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Growing Protectionism and its Implications on Kenya's Foreign Trade with the USA and UK

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Background

Until after the global financial crisis, interdependence of world economies and increased cross-border trade in goods and services underpinned the growth of world economies. World trade grew faster than output by around one and a half times since 1991. At the same time, there was increasing degree of openness in trade, rapid developments in information and communication technology, falling cost of transportation and increasing in cross-border activities, with more domestic companies increasingly being involved in international trade.

However, the unprecedented 12.2% decline in world trade in 2009 triggered a rapid descent into protectionism to shield domestic businesses and jobs from foreign competition. Anti-globalization rhetoric also gathered momentum especially in the US and most parts of Europe. Indeed, the world's top 60 economies introduced 7,000 protectionist trade measures since the financial crisis. Thus, the impact of the crisis quickly depressed economic indicators, raised the levels of inequalities and social deprivation, and fuelled resentments against free trade. Subsequently, the backlash against progressive cultural changes brought about by greater global openness and the threats associated with international migration and terrorism added even greater impetus to proponents of protectionism.

Protectionism of world trade takes the form of tariff and non-tariff measures, including human and plant health, technical standards and various forms of production conformity requirements. Ideally, protectionism breeds regulations which slow movement of persons, goods, finance and other services. Besides, power plays of protectionism and economic openness influence political landscapes as happened in the latest general election outcomes in the US. It is widely believed that President Trump won the US elections on the premise that prevailing trade deficits and unemployment were largely attributed to unfair trading practices by her bilateral partners, notably China and Mexico, and regional economic blocs including the North American Free Trade Agreement (NAFTA). In fact, the US subsequently withdrew its membership from the Trans-Pacific Partnership (TPP) agreement involving Australia, Asia and other countries in the Pacific Rim, signalling her strong desire towards fomenting inward-looking policies. Regarding the UK, the referendum vote taken on 23rd June 2016 endorsed its exit from the European Union. In the UK, the referendum outcome was largely driven by protectionist ideals including rallying calls for restoration of national sovereignty, greater flexibility in policy and decision making and immigration issues.

Bilateral Cooperation between Kenya and the United States of America

Kenya and the USA have a long-standing partnership. In a recent invitation of Kenya's President to the White House, the two leaders committed to expand economic cooperation and trade and investments, and strengthen social, peace and security matters. Among the issues on top of the bilateral ties include the fight against terrorism, peace building efforts and governance.

Trade between Kenya and the USA is conducted within the frameworks of the Most Favoured Nation (MFN) and the African Growth and Opportunity Act (AGOA). The two countries enjoy cordial trade and investment bilateral policies as provided for in the AGOA Act which give Kenya and other Sub-Saharan African countries' duty free and quota free access to the US market. Total trade between the two countries is relatively low at about 5 per cent of total Kenya trade. Latest statistics indicate that total trade between the two countries marginally increased from US$ 911 million in 2016 to US$ 1,046 million in 2017. The exports of duty free-quota free exports under AGOA declined by about US$ 16.4 million from US$ 344 million in 2016 to US$ 327.6 million in 2017. Textile goods are the leading export products and constitute 60% of exports followed by agricultural products. The key imports from the US include aircraft, machineries, cereals, and electrical equipment. There was a decline in total imports largely due to reduced importation of aircraft and transportation equipment.

Overall, export performance has remained below targets despite the significant market access opportunities the AGOA framework offers, with the share of exports to the US market being 3% of total exports in 2017. The bulk of exports are largely textiles and apparels, which also face stiff competition from other countries including Bangladesh and China. The US is the biggest market for apparels valued at over US$ 100 billion and Kenya barely captures 1% of it despite the preferential treatment accorded to her export products. On the positive side, the renewed version of AGOA Act 2015 provides for use of third country fabrics, and this allows African apparel exports to the US to remain eligible under AGOA even when the fabrics used in producing those goods are imported from non-AGOA countries.

Further, although capital investments from the US declined by 7.9% to US$ 141 million 2017, nearly US$ 900 million work of commercial deals were secured during the recent visit by the Kenyan President to the US. The establishment of the US–Kenya Trade and Investment Working Group is further expected to boost investment levels especially in infrastructure and other productive sectors.

Implications of Changes in US Trade Policies on Kenya

Despite renewed efforts to strengthen bilateral ties between Kenya and the US, the growing protectionism of the US market in the form of higher protection of domestic firms poses some challenges moving into the future. The AGOA window is a unilateral agreement and the US government is at liberty to make any alterations without reference to beneficiary countries. This was recently demonstrated by the suspension of Rwanda from AGOA eligibility status following the ban on importation of secondhand clothing into the country. The US government's policy to protect and safeguard the interests of the Secondary Materials and Recycled Textiles Association (SMART) was meant to counter proposals by EAC countries in 2016 to impose a phased-out ban on secondhand clothing and increase import duties on these goods.

Therefore, effective protection of domestic and regional textile industries in the EAC is severely weakened and the sustainable growth of textile, leather and automotive sectors grossly undermined. Productivity and competitiveness of these industries holds the key to the region's successful industrialization and structural transformation of the regional economies.

