3 CHAPTER THREE: THEORETICAL FRAMEWORK

The purpose of this section is to attempt a fairly comprehensive and rigorous presentation and examination of theories of international trade relevant to the current study.

To begin with, observations must be made in regards to the themes of international trade. These are inherently qualitative and quantitative in nature. It is important to point out that qualitative themes of international trade relate to the patterns of trade. The theory of comparative cost advantage suggests that different countries will export different goods. Which goods are exported will further be determined by natural and man-made differences that the countries are endowed with such as differences in factor supplies. This qualitative element of international trade impacts on trade because it determines each country’s comparative advantage. Conversely, the quantitative element of international trade is the terms of trade and gains from trade. Terms of trade involve indicators such as the relative prices of exports and imports while gains from trade refers to the net benefits to an agent, e.g a participating country, from entering into voluntary trade. These quantitative elements also depend on indicators such as factor supplies, technology, as well as trade policies, such as tariffs.31

3.1 The Theory of Comparative Costs

The classical theory of Comparative Cost by David Ricardo propounded in 1817 states that,

“international trade takes place because different countries have different advantages (efficiency) in the production (specialization) of different commodities. A country will specialize in the production of

that commodity in which it has a greater comparative advantage or its comparative disadvantage is the least. It follows thus that the country would export the commodity in which it has comparative advantage, and import the commodity in which its advantage is less or in which it has a comparative disadvantage.”

This is to say that international trade plays a role in redistribution of the resource of a country, namely labour, to production of goods and services in which a country possesses a comparative advantage, from production of goods and services in which it possesses a comparative disadvantage. Therefore, according to David Ricardo, the differences in Comparative Advantage in labor productivity predict trade patterns. It also determines resource utilization, even if not explicitly stated by Ricardo.

At this juncture, it is of importance to consider the assumptions that the Ricardian theory is founded on, in order to throw light on the principles of the theory. The assumptions are as follows:

i. There are only two countries trading two commodities

ii. Labour is deemed to be ‘the’ factor of production i.e. there are no other factors of production, or if there are, they can be expressed in the form of labour. This is because Ricardo like Adam Smith subscribes to the ‘Labour Theory of Value’.

iii. The Ricardian theory considers cost of production in real terms, following the Labour Theory of Value, i.e. the theory is founded on the labour cost principle alone

iv. There is perfect mobility of the factors of production within the country but imperfect mobility between two countries.

v. Production is subject to constant returns to scale

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vi. There exists full employment of all the factors of production in the two countries considered

vii. It is assumed in the theory that there exists free trade i.e. no barriers in the form of tariffs or controls between the two countries

viii. In the theory, it is implied that transport costs are ignored\(^3\)

However, it is important to appreciate that the Comparative Advantage of a nation is a dynamic concept i.e. it is not restricted to labor productivity only as initially offered in the classical theory of Ricardo. In the current scenario these variables in respect to the Comparative Advantage can take the form of better governance, inclusive economic reforms, and better business practices, among others. Evidently, the Ricardian theory implies that, in regard to the current study, Kenya and India are differently endowed with natural resources and will trade in their areas of specialization in relation to natural resources, and technology advancement, but it may also depend on things like governance, economic reforms and better business practices of the two countries.

A critical analysis of the Ricardian theory will suggest that the theory is incapable to measure up to the conditions of international trade in the light of present day conditions, especially in developing economies. Also, the researcher would like to clearly point out that the degree of development of India and Kenya differs in many respects so that ‘developing India’ is at the fore front whereas ‘developing Kenya’ is trailing behind in the ‘development race’.

Having considered the above, the application of the theory of Comparative Cost Advantage is relevant to the current study only in one aspect:

1. The Ricardian theory of Comparative Costs supports free trade for efficient production which is viable in countries of the same level of development and

therefore will suggest that the trade between India and Kenya should not be subject to any artificial limitations in the interest of corresponding gains accruing from their trade. Consequently, as India and Kenya are in a general manner clubbed together as ‘developing countries’, there will be benefits resulting from trading due to the specialization along the lines of comparative advantage provided they have free trade.

3.2 Heckscher-Ohlin Theorem: Modern Theory of International Trade

As generally accepted, the Heckscher-Ohlin (HO) theorem is one that is concerned with general equilibrium of international trade. It considers comparative advantage taking into account two factors of production, say labour and capital, whereas Ricardo’s theory takes only one factor of production, labour.

According to this theory:

"The immediate cause of international trade is the difference in the relative prices of commodities between the countries and these differences in the commodity prices arise on the account of the differences in the factor supplies in the two countries."  

Let us consider the assumptions of the HO Theorem before further discussions and applications of the theory to the current study.

