DOING BUSINESS IN
The East African Community

FINANCIAL TIMES **SPECIAL REPORT** | Wednesday November 30 2011

www.ft.com/east-africa-community-2011 | twitter.com/ftreports

A regional market starts to take shape

Katrina Manson and **William Wallis** report on the relaunched trading bloc, 34 years after the first attempt fell apart

When the East African Community (EAC) was first launched in 1967, it was among the most sophisticated regional alliances in the world. External trade, fiscal and monetary policy, even university education operated under the same umbrellla. Europe cert was far behind at the time.

Thirty-four years after it fell apart amid intense political and ideological rivalry between its three member states – Kenya, Uganda and Tanzania – the EAC in its latest and larger iteration – adding Rwanda and Burundi – is at the vanguard once again of African regional integration.

The logic behind its relaunch is not so different from that which informed its creation: if African countries traded more with each other, strengthened co-operation in keeping the peace, and spoke with one voice on the world stage, they would go a long way toward overcoming the frailties associated with their colonial era borders.

By merging into larger trading blocs, the continent's fragmented markets become at once more enticing to outside investors and in a stronger position to negotiate a better deal.

Driven by this logic, and with few of the ideological differences that divided members in the past, regional leaders and bureaucrats have spent the past decade refashioning the EAC for the 21st century.

On paper it is beginning to work. The EAC has a customs union, a common market, a legislative assembly, a bank and a court. It even has an anthem.

More than 133m people with a combined gross domestic product of $80bn in the five countries now trade among each other with fewer barriers. Intra-regional trade up is up as a result, from $1.8bn in 2005 to $2.7bn in 2008 – although this still only repreaents 11 percent of EAC total trade with teh rest of the world Growth across the five was 6.4 per cent a year for the years 2005 to 2009, making the region among the fastest growing in the world.

> Integration cannot succeed with less than whole-hearted political backing, some officials in the region argue

As Burundi, its newest member hosts the 13th EAC heads of state summit today the community is even considering expansion: both South Sudan and Sudan want to join.

"The EAC is the fastest growing of all the Africa regional economic communities," says Donald Deya, head of the Pan-African Lawyers Union, who has worked on the complex legal issues that have emerged.

Next year, the EAC even plans to create a monetary union and, in 2015 political federation. Consultants like to say the bloc is trying to do in 10 years what the European Union achieved in 48.

Yet as momentum gathers, some of the same tensions are arising that dogged the EU as it grew. Integration cannot succeed with less than whole-hearted political backing, some officials in the region argue.

"Half-integration is dangerous in my opinion, because it gets half of the benefits and all of the costs," says Richard Sezibera, the new secretary-general of the EAC, who is a strong advocate of closer political union and a regional currency zone.

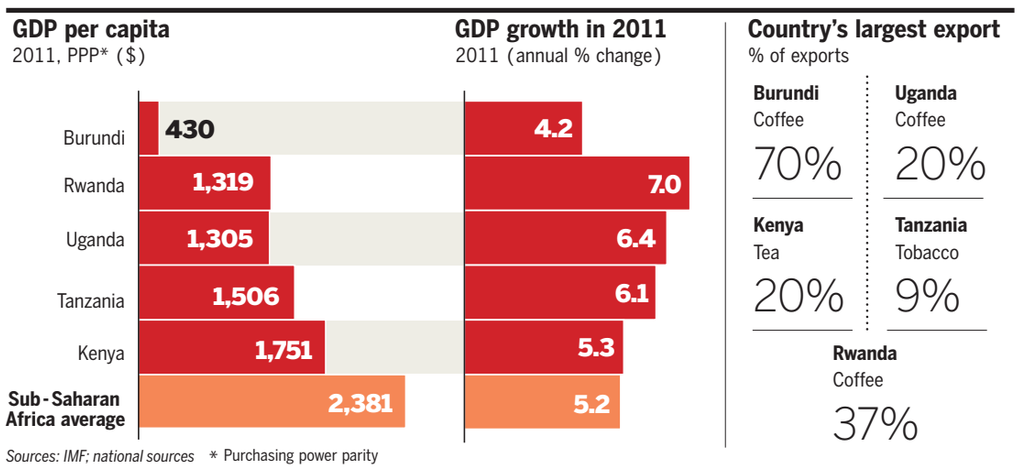
Yet in a year when the future of the eurozone has been called into question and countries such as Britain outside it are pushing for the return of powers ceded in the past, there are obvious lessons about the dangers of allowing political enthusiasm to get ahead of economic reality in countries that still differ greatly in fiscal and economic terms.

Juma Mwapachu, the former secretary-general who stood down this year, says that if the community is to avoid getting bogged down like the EU has in detailed debates about national sovereignty, it should focus initially more on the "bread-and-butter" matter of trade flows.

On this subject, opinions on progress among business people in the region are mixed. Some manufacturers say that in the current global environment they could not keep going without the benefit brought by

Continued on Page 2

Flying the flags: national emblems of the five East African Community members meeting in Burundi today



Sources: IMF; national sources * Purchasing power parity

Inside this issue

Lack of harmony on road to smooth cross-border trade

Barriers to trade

Katrina Manson says transport costs 80% more than in US and Europe

Tourists gazing at the azure horizon of Tanzania's Indian Ocean coast are disturbed by a long line of ships lit up like baubles.

The port at Dar es Salaam is so packed, vessels must anchor outside for days before a space is free for them to offload cargoes.

The delays, along with lengthy customs clearance, road blocks, bribes and duplicate border posts, are among non-tariff barriers that raise the price of goods destined for the entire east African region. Together with Kenya's port of Mombasa, Dar es Salaam supplies a hinterland reaching landlocked Burundi, Rwanda, Uganda and beyond.

The World Bank's latest Doing Business survey finds that while it costs $1,430 to import a container to Tanzania, it costs $4,990 in Rwanda, 1,400km inland.

Woolworths, the South African retailer, says clearance at Dar es Salaam is so time-consuming that goods arrive in stores in Tanzania nearly two weeks after those flown at three times the expense direct to Uganda, where they clear customs in a fraction of the time.

"There are too many agencies checking and inspecting, too many power outages and computers going down, money being paid but not reflected in authorised banks for a whole week at a time – in retail, time is everything," says Ali Mufuruki, a joint owner in Woolworths' Tanzania and Uganda operations.

Businesses are frustrated at the lack of progress delivered by a customs union signed in 2004 and the common market that officially kicked into play last year. "There isn't a lot of commitment and zeal to implement some of these common market issues," says Agatha Nderitu, head of the East African Business Council.

