



Economic Commission for Africa
Sub-regional Office for Eastern Africa

Sustaining Economic Growth and Development in Turbulent Times

Tracking Progress on Macroeconomic and Social Developments in the Eastern Africa Region 2011-12





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Economic Commission for Africa

P.O. Box 3001

Addis Ababa, Ethiopia

Tel: +251 11 544-9900

Fax: +251 11 551-4416

E-mail: ecainfo@uneca.org

Web: www.uneca.org

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Preface and Acknowledgements

THIS REPORT PROVIDES a detailed analytical overview of the performance of Eastern African countries over the last decade, with a particular focus on progress in 2011, with the objective of informing the Intergovernmental Committee of Experts and helping better focus the policy debates on the main socio-economic issues affecting the region. The countries analysed include 13 countries in the region – Burundi, Comoros, Democratic Republic of Congo, Djibouti, Eritrea, Ethiopia, Kenya, Madagascar, Rwanda, Seychelles, Somalia, Tanzania and Uganda – hereafter denominated Eastern Africa Region EAR-13. For the first time, this report also includes data on South Sudan, which official became a member of the Sub-Regional Office – Eastern Africa in March 2012. We hope to expand on the analysis of South Sudan in future editions of this regional report. Developments analysed were carried out on the basis of data available at the end of March 2011, using both national sources and international organisations, including UNECA sources. The region is formed of four overlapping and advanced regional integration processes which involve the following regional members: the Eastern African Community (Burundi, Kenya, Rwanda, the United Republic of Tanzania, and Uganda); COMESA (Burundi, Comoros, the

Democratic Republic of Congo (DRC), Djibouti, Ethiopia, Kenya, Madagascar, Rwanda, Uganda); IGAD (Djibouti, Ethiopia, Kenya, Uganda) and SADC (DRC, Madagascar, Seychelles, Tanzania). Where relevant, the report makes reference to these different economic groupings.

This report was written by a team led by Andrew Mold, Head of the Macroeconomic and Social Policy Cluster, under the overall supervision of Antonio Pedro, Director of the UNECA-SRO-EA. The team comprised of Hamdou Wane, Rodgers Mukwaya, and Emelang Leteane. Rosemary Bagiza and Narve Rowitt provided research support. Useful inputs and comments were received from Godfrey Onyango, Yohannes Hailu, and Daya Bragante (UNECA-SRO-EA) as well as Annalisa Prizzon (ODI, London). Andrew Allimadi (UNECA-HQ) edited the final document.

Finally, a draft version of this report received invaluable feedback from participants at the UNECA's Intergovernmental Committee of Experts Meeting 2011, held in Dar es Salaam between 13th-18th February 2012. UNECA SRO-EA would like to thank participants for their insights.

Acronyms

ACR	Africa Competitiveness Report
AGOA	African Growth and Opportunity Act
CCT	Conditional cash transfers
COMESA	Common Market for East and Southern Africa
CPI	Consumer Price Index
DAC	Development Aid Committee
EAC	Eastern African Community
EAR-13	Eastern Africa Region (the 13 SRO-EA member states)
EPAs	Economic Partnership Agreements
FAO	Food Agricultural Organisation
FDI	Foreign Direct Investment
GDP	Gross Domestic product
GII	Gender Inequality Index
HDI	Human Development Index
HDR	Human Development Report
IGAD	Intergovernmental Authority on Development
IMF	International Monetary Fund
MAF	MDG Acceleration Framework
MFN	Most Favored Nation
ODA	Official Development Assistance
OECD	Organisation for Economic Co-operation and Development
OVC	Orphans and vulnerable children
PRSPs	Poverty Reduction Strategy Papers
PSNP	Productive Safety Net Programme
REER	Real Effective Exchange Rate
SADC	Southern African Development Community
SSA	Sub-Saharan Africa
TOT	Terms of Trade

Introduction

IN THE AFTERMATH to the 2008-09 global economic crisis, African countries have benefited from the quick rebound in commodity prices, and their growth has been shored up by investments and trade with the emerging economies. A significant reduction in the debt burden for many countries, together with greater inflows of private capital and better macroeconomic management in the 2000s, means that the prospects for many African countries are better than they have been since the 1970s (McKinsey, 2010, Mold, 2011, Raddlet, 2010). Over the course of 2011, most countries in the Eastern African region have been registering a strong growth performance.

Nonetheless, there are a number of challenges on the horizon which make the prospects for the region more complex than in 2010, when the global economy seemed to be on the road to a robust recovery. Fears in Europe and the US of a 'double-dip recession' seem to have introduced significant uncertainty, and this could have implications for regional growth prospects. During the 2008-9 growth slowdown, the impact was mitigated by a strong growth performance in the region's emerging partners, particularly China and India. But it is now not so clear that both these economies will post such a robust performance the same way as they did in 2008-9. India is displaying some financial fragility, and there are also clear signs of a deceleration in imports to China, as well as tightening credit conditions. In short, it is no longer evident that the Eastern Africa region can depend on the

continued expansion of the emerging markets to shield it from the economic downturn in the OECD countries.

In macroeconomic terms, the main messages emanating from this report are:

- ▶ **A number of regional economies continue to be among the best performing in the world** – notably, Ethiopia, Rwanda, Tanzania and Uganda. Forecasts, moreover, would suggest that this is likely to continue to be the case over the years,¹ with the important proviso that if the global economic environment suffers a still greater deterioration than that witnessed in the final two-quarters of 2011, then that growth performance could be put in jeopardy.
- ▶ Nevertheless, **there are some underlying macro-economic imbalances which need attention** – especially if the region is to move forward with its ambitious regional integration programmes (COMESA, SADC, EAC, and their Tripartite Agreement, as well as IGAD).
- ▶ Despite a significant reduction in aid dependence in countries like Rwanda over the last 5 years, **most countries in the region are still highly dependent on Overseas Development Aid (ODA) to balance their accounts**. It is of particular concern that the outlook for aid flows is not that positive. The OECD's

24 Development Aid Committee (DAC) members did make considerable efforts to maintain aid flows during the crisis of 2008-9, and in 2010 ODA from DAC countries actually reached a record US\$129 bln, of which US\$ 46 bln went to Sub-Saharan Africa. But a number of DAC countries have begun cutting back already (Ireland, Spain, Italy, France), and the prospects for resisting further cutbacks among the major donors are rather bleak. Government policy in the region therefore needs to react prudently and plan from the perspective that donor support is likely to have peaked.²

- ▶ Although there was some reprieve in the final quarter of 2011, **nominal exchange rates weakened for a number of countries in the region against the US dollar** - in some cases quite sharply (Kenya, Uganda, Ethiopia), something which has complicated macro-economic management.
- ▶ **The reorientation of regional trade towards emerging markets continues apace** – this has contributed in a very significant way to the relative stability of economic performance of many countries in the region, despite the global economic downturn which started in 2008. This report also makes the point that the rise of emerging partners has attenuated the relevance of complex trading agreements with traditional partners (e.g. EPAs, AGOA). Put simply, Eastern African countries now have more policy space to manoeuvre in their negotiations.

These main points aside, the study also points to a number of critical areas which merit greater attention in terms of macroeconomic policy over the coming 12 months. These comprise of:

- a) **Inflation** – many of the region's economies experienced a worrying intensification of inflation in the second half of 2011. Particularly notable have been the inflationary pressures in Ethiopia, Uganda and South Sudan. Some of these trends – but not all – is

explainable by exogenous price shocks (fuels, food), but non-core inflation is also increasing in many countries, suggesting that policymakers need to focus attention on the links with current monetary, fiscal and exchange rate policies.

- b) **Fiscal Deficits** – after adopting counter-cyclical fiscal policies to counter the impact of the global economic situation in 2008-9, in around half of the countries of the region fiscal imbalances have deteriorated, albeit in most cases only marginally so far. Pressures to raise salaries in face of inflation, plus booming infrastructure expenditures and the increasing costs of social programmes have all been exerting pressure on budgets.
- c) Balance of Payments deficits in a number of countries in the region are large, and in some cases at levels which are unsustainable in the long run (particularly in the cases of the Seychelles and Burundi, though they are also in excess of -8 percent of GDP in Kenya, Tanzania and Uganda). In some cases, current account imbalances have been linked to the sharp nominal depreciations which a number of the regions' currencies have experienced. But in others it is more structural in nature, reflecting the lack of underlying competitiveness in the trading sector, as well as a high dependence on continued capital inflows, principally aid and remittances..

In terms of the major social challenges, the following points can be highlighted:

- a) Progress in social development does not always go hand-in-hand with economic development. Improvements in a number of human development indicators related to health and education have generally been quite impressive across the region over recent years.. Tanzania, for instance, has achieved a notable decrease in infant mortality – at approximately twice the rate of improvement that Sweden achieved at a similar stage in its development. Similarly, Madagascar has

achieved the largest drop in infant mortality In Sub-Saharan Africa decreasing by 60 percent over the period 1990-2009. In maternal health, Rwanda has significantly reduced maternal mortality since 1990 (even though it remains at high levels). In contrast, although Kenyan maternal mortality rates improved in the 1990s, maternal mortality rates have not fallen over the past decade. Pinpointing areas of weakness such as this, and identifying the root causes, as well as putting in place peer-learning from best-practice examples, are fundamental to ensuring continued progress in human and social development.

- b) Africa is the continent with the highest birth rate, and in Eastern Africa demographic pressures are especially intense. Fertility rates, especially in rural areas, are particularly high in countries such as Uganda, Burundi and Ethiopia, and when combined with declining mortality rates, is resulting in persistently rapid population growth. To an important extent, governments and other stakeholders' capacity to respond to these demographic trends will determine the quality of life that their citizens are able to attain. A holistic approach is required, which incorporates greater investment in health sector personnel, improved access to contraception, and improving education (particularly for girls). If these policies come together correctly, there are some hopes that the region could benefit, just as India and China have before, from a 'demographic dividend' – that is, when the share of the working-age population rises relative to children and old people, thus giving an additional impetus to GDP growth per person. But this outcome is contingent on the right set of policies being in place, particularly with regard to family planning.

Finally, this report is written against a backdrop of period when regional food security has been sharply compromised by events in the Greater Horn of Africa. According to recent assessments, at least 21 million people were in need of immediate humanitarian assistance in the sub-region.

This represents about ten per cent of the total population of the region – and as much as 40 per cent of the population in Somalia. Small scale farmers and herders, food insecure urban dwellers constitute nearly four-out-of-five people in this group. The famine in Somalia has caused the displacement of more than 800,000 refugees towards Kenya and 260,000 to Ethiopia, with a further 30,000 having sort refuge in Djibouti (GIEWs, 2011). U.N. estimates show that the financial need for immediate, short-term drought relief assistance amount to \$2.5 billion (of which only 63 percent had been funded as of September 9th 2011, leaving a gap of \$1.6 billion) (OCHA, 2011). As dramatic as the prevailing famine is in the Greater Horn of Africa, it illustrates a wider problem regarding the extent and the geographic spread of food insecurity across the sub-region. For instance, there is already potentially a serious situation developing in South Sudan, where the cereal gap for 2012 is already estimated at 400,000 tons due to erratic rainfall, poorly functioning markets and an increased demand resulting from the influx of displaced persons from Southern Kordofan and Blue Nile States.

As a consequence, this report dedicates a special thematic section to analyzing the long term trends behind food insecurity in the sub-region, as well as an overview of the policy responses. It is important that those policy responses are imbedded not only in efforts to enhance agricultural performance (which are crucial), but also in comprehensive social protection policies which avoid the most vulnerable citizens of local communities 'falling through the net'. As this report points out, a more ambitious agenda regarding social protection is now feasible, given the larger resources derived from the sustained economic growth of recent years. It now only requires focus, financial resources and peer-learning from successful examples of social interventions (which fortunately abound) across the region to put such an agenda in place. The food security situation also brings renewed urgency to the process of consolidating regional integration – in an increasingly mutually independent region, true food security can only be achieved through the greater alignment of trade, fiscal and other policies across the region.

Box 1: National Developmental Strategies in Eastern Africa – Ambitious but Realisable Goals

Across the region, countries have been producing ambitious plans to attain higher levels of economic and social development. In the 1990s, many countries in the region articulated development strategies in the context of Poverty Reduction Strategy Papers (PRSPs). However, the agenda was generally speaking a donor-driven one. Over the last decade, countries have made concerted efforts to come up with their own plans. To cite some examples:

- In 1999, Tanzania adopted Vision 2025, where the objective is fixed for a growth rate of 8 percent per annum or more, with the objective of becoming by 2025 a diversified and semi-industrialized economy with a substantial industrial sector comparable to typical middle-income countries.
- In Rwanda, Vision 2020 was adopted by the government in 2002. Vision 2020 was the result of a national consultative process that took place in Village Urugwiro in 1998-99. The major aspiration of Vision 2020 has been to transform Rwanda's economy into a middle-income country, by 2020. Concurrently, in mid-October 2010 the then prime minister, Bernard Makuza, announced a new seven-year plan, designed by the government as a roadmap for the transformation of Rwanda into a middle-income country by 2017. Targets were announced which included:
 - a 30% increase in the level of access to electricity and a surge in national energy production from 80 mw to 1,000 mw;
 - the extension of financial services to 80% of the population;
 - the construction of 220 more coffee-washing stations in order to enable 80% of the total crop to be fully washed; and a 12% rise per year in industrial production.

The plan also promises quantifiable deliverables for social policy, with an emphasis placed on the country's reconciliation and social cohesion." (EIU, 2011).

- Kenya has adopted Vision 2030. The aim of Kenya's Vision 2030 is "to be globally competitive and prosperous country with a high quality of life by 2030." It aims at transforming Kenya into "a newly industrialising, middle income country providing a high quality of life to all its citizens in a clean and secure environment." A key objective is to meet the Millennium Development Goals for Kenya. The Vision was consultative involving an extensive stakeholders' process carried out between October 2006 and May 2007.
- Burundi has its Vision 2025 strategy. This aims to provide the efficient instrument of planning development, to develop policies and strategies for sustainable development. The vision is a materialization of the application of the "Arusha Peace and Reconciliation in Burundi." Signed in August 2000, its Protocol asked the Transitional Government "to undertake, with the support of the international community, a reconstruction program that integrates rehabilitation, peace building, promotion of human and freedom of the individual, economic growth and long-term development."

Notes

1 See the final section of this report, which summaries some of the projections for regional economies. According to a recent paper by Hausman et al. (2011), Uganda, Kenya and Tanzania all have the potential to sustain growth at above 6 percent per annum over the decade.

2 This is not to say that aid cuts are going to be applied across the board. There are a number of DAC countries which are keeping to their

commitments undertook at the G-20 Gleneagles Summit in July 2005. The UK, for instance, is planning to increase DFID's budget by 30% over the next two years – with a particular focus on fragile states. On the other hand, reducing dependence on aid is not just a supply argument but also a demand-side argument where recipient countries in the region are more and more willing to apply an 'aid- exit strategy'. See the foreword by Benjamin William Mkapa in Tandon (2008).

Macroeconomic performance and policy

1

CHAPTER

1.1. Growth Performance in the Region – An Overview

IN AGGREGATE, REGIONAL growth performance has been impressive over the last four years since the global financial crisis hit. Several of the region's economies are among the faster growing economies in the world, with Ethiopia, Rwanda and Uganda at the head of the pack (Table 1). This evaluation, however, has to be mitigated

to some extent by the demographic growth, which is still exceedingly high by international standards, implying that per capita growth rates are less impressive than the headline growth rates. Some policy implications of this will be discussed in a social policy section.

Table 1:

Average GDP growth (2008-2012)

Country	2008	2009	2010	2011*	2012**	Average 2008-2011
Ethiopia	11.2	10.0	10.4	10.0	8.6	10.4
Rwanda	11.2	4.1	7.5	8.8	7.0	7.9
Tanzania	7.4	6.0	7.0	6.5	7.3	6.7
Uganda	10.4	3.9	5.6	5.6	6.9	6.4
DRC	6.6	2.8	7.1	6.7	6.4	5.8
Djibouti	5.8	5.0	4.5	4.6	5.1	5.0
Burundi	4.5	3.4	3.6	4.2	5.2	3.9
Kenya	1.7	2.5	5.6	4.4	5.5	3.6
Seychelles	-1.3	0.7	6.3	4.0	4.5	2.4
Comoros	1.0	1.8	2.1	2.5	3.2	1.9
Eritrea	-9.8	3.6	4.0	7.9	6.1	1.4
Madagascar	7.1	-3.7	0.5	0.6	2.0	1.1
Regional Av.	7.3	5.0	7.0	6.6	6.8	6.5
Sub-Saharan Africa	6.1	1.7	4.8	4.4	5.3	4.3
OECD	0.1	-3.8	3.1	1.9	1.6	0.3
World	1.6	-2.4	4.0	2.8	2.6	1.7

Notes: * Fiscal year July (n-1)/Jun (n) **EAR average is the weighted av. (based on PPP GDP figures) for the EAR-11 (i.e. excluding Somalia and Djibouti, for whom the GDP weights are unavailable).

Sources: National estimates for 2011 are UNECA calculations, based on growth forecasts by AfDB/OECD/UNECA/UNDP (2011/12). Figures prior to 2011 from national sources and the EAC. Figures for SSA and World are from UNDESA, and figures for the OECD-34 are from the OECD (2012). Figures for 2011* are estimates, and 2012* are forecasts. Where quarterly GDP data are available, 2011 growth rates have been re-estimated (Kenya, Tanzania and Rwanda) by UNECA SRO-EA.

This caveat aside, since 2008 the region has showed remarkable resilience in the face of the most serious crisis to hit Western Europe and the United States since the 1930s. Despite suffering the effects of severe drought conditions and famine, and of rising food and fuels prices, most countries in the region have maintained their growth trajectory, making the Eastern Africa region the fastest growing sub-region in Africa in 2011. In the majority of the countries of the region, the expansion of economic activity has benefited from a combination of mutually

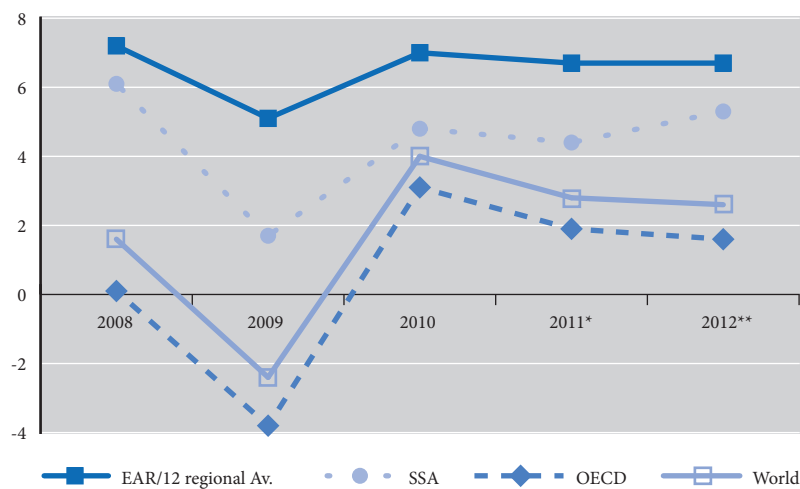
reinforcing factors, most notably sustained public investments in infrastructure (Ethiopia and Tanzania), rising mining output (Tanzania), rising foreign direct investments in energy (Uganda), and increased agricultural production (Ethiopia) (UNECA, 2012-forthcoming). Beyond these specific country factors, strong domestic demand and investment at the regional level has generally contributed to the solid economic performance. Part of the explanation also resides in a greater export diversification in the sub-region, compared to other African regions,

both in terms of products and trading partners, helping Eastern Africa to weather the severe external shocks from the global financial crisis much better.³ It is also partly the product of sustained external support through ODA and

from new emerging partners such as China – a testimony to the importance of ODA as a countercyclical flow of finance for low-income countries in times of economic crisis (see Section 1.8).

Figure 1:

An Exceptional Regional Performance, 2008-2011



Source: Refer to Table 1 sources

For many countries in the region, agricultural performance is still one of the key liabilities in terms of maintaining a strong economic performance, and is still highly dependent on the vagaries of the weather.⁴ In 2011 agricultural output has been hampered in much of Eastern Africa by poor rains. The IMF (2011) estimates that although the initial impact on output in Ethiopia and Kenya – the two most directly affected economies – will be less than half a percent of GDP, the final impact of the drought and its ramifications throughout the region, could ultimately be much larger. For example, in Tanzania, the drought has reduced hydroelectric power generation, with attendant implications not only for output but also for fiscal accounts, in terms of reduced tax income.

The policy responses to the drought have been various. For instance, following the Malawi example, government supported farmer input programs are being implemented in Rwanda and Tanzania. Some governments in the region

(e.g. Ethiopia) have experimented with price controls on foodstuffs, though these have not proven to be effective, and were quickly retracted. Kenya is currently seeking \$1 billion over the next 10 years to build 30 large dams so as to mitigate the impact of climate change.⁵ More detailed analysis of the situation and policy responses to the food crisis and drought in the Horn of Africa are discussed in section 3 of this report.

In contrast to the mixed performance of the agricultural sector across the region, the growth of the service sector has been vigorous in most cases. For instance, Ethiopia's spectacular growth of the past six years has been driven largely by the services sector, which has seen substantial investment by government and the private sector.⁶ Another example is Kenya, which has become a regional hub of professional services such as accounting and computer-aided design. The country has taken advantage of information and communications technologies-enabled services because

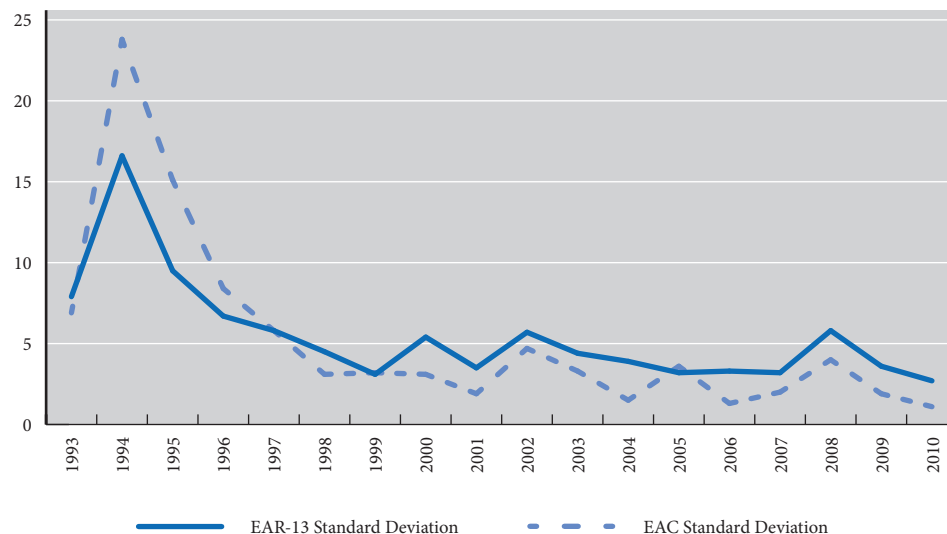
of cost advantages, investment in enabling infrastructure (particularly fibre-optic cable), and in a reasonably well-educated and urbanised workforce (IMF, 2011: 50).

Another interesting dimension of growth in the region is that the dispersion in growth performance is declining over time (Figure 2), as illustrated by the standard

deviation of growth performance within the EAC. The causes behind this are multiple – partly the product of a more robust external environment (high prices for export commodities, growing demand for regional exports from emerging partners, lower debt burden) – but also indicative of greater coordination among regional economies in terms of macroeconomic policies.

Figure 2:

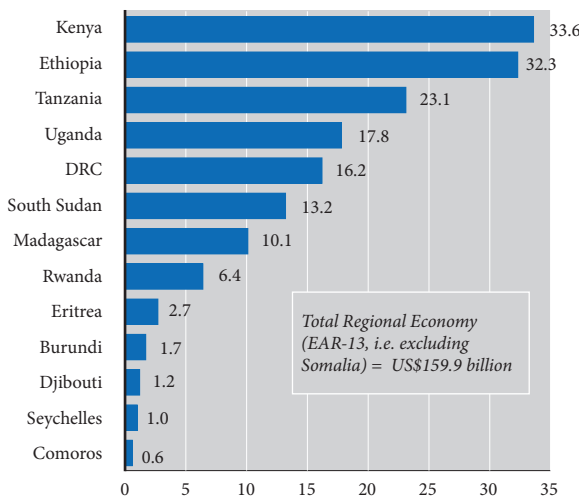
Growing together? The Falling Dispersion of GDP growth within the EAC Standard Deviation of Growth, 1993-2010



Source: UNECA calculations, based on data from UNCTAD <http://unctadstat.unctad.org/>

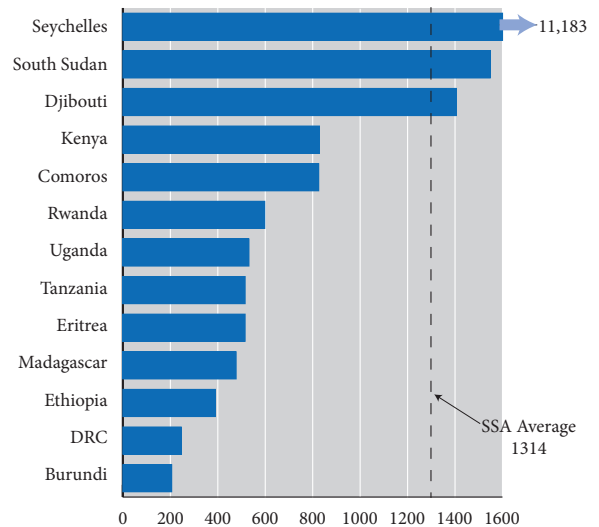
According to UNECA estimates based on official member state figures, and measured in US\$, after several years of sustained growth in excess of 10 percent, 2011 saw Ethiopia approach Kenya as the region's largest economy (Figure 3) (US\$ 32.3 billion vs. US\$ 33.6 billion). This was accelerated by a combination of both faster growth in Ethiopia and a sharper devaluation of the Kenyan shilling vis-à-vis the US dollar than the Ethiopian birr. Together, Ethiopia and Kenya now account for approximately 45 percent of the regional economy.⁷ According to UNECA

estimates, the GDP of the whole EAC-12 region in 2011 (i.e. excluding Somalia, for which reliable GDP data do not presently exist) was US\$ 160 billion, compared to a total GDP for SSA of US\$ 1.22 trillion, thus representing approximately 13 percent of SSA GDP.⁸ Bearing in mind the region is home to 32 percent of the SSA population, this implies that the region is quite seriously under-represented in terms of GDP per capita.

Figure 3:**Nominal GDP 2011 Eastern Africa Region (blns US\$)**

Source: UNECA forecast, based on national sources

In terms of per capita incomes, then, the story is somewhat different. Despite a relatively sluggish economic performance over the last three years, being particularly negatively impacted by the global economic slowdown and the reduction in tourism receipts, Seychelles continues to be the highest income country in the region, with a per capita income in excess of USD 11,000 (Figure 4). South Sudan is the second highest⁹, and Djibouti the third. All other economies in the region are below the SSA average. Kenya's GDP per capita is still approximately three times that of Ethiopia, but because of the much larger Ethiopian population, the Ethiopian economy is only a little lower than that of Kenya. Burundi and the Democratic Republic of Congo are at the other extreme – the two poorest economies in the region in per capita terms. In view of the massive existing resource riches of DRC, and potential resource riches of Burundi¹⁰, there is

Figure 4:**Nominal Regional per capita GDP (US\$), 2010-11**

an opportunity to turn this situation around providing the right mining and natural resource extraction policies are in place, and governance challenges are resolved satisfactorily. Coincidentally, this is also true for several other countries in the region, where there have been a number of new-found discoveries and/or exploitation of natural resources, including oil (Uganda, Kenya), (gold) Eritrea, and gas (Tanzania), among others. South Sudan's rich resource base is also highly relevant here. In short, the region is perhaps on the verge of shaking off the image as a 'resource-poor' region (see Box 2). It is precisely for this reason that UNECA SRO-EA has decided that the ICE Meeting 2012 is focused on how to achieve better governance of the natural resource sectors, through new African-led and owned initiatives like the African Peer Review Mechanism (APRM).

1.2. Governance and Growth

IN THE 1960S and 70s, economic theory stressed the importance of sustaining high levels of physical capital investment. In the 1980s, however, there was a reaction against the focus on physical capital accumulation. As well as increasingly recognizing the key role of human capital, there was a growing acknowledgement of the role of governance in producing satisfactory development outcomes. There is still much debate over the exact meaning of what constitutes 'good governance'. One important regional contribution to the debate is Mo Ibrahim Foundation's 'Good Governance' Indicator, which is based on independent assessments on progress involving the analysis of 86 indicators grouped into 14 sub-categories and four overarching categories to measure the effective delivery of public goods and services to African citizens.¹¹

Figure 5 shows the relationship between changes in the governance- using the 'Good Governance' indicator- and economic growth for the whole of SSA over the period 2006-2010. Highlighted in red are the countries within the region (Figure 6). It is interesting to note that there is in fact a fairly wide-variability in the relationship between the two variables – some countries with a low or negative score in terms of improvement in the Mo Ibrahim index have experienced quite fast economic growth and, conversely, some countries with a good performance in the Mo Ibrahim index have posted less robust results in terms of economic growth. Nonetheless, the overall relationship is positive, suggesting that in general there is a correlation between improvements in governance and economic growth, albeit a weak one.

Growth and governance – a large degree of variability across the region

Figure 5:

GDP growth 2006-10 vs Mo Ibrahim Index 53 SSA Countries

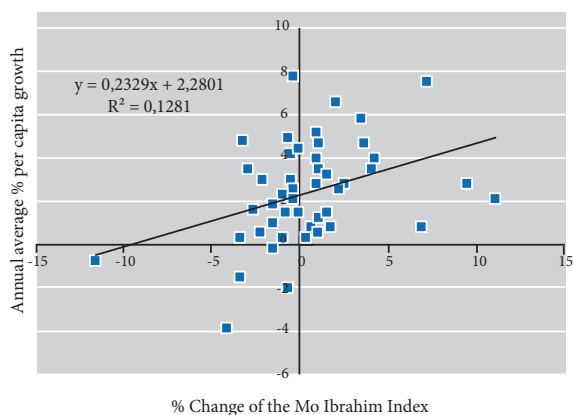
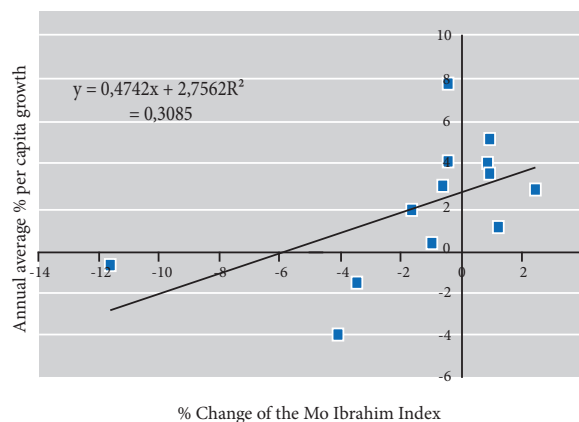


Figure 6:

GDP growth 2006-10 vs Mo Ibrahim Index - EAR-13



Source: Mo-Ibrahim Foundation (2011), UNCTAD online database (2011).

For a low-income country, economic governance in Rwanda continues to stand out in terms of its ranking in international assessments, such as the Africa Competitiveness Report (ACR) (2011). The ACR includes assessments of more than half of the region's countries (7 countries out of the EAR-13). In that report, Rwanda's overall placement was 80, out of a total of 139 countries surveyed. In financial market development, Kenya stands out, obtaining a global ranking of number 27. But in terms of the quality of its institutions, Rwanda achieves a quite remarkable ranking of number 19 globally. In terms of labour market efficiency, Rwanda is evaluated even

more highly by the ACR, ranking number 9 in the world. Of course, the evaluations of what constitutes 'good' in terms of these different aspects of economic governance are inevitably subjective. Nevertheless, the fact that a low-income country ranks so highly in an international ranking is an impressive achievement. The example has spurred other countries in the region to take measures to improve their competitiveness. For instance, Burundi has recently instigated measures under a new investment law to speed up the starting up of new businesses, reducing the average time taken to register a business from 32 days to just 2 days.¹²

Box 2: Eastern African: A region of contrasts?

