Macro-Economic Effects of COVID-19 on the EAC Economies

Ibrahim Mike Okumu

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Bringing Rigour and Evidence to Economic Policy Making in Africa

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Macro-Economic Effects of COVID-19 on the EAC Economies

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List of abbreviatons and acronyms

AfDB	African Development Bank
B2W	Bank to Wallet
BIF	Burundian Francs
BSS	Bank of South Sudan
BoP	Balance of Payments
BoT	Bank of Tanzania
BoU	Bank of Uganda
BRB	Banque de la République du Burundi
CAB	Current Account Balance
CBK	Central Bank of Kenya
CBR	Central Bank Rate
CIs	Credit Institutions
CIEA	Composite Index of Economic Activities
CIT	Corporate Income Tax
COVID-19	Corona Virus Disease 2019
CRR	Cash Reserve Requirements
EAC	East African Community
EMDEs	Emerging Markets and Developing Economies
FDI	Foreign Direct Investment
FY	Financial Year
GDP	Gross Domestic Product
GoR	Government of Rwanda
GoT	Government of Tanzania
GoU	Government of Uganda
IMF	International Monetary Fund
MDIs	Microfinance Deposit taking Institutions
MFIs	Microfinance Institutions
MICE	Meetings, Incentives, Conferences and Exhibitions
MM	Mobile Money
MoFPED	Ministry of Finance, Planning and Economic Development
MSME	Micro, Small and Medium Enterprises
NAADs	National Agriculture Advisory Services
NBR	National Bank of Rwanda

NPLs	Non-Performing Loans
P2P	Peer to Peer
PAYE	Pay As You Earn
PIT	Personal Income Tax
PMI	Purchasing Managers Index
POS	Point of Sale
PSC	Private Sector Credit
PSPs	Payment Service Providers
RCF	Rapid Credit Facility
REPOs	Repurchase Agreements
RRR	Reserve Requirement Ratio
ROA	Return On Assets
ROE	Return On Equity
RWF	Rwandan Francs
SACCOs	Savings and Credit Cooperatives
SARS-CoV-1	Acute Respiratory Syndrome Coronavirus 1
SARS-CoV-2	Severe Acute Respiratory Syndrome Coronavirus 2
SFIs	Supervised Financial Institutions
SSA	Sub-Saharan Africa
SSP	South Sudan Pound (SSP
UDB	Uganda Development Bank
UNCDF	United Nations Capital Development Fund
USA	United States America
USD	United States Dollars
VAT	Value Added Tax
VUP	Vision 2020 Umurenge Programme
W2B	Wallet to Bank
WHO	World Health Organization

Abstract

This paper undertook an exploratory study of the effects of COVID-19 on the economies of the East African Community (EAC) Partner States, and the respective policy choices undertaken by each Partner State. The rationale of the study was to identify the areas of policy convergence in the midst of COVID-19 for purposes of streamlining EAC regional-wide policy choice in an effort to mitigate the impact of COVID-19. Macroeconomic indicators were selected from the financial, real, monetary, external, and fiscal sectors. The study used secondary data collected from the World Development Indicators, central banks of the respective Partner States, statistics agencies of the respective Partner States, and treasury offices of the respective Partner States. Our findings indicate that: COVID-19 resulted in a contraction of real GDP growth and inflationary pressure, especially in the transport sector; the financial sector remained resilient to COVID-19 although profitability tapered off; demand for credit shrunk as economies adopted COVID-19 containment measures; international trade was severely hampered although the trade deficit persisted; exchange rate depreciation pressure was apparent across the EAC, revenue shortfall has persisted through the COVID-19 life span; and EAC Partner States resorted to public debt in an endeavour to fill the persistent revenue shortfall throughout the COVID-19 lifespan in an effort stimulate their respective economies. Across the EAC Partner States, expansionary fiscal and monetary policies with degrees of intensity and extensiveness across the trading bloc were adopted in an attempt to mitigate the distortionary impact of COVID-19. EAC Partner State with intensive and extensive monetary and fiscal policy regimes equally adopted aggressive COVID-19 containment measures.

1. Background and context

The Coronavirus pandemic (COVID-19), caused by SARS-CoV-2[1], is believed to have originated from Wuhan, China, in early December 2019.[2] COVID-19 was declared a pandemic by the World Health Organization (WHO) on March 11, 2020, and since then, it has become a global emergency, given its impact on the global economy. COVID-19 has been categorized as the worst health crisis of our times. According to WHO, COVID-19 has recorded an average fatality rate of 2.19% as of 4th January 2021 with 83,910,386 infections across the world. In Africa, as of the 4th January 2021, there were 2,830,462 infections with a corresponding fatality rate of 2.4%. The East African Community (EAC) has had a total of 146,289 confirmed cases (see Figure 1) with a fatality rate of 1.6%.

Figure 1: Number of confirmed COVID-19 cases in the EAC as of January 4, 2021

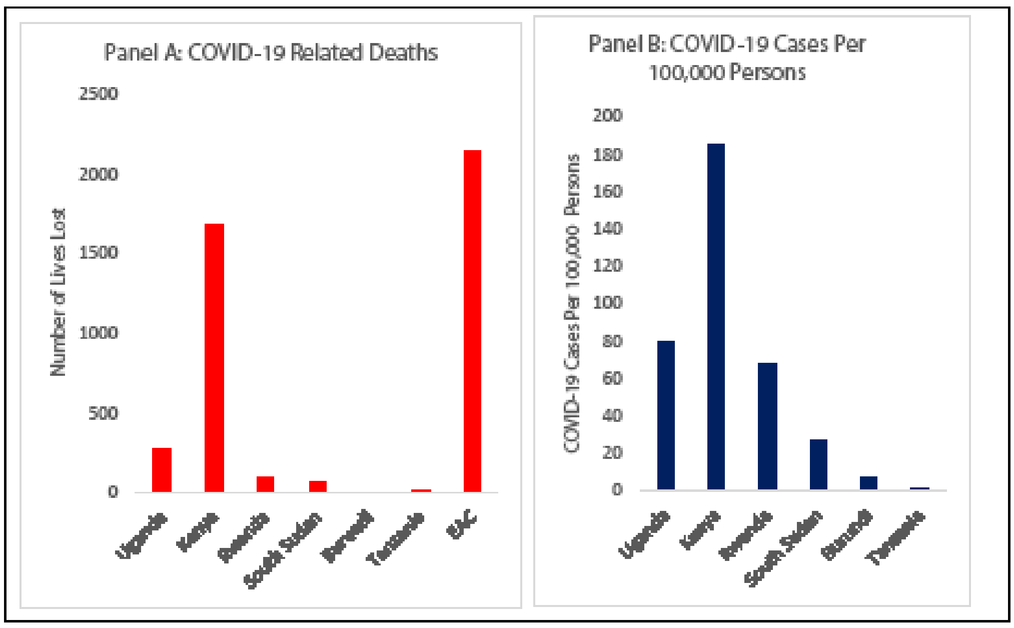
EAC
Tanzania
Burundi
South Sudan
Rwanda
Kenya
Uganda
- 20,000 40,000 60,000 80,000 100,000 120,000 140,000 160,000

Source: Africa CDC (2021).

A disaggregation across the EAC Partner States shows that Burundi, Kenya, Tanzania[3], South Sudan, Rwanda, and Uganda have had 822, 96,802, 509, 3,558, 8,676, and 35,933 COVID-19 cases, respectively, since the first cases were reported in March 2020 to end of November 2020 (see Table 1). Moreover, for every 100,000 persons in the EAC, on average, 61.2 have COVID-19. A country disaggregation shows that for every

100,000 persons, 79, 185, 68, 63, and 7 have COVID-19 in Uganda, Kenya, Rwanda, South Sudan, and Burundi, respectively (see Figure 2, Panel B). Furthermore, the fatality rate among the EAC Partner States is 1.6% which corresponds with a total of 2,146 lives lost due to COVID-19 related illnesses across the trading bloc (see Figure 2, Panel A). A country disaggregation shows that at 1,685, Kenya has the highest number of deaths attributed to COVID-19 related illnesses. While at two, Burundi has the lowest number of deaths attributed to COVID-19 related illness.[4]

Figure 2: COVID-19 cases per 100,000 persons and number of deaths in the EAC as of January 4, 2021



Source: Africa CDC (2021).

Currently, there are vaccines for COVID-19 that have successfully undergone clinical trials and regulatory approval, for example: Oxford/AstraZeneca, BioNTech-Pfizer and Modena vaccines. This is a positive step towards normalization of life; however, for the EAC trading bloc, the pending challenge is the timing for which the vaccines will be made available in the region. This is because wealthy nations making up 13% of the global population had bought off close to 51% of the future supply of promising vaccines (Oxfam, 2020). Besides, it is unlikely that 61% of the global population would have had the vaccine at least by end 2022 (Oxfam, 2020). Under the circumstances, EAC partner countries have to continue relying on COVID-19 containment measures, for example, teleworking, curfews, public awareness campaigns, and travel restrictions, among others.

While the effect of the containment measures was to slow the spread of COVID-19 scourge as the health systems in the respective Partner States adjust to the health shock, the economic costs of the pandemic have been surmounting to the EAC

economy. The effects of the supply chain disruptions, travel restrictions and financial markets volatility rattled economies of EAC Partner States. In addition, COVID-19 has led to a deteriorating external position on account of its adverse consequences on the flow of international trade, tourism, workers' remittances, foreign direct investment and loan disbursement, which may lead to exchange rate volatility.

This study, therefore, seeks to analyse the effect of the COVID-19 pandemic on the economies of the EAC Partner States, and develop macroeconomic policy options for consideration and adoption by the EAC member states. As such, the main objectives of this study are to: analyse the effect of COVID-19 on the economies of EAC Partner States; characterize the macroeconomic policy options undertaken by each Partner State while exploring areas of macroeconomic policy convergence and divergence; and develop macroeconomic policy options for consideration and adoption as a trading bloc. Note that, while it is still too early to empirically determine the full effect of the pandemic on the macro economy among EAC Partner States, discussions and data analysis of the effect of several sectors of the macro economy could enhance the literature and offer macroeconomic policy recommendations.

The rest of the paper is structured as follows. Section 2 presents the methods of analysis. Section 3 presents the effect of the COVID-19 pandemic on the global economy. Section 4 presents a discussion of the effects of COVID-19 on the economies of EAC Partner States. The policy responses adopted across the EAC trade bloc are presented in Section 5. Finally, conclusions and reflections are presented in Section 6.

2. Methodology

The study used secondary data from the central banks, statistics departments, and fiscal offices of the respective EAC Partner States, as well as from the IMF and the World Development Indicators. The analysis was based on the performance of macroeconomic variables before and after COVID-19 was identified in the EAC trading bloc. The macroeconomic variables explored are broadly in the real, monetary, financial, external, and fiscal sectors. In the real sector, the paper captures real GDP growth, inflation and indices of economic activity. The monetary sector has policy rate behaviour with and without COVID-19 and the pattern of selected market interest rates such as lending and 91-day Treasury bills rates. The financial sector captures indicators of financial sector stability relating to capital adequacy, liquidity, profitability, and credit risk. The external sector captures the trade balance, performance of exports and imports, capital flows and foreign exchange market. For each variable, there was emphasis to use high frequency data as much as possible in an effort to fairly capture the effects of COVID-19. We developed a macro tool which was populated with data for each of the aforementioned sectoral variables. Consequently, the analysis was based on the performance of the respective sectoral variables with and without COVID-19. The qualitative data was analysed using thematic and content analysis.

3. Global economy perspective

The unprecedented COVID-19 shock has pushed the global economy into a deep recession. The resultant containment measures aimed at saving lives have devastated the global economy, disrupting global supply chains, trade, financial and commodity markets, and travel. As a result, the world real GDP growth contracted by 3.3% in 2020 from a growth of 2.8% in 2019, with global trade expected to contract by over 10% in 2020. This economic outlook is worse than the growth reported during the 2008/2009 global financial crisis. The growth contraction is widespread across the advanced economies with significant contraction expected in Europe (-5.8%), and United States America (USA, -3.5% see Figure 3). Emerging Markets and Developing Economies (EMDEs) and the sub-Saharan Africa (SSA) equally contracted by -2.2% and -2%, respectively. Additionally, global financial markets experienced increased volatility, impacting asset and commodity prices. The growth outlook remained highly uncertain with resurgence of new infections and re-imposition of containment measures, and the timeliness of finding and distributing the COVID-19 vaccine.

