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The Potential Implications of the Entry of the new Republic of South Sudan into the EAC.

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Abstract

This paper assessed the potential implications of the Entry of the new Republic of South Sudan into the East African Community. The results of the analysis show that currently, South Sudan does not satisfy conditions to be admitted as a full member of EAC. It faces serious development and governance challenges and many observers assert that it will take many years to achieve a sustained economic growth in this country. In addition, to benefit from regional integration, South Sudan needs first to solve many problems including the building of good leadership, security, peace and condition for sustainable and inclusive growth and development. In addition, the admission of South Sudan would complicate the process leading up to the proposed EAC monetary union because the country is unlikely to satisfy the EAC convergence criteria.

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I. Introduction

The interest in regional integration in Africa has been high over the decades and since independence various regional groupings have been formed. Those initiatives were stimulated by the generally small size of individual economies leading to a desire to exploit economies of scale in production and distribution, as well as having more influence on the world's stage. The small domestic markets, combined with generally high production costs and deficient investment climates result in limited investment in Africa.

Regional integration goes beyond simple cooperation, harmonization or coordination; it implies higher degree of loss of sovereignty. There are different degrees of regional integration depending on the agreed objectives. They include more united markets for goods (custom unions), factors (common markets), common currency and political federation.

Regional integration increases trade among member countries and by enabling firms to operate in more and larger markets, this allows firms to realize the benefits of economies of scale and facilitate further cost reductions. It may also attract more FDI both from within and outside the region resulting especially from the increase in the market size and production rationalization that follows regional integration (Estevadeordel and Robertson, 2002; Estevadeordal and Suominen, 2003). Even if this will not lead to more FDI in each member country, benefits among members can be enhanced by agglomeration effects which refer to a spatial clustering of economic activities (Venables, 1999).

Regional trade arrangements may enable countries to coordinate their positions with more visibility and possibly stronger bargaining power. It also promotes the culture of cooperation and mechanism to address issues of common interest including common defense or mutual military assistance, hence increasing global security. In addition, the regional integration may reduce the risk of conflicts between its country members as it may raise the opportunity cost of war.

This research aims at assessing the potential implications of the Entry of the new Republic of South Sudan into the East African Community (EAC) as this country applied on November 2011 to join the EAC. This is crucial because the Republic of South Sudan currently face serious development and governance challenges which may not only limit its benefits as member of EAC but also negatively impact the viability of EAC as region. South Sudan faces many difficulties including ensuring economic stability, building institutions to support sustained growth and development, managing oil revenue wisely and building political stability and security. This is important because both theoretical literature and practice show that key principles for successful regional integration include domestic peace, political stability, minimum threshold of macroeconomic stability, good financial management, and sufficient national reforms to open market as well mutual trust among these countries.

To analyze the potential implications of the entry of South Sudan into EAC, we examine if EAC including South Sudan may be a successful regional integration by considering factors which are key for the viability of a regional integration. These factors include the number of countries composing a regional block which has impact on enforcement mechanism within the region as well as other fundamentals, including economic and political factors.

Before this analysis we first assess if the Republic of South Sudan satisfies conditions to be admitted as new member of EAC.

The rest of this paper is organized as follow: The section 2 presents the Republic of South Sudan. The section 3 presents the process of EAC integration. The analyze of the potential implication of the entry of South Sudan into EAC is presented in the section 4, before concluding the paper.

II. The Republic of South Sudan: Opportunities, challenges and strategies for the world newest countries

2.1. The profile of the country

South Sudan has been subject to the political, economic and culture hegemony and marginalization by the Sudanese state. It has been destroyed by two episodes of civil war (1955-72 and 1983-2005). More than 2 million people have died, and more than 4 million are internally displaced or become refugees in neighboring countries, as well as in various parts of the world. This situation has created socio-economic and political disparities between the two regions. The colonial concentration of economic, political and administrative development in the North at the expense of the South continues to affect the relationships between the two countries (AfDB, 2012).

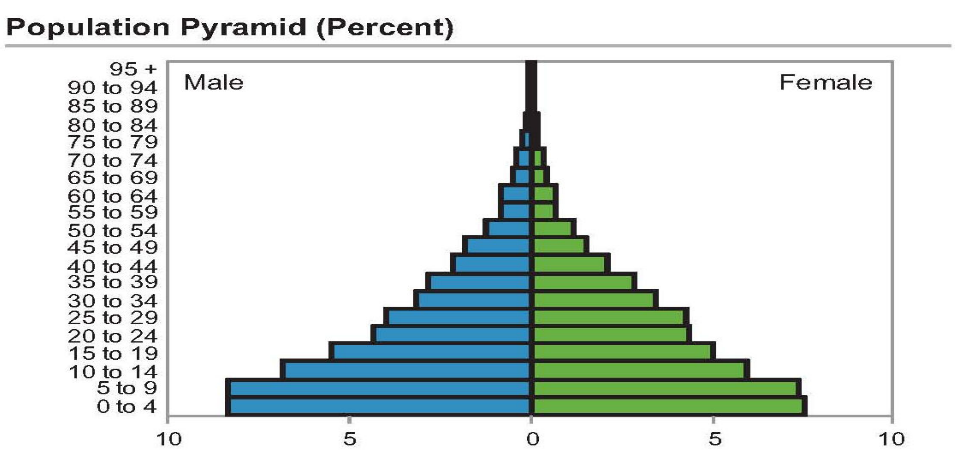
The two countries have signed the Comprehensive Peace Agreement (CPA) in 2005 and its 5 protocols which are: power sharing protocol, wealth sharing protocol, security arrangement protocol, protocol on the resolution of conflict in Southern Kordofan/Nuba Mountains and Blue Nile states, and the protocol on the resolution of Abyei conflict. In the CPA period, south Sudan has realized good achievements considering the low baseline resulting from decades of war and marginalization. Twenty nine ministries, 7 state assemblies, a national legislature and 10 state assemblies have been created. More than 2 million people displaced during the period of civil war returned home. The number of women in decision making positions has significantly increased and approach the target of 25% of government positions at all levels as stipulated in the transitional constitution of the South Sudan (UNDP, 2012).