"They haven't harmonised domestic taxes; non-tariff barriers are still a big issue; and they still don't have a mechanism for revenue-sharing," she says. "We still have internal borders within what is meant to be a single customs territory."

TradeMark East Africa, a donor-funded body intended to help make EAC integration a reality, says transport and logistics costs are 70 to 80 per cent higher than those in the US and Europe.

It wants to cut the cost of doing business across borders by 15 per cent over three years, which it says will save the region close to $6bn, through efforts such as joint border posts and pre-clearance for customs.

It is in the nitty-gritty of regional decision-making – the likes of a three-day axle weight harmonisation workshop, and debate over 26 separate agreements over computerised scales and weighbridges – that costs can be cut.

But it took 10 years for member states to agree on a 56-tonne standard heavy-loaded truck, in the effort to halve waiting time costs at border posts.

There are too many power outages and computers going down – Ali Mufuruki

Member states still have widely differing approaches to regulation. While the tax rate amounts to 31.3 per cent in business-friendly Rwanda, it reaches 49.6 per cent in Kenya, where taxpayers must allot 393 hours to the process, more than double that in Rwanda.

It takes three days to open a business in Rwanda, ranked 45 of 183 countries worldwide for its ease of doing business, but 34 in Uganda (ranked 123). Burundi, at the bottom of the five at 169, is nevertheless ranked among the world's top 10 improvers.

Such disparities are already losing countries business.

Aly-Khan Satchu, a stock market investor who runs Rich Management in Kenya, is so frustrated with regulatory hurdles he is setting up a brokerage in Rwanda and hopes to trade Kenyan stocks directly from there.

Experts cite examples where member states discriminate against each other to the benefit of outsiders.

"It is still easier for a Briton or an Indian to come and work in east Africa than it is for a Kenyan or a Ugandan to find semi-skilled or service sector jobs in each other's country," says Robin George, director at Adam Smith International, following a study by the consultancy in Uganda.

Despite common protocols on freedom of movement, Nakumatt, a Kenyan supermarket chain, says it has received only four permits for its Kenyan expatriate staff of 10 needed to set up its first store in Tanzania.

Despite the official phasing out of internal tariffs, experts say there is plenty of deliberate protectionism. While countries have signed up to the principle of freer trade, the instinct to protect domestic industries and jobs continues to hold up everything from milk to margarine, and beef exports to one-day old chicks.

"Everybody thinks they have their own bureau of standards," says Atul Shah, Nakumatt's managing director. He says each country follows the laws of its former colonial power, with the odd bit of South Africa thrown in, and regularly changes the rules. "Everything. including a banana, they will want to test."

Stock markets Integration has a long way to go

Across a small screen in a reception room at the Dar es Salaam stock exchange, a digital line representing the direction of the index does not deviate from the horizontal. Four minutes before the close of play, two hours of trading has seen 31 deals.

There are six of a total seven brokers in today. And they are sweltering in red jackets they are not allowed to remove in the cramped room with air conditioning that barely tempers the tropical heat.

There is hope regional integration will deliver bigger, faster trading exchanges to enable region-wide listings, investments and attract more capital.

Officially, the East African Community already requires a free flow of capital across borders, but harmonising rules, linking systems and establishing a single trading platform remain far off.

The DSE, the most closed of East Africa's four exchanges, not only has a 60 per cent cap on foreign investment in its 15 stocks, it also defines Kenyans and other east Africans as "foreign", despite the fact that Kenyan cross-listings account for a third of stocks, 65 per cent of the DSE's $3.7bn market capitalisation. In addition, the ban contravenes EAC treaty rules that the country signed up to in 1999.

Not only that, but so fearful is the country of the prospect of capital flight, Tanzania bans its citizens from investing in stock exchanges abroad, including in Kenya, unless the central bank grants special dispensation. When Safaricom, the telecoms operator, listed in the biggest IPO the region is yet to see, Ugandans and Rwandans were among the investors; Tanzanians were not.

Both domestic and foreign investors see the benefits of more open, linked markets that make the most of scale and increase liquidity. Advocates say a regional market would also help raise funds for large-scale infrastructure investments, reduce the cost of capital-raising and attract greater participation from foreign funds.

Dar stock exchange

Michael Turner, East Africa director of Actis, a UK private equity firm, says: "A genuine regional exchange will give us a more liquid market and, of course, a more useful forum for private equity investors such as Actis to exit their investments."

Several companies, including Tanzania's Sumaria Group, say they will list only if a regional stock market exists.

Kenya's Nakumatt Holdings plans to list in 2015 across the region. In a mark of how far regulatory environments diverge, Mr Turner says that when Actis this month sold its 54.4 per cent stake in DSE-listed Tanzania Tea Packers (Tatepa), a start-up tea company supplying Fairtrade, he found "onerous disparities" between regulations in Tanzania and equivalent rules in Kenya and Uganda.

Stock market integration does not fall under EAC treaty rules, but the East African Member States Securities Regulatory Authority (Easra), continues efforts to match up regulation and data sharing. The authority has a two-year midterm strategy, which has made possible the issuance of regional bonds and is feeling its way to connect markets with vastly different characteristics.

While Kenya and its 58 listed companies and $9.9bn market capitalisation has automated trading, others rely on an open outcry system. Burundi has no stock exchange at all. Rwanda has only four stocks to its name.

A late starter, Rwanda is nevertheless way ahead in terms of regulation. It is the only market in the region with a demutualised exchange, something Kenya is struggling with and Uganda and Tanzania are turning to only now. "Rwanda had the advantage of coming in last, so we went for the best," says Robert Mathu, head of the country's Capital Market Advisory Council.

"We are the most compliant capital market with regards to integration, because we deliberately picked requirements with common market protocols in mind."

Mr Mathu, who is also executive director of the Easra, says that, although other markets have agreed to integration, they face a long and cumbersome process to reform laws that govern them. Kenya's Companies Act, for example, is based on 1940s English law.

For now, each country will keep its own regulator, each of which has agreed to implement steps toward integration, although no decision has been taken on the ultimate form it will take.

To integrate, all markets need to demutualise and automate, with the same system, and no one has yet determined who will pick up the bill.

Katrina Manson

In urgent need of serious investment

Infrastructure

Congestion in the region is forecast to hit 'epic' levels, says **Katrina Manson**

Kenya has the largest port in east Africa, moving 19.1m tons of cargo a year. But onward transport connections from Mombasa to the hinterland are so poor that Nduva Muli, managing director of Kenya Railways, says the country loses some of its associated advantage.

"If we don't solve the problem, even we Kenyans can call ourselves landlocked," says Mr Muli.