Figure 3: Global growth (%)

Source: IMF (2021).

The policy makers around the world have implemented a wide range of supportive packages to mitigate health, social, economic, and financial impact of the COVID-19 pandemic. Several central banks have eased monetary policy through reduction in policy rates, quantitative easing, and liquidity support to cushion the impact on the economy. The fiscal stimulus packages have been deployed aimed at enhancing spending on health services and providing social safety nets to support vulnerable groups. The International Monetary Fund (IMF) in June 2020 estimated the global fiscal stimulus packages to mitigate the impact of COVID-19 were equivalent to about US$11 trillion (IMF, 2020). As a result, most economies have experienced increased fiscal deficits and rising public debt.

The subsequent sections explore how COVID-19 affected EAC Partner State economies through the real sector, monetary sector, external sector, and fiscal sector.

4. Effects of COVID-19 among EAC partner states

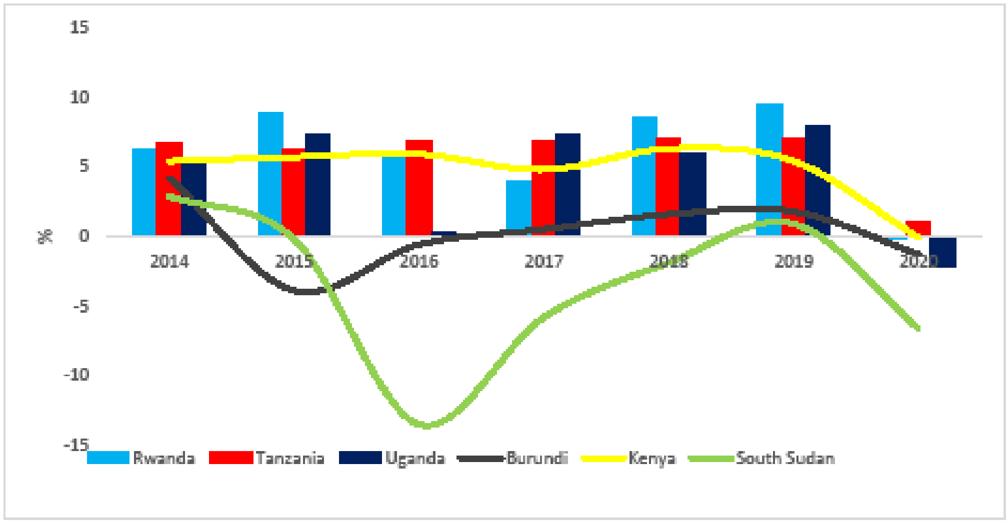
The transmissions mechanism through which COVID-19 impacts the EAC Partner States is through external (exogenous) and domestic (endogenous) effects channels. The external effects channel is conditioned on the extent of trade and financial linkages between the EAC Partner States economies and the global economy. To that extent, the distortionary effect of COVID-19 on global trade and financial flows permeates to the EAC Partner States depending on how closely intertwined their economies are with the rest of the global economy. The EAC trading bloc is generally composed of small economies that are closely linked to the global economy through real and financial linkages. As such, COVID-19 induced distortions through: global supply chain disruptions; weaker global demand on account of a global recession; travel restrictions; and global financial markets volatility which seamlessly permeate directly and indirectly into the EAC Partner States domestic economies. To the extent that in as much as the Partner States have eased their COVID-19 induced restrictions, the recovery process and return to pre-COVID-19 economic situation is closely linked to the upturn in the global economy. This could consequently have dire consequences on the domestic economy within each EAC Partner State and overall EAC trade bloc economy. The domestic effects channel captures the distortionary effect of COVID-19 on the domestic economy in terms of: morbidity, mortality, and measures adopted by respective Partner States to curtail the spread of the virus. Hereunder is a detailed analysis of the effects of COVID-19 among EAC Partner States.

Effect of COVID-19 on the real sector

Other than Tanzania that experienced subdued real GDP growth of 1% in 2020[5], economies of Burundi, Kenya, Rwanda, South Sudan, and Uganda contracted by 1.3%, 0.1%, 0.2%, 6.6%t, and 2.1%, respectively (see Figure 4). To that extent, the overall EAC trading block contracted by 1.6%. The slump in economic growth is partly on account of COVID-19 induced supply chain disruptions, contraction in both domestic and global demand, and contraction in domestic production. At least 40% of exports from the EAC Partner States is destined for the European Union, United Kingdom, China, and USA; implying that a contraction in economic growth in those economies affects the demand for EAC Partner States exports. Indeed, other than China that experienced subdued economic growth of 2.3% in 2020, the other economies went

into a recession, with the Europe, USA and EMDE growing by -5.8%, -3.5% and -2.2%, respectively (see Figure 3). The COVID-19 induced bearish global economy implies a contraction in demand for exports from EAC Partner States, thereby undermining economic growth outlook in the region.

Figure 4: Real GDP growth (%)



Source: IMF (2021).

Supply chain disruptions within and without the EAC equally compounded the effects of the weak global demand on economic growth outlook among the EAC Partner States. For example, across the EAC Partner States, COVID-19 containment measures such as mobility restrictions and COVID-19 testing at border posts undermined the flow of goods. Since the EAC trading bloc is each EAC Partner State's key export market, exports had to shrink. Indeed, on a year-on-year (y-o-y) basis, exports contracted, on average, by 7.6% and 1.7% in Kenya and Uganda, respectively, at the peak of mobility restrictions (March 2020 to June 2020). The contraction in export demand implies a reduction in aggregate demand among EAC member states thereby resulting in sluggish economic growth. Furthermore, disruptions in mobility and trade restrictions undermined import supply of intermediate goods. For example, at the peak of international trade restrictions, imports contracted by 25%, 11.3%, and 22.9% in Kenya, Uganda, and Tanzania, respectively.

The twin effect of low export demand and disruptions in the supply of inputs undermined economic performance of the industrial sector. For example, based on the y-o-y growth, in Quarter 2 (Q2, March to June of 2020), the industrial sector in Rwanda and Kenya shrunk by 3.5% and 0.5%, respectively (see Figure 5). Q2 of 2020 contraction in Rwanda's industrial sector was partly on account of -52.8%, -12.7%, -5.9% and -19.9% growths in mining, manufacturing, electricity, and construction subsectors, respectively (see Figure 5, Panel C). In Kenya, the contraction in Q2 of 2020

was on account of -3.9% and -0.6% growth in the manufacturing and electricity & water subsectors, respectively, albeit slower growth of 3.9% in the construction subsector (see Figure 5, Panel B). In Uganda, the last two quarters (Q3 and Q4) of Financial Year (FY) 2019/20, the industrial sector grew by -6.3% and -8.3%, respectively (see Figure 5, Panel A). Specifically, contraction in Q3 FY2019/20 (January to March) was on account of -30.8% and -7.2% growth in the mining and manufacturing subsectors, respectively. While the contraction in Q4 FY2019/20 (April to June) was on account of -36.8%, -7.9%, -12.3%, and -3.7% growth in the mining, manufacturing, electricity, and construction subsectors, respectively.

The combined effects of restrictive border controls, inability to restock supplies and economy-wide lockdowns undermined the service sector performance. On the y-o-y basis, the service sector in Kenya contracted by 11% and 11.7% in Q1 and Q2 of 2020, respectively, while in Rwanda, it contracted by 7.7% in Q2 of 2020 (see Figure 5). In Uganda, the service sector grew by -4% and -6.7% in Q3 and Q4 FY2019/20, respectively (see Figure 5, Panel A). Evidently, in both Kenya and Uganda, the effects of COVID-19 permeated into the service sector as early as January partly because of sluggishness in trader restocking supplies on account of border controls and production delays, particularly in China. The effects of which were worsened with the respective EAC member countries adopting containment measures to stem the spread of COVID-19 virus. The effects of the aforementioned distortions were to induce a contraction in wholesale & retail trade and transport & storage services by 6.9% and 11.6%, respectively, in Kenya in Q2 of 2020, while accommodation & restaurant services grew by -9.3% and -83.3% in Q1 and Q2 of 2020, respectively. In Rwanda, wholesale & retail trade and transport services grew by -21.7% and -41%, respectively in Q2 of 2020. In Uganda, wholesale & retail trade contracted by 3.6% and 5.6% in Q3 and Q4 FY2019/20, respectively, while transport & storage contracted by 1.3% and 8.1% in Q3 and Q4 FY2019/20, respectively.

COVID-19 pandemic also coincides with contraction in the agriculture sector in Rwanda and Uganda. In Rwanda, the agriculture sector contracted by 0.5% and 1.6% in Q1 and Q2 of 2020, respectively. This was on account of 1.79% and 1.79% contraction in food crop production in Q1 and Q2 of 2020, respectively. Also, export crops production contracted by 15.7% and 18.7% in Q1 and Q2 of 2020, respectively. In Uganda, agriculture sector production contracted by 12.1% and 12.2% in Q3 and Q4 FY2019/20. This was on account of 2.3% and 4.4% contraction in the forestry subsector in Q3 and Q4 FY2019/20, respectively, and 22.7% contraction in the food crops subsector in Q3 FY2019/20. The slowdown in the agriculture sector in Rwanda and Uganda could be partly attributed to weather shocks that led to low harvests of food crops during the 2020 agricultural season. Added to that, COVID-19 led to reduced demand of food and livestock and fishery products from critical customers such as hotels, restaurants and schools as both countries adopted economy-wide lockdowns. Furthermore, the shocks in international demand affected export crops, especially coffee in Rwanda and Uganda. In Kenya, however, the agriculture sector withered the COVID-19 pandemic, posting 4.9% and 6.4% growth in Q1 and Q2 of 2020, respectively.

COVID-19 also affected the demand-side to the extent that the Purchasing Managers Index[6] (PMI), for once, crushed below the 50 threshold. The private sector started accommodating the effects of the pandemic in January 2020 and March 2020 for Kenya and Uganda, respectively, to the extent that the PMI dropped below the 50 threshold for the first time since January 2017 (see Figure 6, Panel A). In Kenya, the PMI averaged 42.4 over the period January to June 2020, hitting the trough with a PMI of 34.8 in April 2020. In Uganda, the PMI crossed the 50 threshold in March, with a corresponding PMI of 45.3 falling to the bottom at PMI 21.5 in April 2020. Over the period March to June 2020, the PMI in Uganda averaged 38.8. Thus the period January to June 2020 in Kenya and March to June 2020 in Uganda signalled toxic and deteriorating business conditions attributed to COVID-19 induced temporary company closures, subdued demand, travel restrictions and lockdowns. Indeed, new orders, employment; supplier's delivery times and stocks of purchases all reduced during the month of March 2020 (Ministry of Finance, Planning and Economic Development [MoFPED], 2020). Similarly, Composite Index of Economic Activities (CIEA)[7] shows a weak economic environment in Uganda and Rwanda from March 2020 to May 2020.

Inflation has generally been subdued on account of low food inflation, low energy and fuels inflation and relatively stable exchange rate. Inflationary pressures have been contained within the 5% EAC convergence criteria (ceiling) medium-term target. Core inflation (non-food-non-fuel inflation) on y-o-y averaged 2.2%, 3.4%, 5.5% and 2% in Tanzania, Uganda, Rwanda, and Kenya, respectively, over the period January to June 2020 (see Figure 7). Headline inflation equally remained subdued, averaging 7.3%, 6.1%, 3.3%, 8.5%, and 3.4% over the period January to June 2020 in Burundi, Kenya, Uganda, Rwanda, and Tanzania, respectively. The low inflationary pressure in Kenya and Tanzania was on account of low energy and fuels inflation which averaged 3.7% and 5% over the period January to June 2020. While in Uganda, the low inflationary pressure was on account of low food crops inflation which averaged -0.8% over the period January to June 2020, relatively stable exchange rate, and declining international oil prices. However, in Uganda, inflationary pressure picked in the months of July to October 2020 due to a pick-up in services inflation associated with capacity restrictions for public transport to prevent the spread of COVID-19 when the lockdown was eased (see Figure 7, Panel D).

