Development Centre Seminars

Regional Integration in Africa

INTERNATIONAL DEVELOPMENT

OECD

Preface by
Jorge Braga de Macedo and Omar Kabbaj

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AFRICAN DEVELOPMENT BANK

DEVELOPMENT CENTRE OF THE ORGANISATION
FOR ECONOMIC CO-OPERATION AND DEVELOPMENT

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Foreword

The first meeting of the International Forum on African Perspectives was convened by the African Development Bank and the OECD Development Centre in 2000 on the theme of "Reform and Growth". The chapters in this current volume relate to the second session of the Forum in March 2001 and form part of the Centre's work programme on the integration of developing countries into the world trading system.

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Preface

The nations of Africa are confronted not so much by the impact of globalisation as by their exclusion from it. Yet, despite the risks of which we have heard so much, an Africa delinked from the world economy is a continent condemned to marginalisation and stagnation. Some individual countries on the continent have attempted to engage themselves more into the world economy and they have had some success; others, however, seem powerless to do so.

The Second *International Forum on African Perspectives* explored the option of regional partnership and action as a way of uniting the forces of African countries in such a way that they might be able to enter the global market reinforced. While the idea of regional approaches in Africa is not new, past failures inject not just poignancy but caution into modern approaches to the problem. It is clear that regional groupings should not come about by willpower alone; rather, political will must facilitate a rational need. It is useless, for example, to attempt the creation or reform of regional institutions without domestic reform and adjustment. In order to reap the international benefits of reform, it is necessary to pay its domestic, economic and political cost.

Market reform is one particular imperative for African countries. It implies improved intra-regional market access, as well as international opening. Where domestic markets are distorted, regional mechanisms can help reduce that distortion through peer pressure and internationally co-ordinated reform policies. These same policies can demonstrate maturity and stability to external investors, thus encouraging inward FDI which is one of the stated objectives of regional integration initiatives in Africa. At the same time, the need for fiscal reform and the maximisation of tax receipts is an absolute necessity for African countries if they are able successfully to implement the levels of market opening required for integration into the world economy.

For most of the last decade, the international business community has unjustly perceived African countries as uniformly failing, and the principal form of financing has been official development assistance. This situation is untenable for all but the short term and the continent cannot remain outside the world economy.

Important initiatives have been taken to reduce indebtedness and to improve private and public governance, and the most important of the latter have been initiated by African countries themselves. With all the healthy caution we would counsel, regional concertation offers part of the solution to Africa's exclusion from the world economy. It may well provide the catalyst for continued economic and political reform throughout the continent so necessary for economic sustained development.

Jorge Braga de Macedo	Omar Kabbaj
President	President
OECD Development Centre	African Development Bank
Paris	Abidjan

April 2002

Introduction

Andrea Goldstein

In 2000, the need to establish a regular mechanism for analysis and dialogue on the growth prospects and policy challenges facing Africa led the OECD Development Centre and the African Development Bank (ADB) to launch the *International Forum on African Perspectives.* African countries are by no means immune from the profound changes that "globalisation" induces on forms of economic interactions and on the governance structures that are desired by governments and civil society. It will mean exposing individual economies more to international trade and trends; it will also offer new opportunities to each country of the continent. As the theme chosen for the Second Forum — "Regional Integration in Africa" — suggests, the considerable action required in this context should be at the country as well as at the regional and sub–regional levels. Regionalism can create a springboard for the process of economic liberalisation and progressive insertion into the global economy. In a world where production and flows of human and financial capital are increasingly taking place across national borders, Africa needs to find mechanisms to solve its riddle by implementing co–operative solutions.

The Forum provided a platform for the participants to debate if current efforts aimed at revamping the process of regional integration in Africa are succeeding in three key areas: *i)* overcoming major bottlenecks to growth; *ii)* addressing major distortions in the functioning of regional markets; and *iii)* promoting export diversification and high–quality integration into the world economy. This Introduction groups the debate under four headings: the relaunch of African regionalism, the implications that can be drawn from the Latin American experience in this domain, the results that can be achieved through co–operation and integration in non–trade areas, such as the improvement of physical and financial infrastructure, and the main challenges ahead.

Relaunching African Regionalism

While Africa has a long track record in regional integration initiatives, the results have been by and large rather disappointing. In their presentation, **Nureldin Hussain** and **Naceur Bourenane** showed that over the last decade, as an increasing number of countries timidly began opening up their economies and removing the most egregious barriers to investment and entrepreneurship, regional agreements have been revived. In the spirit of the Abuja Treaty, regional integration is seen as a strategy to face up to globalisation, while specific policy instruments have to be used to increase domestic capacity and further the national interest. While participation of the private sector is seen as key in this new phase, there is also a perception that the public sector must take the helm in creating an auspicious environment for regional initiatives to flourish and become sustainable.

Adrian Wood, in a speech delivered on behalf of **Clare Short**, argued that there is no need for Africa to choose between multilateralism and regionalism. These are not two conflicting strategies. On the contrary, in meeting the challenges of globalisation, regional integration and co–operation are vital complements to multilateralism. In other words, Africa should practice "open regionalism". Clearly, in the words of **Michael Spicer**, openness works partly because it sends out a signal about what sort of economy the liberalising state wants to have — one that is open not only to trade, but also to ideas, people, skills, and investment; one that wants to compete on a global stage; and one that stands for internationally–acceptable political values and social practices.

Complementary to this, according to **Koos Richelle**, is the necessity that countries in a region exercise ownership of regional activities from the outset. In this respect, more consistency must exist between the national level and the level of regional organisations in order to minimise the negative effects of the variability of economic policies pursued by partner states. One very important practical implication is that the PRSP (poverty reduction strategy papers) process should indeed take into account the regional dimension. On the basis of a careful reading of the history of the East African Community, **Jakaya M. Kikwete** argued that other requirements of successful integration include attention to a proportionate sharing of benefits of economic integration, introduction of adequate compensation mechanisms to redress the situation, creation of formal and informal fora of political discussion between member states, and participatory mechanisms for civil society and the private sector.

Various participants nonetheless cautioned against placing too high expectations on regionalism: according to **Sheila Page**, for instance, in small countries, small changes will give small numbers. Moreover, while Africa has to integrate to increase its chances of surviving external competition, the need to find a development path based on across–the–board opening to other regions and continents was also underlined. According to **Kiichiro Fukasaku**, the continent still compares unfavourably with other developing regions in terms of its unilateral liberalisation effort, partly because general tax collection remains weak and makes it difficult to reduce trade taxes. Moreover, said

Ademola Oyejide, the extent of trade liberalisation that could be ascribed to regional initiatives has been limited. This has also been changing quite rapidly, however. For instance, UEMOA has implemented a regional common external tariff (of four rates ranging from 0 to 20 per cent). It appears that CEMAC has implemented a similar process. In addition, COMESA has recently announced significant progress in the same direction. Moreover, since many countries have been reluctant reformers and poor performers in terms of growth, the weakest countries have often defined the agenda of regional negotiations. The possibility of using a variable geometry approach as a way to break the deadlock was cited by **Jorge Braga de Macedo**, as were the potential benefits deriving from multilateral surveillance in regional groupings.

Implications for Africa from Regional Integration in Latin America

In view of some of the failures of the reform process in Africa, including in the area of regional integration, there is a growing perception on the part of policy makers that a careful analysis of the experiences elsewhere in the developing world may potentially improve the quality of policies. So far most of the attention has been on the European integration model, where of course starting conditions were greatly different and where institutions were built top–down. On the other hand, according to **Andrea Goldstein** and **Carlos Quenan**, Latin America has adopted a different approach to regionalism, implementing policy changes in a relatively rapid manner and accompanying trade opening with a host of deep reforms in domestic economic policies. Another point that has characterised the Latin American experience in the 1990s has been the clarity of the goals assigned to regional integration, especially in the case of Mercosur, and the resulting lightness of the institutional framework governing it. These stand in stark contrast to Africa, where often unrealistic objectives have combined with a rather baroque structure of official bodies. Integration is more of a process than a goal in itself and political will is crucial, as proven in Mercosur by the fact that Brazil has served as the power engine — while, in the past at least, no country seemed capable of doing so in any of the major regional initiatives in Africa. Participants also highlighted the fact that regional bodies such as the Inter–American Development Bank and the UN Economic Commission for Latin America and the Caribbean have played a crucial role in articulating a coherent doctrine of open regionalism. The public and the private sectors in the EU, in Mercosur, and in Nafta have been complementary, but in none of these cases has there been an exclusive lead of either the public or the private sector.

However, the point in making the comparison between these two different continents is not so much in setting up Latin America as a model, as it is in drawing African policy makers' attention at an early stage to the challenges that the most advanced groupings are facing now and which Africa will also encounter in the near future. In particular, insofar as the measures implemented in Argentina at the time of the meeting might jeopardise the very existence of Mercosur, various participants, including **Marie–Christine Crosnies**, observed that African countries have to find

mechanisms to co–ordinate economic policies and to reduce vulnerability to external shock. **Paul Isenman** also highlighted that Mercosur has succeeded where previous efforts failed because its members were like–minded: the view they shared was "open". If a regional grouping has an avowed goal of openness, but members in fact are not much committed and have widely divergent views among and within countries, chances for success are highly limited. Lack of apparent quick returns, an understandable feeling of injustice *vis–à–vis* the world trading system, and aid dependency can add to those problems. **Rolf J. Langhammer** also stressed that Latin America has so far met with limited success in improving the quality of physical infrastructure so as to remove barriers to trade. Reforms and open regionalism have not been able to deliver sufficiently high growth rates to curb the "brain drain", a phenomenon which is common to Africa and Latin America. At the same time, it must also be borne in mind that conflict and famine are not as rife in Latin America as they are in Africa, so that crisis prevention and resolution is a matter of lower priority in the former.

Investing in Infrastructure and Strengthening Capital Markets

Africa's infrastructure is plagued by many problems that were nicely summarised by **Hilde F. Johnson**. Decisions on what and where to build were taken during the colonial period, with a focus on getting one or two primary commodities to the market transported to ports where they can be exported. Not surprisingly, many African countries remain highly dependent on a single export product and complementarities are few and far between. Infrastructure remains concentrated in urban areas, reflecting the priorities of urban elites, despite the fact that the rural poor constitutes 80 per cent of Africa's poor. Africa's infrastructure is also poorly maintained and expensive to operate, it suffers from the lack of private investment and participation, and new investment is often driven by concessional funding, either from international financial institutions or donor countries. Not surprisingly, then, investment in infrastructure can have very positive externalities on growth, especially in tourism, construction, and agriculture — sectors that, according to **Nazir Alli**, may account for 90 per cent of the jobs expected to be generated in South Africa over the next seven years.

W.T. Oshikoya and **M. Nureldin Hussain** analysed how the recognition that regional integration is a concept that extends beyond trade and production and that it must include a solid financial system and an efficient network of infrastructure has gained ground in the 1990s. With non–existent or poor infrastructure, agglomeration economies cannot be created. Examples of infrastructure projects that explicitly take the regional dimensions into account are the "economic corridors" in the Southern African Development Community, the West African Regional Stock Exchange in Abidjan, or Air Afrique. For all such initiatives to function, it is crucial for concepts such as governance and transparency to be given a real meaning and not to remain simply as wishful thinking. More needs to be learned about alternative strategies that could be pursued by African countries in responding to these challenges, not least to understand a quandary highlighted by **Shemmy C. Simuyemba**: other emerging regions like Eastern Europe and Latin America receive more investment than Africa despite

corruption risks that are no less serious. It is also important to use infrastructure development to help the informal sector participate in and benefit from the process of globalisation and liberalisation. On the basis of her own experience, **Hilde F. Johnson** stressed that civil society can be an extremely effective watchdog, looking on policy makers' shoulders and ensuring that they act in the interest of all stakeholders, thus improving the credibility of the whole process.

In all these areas there are some rather formidable hurdles to overcome. While investment is key in promoting integration, Africa is already financially linked to the world economy through a number of negative channels, including indebtedness, money laundering, and capital flight. Solving the debt crisis through innovative strategies such as the Highly Indebted Poor Countries (HIPC) Initiative is, therefore, a priority, especially in view of creating bond markets for financing long–term infrastructure projects. Secondly, growing global integration of financial markets reduces the need for national market places, especially in countries that are too small and poor to reach a minimum efficient scale in terms of turnover and liquidity. Yet, show **Keith Jefferis** and **Kennedy Mbekeani**, the home bias of investors risks excluding all but a few "blue chip" African corporations from major OECD financial markets. Regional markets may therefore carve a niche for themselves if they increase competition between different forms of financial intermediation, which is an important vector of market development. The experience of the West African Regional Stock Exchange in Abidjan, in particular, was presented by **Jean–Paul Gillet**. Moreover raising funds at the domestic level remains necessary for companies to issue shares in OECD stock exchanges. Another major problem derives from the lack of skills in many African countries. Heavy reliance on foreign consultants, technicians, and contractors weakens the sense of ownership of the projects and may perpetuate aid dependency. On a more positive note, it was mentioned that strong political will may create at least some prerequisites for deeper regional integration even before all necessary structural reforms are implemented in individual countries. One participant did, indeed, suggest using pension reform in Africa as a tool to deepen its capital markets in the way this has happened in some countries in Latin America.

Main Messages and the Road Ahead

A general consensus seemed to emerge during the Forum on the importance of creating a more positive and coherent interaction between domestic reform, regional initiatives, and structural adjustment policies. It is also becoming evident that globalisation cannot be distinguished from governance. What is happening in modern international economic relations is that the link between globalisation and governance has implications for all sorts of aspects of international economics. **Jorge Braga de Macedo** cited Development Centre research showing, among other things, that good, long–term foreign direct investment is discouraged by corruption; that portfolio investment is weak where the government of enterprises is poor; that sustained growth is compromised by undemocratic structures; that the relationship between governance and growth goes both ways.

Moreover, all agreed that it would be misleading to think that social policies can only tackle poverty, while macro–economic policies foster economic growth. Infrastructural development, for instance, has to be seen in the context of the international development goals of halving the number of people in absolute poverty in the world by 2015. In this context **Omar Kabbaj** noted that debt service obligations are currently twice as high as the development assistance outlays, so that opening global markets to African countries — by removing both trade impediments and all forms of subsidies, in textile and agriculture in particular — must proceed in parallel with efforts at improving the working of African markets.

Gradually, the *raison d'être* of regional integration seems to be changing, moving away from a mere process of intra–regional trade liberalisation to a vehicle for attracting foreign direct investment through confidence building. Regional collaboration can also help non–economic dimensions of national governance. **William Lyakurwa** observed that one of the few areas of co–operation in East Africa that weathered the storm of the collapse of the East African Community in 1977 was the co–operation among the East African universities through the Inter–University Council. The African Economic Research Consortium (AERC) is currently playing an important role creating capacity in the areas of research and training through networking and collaboration on what may be called knowledge integration.

Finally, in Africa more than elsewhere, wars and infectious diseases, particularly HIV/AIDS, pose a significant threat to human capital development, sustainable growth, and poverty reduction. The image of the continent, however, is very often worse than reality. There is a need to present a balanced view of achievements and difficulties in African economies, and to differentiate between countries, in order to counter the propensity of much of the media to sketch only grim pictures of the continent. **Omar Kabbaj** and **Jorge Braga de Macedo** took the opportunity to present joint work by the two institutions, in partnership with the European Union and African researchers, to provide this kind of fact–based analysis. The first edition of the *African Economic Outlook* was subsequently released in February 2002 at the Third International Forum on African Perspectives.

Part One

Understanding the Challenges

Regional Integration in Africa: Situation and Prospects

Naceur Bourenane

Experiences of economic co–operation and regional integration go as far back as the 1960s. Since independence, states have initiated with differing success, and with results always below expectations, a set of projects aimed at establishing the bases for regional entities. The purpose was multiple and went beyond the strict economic framework. More often than not, this was in keeping with the continuity of the struggle engaged by national liberation movements and was an illustration of the desire to break away from the colonial era for the construction of geographic entities that were economically viable and politically united. This is probably the reason for the discrepancies that have been observed between the official instruments and official discourse on the one hand, and the specific problems of community building on the other, be it the implementation of decisions or the attainment of set objectives.

The results have fallen short of expectations, suggesting a lack of political will among leaders and those in power. But this is a simplification and somewhat of an exaggeration in view of the circumstances of these efforts and of government ignorance of the economic players involved. These interests have their own aims and strategies and their support for government plans cannot be immediately taken for granted.

The purpose of this paper is not so much to measure these shortcomings and discrepancies, but rather to carry out a review of internal and external constraints that are linked to the environment in which the regional economic communities are to be established. The final objective of the exercise is to comprehend better the conditions enabling the success of on–going experiences, it being understood that we shall essentially focus on structural constraints, and in particular economic ones.

We have intentionally chosen to focus on certain experiences concerning the setting up of regional economic communities. In this regard, we shall not review the numerous initiatives of the last 40 years, some of which are of a political nature or even security–oriented, while others cover a sector of activity or a specific area.

We shall not, for example, consider groupings such as the Mano River Union (UFM) in West Africa, the Central African Economic Community (CAEC), the Central African Great Lakes Community (CAGLC) or the East African Community (EAC). Or more focused bodies, such as those trying to develop natural resources (the Niger Basin Authority) or boost trade and investment (the Regional Integration Facilitation Forum — RIFF — in East Africa and the Indian Ocean). We shall confine ourselves to a few of the most typical integration efforts that best illustrate the problems and limitations of building economic groupings. The examples chosen will enable us to assess the efforts under way and the future for building such communities.

This presentation will be centred around the following questions:

- What is the status of economic co–operation and regional integration in the major regional economic communities?
- What are the constraints to their development?
- What are the perspectives and conditions for an effective and rapid implementation of the construction projects proposed by the countries concerned?

Situation of Economic Co–operation and Regional Integration

Beyond the political determinants linked to the origins of national liberation movements, the most important regional integration accords and the setting up of regional economic communities initially translated the concern of countries to revamp local economic growth, by lifting the constraints of the narrowness of local markets, and enabling the realisation of economies of scale. On the whole, these initiatives slowed down in the 1980s, owing mainly to the effects of the global economic conjuncture, the internal economic situation of countries concerned and the kind of structural adjustment programmes implemented in them. The next decade was marked by a conspicuous revitalisation of the integration process accompanied by a change of approach. They expressed the will of the states to face up to the creation of a new world of integrated economic blocs providing a forum for negotiations depending on countries' membership in a large economic entity. In this way, integration became an additional reason for assertion in international negotiations. Such renewed interest is also partly the result of pressure from external partners. This concern for economic revival, renegotiation of position in the world economy and for attracting more aid money is the basis of integration accords and their amendment which resulted in the setting up of the following Regional Economic Communities (RECs): the Arab Maghreb Union (UMA), the ECOWAS (Economic Community of West African States), the Community of the States of Central Africa (CAEC), the Common Market for Eastern and Southern Africa (COMESA), and the SADC (Southern African Development Community) in Southern Africa. Although more particularly because of the ties linking them to a developed economy (the old colonial power, France), the West African Economic and Monetary Union (WAEMU) and the CEMAC (Central African Economic

Community) have been instituted on the same lines. These common concerns demonstrate a similitude of approach and will of the states to create free trade areas and form customs unions, set up consultative and decision–making bodies conferring to these community groupings the formal attributes of a union comparable in its external attributes to the European Union. The same thinking was probably behind schemes such as the RIFF.

The accords governing the creation of regional communities and their strengthening in Africa implicitly or explicitly still pursue the objectives of setting up largely integrated economies, the promotion of a fundamentally endogenous and self–sustained development, based on a collective and planned approach. The setting up of a free trade area as an intermediary phase in the constitution of a customs union is in this framework supposed to facilitate and guarantee a certain profitability of investment geared towards meeting internal requirements. Thus the problem would not be one of export promotion but the search for import substitution. Today, Africa's development partners on the contrary give priority to an approach based on the exploitation of existing comparative advantages and to changes in the world market, according to a pragmatic and flexible approach.

On the continental level, the Abuja Treaty is in line with this perspective. It provides for several phases, starting with the reinforcement of RECs to the setting up of an African Economic Community endowed with its very own mechanisms and institutions (one central bank, a monetary fund, a single currency etc.), passing through a stabilisation phase of tariff and non–tariff barriers, the creation of free trade areas and the putting in place of a customs union, which in time will give place to a continental customs union.

This commitment was confirmed by the final decision by African Heads of State to form an African Union, depending on ratification of the fundamental instruments by two–thirds of national parliaments foreseen in May 2001.

This union is the political foundation of the future African economic community. It also shows the preponderance of the political over the economic and thus an energetic approach to integration.

These gaps between the physical existence of economic and social constraints and projects for the setting up of community groupings on the one hand, and between the latter and the vision entertained by Africa's development partners with regard to economic co–operation and regional integration on the other, do not mean that ongoing experiences have failed. It helps to explain some of the delays that can be encountered in meeting the implementation schedules of integration programmes. It equally helps to understand why, within a context of a general scarcity of resources, certain initiatives or organisations continue to face difficulties, staying afloat only through help from host countries, or through external aid.

We shall examine the projects and achievements of selected experiences of community construction.

COMESA

The Common Market for Eastern and Southern Africa comprises 20 countries (Angola, Burundi, Comoros, Democratic Republic of Congo, Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Madagascar, Malawi, Mauritius, Namibia, Rwanda, Seychelles, Sudan, Swaziland, Zambia, Zimbabwe and Uganda). It pursues two major and immediate objectives, the putting in place of a customs union, as well as monetary and financial co–operation between its member states. It took over in December 1994 from a preferential trade zone, ZEP, which had more limited goals.

A free trade area was to be created by the year 2000 with a reduction of tariff barriers of about 80 per cent by 1996. Today the reduction level of these barriers is around 70 per cent. Only five countries have been able to attain 80 per cent. These results are largely due to the fact that customs duties are quite different from one country to the other. Their reduction in cases where they are already low has a direct impact on the level of revenue while the question of compensation for loss of revenue remains unsolved.

In 1994, the COMESA adopted the protocol on the rules of origin. According to this, all goods in which local inputs represent at least 35 per cent of the final value were considered as domestic products. This rate was brought down to 25 per cent for goods whose importance for economic development is recognised. Implementation has further proved complex and cumbersome and is awaiting further studies.

In principle, the COMESA countries should introduce a common external tariff in 2004. The rates should hover between 0 per cent for capital, 5 per cent for raw materials, 15 per cent for semi–processed products and 30 per cent for finished goods. Three years before coming into effect, major problems are still pending with no ready answer in sight. These concern the levels and sources of financing of compensation for loss of tax revenue, the *modus operandi* of the common external tariff (CET) and the categories of the goods concerned.

A monetary harmonisation programme was adopted in 1992 and comprises several phases: *i)* between 1992 and 1996, the putting in place of a clearing house with the abolition of all restrictions on internal trade in the region; *ii)* the utilisation of fluctuating exchange rates and adoption of measures that should ensure monetary stability and reduction of budget deficits; *iii)* between1997 and 2000, the lifting of all restrictions to the full convertibility of the different currencies; *iv)* beyond the year 2000, the setting up of a common monetary institution different from the central banks. This institution will be charged with co–ordinating monetary policies and preparing the creation of a single central bank and for the advent of a single currency in the long run (by 2020). The rate of implementing these decisions has been uneven. With the exception of countries belonging to the rand zone, as well as Ethiopia and Eritrea, the other countries have lifted restrictions to exchange rate liberalisation. At the same time, through the various economic reform programmes, some of the objectives of

financial stabilisation, reduction of budget deficits and review of fiscal policies have been attained or will be attained shortly. This led to the need to reorganise certain structures such as the clearing house which has lost its usefulness and, as proposed by a study, may be transformed into an export credit insurance institution.

With the support of some partners including the ADB, COMESA has also put in place a regional bank (the PTA Bank) specialised in trade promotion and financing development projects in member countries, giving priority to projects that should facilitate integration. The result seems quite mixed concerning the promotion of intra–regional trade and integrating projects. Multinational projects account for only 4 per cent of the total of those supported by the bank and loans hardly exceed 2 per cent. Trade financing has mainly concerned trade with the outside world

The most significant achievements have been the dismantling of non–tariff barriers, in particular the lifting of restrictions imposed on currency arrangements and related taxes, the abolition of import–export quotas and some easing of customs formalities. However, trade is impeded by various obstacles, in particular the uneven trade balance between countries which is a source of tension between countries and economic partners (this is the case particularly between Zambia and Zimbabwe regarding an export dispute over Zimbabwean wheat flour that is cheaper than that produced in Zambia).

This paper describes the performances of COMESA. It helps to measure the achievements, while pointing out the difficulties that exist in attaining the set objectives according to schedule. On the institutional plane much progress has been made. Beyond the signing of agreements and drafting of protocols, COMESA has developed instruments that should ensure a more effective monitoring of the outcomes of trade liberalisation and the full lifting of constraints to the circulation of goods and capital, particularly through the setting up of a data collection and analysis system. Thus ASYCUDA/Euro Trace (Automated System for Customs Data and Management), developed with EU assistance, helps to accelerate the processing of files and modernise the country's customs administration.

SADC

The Southern African Development Community is composed of 14 countries (Angola, Botswana, Democratic Republic of Congo, Lesotho, Malawi, Mauritius, Mozambique, Namibia, Seychelles, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe). It became a regional community in 1992 after several years of consultation among member countries. The major objective of SADC is the co–ordination, harmonisation and review of national policies and strategies for sustainable development; this includes in particular measures that should help in lifting all barriers and obstacles to the free movement of persons, goods and capital in the region.

Since its creation, the SADC has adopted various accords, especially concerning trade promotion. The trade issue continues to arouse many reserves and is the root of differences between the countries. The trade agreement envisaging the dismantling of tariffs by about 85 per cent in eight years was ratified by only 2/3 of member states, six years after its adoption by the Heads of State. Its entry into effect, planned for 2000, was postponed because of continuing negotiations. The problem of quotas and rule of origin is equally a bone of contention. Malawi half–heartedly gave way to pressure relating to the question of quotas affecting its textiles and clothing trade. Bilateral agreements are sometimes sources of complication within the Community. Thus, trade between Malawi and South Africa has been free from all tariff constraints since the beginning of the 1990s. However, making use of the principle of the rule of origin, South Africa decided to block the entry of textiles from Malawi by imposing duties and various penalties. The result was the immediate bankruptcy of several firms and the loss of nearly half the jobs created through this agreement (3 000 of 7 000 new jobs).

SADC activities have been largely dominated by institutional matters, in particular those relating to the regrouping and reorganisation of the various commissions that were in existence in the former SADCC, the centralisation of operations and setting up of an operational and autonomous secretariat. This task proved to be relatively difficult to carry out successfully. The differences concerned in particular the management of the various bodies of the Community. So it took five years of discussions to arrive at a compromise on security matters and as to who should head the body in charge of defence and security.

Concerning economic and financial policies, numerous obstacles remain, such as the harmonisation of taxation policies, in particular the revision of the system, but much progress has been made. For instance, this is the case with the harmonisation of the procedures used by the various money markets in view of their integration into a regional system. One of the areas where important headway was made was transport and communications. Thanks to private initiative, the recent Maputo Corridor project, currently underway, makes possible the furtherance of industrial, agricultural and trade activities and services on the highway linking Maputo in Mozambique to Gauteng in South Africa, for an amount exceeding $7 billion.

The particularity of this region is the existence of the Southern Africa Customs Union, which is over 100 years old. Founded in 1889, it is made up of South Africa, Botswana, Lesotho, Namibia and Swaziland. South Africa is the cornerstone of this union. The Board of Tariffs and Trade is the decision–making body regarding the common external tax and other taxes. The Union is backed by a monetary zone based on the rand and the key role is played by the Central Bank of South Africa.

Thus the SADC, endowed with undeniable assets to undertake a rapid integration process, not only with the help of its resources but also because of the dynamism of part of its private operators, seems to be dragging its feet about a determined approach; for instance, the integration by the different markets. It continues, in fact, to be dependent on the existence of the Southern Africa Customs Union whose interests

predominate particularly in international negotiations; bilateral agreements (between South Africa and its chosen partners) have priority over the others, thus the risks of polarisation and marginalisation between the "centre" made up of South Africa and the "periphery" formed by most of the other countries.

ECOWAS

The ECOWAS (Economic Community of West African States) is made up of 16 countries (Benin, Burkina Faso, Cape Verde, Côte d'Ivoire, Gambia, Ghana, Guinea, Guinea Bissau, Liberia, Mali, Mauritania, Niger, Nigeria, Senegal, Sierra Leone and Togo). Its purpose is the setting up of a "self sufficient" community by the formation of an "economic bloc with a single market, based on an economic and monetary union". It was within this framework that it was decided to establish a customs union by the year 2005 with a common external tariff and a common trade policy in which economic, financial and sectoral policies would be harmonised. The creation of a monetary zone is a top priority.

With regard to trade liberalisation, customs duties and taxes were supposed to have been eliminated by the year 2000, both for non–manufactured and industrial products. Fresh information indicates that most of the countries have adopted a common nomenclature for products, a prerequisite for the implementation of related decisions; the harmonisation of customs documents is also underway. Twelve countries already utilise the community's certificate of origin and 11 have adopted the customs nomenclature and customs declaration document. In all, five countries implement the provisions of the protocol relating to the transit of goods by land. At the same time, eight countries have lifted the barriers for non–manufactured products, while one country has lifted all barriers to industrial products. The common external tariff is still in the making.

This rate of performance renders unlikely the establishment of a free trade zone with a common external tariff by 2002. One of the problems confronting the community remains the high cost of compensation for loss of tax revenue. Solutions have been envisaged. However, contributions to the compensation fund for losses (called the solidarity fund since March 2001) remain inadequate and too partial to enable the mechanism to play its role fully. In fact, only three countries have met all or part of their obligations. It is worth noting that like the COMESA, the ECOWAS has developed a system that should speed up the processing of customs documents and the modernisation of customs administration, ASYCUDA/Euro Trace. Another difficulty is the coexistence within ECOWAS of two set–ups, the Community and that of countries belonging to the West African Economic and Monetary Union.

Concerning monetary co–operation and the creation of a monetary zone, a first step has been made with the decision by 12 of the 16 countries to eliminate all non–tariff barriers of a monetary nature. Thus, nationals of these countries could pay their airport taxes, settle their hotel bills and purchase their air tickets in local currency.

Macroeconomic convergence is another area where some progress has been made. Whether it concerns budget deficit, its financing by central banks or inflation control, advances have been made. Many countries should be able to meet the preliminary criteria of convergence by the year 2003 (budget deficit contained at less than 4 per cent, inflation rate at 5 per cent: budget deficit financing at a maximum of 10 per cent of financial resources of the previous fiscal year, and reserves accounting for at least six months of imports). The question still pending is that of the formulation of national programmes for convergence, the follow–up mechanism and the resulting sanctions against countries that fail to abide by the set criteria. The non–CFA countries have decided to set up a monetary zone by 2003, the objective of which is to form a merger of the two monetary zones a year later. This timetable seems unrealistic. On banking, ECOWAS through its fund is the major shareholder of a regional commercial bank, ECOBANK, set up with private capital and established in 11 countries in the region.

The ECOWAS region is probably one that has recorded the most significant achievements regarding the free movement of persons. Indeed nationals of this region move freely from one place to the other without visas. However, problems do exist. Visas have been abolished, but a large number of checkpoints are sources of all sorts of harassment for travellers. They include seven checkpoints every 100 kms on the Lagos–Abidjan highway. National committees have been created to monitor the implementation of the decisions concerning the movements of persons and vehicles; but they have so far failed to do this. A solution seems to be emerging through co–operation with professional trucking organisations.

With regard to infrastructure (road network and telecommunications development) considerable progress has been made. Concerning the road networks, the realisation rate of the coastal highway and the Sahelian road network stands at 83 per cent and 70 per cent respectively. Phase 1 of the INTELCOM project has made it possible to connect the different capitals in the region. This should be accelerated with additional projects, such as the generalised use of fibre optic cables and connection by satellite. Regarding energy, headway has been made in power connections in the region. Liberalisation of air transport, planned for 2002, should also help speed up integration.

As is the case with the COMESA, the most significant results have been those concerning organisational matters with the drafting of protocols and conduct of studies that should help in carrying out decisions taken.

WAEMU

The West African Economic and Monetary Union is composed of eight countries (Benin, Burkina Faso, Côte d'Ivoire, Guinea Bissau, Mali, Niger, Senegal and Togo). and was formed by the merger of two bodies — the West African Monetary Union and the West African Economic Community — each with the same member countries. At

its inception in 1994, the prime objectives of this institution were to strengthen the international competitivity of the economic and financial activities of its member states; see to it that there was convergence in their economic policies; set up a common market based on the free movement of persons, goods and services, and capital, on the right of establishment, on the CET and a common trade policy; harmonise fiscal policies and co–ordinate the sectoral policies of its member states. The WAEMU will also establish a community investments code. Included in the institution's objectives were the putting in place of an accounts tribunal, a law court, a parliament as well as a regional chamber of commerce. The states also adopted a macroeconomic convergence pact, the implementation of which is matched with a supervision mechanism and an implementation schedule.

The particularity of the WAEMU is that it is within a monetary zone backed by an external convertible currency (the euro). It has a central bank, the Central Bank of West African States (BCEAO), which centralises all exchange reserves of its member states and is governed by a single monetary policy. Capital circulates freely within this zone; in principle assets are convertible as the CFAF is backed by France through a special operations account directly administered by the French Treasury. But having a common currency has not boosted trade between member countries.

Regarding its achievements, the WAEMU appears to be the institution that has succeeded in attaining the objectives set at the outset. The CET was adopted in 1997 and the effective putting in place of the taxation mechanism complementing this was undertaken in 1999 (the sliding protection tax to compensate tariff protection decreases and special import tax that should help to compensate tariff protection decreases linked to the fluctuations of world prices). Available information does not make it possible to say if all the decisions have been carried out but it shows that countries are committed to lifting the constraints to their implementation. These concern in particular the provisions concerning the CET and compliance with first and second rank criteria of convergence (base budget balance in percentage of GDP, inflation rate, debt burden; wage bill over income tax; investments from domestic resources as against tax revenue; current external deficit excluding grants over GDP) for which the supervision mechanism operates relatively well. Furthermore, real efforts have been to harmonise tax legislation. In all these areas, steps have been taken by most states to attain set objectives. However, compliance with Community rules and decisions, particularly concerning public finance (adjustment of expenditure to revenue, budget deficit control, control of arrears payments due to the Central Bank) largely depends on the international situation, reflecting the region's economic fragility. It is also the result of reform programmes devised and implemented by individual countries without any consultation with partner states.

