Regionalism and the Global Economy

The Case of Africa

Edited by
Jan Joost Teunissen

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Director: Jan Joost Teunissen

Regionalism and the Global Economy: The Case of Africa

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Abbreviations

AATPO	Association of African Trade Promotion Organizations
ACP	Africa, Caribbean and the Pacific
AERC	African Economic Research Consortium
AfDB	African Development Bank
AMMTaZZ	Angola, Malawi, Mozambique, Tanzania, Zambia, Zimbabwe
AMZ	Angola, Mozambique, Zambia
ANC	African National Congress
APEC	Asia Pacific Economic Cooperation
ASECALs	Agricultural Sector Adjustment Loans
ASECAPs	Agricultural Sector Adjustment Programmes
BADEA	Arab Bank for Economic Development in Africa
BCEAO	Central Bank of the West African States
BLNS	Botswana, Lesotho, Namibia, Swaziland (also called BLSN)
BLNSAS	Botswana, Lesotho, Namibia, South Africa, Swaziland
CBI	Cross-Border Initiative
CEAO	West African Economic Community
CEMAC	Central African Economic and Monetary Union
CEPGL	Communauté Economique des Pays des Grandes Lacs
CET	Common External Tariff
CFA	Communauté Financière Africaine
CMA	Common Monetary Area (SACU members minus Botswana)
COMESA	Common Market for Eastern and Southern Africa
DBSA	Development Bank of Southern Africa
DFI	Development Finance Institution
EAC	East African Community
EC	European Community
ECA	Economic Commission for Africa
ECCAS	Economic Community for Central African States
ECLAC	Economic Commission for Latin America and the Caribbean
ECU	European Currency Unit
ESAF	Enhanced Structural Adjustment Facility
ESECAL	Energy Sectoral Adjustment Loan
EU	European Union
ECOWAS	Economic Community for West African States
FAO	Food and Agricultural Association
FDI	Foreign Direct Investment
FINSECAL	Financial Sector Adjustment Loan
FINSECAP	Financial Sector Adjustment Programmes
FRELIMO	Liberation Front of Mozambique
GATT	General Agreement on Tariffs and Trade
GDP	Gross Domestic Product
GNP	Gross National Product
GW	Giga-Watt
HLM	High-Level Manpower
IFIs	International Financial Institutions
IMF	International Monetary Fund
IOC	Indian Ocean Commission

ISECAL	Industrial Sector Adjustment Loan
kWh	Kilowatt-hour
LLM	Low-Level Manpower
LRMC	Low-Rate Marginal Cost
MFN	Most-Favoured Nation
milex	military expenditures
MMA	Multilateral Monetary Agreement
MNCs	Multinational Corporations
MRU	Mano River Union
MTZ	Malawi, Tanzania, Zimbabwe
MW	Megawatt
NAFTA	North American Free Trade Agreement
NBA	Niger Basin Authority
NORSAD Fund	Export Pre-Financing Revolving Fund in SADC region
OAU	Organisation of African Unity
OECD	Organisation for Economic Co-operation and Development (which comprises 23 developed country members as well as Mexico and Turkey)
OMVS	Organization pour la Mise en Valeur du Fleuve Senegal
PTA	Preferential Trading Area of Eastern and Southern Africa
REER	Real Effective Exchange Rate
RER	Real Exchange Rate
REXSTAB	Regional Exchange Rate Stabilisation Mechanism
RIA	Regional Integration Arrangement
RoW	Rest-of-the-World
RTAs	Regional Trading Arrangements
SA	South Africa
SACCAR	Southern African Centre for Cooperation on Agricultural Research
SACU	Southern African Customs Union (South Africa, Botswana, Lesotho, Namibia and Swaziland)
SADC	Southern Africa Development Community (former SADCC + South Africa)
SADCC	Southern African Development Coordination Conference
SAF	Structural Adjustment Facility
SAPs	Structural Adjustment Programmes
SAR	Southern African Region: Angola, Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe
SARCCUS	Southern African Centre Regional Commission for the Conservation and Utilisation of Soil
SECAL	Sectoral Adjustment Loans
SECAP	Sectoral Adjustment Programmes
SOE	State-Owned Enterprises
SSA	Sub-Saharan Africa
TU	Taxe Unique
UAPTA	Unit of Account of the PTA
UDEAC	Customs and Economic Union of Central Africa
UDEAO	former Customs Union of Francophone West African States
UEMOA	West African Economic and Monetary Union (CEAO + UMOA)
UIM	Urban, Industrial and Mining
UMOA	West African Monetary Union
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
UNICEF	United Nations Children's Fund
UNIDO	United Nations Industrial Development Organisation
UNDP	United Nations Development Programme

US(A)	United States (of America)
USAID	United States Agency for International Development
WAPCO	West African Pipeline Company
WBG	World Bank Group
WTO	World Trade Organisation
ZESA	Zimbabwe Electricity Supply Authority

Preface

With Europe's deep integration, the surge of the "new regionalism" in Latin America, and mega-initiatives such as the Asia Pacific Economic Cooperation (APEC) agreement, regional economic integration has received a new, worldwide impetus. The challenges that this new wave of regional integration arrangements poses to developing as well as industrial countries has led Fondad to embark on a three-year research project which aims to explore how regional integration as well as multilateral cooperation can be promoted, in a mutually reinforcing manner.

In this volume on Africa's integration efforts, eminent experts and policymakers from various African as well as international institutions carefully explore what went wrong, what perspectives exist for doing things better, and how future policies could create the opportunity for success. Questions addressed include: Can regional cooperation and integration help African countries develop more successfully? What form of regional cooperation would be most relevant in different parts of the continent (ranging from regional coordination of infrastructural investments and management of natural resources to regional integration in trade, investment and finance, leading ultimately to economic and even political union)? How can policies of national governments and international financial institutions be improved in design as well as implementation?

The four in-depth papers included in this volume address these broad questions as well as the more specific issues that emerge. Ernest Aryeetey and Abena Oduro provide an encompassing overview of Africa's integration efforts and try to assess what future direction these efforts should take. Peter Robinson takes a close look at the highly promising prospects for infrastructural and natural resources investment coordination. William Lyakurwa researches the links between intra-regional trade and investment, while Percy Mistry, in a path-breaking analysis, dwells on the regional dimensions of structural adjustment programmes.

Earlier attempts at regional integration in Africa have largely failed, so why would a "second round" now have any better chance of success? The main reason for the failure of earlier attempts at regional integration may lie in the fact that most national economies have performed dismally. As the development model in Africa changes toward greater reliance on markets and much greater pragmatism in economic policy, it seems that

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the expansion of regional and sub-regional markets is a *sine qua non* for success. Provided that some degree of internal and external balance is achieved and maintained, African countries may enter a more promising era. In addition, although regional conflicts persist, security has improved in some areas of Africa, removing a major part of the rationale for autarkic policies and providing a new basis for cooperation and integration to be actively pursued.

We are grateful for the solid and spirited contributions by the participants to the conference in Midrand (Johannesburg) from which this book results. Special thanks go to Percy Mistry, Peter Robinson, Rosalind Thomas and her colleagues at the Development Bank of Southern Africa who have been of great help in preparing the conference; and Julie Bivin who assisted in the publishing of this book. Fondad gratefully acknowledges the co-sponsoring of the Midrand conference by the Swedish International Development Cooperation Agency (SIDA), the African Development Bank, the Development Bank of Southern Africa, and the ongoing support of the Dutch Ministry of Foreign Affairs.

Jan Joost Teunissen
Director
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I Regional Integration Efforts in Africa: An Overview

Ernest Aryeetey and Abena D. Oduro

I Introduction

Regional integration arrangements in Africa have generally been perceived to be vehicles for overcoming the constraint of small economic sizes of nations. Their sizes are seen to have hampered their ability to industrialise efficiently, particularly within the context of import-substitution, an approach that many African countries adopted soon after independence in the 1960s. Regional integration was conceived as a means to facilitate the structural transformation of African economies. This thinking is best illustrated by the preamble to the treaty of the Economic Community of West African States (ECOWAS), where the setting up of the community was noted to be in consideration of the "... overriding need to accelerate, foster and encourage the economic and social development of their states in order to improve the living standards of their peoples" (ECOWAS, 1975). The structural transformation envisaged was later clarified to be within the context of "self-reliant and self-sustaining development of member states" (OAU, 1980, p. 128).

While we note that efforts at achieving one form of integration or another have characterised the post-independence history of African states, there have been some differences among various regional groupings and other interest groups on the extent of integration warranted by the goal of achieving structural transformation. Even though they may generally be divided between those who favoured the creation of regional or sub-regional economic groupings and those for a high level of political integration, the spectrum of possible economic integration is certainly broad (McCarthy, 1996). We concentrate in this paper on economic integration efforts, and observe that these may range from simple economic cooperation to an economic union.

McCarthy (1996) has pointed out that historically, various points on the economic integration spectrum have been achieved elsewhere through a step-wise graduation of integration units. They often start with economic *cooperation*, "which refers to any joint activity across national frontiers, for the purpose of cooperation in economic matters, from running a joint regional airline or coordinated rail system to the joint management of river

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basins" (McCarthy, 1996, p. 213). Regional *integration*, which could follow cooperation, is more narrowly focused on expanding intra-regional trade through the removal or lowering of the barriers to trade in goods and services. Integration at the lowest level could involve the operation of preferential trading arrangements, where any number of countries would agree on lower tariffs for imports. This starts with the creation of a *free trade area* where barriers to trade among the participating nations are removed but each member state maintains its own restrictive practices, including tariffs, against trade with non-members. Following an exhaustion of the benefits of a free trade area, a *customs union* might be pursued as members adopt a common external barrier to trade with non-members, sharing tariffs on imports and other restrictions on free trade with non-members. They may follow these arrangements with a *common market* when capital and labour join goods and non-factor services in the free flow among member states. An *economic union* is deemed to have been created when they start pursuing common fiscal and monetary policies.

Most integration schemes in Africa have aimed at achieving a common market eventually (Johnson, 1991). Unfortunately, hardly any schemes have achieved the anticipated progression with time towards that goal. By 1990, the target date for the establishment of a customs union within ECOWAS, very little progress had been made towards a free flow of goods and a common external tariff required for the creation of the customs union. Langhammer and Hiemenz (1991, p. 29) describe the sequence of African regional integration efforts as "a dynamic initial phase, in which numerous programmes are launched ... followed by a period of implementation difficulties or failures and ratification problems". Indeed, most of the integration schemes have not made any headway in achieving their objectives largely because of the lack of implementation of treaties and protocols.

There appears to be some consensus that regionalism in Africa has only achieved very limited success at best (Foroutan, 1992; Fine and Yeo, 1994; Gambari, 1991; Langhammer and Hiemenz, 1991). This has given way to some considerable pessimism as it is suggested by many scholars that current African regional groupings are unlikely to confer net positive static welfare gains on members because they do not have the required conditions for trade creation effects that outweigh trade diversion effects (McCarthy, 1996).

But the formation of African regional groupings in the past has not relied on the expectation of static welfare benefits for their creation. Regional cooperation has been perceived as a means to industrialise efficiently by taking advantage of the opportunities of economies of scale and specialisation which cooperation would make available; and as a means to increasing their bargaining strength vis-à-vis the industrialised countries. Despite the clear difficulties of various integration schemes, official statements expressing the desire for integration amongst African Heads of State are continually being made. The recent formation of a not-yet functional African Economic Community in 1994 under the Abuja Treaty is the latest example. The ECOWAS Treaty has been revised in the light of past experience and changing circumstances. The Preferential Trading Area for Eastern and Southern Africa (PTA) has been transformed into a common market, with the ratification of a treaty bringing COMESA (the Common Market for Eastern and Southern Africa) into existence. SADCC has responded to the changed political circumstances in its sub-region and has evolved into SADC (Southern Africa Development Community) which no longer concentrates only on project coordination but also incorporates trade integration. The CEAO and UMOA in francophone West Africa have been merged to form the West African Economic and Monetary Union (UEMOA). Similar developments have also occurred in francophone Central Africa.

An important issue, however, remains the extent to which these recent developments signify a genuine intent to implement regional integration agreements. Fine and Yeo (1994) in an attempt to answer why efforts at regional integration persist despite their failures, attributed this to the irrelevance of regional integration to most national governments and the lack of political or economic cost in re-affirming solidarity towards ineffective agreements. This view would appear simplistic to us.

Renewed Interest in Integration

Renewed interest within Africa in revitalising and resuscitating regional groupings could be seen as a response to the deepening and enlargement of integration in Europe, the formation of a free trade area in North America, and similar developments in Southeast Asia. There is the fear that Africa's position in the world economy will be weakened further if it does not strengthen its already existing regional groupings. This is because, with the changes in the international economy, "... a failure to overcome, or reduce, the costs of market fragmentation in regions whose countries have not yet begun to cooperate will mean that those regions, as a whole, will be less well placed in the future to attract the foreign investment, technology and know-how on which they will have to depend for their future growth" (Mistry, 1995, p. 38). Thus, from the point of view of governments, regional integration may no longer be irrelevant for the growth and structural change of African economies. Indeed, developments in the rest of the world have forced Africans to take another look at their efforts at regional

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integration. The experience of Europe and developments in North America suggest that there are gains to be made from integration and that these gains go beyond the static welfare effects (Markusen, 1985; Mistry, 1995; and Wonnacott, 1985).

The possibility of current regional cooperation attempts being more successful now than in the past is improved because of economic changes in African economies which have embarked on structural adjustment programmes (SAPs). These changes may have created a domestic interest group which will press for greater regional integration. Most African countries have implemented trade liberalisation programmes, as part of SAPs, which have resulted in substantial tariff reductions so that the adjustment shock accompanying regional trade liberalisation may be lower than it otherwise would have been. If the SAPs have created incentives towards exporting, then the growing number of firms with an export potential will increase the domestic lobby or support group for further regional trade liberalisation.

Aside from the interest emanating from Africa itself, there is also interest expressed from outside to see regional integration efforts succeed. The World Bank's long-term perspective study on a strategy for Africa's economic development states that "progress toward market integration and increased cooperation in a whole range of areas "... is central to Africa's long term development strategy" (World Bank, 1989, p. 162). This is based on the premise that regional integration can accelerate growth in the region if it facilitates an increase in trade. It has been suggested that "... regional integration should be supported as a means of achieving greater outward orientation" (Mansoor and Inotai, 1991, p. 226). The emphasis is more on larger regional units as against sub-regional bodies. This is because "... none of the existing sub-regional bodies ... are large enough to rely on internal trade" (Mansoor and Inotai, p. 226).

The experiences of regional integration in Africa, in relation to those of other regions, need to be analysed within a broad framework. The objective of this paper is to place regional integration efforts in Africa within an appropriate historical and conceptual perspective. The paper is intended to provide an overview for the other papers included in this book. Section 2 reviews what the rationale for integration has been and currently is. In section 3 we present major features of integration in Africa, focusing on experiences with institutional development in the light of given objectives and the difficulties they face. We follow this in section 4 with a discussion of various perceptions of the outcomes of integration efforts before considering what have generally been acknowledged to be broader constraints to regional integration on the continent in section 5. The next section looks at various approaches that have been proffered for overcoming the con-

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straints to effective regional integration. We discuss here the possible paths that African regionalism can take in the future, given the objective of accelerated growth and structural change. Section 7 concludes the paper.

II The Rationale for Economic Integration in Africa

The need for integration is usually perceived to be the result of the nature of the problem that individual African countries are confronted with in the attempts to industrialise and modernise their economies, while achieving self-sufficiency. These problems include difficulties in gaining access to all required materials, following the uneven spread of natural resources and the lack of funds; difficulty in finding efficient and affordable technologies to suit domestic market conditions; difficulty in securing domestic and external markets for manufactured goods; etc. Individual countries are sometimes perceived to be too small to provide any significant domestic markets for both heavy and light industrial goods produced with equipment designed for larger scales of production, thereby forcing the adoption of inefficient production techniques. The smallness of countries and the large number of them competing with one another on international markets often reduces the strength of their bargaining on such markets.

In addition to the small sizes of nations, the fact that many African economies are dependent on a narrow set of similar primary products generally affects their participation in world trade. Africa's participation in world trade, which has never been significant (about 2% in 1990), has reduced in the last decade. Intra-regional trade is itself very low, amounting to only 6% of total foreign trade of African nations in 1990. To offset the unfavourable trends of external markets, it is often suggested that increased trade among African nations could bring greater advantages to the nations involved and help them to mobilise their resources by finding markets for their goods. This would be especially so if it involved some regional groupings (OAU, 1981). McCarthy (1996) has observed that "the small size of most of these developing economies, notably those in Africa, restricts the ability of these countries to benefit from lower unit costs (derived from economies of scale) and viable import-substituting opportunities, hence the argument that African countries should attempt to create customs unions or common markets. This will enable manufacturers to produce at lower unit costs for a larger protected market".

In this light, formation of regional integration arrangements has been pursued as a developmental objective by many African governments. In presenting the Lagos Plan of Action, African leaders expressed their hope and belief in concerted action. The assembled Heads of States and

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Governments belonging to the Organisation of African Unity (OAU) stated, "We commit ourselves, individually and collectively, on behalf of our governments and peoples, to promote the economic integration of the African region in order to facilitate and reinforce social and economic intercourse" (OAU, 1981, p. 5). The OAU sought to achieve this objective through sub-regional and regional groupings operating with reduced barriers to trade. "We hold firmly to the view that these commitments will lead to the creation at the national, sub-regional and regional levels, of a dynamic and interdependent African economy and will thereby pave the way for the eventual establishment of an African Common Market leading to an African Economic Community" (OAU, 1981, p. 6).

Traditional Expectations of the (Static) Gains from Regional Integration

Very often, the discussion of the gains from integration in Africa does not consider the potential consumer gains[1]. It is taken for granted that the removal of tariff and non-tariff barriers on the movement of goods within the region should benefit consumers as prices fall and variety increases. Greater concern is focused on the potential producer gains and how these are to be distributed. This is because, as seen earlier, the major objective behind the formation of these units is structural change through an increase in manufacturing output. This bias is unfortunately reflected in our own discussion below, even though consumer welfare is introduced where possible.

Based on the fact of smallness of African economies, intra-regional trade as a means of expanding markets available to domestic economies has been the main factor that drew nations to seek integration and set up various integration arrangements in the 1960s. In the orthodox conceptualisation, a regional economic grouping is likely to be beneficial to its member states only if trade creation effects outweigh any trade diversion effects. Trade creation is enhanced if the partners are competitive, but with the potential of producing complementary goods through specialisation.

Trade integration can be welfare-enhancing, i.e. if the goods of high-cost domestic producers are replaced with lower-cost goods from regional producers in the union. This is derived from cost reductions if it lessens market distortions arising from national policies, as well as from economies of scale in public sector activities. Static welfare gains are made on both supply and demand sides. They arise from the relative size of trade creation gains as against trade diversion losses. On the supply side, a more

1 This is also a feature of the debate on trade liberalisation in general.

effective reallocation of resources would lead to production efficiencies. On the demand side, consumer welfare is enhanced through greater choice and lower prices. It needs to be emphasised, however, that increasing intra-regional trade as a result of integration need not be welfare-enhancing if it leads to trade diversion where a common external tariff leads to higher prices when high cost regional producers replace low-cost producers outside the market. It is often argued that trade diversion would be short-term, which allows trade creation, which is longer-term, to offset the short-term diversion losses arising from integration by capturing dynamic efficiency.

Mistry (1995) has discussed extensively the orthodox or static gains expected from integration. While he accepts that trade creation could result from integration, he points out this can be sustained only if the issue of regional equity is well accounted for. The differences in capacity of various nations requires that regional policy is utilised to accommodate the complications that arise from inequalities. Trade creation will result from integration if: "(a) each member's pre-integration tariffs are high; (b) production structures of members' economies are roughly similar in their output mix but different in the pattern of relative prices at which similar products are produced; (c) external tariffs applied by the region's members are common and low in comparison with pre-integration tariffs; and (d) the production structures of members are sufficiently responsive to permit intra-regional import-substitution at the same or lower cost than the cost of the same products from extra-regional sources. When any of these conditions is not met, trade diversion may occur" (Mistry, 1995, p. 15).

But McCarthy (1996) is not optimistic about the probability of trade creation offsetting trade diversion in the small economies of Africa that embark on import-substitution and expect to create markets in the region, following their difficulty in competing in the global economy. He notes that "regional integration in this way becomes an inward-looking instrument of industrial development, diverting trade from cheaper sources in the rest of the world to higher-cost producers within the union".

Dynamism in the Gains from Integration

Current discussions on the benefits of regional integration have moved beyond the traditional arguments of trade creation and diversion. Robson (1993) argues strongly that the failure of developing country integration units to generate static gains of integration because they are not optimal trading or currency areas does not justify the discouragement of the formation or existence of these units. Mistry (1995) has argued that sustainable real income growth as a result of regional integration is possible, even if empirical evidence from a number of regions is inconclusive. Such dynamic efficiency gains are expected to arise from "economies of scale in trade-supporting industries and services which are caused by market enlargement; spill-over effects resulting from wider knowledge transfers across the region on both an intra-industry and inter-industry basis; increased competition; increased levels of investment; stepped up pace of technological change; and consumption smoothing during business cycles". Additional dynamic gains arise from the benefits of policy and investment coordination. Regional integration is seen to have the potential to be growth enhancing if it encourages investment in both physical and human capital.

Lowering intra-regional trade barriers can bring about a restructuring of production at the regional level. Whether or not the restructuring occurs depends upon firms' responses to the lowering of regional trade barriers. The options to firms in a national economy facing increased competition from firms of member countries is not limited to exiting the industry. Firms could respond to the increased competition by either cutting production costs, improving product quality or diversifying products. For some firms these may have been options which were not chosen before because of the cushioning effect of the previous trade regime. The ability of firms to choose a combination of these options rather than shut down, depends on domestic policy concerning operation of the labour market, financial markets and the supply of non-traded inputs (i.e. electricity, water and telecommunications). Other important factors are the firms' ability to seek out low cost sources of inputs.

An increase in market access at the regional level will allow firms to increase their utilisation of existing excess capacity. As firms increase their production runs this should allow movement down average cost curves, improving efficiency and probably reducing price. Apart from the benefits of economies of scale the specialisation accompanying this process will allow for a more efficient utilisation of the region's resources.

The larger integrated market should facilitate an increase in investment, both local and foreign. However, the removal of trade barriers is not enough to ensure an increase in investment. Investment will only increase if economic agents perceive that the formation of the integration unit will enhance growth prospects region-wide. Investors need to be assured that the macroeconomic environment will remain fairly stable and expropriation of private capital is not an issue. The regional integration arrangement has to be credible, i.e. investors have to believe that the regional trade liberalisation process will be maintained. Preliminary evidence from Mexico suggests that credibility of the trade integration agreement with the USA and Canada, as well as the prior economic reforms which were implemented, encouraged some of the net increases in investment flows in 1993 (Bannister, Primo Braga and Petry, 1994). Cooperation in the provision of regional economic infrastructure, harmonisation of tax codes, investment codes and fiscal and monetary policy will increase market integration and therefore reduce transaction costs, facilitating greater trade integration, as well as encouraging more regional investment.

Formation of a regional unit can increase the bargaining strength of the member countries. This requires an ability to adopt a unified regional position on the relevant issues. This is particularly important for negotiating trade and international commodity agreements with third parties. A prerequisite for this, however, is the coordination of national agricultural and industrial policies. It may be possible to obtain more trade concessions *en bloc* as opposed to individually. In this case, African countries may be more willing to drop the principle of non-reciprocity in their trade negotiations since they will be negotiating from a more strengthened position.[2]

Related to the argument of a stronger regional bargaining position is the argument that the larger protected regional market could serve as a training ground for African firms anxious to compete equally in the tougher global market place. The regional market affords an opportunity for firms to develop appropriate approaches to medium-term cost-reduction with eyes set on a market beyond the regional boundary. These would be the first steps towards competing in global markets.

Impediments to Realising Expected Benefits

The expected benefits of operating within the protected regional market will not materialise if, despite the formation of the regional integration unit, non-tariff barriers to integration remain, non-transparent forms of discrimination against third parties are maintained and the issue of how to distribute the gains and costs of regional integration is not adequately addressed.

Mistry (1995) classifies non-tariff barriers into three groups, i.e. those which affect trade, production and investment. Quantitative restriction and inconvertible and separate national currencies are the important non-tariff barriers which affect intra-regional African trade. Differences in national product and service regulations, protection of domestic labour markets and the predominance in most domestic markets of parastatals which have purely national objectives constitute the non-tariff barriers on production. These barriers affect both member countries and third parties. An example

2 It has been argued that the non-application of the principle of reciprocity for the developing countries has contributed to their marginalisation in international trade talks. The developing countries were also willing to accept the principle of non-reciprocity for the developing countries in lieu of greater market access.

of non-transparent forms of discrimination against non-member countries is rules of origin that may not only discourage foreign investment but can also adversely influence firms' decisions concerning the sourcing of inputs.

III Features of Regional Integration in Africa

This discussion of the features of regional integration will be divided into two broad areas. The first examines the genesis of the different types of institutions. The second focuses on a number of features of their operations that cut across units and allows some comparisons, dwelling at length on their common problems.

Regional Integration Arrangements in Africa

Probably the most conspicuous feature of African regional cooperation and integration efforts is the large number of units on the continent, as earlier seen, and the membership of individual countries in more than one regional unit (see Table 1). Another important feature is the variety of objectives that the regional integration arrangements have taken (see also Table 1).

Broadly-speaking, a number of the initiatives of regional groupings have been sponsored by the Economic Commission for Africa, making it possible to place them in one category, to be contrasted with another category that sprang up as a result of other initiatives. The ECA has promoted three sub-regional arrangements for West Africa (ECOWAS, established in 1975), East and Southern Africa (PTA, established in 1981, which later became COMESA) and Central Africa (the still-under negotiation ECCAS). We consider first the ECA and those arrangements it sponsored, and then the others.

The Economic Commission for Africa and Regional Integration

The ECA's involvement in regional integration attempts is derived from its interest in Africa's industrial future. In 1979, the ECA's Conference of Ministers passed resolution 332 (XIV) on a strategy for the African region in the International Development Strategy for the Third United Nations Development Decade (1980-1990). The conference opted to declare the decade the *Industrial Development Decade for Africa.* Following its adoption by the OAU Summit Meeting of Heads of State in Monrovia, the decade was declared as such "for the purpose of focusing greater attention and evoking greater political commitment and financial and technical support,

Table 1 Regional Integration Arrangements in Africa

	CEAO	CEPGL	ECOWAS	MRU[2]	PTA[3]	SACU	UDEAC[4]	UEMOA	Lagos Plan of Action
Founded:	1972	1976	1975	1973	1981	1969	1964	1994	1980
Objective:[1]	FTA	FTA	FTA	CU	FTA	CU	FTA	EU	EU
Angola					•				•
Benin	•		•					•	•
Botswana					•	•			•
Burkina Faso	•		•				•	•	•
Burundi		•			•				
Cameroon							•		•
C.A.R.							•		•
Chad							•		•
Comoros					•				•
Congo							•		•
Côte d'Ivoire	•		•					•	•
Djibouti					•				•
Equatorial Guinea							•		•
Ethiopia					•				•
Gabon			•				•		•
Gambia, The			•						•
Ghana			•						•
Guinea			•	•					•
Guinea-Bissau			•						•
Kenya					•				•
Lesotho					•	•			•
Liberia			•	•					•
Madagascar					•				•
Malawi					•				•
Mali	•		•					•	•
Mauritania	•		•						•
Mauritius					•				•
Mozambique					•				•
Namibia						•			•
Niger	•		•					•	•
Nigeria			•						•
Rwanda		•			•				•
Senegal	•		•					•	•
Seychelles									•
Sierra Leone			•	•					•
Somalia					•				•
South Africa						•			•
Sudan					•				•
Swaziland					•	•			•
Tanzania					•				•
Togo			•					•	•
Uganda					•				•
Zaire		•							•
Zambia					•				•
Zimbabwe					•				•

1 FTA: free trade area; CU: customs union; EU: economic union.
2 In effect since 1974.
3 In effect since 1984.
4 In effect since 1966.

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at the national, regional and international levels for the industrialisation of Africa". It was this declaration that subsequently led to the Lagos of Plan of Action (1980).[3]

For the realisation of the decade a number of meetings and negotiations were held with various multilateral agencies, particularly United Nations Industrial Development Organisation (UNIDO), which led to the preparation of a framework for its operationalisation. Within that framework, provision was made for action to be initiated at the national level, sub-regional and regional levels and at the international level. The approach for the establishment of a sub-regional industrial programme was based on the identification of priority branches and the necessary inter-sectoral structures within a sub-region. It was suggested that these might include basic sectors such as the iron and steel, metallurgical, chemical, petrochemical, mechanical and electrical engineering, capital goods, agro-related, forest products and building materials industries.

The ECA proposal considered it important that sub-regional institutions be able to forecast sub-regional demand for products based on analysis and projection, estimate present and future production in the sub-region, calculate quantities required to meet demand with existing capacities, and identify other key industrial projects which utilise these basic products as inputs. Suggestions were further made for the financing of sub-regional programmes through such agencies as the African Development Bank and the Arab Bank for Economic Development in Africa.

For the implementation of the sub-regional plan for Africa's industrialisation, the importance of trade expansion within the region was considered a priority. The ECA noted among the constraints to increased intra-African trade: deficiencies in physical (transport and communications) and institutional (commodity exchanges, clearing houses, etc.) infrastructure; tariff and non-tariff barriers; lack of adequate information on products; relatively high, uncompetitive prices of African manufactures; lack of facilities for trade and export credit; inadequate marketing and distribution channels; instability of supply; and payment difficulties. On the basis of these observed constraints, the following suggestions were made to sub-regional bodies:

(a) Identification and analysis of demand for and supply of industrial products, industrial raw materials and intermediate and consumer goods that meet the needs of African countries;

3 The ideals of the Lagos Treaty were further entrenched in the Abuja Treaty of 1991.

(b) Production of industrial goods in keeping with the needs and complementarity of African markets;
(c) Adoption of incentives that will assist African exporters and importers to increase intra-African trade;
(d) Establishment and strengthening of State or semi-State trading houses that will spearhead intra-African trade and promote the marketing and distribution of raw materials, semi-processed and manufactured goods;
(e) Strengthening the Association of African Trade Promotion Organisations (AATPO), which will promote trade among African countries by bringing together buyers and sellers, promoting trade fairs and disseminating data and information;
f) Strengthening the activities of the sub-regional clearing house that will provide African exporters and importers with short- and medium-term credit facilities.

The ECA proposal outlined various arrangements for product sub-sectors within the industrial sector, with emphasis on the appropriate institutional set-up for improving production in those sub-sectors. It needs to be mentioned, however, that, much as the ECA, the OAU and UNIDO rightly recognised the need to attach priority attention to industrial development, the approach adopted for industrial development focused rather too extensively on the creation and strengthening of institutions that were expected to facilitate the operation of production agents rather than on the production agents themselves. Indeed, it is our view that although an improved and strengthened role for the private sector was implied in some of the strategies outlined, direct private sector development was obviously not a major concern of African policymakers.

The Economic Commission for West African States (ECOWAS)

ECOWAS has always had the aim of eventually becoming a customs union and then a common market while integrating states in the West African sub-region. It comprises sixteen member states, ten of whom have allegiances to other sub-regional groupings. Thus, the Mano River Union embraces Guinea, Liberia and Sierra Leone; the West African Economic Community (CEAO) pulled together Benin, Burkina Faso, Côte d'Ivoire, Mali, Mauritania, Niger and Senegal; the remaining six ECOWAS states of Cape Verde, Gambia, Ghana, Guinea Bissau, Nigeria and Togo had no other sub-regional trade grouping until recently when Togo joined UEMOA. The ECOWAS arrangement holds together some 200 million people and is operated through a conference of Heads of State, a Council of Ministers, an executive secretariat, a development and cooperation fund and five specialised commissions. The five commissions are dealing with: (1) trade, customs, immigration, monetary and payments; (2) industry, agriculture and natural resources; (3) transport, communications and energy; (4) social and cultural affairs; (5) administration and finance.

The areas in which ECOWAS seeks to promote cooperation and development among member states are industry, transport, telecommunications and energy, agriculture, natural resources, commerce, monetary and financial matters, as well as social and cultural affairs. The goal of all this is to raise the living standards of the people of the sub-region. Its legal basis is to be found in the Lagos Treaty, supplemented by a series of 29 protocols and supplementary protocols that guide operations in such areas as trade liberalisation, transport, community citizenship, rights of free movement and residence, and technical cooperation.

Under the Trade Commission, the ECOWAS Fund for Cooperation, Compensation and Development was established and located in Lomé in 1977. The Fund has as its objective the promotion of economic development and integration through the financing of industrial and infrastructure projects of common interest to ECOWAS states. In doing this, it also administers the ECOWAS Trade Liberalisation Scheme Compensation Fund which was set up in 1990 to compensate member states for losses in revenue arising from the introduction of trade liberalisation measures.

The ECOWAS Fund has contracted lines of credit from several sources, including the European Investment Bank, African Development Fund and African Development Bank as well as commercial banks. These sums, totalling some 60.4 million West African Units of Account by May 1992 were on-lent to projects in telecommunications, roads, rural development and industrial sectors.

Trade among member states presently amounts to about only 6% only of official recorded trade, having grown from some 2.1% in 1970, 3.1% in 1975, 3.9% in 1980, 4.2% in 1985 and 5.5% in 1987. In the period 1980-89 the annual average growth rate of exports for the community was -7.2%, thus a reducing trend in importance to the world market. Mansoor and Inotai (1991) note that, "If one takes account of unrecorded trade, which in some cases surpasses the officially registered figures, it is even harder to find evidence of gains".

For Ghana, for example, imports from ECOWAS states amounted to only 8% of total imports while exports to the subregion amounted to some 4% of total exports in 1991. Côte d'Ivoire, Burkina Faso, Mali and Senegal appear to be the only countries with imports from member states exceeding 10% of their total exports. Three of these four countries (i.e. minus Mali) and Benin were also the only ones with exports to ECOWAS states exceeding 10% of total exports. Côte d'Ivoire is by far the most important

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country in terms of intra-ECOWAS trade. It is interesting that while a great deal of traditionally strong trade links exist among the francophone nations (most of whom formed the CEAO), this is usually in the area of livestock and agricultural products. Manufactured exports come mainly from Côte d'Ivoire. Nigeria, another major exporter to the sub-region, offers mainly petroleum products.

The Common Market for Eastern and Southern Africa (COMESA)

The COMESA which began as the Preferential Trade Area (PTA) for Eastern and Southern Africa had an original goal of becoming a common market by the year 2000. It was subsequently transformed in 1993 to the Common Market for Eastern and Southern Africa (COMESA). COMESA embraces twenty-two countries and now focuses on deeper integration objectives after moving from loose cooperation to a free trade area. The most important objective of the earlier PTA was to promote intra-regional trade using trade liberalisation measures. This was to be achieved through protocols on Reduction and Elimination of Trade Barriers, Customs Cooperation, the Rules of Origin, Re-Export of Goods, Transit Trade and Transit Facilities, Clearing and Payments Arrangements, Transport and Communications, Simplification and Harmonisation of Trade Documents, and Procedures on Standardisation and Quality Control. Other areas of cooperation were industry, agriculture, monetary affairs and natural resources. The PTA expected to achieve its trade liberalisation programme of reducing tariffs by September 1992, after having reduced initial tariffs by 10%-70% and planning to reduce these further by 25% every two years.

The new COMESA treaty calls for the establishment of a customs union through the removal of all trade barriers and the establishment of a common external tariff and rules of origin. The new treaty has also introduced cooperation in monetary and financial matters. The treaty anticipates coordination of macroeconomic policies as the countries move towards free movement of services and capital as well as the convertibility of currencies. COMESA stresses a commitment to the re-distribution of the benefits of integration, an issue that was previously not addressed by the PTA. It plans to achieve these through special regional programmes to promote the development of the least developed countries in the region in order to achieve balanced development within the common market.

The PTA was probably best known for its institutional growth. It created specialised institutions to coordinate the development and integration processes of member states, including the setting up of the Trade and Development Bank for Eastern and Southern Africa, the PTA Clearing

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House, the PTA Federation of Chambers of Commerce and Industry. The PTA was also known to be active in organising such activities as trade fairs for member states, organising four such fairs in eight years.

While it achieved a high profile in the region, the PTA is not known to have created much trade. Langhammer and Hiemenz (1991, p. 28) reported that "trade liberalisation in the PTA framework has been biased toward trade diversion". By 1982, the PTA's share in world trade was 0.56%. This dropped to 0.4% in 1993, after a decade of PTA operation. Over 94% of PTA trade was with non-member countries. Intra-PTA exports as a percentage of total PTA exports declined from 7% in 1982 to 6.6% in 1992. At the same time imports within the region remained at only 4.7% of total regional imports. The PTA is seen to have had a number of shortcomings as countries pursued trade policies that did not encourage intra-PTA trade.

Non-ECA Sponsored Integration Arrangements

Within ECOWAS, there are two sub-regional groupings that operate with almost similar objectives, but not sponsored by the ECA. There is the Mano River Union, a weak alliance of Guinea, Liberia and Sierra Leone that seeks to develop the river basin area jointly and the francophone West African Economic and Monetary Union (UEMOA), with Benin, Burkina Faso, Côte d'Ivoire, Mali, Niger, Senegal and Togo, who share a common central bank (BCEAO). UEMOA came out of the re-alignment of francophone West African interests in 1994 which saw the demise of CEAO. In Central Africa, the equivalent of UEMOA is currently CEMAC, the Central African Economic and Monetary Union which embraces Cameroon, Central African Republic, Chad, Congo, Equatorial Guinea and Gabon. They all aspire to achieving customs unions. It appears that while various countries would like to operate from smaller groupings held together by a certain common factor (language or a river in these cases), they would not like to give up membership of the larger ECA-sponsored body. It is simply the adoption of a "wait and see" attitude towards the larger body.

As in West Africa, a number of smaller non-ECA sponsored regional integration arrangements may also be found in Eastern and Southern Africa. The best known of these is the Southern African Development Community (SADC) which replaced the Southern African Development Coordination Conference (SADCC). Whereas the latter was generally perceived to be an organisation whose initial goal was to reduce its dependence on apartheid South Africa (not interested in a customs union), the former has almost all the trappings of an economic integration arrangement. In moving towards trade integration, SADC which embraces eleven

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of the COMESA states has adopted measures that involve tariff reductions and the removal of non-tariff barriers. It seeks greater coordination of external tariffs and the promotion of free movement of capital and people. It also has interest in setting up regional infrastructural authorities and a development bank. The existence of both SADC and COMESA is certainly questionable, considering the congruency of their objectives and their individual circumstances, a point we discuss again later in more general terms.

Other notable regional integration arrangements in Southern Africa include the Southern African Customs Union (SACU), made up of South Africa, Botswana, Lesotho, Namibia and Swaziland, and thc Common Monetary Area (CMA), which involves SACU members minus Botswana. SACU has operated as a customs union since 1910 and McCarthy (1996) suggests that its longevity can be explained by the fact that the four smaller member states have been compensated for losses sustained over the years, a fact which encourages them to stay in a union dominated by South Africa. South Africa has maintained this union because it was its main outlet to African markets during the years of apartheid (McCarthy, 1996).

Important Aspects of the Institutional Development of Regional Integration Arrangements

There are generally a number of characteristics of regional integration arrangements in Africa, most of them indicating the difficulties they have gone through over the past three decades and their attempts to solve them through re-orientation of institutions, as earlier seen. We present below some of these more conspicuous characteristics.

Multiple Objectives

A characteristic of African integration efforts is that most groupings are concerned not only with trade integration but also with harmonisation of agricultural, industrial, transportation, energy, fiscal and monetary policies. SADCC until it was transformed into SADC, was the only large regional grouping which did not have trade integration as an objective. The overriding need to expand the market size available to local industries can explain the emphasis on trade integration within most of these groups. The objective of increasing intra-regional trade in most regional integration agreements is not only to exploit potential economies of scale but also a means to achieve regional self-reliance, hence the need to exploit the potential of all sectors.

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Overlapping Membership

Most countries are members of more than one regional arrangement. In addition to these there are also bilateral, trilateral and quadrilateral arrangements amongst countries. The disadvantage of the large number of regional integration arrangements is that a country may be a member of regional groupings with conflicting means to achieve sometimes similar objectives. An example is the large number of ECOWAS member states also belonging to UEMOA[4]. This is interesting, considering the perception that the latter grouping was derived from CEAO which itself came out of UDEAO, the former customs union of francophone West African states, established in 1973 with French support to counter what was seen to be a growing Nigerian influence in the sub-region (McCarthy, 1996). UEMOA is seen to pose a challenge to ECOWAS, in view of the cohesive nature of the former as an organisation originally intended to counter Nigeria's domination of ECOWAS, and also in view of the convertibility of its currency in a sub-region of highly inconvertible currencies.

The membership of the Common Monetary Area (CMA) in Southern Africa closely overlaps with that of SACU, except for the absence of Botswana from the former. The CMA operates under the Multilateral Monetary Agreement (MMA) which is supported by bilateral arrangements between South Africa and its partners. The implication is that within COMESA and SADC there are forms of integration that are more important to some members.

Problems could arise for parallel membership of several groupings with similar objectives. There is certainly the issue of replication of effort. An example in this case is SADC and COMESA. As McCarthy (1996) observes: "It is difficult to envisage how SADC and COMESA, given their convergence to both sectoral cooperation and trade integration, can live and prosper with the overlapping membership of the Southern African countries. Restructuring seems inevitable if institutional rivalry between COMESA and SADC and malaise in integration are to be contained". The effectiveness of one grouping tends to be undermined by the existence of the other as limited financial resources cannot meet all requirements, and technical expertise in a poor region is stretched to the limit. The overlapping membership and the strain this puts on financial resources can explain some of the difficulty of the Economic Community of Central African States in meeting its objectives.

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4 Benin, Burkina Faso, Côte d'Ivoire, Mali, Niger, Senegal and Togo belong to both UEMOA and ECOWAS.

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Poor Private Sector Participation

Another feature of integration in Africa is the lack of active involvement of the private sector in the formulation of decisions, protocols etc. This is largely because most of the regimes at the time the agreements were ratified, were statist in outlook. Domestic economic policy did not actively encourage private enterprise. Second, the integration arrangements were negotiated among leaders of regimes that were in most cases not democracies. There were limited and non-transparent channels through which the opinions of the general public or groups could be legitimately made known to the authorities. There was a failure to pass down to the relevant national agencies decisions made at the various conferences and meetings. The result was often a lack of sufficient knowledge about some of the provisions of treaties by both the private sector and national agencies whose activities should have been affected by the decisions made at the heads of state and ministerial levels. This might explain why there is often an unwillingness by the private sector to invest time and resources to participate in the trade liberalisation programmes.

Absence of Strong Supra-National Institutions

The concept of supra-nationality has often not been adopted in African integration, even though the Abuja Treaty sought to tackle that problem. The regional institutions in existence do not have the legal backing to implement or enforce treaties and protocols. The ECOWAS secretariat, for example, has few powers to force governments to implement trade liberalisation measures. The result is a lack of transparency in the implementation of the treaties. The lack of supra-nationality allows the progress of the integration process (or lack of it) to be captured by vested interests. If private economic agents have a complaint regarding the operation of a protocol or article of agreement, for example, this has to be made to a national government body which probably sanctioned the policy that contravened the treaty.

Inadequate Sanctioning Authority

Related to the absence of credible supra-national institutions is the fact that the treaties often do not have effective sanctions against member countries pursuing policies which conflict with the articles of agreement. It may be however, that even where the penalties are spelt out (as in the case of the revised ECOWAS treaty) the cost of non-implementation of the treaty may be perceived to be less than the benefits of doing so. This

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perception by member countries is more likely if most members of the union are not implementing the articles of agreement.

Non-Implementation of Harmonisation Provisions

Evaluations of the economic integration process in Europe conclude that the removal of trade barriers is not sufficient for the formation of regional markets. What is also required are positive integration policies, i.e. the development of institutions to expand and integrate markets (Atkinson and Olenson, 1994). This does not appear to have made much impression in Africa. The problem with, and a major feature of African integration efforts, is that very limited progress has been made in the implementation of integration policies, in particular the harmonisation of tariff codes and classifications. The main reason for this is the unwillingness to make regional objectives the priority. The import-substitution development strategy pursued by most of these countries in the sixties and seventies was incompatible with the limited trade liberalisation which these treaties envisaged. An example of the national objective of import-substitution hampering the effective implementation of trade liberalisation was the operation of the *Taxe Unique* within UDEAC. Under the *taxe unique* products from the region should be subject to the same tax rate irrespective of their source. However, because of the import-substitution objectives of various countries, discriminatory tariffs were imposed which often varied by product and by firm for various countries in the grouping. Obviously, the national perspectives of trade policies were at odds with the requirements of regional integration.

For quite a number of African countries trade policy was a macroeconomic policy instrument acting as a substitute for necessary exchange rate adjustments. The active use of trade policy instruments as macroeconomic tools is incompatible with regional integration which requires stability of trade policy instruments in order to encourage cross-border investments and trade, the harmonisation of tariff codes and the reduction of quantitative import restrictions.

In addition to the failure to implement policies to encourage the exploitation of the existing potential for trade integration, the harmonisation of agricultural, industrial, energy, fiscal and monetary policies which have been envisaged in some treaties and the Lagos Plan of Action, has also not taken place. For example, a decision was taken within ECOWAS to harmonise agricultural policies and adopt a common position during negotiations of international commodity agreements. This decision has not been implemented. On the other hand, while the Community's Protocol on the Free Movement of Persons, Residence and Establishment has been imple-

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mented, it is contravened when it suits the interests of member countries. An objective of the UDEAC is to remove barriers to the circulation of factors of production particularly within the industrial and transportation sectors. Unfortunately there is no regional investment code, and there is a bias in the national codes towards the host country (Tiagha, 1996).

The result of the failure to make any headway in implementing treaty provisions is the continued existence of various factors identified by Mistry (1995) as non-tariff barriers to realising the gains from integration. In a study of Ghana's trading relationship with other ECOWAS states,[5] among other things, it has been concluded that "a wide range of barriers makes even this low level of regional trade difficult to achieve and frequently uncompetitive. Market knowledge is inadequate and accurate tariff and technical data is hard to obtain. Trade finance is poorly developed and expensive. Language differences, harassment at borders and road-blocks discourage many entrepreneurs and add to the costs. The ECOWAS secretariat has few powers to force governments to implement trade liberalisation measures. Ten different currencies are in use, but most are not accepted in international trade, and the West African Clearing House is unable to prevent serious delays in settling payments between some member states". A similar assessment is made by Ariyo and Raheem (1991) in a comprehensive analysis of ECOWAS intra-regional trade.

In general, most integration arrangements are constrained by the inconvertibility of member currencies; lack of adequate and cheap transport and communication links between partner countries; differences in national product or service regulations and standards in transport, health and safety; difficulties in establishing letters of credit; border controls and lack of information within partner countries about the existence of potential buyers and sellers in other partner countries. These constraints apply with varying intensity to the different integration units. For example, the members of the UEMOA are not hampered by problems of currency inconvertibility in their intra-regional trade as are the non-francophone members of ECOWAS. The PTA tried to address the issue of currency inconvertibility and the difficulties of undertaking intra-regional financial transactions with the establishment of the Trade and Development Bank for Eastern and Southern Africa, the PTA clearing house and PTA travellers cheques.

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5 CTA Economic and Export Analysts Ltd., *The ECOWAS Trade Liberalisation Scheme*, Draft Study Report for the Ministry of Trade and Tourism, Ghana, September 1992, p. 14.

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Lack of Political Commitment

Lack of political commitment towards the treaties which have been signed is an important explanation for the failure to implement treaty provisions. Diversity in political ideologies and external alliances are important in this regard. Shaw (1990, p. 133) observes that "the basic issue confronting regionalism in Africa is ... compatibility with established political economies and ruling classes. And when these are outward-oriented towards extra-continental integration, intra-continental connections remain undeveloped and unimportant." The formation of CEAO at the same time that ECOWAS was being negotiated, is an example of such a concern, as is the evolution of CEAO into UEMOA and the increasing importance of France in the new regional arrangement. The result of such alliances is that "regional leaders are either disinterested or diverted" (Shaw, 1990, p. 130). They would adopt integration approaches that allow them to preserve their national interests completely.

Unclear Perceptions about Gains

Lack of political commitment also derives from concerns about the gains from integration, the sentiments expressed in the treaties notwithstanding. Unwillingness to 'give up' some sovereignty has been frequently suggested as a reason for the lack of political will (McCarthy, 1996). This cannot be divorced from the concerns about material benefits. For each member country, the objective is to achieve net gains from integration or cooperation. A certain amount of sovereignty will be given up only if there are tangible benefits to be obtained in return. The plethora of integration and cooperation units may be indicative of the search by individual countries to create that grouping which will best serve its interests. The end result, however, is a large number of groupings, none of which can be described as a success.

Inequalities in the Distribution of the Gains from Integration

Yet another major feature of African integration attempts is the fact that the distribution of the gains is hardly adequately addressed in treaties. This is an important factor in explaining the lack of political will and implementation, considering that most African integration arrangements are made up of countries with varying levels of economic development. The emphasis on trade integration means that gains from integration will be unevenly distributed. Equity issues have to be dealt with effectively at the initial stages of the negotiations.

The inadequacy of distributive measures may stem from a fundamental uncertainty about whether the expected gains from integration will indeed materialise. Countries which perceive themselves to be losers therefore desire to reduce the costs of integration as much as possible and potential gainers are unwilling to concede a great deal in case there is not much to distribute. Once the treaties have been ratified, member countries act in various ways to reduce the costs of integration. An example of such a response to the failure to have an adequate compensatory mechanism was the operation of the *taxe unique* (TU) system of UDEAC. According to Decaluwe, Njinkeu and Bela (1995, p. 18), "The TU rates have been fixed so as to limit the trade flow that could grant gains to some countries at the expense of others. The TU, ... is a compromise between strictly national interests and the regional interest. It reduces sacrifices due to integration, in the absence of an appropriate mechanism that could lead to a fair distribution of gains."

Inadequate Compensation Mechanisms

The issue of compensation and the failure of the compensation mechanism to address these concerns was important in explaining the collapse of the East African Community (McCarthy, 1996). Within ECOWAS, even if a free trade area was created, it is unlikely that intra-regional trade will increase dramatically because of the clauses introduced to safeguard the interests of the weaker countries and reduce the cost of integration. Under Article 39 of the revised treaty, trade deflection occurs when "imports of any particular product by a Member state from another Member state increase (i) as a result of the reduction or elimination of duties and charges on that product ..." and "this increase in imports causes or could cause serious injury to production ...". It is expected that as trade barriers are eliminated between member countries, exports will increase from those countries which have a competitive edge in a particular industry and contract in countries which do not. The requirement that the Council of Ministers "... take such decisions as are necessary in order to deal with the causes of this deflection," seems to go against the objective of strengthening region-wide economic relations. Article 39 of the revised ECOWAS treaty makes the occurrence of gains from specialisation and improved efficiency through resource allocation difficult. Also, nowhere in the Treaty is "serious injury" defined.

The compensation mechanism provided for within the Protocol appended to the ECOWAS treaty is a further disincentive towards intra-regional trade. The exporting country is required to pay compensation equal to the "difference between the total duties that would result from the

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application to commodities, duties ... applicable to such commodities before the coming into force of the Treaty if they originated from a third country enjoying most favoured nation treatment and the amount actually collected as a result of the application of the treaty." This clause in the Protocol on Compensation introduces some rigidity into the treaty and again creates a disincentive to exporting within the region. It is not clear how the expected revenues are to be calculated. It also assumes that the structure of revenues cannot be changed. This can create a distortion in the exporting country if in order to finance these payments it raises domestic taxes. The dependence of most African treasuries on trade taxes and the fear that these may be reduced if trade integration programmes are implemented might explain the lack of speed in reducing tariff barriers and, in particular, the compensatory mechanism of ECOWAS.

The experience of some African countries, however (for example, Ghana), shows that there can be reduced dependence on trade taxes as a source of revenue (without total revenues declining) within the context of unilateral trade liberalisation supported by compensating exchange rate adjustments and tax reform measures which tap the potential tax base more effectively. It may be deduced from this then that regional trade liberalisation need not necessarily result in a decline in total revenues.

Stringent Trade Liberalisation Schemes

The desire to reduce the costs of regional trade liberalisation on member countries has resulted in very stringent programmes of trade liberalisation. Even though the domestic manufacturing base is small, such stringent liberalisation schemes constrain further the proportion of output that can actually be exported to regional markets under the scheme. The stringent rules of origin which limit participation based on value added and ownership of enterprises reduce the potential number of participants in the trade liberalisation scheme.

IV The Achievements of African Regional Integration Efforts

Customs union theory suggests that the success of regional integration schemes could be measured by the share of intra-regional trade in total trade. Increases generally imply success while decreases mean failure. This sometimes needs to be qualified, however, when increasing intra-regional trade may reflect a loss in world market positions. Thus, increases in intra-regional trade must be accompanied by increasing relative weight of the region in world trade (Mansoor and Inotai, 1991). Making this qualification, we note that for almost all the regional groupings, there has been no

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significant increase in intra-regional trade (Table 2).[6] Regional integration in Africa so far cannot be described as a success.

Table 2 Intra-Regional Trade as a Percentage of Total Exports of Regional Group

	1970	1980	1985	1990	1992
AMU	1.4	0.3	1.0	2.3	3.0
UDEAC	4.9	1.8	1.9	2.4	2.1
ECCAS	2.4	1.6	2.1	2.3	2.1
ECOWAS	2.9	10.1	5.2	8.3	7.8
CEAO	6.6	9.8	8.3	9.9	10.5
Mano River Union	0.2	0.8	0.4	0.3	0.0
Economic Community of the Great Lakes	0.4	0.4	0.2	0.8	0.3
PTA (COMESA)	9.6	12.1	5.6	6.6	6.7
SADC	5.2	5.1	4.8	5.2	4.4

Source: UNCTAD (1993), *Handbook of International Trade and Development Statistics*, Geneva.

The empirical evidence on the causal link between creation of regional integration units and intra-regional trade is ambiguous. Foroutan and Pritchett's (1993, p. 96) study of intra-African trade finds that trade levels are "actually higher than expected on the basis of the underlying determinants". The study finds that the CEAO does have a statistically significant impact on intra-regional trade, while ECOWAS does not. Ogunkola's study on intra-ECOWAS trade, on the other hand, finds that economic integration has had a positive but small impact on trade within the region (cited in Jebuni, Ogunkola and Soludo, 1994). Kasekende and Ng'eno (1995) estimated that there was a potential for more intra-PTA trade than already existed. Their conclusion is supported by Lyakurwa in his contribution to this book. Lyakurwa finds that in addition to COMESA, there is a significant potential for intra-regional trade within SADC and ECOWAS.

Also, hardly any progress has been made in regional cooperation towards infrastructural development. Indeed, in his contribution to this book, Robinson has noted that "despite its 'win-win' characteristics, the level of regional cooperation in infrastructure and natural resources in the past has been disappointingly low." In the area of energy supply there are

6 A substantial amount of unofficial intra-regional trade does occur. Most of this, however, is in response to the failure to harmonise monetary, fiscal and exchange rate policies.

very few intra-regional supply arrangements, even though as Robinson convincingly argues, the potential for intra-regional grid connections exist at non-prohibitive costs. The potential exists to cooperate in the areas of water and transport with benefits for all parties involved. The absence of appropriate infrastructure remains one of the biggest obstacles to effective regional cooperation, as will be seen shortly.

Aside from there being very little growth in intra-regional trade, for a number of the regional arrangements their creation has had very little impact on economic performance. This is to be expected given the implementation lapses already discussed. In most instances there has been little or no structural change in the regional economy.[7] It was expected that intra-regional trade would be an important stimulus in this direction. However, the skewed production base of African economies towards primary products and a limited range of consumer goods reduces the potential for intra-regional trade. In ECOWAS, for example, manufactures dominate the imports of member countries accounting for approximately 70% of the total, but most member countries have a small manufacturing base with little or no inter-industry linkages. The failure to formulate and implement regional industrialisation strategies has meant that several years after the creation of African regional units, these units may be described as "vacuous" in terms of their ability to generate substantial increases in intra-African trade in manufactures. The small manufacturing base in Africa requires that trade integration should be accompanied by production integration to develop the manufacturing base. The emphasis on trade integration without developing and implementing a regional policy for the production base may explain why the benefits of African regional integration efforts have been limited (Mistry, 1995, p. 36).

V Constraints to Effective Integration

The problems outlined above in our discussion of the features of regional cooperation and integration have been summed up and explained by Mistry (1995, p. 32) as follows:

> 'First-generation regional integration arrangements among developing countries failed to raise efficiency because of: (a) relatively low import demand elasticities, (b) relatively large differences in production cost structures vis-à-vis extra-regional sources; (c) widely disparate income levels; (d) divergent rates of industrial development which made

7 An exception is SACU. An assessment of this regional grouping found a shift out of primary activities in Lesotho and Swaziland.

gains from intra-bloc trade uneven; (e) low levels of initial integration by way of infrastructural links or intra-regional trade; (f) similar non-complementary structures of production and resource endowments: (g) inward-oriented, protectionist industrial development policies under which protection was maintained for too long: and (h) divergence and instability in macroeconomic parameters that made domestic adjustment, as well as regional adjustment, uncertain, fragile and burdensome.'

Various analysts have provided long lists of why cooperation and integration have been and would continue to be problematic (Ariyo and Raheem, 1991). Aside from the institutional problems which we have considered at length already, major issues of concern are the macroeconomic policy variations, the differences in infrastructure development approaches and structural adjustment programmes. Mistry and Robinson deal comprehensively with those issues in the papers which are included in this book.

Macroeconomic Instability, Economic Reform (SAP) and Regional Cooperation

We have made the point that countries involved in a number of regional groupings often have different macroeconomic situations that serve as entry points. Fundamentally, however, many of them have suffered from macroeconomic instability in most stages of their economic history – a fact which often compelled them to pursue structural adjustment programmes (SAPs) in the last decade, albeit with varying intensities and scope. It is believed by Mistry that the considerable variation in intensity, sequencing, scope, etc. of SAPs, has a significant negative impact on the outcomes of both the reform process and on the objective of regional cooperation and integration. According to Mistry, "It is astonishing... that while SAPs have become a feature in Africa since 1985, and (regional integration arrangements) have been pursued with renewed vigour especially over the last five years, there has been no serious, systematic attempt by any agency or donor to operationalise effectively ways in which integration and adjustment might be interwoven and made mutually reinforcing".

The outcomes of most structural adjustment programmes have been as inconclusive as the regional integration efforts of various countries. While it is generally true that a considerable number of countries witnessed varying degrees of growth following reform, there are hardly any countries where macroeconomic stability and policy-induced growth have been consistent over the medium-term. The experience of Ghana, probably the largest adjuster in Africa, and often cited for considerable success in adjust-

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ment, suggests that tenaciously adhering to the principles of adjustment will not necessarily lead to unhindered long-term growth. In Ghana, after the initial success in achieving significant GDP and per capita income growth throughout the second half of the 1980s, a trend of low private investment was followed by increasing difficulty in ensuring macroeconomic stability. While macroeconomic policy targets for 1985-91 were relatively easily reached, they became impossible after 1992. Today a large and growing fiscal deficit with inflation over 55% has become a feature of the Ghanaian economy. Other African countries, including Côte d'Ivoire have had similar SAP experiences.

Why do African economies have considerably greater difficulty in achieving macroeconomic stability than other developing regions of the world, particularly East Asia? A recent study by Easterly and Levine (1995), provides some clues to the answers. After analysing the growth performance of various countries in the different regions of the developing world in cross-country growth regressions using standard growth variables for all countries with data, they concluded that explanations for the relatively poor performance of African countries went beyond what the standard variables provided. There was some factor that was unique to Africa, and hence they included such less standard factors as institutional development, wars, infrastructure and ethnic diversity in the core regression model. But these continued to explain only a part of Africa's poor performance, leaving a significant explanation to what may be described as the "contagion effect". In other words, the condition in which one's neighbours are affects one's own growth and development.

Easterly and Levine find that both failure (in Africa) and success (in East Asia) are regionally concentrated. They suggest that spill-overs from a country's neighbours such as low investment or high political instability are likely to affect that country's own growth. To solve the problem created thereby, "the contagion effect says that Africa's lagging growth relative to policy variables will disappear if a sufficient critical mass of countries provide a demonstration effect to change a negative contagion effect to a positive one" (Easterly and Levine, 1995, p.10). There is significant reason to believe that most of the growth recorded by East Asian countries has resulted from considerable proximity advantages provided by the large economies of the region, notably the Japanese.

In the area of macroeconomic policy, two countries in Africa whose varying policies are bound to affect trade between them adversely and hence affect the outcomes of their respective reform programmes have been Côte d'Ivoire and Ghana. While Ghana's reforms have used a flexible exchange rate policy as its bedrock, Côte d'Ivoire has had a, more or less, fixed exchange rate anchored in the French Franc and supported by developments within UEMOA. Structural adjustment in Côte d'Ivoire has been far less comprehensive, precipitating the description of "too little, too late" (Pegatienan, 1995). The rapid real depreciation of the Ghanaian cedi against all major currencies, which is highly correlated with the high inflation level in Ghana (ISSER, 1995) ensures that trade between the two countries remains unattractive, minimal and one-sided, in spite of what is generally perceived as a large potential for expanded trade between the two. The inherent subsidy that the CFA enjoys as a result of its relationship with the French Franc effectively distorts the trading relationship between the two countries. Membership of ECOWAS, with emphasis on tariff reductions, is unlikely to increase trade significantly if exchange rates are not properly aligned and the underlying macroeconomic framework is unstable in both countries.

Mistry has documented in a comprehensive manner the way in which SAPs in various countries are affected by unstable situations or destabilising activities in neighbouring countries. He provides clear examples of how Zambia's open capital account is used as a convenient route for illicit transactions with South African entrepreneurs to arrange capital flight from Zambia (as South African-made goods are exchanged for US dollars available on the open market). He also shows that unstable macroeconomic conditions in one country are likely to affect the implementation and performance of SAPs in others, with respect to such aspects of policy as the budget, monetary and fiscal stability, as well as the stability of the external sector. As a consequence, individual countries are unable to expand production in response to SAPs and therefore unable to take advantage of opportunities created by regional integration attempts. The solution would therefore lie in a regionally-coordinated reform programme that allows small countries to benefit from more stable conditions in larger neighbouring economies.

Infrastructure Development and Regional Integration Arrangements

Following the argument of a contagion effect, it is our view that large countries (such as Nigeria and South Africa) have not had a desirable impact on their neighbours in view of various constraints to the creation of efficient markets for factors and products. Countries have had difficulty in affecting each other positively following physical and other restrictions in the movement of productive resources across borders. The need to develop infrastructures that allow countries to share resources and gain markets is underscored by an FAO (1975) study into food security issues in Africa. The study into the availability and adequacy of agricultural land in Africa and the rest of the developing world suggested that, even employing basic traditional farm implements, lands in the developing world were capable of providing sufficient food to sustain twice their 1975 population and one-and-a-half times their projected Year 2000 population if only massive and unrestricted movement of surplus potential food production and labour within the region existed. With an improved or intermediate level of inputs applied to the cultivable land, these lands would be able to meet the food demands of more than four times the Year 2000 population. The study also showed that if there was no movement of resources, output and labour, 38 per cent of the total land area available to Africa will not be able to produce enough to feed the 1975 population, using traditional inputs. By 1975 only 51% of the total arable land available to Africa was cultivated. Today, less than 60% is cultivated. The conclusion of the study that the appearance of various 'critical areas', in Africa especially, would be the result of a situation of no international movement of resources, output and labour, is of crucial importance to the potential for growth and development in Africa.

Unfortunately, despite the obvious cost advantages in sharing resources, many countries, out of nationalistic inclinations, often choose to develop infrastructures for mobilising resources alone. In his paper, Robinson catalogues comprehensively many schemes developed by various nations and explains the political and economic rationalisations behind the choices that countries have made. He also documents and explains the difficulties that have been experienced in previous attempts to achieve infrastructure development on a cooperative basis in several areas, including the Tazara rail project, Zimbabwean energy project and the River Basin development projects of Central and Western Africa. Obviously, while the political, and sometimes security, rationalisations cannot be discounted, the projects considered show how often they were seen to outweigh all economic advantages that shared facilities are expected to bring in.

Robinson provides us with a number of reasons why cooperative development of infrastructures has not been substantial. An important one is that "the benefits of regional cooperation have not always been quantified and have not been fully understood and appreciated by the governments involved". He points out that the framework of analysis incorporating trade options and implications for future investments is often beyond the grasp of national governments' institutions. The role of nationalism in subverting cooperation in infrastructure development and resource mobilisation is clearly underscored by Robinson. Other reasons for lack of infrastructural cooperation mentioned by Robinson includes the security situation as perceived by individual nations, and the role of donors as they "compete with other for attention" in African countries. Apart from focusing on individual countries most of the time, and hence encouraging separate developments, when they get involved in regional cooperation projects, donors are often seen to change the scope of projects way beyond the expectation of participating nations and institutions, thus making it difficult for countries to effectively match the resources they put into such projects. Robinson provides the example of the Niger Basin Authority to support this argument.

Of course, cooperation in infrastructure and resource development could lead to a realisation of the positive contagion effect that Easterly and Levine (1995) advocated but this would not take place without a clear framework for such development, especially in view of the expected role that the donor community might have to play. Indeed, a direct intervention is called for and this is where multilateral assistance could play a significant and positive role.

Given the shortcomings and problems associated with current integration arrangements what form should African regionalism take in order to exploit the potential gains? We sum below a number of views that have been put forward for overcoming the constraints and maximising the benefits of regional cooperation and integration in Africa.

VI Overcoming the Constraints to Regional Integration: The Future Direction of Regionalism in Africa

Some observers of African integration suggest that African countries should follow the Asian example of an outward oriented trade policy that encourages trade and eventually may result in greater trade integration (Husain, 1992). However, despite the difficulties encountered with formal integration efforts in Africa, developments in the international economy suggest that African countries no longer have the luxury to decide not to participate in and implement cooperation and integration arrangements. Not having formal integration schemes does away with the problems of integration. However the pace of regional integration may be too slow to allow African countries to achieve their growth and development aspirations in the rapidly changing world economy. Africa needs to encourage investment by local entrepreneurs, and be able to attract foreign investment and technology. "Regional integration may be the most practicable way to minimise the costs of African market fragmentation... It may thus be a precondition for, rather than an obstacle to integrating sub-Saharan Africa more effectively with the world economy" (Robson, 1993, p. 341). Most African countries are pursuing economic reform programmes of the IMF and World Bank. A concern has been that these programmes, although they have the objective of making African economies more outward-oriented, are achieving this at the expense of regional integration.

