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How is Uganda likely to benefit from DRC's membership in the EAC bloc?

Executive Summary

The Democratic Republic of Congo (DRC) has applied to join the EAC to tap into the regional benefits of the bloc. DRC's membership is expected to boost regional trade given its vast market of 81 million people, geographical proximity and natural resource base. Results from our study show that Uganda's formal exports are likely to increase by USD 60 million annually. At a sectoral level, industries in food and beverages, metal (iron and steel), and mineral ores are likely to be the most impacted. However, the realisation of these benefits is contingent on the government's efforts to; invest in agro-industrialisation to add value to agricultural products, iron and steel industry, and pursue long-term but deliberate investment in high-value manufactured products.

Introduction

In June 2019, the Democratic Republic of Congo (DRC) expressed interest to join the East African Community (EAC). More succinctly, the country seeks to tap into the bloc's benefits of the regional trade, expanded markets, and attraction of foreign direct investment (Tabaro, 2019). Noteworthy, the EAC is considered the most successful among all the Regional Economic Communities (RECs) in Africa, with the highest Regional Integration Index and intra-regional trade (African Union, 2020).

Many observers consider DRC's interest in EAC as a game-changer to the bloc's trade performance due to its huge market of 81 million population and vast natural resources. Notably, the country is the world's largest producer of cobalt, a component in the manufacture of rechargeable batteries for electric vehicles, and Africa's leading copper producer. Besides, DRC's geographical proximity positions it as a strategic trade partner for Uganda and other EAC member states. For instance, in 2019, the country surpassed Kenya as the leading export destination for Uganda's exports, estimated at USD 267 million, which represents 14 percent of the country's total export bill (UBOS, 2020).

Whereas DRC's membership presents huge trade benefits to the EAC members, these vary across different sectors and members depending on their trade patterns and economic structure (Mitsuo & Nyuyen, 2008). Notably, more industrialised members that produce highly competitive products are likely to benefit from DRC's membership at the expense of the least developed ones (Mold & Mukwaya, 2015). Additionally, sectors characterised by a poorly regulated and non-competitive environment risk being outcompeted in a regional bloc framework (Cuts international, 2010). In light of these dynamics, the brief examines the potential trade effects of DRC's membership on Uganda and identifies which economic sectors are likely to gain at the expense of others.

Data and Methodology

The brief used secondary data from the Trade Map database of the International Trade Centre (2020). We adopt the analytical framework that follows two approaches; (i) trend analysis of the trade flows between Uganda, DRC and the Rest of the World (ROW) in the period 2010-2020. This analysis seeks to understand the competitiveness of Uganda's exports to replace DRC's imports from the ROW. Secondly, we adopt the excel-based Single Market Partial Equilibrium Simulation Tool (SMART)[1] to estimate trade effects arising from DRC's membership using the most current disaggregated data of 2018. Note that whereas the aggregated country data for both countries was available up to 2020, the disaggregated data (along the product lines) was up to the year 2018.

1 The SMART is a partial equilibrium model developed by the United Nations Conference for Trade and Development (UNCTAD) and the World Bank during the 1980's, mainly to assess the impact of General Agreement on Trade and Tariffs (GATTs) rounds.

Results

Data shows that Uganda is a net exporter to DRC. For instance, export trade is valued at USD 267 million in 2020 compared to imports at USD 10 million (Figure 1). Additionally, this trade balance has been rising over the past decade from USD 174 million in 2010 to USD 257 million, equivalent to a 47.1 percentage growth. Despite this growth, Uganda's share in DRC's total imports has stagnated around 3.1 percent for the past decade. This is mainly because DRC mainly imports high value manufactured products including machinery, electronics, motor vehicles, and pharmaceutical products that Uganda has no competitive edge to produce. Data from Trade Map (2021) shows that DRC imported manufactured products estimated at 40 percent of the total import bill in 2018. This clearly shows Uganda's long-term opportunity to penetrate the DRC market by investing in high-end manufactured products such as electronics, pharmaceuticals, and machinery to tap into the DRC markets.

