conclusion, as irregular political change was found to have a statistically significant negative impact on the growth equation (Feng, 1997). On the opposite side of the issue, major and minor government changes were both found to have a positive impact on the growth equation, although in a joint estimation analysis the effect of minor government changes on growth was only statistically significant at the 5% level, but not at the 1% level (Feng, 1997).

Beyond this research on the effects of stability on growth, there is also research supporting the proposition that corruption has a negative effect on growth. This is based on the idea that corruption within a country and its government lowers the rate of investment. In a 1995 study, Paolo Mauro examined data on corruption drawn from Business International, which measures indicators of institutional efficiency. BI includes an indicator for corruption, but Mauro also combines the indicators for corruption and bureaucracy & red tape into an indicator that he calls "bureaucratic efficiency", as he "consider[s] the bureaucratic efficiency

index to be a better measure of corruption than the corruption index on its own" (Mauro, 1995, p. 686). This combination provides a better measure of corruption within the data. Both the B.E. and corruption indicators are highly correlated inversely to per capita GDP, the investment rate, and per capita GDP growth. There was also a significant correlation between political stability and corruption. In terms of strength, the corruption and B.E. indices were significantly and robustly negatively associated with investment, even controlling for other determinants of investment. The corruption and B.E. indices were also both significantly and robustly negatively correlated with average GDP growth over 1960-1985, although this result was not as robust as the correlation with investment. Corruption was found to work its effect mostly on total investment, rather than just leading to a reallocation of investment (Mauro, 1995).

This data has obvious connections to the Kenyan experience. Mauro found a significant correlation between political instability and corruption (Mauro, 1995), and as Kenya became more unstable under Moi it also became much more corrupt. At the time Mauro's paper was written in 1995, Kenya was rated in the 4.5-5.5/10 grouping of global corruption rankings, which was the second lowest grouping (Mauro, 1995). Demonstrating Mauro's conclusions, Kenyan economic indicators were generally quite low throughout the 1990s.

Kenya and Education

The first development aim adopted by Kenya that furthered both stability and growth was a focus on education. Since gaining independence in 1963, Kenya

has invested heavily in education. In fact, education has become an important part of Kenyan culture. Education had been promoted in Kenya even before independence, as a student loan program was begun in 1957 (Rogers, 1972). The Kenyan investment in education can also be seen in the growing number of schools. The number of primary schools in the country grew from 6058 in 1963 to 12943 in 1986, and the number of secondary schools grew from 51 in 1963 to 2413 in 1985 (Eshiwani, 1993). Completion of primary school in Kenya has also risen dramatically in the years since independence. While it rested at a low 47% in 1987, it had reached 54% by 1975 and 73% in 1980 (World Bank, 2009). By 2005, Kenyan completion of primary school was 93%, a testament to their focus on educating the population (World Bank, 2009). This focus has paid off, as according to the most recent data the Kenyan literacy rate had reached 85% (CIA, 2009). The average school life expectancy in Kenya is 10 years (CIA, 2009), which is fairly high, especially for a developing country. For comparison within Africa, Zambia sits at 7 years, and Nigeria sits at 8 years (CIA, 2009). Despite these high indicators, Kenya has not decreased its levels of investment in education. It currently spends 7% of GDP on education, which ranks 27th in the world (CIA, 2009).

In terms of the link between education and stability, educated populations tend to be more stable, if only because the educated generally have more to lose in any event of political instability. The New York Times undertook a study in 2009 that demonstrated this link. They found a 77% correlation between education levels

in 1960 and the subsequent 40-year average of the Polity IV democracy index (Glaeser, 2009). The study also found that "basically no countries with low levels of education […] have managed to be democratic over the long term, and almost every country with a high level of education has remained a stable democracy" (Glaeser, 2009). This led them to the conclusion that "education […] does an extremely good job of predicting increases in democracy" (Glaeser, 2009). Education can also be structured in such a way that it promotes democracy and markets. In 1994 Poland implemented a program of civic education to foster support for democracy and markets in the youth. A study of the program found that it made students less likely to take extreme anti-democratic or extreme anti-market positions (Slomczynski & Shabad, 1998). However, it also found that the program made them less likely to take extreme pro-democratic or pro-market positions (Slomczynski & Shabad, 1998). Active participation in civic education "results in students' political attitudes regressing to the mean, that is, in their rejection of extreme stances" (Slomczynski & Shabad, 1998, p. 749). Despite not conclusively proving that this program made students more interested in democracy, it still shows a positive result in terms of political stability. Taking extreme positions often is a destabilizing influence, so students' attitudes regressing towards the mean could then be seen as a stabilizing effect.