Across the region, railways – easily the cheapest but most neglected form of transport – shift only 6 per cent of port cargo. The rest goes on roads straining under the pressure of ever increasing traffic.

An inter-governmental study out this year says congestion in the East African Community (EAC) is set to reach "epic" levels.

This will limit the economic growth for which the region is striving. It says road traffic is set to quadruple by 2030. By then, it predicts more than 100m tons will arrive at ports and rail will need to cope with an annual 18m tons.

"Without infrastructure there is no development," Raila Odinga, Kenya's prime minister told a regional conference in September.

Be it unreliable rail, worn roads or clogged ports, transport delays already contribute up to 25 per cent of logistics costs. The World Bank estimates transport unit costs are six times higher in the EAC than in China and India.

Huge investment is needed to bring the region up to scratch. The same study estimated that it would cost $3.4bn over five years to finance 43 infrastructure projects designed to bridge the gap.

These include new container terminals at both Dar es Salaam and Mombasa ports, for $500m and $342m, and improving the two main transport corridors that serve the hinterland.

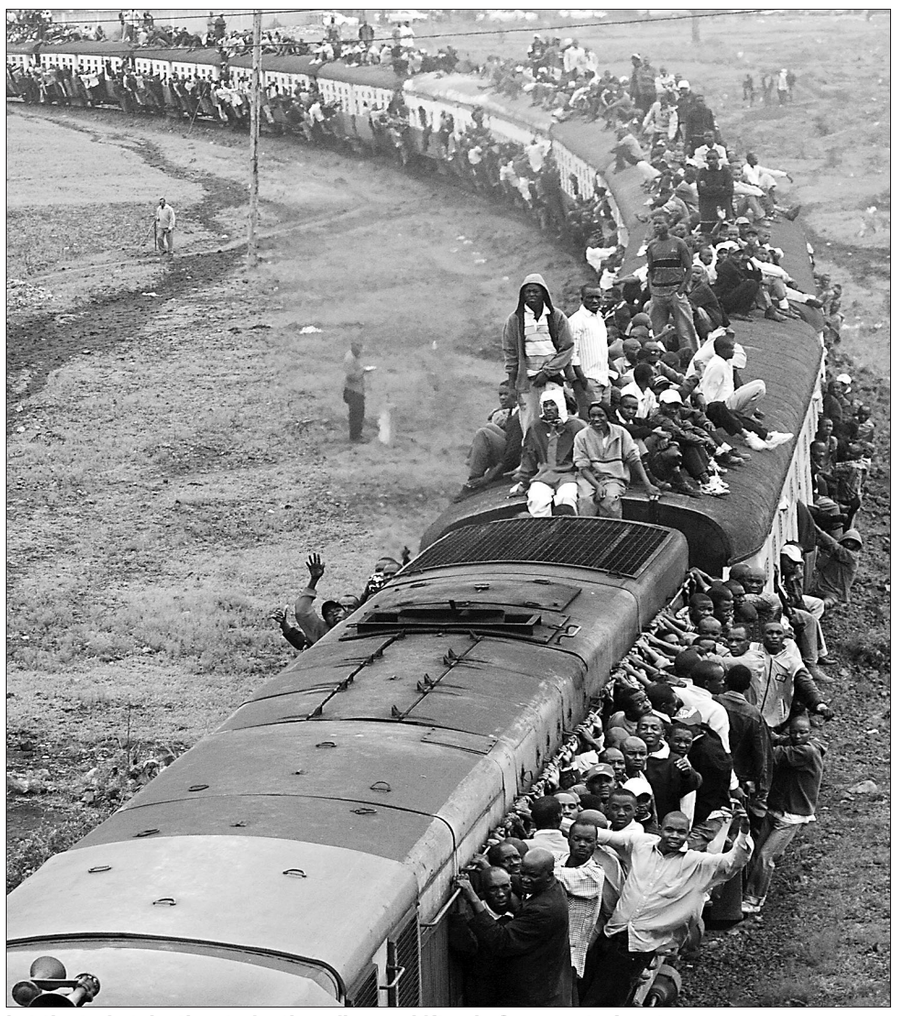
The report says that such investments would save 28 per cent on transport costs, making $1.9bn by 2015.

Among other projects, it also lists a $280m injection into Rift Valley Railways, a private consortium with a 21-year concession to run the beleaguered Kenya-Uganda rail line, built in British colonial times.

Despite the century-old line's reputation as the Lunatic Express, Citadel Capital, an Egyptian private equity invested in RVR and now holds 51 per cent of the company.

The dearth of investment over the past 25 years means a huge rehabilitation project is required. A $345m plan to modernise the railway by 2017 is expected to boost freight volumes from 1.6m tonnes in 2009 to 4.2m.

Karim Sadek, managing director of Citadel Capital, is convinced that the high cost of fuel will ultimately make the project worthwhile. "Rail has a natural competitive edge compared to trucking when it comes to fuel – it is the single largest operating expense for vehicles, at 70 per cent, while for rail it should be 25 to 30 per cent," he says.



Let the train take the strain: the railways shift only 6 per cent of port cargo Reuters

Like many potential investors in the region's dilapidated infrastructure, he says maintenance has long been lacking.

Maintenance costs are regularly overlooked in public infrastructure, so the company is also trying to encourage better working practices to reduce costs. It gives drivers a 30 per cent cash bonus for each safe journey they make.

> Citadel Capital gives drivers a 30% bonus for each safe journey they make

So far, pay-outs have reached $250,000, but Mr Sadek says the company has saved more than six times that as a result of fewer breakdowns. The company also wants to reduce its staff from 3,282 to about 1,000.

Profit-focused lessons such as this may prove critical for attracting the private sector. Officials are counting on a series of public-private partnerships to fix everything from power generation to roads.

Infrastructure will inevitably stretch beyond the five members of the bloc. A conference in Nairobi this year brought together three regional blocs collectively known as "the Tripartite": the EAC; SADC, the Southern African Development Community and The Common Market for Eastern and Southern Africa, with 19 members. The Intergovernmental Authority on Development, which represents six countries in the Horn of Africa joined.

Kenya is keen to start a 32-berth project at Lamu from scratch, along with roads, railways, an oil pipeline and airports intended to serve South Sudan and Ethiopia. The ambition is for the port to transport 23.9m tons a year by 2030 and take 30 per cent of traffic to South Sudan and Ethiopia.

Sindiso Ngwenya, head of both Comesa and the Tripartite, is keen on the $24.7bn project. "This is the land bridge that will connect the east to the west coast of Africa," he says.