The WAEMU has a regional development bank, the West African Development Bank (WADB) whose purpose is the financing of projects considered a priority to further the economic development of member states and foster their integration. Like the PTA Bank within the COMESA, the capital of the WADB includes external

shareholders, in particular France and the African Development Bank. However, unlike the PTA Bank, its financing for integrating projects is far more important. They account for more than 30 per cent of net cumulated commitments. Its commitments to the private sector should also be underlined. They account for more than a third of commitments since the beginning of operations in 1976, are on the increase and were nearly half of the bank's loans in 1999. They have made possible the financing of regional ventures.

CEMAC

The Central African Economic and Monetary Community comprises six countries (Cameroon, Central African Republic, Congo, Equatorial Guinea, Gabon and Chad). At its inception in 1998, the aim of the CEMAC, like the Customs Union of Central African States that it replaced, was to further economic development through the setting up of a customs union to guarantee the free movement of persons, goods and services, and capital. Like the WAEMU, the CEMAC fits into a monetary zone with a currency backed by a strong foreign currency, the euro, within the framework of agreements linking member countries of the Union to France. The Bank of Central African States (BEAC) carries out the same functions as the BCEAO (Central Bank of West African States) within the WAEMU.

The CEMAC has adopted a set of instruments similar to those adopted by the WAEMU. Their implementation has run into the same difficulties and is at the same level of execution. Thus, the taxation and customs reform – with the introduction of a common external tariff, a generalised preferential tariff and a turnover tax to replace the various indirect taxes – is near completion because it has been taken into account in the economic reform programmes undertaken with the help of international institutions including the ADB. The new tax and customs system replaces a complex system whose elements (single tax, turnover tax, exceptional exemptions etc.) had produced unexpected effects, contributing largely to the reduction of intra–regional trade. So a single currency and the possibility of free movement of capital did not in this case help foster trade. Furthermore, unlike the WAEMU, there are limitations to the movement of persons within the Union.

UMA

The Arab Maghreb Union is made up of five countries (Algeria, Morocco, Mauritania, Libya and Tunisia). This organisation, created in 1989, aimed at setting up a common market by the year 2000. For the past years, political differences have led to a halt in activities. It should however be emphasised that numerous bilateral

agreements between member countries have helped in some way to address this situation; especially with regard to the movement of persons and to a lesser degree that of goods and services.

Achievements in terms of economic co–operation and regional integration preceded the creation of the UMA. Road and rail networks link most parts of the different member countries. The electricity network is highly integrated between the three countries at the centre of the Maghreb: Morocco, Algeria and Tunisia.

Constraints to Economic Co–operation and Regional Integration

The above study of the different sub–regional experiences illustrates that contrary to established opinions, significant strides have been made during the past decade. They could be considered as limited when compared to set objectives and schedules. They would all be less limited if due regard were given to the internal and external conditions in which such projects are implemented. A particular aspect that has made great progress is the organisational and regulatory aspect. Unlike previous decades, substantial efforts have been made with respect to elaboration, based on precise and detailed studies often with the support of development partners such as the European Union and the ADB and on a series of decisions and instruments likely to foster rapid action and the parallel creation of follow–up and assessment mechanisms, especially with trade. This initial conclusion makes it possible to put in context any scepticism, arising from knowledge that the aim was to set up by the year 2000 economic norms or common markets within which production factors would move freely.

If it is admitted that regulatory constraints have been or could be lifted through the studies and work carried out within the communities, it is necessary to come back to the other factors that impede or delay the application of decisions taken. At the same time, the questions posed are why in regions where the mechanisms for market integration could fully play their part, the economic situation remains fragile and why economic co–operation has not produced the expected impact in terms of integration and a significant revival of growth, including in areas where the existence of a single currency could have been a key element.

Six groups of constraints will be distinguished, though this is just to facilitate the discussions, as the constraints are intricately linked and largely determine the integration process: *i)* infrastructural constraints, and *ii)* institutional constraints, which refer to organisational matters and choice of economic policies; *iii)* constraints linked to the country's economic structures; *iv)* those concerning the international environment and its changes; and *v)* constraints linked to the players involved and their strategies; and *vi)* conflicts.

Infrastructural Constraints

Numerous studies and analyses conducted on the question of community building underline the incomplete nature of communication and transport networks at the regional level. They illustrate many cases, particularly in landlocked countries, of the isolation of entire regions that could form the basis of meaningful cross–border development. This is widely recognised and (as for their Member States) is often addressed by Regional Economic Communities (RECs) whose major concern is to lift this physical constraint to the movement of goods and persons. The development of roads and telecommunications, linking up electricity networks and making use of shared natural resources is seen as the most basic kind of regional co–operation and the first requirement for integration. It is perhaps the easiest constraint to remove because it does not directly affect national sovereignty or state revenues.

Institutional Constraints

Among the major institutional constraints are first and foremost the way the RECs are organised and work. Apart from the fact that intergovernmental institutions are often seen as mere extensions of national structures without any real authority or autonomy, they are often restricted by their low technical capacities. In addition, given the scope of their missions the profile of available personnel often hired on the basis of country quotas or recommended by governments even though they are not qualified to do the jobs leads to inefficiencies. The second constraint to regional construction concerns the high number of intergovernmental institutions that are often costly and cumbersome. Once set up, they become difficult to abolish or even be held to account for their activities. The third constraint is the membership of several countries in various organisations pursuing similar objectives, but according to different procedures and schedules which ultimately lead to conflicting decisions. This is the case with some COMESA countries that are also members of the SADC, that are concerned by two different projects (or even three or four, if measures by the RIFF and the East African Community are counted), or the establishment of free trade areas that adhere to two customs duties reduction facilities with all the implications in terms of management and related costs. The fourth constraint is the absence of co–ordination of economic, financial and social policies and non–compliance with commitments made. Perceived as one of the common features of past community building in the 1970s and 1980s, this fact is still topical because of the urgency of the problems that states have to deal with at the national level and the prevalence of a short–term rather than a medium or long–term approach in government strategies, largely because of the nature of the adjustment programmes applied. Furthermore, the effects of mismanagement in many countries until the middle of the past decade have still not been alleviated. Financial imbalances and substantial disinvestment that went hand in hand with an increased external debt have, among other things, resulted in the increase of country risk. The consequences in terms of access to external financing are well known. The scarcity of

resources has meant giving high priority to national objectives. States were inclined to fail in meeting their commitments, in the payment of their contributions as well as in the application of decisions taken together and which could lead to losses for one of the states or for an influential component. This is the case with the CEMAC and the COMESA, where the redistribution mechanisms do not always work and where additional taxes have sometimes been introduced in order to compensate for revenue shortfalls. A decision of quite a different nature, taken by Côte d'Ivoire without consulting neighbouring countries, is an illustration of short–sighted management taking account of implications for the movement of the products concerned. To cope with its cashflow problems, Côte d'Ivoire decided to increase the import tax on cocoa by 60 per cent for cocoa beans, and this rate could rise to 200 per cent for by–products, corresponding to a 40 per cent increase of direct tax on the producer. But effective regulation of production and movement of cocoa reaches beyond national borders.

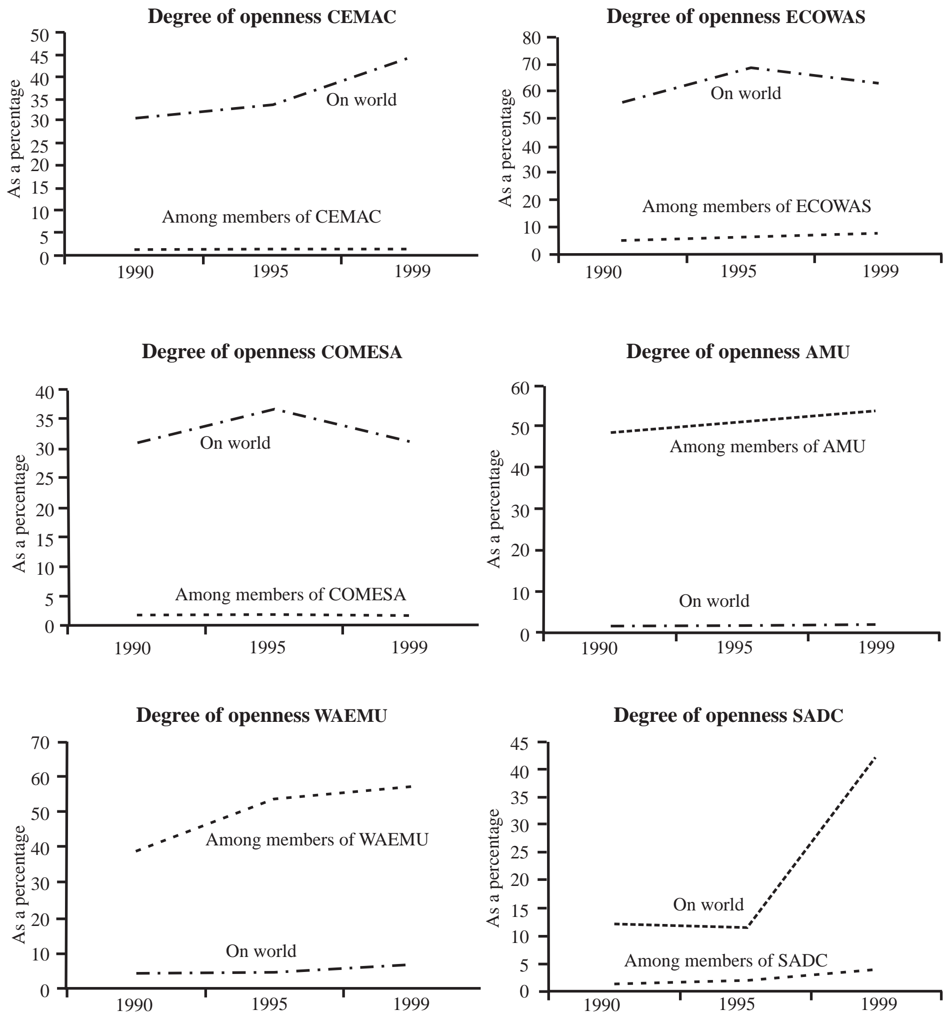
Structural Constraints

Among factors impeding efforts at economic co–operation and regional integration are the low or inexistent complementarity in the supply of goods and services and of capital and expertise, considering the similarity of demand. With a few exceptions, the various RECs are characterised by a poor diversification of production systems and the similarity of goods produced for local markets. At the same time, there is a strong similarity of supply destined for export. Countries within the same region in general draw their external revenues from the export of two or three basic products, accounting in most cases for more than 70 per cent of export earnings — state tax revenue and money to meet external payments. In this case, it is in the interest of the states and partners to promote exports to countries outside the region. This explains the contrasting development of intra–regional trade and that with the outside world (see figures concerning the level of market opening and trade evolution within the RECs in the last decade).

In this regard, if the different economic reform programmes have contributed, thanks to budgetary discipline and strict macroeconomic management that were introduced, to restoring financial equilibrium and a degree of country credibility, the priority they have given export promotion under the existing comparative advantages rule increased the tendency of the international level to prevail over the regional. These programmes have also contributed to developing neighbouring economies by setting up un–articulated programmes with no regard for the regional setting, or the implications of measures taken, or the order or timing of their implementation. The second main constraint is the weakness of purchasing power in the region. With such low income levels, building regional organisations seems secondary, even risky.

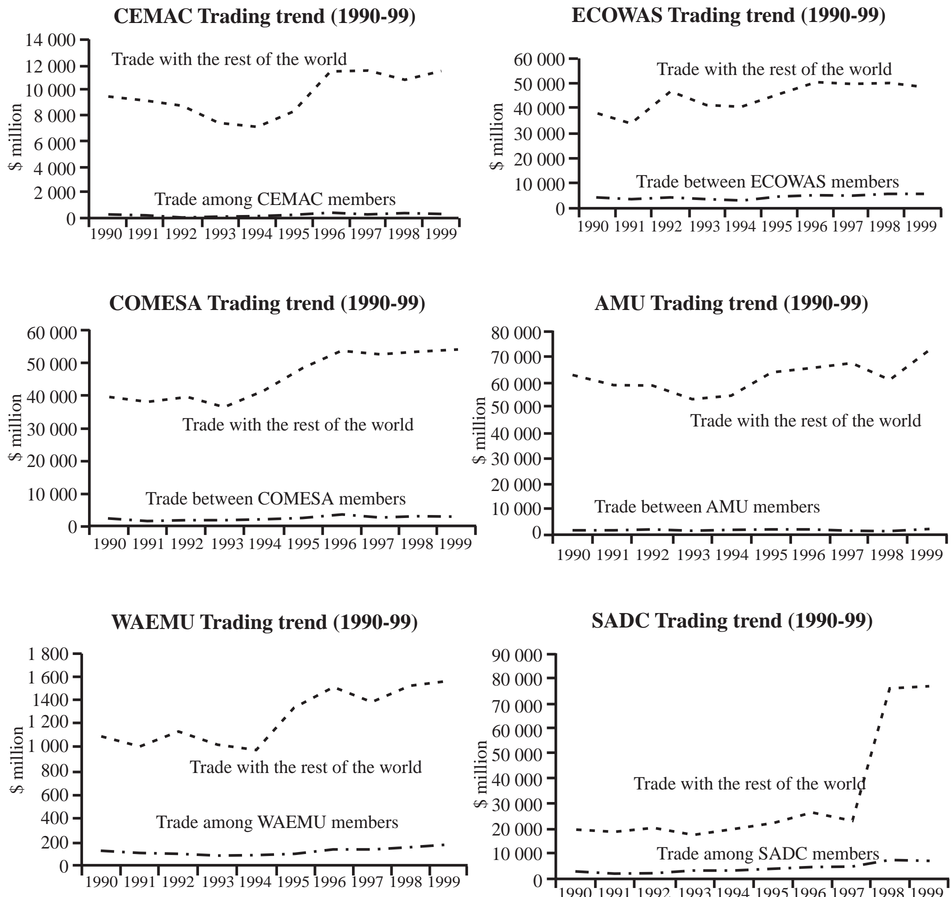
The updated figures from the early 1960s for six EU countries (Germany, Belgium, France, Italy, Luxembourg and the Netherlands), given here for comparison, show the income levels of these countries before they began uniting in a community.

Figure 1. **Degree of Openness**



Source: Drawn from IMF Data (World Economic Outlook).

Figure 2. **Trading Trends, 1990-99**



Source: Drawn from IMF Data (World Economic Outlook).

Table 1. **Average GDP and Average Population (1995-99)**

	Average GDP ($ million)	Average Population (million)	GDP per capita $/inhabitant
ECOWAS	76 093	205.9	357.0
CEMAC	19 098	28.7	669.5
COMESA	142 062	324.2	438.2
SADC	193 118	185.4	1 041.8
WAEMU	26 293	65.1	402.9
AMU[a]	107 414	73.2	1 467.6
EEC Member Countries[b] (1963-66)	1 459 968	180.8	8 074.0

a. Libya is not included owing to insufficient data on the period.
b. Average updated GDP using the growth rate of consumer price indices over the 1966-1999 period.

As the figures below illustrate, except for one region (COMESA) which shows some improvement, purchasing power in all the others has fallen over the past 20 years. Even in COMESA's case, the revival came only five years ago.

The limited nature of local resources seem all the more constraining when changing financial flows to different regions are taken into account.

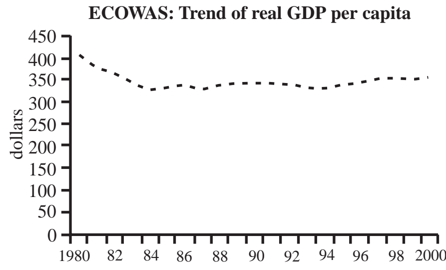
With limited domestic resources, declining financial flows and governments grappling with large budget deficits, investment in integration projects inevitably becomes a secondary matter.

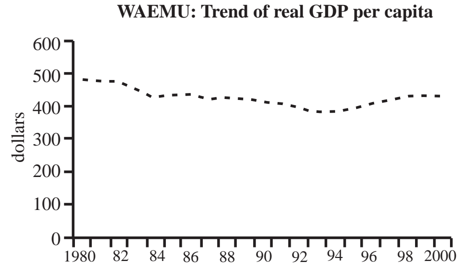
Indeed, gaps in status of wealth and investments favour, in most cases, asymmetric integration, unfavourable to poorer countries and to deprived groups within these structures. This is particularly the case within the WAEMU, between coastal and landlocked countries (involving export of labour, formal and informal taxation of produce from landlocked countries, surcharges on transit from the ports). This is also the case in Southern Africa between South Africa and its neighbours that depend on it for exporting their goods (in particular Malawi).

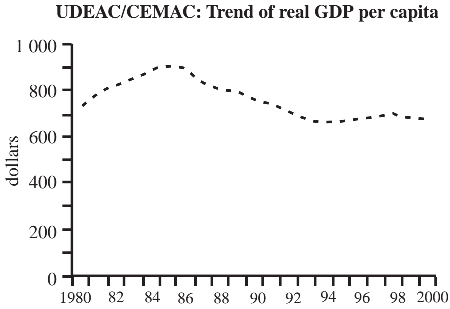
In this context, the question of compensation for loss of tax revenue linked to the establishment of a free trade area becomes more and more crucial. The third constraint concerns the reconversion cost of economic activities at the external level for the benefit of the region.

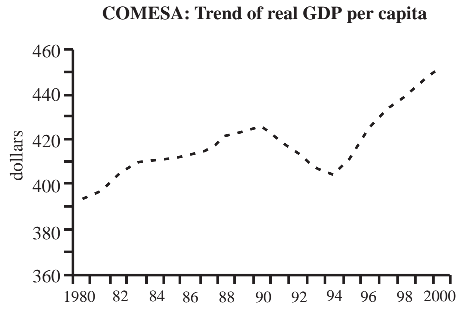
In a setting marked by a host of constraints linked to the costs of infrastructure to be set up in order to profit from a potential market, the costs of these markets and the multiple problems that economic players may encounter because of the absence of transparency in business management, operating from the outside world may be more favourable and less risky, or even more advantageous financially. So, owing to the structure of African economies, trade liberalisation and the setting up of common markets does not automatically lead to a significant increase in the volume of trade, or in that of investments.

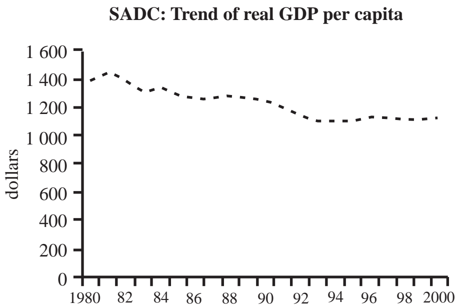
Figure 3. **Trend of Real GDP per Capita (1980-2000)**

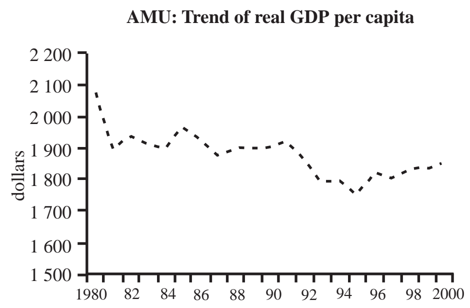






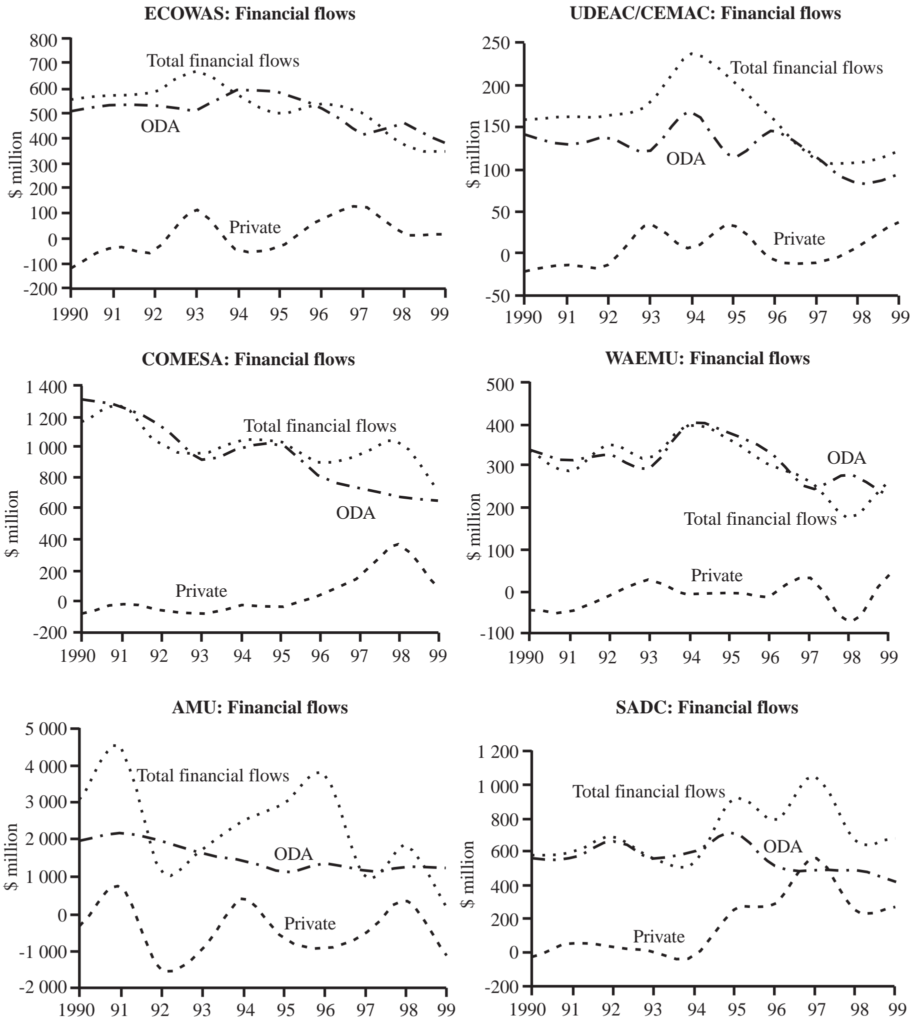






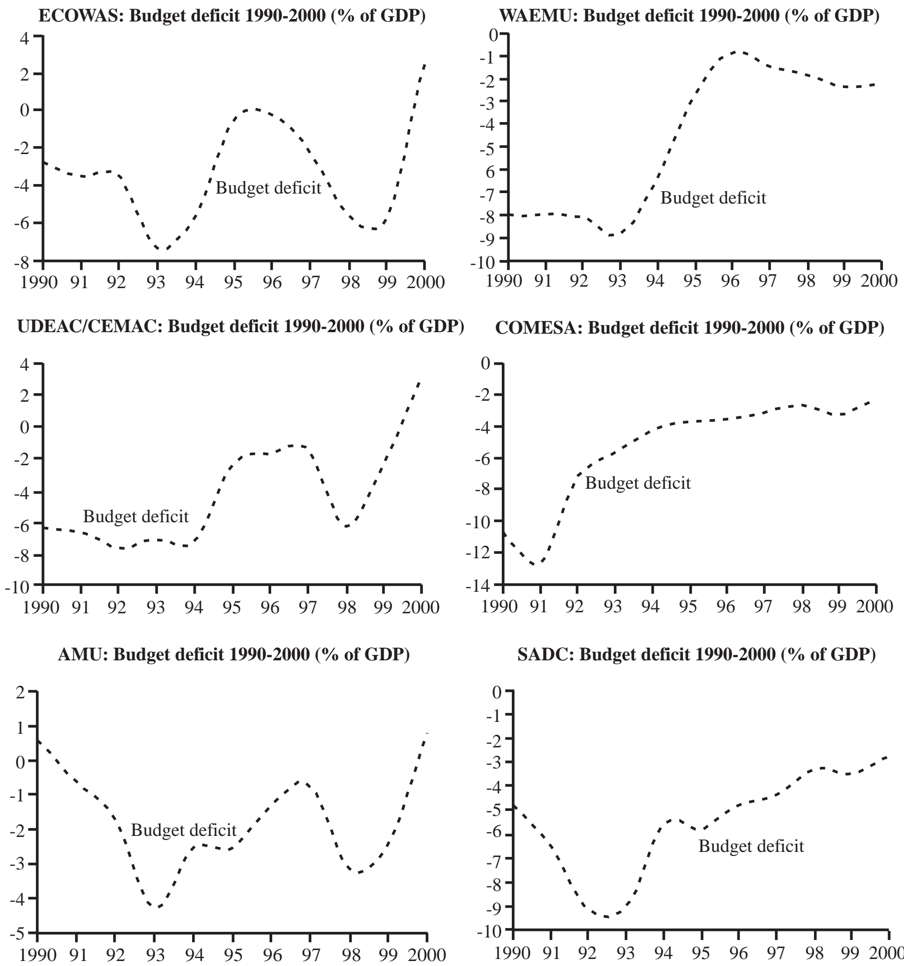
Source: Statistics Division, African Development Bank.

Figure 4. **Financial Flows (1990-99)**



Source: IMF Data (World Economic Outlook).

Figure 5. **Budget Deficits (1990-2000)**



Source: IMF Data (World Economic Outlook).

Figure 6. **GDP Structure (1995-99)**

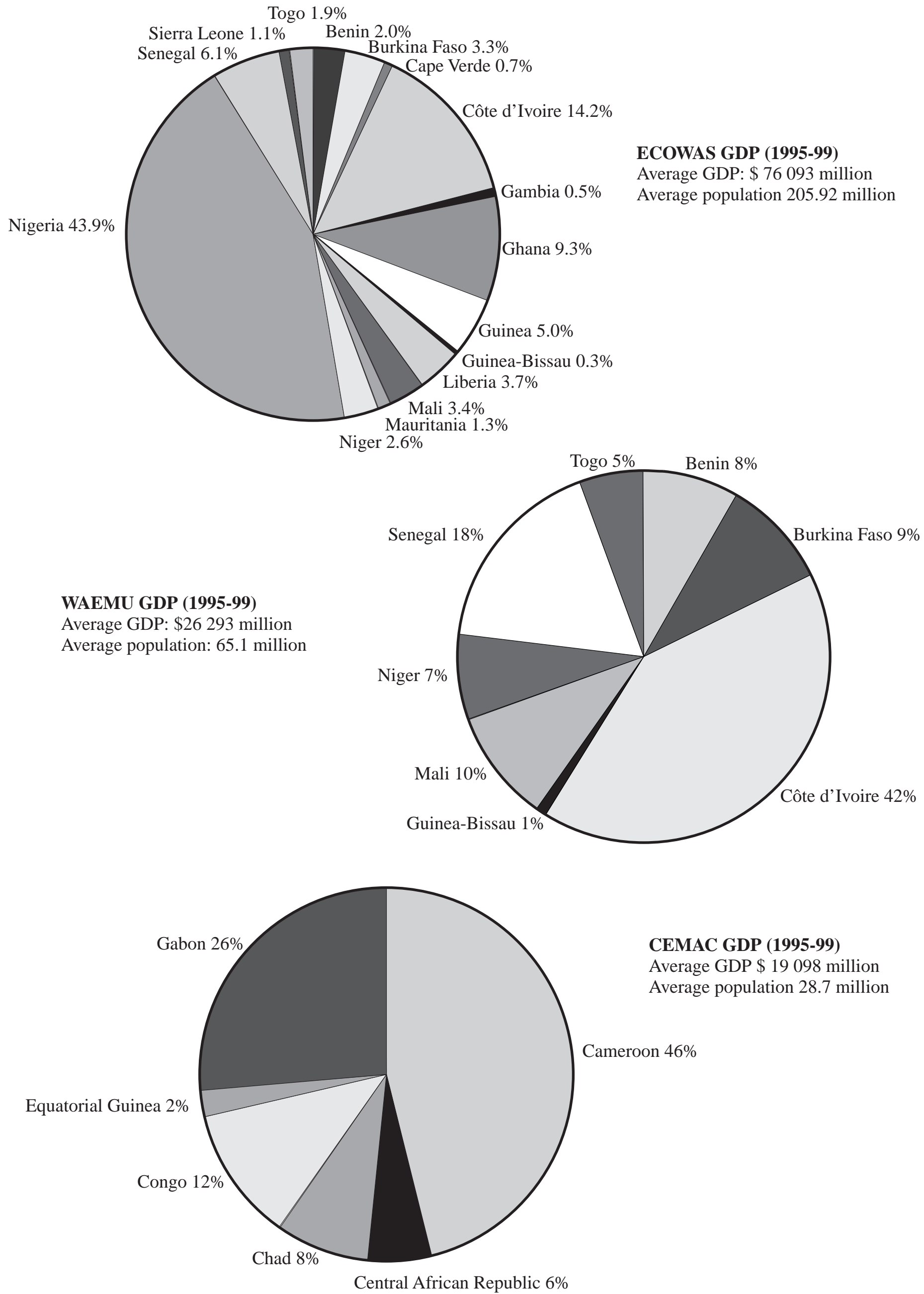
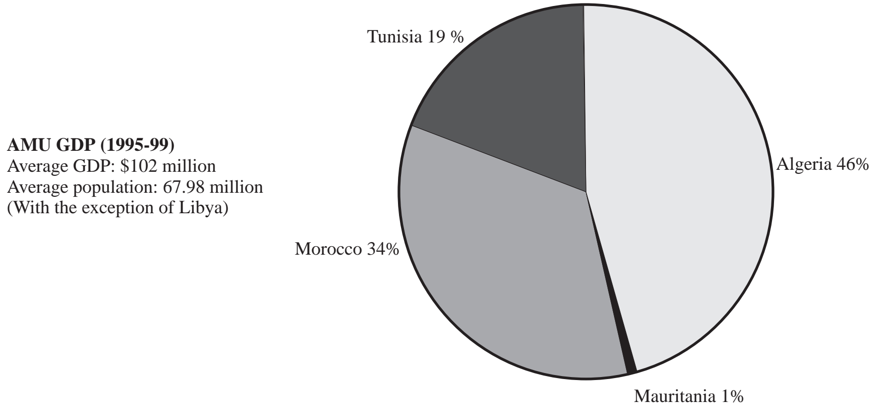
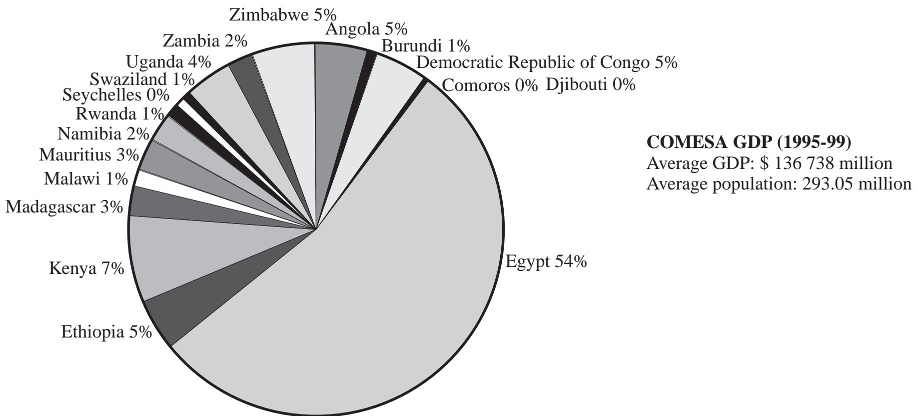
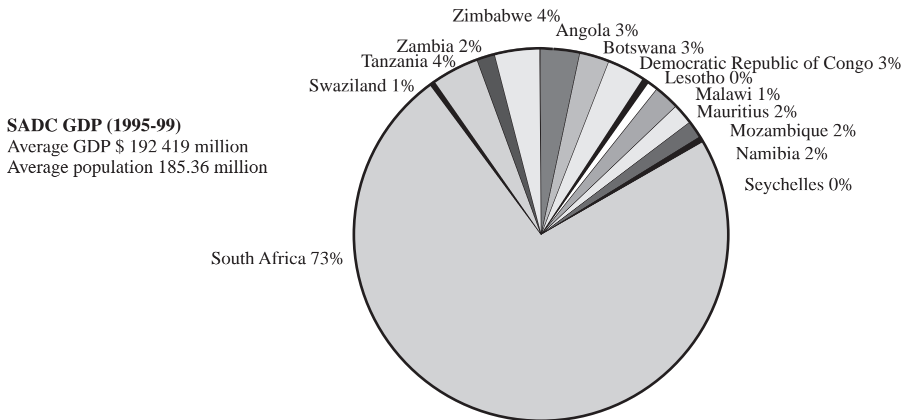


Figure 6. **GDP Structure (1995-99)** (cont.)







Source: Statistics Division, African Development Bank.

Constraints in the International Environment

The furtherance of integration is in keeping with the international setting marked by an accelerated trade liberalisation, the suppression of tariff and non–tariff barriers and the principle of the quota system. The direction taken in the constitution of large economic blocs or groupings that were more dynamic in the recent past has not been so much the closing of markets to private concerns and to other countries in order to escape international competition but to enable the groups of firms that compose them to become more competitive in order to profit from decommissioning; hence the number of mergers, mutual investments and relocations that have taken place in the past two decades. The building of these community structures and the search for economic growth cannot be done through trade diversion, but through a more effective use of opportunities offered by the development of the global economy. At this level is found the first external constraint. It seems difficult in the present international environment to continue searching for economies of scale based on regional integration, while production is increasingly destined for export to world markets.