Education also has a direct effect on economic growth. Education allows a populace to perform higher value-added jobs, and this has enabled Kenya to become

a “regional hub of trade and finance” (CIA, 2009). Education also has a direct impact on GDP growth. A 2004 study by Musila and Belassi demonstrated this by studying the impact of education expenditures in Uganda on GDP growth using time-series data. Since 1995 Uganda has increased the shares of education and health in its budget, and has experienced growth rates averaging 4.2% between 1995 and 2000 (Musila & Belassi, 2004). Musila and Belassi explained this by relating output to education expenditures. They used a logarithmic transformation to make output a function of growth in capital stock, employment, and average expenditure on education per worker. They ended up with the equation LOGRGDPt = 4.92 + 0.177LOGKt + 0.588LOGLt + 0.621LOGEt, with Kt representing capital formation at time t, Lt representing employment at time t, and Et representing education expenditures per worker at time t (Musila & Belassi, 2004). The equation states that for every 1% increase in education expenditures, GDP increases by 0.621%. An interesting fact highlighted by this equation is that increasing education has the strongest positive effect on GDP, beyond even gross capital formation or increasing employment. This study certainly shows that “average education expenditure per worker is positively correlated with economic growth” (Musila & Belassi, 2004, p. 131), and that “macroeconomic policies aimed at increasing investment through foreign direct investment and domestic sources are crucial” (Musila & Belassi, 2004). The study goes on to state, “it is difficult to see how economic growth can improve without providing sufficient fund [sic] for the education sector” (Musila & Belassi, 2004, p. 132). The authors also state “security and political stability also plays a part in attracting foreign direct investment and retaining human capital”

(Musila & Belassi, 2004, p. 132), and that for education expenditures to have the fullest results "it is imperative that there be competent administration at lower levels of government" (Musila & Belassi, 2004, p. 131). The conclusions of this study serve to highlight the links between political stability, education, and economic growth.

However, while education does certainly have a positive impact on GDP, it can affect it in ways beyond stimulating investment and retaining human capital. A 1999 study by Vidal and Brauninger showed that the method of financing education could determine how much of an impact on GDP it has. First of all, they show that more equal societies grow faster than less equal ones (Brauninger & Vidal, 2000), which again supports the claim that stability in the population is a key for economic growth, on the assumption that equal societies are also more stable. In their model they claim that there is a trade-off between learning-by-doing and learning through schooling at low levels of public funding (Brauninger & Vidal, 2000). This means that a mix of public and private education can lead to lower growth than purely private education, as more workers educate their children and crowd out savings (Brauninger & Vidal, 2000). The study concluded however that long run growth is maximized with fully subsidized education (Brauninger & Vidal, 2000), supporting their conclusions that equality promotes economic growth. This is borne out in the Kenyan experience, as after the government implemented mandatory free primary education in 2002 the country experienced much higher average growth rates.

Education can also have a greater effect on specific sectors. A study by Hanson in 1989 showed a positive relationship between increased education and resource development, another trend shown by the Kenyan experience (Hanson, 1989). Between 1970 and 1991 Kenya averaged a rate of growth in value-added by the mining, utility, and industrial sector of 7% (not counting the outlier year of 1982, where growth was -5.6% during the attempted military coup) (United Nations, 2009). This rate of growth of value-added was much higher than any other Kenyan economic activity in this period. Once again, we can see that through a virtuous circle of stability and education, Kenya was able to secure consistent returns in terms of growth.

