PHILIP NDEGWA

the common market and development in east africa

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THE COMMON MARKET AND DEVELOPMENT IN EAST AFRICA

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PHILIP NDEGWA

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For

My Wife

EAST AFRICA — MAJOR LINES OF TRANSPORTATION

PREFACE

This monograph is a contribution to the broader subject of the relationship between trade and development in East Africa. This broader subject can be divided into two major sections: trade among the three countries (Kenya, Uganda, and Tanganyika excluding Zanzibar) participating in the East African common market, and East African trade with the rest of the world. In the present monograph attention is concentrated on some findings about trade among the three countries (referred to as *intercountry trade* in the text). Emphasis is laid on the last few years.

The three East African countries have now embarked on ambitious programmes of deliberately stimulating economic development. To achieve the desired growth rates appropriate trade policies, both in trade among the three countries and in trade with the rest of the world, are absolutely necessary. It is for this reason that policy implications and recommendations are an integral part of this study.

Several people have greatly helped me in preparing these results for publication: in particular I would like to express my deep gratitude to my friend and supervisor Professor Paul G. Clark, Director of the Economic Development Research Project at Makerere. He read the manuscript in its draft form and made many valuable suggestions. The faults and errors which may still remain in the monograph are, however, entirely my own. I should also like to thank my colleagues in the Economic Development Research Project; frequently discussions with them and our weekly seminars were of great value to me. Finally, I would like to thank my wife who struggled hard deciphering my handwriting in typing some of the chapters of the draft.

This monograph was written before I joined the Kenya Ministry of Economic Planning and Development. The views expressed in it are therefore entirely my own and in no way represent those of the Ministry of Economic Planning and Development.

P. N.
January, 1965.

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CHAPTER I

TRADE AND DEVELOPMENT OF UNDERDEVELOPED COUNTRIES IN THE PRESENT WORLD SETTING

"*For generations, humanity has built its life upon a recognition of the primary fact that trade is the lifeblood of economic activity. This is equally true whether within or among nations.*"

——Cordell Hull.

The most common phenomenon in underdeveloped countries today is the deliberate efforts these countries are making to step up their rates of economic development, as evidenced by their development programmes. Economic development is no longer regarded as the automatic process it had generally been taken to be by the classical economists. Moreover, it has been realised that the 'gap' between the developed and underdeveloped nations has tended to widen, despite the fact that the classical prescription of the international division of labour has been energetically pursued—at any rate by the underdeveloped countries. This awareness has therefore led to vigorous discussion among economists about the economic development of underdeveloped countries, and the role of trade in this development.[1] Two general outcomes of this discussion are: (*a*) that the problem of the economic development of underdeveloped countries is now an international problem—as was recently demonstrated when the United Nations Conference on Trade and Development was convened in Geneva from the 23rd of March, 1964 to the 15th of June, 1964; (*b*) that one major problem facing modern underdeveloped countries in their attempts to hasten the rates of their economic development is that they are less likely to find markets for their products—unlike the developing countries of the nineteenth century.[2] Indeed it has been stated by

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1. Examination of the role of trade in economic development is not, of course, a new field of investigation in economics; in fact the classical economists spent a considerable part of their effort in discussing it. For a very good account of this see H. Myint, "The 'Classical Theory' of International Trade and the Underdeveloped Countries," *Economic Journal*, June 1958.

2. This is a simplified statement of the differences between underdeveloped countries of today and the modern developed nations in their pre-industrial stage. For an excellent and reasonably full comparison, see Simon Kuznets, "Underdeveloped Countries and the Pre-industrial Phase in the Advanced Countries," *Proceedings of the World Population Conference, 1954: Papers*, Volume V.

S. S. Harris that there is today a decline in the importance of foreign trade in the economic activities of nations.[3] The alleged causes of this trend are taken to be: widespread international insecurity which has led to a drive towards selfsufficiency; the mercantilist tendencies of the communist countries; the spread of development and technological knowledge leading to a reduction in large comparative advantages; advances in technology which have introduced synthetics and made primary raw materials less important in producing a given output; the increasing percentage share of 'services' (which are mainly domestically provided) in total consumption as per capita incomes rise; and less capital mobility because of international instability and insecurity.

The thesis that foreign trade is of diminishing importance could be questioned on several grounds, theoretical and empirical.[4] It is, in any case, ambiguous unless the word '*importance*' is very strictly defined. What we mean by '*foreign trade*' also needs to be clearly defined: for instance a political merger of several large industrial countries would presumably drastically reduce the volume of '*foreign*' trade but not of '*world*' trade. However, for our immediate purposes there is little to be gained from the examination

3. S. S. Harris, *International and Inter-regional Economics*, McGraw-Hill Book Company, 1957, page 238. Harris was not the first person to make this observation. Many years before the German economists had, according to Jacob Viner, observed that there was a "law of diminishing importance of foreign trade" (see Jacob Viner, "The Prospects for Foreign Trade in the Post-war World," *Transactions of the Manchester Statistical Society*, June 19, 1946; also reprinted in *Readings in the Theory of International Trade*, Blakiston Company, 1949, edited by Howard S. Ellis and Lloyd A. Metzler.)

4. In fact this whole problem was discussed at great length during and immediately after World War II, with no clear and firm conclusions. See for example D. H. Robertson, "The Future of Foreign Trade," *Economic Journal*, volume XLVIII, March, 1938; also Jacob Viner, the article cited in footnote 3 above. It is, however, interesting to notice that whereas the rate of growth of the value of world exports increased by 8.4 per cent a year during the period 1950 to 1955, their rate of increase was only 4.9 per cent a year in the period 1960-62. But the period of 1950-55 was not really typical. The Korean War for instance resulted in sharp rises in the prices of major primary commodities, essentially because of stockpiling. The increases in the export earnings of underdeveloped countries which resulted from these high prices, together with inflows of funds from the developed nations, enabled underdeveloped countries to import more goods from the developed ones. Moreover, in Europe this was still a time of reconstruction. The recent fall in the rate of growth of world exports should not be taken to indicate that in future these exports are going to fall even further. In fact the trend is likely to swing up again, especially if restrictions against imports from underdeveloped countries are eased and accompanied by a greater flow of funds from the developed countries to underdeveloped ones.

of world trade trends over the last century or so; rather it is the recent past which is relevant. Examination of world trade over the period 1950-62 reveals two very important developments.[5]

(i) Whereas the value of exports from the developed market economies and the centrally planned economies increased by 150 per cent and 250 per cent respectively, those of underdeveloped countries increased by only 50 per cent. In other words the value of exports from the developed market economies and the centrally planned economies increased by 8.0 per cent and 11.1 per cent a year while those of underdeveloped countries increased by a mere 3.4 per cent per year. The result has been that, whereas the developed market economies and the centrally planned economies have increased their percentage shares in total world exports—the former from 60 per cent in 1950 to 66 per cent in 1963, and the latter from 8 per cent to 13 per cent—the percentage share of underdeveloped countries in world exports has actually declined from 32 per cent to 21 per cent over the same period.

(ii) The developed countries have increased trade among themselves. This last point is of some considerable relevance to the problems facing underdeveloped countries today. The developed countries have, in the last decade, substantially increased trade among themselves: in 1950 their intra-trade was about twice their exports to the rest of the world, but in 1962 their intra-trade was about two and a half times their exports to the rest of the world. Moreover, these developed countries have not only increased their percentage share in total world trade as we have already indicated (and at the expense of underdeveloped countries), but they have also increased their share in total world exports of primary products —from 49 per cent in 1955 to just over 52 per cent in 1961.

The fall in the percentage share of exports coming from underdeveloped countries in the total value of world exports has been the result of two factors: a slower rate of expansion in the quantity of these countries' exports, and a fall in the prices offered for these exports. To start with the first factor, we notice that whereas the quantity of exports coming from underdeveloped countries increased by only 57 per cent from 1950 to 1962, those of developed countries

5. For most of the figures in this and the next paragraph see U.N. Conference on Trade and Development, *A Review of Trends in World Trade*, E/CONF.46/12. Geneva, 26th of February, 1963.

increased by 112 per cent. There are several reasons for the poor performance of underdeveloped countries' exports. (i) There has been increased production of primary products, usually under various forms of protection, in the developed countries—the chief markets for primary products from underdeveloped countries. This has enabled the developed countries to meet their demand for various primary products increasingly from domestic sources, besides increasing their share in total world exports of primary products. (ii) Underdeveloped countries' exports are primary products whereas in recent years the most dynamic expansion in world trade has been in manufactured goods. In fact between 1950 and 1962 the rate of growth in the value of world exports of manufactured goods was 8.7 per cent a year, compared with only 4.2 per cent a year in the case of primary products. (iii) There has been increasing use of synthetics instead of natural raw materials; this has particularly hit cotton, wool, rubber, and leather. (iv) The rapid advance in technology has resulted in large economies in raw material use. Thus, whereas between 1928 and 1957 world production of manufactured goods increased by 146 per cent, the increase of primary products needed for this expansion was only 55 per cent.[6] This advance in technology has also resulted in the substitution of certain primary products for others. Thus, for instance, aluminium has replaced some other base metals in industry and, since aluminium is produced mainly in the developed countries, its increasing use has replaced imports of base metals from underdeveloped countries. The fall in the value of metal exports from underdeveloped countries helps to explain, incidentally, why these countries' share in total world exports of manufactured goods has fallen from 5 per cent in 1955 to 4 per cent in 1961—for metals are included under manufactured goods in the Standard International Trade Classification system. (v) The widespread use of tariffs and internal fiscal charges in developed countries restrained certain imports from underdeveloped countries.

In addition to the slow growth in quantity of exports, there has been a substantial fall in the prices offered for underdeveloped countries' exports. Since the prices of manufactured goods coming from the developed countries have not fallen proportionately but have, instead, tended to rise on average, underdeveloped countries

6. See U.N., *World Economic Survey*, 1958, Table I.

have experienced a substantial fall in their terms of trade. Moreover, it is important to notice that some of the forces contributing to the unfavourable trends in both quantity and price are irreversible.

However, despite the difficulties facing the underdeveloped countries in their attempts to expand their exports to the world, to most of them foreign trade is now, and will continue to be, of great importance in their economic development. These countries are now embarked on courses of deliberately stimulating their economic development—for development is required at a speed greater than would be attainable under a laissez-faire free-market system. In this effort foreign trade can perform a number of functions, direct and indirect, in favour of development.

Let us begin by considering the *direct* functions. Firstly, through exporting their commodities these countries can get foreign exchange with which to finance the imports needed for capital formation. In other words, and to use Professor Hicks' terminology, underdeveloped countries benefit by exporting goods with "less growth potential" for goods with "more growth potential".[7] The level of a country's imports also depends, of course, on other factors, including foreign aid—either in the form of outright grants or in loans. However, in the case of loans the payment for imports is only deferred and the recipient must ensure that exports will increase as time goes on in order to service and finally repay foreign debts. In attempting to promote foreign exchange earnings most underdeveloped countries will also find it necessary to diversify their exports, so as to reduce the danger of an insufficiency of foreign exchange which might result from fluctuations and other long-term factors affecting export earnings from a few commodity exports.

Secondly, foreign trade is important because through it an underdeveloped country has the opportunity to use foreign saving for its development. Foreign saving occurs when imports are more than exports, i.e. when a country has a trade deficit with the rest of the world. The importance of this is that in such a deficit there is a transfer of real resources from the rest of the world to the underdeveloped country in question, and this supplements her domestic resources for development. This kind of saving becomes especially important when an underdeveloped country which has been paying for its imports with its exports decides to accelerate its rate of

7. J. R. Hicks, *Essays in Economics*, Clarendon Press, 1959, p.182.

economic growth. This usually leads to a greater need for imports (especially of capital goods) and therefore pressure for more foreign exchange. In this, foreign saving and the inflow of foreign capital to finance deficits in the country's balance of payments become of great value.[8] Such temporary deficits in the balance of payments of an underdeveloped country are to be preferred to a balance in her transactions with the rest of the world, for it is only a deficit which increases the resources which the country has for stepping up her rate of growth. Ultimately, of course, the country has to pay for its imports, and as development proceeds the deficits should taper off.

Thirdly, new consumption goods not otherwise available can be obtained through imports. These new goods might well create a further strong demand for others like them and thus lead to greater personal efforts in order to buy them.

Fourthly, governments can raise revenue through taxation of imports and exports in order, *inter alia*, to finance various public projects. This is an important function because sources of revenue open to governments of underdeveloped countries are severely limited. Such sources as personal and corporate income taxation, which are so important in the developed countries, would not yield much in underdeveloped countries because of a whole range of factors, e.g. the existence of subsistence activities, and the desirability of keeping tax rates low in order to attract an inflow of capital. The limited sources of government revenue in these countries must be seen against the background of great public pressure for increased government activities in providing services and stimulating development. In meeting this problem, properly designed taxes on foreign trade could be of great help before other sources of government revenue become important.

This is as much as we shall say about the direct functions which foreign trade can perform to help development in underdeveloped countries. Obviously the list is not exhaustive, but it is hoped that the main ones have been indicated. We now turn to *indirect* func-

8. The role of foreign saving has become a field of extensive investigation. See for example ECAFE, "Deficit Financing for Economic Development with Special Reference to ECAFE Countries," *Economic Bulletin for Asia and the Far East*, 1954. After this early attempt ECAFE has been discussing foreign saving in ECAFE countries in almost every issue of their yearly Bulletin. The Economic Commission for Latin America has also dealt with this problem.

tions—and these are also exceedingly important. Firstly, availability of external markets makes it possible for an underdeveloped country to enjoy economies of scale through large-scale operation. The effect of this in an export industry may be important enough to induce expansion in other industries and sectors. The expansion of a given industry could induce expansion in other industries and sectors through greater demand for their outputs (i.e. backward linkage effect), or by providing inputs needed by other industries (i.e. forward linkage effect).[9] The availability of external markets is particularly important in the case of manufacturing industries, for one of the most formidable obstacles to industrialisation in underdeveloped countries is the small size of their domestic markets arising from very low levels of income per capita.[10] Moreover, it is in these industries that linkage effects are particularly strong. The small size of the domestic market means that if manufacturing enterprises are established they would have to be of very small scale or, if large, be operating with excess capacity. In either case they would be high-cost enterprises, but if external markets could be found these enterprises could be operated at lower costs, if not at the minimum points of long-run average cost curves.

Secondly, foreign trade provides scope for, and induces development in, skills, e.g. in meat canning, cotton ginning, etc. This is an important function, for skilled labour is also one of the most serious constraints on the development of underdeveloped countries. The preparation and processing of primary products for export eases the problem through the introduction of new skills and organisation methods, and thus paves the way for other industries requiring skilled labour.

Thirdly, the actual dependence on foreign imports is, paradoxically, of some advantage in the sense that imports may stimulate domestic production of substitutes, besides providing guidance on the nature and scope of the import substitution that is possible.

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9. For an excellent analysis of these two effects in economic development see A.O. Hirschman, *The Strategy of Economic Development*, Yale University Press, 1958, Chapter 6.

10. The market size is, essentially, a function of two factors: population and per capita income. In underdeveloped countries it is the latter factor which is the main problem. However, we need also to notice that the smaller the population the more permanent will be the obstacle of the small domestic market to the industrialisation process.

The present vigorous discussion on "trade and development", clearly recognizes that availability of foreign markets is now of crucial importance to underdeveloped countries—and to developed countries as well, though less intensely. In the nineteenth century, the developing countries such as Canada, New Zealand and Australia found ready and expanding markets for their produce in rapidly industrialising Europe. They also received large doses of investment from the "mother countries" designed to produce the needed raw materials and food. In those days foreign trade was indeed "the engine of growth",[11] and this close link between economic growth and international trade was, as Ragnar Nurkse pointed out, due to the fact that "the pattern of advance in the rising industrial areas [Europe] happened to be such as to cause a rapidly growing demand for crude products which [the new areas of settlement] were fitted to supply".[12] Today, however, since this engine of growth is in "comparatively low gear",[13] any "*exclusive emphasis on the traditional pattern* of growth through trade would be out of place, and could be interpreted as a hangover from bygone days".[14] This conclusion proceeds from the fact that international trade has changed its nature and is, *for underdeveloped countries*, not growing fast enough. We have seen for instance that the industrial countries have actually increased their percentage share in the value of total world exports of primary products.[15] We have also indicated that the terms of trade facing underdeveloped countries are likely to remain unfavourable and possibly even deteriorate further,

11. D. H. Robertson, "The Future of Foreign Trade," in *Essays in Monetary Theory*, London, King, 1940.

12. Ragnar Nurkse, *Patterns of Trade and Development*, Oxford University Press, 1961 page 49.

13. Ragnar Nurkse, *ibid.*, page 27.

14. Ragnar Nurkse, *ibid.*, page 50.

15. It is not often realised that the so-called industrial countries produce the bulk of the world supply of raw materials and food. It has been estimated that North America, Western Europe and Japan produce 90 per cent and 70 per cent of the food and raw materials, respectively, which they consume. Moreover, it is not often realised that large proportions of some major world exports of primary products (except rice which is mainly produced and traded in underdeveloped countries) come from the so-called industrial countries. Once this is realised underdeveloped countries can only be called primary producers for two reasons: (i) that they depend on the production of primary products for the major part of their national income and employment unlike all developed countries; and (ii) that most of their exports are primary products and often consist of only one or two commodities, again unlike all developed countries.

except perhaps for the oil countries.[16] The net result is that exports, which in the nineteenth century were the leading sector in the economic development of the new areas of settlement, will continue to be the lagging sector in the underdeveloped countries of today. In fact, looking at underdeveloped countries in general, it would appear that the development which has taken place in them after the end of the Korean War commodity boom has been due to increased external borrowing rather than domestic exports. But this source of resources for development is limited because the aid being given is not adequate for the problems at hand, is politically distributed, and is subject to increasingly severe conditions which tend to reduce its effectiveness. In any case increasing indebtedness will severely restrict the ability of the developing countries to import more goods for development purposes.

Because of the poor prospects for underdeveloped countries' traditional exports, it will be recognized that the hope of these countries to improve their living standards and provide employment for their increasing populations must lie in industrialisation.[17] This conclusion becomes even stronger when we recognize that since income elasticities of demand are highest for manufactured goods, a rise of incomes in underdeveloped countries through improvement in the productivity of agriculture leads to more imports of manufactured goods; thus the benefits obtained from such

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16. This view is by no means universal among economists; in fact in the last few years quite a few economists have become very sceptical of the view that there is a *secular* unfavourable trend in the terms of trade of underdeveloped countries. Certainly the figures provided in the United Nations publication, *Relative Prices of Exports and Imports of Underdeveloped Countries* (New York, 1949), showing the United Kingdom's commodity terms of trade, on which some economists base their arguments about the unfavourable secular terms of trade facing underdeveloped countries, leave much to be desired and are not conclusive —if only because of the measurement problems, e.g. new goods and improvement in quality of manufactured goods. Some economists therefore say that the picture is not clear. But this is cold comfort for underdeveloped countries: for *in the last ten years or so* there has been a clear deterioration in their commodity terms of trade, and there are no signs that this trend is reversing itself, or is even likely to in the near future. Moreover, even if their terms of trade did not deteriorate further, underdeveloped countries would still have the unsolved problem of fluctuations and instability in their export earnings.

17. For an excellent discussion on the need and importance of industrialisation in the development strategies of underdeveloped countries see Hollis B. Chenery, "The Role of Industrialisation in Development Programmes," *American Economic Review*, May, 1955.

improvements are likely to be transferred to the industrial countries.[18] The importance and necessity of industrialisation in underdeveloped countries has now been widely accepted, at any rate as the long-term solution.[19] The underdeveloped countries themselves have grasped this point, as is evident from their development programmes.

But in attempting to industrialise themselves underdeveloped countries face serious problems connected with foreign trade. Firstly, manufactured goods from these countries are not initially competitive in foreign markets, and cannot be expected to be so for some time. Such manufactured goods have the great disadvantage of being produced on a small scale and therefore at high cost. They are produced by inexperienced industrialists not in full knowledge of demand patterns abroad, with little commercial contacts in foreign countries, unable to offer servicing facilities, and unable to maintain attractive (expensive) packaging standards and costly advertising campaigns. Moreover, demand patterns in industrial countries are very diversified and fashions shift rapidly. New entrants from underdeveloped countries must compete with long-established firms, and transport costs also work against them. Not least, there are tariffs and internal duties in most developed countries against imports from underdeveloped countries, with the level of tariffs rising in most cases with the degree of manufacturing involved. The most alarming development is that if imports rise too rapidly, it now seems accepted that a developed country can, in order to avoid "market disruption", unilaterally violate the

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18. This is part of the so-called "Prebisch thesis"—see R. Prebisch, "Commercial Policy in the Underdeveloped Countries," *American Economic Review*, May, 1959. Prebisch argues very strongly also for industrialisation in underdeveloped countries. His thesis that the benefits of technological improvements in underdeveloped countries are transferred to the industrial countries is undoubtedly right *given his assumptions*. However, we need to notice that this transfer of income from underdeveloped countries to the developed countries through deterioration in the former countries' commodity terms of trade would be checked if these countries' single factoral terms of trade improved substantially.

19. There is still some controversy among economists about how best to achieve this long-term solution. There are those who recommend that initially emphasis should be given to agriculture, there are those who recommend that it is industry which should be emphasised, and there are those who recommend a *balanced* strategy. Space does not allow detailed examination of these various views. Needless to say, ultimately the issue is not *either* agriculture *or* industry; *both* industrial *and* agricultural revolutions must occur in these countries; at each stage of its economic development the underdeveloped country has to assess its resources and the opportunities available and then base its strategy on that assessment. There can be no blanket or universally applicable strategy for all countries at all times in the development of underdeveloped countries.

professed declaration of liberalisation of trade and impose additional tariffs and quotas if necessary.[20] The total picture is that underdeveloped countries will not find it easy to export their manufactured goods to developed countries. In fact manufactured goods produced in underdeveloped countries are often not competitive, in their home ground, with similar goods from the developed countries. It is because of these problems that one of the most effective ways in which the developed nations can assist the underdeveloped ones is to offer them markets for their goods; this is a necessary part of economic aid, for financial aid alone is not likely to be effective.

The second general problem which underdeveloped countries face in their industrialisation programmes is that the moment they begin planning for industrialisation they find themselves desperately short of foreign exchange—because their traditional exports (primary commodities) are not earning enough to satisfy their requirements for capital investment. This problem has already been discussed above, and we shall not say more on it here.

The conclusion that the underdeveloped countries will not find it easy to export their manufactured goods to developed countries leads us to a second conclusion: namely, that industrialisation in underdeveloped countries must be based, initially at least, on a process of deliberate import substitution.[21] This amounts to a rejection of a development strategy based on laissez-faire policies and a static interpretation of the doctrine of comparative advantage. The doctrine of *comparative* advantage prescribes that a country should concentrate on the production of those goods in which her comparative advantage is most marked, or her comparative disadvantage least marked, and import those goods in which her comparative advantage is least marked or her comparative disadvantage most marked. Another version of it, as stated in the

20. The real danger arising from the "market disruption" clause lies in the fact that so far there are no strict and well-established criteria for defining market disruption. Any country invoking this clause should be asked to prove that the exporting country is producing the particular imports under abnormal conditions, and that these goods are being sold at prices much lower than those generally prevailing in the market. The country invoking this clause should also be asked to indicate clearly the possible consequences on her economy if imports in question were not restricted.

21. For a very able exposition on the importance of import substitution see Hollis B. Chenery, "Patterns of Industrial Growth," *American Economic Review*, September, 1960.

Heckscher-Ohlin theorem, prescribes that a country should concentrate on the production of those goods which use more of its abundant factors, and import those which use more of its scarce factors.

Although the doctrine of comparative advantage sounds sensible, it has a number of weaknesses which become apparent when examined rigorously. In its most rigid form it is an exceedingly static theory, whereas one would expect comparative advantages to change with time; it assumes that there is full employment, for otherwise comparative advantages would not be known; it rests on the assumption that free markets and thorough-going competition prevail, so that market prices are reliable approximations of relative costs; it assumes perfect internal factor mobility, but factor immobility internationally; by and large it ignores transport costs; and it also ignores the now well-known near-zero, zero, or even negative marginal productivity of labour in subsistence sectors of overpopulated underdeveloped countries. Most serious, however, is the fact that either demand aspects are ignored, or it is assumed that demand is infinitely elastic. Thus in the case of underdeveloped countries blind application of this doctrine would lead to policies designed to produce more primary products for which demand prospects today are bleak. Indeed, general applicability of the whole of the *traditional* foreign trade theory to underdeveloped countries is to be questioned. As Myrdal has said, "... to apply a general, and basically static, equilibrium theory of international trade to [underdeveloped countries] without taking into consideration the actual estate of underdevelopment amounts very nearly to scientific fraud".[22]

However, to say that the doctrine of comparative advantage should not be applied blindly to modern underdeveloped countries is not to suggest that these countries should cease or even restrict their production of primary products. It does mean rejection of laissez-faire policies *based on current comparative advantage*—not only because of imperfections in the price system but also because such policies would neglect the fundamental differences between modern underdeveloped countries and the developed countries. Such policies would also neglect the dynamic effects of import substitution. Indeed, deliberate industrialisation through import substitution does not totally reject the doctrine of comparative advantage: rather it aims at accelerating *changes* in the comparative

22. G. Myrdal, *An International Economy*, Routledge and Kegan Paul, 1956.

advantage of the underdeveloped countries vis-à-vis the developed nations—changes which must surely occur with development. Moreover, to be successful a strategy of development based on import substitution must be guided at each step by estimates, however rough or imperfect, of where comparative advantage is rising, or comparative disadvantage diminishing.

To all intents and purposes the process of import substitution in underdeveloped countries will have to start with consumer-goods industries.[23] This hypothesis is easily defended. First, consumer-goods industries are, by and large, less capital intensive than producer-goods industries: this is important because underdeveloped countries are short of capital and should therefore attempt to economise on its use. Second, consumer-goods industries demand, again by and large, less skill and a less sophisticated technology. They also depend more on domestic raw materials than capital-goods industries. Finally, in the early stages of development at least, the demand for consumer goods is more easily assessed, e.g. through an examination of the import bill. Moreover, this demand can be expected to expand as development proceeds because for most manufactured goods income elasticities of demand are high in the early stages of growth.

The conclusion we can draw from the preceding discussion is this: that underdeveloped countries have to rely on import substitution in order to industrialise, but they have also to persuade the countries producing the goods being substituted to open their markets

23. In some underdeveloped countries such import substitution has perhaps gone as far as it can. In Brazil, for instance, the share of manufacturing in the gross domestic product is above 30 per cent, while the share of imports is about 10 per cent. In such countries the strategy should be to explore markets in foreign countries—especially in the developed countries. Incidentally, it is crucial to notice that since some underdeveloped countries are more industrialised than others, the really underdeveloped countries at the earliest stages of development have to protect their industries against manufactured goods from the more developed underdeveloped countries. In fact, it is oversimplification to lump all underdeveloped countries together as a homogeneous group, as we have done so far. There are very wide and significant differences among underdeveloped countries, for they are not all at similar stages of development. The problems facing the more developed countries will, therefore, be different from those facing the countries at the earliest stages of development. In the former group of countries the major constraint in development seems to be the balance of payments squeeze (which would be considerably eased if these countries could export more to the developed countries, especially their manufactured goods); whereas in the latter group of countries the constraint and major obstacle to development is a desperate and all-round scarcity of basic resources, including manpower. We shall return to this problem in the final chapter of this study.

to goods coming from the developing countries.[24] This, unfortunately, provides room for political controversies in this whole field, especially when it is recalled that development brings with it changes not only in the commodity composition of imports but also in the direction of trade of any country. A measure of success has already been achieved in the acceptance, albeit vague, of the "non-reciprocity" principle in tariff negotiations, but this does not solve the problem entirely. A suggestion as to how underdeveloped countries could rely on import substitution and still expect to find markets for their goods, *but mainly* in other developing countries through a system of preferential tariff arrangements, will be discussed in the final chapter of this study.

From what has been said so far it becomes clear that attempts to enlarge and extend the domestic markets of underdeveloped countries are now of great relevance. In particular this study on intercountry trade among the three East African countries is an attempt to examine the way out of the existing international trade problem, by indicating the role of expanded intercountry trade and import substitution within the framework of a common market or customs union among underdeveloped countries.

The subsequent chapters of this study are devoted to various aspects of trade among the three countries[25] participating in the East African common market.[26]

24. Import substitution in the developing countries does not, of course, necessarily mean that these countries' total imports from all the developed nations will fall—at any rate in the long-run.

25. This study was substantially completed before Zanzibar joined Tanganyika to form the United Republic of Tanganyika and Zanzibar—recently re-named the Republic of Tanzania. But Zanzibar is a small country and her exclusion or inclusion in East African intercountry trade would not substantially alter the general picture, either of Tanganyika alone or of East Africa as a whole. In fact most of Zanzibar's trade has been with countries other than the three mainland countries. In large part this has been a result of her non-membership in the East African customs union, although a common currency and close physical proximity have made her dependent on the rest of East Africa for some of her imports.

26. We shall refer to the arrangements defining the economic relationships existing among Kenya, Tanganyika and Uganda as a *common market*. This is justified on the ground that there are very few restrictions on movements of goods and factors of production, besides a common tariff wall against the rest of the world. Actually economic integration is much closer than in most common markets, including the European Economic Community. The three East African countries share the same currency, and operate jointly a number of services (railways and harbours, post and telecommunications, and others) under the East African Common Services Organisation (E.A.C.S.O). But the three countries are politically and economically independent sovereign states, with most of the regulations governing the common market being settled by negotiation.

In Chapter II we examine the various categories of East African trade and certain major features of the pattern of these countries' foreign trade. Chapter III discusses intercountry trade in foreign imported goods, while Chapter IV discusses intercountry trade in domestically produced and manufactured products. Chapter V takes up the problem of estimating each East African country's balance of payments, and indicates the major flows in the current account balance of payments position of each country. Chapter VI considers the development effects of the operation of the East African Common Market. Chapter VII discusses trade between the three East African countries and neighbouring African countries. Finally, in Chapter VIII the major conclusions and policy recommendations are summarised.

For the most part in this study policy issues are discussed and recommendations made as the analysis is developed. The problems of development and trade are so many and diverse that attempting to consider policy recommendations in one chapter only, without discussing the problems in detail in the same chapter, would not be of much value. In these days most economists do not shy away from saying "what ought to be", as they used to thirty-five or so years ago when they regarded their science as a "positive" science primarily concerned with "what is"—an approach ably expounded by Professor Lionel Robbins in his otherwise admirable book, *An Essay on the Nature and Significance of Economic Science* (1932). This change in approach has now received wide acceptance, as evidenced by that new person in the government service—the "economic adviser". Of course ultimate decision-making lies with the politician. But economists can help enormously by pointing out the relative costs of various alternatives, and once these costs are indicated it is to be hoped that the politician will find it difficult to ignore them.

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CHAPTER II

CATEGORIES OF TRADE: MAJOR FEATURES OF EAST AFRICAN FOREIGN TRADE

One major condition for studying East African trade empirically is to understand the various categories in which trade data are given, and also to have an idea about the limitations of the available trade data.[1] The available trade data are grouped into two major categories: foreign trade statistics, and intercountry (commonly called inter-territorial) trade statistics. As far as *visible trade* is concerned, the information available is in many ways excellent, although the coverage is better in the case of foreign trade. In fact, in many underdeveloped countries statistics on foreign trade are the best in the country. This is because the governments of these countries usually depend heavily on revenue raised in the foreign trade sector. Consequently, both in coverage and availability, data on foreign trade are usually much better than those on other sectors of the economy, including population.

As far as *invisible trade* is concerned, however, the picture is quite different. In East Africa information on this trade is very scanty, limited and even non-existent in the case of intercountry trade. In the foreign trade category, however, rough magnitudes of this trade for the whole of East Africa's economic transactions with the rest of the world are indicated in the balance of payments estimates which have been published since 1956. There are no official estimates as yet of each country's balance of payments.[2]

In this chapter we shall first discuss the various categories of foreign trade and then those of intercountry trade. But before doing this we shall briefly explain the Standard International Trade Classification system which is now used in East Africa.

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1. The three main sources of trade data are:—(*a*) *Annual Trade Reports of Kenya, Uganda and Tanganyika*, which are published every year by the Commissioner of Customs and Excise, Customs House, Mombasa. Prior to 1949 Kenya and Uganda (which had a common customs authority) were treated as one trade unit in the Annual Trade Reports. This meant that Tanganyika was treated as a foreign country; and in her trade data Tanganyika did the same for Kenya and Uganda. (*b*) The annual *Statistical Abstract* of each country—published by the Government Printer of the respective country. (*c*) The *Economic and Statistical Review*—a quarterly bulletin produced by the E.A.C.S.O. Statistical Department covering the three countries.

2. This problem is discussed, and some orders of magnitude of each country's major flows on the current account indicated, in Chapter V.

The Standard International Trade Classification (SITC) System.

Since 1954 East African trade data, for both foreign trade and intercountry trade, are shown classified and numbered in conformity with the Official Import and Export List, which is based on the SITC system compiled by the United Nations Statistical Commission in order to make international comparisons easier. In this classification system all commodities traded are grouped into the following ten categories:

SITC Section	*Commodity*
0	Food.
1	Beverages and tobacco.
2	Inedible crude materials, except fuels.
3	Mineral fuels, lubricants and related products.
4	Animal and vegetable oils and fats.
5	Chemicals.
6	Manufactured goods classified chiefly by material.
7	Machinery and transport equipment.
8	Miscellaneous manufactured articles.
9	Miscellaneous transactions and commodities not elsewhere stated.

Prior to 1954, the system of commodity classification used in East Africa had twelve sections. Therefore it is not easy, although not impossible, to trace the commodity composition of this trade prior to 1954. In this study, however, detailed analysis of the commodity composition of East African trade is confined to recent years, mainly the period 1959 to 1963.

In a detailed analysis of the commodity composition of East African trade it is necessary to go beyond SITC sections and examine the actual commodities and articles included in each section. This is especially important in the case of SITC sections 0, 2, and 6. In section 0 (food) there are some articles, such as biscuits and confectionery, which are really manufactured goods. For this reason it would help if this section were divided into two sub-sections: manufactured and unmanufactured food. In SITC section 2 (inedible crude materials except fuels) there is one important item at least which should be included in SITC section 5 (chemicals): this is pyrethrum extract. In SITC section 6 (manufactured goods chiefly classified by material) we find some items, such as diamonds and base metals, which are strictly speaking primary products and not

manufactured goods, and whose inclusion gives the erroneous idea that some underdeveloped countries export large quantities of manufactured goods. Separation of such items from manufactured goods seems sensible.

East African Foreign Trade Classes

This trade is classified into the following categories.

(i) *Domestic Exports.* These figures refer to each country's exports of domestic produce and manufactures *to countries outside East Africa,* and purchases by foreign aircraft and ships. Information on these exports is very good. Data are shown according to SITC system, and the major commodities in each section and the major countries of destination are also shown.

The domestic exports of each East African country also include any produce of the other two East African countries which is imported and blended or processed with the produce of the country in question. However, the domestic exports of, say, Kenya do not include the produce of Uganda or Tanganyika which is simply repacked in Kenya without losing its identity. Such goods are classified as domestic exports of the country in which they originated.

Domestic exports of each country are valued free-on-board (f.o.b.) port of departure from East Africa. This results in Uganda's domestic exports, and those of Tanganyika's domestic exports which depart through Mombasa harbour, being overvalued to the extent of the transport costs between Mombasa and these countries' borders.

(ii) *Re-exports.* These are goods imported *from outside East Africa* and then re-exported *to countries outside East Africa,* or as ships' and aircraft stores, without any substantial change in their form. As in domestic exports, re-exports are broken up into their respective SITC sections. The major countries of destination are also shown for each SITC section, but not for the major commodities. One major problem with re-exports is that goods are not necessarily re-exported in the same year in which they were imported.

