RESEARCH REPORT

An Overview of the Performance of the East African Economies since 1985: Implications for the New Initiative on East African Co-operation

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1.1 Background

In spite of the acrimonious break-up of the East African Community in 1977, followed by a six year long negotiation process that culminated in the sharing of the Community’s assets in late 1984, hope remained that inter-state co-operation would be restored at some point in the future. The World Bank-appointed negotiator, Dr Victor Umbricht, conducted the protracted negotiations that resulted in the signing of an agreement under which Kenya was to retain 42%, Tanzania 32% and Uganda 26% of the assets. During the signing of the agreement, leaders committed themselves to explore areas of renewed co-operation, due to a realisation of the disadvantages of the break-up of the Community. Tanzania soon re-opened its border with Kenya, which further helped to bridge the erstwhile areas of intense disagreement. It was apparent that room was being created for renewed purposeful engagements between the former partners.

This paper reviews trends in economic growth and development and intra-regional trade among the East African states from the time of the division of the assets of the defunct East African Community through to the time of the new initiative of the East African Co-operation (EAC). For the purposes of this study, the period from 1985 to the most recent date for which data has been compiled will be considered. Factors that contributed to the renewed efforts towards integration will be analysed, and recent trends in trade and economic growth will be assessed.

The period between 1977 and 1984 will be omitted for several reasons. Firstly, this was the time when relations between the three East African states were at their worst. Mistrust was rife, the border between Kenya and Tanzania had been closed, while the chaos in Uganda was such that no meaningful engagements with foreign countries were possible. The period was character-
ised by the smuggling of goods and open hostility at the expense of trade and regional development. Secondly, during the same period, Kenya was undergoing an economic and political transition that was to affect its overall development for many years to come. The country’s impressive growth from the 1960s through to the late 1970s was coming to an end. The international financial institutions, mainly the World Bank and the International Monetary Fund (IMF), were prescribing structural adjustment programmes (SAPs) to many sub-Saharan African countries, including those in East Africa. Thirdly, and perhaps most importantly, it was after 1985 that major changes began to be felt across East Africa, which hastened the urgency for closer co-operation.

In 1985, the President of Tanzania, Julius Nyerere, retired from office and was succeeded by Ali Hassan Mwinyi. By this time, it had become evident that the socialist policies which Tanzania had adhered to for more than two decades were not working. In spite of sustained donor support, mainly from Scandinavian countries, the economy was stagnant and inefficient, with high rates of unemployment. Foreign direct investment was not forthcoming because the socialist government viewed such ventures as nothing short of neo-imperialism. However, donors were also becoming fatigued, and Tanzania inevitably had to respond to growing calls for reform.

In Uganda, the National Resistance Movement under Museveni was closing in on Kampala, and by 1986 demoralised government forces had been defeated. Museveni and his followers took control of the country. Many years of fighting had left the country badly ravaged, infrastructure had virtually been wiped out, and the economy was in shambles. Inflation was very high and the country’s productive capacity had shrunk extensively. In these circumstances, external trade had been rendered almost impossible. It is therefore difficult to come up with credible data on Uganda’s external trade for the early 1980s.

In Kenya, the down-turn that had begun in the early 1980s was continuing unabated. High levels of corruption, repression and overall economic mismanagement had seriously eroded any gains that had been made in the preceding two decades. Vital institutions supportive to agriculture, the mainstay of the economy, including the Kenya Farmers’ Association (KFA) and the Agricultural Finance Corporation (AFC), had been systematically destroyed. Furthermore, tourism, the other major public revenue earner, was seriously threatened by a spate of poaching that was only contained by government after an international outcry. Many other factors, including the government’s reluctance to effect the urgently required economic reforms, contributed to a deeper slide into stagnation. However, a coffee boom in 1986 helped to stabilise the country’s foreign exchange position and rekindled hopes for recovery.

It may be argued, thus, that the upheavals of the pre-1985 period limit the possible acquisition of meaningful data for the purposes of this study. Economic statistics since 1985 will bring out more clearly the overall impact of the changes that followed, including market reforms coupled with sluggish politi-
cal reforms, as well as overall global changes. In Section 5.2, differences in per capita incomes and economic size between member countries are considered, while Section 5.3 will mainly analyse the growth performance of the East African economies between 1985 and 1996. Section 5.4 examines differences in economic structure among the three countries. Recent developments are considered in Section 5.5, while East African trading relations are the focus of Section 5.6.

1.2 Per capita income and economic size (GDP)

As Table 5.1 shows, Kenya is the largest of the three economies in terms of GDP. In 1995, Kenya’s GDP of US$ 8142 million was nearly 50 per cent bigger than that of Tanzania, and more than 60 per cent greater than that of Uganda.

Table 1.1: Summary characteristics of the East African economies, 1995

<table>
<thead>
<tr>
<th>Country</th>
<th>Area in sq km</th>
<th>Population in millions mid-1995</th>
<th>GNP per capita (US$)</th>
<th>Life expectancy</th>
<th>Adult illiteracy</th>
<th>GDP US$ millions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kenya</td>
<td>580</td>
<td>26.7</td>
<td>280</td>
<td>58</td>
<td>22</td>
<td>8142</td>
</tr>
<tr>
<td>Uganda</td>
<td>236</td>
<td>19.2</td>
<td>240</td>
<td>42</td>
<td>38</td>
<td>5042</td>
</tr>
<tr>
<td>Tanzania</td>
<td>945</td>
<td>29.6</td>
<td>120</td>
<td>51</td>
<td>32</td>
<td>5488</td>
</tr>
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Kenya’s population was 26.7 million by mid-1995. According to World Bank estimates, Kenya’s GNP, measured at average 1993-95 prices, was US$ 7583 million that year, yielding a per capita income of US$ 280 (Table 5.1). GNP per capita in Uganda and Tanzania was US$ 240 and US$ 120 respectively in 1995. These figures highlight the low and unequal levels of development in the region in terms of per capita income, especially between Kenya and Tanzania. Indeed, for 1995, Tanzania was the poorest country in the world, according to the World Bank figures.