Kenyan Rural Development

A second program that promoted both political stability and economic growth was Kenya's program of rural and small town development. 59% of Kenyan farms are 2 hectares or less, and 52% of those small-scale farmers live on or near the poverty line (Thomas-Slayter, 1992). The majority of land in Kenya is not arable (Gaile, 1988), and 70% of Kenyans are employed in the agricultural sector, contributing 30% of the national GDP (Lewis, 1991). Furthermore, the majority of Kenya's population is rural, and the proportion has grown over the years. There was a 30% increase in Kenya's rural population between 1969-1979 (Jones, 1986). The importance of this sector is therefore clear, both in terms of its contribution to

Kenya's economy and its potential impact on the political stability of the region. Hence, Kenya's rural development policies have been considered a form of population-resource development (Gaile, 1988). These various small town and rural development policies have been used as a way to channel future growth into small and intermediate towns, in order to support economic growth and provide and adequate agricultural surplus.

Kenyan land reform was begun in 1954, before independence. The Swynnerton Plan was "supposed to address African land problems by reforming land tenure, consolidating fragmented holdings, issuing freehold titles, developing and intensifying African agriculture, providing access to credit, and removing restrictions on growing crops for export" (United Nations University, 1995). However, while "the Swynnerton plan created the basis for a market-oriented class of African farmers to work within a commercial farming export sector and was credited with tripling agricultural output between 1955 and 1964" (United Nations University, 1995), it also "succeeded in fostering land concentration and social stratification" (United Nations University, 1995). The first truly Kenyan policy of rural development was the Special Rural Development Program, which was in effect from 1966-1975. It was implemented largely to deal with problems of youth unemployment, and of poor and landless farmers; the program was intended to increase the stability and well being of those population sectors. The SRDP involved global donors (including the US, UK, Sweden, and the Netherlands) (Ergas, 1982), as well as funding from the Kenyan government. Despite being phased out in 1975, the SRDP developed several important innovations, such as the Rural Access Road

Program and the Group Extension Program, which used group settings to teach farmers new techniques and then aided with their implementation (Ergas, 1982). Before being phased out in1975, the SRDP managed to increase the contribution of small farms to monetary agriculture dramatically, from 7.9% in 1957 to 51.6% in 1972 (Ergas, 1982). In addition, the program induced the Kenyan government to adopt more equitable and effective policies, and focused attention on the crucial problem of the poor farmer (Ergas, 1982).

Since the 1970s, the government has stressed the importance of "balanced growth", meaning growth in both rural and urban economic areas (Lewis, 1991). Balanced growth was to be led by agriculture, given the high proportion of the population and GDP tied up in the agricultural sector. To do this they promoted the widespread growth of small towns, which in turn promoted non-agricultural activities that were strongly linked to agriculture. Kenya implemented a small town development program in 1987, testing it first in the Kutus region (Lewis, 1991). This program was designed to support agriculture, and its objectives were to increase production, incomes, and wage employment in regions around those small towns. Once again this was a way of increasing both economic growth, through support of one of Kenya's largest industries, and of increasing political stability by allocating resources to its largest and poorest population group.

The effectiveness of this focus on rural development on Kenya's stability is shown by the fact that 70% of the Kenyan population lives in rural areas. These programs promoted equitable and efficient development, and included the largest proportion of the country in the economic process. By attempting to promote their interests and not leaving them out of the economic system, they gave rural populations a vested interest in supporting stability within the system. The focus on poor farmers served this same purpose. These policies also created a virtuous circle in terms of policy, as the focus put on equity in this context affected the general viewpoint on development. Kenyan development policy in general became more focused on equitability as well as efficiency, and this can be seen in distributional as well as developmental policy decisions. An example of this is in the Kenyan government's reaction to the coffee boom of 1976-79. Rather than increase taxes or purchase coffee from the farmers at previous prices, the government instead passed the price increase on to the farmers (Bevan, 1987).

Generally speaking the Kenyan focus on rural development makes sense, as there is a well-documented connection between agriculture and growth. There are four main contributions made by agriculture to the process of economic development: a product contribution, a factor contribution, a market contribution, and a foreign exchange contribution. The product contribution of agriculture "refers to the fact that agriculture must supply food above subsistence needs in order to feed labour working in alternative occupations" (Thirlwall, 2006, p. 169). It is

impossible to develop other sectors of the economy without a well-fed labour force, and until those sectors are developed it is unlikely that a country will be able to export enough to support importing its food. The marketable surplus, which is the difference between total agricultural output and subsistence needs, is a prerequisite for economic progress. If the marketable surplus does not rise as the demand for food increases, the price of food will rise. This will then cause the wage of workers to rise, and reduce that country's cost position. The marketable surplus is therefore one of the major constraints on industrial growth.