South Sudan is the world newest country which becomes independent on July 9th 2011. It is bordered by Central African Republic, Democratic Republic of the Congo, Ethiopia, Kenya, Sudan and Uganda. The South Sudan is estimated to be the seventh-largest country in Africa with 644,329 sq. km[2] . Its population was 8,260,490 in 2008 of which 83% live in rural area.

The vast majority of South Sudan's population (78%) depends on subsistence agriculture and animal husbandry, 51% of the population lives below the poverty line and 55% of the population has access to improved sources of drinking water. According to the UN, about 90% of the population survives on less than $1 a day, nearly half of the population is expected to face problems to meet their food needs in 2012 and only 1% of the households have a bank account.

According to the 2008 census, 4.29 million out of 8,260,490 are male and 3.97 million are female. More than 51% of the population is below the age of 18, and 72% of the population is below the age of 30. The infant mortality rate is 102 per 1000 live births while the under five years mortality rate is 135/1000. Only 20% of population is estimated to ever use health facilities and maternal mortality is one of the highest in the world (AfDB, 2012).

Figure 1: Population pyramid



Source: Southern Sudan Center for Census, statistics and evaluation (2011). "Key indicators for Southern Sudan"

In the education sector, some progress has been made over the past several years. Enrolment rates in primary schools have more than doubled over the past five years,

[2] Negotiations continue between Sudan and South Sudan over borders.

according to the South Sudanese officials. However, important challenges remain in this sector especially the very low literacy rates which are top priority for the Government of South Sudan. The net enrollment rate in 2010 was 44% in primary school; 63% of the population above the age of 6 years has never attended school. At 37%, the youth literacy rate is half the sub Saharan Africa average. In addition, more than 90% of women cannot read or write. The Government of South Sudan has now prepared its first Development Plan, which covers the period from independence to the end of 2013 and has identified key development objectives across four priority areas: Governance, economic development, social and human development and conflict prevention and security. Establishing good governance by ensuring accountability and enabling citizens to engage in the governance process in the early stage of the state building process is crucial for a new country.

2.2. The economy

A. Real sector

The Republic of South Sudan has sufficient natural resources but many of them are untapped. These resources include oil reserves, hydropower, gold, diamonds, hardwoods, limestone, iron ore, copper, chromium ore, zinc, tungsten, mica, and silver. The country has also potential agriculture sector with fertile agricultural land. The main agriculture products include sorghum, maize, rice, millet, wheat, gum arabic, sugarcane, mangoes, papayas, bananas, sweet potatoes, sunflowers, cotton, sesame, cassava, beans, peanuts, cattle, and sheep. According to the Government of South Sudan, the economy is projected to growth by 7.2% in 2012 (2012 projection, Government of South Sudan).

Oil plays a major role in the economy of South Sudan as it represented 98% of total revenues, with most of it spent on defense forces and government salaries (International Monetary Fund). The Government of South Sudan recognizes the need to raise productivity in non oil export sectors in order to diversify and making growth more inclusive to reduce poverty and maintaining peace and security.

Table 1: Revenues and expenditures

		2005	2006	2007	2008	2009	2010
	Revenues						
Oil Revenue		99.9	99.9	99.5	98.2	97.2	97.8
Non oil revenue		0.1	0.1	0.5	1.8	2.8	2.2
Total Revenue		100	100	100	100	100	100
	Expenditures						
Salaries		7.8	33.1	50.4	32.8	46.7	48.6
Operating		88.9	40.2	36.0	39.0	29.6	29.3
Capital		3.2	26.7	13.6	28.2	23.7	22.1
Total Expenditures		100	100	100	100	100	100

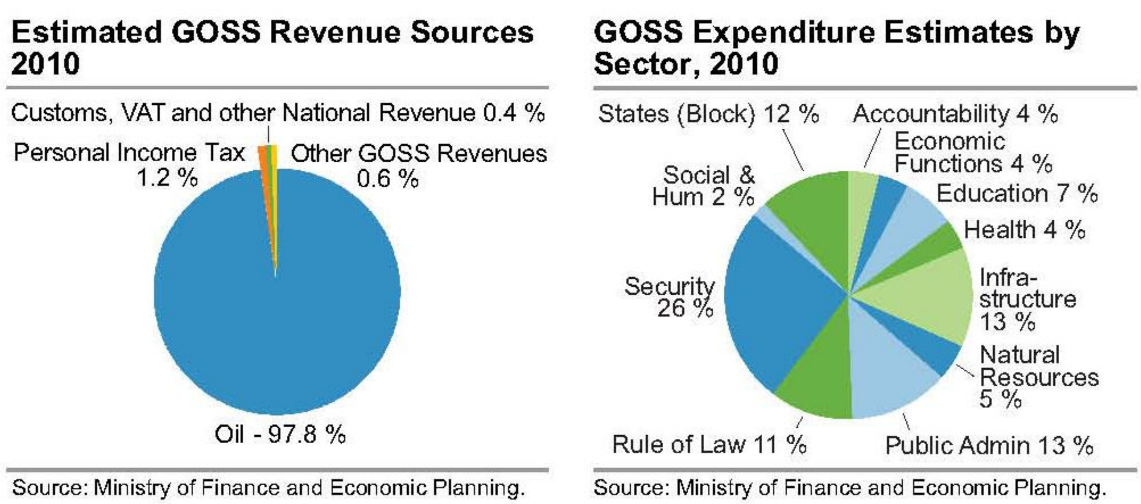
Source: Our own calculation based on data from the Government of South Sudan, Ministry of Finance.

