Why We Like East Africa

Wed Nov 18, 2009 5:54pm BST

Risk Watchdog is not shy about promoting his views to anyone who will listen. Yesterday, I had the opportunity yesterday to talk to a group of potential exporters to East Africa at an event organised by the London Chamber of Commerce and Industry and hosted by Barclays, about why I and my colleagues at Business Monitor International love the region as a trading destination.

Even amidst the worst global recession since the 1930s, the three largest economies of East Africa – Kenya, Tanzania and Uganda – have still managed to post enviable levels of growth, of an expected 2.5%, 4.9% and 7.0% respectively in 2009. Over the next five years, we see growth averaging 5.0%, 6.4% and 7.5% respectively. What will be the key drivers of this impressive performance?

Global recovery

As the global economy emerges from recession, the outlook for exports will become even more favourable. Global prices of key export commodities have been rising, which should offer a boost to foreign exchange inflows that will in part offset falls in output (that have in turn kept prices high). Kenya, Uganda and Tanzania have been hit especially hard in this regard due to the current drought affecting the region that has dented tea, coffee and horticulture production. Kenya's output of cut flowers has fallen too, for the same reason but weaker global demand has weighed on prices. Record gold prices will be of great benefit to Tanzania.

As important as agricultural commodity exports are, tourism has historically been the key export earner for all three countries. Having suffered considerably in 2009 as global consumer, luxury spending fell, although we would expect to see a gradual recovery in 2010.

Oil boost for Uganda

While strong oil prices will add to import bills – we see the OPEC basket supported above US$90/bbl level over the next five years – Uganda is in the latter stages of bringing its domestic oil potential online. Not only will this offer a massive boost to exports, but it could propel growth into the double digits. The extra money in the economy would offer the banking system significant potential to increase its lending, both domestically and regionally. Kenya too would benefit from Ugandan oil, as the country earns a significant amount from transport services exports. For the region as a whole, it would also help to lower energy costs if Uganda develops refining capacity.

Multilateral support

Cushioning the shocks of collapsed export earnings and weaker currencies, Kenya and Tanzania received assistance form the IMF to the tune of US$550mn and US$336mn respectively under the Exogenous Shock Facility. (Uganda has suffered much less and so did not need to tap such funds). These inflows have helped stabilise the two economies.

© 2009 Business Monitor International Ltd

Externally-funded investment

The Kenyan government has implemented a generous fiscal stimulus in order to maintain government spending and support economic activity. Indeed, Kenya has launched over US$500mn of bonds in the local market in 2009 – the second launch is currently open for those interested – to fund infrastructure investment. According to a recent report co-produced by the World Bank, poor road infrastructure costs the continent's economies around two percentage points of potential economic growth each year.

Furthermore, if global financial market conditions continue to improve, we see the increasing possibility of Kenya and Uganda revisiting plans to issue external bonds. Having postponed plans in 2008, the raising of US$500mn by Kenya and US$1bn by Uganda would offer a significant boost to investment. Not only would Uganda benefit from its own improvements in infrastructure, but also those in Kenya, through which 95% of Uganda's exports are transported.

Regional integration

The economic potential of these three countries should become much greater over the coming years, boosted by further integration of the regional trade bloc, the East African Community (EAC) – which celebrates its 10th anniversary this week – and eventual progress on reducing tariffs on EU-originating goods. Building on earlier agreements to facilitate and standardise regional trade policy, the EAC common market is to come into being in January 2010, whereby Rwanda and Burundi will join the other three, and all goods originating in any of the five countries are intended to be able to move tariff-free to any of the others. While lowering duties will inevitably reduce this element of government revenues, the impact of lower imports costs should outweigh this through increased consumption and economic activity.

As the regional heavyweight, and with the largest manufacturing base, Kenya is likely to be the biggest beneficiary. This has thrown up some objections from its neighbours. In Tanzania there is a strong undercurrent of resistance to ceding land rights to foreigners including citizens of Kenya and Uganda, posing a substantial obstacle to cross-border investment. Producers in Uganda have expressed concerns from Kenyan competition.

Despite the speed of progress so far, a single currency and political integration still look to be ambitious goals. However, a point that came out yesterday was just how strong a driving force President Paul Kagame of Rwanda is in pressing ahead with the regional programme.

Domestic politics will also present key risks. Remember the disruption to output in Kenya – and the spill over effects on Uganda – as a result of the violence that followed the disputed 2007 elections that dealt a terrible blow to economic performance and international perceptions.

Rise of the consumer

The key sectors for investment will be infrastructure and agriculture, as well as water, power and information and communication technology. At the heart of these growing investment needs is the great potential of the consumer market. The rise of the African consumer is set to play a key role in the region's development and prospects, and is often overlooked in favour of big capital projects.

The three countries have a combined population of around 120mn. This is already a significant

© 2009 Business Monitor International Ltd

consumer base, but this could be boosted further with the potential merging of Africa's three main trade blocs. In October, the EAC and the other two regional blocs, the Southern Africa Development Community (SADC) and the Common Market for Eastern and Southern Africa (Comesa) agreed on a framework to create a combined free-trade area of 26 countries and some 525mn people.

In Kenya and Uganda, domestic demand is the key driver of the economies. All three countries have young populations, meaning they are likely to spend a high proportion of disposable income. Furthermore, with incomes set to rise with economic growth, the consumer markets will demand a greater volume and variety of goods and services in the years to come, especially as populations grow. In this regard, while Kenya will continue to offer the largest and wealthiest consumer market, Uganda offers the greatest growth potential.

© 2009 Business Monitor International Ltd