MACROECONOMIC AND SOCIAL DEVELOPMENTS IN EASTERN AFRICA

Changing Gears? Catalysing Economic and Social Recovery
MACROECONOMIC AND SOCIAL DEVELOPMENTS IN EASTERN AFRICA 2023

Changing Gears?
Catalysing Economic and Social Recovery

September 2023
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Introduction
1. INTRODUCTION

Magnified by what has recently been described as a ‘polycrisis’ of the COVID-19 pandemic, supply constraints, Russia’s invasion of Ukraine, soaring inflation and tightening monetary and financial conditions, Eastern Africa is currently confronting multiple economic and social challenges. These external shocks have been made more acute by the longer-term slowdown in the growth of world trade, rising protectionism, the build-up of debt and the worsening climate crisis.¹

This report focuses principally on three macroeconomic economic challenges for Eastern Africa: (i) the high debt burden, (ii) the inflationary pressures, and (iii) insufficiently high growth rates. We argue that resolving these challenges are key issues for the region to achieve both national and international development goals. The report also discusses the dynamics of Eastern Africa trade, and argues that priming regional trade, in the context of AfCFTA implementation, will play an important role in creating a stronger regional economy.

Finally, the report provides a review of performance towards attaining the 2030 SDG goals – noting that the region is seriously lagging behind, particularly in meeting the targets of economic development. Eastern Africa has shown a remarkable ability to withstand the adverse effects of the global economic crises in recent years, according to international and regional benchmarks. However, it is essential to address the macroeconomic challenges that limit the availability of financial resources for vital investments in education, health, infrastructure, and other areas that can help the region achieve its development goals.

¹ Wolf, Martin (2023), “Developing countries have hit the financial rocks”, The Financial Times, 13th June.
The Global Context
2. THE GLOBAL CONTEXT

The challenges confronting eastern Africa need to be put in their proper global context. It is quite clear that in the aftermath of the COVID-19 pandemic, the global economy is going through a period of rebalancing and adjustment. This stems in part from disequilibria that were generated during the response to the 2008-9 global financial crisis – in particular a prolonged period of negative real interest rates. How the developed economies manage the adjustment to this new normal will have a lot of implications for the African continent and Eastern Africa in particular.

We start this section with an overview of some of the most profound structural changes that are currently occurring in the global economy and which have a strong bearing on the global economic environment. It also has relevance to current debates on the future of South-South cooperation, and the efforts by the BRICS nations – Brazil, China, India, Russia, and South Africa (and who in 2024 will be joined by Argentina, Egypt, Ethiopia, Iran, Saudi Arabia, and the United Arab Emirates) – to reduce reliance on the dollar and promote a more multipolar international financial system.²

The first stylized fact to be stressed is the extent to which over the last three decades there has been a gradual shift in economic wealth and dynamism away from high-income countries and towards emerging markets and developing countries. Whereas in the 1980s high-income economies accounted for around 2/3 of global GDP, and the developing world barely 1/3, since the 1990s there has been a gradual change. Growth rates in the developing world began to pick up in the 1990s, and there were some significant reforms in the Asian giants China and India which led to them experiencing a very different growth trajectory compared to the anemic performance in the 1970s and 80s. But the story is a broader one than that. Africa, for instance, experienced what has been called its ‘lost decade’³ in the 1980s, but by the mid-1990s the economic situation started to experience a turnaround, and by the 2000s the African economy was showing renewed dynamism. After the Asian financial crisis of 1997, many Asian economies also displayed extremely strong recoveries. A similar pattern could be observed in the western hemisphere where parts of Latin America started to experience of revival in their economic fortunes after the severity of the debt crisis in the 1980s.

As a consequence, by around the time of the global financial crisis of 2008-9, measured in purchasing power parities terms, (which in theory better reflect the purchasing power of consumers), the emerging and developing economies had already surpassed the industrialized economies in terms of their weight in the global economy. According to IMF projections (Figure 1), these trends will continue until by 2028 we will see an almost complete inversion of the situation seen in 1980, where emerging and developing economies will be responsible for around 2/3 of the global economy and the high-income economies only 1/3.⁴ There has been a similar underlying shift in trends regarding global trade (Figure 2).

1 To this end, for instance, the BRICS nations set up the New Development Bank in 2015 as an alternative to US-dominated financial institutions such as the IMF and World Bank. The NDB has lent $33bn for infrastructure and sustainable development projects and has incorporated non-BRICS nations Egypt, Bangladesh and the United Arab Emirates as additional members, with Uruguay in the final stages of admission. It is to begin lending in the South African and Brazilian currencies soon. See Stott (2023).


3 Note that this narrative also holds if we measure the global economy at market exchange rates rather than at purchasing power parities which better reflects the consumption power of the different regions. The shift has however been less pronounced – but even still the developing world is already about on par in terms of its economic size.
These new dynamics in the shape and form of the global economy require a different approach to development policy, particularly with regards to strategic engagement with other developing economies.

There is a further fundamental aspect to this shift in wealth. And that pertains to the changes in the patterns of global debt. During the 1980s and 90s, only developing countries’ debt was seen as deeply problematic. But over the last twenty years, we have been witnessing a steady increase in rich countries’ indebtedness (Figure 3). As pointed out in a recent UN report, over 70% of global public debt is now accounted for by high-income economies, and less than 30% is in the hands of developing economies (Figure 4). Average debt levels in high-income countries are significantly higher than for developing countries. The challenge for developing economies is that the interest payments that they pay on this debt are much higher than it is for wealthier ones. So, for example, whereas Germany pays just 1.5% interest on government bonds, for the African continent the average is around 11%. These inequities in the global financial system are leading to increasing calls for reform. The Economic Commission for Africa has been among the institutions advocating for a fundamental rethink in the global financial architecture.