From 1985 to 1995, GNP per head in Kenya increased in real terms at an average annual rate of 0.1 percent. During the same period, GNP per capita for Tanzania and Uganda grew at 1.0 and 2.7 per cent respectively (World Bank, 1997: 214). The relatively poorer per capita GNP growth performance for Kenya was partly due to bad weather that affected food production and also a high rate of inflation that had been triggered by a large increase in the money supply in the period preceding the 1992 elections (see Section 5.3). In a period when the food import bill was on the increase, Kenya’s export commodities
were becoming increasingly uncompetitive in the international market due to the high domestic rate of inflation.

1.3 Growth performance between 1985 and 1996

As the data in Table 5.2 indicate, after the economic stagnation of the early 1980s that saw the standard of living in most African countries deteriorate, many African countries, including the EAC member states, started experiencing an economic upswing at the close of the decade and during the post-1990 period. This upswing has, however, not been strong enough to raise living standards substantially. Nevertheless, a comparative analysis of the growth statistics points to a positive, though unsteady, upward trend. This is partly attributable to the hastened pace of economic liberalisation during this period. The liberalisation programme was prescribed by the Bretton Woods institutions (the World Bank and IMF) as a policy response to low growth and financial crisis in the affected countries. Although the conditions had been prescribed in the early 1980s, it was not until the end of the Cold War that most countries in Africa began to realise the gravity of the crisis caused by their reluctance to liberalise (Financial Times, November 1996:2).

Table 1.2: Real GDP growth rates for the East African countries between 1980 and 1995 (%)

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</tr>
</thead>
<tbody>
<tr>
<td>Kenya</td>
<td>4.2</td>
<td>2.1</td>
<td>0.5</td>
<td>0.2</td>
<td>3.0</td>
<td>4.9</td>
</tr>
<tr>
<td>Uganda</td>
<td>3.1</td>
<td>3.1</td>
<td>8.4</td>
<td>5.3</td>
<td>10.6</td>
<td>8.5</td>
</tr>
<tr>
<td>Tanzania</td>
<td>3.8</td>
<td>0.7</td>
<td>2.6</td>
<td>4.4</td>
<td>3.5</td>
<td>3.5</td>
</tr>
</tbody>
</table>


Another significant factor was the impact of global changes at the beginning of the 1990s that seriously and negatively affected the fortunes of many countries in sub-Saharan Africa. After the Cold War, the strategic alliances held previously with African countries as bulwarks against rival ideologies became irrelevant and so did the economic support packages that used to accompany such alliances. Western donors started linking their aid to African countries to what has been referred to as market reforms and good governance. Consequently, African countries that had hitherto relied heavily on donor funding as a ‘reward’ for staying in the same ideological camp found themselves under pressure to effect change. Bilateral donors, and even the international financial institutions, started showing their growing preference for Eastern Europe, which was opening up after decades under communism.
The Eastern European countries were viewed as more attractive to direct foreign investment as they were liberalising at a faster rate, and had a sizeable pool of trained manpower. Another possible reason for their relative attractiveness is perhaps more political than economic, namely that Eastern Europe, being at the doorstep of the more industrialised Western Europe, should not be ignored because any social-political upheaval resulting from economic collapse would certainly affect the latter. It is also natural for a rational business person to try and harness markets according to their proximity and accessibility. Besides, having won Eastern Europe from the control of Russia, the former Western bloc would not have wanted a poverty-driven reversal by such countries, possibly into communism or another alliance with the former Soviet Union.

Thus aid and foreign direct investment continued to diminish in East Africa and Africa in general as a result of the apparent shift of attention by donors and investors to other emerging markets. Indeed, due to economic mismanagement and the general market instability caused mainly by political upheavals, it was no longer feasible for investment to trickle readily into Africa. Hence, change became inevitable.

The other contributory factor to the economic upswing in the period after 1990 was the occurrence of good weather which made agriculture, the mainstay of the East African economies, perform well. The agricultural sector remains one of the most important contributors to GDP yet it is the most volatile, since its overall performance is generally determined by weather conditions. In 1995, the agricultural sector contributed 29, 50 and 58 percent of total GDP in Kenya, Uganda and Tanzania respectively (Table 5.3). Water is especially critical as its shortage often leads to a substantial drop in crop yields. Droughts cause huge fluctuations in food prices, especially for a country like Kenya whose arable land is a mere 20 percent of the total. Adverse weather conditions always have negative implications for food security and often result in higher import bills and possible balance of payments problems (EAC/ds, 1997:8).

Since the late 1970s, the primary products produced in East Africa have been subject to a significant decline in their terms of trade. Farmers’ earnings have continually declined, seriously affecting the forward-backward linkage process necessary for economic growth (EAC/ds, 1997:8). In the 1990s, besides the relatively better weather, there has been a substantial diversification that has seen horticulture coming to the fore as a major foreign exchange earner in the region, especially in Kenya.

