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The Political Economy of Import Substitution in the 21st Century: The Challenge of Recapturing the Domestic Market in Rwanda[1]

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ABSTRACT

Import substitution has been marginalised from development policy discourse since the 1970s. This paper examines the Rwandan government's recent attempt at reintroducing industrial policy with some attention devoted to 'recapturing the domestic market' – a term used to replace the ignominy associated with 'import substitution.' The paper examines two cases – cement and textiles – where such policies have been recently established in Rwanda.

The paper argues that any attempt at recapturing the domestic market will require a strategy close to the policies of East Asian developmental states in terms of 'picking winners.' However, strategically maintaining reciprocity through state-business relationships is only part of the challenge. Though foreign investors have been leant on initially, actions must be put in place to develop local capitalist partners who may step in if foreign investors leave once incentives are reduced. This is further complicated by the government's failure to develop partnerships with existing local capitalist partners. The Rwandan government is also constrained by a small market size. Any attempt at import substitution must occur in the context of accessing larger markets through the East African Community (EAC). This paper demonstrates that such regional trade agreements constitute a much greater constraint on the use of industrial policy than multilateral trade agreements or bilateral trade agreements with the United States of America or European countries (although pressure from donors may also contribute to reducing policy space). Such challenges showcase how the Rwandan government has sought to build reciprocal control mechanisms while attempting to access large markets through regional integration. Though the Rwandan government has made some progress recently, state intervention is required to reintroduce import substitution in the 21st century and must be balanced by the need to meet domestic and international political constraints.

Keywords: Import substitution, Industrial Policy, Rwanda, political economy, textiles, cement

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LIST OF ACRONYMS

AfDB	African Development Bank
AGOA	African Growth and Opportunity Act
AMZ	Apparel Manufacturing Zone
API	Agro-Processing Industries
BIP	Backward Integration Policy
BRD	Rwanda Development Bank
CET	Common External Tariff
DMRS	Domestic Market Recapturing Strategy
DRC	Democratic Republic of Congo
EAC	East African Community
ECLA	Economic Commission for Latin America
EGF	Export Growth Facility
EPZ	Export Processing Zone
GCC	Global Commodity Chains
GPN	Global Production Networks
GVC	Global Value Chains
IMF	International Monetary Fund
ISI	Import Substitution Industrialization
KCC	Kigali Cement Company
KGC	Kigali Garments Centre
MIFOTRA	Ministry of Public Service and Labour
MINECOFIN	Ministry of Finance and Economic Planning
MINICOM	Ministry of Trade and Industry
NIE	New Institutional Economics
NSE	New Structural Economics
PPC	Pozzolanic Portland Cement
RIG	Rwanda Investment Group
RPF	Rwandan Patriotic Front
RSSB	Rwanda Social Security Board
SEZ	Special Economic Zone
TRIPS	Trade-related Intellectual Property Rights
UNECA	United Nations Economic Commission for Africa
UNIDO	United Nations Industrial Development Organization
UTEXRWA	*L'Usine Textile du Rwanda*
WTO	World Trade Organization

Introduction: A Brief History of Import Substitution

Import substitution has had a chequered history.[2] Though many attempts at import substitution ended in failure, history demonstrates that such policies were a feature of all successful late development stories. The intellectual origins of 'infant industry' arguments date back to Friedrich List (1928). List argued that Germany (and other latecomers) should protect infant industries to build up productive forces in the national economy. Such arguments, which were closely aligned with import-substituting industrialization (ISI), also had political characteristics and were closely associated with a desire for self-sufficiency and independence (Schmitz 1984). Reinert (2007) and Chang (2002) argue that it was actually Alexander Hamilton, the first Treasury Secretary of the United States, who first developed the infant industry argument. Hamilton's industrial project in the United States was in direct opposition to the work of Adam Smith (1776), who Reinert (2007) argues, was guilty of hypocrisy in advocating for free trade abroad while acknowledging that only nations with manufacturing industries could win wars. Such policies were not the preserve of Western countries. In the first half of the 19th century, the Ottoman Governor of Egypt, countered the expansion of Britain's dominance in trade by erecting tariff walls and moving ahead with industrialization (Waterbury 1999). In the late 19th century, the Meiji government protected industries and secured the home market in its drive to secure structural transformation (Norman 1940, Lockwood 1968).

Though the case for import substitution had its critics, the Early Development Economics scholars (Rosenstein-Rodan 1943, Lewis 1954, Singer 1950, Hirschman 1958, Rostow 1960) generally agreed that industrialization should retain a central position in development policymaking. Industrialization (and associated state intervention) came under heavy attack from some neoclassical economists (Bauer 1971, Balassa 1982, Krueger 1974, Lal 1985). Critics argued that such policies had been associated with wasteful outcomes, created price distortions and resulted in unproductive rent-seeking. The World Bank and International Monetary Fund (IMF) highlighted the sources of the problematic industrial pattern on the continent as government intervention, which distorted markets and encouraged ISI encouraging ISI at the expense of agriculture (Stein 1992). Protectionist policies had been the norm

[2] See Bruton (1998) for a review of the literature on import substitution.

across many African countries. In the 1970s, Kenya had an increasing reliance on import controls, Sudan extensively used quotas and tariffs and Nigeria and Ghana were “on the high end of the scale in terms of the number of good covered by quantitative restrictions” (Bienen 1990, 713). Such arguments provided the scholarly legitimacy for the structural adjustment policies that were forced on developing countries around the world in the 1970s and 1980s. Added to this, most African governments adopted structural adjustment programmes when their economies were weakened by fiscal crises or trade deficits. Several countries went through many rounds of structural adjustment programmes before reducing tariffs. Ghana made the move to low and uniform tariffs in around five years, “which was too rapid for the industrial sector to adjust properly and which yielded disappointing results in terms of growth and competitiveness” (Lall 1995, 2027). In Cote d’Ivoire, a 40 per cent reduction in tariffs led to the collapse of the chemical, textile, shoe and automotive assembly industries with local companies unable to compete against foreign imports (Stein 1992).[3]

Boone (1994) argues that trade liberalization was designed to change the nature of government-business relations by depoliticizing commerce. Instead, outcomes in the two countries she studied (Senegal and Cote d’Ivoire) signaled little improvement in the strength of productive capital in these countries and the “enduring significance of ‘the sphere of circulation’ as a site of both private and public accumulation” (Boone 1994, 463). Liberalization did little to support the creation of domestic capitalist classes and had other adverse consequences. Across the continent, it has led to the dismantling of existing industrial capitalist sectors. Some (Stein 1992) warned of such outcomes in the 1990s and others (Page 2012, Rodrik 2016) have provided evidence that this has indeed occurred.

The dominance of New Institutional Economics (NIE) in the 1990s was associated with the World Bank (1997) proposing reconsidering the role of the state in development thinking. However, such arguments did not play out as promised. Instead, the state was only brought back in to develop the right institutions to support

[3] Today, for the most part, African governments are self-disciplined into operating within the confines of international trade norms. In most African countries, applied tariffs are far below bound tariffs (Khan 2007). Since most African countries have liberalized financial sectors, this reduces their capacity “to take advantage of the WTO’s permissive rules on subsidizing science and technology by placing limits on taxation and public spending” (Shadlen 2005, 758).

free markets. There was no place for industrial policy in NIE's Good Governance paradigm. In fact, industrial policy has remained marginalized from development policy discourse since the heydays of Early Development Economics (Rodrik 2008). It has reappeared recently in the form of Justin Lin's New Structural Economics (NSE). However, Lin is reluctant to encourage governments in developing countries to stray too far away from comparative advantage. This is a far cry from the aggressive state intervention associated with 'picking winners', which developmental state scholars (Amsden 1989, Wade 1990) argue East Asia pursued.

The Ethiopian government is one country that has gone against donor advice to implement industrial policy in recent years. Meles Zenawi's government emphasized the importance of industrial policies in line with developmental states of the past (Oqubay 2015). More recently, there are signals that the tide is turning across the continent. The United Nations Economic Commission for Africa (UNECA) and the United Nations Industrial Development Organization (UNIDO) have both been increasingly vocal about the need for aggressive industrial policies on the continent and focusing on the continent's own regional markets.[4] The East African Community (EAC) – a regional bloc comprising Uganda, Kenya, Tanzania, Burundi and South Sudan – has emphasized similar priorities, beginning with a proposed ban on second-hand clothing to promote local textiles and garments industries.

This paper will examine how the Rwandan government has recently begun to develop industrial policies to promote its domestic manufacturing sector. It will examine the challenges associated with attempts to recapture the domestic market after almost two decades of trade liberalization. This paper will demonstrate how Rwanda has attempted to achieve such goals while adhering to EAC trade agreements and negotiating international pressures from donors and other interest groups.