Mistry argues that the possibilities of success of these reform programmes will be enhanced if they are implemented within a regional context.

Renewed efforts at integration are currently being made with the re-alignment of earlier arrangements. The current trend is to transform regional units (for example COMESA and SADC), that were characterised largely by project coordination and a limited degree of policy harmonisation into regional arrangements which involve closer integration through the gradual replacement of national policy by regional policy.

Proposals for the future direction of African regionalism range from focusing only on project coordination to much broader approaches which require trade and production integration and the creation of an institutional framework. An important question which needs to be raised in an assessment of current developments and proposals for the form of regionalism in the future is the extent to which the issue of poor implementation which has plagued African regionalism in the past is addressed. Future regional arrangements should incorporate measures and mechanisms that adequately deal with the issues of overlapping membership, compensation, and financial and human resource constraints.

A proposal by Foroutan (1992), Langhammer and Hiemenz (1991), and Ravenhill (1985) is that the trade integration approach be avoided. Trade and factor integration are not considered feasible because of the dissimilarity of African economies and the difficulties of putting in place an effective compensation mechanism (Foroutan, 1992). Thus "cooperation, coordination and harmonisation hold greater promise" (Foroutan, 1992 p. 265). Emphasis should be on the provision of infrastructural facilities, and training and research. We observed earlier that Robinson describes regional cooperation in infrastructure investment as a "win-win" aspect of integration because all members benefit irrespective of their size and level of economic development thus avoiding the problems of compensation and loss of some sovereignty.

McCarthy (1996) suggests that regional cooperation for infrastructure development and/or what is described as thematic cooperation, i.e. agreement on cross-border investment, should precede trade integration. This particular sequencing is to be preferred for two reasons. It avoids the problems of distribution of gains and loss of sovereignty. Second, during the period of cooperation on infrastructural projects, the philosophy or culture of regional cooperation will be developed on an incremental basis over time until the critical level of regional awareness has been reached which will then facilitate the implementation of market integration policies.

Mistry provides in his contribution to this book compelling arguments for a much broader approach at integration. He suggests a simultaneous adoption of sectoral investment coordination and cooperation, trade inte-

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gration and the development of an appropriate institutional framework. It will be necessary to improve the operation of the public sector bodies responsible for the development and maintenance of infrastructure. Existing regional banks will have to be re-oriented to address regional issues if they are not already doing so, and sub-regional banks may have to be created. A regional policy environment must be created to allow the gradual integration of markets. This approach differs from the practice of current regional agreements where emphasis is placed on trade integration without addressing adequately the infrastructural and institutional framework which is necessary to facilitate the trade integration process. A problem with this strategy is the constraints of the financial and human capacities of the participating countries. These need not be intractable problems if participating in a regional arrangement can be understood by governments, policy makers and private agents as a re-orientation of the development strategy from a national perspective to a regional one. A regional development strategy may not impose severe constraints on financial resources if it is recognised that a re-allocation of budgetary resources is required in order to avoid replication and therefore waste. Scarce skilled human resources will be more effectively used if they are concentrated in regional institutions rather than in several national ones performing the same function.

The approach suggested by Mistry is not incompatible with yet another proposal for Africa to try to replicate NAFTA, but this time linking up with the European Union (Fine and Yeo, 1994; Collier and Gunning, 1995). Collier and Gunning argue that "The persistent policy question ... is not globalism versus regionalism but unilateral liberalism or Africa-North reciprocal discrimination versus regional reciprocal discrimination" (p. 402). Several advantages are expected to arise from such a union. Collier and Gunning (1995) argue that forming an integration arrangement with the North will generate all the gains from global liberalisation. Second, such a union would enhance the credibility of African trade liberalisation and generate the desired investment inflows (Collier and Gunning, 1994; Robson, 1993). Currently African trade liberalisations may suffer from a credibility problem since private agents have no guarantee against policy reversals. Aid flows are considered inadequate since if these flows should discontinue the policies may be reversed. Integration with the North has effective sanctions incorporated in it which current African regional agreements do not have. The loss of access to Northern markets for example may be an effective means of binding governments to a particular agreed upon policy. The third advantage is that it would ensure Africa's access to European markets at a time when the EU's trading interests lie in Asia and Latin America. Fourth, such a union may import

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institutional arrangements considered desirable by members. If the union does not concentrate only on trade but also incorporates technical assistance for policy reforms and debt relief this may be an effective enticement for those countries worried about the adjustment effects of such a union (Langhammer, 1992). It may also address the issue of the human capacity constraint faced by African countries. The European Union may be willing to consider such an arrangement if it will stem the migrant flow to their economies. The currently created UEMOA is an example of such a regional grouping with France as the Northern partner.

The problem with this form of integration (and recent development in francophone West Africa) is that it is contrary to the concept of self-reliance which is still the objective of some regional arrangements, for example the revised ECOWAS treaty and the Lagos Plan of Action. The problem of self-reliance though is not an intractable one if the formation of such a union does increase the ability of African economies to respond to shocks without external assistance and diversifies their production structures and exports. The success of UEMOA will determine whether other African regional units, in particular ECOWAS, will be willing to consider this type of link with Europe. In the case of ECOWAS the increasing withdrawal of the UEMOA countries may force it to consider this option. The problems with the current ECOWAS trade liberalisation scheme excepted, no firm from Cote d'Ivoire has applied to participate in it. This is unlikely to be because none of the firms are eligible to apply but may be interpreted as indicating that either firms do not consider it worth their effort and/or greater gains are to be made by concentrating on the then CEAO trade integration programme.

The proposal, however, does not address the thorny issue of distribution of gains. Can it be assumed that guaranteed access to the markets of the European Union is adequate compensation for the revenue loss accompanying regional trade liberalisation? The answer is clearly no. The EU is the largest trading partner for most African countries so that duty free entry of goods originating from the EU will have a definite negative impact on trade revenues, and possible negative implications for total revenues in the short run. There is still clearly a role for aid to finance compensatory schemes and support regional infrastructural and industrial projects. However, as noted by Robinson, the aid agencies of donor countries are set up to deal with national governments. In order for donors to make a positive contribution to the regional integration effort organisational changes may have to be made in order to be able to deal effectively with more than one country at the same time. Donors will not introduce these changes if they do not perceive regional arrangements to be permanent.

The Role of External Donors

The proposal of an Africa-North integration arrangement moving beyond the preferential arrangements of the Lomé Convention calls for a relook at the role of bilateral and multilateral donors in the integration process. It argues that assistance through aid flows may not be an adequate means of supporting integration efforts. Aid flows are not adequate to address the credibility issue. This is because, as argued by Robinson, it is not uncommon for there to be cycles of floods and droughts of interest and good offers of financing. A substitution of trade for aid is being recommended here with greater access to Northern markets being proposed to support purely African integration efforts. Will increased market access be a substitute for resources to support industrialisation programmes to build up the manufacturing base of the African economies? Probably not, especially during the early years of the regional arrangement when financial resources will be required to deal with distributive issues.

To facilitate the workings of the comprehensive approach that Mistry has suggested, it would be appropriate for the donor community to reorient the bulk of its project assistance to African countries toward the development of infrastructures that facilitate the movement of goods and services, as well as capital and labour, while easing communications. If 70% of all multilateral assistance was devoted to such investments, leaving mainly bilateral aid and 30% of multilateral project assistance to cater for the social service needs of individual countries, it is highly likely that integration would proceed much faster within the next decade, yielding greater results for all countries.

The Bretton Woods institutions, given their presence in almost every African country, have ample opportunity to make use of the wealth of information they have to put together regional programmes of structural adjustment, as Mistry has suggested. These regional adjustment programmes must address the areas of currency convertibility, fiscal reform, lowering of barriers to entry, trade liberalisation and arrangements to promote credibility. However, the only impetus for the multilateral agencies to tailor their programmes and re-organise their operations to meet regional requirements is if African countries come together in regional groups to negotiate with these institutions.

The Issue of Size of the Regional Unit

It has been suggested that a limiting factor against successful regional cooperation or integration is the size of the units and the diversity of the members (de Melo et al, 1992). The larger the number of members is and

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the greater the economic diversity, (and therefore interests of the members), the more likely it is that problems of implementation will arise. Much as the relevance of the European experience to the African situation is queried, an important lesson from that experience could be that a small number of members to start with, who have a specific goal, may be a way to approach integration efforts. Within Africa, the experience of SADC may be relevant. However, the dissolution of the East African Community which had only 3 members compared to the 16 of ECOWAS and the 22 members of the COMESA suggests that large numbers may be a negative factor in some cases but not in all. It also suggests that what is relevant is not the numbers involved but the ability to form a regional unit made up of a cohesive group of countries which can agree on a limited set of objectives. Rather than have progress on regional integration constrained by the partner least willing to fully implement treaty provisions, Mistry suggests a core group willing to implement a customs union and the existence of "a wider group at the periphery which might constitute itself as a free trade area, and be linked with the former in free trade agreement ..." (Mistry, 1995, p. 42). This concept of variable geometry has been suggested to address the problem of multiple membership of integration units. Thus, for example COMESA could co-exist with SACU (Maasdorp, cited in McCarthy 1996).

VII Conclusion

Whether African regional groupings include a partner from the North or not, it is imperative that trade integration goes hand in hand with a regional industrial policy, the creation of regional institutions and a policy to develop further regional infrastructure to reduce the costs of intra-regional communication thus enhancing the potential for market integration. For this to happen, African governments and the populace must be convinced "... that regionalism can be an effective route to the solution of national problems" (Mistry, 1995, p. 51). There is still a role for the bilateral and multilateral donors to play in Africa's regional integration efforts through the financing of regional infrastructural projects, provision of advise and technical expertise to assist in the strengthening of already existing regional capacities, the development of efficient and effective regional institutions and the provision of financial resources to support compensatory schemes. However the effectiveness of this role depends on Africa's

8 Some such studies already exist (see Robinson's paper in thes volume); but there is a need for more, especially on the dynamic gains of integration.

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ability to create effective regional integration units. The impetus must come from within the African continent. It is unlikely that donors will continue to support regional efforts which it is clear are not working because of lack of implementation and internal commitment to their survival.

The immediate tasks which need to be undertaken in order for African regional integration to become an effective development strategy are first the completion of empirical studies which show that there are gains to be made from cooperation in investment in infrastructure and market integration, and which clearly indicate the opportunity costs of not cooperating.[8] The second is the development of an effective compensatory mechanism to ensure that all countries will receive some of the gains. Third, is the rationalisation of arrangements to reduce replication of efforts and conflicts.

The current political instability on the continent and concerns about internal security, especially in the West African sub-region leave a lot of doubt as to whether the decisive steps in the direction of a more efficient regional integration will be taken in order to guarantee future growth. The variable geometry approach suggested by Mistry (1995) and McCarthy (1996) may be one way to get around this problem. Those countries which are convinced that regional cooperation, however limited, is the best way forward, can move ahead with their integration efforts, and hopefully the stragglers seeing the advantage of such integration efforts will be encouraged to join.

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Comment on "Overview and Summary of Regional Cooperation in Africa," by Ernest Aryeetey and Abena Oduro

Sam K. B. Asante

I found the paper stimulating in the sense that it highlights the fluctuating fortunes of the process of economic integration in Africa. It also tries to address certain crucial and serious issues and to draw attention to various interlocking challenges to the process of regional integration and Africa's development. The paper is well documented and draws on recent literature on the subject. So on the whole, there is much in the paper with which I agree. The few comments that I want to make will focus on certain substantive issues which have not been fully discussed; I will try to complement the paper on those issues.

Reading the introduction, I think it would have been appropriate to highlight more the significance of economic integration, which has for long constituted a key element of Africa's development strategy. The merit of this integration approach has been documented in almost all the landmark studies on African development and is also reflected in all the external or internal guidelines or programmes on Africa. It begins, say from the Lagos Plan of Action and the Final Act of Lagos in 1980, then the United Nations Programme of Action for African Economic Recovery and Development in 1986, and to its successor, the United Nations New Agenda for African Development adopted in 1991, and recently in the Cairo Agenda for Action which was adopted in 1995. All these landmark studies and documents show that African countries are highly interested in this whole idea of economic integration.

So in my view at the very onset, the significance of economic integration should have been brought out more clearly. Meanwhile, only a sparse reference is made to "The formation of an African economic union..." which, according to the authors, "... is still on the Agenda of the Organisation of African Unity (OAU), although the expected date of this creation has had to be postponed." However, there is nothing like an African economic union, as such. I assume the authors were referring to the African Economic Community, that is, the Abuja Treaty which was signed on 3 June 1991 by 48 members of the OAU at the 27th Summit of the organisation, and which entered into force in May 1994.

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Section 2 of the paper presents an interesting debate on the rationale for economic integration in Africa. The authors have highlighted, which is quite true, the smallness of internal markets. But maybe this is not all. It should be stressed that a typical African nation does not only have a small market but also sparse population. In Africa we have nine countries with less than one million people, and thirty five countries with less than ten million people. We only have about five countries with populations of over thirty million. That is Nigeria, Egypt, Ethiopia, South Africa and Zaire. So we have a major problem with this question of sparse population.

Then in addition to that, we have limited infrastructure and, as is rightly pointed out, new and fragile borders and economies which are vulnerable to fluctuating world prices. Because of the continent's fragmentation and poverty, economic cooperation is perhaps more relevant to Africa than any of the developing nations of the world. If we use the conventional indicators of the economic and social well-being, say, per capita income, literacy, calorie intake, mortality and so on, most African countries fall significantly behind Latin American countries and all but a few of the poorest Asian nations. Hence economic integration in Africa has been seen as a means of helping to overcome the disadvantages of small size, low per capita incomes, small population, narrow resource bases and of making it possible that individual countries achieve a higher rate of economic growth and development.

The current discussion of the benefits of regional integration has moved beyond the traditional arguments of trade creation and trade diversion. In fact these were the arguments put forward a long time ago in 1950 by scholars like Jacob Viner and Richard Lipsey, but these arguments about trade creation and trade diversion are relevant only to the industrialised countries, not to us. A number of studies have demonstrated that the situation of developing countries, particularly in Africa, is completely different from the situation in the industrialised countries. So in my view we should not be bothered by this whole question of trade creation and trade diversion.

In Section 3, the paper discusses the features of regional integration in Africa with particular reference to (a) regional integration arrangements in Africa, and (b) aspects of institutional development of regional integration arrangements. The discussion of this section, in my view, is too general and does not always seem to have much relevance to the subject or the region. The reference to the Economic Commission for Africa's involvement in regional integration attempts being "derived from its interest in African industrial future" would appear to be a bit to simplistic and generally not all that accurate. It is true that ECA has been involved in regional integration right from the beginning, but its main commitment has always

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been to promote self-reliant socioeconomic development and to enhance integrated development efforts at the sub-regional level in such areas as trade, transport and communication, and also to encourage African states to engage in forms of technical and economic cooperation among themselves, which will further promote the process of regional cooperation.

On the other hand, I see that the discussion of the main features of regional integration is quite relevant and well presented. It talks about the problem of overlapping membership of economic integration schemes. This is one of the major problems in all the sub-regions, particularly in West Africa. We have as many as forty regional groups, apart from ECOWAS which brings about all of them under its umbrella, that is sixteen countries. In 1990 when the ECOWAS heads of state met in Banjoul, Gambia, it was felt there was a need for rationalisation of the various regional groups in West Africa. But just as we were about to discuss the report on the rationalisation and see to what extent it would be able to have ECOWAS as the only sub-regional grouping, the French-speaking West-African countries came out – clearly supported by France, as France has been doing all the time – saying that they have a common language and wanted to have their own sub-regional community. So again this came out as a disintegrating factor which the French speaking countries have introduced in the West African economic integration process. The same happened with Central Africa. So I agree there is this multiple membership problem.

Another feature which is rightly pointed out in the paper is the poor participation of the private sector in African economic integration. In fact, when it comes to integration in Africa we consider this as a governmental affair. So the private sector is not involved in the drafting of the various protocols and their implementation, and this is quite well put by the two authors.

The lack of commitment of the ruling classes is another important problem. But we have to link this up to the type of approach to integration. In fact, African countries are generally very poor countries, and when you ask for their commitment, you adopt a type of integration approach which compels them to sacrifice the little that they have, before they can derive any benefit from it. It is difficult to get that commitment, and I will come to that later. This question of approach is to me a major problem if we consider the integration process in Africa. Take for example the question of market integration. Here you have to agree to adopt trade liberalisation, which actually means that the countries are going to lose the revenue which they were getting from custom duties; in fact, the majority of the countries depend upon these custom duties as part of the national revenue. So how do you expect countries in Africa to be committed at this stage,

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when they are battling with structural adjustment programmes, battling with debts, battling with civil wars, battling with almost everything? I think that we have to link this lack of commitment to the approach so far adopted by many of the sub-regional communities.

The authors quite rightly talk about the lack of implementation of decisions, acts, protocols and so on. They also point to the important question of equity. The equity problem is one of the main reasons for the downfall of the East African Community. In 1968, because of this Chad withdrew from UDEAC. In 1986, PTA was compelled to come out with a group of consultants to look into the question of equity.

Then the authors talk about this concept of supra-nationality. The Abuja Treaty, which established the African Economic Community, was much concerned with this question of supra-nationality and it was agreed that supra-nationality actually means a situation where an international institution is endowed with powers to take decisions that they are binding, not only on the institutions themselves, but also on all the member states. This was in 1991 and from that time, all the treaties of the regional integration schemes, followed the example of the Abuja Treaty. So when it comes to COMESA, it is the same thing; when they revised the ECOWAS Treaty, it was the same thing. All of these treaties now have the question of supra-nationality reflected in them.

There are certain crucial issues on which the paper is rather silent. For example, nowhere has harmonisation been mentioned as an essential ingredient of integration. Nor is there sufficient attention being paid to the need for a democratic framework as an ingredient of developmental regionalism. Another problem which did not come out clearly in the paper is institutional deficiencies, both at the national level and the sub-regional level. When you go to any African country belonging to a certain regional grouping, you ask yourself, what are the institutions which handle integration issues in this country? Who are the type of people who work on this and what do they see? That institutional integration is actually not a secondary matter at all. And since we do not pay special attention to integration at the national level, obviously we are not going to get integration at the regional level.

Another issue which was not clearly put out in the paper was the meagre financial resources for implementing programmes. Added to this was the poor choice of personnel both qualitatively and quantitatively. And then the lack of participation of interest groups, civil societies, employers' association, trade unions and so on, who were not actually involved. But you have to say that in the final analysis, *man* is both the means and the end; and the best study of the strategy of economic integration, particularly in the 1990s, as we see it, is *man*.

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Besides, attention should be drawn to the recent challenges to integration. The Cross-Border Initiative, what is it about? Is it a major challenge to Africa? We also have the challenge of the emerging trading bloks (particularly the European Union), the impact of the Lomé Convention, the World Bank's mandated structural adjustment programmes, and so on. These issues could have been brought out in the paper.

When is comes to achievement, that is, Section 4, the authors correctly highlight as an important issue of regional integration, the poor record in terms of trade, in terms of policy integration and harmonisation of the various sectors, in terms of infrastructure, of monetary integration, and so on. These are all well brought up in the paper.

There is in Section 5 the constraints to effective integration which does not appear to me to be of relevance. It is focused more or less on the issue of SAPs at a regional level. I do however agree with a good deal of Section 6, the final one of the paper. It seeks to review the several views concerning the path that regional integration in Africa should take. I certainly do not share the views of those who advocate the relevance of the Asian experience to Africa. They say that in the case of Asia, there are no formal institutions which have been adopted. But from what I have said earlier about the rationale for economic integration in Africa, this should really not be considered. On the other hand, I entirely agree with the view which rejects the market integration approach because it is completely inappropriate to the African situation. There is little purpose in liberalising trade when the parties have nothing to exchange. Regional integration, *inter alia*, must create the basis for trade, otherwise market integration will merely be for promoting non-African goods and services. In this case, where are we? Are we then following the colonial pattern? Because if we are talking about integration, we should be in the position to create goals for ourselves and then make it work in terms of infrastructure and in terms of horizontal linkages among the African countries.

I'm not saying that trade is not important. Trade has a role to play in making available products to where demand actually exists. But if supply, that is, production and infrastructure, for transportation of goods do not exist or not at the appropriate level, then trade facilitation mechanisms operate in a vacuum.

One interesting question is whether we should replicate NAFTA, that is African countries joining Europe, and so on. Nobody would actually propose that we in Africa should replicate Mexico by joining the European Union. The Lomé Convention comes out quite clearly that we have got nothing. The record of the Lomé Convention is very poor; if you read the mid-term review of Lomé 4, it comes out clearly that we in Africa have reached a point where we have to reconsider this whole question of the

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Lomé Convention. It has not solved any of our problems. In fact it is making us to be poorer and I am prepared to challenge anybody who feels that we are gaining anything from the Lomé Convention.

So the conclusion to which my comments lead is that although the authors have made a commendable attempt to present the state of the art of regional integration in Africa, there are a few substantive areas which need to be developed to complement the paper. On the whole, an important lesson that one would need to learn from this paper is that if regional integration is to be a basic element of an encompassing development strategy in Africa, then the priority sectors of this strategy ought to be spelt out and mutually developed. For it has become quite evident that perseverance with the present schemes will serve only to undermine the credibility of regional and continental organisations. I am afraid that it will undermine the prospect of a more limited form of regional cooperation, which seems to offer the best hope of circumventing the constraints that Africa faces in pursuing the legitimate goal of greater self-reliance.

Surely, it is high time to rethink strategy towards effective regional integration in Africa and focus attention on the broader aspects of this strategy. Perhaps what we in Africa need to constantly bear in mind is that with the rapid changes taking place in the world – in particular, the emergence of trading bloks, which threaten to marginalise Africa – the sub-regional and regional economic cooperation and integration schemes should be considered as essential keys to a collective self-reliance, self-sustainment, self-improvement, mutual understanding and cooperation, and the joint planning for the future. We in Africa must learn how to use these keys without hesitation and without delay.

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Comment on "Overview and Summary of Regional Cooperation in Africa," by Ernest Aryeetey and Abena Oduro

Gavin Maasdorp

I enjoyed reading the paper by Ernest Aryeetey and am in general agreement with the thrust of his argument. There are some small points on which I might take issue with him, but what I want to do here is to say something about the context in which economic integration schemes in Africa have been formulated and implemented.

Last year I was part of a multinational team from Africa, under the auspices of an independent think-tank, that travelled around Africa, meeting regional organisations and various other institutions, development banks, chambers of commerce, and, in some countries, key government ministries with the aim of evaluating regional organisations. We encountered a great deal of scepticism about regional integration.

Enthusiasm on Paper Only

The context in which regional integration in Africa was originally formulated was in a world very different to the world of today where there is a new global trade order under the World Trade Organisation (WTO). Now, the WTO sets certain limits to what countries can do in regional integration, especially Article XXIV and Part IV of the Agreement.

We also have another development, generally called the globalisation of national economies: the multinational corporations becoming increasingly important and powerful, the information superhighway, electronic media, etc. A lot of people wonder what all this means for the state, for a country. In Australia last year there was quite a debate in one of the major newspapers about what all this meant for Australia: what does the Australian government actually count for in the world as against the MNCs, the big electronic media of people like Rupert Murdoch? These are questions we thought about as we went through Africa.

African integration was formulated in the 1950s and the 1960s in the context of newly won independence and ideas of Pan-African unity. These ideas carried over later into various treaties and plans of action and so on – schemes for developing regional integration in different parts of Africa

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with an ultimate unity at the end, with various dates which have been put back fairly consistently.

What we found on our trip was that there was a great difference between those dreams and the reality, and indeed a lot of the reasons for that have been sketched out by the author of the paper. The dates have been dreams, that's for sure. Aryeetey mentioned that countries don't know why they want integration. In all countries we visited we asked people why they had joined an integration scheme, and there were no really good answers. They joined because there was peer pressure, they felt they had to show solidarity and that sort of thing, and very often they belong to more than one institution which can sometimes lead to contradictions. Political instability was mentioned as a negative factor. There have also been ideological differences, for instance, in the break-up of the old East African community or in the Maghreb Arab Union today.

Another problem has been that integration has been a top-down process. It has been imposed by governments on economies and on sectoral activities: bureaucrats imposing it on operators in different sectors. This is very different to the kind of integration which is emerging in Asia, which is a bottom-up one: it grew from the fact that there was cross-border business on a large scale. One can also look at the European Union, for instance, and see how it grew incrementally, and that of course has been well documented in various sources.

Aryeetey was quite correct in stressing the neglect of the private sector. The private sector is a key factor in integration as has been realised in Asia. The trade statistics he gave are official data but those data do not take into account unrecorded cross-border trade. Nobody knows the extent of that trade, but anecdotally we heard about an enormous presence of cross-border trade in various parts of Africa. I'm sure the authors know only too well what happens in West Africa. We find a lot of that in parts of Southern Africa as well, and there is also quite a bit of movement, for instance, from Zaire right up to Ethiopia. Now, who is doing that trade? It is being done by people in the private sector, and yet the private sector was consistently down-played by governments in the development of integration schemes in contrast with the way in which the Asian countries have approached their move for closer trade links.

Another important point which has been touched on, but perhaps not put quite as directly as this one, is the capacity a country has to participate in a regional integration scheme. This is a very important point which came up time after time in our interviews up and down Africa. There have been a lot of problems: political instability and, very often, lack of political will to implement decisions. One influential person in West Africa said to us: "Integration stops at the pen of the President who signs the Treaty".

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Aryeetey at one stage said something about there being enthusiasm for regional integration but that enthusiasm is on paper only. If one reads all the documents that have come out, all the treaties, all the speeches and so on, there is enthusiasm, but if one looks at what's happened, there is no enthusiasm, and that is a problem. We were given several examples of that. For instance, when the CEAO failed, what happened? Member countries instituted new systems of taxation rather than following the trade liberalisation process of ECOWAS of which they were also members. So what is going on in that part of the world? The ECOWAS Treaty was signed by heads of state in June 1993. They had fixed a time of six months for ratification by all governments. Well, when we were visiting ECOWAS it was two years after that, and only nine countries had actually ratified, so they were way behind schedule.

There are other problems as well. Lack of communication with border officials was a particular complaint in West Africa: border officials are simply not notified about all these agreements and treaties, and hence they don't implement what they're meant to be implementing. There are many security problems, for example, random check points that are set up by the police or the military, completely contrary to regional agreements, and of course when one reaches those check points, one is meant to pay a little bit of "dash". And that has happened, for instance, in parts of Southern Africa as well. So one asks after all this: how relevant is that original vision about African economic integration?

Questions of Younger Technocrats

In our team we were all deeply aware of the history, the sentiments, the political philosophy and so on that gave rise to the movement for African economic integration. But there comes a time when one actually has to challenge views and has to ask oneself: why should there be a continent-wide African economic integration in the future when one is not expecting something like that in Asia, for instance? I read something recently where the author, who was an Asian, said: "Oh well, you know the concept of Asia is simply a concept of cartographers, European cartographers originally. But Asia stretches all the way from the Mediterranean to the Pacific, and one can't expect there to be one Asia in the sense of economic integration".

We certainly encountered, as I mentioned earlier, considerable scepticism about integration. So what does one do about this? That is the important point. One has to look at this country by country and say: what is the capacity of the particular country – given its internal problems, nation building, economic problems and so on – to participate in a regional

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scheme? And this would be very closely related to the concept of variable geometry that has been mentioned in the paper and to the Cross-Border Initiative (CBI) mentioned by Asante. I'm not sure whether I'm interpreting him correctly, but it didn't seem to me that Asante was very enthusiastic about the CBI. But it is an interesting concept because it's a fast-track movement that straddles the boundaries between different regional bodies although a lot of the countries in fact have overlapping membership of COMESA and SADC. It may well be that if this variable geometry concept is taken seriously, the contagion effect could perhaps work positively in that it could spill over from the fast-track countries to the laggards who are not in the particular variable geometry scheme. So that's another issue one needs to look at.

There was a consistent complaint wherever we went when we met regional bodies about the fact that they didn't have teeth: they couldn't do anything to implement the particular treaty or agreement because the member governments had not been prepared to cede sovereignty. Somebody said to us that when there are countries run by dictators, these dictators won't cede sovereignty to anybody, let alone a regional organisation!

I've mentioned the private sector. This must be given scope to do what it was meant to do, and that has not always been the case in African integration schemes. Sectoral cooperation is extremely important. We've heard about constraints to regional integration such as poor transport and telecommunications. Macroeconomic policy convergence is important as well, and that has been spelt out in the paper and also by Asante. For some regional organisations it may well be that their real contribution can be in sectoral cooperation, and macroeconomic policy convergence, rather than in the far thornier area of trade integration.

Then there is another possibility, of course, that has also been mentioned in the paper, namely, North/South integration. There are several instances of that happening in Africa, or possibly happening. And again it challenges the idea of Africa as a single entity. In our discussions in North African countries we were told bluntly that since they trade 70% to 80% with Europe, that is where they are looking, and that sub-Saharan Africa is low on this list of priorities. They may not say so publicly, of course, but we are talking seriously as a group, and we have to take account of reality. Free trade agreements between some of these North African countries and the European Union are being very seriously discussed. For example, there is a proposed Mediterranean Basin free trade area which would take into account North Africa, parts of Western Asia and the southern parts of the European Union.

There are discussions between South Africa and the European Union

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too, of course, and then there is also a proposed Indian Ocean Region Economic Association (although there is no talk at the moment of that being a free trade area). One has to ask whether parts of Africa could benefit from North/South integration (although the Indian Ocean is more a case of South/South integration). If they could, is it really harming the welfare of Africa if they "go for it"? What's the problem if they go for it rather than cling to visions of a single African market?

We found that a lot of the younger technocrats we met in Africa were asking these sorts of questions. They were challenging the basis on which integration schemes had been set up, and the validity of that basis in the age of high technology.

Southern Africa and the Marrakesh Agreement

I want to end up by saying a few things about some developments in Southern Africa at present which seem to run counter to the Marrakesh Agreement. There are a number of bilateral agreements in the region between, for instance, South Africa and countries outside of the Southern African Customs Union. And those bilateral agreements are simply not compatible with Customs Union membership. When a country is a member of a customs union, it is constrained in its ability to enter into trade agreements with third parties, and it is the customs union as a whole which ought to enter into trade agreements, either with third countries or with groups of other countries, or with regional groupings. Now, at the moment there is apparently quite a lot of pressure being brought to bear on South Africa by some countries in the region – Zambia is one but it was also mentioned in the recent SADC communiqué – that SADC countries ought to conclude bilaterals as a matter of urgency with individual SACU countries. This flies in the face of what is allowed in the Marrakesh Agreement. So too do the discussions that have been held between South Africa and the European Union. In fact, those discussions, if they are ultimately going to be about free trade, ought to be between the SACU as such and the European Union.

There is another reason why the move to establish bilateral agreements with South Africa is contrary to the Marrakesh Agreement. And that is that South Africa is treated by the WTO as a developed country, and as a consequence, it is allowed to enter into trade agreements with developing countries on the basis of non-reciprocity. But some special treatment then has to be accorded to all developing countries, not just a sub-group. That is why Lomé, for instance, is simply operating under a waiver until 2000. It received a special waiver because it was challenged by those developing countries which were not part of Lomé and which claimed that it contradicted Article XXIV and Part IV of the GATT. So any country, for instance, Zambia, wanting a free trade agreement with South Africa, would simply have to realise that if it entered into such an agreement, South Africa would have to extend those privileges on a most-favoured-nation basis (which is the cornerstone of the WTO) to all other countries. These are the ways in which we have to think about how we approach regional integration, and how we have to look at the implications of the Marrakesh Agreement. At the time that regional integration schemes in Africa were formulated, many African countries were not members of GATT, the predecessor of the WTO, and they were not constrained. But now in Southern Africa all the countries are members of the WTO, and one has to pay attention to what room for manoeuvre they are allowed.

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Floor Discussion of the Aryeetey Paper

Not surprisingly, the overview and summary nature of Ernest Aryeetey's paper resulted in a wide range of comments on critical issues of African integration such as the problem of multiple membership, the need for private sector involvement and the lack of interest and capacity of both national and regional officials to implement integration agreements. Given the disillusioning experiences with integration efforts in Africa, these issues provoked vivid reactions.

The topic of rationalising regional integration institutions elicited comments from numerous participants who noted the tendency of countries to retain membership in several regional organisations without particularly contributing to the objectives designed by them. Samuel Wangwe, Executive Director of the Economic and Social Research Foundation in Tanzania, pointed out that not only is there a duplication of activity resulting from the existence of multiple integration organisations, but in some cases, certain institutions have even attempted to undermine the activities of other organisations. "More attention needs to be paid to designing institutions which can be complementary to the main agenda of regional integration," he said.

Sam Tulya-Muhika, Chairman of the East African Cooperation Forum, a group which seeks to promote private sector participation in East African integration efforts, welcomed the frank manner in which participants expressed their criticism. "I'd like to say I'm glad there's an attempt to rationalise the regional integration institutions in Africa because at one stage, about twelve years ago, when we were doing research on integration, some of us remember that Benin did not pay salaries to its civil servants for three years. But at the same time Benin was a member of more than twenty regional institutions. So one wondered how it could afford to be an active member of all these." He also alluded to the fact that of the more that 200 regional organisations in Africa, at least 150 are government organisations.

Another vivid example of Africa's poor record in putting in practice its regional integration arrangements was given by Patrick Ncube, a consultant from South Africa. "Most of these integration schemes really are being designed as a means of getting funds from donors, rather than as a conviction that the Africans want to unite themselves. Look at the structure of most of these schemes. There is this meeting of officials which recommends projects to the ministers, and then to the presidents, and then it's endorsed. And, after that, it's given to the donors for financing. I think that this is a major flaw, which means to say that the donors then are going to

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pick and choose what they would like to finance, and at the end of the day, you don't have a programme. At best you have a programme as determined by the donors; this is absolutely at best. At worst, you have a fragmented programme where the donors have picked up what they want, and they've left a mish-mash which you cannot work with."

According to Nigerian economist Uka Ezenwe, part of the blame for Africa's integration failure must be laid, however, with the former colonial powers. "Let me give you the example of ECOWAS. When it was making quite remarkable progress towards West African integration, France came as usual and introduced a totally new body, the Economic Monetary Union of West Africa. This issue of membership rationalisation is very important, and I think it is the best way to make progress with integration efforts.

The other issue is how to put regional integration schemes into practice in terms of production integration and market integration. I think we're talking about the same thing all the time. You cannot have production integration without trade integration or vice-versa. They are different sides of the same coin, and the effort of increasing production is a delicate issue. The trade aspects would normally be handled by the treaties of these various regional organisations, but I would like to stress the crucial importance of this issue of trade integration.

My other concern is the negative influences of extra-African bodies in African integration which up to this point have been straightforward and open. For example, we have had numerous problems in West Africa with French interference. Each time some progress was made, they presented a new scheme, as they did in the case of ECOWAS. I think one way forward is to appeal to other countries to leave Africa alone so that we can attempt to manoeuver on our own."

Edward Tiagha, regional adviser for industry and technology development for the UN Economic Commission for Africa, supported Ezenwe's view and stressed that African countries should focus their attention on improving relations within their own region rather than with the former colonial powers. "Most of the decisions that are taken as far as integration is concerned in Africa, are external to Africa, and they are usually based on the language divide. It is clear in West and Central Africa that whatever the French-speaking Africans decide, the English-speaking Africans try to counteract.

My point is that African countries are not really masters of their own destinies. When it was recognised in the mid-eighties that structural adjustment programmes were a hindrance to regional integration, the Economic Commission for Africa, the ECA, presented a very worthwhile paper called the African Alternative Framework for Structural Adjustment

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Programmes. As usual, the World Bank underplayed this paper, and more importantly, the African countries themselves underplayed this paper. As a result, it took five years for people to recognise that the ECA was talking about the 'human face' of integration and adjustment, and recognition of this was vital if African integration was to be considered. So again, we have no one but ourselves to blame when we set up these organisations and fail to utilise them.

Learning from the experience of NAFTA, I think it would be catastrophic to try to link ourselves to Europe because we've not been able to link ourselves to ourselves. As Dr. Asante and other speakers have mentioned, the Mexican experience should really tell us that you don't integrate for integration's sake. You integrate when you have internal structures which function. If we link up with our traditional colonial powers in order to facilitate our ties, we may find it very disappointing.

What I would propose instead is that we look at integration within Africa itself. Most of our trips to North Africa have proven that many North African countries are indeed willing to consider integration arrangements with sub-Saharan Africa. But probably because of inadequate information and fragmented markets, they've not been able to do it. Instead, they deal with Europe which is closer and has the infrastructure.

We have to identify the critical poles of countries which can serve as an impetus for regional integration in Africa, and we should not dismiss South Africa even though it has just come into the fold. I think South Africa can be used as a strong neighbour to help with integration of the Southern African region and of course, this can then move on to the West African region and the Central African region. I don't think, quite honestly, that we should depend on all the other countries outside of Africa."

Samuel Wangwe disagreed with Tiagha and Ezenwe on this point and suggested that instead of simply rejecting relations with former colonial powers, a fresh look at them should be taken. "I think there is potential for cooperation between the North and the South. Both South/South and the North/South cooperation attempts have performed poorly in the past, so success cannot be the basis for chosing to emphasise one configuration over the other. So why do we continue to examine the prospects for progress with South/South relationships and discard North/South potential out of hand? We should ask whether there are lessons to be learned from the manner in which we have conducted North/South relationships. Can we re-examine the Lomé Convention and ask, 'Is it the form in which we have been participating, or is it the participation *per se* which is wrong?' I don't believe we have answered this question of the form of participation in an entirely satisfactory way.

As we have seen, once a structure or a pattern of trade has been estab-

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lished, it's not easy to change it. If the major trading partner is Europe, we cannot cut it down to minimum within a short period, even if we desired to do so. As a result, the question of how to manage the relationship will arise. Some good examples have already been presented, and I think that these disruptions of our efforts by the North challenge us to decide collectively on how to handle these relations. Instead of looking only South/South, I believe that Africa must decide how to conduct itself in the Africa/North relationship. If we don't face this issue, it will be difficult to counter disruptive influences from the North. I would suggest that the challenge we are now facing is redefining the forms in which we have been relating to the North; we need to be more conscious about it and face it squarely."

Patrick Ncube elaborated on his point that many of the integration schemes were designed primarily to attract donor funding, and argued that donor involvement acted as a limiting mechanism for private sector involvement in regional integration. "How can the private sector enter into a situation where donors and national governments are involved since the funding is meant for the government and not for the private sector, even though this is the entity which should be most involved in integration?"

Although the UN Economic Commission for Africa was reknown for favouring government-led regional integration, Edward Tiagha was now among the first participants to recognise that the private sector should play a crucial role in development.

"As it concerns the role of the private sector, it is clear that the African governments themselves cannot undertake this whole process of regional integration, because it has been proven that they're extremely inefficient to do that. Of course, in the face of the world economic order, the organisation of the world economic order, like the Uruguay Round Agreement and especially the stringent conditions – I'm talking now from the industrial point of view – imposed by the Uruguay Round, such as the ISO 9000, governments must depend on the private sector for efficient production of their goods and services to enhance integration.

This aspect actually was debated in a meeting that was held in Botswana by the Conference of African Ministers of Industry. This conference, for the first time, recognised that the private sector has to be exploited. They told heads of state and governments of Africa that more has to be done to support the private sector in order to facilitate its full involvement in the industrialisation of Africa. Because when we talk about regional integration, we don't want to talk about Africa as a place where goods from outside are stocked, but as a place which produces its own goods.

In Botswana, we also talked about taking measures to support the private sector in organising and mobilising itself to contribute effectively to industrialising our countries, and to also encourage small, medium-scale

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enterprises for high productivity, and to support and strengthen our institutions, and re-establish development institutions."

Lynn Salinger, from Associates for International Resources and Development, combined the themes of the role of the donor and the role of the private sector in her comments. "Countries should not wait for donors to help them invest in regional activities, rather, regional integration will not be successful unless we have a demand-driven, private-sector motivation that requests the activity." Sam Tulya-Muhika followed with a challenge to explore the possibility of organising the private sector to become an informed force which can provide oversight on government and donor activity. "An appropriate and effective division of labour would be as follows: The private sector generates and manages the demand, and the government manages the supply so that the supply is demand-driven to service the private sector." Alieu Jeng, Principal Economist at the African Development Bank, agreed with the need for more private sector involvement. "After all, it is the private sector which produces the goods and services and moves these goods and services across regions for intra- and extra-regional trade."

Colin McCarthy from the Department of Economics at the University of Stellenbosch expanded on the issue of political commitment raised in Aryeety's paper. He agreed with Aryeety that the lack of commitment to regional integration should not be ascribed to an absence of belief. "It is more a problem of reconciling national and regional problems. And if you consider the domestic problems African countries face, it becomes clear that one cannot reasonably expect a government to cede major policy decisions which affect their domestic situation to some kind of supra-national organisation."

Daniel Ndela, a consultant from Zimbabwe, agreed that national policy cannot be ignored when discussing regional integration. "Is regional integration in Africa at the centre of national policy? I doubt it. The centre of national policy is based on the issue of the instability of the macroeconomic regime. When the ministers of finance are designing central government policy, regional integration is a side issue." Jeng suggested that the political will for economic integration can be generated through informed studies which illustrate to politicians that there are benefits to be gained by integration and, indeed, costs to be borne by failing to integrate.

McCarthy also suggested that the linear model used in discussions of integration is not particularly helpful in the case of Africa. "While it serves as a useful descriptive framework, the assumption that Africa will follow a path from customs union, common market to economic union would be misleading and not very helpful in policy formulation." He referred to Francophone Africa where monetary integration exists without trade inte-

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gration as a case which defies the linear logic of the model. Jeng mentioned that the African Development Bank has taken a more practical approach in their study on economic integration. Their work is centered around the concept of regional cooperation which is based on a progression from coordination to harmonisation and eventually to market or economic integration. "We have chosen this approach because our analysis indicates that there are certain sectors that lend themselves, immediately, to coordination of sectoral investments across the region. Transportation, communications, energy and the industrial manufacturing sector are areas where countries can move rather quickly in terms of coordinating their investments in infrastructure on a regional basis."

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II Potential Gains from Infrastructural and Natural Resource Investment Coordination in Africa

Peter B. Robinson

I Introduction

In a continent balkanised into arbitrary nation states, frequently with scant social, geographical or economic coherence, regional integration has always been a key element in African development strategies. The globalisation of the world economy since the mid 1970s, and the consequent profound changes in the nature of production and the requirements of competitiveness, have added further to the need for African countries to coordinate and collaborate. However, with a small number of exceptions, the record of regional cooperation and integration in Africa has been dismal and this constitutes one of the elements in explaining Africa's abysmal performance when compared with other developing regions of the world. For example, in reviewing the period between World Bank assessments of Africa published in 1989, Adam observes that "five years on, the condition of the 540 million people of the sub-continent remains critical: the GDP of the ten per cent of the world's population that live in sub-Saharan Africa (excluding South Africa) was little more than that of Indonesia, a country which was poorer than Nigeria as recently as thirty years ago. By any objective measures of well-being, the region has fared badly over the last decade. The people are poorer, less well educated, less healthy and, arguably, no less vulnerable to the dangers of civil war and insurrection ... for many, conditions are worse than at independence thirty years ago" (Adam, 1995, p. 729).

Given the severity of the problems and the "single country" focus of structural adjustment programmes, many African countries are in fact now pursuing policies antithetical to regional integration. Yet the theoretical arguments, starting from the seminal work by Viner in 1950, clearly indicate that the largest gains from regionalism are to be achieved by pursuing the deepest forms of integration, which necessarily involve trade and investment integration. Once the simple static framework put forward by Viner is replaced with considerations of dynamic gains, there is difficulty in actually enumerating the gains which are of even greater significance in

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the era of globalisation. Dynamic gains involve the capturing of externalities in areas such as technology and skill acquisition, leading to progressive efficiency gains which are sustained and augmented by incremental investment (Mistry, 1995, pp. 15-19).

The requirements for making reasonably complete forms of regional integration work are demanding: the distribution of gains has to be carefully enumerated, compensation mechanisms established to make the distribution equitable and a degree of national sovereignty surrendered in order to achieve the necessary harmonisation at the regional level. In the case of Africa, the lack of compensation mechanisms and an unwillingness to surrender sovereignty are two significant components of the failure of past regional integration efforts in the continent (Aryeetey and Oduro, 1996).

By contrast, regional cooperation in infrastructure and natural resources is far less demanding. Typically, there are clear gains for all the countries involved in regional cooperation in infrastructure, irrespective of their size and level of economic development. There may be need to share costs and set tariffs to achieve an equitable distribution of gains, but the thorny issues of devising explicit compensation mechanisms and the need to surrender sovereignty do not arise. Yet the record of regional cooperation in Africa is not much more encouraging than performance in more ambitious schemes of integration. One of the aims of the paper is to try to explain why this is so and to analyse whether current political and economic trends provide any reason for greater optimism about regional cooperation for the future.

A related theme in the paper is that regional cooperation is attractive as a complementary strategy to deeper forms of integration rather than as a rival approach. In contrast, in some of the literature offering taxonomies of different forms of regionalism, regional cooperation is categorised as a distinct option[1] to be compared with a number of other specific alternatives. This leads to conclusions being drawn such as the following by Foroutan of the World Bank: "It appears unlikely that complete trade and factor market integration is any more feasible today or in the near future than it has been in the past for all of the existing regional (African) groupings ... Cooperation, coordination and harmonisation hold greater promise." (Foroutan, 1992, p. 30).

While supporting the view that regional cooperation has greater immediate potential, the aspects of cooperation feeding directly into integration should be capitalised on, such as improved communication and transport

1 For example, the *neo-functional model* identified by Oden (1995), page 8.

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facilitating greater regional trade, and exports of energy, water and services providing a direct increment to regional trade flows. Indeed, in many specific settings on the continent, regional cooperation may be a prerequisite for trade expansion. Regional cooperation is equally valid as a strategy whether the ultimate objective is integration into the world economy, as assumed in orthodox theory and promoted by the World Bank, or a self-reliant form of regional integration, justified in terms of dynamic gains and advocated in initiatives such as the Lagos Plan of Action.[2] If regional cooperation is a building block, it is important that the process is managed efficiently, so that success in cooperating in infrastructure and natural resources feeds into the growth of a constituency in favour of deeper forms of integration.

The next section identifies the specific sources of potential gains of regional cooperation in infrastructure and natural resource development from a theoretical viewpoint. Section Three documents specific experience in the past and discusses, in general terms, prospects for the future. In Section Four, prospects in specific sectors are analysed in more detail. In Section Five, the important and increasingly related questions of institutional arrangements for and financing of regional projects and programmes is considered. Finally, there are some concluding comments in Section Six.

II Potential Gains from Regional Cooperation in Infrastructure and Natural Resource Development

Contribution to Economic Growth

Regional cooperation in infrastructure has the potential for making a positive contribution to the economic growth of each of the countries involved. There are a number of mechanisms through which economic growth may be augmented by cooperation in infrastructure:

Direct Cost Reductions

Regional cooperation in infrastructure can lead to a reduction in capital or operating costs or both. Direct reductions in costs arise when there are economies of scale in infrastructure provision or possibilities of improving

2 The Bank is in favour of regional integration only if it is an intermediate stage towards general liberalisation. See Keet (1994) for a comparison of the Bank's regional integration agenda with that of some groups of African countries.

the reliability of supply through using shared facilities rather than investing in spare capacity.

Significant economies of scale are characteristic of several infrastructural sectors such as electricity generation, oil refining, water storage, transport of bulk commodities, maintenance of transport equipment such as locomotives and aircraft and telecommunication interconnections between countries in the region and the outside world. There is scope for increasing reliability of supply through sharing spare capacity in a number of infrastructural sectors including electricity generation (sharing "spinning reserve"), water supply (reducing vulnerability to drought through developing a number of different catchments) and provision of services in transport or telecommunications (sharing equipment to meet contingencies, and providing alternative routes in the event of problems arising on normally used corridors).

Reduced Opportunity Cost of Unserved Demand

The cost reduction viewpoint implicitly assumes a level of demand that has to be met at a specified level of reliability. However, financial constraints are such in many African countries that necessary infrastructure projects are not undertaken, reliability is greatly reduced, supply falls short of demand and market allocation mechanisms are often replaced by rationing which inevitably prejudices efficiency and frequently also equity. Where regional cooperation makes it possible to overcome financial constraints and supply is increased, the contribution to economic growth arises from a reduction in the opportunity costs associated with unmet demand.

In situations where, for example, investment is inhibited by lack of access to electricity, water, transport or telecommunications facilities, the opportunity cost associated with unmet demand can be high.[3] Less important economically, but more visible, are the opportunity costs arising from unreliable supplies. These tend to be much higher in some sub-sectors than in others. For example, an electricity shut-down for certain batch chemical or metallurgical processes which result in the loss of raw materials and the loss of production time is extremely costly. In the transport sector, a clothing firm exporting by air may not be penalised for a day's delay, whereas the horticultural exporter may lose an entire consignment.

3 ZESA, the Zimbabwe Electricity Supply Authority, estimates the opportunity cost for the economy of unmet demand at US$1/kWh. This compares with the current unit cost, including finance charges, of around US$0.04/kWh.

The reaction of private sector agents to unreliability is often to replicate public supply investments with private investments which are very inefficient from the national viewpoint. Not only are such investments a duplication of supply capacity, but the unit costs are typically quite high because of the loss of economies of scale. In the case of water supplies, for example, small dams lose a higher proportion of storage to evaporation than a large dam. In the electricity sector, the purchase of standby generators would typically be more expensive in terms of capital costs than large power stations, and for countries with hydro and coal resources, unit running costs would also be much higher. In transport, once fleets of private trucks have been acquired to overcome problems of unreliability in the public rail service, road transport tends to supplant rail on a permanent basis, making the public rail company less viable and thus progressively less able to provide a competitive service. All of these factors have a negative effect on national economic performance.[4]

Additional Supply Through Conjunctive System Operation

Through joint operation of an infrastructural supply system, it may be possible to derive a higher level of output, at no extra cost, than could be achieved from operating system components in an individual fashion. This is known as conjunctive operation.

For example, if one reservoir were spilling while the water level in another reservoir on an interconnected system was low, conjunctive operation would allow generation at the spilling reservoir to be increased while electricity production at the other is reduced, thereby effectively transferring water and storing energy for subsequent use. More subtle conjunctive possibilities arise on such systems even when dams are not spilling. Although less often exploited in practice, conjunctive possibilities also exist in other infrastructural areas including water supply and transport.

Positive Impact on Trade

Economic growth can also be stimulated through regional trade expansion by cooperation in infrastructure. This occurs through two main mechanisms. The first arises from recognising that payments associated with shared infrastructure themselves constitute trade in goods or services

4 In Nigeria it is the rule, rather than the exception, for companies to supply their own electricity, transport and communications, and also where possible water. See *The Costs of Infrastructure Deficiencies: The Nigerian Experience*, Box 1.2, in World Bank (1989).

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for the countries involved, and that payments made for infrastructural items may lead to a general increase in trade, particularly where trade was previously inhibited by foreign exchange shortages.

The second mechanism for regional trade stimulation is more closely connected with the type of infrastructure involved: improvements such as better road and rail transport and telecommunications facilitate greater exchange of goods and services between neighbouring countries.

The trade benefits may arise from a stimulus being given to trade with third parties. This is the specific intention of some specific forms of cooperation, such as regional tourism initiatives targeted at an overseas clientele. But even in cases where the direct effect is an increase in trade between only one of the regional countries and the rest of the world, there may still be second-round trade benefits for other regional countries as increasing incomes result in higher demand for regional as well as international products.

The country that is a net importer of infrastructural services may well end up being better off as a result of the stimulating effect on overall trade than it would have been under a more inward-looking infrastructural strategy. This point is frequently overlooked by those advocating self-reliance in sectors such as energy.

Savings When Infrastructural Investments are "Lumpy"

In many areas of infrastructural investment, economies of scale can be achieved through making large investments. A sizeable dam for hydro-electricity generation provides a good example. The planning problem is that such investments have to be scheduled well in advance of commissioning, over ten years in the case of a large dam, and the project justification has therefore to be based on long-term demand forecasts. When considering the fortunes of a single country operating in isolation, the economic costs of getting the demand forecasts wrong can be very high.

This applies whether the out-turn is higher or lower than forecast. In the hydro-electricity example, if demand rises faster than projected, there is likely to be shortfall in supply before the new dam is commissioned. The economic cost is the production lost as a result of shortages in electricity and/or welfare losses if the shortages are made to affect households rather than enterprises. If, on the other hand, demand rises more slowly than projected, but the investment is nonetheless made, the project will become non-viable as there will not be sufficient revenue to service project loans. The economic cost in a small country of an unnecessary, large infrastructural project is the "crowding out" effect as development capital and foreign currency is expended on the one big project at the expense of a

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diverse range of activities in the productive sectors. Whether via a shortage of inputs such as electricity or of access to capital and foreign exchange, it is not only in the short term that the level of activity and of investment might be adversely affected: such economic problems could well affect investor perceptions and thereby have a dampening effect on economic growth over a much longer time period.

Given the impossibility of making accurate demand forecasts over long periods, costs arising from infrastructural investment planning in an isolated economy are virtually inevitable. However, through regional cooperation involving trade in commodities such as electricity, there is potential for these costs to be greatly reduced, if not eliminated altogether. Once there are options for imports and exports of electricity, the timing of major supply augmentation projects is no longer quite so crucial because shortfalls prior to commissioning can be covered by imports, while excess capacity after commissioning can be profitably exploited by exporting. As a large economies-of-scale project is being assumed, an initial excess capacity would be anticipated even if demand forecasts were accurate, and the possibility of exports would thus considerably enhance the viability of the project. This, in turn, may lead to increased profitability if the project is implemented earlier than would be the case without the regional dimension. A complementary advantage of bringing the project forward is that the risk of supply shortfalls prior to commissioning would be reduced.

In sum, when investments are "lumpy", infrastructural planning in a single country is likely to result in either oversupply or undersupply, both of which give rise to immediate losses of output and to longer-term negative impacts on investor intentions. The associated economic costs may thus be substantial. Regional cooperation in many cases offers the opportunity to augment economic growth in participating countries through obviating the problems arising from too little or too much investment in infrastructure.

Dynamic Gains

It was mentioned in Section One that dynamic gains, difficult though they are to measure, are thought to be far more important in assessing the benefits of regional trade arrangements than the traditional, more readily quantified static gains. Dynamic gains are also likely to accrue from regional cooperation in infrastructure. In infrastructural systems which operate more efficiently as a result of regional cooperation, technological and managerial skills are acquired by the nationals of the countries involved, and these will spread into other activities in the same sector, or into other sectors, contributing to progressive efficiency gains. Foreign investors participating in regional projects are also more likely to participate in member countries when they have acquired some experience and familiarity with the region.

With the focus shifting from the neo-classical conception of capital and labour as the basic factors of production to the notion of industrialisation and growth being driven by technological capability, the longer-term significance of successful regional cooperation in infrastructure could well exceed the more directly measurable benefits (Lall, 1993). Care should be taken in designing regional infrastructure projects to maximise opportunities for skill acquisition, not just in technological areas but also in managerial and regulatory aspects.

Contribution to Sustainable Development

Increasing the pace of economic growth does not, of course, ensure that broad socio-economic goals will be met. However, as the lack of growth precludes achieving goals such as higher standards of living for the majority of the populace, economic growth is back in vogue as a primary objective, although controversially so to the extent that growth has an adverse effect on the environment. Sustainable development is a more widely endorsed objective, with growth being broadened into "development" and "sustainable" referring partly to political and institutional issues but primarily to the environment.

In the realm of natural resource management and tourism, properly conceived regional cooperation has considerable potential to contribute to sustainable growth. In the global environmental issues, such as carbon dioxide emissions, Africa plays a small part. But in a continent of 50 countries, there is significant sharing of resources such as river basins, lakes, forests, wildlife and coastal environments. Exploitation of these resources by one country very often affects neighbouring countries or even, in the case of major rivers, distant countries. Thus, the scope for exploiting resources for the benefit of all is considerable.

Environmental management in many African countries is tied to tourism which is increasingly important as a source of foreign currency and employment. Africa's natural resource-based tourism potential is immense and at present unevenly developed across the continent. Africa accounts for only 3.4% of world tourism arrivals,[5] and even a small increase in this proportion would have a marked effect on revenues and employment in the sector. Where the primary interest of the high-paying foreign visitors is in

5 African Development Bank (1993), Table 8.1, Volume 3, page 227.

the environment, relatively modest capital investments produce high returns, but only if the natural resource base is preserved. As a result, care must be taken to limit development of tourism to environmentally acceptable limits.

Fortunately, market forces point in that direction. The airfare structure is such that a large proportion of those flying to sub-Saharan African destinations (as opposed to north African destinations) want and are prepared to pay for facilities which blend into the environment and offer a degree of exclusivity. There is less incentive for tourist operators to aim at large-scale tourism at the lower end of the market for which big hotels, far more injurious to the environment, would be required. The regional possibilities are also important in relation to the airfare structure because the tourist sites of several countries may be needed to tip the balance in favour of Africa as a destination.

Through its positive effects on economic growth and more broadly on sustainable development, regional cooperation in infrastructure and natural resource development can contribute momentum to a "virtuous circle" of growth coupled with measures to protect the environment. While this may be partly endogenously driven, the momentum can be increased through the involvement of donors and private financiers eager to support environmentally sound growth. Examples of successful regional cooperation may also contribute to a constituency emerging in favour of deeper forms of integration, including the removal of regional barriers to trade and financial flows. At least in theory, the consequent rising levels of economic prosperity should, in turn, provide the basis for enhanced political sustainability and military security, issues of fundamental concern if regional integration is itself to be sustainable.

III Past and Future Regional Cooperation in Infrastructure

Past Experience

Compensation schemes are often needed to make regional integration acceptable to all the parties involved in trade, investment and financial integration, where difficult-to-quantify gains accrue highly differentially. In Africa, the record of designing and implementing compensation schemes has been particularly weak. In contrast, one of the interesting features of regional cooperation in infrastructure and natural resources is that the gains are typically clearer and tend to accrue to all of the countries involved. Negotiations would still be necessary for items such as the sharing of costs and the structure and levels of tariffs, but the focus is on the distribution of gains rather than on compensation *per se*. Despite this "win-win" characteristic, the level of regional cooperation in infrastructure and natural resources in the past has been disappointingly low. In view of the size of the potential benefits and the political rhetoric in favour of regionalism, an important question is why national approaches have so often been preferred over regional ones.

One reason is that the benefits of regional cooperation have not always been properly quantified and fully understood and appreciated by the governments involved. As is clear from Section Two, direct cost savings may be only one component of the benefits of regional cooperation. To appreciate the full picture requires adopting a wide framework of analysis incorporating trade options and implications for rationalising future investments. This may be difficult to achieve in a government structure where responsibilities are divided and where, typically, responsibility for regional cooperation is weak or diffuse.

More fundamentally, nationalism has had a strong influence in decisions relating to infrastructural development. Following the high degree of *de facto* regional cooperation under colonialism, when countries became independent they sought to go their own way. In areas such as electricity, transport and telecommunications, parastatal supply companies were set up and the strategic nature of such industries was cited as reason for their appropriation of national resources, often without adequate cost recovery being in place. The failure of cooperation efforts such as the East African Community fed into hesitancy to opt for regional projects, despite the higher costs of national solutions. In practice, lack of financial viability of the parastatals led to underinvestment, poor maintenance and operational inefficiency. Inadequate infrastructure became a significant constraint on development in many countries and regions where infrastructural facilities were shared. An example of this is provided by the Dar-es-Salaam and Beira Corridors (see Box 1).

In response to political instability in neighbouring countries, security of supply has often been cited as a reason for pursuing national rather than regional projects. This overlooks the likelihood that part of the reason for instability and, in extreme cases, armed conflict is poor economic performance, and regional cooperation can contribute to reversing this negative spiral. There has been a tendency for self-reliance, the logical concomitant of the nationalist approach, to be confused with security of supply. Zimbabwe's energy policy during the 1980's provides a good example (see Box 2). Similarly, in Tanzania an unacceptably high level of unreliability in the supply of electricity "probably would not have happened if Tanzania had taken a regional approach in energy planning. It has come to be recognised in Tanzania that connecting to the Uganda and Zambia grids could enhance security of power supply" (see Wangwe comment).

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Box 1 Problems Arising From Inefficiency in the Dar and Beira Corridors

The TAZARA railway line linking the Zambian Copperbelt to the port of Dar-es-Salaam, was built in the mid-1970s specifically to enable Zambia to avoid having to rail its major exports and return flows of imports via the hostile regimes in Rhodesia and South Africa. Beira, by contrast, had been linked to its hinterland countries at a much earlier stage (Salisbury, now Harare, in 1900 and Blantyre in 1935), but was closed to Rhodesian traffic when FRELIMO came to power in Mozambique in 1974. The lack of revenues, coupled with inexperienced personnel taking over operations, resulted in a significant deterioration in facilities of the port and the rail system by the time of Zimbabwe's independence in 1980. Through inefficient public management, the Dar Corridor system suffered a similar fate.

For Malawi, Zambia and Zimbabwe, the port systems of Tanzania and Mozambique are closer than other options and should be used for the bulk of overseas cargoes. Yet by the mid-1980s high port charges, lack of shipping options because of low levels of traffic and high implicit costs due to delays and inefficiencies, resulted in the bulk of cargoes being routed through South Africa. In the case of Zambia, for example, despite having its own facilities at the port of Dar 2,150 km away, a significant proportion of copper exports were shipped through East London (2,980 km) and Durban (2,805 km). Malawi was in a much worse position, having to use road and lake transport rather than rail, and the country's bridging costs rose to over 40% of export revenues, compared with an already high figure of about 25% for SADC as a whole. By 1985, Beira was handling less than one-third of the cargoes handled 20 years previously.

Concern was rising in SADC countries at that time about the direct costs of using South African transport routes and, in an atmosphere of rising political tension, the threat of curtailment of transport services if South Africa chose to exert this form of pressure on neighbouring countries. With considerable assistance of external donors, massive rehabilitation programmes for the Dar and Beira Corridor systems were initiated.

A major part of the explanation of the failure of past regional integration attempts lies in the disparities between member countries. The tendency has been for the benefits to accrue disproportionately to the members already somewhat better off than their neighbours. This could have been obviated by establishing an equitable distribution of benefits clearly in advance or, better still, a flexible mechanism to alter the distribution as circumstances change. Disparities between countries also explain why

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Box 2 Zimbabwe's Energy Policy in the 1980s

Under normal circumstances, Zimbabwe imports its main liquid fuels via a pipeline from the port of Beira in Mozambique. An attack by South African saboteurs on the tankfarm at the head of the pipeline in 1982 made Zimbabwe totally dependent on South Africa for fuel imports by rail. The authorities there kept down deliveries to such an extent that by the end of 1982 there was an acute shortage of fuel which almost brought Zimbabwe to a standstill. While the country had no immediate alternative to importing liquid fuels, this incident rekindled interest in enormously expensive oil-from-coal technology and provided the backdrop to a costly policy of self-sufficiency in the electricity sector.

This was embodied in the building of Stage I (480 MW) and Stage II (440 MW) of the Hwange coal-fired power station in preference to building a transmission line from the underutilised Cahora Bassa hydro station in Mozambique and increasing imports of power from Zambia. Because of its sheer size, the Hwange project imposed significant macroeconomic costs on the economy. It has been estimated that, compared with a scenario of delaying the project for 5 years through importing electricity from Mozambique and Zambia, the total economic costs were approximately double the nominal cost of the project. Expensive self-sufficiency did not, however, result in security of supply because of persistent operational difficulties and specific events, including a boiler explosion in 1984 which delayed the commissioning of Stage I and mechanical problems in 1989 which put 260 MW out of commission just when there was a fire at Kafue in Zambia which removed 900 MW from the Zambia-Zimbabwe interconnected grid.

Lack of grid interconnections was a major problem in 1991-92, when the severe drought exposed just how vulnerable the Zambia-Zimbabwe system had become. Since that time, grid interconnection projects with South Africa and Mozambique have gone ahead. Strengthening of the links to Zaire, and other options within the context of the Southern Africa Power Pool, are under active consideration (see Section IV).

many potentially beneficial regional projects have not been implemented at all. projects are stalled 'first, if one of the parties does not have the capacity to contract and service a loan, second, if the same party has (at least in the short term) the capacity and ability to supply services to the deficit country, and third, if it is perceived that the other cooperating country or countries would reap more benefits than the supplying country" (see Ngwenya's comment).

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Box 3 African River Basin Organisations

A recent study by the World Bank (Rangeley et al., 1994 reports on eleven international river basin organisations in sub-Saharan Africa. These vary in scope from those concerned only with water management and environmental issues, to organisations having responsibilities in a range of other activities such as agriculture, energy, transport. fisheries and forestry. While careful to document successes as well as failures, the agenda emerging from the report indicates that the majority of the organisations require extensive revamping if they are to be really effective.

The *Niger Basin Authority* (NBA) is a case in point. It is one the earliest river basin organisations to be formed (1964) and has the largest area of operation (over 1,2 million square kilometres, covering 100 million people). The Niger has highly variable seasonal flows, and is also affected by periodic droughts. About 30 million people live in the arid part of the basin, where continuous degradation of the ecosystem is taking place. The main objectives of the NBA are to raise funds and promote the study and implementation of storage works.

The assessment of the World Bank mission (p. 9) is that "the NBA has been beset by difficulties since its creation. As a result, it has little to show for the considerable sums of money invested in it (about US$30 million, 1993). Some of the main difficulties arise because there are too many member states (nine) and because the objectives have often been diffuse without a clear identification of real beneficial targets. At present, NBA has ceased to be operational and the Hydroniger project is in danger of similar collapse unless urgent action is taken". An in-depth diagnostic study to review the objectives, structure, constitution and programme of the NBA is recommended.