The assumptions in HO theory are:

i. The theory uses a double model approach in its process of argument i.e. two countries, two commodities and two factors of production – labour and capital.

ii. The relative endowments of the factors (labour and capital) are disproportionate in the two countries i.e. factors are quantitatively fixed and qualitatively homogeneous in each country but the countries are not

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endowed with the factors in the same proportion. One country is labour abundant and one country is capital abundant. Factor abundance can be defined in two categories: price criterion and physical criterion. According to price criterion, a country is regarded as capital abundant if capital is relatively cheap and labor relatively more costlier, regardless of the physical quantities of capital and labor available in that country as compared to the other country. In physical criterion, a country is regarded as relatively capital abundant if, and only if, it is endowed with higher proportions of capital to labor than the other country\textsuperscript{35}.

iii. Perfect mobility of factors of production \textit{within} the countries but \textbf{not} between the two countries.

iv. There is perfect competition in both factor and commodity markets and full employment of resources in the two countries.

v. The production functions are different for different goods in each country but the same for each good in the two countries.

vi. The production functions for different goods determine their classification i.e. in terms of factor intensity e.g. labour intensive and capital intensive.

vii. Each production function is subjected to constant returns to scale. That is to suggest that a given proportion of factor inputs results in the same proportionate output.

viii. Trade between two countries is free and costless i.e. no existing systems of tariffs or barriers and no transport or similar costs.

ix. There exist identical consumer preferences in the two countries.\textsuperscript{36}

\textsuperscript{35} Op cit 118

Having considered the assumptions on which the HO theory is based, our emphasis will be on the relationship between price and the terms of trade. This will set the stage for the General Theory of Value where the argument is that the prices of commodities in international trade will be pivotal to determine the terms of trade as well as the patterns of trade.

Moving on, the prices of commodities are inherently determined by the supply and demand features which, in essence, point to the cost of production, which in turn depend on the prices paid for factors of production. Therefore, this will result in a relationship between prices of commodities, the prices for factors of production, the demand created, and as well as the demand for and supply of factors. However, in respect to the current study, India and Kenya may differ in factor endowments (i.e. their comparative advantage) and this may also be reflected in the commodities that are produced and traded between the two economies. Therefore, there has to be an inter-relationship between India and Kenya in respect to prices of commodities for trade which are determined by the prices for the factors of production employed.37

The researcher therefore opines that the HO theorem is of relevance to the current study considering that:

1. India and Kenya differ in factor endowments which creates the foundation for the source of comparative advantage in their trade. This results in a disparity in the prices of products on the account comparative advantage or factor endowment as well as a variance in factor proportions in question for the manufacture of the different products.

2. On the one hand, India has a large work force which is likely to make it relatively labour abundant, and at the same time capital is also largely used specially in

large industry. This has been made possible because of the policy of keeping interest rates lower than would otherwise be the case in banks and financial institutions. On the other hand Kenya is relatively labor abundant and land abundant but not capital abundant. Kenya, in as much as it is labor abundant, has not adopted the policy to make the cost of capital artificially cheaper, as it is considered a capital scarce nation.

3. Consequently, India should export products that are intensive in the factor which is abundant. India should import products that use relatively scarce factors of production. Similarly, Kenya should export more products that are labor intensive and import products that are capital intensive which is reflective of its comparative advantage.

3.3 Porter’s Theory of Competitive Advantage of Nations

Michael Porter’s theory of Competitive Advantage of nations is based on the argument that a nation has a higher competitive advantage due to the assumed reasons given herewith:

i. Competitive advantage stems from the differences in industries;

ii. That the value chain of worldwide network contributes significantly to increase its competitiveness;

iii. That innovation has a significant role in gaining and retaining competitive advantage; and

iv. Competition increases with pioneering as well as aggressiveness in exploiting new markets and technology.\(^{38}\)

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The current study on several accounts can be related to Porter’s theory if we consider the above reasons that contribute to a nation’s competitive advantage. Between the two nations, India and Kenya, it is seen that India has the competitive advantage over Kenya in terms of their trade. This is discussed further in chapter six of this thesis. However, it is important to consider the attributes that govern the competitive advantage between the two countries as discussed in Porter’s theory which are explained by him using the Porter’s Diamond.

According to Porter’s Diamond, there are four major attributes that will either support or hamper the competitive advantage of any given trading nation. These are: Factor Conditions, Firm Strategy, Structure and Rivalry, Demand Conditions and Suppliers and Related Industries.

Figure 1: Porter’s Diamond: Determinants of a National Competitive Advantage

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Factor Conditions: The factor endowments in respect to India and Kenya will definitely be an important aspect in determining the competitive advantage. Factor endowments between India and Kenya will comprise human resources, physical resources, knowledge resources, capital resources, location, and infrastructure. When comparing India and Kenya in light of the above named factor endowments, India generally supersedes Kenya by far on all accounts e.g. India has a bigger population in working age as compared to Kenya. According to India's census report of 2011, India has 62.5% of her population between the age of 15-59 involved in employment\textsuperscript{40}. Kenya on the other hand has a working population of 47.5%\textsuperscript{41}. Also, in India has a larger land area compared to Kenya, with India having around 3.3 Million sq. km\textsuperscript{42} while Kenya has only 581,309 sq. km\textsuperscript{43}. It is also noted that India has a better resources in terms of quality and quantity in respect to knowledge, capital and infrastructure resources. It is of importance to note that advanced factors such as skilled labour, communication infrastructure, technology are more abundant in India as compared to Kenya and therefore, India will enjoy a higher competitive advantage than Kenya\textsuperscript{44}.