Table 2: South Sudan forecast summary

	2011	2012
Oil production ('000b/d)	177	345
Crude oil exports (USD bn)	5 841	10 700
Government balance (% of GDP)	2	5
Export of goods fob (USD bn)	5.9	10.8
Imports of goods fob (USD bn)	1.6	4
Current account balance (USD bn)	2.8	2.9

Source: The Government of South Sudan, Ministry of finances 2011

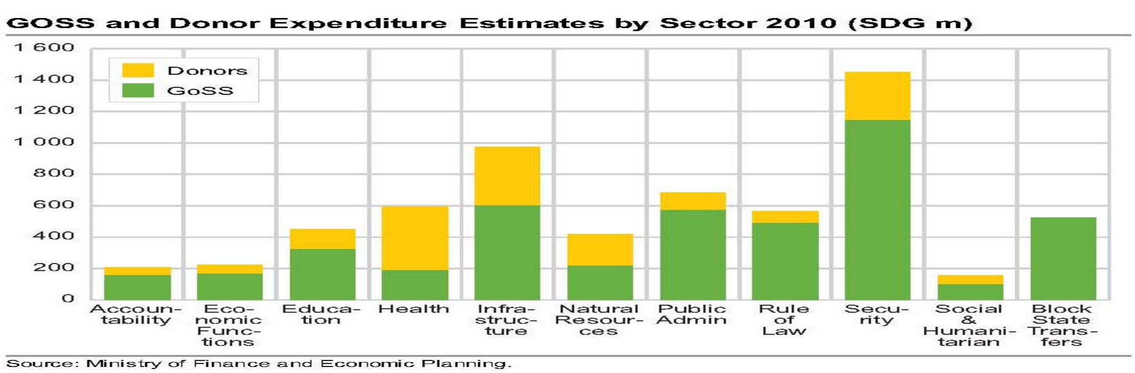
Figure2: Estimated Government of South Sudan (GOSS) revenue sources and expenditures by sector



As indicated in the figure 3 below, the Government of South Sudan is receiving substantial foreign aid to support its reconstruction program. Funds from donors are more used in health sector, infrastructure, natural resources, education and security. USAID is supporting the Government to put in place policies and systems to improve agricultural productivity and investment. It is also rehabilitating hundreds of kilometers of roads and building bridges across the country, including the major transport road for trade linking Juba to Nimule, the Ugandan border crossing. The USAID is also expected to fund the improvement of feeder roads linked to agriculture development objectives and other strategic small scale infrastructure projects.

The UNDP is planning to support the Government of South Sudan to create an enabling environment for inclusive growth through policy development. It will also support to enhance the financial literacy in rural areas, link communities to microfinance services and market channels, strengthen institutional capacity for trade policy formulation and the development of policy framework for environment governance and develop financial incentives for green energy development (UNDP, 2012).

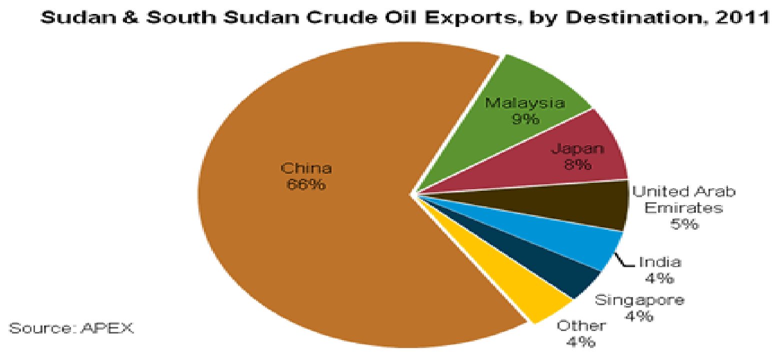
Figure3: Estimated government of South Sudan revenue sources and expenditures by sector



B. External sector

Exports from South Sudan are essentially limited to oil and are destined to Asian. According to international trade data, Sudan and South Sudan exports averaged 330,000 bbl/d in 2011 and went almost exclusively to Asian markets. China imported around 220,000 bbl/d followed by Malaysia (30,000 bbl/d) and Japan (25,000 bbl/d). The two countries also exported some processed fuels to neighboring countries like Ethiopia. South Sudan depends heavily on imports of goods, services and capital from Sudan, but disruptions in trade have occurred since its independence due to blockades being imposed on goods and capital going to South Sudan as well as on oil exports from South Sudan.

Figure 4: Sudan and south Sudan crude oil exports, in 2011



The concentration of export sector in terms of production and destination makes the country vulnerable to external shocks including restrictions imposed by Sudan and the volatility of oil prices in the international market. High dependence on revenues from oil may lead to excessive government spending in a boom, which becomes semi-permanent and leads to excessive borrowing when the oil price and revenues fall. Finally, the impact of oil on the balance of payments of a country like South Sudan can appreciate the real exchange rate, crowding out other production and export activities, principally in agriculture and manufacturing. This is the so-called "Dutch disease."

South Sudan has important trade with EAC countries like Kenya and Uganda. Available data show that Uganda formal exports value to South Sudan have significantly increased by 56.9% between 2010 and 2011, from USD 256.6 million to USD 402.5 million. In the first quarter 2012, the value of exports from Uganda to South Sudan stood at USD 112.2 million, compared to USD 73.3 million in the first quarter 2011 and USD 54.0 million in the first quarter 2010--an increase of 53.1% and 107.8% respectively. Including informal cross border trade, the total exports value of Uganda to South Sudan is estimated at USD 507.5 million in 2011 compared to USD

530.7 million in 2010. Uganda's trade balance with South Sudan has been positive since 2010, showing how the country is a potential market for Ugandan exports.

Table 3: Trade between South Sudan and Uganda (in USD million)

	Formal		Informal				
	Export	Import	Export	Import	Tot. Export	Tot. Import	Trade balance
2010Q1	54.029	0.170625	77.25625	1.641525	131.2852	1.81215	129.4731
Tot2010	256.5788	3.196975	274.1514	4.806756	530.7302	8.003731	522.7264
2011Q1	73.32329	0.857114	21.30515	0.279872	94.62844	1.136986	93.49145
Tot2011	402.5283	5.162229	105.0207	1.653011	507.549	6.81524	500.7338
2012Q1	112.166	0.7203	21.74131	0.372503	133.9073	1.092803	132.8145

Source: Bank of Uganda, 2012.

C. Challenges and strategies for the South Sudan

As new country, South Sudan faces serious development challenges and many observers assert that it will take years to achieve a sustained economic growth in this country (Congressional research service, 2011). These difficult are linked with building a viable politically and economically state, building its legitimacy and accountability in terms of good governance, peace, security, justice, service delivery, mobilization of revenues, economic development and generation of employment (AfDB, 2012).