The Hydroniger project is NBA's main activity at present. It involves sixty-five data collection platforms for the measurement and retrieval of real time meteorological data. Even Hydroniger shows "the difficulties of cooperation, as the project almost foundered on the desire of one country to prevent a neighbour knowing what the flows were in its rivers".

The problem of disparities in levels of development is also important in explaining why so many institutions set up to execute programmes of regional cooperation have failed to achieve their objectives. Conditions of service must be established which are at least as good as those of the wealthiest country member, and this may well lead to obstructive problems from officials in national governments. This is exacerbated by the previously mentioned problem of responsibility in governments for regional issues being weak or diffuse. Regional matters are more often handled by political ministries, such as foreign affairs, and the economic significance of regional cooperation opportunities and importance of creating appropriate institutions to exploit them, is not often appreciated. African river-basin organisations provide a good illustration (see Box 3). It is not by chance that the commitment to regionalism is downplayed by politicians and civil servants: national solutions typically offer greater opportunities for rent-seeking behaviour than would be the case in regional projects.

Finally, in documenting the reasons why past regional cooperation has not been as extensive and as effective as might have been expected, the role of donors must be mentioned. As pointed out by Sindiso Ngwenya, the high level of dependence on donor financing for capital and, in recent years, recurrent expenditures is somewhat ironic given the rhetoric of regional cooperation in Africa which emphasises the promotion of self-reliant development (see Ngwenya's comment). In Wangwe's view, this contradiction could be overcome to some extent if recipient countries rose to the challenge of establishing coherent regional programmes, and then inviting donor support (see Wangwe's comment). All too often, however, it has been the other way around with recipient activity fitting into programmes reflecting donor priorities. While donor enthusiasm for regional over national programmes has varied, the high level of resources which have been put into regional efforts has not led to a consistent regional focus in donor activity. Such a focus could have helped reduce the nationalistic tendencies amongst the countries themselves. Most agencies remain clearly structured to deal with national governments rather than with regional organisations. Almost inevitably, therefore, programmes tend to be national rather than regional in character.

Regional programmes may require working with several governments at once and this is difficult and time consuming. It may even be considered inefficient. The World Bank's Operations Evaluation Department reports that "the Bank should not engage in projects with excessively complex managerial arrangements: for example, with two separate utilities involved in a project". Talking of the Great Lakes Region, another Bank document, prepared jointly with the PTA, candidly admits that the six affected countries "are allocated among three divisions of the Bank (AF2, AF3 and AF6), and the problem of cooperation and coordination within the region seem mirrored in Washington" (World Bank, 1990, p. 93).

Another problem which may arise from donor interventions is incompat-

6 Quoted in World Bank/European Commission (1995), page 27.

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ibility of equipment and institutional arrangements when different donors support the same sector in neighbouring countries. When donors do get involved in regional cooperation efforts, cycles of floods and droughts of interest and offers of financing are not uncommon. The Niger Basin Authority again provides a good example: in 1976 a $27.5 million action plan was launched, but this was "stillborn mainly because the enthusiasm of the donors in the mid-1970s built it up to a size that was quite beyond the counterpart implementation capacity of the then Niger Basin Commission or indeed of the member states themselves" (Rangeley et al., 1994, p. 45). In 1981, the pattern was repeated with a $56 million programme being proposed by the donors, $22 million pledged but only a small portion actually materialising as projects.

Future Prospects

With the extensive catalogue of problems outlined in the previous section, is there any reason to suppose that prospects for regional cooperation will be brighter in future?

The first positive factor is the improvement in the security situation in some parts of the continent, in part due to the end of the Cold War. The persistence of old conflicts and emergence of new ones shows, however, that there is no assurance of an end to war and the reaping of a peace dividend. At least in southern Africa the elimination of apartheid and the end to conscious acts of regional destabilisation perpetrated by the former minority government in South Africa has positive implications. While the stance against South Africa forged important elements of cooperation amongst the frontline states, the main expression being the formation of the Southern African Development Coordination Conference (now transformed, with South African membership, into the Southern African Development Community), it also led to states adopting an inward-looking view when it was possible for them to do so. Zimbabwe's electricity supply policy (Box 2) is a case in point. More importantly, as documented in the massive 1993 African Development Bank study on *Economic Integration in Southern Africa*, legitimate government in South Africa has opened up an enormous spectrum of areas of potentially fruitful cooperation.

A second factor relates to the widespread adoption of economic reform programmes which, whatever their immediate effects, do require governments to take resource constraints seriously. The considerable cost savings associated with regional options are thus more likely to attract attention in the current economic climate. Structural adjustment programmes also require parastatals to be more efficient and market-oriented and pave the way for some categories of infrastructural services to be supplied by the

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private sector, offering some prospect of overcoming resource, technology and skill constraints. This could well include private suppliers tackling regional projects through finding ways of working with several governments at once in order to execute schemes of mutual economic benefit to all parties. This is yet to be tried, but in certain areas it could well be that private suppliers may be able to overcome the seemingly intractable problems which characterise present government- and donor-backed regional projects and institutions.

These general factors underpin prospects in specific sectors. Energy, water, transport and telecommunications are considered in some detail in the next section.

IV Sectoral Perspectives

Energy

In terms of the range and size of benefits and the extent of potential linkage, electricity is clearly the most promising infrastructural sub-sector for regional cooperation. Yet, besides a number of relatively minor cross-border supply arrangements, the only effective interconnections currently on the continent are the West African Grid, between Côte d'Ivoire, Ghana, Togo and Benin (2,128 MW) and that between Zambia and Zimbabwe (3,660 MW). This compares with total potential of hydro alone of over 300,000 MW, of which less than 15,000 MW (5%) has already been developed.

The African Development Bank has been taking the lead in exploring options for further grid interconnections at the continental level. In a key study carried out in 1990, it was concluded that "there is not a single region in Africa which, according to this review, cannot benefit from joint power development, and thus share the project costs without denying investment in other productive sectors of the economy. Joint power development is therefore considered a means to aid the recovery of economic performance and reverse the erosion of the continent's productive base and human resources" (AfDB, 1990, p. 56).

The study divided the continent into ten regions and examined the possibilities for strengthening interconnections within and between each region. The epicentre of Africa's electricity generation potential is a remarkable site, Inga on the Zaire River. At that one site, with very limited civil works and negligible direct environmental impact, there is 44,000 MW of hydro-electricity generation potential, more than the present entire installed capacity of South Africa or the rest of the African continent excluding South Africa. At present, only 2,486 MW have been developed, but even this allows exports of power to the Zambia-Zimbabwe integrated grid via a DC transmission line running through Shaba province. The African Development Bank study envisages Inga eventually supplying power both northwards and southwards, and to this end recommends interconnections and strengthening of existing transmission lines to provide key "backbones" across the continent.

The northern backbone would require an interconnection from Zaire to Nigeria, a link from Nigeria to the West African Grid and an extension west into Senegal and Mauritania. One southern backbone already exists via the DC transmission line from Inga, but the linkage to the Zambian grid needs to be upgraded as a first step, and a duplication of the lines considered subsequently. With the completion of the Bulwayo-Mathimba line, the Zambia-Zimbabwe system is now connected to the South African grid via a 500 MW link. A further development would be a second southern backbone from Inga through Angola and Namibia to Cape Town.

On the east coast, the first step is the rehabilitation, now underway, of the 1750 megawatt DC transmission line from outside Pretoria to Cahora Bassa on the Zambezi in Mozambique (533 kilowatt, 1360 km). Connections into Malawi and Tanzania are under consideration, and the east coast backbone would become a reality with links from Tanzania into Kenya, from northern Kenya into Ethiopia and from Ethiopia into Sudan. To make electricity trade between Zaire, the West African Grid and Egypt possible, a cross-continent loop connection would be required which might be routed through the Sudan. The final recommended connection is an inland link from Nigeria/Niger through Mali to Mauritania, taking advantage of hydro resources on the western rivers, providing power to the countries through which it runs and reinforcing the coastal interconnection already discussed.

Work in the SADC region gives an indication of the size of potential benefits likely to accrue from grid interconnections. A study carried out in 1991-92 calculated the capital costs of providing electricity to the year 2010 through strengthening regional interconnections as being $8.6 billion. This was 24% less than the corresponding combined costs of independent country programmes of $11.3 billion.[7] The benefits would be most marked for countries which presently have very high unit costs, for example Tanzania at 11 cents per kilowatt hour as compared with Zambia at less than 3 cents per kilowatt hour because a regional strategy would reduce these wide disparities in costs. Total costs would also be minimised. According to the World Bank, for all of sub-Saharan Africa, electricity

7 Results from SADC Project AAA 3.8, quoted in Chapter 5 of AfDB (1993).

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investment should be over \$4 billion per annum over the next decade, a sum widely felt to be unfeasible. If regional cooperation could reduce these requirements by \$1 billion per annum, it is far more likely that adequate provision of electricity will be possible.

At the time that the SADC interconnector study was carried out, South Africa was still under apartheid and was excluded from the core recommendations. However, the benefits of linking the predominantly thermal system in South Africa with the mainly hydro systems to the north are considerable, a point that came to be widely appreciated in Zambia and Zimbabwe during the load shedding and electricity rationing consequent on the severe drought of 1991-92. For Zimbabwe, the immediate benefit of the recently completed Mathimba link is the restoration of adequate reserves on its system, and hence a considerable improvement in reliability. In the early years of next century, when South Africa's present surplus of generating capacity is expected to be exhausted, the link can be used to export hydroelectricity, either from Batoka if that joint Zambia/Zimbabwe project goes ahead, or from lower Kafue in Zambia or power wheeled from Inga in Zaire. Exports from coal or coal bed methane projects in Zimbabwe or elsewhere are also possible. While the DC line from Cahora Bassa to Johannesburg is being restored, Zimbabwe has negotiated to import power from Cahora Bassa via a 500 MW link to a point near Harare which is due to be completed in 1996.

Particularly for a country like Mozambique, which has limited merchandise exports and large import requirements, exports of electricity (and transport services - see next section) have a crucial role to play in economic recovery. For each 1000 MW at an 80% load factor, the revenues accruing from energy sales would be \$70 million for each 1 cent per kilowatt hour negotiated in the tariff. The indicative figure for energy trade in the region is presently 1.5 cents per kilowatt hour, implying a revenue potential of over \$100 million for each 1000 MW. Cahora Bassa has 2075 MW of installed capacity, implying a revenue potential of over \$200 million per annum, or 33% more than the 1994 level of merchandise exports of the country.

West Africa has similar opportunities for stabilising electricity provision by integrating hydro and thermal systems, and thereby creating considerable opportunities for trade in energy. There are untapped natural gas fields in Angola, Cameroon, Congo, Côte d'Ivoire and Ghana. In Nigeria, the equivalent of 10,000 MW of gas is presently being flared, with significant adverse environmental consequences. The now politically controversial projects to utilise albeit a small proportion of this gas could form the basis of a thermal generation system to counterbalance existing and future hydro capacity. The signing of the West African Pipeline Company (WAPCO)

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agreement, covering the supply of gas from Nigeria to Benin, Ghana and Togo, in September 1995 was the culmination of a process started in the early 1970s, illustrating, in the words of the Executive Secretary of ECOWAS, " the length of time that it takes to finalise projects such as this one".[8] It is significant that the project is to operate purely as a commercial concern with the company being owned by private sector interests. The associated power generation and transmission projects are also likely to be undertaken by private sector interests, although in some cases in partnership with public energy utilities.

As a complement to continental scale electricity grids, there are proposals for a gas pipeline which would link all of the west coast gas resources from Côte d'Ivoire through Namibia to South Africa. The Chief Executive of the Ghana Petroleum Corporation, Tsatsu Tsikata, claims that unit costs of gas in such an extensive trunkline would be attractive, and that "the availability of cheap gas can be a tremendous catalyst for natural resource development".[9] In east and southern Africa, natural gas deposits in Tanzania and Mozambique and coal bed methane associated with many of the coal deposits of the region could be similarly linked, or else used to generate electricity to be fed into the regional grid.

Water

Shared river basins are a common feature in Africa, in part because many major rivers were designated as national boundaries under colonial rule. There are 17 international drainage basins with catchment areas greater than 100,000 square km, and an additional 11 with catchment areas greater than 30,000 square km. The largest of these in terms of discharge are the Zaire River, the Volta, the Zambezi, the Niger-Benue and the Nile.

The development of shared water resources embraces not only hydroelectricity potential, but supply of bulk water for urban, industrial and mining (UIM) use, irrigation, tourism and inland transport. The largest and arguably most successful regional project is the Lesotho Highlands Development Project which involves the construction of dams and tunnels to supply 2,000 million cubic metres per annum of water from the headwaters of the Orange River in Lesotho to the Gauteng area, the urban-industrial heartland of South Africa, and supply electricity from a 166 MW hydro station to Lesotho. The eventual cost of the four phases of the

8 *Africa Review*, November 1995, page 45.
9 Quoted in *Africa Review*, October 1995, page 30.

project is expected to be $7.5 billion, one third of which is to be spent in the first phase currently underway. The advantage to South Africa of the scheme is the avoided cost of pumping the Orange River water from the much lower elevation where it enters South Africa, while for Lesotho, in addition to the hydro-electricity plant, the project offers royalties ($3.5 million per annum), training and employment opportunities and compensation for the negative environmental impacts.

Part of the success of the project to date has been ascribed to the legal agreements and institutional structure which was established for it, although given the David and Goliath status of the two countries involved, the size of the royalties payable by South Africa remains controversial. There is also concern about the longer-term environmental consequences of inter-basin transfers. Once the Lesotho Highlands water is fully utilised, Gauteng would seek other large-scale transfers, from the Zambezi or perhaps the Okavango. Draining the swamps would, however, have a devastating effect on the ecosystem of a unique wilderness area, and it is unlikely that the Botswana government would readily agree.

In contrast to the potential offered by Africa's rivers for hydro-electric generation, the potential in aggregate for irrigation (20 million hectares) is modest in relation to the size of the continent (3,000 million hectares). Irrigation is nonetheless an important component of some regional water development programmes. In a case such as the dams built by the *Organisation pour la Mise en Valeur du Fleuve Senegal* (OMVS), the bulk of the expected benefits have not materialised because the irrigation projects under national rather than regional control have fallen far short of intended targets.

Inter-basin transfers and irrigation are hydrologically significant because they reduce overall catchment flows. Other uses, such as navigation and tourism, are non-consumptive. Except for the lower Niger and Zaire rivers, navigation on rivers has never been commercially important and proposals for the Senegal River have not proved economical. Inter-country transport on inland lakes, such as Victoria, is much more significant. Tourism-related river and lake activities are also common. Fishing is an important activity in major lakes, locally providing employment and income and nationally contributing a vital source of affordable high quality protein. Provided riparian countries cooperate, there is considerable scope for beneficially expanding these activities. For example, data for the land-locked SADC countries indicate that less than 50% of the potential inland fish yield is being harvested. [10]

10 AfDB (1993), Table 4.6, based on FAO data.

Transport

As compared with electricity and water, the potential for and benefits from cooperation in transport are diverse and far more difficult to quantify. For a start, there are usually several different modal and routing options for cargoes or passengers, so a multiplicity of alternatives has to be taken into account. Costs are a function not merely of distance, but of facilities and alternatives available at origin and destination and the efficiency with which traffic is handled. Starting from a position where "the landlocked countries pay up to 90% of CIF (cost, insurance and freight) value of imports as total transport costs of their cargo",[11] the cost savings can be substantial. For example, a 1995 World Bank/EC study of the Great Lakes Corridor suggests that potential savings for the landlocked countries from simple policy changes (improvements in road services and transit trade procedures) would be of the order of $13-30 per tonne, equivalent to between 14% and 33% of typical values of the commodities being carried (World Bank/European Commission, 1995, p. 73).

The above serves to emphasise that for the 15 landlocked countries,[12] regional cooperation in transport is essential for survival. The same can be said for many of their neighbours for whom revenues from transport services provide a crucial component of national income. Yet, as outlined earlier, various forms of inefficiency in the past have limited the effectiveness and economic benefits of regional transport arrangements and there is plenty of scope for benefits to be increased.

COMESA (formerly the PTA) has made a major effort to coordinate the removal of non-physical barriers to transit with the development of the physical infrastructure. Lack of commitment from member states and overlap with other regional organisations has to some extent frustrated these efforts. An example of the latter is the establishment of different Axle Load Limits and Gross Vehicle Mass by the PTA and SADCC, necessitating further studies and negotiations in order to achieve harmonisation.[13]

At the regional level, the Sub-Saharan Africa Transport Programme, which has been running since 1988, has formed the basis for the formulation of subsectoral objectives and strategies for the second UN Decade for

11 USAID (1994), page 132. Another reference quotes the cost of ocean freight in 1987 as 5% of GDP for Mali, 7% of GDP for Burkina Fasso and 3% of GDP for Niger (Creightney, 1993, page 25).

12 Mali, Burkina Faso, Niger, Chad, Central African Republic, Ethiopia - following the independence of Eritrea in 1993, Uganda, Rwanda, Burundi, Malawi, Zambia, Zimbabwe, Botswana, Swaziland and Lesotho.

13 World Bank/European Commission (1995), Annex 2, page 2.

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Transport and Communications in Africa. The emphasis in the programme is on policy and institutional reform, including a gradual opening up to the private sector, and priority being given to repair and maintenance rather than to the building of new capacity.

Maintenance, especially of roads, has emerged as a central issue in the transport sector. The reason is clear: the cost of restoring a damaged road far exceeds what annual maintenance costs should be. For example, a recent European Commission study puts the cost rehabilitation at ECU 26,800 per km for a non-surfaced road and ECU 180,000 per km for a surfaced road, as compared with an annual routine maintenance charge of between ECU 270 and ECU 1340 per km. As of 1993, only 50% of paved roads and less than 30% of unsurfaced roads were said to be in an acceptable condition (European Commission, 1994, p. 11). According to Ngwenya, the persistent underspending on maintenance that this reflects is not due "to budgetary constraints, as conventional wisdom would have us believe, but to the absence of appropriate pricing policies and institutional arrangements" (Ngwenya, 1994, p. 9). The solution lies in a coherent system of user charges and accountable institutions capable of using the funds to good effect, including maximising on opportunities to use local firms and labour intensive construction methods.

In the rail sector, similar issues dominate. For example, at the World Bank/Union of African Railways seminar on *Railway Restructuring* held in Bulawayo in 1992, the main areas of discussion were the policy, institutional, management and operational reforms needed for railways to become efficient and commercial and hence to have the ability to contribute effectively to economic development. In comparison with railways in other parts of the world, African railways have high overheads and low labour productivity. In terms of measurable technical indicators, performance is poor. For example, figures for 11 sub-Saharan railways in 1987 are an average of 14 million traffic units per locomotive, compared to 44 million in Asia; and 240,000 tonne-kilometres per wagon, compared to 700,000 tonne-kilometres in Asia. In 1990, for example, SADCC locomotive availability was 47-70% and wagon availability 42-64%, as against comparable figures of 75-80% for locomotives and 90% for wagons elsewhere in the world.[14] While the starting point for improvements is the national railway authorities, collaboration between railways and, ultimately, the formation of regional coordinating institutions or fully-fledged regional companies, could have a significant role.

Similarly in the airline industry, there is considerable scope to ration-

14 Figures from Doyen (1992).

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alise operations and achieve economies of scale through having regional companies rather than national ones. A national airline is one of the symbols of nationhood, however, and regional companies, such as *Air Afrique*, are very much the exception rather than the rule. As privatisation gains ground, inefficient and inappropriate parastatals will be challenged to reform or be supplanted, a recent example being the demise of *Zambian Airways* and its replacement by a smaller, leaner private carrier. Significantly, this firm is based in South Africa. In the rail sector, too, the South African company Spoornet is already heavily involved with railways elsewhere in Africa. The formation of a joint venture with a Belgian company and the national rail company of Zaire as a means to recover outstanding loans from Zaire through making the rail system pay, is an interesting pilot development which may well lead to similar arrangements elsewhere on the continent.

Telecommunications

The development of telecommunications has been relatively neglected in the past in the majority of countries of sub-Saharan Africa. In part this has been the outcome of policies such as poor pricing, inadequate public investment resources and exclusion of private participation common to other infrastructure sectors. There has also been a tendency for telecommunications to be regarded as something of a luxury and has not attracted significant donor financing. That view has changed dramatically in recent years, as telecommunications has rightly come to be recognised as "a fundamental factor of production, alongside capital and labour" (World Bank, 1992, p. 1).

Over 80% of telephone lines in African countries are typically used for Government or business purposes, and an inefficient telephone service becomes a severe dampening factor on economic performance. In the World Bank's view, the main economic benefits of telecommunications are realised by improving the efficiency through which markets operate. Efficient telecommunications have thus become an increasingly important factor in determining the success of the structural adjustment programmes, based on trade and market liberalisation, which many countries are in the process of implementing (World Bank, 1991a, p. 4). The explosive growth of services which go beyond basic voice communication, including fax, information services and e-mail, further enhances the economic significance of having an efficient telecommunications service.

In sub-Saharan Africa, access to telecommunications is extremely low and the quality of service is poor. The average density of telecommunications service is about 0.3 direct exchange lines per 100 people, as compared with 0.6 in Asia (excluding Japan, which has 41.7) and 3.4 in Latin America. Local call completion rates are less than 30%, as compared with more than 70% in OECD and many developing countries.[15] Unreliability is partly a reflection of African telecommunications companies using antiquated equipment, and in many cases wholesale replacement of equipment is required. In this regard, however, the rapid advances in telecommunications technology can be seen as offering an opportunity to modernise and upgrade at the same time as expanding capacity at a unit cost which, in real terms, is often lower than it would have been even a few years ago.

The level of required investment is, however, daunting partly because of the replacement aspect and partly because of the fact that a much higher growth in telecommunications is required to underpin any given target rate of growth in GDP. The World Bank has estimated that the difference may involve a factor of 3: telecommunications growth of the order of 15% per annum may be required to underpin GDP growth of 5% per annum (World Bank, 1991b, p. 19). With national budgets already under pressure, there is no possibility of telecommunication investment targets being met without the significant participation of the private sector. To illustrate with a particular example, the investments required in Zimbabwe's telecommunications sector in the next five years to underpin a GDP growth rate of 5% per annum are equivalent to over 40% of the total public investment budget over the period. In practice, at most a small proportion might come from the Public Sector Investment Programme, and the remainder will have to be sourced from the domestic capital market and from attracting private participants.

However, in Zimbabwe as in other African countries, there is no experience and institutional structure to effectively regulate the telecommunications sector when it is opened to a mix of public and private ownership and is required to operate on commercial lines but without exploiting monopolistic positions. With a weak regulatory structure, the expected efficiency benefits of sector reform may well not materialise.

Telecommunications in Africa is becoming constrained by the twin inability of governments to finance the massive investments required from national budgets and to effectively manage the participation of the private sector. Regional cooperation in telecommunications development could help overcome both of these problems, by taking advantage of economies of scale to reduce unit investment costs and by using scarce skilled manpower to manage and regulate the sector effectively at a regional level for the benefit of participating countries.

15 Figures from World Bank (1991a) and World Bank (1991b).

The size of investment savings which can be expected may be illustrated with data from a recent study commissioned by COMESA (COMESA, 1996). The study found that the national investment costs of a 1000 line digital international exchange were on average $4.2 million, whereas in a regional project with joint procurement at world market prices, a similar exchange would cost about $2.2 million, a 47% saving. Savings would also be made on transit out-payments, which presently accrue to countries outside the region, but which after implementation of the interconnected network would remain within the region, making possible further infrastructural expansion.

Significantly, however, the study warns that "the impact on national development and the economic costs and benefits for each member state will not be proportionate ... What member states should appreciate is that the programme will benefit the region as a whole in the long term ... We recommend that the COMESA Secretariat ... make sufficient and effective dialogue and consultations to ensure that all members share a common vision on both the short-term and long-term economic costs and benefits. Without this dialogue, the project will face problems in mobilising the required political goodwill, commitment and a spirit of give and take, all of which are important ingredients to the success of such regional cooperation initiatives" (COMESA, 1996, p. 103).

V Financing and Institutional Arrangements

Section Two addressed the potential gains from a theoretical viewpoint, while Section Four outlined some of the specific opportunities for mutually beneficial cooperation in a number of infrastructural sectors. The realisation of that potential, and sharing of gains, depends crucially on overcoming the constraints encountered in the past which were outlined in Section Three. Some of these are macro issues related only indirectly to cooperation in infrastructural and natural resource development, principally the existence of political, military, social and economic stability. Other issues are more directly related, in particular the existence of effective institutions to direct and manage opportunities for regional cooperation.

Private interests are increasingly likely to play a role to ensure that benefits are maximised, while parastatal institutions will have regulatory functions to ensure that benefits are equitably distributed. This is because the widespread acceptance of the view that the private sector is better equipped to manage an organisation with a commercial function than a parastatal one has coincided with a sharp reduction in the capacity of sovereign states in Africa to guarantee loans for infrastructural development. Achieving the right balance within financing packages and institutional arrangements is a major challenge for the future. A mixed solution with some public provision of services remaining seems likely in most countries, but some may favour the extreme route of immediate and full privatisation of state-owned utilities. This would at least have the benefit of putting considerable momentum into direct foreign investment with likely spill-over effects in other sectors.

Despite the impression that innovative private sector arrangements are common elsewhere in the developing world, there are in fact a relatively small number of examples of such projects in other continents.[16] Very rapid growth is predicted, however, and Africa can usefully draw on experience of the various options, such as BOO (build, own, operate), BOOT (build, own, operate, transfer), DBFO (design, build, finance, operate).[17] Major issues in such arrangements are the extent of responsibilities of different actors (including ownership of facilities), risk sharing, tariff structures and financial arrangements over the entire lifetime of projects. Governments need to gear themselves up very quickly to understand the complexity and the richness of the options which can be negotiated with private investors.

As regards private sector participation in the specific sectors already discussed:

- In **electricity**, there is scope for independent power producers at the generation end, but also for private transmission and distribution companies. At the regional level, a private Power Pool company is certainly feasible. The institutional structure for the Southern Africa Power Pool is yet to be finalised, and could embrace private participation to a greater or lesser degree. Similarly, in other forms of **energy** private sector participation is also feasible: in Section Four, mention was made of the private role in the WAPCO gas utilisation project.
- In **water,** operational roles such as hydrology, water management, dam operation and management and environmental management could increasingly be contracted out to private concerns with public institutions assuming regulatory functions. This could dramatically reduce the size of many of the river basin organisations while, in all likelihood, improving the performance and cost effectiveness of specific functions.
- In **transport,** changes in the direction of private or quasi-private institutions have already been alluded to in Section Four. There are poten-

16 See, for example, *The Economist*, "Asia delivers an electric shock", October 28th, 1995, page 77.

17 There are African examples, too, from which much can be learnt. See, for example, Van Wyck (1995) for an analysis of financing major African water projects.

tial benefits from moving in this direction in the institutional arrangements for all transport modes.

- In **telecommunications,** the argument has been made that the scale of investments required is well beyond the means of national budgets in most African countries. In addition, in a sector characterised by rapid technological change, effective collaboration with partners with technical expertise may also be critically important in determining the success of telecommunications strategies.
- In **tourism,** in most African countries the private sector is dominant. What is required is more sophisticated regulation of the sector to ensure that the gains for the nation from tourism are maximised and that environmental sustainability is given due weight.

To avoid expensive duplication and inefficiency as the extent of private sector participation grows, it is important that the role of existing parastatal institutions be changed in step. Even where areas remain in control of the government-owned regional institutions, cost recovery policies, coupled with continuous efficiency improvements to minimise costs, are needed to ensure sustainability. Where continued subsidies are justified on equity grounds, these can be provided from tax revenues or from cross-subsidisation within the tariff structure. The direct approach is more satisfactory from an economic viewpoint, but the cross-subsidisation route in many cases is more workable and hence sustainable.

Across all the areas, donor support will continue to be important, but the scale of infrastructural investments that is required and the need for countries to become less dependent on direct donor subventions implies that imaginative new financing arrangements will have to be found. With the projects being executed increasingly by private sector entities, donor funds might best be devoted to strengthening financial institutions, such as the COMESA Trade and Investment Bank and the Development Bank of Southern Africa as well as the African Development Bank, which in future could play key roles in arranging financing packages for regional infrastructure projects. The capacity of development finance institutions needs to be rapidly enhanced if targets are to be met, but the potential of existing institutions should be fully explored before new ones are created. Useful lessons can be drawn from the financing of regional cooperation elsewhere, such as the experience of the European Investment Bank in financing infrastructural investments in the European Union and a growing body of experience in developing countries.[18]

18 See, for example, World Bank (1994), Chapter Five. As countries develop their capital markets and the sophistication of the banking system increases, the options for financing become much broader.

VI Conclusions

Regional cooperation in infrastructure and natural resources in Africa has a potentially significant role to play in increasing the pace of economic growth and underpinning sustainable development. Direct gains arise from trade in areas such as electricity, water, transport and telecommunications services and from the reductions in national investment costs, especially where supply expansion is "lumpy". Greater reliability in supply, reductions in unmet demand and learning externalities, such as technical and managerial skills, are developed through operating complex systems. Common natural resources, such as shared river basins, coastal ecosystems and wildlife habitats, cannot be effectively managed without regional cooperation. Properly managed regional tourism strategies could contribute to that process while increasing the revenue and employment benefits for participating countries.

Electricity is the sector with the greatest scope for cooperation. Grid inter-connections, fed by hydro and gas-fired power stations, offer considerable benefits, potentially reducing continent-wide investment requirements in this sector from around $4 billion per annum to $3 billion per annum. Ultimately, backbone connections could span the entire continent, with national and sub-regional electricity grids being secured with connections to the main supply channels.

In water management, there is considerable scope for better use of shared water resources for hydro-electricity generation, urban supply, agricultural development, fisheries development and tourism. In the transport sector, improvements in facilities and the quality of service is essential to reduce high bridging costs, especially for the 15 landlocked countries of Africa. In many cases, nominal capacity of transport systems is more than adequate for present levels of traffic, but is in need of rehabilitation, proper maintenance and improved management for an effective service to be provided. This is not the case in telecommunications, where high levels of investment are required to replace antiquated equipment and to expand capacity ahead of economic growth. Regional cooperation in telecommunications offers the potential to significantly reduce investment and recurrent costs. With an increasing role envisaged for the private sector and the consequent need for effective regulation, the emphasis in current transport and telecommunications programmes is on institutional reform.

In the past, despite obvious benefits typically for all participating countries, the potential for regional cooperation in infrastructure and natural resources has not been exploited for a number of inter-related reasons. The benefits may not have been properly quantified and understood; nationalism, compounded by confusion between self-reliance and security

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of supply, was a strong influence despite rhetorical commitment to regionalism; regional projects tended to stall when disparities between countries meant one country not being able to raise the necessary loan, or being less committed because of a perception of disparate gains accruing; inefficient parastatal control of facilities and inappropriate institutions responsible for regional programmes undermined the attainment of regional goals. Despite considerable donor support for regional projects and programmes, donor procedures, which are oriented to nations rather than regions, also contributed to the bias towards national rather than regional projects in the past.

These problems will not immediately be overcome in the future, but the emergence of peace in Southern Africa and in some other parts of the continent and the greater degree of economic realism characteristic of the structural adjustment era, including acceptance of a role for the private sector in infrastructure provision, are reasons for greater optimism about the prospects for regional cooperation in the years to come. The challenge will be to design financing and institutional structures which will turn potential regional benefits in infrastructure and natural resource management into reality on a sustained basis. In this, the mix between private sector resources and management to maximise benefits and public sector regulation to ensure their equitable distribution, will need to be carefully handled, drawing on experience in other continents. Rather than financing projects directly, donor finance should be channelled towards building up development finance institutions capable of arranging the increasingly complex financial packages which are likely to be required in future regional infrastructure projects.

Success in regional cooperation could well contribute to building a constituency in favour of deeper forms of integration, including the removal of barriers to trade and financial flows, this in turn sustaining the pace of regional development. Regional cooperation is thus not an alternative to regional integration, but a complementary strategy which can advantageously be pursued in parallel to the more difficult forms of regionalism.

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Comment on "Potential Gains from Infrastructural and Natural Resource Investment Coordination," by Peter Robinson

Samuel Wangwe

The paper identifies sources of potential gains of regional cooperation in infrastructure and natural resource development. In spite of what Peter Robinson refers to as a "win-win" characteristic, the level of regional cooperation in infrastructure and natural resources in the past is found to have been disappointingly low. The author, however, is optimistic about future prospects banking on the improvement in the security situation and the widespread adoption of economic reforms in the region. It is argued that these factors underpin prospects in specific sectors notably energy, water and transport. I am basically in agreement with the main thrust of the paper. In fact, the arguments in the paper are so convincing that one wonders why regional cooperation in infrastructure and natural resources is still so low. My comments will largely reflect on points of agreement with the paper and on additions which reinforce the general thrust of the paper.

Peter Robinson emphasises correctly that the largest gains arise from trade and investment integration and recognises that considerations of dynamic gains are of even greater significance in the era of globalisation. At the outset the author of the paper acknowledges that these dynamic gains involve the capturing of externalities in areas such as technology and skill acquisition. However, in the paper itself greater attention is given to gains accruing from pooling investment resources to make joint investments than on gains arising from technology and skills acquisition. Yet opportunities for reaping benefits of technological capability building could be demonstrated in technologies and skills associated with power generation and distribution, water management and transport. The case for the "win-win" characteristics of regional cooperation could be strengthened further if gains associated with technological capability building were brought out more clearly in the paper.

Robinson makes many good points on regional cooperation in infrastructure and natural resources but I would like to pick two points which I think deserve greater emphasis even in other areas of regional cooperation. First, the complementarity between regional cooperation and regional

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integration is a commendable idea. Regional cooperation as a complementary approach to regional integration rather than its rival is a useful idea for reconciling the otherwise common tension between the two approaches. Second, the tendency to confuse security of supply of infrastructural services with the nationalist approach to self sufficiency is shown to be fallacy. Zimbabwe's energy policy during the 1980s has provided a good example of this fallacy. Another example is Tanzania. The insecurity of supply of power that Tanzania has been experiencing in the past few years would probably not have occurred if Tanzania had taken a regional approach in energy planning. It has come to be recognised in Tanzania that connecting to the Uganda and Zambia grid could enhance security of power supply.

Regional cooperation in energy not only enables cooperating members to tap significant economies of scale but also increases reliability of supply and reduces eventualities of unmet demand or reduce occurrences of replicative private investments in energy supply to cushion the negative effects of unserved demand. Regional cooperation in energy, in particular, enhances reliability in supply partly because of the diversity of climatic conditions (e.g. timing of rain and dry seasons) and diversity of sources of energy supply (e.g. natural gas, coal, hydro power).

In addition to enhanced reliability of supply and savings in energy investment requirements regional cooperation is likely to bring advantages as well in terms of cost of generating energy in the region. Regional cooperation in energy supply would reduce the wide disparities in inter-country levels of cost of energy. For instance, the cost of a kwh of electricity ranges quite widely from 3.5 US cents in South Africa to 11 US cents in Tanzania. Linking energy generation to a regional grid is likely to reduce these disparities and allow low cost suppliers to reach several countries in the region. The advantage of energy cost reduction on various economic activities in the region would be considerable.

The paper has pointed out that while some regional cooperation programmes have been facilitated by the activities of donors the role of donors has contributed to dampening regional cooperation efforts at least in two respects. First, most donors programmes have had national rather than a regional focus. Second, different donors support programmes have been associated with different kinds of equipment and institutional arrangements which have often been incompatible. These observations are to a large extent valid. However, it is important to point out that the challenge here lies in the need to coordinate donor activity, an initiative which must be taken up by the recipient governments. The adoption of a national or regional approach to development programmes and the choice of equipment and institutional arrangements for implementing these programmes

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can be influenced more by national initiatives than by donor initiatives. The challenge is on the recipient governments to put in place national and regional programmes in which donor activity should be invited to fit in rather than the other way round (recipient activity fitting in donor arrangements). The tasks of coordinating donor activity is within the powers and mandate of recipient country governments.

The paper has covered three specific sectors: energy, water and transport. While it is not expected that all sectors related to infrastructure must be covered I feel that one of the sectors which should not be excluded from the discussion is telecommunications. The potentials of regional cooperation in using satellite facilities and in making best use of the super highway of information and utilising other benefits associated with the unfolding information technology deserve great attention at present and in future. This is an area where benefits of regional cooperation could be very high.

In section 5 of the paper reference is made to "Financing and Institutional Arrangements". This section says very little about financing arrangements. Yet, the paper indicates quite convincingly that the financial requirements of infrastructural investments are considerable. To date these investments in the region have largely come from donor funding, a source which is not sustainable. The challenge here is on establishing regional cooperation arrangements in financing infrastructure. In doing so the possibility of making use of existing financing institutions (e.g. Development Bank of Southern Africa) should be explored before creating new ones. In taking initiatives in putting in place financing arrangements lessons should be drawn from the experience of regional cooperation arrangements elsewhere. For instance, the experience of the European Investment Bank in financing infrastructural investments in the European Union may be useful in this context.

Comment on "Potential Gains from Infrastructural and Natural Resource Investment Coordination," by Peter Robinson

Sindiso Ndema Ngwenya[1]

Peter Robinson's paper presents a comprehensive examination of the potential gains from infrastructural and natural investment coordination from a theoretical and sector-specific viewpoint. On the basis of detailed and well argued analysis, the author draws policy proposals on how future cooperation could be designed and successfully implemented.

The following are the *prima facie* reasons for concluding that cooperation in infrastructural and natural resource investment coordination in Africa is less problematic and contentious than other sectors:

(i) Clear gains for all of development (hence no compensation mechanism is required);
(ii) No surrender of sovereignty;
(iii) Possibilities for private sector participation; and
(iv) Benefits from trade in electricity, water, transport services, etc.

It would be difficult and unreasonable for me to dispute the broad analysis and conclusions of the paper. My contributions are, therefore, aimed at providing a slightly different perspective on why regional cooperation in infrastructural and natural resource investment coordination has not been effective and to propose the way forward.

My comments and observations are based on my experience with regional cooperation in Eastern and Southern Africa. To understand the constraints for effective regional cooperation in the sectors of infrastructure and natural resource development, the following critical institutional and policy issues need re-examination:

- the ownership of infrastructure, management and operations at country level;
- the role of inter-governmental organisation in articulating and coordinating joint efforts in infrastructure and natural resource development; and

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1 The views expressed in this commentary are personal and should not be attributed to COMESA.

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- the role of bilateral and multilateral donors.

Infrastructure Issues

Ownership

Without exception, the ownership of infrastructure and public utilities is vested in governments. This is the case with roads, railways, civil aviation, electricity, ports and harbours, dams, etc. Hence, the issue of national sovereignty cannot be avoided. In order for joint efforts in infrastructural and resource investment coordination to take place, there must be a convergence of interests among the countries involved. Experience has shown, however, that regional cooperation in common projects may be stalled for three reasons: (1) one of the parties does not have the capacity to contract and service a loan; (2) the same party has (at least in the short term) the capacity and ability to supply services to the deficit country; and (3) it is perceived that other cooperating countries would reap more benefits than the supplying country. The region has a few cases for joint development in the area of electricity generation and harnessing of water from river basins for urban use.

It is conceivable that the ongoing economic reform programmes would, in the medium to long term, lead to private sector investment in infrastructure and natural resource development. This would of course depend on the resolution of imponderables such as, political and economic stability and adequate returns for investors who are probably likely to be from outside the region given the huge capital outlays required. It follows, therefore, that governments in the short to medium term would continue to be primary players in regional cooperation in this sector.

Financing

Closely related to the ownership question is the issue of financing. Perhaps this aspect, more than issues of sovereignty (which may be a causal factor), negatively affects regional cooperation efforts. In fact, the inability of cooperating countries to mobilise significant amounts of financing to support and sustain regional projects may be the "Achilles Heel" of regional cooperation. The failures have to be viewed against the background of the institutional and economic structural weaknesses and the crushing of burden of both domestic and external indebtedness. Given this situation, there is a tendency for countries to support regional infrastructural and natural resource programmes only if they are underwritten by bilateral donors and multilateral financing institutions. Paradoxically, however,

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some of the recipient countries have failed to provide the necessary counterpart funding thus delaying coordinated project implementation. It is not uncommon to find a paved road running to a border without a corresponding facility on the other side. This has led analysts to conclude that some countries view regional economic cooperation as a substitute for concerted national efforts to economic development. In fact, the degree of support that countries tend to give a regional organisation is closely related to the amount of money they expect to obtain from donors.

To address the issue of the resource gap, some regional organisations have established development banks which so far have, regrettably, been ineffectual due to weak capitalisation.

There is now consensus that a long-term solution to sustainable infrastructural and natural resource development at both national and regional level requires radical institutional and policy reform. Among others, this entails commercialisation, privatisation (where possible), corporatisation and the application of cost-based tariffs. Efforts to introduce road pricing at the regional level have had limited results, mainly because of the divergent interests of countries. The landlocked countries have generally favoured marginal cost pricing while the coastal countries have preferred and applied direct road user charges on the basis of full-cost pricing. Due to lower road traffic densities on most of the regional links, the application of full-cost pricing (which does not result in optimal resource allocation) has deterred the traffic from using certain transport corridors and ports. In addition to direct road user charges, there is a tendency for some coastal countries to introduce additional road user charges in order to raise government revenues. These practices have led to friction between (and among) countries.

Management/Operation

There is evidence that over the years, infrastructure has experienced inadequate funding and management practices. Due to the availability of subsidies, there have been no pressures on management to improve productivity and performance. The same argument can be extended to the arena of regional cooperation where the lack of imaginative and innovative perspectives has resulted in the replication of identical paradigms of cooperation irrespective of different socio-economic settings.

National solutions appear to be preferred over regional ones, among other things because the former affords opportunities for maximising rent seeking behaviour. Examples of regional cooperation initiatives that have had limited impact due to nationalism, political sovereignty, rent seeking, etc. include:

- The pooling of aircraft maintenance centres on the basis of intercountry

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specialisation and complementarity. The replication of aircraft maintenance facilities for a relatively small regional fleet has resulted in excess capacity and higher unit maintenance costs. The same applies to joint acquisition of aircraft and operations.

- Joint procurement of railway rolling stock, locomotives and spare parts.
- Joint railway operations across national frontiers to haul international traffic. In the early 1990s, the PTA (now COMESA) and Spoornet independently proposed establishing a regional Railway Operating Company whose mission and core business was to market and ship international traffic.
- Acquisition and use of jointly owned equipment for dredging regional ports. This would ensure maximum and cost effective utilisation of equipment.
- Joint planning and tendering of regional telecommunications network (e.g. the Nordic countries have over the years successfully tendered for common projects). This would reduce installation and procurement costs due to economies of scale. For example, the COMESA Telecommunications Network Interconnection project reveals that based on investment costs obtained from various administrations, a 1000 line digital international exchange costs on average $4.2 million, whereas, if the project was carried out jointly using world market prices, a similar digital exchange would cost about $2.2 million.

The Role of Inter-Governmental Organisations

In a nutshell, the mandates and terms of reference of African intergovernmental organisations including the United Nations Economic Commission for Africa (UNECA) are to:

- Identify, in collaboration with the countries, potential areas of infrastructural and natural resource development with a regional dimension.
- Coordinate the mobilisation of funding for feasibility studies and project implementation among the affected countries.

As alluded to earlier, the implementation of regional projects is predated on donor support. Ironically, whereas the rhetoric of regional cooperation is promotion of self-reliant development, there is heavy dependence on donor funding for capital and, in recent years, recurrent expenditure. A common feature of regional organisations is that they have not built institutional structures and capacities to foster cooperation which is regionally driven. I would therefore favour a critical appraisal of the existing paradigms of regional cooperation in order to craft institutional structures and mechanisms that would result in effective regional cooperation and integration.

The Role of Donors

While little would have been achieved without the donors' generosity, this generosity has carried costs and pitfalls. It has created an unhealthy dependence by recipient countries on external funding and has sustained a lack of fiscal discipline. The situation has actually worsened in that in some countries, donors are providing substantial funding for both capital and recurrent expenditure. This is a situation which donors are increasingly finding unsustainable. Fortunately, there is an emerging consensus on the need for policy reforms that would enable the private sector to invest (where feasible) in infrastructure and natural resource projects. A case in point is the proposed investment by the private sector in building a hydropower generation facility in Zambia.

Concluding Thoughts

The paper by Peter Robinson provides new perspectives on how regional infrastructural investment and natural investment coordination could be successfully realised. There is a need to build further on the analysis contained in the paper by exploring the following areas:

- Potential areas where *private* investment could either substitute or complement *public* investment in infrastructural and natural resource development of common projects. This examination could include an exploration of how funding could be mobilised from domestic and foreign investors.
- Appropriate and robust institutional structures involving all stakeholders that promote and sustain regional cooperation projects.
- Contributions by donors and multilateral financing institutions for developing the capacity and expertise to quantify the costs and benefits of regional cooperation using the broader analytical framework suggested by the author. Donors should also consider the costs and benefits of regional cooperation and financing in project financing.

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Floor Discussion of the Robinson Paper

Elty Links, the Director of International Development Finance at the South African Ministry of Finance, began the discussion with some comments about the concept of integration. "When we speak of integration in the government circles, we'd like to think more incrementally of the concepts that Peter Robinson uses in his first paragraph of coordination, collaboration, compatibility, harmonisation and such. What makes this paper specifically important in my mind is that it is a good starting point for those concepts to be instituted when we discuss infrastructural arrangements with regard to telecommunications, electricity and similar sectors.

What is South Africa's experience in this regard? The best way to examine this is to use the concept of a hub mentioned earlier by Colin McCarthy. All of these models make little sense without a hub. South Africa is loathe to take that responsibility even though it is seen by many in the SADC region as being such a hub. The reason a hub is so important in infrastructure is that there must be a centre around which financing can be coordinated and launched. Without such a hub, I think donor support would dry up as well. In the case of SADC, there is absolutely no doubt in my mind that much of the support that donors would be bringing into infrastructural projects across borders would be built around such a hub as South Africa. Our own experience in the Department of Finance has shown this to be the case. Still, our preference would be the establishment of a body within SADC to perform that type of function

On this issue of donor support, our experience is that the donors are ready to support such projects. Instead of focusing on sovereign nations, the multilaterals are rethinking their position on funding of programmes for across-border projects. It is important that we initiate and steer this new approach to multilateral financing. We have had past examples of multilateral financing across borders, such as the Lesotho Highlands Water Scheme, that cannot be easily repeated. Still I think there is a scope for multilateral organisations to provide this type of financing. Some of the bilateral donors are also convinced that there is a role for them to play. While the mechanism has not been worked out entirely, this is something that we anticipate in the future. In collaboration with other co-financiers, I think that the donor community is beginning to view across-border infrastructural projects as important. Bongi Kunene is heading up a unit in the Department of Finance to coordinate the function of cross-border financing, so I will turn to her now."

Bongi Kunene had some more specific comments on financing. "Peter

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Robinson's paper was quite good on identifying areas for investment possibilities on a regional basis in the future, and it seems to me that we ought to be thinking about different modes of development finance for such projects. We have already identified the projects that need to be undertaken, but how do we assess the risk applied to each project. Another question is whether we have the capacity at the regional level to develop different strategies for financing. Should the financing be applied individually, nationally or on a shared basis and what is the role of the multilateral institutions in such financing?"

Percy Mistry added that the regional financing is not unknown to the multilateral development banks. "In fact, the World Bank was a major financier of East African projects and projects in South Asia and Asia, so the technology is there. It hasn't been done for a while and there was a searing experience of unwinding some of these regional arrangements and redistributing assets and liabilities which I am sure the World Bank is much more cautious about now."

Gene Tidrick noted that the World Bank, the IMF, the European Union and the African Development Bank all support the Cross-Border Initiative and commented on the basis of that support. "I think that one of the essential premises of our support and the way in which the initiative is designed is that variable geometry is a promising way to proceed. We want to support whatever specific regional cooperation or integration efforts that are underway by whatever fast movers there are. We usually support these efforts through the topping-up of structural adjustment loans to individual countries, in particular those countries who are involved in the COMESA agreement, to form a free trade area under COMESA.

Another premise of our approach is the same which underlies the African Development Bank report on regional integration in Southern Africa. It is an excellent report, and we have discussed it with the AfDB and tried to insure that it is taken on board. This premise is that cooperation, coordination and harmonisation are probably more important in the short term than trade integration. Even simple cooperation in activities such as facilitating entry, literally, at the border to promote tourism can be more beneficial in the short term than trade integration where trade links are very small. We do believe that trade integration is important, as long as it is not inward-looking. Trade integration within the region should go hand in hand with a programme which anticipates external trade liberalisation and integration into the world economy.

Percy mentioned earlier that the Bank supports multinational projects. In the mid-1970s, the Bank was lending to the East African community for a number of projects, but it was very difficult to unwind from that experience. We spent a great deal of time trying to save the East African com-

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munity and some of the institutions, and then trying to mediate the dissolution. At the Bank, we continued pushing that particular regional integration even after the individual countries had already given up. Nevertheless, it is difficult for the Bank to deal with regional organisations, or more than one government, since we are set up to deal with national governments. By and large, I think that we would accept some of the criticisms that the Bank has not always effectively supported regional integration. Of course, it is true that we do not always agree on the type of regional integration which is proposed. But within the parameters I have outlined, we do support an essentially outward-looking regional integration.

With regard to the composition of regional integration, I think it is best to look at integration between South Africa and the rest of SADC as essentially a North/South type of integration because the levels of development and industrialisation are quite different. Such a union can provide the basis for very productive and dynamic trade creation as has occurred in Malawi where South African firms have set up textile and garment operations for exporting back to South Africa. This does not mean that everyone within the countries would benefit, and it may be opposed by organised labour in South Africa, but these are things that need to be considered and discussed."

Mohsin Khan followed with some comments regarding the time dimension of regional integration which he believed was lacking in Robinson's paper. "Personally, I am very suspicious about win-win situations. With regard to regional integration, it may be a win-win situation in the medium to long run, but there are undoubtedly costs in the short term."

He then discussed the potential role of the Fund in regional integration. "There is a legal question of whether we can deal with regional organisations. This issue came to a head recently in the case of the CFA zone. It was made clear, at least by the lawyers, that the Fund could not deal with regional organisations in formal sense. In an informal sense, we can, but we have run into a number of hurdles. Let me give you three examples. The first two examples concern monetary unions, and the third individual countries.

The European Union is the first hurdle. We have tried at various points to talk to the European Union in Brussels about issues such as regional or Union monetary policy or fiscal policies. But the countries themselves have opposed this and claimed that monetary policy should be discussed in the nations' capitals. In the CFA zone, we had a similar problem. With the exception of one country, the devaluation was identical. We decided to deal with the devaluation on a regional basis to have a consistency of programmes. We wanted to organise a group of individuals to oversee the design of the programmes for all of the countries which were loosely

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harmonised. But the countries themselves objected. They wanted to be dealt with separately. The third example was when India and Pakistan came to the Fund for Extended Fund Facilities. Given their similarities, we thought it would be wise to deal with them jointly to ensure consistency of advice. The moment the two countries found out that the two teams were sharing information, they made a formal objection to the IMF and stated that treating them jointly was patently unfair.

The bottom line is that formally, we cannot deal with regional institutions and informally, we have encountered several obstacles from the countries themselves. I basically feel that the Fund would be supportive of regional trading arrangements provided there is some kind of movement toward multilateral liberalisation."

Patrick Ncube, from Donsi Consultants in Cape Town, wondered what consideration had been given to the environmental consequences of the electricity potential that Peter Robinson pointed out in his paper. Robinson responded that the Batoka project was "incredible environmentally benign, only a few white water rafters will get displaced." With regard to the Inga, Robinson said that very little needs to be done by way of civil works to access the 40,000 mega-watts. "You don't have to build big dams, you just rechannel the water. There's a sort of natural power house which makes it a very remarkable place." Robinson was certain to stress that down sides exist as well, but that the main reason South Africa has shown interest in the hydro resources of the North was to avoid building smaller power stations which are causing such pollution problems in the Rand or moving on to the nuclear power route.

Phakamani Hadebe, a Deputy Director from the South African Department of Finance, suggested that while Robinson had outlined the inefficiency and unproductiveness of the government, he seemed to dwell on the government, and not the private sector, as the solution for promoting and supporting regional integration schemes. He also brought up the issue of national sovereignty. Robinson answered that the issue of sovereignty involved "getting the countries to think more constructively about where their national interests really lie. In Sindiso's comment, he noted that national solutions are often preferred since they offer greater opportunities for rent seeking. We have to recognise these rather grim realities about sovereignty versus cooperation. The role of the private sector offers some attractive possibilities vis-à-vis the government, and I referred to this in my paper. If we could get the private sector involved, a lot of finance could be unleashed which would be very important."

Sam Tulya-Muhika, Chairman of the East African Cooperation Forum, turned the conversation to the specific issue of the role of politicians and whether regional cooperation or integration is more likely. "Peter's paper

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gave the distinct impression that possibilities exist and that natural resources are abundant. There are certainly some sectors in Africa where cooperation is possible. From historical experience, I think cooperation has been less problematic than integration. But my enthusiasm was quickly dampened by the discussants because the good of the programme and the attitude and management of the political economy by our politicians surfaced as the major problem, and I have to agree with that appraisal. We have this potential in Africa. Do we want to live with the prospect of an energy deficit in the next century when we have the potential to have a surplus? If the politicians cannot see this, what can we do? I am appealing to the redirection of our energy, to focus on the people and organise the private sector to make these electoral issues.

I would also like some clarification on the pricing issue in power supply. Ugandans pay 10c per unit, and we are rather bitter about it because we have the cheapest power supply. But the cost was a conditionality set by the World Bank to subsidise Kenya's consumption. Our arrangement with Tanzania is more recent and as a result, it is a better arrangement. Why does the World Bank get involved in the pricing mechanisms in the member countries? Is this their business? They encourage private enterprise and then fix the prices."

Peter Robinson responded to this last issue with an example of electricity pricing in Zimbabwe. "I was involved recently with the team from the Ministry of Energy which was asked to work with our utility company Zesa on the long-run marginal cost of electricity. This was vital because there was a cross-cutting agreement into the main structural adjustment loan which required Zesa to go onto LRMC tariffing by a specific date or disbursements would be terminated. We thought that if we applied the methodology supplied by the World Bank and suggested a price, everything would be fine. We did this in a very conscientious manner and came up with 3.5 US cents. The official from the World Bank arrived and said, '3.5 cents? Far too low. In Africa, it's at least 7 cents. No question, you must have it wrong.' We showed him the methodology, the spreadsheets and each step that we followed. The problem was that it was a 1973 document and 'we don't hold with that anymore', he said. He produced some other methodology which came up with a figure more to his liking. Fortunately, he didn't go so far as to actually insist upon the implementation of this excessive tariff.

I think there has to be a bit more give and take. It's unfortunate that we are so dependent upon the Bank in the electricity sector to the extent that a number of projects have been stopped by Bank processes and Bank requirements. It is interesting to compare Zesa with Eskom which has more financial clout and can more easily raise finance. It can get ahead and make decisions.

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On Sam Tulya-Muhika's question about making the politicians realise what is at stake, the approach we are taking in Zimbabwe is to try to make government more accountable. We have had a lot of success in the energy sector. In liquid fuels, the government formed a task force which became an open forum with discussions held between the different parties. This had never occurred before. In the electricity sector, I think there will be open discussions and debates next year when the tariffs are announced.

As for getting to the grassroots, there are some obstacles that need to be overcome. The first is that these organisations aren't accustomed to expressing their opinion since their opinion hasn't been asked before. A second related problem is that many of these organisations don't have the technical competence to grasp the issues and really deal with them in a satisfactory way. This holds true for the broader cross-section of society in general."

Daniel Ndela from Zimconsult asked Robinson for some clarification on the linkage between the stages of regional cooperation and integration. "My view is that we shouldn't be thinking of stages," Robinson replied, "I think that cooperation and integration can proceed at the same time. The whole idea of variable geometry and multi-speed is that one has to exploit whatever opportunities exist; there's no point in waiting for cooperation and integration. If one is moving ahead as quickly as possible in all directions, the complementarities will emerge and this will help to keep the process going. If we confine ourselves to specific, prescribed actions at particular stages, opportunities for unleashing a dynamic process will be lost."

Edward Tiagha, the Regional Advisor in Industry Technology Development for the UN Economic Commission for Africa, suggested three other areas where African countries could benefit from regional cooperation in infrastructure. "Why do most African countries hop to Europe to have their planes repaired when we all know that Ethiopian Airlines has fantastic facilities for repairing aircraft? This could form a basis for regional cooperation or integration. The same thing goes for a dry dock. A huge multi-billion dollar project was set up by the World Bank to build a dry-dock in Duwala, but ships are still being repaired elsewhere. The third area is the industrial component of the aircraft and shipping industry. If we were to utilise the facilities for aircraft repair in Ethiopia and ship repair in Cameroon, we would have the potential to develop the manufacture of spare parts for both of these industries."

Alieu Jeng, Principal Economist at the African Development Bank, returned the discussion to the issue of political accountability and the failure of integration schemes in Africa. "There is a good governance dimension to this issue. African governments have not been accountable to their people. Regional integration agreements that have been agreed upon have not been respected; why is this the case? It seems to me that it is probably because politicians can renege on agreements that they have entered into, and they can do so with impunity. It is easy for integration agreements to be violated because there is no constituency back home to whom the politician is accountable. He is not required to answer to his people and explain why he has opted out of an integration. To hold the politician accountable, the integration arrangement and the issues related to it have to be extensively discussed and the people have to be informed. To do this, we have to reach the grassroots level and clarify the costs and benefits. If this were to occur, it would be much more difficult for the politicians to opt out of agreements."

Michael Matsebula, from the Department of Economics at the University of Swaziland, agreed wholeheartedly with Jeng and added an example as illustration. "The DBSA was mounting a research project to find out what individuals in selected countries in Southern Africa thought about SADC. It was interesting to discover that some of the executives working for big companies involved in international trade didn't even know what SADC was about. They believed it was something that belonged to the government and was not a topic of discussion for them. This is just an indication of the limited circulation of information about regional issues. If company executives are uninformed, how about the ordinary person? How can we sensitise the business community, non-government organisations and individuals about regional issues?"

The discussion on democracy, sovereignty and regional integration continued with a comment from Sam Asante, Senior Advisor on Regional Cooperation for the UN Economic Commission for Africa. "We have been saying that if we want to strengthen the African economic community, we need to strengthen the various regional groupings; ECOWAS, COMESA, SADC and so on. But we tend to forget that the building blocks for the regional organisations are found at the national level, and this is the major problem. We see governments enter into agreements, and then they don't observe what they have signed. This is because we have been unable to involve the man-in-the-street in this whole question of integration."

Asante went on to suggest how awareness could be increased at the national level. "I think that each country should attempt to establish a ministry of economic cooperation – and if not a full ministry then at least let them have a strong focal point so that when a regional issue comes up in the Ministry of Agriculture or the Ministry of the Environment, there is a central institution to which they can turn. This ministry must be vested with legitimacy and respect because in many countries, we have seen such focal point organisations become a repository for the deadwood in the other ministries."

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Mohsin Khan added some skepticism to the idea of reaching out to the grassroots level. "Let me put it in perspective. In December a CNN-ABC poll done in the United States found that 40% of the people did not know what NAFTA was. This idea of getting the man-in-the-street involved in these types of issues is simply not realistic. I just don't think that a national education campaign would be very successful or productive."

Samuel Wangwe, Executive Director of the Economic and Social Research Foundation in Tanzania, agreed with Khan and gave his own example of the difficulty of promoting awareness at the government level. "In following up on the Lagos Plan of Action, we went to the Ministries of Industry and Agriculture to ask how it had been implemented. We were told that if we gave them a copy of the Plan, they would tell us how the implementation was proceeding. So, they don't even have copy of the Plan which they are supposed to implement. The framework was ignored and the documents cannot be found. It is a challenge to our own governments to disseminate this information. I know that the World Bank feels bombarded by documents, and this is one thing that we can learn from the World Bank. Please bombard our governments with these documents."

Peter Robinson thought that setting up ministries of regional cooperation would be a disaster. "That's part of the problem. I think that South Africa has the right approach with establishing a portfolio inside the Ministry of Finance since this is the key institution in government. In these infrastructural areas, the actual sectors can take the initiative. This should be done much more at the level of the individual actor than at the ministerial level."

Reply by Peter Robinson

"I would like to go back to the questions of finance and the points raised by Gene Tidrick and Mohsin Kahn. I think we need to highlight that there is a major difference of opinion and approach between the Washington institutions and the majority of the African parties. This difference is that in Africa, regional integration is viewed as a means to self-reliant economic growth while in Washington, it is viewed as integration into the world economy. The question is, what does one mean by development? I think that Mohsin was quite provocative on this issue when he said that it was not clear whether trade liberalisation actually leads to greater prosperity and welfare. Are we simply taking the East Asian model and applying it to Africa? I don't have the answer to that, but I have been involved in a number of studies with Sam Wangwe on industrialisation in Africa and it is a difficult area. South Africa is in the running and maybe one or two other countries are relatively similar. But if we look at Percy's figures just for

SADC and SACU in the last few years, value added in manufacturing is actually declining.

Are we talking about a strategy that is going to lead to greater prosperity and welfare, or are we talking about a strategy that is pleasing to the Washington institutions because it fits into their preconceived ideas of what the long-run marginal cost or trade strategy should be? I put this provocatively. I don't have the answer and I'm not necessarily coming out on one side or the other because I think that Africa is a complex continent full of different possibilities and opportunities. But I do think that by pushing this particular line, you are ultimately encouraging countries to pursue different strategies and that is undermining possibilities for regional cooperation.

There is certainly a school of thought which sees the Cross-Border Initiative as a trojan horse, under the guise of the European Union, to sideline COMESA and SADC. These organisations might be a mess, but they do represent a political process that is occurring on the continent. As for the World Bank and the European Union, it is all well and good to suggest strategies which are more coherent from an economic point of view, but if they don't have the support and are not an organic part of the African process, maybe they are doomed to fail anyway.

Having said this, I would like to challenge you to take up some of the points made by Elty Links and Bongi Kunene. What ideas do the Washington institutions have about financing these infrastructure projects? Can we get more of a debate going on this issue, particularly since South Africa is assuming this mantle and looking to provide a solid basis for this sort of financing in the future?"

III Trade and Investment Integration in Sub-Saharan Africa

William M. Lyakurwa[1]

I Introduction

Regional integration in sub-Saharan Africa is not a recent phenomenon. At least two unions, the Southern African Customs Union (SACU) and the East African Community (EAC) have existed since 1910 and 1919, respectively. However, the majority of the regional economic integration schemes were established in the 1970s. There are currently ten such schemes and the revival of the EAC is being pursued seriously.

The motivations behind the establishment of regional integration schemes in sub-Saharan Africa (SSA) have been both political and economic. Most schemes were formed as a result of disillusionment with international political and economic systems that were viewed as unfavourable to developing countries. Some, such as the EAC and those in the CFA zone, were formed at the instigation of the former colonizers with the view of maintaining closer links across countries under their rule.

The formation of most of the unions also coincided with the era of export pessimism. This school of thought argued that the world trading system was not favourable to developing countries as a result of declining commodity terms of trade against those countries' exports, export earnings instability, low trade elasticities and unfair protectionism against their exports in developed countries. These arguments led to the conclusion that free trade could not promote development in developing countries and were used to justify import substitution-industrialisation policies and regional trading arrangements based on trade preferences.

A substantial literature on regional integration schemes in SSA exists. Recent studies include World Bank (1991), Mansoor and Inotai (1991), Lipumba and Kasekende (1991), Ariyo and Raheem (1991), de la Torre and Kelly (1992), Foroutan (1993), OECD (1993), de Melo and Panagariya (1993), and Lyakurwa et al. (1995). All these studies point to the fact that

1 I would like to acknowledge the very useful comments from Dr. Mohsin Khan and research assistance from Ms. Sheila Nyanjui. The usual disclaimer applies that the views expressed in this paper are those of the author and any errors or omissions are entirely his responsibility.

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the implementation of these schemes has been minimal and intra-regional trade flows have been insignificant, overall less than 5 per cent of total trade flows.

It is not surprising that despite strong political appeal, regional integration in Africa has achieved very little (de Melo et al., 1993; Foroutan, 1993; Elbadawi, 1995; Lyakurwa, 1995). Many of the regional schemes were designed without regard for the incentives of the contracting parties (Fine and Yeo, 1994) and in particular without compensation arrangements in cases where benefits were likely to be unevenly distributed. It has further been argued (Mistry, 1995) that adopting a framework of cooperation inappropriate to economic realities is a certain recipe for subsequent failure. Elbadawi (1995) reports on preliminary estimates of a gravity model and concludes that regional integration has been a failure. Lyakurwa (1995), using similar methodology, concludes that although intra-SADC trade flows have been low, there is significant trade potential within the Southern African Development Community (SADC); and with the participation of South Africa, SADC is a viable trade bloc as the results of the econometric estimates indicate.

