# IMPACT OF THE EAST AFRICAN CUSTOMS UNION ON FIRMS IN THE EDIBLE OILS SUB SECTOR IN KENYA

BY

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R50/P/7081/06

A RESEARCH PROJECT IN PARTIAL FULFILLMENT FOR THE AWARD OF

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A DEGREE IN MASTER OF ARTS IN INTERNATIONAL STUDIES AT THE

INSTITUTE OF DIPLOMACY AND INTERNATIONAL STUDIES (IDIS),

UNIVERSITY OF NAIROBI

NOVEMBER 2008

## DECLARATION

I declare that this is my original work and has never been presented in any- other University or examination body.

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Signature: . . m u ................ Date:

This research project has been submitted for examination with my approval as the Nairobi University supervisor.

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## ACKNOWLEDGEMENT

Many thanks to the Almighty God for guiding me through the entire period of project making and to my family for their encouragement and support during this entire period. I have a wonderful family and I thank all for whatever role they have played in my life. The special people who have filled my life with hope and joy include my mother who embodies strength , endurance and wisdom and my four sisters who treat me as the family trail blazer. Also to my eldest nephew who finds inspiration in my achievements.

Many thanks too to my supervisor Dr. Lucas Njoroge for his patience during this entire research period. You gave me the chance to see my best side.

# DEDICATION

This research project is dedicated to all those who believe in regional integration in East Africa.

## LIST OF ACRONYMS AND ABBREVIATIONS.

| | |
|---|---|
| AEC | AFRICA ECONOMIC COMMUNITY |
| EACCU | EAST AFRICA CUSTOMS UNION |
| EAC | EAST AFRICA COMMUNITY |
| EC . | EUROPEAN COMMISSION |
| ECOWAS | ECONOMIC COMMUNITY OF WEST AFRICAN STATES |
| ECCAS | ECONOMIC COMMUNITY OF CENTRAL AFRICA STATES |
| EPZ | EXPORT PROMOTION ZONE |
| COMESA | COMMON MARKET FOR EAST AND SOUTHERN AFRICA |
| IMF | INTERNATIONAL MONETARY FUND |
| RI | REGIONAL INTEGRATION |
| RECS | REGIONAL ECONOMIC COMMUNITIES. |
| OAU | ORGANIZATION OF AFRICAN UNION |
| SADC | SOUTHERN AFRICA DEVELOPMENT COMMUNITY. |

## ABSTRACT

Though the Customs Union is relatively new in East Africa, only a few studies on its influence have been done. Local manufactures of consumer goods are affected, as duties on majority of fast moving consumer goods drop due to reduction and eliminations of tariffs and other barriers.

The research design was a case study of selected firms in edible oil sector. Data was collected through semi-structured questionnaires administered through email or hand delivery to managers and policy makers. Quantitative analysis was used to determine the influence of the East Africa Customs Union on the said sector. The responses of the . respondents were used to make inferences on the effects mentioned.

The findings indicated that with the starting of the EAC, firms operating in Kenya have made efforts to establish branches in partner states. Both companies were agreeable to an increase in sales volumes, profits as well as market share due to the enlargement of the market. This study reveals that the establishment of the EACCU was a great step towards economic and social development for the East African people. It is therefore an effective tool to improve the living standards of the East African people.

From this study, I recommend that there is need to eliminate all existing non-tariff barriers as stipulated in article 13 of the EACCU which are a major hindrance to good business in East Africa. The EAC secretariat should formulate policies in consultation with the business community as well as other stakeholders such as manufacturers and the national government bodies such as revenue authorities.

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# CHAPTER 1: INTRODUCTION

## 1.1 Background to the Study

The research seeks to address a specific question: what have been the effects of the regional integration as it has progressed so far on the edible oils sub-sector? Specifically, how has the EACCU affected the performance of firms in this sub sector?

Integration is complex and multi-dimensional, it presents different faces to different individuals, groups and nations. It has been subject of debate and mixed emotions in the recent years.

For the purpose of this research, Regional Integration refers to the process of creation or enlargement of regional arrangements of cooperation and the efforts of nations to connect or reconnect themselves to an organization spearheading the cooperation. African countries have pursued regional integration arrangements to accelerate their economic developments. Such arrangements hold promise for individual countries and the continent as a whole and they require economic analysis of costs and benefits to inform the expectations of what such arrangements can realistically achieve and to help them succeed. East Africa has hence pursued regional integration through establishment of the East African Community.[1]

The record of integration is mixed. Some countries have been able to take advantage of the market economy and the resultant expansion of market size while others have felt

[1] **P.Nyongo,Regioanl integration in Africa;unfinished agenda, Academy Publishers Nairobi 1995**

marginalized. These market forces have not been able to guarantee employment and economic development in equitable proportions. The study will focus on the process of integration with an emphasis on the performance of firms in the edible oils sub-sector and thereby draw conclusions of the effects of the customs union in the large macrocosm of the manufacturing as well as the agricultural sectors. This is because agriculture is the mainstay of the economies in these countries. By studying a sector in this industry, we will understand how firms have reacted to the customs union.

With a vision to create wealth, raise standards of living for all people of East Africa and enhance the international competitiveness of the region through increased product, trade and investments, the East Africa integration process was envisaged to be a progressive process. The movement from one level of economic integration to the other was to be through negotiated protocols. In line with this undertaking, the EACCU protocol was signed in March 2004 and ratified in December of the same year. The study will therefore endevour to examine whether the customs union has led to growth of the firms. Trade liberalization that comes form establishing a customs union may result to trade creation and this is reflected with increases in sales volumes, profits and enlarged market share. By studying the firms, one can also make deductions on the role of the private sector in fast tracking the integration process.

## 1.2 Problem Statement

The treaty establishing the new EAC envisaged the establishment of a Customs Union as a first step, followed by a Common Market, a Monetary Union and a Political Federation. The Customs Union protocol was signed in March 2004, and came into force in January 2005.[2] However, only one year afterwards, the business community in the three countries began voicing complaints regarding the Customs Union. The contention being that Kenya being seen as the economical giant in East Africa would benefit more from the East Africa Community. The edible oils industry being one of the major export earners of the Kenyan government is a very crucial contributor to the GDP of the economy and therefore the need to ensure its growth and development both in Kenya and beyond the East African region.

With the mixed reactions ensuing from the ongoinfg implementation of the EACCU, there was need for a comprehensive study on the influences of the EACCU to sectors in the partner states so as to ensure corrective measures are taken on concerns that arose or promotion measures on areas that were beneficial to the EAC people. This paper is a critical analysis of today's key policy questions on regional integration in the East African community that resulted into the formation of the EACCU and how this impacts on performance of Kenyan firms in the Edible oil sector. This is because by studying the influence on one sector, one can make inferences on effects in other sectors. It seeks to

**2 Radelet S, Regional integration and cooperation in sub-Saharan africa:are formal trade agreements the right strategy? Development discussion paper no 592 HIID Harvard university 1997**

investigate the influence of the Customs Union on the sector before and after the Customs Union implementation.

Guided by the protocol establishing the EACCU, it will explore aspirations outlined which include customs administration, trade liberalization, trade related aspects, and how the implementation of these goals affect the business performance. It will seek to determine the costs and benefits of the Customs Union implementation. This will include the revenue implications of establishing a Common External Tariff and removing internal trade tariffs for the EAC trade.

Local manufactures of consumer goods are affected, as duties on majority of fast moving consumer goods drop. Goods in this category include cooking oils, tinned foods and electrical goods.[3] Though the Customs Union is relatively new in East Africa, only a few studies on its influence have been done.[4] This research therefore seeks to fill this gap by giving an insight of the EACCU on Kenyan firms in the edible oil sector.

## 1.3 Research Objectives

This study was guided by the following objectives;

- To evaluate the impact of regional integration on business performance in the East African region.
- To determine the influence of the East African Customs Union on the performance of selected firms in the edible oils industry.

[3] ***Daily nation business weekly,*** **January 2005**
**Friedrich ebert stiftung and collaborative centre for gender and development**

## 1.4 Research Questions

The study will be guided by the following research questions;

- What impact does regional integration have on business performance in the East African region?

- What is the influence of EACCU on the performance of firms in the edible oils industry?

## 1.5 Literature Review

This section contains an overview of general theories of regional integration, a few theories of economic integration and an overview of the industrialization and regional integration. It lays a background of the motivations for regional integration and the importance of this integration to development.

### 1.5.1 Theories on Regional Integration ,

The growth of regional trading blocs or regional integration agreements is one of the major international relations developments of recent years. Most industrial and developing countries in the world are members of one or more regional integration arrangements. Nearly sixty percent of world trade takes place within such agreements (World Bank). There have been attempts to revive dormant regional integration schemes, resurrect failed ones, reorganize and strengthen existing ones, and initiate new schemes where none existed.[5] This current resurgence of regional integration is both a

**P.Nying'uro, The EACs prospects on the global stage in** ***The making of a region:revival of the East*** **African Community (** ***institute for global dialogue Midr and South Africa 2005 )pg 30***

consequence of, and a reaction to, emerging trends in the global political and economic order.[6] Most regional trading blocs have one major objective of reducing barriers to trade between member countries. At their simplest they merely remove trade barriers and at their deepest they have the objective of Economic Union. The integration process may be based on various approaches. The market approach is achieved through liberalization by way of removal of tariff and non tariff barriers while production integration emphasizes coordination in planning and implementation of productive activities.

The ground theories of regional integration come from the field of International Relations. These looked at integration as a process. Later in the 1980s theories from comparative politics also aimed to explain integration though this was approached from the governance point of view. In the first part of this paper, certain theories of regional integration will be examined in terms of achievements and challenges, then focus on the EAC itself, while the second part will concentrate on the EAC Customs Union per se and how its existence has impacted business performance. The aim is not to exhaust or compare the theories but to provide a sense of direction that gives impetus to regional integration and its economic impact. These theories will help us understand why countries follow the path of regional integration and what benefits result from such unions. With integration comes the formation of a Customs Union which impacts basically all sectors of the economy.[7]

[10] **P.nyo'ngo, Regional integration in Africa:an unfinished business agenda. In nyo'ngo P.A (ed)** ***regional integration in Africa:unfinished*** **agenda 3-13**

[7] **Walt. W. Rostow,** ***The stages of economic growth :a non-communist manifesto,*** **Cambridge university press 1960**

Economists like Walt Rostow are proponents of the economic dimension of modernization theory. He argues that all countries evolve through the same stages of growth as leaders seek to transform backward agriculturally based societies into modern industrial economies.[8] Drawing upon the experience of the western industrialized countries, modernization theorists argued that African countries^ were at the starting point of a process that would mechanize agriculture and industrialize major urban areas. According to these theorists, the growth rate of a country's Gross National Product constitutes one of the best measures of the modernization process.[9]

The study of African politics and society has been dominated by a liberal tradition that envisions the development of free market democracies on the African continent similar to those found in the .western democracies of Canada, Europe, Japan and the United States. In the 1950s, liberal scholars assumed that African countries as well as developing countries in other regions of Third World such as Africa, Asia and Latin America would advance along the same path of political and economic development already traveled by their western counterparts. Subsequent decades clearly demonstrated however that political and economic development can proceed along many different paths each strewn with different obstacles and dead ends. The dramatic changes associated with the end of the cold war, most notably the spread of pro-democracy movements through out the African continent, have reinvigorated research within the liberal tradition, which continues to point to the western democratic tradition as the model to be emulated by

[8] **Walt. W. Rostow,** ***The stages of economic growth :a non-communist manifesto,*** **Cambridge university press 1960**

**Peter J Schraeder, African politics and society, a mosaic in transformation Loyola university Chicago 2000 pg 24** . •

African leaders. This theory was promoted by Africanists within the liberal tradition as the key to the development of the African continent.

From this discourse one can observe the richness of perspectives through which the process of integration has been analyzed. If we ask ourselves the question why countries integrate, the logical answer that comes to mind is that supranational organizations are better means of satisfying the individual country interests than each of them would satisfy on their own.

David Mitrany argued that the rise of regional economic integration is inspired by the belief that the conflict between states is reduced by creating a common interest in trade and economic collaboration amongst, members of the same geographic .region. Society will develop by our living it, not policing it and economic unification will build up the foundation for political agreement.[10] Africa has embraced this reasoning. It is the economic predicament facing Africa that explains increasing voices for regional integration as one way out of the muddle of underdevelopment. On June 3, 1991 at the 27th summit of the OAU in Abuja, Nigeria, 35 heads of state and government signed a treaty establishing the African economic community (AEC) with a timetable for the phased removal of barriers to inter-african trade. At this gathering it was agreed on the need to strengthen existing regional efforts towards African cooperation. To achieve these objectives, the AEC treaty intends among other things to strengthen existing regional economic communities establish other communities where they do not exist and

[10] **David Mitrany, A working peace system Chicago Quadrangle pg 22 and pg 54**

conclude agreements on the harmonization and coordination of policies between existing sub regional and regional economic communities.[11]

Ahmed Mohiddin [12]traces the East African efforts at integration and argues that economic integration is the road towards a federation that the region hopes to achieve. Economic integration however will be possible only in the context of involving all stakeholders including governments, the private sector and people of East Africa.

The removal of internal EAC trade tariffs will cost the country about USD58.7 million per year in potential revenue. Therefore the removal of internal tariffs for EAC may not be a serious problem for Kenya. The major concern for the country is the level of the common external tariff. Available data shows that the lower the levels of CET the higher the revenue loss for the country. But revenue loss should not be the only consideration as welfare gains or losses and impact on industrial development of members of the union are also important.[13] Most of the theoretical literature relates to static effects of the Customs Union(changes in terms of trade) while the dynamic effects (specialization, economies of scale and efficiency changes) are rarely dealt with as they are difficult to model. Due to the shortcomings of the standard trade theories and observed lack of progress in the integration process, some authors like Fine and Yeo(1997) suggest that the focus of regional integration in Africa should re-orient itself to the enhancement of economic growth through stable and sound macro economic policies and rapid accumulation of human and physical capital. They also argue in favour of focusing on cooperation in

[1] **Nyirabu Mohabe, *The new east African communit;the challenges ahead,* The African review vol 29 no 1&2 2002**
[12] **Ahmed Mohiddin, <u>Deeepening political integration in the east African community,</u> in *deepening regional integration* by DPMF 2005 pg3**
**Ibid pg viii**

infrastructure and natural resources development. This is because the requirements for making reasonably complete forms of regional integration work are more demanding. The biggest challenge in understanding the successes and or failures of RI in Africa perhaps is the analysis of benefits and costs. The empirical evidence is scanty and is based mostly on simple descriptive intra-regional trade statistics.[14] Given these kinds of arguments, the researcher finds impetus to carry out the study in order to add on to the body of knowledge that exists on the effects of integration in Africa. The data itself can be used by policy makers in determining whether the road towards integration is of benefit to the partner states.