The central argument for this paper is that for small countries like Rwanda, successful import substitution is likely to depend on the government's capacity to develop and sustain reciprocal control mechanisms with emerging capitalists while abiding by bilateral and multilateral trade agreements. Related to this central argument, there are four sub-arguments. First, the paper follows Gerschenkron (1962) in arguing that the nature of late development has meant that industrialization will

[4] UNECA has a long tradition with supporting work on industrialization, with interest sparked by S.J. Patel's study of industrial growth in Africa (Ewing 1964).

require heavy state involvement and the trajectory of industrial transformation will be particular to the context and institutions in Rwanda. Thus, successful import substitution is likely to depend on 'picking winners' and retaining space to experiment and learn from failure in the vein of developmental state scholarship than NSE's more market-friendly approach. The second sub-argument is that any protectionism for Rwandan-based companies must be limited by the current imperative of remaining open to regional competition so as to access larger markets in the future. Thus, the Rwandan government has made the creation of a stronger EAC a priority for its long-term development. However, such regional engagement must be counteracted by strong state-business relationships to compete with regional firms in the domestic Rwandan markets and regional markets (EAC and also, the Congolese market). Given such constraints, the third sub-argument follows that for import substitution to succeed, the Rwandan government has to develop and sustain reciprocal control mechanisms with capitalist partners. Amsden (2001) argues that East Asian developmental states retained such mechanisms where incentives were tied to results and contributed to prevent wasteful rent seeking behaviour. The government must ensure such mechanisms are used to discipline and monitor private enterprises to promote learning (Khan 2000).[5] Lastly, since import substitution itself is a political act (as is the support of backward and forward linkages) (Hirschman 1968), the government is constrained by having to rely on foreign investors to be lead capitalist partners in these strategies. To ensure the transfer of technologies, local firms must be supported to ensure that the benefits of such strategies are absorbed within the country in case foreign firms leave. Though recent attempts at industrialization in Rwanda should be welcomed, it is increasingly difficult for the government to find local capitalist partners while having to lean on foreign investors in the short-term for technological acquisition and local linkages development.

The Marginalization of Import Substitution in the 21st Century

After World War II, Raul Prebisch was among the main advocates for import-substitution industrialization. He (1950) argued that the prices of raw materials, which

[5] As Amsden (1989) explored in Korea, "rents in the form of policy-induced conditional subsidies may be created by a developmental state" (Khan 2000, 22).

accounted for nearly 90 per cent of exports from developing countries, fell over time relative to the prices of manufactured goods. As head of the United Nations Economic Commission for Latin America (ECLA), Prebisch's ideas provided a platform for import-substitution industrialization policies across the continent. Though neoclassical free trade theory would eventually gain more support, Prebisch's ideas influenced heterodox thinkers and dependency theorists including Andre Gunder Frank's (1966) theory of unequal exchange (Love 1980). Such ideas have been contested recently with some (Sarkar and Singer 1991) reasoning that manufacturing may not have enjoyed better relative prices than agriculture in recent years. Kaplinsky (2006) argues that China's increasing growth and growing domestic demand for commodities skewed the terms-of-trade in favour of some agricultural goods. Meanwhile, others (Evans 2014) have argued that development has become increasingly 'bit-driven' in the 21st century and that the knowledge economy is a central arena for capturing surpluses today. Despite these arguments, investing in domestic manufacturing (which has been traditionally associated with import substitution) continues to have significant positive effects for late developers. The benefits are not just restricted to jobs. Manufacturing is traditionally perceived to be a 'learning centre' in the economy (Chang 2010). The sector also organizes technological innovation and provides opportunities for backward and forward linkages, as well as diversification of the economy.

In the 1980s, African countries had been gaining a comparative advantage in labour-intensive manufacturing (Jomo and Von Arnim 2011). However, trade liberalization prematurely exposed African infant industries to global competition with comparatively mature industries, precipitating deindustrialization. Trade liberalization in Africa occurred at a much faster pace (primarily because of pressure of donors) than in Asia and left no opportunities for industrial restructuring and diversification of the economy (Mkandawire and Soludo 1998). In the era of structural adjustment and the associated market-enhancing decades of reforms that have followed, import substitution has become nothing short of an odious word for development policymakers. Most within the mainstream agree that under import substitution, efficiency failed in the short run because imports were only produced and sold locally if tariff protection was undertaken. Such policies provided opportunities for corruption and usually led to outcomes with governments unwilling to withdraw subsidies from firms enjoying unproductive monopolies. It is rarely acknowledged that import substitution increased output, saved foreign exchange and was demand-driven: "if something was imported, obviously locals were willing to pay for it, so the demand was there" (Amsden 2007, 12). It also provided opportunities for locally-owned firms to learn and access technology while enjoying government protection. It even led to the development of backward and forward linkages as a result of protection within countries rather than an increase in reliance on inputs from other countries. However, despite the possibilities, governments often got such policies wrong either willfully or due to vested interests or their limited understanding of the dynamics of import substitution policies.

Even in today's development policymaking climate where industrial policy is slowly becoming 'fashionable', policies of the export-oriented variety have been favoured, with import substitution largely being perceived as old-fashioned. The World Bank continues to push such export-orientation today, with its reasoning following Say's Law where it is assumed that supply will create its own demand (Ocampo and Taylor 1998). There is a false distinction between export orientation and import substitution though such a distinction has usually (Krueger 1985) been applied within the literature. Most successful 'winners' in manufacturing sector exports have developed through synergistic policies of protectionism and outward orientation, often occurring simultaneously. Through such policies, governments not only offer protection to their infant industries but also help them compete in export markets and gradually acquire technology through such engagement.[6]

The case for import substitution lost further significance with the increasing power of the World Trade Organization (WTO) and the associated limitations on policy space in developing countries. The WTO's demands on developing countries have reduced the capacity of developing countries to experiment with industrial policies in the way they did in the post-war years. Though some (Wade 2003) argue that this has made the task of accessing policy space almost impossible, others (Amsden and Hikino 2000; Weiss 2005) have long argued that there is still space for developing countries to innovate with industrial policies despite the large demands placed on them. Still, others (Shadlen 2005) argue that the WTO's influence is exaggerated and regional or bilateral trade agreements have a much larger impact in

[6] Zhou (2008) examines how the Chinese government used such synergistic policies to support local high-tech companies.

reducing policy space. The WTO has restricted industrial policy measures available to developing countries. However, there are still many policies available. Tariffs can be increased (although there are ceilings, which are 'bound'), and it is still possible to impose import surcharges in emergency cases. Export subsidies are still used and though technology absorption is more expensive because of trade-related intellectual property rights (TRIPS), the technologies that most African countries need are too old to have patents (Chang 2013). However, WTO restrictions are rarely the main reason for the restriction of policy space in developing countries. They must also deal with conditionalities related to bilateral and regional trade and investment agreements, which can often be more restrictive (Thrasher and Gallagher 2008). Also, foreign donors (especially American and EU governments) and international financial institutions (World Bank and IMF) exert considerable pressure on the policy space for developing countries to use industrial policy instruments (Shadlen 2005).

The commodity studies literature, including literature on Global Value Chains (GVC), Global Production Networks (GPN) and Global Commodity Chains (GCC) ignores discussions of import substitution. Since commodity studies is largely engaged with how domestic production networks are increasingly engaged in global commercial circuits of trade, it does not emphasize the importance of securing the home market. Such an orientation within the literature is natural given its methodological considerations.as well as the dominance of such logic in development policymaking. However, such arguments operate firmly against heterodox structuralist developmental state literature, which acknowledges the positive productive forces associated with import substitution. The commodity studies literature has done very little to advance an adequate theory of facilitating the state's role in upgrading within value-chains and implementing industrial policies in alliance with firms (Cramer 1999, Bernstein and Campling 2006). There have been recent attempts (Smith 2015) at filling this gap but more emphasis needs to be placed on how the politics of relationships between governments and businesses can support technology acquisition and firm upgrading in developing countries.

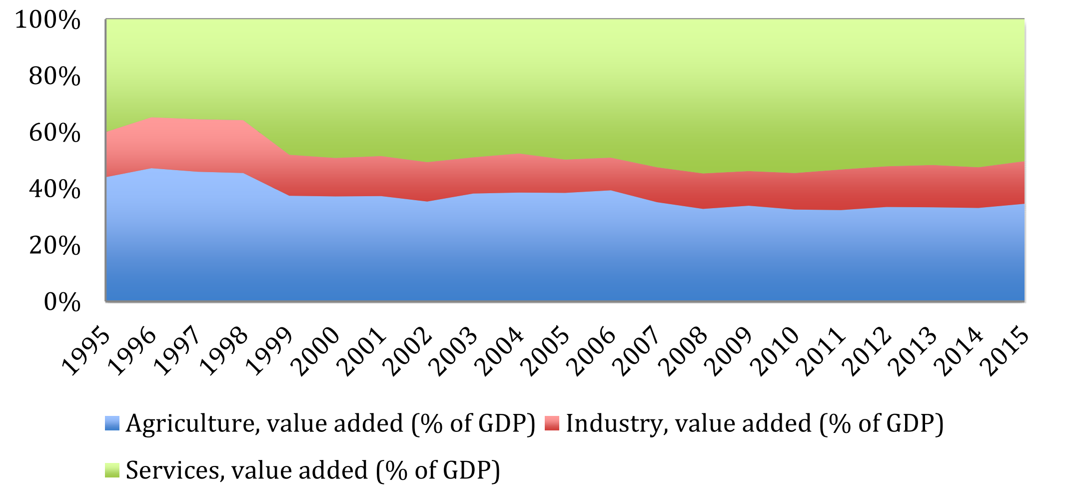
Despite the marginalization of discussions of import substitution, it is beginning to reappear in some contexts. In Rwanda, import substitution has reappeared in the form of a *Domestic Market Recapturing Strategy* (DMRS) – a name that government officials and donors alike admit is not used simply to avoid using the term – ‘import substitution’.[7] There are at least four broad categories of constraints facing industrial policy. The first are those policies, which are not legally allowed as part of bilateral, regional or multilateral trade agreements. The second are those constraints that pertain to the lack of state capacity in developing countries. The third are to do with constraints existing because of the infeasibility of certain policy measures given the changes in the global economy. Lastly, the fourth are to do with domestic political constraints to enacting industrial policies and supporting the acquisition of technological capabilities in developing countries. The following section examines the context in which the Rwandan government began to reintroduce import substitution after two decades of trade liberalization and the marginalization of the domestic manufacturing sector.

