

**UNIVERSITY OF NAIROBI**

**TRADE BARRIERS AND ECONOMIC INTEGRATION: A CASE STUDY OF  
KENYA AND UGANDA**

**IMELDA MBITHE**

**R50/63541/2010**

**A Research Proposal Submitted in partial Fulfillment of the Requirement for the  
Masters Degree in International Studies. University of Nairobi**

**2015**

**DECLARATION**

I **Imelda Mbithe Ngungui** hereby declare that this research project is my original work and has not been presented for a degree in any other University.

Signed..... Date.....

This Project has been submitted for examination with my approval as University

Supervisor.

Signed ..... Date.....

**Dr. Anita Kiamba**

**Supervisor**

## **ACKNOWLEDGEMENT**

First I would like to express my sincere gratitude to my Supervisor Dr. Anita Kiamba for her support, patience and guidance which has resulted in the successful finalizing of this project.

Secondly I also wish to thank Mr. Job Elogu, Commercial Attaché, Uganda High Commission, Matthew Kaikai from the Ministry of Foreign Affairs of the Republic of Kenya, Rose Frida Karoki leader of Kenyans living in Uganda and Nathan Biyinzika President of Uganda living in Kenya Association (UKEYA) who assisted me with data collection.

Lastly, I would like to thank my beloved mother for her continued support.

## ABSTRACT

The exchange of capital, goods and services across international borders or territories is known as international trade. This study focused particularly on the bilateral trade between Kenya and Uganda and the effects that certain barriers to trade have on the countries' economic integration. The study aimed at examining the effects of trade barriers on economy integration between Kenya and Uganda. A descriptive survey was conducted to collect detailed description of the existing status in Uganda. This was both qualitative and quantitative data collection. The research design was appropriate because of its purpose and objective, which was to collect detailed description of the existing status with the intention of employing data to improve the current conditions. The study involved the Uganda Embassy, Ministry of Foreign Trade and traders of both Kenyan and Ugandan nationality. For consistence it focused on relative individuals under common areas named. The study concludes trade barriers affected economic integration between Kenya and Uganda. The study concludes that a large trade potential exists between Kenya and Uganda and that trade liberalization through regional cooperation initiatives will enhance the realization of this potential. More appropriate trade policies are needed. While policies are being considered, and to some extent implemented, emphasis should be given to the elimination of trade obstacles, such as nontariff and institutional barriers, which increase transaction costs for importers and exporters. The study also concludes that there is need for support coordinated regulatory reforms and setting up of regional regulatory institutions as countries invest in regional infrastructure and liberalize trade in services. The objective of maximizing revenue collection through high tariffs is sometimes considered by governments in a short-term perspective and overrides other important criteria, such as efficiency in production through increased trade. The study recommends that infrastructure investments need to be complemented with trade facilitation measures for intra-regional trade to easily move across borders. Reducing bureaucratic requirements, streamlining border management procedures and implementing trade facilitation measures will reduce border crossing times. Own reforms will be required to harmonize and reform transport-related standards and policies affecting trade and, eliminate obstacles to the free movement of goods and services including service providers. The study also recommends that Uganda and Kenya should provide technical assistance to the industries and it should be provided free. It also recommends that governments should serve as a check on one another so that Kenya and Uganda commitment is seen as more credible than a national commitment. The focus on regional infrastructure development will further boost regional trade, investment and integration and make the region economically competitive.

## TABLE OF CONTENTS

<b>DECLARATION</b> .....	<b>ii</b>
<b>ACKNOWLEDGEMENT</b> .....	<b>iii</b>
<b>ABSTRACT</b> .....	<b>iv</b>
<b>TABLE OF CONTENTS</b> .....	<b>v</b>
<b>LIST OF TABLES</b> .....	<b>ix</b>
<b>LIST OF FIGURES</b> .....	<b>x</b>
<b>LIST OF ABBREVIATIONS</b> .....	<b>xi</b>
<b>CHAPTER ONE</b> .....	<b>1</b>
1.0 Introduction.....	1
1.1 Background of the Study .....	3
1.2 Statement of the Problem.....	5
1.3 Objectives of the Study.....	6
1.3.1 General Objective .....	6
1.3.2 Specific Objectives .....	6
1.4 Justification of the Study .....	7
1.5 Literature Review.....	8
1.5.1 Literature on Economic Integration .....	8
1.6 Conceptual Framework.....	10
1.7 Hypothesis.....	15
1.8 Research Methodology .....	15
1.8.1 Research Design.....	16
1.8.2 Target Population.....	16

1.8.3 Sample Design and Size.....	16
1.8.4 Research Instruments.....	17
1.8.5 Validity and Reliability of the Data.....	17
1.8.6 Method of Data Analysis.....	17
1.8.7 Scope, Delimitations and Limitations of the Study.....	17
1.9 Chapter Outline.....	18
<b>CHAPTER TWO:TRADE BARRIERS AND ECONOMIC INTEGRATION.....</b>	<b>19</b>
2.1 Introduction.....	19
2.2 Economic Integration Theory.....	19
2.2.1 Regional Integration.....	23
2.3 An Overview of Theoretical and Empirical Issues.....	25
2.4 Theoretical Framework.....	26
2.4.1 The Trade Simulation Model.....	26
2.5 Transitional Costs.....	29
2.6 Other Reasons for Integration.....	30
2.6.1 “Widening and Deepening” of Regional Integration.....	30
2.6.2 Trade Facilitation and “Behind the Border” Reforms.....	31
2.6.3 Public Goods.....	32
2.7 Overview of Trade Barriers in Kenya and Uganda.....	34
2.8 Barriers to Uganda’s Trade Within the Regional Trade Blocs.....	35
2.9 Tools for Economic Integration.....	38
2.9.1 Free Trade Area.....	38
2.9.2 Customs Union.....	39

2.9.3 Common Market .....	40
2.9.4 Economic Union .....	41
<b>CHAPTER THREE: HISTORICAL BACKGROUND OF THE KENYA AND UGANDA TRADE RELATIONS .....</b>	<b>48</b>
3.1 Introduction.....	48
3.2 The History of Kenya and Uganda Relations .....	48
3.3 Cross-Border Trade between Kenya and Uganda.....	48
3.4 Kenya and Uganda Convergence and Divergence in Regional Integration Agreements	55
3.4.1 Variations in Uganda’s Trade Patterns .....	56
3.4.2 Variations in Kenya’s Trade Patterns .....	58
3.5 Conclusions and Policy Concerns for the Future.....	64
<b>CHAPTER FOUR: TRADE BARRIERS AND THEIR EFFECTS ON ECONOMIC INTEGRATION FOR KENYA AND UGANDA .....</b>	<b>65</b>
4.1 Introduction.....	65
4.2 Trade Barriers between Kenya and Uganda .....	65
4.3 Experiences of Other Trade Blocks on the Elimination/Reduction of NTBs .....	66
4.4 Effects of Trade Barriers between Kenya and Uganda.....	68
4.4.1 Inadequate Information Barriers .....	69
4.4.2 Irregular Policies .....	70
4.4.3 Inefficiency of Ports.....	71
4.5 Conclusion .....	72
<b>CHAPTER FIVE: CONCLUSIONS AND RECOMMENDATIONS .....</b>	<b>73</b>
5.1 Introduction.....	73

5.2 Conclusions and Policy Concerns for the Future.....	73
5.3 Recommendations.....	74
<b>BIBLIOGRAPHY.....</b>	<b>78</b>



## LIST OF TABLES

Table 3.1: Selected indicators for Kenya and Uganda, 2011 (World Bank, 2012) .....	53
Table 3.2: Uganda's imports by country of origin, million USD .....	56
Table 3.3: Uganda's main export, million USD .....	57
Table 3.4: Kenya's imports by country of origin, million USD .....	58
Table 3.5: Kenya's exports by country of destination, million USD .....	59

## LIST OF FIGURES

Figure 2.1: Conceptual Framework .....	11
Figure 3.1: Uganda Trade Balance, million USD.....	54
Figure 3.2: Export of selected primary products as a ratio of total exports of goods from Kenya to Uganda <sup>1</sup> .....	60
Figure 3.3: Export of selected manufactures as a ratio of total exports of goods from Kenya to Uganda .....	61
Figure 3.4: Uganda's export to Kenya as a share of total export of goods, selected primary products .....	62
Figure 3.5: Uganda's export to Kenya as a share of total export of goods, selected manufactures .....	63

---

<sup>1</sup> UN Comtrade, 2012.

## LIST OF ABBREVIATIONS

CDS	:	Central Deposit System
CET	:	Common external tariff
CM	:	Common Market
COMESA	:	Common Market for Eastern and Southern Africa
CU	:	Custom Union
EABC	:	East African Business Council
EAC	:	East African Community
ECOWAS	:	Economic Community of West African States
EU	:	European Union
GATT	:	General Agreement on Tariffs and Trade
GDP	:	Gross Domestic Product
GSP	:	Generalized System of Preferences
IMF	:	International Monetary Fund
LDC	:	Least-Developed Countries
MFN	:	Most-Favoured Nation
NAFTA	:	North American Free Trade Agreement
NGO	:	Non-Governmental Organization
NTBs	:	Non-tariff barriers
PTA	:	Preferential Trade Agreement
ROO	:	Rules of Origin
RTAs	:	Regional trading arrangements
SADC	:	Southern African Development Community

SPS	:	Special and Differential Treatment
STABEX	:	Sanitary and Phytosanitary Standards
TRA	:	Trade-Related Assistance
Trips	:	Trade-Related Aspects of Intellectual Property Rights
UNCTAD	:	United Nation Conference on Trade and Development
WTO	:	World Trade Organization

## CHAPTER ONE

### 1.0 Introduction

Trade being the transfer of ownership of goods and services from one person or entity to another by getting something else in exchange; is normally carried out on a network which is the market. Sometimes known as commerce or financial transactions, trade has its own barriers that hinder these exchange activities. Originally the traders used the barter trade which was a form of a direct exchange of goods and services. Modern traders negotiate through a medium of exchange which is money. This medium simplifies trade, although currently it sometimes acts as a barrier in the economic integration. The invention of money (and later credit, paper money and non-physical money) greatly simplified and promoted trade. Trade between two traders is called bilateral trade, while trade between more than two traders is called multilateral trade<sup>2</sup>.

Trade exists as a result of specialization and division of labor, with most people concentrating on a small aspect of production, and opting to acquire other products through trade. One reason for trade between regions is the fact that different regions have different comparative advantages in the production of some tradable commodities. Also, the size of a particular region can give it an advantage of producing a particular product as a result of benefits obtained from mass production. As such, difference in market prices between locations brings about benefits of trade for both locations<sup>3</sup>.

An economy consists of the economic system of a country or other areas; the labour, capital and land resources; and the manufacturing, production, trade, distribution and consumption of goods

---

<sup>2</sup> Madison, James (1997) *The Federalist Papers, No. 10*. J. A. McLean, New York.

<sup>3</sup> IMF (2013b). *New Pacts Ease Path toward East African Single Currency*, IMF African Department, December 30.

and services of that area. A given economy is the result of a process that involves its technological evolution, history and social organization as well as its geography, natural resource endowment, and ecology, as main factors. A market based economy may be best described as a spatially limited social network where goods and services are freely produced and exchanged according to demand and supply between participants (economic agent) with a medium of exchange acceptable within the network.<sup>4</sup>

The exchange of capital, goods and services across international borders or territories is known as international trade. In most countries such trade represents a significant share of Gross Domestic Product (GDP). While international trade has been present throughout much of history, its economic, social and political importance has been on the rise in recent centuries. Industrialization, advanced transportation, globalization, multinational corporations and outsourcing are all having major impact on the international trade system. Increasing international trade is crucial to the continuance of globalization. Without international trade, nations would be limited to the goods and services produced within their own borders<sup>5</sup>.

International trade is, in principle, not different from domestic trade as the motivation and the behavior of parties involved in a trade do not change fundamentally regardless of whether trade is across a border or not. The main difference is that international trade is typically more costly than domestic trade. The reason is that a border typically imposes additional costs such as tariffs,

---

<sup>4</sup> Grossman, Gene M. and Elhanan Helpman (1991). *Innovation and Growth in the Global Economy*. The MIT Press.

<sup>5</sup> Giavazzi, Francesco, and Guido Tabellini (2005). "Economic and Political Liberalizations." *Journal of Monetary Economics*, 52, 1297–1330.

time costs due to border delays and costs associated with country differences such as language, the legal system or culture.

Another difference between domestic and international trade is that factors of production such as capital and labour are typically more mobile within a country than across countries. Thus international trade is mostly restricted to trade in goods and services, and only to a lesser extent to trade in capital, labor or other factors of production. Trade in goods and services can serve as a substitute for trade in factors of production.

### **1.1 Background of the Study**

This study focuses particularly on the bilateral trade between Kenya and Uganda and the effects that certain barriers to trade have on the countries' economic integration. For instance, lack of a harmonized central deposit system between Kenya and Uganda has been a great barrier to economic integration. The CDS is a computerized system that facilitates faster and easier processing of transactions for shares and bonds at the stock market. CDS account holders have up-to-date information on their holdings and the convenience of electronic securities transfers to facilitate trade settlement. CDS reforms would facilitate trade integration systems, harmonise local stock market laws and trading modalities among the East African countries in the perspective of regional integration. Ultimately, East Africans would be treated as local investors and not as foreign ones. It would also reduce the costs and time of buying or selling shares of those firms that are cross-listed at the various houses. This system will reduce the risk of trading in securities listed on the regional exchanges, boost investor confidence and facilitate greater access by enabling Internet trading.

Many of the regulations for international trade are in the form of non-tariff barriers to trade. These include rules, standards, and principles imposed by governments or industry groups designed to restrict and regulate the flow of goods and services. They are no less an impediment to trade than blanket prohibitions or taxes and tariffs. Random road blocks, entrenched bribery and bloated tariffs along the Kenya - Uganda corridor are seriously affecting the achievement of the ECOWAS Trade Liberalization Scheme (ETLS) and affecting inter-country trade within the sub-region. The ineffective implementation of the various trade protocols and ETLS collectively signed and agreed by ECOWAS members is costing the sub-region millions of dollars in trade forgone.

Non-Tariff Barriers (NTBs) have played a significant role in slowing the progress of integration process which has prompted Kenya to have bilateral negotiations with her neighboring Uganda to solve the challenges bilaterally with the aim of elevating the trade. Unfair trade treaties are also some of the barriers facing the integration. African leaders for example those from Kenya and Uganda have signed several unfair trade treaty agreements and joint-venture deals on behalf of their states - and many of these deals are in force for seemingly endless periods. It was the understandable desperation of African nations to fully integrate into the wider world economy that led them to hastily conclude often one-sided but legally enforceable treaties with several non-African states and other Western-dominated "international" bodies, such as the International Monetary Fund, the World Bank and the World Trade Organisation.

In Africa, legal obligations to these bodies are often taken more seriously than obligations to integration schemes within the continent. African nations are indebted to these bodies and their



countless affiliates, causing economic woes at home. Other barrier affecting the economic integration of Kenya and Uganda is the ongoing regions conflicts, the rising inflation, road blocks, lack of parking yards at boarder points, corruption along the northern and central corridors, lack of certifications as some items required certificates of origin while others do not and it varies with each state.<sup>6</sup>

## **1.2 Statement of the Problem**

The trade barriers have brought about a lot of inconvenience for traders between Kenya and Uganda Corridors. The lack of a harmonized central deposit system between Kenya and Uganda has been a great barrier to economic integration. This has made the processing of transactions slower and complicated and the account holders are not in a position to have up to date information on their holdings and their securities. The cost and time used for buying and selling shares is quite long and tedious and there is lack of investors' confidence.