The major destinations for Kenya's exports are Europe at 33 percent and East Africa at 28 percent. Trade, with COMESA countries excluding East African states constitutes about 14 percent and shows an increasing trend. The European Union is the major source of imports for Kenya followed by Middle East. Kenya's imports from EAC are about one percent of the total imports and comprise mainly' agricultural products. Research has shown that there is potential to expand trade within the East African states.[15] This research will seek to confirm if the Kenyan perspective on an EAC Customs union is favourable.

Dominic Salvatore[16] argues that many developing countries have seen the infant industry argument as a compelling reason to provide special support for the development of manufacturing industries. In principle such support could be providing subsidies to

**[4] Nehemiah Ngeno, Hezron Nyangito, Moses Ikiara, Eric Ronge, Justus Myamunga Regional integration study of East Africa; the case of Kenya KIPPRA WP/09/2003 Pg 9**

**|6 KIPPRA *Regional integration study of east Africa :the case of Kenya,* working paper no 9 2003 pgvii.**
**Dominic Salvatore International Economics Pg355**

manufacturing production in general or they could focus their efforts on subsidies for the export of some manufactured goods in which they believe they can develop a comparative advantage. He continues to argue that each nation ought to specialize in production of commodities of its comparative advantage. Each nation will then share the gain of cross border trade. He is however conscious of the fact that developing nations now demand changes in the pattern of trade to take consideration of their special development needs.

In most developing countries however, the basic strategy of industrialization has been to develop industries oriented toward the domestic market by using trade restrictions such as tariffs and quotas to encourage the replacement of imported manufacture by domestic products. The strategy of encouraging domestic industry by limiting import of manufactured goods is known as the strategy of import substitution industrialization.[17] This is in line with the ideals of the Customs Union.

### 1.5.2 Economic Theories of Integration

In the economic literature, integration theory is almost synonymous of theory of customs unions. In this the issue that is particularly important is the distinction between trade creation and trade diversion introduced by Viner (1950) in his classical book "The Custom Union Issue." This is an approach to customs unions that basically considered their static effects, in the sense that it is related to gains and losses incurred by the establishment of a preferential trade agreement. Briefly, trade creation occurs when trade between the customs union's partners is increased. In this case, expensive and protected domestic production is displaced by cheaper production coming from the partners'

**Paul R Krugman** ***International Economics, theory and policy,*** **pg 247**

countries. This shift would imply a move from less efficient to more efficient producers. By contrast, trade diversion would occur when imports from the efficient, or cheaper, "world market" producers are replaced with imports from a higher cost or less efficient producers from the customs union[18]. To explain trade creation and trade diversion, economists assumes the existence of variables such as perfect competition in both the commodity and factor markets, automatic full employment of all resources, costless adjustment procedures, perfect factor mobility nationally, perfect immobility across national boundaries and prices determined by costs. It is also assumed that the supply from the producers in the rest of the world is fully elastic at price level[19]. The consequences of creating a custom union will differ depending on whether the initial situation was protectionism or free trade. If protection was the initial situation of country A, a new trade flow would occur between partners originating a trade creation effect. By contrast, if free trade was the initial situation of country A, a negative development will occur. There would be then, a reduction of trade on the producer side and on the consumer side. Additionally, trade would be diverted from the lower-cost world producer to the high-cost partner country. This is the trade diversion effect.

In short, Viner concluded that customs unions do not always enhance welfare. They can promote trade creation, by eliminating obstacles to free trade among member countries[20]. As a result, the world welfare would increase. However, if they lead to take trade away

[18] **Jacob, Viner (1950) The Customs Union Issue, New York: Carnegie Endowment for Peace:**

**El-Agraa, Ali (1989) The Theory and Measurement of Economic Integration, London: McMillan-St. Martin's: pp 13**

[20] **Jacob, Viner (1950) The Customs Union Issue, New York: Carnegie Endowment for Peace.**

from efficient outside suppliers and giving it to inefficient member countries, they would be "trade diverting" integration schemes. Welfare would diminish in this sort of customs unions. As states are assumed to be utility maximisers intending to enhance their economic welfare, then, integration would aim to expand trade exchange. In other words, states should promote "trade creating" customs unions. Thus, by examining the edible oils sub sector, the researcher aims to confirm if there has been trade creation or otherwise.

Another approach to customs union is proposed by specialists such as Cooper, Massel and Jonhson. They stated that the main objective of integration is not furthering of trade and welfare but the creation of conditions for the provision of public goods. Consequently, research about customs unions should evaluate the extent to which these latter could be an instrument to promote policies such as industrialisation, economies of scale and stabilisation and strategic policies in an area or jurisdiction smaller than the world and larger than states. Cooper and Massel (1965), argued that regional integration motivation was not for the searching for an optimal allocation of the economic activity or the promotion of welfare, as Viner asserted. This is because empirical evidence demonstrated that unilateral trade liberalisation is a better mechanism to fulfil these above mentioned goals than customs union. In consequence, there should be other reasons leading states to further economic regionalism and the study of tariff protection would be the main point to explain it. Thus, the promotion of customs unions is conceived as a deliberate employment of tariff policy by one or more states in order to achieve objectives which cannot be attained by individual action[21].

Jonhson (1965) argues that the decision to further customs union could be explained by the interest of states in promoting "public goods". He proposes a new approach to the customs union issue that was based upon the following assumptions: (a) governments use tariffs to achieve certain non-economic objectives; (b) actions taken by the governments are aimed at offsetting differences between private and social costs, consequently, they are rational efforts (c) governments policy is a rational response to the demands of the electorate; and (d) countries have a preference for industrial production." Johnson's analysis also distinguishes between private and public consumption, real income and real product. Consumption is understood as the sum of planned consumption expenditure and planned investment expenditure. Real income is defined as the utility enjoyed from both public and private consumption.[22]

Finally, real product is conceived as the total production of privately appropriable goods and services. According to Johnson, competition among political parties can lead governments taking policies in order to maximise consumer satisfaction of private and public goods. This is achieved when the rate of satisfaction per unit of resources is the same for both types of consumption goods. Additionally, Johnson assumed a "collective preference" for industrial production. This implies that consumers are willing to expand

**21 Looper C. A. and B. Massel (1965) "Towards a General Theory of Customs Unions for Developing Countries", Journal of Political Economy, 73, pp. 461-476.**

**22 ibid**

industrial production (and industrial employment) beyond what it would be under free trade". This industrial promotion policy is basically financed through tariffs but, on the one side, General Agreement of Tariffs and Trade regulations rule out exports subsidies and, on the other hand, internal political considerations make tariffs the usual instruments of protection. Then, the creation of customs union is seen a mechanism to stimulate investment and promote competition in the industrial sector as well as a way of capturing economies of scale. Customs unions are created basically to protect the collective preference for industrial protection, promote the expansion of industrial sector and improve its efficiency. Accordingly, Johnson regards custom unions as a mean of capturing economies of scale, stimulating investments and promoting competition in the industrial sector. In addition, customs unions could help states in achieving other collective objectives such as the improvement of their term of trade vis-a-vis the rest of the world or the improvement of the bargaining power vis-a-vis larger countries[23].

A very significant debate about the relevance of these traditional theories for explaining integration among Third World countries (south- south integration) took place during the 1960s and 1970s. In short, most of specialists believed that traditional concepts of trade creation and trade diversion were not applicable to customs unions among developing countries. Economic integration would unlikely produce trade creation but likely will generate trade diversion. As Lipsey demonstrated, trade diversion was not necessarily negative and developing countries could benefits from it. Arguably, trade diversion was a

**Johnson, Harry (1965) "An Economic Theory of Protectionism, Tariff Bargaining and the Formation of Customs Union", Journal of Political Economy, 73, pp. 253-283.**

mean to expand production by furthering import substitution on a regional scale. As Under asserted, "to the extent that it consists of diverting the importation of non-inputs goods away from advanced industrial countries, trade diversion is almost the very essence of customs union postulate [among developing countries]. It enables the concentration of scarce foreign trade on inputs imports, thereby enhancing capacity use and growth"[24].

Other specialist such as Axline, considered that one of the most salience consequences of integration among developing countries is the reduction of the degree of dependence on the rest of the world. Integration intends broadening regional market and reducing regional dependence on trade with outside of the world. Similarly, it restrictions on foreign investment and transfer of technology on regional basis must be included in the integration schemes[25]. Again, this applies well to the EAC case because the partner states are developing states and most of the integration efforts are aimed at increasing the regional markets and enhance the industrialization efforts.

### 1.5.3 Overview-Industrialization and Regional Integration

With regional integration comes many opportunities and threats to companies in the region. The ultimate goal of any organization is to maximize on profits while remaining cost effective. Organizations are geared towards gaining competitive advantage in the

[24] **Under Stafan Burenstam(1972) "Uniones Aduaneras y Desarollo Econ6mico", en Wionczek, Miguel(ed), *Integration Economica de America Latina. Problemas y Perspectivas,* Mexico: Fondo de Cultura Econ6-mica, pp. 23.**

**Andrew, W. Axline (1977) "Underdevelopment, Dependence and Integration: The Politics- of Regionalism in the Third World", International Organization, 31:1, Winter, pp. 87.**

industry they are operating in and with regional integration, they seek opportunities to expand their operations and hence their revenues. Highly successful business groups are very aggressive through their customer driven and market driven strategies in creating big markets for their products/services in the region. Therefore, performance in firms may be attributed to the overall organizational competitiveness in an industry and how it blends its strengths with the opportunities provided by the integration.[26] Kenya's domestic production of edible oils is estimated at 380,000 tonnes. Kenya exports mainly to the East African Community and COMESA region as well as Europe and it is ranked as 15 world wide in export of vegetable fats and oils in their fractions. EACCU therefore provides Kenyan firms with more markets for their products.

The benefits of regional integration include scale effects and competition, improved terms of trade and its effects on foreign direct investment, location and trade effects. Jones "also argues that the goal of an organization is to minimize its dependence on other organizations for the supply of scarce resources in its environment and find easy to influence them in order to make resources available. For instance intense competition within a bloc has potential of inducing non-member countries to reduce prices of exports to the bloc and improve terms of trade within the bloc. Regional integration has costs associated with it such as the loss of national sovereignty, creation of internal tensions and resentments where unfair distribution of integration benefits and costs results.

26
27 **Aravindan P, *Team engineering and world class management(Whee\er* publishing, New Delhi, 1997)**
**Jones G R Organization theory, design, and change 4th edition New Jersey: Prentice Hall 1969**

Whether regional integration improves or worsens the intra regional trade depends on the characteristics of the member countries and the design and style of the integration.[28]

## 1.6 Justification

This part provides the justification of the research project. It provides both academic and policy justification.

### 1.6.1 Academic Justification

The east African customs union has been in existence for less than five years. In this regard, very few studies have been carried on the effect of this union on the overall economic performance of the member countries. In the inception of this union, many scholars and policy makers speculated on the effect of this union on East African countries and their industries and citizens. This form of union is the first in Africa and it needs to be studied to establish whether it is workable and if it can be taken a step further as the members have indicated. There can be underlying effects that cannot be evident without an industry by industry study. This study therefore investigated the effect of the union on firms in the edible oils industry to find out whether they have benefited. This area therefore needs more research to add up to the limited body of knowledge on the subject. To the academic community, it also forms a basis for further research especially so because there are still various effects of the Customs Union that stakeholders are yet to comprehend.

**Andrew Mullei, Steering East Africa towards a Customs Union:suggestions from pilot study(African center for economic growth and USAID,2002)**

### 1.6.2 Policy Justification

From the literature review, it is apparent that there is literature dealing with issues related to effects of the EACCU on various sectors of the economy. However, not all areas have been explored as the Customs Union has only been in effect for less than five years. The fact of regional integration clearly influences the way business is carried out across the borders and this study attempts to capture this. An increase in investment is crucial to the attainment of sustained growth and development in the region. This requires mobilization of both domestic and international financial resources. As Stiglitz notes, in this era of globalization, the problem is not with globalization but with how it is managed. It has brought huge benefits such as opportunities for trade as is seen in the integrated region [90] and increased market access. The transport operators are influenced by such factors as locational advantage, total population, proximity to financial centers and institutional factors such as good governance and reduced bureaucracy. In addition, regional integration entails creation of an enabling envirohment, the strengthening of various institutions of governance and the empowerment of the various agencies of the civil society, the communities, the private sector and the people at large.[30]

The findings of this study will be important to policy makers in all the member countries. The government through the ministry of trade and the ministry of East Africa Cooperation will have a basis for knowing the influence of the EACCU on economic development and can form a basis for doing comparative analysis on other sectors of the

30 **•'•Stiglitz, Globalization and its discontents op cit pg214**

A.**Mohiddin,** ***Introduction:deepening political integration in the east Africa community*** **(DPMF2005) pg** economy. Likewise, to the East African Community, it will increase the need for an efficient and effective system that will serve the people of the region.

### 1.7 Hypotheses

- Regional integration and specifically creation of a Customs Union increases the opportunity for growth in the manufacturing industry

- East African customs union helps the East African countries to compete in the global market.

- The Customs Union is negatively associated with the growth of manufacturing industry in Kenya.

- The customs union has made companies in the edible oil industry more competitive.

