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Determinants of Uganda's Export Performance: A Gravity Model Analysis

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Abstract: *Exports play an important role in Uganda's economy, influencing the level of economic growth, employment and the Balance of Payments. Uganda has initiated several trade policy reforms aimed at promoting the export sector. However, Uganda's share in total world exports is still very low. Given the central role of exports in the economy, it was important to identify the plausible factors affecting export flows between Uganda and its trading partners. Thus, this paper examines the factors affecting Uganda's exports using an augmented gravity model of trade. The panel dataset used was for the period 1980 to 2012. The results suggest that Uganda's GDP, importer's GDP, importer's GDP per capita, per capita GDP difference between Uganda and its trading partners, real exchange rate, official common language, and contiguity had a positive and statistically significant effect on Uganda's exports. The study further, shows that the formation of COMESA and EAC had a significant positive effect on Uganda's exports. On the other hand, Uganda's GDP per capita and distance between Uganda and its trading partners had a negative effect on Uganda's export flows. These results are important for trade policy formulation in order to ensure that Uganda's export potential is exploited so as to enhance economic growth.*

Introduction

The failure of the in-ward looking policies to stimulate the desired growth in Sub-Saharan Africa in the 1960s and 1970s, led most African countries to rethink on the most appropriate development policy to adopt. Since the 1980s, the development strategy of Sub-Saharan African countries changed in favour of export orientation and trade liberalization in order to overcome the inherent limitations and adverse effects of the import substitution industrialization strategy (Dedrick *et al*, 2001). Thus, the focus was shifted from producing for the domestic market to producing for the export market.

Exports play an important role in an economy, influencing the level of economic growth, employment and the balance of payments. Exports open up domestic industries to foreign markets. The increase in potential market size can lead to increasing returns, economies of scale, and increased capacity utilization. Exposure to world markets may also induce competitive pressures and may spur innovation and facilitate technological advancement and knowledge spillovers into the domestic economy, leading to efficiency gains in production and management practices. Exports also generate the much-needed foreign exchange, which can be used to import superior capital goods and intermediate inputs that are critical to the domestic production of a country. Thus, an expansion of exports will have positive spillover effects on the rest of the economy. The wave of growth of East Asian economies during the 1970s and 1980s provides a good example of the importance of the export sector to economic growth and development, which led economists to stress the vital role of exports as the engine of economic growth.

Uganda is one of the countries in Sub-Saharan Africa that adopted the export-oriented growth strategy in 1980s. Since then, Uganda has initiated several trade policy reforms aimed at promoting the export sector. Such reforms include the liberalization of foreign exchange rate regime, elimination of export taxes and abolition of taxes on import inputs meant for the export sector (Musinguzi, 2002). Statutory bodies were also set up to facilitate, coordinate and promote the export sector and attract export-oriented investments. These include Uganda Investment Authority, Uganda Exports Promotions Board, and Uganda National Bureau of Standards. Uganda has also actively been involved in regional integration initiatives with the aim of promoting her exports in the regional market. It is a member of the East African Community (EAC), the Common Market for Eastern and Southern Africa (COMESA), and Intergovernmental Authority on Development (IGAD).

As a result of the above policy measures, Uganda has registered some improvements in export performance. Trade statistics show that export earnings have increased during the post reform period from 0.20 billion US dollars in 1980 to 5.1 billion US dollars in 2012. The major export commodities were coffee, fish and fish products, tea, cotton, flowers, horticultural products, and gold. According to the 2012 trade statistics, goods were primarily exported to Sudan (14.3%), Kenya (9.5%), Switzerland (9%), Rwanda (7.9%), United Arab Emirates (7.4%), Democratic Republic of the Congo (7.3%), United Kingdom (6.9%), Netherlands (4.7%), and Germany (4.4%).

However, Uganda's share in total world exports is still very low, amounting to 0.02% in 2012 (WTO, 2013). Given the central role of exports in the economy, it is important to identify the plausible factors affecting export flows between Uganda and its trading partners. These factors are expected to be useful in explaining the low levels of Uganda's exports. Identifying and examining the factors that significantly affect Uganda's export performance should facilitate the design of policies to improve the performance and ultimately overall economic growth. The objective of this paper is thus to examine the factors that determine export performance of Uganda using the gravity model of trade.

The literature on the application of the gravity model in the case of Uganda is limited, notwithstanding the growing interest of researchers and policymakers in the subject. The majority of the empirical studies on Uganda's external trade focus on the effects of exchange rate on the nation's trade balance (Wokadala, 2011), effects of exchange rate variability on exports (Kihangire, 2005), trade liberalization, export and import growth (Kilimani and Sebaggala, 2012) and export performance and economic growth (Kaberuka, Rwakinanga and Tibesigwa, 2014). None of these studies analyzed the factors that influence the pattern and the volume of bilateral trade flows between Uganda and its trading partners. Hence, this study is meant to fill this gap.

Review of Empirical Evidence

The gravity model has been extensively used in analyzing the pattern and the determinants of trade flows of countries particularly in Europe, Latin America, and Asia. For example, Gani (2008) applied the gravity model to examine the factors influencing trade between Fiji and its Asian partners, using a panel data for the period 1985 to 2002. The results suggested that Fiji's exports are significantly influenced by Fiji's infrastructure, the distance to export markets, and the real exchange rate. On the other hand, Fiji's and its partners' GDPs were found to be statistically insignificant. Further, the study fails to account for the possible influence of regional trade agreement on Fiji's bilateral trade flows.