Non-Tariff Barriers (NTBs) have played a significant role in slowing the progress of integration process which has prompted Kenya to have bilateral negotiations with her neighboring Uganda to solve the challenges bilaterally with the aim of elevating the trade. These NTBs include such thing as rules, standards, and principles imposed by governments or industry groups designed to restrict and regulate the flow of goods and services. They are no less an impediment to trade than blanket prohibitions or taxes and tariffs.

---

<sup>6</sup> Giavazzi, Francesco, and Guido Tabellini (2005). "Economic and Political Liberalizations." *Journal of Monetary Economics*, 52, 1297–1330.

Unfair trade treaties are also some of the barriers facing the integration. African leaders for example those from Kenya and Uganda have signed several unfair trade treaty agreements and joint-venture deals on behalf of their states - and many of these deals are in force for seemingly endless periods.

Presence of conflict between the two countries and inside their territories has brought a great impact on the economic integration for the two nations. Low levels of trade have been observed at the particular time when there has been unrest in the two countries and across their borders. These low levels of trade have in one way or another affected the GDP for both Kenya and Uganda. Inflation also has played a big role in hindering economic integration.

### **1.3 Objectives of the Study**

#### **1.3.1 General Objective**

The study aimed at examining the effects of trade barriers on economy integration between Kenya and Uganda.

#### **1.3.2 Specific Objectives**

- i. To establish the effect of unfair trade treaties on Kenya's economic integration with Uganda.
- ii. To examine the effect of CDS on the country's GDP
- iii. To find out the effect of NTBs on the Kenya and Uganda trade.
- iv. To assess the effects of inflation and regional conflicts on the economic integration between Kenya and Uganda.

#### **1.4 Justification of the Study**

A lot of emphasis has been put on the trade barriers, their magnitude and impact on the economic integration. However, more study has been done on the general impact on the barriers rather than specifically and exclusively examining the effects in different categories such as social, and others. This study aims to highlight the impact caused by the barriers over the years despite the signing of different treaties such as the common union treaty by Kenya and Uganda. The study will thus put emphasis on the specific four areas of unfair trade treaties which are harmonized Central Depository System, the Non-Treaty Barriers and the inflation and regional conflict on the economical integration of Kenya and Uganda.

While reporters, journalists and other researchers have mainly concentrated on day to day occurrences and activities by the international trade barriers, this research aims at connecting the academic perspective with the countries affected by the trade barriers.

This research certainly lays the foundation for further research in the area. Further research could explore specific rules and regulations to trade, the documentation and restrictions on import and export. Examining the effects of the barriers would also provide insight into the possible increased long-term effects of these barriers. In conducting a research such as this, we can pinpoint the precise effects of trade barriers and implement programs to offset the negative consequences.

The information which will be obtained after the study has been undertaken will offer useful literature to future students who will be undertaking research on trade barriers, International

trade treaties; as well as the governments of Uganda and Kenya, in order to formulate policies which will help bring a common and harmonized treaty.

## **1.5 Literature Review**

Literature review refers to analysis of written materials such as books, reports and journals by scholars and researchers. A lot of literature on the trade barriers has been mainly reports made by journalists and Institutions like the non-governmental organizations, on the day to day happenings on the effects of the trade barriers on the economic integration of Kenya and Uganda. However, not much research has been carried on why the barriers have continued to be on despite signing of numerous treaties by the two countries.

### **1.5.1 Literature on Economic Integration**

Economic integration is seen to be the unification of economic policies between different states through the partial or full abolition of tariff and non-tariff restrictions on trade taking place among them prior to their integration. This is meant in turn to lead to lower prices for distributors and consumers with the goal of increasing the combined economic productivity of the countries.

Economic theory shows free trade on a worldwide basis as the first best outcome, in as much as it allows specialization and exchange to take place globally, thus leading to greater world output and welfare. PTAs among a subset of countries are therefore a second best solution. They create trade among their members as trade barriers fall, and they divert trade from efficient non-member producers to members because of their privileged market access. It should be noted that PTAs can take a variety of forms. These range from low-level integration by means of FTAs or

CUs to higher levels of integration, such as a common market, economic (and monetary) union, or even economic and political union. A PTA also refers to two or more countries forming a union with lower tariffs (and other trade barriers) for goods and services from member countries<sup>7</sup>. FTAs eliminate tariffs on goods from members entirely, and CUs are FTAs with a common external tariff.

More specifically, economic integration proceeds by agreements to either; abolish tariffs and import quotas among members (FTAs and sectoral FTAs) or to establish common external tariffs and quotas (CUs). Other ways could also be by allowing free movement of goods, services and workers (Common Market), or harmonizing competition, structural, fiscal, monetary and social policies (Economic Union). Agreements can also be made to unify economic policies and establish supra-national institutions (Economic and Political Union).

Thus three progressively higher levels of integration can be distinguished. The first level entails modest integration by means of an agreement to apply symmetric preferential treatment of imports and assign supporting functions and instruments to jointly operated institutions.

Examples would be NAFTA's commitment to eliminate tariffs among its members, its dispute settlement provisions, and the various working groups and committees that serve to facilitate trade and investment among the three partners. In the case of a CU, the agreement would additionally involve a common external tariff applicable to non-members, which, in turn, requires an understanding on how to apportion among the partners the tariff revenue collected.

---

<sup>7</sup> ECA (2010). Assessing Regional Integration in Africa IV. Enhancing Intra-African Trade, Addis Ababa

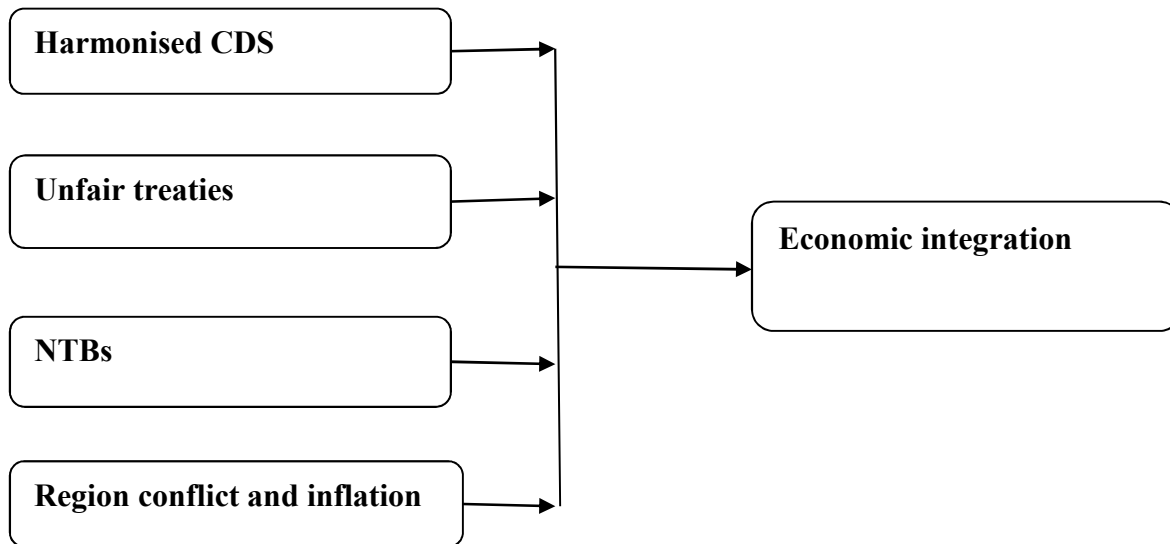
The second level of economic integration would be the harmonization of instruments over which the parties retain control, and through which, due to different national approaches, obstacles to a common market exist. This could be the case in the area of migration of workers, competition policy, and production standards. One example of such harmonization is the European Single Act. Among other provisions this act applied the “principle of mutual recognition” to product standards. More co-operation and supranational institutions, such as a joint tribunal on competition policy, are also characteristic of this second level.

The third and highest level of economic integration adds coordination of national policies and the creation of further supranational bodies which entail not only economic but increasingly political integration. Examples here are the creation of a common currency and central bank, and even a supranational parliament as in the case of the EU.

## **1.6 Conceptual Framework**

The research study uses the conceptual framework rather than the theoretical framework due to the lack of a specific set of reasoned propositions supported to explain the connection between trade barriers and the effects on economic integration. Currently there is no theory that captures the variables of the activities of trade barriers and economic impact on a country. Thus an important conceptual distinction is often drawn between trade barriers and the after effects.

The conceptual framework will thus help to substitute the theoretical structure to connect to the variables.

**Independent Variables****Dependent Variable****Figure 2.1: Conceptual Framework**

Since theory is a construct which assists in seeking and interpreting facts, Tidwell observes that theory in itself cannot overcome all obstacles, though it can help us to understand them. Therefore, a study of the efficacy of examining the effects of trade barriers on the economic integration in Kenya and Uganda will be of little practical utility unless it was contextualized within a broader conceptual framework which would assist in analyzing such approaches while allowing the drawing up of conclusions which would have wide applicability. It has been necessary to adapt a conceptual framework as it will allow linkages between the various management approaches to the networks whose complexity which mixes various actors, issues and interests has made the trade barrier resolution a nightmare to both practitioners and scholars. The independent variables in this study will be harmonized CDS, Unfair Treaties, NTBs and Region conflict and inflation.

## **Economic Integration**

The impetus for economic integration draws its rationale from the standard trade theory, which states that free trade is superior to all other trade policies. As an extension of this basic principle, therefore, free trade among two or more countries will improve the welfare of the member countries as long as the arrangement leads to a net trade creation though regional agreements do not guarantee an improvement in the welfare of member countries, they could do so provided that trade diversion is minimal and/or trade-creation tilts the balance.<sup>8</sup>

Despite their obvious differences, Kenya, and Uganda share many development challenges. The two countries are apparently undergoing the same demographic transition, with substantial lags but posing similar challenges to education systems and job markets. Economic growth constraints arising from weak infrastructure and energy supply are more or less serious across the region. Policies for market-based development have been improving, but too slowly for investment and employment needs to be met.

Failure to attract sufficient private capital and expertise into agriculture to transform the livelihoods of the poor majority of the population is a critical challenge in all the three countries. The political and economic systems of the countries differ. However, they also share some important features, which have persisted through time. In both countries, the quality of policy making is limited by the interest of politicians in the ‘discretion’ that incomplete economic

---

<sup>8</sup> Ndung’u, Njuguna (2000) ‘Regional Integration Experience in Eastern African Regions’  
Graduate Institute of International Studies, Geneva



liberalisation and imperfect regulation give them. The importance of discretion arises from the character of the political system, or the form of the state.<sup>9</sup>

### **Trade Barriers between Kenya and Uganda**

In practice, the identification of trade barriers is subjective as what appears as a Non-Trade Barriers (NTB) to one person is a legitimate activity to another (Tand 2003). However, there have been several approaches to NTB identification.

A survey of companies trading in Eastern and Southern Africa confirms that tariffs play a much less important role as a barrier to cross-border trade in Sub-Saharan Africa, than NTBs (Stahl, 2005). A report by the East African Business Council (EABC) ranked Kenya as the “worst offender when it comes to non-tariff barriers” with Ugandan exporters of dairy products to Kenya accusing “their bigger neighbour of imposing non-tariff trade barriers to block their produce from entering markets in Kenya.

Other incidences of Kenyan NTBs include holding Uganda milk at the border for prolonged period (up to weeks), a-34 percent protein level requirement for full cream powder milk yet the protein levels for cow milk are in the range of 25 to 26 percent, harassment of Ugandan transporters, blocking Ugandan chicks and excessive customs and administrative entry, advocacy for policy reforms to eliminate non-tariff barriers, excessive number of roadblocks between Mombasa and Ugandan eastern border entry points (Osere 2009).

---

<sup>9</sup> Epifani, Paolo and Gino Ganica (2009). “Openness, Government Size and the Terms of Trade.” *Review of Economic Studies*, 76, 629–668.

A series of EAC trade studies reported some major NTBs that included customs and administrative entry procedures barriers; sanitary and phytosanitary measures; technical barriers to trade, standards, inspection time spent, un-harmonized procedures for issuance of certification and other distribution related obstacles.

### **Transiting Procedures**

Uganda, being a landlocked country critically depends on its neighbours Kenya and Tanzania to provide it access to the sea and Trade Facilitation services which include rail, road, sea freight, port, clearing and forwarding services. Also the numerous weighbridges along the main road transport routes like the Northern corridor makes it difficult to transport goods to destination markets on time. The time and costs involved in accessing these services are considered uncompetitive, which act as NTBs.

### **Sanitary and Phytosanitary Measures**

Problems involved under this cluster include standards, time spent during inspection in export destination markets especially Kenya, and lack of harmonized procedures for issuance of certification marks within EAC.

### **Immigration Procedures**

Many Ugandans lack an EAC passport which makes it difficult to travel across borders in search of business opportunities. Also, work permits are a requirement in Tanzania and Kenya, making it difficult to open branches and therefore penetrate the markets of these two countries.

## **Police Roadblocks**

There are too many roadblocks along the major road transport routes, which greatly disrupts efficient movement of goods to the markets. Also, Ugandan exporters allege that Kenyan Police obstruct Ugandan transport trucks since they are not registered in Kenya, which acts as an obstacle in choosing the most competitive means of transport for Ugandan exports.

## **1.7 Hypothesis**

**The study answers the following propositions.**

- i. Common world treaties that have led to the formation of trade barriers which have become unfair treaties to countries especially in East Africa particularly to Kenya and Uganda.
- ii. The common CDS that has not been fully implemented causing a barrier and lack of transparency to the international traders especially in Kenya and Uganda.

The Ministries of Trade and foreign affairs, the Embassies and other trading bodies are effectively trying to control the barrier on the economic integration.

## **1.8 Research Methodology**

The chapter describes the research design, the sampling procedures, instruments, methods of data collection and data analysis. It also describes the techniques used in the presentation of the analyzed data.

### **1.8.1 Research Design**

A descriptive survey was conducted to collect detailed description of the existing status in Uganda. This was both qualitative and quantitative data collection. The research design was appropriate because of its purpose and objective, which is to collect detailed description of the existing status with the intention of employing data to improve the current conditions.

Surveys are conducted to establish the nature of the existing situation or condition. They help to describe the status of events and also help to collect data over large areas. The research was of survey nature and case study. The survey collects data which was analyzed quantitatively using descriptive and inferential statistics. In addition the data collected using a survey strategy was used to find the reasons for particular relationship between variables and to produce models of these relationships. Using a survey strategy gives a more control over the research in investigating the effects of trade barriers on economic integration of Kenya and Uganda.

### **1.8.2 Target Population**

The study involved the Uganda Embassy, Ministry of Foreign Trade and Traders of both Kenyan and Ugandan nationality. For consistence it focused on relative individuals under common areas named.

### **1.8.3 Sample Design and Size**

The population under investigation consists of the Uganda Embassy in Kenya, Ministry of Foreign Trade, Kenya Business Community and Uganda Business Community. This was done to gain a maximum degree of insight into the problem. Using simple purposive sampling, a sample

of 4 persons from each of the preselected areas was selected to be interviewed. The reason for using purposive sampling is that the study would only be targeting specific respondents who will have the necessary information needed.

#### **1.8.4 Research Instruments**

Interview schedule to collect data for the study. This is due to the fact that this is a qualitative research that aims to uncover detailed explanation on the subject area. This was used to collect information from diplomats and staff working in the Uganda Embassy in Kenya, Ministry of Foreign Trade, Kenya Business Community and Uganda Business Community.

#### **1.8.5 Validity and Reliability of the Data**

Piloting was done in one area; this is necessary to find the flow of the statement and interviews for the sample.

#### **1.8.6 Method of Data Analysis**

Data for this study was analyzed using descriptive statistics, tables and frequencies as well as percentages.