Figure 5: Sources of growth in Uganda, Kenya, and Rwanda

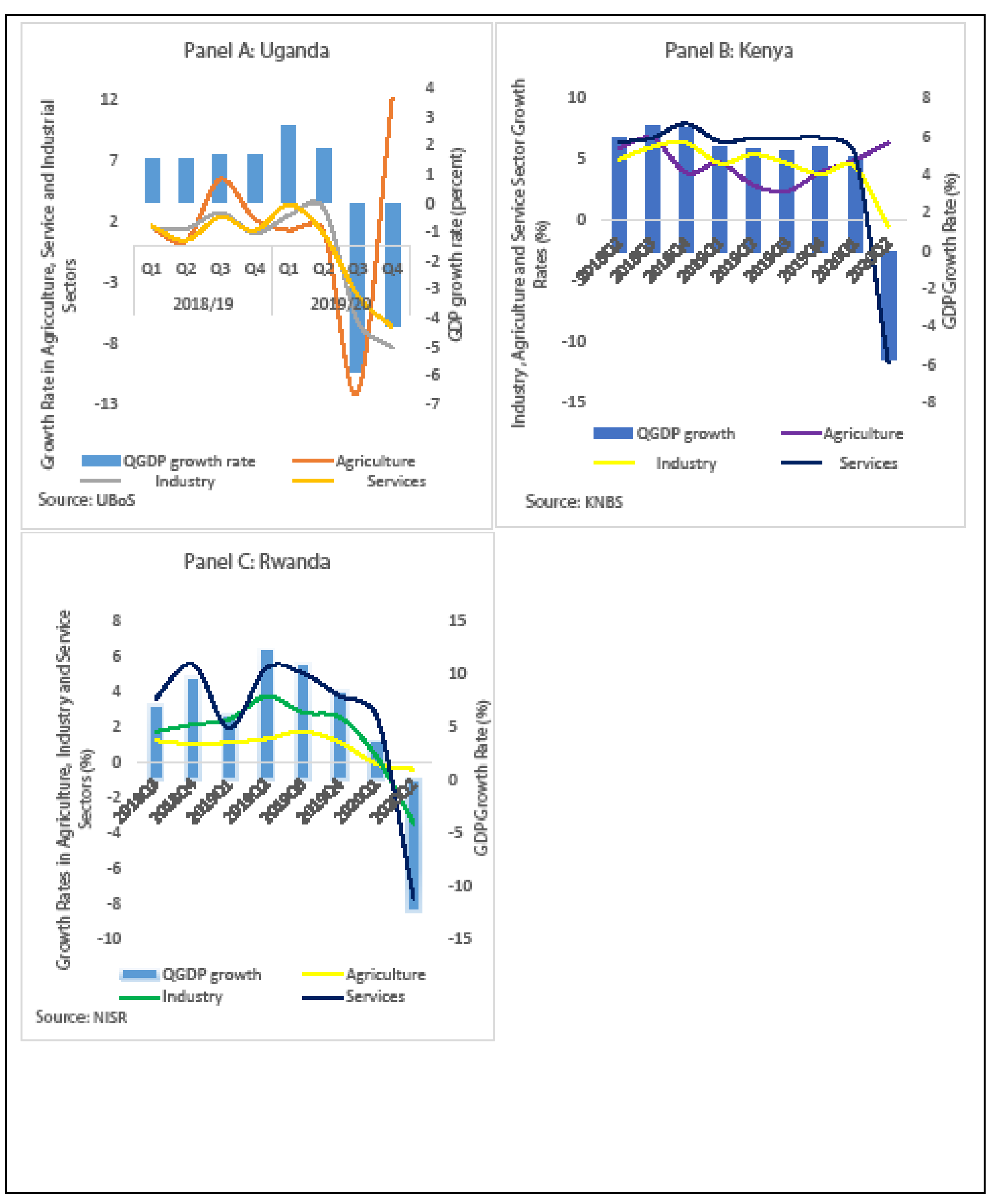
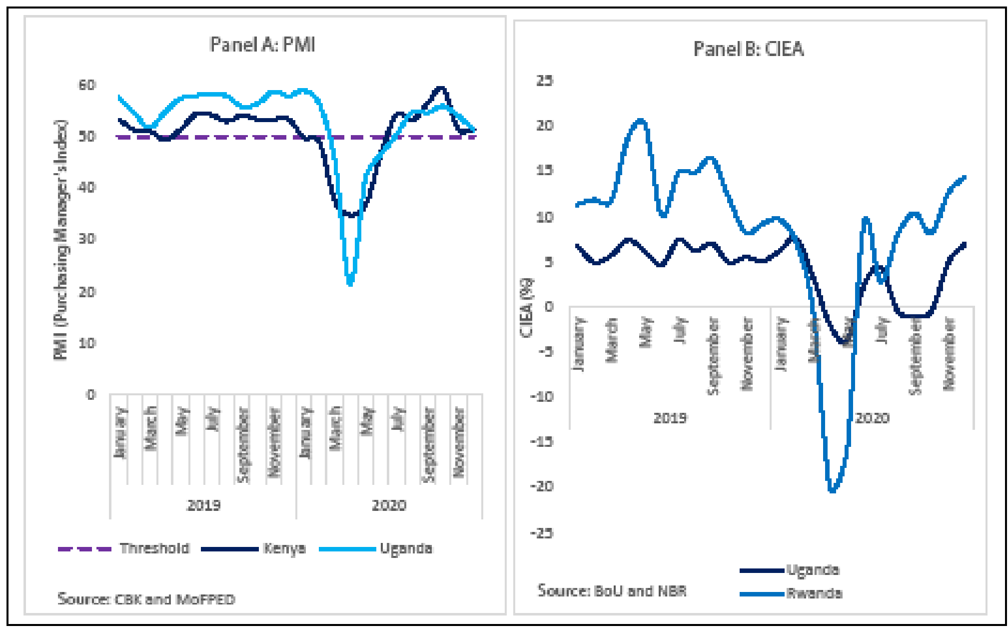
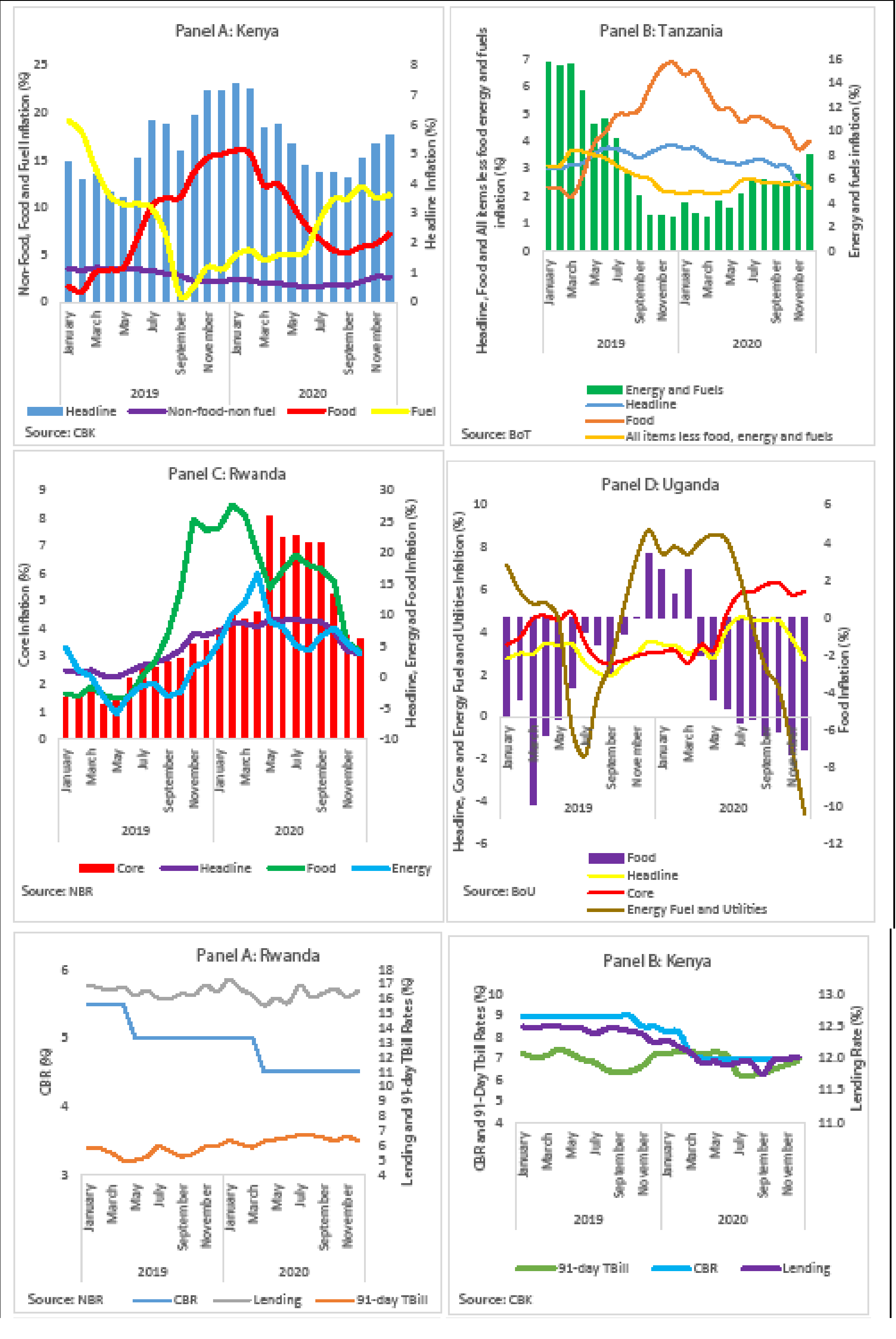


Figure 6: Indices of economic activities



COVID-19 has rattled gains made in the fight against poverty. Owing to sustained economic growth, the EAC trading bloc was fighting a successful war against poverty. For example, by 2018, poverty in Tanzania, Rwanda, Kenya, and Uganda had reduced to 26.4%, 38.2%, 36%, and 21.4%, respectively (World Bank, 2020a). However, due to the structure of the EAC Partner State economies, where the majority of the workforce is in vulnerable employment, any economic shock induces transition back into poverty. For example, 83% of the workforce in Kenya is employed in the informal economy. Also, 80% of youths in Kenya are underemployed (Danish Trade Union Development Agency, 2020). In Uganda, 84.9% of labour force outside agriculture is in the informal sector (Uganda Bureau of Statistics, 2018). As such, the containment measures that were adopted in Kenya, Rwanda, Uganda, and Tanzania directly affected livelihoods. Indeed, poverty is likely to increase in Uganda and Tanzania by at least 2% (UNCDF, 2020; World Bank, 2020b). Also, two million and one million Kenyans and Tanzanians, respectively, are projected to transit into poverty (World Bank, 2020c; World Bank, 2020d). This is because of the income reduction among informal Micro and Small Enterprises[8] where 36%, 43%, and 41% of informal workers in the manufacturing, hospitality, and trading and services sectors have been pushed below the poverty line (UNCDF, 2020). In the rural areas, the COVID-19 induced slowdown in trade, and subsequent contraction in demand for food and agriculture produce, is likely to undermine household incomes thereby perpetuating poverty.

Figure 7: Trends of broad inflation categories (year-on-year, %)



COVID-19 has disrupted human capital development, especially households in the bottom 40%. Owing to fiscal pressure, this is likely to undermine the provision of social services such as education and health care which are critical in human capital development, as fiscal resources and health services are diverted towards COVID-19 emergency response. As such, given the limited capacity of health care systems in the EAC trading bloc, this is likely to undermine the consumption of health care and delivery of health services outside COVID-19. With regard to education, the closure of schools is likely to aggravate low progression to secondary education and primary education through increased dropout rates and lower the quality of education in especially Uganda, Burundi, Rwanda, South Sudan, and Tanzania.[9]

Effect of COVID-19 on interest rates and private sector credit

In an effort to abate the distortionary effect of the COVID-19 pandemic on the economies of the respective EAC Partner States, central banks adopted an accommodative monetary policy stance (see Figure 8). To this end, policy rates across the board were adjusted southwards. For example, in March 2020, Bank of South Sudan (BSS) reduced the policy rate (Central Bank Rate, CBR) to 13% and further to 10% in July 2020. In Uganda, the policy response to the pandemic coincided with the accommodative monetary policy regime. Indeed, the pandemic only induced Bank of Uganda (BoU) to further deepen its expansionary monetary policy regime by reducing the policy rate to 8% in April and further reducing it to 7% in June, the lowest it has been since 2011. Like in Uganda, COVID-19 deepened Central Bank of Kenya (CBK) expansionary monetary policy as the CBR was reduced from 7.31%, the highest it has been since December 2018, to 7.21% in April 2020 to as low as 6.2% in August 2020. Also COVID-19 further deepened Bank of Tanzania (BoT)'s accommodative monetary policy stance that it had maintained since August 2018 by reducing the discount rate from 7% to 5% in May 2020. Also, the National Bank of Rwanda (NBR) reduced the policy rate from 5% to 4.5% in April 2020.