With a total population of 322 million, Eastern Africa accounts for approximately 32% of the population of the African continent. The region has many topographic extremes, including Africa's highest and second highest mountains (Mount Kilimanjaro and Mount Kenya). Approximately 85% of the highlands of the African continent are located in the region, split between the Ethiopian and Kenyan highlands. Eastern Africa also hosts the lowest part of the continent - the Danakil Depression. Beyond the topographic extremes, the region also displays an interesting array of policy-driven outcomes, among which are the following:

- Seychelles has 1,049 mobile phones per 1,000 people; Eritrea has 28 per 1,000 people. They are the countries with the highest and lowest number of mobile phones per 1,000 people in Sub-Saharan Africa.
- Between 2000–2009 Rwanda and Uganda made the greatest gains in life expectancy - 8 and 7 years, respectively - in the Sub-Saharan African region.
- Madagascar has the highest reported primary school enrollment rate in the world (160 percent of enrollments of the relevant age group). Somalia has the lowest primary school enrollment rate in the world, with only 33 percent enrollment rate.
- Rwanda has the highest number of women in national parliament, with 56% of total seats in the world. Comoros has the lowest with 3%.
- The largest recipient of net official development assistance (ODA) in Sub-Saharan Africa received an amount 165 times larger than the smallest recipient. The largest recipient is Ethiopia, and the smallest is Seychelles.
- Infant mortality increased by 21% in Democratic Republic of Congo during 1990-2009, the largest increase in Sub-Saharan Africa. The largest drop was in Madagascar, by 60%.

Source: Drawn from Reader (2001), WDI (2011), The Economist (2011).

1.3. Renewed Inflationary Pressures

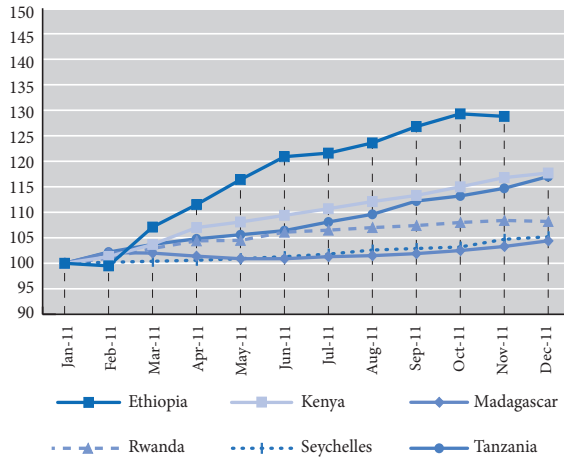
INFLATION IS BECOMING a major problem again across the Eastern Africa region. In Ethiopia, prices peaked in September 2011 at over 40% year-on-year increase; in Kenya in November, up from 18.9 per cent. It was reported in October that Kenyan Airways had ceased to bill customers in Kenyan shillings, and now bills customers directly in US dollars, as a way of hedging against inflation. In Uganda, it moderated somewhat, to 29 per cent in November, from 30.4 per cent the previous month. Rwanda's cost of living rose to 7.7 per cent in October, up from 6.6 per cent the previous month, while in Tanzania, inflation shot to 17.9 per cent in October, up from 16.8 per cent a month earlier. Madagascar, in contrast, has achieved a moderate rate of inflation, average an estimated 2.4 percent over the year, helped by the exchange-rate appreciation which contributed to tightening monetary conditions from the second semester onwards. There are at least 10 countries in the region where in the third quarter of 2011 non-food inflation was above 10%, including Ethiopia, where overall inflation was close to 40% and Uganda where it was standing at around 20%. Food prices accelerated in 2011 by 36%, 27% and 17% in Ethiopia, Uganda and Kenya, respectively (Figure 8) (UNstats, 2011). The worst inflationary performance, however, was experienced by the South Sudan, shortly after the introduction of the South Sudanese pound in August 2011 – in October it registered inflation equivalent to an annual rate of 71.7 percent – though it subsequently moderated somewhat towards the end of the year and the beginning of 2012.¹³

It is clear that for Eastern Africa, a region which is largely dependent on fuel products and food imports, commodity

price inflation has been a major problem. Burundi, Rwanda and Uganda are landlocked and rely on fuel imports through the northern corridor to Mombasa on the Kenyan coast and through the central corridor to Dar es Salaam on the Tanzanian coast. The cost of fuel therefore has a disproportionately large impact on domestic inflation. In Ethiopia, drought has played a role in inflation. An equally important factor for Kenya, Uganda and Tanzania was September 2011's sharp exchange rate adjustment against the backdrop of looser monetary conditions and high public spending.

Nonetheless, the negative repercussions of higher commodity prices needs to be put against the context of the extent to which countries in the region have also benefited from higher prices for their export commodities, such as tea and coffee, something which on balance has had a positive impact on regional growth performance. This impact in turn has to be balanced against a rising import bill for fuels and other commodities which the region lacks. As shown in Figure 20, the terms of trade in 2011 have generally not been favourable for most countries in the region. Finally, rapidly shifting relative prices over the last 5 years have impacted in a differential manner on consumers and producers, urban and rural dwellers within the region, producing a wide range of distributional effects. Disentangling these effects is beyond the scope of the present report, but it is important to note their complexity when discussing the social and economic impacts of the price rises.¹⁴

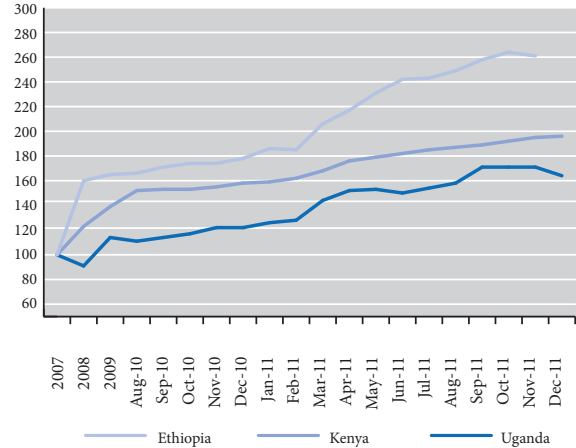
Figure 7:
National CPI Inflation Index 2011 (January=100).



Source: National Sources, 2011

Concerns have also been raised about the impact of rising public sector wages on the fiscal situation, diverting resources away from development expenditures. Kenya's pay to state workers rose from \$2.1 billion in 2006 to \$3 billion in 2010, pushed up by higher salaries for teachers and other civil servants. Similarly in Tanzania, the wage bill has nearly tripled from \$537 million in 2006 to \$1.5 billion in 2011.¹⁵ The situation is even more difficult in Burundi, where the government is spending \$264 million on salaries in 2011, a four-fold increase from five years ago. Although Rwanda has made strident efforts to contain the share of its budget dedicated to salaries, and thereby maximizing non-recurrent development expenditures, Rwanda's spending on civil servants rose to \$200 million in 2010, from \$114 million in 2005. Such pressures are of course difficult to resist when living standards for public employees are being eroded rapidly by higher-than-anticipated rates of inflation – regional governments already have to contend with the loss of skilled employees to better remunerated posts in the private sector or (more frequently) positions in international organizations. But the implications of

Figure 8:
Food price Indices, Ethiopia, Kenya and Uganda (2007=100)



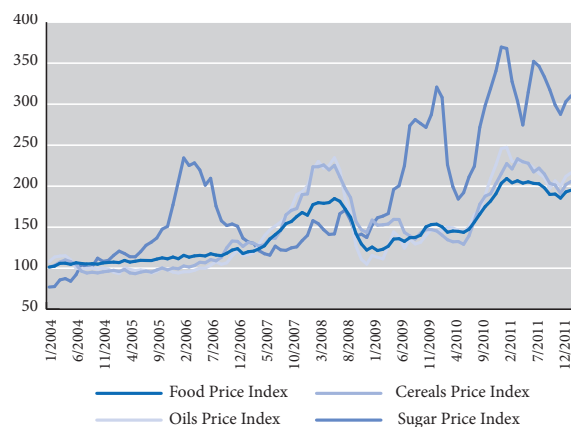
Source: UNstats, 2011

expanding recurrent expenditures like salaries rapidly can be serious, undermining the considerable efforts made by regional governments to increase the share of non-recurrent expenditures (i.e. for long-term development) in total expenditures.

The key concern, however, is the impact of inflation on social stability, as well as its impact on economic growth and macroeconomic stability.¹⁶ Governments in the region have responded in a variety of ways, including the introduction of price controls. Ethiopia, Uganda and Kenya have implemented such measures– though they have not proved particularly effective in mitigating price increases (Ethiopia experimented with price controls in the first half of 2011, but they were abandoned after five months). Rwanda temporarily reduced duties on fuel, so as to limit the carry-through impact of fuel prices onto other domestic prices and also to reduce the impact on the transport sector. Given the importance of food price inflation in overall CPI inflation, more long-term approaches include measures to increase agricultural output. Rwanda has taken a number of additional measures to

moderate food price increases, including the launch of the crop intensification programme which includes land consolidation, an accelerated irrigation programme and improved input provision through the fertilizer subsidisation schemes, with the goal of increasing agricultural crop productivity. The government is also rapidly building up a strategic grain reserve, which is expected to reach 60,000 tonnes by the end of the current fiscal year. It is worth noting that these measures started showing results. As of June 2011, food imports had declined by almost 20% in volume compared to the same period in 2010 (World Bank Rwanda Study, 2011). With a similar objective in mind, Kenya has recently announced it is seeking funding of \$1 billion over the next 10 years to enable the construction of 30 large dams, in order to mitigate the impact of climate change.¹⁷

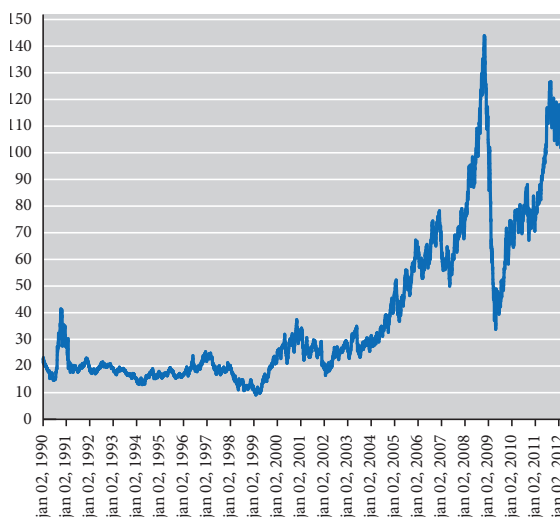
Figure 9:
FAO food price Indices (2004=100)



Source: FAO, 2011

Designing the right policy response is dependent upon a sound diagnosis of the underlying causes of this inflationary bout. What are the causes of these inflationary processes? As mentioned earlier, the most commonplace explanation is related to increasing prices for foodstuffs and imported inputs, particularly fuel, but this in itself is not a sufficiently convincing explanation. Global commodity prices accelerated from May 2010 but peaked in mid-2011 (Figure 9 and Figure 10), due to increased global demand for commodities and weather related food supply shocks. In the Eastern Africa region -where food is the largest component of the consumption basket- inflation has been fuelled by high food and energy prices coupled with expansionary monetary and fiscal policies put in place as a response to the 2008 financial crisis.

Figure 10:
Daily Europe Brent Spot Price FOB (Dollars per Barrel)
1990-2012



Source: Thomson Reuters, 2012

Unfortunately, recent empirical studies on the determinants of inflation applied to the Eastern Africa case have been rather scarce.¹⁸ Generally speaking, empirical studies on the region find that inflation is the result of both ‘cost push’ (e.g. higher fuel or input costs) and ‘demand pull’ (e.g. excessive demand pressures) factors, though psychological/sociological determinants associated with expectations have also been shown to play an important role. Thus inflation tends to be the consequence of a combination of variations in monetary policy, fiscal policy, exchange rates, the prices of imported commodities, in-built expectations driving to a wage-price spiral, agricultural production, etc. Recently, some skepticism has been expressed regarding the traditional channels of monetary transmission of inflation in the context of low income countries with little financial market depth (Mishra et. al., 2010). Buigut (2009) examined monetary transmission in three countries (Kenya, Tanzania, and Uganda) belonging to the Eastern African Community (EAC), and found that changes in policy interest rates had

only small and statistically insignificant effects on output and inflation, and concluded that monetary transmission is weak in all three countries. In sum, monetary policy alone may have only limited ability to slow inflation in the sub-region, which is largely determined by fluctuations in local agricultural output and world commodity prices.

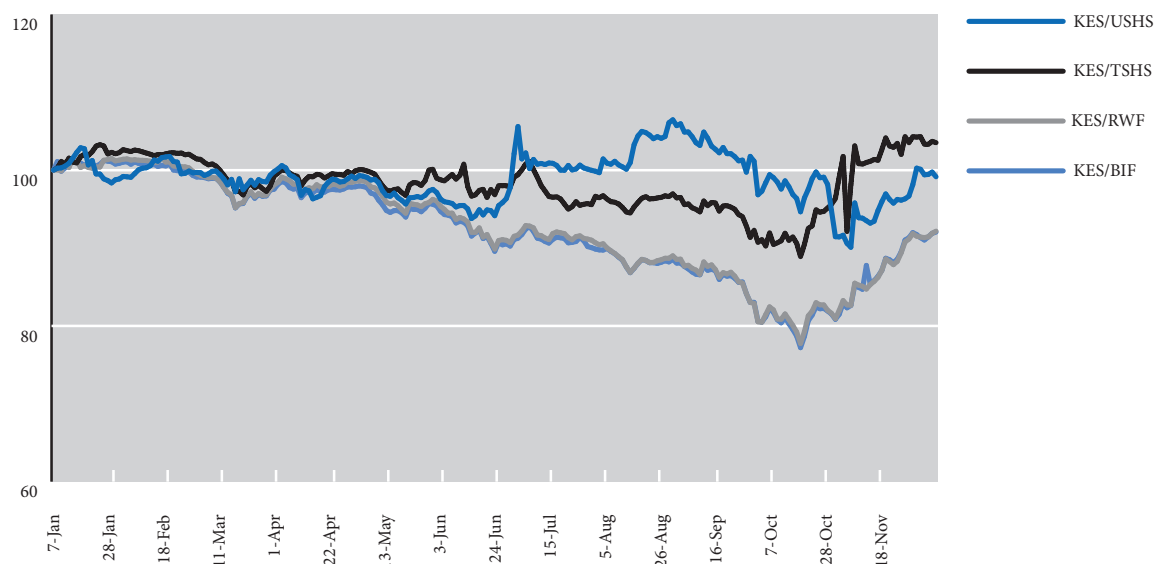
In contrast, there is evidence to suggest that the exchange rate channel may be operative in at least some low-income countries that allow more scope for market determination of exchange rates (Mishra et. al., 2010). For example, in Kenya, which maintained a managed float during the period under study, Cheng (2006) used VAR techniques to find that policy-driven interest rates had a considerable impact on the foreign exchange value of the shilling. Pointedly, however, the exchange rate channel accounted for about one-fourth of the variation in inflation. As we shall see in the next section, this finding has particular relevance to the Kenyan experience in 2011.

1.4. Exchange Rate and Monetary Policy Evolution

UNTIL THE SECOND semester of 2011, interest rates in the region were generally moderating, in part influenced by the global context where there has been a significant reduction in interest rates in many industrialized countries to levels which implied negative real interest rates (the first time that this had been seen since the 1970s). Despite the evidence cited earlier regarding the relative ineffectiveness of changes in policy rates, EAC central banks have tightened monetary policy in response to increased inflation rates. Perhaps more relevant, however, is the exchange rate evolution, which in countries like Kenya and Uganda has become key to understanding the inflationary pressures – inflation has accelerated as the exchange rate has devalued. The Central Bank of Kenya tightened monetary policy in September by lifting the central bank rate to 7%, but the increase was too modest to defend the Kenyan shilling which had been depreciating

sharply over the course of 2011. Only in December 2011 was there a reprise in downward pressure on the Kenyan shilling, which started to recover on the back of weaker demand for the US dollar.

It is interesting to compare trends with respect to the country registering the lowest inflation in the region in 2011 – the Seychelles. The Central Bank of the Seychelles formerly relied on exchange-rate management to tackle inflation, as most consumer goods are imported, but since 2008 the country adopted a liberalization programme whereby the rupee was freely floated. It has subsequently employed indirect instruments, including Treasury-bill auctions, to help manage money supply and, after a period of prolonged devaluation of the rupee, the exchange rate stabilized in 2011.

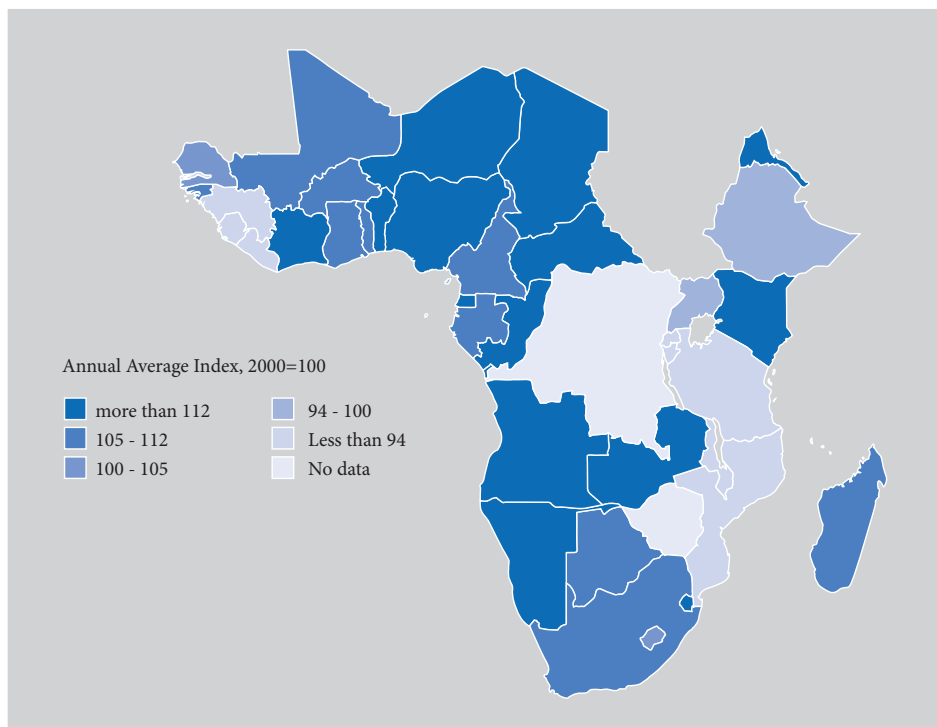
Figure 11:Nominal Value of Eastern African currencies relative to the Kenya shilling, 2011¹⁹

Source: Calculated from figures from the Kenyan Central Bank

Also interesting in terms of the evolution of the exchange rate (Figure 11) is the comparison between the Ugandan and Tanzanian shilling, on the one hand, and the Rwandan and Burundian franc, on the other. The Rwandan and Burundian Franc have remained broadly stable against the US dollar over the course of 2011. The Rwandan franc depreciated by only 0.9% against the US dollar in the nine months from December 2010 to September 2011, and strengthened against other Eastern African community currencies (with the exception of the Burundian franc) (World Bank, 2011). The other notable country in the region experiencing a much higher degree of exchange rate stability is Comoros, whose currency is pegged to the euro, restricting growth in the monetary supply and providing an important degree of price stability. However, given the great uncertainty surrounding the future of the euro, this could be a mixed blessing, in the sense that it could prove to be a future source of instability.

It is interesting to note that, from a longer term perspective, real effective exchange rates (REER) (i.e. exchange

rates which factor in inflation rate differentials between trading partners) in Eastern Africa have been weak compared to the average for Sub-Saharan Africa (Figure 12) – that is to say, in real terms regional currencies have failed to revalue to the same extent as other parts of the continent, particularly the resource rich countries of Central and West Africa. This is partly a reflection of weaker natural resource endowments, which reduces the demand for regional currencies. A weaker REER has the important advantage of helping maintain regional competitiveness for exports. However, given the superior growth performance of the Eastern Africa region over recent years, with several of the fastest growing economies in the world, it is conceivable that in the future there will be a real appreciation in regional currencies once the turbulence in international markets has subsided. This said, this is dependent on assuring that macroeconomic stability is not compromised by inflation or excessively lax fiscal and monetary policy.

Figure 12:**Real Effective Rates are weak compared to the SSA average -2000-2011**

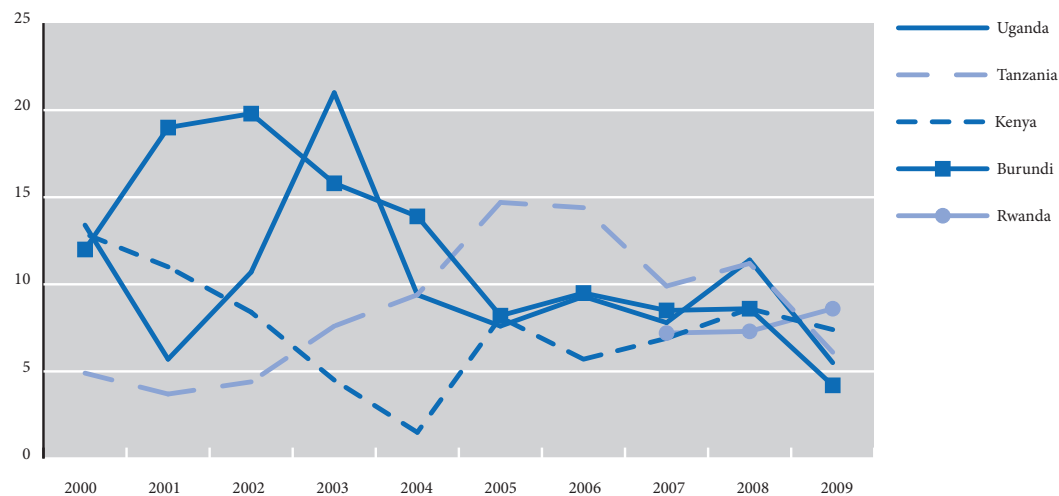
Source: calculated from IMF datamap, November 2011.

In response to the situation created by both sharply declining nominal exchange rates and also higher inflation, Eastern African central bank governors, on October 12th 2011, agreed to coordinate on tightening monetary policy. In October, Kenya hiked benchmark interest rates by 400 basis points, Tanzania increased interest on its discount window by 200bps to 9.58%, Rwanda by 50 bps to 6.5% and Uganda increased by 300 bps to 23% on 1st November. The Bank of Uganda claims that as a result of the interest rate hikes, the shilling has regained most of the value lost against the US dollar in 2011. It is interesting to note that

over the last decade there was in fact a slow convergence of interest rates across the EAC region (Figure 13), demonstrative of an increasing degree of macroeconomic coordination. But the bout of inflation and exchange rate volatility seen in 2011 risks undermining this achievement as interest rates edge up sharply in the second semester (Figure 14). The rise in interest rates is particularly worrying from the point of view of starving off new investment by small and medium enterprises (SMEs), which are important generators of employment.

Figure 13:

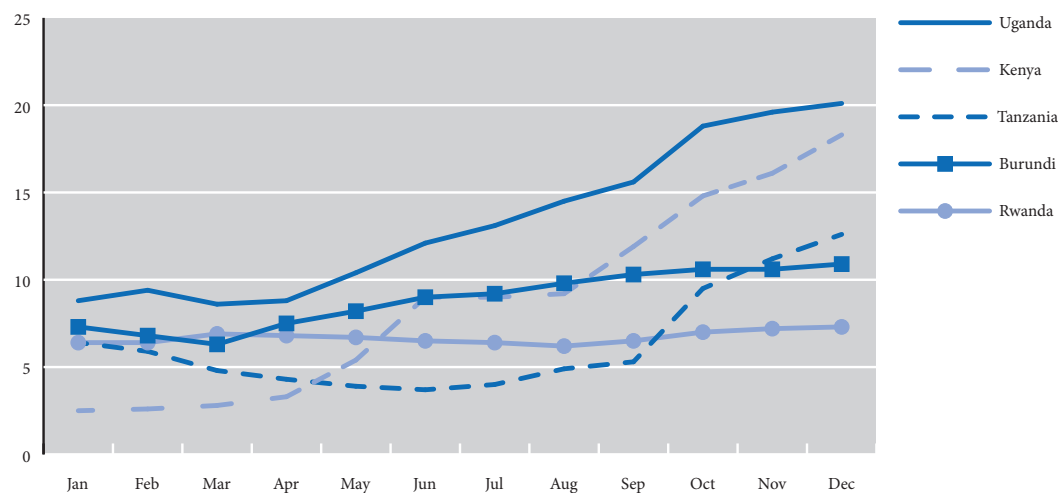
A slow convergence of interest rates across the EAC in the 2000s – Central Bank Rates, 2000-9



Source: EAC, 2011

Figure 14:

Interest rates in the EAC have been edging upwards....3-month Treasury Bill rates, 2011



Source: National Central Banks

1.5. Trends in Regional Trade

DESPITE INITIALLY PESSIMISTIC appraisals, in the aftermath of the financial crisis, there was a strong (and partially unexpected) rebound in Sub-Saharan Africa (SSA)'s trade growth, something that was particularly notable in the EAR. The increase was ascribable to rising demand for commodities from the emerging markets, and the rapid rebound in global commodity prices after the sharp falls in the last quarter of 2008. As a result, after falling in 2009-9 by nearly 10 percent to US\$ 59.5 billion, total EAR-13 trade (excluding South Sudan) was worth

US\$ 70.15 billion USD in 2010 (Table 2). Given the size of the regional economy (US\$ 147blns for the EAR-13), this means that, using the standard definition of 'trade openness' as total imports and exports as a share of GDP, the Eastern Africa region is extremely open to trade, with all the attendant advantages and vulnerabilities that this entails. Kenya, Ethiopia and Tanzania are the major traders, accounted for 24.6, 17.5 and 16.7 percent of total regional trade respectively.

Table 2:

Total Exports and imports of goods and services, billions of US dollars at current prices

	2008	2009	2010	Trade, % of GDP, 2010
Burundi	0.46	0.46	0.61	46%
Comoros	0.18	0.18	0.2	38%
Djibouti	0.64	0.53	0.49	44%
Eritrea	0.61	0.6	0.7	30%
Ethiopia	10.28	9.59	12.27	57%
Kenya	16.05	14.67	17.24	57%
Madagascar	5.52	4.26	3.63	43%
Rwanda	1.44	1.5	1.73	32%
Seychelles	1.48	1.2	1.3	138%
Somalia	1.55	1.35	1.41	-
Uganda	6.73	6.57	6.83	43%
Tanzania	10.12	9.28	11.75	51%
DRC	8.7	7.3	9.9	78%
Total	65.77	59.51	70.15	57%
Median	1.78	1.76	1.87	54%

Source : UNCTAD trade statistics, authors calculations

The degree of openness to international trade in the region is reflected quite clearly in developments regarding trade policy. Tariffs have come down sharply in the region over the last two decades, partly in response to unilateral processes of liberalization encouraged by international organizations, partly through the implementation of multilateral agreements and, more recently, through regional processes (COMESA, SADC and EAC).²⁰ In countries such as the Seychelles, Burundi, Kenya and Djibouti, the scale of reductions in Most Favoured Nation (MFN) tariffs since 2001 compares favourably, in percentage terms, with reductions in high income countries (Table 3), such as the EU and the United States (albeit from much higher levels than those which prevail in high income countries).²¹ Uganda, in contrast, was an early trade liberalizer, and

actually found its MFN tariffs on manufactured goods and minerals increasing in the 2000s to align its tariff regime with that of its EAC partners.

In spite of the global financial crisis then, most countries in the region experienced growth in the total trade values for the period 2008-2010. Four countries in the region (Madagascar, Djibouti, Seychelles and Somalia), however, did report declines in trade over the same period, due to diverse factors including disruptions to shipping in the Horn of Africa caused by piracy, the continued conflict in Somalia, and the suspension of Madagascar from the African Growth and Opportunity Act (AGOA) trade agreement with the United States of America.

Table 3:

Most favoured nation rate (MFN rate) and effectively applied rate, annual, 2001-2010 (or nearest available year).

	2001	2010	% reduction 2001-10
Seychelles	25.3	4.8	-81.3
Burundi	21.0	9.1	-56.9
Kenya	18.8	11.6	-38.2
Djibouti	32.6	21.4	-34.5
Tanzania	14.1	12.4	-12.0
Ethiopia	19.1	17.8	-7.0
DRC	12.8	12.6	-1.6
Rwanda	9.4	9.6	2.6
Uganda	7.7	11.5	49.1
Madagascar	5.2	10.3	99.0
Eritrea	9.9	NA	NA
Comoros	NA	8.3	NA
Memo:			
EU	3.6	2.9	-18.7
US	3.2	1.8	-42.2

Source: UNCTAD data. Note: MFN tariffs are for Manufactured goods, ore and minerals. NA- not available.

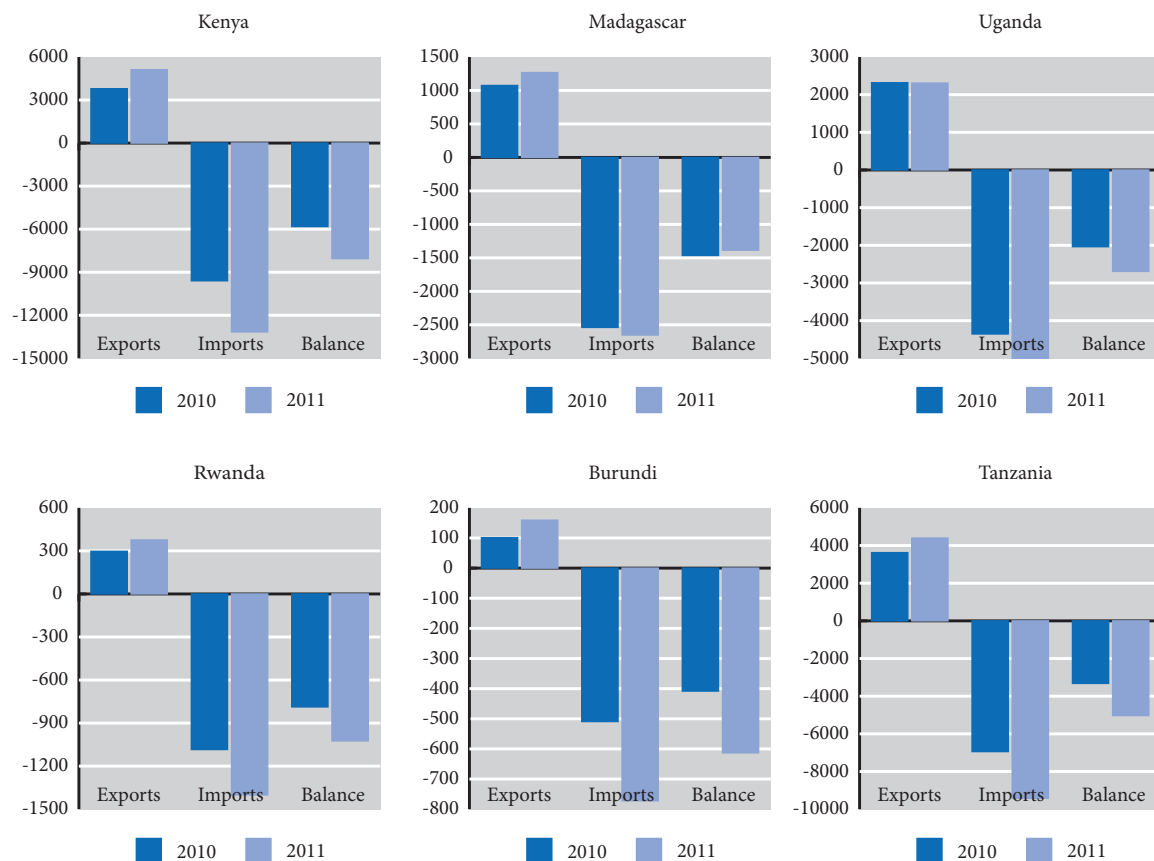
Trends in exports values for 2011 where monthly or quarterly data are available suggest a strong performance in a number of countries in the region.²² For example, thanks in part to the strength of the US dollar against the shilling the main Kenyan export earners of tea and horticulture (at over US\$1 billion a year) performed well in 2011. Similarly, in Tanzania, the value of export of goods and services stood at US\$ 6.58 billion in the year ending August 2011 compared with USD 5.3 billion recorded a year earlier, largely attributable to the increase in gold prices on the world market²³, greater demand for manufactured goods from neighbouring countries, as well as an increase in

unit prices of coffee and cashew nuts, the export volume of tobacco and an increase in the number of tourist arrivals (Bank of Tanzania September, 2011).