The second constraint imposed by international changes concerns the growing interdependence of markets for basic products that are gradually becoming capital markets in search of maximum rates of return, with no regard for the type of products or the economic consequences of sudden price changes on the producer countries. In these markets, only the large groups, and not traditional producers, can hold their ground. So states will have less and less of a share in the profits from higher production, while they are at the same time penalised by a fall in prices. Their internal resources as well as their capacities to support regional integration programmes would be affected, and priority would be given to national programmes.

Another aspect that needs consideration is the increasing numbers of international accords based on the reciprocity of rules and advantages. Each time such agreements are signed between a constituted bloc and a given country, they are likely to be detrimental to the region’s economy as a whole. This is the case with the agreement concerning the creation of a free trade area between the EU and South Africa, although the latter is a member of a customs union whose membership has no specific agreements with the EU. The US–Africa Trade and Investment Initiative that recommends unilateral trade liberalisation is in the same position. At the same time, the WTO agreement should ensure a reduction of 36 per cent of non–tariff barriers for basic products of 20 per cent in support to producers and 20 per cent in support to export for the next four years. Transitional exceptions will have to disappear in less than ten years, as they may render useless the building of regional common markets, particularly with regard to the present nature and structure of African exports.

Constraints Relating to Economic Operators and their Strategies

In general, it can be said that in the different RECs the movement of money and persons is more important than the exchange of goods; and in this framework, re–export and transit trade are more than trade in local products. Trade with the rest of the world is a source of taxes and major revenue that profit only a category of economic operators that often predominates in the various RECs. They have often made large fortunes out of the liberalisation of foreign trade and their major concern is to safeguard and expand their own interests. They will therefore be reluctant to make heavy investments for production that may be profitable only in the long term. Like governments, they will be more inclined to give priority to external trade. At the same time, those who make a lot of money from informal cross–border trade, linked in particular to different import taxes and prices and to unilateral monetary and exchange policies, will be opposed to any development that may threaten their interests, even where such attitudes would create problems for the economy. In fact, the most dynamic informal trade is short term. Getting a lot of money in the shortest time is the rule: thus the fragmentation of trade offering the indispensable flexibility in any approach that seeks constant adaptation to the economic situation. Steps towards community building tend to minimise the existence and weight of powerful pressure groups with specific interests and do not automatically favour the strengthening of RECs. There are four types of players in these groups: local importers who make their profits and build their fortunes thanks to external trade liberalisation and the recourse to imports from outside the region; corporate groups directly threatened by a regionalisation of the markets; import traders in food and agricultural products whose sphere of influence and fortunes makes them leading national partners; and public administration and banks enjoying privileges and advantages from their position in trade matters.. These groups will always try to take control of or dodge these measures so as to maintain and strengthentheir interests. It is easier for them because the change in the nature and composition of domestic demand is more and more pre–determined by worldwide demand and tends to steer away from domestic supply, whether national or regional.

Conflictual Constraints

Up until now, only economic and social players operating in situations of relative political stability have been considered. Today, all the regions are confronted with conflicts whose extent and importance go beyond national level and are likely to persist. An economy of armed conflict with its own rationale and operators is growing in all regions. It distorts economies in the long term and produces, at least in conflict areas, another type of economic integration based on the principle of deconnection from other regional economies. This makes regional construction more difficult both through the resources that its confinement and reduction require and through its geo–strategic location.

These constraints lead us to raise again the issue of the integration process using the classic devices of import substitution or the search for economies of scale, or, better still, giving priority to market integration based on the implementation of the rule of origin and the common external tariff.

Conditions for Attaining Regional Integration

Considering the internal and external constraints and the achievements and their costs, it is right to question the advantages offered by economic co–operation leading to integration, in a context of trade globalisation and internationalisation of production based on the separation of the production areas of goods and services. Nevertheless, the pursuance of community building in Africa presents more advantages than disadvantages.

Community Building

In nearly all African countries, community building, because of the consultations involved and taking into account collective interests that do not always converge, is a factor for socio–political stability in the different countries.

It provides an appropriate framework in the resolution of costly conflicts. In this way, it is possible to bank on a transformation of Great Lakes region into a region of economic prosperity, transcending all sentiments of nationalism and sectarianism that undermine the future of countries beyond the war zone. ECOWAS and, to a lesser extent, the SADC are examples of this.

Through the mobility of the resources it harnesses, regional integration can also contribute to reducing the flight of capital from the region. Considering the assets of nationals in neighbouring countries (for instance in the Maghreb, in COMESA and the SADC), it is evident that in situations of uncertainty, part of domestic savings is invested as a measure of security in the region. A study of the structure of the IDE in Côte d'Ivoire and in Benin are good examples, as is the flow of remittances from Zimbabwe to Zambia.

Regional co–operation and integration help in bringing together the efforts of several partners to develop joint projects with positive spin–offs for all, but whose conditions of implementation and cost are over and beyond the capacities of a single country. This is so in areas such as research and development and the strengthening of institutional capacities. The same is true for the holding of international negotiations with the WTO. These negotiations demand expertise and resources that largely exceed the capacity of each of the African states.

The dismantling of tariff and non–tariff barriers helps to create markets that reach the general population and could help replace major trading firms by small and medium–scale individual importers, resulting in cheaper imported goods. This could either cause a general decline in prices and factor costs or a redeployment of importers to other less captive activities, contributing to strengthening the economic fabric.

In this context, the building of community groupings is in conformity with the evolution of the global economy and takes account of the argument of operators who do their business in this environment; this in turn will make the latter more attentive to the needs of their local partners.

It is therefore necessary to address regional economic co–operation and community building by placing them within the perspective of regionalism open to the outside world. The economic and political environment calls for an in–depth review of the neo–classical issue of integration through the market which is supposed to reduce distortions observed in national policies and create entities, where goods, services, and capital move without hindrance, as well as an approach that seeks to carry out according to collective and planned measures the building of self–centred economic systems. It is more appropriate to set up an integration process for growth with equity. In this regard, it has to be selective and flexible, with due regard to the constraints imposed by the evolution of the global economy, the nature of production systems and local consumption patterns, the arguments and interests of the economic players and, in particular, their common concern to reduce the risks and uncertainties to which they are exposed.

In this light, community building should seek the consolidation of factors and mechanisms likely to strengthen comparative advantages within the global economy. Therefore, in areas where basic products constitute the driving force for growth, collective investment and organisational strategies likely to improve competitiveness in international markets should be developed. This implies measures, such as the promotion of research and development, within a collective framework, and the putting in place of joint monitoring and market intervention structures. Taken from this viewpoint, the similarity of production systems will no longer be an impediment but, on the contrary, an opportunity to be seized.

It is therefore necessary to transcend the problems which tend to pit national construction against regional construction. Integration should contribute to strengthening economies and not their dissolution within a supranational entity. Such an approach will, among other things, reduce xenophobia and nationalistic tendencies that constitute the ideological basis of destroying community building efforts, especially in times of crisis or during periods of slow economic recovery or when economic results are not immediately published. It is within this framework that the concept of subsidiarity takes on its true value and importance.

Setting up a Local Structure as a Condition for Integration

Integration is a collective process based on the solidarity of its members and on agreed goals, so its implementation means setting up a local structure governed by a minimum of basic principles. This facility need not be geographical; it should however be institutional, economic, political, social and cultural.

The institutional fabric underlying community building at both regional and national levels should tend towards coherence and be governed by the same rules, in particular consultation before decisions of common interest are taken, transparency in management, compliance with regulations, information sharing and respect of all decisions. In this regard, it is necessary to fine–tune the different structures and initiatives that overlap, duplicate, or are contradictory. This operation should lead to a gradual reorientation of organisations and structures (including those at country level) towards the creation of maximum synergy and not their disappearance, at least in the short term. This should go hand in hand with the strengthening of policy co–ordination mechanisms.

On the economic front, it would be illusory to think that it is possible to obtain over the short and long terms a substantial modification of production systems. However, it is possible to increase their efficiency through joint investments and harmonisation of management frameworks. Integration implies the mobilisation of the appropriate financial, material and human resources for set projects. The best way to resolve the problem, at least in part, is to identify and exploit the productivity resources of each partner. A regional approach by sub–sector (particularly for basic products) could be quite useful in identifying corresponding products and harnessing these synergies. The priority development of border areas could be placed within the same perspective. Apart from its contribution to regional stability, it would draw on the formal and informal networks of the trade in goods and services, persons and capital in the area in question. Another aspect to take into account is the breakdown of costs and advantages. As in all other economic activities, integration is a game where people either win or lose. It is therefore necessary to anticipate the losses and gains and ensure an equitable distribution of profits and costs. This affects important issues, such as the fixing of basic prices which, within the framework of the regional trade liberalisation, deserve special attention. World prices cannot be utilised mechanically as they do not always reflect the balance between supply and demand; their levels are the result of a combination of several things, such as subsidies, dumping in the case of manufactured products, the existence of surpluses and non–compliance with the social provisions of labour laws. Local market prices, mostly informal, are in many cases opportunity prices linked to the temporary absence of equilibrium between supply and demand, and express short–term realities.

On the political front, it is essential to foster the rules of good governance and build legitimate decision–making bodies at all levels of authority. This helps create the conditions needed to implement the principle of subsidiarity and so ensure the irreversibility of decisions and actions at the regional level, making easier the handling of difficulties inherent to any undertaking geared towards community building.

From the social viewpoint, it is important to help in the formation of a critical mass of economic players on a supranational level whose development and maintenance requires the existence of broader economic entities. These types of players can ably serve as a driving force in efforts of integration. It is also essential that social disparities in terms of access to income be reduced. High–level internal or regional imbalances will only help to generate social conflicts and unrest that will impede all progress to integration.

One of the lessons to be drawn from the building of Europe is that it has allowed imbalances between the partners to be contained and even somewhat reduced. At the same time, a key sector such as agriculture has been able to receive funding to ensure its growth and give some protection to a part of the population destined to die out.

The cultural dimension is one of the factors often neglected and taken for granted. At this level a central objective should be pursued — the furtherance of the culture of mutual respect. This implies acknowledging and respecting social, ethnic and linguistic differences.

This is where the complexity of community building appears and can only be successful if all the constraints and factors underlying its progress and realisation are integrated. The role of states and bodies they help to set up become crucial, as they should help instil a collective energy by creating conditions for the development of economic operators and social players (local private firms, foreign investors, civil society organisations) and frameworks for transparent regulation of their activities. It is probably at this level that the most important gap between African community projects and the reality imposed by globalisation is to be found. It should be reduced for integration to succeed, with Africa's development partners taking an active part, either through special agreements such as the one linking the EU and Africa (including the Mediterranean countries) or through arrangements worked out in the course of international negotiations at the WTO.

The success of integration efforts as part of an open regional movement, with the goal of economic growth and sustainable development, requires taking into account the constraints discussed here, and building local structures that encourage the emergence and success of social players with projects that promote integration.

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Regionalism and Development in Latin America What Implications for Sub–Saharan Africa?

Andrea Goldstein and Carlos Quenan

Regional integration is one of the major developments in international relations in the recent past. In a simplistic description, the world structure has been transformed from one based on nations interacting within an international system to one of regions reacting within a globalised framework (Guerrieri and Falautano, 2000). On the one hand stand multilateral institutions, of which the World Trade Organisation, if not necessarily the most important, is probably the one with the strongest role and widest powers. On the other hand, commercial and production flows have become increasingly regionalised, around the three key geo–economic poles of the OECD — Europe, North America, and Northeast Asia — and the institutions they created to manage this process — in particular the European Union (EU) and the North American Free Trade Area (NAFTA). Developing countries have joined this bandwagon and nearly every one of them is in — or is discussing — a regional integration arrangement (RIA). Indeed, the number of new RIAs notified to the GATT/WTO each year, which averaged one or two until the early 1990s, has skyrocketed to 11 since 1992[1].

Against the background of globalisation, three major factors explain the development of RIAs (World Bank, 2000). First, the acknowledgement that regionalism must be "deep" and go beyond the reduction of tariffs and the removal of quotas and other non–tariff barriers (NTBs). Second, the commitment to design RIAs that — instead of being tools to implement import–substitution industrialisation on a regional scale behind high external trade barriers — may boost international commerce and contribute to the insertion of Southern countries in global markets. Third, the advent of North–South RIAs, linking high–income industrial countries and developing ones[2].

Most theoretical models in international trade conclude that across–the–board unilateral liberalisation is the superior solution in terms of welfare. As the choice confronting (democratic) governments, however, is between the *status quo* and some second–best form of market opening, including RIAs, rather than between the *status quo* and optimality, theory has left a gap that empirical work has tried to fill. Regional integration is a potentially valuable tool for modernisation in a sub–optimal world;

one characterised by imperfect markets at the national and international level. Policymakers have thus to decide not only whether to pursue regional arrangements but also how best to manage them. What are the effects of trading blocs on growth and on policy credibility? What are the diplomatic and political benefits of regional integration? Should countries harmonise standards or industrial policy? Should RIAs involve the construction of shared executive, judicial and legislative bodies? And more generally, are regional blocs undermining the multilateral trading system?

Proponents of RIAs present them as a means of stimulating competition, reaping economies of scale, attracting capital inflows and promoting technology transfer. They claim that such arrangements allow some liberalisation by countries unwilling to open up on a non–discriminatory basis and facilitate liberalisation in areas too complex to be negotiated successfully in the WTO. Equally important, regionalism is seen as good politics, both domestically — insofar as it includes commitment mechanisms that make it possible to overcome problems of time–inconsistency (Kydland and Prescott, 1977) — and across borders, insofar as increased economic interrelationships decrease the risk of conflicts[3]. There is indeed empirical evidence that, in the second half of the 20th century, parties to the same RIA have been less prone to engage in military hostilities, and that the likelihood of disputes dips markedly as trade increases between them (Mansfield and Pevenhouse, 2000). Last but not least, poor countries may find in RIAs the tools to make their voice heard in international fora.

From a theoretical perspective there are pros and cons to the rationale of joining a regional trading bloc (Bonaglia *et al.*, 2001). Indeed, on a purely economic basis, the integration in a regional market can produce mainly three effects:

— *Trade creation and trade diversion:* in a static economic framework, trade creation means that a free trade area creates trade that would not have existed otherwise. Trade diversion, on the other side, means that a free trade area diverts trade away from a more efficient supplier outside the RIA towards a less efficient supplier within the RTA.

— *Competition and scale effects:* in an imperfect competition framework where scale economies exist, RIA theory suggests the potential gains that may arise from market enlargement. Indeed, the latter may give simultaneous gains reducing monopolistic distortion through a greater number of firms in the marketplace avoiding firm fragmentation through the larger market. Moreover, market enlargement can create attractiveness for foreign investment (FDI) in the region.

— *Agglomeration effect:* production activities tend to concentrate in areas dense in capital and population, hence spatial clustering of economic activities may occur in a regional bloc. In the presence of economies of scale and scope, countries may benefit from technological and knowledge spillovers, coupled with linkages between buyers and sellers (backward and forward linkages) that are made more efficient by physical proximity[4]. The negative counterpart to this may be a worsening of regional disparities.

Table 1. **Basic Statistics for Selected Countries in Latin America and Sub-Saharan Africa**
(1996-98 averages)

	Agriculture, value added (% of GDP)	Urban population (% of total)	GNP per capita, Atlas method (current $)	GNP per capita, PPP (current international $)	Life expectancy at birth, total (years)
Argentina	5.77	89.00	7 986.67	11 493.71	73.23
Bolivia	16.23	60.70	970.00	2 196.04	61.70
Brazil	8.20	79.56	4 590.00	6 597.73	67.00
Chile	7.65	84.92	4 680.00	8 110.91	75.30
Colombia	13.11	72.64	2 450.00	5 962.44	70.26
Costa Rica	15.21	47.20	2 710.00	5 772.00	76.62
Ecuador	12.31	62.30	1 516.67	3 002.49	70.31
El Salvador	12.77	45.64	1 780.00	4 025.59	69.45
Haiti	30.80	33.84	383.33	1 397.42	53.66
Mexico	5.16	73.80	3 953.33	7 297.33	72.02
Nicaragua	33.99	55.14	370.00	1 849.76	68.26
Peru	7.12	71.66	2 500.00	4 285.01	68.59
Uruguay	8.61	90.52	5 863.33	8 403.10	73.65
Venezuela	4.56	86.06	3 386.67	5 781.65	72.88
Benin	38.21	39.96	373.33	854.10	53.41
Botswana	3.60	48.74	3 250.00	5 868.57	46.68
Congo, Dem. Rep.	57.73	29.34	116.67	766.92	50.77
Congo, Rep.	10.03	60.04	676.67	815.98	48.43
Côte d'Ivoire	26.72	44.54	700.00	1 453.64	46.41
Ethiopia	52.64	16.28	106.67	586.74	43.13
Gabon	7.19	78.10	4 113.33	5 537.72	52.47
Ghana	12.39	36.90	390.00	1734.93	60.01
Kenya	27.71	30.40	336.67	979.83	51.52
Mali	48.09	28.08	250.00	671.38	50.39
Mauritius	9.03	40.82	3 760.00	8 045.77	70.44
Mozambique	35.67	36.36	183.33	688.70	45.34
Nigeria	31.70	41.30	273.33	756.14	53.48
Senegal	19.04	45.24	526.67	1 278.21	52.32
South Africa	4.09	54.15	3 583.33	8 508.23	64.29
Tanzania	46.89	29.30	196.67	477.52	47.54
Uganda	43.92	13.18	306.67	1 063.71	42.15
Zambia	16.35	39.36	356.67	707.15	42.85
Zimbabwe	20.28	33.20	676.67	2 554.53	51.65
Latin America &Caribbean	***7.72***	***74.13***	***3 843.33***	***6 350.00***	***69.66***
Sub-Saharan Africa	***17.60***	***32.80***	***526.67***	***1 463.33***	***50.58***

Note: GNP per capita refer to 1996-98 averages.
Source : World Bank (2000), *World Development Indicators.*

Opponents, on the other hand, see RIAs as fostering discriminatory trade restrictions, causing governments to look inward rather than outward, and undermining the multilateral trading system. They also question the political advantages of closer integration. Promotion of intra–area trade through preferential treatments may bring about substantial income and wealth transfers between members and can lead to a concentration of industry in a single location. If this happens, the incentive for each member country to free–ride — for example by competing for scarce foreign capital on the basis of tax and regulatory incentives (Oman, 2000) — may easily offset any possible benefit from negotiating as a bloc.

Latin America and the Caribbean (LAC) and sub–Saharan Africa (SSA) hardly constitute an ideal pair for a most–similar–systems comparison: across various dimensions, differences between them are big, as clearly shown in Table 1. We think, however, that experience in the former region contains some interesting implications for the latter. The interest in the exercise therefore stems from other reasons: in the 1960s and 1970s policymakers in both regions tried to supplement their inward–oriented strategies with protectionist RIAs, with rather bad consequences. Compared to SSA, Latin America started its adjustment earlier, included regionalism among the policy instruments and has made more progress, so that it may be time to take stock and identify the main "open wounds" of RIAs there, in the Mercosur in particular. Therefore, despite the above–mentioned caveat, it is possible to draw some lessons from the Latin American experience that can be of interest for SSA.

Regionalism in Latin America: Past Failures

In the vision sponsored by the UN Economic Commission for Latin America and the Caribbean in the 1950s and 1960s, regionalism was seen as a tool to overcome two major development obstacles, namely the difficulty of exploiting economies of scale due to the limited size of plants producing for (closed) domestic markets and the excessive diversification of production lines across different goods, and the lack of competition (Ocampo, 2000; Tavares and Gomes, 1998)[5]. The first step towards regional[6] integration in Latin America, the signature in 1960 of the Montevideo Treaty, came only a short while after the creation of the European Coal and Steel Community (1952) and the European Economic Community (1958). The Latin American Free Trade Association (ALALC) provided for the creation of a free–trade zone, by means of periodical and selective negotiations between member states. This choice — negotiation at the discretion of the member states, rather than automatic reduction of import duties — allowed the trade opening programme to develop reasonably well in its first years, but progress lost impetus as of 1965, and came to an almost complete standstill in the 1970s. ALALC was replaced in 1980 by the Latin American Integration Association (ALADI), a loose association of 11 Latin American countries with a flexible mandate to establish, in a gradual and progressive manner, a common market.

The most ambitious attempt at sub–regional integration has been the Andean Pact, established in 1969 between Bolivia, Chile, Colombia, Ecuador, Peru, and Venezuela[7]. While the Agreement foresaw the setting of a common external tariff (CET), its intention was to a large extent limited to widen protected markets, maintaining and even raising barriers against the rest of the world in an ultimately doomed effort to make import–substitution work better (Goldstein, 1998). Very few results were achieved, leading Chile — the first country in the region to implement wide–ranging, across–the–board trade liberalisation — to withdraw in 1976. A similar fate of failure was that of the Central American Common Market (CACM), formed in 1962 to foster co–operation among Costa Rica, Guatemala, Honduras, El Salvador, and Nicaragua. By the late 1960s the CACM had made considerable progress in stimulating the expansion of commerce and manufacturing. Many intra–area barriers were eliminated or reduced, and between 1961 and 1968 trade among them increased to a figure seven times its previous level. But in 1969 Honduras and El Salvador engaged in a war that resulted in a break in their commercial and diplomatic relations. After cutting off El Salvador's access to the Pan–American highway, Honduras virtually withdrew from the CACM in early 1971 and imposed tariffs on imports from the other partners. The other members agreed to continue the CACM in spite of growing discontent within the group, but in 1983 Guatemala as well imposed many restrictions on trade within the region. The CACM entered a state of suspension in the mid–1980s owing to internal political instability and violence in some member countries and mounting debt and protectionist pressures.

The Commonwealth Caribbean made a serious move toward establishing a unit of integration by creating the West Indies Federation in 1958. The federation failed when Jamaica and Trinidad and Tobago attained independence and withdrew in 1962. Nevertheless, a few institutions, such as the University of the West Indies and the Regional Shipping Council, were established under the short–lived federation and continue today. The Caribbean Free Trade Association (Carifta) was established in 1965[8], but the prospect of Britain's joining the EEC alerted the islands to their vulnerability to any disruption in their preferential trading ties with Britain. In 1973 the Carifta members signed the Treaty of Chaguaramas, replacing the ineffective Carifta structure with the Caribbean Community and Common Market (Caricom). Caricom has three essential components: economic integration, functional co–operation, and co–ordination of foreign and defence policies[9]. Together, the CET and the Common Protective Policy, coupled with intraregional trade liberalisation, were expected to stimulate reciprocal investment and trade among members. In reality, in the decade of the 1980s the performance of the Caricom was dismal, as reflected in the impossibility of establishing the CET by the 1981 deadline, the intensification of regional protectionism, the collapse of its Multilateral Clearing Facility, and growing controversy over rules of origin (Nicholls *et al.,* 2000).

In sum, in the past, integration in Latin America and the Caribbean was dominated by the desire to avoid challenging the interests of protected groups in the participating countries and led, at most, to a reduction of protections on non–competing imports. To defend their markets from competition by other regional industries, small countries combined resistance to regional integration with ever–increasing tariff and non–tariff barriers, instead of embarking on unilateral trade liberalisation. By providing slightly longer survival horizons to inefficient producers groomed by import–substitution, such attempts postponed the emergence of a free trade culture.

Regionalism in Latin America: New Attempts

Institutional Arrangements

The 1982 debt crisis marked the time of reckoning for Latin America. In the second half of the decade, governments tried to face external and budgetary imbalances by adopting adjustment programmes often based on price freezes, exchange–rate depreciation and ambitious export support schemes. None of these measures worked: severe internal bottlenecks, that partly resulted from an inefficient and overblown state sector, were not adequately addressed and the international environment proved hardly supportive, not least because of a resurgence of protectionism in OECD countries. In parallel, Argentina, Brazil and Uruguay signed bilateral agreements in the framework of the Latin American Integration Association (ALADI) to increase bilateral trade. In particular, the Integration and Economic Co–operation Programme, signed by Argentina and Brazil in 1986, provided for sector–level negotiations to reach a higher degree of production complementarity. While selective, gradualist, and without a clear time schedule, this first wave of "new" regionalism produced some encouraging results, doubling bilateral trade flows in three years. Trade and market liberalisation, financial deregulation, and privatisation have been part and parcel of economic policy everywhere in the Americas in the last decade (CEPAL 1994; Edwards 1995). Results have been notoriously mixed: in a nutshell, lower inflation, basically unchanged growth performance, and somehow increased volatility and inequality (CEPAL, 2000). For the purposes of this paper, it is important to underline that RIAs have been part and parcel of most countries' structural adjustment policies from their very beginning (Table 2).

Argentina, Brazil, Paraguay and Uruguay established Mercosur in 1991 with the Asunción Treaty. Countries agreed an automatic scheduling of tariff reductions that led to the creation of a customs union and the setting of a common external tariff by the end of 1994. Harmonisation in customs duties, non–tariff barriers (NTBs), antidumping legislation, and safeguards have been favoured by the fact that unilateral liberalisation, aimed at reaching convergence with international standards, was already underway. Negotiations in specific sectors, such as machinery, petrochemicals, steel, electronics and pharmaceutics, have proved more cumbersome. The underlying rationale was that outright liberalisation was either insufficient or too costly and that

Table 2. **Regional Integration Agreements in Latin America since 1990**

1.	Argentina-Brazil 1990	18.	Bolivia-Brazil 1994
2.	Bolivia-Uruguay 1991	19.	Mexico-Bolivia 1994
3.	Argentina-Colombia 1991	20.	Chile-Bolivia 1994
4.	Mercosur 1991	21.	Chile-Ecuador 1994
5.	Chile-Mexico 1991	22.	Colombia-Mexico-Venezuela (G3) 1994
6.	Chile-Argentina 1991	23.	Venezuela-Caricom 1994
7.	Argentina-Bolivia 1992	24.	Colombia-Caricom 1994
8.	Bolivia-Peru 1992	25.	Brazil-Venezuela 1994
9.	Argentina-Venezuela 1992	26.	Bolivia-Paraguay 1994
10.	Argentina-Ecuador 1993	27.	Chile-Mercosur 1996
11.	Bolivia-Chile 1993	28.	Chile-Canada 1996
12.	Chile-Venezuela 1993	29.	CAN (former Andean Pact) (1996)
13.	Chile-Colombia 1993	30.	Bolivia-Mercosur 1997
14.	Nafta 1993	31.	Dominican Republic-Caricom 1998
15.	Brazil-Peru 1993	32.	Mexico-Nicaragua 1998
16.	Mexico-Caricom 1993	33.	Dominican Republic-CACM 1998
17.	Mexico-Costa Rica 1994	34.	Mexico-EU 2000

Source: Fischer and Meller (1999).

specific safeguard mechanisms had to be adapted to face sector–specific problems. Finally, Mercosur does not cover the car industry, for which an *ad hoc* regime exists that ensures that trade between Argentina and Brazil remains balanced. Bolivia and Chile joined in 1996 as associate members.

The revival of the Andean Pact was initiated by the Declaration of Ica at the 1989 Galápagos summit. Since the establishment of free trade in 1991, Andean Pact trade patterns have altered dramatically. Bolivia, Ecuador and Colombia show a noted and rapid increase in total and relative industrial imports and exports with regional partners. In fact, exports to regional partners grew five times faster than manufactured exports to the world. All members of the Pact also implemented deep unilateral liberalisation almost simultaneously with this regional revival. Bolivia, the early reformer, started its programme in the mid–1980s, and by 1992 its weighted average *ad valorem* tariff rate was 10 per cent, a reduction of more than 50 per cent compared with 1986[10]. Member countries confirmed their commitment to the integration effort by turning the loose Pact into the Andean Community of Nations (Comunidad Andina de Naciones, CAN) at the Trujillo summit in 1996. All existing bodies have been reorganised within the Andean Integration System.

The road map for the new regionalism in the Caribbean and Central America also reflects a paradigm shift in the earlier theory and practice of integration. Flexible adaptation to external conditions and integration into the world economy should in theory make it possible to overcome such structural disadvantages through openness and liberalisation. In practice, the usual curse of structural adjustment — uncertain long–term benefits vs. all–too–sure short–term costs — are compounded in the case of small economies by their greater vulnerability to external shocks (including weather conditions). For these countries regionalism has emerged as a response to overcome the development constraints of small size.

Caricom adopted a CET in 1991 and members implemented between 1995 and 1 July 1998 the four–phase schedule of CET reductions. As a result, the maximum tariff on industrial goods fell from 35 to 20 per cent[11]. Deeper integration is expected to result from reforms aimed at consolidating the Caricom Single Market and Economy (CSME). Equally important are developments with third parties. The CBI Agreement offers duty free access to exports of selected Caribbean and Central American countries into the market of the United States of America. CARIBCAN offers a similar facility for Caribbean exports into the Canadian markets. However, some preferential conditions that were accruing to Caribbean countries have been put in question after the implementation of NAFTA in 1994. This prompted Caricom to demand equal conditions *vis–à–vis* Mexico, most notably in textiles and apparel, and led to the approval of the US–Caribbean Basin Trade Partnership Act in May 2000[12]. Finally, in 1993 all of the CACM's members except Costa Rica signed agreements creating a new Central American Free Trade Area (CAFTA), which was basically an agreement gradually to reduce tariffs on intraregional trade over a period of several years. In order to gain easier access to the US market, while lessening the diversion of investments into Mexico, CAFTA countries signed the Interim Trade Programme (ITP), which is equivalent to the CBI for Caricom.

Summary of Results

Empirical studies do not allow reaching unequivocal conclusions concerning RIAs' economic results in the LAC region, although the balance is tilted on the positive side[13].

— *Simple data* suggest that RIAs have had a positive effect on trade intra–bloc and extra–bloc trade volumes (Tables 3 and 4). Under the joint pressure of unilateral and preferential trade liberalisation, economic intercourse in the Americas increased substantially in the 1990s, especially before the slowdown recorded in the aftermath of the 1998 Brazilian devaluation[14]. Mercosur and the Andean Pact have been particularly buoyant groupings, with 5– and 4–fold increases in the value of trade. It is interesting to note that the increase in intra–area trade has been much more limited for the two smaller groupings — and the Caricom in particular —reverting a long–time regularity that saw the weight of trade with neighbours representing a larger share in total exchanges for small than for larger American countries. As far as the Southern Cone is concerned, the Mercosur market is, not surprisingly, much more important for the two smaller partners, Uruguay and Paraguay, for which intra–area trade represented 45 and 60 per cent of total exchanges in 1997 (Table 4). For Argentina, Brazil has become the largest single trading partner. At the same time, the past decade has been marked by an increasing degree of synchronisation of the business cycle (Figure 1). This development, in a context of increasing vulnerability to capital markets' volatility, calls for at least some degree of co–ordination in macroeconomic policy (see below). An additional typology of economic exchanges that has registered a considerable growth is foreign direct investment. While still limited in absolute values, these flows are growing fast and already represent a significant factor in some industries, such as the utilities (Chudnovsky and López, 2000).

Table 3. **Trade Statistics for the Americas**
($ million)

	1990	1994	1995	1996	1997	1998	1999
ALADI							
1. Total exports	112 694	167 192	204 170	229 164	255 390	251 345	264 235
Annual growth rate (%)	10.6	36.8	22.1	12.2	11.4	-1.6	5.1
2. Intra-area exports	12 302	28 168	35 552	38 449	45 484	43 231	34 391
Annual growth rate (%)	13.2	26.2	26.2	8.2	18.5	-5.0	-20.4
3. Intra-area exports intensity (2/1)	10.9	16.8	17.4	16.8	17.8	17.2	13.0
Andean Pact							
1. Total exports	31 751	33 706	39 134	44 375	46 609	38 896	43 211
Annual growth rate (%)	30.2	13.6	16.1	13.4	5.0	-16.5	11.1
2. Intra-area exports	1 324	3 472	4 859	4 698	5 621	5 411	3 940
Annual growth rate (%)	31.0	21.5	39.9	-3.3	19.7	-3.7	-27.2
3. Intra-area exports intensity (2/1)	4.2	10.3	12.4	10.6	12.1	13.9	9.1
Mercosur							
1. Total exports	46 403	61 890	70 129	74 407	82 596	80 227	74 300
Annual growth rate (%)	-0.3	13.9	13.3	6.1	11.0	-2.9	-7.4
2. Intra-area exports	4 127	12 048	14 451	17 115	20 478	20 027	15 133
Annual growth rate (%)	7.3	17.8	20.0	18.4	19.7	-2.2	-24.4
3. Intra-area exports intensity (2/1)	8.9	19.5	20.6	23.0	24.8	25.0	20.4
CACM							
1. Total exports	3 907	5 496	6 777	7 332	9 275	11 077	11 633
Annual growth rate (%)	9.2	7.2	23.3	8.2	26.5	19.4	5.0
2. Intra-area exports	624	1 228	1 451	1 553	1 863	2 242	2 333
Annual growth rate (%)	8.9	6.0	18.2	7.0	19.9	20.3	4.1
3. Intra-area exports intensity (2/1)	16.0	22.3	21.4	21.2	20.1	20.2	20.1
Caricom							
1. Total exports	3 634	4 113	4 511	4 595	4 687	4 791	4 223
Annual growth rate (%)	11.6	3.1	9.7	1.9	2.0	2.2	-11.9
2. Intra-area exports	469	521	690	775	785	…	…
Annual growth rate (%)	2.9	2.6	32.4	12.3	1.2	…	…
3. Intra-area exports intensity (2/1)	12.9	12.7	15.3	16.9	16.7	…	…
Latin America							
1. Total exports	120 572	177 336	216.031	241 648	269 996	267 213	280 091
Annual growth rate (%)	6.5	32.6	21.8	11.9	11.7	-0.8	4.8
2. Intra-area exports	16 802	35 065	42 740	46 562	54 756	51 674	42 624
Annual growth rate (%)	8.2	20.1	21.9	8.9	17.6	-5.6	-17.5
3. Intra-area exports intensity (2/1)	13.9	19.8	19.8	19.3	20.3	19.3	15.2

Source: UN Economic Commission for Latin America and the Caribbean.