The accommodative monetary policy regimes resulted in the lending rates being the lowest they have been in the region for at least two decades. Lending rates responded to the easing monetary policy adopted by the respective central banks in the EAC Partner States. For example, the average lending rate in Kenya was 11.75% in September 2020 compared to 12.24% in December 2019—the lowest rates in over 29 years (see Figure 8, Panel B). The persistence of favourable lending rates in the midst of accommodative monetary policy stance is attributed to improved liquidity conditions partly reflected through increased government payments including COVID-19 related expenditures and payments for pending bills as well as CBK measures. In Uganda, the average lending rate was 17.73% in April 2020—the

lowest it had been since June 2018 (see Figure 8, Panel D). However, the average lending rates picked up following the onset of easing the economic lockdown, peaking at 20.93% in July and tapering off to 19.3% in October. Like Uganda, in Rwanda interest rates dropped to an average of 15.54% in April 2020, although they picked up in July 2020 onwards (see Figure 8, Panel A). Implying that, in both Rwanda and Uganda, the temporal reduced lending rates could partly reflect the reduced demand for loans at the peak of the economic lockdown. In Tanzania, lending rates reduced to an average of 16.3% in September 2020—the lowest they have been since January 2017 (see Figure 8, Panel E). In South Sudan, however, the favourable monetary policy stance does not seem to have transmitted into lending rates. For example, even at 10% policy rate, the average lending rate was 15.65% in July 2020 (see Figure 8, Panel C). The lending rates are still high considering that, at a policy rate of 25.4% in November 2017, the corresponding average lending rate was 12.98%, implying that liquidity constraints could be undermining the effectiveness of monetary policy in South Sudan.

Note, however, that South Sudan is the first country in the trading bloc to tighten monetary policy during the COVID-19 pandemic. As such, in November 2020, it increased the CBR to 15%, and the Reserve Requirement Ratio to 20%.

Private Sector Credit (PSC) growth signals vulnerabilities in spite of expansive monetary policy stance in Uganda and Rwanda. In Uganda, PSC growth remains subdued, reflecting concerns about the economic environment and risk aversion owing to COVID-19 (see Figure 9). The annual growth in PSC averaged 9.2% in the year to December 2020 in comparison to 13.2% in the year to 2019, a reduction of 4% in credit growth. Also in Burundi, PSC growth was 15.7% in the year to October 2020 compared to 19.6% in the year to October 2019, a 3.7% reduction. Figure 9 indicates a decelerating annual growth of PSC in Uganda and Burundi. Indeed, over the COVID-19 period, lending declined across all sectors as lenders tightened standards, reflecting increased risk aversion. In Kenya, Rwanda, and Tanzania, however, PSC growth has remained resilient in 2020 in the midst of headwinds. For example, in Kenya growth in PSC credit stood at 8.1% in the 12 months to December 2020 compared to 5.5% in the year to December 2019. In Tanzania, PSC growth was 7% in the year to October 2020 compared to 8.2% in the year to October 2019. Finally, in Rwanda, PSC growth was 15.6% in the year to December 2020 compared to 16.77% in the year to December 2019.

Figure 8: Development of interest rates among EAC Partner States

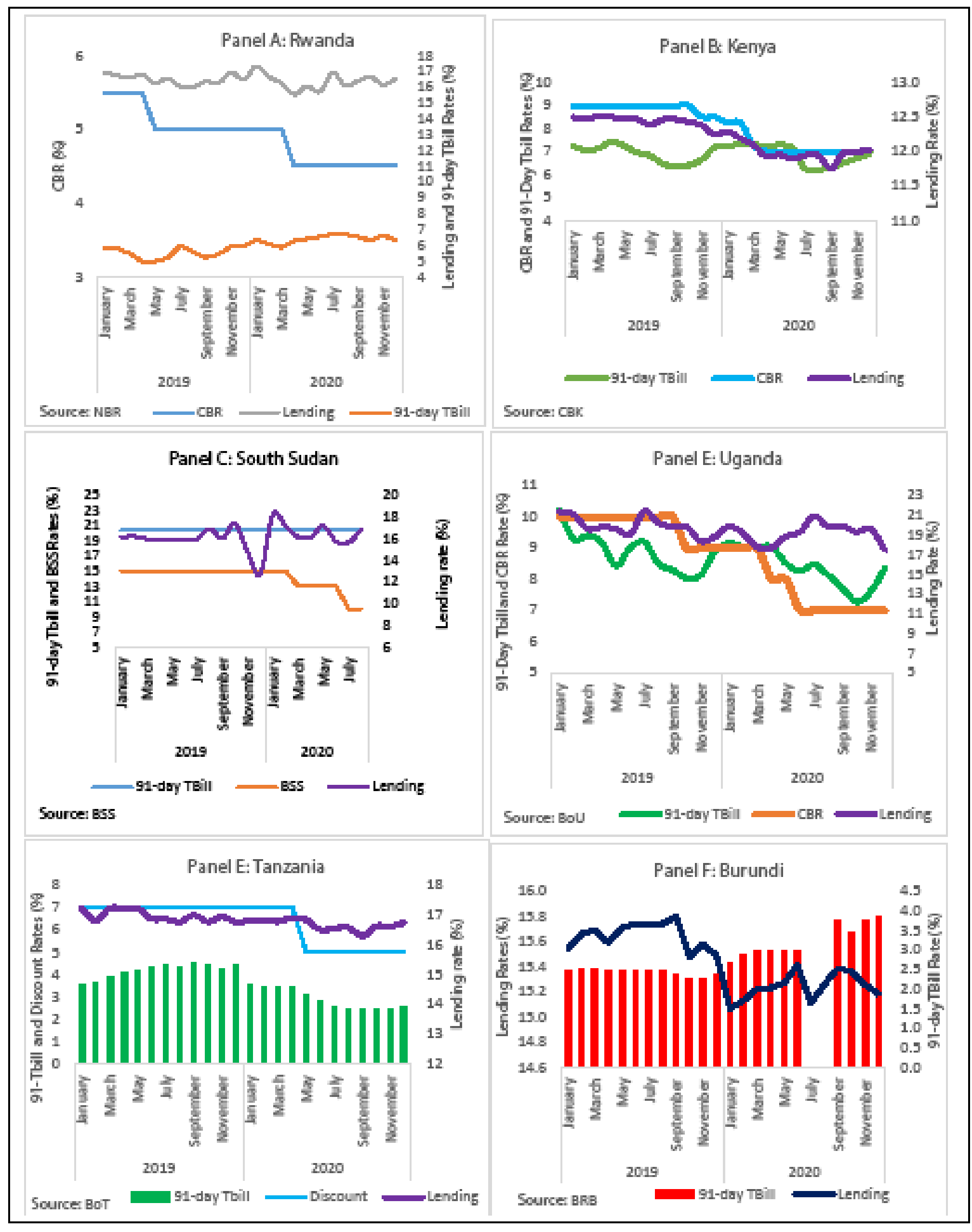
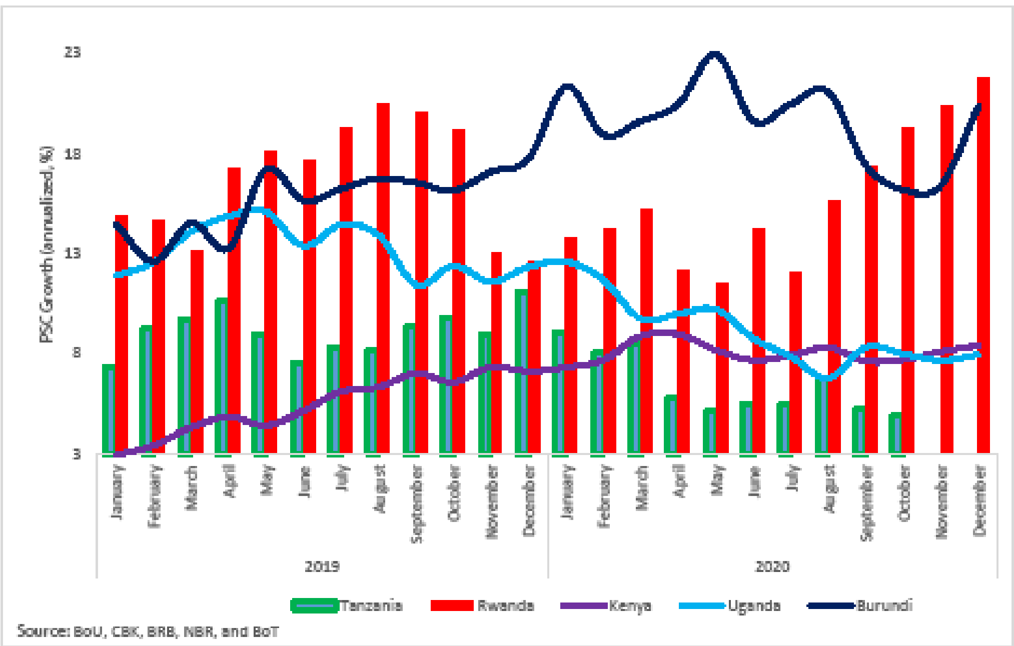


Figure 9: PSC signals vulnerabilities



Source: BoU, CBK, BRB, NBR, and BoT

Effect of COVID-19 on the financial sector

During the COVID-19 pandemic, the key role of the banking sector was "keeping lights on", supporting borrowers and strengthening resilience for the post-pandemic recovery. This role was anchored by central banks across the EAC trading bloc. For example, in Kenya, CBK requested banks to work with their customers in restructuring performing loans whose repayments were adversely affected by the pandemic and the reduction in Cash Reserve Requirements (CRR) to avail additional liquidity for banks to support borrowers. In Uganda, to ensure that financial institutions have adequate capital buffers, ease liquidity constraints in the banking system, and alleviate the financial stress experienced by households and businesses, BoU directed all Supervised Financial Institutions (SFIs) to defer dividend and bonus payments for at least 90 days effective March 2020 and committed to: providing exceptional liquidity assistance to commercial banks that are in liquidity distress for a period of up to one year; providing liquidity to commercial banks for a longer period through issuance of reverse REPOs of up to 60 days at the CBR, with opportunity to roll over; and purchasing Treasury Bonds held by Microfinance Deposit taking Institutions (MDIs) and Credit Institutions (CIs) in order to ease their liquidity distress whenever it arises.

Overall, the banking sector across the EAC Partner States remained sound and stable, despite challenges attributable to COVID-19. For example, with regard to capital adequacy, in Tanzania, total capital to total risk-weighted assets[10] stood at 17.31%. In Uganda, as at the quarter to December 2020, the sector's capital to

risk-weighted assets was 22.15% in comparison 21.36% and 21.72% as at quarters to December 2019 and March 2020, respectively. Similarly, in South Sudan, the sector's capital to risk-weighted asset as at quarter to September 2020 was 14.1% in comparison to 14.8% and 15.3% as at quarters to March 2020 and June 2020, respectively. As at October 2020, Kenya's banking sector total capital adequacy ratio[11] was 17.6% compared to 18.5% in March 2020. With regard to Burundi, as at the quarter to December 2020, the sector's capital to risk-weighted assets was 29.98% in comparison 26.97% and 29.68% as at quarters to December 2019 and March 2020, respectively. Finally, in Rwanda, as at the quarter to December 2020, the financial sector's capital to risk-weighted assets was 20.3% in comparison to 22.6% and 23.4% as at quarters to December 2019 and March 2020, respectively. Overall, there is capital adequacy across the EAC Partner States.

With regard to liquidity, Kenyan banking sector had liquidity ratio of 53.3% as at October 2020. In Tanzania, the ratio of liquid assets to demand liabilities was 31.27%. In Uganda, Rwanda, and Burundi, the ratio of liquid assets to total deposits was 50.65%, 39.5%, and 55.53%, respectively, as at the quarter to December 2020. While in South Sudan, the ration of liquid assets to total assets was 39.5% as at the quarter to September 2020. Across the EAC Partner States, the liquidity ratio is above the 20% regulatory requirement.