Table 1 summarises the top 10 products imported by DRC in 2018 as classified according to the Harmonized Standard Classification (HSC). The results indicate Uganda accounts for a very insignificant share of DRC's top imports, which affects its total export revenue from its bilateral trade with DRC. Noteworthy, the main products include machinery (0.13 percent) and mechanical appliances (0.31 percent), vehicles (0.14 percent), electrical equipment (0.31 percent). This is largely because developed countries with advanced manufacturing industries produce these products as opposed to Uganda. Even in sectors where Uganda has grown in production capacity, the country commands a weaker market share- lime and cement (5.1 percent); iron and iron and steel (0.84 percent). Relatedly, Uganda has been emerging in pharmaceutical, automotive and electronics that exhibit great potential. Remarkably, the recent development efforts in the automotive industry by Kiira Motors cooperation (Kiira EV) and the mobile phone manufacturing plant in Namanve Industrial Park are critical to tapping into the DRC market. Additionally, the investment efforts in the pharmaceutical industries whose exports have grown in the recent past from CIPLA Uganda, Quality Chemicals Limited should be scaled up.

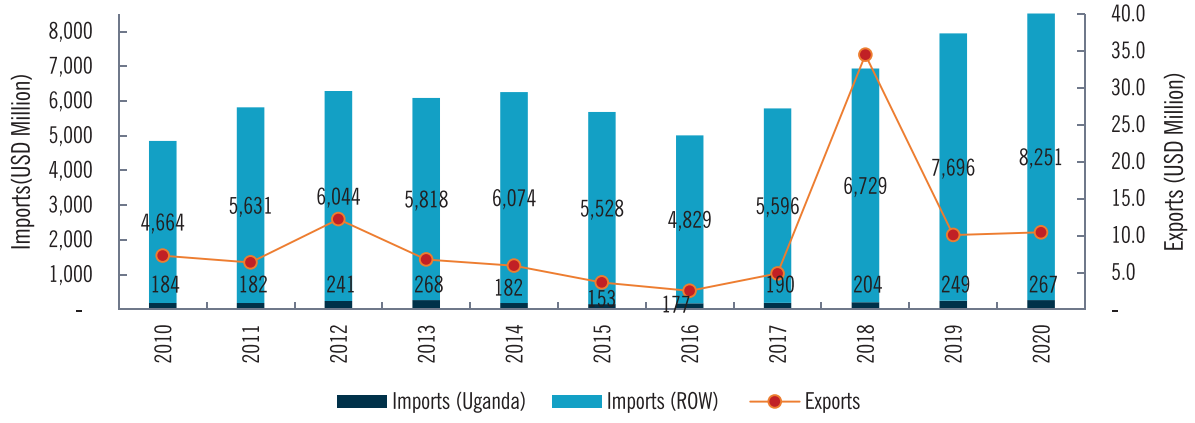
Table 1 Uganda's market share in the top 10 DRC's imports in 2018

HSCODE	Products	Amount(USD million)	Market share
84	Machinery, mechanical appliances	1,064	0.13%
87	Vehicles and railway accessories	571	0.14%
25	Lime and cement & Sulphur, salts	534	5.10%
28	Inorganic chemicals	446	0.07%
85	Electrical machinery and equipment	422	0.31%
27	Mineral fuels, mineral oils	305	0.26%
73	Articles of iron or steel	299	0.56%
39	Plastics and articles thereof	240	0.69%
30	Pharmaceutical products	211	0.37%
72	Iron and steel	174	0.84%

Source: Authors computation based on Trade Map (2020)

To further illustrate the dominance of DRC's imports by manufactured products, analysis of the 10 top exporters of the DRC shows that the main sources of the country's imports are China, South Africa, Zambia, Belgium, USA, and France, among others (Table 2). Unlike Uganda, these are mainly countries with developed manufacturing sectors with the competitive edge to readily supply electronic and manufactured products. On the EAC front, Kenya is the only member country that ranks among the top exporters over the past decade, given that it's the most advanced industrial member in the EAC. However, its share has since declined, evidenced by a fall in percentage share from 3.7 percent in 2010 to 2.0 percent in 2018. Notably, China's market power in the DRC market has grown due to its distinctive competitive edge in exporting machinery and electronics compared to other competitors such as South Africa and Belgium. For instance, between 2011-2018, the value of DRC's machinery imports from China grew more than threefold from USD 106 million to USD 382 million. The same imports from South Africa only rose by 7.6 percent in the period under review (ITC, 2020).