Price effects predominated in explaining the good export performance in the region, however - in volume terms, exports did not always respond so positively. In Burundi, for instance, coffee exports were lower following poor harvests (GoB, 2012). A similar story can be told in Rwanda, where coffee export volumes fell by -16 percent over the course of 2011, but the fall was offset by higher export prices, translating into a 33 percent increase in coffee export values.

Figure 15:

Exports, Imports and Trade Balance 2011 (in millions US\$)



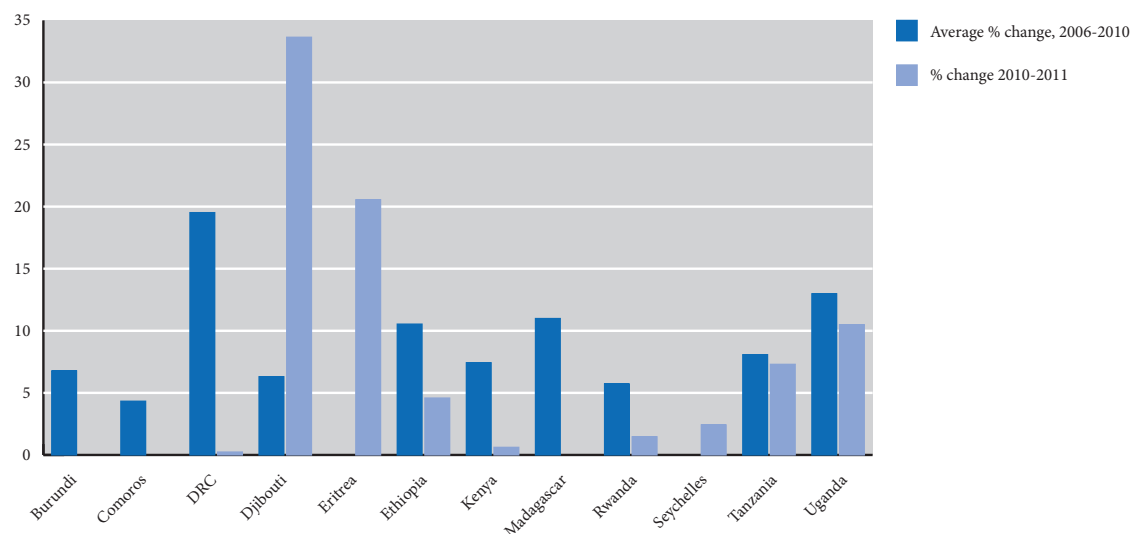
Source: UNECA estimates from national sources

Broadly speaking, export growth in the region has not kept pace with surging imports, with the consequence of a deterioration in the trade balance. This is principally attributable to the rising price of fuel and food imports, on which the region is particularly dependent (see Box 3), but also in some cases due to exchange rate developments, as well as the low capacity for export in particular cases. For example, Comorian exports of ylang-ylang, vanilla and cloves fell sharply in 2010 and have been dwarfed by goods imports (EIU, 2011). As recorded in Figure 16, there has been a marked increase in the volume of imports in 2011 in Djibouti and Eritrea, but import growth has

been rapid too in the cases of Ethiopia, Tanzania and Uganda. In the Eritrean case, this is related to both food and capital goods imports. On the former, Eritrea is one of the few countries in the region that has not declared a famine emergency, and it is likely that food imports went up in 2011 to meet domestic demand. The latter relates to the importation of agricultural machinery in large quantities, and the import of heavy equipment for a new cement factory launched in 2011. Across the region, the increased fuel import bill (rather than volumes) has weighed heavily on regional trade balances.

Figure 16:

% Change in Volume of imports, 2006-2011



Source: IMF, authors' calculations

A partial exception to these trends was Madagascar, which in 2011 have combined more modest import growth with a stronger export performance. In Madagascar, after the problems encountered due to the application of sanctions in 2009, it appears that there has been some recovery in both export volumes and values. Measured in US dollars, the export of goods expanded by 18 percent in 2011, standing at US\$ 1.3 billion. Some recovery in textile exports, after the sharp fall in 2009 and a subsequent more modest

fall in 2010, are also evident (Table 4).²⁴ In sum, across the region there are signs of an improved trade performance in 2011, something that should be confirmed once the data for the full year is available for all countries.

Table 4:

Exports of the Madagascar Free Zone, 2008-1st Semester 2011

Exports		2008	2009	2010	2011
Sea food and other Fish Products	Value	37.4	20.4	19.8	20.3
	Volume	4.6	2.9	2.6	2.4
	Unit Price(PU)	8.2	6.9	7.7	8.6
Textiles	Value	163.3	119.2	101.9	108.9
	Volume	14.3	11.5	7.7	7.1
	Unit Price	11.4	10.4	13.3	15.4
Others	Value	26.7	23.8	34.5	45.2
	Volume	7.2	6.4	9.4	12
	Unit Price	3.7	3.7	3.7	3.8
TOTAL		227.4	163.4	156.2	174.4

Source: *Bulletin de la Banque Centrale de Madagascar* * Values in millions of Special Drawing Rights, volumes in thousands of tons and unit prices in SDRs per kg.

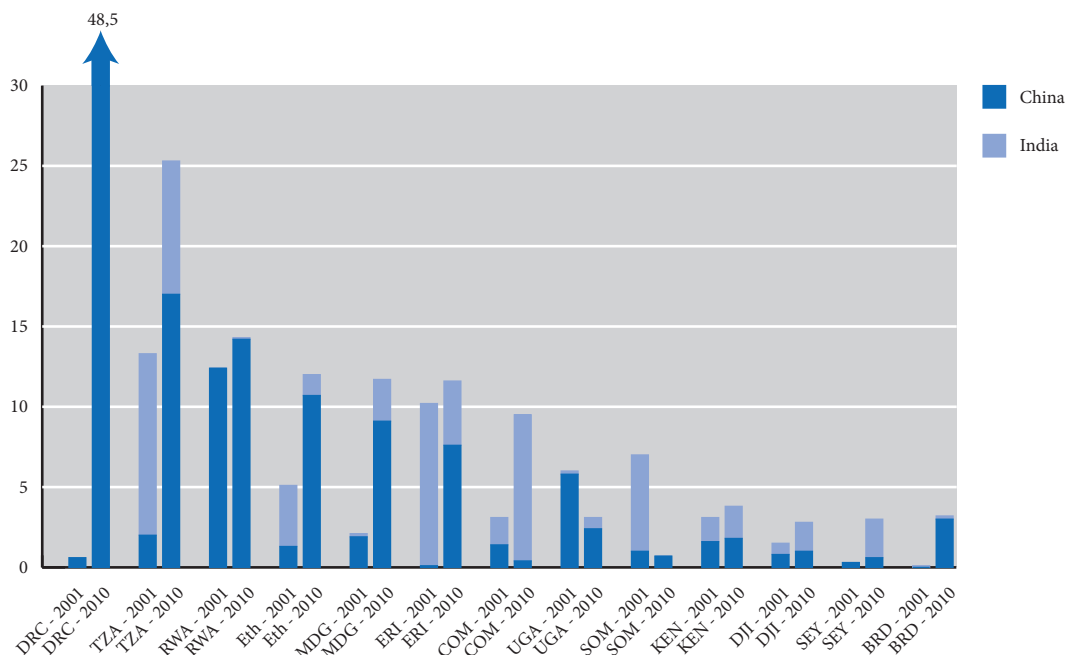
Countries in the region have also been successful in recent years in diversifying their exports away from traditional export markets towards new trading partners. This is important to the extent that it allows countries from the region to reduce their dependence on traditional trading partners and increase their resilience to economic shocks. As a reflection of progress in regional integration, intra-African exports have grown significantly as a share of total trade over the last decade. In 2010 Rwanda, Uganda and Kenya had the largest share of exports which remain within the Sub-Saharan region, accounting for 58%, 35% and 34% of their total exports, respectively. For some exporters, new regional markets have emerged in the manufacturing sector. For instance, Kenya has increased its machinery and transport exports within the EAC region.

Especially remarkable has been the rise of China and India as new export destinations since the early 2000s.

For instance, in 2010 Sino-EAC trade stood at nearly \$4 billion, an increase of 39 percent on the previous year.²⁵ Kenya's chemical exports have begun to rise in Asia, especially India, which could become the base for future export growth beyond the confines of the region. The leading exporters to China and India in Eastern Africa in 2010 were in DRC and Tanzania at 49% and 25% of their total exports, respectively. India and China also now count for more than 10 percent of the export markets for four other countries in the region - Eritrea, Ethiopia, Madagascar and Rwanda. The principal exports to China have been minerals and raw materials: copper and cobalt (DRC), ores (Tanzania), niobium and tungsten (Burundi and Rwanda) and sesame seeds (Somalia) (Standard Bank, 2012:4). A different example of geographic diversification in export markets can be found in Ethiopia – the country has become one of the ten largest livestock exporters in the world as a consequence of its vibrant trade with the Arabian Peninsula.

Figure 17:

Exports to India and China, as a percentage of total Exports, 2001-2010



Source: UNECA calculations derived from UNCTADstat data

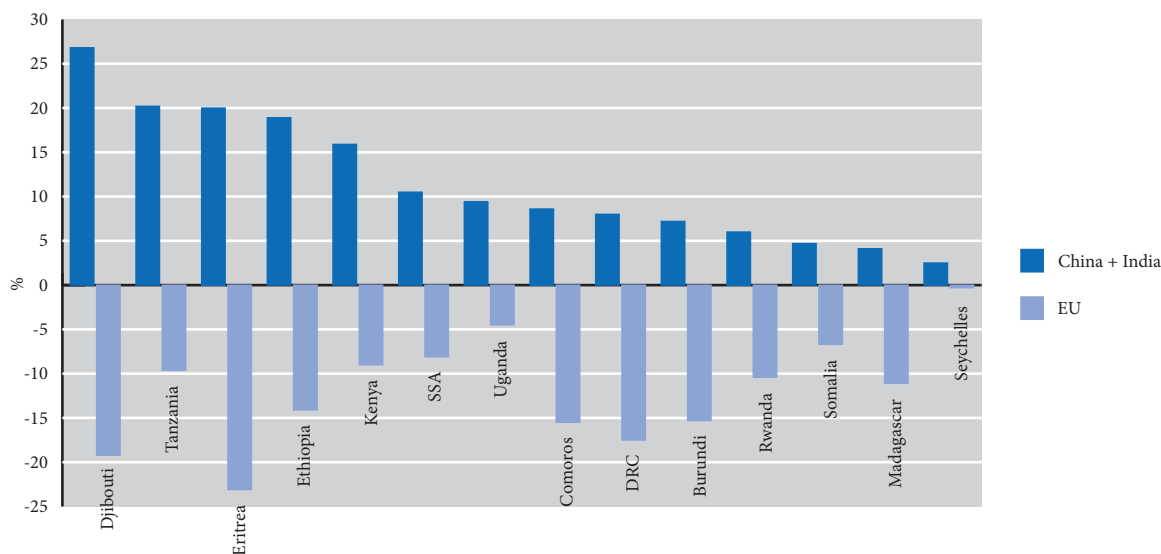
This kind of diversification is particularly important at a time when European trading partners find themselves in a serious predicament regarding the future of the Euro, and that a double-dip recession seems a real possibility – those countries with more diversified export markets are likely to weather the downturn in the western economies better than those with a heavy concentration on traditional trading partners in Europe and North America.

However, even more striking has been the reduction in importance of Europe as a source of imports for the region. Figure 18 shows the shifts in the percentage shares of total imports between 2001-2010 from the EU on the

one hand, and China and India on the other. For the largest regional traders (Kenya, Ethiopia and Tanzania), China and India together account for around 20 percent of total imports. But it is also true for landlocked countries like Uganda, where the Asian continent is now the leading source of Uganda's imports – accounting for 42 percent of total imports (Ugandan Statistical Abstract, 2011: 72). Pointedly, the extent to which increases in import penetration across the region by the two Asian giants is mirrored by the sharp fall of imports from the EU.²⁶ As the East African region negotiates Economic Partnership Agreements with the EU, it is worth taking these new dynamics in regional trade fully into account.

Figure 18:

Change in Percentage share of Total Imports, 2001-2010



Source: UNECA calculations derived from UNCTADstat data

Simultaneously, a number of countries in the region have been implementing measures to push their export structures towards higher valued products. For example, Rwanda has successfully moved up the value chain by exporting branded coffee and has also broken into the US handicraft market. Through the 2002 National Coffee Strategy, they managed to increase income and revenue,

and improve price stability, because specialty coffee prices fluctuate less dramatically than does the price for semi-washed coffee (Boudreaux, 2011).²⁷ Thus in some cases the observed increase in unit values for exports has not just been the consequence of market trends, but have also been part of intentional policy measures.

Box 3: Expanding the region's Comparative Advantage – The role of South Sudan's Oil Production and Natural Resources

Despite its natural beauty and fertile agricultural land, most economists consider the Eastern African region (traditionally conceived as excluding DRC) to be 'resource poor', in the sense that it does not possess large natural endowments of fuel or minerals. Given high population densities and/or fast expanding populations, in some countries in the region the amount of arable land is also quite restricted. Above all, the region is heavily dependent on the import of fuel and oil. Ethiopia produces oil on a very small scale, and although significant oil deposits been found in Uganda these are not expected to come on tap until 2014 at the earliest, according to recent declarations by President Museveni.

However, the idea that Eastern Africa is a 'resource poor' region may be about to change. Firstly, there have been a number of new recent resource finds over the last year, including the announcement in March 2012 of a major oil find in northern Kenya (The Economist, 11/4/2012). Perhaps more significantly still for the region, in July 2011 South Sudan became independent – the first African country to do so since 1993. As a new member to the Eastern Africa region, South Sudan brings with it the enormous potential of its natural resources. In terms of oil imports, as shown by Table 5, the region imports approximately 64 million barrels of crude a year. This has enormous implications on the region's current accounts. For instance, approximately 30% of Kenya's import bill is made up of fuel. Similarly, Ethiopia spends 19 percent of its import bill on fuel. Notwithstanding recent interruptions to production, South Sudan is currently estimated to be able to produce around 300,000 barrels a day, or approximately 100 million barrels a year. That is to say, South Sudan alone could produce much more oil than the whole of the rest of the Eastern African region imports on an annual basis.

Table 5: Oil Imports (1,000s barrels a day), EAR-11 countries, 2005-8

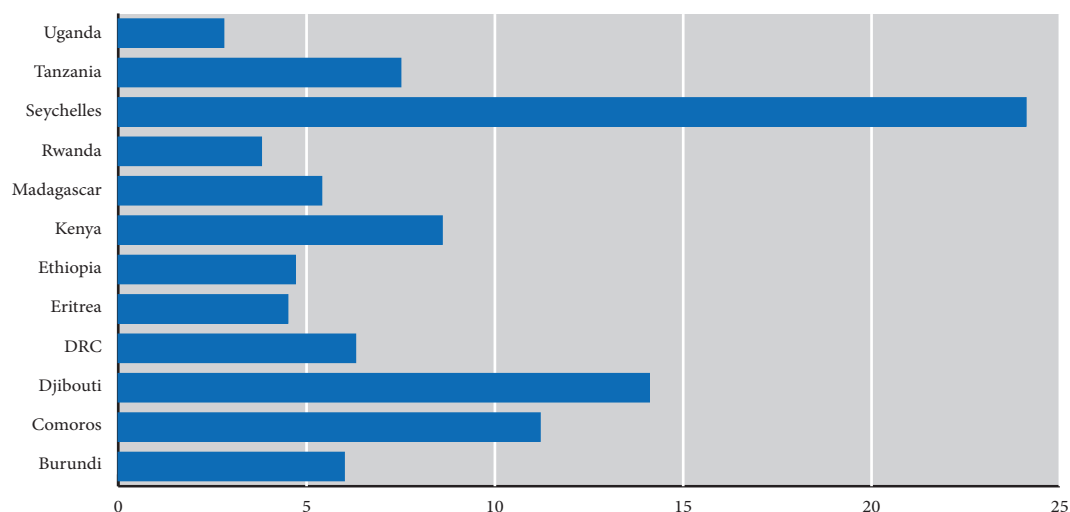
	2005	2006	2007	2008	% of EAR-11 total (average for 2005-8)
Burundi	2.6	2.5	2.4	1.3	1.3
Congo (Kinshasa)	11.7	11.4	13.1	11.5	6.8
Djibouti	11.8	8.5	11.2	8.0	5.6
Eritrea	4.9	4.8	3.9	2.7	2.3
Ethiopia	29.8	33.6	33.5	42.5	19.9
Kenya	36.7	46.4	48.2	35.0	23.7
Madagascar	8.9	16.9	16.4	14.3	8.1
Rwanda	5.6	5.6	5.1	5.1	3.1
Seychelles	5.7	5.9	6.2	6.9	3.5
Tanzania	26.8	28.1	30.0	32.7	16.8
Uganda	11.5	13.1	13.8	23.9	8.9
Total EAR-11 (1,000s barrels)	156.1	176.8	183.8	183.9	175.1
Total EAR-11 per year (millions barrels)	57.0	64.5	67.1	67.1	63.9

Source: EIA, 2011

At present, the lion's share of South Sudanese exports (approximately 70%) is exported to China, which has taken an active lead in the exploration, development, and exploitation of Sudanese fields. However, it would not require a major reorientation of Sudanese oil export markets to start to satisfy regional demand. In addition, because of political instability, South Sudan is currently producing under its full capacity. These facts suggest an important impetus for a regional energy strategy. The story of the contribution of South Sudan to regional resources does not stop at oil of course. The country has an enormous amount of agricultural land and plentiful supplies of water. These are potential fertile lands upon which large-scale commercial farming could be established, again helping to reduce the region's dependence on food imports. In short, the full integration of South-Sudan into the regional economy could bring enormous mutual benefits to the whole region.

Figure 19:

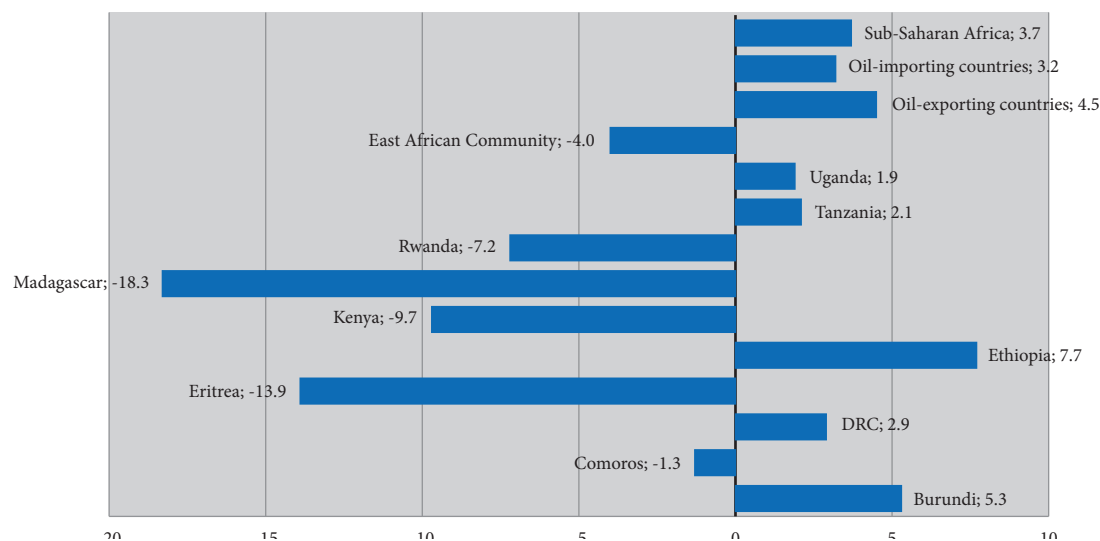
Value of oil imports relative to GDP (%), 2010 or latest year.



Source: UNECA

Despite the generally positive impact of higher commodity prices and weak manufacturing inflation on sub-Saharan Africa's terms of trade, the sub-region's terms of trade (ToT) shifts have been far more mixed over the last year (Error! Reference source not found.), with some countries

such as Madagascar, Eritrea and Kenya, suffering sharp deteriorations in their terms of trade – partly through lower prices for their exports²⁸ but particularly through a higher fuel and food import bill.

Figure 20:**Terms of Trade Shifts – 2010-2011**

Source: UNECA calculations from IMF WEO database

A considerable dispersion in the vulnerability of the region to terms of trade shocks would also appear to exist. Correlations are high between some trading partners in the region (e.g. Tanzania, Kenya and Burundi), but puzzlingly out of synch between Rwandan and its neighbouring countries (Table 6). One possible explanation is that these

ToT correlations are based on annual price data, and these may not be the most appropriate for detecting shifts in the prices of import and export goods which are constantly ongoing. Unfortunately, comprehensive price data for exports and imports are not currently available across the region on a monthly basis to allow such an analysis.

Table 6:**Correlation of TOT shocks 2004-2011**

	Burundi	Comoros	DRC	Eritrea	Ethiopia	Kenya	Madagascar	Rwanda	Tanzania	Uganda
Burundi	1.000									
Comoros	-0.106	1.000								
DRC	-0.658	-0.164	1.000							
Eritrea	-0.129	0.535	-0.329	1.000						
Ethiopia	-0.292	-0.228	0.426	-0.28	1.000					
Kenya	0.665	-0.079	-0.317	-0.365	-0.529	1.000				
Madagascar	-0.631	-0.629	0.584	-0.337	0.089	-0.26	1.000			
Rwanda	-0.222	0.848	-0.306	0.796	-0.169	-0.382	-0.49	1.000		
Tanzania	0.449	-0.241	-0.057	-0.809	0.349	0.482	-0.209	-0.555	1.000	
Uganda	0.144	-0.675	0.337	-0.941	0.477	0.224	0.345	-0.806	0.758	1.000

Source: UNECA calculations based on IMF (2011).

1.6. Current Account Developments

CURRENT ACCOUNT POSITIONS improved in three-quarters of the countries in the region in 2011. The regional current account profile (Figure 23) has varied in 2011 with Seychelles and Burundi having the highest deficits at -21.3%, and -17.2 percent of GDP, while Eritrea, Uganda and Madagascar had the lowest deficits in the region at 0.5%, -3.8% and -5.8%, respectively. Eritrea benefited in 2011 significantly from exporting gold at high prices, something which explains the sharp departure of current account results from historical trends of above -5% to a positive value in 2011. It is likely that these trends will continue in the coming years, thanks to the contribution of the mining sector to significant export earnings.²⁹ The deterioration of the current account in the case of Burundi is due to the deterioration in the trade balance as a result of the combination of lower coffee exports following poor harvests and higher food and oil prices, which significantly raised the import bill. Late disbursement of external aid flows has also contributed to the deterioration in the current account balance (GoB, 2012). Kenya's current-account position also weakened in 2010 and 2011, as the deficit increased from US\$1.6 billion in 2009 (-5.8% of GDP) to US\$2.3 billion in 2010 (-7.0% of GDP) to an estimated US\$ 3.8 billion (-11.4 of GDP) in 2011. This was driven by a sharp rise in the import bill rather than by weak exports, though the recovery of the Kenyan shilling in the last quarter mitigated the impact of the import surge. On the other hand, Ethiopia managed to contain its current account deficit, on the back of a stronger export performance. Both Kenya and Ethiopia (as well as Uganda) are large remittance recipients, a source of income that has held up well during the

2008-9 financial crisis – and an important contribution to help offset imbalances in the current account.³⁰ In the cases of smaller countries in the region like Eritrea and the Seychelles, however, the relative importance of these remittance flows is much more important.³¹ For Eritrea, remittances account for approximately 10 percent of the country's total GDP (EIU, 2011).

The tourism industry is another industry which has a major incidence on the balance of payments of many countries in the region, as well as a number of positive impacts on the broader economy. The industry is, for instance, projected to contribute about 57.6% of the GDP in Seychelles, a tourism-dependent country and over 10% in Ethiopia, Kenya, Madagascar and Tanzania. The industry is projected to generate over 23 million jobs in the region, with the share of national employment being fairly significant, with the exception of DRC (1.6%). It is, nonetheless, important to note that, owing to massive potential for tourism development in DRC, the industry can play an important role in economic development, but this will be subject to the prevailing challenges, including political instability and lack of infrastructure, being addressed. It is also, worth noting that, the industry's share of total exports is further projected to high in most Eastern African countries, with the exclusion of Burundi and DRC, accounting for over 30% of the total exports for countries, such as, Ethiopia, Kenya and Seychelles. What is more, the industry continues to attract investments, with the share of total investments ranging between 0.9% on the lower scale for Burundi and 38.2% for the Seychelles. Table 7 summarises these projections.

Table 7:**Estimated Economic Impacts of Tourism in Africa and Eastern Africa Region (2011)**

	GDP (%)	Employment		Visitor exports %	Investment %
		%	Number in millions		
Africa	9.0	7.0	18.2	8.2	6.4
Burundi	4.6	4.0	0.072	1.2	0.9
Comoros	4.6	4.0	0.008	18.5	2.6
DR Congo	2.0	1.6	0.25	0.4	2.8
Djibouti	-	-	-	-	-
Ethiopia	10.7	9.3	2.2	33.0	9.7
Eritrea	-	-	-	-	-
Kenya	11.4	9.9	0.64	14.3	7.2
Madagascar	14.3	12.1	0.56	23.7	9.7
Rwanda	7.8	6.8	0.13	34.0	7.5
Seychelles	57.6	56.4	0.02	30.9	38.2
Somalia	-	-	-	-	-
Tanzania	12.9	11.2	1.12	22.6	9.6
Uganda	7.6	6.6	0.44	14.6	4.6

Source: WTTC 2011

The region's principal sources of foreign exchange are not necessarily the ones which are usually anticipated. Thus, while Ethiopia still has a fairly heavy dependence on its traditional exports of coffee³², the country's second largest revenue source from a cash crop is the leafy narcotic called qat, which is extremely popular in export markets of Djibouti, Somalia and Yemen. Revenues in 2010-11 from qat exports were up 14% to 238.4 million US\$. Beyond this, however, the largest single source of foreign exchange for Ethiopia is on the services account - Ethiopian Airlines, reported revenues of US\$1.26 billion in the year to June 2010, for instance. A similar story can be told about Rwanda. Coffee continues to be the major cash crop. However, the income from tourism is now higher than that from its traditional exports. Kenya's major source of foreign exchange is its horticultural sector.

Kenyan National Bureau of Statistics (KNBS) figures for the first nine months of 2011 to September, the sector earned \$893 million in export revenues, a 50 percent growth over the figures for the same period for 2010. Earnings are expecting to be in excess of US\$1.1 billion for the whole of 2011.³³

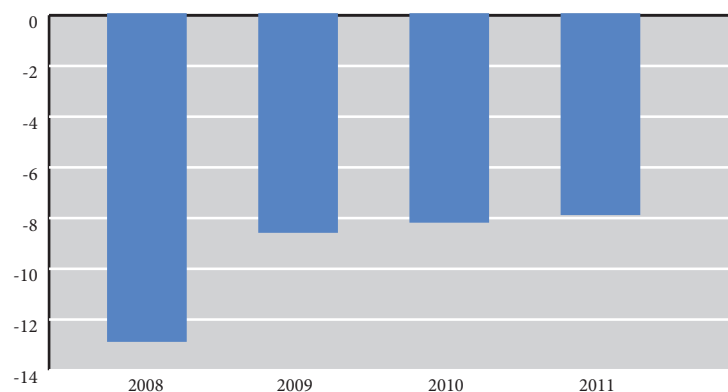
On a regional basis, the median current account balance (Figure 21) improved slight in 2011, continuing a trend that began in 2008. In line with these trends, the foreign exchange reserve position remained broadly unchanged in the region for the 9 countries where data for 2011 is available, though there was a sharp rise in reserves in Eritrea, Kenya and Rwanda, where reserves climbed by 57, 23 and 18 percent, respectively. The Eritrean case is explainable by the high global price of gold, which brought

windfall gains from the newly exploited gold deposits. In terms of months of imports, however, the level of foreign reserves did decline for some countries in the region—this was the case of Uganda, Madagascar and Ethiopia which experienced declines of 16, 14 and 10 percent, respectively, mainly due to rising import prices and, in the Ugandan

case, a strong depreciation of the shilling. Nonetheless, in only three countries in the region (Ethiopia, Seychelles and Eritrea) are foreign exchange reserves below the ‘three month’ import rule which is considered prudent to guard against possible current account shocks.

Figure 21:

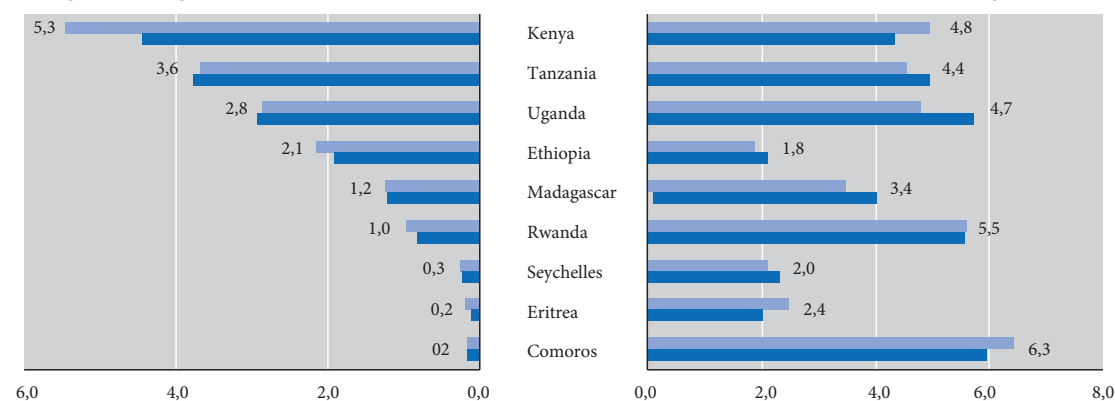
Median Regional Current Balance % of GDP



Source: World Economic Outlook, IMF, Authors calculations.

