WORLD TRADE ORGANIZATION CHAIRS PROGRAMME

SCHOOL OF ECONOMICS

UNIVERSITY OF NAIROBI

**RESEARCH DISSEMINATION WORKSHOP on**

# EFFECTS OF COVID-19 ON INTERNATIONAL TRADE AND POST-RECOVERY STRATEGIES IN KENYA

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## SUMMARY OF RESEARCH FINDINGS

The measures taken by different government to combat the spread of COVID-19 translated to NTBs which disrupted trade (global and regional value chains) not only in the East African region, but also the whole world.

COVID-19 lead to a drop in GDP dropped due to reduced aggregate demand when businesses closed, while others laid off many workers as Kenya entered into a recession and unemployment increased. Kenya’s Foreign exchange reserves fell to 7.8 billion dollars by the end of 2020, down from 8.96 billion dollars in 2019 due to reduced net inflows as a result of international lockdowns to contain the COVID-19 pandemic. Effectively Kenya's national currency depreciated by 8.9% to KShs 110 per US dollar in 2020, down from KShs 101 in 2019.

COVID-19 further disrupted exports of EAC countries. Burundi had the greatest slump in exports in 2020 (-20%) followed by Uganda (-16%), Kenya (-13%), Rwanda (-12%) and Tanzania (-3%) respectively.

The advent of COVID-19 in 2020 led to a drop in imports in all EAC countries. The magnitude of collapse was highest in Burundi (40%) followed by Uganda (12%), Rwanda (8%), Tanzania (2%) and Kenya (0.2%) respectively. Kenya’s top imports; ores,slag and ash declined by 2% in 2019 and by 34.4% in 2020, articles of base metal declined by 1.5% in 2019 but by 12.7% in

2020, machinery increased by 5.1% in 2019 but decreased by 5.4% in 2020 and railway products decreased by 1.9% in 2019 and by 7.4% in 2020. The largest negative impact of the spread of COVID-19 was observed on imports of fuel and lubricants as imports in this category dropped by 37%.

In terms of shares of total exports, Kenya made up 42% of exports from EAC in 2018. However, this rate reduced to about 37% in 2019 and 2020.

In terms of trade balance of goods (exports less imports) all EAC countries had a trade deficit over the three years 2018 to 2020, meaning that imports surpassed exports.

Between 2018 and 2020, the top ten export products (ores, slag and ash; mineral fuels, oils & product of their distillation; etc; and iron and steel) made up at least 55% of total exports in EAC countries with Burundi and Rwanda having the highest rates (93.7% and 89% respectively). This indicates low product diversification in EAC countries.

Outside Africa, China, the United Kingdom and the United States of America are the major trading partners of all EAC countries, particularly in Kenya where the three countries accounted for close to 18% of total exports. Overall, there is little market diversity in exports of most EAC countries: at least 90% of exports from Burundi, Rwanda and Uganda were to the top twenty trading partners. From 2018 to 2020, China was by far the top import trading partner of EAC countries and about 21.3% of Kenya's goods imports were from China.

The largest negative impact of COVID-19 is observed on imports and exports of industrial supplies. Imports reduced by 15 to 23% while exports reduced by 25 to 35%. This shows that manufacturing sectors that are dependent on these industrial supplies were the most affected by COVID-19. Specifically, the results reflect a situation where COVID-19 led to a shutdown of some manufacturing industries. This led to a decline in the demand and supply of industrial supplies in the country.

Activity in the accommodation sector and the restaurant subsector was severely impacted by the pandemic as international travel was suspended for much of 2020. Hotels closed or significantly scaled down their operations since movement restrictions were imposed in most countries. From March 2020 to June 2021 receipts from services exports fell sharply reflecting the collapse of international travel and transport. The subsector contracted by 57.9%.

The pandemic caused a serious drop of FDI to Kenya as it muzzled trade arrangements across the world. The UNCTAD (2021) investment report on FDI shows that Kenya attracted US $ 717 million worth of FDI investments in 2020 compared to US $ 1.3 billion in 2019. This was the second straight drop considering that US $ 1.6 billion was attracted in 2018. Kenya lagged its neighbors Uganda at US $ 823 million and Tanzania at US $ 1.013 billion.

COVID-19 led to more formalization of informal cross border trade as borders were closed and movement across the borders curtailed.

Even as the Government of Kenya is optimistic of Economic Recovery in 2021 gauging by the 2020-2022 Economic Recovery Strategy, COVID-19 is not yet over. The pandemic is still with us and Kenya is now experiencing the 4$^{th}$ wave of the pandemic. The prospect of re-imposing lockdowns and other restrictions, while necessary to bring the pandemic under control, could have devastating economic and social consequences for many Kenyans. At the same time, the initial Kenya Government's economic stimulus plans that provided cash assistance to the most vulnerable, reduced taxes, among others have already come to an end. The situation of most Kenyan individuals as well as households still remains uncertain. It is therefore important for the government to put in place strategies that can cushion individuals and households against falling into the poverty trap. Some firms that closed when the pandemic struck have not opened as yet.