Table 4. **Export Statistics for the Americas in 1999 (excluding Mexico)**
(percentage)

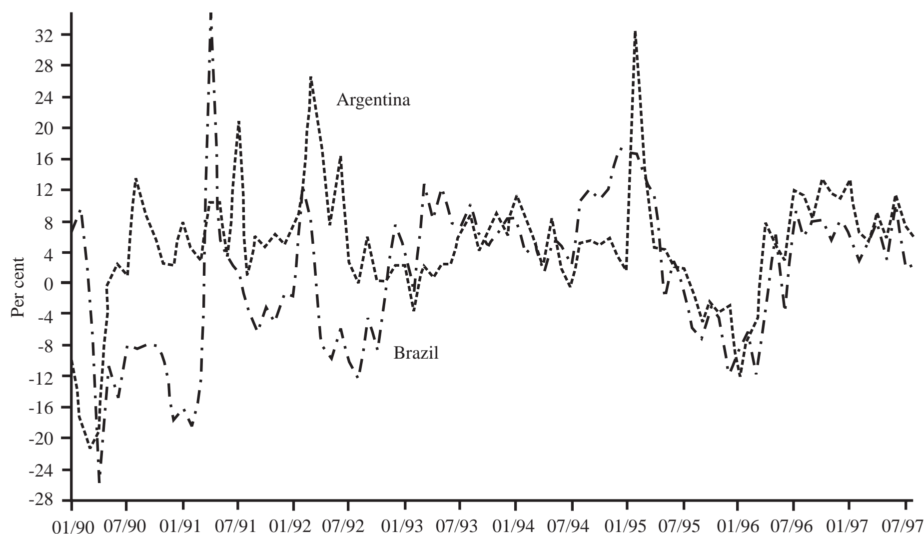
	Region	United States	Japan	European Union	Asia	Others	World Total
A. Export composition according to destination							
Primary goods	**18.6**	**42.6**	**53.3**	**39.3**	**31.4**	**35.5**	**34.1**
Agriculture	8.5	15.5	28.0	28.8	14.3	13.6	**16.3**
Mining	1.7	0.8	25.1	6.2	14.1	6.8	**4.7**
Energy	8.4	26.3	0.2	4.3	3.0	15.1	**13.1**
Industrial goods	**81.1**	**57.1**	**46.5**	**59.7**	**68.5**	**59.0**	**64.7**
Traditional	26.5	17.5	19.0	27.7	26.7	24.5	23.6
Food, beverages, tobacco	12.4	4.5	12.5	20.0	17.3	20.7	13.1
Other traditional	14.1	13.0	6.5	7.7	9.4	3.8	10.5
With economies of scale	30.4	24.1	24.8	20.8	35.0	28.6	26.5
Consumer durables	10.6	2.6	0.1	3.3	0.6	1.3	4.5
High-tech	13.6	12.9	2.6	7.9	6.3	4.5	10.1
Other goods	**0.3**	**0.3**	**0.2**	**0.9**	**0.0**	**5.5**	**1.2**
Total	**100**	**100**	**100**	**100**	**100**	**100**	**100**
Total (value)	**40 479**	**41 950**	**6 126**	**28 203**	**8 305**	**21 401**	**146 463**
B. Export destination							
Primary goods	**15.1**	**35.7**	**6.5**	**22.2**	**5.2**	**15.2**	**100**
Agriculture	14.4	27.3	7.2	34.0	5.0	12.2	**100**
Mining	10.0	4.6	22.1	25.3	16.9	21.0	**100**
Energy	17.7	57.6	0.1	6.4	1.3	16.9	**100**
Industrial goods	**34.6**	**25.3**	**3.0**	**17.8**	**6.0**	**13.3**	**100**
Traditional	31.1	21.3	3.4	22.6	6.4	15.2	**100**
Food, beverages, tobacco	26.1	9.8	4.0	29.4	7.5	23.2	**100**
Other traditional	37.3	35.6	2.6	14.2	5.1	5.3	**100**
With economies of scale	31.1	26.0	3.9	15.1	7.5	15.8	**100**
Consumer durables	64.8	16.2	0.1	14.0	0.7	4.2	**100**
High-tech	37.3	36.6	1.1	15.0	3.5	6.5	**100**
Other goods	**6.4**	**7.9**	**0.6**	**15.7**	**0.2**	**69.2**	**100**
Total (average)	**27.6**	**28.6**	**4.2**	**19.3**	**5.7**	**14.6**	**100**

Source : UN Economic Commission for Latin America and the Caribbean.

— Quantitative analyses do not provide a clear–cut answer about the net welfare effect of an RIA.

Most gravity models[15] conclude that in Latin America, after the signing of the regional agreement, new trade has been created (Frankel, 1997; Piani and Kume, 2000; and Winter and Soloaga, 1999). Studying Mercosur's *exports*, Yeats (1997) argued that trade–diversion dominated trade–creation. His oft–cited results, however, were criticised by Devlin (1997) for not taking into account that protection might be independent from Mercosur. Nagarajan (1998) applied Yeats' methodology to the study of intra–Mercosur *imports* and rejected the contention that trade diversion has dominated trade creation, as well as the case that the shift in the origin of imports has been inefficient.

Figure 1. **Industrial Production Growth in Argentina and Brazil**
(year-on-year change)



Source: EIU.

CGE models[16] generally give positive results. Flôres (1997) and Diaz–Bonilla and Robinson (2001) found substantial potential gains from competition and scale effects in Mercosur[17]. In the case of Argentina, dynamic effects from Mercosur have been positive, thanks to investment growth as well as knowledge dissemination through trade and FDI flows (Calfat *et al.*, 2000). For the Andean Pact, however, Madani (1999) found that expected gains from regional arrangement through scale effects are neither large nor across–the–board, although using a different methodology (expanded growth accounting). Bussolo and Roland–Holst (1999), for Colombia, also show that, given current trade shares, selective liberalisation towards major partners may bring larger welfare benefits than if limited towards neighbours only.

— *Industry studies* based on micro and sectoral field research offer a number of interesting hints, especially in Mercosur. Insertion into the global economy is associated with long learning curves, so firms can benefit from the exploitation of familiar regional partners before venturing into the stormy waters of international markets. The car industry has attracted a lot of research attention, both for its sheer size and for the peculiar trade framework under which it operates. While the evidence of trade diversion is not disputed, quality indicators as well as the sizeable increase in exports to third countries suggest the presence of positive dynamic gains from specialisation and longer production runs (e.g. Tigre *et al.*, 1999). In this context, intra–industry and intra–firm trade flows have

increased: in other words, in relatively sophisticated industries, such as car and car parts, Mercosur has seen the emergence of exchange patterns usually associated with North–North trade (Miotti *et al.*, 1998). Nofal and Wilkinson (1999) also identify a number of positive consequences from trade integration in the dairy industry. In Uruguay, in particular, the exploitation of an existing comparative advantage has led to both the strengthening of the leading firm, which has proved able to compete internationally, and to the entry of new players on the domestic market, increasing the degree of competition. On the other hand, Bekerman and Sirlin (2000), examining the footwear industry in Mercosur, conclude that the existence of preferential treatment has had no major impact[18]. They also note, however, growing interlinkages between Argentinian (and Uruguayan) firms and their Brazilian counterparts, both in terms of production structure — the first two providing leather, the last producing shoes — and organisational and technological know–how. In view of the fact that NTBs are particularly rife in this sector (Berlinski, 2000), it is possible that the full realisation of Mercosur integration will bring about a larger degree of productive integration.

Examining the non–economic gains from regional integration, on the other hand, is intrinsically more difficult, although results are also less controversially positive. The aborted coup in Paraguay is frequently cited as the most illustrative example of the positive political dynamics triggered off by Mercosur. In April 1996, for the first time, Mercosur was challenged not only as a trade community dealing with common and interdependent economic issues, but also as a political body whose commitment to democracy was an inherent part of its charter, the Treaty of Asunción. During the military crisis the governments of the remaining member countries acted promptly, exerting strong public pressures against the coup and applying coercive diplomacy on the spot. At the first official meeting of the Mercosur Council, two months later, a Presidential Declaration was issued on the democratic commitment in Mercosur, followed by another Presidential Declaration on political consultations among the members.

Another important non–economic gain from integration is the fact that common positions on foreign policy have higher chances of being considered in multilateral fora. For instance, the Cairns Group, whose 15–country membership includes Argentina, Brazil and Uruguay, contributed effectively to the establishment of a framework for reform in agriculture in the Uruguay Round. Co–operation does not always ensure that partners are able to resolve political conflicts, as shown most recently by the low–intensity war between Ecuador and Peru in 1995[19]. Still, the Andean integration process, together with mediation by Mercosur, has eased subsequent negotiations[20]. As concerns Argentina and Brazil, closer political collaboration has accompanied growing trade and economic integration (Campbell, 1999), most notably the abandonment of their respective nuclear weapons programmes and the signature of a Declaration on Common Nuclear Policy in 1990. If this has not led to the adoption of a common external policy — an objective which is indeed far from completed even within the European Union — Mercosur countries have certainly tried to internalise

"strategic negotiating considerations" (Bouzas, 1999), in other words the capacity to negotiate jointly with third parties. An on–going example in this respect is the talks between Mercosur and the European Union to establish a free trade area[21].

Denser interactions, not least through immediate eye–catching measures such as regional sports events or dedicated lanes for Mercosur nationals at airports, have fostered mutual attention to each other's domestic political and economic processes. In line with global trends towards growing participation by the civil society, public opinion in these countries also contributed to voicing regional concerns on such themes as the rule of the law, human rights or sound environmental policies. Transnational networks already existing in Mercosur can also transmit outside the region, and with greater speed, local concerns regarding those themes. It is more difficult to detect whether Mercosur really acted as a strong tool to lock in reforms and increase credibility. Writing before the devaluation of the real, Albuquerque (1998) argued that with Mercosur the Brazilian government finds it less difficult to resist pressures to raise tariffs or to loosen public expenditure, a predicament that subsequent events proved unfounded, as explored below in greater detail.

The Open Wounds of Latin American Regionalism: the Case of Mercosur

The most important lesson from the economic slowdown of the late 1990s (which continues in the case of Argentina) is that, notwithstanding structural reforms, Latin American countries remain fragile (Morley, 2001) and still do not shy away from "beggar thy neighbour" policies. This temptation has made all the more clear the costs resulting from the absence of formal dispute resolution mechanisms and the continuing reliance on diplomatic channels. This calls for a rationalisation of regional institutions, taking account of their heterogeneity in Latin America (Table 5). The Mercosur example is particularly interesting on this account: reinforcing the institutional framework has been seen as a non–priority for a long time, in the face of continuing success in increasing trade flows and attracting investment, until its feebleness suddenly emerged as a major stumbling block for the very process of integration. In an environment characterised by continuing volatility, the lack of macroeconomic co–ordination proved extremely costly in the aftermath of the 1999 Brazilian crisis.

The Asunción Treaty refers to macroeconomic co–ordination in its preamble, in article 1, and in annexe V. The Mercosur summit held in Ouro Preto in December 1994 also highlighted the pressing need to accelerate and strengthen co–operation in budgetary, monetary and exchange–rate policy "in order not to introduce distortions in the process of improvement of the customs union and to facilitate the medium–term construction of a common market". A number of reasons explain why, notwithstanding such ambitious official statements, very little progress has been recorded in this field.

First of all, fate has been benign towards Mercosur in its early life. The business cycle was initially desynchronised between Argentina and Brazil, basically because of diverging exchange–rate policies. Between 1989 and 1990 Argentina went through a recession accompanied by hyper–inflation and real exchange–rate depreciation, with

Table 5. **Institutions of Regional Integration**

	NAFTA	CACM	Caricom	CAN	Mercosur
Supreme Body		Meeting of Presidents	Conference of Heads of Government	Presidential Council	Common Market Council
Principal Body	Free Trade Committee	Council of Ministers	Community Council of Ministers	Council of Foreign Ministers	Common Market Group
Executive Body (ies)	Secretariat	Executive Committee General Secretariat	Caribbean Community Secretariat	General Secretariat	Administrative Secretariat
Judicial Body		Court of Justice		Court of Justice	Trade Committee
Deliberative Body		Parliament		Parliament	Joint Parliamentary Committee
Financial Institutions		Central American Integration Bank	Caribbean Development Bank	Development Corporation; Latin American Reserve Fund	
Consultative Institutions		Advisory Board		Business Advisory Council; Labor Advisory Council	Economic and Social Consulting Forum
Educative Institutions				Simón Bolívar University	

Source: Elaborated from Dabène (1998).

negative consequences for Brazilian exporters that were priced out of that market. But things started to change as Mercosur formally came into force. The Argentinian currency board, turned into law in April 1991, brought about a real term appreciation of the peso (which had replaced the austral in January 1992) and a strong recovery yearly average growth of 7.8 per cent in 1991–94) pulled by domestic consumption (Heymann and Kosacoff, 2000). Brazil recorded a much more modest growth performance over the same period (2.6 per cent) while macroeconomic instability turned consistently very high inflation into hyper–inflation. As a consequence Argentina, which traditionally suffers a deficit in bilateral trade, introduced a series of *ad hoc* barriers on exports and started demanding a stricter policy orientation in Brazil.

This happened in Brazil with the launch of the Real Plan in 1994. Inflation, which hovered around 50 per cent *per month*, has quickly come down, while the availability of consumer credit and the rise in real disposable income have combined to produce a boom in internal consumption. As the Brazilian real appreciated *vis–à–vis* the US dollar (and hence the peso), the trade balance switched sign to the advantage of Argentina. Faced with the Mexican shock between late 1994 and early 1995, the Argentinian authorities decided to sacrifice growth to the altar of the currency board.

The recession would have been deeper, and the unemployment increase larger, had the real not appreciated and the Brazilian economy proved resilient. Starting from the second quarter of 1995, and also thanks to the good performance of primary goods, exports to Brazil allowed Argentina to record a trade surplus. Capital inflows returned to the pre–tequila levels and growth rates in Mercosur accelerated again in 1996 and 1997. Following the 1995 recession, the relative cyclical position switched, with growth gathering momentum in Argentina (and Uruguay) while losing steam in Brazil (and Paraguay).

The lack of policy co–ordination, however, must also be explained in terms of a second set of reasons. In an environment marked by endemic macroeconomic instability and feeble initial levels of interaction, limited co–ordination was on offer (Lavagna, 1995). This phenomenon is in turn associated with the diversity of exchange–rate regimes and the difficulties encountered in reining in public finances, especially in Brazil. It is well–known that the monetary and exchange–rate regime introduced in Argentina is completely rigid. Nonetheless, insofar as the strategy implemented in Brazil to fight hyper–inflation centred on a quasi–fixed parity against the dollar[22], it was reasonable to expect that the success of the Real Plan could lead to closer co–ordination. At the same time as concerns about the post–tequila performance of the LAC region lost immediacy and a downward convergence of inflation rates was recorded, the fiscal position in most countries worsened. Following the almost spectacular progress in the first half of the 1990s, Argentina's fiscal position deteriorated, still at levels that are low in absolute terms but that are worrying given the currency board straitjacket. The same can be said in the case of Brazil, where exchange–rate management had taken central stage in the policy menu.

The fiscal situation proved to be Brazil's Achilles' heel when the Asian and Russian crises erupted. The contagion led authorities in Brasília to raise interest rates in order to resist speculative attacks against the domestic currency. The resulting explosion of the domestic debt burden proved unsustainable and spaced out the prospects of macroeconomic co–ordination. Already hit by the Asian crisis *via* the fall in international commodity prices and the rise of the emerging markets' risk premium, Argentina tried to differentiate itself from its Mercosur partner to the eyes of international investors. Brazil, for its part, turned a deaf ear to partners' requests for transparent information in the face of the short–term need to resist the speculative attack.

The devaluation of the real in January 1999 triggered a series of niggling trade disputes between Argentina and Brazil in a context of declining intra–regional exchanges (although they recovered sharply the following year, see Table 3). Authorities in Brasília considered that their counterpart in Buenos Aires had done precious little to help them, and there have also been arguments over the domestic content of cars made in the region and allegations of dumping in the sugar, poultry and dairy industries. But recent disputes must be set against a more positive broader context. None of this amounts to anything like a return to the protectionism that characterised Latin America's development for much of the post–war period. Even if Mercosur further delays moves to reduce its common external tariff as a result of Chile's decision, it remains — at a level of 14 per cent — about a third of average Latin American rates of the mid–1980s. Although the pace may be painstakingly slow, the union is committed to expansion.

Moreover, as it is often the case, the crisis situation also induced policymakers to analyse hitherto taboo subjects. A proposal to dollarise the Argentinian economy was launched by President Menem in January 1999. This was mainly a signal given to markets to reassure them and push back the lingering risk of an attack on the currency board. But in order to be a credible tool, the proposal had to be perceived as a long–term strategy and therefore had to include a regional element. Brazilian authorities, however, have met the dollarisation proposal with more doubts than enthusiasm, for both economic and political reasons. On one hand, the use of the dollar is much less widespread in Brazil than in Argentina; on the other hand, public opinion in Brazil associates dollarisation with the relinquishment of national sovereignty and the abandonment of the country's aspirations to play a regional leadership role. Brazilian policymakers and top businesspeople have not shied from accusing Menem of playing to the interests of the United States and of trying to kill Mercosur.

The crisis — and more generally the impossibility of any emerging economy autonomously resisting contagion effects — has brought home the need to improve the fora and the processes for macroeconomic policy co–ordination. The interest which arose from the dollarisation proposal did indeed convince Brazilian authorities to present a plea to introduce a Mercosur currency. While this goal will only be realised in the medium, if not long, term, putting it on the policy table has allowed it to go beyond a debate that was largely confined to academic circles (Eichengreen, 1998; Lavagna and Giambiagi, 1998; Heymann and Navajas, 1998). In 2000 authorities chose to focus their attention on the setting of common convergence criteria in terms of fiscal balance, public debt and inflation. The underlying hypothesis is that the macroeconomic environment in each member country can be improved by ensuring fiscal solvency and price stability (Rozenwurcel, 2001). In order to accelerate progress in macroeconomic policy co–ordination, as required to allow a continuous rise in trade intensity and to provide investors and other economic agents with a long–term horizon in which to take their decisions, most economic and financial statistics were harmonised in 2000. The next step is the monitoring of a small set of policy variables: level and variation in net public debt and inflation rate (currently the consumer price index, before moving on to measures of "core inflation" from 2006). The year 2001 is considered as a "transition period" before the "common goals" period starts in 2002 (Rozenwurcel, 2001). As far as the ratio between net consolidated public debt and GDP is concerned, for example, the ceiling is set at 3 per cent from 2002, although Brazil was granted a temporary transition period (no more than 3.5 per cent for 2002–03). A light institutional framework is in place to manage the monitoring process. The Macroeconomic Monitoring Group (*Grupo de Monitoreo Macroeconómico*, GMM), composed of senior Treasury officials, set the convergence criteria in March 2001. Countries unable to meet such criteria will have to present to the GMM which measures they intend to put in place to redress the situation and ensure that goals are eventually achieved by the end of the year in which corrective measures are communicated.

The Mercosur convergence approach is certainly inspired by the Maastricht experience within the EU. There is however a major difference in that the focus, at least for a fairly long period, is not on the introduction of a common monetary and exchange–rate policy (Quenan, 2000). Choosing this strategy presupposes that the private and public sectors in member countries — and most importantly in Brazil and Argentina — are willing and able continuously and frankly to exchange feedbacks so to improve the degree of mutual understanding of the determinants of the exchange–rate regime. Meanwhile, against the background of the growing number of countries that officially dollarise their economy to reduce instability and/or reinforce policy credibility (Ecuador in 2000 and El Salvador in 2001), Mercosur has chosen an "open–ended" strategy as opposed to a corner solution[23].

Implications for Africa: Making RIAs Work for Effective Global Integration

Both Latin America and Africa are highly heterogeneous regions, so that drawing broad–based implications may be too ambitious[24]. SSA has seen an acceleration of integration initiatives over the last decade, and it is possible to advance the hypothesis that the current situation there is similar to the one prevalent in Latin America in the early 1980s. The past record of African RIAs is notoriously negative, not least because of a low degree of economic complementarity and high transport costs. It is important to bear in mind, however, that in Southern Africa intra–area trade is at levels comparable, if not superior, to those of Mercosur some 15 years ago. We think, however, that this is a risk worth taking: this is a list of ten major implications — some positive, others negative — that we think policymakers in sub–Saharan Africa should draw from the RIA experiences analysed in this paper.

i) *Objectives* should be clear, easy to prioritise, fit into a coherent framework of domestic policies and constitute the basis for the design of the regional agreement. Mercosur was initially about locking in trade and other reforms (including democratisation) and convincing foreign investors that the Southern Cone was a great destination: its institutional structure has been accordingly "light". The Andean Pact in the 1970s, on the other hand, eyed politics and industrial planning, and necessitated a much heavier institutional apparatus, so no wonder it failed. More in general, and rather obviously, political leaders who are strongly committed to protecting national interests — labour or capital, if not both — hardly have the credibility to open markets, even among associate members. The experience in SSA is unfortunately rather inauspicious, since objectives have usually been far too ambitious to be credible, especially in view of the weakness of policymakers and the dearth of administrative skills (Andreatta *et al.*, 2001). It is also rather natural that RIAs associating countries that are politically, when not geographically, far away are doomed to fail, no matter the length of rhetorical statements.

ii) Trade integration requires *accurate political guidance* to anticipate or react to the regional disparities. Economic geography suggests that spillovers can produce agglomeration and regional divergence. One of the great risks of South–South regionalism is indeed that of increasing divergence, rather than assisting convergence. Less favoured areas should be protected from the potential income disparities arising within the free trade area. Therefore, regional institutions should be built and designed to provide *social insurance* as the price for accepting larger doses of liberalisation. Mercosur has certainly not found a solution to this problem, not least because Brazil is itself a country marred by deep regional inequalities. Caricom has a number of mechanisms aimed at providing guaranteed markets and prices for exports to overcome the volatile trade in primary commodities[25]. In SSA there are still very sensitive ethnically–generated tensions that often erupt into severe strife, so politicians shy away from the kind of gestures that provide guidance and assure citizens who are concerned about the short–term costs of regional opening. High dependence of SSA countries on customs revenues also makes it difficult to create development and compensatory funds at the regional level.

iii) *Coherence* is key between regional and multilateral trade liberalisation as well as between domestic and regional policies. Growth, trade openness, and poverty reduction may be associated in a virtuous circle only when domestic economic reforms solve the most egregious supply–side bottlenecks, as shown *a contrario* by the Andean experience. In the case of Egypt and other Southern Mediterranean countries, for example, free trade with the EU will deliver welfare gains only if it is accompanied by domestic reforms such as privatisation and regulatory reform and further trade liberalisation at the multilateral level (Dessus and Suwa–Eisenmann, 2000). There is also considerable evidence, for instance in East Africa, that the supply response to more liberal economic incentives is held up by poor infrastructures and institutions (Bonaglia and Fukasaku, 2001). But this sacrosanct call for least developed countries to do more to heal their wounds cannot mask the costs of trade restrictions.

iv) The politics of regional integration are complicated enough to suggest to developing countries that they adopt an *efficient framework of regional institutions*. The challenge is to find the right balance between quantity and quality. In other words, the number of institutions required to make integration work is rather reduced, but those that are created must contribute effectively to deliver commitment through credibility. Mercosur testifies to the fact that with few and clear objectives it is possible to advance with a very slim institutional apparatus — although developments in the second half of the 1990s have also made it clear that the qualitative and quantitative increase in economic interaction calls for a richer texture of regional institutions and policy–making bodies[26]. The experience of Africa, unfortunately, is one where many different bodies have been established but none of them has ever developed properly. The opportunity cost of keeping such bodies is also likely to be higher nowadays as countries simultaneously

embark on domestic and multilateral liberalisation, with the associated regulatory and negotiating requirements. Caribbean nations have been relatively successful —and certainly much more so than similarly small African countries — in finding common mechanisms to participate in the WTO mechanism and similar multilateral exercises.

v) To promote *trade creation* and avoid trade diversion, RIAs must be "open", i.e. be a vehicle for multilateral liberalisation. The advantage of regionalism is that policymakers may proceed on the path leading to multilateral liberalisation along more predictable lines, in a "controlled environment of a reciprocal agreement of circumscribed scope" (Devlin and Ffrench–Davis, 1999). Even a country with a liberal trade regime like Singapore sees free–trade pacts with like–minded strategic and trading partners such as New Zealand, Australia, Chile, and Mexico as a means to reduce vulnerability in Southeast Asia, encourage competitive liberalisation, and in turn provide a positive impetus to WTO. At the same time, comparative advantages should be fully exploited: in the long run, a closed trading bloc produces negative welfare effects. So, for the proliferation of RIAs not to become a threat to the objective of achieving a rule–based world trading system, attempts should be made to extend RIA–based liberalisation with most favoured nation (MFN) provisions.

vi) Increasing interdependence may also have unpleasant implications, i.e. make a partner (usually the weakest one) more vulnerable to problems than the others. But a crisis — as is well–known in the literature on the political economy of reforms — may turn out to be positive if it proves a catalyst for change, in this case by showing the need to attain *macroeconomic co–ordination*, as proven by Mercosur's recent experience. This is an area where small countries may have something to teach large ones, in both LAC and SSA regions. The Caricom Multilateral Clearing Facility (CMCF) is the principal vehicle for financial co–operation in Caricom. It was established in 1977 to reduce the use of foreign exchange, expedite intraregional payments through credit and other financial arrangements, harmonise exchange rates by pegging the six existing currencies to the US dollar, and issue regional traveller's cheques through the Central Bank of Trinidad and Tobago.

vii) In developing countries, filling the large gap in the quality and quantity of *infrastructure* is a key issue to increase trade integration and support export diversification, as shown for example by Longo and Sekkat (2001) for Africa[27]. However, investment in infrastructure is very costly and may not be bearable by individual countries. This should be a win–win situation for policy makers in poor developing countries, but the contrast between the ambitiousness of goals and the modesty of results is staggering. Co–operation in maritime transportation, for example, is envisioned through the West Indies Shipping Corporation (WISCO), established in 1961, which theoretically provides services to all Caricom nations. In early 1987, however, Belize, Dominica, and St. Vincent and the Grenadines withdrew from WISCO, claiming they had received few benefits

from the service. Therefore, a co–ordinating regional agency could be useful to ensure the development of infrastructure. Research by one of us on the far too slow progress in establishing a more competitive air transport industry in SSA (a first–order requirement for achieving the ultimate objective of fully integrating into the global economy through tourism, exporting high value–added primary produce, and participation in global supply chains) has shown the almost insurmountable obstacles posed by bureaucracies, favouritism, and nationalism (Goldstein, 2001).

viii) Just as individual countries are encouraged to adopt them, a regional way to *second–generation reforms* is needed. Insofar as open regionalism sees a complementarity between integration among members and liberalisation towards non–members, it requires an increasing attention to microeconomic and structural issues, in economic and financial areas as well as elsewhere in the policy–making domain. The record in Latin America is so far rather poor, although it is increasingly clear which areas should be prioritised. Comprehensive and consistent enforcement of competition policy both at the national and the sub–regional level, in particular, is required for firms to take investment decisions and consumers to benefit from a wider regional market. Limiting the race to the bottom of fiscal incentives between different countries and states to attract investment, mainly foreign, is another (Oman, 2000). In the medium term, a regional strategy aimed at promoting the capacity to acquire and use knowledge and to innovate is of paramount importance to allow participation in the global economy.

ix) The capacity of the Mexican economy to overcome the 1995 recession in a relatively short period, thanks to NAFTA, is frequently cited as convincing evidence of the much higher benefits of *North–South preferential integration*. Chile, in particular, has repeatedly tried to launch bilateral talks with the United States. But just because Canada and the United States accepted to open their grouping to Mexico does not mean that all Southern countries can count on willing Northern partners: Santiago authorities have indeed no assurance that the US administration will ever obtain the necessary free–track mandate. At any rate NAFTA does not cover a very sensitive — but otherwise crucial for Mexico — area such as freedom of labour circulation; and Brazil was equally successful in overcoming its 1998 crisis despite its different policy stance. Equally important, Southern countries may find unpalatable the urge of Northern partners to include commitments to labour and environmental standards[28]. More generally, countries which still maintain high barriers to trade — like most of Africa's — may still derive higher benefits from unilateral liberalisation, although decreasing trade taxes will have important consequences for fiscal revenues.

x) Capital volatility and the contagion effect can undermine any economic initiative, whether at the national or sub–regional level. However, there is still inadequate co–operation in the domain of *international financial architecture* to address this problem. Policymakers in Latin America are following with interest discussions in Asia between ASEAN, China, Korea, and Japan in view of the

creation of a mechanism for mutual support among central banks in case of a crisis. What of course is peculiar to these countries is that they can count on official reserves which are among the world's largest, at levels that Latin America is unlikely to attain in the short run. For this reason some observers argue that existing regional financial institutions — such as the Fondo Latinoamericano de Reservas, Corporación Andina de Fomento (CAF), Banco Centroamericano de Integración Económica, Banco de Desarrollo del Caribe — could be reinforced in terms of resources and instruments to assist, if needed, countries facing severe liquidity problems (Ocampo, 2000). Already in 1999–2000, when Ecuador faced a severe financial emergency, the CAF came to the rescue by providing a bridging loan while the country negotiated a rescue package with the IMF[29].

Conclusions

What has open, or new, regionalism delivered in Latin America? Can positive experiences be replicated elsewhere in the developing world, and in SSA in particular? What should SSA countries do to avoid the negative side effects of Latin American RIAs? And finally, what implications does the latters' experience have for SSA trade policies, against the background of North–South integration and unilateral WTO–plus liberalisation?

These questions elicit a variety of answers, so that making sense of available evidence is partly dependent on the *a prioris* held by analysts. The debate on regionalism is no exception: sceptics privilege static reallocation effects, supporters contend that this is only part of the story and that integration also includes dynamic and non–traditional consequences[30]. We range ourselves among the latter, not least because we think that even from the viewpoint of traditional effects the evidence is supportive of "open regionalism" in Latin America. In other words, we think that "other" effects are worth considering because they have not materialised to the detriment of consumer welfare. Moreover, sectoral empirical research which pays attention to the micro level of regionalism — where indeed most of the activities associated with an integration process take place — allows a much more precise and optimistic understanding of the dynamic of this process.

Mercosur, in particular, is generally considered as a successful example of open regionalism —and has indeed elicited a great interest in Southern Africa (e.g. Mill and Mutschler, 1999)[31] — for three reasons: the achievement of the statutory objectives in a short period and despite the lack of strong institutions and enforcing mechanisms; the dynamism of trade activity; and the union of Mercosur, in spite of differences over the timing and speed of expansion, in its desire for freer international trade. The historically defensive and mutually distrustful attitude of the two largest members, evidenced by economic and commercial "disconnection" throughout much of their history, has been largely eliminated. Corporate responses have been supportive of the

integration effort — enterprises eye the regional market when taking strategic decisions — and growing interpenetration, although not always welcome, is also evident in macroeconomic variables. The agreement by its governments to co–ordinate fiscal policy and inflation targets could then help underpin hard–won stability in Brazil and Argentina.

The commitment of these and other Latin American countries to economic co–operation has gained momentum over the past decade. This has, to some extent, been an outcome of changing global economic environment and its apparent unpredictability. Financial market volatility and the apparent bias in the WTO process towards non–OECD countries have become driving forces for the countries in the region: not only have they developed joint positions and strategies, but also, and increasingly, sought ways and means of regulating markets, protecting natural resources and heritage, and fostering the creation of knowledge. This is obviously not to hide that substantial problems remain and that, in more than a few issues, domestic reforms and multilateral, rather than regional, approaches remain more effective and less likely to create distortions. RIAs such as Mercosur can be useful building blocks in the move towards free and open global trade only if emphasis is placed and provisions are made eventually to multilateralise preferences.

In order to remain useful, the analysis of RIAs in Latin America and Africa will have to be widened to new emerging themes, such as, in particular, the consequences for existing groupings and individual countries of North–South integration programmes. Following the NAFTA, other initiatives have been started or are being explored in the Western Hemisphere, such as the Mexico–EU free trade agreement (effective since July 2000), a similar accord between Mercosur and the EU, and the Free Trade Area of the Americas. A rather similar process is underway in sub–Saharan Africa, as recently testified by the South Africa–EU free trade agreement (effective since January 2000) and the new framework for EU co–operation with ACP countries set up by the Cotonou convention. We hope that this paper has provided knowledge and information on the Latin American regionalism experience to African policymakers and that other institutions may act as “honest brokers” to bring interested parties together and provide non–partisan policy advisory services.

Notes

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1. While regionalisation of production, trade and capital flows may be a world phenomenon, the degree to which it is institutionalised varies. In Asia, in particular, RIAs are much looser, and Korea and Japan are indeed the only OECD members which are not signatories of at least one preferential trade agreement. In the ASEAN Free Trade Area, apart from harmonising customs procedures and tariff nomenclature, and fast tracking a common customs valuation method, progress in deepening integration has been limited.

2. Although the focus of this paper is on South–South integration, references are also made to North–South experiences, NAFTA in particular.

3. This argument is far from negligible. It has already been used in favour of European integration. The interlocking of strategic industries such as coal and steel was considered by the founding fathers of the EEC as a way of reducing the risks of intra–European war, especially between France and Germany. Similarly, we stress that the creation of Mercosur contributed to the evolution of relationships between Argentina and Brazil. These countries, which experienced a conflictive relationship in the past, now are involved in a process of co–operation.

4. Whether new technologies may allow (relatively) backward areas to catch up more rapidly is a moot point, although early evidence seems to suggest that agglomeration is, if anything, playing a stronger role (e.g. Le Blanc, 2001).

5. With a one–decade lag, the UN Economic Commission for Africa embraced a similar view. In a broader sense, Pan–Africanism finds its comparison in Latin American *Bolívarismo*, a sentiment that common heritage, language and culture should lead to political union.

6. In this text, "hemispheric" refers to North, Central and South America and the Caribbean; "regional" to Latin America (including Mexico); "sub–regional" to Mercosur and other RIAs.