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6 UN Global Crisis Response Group (2023), “A World of Debt”.
The key question for the global economy is how it will adjust to this new situation of trying to manage global debt. In the aftermath of the global financial crisis of 2000 and eight 2009, high-income economies reacted by reducing interest rates to historically low levels, to such an extent that real interest rates were negative (that is to say, the capital was extraordinarily cheap for market actors). This led to speculative bubbles in equity markets and many other asset classes (e.g. real estate, commodities, etc.). This was all sustainable at a time when global inflation was extremely low. But because the COVID-19 pandemic further pushed global debt levels beyond sustainable limits, and because inflation made a sudden (and largely unexpected) return in developing and developed economies alike, monetary authorities globally had to take a new stance towards monetary tightening. We are thus witnessing the winding down of a monetary policy that was intended to be a temporary one to tackle the global financial crisis but has now led to a situation whereby debt levels are unsustainable in both developing and developed economies. Indeed, to some extent, global inflationary pressures are symptomatic of the inability of governments to either raise taxes or reduce public spending. Inflation assists governments in managing difficult debt situations in the sense that it acts like a tax on the general population and reduces debt-to-GDP ratios to more manageable levels.⁸

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How the high-income countries decide to tackle these challenges and rebalance the global economy will have a lot of implications for the African economies. Debt levels in Eastern Africa, broadly speaking, are in no way comparable to the debt to GDP levels that are prevalent in high-income countries at the moment, but their capacity to pay those higher interest rates is also much more limited. And their fiscal situations are being compromised by the decisions of high-income economies. For instance, according to the Kenyan Treasury, recent aggressive interest rate increases by central banks in high-income countries, together with the sustained weakening of the Kenyan shilling, have resulted in Kenya having to pay 7.5% more in foreign debt repayments, leaving less cash for building roads and affordable housing units, revamping of the ailing health sector and putting up power plants for cheap electricity — all of which are key for industrial development and job creation. Most countries in Eastern Africa also struggle with large merchandise trade deficits and consequently also sustain large current accounting balances. This makes it much more difficult for them to mobilize the necessary financial resources to make interest payments and returns on the principal of their debt holdings.

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Kenya has had to pay 7.5% more in foreign debt payments in 2023, as a result of a weakened shilling and aggressive interest rate hikes by high income economies.

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Macroeconomic Considerations
3. MACROECONOMIC CONSIDERATIONS

3.1 Regional Growth Performance

Collectively, Eastern African grew at a slower pace during the COVID 19 pandemic, with the GDP growth declining from a very buoyant 6.3% in 2019 to just 1.7% in 2020. Though this represents a 4.5 percentage point drop, the region did avoid the recession observed in the rest of the continent and around the world (Table 1). This reveals a degree of economic resilience, although the outcome is relatively heterogeneous between member states (Table 1), with eight of the 14 countries in the region experiencing an economic contraction in 2020. During the subsequent period of economic recovery, several economies have displayed remarkable dynamism. The Democratic Republic of Congo – one of the poorest countries in Eastern Africa in per capita terms – benefited from strong demand and high prices for its commodity exports. Its economy grew at 6.2 and 8.9% in 2021-22, respectively. The Seychelles’ economy bounced back after suffering the largest economic contraction in the region in 2020, and only a shaky recovery in 2021, to become the second fastest growing country in the region in 2022, on the back of a robust revival of its tourism sector. Rwanda’s economic performance was also very strong, based principally on the recovery of its service sector. In Ethiopia – the region’s largest economy – reconstruction after two years of conflict are helping sustain growth, boosted also by a process of economic liberalization which is attracting more private investment in crucial sectors (notably mining, retail, banking, and telecommunications). Nonetheless, growth remains below government targets of more than 9% owing to instability.

At the regional level, in 2021, growth recovered to 6.0%, but declined marginally in 2022 to 5.6%, because of both fiscal pressures and the poor performance in agriculture due to adverse climatic conditions. Our regional estimates for 2023 and 2024, based on national and AfDB forecasts, foresees a modest improvement in growth for 2023 and 2024, to 5.8% and 6.2% respectively. But this is contingent on no further dramatic negative developments in the global economy (for instance, a sharp deceleration in Chinese economic growth or an escalation in the Russia-Ukraine war), as well as avoiding a deterioration in peace and security and an improvement in climatic conditions within the region.

In the midst of the pandemic, Rwanda’s service sector exports had collapsed by -62% in 2020, but the rebound was impressive (26 and 98% growth, respectively, in 2021 and 2022). See WTO (2023) “World Trade Statistical Review 2023” Table A13.
### Table 1: Real GDP growth (%)

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Note: *Ethiopia and Uganda use fiscal year data, *Eritrea data is from AfDB East Africa Economic Outlook 2023

** Weighted Average for Eastern Africa.

Quarterly GDP data is available for five countries in the Eastern Africa region (Figure 5). This provides a more granular view of the trends with regards to economic growth in the region. Although two of the region’s smaller economies (Rwanda and the Seychelles) have experienced very high rates of economic recovery and expansion, one area of concern is this significant slowing down of growth in one of the region’s largest economies. Kenya’s GDP expanded by 4.8 per cent in 2022 compared to a revised growth of 7.6 per cent in 2021. The lower growth was due principally to the poor performance of agriculture, forestry, and fishing, which contracted by 1.6 per cent in 2022, attributable to drought conditions. Although the economy improved its performance from the last quarter of 2022, posting 5.3% in the first quarter of 2023, civil disruptions in the second and third quarters of 2023 mean that growth for the whole year is likely to be more subdued. More generally, it is evident that the three largest economies (Kenya, Uganda and Tanzania) of the East Africa Community, while growing at respectable rates of growth, are not enjoying the same dynamism that they did prior to the pandemic. A tightening fiscal situation is one of the explanatory factors. It is to this point that we will now turn.

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3.2 Regional Debt Dynamics

The global COVID-19 pandemic provoked a serious deterioration in public finances in eastern Africa, as fiscal revenues dried up, and spending commitments – especially payments to mitigate the impact of the pandemic rose. This resulted in a situation where fiscal deficits grew significantly while debt levels increased to an extent which had not been seen since the early 2000s. Of all 14 countries in Eastern Africa, four countries now have a debt to GDP ratios over 60% (Burundi, Kenya, Rwanda, and Seychelles) – above the level that is considered prudent under the debt sustainability framework. That said, there are some reasons for cautious optimism with regards to the trends going forward.