The political economy of South Sudan will continue to be affected by its relation with Sudan because the CPA provisions have left many issues unresolved such as border demarcation. The agreement had been reached on delimitation of 80% borders, differences remained with regard to five disputed areas along the boundary including south Kordofan and the Blue Nile, together with Abyei, they incorporate grazing lands used by pastoralists on both sides of the North/South and are rich in agricultural land, mining and oil.

The Economy of South Sudan is fragile due to its dependency on oil. This results in volatile revenues caused by world oil price volatility and unstable government expenditure patterns. This situation of volatile public spending is damaging for the social economy of the country as it increases the risk of not respecting spending commitments such as teacher's salaries or payment of other contracts.

In addition, the experience of other countries in Africa suggests that "large oil revenues can have major disruptive effects on the country concerned and its neighbours. While resource revenues can in principle increase sources of funds available for investment to promote development, Nigeria and Angola, among other countries, illustrate the "curse of oil" under which resource revenues are poorly used and the general population does not gain from them. Nigeria, for instance, has roughly the same dollar per capital income as it did in 1965, despite earning hundreds of billions of dollars of oil revenue over that period (Masson, 2012).

The experience shows that unless a country benefits initially from good governance, oil revenues tends to exacerbate corruption and encourage rent seeking at the expense of productive activities. It can also lead to conflict between the central government and the states or provinces that produce the oil.

The new political leaders in South Sudan are aware of the unsustainable oil dependent economy. Though progress in improving non oil revenues has been slow, the Government of South Sudan has embarked on fiscal reforms to boost revenues from various tax sources and customs. In 2009, a taxation act was enacted defining the tax system of South Sudan and establishing the general principles for assessment, collection of taxes and other charges as well as the rights and obligations of tax payers.

An agriculture policy is under development in South Sudan and aims to guarantee food security for its population. This policy will focus on rain fed agriculture but will also include plans for irrigating farmland with Nile water. The development of agriculture sector is key in South Sudan not only for food security but also in reduction of poverty, diversification of exports and industrialization of the country. This will require a clear agriculture policy focusing on the productivity of the sector, including land policy, supply of seeds, fertilizers and agricultural tools to farmers. In 2011, AfDB has supported the Government of South Sudan to realize the agriculture sector assessment study which has identified constraints and opportunities with the ultime objective of enforcing AfDB's prospective interventions and areas of support to the Government of South Sudan.

The country has also to deal with the unsustainable allocation of public resources. According to the Government of South Sudan (2010), 53% of the government spending was on salaries, 29% on operating costs and only 18% on capital. Over the period 2008-2010, social and human development sector had the lowest budget allocation (10% of the government expenditures). This allocation of public resources is not sustainable for a country which lack infrastructure (roads, electricity, water and sanitation system, hospital, schools, etc…).

The lack of infrastructure is the great burden for the economy of the new state. With the support of World Bank, there is improvement in electricity and water supply and expending dirt road networks in many parts of South Sudan and the World Bank is intended to concentrate future concessional funding in this sector.

The country also lacks human resources for its social economic development. According to UNDP, half of all positions in ministries remain unfilled, 50% of public service staff have only early education and only 5% have a graduate degree or higher. In addition, many of current staff lack necessary work experience and have major difficulties in English communication, the official language of the government. The country also needs to train human resources at all levels of the health sector. Only 23% of the health facilities are functional, but lack infrastructure in terms of blood banks, medical support stores, laboratories, pharmaceutical equipments and medical staff.

Recognizing the critical importance of promoting economic growth for delivering the peace dividend, the Government of South Sudan Growth strategy has been developed in 2009. It broadly defines the role that government should play in the economy, identifies the highest priority constraints on which public sector actions should focus (insecurity, poor infrastructure, and multiple taxation) and defines the private sector as the key driver of economic growth. The government will not undertake economic activity directly; it will promote economic growth by creating enabling environment and addressing the key constraints or barriers to private investment.

III. East Africa Community

3.1. Process of integration

On 30 November 1999, Kenya, Tanzania and Uganda signed the Treaty for the establishment of the East African Community (EAC), which entered into force in July 2000. In 2007 the Treaty was signed by Burundi and Rwanda, expanding the EAC to five countries. According to the Treaty, the EAC should first form a customs union, then a common market and a monetary union, and finally a political federation. The customs union became operational in 2005, and was formally completed in 2010. The Common Market Protocol, which includes free movement of goods, labour, persons, services and capital, and the right of residence and establishment, was signed in 2009 and its full implementation is to be completed by 2015.

EAC organs are in place and they include the East African Legislative Assembly, the East African Court of justice, a Secretariat, the Council of Ministers and the Summit of Heads of States. These achievements are a good indication of political will to have a strong regional integration.

At their Summit in 2007, the heads of States of the EAC Partner States decided to fast tract the achievement of Monetary Union by 2012. Some progress in the preparation for monetary union has been made. A study on the preparedness for a monetary union has been conducted by experts from the European Central Bank in collaboration with experts from the EAC central banks.

Good progresses have been made by the EAC central banks' 'Governors Monetary Affairs Committee (MAC). They include the harmonization of banking regulation, the payment system integration, the harmonization of monetary and exchange rate policy implementation. On the fiscal side, Finance ministers conduct pre and post budget consultations, share regularly budget information and budget statements are read the same day.

The negotiations of an East Africa Monetary Union (EAMU) protocol started in January 2011 and so far, the HLTF have held seven negotiation meetings and a number of articles have been negotiated.

3.2. Current status of EAC integration

3.2.1. Macro-economic convergence in EAC

The evaluation of prospective regional integration has been done on the basis of macroeconomic convergence rooted in the Optimum Currency Area (OCA) theory and refers to the convergence of a set of macroeconomic fundamentals among countries.

The macro economic convergence criteria that were adopted by EAC partner states in 2007 include the convergence of inflation to a low value and the reduction of public deficits and debt ratios below some critical values. They are set for three different stages and divided into primary and secondary criteria in the first two stages (customs union and common market), followed by introduction of a single currency at the last stage (see table 1 in appendix). Performance in achieving agreed macroeconomic convergence criteria in EAC has been mixed so far, with the fiscal deficits excluding grants and inflation persistently exceeding the targets.