Demand Conditions: Porter points out that the demand conditions in the domestic market will encourage the domestic firms to innovate and improve their products\textsuperscript{45} so as to make a maximum market penetration. When considering India and Kenya, India possesses a higher demand base, which is its population, (India 1.25

\textsuperscript{43} UN. http://data.worldbank.org/indicator/AG.SRF.TOTL.K2. accessed on Feb 11, 2015
billion, Kenya 44.35 million). Such a base encourages competition between firms and hence innovation and improvement in the quality of products.

**Suppliers and Related Industries:** Vigorous domestic supply of cost effective and quality inputs and the related supporting industries improves a nation’s competitive advantage.\(^{46}\) India as compared to Kenya, possess a very strong, vigorous domestic supply of cost effective and quality inputs in petro-chemicals and pharmaceutical sectors. On account of this and a very strong supportive base of related industries, India possess a higher competitive advantage than Kenya in regards to trade activities involving capital resources and finished products in petro-chemical and pharmaceutical sectors.

**Firm Strategy, Structure and Rivalry:** Porter points out that a nation’s competitive advantage in international trade depends on the behavior of individual units or business firms that are involved in the nation’s exporting trade. Therefore, the firm strategy, structure and rivalry will have a direct impact in the nation’s competitive advantage in the international trade scenario.

The firm’s strategy and structure will therefore design their operations in accordance with the government policy in operation. This will consequently depend on whether the government is implementing effective and positive industrial and trade policies in the open economy. In our case, India and Kenya follow a liberalized economy structure. Porter argues that a government that employs effective and positive industrial and trade policies will encourage the local firms to compete in international trade.\(^{47}\) In light to the current study, it is evident [as discussed in chapter 5 of this thesis] that the Indian and Kenyan governments have fine tuned their respective Industrial and Trade


\(^{47}\) Ibid, 111.
policies to encourage individual firms to engage in international trade between the two countries. A paper on India-African Partnership Initiative points out that, “India has been a willing partner to share its experience and expertise for developing entrepreneurship and small industries and thus has been making efforts to promote economic and technical cooperation with the developing countries i.e. in this case Ethiopia, Kenya and Tanzania, in the context of South-South Cooperation.”

In the eyes of Porter, the role of government will therefore be that one of a catalyst and a challenger. Government as a catalytic and challenger agent will encourage the firms in the nation to rise to high levels of competitiveness through transmitting and amplifying the forces of the diamond i.e. to design policies that necessitate an environment that put companies at an advantage in gaining competitiveness. Porter continues to suggest that the role of government will be to encourage change, promote domestic rivalry, and stimulate innovation as well as:

i. Focus on specialized factor creation

ii. Avoid intervening in factor and currency markets

iii. Enforce strict product, safety, and environmental standards

iv. Sharply limit direct cooperation among industry rivals

v. Promote goals that lead to sustained environment

vi. Deregulate competition

vii. Enforcement of strong domestic antitrust policies

viii. Reject managed trade

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To this extent, the researcher concludes that Porter’s theory of Competitive Advantage is relevant to the current study in respect to India and Kenya in that on several accounts and as supported by data from their trade activities pointed out in this current study, India has a higher competitive advantage over Kenya in regards to their trade interactions and as a trading partner.

3.4 The Vent-For-Surplus Approach

The theory of ‘Vent-For-Surplus Approach’ was originally developed by Adam Smith in his classical work in the Wealth of Nations. However, economists such as Myint and Williams revised Adam Smith’s theory to offer a more effective approach. In his theory, Myint argues that when a country produces more product than it can utilize, it creates a surplus. This over production sets off an inward movement of production, inside the production possibility frontier, that results in idle resources. The idle resources can be employed through trade with another country to vent (provide an outlet for) this surplus and thereby the country avoids any possibilities of contraction in the non-export sector and also facilitates movement to the production possibility frontier.50

Features:

- The theory seeks to provide an explanation of how colonial underdeveloped countries such as in Africa, South-East Asia and Latin America had entered into foreign trade and eventually experienced contraction of trade. Therefore, it possesses a limited scope in application.

- The theory contends that underdeveloped countries typically hold a surplus of primary goods that by and large lie idle and therefore are exportable.

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The principle distinction between the classical theory and Vent-For-Surplus theory is that the former presupposes that the trading country operates on its production-possibility frontier both before and after trade with an assumption of full employment condition, whereas the later, more practically, presumes that the country is operating, before trade, below its production-possibility curve.  

A critical conclusion by the Vent-For-Surplus Approach observes that the characteristic less developed country under the colonial rule eventually experiences an unfavorable impact of foreign trade with the mother country when it exports raw materials and imports mechanized goods i.e. the traditional sector seem to fade away under the intense competition from imported mechanized goods, employment of primitive technology, stunted growth when prices of raw materials rises among others.\(^51\)

### 3.5 The Gravity Model of Trade

According to this theory, bilateral trade between two countries is a result of ‘push’ and ‘pull’ factors that determine the total exports and imports of two trading nations. Consequently, as the name of the theory suggest, the theory is based on the gravitation forces that are connected to the geographical and spatial relationship of the two trading nations in question. This further suggested to Tinbergen (1962) the Gravity equation and hence the Gravity Model of Trade which suggested that economic size and geographic-spatial distance were the fundamental aspects that dictated bilateral trade flows in a trading relationship. Tinbergen’s equation to express the concept is as follows:

\[
T_{xy} = k \left[ S^A A S^B B / D^{AB} \right] \tag{52}
\]

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Where,

\[ T_{xy} = \text{Trade flows between countries X and Y} \]

\[ k = \text{Constant} \]

\[ S = \text{Size of the country} \]

\[ D = \text{Distance} \]

The propounded hypothesis for the Gravity Model of Trade holds that:

(i) Size of the nations and the trade flows have a positive relationship, and

(ii) the distance between the two trading nations and the trade flows have a negative relationship.