Such grandiose projects need support from multiple governments, which is why Gabriel Negatu, east Africa head at the African Development Bank, describes infrastructure as "the big integrator" that will elicit government backing and commitment by necessity.

"Infrastructure is an enabler, it allows the private sector to come in and it allows domestic resources to be effective," he says, adding the bank will put hundreds of millions of dollars into these projects.

"If we get this right, then the whole region, even if some are landlocked, will become connected."

Regional market starts to take shape

Continued from Page 1

the 25 per cent common external tariff (CET) that fends off Asian competition.

Yet, even where there has been significant progress on the rules, reality on the ground is slow to follow.

A study carried out by Rwanda's private sector business association found the cost of trucking a container from the Kenyan port of Mombasa to Kigali, the capital, 1,500kms and three border crossings away, can be three times the price of shipping the same container from the US to Mombasa. Bribery at weighbridges and roadblocks in Kenya and Uganda can add more than $1,000 to the cost.

Attempts to phase out waivers to the CET and phase in zero internal tariffs have also run into obstacles. Five-year exemptions intended to help weaker economies expired in 2010. Yet each country is still negotiating rolling exemptions; some governments use these as patronage, while many paper commitments remain just that.

Agatha Nderitu, executive director of the East African Business Council, says: "Bringing our fragmented markets together and removing the barriers to trade is very beautiful, but our feeling is that there is a lot that is committed on paper that is not translated on the ground."

Dr Sezibera says 27 non-tariff barriers have been removed so far, leaving another 28 to go. Meanwhile, member states still cannot clear cheques in each other's countries nor invest easily in each other's capital markets.

Some of the bigger stumbling blocks that led to the collapse of the EAC in 1977 have disappeared – between capitalist Kenya and socialist Tanzania, for example – nevertheless continue to slow the way.

The region's economies complement each other better today and governments now follow broadly similar policies. Kenya has a fairly advanced and diverse economy, a sophisticated financial sector, and the largest manufacturing base in the region. Tanzania and Uganda both have abundant fertile land and natural resources and the discovery of oil in Uganda and gas in Tanzania means that the region will soon have its own energy supply. As the smallest countries in the region, Rwanda and Burundi perhaps stand to gain most from inclusion in a bigger market.

The incentives for closer co-operation on infrastructure development are also strong. Mombasa port has reached capacity, the railways are dilapidated, and roads everywhere are in need of upgrading.

'Removing the barriers to trade is welcome' – Agatha Nderitu

Fears of Kenyan dominance, however, are ever present, and to the frustration of many Kenyan businesses, remain an obstacle to faster integration.

"In Tanzania in particular and Uganda to a lesser extent there is this fear that Kenya is the dominant partner," says Sumaria group's Mr Shah.

Mr Deya at the Lawyers Union says supranational justice offers the best way of forcing the pace and challenging states that fall behind on their commitments. "Eventually, it's litigation that will embarrass states into action."

Business can take laggard states to task over failures to meet protocols on the customs union and the common market in the East African Court of Justice.

He adds: "Governments don't like being sued. But the courts have said 'No no that's exactly what you signed up to. Too bad; the fleas come with the dog'."

He may be right. But whether bureaucrats are forced on board or not, businesses are already forging ahead. Banks and supermarket chains are building networks throughout the Community. Telecoms companies are harmonising their operations to gain economies of scale. As the informal sector has always shown, African borders are mostly artificial.

Contributors

Katrina Manson
East Africa Correspondent

William Wallis
Africa Editor

Parselelo Kantai
FT Contributor

Stephanie Gray
Commissioning Editor

Steven Bird
Designer

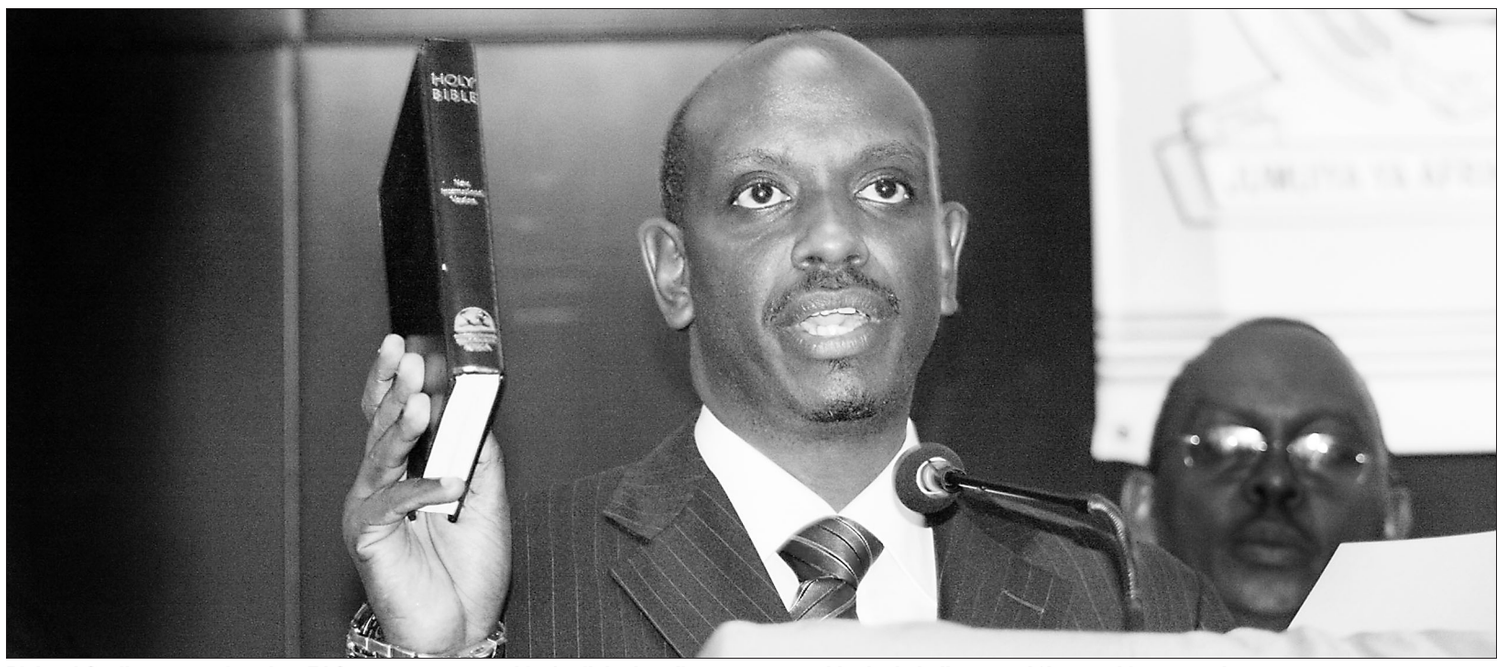
Andy Mears
Picture Editor

For advertising details, contact:
Mark Carwardine:
+44 (0) 20 7873 4880;
email:
mark.carwardine@ft.com
or your usual representative

All FT Reports are available on FT.com.
Go to:
www.ft.com/reports

Follow us on twitter at
www.twitter.com/ftreports

All editorial content in this supplement is produced by the FT.