Domestic Market Recapturing in Rwanda

Since the 1994 genocide, the victorious Rwandan Patriotic Front (RPF) government has led the country through a remarkable recovery. It has experienced a period of ‘miracle growth’, with annual GDP growth marked at below six per cent in only two years since 1994 (Behuria and Goodfellow 2015). Figure 1 demonstrates that though agriculture has reduced as a share of GDP, the services sector has grown most significantly in recent years. In comparison, there has been very little manufacturing sector growth. Such a development trajectory is distinct from East Asian developmental states. In fact, at 20.4USD, real manufacturing output per capita in 2011 was only about half what it was in the late 1980s and it was projected that “Rwanda would only achieve its pre-genocide maximum of 41USD per capita around 2025” (Gathani and Stoelinga 2013, 1). The contribution of manufacturing in the economy has contracted since the 2000s. In 2002, the share of manufacturing in GDP 2014 was seven per cent. By 2014, it had dropped to 4.8 per cent (UNECA 2016). Figure 2 demonstrates that Rwanda’s manufacturing sector represents a lower share of GDP than in other East African countries.

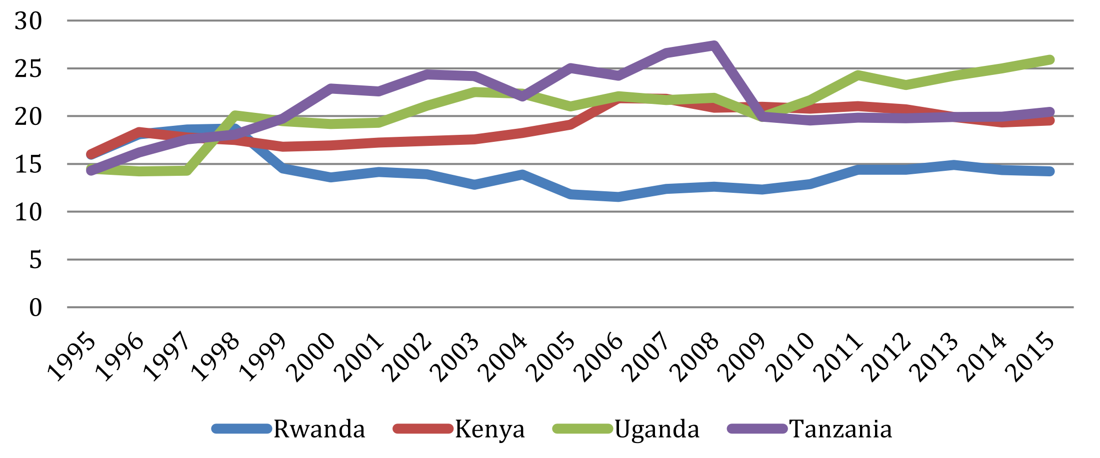
[7] Interviews, Ministry of Trade and Industry (MINICOM) officials and donors, August 2016.

Figure 1: Composition of GDP in Rwanda: 1995-2015



Source: World Bank

Figure 2: Comparison of East African Countries (Manufacturing, Value Added % of GDP): 1995-2015

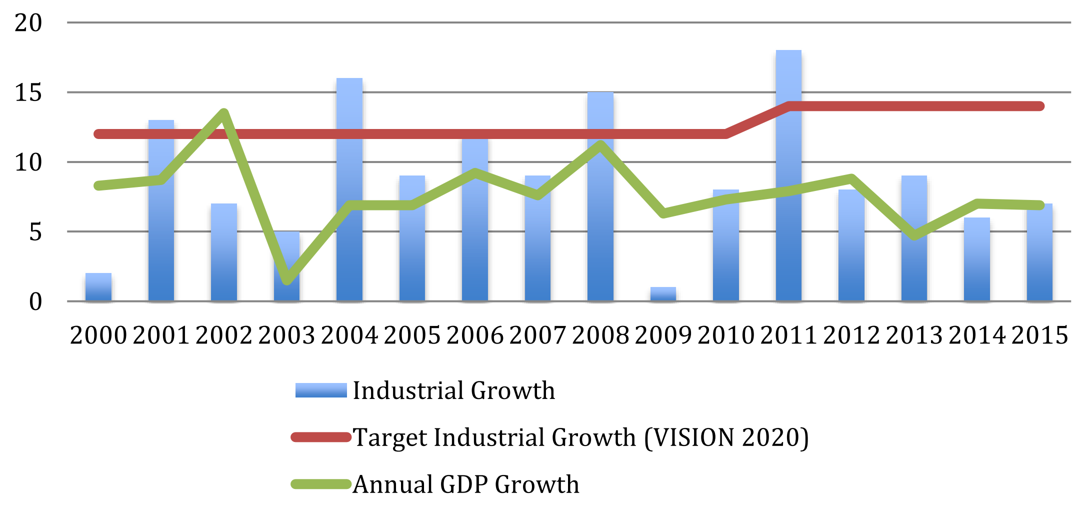


Source: World Bank

Figure 3 indicates that manufacturing sector growth in Rwanda targets have not been achieved in most years. Targets were initially set at 12 per cent annual industrial growth per year in the Rwandan development strategy – VISION 2020 (GoR 2000). However, beginning in 2011, this was later revised to 14 per cent annual growth per year. In 2012, the Rwandan government revised its national development strategy to refocus on manufacturing sector growth. In doing so, it went from purely targeting the creation of a ‘knowledge-based economy’ to targeting a ‘manufacturing and knowledge-based economy’ by 2020 (MINECOFIN 2013). One motive for the revision was a concern about the lack of employment opportunities in the country. Though officially, unemployment was estimated to be at only two per cent in 2001, there was severe underemployment. One World Bank study argued that underemployment was 36 per cent (with 36 per cent of workers working less than 35 hours per week but wanting to work more).

The same study estimated that the working age population will grow at 220,000 every year. In 2012, the government set a target of creating 200,000 jobs per year. Between 2006 and 2011, the government had not met the country's employment demand, creating only 126,000 jobs on average every year between 2006 and 2011. In 2011, around 70 per cent of the working-age population was still employed in agriculture. Employment remained characterized by agriculture, informality and low earnings. The industrial sector has been a source for job creation between 20001 and 2014, creating 350,000 jobs. However, out of the existing 412,000 jobs in the industrial sector, 57 per cent were employed in construction.

Figure 3: Comparison between Industrial Growth, Targets and Annual GDP Growth: 2000-2015



Source: Ministry of Trade and Industry (MINICOM)

Figure 4 highlights the composition of industrial sector growth over the last 15 years. Construction and agro-processing comprise the most significant shares of the industrial sector. Only one manufacturing sub-sector has experienced significant growth – beverages and tobacco. All others have contracted (UNECA 2016).[8] The mining sector is categorized as part of the sector although its share is quite small. Rwanda's exports are still largely dependent on primary commodities (coffee, tea,

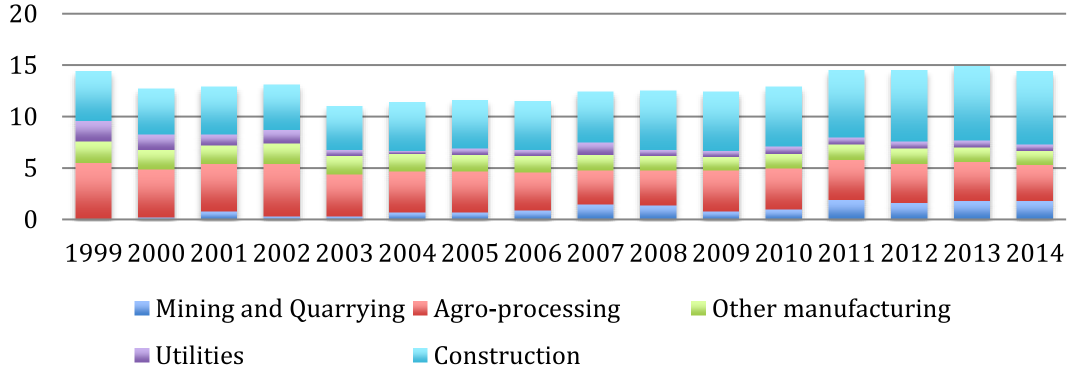
[8] This refers specifically to manufacturing sub-sectors and does not refer to construction, mining, agro-processing or other sectors within industry.