Apart from the hypothesis, the gravity model suggests that distance between two trading nations adversely affects the trade by creating barriers which eventually lead to higher costs. Therefore, it proposes to address the distance problem by ensuring the measurement of the attributes for gravity distance through:

(i) physical size i.e. geographical area in kilometers and population number,

(ii) economic size i.e. GDP and GDP Per Capita, and

(iii) distance attributes i.e. common attributes such as border, language, regional trading block, currency, Colonial relationship, policy, etc.\textsuperscript{53}

Mithani in his discussion of the Gravity Model of Trade (GTM) points out that GTM is effective in explaining the trend and pattern of bilateral trade flows; that GTM is an ex-post analysis i.e. it describes the preceding performance but cannot predict the future; and as a drawback, GTM does not outline any welfare outcome of the trade. On the other hand, however, empirical findings of the GTM state that:

\textsuperscript{53} Ibid, 155.
i. Spatial distance matters i.e. larger distance means lesser/smaller trade volume

ii. Large distance means high transportation costs and longer time. Hence greater risks.

iii. There is positive border effect on trade i.e. provinces on border surroundings of the connected nations have greater trade involvement from the Small and Medium Enterprises than in the case of distant states of the nations.54

3.6 The Stolper-Samuelson Theorem

Stolper-Samuelson Theorem assumes a model of two factors of production, two goods and two countries to boldly suggest that protection measures in international trade between the two countries in question will promote the scarce factors of production. Consequently, this implies that, free trade i.e. the practice of trade without protection measures hurts the scarce factors of production.55 The theory employs a two sector general equilibrium analytical model that shows that when tariffs are enforced in a labour-scarce country, the impact will result in a price rise in the imported good relative to exports and consequently raising significantly the wage of labour.56

Suggested Versions of Stolper-Samuelson Theorem

Economists have analyzed the Stolper-Samuelson tenet and have suggested various versions in the spirit of trying to understand and apply the theory with regards to various situations and circumstances. These suggested versions include:

1. General Version

An increase in protection raises the real wage of the scarce factor of production and lowers the real wage of the abundant factor of production.

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56 Ibid, 10.
Features:

- This version expresses a simple and strong relationship between goods prices and factor prices.
- Goods prices and factor prices have nothing to do with factor scarcity or abundance.
- This is independent of whether prices change because of protection or any other reason.\(^\text{57}\)

2. **Restrictive Version**

Free trade lowers the real wage of the scarce factor and raises that of the abundant factor compared to autarky.

Features:

- Like the General Version, this projects a simple and strong connection relating goods prices and factor prices.
- It is not tied to the factor insufficiency or abundance of the factors.
- It is independent of prices change due to protection or any other reason.

3. **Essential Version**

An increase in the relative price of a good increases the real wage of the factor used intensively in producing that good and lowers the real wage of the other factor.

\(^{57}\) Ibid, 12.
Features:

- Essential Version embodies the essence of Stolper-Samuelson insight
- Requires the fewest assumptions for its validity.
- Does not have a relationship with trade or even more than one country.
- Does not address the effects of protection.
- Compared to the former two versions, the Essential Version is the most generally valid of the three.  

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4. Strong Version with Even Technology

A rise in the price of any good, all other prices remain constant, causes an increase in the real return to the factor used intensively in producing that good and a fall in the real returns to all other factors.

Features:

- Requires restriction on technology that permits an unambiguous definition of the intensively used factors.
- Takes into account the losses to all other factors.

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5. **Friends and Enemy Version**

Every good is a friend to some factor and an enemy to some other factor.

**Features:**

- “Friend” – if rise in the price of the good, with all other goods prices constant leads to an unambiguous rise in the real return to the factor.
- “Enemy” – if the same price changes leads to an ambiguous fall in real return.
- The same result is valid for uneven technologies according to economists Kemp and Wan.
- Version rests critically on the assumption of non-joint production.
- Proven to be the simplest and most intuitive version of the Theorem available for more than two goods and factors.\(^{60}\)

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6. **Correlation Version**

For any vector of goods price changes, the accompanying vector of factor price changes will be positively correlated with the factor-intensity-weighted averages of the goods prices changes.

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\(^{59}\) Ibid, 15-16.

Features:

➢ Deduces a three-way relationship between vector changes in factor prices, vector changes in good prices and a particular matrix of factor requirements.

➢ Complements the Friend and Enemy version since it introduces a third variable

➢ Does not address the question whether the gains and losses are real.