(iii) *Direct Imports.* These data show goods imported *from outside East Africa* and which are *directly consigned* to a given East African country for consumption or warehousing. They include goods which are subsequently re-exported to countries outside East Africa and goods subsequently transferred to another East African country.

(iv) *Transfers.* These are the direct imports which, after importation by one East African country, are subsequently transferred *to another East African country.* Another way of putting it is to say that transfers are intercountry re-exports, or that in the case of each East African country they are indirect imports. There are no separately published figures on transfers, although they have become a very significant part of intercountry movement of goods among the three countries; we have devoted the next chapter to examine them in more detail.

As there is a substantial trade in these foreign imported goods in East Africa, what matters most from the point of view of each country is the *net* result, i.e. each country's transfers to the rest of East Africa *minus* the transfers of the rest of East Africa to her. This difference is *Net Transfers.* It is important to notice that, as in the case of re-exports, not all transfers take place in the same year as they were directly imported. This explains why in some cases there are negative totals—caused by transfers of goods imported in a previous year, or transferred at a much higher value than originally imported. The valuation of these transfers is discussed in the next chapter.

(v) *Net Imports.* These data show each country's *Direct Imports plus or minus Net Transfers.* Net imports include goods which are subsequently re-exported outside East Africa.

(vi) *Retained Imports or Net Retentions.* These data show *Net Imports minus Re-exports.* These figures are very important because they show the total foreign imports absorbed by each East African country; although we have to be aware that not all re-exports and transfers take place in the year of their importation.

All foreign imports are valued cost-insurance-and-freight (c.i.f.) port of entry into East Africa, irrespective of the country to which they are consigned. East African customs duties are not included. This system of valuation means that Uganda's foreign imports, and those imports of Tanganyika which come through Mombasa, are undervalued to the extent of transport costs between Mombasa and these countries' borders.

Coverage on each country's exports (domestic and re-exports) is good, but there is some unrecorded trade with the neighbouring African countries. Moreover, the following are excluded from the published export data: naval and military stores, goods exported

by parcel post, goods exported by air freight unless their value exceeds £25, travellers' samples, and passenger baggage. But these items are not likely to amount to very much.

Coverage on foreign imports is good because, like foreign exports, most of them come through the few Kenya and Tanganyika ports, especially Mombasa and Dar es Salaam. The volume of unrecorded imports from the neighbouring African countries is not known, expecially between Uganda and the Sudan, Congo-Leopoldville, and Rwanda; and between Tanganyika and Burundi, Zambia, and other countries with which she shares boundaries. But the volume of such unrecorded imports is likely to be small, and perhaps much smaller than unrecorded East African exports to these countries. The following items are also left out of the published data on foreign imports: travellers' samples, passengers' baggage except dutiable goods, duty-free goods imported by air freight and whose value does not exceed £25, naval and military stores, and motor-cars imported on a triptyque unless they are subsequently re-exported.

East African Intercountry Trade

There are three categories in this trade:

(*a*) Trade in foreign imported goods from one East African country to another, i.e. transfers as defined above.

(*b*) Trade in domestically grown or manufactured goods which do not include foreign imported materials, or for which the value of such materials is less than twenty shillings.

(*c*) Trade in domestically produced or manufactured goods which contain imported materials to the value of twenty shillings or more.

However, in the regularly published intercountry trade data only domestically grown or manufactured goods, i.e. categories (*b*) and (*c*) combined, are shown. Trade in foreign imported goods, i.e. category (*a*), is not shown as such, and the only way of assessing it is to calculate net transfers by deducting each country's direct imports from its net imports.

The grave problems involved in valuing transfers will be discussed in the next chapter. Here we shall only discuss the valuation of trade in categories (*b*) and (*c*) above. The valuation and recording of goods in intercountry trade in East Africa depends on a system of consignors' declarations. Before dispatching goods to another

East African country, the consignor is required by law to fill in a form specifying certain details, and then to send it to the East African Customs and Excise Department where the relevant details are recorded. In the case of goods produced or manufactured domestically, which do not include foreign imports of raw materials or for which the value of such materials is less than Shs. 20/- (i.e. category (*b*) above), the values shown are those declared by the consignor as the selling price to the buyer. (This value will often include costs of transport from the seller to the buyer and insurance, if any). In this case the value of any duty on imported foreign materials used in production, though small in magnitude, is still included in the recorded value. In the case of excisable commodities the value is reduced, however, by the amount of excise duty.

In the case of intercountry trade in domestically produced or manufactured goods which contain foreign imports of raw materials worth more than Shs. 20/- (i.e. category (*c*) above), the "consuming country gets a credit of the value declared by the consignor as the selling price to the purchaser and, in the case of goods liable to *ad valorem* rates of duty, the amount of duty chargeable at the appropriate rate on 70 per cent of the declared value of the imported articles contained in such goods, or in the case of goods subject to specific rates of duty, the amount of duty collected on such goods at the time of importation".[3] In other words the value recorded *excludes* these duties. This procedure is maintained for two reasons: to give each country its proper share of the customs revenue collected on foreign imports ultimately consumed within its borders; and to remove elements of customs duties and excise taxes from the value of intercountry exports and imports.

The removal of these duties and excise taxes, which was first done in 1959, improves our information on intercountry trade considerably. The inclusion of these elements inflates the value of intercountry trade before 1959 considerably, especially when it is recalled that in those years the excisable commodities (mainly cigarettes, tobacco, beer and sugar) were very important in this trade. The change in practice in 1959 also makes it difficult to compare the growth of this trade in the former years with the latter years; and it is partly for this reason that in this study we shall for the

3. *1963 Annual Trade Report*, page vi.

most part confine our analysis to the years 1959 to 1963. Moreover, coverage and data collection have been improving with time, and therefore the more recent the data the more accurate they will be.

The coverage on intercountry trade is not as good as in foreign trade. As the Annual Trade Reports say every year, "it should be borne in mind that there are only four customs posts on the water frontiers and two on the land frontiers between Kenya, Tanganyika and Uganda and that it is not difficult for goods to cross the frontiers without transfer forms being completed. The extent to which this traffic takes place is not known".[4] It should be pointed out, however, that where intercountry movement of goods takes place by railway or East African Railways and Harbours' boats, transfer forms are completed without fail—except for those goods which are moved as people's luggage. But it is when goods are transported by road that transfer forms are unlikely to be completed. Furthermore, observations would indicate that there is considerable boundary trade in some parts of East Africa. The general picture therefore is that the coverage on this trade is not anywhere near complete. It would be extremely difficult to record all intercountry trade because of the following factors: (*a*) the existence of extensive land frontiers which would be very expensive to control; (*b*) the existence of a common currency in the three countries; (*c*) the prevalence of barter trade, especially in foodstuffs, along the boundaries; (*d*) the fact that people in East Africa often travel with goods and not just baggage.

Trade with Neighbouring African Countries

In this study East African trade with neighbouring African countries ("the Neighbours") is examined in Chapter VII. However, references to this trade will be made from time to time in earlier chapters. For the purposes of this study "the Neighbours" are Zanzibar, Somalia, Ethiopia, the Sudan, Congo-Leopoldville, Rwanda, Burundi, Zambia (formerly Northern Rhodesia), Malawi (formerly Nyasaland), Rhodesia (formerly Southern Rhodesia), Mozambique, Reunion, the Seychelles, Madagascar, and Mauritius. East Africa shares common borders with many of these countries—hence the term Neighbours. For comparison purposes this trade is

4. *1963 Annual Trade Report*, page vi.

particularly important since the Neighbours are at a broadly similar stage of economic development as East Africa.

For statistical reasons it is very difficult to deal with some of the Neighbours individually. Until the end of 1963 Malawi, Zambia and Rhodesia formed a single political and economic unit known as the Federation of Rhodesia and Nyasaland (or the Central African Federation). Therefore, in the East African trade data these three countries were considered as one country, and it is thus impossible to trace the East African trade with any of these three countries alone for the last five years. We shall, therefore, refer to these countries collectively as Rhodesia and Nyasaland. The same problem arises in the case of East African trade with Rwanda, Burundi, and Congo-Leopoldville—for these countries were, until they achieved political independence from Belgium, regarded as one country in the Annual Trade Reports. However, from 1964 trade data with each of these countries should be available, and will fill an important gap in our knowledge and future analysis of East African trade with the Neighbours.

Major Features of East African Foreign Trade

The fact that this study concentrates on East African intercountry trade should not be taken as suggesting that East African foreign trade is unimportant. In this short section we shall briefly mention some of the main features of East African foreign trade which should be kept in mind, in order to put the discussion of East African intercountry trade in its proper perspective. In the following chapters we shall also refer to foreign trade from time to time for comparison purposes.

The first thing that we should mention is that East African foreign trade is of relatively recent origin—if compared with the West or North African countries. It is true that for many centuries before being "discovered" by Europeans, East Africa had been known to the Chinese and the Arabs; but trade with Asia was very small and confined to a few coastal towns. Moreover, after the Arabs re-established their authority along the East African coast by driving out the Portuguese, the main East African domestic exports became ivory and slaves. It was not until the penetration of Europeans into East Africa at the end of the nineteenth century (to "convert the heathen", abolish the slave trade and slavery, and

tap new sources of raw materials, as well as to establish new markets) that East Africa was effectively introduced to foreign trade. Ivory and slaves were replaced by cotton, coffee, sisal, and other primary commodities as East Africa's leading exports to the world. This process was given a tremendous stimulus by the immigration of Europeans and Asians into these countries—the two communities which provided the entrepreneurial ability needed both in exporting these commodities and in importing and distributing foreign goods. But it was not until the end of World War II that the rate of growth of East African foreign trade became really significant—as the figures in Table II.1 reveal.

TABLE II.1
The Growth of East African Foreign Trade
(£ *million*)

	Domestic Exports	*Imports*
1939	11.7	9.5
1945	23.9	16.6
1946	25.6	25.5
1947	32.2	39.3
1948	42.1	58.7
1949	54.3	75.2
1950	68.9	71.3
1951	110.6	104.1
1952	119.5	121.1
1953	87.1	105.8
1954	97.1	117.5
1955	103.8	149.0
1956	114.3	133.8
1957	119.1	140.1
1958	116.4	121.4
1959	120.7	121.5
1960	131.6	133.9
1961	123.2	135.2
1962	126.8	135.5
1963	158.9	145.0

Source: East Africa *Economic and Statistical Review*, various years.

There are two major characteristics of this trade which are not brought out in these figures and which should be noted. (i) The first is the overwhelming dominance of a few agricultural commodities in the total East African domestic export earnings. In 1963 the four main agricultural commodities in East African domestic exports were coffee, cotton (raw), sisal and tea. These four commodities accounted for £110 million out of total domestic export earnings of £158.9 million—with coffee alone contributing £45 million or 28 per cent of the total. The importance of these commo-

dities differs from country to country: in 1963 coffee, cotton and tea contributed 84 per cent of Uganda's total domestic exports (with coffee alone accounting for 53 per cent); in Tanganyika sisal, coffee and cotton contributed 63 per cent (with sisal alone accounting for 36 per cent); and in Kenya coffee, sisal and tea contributed 55 per cent. This concentration of East African domestic exports stands in strong contrast with the tremendous diversity of her purchases from the rest of the world, although most of these purchases are manufactured goods. In 1963 the main East African imports from the rest of the world, out of a total of £145 million, were machinery 13.7 per cent, transport equipment 12.6 per cent, cotton piece-goods 5.9 per cent, iron and steel manufactures 5.1 per cent, paper and paperboard manufactures 2.8 per cent, and petroleum products 9.1 per cent. Concentration of export earnings in one, two or three primary commodities, and a relatively more diversified commodity composition of imports, is a common feature of an underdeveloped country.

(ii) The other observation which is not brought out in Table II.1 is that East African foreign trade is only with a few countries—the United Kingdom, West Germany, the United States, Japan, and four important underdeveloped countries, India, Iran, Hong Kong and China. Again there is greater concentration in the destination of East African exports than in the sources of her imports. In 1963, out of a total of £158.9 million of domestic exports £106.6 million or 67 per cent went to the United Kingdom, the United States, West Germany, Netherlands, China, Hong Kong and India;[5] while on the imports side the main sources were United Kingdom 32.4 per cent, West Germany 6.8 per cent, Japan 13.1 per cent, United States 4.6 per cent, Iran 6.3 per cent and India 4.8 per cent.[6]

Going back to data provided in Table II.1. it will be observed that the rate of growth in East African foreign trade (both exports and imports) was greatest between the end of World War II and

5. China, Hong Kong and India figure significantly in the domestic exports of East Africa because of one export commodity alone—raw cotton. In fact China is a completely new market for East Africa, and this seems to be due to this country's deliberate switch from buying Russian cotton.

6. Iran, an underdeveloped country, is an important source of East African requirements of petroleum products. However, India figures here because she exports quite a lot of cotton piece-goods to East Africa. This, incidentally, indicates that some underdeveloped countries are more industrialised than others—even given similar per capita income levels.

1952: exports increased five times and imports seven times in value.[7] From 1952 there was an abrupt fall in the value of exports, and after a mild recovery this was followed by a period of relative stagnation up to 1958: in 1958 the value of East African domestic exports was £3 million less than it had been in 1952. The fall in the value of these exports was due to a tremendous fall in the prices offered for them in foreign markets. In fact, but for the steady increase in quantities exported, the value of exports would have fallen even more drastically. However, in 1963 there was a pronounced improvement in world prices, notably for robusta coffee, and this improvement in prices was primarily responsible for the increase of more than £31.5 million in the value of exports in 1963 over their value in the previous year.

This brings us to another important characteristic of East African export earnings, namely their marked fluctuations. Looking at both exports and imports, it will be observed that whereas imports increased fairly steadily (except for the phenomenal rise in 1955, due to the relaxation of the use of Mombasa harbour coupled with a great backlog of demand), exports have been characterized by frequent and often substantial fluctuations. This is a common feature in those underdeveloped countries which depend on one or two primary products for their export earnings. The causes of these fluctuations are twofold: instability in (*a*) the output of the important commodities, and (*b*) the prices at which these commodities sell in foreign markets. However, as already indicated, the fall in the value of exports in East Africa after 1952 was mainly due to the fall in prices, and fluctuations in the value of exports are also mainly explained by changing world prices. Looking at the period 1954 to 1962, the quantity exported increased by 71 per cent, while the unit value declined by 24 per cent; thus if prices had remained constant the value of these exports would have been about £166 million in 1962 instead of the £126.8 million actually recorded.

However, it seems likely that, due to both national and inter-

7. These East African totals conceal great differences in the individual countries' increase in both exports and imports. In both Uganda and Tanganyika the value of exports increased very fast due to these countries' bigger quantities of the chief East African primary exports—coffee and cotton in the case of Uganda, and sisal in the case of Tanganyika. In fact Kenya's percentage share in the total value of East African domestic exports fell from 34 per cent in 1939 to 22 per cent in 1952, while Uganda's share increased from 33 per cent to 39 per cent, and Tanganyika's also from 33 per cent to 39 per cent. On the side of imports, however, Kenya's percentage share averaged over 50 per cent in this whole period.

national efforts, the export earnings of East Africa will not again fall as abruptly as they did after 1952. Internationally the International Coffee Agreement will probably prevent disastrous falls in the price of this important commodity,[8] and nationally the three East African countries are trying hard to diversify their foreign exports. If then we assume that the rate of growth in the value of exports will be 4.5 per cent per year—the rate achieved between 1953/55 and 1961/63—then by 1973 exports should be about £194 million. On the other hand, in order to achieve the rather high rates of growth which these countries are planning for—6 to 8 per cent per year in gross domestic product—the imports required will soon outrun export earnings unless the value of exports increases faster or there is tremendous success in import substitution. The main point, therefore, is that the three East African countries should try hard to promote their exports, while at the same time carrying out a vigorous programme of import substitution. At this stage these two aims are not really competitive or mutually exclusive.

Another observation we should make about East African foreign trade is that domestic exports are of crucial importance in determining the level of gross domestic product. In a broad aggregative fashion we can think of a country's gross domestic income as the income generated in producing goods for consumption, investment, and export minus imports, i.e.:—

$$Y=C+I+E-M$$

where Y stands for gross domestic income, C for consumption, I for investment, E for exports, and M for imports. In East Africa the importance of foreign exports in the monetary gross domestic product is indicated in Table II.2 for each country for the period since 1954. For East Africa as a whole the ratio of domestic exports to monetary gross domestic product has been consistently between 30 and 35 per cent. The importance of domestic exports, moreover, is even greater in Uganda and Tanganyika. Between 1954 and 1963, while the ratio of domestic exports to gross domestic product averaged 20 per cent in Kenya, in Uganda the average was 40 per cent and in Tanganyika 45 per cent. In the earlier years not shown in the table, these ratios were even higher: during the Korean War commodity boom, for instance, domestic exports were over 60 per cent of Uganda's gross domestic product.

8. East Africa, however, will still face the problem of disposing of her coffee output—for output is increasing fast while her quota under the International Coffee Agreement is small, especially for Kenya.

TABLE II.2

Monetary G.D.P. at Factor Cost and Domestic Exports, 1954-63
(*£ million*)

	1954	1955	1956	1957	1958	1959	1960	1961	1962	1963
KENYA										
Monetary G.D.P. (A) ..	112.5	134.7	145.2	154.2	155.5	161.8	175.3	176.8	180.9	193.3
Domestic Exports (B) ..	20.3	25.7	29.0	26.4	29.3	33.3	35.2	35.3	37.9	43.8
B% A	18.1	19.1	20.0	17.1	18.8	20.6	20.1	20.0	21.0	22.6
UGANDA										
Monetary G.D.P. (A) ..	92.8	102.0	102.8	109.4	106.3	107.7	110.5	111.2	107.9	128.7
Domestic Exports (B) ..	40.6	41.9	40.4	45.9	45.4	42.1	41.6	39.2	37.6	51.5
B % A	43.8	41.1	39.3	42.0	42.7	39.1	37.6	35.3	34.8	40.0
TANGANYIKA										
Monetary G.D.P. (A) ..	79.1	81.8	89.3	92.9	97.9	106.2	114.4	113.5	123.3*	140.3*
Domestic Exports (B) ..	36.2	36.2	44.9	39.4	41.7	45.3	54.9	48.6	51.2	63.6
B % A	45.8	44.2	50.3	42.4	42.6	42.7	48.0	42.8	41.5	45.3
EAST AFRICA										
Monetary G.D.P. (A) ..	284.4	318.5	337.3	356.5	359.7	375.7	400.2	401.5	412.1	462.3
Domestic Exports (B) ..	97.1	103.8	114.3	111.7	116.4	120.7	131.7	123.1	126.7	158.9
B % A	34.1	32.6	33.9	31.3	32.4	32.1	32.9	30.7	30.7	34.4

* Revised series.

Source: *Statistical Abstracts.*

Table II.2 also suggests that variations in gross domestic product are associated with variations in domestic exports. Looking at Uganda, for instance, we notice that the stagnation in her gross domestic product between 1957 and 1962 was associated with a steady fall in export earnings; during that period the value of her exports fell by £8.3 million, and her gross domestic product fell by £1.5 million. But in 1963 there was a tremendous recovery in her gross domestic product—an increase of £20.8 million—and this recovery was largely due to an increase of £13.9 million in exports. In Tanganyika the close association between exports and gross domestic product is also apparent.

The dependence of a country's gross domestic product on foreign exports is often deplored, and also taken to be an indicator of the country's stage of economic development. However, starting with the latter point we can say that the ratio of exports to gross domestic product is only slightly correlated to a country's stage of development; what is more directly linked is the ratio of exports of *primary products* to the country's gross domestic product. For the three East African countries, and especially Uganda and Tanganyika, exports of primary products (which constitute nearly all their foreign exports, as noted earlier) are a very high proportion of their respective gross domestic products. The three countries not only depend a great deal on exports of a few primary products for their gross domestic incomes, but they also depend heavily on foreign imports for their total consumption.[9]

The dependence of the three East African countries on foreign exports *is not bad in itself*, but it does pose significant development problems, essentially for the following two reasons. (i) The earnings of these domestic exports are not large enough for the investment problems at hand, nor can they be expected to increase substantially in the next few years. For all these commodities world supply is chronically above world demand, and this is likely to continue to be so

9. Even for Kenya—which is taken to be more developed than Uganda or Tanganyika—it is estimated that perhaps as much as 40 per cent of the goods purchased domestically are imported, while over 30 per cent of the goods produced domestically are sold abroad (including intercountry trade). See Government of Kenya, *The Growth of the Economy 1954-1962*, Economics and Statistics Division, Ministry of Finance and Economic Planning, December, 1963, page 2.

unless world supply is cut down and consumption stepped up.[10] To illustrate: in order to solve the world coffee problem (existence of large stocks, large potential capacity, and prevalence of low prices) the producers would have to restrict their output, while the consumers would have to abolish the tariffs and internal duties which they now impose on coffee imports—and thus stimulate coffee consumption. It is because of the disequilibrium between world supply and demand for the major East African export commodities that these three countries cannot expect export earnings from their traditional commodities to improve substantially in the next decade or so. The tremendous increase in export earnings in 1963 should not be taken to be a permanent up-turn, for of the total increase of £32 million, £7.7 million was due to coffee, £9.4 million to cotton, and £10.2 million to sisal. These are commodities which, looking at the world supply and demand conditions, cannot be expected to do very well in future.[11]

(ii) The second reason why dependence on a few export commodities is a weakness in the East African economy is that it makes the prosperity and general level of economic activity here vulnerable to world price fluctuations and vagaries of nature. It is partly to seek greater stability that attempts to increase intercountry trade (and therefore development through import substitution on a wide front) should be intensified.

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10. For an excellent discussion on production and export prospects for most agricultural commodities, see F.A.O., *Agricultural Commodities Projections for 1970*, F.A.O. Commodity Review 1962, Special Supplement, E/CN.13/48 / CCP 62/5.

11. These increases were the result of increases in quantity and some recovery in prices (although the prices offered for arabica coffee actually declined further in 1963). Although East Africa is able to maintain, and indeed increase, the outputs of these commodities, the prices are unlikely to continue improving. Moreover, in the case of coffee there is the major problem of a small quota.

The improvement in the price of robusta coffee seems to have been due to a combination of special factors: the frost in Brazil, plus the fact that coffee merchants felt that, although coffee stocks would be available to meet their contract requirements, it would not be of sufficiently good quality. The slight panic which resulted led to an unsustainable rise in coffee prices.

CHAPTER III

INTERCOUNTRY TRADE IN FOREIGN IMPORTED GOODS

In this short chapter we are going to examine what has come to be a substantial part of intercountry transactions in East Africa: namely, trade in foreign imported goods. In East Africa there is free transfer of foreign imported goods, dating back to 1927 when it was also agreed that the customs revenue collected on transferred goods would be credited to the consuming country. Thus foreign goods directly consigned to, say, Kenya may subsequently be transferred to Uganda and Tanganyika. Therefore, in order to get the net foreign imports of each country we have to add (or subtract where appropriate) these transfers to the direct imports of the country in question.

For statistical reasons it is difficult to work out the proportion of *gross* transfers in intercountry trade. In fact from the published figures the only way of estimating this trade is to subtract direct imports from net imports and thus get the *net* transfers; although in the offices of the East African Customs and Excise Department all declarations of transfers, which are required by law, are available. But there is little doubt that the proportion of goods in this trade is much larger than what one would infer from net transfers, and it is likely that something like a quarter of all imports from foreign countries are consumed in countries other than those to which they were directly consigned. However, it is net transfers which are important for the purposes of customs revenue distribution.

Table III.1 shows the value of each country's direct imports, net imports, and net transfers for the years 1956 to 1963. In Table

TABLE III.1

Direct Imports, Net Imports and Net Transfers, 1956-63
(*£ thousand*)

KENYA

	Direct Imports	*Net Imports*	*Net Transfers*
1956	84,615	69,823	+14,792
1957	87,995	72,003	+15,992
1958	77,029	60,869	+16,160
1959	78,820	61,508	+17,312
1960	89,971	70,069	+19,902
1961	88,672	68,937	+19,735
1962	91,254	69,494	+21,760
1963	96,398	73,688	+22,710

UGANDA

	Direct Imports	Net Imports	Net Transfers
1956	16,185	28,106	—11,921
1957	17,603	28,869	−11,266
1958	15,782	27,002	−11,220
1959	14,338	25,534	—11,196
1960	14,422	26,030	−11,608
1961	14,850	26,546	−11,696
1962	14,164	26,206	−12,042
1963	18,213	30,922	−12,709

TANGANYIKA

	Direct Imports	Net Imports	Net Transfers
1956	33,013	35,885	− 2,872
1957	34,548	39,275	− 4,727
1958	28,630	33,568	− 4,938
1959	28,339	34.455	− 6,116
1960	29,523	37,817	− 8,294
1961	31,648	39,686	− 8,038
1962	30,099	39,817	— 9,718
1963	30,418	40,418	−10,000

Source: *Annual Trade Reports.*

TABLE III.2

Net Transfers as % of Direct or Net Imports, 1956-63

	KENYA [a]	UGANDA [b]	TANGANYIKA [b]
1956	−17.7	+42.4	+ 8.0
1957	−18.2	+39.0	+12.0
1958	−21.0	+41.6	+14.7
1959	−22.0	+43.8	+17.8
1960	−22.1	+44.6	+21.9
1961	−22.3	+44.1	+20.3
1962	−23.8	+46.0	+24.4
1963	−23.6	+41.1	+24.7

a.—Per cent of direct imports.
b.—Per cent of net imports.

Source: *Annual Trade Reports.*

III.2 net transfers, as percentage of direct or net imports, are shown for each country for the period 1956 to 1963.

Several comments and observations can be made on these figures. First, it will be seen that the flow of these transfers is mainly in one direction—from Kenya to the rest of East Africa. In 1963 nearly 24 per cent (£22.7 million) of Kenya's direct imports were subsequently transferred to Uganda and Tanganyika, with Uganda taking £12.7 million and Tanganyika £10.0 million. The reasons for this phenomenon seem to be twofold: (*a*) Kenya has a fine modern harbour at Mombasa whereas Uganda is completely landlocked

and northern Tanganyika is more easily served by Mombasa than Dar es Salaam. Thus the distributors in Uganda and some parts of Tanganyika depend on the Nairobi importers for their supplies. (*b*) Kenya has large and well-established importing firms which consider the whole of East Africa as their market. This point is further strengthened by the fact that in East Africa there are some large companies which operate in all three countries, usually with headquarters in Kenya, and since there is free movement of foreign imported goods they use their Kenya headquarters for supplying their other outlets in the rest of East Africa. Examples of such firms are the motorcar and oil companies.

Secondly, both the volume and the relative importance of this trade have been increasing steadily. Thus whereas in 1956 Kenya transfers to Uganda and Tanganyika were £14.8 million, by 1963 the value of these transfers had increased to £22.7 million. In percentage terms Kenya transferred 17.5 per cent of her direct imports to Uganda and Tanganyika in 1956, but by 1963 this proportion had risen to 23.6 per cent. This has meant that in Uganda and Tanganyika transfers have been of increasing importance in their net imports. In Uganda, imports through transfers in 1956 were 42.4 per cent of net imports; in 1962 this proportion had gone up to 46.0 per cent. However, the main point is that between 1956 and 1963 Uganda has been getting an average of 42.8 per cent of her total imports in the form of transfers, almost entirely from Kenya, with a tendency for this proportion to rise. In Tanganyika the increasing importance of this transfer trade, both in volume and relatively, has also been very marked. In 1956 net transfers to this country were only £2.9 million, or 8.0 per cent of her net imports; but by 1963 these figures were £10.0 million and 24.7 per cent respectively.

The increasing importance of transfers in the net imports of Uganda and Tanganyika is fundamentally a reflection of the increasing effectiveness of the common market. But there are other specific reasons for this growth. In Uganda, for instance, it is said that the increasing importance of transfers in bicycle imports since 1956 (in 1956 net imports of bicycles were 1.3 times direct imports; in 1963, 3 times) has been "due to a change in the trading channels which was itself due to the slackening demand (for bicycles). As the current demand for bicycles is now relatively low, some companies

retain all reserve stocks in Kenya and forward to Uganda only against definite orders."[1] This, of course, applies to many other goods, and not only to bicycles. The distributors in Uganda and northern Tanganyika, by ordering goods from Kenya only against definite demand, reduce their operating costs by not having so much of their capital tied up in stocks. In fact the process feeds on itself: since supplies are available in Kenya and can be brought in, at no extra duty, the sellers in Uganda and northern Tanganyika do not want the risk of carrying large stocks. Of course, the Kenya importer and "stockholder" charges a commission for undertaking the risk, having his capital tied up, and breaking the bulk. This transfer trade is also affected by changes in the country of origin of imports. For example, where a government licence is required to import certain goods from a certain country, the ratio of direct imports to net imports is very high.

An indication of the commodity composition of this transfer trade is given in Table III.3. In this table selected transfers as percentage of direct imports for Kenya and of net imports for Uganda and Tanganyika, are shown for the year 1963. It may be noticed that Kenya transfers to the rest of East Africa 40 per cent or more of her direct imports of motor spirit, lubricating oils and greases, kerosene, salt, rubber tyres and tubes, cotton fabrics, synthetic fabrics, sewing machines, bicycles, clothing, footwear and matches. Correspondingly, these are also the most important articles in the transfer inflows in Uganda and Tanganyika. For example Uganda does not directly import *any* aviation spirit, motor spirit, kerosene, diesel and other fuel oils, while her direct imports of the rest of the articles listed above are much smaller than transfer inflows.

The growth of transfer trade among the three countries, as indicated in Table III.1, raises two major problems in the analysis of East African trade. Firstly, it makes it very difficult to estimate each country's balance of payments, for several reasons. (i) Certainly not all transfers are declared and recorded, although this is required by law; perhaps as much as 10 per cent are unrecorded. Coverage on transfers varies significantly from commodity to commodity. For bulky and heavy goods which must go by railway, coverage

1. Uganda Government, *The External Trade of Uganda, 1950-60*, Entebbe, June 1962, page 10.

TABLE III.3

Selected Transfers 1963
(£)

COMMODITIES	KENYA Net Imports(C)	KENYA Direct Imports(A)	KENYA Transfers B	KENYA B%A	UGANDA Net Imports(C)	UGANDA Direct Imports(A)	UGANDA Transfers B	UGANDA B%C	TANGANYIKA Net Imports(C)	TANGANYIKA Direct Imports(A)	TANGANYIKA Transfers (B)	TANGANYIKA B%C
1. Milk and cream, tinned	324,704	432,378	−107,674	24.9	243,293	153,169	90,124	37.0	816,681	799,131	17,550	2.1
2. Sugar, beet and cane	790,073	799,099	−9,026	1.1	7,619	2,927	4,692	61.6	565,387	561,053	4,334	0.8
3. Wines	171,413	261,263	−89,850	34.4	48,587	8,496	40,091	82.5	71,298	21,539	49,759	70.0
4. Ale, beer, cider, and stout	105,587	145,209	−39,622	27.3	41,058	4,333	36,725	89.4	33,475	30,578	2,897	8.7
5. Liqueurs and other alcoholic beverages	12,797	18,868	−6,071	32.2	3,264	332	2,932	89.8	4,048	909	3,139	77.5
6. Tobacco manufactured (including cigarettes and cigars)	125,974	173,818	−47,844	27.5	29,183	1,499	27,684	94.9	21,996	1,836	20,160	91.7
7. Salt	73,527	153,988	−80,461	52.3	164,313	85,019	79,294	48.3	29,417	28,250	1,167	4.0
8. Aviation spirits	337,104	502,127	−165,023	32.9	118,965	—	118,965	100.0	75,296	29,238	46,058	61.2
9. Motor spirits	1,281,826	2,559,550	−1,277,724	49.5	938,012	—	938,012	100.0	929,874	590,162	339,712	36.5
10. Kerosene	1,177,615	1,842,589	−664,974	36.1	484,735	—	484,735	100.0	564,585	384,346	180,239	31.9
11. Gas, diesel and other fuel	3,556,075	4,457,943	−901,868	20.2	552,897	—	552,897	100.0	1,680,642	1,331,671	348,971	20.8
12. Lubricating greases	83,012	138,094	−55,082	39.9	31,820	1,228	30,592	96.1	54,654	30,164	24,490	44.8
13. Lubricating oils (all types)	380,310	812,906	−432,596	53.2	193,562	17,893	175,669	90.8	335,621	78,694	256,927	76.6
14. Medicinal and pharmaceutical products	1,302,865	1,884,664	−581,799	30.9	589,505	333,319	256,186	43.7	767,824	442,211	324,613	42.3
15. Disinfectants, insecticide cattle dips and similar preparations	807,739	1,088,627	−280,888	25.8	175,493	46,207	129,286	73.7	304,775	153,173	151,602	49.7
16. Rubber tyres and tubes	1,065,295	1,819,394	−754,099	41.4	911,892	397,472	514,420	56.4	887,192	647,513	239,679	27.0
17. Paper, paperboard and manufactures, thereof	3,019,217	3,388,614	−369,397	10.9	481,843	287,762	194,081	40.3	589,292	413,379	175,913	29.9
18. Cotton fabrics (piece goods) all types	2,677,140	4,849,787	−2,172,647	44.8	1,990,935	914,433	1,076,502	54.1	3,939,674	2,843,529	1,096,145	27.8
19. Fabrics of synthetic fibres including artificial silk	2,343,969	4,212,948	−1,868,979	44.4	2,113,074	1,173,889	939,185	44.4	1,480,059	550,265	929,794	62.8
20. Blankets and travelling rugs	830,248	1,254,091	−423,843	33.8	346,251	80,808	265,443	76.7	340,175	181,775	158,400	46.6
21. Non metallic mineral manufactures, other	763,488	978,422	−214,934	22.0	508,952	373,663	135,289	26.6	439,150	359,505	79,645	18.1
22. Iron and steel, all types	4,300,341	4,721,820	−421,479	8.9	958,713	650,432	308,281	32.2	1,623,109	1,509,911	113,198	7.0
23. Other base metals and manufactures of base metals	4,024,758	4,891,000	−866,242	17.7	1,560,601	1,014,015	546,586	35.0	2,006,927	1,687,271	319,656	15.9
24. Agricultural machinery and implements	381,889	537,049	−155,160	28.9	180,377	104,638	75,739	42.0	385,287	305,866	79,421	20.6
25. Tractors, including agricultural	700,138	898,236	−198,098	22.1	216,822	140,231	76,591	35.3	694,731	573,224	121,507	17.5
26. Sewing machines other than electrical	353,910	719,784	−365,874	50.8	220,221	1,977	218,244	99.1	254,996	107,366	147,630	57.9
27. Industrial and commercial machinery	6,175,236	7,436,411	−1,261,175	17.0	2,285,781	1,587,981	697,800	30.5	2,799,858	2,236,483	563,375	20.1
28. Radio and television, all types	876,510	1,292,002	−415,492	32.2	504,669	289,181	206,488	40.9	425,492	216,488	209,004	49.1
29. Electrical machinery, apparatus and appliances	2,186,476	2,647,574	−461,098	17.4	1,220,020	963,408	256,612	21.0	1,730,303	1,525,817	204,486	11.8
30. Passenger road vehicles and chassis excluding buses	3,257,811	4,090,895	−833,084	20.4	1,743,873	1,058,132	685,741	39.3	1,640,858	1,493,515	147,343	9.0
31. Buses, trucks, lorries, vans and chassis	2,189,454	3,217,762	−1,028,308	32.0	1,414,816	918,986	495,830	35.0	1,764,898	1,232,420	532,478	30.2
32. Bicycles	137,260	297,020	−159,760	53.8	161,141	54,003	107,138	66.5	295,376	242,754	52,622	17.8
33. Other transport equipment	2,244,644	3,155,018	−910,374	28.9	1,344,679	872,195	472,484	35.1	1,274,601	836,711	437,890	34.4
34. Clothing	1,547,496	2,903,160	−1,355,664	46.7	1,235,864	584,323	651,541	52.7	1,213,848	509,725	704,123	58.0
35. Footwear	188,438	366,463	−178,025	48.6	175,915	77,227	98,688	56.1	188,649	109,312	79,337	42.1
I. Total transfers of selected commodities			−19,154,234				10,990,567				8,161,264	
II. Total of all transfers			−22,709,151				12,709,046				10,000,002	
Total I as % of total II			84.3				86.4				81.6	

Source: *Annual Trade Report*, 1963.

can be assumed to be complete. However, for smaller and lighter goods which can be carried by trucks or in passenger cars, substantial percentages may be unrecorded. A notable example is second-hand motor-cars. Second-hand cars are cheaper in Nairobi than in Kampala—not only because of the transport costs involved (about £30 per car), but also because of the concentration of higher incomes in Nairobi, with the result that there are more second-hand cars in the Nairobi market. The supply has been further increased in the last few years by the emigration of expatriates from Kenya, and also by the recent phased departure of British troops. Second-hand cars being cheaper in Nairobi, some people from the rest of East Africa, especially from Uganda, travel to Kenya to buy cars there and drive them back. If all these cars were re-registered in Uganda (or Tanganyika, as the case may be), the trade data could be adjusted for these transfers; but it is certainly the case that only a proportion of these cars are re-registered, and then only after a considerable period of time.