Richard Sezibera: appointed as EAC secretary-general in April, he has five years to tackle dual challenges of 'fear and ignorance'

Not by halves, says EAC boss

Interview
Richard Sezibera

Katrina Manson talks to the EAC secretary-general

Richard Sezibera has five years to tackle what he sees as the two greatest challenges to regional integration: fear and ignorance.

The former minister of health in Rwanda took the helm of the East African Community in April, determined not to do things by halves. He looks set to use his five-year tenure trying to accelerate the pace of integration at a critical moment in the regional bloc's existence.

"Half-integration is dangerous in my opinion, because it offers half of the benefits but all of the costs," says Dr Sezibera, who has the support of the EAC's most ardent advocate among heads of state, Paul Kagame, Rwanda's president.

He says that trade between the most reluctant integrationist, Tanzania and other EAC member states has actually grown the fastest of the three original member states:

"There is ample evidence that the fears and expressed by most Tanzanians and Ugandans at the beginning were not borne out."

Dr Sezibera says the overarching aim of integration is "about becoming a competitive, secure, prosperous east Africa" leading towards monetary union and political federation.

"To be competitive, secure and prosperous, we have no choice but to do it together, because we cannot do it separately," he observes.

The former doctor of medicine says the experience of integration of both the US and the European Union shows the need to overcome long, costly and difficult issues.

"Integration by its nature may front-load the cost, so that constitutes the challenge, because the people and the nations look at the costs to them, which may be immediate unless they're handled well," he says.

For all the bugbears over halting implementation of grandiose pledges, Dr Sezibera says progress has been "remarkable".

Creation of a single customs territory, the most immediate issue, will still take "a lot of leadership and commitment from partner states. We are determined to make sure this gains momentum", he says.

He attributes delays in realising the dividends of the common market, such as free movement of labour and capital, to a process under which national governments must ratify each agreement. Already the EAC has scored some significant victories, given protectionist concerns about the job market. Member states have agreed to mutual recognition of professional qualifications, putting workers on an equal footing throughout the region.

He is determined to chivvy governments to do more: a new common market scorecard will expose the dawdlers.

"Every time the countries meet, we see who is not doing what. They give an explanation and provide a plan to redress where they're falling behind," he says.

> 'There is a lot of work, and a lot of it will be acrimonious but it has to be done'

The best way to deal with the problems of slow progress, non-tariff barriers and discordant fiscal regimes, he says, is through the institutions of the community itself.

"Anybody who is aggrieved in commercial transactions has the right to be heard nationally or regionally and take up their cases. They're absolutely right to go court if their rights are being trampled on."

The embrace of regional legal recourse forms part of his backing for the development of stronger and wide-reaching supranational institutions, including the legislative assembly. These raise member concerns about loss of sovereignty.

"As we integrate more, there is need for supranational bodies to drive the agenda," he says, adding that such bodies must further avoid the risk of "democratic deficit" by embracing region-wide elections, which critics argue will further erode national pre-eminence.

That way, he says, citizens can retain control of their political and economic destiny.

Juma Mwapachu, the former EAC secretary-general, who stood down this year, argues the contrary. He says the community should be less giddy about political integration and focus more on the "bread-and-butter" matter of trade flows if it is to avoid becoming stuck in the kind of debates about national sovereignty that bogged down the EU for years.

"Let the legislative assembly be the driver of deeper economic legislation and be better recognised and appreciated," says Mr Mwapachu. "If you begin to create some kind of a supra-institution to address democratic deficits at national levels, it will never work," he says, warning of the continuing primacy of national politics.

Dr Sezibera refuses to accept that fine-tuning the bread-and-butter issues and pursuit of more ambitious plans for political integration are mutually exclusive.

"They are not different. My belief is that the EAC can walk and chew gum at the same time, so we're doing both." he says.

"Sometimes governments are not quite ready to relinquish their sovereign power; that is normal. It happens in the EAC, in Europe, in every regional community," he says.

But, he counters, member states know they signed up to a "rightly ambitious" treaty intent on ultimate political federation.

"To have agreed on a customs union and engaged earnestly in negotiating a monetary union means the five partner states are quite willing to pool their sovereignty in pursuit of a common good," he says.

"We must make sure the community brings everybody on board – businesses, students, MPs must be on the same page.

"The women of east Africa must agree. There is a lot of work, and a lot of it will be acrimonious, but it has to be done."

Counterfeit goods Where to go for a Chinese BlackBerry

For $50, you can get yourself a brand new BlackBerry in one of a row of little shops selling mobile phones near Jamia Mosque in central Nairobi.

It does not come with a warranty and the shop assistant – briefly lowering his eyes – signals that it is a "Chinese BlackBerry", exquisitely possessed of all the external brand features of the phone, but none of its applications.

Similar counterfeit brands exist for other phones in similar markets across east Africa's towns and cities. They sell in the thousands to lower income consumers, unable to afford the real thing, but seduced by big brand names.

From pharmaceuticals, to cigarettes, foodstuffs, phones, CDs and DVDs, the trade in counterfeits is increasingly biting into the profits of east African manufacturers and traders.

Shipped in mostly from Asia and smuggled through the region's porous borders or through legitimate ports staffed by corrupt officials, they affect virtually all areas of trade.

It does not help that Somalia's southern port of Kismayu, controlled by the militant group al-Shabaab, has become an entry point for illicit goods.

The trade is increasingly linked to organised crime syndicates, and attempts to fight it are hampered by an unhappy combination of underfunded agencies, uneven regional tax regimes and endemic corruption.

In Kenya, the tobacco industry is the worst affected, with counterfeits representing up to $19m or 5 per cent of product sales.

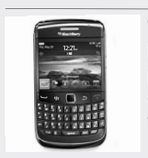
"Part of it has to do with the lack of a harmonised tax regime in the Community, the rise of Dubai and China as export outlets and the conflict in Somalia.

It's a regional problem. If there's a peak in imports, we normally see a corresponding spike in illicit trade," says Selena Olende of British American Tobacco in Nairobi.