tantalum, tungsten, wolfram and pyrethrum). Since 1994, there has been some progress in terms of export diversification. In 2007, it was argued that Rwanda has achieved many small-scale new discoveries but with limited scale achieved in terms of those discoveries (Chandra et al. 2007). There had been significant diversification within primary commodities. In the 1980s, coffee comprised close to 70 per cent of exports in Rwanda in some years. However, minerals exports have surged in recent years. There has also been significant value-addition in coffee and tea sector, with high-quality coffee and tea now sold as packaged coffee to foreign markets. Collectively, traditional primary commodities (coffee, tea, minerals and pyrethrum) comprised around 40 per cent of exports in 2015. Manufacturing exports have increased more than tenfold between 2001 and 2014. Agro-processing and beverages are the most prominent manufacturing sector exports, with agro-processing recognized to be the most promising sector for the diversification of exports.[9] Bralirwa (Heineken's subsidiary in Rwanda) is the largest firm engaging in manufacturing exports, as of 2010. Others included Bakhresa Grain Milling and Pembe flour mills, with all firms exporting to neighbouring countries (Gathani and Stoelinga 2012). New firms entering the sector have also begun to export new nontraditional exports to neighbouring countries such as the Democratic Republic of Congo and Burundi (Zangrandi and Mogollon 2015). Opportunities to access those markets, despite a lack of reliability with regards to such access, have enticed several new investors to Rwanda.[10] However, Rwandan-based firms compete with other regional firms (including Ugandan firms) to access markets. Thus, there is a contradictory requirement of abiding by EAC rules while also developing strong relationships with locally-based firms to challenge regional competition. By embracing regional trade agreements, developing countries obtain opportunities to access large markets but “sacrifice the rights to use the array of industrial policies that countries have traditionally used to generate new productive capacity in new sectors” (Shadlen 2005, 769). In the Rwandan case, the government must access new markets while agreeing to abide by common rules and also finding ways to acquire technological capabilities in its local firms at a faster pace than its regional competitors. The task is a difficult one. It is only possible through an interventionist

[9] Interview, MINICOM, August 2016.
[10] Interviews, foreign investors, August 2016.

government, which prioritizes learning and experimentation and understands the importance of building and sustaining reciprocal control mechanisms with local capitalist partners.

Figure 4: Composition of Industrial Sector in Rwanda: 1999-2015



Source: Ministry of Finance and Economic Planning (MINECOFIN)

There were reasons why the Rwandan government did not prioritize manufacturing sector growth and preferred a more service-oriented development strategy. Government officials argued that high transport costs, the lack of availability of local raw materials, inadequate and inconsistent supplies of energy and lack of skills and local training impeded manufacturing sector growth.[11] The government estimated that "Rwanda's transport costs represent as high as 40 per cent of export and import values", which made the promotion of local industry expensive (MINICOM 2010, 12). In 2011, the import cost per container to Rwanda totaled $4,990, compared to $3,725 for a container for export and rated in the bottom 10 per cent of nations globally (MINICOM 2011). Rwanda's position as a land-locked country, with access to a very small market, meant that it was unlikely that the government would be able to nurture firms as regional or global champions. Instead, President Paul Kagame chose to become a leading advocate of regional integration.

In 2007, Rwanda became a full member of the EAC. In 2009, Rwanda joined the EAC Customs Union with Kenya, Uganda, Tanzania and Burundi. Since July 2009, Rwanda has applied the EAC Common External Tariff (CET). The CET uses a

[11] Interviews, MINICOM and MINECOFIN officials, January 2015 and August 2016.

three-tier 0-10-25 structure, with tariff rates for imports sourced outside the EAC at 25 per cent for finished goods, 10 per cent for intermediate goods and 0 per cent for raw materials and capital goods. There are no internal tariffs within the EAC except for sensitive items.[12] During this phase, Rwanda committed to a trade policy that left its national firms open to regional competition in exchange for larger markets.

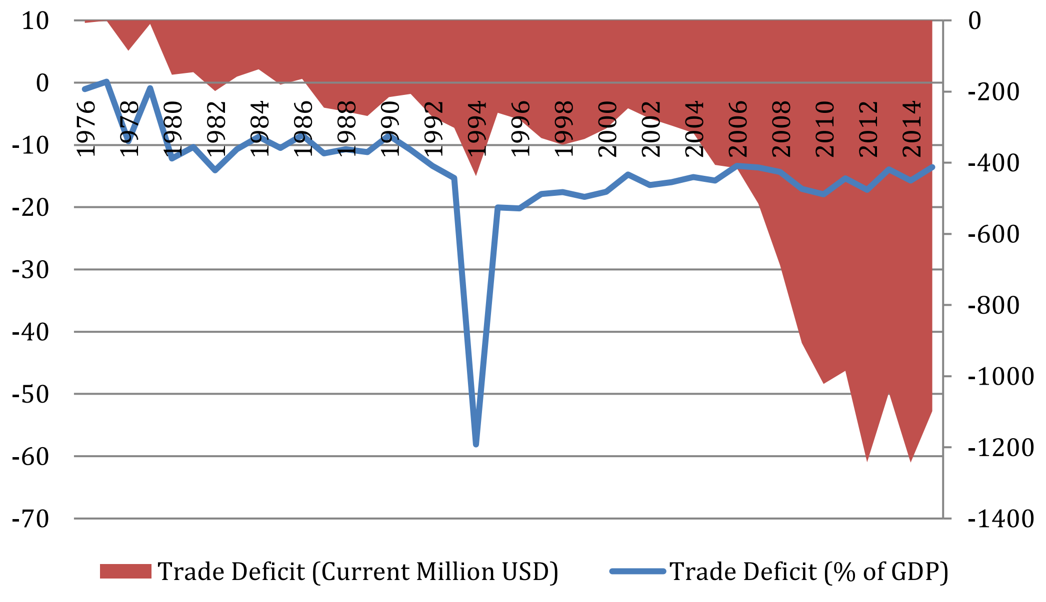
By 2010, the EAC's Customs Union was established. Prior to joining the customs union, in 2007, Rwanda enjoyed a positive trade balance with only one other EAC member, Burundi. In the same year, Rwanda's imports from EAC members were four times its exports to the same countries. There were dangers to East African integration. History had shown that Kenya profited from the East African Common Market in the 1970s and expanded its industries, with Uganda and Tanzania complaining that their countries had subsidized Kenyan growth (Mugomba 1978). These factors and other political tensions led to the breakdown of the EAC in its earlier incarnation (Ravenhill 1979). Though domestic firms in Rwanda find it difficult to compete against regional competitors without protection, the government is convinced of the long-term benefits of East African integration and accessing larger markets ahead of insular protectionism of the small, domestic market. In 2014, Rwanda received 26.3 per cent of its total imports from within the EAC, which was marginally less than the proportion of imports it received from the region prior to joining the EAC in 2008. However, in dollar amounts, imports from the region increased by 1.5 times within the same period. Exports to the region increased manifold, with official statistics highlighting an increase from 15 million USD in 2008 to around 320 million USD in 2014. When analyzing these statistics, it must be kept in mind that new figures included the exports of minerals through Tanzania, as well as the export of coffee and tea through Kenya. Neither Kenya nor Tanzania was the final destination of these goods.[13]

Figure 5 illustrates the evolution of trade deficit in Rwanda. Hirschman (1968) argued that there were four 'motive' forces behind Import Substitution Industrialization (ISI) – wars, balance-of-payments difficulties, growth of the

[12] In 2012, Rwanda applied additional tariffs on 12 sensitive items: maize and milk products, wheat flower, maize, maize flour, rice, cigarettes, matches, woven fabrics, bed linen, sacks and bags, crown corks, and primary cells and batteries.
[13] In 2014, 86.5 per cent of exports from Rwanda and Tanzania were in the form of minerals. 71.1 per cent of exports from Rwanda to Kenya were in the form of coffee and tea. These goods were eventually exported elsewhere.

domestic market (as a result of export growth) and official development policy. In Rwanda's case, only war has not been a salient motive recently. In fact, given that Rwanda is often accused of supporting rebel groups in the Democratic Republic of Congo (DRC), it could be argued that an absence of war has actually accompanied the motives for ISI. Also, though the domestic market has grown, this is still not enough to entice domestic or local investors to make bets on domestic manufacturing without government incentives or orders. Instead, access to the regional markets and markets in the DRC were motives for ISI. However, the most significant motive is with regard to balance-of-payment difficulties.