➢ It is a weak statement in regards to factor prices since it makes an average statement about all relative factor prices changes.\(^{61}\)

3.7 Product Life Cycle Theory

The Product Life Cycle Theory like Porter’s Competitive Advantage theory is a recently developed theory that mainly focuses on individual firms in a country rather than considering the country as a whole. Propounded by Raymond Vermon in 1960, the Product Life Cycle theory, also called the International Product Life Cycle Theory (IPLC), sets out to address two principal questions:

i) Why does trade take place?

ii) Why does investment occur?

Further, the theory seeks to elucidate how a company will export its product initially, to later be followed by Foreign Direct Investment through a process of evolution in the Product’s Life Cycle.\(^{62}\)

It is to be noted that Raymond Vermon extensively disagrees with the authors of the classical and Neo-classical theories on trade especially those tenets that promote the Comparative Cost theory. He instead argues that information, uncertainty and economies


of scale\textsuperscript{63} propel his theory to sustain a product that is exported at first, and then eventually FDI plays a major role in marketing of the same product.

Features:

The theory points out three distinctive stages of in the life of a product. These are:

i. New Product Stage

- Firm introduces an innovative product to supply a need in the market.
- Production in limited volume mainly for domestic market.
- Exports are either nonexistent or in a limited quantity as the product grows into the second stage.

ii. Maturing Product Stage

- Domestic and foreign demand for product increase due to acceptance and popularity.
- Firm expands production by setting up a manufacturing facility abroad to meet both domestic and foreign market demand.
- High levels of competition at this stage, plans are made to produce the product in developing countries.

iii. Standardized Product Stage

- Last stage in the Product Life Cycle Theory.
- Market for product stabilizes and the commodity becomes price sensitive.
- Manufacturers search for low cost producing countries with objective of being cost effective.\textsuperscript{64}

\textsuperscript{63} K. Aswathappa, \textit{International Business, 4\textsuperscript{th} ed.}, (New Delhi: Tata McGraw Hill, 2010), 92.
\textsuperscript{64} K. Aswathappa, \textit{International Business, 4\textsuperscript{th} ed.}, (New Delhi: Tata McGraw Hill, 2010), 92.
When analyzing the Life Product Cycle Theory, it can be clearly seen that the theory possess an element of versatility due to the wide room for application in various products. It is also important to take note that the theory has the flexibility to explain the core questions that Vermon seeks to address i.e. why trade takes place and why FDI is an investment option. The IPLC theory has a wide acceptance in the modern international trade especially with regard to high-income and mass consumption countries. To be fair, critics to the IPLC theory point out that Vermon’s approach offers a weak explanation as to why international trade takes place. The critics emphasize that innovation, large domestic markets, and capital intensity are dynamic variables and therefore the theory stands weak as offered by Vermon. It is further argued that the theory supports products developed and produced in the USA when it was dominant in world trade, but as it is, the USA is not the only country with ability to innovate since R&D activities are cropping up from everywhere. Therefore, the generalizations drawn from the theory no longer hold relevance.\textsuperscript{65}

3.8 TERMS USED

Having had a bird’s eye view of the theoretical framework, we shall now turn to the terms used in this research exercise. This section seeks to highlight the unique terminologies by way of definition in relation to the context they have been used so as to exhaustively understand the concepts used there in. The terms used include:

\textbf{Majimbo} - a Swahili word for ‘regionalism’. An abstract noun from the word “region” (in Swahili, sing.\textit{jimbo}, pl.\textit{ majimbo}). Regionalism sought to divide Kenya into regions based on ethnic affinities. One aspect of the move was benign in that it aimed at instituting a federal system of government in Kenya, thereby empowering different

\textsuperscript{65} K. Aswathappa, \textit{International Business, 4\textsuperscript{th} ed.}, (New Delhi: Tata McGraw Hill, 2010), 93.
ethnic groups by giving them certain autonomy to run their own affairs instead of depending on central government planning.66

‘Mwanainchi’ – a Swahili word which means “a child of the earth” or child of the land. Therefore the phrase ‘Mwanainchi’ will translate to ‘citizen’ of the land.67

Bantus – a group of people speaking the Bantu family languages originally from West Africa that with time have spread over the Sub-Sahara Africa including East Africa and South Africa. Economic activities of the Bantus were farming, iron smelting.68

Cash Compensatory Support (CCS) – This is a scheme introduced in 1966 by the Indian government. It is a scheme that is selective in nature and offers assistance in form of compensation to Indian exporters for unrebated indirect taxes paid by exporters on inputs, higher freight rates, and market development costs.69

Census of Industrial Production (CIP) – A systematic survey of Industrial productive enterprises carried out by the government. The survey involves the nature of product, quantity and type of inputs, the number and types of employees, and value added.70

Common External Tariff – this is a tariff charged on trade with non-members by all countries in a customs union or a common market. However, when used with capitals, Common External Tariff normally refers to the external tariffs of the European Union.71

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71 Ibid, 68.
**Common Market for Eastern and Southern Africa (COMESA)** – with its headquarters in Lusaka, Zambia, COMESA is the largest regional economic integration scheme in Africa in terms of spatial extent and the number of member countries. It was established by a treaty signed in 1993 in Kampala, Uganda and was ratified in 1994 in Lilongwe, Malawi as a strengthened successor to the erstwhile Preferential Trade Area (PTA) for Eastern and Southern Africa which had existed since 1981. The COMESA members include: Angola, Burundi, Comoros, Democratic Republic of Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Madagascar, Malawi, Mauritius, Namibia, Rwanda, Seychelles, Sudan, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe.72