(ii) The Kenya distributors charge a mark-up on transfers to Uganda and Tanganyika. Broadly speaking we can distinguish two main categories of this trade as regards the size of the mark-up: (a) those goods transferred in their original packages; (b) those goods transferred after bulk-breaking. In each category the mark-up will depend on the costs of holding stocks, the risk undertaken, and the degree of bulk-breaking which takes place. The main problem here is to get the exact value of these mark-ups. In the Annual Trade Reports, in the case of goods transferred in their original packages, the consuming country is credited with the cost of the goods at the time when the goods in question were originally imported. This procedure thus leaves out the mark-up, as well as transportation costs. In the case of goods transferred after bulk-breaking, the consuming country is generally given 70 per cent of the value declared by the consignor; thus 30 per cent of the value declared is taken to be an additional charge by the consignor.

(iii) The transport costs charged are also difficult to estimate, especially when goods are transferred by road.

For these reasons there are grave statistical difficulties in estimating the balance of payments of each East African country alone. (We shall return to this problem in Chapter V.) They also represent a great gap in our knowledge on intercountry trade.

The second major problem arising from the growth of this transfer trade is the proper country allocation of customs revenue. Ideally each country should get the customs revenue on all foreign imports consumed within her borders; but, as we have seen, it is difficult to arrive at the total foreign imports consumed. For the *recorded* transfers, in cases where goods are transferred in their original packages, the convention adopted is that the consuming country gets the amount of duty collected at the time of importation; here the problem of customs revenue allocation is relatively easy. The main problem is with goods transferred after bulk-breaking. Here the convention adopted is that after the value of transfers declared by the consignor has been deflated by 30 per cent (in order to exclude the mark-up), the consuming country gets, in the case of goods subject to *ad valorem* duties, the appropriate *ad valorem* rate on 70 per cent of the value, or in the case of goods subject to specific rates of duty, the amount of duty collected at the time of importation.[2] This convention works reasonably well for goods with normal duties; but where the duty is unusually high the trade figures of the consuming country may be inflated and those of the transferring country deflated, since the selling price includes the high duty paid at the time of original importation. In order to avoid this, in the case of goods liable to high rates of duty (e.g., spirits, cigarettes, cigars, motor spirit), the value credited to the consuming country is the *average* landed costs of such goods at the port.

These devices, although rough, try to deal with a very important problem; for the three countries depend quite heavily on customs duties for their revenue. In 1963 Kenya, Uganda, and Tanganyika got £15.1, £9.3, and £11.0 million respectively from import duties; and of Uganda's and Tanganyika's revenue £5.6 million and £3.7 million respectively were transferred by Kenya because of this transfer trade. These are substantial sums, and their accurate allocation is of great importance, not only to Uganda and Tanganyika (the net recipients) but also to Kenya (the net transferrer). Obviously, as long as there is a common currency and only four customs posts on the water frontiers and two on the land frontiers between Kenya, Uganda and Tanganyika, it will still be possible

2. See *Annual Trade Report, 1963*, explanatory notes, page vi.

for goods to be transferred without transfer forms being completed. A complete solution to this whole problem would be total political integration of the three countries; but until that is achieved allocation of customs revenue will continue to be a source of political conflicts.

Two final observations on this trade are in order. (i) The goods transferred from one country to another indicate, albeit crudely, the sorts of goods which could in future be of great significance in East African intercountry trade. There are, of course, some items such as motor-spirit which will continue to be imported from foreign countries; but there are many manufactured goods such as textiles whose domestic production is capable of being considerably increased, and which would certainly find a market in East Africa. (ii) The existence of this trade and its rapid growth over the last decade or so brings out the scale advantages of Nairobi—the biggest city and commercial centre in East Africa. The increasing importance of the commercial sector in the Kenya economy owes a lot to the growth of this transfer trade.

CHAPTER IV

INTERCOUNTRY TRADE IN DOMESTIC PRODUCE AND MANUFACTURES

The object of this chapter is to discuss trade among the three East African countries in domestically produced and manufactured products. The idea was developed in a previous chapter that under-developed countries have to try their hardest to develop through their domestic markets and, therefore, political federations, customs unions, common markets, and other forms of cooperation among states are generally to be welcomed in developing countries. The East African countries already have a customs union which has developed into a *de facto* common market; in this chapter the contribution of this common market to the growth of intercountry trade will be examined.

Growth of Intercountry Trade

The volume of intercountry trade has been increasing very fast, especially after World War II. It is difficult to isolate the volume of this trade before the customs authorities of Kenya/Uganda and Tanganyika were amalgamated in 1949.[1] For instance, some of Tanganyika's exports to Kenya before 1949 were not intended for consumption in that country but for shipment to countries outside East Africa. However, it would seem that the volume of intercountry trade in 1939 was just over £1 million; in 1949 it had gone up to £7.3 million; in 1952 it was £11.1 million; and by 1963 it was £31.5 million. The rapid growth of this trade is best appreciated when seen against the growth of East African exports to other markets. In Table IV.1 the value of each country's intercountry exports, exports to the Neighbours, and exports to all other countries are shown for the period 1954 to 1963, as well as the East African totals.

Several observations emerge from these figures. Firstly, the fast growth of intercountry trade is apparent. This growth would appear even more rapid (which would be realistic) if the data of intercountry exports through 1958 did not include excise taxes and customs

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1. The customs departments of Kenya and Uganda were amalgamated in 1917 when the two countries decided to form a customs union. Tanganyika was then a German territory, and therefore was not a founding member of the East African customs union.

TABLE IV. 1

Value of Domestically Produced Exports of Kenya, Uganda and Tanganyika to various Markets, 1954-1963
(£ *thousand*)

KEY: A=Domestic Exports to countries other than the Neighbours.
B=Domestic exports to the Neighbours.
C=Total domestic exports.
D=Intercountry exports.
E=All domestically produced exports.

	1954	1955	1956	1957	1958	1959	1960	1961	1962	1963
KENYA										
A	18,945	24,508	27,839	25,109	28,059	31,695	33,234	33,332	35,544	41,245
B	1,315	1,159	1,144	1,252	1,241	1,611	1,957	1,994	2,369	2,587
C	20,260	25,667	28,983	26,361	29,300	33,306	35,191	35,326	37,913	43,832
D*	5,808	6,035	8,977	11,437	12,925	12,297	13,771	15,948	17,320	19,791
E	26,068	31,702	37,960	37,798	42,225	45,603	48,962	51,274	55,233	63,623
UGANDA										
A	39,067	40,234	38,456	43,807	44,275	40,820	40,011	37,805	36,183	49,600
B	1,508	1,668	1,962	2,050	1,134	1,271	1,577	1,390	1,452	1,875
C	40,575	41,902	40,418	45,857	45,409	42,091	41,588	39,195	37,635	51,475
D*	7,538	7,879	4,429	5,325	6,225	5,228	6,694	6,855	7,054	8,241
E	48,113	49,781	44,847	51,182	51,634	47,319	48,282	46,050	44,689	59,716
TANGANYIKA										
A	34,994	35,225	43,721	38,446	40,505	44,147	53,587	47,507	50,130	62,465
B	1,257	963	1,084	1,031	1,202	1,140	1,267	1,142	1,111	1,088
C	36,251	36,188	44,805	39,477	41,707	45,287	54,854	48,649	51,241	63,553
D*	1,053	1,701	2,087	2,031	2,603	2,574	2,324	2,233	2,391	3,423
E	37,304	37,889	46,892	41,508	44,310	47,861	57,178	50,882	53,632	66,976
EAST AFRICA										
A	93,006	99,967	110,016	107,362	112,839	116,662	126,832	118,644	121,857	153,310
B	4,080	3,790	4,190	4,333	3,577	4,022	4,801	4,526	4,932	5,550
C	97,086	103,757	114,206	111,695	116,416	120,684	131,633	123,170	126,789	158,860
D*	14,399	15,615	15,519	18,794	21,753	20,099	22,789	25,036	26,765	31,455
E	111,485	119,372	129,725	130,489	138,169	140,783	154,422	148,206	153,554	190,315

* Intercountry exports through 1958 include excise taxes on excisable commodities and customs duties on dutiable foreign imported inputs.

Source: *Annual Trade Reports.*

duties.[2] However, considering only the period 1959 to 1963, the value of intercountry trade has increased by £11.4 million, or by an annual growth rate of 11.6 per cent. At this rate the value of this trade would be about £94 million by 1973.

Seen against East African domestic exports to the Neighbours and the rest of the world, the increase in the value of intercountry exports is even more impressive. Exports to the Neighbours have not only been small (about one sixth of intercountry exports in 1963) but they have been fluctuating as well, although with some tendency to increase in recent years. Fluctuations have also been one of the main features of East African exports to the rest of the world; these exports rose from £93 million in 1954 to £127 million in 1960, then fell by £8 million in 1961, whence they increased by £3 million in 1962, and then increased by £31.5 million in 1963 to an all-time record of £153.3 million. The rate of growth of all East African domestic exports (i.e. to the Neighbours as well as to all other countries) was 3.3 per cent a year between 1954 and 1962, but 5.6 per cent between 1954 and 1963—because of the tremendous increase in 1963. This latter rate of growth is unlikely to be maintained in future, for the favourable circumstances of 1963 are unlikely to remain so favourable.[3] By comparison, intercountry exports have been increasing in value nearly every year. (The fall in 1956 was due to the fact that the East African Tobacco Company

2. Removal of excise taxes on cigarettes, tobacco, beer, and sugar was attempted for the period 1954 to 1958. The method used was to take each country's total excise tax revenue collected on each of these commodities in every year and divide by the number of units of each commodity consumed. This gave the average amount of excise duty collected on each unit of exisable commodity—and this rate was used to remove the excise duty element from intercountry imports. Removing only these excise taxes (but not import duties on various dutiable inputs used in local production), each country's intercountry exports were:

(£ *million*)

	1954	*1955*	*1956*	*1957*	*1958*
Kenya	5.53	5.74	7.61	9.70	10.75
Uganda	5.76	5.69	2.74	3.87	4.83
Tanganyika	1.22	1.68	2.06	2.58	2.59

3. See the discussion in Chapter II above. A reasonable estimate of the probable future rate, on average, is in the order of 4.5 per cent per year. This was the rate actually achieved in the period 1953/55 to 1961/63—a period which combined good years and bad years, the kind of pattern we can expect in future. For a fuller discussion on balance of payments prospects see Brian Van Arkadie and Philip Ndegwa, "Future Trade Balance of Payments and Aid Requirements of East Africa," Economic Development Research Project, Paper 31, 27th May, 1964, East African Institute of Social Research, Makerere University College.

moved its factory from Uganda to Kenya, and during this reorganisation cigarette production declined temporarily).

Another observation is that the relative shares of various markets for East African exports have been changing. The trends in the shares of intercountry exports, exports to the Neighbours, and exports to the rest of the world are summarised in Table IV.2

TABLE IV.2

Relative Shares of Various Markets for East African Domestic Exports

	1954	*1959*	*1962*	*1963*
A	100.0	100.0	100.0	100.0
B	83.4	82.9	79.4	80.6
C	3.7	2.8	3.2	2.9
D	12.9	14.3	17.4	16.5

where A = Intercountry exports+Exports to the Neighbours+Exports to the rest of the world.
B = Exports to all foreign countries other than the Neighbours as a percentage of A.
C = Exports to the Neighbours as a percentage of A.
D = Intercountry exports as a percentage of A.

These figures bring out more clearly the point made earlier that East African domestic exports to the Neighbours are small. In 1963 intercountry exports of Kenya, Uganda and Tanganyika were 7.6, 4.4, and 3.1 *times* these countries' exports to the Neighbours, respectively. As will be argued in a later chapter, unless deliberate measures are taken to increase trade with the Neighbours, East African exports to these countries will remain small, and very likely their relative share in total East African exports will fall further.

Looking at intercountry exports, on the other hand, it will be noticed that the percentage share of these exports in total East African exports has been increasing steadily, except when it fell slightly in 1963. This fall was not due to a decline in the value of these exports (in fact their value increased by more than £4.5 million from 1962 to 1963), but due to the tremendous increase in exports to the rest of the world already mentioned. If the rate of growth of intercountry exports recorded between 1959 and 1963 (11.6 per cent) is maintained, and if the rate of growth in exports outside East Africa is 4.5 per cent, intercountry exports will be over a quarter of total exports within ten years. The significance of this trend to an economy at present so heavily dependent on exports of a few primary products to a few markets, can hardly be exaggerated, for it introduces a strong possibility of stability. The economy will

become increasingly dependent on local demand for its level of economic activity, instead of unpredictable world prices for a small range of primary commodities. Some progress towards this possibility has already taken place: in 1950 intercountry exports as a percentage of monetary output for local consumption (i.e. monetary GDP minus domestic exports) were 5.5 per cent, but by 1962 this ratio had gone up to 9.5 per cent.

Several factors have facilitated the growth of intercountry trade. First, a factor of great importance has been the existence of better means of transport by road, rail and water among the three East African countries than between East Africa and the Neighbours. For instance, there are no rail or all-weather road connections between East Africa and any of the neighbours. Cheap and reliable means of carrying goods encourage trade directly by opening up new areas of demand and indirectly by lowering the prices of goods sold. Any measure designed to increase East African trade with the Neighbours surely must include an improved transportation and communication system, not only in building trans-frontier roads and in some cases railways, but also in standardisation of highway codes.

Secondly, the existence of a common currency in East Africa has been helpful.[4] The existence of different currencies in the world does not hinder trade as much as is commonly alleged; where there is a fixed exchange rate, like the gold standard, differences in currencies are of comparatively little importance. But in underdeveloped countries differences in currencies have a more than peripheral effect on trade, especially when this involves small traders and producers. This has certainly been true in the case of East African trade with the Neighbours; the problem has been reinforced by currency instability in some of the Neighbours, notably Congo and Rwanda.

The most powerful factor in the expansion of intercountry trade, however, has been the existence of a common market and some intercountry economic cooperation. The mere existence of a customs union, *by itself*, is not sufficient; it is only when the opportunities it offers are seized and industries established, in most cases initially based on import substitution, that its effect on intra-union trade becomes significant. This explains why intercountry trade in East Africa has become important only recently, although a *de facto* common market has been in existence for more than forty years.

The emergence of new domestically produced goods in East Africa has been facilitated by protection. As we shall see below, some agricultural products and manufactured goods have been taking an increasing share of intercountry exports, and these goods are effectively protected. Among food products, for instance, bacon, ham, condensed milk and cream, cheese, ghee, and wheat are all protected by a duty of $33\frac{1}{3}$ per cent *ad valorem*; while butter, biscuits, margarine, sugar, confectionery, and a few others are protected by a duty of $25\frac{1}{2}$ per cent *ad valorem*. By stimulating production, protection has led to an increase in intercountry trade directly, for protection is done on an East African basis. In East Africa after the initial difficulties of the early post-war period (shortage of staff, capital equipment, materials, together with increased costs of imports in post-war world economic expansion), investment to produce new goods (e.g., bicycle tyres, shoes, cement) and more of the old ones (e.g., soaps, clothing) increased tremendously. This investment, with protection, led to a rapid increase in intercountry trade, especially because the producers were operating on scales designed to supply the whole of the East African market and not just each individual country.

The discussion so far would tend to give the impression that intercountry trade has been expanding at the maximum possible rate. This is far from the truth. Trade could have increased even faster but for two factors: (*a*) the existence of special statutory regulations controlling the movements and prices of some products;[5] (*b*) the absence of really significant economic coordination in the whole area.

In the case of special statutory regulations, there are several Marketing Boards, especially in Kenya, which control the sale and prices of a whole range of agricultural products. In some cases the internal prices charged are higher than the prices these products fetch in foreign countries, and it could be argued that had the prices been lower, this could have stimulated greater demand and therefore

4. There has been, unfortunately, a break-up of the common currency. The three Governments announced, during the presentation of 1965/66 budgets, their intentions of introducing separate currencies.

5. These are what the Economic and Fiscal Commission to East Africa referred to as "artificial impediments to trade". *Report of the Economic and Fiscal Commission*, H.M.S.O., Cmnd 1279, 1961, page 62. This commission is hereafter referred to as the Raisman Commission, after its chairman, Sir Jeremy Raisman.

more trade. However, for the most part the internal prices are not higher than import prices. If they had been higher than import prices, then protection would have taken the form of quantitative restrictions; the only important commodity where this has been true is wheat. However, the most serious obstacle to the faster growth of intercountry trade has been the existence of controls over certain commodities by individual governments. For instance, Kenya prohibits imports of maize from Uganda or Tanganyika, while in these two other countries there are stringent regulations controlling imports of livestock. Needless to say such regulations and controls are not in keeping with the principles of a common market. Since controls hindering intercountry trade have been confined to agricultural products, removal of these controls would presumably lead to an upsurge in the volume of agricultural products in intercountry trade, and would encourage the process of specialisation in production.

In the case of factor (*b*), i.e. the absence of effective economic coordination among the three countries, the result has been independent development strategies and different marketing policies. There is little doubt that had there been more coordination in the development efforts of these three countries, intercountry trade expansion would have been even greater. One of the main sources of conflict has been that, whereas a *de facto* common market has existed, there has not been a common economic policy in other spheres. This is a point which will be discussed later.

Another unfavourable factor has been that since the middle fifties the growth in incomes per head has been very small, especially in Uganda and Tanganyika, compared with the immediate post-war period and early fifties. In fact in Uganda the monetary gross domestic product fell from £109.4 million in 1957 to £106.4 million in 1962. In the same period the increase in monetary gross domestic product was only £22.1 million in Tanganyika, and only £25.8 in Kenya.[6] The sluggishness in individual incomes limits demands, though this seems to affect foreign imports more than domestically produced goods.

6. This disappointing performance in the economies was due both to poor performance in the value of their domestic exports after the Korean War commodity boom (as has already been seen) and to an actual fall in gross capital formation—from nearly £92 million in 1955 to £75.6 million in 1962. In 1963 gross capital formation fell further to £73.5 million.

Commodity Composition of Intercountry Trade

In this section we are going to examine the commodity composition of East African intercountry trade in the last few years. Because of the statistical difficulties noted in the last two chapters, emphasis will be given to the period 1959 to 1963 (when data on various years are wholly comparable), referring to earlier years only to indicate *roughly* the shifts in relative importance of various commodities in this trade. Moreover, we shall concentrate on exports. It hardly needs pointing out that since East Africa is an underdeveloped economy, her imports will be mainly manufactured goods (consumer and producer goods) and fuel—for so far no oil deposits have been discovered in East Africa. In 1963 of her total imports of £145 million, manufactured goods in SITC sections 5-8 accounted for £111 million.

The comparative structure of East African intercountry exports, exports to the Neighbours, and exports to the rest of the world is shown in Table IV.3.

TABLE IV.3

Commodity Distribution of East African Intercountry Exports (A) Domestic Exports to the Neighbours (B) and Domestic Exports to other Countries (C).
1959 and 1963
(percentages)

	1959			*1963*		
SITC	*A*	*B*	*C*	*A*	*B*	*C*
0. Food	30.8	58.9	43.8	28.3	62.6	44.6
1. Bev. & Tob	23.5	1.0	—	14.5	0.9	—
2. Crude mater. ..	3.6	15.6	45.0	2.9	11.4	45.9
3. Fuels	1.4	—	—	1.4	0.1	—
4. Oils & fats	8.0	4.9	0.4	4.4	1.9	0.2
5. Chemicals	5.7	3.4	2.5	8.7	3.5	1.5
6. Mfd. prod.	18.2	13.7	7.0	26.2	14.9	6.5
7. Machinery	0.5	0.6	—	0.7	0.9	—
8. Misc. mfd.	8.0	1.9	0.1	12.8	3.6	0.2
9. Other	0.4	—	1.1	—	0.2	1.0
0—4.	67.3	80.4	88.2	51.5	76.9	90.7
5—9.	32.7	19.6	11.8	48.5	23.1	9.3

Source: *Annual Trade Reports.*

In discussing the commodity composition of exports to these three markets, it will simplify the analysis to regard SITC sections 0—4 as primary products (which is by and large true, although we should keep in mind that section 0 includes some manufactured foods such as biscuits and confectionery; section 1 includes manufactured tobacco products; and section 2 includes pyrethrum extract)

and sections 5-9 as manufactured products (which is again broadly true, although section 6 includes base metals and section 9 includes gold).

One major observation we can make from Table IV.3 is that East African domestic exports both to the Neighbours and to all other countries are concentrated in sections 0-4. Thus in 1963 these five sections accounted for 76.9 per cent of exports to the Neighbours and 90.7 per cent of exports to the rest of the world. It will also be noticed that within these five sections the two overwhelmingly important ones are sections 0 (Food) and 2 (Crude materials). In SITC section 0 the main commodity is coffee, which in 1963 contributed slightly over 28 per cent of total domestic exports. The importance of coffee, incidentally, explains why food exports to the Neighbours are relatively large, although these countries are at broadly similar stages of development as East Africa. In 1963 22 per cent of exports to the Neighbours were coffee, virtually all of it to the Sudan. In SITC section 2 the major items are sisal and raw cotton. In 1963 they contributed £55.7 million, or 35 per cent of total domestic exports.

The large share of SITC sections 0-4 in East Africa domestic exports to the Neighbours and other countries means that manufactured exports to these markets are small. But it is most significant to notice that exports of manufactured goods are relatively more important among exports to the Neighbours than in exports to the other countries—mainly developed countries. In fact the contrast would be even greater if copper, diamonds, and gold (exported to the industrial nations and worth nearly £9 million in 1963) were excluded from manufactured goods. Moreover, we should also notice that the relative importance of manufactured goods among East African exports to the Neighbours has risen in the last five years—from 19.6 per cent in 1959 to 23.1 per cent in 1963. These two points underline a very important fact, namely that underdeveloped countries are more likely to find markets for their manufactured goods in other underdeveloped countries, rather than in the developed industrial countries where competition is keen and tastes are sophisticated.

Against this concentration on primary exports in trade with the Neighbours and the rest of the world, we need to notice the substantial importance of manufactured goods in intercountry exports.

Manufactured goods (i.e. SITC sections 5-9) have increased their percentage share in these exports from 32.7 per cent in 1959 to 48.5 per cent in 1963. What this means is that the process of industrialisation in East Africa so far has depended tremendously on the domestic market—a market which has been enlarged considerably by the existence of the common market (and protection). East Africa as a whole has a population three and a half times that of Uganda, about three times that of Kenya, and about two and a half times that of Tanganyika. Moreover, as far as monetary gross domestic product is concerned, the East African total is 2.4 times that of Kenya, 3.3 times that of Tanganyika, and 3.6 times that of Uganda. Consequently, East Africa as a whole offers a much larger market than any of the three countries could, and this larger market has contributed enormously to the emergence of manufacturing activities in East Africa. Lack of any form of economic cooperation between East Africa and the Neighbours helps to explain why exports to these countries have been so small. Had there been a customs union between East Africa and these countries, trade would doubtless have been substantially larger than it is now.

Another observation we can make from Table IV.3 is that it is only in intercountry exports that substantial shifts in the relative shares of particular SITC sections have taken place. In fact these shifts are even more marked if the commodity composition of these exports is traced from an earlier date. In 1950, for instance, 77 per cent of intercountry exports were in SITC sections 0 and 1; but in 1963 these two sections accounted for only 42.8 per cent.

Several explanations could be offered for the substantial shifts in the commodity composition of intercountry exports. These will be discussed more fully when analysing the commodity composition of each East African country's intercountry trade. Here we need only generalise that as development has proceeded so have these countries introduced new industries, especially in manufacturing, to serve the whole of East Africa. Unfortunately, the only East African country with anything like a meaningful industrial survey is Kenya, where industrial surveys for 1954, 1956, 1957, and 1961 have been undertaken, although not always on a comparable basis. Therefore it is difficult to trace these developments statistically.

In some SITC sections the actual volume of goods in intercountry exports has remained more or less constant, and therefore of declin-

ing relative importance. This is notably the case in SITC section 1 (Beverages and Tobacco). The reason for this phenomenon is largely that the domestic consumption in each country has risen to levels which can absorb most of the domestic supply of beer and cigarettes. Moreover, some goods formerly exported to other East African countries either as raw materials or processed raw materials have now almost vanished because the exporting countries have set up their own plants to produce the finished product. This is what has happened in the case of Tanganyika's intercountry exports of tobacco. In 1961 these exports were £434,000, but in the following year they fell to £65,000—not because of a decline in Tanganyika's output of tobacco (if anything there was an increase) but because a cigarette factory was established in that country.

Our discussion on the commodity composition of East African intercountry trade has so far been confined to exports. For East Africa as a whole the commodity composition of intercountry imports will, of course, be the same as for exports. Let us now compare East African intercountry imports with retained imports from foreign countries. This is useful because it indicates crudely where import substitution has been successful. Table IV.4 shows

TABLE IV.4.

Commodity Distribution of East African Retained Imports (*A*) and Intercountry Imports (*B*), 1959 and 1963

(£ *thousand*)

SITC	*1959*			*1963*		
	Retained Imports (*A*)	*Inter-country Imports* (*B*)	*B%A*	*Retained Imports* (*A*)	*Inter-country Imports* (*B*)	*B%A*
0. Food	8,346	6,188	74.6	7,877	8,889	112.8
1. Bev. & Tob.	1,281	4,724	368.8	1,072	4,521	421.7
2. Crude mater.	a	727	a	1,313	907	69.1
3. Fuels	9,780	279	2.9	9,416	435	4.6
4. Oils & Fats	671	1,604	239.0	1,253	1,393	111.2
5. Chemicals	8,216	1,145	13.9	10,699	2,728	25.5
6. Mfd. prod.	40,011	3,654	9.1	46,435	8,249	17.8
7. Machinery	30,472	103	0.3	36,487	205	0.6
8. Misc. Mfd.	9,232	1,603	17.4	12,149	4,020	33.1
9. Other	5,456	71	1.3	6,575	107	1.6
TOTAL	113,350	20,098	17.7	133,273	31,455	23.6

(*a*) Retained imports in this section were negative. Such negative items occur because goods may not be re-exported in the year of original importation. Consequently, re-exports in a given year might include goods imported in a previous year. Section 2 re-exports were £992,000 while net imports were £876,000 in 1959.

Source: *Annual Trade Reports.*

this comparison. If we crudely define import substitution as a rising share of domestically produced goods in any SITC section, it will be observed that East Africa has carried on a process of import substitution in practically all SITC sections in the five years covered. Adding all intercountry imports together, by 1963 they were 23.6 per cent, whereas in 1959 they were 17.7 per cent, of retained imports. In particular, we should observe that in the SITC sections which contain most consumer manufactured goods (i.e. SITC sections 5, 6 and 8) the ratio of intercountry imports has risen by more than this average rise. For chemicals the rise has been from 13.9 per cent to 25.5 per cent; for manufactured products from 9.1 per cent to 17.8 per cent; and for miscellaneous manufactured articles from 17.4 per cent to 33.1 per cent. These increases occurred even though in 1963 retained imports were a good deal higher in each of these sections than they were in 1959.

It should also be observed that while the value of retained imports of food has actually declined over the last five years, the value of intercountry food imports has increased, and is now £1 million greater than imports from abroad. We can expect this trend to continue—as it should—because import substitution in food is as important as elsewhere. An underdeveloped country should try hard to provide herself with food requirements so that foreign exchange earnings can be used primarily for importing capital goods. It is unfortunate that some underdeveloped countries are unable to do so—mainly as a result of the neglect of agriculture in their development expenditures.

Direction of Intercountry Trade

Before we embark on an examination of each country's pattern of intercountry trade, we must say something about its general direction. Briefly, the principal trading partner is Kenya. This is brought out in Table IV.5.

TABLE IV.5

The Direction of East African Intercountry Trade, *1959-63*
(*Percentage Shares of each country's exports*)

A. Kenya's Exports

	To Uganda	*To Tanganyika*
1959 ..	47.0	53.0
1960 ..	44.7	55.3
1961 ..	44.2	55.8
1962 ..	41.9	58.1
1963 ..	47.6	52.4

B. Tanganyika's Exports

	To Kenya	To Uganda
1959 ..	71.8	28.2
1960 ..	80.6	19.4
1961 ..	82.5	17.5
1962 ..	81.7	18.3
1963 ..	85.2	14.8

C. Uganda's Exports

	To Kenya	To Tanganyika
1959 ..	69.6	30.4
1960 ..	76.5	23.5
1961 ..	75.1	24.9
1962 ..	76.3	23.7
1963 ..	75.8	24.2

Source: *Annual Trade Reports.*

There is comparatively little trade between Uganda and Tanganyika, while Kenya trades extensively with both countries. In 1963 85.2 per cent of Tanganyika's total intercountry exports went to Kenya, and in the same year Kenya absorbed 75.8 per cent of Uganda's intercountry exports. On the other hand, Kenya's exports were distributed equally between Uganda and Tanganyika. Moreover, over the five year period covered in Table IV.5 there has been a distinct trend for Kenya to become more and more the market for the other two countries' intercountry exports. The increasing importance of Kenya as a market, of course, meant that trade between Uganda and Tanganyika was becoming relatively smaller. In fact, the two-way value of trade between Uganda and Tanganyika *fell* from £2.313 million in 1959 to £2.024 million in 1960, from where it sluggishly recovered and in 1963 was only £2.501 million. In other words, trade between these two countries has been stagnating.

There are two main reasons which can be offered to explain the present direction of intercountry trade. First, the small volume of trade between Uganda and Tanganyika can be attributed partly to lack of adequate means of transportation between the two countries. There is no rail link or all-weather road connecting Uganda and Tanganyika, whereas between Uganda and Kenya, and Tanganyika and Kenya there are both. Uganda and Tanganyika do, of course, share Lake Victoria; and this will perhaps be an important route in the years to come, although the loading and unloading charges, together with the small number of lake vessels which the East African Railways and Harbours Administration has,

will remain a major problem in the next few years. Moreover, the lake could only be an important route for goods produced or consumed in the areas around the lake, for the internal means of transport in Tanganyika are still very poor. As Tanganyika's recent development plan says, "a serious weakness in Tanganyika's economy lies in the relative underdevelopment of the distributive and transport sectors. There is an almost complete absence of inter-regional trade. This state of affairs stems not only from the one-sided development of the economy in the past, but is also due to the insularity of the regions . . . for this country is in fact made up of six or seven regions which are separated by vast semi-deserts and constitute independent economic entities with virtually no commercial ties between them".[5]

The second reason (and this is really the crucial one) why Kenya is the principle trading partner is that Kenya is a relatively more developed and industrialised country, with a number of industries designed to serve the whole of East Africa. Consequently, she has more and diversified products to offer to the other two countries, besides having an increasing demand for some products from the other two countries, either raw materials or other goods which she is not producing. An additional point is that in Kenya there are some marketing boards and an exports promotion council working hard to increase sales not only in East Africa but in foreign countries as well.

Country Shares in Intercountry Trade

The purpose of this section is to examine each country's share in intercountry trade. The importance of this exercise lies in the fact that the extent to which each country benefits from the operation of the East African common market is more or less directly linked to the quantity and nature of her intercountry exports and imports. In general, if a country joins a common market and does not increase her exports to the other partners, but only changes the source of her imports from third countries to the partners, she is not gaining anything; indeed, she will lose if the new sources of her imports are more expensive than the previous ones. Where there is not full integration, so that fiscal and other devices for redistributing incomes and economic activity cannot be used, a country joining

5. *Tanganyika Five-Year Plan, 1964-1969*, volume 1, page 11.

a common market has to increase her exports to the other participants in order to benefit. Moreover, for underdeveloped countries aspiring to industrialise, the commodity composition of intra-union exports is also relevant.

In Table IV.6 we have shown the value of each country's exports to and imports from the rest of East Africa for the period 1959 to 1963. In Table IV.7 we show each country's intercountry exports and imports as a proportion of the East African total.

TABLE IV.6

Intercountry Exports and Imports By Country, 1959 to 1963
(£ *thousand*)

	Kenya		*Uganda*		*Tanganyika*	
	Exports	*Imports*	*Exports*	*Imports*	*Exports*	*Imports*
1959 ..	12,297	5,488	5,228	6,510	3,574	8,100
1960 ..	13,773	6,995	6,694	6,613	2,324	9,182
1961 ..	15,948	6,995	6,856	7,437	2,234	10,605
1962 ..	17,320	7,339	7,055	7,740	2,391	11,685
1963 ..	19,790	9,163	8,242	9,933	3,423	12,358

Source: *Annual Trade Reports.*

TABLE IV.7

Country Percentage Shares in Intercountry Trade

A. Exports

	1959	*1960*	*1961*	*1962*	*1963*
Kenya	61.2	60.4	63.7	64.7	62.9
Uganda	26.0	29.4	27.4	26.4	26.2
Tanganyika ..	12.8	10.2	8.9	8.9	10.9

B. Imports

	1959	*1960*	*1961*	*1962*	*1963*
Kenya	27.3	30.7	27.9	27.4	29.1
Uganda	32.4	29.0	29.7	28.9	31.6
Tanganyika ..	40.3	40.3	42.4	43.7	39.3

Source: *Annual Trade Reports.*

Looking at exports first, we notice that the main supplier of goods has been Kenya, with her percentage share averaging 62.6 per cent in this period; Uganda comes next with an average share of 27.1 per cent; and Tanganyika comes last with an average share of 10.3 per cent. A more forceful way of indicating the position is to look

at the absolute figures: in 1963 Kenya's intercountry exports were almost *six* times those of Tanganyika and nearly *two-and-a-half* times those of Uganda. Moreover, over the last five years Kenya has tended to increase her percentage share, even though this trend was checked in 1963 when Tanganyika's exports increased by almost £1 million to an alltime record of £3.4 million But even at this record level, Tanganyika's proportion in intercountry exports was smaller than in 1959 by almost 2 per cent.

However, it would be wrong to think that the present pattern of country shares in intercountry exports has always been the same. In fact as recently as 1954 country shares in intercountry exports were 44 per cent, 46 per cent, and 10 per cent for Kenya, Uganda and Tanganyika, respectively (using the adjusted figures in footnote 2). These figures indicate that in this period Uganda's share was greater than that of Kenya, although Tanganyika's share was still the smallest. This situation was altered almost overnight when the East African Tobacco Company decided to move their cigarette factory from Uganda to Kenya. Uganda's exports of cigarettes to the rest of East Africa, which in 1955 were nearly £5.75 million (inclusive of excise taxes) fell by more than 50 per cent in 1956; in 1963 they were worth under £660,000 (exclusive of excise taxes). From being a net exporter Uganda became a net importer, not only in cigarettes but also in overall balance of trade with the rest of East Africa. It was the relocation of that single factory which initially increased Kenya's share in intercountry exports. Since then, however, new industries have increased her share further.