7. Venezuela actually joined the Pact in 1973, while Chile exited in 1976.

8. Antigua and Barbuda, Barbados and Guyana signed the 1965 Treaty of Dickenson Bay. Membership was widened in 1968 to include Anguilla, Dominica, Grenada, Jamaica, St. Kitts and Nevis, St. Lucia, Montserrat, St. Vincent and the Grenadines, and Trinidad and Tobago.

9. Although the regional Common Market is an integral part of the broader based Community arrangements, it has a completely separate identity juridically. Thus, it was possible for the Bahamas to become a member of the Community in 1983 without joining the Common Market. In 1981 the Eastern Caribbean islands of Antigua and Barbuda, Dominica, Grenada, Montserrat, St. Kitts and Nevis, St. Lucia, and St. Vincent and the Grenadines established an associate entity, the Organisation of Eastern Caribbean States (OECS), which replaced the West Indies States Association (WISA) as the islands' administrative body. The OECS was created after studies indicated that most of the benefits derived from integration were flowing to the larger islands (especially Jamaica and Trinidad and Tobago) at the expense of the smaller.

10. Colombia cut its weighted average *ad valorem* tariff rate from 45 per cent in 1988 to 21 per cent in 1990 and to 11 per cent by 1992. Venezuela reduced its *ad valorem* tariff rate from 26 per cent in 1988 to 12 per cent in 1992 and Ecuador's rates went from 29 per cent to 10 per cent between 1990–92. Furthermore, most non–tariff barriers were eliminated in the region by 1991: their coverage was 0 per cent in Bolivia and Ecuador in 1991–1992, 1 per cent in Colombia and 5 per cent in Venezuela.

11. In the case of agricultural goods, CET rates now range between 0 and 40 per cent. The average applied CET Most–Favoured–Nation (MFN) tariff is currently 9.1 per cent, down from 11.2 per cent in 1997. For agriculture, the average is 19.1 per cent (down from 19.6 per cent) and for industry, 7 per cent (down from 9 per cent). In general, the tariff structure offers higher protection to final consumption goods and agricultural products than to inputs and capital goods. Final goods that compete with domestic or CARICOM production face the highest rates.

12. Together with the Africa Growth and Opportunity Act, this constitutes the Trade and Development Act of 2000, extending preferential treatment to a broad range of imports from 48 sub–Saharan African and 23 Caribbean Basin countries. The Caribbean Basin Trade Partnership Act came into force in October 2000 and will be effective until 30 September 2008, or the signing of the Americas Free Trade Agreement, or of another trade accord between the United States and the Caribbean Basin nations (Gitli and Arce, 2000).

13. See Robinson and Thierfelder (1999) for a review of multi–country CGE models which analyse RIAs and overwhelmingly show that trade creation dominates trade diversion.

14. The high elasticity of intra–area trade to total economic activity — an abrupt fall in the last two years of the past decade followed by an equally fast recuperation in 2000 — suggests a high level of complementarity in the production structure of Latin American countries.

15. The gravity model analyses flows of bilateral trade based on analogy with the law of gravity in physics:

    $T_{ij} = AY_iY_j/D_{ij}$, where T_{ij} is exports from country i to country j, Y_i, Y_j are their national incomes, D_{ij} is the distance between them, and A is a constant. Other constants as exponents and other variables are often included. See *Deardorff's Glossary of International Economics* at http://www–personal.umich.edu/~alandear/glossary/g.html.

16. Computable general equilibrium refers to economic models of microeconomic behaviour in multiple markets of one or more economies, solved computationally for equilibrium values or changes due to specified policies. The equations are anchored with data from the countries being modelled, while behavioural parameters are either assumed or adapted from estimates elsewhere. We thank Michael J. Ferrantino of the United States International Trade Commission for sharing with us his review of the CGE literature on trade integration in the Americas.

17. The result from Diaz Bonilla and Robinson holds even when considering only the pure–Mercosur scenario (i.e. the regional agreement only, without the small unilateral trade liberalisation of the full scenario).

18. Certainly not in terms of trade diversion, as domestic markets were basically closed to imports before the early 1990s.

19. Peru reported losing several warplanes and almost 50 soldiers; Ecuador's official toll was about 30 dead and 300 wounded, but the casualties on both sides most likely were greater.

20. In October 1998, the two countries signed a peace treaty defining the 48–mile stretch of border, creating a committee to resolve boundary issues peacefully, and setting down terms for bilateral trade and navigation rights.

21. On the other hand, Brazil has taken a less favourable attitude than Argentina *via–à–vis* the formation of the Free Trade Area of the Americas.

22. Although the nominal anchoring was *a priori* relatively flexible because it was accompanied by a fluctuation band that could be modified according to conjunctural developments.

23. This strategy appears justified since Mercosur countries, and Brazil in particular, trade extensively with Europe and have a sizeable euro–denominated foreign debt. In the long term, member countries may therefore decide to peg their currency (or a common one) at least partly to the euro, in a basket where the US dollar would still account for a larger share. On the likely effect of the euro in Latin America, see Miotti, Plihon and Quenan (2001).

24. In particular, smaller countries — especially small islands and land–locked nations — face a number of structural impediments that, at least in the developing world, offset any advantage that smallness may present in terms of higher socio–political cohesion. In small economies it is difficult to attain minimum efficient production scale, to capture gains from specialisation, to benefit from interactions with complementary firms and sectors (so–called economies of agglomeration), and to reduce transaction costs, especially in the presence of indivisibility and for islands (CEPAL, 2000, chapter 11).

25. The Agricultural Marketing Protocol and the Oils and Fats Agreement regulate intra–regional trade *via* buy–and–sell accords at fixed prices. According to the Guaranteed Market Scheme, in certain circumstances Jamaica, Barbados, and Trinidad and Tobago will purchase fixed quantities of agricultural products from the other, smaller members.

26. Buried among the negative news of 1999 was for instance the fact that Mercosur's dispute settlement system, set up by the Brasília Protocol, was activated twice, or that Argentina and Brazil agreed mutually to recognise quality certificates and technical requirements for a series of industrial products.

27. Besides making it easier for exporters to ship to overseas markets, better infrastructure may accelerate the adjustment of inefficient regional producers whose competitiveness is solely based on positive price differentials due to high transport costs.

28. A useful introduction to this theme is provided by OECD (2000).

29. We thank Andrés Solimano for this information.

30. This is also true within each country, as shown by Chudnovsky *et al.* (2000), who argue that the consensus that emerged between "orthodox" and "heterodox" Argentinian economists in the mid–1990s concerning the benefits of Mercosur has been challenged by the crisis that followed the devaluation of the real.

31. President Thabo Mbeki of South Africa took part at the twenty–first Mercosur Summit in Florianópolis, Brazil in December 2000, the second Head of State outside South America to attend and address the Presidential Summit after former President Nelson Mandela, on 24 July 1998, in the Argentine city of Ushuaia. A Framework Agreement was signed between South Africa and Mercosur establishing terms of negotiations for a Free Trade Agreement.

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Infrastructure for Economic Development in Africa

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Introduction

Physical infrastructure, comprising telecommunications, power, transport, water supply, and information technology, is often viewed as the "wheels" of economic activity since it provides the environment for productive activities to take place and facilitates the generation of economic growth. In the absence of adequate power, water, transport and communication facilities, for example, production processes or locational advantages may not be optimised. By efficiently moving goods and services to where they can be used most effectively, transport adds value and spurs growth. The provision of power permits the use of modern technologies and processes. Efficient infrastructure development is necessary if the national economy is to be integrated and the benefits of economic growth are to be spread throughout a country. The provision of infrastructure encourages investment in less developed areas, allows wider movement of goods and people, facilitates information flows and helps commercialise and diversify the economy. The development of regionally focused infrastructure projects facilitates the process of regional integration and assists in increasing the project size. The larger scale economies will attract private investment and enable the development of transport networks, telecommunications, power and markets that sustain expanding private sector activities and regional markets. Infrastructure services are central to poverty reduction. The activities of households and the lack of access to infrastructure are real welfare issues, particularly in rural areas where poverty is most predominant. The existence of an adequate rural infrastructure is a *sine qua non* for successful rural transformation and agricultural development.

Inadequate infrastructure in Africa is a major obstacle to the region's economic growth, and adversely affects the living standards of its people. The inadequate state of infrastructure has adverse impacts on health, education and the capacity of local producers as well as their ability to compete in international markets. The purpose of

this paper is to take stock of the state of infrastructure in Africa and assess the significance of infrastructure in the development of the continent. The paper also explores the strategies and policies required for improving infrastructure services in the pursuit of Africa's overarching objectives of regional integration, private–sector–led growth and poverty reduction.

Why Infrastructure is Important for Africa's Economic Development

Infrastructure is essential for virtually all aspects of economic growth. It is both an intermediate input into the production of other sectors, such as power and water inputs into manufacturing and agriculture which raises factor productivity, and a final good, providing services directly to consumers such as water and power for households. At the macroeconomic level, the evidence shows that there is strong association between infrastructure spending and growth of real GDP, and that investment in infrastructure has a very high return. One of the well–established patterns of this association is that as national income grows the share of infrastructure in GDP rises (ADB, 1999). However, at higher income levels, as in developed countries, it is power and telecommunications that tend to have higher shares in GDP than roads or water. At low–income levels, as in developing countries, water shows the highest GDP share followed by transport. It can generally be asserted that although infrastructure plays an important role in stimulating and facilitating directly productive activities, the presence of complementary resources and favourable economic environments are also crucial in triggering and sustaining the process of growth. While there are several ways in which infrastructure can impact economic growth, this paper concentrates on the relationship between infrastructure and two important elements which are vital for African countries: global competitiveness and poverty reduction.

Infrastructure and Export Competitiveness

The centrality of regional and international trade to the process of economic growth cannot be overemphasised. Export performance sets the limit to which investments and growth can be expanded without encountering balance of payments and debt repayment problems. The export performance of African countries in the last two decades has, however, been unsatisfactory. Africa's share in world trade declined from about 5 per cent in the early 1980s to 2 per cent currently. This is the direct result of the displacement of Africa's exports by new and relatively efficient suppliers from other developing regions. For instance, over the last two decades the region's market shares in cocoa beans fell from 80 to 60 per cent. In coffee, Africa's share declined from 25 per cent to 14 per cent; in cotton from 31 per cent to 17 per cent; in timber from 13 per cent to 7 per cent; and in iron ore from 12 per cent to 2 per cent. The loss of Africa's market share in cocoa beans, coffee and timber was mainly to Asian countries; in iron ore to Latin American countries; and in cotton to Eastern European countries. Table 1 provides an example of how Africa lost its market share in traditional commodities to Asia.

Table 1. **Africa's Loss of Traditional Markets to Asia**

	International Export Market Shares					
	Africa		Change	Asia		Change
	1970	1993	%	1970	1993	%
Cocoa	80.3	60.1	-20.2	0.4	20	19.6
Coffee	24.6	14.3	-10.3	4.9	10.9	6
Rubber	7.4	5.6	-1.8	89.1	90.8	1.7
Timber	13.4	7.3	-6.1	43.3	52.5	9.2
Cotton	30.7	17.2	-13.5	16.6	35.6	19

Source: Computed from IMF *Direction of Trade*, various issues.

Competition in regional and international markets is especially dependent on the availability of adequate and efficient infrastructure. Infrastructure development is one of the major determinants of price and non–price competitiveness in international markets. Although the effect of infrastructure cuts across the distinction between the price and non–price elements of export competitiveness, some generalisations can be made. Viewing infrastructure services as intermediate inputs, low cost and high quality of any form of infrastructure service will tend to improve price competitiveness. Also, by improving communication between exporters and importers and allowing timely and safe delivery of goods, infrastructure can improve non–price competitiveness. The relationship between infrastructure and export competitiveness is illustrated below.

Price Competitiveness

Price competitiveness is measured by the export price of a country relative to the price of competitors; both valued in a common currency. A country whose export prices are higher than the price of competing countries selling the same product is said to be uncompetitive and will lose its market share. Among the interrelated factors contributing to a country's price competitiveness are labour unit costs, wage/ productivity relationship, exchange rate and transport costs. Reduced competitiveness emanating from transportation costs is evident in many African countries. In Africa transport costs are generally higher than those in other regions constituting a large portion of export (fob) prices. This is partly due to geography in the case of landlocked economies, and partly because of the slow and high cost nature of the transport network. High transport costs in moving goods between countries mean that there are significant natural barriers to trade within the region and that, therefore, there can be significant differences between countries in prices for similar goods, even after the lowering of import tariffs on intra–regional trade.

The effect of transport costs on competitiveness is best illustrated with reference to landlocked countries. Table 2 gives average transport costs for exports from the border to the exit ports of Mombasa or Dar es Salaam in the early 1990s. Transport costs are given as a percentage component of the total costs measured by (cif) prices.

Table 2. **Internal Transport Costs for Landlocked Countries**
(% of cif price)

	Uganda		Burundi		Rwanda		Zaire	
Imports	BB	CNT	BB	CNT	BB	CNT	BB	CNT
Mombasa								
Road	16.5	9.3	27.0	13.8	26.2	-	32.0	16.0
Rail	11.9	7.5	-	-	-	-	-	-
Dar es Salaam								
Road	18.7	8.6	22.8	10.5	22.8	-	16.0	7.0
Rail	23.0	5.3	13.4	6.5	-	-	23.0	7.0
Exports	BB	CNT	BB	CNT	BB	CNT	BB	CNT
Mombasa								
Road	10.6	9.6	17.4	13.6	16.3	12.9	20.0	16.0
Rail	10.3	8.8	-	-	-	-	-	-
Dar es Salaam								
Road	8.1	9.0	25.8	11.3	9.8	10.7	17.0	12.0
Rail	10.2	10.5	10.7	11.7	10.0	10.9	16.0	12.0

Source: World Bank (1998).

They vary depending on whether break–bulk (BB) or containerised shipments (CNT) are possible, with the latter usually cheaper owing to economies of scale. Clearly, transport costs constitute significant proportions of total costs. In the case of Burundi, for instance, road transportation to the port of Mombasa using containerised shipment constitutes about 14 per cent of the total export price, while the cost of break–bulk is much higher reaching about 26 per cent of the total export price (see Weiss, 1998).

In addition to the high cost of domestic transportation, another factor that reduces price competitiveness is the fact that international transport costs paid by African exporters are higher than those incurred by other developing countries. A study on exports to the US (Amjadi and Yeats, 1995) found that freight charges (approximately the difference between cif and fob prices) as a proportion of cif value are higher for African exports than for similar goods from other low–income countries by about 20 per cent on average. The problem is particularly acute for processed primary goods with freight rates that escalate with the degree of processing. This high freight element is attributed to lack of competition in cargo reservation policies of many African economies, where it has been common to introduce a 40–40–20 division of trade between national fleets. This means that 40 per cent of cargo is reserved for carriers of the exporter country, 40 per cent for those of the importer and only the remaining 20 per cent is subject to open competition. There have been suggestions that freight costs for African trade may fall by as much as 50 per cent if all such trade is subject to open competition (Weiss, 1998; Amjadi and Yeats, 1995).

Power supply in many African countries, which is known for its unreliability and high cost, is also a constraint on production efficiency and competitiveness. A survey of small firms in Ghana in the early 1990s, for instance, cited power outages, transportation costs and other infrastructure problems among the top four problems of operation, behind business taxes, with this response strongest amongst very small firms (Steel and Webster, 1991). A survey of manufacturing establishments in Nigeria reported that total expenditure on all types of infrastructure averaged 9 per cent of variable costs, with electric power taking half of this share (Lee and Anas, 1992). Unreliable power can lead to production interruptions, loss of perishable goods, damage to sensitive equipment and loss of orders. To avoid these problems firms tend to invest in their own power supply in the form of private generators. However, the purchase of generators represents an addition to fixed costs, incurred regardless of the scale of firms' output. This tends to raise the capital requirements of existing firms, reduce their production capacity, increase production costs and reduce competitiveness. By discouraging new investments, problems related to the inadequacy of infrastructure can also reduce non–price competition (Table 3).

Table 3. **Cost of Private Infrastructure Investment among Nigerian Manufacturers**

Privately provided machinery and equipment	Average cost ($ 000)	Small Firms	Large Firms	All Firms
Generators for electricity	127.2	24.8	10.1	10.4
Boreholes for water supply	34.9	2.8	1.9	1.9
Vehicles for garbage disposal	8.6	0.2	0.5	0.5
Radio equipment to substitute for telephones	11.2	1.5	0.6	0.6

Note: Infrastructure per firm as a percentage of a total investment, unless otherwise stated.

Source: Lee and Anas (1992).

Non–price Competitivenes

Non–price competitiveness encompasses all those factors, other than price, that affect a country's market share. These factors are normally grouped into two broad aspects: the first is related to the act of selling or marketing; and the second is related to the product sophistication or what is called by Hussain (1997) the income–dimension of global competition. This relates to the ability of the export product to capture a higher proportion of world income growth. The quality and quantity of infrastructure services are important determinants of both aspects.

Marketing Aspect

Marketing depends on the improvement of packaging, foreign contacts, the speed of delivery of products and the provision of after–sale services in the case of durable goods. These aspects are determined in part by the availability of transport and export–servicing facilities such as ports, airports and communications, which provide faster, safer and more reliable movement of goods in order to make it possible for more trade to take place. Thus, even if African exports are price competitive, the inadequacy of elements pertaining to good marketing could drastically reduce their ability to compete. For example, it is found that, on average, transporting between Kampala and Mombasa took 40 days in 1997 with a further 20 days for transit to European ports (Rudaheranwa, 1998). With a three month time lag between order and delivery, an importer from Europe would be inclined to look for alternative suppliers. Indeed, empirical evidence reveals that about 75 per cent of the decline in Africa's international market share was attributed to this aspect of non–price competitiveness, while the remainder (25 per cent) is explained by non–price factors (see ADB, 1995).

An inadequate flow of trade information is among the important determinants of marketing outcomes. Trade and commercial activities record their best performance when producers, exporters and consumers are made to be aware of each other's products and product quality, and supply and demand capabilities. These functions are traditionally performed by trade exhibitions, trade promotion organisations, business travel, embassies and contacts through telephone or facsimile. In the present information age, technology offers effective methods to perform these trade promotion functions and to improve competitiveness in international markets. For instance, using the Internet, it is possible to access online information on markets, market regulations, prices, potential buyers and many import–export data. The use of PCs for data processing will speed up delivery time by improving the internal and external networks, export–servicing facilities and customs operations, and reducing transaction costs.

The application of information technology will also make it possible for export producers to "disintermediate" middlemen and conduct their transactions directly with importers or export markets, thereby increasing their profitability and incentives to produce. Equipping regional trading communities with efficient information technology systems that provide them with accurate and relevant information and exchange mechanisms could be developed to become a major means of enhancing the growth of inter–African trade.

Some African countries have embarked on using information technology for the promotion of regional and international trade. Mauritius, for instance, instituted a trade system with an initial investment of $1 million that reduced the transaction costs associated with external trade. The customs processing time was also reduced from 48 hours to only 30 minutes, and the time it takes for most goods to be declared to one to two days instead of five to 20 days (Talero and Gaudette, 1996). However, as will be discussed in the next sections, the state of information technology infrastructure in Africa would need to be improved substantially in order to exploit the full potential of this conduit.

The Income Dimension

An important factor that contributed to the decline in Africa's international market share is the inadequate development of alternative products, such as manufactures, which command larger international demand. The markets for such knowledge–based products are promising because their demand increases more than proportionately with the growth of global income. This feature of trade has gained significance in today's globalised world as countries strive to build dynamic export sectors and acquire new competitive advantages in products where world demand will be high, technological progress will be rapid and labour productivity will rise fast. However, much of the continent continues to depend heavily on the export of a few primary commodities. Even as we enter the 21st century nearly 80 per cent of African countries continue to depend on only one or two primary commodities for over 50 per cent of their export earnings.

While the persistence of this pattern of production and trade can be attributed to many political and economic factors, the root cause may be traced back to the trade–infrastructure nexus established during the colonial era. Africa's road, rail and other infrastructure networks generally have been established to run from centres of production to seaports with little inward expansion (see Simuyemba, 1999). This is because the systems are geared to bulk outward transportation of primary commodities and importation of raw materials and finished products with the colonial power as opposed to inward distribution of finished products traded among African countries. This system has direct implications for the pattern of both trade and infrastructure development in Africa and continues to retard the development of alternative exports.

The promotion of manufacturing exports requires building healthy capabilities in industries with difficult technologies, and a long, risky and costly learning process (Lall, 1996). A premature exposure to international competition (where latecomers have to face firms that have already undergone the learning process) may lead to the abortion of the industrialisation process. As has been shown by the experiences of many developed and developing countries, the starting point of building these capabilities is to produce, first, for the domestic and regional markets. Important transport and communications constraints, as evidenced by the lack of inward–oriented infrastructure networks, discouraged the successful development of infant industries that target domestic and regional markets in many African countries.

Also, the scope of industrial dynamism through intra–industry trade in Africa, which is essential for the promotion of income–attractive exports and deepening regional integration, is partly constrained by the inadequacy of infrastructure services. Production sharing, which is the engine of such trade, involves the initiation of part of a manufacturing process in one country and the transfer of the activity to another country for further processing. Intra–industry trade increases scope to realise the gains from specialisation and the promotion of differentiated products. Intra–industry trade is very small or non–existent among many African countries. The few African countries that have managed to establish a reasonable industrial base (such as Egypt, Tunisia, Mauritius, Kenya and Zimbabwe) are far from each other and face infrastructure

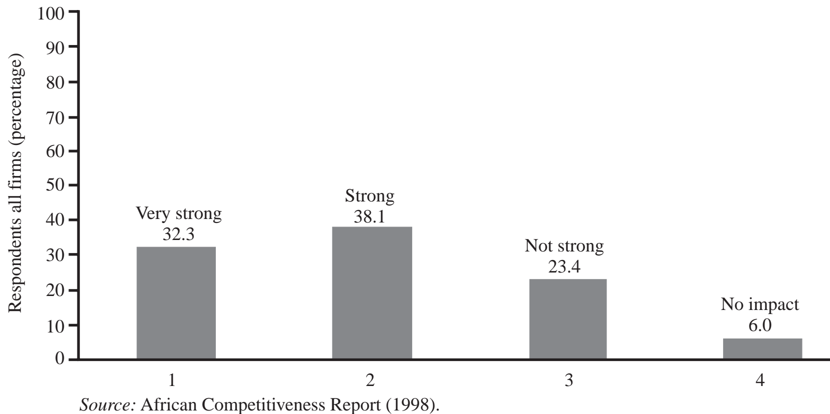
constraints that limit their ability to trade with each other. Furthermore, foreign direct investment, which provides proven channels for technological advancement and development of alternative exports, is also discouraged by the poor state of infrastructure.

Competition for Foreign Capital

An important dimension of global competitiveness, which is becoming increasingly significant, is related to competition among countries to attract private capital inflows in the face of declining public flows. Africa has fared badly in such a competition. The continent has not been successful in capturing an increasing share in the enormous growth in private direct and portfolio investment of the last two decades. Net private capital to all developing countries, comprising portfolio and direct investment, increased 17–fold between 1980 and 1996. In contrast, net private capital flows to Africa during the same period increased by just over twofold. Regions and countries that attract and hold private investors are those with stable political and economic environments, open markets, minimal regulation and low production costs. In addition to these fundamentals, the state of infrastructure has been shown to play an important role in the determination of the direction and magnitude of private capital flows. In making an investment location decision, a potential investor will examine the availability, cost and reliability of infrastructure — power, water, transport and telecommunications. If these are not favourable, the investor is unlikely to locate. This translates not just in loss of investment for a location or country, but is a high opportunity cost in terms of lost employment, incomes and potential economies of scale arising from linkages in the supply–distribution–consumption chain (Simuyemba, 1999).

The evidence obtained from a recent survey of African businesses which measures the competitiveness index of 23 African countries shows a strong correlation between the quality of infrastructure and the sentiments of foreign businesses. The index of competitiveness takes into account the state of infrastructure together with other characteristics of interest to businesses such as political and policy stability, taxes and corruption. The results show that firms indicate strong feelings about infrastructure's importance in their business decisions and operations; it ranks high on the list of complaints for all businesses and third for foreign–owned firms (Figure 1).

Figure 1. **Impact of Infrastructure on Foreign Direct Investment**



Source: African Competitiveness Report (1998).

Firms overwhelmingly indicate that roads are most important, followed by airports.

Infrastructure and Poverty Reduction

There are two possible routes by which new or improved infrastructure activity can help reduce poverty. First, there is the link between infrastructure and economic growth discussed above. There is general agreement that higher rates of economic growth are essential if substantial reductions of the numbers living in poverty are to be achieved. However, on the basis of the existing distribution of income and population growth rates in the region, it is likely that GDP growth of some 7 per cent annually will be required just to reduce the absolute number of the poor. This figure substantially exceeds the growth achieved in most countries in the last two decades. At any given growth rate the reduction of poverty could be accelerated by ensuring that the growth that takes place is pro–poor. This refers to a process of growth that makes the share of the poor in additional income growth higher than their share in existing income, which makes their incomes grow more rapidly than those of the non–poor (Weiss, 1998).

The second link between infrastructure activity and poverty reduction arises through the contribution of infrastructure to the process of pro–poor growth. The poor are usually identified with inadequate access to infrastructure services such as clean water, sanitation, and transportation and communication, which are considered as “input indicators” of poverty. These limit their access to another set of “input indicators”, namely health services, education facilities, food and markets which will have a negative impact on the set of “output indicators” of poverty such as life expectancy, literacy, income and nutrition. Hence, the provision of infrastructure services can directly reduce poverty through its effects on its input and output components.

To achieve this requires the identification and financing of a significant number of projects for which a high proportion of the beneficiaries will be below the poverty line for the country concerned. Not all infrastructure projects will have this characteristic, but it is through this route that infrastructure activity can make its main contribution to the process of poverty reduction. Water supply and sanitation, and rural transportation projects, are the components of infrastructure most likely to promote pro–poor growth[1].

Water Supply and Sanitation

The Policy Paper of the African Development Bank on Health establishes that the primary causes of disease and ill health amongst the poor are water–related, such as the prevalence of diarrhoeal diseases. Some of these water–related health problems can be contained through the provision of safe water and hygienic sanitation services. Investments in water supply and sanitation are thus central to improving public health. It is estimated that 80 per cent of endemic disability in developing countries is due to diarrhoeal disease. A review by the WHO demonstrates that improvements in water supply and sanitation have a direct and significant payoff in reducing diarrhoeal morbidity, particularly among children. It has been shown that when both water quality and water quantity are improved, diarrhoeal morbidity rates can be reduced by some 37 per cent. When health education and excreta removal are carried out, the reduction in diarrhoeal disease reaches about 50 per cent and more. In Guinea, well construction plus health education have cut the rate of infection from guinea worm disease (dracunculiasis) by 85 per cent. Similar results have also been recorded in rural areas in Togo, Mali, Nigeria and Burkina Faso.

Observations in Egypt show a large and statistically significant reduction of schistosomiasis as a result of the installation of community standpipes. Trachoma infection is the leading cause of loss of vision and blindness in poor countries. Personal and public hygiene emphasising the use of water is among the most effective methods for prevention or reduction of trachoma. The use of adequate amounts of water for personal hygiene also reduces the prevalence of skin and fly–borne diseases. Improvements in water supply and sanitation have been shown to aid and enhance other measures tending to ameliorate the nutritional status of communities. The prevention of diarrhoeal diseases improves nutrition because such infections decrease food intake and increase metabolic loss.

Benefits to the poor from improved water supplies arise not just through improvements in health, but also through the positive impact of good health on productivity and output growth. Benefits from the improved availability of water can also be viewed as savings in collection time, of which some portion may be used for leisure and the rest for productive activities such as in agriculture.

1. This section draws on Weiss (1998) and ADB (1999).

In rural areas it is well established that water collection is the responsibility of females and from a series of case studies the average time rural women spend on domestic transport (water and fuel wood collection) is in the range of 0.9 to 2.2 hours per day (Barwell, 1996). Women in Africa spend a considerable amount of time and resources fetching water. The delivery of water to households means that more time will be devoted to other functions such as childcare or income–earning activities.

Water supply and sanitation programmes in rural areas will also facilitate community organisation and development among rural populations. The efficient and effective design, implementation and operation of these programmes will instil direct expressions of community cohesion and involvement. Participation in rural water supply and sanitation projects will thus enhance community involvement and foster the community's willingness to apply its experience to other poverty–reducing activities such as literacy and vaccination campaigns.

Rural Transport

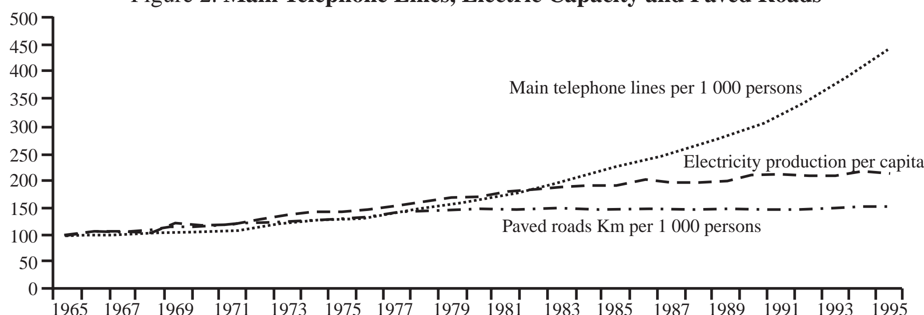
Improvements in rural feeder roads and paths have the potential to improve the position of the poor in several ways. Evidence from surveys in Zambia, Uganda and Burkina Faso suggests that the average rural adult spends 1.25 hours per day on essential travel and transport. Of this time, 75 per cent is for domestic purposes (including collection of water and fuel wood, and trips to a grinding mill to produce ground flour for family consumption). The share of agricultural activities (covering trips to the fields for different cultivation activities, movement of farm inputs, collection of harvested crops) is 18 per cent, while the share of health visits to rural clinics or doctors is only 1 per cent. The remaining 6 per cent are for marketing of crops. The average adult also spends a carrying effort equivalent to moving a load of 20 kg over 2 km a day (Barwell, 1996).

Improvements in rural transport can raise incomes of the poor through several mechanisms. First, agricultural output can benefit particularly where bulky low value crops are involved. For instance, trucks can be hired to move bulk produce to the market and fertiliser can be moved to the farms and stored close to where they are needed. Also, improved tracks and footpaths facilitate the movement of hired farm labour to the fields. Second, in isolated rural areas where communities will have great difficulty in marketing their produce, crops can also be moved in smaller quantities by cart or bicycle if adequate roads or paths are available. Likewise, access to social services and non–agricultural income–generating activities including schools and health clinics for which travel time is reduced, and travel from semi–urban locations to work in services and construction in the urban sector.

The Status of Infrastructure in Africa

In the decade immediately following independence, the public sector in Africa made significant strides in promoting infrastructure development. For instance, the average provision of main telephone lines per 100 inhabitants in 1980 was 0.74, a 64 per cent increase from 0.45 main telephone lines in 1965. In 1986, this figure increased again by 43 per cent to 1.06 mainlines. In the same way, electricity production increased from a per capita of 43 kilowatts in 1965 to 87 kilowatts in 1986, a 100 per cent increase, only to remain virtually stagnant since then. The density of paved roads also exhibited a similar trend, with the length of paved roads per 1 000 persons increasing during the period immediately following independence until 1986 but stagnating thereafter (see Figure 2). Apart from some elements of ideological orientation, the primary rationale for public sector involvement in infrastructure was to address what was perceived as pervasive market failures in African economies.

Figure 2. **Main Telephone Lines, Electric Capacity and Paved Roads**



However, the decade following the 1980s witnessed an increasing disillusionment with the performance of public enterprises in general. The explosion of urban populations and subsequent shrinking of resources in the wake of economic crisis after the mid–1980s have meant that public provision of infrastructure services is for the most part now characterised by less than adequate performance, especially with respect to resource allocation and enterprise management. The combination of poor management, inadequate capital structures, bad investment decisions and the bureaucratisation of the decision–making process halted and reversed earlier progress. The state of Africa's infrastructure can be characterised as follows:

Inadequacy of Provision

The provision of infrastructure services in Africa falls short both in comparison with other developing countries as well as in relation to the needs of the African peoples. With only 14 million telephones, Africa's share is only 2 per cent of the world's telephone lines (Table 4). There are more telephones in Brazil than in the whole of Africa. The continent is also characterised by low teledensity measured as the number of main telephone lines per 100 inhabitants. In 1999, Africa averaged two compared with 30 in the Americas, six in Asia and 31 in Europe. In the water sector only 60 and 40 per cent of the region's urban and rural population, respectively, had access to safe water. Africa's performance in terms of access to sanitation is equally poor. In 1995, only 36.6 per cent of the population had access to sanitation compared with 51 per cent in East Asia, 64.1 per cent in Latin America and 96.7 per cent in OECD countries.

Table 4. **Infrastructure Indicators by Region**

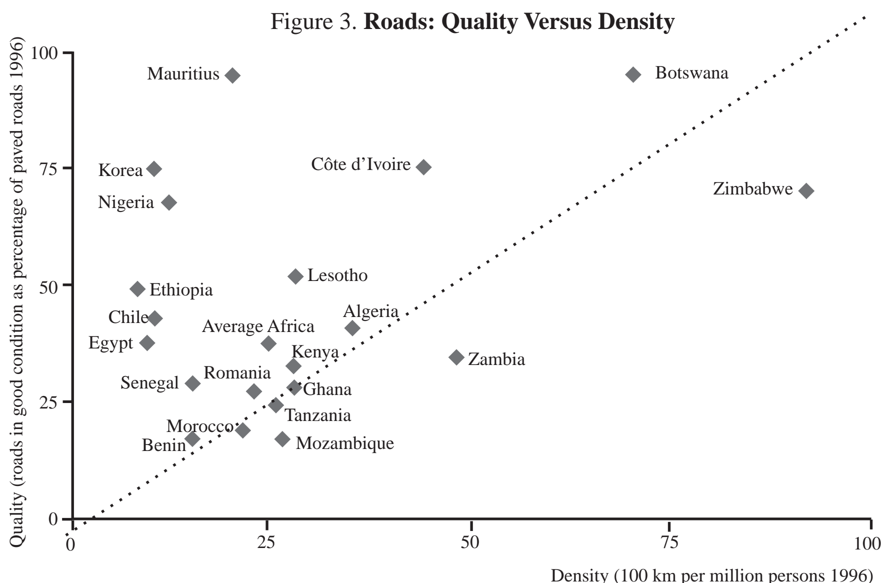
Country Group / Region	Electric power consumption per capita (kilowatt) 1997	Telephone Mainlines Per 1 000 people 1998	Paved roads (Percentage of total roads) 1997	Population with access to safe water (per cent) 1995	Population with access to sanitation (per cent) 1995
Lower middle income	1 737	115	50.7	75	..
East Asia and Pacific	771	70	17.4	77	..
Europe and Central Asia	2 692	200	86.5	..	..
Latin America and Caribbean	1 402	123	26	75	68
South Asia	324	19	57	81	20
Middle East and North Africa	1 158	81	50.2	..	..
Sub-Saharan Africa	446	14	15	47	47

Source: World Bank, 2000.

