

## AFRICA RISK CONSULTING

### Country briefing – Uganda

19 December 2013

## Summary

*East African Community member states sign monetary union protocol in November. While tough preconditions mean the monetary union will not happen soon, it indicates a wider commitment to integration which should increase regional stability and improve trade flows.*

### 1.1 East African Community integration moves closer...

Uganda with its relatively developed economy and regional political aspirations is well placed to take advantage of the emerging East African economic community.<sup>1</sup> The **East African Community (EAC)**'s five member states - **Burundi, Kenya, Rwanda, Tanzania** and Uganda - signed a monetary union protocol on 30 November.<sup>2</sup> President **Yoweri Museveni**, chairman of the EAC until 30 November, has been at the forefront of efforts to further integration.

Regional cooperation has increased steadily in the past few months amongst a number of states within the EAC. In June, Uganda, Rwanda and Kenya entered into a **Tripartite Agreement**.<sup>3</sup> At the inaugural Tripartite Summit in **Kigali**, the respective heads of state committed to spearheading components of joint projects which will promote regional cooperation and trade. Uganda is leading the railway development and political federation sector; Rwanda is focused on customs, single tourist visa and the EAC e-identity card; Kenya is driving oil pipeline and electricity generation projects.<sup>4</sup>

However, speedier integration faces opposition both domestically and abroad. The opposition **Forum for Democratic Change (FDC)** questions the value of the EAC, observing that most Ugandans are unaware of the purpose of the EAC and the country's strategic interest in integration. *“Parliament and district leaders are all not visible in the processes, something that contradicts the initial essence of the*

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<sup>1</sup> Source, academic

<sup>2</sup> The East African, 1 Dec 2013

<sup>3</sup> Chimpreports, 27 Aug 2013

<sup>4</sup> ibid

*federation being people-centred.*"<sup>5</sup> As the 2016 election approaches Museveni will probably devote political capital to voters' domestic economic concerns at the expense of regional integration.<sup>6</sup> Dissent is already evident among member states with Tanzania and Burundi complaining in November that the other member states have marginalised them<sup>7</sup>. **East African Legislative Assembly** and **Democratic Party** legal adviser, **Fred Mukasa Mbidde** has confirmed that EAC lawyers are to challenge this perceived exclusion as well as any decisions taken by Kenya, Rwanda and Uganda relating to the proposed **East African Federation** without Tanzania and Burundi.<sup>8</sup> Further, Tanzania and Burundi are fostering closer ties with each other and with other neighbouring states such as the **Democratic Republic of Congo (DRC)**.<sup>9</sup>

Should East African integration take place, it would contribute to greater stability across the region. In December, Uganda closed its border with **South Sudan** and mobilised greater numbers of the **Uganda People's Defence Force (UPDF)** to the border following an apparent coup attempt.<sup>10</sup> Fighting between forces loyal to South Sudan president **Salva Kiir Maya** (2011-present) and those backing former vice president **Riek Machar** has spread beyond **Juba**. Concerned that the instability might spill over, Uganda has reinforced its security presence and deployed the UPDF 14th and 5th Divisions along the border. The East African region's **Intergovernmental Authority on Development** which includes **Horn of Africa** and **Nile Valley** member countries, is leading diplomatic efforts to resolve the situation. Growing interdependence with the other four members of the EAC will reduce the likelihood of regional animosity leading to outright diplomatic disputes.

## 1.2 Value of monetary union lies in steps taken to reach it

The five heads of state of the EAC member countries signed the **EAC Monetary Union (MU) Protocol** on 30 November 2013.<sup>11</sup> Although a monetary union remains a distant possibility, barriers to trade and movement will continue to fall.<sup>12</sup> The protocol will see the member states harmonise economic and monetary policies, with the eventual aim of establishing a single currency. The MU Protocol is expected to be ratified by April 2014, at which point states will begin to work together to

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<sup>5</sup> Source, journalist, Kampala

<sup>6</sup> *ibid*

<sup>7</sup> Source, international relations analyst

<sup>8</sup> Waswa, *op.cit.*

<sup>9</sup> Source, international relations analyst

<sup>10</sup> Daily Monitor, 18 Dec 2013

<sup>11</sup> Daily Nation, 1 Dec 2013

<sup>12</sup> Source, academic

synchronise monetary policies to ensure coordinated inflation rates, tax to GDP rates, debt to GDP ratios and fiscal deficits. A regional central bank will encourage effective coordination.

Discrepancies continue to exist between expectations and the practical implementation of policies on the ground.<sup>13</sup> The difficulty in achieving a single currency lies in the number of preconditions to the monetary union that states must meet. Members must attain, and maintain for three consecutive years, the following macroeconomic criteria: core inflation at 5%, fiscal deficits of no more than 6% and minimum tax to GDP ratio of 25%. The states must then meet the macroeconomic convergence criteria: ceiling on headline inflation of 8%, ceiling on fiscal deficit of 3% of GDP, ceiling on gross public debt of 50% of GDP, and reserve cover of four and half months of imports. They must also fully implement the EAC customs union and common market protocol. At least three states must meet these criteria to adopt the single currency.