#### **1.8.7 Scope, Delimitations and Limitations of the Study**

The study concentrated specifically on the trade barriers on economic integration between Kenya and Uganda which is chosen as the case study.

## **1.9 Chapter Outline**

Chapter One is the foundation for the study and contains the background of the area of study, the statement of the problem, the objectives that the study sought to address and the methodology that was used.

Chapter Two gives an analysis of the theory and definition of integration with relation to Kenya and Uganda.

Chapter Three provides a historical background of the Kenya and Uganda trade relations.

Chapter Four focuses on the trade barriers and their effects on the economic integration for Kenya and Uganda.

Chapter Five presents the conclusions, possible recommendations and suggestions from the study done.

## CHAPTER TWO

### TRADE BARRIERS AND ECONOMIC INTEGRATION

#### 2.1 Introduction

This chapter looks into the concept of economic integration and the effects that certain barriers to trade can have on this integration; while examining various insights that previous scholars have pointed out.

#### 2.2 Economic Integration Theory

Regional trading arrangements (RTAs) alter the prices of imports from members (as tariffs are phased out) relative to imports from the rest of the world. Consequently, demand patterns will change, resulting in adjustments in trade and output flows. Will these changes be beneficial to participants in an RTA? Alternatively, will an RTA generate gains from trade? Viner (1950) investigated this question and found that the welfare impact of an RTA is ambiguous. Gains will occur if higher-cost domestic production is replaced by cheaper imports from a partner country—trade creation. But if partner-country production replaces lower-cost imports from the rest of the world; trade diversion there will be losses<sup>10</sup>.

Therefore, membership in an RTA will have positive and negative effects on an economy, and it is the net impact that will determine whether a member experiences welfare gains or losses. In assessing the static effects of forming an effective RTA three important principles from the theory of integration must be considered. First, the allocative or efficiency gains of economic

---

<sup>10</sup> Melitz, Marc J. and Gianmarco I. P. Ottaviano (2008) “Market size, trade, and productivity.” *Review of Economic Studies*, 75, 295–316.

integration depend on whether the products produced by members of the RTA are in direct competition with, or complementary to, each other<sup>11</sup>.

For there to be competitive economies or efficiency gains in an RTA, there must be a considerable overlap in the range of commodities that members of the RTA produce. The creation of an RTA where there exists overlapping production with significant differences in production costs between members can lead to large gains from trade as resources are allocated more efficiently among member countries. Intra-industry trade (for example, Ford cars for Honda) characterizes most trade between industrial economies, and the formation of an RTA is likely to lead to competitive gains.

The economies of members of an RTA can also be both competitive and complementary. For example, in the North American Free Trade Agreement (NAFTA), the United States and Mexico have important industries but compete directly against each other; for example, textiles and clothing and consumer electronics. To some extent, the two economies are also complementary. In these circumstances, members can derive efficiency gains from an RTA but, to avoid trade diversion, must keep their external tariffs low<sup>12</sup>.

States and Canada (members of a free trade agreement FTA), and Australia and New Zealand (also members of an FTA) are competitive economies and that there were significant gains from trade. It is questionable whether the developing country members of a large number of RTAs can

---

<sup>11</sup> Ottaviano, Gianmarco, Takatoshi Tabuchi, and Jacques-Francois Thisse (2002) "Agglomeration and Trade Revisited." *International Economic Review*, 43, 409–435.

<sup>12</sup> Foroutan, F., 1992. Regional Integration in Sub-Saharan Africa. World Bank Policy Research Working Papers1, Issue WPS 992.



be characterized as competitive economies. Typically, members of developing country RTAs have a narrow range of exports of goods and services, invariably primary commodities that are exported to industrial countries often under unilateral preferential arrangements. Therefore, there is little scope for efficiency gains<sup>13</sup>.

Economies whose structure of production is not competitive tend to be complementary and both benefit and loss from RTAs. Complementarities exist when members of RTAs produce commodities or products that do not compete much with the local production of other RTA members. Traditional integration theory contends that, in the case of complementary economies, economic integration will have the usual trade diversion and trade creation effects; the higher the barriers to trade with non-members, the higher the risk of trade diversion. Intuitively, one can argue that complementarities exist between developed and developing country members in an RTA (that is, North/South RTAs).

Trade between industrial countries and many developing countries is often characterized as trade in homogeneous products, for example, wheat for textiles. In this case, each country will have a comparative advantage in the export of a different type of goods, while all goods will be consumed by all member countries. The proposed regional economic partnership agreements that are part of the Continuous Agreement between the EU and the member states of the Africa, Caribbean and Pacific (ACP) region might be characterized as RTAs between complementary economies.

---

<sup>13</sup> Foroutan, F., 1992. Regional Integration in Sub-Saharan Africa. World Bank Policy Research Working Papers1, Issue WPS 992.

Outside Africa, the US and the EU appear at the center of many new integration arrangements, raising the specter of a world of trade mega-blocs (Crawford and Laird, 2000). Any economic gains for countries that are successful in creating an RTA with one of the larger economies will come partly at the expense of countries which are unable or unwilling to do so. A ‘domino’ effect may drive outsiders to seek their own preferential agreement at a later stage. The addition of these late comers may be resisted by the incumbents who might interpret a widening of the RTA as diluting their earlier welfare gains also the emerging mega-blocks ignore, for the most part, the least-developed countries, particularly those in sub-Saharan Africa and South Asia<sup>14</sup>.

The EU’s willingness to transform non-reciprocal preferences under the Cotonou Agreement into reciprocity-based Economic Partnership Arrangements is an obvious exception to this generalization. Their conclusion must also be qualified by noting that both the US and the EU offer non-reciprocal preferential access to many of these countries through, for example, GSP schemes, the Cotonou Agreement, the US Trade and Development Act, and the EU’s Arms initiative. However, these preference schemes are unilateral and do not extend to the deeper areas of integration now increasingly common in RTAs.

North-South RTAs have been seen as more likely to result in gains to developing countries as compared to South-South RTAs, on the grounds that they minimize trade diversion costs and maximize the gains from policy credibility. Closer examination of these arguments, however, suggests that the assumptions on which they are based may not always stand up. Positive

---

<sup>14</sup> Crawford and Laird (2000)

economic outcomes will depend on the deliberate design of these agreements, and cannot simply be assumed.

### **2.2.1 Regional Integration**

The past experience of developing countries with regional integration schemes is not a happy one. The reasons for this can be illuminated with the aid of the simple theory of customs unions outlined in this chapter. Preferential trade arrangements give rise both to trade creation and trade diversion effects, as well as to transfers between the member countries. The design of RTAs among developing countries in the past tended to maximize the costs of trade diversion (because of high external tariffs) and also encouraged regressive transfers from poorer to better-off members of such arrangements.

The recent more favorable assessment of regional integration arrangements involving developing countries is based on various considerations. Regionalism will lead to net trade creation as long as it is coupled with a significant degree of trade liberalization and where emphasis is put on reducing cost-creating trade barriers which simply waste resources. Regional economic integration may be a precondition for, rather than an obstacle to, integrating developing countries into the world economy by minimizing the costs of market fragmentation<sup>15</sup>.

Regional integration may also be pursued to provide the policy credibility which is necessary to attract investment inflows. For those who emphasize this effect, North-South arrangements are to

---

<sup>15</sup> Foroutan, F., 1992. Regional Integration in Sub-Saharan Africa. World Bank Policy Research Working Papers1, Issue WPS 992.

be preferred to South-South agreements which are unlikely to generate significant credibility gains.

The trading patterns of the EAC members indicate that trade linkages are relatively weak. Therefore; one cannot really characterize the economies as either complementary or competitive. Khandelwal (2004) developed estimates of bilateral product within COMESA, product complementarities between Kenya's exports.

It is questionable whether the developing country members of a large number of RTAs can be characterized as competitive economies. Typically, members of developing country RTAs have a narrow range of exports of goods and services, invariably primary commodities that are exported to industrial countries often under unilateral preferential arrangements. Therefore, there is little scope for efficiency gains.

The growing propensity of RTAs to include aspects of policy integration also poses a challenge for developing countries. Although these aspects are most common in RTAs involving high-income countries, a growing number of North-South agreements now have broad integration objectives. The removal of non-tariff barriers which act to segment markets can be potentially beneficial, but whether this turns out to be the case in practice will depend on the nature of the policy integration.

### **2.3 An Overview of Theoretical and Empirical Issues**

The impetus for regional integration draws its rationale from the standard trade theory, which states that free trade is superior to all other trade policies. As an extension of this basic principle, therefore, free trade among two or more countries will improve the welfare of the member countries as long as the arrangement leads to a net trade creation in the Vinerian sense. That is, as the theory of the second best indicates, regional agreements do not guarantee an improvement in the welfare of member countries, they could however do so provided trade diversion is maximum and/or trade creation tilts the balance.

Historically, the customs union theory (in the context of which economic integration issues are discussed) was concerned with welfare gains and losses that follow the formation of customs union.

The traditional theories of trade, which assume constant returns to scale and focus on static gains, provide a limited practical insight to regional integration policy issues, in particular in developing countries such as in Africa. Even the theoretical insights of the more recent trade theories do not fare better. For instance, ‘economic geography’ models which attempt to explain the determinants of regional concentration of economic activity, is yet to be fully explored and its practical relevance to be tested (particularly in the African context)<sup>16</sup>.

---

<sup>16</sup> Krugman’s (1991)

## **2.4 Theoretical Framework**

This study takes a look at the Trade Simulation Model in relation to trade policies and agreements, particularly between Kenya and Uganda.

### **2.4.1 The Trade Simulation Model**

Partial equilibrium models are widely used to simulate and measure the effects of changes in trade policy. The models assess the effects of specific changes in tariffs or other trade taxes on trade flows, revenue, prices, and some measures of welfare (consumer surplus) at a given point in time. Typically, a simulation model based on simple Vinerian customs union theory is employed. To gauge the likely effects of introducing the new EAC CET, including the removal of tariffs on Kenyan imports from Tanzania and Uganda, that will lower external tariff rates, a static partial equilibrium methodology—SMART—was employed<sup>17</sup>.

Notably, SMART, unlike some partial equilibrium models, assumes that products imported from different regions are imperfect substitutes for each other. The World Integrated Trade Solution (WITS) software developed by the World Bank was used to conduct the simulations. WITS utilizes the UN Statistics Division COMTRADE and the UNCTAD Trade Analysis and Information System (TRAINS) databases that provide access to data on trade flows<sup>21</sup> and most-favored nation (MFN) tariff rates at the HS six-digit level of disaggregation. World Bank staff and the Kenya Revenue Authority provided information on the tariff preferences offered to COMESA partners and the negotiated CET.

---

<sup>17</sup> Foroutan, F., 1992. Regional Integration in Sub-Saharan Africa. World Bank Policy Research Working Papers1, Issue WPS 992.

The SMART simulations were done using the WITS software. The simulation results produced by SMART indicate that the move from the current MFN tariff rates to the three-band EAC CET is likely to have a positive impact on trade with an increase in trade of millions with trade creation estimated at millions and trade diversion at millions. The impact on trade and the estimated trade-creating and trade-diverting trade flows for all products in each tariff band (i.e., 0 percent and 25 percent). The trade creating flows results from the move to the new EAC CET are accounted for by products that attract a 0 percent tariff rate. Trade creation has a positive effect on welfare because consumers can purchase cheaper imports instead of more expensive local goods. However, it means import-competing producers will need to become more competitive or move into new product lines. These sectoral adjustments are the transitional or adjustment costs of lowering trade barriers<sup>18</sup>.

The move to the maximum tariff rate of the EAC CET results in trade creation estimated at millions. The model reports the results as negative trade creation, but this really reflects lower trade flows resulting from higher tariff rates. In other words, this means that the new EAC CET led to higher tariff rates for some of these product lines, and that with higher import prices, import flows declined. Further examination of the individual product tariff lines, revealed that many products that attracted a 15 percent MFN tariff rate now face the maximum tariff rate. Notably, some of these products—fish, pigs, black tea, yeasts, pictures and designs, and steel products—are produced locally in their respective countries, hence there is a protectionist objective.

---

<sup>18</sup> Epifani, Paolo and Gino Ganica (2009). “Openness, Government Size and the Terms of Trade.” Establishment of the African Economic Community, Academia.edu.

Another important feature is the negligible trade diversion resulting from the new EAC CET. An important factor that might be affecting the quantitative results is that the baseline Kenyan imports from Uganda reported in the official statistics significantly underestimate intraregional trade because of the prevalence of unrecorded informal cross-border trade. Mkenda (2001) cites surveys that indicated that in the 1994-95 periods, unofficial cross-border trade between Kenya and Uganda was about 49 percent of official trade. Between Tanzania and Kenya, cross-border trade as a percentage of official trade in the 1995-96 period was about 12 percent, and between Tanzania and Uganda it was about 45 percent.

The simulation results provide preliminary evidence that the EAC customs union will have positive trade benefits for Kenya because the adoption of the EAC CET will lead to increased flows of cheaper extra regional imports that are likely to lower consumer prices with positive welfare effects. Note that in the simulation, the removal of internal tariffs was accompanied by a lowering of MFN tariffs with the adoption of the EAC CET.

A World Bank (2000) study concluded that regional integration arrangements (RIAs) between developing countries (South-South RIAs) that provide preferential access to member states but keep external trade policy with respect to the rest-of-the-world unchanged are likely to lower welfare for the bloc as a whole. High external tariffs encourage trade diversion and provide strong incentives for inefficient firms to expand. Fundamentally, high external barriers negate the benefits from increased competition. Therefore, to ensure that an RTA does not encourage inefficiency, facilitate trade diversion, and ultimately reduce economic welfare, it is essential to lower MFN tariffs as barriers to intra-RTA trade are eliminated. Therefore, Kenya could



continue to derive benefits from progressively lowering trade barriers, specifically the EAC CET<sup>19</sup>.

## **2.5 Transitional Costs**

Despite the potential benefits from liberalization of the trade regime, there are costs that would have to be addressed. As noted earlier, trade creation means that the import-competing sectors would face increased competition and would need to make adjustments to improve efficiency and overall competitiveness. Consequently, there may be transitional output and employment losses associated with the EAC customs union. Policies would need to be put in place to minimize the dislocations caused by the lowering of tariffs. For import-competing sectors to respond to increased competition from cheaper imports, it is vital that Kenya, over the medium term, sustains the implementation of a comprehensive package of macroeconomic and structural reforms to improve efficiency and international competitiveness. This would include things like strong governance policies to improve transparency and accountability and eliminate corruption; strengthening the efficiency of the financial system; labor market reforms to increase labor market flexibility; an accelerated program of parastatal reform and privatization to increase efficiency and private sector involvement in the economy; and prudent fiscal policies to ensure that adequate resources are devoted to infrastructural development and improving the levels of education and health among others.

A poverty and social impact analysis (PSIA) of trade reforms is planned by the authorities and could provide the basis for programs to address these concerns. The customs union is expected to

---

<sup>19</sup> Ottaviano, Gianmarco, Takatoshi Tabuchi, and Jacques-Francois Thisse (2002) “Agglomeration and Trade Revisited.” *International Economic Review*, 43, 409–435.

result in revenue losses. The SMART simulations estimated that the full implementation of the EAC CET in Kenya would result in customs revenue losses of US\$113.3 million. An earlier analysis by the World Bank (2003) projected possible revenue losses from the proposed three-band structure (0,10,25) in millions for Kenya. The empirical evidence thus suggests there will be short-run revenue losses from the full implementation of the EAC customs union and policymakers have to design policy responses to recoup revenue losses. World Bank (2003) estimated that in Kenya customs exemptions amount to 22 percent of potential customs revenue, so to compensate for revenue losses, policy makers could streamline<sup>20</sup>.