Firstly, there was some improvement in debt-to-GDP ratios in 2022, due to the uptick in economic growth since 2021 and the recovery in revenues. Secondly, the high inflation that the region started to experience from mid-2022 onwards contributed to a modest decline in debt-to-GDP ratios, because of the higher nominal value of GDP. Indeed, as was mentioned in Section 2, higher inflationary pressures can partially be seen as a consequence of higher levels of indebtedness at the global level – if governments are either unable or unwilling to sharply reduce spending, or unable to raise taxes, the result is often a laxer monetary policy. Put simply, inflation acts as a broad tax that helps the government postpone difficult spending decisions. A final point to bear in mind is the differential cost of the debt depending on its composition. In Kenya, for example, there is a higher share of non-concessional debt given its status as a lower middle-income country. Its repayments are correspondingly higher.\(^\text{12}\) By contrast, a country like Rwanda has a much higher share of concessional financing and, as a consequence, the burden of the debt as a percentage of GDP is significantly lower.

Nonetheless, it is important not to underplay the economic impact of the debt burden on regional economies. The last time Eastern Africa saw debt-to-GDP ratios as high as they are

\(^{12}\) In fact, in July 2023, for the first time in recent years Kenya’s debt repayment costs exceeded revenue from taxes and fees on services, with the Treasury spending nearly Ksh161.8 billion ($1.12 billion) on monthly debt repayments, surpassing Ksh156.9 billion ($1.08 billion) receipts from taxes and non-tax revenue from state services. See Business Daily “Debt expenses surpass Kenya’s ordinary revenue flows”, Wednesday 23rd August.
Currently was in the early 2000s. A large-scale international initiative – the HIPIC initiative\(^\text{13}\) – was required to turn things around. At present, although several countries have benefited from the enlargement of special drawing rights, and some have been included in the new G20 initiatives to support highly indebted poor countries, this does not yet amount to anything as bold as the previous HIPIC initiative. Moreover, in the face of the strength of the US dollar, debt burdens continue to impose significant strains on government finance.

For instance, Ethiopia was one of the beneficiaries of the Debt Sustainability Initiative (DSSI) announced by the G-20 in May 2020, in the midst of the global pandemic, to temporarily pause official debt repayments of the poorest countries. Under the agreement, Ethiopia received a $800mn payment holiday. However, the fall of the Ethiopian birr over the course of 2020-22 increased the effective burden of debts by 35 per cent – in US dollar terms that was equivalent to an increase in the debt stock of an estimated $9.7bn\(^\text{14}\), thereby completely overshadowing any benefits from the DSSI. Cases like these illustrate the need for some fundamental rethinking of the global financial architecture to bring down the costs of borrowing for developing countries.\(^\text{15}\)

One consequence of the high levels of debt has been the gradual tightening of monetary policy in the region, a trend which has been reinforced by the need to reduce inflationary pressures (Figure 8). Since 2021, Rwanda has raised its base rate by 3% and Kenya by 2.5%. Uganda did recently (in August 2023) implement a 0.5% reduction in its base rate, bringing its monetary policy rate to be on par with Kenya. Surprisingly perhaps, given that its debt situation and fiscal deficit are much more modest, the Democratic Republic of Congo has increased its rates the most. The effectiveness of monetary policy tightening in the case of small low-income economies is in any case debatable – with significant dollarization of the economy, and mostly large current account deficits, the ability of governments to directly influence changes in prices or to finance the bulk of its debt through the issuing of domestic debt is perhaps questionable.\(^\text{16}\)

\(^{13}\) The IMF and World Bank launched the Heavily Indebted Poor Countries (HIPC) Initiative in 1996 to ensure that no poor country faces an unmanageable debt burden. See IMF (2023). “Fact Sheet – Debt Relief under the Heavily Indebted Poor Countries (HIPC) initiative.”


\(^{16}\) The link between monetary policy instruments and aggregate demand – the monetary transmission mechanism – may be significantly weaker in low-income countries than it is in advanced and emerging economies. Weak and unreliable monetary transmission would suggest restraint in the use of monetary policy, implying that placing primary responsibility for domestic macroeconomic stabilization on central banks may be misguided. After reviewing the relevant studies, Mishra and Montiel (2012) conclude that “It is very hard to come away from this review of the evidence with much confidence in the strength of monetary transmission in low-income countries.”
**Figure 6: Cost of debt (% of GDP), 2021**

![Cost of debt chart](source)

**Figure 7: Debt and Fiscal Imbalances (% of GDP), 2022**

![Debt and Fiscal Imbalances chart](source)

**Figure 8: Base Point Changes in Monetary Policy Rates in Eastern Africa, 2021-2023**

![Base Point Changes chart](source)

In August 2023, Uganda implemented a 0.5% reduce in its base rate, bringing its monetary policy rate to be on par with Kenya.
Adapting to a more inflationary environment
4. ADAPTING TO A MORE INFLATIONARY ENVIRONMENT

4.1 Regional Inflationary Trends

It is well recognized that the global inflationary environment has been an important factor in terms of generating inflationary pressures in Eastern Africa. However, as revealed by Figure 9, there has been a large heterogeneity in regional inflationary trends over the past year and a half. Ethiopia is clearly the most affected economy in the region in terms of persistently rising prices, but both Burundi and Rwanda have also suffered high inflationary experiencing peaks in the latter part of 2022 and early 2023.

Figure 9: A large heterogeneity in regional inflation trends, Consumer Price Indexes, (Year-on-Year, January 2022 – June 2023)

Source: UNECA elaborated from national sources
The good news is that inflation seems to have peaked in the third quarter of 2023 and has been coming down markedly in most economies. Part of this decline is attributable to lower fuel import bills – although, in the face of recent announcements by Saudi Arabia of significant cutbacks in oil production, the reprieve may be temporary. At the other extreme, we have Seychelles, which since April has been experiencing deflation rather than inflation – something that could also be cause for concern given the high indebtedness of the Seychellois economy.