Figure 5: Evolution of Trade Deficit in Rwanda: 1976-2015



Source: World Bank

Though the trade deficit has remained relatively steady, between 10 to 16 per cent of GDP, imports have increased substantially over that time. The Rwandan government has stated its intention to diversify its exports since 1994 unlike the previous government, which retained a preference for prioritizing coffee exports as part of a nation-building project (Verwimp 2003). However, when aid was temporarily withdrawn in 2012 after allegations that the Rwandan government was supporting rebel groups in the DRC, a significant shift took place within Rwanda. It became clear that "aid could no longer be relied on."[14] More importantly, donors moved towards permanently ending the budget support that the government received

[14] Interview, MINICOM official, January 2015.

before 2012 and shifting to more project aid.[15] Commodity prices also dropped substantially. This was particularly true for minerals with a leading minerals exporter claiming that "in 2013, he alone contributed to 20 per cent of GDP but it all changed when the prices of minerals crashed."[16] In 2014 and 2015, export receipts from minerals reduced by more than 40 per cent in comparison with 2013. Since then, the government has been particularly worried about its access to foreign exchange. This came to a head in June 2016 when the International Monetary Fund (IMF) approved an 18-month Stand-by Credit Facility, worth 204 million USD, to support Rwanda's foreign exchange reserves. In return, the Rwandan government committed to higher exchange rate flexibility, reducing imports and restraining fiscal policies (IMF 2016).

In 2015, the government published its Domestic Market Recapturing Strategy (DMRS), which complements existing strategies including The National Industrial Strategy, National Export Strategy and Special Economic Zone Policy, in providing a platform for reinvigorating Rwanda's domestic manufacturing sector. Several MINICOM officials argued that 2015 was a significant year for refocusing efforts on the manufacturing sector, with the President acknowledging the weak performance of the sector.[17] The objective of the DMRS is to increase domestic production for local consumption while contributing to structural transformation of the productive sector and increasing international competitiveness (MINICOM 2015). The DMRS highlights three priority sectors: construction materials, light manufacturing and agro-processing. These three priority sectors include 21 specific sectors, with selection based on potential contribution to import reduction, the existence of planned projects in the sector, the size of the domestic market and export potential to neighbouring countries, availability of raw material and whether projects had strong linkages to other domestic sectors. There was a preference for sectors, which were labour and capital-intensive rather than those that were land or skills-intensive. Cement, textiles and garments were highlighted as high-priority sectors for the DMRS, with a large potential for recapturing the domestic market.

To support the DMRS, the government has launched a 'Made in Rwanda' campaign to "change the mindset" of the local population to consume locally and trust

[15] Interviews, donors and government officials, August 2016.
[16] Interview, Foreign owner of mining company, August 2016.
[17] Interviews, MINICOM officials, August 2016.

in the better quality of locally-produced goods.[18] As part of the strategy, the government has also committed to supporting local companies through its own procurement contracts, as well as holding fairs and investing in publicity campaigns for locally produced goods. The government has also established an Export Growth Facility (EGF), worth more than one billion Rwandan Francs. The EGF allows exporters to access funds at 8 per cent interest per annum up to 50 per cent of the costs exporters incur when seeking new markets abroad.

Several new investors have entered the manufacturing sector in recent years. To support the industrial sector, the government began a Special Economic Zone (SEZs) programme in 2006. From the outset, there was recognition that SEZs were not a "panacea" (MINICOM 2010b), with the government cognizant of the mixed experiences with SEZs around the world (Farole 2011, Stein 2012). Such zones are usually created to address infrastructural deficiencies, procedural complexities and barriers raised by monetary, trade, fiscal, taxation, tariff and labour policies (Aggarwal 2006). Rwanda's use of SEZs has not developed as per initial planning. Initially, there were plans to develop two separate zones: a Kigali Free Trade Zone and an Industrial Park. However, these projects have now merged. The SEZ now has two phases. The first phase was fully operationalized in 2014. All 61 plots are currently booked, with some existing companies relocated from the former Gikondo Industrial Park. The government is currently pressuring remaining factories in Gikondo to move to the SEZ.[19] The second phase has also nearly been completed, with the government reporting that more than 80 per cent of plots were booked.[20] Most investments are in line with strategic DMRS targets. However, there have also been big bets. Positivo BGH – a joint venture between Argentinian and Brazilian investors – has invested in a computer components assembling factory in Kigali. Such investments aim to complement Rwanda's One Laptop per Child programme. The plant currently has the capacity to produce 60,000 computers per month although it has only produced around 100,000 computers, as of May 2015. The government has a deal in place to buy 150,000 computers from Positivo every year. However, there have been some initial complaints with students arguing that the software on the

[18] Interview, MINICOM official, August 2016.
[19] Interviews, domestic and foreign firms, August 2016.
[20] Interview, Special Economic Zones Regulatory Authority of Rwanda (SEZAR), August 2016.

computers is not appropriate for their needs (Kanamugire and Afadhali 2016). For such large gambles to amount to anything, the government must retain disciplinary control and provide reciprocal benefits to investors to ensure they reinvest to adapt their products in line with the needs of domestic and regional markets.

This is the context in which import substitution has assumed centre stage in Rwandan development policy. Since ISI was marginalized in mainstream development policymaking, the Rwandan government chose to avoid going against donor advice. The following sections demonstrate the restricted policy environment in which ISI strategies operate and the increased extent of state intervention that is required if aims to recapture the domestic market are to be realized. In both sectors, the government must rely on foreign investors for action while also retaining ‘zero tariffs’ for competitors from within the EAC. Developmental patrimonialism arguments (Booth and Golooba-Mutebi 2012, Kelsall 2013) with regard to Rwanda would assume that party- and military-owned actors would be used as leading firms in these sectors. However, this paper supports previous work (Behuria 2015, 2016) that shows that contestation among elites has reduced the space in which such enterprises operate and inevitably, this results in increased reliance on foreign actors. Though this may be because local capitalists lack technological capabilities in the sector, it is also because many domestic capitalists are either in exile or are no longer trusted by the RPF. Further, two decades of liberalization have made it increasingly difficult to incentivize local investors to take risks in sectors where importers have dominated market share.

Made in Rwanda or China Makes in Rwanda? Recapturing the Apparels Sector

Apparel production has historically been a springboard for structural transformation. It is a typical starter industry for countries engaging in export-oriented industrialization because of its low fixed costs and associated labour-intensive manufacturing (Gereffi 1999). China has dominated global apparel exports in recent years, doubling its market share from 15.2 per cent to 33.2 per cent between 1995 and 2008 (Gereffi and Frederick 2010). Building a national champion in the sector that can compete with Chinese companies is a non-starter. In particular, securing the home market has several benefits aside from reducing the trade deficit. Amsden (2013) argued that such policies allow firms to reach scale economies, build a supplier network, learn to raise productivity and profit from natural protection because of tastes, transport costs, import duties, local supplier loyalties and government procurement practices. However, in Rwanda, the lead firms used in securing the home market in the two sectors of this study are foreign-owned. Thus, the challenge of building reciprocal control mechanisms with such firms and ensuring technological acquisition among local firms becomes even more difficult.

The textiles and garments sectors have never been strong contributors to growth through Rwandan history. Stephen Haggblade (1989) conducted a study of the Rwandan textiles sector in the 1980s. He found that there were four distinct ways in which clothing was supplied to Rwandan consumers. The first was through different kinds of retail shops, which imported clothing from abroad. The second included five medium-scale companies, employing between 10 to 100 people, which produced clothes for the domestic market. The third included firms, which distributed imported cloth to local consumers who then approached tailors to produce garments. The fourth included firms who imported second-hand clothing from Europe and the United States. Channels 3 and 4 held the majority share of the market.

The Struggle to Build Reciprocal Control Mechanisms: UTEXRWA in Rwanda

Until 1984, all textiles were imported in Rwanda although some cotton was produced domestically for some years in the 1970s and 1980s. In 1984, Kishor Jobanputra, who initially worked as a trader in Rwanda, established a small-scale firm, which initially focused on weaving and spinning but later became Rwanda's first vertically integrated textile company – *L'Usine Textile du Rwanda* (UTEXRWA). In 1985, UTEXRWA began printing and dyeing imported raw cloth. Soon after that, UTEXRWA began to dominate the second cluster in the textiles and garments sector, identified by Haggblade (1989). UTEXRWA quickly became a 'winner' for the Rwandan government (under President Juvenal Habyarimana) and profited from supplying a large share of the cloth and fabrics produced domestically. UTEXRWA also profited from contracts to supply uniforms for industry wear, schools, military and hospitals. It also developed contracts to supply garments on order to the DRC and enjoyed duty exempt status on its exports. These privileged contracts with customers in the DRC were a source of significant profits for

UTEXRWA. In 1993, UTEXRWA received 20 million dollars in revenues. However, the contract with Congolese customers was ended in 1994.[21]

After 1994, UTEXRWA officials described their experience “as a struggle” since “there was no buying power locally.”[22] During the genocide, UTEXRWA lost its trained workers. Parts of the factory were destroyed and raw materials warehouses were burned (Mukaaya 2007). In 1999, UTEXRWA received revenues worth 5.5 million dollars but was suffering losses of over two million dollars. At the time, Jobanputra considered shutting the factory down. However, in 2000, UTEXRWA began working with the government and consultancy company – On The Frontier (OTF) – to diversify into the production of silk products. Gradually, the company recovered after receiving contracts to supply uniforms to the military, the police and some local industries. It also began to export products to North America during this time. In 2005, it targeted new customers and produced antibacterial medical fabrics and also supplied uniforms to hotels, schools, colleges and laboratories.