Despite the failures, the glamour of regional integration in SSA has not diminished. It is hoped that, with a population of about half a billion people, SSA forms a potentially large market if only per capita incomes could be raised. It is evident, however, that the region has been experiencing economic decline since the 1970s (see Figure 1). Moreover, with the economy

Figure 1 Trends in Average GDP Growth and Average Secondary School Enrollment Growth

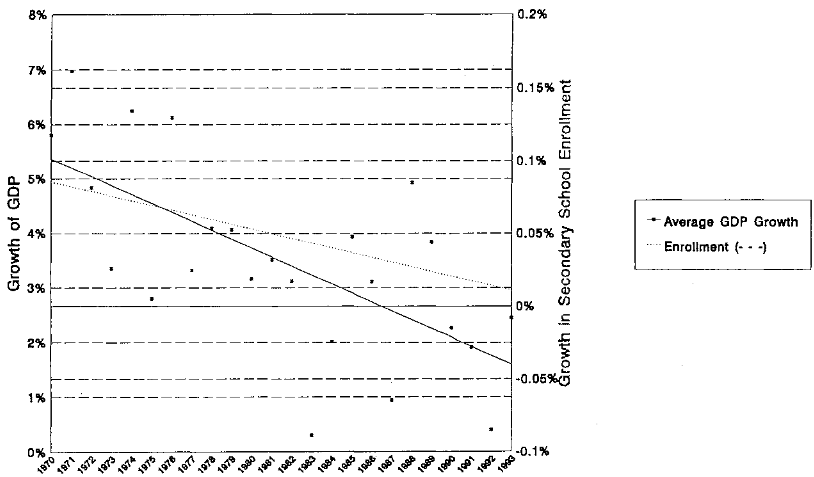

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Figure 2 Manufactured Exports to GDP and Foreign Direct Investment to GDP

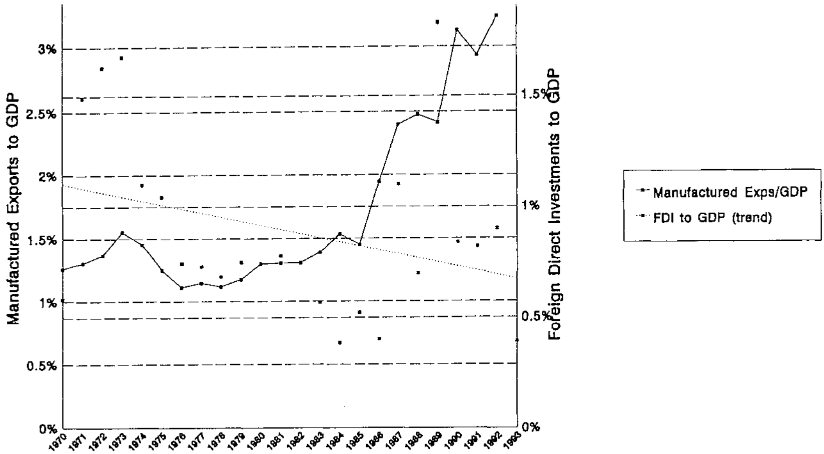
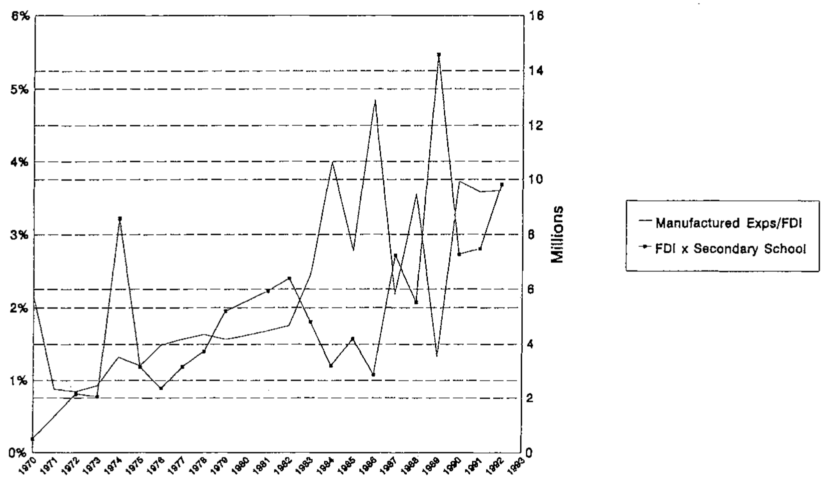


Figure 3 Manufactured Exports to Foreign Direct Investment and Foreign Direct Investment x Secondary Schooling



predominantly agricultural and a trade structure dominated by exports of fuels and other primary products (92 per cent) and imports of machinery and other manufactures (69 per cent), the conditions for successful regional integration appear to be lacking.

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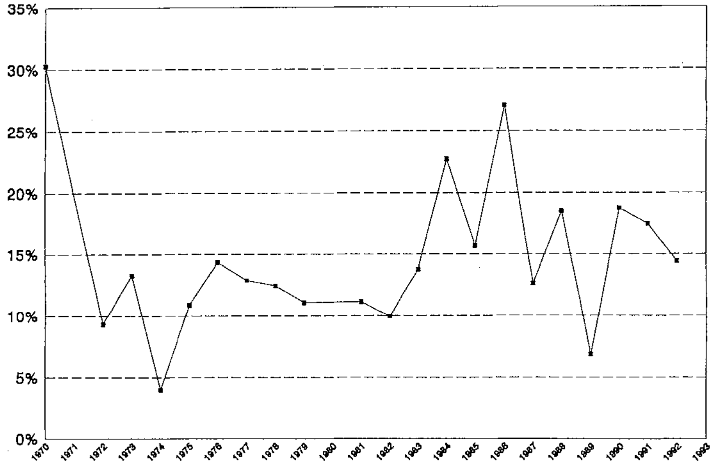
Figure 4 Manufactured Exports as a ratio of Foreign Direct Investment x Secondary Schooling



It has been argued (Gunning, 1995) that there is a more fundamental criticism than the one pointing to incomplete implementation, and that students of regional integration in Africa agree that it is an idle hope that trade policy could be used to promote regional integration by reciprocal discrimination between members of a regional scheme. The argument is simply that most African countries are too similar in endowments (unlike, for example, the members of the North American Free Trade Agreement, NAFTA) for such collusive trade policy to lead to substantial trade creation. In this view regional integration is – with the exception of schemes involving South Africa – at best vacuous (de Melo et al., 1993) and at worst trade diverting.

Gunning (1995) argues further that while in Africa regional integration has probably been pursued for the wrong reason, it can nevertheless perform a useful function. He notes that unilateral trade reform has often failed since it is usually undertaken in circumstances where trade liberalisation is time-inconsistent. In structural adjustment programmes there have usually been no incentives for maintaining reform and no credible penalties for policy reversals. The absence of a mechanism for locking-in reform, reversals of trade liberalisations and other economic reforms have become a serious problem in Africa.

In the past five years there has been renewed interest, and significant changes, in the approach to regional cooperation. The fear of the region's increased marginalisation has intensified in response to the perception of

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growing regionalisation of the world economy. Unilateral tariff liberalisation in many countries implementing economic reforms has questioned the previous emphasis on preferential tariff treatment for members. The more liberalised economic and political environment in many countries in the region has opened up opportunities for parties other than governments to pursue economic cooperation initiatives.

All these integration groupings attempt to build on the common characteristics and goals of relatively smaller groupings. However, their activities need to be conducted in such a manner that they harmonise with, and converge towards, those of larger sub-regional groupings such as the Economic Community of West African States (ECOWAS) and the Common Market for Eastern and Southern Africa (COMESA). Small groups progressing at different speeds are useful mechanisms in the interim, but this should not preclude the goal of strengthening larger integration arrangements which would be more commensurate with global developments in this respect. Such an approach, while facilitating achievement of the Abuja Treaty, could also pave the way for future relations with other regional trading blocs (Global Coalition for Africa, 1995).

Under regional integration arrangements (RIAs), there must, at the very least, be a willingness on the part of partners to agree on a minimum harmonisation of incentives if the benefits of integration are not to be dissipated in higher costs due to smaller scale production than a regional market warrants. This need not mean complete uniformity of incentives, especially if there are large disparities in the levels of development of members in an RIA. To make sure that the benefits of integration are appropriately distributed, it might be appropriate to allow certain countries to offer more favourable incentives, as is permissible in the case of the European Union's (EU) own regional policy. Differentiation on such grounds would imply a trade-off between efficiency and equity, but this may have to be accepted as the price of regional accord and to achieve the objective of levelling-out.

The new initiatives have also broadened the range of objectives for regional cooperation to include the removal of non-tariff barriers to trade; facilitating capital mobility and other business transactions; addressing sectoral issues; and pursuing conflict resolution. Constraints of multilateral agreements make "open regionalism" necessary, rather than closing the region to the rest of the world. The region seems to be moving in the direction of "variable geometry", providing for flexible institutional frameworks and accommodating progress at different speeds consistent with the Abuja Treaty (1991) principles. Furthermore, adoption of the principle of "subsidiarity", which involves the broadening of the participation of the private sector and other stakeholders in cooperation decisions,

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promises to keep the responsibility of dealing with issues of interest as close as possible to the concerned population.

These developments represent a significant departure from the past, building on existing institutions but accommodating greater flexibility in membership and rationalisation of operations.

The key question that has been posed by Elbadawi and Ndulu (1995) in the light of the glaring failures in regional integration schemes in SSA and the rekindled interest in regional integration arrangement in recent years is: can the current regional institutions in SSA guarantee market integration?

In a comprehensive paper, Fine and Yeo (1994) argue against renewed regional integration efforts in SSA along the traditional lines, where the existing regional schemes are called upon to attempt directly promoting regional trade despite repeated failures. In their view, these schemes are inappropriately structured, since they were designed to pursue the now ill-fated and out-moded import-substitution development strategy. They propose a new paradigm for regional integration in SSA inspired by the experiences of post-War II Europe and the recent "miracle" experience of East Asia. Regional integration initiatives in SSA should be designed to achieve the twin objectives of fostering national policy credibility, and rapid physical and human capital accumulation, the latter being initially triggered by enhanced direct foreign investment and by saving and investment surges within the region in subsequent stages. Fine and Yeo provide an exhaustive review of the evidence linking regional integration to these two objectives, which are now being accepted as the two main fundamentals behind East Asia's economic miracle.

Elbadawi and Ndulu (1995) argue that the key element of this strategy adopts the Collier (1991) and Collier and Gunning (1993) proposal of "participatory supranational agencies of restraint" in which national economic policy will be tied in a reciprocal threat-making arrangement to a northern anchor (e.g. the European Union). Fine and Yeo then ask the question as to why the European Union might be interested in playing such a role and argue that unlike the case of Eastern Europe, enhancement of trade, fear of mass migration or imminent security concerns could not be major factors. Instead, they suggest that the precedent of *Union Economique et Monétaire Ouest Africaine* (UEMOA); the vast interest of the EU in South Africa; the realisation that the African, Caribbean and Pacific (ACP) agreement which is administered by the European Commission has met with limited success; and the growing EU concerns with political stability as a prerequisite for economic growth may prompt a more active policy towards SSA. More recently, Gunning (1995) provides a further articulation of this argument, including an important extension linking the

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above approach to regional integration with direct foreign investment. This will be discussed further in Section Three below.

Four important current initiatives are pointing the way to a more pragmatic regional integration policy.

- The integration initiative to facilitate cross-border investment, trade, and payments in Eastern and Southern Africa and the Indian Ocean – the Cross-Border Initiative (CBI) – is pushing for accelerated tariff reductions between participating countries. It is establishing external payments and domestic regulatory systems to permit scarce investment capital to pursue the most efficient location, thus creating more growth throughout the region.
- The transformation of the *Union Monétaire Ouest Africaine* (UMOA) into a monetary and economic zone (UEMOA) includes provisions for coordination and harmonisation of macroeconomic and sector policies; creation of a single market for goods, services and factors of production; and harmonisation of the administrative and legal framework regulating economic activity.
- Recent reform of the *Union Douanière des Etats de l'Afrique Centrale* (UDEAC) is also designed to reform the tariff and indirect taxation systems, facilitate transit traffic, and strengthen monetary policy and financial management.
- Similarly, in Southern Africa, SADC is exploring the scope for harmonisation of macroeconomic policies among its members.

Clearly, all integration initiatives will have to be designed and pursued in an outward-oriented manner, consistent with achieving multilateral liberalisation. At the heart of these arrangements must be the objective of making trade and investment easier across present borders, allowing not only gains from trade but those from scale economies to be reaped.

This paper is divided into five sections. Section One covers the introduction, Section Two reviews the literature related to regional cooperation and using the gravity model tries to establish the potential for trade flows within the current regional economic groupings in SSA. In Section Three we discuss the link between foreign direct investment and regional integration arrangements with reference to SSA. Section Four deals with the empirical evidence of intra-regional foreign investment flows. This section discusses trade flows particularly in manufactures and the factors that influence the increase in intra-regional trade flows in manufactures which may foster enhanced regional economic cooperation. It then examines to what extent foreign direct investment (FDI) may lead to an increase in manufactured exports where in this case increases in manufactured exports have been used as a proxy for increased intra-regional trade flow in the econometric estimation. The section draws partly from the literature

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which emphasises that success with regional integration arrangement has occurred where trade in differentiated products, intra-industrial and intra-firm trade across member countries is dominant. Section Five ends the paper with some concluding remarks.

II Sub-Saharan Africa's Trade Potential

Earlier studies that have investigated the potential for intra-SSA trade include Ogunkola (1994), Foroutan and Pritchett (1993), Elbadawi (1995a) and Lyakurwa (1995) among others. The results of the econometric estimates using gravity models indicate that although intra-regional trade flows are low there is significant potential for increased flows.

In this section, using an expanded data set, we try to estimate the SSA trade potential using the gravity model and applying dummies to take into account the various regional groupings in SSA with a view to determining whether there is significant trade potential within the region. This section is also used to stimulate discussion on investment integration in SSA. The growing importance of foreign direct investment (FDI) as a means of accessing capital, technology, skills and foreign markets is accompanied by a (market) expansion of intra-firm and inter-firm trade by multinational corporations (UNCTAD, 1995b). Investment, trade and technology flows are closely intertwined and the potential benefits of FDI are widely recognised by developing countries as a contribution towards the achievement of their development objectives.

Regression Equation

$$\begin{aligned} TRADE_{ijt} = {} & \alpha + \beta_1 \ln(GDP_{it} \times GDP_{jt}) + \beta_2 \ln(GDPPCit \times GDPPC_{jt}) \\ & + \beta_3 DIST_{ij} + \beta_4 ADJ + \beta_5 COMESA + \beta_6 UDEAC + \beta_7 SADC \\ & + \beta_8 CEPGL + \beta_9 CEAO + \beta_{10} ECOWAS + e \end{aligned}$$

Method of Estimation = Ordinary Least Squares
Number of observations: 3675

Variables

$TRADE_{ijt}$: Natural log of intra-country imports for each year between 1980-1992.

$(GDP_{it} \times GDP_{jt})$: Natural log of the product of the real GDPs of country i and j at time t.

$(GDPP_{it} \times GDDP_{jt})$: Natural log of the product of the per capita GDPs of country i and j at time t.

$DIST_{ij}$: The straight line distance in miles between country i and j.

ADJ: A dummy variable: 1 if the two countries share a border and 0 otherwise;
Regional Dummies: 1 if both countries belong to the regional grouping and 0 otherwise; COMESA, UDEAC, SADC, CEPGL, CEAO and ECOWAS.

Country Sample

All countries in sub-Saharan Africa that are members of the IMF were used. Angola, Seychelles, Djibouti, Reunion and Mauritius were dropped due to the unavailability of GDP data. Intra-SACU trade data was also unavailable and hence SACU as a regional grouping was dropped from the analysis.

Organisation of Data

A pooled format was used with each available import value between reporter and partner along with all the other variables represented an observation.

All available import data for pairs of countries (reporter and partner) in SSA between 1980 and 1992 were collected and tabulated. As a result, 12,207 observations were realised. Due to the unavailability of GDP data, 8,257 observations were dropped leaving 3,675 complete observations. Each observation consisted of the following variables: Reporter, Partner, Year, GDP, GDPPC, Distance, Adjacent, <Regional Dummies>.

For example, for i = Mozambique, j = Benin and t = 1980
$TRADE_{ijt}$, GDP_{ijt}, $GDPPC_{ijt}$, DISTij, ADJ, [+ all regional dummies] would be one observation.

GDP is a measure of total economic size and in the gravity model it stands for the natural log of the product of the pair of countries' GDPs. That is, $(GDP_i \times GDP_j)$ where GDP_i is the real GDP of the reporter country and GDP_j the real GDP of its trading partner.

GDPPC – countries with similar living standards could realise higher level of intra-industry trade to the extent that they share a broader range of goods to trade. On the other hand, to the extent that GDPPC differences

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are highly correlated with differences in factor endowments, inter-industry trade driven by comparative advantage could be smaller between countries with similar level of income.

The variable distance was measured as the straight line distance (in miles) between capital cities regardless of whether the countries are islands or non-contiguous. The exception was South Africa where Johannesburg was used instead of Pretoria.

Methods of estimation = Ordinary Least Squares
Dependent variable: TRADE
Number of observations: 3675

The results of the regression estimates are shown below and the standard errors are heteroskedastic consistent (HGTYPE=2).

Regression Results

Variable	Estimated coefficient	Standard Error	t-statistic
C	-29.9043	2.55.21	-11.7262
GDP	.750078	.035322	21.2353
GDPPC	7.13236	1.19593	5.96386
DIST	-.345825E-03	.663401E-04	-5.21290
ADJ	.654900	.132875	4.92870
COMESA	.858100	.154931	5.53858
UDEAC	-.084336	.286960	-.293895
SADC	1.33212	.206915	6.43802
CEPGL	.031308	.385402	.081235
CEAO	-.096303	.188886	-.509844
ECOWAS	.962625	.172083	5.59397

Mean of dependent variable	= 13.2257	Adjusted R-squared	= .171518
Std. dev. of dependent var	= 3.24.59	Durbin-Watson statistic	= .987956
Sum of squared residuals	= 31877.6	F-statistic (zero slopes)	= 77.0615
Variance of residuals	= 8.70022	Schwarz Bayes. Info. Crit.	= 2.18492
Std. error of regression	= 2.94961	Log of likelihood function	= -9184.24
R-squared	= .173773		

The results of the econometric estimation indicate that the variables GDP, GDP per capita, distance and adjacency are significant determinants of the trade potential in SSA. Applying dummies for regional groupings, it can be observed that there is significant trade potential within COMESA, SADC and ECOWAS which is consistent with the results of earlier studies. The other regional groupings do not demonstrate significant trade potential as indicated by the results of the econometric estimation.

It should be noted that ECOWAS, COMESA and SADC are the largest regional groupings and with the monetary arrangement within CFA, which is also part of ECOWAS, intra-regional trade flows may easily be facilitated. It should also be noted that both ECOWAS and COMESA have established clearing house mechanisms where intra-regional payments can be settled without recourse to foreign currency. However, the utilisation of the clearing house mechanism has been very limited. This may be explained in part by the fact that a majority of the countries in SSA have implemented structural adjustment programmes which involve substantial trade and foreign exchange liberalisations wherein availability of foreign exchange has become less of a constraint in trade finance. However, recent reversals of the reform process in Nigeria may affect official intra-regional trade flows in the region though unofficial trade flows which have thrived over the years should not be affected.

In the case of SADC, there was also a mechanism put in place to extend foreign exchange to firms producing for the regional market (Export Pre-financing Revolving Fund established under the acronym NORSAD Fund). The objective was to assist and support the creation of commercially viable enterprises that would contribute positively to the economy of the host country. This objective would be achieved by supporting export oriented projects which optimise the use of local raw materials. By 1994 a total of DKr 200 billion had been earmarked for this activity but by the end of the year only DKr 30 million had been disbursed. It has been argued that supporting credit facilities might encourage intra-regional trade but in most developing countries, and in particular in SADC, the absence of donor interest in providing financial support to public institutions, which in most cases are not financially sound, has made it difficult for implementing such facilities to the extent required. The Export Pre-financing Revolving Fund, as in the case of the clearing house mechanism, is no longer as attractive as it was during the period of the foreign exchange crisis. The constraining factor is now the availability of local currency to acquire foreign exchange. All said, despite the presence of significant trade potential within some SSA regional groupings, trade flows have been very low as has been observed earlier.

One of the oldest schemes, the sixteen member Economic Community of Western African States (ECOWAS) may serve as an example of the failures of regional integration groupings in SSA. ECOWAS became effective in 1977. According to the 1975 Treaty, trade liberalisation was to start in 1979 and to be completed by 1989. In fact, trade liberalisation did not even start until 1990, fifteen years after the signing of the Treaty (Jebuni et al., 1995) and so far none of the goals set out in the Treaty have been reached. ECOWAS is dominated by one very large country, Nigeria, and

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fear of Nigerian hegemony has made the other members reluctant to import Nigerian goods (at least officially; there is a thriving parallel market). Conversely, Nigeria is suspicious of the Franc Zone membership of its fellow ECOWAS members. To make matters worse, Nigeria reversed seven years of liberalisation in 1993, including the trade reforms it had initiated in 1986.

In the case of one of the relatively successful schemes, the Customs Union of Central African States (UDEAC), a common external tariff was one of the objectives. In fact, as documented by Decaluwe et al. (1995), the members adopted widely different rates. In one case all six member countries used different rates, ranging from 8 to 49.5 per cent (Gunning, 1995). Similarly, the CEAO is supposed to have a common external tariff but this is not effective and the members frequently use non-tariff barriers against each other. The Common Market for Eastern and Southern Africa (COMESA), which aims at complete trade liberalisation by the year 2000, indicates that while all members should have attained tariff reductions of up to 60 per cent by 1993 only six of the 20 members had their tariffs published by then.

The lack of success of the regional integration attempts is also illustrated by the experience of structural adjustment in Africa. Typically, far-reaching changes in economic policies, including trade policy, have been achieved under structural adjustment programmes, but without coordination or even consultation with fellow members of regional groupings. Foroutan (1993, p. 239) concludes that "thus far [there has not been] any meaningful trade integration in SSA". Indeed, the share of intra-group exports in total exports is minimal in almost all schemes and often has stagnated or even fallen after the start of regional integration. Would the schemes have been more successful if regional integration had been more seriously pursued? A growing literature[2] gives a negative answer.

The above analysis and the conclusions reached, notwithstanding, there is a window of opportunity for SSA to use regional integration as a supranational mechanism to foster national policy credibility, and as a means for pooling risks between otherwise vulnerable small economies; to resolve conflicts and minimise political risks; to exploit complementarities; and to develop regionally-based links in a *reciprocal and mutually* beneficial basis. Reciprocity is a key word here because it is the only guarantee against having strategic cooperation with a dominant economic and political core stifling considerably indigenous African initiative for owning and under-

2 See, for example, Foroutan (1993), Foroutan and Pritchett (1993), Gunning (1994), Collier and Gunning (1995), Fine and Yeo (1994), Elbadawi (1995), Lyakurwa (1995).

taking their own development vision. In this context the new regional schemes in SSA should also take into account, the incentives facing the government bureaucracy and the private sector; address the issues of concentration and agglomeration, and the distribution of gains and losses; attempt to deal creatively with the problems of "hub and spoke"; and create strong institutions that can effectively implement integration measures. (Elbadawi, 1995a).

III The Link Between Foreign Direct Investment and Regional Integration Arrangement.

Theories of intra-industry trade which are based on the neoclassical trade theory offer explanations of comparative advantage as a result of factor endowment, draw attention to technological differences between countries and accord an important role to economies of scale.

The development of intra-industry trade, while based on differences in endowments, also depends on market imperfections such as economies of scale in production, technological leads and lags, learning from experience, product differentiation and linkages between industries. In this way it can be explained why particular products within industry groups are competitively manufactured in particular locations (Keesing and Lall, 1992). National economic characteristics do not fully determine trade patterns, intra-industry trade flows rely to a large extent on regional economic cooperation.

However, both the old and new trade theories do not properly recognise other critical problems of exporting manufactured goods from developing countries, such as obtaining access to competitively priced inputs, export incentives, services and infrastructure. The complexity of learning to export, the information required and the vulnerability of exports to inappropriate government controls and policies require coordination at national and at the regional level. For further discussion of export promotion measures see Lyakurwa Lyakurwa (1990).

The importance of FDI participation in manufactured exports and of intra-firm trade more generally have been observed by many authors (Helleiner, 1973; Naygar, 1978). Both seem to be on the increase under the influence of the trading opportunities made possible by both regional and global vertical integration. Most SSA economies need to develop a significant amount of manufacturing for export to foster increased intra-regional trade flows. The issues that have been raised but not discussed in this paper in any detail are: What type of technology, marketing and other promotional policies are necessary to support manufactured exports for regional as well as global markets?

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It has been observed by Musonda (1995) that intra-industry trade is more common among countries at the same level of development, that have similar tastes and similar levels of factor endowments, among others. She argues that this trade is further enhanced by the formation of regional groupings since the removal or reduction of trade barriers increases trade in general and intra-industry trade in particular. This explains why similar types of products are traded among neighbouring countries.

Most African countries have now adopted national regulatory frameworks conducive to FDI. They permit profit repatriation and provide tax and other incentives to attract investment. In addition, efforts to increase FDI inflows have included the simplification of the investment-approval process (e.g., by setting up "one-stop" investment centres), the establishment of investment-promotion institutions and the increased use of representative offices abroad to publicise investment opportunities. In addition, the parastatal reform process, which involves the sale of a large number of parastatals, should provide an additional window for FDI inflows. The reformist mood has been widespread and, at times, exhibited itself in quite rapid policy and legislative changes. For instance, in just one five-year period alone (between 1982 and 1987), about one half of all African countries either introduced or made adjustments to their investment codes or guidelines in order to attract more FDI. The end of the 1980s and the beginning of the 1990s also saw many other countries among the other half introduce new investment laws or amend old ones. Countries that have traditionally been regarded as being relatively open to FDI, such as Kenya and Zimbabwe, went out of their way to revise their regulatory frameworks to become more attractive. But even countries with a previous reputation of hostility to FDI, such as Ethiopia, Guinea and Mozambique, introduced new legislation offering a wide range of guarantees and opportunities for foreign investors. Prospectively, all these new measures should lead to inflows of FDI.

It would be natural, therefore, to infer that the specific trade orientation embodied in the different waves of incoming foreign investment would influence very significantly the outward orientation of the industrialisation drive. However, little has been done in this direction. The present study is an attempt to establish possible linkage between manufactured exports and FDI. It has been observed that the high export growth rates in Brazil were not confined to natural resource based or labour intensive industries. Export performance was also exceptionally good in sectors receiving "vintages" or more outward oriented FDI, and in several of the more technology or capital intensive sectors intensive FDI penetration during the formative stages was a critical factor (Fritsch and Franco, 1992).

Notwithstanding the liberalisation of FDI regimes – at least in terms of

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removing foreign ownership limitations – most countries still maintain a requirement that the government must approve the establishment of any FDI project. In other words, they have in place a "screen-and-approval" process for foreign investors. Proposed investments have to meet certain criteria stated in the investment code in order to obtain approval. However, several countries are recently adopting more open regimes. In some cases such as Namibia, there is no approval process, and national treatment is assured by law. In others, such as Mozambique and Eritrea, there is no specific requirement for FDI approval, but many foreign investors nevertheless go through an approval process to obtain wide-ranging tax concessions.

Much of the focus of the discussion on regional integration in SSA rightly focuses on trade aspects. It should be noted that also crucial in the integration process – especially regionally but also multilaterally – are its international financial aspects. Although very important, these financial aspects tend to be insufficiently emphasised in many of the studies on integration as well as in policy discussions on the subject.

It has been argued (Griffith-Jones, Canto and Ruiz, 1995) that there are at least five major aspects in which international financial flows and mechanisms play a very important role in regional integration:

1. Financial mechanisms are created explicitly with the purpose of enabling or facilitating trade integration. As mentioned earlier, the COMESA and ECOWAS clearing house mechanisms were established to facilitate payments and clearing arrangements for intra-regional trade. The relevant question that needs to be addressed is whether the mechanisms created operate efficiently and whether they are sufficient and on appropriate terms to meet the needs of integration. As noted earlier, the performance of the clearing house mechanisms in facilitating intra-regional trade flows has been fairly limited. Similarly, the NORSAD fund established to support SADC institutions to increase production for the sub-region, did not perform as effectively as it had been anticipated. Part of the reason was that the NORSAD management did not have sufficient staff to deal with requests from all the countries in the region.
2. Regional integration can be more or less spontaneously stimulated by intra-regional direct investments. Such flows have played a particularly large role in the market-driven integration processes of Asia; they are also, however, playing a fairly important role in the move toward the policy-driven process of Western Hemisphere integration. Insufficient research and data compilation hinders full understanding of this phenomenon (Griffith-Jones et al., *op. cit.)*.
3. Regional integration leads to a process of increased investment from

outside the region. This dynamic effect of investment creation for the country or region relates to the additional flows of foreign investment from outside the region generated by three factors linked to regional integration: (a) preferential and stable access to a significantly larger market; (b) potential regional complementarities in terms of resources and productive capacity; and (c) a decline in uncertainty on economic policies which countries will follow, called the "lock-in" effect.

4. To the extent that FDI represents an addition to a country's capital stock, it affects resource allocation in a number of ways. It affects capital accumulation, industrial structure and the country's trade propensity with a bias towards outward orientation.
5. It is important to observe that foreign subsidiaries are perhaps more sensitive to changes in the policy environment within which they operate. Since export promotion has become one of the more common performance requirements, this, to some extent, explains why some multinational corporations have become over-reactive to incentives for export promotion for both intra-regional and extra-regional markets.

IV Intra-Regional Foreign Investment Flows: Empirical Evidence

It has been argued (Griffith-Jones et al., *op. cit.)* that an important distinction made in the literature on economic regionalism is that between market-driven (or *de facto)* versus policy-driven (or *de jure)* regionalism. The classical example of policy-driven regionalism is European integration, whilst the main example of market-driven regional integration is the Asian experience. Within this latter process, intra-regional foreign direct investment has played a key role in supporting both rapid economic growth in that region and stimulating rapidly growing intra-regional trade. Indeed, while in the 1980s, 70 per cent of investment flows from underdeveloped countries were channelled to the developed world, the majority of Asian FDI flows went to developing countries in Asia, mainly for investment in export-oriented manufacturing.

Africa seems to lie at the bottom of the ladder. Though to an important extent integration within Africa is policy driven, there is emerging an increasingly dynamic undercurrent of market-driven investment flows stimulated by the substantial trade and payments liberalisation that has taken place. As the growth of intra-regional investments is a new phenomenon, information on these investments is completely lacking and efforts at analysing their impact are even more rudimentary. In what follows, we will attempt to present a broad picture of FDI in SSA and by proxy try to estimate the effects of FDI on the export of manufactures. If attention is focused on manufactures, growth and shares are notably higher though

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Table 1 FDI Inflows to Africa, 1981 - 1994

(billions of dollars and percentages)

Region/Country	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990	1991	1992	1993	1994a/	Total 1981-94	Annual Averages 1981-85	1986-90	1991-94
All Countries	63.7	54.6	50.4	58.9	58.5	84.0	136.0	161.4	198.6	210.4	162.3	163.4	184.5	204.0	1,790.6	57.2	158.1	178.5
Developing Countries	20.6	25.7	17.1	18.2	15.4	16.2	22.6	29.0	28.6	33.9	40.3	53.2	71.8	83.6	476.2	19.4	26.1	62.2
Africa	1.4	1.4	1.2	1.4	2.9	1.8	2.5	2.8	4.8	2.2	2.8	3.3	2.9	3.5	35.0	1.7	2.8	3.1
Africa's share in %																		
All Countries	2.2	2.6	2.4	2.4	4.9	2.2	1.9	1.7	2.4	1.0	1.7	2.0	1.6	1.7	2.0	2.9	1.8	1.8
Developing Countries	6.8	5.6	7.0	7.9	18.9	11.3	11.2	9.6	16.8	6.5	7.0	6.1	4.1	4.2	7.4	8.6	10.8	5.0
Oil Exporting Countries of Africa, b/ c/ (billions of dollars)	1.1	1.0	1.2	1.1	2.5	1.7	1.8	2.1	1.2d	2.1	1.8	2.3	1.8	2.3	24.3	1.4	2.0	2.1
- Egypt	0.8	0.3	0.5	0.7	1.2	1.2	0.9	1.2	0.7	1.2	0.5	0.5	0.5	0.5	9.8	0.7	1.1	0.4
- Nigeria	0.5	0.4	0.3	0.2	0.5	0.5	0.6	0.4	0.6	0.4	0.7	0.8	0.9	0.8	8.2	0.4	0.7	0.8
Other, non-oil exporting countries of Africa c/	0.3	0.4	0.02	0.3	0.4	0.2	0.7	0.7e/	1.4e/	1.0e/	1.0	1.0	1.1	1.2	9.3	0.3	0.8	1.1
Share in Africa's total f/(percent)																		
Oil Exporting countries	80.5	70.7	98.0	80.5	87.6	90.3	71.7	74.8	71.4	56.5d	65.0	69.6	62.5	66.1	69.5	83.7	72.2	65.9
- Egypt	53.6	20.5	40.8	50.9	41.2	66.6	37.7	42.8	26.0	33.3	9.0	14.1	16.8	15.1	27.9	41.3	37.8	13.9
- Nigeria	38.9	30.1	28.6	14.0	16.7	9.1	23.9	13.6	39.1	26.6	25.3	27.5	24.9	22.2	23.4	24.0	25.6	24.9
Other Countries	19.5	29.3	2.0	19.5	12.4	9.7	28.3	25.2	28.6	43.5	25.0	30.4	37.1	33.9	26.5	16.3	27.8	34.1

Sources: UNCTAD Division on Transnational Corporations and Investment, based on IMF, balance-of-payments tape, 15 March 1995; estimates of the OECD and official national sources.

a/ Estimates.

b/ Algeria, Angola, Cameroon, Congo, Egypt, Gabon, Libyan Arab Jamahiriya, Nigeria and Tunisia.

c/ Figures may not add up to Africa's total because of rounding.

d/ Africa's total is less than the total for Egypt and Nigeria because it includes disinvestment in other countries

e/ Figures are inflated by unusually high investment in Liberia in 1988-1990 ($290, $656, $225 million, respectively), most likely in flags-of-convenience facilities. Inflows to "other Africa" net of Liberia were as follows: 1987 - $674 million; 1988 - $411 million; 1989 - $719 million; 1990 - $735 million and 1991 - $977.1 million.

f/ Percentages based on the figures before rounding.

FDI to GDP ratios have been declining (see Figure 2). It has been argued that intra-regional exports are actually more intensive in manufacture and in non-traditional products (Ffrench-Davis, 1995; Lyakurwa, 1995).

FDI flows to Africa increased marginally from $1.4 billion in 1981 to $2.8 billion in 1988 and $4.8 billion in 1989 but declined drastically to $2.2 billion in 1990 and have since been rising slowly to $3.5 billion in 1994. As a ratio of GDP, however, the trend has been declining between 1970 and 1993 (see Figure 2). When this trend is compared to all developing countries, a different picture is observed. While FDI flows to all developing countries increased from $20.6 billion in 1981 to $33.9 billion in 1990, there was a very significant jump from $33.9 billion in 1990 to $83.6 billion in 1994 with Africa's share only at 4.2 per cent (see Table 1).

Net foreign direct investment in Africa increased sharply from $0.4 billion in 1988 to $1.1 billion in 1990. It has averaged about $1.8 billion between 1991 and 1995. In contrast, net foreign direct investment in Asia increased rapidly from $9.8 billion in 1990 to $41.4 billion in 1994, an increase of over 400 per cent and representing about 70 per cent of the net flow to developing countries. This high growth declined slightly to $36.8 billion in 1995 representing about 65 per cent of the net flow to developing countries (see Table 2).

Table 2 Developing Countries: Net Foreign Direct Investment, 1988-96*

	1988	1989	1990	1991	1992	1993	1994	1995	1996
Developing countries	19.0	17.6	19.0	27.2	34.5	49.2	59.2	56.2	54.9
Africa	0.4	3.7	1.1	1.4	2.5	0.7	2.5	2.1	3.1
Asia	8.6	5.6	9.8	13.7	17.6	33.9	41.4	36.8	33.4
Middle East and Europe	1.3	1.2	1.2	1.0	1.7	1.3	0.6	0.8	1.3
Western Hemisphere	8.7	7.2	6.9	11.2	12.8	13.4	14.8	16.5	17.0

* Projected data for 1996.
Source: International Monetary Fund, *World Economic Outlook*, Data Base.

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It may be noted that as a result of severe foreign exchange shortages, many African countries imposed restrictions on capital flows in the 1970s and 1980s, including capital repatriation. Over the years, many of the countries recognised that their foreign exchange control laws were a strong disincentive to foreign investors and decided to guarantee foreign investors a right to repatriate capital and profits, thus exempting them, to a certain extent, from the otherwise restrictive foreign exchange regime.

Although there may not be a one-to-one correspondence between low FDI flows and real output growth, there is evidence that FDI, when complemented with adequate human capacity, engenders growth via technological learning and crowding in of domestic private investment (Elbadawi and Ndulu, 1995; see also Figure 3). Africa's real output growth has been below 2 per cent per annum between 1986 and 1994 while real output growth for all developing countries has increased from 4.8% in 1986-90 to 6.1% in 1993 and 5.6% in 1994 with Asia registering the highest growth rates of over 8% per annum (see Table 3). While FDI flows to Africa were low during the 1980s and the early 1990s, the continent's foreign indebtedness reached high levels in the 1990s with total debt rising from $249.55

Table 3 World Real Output Growth, 1986 - 1994
(annual percentage change)

Region and Sub-Region	1986-1990	1991	1992	1993	1994
World	**3.6**	**0.9**	**1.7**	**2.3**	**3.1**
Industrialised countries	**3.2**	**0.8**	**1.5**	**1.3**	**2.7**
United States	2.7	-0.6	2.3	3.1	3.7
European Union	3.3	1.2	1.1	-0.3	2.1
Japan	4.5	4.3	1.1	0.1	0.9
Other industrialised countries	2.8	-1.1	0.6	1.5	3.5
Developing countries	**4.8**	**4.5**	**5.9**	**6.1**	**5.6**
Africa*	-	2.7	1.2	0.7	1.9
Asia	7.1	6.2	8.2	8.5	8.0
Middle East and Europe	3.3	1.9	7.0	4.8	1.4
Latin America and the Caribbean	2.1	3.4	2.5	3.4	2.8
Countries in transition					
Central and Eastern Europe	-	-11.5	-11.7	-5.7	-5.4
Russia	-	-13.0	-19.0	-12.0	-12.0
Transcaucus and Central Asia	-	-8.2	-17.3	-10.7	-6.6

* African Development Bank estimates for regional members only.
Sources: IMF, *World Economic Outlook*, October 1994.

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billion in 1990 to $269.47 billion in 1994 and the debt service ratio increasing from 30.54% to 35.38% over the same period (UNCTAD, 1995a). At the same time, the continent experienced capital outflows of around $2 billion per annum between 1990 and 1994 (UNCTAD, *op. cit.).* These figures present a disappointing picture in terms of SSA future growth prospects.

Capital investment and technological progress are the keys to economic growth. While the production of technology (that is, research and development) is largely concentrated in the developed world, its results spread rapidly through licensing and direct foreign investment. The effective absorption of this advanced technology and hence its growth effect, critically depends on the presence of a level of human capital in the host country (Borensztein et al., 1994; Elbadawi and Ndulu, 1995). Secondary education attainment is considered the prime measure for attaining the required human capacity and competence for the effectiveness of FDI in generating growth. There is a large volume of literature on direct foreign investment and the multinational corporations, but in general the quantitative documentation available is poor (Blackhurt, et al., 1978). In SSA, as a result of the declines in GDP growth rate which gives rise to lower budgetary allocations to education expenditures and the very high population growth rate, the trend in secondary school enrollment has been on the decline (Figure 1) and this is likely to pose a very serious constraint to future economic growth in the region.

It has been argued that regional cooperation in SSA requires an external anchor to be viable and sustainable (Collier, 1991; Collier and Gunning, 1995; Elbadawi, 1995a; Fine and Yeo, 1994). This might be an attractive option if it would lead to increased FDI into the region. It has further been argued that such a proposal would be reciprocal; access for the exports of the regional grouping to the northern anchor would be conditional on the regional group removing restrictions on imports from the north.

The link between integration with a major market and increased FDI seems to be confirmed by the experience of Portugal and Spain when they joined the European Community (EC). FDI to those countries increased significantly, apparently showing the close link between increased FDI and regional integration with a very important market. However, it should be stressed that participation in a regional market though necessary is not a sufficient condition for a developing country to attract FDI. Greece joined the EC, but did not experience a large increase in FDI inflows. (Griffith-Jones et al., *op. cit.)*

A key question posed by Gunning (1995) is how the sub-regional groups should be organised. He proposes the formation of small groups of nations submitting themselves to a participating supranational agency, following

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the model of the franc zone. Such an arrangement may attract foreign investment for two reasons. First, it creates credibility which attracts investment by reducing option values. Collier and Gunning (1995), Fine and Yeo (1994) and Gunning (1995) argue that if there is no uncertainty about whether (and in what direction) policy will change then investors will have no incentive to remain liquid or engage in what has come to be known as "foot loose investments". This is important since there is growing evidence that policy uncertainty is currently the main impediment to foreign investment in Africa. However, Elbadawi (1995b) argues that even in the aftermath of stabilisation (in Latin America and now SSA) it has been observed that capital (new or flight capital) does not return and even if it does, it is usually placed in liquid form rather than irreversible assets. Anecdotal evidence suggests that the recent repatriation of capital flight and the flow of new private capital in SSA following trade and exchange liberalisations may be motivated by speculative behaviour. When the domestic rate of return is not sufficient to warrant the risk of repatriation, no capital comes in.

Another point that has been raised regarding FDI is relevant here. It has been argued that additional FDI and other capital flows, linked to regional integration, have important economic benefits, both of a macroeconomic kind (by providing foreign exchange that allows higher growth) and a microeconomic kind (by facilitating improvement of technology and management). However, there are also risks in capital flows, especially clear in non-FDI flows. Thus, surges in capital flows can – and recently have – led to overvaluation of currencies, which discourages exports, even though increased exports are precisely a key aim of regional integration. Clear examples of over-valuation arising from increased capital flows have recently been observed in Kenya and Uganda, and to a lesser extent, in Tanzania. Increased capital inflows may also partly replace domestic savings, and therefore lead only partly to increased investment. If insufficient capital inflows are channelled into increased investment in tradable, the country could be creating balance of payments problems for the future. If inflows are to a large proportion devoted to increased investment in tradeable (more likely in the case of FDI), their long-term effects are more likely to be beneficial. Recent events in Mexico have demonstrated that portfolio and short-term capital flows can be incredibly volatile, with very negative effects on countries' economies.

Finally, we should point to the importance of the "neighbourhood effect". Widespread return to democratisation of South Africa is likely to lead to a surge in FDI with South Africa possibly acting as a conduit for the rest of the sub-region. Much is expected of South Africa and the "regional pole" projected to emerge in the south with growth there.

Already, investment by South Africans in other countries in Africa are beginning to occur at an increasing rate. For example, South African Breweries has 50 per cent shareholding in Tanzanian Breweries; Alliance Airlines in a joint venture between South African Airways, Uganda Airlines and Air Tanzania; and Aero Zambia, a small private carrier that replaced the collapsed Zambian Airway, has its base in South Africa. In the rail sector, the South African Company Spoornet is already heavily involved with railways elsewhere in Africa. A number of South African financial institutions have subsidiaries in the Eastern and Southern African sub-region. The hotel and tourism industry is also attracting substantial South African investments in the sub-region. More recently, Kenyan registered banks have opened subsidiaries in both Uganda and Tanzania to take advantage of the improved investment climate in both countries.

The increase in cross-border investments is more likely to lead to enhanced intra-regional trade flows. However, South Africa could play a more significant role in both intra-regional trade flows as well as increased cross-border investment in Eastern and Southern Africa if present controls were removed. The contemplated liberalisation of trade and foreign exchange controls in South Africa in recent times is a necessary, but by no means sufficient, precondition for increase FDI in the sub-region. If on the other hand, this does not happen soon enough, there will be an influx of workers seeking employment in South Africa from the surrounding countries. This will exacerbate the current unemployment levels in South Africa which are already above 45 per cent.

The option of trade and foreign exchange liberation and hence possible increases in capital outflows has two distinct advantages. First, it will have a tendency to reduce the influx of job seekers into South Africa as employment opportunities at home increase. Second, it will increase the production of goods and services, not only for the domestic market but also for the region as a whole including South Africa itself which at present is a very high-cost producer because of inflated wages and very high tariff structures which were meant to protect domestic industries. By the same token, Africa awaits the revival of the Nigerian economy so that it can act as a growth pole in the west of the continent.

The statistics are too fragmented to allow a comprehensive view concerning the role of foreign direct investment in SSA, in particular of multilateral corporations, and its effect in the exports of manufactures from the region. Nevertheless, some general observations may be possible. Gunning (1995) observes that it is not sufficient to have a satisfactory account of export-related FDI in developing countries and that additional explanation is needed as to why multinational operations can become optimal when previously exports from the foreign country consisted entirely of good produced by foreign firms. He suggests three possible explanations: changes in credibility, changes in labour costs and changes in transport costs.

As long as government policies are seen as credible by foreign investors – which may be enhanced by the provisions contained in a regional integration arrangement – they have an incentive to engage in long-term investments and enlarge the production bases. As for wages, Gunning (1995) quotes some evidence from Biggs et al. (1994) that recent policy changes in Africa, particularly the large exchange rate adjustments under structural adjustment programmes, have led to a substantial fall in labour costs, sufficient to make Africa competitive in the supply of garments for both regional and extra-regional markets. Whether this will attract FDI is yet to be seen empirically. The recent experience in Mauritius, however, shows that the situation may not be as rosy as it sounds as increased exports from developing countries often face quantitative restrictions in developed country markets. Another important step taken by a majority of African countries has been the introduction of liberalised currency markets as part of structural adjustment programmes. They have generally made it easier for multinational corporations to repatriate earnings. Though freer exchange rate regimes have increased the cost of foreign exchange, they have at the same time improved foreign exchange accessibility and reduced delays associated with the central banks' queues. A number of countries (e.g. Ghana, Kenya, Uganda and the United Republic of Tanzania) have implemented such policies.

Improved transportation between African countries as evidenced by the large investment in the transport infrastructure in SADC has two important implications. It increases the incentives for FDI to take advantage of the reduced transport costs and, of course, the larger market. It also increases the credibility of the region as a viable trade bloc.

Latin America has experienced a surge in intra-regional exports, particularly in manufactured exports as a result of regional cooperation. A notable feature of the increased intra-regional exports is that products which encounter a relatively high share of their demand in the regional market exhibit more complex technological characteristics than exports channelled towards extra-regional or domestic markets (Ffrench-Davis, 1995). This is consistent with Elbadawi and Ndulu's (1995) finding that FDI, because of the higher level of technology embedded, requires a higher level of educational attainment for it to be more productive and hence contribute to a higher level of economic growth. Elbadawi (1995b), while emphasising the point of regional cooperation and policy credibility, argues further that deeper economic integration in a given region could permit expansion of the regional economy to generate the threshold scales necessary to trigger the much needed strategic complementarity, and to attract adequate levels of investment for the development of modern manufacturing and the transfer of technology within the region.

From the research carried out by the UN Economic Commission for Latin America and the Caribbean (ECLAC) and quoted by Ffrench-Davis (1995), two main conclusions emerge:

(a) The production of goods which depend to a greater extent than others on intra-regional trade has more sophisticated technological features. Such goods are to be found mainly in the chemical sector, non-electrical machinery and transport equipment. They are also sectors in which international demand tends to be more dynamic. Their price trends are more stable and more positive over the long term than traditional exports, which over the years have faced wide fluctuations in world market prices.

(b) The sectors which exhibit a strong export drive toward the region also tend to show (sometimes with a lag) a drive towards extra-regional markets, which suggests that the promotion of intra-regional trade complements the promotion of extra-regional exports. Significant amount of effort has gone to promote intra-regional trade in the Southern African region by identifying obstacles and opportunities, e.g. trade facilitation in SADC and trade information network in COMESA.

The methodological and theoretical advances in the recent literature on development and economic growth and the lessons from the East Asian development strategies suggest the following broad ideas for African countries. Regardless of the trade orientation or the chosen development strategy, respecting fundamental macroeconomic balances and static efficiency rules on a sustained basis is an essential pre-requisite (Elbadawi 1995b). Intra-regional trade and investment flows can be raised in several ways.

First, in order to attract foreign portfolio investment, it is necessary to institute credible stock markets as well as develop new financial markets, a feature that is still rudimentary at best in most countries in the region. Several countries are currently engaged in setting these up but much still needs to be done in establishing the credibility of these markets and establishing the required confidence to operate in them.

Second, is the issue of the very large external debt overhang currently compounded by a growing overhang of public domestic debt. The uncertainty such overhang generates with respect to the stability of the macroeconomy in the future and contingent taxes to service it remains a major bottleneck to the confidence of investors and expected returns to portfolio investment. Unless a solution to this problem is arrived at, SSA countries will be hard pressed to position themselves to benefit from both direct and portfolio foreign investment.

A third factor, stressed by Fine and Yeo (1994) is that regional integra-

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tion may enhance FDI as foreign firms are attracted to a larger and better integrated market. As noted by Gunning (1995), this form of FDI is aimed at the domestic market, and not necessarily for the regional market although spillover effects into the region may occur.

A fourth channel through which regional integration could attract FDI is derived from applying specific set of assumptions to a popular model in the modern FDI literature (see Gunning, 1995). Assuming that multinationals consider producing abroad for export to the home market, Gunning shows that a combination of policy credibility, lower wages and transport costs could stimulate FDI. To the extent that regional integration in SSA achieves the above four requirements, it could stimulate export-oriented FDI.

In an attempt to determine the effect of FDI on intra-regional trade flows we use a model where the log of manufactured exports as a proxy for intra-regional trade flows is considered as the dependent variable. Total manufactured exports are used as a proxy for intra-regional trade flows because of lack of data on intra-regional trade in manufactures. By and large, manufactured exports are destined in the regional markets because they cannot compete internationally. We also use human capital development as exemplified by the level of secondary schooling to have direct effect on FDI inflows and hence on manufactured exports. The log of the product of FDI and secondary education is used as an explanatory variable to take into account the fact that FDI requires a higher level of human capital development for it to be more productive. The level of the countries' development as exemplified by GDP and GDP per capita is of course important. A decadal average of the ratio of FDI to GDP and the log of the decadal average of GDP were used as explanatory variables. We also use regional dummies to account for the fact that some regional groupings have benefited more from FDI than others and that this may have contributed to the increase in manufactures exports for the regional market.

Regression Equation

$$\begin{aligned}\text{LMEXP} = \alpha &+ \beta_1\text{FDIGDP} + \beta_2\text{LFDISEC} + \beta_3\text{LGDP} + \beta_4\text{ECOWAS} \\ &+ \beta_5\text{CEAO} + \beta_6\text{MRU} + \beta_7\text{CEPGL} + \beta_8\text{UDEAC} + \beta_9\text{COMESA} \\ &+ \beta_{10}\text{SADC} + e\end{aligned}$$

Variables

LMEXP:	The log of the decadal average of exports of manufactured goods.

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FDIGDP:	The decadal average of the ratio of foreign direct investments to GDP.
LFDISEC:	The log of the decadal average of the product of FDI and the ratio of secondary school enrollment to school age population.
LGDP:	The log of the decadal average of GDP.
Regional Dummies:	1 if both countries belong to the regional grouping and 0 otherwise; ECOWAS, CEAO, MRU, CEPGL, UDEAC, COMESA, SADC

Method of estimation = Ordinary Least Squares.
Dependent variable: LMEXP.
Number of observations: 58.
The results of the regression estimates are shown below and are heteroskedastic consistent (HCTYPE = 2).

Regression Results

Variable	Estimated Coefficient	Standard Error	t-statistic
C	.840906	1.63327	.514859
FDIGDP	-29.1721	12.2756	-2.37643
LFDISEC	.754207	.230199	3.27632
LGDP	.125317	.300314	.417288
ECOWAS	.374098	.433009	.863948
CEPGL	.464306	.406814	1.14132
COMESA	.524989	.404388	1.29823
SADC	.643789	.424564	1.51635
CEAO	.725922	.240655	3.01645
UDEAC	1.08720	.484346	2.24468

Mean of dependent variable	= 7.18652	Adjustment R-squared	= .566159
Std. dev. of dependent var.	= .822012	Durbin-Watson statistic	= .602769
Sum of squared residuals	= 14.0711	F-statistic (zero slopes)	= 9.26494
Variance of residuals	= .293148	Schwars Bayes. Info. Crit.	= -.716242
Std. error of regression	= .541432	Log of likelihood function	= -41.2252
R-squared	= .634660		

With low and declining GDP growth rates, the ratio of FDI to GDP has been found to be a significant determinant of manufactured exports although with a wrong sign (see also Figure 2) which is a reflection of the declining GDP growth rate and increasing FDI. However, the log of GDP has been found to be insignificant in determining manufactured exports. This is inconsistent with earlier findings relating GDP growth rates to the growth in manufactured exports. A more striking result is the product of FDI and secondary schooling indicating that FDI, which embodies a much higher level of technology, requires a much higher level of human capital to enhance its productivity and contribute more positively to the growth in manufactured exports. It has further been observed that using a decadal average, the trend of manufactured export as related to FDI portrays an upward trend, though fluctuating, over the period 1970 to 1993 (see Figure 3). Dummies are used to take into account the various regional groupings.

For the regional groupings, preliminary results of the econometric estimation indicate that the ratio of FDI to GDP, the product of FDI and the level of secondary education as well as the log of GDP jointly influence the intra-regional flow of manufactured exports in CEAO and UDEAC with significant levels above 90% and SADC at 80%. These results are consistent with the results obtained in estimating SSA trade potential using the gravity model. It has been argued (Mistry, 1995) that within some common monetary areas and in regions where currency convertibility has been achieved, there is both current account convertibility and a fairly liberal capital account transfer regime, though the capital account transfer need not necessarily be within the regional grouping. If the above results are anything to go by, FDI, along with the other variable identified, seem to have significant influence in the increased intra-regional flows in manufactures and possibly cross-border investments in CEAO and UDEAC – two regions in a monetary union.

A general review of FDI entry procedures would not be sufficient without reference to the relevant sectors which also impinge on the approval process. For example, in all African countries, minerals and petroleum in the ground are the property of the State and no one can prospect, mine or produce them without a license. Besides having to comply with the basic requirements of the FDI legislation, investors in the mining and petroleum sectors therefore have to undergo additional approval procedures under the mining and petroleum laws of these countries. Such sectoral laws could, if not reviewed, in some instances defeat the purpose of new FDI laws.

A major benefit of RIAs in the developing world should be immediately seen through an expanded inflow of foreign direct investment into the region. Even in the European Union this effect has been pronounced initially vis-à-vis inflows from the USA, and more recently from Japan and East Asia. In addition, cross-border investment flows from within the region can yield significant benefits. To the extent that these two categories of investment depend on the creation of a regional market, extra-regional FDI and intra-regional cross-border investment will both be influenced by the trade and production barriers, and by the hindrances represented by investment licensing. The removal of these barriers is a precondition for exploiting the gains from investment under RIAs.

Some investment incentives take the form of duty drawbacks or rebates; others take the form of tax holidays. Direct subsidies may also be used. All parties to an RIA have a legitimate interest in the incentives offered by the others, since these may affect the level and location of regionally justified investment in the bloc and thus also affect the direction of trade, and the distribution of the benefits of integration. If investment incentives are provided in the context of regional integration agreements, this should be done directly and openly, in a way that does not raise the price of products to consumers. If existing incentives could be shifted to such a basis, one of the major distributional obstacles to operating a customs union would be immediately overcome.

It has been argued (Mistry, 1995) that the constraints posed by non-tariff barriers to cross-border investment in developing regions are real. First, except within the common monetary areas, exchange control and investment licensing controls usually apply. Second, it is in the nature of developing countries that domestic capital is perceived to be short (when it is usually misutilised) and capital markets are generally under-developed. Finally, tax regimes are complex, the burden of business taxation is not uniform, and double taxation agreements among developing countries within a region are not very common.

Future external funding in SSA may require some degree of reorientation, for it to be more effective and these may include, among others: (i) a reorientation of donor funding with a more private sector orientation so as to avoid government debt overhang and to minimise donor fatigue; (ii) more efficient mobilisation of private foreign capital both direct and portfolio; (iii) aggressive mechanisms to attract African flight capital; (iv) more efficient means of mobilising and rechannelling personal remittances; (v) development of new financial institutions such as funds, venture capital, leasing, stock markets, women's finance institutions, rural banks etc.; and (vi) development of new financial instruments like guarantees, industrial funds, debt/equity swaps etc.

V Conclusions

In the past three decades, there have been several initiatives toward regional integration and cooperation in sub-Saharan Africa. However, while the need for economic integration received widespread support, both

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on pragmatic grounds and as a step toward African unity, very little progress has been made.

The main thrust of early initiatives was to promote preferential arrangements for intra-regional trade, so as to expand markets and reap efficiency gains from larger-scale production. This was considered to be particularly important for import-substituting industries. The first generation of such initiatives were unsuccessful for three main reasons: complementarity in production was too low to foster fruitful exchange; payment arrangements to circumvent the problem of inconvertible currencies were inadequate; and overriding concerns of individual countries with their own industrial plans made it difficult to arrive at an acceptable distribution of costs and benefits from the schemes. The collapse of the once successful East African Community was particularly unfortunate.

In short, integration efforts have been driven more by unrealistic political aspirations and bureaucratically defined blueprints than by their real potential. Despite over 50 regional organisations, there has been little actual economic integration. By and large, the successful cross-border networks of traders which have developed have done so more in spite of official policies than because of their support (Global Coalition for Africa, 1995).

Although intra-regional trade flows have been limited, the potential to increase such flows exists. Increased flows of FDI could foster enhanced intra-regional trade flows. Since most SSA countries have extensively liberalised their trade and payment mechanism, an enabling environment for FDI flows has been created with possible increases in cross-border investments. Investment liberalisation should be combined with other measures aimed at improving the investment climate such as investment promotion and protection; the strengthening of the general legal framework relating to business activities (including especially company law); and, in the light of the interrelationships between FDI, trade and technology, ensuring the consistency of their respective policy frameworks.

The results of econometric estimation point to the importance of human capital development for enhanced economic growth. This suggests that African governments should place special emphasis on education expenditures (particularly secondary and technical education) if past growth declines are to be reversed.

A striking feature of regional integration arrangements today is their expanded scope in terms of policy measures and diversity of objectives. In this regard, there is a window of opportunity for SSA to use regional integration as a supranational mechanism to foster policy credibility, and as a means to pool risks between otherwise vulnerable small economies; to resolve conflicts and minimise political risks; to exploit complementarities

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and to develop regionally-based links on a reciprocal and mutually beneficial basis.

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Comment on "Integration of Trade and Finance in Africa," by William Lyakurwa

Mohsin S. Khan[1]

Introduction

This is an interesting and informative paper combining a nice mixture of normative and positive economics. The paper is divided into two related parts: first, it contains a general discussion of regional trading arrangements (RTAs) in Africa and provides some empirical evidence on the trade potential in these arrangements. And second, it looks at the relationship between RTAs and foreign direct investment. This latter part of the paper is relatively new, in that this issue has not been hitherto rigorously examined when considering the issue of RTAs. This comment can be conveniently divided in a similar way.

Regional Trading Arrangements: General Aspects

It is widely accepted that the first-best trade policy is liberalisation on a most-favoured nation (MFN) basis. When a country chooses to participate in an RTA, it should do so in a manner that is compatible with the process of multilateral trade liberalisation.[2]

The paper accepts this general view, arguing that RTAs in Africa indeed have the objective of trade liberalisation, first among members and then between the group and the rest of the world. It then goes on to say that RTAs can be quite successful in increasing intra-regional trade. This is a somewhat controversial conclusion, and there are several issues and questions that can be raised about the analysis that supports this conclusion.

First, in discussing the "success", or lack thereof, of RTAs in sub-Saharan Africa (SSA), the author does not seem to make a distinction between two kinds of success/failure: (i) failure of completed regional trade

1 The views expressed here are the sole responsibility of the author and do not necessarily reflect the opinions of the International Monetary Fund.

2 As a minimum, RTAs should be consistent with the obligations of GATT Article XXIV. These obligations include, among others, that substantially all trade among members be liberalised, that extra-regional trade barriers not be raised, and that these arrangements be notified to the World Trade Organisation.

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liberalisation to produce regional economic benefits; and, (ii) failure of a regional liberalisation initiative to achieve substantive regional liberalisation. The two are not the same. The former would attempt to say something about the expected welfare consequences of regional integration, while the latter would look at the political economy of regional integration initiatives in SSA.

Second, what is important in terms of prescriptive public policy analysis is not an estimate of the potential for expanding intra-regional trade, but some indication of the associated welfare effects. At times, it seems that the author simply equates increased intra-regional trade with increased prosperity.

Third, regarding the proposition that RTAs can help to lock-in trade reforms and that unilateral reforms have been time-inconsistent, it should be pointed out that the multilateral trading system also offers policymakers a chance to lock-in trade reforms through tariff bindings. The question is why countries of SSA appear to be able to make regional trade liberalisation commitments that they cannot make multilaterally. One answer is that many of these regional commitments are not typically kept, or they are delayed over long transition periods, or in practice they cover only a limited amount of total external trade as intra-regional trade in Africa is generally low.

Finally, the author discusses the possible need to provide, in effect, "side-payments" to entice partners to join the RTA. However, there is no explanation why some countries would be willing to pay these, apart from the case when they expect to benefit from trade diversion. Can one argue that this was why South Africa agreed to a formula to redistribute SACU tariff revenues that benefitted its neighbours? Might the prospect of such side-payments stimulate rent-seeking by some potential members and possibly inhibit the formation of RTAs?

To provide empirical estimates of trade potential in the various RTAs currently in place in Africa, the author estimates a standard gravity model of bilateral trade flows augmented by dummy variables for eight regional integration arrangements in SSA. A positive and significant coefficient on these dummies – obtained in four of the eight cases – is interpreted as evidence of "significant trade potential" within that regional arrangement. In my view, such an interpretation is not necessarily correct. "Trade potential" is a dynamic, forward-looking concept that either takes as a benchmark the prediction from a well-structured trade model (say, the standard Hecksher-Ohlin model), or that tries to capture in some way the efficiency/trade gains from: (i) the elimination of trade distortions; and/or (ii) the expansion of the market size. It is difficult to argue that the dummy variables in the regression are capturing any of these effects, especially

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since the coefficients are obtained for a period where the regional integration attempts were plagued with serious deficiencies – in terms of their overall orientation and incentive structure. In fact, I would argue that the "trade-enhancing" effects that the four arrangements where the dummy coefficient was significant appear to have had were not welfare-enhancing, as they are likely to have fostered the "wrong-type" of trade. One has to be careful with this type of analysis, since econometric evidence of trade potential does not separate "trade potential" which derives from trade *diversion* from that which derives from trade *creation.* Because most SSA countries maintain rather high external tariffs, the potential for trade creation – increasing intra-regional trade – may be well high, but increased trade may equally well represent trade diversion, i.e., a shift in consumption patterns from low-cost to higher-cost suppliers.

RTAs and Foreign Direct Investment

The paper also makes a novel argument in favour of RTAs, namely that they may lead to an increase in foreign direct investment (FDI). To date, Africa has received a very small share of FDI going to developing countries. For example, between 1990 and 1995, all developing countries received approximately $245 billion of (net) FDI. For the same period, Africa only received $10 billion. The 1996 net FDI to developing countries is projected to be around $55 billion, with Africa getting about $3 billion. Clearly, any measures that increase Africa's share in the flow of FDI would be of enormous benefit to the continent.

Are RTAs a way of generating an increase in FDI? The author basically relies on an extension of the argument that FDI has tended to go to larger markets. An RTA is undoubtedly a larger market, and this should benefit FDI. But at the same time, a larger market is only one – and by no means the most important – factor influencing FDI. Many other factors are important, including macroeconomic stability, currency convertibility, political stability, favourable rates of return, and flexible labour markets, to mention a few. In general, FDI has proved to be notoriously difficult to explain, let alone model in an acceptable fashion.

The author does make a brave attempt at modelling the relationship between RTAs and FDI in Africa, but does not control for the myriad other factors driving FDI to developing countries. Two specific points are worth making regarding these empirical estimates.

First, due to lack of data, the author uses (the log of the decadal average of) manufactured exports as a proxy for intra-regional trade flows. It is apparent that the correlation between these two variables cannot be taken for granted. It is not fully clear why the author opted for focusing on the

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"manufactured" dimension of intra-regional exports over the "intra-regional" dimension (on which he had the data that was used in the estimates of trade potential); be it as it may, the author needs to provide some evidence in support of the existence of a relation between manufactured exports and intra-regional trade in SSA.

Second, the conclusions from the empirical results on the relation between exports and foreign direct investment (FDI) need to be stated more cautiously. The coefficient of the ratio of FDI to GDP has the wrong sign! As such, it is not particularly meaningful to interpret too strongly the significance and sign of the interaction between FDI and education.

Conclusions

In summary, I feel that the paper makes an interesting start in looking at how RTAs could be helpful in attracting foreign direct investment to Africa. Intuitively, this idea makes a lot of sense. The author should also be commended for pushing the argument further by providing empirical tests of the hypothesis. While the results are weak, they nevertheless represent a useful beginning. Africa has to attract foreign direct investment and RTAs may be a way to do it, providing of course, the other factors typically affecting foreign direct investment are playing their respective roles. In that sense, the paper does have considerable policy relevance. At the same time, should one be optimistic about the future success of RTAs in Africa? The author's own brief description of the history of such arrangements says otherwise.

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Comment on "Integration of Trade and Finance in Africa," by William Lyakurwa

Louis Kasekende

There is always a problem when speaking last because most of the views have already been covered and for this particular topic a number of aspects related to it were extensively covered yesterday. In my comments, I want to focus on three issues which are also relevant to the earlier presentation by Ernest Aryeetey:

- One is that the regional groups were designed without regard to incentives to the contracting partners, and compensation mechanisms;
- Two is that adopting a framework of cooperation inappropriate to the current economic realities is a recipe for subsequent failure;
- And third is the lack of credible penalties for delay in implementation or non-implementation.

Trade Promotion

The gravity model Bill uses reaffirms an earlier view that there is a trade potential. The question Bill puts forward is, 'Why hasn't it been exploited?' Part of the answer concerns infrastructural links and trade promotion, but that is not all. There is one thing that we have to recognise and that is trade liberalisation. This has occurred in most of the countries since 1985, and more so in the 1990s. One has to link regional integration, the schemes that we have, the institutions that we have developed and the instruments, and see whether they are compatible and consistent with the current liberalised environment in the cooperating partner countries. One thing that I really welcome is the recognition of the critical role of the private sector. In a number of countries with more liberal trade and investment regimes, the private sector has actually been given a more active role, and we should take them into consideration if we want to promote trade.

Furthermore, under the liberal economic environment, countries have eliminated export licensing, allocation of foreign exchange and quantitative restrictions on trade. If the region has a system which is designed to exploit controls in promoting intra-regional trade, then liberalisation is likely to reduce trade flows. Related to this, the private sector currently makes

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business decisions relating to the financing of international trade without reference to central banks. The financing of imports is fully handled by commercial banks and there are no restrictions on the sourcing of imports. The producers within the region must be competitive if they are to be preferred to non-regional producers. The case of South Africa is illustrative. Between 1990 and today, South Africa has broken into a number of areas without trade preferences. They are not a member of COMESA and so a very important question is: How have they done it?