Given this heterogeneity in regional inflation, it is reasonable to assume that imported inflation is only part of the story, and there are several local or regional drivers of higher inflation that take precedence over global inflation. Particularly worrying is the way that inflationary trends have been driven by food price inflation. This has had a deleterious effect on real incomes in the region, especially as wages have generally been slow to respond. The other key factor to consider is the erratic nature of regional food production which has been hit hard by extreme climatic events. This has been perhaps the overriding explanatory factor with regards to high food prices. It has been seen in countries such as Burundi, Ethiopia, Kenya, Rwanda, and Somalia, although the high price of imported foodstuffs and agricultural inputs have also been major contributory factors, especially for the more heavily food import-dependent countries in Eastern Africa. We now turn to a discussion of global food and commodity prices.

4.2 The Ambiguous Impact of Commodity Prices Shifts

Global commodity prices initially declined in the initial stages of the COVID-19 pandemic as lockdowns were imposed across the globe and aggregate demand fell precipitously. However, that began to change in early 2021 with the gradual lifting of restrictions on movement and the pickup of the economic recovery. Global commodity prices then suffered a new shock in the form of the start of the Ukrainian-Russian conflict in March 2022. This immediately led to a spike in global commodity prices, particularly in fuel, fertilizer prices, and food. Nevertheless, by August 2022 the IMF’s all commodity price index peaked. Thereafter, there were some marked falls in commodity prices, led by declines in fuel prices (Figure 10). On a year-on-year basis, maize and wheat prices are 15 percent and 17 percent lower, while rice prices are 16 percent higher. With growing evidence of a sharp contraction in economic growth in China\(^{27}\), commodity prices (particularly for minerals) are likely to fall further.

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The implications of all this for the Eastern African region are complex. As has been pointed out in earlier reports, Eastern Africa is not one of the most resource rich parts of the African continent, and the majority of countries are net commodity importers – that is to say, they import in value terms more commodities than they export. Fuel and fertilizer imports, as economic inputs, have had an especially deleterious impact on supply chains and resulted in significantly higher prices in agriculture and other sectors that use these inputs intensively.

On the other hand, various countries in the region are among the major exporters of tropical beverages (tea, coffee). Prices for these commodities have been very strong since early 2022 and from a macroeconomic perspective, this has given the main exporters some reprieve from the higher import bills. Finally, several countries in the region are exporters of precious metals – particularly the Democratic Republic of Congo of course but also countries such as Eritrea, Rwanda, Tanzania, and Uganda. These countries experienced a boom in revenues in 2021, although prices stabilized in 2022. Despite encouraging evidence that food price rises are beginning to subside (Figure 11), there is an important consideration regarding the extent to which global falls in price are not necessarily being passed on to consumers. Analysis by UNCTAD shows the extent to which high food prices have led to a surge in earnings for food traders (Figure 12).

Figure 10: Global Commodity Price Indexes (Jan-2019=100)

Source: IMF Primary Commodity Prices (2023)

18 For instance, on a year-on-year basis, by the end of July 2023 maize and wheat prices were 15 percent and 17 percent lower. Conversely, rice prices were 16 percent higher, due largely to the announcement on July 19th by the government of India to impose an export ban on non-basmati rice. India accounts for nearly 40 percent of the global rice market (World Bank, 2023).

There are rising concerns that, just as in the oil markets, there is stickiness in the reaction of market operators to price changes – upward shifts in global prices are quickly reflected in market prices, but downwards shifts are not. This is not purely of international concern. For example, in April 2023 the Rwandan Ministry of Trade MINICOM imposed some price caps on maize flour, rice and irish potatoes, having established the market traders were not transmitting price reductions in international markets into lower prices for consumers.

One consequence of this is that food import bills have risen dramatically since prior to the pandemic. Among the worst affected countries are Ethiopia and Kenya, both of which now have a food import bill in excess of $3 billion in 2022, up by 99 and 55% respectively. There is a need for concerted policy action to tackle these deficits through both improved national food production and greater intra-regional trade in foodstuffs. Building greater resilience to extreme climatic events is also clearly a priority. An associated paper (SRO-EA, 2023) to this report explores the issues related to this topic.

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In April 2023, Rwanda imposed some price caps on maize flour, rice and potatoes.
Among the most affected countries are Ethiopia and Kenya, both of which now have a food import bill in excess of $3 billion in 2022, up by 99 and 55% respectively.

### Figure 13: Regional Imports of Food have Risen Sharply (imports in billions of USD)

<table>
<thead>
<tr>
<th>Country</th>
<th>Imports 2022</th>
<th>% Change since 2019</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ethiopia</td>
<td>3,660</td>
<td>99</td>
</tr>
<tr>
<td>Rwanda</td>
<td>686</td>
<td>85</td>
</tr>
<tr>
<td>Tanzania</td>
<td>1,092</td>
<td>74</td>
</tr>
<tr>
<td>South Sudan</td>
<td>334</td>
<td>68</td>
</tr>
<tr>
<td>Dem. Rep. Congo</td>
<td>1,712</td>
<td>63</td>
</tr>
<tr>
<td>Madagascar</td>
<td>923</td>
<td>59</td>
</tr>
<tr>
<td>Kenya</td>
<td>3,275</td>
<td>55</td>
</tr>
<tr>
<td>Djibouti</td>
<td>1,063</td>
<td>49</td>
</tr>
<tr>
<td>Burundi</td>
<td>164</td>
<td>32</td>
</tr>
<tr>
<td>Uganda</td>
<td>952</td>
<td>30</td>
</tr>
<tr>
<td>Eritrea</td>
<td>558</td>
<td>29</td>
</tr>
<tr>
<td>Somalia</td>
<td>474</td>
<td>28</td>
</tr>
<tr>
<td>Seychelles</td>
<td>222</td>
<td>19</td>
</tr>
<tr>
<td>Comoros</td>
<td>78</td>
<td>4</td>
</tr>
<tr>
<td>Eastern Africa 14</td>
<td>15,192</td>
<td>62</td>
</tr>
</tbody>
</table>