Figure 22:

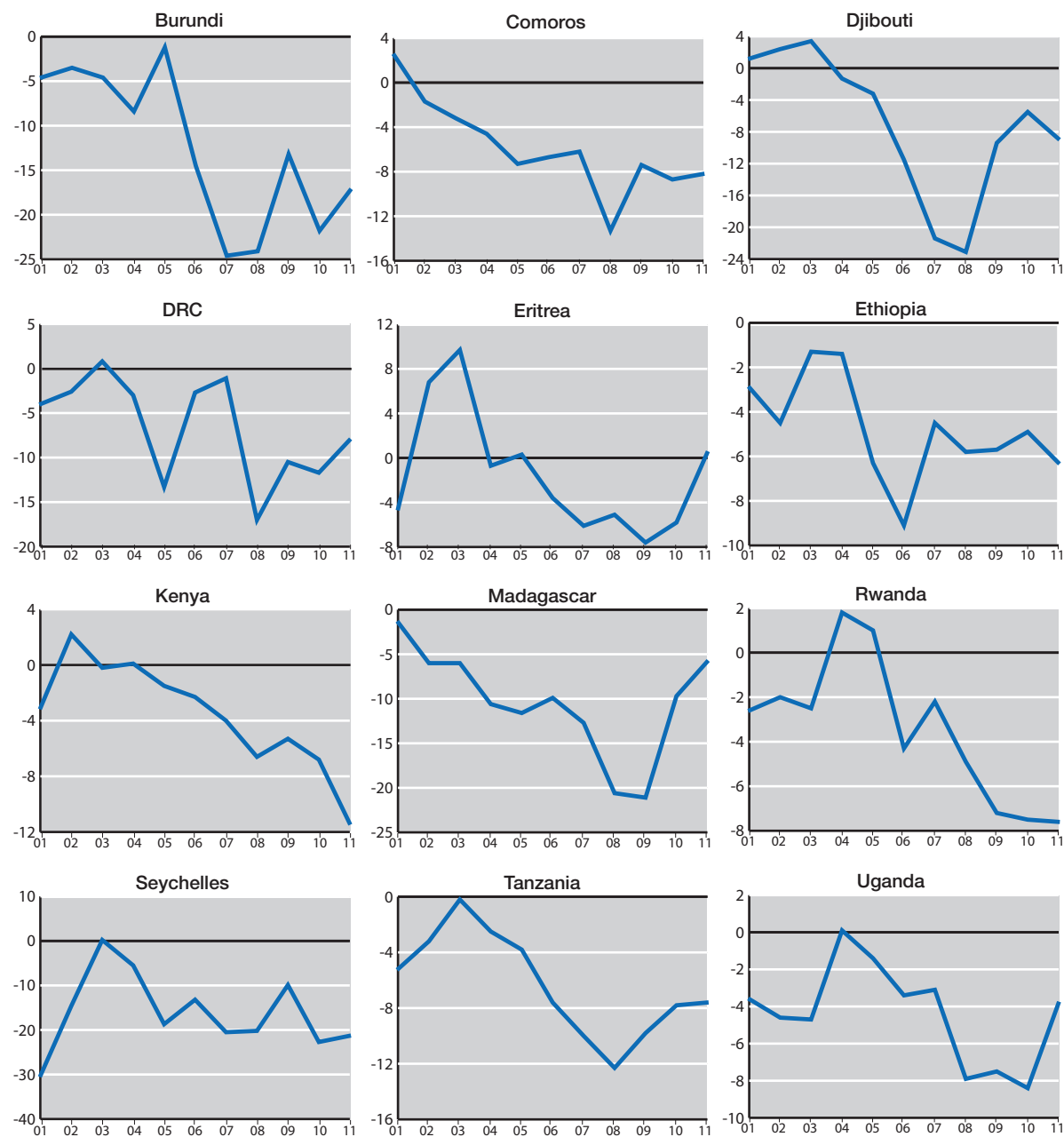
Foreign Exchange Reserves in terms of billion US\$ (left-hand side) and months of imports (right-hand side)



Source: EIU, IMF

Figure 23:

Current Account Balances as a Share of GDP, EAR-12, 2001-2011*



Source: 2011* figures are estimates. World Economic Outlook database prior to 2008, AfDB/UNECA/UNDP/OECD (2011/12) otherwise.

1.7. The End of a Period of Expansionary Fiscal Policy?

AS A COUNTERCYCLICAL measure against the global economic downturn, since 2008 many Eastern African governments have expanded their budgets in an attempt to stimulate growth and cushion against high inflation rates. But as a result, government deficits have widened in 2011 in around half the countries of the region, albeit very moderately in most cases (Figure 24). However, to put things in perspective, for most countries in the region the fiscal imbalance was still lower than the median deficit (8%) for low income countries (IMF, 2011). Strong economic growth has meant that generally speaking revenue collection has also been good. Whether the region is about to enter into a period of fiscal consolidation is the moot point – certainly, governments in the region are aware of

the importance of increasing revenue collection in order to better balance expenditures, but generally speaking the tax base is narrow and the scope for aggressive revenue collection is rather limited. Moreover, across the EAC region, as trade shifts increasingly to the EAC partners, losses in the collection of international trade taxes are expected to be permanent. Thus revenue collecting authorities have a significant challenge in terms of improving collection from existing tax structures, and searching for new sources of revenue. The most extreme example is South Sudan, where it is thought that oil revenues will provide all but 2 percent of the new country's \$2.3 billion budget (Shankleman, 2011).

Figure 24:
Change in Fiscal Balance



Source: IMF, authors calculations. Note: countries above the diagonal line experienced a deterioration in 2011 of their fiscal balance vis-à-vis the average for the period 2008-2010, those below the line an improvement.

In Tanzania new legislation introduced in 2011 removed the tax holiday for mining companies still recuperating their investment outlays, and the government also plans to raise royalty payments on gold exports from 3 to 4 percent (Africa Report, 2011). Improvements in tax

collection have succeeded in moderating the deficit for Comoros (EIU, 2011). In Rwanda, for the fiscal year that ended in June 2011, revenues performed strongly, growing by 23.7%, boosted by increased volumes and value of imports, payments of dividends to shareholders by some

companies, as well as an increase in Pay as You Earn registration. During the current 2011-12 fiscal year, the one-off revenue from the sale of government assets (including a telecommunications license) is intended to compensate for the permanent revenue losses from lower fuel taxes – a measure implemented to mitigate the impact of high international oil prices. Also important in explaining the increase in revenues were efforts to extend VAT invoicing operations all over the country. Despite being a new body, the Burundi Revenue Authority has also reached an ambitious target for the growth of revenue, recording a 24 percent increase in revenues in June 2011. Within the EAC region, only Kenya Revenue Authority recorded a lower-than-expected income from taxation, registering US\$ 6.3 billion vis-à-vis a target of US\$6.5 billion. This was ascribed to lower than anticipated income from excise duty, VAT and PAYE.³⁴

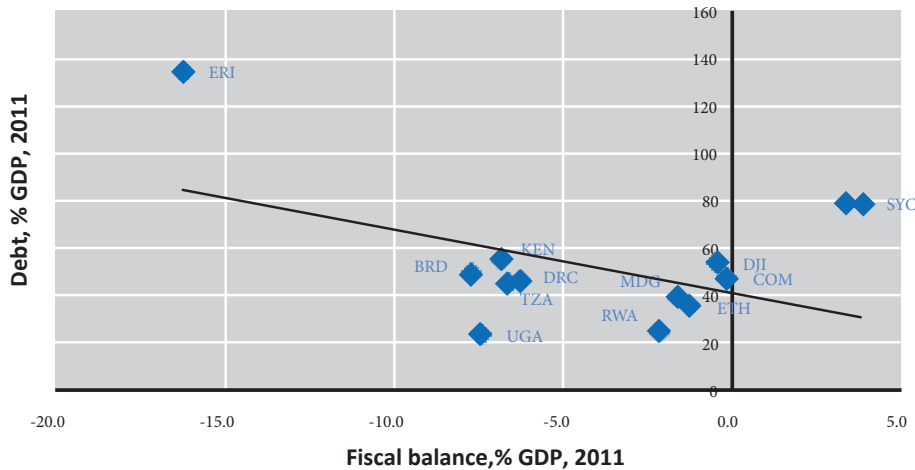
On the spending side, in Ethiopia government outlays increased in the 2011-12 fiscal year, driven by increased public sector investment and public sector pay rises. Although revenue growth is expected as the Ethiopian Revenues and Customs Authority continues to implement measures to broaden the tax base and reduce evasion, the IMF (2011) estimates that the drought in the horn of Africa will have a negative impact on GDP (an initial impact estimated at less than 0.5% of output) and therefore a negative impact on revenue growth. The Kenyan government announced a KSh 1.16 trillion (US\$13.4 billion) budget for the 2011-2012 fiscal year, a 16% increase in spending. The budget deficit excluding grants is projected to grow to -8.8% of GDP in 2011-2012 (7.4% including grants). Government spending will be driven by energy and transport infrastructure (19.1 percent of the total budget, equivalent to a 35% increase), and “human resource development” (18.5 percent of the

total budget). Revenue collection will be constrained by the proposed tax and duty reductions intended to help consumers to cope with high inflation rates and the effects of the drought. Tanzania has also announced increased spending and revenue collection by 16.4% and 9.7% for 2011-12 fiscal year, with the biggest budget items being infrastructure (21%) and education (17%).

According to the IMF (2011), “rebuilding fiscal policy buffers is a particularly urgent goal, as exposure to less concessional financing increases, there is a need to strengthen debt management processes to safeguard hard-won debt and fiscal sustainability.” The fiscal balances (for 2011-2012 period) for Burundi, Eritrea, DRC, Kenya, Tanzania and Uganda are not currently consistent with stabilizing the debt-to-GDP ratios. However, generally speaking debt levels remain moderate (Figure 25) and debt servicing ratios within manageable limits. The trend in East Africa has been to reduce gross government debt as a percentage of GDP. For instance, between 2002 and 2010 Burundi reduced its government debt from over 200 per cent to 50 per cent of GDP, the most dramatic reduction in the region. Rwanda also slashed its debt from 108 per cent to a frugal 23 per cent, the lowest in East Africa in 2010. Uganda, Tanzania and Kenya had debt levels of 24 per cent, 40 per cent and 52 per cent of GDP in 2010. By way of comparison, in 2010 the G7 economy with the lowest gross government debt-to-GDP ratio was Britain with 75 per cent, and the highest was Japan with 220 per cent (SID, 2012:74). One example of the generally positive light in which regional finances are viewed is Standard & Poors recent sovereign credit rating of ‘B’ for Rwanda.

Figure 25:

Average Debt VS Average Fiscal Balance



Source: IMF, Economist Intelligence Unit, National Sources

1.8. Overseas Development Aid – Current Receipts and Prospects for 2012

THE EASTERN AFRICAN region, as a whole, still depends quite heavily on ODA, in terms of both financing government budgets and for covering the current account deficit.³⁵ Prior to the global economic crisis of 2008-9, the major debate within donor circles had been centered on the scaling up of aid, especially for Africa, in line with the commitments undertaken at the Gleneagles G8 Summit in July 2005. Surprisingly, given the international financial context, in 2010 net official development assistance (ODA) flows from members of the Development Assistance Committee (DAC) of the OECD reached USD 128.7 billion, representing an increase of +6.5 % over 2009. This was the highest real ODA level ever, surpassing even the volume provided in 2005 which was boosted by exceptional debt relief. Bilateral ODA to Africa was USD 29.3 billion, of which USD 26.5 billion was for sub-Saharan Africa. These amounts represented an increase in real terms of +3.6% and +6.4%, respectively over 2009.³⁶ Excluding debt relief grants, bilateral ODA rose (+1.7%) for sub-Saharan Africa, still somewhat short of the target promised at Gleneagles

in 2005 concerning the doubling of resources in real terms to SSA, but encouraging nevertheless.³⁷

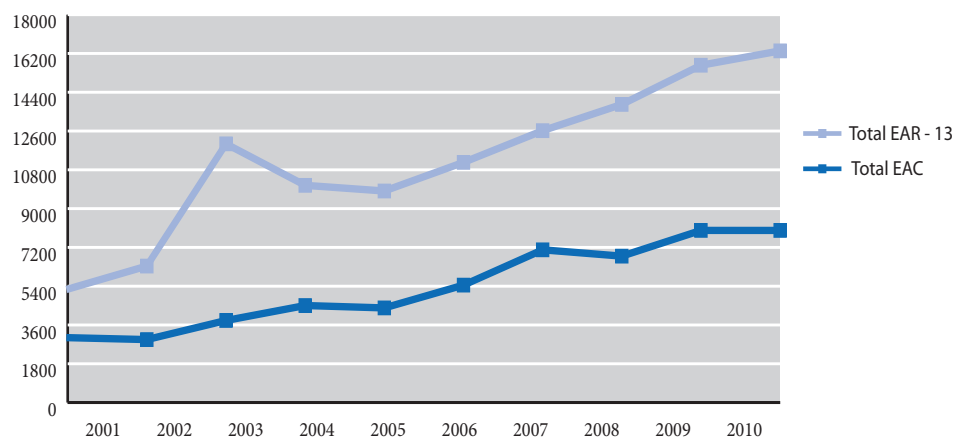
However, going forward, the prospects for ODA over the next five years surely does not give grounds for much optimism. Roodman (2008) has argued that in the aftermath of the financial crisis, even existing aid budgets may be at risk. He points to some particular historical examples (Finland, Japan, Norway, and Sweden) of sharp falls in aid during previous financial crises. For instance, as its economy began to fall into a protracted period of stagnation, Japan's aid fell 44 percent between 1990 and 1996. In Finland, according to Roodman's figures, the fall was even more dramatic; during its banking crisis, between 1991 and 1993, when GDP dropped by nearly 11 percent, development aid fell by 60 percent. It was certainly not encouraging that countries such as Austria, Ireland, Italy and Spain announced significant cutbacks in their bilateral aid programs for 2010 and 2011.

As discussed in the introduction, the Eastern Africa region is particularly vulnerable to aid cutbacks. Based on OECD statistics of the 24-members of the Development Assistance Committee on multilateral and bilateral flows, in the 2000s ODA receipts to the EAR-13 boomed,

from approximately US\$5.3 billion in 2001 to nearly US\$ 16.3 billion in 2010 (Figure 26). And these figures do not count the substantial amounts of ODA that the region is receiving from non-traditional donors.³⁸

Figure 26:

A Veritable Boom of ODA, but is it Coming to an End?: Total ODA Receipts, 2001-10 EAR-13 and EAC-5 (current prices millions US\$)



Source: OECD (2011) database

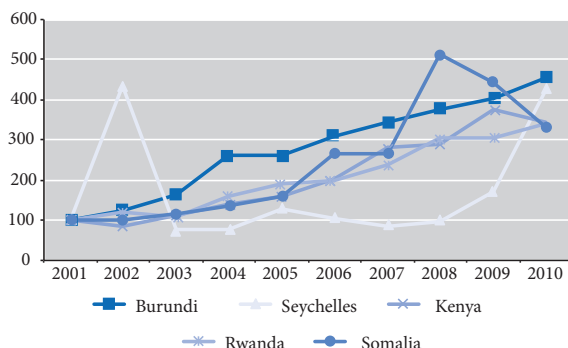
As revealed in Figure 28, beyond the DRC (which has benefited from large inflows and debt-relief since the beginning of the 2000s) some of the smaller countries have been among the major gainers over the last decade in terms of their ability to attract greater flows of ODA – Burundi, Somalia, and (ironically, perhaps as the country with the highest GDP per capita) Seychelles.³⁹ After the end of the Moi administration in Kenya, donors increased support for Kenya, with ODA increasing by 4 times between 2001-10 (Figure 27). Nonetheless, in absolute terms, the pattern of receipts of ODA is dominated by just three countries

in the region – Ethiopia, DRC and Tanzania (Figure 28). These three countries account for more than half of all aid to the EAR-13.⁴⁰ As revealed in a recent report (ActionAid, 2011), a number of countries in the region have in fact been quite successful in terms of reducing their aid dependence on aid over recent years – among them, Rwanda, where donor contributions are responsible now for funding about 43 percent of the government's budget (2010-11), down from around 86 percent in the year 2000.

Aid Dependence in the region

Figure 27:

Increases in ODA, 2001-2010 (2001=100)



Source: OECD (2011), based on current prices and disbursements

The impact of ODA on long-term growth and development is partly dependent on its sectoral composition. Figure 29 shows the sectoral composition of aid in the region, according to commitments. The pattern is an interesting one, in the sense that it reveals a) the relatively small share

Figure 28:

The big three recipients, 2005-2010

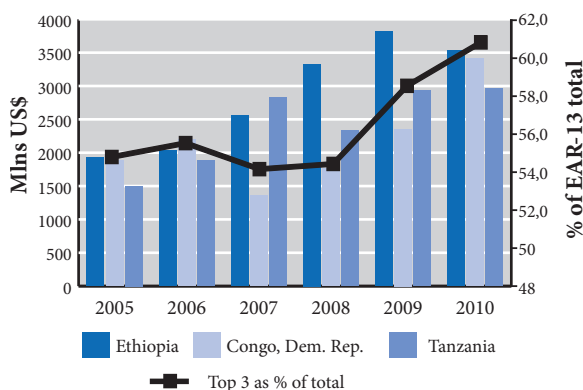
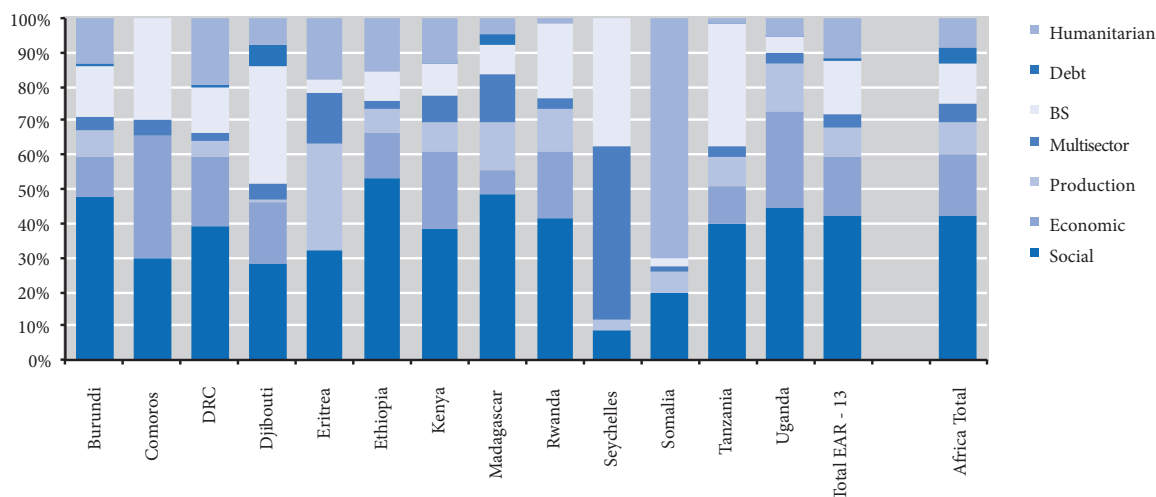


Figure 29:

ODA to EAR-13 by Sector in 2009 (% shares of total), based on Commitments in mlns US\$



Source: OECD (2011), based on constant price and exchange rate ODA data.

of economic and productive sectors in overall ODA; b) the dominance of social sectors in DAC aid delivery; c) the importance of budget support for certain countries in the region, particularly Rwanda and Tanzania⁴¹; and d) the importance of humanitarian aid to Somalia.

The figures above apply to traditional donors – the ‘DAC grouping’. The figures do not take into account the increasingly fundamental role of emerging donors in the region, particularly China and India. Each new donor has a different comparative advantage. Thus India has a lot of expertise in technical training and education. India’s support to eastern Africa includes lines of credit, which until recently were very modest (about \$5 million) and some 50 technical training centres (UNECA-SRO-EA,

2011). China has a reputation as a formidable provider of infrastructure and construction, although it is increasingly moving into manufacturing within the region (see the following section). In DRC, Brazil is facilitating its knowledge in agricultural production. Because of much of the economic focus of much of the cooperation from emerging partners, we deal with this in the final section of this report, where we discuss recent trends in foreign investments, including Foreign Direct Investment (FDI).

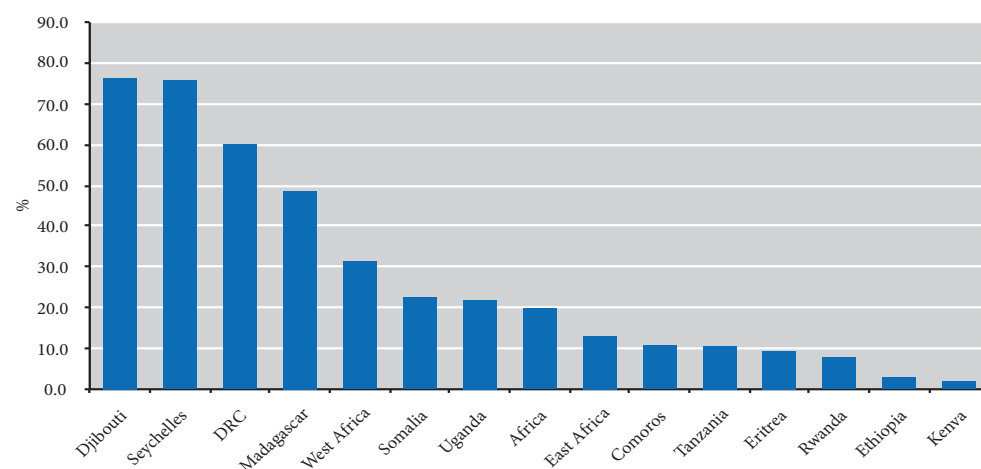
1.9. FDI Boom – Reaping the Benefits of Regional Integration?

TRADITIONALLY, THE EASTERN African region has been far more dependent on ODA as a form of external finance. In recent years, that has begun to change, as the region has increasingly been able to attract large amounts of Foreign Direct Investment. Of course, dependence on FDI as a form of development finance varies across the region. Although the absolute amounts may be low, as a share of total gross fixed capital formation, FDI is especially important in countries such as Djibouti and the Seychelles (Figure 30). It is also a major contributor to

Gross Fixed Capital Formation in larger countries in the region such as DRC and Madagascar. It is interesting to highlight the fact that FDI is also important in terms of its contribution to gross fixed capital formation (GFCF) in Somalia (reflecting investments in Somaliland and Puntland), though it should be noted that this is more the product of an extremely low level of GFCF rather than a high level of FDI. For Eastern Africa on average, FDI is equivalent to approximately 13 percent of total GFCF.

Figure 30:

FDI as a Share of Gross Fixed Capital Formation, Average 2008-2010



Source: UNCTAD, FDI/TNC database (www.unctad.org/fdistatistics).

In the Eastern Africa region (excluding DRC according to the UNCTAD definition) inflows of FDI increased for the EAR-13 in 2010 reaching \$6.3 billion, nearly double for the average of the 2005-9 period (Table 8). This has to be put in the context of a period of sustained increase in the levels of FDI received by the region, particularly towards the EAC (Figure 31). It may be argued that the increases in FDI are driven by new resource finds in the region. In 2010, both Uganda and the DRC received significant oil-related investments. In Tanzania, a major

project was announced to build a 532-km pipeline to exploit natural gas from Songo Songo Island to Dar es Salaam to be built by the China Petroleum and Technology Development Corporation, in conjunction with the Tanzanian Petroleum Development Corporation. It is reported that construction will be fast-tracked, with a provisional completion date of December 2012, and 90% of the project cost will be financed by a US\$1bn loan from the Export-Import Bank of China (Exim Bank) (EIU, 2011).

Table 8:

FDI Inflows to Eastern Africa, 2005-2010 (Millions US\$)

Economy	2005	2006	2007	2008	2009	Av. 2005-9	2010
Burundi	0.6	0.0	0.5	13.6	9.9	4.9	14.1
Comoros	0.6	0.6	7.5	7.5	9.1	5.1	9.4
Dem. Rep. of the Congo	0.0	256.1	1808.0	1726.8	663.8	890.9	2939.3
Djibouti	22.2	108.3	195.4	228.9	99.6	130.9	26.8
Eritrea	-1.0	0.5	-0.1	-0.2	0.0	-0.2	55.6
Ethiopia	265.1	545.3	222.0	108.5	221.5	272.5	184.0
Kenya	21.2	50.7	729.1	95.6	140.5	207.4	133.0
Madagascar	86.0	294.5	773.3	1169.4	1066.1	677.8	860.4
Rwanda	14.3	30.6	82.3	103.4	118.7	69.8	42.3
Seychelles	85.9	145.6	238.6	179.3	274.9	184.8	369.0
Somalia	24.0	96.0	141.0	87.0	108.0	91.2	112.0
Uganda	379.8	644.3		728.9	815.9	642.2	847.6
Tanzania	494.1	597.0	647.0	679.3	645.0	612.5	700.0
Total EAR - 13	1392.7	2769.3	4844.5	5127.9	4172.9	3789.9	6293.5

Source: UNECA calculations on the basis of UNCTAD (2011).

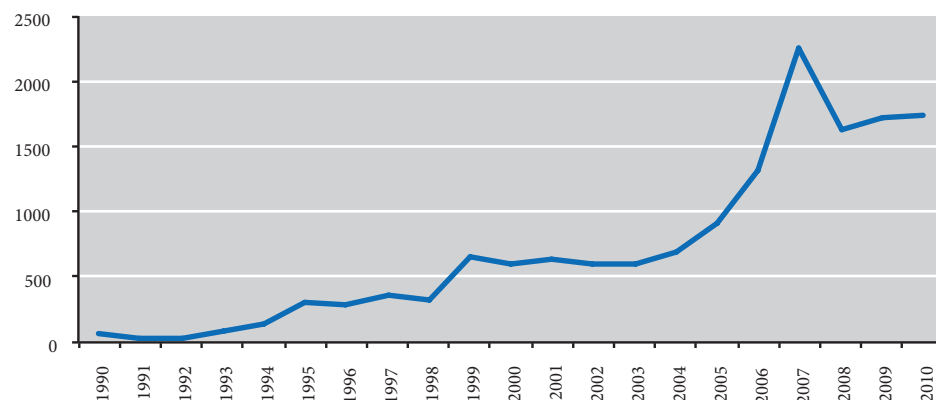
Note: figures in red reflect FDI inflows in 2010 which were higher than the average for the 2005-09 period

Nonetheless, the story is far from one of simply an upsurge of FDI in response to a resource boom. For instance, DRC also received significant investments in telecommunications. One of the major ‘game-changers’ has been increased investments by China in the region. But whereas in other regions, FDI investments by China have been principally linked with the natural resource sector, in Eastern Africa the sectoral distribution is rather more diversified. By September 2011, China’s investments in the EAC reached \$750 million, focused on sectors such as textiles, shoes, pharmaceuticals, industrial machinery, electronics and ICT. China hopes to raise its business interests in the region to \$1.500 billion by 2013.⁴² Similarly, according to the Ethiopian Investment Agency (2010), 83% of the Chinese FDI to Ethiopia between 2003 and 2009 has been in the manufacturing sector, attracted by a combination of low cost labour, large-scale land leases, as well as Ethiopia’s large market size. Finally,

the Chinese company Chery Automobiles has invested about USD50 million in their plant in Nairobi to serve the Eastern African market. In a similar vein, India’s largest automobile company TATA is eyeing investment opportunities in Kenya, with plans to set up an assembly plant worth USD 20 million in Nairobi (Brandkenya, 2011).⁴³ It seems, in other words, that foreign companies are starting to target the wider Eastern African market, rather than target individual countries – one of the true payoffs from regional integration.⁴⁴ Inflows of FDI into Seychelles jumped strongly in 2010, by 34% to US\$369m, a record high, underpinned by tourism projects. The increase contrasts with a 9% overall decline in FDI inflows into Sub-Saharan Africa (from 41.9 to US\$38.1bn), owing partly to uncertainty in the aftermath of the global recession. Madagascar reported a 19% decline compared to 2009, but is still the second highest recipient of FDI in the region after DRC.

Figure 31:

FDI to the East African Community, 1990–2010 (Millions US\$)



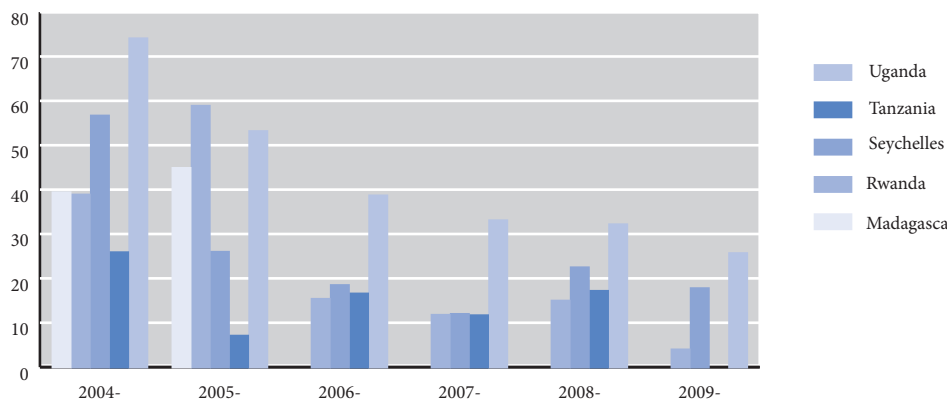
Source: UNCTAD (2011)

On a more negative note, available (but patchy) data on profit repatriation suggests that at times the financing cost of FDI in the region has been quite high. Profit repatriation in some countries, such as Uganda, the Seychelles or even a newer destination such as Rwanda, has been

running at high levels – in some years over 50% of the value of new inflows (Figure 32). That said, the trend overtime appears to have been downwards, suggesting a higher rate of reinvestment in earnings as prospects for the regional economy has improved.

Figure 32:

Profit Repatriation as a % Share of Total FDI Inflows



Source: World Development Indicators, 2011

Although there have been a number of important Mergers and Acquisitions (M&As) of existing firms in the region, as a way of quick access to new markets, what policymakers truly search for is greenfield investment – that is, the construction of new plants and businesses, rather than changes in ownership of existing businesses (even if this does bring in its wake efficiency improvements). As shown

in Table 9, the data is again encouraging regarding the capacity of the region to attract greenfield investment. Although there was a dip in the number of projects post the 2008/9 financial crisis, the number of greenfield investments subsequently recovered to 106 in the region in 2010, and UNECA estimates for 2011 are that there will be a record 128 projects announced for the whole

Table 9:

Greenfield FDI Projects in the Eastern Africa Region

	2003	2004	2005	2006	2007	2008	2009	2010	2011*
DRC	3	2	10	8	5	15	5	8	21
Djibouti	-	-	1	2	1	3	2	3	-
Eritrea	1	1	4	1	-	-	-	-	-
Ethiopia	2	1	1	3	10	10	8	8	20
Kenya	13	15	13	12	8	19	29	35	49
Madagascar	4	3	4	3	3	4	3	-	-
Rwanda	-	-	2	-	8	13	26	6	9
Seychelles	-	3	3	-	3	2	1	1	-
Somalia	-	1	-	1	-	2	-	1	-
Uganda	5	5	6	15	7	41	16	21	8
Tanzania	7	6	11	7	6	17	11	23	21
Total	35	37	55	52	51	126	101	106	128

Source: UNCTAD, based on information from the Financial Times Ltd, fDI Markets (www.fDimarkets.com). * Figures for 2011 are UNECA estimates

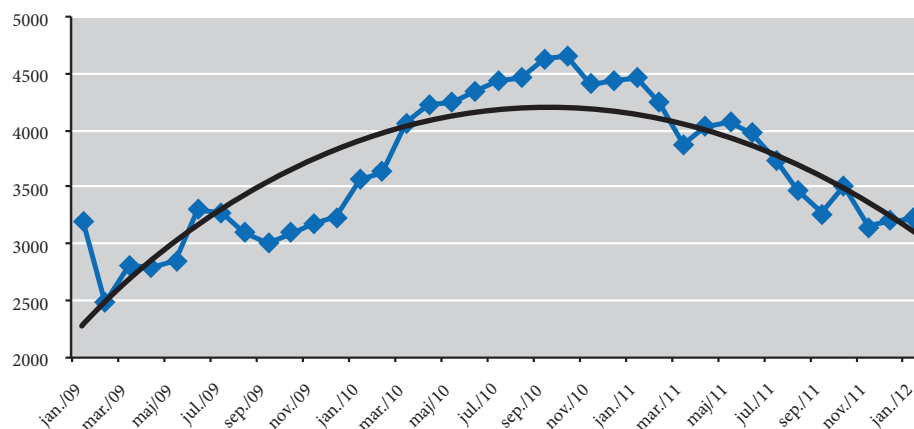
year – an almost three fold increase over the period of the last 8-9 years.