Strategies and Coping Mechanisms

Kenya and the other EAC partner states should lobby for transformation of AGOA into a bilateral agreement within the framework of the proposed US-Kenya Trade and Investment Working Group. This may facilitate identification of priority areas for collaboration and capacity development targeting specific export commodities, including skills and value addition to enhance sustainable development of local industries. This would make the investment environment more predictable and guarantee long term returns to local and foreign investors.

In addition, it would be important to effectively support implementation of the EAC and national AGOA strategies which have already been developed. Besides, the envisaged EAC-US trade and investment partnership is pertinent especially in defining the relations beyond the AGOA 2025 window. Close partnership would support trade facilitation and industrialization in the region. The latter would also promote diversification of the export base from apparels, for example services sectors, including tourism and transport sectors, for full exploitation of the 6,000 AGOA eligible tariff lines. Besides, Kenya should take advantage of the direct flights between the Jomo Kenyatta International Airport (JKIA) and New York city to promote tourism and market Kenyan products in US markets. Greater efforts should therefore be directed towards enhancing efficiency in related infrastructures, strengthening security and surveillance, expansion of the scope of tourism products, and marketing. Harnessing the potential of the tourism sector can support inclusive growth, employment and sustainable development. Kenya should take advantage of the US good-will for maintenance of regional peace and security and reduction of the threats of terrorism. Kenya's strategic location, connectivity and economic resilience places it at a locus for strengthening relations beyond trade and investments.

Implications of Protectionism on Kenya's Relations with the United Kingdom

Kenya and the UK have had long-standing bilateral ties guided by the Lome Conventions (1975-2000) and later the Cotonou Agreement (2000-2007) followed by the Africa Caribbean Pacific (ACP) and the European Union (EU). It is also a former British colony and a member of the Commonwealth which further strengthens their political and socio-economic ties.

The UK is one of Kenya's major trading partners with total trade standing at US$ 686 million in 2017. The trade balance is in favour of Kenya, with total exports being US$ 385 million against US$ 300 million of imports from the UK in 2017. Approximately 6% of Kenyan exports went to UK and 2% of imports were sourced from UK during the year. Tea, flowers fish and vegetables account for the largest share of total commodity exports while the major import products are motor vehicles, tractors, aircraft parts, and secondhand clothes. Imports from UK are diversified, unlike the exports which are concentrated on a few products. UK is the second largest export destination for cut flowers after the Netherlands.

Besides, UK is one of Kenya's most committed investment partners over many years. At the end of 2015, UK was among the top five major sources of foreign direct investment (FDI) inflows to Kenya, with investments worth US$ 41 million. British FDI is largely in the telecommunications and financial services sectors and development aid and infrastructure projects. UK development assistance is generally geared towards driving sustainable, inclusive economic growth, including progress on health, education, social protection and other basic social services.

Beyond direct investments, the UK also funds key trade facilitation programmes in the East Africa region under the Trade Mark East Africa (TMEA). TMEAs programmes help increase access to markets for Kenya's businesses, increase trade and reduce transport costs and time. Specifically, TMEA's support for the modernisation of the ports, including Mombasa, and one-stop border posts including at Taveta, Busia, Malaba and elsewhere in East Africa is helping transform cross border trade in East Africa.

The recent visit to Kenya by the British Prime Minister could only have strengthened existing economic and political ties between the two countries. Kenya and the UK signed an agreement to ensure proceeds of corruption and crime hidden in Britain are returned, in an effort to fight corruption. Defence and military support to Kenya was another area discussed during the visit.

Despite the cordial relations between the two countries, the UK is among the top countries which have put in place significant protection measures on health, safety, economic and legal interests. Whereas these measures may have good intensions, some of the obligations placed on producers can be burdensome and amount to restricting access to the UK market despite duty free and quota free conditions. For instance, the traceability requirements compel producers to put in place mechanisms to facilitate tracing and follow-up of food, feed, and ingredients through all stages of production, processing and distribution to guarantee product safety and conformity to generally agreed standards or norms. Given that the bulk of Kenya's exports to the UK are agriculture-based, the regulations require that the export products are traceable, with details recorded, retained and submitted as required by operators.

The other form of restriction relates to entry of independent professionals who are either service suppliers or who work for a service supplier in the UK, otherwise commonly referred to as mode IV supply of services within the WTO framework. These restrictions include recognition of qualifications or certificates, what suppliers can do, on who can supply, and on allowed forms of supply that stem from statute, from rules set by the professional bodies, and from custom and practice.

Besides, the UK has aimed to reduce net migration since 2010 and several policy changes have been introduced to limit immigration of non-EU nationals in one of the three main categories: work, study, and being re-united with their families. Indeed, eligibility criteria to enter the UK for work, for example by professional footballers have become even more restrictive especially for non-EU nationals. These have been driven by numerous factors including increased threat of insecurity and terrorism, increased number of asylum seekers due to wars and conflicts, economic hardships especially among the youth especially from less developed countries, and growing unemployment, resentments and competition for available jobs within the UK itself.