Tanganyika's share has been consistently smaller than either of the other two countries'. There are two related main explanations which we can offer. (i) The immigrant communities in that country (and we have to remember that it is the immigrants who have supplied entrepreneurial ability in East Africa) have concentrated on production of export commodities, notably sisal and coffee, while in the other two countries immigrants have attempted to exploit both the domestic and foreign market. (ii) Tanganyika does not have so far a single major industry which depends on the East African market as a whole. This is an important point, for if we look at Uganda we shall see that she has been able to maintain her share in total intercountry exports because of her sugar and textile industries alone. The tremendous importance of large

industries which depend on the East African market as a whole in determining each country's share in the benefits accruing from the common market will be taken up later.

Looking at the future development of intercountry trade, it is most unlikely that Tanganyika's share will remain so small. One thing seems eminently obvious: namely, that as intercountry trade grows it is unlikely that Kenya's share will remain as high as it is at present. It must fall in order to allow the shares of the other two countries, especially Tanganyika, to increase—as is politically necessary if the common market is to be maintained. In order that both Uganda and Tanganyika can increase their intercountry exports, it was agreed in April, 1964 by all three Governments to allocate certain industries to each country. Under this arrangement (the so-called Kampala Agreement) Tanganyika was given the exclusive right of assembly of trucks,[6] manufacture of motor vehicle tyres and tubes, and assembly and manufacture of radio sets; Uganda was given the right to manufacture nitrogenous fertilisers, and bicycles; and Kenya was allocated one industry—manufacture of light bulbs.[7] It will be noticed that the lion's share went to Tanganyika, and these new industries should, when set up, increase her share in intercountry exports substantially. The Kampala Agreement actually went furthei : it was also agreed that in the case of certain industries already found in each country (e.g. beer, cigarettes, shoes, cement), the companies concerned should be approached and persuaded that each country's consumption should be produced within its borders. Further, it was agreed that for industries which could operate efficiently and economically in one country, a country with large intercountry trade deficits intending to expand or start such industries could apply quotas against similar imports from the rest of East Africa. Tanganyika has already used this agreement to apply quota restrictions on intercountry imports of beer, wheat flour, paints, varnishes, shirts of textile fabric, writing books, and some other goods. Fuller evaluation and

6. Subsequently and at her request, Tanganyika was given the exclusive right of producing aluminium sheets, circles and foils instead of assembly of trucks.

7. It may be that some of the industries allocated to a country are already operating in another country on a small scale. Such industries will not be given up, but it is the agreed aim that future expansion in those industries will take place in the country allotted them.

discussion of the Kampala Agreement will be taken up in the final chapter of this study.

For the present we need only observe that the effect of this agreement will be to increase, in the near future, the shares of Uganda and Tanganyika in intercountry exports. However, for Uganda and Tanganyika to increase their shares in intercountry exports substantially they must also increase trade between themselves; for as long as they continue to trade primarily with Kenya (and hardly at all between themselves) Kenya's exports to them will continue to be very high.

Looking at country shares in intercountry imports the whole picture is reversed, although Uganda still retains her middle position. The largest importer has been Tanganyika, with an average percentage share of 41 per cent in the period 1959 to 1963; next has been Uganda with an average share of about 30 per cent; while Kenya's average share has been about 29 per cent. Between 1959 and 1962 Tanganyika's share increased from 40.3 per cent to 43.7 per cent, but then fell suddenly to 39.3 per cent in 1963. This percentage drop was not a fall in the actual value, and was due to two factors: (*a*) a dramatic increase in the exports of cotton fabric piece-goods from Uganda to Kenya; and (*b*) a marked increase in Tanganyika's intercountry exports, largely to Kenya. One tenuous suggestion is that the 1963 shares in intercountry imports may be expected to prevail for some time, although with time Kenya's share is likely to go up towards one-third.

Bringing intercountry exports and imports together, since Tanganyika's share in intercountry exports has been the smallest and has been falling, and since her share in intercountry imports has been the greatest and has tended to increase, it seems clear that she has gained the least from the operation of the common market. Indeed it is likely that she has actually lost. This last tentative conclusion is made stronger by examination of the commodity composition of each country's intercountry exports and imports, to which we now turn.

Commodity Composition of Each Country's Intercountry Exports

The commodity composition of each country's exports and imports, by SITC sections, is set out in Table IV.8 for 1959 and

TABLE IV.8

A. Commodity Composition of each Country's Intercountry Exports, per cent Distribution by SITC Sections: 1959 and 1963

	1959			1963		
	Kenya	*Uganda*	*Tanganyika*	*Kenya*	*Uganda*	*Tanganyika*
0	33.4	19.5	41.1	24.8	33.2	36.4
1	19.9	36.6	14.2	15.1	17.2	3.1
2	1.4	1.6	18.3	0.9	1.6	17.2
3	0.2	3.8	2.5	0.3	4.2	1.1
4	1.6	20.3	13.4	1.0	10.9	8.4
5	7.1	3.3	3.9	11.9	4.0	1.5
6	22.8	13.9	4.9	27.3	27.7	16.5
7	0.8	0.1	0.1	0.9	0.3	0.2
8	12.3	1.0	1.4	17.3	0.8	15.4
9	0.5	—	0.1	0.5	0.1	0.2
0–4	56.5	81.7	89.6	42.1	67.1	66.2
5–9	43.5	18.3	10.4	57.9	32.9	33.8

B. Commodity Composition of each Country's Intercountry Imports, per cent Distribution by SITC Sections: 1959 and 1963.

	1959			1963		
	Kenya	*Uganda*	*Tanganyika*	*Kenya*	*Uganda*	*Tanganyika*
0	25.1	37.7	29.1	38.2	24.0	24.3
1	25.9	19.2	25.4	11.7	13.1	17.4
2	9.3	1.9	1.1	7.3	1.3	0.9
3	4.7	0.2	—	4.2	0.2	0.2
4	19.9	3.1	3.8	10.4	1.9	2.0
5	2.9	7.1	6.5	2.8	12.9	9.6
6	11.0	20.0	21.6	19.2	29.9	28.5
7	0.1	0.7	0.7	0.2	1.0	0.8
8	1.1	9.9	11.1	5.9	15.5	15.7
9	0.1	0.2	0.6	0.1	0.3	0.5
0–4	84.8	62.1	59.5	71.8	40.4	44.9
5–9	15.2	37.9	40.5	28.2	59.6	55.1

Source: *Annual Trade Reports.*

1963. Three general points may be noted. (i) It is in Kenya's intercountry exports that manufactured products play the greatest part; in 1963 Kenya's exports in SITC sections 5-9 accounted for 57.9 per cent of her total intercountry exports, while in Uganda and Tanganyika these five sections contributed 32.8 per cent and 33.7 per cent respectively. In value terms Kenya's exports of manufactured goods were £11.5 million, compared with £2.7 million for Uganda, and £1.2 million for Tanganyika. If we add all intercountry exports in SITC sections 5-9, Kenya's percentage share in 1963 was 74.7 per cent compared with 17.7 per cent and 7.6 per cent for Uganda and Tanganyika respectively. (ii) The small share of manufactured goods in the exports of Uganda and Tanganyika means that agricultural products play a proportionately greater part, although in value terms Kenya's exports in SITC section 0-4 are much greater than either Uganda's or Tanganyika's. (iii) As regards intercountry imports, Tanganyika absorbs the largest share of manufactured goods, followed by Uganda and then Kenya. In 1963 Tanganyika's intercountry imports in SITC sections 5-9 were worth £6.8 million, compared with £5.9 million and £2.6 million for Uganda and Kenya respectively. Relatively, Tanganyika's share in these sections was 44 per cent in 1963, while Uganda's was 39 per cent, and Kenya's only 17 per cent.

These general observations pave the way for detailed discussion of each country's share in intercountry trade. In Table IV.9 we have shown the main commodities in Kenya's intercountry exports for the period 1959 through 1963; and in Tables IV.10 and IV.11 we have done the same for Uganda and Tanganyika respectively. In this analysis we shall make the simplifying assumption that SITC sections 0-4 represent agricultural products (the value of section 3, petroleum products, is very small); and SITC sections 5-9 represent manufactured products.

TABLE IV.9

Kenya Exports to Uganda and Tanganyika, 1959-63
(*£ thousand*)

COMMODITY	1959	1960	1961	1962	1963
0—*FOOD*					
Meat and Meat preparations	279	307	440	505	307
Milk and Cream—fresh	344	266	374	413	458
Butter and Ghee	415	476	439	462	517
Wheat, spelt and meslin, unmilled	577	858	869	540	547
Rice	—	66	238	232	188
Meal, wheat and spelt flour	851	779	725	733	569
Biscuits	110	135	156	166	177
Fruits and vegetables	248	281	356	432	531
Sugar, unrefined	87	88	123	84	110
Coffee—roasted and ground	100	114	158	168	141
Tea	567	444	562	611	400
Margarine and shortenings	82	104	158	206	178
Food, other	453	421	450	554	781
TOTAL	4,113	4,339	5,048	5,106	4,904
% of TOTAL EXPORTS	33.4	31.5	31.7	29.5	24.8
1—*BEVERAGES AND TOBACCO*					
Beer	471	592	698	655	681
Cigarettes	1,646	1,762	1,734	1,590	1,910
Tobacco, manufactured	205	188	192	185	227
Beverages and Tobacco, other	126	86	211	198	177
TOTAL	2,448	2,628	2,835	2,628	2,995
% of TOTAL EXPORTS	19.9	19.1	17.8	15.2	15.1
5—*CHEMICALS*					
Organic and Inorganic Chemicals	92	94	94	107	107
Paints, Varnishes, Pigments, etc.	67	95	231	251	266
Perfumery, Cosmetics, etc.	46	59	63	125	163
Insecticides, fungicides, disinfectants, etc.	94	118	180	439	492
Soaps	468	593	915	957	1,007
Chemicals, other	107	111	107	183	313
TOTAL	874	1,070	1,590	2,062	2,348
% of TOTAL EXPORTS	7.1	7.8	10.0	11.9	11.9

6—MANUFACTURED GOODS					
Bicycle tyres and tubes	100	143	193	221	326
Paper, paper board and manufactures	281	365	495	527	703
Sisal bags	281	397	299	292	344
Cement, building	777	800	739	664	687
Corrugated plates, sheets, etc.	—	—	114	594	1,112
Steel doors and windows	200	271	269	257	252
Household aluminium utensils	236	296	206	247	324
Metal Containers	232	243	197	227	163
Manufactured goods, other	692	847	1,255	1,274	1,493
TOTAL	2,799	3,362	3,767	4,303	5,404
% of TOTAL EXPORTS	22.8	24.4	23.6	24.9	27.3
8—MISCELLANEOUS MANUFACTURES					
Clothing	591	743	875	1,113	1,394
Footwear	579	638	713	860	1,200
Furniture and Fixtures and mattresses	160	158	194	231	346
Other	186	238	308	348	488
TOTAL	1,516	1,777	2,090	2,552	3,428
% of TOTAL EXPORTS	12.3	12.9	13.1	14.7	17.3
SITC Section 2	173	161	145	201	184
" " 3	19	16	28	45	49
" " 4	195	266	278	198	205
" " 7	95	89	92	124	179
" " 9	65	65	75	101	94
TOTAL 2, 3, 4, 7 & 9	547	597	618	669	711
% of TOTAL EXPORTS	4.4	4.3	3.9	3.9	3.6
GRAND TOTAL	12,297	13,773	15,948	17,320	19,790

Source: *Annual Trade Reports*

TABLE IV.10

Uganda Exports to Kenya and Tanganyika. 1959-63
(£ *thousand*)

COMMODITY	1959	1960	1961	1962	1963
0—FOOD					
Meat and meat preparations	—	67	194	182	75
Fish	—	35	52	59	53
Millet, unmilled	—	11	30	134	52
Biscuits	55	44	76	69	86
Beans, peas and pulses	—	34	58	72	27
Sugar—unrefined	616	1,455	1,582	1,627	1,836
Sugar, confectionery and preparations	84	89	79	58	65
Tea	81	91	137	92	67
Animal feeding stuffs	83	94	81	54	55
Food, other	—	90	273	128	422
TOTAL	1,017	2,010	2,562	2,475	2,738
% of TOTAL EXPORTS	19.5	30.0	37.4	35.1	33.2
1—BEVERAGES AND TOBACCO					
Beer	60	40	51	81	70
Tobacco—unmanufactured	809	725	196	363	449
Cigarettes	1,034	958	723	712	893
Beverage and tobacco, other	9	15	13	12	7
TOTAL	1,912	1,738	983	1,168	1,419
% of TOTAL EXPORTS	36.6	26.0	14.3	16.6	17.2
2—CRUDE MATERIALS					
Wood and timber	—	66	62	34	38
Crude materials, other	—	52	65	45	95
TOTAL	83	118	127	79	133
% of TOTAL EXPORTS	1.6	1.8	1.9	1.1	1.6

4—OILS AND FATS					
Cotton seed oil	835	985	938	612	753
Groundnut oil	—	8	22	54	14
Hydrogenated oils and fats	—	242	199	142	133
Oils and fats, other	—	5	8	37	1
TOTAL	1,063	1,240	1,167	845	901
% of TOTAL EXPORTS	20.3	18.5	17.0	12.0	10.9
6—MANUFACTURED GOODS					
Cotton fabrics (piece goods)	605	954	1,295	1,707	1,870
Enamel hollowware	—	21	60	68	106
Manufactured goods, other	—	133	155	169	304
TOTAL	728	1,108	1,510	1,944	2,280
% of TOTAL EXPORTS	13.9	16.6	22.0	27.6	27.7
SITC Section 3	196	218	290	318	349
" " 5	171	207	170	152	331
" " 7	6	6	9	24	20
" " 8	50	48	35	46	66
" " 9	3	3	3	5	6
TOTAL	426	482	507	545	772
% of TOTAL EXPORTS	8.1	7.2	7.4	7.7	9.4
GRAND TOTAL	5,228	6,694	6,856	7,055	8,243

Source: *Annual Trade Reports*

TABLE IV.11

Tanganyika Exports to Kenya and Uganda, 1959-63
(*£ thousand*)

COMMODITY	1959	1960	1961	1962	1963
0—FOOD					
Meat and meat preparations	70	53	51	83	80
Ghee excluding butter	109	110	98	84	86
Honey—natural	—	39	50	30	49
Wheat, spelt, and meslin unmilled	—	33	26	111	35
Rice	53	72	90	75	149
Meal and flour of wheat	—	2	8	40	35
Potatoes excluding sweet potatoes	—	11	14	68	11
Beans, peas and pulses	—	218	157	285	183
Onions	90	146	181	156	175
Sugar confectionery and preparations	—	1	6	25	42
Tea	—	48	64	19	27
Food, other	—	197	168	150	375
TOTAL	1,058	930	913	1,127	1,247
% of TOTAL EXPORTS	41.1	40.0	40.9	47.1	36.4
1—BEVERAGES AND TOBACCO					
Tobacco unmanufactured	349	371	434	65	96
Beverages and tobacco, other	16	15	11	13	11
TOTAL	365	386	445	78	107
% of TOTAL EXPORTS	14.2	16.6	20.0	3.3	3.1
2—CRUDE MATERIALS					
Oil seeds, nuts and kernels	199	155	135	136	217
Wood and timber	86	56	50	58	71
Cotton—raw	—	—	1	70	—
Pyrethrum flowers	99	86	95	34	2
Crude materials, other	—	57	65	70	300
TOTAL	472	354	347	368	590
% of TOTAL EXPORTS	18.3	15.2	15.5	15.4	17.2

4—*OILS AND FATS*					
Cottonseed oil	—	33	49	57	101
Coconut (copra) oil	296	224	147	149	135
Oils and fats, other	—	32	6	29	51
TOTAL	345	289	202	235	287
% of TOTAL EXPORTS	13.4	12.4	9.0	9.8	8.4
6—*MANUFACTURED GOODS*					
Cotton fabrics (piece goods)	—	21	32	79	154
Fabrics and synthetic fibres	—	17	34	61	84
Metal containers	89	65	13	16	30
Manufactured goods, other	—	50	67	75	298
TOTAL	127	153	146	231	566
% OF TOTAL EXPORTS	4.9	6.6	6.5	9.7	16.5
SITC Section 3	64	62	57	50	38
,, ,, 5	102	88	39	42	49
,, ,, 7	2	1	2	2	6
,, ,, 8	36	57	76	254	526
,, ,, 9	3	4	7	4	7
TOTAL	207	212	181	352	626
% of TOTAL EXPORTS	8.0	9.1	8.2	14.7	18.3
GRAND TOTAL	2,574	2,324	2,234	2,391	3,423

Source: *Annual Trade Reports*

KENYA

During the last five years the most conspicuous change in the commodity composition of Kenya's intercountry exports has been that food exports, although increasing in value, have been decreasing relatively in the total. The same thing has also happened to her exports of beverages and tobacco. These two sections contributed 53.3 per cent of Kenya's intercountry exports in 1959, but in 1963 they were only 39.9 per cent. The decrease in the relative share of these two sections has been due to above-average increases in the value of commodities in other SITC sections which Kenya sells to Uganda and Tanganyika. This is what one would expect for, as this country has developed, so has she turned her attention more and more towards production of more sophisticated goods. Consequently, her exports in SITC sections 5-9 have increased their relative share from 43.5 per cent to 57.9 per cent between 1959 and 1963. Their growth is summarised in Table IV.12.

TABLE IV.12

Kenya's Intercountry Exports of Manufactured Products, *1959* to *1963*

	Value (£ thousand)	*Percentage of Kenya's Intercountry Exports*
1959	5,349	43.5
1960	6,363	46.2
1961	7,614	47.7
1962	9,142	52.8
1963	11,453	57.9

Source: *Annual Trade Reports.*

The most important thing which emerges from these figures is that exports of manufactured goods have more than doubled in five years, and now constitute the bulk of Kenya's exports to Uganda and Tanganyika. This is a tremendous performance, and it means that Kenya has become the industrial partner in the East African common market. Moreover, the extent of industrialisation which has taken place in Kenya is understated in these figures, for they do not include the value of manufactured goods produced in Kenya for local consumption. This last point applies to all commodities; for example, in the meat industry in 1961, of all recorded meat and meat preparations prepared in Kenya, 14,607 tons were consumed locally while total exports (and a lot of these went to Britain) were 8,943 tons.

The extent of diversification which has taken place in that country is indicated roughly[8] in Table IV.9. Looking at the main SITC sections first, it will be noticed that the chemicals category has nearly trebled, that of manufactured products has doubled, and that of miscellaneous manufactures has increased two-and-a-quarter times. Looking at the individual commodities, new industries have emerged and assumed great importance. For instance, the exports of soap and soap preparations were only £468,000 in 1959, but in 1963 they had gone up to over £1 million. In the same period footwear exports have increased from £579,000 to £1,200,000; and clothing from £591,000 to £1,394,000. Other promising commodities are corrugated iron and aluminium sheets (none in 1959 but worth £1,112,000 in 1963); paper and paperboard manufactures (which have increased two-and-a-half times); and insecticides, disinfectants, etc. (which have increased *five* times). These increases in exports reflect the expansion of these industries. The Census of Manufacturing states that clothing, soap and footwear industries expanded by 75 per cent, 75 per cent and 62 per cent respectively between 1957 and 1961.[9]

This expansion has been the result of three factors: import substitution, the expansion of the home market, and export possibilities to the rest of East Africa. The extent of import substitution over a fairly wide range of products has been quite impressive. A rough way of assessing this is to look at the foreign import figures of various years, although since total consumption has increased, this underestimates the extent of manufacturing activity that has taken place in the country. Nevertheless Table IV.13 gives an indication for selected products.

TABLE IV.13

Kenya's Foreign Imports of Selected Manufactured Products, *1957* and *1961*

(*£ thousand*)

		1957	*1961*
(*a*)	Steel doors and windows and other iron structures	436	107
(*b*)	Ferrous and non-ferrous wire cables	232	72
(*c*)	Barbed wire and netting	239	157
(*d*)	Bicycle tyres and tubes	158	94
(*e*)	Household aluminium and iron utensils	220	117
(*f*)	Metal containers	424	216
(*g*)	Locks, bolts, and other fittings	339	256
(*h*)	Bricks, tiles, etc.	220	62

Source: *Census of Manufacturing*, *1961*.

8. An excellent examination of manufacturing activities in Kenya is given in Kenya Government, *Census of Manufacturing*, *1961*, 1963.

9. *op. cit.*, page 10.

Although import substitution within Kenya has been important, there is little doubt that the export possibilities to the rest of East Africa have been of crucial importance. Almost all exports of soap, footwear, clothing, food preparations (e.g. jellies) go to Uganda and Tanganyika. In examining this point the Raisman Commission came to the conclusion that Kenya's dependence on the common market is great and that "at a very rough estimate, something like a third of Kenya's recent growth may have depended upon increased sales, *or the prospect of increased sales*, to the other two territories,"[10] (my emphasis.) It should not be forgotten, however, that since something like half of the East African market is in Kenya, her domestic market remains of great importance.

All in all manufacturing activities now contribute about £25 million to Kenya's monetary gross domestic product, while in 1954 their contribution was only £14 million.[11] Even so, manufacturing activities constituted only 12.8 per cent of Kenya's monetary gross domestic product in 1962. Moreover, whereas it is true that some industries have been growing fast, the total manufacturing sector could have grown even faster but for the fall in the level of capital formation in the last few years. Whereas in 1956 capital formation reached the record level of £45.7 million, in 1963 it was only £29.0 million.

It will be noticed that almost all of Kenya's exports of manufactured goods to the rest of East Africa (and in fact to the rest of the world as well) are consumption goods. Indeed, machinery and transport equipment (SITC section 7) exports reached their peak in 1963 when they were worth £179,000 or 0.9 per cent of total intercountry exports. This phenomenon is due to the fact that import substitution is easiest in consumption goods—for the reasons given in Chapter 1. There is little doubt, however, that as manufacturing of consumption goods proceeds, so will there be a stimulus to produce investment goods. It is only after this stage has been reached that the industrialisation of a country becomes really well established. However, the production of investment goods requires skill, capital investment, and a wide and expanding market. This would indicate the importance of cooperation among developing countries.

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10. Raisman Commission Report, page 23.
11. Kenya Government, *The Growth of the Economy, 1954-62*, Economics and Statistics Division, December, 1963.

Certainly in the case of East Africa, there is no country which could alone offer a sufficiently wide market to support substantial development in investment goods industries.

Finally we need to point out that most of the industrial establishments in Kenya are still of small scale. The 1961 census of manufacturing mentions that establishments with 50 or more employees numbered only 174, or 22 per cent of all establishments examined. But these "large" establishments (industrial chemicals, cement, footwear, fruit and vegetable canneries, meat, dairy products, etc.) accounted for 78 per cent of industrial employment and 80 per cent of the value of production.

UGANDA

The main commodities in the exports of Uganda to the rest of East Africa are shown in Table IV.10. Several striking observations can be made. First, whereas in the case of Kenya food exports were found to have increased only modestly in the last five years, those of Uganda have more than doubled in value, from £1,017,000 in 1959 to £2,738,000 in 1963. These exports' relative share has also increased; it was 19.5 per cent in 1959, and 37.4 per cent in 1961, from where it declined to 33.2 per cent in 1963. This increase has been due, almost wholly, to sugar exports; they were worth £616,000 in 1959, but by 1963 they had trebled and were worth £1,836,000, and at this level were two-thirds of Uganda's intercountry exports of food. For the future, it is significant that Kenya, the main importer of sugar from Uganda, expects to be self-sufficient in sugar within a few years (although in 1964 she will import even more sugar from Uganda because of strikes in her plantations and factories). Should this happen we can expect a severe fall in Uganda's intercountry exports of sugar.

Second, beverages and tobacco, while still very important, have been falling down relatively and absolutely. Complete recovery of these exports could only come through the introduction of new goods: for instance if gin production could be stepped up.

Third, in Uganda unlike Kenya, exports of animal and vegetable oils and fats (SITC section 4) are of some importance, although also declining both in value and relatively. The main commodity exported is cottonseed oil, which in 1960 was valued at £985,000. The second important commodity in these exports is hydrogenated oils and fats.

Fourth, exports of manufactured goods classified chiefly by material (SITC section 6) have increased threefold in the last five years, from £728,000 in 1959 to £2,280,000 in 1963. Relatively they have increased from 13.9 per cent to 27.7 per cent. This is a tremendous achievement but it has been almost entirely due to one product—the emergence and growth of cotton fabric exports. In fact in 1963 exports of cotton fabrics were more than 80 per cent of Uganda's exports in this section. In future, however, other manufactured exports like iron and steel (when the new iron and steel plant established at Jinja expands) should make Uganda's exports of manufactured goods more diversified.

Two comments may be made about Uganda's exports in other SITC sections. (i) SITC section 3 exports, which incidentally have been increasing fairly steadily, are entirely electric energy which Kenya buys from Uganda. (ii) In future the most promising section is SITC section 8, small as it is at present. When industrialisation in Jinja is firmly established, it will be very well placed to supply miscellaneous manufactured goods such as clothing to western Kenya.

It is apparent that Uganda's manufacturing activity is not as diversified as that of Kenya. Uganda's intercountry exports are very concentrated in SITC sections 0 and 6, and these two sections are dominated by sugar and cotton fabrics. In fact, these two commodities contributed 45 per cent of the total value of Uganda's exports to East Africa in 1963.

TANGANYIKA

Detailed commodity composition of Tanganyika's exports to the rest of East Africa is shown in Table IV.11. Several things stand out. First, Tanganyika food exports form the highest percentage in total exports of the three countries, 41.1 per cent and 36.4 per cent in 1959 and 1963 respectively. Although there has been a relative decline in these exports, absolutely there has been an increase, from £1.0 million to £1.2 million. Unlike Kenya or Uganda there are few large food exports. In 1963 the big items were rice (£149,000), onions (£175,000), and beans and pulses (£183,000). Another thing to observe is that the Tanganyika exports in this section are not as processed as those of Kenya. A major problem which faces Tanganyika's food exports is that the other two countries produce most of

these products, and therefore their imports from Tanganyika depend on conditions affecting local supply, i.e. they are marginal imports. This is especially true in the case of Kenya's food imports from Tanganyika.

Second, between 1959 and 1963 exports in several SITC sections have declined both absolutely and relatively—for instance, SITC section 1 (beverages and tobacco) and SITC section 4 (animal and vegetable oils and fats). These are substantial falls, but it would be wrong to attribute the whole of this phenomenon to competition from Uganda and Kenya goods. It should be remembered that in Tanganyika means of transport have been exceedingly poor: as improvement in roads has taken place, local producers have been able to sell a greater part of their output in the home market. Moreover, as we have already seen, some of the goods formerly exported to the rest of East Africa are now being used locally, e.g. containers, raw tobacco, and pyrethrum. Tanganyika now has her own cigarette and pyrethrum extract factories.

Third, the poor performance of Tanganyika's exports would have been even worse but for the emergence of some new commodities for export to the rest of East Africa. For instance, there were no exports of cotton fabrics in 1959 but in 1963 these exports were valued at £154,000; similarly exports of blankets in 1962 were barely £14,000 but in 1963 they were £152,000. These two exports actually explain why SITC section 6 increased sharply in 1963. The emergence of new goods should make this section very important as time goes on—items such as plastics and domestic plastic ware, blankets, synthetic fibres, motor tyres and tubes,[12] razor blades, radios,[12] and trucks.[12]

Another very promising section is SITC section 8 (miscellaneous manufactured goods). This section has increased its percentage share in total exports from 1.4 per cent in 1959 to 15.4 per cent in 1963; in value terms the increase has been from £37,000 to £526,000. The reason for this increase has been largely exports of clothing and footwear. In 1962 footwear and clothing exports were £187,416 and £7,908 respectively; but in 1963 they were £361,749 and £86,164.

12. Tanganyika has included these industries, which were allocated to her in the Kampala Agreement, in her Five-year Plan. See *Tanganyika Five Year Plan, 1964-69*, page 59.

In total the picture is that Tanganyika has so far had little in the way of goods to sell to the rest of East Africa, and only in 1963 began to participate more actively.

Commodity Composition of Each Country's Intercountry Imports

What has been said about the commodity composition of each country's exports to the rest of East Africa is almost the exact opposite of the commodity composition of each country's imports from the rest of East Africa. This is made apparent in part B of Table IV.8.

Looking at intercountry *food* imports, we notice that in both 1959 and 1963 food imports were a quarter or more of each country's total imports from the rest of East Africa. In both Uganda and Tanganyika the percentage share of these imports has declined (in Uganda from 37.7 per cent to 24.0 per cent and in Tanganyika from 29.1 per cent to 24.3 per cent); whereas in the case of Kenya food imports have increased their percentage share—from 25.1 per cent in 1959 to 38.2 per cent in 1963. In absolute terms the value of these imports has increased in Kenya by more than £2 million, and she now has the largest value. This is in part to be explained by the huge growth in her sugar imports from the rest of East Africa.

The extent to which Kenya has industrialised relative to her partners in the common market is reflected in the comparatively small proportion of her imports in SITC sections 5-9, though these imports have been rising both absolutely and relatively.

Country Shares in Intercountry Trade in Manufactured Goods

It would be helpful to conclude our discussion so far by examining the changes in country shares in total East African trade in manufactured goods between 1959 and 1963. This is summarised in Table IV. 14.

TABLE IV.14

Country Shares in Intercountry Exports and Imports of Manufactured Goods, *1959* and *1963*

(*£ thousand and percentages*)

	1959			
	Exports		*Imports*	
	Value	%	*Value*	%
Kenya	5,349	81.3	829	12.7
Uganda	957	14.6	2,463	37.4
Tanganyika ..	271	4.1	3,281	49.9

	1963			
	Exports		*Imports*	
	Value	%	*Value*	%
Kenya	11,454	74.8	2,579	16.8
Uganda	2,702	17.6	5,906	38.6
Tanganyika ..	1,154	7.6	6,823	44.6

Source: *Annual Trade Reports.*

These figures reaffirm the point that Kenya is the principal industrial partner in the common market, and that Tanganyika is the main importer of manufactured goods. In 1963 Kenya's exports of manufactured goods were more than four times her imports; while in the case of Tanganyika imports were nearly six times exports; and in Uganda imports were over two times exports.

Kenya's share in intercountry exports of manufactured goods is greater than her share in total exports of all goods. However, as intercountry trade expands Kenya's share in exports of manufactured goods, as well as total exports, is likely to fall. Indeed this has already happened, even if only slightly, between 1959 and 1963. But in absolute terms Kenya's exports of manufactured goods will continue to be bigger than those of either partner for some time.

This detailed discussion on the commodity composition of each country's share in intercountry trade has been undertaken in order to help us assess the distribution and rough magnitudes of the benefits accruing from the common market. We cannot consider only the total volume of trade; what needs to be examined in great detail is the commodity composition of each country's exports and imports to and from the partners. This is particularly important for developing countries where each country wants to industrialise. With this as the yardstick, it will be obvious from the foregoing discussion that Kenya has gained substantially, that Uganda has certainly gained, and that Tanganyika has probably lost, although there are signs that she is beginning to gain. We shall, however, reserve further discussion on this point for Chapter VI.

CHAPTER V

COUNTRY BALANCE OF PAYMENTS ON THE CURRENT ACCOUNT

Perhaps the most serious gap in our knowledge of the economies of the three East African countries is the absence of officially published estimates of each country's balance of payments. This is especially serious now because each of the three countries has embarked on fairly ambitious programmes of rapid economic development. In this short chapter we aim to discuss each country's balance of payments on the *current account* only; this limitation arises from the fact that it is even more difficult to estimate the *capital account* —as we shall see presently. In this discussion we shall also offer, *for purposes of indicating orders of magnitude only*, rough estimates of the various large items in invisible trade of each country with other East African countries and the rest of the world.

Obviously, estimating each country's balance of payments is a task bigger than can be adequately accomplished by a private researcher with limited resources at his disposal. But our analysis of East African intercountry trade would leave a serious gap if it did not say something on invisible items in the balance of payments. Moreover, it is difficult to discuss the distribution of benefits accruing from the common market without such an analysis. There is evidence to show that the balance of payments of each country on current account is very different from what one would infer from the visible trade data provided in Table V.1. In this table it will be noticed that as far as external visible trade is concerned, both Uganda and Tanganyika have been having substantial *surpluses*, while Kenya has been having persistently large deficits. On the other hand, in intercountry visible trade, Kenya has been having substantial surpluses, while both Uganda and Tanganyika have been having deficits. Combining external trade and intercountry trade, the result is that Kenya's deficit is reduced, while Uganda's and Tanganyika's surpluses are accordingly reduced. In this chapter we shall also see that when invisible trade is included, Kenya's deficit is reduced further, while Uganda's and Tanganyika's surpluses are drastically reduced.

TABLE V.1

Balance of Visible Trade, by Country, 1959-63
(£ *thousand*)

	Domestic Exports	*Re-exports*	*Intercountry Exports*	*Total Exports*	*Net Imports*	*Intercountry Imports*	*Total Imports*	*Balance External Trade*	*Balance Intercountry Trade*	*Total Balance*
					KENYA					
1959 ..	33,306	5,079	12,297	50,682	61,508	5,488	66,996	−23,123	+ 6,809	−16,314
1960 ..	35,191	5,006	13,771	53,968	70,069	6,995	77,064	−29,872	+ 6,776	−23,096
1961 ..	35,326	6,418	15,948	57,692	68,937	6,995	75,932	−27,193	+ 8,953	−18,240
1962 ..	37,913	7,235	17,320	62,467	69,494	7,339	76,834	−24,347	+ 9,980	−14,366
1963 ..	43,832	7,147	19,791	70,769	73,688	9,163	82,852	−22,710	+10,627	−12,082
					UGANDA					
1959 ..	42,091	1,137	5,228	48,456	25,534	6,510	32,044	+17,694	− 1,282	+16,412
1960 ..	41,588	1,338	6,694	49,621	26,030	6,613	32,643	+16,897	+ 81	+16,978
1961 ..	39,195	2,062	6,855	48,112	26,546	7,437	33,983	+14,711	− 582	+14,129
1962 ..	37,635	3,317	7,054	48,005	26,206	7,740	33,946	+14,745	− 686	+14,059
1963 ..	51,475	3,023	8,241	62,739	30,922	9,933	40,855	+23,576	− 1,692	+21,884
					TANGANYIKA					
1959 ..	45,287	1,931	2,574	49,791	34,456	8,100	42,556	+12,762	− 5,526	+ 7,235
1960 ..	54,823	1,747	2,324	58,894	37,817	9,182	46,999	+18,752	− 6,858	+11,895
1961 ..	48,667	1,951	2,233	52,852	39,686	10,605	50,291	+10,932	− 8,371	+ 2,560
1962 ..	51,241	2,334	2,391	55,966	39,817	11,685	51,502	+13,758	− 9,295	+ 4,463
1963 ..	63,553	1,585	3,423	68,561	40,418	12,358	52,776	+24,721	− 8,935	+15,786

Source: *Economic and Statistical Reviews.*

N.B.: Separate figures may not add up to the total because of rounding.

Balance of Payments of East Africa as a Whole

The balance of payments of East Africa as a whole has been officially estimated since 1956 by the East African Statistical Department. The first estimate was made as a result of a World Bank request, as a condition for a $24 million loan to the East African Railways and Harbours Administration. The estimate for 1956 was published in 1958, and since then annual estimates have been made and published.[1] Estimates for 1959, 1960 and 1961 are shown in Table V.2. These estimates have been improved considerably with time, following the International Monetary Fund manual on balance of payments calculation.