With regard to credit risk, in Tanzania, the ratio of non-performing loans (NPLs) to gross loans (NPLs ratio) was 10.33%. However, NPLs from new loans granted since February 2018 have declined to less than the threshold of utmost 5% due to measures pursued by the BoT. In Kenya, as at the end of March 2020, the NPLs ratio stood at 12.54%, a decrease from 12.78% recorded in March 2019 and from 12% in December 2019. Prior to COVID-19, credit risk was expected to ease in the short to the medium term. The NPLs ratio stabilized at 13.6% in August and October 2020. In Uganda, at the onset of COVID-19, the NPLs ratio increased from 4.85% as at the quarter to December 2019 to 5.41% as at the quarter to March 2020. The ratio further increased to 6.01% as at the quarter to June 2020 and later decreasing to 5.27% as at the quarter to December 2020. In South Sudan, the NPLs ratio increased from 2.1% as at the quarter to March 2020 to 2.6% as at the quarter to June 2020 and later increasing to 2.9% as at the quarter to September 2020. Finally, in Burundi, the NPLs ratio increased from 5.6% as at the quarter ending December 2019 to 6.6% and 6.8% as at the quarters ending March and September 2020, respectively. The NPLs ratio, however, decreased to 5.46% as at the quarter ending December 2020, lower than 5.6% NPLs ratio as at the quarter ending December 2019. In Rwanda, NPLs ratio increased from 4.9% as at the quarter ending December 2019 to 5.5% as at the quarter ending March 2020, and later tapering off to 4.5% as at the quarter ending December 2020.

Overall, the banking sector experienced reduced profitability mainly reflecting subdued business environment due to COVID-19 pandemic. In Kenya, the banking sector profitability, as measured by reduced return on assets (ROA) declined to 1.8% in October from 2.3% in March 2020, while return on equity (ROE) also declined to 14.8%

from 20.4%. In Uganda, the ROA reduced from 2.9% as at the quarter to December 2019 to 2.76% as at the quarter to March 2020 and further reducing to 2.58% as at the quarter to September 2020; while the ROE reduced from 16.74% as at the quarter to December 2019 to 15.89% as at the quarter to March 2020 and further reducing to 15.12% as at the quarter to September 2020. In Rwanda, ROA reduced from 2.2% in the quarter ending December 2019 to 2.1% in the quarter ending March 2020 and to 2% in the quarter ending December 2020. Regarding the ROE, it equally tapered off from 12.5% in the quarter ending December 2019 to 11.8% in the quarter ending December 2020. In South Sudan, the ROA reduced from 1% as at the quarter to December 2019 to 0% as at the quarter to March 2020, and later recovering to 1% as at the quarter to September 2020; while the ROE reduced from 12.8% as at the quarter to December 2019 to 0.6% as at the quarter to March 2020 and later recovering to 15.9% at the quarter to September 2020.

Effect of COVID-19 on the external sector

COVID-19 induced uncertainties and economic activities' shutdown have constrained global trade, reduced international travel and disrupted global value chains. While mitigation measures to control the spread of COVID-19 are essential, they had substantial impacts on commodity markets and supply chains through much lower commodity prices, lower demand for exports across the board, disruptions to value chain linkages, as well as a collapse in tourism and business travel.

Overall, the current account deficit is rather persistent across the EAC trading bloc with the deficit widening in Kenya and Rwanda while reducing in Uganda and Tanzania. In Tanzania, the current account deficit as a percentage of GDP narrowed from 3.5% in FY2018/19 to 1.2% in FY2019/20. The narrowing of the current account deficit was on account of US$1,302.5 million increase in export earnings (a 28.3% increase) which largely reflects improved gold export performance. Indeed, gold exports increased by US$846.4 million (48% increase). Indeed, y-o-y exports earnings averaged 40% in the period March 2020 to June 2020, which corresponds with 52% average growth in gold exports over the same period. On the other hand, imports reduced by 4.6%. The reduction in imports was partly COVID-19 related as y-o-y import growth averaged -20.2% for the period March 2020 to June 2020. This was partly on account of a -52% growth in intermediate goods imports over the same period.

In Uganda, the current account deficit as a percentage of GDP narrowed from 7% (in FY2018/19) to 6% (in FY2019/20). This was on account of a reduction in the import bill, reducing more than the export earnings in the midst of the COVID-19 pandemic. The import bill reduced by US$ -664.59 million in FY2019/20 compared to that of FY2018/19, while export earnings reduced by US$162.19 million over the same period. Particularly, import growth decelerated at an average of 32% over the period March 2020 to May 2020 largely contributing to the reduction in the import bill as the economy adopted an economy-wide lockdown strategy to abate the spread of

the COVID-19 virus (see Figure 10, Panel C). While export earnings growth decelerated y-o-y over the same period at an average of 34% (see Figure 10, Panel D). Exports earnings could have dropped further, however, coffee earnings held firm, averaging y-o-y growth of 28.2% over the period March 2020 to May 2020.

In Kenya, as a percentage of GDP, the current account deficit increased by 0.3% to 5.2% in FY2019/20. This was in spite of both export earnings and the import bill reducing by US$8 million and US$712 million, respectively. Like Uganda, Kenya adopted a lockdown strategy to abate the spread of COVID-19 virus which in addition to banning international travels, resulted in a reduction in export earnings while the lockdown in intermediate and final goods producing countries like China resulted in delays in the delivery of goods. Consequently, exports earnings and the import bill decelerated at an average of 10% and -26.8%, respectively, over the period April to June 2020 (see Figure 10, Panel C and Panel D). Particularly for exports, the -0.3% average y-o-y growth over the FY2019/20 is largely attributed to COVID-19, this is because up until March of FY2019/20 the average y-o-y growth was 2.2%. Also, the service account balance declined, largely reflecting reduced travel and transport receipts on account of travel bans to contain the spread of COVID-19 pandemic.

As a percentage of GDP, the current account deficit for Rwanda increased by 1.4% to 6% in FY2019/20. This was largely on account of the weak services account balance, since the share of services exports was 66.8% of total exports, and was mainly driven by travel and tourism (42% of total services exports in 2018); as such, any distortions to the travel and tourism undermines the economy's current account balance. With COVID-19-led travel restrictions and lockdowns across all regions in April 2020, revenues from tourism and transport exported services shrunk dramatically by almost a 100%. This is reflected in the hospitality performance, where hotels have lost more than US$80 million revenue associated to Meetings, Incentives, Conferences and Exhibitions (MICE) events between mid-March 2020 and November 2020. This loss was caused by the cancellation and postponement of international meetings, including CHOGM that was planned to take place in June 2020. Consequently, the service balance weakened on account of US$730 billion loss from international tourism and is consistent with the decrease in international air demand (-70% in January-August 2020). Globally, tourism is timidly recovering, supported by domestic tourism. However, the prospects of the tourism industry remain weak amidst increased number of cases, travel restrictions, and low confidence. Passenger bookings had a dramatic fall of 79.8% by mid-October 2020.

Also, COVID-19 worsened an already weak export sector by plunging traditional exports to a negative growth of 27.3% in FY2019/20Q4 (NBR, 2020). Other export sectors also fell in FY2019/20Q4. Non-traditional exports composed of other minerals, flowers, fruits and vegetables, agro-processing, and locally manufactured products fell by 62.5%. Re-exports also decreased dramatically due to weak the regional demand that resulted from economies' shutdowns. Cross-border trade was muted due to the closure of borders and the sector faced a 100% decline.

Regarding Rwanda's imports, general merchandise imports decreased by 27% in FY2019/20Q4 due to challenges imposed by COVID-19 containment measures and they returned to the previous year's level in FY2020/21Q1 as the economy recovered (NBR, 2020). Indeed, all import categories have been recovering. Intermediate goods were boosted by infrastructure projects, while capital and consumer goods were bolstered by increase in the domestic demand as businesses resumed activities. Food imports were not affected much by business closures as food businesses were allowed to run all through. They were boosted by the food distribution scheme, rolled out by the government, as a way to provide for the most vulnerable people in the society, mostly urban poor, who are unable to work and have no garden to get food from during the lockdown.

With South Sudan, CAB worsened from US$256.86 million in 2019 to US$ -932.91 million in 2020. This is on account of trade balance deterioration due to the fall in the volume of exports, and the value of those exports as oil prices fell at the international market. Exports declined from an average of US$2,902 million at the end of the 2019 prior to the outbreak of COVID-19 to about US$1,311 million in 2020 (see Figure 10, Panel B). Particularly, oil earnings, which contribute over 96% of the foreign exchange earnings, reduced from US$2,839.95 million in 2019 to US$1,311.47 million in 2020, a 54% plunge in earnings. Similarly, imports reduced from US$2,014.56 million in 2019 to US$865.56 million in 2020, a reduction of the import bill by a magnitude of US$1,149 million. While the exports earnings were higher than the import bill in 2020, the significant reduction in export earnings resulted in a 50% decline in trade balance from US$888 million in 2019 to US$445 million in 2020, and consequently current account deficit of US$932.91 million in 2020.

Overall, COVID-19 shock exacerbated an already weak export situation that prevailed since 2019 due to the decrease of commodity prices on international markets. Mineral prices weakened since 2019 due to rising trade tensions between USA and China, as well as slowing growth in China which adversely affected demand, but these prices recently stated to recover in response to supply shocks and a quicker-than-expected pick-up in China's industrial activity. Concerning coffee and tea, in 2019, the world recorded ample supply of these commodities following large harvests in Brazil and Vietnam, the world's largest Arabica and Robusta suppliers, respectively, and favourable weather conditions in East Africa, especially Kenya, and India leading to good harvest of tea, resulting in the collapse of coffee and tea prices.

COVID-19 induced depreciation pressure as export earnings, remittances, and Foreign Direct Investment (FDI) reduced. At the onset of the global spread of the COVID-19 pandemic in February 2020, financial market sentiments deteriorated due to the uncertainty that led to the flight to safety of offshore investors from developing markets such as the Kenya, Rwanda, Uganda, Tanzania, South Sudan, and Burundi thereby inducing depreciation pressures. The Kenya shilling (Ksh), Rwandan Francs (RWF), Uganda shilling (Ush), South Sudan Pound (SSP) on average depreciated by 0.99%, 0.44%, 0.15%, and 8.18%, respectively, over the period March 2020 to October 2020 (see Figure 11). The Burundian Francs (BIF) and the Tanzania shilling (Tsh) depreciated on average by 0.29% and 0.06%, respectively, over the period March 2020 to December 2020.