While BAT has lobbied governments to address the problem, its efforts are ironically hampered by the stringent Tobacco Control Act, which, owing to its ban on advertising, limits what the company can do to educate consumers about the presence of counterfeit cigarettes.

While east African governments readily acknowledge the problem, they find themselves hamstrung by overworked quality inspectors at the ports and the ingenuity of smugglers. More than 2,000 containers arrive at the ports of Dar es Salaam and Mombasa each day, posing a Herculean task to the small inspection unit.

"Motor bikes have become a great means of transport for counterfeiters and their distributors. They bribe security officers staffing the crossing or use *panya* [illegal] routes to smuggle a whole container in minutes," said one inspector quoted in a local daily.



The Chinese BlackBerry: possessed of external features only

Just as problematic is the lack of a harmonised tax regime. Although the East Africa Community has a common external tariff in place, it is observed more in the breach than in practice. "There are still many parallel taxes, with various regimes, some of which are punitive.

To make the EAC common market an enabling platform for accelerated business investment and growth, there is a need to harmonise taxes – excise taxes, VAT and even corporation taxes.

Excise tax on soft drinks, the biggest element of the retail price, is administered differently in all five countries.

Tanzania runs a specific rate charging TS69 per litre of beverage, Kenya, Uganda and Rwanda run an ad valorem rate of 7, 13 and 39 per cent respectively. Burundi instead charges a sales tax of 50 Burundian francs per litre of beverage.

"We are engaging with the countries under the umbrella of the East Africa Business Council to lobby for some level of harmonisation of these taxes," says Nathan Kalumbu, business unit president for Coca-Cola in central, east and west Africa.

The presence of transporters willing to export illicit goods for small margins has also undermined the operations of legitimate hauliers, making legal business almost unsustainable.

"Somalis are killing the transport rates. Because of their competition, nobody can now make money out of it. If somebody makes a little commission from piracy, the only place they can invest and run a decent business is Nairobi.

"So a lot of them now go for trucks, second-hand trucks from Europe. There are hundreds, everywhere. Fuel trucks alone will be in thousands," says Hassan Guleid, a transporter and chairman of the Eastleigh Business District Association.

For manufacturers such as Jayesh Shah, head of the Sumaria Group of companies, the results have been little short of disastrous.

"We were the number one detergent company in Tanzania, but we found that, legitimately, we would not be able to compete," says Mr Shah. The company had no choice but to sell off its detergent company as a result.

"In Tanzania, there is a lot of business taking place without the payment taxes, and for us as taxpayers it was not making economic sense," he says.

His company's turnover has thus fallen from $200m three years ago to $120m today.

Parselelo Kantai
With additional reporting by Katrina Manson

Convergence efforts 'can only be helpful'

Monetary union

Katrina Manson reports on what may be unrealistic deadlines

The East African Community has already missed a 2009 deadline for monetary union, and the prospect of a common currency, now set for next year, still looks unlikely.

Growth across the region shrank to 1.8 per cent in 2010, down from 4.4 per cent in 2009. Galloping inflation in food and fuel prices, on top of depreciating currencies, has undermined much hope of macroeconomic convergence in 2011 and next year.

Besides, the economies are already vastly at odds. Incomes range from $833 a head in Kenya down to $173 in Burundi, while growth rates last year deviated between 7.5 per cent in Rwanda to 3.9 per cent in Burundi.

Tanzania is a member of two regional blocs – the EAC and the Southern African Development Community – both of which tout their desire for a single currency, which means at some point it may have to choose.

Richard Sezibera, EAC secretary-general, is adamant that members will sign a memorandum of understanding committing them to a common currency early next year. But that is different from realising a single currency.

"There are complications undoubtedly," says a bullish Dr Sezibera of the crisis in the eurozone alongside rampant inflation and crashing currencies within the EAC.

The regional target of 5 per cent inflation is way out of reach. Following a series of shocks and mismanagement at home, Kenya, the dominant economy, is battling 18.9 per cent inflation.

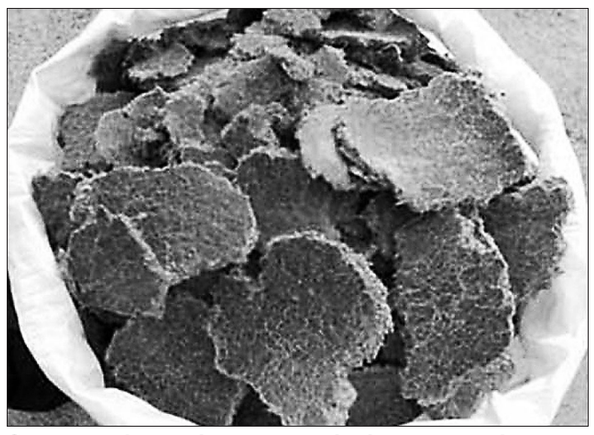
A European Central Bank study requested by the EAC says monetary union next year is "unrealistic" and that the group is not ready, warning that constantly shifting deadlines will also damage the project.

"Unrealistic timetables and consequent postponements may undermine the credibility of monetary union and thus the support from market participants and the general public that is necessary to the whole process," says the study. Yet, EAC officials insist the project is still on.

> It is an open question whether members have the commitment to cede fiscal control

Many companies operating in the region would welcome a single currency.

Sumaria Group says cross-border sales into Kenya of its cotton seed cake, an animal feed by-product from its Tanzania cotton ginning operations, are down after the Kenyan shilling depreciated further than the Tanzanian shilling, making it too expensive for its customers on the other side of the border.



Currency swings make cotton seed cake too expensive

"This is a clear example where, if we had a common currency, that problem would not be there," says Jayesh Shah, group managing director at Sumaria.

The EAC says it has learnt the importance of matching up fiscal policy in addition to monetary policy from the eurozone experience. It is seeking advice from the International Monetary Fund to revise the rules on convergence.

"In terms of the ultimate objective of a common currency, that's clearly a long way off," says John Wakeman-Linn, IMF head in Tanzania. The IMF nevertheless believes the effort to converge is worthwhile.

"All the things they need to do to achieve a common currency – integrate financial markets, labour markets, capital markets, trade policy, statistics databases, develop easy mechanisms for exchanging each others' currencies – all of these would be extremely valuable and would help develop the regional economy, and so they should do them," Mr Wakeman-Linn says.

It is "an open question" whether member states really have the commitment, willingness and ability to cede fiscal control to the regional level, he says.

Member states have yet to agree on the prospect of special funds that individual countries might draw on to cushion their economics in times of external shocks, such as a drought affecting only one member, or tax transfers from the likes of Kenya to Burundi to even out inequalities.