Here we shall comment on the most difficult item to estimate, namely *private capital transactions.* The basic difficulty arises because in East Africa there is no exchange control with Sterling Area countries, while it is with these countries that East Africa has most of her transactions.[2] Moreover, exchange control with other monetary areas is not at all effective. Therefore, whereas many other underdeveloped countries depend on exchange control records for purposes of estimating their balance of payments, in East Africa this is not possible. The East African Statistical Department attempts to overcome this problem through questionnaires to each government, the East African Common Services Organisation departments, the Currency Board, the commercial banks, the East African Airways Corporation, the members of foreign missions, and large companies operating in East Africa. However, whereas reports from the governments, E.A.C.S.O. departments, and East African Airways could be relied on as accurate, reports by private companies, in so far as they respond to such questionnaires, cannot be relied on. Moreover, since *only corporate* bodies are covered by such questionnaires, there is little doubt that there must be a large degree of error in the reported totals. This largely explains the size of the Net Errors and Omissions item in Table V.2. It, therefore, seems that until some form of exchange control is introduced in East Africa,

1. See East African Statistical Department, *The Balance of Payments of East Africa*, March, 1960 and September, 1963. For a discussion on these estimates see A.G.T. Carter, "The Balance of Payments of East Africa", *East African Economics Review*, Volume 10 no. 2, December, 1963, pages 75-87. Estimates for more recent years are published in the *Economic and Statistical Review*.

2. With the announcement of the intention to introduce separate currencies, the three countries have now introduced exchange control regulations which cover the Sterling Area.

TABLE V.2

Balance of Payments of East Africa, 1959, 1960 and 1961*

(*£ thousand*)

CURRENT ACCOUNT	*CREDIT* 1959	1960	1961	*DEBIT* 1959	1960	1961	*NET DEBIT* 1959	1960	1961
1. Merchandise transactions	125,831	136,463	129,994	121,104	135,695	132,259	Cr. 4,727	Cr. 768	2,265
2. Non-monetary gold movement	1,185	1,348	1,397	7	9	7	Cr. 1,178	Cr. 1,339	Cr. 1,390
3. Foreign Travel	6,456	5,643	6,762	7,032	6,669	7,297	576	1,026	535
4. Transportation	5,548	6,516	7,720	6,459	6,878	7,733	911	362	13
5. Insurance	5,717	6,675	7,095	9,705	10,439	9,837	3,988	3,764	2,742
6. International investment income	6,260	6,403	7,112	16,969	18,703	16,247	10,709	12,300	9,135
7. Public transactions n.e.i.									
(*a*) H. M. Forces	4,397	9,234	10,904	1,158	174	155	Cr. 3,239	Cr. 9,060	Cr 10,749
(*b*) Other	909	1,886	1,732	2,975	3,003	4,102	2,066	1,117	2,370
8. Miscellaneous services	1,379	1,321	1,373	5,294	5,639	5,703	3,915	4,318	4,330
9. Donations, recurrent	3,193	3,258	3,311	2,233	2,097	2745	Cr. 960	Cr. 1,161	Cr. 566
TOTAL CURRENT TRANSACTIONS							12,061	10,559	8,685

CAPITAL ACCOUNT	*Liabilities (Net Increase)* 1959	1960	1961	*Assets (Net Increase)* 1959	1960	1961	*Net Credit* 1959	1960	1961
10. Donations, official grants	—	—	—	—	—	—	4,587	3,910	17,686
11. Private long term capital transactions	10,963	21,182	6,834	571	220	770	10,392	20,962	6,064
12. Private short term capital transactions	553	522	491	2,449	Cr. 384	Cr. 27	Dr.1,896	906	518
13. Public long term capital transactions	1,032	12,655	18,513	Cr. 1,812	Cr. 129	172	2,844	12,784	18,341
14. Public short term capital transactions	Dr. 1,859	1,075	Dr. 298	1,273	Cr. 2,907	5,796	Dr.3,132	3,982	Dr.6,094
15. Capital transactions of the Currency Board and commercial banks	—	—	—	Cr. 4,221	Cr. 15,909	6,361	4,221	15,909	Dr. 6,361
TOTAL CAPITAL TRANSACTIONS							17,016	58,453	30,154
Net Errors and Omissions							Dr. 4,955	Dr.47,894	Dr.21,469

* Provisional

Source: East African Statistical Department, *The Balance of Payments of East Africa* 1959, 1960 and 1961.

our knowledge of private capital movements will continue to be vague and unreliable. This is not to suggest, of course, that East Africa should introduce exchange control *so that* information on private capital movements may be made more reliable and complete. Rather exchange control might be needed in future so that outflows of funds from East Africa can be controlled and, hopefully, minimised. In particular the East African countries should ensure that *sudden* and enormous outflows of funds like the ones which have taken place in the last few years, especially 1960 and 1961, would not take place.[3]

The difficulty in estimating the private capital movements of East Africa as a whole is multiplied several times when trying to estimate the balance of payments of each East African country. This is the main reason why in our subsequent discussion only estimates of each country's balance of payments *on current account* are considered.

Each Country's Balance of Payments

There are still many difficulties, statistical and conceptual, in estimating each East African country's current account transactions. We shall mention the most important of these, and where appropriate indicate the solution used in arriving at our rough estimates in Table V.3. It will clarify our discussion to think of each country's current account as falling into two categories: (*a*) the *external account*—merchandise and invisible transactions with countries outside East Africa; and (*b*) *the intercountry account*—merchandise and invisible transactions with other East African countries.

One major problem in external visible transactions arises from the fact that whereas exports are valued f.o.b. port of departure from East Africa, imports are valued c.i.f. port of entry into East Africa. One of the most important effects of this system is that Uganda's exports and imports are *overvalued* and *undervalued*, respectively, to the extent of transportation costs between this country's border and Mombasa—a distance of about 600 miles. The same is also true of Tanganyika's exports and imports which go and come through Mombasa. For Uganda alone it has been

3. Due to political uncertainty, overseas investment in East Africa fell from £21 million in 1960 to less than £7 million in 1961. See A.G.T. Carter, *op. cit.*, page 81.

TABLE V.3

Country Balance of Payments on the Current Account, 1961

(*£ thousand*)

	KENYA Credit	*KENYA* Debit	*UGANDA* Credit	*UGANDA* Debit	*TANGANYIKA* Credit	*TANGANYIKA* Debit
1. Domestic exports & net imports	35,326	68,937	39,195	26,546	48,667	39,686
2. Re-exports	6,418		2,062		1,951	
3. Balance on external trade	−27,193		+14,711		+10,932	
4. Intercountry exports & imports	15,948	6,995	6,855	7,437	2,233	10,605
5. Balance on intercountry trade	+8,953		−582		−8,371	
6. Balance on trade with world	−18,240		+14,129		+2,561	
7. **Invisible Transactions, External:**						
(*a*) Foreign travel	4,824	3,869	1,069	1,780	869	1,648
(*b*) Insurance	4,045	5,410	1,717	2,558	1,333	1,869
(*c*) Transportation	4,979	3,982	1,123	1,927	1,618	1,824
(*d*) Investment income	2,547	10,000	2,885	2,981	1,680	3,266
of which E.A.R. & H.	225	706	225	706	225	706
E.A.P. & T.	64	133	63	133	63	133
P.O.S.B.	168	—	37	—	47	—
Other E.A.C.S.O.	16	2	16	1	16	2
(*e*) Public transactions	10,052	1,455	959	1,300	1,625	1,502
(*f*) Private donations	931	1,105	495	716	1,885	924
(*g*) Miscellaneous	745	2,109	278	1,369	350	2,225
8. Balance on external invisibles	+193		−4,105		−3,898	
9. Balance on current external	−27,000		+10,606		+7,034	
10. **Invisible Transactions, East Africa:**						
(*a*) Mark-ups on transfers	3,947	—	—	2,369	—	1,578
(*b*) E.A.R. & H. expenditure & revenue	10,954	11,653	2,738	7,438	4,564	5,703
(*c*) E.A.P. & T., expenditure & revenue	3,779	4,144	886	1,381	1,240	1,382
(*d*) E.A.R. & H. and E.A.P. & T, surplus	2,514	—	2,513	—	2,513	—
(*e*) Other E.A.C.S.O., expenditure & revenue	4,081	1,111	720	398	1,200	635
(*f*) Education		200	400			200
(*g*) Transportation, travel						
(*h*) Labour incomes						
(*i*) Head offices	500			200		300
(*j*) Other						
11. Balance on invisibles with East Africa	+8,667		−4,529		−281	
12. Balance on invisibles with world	+8,860		−8,634		−4,179	
13. Balance on current with East Africa	+17,620		−5,111		−8,652	
14. Total balance on current account:	−9,380		+5,495		−1,618	
15. Newman estimates	−£8.0 million		+£2.0 million.		−£5.4 million.	

Source: *See text.*

estimated that these costs must be at least £7 million a year.[4] The solution adopted for our rough estimates was to treat E.A.C.S.O. as a "fourth state" in East Africa, and then estimate its earnings and expenditures (these constituting each country's payments to and receipts from E.A.C.S.O.) in each of the three countries. This is further discussed below.

One further effect of valuing exports f.o.b. and imports c.i.f. is that trade deficits are increased, while Insurance and Transportation items are reduced accordingly. For other invisible items, our estimates were taken from unpublished information by E.A.C.S.O. departments and is shown separately.

Another problem arises from the fact that since Kenya houses most of the headquarters of the departments of E.A.C.S.O., imports by these bodies are credited to Kenya. Kenya's total foreign imports are consequently inflated in relation to those of Uganda and Tanganyika. Unfortunately this is a problem impossible to solve because in the Annual Trade Reports imports by E.A.C.S.O. departments are lumped together with government imports.

On the intercountry account there are also major problems. First, the fact that the three countries have common boundaries means that not all visible intercountry transactions are recorded. For this item we assume that unrecorded visible trade is self-cancelling for each country; this assumption is sensible in the case of intercountry trade conducted in barter terms, but Kenya doubtless has an unrecorded net credit overall. The same assumption was also made for unrecorded trade with the Neighbours. Here, however, it would appear that both Uganda and Tanganyika, especially the former, have net credits in such trade.

Second, the existence of a common currency in the whole of East Africa means that each country's balance of payments cannot be estimated through currency exchanges. Moreover, since the same commercial banks operate in all three countries, the claims of one country against another may be settled in the same country without any flow of funds taking place. This problem could only be solved by institution of exchange control among the three countries; and this would be neither possible nor desirable.

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4. Peter Newman, "Trends in the Economy of East Africa", *Problems of Economic Development in East Africa*, East African Publishing House, 1965.

Third, the fact that both Uganda and Tanganyika get large proportions of their imports from outside East Africa as transfers from Kenya means that the mark-ups charged by Kenya importers constitute an income to Kenya and payments by both Uganda and Tanganyika. In our estimates we assumed that the size of this mark-up is 15 per cent for all recorded net transfers.[5] To this mark-up we have added another 5 per cent in order to cover the unrecorded transfers. Payment made by each of these two countries to Kenya on this item was calculated by taking each country's percentage share in total net transfers. Since Uganda's net transfers are greater than Tanganyika's, the latter country pays a proportionately smaller amount. However, strictly speaking the amount of mark-up charged each of these countries by Kenya importers will also depend on the degree of bulk-breaking, costs of holding stocks, and risk undertaken.

Fourth, the most important and difficult problem arises from the existence of large transactions by the departments of E.A.C.S.O., especially the Railways and Harbours and Posts and Telecommunications Administrations. Conceptually, this is also a major problem. In the national income publications of all three countries the activities of E.A.C.S.O. are divided into three equal parts, each country being credited with one share. This is, however, an unsatisfactory method, for the activities of these departments are not equally distributed among the three countries. On the other hand, it does not seem right to credit each country with *all* the activities of the E.A.C.S.O. departments within her borders—for E.A.C.S.O. is owned and operated jointly by the three countries. This is especially so where the E.A.C.S.O. departments make profits in their operations. Conceptually, the method followed in our rough estimates was to treat E.A.C.S.O. as a "fourth state". Consequently, the *working expenditure* of these departments in each country was credited as a receipt to that country, while revenues of these departments were treated as payments by each country.

5. The census of distribution for 1960 which was conducted by the Kenya Statistics Department found that wholesalers in Nairobi had a mark-up of 15 per cent on average. See *Survey of Distribution, 1960,* Economics and Statistics Division, Ministry of Finance and Economic Planning, 1963, page 31. The size of this mark-up, however, might be smaller than on transfers of imported goods from Kenya to Uganda and Tanganyika.

Unfortunately, the expenditures and revenues of E.A.C.S.O. departments are not reported by country, and statistically we had, therefore, to follow the method and allocations of Mr. Ord.[6] In this article Ord is not primarily concerned with country balance of payments but with more meaningful gross domestic product aggregates. Ord estimates operating surpluses and employment income (including passages and pensions) generated by the East African Railways and Harbours Administration, the East African Posts and Telecommunications Administration, and the non-self-contained services of E.A.C.S.O. Each country is then credited with the income generated within her borders. The results are indicated in Table V.4.

TABLE V.4

Contribution of East African Common Services to GDP, by Country, ***1957***
(*£ million*)

	Kenya		*Uganda*		*Tanganyika*	
	a	*b*	*a*	*b*	*a*	*b*
Non-selfcontained Services	1.6	1.7	0.2	0.2	0.4	0.4
Posts and Telecommunications ..	1.8	2.3	0.4	0.6	0.6	0.8
Railways and Harbours	6.5	10.9	1.0	1.2	2.9	3.4
Total	9.9	14.9	1.6	2.0	3.9	4.6
Percent	64	69	10	9	25	21

Kenya: *a*=employment income, including pensions and passages.
b—total, including gross operating surplus.

Source: H. W. Ord, *op. cit.*

In our rough estimates of the balance of payments, it was assumed that each country's receipts from E.A.C.S.O. were proportional to *employment income* generated in that country. However, Ord's proportions were modified slightly, because since 1957 E.A.C.S.O. has extended its activities in both Uganda and Tanganyika. (For instance, the extensions of the railway to northern Uganda and from Kampala to Kasese must make Uganda's share in the total expenditure of the Railways greater than in the past.) In the allocation of the working expenditure of the Railways and Harbours, it was assumed that 60 per cent takes place in Kenya, 25 per cent

6. See H. W. Ord, "Social Accounting and Inter-territorial Transactions in East Africa", *East African Economic Review*, Volume 9 No. 2, December, 1962, pages 138-148.

in Tanganyika, and 15 per cent in Uganda. For the Posts and Telecommunications Administration, the shares of Kenya, Tanganyika and Uganda were taken to be 64 per cent, 21 per cent, and 15 per cent respectively; and for Non-self-contained Services the shares used were Kenya 68 per cent, Tanganyika 20 per cent, and Uganda 12 per cent.

The next stage was to estimate country shares in the revenues of these services. For the Railways and Harbours we used gross tonnage—locomotives plus trailing loads—handled in each country. However, the gross tonnages of Uganda and Tanganyika were weighted—the former by 100 per cent and the latter by 25 per cent —in order to take account of their longer distances to the coast. In the end we assumed that the Railways and Harbours earn 47 per cent of their total revenues from Kenya, 30 per cent from Uganda, and 23 per cent from Tanganyika. In the case of the Posts and Telecommunications, examination of the published accounts suggested that perhaps 60 per cent of total revenue was made in Kenya, and the rest was arbitrarily divided equally between Uganda and Tanganyika. For the Non-self-contained Services, each country's contribution to their revenue is regularly published, although unfortunately not by calendar years. Revenue from the Distributable Pool is more difficult to estimate, but it would appear that Kenya's share is about 50 per cent, Uganda's 20 per cent, and Tanganyika's 30 per cent. Incidentally, it should be noticed that the working expenditures of the Non-self-contained Services are much larger than the revenue they get from the three countries, because they receive substantial grants from foreign countries.

The rough and ready methods used in our calculations indicate the extremely tentative nature of the estimates provided in Table V.3. However, as orders of magnitude they provide an insight into the invisible flows arising from the activities of the East African Common Services. *Only the working expenditures* of these Services were allocated according to this method. The capital expenditures of the Common Services are not included in Table V.3—for since we have regarded the E.A.C.S.O. as a "fourth state" such items properly belong to the capital account. We have included the operating surpluses of the Railways and Harbours and the Posts and Telecommunications in our estimates, using the "one-third rule", but have not allocated the grant-supported deficit of the other

E.A.C.S.O. services. It will also be observed that we have distributed the transactions of the Common Services in the investment income item in the external account by the one-third rule, on the ground that the loans raised by these Services in foreign countries are guaranteed jointly by the three governments.

In Table V.3 there are numerous empty boxes in item 10. Filling in these gaps would require a large and well-organised survey to determine the size of the flows. As far as the direction is concerned, however, there is little doubt that Kenya has a net credit in most of them—certainly in transportation, insurance, and travel.

Interpretation of Findings

The main purpose of our exercise has not been to give *accurate* estimates on the balance of payments for each country, but rather to indicate the orders of magnitude and direction of the main transactions. For this purpose our rough estimates are suggestive enough, and the fact that they do indicate the orders of magnitude and direction is suggested by the estimates in Table V.3 calculated by Peter Newman.[8]

From our calculations it will be observed that, whereas Kenya had a small surplus in invisible transactions with countries outside East Africa in 1961, both Uganda and Tanganyika had substantial deficits. The explanation for Kenya's surplus in this item was the large expenditure by British Forces based in Kenya; in 1961 this expenditure was about £9.5 million. There is little doubt that the recent removal of British Forces from Kenya will have a direct and serious repercussion in the balance of payments of that country.

But perhaps a more important observation is that, in the invisible transactions within East Africa, Kenya had a large surplus, while Uganda had a large deficit, and Tanganyika's payments and receipts about cancelled each other. The effect of this was to reduce Kenya's large deficit in external merchandise transactions, while Uganda's large surplus on external merchandise transactions was reduced. Moreover, if we combine each country's visible and invisible transactions within East Africa, we notice that while in Kenya

8. See Peter Newman, "Foreign Investment and Economic Growth: The Case of East Africa 1963-1970", a paper prepared for the Third Conference on Public Policy, University of East Africa, Dar es Salaam, September, 1964, proceedings forthcoming.

both visible and invisible intercountry transactions markedly improve her overall balance on the current account, in Uganda, largely because of invisibles and in Tanganyika largely because of visibles, intercountry transactions make their overall balances on the current account less favourable. This picture would be even clearer if intercountry transactions in transportation, travel, and insurance were included in our calculations—for, as we have already mentioned, Kenya has an unrecorded surplus in these transactions.

The large surplus of Kenya in both invisible and merchandise transactions with the rest of East Africa helps to explain how this country has been able to run persistently large deficits in her merchandise transactions with countries outside East Africa. In other words both Uganda and Tanganyika have been indirectly earning foreign exchange for Kenya. Incidentally, we should notice that Tanganyika's overall deficit on the current account in 1961 was exceptional, due to a sudden fall of £6 million in the value of her domestic exports in that year.

Looking at the future, it seems likely that both Uganda and Tanganyika will continue to have surpluses in external trade for some years. On the other hand Kenya is likely to continue having deficits in external trade but surpluses in trade with the rest of East Africa. In other words past patterns are likely to be maintained for some time in the future, even though the sizes of country trade balances change. Past deficits in external invisible transactions are also likely to continue for Uganda and Tanganyika; in fact these deficits can be expected to increase with time, because of increased borrowing to finance development projects. As far as Kenya is concerned, however, the small surplus in the external invisible transactions realized in 1961 is most certainly going to be replaced by large deficits in the future, both because of the withdrawal of British Forces and greater borrowing for development purposes. Kenya, however, will continue to have surpluses in her invisible transactions with the rest of East Africa—as a result of her geographical position, the fact that she houses most of the E.A.C.S.O. departments, and the fact that she is generally more developed than the other two countries.

CHAPTER VI

NATURE AND DISTRIBUTION OF BENEFITS OF THE COMMON MARKET

The customs union among Uganda, Kenya and Tanganyika, which has developed into a *de facto* common market, has been achieved through a number of stages. Kenya and Uganda agreed on the free transfer of domestically produced goods and amalgamation of their customs authorities in 1917; in 1923 Tanganyika, although still retaining a separate customs department, was brought into the arrangement; in 1927 free movement of foreign imported goods was accepted by the three countries; and in 1949 Tanganyika's customs department was amalgamated with that of Kenya and Uganda.[1] In this chapter we shall first say something about the theory of customs unions in general and then examine the operation of the East African common market.

Theory of Customs Unions

This has now become an important field of theoretical and empirical investigation.[2] As so often happens in economics, discussion among economists at any one period centres on a major contemporary phenomenon. The current interest in the theory of customs union has now reached a high level of refinement and volume in theoretical model-building and empirical testing. This is a reflection of the widespread emergence of customs unions in various parts of the world: the European Economic Community; the Montevideo Treaty Free Trade Area (of which members are Peru, Chile, Argentina, Brazil, Paraguay, Uraguay and Mexico); the Central American Common Market (of which members are El Salvador, Guatemala, Honduras and Nicaragua); the East African

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1. For an excellent account of the historical development of this customs union see T.A. Kennedy, "The East African Customs Union: Some features of its History and Operation," *Makerere Journal*, No. 3, 1959.

2. Two major works on this subject have recently appeared:
(*a*) Bela Balassa, *The Theory of Economic Integration*, George Allen and Unwin, 1962.
(*b*) S. Dell, *Trade Blocs and Common Markets*, Constable, 1963.
Besides these two recent works there are many articles on this subject (for a fairly complete bibliography see Balassa, *op. cit.*, pp.274-289), and, of course ,the well-known works of Viner and Meade:
J. Viner, *The Customs Union Issue*, New York, 1950.
J. E. Meade, *The Theory of Customs Union*, Allen and Unwin, 1955.
Also see T. Scitovsky, *Economic Theory and Western European Integration*, Stanford University Press, 1958.

Customs Union; customs unions in former French colonies in Africa; etc. Besides these trading blocs there are those in the Soviet orbit.

There are several forms of economic integration and co-operation, and we can distinguish at least five main types[3]: a free trade area, a customs union, a common market, an economic union, and economic integration. In a free trade area there is free trade for *locally produced goods* but there is no common tariff wall with third countries; in a customs union there is a *common tariff* wall besides, of course, having free trade in local goods; a common market goes further than this and allows free movement, not only of goods, but also of factors of production; an economic union is a common market with some degree of *coordination* of national economic policies; and with economic integration a *single economy* is created with unified fiscal policies, social policies, foreign trade, etc. In economic integration there is need for a supra-national government to formulate and administer unified economic policies.

The purpose of this section is to show that the established theory of customs union cannot be applied blindly in underdeveloped countries. The established theory of customs unions concerned itself with welfare effects and was based on the economic gains to be derived from free trade. At first it had been thought that since free trade maximised world welfare, a customs union was to be welcomed because it was a movement towards free trade and thus led to greater, even if not maximum, world welfare. Later, Jacob Viner[4] demonstrated that this was not necessarily so; he introduced *trade creation* and *trade diversion* as analytical tools to prove his case. In trade creation a good which was formerly produced at high cost under protection in country A is now produced at lower cost in country B after A and B form a customs union. As far as resource allocation is concerned, this is unanimously declared to be a good thing because it leads to a more efficient employment of resources in the union. In trade diversion, a good which was formerly imported from a third country is now produced under protection, and therefore at higher cost than in the case of former imports, in, say, country A. Again looking at resource allocation alone, this is declared to be an undesirable

3. See Balassa, *op. cit.*, page 2.
4. J. Viner, *op. cit.*, Chapter IV.

effect—for it leads to inefficient use of resources. The intensity of these two effects will depend on the nature of the economies forming the customs union. It can be expected that where economies are competitive, trade creation will predominate; while where economies are complementary trade diversion will tend to outweigh tne other effect. On this analysis the desirability of the customs union will depend on the degree to which trade creation can be expected to outweigh trade diversion.

This analysis, although theoretically very neat, is essentially static, depends on a number of doubtful assumptions, and can hardly be applied blindly to customs unions among underdeveloped countries. For instance in discussing trade creation, we assume that both A and B have been producing the goods in question at different costs. This might not be the case. In fact there are several possible situations we can distinguish: (*a*) before forming a customs union both A and B had not been producing the goods at all; (*b*) both A and B were producing the goods before the union, either protected or unprotected; and (*c*) either A or B was producing the goods before the union, with protection or without. In the established theory case (*a*) was not discussed. This is a serious omission in view of the common phenomenon of idle resources (especially labour) in underdeveloped countries—resources which could be employed if infant industries were established after the formation of customs unions. As for cases (*b*) and (*c*), the likely analytical results will depend, in the established theory, on the difference in costs of production. For instance if country A was the cheapest producer of the goods in the world before the union, there would be no trade creation unless country B had been producing the goods under protection and therefore at higher cost than A. However, costs of production are not constant, and any analysis which is founded on their differences at any one point of time is likely to be misleading, and certainly should not be used for giving very long-term prescriptions. In any case in underdeveloped countries there is, more often than not, extensive unemployment, which makes market costs misleading. Moreover, most underdeveloped countries depend on a few primary commodities for their foreign exchange and monetary gross domestic product and are therefore in a vulnerable situation, as argued in Chapter I. Therefore one of the reasons why underdeveloped countries should

form customs unions and common markets is, indeed, deliberately to increase trade among themselves. Sponsored industrialisation means an attempt by underdeveloped countries to change their comparative advantage position vis-à-vis the developed countries.[5]

For underdeveloped countries which do not trade much among themselves, the formation of a customs union must inevitably lead to some trade diversion. But this trade diversion is not to be condemned,[6] for a customs union will facilitate large-scale operation and therefore economies of scale, development of skills, and rising employment for people who were previously unemployed or producing little on the land.

Instead of dwelling on trade creation and trade diversion, analysis of customs unions in underdeveloped countries should rather concentrate on the following: (i) the effect of the larger market on the growth of combined output (ii) the possible economies of scale and consequent reductions in the costs of production; (iii) the possible emergence of new industries which would reduce dependence on a few exports of primary commodities; (iv) the effect on employment; (v) the effect on productivity through competition in the area; and (vi) the effect of all these on inflow of foreign capital and on local and foreign entrepreneurial decisions. Above all, attention must be paid to long-run expected changes in the patterns and methods of production.

Some new ideas in the theory of customs unions are, however, very important; they owe their emergence to the study of customs unions in areas where the participants are at different stages of growth. I am thinking in particular of two concepts: *polarisation effects* and *spread effects*.[7] The importance of these ideas lies in the

5. Here one must warn, however, that although the doctrine of comparative advantage is not one to be adhered to blindly, it remains significant because after satisfying the demand within the union, any extra output has to be sold to the rest of the world, where competitiveness is vital.

6. Actually even in developed countries trade diversion could in some cases be beneficial. For a good discussion on this point see R. Triffin, "The Size of the Nation and its Vulnerability to Economic Nationalism", in E.A.G. Robinson (editor), *Economic Consequences of the Size of Nations*, New York, St. Martins Press Inc., 1960, pages 247-264.

7. We owe these two concepts to Hirschman and Myrdal. Hirschman uses 'polarisation' and 'trickling down' effects, while Myrdal uses 'backwash' and 'spread' effects to explain the same processes. I prefer the terms 'polarisation' and 'spread' effects—for they seem more descriptive. See A. O. Hirschman, *The Strategy of Economic Development*, Yale University Press, 1958, pp 187-201; and Gunnar Myrdal, *Economic Theory and Underdeveloped Regions*, Duckworth, 1957, Chapters 3-5.

fact that they focus on the effects of forming a customs union *on each participant*. Briefly, the polarisation effect is the process by which, after formation of the customs union, economic activity (industrialisation, rise in incomes, and growth of employment) concentrates in one country or region. The spread effect is the opposing process, by which economic activity spreads from the relatively advanced areas to the relatively poorer areas. This analysis is important because what is true for the whole union might not be true for each individual country. The formation of a common market might lead to industrialisation and rises in national income and employment for the common market as a whole; but if one participant does not increase her exports to the others but simply shifts her imports from cheaper third countries to more costly (at any rate initially) partner-countries, the deterioration in her terms of trade could mean real hardship. In fact even at this early stage of our analysis we can say that unless there are deliberate forms of intervention, the former disparities in growth rate and income levels in member countries are likely to be intensified by the formation of a common market. In other words for underdeveloped countries spread effects[8] are, initially at least, either slow or ineffective, and intervention is necessary to reduce any harmful effects of the more powerful polarisation forces.

The usefulness of a customs union in underdeveloped countries has at times been belittled by economists who concentrate their analysis on trade creation and trade diversion effects. It is said, for instance, that countries which would benefit from a customs union are those whose economies are competitive but potentially very complementary, and in which there are high pre-union tariff rates against each other, a high proportion of trade among the partners relative to their total world trade,[9] and a low proportion of foreign

8. The poorer members of the common market are supposed to benefit through increased demand for their products; relocation of industries (or attractiveness in industrial expansion) in poorer countries because of wage differentials and lower rents and transmission of technical knowledge and skills. But polarisation effects tend to make the growing areas, at any rate in the early stages of development, even more attractive to additional industries. For a good discussion on these and other points see Hirschman, *op. cit.*, Chapter 10.

9. This would suggest that a developing country could gain more if she formed a common market with a developed country with which she has substantial trade. But this could only be so if deliberate actions to move industries to the poor country are taken, in order to ensure that the latter moves out of a position of economic inferiority and backwardness. In practice there are great dangers for the poor country in such an arrangement.

trade in each member's domestic purchases. Looking at underdeveloped countries, it is concluded that since they do not fulfil these conditions they cannot gain much from economic integration. Statically these traditional arguments are correct. But in analysing the effects of customs unions in developing countries the emphasis should be laid on the future; and such economic arrangements are of particular advantage because they increase the scope and feasibility of future import substitution. Moreover, if a customs union could be accompanied by economic coordination and cooperation, as in an economic union, there would be the additional advantage of economising on capital through avoiding duplication of big industries. But the potential benefits of a customs union among developing countries would be seriously reduced if the principle that tariff rates should not be raised above the formerly existing ones were internationally enforced. Since there is at present little trade among underdeveloped countries, and since most of them have very little in the way of manufacturing activities, these countries are not likely to have high enough tariff rates against other countries to make it possible to embark on a wide programme of industrialisation without additional protection. Restricting the degree to which developing countries could offer protection to their industries would remove the strongest weapon these countries have for fostering industrialisation.

It has been suggested at times that the best way towards economic integration is to proceed on a *sectoral basis;*[10] i.e., countries intending to form a common market should start by having a common market in one industry, and so on until a full common market is formed. This approach is advocated on the grounds that the system is flexible and that it is easier to reach agreement in negotiations. This approach has much to support it where there are large national differences and where the countries have a wide range of industries which could benefit from the abolition of tariffs. But in the case of underdeveloped countries where there are few established industries integration on an industry by industry basis is almost impracticable. Even in developed countries this approach could make the necessary readjustment in member countries unnecessarily lengthy and

10. The European Steel and Coal Community is a good illustration of this. For detailed treatment of this suggestion see D. U. Stikker, "The Functional Approach to European Integration", *Foreign Affairs*, April, 1951.

painful. As Balassa points out, "simultaneous integration in one sector will lead to readjustment in this sector alone, the reallocation of resources in other sectors being impeded by the continued existence of tariffs and other trade barriers—hence the losses suffered by countries whose productive activity in the newly integrated sector contracts will not be compensated for until the next phase. [Moreover] under the sectoral approach every step in integration results in a new and temporary equilibrium of prices, costs, and resource allocation, and this 'equilibrium' is disturbed at every further step. Production decisions will then be made on the basis of prices that are relevant only in certain phases of integration, and shifts in resource allocation will take place which may later prove to be inappropriate".[11] Against this we have to set the advantage of a once-for-all disturbance, after which readjustment can proceed on the whole front with some industries expanding and others contracting in various member countries.

In conclusion, customs unions or common markets are important today for underdeveloped countries, not only because of the greater possibilities they offer for specialisation, economies of scale, better terms of trade, but also in general higher rates of development and industrialisation. It is wrong therefore, as most postwar trade policies advocated by the developed industrial countries tend to do, to adhere to the belief that measures of trade restriction such as tariffs are bad even for the countries instituting them. In fact if tariffs can lead to greater incomes in the developing countries they may even increase the volume and value of world trade.

However, it is also true that for most underdeveloped countries the formation of customs unions may lead to greater disparities in incomes of member countries. In a national economy, differences in incomes of various regions are minimised through government intervention; but in a customs union there is often no such mechanism. As the forces working towards polarisation are *initially* stronger, there will be a tendency for concentration of industry and general economic activity in certain areas to feed on itself. Where basic services are lacking in many areas, external economies are often more important than internal economies of scale. Moreover, entrepreneurs tend to take the view that there is safety in large numbers, and this is a psychological factor contributing to polarisa-

11. Balassa, *op. cit.*, page 16.

tion effects. Indeed, there seems to be much truth in the observation by Hirschman that entrepreneurs often tend to overestimate the size of external economies.[12] When there tends to be too much polarisation, deliberate intervention is called for. Such deliberate action can be effected through indirect instruments (e.g. differential tax rates in favour of those industries going to poor areas;) and direct ones (e.g. starting public projects in the areas lagging behind). These two sets of instruments should be used together; in particular indirect instruments are unlikely to do the job thoroughly.

Operation of the East African Common Market

The various stages by which a *de facto* common market has evolved in East Africa have already been noted. The move from a customs union to a common market has been facilitated by the existence of common boundaries, common services, similar history under Britain, and a common currency. However, each country retains its sovereignty; tariffs levied against foreign goods and even income tax rates need not be the same, although this is usually the case. The only mechanism for bringing about uniformity is the annual intergovernmental negotiations just before the presentation of national budgets.

The operation of the East African common market has been very much influenced by historical accidents. Though we cannot go into a detailed historical account, it is necessary to mention briefly the circumstances which have contributed to Kenya taking the lead in the common market. Kenya became a Crown Colony in 1920 after about twenty-five years of being a protectorate; because of its geographical position and attractive climate it attracted a substantial population of Europeans who settled in the country's fertile highlands and established a diversified commercial agriculture with Nairobi, Nakuru, Kitale and Eldoret as their major towns. Kenya also attracted even larger numbers of Indians who established themselves as traders in the major and small towns of the country. Uganda, on the other hand, did not attract as many Europeans and Indians, partly because of a less attractive climate but mainly because there was little official encouragement for European settlers to establish themselves in the country. In any case there was plenty of land in Kenya to settle all those who wanted to be farmers, besides the

12. See A. O. Hirschman, *op. cit.*, page 185.

very important point that Kenya was more accessible from the coast than Uganda. Uganda therefore remained an essentially peasant-based economy producing coffee and cotton for export, unlike Kenya where plantation agriculture has been of dominant importance. Tanganyika is somewhere between Kenya and Uganda. The Germans had started a major programme of development based on plantation agriculture, and had already laid down a relatively effective transportation system for evacuating produce from the hinterland. After the country became a British mandated territory at the end of World War I, further European settlement was not greatly encouraged, though the former German estates were maintained. So, whereas peasant production of export commodities has not been unimportant, there are quite a few large non-African estates producing coffee and the bulk of the country's sisal and tea.

These sketchy points help to explain why Kenya has taken the lead in the common market. Firstly, in East Africa entrepreneurial ability in the monetary sector has been among the immigrant communities (as has been the case in the development of some other underdeveloped countries, e.g. Malaya). This has meant that Kenya, with more Europeans and Asians, has been in a much stronger position to exploit the opportunities offered by the common market. Tanganyika has also had a larger population of Europeans and Indians than Uganda, but her immigrant communities have confined themselves to production of major export commodities and distribution. Secondly, the presence of a large European and Asian population in Kenya has meant that a good proportion of high incomes in East Africa has been concentrated there; in fact, nearly 50 per cent of East African monetary income is in Kenya. This has made it more attractive to set up in Kenya those industries catering for the East African market. This process has been reinforced by the fact that industries have also found it easier to recruit skilled labour, again mostly European and Asian, in Kenya. Thirdly, and partly as a result of the many Europeans within her borders, Kenya has been more favoured, at least economically, by British colonial policy. British assistance to Kenya has certainly been of great importance in establishing the existing economic base, especially in the agricultural sector.