Figure 10: Characterizing the impact of COVID-19 on trade

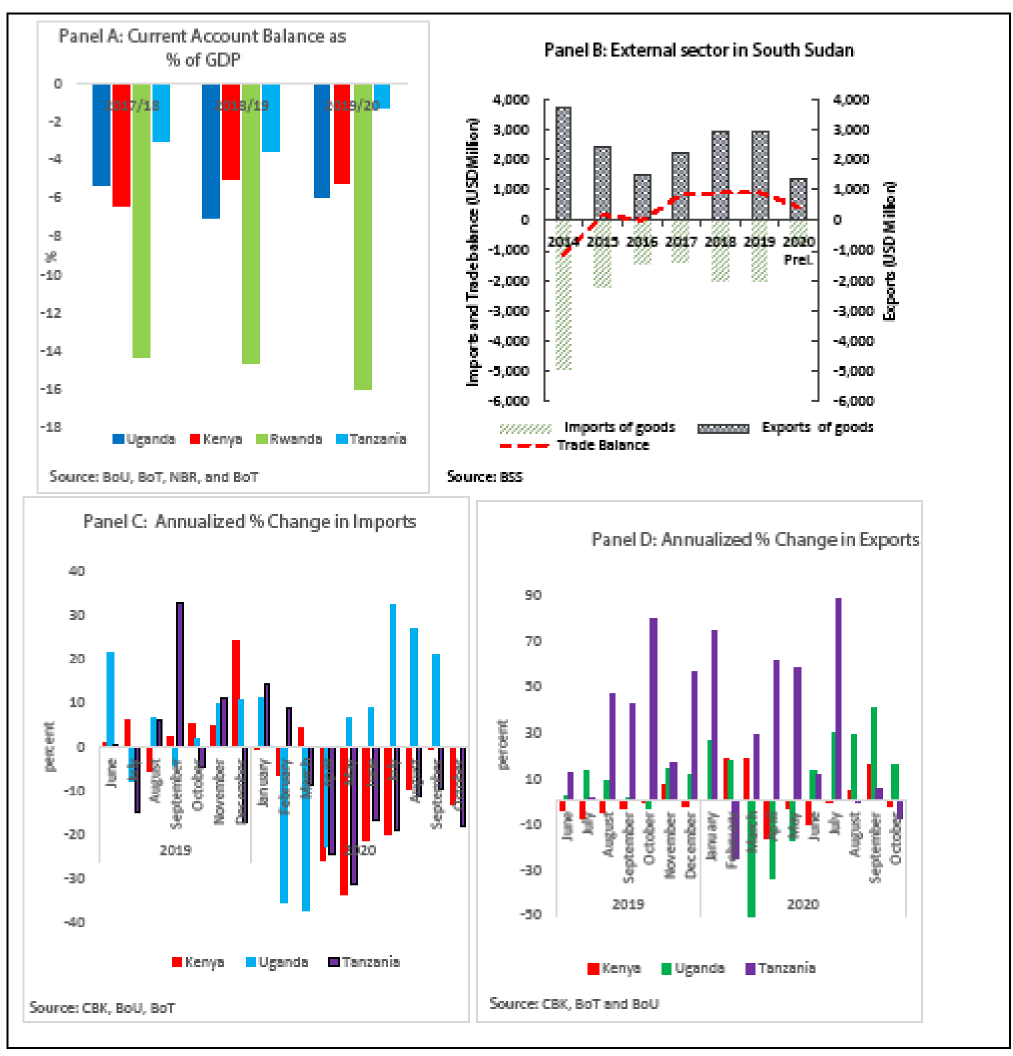
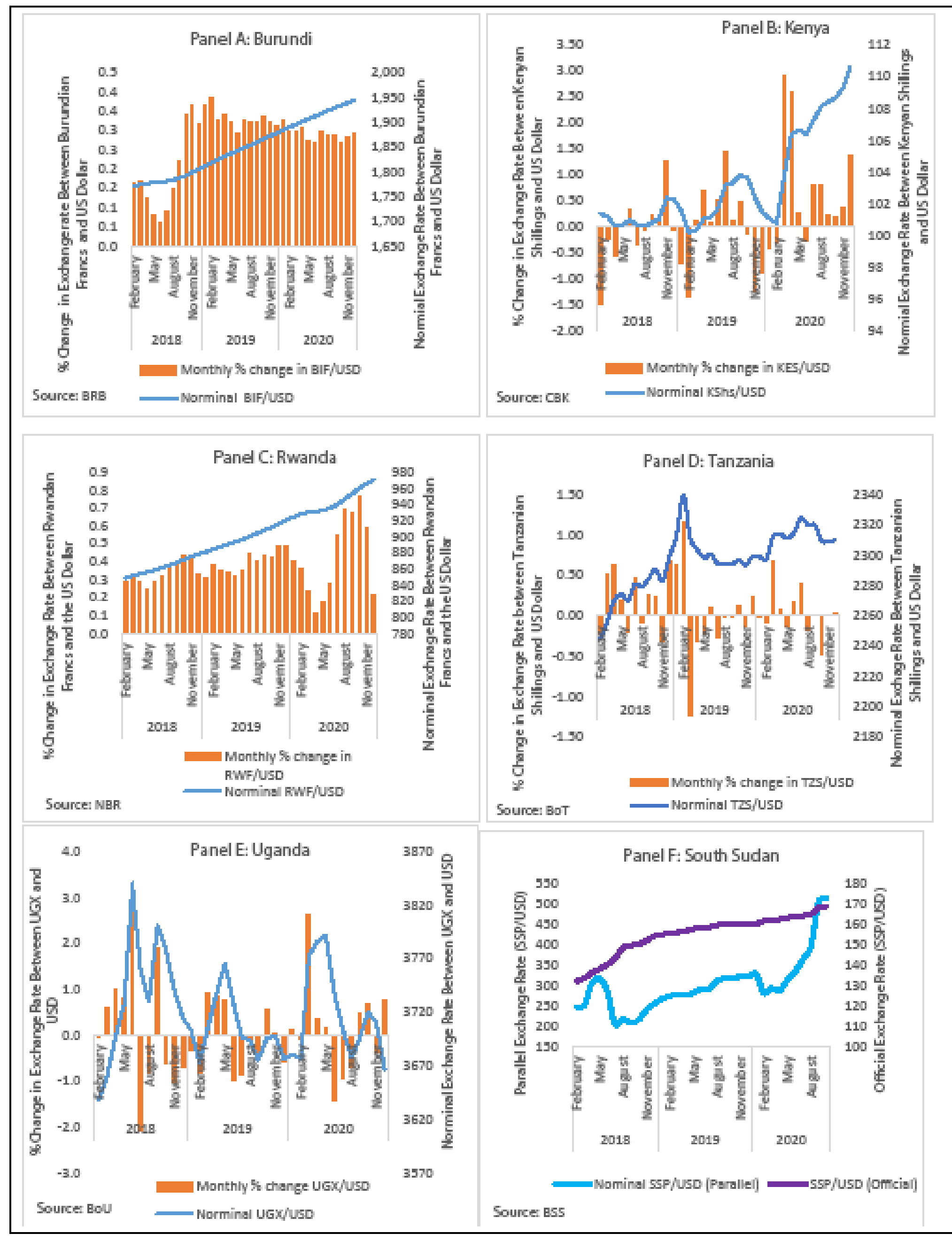


Figure 11: Exchange rates during the COVID-19 period



Exchange rate

Foreign exchange reserves in months of imports remained robust in Kenya, Uganda, and Tanzania. The EAC Benchmark foreign exchange reserves in months of imports is 4.5 months of imports. In Tanzania, while reserves in months reduced from 6.4 in February 2020 to 5.8 in month?[NEED MONTH] they remained largely adequate (see Figure 12). In Kenya, other than in April when reserves in months of imports signalled weakening (5), they quickly regained to 5.9 in June 2020 although thereafter they reduced to 5.4 which is still higher than the EAC Benchmark. Uganda signalled vulnerability in May 2020, reserves in month of imports reduced to 4.1 which is below the EAC Benchmark, even then the economy signalled resilience with reserves in months of imports recovering to 5.2 in June 2020 and 4.9 in September 2020.

Figure 12: Months of import cover

Effect of COVID-19 on the fiscal sector

Fiscal deficit worsened partly due to COVID-19 undermining the already low revenue mobilization potential. For example, in Burundi, Kenya, and Uganda, the FY2019/20 budgets indicated fiscal deficits as a percentage of GDP of 2.6%, 6%, and 7.5%, respectively. However, the projected deficit for the same period is 8.1%, 8%, and 7.6% in Burundi, Kenya, and Uganda, respectively. Also in Rwanda, the fiscal deficit as a percentage of GDP increased from 5.6% in FY2018/19 to 9.4% in FY2019/20. This was

partly as a result of the COVID-19 containment measures adopted across the three countries which resulted in the economic slowdown hence lower than targeted tax revenue was collected. Secondly, there was increased spending aimed at COVID-19 emergency response, support to private sector and social protection. For example, across the region, there was financing to bail out the struggling private sector. An Economic Recovery Fund worth US$101 million was set up in Rwanda to support ailing firms. Overall, the recovery plan is estimated to cost 3.7% of GDP. In Uganda, there was a proposed loan of US$153 million to Uganda Development Bank and doubling domestic arrears payments to US$213 million (0.6% of GDP) (World Bank, 2020a). Furthermore, tax exemptions across board were adopted in an effort to provide liquidity to the ailing private sector. For example, tax exemptions in Uganda were worth 0.2% of GDP. In Kenya, 0.4% of GDP (Ksh40 billion) was earmarked as COVID-19 related expenditure which included: medical supplies and equipment, social protection (cash transfers and food relief), and paying off domestic arrears to the private sector during the crisis (IMF, 2020).

Tax revenue collection weakened. For example, in FY2019/20, tax as percentage of GDP was budgeted at 16.3% and 13.5% in Kenya and Uganda, respectively. However, the actual tax collections as a percentage of GDP were 13.6% and 11.6% in Kenya and Uganda, respectively. During the first half of 2020, tax on goods and services in Rwanda fell by 7.8% as compared to the same period in 2019, while tax on international trade fell by 7.1%. Therefore, total revenues for the FY2019/20 had a slower growth of 5.7% while in the previous fiscal year they had grown by 14.3%. Overall, Rwanda expects a revenue shortage of 2.8% of GDP (IMF, 2020). The low tax collection is attributed to the COVID-19 induced ailing economies and tax relief packages adopted by the respective countries. For example, in Uganda, tax relief package between April and June 2020 was 0.2% of GDP (World Bank, 2020b).

Note, however, that the fiscal deficit as a percentage of GDP in Tanzania improved from 3.2% in FY2018/19 to 1.4% in FY2019/20, which is below the EAC monetary policy convergence criteria of 3% of GDP. While revenue performance was slightly lower than target in much of 2020, the overall fiscal deficit as a percentage of GDP was 1.4% in 2019/20 compared to 3.2% in FY2018/19. Domestic revenue collection as a percentage of GDP was 14.7% in 2020, up from 13.9% in 2019. Tax revenue performance was relatively satisfactory, averaging around 87% of the target in January-October 2020. The good revenue performance, relative to the target and given the extraordinary times, was bolstered by the flexible approach of COVID-19 containment measures, which included not locking down economic activities.

Due to tax revenue shortfalls, COVID-19 induced reliance on debt to fill the revenue gap. For example, Kenya's public and publicly guaranteed debt stood at Ksh7.1 trillion as at end September 2020. Domestic debt was Ksh3.5 trillion (48.6% of total debt), while foreign debt was Ksh3.6 trillion (51.4% of total debt). Domestic debt consisted of Treasury bonds of Ksh2.5 billion (74.5% of total government securities) and Treasury bills of Ksh0.9 billion (25.5%) as at October 2020. Foreign debt was composed of multilateral (38.8%), commercial (31.1%), and bilateral (30.1%). The

substantial share of multilateral debt partly reflects recent financial support from international financial institutions, including the IMF's Rapid Credit Facility (RCF) of US$739 million, a World Bank loan (US$1 billion) and AfDB credit (US$250 million) to support initiatives to strengthen health care system to respond to the pandemic, as well as funding critical interventions to address the impact of the COVID-19 pandemic. Notably, the latest IMF/World Bank Debt Sustainability Analysis (May 2020) finds that Kenya's debt position remains sustainable, but that the risk of debt distress has increased to high, due to the COVID-19 crisis weakening exports and real GDP growth and delaying fiscal consolidation. Similarly, due partly to COVID-19, the stock of total public debt in Uganda increased from US$12.55 billion in FY2018/19 to US$15.27 billion in FY2019/20 (Ush56.94 trillion) by end June 2020, representing an increase of 21.7%. The effect of the increase in public debt induced an increase in debt stress risk from low to moderate. This was on account of vulnerabilities to the debt outlook arising from dampened export growth coupled with increasing debt service burden (MoFPED, 2020). In Rwanda, public debt as percentage of GDP increased from 58.5% in 2019 to 68.1% 2020, a 9.6% increase. The increase was largely attributed to external debt, which as a percentage of GDP, increased from 45.6% in 2019 to 55% in 2020. As a result, Rwanda's increase in public debt stock equally resulted in the overall debt stress moving from low to moderate, albeit still sustainable on account of weak revenue collection and a sharp decline in exports and remittances (IMF, 2020c). In Tanzania, external pubic debt increased from 17.657 billion in December 2019 to 18.544 billion in December 2020, a 5% increase. While public domestic debt was Tsh 16,179.6 (US$7.04 billion[12]) in December 2020 compared to Tsh 14,435.2 (US$6.31 billion[13]) in December 2019 (BoT, 2020). As such the total public debt increased from US$23.967 billion in December 2019 to US$25.584 billion in December 2020, a 6.7% increase. Even then, overall Tanzania's public debt is sustainable with the external debt characterized low risk of distress.[14]

5. Policy choices undertaken among EAC Partner States to ameliorate the effects of COVID-19

The governments across the EAC Partner States undertook measures aimed at containing the spread of COVID-19 pandemic, and moderating the economic and social impact (see Table 1). The measures included fiscal, monetary, financial, prudential, and other regulatory measures. The extent of each policy initiative varied on how much the policy makers in the different Partner States evaluated the socioeconomic cost of COVID-19 in the respective economies. Otherwise, overall, the measures offered relief to the economy through injection of cash and provision of additional disposable incomes to the people and businesses.