### 1.8 Methodology

The study relied on both primary and secondary sources of data. Secondary data was obtained from analysis and review of books, journals, papers and unpublished works. Government documents such as Sessional papers and policy documents were reviewed. Primary data was obtained from interviews and other company documents. This was done through convenience sampling to select the population. Data was collected through semi-structured questionnaires administered through email or hand delivery to managers 2nd policy makers. The questionnaire focused on the company demographics, its performance before and after the implementation of the customs union, any strategic decisions made as a result of the EACCU, challenges faced and any recommendations the respondents may have. Quantitative analysis was used to determine the influence of the East Africa Customs Union on the transport sector. The responses of the respondents were used to make inferences on the effects mentioned. In order to obtain the relevant primary data, questions were formulated for the study in line with the manner in which the variables were operationalized.

The questions were administered to various managers in the firms. This was by way of semi-structured questionnaires sent via email and hand delivered to the respondents. The respondents were senior managers who are involved in the policy making process such as general manager and Chief Executive Officers and also middle level managers who are policy implementers such as sales and marketing managers and export managers. The questionnaire contained the three sections as follows; the first section contained the company demographics such as the company name, title of respondent, nature of ownership and number of employees. The second section was seeking to unveil the performance of the company before and after the entry into force of the customs union. Section three looked at the levels of satisfaction and challenges the company faced during the implementation of the Customs Union as well as recommendations from the respondents. Secondary data was collected through consultation of relevant books, websites, journals, magazines, newspapers and statistical abstracts.The data was analyzed through content/ qualitative analysis. Content analysis is any technique for making inferences by objectively and systematically identifying specified characteristics of responses.

## 1.9 Significance of the Study

The study will be of significance to the East African countries, companies in these countries and also residents in these countries. To the countries, the study will provide effects of policies, laws and declarations of the EACCU on business performance and economic advancement hence will be a basis for future decisions regarding economic integration in the region. The study also will provide policy makers in these three countries with consequences of the actions they make regarding the union and its effect on economic condition of the region. This will make them more informed and better policy makers in the future. The study will also prove to be important to companies in the region since they will be aware of benefits and risks emanating from the union and they therefore can better place themselves to take advantage of the benefits and cushion themselves from the risks.

## 1.10 Organisation of the Project

The project is organized into six chapters. Chapter one looks at the introduction of the project. It discusses and outlines the research problem at hand. It then outlines the research objectives, research questions, significance and organisation of the study. Chapter Two looks at the literature review. The chapter discusses the various publications discussing regional integration and its impact on firms.

Chapter Three explains and justifies the research design and methodology. The research design, target population, sample and sampling technique, research instruments, validity, reliability, data collection procedures and techniques of the study are explained.

Chapter Four discusses the research findings. It presents how data from the study was analysed and the presentation of the findings. Chapter Five includes a critical analysis whereas chapter six includes the conclusion and recommendations for the project.

# CHAPTER 2: NATURE AND IMPACT OF REGIONAL INTEGRATION

## 2.1 Overview

This chapter will provide a critical assessment of the latest attempt at regional integration first in Africa and then in East Africa. Starting from different intellectual perspectives, the arguments provide robust perspectives on the architecture of the new EAC and its prospects of moving the region towards greater participation in the global economy. The aim is to enhance understanding of the complex relations at crafting economic blocs at regional and continental levels as states strive to remain relevant in the process of globalization.

## 2.2 The Concept of Regional Integration

Regional Integration (RI) refers to the process of creation or enlargement of regional arrangements of cooperation and the efforts of nations to connect or reconnect themselves to an organization spearheading the cooperation. It-is an arrangement in which three or more countries with common interests come together to achieve those interests as opposed to the respective national interests. Regional integration involves political and economic aspects. It's worth noting that the new processes of economic integration are predicated on the assumption that engagement with the global economy is unavoidable. They do not seek to 'de-link' their participants from the global economy, but rather to engage with globalization in ways that benefit the weak and the poor. Because of this, it is commonly assumed that successful engagement with the global economy must be state driven, but occur via the market; in other words, these integration exercises must be aimed at governing markets at regional levels.[31]

**Institute for global dialogue, The making of a region: Rrevival of the East Africa Commnunity pg18**

The number and proportion of international regional institutions has been increasing in the opinion of Jean Rey, "the political life of the world is becoming less at the level of national states and more at the level of continents". Has world politics become increasingly "regionalized"?. The evidence is varied and different types of behaviour point in different directions. On the one hand, those who see a trend toward regionalism cite the fact that non-regional organizations like the Commonwealth which once represented the paragon of effective international organization have undergone a decline.[32] Intra- Commonwealth trade in 1967 was roughly a quarter of the total trade of member countries, but the figure has declined steadily and even the report of the Common Wealth secretariat refers to "the drive towards regional economic emphasis" among its members.[33] At the same time, the countries of the European Community more than tripled their intra-regional trade in the first decade. This striking success caused other countries to try to imitate it. Indeed RI efforts in Africa are modeled after the European Union and therefore if the EU countries have reaped the benefits of integration, the same would be expected of the East African region and this study will confirm the same. If this is not the case , then it will give more understanding on what needs to be done. In addition, not only has the number and proportion of new intergovernmental organizations increased but what is probably a more accurate indicator of transactions, the same has been true for non-governmental organizations. From 1957 to 1963, international organizations of the regional type increased some five times as rapidly as

**The Commonwealth stands today as a foremost example of international cooperation Daniel S Cheever and H.Field Haviland, *Organizing for peace,* Boston 1954**

**Commonwealth secretatiat, second report of the commonwealth secretary general, London 1968, pg3**

non-governmental organizations.[34] Turning to international trade, geography remains an important determinant[35], and there have been dramatic increases in trade among members of regional organizations. Again we find that this gives impetus to the study in order to determine whether there has been increased trade between the member states. The edible oils sector provides products to consumers across borders and thus provides a perfect sample of the study. Steven Brams and Bruce Russett have made systematic efforts to map the pattern of transactions in the international system.

Looking at exchange of diplomatic personnel, trade, and shared membership in inter governmental organizations in the early 1960's Brams found that "geographical proximity seemed to be the dominant influence in the structuring of most of the sub-groups". However, bearing out our suspicions, he found that neither diplomatic exchanges nor trade showed as clear a regional principle as was apparent in the memberships in international organizations.[36]

Russet factor analysed socioeconomic homogeneity, UN voting patterns, trade shared memberships and geographical proximity among states in the 19510s and 1960s, Russett and Lamb found that most groupings were regionally based but three of their nine factors were non- regionally labeled. Joseph Nye asks the question, if there does not seem to be strong trend toward or away from regional systems as the dominant set of interdependence, how then do we explain the increase in the number and proportion of regional institutions? What incentives are there for elites and statesmen to use them?

**Robert Angell, The growth of transnational participation, the journal of social issues XXIII, January 1%7,pg 125**

**36 See Hans Linneman, an econometric study of international trade flows, Amsterdam 1966**

**Steven Broms, transactions flows in the international system, American political science review LX,December 1966,pg889**

Regional organizations like all international organizations have derivative uses as well as declared ones. They may for instance serve a number of diplomatic purposes where states communicate the administrative actions of regional organizations are among the many means available for communicating to foreign populations. Economic regional organizations can also be part of the same diplomatic use. Control of Germany was a major derivative function of ECSC. Charles De Gaulle tried to use the EEC as a means to press his economic partners toward a French conception of a European foreign policy.[37]

International integration may be seen as a dynamic process involving emerging communities, functional and treaty relationships and organs that range along an ideal continuum from more or less sporadic connections between sovereign states under international law .to federal and unitary supranational institutions governed by constitutional law. To the extent that it is deliberate, integration represents a manipulative approach to order, security and welfare. Nations may be pulled together among other things by an active sense of larger community 'needs of interdependence and the anticipation of advantages flowing from a more inclusive union.

Etzioni argues that integration proceeds along rather definitive paths rather than by trial and error. He treats integration as the terminal condition not as process of getting there. Phillip Jacob and Henry Teune regard integration both as a process and as a terminal condition while Karl Deutsche speak of integration as process leading to the creation of security communities.[38] Etzioni argues that these definitions are too well known to

**Jg Lyndon Johnson, department of state bulletin, September 26, 1966, pg 453**
**oseph Nye, *Comparative regional integration:concept and measurement*, International organization Autumn 1968, vol 22 no.4 pp856-858**

require extensive recapitulation.[39] The study of regionalism or regional cooperation or regional organizations furnishes simply materials on important activities of actors or on their beliefs. The study of regional integration is concerned with the outcomes of such activities in terms of a 'new deal' for the region in question even though these activities could of course be analysed for other purposes as well. Economists who have studied integration have tended right from the outset to be sensitive to the repercussions of regional integration on world trade and total welfare.[40] The internal consequences of integration for patterns of consumption and competition have also been matters of concern for economists.[41]

Stuart Scheingold focuses on consequences of integration in the European Commission. The first is to consider the results of integration in terms of the original incentives for creating a region. For instance, the integrative process of the EC was expected to alter dramatically the relationships between the nation states of Europe, transform faltering economic systems and even change continental lifestyles. It has been associated with peace, economic growth and an apparent Americanization of lifestyle. There is also a second set of questions which directs our attention to a range of distributional issues, transcending the original aspirations of founders of regional integration. How is integration affecting the distribution of influence and material well-being among the peoples of the European communities and what is its impact on other regions of the

**Amitai Etzioni, *political unifications: a comparative study of leaders and forces,* New York:Holt Rinehart and Winston 195 Chap 1 the process of political unification**

**See example one of the standard works:bela balassa, the theory of economic integration, Homewood III Richard D Irwin 1961, Chap 1**

**This was probably first explored by Tibor Scitovsky economic theory and western European integration, Stanford California:Stanford university press 1958**

world?.[42] One must thus think of the purpose to be served by integration on two rather distinct levels. Most obviously and directly integration was to be an agent of economic reconstruction and a vehicle for creating among the member states permanent institutional ties. At another level integration was related to a general social theory which saw productivity and affluence as a kind of universal problem solvent. There is considerable dispute about the contribution of integration, if any to either of these objectives.

Lawrence Krauses carried out actual measurement of the impact of integration on the income levels of the member states, Krause concluded that the income of the member countries has been stimulated by integration.[43] He calculated the increment with precision, determined the portion attributable to increases in efficiency and investment and supported his findings with reasoned argument. The regional development literature in the 1980s reflects the main features of what has been called 'the new comparative political economy'. Development paths are viewed ds historically contingent, and there is an emphasis on the role of external as well as institutional factors in shaping domestic development outcomes. There has been resurgence in the political impact of neo-classical economics in the third world during the 1980s. this perspective has been closely associated with the world bank and its sister institution the IMF which often condition their lending decisions on the willingness of developing nations to conform to neoclassical economic policies and related institutional changes. The neoclassical framework advocates laissez-faire trade policies like low tariffs, few import controls and

42 q
**aee angus maddison, economic growth in the westxomparative experience in europe and north America, New York** 20th **century fund** 1964, **pg** 37
**Lawrence Krause, European economic integration and the united states, Washington, brookings** institution 1968, pg73

no export subsidies a free labour market and a limited non interventionist role for government in the economy. Neo classical economists also tend to defend traditional notions of comparative advantage in which resource-rich third world countries are encouraged to concentrate on exports of raw materials and labor intensive manufacturers and to abandon attempts to promote advanced industrialization through industrial policies that seek to improve a country's position in the existing international division of labor.

The espousal of neoclassical economists by international financial organizations like the World Bank and IMF is particularly significant because they have the policy networks to diffuse their message to a wide range of countries and the economic resources to make their opinions matter.[44] Latin America south and East Asia as well as sub-Saharan Africa are frequently grouped together under the third world label though they have different economic and social indicators of development. In terms of the level and rate of growth of GNP per capita, East Asia has outdistanced the other regions. In 1989, it had GNP per capita of USD 1950, while sub-Saharan Africa was at USD340. Since then, there has been dramatic reversals of fortune in some Latin America and African countries like Tanzania having their per capita income drop more than 50 percent and Kenya's by almost 20 percent.[45]

The sub-Saharan Africa and South Asian economies place far more emphasis on agriculture and extractive industries while manufacturing has been the cornerstone of development for the East Asian and Latin American newly industrializing countries. The manufacturing sectors share of GDP in the newly industrializing countries in 1989 ranged

**Gary Gereffi and Stephanie Fonda, Regional paths of development;artnual review of sociology, Vol - 18,1992 pg.419-448**

**World bank 1982:1983, 1991**

from 23 percent(Mexico) to 36 percent(Taiwan) which is well above the level of the united states and in several cases its even above Japans manufacturing /GDP ratio of 30 percent.(World bank 1991:209). By 1989 the East Asian countries had clearly established themselves as the third worlds premier exporters, especially of manufacturers. Taiwan and South Korea topped the list with USD66.5 and USD62.3 BN in exports, respectively followed by China USD52.5BN and Brazil USD34.4BN. Manufactured products constituted over 90 percent of total exports in the East Asian newly industrializing countries and around 70 percent of China and Indias exports.

For the Latin American nations manufacturers are only about one half to one third of total exports while in sub-Saharan Africa manufacturers are just above 10 percent of the exports total. The.maturity or sophistication of a country's industrial structure can be measured by the complexity of the products it exports. Here again, the East Asian newly industrializing countries are the most advanced. Machinery and transport equipment which utilize capital-and skill -intensive technology, account for well over one third of their overseas sales. In Mexico and Brazil this sector represents one fifth to one fourth of total exports.

## 2.3 The imperatives of integration

Mwesiga Baregu[46] argues that there are at least four types of rationales or imperatives that lie behind the formation and sustenance of regional integration. They are affection, gain, threat and power. Imperatives in this case mean the kinds of factors that create the

**. ^wesiga Baregu,, 2005, "The African Economic Community and the EAC: Any Lesson from the EH?" ,Julu, A-> (ed), *The Making of a Region: The Revival of the East African Community,* Midrand, South Institute for Global Dialogue.**

impetus and give rise to the drive and yearning for integration among the members. They may belong to the domain of choice or to the domain of necessity. The more the imperative impinges upon ones vision, the more it is likely to belong to necessity rather than choice. This is according to the perceptions of those involved in envisioning their future. These visions are usually expressed in the preambles of the treaties establishing the integration schemes. The affection imperative is essentially emotive. It refers to a situation where countries come into an integration arrangement because they have a lot in common and feel some bonds of affection. For instance the East African countries are connected by a common language, a common colonial heritage and cross border affinities among different ethnic groups hence regional integration should automatically follow. But affection does not seem to be a strong imperative as it could not stop the collapse of the original EAC (EAC 1977). Gain is by far the most celebrated imperative held responsible not only for the initiation but also the sustenance of regional integration.