The initial threshold of allowable deficits of three percent of GDP including grants is relatively close to the countries' actual deficit levels. Uganda, Rwanda and Burundi have been achieving this criterion since 2004. No country, except Kenya in 2007 and 2008 has ever met the criterion of budget deficits excluding grants (six percent). In addition, the future criterion for deficits including grants (two percent) is lower than the levels countries have been recently achieving (see tables 2 and 3 in appendix).

Table 4: EAC convergence criteria

	Primary criteria		Performance of member countries in 2010				
	Stage 1	Stage 2	Burundi	Kenya	Rwanda	Tanzania	Uganda
Overall fiscal deficit (exc. Grants) as percentage of GDP	$\prec 6\%$	$\prec 5\%$	31.8	7.2	14	11.6	7.5
Overall fiscal deficit (including grants) as % of GDP	$\prec 3\%$	$\prec 2\%$	3.0	6.2	0.4	6.9	5.0
Inflation, period average	$\prec 5\%$	$\prec 5\%$	6.4	3.9	2.3	10.5	9.4
Foreign exchange reserves in months of imports	$\succ 4$	$\succ 6$	5.2	2.9	4.4	4.8	5.6

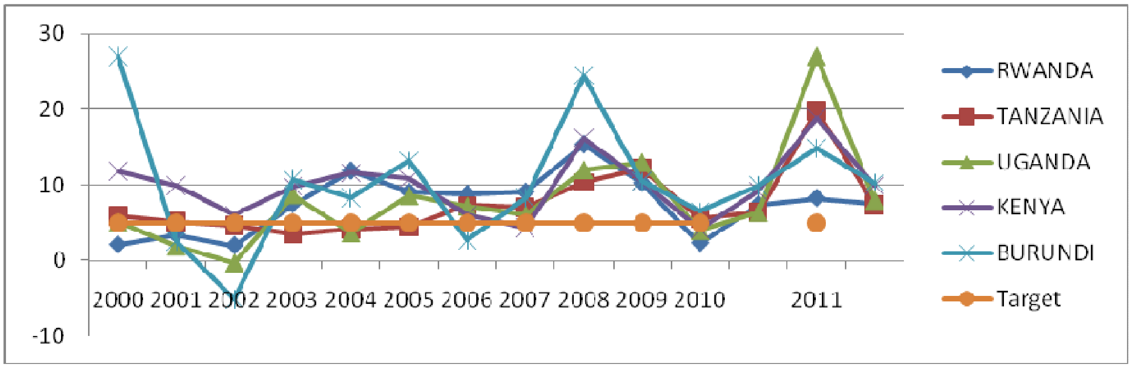
Source: IMF, 2012.

3.2.2. Policy harmonization

One way of assessing the policy harmonization in economic block is to analyze the similarities in inflation developments and convergence in real exchange rates.

About inflation, the current target of 5% as ceiling is far below inflation rates in EAC countries even if we exclude periods when countries have faced severe shocks. Over the period 2000-2011, the average headline inflation was high in Burundi (10.3%), followed by Kenya (10%), Uganda (8.1%), Tanzania (7.5%) and Rwanda (7.5%). Excluding the year 2011 when all EAC region has faced shocks from food prices and international oil prices, the average headline inflation was 9.09% in Burundi, followed by Kenya (9.2%), Rwanda (7.4%), Uganda (6.4%) and Tanzania (6.4%).

Figure 5: Inflation development in EAC



Source: Our own calculation based on data from EAC central banks

In addition, there are significant differences not only in inflation rates but also in their volatility indicating both differences in the way countries conduct their economic policies and that they face different shocks. As indicated the table below, over the period 2000- 2011, inflation has been more volatile in Burundi which a standard deviation of 8.8 in average, followed by Uganda (4.2), Kenya (3.7), Rwanda (2.7) and Tanzania (2.1).

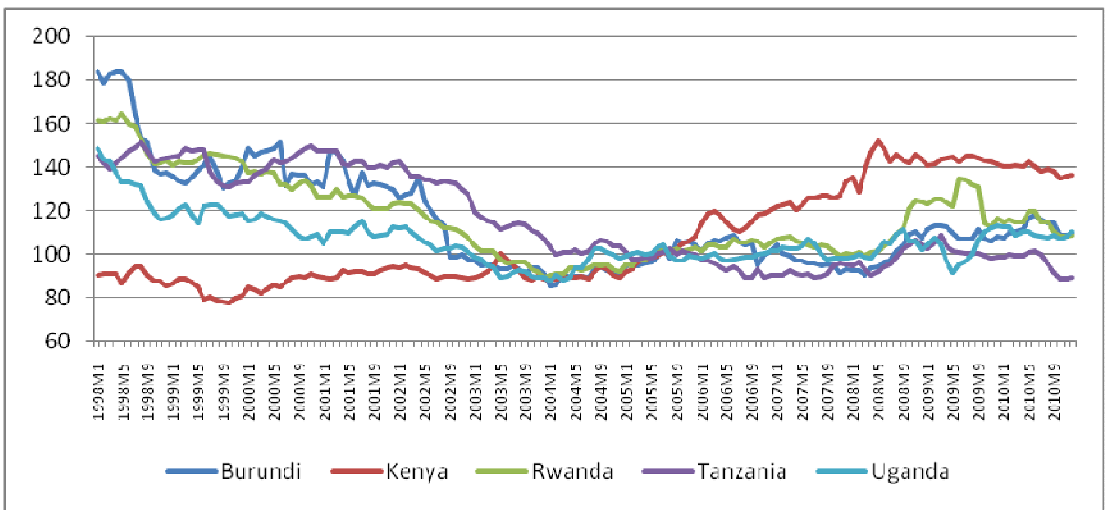
Table 5: Volatility of inflation in EAC (measured by standard deviation)

Year	Rwanda	Tanzania	Uganda	Kenya	BURUNDI
2001	0.9	0.6	2.3	1.3	2.6
2002	1.0	0.4	1.6	2.8	-5.1
2003	3.9	0.8	6.4	2.7	10.7
2004	3.1	0.5	3.5	1.3	8.3
2005	2.0	0.1	3.5	0.6	13.2
2006	0.2	2.1	1.0	3.4	2.7
2007	0.2	0.2	0.8	1.2	8.3
2008	4.5	2.3	4.2	8.4	24.5
2009	3.6	1.3	0.7	4.0	10.5
2010	5.6	4.7	6.4	4.5	6.5
2011	4.2	10.1	16.3	10.5	14.9
Average	**2.7**	**2.1**	**4.2**	**3.7**	**8.8**

Source: Our own calculation based on data from EAC central banks

The convergence of real effective exchange rates is based on the assumption that the real exchange rates are influenced by economic fundamentals in such way that these fundamentals must move together in countries members of a currency union. One way of assessing this convergence is to test whether real effective exchange rates were co-integrated. The figure below shows how effective exchange rates are different in EAC countries.