There is the other issue relating to institutions which are inconsistent with the current institutional arrangement for financing trade. Currently we have a PTA Clearing House that is linked to the central banks, but the central banks are no longer directly involved in financing trade; trade is financed at the level of commercial banks. So if we want the businessmen to take advantage of the credit arrangements offered by the clearing house, the commercial banks should become members of the clearing house. It no longer makes a lot of sense for the central banks to remain members of the clearing house (except at the level of providing credit guarantees). In Bill's paper, it is recognised that business conducted through the clearing house has declined significantly in the recent past.

The other instrument – this is in terms of promoting travel – that we have in the COMESA region (and I am using COMESA as an example) is the UAPTA travellers cheques. The PTA Bank continues to aggressively promote the UAPTA cheques in addition to prevailing over member states to do the same, but the travelling public does not want to use them. They prefer other fully convertible instruments. We have to re-examine the UAPTA travellers cheques with a view to redesigning them. One of the constraints is that it is only convertible into the regional currencies and circulation is limited to the COMESA region.

The other issue in terms of promoting trade in the region is the issue of non-tariff barriers. There are so many policy reversals in this area. Uganda, for example, has a ban on imports of beverages, for reasons relating to tax revenue. That is the same point Mohsin Khan has raised of assessing the impact of removing such bans on tax collections. Kenya, from time to time, has also imposed bans on importation of maize. We should look at all these non-tariff barriers. If we are going to promote trade on a sustainable basis, such measures have to be eliminated. There are also issues relating to transit requirements which vary from time to time, constraining free movement of goods. In fact, this point also relates to the issue of attracting foreign investors. If we have these policy reversals coupled with non-tariffs barriers and infrastructural constraints, it will be difficult for the region to attract foreign investors to take advantage of the large COMESA market.

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Foreign Investment

With regard to FDI and regional integration, I agree with quite a number of views expressed in the paper but I just want to add on a few issues. One is that the author has recognised that a number of countries within the region have eased conditions for FDI. A number of them now have revised investment codes, providing for repatriation of profits and dividends and have simplified the approval process. In Uganda, for example, we have a one-stop centre; it has taken a strong lead in publicising investment opportunities. The President has also played a supportive role by joining investors' search missions. Second, parastatal reform is another key factor in attracting foreign investors. In addition to this, one factor that we have to emphasise is a stable macroeconomic environment.

Still, having put all these in place, the flows remain small and we have to learn from the country experiences. In the case of the East African region, the flows that have responded to this environment were private transfers which increased substantially. Next in line are short-term trade flows. But beyond that, there has been very little. I think there is a timing issue. There must be confidence building and it will take some time, and that is at country level. A number of other issues come into play such as sustaining macroeconomic and political stability within the whole region.

How do we achieve policy sustainability? The regional bodies do not always have effective mechanisms for ensuring implementation of agreed policy decisions and guarding against policy reversals. There is need for weaknesses in regional groups to be addressed if investors are to take advantage of regional investment opportunities. For now, investors will move resources to exploit investment opportunities at a country level. Such investments may expand to take advantage of the regional markets.

Let me share with you some examples of where a policy change stimulates investor interests. First, when the currency convertibility within the East African region was announced, a number of investors came to my office inquiring what it meant for the East African region. I think there must be investors who want to take advantage of the East African market. The case that Bill has just mentioned of tourists is one of them; tourists are coming in, maybe in Kenya, and taking advantage of the other sites within the region.

Second, following liberalisation, we have seen cross-border investments, especially in the financial sector. Banks in Kenya have started moving into Tanzania and Uganda. We also have one bank from Uganda which has set up a branch in Tanzania. Third, when we liberalised coffee marketing in Uganda, a number of companies moved into coffee marketing and these are mainly European-based companies. Similarly, following the liberalisation of cotton growing and marketing, a number of companies, especially

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South African companies, have invested in the cotton industry in Uganda. Since the telecommunications area was liberalised, a number of South African companies have moved in. This was also observed in the Airline business where a joint Airline service between Uganda, Tanzania and South Africa has been set up with South Africa as a major shareholder.

So there is evidence of the "neighbourhood effect" and I think we should exploit it to the maximum. If the South African investments yield positive results, then we may see other investors from outside the region also coming to take advantage of the investment opportunities.

Government Policy

I want to end with some issues which need to be addressed. One is the issue of policy coordination. The countries in the region have been implementing structural adjustment policies, but the speed has varied and the sequencing has varied. It becomes extremely difficult to coordinate policy.

An attempt has been made by the Governors of the three central banks in the East African region to share experiences and also to identify areas of cooperation for the benefit of strengthening the reform process. Given the fact that policy emphasis in the three countries is different and that the autonomy of the central banks is limited, there have been problems in implementation of decisions. Currency convertibility announced by the Governors in September 1995 for implementation by end-November 1995 had not been fully implemented by Kenya by end-January 1996.

The other issue relates to COMESA. We previously believed that bigger was better, especially when referring to economies of scale. But in the case of COMESA, we have stretched it too far. Egypt has expressed interest to join the region and Zaire has joined. Even if we do not have an idea of the appropriate size, we need to rethink this particular regional group. The decision-making process becomes increasingly complicated as the number of member countries increases.

Last, I turn to the possible role of the private sector in regionalism. We have said that the private sector should be given a key role, but there are times when the private sector becomes an obstacle to regionalism. The manufacturers, for example, always agitate for protection and are, at times, a source of policy reversals on the issue of opening up the economy to competition. The private sector needs to fully appreciate government policy and regional policy if they are to be supportive.

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Floor Discussion of the Lyakurwa Paper

Mohsin Khan from the IMF began the discussion by relating the issue of trade integration to foreign direct investment. "There are two separate issues here. One is, what drives foreign direct investment in Africa? While some individuals are looking to South Africa as a conduit for investment, I'm less optimistic. One of the things we discover consistently in reading the surveys of businessmen is that they are looking for areas which have political stability, currency convertibility and flexible labour markets. What does flexible labour markets mean? To be candid, it means low-wage economies and lack of unionisation. That's what they're looking for. And so the chances of large-scale foreign direct investment taking place in South Africa from multinationals are slim. Most of the capital coming into South Africa right now is like the capital going into Uganda. It's short-term money; it's basically taking advantage of rates of return. There is foreign direct investment but not a whole lot.

I know of no serious study surveying businessmen who are either actually in the market in Africa or are looking to Africa as a possible market. I would propose that this type of survey be conducted. Now it's unlike me to say, 'Hold off on the econometrics, let's go for surveys.' But in this particular area, the survey evidence could be much more persuasive.

The second area concerns regional trading arrangements. As I mentioned earlier, from my own institution's point of view there is a greater openness to this concept of regional trading arrangements, but I hasten to add, provided this is leading to liberalisation. I think the problem that you're observing right now is that countries are at very different stages of liberalisation. Uganda, for example, has an effective tariff right now of 20% which continues to decline. If the tariff comes down to 10% over the next few years, it's not going to make a big difference to Uganda whether it joins a regional trading arrangement or doesn't. It didn't even matter when it was 200%. Do you want to use regional trading arrangements in order to integrate in a better way with the rest of the world, from a stronger position? Or is it a question of self-reliance in that you want to hide behind walls because you don't want to integrate?

Let me end by saying that it's a bit difficult for me still to be optimistic about the future success of regional trading arrangements in Africa, partly because history hasn't been very good in that context. Some people really feel that South Africa will lead the way and yes, now you've got a big player that has its act together in some sense and could provide the impetus for regional integration. But one might question whether it is entirely

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in South Africa's interests to be a member of regional trading arrangements. Politically, it is of course, but from an economic standpoint, it is a worthwhile question."

Percy Mistry suggested that along with surveys, industry studies should be conducted as well in Africa. "When we were doing our African Development Bank study, we noticed that Africa is very short of industry studies and inter-industry and intra-industry linkages. People keep tossing out numbers about factor productivity efficiency based on aggregates, without any appreciation of what really is there on the ground, and much of it is hidden. There are some extremely efficient private sector firms in Africa who simply operate outside the recorded economy. We need to know far more about it. Trade economists should look at the residual linkages, stripping out what I call the Africa-with-the-world colonial economy type trade, which actually hasn't changed much in 45 years, and that's the tragedy of Africa.

Point number two. I'm a bit confused by your projections for 1996, Mohsin, on FDI. You've talked about $55 billion to developing countries. I assume that's net because the gross figures are much larger. Now if that's net and you say 33 for Asia and 17 for Latin America, that's 50, plus 3 for Africa; only leaves 2 for Eastern Europe and other regions. That can't be right. Apart from which, what worries me is, out of the 3 to Africa, 2 will go to South Africa and the rest will really be distributed between Kenya, Côte d'Ivoire, Mauritius and Zimbabwe. Here again to talk about Africa *qua* Africa, as opposed to the four or five countries, really leads to fallacies of aggregation, and one needs to be careful about that. But I'd really like a relook at that number.

The third thing is most econometricians give too much attention to prima facie numbers, and perhaps Bill falls into that problem as well, because one of the things about econometrics is you're desperate for a data series that makes some sense, even if in reality it conveys nothing. In Africa, outside of SACU, stated tariffs mean nothing. Because most of the cross-border trade that actually occurs on both exports and imports is through negotiated tariffs at the border. Looking at nominal tariffs and making a whole series of postulations based on nominal tariffs for Africa is very misleading.

Also, Africa suffers from something that no other developing country or region suffers from and that is both tariff exemptions and massive trade distortions caused by tied aid imports. This has been particularly high during the import-support period. Again, if you're going to do econometric analysis, you obscure a lot when you don't take those distortions into account. The southern African region, excluding SACU, is a major victim of this because for Zambia and Mozambique, foreign aid accounts for such

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a huge volume of import financing that you really can't make much sense out of it unless you actually analyse the distortions that take place.

With regard to FDI, the Cross-Border Initiative and privatisation, I think Mohsin has pointed to one very important feature, which is actually characteristic only to Asia and nowhere else. The Japanese, Koreans and overseas Chinese have very powerful herd instincts and competitive instincts. If they see family member X investing somewhere, they're there right after him. In fact one even sees it in Mauritius, which leads to an over-investment in things like knitted gloves, of which Mauritius now provides 97% of the world's supply. But that is not true of European and American investors and it is certainly not true of Indian investors. It is not even true of South African investors, although there's a South African predilection for things like breweries, mining companies, food processing companies, hotels and those kinds of related investments.

I think there will be cascade effects. I actually agree with Louis Kasekende that there will be a lot of volume FDI coming into South Africa, not just repatriated South African capital, but also companies that exited South Africa in sanctions, which are going to rebuild their market base. I mean basically it's an asset swap in the sense that it's not new FDI – it's new incoming investment taking over assets which already exist with a cash swap. Second, India has a very important economy for Africa, especially the Eastern and Southern seaboard is much more liberal than it ever used to be. Third, I think African approaches to Indian investment, or sub-continental investment, are changing as one sees in Uganda. And there is some of that repatriation, not only of the Ugandan and Kenyan and Tanzanian Asians, but Indians from India now wanting to invest in these countries. And you're beginning to see Mauritius become an entrepole for that.

One also has to look at two other kinds of behaviour as far as FDI is concerned, which is the FDI-related enclave investments in minerals and plantations, and FDI-related privatisations where Africa has really shot itself in the foot. Africa could have competed much more for FDI, particularly from Asia, if it had privatised faster, particularly in utilities."

Jeffrey Fine, formerly with the International Development Research Center in Canada, brought up the issue of debt overhang in relation to foreign investment behaviour. "One question is rather critical in terms of the foreign investment behaviour and that is the whole issue of debt overhang, which I think requires a lot of work. Because clearly it means that depending on who is driving public policy, to what extent the policy is actually going to remain credible in the long-term and of course whether you can repatriate; a number of issues rest on the overhang issue and the flow of investment.

The second key issue which Percy mentioned is privatisation. It certainly is a key issue for South Africa at the moment, particularly with regard to public utilities and the telecommunications field. This is a domestic policy issue, but a lot of future investment flows will hinge on it. I also think that it is driving a lot of South African investment in certain sectors into the rest of the region.

A third issue has to do with resource-based commodity production in Africa. Percy says that Africa needs to get out of this type of production and look at the residuals, but the fact is that growth is going to be based on resources, renewable and non-renewable. Another issue in this context is the whole question of transaction costs of this type of trade. With the revolution that is occurring in informatics and telecommunications, the marketing chain is collapsing. I can sit with my Internet in Canada and pick off a trade base which is literally a huge database that will tell me by sector, by country, by manufacturer, the particular business opportunities. I sit and I say, 'Well if I'm in Africa, where's my opportunity?' The transactions costs of doing trade in what are relatively small markets is extremely high. So I raise that as an issue on the regional integration front in terms of what's driving it, at what we might call a micro level or technology level.

My last point is what I would call the opportunity cost of international trade agreements. Countries in this region have very limited expertise and capacity to negotiate international agreements. That's a fact. Trade law and knowledge of the country takes a long time to cultivate. Certainly this is the case when you go into something like a NAFTA. This is an enormous investment of very skilled time and personnel. So I ask from a point of view of countries that are sitting in this region and even South Africa, given this high opportunity cost, where do you put your first eleven in terms of negotiation and the work of time? Do you put it into negotiating a *regional* agreement which has very limited value and is quite problematic? Do you put it on international agreements, where you see major markets? Or do you put it also on bilateral agreements within the region with countries that want to negotiate with you, say Zimbabwe in the case of South Africa?"

Uka Ezenwe from the Department of Economics at Ahmadu Bello University suggested that it was not the politicians who are involved in the integration of trade, but market men and women. "Once they find economic opportunities, they will exploit it, whether or not you have integration. You have to ensure that they have proper exchange rates, that the tariff system is right, the political environment is good and that people can move about. It's not whether people are willing to buy. People are willing to buy if they find they are going to make profit at the end of the day. In fact, most of the time, particularly in that massive region, the most active operators are women in most of the countries of the sub-region. They buy

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all sorts of things from one country to another to sell. The problem is not political economy or political differences between individual countries. Peasants are definitely not interested in politics, they are interested in survival, and integration is for them and should be made to serve their purpose.

The other thing that attracted my attention was the point made on the issue of providing incentives. I am not as optimistic as you are about the importance of incentives. Other factors such as political considerations, the nature of labour markets and so on play a more important role I think. Investments don't come because there's a tax holiday. If they are not sure of political stability, they are not sure they will repatriate their profits. I think those are more important than these incentives you are talking about.

The last point concerns privatisation. What are the limits of privatisation? In some African countries, corrupt politicians and businessmen have bought up public assets at very low prices and they have been encouraged to do so. Also, some countries are selling their basic industries to foreigners. A glaring case is the Ashanti Gold Mine. I'm not providing any answers, but I think the question is an important one. If you're selling all your basic industries to foreigners because you have a foreign exchange problem today, tomorrow that foreign exchange problem will reappear when they start repatriating their profits."

Sam Tulya-Muhika, the director of an Ugandan consultants firm, thought that the paper over-focused on FDIs. "I know this is a new fad, that if you don't get private sector inflows, the economy is not going to grow fast enough. This is probably true, but I think there are other impediments that are detrimental to market integration in Africa, especially the compensation mechanisms.

The paper does not say enough about the importance of trade information. This is one of the major problems in Africa. Most traders in the COMESA do not know what opportunities exist for trade. There's no COMESA information centre in Kampala that provides such crucial information."

Samuel Wangwe, the Executive Director of the Economic and Social Research Foundation in Tanzania, returned the discussion to the issue of resource-based trade raised earlier by Percy Mistry. "Three years ago we did a study for a book which has just come out on African exports looking at industrialisation, technology and industry. In that study we looked at the manufacturing firms which were exporting or had just been pushed out of the export market in order to understand what is it that determines the capability to remain in the world market. We looked at fifty-five firms in six countries: Zimbabwe, Mauritius, Tanzania, Kenya, Nigeria and Côte d'Ivoire. I would like to highlight four quick points from that study which are relevant to this discussion.

One, the firms which were competitive had links with the outside world through foreign investment arrangements, market arrangements or by production arrangements in order to keep informed about technological advances and to undertake the same. FDI can have a positive bearing in terms of international competitiveness.

The second point from the study concerns which factors were important to investors. Three factors came out as most important: political stability, the policy climate and the infrastructure – including skills as well as telephones and electricity.

A third point has to do with regional trade in products which appeared to be regional specific for quite a while, like African prints for instance. With liberalisation, the regular markets were being lost to Asian manufacturers which were more dynamic. African prints, Kangas, are now being produced by Asian firms, and some of the African firms were being phased out of production completely. Within regional integration arrangements, if competitiveness is not assured, sooner or later the markets within the region may be lost to the more dynamic producers.

A final point from the study on African exports is that in a number of places, the competitiveness of the firms was not based on the cost level or price they charged, but on the appropriateness of the product to the peculiarities in the region – especially those which are sensitive to the kind of climate and soils we have. For these products, such as agricultural equipment, their competitiveness continues to be assured, even if the prices charged were higher."

Colin McCarthy, from the University of Stellenbosch, expressed concern about the future configuration of the labour market in South Africa. "I think it's still very anecdotal, but there are now signs of a different reason for South African foreign direct investment in the region and that relates to what Mohsin referred to earlier, namely flexibility of labour markets as a determinant of investment. A recent case has been the closure by Pepkor of their clothing plant in Butterworth, relocating it to Malawi. The reason being given is the perception of an inflexible labour market in South Africa.

In view of this, and if this should become a significant factor in investment flows in the region, one can expect that the South African Trade Union Movement will become a major player in the debate and in negotiations and discussions on regional integration. One doesn't need to have a very good crystal ball to forecast that the South African labour market will be the space to watch in the future, not only because of these capital flows at the cost of employment creation in South Africa, but also because

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of the growing inflow of migrants from the region into the South African economy which will tremendously complicate labour affairs in South Africa."

Dan Ndela, from Zimconsult, noted that South Africa has not been a participant in SADC and questioned whether a hub should be created around South Africa. "We've been talking about regional integration. SACU countries have been in a delegation which excluded South Africa, and South Africa is currently raising tariffs. The challenge is how do we create a hub around South Africa when in fact the hub is outside regional integration arrangement." Ndela also questioned the motives behind South African investment in the region. "Are they investing in the region to escape from unionised labour and inflexible labour conditions, or are they going there to exploit regional integration? These are issues we should be looking at."

Sam Asante, from the UN Economic Commission for Africa, warned of the potential deleterious effects of foreign direct investment on integration. "We are concerned about attracting FDI, whether at a national level or at a sub-regional level, and we do so without considering its effects on regional integration. In 1981 the ECA conducted a survey of UDEAC to determine whether the member states of that organisation had derived benefit from the large market which UDEAC had brought. We found that the benefits were actually going to foreign investors, transnational corporations, to the detriment of the member states of UDEAC. Why are we anxious to attract FDI when the benefits are scarce?"

Gene Tidrick from the World Bank elaborated on the issue of South African investment in the region. "I think South Africa is itself a major player in investment in Africa. South African companies see themselves as having a comparative advantage because they know how to do business in Africa. Rightly or wrongly, that is the way they perceive themselves. And so you see South African banks moving into the neighbouring countries and feeling very comfortable with competing with banks from Portugal in Mozambique.

Still, there's no doubt that a lot of South African investment would be motivated by lower labour costs for exporting back into South Africa; it has happened in Malawi. Moreover, if there were regional integration within SADC, no doubt you would get foreign investment attracted to the region, not so much to invest in South Africa or export to other SADC countries, but to invest in low-wage countries for export to the South African market. Because foreign investors also see South Africans as having a comparative advantage in dealing with the local situation in Africa generally; a lot of this investment would probably be of a joint venture sort if it is directed to a regional market. Foreign investors typically want to hook up with a local firm because they know the country's circumstances.

On an entirely different note, however, I would like to mention that Lesotho has recently been very successful in attracting foreign investment, Taiwanese investment in particular, for export of garments to outside the region. This is essentially a quota-shopping investment. Taiwanese firms who are facing quotas but have market links, can shift production to Lesotho. The attraction is twofold. One is relatively low labour cost in Lesotho – about a third to a half of South African levels – but the policy framework and the credibility derived from being part of the monetary area in South Africa also plays a role. It is a stable policy environment with relatively low wages."

Elty Links, from the South African Department of Finance, brought up the issue of establishing the borders of a region. "What determines the borders of a region that wants to integrate? This is a legitimate question, and it is the same problem that we have everywhere, including Europe, of historical borders being drawn for whatever reasons and then becoming impractical. It seems that our discussion on trade and FDI has led to the conclusion that there is no need to have such defined borders. Trade and FDI go wherever they want and the private sector is not being driven by the fact that we're SADC countries or COMESA countries. We should be concentrating on the question of the investment environment and the enabling environment that we want to create within a region. Financial policies, for instance, among countries must be such as to make it more conducive for investors to come in."

Response by William Lyakurwa

"On the physical complications of tariff reductions, I have examined this particular issue and the conclusions reached from the various country studies on the physical impact of trade policy reforms seem to indicate that it's not really a major issue. Some of the countries have liberalised far more than the regional integration schedules require and the tariffs are no longer binding, even within regional trading arrangements. So it wouldn't really be a big problem in terms of the physical impact. I accept the issue raised with regard to non-tariff barriers. It's an important issue in terms of explaining trade flows. They are not necessarily tariff binding, but non-tariff barriers play a significant role in terms of inhibiting trade flows.

The next issue I want raise is in response to Percy's suggestion of conducting an industrial survey. It might be an extremely difficult task both in terms of the logistics as well as the financial costs. Survey studies will definitely complement the results of economic estimations, but given the costs, I'm not quite sure it is worth the effort.

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In relation to the point raised by Mohsin, the discussion here as far as regional integration is concerned is not a movement towards self-reliance. It is more a movement towards the globalisation of the market. There are merits and demerits associated with moving from regional integration towards globalisation, and measures would need to be taken both at the national and at the regional level to mitigate any factors that will counter this move.

With regard to the point raised on debt overhang, I brought up this particular issue in relation to what role direct foreign investment could play in reducing the debt burden in two ways. One is making foreign exchange available, which would contribute to economic growth and reduce the debt overhang. Second, private sector participation in the national economies will reduce the dependency of governments on both the multilateral and bilateral donor agencies.

I raise the issue of privatisation mainly in relation to what national states can do in terms of their own *national* economic strategies, but they should still try and bring these more in line in terms of harmonisation of policies and strategies at the regional level so that it includes a regional dimension which supports regional objectives. The issue here is, to what extent national policy could be harmonised within regional objectives so that there is compatibility in terms of the privatisation, particularly in relation to strategic points like utilities and security.

On the impact of trade liberalisation on regional integration, national economic policy and growth, there is a significant amount of work that has already been done, particularly from networks relating trade liberalisation to regional integration and national economic policy-making. I didn't think it was necessary for me to summarise the findings of these studies but I may have to bring in a paragraph linking trade liberalisation and regional economic integration."

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IV Regional Dimensions of Structural Adjustment in Southern Africa

Percy S. Mistry

I Introduction

This paper attempts to draw out some of the important, yet imperfectly understood, interrelationships between second-generation regional integration arrangements (RIAs) and structural adjustment programmes (SAPs) which are being attempted simultaneously in Southern Africa (SAR).[1] In theory, these twin pursuits are neither contradictory nor mutually exclusive. In practice, however, they sometimes appear to conflict. As the whole of Africa provides too wide a canvas for a monograph such as this, its focus has been deliberately limited to integration and adjustment in one particular African sub-region which may have lessons for others.

Profound economic and political changes have occurred in SAR between 1990-94 suggesting the prospect of further transformations occurring in coming years which will influence integration and adjustment attempts in this region. Interestingly, in SAR and throughout Africa, RIAs and SAPs are being promoted simultaneously by the multilateral agencies and bilateral donor governments. The specific lending and technical assistance programmes of the International Monetary Fund (IMF) and the World Bank Group (WBG) point to the deep involvement of these agencies with both integration and adjustment in Africa. That is also true, if to a lesser extent, of the African Development Bank (AfDB). Judged by its efforts, the AfDB has, arguably, contributed more to the cause of integration in Africa than it has to original thinking about how African countries might adjust more successfully. The IMF/WBG, on the other hand, have been more obsessed with adjustment and have not focused enough on integration, often emitting ambiguous signals about whether they favour integration in Africa or not (Haarlov, 1995; Mistry, 1995c).

1 Throughout this paper, Southern Africa or the Southern African sub-region (SAR), is defined as comprising the 12 countries of the Southern African Development Community (SADC) in January 1996: Angola, Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe.

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Various United Nations agencies – including in particular UNCTAD, UNICEF, UNDP and the Economic Commission for Africa – have contributed to promoting the cause of integration in Africa while engaging more in critical commentary on adjustment. In the 1980s, the Economic Commission for Africa (ECA) advanced its own alternative notions of how adjustment programmes might be more appropriately designed for Africa (ECA, 1988), but unfortunately that initiative did not go very far because of opposition from the Bretton Woods twins in general and WBG in particular (World Bank, 1989).

Finally, the secretariats of the various regional integration arrangements (e.g. of the Southern African Development Community – SADC) which exist throughout Africa have also been caught up in concerns about the impact that SAPs are having on either advancing or compromising their particular RIAs.

It is astonishing, however, that while SAPs have become a feature in Africa since 1985, and RIAs have been pursued with renewed vigour especially over the last five years, there has been no serious, systematic attempt by any agency or donor to operationalise effectively ways in which integration and adjustment might be interwoven and made mutually reinforcing. The World Bank's landmark report in 1989, Sub-Saharan Africa: From Crisis to Sustainable Growth, placed considerable emphasis on regional integration as a means for overcoming the deficiencies of fragmented and small national markets which were economically unviable. Yet IMF/WBG adjustment programmes in Africa have contained little to translate those worthy thoughts into operational reality. The Cross-Border Initiative (CBI) for Eastern and Southern Africa supported jointly by WBG, the European Union (EU) and the AfDB provides an umbrella under which different experiments are being tried to induce greater regional interaction in trade and investment. But the linkage between CBI initiatives and adjustment efforts is not particularly clear.

To the author's knowledge at least, no attempt has yet been made to link SAPs with RIAs within either an intellectual framework, or an operational paradigm which is holistic, coherent and consistent. There have, of course, been frequent acknowledgements of an almost axiomatic nature that RIAs and SAPs affect one another. Obviously they must. And, indeed, a regional adjustment programme was attempted in the case of the Customs and Economic Union of Central Africa *(Union Douanière et Economique de l'Afrique Centrale* - UDEAC). But, other than that, the connections made between integration and adjustment have, by and large, demonstrated a lack of rigorous analysis.

The regional adjustment programme for UDEAC has not yet been repeated in other regions for understandable reasons despite calls to do so

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(World Bank, 1989; AfDB, 1993; Robson, 1993).[2] After all there is no example of a sub-regional arrangement in Africa which has an institutional structure that permits negotiating and enforcing adjustment policies on a regional basis. For this, and other reasons, RIAs and SAPs have invariably been pursued throughout Africa as two separate processes despite the fact that both involve drastic changes in economic policies. The artificial separation of RIAs and SAPs in this fashion may have harmed the cause and content of both, especially in Africa and SAR.

Of course, since (newer) RIAs and (improving) SAPs are both based on confluent market-friendly principles, it can be argued that SAPs will have a benign effect on RIAs. The converse possibility, i.e. that RIAs might be useful in fostering effective adjustment, however, is generally regarded with suspicion. This is on the grounds that RIAs, given the preferences implied to regional partners over non-regional ones, may actually dilute and compromise the strength of SAP medicine which, after all, is aimed at making African economies more competitive in the international (and not just regional) marketplace. Empirical evidence suggests, however, that such loose thinking based on first principles is contradicted by reality.

This paper attempts to examine the *regional* implications of structural adjustment being pursued at the *national* level across Southern Africa. The paper does not attempt primary research involving quantitative correlational or causal analysis to develop a framework of the kind that is necessary to understand fully the linkages between integration and adjustment in SAR. Instead, it focuses on developing an impressionistic understanding of how SAPs might impinge on RIAs (and vice-versa) through an analysis of existing literature coupled with reasoning based on the author's own empirical observations.

SAPs in Southern Africa

Over the last decade, most SADC countries have been subject to the intense economic and social pressures usually associated with macroeconomic stabilisation and structural adjustment programmes promulgated by the IMF and WBG. Some of these (e.g. Lesotho, Malawi, Mozambique,

2 This despite a call from the World Bank at the January/February 1990 SADCC Consultative Conference held in Lusaka where the Bank's representative called for "... the promotion of regionally coordinated and rationalised macroeconomic policies and programmes." (Haarlov, 1995). A similar call was made by the World Bank in its classic 1989 study of Africa entitled *From Crisis to Sustainable Growth,* in which the Bank observed that "Donors can facilitate such initiatives by funding regional structural adjustment programs, which would support measures and help meet compensation costs aimed at both promoting market integration and strengthening selected regional institutions."

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Tanzania, Zambia and Zimbabwe) have had one or more IMF/WBG financed SAPs implemented over that time frame with their adjustment efforts being far from successful or over. Overall they still have a long way to go. Others (Botswana, Mauritius) have undertaken SAPs either on their own initiative or with the support of IMF/WBG. Both these countries have achieved structural transformations and output growth of a kind which have placed them in a sound position to confront the future. They still face major obstacles in terms of economic and export diversification which they must surmount. But the quality of their economic management, proven over a long period of time, is such as to engender a degree of cautious optimism about their future prospects. It is often said that both of these countries have certain unique characteristics which make it hard to replicate their success in other SAR countries, but such a statement needs to be carefully scrutinised before its validity is confirmed.

Still others (Namibia, South Africa and Swaziland) have made their own attempts at adjustment and reform within the framework of formal trade (SACU) and monetary (MMA) arrangements among these countries.[3] Under these, the major macroeconomic policy parameters are established and enforced by South Africa through its hold over customs revenue collections and distributions, its administration of joint reserve holdings and the pervasive presence of South African institutions and corporations in the economies of these countries. South Africa is now attempting (without immediate IMF/WBG tutelage) its own structural reforms in order to become more internationally competitive, diversify its production and export base, generate more employment for indigenous labour, and achieve higher levels of growth (5-7% per year) than it enjoyed under *apartheid* for the last 15 years (barely 1% per year). As it does so, some stresses and strains are bound to arise which will affect its neighbours both immediate (the BLNS countries) and more distant (the non-SACU members of SADC).

Finally, oil-rich Angola, is just emerging from the throes of a long and debilitating internal conflict which has crippled its economy. Doubtless, it will shortly be subject to the adjustment discipline and ministrations of the international financial institutions (IFIs) if it is to receive the external largesse it needs to revive its agricultural, non-oil mining and manufacturing

3 These arrangements include: (1) the Southern African Customs Union (SACU) comprising South Africa and the smaller countries of Botswana, Lesotho, Namibia and Swaziland, collectively referred to in SACU literature as BLNS or BLSN; and (2) the Multilateral Monetary Area Agreement (MMA) which comprises all the SACU countries except Botswana which specifically opted out of this arrangement in order to run its own monetary affairs independently especially as its reserves are larger than those of South Africa.

sectors. Angola must now make the transition from a quasi-command economy which has eluded effective official governance for some time (and is dominated by an uncontrolled parallel market) to a market regime with normal characteristics. For a country that has not been acquainted with normalcy of any kind for a very long time, that is a daunting task even under the most favourable of conditions.

RIAs in Southern Africa

Even as they have pursued adjustment programmes at different degrees of intensity and levels of foreign agency involvement, the independent countries of Southern Africa have also been engaged in various efforts towards regional economic integration since 1980. After unimpressive beginnings, these efforts have been pursued with renewed vigour in the 1990s. Indeed, SAR has had a century-long history of plurilateral cooperation with RIAs of various kinds; ranging from preferential and free trade areas to customs unions, joint infrastructural development initiatives, and common monetary arrangements which have bound together different countries of the region in both colonial and post-independence periods (Haarlov, 1995; AfDB, 1993). Current RIAs in SAR include plurilateral arrangements involving the now-competing frameworks of SADC and the Common Market for Eastern and Southern Africa (COMESA), and the smaller but more closely integrated SACU arrangement coupled with its sister MMAA. The most recent member of SADC, Mauritius, is also a member of the smaller Indian Ocean Commission (IOC), a RIA among the independent island states off the eastern shores of Africa. These arrangements are supplemented by a pastiche of bilateral agreements (negotiated mainly by South Africa with its neighbours).

It is important to note that whereas RIAs (both old and new) generally focus on *trade* as the centrepiece, in SAR one RIA in particular – i.e. SADCC (which preceded SADC) – was designed as a functionally (sector) oriented integration mechanism built to foster *other* economic interrelationships without emphasising trade per se.[4] Paradoxically, the two RIAs in SAR which were *trade-focused*, i.e. SACU and the erstwhile PTA, are now both taking a back-seat to the emergence of SADC as the primary Southern African RIA. However, as SADC evolves it is likely that, with South Africa as the pivotal member economy, trade issues will feature more prominently in SADC than they have before. Nonetheless, it would be reasonable to expect that SADC's agenda will continue to be driven for some time yet by the sectoral investment coordination and harmonisation approach which has become its hallmark.

A second noteworthy aspect of RIAs in SAR is that they have either

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centred around the regional hegemon, South Africa, (in the case of SACU and now even SADC), or aimed at reducing dependence on it (as was the case with the former SADCC and PTA). Where lessened dependence was the aim, the opposite was achieved largely because political resolve could not overcome geoeconomic and topographical reality. SADC economies are now arguably more, not less, dependent on South Africa than they were before. As the future unfolds, SADC's success will be gauged by whether it provides a framework within which the economies of SAR become genuinely interdependent under the new *realpolitik* of the sub-region. If SADC repeats the SACU experience in entrenching South Africa's regional hegemony and cementing the role of the other Southern African economies as its dependent satellites, it will have failed and its future will be uncertain.

Third, it should be appreciated that apart from SACU, SADC and COMESA, other types of more limited regional cooperation arrangements in SAR also exist along sector-specific lines such as, for example, agricultural research (e.g. the Southern African Centre for Cooperation on Agricultural Research – SACCAR) and land use (the Southern African Centre Regional Commission for the Conservation and Utilisation of Soil – SARCCUS), unrelated as yet to the broader plurilateral RIAs (AfDB, 1993). Similarly, informal cooperation arrangements exist among transport corporations, telecommunications and power companies, as well as specific regional water basin management arrangements (which are mainly in the public sector in SAR). Many of these are covered by the SADC sectoral umbrellas although some are not.

Between 1985-93, the predecessors of SADC and COMESA complemented one another quite well even though both competed with (but were much looser than) the SACU/MMA arrangements. SADCC (Southern African Development Coordinating Conference) was set up initially to

4 One early (1983) unpublished internal SADCC document entitled *Toward Regional Trade Development* went so far as to observe that, "To assume that expanding trade is the purpose of economic coooperation is one of the two basic errors of the standard free trade area approach to economic integration. States are less concerned with trade as such than with material production, employment and economic security. The second error is to argue for an unregulated, free-market approach to regional trade when, in fact, all the participating governments practice economic interventionism (even if to varying degrees) nationally. (...) Further, regionally as well as nationally, free markets (as opposed to managed markets) are inconsistent with ensuring an acceptable division of gains and costs among members." This quote illustrates how far Africa has had to come in its thinking over the last decade and explains why, with the ethos embedded in regional thinking of old, there was a fundamental conflict between the market principles of structural adjustment and those of interventionist regionalism. In the new regionalism the philosophical chasm between the two has been bridged although not entirely.

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concentrate on project and sectoral investment coordination. On the other hand, the Preferential Trade Area of Eastern and Southern Africa (PTA) which preceded COMESA – with more members than SADCC because of its wider geographical remit – concentrated largely on trade (tariff-reduction) and monetary (clearing-house) issues. Both were aimed at integrating African countries *excluding* South Africa, with the explicit objective of reducing their dependence on the apartheid regime. Indeed, many members of SADCC and PTA were *front-line* states unified in their militant opposition to apartheid. For that reason, they became targets of the old South Africa's efforts to destabilise them, overtly and covertly, through political, military and economic confrontation and subversion.

With the end of open conflict in the region in 1993, and the birth of a new South Africa in 1994 of the kind that most countries in the region had fought and sacrificed for, complementarity between SADC and COMESA has turned to competition, despite studied attempts on the part of their respective memberships to avoid it. Competition became unavoidable when the overlapping memberships of SADCC and PTA voted simultaneously to have both organisations aim at the ambitious, and perhaps unrealistic, objective of achieving full economic union among their members within the next 25-30 years.

Thus were SADC and COMESA revamped in 1993-94, with both organisations engaging in counterproductive rivalry to attract South Africa into their respective memberships. In the event, SADC – in whose predecessor organisation, the African National Congress (ANC) of South Africa had observer status – succeeded whereas COMESA did not. That difference is significant and may have a profound effect on the future prospects of each organisation and, hopefully, on the long overdue rationalisation of multiple overlapping RIAs in SAR (see Table 1). If South Africa so chooses, SADC may evolve at a faster pace while COMESA struggles to cope with the exigencies created by its unwieldy, fractious membership. Many of COMESA's members (Zaïre, Rwanda, Burundi, Sudan, Somalia, Ethiopia and Eritrea) are in domestic disarray. They can barely manage their national polities and economies, let alone engage meaningfully in, or keep any of their commitments or treaty obligations to, formal RIAs.

There is also the prospect of the former East African Community, comprising Kenya, Tanzania and Uganda, reconstituting itself and developing its own nexus with SADC. Though perhaps difficult for its Secretariat to accept, South Africa's absence from COMESA's membership deprives that organisation of the regional credibility it needs. Moreover, COMESA must now cope with not just the competing presence of SADC but also that of SACU-MMA in an entirely new political and economic environment. And it does so at a considerable disadvantage.

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After South Africa joined SADC in 1994, SACU-MMA represents a much tighter trade and monetary union, whose members constitute a fused *inner-core* of SADC while the non-SACU members are at the periphery.

The issues raised, and confusion caused, by this plethora of overlapping RIAs in Southern Africa has been well explored in the literature (AfDB, 1993) and need not be taken up again in this paper. They must however be resolved among the member states themselves (and by the donors who support these different arrangements) to ensure that competition across these frameworks does not become fissiparous and counterproductive.

Table 1 Membership of Different RIAs in Southern Africa

MMA	SACU	SADC	COMESA	IOC
Lesotho	Botswana	Angola	Angola	Comoros
Namibia	Lesotho	Botswana	Burundi	Madagascar
Swaziland	Namibia	Lesotho	Comoros	Mauritius
South Africa	Swaziland	Malawi	Djibouti	Seychelles
	South Africa	Mauritius	Eritrea	
		Mozambique	Ethiopia	
		Namibia	Kenya	
		Swaziland	Lesotho	
		South Africa	Madagascar	
		Tanzania	Malawi	
		Zambia	Mauritius	
		Zimbabwe	Mozambique	
			Rwanda	
			Somalia	
			Sudan	
			Swaziland	
			Tanzania	
			Uganda	
			Zaire	
			Zambia	
			Zimbabwe	

Neighbourhood Effects on Growth

This introduction, already too long, would be incomplete without mention of a recent analysis (Easterly and Levine, 1995) which underlines the

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raison d'être of this paper. Based on cross-country regressions (growth over a long period tested against several variables) they suggest that, in Africa, geography may strongly influence the outcome of policies aimed at inducing growth.[5] The authors conclude that,

> 'The relationship between particular policy indicators in one country and growth in its neighbours' economies suggests that there may be growth spillovers with strategic policy implications. While requiring much additional work to establish causal relationships, ... the results are consistent with the view that improving policies alone boosts growth substantially, but if neighbouring countries act together, the growth effects are much larger. Specifically, the coefficients suggest that a policy change by a set of neighbours will have an effect on growth ... 2.2 times larger than if a single country had acted alone.
>
> Each country's neighbours' growth rate has a surprisingly large and statistically significant effect on each country's own growth: one percentage point more growth by the neighbours in a given decade translates into higher own growth of 0.55 percentage points. ... a large policy change in unison would have a multiplier effect on the countries in the region that is even larger than the strong direct effect of a country's policies on its own growth rate. ... a set of neighbours adopting a set of policy changes that would have raised growth by 1.04% if they had each acted alone, will see growth increase by 2.2% if they acted together. This also works in the other direction: with a set of neighbours all simultaneously adopting bad policies like exchange controls leading to a high black market premium, the negative effect on all of them would be magnified.'

Cross-country regressions are, of course, subject to several shortcomings which require considerable caution to be exercised in drawing firm conclusions. Such regressions do not establish causality between growth and the

5 This seemingly self-evident proposition has many instinctively obvious parallels. Just as development failure is concentrated geographically in Africa, development success has been concentrated in East Asia, the debt contagion was largely synchronic in Latin America, and the transition crisis is concentrated in the former Soviet Empire. But these observations obscure more than they reveal. Correlations alone, even when they support instinct, are not enough to go on. A deeper understanding of why a good or bad neighbourood is as important for the economic performance of countries, as it is for ethnic groups, communities, families and individuals, is clearly essential to take us further. In Africa, where there are development successes (like Botswana and Mauritius), as in Asia where there are failures, even the exceptions seem to prove the rule. For now, proper understanding of causality in determining the effect of a neighbourhood remains superficial and elusive.

variables that are tested. The definition and quantification of the variables themselves (in this case the neighbours' average growth rate weighted by their economic size in terms of GDP) imposes certain problems and difficulties. Coefficients in such regressions cannot be interpreted as elasticities.

For these reasons, Easterly and Levine are cautious about speculating on how what they call the *neighbour spillover effect* actually operates in Africa. Having tested for it, they rule out cross-border trade with neighbours as having a significant effect in Africa. Even taking into account parallel market trade, the numbers usually quoted show that Africa's *intra-regional* trade is minuscule compared to its *international* trade (in SADC and PTA it was less than 5% of total trade of members).

But this observation may conceal more than it reveals. The numbers used in the past for trade within Africa did not include trade involving South Africa. This was because under a *sanctions regime* it was embarrassing for African countries to acknowledge openly that they were trading with South Africa; in fact, most denied vehemently that any such trade was taking place. Such trade was therefore, of necessity, clandestine even when governments were indulging in it. South Africa kept reasonably accurate records of such trade but refused to disclose these until 1993 (AfDB, 1993). In 1990, South Africa's total trade with other SAR countries (including SACU members) was recorded at about $5 billion (Maasdorp, 1992b). In 1994 that amount was estimated to have increased to about $7 billion.

But there was also a considerable amount of parallel or black market trade between South Africa and the rest of Africa usually estimated at between 50-100% of the recorded amounts. Excluding intra-SACU trade, which is recorded, within the rest of SAR (i.e. between SACU and other SADC members and among other SADC members themselves) such parallel market trade was estimated in 1990 as being as large as, if not larger than, the amount of recorded, if clandestine, trade. In 1994, that proportion is estimated to have been reduced substantially with greater economic openness throughout the region. Nevertheless, outside of SACU, it is still estimated at between 40-60% of recorded trade in SAR largely because parallel market trade still successfully evades taxes in countries of origin, transit and destination.

In SAR it is difficult to imagine trade (including parallel market trade) with South Africa *not* being important to its SACU and SADC neighbours. And perhaps even the reverse may be true even though the aggregate numbers may obscure that reality. Taking its total trade into account (but excluding its gold exports) even South Africa is quite dependent on its neighbours for some of its exports but much less dependent on them for its imports (see annex Tables 4-5). If trade in manufactures is looked at closely, South Africa's access to SACU markets certainly keeps a large part of its

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relatively inefficient (by world standards though competitive by regional standards) domestic manufacturing industry going (AfDB, 1993; Haarlov, 1995; Riddell, 1990).

In that sense South Africa's visible budgetary costs of compensatory flows to the smaller SACU members amount to an invisible tied-export subsidy to its own private manufacturing enterprises (AfDB, 1993) achieved by propping up public demand in the smaller SACU economies. It is debatable (more research is needed on this) whether that subsidy offsets fully the economic opportunity costs incurred by the smaller members of SACU in providing such protection for South African manufacturers at the expense of developing their own industrial capacity or availing of other global options.

One of the intriguing speculations triggered by the Easterly and Levine analysis is whether one particular pernicious neighbourhood spillover effect might be connected with the common types of rent-seeking behaviour (e.g. corruption) on the part of governments and the private sector which are clearly observable in Africa at large. Although this was not a specifically tested correlation, instinct and anecdote lend strong evidence that the connection might be quite strong.

As the authors suggest, more research is needed on growth interactions among countries to understand better the dynamics of the development process in Africa and how RIAs might influence SAPs (and vice-versa). What the analysis makes clear is that nationally-focused SAPs in Africa might perhaps have had more successful outcomes if they had been: (i) designed to take account of repercussions in neighbouring countries; and (ii) attempted to achieve harmonised policy changes on a coordinated, regional basis rather than on an isolated, national basis.

Taking that argument a step further, the paper in its succeeding sections turns to: exploring why regional integration may be important for structural adjustment to be successful in Southern Africa (Section 2), outlining briefly the key features of SAPs (Section 3) in major areas of policy reform, and discussing the regional dimensions and implications of each in the SADC context (Section 4) before concluding (Section 5).

II Links between Regional Integration and Structural Adjustment

Why might RIAs be important for SAPs to show a much higher degree of success in Southern Africa than they have shown thus far? From an economic perspective, in SAR (as in other parts of Africa) national boundaries, which were colonially imposed, are confining artifices which make little economic sense. That alone is an important reason for looking to sub-regions rather than nation-states in Africa as more appropriate objects for adjustment.

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Why might RIAs be important to effective adjustment? *First*, because the success of SAPs depends heavily on how well markets are made to work and how the supply side of the economy responds to overdue changes in the relative big prices. In Africa, after more than a decade of adjustment, markets have not yet begun to function as efficiently as might be expected from experience in other continents. Most observers, including the IMF/WBG, generally acknowledge that, because markets in Africa are not functioning in the way they should, the supply-side response of African economies to adjustment has been disappointingly sticky.

In Southern Africa, RIAs offer the opportunity for market functioning to be enhanced significantly in markets for goods and services, as well as in factor markets (capital, labour), through: (i) enlargement and resultant economies of scale; (ii) improved factor mobility; (iii) regional sharing of technology and of highly skilled human capital; and (iv) sharing of market-supporting regulatory capacity and institutional systems and structures.[6] There is little disagreement with the view that, in SAR, *regional* markets might offer better prospects for reducing market imperfections than *national* ones; particularly so in the smaller economies of the region (i.e. Botswana, Lesotho, Malawi, Mauritius, Namibia, and Swaziland) but also in the larger, less developed ones (Angola, Mozambique, Tanzania and Zambia). That argument may be even stronger now that South Africa is legitimately accepted as an integral part of the region than when it was not. Unfortunately, the era of apartheid and sanctions compelled regional actors to oppose *politically* a phenomenon that was inescapable *economically*.

This reasoning suggests that, under the right conditions, regional market development could be a potentially vital mezzanine step in the African adjustment proces-perhaps even the *missing link* in understanding the supply side weakness of African economies especially insofar as manufacturing industry is concerned (Riddell, 1990, AfDB, 1993; Haarlov, 1995). In many of the countries of SAR, structural adjustment carried to its logical limit would be beyond the capacity of local industry to cope with. Few local firms have the internal wherewithal (in terms of management

6 The argument was best expressed at the February 1988 SADCC Conference of Businessmen on Opportunities for Investment and Trade held in Harare, where the World Bank's representative observed, "The World Bank is coming around to the view that Africa's economic future may lie in economic integration. Why? The continent is simply too subdivided with 165 borders, 51 countries, 22 of them with a population of under 5 million and 11 with a population of under 1 million. There are too many trade barriers, too much competition for the same scarce resources, human, institutional and financial; and, from a business standpoint, markets that are simply too small to sustain industry and investment. "Since then, of course, the numbers of countries and borders have only increased. (Extracted from The Conference Proceedings published by the SADCC Secretariat; Haarlov, 1995).

capacity, information, technology, capital, quality, labour skills or extended market access) to adapt and adjust to the price/cost and import availability realignments that high-pressure adjustment, in a compressed time-frame, usually results in.

When traditional trade regimes are suddenly reversed with a lowering of protection they can, if firms are insufficiently robust and resilient, result in closure of most units designed to produce for fragmented national markets (i.e. de-industrialisation) with immediate consequences for large-scale lay-offs, unemployment and a dissipation of the internal tax revenue base. At the same time newer, more competitive industries whose emergence adjustment is supposed to encourage are not appearing at the rate needed to absorb the high social and political costs of adjustment-induced dislocations. Under the consequent threat of de-industrialisation, the vested interests of industrialists and investors (including foreign investors who invested with explicit assurances of protection), providers of supporting infrastructure and services, labour, politicians and the state bureaucracy, usually coalesce into slowing down or thwarting the adjustments that need to occur.

In Latin America and Asia, *national* firms in most industries have adjusted quickly to required changes in trade and exchange regimes. Some have gone out of business, but with manageable repercussions. In Africa, apart from a few exceptional cases, they have not adjusted and governments (which own most of them) are reluctant to let them go out of business. When most national markets in a region (as is the case in SAR and other African sub-regions) cannot support such units, and they are incapable of adjusting sufficiently rapidly to compete effectively in world markets, the adoption of a *regional* market approach to liberalisation through appropriate RIAs, can provide a useful temporary alternative. Regional markets can provide the needed environment in the medium-term over which local industries can be restructured, rationalised and merged with fewer overall costs and better long-run prospects of achieving international competitiveness. A regional approach can buy time for local firms to improve efficiency and quality, raise productivity, increase capacity utilisation, upgrade technology and improve international export performance through experience gained in regional markets.

In providing an opportunity for learning effects to occur without destroying viability, the regional market option can be constructively deployed in a manner congruent with adjustment and liberalisation through the adoption of common external tariffs (CETs) which are lower than prevailing national tariff regimes but higher than tariffs applicable to non-regional sources of products. But the *buying time for learning* approach can only work well, if it places time-bound limits on regional firms to

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achieve international competitiveness. Otherwise, like most import-substituting industrialisation experience, the regional approach risks becoming an entrenched soft-option for firms to operate for too long behind protective walls even if these are lower than they were under former national regimes (Mistry, 1995).

Second, in the capital-short economies of SAR, whose geography and topography makes them particularly inter-dependent on regional river systems and regional ecology (Mauritius being the isolated, independent exception), fiscal pressures as well as crowding-out pressures on private investment can be substantially ameliorated by employing regional approaches to infrastructure investment and service provision. The projected capital requirements for infrastructure investment in SAR are well beyond the capacity of governments to provide through the fiscus and yet retain a viable macroeconomic stance. Apart from substantial savings in capital costs, a regional approach to infrastructural investment in SAR is likely to produce savings through more cost-efficiently delivered services on an on-going basis, especially where electricity, water supply, telecommunications, transport (surface and air) and tourism services are concerned (Maasdorp, 1989; Blumenfeld, 1991; Kimaro, 1992; AfDB, 1993).

In all of these areas, large cost and price subsidies (to producers and/or consumers) distort the true costs of infrastructure and utility service provision throughout the region. Electricity and water in particular are grossly underpriced with subsidies on these goods (especially in South Africa) being directed more to relatively rich commercial farmers and large industries rather than to the poorer segments of the population. Indeed, because the tariffs charged to better-off consumers do not allow for sufficient cost recovery these services are rarely accessible to the poorest segments of the population in either urban or rural areas. Apart from being misdirected, ,such subsidies – which were rooted in a climate of apartheid, self-reliance and sanctions – impose large unaffordable burdens on the fiscus in every SAR country.

The progressive withdrawal of such subsidies (a key feature of SAPs) at a socially and politically acceptable rate, is likely to be more tractable if regional rather than national approaches are taken to infrastructure investment and service provision. Resultant cost savings in investment capital, and from cheaper sources of production, could be passed on to regional consumers without tariffs having to be raised to unaffordable levels. The supply response on which the success of SAPs so heavily depends is unlikely to be forthcoming unless adequate infrastructural support and services are provided to productive entities at affordable costs. Because the private sector, and the Southern African production structure, are heavily depen-

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dent on the provision of such services at prices which enable them to remain competitive and viable, a regional approach may provide the most cost-effective option for future infrastructural investment.

Third, the success of SAPs also depends on how quickly distortions and false price-signalling in major *factor* markets (especially for capital and labour) can be removed and these markets be made to work more efficiently. In SAR that is more likely to happen if factor price distortions are tackled on a regional rather than national basis. In some instances, e.g. in South Africa, it may actually prove easier to achieve *labour* market and wage adjustments through a regional rather than national approach in which localised social and political pressures would derail or delay the needed reforms (AfDB, 1993; Lachman and Bercuson, 1992).[7] The free movement of labour is of course a complex and contentious issue in RIAs, especially when the disparities in levels of development and income among the members of a regional arrangement are as wide as they are in SAR (Haarlov, 1995). Nonetheless, freeing intra-regional labour and capital markets to allow for unimpeded flows of capital and labour across the region can help to ameliorate national pressures and provide a more tractable approach for the South African government to adopt. Freeing intra-regional *capital* flows alone would have a moderating effect on domestic wage pressures by providing capital-rich SAR firms with the option of shifting production to areas where factor costs would induce greater cost-efficiency and favour greater competitiveness. Moreover, freeing capital flows within the regional market may have the beneficial effect of diverting outward capital flows (whether induced by flight or diversification motives) from extra-regional directions to intra-regional targets.

Fourth, the combined effect of (i) removing subsidies on electricity and water and (ii) opening up regional markets in *land*, along with free flows of labour and capital, could bring about a geographical and structural shift of agricultural and manufacturing production in SAR. Such a shift would favour more cost-efficient, agro-climatically favourable areas for grain production on a commercial scale and encourage the dispersion (through

7 To illustrate, it is widely recognised that a major barrier which South African firms (and, by spillover, firms in neighbouring SACU economies) face in becoming more cost-efficient and competitive in the industrial sector, is the relatively high productivity-adjusted wage rate for labour employed formally. Any attempt to reduce that wage rate in real terms is likely to meet with powerful opposition from entrenched unions to whom a political debt is owed by the present ANC-led government. At the same time there is powerful pressure within South Africa to reverse its long-standing policies on migrant labour in the mining sector and to clamp down on illegal inward migration of labour, especially from the poorest countries in the region. Here the unions are caught in a bind since the mineworkers union has a large number of migrant members.

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market forces) of manufacturing investment to areas where cheaper labour and large cachement areas exist providing that the public sector focused on filling the gaps in infrastructure and supporting services which presently impede such dispersion (AfDB, 1993). A regional approach thus offers the potential – in theory at least – of achieving more in terms of *investment productivity* (i.e. improved incremental capital-output ratios), output growth, and efficiency effects for each country in SAR than nationally oriented SAPs could hope to achieve. In the latter case, while SAPs may remove policy distortions within confined geographical areas they can do little to remove the other significant impediments to increasing factor productivity, efficiency and output which exist in the individual countries of SAR.

Fifth, apart from South Africa, and to a lesser extent, Zimbabwe and Mauritius, no other country in SAR has the indigenous capacity to diversify its production and export base to the extent or as rapidly as is required for SAPs to show successful results by way of supply-side responses in the medium-term. SAR, and even South Africa, are far too dependent on unprocessed mineral and agricultural exports which, it has long been recognised, must account for a progressively diminishing proportion of their GDP and trade in the future. For that to happen, and for a reversal of the rapid increase in aid-dependency which SAPs have unfortunately caused in their wake, countries in SAR need to attract *foreign direct and portfolio investment* in much larger quantities, from more diverse sources (especially from Asia), than they have hitherto been able to do.

Regional markets in SAR present more viable investment opportunities for foreign direct investors than do fragmented national markets (especially ones with a recent history as debilitating and painful as that of many SAR countries). Such investment is likely to have a quicker, larger impact on diversifying SAR's manufacturing output and exports than if reliance were placed on indigenous investors alone (Riddell, 1993; Meier and Steel, 1989). To put it bluntly, foreign direct investment (FDI) in countries like Zambia, Angola, Malawi, Tanzania and Mozambique, and in the smaller SACU members, is likely to be materially larger, and probably of better quality, if coursed through Mauritius and South Africa (and to a lesser extent Botswana and Zimbabwe) as the region's investment centres and the region's prime locations for the regional headquarters of foreign companies.

Sixth, there may be a number of *political* reasons why RIAs might affects SAPs benignly in Africa and SAR. Citing Mansoor and Inotai (1991), Haarlov (1995) observes, with some scepticism about the market-focused adjustment process and about political intent vs. economic reality in Africa, that,

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'A regional approach may offer a new dimension to supplement the unilateral and uncoordinated national efforts of the sort currently being engaged in with World Bank and IMF support. Regional liberalisation may be more politically acceptable than unilateral concessions (because)

- governments can draw upon the positive connotations and sentiments of pan-Africanism and the OAU and ECA sponsored schemes of working towards a united Africa ... expressed in the Lagos Declaration (1980) and the Abuja Treaty (1991) aiming at African unification by 2025;
- in contrast to unilateral liberalisation, it implies trade-offs with neighbouring countries with a clear element of mutual concessions involved;
- internal vested interests (in individual African countries) which survive and profit (from rent-seeking behaviour in a controlled economy) would confront more difficulty in unwinding agreements with *regional* partners than they would in opposing unilateral reforms at the national level; by compelling competition among regional firms that are at comparable levels of inefficiency a regional adjustment process would reduce the costs of adjustment by encouraging mergers, acquisitions and takeovers to achieve competitiveness at an industry-level rather than forcing outright immediate closures of firms of the type that occurs when adjustment is focused at the national level'. (Haarlov, 1995; p. 42-43, paraphrased for brevity)

Seventh, a key aspect of SAPs in Africa goes well beyond the reform of trade and exchange policies and domestic demand management (the traditional realm of classical IMF stabilisation programmes). It involves structural change in production paradigms with an explicitly reduced role for the state in directly productive and infrastructural provision activities and a correspondingly enlarged role for the private sector. A key instrument under IMF/WBGs for achieving the desired restructuring is *privatisation.* Attempted at the national level, ambitious programmes of privatisation (e.g. in Zambia and Tanzania) are running into major problems caused by the absence of (i) properly functioning capital markets with any depth or width, (ii) an equity-ownership culture on the part of the general public (which has become so embedded in Asia), (iii) an effective capital market regulatory framework, (iv) a sufficiently large pool of private domestic financial savings to absorb the transfer of ownership within the national economy, (v) indigenous management capacity to restructure and run privatised enterprises profitably after their privatisation, (vi) interest on the part of acceptable foreign investors in these individual economies on a fragmented basis, and so on.

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There is also much social and political opposition to ownership of privatised enterprises being concentrated in the hands of a few wealthy indigenous business groups not known for their probity, or in the hands of indigenous, non-African resident communities, or of a few foreign multinationals well-established in Africa. All of these constraints which are hard and binding at the national level can be considerably eased if a regional approach were taken to the privatisation of state-owned enterprises (SOEs); relying on *regional pools* of technology, management, and savings and on *regional capital markets* in South Africa, Zimbabwe, Mauritius and Botswana for public flotations of privatised enterprises throughout SAR. These markets are relatively sophisticated and could serve as entry-points for willing foreign portfolio (institutional) investors in such enterprises from within the region and from outside.

The absence of speedy and successful privatisation in SAR may help to explain, in large part, the absence of the anticipated post-reform supply-side response which SAPs are supposed to bring about. It is clear, especially with South Africa as a member of SADC, that a regional approach to privatisation could have a much higher pay-off in accelerating the pace and improving the quality of SOE restructuring and privatisation programmes. Moreover, a regional approach to privatisation has the added attraction of providing privatisation-induced development and deepening of SADC capital markets by widening the number of listed securities on market exchanges and adding to trading depth.

The threat that opening up privatisation to regional investors would essentially result in a South African and Zimbabwean takeover of the regional economy can be countered with the construction of specific trust-fund arrangements (funded by debt-equity swaps) involving a syndicate of public international investors (like the IFC, CDC, OPIC, IFU, FMO, DEG and Swedfund) which hold privatisation shares in trust for local nationals gradually releasing them in local capital markets as such markets expand their absorptive capacity (Mistry and Griffith-Jones, 1992).

Eighth, the success of SAPs also depends on how rapidly countries undergoing adjustment can develop their own sources of free foreign exchange to ease balance of payments pressures without resorting to enhanced levels of already extraordinary concessional aid flows. As very few countries in SAR are creditworthy for borrowings on commercial terms, the only other options they have are to (i) diversify sources of export earnings from primary commodities, something which is not happening fast enough in the region; (ii) do more to attract foreign investment, both portfolio and direct, although most SAR countries remain unattractive to non-regional foreign investors except in mining and plantation agriculture for reasons already mentioned; and (iii) enter into

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regional payments and settlements arrangements which result in increased trade and output. The first two options have been explored earlier. Although the last of these options is being used in SAR (through the MMA and, in the non-SACU countries, the PTA clearing house) it has not yet been developed, outside of the SACU-MMA arrangements, to a degree which exploits fully the potential that the region has to offer its individual members in facilitating their adjustment.

Ninth, no attempt at structural adjustment in SAR can be successful without its member nations achieving basic *food security*. As events over the last three decades have proven, no nation in SAR other than South Africa can achieve food security easily over the near or medium-term, in a purely national context. The food security objective, however, becomes eminently achievable in a regional SAR-wide context providing the right macroeconomic, agricultural pricing, and infrastructure input pricing policies are pursued in harmony by all countries in the region. As the AfDB study points out (AfDB, 1993), such policies would also result in a major locational shift of agricultural production which would enhance regional and national welfare substantially. But the food-security argument on a regional basis applies even more forcefully to *energy security*, and much more critically, to *water security* which threatens, over the next 15 years, to become perhaps the most contentious and potentially explosive issue dividing neighbouring countries in the sub-region (AfDB, 1993).

These nine reasons for believing that appropriately structured RIAs can materially influence, if not positively enhance, the outcome of SAPs in SAR could be expanded much further. But there is little purpose in belabouring the point herein with a complete and exhaustive list, once the general thrust of the argument is clearly established in intellectually satisfactory terms. Assuming that to have been done in the foregoing pages, the next section (Section 3) moves on to outlining the features of structural adjustment programmes (especially in SAR) while Section 4 assesses their regional implications and dimensions in each case.

III Key Features of Structural Adjustment Programmes

The design, content and sequencing of structural (and supporting sectoral) adjustment programmes have been examined in a vast literature generated by the IMF, WBG and economic academia at large, which will not be revisited here. Suffice it to say that SAPs are partly *crisis-management* programmes which are aimed at restoring the liquidity and solvency of economies which have become unviable and partly *foundation restructuring* programmes creating conditions under which normal economic life can be resumed and development momentum can be maintained thereafter. For that reason SAPs are necessarily disruptive; but their dislocations need to be kept within social and political limits of tolerance for their effects to take hold.

In the absence of an economic crisis there is usually little need for a SAP though there may still be need for gradual and continual non-disruptive adjustment. Although no one would argue in favour of bad policies, wrong prices and non-functioning markets, the debate about virtually every aspect of SAPs continues to rage unabated. It is particularly intense about the effects and results of adjustment in Africa (Martin and Mistry, 1991, 1996; Patel, 1992; World Bank, 1992, 1994ab, 1995a; van der Geest, 1994; van der Hoeven and van der Kraaij, 1994; Mosley et al., 1995; Killick, 1995a). But in this debate there is little argument about what SAPs incorporate as core features and what they leave out.

Before going into these, it needs to be observed that there is no *theory of structural adjustment* as such. The IMF and WBG often issue edicts, postulate relationships, and make *ex cathedra* assertions, about specific reforms, instruments, targets and policies, which sometimes appear to suggest that there might be. The only theories underlying SAPs are those of markets, trade, money, price, public finance, and – regrettably, to a much lesser extent – rational expectations, public choice and new development theory stressing the importance of human capital. All of these theories, taken together, involve the practice of sound macroeconomics at the level of the economy and sound microeconomics at the level of the sector and firm. The design of SAPs is usually based therefore more on convention, empiricism, experience and – all too often – on crude heuristics combined in an IMF/WBG ten-point code of conduct which has come to be recognised as *the Washington consensus* (Williamson, 1990). It is relatively strong on the macroeconomics of adjustment but relatively weak on its *mesoeconomic* (sector level) and *microeconomic* concomitants.

Essentially, SAPs are designed to achieve two things: (i) get countries over the immediate crisis they face with the unsustainability of internal and external accounts through demand and debt management measures which usually involve major price and budgetary realignments, i.e. *macroeconomic stabilisation;* and (ii) create conditions for maintaining macroeconomic stability over the long term by *transforming* productive and institutional *structures* of the economies concerned by removing non-market distortions, improving price signalling and making economic agent behaviour responsive to price changes. In a theoretical sense the process of adjustment is never complete; healthy, stable economies adjust continuously to changing internal and external market conditions. But, SAPs imposed and monitored by external interlocutors, in particular the IMF and WBG, are supposed to

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have a definite time-bound limit by which time the crisis is supposedly relegated to history with macroeconomic stability being re-established, and sufficient headway having been made with transformation to leave further adjustment to governments and markets within the economy itself (Corbo and Fischer, 1992).

Stabilisation measures under SAPs are usually those which try to restore macroeconomic equilibrium by reducing the level and composition of demand to match the availability of financing (external and internal) and of output. The three principal means of doing so quickly are fiscal compression (for internal balance), devaluation of the exchange rate (for external balance), and tight monetary control connecting the two. *Structural reform* measures are usually aimed at creating markets (where there are none) and/or making them work as well as possible by removing distortions and creating the right types of incentives. These invariably involve liberalising trade and exchange regimes, reforming the financial system, deregulating markets for goods and services, removing artificial constraints operating on factor markets (land and capital), removing bureaucratic and tax obstacles to savings and investment, rationalising and reforming the public sector, reducing the role of state-owned enterprises, concomitantly encouraging privatisation and private-sector development, and reforming market-supporting systems and institutions.

Although it is generally the case that stabilisation measures precede structural transformation attempts, sometimes certain structural reforms are needed before stabilisation can be achieved. For example, in Africa and many Eastern European countries in transition, public enterprise reform and privatisation may be needed in the early phases of a SAP for the fiscal deficit to be brought under control and a supply-side response to be felt. Or, financial systems may need to be reformed in certain aspects of their functioning for monetary control to be properly enforced before stabilisation can be achieved. Conversely, because adjustments in the financial sector take hold more rapidly than in the real sectors, there may be a case for achieving certain real sector adjustments before full-scale financial liberalisation is attempted (World Bank, 1994ab).