Source: Computed from UNCTADStat (2023)
5. TRADE DEVELOPMENTS

5.1 The Recovery of Regional Trade – Is it Sustainable?

At the time the Covid-19 pandemic hit, concerns were raised about the extent of the hit to commerce, with many analysts predicting an unprecedented fall in global trade. The World Trade Organization estimated that global trade would fall between -13 and -32% because of the disruptions caused to normal economic activity. In the end, the result was a more modest reduction of -8% for merchandise (-18% for commercial services), and the subsequent recovery entailed a 27% expansion in merchandise trade in 2021, and 14% in 2022. Although the impact of services trade was profound, East Africa avoided the worst of the merchandise trade impacts, with a slight (1%) increase in aggregate exports if we exclude the Democratic Republic of Congo (DRC). The crisis was mainly felt through imports, which declined by 10%, with the consequence that trade imbalances in the region generally improved, despite the severity of the global economic shock.

The subsequent rebound in exports in 2021, was strong – a 34% increase – principally due to strong demand for the region’s commodity exports and higher prices for cash crops, such as tea and coffee. However, the recovery looks less impressive (a 15% increase) if we exclude DRC – the region’s largest commodity exporter (Figure 14). Thereafter, trade performance was more subdued in 2022. Looking forward, tentative estimates for 2023, based on the performance of the first 4 months, suggest that softening commodity prices and falling demand from China will adversely impact DRC’s export performance, but for the rest of the region, growth should remain robust. Import growth was strong in 2021 and 2022 after the marked decline (of -10%) in 2020. But preliminary results for the first four months of 2023 suggest some moderation.

Figure 14: Regional Trade Performance 2020-2023* (% Change)

*Calculations for 2023 based on the data for the first trimester of 2023 (Jan-April)
Source: UNCTADStat (2023) for data from 2020-2022, and IMF DoTs (2023) for 2023.

With regard to the trade performance of individual countries, the island states of Comoros, Madagascar, and Seychelles experienced robust export growth in 2022 (although the absolute magnitudes are very modest in the case of Comoros). The Democratic Republic of Congo saw a much lower rate of growth in its exports in 2022 vis-à-vis 2021, as demand faltered for some of its major commodity exports. Nonetheless, it remains the region’s largest exporter, responsible to 43% of Eastern Africa’s total exports. Ethiopia’s export performance was negatively affected by civil unrest and the conflict.

**Figure 15: Change in Export values, 2021 and 2022 (% from previous year)**

A recent paper posited that trade within trade agreements was relatively more resilient against the global trade collapse of 2020 (Nicita and Saygili, 2021). Intra-regional trade figures for the EAC-6 member states certainly lend credence to that narrative, with intra-EAC exports surpassing, for the first time, USD 5 billion in 2022 (Figure 16). After a lull in intra-EAC trade between 2016 and 2019, intra-regional trade has experienced three years of robust growth, taking the share of intra-regional trade in total trade to 24% – making the EAC the most integrated economic bloc (in trade terms) on the continent.

The island states of Comoros, Madagascar, and Seychelles experienced robust export growth in 2022.

After a lull in intra-EAC trade between 2016 and 2019, intra-regional trade has experienced three years of robust growth, taking the share of intra-regional trade to 24%.

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Interestingly, the revival in intra-EAC trade has been led by the three larger economies, with a particularly notable rise in exports from Tanzania, after nearly a decade of relative stagnation. Uganda too has been taking advantage of opportunities to expand its exports to its EAC partners, to such an extent that both Tanzania and Uganda are on course to surpass Kenya in the next few years as the leading regional trading partner. However, Non-Tariff Barriers continue to pose serious problems to intra-EAC trade, and there have even recently been some (erroneous) reports that intra-EAC trade is down. But the general direction of travel is positive, especially against the backdrop of the AfCFTA. It is to that topic that we now turn.

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A report entitled ‘The Intra-EAC Trade Brief Analysis’ by the East African Business Council (EABC) claimed that the value of trade among the EAC members states fell by more than 33% to $3.6 billion in 2022 (see Anyanzwa and Anami, 2023). But these figures do not align with official EAC figures nor with the data from international databases (IMF DoTs and UNCTADStat).
5.2 The need to Double Down on the AfCFTA

In a recent book, David Luke, former director of ECA’s African Trade Policy Centre, claimed that

“The ignition of the AfCFTA project is stutter-starting. Several ‘launch’ attempts and an increasing breadth of complementary projects, tools, and initiatives within the growing AfCFTA ecosystem conceal the fact that trade is yet to substantively flow under the arrangement. The Guided Trade Initiative is to be welcomed as a gateway for formal trade under the AfCFTA but is not a substitute. The real risk of this is to the remarkable political momentum behind the AfCFTA, which, having weathered the Covid-19 storm, remains strong.”

While this may be exaggerating the situation, it is certainly true that there is a need to accelerate the implementation of the AfCFTA. This would logically start with respecting the tariff reduction schedules that have already been agreed to and start applying the tariff reductions on intra-African imports. There have been some complaints that the private sector is not seizing the moment. But until tariffs are reduced and market access granted as per the protocols, there will be no new opportunities to seize. In the first instance, it is first incumbent on governments to act. One way forward suggested by Luke and colleagues is the importance of regional ‘hegemons’ to lead in unlocking progress. In their regional economic communities, economic powers such as Kenya and South Africa could undertake liberalisation more rapidly or fully than their neighbours, emphasising their leadership roles and corresponding responsibilities. There are interesting precedents for this. For instance, Kenya immediately allowed duty-free

There is a need to accelerate the implementation of the AfCFTA. This would logically start with respecting the tariff reduction schedules.

There have been some complaints that the private sector is not seizing the moment. But until tariffs are reduced and market access granted as per the protocols, there will be no new opportunities to seize.
imports into its market from its neighbours when the East African Community customs union was established in 2005 while permitting its own exports to be progressively liberalised over a longer five-year period: “If Africa’s regional powers could again show greater leadership, creativity and ultimately compromise in realising the start of trade under the AfCFTA, it could help to generate the momentum needed to get trade flowing across and transforming the continent.”