## **2.6 Other Reasons for Integration**

In addition to economic growth, there are other driving forces behind the movement for integration.

### **2.6.1 “Widening and Deepening” of Regional Integration**

From a Kenyan perspective, some commentators see the recently established EAC customs union as providing an impetus to the COMESA customs union. Uganda being a member of COMESA, it is felt that the EAC group led by Kenya could set the EAC CET as the goal for the COMESA customs union and be the prime force in the negotiations. A wider COMESA customs union is attractive to Kenya because it provides a larger market to encourage the expansion of its manufactured or non- traditional exports to the region.

---

<sup>20</sup>World Bank (2003) World Development Indicators, Washington D.C.

Another important factor might be the “Economic Partnership Agreements” (EPAs) that are to be negotiated between the European and sub-Saharan Africa countries. The Cotonou Agreement provides for the negotiation of reciprocal trade agreements between various geographical configurations in sub-Saharan Africa and the EU covering trade in goods and services and some trade-related areas. Currently, the regional groupings identified to negotiate EPAs include COMESA. The EAC has not been identified as a regional grouping for the negotiations. However, if the EAC is able to drive the negotiations for a COMESA customs union, it could be an important partner in the negotiations with the EU. Potentially, this is the most important regional agreement Kenya will negotiate because it offers a favorable opportunity for sub-Saharan Africa countries to integrate into the global economy and to benefit from deeper integration with a developed region.

### **2.6.2 Trade Facilitation and “Behind the Border” Reforms**

Small and/or poor developing countries can pursue enhanced trading arrangements including outside the framework of an RTA by deepening cooperation in trade facilitation and “behind the border” reforms. An important question is whether more intensive regional cooperation in trade-related areas such as trade facilitation and “behind the border” reforms—those areas include sanitary and phyto-sanitary (SPS) standards, technical standards, investment code, competition law and intellectual property rights—is likely to expand trade and raise economic growth by increasing efficiency as well as private investment (domestic and foreign). Conceptually, adopting and implementing simple, transparent import and export regulations and efficient procedures for customs clearance will reduce transaction costs and enhance efficiency in EAC member countries and improve the environment for trade expansion. “Behind the border”

reforms are increasingly an important part of the international trade architecture and of growing importance in the multilateral trade negotiations in the WTO<sup>21</sup>. These reforms place great demands on a country's human resource and institutional capacity, and it seems intuitive that regional approaches will be beneficial for sub-Saharan Africa countries with limited human resources and weak administrative capacity.

### **2.6.3 Public Goods**

Regional cooperation on public goods—such as water basins (lakes, rivers), infrastructure (roads, railways, and dams), the environment, hydroelectric and other sources of energy, and fisheries—can generate benefits for member states. In the case of the EAC member states there is a lot scope for cooperation in these areas and support can be received from the World Bank together with other multilateral, regional, and bilateral agencies.

Kenya and Uganda have undertaken trade policy reforms that have consisted of liberalization of their trade regimes at both the regional and global levels. As they have promoted more open and liberal trade policies the three countries have simultaneously embarked upon a process to integrate their economies through the creation of the East African Community (EAC)<sup>22</sup>.

The formation of the EAC customs union is an important step in the process of deepening regional integration. Generally, RTAs between competitive and/or complementary economies have resulted in positive static and dynamic benefits for the participating countries. However,

---

<sup>21</sup> World Bank (2003) World Development Indicators, Washington D.C.

<sup>22</sup> Yang, Y. & Gupta, S. (2005). Regional Trade Arrangements in Africa: Past Performance

many RTAs between developing countries are not between economies that have these characteristics, and the results have been disappointing.

The trade linkages among the three EAC member states are not strong. However, the establishment of the EAC customs union and the introduction of the EAC CET do seem to have potentially positive benefits for Kenya. The results from a SMART trade simulation model suggest that the EAC CET, by lowering tariffs, has a positive impact on trade largely from trade creation. Lower tariffs result in lower import prices and increased flows of cheaper imports that improve consumer welfare.

However, there are still the transitional costs discussed earlier that must be addressed to minimize economic dislocation, including revenue losses. Furthermore, trade creation means the import competing sectors will face increased competition from cheaper imports, and producers will have to improve efficiency and competitiveness. Sustained macroeconomic and structural reforms will be needed to ensure that a favorable enabling environment is created that will facilitate internationally competitive production.

In summary, these factors beyond trade integration should be considered by Kenyan and Ugandan policy makers while pursuing a closer East African integration. These are; first, the widening and deepening of regional integration with other countries in the Eastern and Southern African region through COMESA and the negotiation of an EPA between COMESA and the EU, with its centerpiece being a comprehensive regional trade agreement. Second, regional cooperation in trade facilitation and “behind the border” reforms offer potential benefits to

Kenya. Improvements in trade facilitation can improve transparency, reduce the costs of doing business, and promote trade. Regional cooperation in implementing “behind the borders” reforms, which are an increasingly important part of the architecture of the international trading system, can improve efficiency and facilitate trade in goods and services. Finally, regional cooperation in public goods can, among other things, lower the cost of infrastructural development, promoting growth and development<sup>23</sup>.

## **2.7 Overview of Trade Barriers in Kenya and Uganda**

Although there has been much progress in trade liberalization within the EAC and COMESA, a range of reforms still need to be addressed, especially nontrade measures hindering full exploitation of the trade potential within these blocs. A number of attempts have been made and are now underway to deal with some of the trade barriers within the blocs. However, many of the efforts require more resources and political will aimed at addressing issues of poor physical infrastructure to reduce the cost of transportation, as well as facilitating the free flow of trade within the region.

Another challenge is the slow implementation of the member states’ commitments to eliminate tariff and nontariff barriers. The current tariff barriers refer to category B products (i.e. products that are considered particularly sensitive to competition from other countries, including for example agricultural products and various manufactured goods), which were granted asymmetrical tariff liberalization among the EAC partner states, on Kenyan products. The common\ nontariff barriers still prevailing within the two blocs include the major impediments

---

<sup>23</sup> Institute of International Affairs, Johannesburg, South Africa. Organization for Economic Co-operation and Development (OECD) (2013). Development aid at a glance. Statistics by region

of cumbersome customs documentation and clearance procedures, border controls, transportation and transit traffic regulations, visa requirements and corruption.

The primary barrier to Uganda's trade with its regional partners is the poor physical infrastructure development in terms of quality, maintenance and connectivity within the region. The railway and road networks linking Uganda to its regional partner states remain in poor condition. Their connectivity also remains limited to EAC and COMESA partners. These deficiencies have increased trade transaction costs and depressed trade opportunities within the region.

## **2.8 Barriers to Uganda's Trade Within the Regional Trade Blocs**

The first issue is the persistent interference with ground transportation, especially truck transportation, which is characterized by arduous customs and roadblock checks. For example, it takes four and five days, respectively, to secure export and import customs clearance and technical controls in Uganda. In addition, there are about six truck scales from Mombasa to Malaba, including those in Mariakani, Narok (mobile), Gilgil (Static), Eldoret (mobile), Webuye (static) and Amagoro (mobile, but permanent). In Uganda, there are three truck scales between Malaba and Kampala located in Malaba (permanent) just before customs, Busitema (permanent) and Iganga (mobile).

The second issue is the barrier to Uganda's trade with its regional partners is the poor physical infrastructure development in terms of quality, maintenance and connectivity within the region. The railway and road networks linking Uganda to its regional partner states remain in poor

condition. Their connectivity also remains limited to EAC and COMESA partners. For example, Uganda lacks railway connection to African countries in the EAC and COMESA partner states. Likewise, Kenya lacks the same infrastructural linkages. These deficiencies have increased trade transaction costs and depressed trade opportunities within the region. For example, inland transportation and handling for Uganda costs \$2,150 during exportation and importation (World Bank and International Finance Corporation 2011). However, other landlocked countries in East Africa suffer similarly, for export-related costs.

There are about 13 checkpoints in Kenya staffed by security agencies (mainly Kenyan police and administration police), which are located in Mombasa (town exit), Miritini, Mazeras, Voi, Konza, Athi River (before the truck scale), Mau escarpment, Mai-Mahiu, Gilgil, Salga, Timborwa and Kandui. Likewise, in Uganda, there are more than seven checkpoints, which include Malaba (Special Protection Revenue Unit, SPRU), Busitema (Uganda Revenue Authority, URA), Busitema (Police, 1 kilometer from URA checkpoint), Kitende (police), Lukaya (URA/SPRU), Kyazanga (police), Mbarara (URA) and Kabale (police). These holdups act as avenues for corruption, consequently undermining the efforts toward trade facilitation practices at border entry and exit points, roadblocks and truck scales (Uganda Freight Forwarders Association 2011).

This restriction undermines the free movement of people within the region. Similarly, in terms of capital movement,—among others, according to the EAC Protocol on the Movement of Capital, the purchase of foreign securities locally by nonresidents, the sale or issuing of debt securities locally by nonresidents, the sale or issuing of debt securities abroad by residents, the purchase



and sale of money market instruments locally by nonresidents and the purchase or sale of money market instruments abroad by residents.

The EAC and largely COMESA partner states are currently entwined in exporting substitutable products rather than complements. For example, all the EAC partner states export to each other, inter alia, plastics, dairy products, food stuffs, soap products, cement, paints and varnishes, and vegetable, fats and palm oil. This has generated unnecessary competition within the single market, which in turn has limited the gains from trade, especially for Uganda because it is landlocked and incurs more production costs for the transportation of some raw materials.

Uganda needs to rapidly diversify its exports, especially in the services industry, in order to reap the gains of integration. Uganda first and foremost needs to address the stock and quality of its physical infrastructure affecting the efficiency of its producers and traders. This will require extensive investment in the road, railway and energy sectors. This could be done more effectively, especially for the energy sector through a public–private partnership framework, which seems to be the current alternative.

However, this should be done in rationalized formulas, that is, with appropriate laws and policy strategies to guide the process. Likewise, with regard to the road and rail infrastructure, there is a need for a joint venture among the partner states to combine their resources to construct highways and rail networks that would connect regional markets. These barriers can be indefinitely removed or eliminated through political interventions. However, the staffs of the committees that are charged at national levels with monitoring the elimination, of these barriers

are made up of mere civil servants who do not have any political authority to ensure enforcement. Therefore, the political heads need to strengthen institutions with sufficient political authority to deal with such barriers to improve trade flow.

The free mobility of skilled labor is a prerequisite for open trade, there is a need to ease and adjust the respective partner migration policies toward skilled labor to facilitate the flow of labor and to address persistent skills shortages in specific fields. This would help foster regional trade and raise competitiveness.

Creating a common market means removing obstacles to the free movement of both labour and capital. Freer labour movement is seen as highly desirable in Uganda and Kenya, and could have important developmental benefits in Uganda. However, it is politically sensitive, especially in Uganda, so the negotiations may be difficult. Harmonization of taxes and investment incentives may be easier, and there is much to be gained from it, both in promoting the region as an investment destination and in enabling more competition among investors and potential investors.

## **2.9 Tools for Economic Integration**

There are various ways in which Kenya and Uganda can improve trade between both countries.

### **2.9.1 Free Trade Area**

This is the preferred option for countries embarking on economic integration and for those unwilling or unable to engage in higher levels of integration. An FTA can be limited to particular

sectors, thus retaining a high level of control at the national level and preventing exposure to competition for the other sectors. The authority to decide how third countries are to be treated remains unaffected (independent trade policy) in an FTA. However, rules of origin (ROO) have to be agreed upon among members so as to determine which products can be transferred duty-free. In the case of NAFTA a product has to have been substantially transformed so that a change in tariff classification has occurred, or it must have 50% (62.5% for cars) member-country content<sup>1</sup> to qualify for duty-free treatment. There are extensive and complex provisions on how such content is arrived at and what documentation is necessary at the border. If there were no such ROO third country, products could be landed in the lower duty jurisdiction and then transferred duty-free to the higher tariff member thereby circumvent its tariff. As a result, in an FTA border controls are necessary for commerce among members, and arguments over interpretation of ROO can lead to delays and disputes. These restrictive effects of ROO have led one eminent economist to observe: “It is reported that Canadian producers have on occasion chosen to pay the relevant duties rather than incur costs of proving origin.” (Krueger, 1995).

### **2.9.2 Customs Union**

When two or more countries agree to remove (essentially) all restrictions on mutual trade and set up a common system of tariffs and import quotas vis-à-vis non-members, the result is referred to as a CU. The adoption of a common external tariff (CET) and joint quotas necessitates closer cooperation with respect to the sharing of customs revenues collected on non-member imports. Rules of origin are no longer necessary: when a common external tariff exists, imports into the CU-area face the same tariff in each CU-member country; hence there is no incentive for transshipment of imports between members. The CET effectively creates “destination-neutrality” for

imports into the CU. Both FTAs and CUs imply that the member countries remain nation states, yet when viewed in the historical context there are some subtle differences between the agreements.

Nevertheless, it was recognized at the time that free trade and the consequent rationalization and specialization of production in coal and steel products would require a supranational body to regulate pricing practices and commercial policies. This historical precedent therefore suggests that a successful CU implies a common competition policy. Subsequently the European Common Market naturally adopted and extended this competition policy.

A common competition policy would replace the need for, and the application of, trade remedy laws among the CU-members. Predatory pricing (dumping) would be dealt with by the common competition watchdog, and Article 19 of the GATT/WTO could be relied upon to obtain temporary relief from import surges that threaten an industry's survival.

That said, the key feature of a CU remains the CET. Derivative issues are a matter of negotiation and will determine how successful the CU is.

### **2.9.3 Common Market**

A common market (CM) can be considered the first stage of deep economic integration. Free mobility of the key participants in the process of production is its characteristic. In addition to goods and services, capital and people move freely inside a common market. The benefits expected consist of further gains in efficiency through a more appropriate allocation of resources: capital moves to where skills are and people move to where opportunities beckon.

In addition to the common external tariff that defines a CU and to ensure the viability of a common market, uniform regulations have to be worked out among the members regarding the movement of people and capital. This is a major task that requires, at least over time, agreement on qualifications and certifications of workers from different member countries.

For a common market to become effective, therefore, co-operation in decision-making is required in yet more areas. Non-tariff barriers have to be dismantled, structural adjustment policies have to be jointly reassessed, distribution policies will face harmonization pressures, and fiscal and monetary policies, as a dynamic consequence or by design, will show greater convergence. This convergence results from the increased economic interdependence among the members and necessitates that greater consideration be given to the effects of national policies on the welfare of CM partners.

#### **2.9.4 Economic Union**

The next step in deep economic integration, economic unions, add to the common market harmonized fiscal, monetary and labor market policies. Tax and monetary policies affect where a business locates, and because labor market policies affect migration patterns and production costs, these will have to be streamlined among members. There will be no room for different national transportation, regional or industrial policies, as these distort competition among firms from different member countries.

To achieve such a union, it is necessary to form supranational institutions that legislate the rules of commerce for the entire area, leaving the administration to national bodies, but with recourse

to supranational administrative tribunals to ensure uniform application of these rules. In an economic union supranational commercial law replaces national law.

For example, the European Union's (EU) regional adjustment policy provides infrastructure funds to regions within the EU that have 75% or less of the average EU-income level, with a budget of 0.45% of the EU's GDP. This illustrates the degree of co-operation necessitated by an economic union.

An economic union is made more effective, furthermore, by a common currency. When there is no uncertainty about exchange rates among members, location decisions and trade patterns will follow efficiency considerations, and borrowing costs will not be affected by an exchange risk premium on a particular member country's currency<sup>24</sup>.

At this level of integration pressures for uniform taxation policies will increase even if agreement on such may prove elusive as shown in the case of Europe. The final outcome of economic union may well be a political confederation with unified economic policies. Economic union will stop short of political union if no supra-national bodies regarding defense and foreign policy are created.