This issue of course brings to light the third key feature concerning SAPs, i.e. the importance of *sequencing*. The wrong sequencing of adjustment measures and reforms (as may have been the case with many SAPs in Africa and SAR) can result in prolonged macroeconomic instability which then feeds back into vitiating the impact of structural reforms aimed at improving the quality of resource allocation and efficiency of resource use through changes in relative prices. Unfortunately, it is not always as clear in prospect (i.e. before the fact) as it seems in retrospect that the sequencing of adjustment measures, or of the relative pace of adjustment between financial and real sector liberalisation, may be (or have been) wrong. When it is clear that sequencing may have been flawed the realisation usually dawns after damage has been done; the costs are then invariably borne by the adjusting economy and never by the prescribing agency.

Faulty sequencing (along with faulty policies or poor SAP design) can result in a vicious cycle of spiralling inflation, continued devaluation, and rapid debt-accretion, coupled with a loss of control over public finances, which eventually results in an implosion of domestic output when levels of external finance needed to support the cycle are no longer affordable. There is no ready-made recipe for sequencing (or even for the precise content of policy changes) which can be applied mechanistically to all countries. Country characteristics and initial starting conditions are critical factors in determining what needs to be done, how and when.

It is often the case that what are frequently seen as implementation failures, when SAPs do not bear the expected fruit, are, in retrospect, failures of design and sequencing (World Bank, 1994a, 1995a). Since SAPs usually enlarge the multilateral debt burdens of adjusting countries very rapidly, they should be prescribed with caution unless there are reasonable prospects that they will succeed. Sadly, in Africa, most SAPs have not yet yielded the results that were expected when they were launched (World Bank, 1994a; Mosley et al., 1995) resulting in too many African countries now having built up levels of debt, especially of multilateral debt, which they can no longer afford to service without incurring massive opportunity costs (Mistry, 1995e; Martin, 1993; Killick, 1995b).

As this section is not intended to be either a compendium or critique of SAPs per se, but a reminder of what the main ingredients of SAPs are, in terms of policies and reform measures, further general discussion of the *intent-vs-effects* of SAPs will be eschewed at this point although it will be taken up again in discussion of SAP aims and outcomes in each of ten key areas of policy reform (Section 4). Instead attention is focused on highlighting the ingredients of adjustment programmes in abbreviated form. Most SAPs, usually supported by one or more sectoral adjustment programmes (SECAPs) usually require countries to undertake broad policy reforms aimed at: (a) reducing *absorption;* (b) improving *switching* from imports to domestic production; (c) reviving growth through a *supply-side* response achieved by improving the structure of incentives. The specific policy reforms prescribed for achieving these three broad objectives are as shown below.

Table 2 Specific Policy Reforms for Adjustment

Absorption Reduction	Switching Policies	Supply-Side Policies
Fiscal Policy		Trade Regime Reform
	Exchange Rate Reform	Real Sector Reform
Monetary Policy		Financial Sector Reform
	Labour and Wage Policy	Public Sector Reform and Privatisation
		Social and Other Policies

The specific sub-policies and adjustment measures which are agreed as conditions under SAPs or SECAPs in each of these broad policy areas are enumerated in Annex 1. Under each policy area, broad policies and objectives are listed in the left column and the specific policies/measures designed to achieve them on the right. The problem with such schematics is that, while helpful as aide-memoirs, they risk leaving the impression that things are simpler and more cut-and-dried than they are in reality. It needs to be stressed therefore that although sets of policies and actions are shown as discrete sections, they are intricately interrelated. These interrelationships are not easy to explain. Many of them are imperfectly understood even by experts. Different macroeconomic policies have much to do with one another. Improperly synchronised, failure in any one policy area (fiscal, monetary or exchange rate) will usually have immediate and large repercussions in other areas causing the failure of the adjustment effort as a whole.

Similarly, sector-specific adjustment policies are not likely to be effective if the overall macroeconomic regime is not functioning well. In the absence of proper signals being emitted by fiscal, monetary, exchange rate and other key *big price* policies, the effects of sector-specific adjustment measures are likely to be vitiated or obscured in the industrial and agricultural sectors (World Bank, 1994a; 1995a). It is equally true that unless the key productive sectors of the economy respond well to relative changes in prices and other macroeconomic, sector-specific and micro-level policy reforms – by way of increased output, greater productivity and higher efficiency – then macroeconomic adjustment is unlikely to occur effectively within any reasonable time span.

These critical interconnections point to the importance of overall adjustment programme design and the distinctions that need to be drawn between the whole and its constituent sectoral parts. African adjustment

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experience certainly suggests that much more learning needs to be acquired about adjustment in Africa's somewhat unique conditions which are dissimilar to those in Asia, Southern Europe and Latin America where much adjustment experience has been gained. Architectural knowledge in this area is distinctly weak and countries can be caught in a trap when the architects themselves are learning by doing and making it up as they go along.

Annex 1 shows lists of indicative and reasonably comprehensive (though not exhaustive) impressions of the content and complexity of SAPs. An in-depth assessment of the *regional vs. national* approach to adjustment would need to undertake quantitative econometric analysis on the relative effects of each of a large number of different variables reflecting specific adjustment measures whose independent effects on outcomes could not easily be isolated from the effects of other variables operating at the same time. That task is not attempted by this paper.

Instead the next section turns to an impressionistic analysis of national adjustment experience in Southern Africa on the first ten of the eleven broad areas of policy identified in the boxes above, discussing (i) the observed impact in each of these areas at the national level based on adjustment experience in SAR countries, (ii) indulging in educated speculation about what a regional perspective in each of these ten areas might have had to offer as an alternative to nationally focused adjustment, and (iii) hypothesising about whether desired outcomes might have been more efficaciously achieved had a regional approach been taken.

Such an analysis of course has one major weakness. It has to be recognised immediately that, in SAR and SADC, the political conditions did not exist until 1994 for a genuinely regional approach to adjustment. The former SADCC and PTA structures did not provide the right frameworks under which regional adjustment programmes could have begun to be conceptualised, leave alone designed, negotiated and implemented. The interesting questions now are (i) whether the emerging SADC structure offers that opportunity, and if it does, (ii) whether that route is worth taking?

Without South Africa as the region's centrepiece, it is debatable whether a regional approach to adjustment confined to the other SAR countries would have achieved very much. In the present SADC structure, the macroeconomic and sectoral interlinkages among countries are perhaps best represented by a spoked-wheel with South Africa (and to a lesser degree Zimbabwe) at the hub while the other countries at the other end of separate connecting spokes; the rim connecting the smaller economies is weak and, in some cases, broken. The SADC arrangement does not have the features of the European Union (EU) in which countries are linked through a web of well-established intra-industry and inter-industry trading and cross-ownership arrangements among companies.

However, the analysis, bringing South Africa into the picture as the 1993 AfDB study has done, may nonetheless be a useful exercise in sharpening thinking about the future. It opens the possibility of a different approach being taken to structural adjustment in the African environment – and, concomitantly, to closer economic integration. For this to happen, all parties (i.e. SADC countries, AfDB, IFIs and the major donors) should be prepared to seriously consider and negotiate regionally designed adjustment programmes.

IV Analysis of National vs. Regional Approaches to Adjustment in Southern Africa

Of the twelve countries of SADC, seven have undertaken SAPs financed by the IFIs, with Zambia having had the longest, most difficult and as yet inconclusive experience. Zambia has been adjusting, on-and-off, with various IMF and WBG programmes since 1979, but with the most intense pressure being felt between 1987-93. Malawi has had successive SAPs since 1984, Mozambique and Tanzania since 1986, while Lesotho has been adjusting since 1988 primarily with IMF assistance (SAF/ESAF), and Zimbabwe with WBG assistance since 1990.

Of the SADC countries, only Mauritius has adjusted successfully between 1981-85 having exited from IFI-supervised adjustment by the late-1980s. Its government recognises, however, that it still faces major challenges of economic diversification and finding new sources of future growth. It is perhaps the one member of SADC whose ongoing adjustment process depends less on regional influences than on what happens in its principal international markets. Nonetheless, it is possible that Mauritius' growth and economic relations over the next decade may be influenced more by regional developments than has been the case previously.

Angola has undertaken its own partial stabilisation measures since 1991 including several devaluations and unsuccessful attempts to cut the fiscal deficit, restrain money supply and control inflation. Its political circumstances, however, need to stabilise further for any progress to be made on the economic front. As observed earlier, it is likely that Angola will need to undertake IFI financed SAPs in the second half of the 1990s in order to secure the external financing that it needs for a massive rehabilitation and reconstruction effort.

Other than Lesotho none of the SACU members have undertaken IFI-designed SAPs although in one way or another most have faced upto the need for adjustment. Botswana has applied rigorous financial discipline and

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prudent (if cautious and risk-averse) economic management approach to self-correct swiftly when growth has fallen and exogenous influences have threatened to become malign. Botswana, Swaziland, and to a much lesser extent, Namibia benefited from the sanctions regime during the 1980s and early 1990s as conduits for South African transactions with the rest of the region although that benefit may now be reversed.

Severely constrained by externally imposed sanctions, South Africa has pursued relatively cautious economic policies but with *stagflation* for nearly 15 years. It has now entered a period when it must undertake long-delayed adjustments to accelerate growth. That process, whether guided by the IFIs (a prospect South Africa is valiantly and sensibly attempting to avoid) or not, must occur inevitably. The question is whether it occurs in a controlled manner with the government in full command of the process or whether it occurs disruptively with the consequences that South Africa's neighbours in SADC have suffered. Adjustment in the new South Africa cannot be delayed if the political expectations created during the process of democratic pluralisation are to be met over the foreseeable future (Lachman and Bercuson, 1992; Howe and le Roux, 1992).

That of course raises an issue which cannot be ignored, either by the South African government or the international community, i.e. that South Africa's adjustment process will have major repercussions for its neighbours in SACU and, beyond that core, to the periphery embracing other SADC members as well. Whereas adjustment in the other (non-SACU) SADC economies caused barely discernible ripples in South Africa, the opposite is not likely to be the case. Major adjustments in the region's largest economy over a short time-frame could generate tsunamis for its neighbours.

That is not surprising when South Africa accounts for 76% of the region's GDP (see Annex Tables 1-3) and when its total trade with these economies (including unrecorded trade) is not large from its own perspective but is large when seen from the other end (see Annex Tables 4-7).

When South Africa adjusts, the rest of the region will inevitably need to "adjust to its adjustments". Reactionary *nationalistic* policy responses of the wrong kind by its neighbours, if triggered suddenly and arbitrarily, could risk vitiating what has been achieved by adjustment thus far in the other SADC countries. They may even feed back to destabilise, or at least impede, South Africa's own adjustment process. Consequently, a powerful intellectual case could be made that the need for a regional perspective on the adjustment process in SAR has perhaps never been stronger nor more urgent than it is now.

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1. *Fiscal Policy*

Bringing large budget deficits under control and reducing them to sustainably financeable levels has been a major concern under all IFI-financed SAPs; nowhere more so than in Africa and SAR. Reducing the overall fiscal deficit and, in particular, the primary deficit (before grants are taken into account) has been a key objective in order to restore internal balance and debt sustainability. The focus of fiscal stabilisation in SAR countries has generally been to achieve an immediate reduction in domestic *expenditure* (especially government and public sector expenditure) and diminishing resort to monetisation (i.e. an inflation tax) for financing the deficit. Fiscal *adjustment* on the *revenue* side has focused more on revising the structure of taxes to: remove biases and distortions; increase tax neutrality, yield and buoyancy; widen the tax base while lowering very high marginal tax rates reduce overdependence on trade taxation; and increase taxation of domestic transactions with broadly based indirect taxes such as value-added taxes.

Other (and belatedly introduced) objectives in the context of overall fiscal compression have been to achieve expenditure *switching* so as to reduce: unproductive expenditures (e.g. defence, excessive foreign representation, etc.); widely entrenched producer and consumer subsidies which are enjoyed mainly by middle and upper income groups (e.g. on food, electricity, water, secondary and tertiary education, other utilities, transport services etc.); and to protect social expenditures aimed at human capital development (health and education), social security and targeted subsidies for the poorest groups. Attempts have also been made to protect priority development investment expenditures while reducing the burden of recurrent costs imposed by excessively large civil services and chronic overemployment in state enterprises. Administratively, SAPs have placed a considerable amount of emphasis on improved tax compliance and on increasing collections largely because actual revenue yield in the non-SACU members of SADC was estimated to be less than 30% of what it should have been with proper compliance and enforcement.

What has experience in SAR been with improvements in fiscal performance through nationally focused SAPs? Mixed, as Annex Table 8 illustrates. Lesotho has perhaps achieved the most striking turnaround from an overall deficit of over 20% of GDP in 1988 – largely as a result of parastatal losses and imprudent military expenditures – to a surplus of 3.6% in 1994. This turnaround was attributed to parastatal reform, cut-backs in non-essential expenditures, civil-service rationalisation, and increases in revenues supported by enhanced output growth in manufacturing (stimulated by South African and East Asian inward foreign investment). From an average fiscal deficit of 6% of GDP in the mid-1980s, Mauritius has maintained a steady and sustainably financeable overall deficit of 2-3% of GDP through the 1990s represented mainly by its capital expenditures on development. Zambia's fiscal deficit was reduced from an average of 15% of GDP between 1981-86 to an average of 5% between 1990-94, dropping to around 1% in 1994. This impressive performance was attributed to (i) Zambia's moving to a cash budgeting system in 1993, and (ii) the creation of a single Zambia Revenue Authority with foreign assistance which resulted in tax collections increasing by 2% of GDP in that year alone. Whether that improvement proves to be yet another Zambian flash in the pan or whether it presages the arrival, after nearly three decades, of a stable macroeconomic regime remains to be seen.

Apart from these three countries, the record has been poor. Tanzania's deficit was reduced from 11% of GDP between 1981-86 to a low of 3% in 1992 but has risen again to an average of 13% in 1993-94. Similarly, in Malawi the deficit fell from an average level of 11-12% of GDP in 1981-86 to below 7% in 1991 but rose again to nearly 15% in 1994. In Zimbabwe, the deficit has remained stubbornly at an average of around 9-10% of GDP (fluctuating in a range of 6-12%) through the 1990s, and is roughly at the same level as in the 1980s; while Mozambique's fiscal deficit has actually increased from an average of 16% between 1981-86 to around 28% of GDP between 1990-94.

Lesotho apart, in SACU, Namibia has run large fiscal deficits averaging about 19% of GDP in the late 1980s. These were reduced to around 12% in 1992 although the decline was reversed in 1993-94 due to drought. Botswana has generally run a budget surplus. South Africa kept its overall fiscal deficits to between 3-5% of GDP between 1980-90. The deficit increased to a peak of 9.8% of GDP in 1993 before being reduced to 6.4% in 1994-95 and a targeted 5.8% in 1995-96. Swaziland averaged a deficit of around 4% of GDP through the 1980s, generated budget surpluses in 1990-91, after which the deficit has again grown from 1.6% of GDP in 1992 to 7.8% in 1994.

At first glance it would appear that fiscal policy is an area of adjustment where a *regional approach* in SAR might not have significant pay-offs in enhancing adjustment effectiveness. But first glances would be superficial and misleading. To begin with, the most telling example of fiscal adjustment in SAR, i.e. Lesotho, has as much to do with its internal reforms as with what happens in South Africa. Lesotho is encircled by South Africa which accounts for 82% of its total trade, employs 40% of its male labour force – whose remittances are about the same size in money terms as the total value of Lesotho's GDP and therefore constitute 50% of its GNP. Lesotho will generate substantial future revenues from the Highlands

Water Project, the output of which will be purchased entirely by South Africa. Its customs revenues, which constitute 50% of its total revenues, are collected by South Africa under SACU and repaid through unencumbered budgetary transfers with compensatory and revenue stabilisation elements added.

Under the MMA, Lesotho's use of monetary and exchange rate tools to effect adjustment when its economy hit a crisis in 1988 were circumscribed. For Lesotho, it was perhaps just as well that was the case. Had these options been available, the unsustainable fiscal deficit in the mid-1980s would almost certainly have been monetised leading to escalating inflation, a collapse in the exchange rate, and resulting in a much larger burden of eventual adjustment which would have taken much longer to achieve, and been more painful in terms of social and political costs. In fact that is precisely what happened in Malawi, Tanzania, Zambia and Mozambique. It is interesting to speculate on whether their internal and external imbalances, and consequent burdens of adjustment, would have got so far out of hand had their monetary and exchange arrangements been anchored in the same way that Lesotho's were, however inconvenient that may have seemed.

Although Lesotho perhaps represents an extreme case of suffocating fiscal dependence on its elephantine neighbour, the same type of arguments can be made for Swaziland and Namibia, albeit to a lesser extent, and to an even lower extent for Botswana. However, a closer look would suggest a relatively high degree of indirect fiscal dependence on South Africa even on the part of more distant Malawi, Zambia and Mozambique (with Southern Mozambique rapidly becoming an economic extension of the Eastern Transvaal) and of Zimbabwe. Perhaps the only countries in SAR which are presently least fiscally affected by South Africa are Angola, Mauritius and Tanzania.

In Malawi and Zambia, a large part of unrecorded trade and therefore untaxed transactions are directly with South African enterprises and privateers many of whom use Zambia's open capital account as a convenient route for arranging capital flight. A typical arrangement would involve container loads of second-hand clothing, other scarce consumer goods and contraband purchased in rand in South Africa, being driven into Malawi or Zambia (which is least efficiently administered) to be sold on the open market for local kwacha, with these being converted through bureaux into dollars which are then kept in dollar accounts in Zambia or remitted abroad.

Illicit South African dollar holdings in Zambia were estimated to have become substantial by 1993-94. They were suspected of playing a major role in destabilising both the foreign exchange markets a well as the 30-day

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Government Treasury Bill (T-Bill) market in Zambia thus increasing Zambia's deficit in 1993. This was possible through arbitrage transactions aimed at seizing opportunities offered by transient and extraordinarily high real interest rates during a monetary squeeze, or by the profits offered when mismanagement of the exchange rate resulted in unexpected appreciation of the kwacha unwarranted by the fundamentals (Mistry, 1993; Adam et al., 1993; Musokotwane and Ndalamei, 1993). These types of transactions were not seen to any extent in Botswana and Zimbabwe largely because of the domestic availability of goods which were scarce in Malawi and Zambia and because of the more efficient policing of their internal regimes.

Another regional aspect which affects government budgets and deficits in SAR is the recurrence of periodic, severe droughts which destabilise government finances despite substantial external emergency relief and food aid. The last such drought occurred in 1992-93 and resulted in extra-budgetary burdens on almost all SAR governments. Deficits (as a percentage of GDP) for 1992-93 showed a significant rise (and in Botswana the surplus showed a fall) over 1990-91 in the case of Malawi, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe, partly to cover the extra expenditures governments had to incur to cope with the drought and to mitigate its significant repercussions on agricultural output in the affected SAR economies. Had the response of donors not been as generous and swift, and had regional coordination on grain transport (by sea, rail and road), storage and distribution not been as effective, the deleterious fiscal impact could well have been much larger. From the viewpoint of food security, permanent regional arrangements for financing and holding grain buffer stocks, as well as for grain storage, transport and distribution, would go a long way towards ameliorating exigent, unanticipated pressures on government finances in SAR, which are fragile enough.

Although several other regional phenomena have an impact on government budgets and fiscal deficits in SAR, there is little value in belabouring a point already illustrated. Three specific observations are, however, worth making. *First*, as observed earlier and as later paragraphs will elaborate on, common regional approaches to infrastructural investment and service provision could have major implications for easing public development expenditure as well as recurrent expenditure burdens thus contributing significantly to deficit reduction and fiscal stabilisation throughout the region. To quote one instance, the individual airlines of SADC countries (including South Africa) are insatiable consumers of foreign exchange and incur significant annual operating net losses requiring state subsidies of between 3-8% of GDP each year (AfDB, 1993; Medhane, 1990).

Rationalisation of airlines, airport networks and air traffic control and navigation systems in the region would result not only in improved services at lower costs with more customer-friendly schedules but would probably save 4-5% of the region's GDP with a relatively even distribution of such savings across SADC countries. Privatisation of these airlines would induce not only market-based rationalisation and merger; it would eliminate the need for governments to provide operating subsidies and investment capital to the industry. In recognition of the drain that national airlines impose on public budgets, the IMF/WBG eventually forced closure of Zambia Airways in 1994. But that was only one case and similar action has not been taken elsewhere. Extending the airline example to railways, road haulage services, ports, coastal shipping and other infrastructure, a regional approach to infrastructure service provision would have a major beneficial fiscal impact enabling governments to focus scarce budget resources on higher priority social and development expenditures which would facilitate adjustment rather than having it impeded by vested interests which see themselves as losing out from it.

Second, as the region enters a new era of peace and security for the first time in over a quarter-century, opportunities have arisen for drastic reductions in military expenditures (milex) which could be reciprocally negotiated among SADC countries under a regional protocol. Excluding Angola, for which official recent figures are not available, milex in the region averaged about $6 billion (in 1993 dollars) annually between 1986-93 dropping from a peak of nearly $7 billion in 1989 to around $4.5 billion in 1993 (Mohamed, 1995) but nevertheless accounting for about 4% of regional GDP in 1993 (see Annex Tables 9-11). Angola's milex in 1993 was estimated at roughly $1.2 billion. For individual countries, milex in 1993 ranged from 0.4% of GNP (Mauritius) to 7.6% (Mozambique) and (an estimated) 12% of GNP for Angola. Although milex has already been substantially reduced by countries like Tanzania, Zambia, Zimbabwe, Lesotho and South Africa (albeit increased by Botswana) there remains scope for further reductions to an average for countries across the region of no more than 2% of GDP. Regionally agreed reductions of that scale, coupled with mutual defence and security arrangements binding SADC countries together, would release around $2-3 billion for either budget savings or for other higher priority public expenditures across the region. That is perhaps the least that SADC members and the IFIs should seek to achieve following a decade in which the cost of physical destruction and loss of GDP resulting from regional conflict is conservatively estimated at having been around $10 billion annually (ECA, 1989).

The *third* and final point about approaching fiscal adjustment under SAPs with a regional perspective in mind is concerned less with the size of savings that could be derived from regional cooperation on various fronts and more with the prospect of increasing revenue yield across all the members of SADC by (i) harmonising tax and tariff structures (to avoid intra-regional tax arbitrage by individuals and corporations), and (ii) collaborating on revenue administration and collection to enforce greater compliance with more reasonable rates of direct and indirect taxation. The experience of the SACU vs. non-SACU members of SADC in that regard is salutary.

Much could be gained by contemplating the coordination of customs and revenue administration throughout the region especially by employing common taxation codes, training practices, standards, principles and information sharing, as well as engendering higher levels of probity throughout the region where revenue administration is concerned. In many instances in SAR (e.g. Malawi, Tanzania, Zambia and Mozambique) sweeping changes in the tax code have been prescribed which call for massive legal, regulatory and administrative efforts, the capacity for which simply does not exist within individual SAR countries except perhaps South Africa. And these changes are being prescribed at a time when simultaneous prescriptions are made to cut expenditures on the civil service, restructure and privatise state enterprises and generally increase the administrative burden which relatively incapable governments must bear to effect the transformations desired. A regional approach, involving a large dose of tax regime harmonisation during the redesign stages, would probably offer a far more effective way of improving tax administration and revenue enhancement than relying solely on national capacity.

Moreover, given the dependence of SADC countries on mineral production for their output and exports, and the complementarity of production in similar minerals (copper, diamonds, gold) across several SAR borders, often undertaken by the same global mining conglomerates, it is particularly important that mining legislation and taxation be regionally harmonised (AfDB, 1993) and that tax codes are evenly enforced. This is equally true when it comes to the frenetic race that every country in the region is now in, often at IFI urging, to attract foreign investment (portfolio and direct) through, *inter alia*, fiscal incentives when other conditions for attracting the entry of such investment – infrastructure, capital markets, administrative capacity and business support services – are distinctly unequal. Experience in other developing regions (including East Asia) suggests that inappropriate or thoughtless fiscal competition to achieve specific and limited objectives in attracting FDI usually attracts the wrong kind of FDI and is likely to leave the region as a whole worse off while leaving no member country significantly better off.

In SAR virtually all countries confront a major shift in sources of revenue away from taxes on trade to taxes on other transactions which may be more difficult to calculate and collect. What national SAPs have achieved to a limited extent in SAR is expenditure-reduction with the singular aim of reducing an unsustainable deficit. What they have not yet achieved are (i) sufficient expenditure switching in desirable directions to make adjustment more palatable and effective; (ii) increases in revenues from other sources of taxation and from improved compliance and collection; (iii) adjusting governments and IFIs making the right choices in balancing the mix of revenue-raising, expenditure-reducing and expenditure-switching measures (World Bank, 1994a); (iv) resolving conflicts in the revenue enhancing advice offered by the IFIs at the national level in terms of overall fiscal policy (usually by the IMF) vs. sector-specific advice given to promote sector adjustment and growth (usually by WBG); and (v) effective approaches to intersectoral prioritisation to achieve efficient public investment programme rationalisation especially in expenditure-constrained environments which usually result in sharpened political competition for conflicting expenditure priorities.

These five areas of relative failure may have a negative impact on both medium-term adjustment and long-run development even when the desired deficit reduction is achieved in the short-run through just expenditure cuts. Attempting to enhance revenues by increasing marginal rates and tax burdens on a narrow taxable base may have exactly the opposite incentive effects to those intended by a SAP. Similarly, prescribing savage expenditure reduction in countries where the supply of public goods and service is already below an acceptable level can impair long-run development prospects.

Perhaps the saddest example in SAR (and throughout Africa) is that a decade of adjustment focused excessively on expenditure reduction, and not enough on revenue raising and expenditure switching until much later in the game, has probably resulted in compromising the lives of yet another generation of young Africans. Savage across-the-board public expenditure cuts were countenanced in the face of misdirected government priorities in health, education, food subsidies and social safety nets at a time when population growth, the spread of chronic contagious diseases and the onslaught of AIDS have increased the problems which governments confronted. The net result has been a deterioration in the quality of human capital available to tackle future challenges of growth in SAR when its adjusting economies require precisely the opposite.

Whether a regional approach would necessarily help in tackling these five problem areas better than a national approach to adjustment is an interesting but open question which needs further contemplation. What is clear is that these problem areas need to be addressed and any approach which progresses matters is worth trying. What a regional approach might achieve is to give SADC a much more powerful collective voice in constructive dialogue with its IFI and donor interlocutors than any individual SAR country could possibly have on its own. Moreover, a sharing of regional experiences with these problems may point to ways of resolving them and might induce greater harmonisation on the fiscal policy front as commonalties and mutual interests become clearer.

2. *Monetary Policy*

The proposition that monetary policy is perhaps an area of adjustment in which a regional approach might yield significant benefits and facilitate swifter adjustment is intuitively more acceptable than when the same argument is attempted on *prima facie* grounds for fiscal policy. But as the European Exchange Rate Mechanism's experience between 1992-95 suggests, intuitive judgements cannot always be taken for granted. The conditions under which regional monetary policies are beneficial to participants need to be clearly appreciated – whether coordinated informally by tracking a regional anchor and undertaking whatever macrofinancial policy adjustments are necessary to maintain equilibrium with it, or through formal arrangements involving reciprocal obligations. Equally, the commitments and obligations which member nations need to make for such arrangements to work properly need to be honoured in the keeping and not the breach.

A cursory look within SAR suggests that members of MMA appear to have fared better in managing their monetary parameters than their other SADC neighbours between 1980-95. SACU members have suffered from less ravaging inflation, less volatile and large swings in real interest rates and have had more stable exchange rates. Though two SACU members (Lesotho and Namibia) suffered from excessive *internal* account imbalances, the other three did not. In all SACU countries and Mauritius, *external* account imbalances have been lower than in other SADC countries between 1985-94. Consequently they did not have to make such large and painful eventual adjustments to restore balance.

The catch, however, is that SACU-MMA are not arrangements among economic equals but among countries which are highly unequal. SACU-MMA have been sustained so far by strong political motives on the part of South Africa, rather than by considerations of economic efficiency alone. It is clear that the *raison d'être* for the continuation and inevitable renegotiation of these arrangements will need to be based on economic rather than political rationales. They will also need to be based on an understanding of the real costs and benefits to the members rather than empty public posturing on the basis of visible (but misleading) budgetary costs and other superficial effects.

Some of the consequences of SACU and MMA being underpinned and controlled largely by South Africa are sufficiently unattractive for Botswana (whose international reserves are now larger than South Africa's) to exclude itself from the MMA and for Namibia to contemplate the same possibility. To some South Africans, of course, that asymmetry suggests that Botswana is being opportunistic in benefiting from SACU but not doing enough to share the burdens of MMA. More pertinently, however, South Africa may be entering a difficult and prolonged phase of its own adjustment (much as Germany did with unification in 1992) which could threaten to destabilise, if not rupture the MMA if South Africa chooses to pursue unilateral adjustment policies detrimental to its partners.

Before going into the pros and cons of a plurilateral regional vs. national approach to achieving and maintaining monetary stability in SAR, it is useful to review recent experience with the monetary characteristics of SADC members and efforts at achieving monetary stabilisation in the region (see Annex Tables 12-13).

As alluded to earlier, the core SACU countries have experienced relative monetary stability although domestic credit creation and monetary expansion in Lesotho, Namibia and Swaziland reached disturbing levels but with Lesotho having corrected itself by the mid-1990s. In all three countries, monetary expansion, though moderate by the standards of the non-SACU members of SADC (Mauritius of course being excepted), has been larger than it should have been, particularly in 1993-94. In South Africa, the anchor economy of SACU (and increasingly of SADC), domestic credit creation averaged 11% annually between 1990-94, money supply (M2) growth averaged 11.6% and inflation declined from 15% to under 9%. These parameters have been kept under reasonable control with a regime of positive real interest rates applying to deposits and lending throughout 1985-94. In Botswana, there was significant contraction of net domestic credit creation between 1985-94, accounted for entirely by the government sector reflecting its comfortable fiscal surplus position throughout that period. Money supply growth, however, exploded in the late 1980s reaching over 46% in 1989 but has since moderated to an average of just over 10% between 1990-94 while inflation has remained in a 8-16% band over the last decade. Real (lending) interest rates in Botswana which were around +3% in the mid 1980s, turned negative between 1989-92 but reverted to being positive again in 1993-94. Reflecting the controlled monetary stance of South Africa and Botswana, the real effective exchange rates of the rand and pula remained relatively stable between 1985-94 while the nominal effective rates reflected a gradual depreciation in line with inflation differentials between the rand/pula on the one hand and the US dollar on the other.

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In the non-SACU members of SADC, the monetary picture has been more mixed. There is no reliable annual information available for Angola; a war economy which has been out of control for a considerable period of time. Several partial attempts at reducing inflation and stabilising the exchange rate since 1987 have failed because government has been unable to apply sufficient fiscal and monetary restraint. Inflation was over 500% in 1992, 1800% in 1993 and, though reduced to 900% by mid-1994, it escalated again to a rate of 58% per month toward the end of the year. The kwanza was in a free fall in the parallel market during 1993 and though the ratio of the parallel market rate to the official exchange rate was reduced from 16:1 at the end of 1993 to 3:1, by mid-1994 it started rising again. Officially controlled interest rates have remained highly negative in real terms. When Angola does undertake an IFI-supported SAP, the assertion of monetary control will be among the most difficult objectives to achieve.

In the other SADC countries, Mauritius re-established stability in its monetary regime in the mid-1980s bringing M2 growth down from over 30% in 1985 to an average of around 15% between 1990-94 and inflation down from a peak of over 13% in 1990 to an average of 7% for 1992-94. The nominal exchange rate has been permitted to drift to reflect inflation differentials while keeping real effective exchange rates stable. The story is less encouraging in Malawi, Mozambique, Tanzania, Zambia and Zimbabwe where matters worsened progressively between 1985-91, took a turn for the better in Malawi and Tanzania in 1991-92, but reversed again in 1993-94. Monetary stability has thus remained elusive between 1990-94. Domestic credit (mainly to government) in these countries, has grown in the range of 27-68% annually between 1990-94. Over the same period M2 growth has been between 27-84% annually.

Although real interest rates have been maintained at generally positive levels in Malawi and Tanzania over most of this period (in the range of +5 to +10%) they have been highly negative in Mozambique and Zambia until 1994. In that year they turned positive with a vengeance in Zambia (+33%). Zimbabwe permitted real interest rates to remain negative for too long between 1989-1992 before liberalising rates and seeing them become positive in 1993-94. The absence of sufficient monetary discipline has resulted in these countries experiencing high levels of annual inflation (ranging from a low of 25% for Malawi to a high of 200% for Zambia) during 1990-94 as well as high instability in their nominal and real exchange rates.

This overall picture suggests that, other than in SACU and Mauritius, monetary policy in the rest of SADC has not yet been as effective as hoped. Monetary stability in the six other SADC countries remains elusive with major reversals occurring each time that the IFIs and governments have begun to believe that the corner has been turned. Would embracing these six countries progressively within multilaterally-backed regional arrangements – an extended MMA – provide the anchor they need to break the vicious cycle of deficit-monetisation-inflation-devaluation-deficit they seem locked into, and achieve greater monetary stability more swiftly than has been the case so far?

Perhaps the best single reason for believing that regional monetary arrangements in SADC might work is that a plurilateral framework, involving peer group pressure for exerting monetary discipline, might well serve to exercise greater restraint over the abuse of seigniorage powers than SAR's politically vulnerable national governments are capable of exercising under short-term domestic political pressure. It would be much more difficult for SADC governments to run large deficits and monetise them for short-term political expediency if the process of monetisation was restrained by plurilateral decision-making involving wider, long-term regional interests. But the economic characteristics, structures and monetary/fiscal parameters between SACU/Mauritius on the one hand and the other SADC-six (AMMTaZZ) on the other, appear at present to be too divergent to contemplate such arrangements being sufficiently robust and resilient to endure. Nevertheless, if regional arrangements were to be aimed at, various convergence criteria (i.e. monetary, inflation and fiscal targets) could be established which might induce individual countries to strive harder to meet these criteria and attain membership.

In this context, it used to be believed, axiomatically, that real/nominal convergence were essential *prerequisites* to the effective operation of common monetary arrangements; following from the view that the location of economic activity is subject to centripetal forces generated by the process of economic integration (Myrdal, 1957; Perroux, 1959). The neo-classical view is now inclined toward believing that, instead of being a prerequisite, convergence may actually be a *consequence* of closer economic and monetary integration for two reasons. *First,* free movements of goods and services, in an environment which is free of foreign exchange risk, will lead to eventual equalisation of factor prices, factor productivity and output per capita. *Second,* as there is no trade-off in the long run between inflation and unemployment, price stability can legitimately be pursued as an economic objective in its own right without raising the spectre of entrenched unemployment. Moreover, when regional arrangements hold out the promise of resulting in greater price and exchange/interest rate stability, they can improve the trade-off between inflation and unemployment in the short-run because of the positive effects of expectations on trade and investment. Such arguments support the logic that inflation

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convergence need not be a precondition for common monetary arrangements but will come about as a result of their existence and operation (Chipeta and Mkandawire, 1994).

The other arguments in favour of common monetary arrangements in SAR around a *rand zone*, gravitating eventually towards monetary union (though this need not be an objective of such arrangements at the outset) are that:

- they require credible commitments on the part of members to monetary, fiscal, exchange rate and price stability which might be difficult for them to meet unilaterally;
- potential savings can be derived from the pooling of international reserves;
- ensuing intra-regional exchange rate stability and interest rate convergence will reduce barriers to trade and investment caused by high exposure on the part of traders and investors to foreign exchange and interest rate risk in excessively volatile regional currencies and monetary regimes;
- there would be a general reduction in intra-regional transaction costs;
- freer intra-regional flows of investment capital and trade finance would be triggered and sustained, especially between SACU/Mauritius and AMMTaZZ, than would be the case if present circumstances persisted;
- significant capital and administrative cost savings would result from a common financial institutional and regulatory framework whose operations are more viable when applied over a larger market base;
- more rational, effective operation of monetary policy, and prudential supervision of banks and securities exchanges could be achieved at the regional vs. national level especially when the resources of several small economies are pooled to share in the advantages of a strong, independent central monetary authority, the core of which already exists in South Africa and Botswana;
- the re-establishment of monetary stability in AMMTaZZ, would restore lost public confidence in local currency as a store of value and result in both increased overall savings as well as an increase in the proportion of financial savings; and,
- the perennially increased needs for extraordinary levels of concessional aid from donors to finance the costs of fiscal and monetary instability in the region – which are exacerbated by unaffordable external debt service burdens in AMMTaZZ – could be substantially reduced, if aid was applied instead to backstopping regional monetary arrangements which had more efficient macroeconomic effects (AfDB, 1993).

As with every economic tool or policy, common monetary arrangements (which have actually characterised SAR for much longer than unilateral ones albeit through a colonial history) are double-edged mechanisms; they are not costless. Issues arise with the distribution of seigniorage returns; the implied loss of sovereign flexibility in the use of the exchange rate as a tool for correcting external account imbalances, and for macroeconomic correction and adjustment; and the intra-regional developmental imbalances that can be perpetuated if not compensated for through appropriately designed regional policy and compensatory financing arrangements (Robson, 1993).

Moreover, many previous theoretical and empirical analyses have suggested that common monetary arrangements and optimal currency areas only work well when the following conditions are met: geographical contiguity of members; a high degree of intra-regional trade; free intra-regional factor mobility, particularly for capital and labour; wage-price flexibility; strong political will and technocratic cooperation to make regional arrangements work; gains from monetary integration are not asymmetrically captured by the more developed members;[8] there are checks-and-balances operating on the larger anchor economies to avoid passing on the costs of their macroeconomic miscalculations to their partners; reserves are adequate to backstop these arrangements under temporary balance-of-payments stress; there is relative openness in the economies of participating members vis-à-vis each other; participating economies are relatively diversified in their production structures so that exogenous shock effects are not overly concentrated; and participating members are committed to coordinating balanced fiscal policies with strict budget discipline.

Without going much further into the theoretical and empirical pros and cons of whether regional monetary arrangements might provide a superior option for achieving monetary stability in SAR (especially in the AMMTaZZ countries) and taking into full account the experience of the

8 On the issue of extant regional asymmetries in levels of development becoming embedded, recent analysis (Krugman, 1990 and 1991) suggests that under regional integration arrangements, the *centralisation* of economic activity is likely to be reinforced when returns from economies of scale are large and the location of manufacturing activity is relatively immobile, whereas *decentralisation* is likely to occur in a region where transport costs are more important as a proportion of final product cost. In SAR: (i) the returns from economies of scale are likely to be large; (ii) manufacturing activity can be quite mobile in response to sufficiently large differentials in tax-adjusted factor costs adjusted for factor productivity, but may be immobilised by gaps in the availability of infrastructural and business support services and in the availability of an appropriate and honest regulatory framework in which political and bureaucratic rent-seeking is minimal (in relative if not absolute terms); and (iii) transport costs constitute a very high proportion of final product costs.

MMA in SAR (AfDB, 1993) and of the CFA arrangements in Francophone West Africa (Honohan, 1991) there is a powerful intellectual case for the IFIs to rely more on *regional* rather than national approaches to monetary stabilisation in SAR. It is a case which neither the WBG nor the IMF have given sufficient thought to, perhaps because of the obvious impracticality of doing so under political and economic conditions in SAR which were quite different to what they are now. The current constitution of SADC offers more benign and more efficient (although by no means as yet problem free or entirely practicable) options for regional monetary cooperation as a means to the stabilisation end and thereafter to the maintenance of monetary balance in the region on a sustained basis.[9]

3. *Exchange Rate Policy*

Related closely to the question of whether common monetary arrangements might facilitate monetary stabilisation throughout SAR is that of whether greater exchange rate stability can be achieved and maintained (intra- and extra-regionally) as an integral part of such arrangements. Before that question can be answered, it is necessary to ask what the experience of SADC countries has been with exchange rate policy and exchange rate management regimes. Has exchange rate stability in the context of competitiveness and greater openness been achieved over the last decade? Have exchange rate adjustments resulted in anticipated current account adjustments and rectified resource imbalances in SAR? Clear-cut answers to these questions are difficult to come up with although the evidence suggests that exchange rate adjustments by themselves have not achieved the desired effects, especially in the non-SACU economies of SADC. This despite the fact that the size of exchange rate adjustments in all of these countries, other than Mauritius, has been quite large and, in the case of three countries, excessively so mainly because devaluation-inflation spirals went out of control.

That said, it is particularly difficult in any of these countries to isolate

9 In that context it is worth mentioning three independent efforts undertaken in the 1990s arguing the case for closer regional monetary cooperation for achieving adjustment and growth objectives in SAR which the IFIs need to take cognizance of (i) the African Development Bank's analysis, particularly in the Finance Chapter of its 1993 report on *Economic Integration in Southern Africa;* (ii) the former PTA's (now COMESA) 1990 study on its proposed *Monetary Harmonisation Programme;* and (iii) a recent paper produced under the aegis of the African Economic Research Consortium (AERC) on *Monetary Harmonisation in Southern Africa* (Chipeta and Mkanadawire, 1994). Using the substantially larger intellectually resources available to the IFIs, these initiatives need to be built on and developed into operationally viable concepts.

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the effect of the exchange rate adjustment alone in restoring current account balance or in achieving a switching from imports to domestic goods in the case of tradables. The macroeconomic programming model for guiding adjustment treats the real exchange rate (RER) as a key variable in restoring equilibrium when there is a large current account deficit or resource imbalance. If – under the econometric models used to calculate required adjustments in different targets, prices and parameters – the fiscal and monetary measures required to restore internal and external balance show an unsustainably large and persistent current account deficit at the prevailing exchange rate, then a large real exchange rate devaluation is prescribed. This is generally brought about by a large initial *nominal* devaluation, accompanied by tight fiscal policy, to control the inflationary effects of the exchange rate adjustment thus transforming a nominal devaluation into a real one. If, in the short run, devaluation triggers destabilising impulses on the capital account, tighter monetary policy is brought into play to mitigate the consequences and restore external balance.

African countries in general and SAR countries in particular have had reservations from the outset about the impact of devaluations on the subsequent controllability of their unusually fragile economies whose structures are rigid and unresponsive. Except for Tanzania (1990) they have been unable to articulate their fears and concerns in cogent terms using the jargon that IFIs comprehend. They were intellectually overwhelmed by the IFIs when it came to arguments in negotiating adjustment conditionality on exchange rate adjustments. The two recent reports from the World Bank on adjustment experience in Africa (1994a and 1995a) are disturbingly vague and obscure in their assessment of whether exchange rate adjustment in Africa has worked or not, conveying a general sense of discomfort about outcomes but not advancing sufficiently clear or cogent explanations or alternatives. The IMF, with its usual aura of intellectual and operational infallibility of course suffers from no such inhibitions (Schadler et al., 1993) claiming considerable success for exchange rate adjustments but on the basis of evidence that is open to debate. The following paragraphs attempt to discuss in much simpler terms whether the experience of countries in SAR confirms theory.

Over the 1988-95 period, the level of domestic currency depreciation has been least in Botswana and Mauritius, the two strong economies of SAR, although Botswana was affected by importing South African inflation with the pula being dragged by a faster depreciating rand. Over the eight-year period, the Botswana pula has depreciated in nominal terms against the US dollar by 30% and the Mauritian rupee by 18%, while both currencies have appreciated against the rand. Both countries have attempted to pursue policies of maintaining a relatively stable trade-weighted real effec-

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tive exchange rate (REER) and have generally succeeded in doing so with few hiccups. In terms of stability, the MMA regime has performed next best, with South Africa's rand – which underpins the Namibian dollar, Lesotho loti, and Swazi lilangeni at unit parity – depreciating over the 1988-95 period by 34% against the US dollar and to a lesser extent against the pula and Mauritian rupee.

Nominal devaluations in the AMMTaZZ economies have been much greater, falling into two categories. The depreciation of the Angolan, Zambian and Mozambican currencies have approximated Latin American levels of the 1980s with the kwanza and Zambian kwacha depreciating by over 99% against the US dollar and the metical by 91%. The level of annual inflation has made it difficult in these countries to attempt any fine-tuning of the REER to retain competitiveness – whatever that term means in these particular countries. Nonetheless, available indices suggest that Zambia has had some success in stabilising its REER although the impact of that achievement on its current account remains difficult to fathom. Mozambique has been less successful and despite large devaluations has seen its REER appreciate and Angola even more so, although any attempt to measure the REER in that country, leave alone stabilise it, may border (under present conditions) on the absurd. Moreover, officially set rates in Angola mean very little in practice since most transactions outside of government accounts are settled at parallel market rates.

In the second category are the less drastic but nonetheless large nominal devaluations of Malawi's kwacha, the Tanzanian shilling and the Zimbabwe dollar, against the US dollar which have approximated 83%, 79% and 77% respectively. In these countries there have been attempts to stabilise or actually depreciate the REER with continued nominal devaluations, but the inevitable lags in the timeliness of devaluations has resulted in REERs appreciating in Tanzania and Zimbabwe and stabilising in Malawi. Thus the countries of SAR fall into bands as indicated in Table 3.

Table 3 Exchange Rate Adjustment, Inflation and Actual Adjustment in SAR

Devaluation vs. US dollar (1988-95)		Inflation Countries	Adjustment Range
A. 20% <<	Mauritius	10%<<	Internal and External
B. 30-40%	The SACU Five (BLNSAS)	12%-15%	External
C. 75-85%	Malawi, Tanzania, Zimbabwe (MTZ)	25%-35%	Neither Satisfactory
D. >> 90%	Angola, Mozambique, Zambia (AMZ)	75%-1,000+%	Out of Control

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The overall impact of exchange rate adjustments in the four categories mentioned in Table 3 tends to mirror the size of the devaluations which have occurred. Of the SADC economies Mauritius has adjusted best while depreciating the least.[10] At present it has the fewest problems of inflation, monetary and fiscal control, trade regime liberalisation and savings/investment. Its internal and external accounts are in sustainable balance. The SACU-5 have adjusted less well with higher inflation and mixed experiences with fiscal deficits although all have reasonable monetary control. They have been more successful in stabilising their external accounts than their internal accounts. Their adjustment problems however may continue for some time as South Africa undertakes its own adjustments and begins to liberalise its trade and exchange regime with the hiccups that can be expected as a result of a more fractious and less predictable system of political governance.

Malawi, Tanzania and Zimbabwe face more difficult problems with exerting fiscal and monetary discipline, and have significantly higher levels of inflation than the SACU countries (25-35% vs. 12-15%). Yet they appear to be veering towards internal account stabilisation despite several reversals, while external account stabilisation remains problematic. The AMZ countries are the worst off by far. Their devaluation-induced inflationary spirals remain out of control and internal and external account stabilisation are remote prospects.

Most SAR countries continue to be heavily dependent on commodity exports for which they are price takers (except perhaps for gold and diamonds) and whose volumes are entirely dependent on world market demand-supply conditions. From the evidence available it would be difficult to assert, for any SADC country other than Mauritius, that the conduct of exchange rate policy has made a material difference to improved export performance or diversification or to improving fundamentally the resource imbalance. It would be equally difficult to establish, in most of these countries, the extent to which import demand was influenced by exchange rate policy and the large relative price changes which successive exchange rate adjustments resulted in. The absolute constraint of import finance availability – which (except in SACU countries and Mauritius) was alleviated mainly, if not only, by concessional aid flows – makes it difficult to estimate the domestic demand-reducing effects of depreciation in the chronically aid-dependent SADC economies. Moreover, with liberalisation, long-repressed demand for consumption imports was unleashed

10 The IMF and World Bank might argue conversely (and perversely) that Mauritius has had to devalue the least because it adjusted the fastest; but this argument confuses the question of cause and effect.

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resulting in an unanticipated surge of consumption imports (instead of capital goods and intermediates) being financed which did not have any lasting growth-inducing effects (Martin and Mistry, 1996).

In those countries (Lesotho, Malawi, Mozambique, Tanzania and Zambia) where donor-disbursed concessional flows provide the largest source of free foreign exchange the concept of a *market-determined* exchange rate is, to say the least, a bit odd. The market for foreign exchange can be severely destabilised by inadvertent or deliberate slowdowns or acceleration of fast disbursing loans and grants resulting in parallel market signalling which can throw monetary and exchange rate policy (and by linkage) even fiscal policy completely off course. Consequently, outside of SACU and Mauritius, what frequent and significant devaluations in previously fixed or quasi-fixed exchange regimes in SAR – with economies whose imports are largely price inelastic and whose domestic supply side capacity is weak or non-existent – appear to have achieved is the following:

- significant increases in the interest component of primary budgetary deficits in domestic currency (often covered by parallel increases in the quantum of external grants) as a result of the need to meet inflated debt service obligations to preferred creditors even as other debt remains unserviced;
- enlargement of the fiscal deficit as a result of more local currency being required by government to finance essential survival imports (again often covered by donor-provided import-support grants);
- a general cost-push rise in domestic price levels triggered by each devaluation adding to inflationary pressures because of the incapacity of SAR economies other than South Africa and Zimbabwe to benefit from switching effects;
- an environment in which, even as public investment is being sharply compressed, volatile exchange and interest rates, accompanied by frequent monetary squeezes, eliminate any incentive for long-term investment on the part of the domestic or foreign private sector because of increased risk and exacerbated uncertainty; and
- diminishing any incentive for long-term financial savings in domestic currency holdings or in domestically denominated financial instruments, except on a speculative basis, to capture arbitrage opportunities arising from inevitable temporary policy twists or failures.

These five effects have increased the intensity and volatility of the devaluation-inflation cycle and created a chronic degree of aid dependency in the non-SACU economies of SADC with extraordinary assistance rising to unsustainable levels (e.g. $100 per capita in the case of Zambia), yet with no clear strategy in sight for an exit from the debt-aid trap. Somewhat disconcertingly, SAP prescriptions contain no remedies for weaning these economies off their absolute dependence on external assistance within the next decade without running the risk of destabilising them completely yet again. Instead, they attempt to justify requests for continually higher levels of extraordinary grant financing from donors on the grounds that adjustment is taking longer than earlier anticipated.

Moreover, a careful look at changes in the volume, value and structure of exports and imports in SADC countries over the last decade of adjustment, does not suggest that exchange rate adjustments have worked their magic in any of the countries (Martin and Mistry, 1996, forthcoming) except perhaps in Mauritius which has undertaken the least amount of it while keeping its other policies in balance. Indeed, if improvements in export and import growth and diversification were to be correlated with the relative sizes of real exchange rate adjustments undertaken by SAR countries, the exercise would probably end with inconclusive results, if not a statistically significant inverse correlation. But such an exercise would be intellectually suspect since the structure of SAR exports is not particularly affected by the relative exchange rate, nor is the demand for imports affected by an increase in their domestic price, at least not at these low, rock bottom levels of demand for the AMMTaZZ countries.

Other policies and physical phenomena (not least drought, weather, war, and movements in the terms of trade) play a much more powerful role in influencing external account outcomes – suggesting that the IFIs' obsession with exchange rate adjustments in SAR may have been excessive and misplaced. That large initial nominal devaluations were required is unarguable. That the IFIs expected such nominal devaluations to be accompanied by the kind of fiscal and monetary restraints which would contain inflation was naïve beyond belief. That they predicated their prescriptions on the ability of weak and ineffectual institutions and governments to hold the line on domestic pressures after these large devaluations was mildly absurd. What was needed were large nominal devaluations immediately succeeded by credible arrangements (backstopped by sufficient financing and early action on debt and debt service reduction) to *stabilise* the devalued exchange rate – nominal and real – permitting enough time for stability to be achieved without igniting an inflationary spiral. Instead, initial devaluations were not bolstered by credible arrangements nor by sufficient external financing, forcing large and repeated adjustments tuned to over-exaggerated price signals emitted by parallel market premia; when it was widely accepted that these markets were highly imperfect and ultra-sensitive to expectations about exchange rate movements which neither the IFIs nor governments fully understood. In that sense, an overdone preoccupation with theoretical purism may have obscured the need to consider more pragmatic options to achieve external account improvement in a context of growth, with lower rather than heightened risk for investors and savers.

More evidence needs to be marshalled to convince the IFIs that continuous devaluations are probably not the right policy response to adjustment failure or stickiness in SAR. The time may well have come to contemplate the possibility of stabilising (though not necessarily fixing rigidly as in the case of the CFA) exchange rates for a reasonable period of time to reduce risk and uncertainty, and to create a more benign climate for trade and long-term investment. Moreover, it may also be an opportune time to pause and reflect on the effect that exchange rate turbulence in SADC, outside of SACU and Mauritius, is having on closer regional integration, especially in terms of investment and trade.

These effects have been carefully considered in the AfDB's Report (1993) on integration in SAR leading to suggestions for a regional exchange rate stabilisation mechanism (REXSTAB). That study has recommended expanding payments and settlement arrangements based around the South African rand in SAR, coupled with regional exchange rate stabilisation arrangements between the rand and other regional currencies. By extending the embrace of a rand-zone throughout SADC, the foreign exchange constraint to adjustment and development could be relieved far more effectively than has been achieved so far by IMF/WBG prescribed SAPs. Neither the IMF nor WBG have taken up seriously the idea of extended *regional monetary arrangements* in SADC perhaps because political conditions in the region until 1994 precluded any prospect of such arrangements being put in place in the non-SACU countries. Those conditions have now changed radically and the idea needs to be revived and operationalised.

REXSTAB is conceptually equivalent to extending MMA cover to non-SACU countries on a progressive basis, but with the support of external underwriting arrangements (multilaterally funded) similar to those which operate under the relatively successful, if excessively rigid, CFA franc arrangement. Such an arrangement might have accomplished more by way of closer integration and more effective adjustment in SAR than the painful and unsatisfactory sequential devaluations which have been resorted to repeatedly under SAPs; often leading to devaluation-induced inflation spirals which have proven difficult to control and reverse. These have had unanticipated and unintended consequences not the least of which have been (i) rapid de-industrialisation; (ii) absence of domestic switching effects which exchange rate corrections should produce; and (iii) ever-increasing reliance on scarce concessional aid flows to keep these economies afloat, especially in the absence of satisfactory debt and debt service reduction arrangements – in particular for multilateral debt.

It needs to be emphasised, however, that this argument is predicated on two critical assumptions (i) that the present and future governments of the new South Africa can *always* be relied on to pursue prudent and sound macroeconomic and structural policies which are of benefit to itself and the region, and (ii) that REXSTAB will be prudently governed by an independent plurilateral monetary authority. Sufficient international safeguards need to be put in place to ensure that default by South Africa in this respect can be either swiftly corrected or that its neighbours can be insulated from the effects of such default. Should that caveat not apply, the argument would of course be invalidated.

In making its suggestion the AfDB observed that further analytical work needed to be done to examine the feasibility of REXSTAB and define its institutional and operational contours after intra-SADC consultations had been held among the region's ministries of finance and central banks. In the meantime, Malawi and Mozambique have already indicated their desire to join the MMA on various occasions precisely in order to re-establish exchange rate and monetary stability. It is a matter of some urgency that this proposal, which has been on the table for nearly three years, now be taken up by the IFIs and SADC governments as a concrete regional step. Extending MMA and establishing REXSTAB would facilitate adjustment in a manner likely to be more efficacious than attempts with continued unilateral exchange rate adjustments. Such attempts have been tried since 1980 but have failed to deliver the goods for most countries in the region. It is time to consider an alternative approach with regional dimensions which would further the prospects for successful adjustment and closer integration simultaneously.

4. *Labour and Wage Policy*

In theory and rhetoric SAPs usually call for removing rigidities and distortions which impede the efficient functioning of factor markets, often alluding specifically to rigidities and distortions in formal labour markets. But this particular aspect of macroeconomic adjustment does not feature as strongly in the conditionality of IFI-supported SAPs as do aspects concerning fiscal, monetary, exchange and trade policies. Perhaps that is because labour-related conditionality is too politically charged; or because it involves trade unions – institutions which the IFIs do not have the same comparative advantage in dealing with as they do with central banks and ministries of finance – or even perhaps because it has profound societal implications which the IFIs cannot cope with.

It is not that IFIs are oblivious of the problems that SAPs create in terms of widespread dislocations and displacements of labour in Africa and SAR. They usually side-step these with references to the experiences of adjusting countries in Asia and Latin America – in which post-adjustment employment generation and export effects have been undeniably impressive – without mentioning that those conditions often do not apply in Africa. In Africa, human capital is still largely undeveloped, traditions of entrepreneurship are not particularly deep or wide, indigenous, non-African entrepreneurs are distrusted and often vilified as exploitative, and a sufficiently broad-based private sector has yet to develop.

Major difficulties will be faced by African countries and firms attempting to force competitive entry into world markets for manufactured and service exports already dominated by other developing countries and by economies in transition, especially when Africa lacks the competitive business support services or infrastructure. In IFI reports, it is usually argued that adjustment has resulted in benign effects in unleashing markets, unlocking entrepreneurship, and – relying on private small and medium enterprise – generating labour-intensive opportunities. But these hypothetical palliatives, even if they worked in practice, would be woefully inadequate when the IFIs advocate public retrenchment at a pace much too rapid for adjusting African economies to absorb without running the risk of counterproductive social and political resistance-often within the structures and institutions of government itself. These real world problems are usually dealt with by the IFIs at the level of vague generalisations rather than through imaginative and concrete labour absorption measures and conditionalities.

Neither of the World Bank's two recent reports evaluating adjustment experience in Africa (1994a and 1995a) are particularly illuminating on how its SAPs and SECALs have fared with the liberalisation of labour markets (apart from attempting to persuade a few governments to remove restrictions on hiring and firing) or wage policies.[11] They have, however,

11 The 1995 World Development Report of the World Bank entitled *Workers in an Integrating World*, alludes to the African problem of labour absorption and labour market adjustment observing that (i) There are about 70 million workers in sub-Saharan Africa struggling with adjustment (p. 99); (ii) Labour does tend to suffer during the initial period of adjustment and possibly more than capital ... because capital can flee but labour cannot (p. 104); (iii) Adjustment can pay off for labour despite temporary declines in employment and real wages as the experience of adjusting African countries during the 1990s demonstrates (p. 104); (iv) Although data on wage and employment trends in Africa are scarce, evidence on two adjusting countries – Ghana and Tanzania – reveals that both employment and wage performance improved following structural reform (p. 104). However, the picture the World Bank presents is misleading. Various independent commentators (e.g. Mosley et al., 1995) have debunked convincingly the methodology and statistical analysis that leads the Bank to assert that adjustment is working in Africa. The differences in performance which the Bank points to between strong-adjusting and weak-adjusting African countries is statistically insignificant. Moreover, the two examples the Bank quotes are subject to qualification. Ghana has had reversals causing it to lose its lustre as a paragon of adjustment success, and it is much too early to trumpet success in Tanzania, especially on the employment front.

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invoked the usual theoretical implications that labour market and wage policy rigidities might have in increasing production costs, reducing productivity, stifling investment, inhibiting formal-sector job creation, and protecting workers in the formal sector to the detriment of those unemployed. The IMF's Occasional Paper on *Economic Adjustment in Low-Income Countries* (Schadler et al., 1993) does not discuss labour market policies except in referring *en passant* to token gestures for retrenched workers as part of a side-discussion on the social dimensions of adjustment.

The World Bank's 1994 report suggests that its experience with labour market reform in Africa is limited to three countries in the CFA zone and in other countries to the limited issue of compensating retrenched workers in state-owned enterprises. It goes on to note that:

> 'There has been little systematic study of labour market regulations in Africa or of their impact on economic activity, so it is difficult to evaluate the costs of various restrictions and the benefits of reforms. Most of the barriers are believed to be more of an implicit tax than an absolute barrier. Firms usually find ways – sometimes costly – of getting around the regulations.' (*Adjustment in Africa*, World Bank, 1994, pp. 92-93)

This reflects scant regard for the interplay between other macroeconomic reforms and their impact on a critical factor market, suggesting that the only factor market the IFIs are interested in transforming is the market for money and capital. That is a glaring omission given the challenge that labour markets in Africa pose to the adjustment process, especially in view of Africa's disconcerting demography, its rate of unbridled population growth, its relative lack of resources to focus on rapid and broadly based human capital development, and its incapacity to absorb the about-to-be-retrenched, leave alone new additions to the active labour force.

These factors are already creating significant social pressures translated into higher crime rates, widespread lawlessness, a counter-culture of dispossession, and other pernicious social effects with potentially explosive political repercussions for the medium term. Such trends do not bode well at a time when African economies are being severely tested by attempted transitions toward more genuine forms of democracy which are all too vulnerable to demagogic capture. IFI-generated literature therefore does not provide an acceptable basis on which to judge what has happened with regard to labour market and wage policy at the *national* level in SAR nor to compare that with what might be possible if labour markets and their reforms were approached with *regional* dimensions in view. The AfDB's

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report on integration in SAR (1993) on the other hand is more informative and useful in indicating the need for a regional labour strategy.

In 1995, SAR had an economically active population of about 42 million of which South Africa accounted for a third, Angola, Mozambique and Tanzania, for another third, and the other eight SADC countries for the remainder. This pool will increase by about 15% by 2000 and by a further 32% between 2001-2010. Most employment (and unemployment) in SAR is a national phenomenon. But formal labour markets in SAR – especially in the mining sectors of all SADC economies, highly-skilled professional services (in education, health, law, accounting etc.), in transport and infrastructure, in the tourism industry, the information technology, business support services and financial services sectors, and more generally in high-level management positions across the private sector – have a significant regional dimension. The only SADC economies which are not as yet integrated within a discernible regional manpower pool are the more geographically distant countries of Mauritius (which imports labour from Madagascar and Sri Lanka, and it is beginning to attract high-level professional manpower from South Africa, Zimbabwe, Europe and India) and Tanzania, which is more linked to labour markets in East Africa (particularly Kenya) than in SADC.

Cross-border flows of labour across SAR have been shaped mainly by (i) former policies favouring a tradition of migrant labour in the South African, Namibian and Botswanan mining and industrial sectors; (ii) widely varying per capita income levels across the region, with accompanying (iii) wide compensation differentials for the same types of jobs which encourage legal and illegal (informal sector) migration from low-income economies (such as Lesotho, Malawi, Mozambique, Swaziland and Zambia) to the high-income economies (mainly South Africa and to a lesser extent Botswana) with Zimbabwe on the cusp – attracting manpower from lower-income economies (Malawi, Mozambique and Zambia) and exporting its own to higher-income neighbours (South Africa and Botswana); and (iv) a network of family ties which straddle much of the region.

Regional labour flows, especially of well-qualified high-level manpower (HLM), have been accentuated between 1988-95 by large outward flows of non-African HLM from South Africa to Europe, North America and Australia, and to Botswana. This has created a regional *backdraft* effect, i.e. inducing into South Africa flows of trained manpower from neighbouring countries (especially in the health and education sectors). The result is a serious regional brain drain from the lower-income economies (especially Malawi, Zambia and Zimbabwe) to South Africa and Botswana. Its negative effects on neighbouring countries is being exaggerated by two other factors (i) increasing indigenisation of the South African civil service at national and provincial levels, which is attracting trained Africans from the education and health sectors into government and creating a vacuum which is being filled by inward cross-border flows of HLM; and (ii) increasing resistance to absorption of cross-border flows of unskilled and semi-skilled labour (i.e. low-level manpower – LLM) which is being encouraged to repatriate to countries of origin as South Africa attempts to absorb its own large pool of such labour in productive employment. Regional labour flows are connected with outward and inward flows of remittances which are of critical importance to economies such as Lesotho and Mozambique, and to a lesser extent to economies like Malawi and Zambia, in balancing their external accounts.

Apart from the large number of microeconomic issues which need to be addressed in regional and national labour markets in SAR, there is a major *wage policy* issue emerging in SAR. While inevitably having to be tackled at national level, it has widespread regional implications which must be taken into account. The large pool of surplus LLM in South Africa and SAR, coupled with a large deficit in HLM, would suggest the need for downward pressures on real (productivity adjusted) wage rates to clear the labour market for LLM and relatively high LLM vs. HLM compensation differentials.

Yet real wage rate distortions, with their roots in the apartheid regime's labour policies entrenched by union-supported rigidities set by the mining sector, have driven real wage rates for LLM in South Africa to uncompetitive levels which (i) cannot possibly clear national or regional labour markets and (ii) render South African industry generally uncompetitive by international standards (or compel it to become artificially capital-intensive). They also create incentives for inward labour flows (legal and illegal) of LLM which are now administratively impossible for South Africa to curb or control simply because the administrative machinery to enforce draconian entry-barriers or forced repatriation/deportation programmes has been dismantled. It would be much too costly to reassemble and would probably be subverted by rent-seeking behaviour even if it was.

Consequently a major policy twist has developed in regional real wages through the 1987-95 period in SADC. As a result of unending adjustment and devaluation, real wages have fallen sharply in virtually all the SADC economies outside of SACU where they have risen sharply. Thus, in continental SAR, the gap between real wages in the SACU economies and the other countries, which was already large, has widened considerably over the last decade and has been particularly problematic in the HLM labour market exacerbating brain drain effects.

As the AfDB report (1993) emphasises, the brain drain phenomenon has important policy implications for adjusting countries in SAR. Whereas migrant LLM and HLM and recipient countries may benefit, supplying countries bear the cost of wasted public investment in human capital, reduced quality of public services and a loss of HLM manpower critically needed for their adjustment to be successful. Supplying countries of course benefit from remittances which these HLM outflows generate, but it is questionable whether the benefits (captured largely by private households) are sufficient to offset the costs (borne mainly by the fiscus). Regional real wage differentials then create pressures within national markets to raise wages of HLM thus widening internal wage differentials and reversing the pressure for budgetary savings.

Regional wage twists, as well as supply-demand conditions in national labour markets, have created a serious conflict of interest situation between South Africa and its SADC neighbours. It is clearly in the interests of South Africa to curb inflows of migrant LLM and perhaps even to attempt repatriating the surplus which is now resident, while encouraging the HLM inflows from the rest of SADC which it needs. Neighbouring governments have exactly the opposite interest – i.e. to discourage HLM outflows while encouraging LLM exports. Against these conflicts of interest, South Africa has an obvious stake in promoting economic development and growth throughout SADC to (i) create growing markets for its own output and (ii) prevent the spillover effects of their economic and social dislocations being imported into South Africa. All of this points to a need for a region-wide perspective.