In the late 2000s, UTEXRWA continued to face problems. It lost its contract to supply the military with uniforms since the military chose the cheaper option of importing uniforms from China. In February 2011, more than 500 UTEXRWA workers began industrial action, going on strike in protest of the unfair dismissal of 33 workers, low wages, denial of annual leave and poor working conditions. After a six-day strike, The Ministry of Public Service and Labour (MIFOTRA) ensured the reinstatement of 33 UTEXRWA workers (Ndoli 2011). Such difficulties meant that UTEXRWA was unable to re-establish itself in the domestic market. It also did not enjoy the privileged status it enjoyed in the late 1980s. Currently, UTEXRWA employs around 600 workers. Until recently, the company only focused on producing uniforms but because of opportunities associated with the DMRS, it has begun production of clothing for the local market.

In the 2000s, UTEXRWA worked with the government to begin silk production in Rwanda. Silk was perceived to be a priority export since there was potential for locally sourcing silk inputs and Rwanda enjoyed a suitable climate for mulberry cultivation. Since inputs (cotton, polyester, accessories, dyes and chemicals) for traditionally produced Rwandan textiles were not locally sourced and there was a

[21] Interview, UTEXRWA, August 2016
[22] Interview, UTEXRWA, August 2016

growing market for such products in the United States and Europe, silk could contribute to reducing the trade deficit. UTEXRWA officials claim they invested more than a million dollars in machinery. The government was hopeful, initially characterizing UTEXRWA as an "anchor firm" in the silk value-chain, with a "remarkably modernized facility as a production entity" (MINICOM 2009, 78). At the time, UTEXRWA employed 650 workers and boasted processing functions from spinning, weaving, printing to garment-making. It also had over 5,000 spinning spindles and a capacity of one million kg of yarn per annum. By 2009, it had launched its production line for silk products and established the brand name – Silk Hills – to sell products. UTEXRWA was also looking at developing other backward linkages, beginning research on producing natural fiber textiles (from banana and pineapple). By 2011, UTEXRWA had only received four tons of cocoons over three years. Since the company needed 7.5 tons of cocoons per month to sustain production capacity, UTEXRWA officials argued that they stopped investments.[23] As of 2016, the government had made progress in organizing farmers into 40 cooperatives and establishing sericulture centres in four provinces. However, raw materials were still insufficient to run a factory. In 2016, UTEXRWA's silk production was not in operation and it had rented out its warehouses to private businesses. Though capacity utilization in the factory has not been more than 40 per cent since independence, this has dropped to 20 per cent in 2016.

UTEXRWA officials complained that instead of supporting its investments, the Ministry of Defence started a rival company "when they were supposed to be our partners. The government should have supported us but they became a competitor."[24] The military was briefly involved in the sector through its company, Agro-Processing Industries (API).[25] However, it has now exited the sector. Instead, the government has recently begun speaking to new investors including receiving an initial commitment from Korean investors – HeWorks Rwanda Silk Ltd. – to invest over five million dollars in the silk sector, with an agreement to buy all silk cocoons produced in the country and processing them into finished products.

[23] Interview, UTEXRWA, January 2015.
[24] Interview, UTEXRWA, August 2016.
[25] Agro-Processing Industries has now been renamed Agro Processing Trust Corporation Ltd. (APTC). The Ministry of Defence still has full ownership of the company. APTC has three subsidiaries: Agro-Processing Industries Ltd., Rugari Meat Processing and Nyanza Milk Industries.

New Entrants: Opportunities and Challenges

In 2014, Chinese investors – C&H Garments – signed a Memorandum of Understanding with the Rwandan government, agreeing to invest six million dollars to begin garment production in Rwanda. Helen Hai and Candy Ma, the owners of C&H Garments, had already established factories in Ethiopia, Lesotho and Kenya. Managers said they invested in the Rwandan market because of the country's leadership and the incentives that were on offer. C&H was one of the very companies in Rwanda to be given Export Processing Zone (EPZ) status since it committed to export 80 per cent of its products. Seventy per cent of C&H production is currently uniforms, which it exports to China and the United States. It has also begun exporting garments for the European and American markets, with some products also exported through the African Growth and Opportunity Act (AGOA). Trials are underway for producing embroidered table cloths for foreign markets. It received several incentives including tax exemptions, duty exemptions on imports. The government also invested in constructing the company's factory in the SEZ. The government, through funding from the African Development Bank (AfDB), has funded a large share of the training for workers to be employed in C&H's factories. In September 2016, 400 workers had already finished training while a further 500 were being trained. C&H's planned expansion from 900 employees in 2016 to 3,000 employees by 2018 will depend on expansion of its factory and the completion of Phase 2 of Kigali's SEZ. C&H managers said they were still worried about the high transport costs and the lack of availability of inputs. However, they were positive about the growth of their factory and said they had plans to invest in a textile factory by 2018.[26] MINICOM officials considered C&H investments to be "worth the incentives" and they hoped that this would be a "demonstration to attract other Chinese investors as they relocate their manufacturing to Africa."[27]

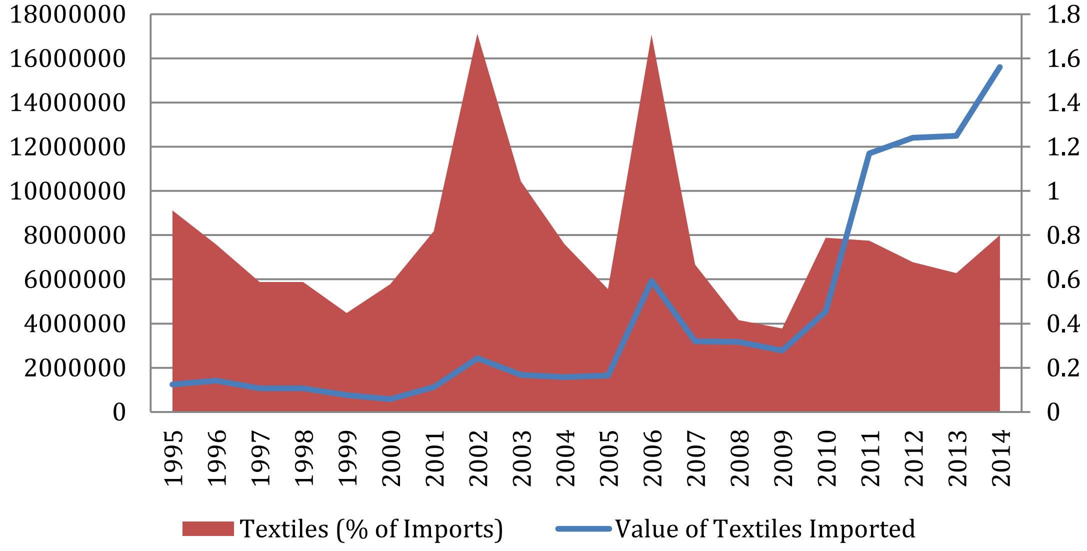
The government has also supported the establishment of Kigali Garments Centre (KGC) – a company with over 400 shareholders. KGC will begin by training over 1200 workers at a new plant this year. This effort is a way to formalize Channel 3, which includes a share of how garments are channeled through Rwanda. Recently, Albert Supplies Ltd. has also invested in the sector. There is disagreement about the

[26] Interview, C&H Garments, August 2016.
[27] Interviews, MINICOM, August 2016.

origin of the company, with some arguing that the company is Guangzhou-based (Gahigi 2016) and the government claiming that it is a local company. Albert Nsengiyumva, the director of the company, has committed to investing over 12 million dollars and beginning production next year. These investments are part of the establishment of the Apparel Manufacturing Zone (AMZ), with Burundian-based Rwantan also agreeing to a deal to set up a shoe factory in the zone (Kuteesa 2016). Other leather factories already operate in Rwanda including a Kate Spade 'On Purpose' project, which employs 173 employees to produce leather bags. Every quarter, the company has been exporting 6000 bags through AGOA from Rwanda. AGOA presents a substantial opportunity to new investors in the sector, with existing textile companies claiming to be unaware of its existence and potential in recent years (MINICOM 2016) although UTEXRWA had been exporting through AGOA in the 2000s. Rwanda only received 1.76 million dollars through AGOA exports between 2011 and 2013.