Some countries in the region are trying to court FDI much more energetically than in the past. Improvements in political stability in Comoros are making it much easier to attract FDI. The government has established an investment promotion agency and generous fiscal incentives are being offered under an investment code introduced in 2007, including a ten-year exemption from corporate tax on investments worth over Cfr100m (US\$290,000) (EIU, 2011). The government is particularly targeting FDI in tourism, infrastructure, agriculture and fishing.

Perhaps the big story in the region, however, in terms of potential ability to attract FDI, is South Sudan. In 2009, SABMiller became the first multinational to venture into South Sudan, with a US\$37 million investment in South

Sudan Beverages Limited in Juba. But the really large scale investments are in land and oil. So far, for instance, the American company has leased 600,000ha to ‘develop, produce, and exploit timber and forestry resources on the leased land.’ (African Business, October, 2011:22). Beyond SABMiller, other South African firms have also began to establish a firm foothold in the country – in July 2009, the South African Department of Trade and Industry (DTI) organized a meeting in Juba involving 20 companies covering telecommunications, agriculture, forestry, water purification, timber, financial services, infrastructure development, energy and minerals. The key challenge for South Sudanese authorities is managing the inflows in a way which underpins their own national development priorities. With this objective, South Sudan is currently setting up of a national investment promotion agency, along the lines also being attempted in Comoros.

Figure 33:
Nairobi Stock Exchange, January 2009-January 2012



Source: NSE

Finally, regarding portfolio investment in the region, this has traditionally been very limited. The region's leading stock exchange, the Nairobi Stock Exchange (NSE) performed quite poorly in 2011 (Figure 33), after a stellar performance in 2010 when stocks surged on the back

of genuine enthusiasm in the prospects for the region's largest firms, as well as the NSE's status as an emerging market, in which foreign investors took refuge during the turbulence and uncertainty in their traditional markets. The turn-around in performance in 2011 was not due

to any reduction in this global uncertainty, but rather explainable by a combination of certain political uncertainties in Kenya combined with profit-taking behavior after the surge in prices in 2011. In the future, there will be more discussion about combining national markets into one large regional stock exchange – certainly, a way of increasing the attractiveness of investing in the region, and encouraging larger, more regionally based, operations

by international and national firms. The EAC is currently spearheading a set of discussions around this issue. One encouraging sign is the growing number of Rwandan, Tanzanian and Ugandan investors who trade on the Nairobi Stock Exchange, attracted in part by a growing number of cross-listed shares by regional companies such as Centrum, Kenyan Airways, and Jubilee Insurance.

Notes

3 For example, in terms of product diversification, in 2009 in Kenya, Uganda and Tanzania, the top three export products accounted for less than 40 percent of total exports. These shares are well below those observed in resource rich countries of West or Southern Africa, where the main exports typically account for 80-90 percent of total exports (African Competitiveness Report, 2011:16).

4 To give one example, although the country escaped the drought of the Horn of Africa, in the first half of 2011 Rwandan growth performance softened significantly, as a result of irregular rains. However, in the second half of the year, weather conditions were much more favorable, leading to a growth rate in excess of 10 percent, a very robust performance given the global economic context.

5 See 'Kenya seeking \$1 billion to build dams for water storage', *The Eastern African*, December 12-18.

6 See *African Business*, October 2011 for some discussion of this.

7 This figure does not include the GDP for Somalia (data for which is unavailable). It should be noted that the relative rankings here of countries according to the size of their GDP is contingent on a number of factors, such as the GDP deflator used, the exchange rate applied, as well as the accuracy of the growth forecast. It should also be noted that official figures are revised as more robust information about the different components becomes available.

8 The corresponding GDP for the Eastern African Community in 2011 is US\$ 82.5 billion

9 The high GDP per capita for South Sudan is explainable by the importance of oil exports – if instead of GDP per capita the GNI per capita is used (which is arguably a more accurate reflection of real incomes), the figure for 2010 is US\$984 – still high by regional standards, but considerably lower than the GDP per capita figures (South Sudan NBS, 2011).

10 Burundi Mining Metallurgy hopes to start nickel production in two years in the world-class Musongati deposit, which has estimated reserves of 250 mln tonnes. There are also reportedly hopes on oil production, with ongoing exploration on Lake Tanganyika (*The Africa Report*, No. 36, December – January 2012, page 138).

11 Established in 2007, the Ibrahim Index is the most comprehensive collection of quantitative data that provides an annual assessment of governance performance in every African country. It is funded and led by an African institution and uses indicators from 23 data providers, made up of over 40,000 raw data points. For details, <http://www.moibrahimfoundation.org/en/section/the-ibrahim-index>.

12 See *The Eastern African*, 1/1/2012, 'Burundi is Too Business Friendly' <http://www.theeastafican.co.ke/business/Burundi+is+too+business+friendly+/-/2560/1298414/-/g0poakz/-/index.html>

13 <http://ssnbs.org/home/2011/10/7/october-2011-consumer-price-index-press-release.html>

14 For some discussion of these issues, see OECD (2011).

15 <http://www.trademarksa.org/news/rising-wages-cast-dark-shadow-over-performance-regional-economies>

16 There is also some controversy regarding the threshold effects for the negative impact of inflation. High inflation rates are a cause for concern for policy makers because of the negative effect on growth. It can also have major distributional consequences – commonly, it is thought to impact most negatively on people unable, through collective action, to secure increases in their incomes in line with inflationary expectations. However, some economists consider that moderate levels of inflation are not so damaging as is often believed – and that those levels can reach as much as 15-20% before a negative impact is observable on economic performance. Supportive of such views, through a series of statistical tests Bruno and Easterly (2005) examined the effect of inflation on growth, and found that only an inflation rate above 40% had a robust negative effect on growth. This is a much higher threshold effect than previously had been thought.

17 'Kenya Seeking \$1 billion to build dams for water storage', *The East African*, December 12-18 2011, page 5.

18 See, for instance, Durevall and Ndungu'u (1999) on Kenya, Nachega (2001) on Uganda, and Laryea and Sumaila (2001) on Tanzania.

19 KES- Kenya Shilling, BIF- Burundi franc, RWF- Rwanda Franc, TSHS- Tanzania Shilling, USHS- Uganda Shilling

20 Of the members of the EAC-13, only four countries are not currently WTO members – Comoros, Ethiopia, Seychelles and Somalia.

21 See Morrissey and Jones (2008) for a discussion of trade liberalization within the EAC countries.

22 It is interesting to reflect on the role of cross-border ‘informal’ trade in the region – countries are generally encouraged to include informal trade estimates in their national statistics. However, not many countries do so in a systematic way. Uganda provides figures on informal trade that were estimated to be the equivalent to approximately 30 percent of exports in 2010 (see Ugandan Statistical Abstract, 2011).

23 Tanzania earned record receipts of \$2.1 billion in 2011 from gold, a 33% increase on 2010. (See *The Economist*, April 7th 2012, <http://www.economist.com/node/21552265>).

24 Textiles accounted for as much as 60% of Madagascar’s total exports in 2008-2009 and the country had been one of the biggest beneficiaries of the AGOA trade agreement (Cling et. al, 2005). The suspension of AGOA is estimated to have cost 50,000 textile jobs in the Export Processing Zone (EPZ).

25 See ‘China, EAC in new \$500m trade, investment deal’, *The Eastern African*, November 28-December 4th, page 12.

26 It needs stressing of course that Europe is a regional block comprising of many different national markets – significantly for the region, the UK, France and Germany.

27 Inspired by the examples of Ethiopia and Kenya, who now have strong horticultural export sectors, the Rwandan governments has recently announced the investment of at least \$75 million beginning in 2012 to bolster its own horticultural sector. See *The Eastern Africa*, 5-11/12/2011, Rwanda to invest \$75m in horticultural exports.

28 Approximately 30% of Kenya’s exports are now in manufacturing – and manufacturing exporters have had to confront decreasing TOT in recent years – See Kaplinsky (2008) for a discussion of this.

29 Eritrea features the largest number of mining operators in the region largely due to its generous concessions, which includes a 10% rent payment, with a 30% chance for the government to buy into mining company stakes.

30 There are some discrepancies on the precise figures however. The remittance inflows data reported by country authorities themselves are often higher than the IMF figures, for instance. To cite one example, in 2010 Ethiopia’s Central Bank reported more than \$700 million—about twice the \$353 million reported by the IMF. These discrepancies are in part related to the misreporting of migrant remittances with other types of current transfers, such as transfers to nongovernmental organizations and embassies and payments related to small-value-trade transactions (Ratha et. al., 2011).

31 It is estimated by Ratha et. al. (2011) that between 15-18% of their populations live abroad.

32 In the financial year 2010-11 the value of coffee exports rose 38% to US\$841.7 million. This was equivalent to exports of 196,188 tons of coffee.

33 ‘Weak shilling, increased production boot Kenya’s horticultural sector’, *The East African*, 2-8 January 2012. Page 45.

34 See ‘EAC records impressive revenue growth’, *The New Times*, 17 December 2011.

35 Part of ODA is counted as a transfer, and so enters in a positive contribution to the current account, and other parts are counted on the capital account (e.g. technical cooperation).

36 http://www.oecd.org/document/35/0,3746,en_2649_34447_47515235_1_1_1_1,00.html

37 To give one notable example of the up-scaling of aid to the region, the United States pledged to double its aid to sub-Saharan Africa between 2004 and 2010 and surpassed this goal in 2009, a year early.

38 For a discussion of aid from emerging partners, see UNECA (2011).

39 This is also reflected in per capita ODA figures, which give quite a different picture on aid dependence in the region. On this measure, the Seychelles and Djibouti are the major recipients, receiving 648 and 150 US\$ per person in 2010. The lowest recipients in per capita terms are Madagascar and Eritrea (23 and 31 US\$ per capita respectively). When looked at in per capita terms, even large recipients like Ethiopia seem less blessed – with a per capita figure of US\$43 per person.

40 DRC’s especially large ODA inflow in 2003 was accounted for by exceptional debt-relief, something which subsequently provoked some controversy because of new engagements with China.

41 We ignore the budgets support for Seychelles and Djibouti here, because the absolute amounts involved are very small.

42 ‘China, EAC in new \$500 m trade, investment deal’, *The East Africa*, November 28-December 4th, Page 12.

43 See Brandkenya website http://www.brandkenya.co.ke/index.php?option=com_content&view=article&id=88:tata-to-open-base-in-kenya&catid=19:news-a-events&Itemid=88

44 These trends are not of course restricted to investors from outside the region – there is an increasing number of investors within the region who are targeting the enlarged regional markets. Thus, for instance, Bakhresa Group of Companies, based in Tanzania, has invested in the largest wheat mill in Uganda; Kenya’s Bidco Oil Refineries has an edible oil business in Uganda, and the regional retailer Nukumatt has 35 outlets across Kenya, Uganda, Rwanda and Tanzania (SID, 2012:69).

Recent Trends in Social Development



2.0. Introduction

IT IS WELL acknowledged in the literature that ‘good things don’t always come together’ and that economic progress and social progress often do not go hand-in-hand. Countries which attain fast economic growth sometimes have relatively poor performance in terms of improving human development indicators (e.g. life expectancy, infant mortality, etc.) and, conversely, some countries have achieved enormous progress in terms of human development, despite experiencing only a sluggish economic performance.⁴⁵ In a recent much discussed publication,

Kenny (2011) notes that there have been remarkable improvements over recent decades in a whole set of development indicators related to education and health.

This section tracks the progress in the East African region in terms of human development indicators. We start by providing an overview of regional performance, focusing on UNDP’s Human development Index (HDI), and comparing it with subjective evaluations of well-being, through survey data.

2.1. Tracking Human Development in the sub-region using the HDI

THE STANDARD HUMAN Development Index is a composite index consisting of GNI per capita, life expectancy at birth and the mean years of schooling, with each of these indicators being given an equal weighting. Since 1990, UNDP has classified countries in this way, given the opportunity to trace progress in terms of human development over an extended period. According to the 2011 Human Development Report (HDR), globally the HDI has shown an 18 percent increase between 1990 and 2010, with large improvements in life expectancy, school enrolment, literacy and income (UNDP, 2011:23). It is certainly not an index which is exempt of controversies,

but it does have the merit of simplicity in computation and interpretation.

Concomitant with low levels of per capita income, the Eastern Africa region is a region of low levels of human development. Of the 13 countries in the region, 11 of them are classified in the bottom quintile of UNDP’s human development index. As shown in Table 10, the 2011 rankings indicate that of the 13 countries comprising Eastern Africa, 9 have registered no change from the 2010 rankings, Djibouti and Madagascar have moved down a place and two each, while Kenya and Tanzania

have moved up a place each. Seychelles is the highest classified, reaching the ranking of 52 in 2011. The lowest in the region is DRC, which is classified in 187th place (Somalia would also class among the lowest, but data on income per capita is not available, so its ranking is not available). For the purpose of being able to compare more easily across countries within the region, UNECA has constructed a population-weighted HDI for the EAC-12, on which the average performance of the region in terms of improving its HDI index can be measured. In Figure

34, the regional average HDI is plotted with red dots, and the individual countries' HDI's are plotted with a blue line. While most countries in the region display an improvement in the index, in some cases that progress has been faltering, as in the case of Comoros, DRC, or Madagascar. In contrast, the EAC countries stand out as relatively strong performers in terms of improving their HDI indexes over this period. Rwanda, Tanzania, Ethiopia, Uganda and Burundi have all improved their HDI at a faster rate than the regional average.

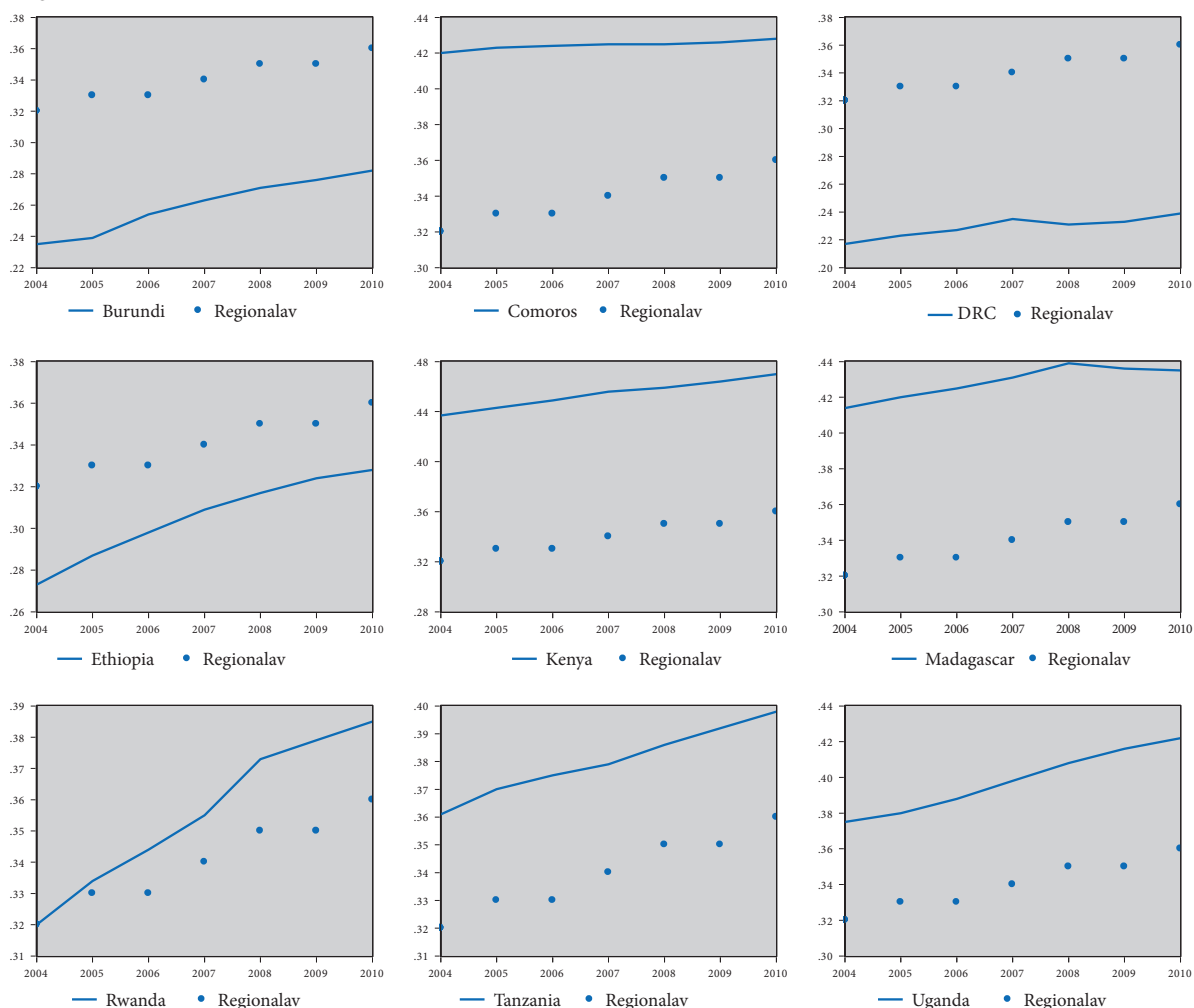
Table 10:
Human Development Indicator (HDI) and its sub-Components, 2011

		HDI	Life expectancy at birth	Mean years of schooling	Expected years of schooling	Gross National Income (GNI) per capita	GNI per capita rank minus HDI rank	Non income HDI
HDI rank		Value	(years)	(years)	(years)	(Constant 2005 PPP\$)		Value
		2011	2011	2011a	2011a	2011	2011	2011
52	Seychelles	0.773	73.6	9.4	13.3	16,729	-4	0.794
143	Kenya	0.509	57.1	7.0	11.0	1,492	15	0.584
151	Madagascar	0.480	66.7	5.2	10.7	824	26	0.605
152	Tanzania	0.466	58.2	5.1	9.1	1,328	10	0.523
161	Uganda	0.446	54.1	4.7	10.8	1,124	7	0.506
163	Comoros	0.433	61.1	2.8	10.7	1,079	9	0.488
165	Djibouti	0.430	57.9	3.8	5.1	2,335	-25	0.420
166	Rwanda	0.429	55.4	3.3	11.1	1,133	1	0.477
174	Ethiopia	0.363	59.3	1.5	8.5	971	0	0.383
177	Eritrea	0.349	61.6	3.4	4.8	536	6	0.421
185	Burundi	0.316	50.4	2.7	10.5	368	0	0.412
187	DRC	0.286	48.4	3.5	8.2	280	-1	0.399
..	Somalia	..	51.2	..	2.4

Source: UNDP, 2011

Figure 34:

Regional performance on HDI quite mixed



Source: UNECA calculations based on UNDP (2011) data, and a population-weighted regional HDI, based on 9 EAR countries for which data is available.

2.2. People's Evaluations of Well-being in the region do not always coincide with Income

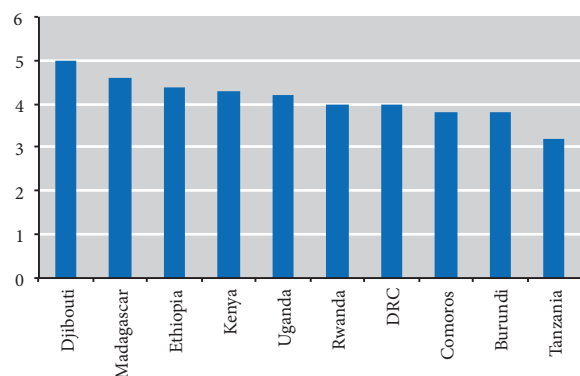
A NUMBER OF high income countries are beginning to take very seriously the importance of welfare evaluations provided by qualitative surveys of public opinion.⁴⁶ Such data would seem to suggest that people increasingly expect

high levels of well-being. Thus it could be argued that the HDI progress masks the rise in the level of unfulfilled expectations, especially those relating to socio-economic development. In other words, better performance with

respect to the HDI or economic performance is not necessarily concomitant with life satisfaction, as shown in Figure 36 below. Figure 35 also reveals a fairly large (and perhaps rather unexpected) dispersion in life satisfaction within the region. While on the whole, satisfaction is

Figure 35:

Life-Satisfaction Score (10.0 = most satisfied, 0.0 least satisfied), 2011

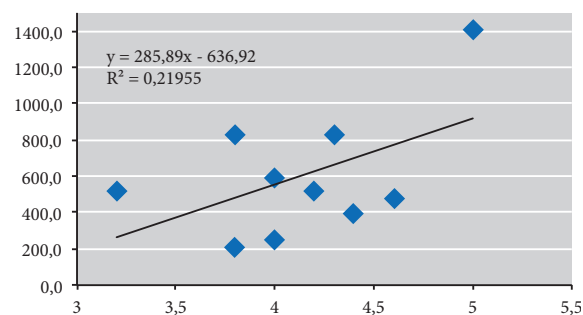


Source: GALLUP (2011).⁴⁷

higher in wealthier countries in the region, there are some notable exceptions, such as Ethiopia (a higher than expected level of satisfaction) and Tanzania (a lower level). DRC also notably performs well by this measure of welfare.

Figure 36:

Life Satisfaction and Income Per capita, EAR, 2011



2.3. How serious are Population Pressures in the Eastern Africa Region?

AFRICA IS THE region of the world with the highest birth rate. Africa's population is forecast to reach 2.3 billion by 2050. This accounts for half of the projected global increase. The Migration Policy Institute (2008) predicts that sub-Saharan Africa's population will grow faster than any other part of the world in the next century. Much concern is raised about the extent of population pressures in the Eastern Africa region. It is certainly the case that fertility rates remain extremely high- over six children per woman in Somalia, Uganda and DRC, for instance (Table 11). Fertility, especially in rural areas, is particularly high in countries such as Uganda, and when combined with lowering mortality, is resulting in persistently rapid population growth. Contrasting situations exist within countries however. For example, in Ethiopia fertility is substantially higher among rural women than among

urban women; rural women will give birth to nearly three more children during their reproductive years than urban women (5.5 and 2.6, respectively) (Ethiopian DHS, 2011). Despite successful efforts to reduce the birth rate, Kenya is still registering a fast rate of population growth because people live longer. The World Bank's Kenya Economic Update notes that Kenya's population will grow to an estimated 75 million people by 2040, even though the average number of children per family has fallen from 8.1 in 1978 to 4.6 in 2008.⁴⁸ Madagascar is another example of a country in the region that has successfully brought down fertility rates in recent decades (Sharan, 2011:451). Yet in a few countries in the region - notably Uganda - the fall in fertility has barely begun.⁴⁹

Table 11:

Fertility Rates (children per woman) 1990-2010

Major area, region, country or area	1990-1995	1995-2000	2000-2005	2005-2010	% Change 1990/5-2005/10
Ethiopia	7	6.48	5.6	4.6	-2.4
Djibouti	5.85	5.11	4.52	3.95	-1.9
Burundi	6.45	6.08	5.41	4.66	-1.8
Eritrea	6.08	5.66	5.19	4.68	-1.4
Madagascar	6.14	5.8	5.28	4.83	-1.3
DRC	7.14	7.04	6.7	6.07	-1.1
Rwanda	6.3	6	5.6	5.43	-0.9
Kenya	5.57	5.07	5	4.8	-0.8
Uganda	7.06	6.95	6.75	6.38	-0.7
Tanzania	6.05	5.75	5.66	5.58	-0.5
Comoros	5.3	5.3	5.3	5.08	-0.2
Somalia	6.5	6.5	6.5	6.4	-0.1
Memorandum					
Eastern Africa	6.29	5.92	5.54	5.11	-1.2
Sub-Saharan Africa	6.05	5.73	5.44	5.1	-1.0
WORLD	3.04	2.79	2.62	2.52	-0.5

Source: UNDESA, 2011.

How much do all these trends matter? Two alternative but complementary ways of viewing the statistics is with reference to population density and the amount of arable land per capita. Regarding population density, it would seem that some of the smaller countries in the region do indeed face a serious challenge. Rwanda, for instance, is ranked number 24 in the world regarding its population

density, and Comoros, number 26 (Table 12). With a population per hectare of 406 and 375 respectively, this is more than 10 times higher than the average for sub-Saharan Africa. Eastern Africa's most populous country, Ethiopia, in contrast has a population density of 79 per hectare.

Table 12:
Population Density

Ranking in world	Country	Population per square km of land area
24	Rwanda	405.5
26	Comoros	374.7
38	Burundi	309.3
60	Seychelles	189.0
67	Uganda	159.0
114	Ethiopia	79.4
131	Kenya	67.6
151	Eritrea	49.0
153	Tanzania	47.7
171	Djibouti	36.9
176	Sub-Saharan Africa	34.4
177	Madagascar	33.6
192	Congo, Dem. Rep.	27.6

Source: *Africa Development Indicators, 2011*

However, what is more important from the point of view of sustainability is the amount of arable land per capita, rather than the land per person. In this sense, the picture is rather different. From this perspective, Djibouti is the worst endowed country in the region, with scarcely 0.001 hectares per capita (the second lowest ratio of arable land per capita in the world). Seychelles is not far behind, with only 0.012 hectares per capita (Table 13). However, the situation of Burundi, Comoros and Rwanda looks much more favourable from this perspective. They are ranked numbers 93, 94 and 103 in the world in terms of the amount of arable land available (ranked in order of those with least arable land first).

Table 13:
Arable Land Per capita (hectares per capita)

Ranking	Country	Hectares per capita
1	Singapore	0.000
2	Djibouti	0.001
12	Seychelles	0.012
92	Somalia	0.112
93	Burundi	0.113
94	Comoros	0.115
103	Rwanda	0.129
109	Kenya	0.138
117	Madagascar	0.151
125	Ethiopia	0.171
130	Uganda	0.180
146	World	0.207
150	European Union	0.217
157	Tanzania	0.227
163	Sub-Saharan Africa (all income levels)	0.244

Source: *Africa Development Indicators, 2011*

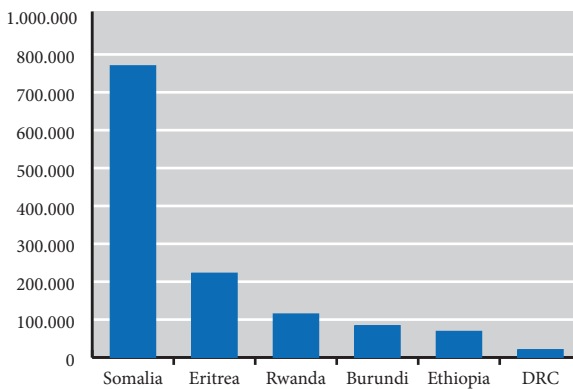
From this perspective, therefore, the issue of population pressures may be considered less pressing. Is this the right conclusion to draw, however? In the sense that the regional rate of population growth is among the highest in the world, and that rapid expansions of population put pressure not only on natural resources, but also the provision of social services, there is still a major sustainability challenge to be addressed. High rates of population growth put a burden on health and educational budgets, and increase the dependency ratio (i.e. the number of dependents per person within the labour force), causing a significant drag on economic growth.⁵⁰

Another population-related issue with which the region has to contend is migration. Migratory flows are generally

part and parcel of processes of regional integration, and economic theory suggests that migratory flows, like trade and investment flows, need to be encouraged. But the Eastern Africa region suffers particularly from ‘forced migration’ – displaced peoples due to conflict or climatic hardships. For example, large numbers of immigrants from Burundi and the Democratic Republic of Congo live in Tanzania; Somalis are still living in Kenya. Figure 37 and Figure 38 show data from the United Nations High Commission for Refugees (UNHCR). Somalia is in fact the largest source country of cross-border refugees in

Figure 37:

Source Countries of Cross-Border Refugees, 2010



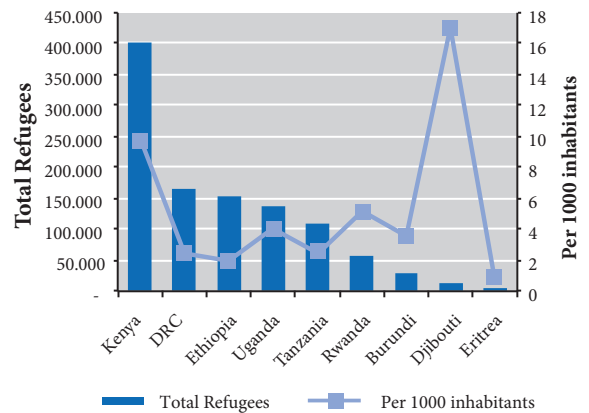
Source: UNHCR, 2010

Finally, the other major demographic trend which is affecting the region and changing the parameters for social development is urbanization. Eastern Africa has been one of the least urbanized regions in the world. In 2010, the average percentage of the population which is urbanised in Eastern Africa was estimated at only 23.7 percent, compared to 37.3 percent for the whole of Sub-Saharan Africa, and 50.6 percent for the global average. In South America, at the other extreme, more than 80 percent of the population are now estimated to be living in urban areas (UN-Habitat, 2011). In fact, Burundi has the lowest share of its population living in urban areas in the whole world – just 11 percent (Figure 40). The two largest economies in the region – Kenya and Ethiopia – are

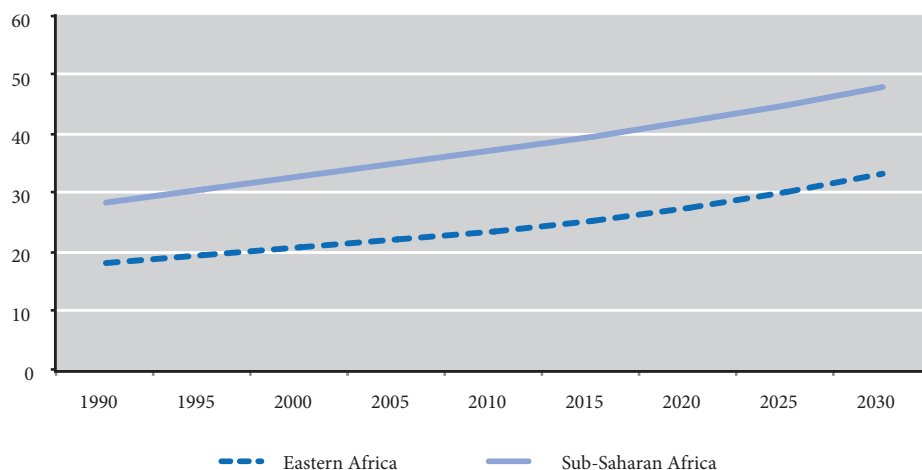
Africa. Refugees can impose a substantial burden on host countries by requiring additional public expenditures, putting pressures on infrastructure, and contributing to environmental degradation. A large influx of refugees can lead to the transformation of forest and rural land into camps and settlements, and displaced people may resort to unsustainable activities in absence of other means of survival (Ratha et al, 2011). In relative terms, Djibouti and Kenya are the countries in the region sustaining the largest populations of refugees.