Road infrastructure in Africa is also poorly developed. The data available show that Africa had approximately 311 184 kilometres of paved roads in 1996, with half of them in poor condition. With the exception of Mauritius and the North African countries of Algeria, Egypt, Morocco, and Tunisia, paved roads account for less than 50 per cent of the road network in Africa. Indeed, paved roads in Sub–Saharan Africa account for less than 17 per cent of the road network in 1996, with many countries falling below the average. About 57 per cent of the roads in North Africa were paved compared with 25 per cent in Southern Africa and 10.2 per cent in Central Africa. Road density per km^2 is generally much lower than that of Asia and Latin America.

With regard to both density relative to population and quality of roads, Figure 3 shows the record for 22 African countries selected according to data availability, compared with the three developing countries, namely Chile, Republic of Korea and Romania. Among the countries in the sample, Zimbabwe and Botswana have a good record on both counts. Mauritius, which outperforms Korea on both density and quality, has a large proportion of its roads in good condition, but its road density is lower than the average for Africa. Côte d'Ivoire and Nigeria have relatively good road conditions, while Gabon has a relatively high density of roads. The bulk of the remaining countries in the sample are in the south–western quadrant of the figure where density is less than 500 km of roads for one million persons and less than 50 per cent of paved roads are in good condition.

Figure 3. **Roads: Quality Versus Density**



The air transport network in Africa is still relatively underdeveloped. All countries in the region have at least one international airport as well as several smaller ones but few of them are capable of handling large amounts of traffic. Less than 50 per cent of the 5 304 potential air links among the countries in the region are actually operational or being actively exploited at present. The countries with the highest number of airports are Egypt (17 airports) and Nigeria (15 airports).

War–affected economies in Africa are perhaps the hardest hit by the inadequate provision of infrastructure services. Physical infrastructure stocks — telecommunications, airports, ports, roads, bridges — are often key targets during war. Although some parts of these countries may not be directly affected by war, infrastructure maintenance is neglected during war, and capital spending is cut back in favour of military spending (see ADB, ECA, WB, 2000).

Unequal Development

The average statistics on Africa mask the large differences that exist between the different regions in Africa. The provision of infrastructure services is heavily concentrated in Northern and Southern Africa. In teledensity, North African countries have three times the Sub–Saharan African rates. Of the 14 million telephones in Africa about 5 million are located in South Africa. The remaining 9 million are so dispersed that the majority of Sub–Saharan Africans live about two hours away from the nearest telephone. In power generation, Southern Africa produces the largest share of Africa's electricity production — about 55 per cent, which is dominated by hydroelectricity and coal–burning generating plants. North Africa accounts for about one–third of Africa's electricity production based largely on burning oil supported by coal and natural gas. West Africa's share of 9 per cent is based on a mixture of hydroelectricity, oil and gas. Central Africa's share of 4 per cent is dominated by hydroelectricity and East Africa's share of 3 per cent consists of a mixture of oil and hydroelectricity.

These differences among countries are associated in part with variations in per capita GDP. Countries with higher per capita income, including South Africa, Mauritius, Botswana, Tunisia, Libya and Morocco, have higher penetration rates. Landlocked countries, particularly those in the Sahel including Chad, Niger and Mali, have low penetration rates. Countries affected by conflicts, including Rwanda, Burundi and Somalia, have also not fared well.

Low Quality and High Cost

Africa's infrastructure services are also of low quality and high costs. One measure of quality of telephone is faults per number of main lines. The average faults per 100 main lines for the region in the late 1990s was 78 compared with average rates of 8.9 for America, 19.9 for Europe and 43.7 for Asia. Another measure of quality is speed of delivery. In spite of high cost of services, the demand for telephone services remains high with the waiting list generally long in countries with higher per capita income. In North Africa, Egypt has the largest number of applicants waiting for service, estimated at 1.3 million in 1996. The waiting list is also high in countries such as Cameroon, Ghana, Kenya, Nigeria, South Africa, Tanzania and Zimbabwe. The overall average expected waiting time for services in Africa in the late 1990s was 3.5 years, the highest in the world, compared with 0.3 in America and 0.7 in Asia. In terms of technological development, Africa's telecommunications infrastructure has not kept pace with the rest of the world. While the rest of the world has been moving towards digital exchanges, the networks in the region are generally analogue with outmoded equipment and high fault rates.

The quality of services in power generation also exhibits similar weaknesses. The region's generation, transmission and distribution systems tend to be old and inefficient, resulting in often substantial losses of generated energy, as much as 40 per cent in some cases. These system losses have further limited the amount of energy

available for production and consumption. Furthermore, in many countries consumers have experienced frequent power outages as well as voltage fluctuations, which damage electronic equipment and motors. Table 5 presents two indicators for selected countries in the region: transmission and distribution losses and rate of return on net fixed assets. Uganda has, for instance, transmission and distribution losses of 38 per cent and a zero rate of return on net fixed assets, while Ghana has lower transmission and distribution losses (17.8 per cent) and a higher rate of return on net fixed assets (6 per cent) than Uganda.

This unreliability has forced many enterprises in the region to buy and install their own generators, thus raising their overhead costs. Because of the unreliability of public supply, self–provision of electricity is common across the region. In Uganda, most large customers maintain stand–by diesel generators. In Guinea, between 1983 and 1992 the private sector installed for its own use some 70 MW of power generation, and in the mid–1990s produced some 109 GWH of electricity, almost as much as the national electric utility.

The quality of maritime transport is extremely poor. Port productivity is, on average, about a third of the international norm as a result of poor management, excessive bureaucracy and inadequate as well as unreliable equipment. Delays in clearing goods are frequently a problem. Most ports in low–income African countries are in need of modern, better–managed facilities to serve traffic for which sea transport has a significant cost advantage over surface transport, such as dry and liquid bulk cargoes or containerised cargo. Manufacturers and suppliers often have to post their employees in the port for several days on end to make sure that the goods move in and out on time.

Table 5. **Power Sector Performance Indicators of Selected Countries, 1993/1994**

	Transmission and distribution losses (per cent)	Rate of return on net asset (per cent)
Ghana	17.8	6.0 (1993)
Côte d’Ivoire	16.3	NA
Mali	21.2	1.2 (1994)
Guinea	27.0	-6.2 (1993)
Sierra Leone	38.5	-16.0 (1993)
Nigeria	30.0	-8.2
Senegal	14.3	3.7 (1993)
Cameroon	13.0	NA
Zambia	8.0	-8.0 (1994)
Zimbabwe	11.0	5.8 (1993/94)
Kenya	12.5	15.0 (1994)
Uganda	38.0	0.0 (1994)
South Africa	7.0	11.5 (1994)
Chile	10.6	8.1 (1994)
Malaysia	15.8	8.2 (1994)
Argentina	25.4	7.0 (1994)

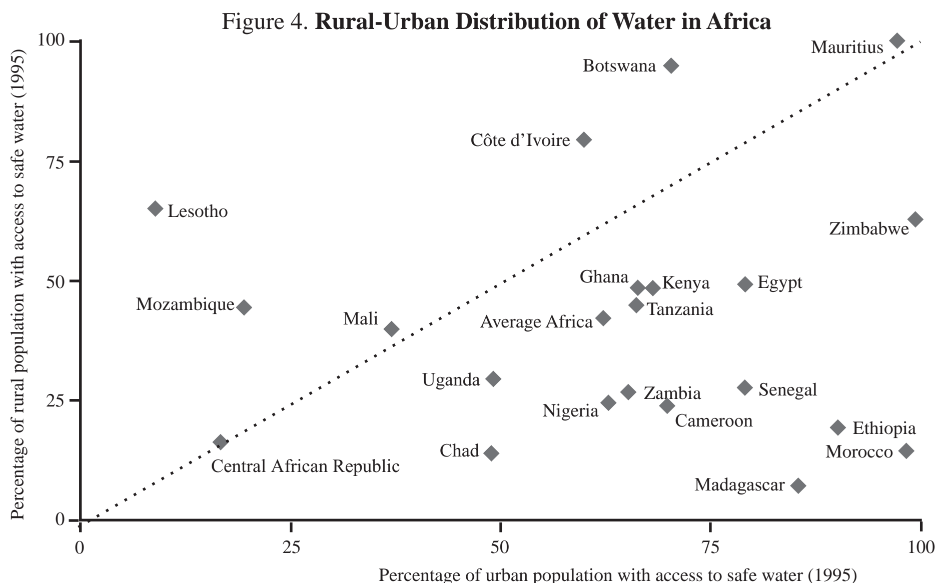
Source: Turkson and Rowlands (1998).

Likewise, most airports lack modern equipment and infrastructure. They are characterised by deteriorating runways, and obsolete traffic control equipment. Much of the infrastructure required for ancillary activities, such as customs and immigration, air cargo, catering, baggage handling and connecting surface transportation, is inadequate to meet market needs. The operational and safety shortcomings that plague Nigeria's international airports have given them the reputation of being among the worst in the world.

Urban Bias

There is also bias in favour of urban centres in the distribution of services. Urban areas account for over 80 per cent of the telephone services, while rural areas, where over 80 per cent of the population reside, have access to only 20 per cent of the service. Two countries, however, had most of their telephone mainlines located in rural areas. These are São Tomé and Principe (87.0 per cent) and Central African Republic (57.0 per cent). The distribution of telephone networks in South Africa presents striking internal contrasts. The average teledensity in South Africa is about 10 per 100 inhabitants, but on a provincial level this falls to about two per 100.

Figure 4. **Rural-Urban Distribution of Water in Africa**



In the water sector, the majority of African countries have a biased distribution favouring urban areas, excepting Côte d'Ivoire, Lesotho and Mozambique where the bias is reversed. There is, however, a substantial variation in different countries with regard to both coverage and rural–urban distribution. As shown in Figure 4, which exhibits the distribution of water services, the range was 18 and 18 per cent in Central African Republic for urban and rural areas, respectively, compared with 95 and 100 per cent in Mauritius. While in these two cases, access to safe water is evenly distributed between rural and urban areas, the Central African Republic shows low coverage, while Mauritius has a full coverage. In comparison with countries in South East Asia, the figure shows that Africa lags behind in terms of both services coverage and rural–urban distribution. However, while Africa has a lower coverage compared with Latin America it marginally outperforms Latin America in terms of rural–urban balance.

Inadequate Regional Linkages

Africa's national and regional markets are not adequately linked. Road networks in Africa have not kept pace with the growing demand: kilometre lengths are limited and their standards of construction often low. And few cities have been able to keep pace with road network needs. Although the construction of regional road networks on a sub–regional basis is crucial for economic co–operation and integration, a real regional African road system does not as yet exist. A large number of separate national road networks are not effectively co–ordinated. As agriculture and industry expand, and as national and sub–regional economies develop, existing road networks will require tremendous extensions and improvements in quality. In particular, road links between nations will have to be strengthened to meet large–scale demand for intra– and inter–regional goods traffic; all of this requires heavy capital investment and expenditure on roads in many African countries.

Railways in Africa are fragmented and can hardly be described as a system. As has been noted before, the railways run from the interior to seaports, a reflection of their antecedent as a transport system designed for external trade purposes. The aggregate network of African railways is estimated at 73 000 route kilometres, of which South Africa alone accounts for some 22 500 km. Countries such as Burundi, Central African Republic, Chad, Cape Verde, Comoros, Mauritius, Seychelles, Somalia, Gambia, Guinea–Bissau and Libya have no railway system. With the exception of North Africa, railways in Africa generally have a low level of traffic. Most of the lines are of light rail, and are unsuited for fast or heavy traffic. Moreover, there is general deterioration due to poor maintenance.

With the exception of Eastern and Southern African railways, the national railway networks in Africa are mostly independent of, and unconnected with, each other. All networks in Africa were built at the end of the 19th century or the beginning of the 20th century, often with different technical characteristics, gauges, couplings, brake

systems, buffers, etc. The only exceptions are Tazara, the Trans–Gabon and the Trans–Cameroon. The 1.067 m gauge predominates, especially in Sub–Saharan Africa, whereas the 1.435 m gauge accounts for 76.1 per cent of the total kilometrage in North Africa. Upgrading existing railway lines would involve major investments in track realignment, resignalling, safety systems and rolling stock. Additionally, border crossings entail high transaction costs. Even if rail systems are compatible, co–ordination between independent systems entails long delays and high costs that lead to a disproportionate share of bulky items being transported by road rather than rail in East and Southern Africa.

Additionally, taxes, licences and insurance requirements raise the direct costs of transport. The lack of regional co–operation in harmonisation of transport policy and in joint exploitation of resources is among the factors that contribute to the absence of adequate regional linkages. For instance, protection of domestic transport operators further raises costs, impedes the development of cross–border tourist circuits, and greatly reduces competition and service in air transport. World–class, low–cost sources of hydropower have not been exploited because of the difficulties, rivalries and uncertainties attached to producing energy in one country for consumption in another — often with transmission across a third (ADB, ECA and WB, 2000).

The Way Ahead

While geographical and structural factors might help explain the current state of infrastructure in Africa, the main barriers to its provision point at the failure of the public sector model. As noted before, almost without exception infrastructure services have been provided exclusively by governments, which own, finance, and manage nearly all infrastructure projects. Public provision typically leads to low efficiency and high costs, with more attention given to job creation in the public sector than to providing services. Low government–fixed prices reduce profitability and discourage investment, whereas high subsidies to insolvent utilities undermine macroeconomic stability and growth.

Disillusionment with public sector performance, combined with the fiscal crises, induced governments to reconsider the public enterprise model and encourage more private sector participation in infrastructure investment and operations. Thus, over the last 15 years, the global private infrastructure industry has been transformed as governments redefine their roles in providing infrastructure services. The consensus that has emerged is that a form of partnership, which provides for the engagement of government, the private sector and the local community, is required to make headway in taking the necessary measures for improving infrastructure services. Such measures include prioritising investment and finance, rehabilitation of existing infrastructure, particularly in war–affected countries, fostering private–sector partnership and regional integration, and harnessing information technology.

Priorities in Investment and Finance

Africa's infrastructure financing needs are difficult to ascertain precisely. This is not only because of the complexity of costing variant types of infrastructure with varying types of technology, but also because such estimates must be anchored on the attainment of certain socio–economic objectives. Crude estimates can be obtained, however, by relating norm values of the stock of infrastructure to either GDP or population and then use projections of these two variables to estimate financing requirements. One such estimate indicates that some $18 billion needs to be mobilised over the next decade in just 21 countries for the power sector alone. Other estimates generally suggest that infrastructure investment requirements in Africa are between 5–6 per cent of GDP, per annum. This implies investment needs of over $250 billion during the next ten years — an estimate which provides an initial indication of the continent's funding requirements, as well as of the investment opportunities in the sector (see ADB, 1999).

With estimates of resource requirements crude as they are, the fact of the matter is that Africa faces severe resource constraints which necessitate drawing clear priorities for both investment and finance. While such priorities should be, by necessity, country–specific some generalisations could be made.

First, there is a need to look for quick–payoff changes that do not involve investment. Such quick payoffs are often found in the domain of regional protocols and arrangements which will be discussed below. These include, among others, improving border crossings for freight and tourists and eliminating unofficial tolls.

Second, given the severe financial constraints in many African countries, spending on rehabilitation and maintenance should be the starting point of efforts to invest in infrastructure services. Inadequate maintenance caused power systems in Africa to operate at only 60 per cent, on average, of their generating capacity available at a given time, although best practice would achieve levels over 80 per cent. Also, water supply systems lose an average of 30 per cent of their output to users, compared with best–practice of 15 per cent (ADB, 1999). However, before starting to invest in rehabilitation, policies should be examined to ensure that incentive systems are conducive to the well functioning of the rehabilitated infrastructure. It is also important to consider whether a facility should be rehabilitated to the same standard as its original construction. However, in extreme cases the state of the facility might have deteriorated so much that rehabilitation might be more costly than establishing a new facility.

Third, private investment may not be forthcoming in a country which is incapable of creating the minimum conditions under which the private sector can operate. In this case, the country will need to draw plans that can solicit the support of international assistance, in the form of grants and concessional resources. The country must also endeavour to strengthen the effectiveness of macroeconomic, institutional and governance reforms that could make international assistance possible. The provision of rural infrastructure may also not be attractive to the private sector and it will require the support of the international community as well as local community participation.

The challenge of infrastructure reconstruction in war–torn countries is especially daunting. Direct war damage, the neglect of infrastructure maintenance investments during the war and poor public policies have left most of the countries with deteriorated water, transport, energy and telecommunications infrastructure. As a consequence of prolonged conflicts, countries tend to be very poor and the challenges of infrastructure rehabilitation and reconstruction are beyond the financial capacity of the governments. War and civil strife are a major impediment for investors who are unlikely to invest in war–affected countries or in post–conflict countries if a renewal of the civil war is perceived as likely, or in countries plagued by civil strife and banditry (see Höffler, 1999).

Fourth, the participation of the private sector could be envisaged both in rehabilitation as well as in new investments. The choice of the appropriate areas where the private sector could be involved depends on technology and market structure. The key to this is whether the market can be made contestable, that is, potentially competitive even if only one firm is active. A starting point is the recognition that infrastructure services can be unbundled into stand–alone services with distinct market structures. The electric power sector, for example, can be unbundled into generation, transmission and distribution (ADB, ECA, WB, 2000). However, it is important to develop appropriate regulations before inviting the private sector to participate actively in the provision of services.

Enhancing Private Sector Participation

Private sector participation in infrastructure yields many financial and efficiency gains. It increases the aggregate rate of investment, reduces public sector financial constraints and strengthens commercial orientation in the provision of services, thereby leading to lower unit costs. Private finance also provides opportunities for expanding the liquidity and depth of local capital markets, which are currently underdeveloped in most countries. Such benefits ensue from several factors, including commitment to cost–covering tariffs, increased pressure for operational efficiency and access to technological and managerial know–how.

Many African countries are thus turning to the private sector with positive responses and encouraging outcomes. For instance, during the period 1994–1996 over 20 large private infrastructure projects with total costs amounting to about $4 billion were concluded with foreign investors. The projects financed by private investment ranged in size from $14 million for Mauritania's Urban Infrastructure Decentralisation project to $1.5 billion for Morocco's Jorf Lasfar Power Project. Although private sector participation covered virtually all infrastructure sectors, its early beginnings were in telecommunications, which provided learning experiences for engagement in other sectors. Over the period 1990–1998, 29 African countries involved the private sector in telecommunications, 15 in the power sector, 12 in the water sector, 12 in airports and 11 in the railway sector. Private participation has been pursued through various approaches, including divestiture, leases, management contracts, and concessional arrangements, such as build–operate–transfer (BOT) and build–own–operate (BOO).

In telecommunications, private sector participation has been predominantly in the form of concessions and demonopolisation (25 cases), followed by divestiture (five cases) and management contract (four cases). Management contracts have been the dominant modality in all other sectors (see Table 6)

With regard to benefits and efficiency gains accruing from private sector participation, the experience of the power sector in Côte d'Ivoire illustrates some of the positive outcomes. In 1990, Côte d'Ivoire decided to privatise operations in the power sector. In the period following privatisation, gross power production increased, average power cuts dropped, the repair time decreased, billing anomalies fell and the tariff collection rate increased. Between 1990 and 1997, electricity subscribers benefited from two price cuts that lowered the tariff by 13 per cent, on average. Furthermore, the number of communities served increased by 30 per cent as a result of the resumption of rural electrification programmes. This was made possible through the increased self–financing capacity of the sector. The power sector has enjoyed the confidence of investors who have financed two independent private power generation projects through investment concessions (ADB, 1999).

Notwithstanding the encouraging progress with private sector participation, much remains to be done to meet the financial requirements for the development of Africa's infrastructure. Given the tight budgetary positions in many countries and the declining trend in concessional flows to the continent, the required investments would need to be significantly financed by private capital, both domestic and foreign. In helping to bring this about, the role of private sector participation would need to be enhanced by further improving the business climate.

A key component of such a climate entails having in place a system of good governance, which addresses issues of accountability, transparency, corruption, human rights and the rule of law. The incentive to private sector participation would be stronger when the regulatory and legal frameworks for commercial infrastructure investments are clear, transparent and enforceable.

In this regard, it is appropriate to note that many African countries have taken concrete steps to provide a favourable climate for private investment. These include making marked progress towards achieving macroeconomic stability; revising existing laws to remove or reduce impediments to private ownership; facilitating profit and capital repatriation; simplifying approval procedures for new investment by starting promotion programmes and setting up "one–stop" investment centres; and becoming members of the Multilateral Investment Guarantee Agency to insure foreign investors against political risks.

These measures are working alongside other drivers to push the African infrastructure market forward. An important driver which is working to enhance private sector participation is the increased realisation, on the part of private investors, that risk perceptions in Africa are often overstated. A measure of the extent to which perceptions of corruption are prevalent in African countries can be obtained from the

Table 6. **Selected Modalities of Private Participation in Telecommunications in Africa**

Modality	Countries	Year
Management contract	Benin	pre 1996
	Botswana	pre 1996
	Seychelles	pre 1996
	Madagascar	pre 1996
Concession/BOT	Guinea-Bissau	pre 1996
	Botswana	1997
	Burundi	pre 1996
	Cameroon	1998
	Côte d'Ivoire	1997
	Dem. Rep. Congo	pre 1996
	Eritrea	pre 1996
	Gambia	pre 1996
	Ghana	pre 1996
	Guinea	pre 1996
	Kenya	1996
	Madagascar	pre 1996
De-monopolise/BOO	Malawi	1995
	Mauritius	pre 1996
	Morocco	1996
	Mozambique	1996
	Namibia	pre 1996
	Nigeria	pre 1996
	Senegal	1996
	South Africa	pre 1996
	Tanzania	pre 1996
	Uganda	pre 1996
	Zambia	1998
	Zimbabwe	1996
	Cape Verde	1995
Divestiture	Sudan	pre 1996
	Ghana	1997
	Senegal	1998
	South Africa	1998
	Uganda	1998

Source: Kerf and Smith (1996) and Business Africa, various issues.

Corruption Index of Transparency International (CITI). The CITI measures the perception of corruption as seen by business people, risk analysts and the general public. The CITI ranges between ten (highly clean) and zero (highly corrupt). The classification of country CITI scores by regions reveals that the degree of corruption in Africa is similar to that of Eastern Europe. The 22 African countries covered by the CITI scored an average of 3.4 points (Table 7). Reference to individual cases in Africa would also support the notion that corruption perceptions vis–à–vis Africa are overstated, because the continent has, perhaps, an image problem. For instance, Nigeria registers the worst record among all the countries covered by the CITI (1.2), but its score is comparable to that of Yugoslavia (1.3). Also, the average score for Africa fares better in comparison with the scores of individual countries that are highly regarded by foreign investors– for instance, Mexico (3.3), Thailand (3.2), China (3.1), Romania (2.9), India (2.8), Russia (2.1), and Indonesia (1.7). In a nutshell, although the degree of corruption in Africa must not be underplayed, the comparison with other developing countries in Eastern Europe and Latin America countries supports the fact that the extent of corruption in Africa is often overstated. Many foreign investors are increasingly recognising this fact.

A second factor is that many investors are realising the need for building relationships in the African continent, which are necessary to take advantage of the emerging investment opportunities. This might be particularly so, in view of the potential market growth in the continent and its rich but under–utilised resources. A third positive factor is the catalytic role played by regional and international financial institutions and financiers such as the African Development Bank and the World Bank. For instance, the World Bank's Partial Risk Guarantee, which has been used in the case of the Jorf Lasfar power project in Morocco, offers full cover against certain political uncertainties, making investors more comfortable with perceived country risks.

It must be remembered, however, that the need to attract more private investment should not detract from the important role of the government as a regulator and as a provider of infrastructure services. As a regulator and facilitator of private sector participation, the government establishes regulatory institutions, sets the platform for private competition in the market and enacts rules that protect consumers. The government should also provide vitally needed services in areas where private sector investment is not forthcoming — for instance, in rural development, and in post–conflict rehabilitation programmes. Government actions in these areas can have significant results especially if supported by increased community participation and, where necessary, by financial and technical assistance from external development partners.

Table 7. **Corruption Perceptions in Africa Compared with Other Regions (2000)**

Country Rank	Country	2000 CPI Score	Surveys Used	Standard Deviation	High-Low Range
African countries					
1	Botswana	6	4	1.6	4.3 - 8.2
2	Namibia	5.4	4	0.8	4.3 - 6.1
3	Tunisia	5.2	4	1.5	3.8 - 7.1
4	South Africa	5	10	0.9	3.8 - 6.6
5	Mauritius	4.7	5	0.8	3.9 - 5.6
	Morocco	4.7	4	0.7	4.2 - 5.6
7	Malawi	4.1	4	0.4	3.8 - 4.8
8	Ghana	3.5	4	0.9	2.5 - 4.7
	Senegal	3.5	3	0.8	2.8 - 4.3
10	Zambia	3.4	4	1.4	2.1 - 5.1
11	Ethiopia	3.2	3	0.8	2.5 - 3.9
12	Egypt	3.1	7	0.7	2.3 - 4.1
13	Burkina Faso	3	3	1	2.5 - 4.4
	Zimbabwe	3	7	1.5	0.6 - 4.9
15	Côte d'Ivoire	2.7	4	0.8	2.1 - 3.6
16	Tanzania	2.5	4	0.6	2.1 - 3.5
17	Uganda	2.3	4	0.6	2.1 - 3.5
18	Mozambique	2.2	3	0.2	2.4 - 2.7
19	Kenya	2.1	4	0.3	2.1 - 2.7
20	Cameroon	2	4	0.6	1.6 - 3.0
21	Angola	1.7	3	0.4	1.6 - 2.5
22	Nigeria	1.2	4	0.6	0.6 - 2.1
Other Regions	Average number of countries	Averages			
		3.4	4.4	0.8	2.6 - 3.5
Eastern Europe	21	**3.4**	4.1	0.7	2.5 - 4.7
Latin America	11	**3.9**	3.8	0.5	3.0 - 5.3
Asia	12	**4.5**	3.8	0.5	2.8 - 5.8
Western Europe	18	**7.8**	4.2	0.7	6.3 - 8.9
America	2	**8.5**	4.0	0.6	7.2 -9.6

Notes: 2000 CPI Score: Relates to perceptions of the degree of corruption as seen by business people, risk analysts and the general public and ranges between 10 (highly clean) and 0 (highly corrupt). Survey Used: Refers to the number of surveys that assessed a country's performance; 16 surveys used and at least three surveys were required for a country to try to be included in the CPI. Standard Deviation: Indicates differences in the values of the sources: the greater the standard deviation, the greater the differences of perceptions of a country among the sources. High-Low Range: Provides the highest and lowest values of the sources.

Source: Compiled by the Research Division from Transparency International, Corruption Perceptions Index 2000.

Grassroots and Local Participation

Participation in infrastructure construction, management and maintenance by the local community constitutes a major component of a successful infrastructure policy. Projects that are planned and executed from the central authority, without inputs from local beneficiaries, often have a higher probability of failure and are usually not well maintained. Historically, governments provided most of the public goods, with infrastructure services considered primarily the job of technocrats and experts at the centre.

The users of the services were rarely consulted in planning and managing infrastructure projects. Instead, technocrats took decisions on behalf of the local community regarding the location of projects, their construction and the materials to be used. Unfortunately, a number of the projects planned this way produced services that did not meet the needs or preferences of the end users, the local community, and nor did they utilise appropriate technology. Local participation is thus a key element in the process of development. Not only is it a means of increasing efficiency, but it also strengthens the sense of community ownership of projects and ensures transparency and accountability in project planning and implementation. Compared with centrally planned and executed projects which tend to be uniform and allow for little local variation, local participation allows projects to be customised to the needs of the users. Thus, greater local participation can be seen as a tool for mobilising the collective action of a community and empowering the users or beneficiaries of the project. It ensures that the local community claims ownership at different stages of the project, at the planning, construction and maintenance stages. To be effective, it should incorporate all users of infrastructure services to ensure that the project meets local requirements, utilises local materials and technologies, and is provided and maintained at lower costs. Consumers are less willing to contribute to the operations and maintenance costs of a project in which they lack a sense of ownership.

Participation of the local community can be made effective by encouraging people to contribute partly to the construction, management and maintenance of infrastructure. This participation can be either in cash or in kind. When the stakeholders bear part of the cost of providing infrastructure services, their commitment to the success of the project is greater. In some instances, local people have been encouraged to supply their labour in return for food, cash or materials. However, others have observed that "these material incentives distort perceptions, create dependencies, and give the misleading impression that local people are supportive of externally–driven initiatives" (Pretty, 1995).

An effective way of involving the local community in building and maintaining infrastructure is to devolve some of the decision–making from the central authority to lower levels. In a number of countries, there is a tradition of heavy dependence on centralised command and control in the provision of infrastructure services, with government ministries and agencies developing, operating and maintaining

infrastructure projects. However, planners at the centre have no way of effectively deciding on the optimal quantity and least–cost provision of public goods. Decentralised planning and implementation results in better targeting of social uplift programmes, and thus allows for an efficient allocation of infrastructure services. Local authorities, non–governmental organisations, grassroots groups and other community–based organisations have a better handle on what their localities require and in what quantities.

Support for decentralised planning and local participation requires that the local community be granted greater autonomy and is accountable, and that there should be functioning channels of co–ordination. Greater autonomy can be provided through the establishment of a decentralised system, which ensures that funds are made available to implement local priorities as determined by a democratic process. Transferring central resources allocated to programmes in education, health, welfare and poverty reduction to local bodies to manage can facilitate greater autonomy at the local level. Also, local implementing agencies should be given some degree of financial independence in charging and collecting fees for the services they provide. Greater autonomy should be complemented by the establishment of a system of accountability to enable local governments and community–based groups to monitor the implementation of projects.

Decentralisation and local participation need not minimise the significance of co–ordination and decision–making at the national level. Water sources are not limited by administrative boundaries, which may require a central authority to co–ordinate the activities of different local water associations, for example. There is still a need in a number of countries for a national water plan or a national transport plan.

Local participation and decentralisation may however be constrained by inadequate financial and human resources. In most countries there is a lack of financial and policy support for local activities compared with those planned at the national level. Local governments and community–based groups have limited capacity to mobilise financial resources to meet their growing expenditure obligations and responsibilities that come with devolution of powers. Many local authorities are under–funded, and may not be able to raise sufficient financial resources from the local population. Unlike central government, they have limited opportunities for receiving tax revenue and may have to rely on subsidies and grants. This indicates a need to bridge the gap between national organisations and local communities and to support structures which monitor the effective involvement of civil society in decision–making. Steps should be initiated to strengthen local institutions and to reorient and integrate local development activities planned by local bodies.

Lack of adequate human resource development at the local level also limits the effectiveness of local participation and decentralisation. For the local communities effectively to manage and maintain infrastructure services, it is necessary to communicate technical know–how through the transfer of knowledge. Decentralisation policy needs to encompass all aspects of building local capacity, including the human, scientific, technological, organisational and financial aspects.

Governments and the international community need to facilitate the process of local community participation, by creating the institutional infrastructure to get people involved in social tasks and social mobilisation and affording access to information and opportunities for consultation. Further efforts need to be made to decentralise the planning process at the grassroots level and develop suitable mechanisms for district planning exercises.

Regional Co–operation

Infrastructure development and regional integration and co–operation are positively associated and mutually reinforcing. While infrastructure development can lead to closer integration of national markets, regional co–operation is an effective instrument for improving regional infrastructure. Regional co–operation in Africa usually takes two main forms: project and programme co–operation.

Project co–operation involves initiating and implementing regional infrastructure projects and joint exploitation of energy and water resources. Potential is also particularly high in the areas of telecommunications, rail and road transport and river basin development. Since the required investment is often substantial, regional co–ordination could ensure greater efficiency and developmental impact. For the land–locked countries, the deepening of regional Cupertino for infrastructural development may be particularly crucial. These are areas where economies of scale and considerations of market size could induce significant foreign private investment financing and, possibly, joint management.

Opportunities are also plentiful in Africa's low–cost sources of energy and water. For instance, world–class sources of hydropower have not been exploited. In the energy sector, there is an enormous amount of energy wasted through gas flaring, particularly in West Africa. Africa flares gas at an amount many times greater than the energy it uses. Such energy could be harnessed, to the benefit of producers and consumers, by wielding a strong commitment to regional solutions to the problem of energy shortages in Africa. Adopting regional approaches could significantly reduce the cost and improve the quality of infrastructure services in many parts of Africa. It has been estimated, for instance, that by exchanging electricity with its neighbours, South Africa could save $80 million per annum in operating costs. And with regional construction (as opposed to national), it could save $700 million in expansion costs over the next 20 years (Weiss, 1998).

In recent years, there has been increased evidence of Africa's efforts to undertake such regionally based projects. For instance, member countries of the Southern African Development Community (SADC) have embarked on the implementation of the Southern Africa Power Pool (SAPP). Ratified in 1996, SAPP provides an opportunity to generate and allocate power efficiently among SADC countries. Southern Africa has also embarked on building growth poles of which the most significant is the Maputo Development Corridor that links South Africa's industrial heartland of Gauteng with

the Mozambican port of Maputo. In total, the Corridor has 180 projects at an estimated cost of $7 billion. Already $2 billion has been committed while the remainder is in tender. The Corridor, which has become a model for integrated infrastructure development, is expected to spur the growth of other projects and expand private sector investment opportunities.