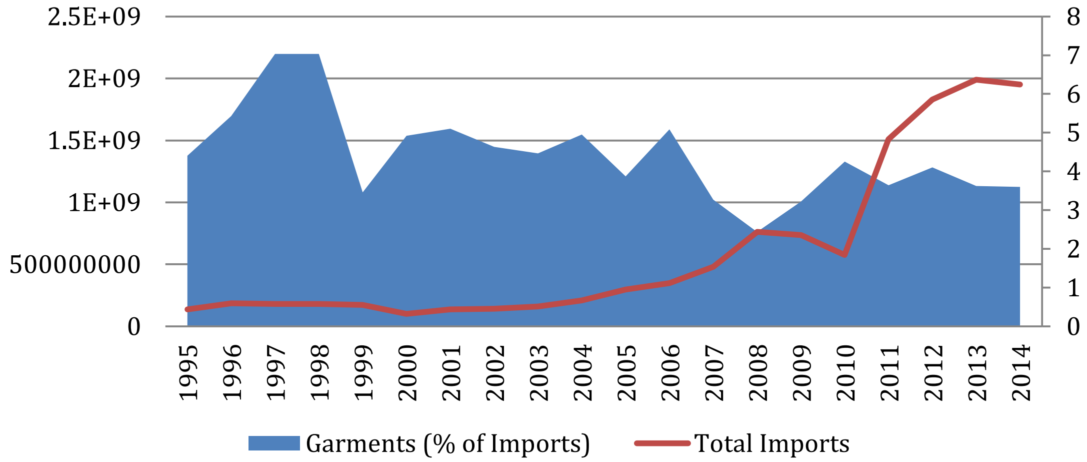
A significant factor, which has bolstered new investments in the apparels sector, has been the increase of duties on second-hand clothing imported in Rwanda. In an EAC Heads of State meeting held in early 2016, East African leaders held discussions about banning the import of second hand clothing and shoes (Brooks 2016). Though this plan may only eventually be rolled out in 2019 if the EAC can agree to a common industrialization policy, some countries including Rwanda began to impose increased duties on second-hand clothes and shoes. Rwanda has already spent more than 15 million dollars on importing second-hold clothes. Figures 6 and 7 demonstrate the evolution of the value of textile imports over time. Though the share of textiles and garments as a share of GDP has varied, the value of imported textiles has increased significantly since 2009.

Figure 6: Evolution of Value of Textile Imports: 1995-2014



Source: MINICOM

Figure 7: Evolution of value of garments imports: 1995-2014



Source: MINICOM

In June 2016, to support the DMRS, the Rwandan government increased duties on the import of used clothes from $0.2/kg to $2.5/kg. Duties were also imposed on used shoes from $0.5/kg to $5/kg. Though there is no doubt that such policies have acted as a filip to new investments in the apparels sector, it is likely that prices will increase in the short-term and local newspapers are already warning of such outcomes (Mugabo 2016, Esiara 2016) The government also worries that cartels, which import second-hand clothes and operate in the sector, will find ways to by-pass the rule.[28] MINICOM estimates that reforms will not only help recapture the domestic market (with a 37 per cent decline in imports of apparels) but will also contribute to increasing apparel exports by 17 million dollars.[29]

The transformation of the apparels sector in Rwanda has demonstrated several characteristics about the nature of the challenge of import substitution in the 21st century. Firstly, import substitution has only occurred through active state intervention. This has taken the form of the government seeking investors and providing tax incentives, imposing increased duties to encourage import substitution and developing several policies to guide industrialization. Second, the government has had to negotiate the dual challenge of protecting its domestic market while seeking to abide by EAC rules and accessing large markets. Third, the government has had to find ways to build reciprocal control mechanisms with capitalist partners. However, there is very little evidence to demonstrate that such relationships will be sustained if exemptions are withdrawn. Additionally, the government exhibited a lack of trust in UTEXRWA who government officials argue "was more concerned with businesses in Uganda" and "was not serious about doing anything" in Rwanda.[30] The reasons may be political as foreign investors claim that "the government has no interest in supporting foreigners unless there is no other option" and because UTEXRWA was closely associated with the Habyarimana regime.[31] There are serious concerns in the sector with few local partners in place to acquire technological capabilities as the country attempts to sustain industrialization going forward.

Tentative Recapturing: The Revitalisation of CIMERWA amidst trade liberalization

Amsden (1989) compared the differences between industrial policies in light and heavy industries in Korea. Similar to this study, she chose to focus on textiles as a light industry and cement-making as a heavy industry. She found that learning in the textiles industry did not spur further industrialization while two *chaebols*, including Hyundai, gained from the diffusion of managerial capabilities within their

[28] Interview, MINICOM, August 2016.
[29] Internal government report.
[30] Interviews, MINICOM, August 2016.
[31] Insert, business owner, August 2016.

conglomerates. Despite the central place cement production has occupied in the industrial histories of many late developers, it has been relatively marginal to African industrial histories. In 2011, Africa's share of global cement production was five percent and production was dominated by multinationals – LaFarge, Holcim, Heidelberg Cement and Italcemento (Oqubay 2015). In recent years, Nigeria's Aliko Dangote began Dangote cement, which has established a presence in several countries around the continent. Dangote's ventures in cement began as a cement importer. He then worked closely with Nigerian President Obasanjo and took advantage of the government's Backward Integration Policy (BIP) to become the leading domestic cement producer and contributed significantly to reducing the country's trade deficit (Akinyoade and Uche 2016). Despite the Rwandan government owning shares in the largest domestic cement production company, the presence of a foreign investor as a majority owner reduces the potential for creating a national champion. The nationality of the leading actor in the sector alters the dynamics of power and bargaining required to sustain reciprocal control mechanisms. This section demonstrates that it has been difficult to build reciprocal control mechanisms not only with the new foreign investor-led company but also when the company was owned by an informal investment group closely linked to the party – Rwanda Investment Group (RIG).

The History of Cement Production in Rwanda

In the 1970s, limestone, quartz and clay deposits were discovered at a hot spring in Bugarama in the Rusizi district. In July 1976, an agreement was struck between the Rwandan government and the Chinese government to establish a joint venture to construct a cement production plant. As part of the agreement, the Chinese government offered a 30-year 13 million dollar interest-free loan (Gathani and Stoelinga 2013). In 1984, the CIMERWA plant was commissioned. CBMC, a Chinese company, managed the plant under a "Build, own, operate and transfer" agreement. Initially, the plant had a capacity of 50,000 tons per year. Though production stopped during the war and genocide in the 1990s, the Chinese company returned after the genocide. In 2001, the plant was expanded and production capacity was increased to 100,000 tons per year. In 2006, the Chinese loan expired and the government chose to privatize the company. An informal investment group – RIG – took control of 90 per cent of CIMERWA. However, "RIG didn't really do much.

They said they would invest as per the privatization agreement but they failed."[32] RIG even made some investments to build a new plant. One of the reasons for the lack of activity was that a leading investor in RIG, Tribert Rujugiro, left Rwanda because of tax evasion and money laundering charges in the United Kingdom. He later fell out with the President Kagame. Later, his Rwandan properties and businesses were ceased (Behuria 2015).

CIMERWA remained "in a bad situation since the plant was old and maintenance costs were high."[33] In 2010, the AfDB approved a 130 million dollar loan to CIMERWA to construct a new plant (Gathani and Stoelinga 2013). However, CIMERWA struggled to find additional funding. In 2011, some state-owned institutions and local actors also reinvested in CIMERWA. Under the new ownership structure, the Rwanda Social Security Board (RSSB) held 37.5 per cent of shares, the government held 30.7 per cent of shares, the Rwanda Development Bank (BRD) held 8.5 per cent of shares, RIG held 21.2 per cent of shares, SONARWA (a local insurance firm) held 1.4 per cent of shares and the remaining shares were owned by two local businessmen (Paul Mubiligi and Eugene Nyagahene). In January 2013, South Africa's largest cement producer – PPC Ltd. – invested 69 million dollars to assume majority (51 per cent) control of CIMERWA. PPC was enticed to invest in Rwanda because of the "investment policies, business climate and tax rebates."[34] One of their most significant worries was the availability and price of power. The remaining shares were retained by RSSB (20.24 per cent), the government (16.55 per cent), RIG (11.45 per cent) and SONARWA (0.76 per cent). Since PPC assumed majority ownership, CIMERWA has invested 170 million dollars in a new modern dry process production plant with a capacity of 600,000 tons of cement per year.

In 1999, Kigali Cement Company (KCC) was established by a local investor, Jean Damascene Ndayambaje (Gathani and Sotelinga 2013). Unlike CIMERWA, which is a full manufacturing process plant in Rwanda and produces its own clinker, KCC imports clinker. Between 2007 and 2011, KCC imported clinker from Athi River Mining Ltd., which was the largest cement manufacturer in East Africa (Gathani and Stoelinga 2013). In 2011, ARM acquired 35 per cent of KCC and by

[32] Interview, CIMERWA employee, August 2016.
[33] Interview, CIMERWA employee, August 2016.
[34] Interview, CIMERWA employee, August 2016.