There are other historical accidents which have been of considerable influence; but we shall mention only one. When the "Uganda

Railway" was being built from Mombasa, Nairobi became an important workshop and station and it was principally because of this factor that the city grew up in just this location.

The history of the common market has not been a peaceful one. There have been two major controversies among the three participating countries: the first was in the 1920's, and the second, starting in the late 1950's, is still with us today.

The first controversy was sparked off by protection, for which Kenya had fought hard, and won, early in the 1920's. Protective tariff rates had not been introduced before because the metropolitan powers ruling the "Congo Basin" countries, in which East Africa was included, had agreed at the Brussels Conference of 1890 that their dependencies were not to raise tariffs above 10 per cent. This tariff ceiling was removed by the Convention of St. Germain-en-Laye (although the policy of non-discrimination in tariffs was still maintained). Accordingly, after the end of World War I Kenya appointed a committee (the Bowring Committee) to investigate the possibilities of using tariffs for promoting development. This committee reported in 1922, and its recommendations for protecting selected domestic products, especially agricultural ones, were accepted by the Government. Protective tariffs, averaging between 30-50 per cent, were accordingly introduced in 1924 for sugar, timber, wheat and wheatflour, butter, cheese, ghee, ham and bacon. In fact it was stated by a later committee—the Kenya Tariff Committee of May 1929—that after 1922 Kenya "discarded the laissez-faire principle and deliberately adopted the principle of fostering suitable industries as the foundation of her economic policy . . . export duties were abolished . . . [and this made possible] a development policy assisted by customs tariffs . . . "[13]

Protection led to problems; as long as the tariff was designed to raise public revenue there was little danger of serious disagreements among the three countries, but once tariffs were used for protection, possible conflicts of interest increased. This controversy led to the appointment of the 1929 Kenya Tariff Committee already mentioned, and a similar committee in Uganda in November of the same year.[14] The Kenya Tariff Committee recommended continued exploitation of protective tariffs for promoting development, while Uganda

13. Kenya Government, *Report of the Tariff Committee*, May, 1929, Nairobi.
14. Uganda, *Report of the Tariff Committee*, November, 1929, Entebbe.

recommended their withdrawal. The Kenya committee argued that protection led to employment of local resources; that each East African country was in a position to establish similar industries as Kenya had if it so desired; and that, in any case, it was wrong to keep on changing tariff rates because this would introduce uncertainty and lack of confidence among entrepreneurs. The Uganda committee, on the other hand, argued that Kenya could not adequately supply the protected goods (in fact Tanganyika had already abolished the protective duty on butter for this reason); that Kenya goods were of poor quality and highpriced, and therefore exploited consumers in Uganda, especially Africans; and that the protected industries had not been able to stand on their own after seven years of heavy protection.[15] However, while convinced that "... any measure of protection either by special import duties or preferential railway rates would be wholly unjustified, and indeed a thoroughly unsound policy in the case of Uganda", the Committee went on to say that " . . . a customs union and arrangements for free interchange of goods between the three territories are of so great importance to the welfare of East Africa that it is worth some considerable sacrifice on the part of each territory concerned to ensure that there shall be a customs union in fact as well as in name . . ."[16] Here Uganda was taking the part of the consumer vis-a-vis Kenya, and had no intention of protecting her own industries.

To resolve this controversy a conference of the three countries was convened in 1930 and as a result some of the tariff duties were reduced, but protection continued. This protection was reinforced by railway tariffs which were higher on certain imports than exports. In fact the railway policy was aimed at expanding exports and taxing imports, and was justified on two grounds: (*a*) to make the railway pay (it was not doing very well; its first working profit of £2,639 was in 1905, and in 1920 its profit was even lower than this); and (*b*) to give further protection to local industries.

The operation of the railway led to another controversy in this early period between Uganda and Kenya. Prior to 1909 Kenya used to get all the revenue collected at Mombasa. Before the railway had been completed this had little effect on Uganda's revenue, for

15. The Uganda arguments were heavily influenced by the views of a tariff committee in India which had some time before laid down criteria for protection.
16. Uganda Tariff Committee, *op. cit.*, page 3.

about two-thirds, of her goods came and went through the German Territory of Tanganyika; but after most of her trade had shifted to Mombasa, Uganda's customs revenue dwindled. She put pressure to bear on Kenya and it was agreed that Kenya should hand over some of the customs revenue collected at Mombasa. However, this arrangement did not solve the problem of loss of revenue to both Uganda and Tanganyika due to the replacement of dutiable foreign imports by Kenya products which entered without paying duties. It is interesting to note that as early as 1932 it was urged that "Tanganyika should take steps forthwith to levy customs import duty (on goods from the rest of East Africa) at the same rate on *foodstuffs* imported from foreign parts, and should cease to deplete her revenue and impoverish her citizens by protecting the products of her neighbours",[17] (my emphasis).

Looking back, three things stand out. Firstly, the main arguments advanced by both Uganda and Tanganyika were based on the *welfare* effects the customs union was having in their countries. On the other hand Kenya's arguments were those of a producer, and they were designed to show the benefits of the customs union in stepping up the rate of development. Secondly, this early protection, although it did not lead to a spurt of industrialisation or even widespread economic development in Kenya, gave her an early start in some aspects of development, especially in industries processing foodstuffs, compared with the other two countries. This was important for Kenya because the late '20s and most of the '30s were bad years. As Kennedy has pointed out "... there can be no doubt that these [protective] duties did prove to be highly successful in encouraging a number of Kenya's industries *in a period when world economic conditions were far from conducive* to agricultural development,"[18] (my emphasis). Thirdly, the whole controversy illustrated the importance of working out in detail how customs revenue would be distributed once a group of underdeveloped countries, heavily

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17. Report by Sir Sydney Armitage-Smith, Cmnd. 4182, September, 1932. It is interesting to notice that it was the foodstuffs which were prominent in intercountry trade in this period. Nowadays the loss of revenue is greater because of the manufactured goods which Tanganyika imports from the rest of East Africa.

18. T. A. Kennedy, *op. cit.*, page 26.

dependent on customs duties for their revenue,[19] formed a customs union. This is always a thorny problem. As Viner says "whenever customs revenues are important, the method of their allocation as between members of a customs union is almost certain to become a major issue, which has a close counterpart in the controversies which have always arisen in federal unions over the distribution of revenues, or the allocation of taxation rights, as between the central and the regional political authorities".[20] This problem becomes even more acute where countries are at different levels of economic growth—with the advanced countries carrying out vigorous programmes of import substitution.

The controversies over protection ebbed dramatically during the years of the Great Depression, for this depression brought other difficulties and hardships. After the depression there was little controversy because Uganda's cotton, for instance, was doing very well; and during the Second World War attempts towards self-sufficiency were welcomed all round. This happy situation continued right through the Korean War commodity boom; there was prosperity in each country.

The Korean War commodity boom soon worked itself out, and East Africa, like most other underdeveloped areas, experienced a severe deterioration in her terms of trade, as the prices of coffee, cotton and sisal collapsed.[21] This was also the time when the three countries were seriously thinking of how to increase their rates of growth. The fall in export earnings made it very difficult to achieve

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19. It is always difficult to distinguish between revenue duties and protective duties, because the distinction is based on the purpose envisioned. To the extent that the domestic production does not wholly replace imports of similar goods, protective duties will also bring in revenue. Similarly revenue duties, by raising import prices, will have some protective effect on any similar goods produced at home.

20. J. Viner, *op. cit.*, page 78.

21. For East Africa as a whole, the quantity, price and value indices of domestic exports (Fisher's ideal indices with 1954=100) were:

	Quantity	*Price*	*Value*
1950 ..	81	88	71
1951 ..	88	130	114
1952 ..	102	121	123
1953 ..	92	96	88
1959 ..	158	78	124
1962 ..	171	76	130

Source: E.A.C.S.O. *Economic and Statistical Bulletin*, 1960 and 1963. Of the three countries Uganda was hardest hit.

this objective, especially for Uganda. In Tanganyika, unlike Uganda, the value of exports continued to rise, however. In Kenya the tremendous government expenditure which followed the outbreak of the 'Mau Mau' rebellion, together with the fact that intercountry exports to Uganda and Tanganyika had become an important source of income, helped to maintain a fairly respectable rate of growth. Uganda and Tanganyika therefore felt that they were not benefiting from the common market as much as Kenya. This sparked off the second controversy, which caused so much tension that the Raisman Commission was appointed to investigate and recommend how the working of the common market could be improved.

Three main arguments were advanced by Uganda and Tanganyika: (*a*) that the common market meant to them a "fiscal strait jacket" at a time when they needed fiscal policies different from those of Kenya; (*b*) that through importing Kenya goods instead of foreign ones they were losing substantial revenue; and (*c*) that they were losing an opportunity to industrialise, while not sharing the benefits that Kenya received from the growth of manufacturing. These arguments, especially the last, were dynamic compared with the welfare arguments used in 1920s. We shall discuss each argument in turn.

Limitation of Each Country's Economic Sovereignty

In a common market where there is free movement of goods and factors, each participating country's ability to follow an independent line in its economic policies is reduced. Firstly, a common market requires that customs duties in each country be substantially the same, or else commodities would come into the country with lower duties and then be transhipped into the partner-countries which levy higher duties. Secondly, there is also built-in pressure against following an independent fiscal policy in other respects. For instance if A and B form a common market and country A raises her company taxation, then firms, in so far as they could do this, would flee to country B, produce goods there, and sell them in country A without having to pay the higher taxes. Moreover, new firms would find country B more attractive, unless there were other factors in country A which offset her higher tax rates. Because of effects such as these, each country's government must feel that it cannot do much which is not done in the other participating

countries. The loss of sovereignty is particularly severe where there is no coordination in economic policies other than the tariffs.

In the East African common market the rates of income taxation and tariffs on imports are fixed by each government, and they need not be the same in all details, although a change in rates can only be introduced after consultations. However, tax rates and tariffs are substantially the same.[22] If, say, Uganda would like to attract capital otherwise going to Kenya by offering lower tax rates, while Kenya would like more revenue through higher company taxes, there is no solution to this kind of conflict except by bargaining for agreed rates. Above all it needs to be emphasised that if competitive tax inducements were offered, none of the three countries would benefit because such competitive inducements would cancel each other out, yet each country would lose revenue. In East Africa it is true that there has been little intercountry migration of capital; but this is very unlikely to remain permanently so in future, and therefore a common approach to industrialisation and development is required.

Loss of Revenue

In any common market where customs revenue is important to the participants, the allocation of this revenue must be a thorny problem. In the operation of the East African common market there is no doubt that by importing Kenya goods instead of dutiable foreign imports, Uganda and Tanganyika lose revenue; while in Kenya the loss of revenue due to import substitution is more than compensated for by increase in domestic incomes, revenue from company and personal income taxation, increase in employment, and development of skills. Kenya does lose revenue by importing goods from Uganda and Tanganyika which could have been taxed if imported from abroad, but what matters is the net result of these two effects. As Kenya sells more goods to the other two countries than she imports from them, and as she exports the bulk of East African intercountry exports of manufactured products, which

22. There are, of course, other taxes which need not be uniform, e.g. export taxes, but even here there is the possibility of smuggling goods into other countries where export taxes are not so high.

would carry the bulk of import duties if imported from abroad,[23] it is clear that the net result is revenue losses to both Uganda and Tanganyika. Moreover, this loss of revenue is likely to have become larger in the last few years for two reasons. (i) Kenya has been increasing her share in total intercountry exports, and particularly in intercountry exports of manufactured goods. (ii) The average rates of protection have been going up.

With regard to the level of protection, because of the difficulties involved in trying to summarise changes in individual rates of duty, perhaps the best way is to work out average rates of protection in various SITC sections. This has been done for 1958 and 1963, and the results are shown in Table VI.1. Average protection computed in this way would be somewhat different for each East African country because of differences in commodity composition of imports, but these figures do give an indication of protection in various SITC sections. It will be noticed that this protection has increased over the last six years. As Kenya's share in total intercountry exports is far greater than those of Uganda and Tanganyika, even when these are combined, it seems clear that on a net basis Kenya has not lost any revenue, while the other two countries have.

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23. One good way of illustrating this point is to look at the value of each country's exports in the various rates of duty which would be applied to similar goods if imported from abroad. Doing this for 1962 we get the following:

Rates of Duty and Country Exports to the Rest of East Africa, 1962
(£ million)

Duty, ad valorem	*Kenya*	*Uganda*	*Tanganyika*
Free	2.36	1.41	1.11
1—10%	0.90	0.01	—
11—20%	2.37	0.20	0.11
21—30%	5.28	2.24	0.62
31—40%	3.52	1.48	0.36
50—60%	0.78	0.62	0.07
75%	0.16	—	—
200—230%	1.94	1.09	0.13

It will be noticed that a good proportion of Kenya's intercountry exports enjoy considerable protection. For instance, if we take all intercountry exports with a protective duty of 31-40 per cent, Kenya's share in these exports was 65.7 per cent, compared with 27.6 per cent in the case of Uganda and only 6.7 per cent in the case of Tanganyika.

TABLE VI.1.

Average Protection by SITC sections, 1958 and 1963[a]

SITC		1958 Value[b] (£thous)	1958 Duty (£thous)	1958 Average Protection[c] (%)	1963 Value[b] (£thous)	1963 Duty (£thous)	1963 Average protection[c] (%)
0. Food ..	..	7,206	928	12.88	8,199	1,660	20.24
1. Bev. & Tob.	..	1,426	3,027	212.28	1,155	2,626	227.40
2. Crude materials	..	911	39	4.23	1,392	52	3.73
3. Fuels ..	..	13,419	2,710	20.19	12,879	9,196	71.40
4. Oils and Fats	..	795	32	4.03	1,257	113	8.96
5. Chemicals ..	..	7,162	572	7.99	10,094	901	8.95
6. Mfd. Prod. ..	..	36,161	6,792	18.78	44,607	11,769	26.38
7. Machinery ..	..	28,221	1,816	6.44	36,033	4,508	12.51
8. Misc. Mfd. ..	..	7,893	1,795	22.74	11,335	3,225	28.45
9. Other ..	..	6,672	1,374	20.60	6,383	1,561	24.45
TOTAL	..	109,866	19,085	17.37	133,334	35,612	26.71

Notes: (*a*) I am indebted to Mr. D. Ghai for these figures.

(*b*) Value of net home consumption imports less government duty-free imports for the whole of East Africa.

(*c*) Duty as percentage of value.

This conclusion is further supported by examination of the role which intercountry imports play in each country's need for all imports. In Table VI.2. each country's intercountry imports and retained imports are shown by SITC sections for 1959 and 1963. It will be observed that in various SITC sections, but especially in those sections containing consumer manufactured goods, both Uganda and Tanganyika get larger proportions of their import requirements from intercountry trade than Kenya does. For example in SITC sections 5, 6, and 8 intercountry imports were 60.4 per cent, 29.6 per cent, and 52.7 per cent respectively of Uganda's retained imports in 1963; and in Tanganyika the corresponding ratios were 46.0 per cent, 24.8 per cent, and 57.8 per cent respectively. These ratios are very large when compared with those of Kenya, which were 4.3 per cent, 7.7 per cent, and 9.2 per cent, respectively. Moreover, the ratio of intercountry imports to both Uganda's and Tanganyika's retained imports of manufactured consumer goods has increased tremendously since 1959, and it is therefore arguable that revenue loss to these two countries has been increasing over time.

TABLE VI.2

Comparison of Retained and Intercountry Imports, by Country, 1959 and 1963

(£)

	1959			1963		
SITC	*Retained Imports (A)*	*Intercountry Imports (B)*	*B%A*	*Retained Imports (A)*	*Intercountry Imports (B)*	*B%A*
KENYA						
0	4,911,710	1,375,881	28.0	3,994,729	3,499,098	87.6
1	809,891	1,419,233	175.2	663,831	1,068,546	161.0
2	*a*	508,126		800,540	672,235	84.0
3	5,903,474	260,233	4.4	5,894,006	386,432	6.6
4	250,376	1,094,143	437.0	652,827	956,888	146.6
5	4,335,746	157,406	3.6	5,991,461	258,301	4.3
6	17,652,159	604,486	3.4	22,223,207	1,758,241	7.7
7	14,921,575	3,393	—	16,369,871	13,782	0.1
8	4,482,165	61,295	1.4	5,868,098	539,386	9.2
9	3,249,756	3,999	0.1	4,083,136	10,426	0.3
Total	56,516,852	5,488,195	9.7	66,541,706	9,163,335	13.8
UGANDA						
0	1,108,307	2,455,711	221.6	1,081,907	2,382,659	220.2
1	200,897	1,248,133	621.3	180,925	1,303,123	720.3
2	59,169	126,775	214.3	259,596	127,711	49.2
3	1,346,677	15,728	1.2	879,729	21,112	2.4
4	278,845	199,556	71.6	302,150	192,295	63.6
5	1,855,737	461,248	24.9	2,117,107	1,278,116	60.4
6	9,366,422	1,302,376	13.9	10,037,785	2,969,120	29.6
7	6,721,962	42,373	0.6	8,839,228	94,467	1.1
8	2,292,630	642,234	28.0	2,912,300	1,535,692	52.7
9	1,166,774	15,734	1.3	1,287,938	29,016	2.3
Total	24,397,420	6,509,868	26.7	27,898,665	9,933,311	35.6
TANGANYIKA						
0	2,325,780	2,356,658	101.3	2,800,274	3,007,508	107.4
1	270,404	2,056,559	760.6	226,526	2,149,408	948.9
2	*b*	92,497		252,508	107,049	42.4
3	2,529,183	3,220	0.1	2,641,617	27,838	10.5
4	142,255	309,964	217.9	297,658	243,784	81.9
5	2,024,384	526,710	26.0	2,589,896	1,191,619	46.0
6	12,992,529	1,747,498	13.5	14,174,558	3,521,619	24.8
7	8,828,719	56,802	0.6	11,277,594	96,703	0.9
8	2,457,576	899,342	36.6	3,367,630	1,945,200	57.8
9	1,040,152	50,901	4.9	1,204,139	67,399	5.6
Total	32,610,982	8,100,151	24.9	38,832,400	12,358,127	31.8

(*a*), (*b*). Retained imports in these figures were negative. In the case of "a" re-exports were £759,591 while net imports were £671,416. In the case of "b" re-exports were £198,770 while net imports were £112,586.

A crude method of estimating this loss of revenue is to multiply Kenya's exports to the other two countries by the appropriate rate of duty had the goods been imported from abroad (call this A), to do the same for these countries' exports to Kenya (call this B), and then subtract B from A. From this estimate we should also deduct the net revenue which these countries get from intercountry imports of excisable commodities (sugar, beer, cigarettes, tobacco, spirits, and matches), for excise tax revenue is credited to the consuming country. This method is quite crude, of course, because it is based on the very brave assumption that income levels and patterns of consumption in the three countries would have been the same even if the tariff preference within the common market had not existed. However, this calculation was attempted for 1962. Unfortunately, it was found very difficult to deal with excisable commodities. Partly the problems were statistical; some of the excise tax rates are given by specifications which are not found in the intercountry trade data, e.g. excise tax rates on cigarettes are given by various weights of the packet, while in the trade data cigarettes are shown by whole pounds. More fundamentally, however, in the case of excisable commodities it was felt that our assumption that consumption levels and patterns would have been the same was very unrealistic indeed, in view of enormous differences between import duties on the imported grades of commodities and excise tax rates on the domestically produced grades. To take cigarettes, for instance, while import duties were Shs. 44/- per lb. in 1962, the average excise tax rate was only Shs. 15/-. Applying our method mechanically, and multiplying the Shs. 29/- difference by intercountry trade in cigarettes, Tanganyika would have appeared to have lost over £2.4 million in 1962 on this one commodity. Actually, however, if excise tax rates were the same level as import duties, the prices of domestically produced grades of cigarettes would generally have doubled; and this would have led to a drastic reduction in the consumption of this commodity. Similar effects would have taken place in most of the other excisable commodities. It was therefore felt that it was better to omit excisable commodities from the revenue loss calculation.

For all dutiable non-excisable commodities in each country's intercountry exports and imports in 1962, it was found that Tanganyika lost £1,783,000 in customs revenue, and Uganda £204,000.

These figures are smaller than one would expect from the volume and intensity of controversy centred on this point. Tanganyika loses much more than Uganda does because (*a*) Uganda, unlike Tanganyika, has major intercountry exports, notably cotton fabric piecegoods, which enjoy considerable protection; and (*b*) Tanganyika's intercountry trade deficit is much larger than that of Uganda.

The loss of revenue to Uganda and Tanganyika would not be a serious issue but for the fact that these countries' shares in intercountry exports are so small compared with that of Kenya. It has at times been suggested that in order to solve this problem of revenue loss, excise taxes equal to import duties should be put on domestically produced goods, and the revenue from these additional excise taxes should also be credited to the consuming country. Superficially, this may appear attractive since any country which wanted to encourage import substitution could reimburse the industry producing import substitutes the excise taxes paid on its products. However, levying excise taxes equal to import duties would *totally eliminate* protection of domestic products against competing foreign imports. Moreover, as the Raisman Commission pointed out, such a device would give disproportionate benefits to the consuming country; not only would it avoid any loss in revenue due to import substitution in the other countries, but it "would also receive such increments in [its] government revenue as resulted from the spilling-over into [it] of increased demand from the [countries] producing the import substitutes in question". [24]

After examining this problem of revenue loss, the Raisman Commission came out with a novel solution—a formula for revenue distribution based on the operation of a common revenue pool. This solution was based on the belief that "the common market is of such great importance to [the East African countries'] economic future, and the danger to it from internal strains so great, that some inter-territorial redistribution of income, offsetting in some degree the inequalities in the benefits derived, is urgently called for in order that the common market may be preserved".[25] The formula suggested was that a Distributable Pool of Revenue be established from (*a*) 40 per cent of net yearly proceeds from income tax charged

24. Raisman Commission Report, page 28.
25. *Ibid:* page 65.

on the profits of manufacturing and finance companies operating in the three countries; and (*b*) 6 per cent of each country's net yearly collection of customs duties and excise taxes. This revenue was to be distributed as follows; (*a*) 50 per cent to the E.A.C.S.O. services which do not finance themselves (e.g. income tax department, customs and excise department, statistical department); and (*b*) the remaining 50 per cent to be distributed in equal parts to the three countries. The share to E.A.C.S.O. was designed to give these non-self-contained services some measure of financial independence, instead of depending on yearly votes from each country; while the other half of the distributable pool was designed to transfer income from Kenya to Uganda and Tanganyika—since Kenya would pay more into the pool than she would get out of it. A calculation based on the Raisman formula for income distribution is set out in Table VI.3. for the 1962/63 fiscal year.

TABLE VI.3

Operation of the Distributable Pool of Revenue, 1962/63

(£ *thousand*)

	Kenya	*Uganda*	*Tanganyika*	*Total*
Customs and Excise	1,209	723	827	2,759
Income Tax	947	189	236	1,372
Less collection costs	54	23	27	104
Gross contribution	2,102	889	1,036	4,027
Less 50 per cent distribution	671	671	671	2,013
Net contribution	1,431	218	365	
Estimated contribution by old system	694	506	677	1,877
Gain or Loss	−737	+288	+312	
Payments to E.A.C.S.O. on Raisman Formula				2,014
Payments to E.A.C.S.O. on previous system				1,877
Gain to E.A.C.S.O. on Raisman Formula				137

Source: Unpublished information from E.A.C.S.O.

From the calculations in Table VI.3. it will be noticed that in the 1962/63 fiscal year Kenya "lost" £737,000—which was distributed to Tanganyika (£312,000), Uganda (£288,000), and E.A.C.S.O. (£137,000). We should also observe that while the revenue gain to Uganda from the pool approximates her revenue loss estimated earlier, in the case of Tanganyika the Raisman formula does not go

far enough in offsetting this country's estimated loss of revenue. A better way of income redistribution would be to relate each country's contribution to the distributable pool to intercountry exports. There are also several other observations we can make on the Raisman formula.

First, the Commission was quite right in singling out, as the sources of revenue for the pool, those industries which can be said to depend on the common market as a whole, i.e. manufacturing and finance companies. However, the Commission did not go to the root of the problem. Instead of just looking at the differential rates of growth and devising ways of mitigating their *fiscal* effects, the Commission should have concentrated on the *causes* of these inequalities; then perhaps they could have spent some time investigating possible ways of distributing industries among the three countries. In absence of a strong political union this must be the solution—for what Uganda and Tanganyika want is not just extra revenue but a share in the industrialisation process taking place in East Africa. In any case the sums distributed to these two countries are very small compared with the benefits of more industry, employment, development of skills, and higher incomes generally. The major weakness of the Raisman formula, therefore, is that it stresses the revenue problem instead of the more fundamental development problem of each country. Moreover, a case could be made that the funds transferred from Kenya to the other two countries could perhaps, from an economic efficiency point of view, be more productively used in Kenya.

Secondly, it is doubtful if the Kenya Government, faced as it is with substantial and persistent deficits, will be prepared to borrow from abroad (indirectly) in order to "compensate" Uganda and Tanganyika, where similar problems may be non-existent. Moreover, in a scheme like the Raisman formula frequent negotiations about percentages to be channelled into the pool are necessary and may lead to strong political conflicts. This is especially so because the more Kenya establishes industries the more she will have to pay to the other countries. It should also be pointed out that the Raisman formula was based on rates of taxation (of companies and imports) which were in force in 1961; if these tax rates are to rise by more than they have done already, the possibilities of conflicts over revenue allocation will be increased.

Thus the Raisman device should not be regarded as a permanent solution to this particular aspect of the effects of the common market. In any case the operation of this device since it was put into effect does not seem to have reduced strains and controversies in the common market. However, as a temporary measure before more appropriate policies are formulated the Raisman device is commendable. In particular we should notice that it has enormously improved the system of financing the non-self-contained services of the E.A.C.S.O. Previously, finance for these services was voted annually by each country; and as a result these services could not plan ahead. Moreover, even though each country's contribution was to be in proportion to the amount of services rendered to her, it was always difficult to estimate this amount. The Raisman formula, by giving these E.A.C.S.O. services an independent source of finance, has been a tremendous improvement.

We should end this section by discussing briefly an argument, related to the loss of revenue controversy, that Uganda and Tanganyika are "exploited" by Kenya—because she sells some goods to them at prices higher than those she obtains in foreign markets. Domestic prices higher than f.o.b. export prices can be charged because the prices of competing imports include cost, insurance, freight, and import duty. Domestic producers therefore can raise their prices to the level of import prices. If there were sufficient competition among domestic producers, domestic prices might be forced down to f.o.b. export prices; but there is not sufficient competition in East Africa *as yet*, and it is therefore likely that domestic prices are higher than need be. This means that all *East African consumers* are "exploited", not just Uganda and Tanganyika. Moreover, as most of Kenya's production is consumed in Kenya, the exploitation is greatest there. We should also notice (*a*) that in the early post-World War II period the prices charged by Kenya for a number of agricultural intercountry exports were substantially lower than the prices prevailing in world markets;[26] (*b*) that prices charged for some important agricultural commodities —notably ham and bacon—have been generally lower than import prices *exclusive* of import duty; and (*c*) that with more development in East Africa competition among domestic producers should

26. See Raisman Commission Report, page 8.

increase and thus lead to lower domestic prices. This, incidentally, emphasises the need for *freer* intercountry trade.

Unequal Growth Rates

In this section we shall limit most of our discussion to the period 1954 to 1961; it was during this period that distinct differences in the pattern and growth rates of the three countries emerged, and it was in 1961 that the Raisman Commission's correction formula was introduced. From the data provided in table VI.4 it will be seen that whereas Kenya's monetary gross domestic product increased by £64.3 million between 1954 and 1961, the increases in Uganda and Tanganyika were £18.5 million and £34.4 million respectively. Kenya's annual rate of growth was 6.7 per cent, compared with 5.2 per cent for Tanganyika and only 2.7 per cent for Uganda. If we agree with the World Bank Mission to Uganda that "there can be little doubt that the satisfactory rate of growth of East African *as a whole* has been facilitated by the existence of the common market"[27] (emphasis added), then it is easy to conclude, as Uganda and Tanganyika seem to have done, that Kenya has been benefitting almost at the expense of her partners. However, the lower overall rates of growth in Uganda and Tanganyika are not to be attributed solely to the slower growth of these countries' intercountry exports. Since these countries depend more on exports of primary commodities, they have been more affected by the deterioration in their terms of trade.

The effects of the fall of export prices were especially severe for Uganda. This country's export price and quantity indices, with 1954 as the base year, stood at 63 and 147 respectively in 1962;[28] thus but for the fall in prices her domestic export earnings would have been £59.4 million in 1962 instead of the realized value of £37.6 million. Her monetary gross domestic product in 1962 would therefore have been greater by the difference between the two figures *plus* any additional income through multiplier effects of larger export earnings. The importance of domestic export earnings in both Uganda and Tanganyika is clearly brought out by the sudden increases in these countries' monetary GDP in 1963. Uganda's

27. *Economic Development of Uganda*, report of the International Bank for Reconstruction and Development Mission, page 91.

28. See Uganda Government, 1963 *Statistical Abstract*, page 28.

TABLE VI.4

Monetary Gross Domestic Product, Domestic Exports, Intercountry Exports, and Gross Capital Formation, 1954-63
(*£ million*)

	KENYA				*UGANDA*				*TANGANYIKA*			
	Monetary G.D.P.	*Domestic Exports*	*Inter-country Exports*	*Gross Capital Formation*	*Monetary G.D.P.*	*Domestic Exports*	*Inter-Country Exports*	*Gross Capital Formation*	*Monetary G.D.P.*	*Domestic Exports*	*Inter-Country Exports*	*Gross Capital Formation*
1954	112.5	20.3	5.5*a*	35.3	92.7	40.6	5.8*a*	18.6	79.1	36.2	1.2*a*	21.8
1955	134.7	25.7	5.7*a*	43.8	102.0	41.9	5.7*a*	23.2	81.8	36.2	1.7*a*	24.6
1956	145.2	29.0	7.6*a*	45.7	102.8	40.4	2.7*a*	21.8	89.3	44.9	2.1*a*	23.3
1957	154.2	26.4	9.7*a*	45.6	109.4	45.9	3.9*a*	20.4	92.9	39.4	2.6*a*	24.1
1958	155.5	29.3	10.8	40.0	106.4	45.4	4.8	19.6	98.0	41.7	2.6	22.7
1959	161.8	33.3	12.3	40.3	107.8	42.1	5.2	17.1	106.2	45.3	2.6	21.8
1960	175.3	35.2	13.8	41.4	110.5	41.6	6.7	19.0	114.5	54.8	2.3	25.0
1961	176.8	35.3	16.0	31.9	111.2	39.2	6.9	17.3	113.5	48.7	2.2	24.9
1962	180.9	37.9	17.3	33.3	107.9	37.6	7.1	16.5	123.3	51.2	2.4	24.4
1963	193.3	43.8	19.8	29.0	128.7	51.5	8.2	19.4*b*	140.3	63.6	3.4	25.1

Notes: (*a*) In these figures we have estimated and excluded the amount of excise tax revenue on cigarettes, tobacco, beer, and sugar. 1958-63 Intercountry exports are comparable, and do not include excise taxes or customs duties on inputs.

(*b*) Estimate

Sources: *Statistical Abstracts.*

export earnings increased from £37.6 million in 1962 to £51.5 million in 1963, and her monetary GDP increased from £107.9 million to £128.7 million.

In Tanganyika, on the other hand, the prices offered for her domestic exports were about the same as those offered for Kenya's domestic exports throughout the whole period. Moreover, the value of Tanganyika's domestic exports did not decline, as in Uganda but increased from £36.2 million in 1954 to £54.8 million in 1960, from where it declined to £48.7 million in 1961 and then recovered immediately. It therefore seems possible that, when compared with Kenya, the lower rate of growth of Tanganyika's monetary GDP might be partially explained by the lower rate of growth of her intercountry exports.

In order to give some indication of the importance of each country's intercountry exports in the growth of her monetary GDP, a simple regression of each country's monetary GDP on intercountry exports plus domestic exports plus gross capital formation was attempted for the period 1954 to 1963. The regression equation thus:

$$GDP_m = a + b\ A$$

where GDP_m=monetary gross domestic product,

and A=intercountry exports+domestic exports+gross capital formation.

The increase in GDP is the "multiplier" (i.e. b) times the change in A:

$$\Delta GDP_m = b \Delta A$$

=b (change in intercountry exports)+b (change in domestic exports)+b (change in gross capital formation).

The regression equations for the three countries were:

Kenya: $GDP_m = -\ 45.638 + 2.493\ A$, $r = .930$

Uganda: $GDP_m = 33.823 + 1.096\ A$, $r = .618$

Tanganyika: $GDP_m = 29.930 + 1.847\ A$, $r = .948$

Unfortunately the fit in the case of Uganda was so bad that this country was left out for this particular part of the analysis.

Comparing Kenya and Tanganyika, however, using their regression equations, a revealing contrast emerges. Over the period 1954-61,

when Kenya's economy was growing at 6.7 per cent per year, rising inter-country exports "explained" over two-fifths of the increase and rising exports abroad nearly three-fifths; the fall in gross capital formation actually tended to decrease gross domestic product, and there was some increase unexplained by the equation. In Tanganyika during the same period, with the economy growing at 5.2 per cent per year, rising intercountry exports explained only 5 per cent of the increase, whereas rising exports abroad accounted for over two-thirds, and rising gross capital formation about a sixth; there was also a small unexplained increase. The substantial contribution of intercountry trade to Kenya's growth, and its small contribution to Tanganyika's growth, are apparent. We can also consider what might have happened if Tanganyika had succeeded in expanding her intercountry exports more rapidly. If they had risen by £5 million instead of £1 million, i.e., if she had increased her intercountry exports by approximately the same amount as her intercountry imports, this would probably have added about £7.5 million to monetary gross domestic product, and raised her rate of growth from 5.2 per cent to 6.3 per cent per year. Of course, raising any of the other demands included in A would have had a similar effect; for instance, expanding exports abroad by 5.5 per cent per year rather than 4.4 per cent (compared to Kenya's 8.2 per cent), would also have added about £7.5 million to GDP.

Summarising our discussion in this section we can say that Kenya has been growing faster than her partners, partly because she has benefited more from the common market, in the sense that her sales to the other two countries constitute a higher percentage of her monetary GDP. However, as we have already pointed out, there are other causes of these unequal rates of growth—some intrinsic in Kenya's location and economic structure, and some associated with the growth of other demands on the economies.

In the working of the common market there has been one body, the Industrial Council, which could perhaps have reduced this industrial concentration in Kenya. The aim of the Council was to encourage the establishment of industry on an East African basis, to provide protection, and to discourage duplication. But the Council did not have much authority and there was no comprehensive plan on which it was to operate. Very soon after its establishment Uganda and Tanganyika, which were receiving very few industries

in comparison with Kenya, refused to allow more industries to be added to the list of industries which required a licence before being established. The Council has therefore achieved very little in industrial direction. But as we shall see in the next section, there is tremendous scope for further import substitution, and it is here that industrial allocation to each country on an East African basis could be tackled with substantial benefits to all three countries.