Figure 6: Real effective exchange rates 1998:1-2010:12



Source: Data from UNECA.

Performing the formal Johansen test of cointegration, we find that the real effective exchange rates in EAC are not cointegrated showing how economic fundamentals in these countries are not moving together overtime.

Table 7: Co integration between real exchange rates

Unrestricted Cointegration Rank Test (Trace)

Hypothesized No. of CE(s)	Eigenvalue	Trace Statistic	0.05 Critical Value	Prob.**
None	0.150807	49.94672	60.06141	0.2653
At most 1	0.091003	28.69583	40.17493	0.4255
At most 2	0.065284	16.29205	24.27596	0.3588
At most 3	0.045166	7.515416	12.32090	0.2767
At most 4	0.011526	1.507110	4.129906	0.2575

Trace test indicates no cointegration at the 0.05 level

* denotes rejection of the hypothesis at the 0.05 level

**MacKinnon-Haug-Michelis (1999) p-values

3.2.3. EAC economic structure

We analyze the structures of the economies in the five EAC member countries with the objective of identifying similarities and differences between them. GDP per capita is similar in EAC countries; except for Burundi whose GDP per capita in 2010 was only 189 USD. It varies between 503 USD in Uganda and 767 USD in Kenya. The structure of GDP in terms of contributions of different sectors of the economy is quite similar. Based on 2010 data, respective shares of the agriculture sector in GDP are 22.6%; 28.8% and 24.7% in Kenya, Uganda and Tanzania respectively. Agriculture's share in Rwanda, 32%, is relatively large3.

Table 8: Indicators of economic structures

Indicators	Burundi	Kenya	Rwanda	Tanzania	Uganda
GDP per capita (Current USD) in 2010	189	767	548	527	503
GDP per capita, PPP (Current international $) in 2010	399	1621	1194	1423	1249
Industry, value added (% of GDP) in 2009		15.3	14.5	24.3	25.8
Manufacturing, value added (% of GDP) in 2009		8.7	6.4	9.5	8
Agriculture, value added (% of GDP) in 2009		22.6	34.2	28.8	24.7
Services, value added (% of GDP) in 2009		62.1	51.3	46.9	49.5
Trade (% of GDP) in 2010		63.5	40.9	58.4	58

Source: World Development indicators

In addition, there is not significant structural change in composition of GDP in the five countries between 1995 to 2009 as indicated by the Herfindahl Index (Kigabo and Masson, 2012).

Table 9: HI Indicator: GDP concentration

	Burundi	Kenya	Rwanda	Uganda	Tanzania
1995	0.42	0.38	0.40	0.37	0.37
1996	0.46	0.38	0.39	0.37	0.37
1997	0.46	0.39	0.39	0.37	0.38
1998	0.41	0.39	0.39	0.37	0.37
1999	0.39	0.39	0.38	0.37	0.37

[3] Data on Burundi are not available in 2010.

2000	0.38	0.39	0.38	0.37	0.38
2001	0.39	0.40	0.39	0.38	0.38
2002	0.38	0.40	0.39	0.39	0.37
2003	0.38	0.40	0.39	0.38	0.36
2004	0.39	0.40	0.39	0.38	0.36
2005	0.38	0.40	0.38	0.38	0.36
2006	0.39	0.41	0.39	0.39	0.37
2007	0.40	0.42	0.39	0.39	0.37
2008	0.39	0.41	0.39	0.38	0.36
2009	0.39	0.40	0.39	0.39	0.37

Source: Kigabo and Masson, 2012

3.2.4. Degree of openness and intra-regional trade

Measured by trade as percentage of GDP, the level of economic openness is different between the five countries but has been increasing in all countries except Burundi where the situation deteriorated between 2006 and 2010. Kenya is the most open economy in the region (60.6%) followed by Tanzania (49.5%), Uganda (41.3%), Rwanda (35.4%) and Burundi (28.8%). So far the customs union does not appear to have much increased total intra-regional trade, which represented only 17.5% of total exports and 7% of imports in 2007. According to the EAC Trade Report 2008, gross intra-EAC trade was 7.8% of the members total gross trade, and 3.1% of their GDP (EAC, 2010).

able 10 : Intra EAC exports as share of total exports, 2009

Country	Burundi (%)	Kenya (%)	Rwanda (%)	Tanzania (%)	Uganda (%)
Burundi		0.08	0.19	0.00	0.09
Kenya	1.53		9.29	25.2	25.87
Rwanda	0.35	7.06		0.06	0.39
Tanzania	0.85	2.57	2.71		2.81
Uganda	2.53	9.13	7.62	1.69	
EAC	**5**	**19**	**20**	**27**	**29**

Source: IMF, 2010

3.2.5. Free movement of capital

There is a plan of integrating capital market in EAC by removing all controls on capital transactions among the member countries and harmonization of capital market infrastructure including regulations, taxation, accounting, trading systems, and cross listings of securities (capital market protocol, article 85). However, there still much to do to achieve this objective. There is a need of developing domestic capital markets, further harmonizing market infrastructure and completely removing all constraints on movement of capital. Uganda, Rwanda and Kenya have fully liberalized capital transactions within the region, even if restrictions on investments in Kenya domestic market by non-residents of the EAC remain. Tanzania and Burundi have committed to fully liberalize their capital accounts by 2015.