Gain and loss are the central tenets of rational choice theory, which contends that states tend to behave in a manner which maximizes their gains while minimizing their losses. Regional integration theories including Jacob Viners concerns with trade creation and trade diversion have largely been preoccupied with economic welfare gains from trade within bloc or without. The unequal distribution of gains among members of a bloc is also held to be a vital source of potential discontent except perhaps if the cost of non-integration is perceived to be too high. The shared perception of threat and the quest for collective security and protection is perhaps the strongest incentive toward integration. This may arise from two distinct situations. One is where two or more countries find themselves locked in a mutually threatening relationship and have to reach some compromise leading to a peaceful coexistence as happened between France and Germany in formation of ECSC. The other is when there exists a perception of a common external threat in which case the countries come closer to enhance their capacity to defend themselves as happened in the formation of NATO against perceived threat from Soviet Union. Power as an imperative refers to the situation where a regional hegemon forces the neighborhood into integration arrangement.

Hegemonic integration involves not only the existence of a relatively more powerful country in the region but also the capacity and inclination on the part of that country to meet the costs of hegemony by offering incentives for members to stay and imposing sanctions on those that may want to break away. The NAFTA bloc for example is essentially maintained by the United States. This is unlikely to work in East African setting because there is hardly a country that could be considered a viable hegemon that is able to muster the resources to pay costs of maintaining a stable hegemonic arrangement.[47]

## 2.4 Efforts at Regional Integration in Africa

Free trade leads to the most efficient utilization of world resources and thus maximizes world output and welfare. Prior to 1950, it was widely believed that any movement towards freer trade would also increase welfare. To the extent that a Customs Union does not increase trade barriers against the rest of the world, the elimination of trade barriers among union members represents a movement toward freer trade. As such, it was

**Baregu M, Economic and military security. In Baregu M and Landsberg C(eds)** ***from cape to Congo:southern africas evolving security challenges,*** **and** ***the African economic community and the EAC.any lessons learnt.*** **Boulder and London:Lynne Rienner 2002**

believed to increase the welfare of member and non-member nations alike. However, Viner[48] showed that the formation of Customs Union could increase or reduce the welfare of member nations and of the rest of the world depending on the circumstances under which it takes place. This is an example of the theory of the second best; which states that if all the conditions required to maximize welfare or reach Pareto optimum cannot be satisfied, trying to satisfy as many of these conditions as possible does not necessarily produce the second best welfare positing. This somewhat startling conclusion has great significance not only for the field of international economics from which it originated, but for the study of economics in general. This theory of Customs Union is just one example from international trade of this general principle.[49].'

The intellectual lineage of functionalist thinking on international economic relations may be traced to the classical liberal economic philosophers of the 19th century who held that trade was fundamentally contrary to war, that whereas political rivalry inflamed the passions, trade pacified. This was essentially a rationalist doctrine under which Raymond Aaron has pointed out' a universal republic of exchanges' was assumed to exist.[50] Ever since the 1700s, liberals have held that mutual economic dependence between countries will promote cooperation rather than conflict.[51] Writing at the end of the 18th century, Immanuel Kant explained how mutual economic dependence promotes cooperation instead of conflict. In the 1800s, the Manchester School, with David Ricardo, Jeremy Bantham, and Richard Cogden among others, also argued that mutual trade and contact

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49 **David Mitrany, *Aworking peace system,* Chicago Quadrangle books, 1966 p.97**
jo **Goldstein Joshua, *International relations* 4th ed (New York:Longman 2000)p.382**
5| **Raymond Aron, *Peace and war,* Weidenfeld and Nicholson London 1966 p245-252**
**Montesquieu Charles de, *The spirit of laws* Transalted by T. Nugent(New York :Hafner 1759/1949)p3**

provide a stimulus for cooperative solutions.[52] Liberalism holds that states are not the only actors on the international plane but individuals, non-governmental organizations, civil society among others also influences the operations in the international sphere.[53] This assumption is in line with this study since it incorporates the role of the business community in their operations under the customs union as well as the role of individuals in accepting the federation. The ultimate expression of integration would be the merger of several states into a single state-ultimately into a single world government. The most successful example of the process by far is the European Union.

**2.5 Regional Path to Development**

Since independence, sub-Saharan Africa's development trajectory has been characterized by two main transitions from expansion to contraction in economic performance and from optimism to pessimism in political analyses.[54] These economic and political trends clearly pose special challenges.

First, the sub Saharan African economy is less stable than the other regions of the third world, a condition that is exacerbated by drought and global recession. Second, the cultures, geography, and political systems of sub Saharan Africa's 51 countries and territories are exceptionally diverse, making it difficult to generalize about the problems of this region and the policies suitable to change them. Nonetheless, there is strong consensus about one topic: African agriculture is suffering. Agricultural production is no longer able to keep pace with population growth, so an increasing number of Africans do

" **Blainey Geoffrey,** ***The causes of*** **war.(London:Macmillan, 1973)p.8**
**Joshua Goldstein op cit p.65**
**Shaw TM** ***Reformism and revisionism in african political economy in thel990s,*** **pres.int.stud.assoc.annu.meet Vancouver Canada 1991**

not have access to adequate food resources.[55] The reasons for low agricultural productivity are interrelated. Poor soils, unstable climatic conditions, and inadequate farming techniques to deal with these conditions are a few of the obvious internal constraints on agricultural output.[56] However these internal limitations do not receive the critical attention they require because of the greater priority given by public officials to foreign exchange controls, reduction of inflation and import substitution investments.

The majority of African industries use minimal technology. These include final-stage manufacturing like automobile assembly in Tanzania and Nigeria as well as labor intensive industries like textiles and leather. When more advanced technology is required, it is imported thus further retarding African technological development.[57] This limits the creation of indigenous backward and forward linkages and increases the vulnerability of African industries to technological changes in competing regions.[58] There is skepticism about whether the strategies pursued by African industrialists are capable of fostering economic growth at all.[59] After independence the majority of capital was invested in agricultural and extractive export commodities. Limited attempts at import substituting industrialization were made but this strategy was less successful in Africa than in East Asia or Latin America because the domestic demand for mass produced commodities was

56 **Berry S *The food crisis and agrarian change in Africa: a review essay,* African study rev 27(2):59-l 12**
**Richards P, Farming systems and agrarian change in west africa ,prog.hum.geogr 7(1): 1-39**
**^ Leys C African economic development in theory and practice Daedalus 3:99-124, 1982**
**Mytelka LK, Stimulating effective technology transfer:the case of textiles in Africa, In *international technology transfer concepts, measures and comparisons* ed N.Rosenberg, C Frischtak New York Praeger ^77-125**
**oeveridge A Oberschall A *African businessmen and development in Zambia* ,Princeton NJ Princeton University Press, 1979**

too small and the scarcity of indigenous sources of technology made it necessary to import most gods.[60]

Mytelka claims that import substitution was never actually pursued in Africa. Instead, 'import reproduction' was the primary strategy. Import reproduction strategies are those that 'ignore the extent to which products incorporate concepts of functionality, cost, quality, and aesthetics that correspond to the producers principle market sale'. In other words, import reproduction fails to address the needs of the intended market so that African industrialization was only superficially inward oriented. As a result, import reproduction in Africa was exhausted by mid 1970s while import substitution continued to bolster economies in other regions of the third world. Industrialization in Africa has largely been funded by agricultural exports and foreign capital.

Agricultural exports have not been sufficient to sustain industrialization owing to worsening terms of trade and declining productivity. This left foreign aid and direct investments by multinational corporations as the primary sources of development capital. Multinational corporations in particular have maintained control over industries through management, technological input, and investments even after the 1967 period of indigenization in countries such as Nigeria, Kenya Tanzania and Zaire. Further more the fact that the major economic agents of sub-Saharan African development were foreign capitalists and donors is an important reason why the African economy dramatically worsened in the 1970s and early 1980s with the decline of foreign aid and foreign direct

**Ollawa P The political economy of development: a theoretical reconsideration of some unresolved issues, African studies rev. 26(1): 125-55**

investment.[61] The influence of foreign capital in parts of sub Sahara Africa has fostered the emergence of predatory capitalism brokered by corrupt states, as exemplified by the cases of Zaire, Uganda, and Sudan. According to Evans , 'predatory' capitalism exists when 'the preoccupation of the political class with rent seeking has turned the rest of society into 'prey'.[63] Consequently, the development of a class capable of investing in long term capitalist enterprises is inhibited. Economic development in sub Saharan Africa over the past 20 years has lagged behind that of other regions of the third world.

Worsening social development has coincided with poor economic performance. Sub Saharan Africa has the lowest life expectancy, the highest rate of infant mortality and the rate of illiteracy of the four regions examined here. In addition, Africa's infrastructure has been neglected throughout the past 30 years, creating a disincentive for further investment by foreign capital. Rapid population growth and over crowding in the cities place excess demands on agriculture and the underdeveloped industrial sector. Finally, the unequal distribution of wealth, disparate wages 'among African laborers and Africa's long history of poverty are inimical to the growth of healthy domestic markets. It appears that sub Saharan Africa is in a situation of long term decline for which contemporary theories of development have few if any answers.

### 2.5.1 The Motivation for East Africa Region Integration

Despite the sound economic arguments for free international trade, all countries impose quantitative and tariff restrictions on imports. Trade restrictions are also increasingly

^ **Mytelka L K The unfulfilled promise of african industrialization african stud, rev.32(3):77-137**
**Evans PB,** ***Predatory developmental and other apparatuses a comparative political economic perspective on the third world state*** **socio.forum** 4:561-87
**Ibid** pp 570

being introduced by groups of countries that have entered into regional integration agreements. These have become very important features of international trade in recent years. Since the 1940s, some 200 regional trade agreements have been concluded, of which about 100 have been created since the 1990s. It is not clear whether growing regionalism will evolve into free multilateral trade as regional trading blocs enter into agreement with each other.

The main economic reason for forming regional trade blocs is to enable the countries concerned to develop industries characterized by economies of scale. This is especially relevant for the East African countries. Following economic liberalization, adjustment costs are likely to be high as domestic industries lose their markets to more efficient foreign supplies. Within the region, the loss of less efficient firms will be offset by gaining more efficient suppliers in each of the partner countries.

Maturity within the region while remaining protected against competitive pressures from outside may prepare East African countries for greater competition. This is the standard 'infant industry' argument in favor of protectionism. It does seem to be warranted, though, in this case of a particular group of developing countries, many of whose industries are unlikely to survive unmediated exposure to global competition. Razia Khan[64] respected analyst and head of research for Standard Chartered Africa argues that Kenya should concentrate on improving trade with its neighbours as opposed to countries from developing world. This she says is the surest way to accelerate economic growth and recovery. Regional trade has been very important to the growth of Kenya's economy and sometimes its importance has been underplayed by officials and captured data. While

**Razia Khan, Focus on regional trade. Kenya urged. Daily Nation Thursday 7 2008**

overseas marketing has been a government obsession, statistics from central bank of Kenya show that African countries absorbed almost half of the country's merchandise exports. In terms of regional trade, Kenya's exports to EAC countries increased by 31 percent (about KES.70.4BN) in the year to April 2008 from KES.53.5BN in the year to April 2007. Exports to the COMES A region also rose 23 percent within the same period.

Major African export markets for Kenya include immediate neighbors Uganda 12.5 percent, Tanzania 7.8 percent, and Egypt 3.6 percent. It is growth in Africa's economy rather than growth in the melting down global economy that has been driving Kenya economy. And with Africa's economy showing resilience that is good news for Kenya. To drive the growth further Kenya should concentrate on improving its infrastructure especially roads and railways that link it to other markets.[65]

### 2.5.2 The EAC

The treaty founding the EAC in its present form was signed by the parties in November1999, and came into force in July 2000.the organization itself, however, has a long and chequered history that dates back to the British colonial era in East Africa going as far back as the early 1920s when Kenya, Uganda and Tanganyika united to form, first, a free trade area, and later (1927), a customs union. In post WW2 period the union was transformed into the East Africa high commission, providing several joint services, including railways, harbors and a common currency to the three countries[66].

>id
**Article 3, Protocol establishing the East Africa Customs Union**

This arrangement was to evolve into the East African Common Services Organization in the post-independence period, after the efforts to establish an East African federation had failed in the face of parochial nationalism. The common services organization itself experienced a number of difficulties before being transformed into the first EAC through the treaty for East African Co-operation in 1967. Owing to the persistent problems arising primarily from completing, narrow 'national' self interest, divergent ideologies, and parochial sovereignty, the community finally collapsed in 1977, triggering a long and quite acrimonious process of distributing assets and assigning liabilities to the member states.

The present EAC arose out of the ashes of the collapsed one. It was a result of protracted negotiations among Kenya, Tanzania and Uganda, beginning in 1993 when the heads of state signed an agreement to revive co-operation among them. These negotiations were in accordance with article 14.02 of the EAC Mediation Agreement of 1984, which provided for the exploration and identification of areas of ftiture co-operation. As if no lessons have been learned from the collapse of the community 25 years ago, the treaty adopts a gradualist and functionalist approach and thus does not differ fundamentally from the earlier efforts. This is particularly true since the treaty fails to abandon parochial sovereignty in favour of pooled sovereignty, to transcend relative economic gains as the driving force and embrace long-term strategic goals, and meaningfully to mobilize and organize East Africans from below.[67]

**[67] On a recent visit to East Africa, chancellor Gerhard Schroder of Germany 'urged EAC members to meve quickly toward full integration', but cautioned them against hasty adoption of the EU model (see Africas 2004)**

The imperatives underlying the renewed EAC are not very explicit (see EAC 1999). Basically, the treaty adopts the 'affection' imperatives when, in the first paragraph of the preamble, it invokes the fact that the three countries 'have enjoyed close historical, commercial , industrial, cultural and other relations', and proceeds to recount the organizational forms this relationship has assumed since the colonial days. It is also inspired by the 'gain' imperative in so far as it repeatedly stresses equitable sharing of benefits among the partner states. Although the secretary general's foreword highlights the recognition 'that small and weak states have no future in this highly competitive world '(which is the recognition of threat), this is not reflected in the treaty itself.