Further Scope for Import Substitution

In economic theory there seems to be no accepted measuring rod for assessing the benefits accruing from a common market. One interesting point has been suggested by Professor Meade. He says that "in order to determine whether a customs union on balance raises or lowers the total cost of production . . . we must consider not only the total volume of trade on which costs have been raised and the total on which costs have been lowered; we must also consider the extent to which costs have been lowered on each unit of the newly created trade."[29] In other words the method suggested is to multiply each item of trade diverted by the rise in the unit cost (call this the negative item), and to multiply each item of the trade created by the fall in unit cost (call this the positive item); if the negative item is lower than the positive item then the customs union has, on balance, been beneficial.

Whereas this method is certainly better than the one which seems implicit in Viner's analysis,[30] i.e. merely subtracting the volume of trade diverted from the volume of trade created, yet it rests (and Meade clearly admits this) on the assumption that all demand elasticities are zero and all supply elasticities infinite. This must be so because if after removal of the tariff (and therefore lowering of the price) there is a greater consumption of the goods in question, it would be wrong to multiply the *new* volume of trade with the change in unit cost for this would only make sense if the volume of trade remained constant. Moreover, in this method, no account is taken of any *changes in the commodity composition* of the trade among the participants; for example new goods which are now introduced to serve the whole of the customs union are not considered.

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29. J. E. Meade, *op. cit.*, page 35.
30. Jacob Viner, *op. cit.*, 1950.

In East Africa what one should do, ideally, in order to assess the benefits[31] of the common market, is to *imagine* what the development would have been like, both in magnitude and structure, in the absence of the common market, and then to compare this mental picture with the existing one. This would not be a simple task, if indeed it were possible; therefore any attempt to assess the benefits and costs of the common market to East Africa as a whole must include non-quantitative judgments. The truth is that we do not know what would have happened had the common market not been established. Nevertheless, examination of trade data and the existing industries in East Africa as a whole, in Chapter IV above, suggests strongly that the common market has been of crucial importance in the development of the area as a whole.

As far as the existing industries are concerned, it helps to think of three types of industries: (*a*) those industries which can flourish in each country's domestic market; (*b*) those industries which can flourish in each country's domestic market *plus a fraction of the market* of another country; and (*c*) those industries which depend *on the whole* of the East African market. In the first category there is a whole range of industries which each country could support—bakeries, repair workshops, furniture and fixtures, and many others. For these industries the domestic market of each country is sufficient. In the second category we have such industries as dairy products, tobacco manufacture, and footwear, whose exports represent only a small proportion, but a vital one, of their gross output. These industries depend on the common market in varying degrees. In the Kenya meat industry in 1961 the gross production was £5.5 million; of this local consumption was £2.8 million, exports to Uganda and Tanganyika were £0.4 million, while exports to the United Kingdom alone were £1.6 million. In the beer industry gross output was £3.7 million, exports to all countries were £713,000, and of these £698,000 went to Uganda and Tanganyika. In the case of wheat flour total production was 68,000 tons, and of this Kenya absorbed 51,100 tons while exports to the rest of East Africa were 17,000 tons. On the other hand, the Kenya footwear

31. In this discussion we shall leave out *administrative* advantages which in some cases could be very substantial. The saving in having only one customs and excise department instead of three must be quite large, especially now that East Africa does not have many trained personnel to do the job properly.

industry depends more on the common market: in 1961 of the total Kenya exports of 1,605,000 pairs of shoes, 1,400,000 went to Uganda and Tanganyika.[32] Although some of these exports might appear small in relation to total output of the goods concerned, they are nevertheless important; depending on the nature of cost curves, inability to export them could lead to higher costs if outputs were curtailed.

In the third category there are some industries which but for the existence of the common market would probably not have been established, or if established they would not be doing nearly as well as they are doing now. The best examples of such industries are the Nyanza Textiles factory at Jinja, the proposed iron and steel plant in Uganda, the proposed paper factory in Kenya, and the truck assembly plant proposed in Tanganyika's plan. More of this kind of development can be expected in the future if the common market is preserved. Among the industries which can be expected to benefit particularly are iron and steel and manufactures thereof, asbestos, fertilisers, paper and paperboard, chemicals, motor tyres and tubes, and several food manufacturing industries. Then there are those industries which have yet to be established.

There are also other things the common market has done for East Africa which we cannot quantify; for instance but for the common market the three countries probably would not have received as much foreign capital as they have done.

However, we feel it is even more important to examine potential future benefits through greater import substitution. In current discussion about unequal growth rates and unequal distribution of industrialisation in East Africa, even from the reports of the Raisman Commission and various World Bank Missions, one would get the impression that industrialisation in Kenya is now extensive and well-established. This is not so: as we have already mentioned, in 1962 the share of manufacturing in the monetary GDP of Kenya was only 12.8 per cent, or £23.0 million.Moreover, many of these industries are very small, as the figures in Table VI.5 illustrate.

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32. For this and other figures see Kenya Government, *Census of Manufacturing*, 1961.

TABLE VI.5

Gross and Net Output of Manufacturing Industries in Kenya, 1957 and 1961
(£ *Thousand*)

	1957		1961	
	Gross Output	*Net Output*	*Gross Output*	*Net Output*
Meat products	2,962	412	5,544	956
Dairy products	3,583	250	4,439	388
Canned fruit and vegetables ..	650	162	747	169
Grain mill products	7,156	1,056	8,612	1,477
Bakery products	1,582	325	1,870	389
Sugar	918	278	1,562	431
Chocolate & sugar confectionery	82	18	123	40
Miscellaneous foods	396	78	475	97
Beer and malt	2,769	1,479	3,677	1,746
Mineral waters & squashes ..	1,002 }	2,077	1,095 }	1,742
Tobacco	3,681 }		3,001 }	
Cordage, rope & twine	716 }	313	1,184 }	631
Textiles, spun, woven & knitted	138 }		737 }	
Clothing	361 }	398	632 }	897
Footwear	891 }		1,442 }	
Sawn timber	1,599	645	1,213	622
Other wood products	35	13	91	32
Furniture & fixtures	1,031	434	875	370
Pulp, paper & paperboard ..	600	218	1,261	375
Printing & publishing	1,707	878	2,428	1,095
Leather and leather goods ..	173	19	453	116
Rubber products	344	122	454	119
Basic industrial chemicals ..	2,469	981	2,441	1,350
Soap	1,373	334	2,409	504
Misc. chemical products	518	159	5,027	427
Clay and concrete products ..	545	262	481	143
Cement & other mineral products	2,789	1,275	3,358	1,966
Non-electrical machinery ..	520	163	657	326
Electrical machinery	155	62	212	116
Shipbuilding & repairing	748	430	748	432
Railway rolling stock	1,820	799	2,504	960
Motor box bodies	395	147	279	102
Motor repairs	1,334	564	1,214	461
Metal products	2,621	644	3,741	1,088
Miscellaneous manufacturing ..	522	178	536	204
Total	48,185	15,173	65,521	19,769

Source: Kenya Government, *Census of Manufacturing*, 1961.

The limited extent of present industrialisation is an important point to keep in mind when discussing distribution of industry in East Africa. The first problem is really how to increase the volume of industrial activity, and after that to devise ways of allocating the increasing volume to each country. Redistribution of the existing industrial activity would confer little benefit to Uganda or Tanganyika, and would very likely do almost permanent harm to

future industrialisation in East Africa as a whole. Possible ways of distributing manufacturing activity, given that the first goal is to increase its volume, are discussed in the final chapter of this study.

The scope for more import substitution is still very great in East Africa. Just looking at some items which East Africa already produces, but not in enough quantities so that she still imports from abroad to meet part of domestic demand, we get the list in Table VI.6. The value of these imports exclude duty; if this is added, then the real value is in the order of £40-45 million.

TABLE VI.6

Selected Imports, for Commodities already produced in East Africa, 1963
(*£ Thousand*)

Commodity	£ Thousand
Tinned milk and cream	1,385
Manufactured tobacco, incl. cigarettes & cigars ..	177
Matches	257
Chemicals, organic and inorganic	1,179
Manufactured fertilisers	1,288
Disinfectants, insecticides, etc.	1,281
Footwear	553
Clothing	3,997
Blankets, travelling rugs	1,517
Cotton fabrics	8,608
Corrugated iron sheets	418
Other iron sheets, plates, hoops, strips etc.	3,585
Paper & paperboard manufactures	4,090
Wood and cork manufactures	517
Rubber tyres and tubes	2,864
Soap and cleansing preparations	672
Paints and varnishes	884
Total	33,273

Source: Annual Trade Report of Kenya, Tanganyika and Uganda 1963.

Most of the commodities listed in Table VI.6 are consumer goods, more or less simple goods which are capable of being replaced entirely by domestic products. It is unwise to treat industrialisation as the existence of such spectacular plants as iron and steel mills. Industrialisation has to start with simple manufactures, and as import substitution succeeds the foreign exchange saved can be used to import more capital goods. East Africa will continue to depend on foreign sources for the majority of capital goods for a long time. Moreover, as manufacturing activities increase the country becomes better prepared to engage in the production of more sophisticated goods.

Most relevant to our present discussion, however, is the point that it is only through greater import substitution in East Africa as a whole that Uganda and Tanganyika will raise their percentage shares in intercountry exports, especially of manufactured goods. The best way to increase the total volume of import substitution is to tackle it on an East African basis, as the Kampala Agreement seems to have recognised, if only in part. If such planned import substitution on an East African basis could be increased, the three countries would mutually gain, and there would also be less tension in the common market.

The feasibility of more import substitution has recently been questioned, especially by Professor A. J. Brown.[33] Brown sets out to investigate those industries which can be established with advantage in East Africa. To do this he computes ratios of total consumption of a number of products in East Africa to the production of those goods by the median-size United Kingdom plant in that industry—median being defined in terms of employment. If the East African local consumption could support a median-size U.K. plant, then the industry in question could operate efficiently in East Africa, and vice versa. Brown then looks at some of the plants at present operating in East Africa and their levels of employment (the cotton textile plant in Uganda: employment 1,400; Kenya tobacco factory: employment 1,120; seven establishments engaged in shipbuilding and rollingstock repairs: average employment 920; the Kenya shoe factory: employment 800; three establishments in the jute, sisal and coir industry: average employment 500; two fruit and vegetable canneries: average employment 400; eleven establishments in sugar, brewing, fats and miscellaneous food manufacturing: average employment 300) and comes to the conclusion that "despite the limitations of the market and the shelter of substantial tariff, manufacturing establishments [in East Africa] seem to show the same effects of technical indivisibilities and other factors favouring large scale as do those in developed countries: indeed it is arguable that they are acted upon more strongly by them." The implicit conclusion is that since the market size in East Africa is small, then very little *efficient*

33. A. J. Brown, "Economic Separation versus a Common Market in Developing Countries," *Yorkshire Bulletin of Economic and Social Research*, Vol. 13, May, 1961, pp. 33-44; also in the November issue of the same journal.

import substitution can be expected—for the sizes of efficient plants would be too large for domestic demand.

Professor Brown's method is questionable on a number of grounds. Firstly, it seems inappropriate to use United Kingdom data, for since East Africa has different factor endowment from Britain, she should not necessarily use the same method of production. In any case industrial data of slightly more advanced developing countries where import substitution has been carried to a greater degree than in East Africa would have been more relevant.[34] Secondly, such an analysis, concentrating as it does on the current methods of production and size of demand, is quite static. In establishing factories in East Africa, local entrepreneurs are not only interested in the existing demand but also in the future size of the market, especially since quite a few have legal assurance of protection against potential competitors until 1973. Thirdly, it seems dubious to think of efficiency, as Brown does, purely in terms of technology; for the feasibility to operate efficiently the various sizes of plants will also depend strongly on other factors, such as the availability of finance and skilled labour. Fourthly, the whole analysis breaks down the moment export possibilities are brought in, although as we noticed earlier the export prospects of manufactured goods from the developing countries are not bright.

Fundamentally, even apart from the now familiar argument of near zero marginal productivity of labour in the subsistence sectors of underdeveloped countries, the foreign trade prospects of these countries mean that they must aim at industrialising themselves if they are going to raise living standards and give employment to their increasing population.[35] Import substitution does not

34. However, the problem arising from the fact that most of the capital goods which underdeveloped countries use in their industries come from developed countries is an important and relevant issue: for those capital goods are designed for use in countries where factor endowments are different from those of the developing countries, and they usually aim at economising on labour whereas in the developing countries it is labour which is abundant and capital scarce. It is therefore becoming increasingly apparent that underdeveloped countries should attempt to develop engineering industries aimed at producing capital goods more appropriate to their factor endowment. It is also to be hoped that technological advance will lead to the production of capital goods which can be employed efficiently on small-scale operations.

35. One of the problems facing the developing countries is that their populations are increasing at very high rates. Whereas it is relatively easy these days to bring down death rates, it is not so easy to reduce high birth rates. It is only after children become "expensive" that high birth rates are easily reduced, as is seen in the history of the now developed nations.

mean reduction of the import bill; what it means is that as industrialisation is proceeding domestic incomes are able to rise faster than foreign exports and imports. In East Africa today, it would be wrong to write off the future importance of primary products exports to the developed countries. A great deal could still be obtained from extra effort in the production of the traditional exports, notably cotton, sisal[36] and tea. But in the long run the case for industrialisation is unassailable, for it is here that East Africa can expect to find linkages in the economic system which would lead to greater growth rates, solve the problem of unemployment, and disconnect the direct link between her monetary incomes and the level of world prices for her primary exports.

To conclude this chapter we need to emphasise that the full benefits from the East African common market have yet to be realised. This is not to minimise the past achievement. But these benefits could have been greater for all three countries if there had been greater economic coordination in development policies. So far there has been little intercountry specialisation, but after labour has become more skilled and *scarce*, there should be tremendous scope for specialisation, and also greater economies of scale.

[36]Since writing this, however, the prices offered for sisal have fallen steadily, and there seem to be no prospects for sustained higher prices.

CHAPTER VII

EAST AFRICAN TRADE WITH THE NEIGHBOURS

The countries referred to collectively as the "Neighbours" in this study were listed in Chapter III. A complete discussion of East African trade with these countries would have to discuss visible exports, visible imports, re-exports and invisible trade. It has been found impossible to quantify invisible trade, but it must be exceedingly small, even though some of the Congo's, Rwanda's and Burundi's exports and imports pass through East Africa. Our main emphasis will be laid on East African domestic exports to these countries, since for the purposes of economic development it is domestic exports which embody the resources of East Africa. In the case of re-exports East Africa simply passes on to the Neighbours what has been produced by other countries, and gets the "trader's margin". It is difficult to imagine these margins being as important a source of income to East Africa as her domestic exports. However, re-exports to the Neighbours do give an indication as to the sorts of goods which, if produced in East Africa, she could sell to them. As far as imports from the Neighbours are concerned they are very small in value and volume; but they are perhaps the sorts of goods which the Neighbours could sell in increasing quantities if trade between them and East Africa was increased. Again in the discussion we shall concentrate on the last few years.

Re-exports to the Neighbours

The total re-exports of East Africa to the whole world would have shown an upward trend in recent years, except in 1963. Re-exports to the world and to the Neighbours in the last five years are shown in Table VII.1.

TABLE VII.1

East African Re-Exports, by Country, 1959-63
(£ *Thousand*)

A=total re-exports to the world
B=re-exports to the Neighbours

KENYA

	1959	1960	1961	1962	1963
A	5,079	5,006	6,418	7,235	7,147
B	777	865	1,999	1,665	2,211
B % A	15.3	17.3	31.1	23.0	30.9

	1959	1960	1961	1962	1963
UGANDA					
A	1,137	1,338	2,062	3,317	3,023
B	890	961	1,765	2,586	2,472
B % A	78.3	71.8	85.6	78.0	81.8
TANGANYIKA					
A	1,931	1,747	1,951	2,334	1,585
B	1,412	1,297	1,340	1,562	1,147
B % A	73.1	74.3	68.7	66.9	72.4
EAST AFRICA					
A	8,146	8,091	10,430	12,885	11,755
B	3,078	3,122	5,103	5,813	5,830
B % A	37.8	38.6	48.9	45.1	49.6

Source: *Annual Trade Reports.*

One thing which stands out in Table VII.1 is that Kenya's total re-exports are a good deal greater than those of Uganda and Tanganyika. In percentage terms, Kenya's share in total East African re-exports in 1963 was 61 per cent, Tanganyika's 13 per cent, and Uganda's 26 per cent. There are two main explanations: (i) Kenya, with a fine modern harbour at Mombasa, re-exports substantial amounts of foreign imported goods through the foreign ships which call at the port. For instance in 1962, when re-exports reached an all-time record, Kenya's re-exports of ships-stores were £2.2 million, whereas those of Uganda and Tanganyika were £.5 million and £.2 million respectively. (ii) Kenya imports more from abroad (again more than Uganda and Tanganyika combined) and has therefore more to re-export to the world—and as we saw in Chapter II to the rest of East Africa as well. But it will be noticed that Uganda's share in these re-exports has about doubled in the last five years. This rapid increase has been due to disturbances in Congo, Rwanda and Burundi, which have made distributors there unwilling to take the risk of carrying large stocks, and also because of the extension of the railway from Kampala to Kasese which has made transport between Uganda and the western Neighbours much better. There has also been some considerable improvement in roads to Uganda's western border.

Another thing we notice from Table VII.1 is that although Kenya's total re-exports are the largest, her re-exports to the Neighbours are smaller than those of Uganda, and until 1961 smaller than those of Tanganyika. In the peak year 1962 Kenya's percentage share of re-exports to the Neighbours was 29 per cent, and those

of Uganda and Tanganyika 44 per cent and 27 per cent respectively. This phenomenon is to be explained by the fact that the best customers for re-exports to the Neighbours are Congo, Rwanda and Burundi—countries which are physically closer to Uganda and Tanganyika with whom they have common boundaries. Moreover, the most prominent items in re-exports are petroleum products, and the biggest markets for petroleum re-exports are Congo, Rwanda and Burundi.

A complete percentage breakdown of the commodity composition of East African re-exports to the Neighbours is shown in Table VII.2.

TABLE VII.2

Commodity Composition of Re-exports to the Neighbours, 1960-63
(*percentage*)

SITC	1960	1961	1962	1963
0. Food	2.3	6.2	5.1	12.8
1. Bev. & Tob.	.5	.9	1.6	.6
2. Crude materials	3.3	3.3	1.5	1.2
3. Fuels	61.2	40.8	45.4	41.6
4. Oils & fats	.3	2.6	.4	—
5. Chemicals	2.1	3.4	1.7	2.8
6. Mfd. Prod.	11.3	21.5	23.5	18.5
7. Machinery	13.4	16.6	12.5	16.9
8. Misc. Mfd.	5.6	4.5	8.3	5.5
9. Other	.1	.3	.1	—

Source: *Annual Trade Reports.*

Looking at this table it will be noticed that re-exports to the Neighbours are concentrated in SITC sections 3, 6, 7, and 8; thus in 1963 these four sections accounted for 82.5 per cent of the total. However, there are great differences in commodity composition of re-exports of each East African country to the Neighbours. In both Uganda and Tanganyika SITC section 3 (petroleum products) dominates the picture; in 1963 in Uganda and Tanganyika petroleum products accounted for 44.0 per cent and 79.3 per cent respectively. Kenya's re-exports to the neighbours, although small, are much more diversified.

Also significant is the point that Kenya's re-exports are distributed widely among the Neighbours whereas those of Uganda and Tanganyika are mainly absorbed by Congo, Rwanda, and Burundi. In 1963 Kenya's re-exports to the Congo, Rwanda and Burundi combined were 10.2 per cent of the total, while the corresponding

shares in the case of Uganda and Tanganyika were 97.1 per cent and 74.8 per cent respectively. Countries of destination for each East African country's re-exports to the Neighbours are shown in Table VII.3.

TABLE VII.3

Origin and Destination of Re-exports to the Neighbours, 1963:
(£ Thousand)

To	*From*			
	Kenya	*Uganda*	*Tanganyika*	*East Africa*
Zanzibar	260	1	118	379
Somalia	509	1	27	537
Ethiopia	73	—	1	74
Sudan	706	59	—	765
Congo (Leo.)	158	1,912	286	2,356
Rhodesia and Nyasaland ..	98	2	130	230
Mozambique	26	7	6	39
Rwanda	11	390	2	403
Burundi	58	100	571	729
Madagascar	94	—	2	96
Mauritius	91	—	1	92
Seychelles	123	—	2	125
Reunion	4	—	—	4
Total	2,211	2,472	1,146	5,829

Source: *Annual Trade Report*, 1963.

A most important observation is that the Neighbours are important markets for the re-export of manufactured goods. This is indicated in Table VII.4.

TABLE VII.4

Re-exports of Manufactured Goods, to the World and to the Neighbours, 1960-63
(£ thousand and percentage)

SITC		1960	1961	1962	1963
5. Chemicals:	All re-exports ..	155	222	175	213
	% to Neighbours ..	42	69	78	79
6. Mfd. Prod.:	All re-exports.. ..	730	1,483	1,769	1,271
	% to Neighbours ..	48	71	77	85
7. Machinery:	All re-exports ..	1,995	2,566	3,655	3,423
	% to Neighbours ..	21	32	20	29
8. Misc. mfd.:	All re-exports.. ..	315	498	602	392
	% to Neighbours ..	56	44	80	81

It will be noticed that the Neighbours take substantial proportions of East African re-exports of manufactured goods, and that in recent years the Neighbours' share has been increasing. The significance of this is that potentially East Africa could meet the Neighbours' demand for these goods with her own products—a sort of import

substitution. This substitution would be facilitated by the fact that trade in re-exports has already established trading relations with these countries, besides indicating the sorts of goods which the Neighbours demand. Among these re-exports there are many which East Africa produces already, e.g. clothing, footwear, glassware, matches, household utensils, textile products. The value of such articles in re-exports to the Neighbours might appear small taken individually, but in 1962 they were worth well over £2.3 million.

Moreover, East Africa should also consider replacing food re-exports to the Neighbours with her own products. In food re-exports, the prominent items are sugar, tea, meat and meat preparations, cheese, curd and cereals; most of these go to Sudan. These are items which East Africa actually produces and although it may be that East Africa can get better prices for them in other countries, the aim should be to produce more, replacing re-exports with domestic exports while at the same time maintaining supply to other markets.[1] Most of these food re-exports are manufactured foodstuffs.

In concluding this discussion on re-exports it is worth repeating the two most important observations: (*a*) that re-exports are not as important to the development of East Africa as domestic exports; and (*b*) that present re-export trade does give a rough guide to the sorts of goods which East African countries could produce and hope to sell to the Neighbours.

Domestic Exports to the Neighbours

The trade between East Africa and her Neighbours is very small, not only in comparison with trade between East Africa and other foreign countries, but also in comparison with East African inter-country trade; it is even less than re-exports to the Neighbours. This is clearly brought out in Table VII.5. which shows East African total domestic exports to the Neighbours, to India, to other under-

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1. It has been argued, for instance, that Kenya meat fetches such good prices in Europe that it would be ridiculous to try to sell these products instead to the Neighbours. But it is to be doubted that this could be true for all these commodities; what needs to be done is to establish trading relations with the Neighbours and carry out market surveys. Even if sales prices had to be lower, there is no full employment in these industries, and in most of them production could be increased several times.

TABLE VII.5

East African Exports to Various Markets, 1963
(£)

A=Exports to rest of East Africa
B=Exports to the Neighbours
C=Exports to India
D=Exports to other *underdeveloped* countries
E=Exports to *developed* countries

	Kenya	*Uganda*	*Tanganyika*	*East Africa*
A	19,790,819	8,241,276	3,422,678	31,454,773
B	2,587,058	1,874,880	1,087,529	5,549,467
C	996,487	2,574,492	2,685,580	6,226,559
D	3,116,335	8,794,381	10,420,501	22,331,217
E	37,132,005	38,230,931	49,359,764	124,752,700
Total Domestic Exports: (B+C+D+E)	43,831,885	51,474,684	63,553,374	158,859,943
Re-exports	7,146,684	3,023,052	1,585,367	11,755,103

developed countries, and to the developed countries, as well as intercountry exports, for the year 1963.

East Africa's limited trade with the Neighbours is a widespread phenomenon among underdeveloped countries. In fact trade among all underdeveloped countries is estimated to be only 10 per cent of their total world trade. In Africa too intra-trade forms about one-tenth of the continent's total world trade. About half is between the Republic of South Africa and the former Federation of Rhodesia and Nyasaland. Leaving out South Africa, African intra-trade is only about 5 per cent of total African trade.[2] On the other hand, this figure leaves out trade within existing customs unions and if this trade were included then intra-African trade (excluding South Africa) would form a higher proportion—perhaps something like 8 per cent. Moreover, leaving out both South Africa and trade within customs unions, most of intra-African trade is confined among the French-speaking North African countries, and between these countries and the French-speaking West African countries. There is also some trade between United Arab Republic and Sudan.[3]

But what is of even greater interest is that the volume of East African trade with the Neighbours is so much smaller than the volume of East African intercountry trade, as is shown in Table VII.6 below. In 1963 East African imports from the Neigh-

2. See Economic Commission for Africa, *Proposals for the Establishment of an African Payments Union*, E/CN.14/STC/APU/7, June, 1964, page 5.

3. For data on the flow of intra-African imports and exports, see E.C.A., *op. cit.*, Annex III.

TABLE VII.6

East African Trade with the Neighbours: Domestic Exports, Imports and Re-exports, 1959-63

(£ *Thousand*)

	Exports	*Imports*	*Re-exports*	*Intercountry Exports*
1959	4,022	960	3,078	20,098
1960	4,800	1,734	3,123	22,790
1961	4,525	3,608	5,103	25,037
1962	4,931	2,062	5,813	26,764
1963	5,549	2,088	5,830	31,455

Source: *Annual Trade Reports.*

bours were only 6.6 per cent of intercountry imports. Moreover, while East African domestic exports to the Neighbours have been hesitantly increasing over the last five years, intercountry exports have been increasing rapidly and steadily—by £11.4 million between 1959 and 1963 compared with £1.5 million for exports to the Neighbours.

In the case of East African imports from the Neighbours there have been wide fluctuations in value in the last five years. The record figure of £3.6 million in 1961 was due to the fact that in that year East Africa suffered disastrously from adverse weather conditions; food imports, especially maize from the Rhodesias, were increased, but when normal conditions returned they were reduced. This illustrates an important point: namely, that imports from the Neighbours are marginal imports.

The small volume of trade between East Africa and the Neighbours is not to be attributed to lack of purchasing power, for these countries' total imports from the world are substantial; those of Rhodesia and Nyasaland were over £140 million in 1962, while those of Congo and Sudan were £76 million and £92 million respectively.[4]

4. Total 1962 imports of the following countries among the Neighbours were:

	£ *Million*
Rhodesia and Nyasaland	143.0
Congo	76.3
Sudan	91.8
Mozambique	48.6
Ethiopia	36.8
Madagascar	43.6
Mauritius	23.7
Reunion	22.6

Source: UN, *Monthly Bulletin of Statistics*, Dec. 1963. If we add the imports of the other Neighbours not listed above, the total imports of the Neighbours were well over £500 million, and of these about £200 million would be consumer goods.

There are several explanations for this limited trade. Firstly, climate and geological similarities make East Africa and the Neighbours competitive rather than complementary—competitive in the sense that production for export is concentrated on similar primary products to be sold to the developed countries.

Secondly, means of transport and communications between these countries are very poor. As we have already mentioned, there are no rail links between East Africa and the Neighbours while road connections are hazardous and often unusable during the rainy seasons. For instance, goods shipped from central Kenya to central Ethiopia would have to go down to Mombasa by rail, through the Indian Ocean, and then again by railway from Djibouti to Addis Ababa—the latter distance being about as long as that from Nairobi to the Ethiopian capital. This inadequacy of transport facilities is enhanced by the fact that southern Sudan, southern Ethiopia, and western Somalia, and also northern Kenya and northern Uganda, are the poorest areas of these countries. Moreover, this phenomenon makes potential improvement in transport facilities between these countries expensive; roads will have to go through areas of relatively small economic potential before they reach the relatively rich areas which can be expected to benefit from improved communications.

Thirdly, different fiscal and monetary systems have inhibited the growth of this trade. This difficulty has been enhanced in recent years by currency instability in Congo, Rwanda and Burundi. Moreover, border conflicts and social upheavals in Congo, Rwanda, Burundi, Sudan and Somalia have also severely disrupted East African trade with these countries.[5]

Fourthly, some countries in East Africa and among the Neighbours which might have increased their exports to the neighbouring countries have not seriously attempted to do so because they have had better markets elsewhere. For example, the former Federation of Rhodesia and Nyasaland, especially Southern Rhodesia, directed its exports to the rapidly industrialising and developing

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5. The outbreak of hostilities in the Congo, ironically enough, led to greater East Africa domestic exports, mainly of foodstuffs. These hostilities have also been responsible for the fast increase in the volume of East African re-exports, mainly from Uganda, going to Congo.

South African Republic.[6] In the case of Southern Rhodesia she also found an expanding market in Northern Rhodesia and Nyasaland for her manufactured goods and foodstuffs. The same thing has happened in East Africa; here Kenya has found a more or less ready and expanding market in the East African Common Market.

Fifthly, some of the Neighbours have been under different colonial masters and their commercial policies were directed and controlled by their metropolitan power. This helps to explain why the United Kingdom's share in East African imports has been so high, and also why some of the Neighbours trade almost exclusively with France and Belgium. This point, incidentally, also helps to explain why the Neighbours and the East African countries have remained basically primary producers, with little share of public expenditure going into deliberate development of manufacturing sectors; for the metropolitan powers were really interested in creating complementary economies in their colonies.

Sixthly, one of the most important explanations is that there has been no economic cooperation between East Africa and the Neighbours. This explains why while East African intercountry trade has been flourishing and expanding rapidly since the early 1950s, East African trade with the Neighbours has been increasing only slowly and hesitantly. This is an important point, and we shall take it up later when discussing policy recommendations.

Characteristics of Domestic Exports to the Neighbours

So far we have been discussing only the absolute size of the East African trade with the Neighbours. We shall now examine each East African country's share in these exports, the direction of these exports by country, and the commodity composition of exports to the Neighbours. To do this we need a number of tables. In Table VII.7 we show each East African country's value and share of total East African domestic exports to the Neighbours for the period 1959 to 1963; in Table VII. 8, exports to the Neighbours by country

6. It should also be mentioned that the former Federation had, until recently, a preferential tariff agreement with South Africa. The termination of this agreement has, no doubt, contributed generously to the fall of South African exports to the former Federation—a fall of over £10 million between 1960 and 1962.

TABLE VII.7

Country Shares in Domestic Exports to the Neighbours, 1959-63
(*£ thousand and percentage*)

	1959		1960		1961		1962		1963	
	Value	%	*Value*	%	*Value*	%	*Value*	%	*Value*	%
Kenya	1,611	40.1	1,957	40.8	1,994	44.1	2,369	48.0	2,587	46.6
Uganda	1,271	31.6	1,577	32.8	1,390	30.7	1,452	29.4	1,875	33.8
Tanganyika ..	1,140	28.3	1,267	26.4	1,142	25.2	1,111	22.5	1,088	19.6
Total	4,022		4,800		4,525		4,931		5,550	

Source: *Annual Trade Reports*

TABLE VII.8

Origin and Destination of East African Exports to the Neighbours, 1963
(*£ Thousand*)

To	*From* Kenya	Uganda	Tanganyika	East Africa
Zanzibar	420	120	445	985
Somalia	417	209	18	644
Ethiopia	140	—	7	147
Sudan	243	1,357	128	1,728
Congo	273	119	65	457
Rwanda	107	19	14	140
Burundi	152	4	134	290
Rhodesia and Nyasaland	231	38	181	450
Mozambique	85	1	48	134
Madagascar	34	—	9	43
Mauritius	352	7	37	396
Seychelles	51	1	1	53
Reunion	81	1	1	83
	2,586	1,876	1,088	5,550

Source: *Annual Trade Report*

of origin and destination for 1963; and in Table VII.9, the commodity composition of exports to the Neighbours from each East African country, again for 1963.

Looking at Table VII.7 first, we see that Kenya exported almost half (46.6 per cent) of total East African domestic exports to the Neighbours in 1963, and the corresponding shares for Uganda and Tanganyika were 33.8 per cent and 19.6 per cent respectively. The relative importance of each East African country in these exports is thus like that of intercountry exports, Kenya exporting the most and Tanganyika the least, although in the exports to the Neighbours the differences are not as pronounced as in intercountry exports. It will also be noticed that the trends of the three countries' exports to the Neighbours have been different: Kenya has been increasing her percentage share, while Uganda's share has been fluctuating around 32 per cent, and Tanganyika's share has been declining constantly.

From Table VII.8 it will be noticed that the largest markets among the Neighbours for East African exports are Sudan, Zanzibar, Somalia, Congo, and Rhodesia and Nyasaland. These countries took 31.1 per cent, 17.7 per cent, 11.6 per cent, 8.2 per cent and 8.1 per cent respectively of the exports from East Africa to the Neighbours in 1963. The reason why Sudan is so important will be explained below when discussing the commodity composition of

TABLE VII.9

Commodity Composition of Domestic Exports to the Neighbours, 1963

(£ and percentage)

SITC	Kenya Value	Kenya %	Uganda Value	Uganda %	Tanganyika Value	Tanganyika %	East Africa Value	East Africa %
0	1,305,948	50.5	1,640,438	87.5	528,295	48.6	3,474,681	62.6
1	10,596	.4	2,666	.1	38,329	3.5	51,591	.9
2	155,761	6.0	55,732	3.0	420,608	38.7	632,101	11.4
3	5,217	.2	—	—	—	—	5,217	.1
4	8,871	.3	87,536	4.7	8,368	.8	104,775	1.9
5	157,458	6.1	3,415	.2	32,783	3.0	193,656	3.5
6	714,939	27.6	75,655	4.0	38,632	3.6	829,226	14.9
7	47,086	1.8	73	—	3,880	.4	51,039	.9
8	170,759	6.6	9,365	.5	16,486	1.5	196,610	3.6
9	10,423	.4	—	—	148	.1	10,571	.2
Total	2,587,058		1,874,880		1,087,529		5,549,467	

Source: *Annual Trade Report*, 1963.

TABLE VII.10

Imports from the Neighbours, by Country, 1959-63

(£ thousand and percentage)

	1959 Value	1959 %	1960 Value	1960 %	1961 Value	1961 %	1962 Value	1962 %	1963 Value	1963 %
Kenya	585	61	1,032	60	2,360	65	1,213	59	1,410	68
Uganda	262	27	559	32	365	10	227	11	364	17
Tanganyika ..	113	12	143	8	882	25	622	30	314	15
Total	960		1,734		3,608		2,062		2,088	

Source: *Annual Trade Reports*

these exports. The importance of Zanzibar is to be explained mainly by her nearness to East Africa. Also Zanzibar is a small island which depends on the mainland countries for some of her food and other commodities like timber. But Zanzibar has not been a member of the East African common market, and her trade with the three mainland East African countries forms only a very small proportion of her total trade—less than 7 per cent.

The commodity composition of East African exports to the Neighbours, broken into SITC sections for the year 1963, is shown in Table VII.9. It will be noticed that food plays a most important part in the exports of each East African country to the Neighbours, much greater than food exports play in the intercountry exports of each country. For the whole of East Africa food exports were 62.6 per cent of the total value of exports to the Neighbours in 1963, compared with 28.3 per cent in the case of intercountry exports. The importance of exports to the Neighbours is especially considerable in the case of Uganda. The importance of this SITC section is to be explained, in the main part, by coffee exports to Sudan, the bulk of which come from Uganda.