With regard to monetary policy across the board, there was convergence to the extent that each Partner State opted for expansionary monetary policy while ensuring financial market stability. In Rwanda, for example, in April 2020 the National Bank of Rwanda (NBR) reduced the policy rate from 5% to 4.5%. To ease banking sector liquidity constraints, the NBR offered to buy back Bonds at the prevailing market rate, and the waiting period if one fails to sell the bond at the secondary market will be reduced from the current 30 days to 15 days. Furthermore, effective 1 April 2020, NBR lowered the Reserve Requirement Ratio (RRR) from 5% to 4% thereby releasing RWF 23.4 billion additional liquidity for banks in order to allow banks more liquidity to further support affected businesses. In addition to existing central bank liquidity facilities such as Intra-day liquidity facility, Overnight lending facility, Reverse Repo for seven days and Refinancing facility for seven days, the NBR introduced an extended lending facility to Banks: The NBR put in place a facility of RWF 50 billion that banks with liquidity challenges can borrow from at the Central Bank Rate (CBR). The tenor was extended from overnight to three, six and 12 months.

To ease credit risks, NBR allowed banks to restructure outstanding loans of borrowers facing temporary cash flow challenges arising from COVID-19 pandemic. Finally, to encourage use of digital channels and contactless mobile payments: In an effort to limit the risk of transmission of the virus through handling of cash and other non-virtual means of payment, for three months and effective from 19 March 2020, mobile network operators and banks agreed to: zero charges on all transfers between bank accounts and mobile wallets (Pull and Push services); zero charges on all mobile money transfers; zero merchant fees on payments for all contactless Point of Sale (mobile and virtual POS) transactions; and the limit for individual transfers using mobile money wallets increased from RWF 500,000 to RWF 1,500,000 for Tier I customers and from RWF 1,000,000 to RWF 4,000,00 for Tier II customers.

In Kenya, the Central Bank of Kenya (CBK) implemented monetary policy measures to improve liquidity and enhance credit access by the private sector at an affordable cost. The monetary policy measures implemented were as follows: lowered CBR from 8.25% to 7.25% in March 2020, and further to 7% in April 2020. The reduction was aimed at signalling to commercial banks to lower their interest rates on credit facilities and to avail affordable credit to Micro, Small and Medium Enterprises (MSMEs) countrywide; lowered the Cash Reserve Ratio (CRR) for commercial banks by 100 basis points with effect from March 23. This released Ksh35.2 billion as additional liquidity to banks to directly support borrowers adversely affected by COVID-19, of which Ksh32.6 billion (92.7%) had been utilized in the six months to October 2020 to support lending, especially to the tourism, trade, transport and communication, real estate, manufacturing, and agriculture sectors; and to enable banks secure longer-term liquidity, CBK extended the maximum tenor of Repurchase Agreements (REPOs) from 28 to 91 days. CBK also provided flexibility to banks with regard to requirements for loan classification and provisioning for loans that were performing and whose repayment period was extended or restructured due to COVID-19.

To facilitate electronic payments, CBK adopted the following measures: elimination of charges for mobile transactions under Ksh1,000; elimination of charges by Payment Service Providers (PSPs) and commercial banks for transfers between mobile money wallets and bank accounts. Banks also waived all charges for balance inquiry through digital platforms; increase of daily M-PESA transaction limits from Ksh70,000 to Ksh150,000 specifically to support small and micro business enterprises (SMEs); and increased the daily transaction limit up to Ksh300,000 in M-PESA wallets up from Ksh140,000.

In order to shield borrowers from adverse effects of COVID-19 pandemic, CBK provided the following emergency measures: 1) Loan restructuring: Banks committed to discussing restructuring of loans with customers whose loans were performing as at 02 March 2020 but were adversely impacted by the pandemic. Banks were to meet all the costs related to the extension and restructuring of loans; 2) Credit Referencing: The Cabinet Secretary for the National Treasury and Planning, on the recommendation of CBK, published through Gazette Notice No. 3096 of April 8, 2020 the temporary suspension for a period of six months, from April 1 to 30 September 2020, the listing of negative credit information for borrowers whose loans were performing previously but have become non-performing from 1 April 2020; and 3) Business Continuity Planning: On March 27, CBK issued guidance to the banking sector on pandemic planning and business continuity. The guidance, which was aligned to protocols from the Ministry of Health, was aimed at monitoring the incidence of the pandemic in the sector and guiding responses thereto.

In Uganda, Bank of Uganda (BoU) reduced the CBR to 8% in April 2020, and later to 7% in June, and that has been maintained to date. To ensure financial institutions have adequate capital buffers, ease liquidity constraints in the banking system and alleviate the financial stress experienced by households and businesses, BoU directed all Supervised Financial Institutions (SFIs) to defer dividend and bonus payments

for at least 90 days effective March 2020 and committed to: providing exceptional liquidity assistance to commercial banks that are in liquidity distress for a period of up to one year; providing liquidity to commercial banks for a longer period through issuance of reverse REPOs of up to 60 days at the CBR, with opportunity to roll over; and purchasing Treasury Bonds held by Microfinance Deposit taking Institutions (MDIs) and Credit Institutions (CIs) in order to ease their liquidity distress whenever it arises.

Credit relief measures included: repayment holidays for a maximum of 12 months, loan tenor extensions, and any other forms of debt restructuring covered in existing regulations; the prepayment of arrears as a condition for restructuring a credit facility suspended for 12 months with effect from 1 April 2020; liquidity support: BoU set up a Liquidity Assistance Programme for all supervised financial institutions (SFIs) facing liquidity pressures; provision of liquidity assistance to SFIs for longer periods of up to one year, through issuance of reverse REPOs of up to 60 days at the CBR, with the opportunity for roll over, as well as standing facilities; purchase of Treasury Bonds held by Microfinance Deposit taking Institutions (MDIs) and Credit Institutions (CIs); and MDIs and CIs that do not hold Treasury Bills or Bonds in their asset holdings would be provided with liquidity secured by their holdings of unencumbered fixed deposits or placements with other SFIs.

With regard to mobile money charges: GoU through BoU spearheaded the zero rate charges for Peer to Peer (P2P), Wallet to Bank (W2B) and Bank to Wallet (B2W) transactions. The above measures were aimed at reducing the use of paper money as well as physical visits to commercial banks premises and designated Automated Teller Machine areas. These measures were effective from 25 March 2020.

In Tanzania, the Bank of Tanzania (BoT) revised the discount rate from 7% to 5% in May 2020 besides reducing haircuts on government securities pledged by banks for central bank credit from 10% to 5% for securities maturing within one year, and from 40% to 20% for securities with remaining maturities exceeding one year. Furthermore, to enhance financial market liquidity, the BoT reduced the RRR from 7% to 6%. In addition, the central bank intensified the deployment of instrument for liquidity injection. Furthermore, the central bank granted regulatory flexibility for loan restructuring for borrowers facing financial difficulty and incentivized the use of digital payment platforms by relaxing daily transactions for mobile money from Tsh3,000,000 to Tsh5,000,000 and daily balance from Tsh5,000,000 to Tsh10,000,000 for all mobile wallets.

In Burundi, the Banque de la République du Burundi (BRB) continued the quantitative easing that aimed at supporting the economy and intensified liquidity injection in the commercial banks at 3% on average. To facilitate investment in growth conducing sectors such as agriculture, agro manufacturing and agribusiness, among others, BRB reduced the refinancing rate to 2% for the above mentioned sectors. In order to support hotels and the accommodation sector severely hit by the pandemic, BRB allowed commercial banks the restructuring of defaulting loans on a case by case basis. While not being explicit as to cost reduction in mobile money and digital payment, BRB encouraged the use of these means of payments through sensitization of the key stakeholders, namely, telecom companies and commercial banks.

In South Sudan, the Bank of South Sudan (BSS) reduced the policy rate from 15% to 13% in April 2020, and further to 10% in July 2020. Furthermore, the BSS reduced the RRR from 20% to 18% in April 2020 and further to 10% in July 2020. However, the BSS reversed its expansionary monetary policy through increasing the policy rate and RRR to 15% and 20%, respectively, in November 2020. To ease capital constraints, the BSS in July 2020 suspended the recent regulation of higher minimum paid-up capital for commercial banks. Also to reduce credit risk, BSS advised banks to restructure loans on a case by case basis.

With regard to fiscal policy, Government of Rwanda (GoR) adopted the following measures: Value Added Tax (VAT) and Corporate Income Tax (CIT) deferred for several months to ease the payment of taxes; computation of quarterly payments for CIT and Personal Income Tax (PIT) will be based on the transactions of the current year (instead of the previous year); Pay As You Earn (PAYE) waived for a period of six months (April to September 2020) for teachers earning net salary of up to RWF 150,000 and for a period of three months (April to June 2020) for employees of companies operating in the tourism and hotel sector earning net salary of up to RWF 150,000; VAT exemption on masks made in Rwanda to prevent the spread of COVID-19; and Economic Recovery Fund worth US$311 million or 3.3% of GDP to support firms that were badly affected through providing subsidized loans to eligible businesses using banks and Micro Finance Institutions (MFIs), with US$50 million dedicated to the tourism subsector alone. Furthermore, GoR pledged to avail credit guarantees to SMEs and micro businesses in the informal sector in order to maintain liquidity, protect jobs and livelihood. Also, at the cost of RWF 133.6 billion (1.4% of GDP), scaling up existing social safety net programmes with the rationale of providing emergency relief and supporting the economic recovery, while ensuring access to basic services among vulnerable sections of the population affected by COVID-19. The emergency relief response involved door-to-door food distribution to vulnerable households affected by COVID-19 containment measures. While support for economic recovery involved casual employment opportunities in labour-intensive projects (e.g., road rehabilitation programmes), subsidized access to agricultural inputs (e.g., fertilizers and seeds), pro-poor credit schemes for investing in income generating activities, and basic equipment to start new businesses with a view to restoring livelihoods disrupted by the pandemic. Finally, access to basic services involved vulnerable households having access to basic health and education amidst COVID-19 through reducing contributions to the community-based health system, subsidized tuition fees and school material for children, and the construction of shelters and sanitation facilities.

GoU also adopted tax relief to businesses: deferred payment of corporate tax income or presumptive tax for corporations and SMEs; deferred the payment of PAYE until September 2020 by sectors severely affected by COVID-19 pandemic such as, manufacturing, tourism and floriculture; waived interest on tax arrears, provided for tax deductibility of donations for the Coronavirus response and committed to expedite payment of outstanding VAT refunds. GoU spent 0.2% of GDP in FY2019/20 towards strengthening health systems, additional security measures and mitigating the impact

of COVID-19 containment measures on livelihood. Specifically, GoU committed to provide credit through SACCOs and Micro Finance Institutions to support Micro and Small-Scale Enterprises; increased access to credit by providing Ush1.045 trillion over the medium term to Uganda Development Bank (UDB) to offer low interest financing; and expedite the payment of domestic arrears. GoU deemed water and electricity as essential services; as such, it instituted a temporary ban on disconnecting water and electricity services to vulnerable businesses and firms. GoU also sought to buffer livelihoods through restoring household incomes and safeguarding jobs. Specifically, government committed to: enhance the provision of improved agricultural inputs using the NAADs; create jobs for the vulnerable but able bodied persons affected by the COVID-19 by extending labour intensive public works in urban and peri-urban areas; provide rainwater harvesting technologies in rural communities and roll-out regional and community based storage facilities; provide seed capital to organized special interest groups under the Youth Fund, Women Entrepreneurship Fund and the "Emyooga" talent support scheme.

In Tanzania, GoT increased spending on the health sector to deal with COVID-19 effects, including granting exemption of VAT and custom duties on imported medical equipment and medical supplies. To support the private sector, GoT expedited the payment of verified expenditure arrears with SMEs being given priority. In that regard, US$376 million was paid out to the private sector in March 2020. The government has also expanded social security schemes by US$32.1 million to meet the increase in pension withdrawals for retrenched staff due to COVID-19. In 2020, GoT also obtained debt relief from the IMF under CCRT of about US$25.5 million.