When the potential exists for powerful and disruptive conflicts of interest – on perhaps the most politically sensitive and explosive of issues – among countries in a regional community, the rationale for freeing markets in labour, along with concomitant freeing of markets for goods, services and capital (to avoid other more damaging twists from emerging when one market is freed and others are not) becomes a compelling one. The pay-offs from doing so for all the economies of SADC are obviously high although, as with any adjustment, temporary dislocations and political repercussions are inevitable. Freeing goods and services markets in the region must be accompanied by freeing capital flows within SADC. Otherwise current account imbalances between countries in the region cannot be counterbalanced by compensating capital account transactions (which are privately induced rather than publicly negotiated). If left to the market, free capital account flows would be directed by differentials in relative costs, relative differences in factor productivity and other competitive factors. Obviously some public investment must be directed towards reducing these differentials, but free cross-border capital movements will certainly contribute to a moderation of factor price pressures (in particular wage rates for LLM).

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The South African region at present faces an extraordinary opportunity for doing something more positive about employment generation by combining public and private sector investment initiatives with IFI and donor support. Opportunities for large scale employment generation in SAR can be found in sectors such as construction, infrastructure development, and the expansion of services (especially in transport, finance and tourism) rather than in agriculture, mining and manufacturing. Construction and services provide more typical entry points for upwardly mobile indigenous entrepreneurial start-ups and as a training ground for LLM than do other sectors. Growth in the construction sector also has a backward multiplier effect in requiring increases in the output of domestic basic industries (cement, steel, glass, aluminium, building materials, fabricated structures etc.) which need reviving in SAR.

Happily, as it happens, the region now confronts the challenge of massive land-mine clearance, and country-wide reconstruction and rehabilitation efforts in Angola and Mozambique with the equally daunting task of providing low-cost housing and infrastructure provision on an accelerated basis to the hitherto dispossessed majority in South Africa. These three areas alone – quite apart from similar opportunities which exist, but on a smaller scale, in other SADC countries – provide considerable opportunity for SAR governments, regional and foreign construction firms, donor governments and IFIs to work together in formulating market-friendly strategies which would achieve simultaneously the objectives of increasing LLM incomes, creating demand in low-income groups, alleviating poverty, generating employment, inducing output growth and regional regeneration. Leaving such opportunities for the market alone to develop would be both naïve and short-sighted.

A more holistic cooperative approach to LLM absorption, supported by the proper regional and national adjustment policies, needs to be accompanied by a deliberate, integral strategy for increasing rapidly the supply of indigenous HLM within the region. In an environment where all SAR governments are under pressures to reduce public expenditures that objective can best be achieved by pooling available regional resources (institutional and financial) for human capital development and maximising the efficiency/effectiveness of their use, rather than by pursuing more costly, and probably ineffectual, alternatives for doing so through initiatives confined to national economies.

Labour market and wage policy adjustment in all their various dimensions therefore need to be urgently considered with a regional perspective on the part of SADC governments, the donor community and the IFIs. With its broad but useful analysis of regional labour markets and regional wage policy issues, the AfDB has taken a lead in raising key questions

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which need urgent answering – through the development and re-orientation of regional institutions focusing on labour markets as well as the accompanying adjustments that are required in the structure of SAPs designed for SAR economies.

5. *Trade Policy*

In Africa and the adjusting economies of SAR the impact of SAPs has perhaps been most visible in the area of trade and exchange regime reform. The policies pursued under SAPs have considerably reduced foreign exchange rationing and accompanying import scarcity premia – enabled mainly by expanded donor financing for import support. Progress thus far with trade liberalisation has reversed the distortionary policy excesses of the 1980s but, viewed in a long perspective, has simply restored most adjusting SAR economies to the position they enjoyed before they were overwhelmed by unsustainable imbalances in their external accounts. Moreover, the sustainability of their trade regime reforms is dependent almost entirely on the continuation of extraordinary levels of concessional aid flows.

Sufficient structural adjustment and production structure transformation has not yet taken place in the poorer SADC countries for their own commodity (and other) export earnings to finance simultaneously (i) the minimum levels of imports they require and (ii) their debt service obligations to preferred creditors even after foregoing debt service to other creditors. This is particularly true for Lesotho, Malawi, Mozambique, Tanzania and Zambia and may become increasingly true of Angola in the latter half of the 1990s and beyond, despite its large earnings from oil exports (which account for nearly half of its GNP). Their experience is in line with the World Bank's observation (1990) that poorer and less diversified economies – which face a discouraging combination of institutional weaknesses, relatively undeveloped production structures, and impediments to factor mobility – usually react very slowly to changes in the real exchange rate and tariff structure rationalisation.

The other six more developed and higher-income SADC economies (Botswana, Mauritius, Namibia, South Africa, Swaziland and Zimbabwe) have either achieved, or are capable of achieving, external account balance more easily from commodity exports and services income. The wealthier six of course account for a much larger amount (nearly four-fifths) of the region's total trade than the poorer six, suggesting that the region's external account imbalance taken as a whole can be corrected more easily than might be the case with external balances in the six poorer countries (see Annex Tables 17-18).

The current external tariffs of countries in SAR range from 20-65% with much lower tariffs applied to intermediates and capital goods. A COMESA-induced round of tariff cuts was scheduled for 1995 but, given the desultory performance of implementing previously negotiated tariff cuts in PTA, expectations that the latest round will be implemented quickly would be unrealistic. More significant than tariff inhibitions on intra-SADC trade are non-tariff barriers which include acute foreign exchange shortages throughout the region (except for Botswana and Mauritius); lack of intra-regional currency convertibility outside of SACU and Mauritius; import licensing; lack of trade finance and letter-of-credit facilities; lack of country creditworthiness, which heightens credit and transfer risks; high internal transport costs; border controls characterised by rent-seeking behaviour; adjustment pressures inconducive to expanding intra-regional trade; the dominance of inefficient parastatals in production and marketing activities throughout the region; and an absence of adequate product/market information for supply sources within the region. The dependency of so many SADC countries on aid-funded import support has also reduced opportunities for intra-regional trade by diverting procurement to tied, extra-regional (i.e. donor) sources of import supply even when regional sources would have been more efficient and economical. Moreover, a long legacy of apartheid and sanctions was hardly conducive to the development of properly structured trading arrangements within the region.

Much of the trade liberalisation which took place till 1992 in SAR addressed the progressive withdrawal of import controls through foreign exchange rationing. It did not fully address trade restrictions imposed by tariff and non-tariff barriers such as quantitative restrictions through import licensing. Since then import regimes in SAR have been liberalised further with open general licensing, significant tariff rationalisation with accompanying tariff reduction (before 1993, tariff reduction in SAR through successive PTA rounds of tariff cuts occurred more in rhetoric than reality) and further movement in the direction of current accounts becoming progressively more open. However, imports are still restrained in most SAR economies by tariffs which are high by international standards (in developed economies) but not by developing country standards.

The general picture is one of more happening on the import liberalisation front than on the export promotion and diversification front in SAR. Though the disincentive to exports posed by overvalued currencies has now been largely eliminated in much of the region (except in Angola and Mozambique) exports are still restrained by reduced but residual export licensing; export taxes; inefficient parastatals which continue to monopolise principal export production and marketing; and state-run agricul-

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tural export commodity marketing boards (which are not being phased out quickly enough). The type and sequencing of different types of trade reforms which have been undertaken in Africa and SAR are well documented (World Bank, 1994a, 1995a) and need not be recounted here.

Although attention has been paid in most SAPs to increasing non-traditional exports, not much has been achieved in practice, despite measures such as: duty drawback schemes for imports used in exports; special export-processing zones; relaxation of foreign investment codes and specific government incentives (as well as regulatory streamlining) for non-traditional exporters. Manufactured exports from SAR have not yet diversified or increased sufficiently in response to structural adjustment measures in the same way that they have in Latin America and South Asia (e.g. India's export performance since 1992 has been dramatic with export diversification and growth averaging 25% annually between 1992-95).

This outcome suggests that, outside of South Africa and Zimbabwe, African production structures may still have a long way to go in adjusting properly to the measures taken so far and becoming globally competitive. It is possible that African economies may lack the basic essentials of more established private-enterprise cultures elsewhere. In other regions, these entrepreneurial cultures, even though repressed for a long time, are responding swiftly to the opportunities created by liberalisation and taking advantage of competitiveness created by overdue changes in relative big prices. In Africa they are not.

Outside of SACU, recorded imports are an unreliable guide to actual imports in the non-SACU economies of SAR, as are customs revenue data which are frequently misleading. The same applies to recorded exports. Monetary, fiscal and exchange rate changes have had a dramatic impact on relative prices (in domestic currency) of imports and exports in the adjusting countries and less so in the six middle-income countries of the region. They have made most manufacturing parastatals uncompetitive and subjected them to increased competition from imports. Many have simply become unviable. In the private sector the de-industrialisation impact has been more mixed since many private firms without privileged access to import purchases at overvalued exchange rates had already adjusted to parallel market import prices or gone out of business.

The principal difference between trade reform prescriptions under SAPs in each Southern African country vs. a *regional* trade-focused approach, is that the former aim mainly at achieving unilateral competitiveness vis-à-vis the rest of the world while the latter attempt a two-stage process of achieving regional competitiveness first and having the region as a whole becoming globally competitive later. The 1989 *(Crisis to Growth)* World Bank report acknowledged forcefully the role that regional integration in Africa

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could play in achieving competitiveness through a regional approach which would buy time for *learning effects* to occur. But subsequent IMF/WBG publications (and indeed the contents of SAPs in SAR themselves) seem to take a more purist (trade theoretic) view. They express considerable scepticism about extending customs unions and common external tariffs seeing them as soft options which vitiate the adjustment message rather than reinforcing it. The AfDB (1993) on the other hand throws itself squarely behind the regional integration trade approach, taking a pragmatic rather than a theoretical approach.

Before South Africa joined SADC in 1994, regional trade analysis invariably emphasised the lack of complementarity in member economies and the very low volumes of intra-regional trade that occurred as evidence that there was little to be gained by a regional approach. At that time most trade between (non-SACU) SADCC members and South Africa was clandestine and unrecorded. As observed earlier, with South Africa in the frame, the trade picture within SADC changes dramatically (Maasdorp, 1992; see also Annex Tables 4-7). Although the non-SACU economies in SADC do not trade much with each other (intra-SADC trade excluding South Africa was less than 5% of the total trade of SADC countries), they do trade with Zimbabwe, and in much more significant amounts with South Africa, especially when parallel market trade is factored in.

The trade figures appear dramatically different when one looks at that portion of trade which excludes (i) the region's principal mineral and cash crop commodity exports, which are all directed at world markets although some, e.g. tropical beverages, do go to South Africa; (ii) Angola's oil exports; and (iii) the region's imports of crude oil. The picture is reinforced when one considers the destination of South Africa's manufactured exports, nearly a third of which are directed primarily at SACU, SADC and other African markets (AfDB, 1993). Trade by SADC countries with South Africa has increased from under 17% of their total trade in 1970 to over 23% in 1984 and possibly an estimated 35% in 1994.

On the other hand, of South Africa's total trade, SACU accounted for 10% in 1990 and an estimated 12% in 1994 whereas the rest of SADC accounted for less than 3% in 1990 and perhaps not much more than 5-7% in 1994. These percentages do not take account of the large parallel market trade which occurs within SADC. With the entry of Mauritius into SADC and the dawn of a new political era in April 1994, this proportion (especially if trade in invisibles is included) might be expected to rise significantly.

The AfDB's analysis (1993) of extant intra-regional trade and future trade potential (see especially, Vol. 2, pp. 3-90), demonstrated clearly that there was considerable scope for expanding intra-SADC trade within a

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context of *trade creation and expansion* and minimising *trade diversion*. This could be achieved by (i) shifting some of South Africa's commodity imports from the rest of the world (RoW) to imports from efficient producers within the region; (ii) reciprocally shifting some of the region's imports of manufactures and intermediates from RoW to South Africa, Zimbabwe and Mauritius to the extent possible without trade diversionary effects; and (iii) expanding intra-regional trade in services and invisibles (especially financial, tourism and transport services).

None of these shifts can be induced by fiat but they can be encouraged by market forces acting on better information and new trade linkages. Finally, given the topography and natural resource base of SAR, and as the Lesotho Highlands Water Project symbolises, considerable further potential exists for (iv) significant expansion of intra-regional trade in utilities (electricity, water and telecommunications) which are tradable regionally but not internationally. Such trade would help to balance current account asymmetries since, for these goods, South Africa would be the principal buyer while its regional cohorts to the north would be the main sellers.

Regional trade expansion would be encouraged and made more sustainable if the existing current account imbalances between South Africa and Zimbabwe on the one hand, and the rest of SADC on the other, were counterbalanced by free flows of investment capital in the opposite direction. The potential for converting a hub-and-spoke regional trade nexus in SADC, with South Africa at the centre, into a richer weave involving enhanced trade between all the countries of the region is considerable.

This would be especially true if factor markets were freed, enabling capable firms located in the region to spread their diversified mining, production, commercial farming, infrastructural and financial service capabilities across the region in search of the most favourable environment (taking into account total factor productivity) and locating closer to major consuming markets. That is even more likely to happen if the regional macroeconomic environment is structured so as to reduce exchange, payments, settlements/transfer and credit risks. Greater cost efficiencies are also likely to result under such an approach (Riddell, 1990, 1993; Meier and Steel, 1989; AfDB, 1993; World Bank, 1989).

A regional approach to trade policy – though perhaps theoretically second best – is more practicable, achievable and in the interests of SAR as a whole as well as in the growth and diversification interests of individual member economies. Moreover, since the present SAP trade-regime adjustment paradigm has failed to deliver the goods in SAR, especially in encouraging the rapid diversification and growth of exports, the case is strong for attempting a different approach, along the lines specifically suggested by the AfDB (1993).

6. *Industrial Sector Policy*

Apart from the focus on macroeconomic reforms in its SAPs, the WBG (more than the IMF) extends its adjustment reach into key sectors of African economies with sectoral adjustment programmes (SECAPs) aimed at supporting meso- and micro-policy adjustments to induce sectoral output growth and diversification. These SECAPs have been confined mainly to the industrial, agricultural and energy sectors in which changes in the big prices are likely to make the most difference. Surprisingly, SECAPs have not been focused on transport or other infrastructural sectors (such as telecommunications) except in the context of parastatal rationalisation, restructuring and privatisation.

Also, beyond the financial services sector, in which major adjustment efforts have been supported through specifically designed FINSECALs, no serious efforts have been made to achieve equally important adjustments in key revenue generating and export earning sectors such as tourism and construction; although much attention has been given to sectors such as health and education. But, even in these social sectors, emphasis has been placed on project and sector loans involving improved prioritisation and expenditure-switching rather than on sectoral policy adjustment as such. The conditionality of several SAPs have also often contained requirements for policy reform in the industrial, agricultural and energy sectors. This sub-section focuses on industry while the ones that follow focus on agriculture and energy.

The characteristics of the industrial and manufacturing sectors in SAR are discussed in considerable detail in the AfDB's 1993 report and will not be repeated here. Industry is dominated largely by mining in the region, although the mining sector does not feature prominently in the economies of Lesotho, Malawi, Mauritius and Tanzania.

Mining

Mineral output far exceeds manufacturing output for most of the other economies in SAR and mineral exports are much larger than manufactured exports. There is considerable scope for greater efficiency through rationalisation of mining activity in the region with the possibility of welfare gains being captured by individual countries and by the region at large. In the case of Zambia, the success of its overall adjustment effort depends largely on how effectively its mammoth mining company (ZCCM) which monopolises copper production is eventually transformed – a problem which has eluded a solution for the last thirty years! IFI-supported SAPs in SAR have been concerned with the mining sector primarily in Zambia

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because the interplay between copper production and the rest of the economy has introduced the greatest number of distortions and policy twists in the economy at large. Given the importance and complementarity of mineral production across most of SAR, and its geostrategic importance to the rest of the world, it would be remiss to avoid focusing on the key regional issues which the mining sector raises and to suggest the benefits of a regional instead of nationally focused approach to making the obvious policy adjustments required in that industrial sub-sector.

National adjustment policies for the mining sector across SAR are broadly similar and preoccupied with the same issues: encouraging further exploration; attracting the investment interest of regional and international mining conglomerates; increasing the extent of domestic mineral beneficiation value-added throughout the region, with the concomitant reduction of the region's raw ore exports; the exploitation of further forward integration in mining-related manufacturing, e.g. the development of a regional jewellery manufacturing industry which, surprisingly, does not exist to any significant extent; and phasing out the role of parastatals in dominating mineral production in SADC countries outside of SACU with a concomitant increase in private sector involvement/investment.

The key questions of regional importance concern the structure of ownership and its excessive concentration among six inter-related and collusive South African mining conglomerates whose complex cross-shareholding structures are opaque and appear threatening to SAR governments; competition and regulation in the mining sector in SAR; the introduction of new and improved mining technology for exploration, mineral production and beneficiation; the role of the state vis-à-vis mining conglomerates with massive resources and countervailing power in maximising overall economic (and not simply private financial) gains from the exploitation of the region's mineral resources; further regional cooperation in mineral marketing arrangements; the issue of regional migrant workers in mines across the region; and the real wage policy distortions caused by wage price setting by the mining sector. None of these problems has been adequately addressed by the IFIs or the international community on a region-wide basis as key issues for adjustment despite their critical importance for the future of most SAR economies.

The future development of the mining sector in SAR is dependent on constraints and parameters which have major regional dimensions and can be best tackled at the regional level. Apart from SADC as a whole being affected by terms of trade shocks transmitted through the volatility of mineral prices and global demand fluctuations, these include an inadequate regional network of surface transport infrastructure outside of South

Africa; obstacles imposed by the close involvement of the public bureaucracy and endemic corruption associated with mineral rights and mineral production; vulnerability to frequent regional droughts which have an immediate impact on power and water availability for the mining sector.

These factors combine to discourage rational regional exploration and reserves accretion activities; slow down extraction of proven reserves in ways that do not capture fully the opportunities offered by occasionally favourable price movements; and discourage large-scale long-term private investment in downstream beneficiation and forward integration. They also result in cross-border spillover effects with constraints on mining production in one country influencing patterns of production in its contiguous neighbours.

Post-1994 political and economic developments in SAR raise the question of whether the time has come to consider harmonising (or even eventually replacing) disparate nationally based mining codes, legislation, regulatory practices and mining investment incentive structures within a regionally consistent framework. The AfDB (1993) study has examined this issue in depth and concluded that, while having obvious benefits in attracting rational inward flows of foreign investment in the SAR mining sector, there are major risks involved in moving too fast and prematurely on this front given (i) the uncertainties of present political dispensations and the nascence of regional cohesion in a SADC framework which now includes South Africa; and (ii) differences in the types of minerals produced, mineral potential, the extent to which factors outside the mining sector constrain exploration, production and development, and in the scale of mining operations across different SAR countries.

The AfDB argues for gradual movement towards a regional mining regime and regulatory framework as more experience is gained and after structural changes have occurred which would make the development and management of such a framework more politically acceptable and economically efficient. The AfDB does suggest immediate regional actions aimed at developing the capacity for research and development, and information and technology sharing, through a regional mining technology centre and regional mining commission.

In short, the analysis undertaken by the AfDB strongly suggests the advantages of (i) capturing significantly higher economic gains by adopting a regional perspective to the future development of the region's mineral resources, and (ii) exploiting more effectively the linkages between the SAR's mining potential and the development of a connected downstream manufacturing base by adopting a regional approach. It needs to be incorporated into the debate on structural adjustment in the region and taken up more effectively by the IFIs.

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Manufacturing

Total manufacturing value added in SAR in 1994 was over $33 billion with South Africa accounting for 82% of that amount. Manufactured exports of the region were about $8 billion with South Africa, Mauritius and Zimbabwe accounting for 95% of those. Nowhere are the development disparities among SADC economies reflected more starkly than in their manufacturing sectors. South Africa, Zimbabwe and Mauritius are relatively highly industrialised, as (but to a much lesser extent) is Zambia. Of these four only Mauritius has achieved a degree of sector-specific international competitiveness while South Africa dominates overwhelmingly in being the region's industrial engine and principal exporter of manufactures to the rest of the region. Angola, Mozambique and Tanzania have antiquated industrial sectors in a state of severe disrepair and in need of major overhaul. The smaller SACU economies (BLNS) and Malawi characteristically have small consumer-oriented industries (food processing and brewing) dominated by local product processing.

Industrial development in the region outside of the PWV-Harare corridor is constrained by geography, high transport costs, the minuscule size of most national markets and a chronic shortage of the appropriate skills and technology. SAR (including South Africa) is severely handicapped by a deficit of human capital specialised in engineering, science, business support skills and the vocationally honed technician/artisan skills needed for industrial widening and deepening commensurate with the needs of the region.

Outside Mauritius, industrial and manufacturing growth in SAR has been (and continues to be) dominated by protected import-substituting production for national domestic markets behind high tariff walls and a range of non-tariff barriers. It has been dependent on relatively weak and stagnant domestic demand with duplicative production structures built up in every SAR economy concentrating mainly on foodstuffs, clothing and textiles.

The industrial sector has been the focus of SAPs and SECALs in Africa and SAR (specifically in Malawi, Tanzania, Zimbabwe, and indirectly, Zambia) perhaps because industrialisation has invariably been viewed as being synonymous with development. However, attempts to promote industrialisation efforts (especially the inefficient, highly-protected import-substituting, parastatal-dominated kind) have been a major cause of resource misuse and dissipation, of burgeoning fiscal deficits, and of the overall internal macroeconomic imbalances which African countries experienced through the 1980s and early 1990s.

Industrial sector policy reform under SECAPs was aimed at being achieved largely through macroeconomic policy changes. Monetary, fiscal, trade and exchange rate reforms were intended to improve competitiveness in tradables. Industries producing tradable goods, and capable of responding to these changes, were supposed to have benefited. But the examples of firms doing so in SAR and Africa were few. By and large the combination of macroeconomic reforms in SAR generally worked toward making most parastatals (which dominate industry) unviable. Cuts in public expenditure affected industrial parastatals in two ways: they resulted in a sharp, sudden fall in domestic demand for their products, and in an absence of financing for new capital investment and for covering operating losses. Accompanying monetary squeezes usually resulted in severe constraints on working capital, which reduced capacity utilisation and added to plant inefficiency. Loss of privileged access to cheap foreign exchange (because of exchange rate reform) and increasing competition from imports (because of trade liberalisation), at the same time, also affected industrial parastatals in SAR adversely compounding their operating problems and pushing many of them over the brink before they had any time to restructure or adjust.

Surprisingly, most industrial sector adjustment loans (ISECALs) which were supposed to focus on industrial sector issues and sub-sectoral restructuring, actually focused on prescribing reforms in trade policy (Jayarajah and Branson, 1995). The aim of nationally focused ISECALs in SAR was to (i) remove biases against manufactured exports by removing export taxes, introducing duty-drawbacks on imported inputs, providing export subsidies, and creating special export processing zones; (ii) introduce efficiency-inducing competition mainly through import liberalisation rather than by expanding domestic competition; and (iii) increase responsiveness to changes in real relative prices and to the removal of other distortions (such as non-tariff barriers and quota restrictions) on the part of domestic manufacturers that trade and exchange regime adjustment is supposed to achieve.

In contrast to their preoccupation with trade policy reforms, ISECALs paid scant attention to other policy distortions which fostered sectoral inefficiency such as: price controls and wage rigidities, excessively onerous and irrelevant regulatory requirements, industrial licensing to control capacity expansion and competition, distorted pricing of publicly produced non-tradable inputs, restrictions on entry and exit, and restrictions on foreign direct investment (Jayarajah and Branson, 1995). Left unattended, these types of policy distortions continued to (i) constrain the efficiency with which resources were allocated when relative prices changed – thus inhibiting domestic efficiency and structural adjustment gains from materialising and limiting the gains that did accrue to increases in consumer welfare from expanded choice with the increased availability of imports; (ii)

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exacerbate the domestic costs of adjustment caused by higher domestic price levels; (iii) perpetuate resource misallocation throughout the industrial sector with knock-on effects for the economy at large; and (iv) deprive adjusting economies of benefiting from external sources of technology upgrading and improved production, quality control and industrial management techniques.

Judging the performance of intended reforms in the industrial sector by their visible results in SAR leads to disheartening conclusions (see Annex Table 19). Theoretically, success should be gauged in terms of ensuing productivity growth rates, the efficiency of intra-sectoral and intersectoral resource allocation, exploiting dynamic comparative advantage more fully, and shaping an efficient, competitive industrial sector (and its component sub-sectors) commensurate with the size and structure of the overall economy. Apart from the problem of poor data availability, which precludes definitive judgements from being made, existing evidence suggests that ISECALs in SAR have not achieved these intended objectives to any discernible degree.

Looking at crude figures of growth in industrial and manufacturing value added, or at the growth and diversification in manufacturing output and exports, or at the extent of internal restructuring and sub-sectoral balancing which has taken place so far, it is difficult to claim any obvious success with industrial sector reforms at the national level in SAR. What is visible in Malawi, Tanzania and Zambia is stagnation in industrial/manufacturing output and exports, relatively little diversification and a considerable amount of dislocation and de-industrialisation without the resultant emergence of a new, more dynamic and efficient industrial sector in adjusting SAR countries anywhere in the offing. The question is whether these signs reflect sectors, which are at the low point of the adjustment cycle, about to spring back with renewed dynamism and vigour, or whether the signs indicate progressive, and not easily reversible, de-industrialisation.

There are clearly some signs of promise in Zimbabwe which has a relatively efficient, resilient and robust manufacturing sector. In Zimbabwe, private manufacturing investment is rising, foreign direct investment is interested in expanding, manufactured exports showed strong growth (except when affected by power shortages caused by the 1992 drought), and some overdue restructuring and modernisation is taking place in the privately owned part of the industrial sector. Even so, much remains to be done in restructuring the parastatals which dominate the industrial sector.

Moreover, as mentioned earlier in the paper, the industrial sectors of other SADC economies are in for another adjustment shock when industry in South Africa undergoes the sectoral changes (in addition to the macroeconomic changes) which are necessary for that economy to achieve international competitiveness; an objective to which the present South African government is apparently committed but not fully aware of the transitional costs involved nor of the political repercussions which may ensue, especially in terms of labour union resistance.

Part of the reason for an absence of the right supply response in the industrial sectors of individual SAR economies is that while public enterprise activity in the industrial sector is winding down – more as a result of fiscal constraints than a deep seated conviction about the inherent efficiency of such enterprises – there is little visible sign of new and more efficient investment and restructuring being undertaken by the private sector in SAR outside of South Africa, Zimbabwe and Mauritius. In these, and even more so in the other, SADC economies excessive reliance on the market alone for allocating resources efficiently is likely to be misplaced. Market-determined allocation of resources in the industrial sector at the national level may prove sub-optimal because of (i) inadequately functioning product and factor markets at that level; and (ii) chronic deficits in essential public goods in the form of adequate infrastructure and other essential frameworks to support industrial enterprise (legal and regulatory frameworks and properly functioning legal, accounting and other business support services).

Also, in the industrial sector, non-appropriable *dynamic* gains arise from learning effects, tapping a wider pool of HLM skills than is available in small national markets; technology sharing and development; and experience with exporting activities (Mistry, 1995). In such circumstances market allocation of resources in a static efficiency framework can and does lead to sub-optimal long run allocation of resources. With these caveats in mind, and given its characteristics and size, it is increasingly clear that manufacturing industry in SADC will have to develop with *regional* considerations in mind if it is to achieve five critical objectives: (i) maximising output growth; (ii) raising manufacturing value added through increased beneficiation of the region's mineral and agricultural products; (iii) diversifying and increasing manufacturing exports; (iv) increasing labour intensity in the manufacturing sector; and (v) increasing efficiency and total factor productivity to levels which permit regional and international competitiveness to be achieved in that order.

That nationally oriented SAPs and industrial SECALs do not incorporate regional dimensions in their design is a serious shortcoming in need of urgent rectification. The World Bank (1989), explicitly acknowledges the importance of sub-regional markets in Africa as stepping stones to achieving international competitiveness and in the development of viable intermediate and capital goods industries. Yet its SAPs and ISECALs fail to address that fundamental issue in an operationally meaningful manner.

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The major problem with the *laissez faire* SAP paradigm for the industrial sector in SAR is that, for the reasons provided above, it will result in manufacturing concentration being entrenched in the industrially endowed economies with the risk of progressive de-industrialisation in the others. The existence of considerable excess capacity in the same low-technology, consumer-goods industries across SAR will compel governments pursuing trade liberalisation policies to make unpalatable choices from three options: (a) allowing firms which are unable to compete regionally to shut down; (b) scrapping plans to restructure, privatise and rehabilitate temporarily moribund enterprises; or (c) revert to protective trade regimes with high tariff walls because of their inability to face the immediate political repercussions of doing otherwise (AfDB, 1993). For that reason an approach to industrialisation in SAR, whether national or regional, which ignores these difficulties at the national level, will be politically and economically unsustainable and will create problematic intra-regional conflicts which will be difficult to resolve.

To exit from the *cul de sac* that national industrialisation strategies and adjustment programmes have led to in SAR, some form of regional industrial policy, accompanied by appropriate compensatory offsets, or industrial relocation subsidies, may be essential in the initial stages of re-industrialisation to achieve a more pragmatic, if theoretically inferior, regional industrial balance. An immediate extension of the SACU framework to embrace all of SADC may seem tempting, superficially, as a quick-fix; but it would lead to emphasising the very problems that the BLNS countries face with their own industrialisation in the face of overwhelming South African advantage.

Too quick an opening of the region to the full force of industrial competition from South Africa could frustrate the industrialisation aspirations of other SADC economies and even delay necessary adjustment in South Africa itself. Intra-regional opening of national industrial sectors may therefore need to incorporate a system of two-tiered preferences (a higher initial barrier to imports from the rest of the world and a lower barrier to those from South Africa with both barriers being lowered progressively and automatically in a pre-announced time-bound manner) which give industries in all SADC economies time to adjust before completely free intra-regional trade can be achieved behind a moderate common external tariff.

To achieve progress along these lines the AfDB (1993) suggests two options for further study by SADC governments before their opting for either:

(1) *A delayed free market option* which involves lowering national tariff and non-tariff barriers and progressively within a framework of mutual

regional reductions, giving affected industries enough time to adjust to market discipline and become competitive, or to close down. Such a time-bound option would allow for cross-regional rationalisation and restructuring to occur through mergers, acquisitions, divestitures, privatisations and closures.

(2) *A regional integration option* which would combine the delayed free-market approach with incentives to effect more orderly rationalisation of industrial structures on a regional basis, guided mainly by efficiency criteria but sensitive to the need for regional equity and balance.

These options are discussed at length in the AfDB's study (1993, Volume 2, pp. 239-318) which takes a different view to regional industrialisation from the IFIs – as reflected in their SAPs and SECALs – and will not be elaborated upon further here.

7. *Agriculture Sector Policy*

Agriculture accounts for 35% of Africa's GDP, 40% of its exports and 70% of its total employment.[12] But, African farmers have been burdened with disincentives in the form of the highest effective rates of (explicit and implicit) agricultural taxation in the world[13] leading to falling agricultural output. It is hardly surprising then that agriculture was targeted for sectoral adjustment and policy reform. In SAR, such reforms were attempted through WBG-financed SAPs in all adjusting countries and through specific ASECALs in Malawi, Mozambique, Tanzania and Zambia. They were aimed primarily at reducing the overall tax burdens on farmers, raising agricultural production and encouraging crop diversification by: improving real producer prices; removing the implicit taxation burden of an overval-

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12 The equivalent proportions for SAR as a whole are quite different, with agriculture accounting for under 10% of regional GDP, 20% of SAR exports and about 50% of total employment. However, these figures are distorted by the mining economies of South Africa and Botswana (where agriculture accounts for less than 5% of GDP but still accounts for over 50% of total employment) and the industrial economy of Mauritius (where agriculture accounts for less than 10% of GDP but about 30% of employment). Excluding those economies, the ratios of agricultural production and employment of the other nine SADC countries approximate the averages for Africa as a whole, with the share of agriculture in GDP ranging from a low of 13% for Angola (for unusual and specific reasons involving war and the relatively large size of its oil production and refining sector) to a high of 61% for Mozambique and Tanzania.

13 The explicit tax burdens were manifested in the form of producer-price controls, export taxes, and high input prices and taxes. Implicit taxes resulted from overvalued exchange rates, inefficiencies in state marketing boards, and high levels of domestic industrial protection which raised consumer prices on farm inputs and wage goods with input subsidies going only a small distance towards offsetting them (World Bank, 1994a).

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ued exchange rate for export crops; lowering explicit export taxes; reducing marketing costs and improving domestic marketing arrangements, especially for export crops; improving the efficiency of input and credit distribution; while removing input (e.g. fertiliser and water) subsidies for fiscal reasons in ways that would still leave farmers with higher net incomes taking into account the effect of all the other measures.

Just as ISECALs focused more on *trade policy* reforms than on meso-policies affecting the industrial sector, most ASECALs attempted to focus on *fiscal and exchange rate policies* rather than on meso- and micro-policies affecting the agricultural sector as such. In Tanzania, the ASECAL actually attempted to substitute for a SAL (Jayarajah and Branson, 1995) when negotiations for a SAP failed. In such instances it became difficult to distinguish between the macro-reform objectives of SAPs and the specific sectoral reform objectives of ASECAPs. This usually resulted in fiscal reforms being emphasised in a way that was unbalanced; often leading to conflicts between prescriptions at the macro and meso levels (Jayarajah and Branson, 1995), especially when it came to the budgetary effects of reductions in export taxes, or conversely when reductions in fertiliser subsidies were programmed at a rate which was sectorally (and politically) unachievable.

In promoting agricultural exports from adjusting countries, IMF/WBG-SAPs and WBG-ASECALs have been criticised for indulging in fallacies of aggregation by compelling neighbouring countries in Africa to expand export production of the same crops to their singular and collective detriment (e.g. cocoa from Ghana and Côte d'Ivoire, coffee and tea from Kenya, Tanzania, Uganda, Malawi, Madagascar and Zimbabwe, tobacco from Malawi and Zimbabwe, sisal and cashews from Tanzania and Mozambique, etc.). Such compulsions[14] exercised simultaneously in Latin America, the Caribbean and Asia as well as in Africa, often resulted in expanded supplies of tropical beverages and other export crops on world markets at a time when world demand for these crops was stagnant or

14 IFI-induced emphasis on increasing traditional (agricultural and mineral) exports in Africa and elsewhere has much to do with (i) their implicit bias towards maximising external debt servicing capacity on the part of adjusting countries (resulting in the immediate benefits of adjustment being exported rather than internalised) as it has with (ii) growing convictions among IFIs and the donor community (which have rapidly turned into yet another new neoclassical ideology) about the need to make developing economies more open and capable of earning their own way in a world – i.e. financing their import needs from export earnings rather than from over-reliance on aid or external borrowings – in which the market paradigm has taken almost universal hold. The consequence of such emphasis has often been the opposite of what was intended, at least in terms of short-run effects as the early debacles with first-generation adjustment programmes of 1982-85 vintage have clearly suggested.

declining. The result has been increased volatily and a declining trend in the world prices of these commodities, relieved or reversed temporarily only by occasional crop failures in particular countries (e.g. coffee frosts in Brazil).

This problem – clearly one with major regional implications in SADC given the commonality of agricultural output in its member countries – has become familiar in the literature as the *adding up problem.* In some cases it is serious (World Bank, 1994a; Schiff, 1994; Akiyama and Larson, 1994). It is particularly acute for countries with large world market shares in particular commodities. In theory, the remedies are export diversification and, paradoxically, the imposition of export taxes (which are aimed at eliminating high-cost producers from the market thus lowering relatively cost-efficient output to levels that markets can sustain without major price effects), although such taxes have been problematic in Africa with the WBG generally arguing for their reduction and elimination. In practice, these remedies are not easy to implement.

Though there can be little disagreement that the reform of policies applying to agriculture in Africa and SAR was long overdue, actual experience with agricultural reform has been mixed if not disappointing (Jayarajah and Branson, 1995). In SAR, droughts between 1985-1995 dampened the output response of the agricultural sector for food crops, export crops and other domestically produced agricultural products (especially in 1992-93; see Annex Table 20). Another problem was that between 1985-94 world prices for some of SAR's agricultural exports fell, making it difficult to improve real prices for producers even with large exchange rate adjustments, export tax reduction, reduced marketing costs and the easing of credit and input constraints. Although most adjusting SAR countries reduced the overall tax burden on agriculture they did not, except for Malawi, manage to reduce both implicit and explicit taxation at the same time. Where massive devaluations (Tanzania and Zambia) reduced implicit taxation, part of the domestic price gain was recaptured by the fiscus through export taxes.

Unsubsidised fertiliser prices are much higher in SAR countries than elsewhere because of small procurement lots, inefficient parastatal marketing and distribution with substantial leakages, and very high shipping, handling and domestic transport costs. For that reason, and to encourage greater use of fertilisers, subsidies have traditionally been very high and had become a major drain on the fiscus, being a government hand-out with considerable political appeal. Efforts with fertiliser subsidy reduction (politically very unpopular) have proven slow and only partially successful. Some countries believe that removing subsidies would discourage fertiliser use and cause yields to drop. For a variety of reasons, mainly political, most

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countries in SADC still maintain these subsidies, albeit at a lower level than before SAPs were implemented. In Tanzania, subsidies have been reduced from 80% of the farmgate price in 1989 to 40% in 1993 without any evidence that fertiliser use has fallen. Malawi's target of eliminating the fertiliser subsidy (30% of farmgate price) by 1989 was initially successful but was aborted when kwacha devaluation induced sudden, large price increases in transport and fertiliser import costs.

Maize production is a particularly critical region-wide problem in SAR. Although SADC has the potential to be in a large surplus position, it is actually in chronic maize deficit. Reforms to increase domestic maize production in SAR have focused on moving domestic producer prices closer to border prices; announcing attractive administered prices before planting commences; expediting payments to farmers; relaxing controls of maize movements across SAR borders; and restructuring or privatising maize marketing parastatals. Some of these reforms have taken hold and had a positive impact which has not been fully reflected in sustained output gains because of droughts. But it remains difficult to inject private entrepreneurship into maize marketing and, concomitantly, diminish the role of parastatal maize marketing companies into becoming buyers of last resort and holders of emergency grain buffer stocks. A *regional approach* to the issue of agricultural reforms affecting maize production would yield results far superior to measures being taken at the national level and has major structural implications for patterns of agricultural production in SAR.

Despite more than a decade of structural adjustments in agriculture at the national level, most SAR countries (other than South Africa) are still producing well below their agricultural potential with no clear indication that policy reforms have triggered decisive, sustainable increases in either agricultural output or exports. The weak supply and diversification response of the agricultural sector to adjustment measures is generally attributed to continuing macroeconomic imbalances and policy distortions leading to continuing agricultural pricing distortions; inefficient marketing arrangements which are not being corrected speedily enough; excessive vulnerability to weather patterns; sudden shifts in terms-of-trade; and the generally long lag with which agricultural output responds to policy reforms – raising the question of whether it is too early to judge the success of the reforms undertaken (Jaeger, 1992).

Agricultural market liberalisation will not, by itself, secure the sustained annual increases of annual agricultural output and exports that are required to achieve both food security and long-term external account viability. What SAPs and ASECALs in SAR have failed to address is a more fundamental structural issue concerning agricultural patterns of food production in SAR. This was brought to the fore by the AfDB's (1993) report and can only be addressed properly at the regional level. Anomalous though it is, SAR has agricultural production patterns which go against the grain of climatic logic. The largest amount of grain production in SAR takes place in areas which are agro-climatically unsuitable and economically inefficient. The large *real* costs of such production are being obscured by input subsidies (especially for water and electricity) being provided to wealthy non-African commercial and corporate farmers in South Africa to encourage maize production. These policies and patterns were established some time ago and entrenched by apartheid. They involve biases and subsidies which are neither fiscally affordable nor politically sustainable over the long term, especially as other fiscal and political priorities which have not received any weight before (largely because they involved expenditures on the majority native communities) begin to assert themselves under a new political nexus.

Food production in SADC countries (excluding South Africa) between 1965-95 has grown at an average of just over 1% annually in the face of a population growing at around 3.5% annually. By contrast, in South Africa, food production grew by 3-4% annually with exportable surpluses of food being available throughout the 1970s to the early 1990s (albeit at the expense of deliberate deprivation in the larger but dispossessed part of the domestic market). Since 1980, however, there has been a steady decline in the value of food crops produced by South Africa, compensated by increases in higher value output of horticultural, poultry and cattle production. With the progressive phasing out of subsidies for maize production and fertiliser inputs, cereal production in South Africa will decline further and its exportable surplus will diminish to the point of disappearing. By the turn of the century South Africa will probably become a net cereal importer dependent on either regional or (more expensive) extra-regional imports of grain.

For the region to achieve and retain food self-sufficiency, the production of maize and other cereals must shift from the irrigated, semi-arid areas of the South African *veldt* to higher potential rain-fed areas further north in Angola, Zambia, northern Zimbabwe, Malawi, northern Mozambique and southern Tanzania, where regular rainfall is higher (despite droughts) as is soil fertility and water retention capacity. Moreover, the ownership of land in the low rainfall of areas of South Africa and Zimbabwe (with pressures on cultivable land being exacerbated by animal herds and relentless population growth) is grossly skewed in favour of minority white and commercial farmers. The much larger numbers of poorer indigenous farmers (confined in South Africa largely to the former homelands) have been displaced to marginal and much smaller land areas –

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a pattern which cannot remain undisturbed as recent upheavals in Zimbabwe suggest.

On the other hand, to feed the region's burgeoning population, about 20 million hectares of new land will need to come under cultivation for maize alone (AfDB, 1993) – an increase of about 60% in the total amount of land presently under cultivation in SAR. Given limitations on cultivable land in South Africa, most of the increase in cereal production will need to come from cultivation of new land opened up in the northern part of the region and from substantially improved agricultural productivity (i.e. yields per hectare) if the region is to become food secure.

A regional rather than a national approach to this critical strategic challenge faced by SADC would permit the settlement of new land areas in a manner which reconciled meeting the food requirements of the region with the imperatives of addressing thorny and urgent land reform and redistribution problems in South Africa and Zimbabwe. At the same time, yields need to be improved, while aggregate output and agricultural exports with progressively higher value need to be increased. If long overdue land reform is to be achieved in SAR it must be managed in a way which does not compromise medium-term prospects for: achieving food security; expanding output to meet the needs of a growing population; increasing basic nutritional levels; and expanding agricultural exports from all SAR countries and not South Africa alone.

The expansion of production in the more northerly areas of SAR, where available arable land is barely being utilised, will require the prior provision of infrastructure (especially roads and water supply) with development plans being made for mixed settlement of small and large farms and for maintaining an environmentally appropriate ratio of farmland to woodland. Markets by themselves cannot possibly develop or clear the amount of land which needs to be transferred to address the size of the problem the region faces. Land transfers through markets will need to be augmented by regionally managed transfers of a reasonable size.

Regionally organised and financed infrastructure development in the new land areas, coupled with appropriately designed *land swap* arrangements are necessary to enable minority and large commercial farmers from South Africa and Zimbabwe (who are more regionally mobile and whose relocation would not necessitate major transmigration and resettlement programmes) to sell their existing holdings in these two countries and purchase more productive land further north. Zambia and Mozambique have already taken steps to attract commercial farmers from South Africa and Zimbabwe. The time is ripe for SADC to develop a *regional* land utilisation programme which would facilitate land reform while increasing food and export production. In the process, the skills of minority farmers in SAR

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will have to be redeployed since these constitute a scarce and precious regional asset which should not be dispensed with or treated lightly in an area short of food and human capital.

Establishing a regional land bureau might be contemplated to map out and monitor usable land reserves (without imbalancing the fragile ecology of these areas) in SAR countries; help to intermediate land swaps between countries at the first cut, and between private parties at the second; undertake development of infrastructure on new land; and facilitate a smooth transition from a politically and socially untenable land ownership regime to one which is more equitable, corrects previous injustices and absorbs the rural population in a productive manner. Such an institution might be complemented with a regional initiative which pulled together under one SADC umbrella the cooperative work being undertaken on agricultural research, extension services, and farmer training programmes aimed at raising agricultural productivity in the region as a whole.

The regional imperatives of cultivation are no more impelling than are the regional imperatives of forestry where there are equally strong arguments for regional aspects of policy reform and adjustment to be given more play, but to which IFI-supported SAPs and ASECALs have not paid much attention. There is recognised interdependence between the extent of tree cover and the incidence of rainfall in the region. Expanding cultivated land areas will have major implications on wildlife herd movement and on existing systems of agriculture. Moreover, demand for wood (much of which is presently being pre-empted to meet basic energy needs in rural areas) for industrial use to support the region's growth will continue to increase; a reasonable proportion of it will need to be regionally met. Equally, a regional perspective on fishery resources exploitation, especially where inland fish sources are concerned, is a *sine qua non* because the key sources are the natural and man-made lakes of the region which constitute several borders and in which the conservation of fish stocks are regional rather than national concerns.

Obviously, continuing adjustments in South Africa's agricultural sector, with reduction of subsidies and a shift in emphasis from commercial to small indigenous farmers, will have consequences for regional agriculture as a whole. The entry of South Africa into the regional agricultural equation could result in major benefits if regional receptivity to the skills, research knowledge and technology it has can be developed to capitalise on them. At the same time, South Africa's food security, which has been a goal attained at considerable national expense and high opportunity costs under a different political climate, will depend increasingly upon regional performance and initiative.

As the foregoing paragraphs have suggested, the main regional dimen-

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sions of agricultural transformation have till now been largely ignored in national SAPs and ASECALs (even where key regional issues such as maize are concerned). They are likely to become much more prominent as the rest of the decade unfolds and a different appreciation of interdependencies across countries in agriculture and the connected areas of natural resource management and efficient land utilisation, begins to permeate the thinking of SADC governments. Such a trend needs to be reinforced, rather than ignored or vitiated. Present national policy reform agendas focus too narrowly on *intra*-border adjustments and changes at a time when attention on managing issues of land and water in SAR should be shifting toward better understanding of *inter*-border adjustments and changes.

8. Energy Sector Policy

Africa and SAR are characterised by inadequate and unreliable supplies of power and energy which compromise their growth, development and adjustment prospects in pervasive ways. Excessive dependence on domestic fuelwood used by a rapidly growing population is leading to major problems with deforestation and denudation with its consequent implications for rainfall, cultivation and wildlife. At the same, time energy shortages at points of consumption and the unreliability of electricity supplies in most SAR countries are inhibiting industrialisation. Yet, neither Africa as a continent nor SAR as a region are short of natural resources, because the different forms of energy needed for targeted economic growth rates in SAR represent only a fraction of the known oil, gas, coal, hydro and geothermal resources available (World Bank, 1989). Moreover, increasing use of renewables (wind, solar, biomass and mini-hydro) – with the latest technologies in these sources of power-generation having improved far more than is generally appreciated – would stretch SAR's energy resources even further than has presently been estimated.

The gap between energy potential and energy reality in SAR is explained by (i) poor policies which have consistently underpriced energy sources and in particular electricity supply; (ii) an unequal distribution of energy resource endowments among individual countries which virtually disappear in their importance when a *regional* perspective is taken with SAR being an energy surplus region for almost all sources of energy, except perhaps woodfuel; especially if the hydro-potential of southern Zaïre bordering on Angola and Zambia is factored in; (iii) physical barriers which pose technological challenges, e.g. immense transmission distances for power and gas; (iv) fragmented and limited consumer market sizes which impose limits on the development of economic power supply; (iv)

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over-investment in duplicative facilities such as too many uneconomically sized electricity generating plants and too many oil refineries with countries determined to be self-sufficient and energy secure; (v) procurement of crude oil in uneconomically small quantities by individual countries; (vi) poorly planned energy infrastructure with imbalanced investment in generation and too little in distribution leading to low capacity utilisation and high maintenance costs; and (vi) growing environmental constraints to energy use which have regional implications.

More than 95% of Africa's coal deposits (of over 135 billion tonnes) are located in SAR (Botswana, Mozambique, South Africa, Swaziland Tanzania and Zimbabwe), although, apart from South Africa, these deposits are largely undeveloped for energy generation due to lack of capital, trained labour, negligible domestic market demand and very high transport and transmission costs and losses. Immense hydropotential (over 70 GW) in the region remains undeveloped because of the absence of proper regional grid connections or management, and the lack of cooperation across countries in trading electricity. The last unfortunate reality results in under 10% of electricity generated in SAR being traded across borders.

Apart from ESKOM in South Africa, national (parastatal) power utilities are much too small and cannot provide the economies of scale needed to develop viable hydro-projects of the kind that a regional market could easily support, or invest in the costly infrastructure needed for gas use. Yet, because they are public rather than private enterprises they have not been active in seeking ways of achieving market efficiency being more responsive to political signals rather than commercial imperatives. Power transmission losses are high because of both the inevitable resistance losses over long distances and extensive pilferage. Most of the utilities in SAR (outside Botswana, South Africa and Zimbabwe) are overstaffed and overindebted with large scale arrears and inadequate tariffs or revenues to finance ongoing operations, let alone regular maintenance and capital investment.

The urgency of energy sector reform in SAR has been acknowledged with SAPs for adjusting countries in the region incorporating conditionality on energy pricing, and on energy investment rationalisation and restructuring. But there have been no energy sectoral adjustment loans (ESECALs) in SAR as in other parts of Africa and the developing world. The emphasis on reforms in the energy sector through SAPs in different SADC countries have again been *nationally* focused based on their energy intensity; share of imported fuels in energy production; distortions in energy pricing; and the size of public investment in the energy sector. Despite what should have been the sobering impact of three oil shocks between 1973-85, the general picture in SAR in the mid-1980s was one of distorted price structures encouraging uneconomic fuel substitutions and poor utili-

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sation of capacity. Pricing policies – with prices well below long-run marginal resource costs – induced suboptimal development of domestic energy resources and subsidised uneconomic levels of energy consumption. Consumer price subsidies were unaffordable and enlarged the fiscal deficit. Moreover, skewed electricity tariff structures resulted in large supply-demand inefficiencies with the largest subsidies being transferred to the costliest consumers.

The reforms incorporated in SAPs were aimed at improving allocative efficiency and restructuring the energy sector so that its operating and investment costs would be met through internal cash generation based on cost-recovery based tariffs and revenues. Emphasis was placed on deregulation of the energy sector, enhanced scope for private sector ownership and participation, elimination of distortions in energy trading regimes, and in fiscal and financial incentives for energy production and consumption and, finally, on extricating governments from an ownership role and emphasising their role as system and market regulators. But, surprisingly, virtually no attention has been paid in SAPs to the arguments that the World Bank itself had made in 1989 on the critical importance of market enlargement and coordinated investment through regional cooperation.

The history of conflict in the region, with military action often being aimed at energy source targets, has made the goal of energy self-sufficiency a national obsession in SAR. Few governments seem able to accept that continuing with such a strategy in new (and, hopefully, very different) circumstances might result in energy *insecurity* because of the affordability constraint. As the region becomes a zone of peace, SADC countries should become more aware that security of supply at the national level may actually be enhanced, rather than diminished through regional cooperation in electricity generation and transmission.

Intra-regional exports from the northern SAR countries to South Africa after the turn of the present century, when South Africa's excess generating capacity will have been fully absorbed, would provide an important source of earnings for countries who are in chronic trade deficit with South Africa. In addition, a regionally connected power grid with open pooling, wheeling and trading arrangements across borders would reduce electricity costs in most national markets in SAR. It would improve supply reliability and frequency stability, reduce the incidence of frequent and long power outages, and reduce the need for high-pinning reserve requirements and costly investments in extra generating capacity to meet seasonal and peak loads. These savings would translate into large economic gains with SADC and AfDB estimating investment cost savings of $2.7 billion between 1995-2010, and the generation of over $800 million worth of annual trading in electricity by 2010.

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The AfDB report's analysis is convincing in making the argument that the energy sector in SAR needs to be structurally transformed taking a regional view with (i) early completion of the regional electricity grid; (ii) linking the SAR grid to southern Zaire; (iii) developing the hydropotential of the Inga river (44 GW) through regional investment involving a large role for the private sector; (iv) developing and institutionalising flexible intra-regional power pooling and system management arrangements; (v) agreeing on a satisfactory level of tariffs for cross-border power exports; along with (vi) suitable payments and settlements systems which minimise exchange and transfer risks in settling accounts for electricity traded between countries.

Clearly, the risks of monopolistic or monopsonistic behaviour on the part of the largest buyers and sellers of electricity in a regional context need to be guarded against through appropriate regional regulation. There are also technical and engineering risks involved in planning and managing the second-to-second operations of interconnected power systems in real time to avoid the costs and risks of inordinately costly systems crashes.

Outside of the electricity power sub-sector there are major opportunities in SADC for rationalising and redirecting crude oil and refined product flows involving Angolan oil more sensibly through the existing refineries in the region; developing gas fields for regional markets through private sector ownership and investment; and in finding ways of exploiting the region's coal resources for energy supply (AfDB, 1993).

9. *Financial Sector Policy*

The broader *real sector* adjustment problems faced by Africa and SAR are reflected in the poor condition of their *financial systems* whose health and capacity are profoundly affected by what happens in the real economy and vice-versa. To any casual observer Africa's financial systems appear patently dysfunctional in performing their main roles: adequate financial resource mobilisation to meet the investment and working capital needs of the real economy; efficient allocation of financial savings through effective intermediation; operating payments and settlement mechanisms which lubricate real sector transactions; offering holders of financial assets sufficient opportunity for portfolio risk diversification; and providing the financial services and credit facilities needed to facilitate trade and investment transactions across borders.

In SADC, South Africa has a financial system whose depth, diversity, sophistication and level of development probably exceeds the needs of its real economy. That has perhaps created a different type of real vs. financial sector imbalance which is exacerbated by its excessive risk aversion in

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dealing with the hitherto dispossessed part of South Africa's economy. Its SACU neighbours, to which the South African system extends (albeit not as prominently or effectively), are also reasonably well served, as is Mauritius whose financial system is not quite as sophisticated as South Africa's. But financial systems in the rest of SAR reflect the characteristics of those found elsewhere in Africa. The need for policy reform and adjustment in the financial sectors of Africa and SAR has therefore been as strong, and perhaps more urgent, than parallel reforms in the real sectors.

In the other SADC countries, financial systems (Zimbabwe's being the strongest, Angola/Mozambique the weakest, and Malawi, Tanzania and Zambia in the middle) are to varying degrees characterised by poor resource mobilisation capacity and effectiveness; high levels of credit risk and non-performing assets; egregious overmanning; poor technology and high intermediation costs; and an intrusive role of government in the ownership and direction of financial institutions. These factors have combined to exacerbate overall resource misallocation and misuse in real sectors dominated by parastatals. With government dominated as both borrowers and lenders, financial systems in Africa and SAR ceased playing any useful independent or impartial role in monitoring/disciplining the use of credit and financial resources in the economy.

What were supposed to be independent intermediation systems, effectively became payments, clearing and bookkeeping mechanisms for deteriorating fiscal systems. Central and commercial banks lent mainly to governments and state-owned enterprises resulting in the private sector being crowded out from credit. Excessive deficit monetisation over long periods retarded the growth of properly functioning interbank or money markets to equilibrate liquidity. Non-performing portfolios, high taxes, and excessive administrative costs steadily eroded bank profitability. Consequently, the integrity of Africa's and SAR's financial systems has degenerated over time becoming shallower and narrower, reflecting (and resulting in) low rates of financial savings, and a general lack of public confidence in financial institutions and domestic currency denominated financial assets.

With the successive financial shocks triggered by external payments crises and subsequent adjustment programmes resulting in monetary and exchange rate instability, the level of non-performing assets owned by many SAR financial systems increased to a point where systemic portfolio risk actually materialised and the financial sector became essentially insolvent (World Bank, 1994a). SAPs and FINSECALs in Africa and SAR began paying serious attention to these problems around 1989 and have aimed to achieve five broad objectives: reducing financial repression (in the classic McKinnon-Shaw sense); restoring solvency of the banking system; improving its incentive structure and operating environment; improving standards of financial practice; and upgrading the quality of institutional infrastructure supporting the financial system.

The specific measures taken to achieve these objectives have included (i) interest rate liberalisation involving shifts from negative controlled real rates to positive quasi-market determined rates along with the elimination of interest rate subsidies and reduction of excessively high statutory liquidity and reserve ratios; (ii) market determined allocation of credit to replace fiat-driven, subsidised credit; (iii) restructuring, recapitalisation and in some cases privatisation of public banks with more stringent rules on capital adequacy ratios and provisioning requirements; (iv) liquidating many insolvent non-bank financial institutions (including some development finance institutions); (v) introducing greater domestic and foreign competition in the banking sector by liberalising former entry barriers; (vi) encouraging development of incipient capital market institutions; (vii) strengthening regulatory capacity and prudential supervision in the banking system and over nascent capital market activity; (viii) reducing overmanning levels and introducing new technology to bring payments, settlements, accounting, auditing, control, and risk management systems in line with acceptable standards (using international benchmarks from other developing countries) on a phased basis; (ix) aiming at more general improvements in the quality of financial reporting practices and standards; and (x) improving the quality of legal standards and practices applicable to financial transactions and collateral realisation/asset recovery procedures.

Both the diagnostics and the prescriptions appear intelligent and exhaustive. So, what has the overall impact of financial sector adjustment in the non-SACU economies of SADC been so far? It has in generally been unimpressive and disappointing (World Bank, 1994a; Jayarajah and Branson, 1995). Some progress has been made with lessening the extent of financial repression with movement from highly negative, controlled real interest rates to positive rates, lower liquidity and reserve ratios, and some success in increasing private participation in banking systems (but with no clear evidence as yet that such participation has improved bank operating performance). Regrettably, many of SAR's financial systems continue to fund large deficits of governments and parastatals; the first round of bank recapitalisations and balance-sheet clean-up has been succeeded by a second round of new portfolio problems.

Financial sector reform has been complicated by the persistence of large fiscal deficits and sudden shift to high real interest rates and more realistic exchange rates. The combined effect of these adjustments has generally been to worsen bank portfolio quality problems and trigger systemic insolvency. A shift to high real interest rates impinges adversely on government and parastatal accounts in countries which have high levels of outstanding domestic debt (e.g. Zambia). Moreover, bank recapitalisations have been extremely expensive, imposing fiscal burdens of between 2-8% of GDP annually. In Tanzania the cost of a partial restructuring of the main state-owned commercial bank was estimated at 40% of GDP (World Bank, 1994a).

Collateral recovery rates on failed loans have been disappointingly low with liquidation costs absorbing a large proportion (30-65%) of the amounts recovered. Relatively little progress has been made with implementing the other measures listed above, or in having those measures which have been attempted yield visible results. Nor is there any persuasive evidence that financial sector adjustment efforts have resulted in increasing total or financial savings or in supporting increased productive private investment in SAR or Africa (World Bank, 1994a; see also Annex Table 16).

Experience with FINSECALs and SAP conditionality related to financial sector reforms in Africa and elsewhere suggests that:

- cause-effect relationships between financial reform instruments and fiscal/monetary targets are either not properly understood *ex ante* or not taken fully into account; e.g. when funds required for bank recapitalisation are so large as to rebound on fiscal targets and destabilise monetary aggregates; or when interest rate liberalisation and credit decontrol affect government finances and destabilise money demand/supply parameters;
- if macroeconomic stabilisation has not been achieved before financial sector liberalisation gets underway, the effects are usually counterproductive; e.g. when interest rates are liberalised *before* inflation rates and budget deficits are brought under control and before external capital flow volatility has been dampened, the result is usually an uncontrolled money spiral;
- financial sector liberalisation should follow, not precede real sector liberalisation because real sector adjustment usually takes place more slowly; e.g. when the big financial prices (interest and exchange rates) are liberalised before real sector prices have adjusted, significant misallocation of credit could result;
- institutional reform in the financial sector may need to precede price reform because weak and fragile institutional structures and operating systems can crack in the face of major financial price adjustments with their implications for portfolio performance;
- interest *structure* rationalisation and simplification should precede interest *rate* liberalisation; and
- banking sector adjustment and reform should be undertaken with performance being stabilised before adjustment is attempted with non-banks and capital markets.

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With the desultory outcomes of attempts at financial sector reform in SAR, and with the benefit of learning from elsewhere, how would a *regional* approach to improving financial sector restructuring and functioning be superior to efforts confined largely to the national level? In answering this important question, the analysis of financial sector issues contained in the AfDB's 1993 report provides vital clues in observing that financial sector reform in individual SAR countries is likely to occur at a much slower pace if the institutional and financial resources of the *region* are not fully deployed in resolving the institutional, human and technological deficits which exist in each national system.

The strategy required by a regional approach to financial sector reform and development would be based on the central pillar of regional linkages being established through a process of financial institutional development, employing a flexible approach which emphasises the following four broad areas:

(a) Fostering an efficient and well-capitalised *commercial banking system* in each individual SAR economy which is inter-linked on a regional basis and operates under a common, rigorous regulatory and supervisory structure. Such a system would require the existing foreign banks in the region, the present strong South African banks, and the region's several strong central banks (in particular those of Botswana, South Africa, Mauritius and Zimbabwe) to play a much larger regional role by bolstering and supporting a market-driven process of new entry, acquisition, merger and restructuring of banks which is already underway. The model would employ a *universal banking* approach permitting banks to engage in term lending and capital market activities. It would be supported by a regional regulatory framework designed to suit multi-purpose banking. Such a framework would require establishing common or at least harmonised regional standards for bank regulation and supervision with respect to matters such as standardised bank documentation; asset and risk classification, provisioning, audit specifications, licensing and regulatory requirements, capital adequacy ratios, deposit insurance etc.

    A regional interbank market in SAR currencies and foreign exchange, and interbank payment clearing arrangements would go a long way toward strengthening commercial banking operations region-wide especially if common monetary arrangements could be expanded beyond the MMA. Moreover, encouraging the development of commercial banks with regional branch networks across SAR would add immeasurably to encouraging cross-border trade. There are advantages to IFIs and SAR governments involving South African banks more actively in the restructuring, recapitalisation and privatisation of

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public sector banks throughout SAR as a means of facilitating their entry into national markets with a nationally beneficial *quid pro quo* attached.

(b) The restructuring of crippled or insolvent *development finance institutions* (DFIs) which litter the landscape of SAR's financial sectors could be dealt with as part of a comprehensive regional financial reform package. DFIs could be restructured on a *regional* basis through acquisition, merger, rationalisation and recapitalisation. This could be achieved either within the DFI community with external assistance or by national public DFIs being offered for sale to regional or foreign commercial and investment banks for low-cost or no-cost buy-outs. The *quid pro quo* would be that the banks would clean out DFI portfolios and revive them within a time-bound frame or wind them up in an orderly fashion after having segregated their good portfolios from the bad. This approach could be extended by establishing a regional asset recovery and reconstruction fund accessible to all DFIs within the region which would enable dormant assets or those in receivership to be sold on a wider regional market with specific arrangements being made to deal with the recovery of assets of public enterprises in default to DFIs.

(c) Using the institutional and financial strength of *insurance* companies in Mauritius, South Africa, and Zimbabwe to develop a region-wide market for insurance open to private sector participation. Under a regional approach to developing a broadly based insurance industry, institutions would emerge which could manage risks better across a wider geographical market than have risks excessively (and artificially) concentrated in small national ones. SAR governments could collaborate to: re-introduce competition in their national insurance industries; develop a reinsurance capability at the regional level; and adopt regional regulation and supervision of insurance companies. The stronger insurance companies in the region could do much to stimulate competition, introduce new products, introduce improved actuarial and market pricing techniques, and transfer up-to-date technology by entering deregulated and open insurance markets in SAR countries beyond their own. Regional cross-investments and management entry by the major insurance companies in southern SAR could assist in the financial restructuring of public national insurance monopolies which are now being restructured and privatised in the non-SACU economies.

Extension of insurance markets and the revival of insurance industries in SAR economies could do much to facilitate the development of regional capital markets by creating a long-term institutional investor

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capability which presently does not exist outside of SACU and Mauritius. Such possibilities are capable of being translated into realities with increasing exchange rate convertibility and open current and capital accounts now emerging across the region.

(d) The establishment of a privately backed *regional stock exchange* operating from an offshore jurisdiction without exchange controls could help to link SAR economies with international capital markets and attracting foreign portfolios which have been conspicuously absent from countries in SAR other than South Africa, Zimbabwe and Mauritius. Such an exchange would be useful in linking SAR markets to capital-surplus markets in Asia which may be more interested in acquiring risk exposure in SAR than traditional markets in Europe and America. This initiative, whilst of lower priority to more urgent reforms in banking and insurance, is worth the support of SAR governments and the international community as a means to foster domestic capital market and stock exchange development, increase and diversify opportunities for mobilising foreign savings, and developing incipient international linkages between nascent markets in SAR and those elsewhere.

These four areas illustrate broadly how individual SAR countries would gain if they leveraged their own limited and overstretched financial and institutional resources, with the more substantial capabilities that the stronger financial systems of the region have to offer. To the extent that financial markets are freed, and entry barriers to regional and foreign investment in domestic financial sectors are lowered, much of what has been suggested is likely to happen anyway. But it will take place more slowly than the needs of the region require.

The national approaches which are taken by traditional SAPs and FINSECALs cannot possibly offer as much. Their orientation and focus needs to be changed to incorporate wider regional dimensions which may make their outcomes more fruitful and effective than they have been so far. For the pace of reform to be accelerated in a manner which is commensurate with the needs of financial systems across the region, concerted action is required within a consensually agreed framework for regional cooperation and financial linkage development, by SADC governments, the region's international interlocutors and economic disciplinarians, and by private sector institutions and agents from within the region and from outside SAR.

10. Rationalisation and Privatisation of State Enterprises

The core of the development crisis and adjustment problem of Africa

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and SAR resides largely in the malfunctioning of state-owned enterprises. These state enterprises which, in SAR, were created in abundance, predominated in virtually every sector of SADC economies in the post-independence era. They were built to get away from the ethos of the free-but-reserved market colonialism which was extractive in nature and did little for local development. Under the populist socialist theories of the day, parastatals were supposed to deploy resources, achieve rapid industrialisation, accelerate development and generate surpluses for the public good. By contrast, markets, private ownership and foreign investment were suspect. In pre-independence Africa, the larger private firms (especially the mining, construction, manufacturing and plantation conglomerates) were owned and operated largely by colonial metropolitan interests. Smaller (mainly trading and services) firms were owned and operated by non-Africans imported from other colonies to perform petty commercial functions. There was little evidence visible of indigenous African private entrepreneurship being in existence when independence was achieved.