Turning to the economic performance of the individual EAC member states, in the period between 1980 and 1990 Uganda’s real GDP grew at an annual average rate of 3.1 per cent which, by 1992, had dramatically risen to 8.4 per cent (Table 5.2). The positive growth performance, especially in the early 1990s, was mainly attributable to the fact that the political and economic reforms the country had embarked on in 1986 were starting to pay dividends. In
the years 1994 and 1995, GDP grew at 10.6 per cent and 8.5 per cent respectively (Table 5.2). These high rates of growth reflect a rapid expansion of the productive sectors in response to the sustained implementation of economic reforms. Gross fixed capital formation also improved tremendously, from US$ 152 million in 1985 to US$ 967 million in 1995. With a population growth rate of around 2.5 per cent per annum, per capita income grew by 8.1 per cent and 6 per cent in 1994 and 1995 respectively (EAC/ds, 1997:9).

Although we have identified the 1990s as a period of economic upswing, it is noteworthy that Kenya was experiencing a difficult transition period at about the same time. The struggle for the restoration of a multiparty system of government accelerated at the start of the decade with pro-multiparty agents openly challenging the government to reform. What followed was a costly and violent confrontation and gross human rights violations by an intransigent kleptocracy fearful of change. With the linking of aid from Western donors and the international financial institutions to issues of good governance and respect for human rights, the activities of the Kenyan government led to the freezing of aid to the country in order to increase pressure for change. Left with no option, the government agreed to allow the registration of more parties. This step, however, was not enough to usher in an era of good governance and sound economic management.

In a subsequent general election in December 1992, the Kenyan government imprudently printed paper money for campaign purposes, increasing the money supply by an enormous 35 percent, which resulted in the highest inflation rate ever recorded in the country (over 46 percent). The adverse effects of this increase in the money supply, coupled with other financial scandals, including the 'Goldenberg case', have continued to be felt in the economy.

Initially, therefore, after 1990, the rate of growth of GDP in Kenya continued on a downward slide, falling to a mere 0.2 percent in 1993, the lowest growth-rate since independence in 1963. Besides the economic and political problems that pervaded Kenya at the time, the slowdown was further compounded by a drought that caused the agricultural sector to register negative growth of approximately 4 percent in 1993. With a population growth rate of 3 percent annually, per capita income grew negatively between 1990 and 1993. However, the economy has been on an up-turn since then, registering GDP growth rates of 3 percent and 4.9 percent in 1994 and 1995 respectively (Table 5.2). This can be attributed to good weather and the deepening of the implementation of economic reform policies. However, per capita income is still low, at US$ 280 in 1995.

In the 1973-1978 period, Tanzania’s GDP grew at an average rate of 5.5 percent, but thereafter, through to the early 1980s, the economy only managed to grow at annual rate of around 0.4 percent (EAC/ds, 1997:9). Average GDP growth picked up from the mid-1980s up to 1990 due to the economic reforms that were beginning to yield benefits to the economy. Consequently, in spite of
the apparent slump at the beginning of the decade, the overall average growth in GDP between 1980 and 1990 was 3.8 percent (Table 5.2). However, during the same period, the economy suffered successive balance of payments deficits and shortages of foreign exchange with which to buy inputs for all sectors, while poor rates of tax collection undermined attempts to achieve a balanced budget. In addition, drought, intermittently depressed commodity prices, and illegal mining and mineral smuggling adversely affected economic development.

As noted earlier, by 1985, Tanzania had started implementing market reforms under the new government of Ali Hassan Mwinyi. The government adopted austerity measures recommended by the IMF, including devaluation of the currency, attempts at stringent budgetary controls and the easing of restrictions on foreign exchange. In the 1990s, Tanzania started reaping the benefits of economic and political change. Indeed, as Table 5.2 shows, the economy experienced a turnaround, and in 1993 grew at 4.4 percent, followed by 3.5 percent in 1994 and 1995. Agriculture remains the dominant sector in the economy, accounting for 58 percent of GDP in 1995 (Table 5.3). With a population growth rate of 2.8 percent annually, per capita income growth has been positive in the last three years, but not strong enough to raise per capita GNP, estimated at a dismal US$ 120 in 1995.

1.4 Economic structure

Generally, agriculture remains the dominant sector in the East African economies. It is the main foreign exchange earner and also one of the largest employers. As noted earlier, in 1995, agriculture accounted for 58, 50, and 29 percent of GDP in Tanzania, Uganda and Kenya respectively (Table 5.3). It is projected that agriculture will remain one of the major sectors driving economic growth in the region in the medium term.

Table 1.3: Sectoral structure 1995 (percentage contribution to total GDP)³

<table>
<thead>
<tr>
<th>Country</th>
<th>Agriculture</th>
<th>Industry</th>
<th>Manufacturing</th>
<th>Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>Kenya</td>
<td>33 29</td>
<td>21 17</td>
<td>13 13.8</td>
<td>47 54</td>
</tr>
<tr>
<td>Uganda</td>
<td>72 50</td>
<td>4 14</td>
<td>4 7.4</td>
<td>23 36</td>
</tr>
<tr>
<td>Tanzania</td>
<td>46 58</td>
<td>18 17</td>
<td>11 6.5</td>
<td>37 24</td>
</tr>
</tbody>
</table>


With 58 percent of its GDP accruing from agriculture, Tanzania has the highest dependency on this sector among African countries, closely followed by Ethio-
pia with 57 percent. The sector employed 83.0 percent of the labour force in Tanzania in 1996 (Europa Yearbook, 1998:3278). The principal cash crops are coffee, cotton, cashew nuts and cloves (Zanzibar's most important export, cultivated on the island of Pemba). Other cash crops include tobacco, tea, sisal, pyrethrum, coconuts, sugar and cardamom. Tanzania's agricultural GDP increased by an average of 5.7 percent in 1986-1995.