He says that Kenya, like Germany, might even benefit from such fiscal transfers.

"It is just like Germany and Greece," he explains, pointing out Germany has benefited from the inclusion of less developed economies keeping the real exchange rate of the euro lower than what the D-Mark would have been.

"Germany has benefited from greater competitiveness because its exchange rate has been affected by having these weaker parties in the market," points out Mr Wakeman-Linn.

But, he acknowledges this might inflame local sentiment, since Kenya's own finances are stretched in one of the most unequal countries in the world.

"Politically, it is a lot harder to point out that to your population when they say 'yeah but why are you transferring x billion shillings to Burundi'," says Mr Wakeman-Linn.

It might be tempting to see Kenya as the Germany of east Africa. But it is a long way from being Germany.

Business and buoyant middle class take to the skies

Airlines

Parselelo Kantai reports on an industry that is bucking the international trend

When John Mirenge was recruited by the Rwandan government to head RwandAir, he was inheriting a company with a history of failure. Air Rwanda, the former national carrier had been defunct for two years.

Attempts to privatise the new venture were successful. Then, in 2009, the government decided to invest directly in it, injecting $200m and giving it exclusive ownership.

The turnaround was remarkable. In a little over two years, RwandAir expanded its destinations to include Juba, Mumbai and various capitals in southern Africa, identifying the rapidly diversifying travelling patterns of its clients.

However, its aggressive low-pricing policy is perhaps most responsible for its increased passenger numbers. For about $280, passengers can shuttle between capitals Kigali and Nairobi; Kenya's flagship carrier would charge more like $380.

Special-deal singles to Johannesburg are half those of competitors. Annual passenger numbers have risen to 500,000. up from 200,000 at the end of 2009. The airline expects to carry 1m people in the next two years.

"RwandAir has never positioned itself as a low-cost airline, but we're now opening up to low-budget travellers," says Mr Mirenge, RwandAir CEO, formerly head of the state-owned water and utilities company.

And while the airline is focused on passengers and not cargo, freight business has also grown from one exclusive flight a week to four.

While RwandAir's return to East Africa's skies and beyond is impressive, it is hardly remarkable. Even as the global aviation industry is in the doldrums, facing rising fuel costs and pinched margins, East Africa's carriers are enjoying growth, posting healthy profits and undertaking ambitious fleet and route expansions.

"The market in this region is undersupplied. You're still getting the best yields here over anywhere else in the world," says Mr Mirenge.

While RwandAir has maximised its lucrative Kigali-Nairobi route, flying into the Kenyan capital seven times a day, the airline is focusing on untapped regional markets such as eastern Democratic Republic of Congo, and also taking advantage of the increasing commuter traffic into favoured Middle East destinations such as Dubai.

The airline, relatively small by regional standards, with a fleet of 11 aircraft buoyed by a recent Boeing purchase, has raised the stakes in an industry that is becoming increasingly competitive.

"For us, it is not about our size. It's about the region we're in," says Mr Mirenge.

In a year marked by volatile fuel prices, currency fluctuations and inflation, East Africa's aviation industry is likely to see an overall drop in profits. However, while global aviation continues to be hit hard by the economic downturn, the region's airlines, tapping into new markets while expanding capacity on existing routes, remain remarkably bullish.

Both Kenya Airways and Ethiopian Airlines, the dominant local carriers, have recently undertaken impressive expansions to their fleet and their regional and international destinations.

Earlier this year, the Kenyans signed a deal for 10 Embraer jets from the Brazilian manufacturers at a cost of more than $400m with purchase rights for an additional 16. Kenya is now among Embraer's top 10 customers.

As business and a buoyant regional middle class take to the skies, airlines are increasingly hard-pressed to meet demand.

Kenya Airways has placed orders with Boeing for 24 new aircraft over the next five years and plans to fly to every African capital by the end of 2013. Kenya Airways' pre-tax profit for the first half of 2011 rose 37.7 per cent to KS 2.83bn, thanks to increased passenger and cargo haulage at higher yields.

Its clever fuel price hedging helped to cushion higher oil costs; it has also started calculating prices in dollars to offset losses from the falling shilling.

"Our hedgebook is healthy. We are in the money for up to $30m," says Alex Mbugua, Kenya Airways' finance director. The airline carried 1.8m passengers this year, up 22 per cent on the same period last year.

The Ethiopians have 35 new jets on order, which would increase their fleet to 83 aircraft flying to 62 international destinations.

Flying used to be the preserve of the elite, in the days when African capitals were linked to each other via their old colonial metropolises.

But as government-owned national carriers were privatised to increase their competitiveness, airlines have become ever more innovative in their pricing and route strategies.

While the Rwandans, being government-owned may stand out as the exception, their attitude to East Africa's growing aviation market is no less competitive.

"We are demystifying flying, we want ordinary people to start flying: it's safe and fast," says Mr Mirenge.

Rising cost of a failed neighbour

Somalia

Three EAC members have troops in the country, writes **William Wallis**

Private army: al-Qaeda-linked terrorists operating from Somalia have put the east Africa tourism industry in jeopardy Getty

There is nothing like a common enemy for cementing cross-border ties. In al-Shabaab, the radical Islamist militia in Somalia, and in the Somali pirates hijacking ships along the Indian Ocean coast, east African countries have found two.

Since the 1998 bombing of the US embassies in Nairobi and Dar es Salaam, al-Qaeda-linked terrorists operating from Somalia have put the east Africa tourism industry in jeopardy. Tourism is an important foreign exchange earner in all but one of the five members.

Al-Shabaab militias broadened the threat with the 2010 bombing of Kampala, and have spread throughout the region. This month, Shamsi Vuai Nadodha, Tanzania's home affairs minister, said 10 Tanzanians had been arrested in the Somali capital, Mogadishu, fighting alongside Somali militants.

Meanwhile, Somali pirates have raised the cost of trade across the board, according to Walter Obado-Okok of the Kenya Private Sector Alliance, pushing up insurance premiums, making African products less competitive and, in areas where pirate money is being laundered, such as Nairobi, contributing to higher property prices.

Having a failed state on the doorstep is becoming an increasingly costly affair. The last iteration of the EAC fell apart in 1977 over ideological and political differences, as well as personal rivalries between heads of state. Shortly afterwards, Tanzania, under Julius Nyerere, invaded Uganda, then under dictator Idi Amin, and the two countries went to war.

In 2011, personal rivalries persist. Yet this time round, there is much more that unites the five members on security issues than divides them.