**Comparative Advantage** – A country is said to have comparative advantage in production of a good if it has lower opportunity costs in producing this good compared to another country or the rest of the world. If countries specialize in production of those goods in which they have a comparative advantage then free trade improves production and consumption efficiency by increasing aggregate output using the same amount of resources and expanding the choice of consumers.73

**Congress (I)** – the party in power in India from 1980 to 1984 with Indira Gandhi as the Prime Minister of India and head of the Congress (I) government.74

**Cushites** – most called ‘Hamites’ in the past, are an indigenous people of North East Africa who are found today as far south as past the Equator in East Africa and are essentially pastoralists.75

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Development Plan – The use of central planning in 3rd World countries as a route to economic development. Records show earliest plans were carried out before and after the 2nd World War in British, French, Belgian and Portuguese colonies. These plans included a crash investment program especially in the Public Sector and a commitment to rapid industrialization.\(^{76}\)

Exchange Rate – The price of one currency in terms of another. A par exchange rate is that agreed between governments, or registered with a central authority such as International Monetary Fund. A market exchange rate is the actual price on foreign exchange markets.\(^{77}\)

Exim Policy – A set of controls used by government to promote Export Import trade.\(^{78}\)

Exports – Goods and services produced in a country and sold to non-residents. Visible exports are goods sent abroad; invisible exports are services sold to non-residents.\(^{79}\)

Export Promotion – (1) Government activities to help sell exports by providing export incentives at home, and various forms of practical assistance for exports abroad i.e. advice on local trading laws and practices, provision of export credits or guarantees on favorable terms. (2) A strategy for promoting economic development in less developed countries. This involves running an open economy, relying on foreign markets to allow export-led growth.\(^{80}\)

Gini Coefficient - A measure of income distribution, devised by the Italian demographer and statistician Corrado Gini (1884–1965). It is the ratio of the area


\(^{78}\) Ibid, 122.

\(^{79}\) Ibid, 146.

between a LORENZ curve and the line of absolute equality to the area of the entire triangle below that line.81

**Globalization** – The increasing worldwide integration of economic, cultural, political, religious and social systems. Economic globalization is the process by which the whole world becomes a single market i.e. goods and services, capital and labor are traded on a worldwide basis, and information and the results of research flow readily between countries.82

**Great Depression** – A worldwide economic downturn beginning in the late 1920s and lasting until the mid 1930s. The effect of the Great Depression was to reduce international trade and national incomes. Farming was particularly badly hit with large declines in agricultural product prices.83

**Import Substitution** – A strategy for industrialization of less developed countries (LDCs), of concentrating initially on replacing imports by domestically produced substitutes. This has the advantage that it is already known what markets exist for the products, but the disadvantage that as the imports most easily displaced fall, further progress becomes ever more difficult.84

**Imports** – Goods and services bought by residents of a country but provided by non-residents. Visible imports are goods physically brought into the country. Invisible imports may involve the supplier entering the country, for example to put out oil-well fires, or residents going abroad to enjoy the services of hotels, or entertainments.85

**Indo-Nepal Treaty of 1996** – signed in 1996 and renewed in March 2007, in which both countries would provide national treatment to each other free of any

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83 Ibid, 178.
84 Ibid, 196.
85 Ibid, 196.
restriction. With respect to manufactured goods, the government of India would provide special treatment to Nepal i.e. India would provide preferential treatment to Nepal, free of customs duty and quantitative restrictions if Nepalese goods fulfilled certain conditions.86

**Industrialization** – The process of moving resources into the industrial sector. This is common in the early stages of economic development, when resources move out of primary production. Industrialization was the norm in the now advanced countries earlier in their development, and was energetically pursued by many less developed countries and by the former planned economies of the former Soviet Union and Central and Eastern Europe.87

**International Economics** – The parts of economics concerning the relations between countries. This includes trade in goods and services, factor movements, including migration, capital movements, and technology transfer, and international monetary arrangements, including exchange rates and exchange reserves. It also studies government policies affecting trade, factor movements, and monetary arrangements, international negotiations, regional institutions such as EU, NAFTA, WTO and IMF.88

**Janata Government** – India’s first non-Congress government in power from March 1977 to July 1979 with Morarji Desai as Prime Minister.89

**Jua Kali** – a Swahili phrase translating to “hot sun” which is a reference to the informal economy of Kenya. The entrepreneurs have their businesses under the equatorial sunshine shaded by plastic bags or old *mabati* (tin roofing).90

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88 Ibid, 217.
Kenya African Democratic Union (KADU) – This party was formed in June 1960 in Kenya and was headed by Ronald Ngala. KADU was the principal opposition to KANU and advocated for regional government system. KADU was later merged with KANU in 1964 to become one KANU.91

Kenya African National Union (KANU) – founded in May 1960 with James Gichuru as President of the party. KANU has dominated the Kenyan politics until the era of multiparty system when it was ousted from power in 2002.92

Kenya Tea Zones – An extensive area in the Kenyan highlands where Tea is grown in large scale for commercial, especially for export, purposes.