Figure 1 DRC's Imports, exports from Uganda, and the Rest of the World (2010-2020)



Source: Authors computation based on Trade Map (2021)

Table 2 Top sources for DRCs imports, 2010-2018

Country/Year	2010	2011	2012	2013	2014	2015	2016	2017	2018
China	11.0	14.1	13.0	13.5	19.7	22.0	19.7	18.2	23.9
South Africa	19.6	18.7	23.0	19.3	17.9	16.0	15.5	16.5	17.4
Zambia	7.5	9.9	12.5	16.9	11.6	8.4	8.0	9.9	11.7
Belgium	8.3	7.5	7.0	6.9	6.1	7.4	7.6	8.3	5.5
France	5.3	4.2	4.3	4.2	3.0	4.2	5.1	2.7	1.7
Netherlands	2.9	2.6	2.2	2.2	2.2	1.6	1.7	3.3	4.0
India	0.3	0.1	1.9	2.1	3.2	5.0	4.6	3.9	3.8
Kenya	**3.7**	**3.4**	**3.4**	**3.0**	**3.5**	**3.3**	**3.9**	**3.4**	**2.0**
Germany	2.9	2.7	2.6	3.0	2.5	2.5	1.8	1.5	1.4
USA	2.2	2.8	3.1	2.4	2.6	2.1	1.6	1.4	1.1
Total (% of total DRC imports)	**73.8**	**73.2**	**83.1**	**84.1**	**83.5**	**82.6**	**83.2**	**83.1**	**83.6**

Source: Authors computation based Trade Map data (2020)

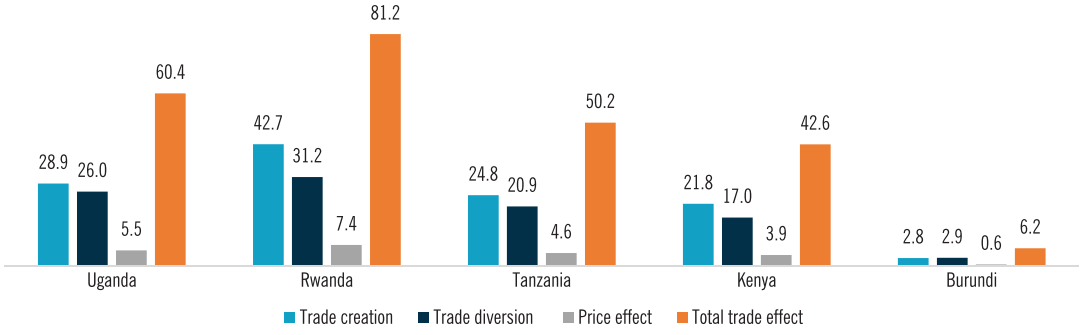
Analysis of potential trade effects accrued to EAC partner states shows that Rwanda and Uganda have the most considerable trade benefits compared to other member countries. Specifically, free trade with DRC will increase exports from Rwanda and Uganda by USD 81.2 million and USD 60.4 million, respectively. This high share in exports by the two countries is attributed to geographical proximity as well as the high pre-FTA trade between the two countries and DRC. Worth noting is that Rwanda currently has designated export zones with DRC, which boosts the trade between countries and renders the country the highest trade competitor for the DRC market. Across all EAC countries except Burundi, exports to DRC are likely to be driven by trade creation (shift of DRC imports to EAC from non-EAC members due to reduction of tariffs) contrary to the trade diversion effect. For instance, Uganda's trade creation effect is estimated at USD 28.9 million compared to USD 26.0 million in trade diversion. Burundi will accrue the lowest trade effect estimated at USD 6.2 million, primarily due to low bilateral trade with DRC.

Figure 2 shows the analysis of the sectoral distribution of the net trade benefits based on HS Code level 2. The results show that Uganda's trade gains are largely in food and beverages (USD 29.3 million), metal products (USD 8.7 million) and mineral products (USD 8.3 million). Uganda will gain most from sugar, palm oil, broken rice, sweet biscuits, and wheat flour, i.e. particularly for the food and beverage industry. Generally, the country derives greater trade benefits from processed food and beverages compared to raw agricultural products and machinery. The high share is primarily explained by Uganda's manufacturing sector structure, which is dominated by food and beverages (accounting for 60 percent of the total output) from the sector (IGC, 2020). Hence, liberalising trade with DRC presents Uganda with an opportunity to transform the agricultural sector from the farm to more value-added/agro-industrialisation in line with the third National Development Plan (NDP III).