In retrospect, African parastatals achieved largely the opposite of what they were intended to. Overmanned, overprotected, fiscally cushioned, financially undisciplined and open to rampant political interference, they became conduits for achieving political rather than commercial objectives. In the process, far from achieving the broader objectives of industrialisation and development, they turned into vehicles through which the private agenda of public officials and political leaders, rather than those of the commonweal or public good, were fulfilled. While absorbing the largest proportion of employment outside of the agricultural sector, parastatals laid claims to disproportionate amounts of fiscal resources for capital investment – very inefficiently used – and for covering operating losses which accounted for a significant proportion of national GDPs, representing a major drain on increasingly insolvent exchequers. Their operations resulted in distorting prices, markets, budgets and money virtually across the board, and introducing untenable rigidities in markets for tradable and untradable goods, services and production factors. This damning indictment of public enterprise performance in Africa is sweeping, but should not convey the impression that no parastatal in Africa can justify its existence. There are in fact many parastatals which can and do. But they are few and most of these are in South Africa and SACU. Even there, their performance is sub-optimal although not quite as draining of scarce national resources as elsewhere.

The adjustment conditionality relating to public sector reform usually focuses on both government and civil service reforms as well as parastatal reforms. In the first category, the objectives supported by specific measures are to (i) reduce the role and size of government as a whole and diminish its intervention capacity in the economy; (ii) reduce the number of goods and services which have been taken for granted as being public in nature and introduce greater private sector involvement and competition in the provision of such goods and services; (iii) shift the government away from direct involvement in productive activity and have it concentrate on core functions of governance and effective market regulation through the establishment and enforcement of rules which ensure competition; (iv) reduce overstaffing in government; (v) use the resource savings from civil service reduction to improve pay scales, working conditions and other incentives to attract and retain a better quality of civil servant; and (v) retrain/retool civil servants to perform at much higher levels of efficiency.

Where parastatal reform is concerned, the aims have been to (i) rationalise and reduce their number; (ii) close enterprises which are inherently uncompetitive and unviable and for which the costs of restructuring would exceed any benefit emanating over the discountable future; (iii) corporatise and commercialise the remaining state enterprises through radical restructuring, downsizing, cost-cutting and technology upgrading into operating efficiently and profitably through increased capacity utilisation and improvement of product/service output as well as its quality/cost; (v) financial restructuring; (vi) management and organisational revamping; (vii) weaning parastatals from dependence on government for subsidies and investment funds; and (viii) privatising as many of them as possible under domestic and foreign absorption constraints.

Though the need to proceed rapidly on all of these fronts has been obvious for some time, little progress is being made with public sector and parastatal reform in Africa (in sharp contrast to experience in Latin America, Eastern Europe and East Asia, but similar to experience in South Asia). Although there are signs that progress in 1994-95 has been more encouraging on this front than between 1989-93, no effective solution has been found to the plethora of problems which is constipating the process of public enterprise reform and inhibiting effective privatisation in SAR and, in the process, preventing the desired supply-side response to adjustment from taking place. Yet of all the sub-regions in Africa, SAR has the greatest potential for rapid movement on this front by using the *regional* capabilities that the stronger economies of SADC have. The capacity exists of meeting extant concerns of adjusting governments while retaining regional and domestic ownership. Opportunities can also be devised for putting in place arrangements to expand domestic ownership at a pace commensurate with the development of absorptive capacity in domestic capital markets, using interim trust fund arrangements for share ownership in privatised enterprises (Mistry and Griffith-Jones, 1992) involving public international investors. Some headway has already been made by South

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African and Zimbabwean firms acquiring former public enterprises in Tanzania, Zambia, Mozambique, and Zimbabwe in areas such as brewing, food processing and cigarette manufacturing sectors as well as in hotels and aquaculture.

But left to market forces alone, progress is likely to be much less rapid than is potentially possible through more systematically organised, concerted initiatives involving IFI-backing and long-term financing including organising pools of external portfolio equity. Almost on an industry-by-industry basis – and nowhere more so than in the financial services, power, transport services (especially air, road haulage and railways), water supply, telecommunications, construction, mining, manufacturing and tourism sectors – the management and institutional capacity exists within one SAR country or other (especially in South Africa, Zimbabwe, Mauritius and in some cases even Botswana) to do much more toward reform and privatisation of parastatals in the weaker SAR economies.

The required merchant and investment banking skills certainly exist within the region (although they appear absent at the national level in AMMTaZZ) as do capital market capacity (in Johannesburg, Harare, Gaborone and Port Louis), accounting, auditing and valuation skills, as well as the makings of an adequate legal framework and judicial capacity, to engineer and absorb privatisations in tandem with cross-regional shareholding arrangements in SAR on a larger, more ambitious scale than can possibly be envisaged if the restructuring focus is confined to domestic markets alone.

Such arrangements, based on a regional perspective, are a feature whose time has come. It is difficult to see a rational, efficient network of utilities, transport services, and supporting financial services developing in the region if the opportunities offered by present privatisation programmes in the non-SACU countries of the region are not seized sensibly to the mutual advantage of all. Private cross-holdings of entities in these sectors would permit much more rational and efficient investment programmes to be undertaken without reliance on government budgets, and much more efficient management and operation of their facilities and services on a region-wide basis (within corporate structures that would allow for much faster development of the HLM resources needed).

Moreover, market enlargement under effectively evolving regional integration agreements coupled with freer movements of capital and labour across borders, would permit the regional market to function much more efficiently than confined and fragmented national markets in facilitating the rationalisation and restructuring of manufacturing capacity across the region in a wide range of industries. As already emphasised, the financial engineering, accounting, legal and technical knowledge and expertise required to design and structure the large number of potential privatisation transactions involved exists within the region, probably at a higher level of sophistication than within the IFIs themselves. It is under-utilised and can be much more effectively used for regional benefit.

Until 1994 it would have been euphoric and prematurely wishful to contemplate such possibilities. But thanks to the remarkable transformation that has taken place in SAR since April 1994 that is no longer the case. It would therefore be a dereliction on the part of the IFIs, the international donor community and the AfDB, if their third-generation adjustment programmes for 1996-2000 did not incorporate in their design architecture a *regional approach* to achieving public sector reform-cum-privatisation objectives in SAR, using the formidable private sector skills and capital market resources that SADC (with South Africa in its membership) now embraces.

V Conclusion

It may suffice to conclude with the reiterated observation that the paper has attempted to demonstrate, based on available empirical evidence and analysis of literature, that a strong case can be made for thinking more carefully about the regional dimensions of the usual structural adjustment prescriptions, and ensuring that reform prescriptions at a national level are consistent with a wider regional perspective. Whether the paper has been sufficiently convincing is for the reader to judge; an attempt has been made to strengthen its arguments by focusing on linkages between adjustment and integration in ten distinct yet inter-related areas of policy reform.

Unfortunately, the paper has not dealt with other important dimensions of adjustment which have regional repercussions such as the *social* dimensions of adjustment, nor has it dealt with the crucial links between adjustment and integration in key sectors such as transport, telecommunications, tourism, water, ecology, health and education. All of these sectors are, arguably, as important to consider as subjects for adjustment in the case of SAR as the three specific sectors which have been analysed. The other areas have been touched on in AfDB's study (1993); but time and knowledge limitations have precluded this paper from examining them. Instead this paper has been confined deliberately to those areas of policy, and to those sectors, in which the WBG has evaluated adjustment experience in Africa and elsewhere in a systematic, organised fashion, so as to have an intellectual peg, with supporting evidence, for this paper to hang its arguments upon.

In its discourse, the paper has drawn attention to the absence of system-

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atic, rigorous thinking by the IFIs about mutually reinforcing linkages between RIAs and SAPs. Virtually no attempt has been made to operationalise the essence of such linkages into adjustment action and conditionality. A close look at what adjustment conditionality aims at, and what it actually achieves, shows not just a large gap between expectations and outcomes, but also a lack of concern for the effects of domestic adjustments on neighbouring countries.

Precisely what stabilisation and adjustment problems one diagnoses, how one arrives at the right prescriptions about controlling and liberalising economies, what range of policy instruments one uses, and in what order one deploys them, are critical determinants of the good or harm that a country risks doing to itself or to its neighbours. For the prescribers of SAPs this has, till now, been a costless process except in terms of lost reputation. But for adjusting countries in Africa the costs have been very heavy. They have been at an intellectual and negotiating disadvantage in determining (except by default) the nature, pace and sequence of the adjustments foisted on them. Indeed, belated concerns about the *ownership* of such programmes implies precisely that unfortunate reality.

When after ten or more years, guaranteed prescriptions have failed to effect the promised cure, African countries have been left with a legacy comprising unserviceable burdens of unproductive multilateral debt and chronic overdependence on the largesse of donors, which is of course heavily politically conditioned. Donors on the other hand are left with the embarrassment of explaining to their constituencies for aid why the tax resources provided have been wasted in such large amounts for so long. As is the case with any patient immobilised for quite as long, recovery in Africa is likely to be much longer, slower and more painful than anyone would wish.

In making the case for the regional dimensions of structural adjustment to be taken into account in a more rigorous fashion, the paper has alluded to specific problems and has made suggestions in key policy areas which, taken together, could constitute a skeletal outline for the contents of a regional adjustment programme for SADC should the occasion ever arise to implement such a programme, and should the membership of SADC ever decide to contemplate the possibility. That, at present appears unlikely. It may be far more likely, and perhaps more desirable, that the members of SADC take on board the problems outlined and the suggestions made in each area of policy, as a possible agenda they might pursue and develop but, preferably avoiding the involvement of external agents in the kind of relationship between an adjusting country and IFIs that typically develops under a SAP.

The agenda could be used as an *aide memoire* by individual countries, as

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they formulate their own adjustment efforts at the national level, to ensure that they are heading in a direction which is compatible with their (and their partners') regional interests and not inimical to it. Some of the problems identified and ideas suggested in highlighting the regional dimensions of adjustment, and suggesting the incorporation of regional features in the design of adjustment, are recapitulated in telegraphic form below.

Fiscal Policy

- Revenue dependency on regional trade and invisibles transactions.
- Fiscal implications of intra-regional remittance-flow dependencies.
- Regional fiscal spillover effects from regional tax arbitrage opportunities.
- Revenue losses from intra-regional parallel market trade.
- Deficit spillover effects of region-wide droughts and measures to combat them.
- Savings in public investment from regional approach to infrastructure.
- Recurrent budget savings from joint operations in transport and utilities.
- Positive fiscal benefits from regionally agreed reductions in military expenditures.
- Fiscal savings from tax harmonisation and joint revenue administration.
- Fiscal savings from reducing arbitrage opportunities in mining taxation regimes.
- Avoidance of counterproductive regional fiscal competition to attract FDI.

Monetary Policy

- The value of peer group pressure in exerting monetary discipline under MMAs.
- Benefits vs. costs of extending the rand zone throughout SADC.
- Reduction of intra-regional financial risks and transaction costs with MMAs.
- Savings realised through cooperative monetary arrangements.
- Savings/leverage effects of reserves pooling.
- Effects of MMAs on forcing greater fiscal and exchange rate discipline.
- Opportunities for regulatory savings and improved enforcement.
- Better prudential supervision of financial systems.

Exchange Rate Policy

- Benefits of stabilising exchange rates after a long period of excess instability.
- Effects of exchange rate instability/inconvertibility on inhibiting regional trade.

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- Regional Exchange Rate Stabilisation Fund (REXSTAB) to support MMA.

Labour and Wage Policies

- Policy twist in regional labour markets: HLM competition vs. LLM displacement.
- SAR labour market problems/anomalies best dealt with in regional context.
- Cross-border labour flows and corresponding remittance effects.
- Intra-regional conflicts of interest with attracting HLM while repelling LLM.
- Brain drain effects of existing wage/labour policies on poorer SAR economies.
- Freeing labour and capital markets to unwind regional wage twist.
- Regional approaches to mass employment creation (Angola, Mozambique etc.).

Trade Policies

- Actual and potential intra-SADC trade much larger than usual figures suggest.
- Two-step approach to achieving competitiveness: region first; world later.
- Regionally coordinated rounds of tariff and non-tariff barrier reductions which deal with intra-regional and extra-regional liberalisation simultaneously; ensuring that extra-regional barriers are not so high as to vitiate reforms aimed at intra-regional efficiency-enhancing initiatives.
- Improvement of regional market sourcing opportunities to encourage trade-substitution effects in favour of intra-regional trade without incurring trade diverting inefficiencies and risks.
- Buying time for regional adjustment through learning effects.
- Two-tier regional protection structure to avoid immediate South African domination (and swamping effects) of regional production of manufactures through initial dumping at the expense of de-industrialisation elsewhere in SAR.
- Offsetting intra-regional current account imbalances with offsetting market-driven investment capital flows in reverse directions.
- Increasing intra-regional trade in invisibles, i.e. water, electricity, transport, tourism and financial services through market driven as well as government promoted efforts.
- Gradual extension of SACU to rest of SADC under modified arrangements.

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Industrial Sector Policies
- Importance of regional adjustment in mining and manufacturing.
- SAP approach to adjustment will reinforce the de-industrialisation already occurring in most SAR countries other than South Africa, Zimbabwe, Mauritius.
- Regional adjustment approach to industrialisation may be theoretically second best but is pragmatically first best.
- Delayed free market regional integration option for industrial adjustment in SADC would be preferable to implied SAP/ISECAL option of exposing very weak domestic industries to pressures of international competition too swiftly.
- Temporary protection of SADC industries from South Africa, Zimbabwe and Mauritius with lower barriers than from the rest of the world, allowing sufficient time for catch-up to occur in other SADC economies.

Agricultural Sector Policies
- Regional approach to structural shift in cereal production areas from southern (irrigated) to more agro-climatically efficient northern (rain-fed) areas in SAR.
- Regionally coordinated approach to agricultural subsidy withdrawal which encourage market forces across the region to bring about changes in production frontiers and agricultural output/export diversification programmes.
- Regional adjustment to future demand patterns for food in SAR, with the prospect of South Africa turning from a grain exporter to importer after 2001.
- Regionally coordinated development of agricultural infrastructure, especially for water, rural roads, communications and power.
- Combining land reform imperatives in southern SAR with food security imperatives of region by opening up arable lands in northern SAR through regionally organised land swaps.
- Regional integration of efforts in agricultural research, animal and plant disease control, agricultural marketing in world markets, training and extension.

Energy Sector Policies
- Regionally coordinated changes in energy pricing policy to enable cost-efficiency benefits of regional power generation and transmission to be realised; such an approach would enable projects to be developed which could not be justified or conceived under fragmented national market limitations.

- Regional welfare benefits and reduction of public investment budget pressures of capital investment savings, and a concomitant shift in investment burdens from the public to the private sector, which could be realised from coordinated investment in economically sized power projects for regional markets.
- Greater security and stability of electricity supply from regional approach.
- Significant reductions in annual operating costs from regional power system management.
- Trading benefits from expanding exchanges of electricity across SAR borders enabling other SADC economies to increase their earnings from invisibles exports to South Africa and partly offsetting the intra-regional current account imbalance.
- Regional grid completion (priority) and establishment of intra-regional electricity pooling and trading arrangements with accompanying arrangements for swift intra-regional payments in settlement of power trading accounts.
- Regional grid link to southern Zaïre Inga river hydropower generating site.
- Regional cooperation on refinery capacity and output mix rationalisation to optimise production and transport cost efficiencies for refined oil products.
- Regional approaches to development of regional coal and gas potential for energy use and energy exports rather than for raw ore exports and wasted gas.

Financial Sector Policies

- Linked with regional monetary arrangements, a regional approach to financial sector stabilisation, institutional rationalisation, rehabilitation and development in SAR would be more efficient than SAP/FINSECAP approaches limited to national markets with limited internal financial and institutional capabilities.
- Need to develop capable regional commercial banking network which is financially strong, institutionally competent, technologically up-to-date, and capable of providing services to expand cross-border trade and investment.
- Regional approach to restructuring and recapitalising national development finance institutions in SADC within a more holistic framework would be more efficient and cost-effective than attempting to resolve their insolvency and illiquidity at the national level.
- Regional approach offers opportunity of developing healthier, more competitive and efficient insurance and long-term institutional savings

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industries in SAR's national markets than would be possible through a purely national approach; a healthier insurance industry would promote the development of capital markets faster than financial systems in which such industries are weak.

- Regional approach is essential to the cost-efficient development of non-banking capital markets for equity, bonds, other financial instruments and foreign exchange.
- Regional multi-market stock exchange initiative.
- Regional approach to financial system regulation (banking and capital markets) would promote visible savings in regulatory costs, avoid regulatory capture risks and produce a number of invisible benefits which would favour the maintenance of prudential supervision and the minimisation of systemic risk; it would prevent the risk of a domino effect of financial system risk materialising in one country having consequential spillover implications for its neighbours.

Public Sector Reform and Privatisation Policies

- Regional approach to public sector reform and privatisation would enable individual countries to access a much wider pool of institutional, financial, knowledge and human resources than can possibly be mustered in any national context to overcome the problems presently being faced with parastatal reform and privatisation efforts across SAR.
- Synchronicity of concurrent reform and privatisation initiatives across SAR provides a unique opportunity for *intra-regional cross-holding* patterns to be developed in the region's utilities and transport companies (i.e. electricity, water supply and river basin management, telecommunications, airlines, airports, railways, road haulage, shipping) as well as in publicly owned financial institutions and tourism facilities.
- Taken advantage of properly, intra-regional cross-holdings would permit, through acquisition and merger, stronger regional institutions to emerge in all of these areas enabling the region to capture economies of scale and operating efficiency benefits.
- Cross-holding opportunities could be availed of even prior to privatisation or public flotation to make the resultant restructured regional companies more attractive to domestic, regional and international investors.
- Such a regional approach would enable SAR governments to derive far more value from divestiture and asset sales over time than under the less efficient national approaches presently under consideration.
- Regional approaches to privatisation in manufacturing and mining would also yield more efficient outcomes than national approaches in matters such as privatisation pricing and regional market absorptive capacity.

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- International trust fund arrangements (to safeguard national interests, most domestic markets in SAR have developed the absorptive capacity to enable widespread public shareholding of privatised corporations) could be devised to go hand-in-hand with regional approach to public sector reform and privatisation.

Regional integration and structural adjustment are both vital to improving the economic, political and social prospects of the region. The imperatives of neither can be escaped. But each can be pursued inefficiently or efficiently. There is more than enough *prima facie* evidence to suggest that a *regional* approach (whether it involves simple cooperation, or progresses to closer coordination, harmonisation or integration) to the economic challenges SAR confronts – including perhaps most immediately and importantly the challenge of successful structural adjustment – is likely to yield greater pay-offs than national approaches which have been tried and not yet yielded very much.

It is perhaps time for the region's governments and the international community to be bolder and more imaginative in the vision they have for the future of the region and in the commitment they have to making it happen. Such a vision cannot avoid incorporating the regional dimensions of structural adjustment in the thinking of the region's political leaders, technocrats, economists, policymakers, market-makers and of everyone at large. The IFIs and the donor community need to go beyond encouraging words about regional integration into operational actions that make its requisites a part and parcel of the adjustment paradigm for SAR and for Africa. Sadly, as a consequence of the economic unravelling of Africa which has taken place over the last three decades – and it has to be honestly admitted that adjustment experimentation has played its part in that discouraging process at least over the last decade – most Africans have lost hope that the future will be better than the present or the past.

For Africa to progress, hope must be restored through delivery and action rather than slogans and rhetoric. A regional approach to adjustment and development in SAR offers an alternative which is not inimical to adjustment but may enhance its outcomes. For that reason alone, more work needs to be done to explore further, and more rigorously, some of the points that have been made qualitatively and impressionistically above.

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Annex 1 Broad Policies, Objectives and Specific Adjustment Measures

A. Macroeconomic Policies

Broad Policies/Objectives	*Sub-policies/Specific Measures*
1. Fiscal Policy Reduce fiscal deficit Enhance revenue efficiency Enhance expenditure effectiveness Focus govt role on "enabling conditions" Reduce role of government Provide affordable social safety nets Reduce state ownership of enterprise	*Reform of tax structure: direct vs. indirect* *Revenue raising and administrative measures* *Expenditure reform:* • *Subsidies* • *Recurrent expenditures* • *Size of civil service* • *Social priorities* • *Human capital priorities* *Public investment reform:* • *Sectoral priorities* *Sovereign debt management policies* *Budget process reform and enhancement.*
2. Monetary Policy Control money supply Align money demand with growth Control inflation Positive real interest rates	*Monetary targeting/direct controls* *Reduction of seigniorage/open market ops.* *Interest rate policy as basis for allocation* *Elimination of directed credit policies* *Sovereign debt service relief/reduction* *Financial programming model approach.*
3. Exchange Rate Policy Establish right level of X-rate Eliminate black market premia Maintain exchange rate equilibrium Stability of real effective X-rate Induce switching effects Reduce current account deficit Encourage capital inflows	*Initial large devaluation* *Elimination of fixed official X-rates* *Crawling peg/dirty float/full float* *Reserves policy/forex open mkt intervention* *Competitive exchange rate policy* *Early liberalisation of current account* *Gradual liberalisation of capital account* *Progressive forex market development.*
4. Labour and Wage Policies Establish/restore competitiveness Reduce labour market distortions/rigidities Reduce excess costs of formal employment Relate wages to "firm" viability Eliminate govt over-employment Increase formal employment	*Revamp rigid labour laws* *Eliminate govt monopoly over hiring/firing* *Remove restrictions on collective lay-offs* *Encourage collective bargaining at "firm" level.* *Eliminate indexation of wages* *Remove govt intervention in setting wages.*
5. Trade Regime Reform Increase/diversity exports (vol./value added) Improve trade competitiveness (price/quality) Reduce imports (in relative not absolute terms) Increase domestic value-added of trade Shift inv. from inefficient to efficient prodn	*Tariff revision/reduction to lower protection* *Lower or remove various non-tariff barriers/qrs* • *eliminate forex rationing measures* • *eliminate import/export licensing measures* *Improve customs efficiency/administration* *Specific import liberalisation measures/policies* *Specific export promotion measures/policies.*

B. Real Sector Adjustment Policies

Broad Policies/Objectives	*Sub-policies/Specific Measures*
6. Industrial Sector Policy	
Eliminate import substitution bias	*Reducing industrial protection (product/sectors)*
Increase/diversify manufactured exports	*Subsidies/duty drawbacks/epzs/ecgis*
Increase industrial value-added	*Capacity-utilisation and investment measures*
Reduce state ownership of enterprises	*SOE restructuring and privatisation*
Reduce SOE losses	*Cost-recovery+profit pricing by SOEs*
Lower entry barriers to new firms	*Reducing/eliminating government licensing*
Eliminate monopolies	*Lower entry barriers to pvt and foreign firms*
Induce competition	*Changes in regulatory law, policy and practice*
Exploit comparative advantage	*Reducing cross industry disparity in protection*
Improve industrial relations	*Removing govt intervention in labour relations*
Improve allocation/investment efficiency	*Greater reliance on price signals/exit barriers*
Upgrade technology	*Investment/accelerated depreciation allowances*
Increase/diversify industrial investment	*Measures to encourage pvt investment/FDI*
Attract foreign direct investment	*Removing restrictions on foreign firms*
Productivity growth	*Removing biases which distort factor utilisation*
Increase industrial employment	*Promoting SMEs through special measures.*
7. Agricultural Sector Policy	
Food security	*Producer incentives and price liberalisation*
Increase in agricultural output	*Improve producer yields/returns, commercial farms*
Diversify product range	*Input cost reduction, financing extension, incentives*
Increase agricultural exports	*Finance high priority imports/market access*
	Reduce export taxes on agricultural commodities
Improve agricultural investment efficiency	*Increase responsiveness to market price signals*
Induce financial self-sufficiency in sector	*Reduce producer/consumer and input subsidies*
Improve marketing of agricultural products	*Open agricultural marketing to private traders*
Improve distribution of inputs	*Open up input distribution to private sector*
Better dispersion/utilisation of agr. credit	*Depoliticise credit provision/improve channels*
Upgrade agricultural technology	*Improve research; open sector to FDI*
Increase domestic processing and v.a.	*Remove price distortions; expand financing*
Develop agro-industries	*Phase out price controls; reduce import input tariffs*
Increase productivity of smallholders	*Land tenure, credit, better input distbn, lower costs*
Expand agr. infrastructure investment	*Cost recovery pricing for irrigation, power, etc.*
Avoid/reverse natural resource degradation	*Environmental consciousness; financing.*
8. Energy Sector Policy	
Reduce price distortions/economic pricing	*Energy price reform policies (centrepiece)*
Effective economic substitution of fuel	*Effective market pricing of all energy sources*
sources	*Rationalisation, restructuring, load management*
Increase capacity utilisation of plants	*Privatisation, FDI, cost-recovery, no subsidies*
Reduce burden on public budget	*Policies to assure sustainability; env. accounting*
Accommodate environmental realities	*Institutional reform, financing, pvt sector entry*
Supply-side adjustment	*Economic marginal cost pricing for customers*
Conservation and sound demand	*Improved technology, investment, network security*
management	*Privatisation; independent regulatory framework*
Reduce wastage and losses	*Rational tariff structures with proper regulation*
Deregulation with improved regulation	*Greater supplier competition at all levels of system.*

C. Financial Sector Reforms

Broad Policies/Objectives	*Sub-policies/Specific Measures*
9. Financial Sector Policy	
Reduce financial repression/ - real rates	*Abandon directed credit; rely on + real int. rates* *Rationalise/liberalise interest rate structure* *Rely on system-wide benchmark guiding rate.*
Improve resource mobilisation and allocation	*Rely on interest rate signalling* *Reduce high statutory liquidity/reserve rqmts* *Eliminate priority sector lending at subsidy rates.*
Increase domestic savings and investment	*Real positive interest rates to attract deposits* *Reduce high implicit taxation on financial savings* *Induce term transformation toward LT instruments.*
Mobilise private foreign savings efficiently	*Positive short and long-term premia on returns*
Lower credit losses and credit risk	*Risk asset classification/monitoring & provisioning*
Lower intermediation costs	*Reduce overstaffing, overbranching, loan loss risk*
Reduce govt/political intervention in finance	*Reduce state-ownership of financial institutions*
Eliminate crowding out of pvt. sector	*Avoid deficit monetisation; reduce public deficit.*
Widen and deepen financial markets	*Strengthen exchange-based trading for equity/debt* *Reduce tax bias against equity/in favour of debt* *Develop markets for government bills and notes* *Emphasis on development of LT bond markets* *Reduce implicit bias for over-gearing of fin. firms* *Reduce risk of systemic insolvency* *Develop exchange market regulatory infrastructure.*
Restore public confidence in financial system	*Privatise; foreign bank entry; avert bank failure*
Reduce/reverse capital flight	*Offer premium forex risk adjusted local returns*
Secure capital adequacy of the banking system	*Restructure BS; enforce capital adequacy ratios.*
Improve profitability of banks	*Close down unprofitable banks; rely on mkt. forces* *Reduce bias towards disintermediation.*
Reduce bank overstaffing and over-branching	*Change labour legislation, back lay-offs, technology*
Extend capital markets/long-term institutions	*Ensure steep positive yield curve*
Restore viability of DFIs	*Rationalise, close, merge and restructure DFIs*
Improve financial institutional infrastructure	*Strengthen central banks, SECs and fraud detection.*
Improve financial supervision & regulation	*Improving Prudential Regulation standards* *Improve quality of manpower and probity.*
Improve auditing and accounting practices	*Encourage entry of foreign accounting firms.*
Enforce property/collateral exercise rights	*Establish fast-track judicial recourse for fin. trans.* *Establish separate recovery agencies.*
Increase competition in financial services	*Remove entry and exit barriers to financial firms*

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D. Public Sector Rationalisation and Reform

Broad Policies/Objectives	*Sub-policies/Specific Measures*
10. Policies for the Public Sector and Privatisation	
Reduce public ownership and no. of SOEs	*Divestiture/privatisation of SOEs*
Corporatise residual SOEs	*Introducing market pricing discipline in SOEs*
Introduce competition in SOE operations	*Removing entry/exit barriers to pvt firms*
Reduce SOE monopolies	*Effective independent regulation and competition*
Improve productivity, efficiency, profits	*Restructuring, recapitalising, widening ownership.*
Improve information on SOEs	*External assistance with accounting/auditing*
Reduce size of Civil Service	*Retrenchment, early retirement, out-placement*
Agency contracting out functions	*Privatisation of service functions; MBOs/EBOs*
Improve service quality	*Public standards, accountability, enforcement*
Good Governance	*Administrative efficiency/productivity.*
Establish privatisation sequence	*Analysis of SOE characteristics and buyers*
Identify future owners	*Analysis of options for sale; broad divestiture*
Price SOEs properly for sale	*Valuation approaches; collateral benefits*
Ensure effective post-sale regulation	*Regulatory framework for PSOEs.*

E. Social Policies to Reinforce Reform

Broad/Policies/Objectives	*Sub-policies/Specific Measures*
11. Policies to mitigate the Social Impact of Adjustment	
Minimise secondary income loss for poor	*Expenditure switching to favour poorest groups*
Minimise negative impact on urban poor	*Targeted expenditure/food subsidy programmes*
Minimise losses in human capital formation	*Protect/target health and education expenditures*
Minimise net loss of employment	*Focus on increasing productive pvt investment.*
Social safety-nets/social security	*Restructuring of public social expenditure*
Avoid urban dislocation	*Compensation policies for retrenched SOE labour*
Induce labour flexibility in LI groups	*Retraining and resettlement programmes*
Enhance LI employment	*Targeted construction and public works programmes.*

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Comment on "Regional Dimensions of Adjustment in Southern Africa," by Percy S. Mistry

Alieu Jeng

This is an excellent paper, so I will comment on only a few aspects of the presentation. First, there has been too much emphasis on South Africa as the regional hegemon. We have viewed South Africa as the giant in the region, but the relationship is one of interdependence; South Africa needs the region as much as the region needs South Africa. This has been demonstrated in a number of key sectors such as energy and water resources. We need to be cautious in depicting South Africa as the regional hegemon. The same holds true for COMESA. To say that South Africa's absence from COMESA deprives that organisation of the regional credibility that it needs is going too far.

With regard to structural adjustment programmes, it will be extremely difficult to negotiate a regional structural adjustment programme, but once the programme is negotiated, it should be fairly easy to implement since all of the parties know what is expected of them. Perhaps we would need an OECD-type of regional forum where finance ministers and central bank governors can meet. This forum could even meet now to discuss issues of convergence in terms of fiscal and monetary policies and so on.

One issue remained unclear. While the title of the paper is "Regional *Dimensions* of Structural Adjustment", there is a lot of phraseology in terms of a regional *approach* to structural adjustment. I'm not sure that these two things mean the same thing, and it isn't just a question of semantics. Regional *dimensions* of structural adjustment, as I see it, implies that structural adjustment will operate on an individual country basis, and that the regional dimension will be considered in the process.

However, when you talk about the regional *approach* to structural adjustment, I conjure up a different picture in which all of the countries sit down together to work out a programme of structural adjustment for the region. The countries would agree to the programme and implement it. We have to be clear about what we are discussing here. I admit that I have difficulty with either position.

Now I would like to turn to the African Development Bank's view which is, in fact, consistent with Percy Mistry's presentation. Following up on

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our 1993 study on economic integration in Southern Africa (of which Percy Mistry was the Chief Consultant), the emphasis is on the next steps. The AfDB has decided to implement the recommendations listed in a recent report that we have taken to our Board, entitled "The AfDB Study on Economic Integration in Southern Africa - The Next Steps". Policy reforms at the country level will be pursued, and specific macroeconomic and sectoral studies will be undertaken to assist policymakers with investment decisions on regional projects and programmes and institutional reforms. The task of coordinating these various activities will be the responsibility of the governments of the region, the African Development Bank, and the sub-regional institutions – mainly SADC, COMESA and SACU. The AfDB is going to be responsible for playing a catalytic role in the dialogue and follow-up actions.

Financial and manpower resources, beyond the AfDB's capacity, are required to implement the recommendations of the report, so the AfDB will have to involve donors for financing the project. We need to identify specific sectors and activities in which we could take a leadership role while consulting with countries on a specific programme.

The objective is to enhance the AfDB's capacity to work out a regional programme of action for economic integration. We would concentrate on trade and finance. In view of the cross-cutting nature of the issues involved in this sector and given their importance for integration, we would continue to support the stabilisation and adjustment process in Southern Africa through policy operations, assistance to development foundations and offering lines of credit.

We will discourage uncoordinated, country-specific adjustment programmes and move, instead, towards operations which consider the coordination and harmonisation of fiscal, monetary and exchange rate policies. To make these interventions more effective, economic integration conditionalities will be incorporated into the design of the structural adjustment programmes of the AfDB. In trade matters, we will give priority to trade finance and the development of a commercial banking system.

The programme we have in mind is phased from 1996 to 2000 with specific agendas regarding a plan of action. I think that our programme will promote the process of linking structural adjustment and economic integration and thus support the proposals made by Percy Mistry.

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Comment on "Regional Dimensions of Adjustment in Southern Africa," by Percy S. Mistry

Gene Tidrick

It is difficult to comment on such a rich paper in fifteen minutes, especially when there is so much in the paper with which I agree. I will therefore concentrate on a few points and emphasise points of disagreement.

The main question posed in the paper is why structural adjustment programmes have fallen short of expectations in Southern Africa. There are many answers that could be given to this:

- One is that expectations were too high. Africa is different, and it will take a lot longer.
- A second is that structural adjustment programmes were poorly designed; there was a lot of experimentation in Africa.
- A third is that critical elements missing, in particular, fiscal adjustment, parastatal reform and utilisation of the energy and resources of minority business communities.
- And the fourth, which is the key point of the paper, is that structural adjustment programmes have taken insufficient account of the regional dimension.

Expectations were too high: A lot of people thought that if you got the prices and the macro-framework right, growth would take-off in Africa. From the time of the Berg Report in 1980, it has been clear that, while you cannot develop if the prices are wrong, even if you get the prices right, you are still going to face all of the difficult, long-term development issues which were the bread and butter of development economics around the time of independence. In a sense, you are just getting back to where you started. But obviously there are a lot of people who had much higher expectations. *Poor design and experimentation:* There have been a lot of poorly designed adjustment programmes, particularly with regard to sequencing. I think that most people feel that we have been trying to use the lessons learnt elsewhere, but no doubt it comes across as experimentation at times. *Missing elements:* I think the main failure on the adjustment side has been a failure to achieve fiscal stabilisation. This is due, in large part, to a failure to redefine the role of the state and especially the role of state enterprises. *Regional dimension:* The regional dimension has not been

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a major factor, but it could play a role in improving the effectiveness of adjustment programmes.

The Bank and the Fund are frequently accused of giving either too much finance, or giving too little finance; financing programmes which are not owned, or not giving the benefit of the doubt; using a cookie-cutter approach, or being inconsistent. All of these can be true in particular cases, but I think it's difficult for them all to be true in general.

Coming now to the regional dimension, I agree with Alieu Jeng that there is a difference between a regional dimension and a regional approach. I don't think the paper suggests that we should negotiate a regional adjustment programme, but that we should be conscious of the regional implications of national structural adjustment programmes.

Fiscal policy has been weak in most of the adjustment programmes in Southern Africa. Lesotho has achieved stabilisation and sustainable fiscal balances in part because of its policy links with South Africa – it's locked into an agreement which forced it to achieve fiscal stabilisation. Mauritius has done it alone, and so has Zambia. The other countries, particularly Zimbabwe and Malawi, have not achieved fiscal adjustment.

What is the regional dimension here? I think that the question of harmonisation of tax and tariff legislation is certainly important, and regional cooperation in this harmonisation could facilitate adjustment and prevent the kinds of arbitrage discussed in the paper. On the other hand, trade integration may make fiscal adjustment more difficult because it implies an important loss of revenue for many of the countries, and that implies attention for tax reform.

I will leave most of the comments on *monetary and exchange rate policies* to Mohsin Khan, but I want to say that I question some of the comments made in the paper about the devaluation-induced inflationary spirals of, particularly, Angola, Mozambique and Zambia. First, most of those devaluations were simply bringing the official rate into line with a parallel rate to which much of the economy had already adjusted. Second, devaluation in most economies in Southern Africa has actually had a positive effect on the budget. And third, I would contest the statement that the devaluation/inflation cycle has created aid dependency. Devaluation and inflation are more often a reflection of dependency on large capital inflows to finance domestic imbalances.

On the issue of *debt and aid dependency*, we have to distinguish between gross and net flows of aid. In the case of Zambia, the agreed debt strategy is to defer the problem for the time being and employ stop-gap measures of high flows of balance of payments assistance to fund debt service as long as Zambia continues its adjustment efforts. There is no viable exit strategy at the moment for Zambia, but Zambia is the only country in Southern

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Africa which actually has a multilateral debt problem. This has prompted us to examine the multilateral debt issue. The Bank and Fund are working on this together, and we expect to present some proposals on this within the next few months. I agree that aid dependency is a major problem in Southern Africa, and that donors, African governments, and the Bank and the Fund need to be looking at a strategy for the excessive levels of aid transferred to Africa.

The paper argues for greater harmonisation of *exchange rate policyand* for using more fixed rates. Obviously, this argument occurs in most countries of the world, and it depends on making sure that countries actually converge on their other policies. It also has particular implications for the rate of the South African rand, because the rand would be the most likely anchor for most countries. If South Africa manages its affairs in its own interests, there can be a divergence of interests, as indeed there has been between Botswana and South Africa, leading Botswana to abandon parity with the rand.

Labour and wage policy have not typically featured in adjustment programme conditionality. The paper suggests that freeing-up labour markets could enhance labour flexibility in South Africa. I think this is true, but for that very reason, it will be a politically difficult thing to do. South African labour tends to resist trade policy integration, which would imply the movement of production of labour-intensive goods to neighbouring countries, the short-term loss of employment in some sectors, and migration of unskilled labour. It might be possible to convince the South African polity that the dangers of migration are so great that trade integration is necessary, but this would not be an easy thing to do.

With respect to the proposal for funding large-scale, employment-generating schemes for housing and other infrastructure in South Africa, we have done some modelling of restructuring of expenditures in South Africa, and concluded that if this is funded by external capital inflows, the employment effect is adverse because of the appreciation of the exchange rate which would result from funding predominantly local cost expenditures.

Regional cooperation is often taken to be synonymous with *trade integration.* I believe that regional trade integration can play an important role in economic development provided that the trading group is not predominantly inward-looking. Trade integration can facilitate development of infant industries, but if the ultimate aim is not to compete in the world economy, then the result of regional trade integration will be detrimental to development. In essence, we are talking about three issues: (i) how much protection and for how long? (ii) what additional measures can be taken to promote exports to the outside world consistent with the level of trade protection? and (iii) what countries are to be included. The World Bank supports trade integration and other forms of regional cooperation through the Cross-Border Initiative, but trade integration may not be the most important form of regional cooperation in Southern Africa. Cooperation in infrastructure investment and harmonisation of policies may be more important.

On *agricultural sector policy*, a lot can be done to harmonise regional policies, particularly in maize marketing and pricing. The proposal for land transfers to South African farmers is worrying because it seems to be based on a faulty premise that large-scale agriculture is more efficient than small-scale, and it gives too little regard to the political problems that arise such as the potential for abuse of land alienation.

State enterprise reform would indeed be easier to do on a regional basis, but you would face exactly the same issues, namely, if you privatise a state enterprise in Zambia or Malawi and it is bought by someone else in the region, it will still be perceived as foreign investment.

Finally, it is true that economic integration requires a vision, but outside organisations cannot provide that vision. The vision has to come from within Africa. International organisations can support African efforts at cooperation and integration, but they cannot use conditionality to insist that it takes place. This is not the role of international organisations.

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Floor Discussion of the Mistry Paper

Philip Clayton, an economist at the Standard Bank in South Africa, began the discussion with a plea for concrete action on regional integration. "We've been talking about regional integration for quite some time, and if forums and conferences led to economic growth, Southern Africa would be a world leader in economic growth and development. We should take the Nike slogan as our motto, 'Just do it!' The Southern African Development Community (SADC) has an economy approximately a third the size of the city of Los Angeles. The case for economic integration is clear, and we need to seize the opportunities to achieve the benefits.

We also need to make it easier for private sector firms to get involved in the region. Standard Bank has had some experience in doing business in Southern Africa, and we have found that there are many irksome things that make it difficult for business to grow across the region. These obstacles need to be addressed. The politicians must make decisions and implement those decisions at home. Free up the business community because they should be able to do a fair amount to make this region grow. We'd all like to see Southern Africa grow and develop, and we could all become richer at the same time."

Patrick Ncube, a consultant from South Africa, dwelled on the role of financial institutions. "There is such uneven development in financial sectors in the region. Four years ago, you couldn't even talk about the financial sector or financial institutions in Mozambique. The central bank was doing everything; it acted as a commercial bank, a development bank; everything. To move from that situation to creating a financial sector is a big step. And it is an even bigger step to develop financial institutions in Mozambique, Tanzania and Angola that are comparable to those of South Africa. How can we can deal with this extreme unevenness? Besides Zimbabwe and South Africa, most of the money markets is just the government selling treasury bills. So it is difficult to talk about money markets, let alone capital markets because they are completely non-existent.

With regard to the development banks in the COMESA/SADC region, I think that all of them have reached a checkmate position and that they should be scrapped. This particular question was raised at another meeting where the Chinese delegation suggested a moratorium on aid to Africa because the way we are going is completely ridiculous. I support that position, and I hope that the financial institutions will seriously consider this question of aid and aid dependence and our inability to use credit. The fact

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is that we don't understand the concept of credit – we take credit and then we go and ask for forgiveness. This type of behaviour cannot continue."

Sam Asante, from the UN Economic Commission for Africa, praised Mistry for bringing the two key issues of adjustment and regional integration together in his paper. He then focussed on Jeng's comment regarding the position of South Africa. "Sometimes we seem to see South Africa as a country with one-way traffic to the Southern African region or the rest of Africa. I find this incredible because it's a two-way street. There are a number of things that South Africa needs and the rest of Africa has. So we have to be careful when we talk about South Africa as if it is a self-sufficient entity.

Another issue is how to design and negotiate the regional dimension of adjustment. In fact, negotiating is an impossibility. How can one apportion the amount of money provided by the World Bank for sustaining the implementation of adjustment in each individual country?

An additional question is: will adjustment contribute to or hinder regional integration? This issue requires careful examination because structural adjustment is focused on the country level. There is simply nothing like regional structural adjustment. As a matter of fact, when I examine the impact of structural adjustment on regionalism, the results have been more than chaotic because in Africa, our borders are very porous. A devaluation undertaken by one country has an impact on the devaluation of the other. A clear case in point is the devaluation of the kelasi in Gambia which had a terrible impact on Senegal's relationship with Gambia. Nigeria devalued its currency on two occasions and this resulted in strained relations between Nigeria and Niger and also Benin. It seems to me that structural adjustment has had a deleterious impact on this whole question of regionalism in Africa.

There is also a central dilemma faced by African countries in that some parts of the liberalisation policies pursued under structural adjustment are incompatible with the objectives of promoting collective self-reliance through regionalism. This results because we have the tendency to reinforce rather than transcend Africa's historical role in the international division of labour. Regardless of which liberalisation aspects of structural adjustment you examine, you come to the conclusion that structural adjustment programmes won't be helping African countries in the same way as regionalism.

I don't think you can negotiate structural adjustment on a regional basis. I feel strongly that now that we all believe that regionalism is a key to African development, and if we strongly believe that structural adjustment can also contribute, then it becomes a major preoccupation of COMESA and SADC and other regional organisations to deal with the links between integration and adjustment."

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Dag Ehrenpreis, Chief Economist at SIDA, reacted to Ncube's remark about aid dependency. "There's no doubt that the issue of aid dependency is gaining exposure, also in donor circles. The concept of donor fatigue has been used a lot in recent years, and the aid dependency syndrome is, of course, part of that. Donors, and tax payers, want to see some results of their efforts. And after all, this year, things don't seem to be getting much better, although there are some moves in the right direction. But the problem of aid dependency is certainly getting worse over time. It's clear from a lot of studies that the closely connected issues of aid dependency and the debt overhang need to be resolved. As has been said, there needs to be an exit strategy.

However, I don't think it is possible for us as donors to say, 'Look, now we're tired of this, we've been doing this for too long' or, 'Aid dependency is just increasing; we'll stop tomorrow'. The Chinese may have said that, but it would create terrible consequences which we would not like to be associated with. On the other hand, we don't want to go on like this either. What do we do? We don't know yet. In the new SIDA, which has recently been set up as merged agencies in Sweden, we have commissioned a study of aid policy for the next twenty years under a project called 2015. One of the key issues that we're looking at is this issue of aid dependency and how to reduce it. It is also coming out as one of the main three topics being studied by a new scientific development advisory council that the Swedish Ministry for Development Cooperation has set up, with international expertise. So there's obviously a lot of concern and a lot of work going on in this field.

When one discusses this and the very modest results of the more than a decade of structural adjustment paradigm in Africa, one also needs to consider the issue of the deteriorating terms of trade in the last ten to fifteen years. The studies I have seen on the price development of the commodities that Africa exports reveal the longest and the deepest decline that has ever occurred, even compared to the Great Depression in the 1930s. This obviously has contributed to the lack of progress of structural adjustment programmes.

Benno Ndulu of the African Economic Research Consortium has examined the flow of aid to sub-Saharan Africa during the 1990s up until 1992. If one compares the net transfer figure to the terms of trade development, one sees an actual decline in the flow of finance including exports and aid. This problem of declining purchasing power of the African economies is a serious problem which explains part of the development problems and the increase in debt and aid dependency."

Ehrenpreis returned to the issue of the unevenness of liberalisation policies across the continent. "I expected an analysis of the issue of sequencing

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of trade liberalisation between neighbouring countries, particularly in the Southern African region. It is an obvious problem that trade liberalisation has occurred in – sometimes forced on – countries in an uneven manner and at different times so that those who had to do it first also suffered most in terms of de-industrialisation; this is the impression one gets at least. But the argument here, of course, is precisely that what is rational on a global basis applied to one country may result in consequences that are not optimal in the long run for that country – and indeed for the region as a whole. It might lead to closing-down companies which could have remained open if their main export markets had liberalised at the same time, particularly in the region.

There are obviously a lot of institutional and political economic factors which are restrictive to the adjustment programmes, and Percy makes a very powerful argument for including such factors much more systematically in the analysis behind these programmes, particularly the regional dimension. I view Percy's paper more as saying that one needs to consider the regional dimension in structural adjustment rather than advocating regional structural adjustment programmes as a whole which would, at this stage at least, be very difficult to carry out institutionally."

Mohsin Khan from the IMF explained how he had read Mistry's paper. "The first thing I did was to look at the bibliography; holding my breath while doing so and hoping that I was not referenced in any way and relieved to find I wasn't. Only then did I know that I could read it without the risk of being savaged. Percy is a master at polemical writing. You just have to get past the polemics – I've read a lot of Percy's papers and after a little bit of practice you can. My rule is, and you may wish to try it at some point, don't read the first paragraph or the last paragraph of each section and skip the footnotes. That way you will get the meat of the paper – and there is a lot of meat in this paper. In fact, I would even go as far as saying that there are sort of gems of brilliance in the ideas that are put forward, as always. I just want to make some general points about criticisms that come out of Percy's paper; and then a few additional points.

First of all, are structural adjustment programmes effective in achieving some notion of improvement in whatever variable you wish to look at? It is typically growth, but it may be productive capacity. There is a continuous debate, not only externally but internally as well, on the effectiveness of programmes. This is nothing new, and there are various statistical methodologies that have been put forward to assess effectiveness. No one is suggesting that we believe the programmes are effective everywhere all of the time. Clearly some programmes are unsuccessful in achieving their objectives. It may be that their objectives are too ambitious. This is often true. But even if you take some basic standard, they may not be leading to

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any appreciable improvement in the variables that you are trying to affect. Thus, they aren't successful, and they may even worsen things.

What could be the cause? Well, it could be design, it could be implementation or it could be exogenous factors such as terms of trade. I'm just categorising but these are the three basic possibilities.

In the operational side of the Fund, and certainly in the research side where I am, design issues are constantly on the table in order to figure out how we can improve the design of Fund programmes. Percy's paper raises the point that in design issues, you ought to be looking at the regional dimension, in other words, groups of countries. Even though you may not be able to negotiate with the group, because of legal restrictions, you may indeed think about the regional level when you negotiate a programme with an individual country. Maybe you ought to incorporate a regional dimension and look at neighbours and what they're doing when designing the programme for a country. It might then be wise, however, not to let the country know that you are looking at his neighbours as well.

Another example of a design issue has to do with sequencing. For quite some time, people talked about optimal sequencing. I can tell you that an awful lot of research has been expended on this idea of sequencing of policies. It is with some regret that I admit to having contributed to this discussion because, ultimately, it led to nothing. In the end, this whole debate about sequencing is, in my view, vacuous. It's a meaningless debate. Now we look at it more pragmatically. We propose a whole set of policies to a country and discuss them. The country's authorities make decisions on these policies as to what is feasible, institutionally and politically, and we consider the constraints. Whatever sequence emerges is, in fact, optimal. We can come up with a lot of nice theories of what should be done first and what should be the optimal sequence, but in the end the sequence will be determined in the negotiating process.

I have a few small points on the paper specifically. First of all, I buy into the argument about the neighbourhood effects because it intuitively makes sense. I do not, I hasten to add, buy into the Easterly Levine results. I think if you look carefully at the paper, the whole thing is being driven by the use of dummy variables and residuals. Percy is right. There's correlation and not causality, and I even have trouble accepting the correlation. Intuitively, it seems to make sense even though there are sufficient counter examples to this neighbourhood effect; the fact that Chile is doing great; Argentina only recently; Uruguay is not; Peru is just coming out. We don't have a theory of this neighbourhood effect but it may be right.

On the combined fiscal policies, Percy made the point that you should worry about fiscal coordination etc., but it is extraordinarily difficult to do. These are very tricky issues. It is even more difficult to do in monetary

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coordination. What you can do is fix the exchange rate between the two countries that you are concerned with, agree on fiscal targets, and monetary policy will then automatically be coordinated over time. But can you get agreement on fiscal deficit targets between countries? I think that is very difficult; macroeconomic management across countries is very difficult.

As for fixing the exchange rate, there is, as Gene Tidrick pointed out, an ongoing debate on this issue of fixed versus flexible. It's very tempting to say yes, fix the rate provided certain preconditions are met. In other words, you must have sufficient reserves to support the rate that you fix. And two, you have to have the fundamentals right. Again I'm going back to my point, you must agree on fiscal deficit targets; monetary policy is being driven by these two variables, the exchange rate and fiscal policy. If you've got your fundamentals right, then you fix the rate. This is a very appealing argument, and it has been made previously. But I think for developing countries to fix the rate for any length of time is extremely dangerous. These countries have massive shifts in their equilibrium real exchange rates, relative to industrial countries. Let's take the case of commodity price changes. All changes and tariffs affect the equilibrium ratio and the rate you fix. If you have a deterioration in commodity prices during that period, you will find that very soon your equilibrium real exchange rate is now depreciated and your actual rate is appreciated. Flexibility is probably the way for developing countries to go and not fixing, except if you are Angola, and you may wish to stabilise inflation suddenly. But for most developing countries, any long-run fixing will cause problems. Very few countries have been able to do that for long periods of time. Businessmen do not like high volatility of exchange rates and that may be an argument for intervention on the exchange rates, but it is not an argument for fixing."

It was suggested by Samuel Wangwe of the Economic and Social Research Foundation that SAPs are a special case of a broader issue. "We could just as easily call this paper 'Regional Dimensions of National Policy Making' and in the case of SAPs, it would still be valid. I think an important point is: To what extent does national policy making, whether it be SAPs or national plans, have a regional dimension? When we did the study on SADC, we looked at the national plans which were supposed to be the guiding instruments for policy making. We looked at all of the national plans in the nine countries, and there was no single plan which referred to the regional dimension. Aid dependency has worsened this neglect of the regional dimension in national policy making. Even when projects are not appropriate, the recipient accepts them in order to receive the aid.

If implementation doesn't work, it could come from two sources. One,

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we implement without being committed. Two, the programmes could be ill-designed. Unfortunately, because of aid dependency, we didn't question the design of the programmes and we didn't question the commitment to implement the programmes. So I agree with the thrust of this paper, but I would like to cast it in the broader context of national policy making and aid dependency, this being a special case of those two pillars."

Tekalign Gedamu, the former Vice President of the African Development Bank, challenged the participants to think in more concrete terms about pushing forward economic integration. "This subject has been discussed for the last 36 to 37 years. Some results have been obtained, but it's very clear from all the papers that have been presented at this meeting that the efforts that have gone into economic integration have not really produced commensurate results. I think in an area like this, progress comes in incremental steps. You cannot expect Africa to integrate by a particular year, the year 2000 or 2025. We should continue to make efforts which will push the process marginally, modestly, and each one of us should ask ourselves, 'What do we do at the end of this conference?'

There are useful suggestions in the papers which can be forwarded to policymakers and particularly to institutions which are in a position to promote the process of integration. I know the World Bank has said that there is not much they can do to promote economic integration through the conditionalities in the loans they provide to African countries, but there are institutions in Africa, in particular the African Development Bank, which have the mandate to promote economic integration in Africa through the financing of multinational projects.

With regard to concrete suggestions, first, Percy Mistry is the first to say that his ideas are still at a preliminary stage. What do we do to with his suggestion of viewing structural adjustment programmes in a regional context in order to accelerate the process of integration? I believe that an institution like the AfDB has a duty to pick up ideas like this and carry the process forward. It is established, and it is mandated to do this kind of thing; it has the financial instruments to carry out studies to more advanced stages. I believe we could promote the process of economic harmonisation and integration by picking on some of the useful ideas which have been made during this meeting and passing them on to institutions which are in a position to implement them in collaboration with groups of governments or individual governments."

Alieu Jeng from the African Development Bank supported Gedamu's plea for concrete action, and then turned to the issue of design raised by Khan. "With regard to designing a regional dimension in the structural adjustment programme, it's fine, but I don't think it is wise not to inform the country that you are looking at his neighbour's performance as well.

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We should want to ensure that Uganda knows that the name of the game is regional dimension of structural adjustment and that you are going to look at what is happening in Kenya or in Tanzania as well. This is something we have to state very clearly. You don't design programmes by yourself without the country being aware of what the parameters are. If you do, you end up with a programme that is not really home-grown, and ownership becomes a problem for a programme like that."

Edward Tiagha from the UN Economic Commission for Africa followed up on Gedamu's concrete proposals saying he had drafted an action matrix for enhancing regional integration efforts in Africa. "In this action matrix, I have a column which deals with the policy issues that should be addressed by governments at a national level, actions by regional economic communities and NGOs and actions by external development agencies and the UN system."

Lynn Salinger, a senior economist from a US-based research institute pointed out some of the positive results from structural adjustment programmes in Francophone West Africa. "I admit that I too, have had a few doubts about the regional wisdom of some of the structural adjustment programmes, particularly in agriculture with which I've been associated. When you tell all three countries of the Magreb to increase citrus exports to Europe and you then realise that the common agriculture policy of the EU and the external tariff that they face would probably prevent all three of them from realising that objective, you start to have a few doubts. But as one of the few people here who has had some practical experience in Francophone West Africa and particularly in the agricultural sector, let me just remind you of some of the amazing things that have gone on in that part of this continent.

With regard to liberalisation of economies, in many instances we have eliminated official prices for commodities, disbanded marketing boards, privatised processing facilities, and gotten rid of import or export bans which were often arbitrarily imposed by governments. When I first started working on regional integration analysis, we were worried about a common external tariff vis-à-vis rice imports into the region; the region was being flooded by rice imports. Today, what are we working on? We're talking about promoting Malian rice exports into the region. You have trade flows that are now viable from the Sahel to the coast and back up again. So let's not kid ourselves that the last ten years have produced nothing of value.

Of course, I understand that there are numerous research issues which remain to be explored, amongst which I might just cite political economy of multilateral development bank relations with countries. If we're honest with ourselves and we look at the evaluations that have been done of

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adjustment programmes in various countries, we realise that the conditionalities were not always upheld. We need to think about implementation therefore and not just about the design of reform programmes.

One issue I would put out on the research agenda has to do with revenue generation in Africa. Let's face it, most of the governments in sub-Saharan Africa are extraordinarily dependent on trade taxes and yet those same taxes have nefarious effects on the incentives regime for producers and traders.

To sum up, I would ask whether we would be here today insisting that the private sector come to the table and discuss regional integration with us if it hadn't been for the events of the last ten years? And my contribution to the concrete actions list would be that we agree not to hold another conference like this without first identifying the private business, and in some countries, the labour interest. They're intimately involved in deliberating these issues."

Patrick Ncube believed that the criticism directed at the World Bank and the IMF for the the poor design of structural adjustment programmes was misplaced. "As far as I'm concerned, there is nothing wrong with the Bank and the Fund. We have not elected the Bank and the Fund to safeguard the interests of the African people. We have elected individuals to public office who are supposed to safeguard the interests of the African people. If these people have failed, they should resign. The buck should not be shifted from these politicians back to the Bank and the Fund. Those who have been elected must take positions and try to protect the interests of the people rather than trying to blame outsiders."

Phakamani Hadebe, a deputy director at the South African Department of Finance, was not convinced that structural adjustment held any promise for the continent. "Percy, according to your paper, it still looks as if SAP is the only solution to the sub-Saharan Africa problem. Unfortunately, your paper then becomes an extension of a package that has already been used and proven to be a failure. Would you not agree with me that sub-Saharan Africa requires something different? Maybe if you can try and look at the domestic regional conditions, it would be a step forward.

A couple of years ago, an African alternative framework for structural adjustment analysed economic trends and the impact of structural adjustment in Africa. It was interesting that they came up with a conclusion that was totally different from that of the World Bank. They concluded that the weak-adjusting countries had done better than strong-adjusting countries. The reason was that the weak-adjusting countries had, to a certain extent, been able to mold the structural adjustment programme to their domestic needs. I ask you, therefore, shouldn't we try to come up with something more tangible.

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Maybe the problem is that Africans have not been vocal enough, but the African alternative framework tried to highlight these problems and I think they were ignored. Shouldn't we try to look at something else before we turn to integration because fusing regional integration to structural adjustment programmes won't win; I don't see it progressing. In fact, I don't see any positive outcome out of it."

Response by Percy Mistry

"Well, I think that at the end of an exhausting conference and the end of a particularly exhausting session, I would probably be thrown out if I attempted to answer all the questions that arose. I'll have to be selective in my response.

First of all in response to Gene Tidrick who said, by a process of *reductio ad absurdum* reasoning, that I was in favour of stronger conditionality. I think this statement needs to be more nuanced. I would have been in favour of stronger conditionality for much faster privatisation in particular areas; no question. But the whole issue of stronger or weaker conditionality and the issue of conditionality itself bothers me a great deal because in Africa in particular, conditionality is a mirror reflection of the degree of ownership, and conditionality is also dependent on design. Sometimes it's overdone because of expectations that implementation will not occur. In so many programmes that I've been intimately involved with, particularly in Zambia, Tanzania and – so far as design is concerned – Zimbabwe, there has been an unfortunate game being played. It's a political game of financial programming and financial upmanship. The Bank and the Fund start off being very reasonable about what the financial requirements for a particular set of adjustments will be, given the magnitude of adjustments that you want to see. At the end of the day, when you add the numbers up, you know it's politically impossible to raise that money, so all you do is go back and change your elasticities and come back with the same programme objectives, which is eminently unfinanceable. As a result of this, you have programmatic failure because of the way the game is played. In two projects that we did for SIDA, we have documented this, almost programme by programme, at least to the satisfaction of the people who've read the reports. So I know whereof I speak on that. In general, I don't think that one can characterise me as being in favour of stronger conditionality; it depends on the condition and the design.

On the issue raised by Alieu Jeng of regional dimension or regional approach, I would agree that it is attractive to think that Southern Africa might eventually have a structure amenable to a regional programme, but I think this is 'blue sky' thinking. What I have literally said in the paper is

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that when adjustment programmes in the different countries in the region are put together, it would behove the governments as well as the Bank and the IMF to ask, 'Supposing we were doing a regional adjustment programme, would these things fit?' Then they should negotiate national programmes which are regionally coherent. I prefer the term regional dimension, except in the case of sectoral investments where I deliberately use the term regional approach because I think a regional approach would actually yield better results.

With regard to SAPs, I keep hearing that we need something different than SAPs and we need something different than integration. Whatever you call it, there is absolutely no question in my mind that you need to transform production sub-structures. If Africa can come out with a better solution, go for it. Unfortunately, there has not yet been enough intellectual investment in African economics.

Patrick Ncube raised the point of good governments. I don't believe in unregulated markets; I don't think that governments need to withdraw. But the role of the state needs to change. As for the nature of that change, I think it depends very much on the country's case or the regional case.

Sam Wangwe's point about this suicidal scorpion dance that donors and recipients have gotten themselves locked into is a valid one. They're unwilling to break out of this embrace because it is damaging to them both – yet they know they must break out of it.

On the points that Dag Ehrenpreis made, I agree with just about everything he has said. I would only add some nuance to his point about Africa's vulnerability in terms of trade. The question to me is, 'Why does Africa's production structure remain so static that it is still the most highly vulnerable region in the world in terms of trade?' After thirty five years, at least this should have changed. I think everybody is at fault, but I agree with Patrick, the primary fault lies with the Africans for not asking more of the Bank and the Fund when expected progress was not made.

There was one other issue that Mohsin Khan raised which I disagree with. The distinction between design and implementation is not quite discrete as it appears. The sad part is that many of these adjustment programmes are designed by people who haven't a clue how to manage a national economy. This ivory tower mentality of Washington, that what happens to people is really a problem for politicians and not for them is something that needs to change.

I hope that just as my multilateral debt paper (published by Fondad in early 1994) started an avalanche which I hadn't quite predicted, that this paper will start a similar avalanche with people thinking about the connections between adjustment and integration which seem to be very powerful indeed."

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Appendix

List of Participants in the Seminar on Regional Economic Integration and Global Economic Cooperation: The Case of Africa, Midrand (Johannesburg), 7-8 February 1996.

Mr. Ernest Aryeetey	Senior Research Fellow, Institute of Statistical, Social and Economic Research, University of Ghana
Mr. Sam K. Asante	Senior Adviser on Regional Cooperation, UN Economic Commission for Africa
Mr. Werner Brummerhof	Head of the Economics Department, International Relations Division, South African Reserve Bank
Mr. Philip Clayton	Senior Economist, Standard Bank of South Africa
Mr. Zdeněk Drábek	Senior Adviser, Economic Research and Analysis, World Trade Organisation
Mr. Dag Ehrenpreis	Chief Economist, Department for Policy and Legal Issues, Swedish International Development Cooperation Agency
Mr. Uka I. Ezenwe	Professor of Economics, Department of Economics, Ahmadu Bello University, Zaria, Nigeria
Mr. Jeffrey Fine	Senior Economist, formerly with the International Development Research Centre, Canada
Mr. Tekalign Gedamu	Consultant, formerly Vice-President of the African Development Bank
Mr. Phakamani Hadebe	Deputy Director, Finance and Investment Sector, Department of Finance, South Africa
Mr. Björn Hettne	Coordinator, New Regionalism and International System Project, UN World Institute for Development Economics Research (WIDER)
Mr. Chris Heymans	Director, Centre for Policy and Information, Development Bank of Southern Africa
Mr. Faizel Ismail	Chief Director, Foreign Trade, Department of Trade and Industry, South Africa
Mr. Alieu Jeng	Principal Economist, Country Programmes Department, South Region, African Development Bank
Mr. Louis Kasekende	Executive Director, Research and Policy and Function, Bank of Uganda

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Mr. Mohsin Khan	Deputy Director, Research Department, International Monetary Fund
Ms. Bongi Kunene	Director, Finance and Investment Sector Coordinating Unit, Department of Finance, South Africa
Mr. Elty Links	Chief Director, International Development Finance, Department of Finance, South Africa
Mr. Hanri van Loggerenberg	Divisional Manager, International Relations Programme Division, Development Bank of Southern Africa
Mr. William Lyakurwa	Deputy Director, African Economic Research Consortium (AERC), Kenya
Mr. Gavin Maasdorp	Director, Economic Research Unit, University of Natal, South Africa
Mr. Michael Matsebula	Professor of Economics, Department of Economics, University of Swaziland
Mr. Colin McCarthy	Professor of Economics, Department of Economics, University of Stellenbosch, South Africa
Mr. Percy S. Mistry	Chairman, Oxford International Group
Mr. Patrick Ncube	Donsi Consultants, South Africa
Mr. Daniel B. Ndlela	Associate, Zimconsult, Zimbabwe
Mr. Sindiso Ngwenya	Senior Transport Expert, Common Market for Eastern and Southern Africa (COMESA)
Mr. Mfundo Nkuhlu	Director, Africa Trade, Department of Trade and Industry, South Africa
Mr. Bertil Odén	Coordinator, Southern Africa Programme, The Scandinavian Institute of African Studies, Uppsala, Sweden
Mr. Peter Robinson	Associate, Zimconsult, Zimbabwe
Mr. Paul Runge	Managing Director, Economic Development for Equatorial and Southern Africa, South Africa
Ms. B. Lynn Salinger	Senior Economist, Associates for International Resources and Development, USA
Mr. Jan Joost Teunissen	Director, Forum on Debt and Development
Ms. Rosalind Thomas	Associate Director and Policy Programme Manager, Development Bank of Southern Africa
Mr. Edward Tiagha	Regional Advisor in Industry and Technology Development, UN Economic Commission for Africa

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Mr. Gene Tidrick	Lead Economist, Southern Africa Department, The World Bank
Mr. Sam Tulya-Muhika	Director, International Development Consultants, Uganda
Mr. Samuel Wangwe	Executive Director, Economic and Social Research Foundation, Tanzania

Observers

Ms. Marie Helene Chavrimootoo	Second Secretary at the Mauritius High Commission
Mr. Dave Farrell	Manager, Operations, Standard Bank of South Africa
Mr. Emile van den Houte	Development Bank of Southern Africa
Mr. Alpheus Manghezi	Development Bank of Southern Africa
Mr. Elvis Sithole	Development Bank of Southern Africa