Contrary to the previous literature which treats political integration as an alternate way of increasing the size of the economic market, we find that economic and political integration can function as complementary institutions. When firms engage in both innovation and unproductive

---

<sup>24</sup> Institute of International Affairs, Johannesburg, South Africa. Organization for Economic Co-operation and Development (OECD) (2013). Development aid at a glance. Statistics by region.

rent seeking, changes in the economic and political markets alter the benefits of each type of activity. By considering political integration as an increase in the size of the political market—and independent of the size of the economic market—we see that it has an ambiguous effect on innovation, growth, and welfare. The results for economic integration on its own are similar. It increases competition for market share, which tends to increase a firm's incentive to innovate<sup>25</sup>. But it also eliminates some of the regional firms, reducing competition and making rent seeking more attractive for the remaining firms. The overall effect on innovation, growth, and welfare is ambiguous. Whether political or economic integration alone increase growth and welfare will depend on the relative level of competition in each market. Joint integration makes both the political and economic markets more competitive without altering the incentives across these markets. Innovation becomes more attractive and growth and welfare increase.<sup>26</sup>

Other arguments that have recently emerged in the literature on globalization and political structure: first, the view that integrated economic markets need political as well as legal and social institutions for their effective functioning. Second, the view that the proliferation of borders reduces trade (and, therefore, growth) even when countries share culture, language, and institutions and third, the view that globalization is creating new policy externalities and that this leads national governments to choose worse economic policies<sup>27</sup>.

The work of Alesina, Spolaore, and Wacziarg (2000) has markedly different results from our model (namely that economic integration should be accompanied by political disintegration), the

---

<sup>25</sup> Grossman, Gene M. and Elhanan Helpman (1991). *Innovation and Growth in the Global Economy*. The MIT Press.

<sup>26</sup> Brink 2000. *The Integration Into Global Financial Markets*. Puchefstroom South Africa

<sup>27</sup> Baldwin, R. E., 2003. What Caused the Resurgence of Regionalism? *Swiss Journal of Economics and Statistics*, 131(3), pp. 453-463.

two works should be seen as complementary. Governments engage in a multiplicity of activities. In some of these activities (e.g. education, cultural policy) heterogeneity of policy preferences may be extremely relevant. In other policy areas (e.g. subsidies, market regulation) rent seeking might be pervasive.

The free trade flows that have powered robust global economic growth since the end of World War II are increasingly coming under threat. If left unchecked, a wave of trade-distorting regulation will harm people in the developing world, particularly small farmers in poor countries.

Consider that the World Trade Organization found that the Group of 20 (G-20) economies – the world's biggest, which account for a vast majority of the world's economic output and trade – added 124 new restrictive measures to international trade between April 2011 and April 2012. These are the countries that have benefited most from lower trade barriers. It appears some in these nations now want to prevent others from enjoying the blessings of free trade.

Many of these regulations are in the form of non-tariff barriers to trade. These include rules, standards, and principles imposed by governments or industry groups designed to restrict and regulate the flow of goods and services. They are no less an impediment to trade than blanket prohibitions or taxes and tariffs. For example, standards designed to regulate the trade in palm oil are now taking hold. These rules will shape the global market for vegetable oils and biofuels.

Three fundamental factors have affected the process of economic integration and are likely to continue driving it in the future. First, improvements in the technology of transportation and



communication have reduced the costs of transporting goods, services, and factors of production and of communicating economically useful knowledge and technology. Second, the tastes of individuals and societies have generally, but not universally, favored taking advantage of the opportunities provided by declining costs of transportation and communication through increasing economic integration. Third, public policies have significantly influenced the character and pace of economic integration, although not always in the direction of increasing economic integration. These three fundamental factors have influenced the pattern and pace of economic integration in all of its important dimensions.

Although technology, tastes, and public policy each have important independent influences on the pattern and pace of economic integration in its various dimensions, they clearly interact in important ways. Improvements in the technology of transportation and communication do not occur spontaneously in an economic vacuum. The desire of people to take advantage of what they see as the benefits of closer economic integration—that is, the taste for the benefits of integration—is a key reason why it is profitable to make the innovations and investments that bring improvements in the technology of transportation and communication. And, public policy has often played a significant role in fostering innovation and investment in transportation and communication both to pursue the benefits of closer economic integration (within as well as across political boundaries) and for other reasons, such as national defense.

The tastes that people have and develop for the potential benefits of closer economic integration are themselves partly dependent on experience that is made possible by cheaper means of transportation and communication. More recently, if less dramatically, it is clear that tastes for

products and services produced in faraway locations (including tastes exercised through travel and tourism), as well as for investment in foreign assets, depend to an important degree on experience. As this experience grows, partly because it becomes cheaper, the tastes for the benefits of economic integration typically tend to rise. For example, it appears that as global investors have gained more experience with equities issued by firms in emerging market countries, they have become more interested in diversifying their portfolios to include some of these assets.

Public policy toward economic integration is also, to an important extent, responsive to the tastes that people have regarding various aspects of such integration, as well as to the technologies that make integration possible. On the latter score, it is relevant to note the current issues concerning public policy with respect to commerce conducted over the internet. Before recent advances in computing and communications technology, there was no internet over which commerce could be conducted; and, accordingly, these issues of public policy simply did not arise. Regarding the influence of tastes on public policy, the situation is complicated. Reflecting the general desire to secure the perceived benefits of integration, public policies usually, if not invariably, tend to support closer economic integration within political jurisdictions. The disposition of public policy toward economic integration between different jurisdictions is typically more ambivalent. Better harbors built with public support (and better internal means of transportation as well) tend to facilitate international trade—both imports and exports. Import tariffs and quotas, however, are clearly intended to discourage people from exercising their individual tastes for imported products and encourage production of domestic substitutes. Sadly, the mercantilist fallacy that seems to provide common-sense support for these policies often finds political resonance. Even

very smart politicians, such as Abraham Lincoln (who favored a protective tariff, as well as public support for investments to enhance domestic economic integration) often fail to understand the fundamental truth of Lerner's (1936) symmetry theorem—a tax on imports is fundamentally the same thing as a tax on exports.

It should be emphasized that the interactions between public policy and both tastes and technology in their effects on economic integration can be quite complex and sometimes surprising.

## **CHAPTER THREE**

### **HISTORICAL BACKGROUND OF THE KENYA AND UGANDA TRADE RELATIONS**

#### **3.1 Introduction**

This chapter will look at the history, the integration between Kenya and Uganda process and provide trends in trade and how it has impacted the integration between the two countries.

#### **3.2 The History of Kenya and Uganda Relations**

Kenya and Uganda are important trading partners, but formal trade links between them have been constrained by a myriad of factors which have spurred the growth of informal (unrecorded) trade. It is widely felt that unrecorded trade between Kenya and Uganda is substantial and vital to both countries. Despite trade promotion protocols and market reforms which, to a large extent, have eased exchange controls and commodity movement restrictions, high sales taxes and bureaucratic import/export procedures still inhibit formal trade between the two countries. In addition, inappropriate policy interventions in the factor and product markets tend to distort relative prices, thus encouraging informal cross-border trade.

#### **3.3 Cross-Border Trade between Kenya and Uganda**

Interest in cross-border trade has been overwhelming, but knowledge of its magnitude, determinants, and consequences remains inadequate, leading not only to undervaluation of figures in the national accounts, but also inhibiting formulation of appropriate policies and strategies to exploit its potential impact, particularly on food security. As part of the effort to begin to understand and quantify the role of unofficial trade in Eastern and Southern Africa.

Functions such as exchange, storage, transportation, processing, and grading, but specialization in these functions is minimal. Most of the transactions are done on a cash basis, with the Kenyan currency as the preferred method of payment. This is because the Kenyan shilling is stronger than the Ugandan Shilling. Due to insufficient working capital, trade is characterized by quick turnover of stocks. Trading is dominated by money speculation, except when Ugandan traders exchange food commodities for Kenya's industrial products<sup>28</sup>.

The traders rely on hired transport and, generally, lack their own storage facilities. In most cases, the goods arrive at the border sites in hired trucks and are stored in rented stalls/shops while arrangements are made to smuggle the goods across the border, either during the day or at night. Traders hire porters to carry small quantities of their merchandise through footpaths.

The major sources of marketing information are interpersonal communication, prevailing supply/demand conditions, experience with seasonality in production and supply, and the established print and electronic media. Lack of working capital was cited by traders as the single largest barrier to starting and/or expanding an import/export business. Other constraints were high tax rates, institutional restrictions in the form of lengthy procedures involved in the issuance of licenses, limited credit facilities, harassment by public officials, poor infrastructure, and increased corruption at the border. These administrative and regulatory burdens inhibit traders' ability to adjust quickly to the volatile domestic and export market conditions.

---

<sup>28</sup> Baldwin, R. E., 2003. What Caused the Resurgence of Regionalism? *Swiss Journal of Economics and Statistics*, 131(3), pp. 453-463.

Various categories of transporters and couriers serve a smaller group of entrepreneurs, while some public officials invariably combine their official duties with active participation in the informal trade. Rent-seeking practices among public officials at the major border crossing points and cumbersome import/export procedures encourage both large and small traders to pass their goods through undesignated routes.

The commodities monitored at the Kenya-Uganda border were classified into two broad categories: agricultural (mainly food items) and nonagricultural (manufactured goods and forest resources). The direction and composition of trade both confirm the common view that Kenya, in relation to her neighbors, has a comparative advantage in manufacturing and processing. During the survey period, Uganda informally exported to Kenya an estimated 84,250 metric tons (MT) of maize valued at about \$12.4million.<sup>29</sup>

Kenya produces about 200,000 MT of beans annually, but this falls short of consumption requirements. Part of the excess demand is met by imports from Uganda and Tanzania. During the survey period, Kenya imported an estimated 9,300 MT of beans that were not registered by the customs officials. These imports were valued at close to \$5 million, using an average price of \$520 per MT. About 13,000 MT of sorghum, simsim, millet, groundnuts, and rice, with a total value of \$5 million, were also imported from Uganda. In addition, Kenya also imported bananas and other fruits valued at more than \$0.5 million and roots/tubers estimated at about \$2 million.

---

<sup>29</sup> World Bank, 2012. World Development Indicators, Washington D.C.: The World Bank.

The results of the study indicate that informal cross-border trade activities between Kenya and Uganda involve an exchange of substantial quantities of agricultural and industrial goods. Uganda were in the form of wheat flour amounting to about 16,000 MT worth \$8 million. Kenya is generally a net importer of wheat, thus implying that her wheat flour exports to Uganda derive from value-added services in her milling sector. The same applies to bread and milk, whose values were estimated at \$2.4 and \$1.2 million, respectively, and maize flour and confectioneries, whose quantities were insignificant. Sugar moved in both directions, but the trade favored Kenya, which exported about 27,000 MT valued at \$20 million compared to imports from Uganda, which amounted to only 1,300 MT valued at just under \$1 million.

The Lake trade routes handled the bulk of the sugar exports as one would expect since Kenyan sugar is produced in the area around Lake Victoria. More than 90% of the sugar from Uganda passed through Busia, suggesting that Uganda's unofficial sugar imports originated from the Jinja/Kakira area. Another major food import from Uganda is fish which, during the 12-month monitoring period, was estimated at 92,000 MT valued at more than \$30 million. Fish trade around Lake Victoria has important socioeconomic implications. The monitoring exercise revealed that the bulk of the fish found on Kenya's beaches originated in Uganda and that the trade was closely linked to exports of Kenya's manufactured commodities to Uganda.

Trade liberalization and consequent removal of restrictions on movement of goods within Kenya has caused the fishing industry to be infiltrated by large, well-organized up-country traders who exchange Kenya's manufactured products directly with Ugandan traders and fishermen. As a

result, the smaller traders and fishermen in Kenya have become more vulnerable to food insecurity.

Policies aimed at promoting international or intraregional trade and weather conditions were found to be the prime determinants of the level and seasonality of informal cross-border trade, especially of food commodities. Whereas comparative advantage exists in the production of some commodities, trade in many of the commodities is driven by demand and supply factors. The gains from informal trade include job creation and provision of both agricultural and industrial goods that would otherwise be unavailable. Informal trade thus plays an important role in food security by moving food from surplus to deficit areas and by providing income to those involved in it.<sup>30</sup>

However, informal trade encourages official corruption and could be a source of revenue loss to the exchequer. In addition, due to the nature of informal trade, there is a low degree of specialization in traders' operations, and the transaction costs could be high. Other problems, including quality control and adherence to phytosanitary requirements, arise from poor handling during transportation and storage of goods. A common feature in the informal cross border trade is the numerous number of times that the goods are shifted from one mode of transport and/or storage to another.

Kenya dominates over Uganda in most aspects, It has larger population and stronger economy compared to its landlocked neighbor. Kenya also has a larger manufacturing and industrial sector

---

<sup>30</sup> Crawford, J.-A. & Fiorentino, R. V., 2005. *The Changing Landscape of Regional Trade Agreements*, Geneva: World Trade Organization.



than Uganda. Although the share of agriculture in the GDP is the same, Kenya's agricultural sector is larger and more modern than that of Uganda.

**Table 3.1: Selected indicators for Kenya and Uganda, 2011 (World Bank, 2012)**

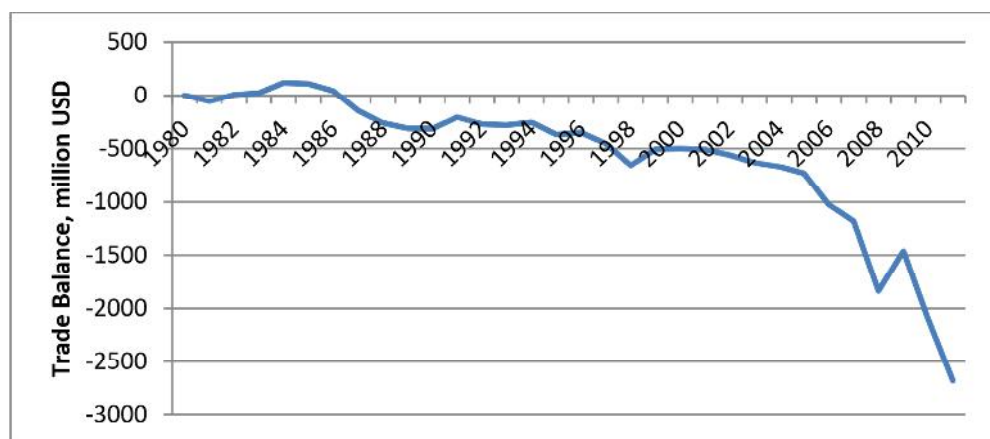
<b>Indicator</b>	<b>Kenya</b>	<b>Uganda</b>
Population (million)	41	33
Population growth rate	2.7%	3.2%
Urban population (% of total)	24.0	15.6
Urban population growth	4.4%	5.9%
GDP (million USD)	33	16
GDP per capita (USD)	808	487
Industry and manufacturing (share of GDP)	40%	33%
Agriculture (share of GDP)	23%	23%
Trade (share of GDP)	73%	58%

**Source, United Nations Conference on Trade and Development (2012)**

In the period 2000-2005, trade in goods and services increased in Uganda. Total imports grew from 950 million USD in 2000 to 1760 million in 2005 (United Nations Conference on Trade and Development, 2012). This was largely due to a considerable increase in the purchase of finished products. Most of Uganda's imports were coming from Kenya (over 25% in 2005; Khorana, et al., 2009). Exports from Uganda increased from 450 million USD in 2000 to 1015

millions in 2005 (United Nations Conference on Trade and Development, 2012). As imports grew more than exports, the trade deficit dramatically increased, as shown.