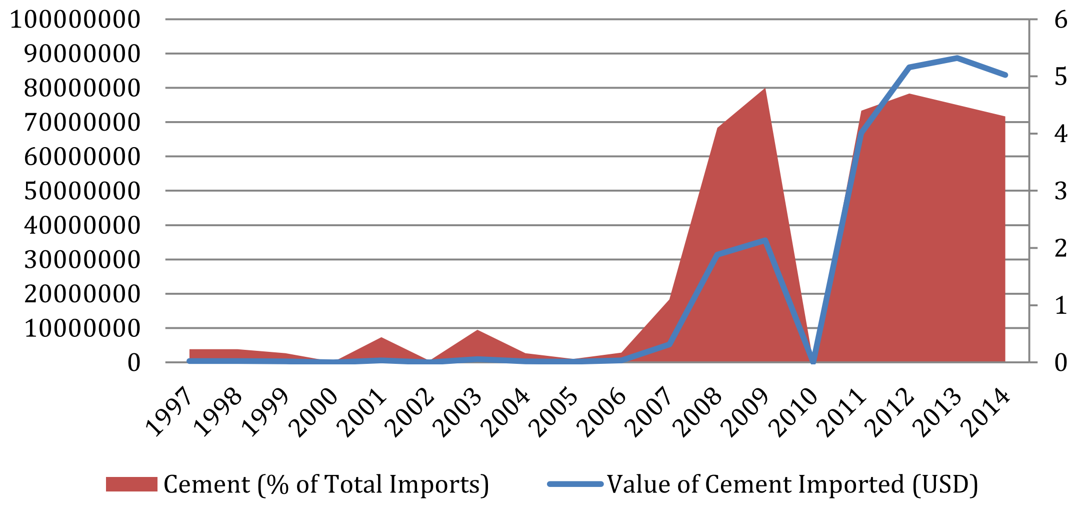
2014, ACC had full ownership of KCC. KCC was a relatively small company, producing about 100-120 tons per day.

Matching construction growth: State intervention versus trade liberalization and the power of importers

Figure 8 illustrates the rapid increase in cement imports, beginning in 2006. This was largely due to the "construction boom" that began in this period in the country, especially focused in and around Kigali (Goodfellow 2014). During this period, RIG's limited production was unable to keep up with the demands for cement. As a result, several new Ugandan, Tanzanian and Kenyan importers entered the country. Uganda's Tororo cement was a significant player in the late 2000s until it fell foul of the East African Gazette Law when it was discovered that the company was importing clinker from outside the EAC.[35] Since then, other importers including Uganda's Hima Cement and Tanzania's Simba Cement have begun to dominate the market. Smaller regional players like Bamburi, Savannah, Twiga and Nyati are also operating as importers. One cement dealer said, "when new cement dealers come in, they reduce the price. However, eventually, they also put their prices up."[36] Tanzania's Kilimanjaro Cement also gained a large market share in 2014. One cement dealer highlighted that "Kilimanjaro was really booming when they came in. They were aggressive and established many outlets."[37] However, in 2015, Rwanda delisted Kilimanjaro from preferential treatment after government officials alleged that Kilimanjaro was importing cement from Pakistan and repackaging it in local bags (Esiara 2015). Though import substitution in the cement sector is clearly inhibited by adhering to EAC trade agreements, the Rwandan government strategically uses the East African Gazette Law to ensure foreign importers are also abiding by the rules.

[35] Interview, cement importer, August 2016.
[36] Interview, local cement dealer, August 2016.
[37] Interview, local cement dealer, August 2016.

Figure 8: Evolution of value of Cement imports: 1997-2014



Source: MINICOM

Until 2015, CIMERWA and KCC's production fell short of domestic demands for cement. KCC was a comparatively small player and remains "happy with its small share of the market and established customers."[38] However, currently, total production capacity in Rwanda is 600,000 tons a year, which should outweigh domestic demand (which some estimate to be between 400,000-450,000 tons a year). CIMERWA and KCC should both reach full production capacity by 2018. CIMERWA has already previously exported small shares of its production to the DRC and Burundi. However, increasing production capacity was one part of the challenge of recapturing the domestic market. Initially, CIMERWA did not enjoy the logistical advantages enjoyed by importers. Comparatively, Hima and Simba had established markets and brands in the country. CIMERWA's cement was also comparatively more expensive than that of importers. For example, in 2015, a 50kg cement bag of CIMERWA cement was 2000Rwf more expensive than that of Hima cement. However, in 2016, the gap between CIMERWA's cement and imported cement had reduced. Rwandan-produced cement had much higher costs because of energy costs and transport costs (given that gypsum and fuel oil were still imported). Since Hima and Simba did not have to pay duties, the Rwandan government could not provide locally-produced cement with any protection against them. Local cement dealers also argued that they continued to buy imported cement not just because of the

[38] Interview, local cement dealer, August 2016.

price but because they trusted quality.[39] However, CIMERWA worked with 'Made in Rwanda' campaigns to persuade local consumers of the comparatively better quality of its cement.[40] CIMERWA officials complained that the government could still do more to ensure local consumers bought locally-produced cement (including in government projects). One cement dealer said, "in some tenders, CIMERWA is the specified dealer to be used but only sometimes. They never specify one of the importers."[41] For example, both Hima and Simba cement was used in the recently completed Kigali Convention Centre project.

> "The government is the one that can help. It should do more through tenders and ensure that companies buy local cement. Leadership has to understand that if anything happens to CIMERWA, industrialization will fail. It can even do more to protect its local companies. DRC, Uganda and Cameroon all stopped imports before. CIMERWA has a loan, which we will start paying in February and it expires in seven years. If we don't get enough government support, we might default in the loan."[42]

Though CIMERWA has increased its production capacity, most of its production is concentrated in Pozzolanic Portland Cement (PPC) 32.5N although it also produces some 42.5N cement. The two products are composed of different raw materials and are used in different kinds of construction projects. Another form of cement, 52.5N cement, is not yet sold in the Rwandan market. However, there is some demand for it. Importers like Simba also supply Ordinary Portland Cement (OPC). Local cement dealers said that Hima and CIMERWA dominate most of the market in 32.5N cement. However, Simba dominates most of the market in 42.5N cement and Simba employees do not see CIMERWA as a direct competitor. Importers interviewed agreed that it would be right for CIMERWA to dominate the market and that they had been impressed with how the company had captured market share to "up to about 50 per cent from having just 15 per cent a few years before."[43]

Clearly, there has been significant progress in import substitution in the Rwandan cement sector. This has occurred through heavy state intervention with the government seeking new investors, providing benefits for CIMERWA and assisting

[39] Interview, local cement dealer, August 2016.
[40] Interview, CIMERWA, August 2016.
[41] Interview, local cement dealer, August 2016.
[42] Interview, CIMERWA, August 2016.
[43] Interviews, cement importers, August 2016.

them in guaranteeing sales through some tenders and marketing campaigns.[44] However, the sustainability of the reciprocal control mechanism with CIMERWA is limited by the government's capacity to manage the demands of the foreign investors while adhering to EAC demands. It lacks the power it would have enjoyed if it had partnered with a domestic investor but it lost the opportunity for such a collaboration because of political reasons, with RIG's former leading investor (Rujugiro) now working with opponents of the government abroad.

Conclusion: The Challenge of Import Substitution in the 21st Century

Late development is always a challenging, unstable process. Initiating ISI had always been fundamentally a political process despite the technical challenges associated with it. In the 21st century, especially for a small, land-locked country like Rwanda with a limited market size, the political and technical challenges associated with ISI have been exacerbated. Given that ISI has been initiated after two decades of liberalization, the degree of state intervention required has been significant. However, the form of state intervention has been reactive, rather than a product of an established plan. It has had to counter challenges pertaining to abiding by regional trade rules and negotiating the power of importers while also finding ways to establish capacity to acquire technological capabilities and sustain reciprocal control mechanisms.

This paper has examined the challenge of developing a reactive strategy of import substitution in the 21st century after two decades of liberalization and market-led policies. Given that the Rwandan government has revised its strategy, its progress has been quite impressive. However, that has largely been down to the active role of the state in reversing some of its past market-led reforms. This paper argues that the Rwandan government has attempted to develop such policies through very active state intervention in the form of 'picking winners.' However, unlike existing literature on Rwanda's developmental patrimonialism, the paper demonstrates how state intervention has taken the form of picking foreign investors as 'winners', rather than party- or military-owned enterprises. Given the nature of "late late late development", as Hirschman (1968) would call it, a reliance on foreign investors should not be surprising. Clearly, like most other African countries, it shows that the Rwandan

[44] Interview, CIMERWA and MINICOM, August 2016.

government has been unable to develop a national capitalist class (Whitfield et al. 2015). However, it also shows that late development in the 21st century must occur while relying on foreign investors. This reliance is particularly unstable given that there are limited domestic capitalists who can absorb the technological acquisition that may be acquired from engagement with foreign investors.

Most importantly, this paper examines how reciprocal control mechanisms are built while negotiating the trade-offs associated with trade integration – where access to larger markets are often associated with limiting the use of industrial policy instruments. For Rwanda, legal restrictions on policy space from the WTO are less important when compared to the needs to abide by regional trade treaties (the EAC) and deal with pressure from donors. In the Rwandan case, increasingly free regional markets may prove to be costly in the short-term and only aggressive state interventionism can ensure that Rwandan-based companies can become regional champions, which acquire technological capabilities. For reciprocal control mechanisms with such champions to be sustained, the government must retain the capacity to discipline foreign investors. It must also be capable of monitoring such enterprises while nurturing domestic capitalists to be in place to absorb technologies and step in when the time is right.

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