Addressing the issue of the collapse of the Treaty for East African Co-operation in 1977 and, therefore, anticipating the pitfalls that must be avoided by the current arrangement, the current treaty identifies the main reasons as a lack of a strong political will, a lack of private sector and civil society participation, a disproportionate share of benefits, and a lack of policies to redress the situation as it deteridrated. It fails to mention the narrow, undiversified production base; the dominance of national interests, and their collusion with foreign capital; or the lack of a clear vision based on a shared perception of a threat. It should also be stressed that the proverbial 'political will' is in reality a function of the interest of the members. It is only to the extent that there is a clearly defined common interest or a convergence of national interests that 'political will' will be forthcoming. The principal objectives of the current EAC include: Developing policies and programmes aimed at widening and deepening co-operation among the partner states in political, economic, social and cultural fields; research and technology; defence; security; and legal and justice affairs; for their mutual benefit; The establishment, presumably sequentially, of a customs union, a common market, subsequently (sic) a monetary union and (sic) a political federation; To ensure sustainable growth and development; co-operation in agreed fields; sustainable utilization of natural resources ; consolidation of historical ties ; gender mainstreaming ; peace , security and stability ; and private sector and civil society partnerships.

The objectives articulated in the treaty are fairly conventional in the sense that they are not innovative in any fundamental way, except, perhaps, in the provision for the formation of a political federation. Moreover, there is no attempt to link these objectives directly with the AEC objectives and, unlike the Abuja Treaty; the EAC does not establish a clear timetable for implementation. Indeed, this has already raised many problems, particularly with regard to the signing of the East African customs union protocol. It was to be signed in November 2003, but was postponed to February 2004 without success. It was finally signed in March 2004 and set for implementation in July 2004. The reasons for the delay are unlikely to gd away any time soon because, in the words of Eats African Business Council chairman James Mulwana, 'it is going to create a very big shock to the business community'. He wanted implementation delayed for three to five years.[68]

The organs or institutions established under the treaty echo those established under the AEC and later the AU, albeit with some significant differences. They include the summit, the council, the co-ordination committees, the sectoral committees; the East African Court of Justice, the East African legislative Assembly, the secretariat, and such other organs as may be established by the summit. These institutions are fairly standard, but it

**[68] Ryan Orla, Ugandan Business fears Customs Union. BBC News 12 February 2004**

is notable that the EAC does not have among its organs a commission, peace and Security Council, economic council, or social council, although these issue areas are highlighted in the treaty itself. Regional peace and security, for example, is provided for under articles 124 and 125, but no framework for defense co-operation has been worked out so far.

It is now just over ten years since the heads of state of Kenya, Tanzania and Uganda met in Arusha and signed an agreement to revive East African co-operation, and nearly five years since the signing of the treaty. In that time, considerable progress has been made in building institutions and establishing procedures to implement the treaty. Notable among these institutions is the East African legislative assembly which was inaugurated in November 2001, with 27 nominated and three ex-officio members. It is instructive to note that the members of the house are drawn from national parliaments, and not popularly elected by East Africans. This runs against the goal of enhancing civil society participation in the activities of the community. It dlso denies the assembly the kind of legitimacy that would lend authority to its decisions.

Mohabe Nyirabu[69] was not at all optimistic about the future prospects of the community. Of the three possible paths he postulates - closer economic integration, an East African federation, and the building of common institutions- he sees some prospects only in the first one. He is skeptical about political federation and equally doubtful about the possibility of effective and sustainable common institutions. Even with economic integration, Nyirabu feels that trade integration can not be sustained without transforming

**Nyirabu Mohabe, *East African community;challenges ahead,* African review 2002, p29(182)**

production in the region. This is because 'past economic practice is not encouraging and therefore current optimism that creating a trade regime to remove tariffs will increase trade integration is not convincing'.[70]

**2.53 The East Africa Customs Union**

The EAC treaty provides for the establishment of a customs union. This means that partner countries will apply common import tariffs, and maintain a unified policy towards third-country goods. The protocol establishing the EACU was signed in March 2004. The partner states agreed to establish the union progressively over a transitional period of five years. The protocol recognizes that the partner states have reached different stages of development, and therefore have different .comparative advantages.

According to the protocol, the customs union is aimed at reducing trade imbalances, and encouraging the accelerated development of the community. The objectives of the customs union are spelled out in article 3 of the protocol. These are to: Further liberalize intra-regional trade in goods on the basis of mutually beneficial trade arrangements among partner states; Promote efficient production in the community; Enhance domestic, cross- border, and foreign investment in the community and; Promote economic development and industrial diversification in the community [71]

These objectives are in line with those of many other regional integration schemes that seek to promote development through trade. They imply that the main thrust of the union is to realize a viable integrated East Africa which will stimulate production, investment,

**Article 3, Protocol establishing the East Africa Customs Union**

and trade. This should then accelerate the socioeconomic transformation of the EAC. Indeed, all three countries have a lot to gain from an integrated market of nearly 90 million people with a combined GDP of about US$ 25 billion.

Despite the enormous benefits likely to accrue from the EACU, there are a number of issues that may challenge the implementation of the protocol. When they signed the EAC treaty, the three partner states undertook to ease the flow of goods and people among them; however, little progress has been made in this respect. Travellers, including traders, are still being harassed at border points, and the free movement of labour is still not permitted. Also crucial for the efficient functioning of a customs union is the harmonization of macroeconomic and trade policies. For example, tax competition among members of a custom union can hamper trade, and frustrate integration efforts. Other areas that need to be harmonized are the rules, and regulations governing the re-exportation of goods, monetary and financial regulations, and standards. Whereas the treaty recognized the need for harmonization, this still has to happen in numerous areas, among them taxation. This is likely to affect the operation of the customs union. Equally important is the co-ordination of macroeconomic policy, which has received very little attention.

The slow implementation of protocols and resolutions has been attributed to the lack of strong institutions capable of enforcing laws and obligations under the treaty. At present, the EAC does not have adequate powers to ensure that its decisions are effectively implemented, and its objectives realized. It should have the power to issue directives, which the legislatures in the partner states would be obliged to implement within a stipulated time frame. Such directives would need to be backed by a regime of sanctions to ensure that they are not simply ignored.

Poor infrastructure may also affect implementation of the customs union. The region has a reputation for poor facilities, border delays, and corruption. Poor port facilities, weak communications links, and an underdeveloped road network all limit the potential for expanding regional trade. Other problems that may detract from regional integration schemes include the lack of complementarity across regional economic communities, and dual memberships of regional trade arrangements.

The objectives of regional integration schemes vary widely. Some are inwardly oriented- i.e., they are primarily established to enlarge domestic markets for import substitution firms in the region in question. In such an arrangement, firms are expected to operate on a regional rather than a national basis. In certain cases, however, the agreements may permit very little competition among firms. Regional integration schemes may also be outwardly oriented; these are usually established as a first step towards integration with the world economy. Casual examinations of the EAC's objectives indicate that the former is the case. The primary objective of the EACU is to promote regional trade, and its outward orientation is seen as an added advantage of trade co-operation in the region.[72]

**Conclusion**

We cannot study the implications of the customs union as an abstract, this chapter is an effort in understanding regional integration as seen by different scholars. It also puts forth

**Radelet S *Regional integration and cooperation in sub Saharan Africa: are formal trade agreements the right strategy?development* discussion paper no 592. HIID Harvard University 1997**

the drivers of regional integration. They may differ in different regions but as the study reveals, there are certain common denominators. Of particular interest are the commonalities between the East African states which gives impetus to the integration efforts. Past attempts at integration were marred by significant political and economic differences but they are now more stable and showing signs of macroeconomic convergence bringing benefits to businesses and residents of the region.

## CHAPTER 3: INDUSTRIALIZATION AND REGIONAL INTEGRATION

### 3.1 Overview

The chapter looks at the relationship between industrialization and regional integration. It reviews the publications that have established a link between the two.

### 3.2 Industrialization and Regional Development

Industrialization and international trade have long been regarded as the principal engines of economic growth. The chapter therefore provides a review of theoretical basis of these sources of growth and also how the East African states are striving to reduce their dependence on agriculture and moving towards manufacturing.

### 3.2 The Advantages of Industrialization

The revolution that began in England in the 18th century, spread to other European countries, and then to the United States, Japan, and,others, transformed the economies of all the countries in which it took hold. This is equally true of other developing countries comparable to those in East Africa which industrialized as recently as the 1960s and 1970s.[73]

Almost every country that has achieved rapid economic growth at any time during the past two centuries has done so by means of industrialization, with increased industrial output and employment accompanied by a corresponding decline in the importance of agriculture as the characteristic development pattern. Manufacturing adds values to productive resources by making use of opportunities for specialization and economies of

"ibid

scale, both of which enhance productivity. Moreover, because industrial activities are technology- intensive, the rapid technological advances in recent decades have increased the growth rates of industrial countries phenomenally. Indeed, the rate at which countries absorb and utilize technological change may well be the most important factor in global economic competition. Thus industrial race among countries has been transformed into a technological one. Advances in information technology, which now pervades all spheres of industrial activity, have also blurred the traditional distinctions between goods and services.

Despite these evident advantages of industrialization, and the achievements of many countries that have industrialized vigorously, this route has not been followed by East African countries, which are still primarily dependent on agriculture. However, given that land suitable for agriculture is a finite resource, and that the populations of these countries are growing rapidly, their agricultural sector can not continue to provide a sustainable basis for future growth, employment, or feven subsistence. Kenya dramatically illustrates the significance of this factor. In 1948, when the first population census was conducted, there were only 5.4 million people in the country. Today, there are more than 30 million, and Kenya recently recorded one of the highest populations' growth rates in Africa of 3 per cent a year.[74]

Because of the continued dependence on agriculture in these countries, people are spreading out to marginal areas that are less and less suitable for agricultural production. Research and development aimed at increasing agricultural production are not remotely matching the pace of this demographic phenomenon. Moreover, the increasingly intensive use of both prime and marginal land has created serious environmental problems that are further undermining the sustainability of the agricultural sector.

### 3.3 The Development and structure of manufacturing in East Africa

Kenya is generally considered to be the most industrialized East African country. However, the economies of all three structurally similar, due, in part, to their common colonial experiences, and Kenya can therefore be taken to illustrate the history and pattern of industrial development in the region as a whole.

Kenya's modern manufacturing sector began early in the colonial period, when an economic infrastructure aimed at linking that country to world markets emerged. By 1905, numerous import-export houses had been-established to trade in primary commodities and consumer goods, the latter principally for consumptions by settlers. Between the two world wars, some firms were established which produced consumer goods mainly for the domestic and East African regional markets. Most of these processed agricultural products, but numerous other companies were established as well; they include, for example, the Magadi Soda Company, East African Power and Lighting, and East African Portland Cement, all subsidiaries of major multinational companies. Practically all the firms founded at the time were established after World War 2, when British firms attracted by East Africa's high tariff walls began to invest in the region. Although, after independence, industrial investment slowed down, and some capital was withdrawn, the import-substitution policy was perpetuated. At the time, this seemed like the natural route to industrialization.[75]

"ibid ~~"

In the post-colonial period, the government sought to promote the entry of Africans into manufacturing and service sectors via a number of schemes. Access to trading networks was promoted through the Kenya National Trading Corporation (KNTC), and subsidized credit was provided through the Industrial and Commercial Development Corporation (ICDC). Kenya Industrial Estates (KIE) sought to promote the formation of African manufacturing firms by establishing manufacturing sheds.

However, the most important means of achieving indigenous participation in manufacturing was establishment of parastatal enterprises. During the three decades after independence, the dramatic growth of state enterprises became the most dominant feature of the economic scene. Similar industrial strategies were pursued in both Uganda and Tanzania.[76]

The bulk of Kenya's manufacturing sector is confined to the southern part of the country, along a belt stretching from Kisumu and nearby towns in the west to the coastal town of Mombasa. Most industries are situated in Nairobi, quite far from Mombasa, the country's main sea port. The need to transport imported raw materials and intermediate inputs as well as petroleum products from the coast to the industrial areas makes the eventual products far more expensive. Products for export have to be transported back to Mombasa, thus further increasing costs. Locating export industries in Mombasa would greatly reduce these costs, thus improving Kenya's global competitiveness. Some of the industries located even further inland in the other major towns of Nakuru, Kisumu, and Eldoret suffer even greater transport disadvantages. In the smaller towns, manufacturing

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is mainly agro-based. There is little manufacturing activity in the arid northern reaches of the country.

Numerous factors have influenced the spatial distribution, size, and ownership of Kenya's manufacturing sector. After World War 2, it was increasingly seen as a regional economic centre. Given the impressive economic growth rates achieved during the first decade of independence, many foreign companies moved into the country, using it as a base for supplying regional markets.

Nairobi became a favored hub for those firms targeting the East and Central African markets. It's relatively well developed infrastructure, supply of trained people, wide range of financial services, and moderate climate were the main considerations. The abundance of raw materials has also played a key role in the spatial allocation of manufacturing activity. This has been most notable in the wood and cement industries. However, proximity to farm output has also been important for the location of food processing plants.

Government policy has played a role in the location of industries. Here a number of considerations have been at play, including the policy-makers' desire to create jobs, enhance the development of remoter parts of the country, and promote certain industrial structures, notably small-scale industries. These efforts were most notable in the development plan of 1970-4, in which the promotions of industrial activities in the rural areas was emphasized. Industrial estates were also established in the major towns.