**Figure 3.1: Uganda Trade Balance, million USD<sup>31</sup>**



**Source, United Nations Conference on Trade and Development (2012)**

The main market for Uganda's exports was Europe: more than 40% of the goods exported from Uganda landed on European markets (Khorana, et al., 2009). In Africa, Uganda mostly exported to Kenya (Khorana, et al., 2009). Exports were mostly agricultural and primary products, including coffee and tea (224 million USD), fish products (140 million USD), gold (73 million USD) and cotton (40 million USD). Uganda's main imports for the same period were petroleum products, vehicles, cereals, iron and steel products.

In the period 2000-2004, trade in goods and services increased in Kenya. Total imports grew from 2900 million USD in 2000 to 4600 million in 2004 (United Nations Conference on Trade and Development, 2012). Twenty-six percent (26%) of imports were originating from Europe,

<sup>31</sup> United Nations Conference on Trade and Development, 2012

11% from United Arab Emirates and only 6% from India and 3% from China; (United Nations Conference on Trade and Development, 2012). Main imports in 2004 were petroleum oils and machinery and transport equipment (both at 24%), chemicals (15%) and manufactured goods (14%; United Nations Conference on Trade and Development, 2012).

Exports from Kenya dramatically increased from 1570 million USD in 2000 to almost 2700 millions in 2004 (United Nations Conference on Trade and Development, 2012). In 2004, Kenya mainly exported agricultural products (37%), minerals (23%) and raw materials (16%; United Nations Conference on Trade and Development, 2012). Four countries were the main destination for these exports: Uganda (18%), United Kingdom (11%), the Netherlands and Tanzania 8% each; (United Nations Conference on Trade and Development, 2012).

The analysis of trade flows show that both Kenya and Uganda export mostly primary products and import manufactured goods and inputs. However, Uganda's economy relies more on the primary sector and on trade with Kenya, which exports manufactured goods to Uganda. From this it can be inferred that both Kenya and Uganda have a comparative advantage in agriculture and a disadvantage in manufacturing compared to the rest of the world. However, Uganda's advantage is stronger whereas Kenya is closer to the world average.

### **3.4 Kenya and Uganda Convergence and Divergence in Regional Integration Agreements**

During the 1990s, Uganda liberalized and simplified its tariff regimes. However, the creation of the EAC Customs Union in 2005 caused a change in trade patterns. The CET introduced three tariff rates: 25% for raw materials, 10% for intermediate products and 0% for finished products.

Khorana et al (2009) assess the change generated by the new tariff system. They state that the average tariffs are relatively high under the CET, especially for agricultural goods (19.7% on average), dairy products, grains and tobacco. However, under the EAC customs regime tariffs are lower for electrical components and machinery. In general, the introduction of CET has raised average tariff for all member states. How has the creation of the EAC Customs Union influenced trade patterns in the region? The analysis of recent trade data can shed some light on this<sup>32</sup>.

### 3.4.1 Variations in Uganda's Trade Patterns

Total Ugandan imports increased from 3500 million USD in 2007 to more than 5600 million USD in 2011. The increase is mainly due to an upsurge in expenses for energy and finished products<sup>33</sup>. Kenya is one of the main sources for these inputs (after India). Imports from China are also growing in importance. However, the most evident trend is the increase in import from India, against which Kenya is losing ground as an exporter to the Ugandan market.

**Table 3.2: Uganda's imports by country of origin, million USD<sup>34</sup>**

	2007	% total	2008	% total	2009	% total	2010	% total	2011	% total
World	3493		4526		4247		4664		5631	
India	345	9.9%	470	10.4%	521	12.3%	684	14.7%	928	16.5%
Kenya	472	13.5%	511	11.3%	503	11.8%	512	11.0%	645	11.4%
China	274	7.8%	366	8.1%	379	8.9%	415	8.9%	522	9.3%

**International Trade Centre (2012)**

<sup>32</sup> Crawford, J

<sup>33</sup> International Trade Centre, 2012.

<sup>34</sup> International Trade Centre, 2012.

In terms of products, the most recent data confirm Uganda as an importer of minerals and oils, electronic equipment, vehicles and machinery<sup>35</sup>. Around 22% of the total imports are constituted by petroleum oils.

In terms of exports, Uganda mainly exports to countries in the region. Exports to Sudan (especially South Sudan), Rwanda and DRC are spurred by the fact that the commercial routes to these countries pass through Uganda. Therefore, most of these products might be re-exports rather than internally produced goods.

**Table 3.3: Uganda's main export, million USD** <sup>36</sup>

	2007	% total	2008	% total	2009	% total	2010	% total	2011	% total
World	1337		1724		1568		1619		2159	
Sudan	157	11,8%	246	14,3%	185	11,8%	209	12,9%	329	15,2%
Kenya	118	8,8%	165	9,5%	174	11,1%	190	11,8%	227	10,5%
Rwanda	83	6,2%	137	7,9%	135	8,6%	149	9,2%	194	9,0%
DR Congo	100	7,5%	125	7,2%	157	10,0%	184	11,4%	182	8,4%

**International Trade Centre (2012)**

Uganda heavily relies on primary products to earn foreign currency. Its main exports are coffee and tea (more than 25% of total exports), electrical equipment, fish and fish products, mineral products (International Trade Centre, 2012). Uganda's exports to Kenya are mainly constituted

<sup>35</sup> International Trade Centre, 2012

<sup>36</sup> International Trade Centre, 2012.

by agricultural products, the main being coffee, tea, (32%), vegetables (8%) cereals (7%) and dairy products and eggs (6%).<sup>37</sup>

### 3.4.2 Variations in Kenya's Trade Patterns

The case for Kenya is quite different. Kenya mainly imports from the United Arab Emirates, India, China and South Africa. Uganda does not appear among the most important exporters to Kenya.

**Table 3.4: Kenya's imports by country of origin, million USD** <sup>38</sup>

	2007	% total	2008	% total	2009	% total	2010	% total	2011	% total
World	8989		11128		10202		12093		15028	
UAE	1329	14.8%	1656	14.9%	1162	11.4%	1463	12.1%	2281	15.2%
India	845	9.4%	1310	11.8%	1078	10.6%	1302	10.8%	1714	11.4%
China	679	7.6%	932	8.4%	965	9.5%	1523	12.6%	1638	10.9%
South Africa	525	5.8%	678	6.1%	914	9.0%	754	6.2%	818	5.4%

**International Trade Centre (2012)**

Kenya's imports are also heavily biased on industrial products: oil (27% of total imports), machinery (10%), electrical equipment (7%) and vehicles (6%). However all these products are

<sup>37</sup> International Trade Centre, 2012.

<sup>38</sup> International Trade Centre, 2012.

imported from the major trading partners, whereas Kenya only imports primary products from Uganda, as shown above.

**Table 3.5: Kenya's exports by country of destination, million USD**

	2007	% total	2008	% total	2009	% total	2010	% total	2011	% total
World	4081		5001		4463		5169		5853	
Uganda	499	12,2%	615	12,3%	598	13,4%	657	12,7%	873	14,9%
UK	428	10,5%	551	11,0%	498	11,2%	507	9,8%	536	9,2%
Tanzania	332	8,1%	425	8,5%	389	8,7%	420	8,1%	476	8,1%

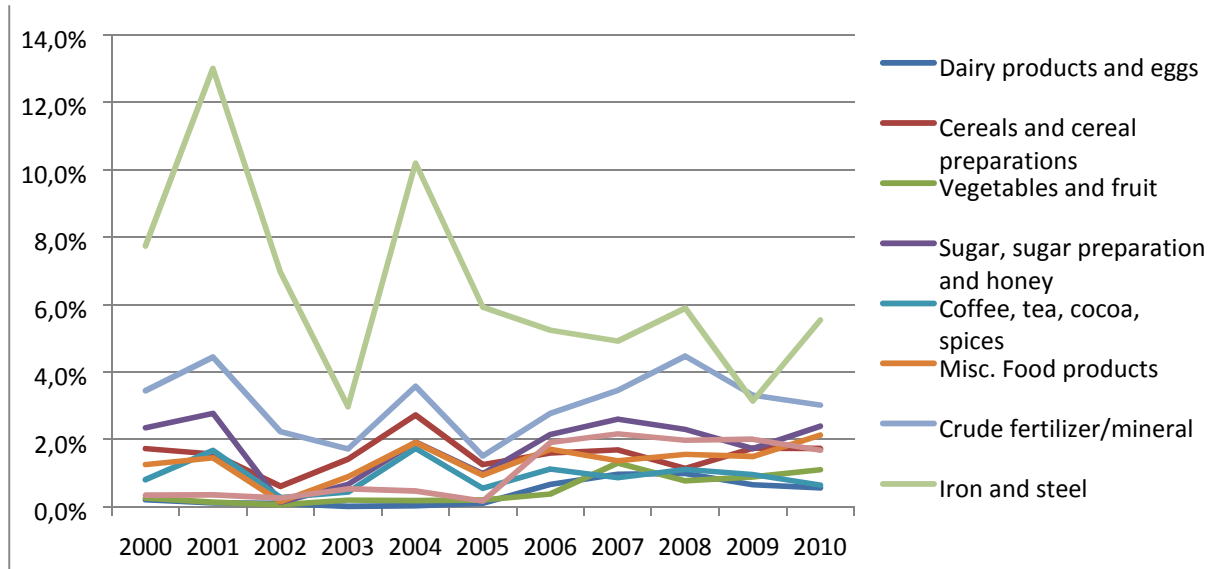
**Source, International Trade Centre (2012).**

In terms of exports, the main market for Kenya's products is Uganda. The trend has been constantly growing: since the inception of the EAC, Kenya has increased its exports to Uganda. Kenya mostly exports primary products to European countries (coffee and tea constitute 24% of the country's total exports, followed by live trees and plants and cereals) and oil to Uganda. Kenya's exports to Uganda have increased since the beginning of the Customs Union (though other exporters are becoming more important suppliers for Uganda).

A more in-depth analysis of the trade flows taking place between Kenya and Uganda yields interesting results. Figure 2 provides a graphic illustration of export trends for some selected primary products.<sup>39</sup> The graph shows that in the period under analysis Kenya's export of primary products to Uganda has decreased or stagnated. Before 2005, export trends appeared to be very

volatile. After the launch of the Customs Union, they became more stable and generally decreased compared to the previous period.

**Figure 3.2: Export of selected primary products as a ratio of total exports of goods from Kenya to Uganda<sup>40</sup>**



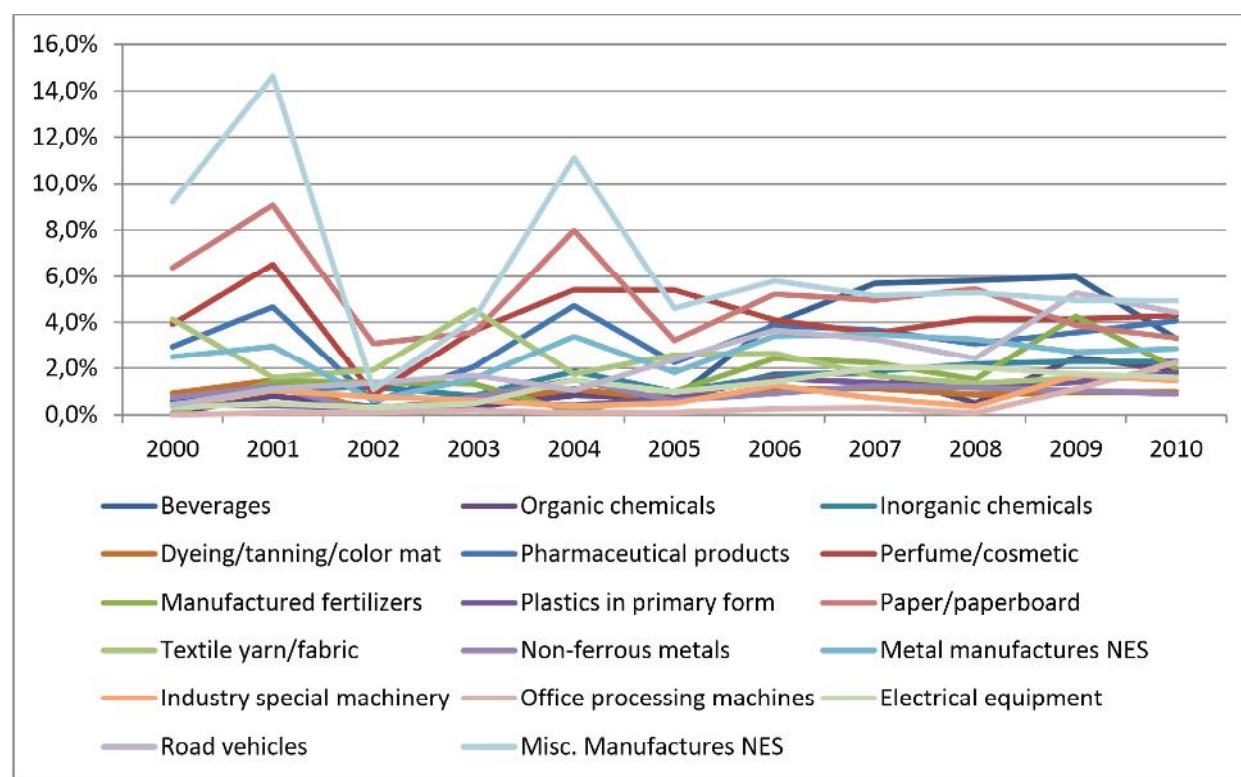
Source, UN Comtrade (2012)

Figure 3.3 shows the trends of Kenya’s export of manufactures to Uganda. As for primary products, the export figures were very volatile before 2005 and stabilized after that date. However, exports of manufactures seem to stagnate. It should be noted that other factors might be influencing these trends. For instance, it has been shown that Uganda is importing more and more from India and China. These two countries are replacing Kenya as major source of Uganda’s imports. These new dynamics are certainly influencing Uganda’s trade relationship with Kenya.

<sup>40</sup> UN Comtrade, 2012.