Kenya Vision 2030 – the country’s new development blueprint covering the period from 2008 to 2030. The vision developed through an all-inclusive and participatory stakeholder consultative process, aims at transforming Kenya into a newly industrializing, “middle income country providing a high quality life to all citizens by the year 2030”.93

Kenyatta Administration – This is the period in which President Jomo Kenyatta was in Power in Kenya from 1963 to 1978. President Jomo Kenyatta was the first president of Kenya.94

Kibaki Administration – This is the period in which President Mwai Kibaki was in power from 2002 to 2013. President Mwai Kibaki was the third president of Kenya.95

90 Steve Daniels, *Making Do: Innovation in Kenya’s Informal Sector* (USA: Creative Common Attribution, 2010), 8
94 Researcher’s Knowledge.
95 Researcher’s Knowledge.
**Liberalization** – A programme of changes in the direction of moving towards a free-market economy. This normally includes the reduction of direct controls on both internal and international transactions, and a shift towards relying on the price mechanism to coordinate economic activities. In such a programme less use is made of licenses, permits, and prices controls, and there is more reliance on prices to clear markets. It also involves a shift away from exchange controls and multiple exchange rates, towards a convertible currency.⁹⁶

**License-quota ‘Raj’** – This is a type of governance [license-quota-subsidy raj (governance)] established in India in the year 1950 which allowed those who possessed a bit of paper signed by a bureaucrat or minister to raise investment capital or find a business partner.⁹⁷

**Limuru Conference of 1966** – The conference was held in Limuru, Kenya in which the KANU Governing Council implement the so called, “conservative plan” which saw the election of eight Vice Presidents.⁹⁸

**Mahalanobis Model** – It represents an alternative approach to planning that focuses on the bottlenecks created by a shortage of capital goods rather than on the shortage of aggregate saving. Accordingly, given a specific time horizon the growth path of the economy is determined by three parameters, viz., incremental capital output ratio in the consumer goods sector and the capital goods sector, and the proportion of total investment going to the capital goods sector. The model concludes that, the higher the allocation of investment to capital goods industries, the lower will the rate of growth of

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real income in the short run covering the immediate future but the growth rate of both real income and consumption will be higher in the long run.\textsuperscript{99}

**Mercantilists** – proponents of Mercantilism, an economic theory popular in the 16\textsuperscript{th} to 18\textsuperscript{th} centuries that viewed a nation’s supply of capital as the determinant of welfare. When this view was coupled with assumptions that the total value of world trade was fixed it implied a policy of seeking balance-of-payments surpluses to increase capital inflow, and advocacy of protectionism to achieve this.\textsuperscript{100}

**Most Favored Nation (MFN)** – A country with rights for equal treatment under a trade agreement. An MFN clause stipulates that imports from the partner country will be treated no less favourably than imports of similar goods from any other country.\textsuperscript{101}

**Moi Administration** - This is the period in which President Daniel Arap Moi was in Power in Kenya from 1978 to 2002. President Daniel Arap Moi was the second president of Kenya.\textsuperscript{102}

**Mudaliar Committee** – This was a sixteen member group also known as the Health Survey and Planning Committee headed by Mudaliar, which was appointed in 1962 to review and assess the implementation of the First and Second Five Year Plans of the Indian Economy and to make recommendations for the future.\textsuperscript{103}

**National Rainbow Coalition government (NRC)** – the party in power in Kenya from 2002 to 2007 with President Mwai Kibaki as head of government.\textsuperscript{104}

\textsuperscript{100} John Black et al, *Dictionary of Economics, 4\textsuperscript{th} ed.*, (UK: Oxford University Press, 2012), 261.
\textsuperscript{101} Ibid, 270.
\textsuperscript{102} Researcher’s Knowledge.
\textsuperscript{104} Researcher’s Knowledge.
New Economic Policy (NEP) – Refers to a set of transformational policy changes introduced by the Indian government in 1991 to reverse the then existing economic policies to achieve the country’s macroeconomic objectives.\(^ {105}\)

Nilotes – A group of people whose languages are closely related. They are pastoralists and are mainly divided into three major branches i.e. Highland Nilotes, Plains Nilotes and River and Lake Nilotes.\(^ {106}\)

Nyanza – This is the South Western region in Kenya home to the abagusii, Luo, Kuria communities.\(^ {107}\)

Open General License (OGL) – OGL includes those items which are freely importable and do not require import license.\(^ {108}\)

Outward looking policies – Policies that not only encourage free trade but also the free movement of capital, workers, enterprises and students, a welcome to multinational enterprise, an open system of communication.\(^ {109}\)

P.C. Alexander Committee of 1978 – Committee on Import Export Policies and Procedures instituted by the government of India which recommended the simplification of import licensing procedures and provided a framework involving a shift in the emphasis from ‘controls’ to ‘development’.\(^ {110}\)

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\(^{107}\) Researcher’s Knowledge.
Parastatal – This is a firm with some government ownership i.e. in legal terms, a parastatal is either government owned or jointly government and private owned.\textsuperscript{111}

Planning Commission – Set up in March 1950 by the Government of India with the aim of promoting rapid rise in the standard of people by efficient exploitation of the resources of the country, increasing production and offering opportunities to all for employment in the service of the community.\textsuperscript{112}