The programme approach relates to the protocols and agreements that aim at stimulating the development of regional infrastructure. Traversing mainland Africa, one would have to deal with literally over 50 different variations in the condition and efficiency of infrastructure systems, infrastructure policies, legal frameworks, rules and regulations, standards and documentation requirements. The purpose of the programme approach is to remove such impediments. An example of applying this approach is the Yaounde Treaty of 1961 which assigns to one company (Air Afrique) the traffic rights of 11 West and Central African countries and allows national carriers to service local markets. It is hoped that liberalisation will increase competition, reduce air transport costs, modernise safety equipment and navigation systems, and promote tourism and trade. Another recent example is the Transport Protocol for Southern Africa, a promising effort to harmonise transport policies and procedures in the region.

Harnessing Information Technology

Information technology and Internet services, which hold great potential for the development of a knowledge–based economy, deserve special attention. Information technology provides new ways of exchanging information and transacting business. It altered the nature of the financial and other service sectors, and introduced efficient means of enhancing human, institutional and production capabilities in both public and private domains. The world is rapidly moving towards knowledge–based economic structures and information societies, which comprise networks of individuals, firms and countries linked electronically in an interdependent and interactive relationship. Consequently, the role of the traditional sources of comparative advantage — large labour force and abundant natural resources –– in determining international competitiveness is diminishing. The comparative advantage in the ascendancy is increasingly becoming man–made, based on knowledge and the application of information technology. Thus, information technology will increasingly determine the pace of economic growth and the level of human welfare.

Africa is perhaps the region for which the information revolution offers the greatest hope to leapfrog decades of development. For all of Africa's difficult development challenges, information technology holds large potential as a rapid and relatively inexpensive means to overcome them. In the area of trade, for instance, information technology applications can help to arrest and reverse the significant deterioration in Africa's international market share. Information technology offers effective applications that can enhance the productivity and supply of exportables as well as the demand for exports. Trade and commercial activities record their best performance when producers, exporters and consumers are aware of each other's

products, product quality, and supply and demand capabilities. Information technology offers effective methods to perform these trade promotion functions and improves Africa's international competitiveness.

In the health sector, African countries are at present encountering serious hazards. Information technology can help control and sometimes eradicate some of the health problems plaguing the continent. It has brought about the powerful innovations of "virtual medicine" and "telemedicine". With the application of these innovations, patients located in rural areas could have access to medical experts located thousands of miles away. Information technology can facilitate the development of computer–aided diagnosis of diseases for the rural areas where highly specialised physicians are not available. Isolated medical institutions and practitioners can treat people better by communicating with colleagues and researchers worldwide.

In education the systems of primary and secondary education in many African countries suffer from serious shortcomings including low teacher–student ratios, limited availability of instructional material and poor quality of education. In higher education there are few libraries, most of them lacking access to international journals and generally deprived of educational materials, while research facilities are limited. Most of these educational problems are related to inadequate funding and inefficient use of available resources. Information technology offers a wide range of low–cost solutions. One of the most important applications of information technology in this area is distance education in Africa, which could be extensively used to pursue entirely conventional educational ends. The main advantages of distance education are economy, flexibility and suitability for widely scattered student bodies. In addition, information technology has the potential to connect African educational institutions continent–wide, and link them with international universities, hence facilitating research and the exchange of ideas. Access to data and educational materials would also be simplified.

African countries could make significant strides ahead if information technology applications were introduced in the education system at an early age in primary schools. It is well known that Africa's population has a young age structure where children below the age of 15 years constitute about 45 per cent of the population, compared with 30 per cent for the rest of the world. It is also well known that children take quickly to computer knowledge the way they do to languages. Hence, introducing properly instructed computer education in our primary schools could turn Africa's high dependency ratio, which has always been viewed as a retarding load, into a powerful source of growth and socio–economic development. There have been many theories of leapfrog development; none of them has yet survived the test of time. This could be changed if Africa focuses its efforts on the younger generation, making Africa one of the leading continents in computer literacy in the new millennium.

These are only a few illustrations, and there are almost an infinite number of information technology applications that will provide powerful catalysts to overcome Africa's complex mix of challenges such as accelerating and sustaining economic growth, reducing poverty, improving the environment, and achieving peace, security, democracy and good governance. However, to exploit these opportunities by entering

the information economy in a significant way, African countries would have to overcome, as a matter of priority, numerous obstacles. Among these the inadequate state of telecommunication services and the high cost of computers and software stand out.

The use of the Internet is expanding rapidly in Africa, its growth compared with other regions, however, is constrained by the inadequate state of telecommunications. The key indicators of Internet development are the number of Internet service providers (ISPs) and the number of users. At the start of 2000, there were about 219 ISPs, about 61 of them in South Africa (Table 8). Internet users amounted to 2.9 million, or just 0.4 per cent of Africa's population. About 1.8 million Internet users were in South Africa accounting for 62 per cent of total users in Africa. On average, excluding South Africa, there are about 12 ISPs and 64.8 thousand users per country. These figures, however, are one year old, and today's figures would be larger given the speed at which the Internet service is expanding. The figures also do not cover a large number of small African countries that have introduced Internet services.

Table 8. **Internet Users and Service Providers**

	Internet Users[a]	% of Population	Internet Service[b] Providers
Algeria	20 000	0.06	2
Botswana	12 000	0.76	6
Cameroon	20 000	0.13	7
Côte d'Ivoire	20 000	0.13	5
Egypt	440 000	0.65	30
Ghana	20 000	0.1	5
Kenya	45 000	0.16	8
Mauritius	55 000	4.66	3
Morocco	120 000	0.4	36
Mozambique	15 000	0.08	4
Nigeria	100 000	0.08	6
Senegal	30 000	0.3	10
South Africa	1 820 000	4.19	61
Tanzania	25 000	0.07	10
Tunisia	110 000	1.16	4
Uganda	25 000	0.11	4
Zambia	15 000	0.16	3
Zimbabwe	30 000	0.27	15
Total	2 922 000		219
Average	162 333	0.75	12.17
Average exc. South Africa	64.82	0.55	9.29
Africa: Population	783 446 000		
Internet Users as % of African Population		0.37	

a. Estimates, March-June 2000.
b. April 2001.
Source: Various, Compiled by NUA Internet Surveys; Mike Jensen: mike@sn.apc.org.

Another indicator of Internet development is the prevalence of e–commerce. Despite its proven benefits, the use of e–commerce is yet to take hold on the continent. South Africa is the most active country in Africa in e–commerce followed by Egypt. Even in the most connected and most ready country for e–commerce, South Africa, the percentage of population with access to the Internet is only about 5 per cent. In Nigeria, only one out of every 100 000 people is connected to the Internet. In Senegal, one of the countries with better Internet access in Africa, an entry level computer cost about $1 000 while 30 hours of on–peak Internet usage per month cost about $92.

Clearly, there is a need to improve the connectivity of African countries into the information age and intensify the use of information technology applications. The poor state of telecommunications in our continent is at present the main constraint on the accessibility of many African countries to the global information infrastructure. Ironically, as a result of the quantum jump in technology, the inadequate state of telecommunications can be transformed into a great advantage if properly managed. The fact that the telecommunications sector in Africa is lacking in both coverage and density means also that the continent is not burdened with extensive networks, built on obsolete technology. Countries with extensive networks built on pre–digital technology, with little connectivity between broadcasting, wireless and point–to–point communications, would require an evolutionary process to update their telecommunication technologies. This is precisely because of the heavy inertia associated with large stocks of old technologies. In contrast, African countries can push to the cutting edge by ensuring that new infrastructure is based on the latest technology. The continent could thus leapfrog decades of development in telecommunication and information technology.

It is necessary to adopt new solutions for old problems in order to exploit the opportunities presented by the advances in information technology. For instance, the problem of inadequate and expensive telephone services in rural areas and the severe limitation it imposes on access to the Internet can be surpassed by a combination of geo–stationary and low Earth–orbiting satellites. Indeed, a remote school in an African village having access to the world's libraries using a one–metre dish, is a change of a very large magnitude. Convenient turnkey satellite links which can perform such services are now affordable to many African schools, and prices are expected to drop further in the future.

The high cost of computers and software represents another serious impediment to Africa's accessibility to the world of information technology. The unit price of personal computers is, for instance, higher than the per capita income of many African nations. But it is a fact that the design capacity and capability of such computers and software are not fully utilised by most users — even at top professional levels. Experts in the field suggest that bare–bone computers, perfectly serviceable for Internet connections, word processing and graphics, can be built today for a price which is six times lower than current prices. It will also be possible to produce simple stripped–down software at very low prices. And one way to induce producers to comply with such requirements is "bulk–purchasing". Computer suppliers would be more inclined

to meet required specifications at sharply reduced prices if there were a commitment to purchase large quantities. The message from this is that, by virtue of their potential market size, African countries should not simply accept what is offered to them by the trends of the industry. They should rather play a collective and active role in determining such trends (see Oshikoya and Hussain, 1998).

Rigorous visionary planning is, however, paramount if African countries are to make their mark in information technology trends. For instance, a government that envisions the computerisation of its various sectors, say in five years, would need to draw plans detailing the quantities and the qualities of computers required and their technical specifications including compatibility and expendability. Using such a planning framework, the government can bargain to purchase, wholesale, the quantities of computers and software over the time horizon of the plan with the specification required and at reduced prices. A similar approach within regional economic groupings will be even more effective because of the larger purchases that could be made.

Unfortunately, most African countries do not have any explicit plans or policies on information technology. In most African countries, the acquisition of information technology and software is a result of isolated initiatives without preconceived strategies and policies. Computers and related materials are acquired by different private and public sector organisations with little co–ordination and planning. There is thus a pressing need to devise clear national and regional long–term strategies and policies that cover the acquisition of information technology, its enabling environment and its applications. The strategies should quantify the investment requirements of the countries and identify the required changes in institutional, training, legal and regulatory frameworks to create the environment that would foster the development of the information societies in Africa. Such strategies would also serve as an explicit recognition of the challenges of the information technology and as instruments for attracting and co–ordinating donor assistance.

The Role of the African Development Bank Group

The African Development Bank Group promotes growth and poverty reduction through enhancing Africa's investment and trade. At the end of 2000 the Bank Group had approved over 2 200 loans and grants for a total cumulative amount of over $34 billion, of which nearly two–thirds was financed on non–concessional terms and the rest on concessional terms. The Bank Group finances infrastructure projects with the aim of strengthening the social overhead capital needed for the expansion of directly productive activities; integrating national markets to spread the benefits of economic growth; and diversifying the economies of the region. The benefits that accrue to the economy as a whole justify the priority accorded by the Bank Group to infrastructure projects such as energy, telecommunications, water supply and transport. By the end of 2000, Bank Group cumulative loan and grant approvals in support of projects in the transport sector and public utilities amounted to $14 billion — representing well over one–third of total approvals.

In addition to projects, the Bank Group finances policy–based operations focusing, among others, on supporting a macroeconomic framework that is conducive for the promotion of private sector development, privatisation, divestiture and rationalisation of state–owned enterprises (Table 9).

Table 9. **Bank Group Loan and Grant Approvals by Sector**
1967-2000

Sector	($ billion)	Shares in %
Agriculture	7.06	19.0
Industry	2.53	6.8
Environment	0.01	0.02
Infrastructure	**13.17**	**35.4**
Transport	5.94	16.0
Water Supply & Sanitation	2.71	7.3
Power Supply	3.56	9.6
Communication	0.96	2.6
Finance	4.78	12.9
Social	4.06	10.9
Urban Development	0.00	0.01
Multisector	5.60	15.0
Total	37.21	100.00

Source: ADB Statistics Division.

The Bank Group fully recognises that Africa's development challenges demand a multifaceted and flexible approach in a changing domestic and global policy environment. Thus, in response to the reorientation of many African countries towards private enterprise, the Bank introduced a new private sector development (PSD) strategy in 1996. The objectives of the PSD programme are to enhance the role of the local private sector in the development process, attract foreign direct investments, catalyse resources for sound and sustainable projects, help create a conducive environment for private business and generate domestic and international business confidence in the region.

Within this strategy, the Bank offers a menu similar to that of other multilateral financial institutions. Among many other aspects, it focuses on the creation of enabling macroeconomic and institutional environments for private sector development; and on financing of industrial activities, projects related to tourism, and infrastructure. The menu also includes microfinance and more focused and enhanced assistance to small and medium–scale enterprises.

While the Bank's financing may be modest in relation to the total financing needs of these projects, the Bank's association with these projects provides confidence to other lenders and investors, who might otherwise hesitate to participate because of the perceived risk or lack of familiarity with conditions in the region. A vivid illustration

of such catalytic role is the Infrastructure Fund Project, which was approved by the Bank in 1998. The Infrastructure Fund is aimed at financing large new projects in power, transport and telecommunications as well as gas, natural resource development, water treatment and distribution systems. The Bank's $50 million contribution to this project has been instrumental in attracting other financiers, with the project's total capital amounting to $500 million.

With regard to regional integration, which is important for enhancing trade and investment, the Bank Group aims to increase its efforts to identify and finance multinational and national projects having integration effects. With this in view, the Bank will strengthen technical assistance operations to support pre–investment studies for integration projects.

The Bank is aware that by mobilising resources in international capital market, it is competing with other financial institutions. In order to improve the Bank's competitiveness, three new loan products were introduced in 1997. These include the single currency variable rate loans, the single currency floating rate loans, and the single currency fixed rate loans. These new instruments are aimed at broadening the menu of loan products and giving each borrower the possibility of selecting the currency and interest rate exposure best suited to its borrowing capacity.

We are also well aware that the development effectiveness of Bank loans will be greatly enhanced if sound procurement procedures are put in place. To this end, the Bank has defined new rules of procedure for the procurement of goods and services applicable to all ADB Group–financed operations. It has also organised its services to ensure that these rules are effectively applied not only by its staff but also by the executing agencies of the projects and programmes financed with its loans. Since 1996, an independent unit endowed with the power to control the procurement process has been created, documentation for use by Bank staff and borrowers prepared, and a mechanism for the review of complaints lodged by bidders established. This important mechanism has enabled the Bank to enhance its proficiency in procurement standards the better to meet the requirements of its borrowers and to regain the confidence of the business community.

Beyond the direct contributions to investment activities, the Bank has promoted the establishment of development institutions with the aim of improving the macroeconomic and business environment and stimulating trade and private investments. Among these institutions it is worth mentioning the African Project Development Facility, the African Management Services Company and the African Business Roundtable (ABR). Also, the Bank has established, with the IMF and World Bank, the Joint African Institute (JAI). Based in Abidjan, Côte d'Ivoire, the JAI is aimed at promoting good economic management and attractive business environments through training professionals from member countries in financial, economic and development issues. Furthermore, in its search for new financing mechanisms for trade, which could be instrumental in stimulating the demand for infrastructure services, the Bank spearheaded the establishment of the African Export–Import Bank.

Conclusion

Improving the state of infrastructure remains an important development challenge given its linkages with Africa's overarching objectives of accelerated economic growth and poverty reduction. In recent years, a number of countries in the region have made progress in involving the private sector in infrastructure provision, initially in telecommunications and subsequently expanding into other services including power, water and transport. Many countries, particularly in Southern Africa, have started to invest in regionally based infrastructure projects. African countries have made large strides in providing an enabling environment that assists in attracting more private investment in infrastructure. Improvements in the business environment, together with the drive towards stronger regional Cupertino, indicate the growing opportunities for investment in infrastructure on the continent. African countries and their development partners will need to work more vigorously to improve Africa's image and bring the growing opportunities in this sector to the attention of private investors. On its part, the African Development Bank will continue to work closely with the private sector, development partners and other stakeholders to enhance aid co–ordination and mobilise additional resources to finance projects, including those related to infrastructure development.

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Laws, Institutions and Capital Markets Integration

Keith Jefferis and Kennedy Mbekeani***

Introduction

The increasing prominence of stock markets in developing countries — emerging markets — is one of the most striking features of international financial development over the past two decades. Although the most important emerging markets are in Latin America and Asia, recent years have seen a number of new stock markets in Africa — indeed, it seems that no programme of financial sector reform in Africa is complete unless it includes the establishment of a new stock market or the rehabilitation of an old one. The establishment of stock markets is generally seen as beneficial for a variety of reasons, including their ability to attract inward portfolio investment, boost domestic savings, and improve the pricing and availability of capital for domestic investment. More generally, stock markets are seen as enhancing the operations of the domestic financial system in general and the capital market in particular (Jefferis, 1995; Kenny and Moss, 1998). The establishment and development of stock markets have also been prompted by privatisation programmes, whereby shares in previously state owned enterprises have been offered for sale to domestic and, sometimes, foreign investors.

Despite the growth of African stock markets, however, most of them remain small, illiquid and, in financial terms, inefficient. As a result their broader economic impact has so far been limited. It has been suggested that one way of overcoming these limitations is to encourage regional stock exchanges, or at least much stronger collaboration between national stock exchanges on a regional basis. There have been some initiatives in this direction, the most prominent being the establishment of a West African regional stock exchange in Abidjan in 1998. There have also been discussions regarding regional stock exchanges or integration of national exchanges in East Africa, Central Africa and Southern Africa. However, progress in these initiatives has been slow, often reflecting the differing technical, legal and institutional standards governing markets in different countries as well as broader economic restrictions such as exchange controls.

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This paper reviews the development of stock exchanges in Africa, and moves towards regional capital market integration, with a particular focus on Southern Africa. Besides providing an overview of recent and current developments, it identifies constraints to further regional capital market integration and suggests the types of reforms that would help to move such integration forward. To put the stock exchange in a corporate finance perspective the paper also discusses the capital structure of African companies.

The paper is organised as follows: the next section provides an overview of stock exchanges in Africa. The following one discusses moves towards regional integration amongst African stock exchanges. Then the legal, technical and institutional environment is outlined. We then look at the impact of privatisation on stock exchange development. The final section provides conclusions.

Stock Exchanges in Africa: An Overview

The Markets

At the end of 1998 there were 14 formal stock markets in Africa monitored by the International Finance Corporation (IFC) (see Table 1). These can usefully be divided into four categories:

i) South Africa, which dominates other African stock markets in terms of both size and sophistication.

ii) A group of medium sized markets, many of which have been established for a long time (e.g. Egypt, Nigeria, Zimbabwe).

iii) Small new markets that have shown rapid growth (e.g. Botswana, Mauritius, Ghana).

iv) Small new markets that have yet to take off (e.g. Swaziland, Zambia).

With the exception of South Africa, African stock markets are extremely small by world standards. Together, the 13 markets apart from South Africa accounted for only 0.2 per cent of world stock market capitalisation at the end of 1998, and 2.9 per cent of emerging market capitalisation. In contrast, South Africa — which accounts for 75 per cent of African stock market capitalisation — is quite large by world standards. With a capitalisation of $171 billion at the end of 1998, South Africa was then the third largest emerging market (after Chinese Taipei and China), and the 17th largest equity market in the world. All African markets (including South Africa) tend to lack liquidity, however, and therefore when ranked by turnover rather than market capitalisation their relative position is diminished. Five of the African markets are included in the IFC's Global Emerging Market Index (IFCG) (South Africa, Egypt, Nigeria, Zimbabwe and Morocco) although, apart from South Africa, they have very small weights in the IFCG index.

Although most African stock markets are relatively small, many have grown rapidly in recent years, and there have been very rapid increases in capitalisation and turnover over the past decade. Turnover, for instance, increased at an average annual rate of 29 per cent (measured in US$ terms) between 1989 and 1998, compared with only 12 per cent a year for emerging markets as a whole. At the same time, many of these markets have performed well in terms of returns for investors. Although in many cases they have also been characterised by high levels of volatility, these markets tend to exhibit relatively low correlations with other stock markets internationally.

A number of factors have contributed to the expansion and growth of African stock markets. Many countries have been undergoing economic reform programmes that have involved a reduction in the role of the state in the economy and a strengthening of the role of the private sector. This has been accompanied by a greater role for market forces in price determination and the allocation of both real and financial resources. Financial sector reforms have often included the establishment of new stock markets, or improving the environment in which existing stock markets operate. Furthermore, privatisation programmes in several countries have involved the listing of shares in formerly nationalised firms, which are often very large in relation to the size of national economies, thus providing a supply of new shares and a further boost to stock market development.

This process has been accompanied by increased attention from international investors. Their interest reflects the growing size of African markets, along with the potential for high returns accompanied by the diversification benefits resulting from low correlations with other markets. At the same time many of the barriers to entry that have previously restricted the participation of foreign investors in many African markets are being progressively eased. One 1993 report noted the following problems facing foreign investors:

> Most African countries with a stock market lack a freely convertible currency, and the margin between official and market exchange rates can be as high as 30 per cent. Except for South African firms, one brokerage house in Zimbabwe, and a new research concern in Ghana, none of Africa's investment houses write research reports. Similarly, there appears to be a four– to five–month lag on earnings reporting, and timely news on listed companies is hard to come by. Many companies do not publish their income statements or balance sheets on a regular basis, as the generally inactive stock markets don't seem to require them. Finally, very few banks meet the minimal capitalisation requirements for custodial banks outlined by the SEC, so there is much delay in seeking suitable custody and settlement arrangements (Morgan Stanley, 1993).

Since that time there have been some improvements: many countries have liberalised exchange controls on both current and capital accounts, making entry and exit easier, and direct restrictions on foreign ownership of shares have also been relaxed, although most of the markets considered here do still retain some such controls.

The lack of liquidity remains a serious problem for African markets, however. Even the most liquid of the markets considered here — South Africa, with a turnover ratio of 30 per cent — fares poorly by world standards. The ten most liquid markets in the world in 1998 all had turnover ratios in excess of 100 per cent, and all of the African markets except South Africa had liquidity below the global median (27 per cent). Lack of liquidity can stem from both sides of the market. On the supply side, many shares in listed companies are held by controlling interests — often foreign parent companies — leaving relatively small proportions of shares available for public trading. This can have implications on the demand side, especially in small markets, where local and foreign institutional investors know that "the costs of trading in and out of African equities are high and that positions once sold may not be easily re–established" (Flemings, 1997).

Below we provide more information on individual African stock markets.

South Africa: the Johannesburg Stock Exchange was established in the 19th century in order to raise finance for emerging gold mining ventures. Although very large in terms of capitalisation, liquidity remains low owing to the domination of share ownership by six large conglomerates linked either to mining companies or financial holding companies. This concentration of ownership is partly a result of strict exchange controls on the capital account, which restricted South African firms from exporting capital and left them with little choice but to take over other domestic firms. The JSE has benefited from substantial inflows of foreign portfolio investment since the ending of apartheid and the lifting of sanctions in 1994. There are no restrictions on the ownership of shares by foreigners, although prior to March 1995 transactions had to be carried out using the "financial rand", a dual exchange rate which applied to capital transactions. Since the abolition of the dual exchange rate regime, foreign investors have not been subject to any exchange control regulations, although domestic investors remain restricted in their ability to export capital. The domination of the JSE by the conglomerates has declined since 1994, as a result of inflows of foreign capital and various affirmative action/black empowerment deals.

The JSE moved to a screen–based electronic trading system (JET) in 1996. It operates as part of a relatively sophisticated financial sector characterised by a wide range of financial institutions, markets and information flows which in many respects is more representative of a developed than a developing country. However, there have been some concerns about insider trading given the prevalence of suspicious share price movements prior to major announcements.

Egypt: the stock exchange is comprised of two exchanges, Cairo and Alexandria. Both exchanges are governed by the same board of directors and share the same trading, clearing and settlement systems. The Egyptian Stock Exchange is the second largest in Africa by both capitalisation and turnover, and is also the oldest on the continent, pre–dating the JSE by four years. The Alexandria Stock Exchange was established in 1888 and Cairo in 1903. For much of its existence, however, its role has been stifled by excessive bureaucracy and regulation, and a large proportion of the listed shares

have been illiquid. Nevertheless, recent moves towards deregulation and privatisation have given the market a boost. However, the potential efficiency of the market is constrained by a daily 5 per cent stock price fluctuation limit.

Morocco: Like Egypt, Morocco has a relatively old stock exchange (the Casablanca Stock Exchange) that has been inactive for long periods. It is the third oldest stock exchange in Africa, established in 1929. The exchange is relatively modern as a result of reform in 1993. It has an electronic trading system. Again, deregulation and privatisation have boosted the market in recent years. Although there are no restrictions on foreign ownership, foreign participation in the market is low. This is partly a result of exchange control restrictions on domestic investors who have few domestic or foreign investment alternatives to the stock exchange. Like Egypt, Morocco has been included in the IFC Investible (IFCI) Index since February 1997, and this is likely to boost foreign participation in the market. The low level of foreign participation did, however, help to insulate the market from the spillover effects of global emerging market crises in 1997 and 1998.

Zimbabwe: another long–established market (established in 1896), characterised as “a cozy club with two members” (Cazenove, 1997) prior to the advent of Zimbabwe’s IMF–inspired Economic Structural Adjustment Programme (ESAP) in 1991. The most important boost to the market came with the opening of the exchange to foreign investors in May 1993, along with a major relaxation of exchange controls. Nevertheless, foreign ownership is still restricted, with individual foreign investors limited to 10 per cent of a company’s shares, and foreign investors collectively to 40 per cent. Continued economic and political problems, and inconsistent implementation of structural adjustment and economic reform policies have, however, made the market highly volatile, especially for foreign investors. For instance, the (US dollar–based) IFC total return index recorded a gain of 143 per cent in 1993, 66 per cent in 1996, and falls of more than 50 per cent in 1997 and 1998. The falls were attributed to high interest rates which attracted investors to the higher yielding money market.

Nigeria: the original Nigerian Stock Exchange was established in 1960. The Lagos Stock Exchange (Nigeria) has been primarily a forum for trading government bonds rather than equities throughout most of its existence, but has shown some signs of life since 1996. Equity trading has been constrained by restrictions on foreign ownership and long–standing political and economic problems, and liquidity has been extremely low. However, despite the inconsistent implementation of economic reform programmes, privatisation has been quite widespread and this has helped the stock market. Nevertheless the market is effectively closed to foreign investors and is driven by domestic sentiment. The Lagos Exchange is an affiliate member of the Federation of International Stock Exchanges (FIBV).

Kenya: the Nairobi Stock Exchange was established in 1954. The Kenyan market has had a very similar history to that of Zimbabwe, with an upsurge in activity since 1993 due to economic reform, privatisation, and relaxation of restrictions on foreign

investors and of exchange controls. This resulted in a market capitalisation increasing from $1.7 billion at the end of 1996 to $2.24 billion at end May 1997. At the same time the reform programme has been inconsistent and political problems remain, leading to market volatility, especially in dollar terms.

Mauritius: the Stock Exchange of Mauritius (SEM) has developed rapidly in a short period of time, from its establishment with five companies in 1989 to 40 listed companies by 1998. The listed companies cover a wide range of economic activities, including manufacturing, tourism, sugar and finance. Another 80 companies are traded on the Over–The–Counter (OTC) market. Although the market remains small and not all that liquid, it is helped by the absence of restrictions on foreign ownership, and foreign investors play an active role in the market. Major reforms have taken place. An electronic clearing and settlement system was established in 1997. In 1998 a Central Depository System was implemented in which all listed companies are registered; this system allows delivery versus payment on a T+5 day rotating basis. The exchange has been promoted from the status of corresponding Exchange to that of affiliate securities markets within the FIBV.

Botswana: the Botswana stock market was established in 1989 with five listed companies and became the Botswana Stock Exchange in 1995. The Exchange had grown to 14 listed companies by 1998. The listed companies are concentrated in finance and services, with little representation from manufacturing and none from the mining sector on which the economy depends. Foreign portfolio investors are limited to 10 per cent individually and 55 per cent collectively of company stocks, and play an important role in the market. Despite the small number of stocks and only one broker (two since early 1998), the market is more liquid than some larger African markets.

Côte d'Ivoire: The BRVM (Bourse Regionale des Valeurs Mobilières) was established in September 1998 as the world's first regional stock exchange. It links eight French–speaking countries in West Africa — Benin, Burkina Faso, Côte d'Ivoire, Guinea Bissau, Mali, Niger, Senegal and Togo — which are all members of the West African Economic and Monetary Union (UMOEA). The exchange was based on the existing Abidjan Stock Exchange. Initially all of the 35 quoted companies were from Côte d'Ivoire, but these were supplemented by the listing of a Senegalese company late in 1998. The establishment of the exchange was led by the UMOEA central bank, the BCEAO, and member governments. The market is however highly illiquid, a situation that is compounded by regulations restricting daily price movements to 7.5 per cent.

Tunisia: the Tunis Stock Exchange dates back to 1969, but has only become active since the mid–1990s under the impact of privatisation and regulatory reforms. These reforms have removed limits on daily price changes and opened up the market to foreign investors. In 1998 a new share index weighted by market capitalisation was introduced. The existing Tunis index of 33 stocks is characterised by a lack of liquidity.

Zambia: the Lusaka Stock Exchange was established in 1994 with assistance from the International Finance Corporation (IFC). The market is small in terms of turnover and capitalisation. Most listings have resulted from Zambia's privatisation process, which offers potential for further listings and market development as privatisation proceeds. There are no restrictions on foreign investment, but uncertainties over the privatisation process and broader economic developments have deterred significant foreign investment.

Namibia: the Namibian Stock Exchange was established in 1992, and began with dual listings of companies quoted on the Johannesburg Stock Exchange that also did business in Namibia. Since then, a number of local companies have also been listed. The exchange is relatively advanced in terms of trading technology, and since 1998 it has been using the JSE's electronic trading system. Nevertheless the market remains small in terms of trading and turnover, with low liquidity.

Ghana: the Ghana Stock Exchange opened in 1990. It is dominated by Ashanti Goldfields, which is also listed in London, Toronto, New York and Zimbabwe, and which accounts for two–thirds of total market capitalisation. Besides Ashanti, firms in the manufacturing and beverage sectors are important on the exchange.

Uganda: the Uganda Securities Exchange was established in 1997 and opened to trading in January 1998. It is run under the jurisdiction of the Capital Markets Authority which reports to the Central Bank of Uganda. Four companies from the privatisation programme are expected to list (Uganda Commercial Bank, Uganda Grain Milling Ltd, National Insurance Company and Uganda Consolidated Properties).

Tanzania: the Dar es Salaam Stock Exchange was opened in 1998 with one listed company (Tanzania Oxygen Ltd). Foreign investors are currently barred from trading and this hampered the development of the exchange.

Mozambique: the stock exchange started operating in October 1999 with the support of the Lisbon Stock Exchange and the World Bank. The development of the exchange may be hampered by lack of necessary physical infrastructure and legislation for trading. Company listings are expected to be encouraged by the government's intended disposal of its remaining shares in privatised companies.

Other small markets include the Swaziland Stock Market, established in 1990. The Malawi Stock Exchange was opened in 1996 with a modest listing; more companies are expected to list from the government's privatisation programme. In Sudan, the Khartoum Stock Exchange started trading in 1995; the exchange operates on the basis of the directives of Islamic Sharia Law.

It is important to note that besides trading corporate equities, most African stock exchanges also trade government debt (bonds), which are often important contributors to overall turnover. However, corporate bonds do not tend to be widely issued or traded (outside South Africa), as this instrument has not been widely used for the raising of corporate finance.

Market Efficiency

There have been few studies of the efficiency of African stock markets. However, the few that have been carried out conclude, not surprisingly, that most markets are inefficient (in a financial sense, meaning that stock prices do not reflect all available information, and that prices are not therefore being appropriately priced at their equilibrium values).

A variety of empirical tests can be used to assess market efficiency. Jefferis and Okeahalam (1999a) apply unit root tests to market indices to assess the efficiency of the stock markets in South Africa, Botswana and Zimbabwe over the period 1989–96, and find that the South African and Zimbabwean markets were efficient during this period, although Botswana was not, at least during the early part of the period. However the unit root test of market efficiency is not a powerful one, and subsequent analysis using different tests provides contrasting results. Jefferis and Okeahalam (1999*b*) use an event study of the same three markets to test the response of individual stock prices to information announcements, by evaluating the speed and efficiency with which information is incorporated into market prices. This finds that the Botswana and Zimbabwe markets are inefficient, while the Johannesburg Stock Exchange is weak form efficient. This corresponds to the findings of Smith, Jefferis and Ryoo (1999), who test whether eight African stock markets follow a random walk using multiple variance ratio tests. Of the eight markets (South Africa, Egypt, Kenya, Morocco, Nigeria, Zimbabwe, Botswana and Mauritius), only South Africa is found to follow a random walk and therefore to be weak form efficient.

The lack of market efficiency can be attributed to various factors, of which lack of liquidity and lack of institutional maturity would appear to be the most important. While the JSE is not particularly liquid by global standards, it is more liquid than most other African markets, and in addition benefits from the trading of its shares on major international markets where they are cross–listed. It is also the only African market that approximates a developed market in size and in availability of information and analysis.

Relationship to Global Markets

It is also apparent that linkages between African markets and developed country markets are weak. The strength of short term relationships between markets can be assessed by correlations of market returns. Except for South Africa, correlations between African markets and the US and UK markets are very low (see Table 1). Longer term relationships can be assessed through cointegration analysis. Using this approach, Jefferis and Okeahalam (1999*a*) find very little evidence of long term relationships between three Southern African markets (South Africa, Botswana and Zimbabwe) and either the US and UK markets or emerging markets in Latin America and Asia. Taking a different approach, Harvey (1999) finds that the Asian financial crisis of 1997 and the Russian/ Latin American crisis of 1998 had little impact on African stock markets, despite the widespread contagion impact of these crises on stock markets generally.