In Kenya, GoK implemented fiscal measures aimed at providing relief and increase disposable income to the people, and protecting jobs and businesses from the adverse economic effects of the COVID-19 pandemic. These measures included: 100% tax relief for persons earning gross monthly income of up to Ksh24,000; reduction of top income tax rate (PAYE) from 30% to 25%; reduction of resident income tax (Corporation Tax) from 30% to 25%; reduction of the VAT from 16% to 14%; reduction of the turnover tax rate from 3% to 1% for all MSMEs; allocation of Ksh13.1 billion to settle verified pending bills owed by ministries and departments and a further Ksh10 billion for payment of verified VAT refund claims in order to enhance liquidity for businesses; appropriation of an additional Ksh10 billion to the elderly, orphans and other vulnerable members of the society through cash-transfers to cushion them from the adverse economic effects of the COVID-19 pandemic; allocation of Ksh1 billion to recruit health workers to strengthen the human capital capacity of the Ministry of Health; and allocation of Ksh400 million for food and non-food commodities for affected households.

In Burundi, the government increased spending on health sector through hiring additional health workers and technicians, importing medical equipment, and all the logistics around the fight against the pandemic. In its campaign "Ndakira, singwara, sinanduza" literally meaning "I will heal, I will not be sick and I will protect" the government subsidized a local sanitizers manufacturing company in order to make the soap affordable to the poor. Hence, the price of a typical soap was cut by 50%

from Bif 300 to Bif 150 per piece. The shortfall was supported by the government. Moreover, the price of water in the countryside was subsidized to encourage people to wash hands and improve hygiene.

Overall, in terms of policy convergence, across the board, there was an effort for the central banks in the respective Partner States to undertake pre-emptive measures to moderate the impact of COVID-19 and support their respective economies to recover from the consequences of the pandemic. This was through reducing the policy rate, strengthening financial sector liquidity, mitigation against credit risk, and ensuring capital adequacy (see Table 1). Besides, there was an effort to support the adoption of digital payment systems especially mobile money as opposed to physically moving money in the payments system. With regard to fiscal policy, overall, governments in Partner States undertook expansionary fiscal regimes to tame the distortionary effect of COVID-19 on livelihood and firms. Even then, the intensity and extensiveness of both fiscal and monetary policy varied across the EAC trading bloc. For example, fiscal and monetary policy in Rwanda, Uganda, Burundi, and Kenya was both deep cutting and wide, unlike Tanzania and South Sudan. This could be partly because of the extent of COVID-19 containment measures in each sovereign state (see Table 1). For example, while Uganda and Rwanda instituted economy-wide lockdowns, this was never the case in Tanzania. As such, it was prudent for authorities in Rwanda and Uganda to mitigate the adverse effects of COVID-19 by induced aggressive containment measures.

Table 1: EAC trading block policy mix to abate the impact of COVID-19

	Kenya	Tanzania	Uganda	Rwanda	South Sudan	Burundi
Fiscal Policy						
Tax exemptions	Yes	Yes	Yes	Yes	Yes	Yes
Social protection	Yes	Yes	Yes	Yes	Yes	Yes
Private sector relief funds	Yes	Yes	Yes	Yes	No	Yes
Increased public debt	Yes	No	Yes	Yes	No	Yes
Monetary Policy						
Reducing the policy rate (CBR and Discount Rate)	Yes	Yes	Yes	Yes	Yes	Yes
Reducing the RRR	Yes	Yes		Yes	Yes	Yes
Increased the maximum tenor of Repurchase Agreements	Yes	No	No	No	No	Yes
Central bank extending lending to commercial banks at longer maturity periods	Yes	No	No	Yes	No	Yes
Regulatory flexibility to central bank Supervised Financial Institutions (SFIs) that extend loan restructuring operations on a case by case basis	Yes	Yes	Yes	Yes	No	Yes
SFIs directed to defer dividend payments	No	No	Yes	Yes	No	No
Insurers directed to defer dividend payments	No	No	No	Yes	No	No
Suspension of listing of negative credit information for loan defaulters	Yes	No	No	No	No	No
New minimum threshold for negative credit information submitted to credit reference bureaus	Yes	No	No	No	No	No
Purchase of Treasury bonds held by Microfinance Deposit taking Institutions and credit institutions to ease liquidity	No	No	Yes	No	No	No
Encouraged commercial banks to reduce electronic transaction charges	Yes	No	No	No	No	Yes
Daily transaction limit for Mobile Money (MM) operators was increased	Yes	No	Yes	No	No	Yes
Reduction of MM and other digital charges payment charges	Yes	No	Yes	No	No	Yes
Exchange rate and BoP measures	No	No	Yes	No	No	No

continued next page

Table 1 Continued

	Kenya	Tanzania	Uganda	Rwanda	South Sudan	Burundi
Other policy						
International flight suspensions except for essential/critical deliveries	Yes	Yes	Yes	Yes	Yes	yes
Establishment of isolation centres	Yes	Yes	Yes	Yes	No	Yes
Land border restrictions	Yes	No	Yes	Yes	No	Yes
Evening curfews	Yes	No	Yes	Yes	Yes	Yes
Social distancing	Yes		Yes	Yes	Yes	Yes
14-day mandatory quarantine period for travellers coming from COVID-19 affected countries	Yes	Yes	Yes	Yes	Yes	Yes
Restrictions on domestic travel	Yes	Yes	Yes	Yes	Yes	No
Working from home was encouraged (teleworking)	Yes	No	Yes	Yes	Yes	No
Closure of schools and educational institutions	Yes	Yes	Yes	Yes	Yes	No
Restrictions on large gatherings	Yes	Yes	Yes	Yes	Yes	Yes
Restrictions on worship	Yes	No	Yes	Yes	Yes	No
Closure of non-essential business	No	No	Yes	Yes	No	Yes
Mandatory wearing of face masks	Yes	No	Yes	Yes	Yes	

Source: IMF (2020a).

6. Conclusion

Undoubtedly, COVID-19 has devastated the EAC trading bloc through slowing the pace of economic growth. The removal of temporary containment measures, continued accommodative macro-policy stance, strong initial economic conditions, resumption of economic activities, de-escalation of the psychology of fear, and gradual relaxation of stringent measures in the rest of the world appears to gradually rejuvenate the economy. However, while there was uniformity in the fiscal and monetary policy choices; the countries diverged in the depth and width of economy-wide COVID-19 containment measures. Even then, going forward, the EAC Partner States ought to continue implementing accommodative monetary policy and expansionary fiscal policy alongside easing the containment measures as these, coupled with the strong initial economic conditions, have the potential to facilitate faster economic recovery.

Also, the increased uptake of debt to abate the distortionary effects of COVID-19 should be done alongside ensuring debt sustainability. This is partly because there is likelihood of a potential debt crisis which could reverse any possible gains made post-COVID-19.

Furthermore, in view of the limited fiscal space in the midst of infrastructure gaps across EAC Partner States, it is imperative that flexibility is introduced among the EAC macroeconomic policy convergence criteria especially in the event of structural shocks such as COVID-19 pandemic.

Ultimately, there is a need to synchronize containment measures across the region in an effort to develop an EAC trading bloc wall against COVID-19. Otherwise, the effort by a select EAC Partner States to aggressively attempt to contain the virus while others approach the disease with slackness will go to waste. This is because countries within the EAC trading block that approach the COVID-19 with laxity will continue to be a super spreader hot spot in a region where there is free movement of labour, goods and services. Furthermore, apathy by some Partner States in containing COVID-19 could most likely induce sluggishness in lifting trade and travel restrictions between the EAC trading bloc and its trading partners because some partner countries are not open about the extent of the COVID-19 spread and are also not aggressive enough to abate its contagion rate.

Also in the interim, both monetary and fiscal policy has been aimed at soothing the distortionary effects of COVID-19. However, while COVID-19 has rattled EAC Partner States economic systems, the effects of which could be long-term, unfortunately both

monetary and fiscal policy regimes across the board have been silent about long-term strategic policy choices. For example, on the upsurge in the digital economy due to COVID-19, what is the direction of fiscal and monetary policy regimes going forward? What is the optimal timing for the fiscal cliff? That is, what is the optimal time for COVID-19 induced tax relief and spending to come to an end?

Furthermore, the success of livelihood relief and economic recovery programmes was partly hinged on the existence of socioeconomic data collection and targeting system based on a mix of community-based identification and survey information for purposes of easing vulnerable segments of the respective EAC Partner States populations affected by COVID-19. Indeed, the success of the COVID-19 relief and economic recovery programmes in Rwanda was on account of the pre-COVID-19 social protection programmes such as the Vision 2020 Umurenge Programme or VUP (cash transfers, public works, and economic empowerment), Girinka (one cow per poor family), and Ubudehe (community projects). The aforementioned programmes ensured that COVID-19 relief and economic recovery efforts were fairly well targeted to the persons in need. As such, it is prudent that the EAC Partner States, using their respective national identification frameworks and survey data, maintain a database of households by livelihood, such that in the event of a shock, targeting livelihood relief is allocatively efficient.

Finally, the main risk to the EAC Partner States economic outlook relates to the persistence of the COVID-19 in 2021, especially given that richer economies have booked at least 51% of potentially successful vaccines. Unfortunately, because each Partner State is negotiating independently with vaccine manufacturers, this undermines the leverage the EAC trading bloc would have had on pricing and supplies. This is especially so if the EAC trading bloc had negotiated for vaccines as a single buyer, implying discounted vaccine prices. Besides, it would also imply synchronized inoculation across the trading bloc. Otherwise, under the current sovereign purchase of vaccines, inoculation across the region is likely to be haphazard. This is because front-runner countries will most likely achieve high levels of inoculation yet right at the border lies a super spreader neighbouring EAC Partner State that is lagging behind on vaccine procurement, not to mention inoculation. Since there is co-movement in economic activities among EAC Partner States, the persistence of the COVID-19 in a given EAC Partner State is likely to undermine economic activities among the other EAC Partner States. Furthermore, the low stocks of vaccines procured imply persistence of COVID-19 containment measures, hence undermining economic recovery.

Notes

1. Severe Acute Respiratory Syndrome Coronavirus 2.

2. A strain of the same virus, the Severe Acute Respiratory Syndrome Coronavirus 1 (SARS-CoV-1), affected nearly 8,000 people in 2002/03.

3. Tanzania stopped releasing COVID-19 statistics at the beginning of May 2020.

4. Note that data gap challenges imply that COVID-19 cases and related morbidity could be higher than captured across the EAC Partner States with the exception of Tanzania that stopped publishing COVID-19 statistics.

5. Note that according to the IMF (2021), real GDP growth for Tanzania is 1% in 2020; however, this contradicts GoT projected real GDP growth of 5%. GoT attributes the 5% real GDP growth on account of not imposing lockdown measures on economic activities.

6. The PMI is a composite index, calculated as a weighted average of five individual sub-components; New Orders (30%), Output (25%), Employment (20%), Suppliers' Delivery Times (15%), and Stocks of Purchases (10%). It gives an indication of business operating conditions in the Ugandan economy. The PMI above 50.0 signals an improvement in business conditions while readings below 50.0 show deterioration. The PMI is compiled monthly by IHS Markit. The index is computed using the recorded reductions during the month of the following components output: new orders; employment; supplier's delivery times; and stocks of purchases.

7. CIEA is an index that is correlated with the current level of economic activity (such as real GDP). It is constructed using seven variables; that is, private consumption estimated by VAT, private investment estimated by gross extension of private sector credit, government consumption estimated by its current expenditure, government investment estimated by its development expenditure, excise duty, exports, and imports. Data comes with a lag of one month.

8. Micro, Small and Medium Enterprises (MSME) constitute 90% of Uganda's private sector. The MSME sector is dominated by informal Micro and Small Enterprises (MSE) that contribute 85% to total employment and over 50% to the national GDP, and as such, any shocks to the sector directly affects Uganda's economy.

9. Progression to secondary education rate is 59%, 71%, 73%, and 76% in Uganda, Tanzania, Rwanda, and Burundi, respectively; while primary education completion rate is 59%, 68%, 53%, and 27% in Burundi, Tanzania, Uganda, and South Sudan, respectively (World Bank, 2020a).

10. The minimum regulatory requirement is 10%.

11. The statutory limit is 14.5%.

12. End of period exchange rate 2,298.5

13. End of period exchange rate 2,287.9

14. http://mefmi.org/2020/01/17/government-of-tanzania-conducts-debt-sustainability-analysis/

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