Industry contributed an estimated 17 percent of GDP in 1995. During 1985-1994, there was an average annual increase of 6.8 percent in Tanzania's industrial GDP. This is estimated to have declined substantially in 1995, however. Mining provides only a small proportion of the contribution of industry to GDP, estimated at 1.3 percent in 1996. Diamonds, other gemstones (including rubies and sapphires), gold, phosphates, salt, coal, gypsum, tin, kaolin, limestone, and graphite are mined, and plans are underway to commence the exploitation of natural gas reserves. Other mineral reserves include nickel, silver, cobalt, copper, soda ash, iron ore and uranium, and exploration for petroleum is in progress. The GDP for the mining sector is estimated to have increased by an annual average of 18.2 percent in 1986-1995 (Europa Yearbook, 1998:3278).

Tanzania's most important manufacturing activities are food processing, textile production, cigarette production and brewing. Pulp and paper, fertilisers, cement, clothing, footwear, tyres, batteries, pharmaceuticals, paint, bricks and tiles, and electrical goods are also produced. Tanzania's manufacturing GDP grew at an estimated annual average of 0.9 percent in 1986-1995. The slower growth in manufacturing meant that the sector's share of GDP declined from 11 percent in 1980 to an estimated 6.5 percent towards the end of 1995 (Table 5.3). Energy is derived principally from hydro-electric power, which supplies more than 70 percent of Tanzania's electricity. Imports of petroleum and petroleum products accounted for 11.2 percent of imports in 1996 (Europa Yearbook, 1998: 3279).

Kenya's agriculture sector contributed an estimated 29 percent of GDP in 1995 and employed about 77 percent of the total labour force in 1996. Principal cash crops are tea (which contributed 24.1 per cent of total export earnings in 1993) and coffee (which contributed 14 percent of export earnings in 1993). Horticultural produce (Kenya is the world's fourth largest exporter of cut flowers), pyrethrum, sisal, sugar cane and cotton are also important (Europa Yearbook, 1998:1951). Maize is the principal subsistence crop. There is also a significant dairy industry producing for domestic consumption and for export. During 1991-1995, agricultural GDP increased by an average of 0.3 percent.

Measured by gross value of output, Kenya's principal manufacturing activities in 1993 were food processing, the manufacture of chemicals, petroleum products (using imported crude oil), electrical machinery and transport equipment. Hydro-electric power accounts for 80 percent of total electricity generated, while geothermal energy supplies about 15 percent and other sources about 5 percent of the total. In 1993, imports of mineral fuels (including crude
petroleum intended for refining) comprised 15.0 percent of total imports. Tourism makes an important contribution to Kenya’s economy and has been one of the principal earners of foreign exchange for the country since 1987 (EAC/ds, 1997:10). However, civil unrest in the coastal region during 1997 posed a serious threat to the sector. In January 1995, the Nairobi Stock Exchange (NSE) was opened to foreign investors and this has contributed to greater capitalisation of the institution. Generally, the GDP of the services sector increased by an annual average of 3.4 percent in the period 1991-1995.

In 1994, there was a slump in the share of industrial output to GDP. A possible reason for this apparent decline in industrial output was the rise in costs of industrial inputs as the value of the Kenya shilling depreciated. However, the decline had started in the early 1980s. The sector contributed an estimated 17.0 percent to Kenya’s GDP in 1995 compared to 21 percent in 1980 (Table 5.3). During 1991-1995 industrial GDP increased by an annual average of 1.6 percent. In 1995 mining contributed an estimated 0.2 percent of GDP. Soda ash is the principal mineral export. Fluorspar, iron ore, salt, limestone, gold, gemstones (including rubies and sapphires), vermiculite and lead are also mined. During 1991-1995, the GDP of the mining sector decreased by an annual average of 0.5 per cent. Kenya has substantial reserves of titanium in the coastal region which have begun to be exploited (EAC/ds, 1997:10).

Uganda’s agricultural sector contributed just over 45 percent of GDP in the financial year ending 30 June 1996, down from 50 percent in 1995, and employed an estimated 83.1 percent of the labour force in the same year. The principal cash crops are coffee, cotton, tea and maize. Tobacco, sugar cane, cocoa, and horticultural produce are also cultivated. The main subsistence crops are plantains, cassava, sweet potatoes, millet, sorghum, maize, beans, groundnuts and rice. Agricultural GDP increased by an annual average of 4.4 percent in the period between 1986 and 1995, and by 4.2 percent in the 1995/1996 financial year ending 30 June 1996 (Europa Yearbook, 1998:3412). Despite this satisfactory growth performance, faster growth in manufacturing (see below) led to the fall in agriculture’s contribution to GDP between 1995 and 1996.

In Uganda, mining makes a negligible contribution to GDP (0.3 percent in 1996). Output of copper, formerly an important export, virtually ceased during the late 1970s. The production of cobalt from stockpiled copper pyrites was expected to commence in 1999. Until the 1970s there was a small scale of mining activity. Uganda is believed to possess the world’s largest deposit of gold, which began to be exploited again in the mid-1990s (Europa Yearbook, 1998:3412). Indeed, in 1996 gold accounted for 6.9 percent of the value of exports. In manufacturing, Uganda’s most important activities are the processing of agricultural commodities, brewing, vehicle assembly and the production of textiles, cement, soap, fertilisers, metal products, shoes, paints, matches and batteries. Manufacturing GDP increased by an annual average of 12.5 percent
in 1986-1995, and by 18.1 percent in the financial year ending in June 1996. This impressive growth performance is reflected in the increased share of manufacturing in GDP from 4 percent in 1980 to 7.4 percent in 1995. Uganda’s energy is derived mainly from hydro-electric power. The country exports a substantial amount of this to Kenya. In 1996, imports of fuels accounted for an estimated 1.5 percent of the value of Uganda’s imports.