Figure 38:

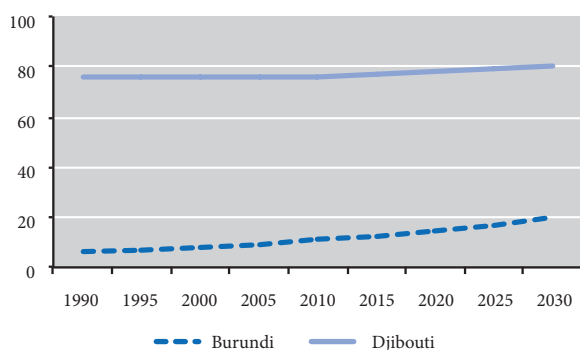
Host Countries of Cross-border Refugees, 2010



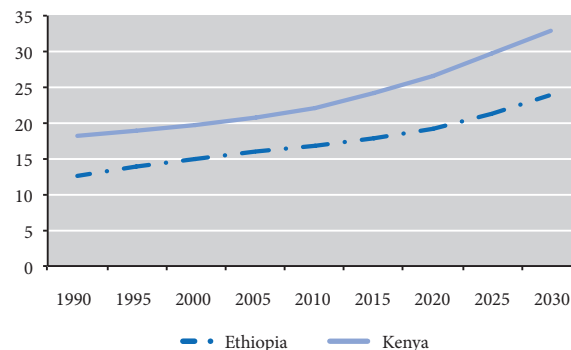
certainly ‘under-urbanized’ (Figure 41), in the sense of having a lower share of their populations living in urban areas than would be anticipated given their size and level of development. But the phenomenon affects practically the whole region (with the exception of Djibouti). As revealed in Figure 39, although there is a relatively rapid increase in the degree of urbanization across Eastern Africa, the region is forecast to continue to remain ‘under-urbanised’ in the coming decades.

Figure 39:**Eastern Africa – Rising urbanization, but still ‘under-urbanised’**

Source: UNDESA, 2011

Figure 40:**Burundi and Djibouti –the two regional extremes**

Source: UNDESA, 2011

Figure 41:**Ethiopia and Kenya**

Nevertheless, the scale of shifts that will be witnessed over the coming 20 years are large and with many social consequences. For instance, every year some 250,000 Kenyans are moving to cities and formerly rural areas are becoming increasingly urban (World Bank, 2011). Such shifts, if not well managed, can lead to slums, higher crime and more congestion. It does however facilitate the provision of social services, whose unit costs declines in more densely populated areas. It also makes the provision of infrastructures cheaper. So the trends present both challenges and opportunities for development.

2.4. Demographic Pressures and Development in the region

GOVERNMENTS AND OTHER stakeholders' capacity to respond to these demographic trends and migratory movements trends will determine the quality of life that their citizens are able to attain. A holistic approach is required, involving a whole range which incorporates greater investment in health sector personnel, improved access to contraception, and improving education (particularly for girls). If these policies come together correctly, there are some hopes that the region could benefit, just as India and China have before, from a 'demographic dividend' – that is, when the share of the working-age population rises relative to children and old people, thus giving an additional impetus to GDP growth per person. But this outcome is contingent on the right set of policies being in place, particularly with regard to family planning.

By some estimates, a quarter of married women in Sub-Saharan Africa wants contraceptives, but cannot get them. Kenya, Uganda, and Tanzania all underwent large increases in contraceptive prevalence in the 1990s, but stagnated in the 2000s (Sharan et al., 2011). This reflects in part reduced aid for family planning over the past 15 years, but also, in some cases, political ambivalence about its desirability. The 2011 MDG report notes that even though demand for family planning will likely increase based on the current unmet need and the expected rise in number of women and men of reproductive age, aid for family planning as a proportion of total aid for health declined over the past decade and stood at only 2.6% in 2009. Aid for family planning has fallen in virtually all recipient countries in the region. Access to contraceptives continues to be a challenge for many, particularly in Eastern Africa.

2.5. Unmet Contraceptive Needs – Eastern Africa is lagging behind

WHILE CONTRACEPTIVE PREVALENCE continues to improve, Eastern Africa is clearly the region with the highest level of unmet contraceptive needs, with Burundi, Ethiopia and Somalia with the lowest levels of provision (Table 14). There is awareness in the region about contraception, but limited access. This is particularly critical for the poor, who may be unable to meet their needs for contraception by independent means, and are dependent on provision through the government.

Table 14:
Contraceptive prevalence rate (Modern methods) (%)

Country	
Burundi	9
Comoros	26
DR Congo	21
Djibouti	18
Ethiopia	15
Kenya	39
Madagascar	27
Rwanda	36
Somalia	15
Tanzania	26
Uganda	24

Source: *The State of Midwifery Today*, 2011.

Note: No data available for Eritrea and Seychelles

Even though they clearly fall short of the demand, governments in the region continue to provide contraceptives. In Rwanda, contraceptives are available at no cost to citizens. The national strategy goes beyond provision of contraceptives to women only, to targeting men through condom distribution and the no-scalpel vasectomy. Additionally, in collaboration with development partners and NGOs, Rwanda developed its national reproductive health policy and national family planning strategy (2006-2010), which together with the condom policy have contributed to lowering the population growth rate. The preliminary findings from the 2010 Rwandan Demographic and Health Survey (2011) are encouraging showing that there has been a decline in the total fertility rate and an increase in the

proportion of married couples using modern methods of contraception. Modern contraceptive use has increased dramatically from 10% in 2005, to 27% in 2007/8 to 45% in 2010 but there is still some way to go to achieve the Economic and Poverty Reduction Strategy's target of 20 per cent by 2012. The total fertility rate (average number of children per woman) has at the same time declined from 6.1 to 5.5 to 4.6. Finally, research over the years has shown a consistently robust link between years of schooling and fertility – education of girls is one of the surest ways to reduce fertility rates, and provides an added reason for governments to invest aggressively in gender-balanced educational opportunities.

2.6. Monitoring social progress – a success story in maternal health

MATERNAL AND CHILD mortality remains a challenge in most countries in the region. It is imperative that as part of implementation of the renewed Maputo Plan of Action, a framework that ensures the rights and health of women, member States address maternal health as prioritized during the AU Heads of States Summit, held in Kampala, Uganda in 2010. Leaders discussed the role of maternal health in moving Africa forward. According to Jones et al (2011), each year between 350 000 and 500 000 women die as a result of pregnancy and childbirth and, an estimated 99% of these deaths are in developing countries, with the vast majority in sub-Saharan Africa. The MDG target is to achieve a Maternal Mortality Rate (MMR) reduction of 75% by 2015. According to the UN, MMR had fallen by only 35% by 2008. This said, there have been some signs of impressive improvement in some countries of the EAR (Table 15), albeit while still registering unacceptably high levels of MMR.

Countries in the region have instituted various measures to address MMR. For example, in Tanzania, women have

received clean delivery kits aimed at reducing mortality due to infection. Jones et al (2011) study found these particularly effective in low-resource settings where home birth is common and clean delivery supplies are scarce. It is an acknowledged fact that skilled health professionals are essential in the reduction of maternal death and morbidity. Quality midwifery education is important for accelerating MDGs 4 and 5. Rwanda and Tanzania reported major shortcomings in midwifery education (UNFPA, 2011). Ethiopia and Somalia need to increase their midwifery workforce by 6 to 15 times, while Tanzania needs to triple or quadruple its workforce. Djibouti, Madagascar and Uganda need to double it (UNFPA, 2011:20). Governments have committed to strengthening midwifery services in the areas of skilled birth attendance (DRC, Ethiopia), provision of additional primary health care workers (Kenya) and training more midwives (Rwanda, Tanzania).⁵¹

Table 15:**Improvement in Maternal Mortality Rates per 100,000 live births**

MMR global rank	Country	MMR 2008	MMR 1990	Annual % change 90-08
154	Burundi	569.6	711.6	-1.2
123	Comoros	225.3	449.9	-3.8
153	DRC	533.6	550.0	-0.2
149	Djibouti	461.6	606.5	-1.5
170	Eritrea	751.2	1292.5	-3.0
157	Ethiopia	589.7	967.7	-2.7
146	Kenya	413.4	452.3	-0.5
141	Madagascar	373.1	484.4	-1.4
143	Rwanda	383.4	813.4	-4.1
166	Somalia	674.6	962.8	-2.0
148	Tanzania	449.0	610.2	-1.7
140	Uganda	352.3	571.0	-2.7

Source: UNICEF (2011)

Comoros has decreased maternal mortality by 36 percent over the past 20 years, but it still remains high even though skilled birth attendants assist a high percentage of births (UNFPA, 2011). DRC has also reduced maternal mortality and has a roadmap to improve maternal and newborn-health which has been budgeted for, but is not yet fully operational at district level. Djibouti provides maternal and newborn care free of charge since 2006. In Ethiopia, on the other hand, only 6% of births are attended by a skilled health worker. In Kenya, maternal health figures improved in the 1990s, but maternal mortality has not

been reduced in the past decade. An estimated 14% of maternal deaths in Kenya are due to HIV. Madagascar has also prioritised maternal and newborn health. Rwanda has significantly reduced maternal mortality, even though it remains high. Through its national health development strategy, the country prioritizes maternal and newborn health, and has an insurance plan that provides free maternal and newborn health services. These interventions clearly show governments' commitment to addressing maternal health.

Table 16:
Costs of Providing Midwife Training

Country	Duration of training	Scope of costing	Cost of each student per year (US\$)
Burundi	4 years	Tuition, transportation, accommodation and living fees, registration fees, internet fees, library charges	3,250
Ethiopia	4 years	School fees (classroom learning and clinical experience in the field)	1,630
Kenya	-	Recurrent expenditures	1,800
Tanzania	-	Recurrent expenditures	3,236

Source: Friedman H. et al.(2011).

If countries are to accelerate reduction of maternal mortality and attain the health MDGs, there is need for health, labour, planning and other Ministries to work together to ensure increased training of midwives (Table 16). Finance is key to improving women's reproductive health care. Huntington (2010) asserts that in 2007 37% of all health ODA went to maternal, newborn and child health.

According to UNFPA (2009), funding for family planning has plummeted over the past decade despite a 25% increase in the number of women of reproductive age, leaving healthcare users with severe financial burdens.

2.7. Progress in Tackling HIV/AIDS-- but levels of infection are still high

THE DECEMBER 2011 ICASA meeting focused on the role of African leaders in the HIV response and the efforts devoted to mobilize resources locally. The June 2011 General Assembly gathering in New York affirmed that HIV/AIDS was still high on the political agenda. Political will is evidenced by commitments including those made during the gathering of African Ministers of Finance and Health in March 2011, where they discussed ways of investing in health, noting that "investment in health is an investment in economic development," with the aim of improving health outcomes to help accelerate achievement of the health-related MDGs. The emergent 2011 Political Declaration on HIV/AIDS is a Resolution that among others recognises that HIV and AIDS constitutes a global emergency, and poses a challenge to the development. Joseph Deiss, President of the United Nations General Assembly recognises the bold targets in

the Declaration, which he argues comes at a time when international assistance for the AIDS response has dropped for the first time since 2001. Member States agreed to increase AIDS-related spending to reach between US\$ 22 billion and US\$ 24 billion in low- and middle-income countries by 2015.

Concerted actions against HIV/AIDS have continued to yield fruit. Population surveys of Ethiopia, Kenya and Tanzania reveal significant declines in new infections due to changing sexual behaviour and more effective treatment. Over the past decade, Kenya has stabilized its rate of new HIV infections. National adult coverage of antiretroviral therapy has expanded from an estimated 4% in 2004 to 72% in 2010. About 78% of pregnant women living with HIV are now receiving antiretroviral treatment to prevent new HIV infections in their children, compared

to 21% in 2006. Kenya and Ethiopia have, in line with the Political Declaration on HIV/AIDS, pledged to eliminate new HIV infections among children by 2015.

In Kenya, Rwanda and Uganda, new infections have dropped due to voluntary medical circumcision, an option that the Rwanda Ministry of Health adopted in addition to piloting the “no scalpel vasectomy” as a way of combating the spread of HIV. According to IntraHealth, this model is built on partnerships with district leaders, community health workers, and local health centres to educate communities about vasectomy and make these services available. HIV prevalence declined among young people (aged 15–24 years) in at least 21 of 24 countries with national HIV prevalence of 1% or higher. The drop

in HIV prevalence was statistically significant among pregnant women attending antenatal clinics in Ethiopia, Kenya and Tanzania. Tanzania also registered statistically significant decline among men.

At the centre of addressing HIV/AIDS is the provision of ARTs. UNAIDS note that increase in ART coverage is helping countries achieve universal access to treatment, care and support. Table 17 maps ART coverage in Eastern African countries, with really quite impressive levels of coverage for low income countries like Comoros, Ethiopia and Rwanda. However, the picture is still a mixed one, and in Ethiopia only 9.3% of pregnant eligible women receive HIV services.

Table 17:

Anti-retroviral Coverage (% share of infected persons)

0-19%	20-39%	40-59%	60-79%	>80%
DR Congo	Burundi	Eritrea	Ethiopia	Comoros
Djibouti		Uganda	Kenya	Rwanda
Madagascar		Tanzania		

Source: UNAIDS and WHO, 2011

HIV and AIDS cannot be effectively tackled outside national priorities. Synergies with other sectors need to be strengthened, for example, by focusing social support on the marginalized including orphans and vulnerable children. It is also important that national strategies continue

to work together with communities in programme design and delivery. Communication strategies hinging on behaviour change, such as that implemented in Uganda in the 2000s, need to be promoted more widely.

2.8. Advancing Social Development - The centrality of social development in policy debates

HELD IN JULY 2011, the third EAC meeting of Ministers responsible for gender and social development acknowledged wider problems in social policies including, among others, youth unemployment, food shortage, irregular weather patterns etc. This shows a need to continue to interrogate the link between different factors impinging

upon social development and calls for a review of social policies across the region, beyond just the EAC member States. While trying to address the interrelated factors, the focus of the following section of the report is to show examples of what has worked, and examine links between social policy and development in general.

2.8.1. Social Protection: Is there a pre-defined path?

Social protection, the means through which Governments cushion beneficiaries from poverty and vulnerability, has assumed different characteristics within the EAF-13. Various novel social protection interventions have included - but are not limited to - cash transfers, school feeding programmes and/ or uniforms, the introduction of pensions for the elderly, unemployment benefits etc. Tanzania was among the first countries to mainstream social protection in its Mkukuta (the Kiswahili acronym for the National Strategy for Growth and Reduction of Poverty), and Rwanda has followed suit with its Economic Development and Poverty Reduction Strategy (EDPRS). The Tanzanian health insurance scheme deserves special mention, having received the ISSA Good Practice Award for Africa in 2011.⁵² The Tanzanian National Health Insurance Fund (NHIF), which started operations in 2001, is a prepayment health insurance scheme that received recognition for improvements in its health insurance scheme. The NHIF received recognition for good practices in social security while the Rwanda Social Security Board was recognised for its strategy of extending social security coverage to the informal sector (2010). Uganda's

electronic service delivery channel is another practice that commenced in 2011, in addition to the Kenyan Mbaao Pension plan (2011) which also targets workers in the informal sector.

At the EAC and IGAD levels, there has been recognition of shortcomings, with calls for concerted efforts to improve social protection for persons with disabilities, and linking social protection with food security, a potentially beneficial approach given the recurrence of droughts in the IGAD region. EAC and IGAD also prioritise social protection, with EAC calling for the harmonization of social policies, and IGAD linking social protection and food security in its Regional Food security and risk management (REFORM) programme.⁵³ With the impressive economic growth that Eastern Africa has experienced in the past few years, there is need to create fiscal space for supporting expenditures on social security. As donor funding cannot be guaranteed over the long term, domestic funding for social protection programmes needs to be a priority to put them on a sustainable footing.

2.8.2. Mapping cash transfers in the region

One important instrument in the armoury of modern social protection systems are cash transfers. Cash transfers, whether conditional or unconditional, have now been instituted in most countries of Eastern Africa. This assistance is mainly targeted at a wide range of disadvantaged persons including the unemployed, girls, widows, orphans and vulnerable children (OVC) with different benefits and administered through different means:

- Kenya, like other Eastern African countries, has collaborated with international organizations to establish its conditional cash transfers (CCT) program, targeting orphans and vulnerable children (OVCs), focusing on poor households fostering OVC aged 0-17. This scheme, first introduced in 2004 with the

support of UNICEF and other partners such as the World Bank, DFID, SIDA and DANIDA, reached over 250,000 people in 2010 (approximately 90,000 households), providing on average about US\$20 per month. It is expected that this will be extended to another 150,000 households in 2013 (UNICEF, 2012).

- In conjunction with DFID, IrishAid and UNICEF, Uganda is piloting the Social Assistance Grants for Empowerment cash transfer scheme providing sh23 000 per month to the elderly and other vulnerable groups e.g. child-headed families, single mothers and the disabled.

- ▶ Ethiopia is also frequently cited as spending the most on safety nets, though most of this funding currently comes through donor support. Ethiopia's Productive Safety Net Programme (PSNP) started in 2005 with between 5 and 6 million Ethiopians (approximately 10% of the population at the time), comprising of a public works programme for the actively productive population, and conditional transfers for very poor people who cannot participate in other forms of productive work e.g. pregnant women, nursing mothers, and unconditional transfers for people with no assets.
- ▶ Burundi has implemented an old age, disability and survivors social insurance system. This covers salaried workers, military and police personnel, contract workers from the civil service and public utility commission.
- ▶ The Rwandan Vision 2020 Umurenge Programme (VUP), which involves public works and cash transfer, has reached about 36,000 households and contributed to the fall of the percentage of extreme poor among beneficiaries from 40.6% to 9% (EUI, 2010). This is a social protection programme to reduce extreme poverty in targeted VUP sectors. This scheme started in 2008, with a budget of £20 million, and will run until 2013 (DFID, 2012).

Table 18:**Transfers in Eastern Africa**

Country	Share of total household income provided by transfers and remittances
Ethiopia (2004)	7.1
Madagascar (1999)	9.6
Tanzania (2007)	16.1
Average across African countries	14.1

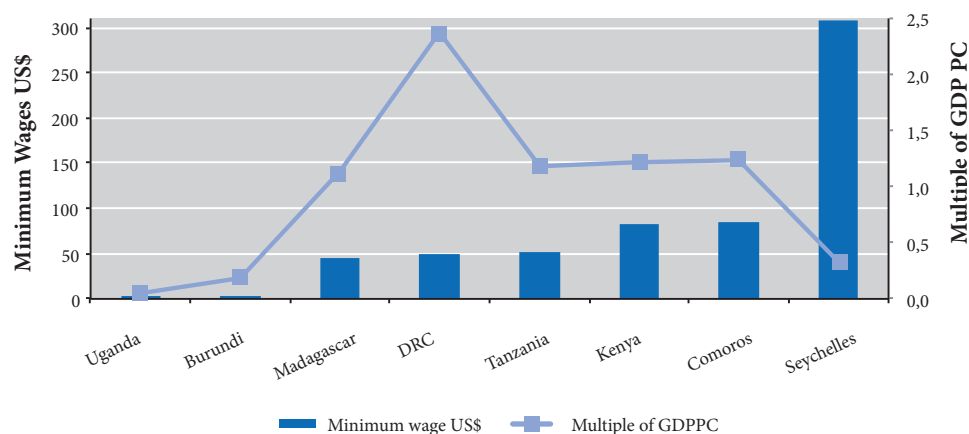
Source: *European Report on Development*, citing Charmes 2010 from income expenditures surveys or living standards surveys.

National social protection strategy designers need greater awareness of evidence regarding the gendered nature of poverty and vulnerability (Jones and Holmes, 2011). Involvement of women in governance structures of cash transfers (Table 18), which is one way that could benefit women, is crucial if social protection is to address gender inequality. While cash transfers have worked in the region, awareness-raising could be scaled-up for those aimed at improving outcomes for females, so as to ensure better results. More generally, regular monitoring and evaluation of social protection programmes is essential if maximum benefits are to be derived. There is of course also a need to ensure that the schemes are financially sustainable in the long run.

2.8.3. Minimum Wages – Towards the setting of regional standards?

A further instrument of social protection which is perhaps under-discussed in the region is the role of minimum wages. Minimum wages are often considered to be a mechanism which are not appropriate for low-income countries - because of large-pools of un and under-employed workers, it is sometimes argued that a minimum wage is not only counterproductive, in terms of undermining the incentive to create employment, but also impractical because it is difficult, if not impossible, to enforce. Such views, however, need to be contrasted with a lot of empirical evidence (albeit mostly from higher income

countries) that minimum wage policies can protect the purchasing power of the most vulnerable workers and reduce the incidence of poverty. In Eastern Africa, the issue has become particularly important in light of the 'double-whammy' food and fuel price crisis of 2011. For instance, in May 2011 the Kenyan Government raised minimum wage by 12.5% in response to rising food prices, as well as removing duties on essential foods and fuel.

Figure 42:**Minimum wage setting, 2011**

Source: ILO (2011) national sources

In a majority of countries across the world, minimum wages are set within a range of 30–60 per cent of GDP per capita (ILO, 2009). In the Eastern Africa region, however, a few countries conspicuously stipulate minimum wages that are above the level of GDP per capita – suggesting that the wages are set at levels which are unlikely in practice to be honoured (Figure 42). This is the case of DRC, for instance. In Comoros, Madagascar and Tanzania, too, minimum wages are set at a level close to that of GDP per

capita. At the other extreme, Uganda has not updated its minimum wage since the beginning of the 1980s, and as a consequence minimum wages are now at levels far below minimum subsistence levels. Finally, there are a group of countries for which no minimum wage is stipulated. Some discussion among regional governments about a more consistent approach to the setting of minimum wages may be fruitful.

2.8.4 Tracking spending on education and health

In recent years, governments in the region have undertaken a number of commitments to spend a targeted amount of their total expenditures on social objectives. In Dakar, Senegal, in 2000, 25 countries from Sub-Saharan Africa signed up to the Education For All (EFA) Fast Track Initiative (FTI) which committed donors to increase their aid commitments to the education sector, while recipient governments agreed to increase education spending to at least 20% of government expenditure, allocating 50% of education expenditure (10% of government expenditure) to primary education. At the Special Summit on HIV/AIDS, Tuberculosis and Other Infectious Diseases held in Abuja, Nigeria in 2002, AU governments committed

themselves to improving the health sector and agreed to a minimum health sector spending target of 15% of government expenditure. These targets are reminiscent of those agreed at the Copenhagen Social Summit 1995, in which it was agreed that both donors and recipient governments would dedicate 20 percent of their expenditures to provide basic social services. However, that landmark agreement – an explicit acknowledgement of the crucial importance of investing in human capital – was slowly eclipsed by the Millennium Development Goals, which emerged from a OECD DAC document, but was in 2000 embraced by the whole of the international community through the United Nations. The two approaches are very

different – one stresses the importance of the required financial resources being dedicated to social services (‘inputs’) and the other focuses on developmental outcomes (‘outputs’). In fact, however, no artificial dichotomy should be drawn between the two sets of indicators – arguably, it is important to track both input and output measures simultaneously. Sufficient financial resources are a necessary but not sufficient condition for achieving improvements in human development.

Given this broad context, what does the data show us about financial outlays for health and education in the Eastern Africa region? Firstly, in education a number of regional economies perform quite well – half of the twelve EAR countries for which data exist exceed the 20% target of general government spending dedicated to the education sector. Countries reaching this target include Comoros, Djibouti, Ethiopia, Kenya, Rwanda and Tanzania, and two others – Madagascar and Uganda – are not far from achieving the target (Table 19). Secondly, in health, the

story is rather different- with only 4 countries dedicating 15 percent or more of their budgets to the health sector (DRC, Djibouti, Rwanda and Tanzania). Thirdly, even for countries reaching the corresponding targets, when converted into dollar-per-capita expenditures, the scarcity of resources in the EAR becomes self-evident – the combination of low per capita incomes, combined with a low priority on social spending, plus in some cases a low share of overall public spending in GDP, means that government social expenditure translates into extremely low levels of expenditure per capita. Uganda, for instance, spends the equivalent of less than 8 dollars per person per annum on health expenditures. This exercise shows that monitoring closely the resources which are dedicated to the social sectors needs to be carried out in tandem with MDG assessments. Although there is a margin of errors in these statistics (because of differences between outlays and budgeted amounts, and different ways of sectoral breakdowns of the numbers), the exercise is thus a useful one.

Table 19:**Government Expenditures on Education and Health, EAR-12, 2008-9**

Country	Education	Health	% of govt. spending		Target		Expenditure per capita (\$ per person)	
	% GDP	% GDP	Education	Health	Education	Health	Education	Health
Burundi	8.3	5.2	16.4	11.8	20%	15%	17.1	10.8
Comoros	7.6	2.1	35.8	8.0	20%	15%	62.7	16.9
DRC	2.0	5.2	6.8	17.5	20%	15%	4.9	12.7
Djibouti	8.4	5.4	20.2	15.3	20%	15%	118.0	75.2
Eritrea	2.2	1.0	7.2	3.0	20%	15%	11.3	5.1
Ethiopia	5.5	2.2	32.0	11.5	20%	15%	21.5	8.7
Kenya	7.0	1.6	23.6	5.8	20%	15%	58.0	12.9
Madagascar	3.0	2.9	19.6	14.5	20%	15%	14.3	13.7
Rwanda	4.9	4.3	20.2	18.2	20%	15%	29.3	25.7
Seychelles	5.0	3.1	13.6	10.1	20%	15%	559.2	351.3
Tanzania	7.2	3.7	27.4	18.0	20%	15%	37.1	19.0
Uganda	3.2	1.4	18.3	10.5	20%	15%	17.0	7.6

Sources: UNESCO (2011) for education data, WHO (2011) for health data. Education figures based on data for 2009, Health data for 2008. Calculations for expenditure per capita based on UNECA estimates.

Notes

45 See, inter alia, Mehrotra, and Jolly (2000).

46 The Sen-Foutoussi-Stiglitz Commission (2010), at the request of the French President Sarkozy, stands out. See OECD (2011) for a discussion of the use of subjective data in policymaking.

47 The question regarding overall life satisfaction, asked by Gallup was “Please imagine a ladder, with steps numbered from zero at the bottom to ten at the top. Suppose we say that the top of the ladder represents the best possible life for you, and the bottom of the ladder represents the worst possible life for you. On which step of the ladder would you say you personally feel you stand at this time, assuming that the higher the step the better you feel about your life, and the lower the step the worse you feel about it? Which step comes closest to the way you feel?”

48 The decline in fertility was particularly sharp in the period from 1980-95, though the rate of decline has slowed in recent years. See Sharanet. al (2011).

49 Miracle or Malthus? The Economist, December 17th 2011, pp. 91-92

50 See, inter alia, Chapter 18 of Bairoch (1992),

51 See the website ‘Every woman, every child’ <http://www.every-womaneverychild.org>

52 ISSA is the International Social Security Association which encourages good practices through its 3-yearly awards. Tanzania was presented with the award on 5 December 2011.

53 EAC(2009), <http://www.aidforafrica.org/wp-content/uploads/2011/01/EAC-2009-Report.pdf> and IGAD Reform.

Special Thematic Section

Towards Greater Food Security in the Eastern Africa Region – An Analytical Overview and Some Policy Implications

3

CHAPTER

3.0 Introduction

DESPITE THE GENERALLY up-beat assessments of the macroeconomic circumstances for the Eastern African Region in Section 1 of this report, one among a number of major challenges which the region still has to confront is food security. The term “food security” is used to describe both the availability of, and access to food. To be food secure, a nation or family must have reliable sources of food and sufficient resources to purchase it. The global food crisis that erupted in 2007 worsened food insecurity among the neediest populations in the Eastern African sub-region. Between March 2007 and March 2008, global food prices increased, on average, by 43 per cent, according to the International Monetary Fund (IMF) figures. Although prices subsequently subsided, food prices again rose sharply in 2010-11, causing more hardship among food insecure populations. Estimates show that the poorest households allocate between 50 – 90 percent of their incomes to staple foods. The price rises are increasing the incidence of food insecurity and income poverty and negatively affecting the prospects of attaining the Millennium Development Goals (MDGs).

However, the crisis has also provided countries of the region with an opportunity to find long-term solutions to food insecurity and hunger through greater investments in agriculture and the pursuit of an agriculture-led growth

and development policy. Therefore, it is imperative to build strong and consistent policies that will respond to the immediate crisis and sustainably develop the agricultural sector over the long-term.

This section of the report reviews the state of food insecurity and hunger in Eastern Africa in the context of the food price surge worldwide as well as global policy responses to the crisis and their impacts on food security and trade within the Eastern African sub-region. It comprises of:

1. A sub-regional review of the main food security issues and an analysis of the key sources of food vulnerability at the country level;
2. An overview of the global food price surge and its effect on local markets and a review of the policy responses at national and sub-regional levels, and their impacts at the household level;
3. A summary of short, medium and long-term policy measures and programmes that are being implemented at both national and international levels to help mitigate the negative impacts of the crisis;

4. A concluding part on the main challenges requiring further actions and policy implications for addressing them.

3.1 The State of Food Insecurity in Eastern Africa

THE 1996 WORLD Food Summit defined food security as “a situation that exists when all people, at all times, have physical, social and economic access to sufficient, safe and nutritious food that meets their dietary needs and food preferences for an active and healthy life.” Conversely, food insecurity exists when people do not have adequate physical, social or economic access to food as defined above. This emphasis on the access to food departed from the conventional approach of the 1970s that focused on food availability.

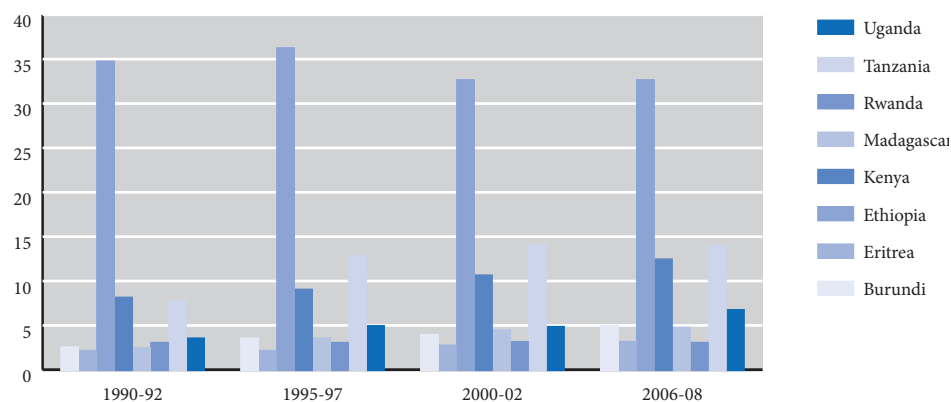
The FAO in its State of Food Insecurity in the world 2011 (SOFI) monitors yearly undernourishment amongst

forty-four (44) countries, of which thirty nine are in sub-Saharan Africa. The measure has some shortcomings when applied to national circumstances and a UN-system wide effort is now ongoing to develop, adopt and promote new internationally accepted standards for measuring hunger in countries (see Box 4).

There has been some real progress in Africa and in the sub-region since the beginning of the 1990s in the fight against hunger but huge challenges remain. With 30 percent of the population of sub-Saharan Africa (SSA) (Djibouti, Comoros, DRC, Seychelles and Somalia excluded⁵⁵),

Figure 43:

Trends in the number (in million) of people undernourished in EAR-8*, 1990-92 to 2006-08



*Comoros, Djibouti, the D.R.C., Somalia and Seychelles excluded.

Source: FAO SOFI 2011 data

On average, in the sub-region, the depth of hunger – i.e. the intensity of food deprivation⁵⁶ is well below (by 44

per cent) the agreed borderline of 200 kilocalories per person per day.

Box 4: Towards new approaches and estimates of undernourishment and hunger

The **World Food Summit Goal** is to reduce by half, between 1990–92 and 2015, the number of undernourished people in the world, while the **Millennium Development Goal 1**, target 1C seeks to halve the number of people suffering from hunger between 1990 and 2015. At this level, food balance sheets are the main sources used to estimate national and per capita food availability through supplies. At the national level, total food availability is also equated to total food consumed. This energy-intake approach has been criticised by nutritionists as a poor measure of nutritional status.

Other quantitative methods – such as household income and expenditure surveys, individual food intake surveys, and qualitative measures of food insecurity can complement the FAO method based on supply. These methods are designed to gather information, at the household and the individual levels, on access and consumption of food or on intake and utilisation of nutrients by the body. This is where the food security status can be practically approached through anthropometry surveys for nutritional and risk assessment and to relate food/nutrient intakes to illness and disease.