The construction of an enabling socio-economic infrastructure in politically strategic regions has led to the expansion of manufacturing activities in some parts of the country at the expense of others. Eldoret and Thika are examples of this. Not surprisingly, a uniform and evenly distributed pace of industrialization has been impossible to achieve. Uganda has all the transport disadvantages of a landlocked country. Industrial development in Tanzania is concentrated in Dar-es-Salaam, which is also the country's largest sea port, and it therefore does not suffer from the transport disadvantage which plagues the other East African countries.

The size of Kenya's manufacturing industry can be gauged from its contribution to GDP and employment. From 1972 to the present, manufactured products have contributed about 14 per cent a year on average to Kenya's GDP- a very low level.[77] From 1966 to 1978, recorded wage employment in manufacturing increased from about 60,000 to about 130,000, a rate of about 6 per cent a year. In the early 1980s the growth rate in employment fell to a mere 2 per cent a year. In the second half of the 1980s, employment increased somewhat more rapidly, but since 1989 it has once again shown very little growth, and has in fact been declining since the early 1990s.[78]

### 3.4 The Edible Oils Industry

Agriculture accounts for about 24 percent of Kenya's GDP with an estimated 75 percent of the population depending on it either directly or indirectly. Vegetable oil is one of the

**[77] The figures in this section are computed from GOK statistical abstracts from 1972 to date. Calculation by the author from Kenya Statistical Abstracts.**

**[78] The figures in this section are computed from GOK statistical abstracts from 1972 to date.**

key sub sectors of agriculture with Soybean and Palm oil being the leading sources in production of vegetable oil in the world respectively. The key players in the vegetable oil industry in Kenya comprise processors who extract the oil from the seeds and also produce oil cake for use in animal feeds and refiners who convert crude oils into a from suitable for human consumption. The private sectors are credited with the edible oils industry growth with the government playing the advisory role. Currently there are about 30 vegetable oils refiners in the country. The exporting companies include Bidco Oil Refineries, Palmac oil refiners and Kapa oil refiners. They engage in production of cooking oils, corn oil and fats edible oils among others. To guarantee supply of raw materials, some of the companies work with small scale farmers in better farming methods. Exports are mainly to East African Community and the COMESA region.[79]

### 3.5 Opportunities and Challenges

If countries today want to achieve rapid and sustainable economic growth and become globally competitive, they need to move away from primary commodity production to industrial manufacturing, in qualitative and quantitative terms. There are huge opportunities for technological advances even in the production of traditional manufactured goods that would increase competitiveness in the economic use of raw materials and improved product qualities, convert traditional waste products into commodities, and generally increase productivity. The real challenge, however, lies in shifting to more modern commodities with a higher technological content.

[78] **Export Processing Zones Authority, Vegetable Oil industry in Kenya, Government printer 2005**

The EA countries have failed to develop viable and sustainable industrial sectors. The industries that have developed behind the protective walls have found it difficult to withstand competitive pressures on a global stage. The trade liberalization policies pursued under SAPs have exposed these industries to external discipline, but have failed to convert them into efficient competitive establishments. Thus industries have lost ground; not only in their traditional domestic markets, but also in the international markets they have been expected to penetrate.

The current export-oriented industrialization policies are relying on market forces to drive domestic industries towards efficient production. This presupposes that domestic firms are able to respond. Becoming globally competitive requires that domestic firms operate with technologies comparable to those of their foreign competitors, and apply them as efficiently as well. In a recent firm-level study of industry in Kenya, Bigsten and Kimuyu[80] found that both the levels of technologies applied and technical efficiencies were extremely low. This suggests that, rather than being able to stand their ground in a liberalized environment; manufacturing firms in the region are more likely to shut down. Firms that installed competitive technologies and operated them efficiently even during the import substitution period are the ones likely to survive. Low and declining exports of manufactured goods are the logical consequences of low-level technologies and inefficiencies.

In the context of rapid technological advances in industrial production, and rapidly changing world markets, restructuring for export remains a major challenge. Clearly, the

[80] **Bigsten and Kimuyu, 2002, *International relations,* sixth edn (New York: Longman 2000)**

liberalization of markets is inadequate as a means of achieving a successful export orientation, as it is more likely to lead to deindustrialization. More directly supportive strategies and policies that could complement market forces in ensuring technological dynamism will be needed. This calls for in-depth analyses of the specific constraints on industrial growth. Policies that directly support the developments of the necessary skills and technological capacities should be introduced.[81]

### 3.6 The role of industrial development within the EAC

Co-operation over industrial development is regarded as vital for generating growth and development in the region. The EAC strategy for the period 2000-5, for example, strongly emphasizes industrialization (EAC 2001). This can be justified on at least two grounds: first theories about and experiences of economic development, especially in Asia, ascribe a high level of dynamism to industry relative to other sectors such as agriculture. Second, industry helps to generate and diffuse technology, which is crucial for the competitiveness of any economy. However, despite previous efforts to promote industrialization in the three partner states, their industrial sectors continue to perform poorly, both in terms of growth and contribution to GDP.

The level of industrial development in the three countries is a contested issue. It is generally accepted that the trade imbalance between Kenya and its partners - which has been blamed for the collapsed of the first EAC- is due to Kenya's industrial superiority. In 2002 Kenya's manufacturing sector contributed about 11 per cent to GDP, compared to 9 and 7 per cent in Uganda and Tanzania respectively. Kenya's industrial sector is thus

[81] **Bigsten A and P Kimuyu,** ***Structure and performance of manufacturing in Kenya, studies on african economies,*** **Palgrave 2002**

larger and more sophisticated than those in the other two countries. However, it has performed relatively poorly during the past few years.

In 2001, Uganda and Tanzania absorbed about 69 per cent of Kenya's total exports. Most of Kenya's exports to Uganda and Tanzania are manufactured goods, including petroleum oil, plastics articles, soap, cleaning and polishing preparations, medicaments, rolled iron products, sugar confections, lime, cement and fabricated material, paper and paper cut size or shape, paperboard and footwear. Petroleum products are also important, although these are simple re-exports. Kenya's imports form Uganda and Tanzania are significantly fewer than its exports to them, and include tobacco products, tobacco refuse, unmilled maize, vegetables, chilled or frozen fish, feed for animals, cotton fabrics, woven or man-made textiles, oil seeds and insecticides. Industrialists and politicians in Tanzania and Uganda sometimes view the dominance of Kenya's industrial exports in a negative light. These negative perceptions have largely been responsible for the delays in implementing the EAC treaty.

If the broad objectives of the EAC are to be realized, its partner states should co-operate fully on industrial development. Key actors have realized this, and the East African Industrial Development Strategy (IDS) has been put in place to guide industrialization in the region. Its primary purpose is to create sustainable economic and social development in East Africa. Its focus is to 'create an enabling environment for the establishment of a single market and investment which would be internationally competitive, while operating in conformity with WTO rules and regulations '(EAC secretariat 2001). Its specific objectives are to: Eliminate identified constraints on industrialization in the region; Develop the existing and potential comparative advantages of the industrial sector; Promote resource -based medium and small-scale industries and processing activities through adding value; Achieve balanced industrial growth in the region; Increasingly export internationally competitive manufactured goods; Develop and maintain environmental and quality standards; Increase income and employment in the industrial sector and Promote indigenous and particularly women entrepreneurs.

Strict implementation of the East African IDS will be key to the success of the EAC. Among other things, this will require the harmonization of policies, regulations and laws governing competition, industrial incentives, and the location of industries. It will also require a strategy for mobilization of resources for industrial development, involving the public and private sector in all three countries. In terms of the current policy framework of economic liberalization, governments will be expected to play a facilitative and regulatory role, and create a conducive environment for industrial development in the region. As regulators, governments will be expected to ensure fair rules for industrial development, and provide services such standardization and the provision of economic and market information. In certain cases, public-private partnerships in service provision will be necessary. The private sector is also expected to play an important role in the EAC. Besides providing the bulk of investment, it is expected to provide most of the services required for industrialization, and play a lobbying and advocacy role to ensure sound industrial policies.

The idea of Regional economic communities (RECS) on the continent is not new. During the past three decades Africa has experimented with various RECs with varying degrees of success. The old EAC was probably the oldest followed by the Economic Community of West African States (ECOWAS) formed in 1975. The decision of the Organization Of

African Unity (OAU) in 1976 to divide Africa into five regions gave added impetus to these initiatives also leading to formation of the Economic Community of Central African States (ECCAS) and the Southern African Development Coordinating Conference (SADCC) later the Southern African Development Community(SADC).[82]

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Felicia Arudo traces African integration to the Panafricanism movement times. Whereas Black Americans from USA and the Caribbean dominated the Pan African movement in the late 19th and 20th century, leaders from Africa began playing a greater role from the mid 20th century. Between 1900 and 1945 six Pan African congresses were held in different European cities. The congresses expressed the hope that the peoples of Africa and Asia would break the chains of colonialism and stand united to safe guard their liberties.[84]

The more recent attempts at economic integration can be traced back to the Lagos Plan of Action (LPA) adopted at the second extraordinary session of African heads of state and government of the OAU in Lagos in July 1980. This was the culmination of a series of continental reflections on how best to deal with the unfolding African political and economic crisis marked by declining terms of trade and a rapidly shrinking share of global trade. They were in a sense the first continental responses to the African economic crisis of the late 1970s and 1980s. A decade elapsed before Africa made another attempt at continental economic integration. In June 1991, at the 27th summit of heads of states and governments, the OAU adopted the treaty establishing the African Economic

**[82] Nyongo P *Regional integration in Africa:unfinished agenda,* Nairobi:Academy publishers**
**[83] ibid 32 .**
**[84] Kenya institute of education(KIE) *Secondary history and government* Nairobi:Kenya literature bureau 1986**

Community (AEC)-The Abuja Treaty. It recognized previous efforts and achievements at regional and sub regional integration and set out to establish conditions for achieving a 'unified and self sustaining economy' on the continent. But like the LPA, the Abuja treaty remained largely on the drawing board and has been overtaken by events as African leaders have scrambled to reposition the continent globally. The inauguration of the AU and NEPAD in 2002 more or less ended Abuja's decade of inactivity. NEPAD also recognizes the need to strengthen Africa's RECs thus enabling them to serve as the building blocks of an African economic regeneration.

The NEPAD initiative also acknowledges the limited markets of existing national economies, and therefore concludes that successful economic regeneration can only be brought about by pooling markets and resources; hence it talks of the need for African countries to combine their resources in order to enhance regional development and economic integration. It is against this broad backdrop of attempted regional economic integration, ultimately directed at African economic'regeneration, that the revival of the EAC must be situated.

### 3.7 Concept of performance

Performance has been defined as 'to fulfill' in the Collins compact dictionary(1999). It is critical for excellence and survival of a company. It is the process by which executives, managers and supervisors work to align employee performance with the firms goals.[85] Performance is also seen in terms of how well the objectives of a particular task is met, looking at the quality of ones work or looking at the quality of the end product. In understanding the concept of performance, it is important to be more concerned with the

[85] **Ivancevich JM *Human resources management* McGraw hill companies 2001**

amount of effort that has been put in an activity and the ability that might have been used.[86] The works collected in Harvard Business Review in measuring corporate performance, including the three ground breaking articles on the balanced score card offer managers practical guidance for measuring their intangible assets(customer relationships, internal business process and employee learning) and aligning corporate strategy accordingly. The balanced scorecard offers the most complete purpose built application for managing business performance in todays complex and rapidly changing business environment. Unlike business intelligence, score carding ,and desktop tools, it combines performance metrics, initiative management, budgeting and planning, reporting in a single, structured environment.[87]

The ultimate goal of any organization is to maximize on profits while remaining cost effective. Organizations are geared towards gaining competitive advantage in the industiy they are operating in. Highly successful business groups are very aggressive through their customer driven and market driven strategies in creating big markets for their product ranges and services. Therefore performance in firms may be attributed to the overall organizational competitiveness in an industry.[88]

The modern way of measuring a company performance is by benchmarking against the performance of its peers in the same industry. Once reserved for larger companies who could afford it, today even Small and Medium Enterprises are benchmarking their positions in the market place as well. With the analysis of specific data, benchmarking

[86] **Ibid.**
[87] **Ibid.**
[88] **Aravindan P, *Team engineering and world class management,* Wheeler publishing, New Delhi 1997**

enables manufacturers to understand how their performance rates within their industry segment and identifies opportunities for improvement. Profitability performance ratios may also be used to measure performance. These ratios measure how effectively a firm is using its various resources to achieve profits. Management performance is often measured by a firms profitability ratio. These ratios include earnings per share, return on sales and return on equity. Earnings per share are important as it helps stimulate growth in the firm and pay for such things as stockbroker dividends. Return on sales is also vital as it helps the firm to measure its return on sales hence help the company to compete against generating income from the sales they achieve.[80]

Competitive advantage[90] is also a measure of a performance especially in competitive markets. Competition is at the core of the success or failure of firms and determines the appropriateness of firms activities that can contribute to its performance such as innovations, a cohesive culture, or good implementation.[91] Competitive strategy is the search for a favorable competitive position in an industry, the fundamental arena in which competition occurs. Competitive strategy aims to establish a profitable and sustainable position against the forces that determine industry competition. The ultimate aim of competitive strategy is to cope with and ideally to change rules of competition in a firms favour.[92] Whether in domestic or international markets, rules of competition are embodied in various forces which include entry of new competitors, bargaining power of

**[89] Nickels *G,understanding business* 7th edn McGraw Hill, New York 2005**
**[90] A firm is said to posses competitive advantage over its rivals when it sustains profits that exceed the average for its industry.**
**[91] Porter Michael, *Competitive advantage;creating and sustaining superior performance,* The Free Press „ New York 1998**
**[92] Ibid**

suppliers, threat of substitutes, bargaining power of buyers and the rivalry among the existing competitors. The collective strength of these five competitive forces determine the ability of firms in an industry to earn on average rates of return on investment in excess of the cost of capital.