The next contribution by agriculture to the process of economic development is a factor contribution, which consists of a labour contribution and a capital contribution. In developing countries, labour for industry and other activities must come from labour, but only becomes available when agricultural productivity rises. This makes developing productivity in the agricultural sector crucial for being able to develop other industrial sectors. Agriculture can also provide a means for saving and capital accumulation for industrial development. This can be done through voluntary savings, or through taxation. Either way, the agricultural surplus provides the base for investing in an industrial sector.

The third contribution by agriculture to economic growth is a market contribution. This refers to the fact that agricultural markets provide the major source of domestic demand for industrial goods, especially at early stages of

economic development. Agricultural growth and industrial growth are therefore in some ways complementary. A World Bank report concluded that "a stagnant rural economy with low purchasing power holds back industrial growth in many countries" (Thirlwall, 2006, p. 170), which would seem to indicate that a strong agricultural sector is a prerequisite for any sort of meaningful industrial growth. This lends additional importance to Kenya's focus on rural development.

The final contribution of agriculture to economic growth is through foreign exchange. At early stages of development, when there is limited manufacturing and industrialization taking place within a country, the agricultural sector is likely to be the only source of goods to be exported. This gives a country access to goods that are difficult or impossible to produce domestically. This foreign exchange gives the country access to highly productive imports, and again furthers the development of its industrial sector.

In terms of Kenya specifically, studies on the small town development policies pursued by Kenya show that agriculture has had a large positive impact on the Kenyan economy. A study by Lewis in the Kutus region of Kenya found that agriculture and related sectors had the highest effect on output. The highest output modifier (3.31) was found to be in the coffee processing industry, which supports the agricultural industry (Lewis, 1991). The next two industries with the highest impact on output were food crops (2.732) and coffee itself (2.727) (Lewis, 1991).

Even the two below those were agricultural, being respectively farm-based non-farming activities (2.698) and livestock (2.585) (Lewis, 1991). This same trend was found in examining the value-added to the economy by various industries. Value-added was led by livestock (1.460), coffee (1.443), and food crops (1.429) (Lewis, 1991). Lewis also examined the effect of stimulating non-agricultural sectors on the agricultural sector itself. He found that stimulating coffee processing had the highest effect on agricultural outut (1.048), followed by farm-based non-farm activities (0.185) (Lewis, 1991). However, the service sector was found to have the greatest effect on stimulating wage employment (0.194), although farm-based non-farm activities ranked second in this category (0.166) (Lewis, 1991). All of this data lends support to the efficacy of small town development. Agricultural industries were found to greatly stimulate the economy, and furthermore industries that support agriculture were found positively stimulate growth of agricultural output, as well as stimulating economic growth in general.

Conclusion

Through the examination of Kenya as a case study, we can see several factors at work. First of all, we can see that stability has a clear impact on a country's general economic performance. This would seem to demonstrate that despite whatever specific development strategies that Kenya pursued at different times, it was the country's level political stability that had the most conclusive effect on the economy. Furthermore, we can see the clear interrelations between education, stability, and growth, and between agricultural and rural development, stability, and

growth. This again shows that not only do these programs have a positive impact on economic growth, but they also have a positive impact on domestic stability, which itself has a positive impact on economic growth. This virtuous cycle seems to play a key role in Kenya's development, and is not limited to the Kenyan experience. Research shows that these policies have a general impact on stability and growth, and therefore can be applied to any country. The advantage of this virtuous cycle of development is that it is highly flexible. Rather than positing specific, cookie-cutter theories of development, we can focus on the factors than make development possible and allow it to happen organically, in a way suited to the environment in which it takes place. While more research would need to be done on the impact of these policies to prove it on a general level, the trends demonstrated here show that stability is something that must not be overlooked, and is a crucial foundation that allows the development process to occur.

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