These conceptual and operational developments tend to focus on: i) “inadequate access” to food as a cause and consequence of the vulnerability of the households and of the individuals within them, and on; ii) their resilience to external shocks. UN agencies are improving the definition and use of measurement methods at the household level for differentiating households at varying degrees of food insecurity in order to target and evaluate their interventions for enhancing adequate access to food.

This has led to the setting by the **Committee on World Food Security (CFS)**, in its meeting in 2010, of a “roundtable to review the methods used to estimate the number of hungry”. The Committee endorsed the key findings and the recommendations contained in the outcome document of the roundtable (FAO, 12–13 September 2011). It asked FAO to make several adjustments to its methodology, namely: 1) include in the estimation of how changes in food access due to changes in income and food prices affect undernourishment; 2) to improve the construction of food balance sheets by using the large number of household survey data that have become available in recent years, to complement measures of undernourishment with a number of other indicators intended to better capture the multifaceted nature of food insecurity.

FAO has set the year 2011 as one of transition while the methodology is being revised. “Therefore, no updated estimates for the number of undernourished people in 2009 and 2010 are reported in [2011] State of food Insecurity in the World, nor has an estimate been made for 2011.” (FAO SOFI 2011:10).

3.2 A region marred with protracted crises: Hunger hotspots and Drought

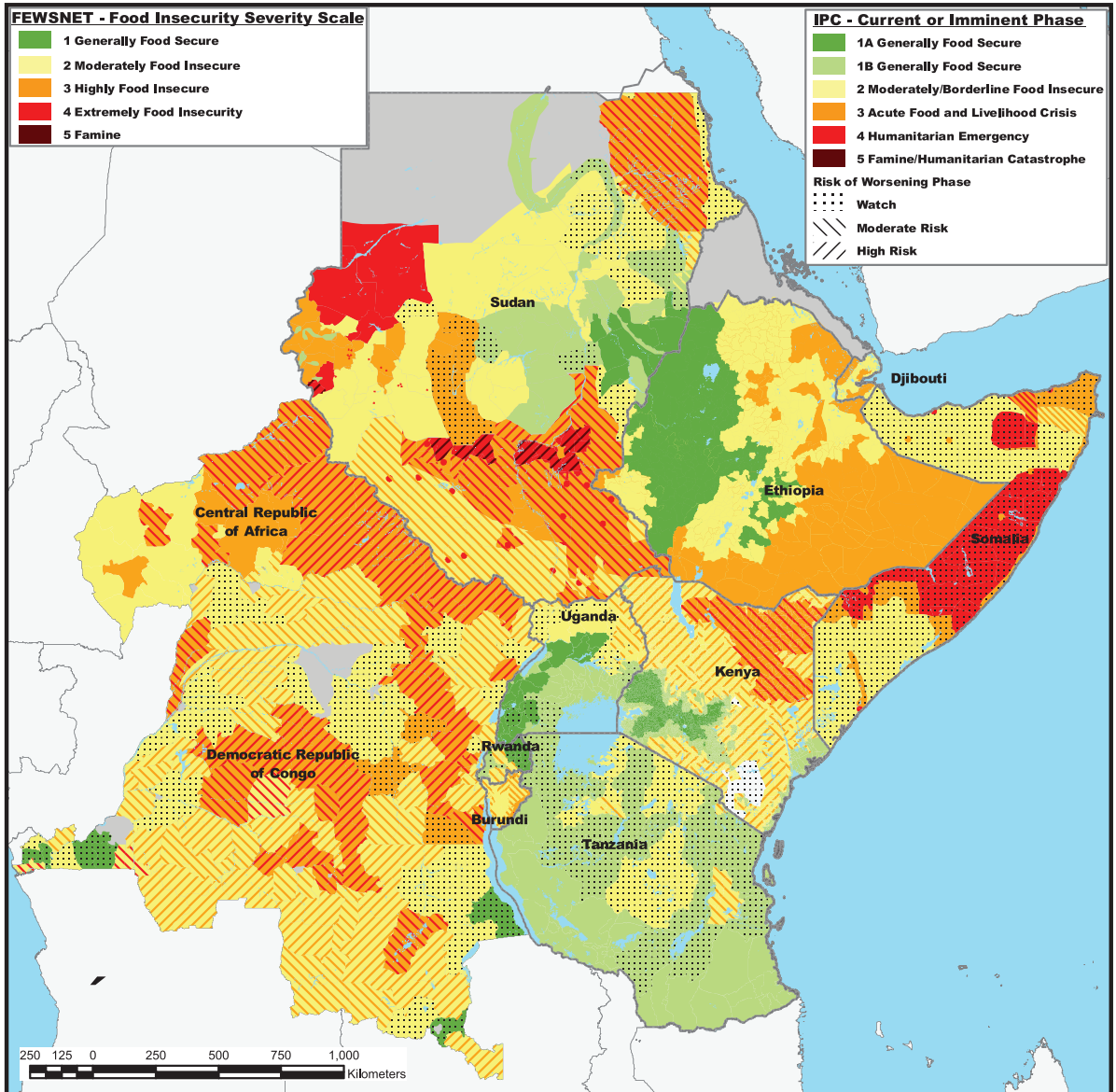
THE FAO GLOBAL Information and Early Warning System (GIEWS) compiles an annual list of countries affected by food crisis. These are countries regarded as having “hunger hotspots” – areas where a significant proportion of people are expected to lack the resources needed to deal with critical problems of food insecurity, such as hunger and malnutrition and famine. In the most critical cases, such a situation results from a protracted crisis – i.e. a more than a decade-long food security crisis. Globally, six of the fourteen countries in a protracted crisis are from the sub-region. In relative terms, Kenya and Uganda have been the least exposed, but nevertheless at a very high level with eleven years of duration each. At the other end of the spectrum, Ethiopia and Somalia endured it for almost a generation (21 years), preceded by Eritrea (18) and the DRC (19 years) (FAO, December 2011⁵⁷). As of November 2011, only four (4) countries of the sub-region – Comoros, Rwanda, Seychelles, Tanzania, were classified as ‘food secure’, i.e. they did not at that time face situations that would require emergency food assistance.⁵⁸ Acute food and livelihood crisis still prevails in parts of Djibouti, Eritrea, Ethiopia, Kenya and Somalia (Figure 44). While Somalia could still be facing a humanitarian catastrophe, the whole of DRC is moderately insecure or at moderate to high risk of worsening situation.

According to the most recent assessment, at least 21 million people are in need of immediate humanitarian assistance in the sub-region. This represents about ten per cent of the total population of these countries – and 40 per cent in the case of Somalia. Small scale farmers and herders, food insecure urban dwellers constitute nearly four out five people in this group. The famine in Somalia has caused the displacement of more than 800,000 refugees towards Kenya and 260,000 to Ethiopia, with a further 30,000 having sought refuge in Djibouti (GIEWS, 2011). U.N. estimates show that the financial need for immediate, short-term drought relief assistance amounts to

\$2.5 billion (of which only 63 percent had been funded as of September 9th 2011, leaving a gap of \$1.6 billion) (OCHA, 2011). As dramatic as the prevailing famine has been in the Greater Horn of Africa, it illustrates a wider problem regarding the extent and the geographic spread of food insecurity across the sub-region. For instance, there is already potentially a serious situation developing in South Sudan, where the cereal gap for 2012 is estimated at 400,000 tons due to erratic rainfall, poorly functioning markets and an increased demand resulting from the influx of displaced persons from Southern Kordofan and Blue Nile States.⁵⁹

The economic impact of the current drought compounds the challenges to build resilient economic blocs within the sub-region. In Kenya, due to the size of the agricultural sector and the strengths of its linkages with the rest of the economy, unseasonal dry weather conditions and poorly distributed rainfall strongly impacted the agricultural sector, its main cash crops sub-sectors (tea and coffee) and, as a consequence, the growth of the overall economy. In the first quarter 2011, growth in the agriculture sector slowed by 5.7%, coffee delivery declining by 28%. For the first half of 2011, tea production fell by 16% year-on-year (World Bank, KEU, September 2011). World Bank estimates for Ethiopia indicate that with a 10% fall in crop and livestock production in the pastoralists’ areas in 2010/11, GDP growth would decline by 0.4 percentage points. Beyond the direct impact of drought on agricultural sector output, other major economic impacts stem from the reduced hydroelectric power generation and the subsequent reduced economic activity, increased operating costs⁶⁰, and higher inflation rates. The Global Facility for Disaster Reduction and Recovery (GFDRR) of the World Bank has estimated at 1 percentage point reduction in GDP growth in Kenya the combined impact of below normal rainfall, high food and fuel prices (GFDRR 2011).

Figure 44:
Hunger Hotspots (QIV 2011)



Source: IPC Country teams, FEWS NET for Ethiopia and Djibouti., downloaded from http://www.disasterriskreduction.net/fileadmin/user_upload/drought/docs/FSNWG%20Update%202011-4.pdf

3.3 Trends and Prospects for Food Supply in the context of the Global Food Price Hike

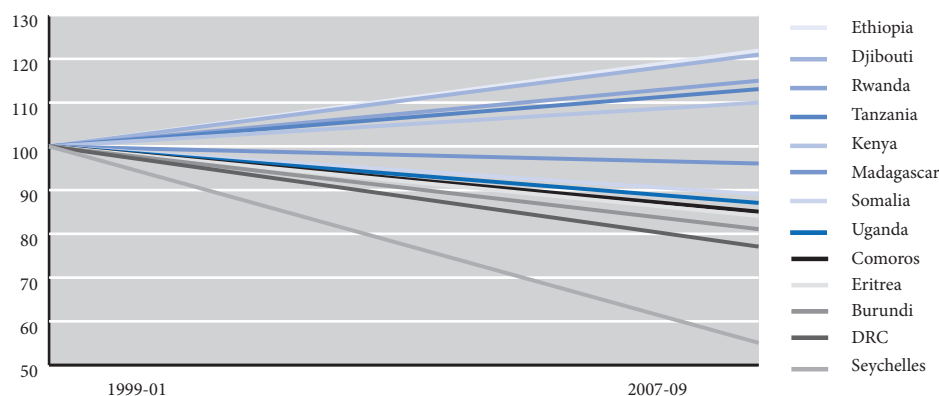
3.3.1 A Faltering domestic agricultural production, more accentuated in the food sub-sectors

Food production in the region expanded in the 2000s. However, because of a rapidly growing population, this often translated into only stagnant or even falling food production on a per capita basis (Figure 45). Only four countries – Ethiopia, Djibouti⁶¹, Rwanda and Tanzania were able to boost levels of output per capita across the sub-sectors, with Rwanda out-performing the whole region in cereal cropping (both Ethiopia and Rwanda also maintained a steady growth of the cash crops, namely tea and coffee). Three countries - the Seychelles, DRC and Burundi - experienced an especially sharp decline

in food production per capita in excess of -20 percent (in the case of the Seychelles, in excess of -40 percent). These examples illustrate how production can have a differential impact according to a country's capacity to pay for food imports: for the Seychelles, with its high average income per capita, the production shortfalls did not translate in an appreciable increase in food insecurity, whereas in Burundi and DRC, with close to 70 percent of the population living under the poverty line, it has led to a sharp increase in these countries' vulnerability to external food price shocks, such as those seen in 2007-8 and 2011.

Figure 45:

Food production per capita, 1999-2001 average vs. 2007-2009, EAR 13 (2001=100)



Source: FAOStat online

Regarding the composition of the production shortfalls, the production of cereals, beans, pulses, cassava, plantains and other roots and tubers (which are the main staple foods around the Great Lakes region) all underperformed in the 2000s. From the mid-2000s, cereal yields stagnated in Tanzania and Uganda and fell in all major producers except Ethiopia, which saw some increases in output.

Another feature of regional production is a very high degree of seasonal variability among marginal producers in countries such as Djibouti, Eritrea and Rwanda, with the latter experiencing a steep increase in 2009, harvesting 60 percent more than its 2004 level. Overall, most African countries became net food importers by 2003, reversing a period of high surplus in the 1980s (UNCTAD, 2006).

Growing commercial imports have not been sufficient to compensate for the shortfalls in production.

3.3.2 Underinvestment in Agriculture and the Uneven Success of Agricultural Research and Development

One of the main reason for this declining production trend is the chronic underinvestment in agriculture across the sub-region triggered by the Structural Adjustment Programmes of the 1980s that called for the withdrawal of state support to farmers. This underinvestment acutely affected research and development and agricultural extension services, leading to a sharp decline in the use of modern inputs such as fertilizers and improved seed varieties. The provision of essential infrastructure such as irrigation and roads also stalled. Public marketing boards were dismantled while subsidies on credit and imported inputs were phased out. In addition, the devaluation of most local currencies against international currencies inflated the prices of the imported inputs⁶²; in some countries, four-fold increases were registered within two years (see Mkumbwa, 2010). As a result, SSA was left far behind the rest of the developing world in terms of fertiliser use (13 kg per hectare of arable land against 94 kg (FAOSTAT data⁶³). On the average, only 1.2 percent of the irrigation potential was mobilised in the EAC against a world average of 18.5 percent in 2007. This indicator was as low as 0.1 and 0.8 percent in Uganda and Rwanda respectively, the highest being in Burundi (1.6), and in Kenya and Tanzania, both at 1.8 (FAO Statistical Yearbook 2009).

Although the damage done to the agricultural sector was serious, there are some good examples of innovation and success that predate structural adjustment. With the right policy choices, countries in the region can once again begin rebuilding the sector, which is the bedrock for economic transformation. For example, Kenya was the beacon of modern maize development in the sub-region where “a combination of factors –primarily the sustained investment in research and development, dedicated scientists, and supportive public policies – all contributed to maize-driven improvements in rural livelihoods and national food security in the region” (Smale and Jayne, 2010: 40).⁶⁴

Policy-makers may also draw some lessons from the large yield differential observed between Uganda and western Kenya, which has been associated with less access to labour, poorer soils, and premature harvesting by less well-endowed farmers (Fermont et al., 2008). Access to on-farm and off-farm labour-saving devices allowed enterprising farmers to plant the high yielding, mosaic-resistant varieties (Nweke and Felix, 2002). Removing these constraints and bottlenecks will help expand the contribution of smallholders’ cassava-maize based farms to national and regional food security.

3.3.3 The 2007 – 2009 and 2011 Food Price Spikes

The World Bank Commodity Price database for Low and Middle Income Countries recorded continuously rising prices between 2007 and mid-2008 and early 2009 for all major food commodities and agricultural inputs (Figure 46). Besides energy-based commodities, the highest price rises were in oils, fats and grains. Rice prices are still well above their 2007 international levels and the price of vegetable oils (palm oil, soybean) almost tripled between

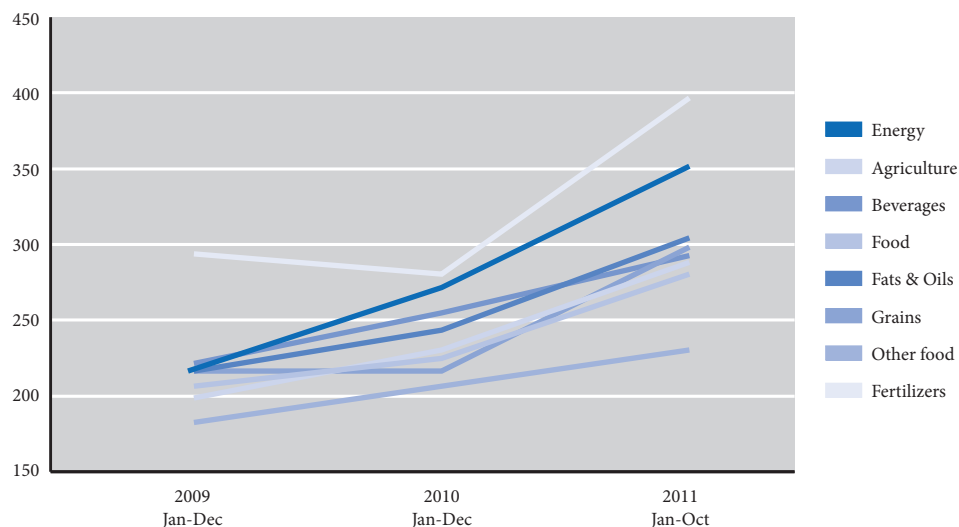
January 2005 and July 2008. In comparison, increases for other food prices – i.e. sugar and meat – were much lower but still up by 30 to 50% over the same period. Prices accelerated sharply again in 2010, reaching new peaks in mid-2011. Although prices of all major food commodities are projected by the World Bank to decrease for the next three years from their 2011 peaks, they will still remain well above 2000 prices measured in constant US\$ terms.

The price increases for energy and derived commodities such as fertilizers have been consistently the highest amongst all commodity groups and are projected to double their 2000 levels in the next two years. This will have significant impact on any developmental scenario

for the low-input agricultural African economies. All forecasts expect food prices to remain high in the long run, mainly as a result of continuously rising demand for biofuels and structural factors related to population and income growth (OECD-FAO, 2009; USDA, 2009).

Figure 46:

Trends in commodity price indices for Low and Middle Income Countries, 2009 to 2011 (2000=100)



Source: World Bank Commodity Price Pink Sheet

3.4 Transmission of Global commodity prices to local markets

THERE IS SOME, albeit limited, evidence of transmission of global prices to domestic markets for agricultural products in countries of the sub-region. The “spatial price transmission” concept tells us that imports and exports will take advantage of price differentials in spatially separated markets and move to locations with higher returns. In a free-trade environment, trade flows would equalise national and international prices of a commodity expressed in the same common currency. Under these conditions, “price transmission” is considered as complete (OECD-FAO 2010:55). However, in practice, trade is not free and transport and informational costs between markets, as well as differences in product attributes and consumer preferences, also impact on

demand and consequently on prices. Domestic policies are also key, such as: 1) policies at the border such as import or export restrictions, variable tariffs or export taxes, sanitary and phyto-sanitary inspection measures; 2) international pricing schemes, such as minimum support prices or intervention policies; 3) market structures as they are shaped by the interplay of national policies and private interests.

A study by IFPRI over the period June 2007 to June 2008 showed that in a sample of 83 markets in 12 SSA countries, food price increases were greater in landlocked countries – except Mali and Rwanda, than in coastal ones. Large mass and landlocked countries of Eastern Africa, poor

infrastructure, transport and communication services compound the effect of the oil and other fuel increase to give rise to large marketing margins (Minot, 2011). The largest increases in domestic food prices occurred in the most regionally (maize: 87 percent), or internationally (wheat: 65 percent; rice: 62 percent) tradable of the staple food commodities. The smallest increases occurred in plantains (9 percent), cassava (12 percent), and beans (41 percent), which are more confined to cross-border trade.

In SSA as a whole, staple grain prices are almost universally higher than the world prices of the same commodities, in some cases significantly higher. For example, the average world price of wheat was \$167 per ton, but the Ethiopian wheat price averaged \$261 per ton. “The only exceptions were the price of maize in Kampala (Uganda), which averaged 24 percent below the world price, and the price of maize in Songea (Tanzania), which was approximately equal to the average world price” (Minot, 2011:17). Moreover, domestic prices can be substantially more volatile, as is the case of maize and wheat in Addis Ababa.

3.5 Policy Responses at the national and sub-regional levels

THE POLICY RESPONSES and measures adopted by countries to address the 2007-2008 and the 2010-2011 food price crises aimed at a dual goal: improving access to food and increasing food supply. The weights of each goal element reflect the explicit or the implicit food security strategy employed by individual countries: food self-sufficiency or food self-reliance. The former implies that sufficient domestic production should meet a substantial part of national consumption requirements. But even in countries that are net food exporters, malnutrition affects substantial number of households. Food self-reliance, on the other hand, reflects a situation in which sources of food are determined by international trade patterns. Countries

that have a comparative advantage in non-food export crops can, then, use their export revenues to import staple food. In both cases, the success of these strategies depend, to a large extent, on the responsiveness of producers to price incentives or on the ability of decision makers to use income gains and policy measures for an efficient resource allocation to purchase food on the international market and to guarantee an equitable access of consumers to food as well (FAO 2003: 20). Therefore, the policies combine measures in the areas of social protection, finance and credit, agriculture and infrastructure, land and institutional development, trade, taxes and tariffs.

3.6 Policy Responses at the national level

Improving access to food: consumption subsidies and food safety nets

AS NOTED BY an FAO’s assessment (FAO 2011c), during the 2007-2008 crisis most of the **consumer-support measures** used by the governments were extensions of already existing instruments and were further reinforced during the financial and economic crisis. The short-term measures taken as a rapid response were meant mainly to expand coverage and benefits so as to immediately improve the situation and protect consumers. These

measures have been continued with a lesser intensity or institutionalization since late 2008 and early 2009. Safety nets, market control, tax reductions and health and nutrition interventions constitute the menu of policy options for consumption protection.

Safety nets consist of cash transfers, direct food assistance in the form of food stamps or vouchers and school

feeding programmes, as well as increased disposable income for vulnerable groups in public works. Intensive nutrition interventions are also included in programs, particularly in school feeding programs such as that catering to well over 60,000 children in Kenya during the crisis. As noted by the FAO Eastern Africa Consultation Meeting on Policy and Programmatic Actions, the previous food crisis of 2007-2008 demonstrated that safety nets were effective in mitigating the effects of high food prices on poor or vulnerable populations. In their broader dimension, safety net programs also include the provision of different packages of support to the rural producers, such as public works schemes, sustainable land management (SLM) projects that are most relevant for reducing the root cause of drought in most of these countries; inputs distribution targeted at farmers (e.g. Burundi, Kenya, Rwanda and Somalia); and the provision of nutritional and health services to the vulnerable groups of the population in Somalia and Uganda. Within the region, safety net programs were already well-established in Ethiopia. Since 2005, programs have been upgraded into productive safety net programs with the further mandate of providing agricultural inputs and assisting in establishing income-generating activities for the vulnerable population. In Rwanda and Kenya, safety nets also include weather index based insurance schemes for farmers aimed to protect farmers against loss of harvests from recurrent extreme weather events such as droughts, floods and landslides.

Most governments have resorted to **stock management** from the first months of the 2008 in order to ensure the availability of food on the domestic market. The development of strategic food reserves is being considered by all governments and RECs as a source of emergency support and in some cases with the intention of stabilizing prices. Ethiopia, Kenya, Rwanda and Tanzania have established or are expanding their strategic food reserves.

Simultaneously, Djibouti, the DRC, Kenya and Tanzania tried, with mixed success, to pre-set prices or freeze retail prices of wheat and maize.

Trade or fiscal measures include import tariff reductions, export restrictions or bans, VAT and other taxes reductions, public food reserve utilization, price control, food imports to increase public stocks and the selling of grain and flour at subsidized prices, etc. These responses have been aimed at preventing the transmission of high global food prices to the domestic markets as well as at reducing prices for consumers. Perhaps owing to the severity of the price hikes, only Ethiopia, among the countries of the sub-region, have implemented all the measures indicated under this category. DRC, Kenya, Rwanda, Tanzania and Uganda implemented the suspension or reduction of import tariffs and the removal of VAT and other taxes.

At the onset of 2008 crisis, most of the countries had reduced or eliminated food **tariffs or taxes**. Late 2008, some reduced VAT, not only on food items but also on agricultural equipments. In Ethiopia, food, grain and flour (and fuel as well for a short period of time) were VAT exempted. In addition; there was an increase in the salaries of public servants. In Uganda and Rwanda, measures were taken in order to ensure **youth employment** as a way to professionalize agriculture and boost productivity and rural entrepreneurship with a pool of more skilled labor.

Health and nutrition interventions are aimed at improving food utilization. These programmes are mainly focused on children and mothers through micro-nutrient fortification, fortified food and vaccines. However, there are still major gaps, with large variations in stunting and wasting rates within countries. And in most countries in the region, they are still stand-alone activities, fragmented from food security policies.

Increasing food supply: input subsidies and stock management

The policy objective is to stimulate a rapid supply response in food production and to smooth price volatility on the local food markets, by increasing the income of smaller producers and improving their living conditions. The most common response has consisted in implementing **agricultural input support programmes** - in particular for fertilizers and seeds. All the countries in the sample provided seeds to farmers either at a subsidized price through input vouchers issued by the governments (Rwanda, Tanzania) or free of charge.⁶⁵ In Rwanda, improved seeds for priority crops were provided freely in accordance with the national Crop Intensification Program. In Ethiopia, the Government increased fertilizer imports by about 60 percent in 2008 from the previous year.

Alleviating the constraints facing the smallholder producers will enable them to exploit the opportunities created by rising food prices and to increase food production. Therefore, most of the countries have taken actions to improve the **access of small producers to finance and credit**. Governments provided public funds and support through public and commercial banks. Although agriculture-oriented insurance schemes have already been introduced in the sub-region (Ethiopia and Tanzania), they were not considered per se as part of the governments tools for reducing the risks to smallholder farmers.

Substantive **efforts to strengthen institutions** have been made through supporting farmers' organizations, strengthening public institutions, or and creating a new institutional framework for the agriculture sector and agri-business. Recognizing the constraint of insufficient investment, African political leaders have committed to scaled-up public sector expenditure to support agricultural development. The Maputo Declaration (2003) of African Heads of State set a target of 10 percent of public expenditure being allocated to the agricultural sector. The African Union's New Partnership for Africa's Development (NEPAD) was tasked with helping governments to achieve this goal, and launched the Comprehensive African Agriculture

Development Programme (CAADP). By emphasizing the role of public expenditure, the Maputo Declaration also served to draw attention to the decades-long decline in overseas development assistance (ODA) to agriculture.⁶⁶

Most countries in the sub-region also signed the CAADP (Comprehensive Africa Agriculture Development Programme) compact (a NEPAD Policy tool for boosting agriculture productivity and production in Africa) and use it as a platform for policy reform, institutional strengthening and increased budget allocation to the agriculture sector. Rwanda was the first country to sign up a CAADP compact in 2007. In line with the Maputo Declaration (2003) target, Burundi has increased its budgetary allocation for agriculture from 3 percent to 12 percent of its national budget. It has also rehabilitated existing irrigation schemes that were not functional and provided more than 200 water pumps to farmers engaged in rice production. To enhance access of smallholder farmers to the market, storage facilities (for reducing post harvest losses) and new public market places have been built and rural roads improved in Rwanda and Ethiopia, which have also exceeded the Maputo target.

Some countries have redesigned or set up **national price or policy information collection system**. Cross-border trade of agricultural is being monitored in the sub-region through a joint initiative by FEWS NET, WFP, and FAO.

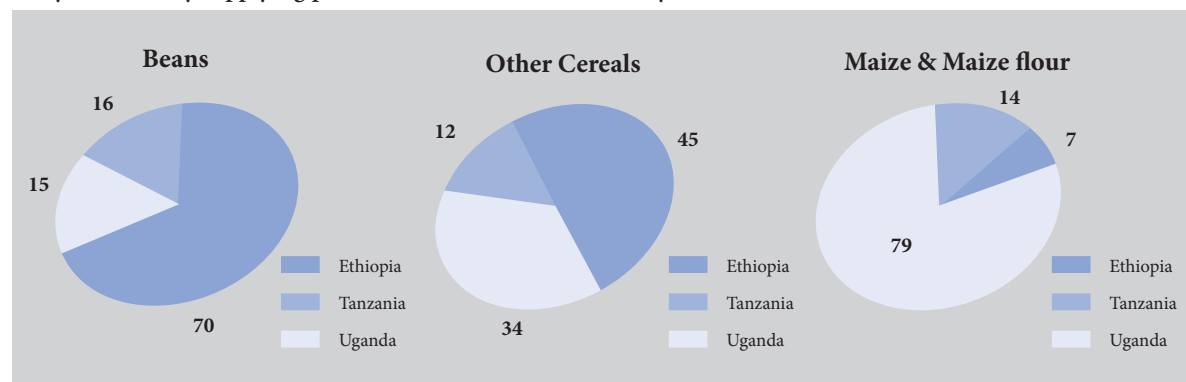
Land and/or water scarcity remain particular constraints to almost all the countries of the sub-region. Rwanda has enacted a **new land policy** with the aim of land planning, and consolidating and securing land holdings for multiple purposes (land allocation for reclamation, investment and cultivation). To enhance employment in the agricultural sector, in 2008 Rwanda introduced incentives for youths to return to agriculture and went through a land consolidation programme supported by a food basket strategy. Uganda has supported diversification of income sources through farm and non-farm activities.

The **banning of grain exports and the release of public stocks and food imports as instruments to influence domestic supplies of food and prices** was used in Ethiopia, Tanzania and Uganda (FAO 2011b). However, despite the export bans of cereals, there were significant volumes of staples traded across markets from the surplus countries (Ethiopia, Tanzania, Uganda) to deficit countries (Kenya, North and South Sudan). The informal cross-border traders can be reactive enough so as to substitute for lower

supplies from Uganda- a key traditional exporting country. This happened in the July-August 2011 when acute shortage of staple food stocks (maize) arose from delays in harvest in Kenya in combination with the late start of season in Uganda, the main maize supplier to Kenya. This led to unprecedented price increases in most cross-border markets which provided sufficient incentives to cross-border traders (FEWSNET/FAO/WFP (2011) (Figure 47).

Figure 47:

Kenya and its key supplying partners – Relative shares of Kenya's cross-border trade



Source: based on data from FEWSNET/FAO/WFP (2011)

Some countries switched measures over short periods of time to adapt to a changing external environment, weather shocks or to accommodate stakeholders' claims. For example, between June 2008 and July 2011, Kenya first reduced import tariffs on wheat from 35 to 10 percent in 2008 and then increased the duty again to 25 percent in 2009, because of larger domestic wheat production and falling international prices. The Government then reduced it to 10 percent again (for hard wheat and barley) in 2010, effective until June 2011. Rwanda decreased the taxes on food products in 2008, but the year after, on par with other EAC member countries, it imposed higher taxes on agricultural products [such as sugar] that are produced in sufficient quantities within the Eastern

African Community (EAC) to encourage local markets and discourage import from non-EAC countries (FAO 2011c). In an example of regional trade cooperation, some common trade policies of EAC member countries were implemented under the Eastern African Common Market Framework. In spite of the many medium- to long-term policy decisions aimed at providing production support and of the renewed interest in export earnings, only the Tanzanian government has been really promoting export through a systematic approach.

3.7 Policy Responses at the international level

THE EASTERN AFRICAN Community has developed a very comprehensive Agricultural and Rural Development Strategy (CAADP) (2005-2030), as a CAADP-Plus Strategy. In addition to the CAADP four pillars – i.e. Land and Water Management, Market Access, Food Supply and Hunger, and Agricultural Research, the EAC Strategy defines, among others strategic interventions, trade and agro-industry development through regionally integrated value chains. There is also an important role for EAC in supporting its regional partner as a think tank for harmonizing policies, promoting policy dialogue on regional dimensions of food and nutrition security, and identifying investment opportunities.

The UNECA has been advocating for a systemic and coherent approach to address food insecurity through the establishment of multi-institutional platforms. Many elements of the recommendations are central to the Programme on Food Security for Eastern Africa developed as a joint initiative of the International Conference on the Great Lakes Region (ICGLR), the Economic Community

of the Great Lakes Countries (CEPGL), the Eastern African Community (EAC), and the Intergovernmental Authority on Development (IGAD) as well as COMESA building on their respective food security related policies. The four following components of the Programme were approved at the 14th meeting of the Intergovernmental Committee of Experts (ICE) on 15-18 March 2010 in Kigali, Rwanda: (a) Marketing and trade development for agricultural, livestock and fisheries products; (b) Research and development for value addition and inputs systems including technology generation and transfer; (c) Sustainable Natural Resource Management; and (d) Nutrition and Social Protection, including safety nets. Key partner institutions include representatives from the participating RECs/IGOs and pilot countries, research institutions, and relevant Eastern Africa organizations that undertake food security-related activities within the region, members of the civil society as well as development partners and foundations. It is expected that the Programme document will be validated at the highest level in 2012.