The dominating role of food exports implies the relative unimportance of exports of manufactured goods to the Neighbours, especially when compared with intercountry trade, or even with East African re-exports to these same countries. In 1963 SITC sections 5, 6, 7, and 8 contributed 22.9 per cent of East African domestic exports to the Neighbours; while in intercountry trade they contributed 48.4 per cent, and in re-exports 43.7 per cent. As would be expected, the main source of manufactured exports is Kenya. The contrast between the role of manufactured goods in exports to the Neighbours and in intercountry trade is principally due to the protection which local producers of manufactured goods enjoy in the East African common market. There is little doubt that if there were preferential tariff arrangements between East Africa and the Neighbours, trade in manufactured products among all these countries would increase, and thus promote industrialisation.

Tables VII.10, VII.11, and VII.12 bring out some of the main characteristics of East Africa's imports from the Neighbours, comparable to those we have just examined on the export side. The small size of these imports and the fact that they are marginal in total East African imports from foreign countries have already

TABLE VII.11

Origin and Destination of East African Imports from the Neighbours, 1963
(£ *Thousand*)

From	*Kenya*	*Uganda*	*To* *Tanganyika*	*East Africa*
Zanzibar	100	—	58	158
Somalia	12	—	—	12
Ethiopia	88	—	6	94
Sudan	1	3	—	4
Congo	470	59	40	569
Rwanda	—	59	1	60
Burundi	—	—	27	27
Rhodesia and Nyasaland	442	184	177	803
Mozambique	192	59	1	252
Madagascar	95	—	—	95
Mauritius	5	—	1	6
Seychelles	5	—	2	7
Reunion	—	—	—	—
Total	1,410	364	314	2,088

Source: *Annual Trade Report*, 1963.

TABLE VII.12

Commodity Composition of East African Imports from the Neighbours, 1963
(£ *and percentage*)

SITC	*Kenya*	*Uganda*	*Tanga-nyika*	*East Africa*	%
0. Food	743,545	186,006	47,724	977,275	46.8
1. Bev. & Tob.	1,958	2	441	2,401	—
2. Crude materials ..	94,750	86,215	51,542	232,507	11.1
3. Fuels	—	—	—	—	—
4. Oils & fats	248,859	26,040	33,223	308,122	14.8
5. Chemicals	31,155	2,151	3,912	37,218	1.8
6. Mfd. Prod.	134,887	15,231	59,461	209,579	10.0
7. Machinery	88,648	39,213	105,180	233,041	11.2
8. Misc. Mfd.	65,608	9,021	11,987	86,616	4.1
9. Other	844	28	443	1,315	—
Total	1,410,254	363,907	313,913	2,088,074	

Source: *Annual Trade Report*, 1963.

been mentioned. Here we shall be concerned with the shares of the three East African countries in these imports, their sources among the Neighbours, and their commodity composition.

As far as the country shares in Table VII.10 are concerned, Kenya is the main market, and the only apparent trend is that her percentage share in total imports has tended to increase over the last five years. The main reason for this tendency will be discussed while analysing the commodity composition of these imports.

It will be seen in Table VII.11 that the main sources of imports from the Neighbours are Rhodesia and Nyasaland and Congo—these two combined had a share of 65.8 per cent in 1963. Mozambique and Zanzibar also had significant shares. The relative importance of Rhodesia and Nyasaland is easily explained—for Southern Rhodesia is the most developed of the Neighbours and consequently has a whole range of manufactured or semi-manufactured products and food which she exports both to East Africa and the other Neighbours. In the case of Congo, however, the relative importance is due almost entirely to tea and palm-oil. Similarly it is tea imports from Mozambique, and imports of coconut (copra) oil, from Zanzibar and almost all to Kenya, which make them important as import sources among the Neighbours.

One interesting observation from Table VII.12 is that the proportion of manufactured goods in East African imports from the Neighbours is moderately greater than in East African domestic exports to the Neighbours. In 1963 SITC sections 5, 6, 7, and 8 were 27.1 per cent of imports from the Neighbours and 22.9 per cent of exports. In value terms however, East African exports of manufactured goods to the Neighbours are about double her imports. The main source of these imports of manufactured goods is Rhodesia and Nyasaland, contributing 91.4 per cent in 1963. Rhodesia and Nyasaland has developed quite a bit of engineering industry and exports a whole range of simple pieces of machinery to East Africa. Some items of exports in SITC section 7 from Rhodesia and Nyasaland to East Africa are listed in Table VII.13. Most of these imports of machinery from Rhodesia and Nyasaland are agricultural machinery, appliances and parts, such as ploughs, harrows, drillers, mowers, etc; but there are also some fairly sophisticated goods such as mining and construction equipment and wireless sets. The importance of machinery imports from Rhodesia and Nyasaland illustrates a point made in a previous chapter: namely, that although the developing countries will continue to depend on the developed nations for their needs of machinery and transport equipment for a long time, because the production of these goods demands heavy capital investment and skills, there is no reason why import substitution should not take place in these countries' needs for simple pieces of machinery, especially agricultural machinery.

TABLE VII.13

Selected East African Imports of Machinery and Transport Equipment from Rhodesia and Nyasaland, 1963
(£)

Item	*Value*
Ploughs, harrows, cultivators, drillers, etc.	111,021
Parts thereof	26,344
Binders, reapers, mowers, threshers	2,933
Agricultural machinery and appliances n.e.s.	960
Machine tools for working metals	394
Pumps for liquids	1,892
Machines for conveying, excavating, etc.	58,772
Wood-working machinery	33
Sewing machines, parts	357
Meal and flour making machinery	61
Machinery and appliances, other non-electric	3,509
Ball, needle, or roller bearings and parts	127
Machine parts and accessories, non-electric	75
Electric generators, alternators, etc.	230
Wireless sets (domestic) including radiograms	14,963
Other, including spare parts	246
Electrothermic apparatus, appliances, etc.	97
Electrical appliances for motor-vehicles, bicycles, etc.	32
Motor vehicle batteries	344
Other electric machinery, apparatus, appliances	623
Bodies, chassis, frames, etc. of road vehicles	547
Road vehicles (complete) including trailers	2,668
Parts thereof	171
All other machinery & transport equipment	5,912
Total	232,311

Source: *Annual Trade Reports*, 1963.

In conclusion we may note that at present East African trade with the Neighbours is predominantly in one direction—East Africa exports relatively a lot to the Neighbours while buying little from them. If in future greater economic cooperation is pursued, both of these flows may be expected to expand dramatically, and the balance to become relatively smaller.

CHAPTER VIII

CONCLUSIONS AND POLICY RECOMMENDATIONS

The Common Market

In this study we have examined the important contribution of intercountry trade among the three East African countries to their economic development. We have also seen that the benefits accruing from the common market have not been equally shared—Kenya has gained substantially, Uganda has certainly gained although not by as much as Kenya, while Tanganyika has probably lost and certainly has gained the least. These unequal benefits derive from unequal growth rates in the manufacturing sectors of the three countries, with the result that tensions and strains have developed in the operation of the common market. It is important to notice, however, that in the present conflict among the three countries it is generally agreed that the common market *is effective* in promoting development and industrialisation; the conflict arises from unequal distribution of the benefits accruing from it. As the ultimate solution to present tensions in the common market, it was pointed out that what Uganda and (especially) Tanganyika want is not financial compensation, as was recommended by the Raisman Commission, but a *share in the industrialisation* process facilitated by the existence of the common market.

In order to correct the unequal distribution of industrial activity in East Africa (in absence of full political union and without breaking up the common market altogether), there are two courses of action open: (*a*) dilution of the common market; and (*b*) closer economic integration. Let us start with the first alternative. Because of the existence of the common market each East African country is now unable to use in full the various instruments for an industrialisation programme usually available to a single country. Such instruments include company taxation, monetary policy, and tariffs. These are now uniform in East Africa; and it is likely that (say) Tanganyika would initially benefit by pursuing policies more suitable to her present position vis-a-vis the other two countries. For instance, if she had a lower rate of company taxation than Kenya it is likely that she could attract some of the industries now favouring Kenya because of external economies available there.[1]

1. This point, however, is not to be given too great importance—for what really matters is that a firm be able to make profits. Low rates of taxation are important only where they increase the profits which an entrepreneur can get, and it may be that modestly lower rates of taxation would not be sufficient, if pre-tax profits are much higher in Kenya.

It is also possible that Tanganyika would benefit, initially at any rate, if she restricted imports from the rest of East Africa, i.e. if she pursued a policy of substituting her own products for goods from the rest of East Africa.

Restriction of intercountry imports of certain products was actually approved by the three countries in the Kampala Agreement. It was agreed that in order to hasten the removal of imbalance in intercountry trade, a country with a substantial trade deficit with the rest of East Africa, and which wanted to produce domestically some goods it is currently importing, could apply quota restrictions against such imports. Tanganyika has accordingly introduced quota restrictions on a whole range of imports from Kenya and Uganda. Several observations on this quota system are in order. Firstly, the system would benefit East Africa as a whole only if, in those cases in which quotas are applied, the country instituting them has immediate and adequate capacity to produce the goods in question. If quota restrictions exceeded this capacity and imports from the rest of East Africa were replaced by foreign imports, the common market would be in great danger of completely breaking up. Secondly such quotas should be made *temporary*. One of the benefits accruing from the common market, and potentially of considerable importance, is that through competition efficiency and increases in productivity are encouraged; but if quotas were permanent they would insulate inefficient industries against such stimulus. Moreover, although some industries could be operated in each country's domestic market, it is likely that additional benefits for East Africa as a whole could be secured if there was country specialisation even in some of these industries. Thirdly, it would be wrong to suppose that having each country's intercountry trade in *complete balance* would benefit the area as a whole or even the country in question in the long run. Even in a single country it is impossible to have simultaneously equal growth rates in all its regions and sectors; there will always be some areas and industries growing faster than the rest. Therefore the word *balance* needs very careful definition—complete balance at present may only be achieved by impoverishing some of the members, and it is questionable whether this would be to any country's long-run interests. Fourthly, a real danger in quotas is that their introduction in one country is likely to be closely followed by restrictive action in the rest of East

Africa, unless these quotas are instituted only after complete agreement and within a strong framework of economic cooperation.

We thus come to the conclusion that although there might appear to be some initial benefits from dilution of the common market, there are great dangers inherent in such a course of action. Paradoxically, the present strains and tensions in the common market indicate that for the sake of each country *and* East Africa as a whole there is urgent need to increase the degree of economic integration. Coordinated economic policies would permit planned intervention to be introduced in favour of those areas lagging behind.

Closer economic integration could be secured even without political union, although the latter is in many ways the ideal for the area as a whole. Closer economic integration would make it possible to use various instruments for fostering industrialisation generally, as well as specifically the lagging areas. In a programme of stepping up balanced industrialisation in East Africa as a whole the following instruments, working with varying degrees of effectiveness, can be used: promotion and persuasion; offering facilities and services to potential investors; public enterprises; company taxation; protection; and licensing.[2] Professor Clark suggested that there should be set up an East African agency to administer the last three instruments, while national governments would administer the first three. One important feature of this proposal is that the agency should be able to use company taxation, protection, and licensing discriminately; i.e., favouring lagging areas would be possible.

There are numerous problems involved in deliberate distribution of industries with the aim of favouring certain areas. However, this policy has already been accepted by the three countries, and in the Kampala Agreement each country was allocated exclusive rights to establish certain industries. For such a policy to work properly there are certain points which should be kept in mind.

Firstly, it is important that if a certain industry is allocated to country A, this country should be able to operate it within a fairly short period of time at costs not too much higher than if the industry were established elsewhere. If costs and therefore prices in country

2. P. G. Clark, "Next Steps for Industrialisation in East Africa", Economic Development Research Project, Working Paper No. 12, E.A.I.S.R., Makerere University College.

A were much higher, there would be a great possibility of serious conflict arising since countries B and C would be paying "unnecessarily" high prices.

Secondly, in allocating industries it would be more meaningful to ignore political boundaries and think in terms of economic zones.[3] In particular, if what Tanganyika wants is to increase exports to Kenya, then industries aimed at achieving this goal are better established at, say, Arusha than in Dar es Salaam. This, however, would only improve the competitiveness of these industries, in relation to similar industries in Kenya, in the Kenya market and in northern Tanganyika; these industries' competitiveness in southern Tanganyika would not be as great if they had been established in Dar es Salaam. This problem is made more formidable by the fact that it is not conceivable for Tanganyika to be allocated an industry *simply in order to buy from her;* most industries will have to depend considerably on the domestic market as well as exports to the rest of East Africa.

Thirdly, it is important to keep in mind that attempts to direct industries to areas other than those initially preferred by foreign entrepreneurs are likely to appear, at this stage at any rate, premature and unwise to the entrepreneurs. For instance, if the Japanese want to set up a factory in Nairobi and then are told that this is not possible but that they could be allowed to put up the factory in, say, Jinja, they might decide not to invest at all. There are other countries which are also trying to attract foreign capital, and the East African countries have to compete with them. Indeed any strong measures aimed at directing foreign private capital to areas other than those of its initial choice are likely to reduce its inflow. This point applies with less force to internal private capital. It is only public capital which is easily directed.

These grave difficulties in deliberate distribution of industries in East Africa emphasise the need for closer integration. In particular, I would suggest that an East African Industrial Development Corporation, with power of taking part in industrial investment either singly or in partnership with private capital, is needed. Its purposes should be: (*a*) stimulating general industrial expansion in East Africa, and (*b*) within that framework introducing measures

3. Allocating industries on the basis of political boundaries is a second-best solution, although with careful planning and coordination the inferiority of this solution could be minimised.

to distribute industries among the three countries. Emphasis should be laid on the word *distribution;* not redistribution, for there are very few industries, if any, which can now be redistributed. In other words the policy adopted should be dynamic rather than static. The possibility of success if such a policy were adopted is great, for the scope of further import substitution on an East African basis is very large in relation to the amount of import substitution achieved so far.

The need for such a Corporation arises from the fact that other instruments of industrial distribution, such as differential company taxation and protection and licensing, are essentially passive, and might operate more slowly than is politically desirable. This is not to suggest that these instruments should not be used. In using them it should also be realised that licensing is inferior to both differential company taxation and protection. This is because these two latter instruments would, while directly increasing the possibility of profit, affect primarily those industries for which other locational considerations are comparatively unimportant. Licensing is essentially a restrictive instrument, and offers little inducement to invest. However, it is unlikely that these three instruments would by themselves work fast enough, especially now that the volume of industrial investment is at a very low level in all three East African countries. A more positive government *agency*, armed with additional powers of directly investing in areas where rates of return might be initially lower due to lack of externalities or high pioneering costs, seems needed. In fact some of the services now operated jointly by the three East African countries, notably the Railways and Harbours Administration, are already attempting to do this in their activities. An East African Industrial Development Corporation would make these attempts more successful.

It might be argued that trying to ensure an acceptable distribution of industries, essentially by covering the gaps of industrial unevenness among the three countries with public enterprises, might end with all public enterprises being located in one country. This need not be so, at any rate in the long run, provided that such a policy is used in conjunction with indirect instruments aimed at directing private capital to the lagging areas. In any case once an area has an established industry, even if public-owned, it becomes more attractive to private capital.

To recapitulate, the need for closer economic integration rests on three important conclusions from our study: (*a*) that closer economic integration would provide opportunities for raising the rate of economic development in East Africa as a whole; (*b*) that the present unequal distribution of benefits accruing from the common market can only be corrected within a framework of general industrial expansion; and (*c*) that potential benefits from continued existence of the common market are enormous compared with the benefits realised so far.

It would be a tragedy if, as a result of present tension, the common market were dismantled. This would hit each member country, although with varying degrees of impact, and it is likely that those countries which might initially gain from a break-up would lose more in the long run. In other words short-run gains from a break-up have to be weighed seriously against long-run benefits of continuation of the common market, especially if its operation were to be improved. Moreover, it is exceedingly unlikely that if the common market breaks up the Common Services Organisation would be left intact; individual country interests and policies would conflict frequently, with each country trying to use the common services to its own benefit. The administrative economies accruing from the joint operation of these common services are very substantial; and there is little doubt that dissolution of this partnership would hurt each country, with Kenya being affected the least.

Promotion of Trade with the Neighbours

In the discussion of East African trade with the Neighbours two important findings were: (*a*) that this trade has not been growing as fast as East African intercountry trade; (*b*) that in East African exports to the Neighbours manufactured goods are not only absolutely smaller but also form a smaller proportion than in intercountry exports. This difference in volume and commodity composition (as well as the difference in the rates of growth of intercountry trade compared with East African trade with the Neighbours) can be attributed to the existence of a common market in East Africa which has offered protection against outside suppliers. Moreover, the difference in commodity composition of East African exports to the two markets reaffirms that import substitution is the most immediately accessible route to industrialisation for countries at East Africa's level of development.

This study would therefore suggest that some preferential tariff arrangements with the Neighbours would not only lead to more trade between East Africa and these countries, but also provide stimulus and scope for more industrialisation through import substitution. To East African countries this seems especially attractive because the import market of the Neighbours is about four times as large as that of East Africa. But cooperation is needed because in East Africa and among the Neighbours there is not a single country, as yet, with sufficient domestic demand to support really large-scale industries (e.g. a modern iron and steel plant). This means that if each country were to follow a policy of thoroughgoing autarchy the plants to be established would either be small-scale and high-cost, or in chronic excess capacity.[4] If what is wanted is rapid industralisation, then it has to be appreciated that a formidable obstacle is the limited scale of the domestic markets. This limitation can be removed by economic cooperation between East Africa and the Neighbours.

Since political union of East Africa and the Neighbours is most unlikely, economic cooperation would take the form of preferential tariff arrangements. Here there is a great obstacle: namely, that preferential tariff arrangements are internationally accepted only in customs unions, common markets, and free trade areas. But any of these three arrangements is more comprehensive than is likely with the Neighbours—at any rate in the next few years. The East African experience should convince us that, whereas a full customs union is more or less certain to benefit the entire area covered by the union, it does not follow necessarily that each country in the union gains. Furthermore, in any attempt to bring about preferential tariff arrangements with the Neighbours, the East African countries should be careful not to reduce the possibilities of even closer economic integration among themselves; the full benefits from the East African common market have yet to be enjoyed.

The problem therefore resolves itself to this: what kinds of trade arrangements, short of a customs union, are possible between East Africa and the Neighbours? There are three main possibilities, although they are not mutually exclusive. First, an across-the-board

4. Actually it seems certain that some of these countries will establish fairly large-scale industries and hence economic cooperation is needed especially to avert excess capacity, with each country hoping to sell to the other.

percentage tariff preference could be used; e.g. Zambia's exports to East Africa would pay only 50 per cent of the duty levied on foreign imports, while she would do the same for East African goods. Second, East Africa and the Neighbours, or some of them, could agree simply to have free trade in certain goods or classes of products. Third, East Africa and some of the Neighbours could come to an agreement about the location of selected large-scale industries among themselves, using licensing to control competition, and then have free trade in the products of these industries.

The first and second methods have the great advantage of avoiding the conflicts inherent in the third method, which are likely to arise when negotiating about the allocation of industries. They also have the additional advantage of permitting competition and pressure towards efficiency. On the other hand, the third method has the tremendous advantage of economical use of scarce capital through avoidance of plant duplication. Moreover, successful allocation of industries would ensure that each country benefits from the cooperation and that economies of large-scale operation are obtained. The main disadvantage of the first method, which is really a partial customs union, is that inequality in the distribution of benefits accruing from the economic cooperation is quite possible. The second method is better in this respect; since only some commodities are affected by tariff preference, we can presume that in the process of negotiation each country will make sure that she has some industries which will benefit from the venture.

Although any of these three methods is better than no cooperation at all, it seems as if the second and third methods offer greater possibilities of mutual benefits for East Africa and some of her Neighbours. The second method could be applied to small-scale industries and food, while the third method should be used for large-scale industries.

Such an arrangement would make it possible to increase the rate of industrialisation while ensuring that each participant is getting a share of it. This could be a feasible goal because the scope of future import substitution for East Africa and the Neighbours together is much larger than for East Africa alone or any of the Neighbours. In a previous chapter we noted that for a limited list of goods which East Africa already produces, she still imported similar goods of the order of £33 million in 1963. The commodity

composition of the foreign imports of some of the Neighbours (Rhodesia and Nyasaland, Zanzibar, Sudan, Madagascar and Mauritius) is shown in Table VIII.1. Looking at these figures and

TABLE VIII.1
Imports of Selected Neighbours by S.I.T.C. Sections, 1961
(*£ thousand*)

	Rhodesia and Nyasaland[a]	*Madagascar*[b]	*Mauritius*[c]	*Zanzibar*[d]	*Sudan*[e]
0. Food	13,164	3,017	6,691	1,829	11,703
1. Bev. & tob. ..	1,141	2,159	634	271	1,077
2. Crude materials ..	4,958	578	612	755	1,682
3. Fuels	9,200	1,964	876	351	6,045
4. Oils & fats ..	946	527	771	72	232
5. Chemicals ..	13,450	3,329	2,705	210	6,372
6. Mfd. prod. ..	39,853	11,485	5,761	1,076	31,520
7. Machinery ..	51,825	8,916	4,100	804	27,316
8. Misc. mfd. ..	16,573	4,837	2,115	566	5,399
9. Other	3,896	101	52	384	50
TOTAL ..	155,006	36,913	24,317	6,318	91,396

Sources: (*a*) *Monthly Digest of Statistics*, Central Statistical Office, Salisbury.
(*b*) UN, *Yearbook of International Trade Statistics*, 1961.
(*c*) UN, *Yearbook of International Trade Statistics*, 1961.
(*d*) *Zanzibar Annual Trade Report*, 1961.
(*e*) *Foreign Trade Statistics*, Department of Statistics, Khartoum. These figures are for 1962, and have been calculated by taking £1 Sudanese to equal £1.0257 sterling.

the commodity composition of East African foreign imports, it would appear that the proportion of consumer goods in total imports of East Africa and the Neighbours has been about 30 per cent in the last four years. If we take this as a rough aggregative indicator of the goods which these countries can aim to produce locally, it would mean a potential market in the order of £200 million. This potential market is four or five times the corresponding figure for East Africa alone (if calculated similarly, rather than from a list of specific goods).

The general conclusion is therefore that there are great possibilities of mutual benefit in an arrangement which could facilitate more import substitution in East Africa and the Neighbours taken together. It is convenient to distinguish three categories of substitution: food products; small-scale industries, whose outputs are not by and large beyond the domestic market of each country; and large-scale enterprises, whose minimum scales of operation would continue to be beyond the likely demand of an individual country for many years. It is likely that most of these countries would be

able to replace food imports largely by local supplies, but given tariff preferences, the present small volume of trade in foodstuffs between East Africa and the Neighbours would certainly be raised. In the case of small-scale industries, several are already established in a number of the countries in question. However, preferential trade arrangements of the second method (preferences for certain classes of products) could stimulate them further, mainly by offering the possibility of larger scales through competitive efficiency and specialisation.

It is for the third category of import substitution, i.e. large-scale industries, that a combination of trade preferences and economic cooperation could produce the most substantial benefits to the whole area. A recent Economic Commission to East and Central Africa[5] recommended that the following industries could be established in the countries indicated.[6]

Steel and iron, an integrated plant	Southern Rhodesia
Steel and iron, a smaller plant ..	Uganda
Copper manufacture	Northern Rhodesia
Phosphatic fertilisers	S. Rhodesia and Uganda
Nitrogenous fertilisers	Northern Rhodesia
Potassium phosphate	Ethiopia
Coal distillation complex	Tanganyika
Sulphuric acid	S. Rhodesia and Uganda
Acetone, acetic & methane from wood	Kenya
Pulp and paper	Kenya, Ethiopia, and S. Rhodesia.

Examination of the feasibility or the relative advantages of locating these industries in the countries recommended needs more careful study. Moreover it is possible to extend the list to large-scale industries which could benefit from such cooperation. This is where the third type of preference system could be of great mutual benefit to East Africa and the Neighbours.

The forms of trade preference and economic cooperation which are discussed here would call for a network of agreements among

5. Sudan and Congo-Leopoldville are regarded by the E.C.A. as outside the East and Central Africa sub-region; that is why they are not allocated any industries in this recommendation.

6. See E/CN.14/247, *Report of the E.C.A. Industrial Co-ordination Commission to East and Central Africa*, 24 Dec. 1963.

the governments concerned. Such negotiations would have to deal with the existing international code of discipline in international trade. It is in the interest of most underdeveloped countries (and East Africa and the Neighbours fall solidly in this category) that there be general international acceptance of the principle of preferential tariff arrangements, with a wide range of possible terms, among underdeveloped countries pursuing cooperative development efforts. The argument that such devices would thwart the trend towards freer international trade is not actually valid, and in any case free trade is only mutually beneficial among equals. The Latin American countries have long recognised this and, under the cloak of the "frontier clause", they have attempted to increase trade among themselves.

One important point, however, is this: if such special trade arrangements among underdeveloped countries are internationally accepted, there should be no requirement that the tariff preference be automatically extended to all underdeveloped countries. The discussion makes the implicit assumption that the countries concerned are at a broadly similar stage of economic development. But all underdeveloped countries are not "equal" or at a similar stage of development; some are relatively industrialised while others are at their earliest stage. This becomes apparent if we examine East African trade with India—East Africa representing the countries at an early stage of development and India representing those

TABLE VIII.2

East African Trade with India, 1963

(£)

SITC		*Kenya*	*Uganda*	*Tanganyika*	*East Africa*
		A. Exports to India			
0	..	223,547	—	1,994,929	2,218,476
1	..	—	—	—	—
2	..	339,005	2,484,199	522,250	3,345,454
3	..	—	—	—	—
4	..	—	—	—	—
5	..	398,162[a]	—	168,081[b]	566,243
6	..	4,850[c]	90,293[d]	—	95,143
7	..	—	—	10	10
8	..	108	—	80	188
9	..	815	—	230	1,045
Total	..	966,487	2,574,492	2,685,580	6,226,559
		B. Imports from India			
0	..	304,871	35,629	50,366	390,866
1	..	5,445	336	297	6,078
2	..	44,701	3,658	12,398	60,757
3	..	69,646	—	—	69,646
4	..	4,589	137	2,298	7,024
5	..	89,300	36,518	35,217	161,035
6	..	3,082,405	733,178	1,874,837	5,690,420
7	..	84,618	19,668	38,913	143,199
8	..	291,026	17,557	58,613	367,196
9	..	—	600	—	600
Total	..	3,976,601	847,281	2,072,939	6,896,821

Notes: (*a*) Of this £326,476 was wattle bark extract, and the rest was sodium carbonate.
(*b*) All this was wattle bark extract.
(*c*) Almost all were pencil slats.
(*d*) All this was copper.

Source: *Annual Trade Report*, 1963.

underdeveloped countries which are relatively more industrialised. A number of Latin American republics would also fall in this latter category.

Table VIII.2 shows East African exports and imports to and from India for the year 1963, broken down into SITC sections. From these figures it will be seen that East African exports to India are predominantly foodstuffs and raw materials (SITC sections 0 and 2); in 1963 exports in these two sections were 89.4 per cent of the total. Even those exports in the manufactured sections were really simple manufactures—such as wattle bark extract, pencil slats, copper and sodium carbonate—as indicated in the table. On the other hand East African imports from India are predominantly manufactured goods; SITC sections 5, 6, 7, and 8 contributed 92.2 per cent of the total. The differences in the commodity composition of East African exports to India and her imports from that country indicate that although India is internationally classified as an underdeveloped country, yet she has a much larger and sophisticated manufacturing sector than East Africa. In fact in 1961 she exported more goods in SITC section 6 than she imported—£199.2 million compared with £156.7 million. In the same year she exported £3 million worth of machinery.[7]

These differences in stages of economic development indicate that the special tariff preferences like the ones being discussed in this study should not be automatically extended to all other underdeveloped countries. If they were, the more industrialised underdeveloped countries would export those goods, especially consumer goods, which the early-stage countries like East Africa and the Neighbours have to replace with local products if industrialisation is going to be achieved at all. In the case of East Africa and India,

7. See U.N., *Yearbook of International Trade Statistics*, 1961.

the problem is that the products which India now exports to East Africa are precisely those which East Africa has to protect in order to establish those industries herself. This is particularly true of textiles; East Africa is already protecting her local textile industries; although in 1963 she imported nearly £5 million of textile products (excluding carpets) from India.

However, India is such an important customer for East African exports,[8] especially for cotton, cashew nuts, and wattle bark and extract,[9] that a trade agreement between East Africa and India would be of mutual benefit. India's demand for raw materials is certain to grow as she industrialises further. An agreement with a more developed country such as India could be arranged on the following lines: that India gives tariff preference to *certain* East African primary products, while East Africa does the same for *certain* Indian capital goods and *certain* consumer goods of sophisticated technology. An agreement of this sort would have to be checked carefully for the capital goods given preference, to ensure that India could supply spare parts and servicing facilities.[10] Furthermore, such an agreement should be subject to change periodically as East Africa becomes able to establish a domestic industry replacing an Indian import. But a periodically amended agreement would in all probability continue to be mutually beneficial for a long time. Moreover, if it contributed to the production of cheap but reliable capital goods suitable for the conditions prevailing in underdeveloped countries, if could be a boon on an even broader scale.

Import Substitution and Internationally Agreed Trade Practices

We need, finally, to emphasise two general implications of this study: (*a*) the crucial importance of import substitution in the

8. Through 1962 India had been the chief customer for East African goods among the underdeveloped countries; in that year her imports were £9,312,766 But in 1963 Hong Kong jumped ahead and imported £6,952,700 of East African products, against India's reduced £6,226,559.

9. In 1963 East Africa exported to India £2.5 million of raw cotton, £2.2 million of cashew nuts, and £0.5 million of wattle bark and wattle bark extract. In 1962 these exports were even larger: raw cotton alone was more than £5 million, and cashew nuts nearly £2.5 million.

10. One of the general problems that developing countries face in their attempts to promote exports of manufactured goods is that they are not able to offer spare parts and servicing facilities on a large scale, as the industrial nations are doing.

development of underdeveloped countries; and (*b*) the need for flexibility in the code of discipline set down internationally to regulate international trade. Import substitution is simultaneously the most promising strategy for the development of underdeveloped countries, and the most difficult to achieve quickly—especially when tackled by each individual country alone. It is difficult because of such fundamental factors as the small size of individual domestic markets, shortage of financial capital, shortage of skilled labour, and limited experience with modern technology; and also because of availability of imports from foreign sources. This necessitates using protection in the industrialisation programmes of the developing countries. It is important also to emphasize export promotion—for this is the main scource of their foreign exchange. Therefore the problem is to so plan the deployment of domestic resources that greater export earnings, mainly through traditional exports, can be realised, while a vigorous policy of import substitution enables domestic production to grow more rapidly than exports and limits imports to the available foreign exchange.

As far as the international code of discipline in the field of international trade is concerned, the main regulations are those enforced by the General Agreement of Trade and Tariffs (GATT). Quantitative import controls are banned, although this requirement can be waived especially for underdeveloped countries who are at the earliest stages of development and in difficulties in their balance of payments. Secondly, there is the requirement for unconditional most-favoured-nation treatment, i.e., each contracting party will have to grant automatically to other contracting parties the tariff preferences it grants to any other country, whether or not the third country is a member of GATT. Thirdly, members have to limit their tariffs on certain products to an agreed level, which can only be modified after negotiations with other members concerned. Fourthly, subsidies in exports are prohibited.

It is to be seriously questioned whether some of these requirements, especially the second and third, are in the interests of underdeveloped countries seeking to industrialise. In particular the most-favoured-nation clause makes it impossible for these countries to have the kinds of tariff arrangements among themselves which are recommended in this study, although we have shown that underdeveloped countries, and certainly the Neighbours and East Africa,

stand to gain from such cooperative development. The third requirement, by limiting the use of increased tariffs, would remove the single most important weapon underdeveloped countries have in their struggle for industrialisation. What is required today is flexibility in the code of discipline in international trade, so that the developing nations can use devices like the ones discussed in this study to step up their rates of growth. Enforcing uniform standards is tantamount to saying that the problems of the developed nations and underdeveloped ones are identical. Fortunately, recent developments would indicate that the GATT policy towards underdeveloped countries is becoming increasingly permissive. It therefore seems likely that if East Africa and the Neighbours take the lead in advocating the type of flexibility in GATT regulations suggested here, there is some possibility of establishing the principle internationally.

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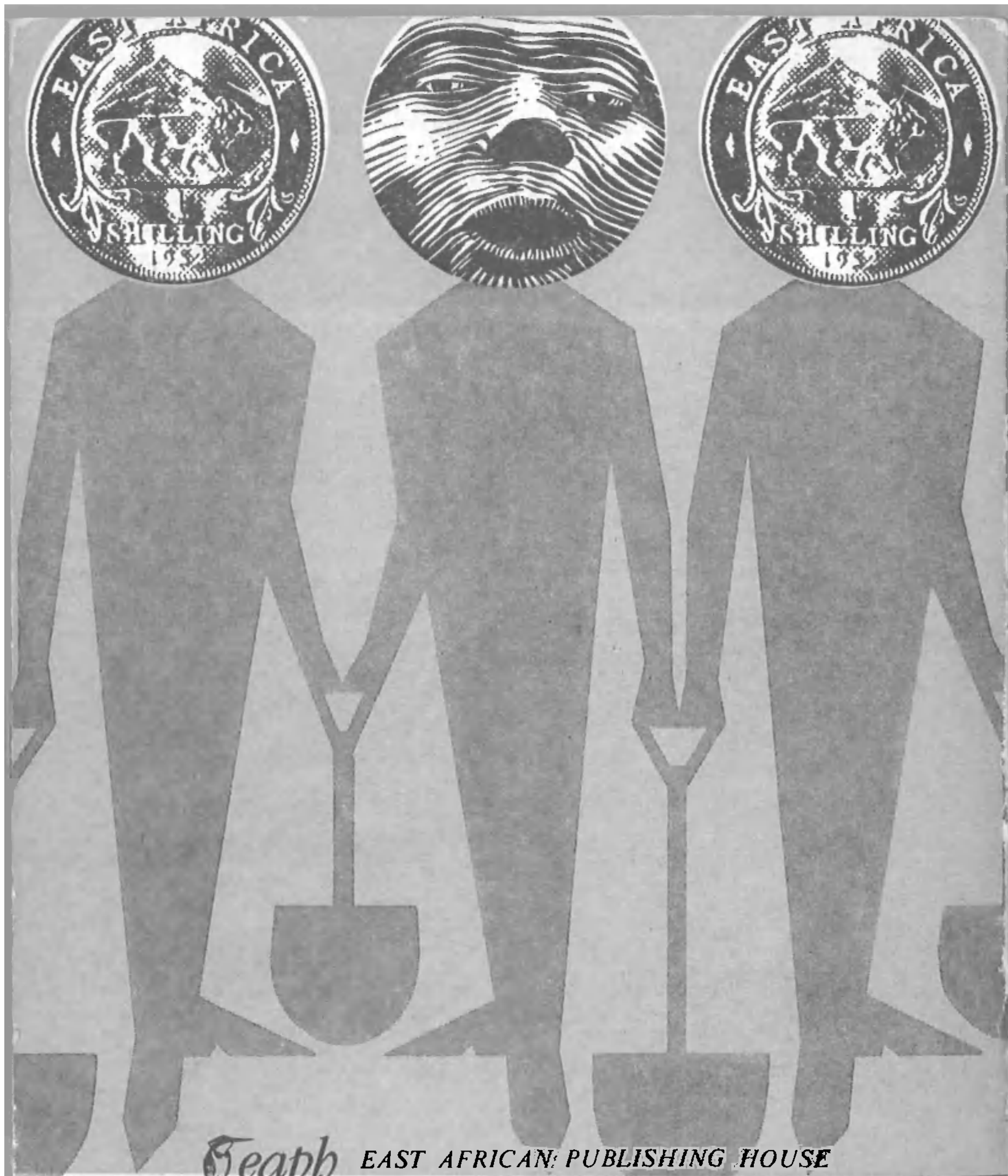
MAP

East Africa showing the Neighbours and main lines of transportation. . . . . *Frontispiece*



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