The services sector, which includes the public sector, has been one of the fastest growing, and contributes substantially to the region’s GDP. In 1995, its contribution to GDP was 24, 36, and 54 percent for Tanzania, Uganda and Kenya respectively (Table 5.3). It also provides the majority of modern wage employment, although the share of those employed in the public sector has been declining due to retrenchments (EAC/ds, 1997:7). The EAC Secretariat therefore views the future prosperity of the private service sector as being of vital importance to the regional economy in terms of direct employment and wealth generation. Furthermore, the service sector also provides support to other sectors, particularly manufacturing. Owing to its future potential within the regional economy, development of service-related activities, particularly in tourism and trade, will be necessary to accord it due priority in the medium and long-term.

Although the share of the manufacturing sector has been growing in both Kenya and Uganda, the increase has been relatively sluggish in Kenya compared to Uganda. Between 1980 and 1995, Kenya’s manufacturing sector registered marginal growth and the sector’s share in GDP only grew by a dismal 0.8 percent. A poorer performance can be noted in the case of Tanzania where, as noted earlier, the share of manufacturing in GDP actually declined from 11 percent in 1980 to 6.5 percent in 1995 (Table 5.3). Consequently, Uganda is the only country showing a significant increase in the share of manufacturing in GDP. The poor performance of the other countries was partly due to the adoption of policies that might not have been conducive for the faster growth of a manufacturing base. Most manufacturing industries in the region are products of import-substituting industrialisation which, it has been argued, led to complacency, inefficiency and rising costs (EAC/ds, 1997:8). Apart from agricultural and other natural resource-based industries, manufacturing in the region has remained predominantly an enclave sector.

In spite of the sluggish growth in the manufacturing sector within the region, its labour productivity remains higher than in other sectors. The experiences of the Newly Industrialised Countries (NICs) have shown that a faster expansion of the manufacturing sector is a necessary condition for sustainable GDP growth, and this is likely to apply in East Africa as well (EAC/ds, 1997:8). In order to sustain the EAC’s projected annual regional GDP growth rate of at least 6 percent, the Secretariat suggests in its Development Strategy that it will be vital to continue aggressively with an export-oriented strategy in order to expand manufacturing at a faster rate.
1.5 Recent developments

1.5.1 Kenya

With the 1997 elections over without the anticipated increase in the money supply and social-political upheavals, Kenya appears to be in a relatively better position than expected. However, it is instructive that aid negotiations between the country and the international financial institutions broke up towards the close of 1997 over accusations of official corruption, and had not resumed by the end of 1998. The IMF still maintains that the government has not done enough to contain or stamp out official corruption, and to collect taxes and duties from individuals within its ranks. Consequently, the Kenyan government has been forced to increase taxes in order to make up for the deficit occasioned by the refusal of the IMF to disburse US$ 205 million in late 1997. This policy has not gone down well with workers who were already overtaxed before the latest fiscal adjustments were considered. Workers in various sectors have thus resorted to work stoppages as they demand salary increments, which has inevitably had a negative effect on an economy already in recession.

Furthermore, the government has had to freeze most of the intended development projects due to lack of funds. However, the reform program is broadly on track and vital indicators such as the budget deficit appear to be well under control. Estimates by the end of 1996 pointed to a deficit (excluding grants) of 1.3 percent of GDP compared with a budget target of 1.7 percent. Growth was forecast at 4.5 percent – a slackening in momentum largely reflecting the relatively poor rains, continued high real interest rates and an increasingly uncompetitive exchange rate.

After the dramatic success in bringing the average annual inflation rate down in 1995 from 24 percent in January to 1.6 percent in December, inflation soon rose again, reaching 7.8 percent for the year to September 1996 and 10.4 percent year on year. In an effort to raise money, the government had been issuing treasury bills at high interest rates of over 20 percent for 91 day bills, and bank lending rates had been ranging from 22 to 28 percent. Real interest rates have been far too high, which is acting as a disincentive to local investors. It has, however, been attracting a lot of short term capital or hot money inflows that are complicating the Central Bank’s efforts to maintain a competitive exchange rate (Financial Times, November 1996:2).

The 1996 figures show the balance of payments on the current account looking quite healthy, with the 12 month deficit falling steeply to only US$ 86 million in August from US$ 631 million a year earlier. The main reason for this was a reduction in the trade deficit. The overall balance of payments position was a surplus of US$ 59.2 million in 1996 compared with a deficit of US$ 134 million in 1995. The improvement in the current account stemmed mainly from better performance in exports and moderate increases in services. An improvement in net private and short-term capital inflows resulted in an increase of

GDP figures in 1996 were much lower than had been expected. GDP in real terms grew by 4.6 percent, below the projected 5.5 percent. Inadequate rainfall caused a shortfall in food production which necessitated food importation, while the high cost of domestic credit as well as power-rationing in the latter part of the year further affected investment and overall production adversely. This, together with an increasingly competitive trading environment, were the main causes of the slow down in growth of the economy (Economic Survey, 1997:115). The agricultural sector performed poorly as a result of the rain shortage. Most other sectors of the economy recorded meaningful growth, albeit lower than that of 1995.