Kenya still faces the risk of weak external demand for its exports as countries continue to put in measures such as lockdowns and travel restrictions to prevent the spread of new COVID-19 variants. There are also risks of reduced international tourist arrivals and increased public expenditure pressures to cushion the public and private sectors against continued reduced demand and rising cost of living. Thus means that the Government of Kenya needs to come up with strategies that require use of appropriate monetary and policy measures to preserve macroeconomic and fiscal stability while strengthening the resilience of the economy. These strategies will help Kenya in its journey of economy recover and achieve sustainable development. The economic recovery strategies are supposed to mitigate the adverse socioeconomic effects of the COVID-19 pandemic and facilitate the opening up of the economy. The proposed strategies are designed to accelerate economic recovery and the attainment of sustainable economic growth. Some of the strategies should be implemented in the short term such as making sure that all adult Kenyans are vaccinated, others medium term such as lowering taxes, temporary basic income for those who lost their jobs due to the pandemic, subsidies on essential commodities such as energy, gas, water, food and transport in order to reduce the cost of production and increase consumption, job retention programs in the form of compensation for firms with income equivalent to wages or salaries retained during this time would provide an impetus to allow for continued operation and rehiring of workers by the firms, restructuring public debt towards longer maturity loans and uptake of new loans on concessional basis as well as use resources efficiently by reducing corruption. Long term strategies include restructuring the economy towards more domestic production in order to achieve goal of being self sufficient by becoming both consumer and producer of goods and services; harnessing digital technology can accelerate Kenya’s way to economic recovery after Covid-19 devastating effects. Digital gig economy apps offer opportunities for autonomy and self-employment and aggregation of demand for services and products. This requires investment in electricity, digital tools and infrastructure to make internet enabled devices and internet services affordable and accessible to majority of Kenyans. Strengthening E-commerce which is considered the engine driving the economies can hence greater reliance on online services connecting supply chains and facilitating merchandise trade is one strategy that Kenya should fully embrace. This requires automation and streamlining of border procedures, simplification of fees and fostering inclusion of MSMEs in the consultation. Need for digitalization and simplification of import, export and transit procedures such as paperless trade should be accelerated as well as expediting electronic lodging of documents in advance, electronic payment of all trade-related taxes, digital certificates and signatures, or 24/7 automated processing of trade declarations.

For Kenya’s exports to compete in both the regional and global markets, they must meet international product and process standards. Need to strengthen technical regulations, develop and implement these standards, conformity assessments, metrology, have laboratories accredited and provide enabling infrastructure for industries to grow. Reduce the behind the borders regulations that act as restrictions to trade in services –they impede FDIs from entering the market and prevent local service suppliers from becoming competitive in export markets.

Need to diversify not only export destinations but also import sources, be inclusive among the participants in productive activities, diversify export products and not just rely on a few products, add value to export products. Other types of diversification include, intermediate goods diversification, quality diversification, and goods-to-services diversification. Kenya needs to diversify and transform its economy by strengthening productive capacity of the private sector to transform raw materials locally, improve domestic resources mobilization, reduce the continent dependence on external financial flows.

Bilateral and regional agreements could ease import and export restrictions on input supplies of key routes.

EAC, COMESA, the tripartite agreement that brings together the South African Development Community (SADC), COMESA and EAC, the African Continental Free Trade Area (AfCFTA) can accelerate economic diversification within an integrated regional economy.

Enhancing regional integration means harmonizing responses in case of future pandemics as well as providing opportunities for the expanding sectors such as the services sector

Kenya is well positioned geographically - in the East, Indian Ocean facing Asia and Australia with access to key shipping lanes between the Mediterranean and Indian Oceans.

Kenya can take advantage of this geographic advantage to work towards greater diversification of its economy and taking advantage of international opportunities such as the fiber optic connection to conduct e-commerce.

The AfCFTA's market, a combined population of one billion people and a GDP of over US$3.4 trillion provides an opportunity for product diversification, industries to grow, provide home grown solutions and drive regional value chains. The FTA is the only conduit/vehicle for framing trade agreements with African countries - increases the continent's bargaining power in the global market preventing fragmentation of trade agreements among countries and their trading partners. The LAPSSET infrastructure project will accelerate the inter-linkage between Kenya and other African countries leading to more trade between Kenya and the rest of the African continent. The AfCFTA will increase Kenya's intra-African trade by reducing the tariff and non-tariff barriers on its trade with African countries. The FTA can enter into PPPs in R&D; deepen regional integration in order to pool financial resources to reduce the risk of shortages as well as collaborating with international development partners who can provide technical assistance.

Kenya can also take advantage of the WTO Trade Facilitation Agreement (TFA), WB Trade Facilitation Support Program (WB-TFSP), UNCTAD, Development partners such as AfDB, EU, OECD among others in aligning their trade practices with the TFA. Such trade facilitation measures will not only support African countries diversify their economies, but also leverage on technology, keep up with innovations but also reduce their vulnerability to exogenous shocks.

Aid for Trade will promote import diversification by increasing the number of both import commodities and import partner countries. All three components of AfT (aid for trade-related infrastructure, aid for building productive capacity, and aid for trade policy regulations and trade-related adjustment) contribute significantly to the import diversification of recipient countries.

Enhanced cooperation among EAC and AfCFTA govts, international organizations and the private sector is critical to ensure that all trading partners have sufficient information to make decisions. This can help promote transparency on essential goods, in particular with regard to production capacity; facilitate trade and mutual recognition of standards, in particular for emergency goods; and to hold inventories to prevent excessive stockpiling. These governments and trading partners can cooperate to collect and share information on potential concentration and bottlenecks upstream and/or develop stress tests for essential supply chains. They can also enter into PPPs in R&D, deepen regional integration in order to pool financial resources to reduce the risk of shortages as well as collaborate with international development partners who can provide technical assistance.

**Conclusion and Key Message**

- Government of Kenya should pursue strategies to support lives and livelihoods of its citizens, support industries to remain in operation
- At the same time take advantage of the opportunities offered by the regional integration, African Continental Free Trade Area, development partners in the form of trade facilitation as well as aid for trade.
- This will chart the path to sustained economic growth and development.