Post-Brexit Relations with UK

Kenya's economic relationship with the UK is intrinsically tied to the latter's membership in the EU. However, trade arrangements will change once the UK officially leaves the EU and the nature of the post-Brexit relationships will depend on the conditions upon which this takes place. Most of the trade arrangements the UK has with African countries, including Kenya, were negotiated under the auspices of the EU. The EU's GSP would no longer apply to trade between the UK and developing countries, including Kenya. If UK exits the EU customs union, any products from third countries would no longer circulate freely within the EU27 member states and might face the EU's common external tariff and other trade policy rules and regulations. This means the agreements will cease to apply or will have to be renegotiated when the UK finally leaves the EU. Indeed, much more is at stake for developing countries, including Kenya, if the UK does not form part of a customs union with the EU and instead decides to offer and negotiate trade tariffs. If the UK were to reduce margins of preference for developing countries, this will increase the duties paid by those countries dependent on such preferences. So far, the two parties have agreed on a 21 month transition period to give businesses and administrations time to adapt, as the UK would stay in a Single Market and Customs Union until 31 December 2020. There is, however, need to negotiate firm commitments on transitional arrangements that extend current market access regimes with the UK beyond the two-year horizon associated with the exit as per Article 50 of the Lisbon Treaty, which could take two or more years.

The UK market is important for Kenya's horticultural products and has been subject to EU technical and standards regulations. Kenya's lucrative cut flower industry, for which UK is the second-largest export market after the Netherlands, is bound to suffer from market access constraints especially if no alternative or effective transitional arrangements are put in place prior to exit of UK from the EU. In addition, should Brexit weaken UK's role, as the world's financial hub, there could be negative effects in domestic banking services given the innovative roles played by leading British banks such as the Standard Chattered Bank in terms of gaps and diminishing consumer confidence.

Furthermore, diplomatic ties could also be affected. Britain has traditionally provided scholarships for undergraduate and higher learning to several students from Kenya in British universities. A more inward-looking UK may therefore affect enrolments in British universities.

On the flipside, some EU market entry regulations, including plant health regulations are considered more restrictive compared to the revised UK's plant health regulations. Less restrictive requirements in the UK market could therefore provide an opportunity for greater access of horticultural and other products from Kenya. The UK remains a critically important donor to Kenya in supporting various development projects. Thus, if Brexit leads to a less globally engaged UK in development assistance, recipients of development assistance from UK will suffer.

During her recent visit to Kenya, the Prime Minister reassured Kenya of duty free and quota free access to her market post-Brexit. However, Kenya should pursue more favourable bilateral relations with the UK beyond tariff preferences. Greater focus on lowering trade costs and enhanced Aid for Trade (AfT) assistance should be prioritized. AfT includes aid funds spent on improving infrastructure and building productive capacities and modernizing institutions dealing with trade, such as customs, standards, health, etc to make their procedures more efficient. Supporting the development of supply-side capabilities to meet standards of UK buyers has greater importance regarding efforts to compensate for the erosion of preferences that is likely to follow Brexit.

Conclusion and Policy Recommendations

Growing protectionist policies in the US and UK directly pose development challenges to less developed and developing countries considering the strong trade and economic linkages the two major economies have with Africa and Kenya in particular. Although the global share of trade in Kenya is barely 1%, there is no doubt that international trade plays a significant role in the domestic economy. Increased protectionism in global markets is likely to further erode flexibilities that support economic structural transformation endeavours and constrain expansion of production and exports of goods and services.

Overall, a continental approach to international trade and development is the optimal platform to respond to growing marginalization of the continent. It reduces the burdens and challenges associated with multiplicity of trade arrangements. Kenya should therefore remain at the forefront in supporting efforts towards realization of continental integration.

Kenya needs to invest in value addition and diversify export production base and markets to reduce the risks associated with increasing protectionism. Besides, there is a need to increase incentives for enhancing innovations and adoption of medium and high technology to enhance industrial competitiveness and facilitate industrial expansion. Furthermore, sub-contracting strategies should be encouraged as new investments are made to support the growth and development of small and medium enterprises and enhance transfer of technology.

Kenya should also put greater focus on expanding exploiting regional markets through regional economic integration. For instance, 70% of Kenyan exports are destined for only 15 countries worldwide. In addition, there is room to increase the share of Kenya's exports in total exports to African markets, which currently stands at a meager 5%. Besides, should its ties with the US, UK or the EU become complicated, China, Brazil, India and South Africa are alternative emerging markets for Kenya's exports.

There is a need to build future Kenya and/or Africa-US relations based on a negotiated bilateral framework beyond the AGOA 2015. This would foster trade and investment confidence necessary for sustainable development. It would also allow pursuit of industrialization as envisaged in national and regional industrialization strategies.

Kenya and the EAC partner states should negotiate a transitional bilateral trade arrangement with the UK to safeguard her market preferences after UK's formal withdrawal from the European Union.

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KIPPRA Policy Briefs are aimed at a wide dissemination of the Institute's policy research findings. The findings are expected to stimulate discussion and also build capacity in the public policy making process in Kenya.

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