Given its limited natural resource base (agriculture and tourism), Kenya has become heavily dependent on its geographical position and existing industrial base which make it the logical growth pole for East Africa, and its huge potential in the form of its relatively well educated, easy-going work-force. While the basis for macroeconomic stability may be in place, the other conditions necessary for sustainable growth of 6 percent to 7 percent annually are not (Financial Times, November 1996:3). The possible contribution of East African regional integration to growth will be considered later.

1.5.2 Uganda

Uganda, as a landlocked country, is concerned about securing efficient outlets to the sea and eliminating the inefficiency and corruption that adds to freight charges and import bills. The restructuring currently under way at the Mombasa and Dar es Salaam ports has benefited the Ugandan business community in its contribution to what has become one of the most remarkable economic recoveries. The country, once synonymous with disaster, now boasts one of the highest economic growth rates in sub-Saharan Africa. Just over ten years after President Museveni took office, the revival of a nation devastated by the despotic regime of Idi Amin and the war to overthrow him has continued apace.

Uganda’s GDP growth has averaged 6 percent annually since 1987, topped 8 percent during the year ending June 1996, and appears set to continue performing well. Inflation is in single figures, the currency is freely convertible, and foreign exchange reserves are in sufficient supply. The return of the Asian community expelled by Amin in the 1970s, and the greater general confidence in the economy, has led to the repatriation of flight capital at a rate of almost US$ 300 million per year, according to IMF estimates (Financial Times, November 1996:3).
If Uganda is to sustain high growth and replace aid by foreign investment, it must start expanding an export base currently reliant on a handful of cash crops, improve an infrastructure in which inadequate power supplies are a big constraint, and make an import substitution manufacturing sector competitive in the region and beyond. Further progress with the difficult task of trade liberalisation is part of the price of continuing approval from the Fund and the backing of the World Bank and other donors, worth US$ 500 million a year (Financial Times, November 1996:3). Tariff reform is also at the heart of the new EAC initiative. But most Ugandan manufacturers, only now reaching the production levels they enjoyed before the years of anarchy and civil war, may need more time to prepare for the competition that reduced trade barriers will bring, from Kenya in particular, as well as from trading partners further afield.

Private investment over the past few years has been concentrated on reviving a manufacturing sector dominated by import substitution, and local manufacturers may need more time to consolidate. A huge trade deficit with Kenya is always cited as a supporting argument for more protection for Uganda’s manufactures. In 1994, Uganda imported goods worth about US$ 172 million from Kenya, but Kenyan imports from Uganda totalled only US$ 3.2 million. The government is also concerned about the impact of trade liberalisation on state revenue. About half of Ugandan government revenue comes from various duties and taxes on imports. Lower tariff barriers would mean less revenue, hence the efforts to expand the country’s tax base by introducing value added tax (VAT).

However, it is argued that Uganda’s medium to long-term potential lies not in its modest manufacturing sector, but in food production, agro-processing, tourism and power supplies. Given its fertile land, it could become an important basic food supplier to neighbouring Kenya, where two-thirds of the land is arid or semi-arid. The second area is power, where plans to expand the country’s capacity could provide a surplus for sale to Kenya. Uganda’s tourism potential, as yet barely tapped, could also be exploited if plans for the joint marketing of the East African region and the easier movement of tourists between the three countries are fulfilled. Furthermore, if existing barriers were lifted, Uganda’s companies could raise capital on the Nairobi Stock Exchange (NSE) as economic co-operation takes hold.

Further growth could come from the revival of the country’s high quality cotton crop, rehabilitation of the tea estates and the development of non-traditional agricultural exports. However, insecurity continues to be a problem for Uganda. The rebels supported by Sudan and more recently by the Democratic Republic of Congo have been able to exploit ethnic rivalries, especially in the North, historical grievances and a sense of neglect highlighted by the contrast with the buoyant South. This insecurity is likely to absorb the attention of the Ugandan government at the expense of regional co-operation matters.
1.5.3 Tanzania

As noted earlier, Tanzania is the poorest of the three countries, with an average per capita income of only US$ 120. The country’s population of 29 million, roughly the same as Kenya’s, offers nothing like the same purchasing power to investors. The country’s infrastructure has been set back by the years of former President Julius Nyerere’s African socialism, and its lumbering bureaucracy remains a brake on development (Financial Times, November 1996:2). Despite being the slowest of the three nations to lower tariffs in line with COMESA recommendations, the country is running trade deficits with both Kenya and Uganda.

The fear among many local business people is that an embryonic manufacturing sector, already threatened by goods flooding in from the Middle East, China and South Africa, risks being overwhelmed by regional imports once co-operation takes root. However, while the short-term benefits remain unclear for Tanzania, long-term benefits could be significant. Unlike Kenya, Tanzania boasts huge tracts of unsurveyed, unexploited land available for leasing. Gold mining has already attracted many South African, British and Canadian firms. Tanzania is just beginning to recognise its failure to market its extraordinary tourist attractions, ranging from the island of Zanzibar to unspoilt game parks.

Moreover, the development of the Songo Songo natural gas scheme stands to turn the country into an exporter of power to the rest of the region. Opportunities also exist in various other sectors of the economy. Following the successful privatisation of Tanzania Breweries and Tanzania Cigarettes, divestiture of the 300 parastatals continues. In spite of the enormous potential, much remains to be done before it can be exploited. Under President Nyerere’s regime, which was marked by de-industrialisation and plummeting living standards, it became impossible to thrive legitimately and the seeds of corruption were sown. Liberalisation under President Ali Hassan Mwinyi simply opened up new avenues for shady personal enrichment. By 1994, the official practice of granting arbitrary tax exemptions to a few well-connected businessmen had reached outrageous proportions, prompting the IMF and donors, who provide a yearly US$ 1 billion in aid, to freeze assistance (Financial Times, November 1996:2).