The argument is compelling but could be extended more widely. Figure 18 shows the net trading position (i.e. exports minus imports) in 2022 for all 14 individual East African countries within the continent. While it can be appreciated that Kenya enjoys a large positive trade balance with the continent (879 million USD), it is eclipsed by the very large positive trade balances of both the Democratic Republic of Congo and Tanzania (3.9 and 2.3 billion USD, respectively). Ethiopia and Uganda also enjoy significant positive trade balances with the rest of the continent. It is in the interest of jump-starting the implementation of the agreement that all these countries rapidly and aggressively reduce their tariff and non-tariff barriers. Only in that way will the new market opportunities conferred by the AfCFTA materialize.

AfCFTA implementation also needs to catalyse policies to ‘recapture’ domestic and regional levels. Import penetration in multiple sectors is very high, and there is plenty of scope, once the tariff reductions are implemented, to compete more effectively with imports from outside the continent. From an export perspective, one interesting dimension of AfCFTA implementation is the extent to which the African market is already more strategically important than the global ones. A way to illustrate this is by computing the ‘regional orientation index’, which takes a value of 1 or above when the continental market takes precedence over international markets and less than 1 when the international market is most important (Figure 19).

It is in the interest of jump-starting AfCFTA implementation that countries rapidly and aggressively reduce their tariff and non-tariff barriers. Only in that way will the new market opportunities materialize.

Figure 18: Intra-African Trade Balance of Eastern African Countries, 2022 (mlns USD)

<table>
<thead>
<tr>
<th>Country</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td>DRC</td>
<td>3,906</td>
</tr>
<tr>
<td>Tanzania</td>
<td>2,354</td>
</tr>
<tr>
<td>Kenya</td>
<td>879</td>
</tr>
<tr>
<td>Ethiopia</td>
<td>663</td>
</tr>
<tr>
<td>Uganda</td>
<td>525</td>
</tr>
<tr>
<td>Djibouti</td>
<td>122</td>
</tr>
<tr>
<td>Comoros</td>
<td>-14</td>
</tr>
<tr>
<td>Eritrea</td>
<td>-29</td>
</tr>
<tr>
<td>Seychelles</td>
<td>-123</td>
</tr>
<tr>
<td>Somalia</td>
<td>-265</td>
</tr>
<tr>
<td>Burundi</td>
<td>-292</td>
</tr>
<tr>
<td>Madagascar</td>
<td>-345</td>
</tr>
<tr>
<td>Rwanda</td>
<td>-353</td>
</tr>
<tr>
<td>South Sudan</td>
<td>-920</td>
</tr>
</tbody>
</table>

Source: ECA Calculations from UNCTADStat (2023)

27 The regional orientation index thus tells us whether exports of a particular product from the region under study to a given destination are greater than exports of the same product to other destinations. In other words, it measures the importance of intra-regional exports relative to extra-regional exports. See UNESCAP (undated).
The data are broken down using the classic Lall (2000)\(^{28}\) sectoral classification reflecting the difference between high, medium, and low technology manufactures. The results are quite striking in the sense that the dependence on the African market is readily apparent not only for low technology manufactures but also for medium and high technology manufactures. Indeed, the only sectors where the extra-African markets are more decisive are for the automobile sector, textiles, garment and footwear, and, unsurprisingly, primary products. It is clear therefore that if African countries wish to accelerate their economic diversification, it is best to do this through expanding their exports further towards the continental market, rather than ploughing the furrow of commodity exports to international markets.

Progress towards the Achievement of Developmental Goals
6. PROGRESS TOWARDS THE ACHIEVEMENT OF DEVELOPMENTAL GOALS

In past editions of this report, we have documented the marked improvements in various dimensions of human development in Eastern Africa over the last two decades, such as the sharp improvement in life expectancy and the massive roll out of educational opportunities at the primary level. Nonetheless, it is clear that both social progress and economic development of the whole of the African continent has been negatively impacted by the polycrises referred to at the beginning of this report. According to the World Bank’s recent Global Economic Prospects Report, by the end of 2024, economic activity in developing economies is expected to be about 5% below levels projected on the eve of the pandemic. In low-income countries—especially the poorest—the damage is stark: in more than one-third of these countries, per capita incomes in 2024 will still be below 2019 levels. As the World Bank report notes, “this feeble pace of income growth will entrench extreme poverty in many low-income countries.”

It is not just a question of economic growth, however – it is also how the burden of adjustment is being shared. It is reasonable to assume, with their heavy dependence on wage labour, that the inflationary bout has eroded real incomes of the poor much more than in the higher quintile groups. In the final section of this report, we will give some consideration to how these trends are impacting on the achievement of the SDGs, and whether the return of higher levels of economic growth, which are ultimately a condition sin qua non for achieving higher per capita incomes and the ability to mobilise the resources necessary to meet the region’s developmental challenges, will be sustainable.

6.1 Tracking Progress towards the SDGs

Before the COVID-19 pandemic, as noted in previous editions of this report (ECA, 2023), efforts to achieve the SDGs in the continent were improving. However, COVID-19 and other global crises slowed African countries’ progress toward the development targets. Figure 20 shows the progress made towards the SDG targets as of May 2023. Out of a total of 169 targets, data is available for 104.

Eastern Africa demonstrates varying degrees of achievement across the 17 SDG targets. What stands out, however, is the fact that only 6 of those targets are on track, reflecting advancements in just 5 SDG targets (partnerships, life on land, life underwater, clean energy, and sustainable cities). Most worryingly, 81 targets are off track, and 17 targets have even regressed, with a particular cluster of poor performance around Goal 8 (decent work and economic growth), and SDG 9 (infrastructure). Reverses are evident in the inability to achieve sufficiently rapid GDP growth (Target 8.1), economic diversification, technological advancement, and support for SMEs (Targets 8.2 and 8.3). Targets 9.1, 9.3, and 9.4 have also been going in the wrong direction.