In 2008, the post electoral violence in Kenya came close to suffocating Uganda and Rwanda, whose trade routes were cut off. Both countries played critical roles in negotiating a solution. This year the continued failure of the state in Somalia is at the top of the list.

Richard Sezibera, the secretary-general of the EAC, notes on his prolific blog that the threat posed by Somali terrorists and pirates requires concerted regional action. "These groups co-ordinate their activities. Our response to them should be co-ordinated too," he says.

Kenya has for long pursued a policy of containment in Somalia, but last month sent its troops across the border for the first time, following the abduction of tourists and aid workers on its territory. Three of the five EAC member states now have troops in Somalia – Burundi and Uganda with the African Union mission supporting the weak transitional government in Mogadishu, the capital, and Kenya in the southern half.

Ethiopia, which is not a member of the EAC but is of IGAD, the Horn of Africa bloc, also sent troops in last month in what looks like an increasingly co-ordinated regional effort to crush the Somali militants.

"The key point is that this [Somalia] is a problem that has grown to immense proportions for these states," says David Anderson, professor at Oxford university's African Studies Centre and a Somalia expert.

"It dates from the al-Shabaab bombing of Kampala last year. Since then, the heads of state in IGAD have been concentrating more on how to solve this problem once and for all; led by Museveni who transformed the Amisom [African Union Mission to Somalia] presence from being a defensive to offensive operation," he adds.

The Ugandan president has staked his country's reputation partly on its success in stabilising Somalia. But, says Prof Anderson, he has looked isolated at times as a result. "Having the Kenyans come in plays very well for Uganda."

There is no guarantee for either of success, however.

Past foreign incursions have inflamed Somali nationalism, ended in failure and almost always complicated a conflict that first erupted in 1991 when Siad Barre, the former dictator, was overthrown. The cost of doing nothing, however, has been rising.

"Kenya decided that the risk if it sat and didn't do anything is greater than going in, so it went in," says a senior western official.

Whether the region can afford to pay for a more aggressive military confrontation, or can persuade weary western donors to foot the bill, is another matter.

George Saitoti, Kenya's interior minister, pleaded last week for broader international support.

"Our position is properly calculated in the hope that the international community will come in and form join efforts to stabilise Somalia," he said in an interview in London.

"This is not Kenya's war. This is a big challenge not only for the Horn of Africa and not only for the African Union, but for the whole international community," he added.

It is a test first, however, of the effectiveness of the region in dealing with the problems on its doorstep.

Discerning consumers are attractive prospect

Retail

Supermarket chains are showing an interest, says **Katrina Manson**

Atul Shah: Nakumatt chief

On her regular fortnightly shop in Tanzania's biggest shopping mall, Anita Mtisi disdains Colgate for local-brand toothpaste.

She opts instead for Whitedent, Tanzania's leading make. The bigger tube is cheaper and emblazoned with pictures of a smiling Tanzanian family: all grinning white teeth.

"I like it for the taste and it really helps prevent tooth problems," she says, wheeling two baskets down aisle 11 of the 13 that make up Shoprite, a South African chain that, like many foreign hopefuls, is moving into the region.

Toothpaste, cough syrup, fridges and flatscreen TVs, – East African consumers are purchasing as never before.

The entry of Walmart, the US group, to South Africa this year has sparked interest in a larger growth story.

In a survey published in September, Deloitte notes that, while 90 per cent of sales are generated by the informal market, independent stores and private sellers, fast and sustained growth of formal shopping centres is guaranteed.

The report says: "The middle class is growing . . . [and] will help to underpin demand for high-end consumer goods, including household appliances, automobiles and processed foods," says the report.

Retailers say the patchwork of standards and customs procedures, which regulate everything from import taxes to inspecting cosmetics and checking salt content, prevents products travelling throughout the region freely.

On-the-shelf prices are about 20 per cent higher in the three landlocked EAC members, partly because of non-tariff barriers, which are used in some cases to protect homegrown industries.

But the opportunities are there nonetheless, and east Africa's growing consumer class is drawing attention from private equity funds.

> Among Tanzanian success stories, Whitedent has found its way to South Africa

Whitedent, manufactured by a one of several big Tanzanian family businesses, has received investment from foreign private equity.

UK-based Satya Capital, founded by Mo Ibrahim, the Sudanese telecoms billionaire, last December invested "tens of millions of dollars" into Chemi & Cotex Industries, whose leading product is Whitedent toothpaste.

Justin Abbot, managing partner at Satya, says: "The regional opportunity is the most immediate and important to us; so we want to deliver on that first.

"You are increasingly seeing formal retail come on, especially in the main urban centres, so it's important that we evolve our own distribution strategy to make sure we're fighting and winning there as well – or else we'll lose our brand to others seen as global."

Among the few Tanzanian expansion success stories, Whitedent has found its way to South Africa.

"It's exciting because it shows we can export from what is perceived to be a less developed market to a more developed market," says Mr Abbot, although the brand still relies on small shops and stalls.

Walmart's entry persuaded Woolworths, a South African chain, to pay more attention to its east African franchises, says Ali Mufuruki, minority owner of Woolworths in Uganda and Tanzania, who opened Tanzania's first formal retail outlet in 1999.

Woolworths quickly bought back into a joint venture with Mr Mufuruki and started on a speedy expansion plan, adding three stores this year to its existing four.

Its new Uganda store will be the region's biggest, at 1,500 sq m. Mr Mufuruki says that at the moment Rwandans travel all the way to Kampala to shop and the chain is eyeing Kigali, the Rwandan capital next.

Retail spending is growing at 15 per cent in Tanzania and 18 per cent in Uganda, about three times the figures for growth in gross domestic product.

Mr Mufuruki says: "The perception exists that Africans are poor, don't consume, don't make a distinction between one type of shirt and another because of their dire circumstances. But the mobile telephone revolution has put paid to those views; we see a very discerning African consumer."

Ms Mtisi says: "Even a free gift makes a difference, and even small price differences can attract a customer," having bagged a free toothbrush with her Whitedent purchase.

Imminent entry of Whitedent into shops in Nakumatt, the undisputed leader among supermarket chains in Kenya, may be its greatest coup yet.

The company, which pioneered 24-hour opening and has 3,500 staff, also backs regional products such as Rwandan tea and coffee and has expanded into Uganda, Rwanda and, next month, Tanzania.

In Kenya alone, it sells 1,600 fridges a month, up from 200 10 years ago. Monthly sales for plasma TVs consistently hit 1,300, alongside more than 600 washing machines and freezers.

"People want to be seen shopping in shopping malls; it's aspirational," says Atul Shah, Nakumatt's managing director.