These forces also influence the prices, costs and the elements of return on investment for the industry at large. The bargaining power of suppliers determines the costs of raw materials and other inputs while the power of buyers can influence the cost and investment because powerful buyers demand costly service. The intensity of rivalry influences prices as well as the costs of competing in areas such as plant, product development, advertising and sales force. Performance may also be measured in terms of success factors. To analyze and determine why some firms may win in the market while others loose include the vision and strategy of the firm, their assumption of the future and the unique resources they possess. Every firm must have a vision and a strategy in order to compete in the market place. The vision represents where the firm intends to go while the strategy is what the company uses in order to achieve the set objectives.[93]

A firm for example may make assumption in areas of supplies which may be caused by the national economies, other companies may not be aggressive enough because they assume the economy will remain as it is for another decade or so. Other firms may have macro environmental assumptions like of growth by the national economy or instability of the government and this may determine the progress of the business. For this study,

[93] **Rothschild William, *How to gain and maintain the competitive advantage in business,* McGraw Hill Book Company New York 1984**

guided by the objectives of the EACCU, the concept of performance shall focus on sales volumes of the firms, efficiency of customs officials, effects of market share and valued opinions of firm management on effects of the customs union.

**Summary**

This chapter was to trace the origin of industrialization. It also reveals how the manufacturing industry has grown in Kenya. The edible oils sector is part of this industry that is often faced by a myriad of problems. However, with the implementation of the customs union, there exists opportunities for the industry to expand within the region

# CHAPTER 4: INDUSTRIALIZATION IN E.A REGION

## 4.1 Overview

In this chapter, the researcher gives an outline of industrialization in the E A region.

## 4.2 Characteristics of the East African Countries

The member states not only share a common history, they also display common economic and social characteristics. However they also differ markedly in some respects. An important feature of all three economies is the predominance of agriculture. While agricultures share of GDP has been reducing steadily, it is still substantial: about 24 percent in Kenya, 29 percent in Uganda and 41 percent in Tanzania (2002 figures). The agriculture sector also accounts for the bulk of the employment and foreign exchange earnings.

## 4.3 Governance and Business Climate

Poor governance has been cited as one of the main impediments to development in Africa. Poorly managed public resources, widespread corruption and poor public service delivery have undermined development in most African countries. Kenya, Uganda and Tanzania are no exception, infact these three countries have earned the dubious distinction of being among the most corrupt countries in the world. Among other things corruption retards economic progress. It leads to misallocation of resources by distorting government expenditure. It can also work to reduce investments as well as financial aid. Corruption affects the business environment, and ultimately competitiveness as well. The discovery of trade and investment barriers as a result of economic globalization has required countries to become more competitive.

### 4.4 The political economic nexus in East Africa

Politics have a major bearing on economic decisions and outcomes for instance, regional integration may be good economics, but its implementation is highly political. A definite feature of East African and indeed most African countries is that different political regimes have had major effects on their economies. After Uganda became independent in 1962, its economy though small, performed quite well until the late 1960s, but badly from then on. This was compounded by the despotic rule of Idi Amin between 1971 and 1979. In that period the country suffered from political repression and instability severe mismanagement of the state and the economy and eventually civil war.[94] By 1986, when the civil war ended, GDP had dropped by about 20 percent. The new president, Yoweri Museveni, introduced various market- oriented economic reforms, and Uganda became the first countries in Africa with a growing economy.

Tanzania has gone through three phases of government since independence. The Nyerere phase was characterized by Liberian and national consolidation. The Mwinyi phase was characterized by the privatization of state institutions and the liberalization of the economy. The Mkapa phase has been characterized by a campaign against corruption, the promotion of good governance via greater accountability and transparency, a more disciplined civil service, enhanced tax collection and austere speeding. The improved performance of the Tanzanian economy has been attributed to the last-named reforms.

**[94] USAID. USAIDs approach to poverty reduction, the case of Uganda evaluation brief no.8, bureau for policy and program coordination,2003**

Kenya has also experienced three phases of government. Economic performance during the Kenyatta regime (1973-1978) was generally impressive.[95] During the Moi regime the economy performed poorly, especially in the 1990s. While external factors such as poor commodity prices and unfavourable international factors played a role, domestic factors such as mismanagement, corruption, and poor infrastructure were also to blame.[96] While the Kibaki regime is still young, early indications are that economic performance may not improve; in particular, the corruption and mismanagement that characterized the Moi regime are still safe.

According to the protocol, the Customs Union is aimed at reducing trade imbalances and encouraging the accelerated development of the community. Most of the elements central to the customs union are not unique to East Africa; however they are implemented in different ways in different regional schemes.

Tariffs interfere with the free flow of goods and services, as they make them more expensive. Almost always, tariffs also cost consumers more than they benefit producers and government. There is therefore a strong case for their removal. As per article 10 and 11, the partner states have undertaken to progressively eliminate internal tariffs over a transitional period of five years. This has clear economic effects for instance, it is expected to spur trade and investment and also enlarge the market as smaller national markets merge to create a large regional market. In a customs union, member states not only abolish restrictions on internal trade but also impose CETs on imports from other

**[95] Ikiara Gerrishon, Olewe Nyunya, Joshua and Odhiambo, Walter, Kenyaiformulation and implementation of strategic trade and industrial policies,2004. In Soludo, Charles, Ogbu, Osita and Chang,Ha-Joon(eds)r "The politics of trade and industrial policy in Africa:forced consensus?", Africa World Process Inc.**
**[96] ibid**

countries. This has far reaching revenue implications and is often a sensitive issue during negotiations. A high CET perpetuates high-cost firms and may erode competitiveness. The partner states have agreed on a three-band regime with a minimum rate of zero percent, a middle rate of 10 per cent and a maximum rate of 25 per cent to be imposed on all products imported into the community.

These objectives are in line with those of many other regional integration schemes that seek to promote development through trade. They imply that the main thrust of the union is to realize a viable integrated East Africa which will stimulate production, investment and trade. This should then accelerate the socio-economic transformation of the East African Community. Indeed, all the member states have a lot to gain from an integrated market of nearly 90 million people with a combined GDP of about USD25 Billion.

The objectives of regional integration vary widely. Some are inwardly oriented, this is they are primarily established to enlarge domestic markets for import substituting firms in the region in question. In such an arrangement, firms are expected to operate on a regional rather than a national basis. In certain cases however, the agreements may permit very little competition among the firms. Regional integration schemes may also be outwardly oriented these are usually established as a first step towards integrating with the world economy. A casual examination of the East Africa Community objectives indicates that the former is the case. The primary objective of the EACU is to promote regional trade and its outward orientation is seen as an added advantage of the trade cooperation in the region.[97]

[97] **Radelet S, Regional integration and cooperation in sub-saharan Africa:are formal trade agreements the right strategy?development discussion paper no 592. HIID Harvard University 1997**

### 4.5 The Effects of the Customs Union

The effects of regional integration on partner countries are modeled in terms of trade standards theory which states that free trade is superior to all other forms. In theory free trade among two or more countries will improve their welfare as along as the agreement leads to net trade creation(difference between trade creation and trade diversion) trade creation occurs when a member switches from the consumption of goods produced domestically(at a relatively high cost) to imported goods produced more cheaply in a partner country. Trade diversion occurs when a member switches from the consumption of lower cost goods imported from outside the region to higher cost goods produced within the region which face lower tariffs after integration. Viner[98] was the first analyst to show that trade creation enhances welfare and trade diversion reduces welfare.

The creation of a Customs Union can be associated with gains and losses. These may emerge from a number of dynamic sources, including specialization, economies of scale, changes in Terms of trade, and forced changes in efficiency due to increased competition." A large competitive market is likely to induce firms to produce more specialized products, thus winning a larger share of the market. Similarly if there are economies of scale in a specific product process, a larger market resulting from integration may enable firms to lower their production costs.[100]

**[98] ibid**

**[99] Lipsey Richard, The theory of Customs Union: a general survey In J.N Bhagwati(ed) "International - Trade selected readings" Cambridge:the MIT press 1987**

**[100] Balassa Bela, "The theory of economic integration" London, Richard D Irvin 1961**

### 4.5.1 The economic impact

Assessing the economic impact of the EACU requires a simulation model of the Viner type. Numerous attempts have been made to simulate the potential effects of the new Customs Union using the Vinerian model, among them by Ngeno et al(2003), Busse et al(2003), and Deroso(2003). Results of Derosas study on associated revenue gains and losses are shown below.[101]

**Projected effects of the EACU (CET 20 percent)**

| Effect | Kenya | Tanzania | Uganda | EAC |
|---|---|---|---|---|
| Trade creation | 81.7 | 46.6 | -29.2 | 102.1 |
| Trade diversion | 297.3 | 90.6 | 32.1 | 420.1 |
| Net trade | -212.6 | -44.0 | -61.4 | -318.0 |
| Forgone tax revenue | -45.2 | -30.3 | -34.8 | -110.3 |
| Change in economic welfare (%GDP) | 1.5 | 1.1 | -0.9 | 0.8 |

Source: World Bank African Report

It shows that trade creation (measured in terms of increased imports) occurs mainly in Kenya, Tanzania rather than Uganda. It also shows that that the EACU will improve the economic welfare of the region by about 0.8percent of combined GDP. However, while

**[101] Derosa Dean A, obwona, Marios and Rorungen, Vernon O The new EAC Customs Union:implications-for trade, industry competitiveness and economic welfare in East Africa, paper prepared for the ministry of finance, planning and economic development, Uganda.www.or.ug/respapers/eac. 2003**

both Kenya and Tanzania will gain from its formation, Uganda will actually lose by 0.9 percent. According to Derosa, this will happen because under the high CET scenario the country must raise its current average external tariff rate by over 50 percent from 10.6 to 16.2 percent. He shows that all three countries will forgo tax revenue, but that Kenya and Tanzania will lose the most. When the CET value is low, the loss will be least. A slightly different scenario emerges in analyses of the revenue implications of the EACU carried out by various researchers in the partner states. (Atingi-Ego et al 2002, Lyakurwa et al 2002, Ngeno et al 2002, Mullei 2003). These simulations show that tehe more tariffs are reduced, the more revenue will be lost. They also show that given the nature of the intra-EAC, Tanzania will forgo more tariff revenue than any of its neighbours and Kenya at least.[102] Therefore, the scenarios show that the establishment of the EACU will probably lead to unequal costs and benefits to members. It's therefore not surprising that the negotiations process has been punctuated and slowed down by strong feelings of inequity coming even after the endorsement of the protocol and despite its compensation mechanisms.

**[102] Mullei A Steering East Africa towards a Customs Union;suggestions from a pilot study.Nairobi:African center for economic growth**

# CHAPTER 5: CRITICAL ANALYSIS

## 5.1 Overview

This section takes an overview of issues that have emerged in each part of the research and makes a critical analysis. It will bring out any contending issues and demonstrate how the views relate. The chapter shall also give a critique on the concept of regional integration and the impact of the Customs Union in the edible oils sector. The study set out to examine the impact the regional integration has on the firms in member states. Specifically it set out to identify the impact of the customs union on firms in the edible oils sector. It also aimed at examining what challenges face countries in their efforts at regional integration in a globalized society.

## 5.2 Research Design

The research design was a case study where selected population of firms in edible oil sector. Some firms within the EPZ were also examined

## 53 Population

In order to achieve the set objectives of the impact of the EACCU the population comprised of only two large edible oil firms in Kenya who are listed and classified as edible oil firms in the Kenya Association of Manufacturers directory. The two firms were selected through the use of convenience sampling. This was done by sending out requests to four firms and only two were willing to be studied. These two firms were engaged in the export business and were well informed on the export and import procedures.

### 5.4 Content Analysis

The findings indicated that the Kenyan perspective on the EACCU is favourable. This is in line with the hypothesis of the study that were postulated as:-

- Regional integration and specifically creation of a Customs Union increases the opportunity for growth in the manufacturing industry

- Developing countries need to integrate in order to compete in the global market.

- The Customs Union is negatively associated with the growth of manufacture in Kenya.

The first and second of this hypothesis was supported by data from both primary and secondary sources. Following interviews carried out, primary data obtained indicated that with the starting of the EAC, firms operating in Kenya have made efforts to establish branches in partner states. In regard to understanding the EACCU, one company gave a brief explanation of the EACCU as simply 'the creation of an expanded market'. The other gave a detailed explanation of the Customs Union and argued that full benefits would be reaped when the EACCU was fully operational after the completion of the transitional process. This indicates that the respondent companies were fully informed of the existence of the EACCU as well as the benefits and challenges that accrue from the Customs Union. When asked about what they would perceive as the effects of the

EACCU on the performance of the firms, both respondent companies gave a nod on better performance after the Customs Union.

In regard to issues on increased sales volumes, Profits and increased market share, both respondent companies gave divergent views. Both companies were optimistic on all the areas mentioned but with varying degrees. Both were agreeable to increase in sales volumes, profits as well as market share due to the enlargement of the domestic market which covers more than 88 million people which has led to generation of larger sales due to larger markets, use the opportunities to maximize on economies of scale for larger mass production. This has also been due to reduced and elimination of internal tariffs.

In response to the main differences between the period before and the period after the implementation of the EACCU, the effects of the performance of the companies and the benefits and challenges the company is experiencing since the implementation they had various views. Despite experiencing benefits such as increase in sales and increase in market for their goods, the companies faced a threat on their goods by the imports into the Kenyan market from the Ugandan market which had been very minimal before the implementation of the customs union. This meant that the Kenyan farms have to increase their expenditures of new investments to improve on productivity so as to march the expectations of external and internal market, that is, to increase competitiveness. From the study, the respondent companies recommended the need for the partner states to look at the long term benefits and avoid the short term in the implementation process as they were reacting to the Tanzanian Government of going against the Customs Union.

They also recommended the need to end all non-tariff barriers as they have greatly impended business. They also recommended the need to have informed and educated customs officials at all border points as well as use computerized process to increase efficiency at the border giving the example of the European Union. The issue of electricity and power generation arose citing the need for the partner states to come out with an effective way of making a cost effective power supply for the region.