In Africa, an ILO (November 2022) study suggests that there was a fall in real wages of -1.4 per cent in 2021 and -0.5 per cent in the first half of 2022. But this misses out the acceleration of inflation in the latter part of 2022.

Target 8.1 specifies a target growth rate of at least 7 per cent GDP per annum in the least developed countries (UNStats, 2023).
direction in terms of the lack of quality infrastructure, the failure to enhance financial access and integration of small-scale enterprises into value chains, and insufficient efforts to adopt environmentally sound technologies in infrastructure and industry.

How can this situation be turned around? The current macroeconomic situation described earlier certainly leaves a smaller room for manoeuvre for regional government in terms of increasing public spending. Nonetheless, a recent book by Bjorn Lomberg (2022) identifies a number of straightforward and effective measures that could be adopted to tackle some of the challenges and address the backsliding in some regional SDG targets. For instance, many chronic health issues and educational gaps already have cost-effective remedies. To cite one example, malaria continues to be a major cause of mortality among children in Eastern Africa. Yet technological innovations are making new treatments available. The first malaria vaccine was recommended for use to prevent malaria in children in October 2021. More than 1.4 million children have since received at least their first dose the vaccine across the 3 pilot countries (Ghana, Kenya, and Malawi), including 400 000 children in Kenya. If implemented broadly, it is believed that the vaccine could save tens of thousands of lives each year. The vaccine has been shown to be safe and effective, reducing life-threatening severe malaria and child deaths (WHO, 2023).
Above all, however, it seems to be in the economic domain where progress has been backsliding the most. Policy innovations to improve agricultural performance – still the mainstay of the poorest Eastern African economies – are important, particularly in light of rising food insecurity. It is projected that up to 60 million people in Eastern African will be food insecure by January 2024: the projected hotspots are Ethiopia (10 million people), Democratic Republic of the Congo (10 million), South Sudan (8 million), Somalia (6 million), and Kenya (5 million). Somalia and South Sudan continue to be at risk of famine. In South Sudan, more than 60 percent of the population are estimated to be acutely food insecure. Some governments in the region are taking decisive measures to deal with these challenges. Tanzania, for instance, has massively increased its budget from $126.7 million in 2020/2021 to $629.31 million in 2022/23, as the government seeks to increase food production for both domestic and export markets and as protection against the vagaries of the weather. But how increased budgetary allocations are made will be key in terms of effectiveness – Lomberg (op. cit.), for instance, claims that greater investments in agricultural R&D are the surest way of improving crop yields, lowering food prices and reducing hunger.

More generally, Mold (2023) argues that there is a need to shift more investment in East Africa towards sectors capable of inducing technological change and productivity growth, rather than ‘safe’ investments in real estate, the banking sector, or the hospitality sectors which involve very little ‘learning’, in the broadest sense. Without ignoring the important contribution of certain sub-sectors of services, this generally implies a renewal of efforts to revive the manufacturing and industrial sectors – which have historically been connected with technological spillovers and faster productivity growth. Ultimately, to achieve the SDG goals, it is important that there is a resumption of strong economic growth in the region. To this point we will now turn.

### 6.2 Is the Bounce-Back in Economic Growth Sustainable?

Mckinsey Global Institute (MGI) has produced a number of influential publications on the prospects for the African economy, starting with its 2010 report, “Lions on the Move: The Progress and Potential of African Economies”. In a recently released report entitled ‘Reimagining Economic Growth in Africa’, MGI notes that while there has been a dramatic turnaround in economic growth on the continent since the 2000s, the rate of economic growth declined in the 2010s. From the perspective of Eastern Africa, the report nonetheless has the encouraging finding that most countries in the region are classified as ‘consistent growers’ (Figure 20).

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32 World Bank (July 2023), Food Security Update, 27th July
34 At a global level, Lomborg reports research suggesting that spending $74 billion in agricultural R&D will make farmers and consumers $2.5 trillion better off while reducing the number of malnourished by more than 130 million by 2030. See Lomborg, op. cit., p. 124).
Over the past 20 years, consistent growers have had above-average growth in urbanization, in levels of capital investment and exports, albeit off a low base. They also have had steady growth in per capita consumption, 3% annually on average. Ethiopia, the largest of the consistent growers, stands out for reducing the number of people living in absolute poverty by 30 million out of a total population of 115 million over the 2010–19 decade. Rwanda, the second-fastest-growing economy during that period, experienced significantly high GDP per capita growth of 4.6 percent, compared with 0.4% on the continent overall. While this is encouraging, it is important to stress that the majority of Eastern African countries – 9 of the 14 – are still low-income economies, according to the classification of the World Bank. This would suggest that even once high growth has been achieved, it is difficult to ‘graduate’ from low-income status (Table 2).

**Figure 21: ‘Consistent Growers’, according to MCI, 2023**

Three countries in Eastern Africa are candidates to move soon to lower-middle income status – Rwanda, Ethiopia, and Uganda.

This drives home the importance of sustaining rapid economic growth going forward. ECA simulations suggest that, under the prevailing circumstances, three countries in Eastern Africa are candidates to move to lower-middle income status – Rwanda, Ethiopia, and Uganda. The first to graduate will be Ethiopia which, according to our modelled data, should surpass the threshold of 1086 USD this year (2023). The second Eastern African country to attain lower-middle-income status will probably be Rwanda which, on current trends, should surpass the threshold in 2025 (although could foreseeably attain the target as early as 2024). Finally, Uganda is on target to reach middle-income status by 2027, although it might be feasible on current growth trajectories as early as 2025.

Table 2: Moving from low-income to middle-income status is hard...