In Uganda's case, it will be the inflation targets which are hardest to meet (see *ARC Uganda August 2013 Briefing*) as oil revenues will improve the tax to GDP ratio.

	<b>Target</b>	<b>Uganda (currently)<sup>14</sup></b>	<b>Uganda (2014)</b>	<b>Year expected to obtain</b>
<b>Core inflation</b>	5%	7.2% <sup>15</sup>	6-7%	N/A
<b>Fiscal deficit</b>	6% and 3%	2.6%	4%	Met, but spending pressure will increase in run up to 2016 election
<b>Tax to GDP ratio</b>	25%	12.6%	N/A	N/A
<b>Headline Inflation</b>	8%	6.1% <sup>16</sup>	5.0%	Currently meeting, but should be noted that stood at 8.1% in October and

<sup>13</sup> Source, international relations analyst

<sup>14</sup> IMF figures unless otherwise stated

<sup>15</sup> Central Bank of Uganda figures for November 2013

<sup>16</sup> Central Bank of Uganda figures for November 2013

				is likely to increase as election increases.
<b>Gross Public Debt</b>	50%	37.6%	40.6%	Met
<b>Reserve Cover</b>	Four and a half months	Four months	N/A	N/A

While the monetary union is ambitious, it is indicative of a wider pattern of policies committing East Africa to business and economic integration. The common market, customs union and **Single Customs Territory** will all increase the flow of trade in the regional arena and attract foreign investors.

### 1.3 Regional infrastructure already underway

A significant objective of EAC member states is to develop and connect the region's infrastructure such as road and rail links to reduce bottlenecks to trade. One of the most recent projects is the construction of the **Mombasa to Kampala to Kigali** railway, undertaken under the tripartite initiative. **Kenyan** president **Uhuru Kenyatta** officially launched the Mombasa standard gauge railway project on 28 November.<sup>17</sup> The **Chinese** funded \$13.8 billion transport link will initially connect Mombasa with **Nairobi**, and eventually with Kampala, Kigali and **Juba** by 2016. Under the tripartite arrangement between Rwanda, Uganda and Kenya, infrastructural developments are expected to boost the flow of investments across the region. The railway will strengthen Kenya's position as a logistics hub, with the government claiming that the cost of transporting cargo will decrease by 60% but will disproportionately benefit Uganda. **Kenya Ports Authority (KPA)** figures show that 73.1% of transit cargo through Mombasa is destined for Uganda, with South Sudan second with 11.6%.<sup>18</sup> The **Voi-Taveta-Moshi** road is also to be scheduled to be launched in December 2013, and the **Lunga Lunga** road is to be renovated so that it connects with Tanzania.<sup>19</sup>

## 2 Implications

The tough economic preconditions to monetary union indicate that there is an underlying tension between the political and economic aspirations of the EAC and the reality of its individual member

<sup>17</sup> Daily Nation, 28 Nov 2013

<sup>18</sup> KPA Figures, 30 Nov 2013

<sup>19</sup> PSCU, 28 Nov 2013



states. While the Tripartite Agreement has aided integration between its three signatories and could potentially benefit trade and cooperation for the broader region through its planned projects, it has also led to political tension and increased mistrust due to its 'exclusivity'.

The central role that Uganda plays in the Tripartite Agreement and the criticism it has come under may lead to increased political opposition on the home front. The government's increasingly authoritarian tendencies are adding impetus to rising discontent. Electoral politics could lead to the Ugandan government's focus shifting significantly from the regional to the national. With the Ugandan presidential elections in 2016, such a shift may occur sooner than anticipated. With Uganda being the driving force behind the latest EAC initiatives, and its particular interest in political federation, its domestic political climate affects the EAC's political developments. A shift in Uganda's focus may diminish the political will of the EAC and affect its ability to implement regional policies and integration.

At the same time, the signing of the EAC MU Protocol indicates a commitment towards economic integration. While the protocol faces issues of sovereignty, power, and the logistics of unifying diversified economies, it suggests long-term cooperation and improved flow of trade - at least on paper.

The feasibility of the MU depends to a certain extent on all the member states fully implementing and subscribing to the practices of the common market and customs union. While this is already partially in place, there is still a long way to go before it is fully implemented. Furthermore, the ability of all the member states to meet the stipulated macroeconomic criteria and sustain them for a minimum of three consecutive years prior to embarking on the actual MU implementation is questionable. Uganda's future oil revenues and willingness to share them may also affect MU implementation.

In the interim, attempts by the member states to comply with the requirements should slowly aid the flow of trade and increase cooperation, making it possible for businesses to extend their reach and scope within the region at potentially reduced costs.