3.2.6. Political factors

Political factors are fundamental in the formation and the sustainability of a currency area. Strong political will by the leaders is crucial because belonging to a sustainable currency union involves strong political commitment to coordinating policies and accepting the loss of a part of national sovereignty. In addition, political will is important to ensuring the public support for the process toward a monetary union. Public support, in turn, is one of key factors which contribute to the sustainability of monetary union beyond political cycles or terms. To create this support from the public, the integration process has to focus mainly on economic growth and jobs creation as well as regional infrastructures which impact directly the daily life of the population. Some empirical studies show that political factors may dominate economic criteria in successful currency area. Put simply, the full implementation of the customs union and common market protocols, the creation of surveillance and enforcement mechanisms, as well as the creation of a strong institutional framework to make monetary union feasible, successful and sustainable will highly depend on the level of political will to support the overall regional integration process.

IV. Potential implications of the entry of South Sudan into EAC

Before analyzing the implications of the entry of South Sudan into EAC, we assess if the Republic of South Sudan satisfies conditions to be admitted as new country member of EAC. To analyze the potential implications of the entry of South Sudan into EAC, we examine if EAC including South Sudan may be a successful regional integration by considering factors which are key for the viability of a regional integration. These factors include the number of countries composing a regional block which has implication on enforcement and coordination mechanism as well as other fundamentals such as political and economic factors.

South Sudan applied on November 11, 2011 to join the EAC. The Summit directed the Council of Ministers to verify the application on the basis of the criteria for admission of a new member and submit recommendations to the summit at its 10th extraordinary meeting. By joining the EAC, the Republic of South Sudan expect to reduce its dependency on Sudan, especially for its external trade by finding alternative transport corridors. Currently, South Sudan has plans to build domestic refineries to export petroleum products to regional markets such as Kenya, Uganda and Ethiopia. The projects include construction of an oil refinery and sea port in Lamu (Kenya), a 1 400 km oil pipeline that will link Juba to Lamu port and construction of a new Mombasa-Kampala standard railway line. Important investment is also being made in a 1 130 km road to link Nairobi to Juba. These projects are expected to serve Uganda, Rwanda, Burundi, Eastern Congo, Southern Sudan and Ethiopia and likely to attract more FDI, especially from Asia's economic giants (Japan and China). Kenya and Uganda are particularly expected to benefit from the thousands of jobs that the large infrastructure projects are expected to create.

Becoming a member of EAC, South Sudan may benefit from all arrangements under the EAC customs union and common market agreements as a new country that needs to build the foundation for its social and economic development. Being member of EAC may also provide the new country opportunities to increase market size, reduce transaction costs and increase economic efficiency by implementing common policies with other EAC members. In addition, this may provide opportunities for mobilizing the human and financial resources necessary to undertake investments supporting trade expansion and economic development. It would also provide an overall supportive policy framework that helps to increase policy transparency, stability and enhance policy credibility and build institutions that match the EAC standards contrary to original members which have to adjust existing institutions to the regional requirements.

However, for these expectations to be realized, South Sudan needs first to solve many problems including the building of good leadership, security, peace and condition for sustainable and inclusive growth and development. Good leadership is key for economic growth and development, since sustainable growth requires committed, credible and capable government (Commission on Growth and Development, 2008). Indeed, sustainable growth and economic development does not just happen, it must be consciously chosen as an objective by the country's leadership and as an organizing principle of the country's politics (Kigabo, 2010). Sound governance reduces the potential for corruption and lessens the risk that scarce public resources become diverted from their intended purpose.

The Government of south Sudan will need first to establish good governance practices and improve the human capacity for credibility and effectiveness of overall development efforts in the medium to longer term. The country needs to establish and strengthen the basic principles of accountability, transparency, integrity, inclusion and professionalism as applied to the operation of government systems and administration.

Another challenge for South Sudan to join the EAC is its ability to face the completion in a common market with free movements of capital, labor, persons, services and right of establishment given that its economic development and institutions are at their infancy.

Based on these challenges, it is clear that for the moment, South Sudan is not a relevant candidate to join EAC. Indeed, according to the EAC Treaty and rules of procedure for admission of a new country as full member, certain criteria have to be met. They include: acceptance of the community as set out in the treaty, adherence to the universally acceptable principles of good governance, democracy, the rule of law, observance of human rights and social justice, potential contribution to the strengthening of integration with the East African region, geographical proximity to and interdependence between it and EAC partner states, establishment and maintenance of a market driven economy, and compatibility of social and economic policies with those of the community (EAC Treaty).

As mentioned, the analysis of the potential implications of the entry of South Sudan into EAC is done by considering factors such as the number of countries composing a regional block as well as other fundamentals, which are key for a viable regional integration.

The traditional K-group theory argues that more participants lower the benefits of cooperation as it increase the enforcement problem (Olson, 1965). The enforcement mechanism is very important because to build a viable regional integration countries have to agree on surveillance and enforcement mechanisms for convergence criteria. The experience shows that, whereas there are some examples of regional organizations that started small and have been successful, there are no cases of large regional organizations that have achieved the same level of regional integration (EDB, 2010) showing that starting out with few states is a better strategy for regional integration.

In the case of South Sudan and EAC, the main issue here may not be a big number of countries forming the EAC, but the disparities between South Sudan and the rest of EAC members because several domestic characteristics of state influence the success of regional integration. The differences in economic and socio development fundamentals between South Sudan and the rest of EAC country members can do more to hamper the cooperation in EAC than the number of members itself. In addition, the lack of sufficient capacity (political, human resources,…) to implement the obligations of membership in EAC may negatively affect the EAC regional integration efforts.

The admission of South Sudan would also complicate the process leading up to the proposed EAC monetary union. The country is unlikely to satisfy the convergence criteria that are intended as pre-requisites to joining monetary union. Hence, if South Sudan joins the EAC, and the existing members want to continue to fast-track monetary union, then necessarily there will be a two-speed process, with a first group proceeding to monetary union and South Sudan and perhaps others joining the monetary union later, if at all.