<table>
<thead>
<tr>
<th>Country Code</th>
<th>Country Name</th>
<th>GNI $ Per Capita</th>
<th>Classification</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Burundi</td>
<td>240</td>
<td>Low-Income</td>
</tr>
<tr>
<td></td>
<td>Congo, Dem. Rep.</td>
<td>590</td>
<td>Low-Income</td>
</tr>
<tr>
<td></td>
<td>Comoros</td>
<td>1,610</td>
<td>Lower-Middle Income</td>
</tr>
<tr>
<td></td>
<td>Djibouti</td>
<td>3,180</td>
<td>Lower-Middle Income</td>
</tr>
<tr>
<td></td>
<td>Eritrea</td>
<td></td>
<td>Low-Income</td>
</tr>
<tr>
<td></td>
<td>Ethiopia</td>
<td>1,020</td>
<td>Low-Income</td>
</tr>
<tr>
<td></td>
<td>Kenya</td>
<td>2,170</td>
<td>Lower-Middle Income</td>
</tr>
<tr>
<td></td>
<td>Madagascar</td>
<td>510</td>
<td>Low-Income</td>
</tr>
<tr>
<td></td>
<td>Rwanda</td>
<td>930</td>
<td>Low-Income</td>
</tr>
<tr>
<td></td>
<td>Somalia</td>
<td>470</td>
<td>Low-Income</td>
</tr>
<tr>
<td></td>
<td>South Sudan</td>
<td></td>
<td>Low-Income</td>
</tr>
<tr>
<td></td>
<td>Seychelles</td>
<td>14,340</td>
<td>High Income</td>
</tr>
<tr>
<td></td>
<td>Tanzania</td>
<td>1,200</td>
<td>Lower-Middle Income</td>
</tr>
<tr>
<td></td>
<td>Uganda</td>
<td>930</td>
<td>Low-Income</td>
</tr>
</tbody>
</table>

Source: World Bank data

It should be stressed that we are using here the threshold of 1086 USD for GNI per capita for the transition to lower-middle income status, as per the recent World Bank (June 2023) reevaluation. This benchmark applies for the financial year 2024 but is of course a moving target. Our simulation did not take into account any future adjustments in the thresholds – which are adjusted annually for inflation using the Special Drawing Rights deflator, a weighted average of the GDP deflators of China, Japan, the United Kingdom, the United States, and the Euro Area.
Figure 22: Short-Run Middle Incomers? – ECA Forecasts for Achieving Lower-Middle Income Status

Reaching middle-income status is an important developmental objective of countries in the region, but it does also have some negative implications with regard to access to concessional financing[38] and also potentially in terms of preferential market access. The fact is that while Eastern Africa is a dynamic, rapidly urbanizing, and fast-growing region, per capita incomes are still very low not only by international standards but compared with continental averages. Indeed, the other countries in the region that are still classified as lower-income countries (Burundi, the Democratic Republic of Congo come on Eritrea, Madagascar, Somalia, and South Sudan) do not under the prevailing circumstances have any prospects of reaching middle-income status before 2040. This highlights the scale of the developmental challenges which still confront the region and reinforces the importance of sustaining high rates of economic growth and development.

[38] Middle-income countries are no longer legible for concessional finance from the multilateral development banks.
Conclusions
7. CONCLUSIONS

This report has provided an overview of some of the contemporary challenges for Eastern Africa. The report’s approach has admittedly been selective, in the sense that it is focused principally on debt, inflationary pressures, and the need to sustain high rates of economic growth. The conclusions from this review are ambiguous – in 2022, growth slowed down from the 6.0% of 2021, to 5.6% – but that is still almost double the continental average. If the regional forecast is accurate, 2023 and 2024 will see modest increments to the growth rate. Yet in a region with still high demographic pressures, it is pertinent to ask if that will suffice. Rising food insecurity is of particular concern. In East Africa, it is projected that up to 60 million people will be food insecure by January 2024 (Fews Net, July 2023). Progress is clearly off-track in the achievement of the SDGs, and inflation has caused a significant regression in living standards for important parts of the population in Eastern Africa.

Against such a backdrop, it is important that regional governments continue to take decisive measures to address these challenges. There are some encouraging examples of new initiatives. We cited earlier the massive increase in the agricultural budget in Tanzania, which has quintupled in just three years. Rwanda is taking action to operationalise the Ireme Invest Fund, a new catalytic green investment facility launched on the sidelines of the UN Climate Change Conference (COP27) in Egypt last year, with an initial capitalisation of slightly over $100 million. Uganda is focusing efforts on rolling out its Parish Development Model, which is aimed at transforming subsistence households into the money economy and lifting 17.5 million Ugandans out of poverty. Ethiopia’s medium- to long-term economic policy is guided by Prime Minister Abiy’s ‘Homegrown Economic Reform Agenda’ (HGER), which focuses on economic liberalisation, privatisation, currency stabilisation and debt sustainability.

In our review, we have paid particular attention to the dynamics of regional trade. For low-income developing economies, trade performance has always been an important catalyst of economic growth. A recent analysis by a team of IMF economists found evidence that increased trade over the period 1990-2010 was responsible for around half in the increase in per capita growth rates on the continent. As a vector of growth, then, trade has a very important role to play. However, the shifting contours of the global economy discussed at the beginning of this report suggest that a new strategic approach is required. India and China, for instance, are now responsible for around one third of all EAC imports, while the European Union – traditionally Eastern Africa’s most important trading partner – has seen its position decline to just over 9 percent. Regional trade policy needs to be cognizant of such profound changes. In this report, we have stressed the strategic importance of ‘going the regional route’ through the implementation of the AfCFTA. This historic agreement offers a unique opportunity to spur economic diversification on the continent, through greater cross-border trade and investment. It is an opportunity that should be seized.

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39 Fews Net (2023), Food Assistance Outlook Brief July.
40 MoFED, 2023.
41 Allard et al. 2016.
42 Of the 1.4 percentage point increase in the annual rate of growth of real per capita GDP between the decades of the 1990s and 2000s, the authors estimate that the increase in trade openness contributed 0.6 percentage points and improved terms of trade by another 0.2 percentage points.
43 ECA calculations from UNCTADStat.
Changing Gears? Catalysing Economic and Social Recovery

MACROECONOMIC AND SOCIAL DEVELOPMENTS IN EASTERN AFRICA 2023