The current leadership under President Mkapa has attempted to institute the transparency needed for conventional investment. An anti-corruption commission has been set up, an independent Tanzanian Revenue Authority (TRA) established, and the ‘Zanzibar loophole’, whereby lower duties on the islands lured container ships away from Dar es Salaam and encouraged vigorous smuggling to the mainland, is being addressed. The heads of graft-ridden parastatals have been sacked and a tight rein kept on expenditure. Inflation, which peaked at 42 percent in early 1995, fell to 18 percent in August 1996, and GDP growth was expected to rise to 5 percent for 1996 (Financial Times, November 1996:2). The tax system, however, still remains complicated and
burdensome which tends to encourage evasion and acts as a disincentive to investment.

1.6 Intra-regional trade in East Africa (1990-1996)

As can be expected, trade between the three East African countries is heavily skewed in Kenya’s favour. Being relatively more industrialised than the rest of her regional partners, Kenya continues to accumulate trade surpluses against them. The data presented below give a clear indication of the general trend of trading activities among the three countries.

There is traditionally only a small volume of trade between Uganda and Tanzania, mainly due to the fact that both countries have relatively smaller manufacturing bases which tends to minimise the number of tradable commodities between the two countries. It is, however, noteworthy that, over the past few years, trade has been increasing and is set to rise further as the region becomes more integrated.

**Table 1.4: Tanzania’s trade (1990-1996)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Value of exports in US $ millions</th>
<th>Value of imports in US $ millions</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Uganda</td>
<td>Kenya</td>
</tr>
<tr>
<td>1990</td>
<td>4</td>
<td>12</td>
</tr>
<tr>
<td>1991</td>
<td>4</td>
<td>7</td>
</tr>
<tr>
<td>1992</td>
<td>5</td>
<td>8</td>
</tr>
<tr>
<td>1993</td>
<td>6</td>
<td>8</td>
</tr>
<tr>
<td>1994</td>
<td>7</td>
<td>9</td>
</tr>
<tr>
<td>1995</td>
<td>8</td>
<td>11</td>
</tr>
<tr>
<td>1996</td>
<td>10</td>
<td>13</td>
</tr>
</tbody>
</table>

*Source: IMF (1990-1996).*

There are many factors that affect the availability, comparability and reliability of the data in use. It is arguable that statistical systems in many developing economies are still weak, and statistical methods, coverage, practices and definitions differ widely. Moreover, cross-country comparisons involve complex technical and conceptual problems that cannot be unequivocally resolved (World Bank, 1997:249). It should therefore be noted that discrepancies will occur in the figures given by various countries and those collected by other
independent agencies. This is why the data in Tables 5.4-5.6 record different figures for, say, Uganda’s imports from Kenya and Kenya’s exports to Uganda.

**Table 1.5: Uganda’s trade (1990-1996)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Tanzania</th>
<th>Kenya</th>
<th>Africa</th>
<th>Total exports</th>
<th>Tanzania</th>
<th>Kenya</th>
<th>Africa</th>
<th>Total imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>1</td>
<td>–</td>
<td>9</td>
<td>181</td>
<td>4</td>
<td>209</td>
<td>226</td>
<td>582</td>
</tr>
<tr>
<td>1991</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>175</td>
<td>5</td>
<td>51</td>
<td>61</td>
<td>402</td>
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<tr>
<td>1992</td>
<td>1</td>
<td>4</td>
<td>6</td>
<td>179</td>
<td>5</td>
<td>79</td>
<td>91</td>
<td>399</td>
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<tr>
<td>1993</td>
<td>1</td>
<td>5</td>
<td>8</td>
<td>135</td>
<td>6</td>
<td>127</td>
<td>142</td>
<td>457</td>
</tr>
<tr>
<td>1994</td>
<td>1</td>
<td>6</td>
<td>9</td>
<td>377</td>
<td>8</td>
<td>151</td>
<td>174</td>
<td>539</td>
</tr>
<tr>
<td>1995</td>
<td>2</td>
<td>7</td>
<td>11</td>
<td>533</td>
<td>9</td>
<td>186</td>
<td>234</td>
<td>740</td>
</tr>
<tr>
<td>1996</td>
<td>2</td>
<td>9</td>
<td>13</td>
<td>559</td>
<td>11</td>
<td>217</td>
<td>272</td>
<td>739</td>
</tr>
</tbody>
</table>