**Figure 3.3: Export of selected manufactures as a ratio of total exports of goods from Kenya to Uganda <sup>41</sup>**



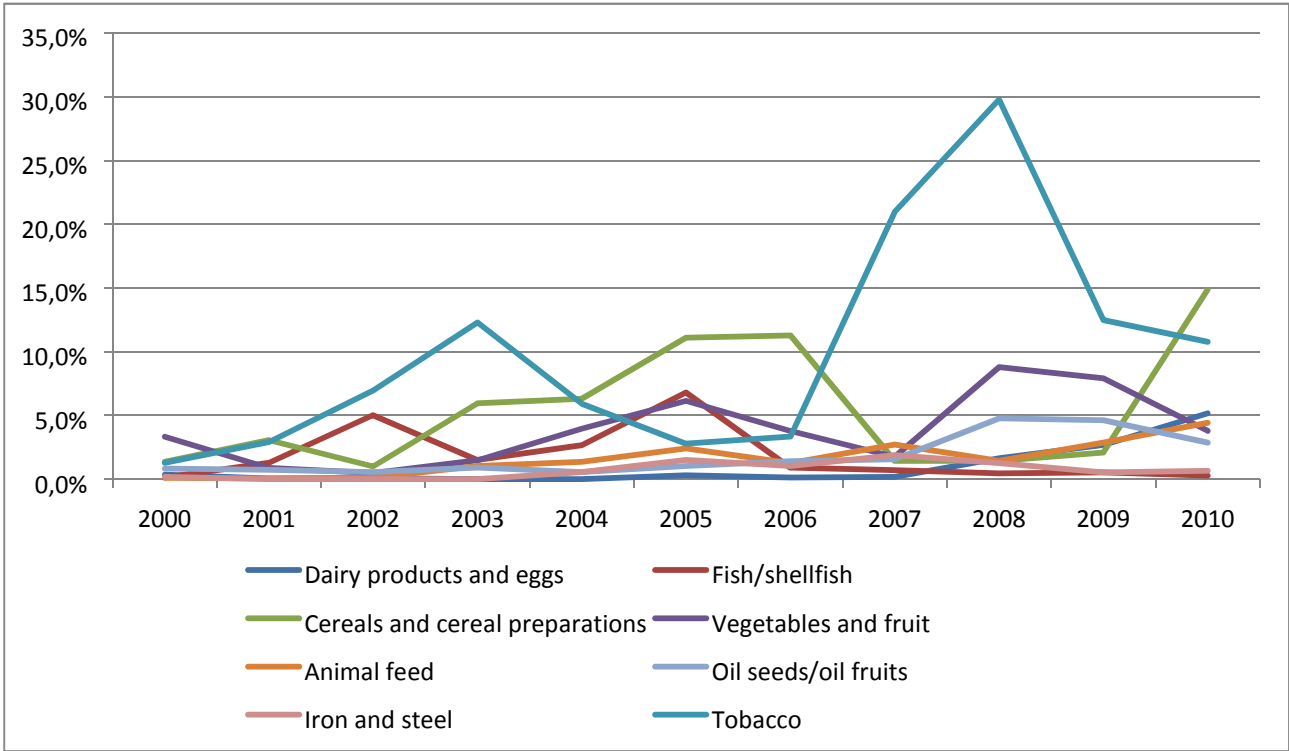
**Source, UN Comtrade, (2012)**

The analysis of Uganda's exports to Kenya also yields interesting results. As seen for the previous years, most of the products exported from Uganda to Kenya are agricultural products. For most of these products, there has been a marked increase in export during the short period under consideration. The graphic illustration provided in Figure 3.4 clearly shows that exports of primary products from Uganda to Kenya generally experienced a steep increase in 2005, coincidentally with the launch of the Customs Union, and an overall increase in the 2005-2010 period. This trend is much more noticeable than in the case of Kenya's export to Uganda. This might be due to the fact that Kenya's exports entail much larger figures and a bigger number of

<sup>41</sup> UN Comtrade, 2012.

trading partners, therefore other factors might influence the trends. Here, as Kenya clearly dominates as recipient of Uganda’s exports, the trend is very noticeable despite the short time span.

**Figure 3.4: Uganda’s export to Kenya as a share of total export of goods, selected primary products <sup>42</sup>**

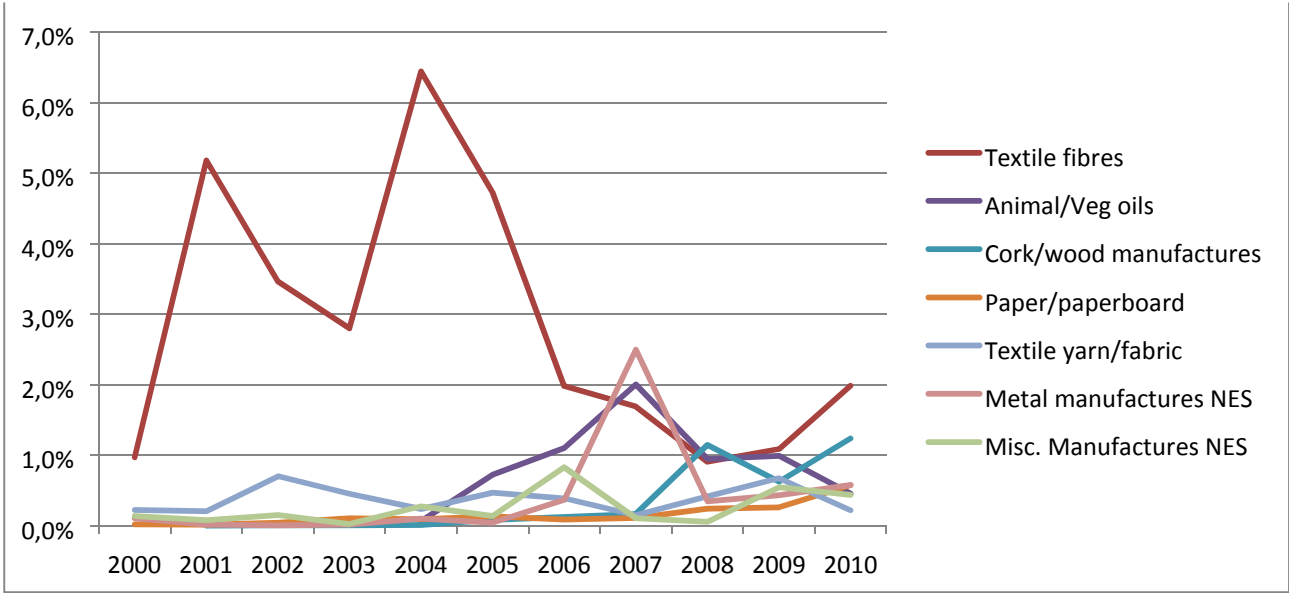


Source, UN Comtrade, (2012)

Figure 3.5 shows the changes in exports of manufactures from Uganda to Kenya. Almost all products (excluding textile fibres) experienced an increase in exports after the launch of the Customs Union.

<sup>42</sup> UN, Comtrade 2012

**Figure 3.5: Uganda’s export to Kenya as a share of total export of goods, selected manufactures<sup>43</sup>**



Source, UN Comtrade, (2012)

In conclusion, the effects of trade creation and trade diversion forecasted can only be partly observed in the trade relationship between Uganda and Kenya in the EAC. In terms of primary products, Uganda’s exports to Kenya increased whereas Kenya’s export to Uganda remained stable. As for manufactures, however, Kenya’s export to Uganda did not experience a considerable change, whereas Uganda’s export to Kenya slightly increased.

<sup>43</sup> UN Comtrade 2012.

### **3.5 Conclusions and Policy Concerns for the Future**

The history and trade relations between Uganda and Kenya has been examined in this chapter. The two countries has a role to play to ensure the ties between the two countries are sustained for mutual benefits which will enhance current process of integration.

A large trade potential exists between Kenya and Uganda and that trade liberalization through regional cooperation initiatives will enhance the realization of this potential. More appropriate trade policies are needed. While policies are being considered, and to some extent implemented, emphasis should be given to the elimination of trade obstacles, such as nontariff and institutional barriers, which increase transaction costs for importers and exporters. The objective of maximizing revenue collection through high tariffs is sometimes considered by governments in a short-term perspective and overrides other important criteria, such as efficiency in production through increased trade. Concern over domestic food security is often used to justify import and export restrictions on maize and other staples, but this takes little account of the role of intraregional trade as a source of external markets and of stabilization of domestic food prices. Trade liberalization will increase the access of small-scale producers and traders to adequate capital and new methods of risk management. An expanded role for the traders requires an expanded supply of working capital to finance purchases and inventories.

**CHAPTER FOUR**  
**TRADE BARRIERS AND THEIR EFFECTS ON ECONOMIC INTEGRATION FOR**  
**KENYA AND UGANDA**

**4.1 Introduction**

The importance of integration is of paramount importance for accelerated development of both Kenya and Uganda. Both countries need to address Trade barriers that can affect the process of economic integration. This chapter therefore focuses on study findings and analysis, based on secondary data relevant to the study. The chapter analyses trade barriers and their effects on economic integration.

**4.2 Trade Barriers between Kenya and Uganda**

In practice, the identification of trade barriers is subjective as what appears as a trade barrier to one person is a legitimate activity to another (Tand, 2003). However, there have been several approaches to trade barriers and Non-tariff barriers (NTBs) identification.

A survey of companies trading in Eastern and Southern Africa confirms that tariffs play a much less important role as a barrier to cross-border trade in Sub-Saharan Africa, than NTBs (Stahl, 2005). A report by the East African Business Council (EABC) ranked Kenya as the “worst offender when it comes to non-tariff barriers” and Ugandan exporters of dairy products to Kenya accusing “their bigger neighbour of imposing non-tariff trade barriers to block their produce from entering markets in Kenya<sup>44</sup>”.

---

<sup>44</sup> Nkululeko Khumalo (2008). Economic Integration Requires New Strategies. South African

Other incidences of Kenyan NTBs include holding Uganda milk at the border for prolonged period (up to weeks), a-34 percent protein level requirement for full cream powder milk yet the protein levels for cow milk are in the range of 25 to 26 percent, harassment of Ugandan transporters, blocking Ugandan chicks and excessive customs and administrative entry, advocacy for policy reforms to eliminate non-tariff barriers, excessive number of roadblocks between Mombasa and Ugandan eastern border entry points <sup>45</sup>.

A series of EAC trade studies reported some major NTBs that included customs and administrative entry procedures barriers; sanitary and phytosanitary measures; technical barriers to trade, standards, inspection time spent, un-harmonized procedures for issuance of certification and other distribution related obstacles.

### **4.3 Experiences of Other Trade Blocks on the Elimination/Reduction of NTBs**

In the European Union (EU), elimination of NTBs was the task of the common market programme. In 1985, the Community's White Paper identified NTBs and proposed 282 measures to be eliminated with a detailed timetable for completion by the end of 1992 (Sarfati 1998). Most of the proposals were adopted and became part of national laws of the various member countries. The programme for elimination of the NTBs abolished a series of technical, physical and fiscal barriers to regional trade through institution of single standards and regulation, the simplification of the fiscal structure and border related controls, and the institution of new rules for public procurement.<sup>46</sup>

---

<sup>45</sup> Osere 2009.

<sup>46</sup> Panusheff, E. (2003). Economic Integration in the European Union, Nekst PH, Sofia (in Bulgarian).

While the EU has significantly reduced NTBs, complete elimination has not been achieved. Ongoing activities for elimination of NTBs include a review of national NTBs reports, national procedures for inter-ministry co-operation on NTBs, exchange of information and views on a range of active NTB elimination programmes/projects and establishing a communication network between NTB focal points. Besides, there are ongoing negotiations and reforms as well measures to strengthen the process in various ways such as seeking support of political authorities to support for continued work on NTBs within the established, directed effort to continue and intensify the work to identify and eliminate NTBs in the region, establishing appropriate procedures for identifying and eliminating NTBs, and procedures to have high-level commitment and support and visibility<sup>47</sup>.

The member states commitment to provide the framework for continued work on NTBs, meet a couple of times per year, otherwise communicating by telephone and e-mail, identify NTBs on a continuous basis, prepare the respective annual reports on NTBs, consider the formation in each country of a national inter-ministry/agency communication network chaired by a high-level official from EU Secretariat.

Furthermore, the programme includes investment in One-Stop-Centres and electronic single window systems at border stations, review of port charges to international levels, political goodwill to facilitate cross-border movement of people while waiting for finalization of relevant protocol, mutually recognize inspection procedures, and inspection reports and certificates, clear

---

<sup>47</sup> Panusheff, E. (2003). Economic Integration in the European Union, Nekst PH, Sofia (in Bulgarian).

guidelines for stopping commercial vehicles, a daily record of vehicles stopped, reasons and measures taken, joint verification of goods at border posts, infrastructure improvement, cancellation of transit bonds, investment in parking sheds and parking yards, lifting restrictions of truck haulage, expand working hours<sup>48</sup>.

Non-tariff barriers (NTBs) are greatly affecting Uganda's competitiveness in the East African market. NTBs like police roadblocks, weigh bridges, poor transport infrastructure and high levels of taxes imposed on the Uganda traders in the past, have greatly affected the country's trade sector. Kenya's idea for allowing sugar from Uganda to be sold in its market. Kenya promised to give Uganda a license to allow our sugar into their country<sup>49</sup>.

#### **4.4 Effects of Trade Barriers between Kenya and Uganda**

Kenya and Uganda are important trading partners, but formal trade links between them have been constrained by a myriad of factors. Data collected through border observation which have spurred the growth of informal (monitoring) at a sample of sites selected on the (unrecorded) trade. It is widely felt that basis of practical considerations such as volume unrecorded trade between Kenya and Uganda is of trade, security, communication, transport substantial and vital to both countries. Despite links, availability of supporting institutions, and trade promotion protocols and market reforms personnel. The sites selected for intensive which, to a large extent, have eased exchange monitoring represented both inland and Lake Controls and commodity movement restrictions, Victoria routes. The monitoring took the form of high sales taxes and

---

<sup>48</sup> IMF (2013b). New Pacts Ease Path toward East African Single Currency, IMF African Department, December 30.

<sup>49</sup> ECA (2012). Assessing Regional Integration in Africa V. Towards an African Continental Free Trade Area, Addis Ababa.



bureaucratic import/export a census, covering all the major agricultural and procedures still inhibit formal trade between the industrial commodities that crossed the border two countries. In addition, inappropriate policy during 2 weeks randomly selected from each interventions in the factor and product markets month over a period of 12 months. Estimated tend to distort relative prices, thus encouraging average monthly trade volumes derived from the informal cross-border trade.<sup>50</sup>

#### **4.4.1 Inadequate Information Barriers**

The total trade diversion is, however, less than 10 % of the total trade created which questions the rationale for the pessimism expressed by the EAC treaty negotiators. One of the main factors that result in high prices is the presence of nontariff barriers (NTBs). The main underlying explanation to welfare losses is the existing cost disadvantage of the Ugandan producers which is aggravated by the existing NTBs. Some of the main NTBs that are faced by the importers are inadequate information on the customs formalities like the inability of the exporters to provide the relevant customs documentation under the rules of origin requirement specified under the CU protocol; lack of trained staff to certify products at the point of entry; corrupt bureaucracy; underdeveloped telecommunications; energy shortages and restrictions; high tolls; and so on. Yet other important NTBs are the existing governmental regulations, as for instance the Kenyan Revenue Authority's (KRA) regulation that all products being transported to Uganda have to travel in escorted convoys from Mombasa to the Malaba border<sup>51</sup>.

---

<sup>50</sup> ECA (2012). Assessing Regional Integration in Africa V. Towards an African Continental Free Trade Area, Addis Ababa.

<sup>51</sup> ECA (2012). Assessing Regional Integration in Africa V. Towards an African Continental Free Trade Area, Addis Ababa.

#### **4.4.2 Irregular Policies**

Kenyan policy makers have been confronted by the classic “food price dilemma.” On the one hand, policy makers are under pressure to ensure that food producers receive adequate incentives to produce and sell the crop. Rural livelihoods in many areas depend on the viability of food production as a commercial crop. On the other hand, the food security of the growing urban population and many rural households who are net buyers of food depends on keeping food prices at tolerable levels. For many years, policy makers have attempted to strike a balance between these two competing objectives – how to ensure adequate returns for domestic food production while keeping costs as low as possible for consumers. Food marketing and trade policy has been at the center of debates over this food price dilemma, including discussions over the appropriateness of trade barriers and the role of government in ensuring adequate returns to food production.

Improving the competitiveness of Kenyan food production is also a primary means of resolving the food price dilemma. The ability to reduce the costs of food production can ensure greater profitability to producers at lower prices while simultaneously improving poor consumers’ access to food. Achieving lower production costs also allows domestic producers to compete more effectively with imports from other countries.

Cost of production varies according to region, the type of technology package employed, farmers’ management practices, and the weather. In light of this, the study disaggregates cost of production into seven region/technology categories, five in Kenya and two in eastern Uganda, in order to compare the relative competitiveness of food among these regions and technology

packages. Variations in cost of production within each region/technology category reflect differences in farmer management practices and micro-variability in soils and rainfall. Therefore, within each region/technology category, we present costs of food production estimates for three terciles: low, medium- and high-cost producers. The results hold important implications for who will benefit and lose from the removal of regulatory and informal trade barriers between Uganda and Kenya<sup>52</sup>.