3.8 Conclusions and some Policy Implications

EASTERN AFRICAN COUNTRIES must see the current food crisis as the moment to rethink and act strategically to ensure food security in the region. They need, more than ever, to translate their policies at the country and sub-regional levels into action, so as to initiate policy reforms that will facilitate national and collective security through the strong growth of the agricultural sectors and markets. However, a basic prerequisite is the control of strategic resources and of their proper allocation in a coordinated manner at the national, sub-regional and regional levels. Some of the wealthiest countries in the world and leading global businesses are responding to the new configuration of global food commodities markets by purchasing or leasing land, abroad

and especially in Africa, with the view to ensuring their own food security.

To make the best of the food crisis to improve food security and promote a competitive agricultural sector, the following principles could be articulated as framing pillars: acting regionally to better serve country and the interests of the local communities; strengthening the links between nutrition, agricultural development and social policies; and achieving the right balance between export-oriented agriculture and locally oriented agriculture.

The various tools that governments have used so far to deal with the immediate impact of the increase in food

prices have included macroeconomic – fiscal and trade – regulatory and social policies that may impede, over the medium term, the emergence of a new agenda for agricultural development in Africa. Indeed, the short term policies should be balanced enough to yield equitably distributed benefits between farmers and non-farmers, urban and rural dwellers, and to promote the development of commercial export-oriented agriculture and of a smallholder agriculture that can ensure a sustainable supply of affordable surplus in basic food commodities for national and regional markets. Maintaining interventions in high potential agro-ecological zones and focusing on anti-poverty interventions in rural areas are other priorities. Engaging the poor in the production of food-for-sale in the local market will not only create localized income, but also contribute to assuring the quality of the diet available for local consumption. Improving the productivity of small farmers has a ripple effect that spreads benefits throughout poor rural communities, and stimulates urban economic activity as well.

Some specific recommendations/implications could be:

1. Promoting greater national and regional investment to increase agricultural productivity and diversify agricultural production

If agricultural growth is to be re-launched in Africa, it is imperative to harness high food prices to increase investments, boost agricultural productivity and diversify production. Incentives are needed to remove the structural constraints facing agriculture. The supply-side response should be framed in regional as well as in national contexts. This requires promoting regionally integrated value chains and open trade in staples, dairy products and farm inputs, among others; and reducing transaction costs between neighbouring countries. Special attention will have to be paid to the livestock value chain in pastoralist communities in all IGAD member states and further promotion of the fisheries sector be considered. This also needs further investment in research and development on seeds' improvement and increased supply of inputs

(both chemical and organic fertilizers). The private sector, including small and medium size farmers and food processing businesses, also needs strengthening.

2. Strengthening the Links between Nutrition and Agricultural development

Food prices are likely to remain high for some time and may have a long lasting negative effect on growth if proper action is not taken to shield the most vulnerable groups, especially women and children. Remaining malnourished for more than two years increases the risks of stunting in children. On top of physical growth, stunting impairs mental potential and becomes an inherited genetic marker. To start tackling this challenge, the solution resides less on the demand side and more on the supply side. Development of the livestock and fisheries value chains can also greatly contribute to improved nutrition and calorie-based diets. In addition to integrating nutritional dimensions into any major food production programmes, food and nutrition surveillance systems should be organised in a way that they can inform decision-making at all levels, not just government policymakers. Such information can provide the elements of predictability and accountability that are required for a human rights-based approach to developing national government responses to the food crisis.

3. Encouraging greater intra-regional trade and development of markets

The lack of efficient information flows on price and quantities of agriculture produce amongst key players both at national and sub-regional level is seen as a major stumbling block to market access. Countries as well as RECs/IGOs need to strengthen harmonization of data collection and define related methodologies. Market information systems (MIS) such as e-soko in Rwanda and RATIN in the Eastern African sub-region play a key role in helping farmers in enhancing their livelihoods and agriculture production. The use of these MIS is facilitated by mobile technologies and be associated with other features such as on-line transfers and payments. Two other aspects which are key to market development and access are the

improvement of infrastructure and harmonized regulatory frameworks in terms of tariffs, customs procedures and most importantly ‘standards, sanitary and phytosanitary (SPS) norms’. It is expected that the implementation of the provisions of the Eastern African Common Market Protocol will help to focus on these aspects for increased regional integration and intra-regional trade. Complementing the production and the regional trade initiatives, regional risk management schemes could be established in order to hedge against market and climate and weather shocks. Among such schemes, the most promising are regional free agricultural commodity fairs; strategic grain reserves; commodity exchange and crop insurance schemes.

Notes

56 The intensity of food deprivation indicates how much food-deprived people fall short of minimum food needs in terms of dietary energy. It is measured as the difference between the minimum dietary energy and the average dietary energy intake of the undernourished population (food-deprived). The intensity of food deprivation is low when it is less than 200 kilocalories per person per day and high when it is higher than 300 kilocalories per person per day. The greater the food deficit, the greater the susceptibility for health risks related to undernutrition.” (FAOSTAT – Notes on Depth of hunger- Online data file)

57 <http://www.fao.org/economic/es-policybriefs/multimedia0/protracted-crisis-map/en/>

58 This statement is made with certain caveats. In Rwanda, for instance, some parts of the country were in a ‘stressed situation’ (FEWS.Net, May/June 2011 Food Security). On 6 July 2011, Tanzania’s Agriculture Minister Tumanne Maghembe announced a ban on crop exports for six months to prevent the food shortages being experienced in many parts of the region. Maghembe noted that “generally there is food surplus” in the country, but pockets of food insecurity existed in several regions, including Singida, Dodoma and Shinyanga, as well as northern regions of Arusha and Tanga in the east (IRIN august 2011). Furthermore, a WB funded project on Emergency food security and unemployment support through cash for work started in 2011.

59 See Refugees International, Fields Report 2011 South Sudan: Displacement Plagues World’s Newest Nation., December 15, 2011; Horn of Africa: Not the Time to Look Away, December 13, 2011.

60 According to Kenya Manufacturing Association, generator power costs alone could account for some 40% of overall costs.

4. Embracing a more ambitious social protection agenda.

Finally, as argued in the section III of this report, now that a decade or more of sustained growth has produced a more propitious economic environment for most countries in the region, there is a need for governments to slowly adopt more comprehensive and ambitious social protection agendas. This would go beyond the idea of providing targeted ‘safety nets’ and move more towards a rights-based universalistic approach to social assistance. Food security would be enhanced through upscaling such schemes by guaranteeing modest incomes to the poorest members of society.

61 The figures for Djibouti are most likely associated with inaccuracies in the data and associated with trade in food crops, rather than production per se – as noted earlier, with the lowest amount of amount of arable land per capita in the world, local food production is negligible.

62 South Africa apart, SSA imports 90 percent of its agricultural chemical fertilizers in spite of its huge deposits of natural phosphates across the continent.

63 Tanzania is still at the SSA’s average level while Uganda is at 1 kg/ha and Kenya ranks well above double the sub-continent’s average.

64 The public program was comprised of complementary investments in agronomic research, extension, seed distribution systems, a dense transport network, marketing board, and pricing policy.

65 The other countries in the sample are: Burundi, the D.R.C., Ethiopia, Kenya, Madagascar, Rwanda and Tanzania.

66 See www.resakss.org for further information on country public sector expenditure supporting agriculture

Conclusions -Moving forward...

4

4.0 Introduction

DESPITE THE TROUBLESOME global context, this report has presented a fairly optimistic overview of both the performance over the course of 2011 and the prospects for the EAR-13 region for the coming years. This broad optimism is shared by the other organisations/companies that provide forecasts for regional growth performance – currently, UNDESA, the African Economic Outlook, the World Bank the IMF and the Economist Intelligence Unit. Of these five sets of forecasts, four are based on underlying macroeconomic models – only the Economist Intelligence Unit provides estimates which are qualitative

in nature.⁶⁷ Table 20 provides summaries of these different sets of forecasts for the region for 2011-12, available in February 2012. In some cases, as can be seen, there is quite a large dispersion in some of the estimates for both 2011 and 2012. This is particularly the case with Eritrea, but is also true of Ethiopia and Madagascar. It is also notable that the IMF and World Bank are on average providing less optimistic (or more cautious) forecasts than the AEO and EIU (UNECA weighted estimates were given previously in Figure 1.

Table 20:

Comparison of Forecasts and estimates for regional GDP growth, 2011-2012

2011 estimates	Release date	BURUNDI	COMOROS	DJIBOUTI	DRC	ERITREA	ETHIOPIA	KENYA	MADAGASCAR	RWANDA	SEYCHELLES	TANZANIA	UGANDA
AEO	Jun-11	4.5	2.5	4.6	6.7	7.9	10.0	5.3	0.6	6.5	4.0	6.9	5.6
EIU	Nov/Dec-11	4.0	2.5	4.6	6.5	17.0	7.5	4.2	1.0	7.2	5.0	6.4	6.6
IMF	Sep-11	4.2	2.2		6.5	8.2	7.5	5.3	1.0	7.0	5.0	6.1	6.4
WB	Jun-11	4.1	2.3		6.5	3.4	7.7	4.8	2.6	7.0	4.0	6.5	6.4
UNDESA	Nov-11	3.5	1.5	5.4	4.3	2.9	7.4	4.7	1.6	5.8		6.3	5.6
Average		<u>4.1</u>	<u>2.2</u>	<u>4.9</u>	<u>6.1</u>	<u>7.9</u>	<u>8.0</u>	<u>4.9</u>	<u>1.4</u>	<u>6.7</u>	<u>4.5</u>	<u>6.4</u>	<u>6.1</u>
2012 forecasts													
AEO	Jun-11	5.2	3.2	5.1	6.4	6.1	8.6	5.5	2.0	7.0	4.5	7.3	6.9
EIU	Nov/Dec-11	4.5	2.7	4.9	6.3	6.0	8.0	5.9	4.0	6.5	4.2	6.9	5.1
IMF	Sep-11	4.8	3.5		6.0	6.3	5.5	6.1	4.7	6.8	4.4	6.1	5.5
WB	Jun-11	4.6	2.3		6.0	3.5	7.2	5.0	3.9	6.8	5.0	6.9	6.6
UNDESA	Nov-11	4.5	2.0	6.3	3.5	3.2	8.1	5.7	4.7	6.3		6.9	5.1
Average		<u>4.7</u>	<u>2.7</u>	<u>5.4</u>	<u>5.6</u>	<u>5.0</u>	<u>7.5</u>	<u>5.6</u>	<u>3.9</u>	<u>6.7</u>	<u>4.5</u>	<u>6.8</u>	<u>5.8</u>

Sources: AEO/EIU/IMF and WB, UNECA calculations

In a context of a global economy which is expected to grow at 3.3% in 2011 and by 2.6 percent in 2012 (Table 1), these results are good ones, though that evaluation must be tempered by the consideration that the high rate of demographic expansion in the region is high, reducing per capita rates of growth substantially. In line with earlier reports (UNECA, 2010), our report also stresses important progress in terms of regional integration within the Eastern Africa region. Tariffs have been coming down across the region, and regional trade has, as a consequence, picked up. Moreover, investment patterns are also beginning to reflect new regional realities. As presented in Section 2, there is a lot of anecdotal evidence (increasingly backed up by statistics) that investors are starting to target regional, rather than national markets- one of the true payoffs from regional integration. This is particularly so for the EAC, the most advanced regional integration project in the EAR. The case is easily made for deeper regional integration - national market size of individual

states within the sub-region are simply too small to be viable in a global economy increasingly dominated by large regional groupings such as the EU, NAFTA, and MERCOSUR, and with the growing protagonism of the two Asian giants, India and China.

Together, the regional market of the EAC reached a size of US\$ 82 billion in 2011, according to UNECA estimates. On a global scale, this is still small. But it does enhance the possibility of attracting both international and national investors in industries where fixed costs are high, and there is a need to sell to larger numbers of prospective customers. Similarly, on the supply side, there are a number of important initiatives regarding collective infrastructure projects and energy security, such as the recently completed power-sharing agreement between Djibouti and Ethiopia.

In line with the conclusions of our special thematic section on food security, regional integration takes on an added urgency against a backdrop of persistent food crises which have been evident in the region. As stressed in the introduction, food security on a national basis is a chimera when countries are so liable to be affected by drought and climate change. More intra-regional trade

in agricultural produce could positively impact on food security across the whole region, but this requires greater efforts not only in removing tariff barriers, but also in the elimination of Non-Tariffs Barriers (NTBs) and reduction of infrastructural bottlenecks which continue to impede the free flow of goods across the region.

4.1. Constraints on Faster Growth

As reflected in Box 1, although regional growth performance has been more than respectable over recent years, political leaders and policymakers have fixed more ambitious goals, with a number of countries explicitly stating the goal of becoming middle-income countries within this decade or early next decade. What are the constraints that need to be overcome to make such a goal realisable? Despite many of the up-beat messages included in this report, the region faces a long list of bottlenecks and potential constraints on economic growth. It is crucial that policymakers focus in on the major constraints and bottlenecks to growth in the region if growth is to be sustainable.⁶⁸ In this report, we have focused more on the short-to-medium term bottlenecks. But that does not mean that the long term ones are unimportant – on the contrary, they represent the major developmental challenges. Chief among these are a) excessive dependence on a vulnerable agricultural sector b) low investment levels in some countries of the region c) addressing the infrastructure deficits, d) creating more (and better) employment opportunities, particularly for the youth, e) addressing technological deficits and f) ecological and climate-change imposed constraints on growth. Taking each of these points in turn:

- a) **Dependence on a vulnerable agricultural sector** – for most of the regions' economies (with the exceptions of Seychelles and Djibouti), agriculture forms the backbone of the economy, exposing countries to the vagaries of weather.⁶⁹ Moreover, although progress has been made in some countries of the region⁷⁰

, fast productivity growth in the sector has proved elusive. Particularly at a time of climatic change, it is necessary for regional economies to accelerate the diversification away from dependence on the agricultural sector. This implies developing more strategies for the rural diversification of incomes, as well as supporting policy measures to smoothen the transition towards more urbanised economies (as noted earlier in this report, the region is one of the least urbanised in the world).

- b) Despite very significant improvements over the last decade, in some countries of the region there is still a need to raise **aggregate investment levels**.⁷¹ Spence (2011:74) notes that, from the evidence of thirteen sustained-high-growth economies as a benchmark, it appears that investment needs to be in excess of 25 percent of total output or GDP to sustain fast growth.⁷² This figure is in line with the LDC's 'Brussels' Action Plan' objective of 25 percent of GDP dedicated to investment. Beyond the Seychelles (which is not an LDC), the countries which are estimated to reach or surpass this target in 2011 include DRC, Tanzania, Uganda, Ethiopia, and Rwanda (Table 21). Burundi, Comoros and Madagascar are the countries which are furthest from reaching this target, though it should be noted that Madagascar's investment rate has fallen sharply against a backdrop of political problems which may not be protracted – investment rates may therefore be expected to recover.

Table 21:**Total Investment as a Share of GDP**

Country	2005	2006	2007	2008	2009	2010	2011	Estimates Start After
Burundi	10.8	16.3	17.5	22.3	22.1	20.9	20.6	2009
Comoros	8.3	8.6	10.0	12.8	11.1	15.4	16.5	2010
DRC	13.8	13.2	18.2	22.4	19.4	27.1	29.3	2008
Eritrea	20.3	13.7	12.7	12.7	9.3	9.3	10.0	2006
Ethiopia	23.8	25.2	22.1	22.4	22.7	22.3	25.5	2010
Kenya	16.9	17.9	19.1	19.5	19.4	21.9	24.7	2010
Madagascar	23.8	25.0	28.3	40.9	32.2	25.1	19.6	2010
Rwanda	20.9	19.7	20.2	23.5	22.4	21.9	25.1	2010
Seychelles	35.4	30.5	29.5	41.5	36.9	40.3	40.5	2009
Tanzania	23.9	26.4	28.7	29.7	29.4	29.0	28.8	2010
Uganda	22.4	21.2	23.7	23.0	23.5	24.3	25.5	2010

Source: International Monetary Fund, World Economic Outlook Database, September 2011

Note: Figures in red are under the Brussels' Action Plan target of 25 percent of GDP investment rate.

c) On infrastructure deficits, there has been much progress recently as governments have embarked on major infrastructure plans and projects, particularly in the energy and transport sectors. Nonetheless, it will still require considerable time and adequate financing to compensate for the grave deficiencies accumulated during the period of slow growth and structural adjustment in the 1980s and 1990s. The emerging partnerships, particularly with China, have proved especially useful in strengthening the provision of infrastructure across the region. However, major bottlenecks still remain, such as Mombasa Port.

d) On employment, population growth puts strong pressure on labour markets for youth, particularly in an environment where decent work opportunities are in short supply (ILO, 2012:79). National surveys suggest that in countries like Uganda (where the last survey was carried out in 2005), the explicit unemployment rates are quite low, with youth and

adult unemployment under 5 percent. In much of the region, the key issue is the quality of employment more than quantity (lack of employment altogether). In Burundi, for instance, more than 85 percent of the employed youth are classified among the working poor. The creation of new, better quality, employment opportunities entails the encouragement of economic diversification into higher value-added activities, with a greater technological input. As argued in this report, at the same time it requires more active labour market policies, in terms of better regulation of pay and salary conditions. In other regions (e.g. in Brazil), minimum wage legislation has been part and parcel of the approach to reducing inequality and sharing the benefits of growth (Lemos, 2007; Barrientos et. al. 2010, OECD, 2011). This report argues that valuable lessons can also be learned from these experiences.

e) On technological capacity, the region has been the source of some highly successful innovations, such

as the M-PESA mobile phones payments system in Kenya.⁷³ Yet there is no escaping the technological ‘vulnerability’ of the region – in terms, for instance, of patents per capita, the Eastern African region is among the most technologically backward regions of the world. Improving this situation requires a complex set of policy innovations and reforms, tied in with better educational policies, particularly at the university level, as well as explicit policies to develop national innovation systems (see UNESCO, 2011). An example of new initiatives in the region to strengthen innovative capacity is the Rwanda Innovation Endowment Fund (RIEF), which was set up in April 2012 by the Rwandan government with the support of the United Nations Economic Commission for Africa. Its objective is to stimulate innovation in three priority sectors: agriculture, manufacturing and ICTs.⁷⁴

- f) Regarding the environmental constraints, people in the Eastern African region are probably more acutely aware of this than anywhere else in the world, as it is something which is consistently reflected in surveys of public opinion. Thus, whereas more than 80 percent of citizens of countries like Burundi, Djibouti, Kenya, Madagascar and Tanzania think that ‘global warming constitutes a serious threat’, in some western countries like the UK or United States the figure is closer to 50 percent (see UNDP, 2011). However, given the enormous resources that are consumed in trying to mitigate the impact of climate change, an effective response is dependent upon receiving adequate (and preferably grant) financing from the international community. Collectively, countries in the region need to lobby hard to ensure that they receive due financial support to tackle the complex and multiple problems caused by global warming, problems that they themselves did not create.

Beyond these medium-to-long term challenges exist a number of short-term risks for which policy makers need to be prepared, namely:

- 1. Dependence on external financing.** For most countries in the region, despite efforts to reduce aid dependency, the need for external financing is still strong (as reflected by the large current account deficits which some countries in the region sustain). This introduces a particularly important vulnerability at a time when aid budgets from traditional DAC donors are beginning to be cut back. While some of the shortfalls can be compensated for through greater finance from non-traditional partners (e.g. China, India), it is likely to act as a break on growth if aid budgets do indeed decline.
- 2. High probabilities of a double-dip recession in some OECD economies.** In November, 2011 the OECD revised its growth forecasts for 2012 for the Euro area down to just 0.2 percent. The Economist predicts stagnant GDP growth – i.e. 0.0% – in the largest European economy, Germany, for 2012. According to the OECD predictions, Italy’s economy will contract by -0.5 percent. Despite the growing interaction with new partners, many of the Eastern Africa region’s economies still display a quite high dependence on weak European and US export markets. This could prove to be a significant drag on growth, especially for economies such as the Seychelles (which is vulnerable through tourism) and Kenya (which is vulnerable through both tourism and its horticultural exports).⁷⁵ A downturn in Europe could also impact negatively on investment projects across the region, as investors put projects on hold.⁷⁶
- 3. A significant growth slow-down in some emerging economies.** The real danger, however, is that growth may also decelerate simultaneously in emerging markets, leading to a marked softening of commodity prices, on which part of the improvement in economic performance of the region has depended over the last decade.⁷⁷ There are already signs of a significant deceleration in China, India, Brazil and South Africa. In India, after achieving a record performance of 10.4 percent GDP growth in 2010, growth is expected to

fall to 7.2 percent in 2012, the slowest growth rate since 2004. In the third quarter of 2011, the Brazilian economy did not grow at all, and its GDP is estimated to growth by only 3.5 percent in 2011, less than half the 7.5 percent registered in 2010.

- 4. Inflation undermining economic growth.** Inflation risks inducing social unrest and undermining macroeconomic stability. Inflation peaked at 40 percent

in Ethiopia in the year to September 2011. In Uganda, inflation peaked in October at more than 30 percent. In Kenya it reached 19.7 percent in November. Although, as this report argues, goals for inflation have in the past been set at levels which may be incompatible with accelerated economic development, at rates in excess of 20 percent, there is a clear danger that inflation spirals out of control, causing a sharp deterioration in real incomes.

4.2. Reaching Middle-Income Status – A Realistic Goal?

In a publication which came out in 2007, Angus Maddison, the renowned economic historian, produced a comprehensive set of forecasts for the global economy. Maddison was relatively pessimistic about Africa's prospects. He highlighted what he perceived as the negative impact of rapid population growth, the pervasive incidence of infectious and parasitic disease, and low levels of literacy as key constraints on growth performance. Ultimately, however, he stressed the indigenous obstacles to improved performance, in terms of what he saw as poor economic policy management. He thus predicted an average economic growth of only 3% per annum from the period from 2008-2030, below that of Asia, Latin America, and barely more than that of Europe and North America – something which goes against the neoclassic logic that poorer countries should benefit from 'catch-up', in terms of being able to benefit from the availability of existing technologies, and should have the ability to grow faster than high income countries.

Subsequent events would seem to warrant a major revaluation of Africa's potential performance, however. As noted in a number of recent publications (Kenny, 2011; Raddlet, 2010), many indicators of human development in Africa have also improved dramatically – schooling, average life expectancy, etc - and at a much faster pace than that experienced by high income countries during their own surge towards development.⁷⁸ Moreover, assessments of Africa's macroeconomic management have

generally been much more positive than they were in the 1980s and 1990s (McKinsey, 2010; Raddlet, 2010). As in Latin America, macroeconomic performance in Africa improved strongly in the period from 2001 to 2008, after two decades of weak performance. Put simply, 'Afropessimism' may no longer be warranted.

As noted in Box 1, encouraged by the stronger economic growth over the last decade, many governments of the region have specifically set the target of reaching middle-income status within this or the next decade. Table 22 and Table 23 show the calculations about when countries in the region would reach middle-income status, as specified by the World Bank classification, which currently stands at a level of income per capita of US\$ 996.⁷⁹ Table 22 shows the estimated timeframe on the supposition that countries manage to achieve the same average growth rate as they obtained over the decade of the 2000s. The results are quite encouraging, in the sense that five regional economies (Rwanda, Ethiopia, Tanzania, Kenya and Uganda) would achieve middle income status between 2022-2030 – perhaps not as quickly as some governments would like, but still indicative that an important symbolic target is realistic. In view of the fact that two (Djibouti, Seychelles) of the 13 regional economies have already achieved Middle Income Status implies that more than half of the regional incomes would be middle income by 2030. More worrying is the considerable length that it would take some lower income economies with a much more sluggish average

growth performance over the 2000s to reach the same objective. This highlights the extent to which it is important to bring up average growth rates – the power of compound

growth means that even quite small differences in growth performance, over time, imply an enormous difference in terms of developmental outcomes.

Table 22:

Looking Forward – Achieving Middle Income Status on the basis of past performance

	2010 GNI per capita	Av. Growth per capita 2001-10	Years until achieving MIC status	Date by when MIC status will be achieved
Rwanda	540	5.06	12	2022
Ethiopia	380	5.91	16	2026
Tanzania	530	3.99	16	2026
Kenya	790	1.48	16	2026
Uganda	490	3.56	20	2030
DRC	180	2.02	85	2095
Somalia	211	0.52	297	2307
Burundi	160	0.31	591	2601
Comoros	820	-0.70	Nd	Nd
Eritrea	340	-2.61	Nd	Nd
Madagascar	440	-0.58	Nd	Nd
Djibouti	1280		already achieved	
Seychelles	9760		already achieved	

Source: UNECA calculations based on growth data from UNCTAD online database, per capita GNI figures from WB

Finally, it may be considered unfair to apply projections of growth performance on the basis of past performance for the 2000s. Some countries in the region, for instance, suffered political disturbances in the 2000s which provoked a reversal in their economic growth that hopefully will not repeat in the future. An alternative way of forecasting the dates for reaching MIC status is to base growth projections on the estimates provided by the IMF for the period from 2010-2016⁸⁰. Assuming that this set of

growth numbers is sustained beyond 2016, a rather different picture emerges regarding the speed with which EAR-13 countries will reach MIC status. More plausibly, in view of its higher initial income per capita and its more diversified economy, after Djibouti and the Seychelles, Kenya becomes the first economy to reach MIC status, followed by Comoros, Tanzania, Rwanda, Uganda and Ethiopia (Table 23).

Table 23:**Looking Forward – Achieving Middle Income Status on the basis of sustaining IMF forecast performance**

	2010 GNI per capita	Forecast 2010-16 growth per capita	Years until achieving MIC status	Date by when MIC status will be achieved
Kenya	790	3.90	6	2016
Comoros	820	1.60	12	2022
Tanzania	530	4.90	13	2023
Rwanda	540	4.60	13	2023
Uganda	490	3.00	24	2034
Ethiopia	380	3.90	25	2035
Madagascar	440	2.00	41	2051
DRC	180	3.40	50	2060
Burundi	160	2.80	65	2075
Eritrea	340	1.10	98	2108
Somalia	211	nd	Nd	Nd
Djibouti	1280	3.00	already achieved	
Seychelles	9760		already achieved	

Source: UNECA calculations based on growth forecasts from IMF (2011), per capita GNI figures from WB

On balance, therefore, there seems to be some reason for optimism regarding the sustainability of growth in the region. One final thing that has consistently handicapped regional growth performance in the past has been the existence of a number of failed or weak states in the region. It is worth highlighting a number of positive trends which give rise to some optimism. One is some tentative signs of stabilization in southern Somalia, as well as in the capital Mogadishu. Security concerns continue to be generated in South Sudan and the eastern part of DRC. But

it is worth pointing out that in all these countries, there are areas and regions which have been mostly untouched by conflict, and in fact have been economically thriving. Thus the economy of the Katanga province in DRC has performed strong, as has Somaliland. This shows the importance of political stability for sustained regional development. Collective policy actions by regional governments to consolidate peace and stability are of course a sine qua non condition for continued economic and social development.

Notes

67 There are a number of ongoing initiatives to improve forecasting capability in the region. In conjunction with its partners the African Development Bank, the World Bank and the Partnership for Statistics in the 21st Century (PARIS21), UNECA is committed to supporting both statistical and forecasting capacities in the region under the auspices of the Reference Regional Strategic Framework for Statistical Capacity Building in Africa (RRSF).

68 At the *Intergovernmental Committee of Experts Meeting 2011*, organized by UNECA SRO-EA and held in Dar es Salaam between 13th-18th February 2012, and where a draft version of this report was discussed, the legitimate issue of the quality of growth was raised on several occasions. Concerns were expressed that, despite the good macroeconomic figures, growth is not being sufficiently widely-spread across the population of the region, and its poverty reduction potential has not been fully realized. In this spirit, the theme of UNECA SRO-EA's next 'Tracking Progress' report will be on inequality within the region, and look at the most effective policy measures to address the multidimensional manifestations of inequality.

69 Levels of irrigation in the region are particularly low. For instance, although Ethiopia has engaged on a number of quite large scale irrigation projects, still only 4.5 percent of arable land is irrigated.

70 See Juma (2011) for some examples.

71 For a considerable period, there was criticism of the idea that high investment rates were a sine qua non condition for sustained economic growth – it was argued that high rates of efficiency in the use of capital was more important than high investment rates per se. While it is clearly true that efficiency is a key consideration, stylised empirical studies of countries which have attained a strong growth performance (e.g. Spence, 2011; Rodrik, 2008) come back time and again to the importance of maintaining high rates of investment.

72 Spence (2011:74) notes that with a typical capital-to-output ratio for a developing country in the early stages of growth in the neighbourhood of 2.5, an investment rate of 25 percent would be consistent with growth approaching 10 percent. He also implies that there is an approximate 3:1 ratio between private and public sector investment – that is, high-growth-sustaining countries typically have a contribution of their public sectors to investment of 5-7 percent of GDP. Thus state investments are important catalysts of investment in the private sector.

73 Since its introduction in March 2007, M-Pesa has expanded rapidly, and is now used by more than 9 million customs – 40 percent of Kenya's adult population. The system reportedly processes more transactions domestically than Western Union does on an international scale. For a description of M-Pesa, see Mas and Radcliffe (2011).

74 See "New Fund to Boost Rwanda's competitiveness" by Berna Namata, *The East African*, Arpil 16-22, 2012, page 3. The first issue of the 'African Innovation Report' (AU-NEPAD, 2011) covered R&D activities in 19 Sub-Saharan countries (including four countries in the region – Ethiopia, Kenya, Tanzania and Uganda). It reveals that although agricultural research dominated the research agendas of African countries in the 1990s, research in medicine and other life sciences has recently come to dominate. It could be argued that this shift in balance should be redressed in the interests of food security.

75 The Seychelles' tourism sector, which generates about 25% of GDP, displayed impressive buoyancy in the first seven months of 2011 (after a record-breaking 2010, when visitor numbers rose by 11% to 174,529) (EIU, 2011). However, in view of the deteriorating economic circumstances in the OECD countries, prospects for the rest of the year are less sanguine.

76 A couple of recent examples in Rwanda of the financing gap are delays in the \$325 million methane gas project by the American firm Contour Global, and also the Kigali Convention Centre, which was scheduled for completion in 2011, but is likely to be delayed for two years due to a \$90 million funding gap (of a total projected cost of US\$ 300. See the 'Key projects in Rwanda delayed as investors cut back on funding', *The East African*, 2-8 January 2012.

77 The caveat here is that, as seen earlier, ToT shifts have not been all favourable for the EAR, suggesting that the improvement in growth performance is much more than simply a story of higher prices for key export commodities.

78 For instance, In Tanzania, child mortality (counted as deaths < 5 years per 1000 born) dropped from 115 deaths per 1000 born to 76 deaths per 1000 born in 2010 – still a high rate, but a very significant improvement. Moreover, this means that Tanzania achieved something in the last 15 years that took Sweden 32 years to do in the early 20th century. In other words, Tanzania improves with twice the speed of historical Sweden. Moreover, Tanzania's average annual rate of reduction of child mortality over the last 15 years was 4.6 % surpassing the Millennium Development Goal rate set by UN (an annual average rate of reduction of 4.3%). See Hans Rosling, <http://www.gapminder.org/news/tanzania-fast-drop-in-child-mortality/>, accessed 4/01/2012.

79 It must be noted that the reference level of income to be met to classify for middle-income status is periodically revised to take into account both rising incomes and the relative valuation of the US dollar. It is unlikely to stay at 996 US\$ for the whole period up until 2030, so this would imply that MIC status would still require some extra time, beyond the calculations here, to be achieved.

80 The IMF is currently the only systematic provider of longer-term forecasts and estimates, with most organizations limiting their forecasts to two years in advance.

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