As indicated, the domestic socio economic conditions of South Sudan are far from those of other EAC countries and this limits the success in regional integration (Russet, 1967), especially the monetary union because these countries cannot form an optimum currency area. This will limit the effectiveness of the EAC central bank monetary policy.

Another issue concerns South Sudan's reliance on oil revenues for financing government and as a source of export receipts. The volatility of world oil prices means that this induces considerable fluctuations on the domestic economy. In a common currency area, these fluctuations spill over to the partner countries. If the country is large enough to influence the monetary policy and exchange rate of the currency area, then it may cause "Dutch disease" problems for its neighbours (see Masson, 2012)—that is, appreciation of the real exchange rate that crowds out other sectors, in particular manufacturing and agriculture. With Kenya, Tanzania, and Uganda also with prospects for exploiting oil and gas discoveries, South Sudan may however not be the outlier.

V. Conclusion

This paper assessed the potential implications of the Entry of the new Republic of South Sudan into the East African Community.

According to the EAC Treaty and rules of procedure for admission of a new country as full member, certain criteria have to be met. They include: acceptance of the community as set out in the treaty, adherence to the universally acceptable principles of good governance, democracy, the rule of law, observance of human rights and social justice, potential contribution to the strengthening of integration with the East African region, geographical proximity to and interdependence between it and EAC partner states, establishment and maintenance of a market driven economy, and compatibility of social and economic policies with those of the community (EAC Treaty). Currently, South Sudan does not satisfy these conditions and can't be considered as relevant candidate to join the EAC today. The country faces serious development and governance challenges and many observers assert that it will take many years to achieve a sustained economic growth in this country. The country needs to adopt and implement principles of governance, establish and maintain a market driven economy as well as efficient social and economic policies before expecting to gain from its EAC membership.

Becoming a member of EAC, South Sudan may benefit from all arrangements under the EAC customs union and common market, mobilize the human and financial resources necessary to undertake investments supporting trade expansion and economic development and limit its dependency to Sudan for the external trade.

However, to benefit from regional integration, South Sudan needs first to solve many problems including the building of good leadership, security, peace and condition for sustainable and inclusive growth and development.

EAC countries may benefit from the important economic resources, especially the oil from South Sudan and also from new market of exports of goods and services. However, the admission of South Sudan would complicate the process leading up to the proposed EAC monetary union because the country is unlikely to satisfy the EAC convergence criteria.

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APPENDIX

Table 1: New EAC Macroeconomic Convergence Criteria

Stage 1 (Year 2007-2010):

Primary Criteria

a) Overall Budget Deficit to GDP Ratio (excluding grants) of not more than 6.0 percent, and Overall Budget Deficit to GDP Ratio (including grants) of not more than 3.0 percent;

b) Annual Average Inflation Rate not exceeding 5 percent;

c) External Reserves of more than 4 months of imports of goods and non-factor services.

Secondary Criteria

a) Achievement and maintenance of Stable Real Exchange Rates;

b) Achievement and maintenance of Market Based Interest Rates;

c) Achievement of sustainable Real GDP Growth Rate of not less than 7.0 percent;

d) Sustained pursuit of debt reduction initiative on domestic and foreign debt i.e. reduction of total debt as a ration of GDP to s sustainable level;

e) National Savings to GDP Ratio of not less than 20 percent;

f) Reduction of Current Account Deficit (Excluding grants) as a percentage of GDP to sustainable level consistent with debt sustainability;

g) Implementation of the 25 Core Principles of Bank Supervision and Regulation based on agreed Action Plan for Harmonization of Bank Supervision; and

h) Adherence to the Core Principles for Systematically Important Payment Systems by modernizing payment and settlement systems.

Stage II (2011-2014)

Primary Criteria

a) Overall Budget Deficit to GDP Ratio (excluding grants) not exceeding 5 percent; and Overall Budget deficit to GDP Ratio (including grants) not exceeding 2 percent;

b) Annual Average Inflation Rate of not more than 5 percent;

c) External Reserves of more than 6 months of imports of goods and non-factor services.

Secondary Criteria

a) Maintenance of Market Based Interest Rates;

b) Maintenance of high and sustainable rate of real GDP growth of not less than 7.0 percent;

c) Sustained pursuit of debt sustainability;

d) Domestic Savings to GDP Ratio of at least 20 percent;

e) Maintenance of sustainable level of Current Account Deficit (excluding grants) as percentage of GDP; and

d) Achievement of Sustainable Growth Rate of Real GDP of not less than 7.0 percent.

Stage III (2015)

Source: MAC report (2008): Review of MAC achievements and challenges since its inception report (1998 – 2008)

Table 2: Budget deficit, including grants as percentage of GDP

Country	2003	2004	2005	2006	2007	2008
Burundi	6.4	5.6	2.2	3.1	2.9	3.1
Tanzania	0.0	4.5	5.9	2.4	4.2	3.1
Uganda	1.6	0.5	2.2	1.9	2.3	3.4
Kenya	7.3	8.2	5.3	6.3	5.0	3.3
Rwanda	2.2	0.2	-0.3	0.2	1.0	-0.4

Table 3: Budget deficit, excluding grants as percentage of GDP

Country	2003	2004	2005	2006	2007	2008
Burundi	16.6	20.0	14.2	14.5	18.9	13.6
Tanzania	6.5	10.2	11.1	8.3	9.9	8.2
Uganda	9.8	7.8	7.1	7.1	7.5	7.7
Kenya	8.6	9.5	6.3	7.5	5.8	4.6
Rwanda	9.8	11.2	11.0	10.5	13.1	10.5

Source: ECB study on EAMU, June 2000

Table 4: Comparison with other regional blocs

Pillars regional blocs (REC)1	Area (km²)	Population	GDP (PPP) ($US)		Member states
			in millions	per capita	
AEC	29,910,442	853,520,010	2,053,706	2,406	54
ECOWAS	5,112,903	300,000,000	703,279	1,748	15
ECCAS	6,667,421	121,245,958	175,928	1,451	11
SADC	9,882,959	233,944,179	737,335	3,152	15
EAC	1,817,945	124,858,568	104,239	1,065	5
COMESA	12,873,957	406,102,471	735,599	1,811	20
IGAD	5,233,604	187,969,775	225,049	1,197	7