In general the respondents were eager to see the success of the customs union as this meant betters business for their companies. Other issues did crop up during the study and this included the various challenges that the sector faced which led to the aforementioned recommendations. These also substantiated the third hypothesis. In response to the effects of article 13 of the protocol about non- tariff barriers, the respondent were very unhappy with the various non-tariff barriers that are in existence. They stated some of them as luck of relevant and adequate documentation for clearance at boarder points. Other major constraints included poor infrastructure particularly electricity and water, government regulations and incompetence of customs officials at border points. In regard to article 5 of the protocol the partner states did not exchange information relating to customs and trade and there in no harmonized system to facilitate the sharing of customs and trade information. This therefore led to slow service at border points and increased costs in form of demurrage charges. The study also showed that some of the respondents understand the objectives of the customs union to some extent. Nevertheless, they are uncertain with respect to specific details. For example they are not sure whether the EAC entails reduction of tariffs or their elimination. A number of respondents said they were disappointed with implementation of the EAC agreement, noting that tariffs have not been involved, and that there was too much talk and little action.

Secondary data also confirmed that the Customs Union implementation faced other challenges in terms of revenue implications. The imports and exports from East Africa are an insignificant proportion of Kenya's total imports. Correspondingly, the potential and actual duty revenue from these East Africa imports are small. A customs Union would require tariffs on intra-EAC trade to be eliminated. The largest revenue losses would be from final goods while the lowest would be from intermediate goods in which there is very little trade. Although the loss in revenue is clear, the exports arising from dynamics of trade such as competition and efficiency would be expected to outweigh the static revenue losses. To improve competitiveness the firms suggested the following; harmonization of tariffs, improvement of the transport network, tightening of customs union, subsidization of water and power rates, reduction of tariffs on imported products and lowering tax on local products '

There have been policy reforms engendered through the EAC that have had positive goals but have brought little or no benefit to Kenya. Despite these, business people are optimistic and support the fast tracking of the EAC. In addition, the often cited problem in respect of integration in Africa of overlapping memberships came to fore. Kenya and Uganda for example are members of EAC, they are also members of COMESA. Tanzania, in turn, has withdrawn from COMESA and joined SAC. All three east African countries are members of IGAD. The issue of dual memberships of regional integration schemes has been associated with a number of difficulties. Overlapping memberships tend to dissipate collective efforts, and lead to wasteful duplication. It has certainly created mistrust among the member states. Moreover, overlapping or dual memberships add to the burdens of member states. A country belonging to two or more regional groupings must, besides meeting more than one set of financial obligations, also spread its resources in terms of time and effort in attending to different sets of issues. Customs officials also have to deal with different tariffs, rules of origin, trade documents and statistical nomenclature. A particular issue arising from dual membership has to do with the CET. While the EAC has agreed on a three- band CET, COMESA maintains a four-band CET. This is likely to create problems as long as members of the EAC are also members of COMESA. Once the EACU begins to operate, conflicts with COMESA will occur. The EAC and COMESA therefore need to agree on an operational mechanism. Similar problems are likely to arise in respect of Tanzania's membership of SADC. This has been recognized and the partner states have agreed that during the first four years the EAC should conclude trade arrangements en bloc with COMESA and SADC.

All the member states are also members of the WTO, and are therefore party to the WTOs multilateral system, and also subject to its core principles of open and liberal trade. A key principle of the WTO is the open and equal treatment of all WTO members. However, there is an exception to this clause:article 24 of GATT, which is administered by the WTO, allows members to form regional trading blocs, including customs unions, and to offer more favorable trade terms to other members of the bloc than to other WTO members. To this extent, the EAC treaty and the resulting customs union is WTO compliant. One important implication of the customs union in the context of the WTO is that its member states are expected to have a single negotiation position. In practice, however, regional blocs, especially of developing countries, do not negotiate as single entities, as this would restrict their ability to formulate and implement trade policy. If this condition is to be met, there is a strong case to be made for cooperation on trade negotiations under the EAC.

**5.5 Critical Analysis**

The concept of globalization remains contested in all fields. It is argued that there are pro-globalization proponents and anti-globalization people in the other side of the continuum who oppose the move towards globalization. The current resurgence of regional economic integration in Africa is neither new nor unique. It forms part of what has been termed the 'new regionalism' in developing countries, initiated largely as a response to the challenges of globalization. Analysts have long recognized that most developing countries do not have the resources to cope with globalization on their own. They need to pool their resources in regional arrangements that will allow them to collectively confront the daunting challenges of global markets and strengthen their bargaining power on the global stage. Given the far reaching impact of globalization, this has been seen not as a matter of choice but rather as an imperative. In other words regional integration is meant to make it possible for weaker countries to benefit from the global economy.[103]

Globalization is essentially an economic phenomenon. But it also has ideological and political dimensions. In political-economic terms it could be regarded as the process of the construction of a 'new architecture' for global economic governance. This new architecture derives its basis from another important feature of globalization namely the

[103] **Mittelman, *i.W,Rethinking the new regionalism in the context of globalization: global governance* may-aug pi 89-213, 1984**

integration of national economies into the global economy, thereby forming a single economy at the international level.

It thus entails the homogenization of national economies into a single global market. Homogenization is achieved through the integration of markets, finance and technologies.[104] In a world, the term globalization captures the extent to which national economies have become more deeply integrated into the overall economy.[105] The globalized international system is also market driven. The pillar of the international economy in the age of globalization is indeed the market. The marketization of the system has transformed the relationship between the market and state. If modern history has all along been shaped by the tension between the state and the market as two fundamentally different ways of organizing human relationships, the emerging trends in the contemporary world seem to suggest the triumph of the of the market over the state. The free market driven liberalization process that has accompanied globalization has tipped the balance in favour of the market. As tussie[406] has observed, 'as liberalization proceeds, national authorities must submit to a gradual erosion of their unfettered prerogative to supersede and regulate the national market.

Public and private investment levels are low, in recent years they have been lowest in Kenya and highest in Uganda. In 2002, public investment in Kenya amounted to only 2.7 percent of GDP in real terms. The corresponding figures for Uganda and Tanzania were 5.8 percent and 3.3 percent respectively. The relatively higher levels of public and private

[104] **Friedman T L, Doscapital*foreign policypg* 1999110-116**
[105] **Richards G A and Kirkpatrick C, *Reorienting interregional cooperation in the global political economy:europes east asian policy,* journal of common market studies , 1999 pg 683-710** -
[106] **Tussie D, Trading in fear? US hegemony and the open world economy in perspective. In Murphy and Tooze(eds)' The new international political economy pg 79-95**

ivestment in Uganda can be attributed to the fact that it was one of the first African juntries to adopt economic reforms aimed at promoting private sector led growth.[107]

**able 4.1 Economic conditions of the countries**

| "actor | Kenya | Uganda | Tanzania |
|---|---|---|---|
| Contribution of igriculture to GDP | 24% | 29% | 41% |
| 'ublic investment in erms of GDP | 2.7% | 5.8% | 3.3% |

ource: world Bank African database, 2004

/hile exports and imports constitute only a small share of the GDP of all three countries, le absolute values of imports and exports are higher in Kenya than in Uganda and *f* anzania. This implies that Kenya, because of its larger economy is able to export and nport more goods than its partners. However, in the case of all three countries, imports ir outweigh exports, implying trade imbalances. Yet another important feature of these :onomies is their level of indebtedness. The ratio of debt to GDP in all three countries is igh, and increasing in Uganda. This heavy debt burden has implications for regional itegration, because payments made to service foreign debts reduce funds that can be evoted to regional trade integration.[108]

**[7] World bank African database,2004**
**[8] Mutasa Charles, Regional integration and debt crisis:a comparative report of africas regional groupings, FRODAD research services,2003**

# CHAPTER 6: CONCLUSION AND RECOMMENDATION

## 6.1 Overview

This chapter gives the conclusion and the recommendations derived from the literature reviewed and the study findings.

## 6.2 Conclusion

The study was based on three objectives that were duly demonstrated. First the research examined an overview of regional integration with emphasis on the African experience. The second and third chapters outlined how the manufacturing industry has developed in Kenya and how the customs union has impacted the manufacturing industry.

The phenomenon of regionalization and globalization have made Kenya party to several regional and international organizations. The membership is intended to expand Kenya's external trade. The agricultural sector that the edible oils firm relies on has declined as a result of these measures. The multiple memberships in EAC, COMESA and WTO among others have impacted negatively on the agricultural sector. These include removal of tariffs and non-tariff barriers, reduction on agricultural spending, liberalization and removal of monopolies. These factors drained the competitiveness of local agricultural products. This in itself reveals a disconnection between the particular intentions of the customs union and individual state interests. This is noted mainly in the apathy displayed by Tanzania in regard to efforts at integration. Additionally Customs Union exposes firms to greater competition in the regional market. This can bring about greater efficiencies in production and marketing which may in turn lead to a positive industrial restructuring.

### 6.3 Recommendations

This study reveals that the establishment of the EACCU was a great step towards economic and social development for the East African people. It is therefore an effective tool to improve the living standards of the East African people. From this study, I recommend the following policies and practices; There is need to eliminate all existing non-tariff barriers as stipulated in article 13 of the EACCU which are a major hindrance to good business in East Africa. This can be done for example by ensuring all relevant documents are available to the business men at the border points such as by introducing the East African certificate of origin to facilitate improved trade.

The EAC secretariat should work in consultation with the business community as well as other stakeholders such as manufacturers and the -national government bodies such as revenue authorities. Ministries of trade and industry in the partner states to modify the EAC competition policy that will promote fair competition amongst companies from the partner states and hence to give the East African people better quality products and services.

There is need to educate the customs officials at all the border points to enable them to exercise the policies within the EACCU effectively and efficiently, partner states should adopt a common educational programme for educating all the customs officials. EAC secretariat should also increase sensitization training sessions for their officials as well as the partner states' revenue authorities officials to ensure a harmonized informative system is in place to facilitate the sharing of trade information. The EAC partner states should work on the computerization of procedures and processes which are vital in faster cross border services to ensure faster efficient and more effective services.

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## Questionnaire

For senior management staff/the policy makers(The chief executive officer, the executive director, senior corporate manager, and the general manager) and the middle level managers(the sales and marketing managers, export managers, the strategic managers corporate managers)

Kindly answer the following questions by giving all the details in the spaces provided.

Section A:Company demographics

1. Name of the company

2. Year of establishment

3.Position of respondent in the company

4. No. of years the respondent has worked for the company

5. What is the nature of ownership: tick appropriately
   - Local
   - Foreign
   - Subsidiary
   - Other(specify)

6. Does the company have branches/affiliates outside Kenya

   Yes No

   If yes where else: name all other countries..........

7. What's the total number of employees in your company?

8.1ndicate the services your company offers in relation to road transport....

Name the countries that the vehicles frequent

Section B.

The performance of the company.

1. What were your total yearly revenues in Kenya shillings and volumes to Uganda

| Year | Turn over |
| --- | --- |
| **2001..** | |
| 2002.. | |
| 2003.. | |
| 2004 . | |
| 2005.. | |
| 2006.. | |
| Total | |

2. What were your total yearly revenues in Kenya shillings and volumes to Tanzania

| Year | Turn over |
| --- | --- |
| **2001.** | |
| **2002.** | |
| 2003. | |
| 2004 | |
| 2005. | |
| 2006. | |
| Total | |

3. What were your total yearly revenues in Kenya shillings and volumes to Burundi.. •

Year Turn over

**2001**
2002
200 3
200 4
200 5
200 6
Total

4. What were your total yearly revenues in Kenya shillings and volumes to Rwanda

Year Turn over

**2001**. . . . ....:.............
**2002**. . ... . . . . . . . . . . . . . ... . .........
200 3__
2004_______________;________________,
200 5. .. . . . . . .. . .. . . . . . . .. . .. . . . . . .. . '
**2006**. . . . . . . . . . . . . . . . . . .....
Total

5.How much corporate taxes and duty did your company pay in the period 2001 to date? For transport services to the 4 countries

Year corporate tax
**2001**
2002
2003
2004
2005
2006
Total

Please indicate any other duties you pay

5. How would you rate the improvement of your market share after the year 2005?

Poor
Good
Fair
Best

Section C:Effects of the EACCU to the firms performance.

1. What is your understanding of the EAC Customs Union?

2.What do you perceive the EACCU to have on the performance of your organization(tick appropriately and note that rating scales is as from 1-4 where 1 is the best improvement while 4 is the least improvement on performance)

1. 2. 3. 4.

a. promote regional trade in EAC
b. Enhance cross border movement
c. Increased turnover
. d. Increased profits/revenues
e. Increased speed at borders
f. Efficiency at customs offices
g. Changes in clearance costs
h. Increased market share in EAC

According to article 5 of the protocol; the partner staes shall exchange information on matters relating to customs and trade and in particular; the prevention, investigation and suppression of customs offences and operation of a harmonized information system to facilitate the sharing of customs and trade information.

3.Do you think this has been done to assist transport business(please tick appropriately) Yes No
If yes how?..……….......

If no, what do you think needs to be done?

According to article 11 of the Customs union protocol; the partner states agree that upon the coming into force of the protocol and for the purpose of the transition into a customs union:

a Goods to and from the republic of Uganda and Tanzania shall be duty free

b Goods from the republic of Uganda and Tanzania into the republic of . Kenya shall be duty free

c. Goods from the republic of Kenya into Uganda and Tanzania shall have a phase out tariff reduction period of five years for all products.

3. What are the implications from this article to your firm and to what extent has this affected your firms revenue?

5. according to article 13 of the protocol; except as may be provided for or permitted by this protocol, each of the partner states agrees to remove with immediate effect all the existing non-tariff barriers to the importation into their respective territories of goods originating in the other partner states and thereafter not to impose any new non-tariff barriers.

6. Are there any non-tariff barriers that you experience while export to the other EAC countries? Yes No

Explain with examples_

6. Explain what you have observed as the main differences between the period before the Customs Union implementation and after the Customs Union came into force

7. In your opinion, has the EACCU led to better performance of your company?

Yes No

8. What are the benefits and Challenges your firm has faced since the coming into force of the EACCU?

Benefits

Challenges

9. In your opinion, is there increased competition for road transport providers in Kenya due to the Customs Union implementation from the other companies in EAC? •

Yes No

Explain

10. In regard to all the above challenges and benefits accrued from the implementation of the Customs Union, what are your recommendations?