*Source: IMF (1990-1996).*

**Table 1.6: Kenya’s trade (1990-1996)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Tanzania</th>
<th>Uganda</th>
<th>Africa</th>
<th>Total exports</th>
<th>Tanzania</th>
<th>Uganda</th>
<th>Africa</th>
<th>Total imports</th>
</tr>
</thead>
<tbody>
<tr>
<td>1990</td>
<td>22</td>
<td>190</td>
<td>421</td>
<td>1120</td>
<td>10</td>
<td>–</td>
<td>96</td>
<td>2041</td>
</tr>
<tr>
<td>1991</td>
<td>34</td>
<td>46</td>
<td>171</td>
<td>1014</td>
<td>8</td>
<td>1</td>
<td>58</td>
<td>2178</td>
</tr>
<tr>
<td>1992</td>
<td>44</td>
<td>72</td>
<td>234</td>
<td>1337</td>
<td>9</td>
<td>5</td>
<td>58</td>
<td>1835</td>
</tr>
<tr>
<td>1993</td>
<td>93</td>
<td>115</td>
<td>385</td>
<td>1275</td>
<td>8</td>
<td>6</td>
<td>42</td>
<td>1744</td>
</tr>
<tr>
<td>1994</td>
<td>111</td>
<td>137</td>
<td>479</td>
<td>1683</td>
<td>10</td>
<td>7</td>
<td>256</td>
<td>2715</td>
</tr>
<tr>
<td>1995</td>
<td>137</td>
<td>169</td>
<td>605</td>
<td>1952</td>
<td>12</td>
<td>8</td>
<td>344</td>
<td>3554</td>
</tr>
<tr>
<td>1996</td>
<td>161</td>
<td>199</td>
<td>707</td>
<td>2203</td>
<td>14</td>
<td>9</td>
<td>398</td>
<td>3606</td>
</tr>
</tbody>
</table>

*Source: IMF (1990-96).*
The data presented in Tables 5.4-5.6 show the general direction of trade for the three countries, and particularly intra-regional trade. The columns showing total exports and imports aggregate the total value of international trade for the country in question. In spite of the obvious trade imbalance, a remarkable feature of this data is the steady increase in the value of trade between the East African countries over the last seven years.

Tanzania’s exports to Uganda, though still modest, have increased by more than 100 percent from US$ 4 million in 1990 to US$ 10 million in 1996. In the same period, the value of its exports to Kenya increased slightly from US$ 12 million in 1990 to US$ 13 million in 1996.

The value of the country’s imports from Uganda doubled, while those from Kenya grew tenfold between 1990 and 1996. It is notable that while there was relatively large proportionate increase in Tanzania’s trade with Uganda, the greatest increase in Tanzania’s intra-regional trade was in its imports from Kenya, worsening its trade balance with that country significantly.

In the period 1990-96, Uganda’s exports to Kenya increased nine-fold. Imports from Kenya, after a sharp fall in 1991, increased steadily to reach a higher level in 1996 than in 1990, accounting for about 80 percent of the country’s imports from Africa (Table 5.5). Uganda has, over the past few years, been emerging as Kenya’s largest trading partner among African countries. This trend appears to be continuing and is likely to intensify when barriers to trade are finally removed. Unfortunately, although Uganda and Tanzania’s exports to Kenya have been on the increase, they have not increased fast enough to narrow the existing trade imbalance.

Another discernible feature of the data presented above is the general increase in intra-African trade, at least from the East African countries’ perspective. The Kenyan Economic Survey (1997:115-116) indicates that African countries continued to be the major destination of Kenya’s exports for three consecutive years. In 1996, the value of Kenya’s exports to Africa and the European Union (EU) accounted for 79.7 percent of total exports, with Africa buying 46.7 per cent of the total as compared to EU’s 33 per cent. Within COMESA, Uganda and Tanzania continue to be Kenya’s major trading partners, absorbing 42.4 percent and 33.7 percent respectively of Kenya’s total exports to the region. Major commodities exported to Uganda include fuel and lubricants, cement, wheat and sugar, while important exports to Tanzania are iron products, beer, sugar, soaps and medicaments.

Most of the items traded regionally are manufactured goods. Kenya, being the relatively more industrialised of the three states, has been exporting the largest share of such products since the pre-independence period. Due to their smaller manufacturing base, Uganda and Tanzania have for a long time been unable to increase their volume of exports to Kenya, which has generally resulted in unfavourable trade balances with the more developed partner. However, as observed in Section 5.5, Uganda and Tanzania have been attracting
more foreign investment and have experienced faster growth than Kenya in recent years. These developments are likely to alter the pattern of trade within the region and also the composition of such trade as the two countries increase their volume of exports to Kenya. Such a scenario is likely to enhance economic integration in the region, as it implies the possibility of a more equitable development that may ease the tension stemming from the perception of unequal gains within the EAC.

1.7 Conclusion

This paper discussed the general economic scenario that prevailed in East Africa in the post-1985 period after major economic and political reforms began to be undertaken in the region. The aim was to show the economic background against which the new initiative of the EAC is being established and also to demonstrate the extent of the unequal levels of development in the region, which has a bearing on the possible pattern of distribution of the benefits of economic integration. A notable point is that, in spite of Kenya being the most developed of the three countries, its current poor growth performance at a time when Uganda and Tanzania are experiencing positive trends in economic growth may actually result in a substantial shift in the pattern of distribution of the benefits of integration in the future.

Notes

1. Uganda was still in disarray after the fall of the Amin regime. Amin’s successor (and predecessor), Milton Obote, who had allegedly rigged his way back to power in 1981, immediately became engaged in a guerilla war with Yoweri Museveni’s National Resistance Movement (NRM). Obote was overthrown by General Tito Okello in 1985, who in turn was deposed by Museveni’s NRM in 1986. In the face of such political instability, little significant economic activity could be carried out in the country.

2. The Goldenberg case involved the alleged collusion of some businessmen and government officials at the Treasury and the Central Bank of Kenya to defraud the government of billions of shillings under the pretext of exporting non-existent gold and diamonds.

3. Agriculture represents value added from forestry, hunting, and fishing as well as cultivation of crops and livestock production, while industry comprises value added in mining, manufacturing (also reported as a separate subgroup), construction, electricity, water and gas. Services include value added in all other branches of economic activity, such as wholesale and retail trade, transport and government, financial, professional and personal services such as healthcare, and real estate services (World Bank, 1997:258).

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