Post-Election Violence – Kenya was engulfed by severe political and ethnic violence which was sparked off by election fraud and controversy over the results of presidential elections that took place in December 27, 2007.\textsuperscript{113}

Protectionist Measures – Policies of restriction of international trade, with the aim of preventing unemployment or capital losses in industries threatened by imports, promoting particular types of industrial development affecting the internal distribution of incomes, or improving a country’s terms of trade by exploiting its international monopoly power.\textsuperscript{114}

Quantitative Restrictions – Quotas especially on imports and foreign exchange, imposed to reduce a Balance of Payments deficit.\textsuperscript{115}

Real Gross Domestic Product – Gross domestic product divided by a suitable price index, to express it in real terms. The price index used for this purpose is usually the GDP deflator; since this covers the prices of investment goods and government

\textsuperscript{113} Researcher’s Knowledge.
purchases as well as consumer expenditure, it is more suitable than the retail price index.\textsuperscript{116}

**Real Growth Rate** – A measure of (economic) growth from one period to another expressed as a percentage and adjusted for inflation (i.e. expressed in real as opposed to nominal terms). The real economic growth rate is a measure of the rate of change that a nation's gross domestic product (GDP) experiences from one year to another. Gross national product (GNP) can also be used if a nation's economy is heavily dependent on foreign earnings.\textsuperscript{117}

**Savings and Credit Cooperative Societies (SACCOs)** – A registered cooperative society whose main function is to promote savings among its members and to create a source of credit to its members at a fair and reasonable interest rate.\textsuperscript{118}

**Shifta (brigand) War** – was a rebellion against the Kenyan government from 1964 to 1967 fought mainly by people of Somali origin who wanted to secede the predominantly Somali populated North Eastern Province of the country to be part of the Republic of Somalia.\textsuperscript{119}

**Simla Agreement of 1972** – An agreement signed between India and Pakistan pledging to use peaceful means to sort differences in the future. Both countries also agreed to pull back their troops in Jammu and Kashmir to their respective sides of internationally recognized border. The agreement also stipulated the countries resume economic and diplomatic relations.\textsuperscript{120}

\textsuperscript{117} Investopedia, Definition of ‘Real Economic Growth Rate’ available from http://www.investopedia.com/terms/r/realeconomicrate.asp; internet; accessed on April 09, 2014.
\textsuperscript{120} James Wynbrandit, *A Brief History of Pakistan* (New York: Infobase Publishing, 2009), 204.
Small and Micro Enterprises (SMEs) – According to the definition by the European Commission, an enterprise qualifies as an SME if it meets the criterion on the employee headcount (between 50 and 249 for medium-sized, between 10 and 49 for small, and between 1 and 9 for micro), and one of two other criteria: a turnover of no more than 50, 10, or 2 million Euros, or a balance sheet of no more than 43, 10, or 2 million Euros, for medium-sized, small or micro, respectively.\textsuperscript{121}

Structural Adjustment Loan – Loans at concessional rates available only to low-income countries. Usually lasting up to three years, covering both structural and macro-economic adjustments and are drawn up in collaboration with the World Bank. These are loans to support structural adjustment programs affecting the whole economy.\textsuperscript{122}

Sub-Saharan Countries – African countries south of the Saharan Desert.

Tariffs – A scale of charges. In economics a tariff was originally a schedule of taxes on imports; it now refers to the actual import duties.\textsuperscript{123}

Terms of Trade – The ratio of an index of a country’s export prices to an index of its import prices. The terms of trade are said to improve if this ration increases, so that each unit of exports pays for more imports, and to deteriorate if the ratio falls, so that each unit of exports buys fewer imports.

The Abid Hussain Committee of 1984 - Committee on Trade Policies instituted by the government of India in 1984 which recommended on export promotion policy and strategy, import policy, technology imports and in perspective: rationalization of duty drawback system, exemption of Cash Compensatory Support (CCS), and 50% of the

\textsuperscript{123} John Black et al, Dictionary of Economics, 4\textsuperscript{th} ed., (UK: Oxford University Press, 2012), 400.
export’s profit from the income tax, reformulation of import replenishment system for export production, and so on.\textsuperscript{124}

\textbf{Trade} – The exchange of goods between individuals or nations. Trade is the basic component of economic activity and is undertaken for mutual advantage. It is the process of distribution.\textsuperscript{125}

\textbf{Trade Policy} – A (Liberal) Trade Policy is aimed at allowing a country’s residents to take part in international trade with the minimum of interference\textsuperscript{126} whereas A (Strategic) Trade Policy is intended to influence the trade policies of other countries.\textsuperscript{127}

\textbf{Westminster Model Of Constitutionalism} – British styled form of constitutionalism.

\textsuperscript{124} Saleem Shaikh, \textit{Business Environment 2\textsuperscript{nd} ed.}, (Noida: Dorling Kindersley, 2010), 94.
\textsuperscript{125} John Black et al, \textit{Dictionary of Economics, 4\textsuperscript{th} ed.}, (UK: Oxford University Press, 2012), 411
\textsuperscript{126} Ibid, 238.
\textsuperscript{127} Ibid, 391.