Similarly, Uganda also has potential in the metal product category, particularly in the iron and steel industries, where the country has the largest advantage in line with Uganda's industrial strategy. In the mineral category, the government will gain from Portland cement and petroleum products. As indicated earlier, Uganda's benefits from manufactured machinery and electronics are lower owing to limited technological advancement to produce these products.

Table 3 shows the top products that will reap the highest trade effects for Uganda at HSC level 6. Uganda will realise the biggest trade effects from Palm oil products (USD 8.2 million), Portland cement (USD 6.8 million) and sugar (USD 6.4 million). Other products that yield high benefits to Uganda include beer (USD 2.7 million), broken rice (USD 2.6 million), iron sheets (USD 2.4 million), Tubes, pipes and hollow profiles of iron (USD 2.3 million), medium oils and preparation (USD 1.4 million). It is also important to note that all the top products are value-added products-mostly from light manufacturing industries. This underscores the need for Uganda to industrialise and produce high-value products to tap into the DRC market.

Figure 2 The potential in exports of EAC countries with DRC membership (USD million)



Source: Authors computation based on the SMART-WITS simulation

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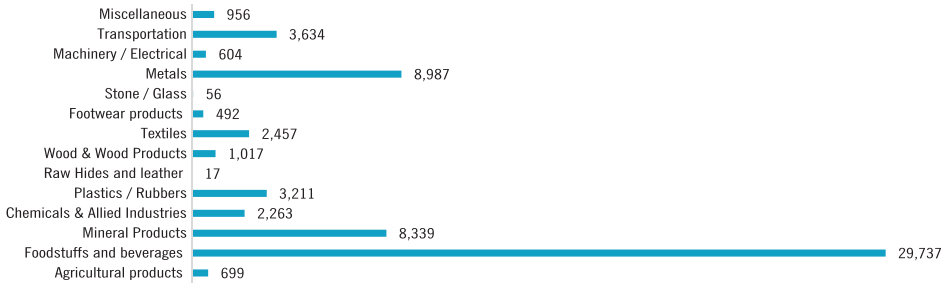
Figure 3 Sectoral distribution of the growth in Uganda's exports to DRC (USD 000)



Source: Authors computation based on the SMART-WITS simulation

Table 3 Top ten commodities with the highest trade effects

HS CODE	Products	Total trade effect
151190	Palm oil and its fractions	8,219
252329	Portland cement	6,816
170199	Cane or beet sugar	6,483
220300	Beer made from malt	2,743
100640	Broken rice	2,653
190531	Sweet biscuits	2,396
721049	Flat-rolled products of iron	2,368
110100	Wheat or meslin flour	1,499
730690	Tubes, pipes and hollow profiles of iron	1,479
271019	Medium oils and preparation	1,402

Source: Authors computation based on the SMART-WITS simulation

Conclusion

We analyse the likely trade effects of the DRC membership in the EAC bloc and further delve into the sectoral distribution of these benefits. The results show that Uganda and Rwanda are the largest beneficiaries of the trade liberalisation with DRC—export growth is estimated at USD 81.2 million and USD 60.4 million, respectively. The results also show Uganda will benefit through the trade creation effect (arising from increased DRC imports from Uganda due to eliminating tariffs with DRC), contrary to diverting trade from non-EAC members. The most extensive sectoral benefits will be realised in food and beverages, metal products, and minerals at a sectoral level. In light of these findings, our study offers the following recommendations;

- To realise the enormous trade benefits in the food and beverages industry, Uganda needs to invest in agriculture and high-value addition agro-processing in line with agro-industrialisation (AGI) under the NDPIII. This calls for strategic investments along the food value chain, right from production to marketing, to meet standard requirements in the DRC market.
- Uganda should adopt a long term strategy of building its capacity to produce high technology products such as machinery, electrical equipment and motor vehicles, which are DRCs leading imports, to overcome supply constraints. In the short run, the country can establish itself as a re-export/assembling hub to supply high-value manufactured products such as electronics and machinery with a strategy to manufacture these products in the long run.
- To increase the exports of iron and steel products, the government should promote the growth of the iron and steel industry's production and attract private investment to overcome the supply constraints such as high taxes and high costs of power.

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