#### **4.4.3 Inefficiency of Ports**

Reasons for the inefficiency range from inadequate equipment to complex regulation. Most container terminals are nearing or have reached capacity limits and are under-equipped. African ports are facing increasing demands for a quick turnaround of vessels from customers with ever increasing sizes of ships. Improving turnaround time by increasing port performance is, however, no easy task, for the main bottleneck is in crane handling. Ports have not made any significant breakthroughs in container handling, even with the arrival of tandem lift and triple lift cranes. The two main bottlenecks within ports are the loading and unloading of cargo and the customs administration— both need to be addressed simultaneously. Container traffic is also impeded by the lack of an integrated land distribution system, particularly for transit traffic. Many maritime ports struggle to offer competitive services and inland waterways are poorly integrated into transport networks. As ports are increasingly challenged by intensified traffic, greater ship size and the growth of trans-shipment traffic, port capacity may have to be expanded in the future. Larger ships are more demanding in terms of port installations. The ship to shore gantry cranes need to be sufficiently large to reach all the containers and sufficiently fast in operation for an

---

<sup>52</sup> Economic Commission for Africa (ECA) (2013b). Best Practices in Regional Integration in Africa, Addis Ababa.

acceptable ship turnaround time.<sup>53</sup> If the containerization rate grows substantially, capacity will become an increasingly serious challenge for most Kenyan ports. Port charges add another dimension to the freight cost problem. Long delays and high port clearing charges affect both import and export containers in many African ports.

#### **4.5 Conclusion**

The trade barriers reflected in the literature on integration process, non-trader barriers affecting flow of trade and limiting maximisation of economic gains, poor infrastructure increasing costs to business, to achieve the greater benefits of integration both Kenya and Uganda need to address these barriers.

The potential gains from trade liberalization are limited by the imposition of non-tariff barriers which is a violation of the provisions of the respective legal instruments. The potential benefits from these protocols will only be realized with effective compliance with commitments undertaken. Compliance requires more than political will and calls for a proper functioning legal Framework. The commitment to eliminate non-tariff barriers remains a challenge. This may be attributed to the current weak regional institutional mechanisms put in place to monitor implementation of the commitments.

---

<sup>53</sup> IMF (2013b). New Pacts Ease Path toward East African Single Currency, IMF African Department, December 30.

## CHAPTER FIVE

### CONCLUSIONS AND RECOMMENDATIONS

#### 5.1 Introduction

This chapter will provide a summary, conclusions and recommendations based on the study.

#### 5.2 Conclusions and Policy Concerns for the Future

The study concludes that trade barriers affect economic integration between Kenya and Uganda. The study concludes that a large trade potential exists between Kenya and Uganda and that trade liberalization through regional cooperation initiatives will enhance the realization of this potential. More appropriate trade policies are needed. While policies are being considered, and to some extent implemented, emphasis should be given to the elimination of trade obstacles, such as nontariff and institutional barriers, which increase transaction costs for importers and exporters.

The study also concludes that there is need for support coordinated regulatory reforms and setting up of regional regulatory institutions as countries invest in regional infrastructure and liberalize trade in services; Support improvements to payments systems and currency convertibility within regions and across the continent; Assist countries to improve capacity of local enterprises to meet product quality requirements, improve their competitiveness and be part of regional and global supply chain.

The objective of maximizing revenue collection through high tariffs is sometimes considered by governments in a short-term perspective and overrides other important criteria, such as efficiency

in production through increased trade. Concern over domestic food security is often used to justify import and export restrictions on food and other staples, but this takes little account of the role of intraregional trade as a source of external market and of stabilization of domestic food prices.

Trade liberalization will increase the access of small-scale producers and traders to adequate capital and new methods of risk management. An expanded role for the traders requires an expanded supply of working capital to finance purchases and inventories. For the producers, a significant supply response would require substantial investments in improved technologies, input supply systems, and supporting services. National governments, on the other hand, should enhance public confidence by reaffirming their resolve to leave trade to the private sector. They should refrain from internal controls on prices and grain movements and intervene only in special circumstances involving grave threats to national food security.

### **5.3 Recommendations**

Based on the highlighted findings the study recommends that infrastructure investments need to be complemented with trade facilitation measures for intra-regional trade to easily move across borders. Reducing bureaucratic requirements, streamlining border management procedures and implementing trade facilitation measures will reduce border crossing times. Own reforms will be required to harmonize and reform transport-related standards and policies affecting trade and, eliminate obstacles to the free movement of goods and services including service providers.

Existing rules of origin are too restrictive. Improving market access is critical to encourage greater intra-industry trade within Africa and attract more foreign direct investment. Own reforms are required to simplify rules of origin and mutually recognize and harmonize standards. Countries should improve and modernize customs and transit systems and procedures (including developing one stop border posts and improving trade facilitation at internal borders) and, develop storage facilities; Support for action-oriented “knowledge platforms” that bring together relevant stakeholders(private sector, government officials, REC secretariats, external experts including from emerging market economies) to identify key binding constraints to market and trade integration and define action agendas, and help monitor implementation would help move the regional integration agenda forward.

The study also recommends that Uganda and Kenya should provide technical assistance to the industries which should be provided free of charge. The states should identify existing technical institutions which can be designated as Technical centres, strengthened National Bureaus of Standards or propose for setting up of Technical centres where they do not exist or share the Technical centres. There is also need to explore the possibility of having both national and regional technical centres for the program. Due to limited resources and the need for maximum impact, there is need to focus on priority sectors as provided in the industrial upgrading and modernisation program. Therefore development of product standards in the two countries should be based on international standards.

The study also recommends that cooperation on regulatory reforms is important to facilitate greater cross-border trade and investment in services and integrate services markets regionally.

For physical integration of infrastructure networks to be fully effective, regulatory frameworks and administrative procedures should be harmonized to allow the free flow of services across national boundaries. Capable regional regulatory bodies should be established to enforce the rules and ensure that the benefits of these investments are realized at a reasonable cost.

Both countries need to invest in priority regional infrastructure projects to fill missing links in the networks that will create stronger and better-connected networks, and help unlock economies of scale and sharpen competitiveness in Uganda and Kenya. Regional infrastructure will facilitate more intra-regional trade and exports from the continent, thus strongly supporting growth agenda. Regional infrastructure involves a high level of trust between countries because of the implied dependence on the neighbors. Political will has to be mobilized behind regional integration infrastructure by improving pace of preparation and implementation of regional infrastructure projects and implementing the sectoral reforms needed to accompany physical investments.

The study recommends that while elimination of tariff and non-tariff barriers is relevant, it will not lead to a significant expansion in intra-regional trade, given the structural deficiencies which exist. The geographical reality is that Uganda being landlocked is dependent upon the infrastructure of the Kenyan coastal members. There is need to develop its railways and ports in order to ease movement of goods. Investment in good quality infrastructure is expensive hence there is need to attract private finance where possible. Currently private investors view multi-country projects more politically risky than single country projects. It is recommended that governments should serve as a check on one another so that Kenya and Uganda commitment is



seen as more credible than a national commitment. The focus on regional infrastructure development will further boost regional trade, investment and integration and make the region economically competitive.

## BIBLIOGRAPHY

- Balassa, B., 2007. 'Revealed' Comparative Advantage Revisited: An Analysis of Relative Export Shares of the Industrial Countries, 1953-1971. *The Manchester School of Economic & Social Studies*, 45(4), pp. 327-344.
- Baldwin, R. E., 2003. What Caused the Resurgence of Regionalism? *Swiss Journal of Economics and Statistics*, 131(3), pp. 453-463.
- Brink 2000. *The Integration Into Global Financial Markets*. Puchefstroom South Africa.
- Buchanan, James M. (1990). "An American Perspective on Europe's Constitutional Opportunity." *Cato Journal*, 10, 619-630.
- Buchanan, James M. (1990). "An American Perspective on Europe's Constitutional Opportunity." *Cato Journal*, 10, 619-630. (Bulgarian).
- Cellini, Roberto and Luca Lambertini (2004). "R&D Incentives Under Bertrand Competition: A Differential Game." Working paper, Università di Bologna.
- Cellini, Roberto. (2000). "Growth and Differentiated Oligopoly." *Economic Letters*.
- Coe, David T. and Elhanan, Helpman (1995). "International R&D Spillovers." *European Economic Review*, 39, 859-887.
- Coe, David T. and Elhanan, Helpman (1995). "International R&D Spillovers." *European Economic Review*, 39, 859-887. Commissioned by GTZ, Nairobi
- Crawford, J.-A. & Fiorentino, R. V., 2005. *The Changing Landscape of Regional Trade Agreements*, Geneva: World Trade Organization. Differential Game." Working paper, Università di Bologna.
- ECA (2004). *Assessing regional integration in Africa*, Addis Ababa. International Food & Agricultural Trade Policy Council (2011). *Economic partnership agreements and African regional integration: Have negotiations helped or hindered regional integration?* in IFATPC Issue Brief, August 2011, IFATPC.
- ECA (2006). *Assessing regional integration in Africa II. Rationalizing regional economic*.
- ECA (2010). *Assessing Regional Integration in Africa IV. Enhancing Intra-African Trade*, Addis Ababa
- ECA (2012). *Assessing Regional Integration in Africa V. Towards an African Continental Free Economic Commission for Africa (ECA) (2013b). Best Practices in Regional Integration in Africa*, Addis Ababa.

- Economic Integration.” *Journal of International Economics*, 60, 177–201.
- English, P., Jaffee, S. & Okello, J., 2004. Exporting Out of Africa—Kenya’s Horticulture Success Story. Shanghai.
- Epifani, Paolo and Gino Ganica (2009). “Openness, Government Size and the Terms of Trade.” Establishment of the African Economic Community, Academia.edu.
- Foroutan, F., 1992. Regional Integration in Sub-Saharan Africa. World Bank Policy Research Working Papers1, Issue WPS 992.
- Gawande, Kishore, Pravin Krishna, and Michael J. Robbins (2004). “Foreign Lobbies and US Trade Policy.” *The Review of Economics and Statistics*, 88, 563–571.
- Gawande, Kishore, Pravin Krishna, and Michael J. Robbins (2004). “Foreign Lobbies and US Trade Policy.” *The Review of Economics and Statistics*, 88, 563–571.
- Giavazzi, Francesco, and Guido Tabellini (2005). “Economic and Political Liberalizations.” *Journal of Monetary Economics*, 52, 1297–1330.
- Giavazzi, Francesco, and Guido Tabellini (2005). “Economic and Political Liberalizations.” *Journal of Monetary Economics*, 52, 1297–1330.
- Greenaway, D. & Milner, C., 1990. South-South Trade: Theory, Evidence and Policy. The World Bank Research Observer, 5(1), pp. 47-68.
- Grossman, Gene M. and Elhanan Helpman (1991). *Innovation and Growth in the Global Economy*. The MIT Press.
- Grossman, Gene M. and Elhanan Helpman (1991). *Innovation and Growth in the Global Economy*. The MIT Press.
- Hume, David. (1987). “Idea of A Perfect Commonwealth.” In *Essays, Moral, Political and Literary*, edited by F, Eugene. Miller. Liberty Fund, Inc.
- Hume, David. (1997). “Idea of A Perfect Commonwealth.” In *Essays, Moral, Political and Literary*, edited by F, Eugene. Miller. Liberty Fund, Inc.
- IMF (2013b). New Pacts Ease Path toward East African Single Currency, IMF African Department, December 3Implications for Growth.” *Quarterly Journal of Economics*, 106, 503–530.
- Institute of International Affairs, Johannesburg, South Africa. Organization for Economic Co-operation and Development (OECD) (2013). Development aid at a glance. Statistics by region:

- Lumenga-Neso, Olivier, Marcelo Olarreaga, and Maurice Schiff (2005). “On ‘Indirect’ Trade Related R&D Spillovers.” *European Economic Review*, 49, 1785–1798.
- Madison, James (1788). *The Federalist Papers, No. 10*. J. A. McLean, New York.
- Madison, James (1997) *The Federalist Papers, No. 10*. J. A. McLean, New York.
- Marinov, V. (1999). Regional Economic Integration. University PH Stopanstvo, Sofia (in
- Mbeki, T. (2011). When Europe Sneezes, Will Africa Catch a Cold? The Euro Crisis, Globalisation and Africa. African Leadership Foundation.
- McCallum, John. (1995). “National Borders Matter: Canada–US Regional Trade Patterns.” *American Economic Review*, 85, 615–623.
- McCallum, John. (1995). “National Borders Matter: Canada–US Regional Trade Patterns.” *American Economic Review*, 85, 615–623.
- Melitz, Marc J. and Gianmarco I. P. Ottaviano (2008) “Market size, trade, and productivity.” *Review of Economic Studies*, 75, 295–316.
- Melitz, Marc J. and Gianmarco I. P. Ottaviano (2008) “Market size, trade, and productivity.” *Review of Economic Studies*, 75, 295–316.
- Mlenga, K. (2012). Assessing the Progress of Africa’s Economic Integration in Light.
- Murphy, Kevin M., Andrei Shleifer, and Robert W. Vishny (1991). “The Allocation of Talent:
- Murphy, Kevin M., Andrei Shleifer, and Robert W. Vishny (1991). “The Allocation of Talent:
- Ndomo, A. (2009). Regional Economic Communities in Africa - A Progress Overview. Study
- Ndung’u, Njuguna (2000) ‘Regional Integration Experience in Eastern African Regions’ (Paper
- Nickell, Stephen J. (1996). “Competition and Corporate Performance.” *Journal of Political Economy*, 104, 724–746.
- Nickell, Stephen J. (1996). “Competition and Corporate Performance.” *Journal of Political Economy*, 104, 724–746.
- Nkululeko Khumalo (2008). Economic Integration Requires New Strategies. South African
- Olson, Mancur (1982). *The Rise and Decline of Nations*. Yale University Press.
- Ottaviano, Gianmarco, Takatoshi Tabuchi, and Jacques-Francois Thisse (2002) “Agglomeration and Trade Revisited.” *International Economic Review*, 43, 409–435.

- Ottaviano, Gianmarco, Takatoshi Tabuchi, and Jacques-Francois Thisse (2002) “Agglomeration and Trade Revisited.” *International Economic Review*, 43, 409–435.
- Panusheff, E. (2003). Economic Integration in the European Union, Nekst PH, Sofia (in Bulgarian).
- Peretto, Pietro F. (2003). “Endogenous Market Structure and the Growth and Welfare Effects of Economic Integration.” *Journal of International Economics*, 60, 177–201.
- Persson, Torsten, Guido Tabellini, and Francesco Trebbi (2003). “Electoral Rules and Corruption.” *Journal of the European Economic Association*, 1, 958–989.
- Persson, Torsten, Guido Tabellini, and Francesco Trebbi (2003). “Electoral Rules and Corruption.” *Journal of the European Economic Association*, 1, 958–989.
- Presented at A Policy Workshop organized by the OECD Development Center at the Graduate Institute of International Studies, Geneva 13 October 2000)
- Rodrik, Dani (2000). “How Far Will International Economic Integration Go?” *Journal of Economic Perspectives*, 14, 177–186.
- Rodrik, Dani (2000). “How Far Will International Economic Integration Go?” *Journal of Economic Perspectives*, 14, 177–186. Trade Area, Addis Ababa. Way Forward, IMF Working Paper 05/36, February.
- Weeks, S. G., 1967. The East African Community. *Africa Today*, 14(5), pp. 2-3.
- World Bank, 2012. World Development Indicators, Washington D.C.: The World Bank.
- World Trade Organization, 2012. World Trade Organization. Available at: [www.wto.org](http://www.wto.org).
- Yang, Y. & Gupta, S. (2005). Regional Trade Arrangements in Africa: Past Performance.