Table 1. **African Stock Markets, 1998**
(ranked by turnover)

	Capitalisation ($ million)	Turnover ($ million)	Turnover ratio (percentage)	No. of stocks[a]	Price-earnings ratio	Correlation		Average annual change in index[b] (percentage)	
						S&P500	FT All Share		
Malawi	-	-	-	-	-	-	-	-	-
Swaziland*	85	0.2	0.2	5	-	-	-	-20	-32
Zambia	293	2	0.8	7	-	-	-	-	-
Namibia*	429	13	2.6	15	-	-	-	7	-9
Côte d'Ivoire*	1 818	39	2.6	35	8.5	-	-	23	11
Ghana*	1 384	60	4.8	21	10.5	-	-	49	12
Botswana	724	70	10.6	14	10.9	0.01	0.04	19	7
Kenya	2 024	79	4.0	58	8.1	0.01	0.02	16	3
Mauritius	1 849	102	5.9	40	11.6	-0.04	0.03	13	6
Nigeria	2 887	161	5.2	182	10.1	0.01	0.05	35	1
Zimbabwe	1 310	166	9.2	67	5.8	0.07	0.06	14	-18
Tunisia	2 268	189	8.3	38	10.5	-	-	18	14
Morocco	15 676	1 385	10.1	53	21.2	0.01	0.02	-	-
Egypt	24 381	5 028	22.3	861	8.7	0.01	0.00	26	26
South Africa	170 752	58 444	30.4	668	10.1	0.24	0.26	9	-2
TOTAL	225 880	65 737	29.1	2 064	-	-	-	-	-
Excl. South Africa	55 128	7 293	13.2	1 396	-	-	-	-	-
MSCI World Index	-	-	-	-	29.0	-	-	-	-
IFCG Composite	-	-	-	-	-	-	-	-	1

a) Refers to domestic primary listings only (i.e. excludes those with primary listings on other markets).
b) 1990-1998, except where marked with * change in index refers to different time period.
Source: IFC (1999); Flemings Research (1997); Smith *et al.* (1999).

The relatively low level of integration of African stock markets — excluding South Africa — into the global financial system is due to a wide range of factors. As noted above, markets are relatively illiquid, and hence prices often do not respond to company or broader economic and financial developments in the way that they would in larger, more liquid markets, simply because there is insufficient trade. Most markets are too small and/or illiquid to attract significant inflows of foreign investment, which again acts as an isolating factor with respect to international markets. There is sometimes concern about company listing standards as well as information disclosure requirements and corporate governance. As a result, foreign investors can be wary of African markets and/or require a risk premium, in the form of higher expected returns, if they are to invest — a requirement that is even more stringent in countries that do not have a stable macroeconomic environment. Finally, many African countries still maintain restrictions on foreign ownership of listed shares and/or exchange controls that restrict capital inflows and outflows. Despite these drawbacks, there is some foreign interest. Low correlations with developed markets mean that African markets can offer substantial portfolio diversification benefits to international investors. Furthermore, African markets have at times offered high returns, although often associated with high levels of return volatility, especially when measured in US dollar terms.

Capital Structure of African Companies

The financial sectors of African economies tend to be quite underdeveloped in relation to both developed countries and many developing countries, with regard to the range of financial instruments, institutions and markets available. Only South Africa really stands comparison with the more advanced developing countries. Financial systems tend to be "bank–dominated", with commercial banks (whether state or privately owned) by far the most important providers of finance. Two results stem from this structural characteristic. First, the availability of risk–friendly financial instruments is highly constrained, with limited availability of equity finance, venture capital or derivatives. Second, companies in most African countries face a limited range of choices with regard to their corporate financial structures.

Large African firms in particular are often heavily geared, with high debt–asset ratios. This reflects both incentives and availability of finance. Bankruptcy costs (a deterrent to debt financing) are often relatively low, because courts are not well developed thus making it difficult for creditors to recover bad debts; thus firms face an incentive to use debt finance. A similar incentive results from the tax shield. Typically debt interest is tax–deductible, whereas dividend payments to equity owners are not. Hence, in countries with high corporate profit tax rates (again, typical of African economies), there is a tax incentive to structure finance as debt rather than equity.

The opposite extreme applies to small and medium–sized firms, which often have very low debt–to–asset ratios. Banks are typically reluctant to offer loans to small or new firms, perceiving them as high risk, a situation which largely reflects a lack of information. The severity of such information problems leads to more credit

rationing for the smaller companies. Smaller firms are unable to obtain the necessary funding or are excessively paralysed by the problem of incomplete information in the sense that not only are they unable to get cheap funding, but they often find it difficult to get any funds at all. Small and medium–sized firms are often heavily reliant on internally generated funds (retained earnings) for equity finance, which can constrain their ability to expand rapidly even when profit opportunities are available. Another result is that such firms may also be forced to deal with informal financial structures.

To the extent that lending to the corporate sector is perceived as high risk by the banks, the situation may be compounded by alternative investment opportunities for banks in the form of government securities. Especially in high inflation environments, banks may prefer to hold high return, low risk government stock such as treasury bills rather than venture into corporate lending.

It is apparent that the establishment of stock exchanges could significantly change the capital structure of African companies, if they can be established in such a way that makes them widely accessible. Capital–constrained small and medium–sized companies could benefit from the new source of finance that becomes available, while larger companies could find it attractive to reduce their gearing.

Moves Towards Regional Integration Amongst Stock Exchanges

As African stock markets have become larger and more widespread over the past decade, there have also been preliminary moves towards regional integration amongst these exchanges. This reflects both the needs of the exchanges themselves and the broader process of regional integration. The latter, however, has generally started with trade liberalisation and integration, whereas regional integration amongst stock markets, being part of capital market integration, has generally progressed more slowly.

Constraints to Regional Integration of Stock Exchanges

As noted above, most African stock exchanges (that is, apart from South Africa) are small and illiquid. This acts as a major constraint to attracting inflows of foreign capital (portfolio investment), which is one of the major objectives of establishing a stock exchange.

These small and illiquid exchanges face a range of problems in attracting inward investment. First, the range of shares on offer is limited, and the size of potential deals is often small. These characteristics may reflect a small number of listed companies, the small size (capitalisation) of many listed companies, or the restricted availability (free float) of shares even when the number or size of companies listed is larger. Hence many markets cannot offer large enough parcels of shares or a diversified enough range of shares to be of interest to international investors, who generally have quite large minimum holding and dealing sizes.

The need for large sizes of deals reflects the fact that there are economies of scale in share dealing: various institutional factors, such as dealing with laws and regulations, dealing with local agents (stockbrokers), carrying out research, setting up custody arrangements, all have a cost and unit costs are lower if they can be spread over a larger number or value of trades. More generally, the existence of different national legal, taxation and institutional regimes makes dealing with Africa difficult and costly for international investors, hence reducing potential returns and thus constraining capital flows.

A second problem of small exchanges is that making cross–comparisons within sectors and across companies is difficult if there are few stocks and if not all economic sectors are represented; hence the relative performance of different companies is difficult to establish.

A third problem is that of pricing: the illiquidity of exchanges means that the pricing process is not well developed. This leads to mispricing and a lack of efficiency, which in turn means that capital is not properly priced, so that the "disciplinary" role of stock markets (rewarding good performers and punishing bad ones) may not work fully. Furthermore risk is not properly priced, and stock markets may not therefore fulfil their potential as a means of allocating capital.

Another problem is poor telecommunications and computer technologies within many African countries, with a great diversity in the levels of automation and of the systems applied. The poor telecommunications and computer technologies are a constraint to any effort to facilitate cross–border transfer of funds, as well as cross–border trading and settlement that are key to facilitating regional integration of stock exchanges.

Finally, exchange controls in many countries prevent the cross–border movement of capital that is essential for regional stock market integration. The problems created by exchange controls can be illustrated by way of example. Perhaps the simplest form of stock market integration is the cross–listing of shares on national stock exchanges in different countries. With capital mobility and a liquid trading environment, the price of the share should be the same (measured in terms of a common currency) in each country. However, Ashanti Goldfields shares listed on the Zimbabwe Stock Exchange trade at a discount to the same shares listed on other stock exchanges, such as Ghana, London and New York. This is because Zimbabwe's exchange controls restrict the movement of locally–listed shares across share registers in different markets and do not allow the free flow of capital from the sale or purchase of Ashanti shares between Zimbabwe residents and non–residents. Hence the Zimbabwe listing of Ashanti shares is segmented from the rest of the world and its price in Harare does not reflect the share's international price movements. Thus, owing to exchange controls, there is no integrated market in these shares.

A deeper form of regional stock market integration would involve investors in different countries being able to buy and sell shares freely on a regional (as opposed to national) stock market. For instance, if a hypothetical Southern African Development Community (SADC) stock market was located in Gaborone, Botswana, an investor in Mozambique should be able to buy a share in a Zimbabwean company listed on the

SADC exchange, using a broker located in Mozambique, Zimbabwe, Botswana or indeed any other SADC country. For this to happen, there has to be unrestricted flow of capital between the participating countries, at least for this type of transaction. Only two regional groupings — the CFA zone in Francophone Central and West Africa, and the Common (Rand) Monetary Area in Southern Africa, at present meet the requirement of full capital mobility (although some individual countries, such as Botswana, Zambia and Mauritius, have individually abolished exchange controls and thus have no restrictions on capital mobility).

Advantages of Regional Integration

African stock exchanges share various characteristics which underlie the importance of the proposal for regional integration. The exchanges are small in size (in terms of market capitalisation measured as a percentage of GDP) and generally illiquid. The low level of deepening reflects the lack of small and medium–sized companies that are suitable for listing and trading.

Regional integration of stock exchanges is essentially seen as a means of overcoming the size and liquidity problems of existing exchanges much more quickly than if these problems were to be overcome by the organic growth of national exchanges. It is also a means of reducing the costs of investing in Africa for international investors. Improving liquidity will help to improve the efficiency of the pricing process, and increasing the range of stocks will help portfolio diversification, and thus improve the risk–return trade–off for national, regional and international investors alike. There is also evidence that increased liquidity can help to enhance the beneficial impact of stock markets on the broader financial and economic development process (Levine and Zervos, 1996).

It is also part of the broader process of capital market liberalisation, allowing savings resources to be allocated more efficiently to competing investment opportunities, with savings less restricted to national capital markets and hence an increase in cross–border capital flows. Cross–border capital flows in an integrated regional market will widen trading (by increasing the number of companies) and thereby reduce risk. In all African stock exchanges there is a concentration of trading in a few companies, reflecting the vulnerability of markets.

Regional integration can also contribute towards a general upgrading of standards, if the process is associated with a convergence on high common standards within a region. These can include standards on accounting rules; corporate reporting and disclosure; listing requirements; protection of minorities; insider trading rules; custody and depository arrangements; takeovers and mergers, etc., and are discussed in more detail below. It is increasingly recognised that stock exchanges can play an important role in raising general standards of corporate reporting, accounting and regulation, especially through the listing requirements that they impose (Levine, 1998). By adopting common regional standards, regionally integrating stock exchanges can spur higher standards on both a regional and national basis, and thus contribute to higher economic growth.

An example of potential gains from regional collaboration in market microstructure issues relates to record keeping and settlement systems. Many financial markets around the world are moving to paperless or "dematerialised" systems with computer–based record systems of share ownership (and of other financial instruments, such as government bonds). Because such systems do not rely on the physical delivery of scrip prior to transfer of ownership, the settlement of trades can be significantly speeded up. Transactions costs can also be reduced owing to the efficiency of computer–based record keeping relative to paper–based systems. However, such systems require a central depository, which can be an expensive undertaking, especially given the level of financial guarantees or sureties that would be required to assure foreign investors in particular of the soundness of such a system. While it is technically possible for small countries to undertake such an initiative, it may be financially unrealistic. Given the economies of scale involved, it is likely to be much more feasible on a regional basis, for instance with smaller markets collaborating to set up a joint system, or making use of a system operated by a larger market, such as South Africa.

Movements towards Regional Integration

Although regional integration amongst African stock exchanges is still at an early stage, there has nevertheless been some progress. The first stage of integration is cross–listing of stocks, whereby a single stock is listed on more than one exchange. If this is associated with open registers (whereby stocks can be moved from one country's register to another without restriction), this will lead to a common pricing of the stock on the different exchanges, with the price determined by trading on both exchanges[1] Cross–listings are assisted by the adoption of common listing standards across exchanges. This course has been pursued by SADC stock exchanges, which are in the process of adopting common rules and requirements for listings as the first step towards regional integration. This initiative is being promoted by the SADC Stock Exchange Committee (SADSEC), whose members are Botswana, Lesotho, Mauritius, Namibia, South Africa, Zambia and Zimbabwe.

The first fully–fledged regional stock exchange (as opposed to co–operation or cross–listings between separate national exchanges) is the Bourse Régionale des Valeurs Mobilières (BRVM), established in Abidjan in 1998 on the basis of the old Côte d'Ivoire exchange. The establishment of this regional exchange is clearly facilitated by the fact that the member countries share a common currency (the CFA franc) and thus have no restrictions on capital movements between themselves. Discussions have also taken place on regional integration of stock exchanges in East Africa (Kenya, Uganda and Tanzania). With more general moves towards reviving regional co–operation in East Africa, some observers believed that the Nairobi Stock Exchange, which dates back to 1954 and which has relaxed rules on foreign ownership of shares in recent years, should have been developed as the market for all listed companies in the region. Instead, Tanzania and Uganda decided to open their own stock exchanges, although the number of listings has so far been very low, owing partly to slow progress with privatisation programmes and restrictions on foreign ownership. There are currently discussions on facilitating cross–listings.

In Central Africa, the UDEAC members Cameroon, CAR, Chad, Congo (Brazzaville), Equatorial Guinea and Gabon have had discussions on a regional exchange. In a parallel with the West African situation, these countries already share a currency (the CFA franc) and a central bank, but unlike West Africa do not have an existing exchange that can form the basis for a regional market.

The Legal, Technical and Institutional Environment

It has been noted above that stock markets play an important role in open economies by facilitating intermediation between savers and investors. Well–functioning financial markets, along with well–designed institutions and regulatory systems, foster economic development through private initiative. The linkage between finance and economic development is of great interest to Africa, since it suggests an indirect linkage between financial sector development and poverty alleviation, along with employment creation. There is empirical evidence strongly suggesting that well–functioning capital markets promote long–run economic growth (see Bekaert and Harvey (1996) and Levine and Zervos (1996). It is therefore important that stock markets be well organised and regulated.

The depth of the capital market infrastructure is judged on the basis of the efficiency with which the various functions are carried out. For instance, the mere creation of stock exchanges is inconsequential if the environment is hostile against opportunities for risk–sharing and liquidity provision and transformation. Economic theory indicates that the ability of stock markets to attract private capital depends on the institutional nature of the markets, which is a function of the regulatory structure under which the market functions, as well as the market's microstructure[2]. The importance of microstructure arises from the role it plays in each of four fundamental market attributes: liquidity, efficiency, trading costs and volatility. Even though the attributes are closely related, each of the attributes is different and can be influenced by microstructure, the regulatory regime under which the market operates, as well as by the economic fundamentals which drive security prices.

Economic theory suggests that microstructure is one determinant of market liquidity. Liquidity, the ability to buy or sell both quickly and without substantially moving prices, is the key to market success. Both aspects of liquidity are important to market participants. The speed with which transactions are consummated depends on the number of market traders and microstructure. However, market structure imposes constraints on trades regardless of the number of potential traders. For example, in a number of African markets, the stock exchanges are open only during certain hours and days of the week (see Table 2). Even when open, some markets allow trades to occur only periodically, rather than continuously throughout the day. By limiting the number of trading hours and the manner in which traders meet, market microstructure has a direct impact on liquidity. Empirical evidence has shown that liquid markets attract more market participants and have an impact on stock prices and the cost of raising capital in the market.

Trading costs include both the fixed costs associated with trade, such as taxes and commissions, as well as the major cost that the market imposes. By adopting a microstructure that allows for competition among traders, or by assigning an individual market maker whose duty it is to ensure that trading is possible, microstructure can have a direct effect on trading costs and liquidity.

Microstructure has an important role to play in encouraging market efficiency, both through the information services that are provided to participants, as well as through the nature of the trading system itself. Markets are said to be efficient if they quickly and correctly incorporate information into prices. The availability of information reduces uncertainty and increases market interest, which leads back to liquidity. An important innovation in microstructure, automated trading systems, has taken place in recent years in a number of stock markets in Southern Africa. The innovation is a reflection of the importance of information and the trading system on market efficiency.

The discussion of stock market development in Africa is not taking place in a vacuum. Unprecedented well–meaning financial and regulatory reforms have accompanied recent enthusiasm for stock market development, and many countries have made attempts to put in place tax reforms that suspend, and even abolish, tax on capital gains for publicly listed shares, reduce dividend withholding tax rates and mitigate the distortionary effects of multiple layers of taxation. There are also some serious attempts to reduce barriers to international capital flows in the form of elimination of rules that discriminate against foreign investors and adoption of legal reforms governing repatriation of return on capital.

However, there are still poor brokerage services and slow settlement and operational procedures (Table 2). Transaction costs in African markets are the highest in the world. Investors get charged for brokerage fees, stamp duty and, in some cases, special charges by regulatory bodies. There continue to be distortionary taxes in some markets, such as taxation of dividend in multiple layers, taxation of capital gains, withholding taxes, and other distortionary taxes against foreign capital (Table 2). More generally, genuine stock market development should be accompanied by credible regulatory regimes that promote, rather than inhibit, private initiative, whereby investors and savers build confidence in the financial systems.

From the review of African stock exchanges above, it is apparent that, apart from the relatively long–established exchanges in North Africa, almost all of the remaining stock markets are in Anglophone Africa. Only one (the Abidjan exchange in Côte d'Ivoire) is in Francophone Africa. This raises the question of why there have been these two divergent paths of stock exchange development in different parts of Africa. Two possible explanations can be suggested. First, there are major differences between the British and French traditions in terms of corporate finance; the British tradition is much more equity–based, with stock markets playing a prominent role in the United Kingdom and the United States, as well as other countries sharing a similar background such as Canada, Australia, and South Africa. In South Africa, for instance,

Table 2. **Trading Environment in Selected Southern African Stock Exchanges**

	Botswana Stock Exchange	Lusaka Stock Exchange	Malawi Stock Exchange	Namibian Stock Exchange
Legal Establishment & Governance of the Stock Exchange	Legally established in 1995, Governed by the Botswana Stock Exchange Act. Informal Botswana share market since 1989	Established in February 1994 and is governed by the 1993 Securities Act	Started in March 1995 and it operates in terms of the Capital Markets Development Act of 1990 and the Capital Market Development regulation of 1992	Started in 1985 and is governed by the 1985 Stock Exchanges Control Act and is licensed by Ministry of Finance
Openness of SE Membership (Domestic/Foreign Brokers)	Corporate or individual	Corporate	Corporate or individual	
Brokers	2	3	1	8
Listed Companies	23	15	7	44
Trading Systems	Open outcry system. Clearing occurs transaction by transaction	Single price auction	Single price auction. Clearing occurs transaction by transaction	Electronic trading system, i.e. JET system adopted from the JSE
Frequency of Trading	Monday to Thursday 09:00 -16:00 Friday 09:00 - 12:00	Monday to Friday: 10:00 - 12:00	Monday to Friday 09:00 - 12:00	Monday to Friday 09:30 - 16:00 with a five-minute variation to the start and close times
Openness/Restrictions on Foreign Ownership/Trading in Shares	No restrictions on foreign investment	No restrictions on foreign investment and foreign investors invest on similar terms as Zambians	Foreign investment is allowed but is limited to 5% of issued share capital for one foreign investor and 49% of issued share capital in total. No regulations regarding capital repatriation provided the investor is registered with the Reserve Bank	No restrictions on foreign investment. Foreign investors must apply through an authorised dealer to ensure free remittance of dividends and proceeds of sales
Exchange Controls on Capital Movements and Tax	15% withholding tax on dividend No capital gains			10% withholding tax on dividends. No marketable securities tax or capital gains tax
Paper/ Paperless Systems; Central Depositories	None	Electronic depository facilities	No depository	Paperless real time clearing
Settlement Rules	T + 5	Electronic clearing and settlement process Settlement 3 days after trade (T+3)	Settlement occurs on a T+7 basis	Planning to introduce a settlement system known as the Southern African Instruments Clearing System which is being introduced by the JSE

Table 2 (continued). **Trading Environment in Selected Southern African Stock Exchanges**

	Stock Exchange of Mauritius	Swaziland Stock Exchange	Zimbabwe Stock Exchange
Legal Establishment & Governance of SE	Established in 1988 under the 1988 Stock Exchange Act. And it is a private limited company	Established in July 1990	Established in1986 and operates according to the Stock Exchange Act (Chapter 198)
Openness of SE Membership (Domestic/Foreign Brokers	Open to foreign investors since 1994. All applications are sent to the SEM via a stockbroking company and should meet the listing requirements		Has been open to foreign investment since 1993.Companies wishing to list on the ZSE must conform with the listing rules and regulations of the Listing Committee
Numbers of Brokers	3	1	14
Number of Listed Companies	40	6	75
Types of Trading Systems	Open outcry, order driven and single-price auction system	Matched bargain type of trading	Manual
Frequency of Trading & Price Adjustment		Monday to Friday: 10:00-12:00	Monday to Friday: 09:00-12:00
Openness/Restrictions on Foreign Ownership/Trading in Shares	Open to foreign investors, no exchange controls and foreign investors do not need approval to trade shares but they cannot have individual holding of more than 15% in a sugar company. No control on currency repatriation	No regulations regarding the foreign ownership of brokers	Companies may not be more than 40% foreign owned and no single overseas shareholder can possess more than 10%. Income and sale proceeds by those bringing funds registered through a commercial bank can be repatriated free of charge. Need for permission to sell imported foreign bought scrip. Locally acquired dual listed scrip cannot be sold outside Zimbabwe
Exchange Controls on Capital Movements and Tax	No tax on dividends or capital gains	Exchange control approval is required for foreigners wishing to invest on the stock market. 15% nonresident tax is levied on dividends and there are no capital tax gains	There is a 15% tax levied on dividends and 10% on capital gains on individuals
Paper/ Paperless Systems; Central Depositories	Central depository system which allows for delivery versus payment on a T+5 day rotating basis		A central scrip depository and a securities and exchange law are being prepared
Settlement Rules	Electronic clearing and settlement system. Settlement can be made in foreign currency		

stock markets in London and Johannesburg were at the forefront of raising capital to finance the early exploration and development of gold and diamond mines. In contrast, French corporate structure tends to make more use of bank finance, in common with the mainstream European tradition, where equity markets play a relatively insignificant role.

A second, related explanation is derived from the different legal and institutional structures of the Anglophone and Francophone economies. Research elsewhere in the world (La Porta *et al.*, 1996 and 1997) concludes that countries with a British (common) law background tend to have relatively good investor protection, that is, legal rules covering the protection of corporate shareholders and creditors, with relatively good enforcement of those rules. By contrast, countries with a background of French civil law tend to have the worst legal protection of investors. These latter countries also have the least developed capital markets. The lack of protection for small and minority shareholders would obviously discourage investors from investing in companies with which they have no direct links, and as a result, "small diversified shareholders are unlikely to be important in countries that fail to protect their rights" (La Porta *et al.*, 1996). Given that the fundamental purpose of stock markets is to enable firms to tap sources of finance provided by minority (i.e. non–controlling) shareholders, the lack of stock market development in the countries of Francophone Africa is consistent with the La Porta hypothesis that legal and institutional structures are of great importance in influencing the manner in which companies can access external finance.

Common legal backgrounds amongst countries in the Anglophone and Francophone groups also suggest that efforts towards regional stock market integration are unlikely to be successful across these two groups (as achieving common legal standards would be very difficult) but could be much more successful given the common backgrounds of countries within each group. It also suggests that the Francophone countries could draw lessons from the British tradition if reforms are being considered that would encourage stock market development.

Impact of Privatisation on Stock Exchange Development

There is a symbolic link between privatisation and capital market development. A large privatisation programme often has a dramatic effect on capital market development, adding greatly to the stock and variety of corporate assets available to the public. Privatisation has been used to accelerate the development of capital markets and to spread the ownership of companies in the stock market economies in Southern Africa.

Privatisation of state enterprises provides an excellent, and maybe the only, means significantly to expand the securities market rapidly in most African countries. Already in a number of African countries privatisation programmes have resulted in expanded share ownership and trading in the securities market. In countries with new stock exchanges (Malawi, Zambia and Mozambique) privatisation of state–owned companies

has enhanced the depth of the existing markets — indeed, the flow of privatised companies has been integral to the very existence of these markets. Other markets (such as Uganda and Tanzania) have the expectation of similar gains.

Zambia's privatisation process led to an increase in the number of companies that listed in the stock exchange since its establishment. Zambia Sugar Plc's public offer in late 1996 had shares that were a combination of those warehoused by the Zambian Privatisation Trust Fund and those owned by the Commonwealth Development Corporation being offered to international investors. The Zambian Breweries Plc also successfully raised over $8.5 million to refinance a loan that had been secured to finance the acquisition of Northern Breweries Plc. Most of these listings have been triggered by Zambia's privatisation process. Companies designated for future floatation of their government owned shares and listing on the Lusaka Stock Exchange include: ZAFFICO (Timber Planting and Processing); ZESCO (Power Generation); ZAMTEL (Telecommunications); ZAMEFA (Manufacturing); ZNCB (Banking); ZSIC (Insurance); BP (Petroleum); AGIP (Petroleum); National Milling (Agricultural Processing); Mpongwe Development (Agriculture); Lever Brothers (Consumer Products); ZAAMOX (Industrial Gases).

Though the stock exchange of Mozambique has been established recently and faces potential listing problems, the state intends to have some of its holdings in privatised companies distributed to the public in order to broaden ownership and raise capital to find the budget deficit. Besides the announcement by Cervejas de Mozambique (CDM), which is Mozambique's leading brewery to list, there are other companies in which the government holds shares which are expected to follow. The government retains up to 20 per cent of the share capital in about 900 companies that have been privatised. Other companies that have been privatised include the country's largest cement, plastics, milling, soap, cooking oil and clothing manufacture companies.

Many examples show clearly that privatisation can contribute directly to the development of capital markets, and that these markets can facilitate the implementation of the privatisation process and thereby increase economic growth and social well–being. For example, privatising the social security system and allowing private pension funds to invest in shares, including those of privatised state–owned enterprises, were major factors in linking the diffusion of ownership and expansion of the capital markets in Chile, and increasingly elsewhere in Latin America. In Argentina privatisation allowed the capital market to gain more dynamics owing to the fact that companies such as Telecom and Telefonica were established in the stock exchange. The listing of privatised companies also makes their shares more liquid and hence more valuable, thus encouraging individual investors to participate in privatisation offerings. Although the examples mentioned are largely from non–African countries, the mutually beneficial and supportive links between privatisation and capital market development are clearly as relevant in Africa as they are elsewhere.

Conclusion

A number of conclusions can be drawn from the foregoing discussion, relating to the process of stock market development in Africa and that of capital market integration. First, the successful establishment and growth of stock exchanges in Africa are both dependent upon and a contributor to the process of financial reform and liberalisation. For a stock market to function there have to be minimal direct controls on the flows and pricing of capital, while at the same time a stock exchange can help to develop the effectiveness of financial markets and the allocation of finance within an economy. Second, the development of stock markets is affected by legal and institutional structures, as well as the availability of technology and information. These affect transactions costs, which are an important determinant of the level of trade and liquidity, risk, and the accessibility of the market, especially to small investors. There are also important issues relating to investor protection (legal environment and the quality of law enforcement) that influence the extent of stock market development. Third, African stock markets (except for the Johannesburg Stock Exchange) are small by international standards, in terms of number of listed companies, market capitalisation, and volume of trade. They are also illiquid, in that large trades may not be possible without triggering excessive price movements. Fourth, the above characteristics cause at least some African stock markets to be of limited interest to foreign investors, owing to their small size, lack of suitable stock, high transaction and information costs and lack of legal or institutional investor protection arrangements.

These characteristics indicate that there may be some gains available through the integration of African markets. In particular, regionally integrated markets (whether through linked national markets or separate regional markets) offer the potential to achieve higher uniform standards, to improve technology and access to information, and to reduce transactions costs and benefit from economies of scale. While there remain numerous obstacles to such integration, including different national legal and institutional environments, and economic barriers such as exchange controls, there are also significant potential gains. However, achieving this objective will require coordinated efforts by participating countries, to ensure that the necessary common high standards of regulation and supervision are achieved, as well as the necessary infrastructural development. It is also likely that integration will be easier to achieve amongst countries with common legal backgrounds, such as within Anglophone or Francophone groupings, than between countries with highly divergent legal traditions.

Notes

1. In the case of closed registers, prices may differ across exchanges. An example is Zimbabwe, which has closed registers for cross–listed stocks, and the price of an Ashanti Goldfields share bought in Harare will not necessarily be the same as one bought in Accra, London or New York, because a share bought in Harare cannot be sold on those exchanges.

2. Market microstructure theory investigates how securities are traded and the influence that trading systems have on market behaviour and success. Microstructure theory highlights the importance of stock market institutional features and trading mechanisms as important determinants of market behaviour. Madhavan (1993) develops a theoretical framework that compares different trading structures.

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Part Two

Policy Options and Responses

The Prospects for Integration Have Improved

*Lansana Kouyate**

In Africa as in other regions of the world co–operation for economic integration has become a recommended stage in the development process. To be sure, this stage is not obligatory for achieving economic development. Many countries in isolation by their effort and even domestic sacrifice have been able to attract foreign investment to assure economic takeoff. However, integration undeniably meets the demands of an increasingly global and open economy. It is reasonable to assume that countries such as African countries which have not been able to achieve development by policies carried out since the 1960s, policies to a large extent restrictive and protectionist, today would have better chances of success with regional integration. The international environment also now suggests that the freedom of economic agents need is indispensable. The continuation of efforts for regional integration is based on the conviction that a more united Africa will have a greater chance of overcoming obstacles to its development. However, the attempts already made in Africa and elsewhere in the world show that co–operation and economic integration are strewn with difficulties during their creation and even more subsequently when the ideals expressed in the various founding agreements and treaties are put into practice. In Africa in particular progress has been slow to show itself. That is why the co–operative study of the steps leading to economic integration should be a concern of all the many people interested in the future of Africa.

Types of Regional Groupings

Schematically, it is possible to distinguish between three main types of regional groupings among developing countries:

a) Those whose integration is closely linked to European integration, such as the Mediterranean countries;

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b) The middle income countries, which are relatively advanced in the process of integration, mainly in Latin America with the MERCOSUR and Andean Pact, and in Asia with ASEAN.

c) The other developing countries, mainly in Africa, where regional integration is confronting political, economic and institutional difficulties.

This paper will deal with the difficulties of regional integration in Africa and its prospects.

On the whole, integration programmes in Africa have six main objectives:

i) Trade liberalisation, in particular the elimination of tariff and non–tariff barriers in interregional trade;

ii) Establishment of a common tariff and trade policy *vis–à–vis* third countries;

iii) Elimination of all obstacles to the free circulation of people, services and capital between the member states;

iv) Harmonisation of macroeconomic and sectoral policies;

v) Creation of a monetary union in some instances;

vi) Handling socio–political crises to improve peace, security and stability.

Progress in carrying out these six main objectives has varied, with some integration programmes having advanced more than others in particular sectors. In this respect, the South African Development Community (SADC) and the Common Market for Eastern and Southern Africa (COMESA) have achieved some noteworthy results in co–ordinating sectoral policies. The Economic Community of West African States (ECOWAS) has made real progress in the free circulation of people, development of infrastructure and the settlement of conflicts, while the eight ECOWAS countries belonging to the West Africa Economic and Monetary Union (UEMOA) have had more success in trade liberalisation with the advantage of a common currency.

It is highly encouraging that the organisations for integration in Africa have begun consultations to exchange experience and possibly to shift their initiatives. The ECOWAS is doing this with the other organisations mentioned here in order to clarify the obstacles to integration, an arduous exercise. These obstacles range from the simplest to the most complex, and from the most subjective to the most objective. The obstacles listed here are the ones encountered daily by the ECOWAS secretariat.

Institutional Obstacles

The success of integration is closely linked to the national administrative performance of countries. At all levels, these administrations are marked by a considerable instability of personnel. The follow–up of files on integration is therefore

disjointed. Also inter–ministerial co–ordination is not always adequate at the national level. Very often decisions by regular community institutions are not passed on to all the ministries concerned. This happened after the ECOWAS adopted a moratorium on importing, exporting and manufacturing light weapons. Moreover, another minister of the same country during a final council of ministers sometimes opposes decisions initiated by a minister in the name of a country during sectoral meetings. As a result of these inconsistencies community decisions are implemented slowly. Also, some signatures are affixed at the very same moment when the reservation not to apply the decision has been signed. This raises the question of respect for engagements undertaken. This question of respect for engagements still arises in the ECOWAS despite an amendment to the treaty in 1993 giving community decisions a supranational character and immediately enforceable after a quorum of ratifications has been acquired.

Another institutional obstacle is that there are many organisations dealing with integration in the same region which compete for the same objectives. This dilutes both human and financial resources and leads to overlapping.

Political Obstacles

Conflicts and civil wars having multiple origins are a worrisome cause of delay in African integration. Wars also lead to a problem of confidence between partners in a community enterprise because of diminished economic and financial resources and the loss of human resources from death or exile. Not only are programmes of building infrastructure interrupted (as in the case of making interconnections between roads in the countries of the Mano River), but the management of conflicts itself absorbs a major portion of a community's time and resources, which become losses for economic integration.

Economic Obstacles

Regional integration is also made difficult by economic obstacles. International transactions in various African countries are subject to different trade and exchange rate regulations, tariff barriers are very high in several cases, and some commercial operations are subject to extremely long and costly administrative procedures.

Some aspects of monetary and fiscal policy in different countries also impede regional integration. These include differing policies on exchange rates and regulations on exchange rates, and overvaluation of exchange rates. Different fiscal policies also lead to a lack of alignment of prices which affects the business climate. Satisfactory convertibility of currencies is indispensable to regional integration.

The deficit of basic infrastructure like roads, telecommunications and electrical energy are also economic obstacles that lead to additional costs which hinder trade.

Other factors that impede integration are linked to a lack of sufficient numbers of private enterprises and their small scale, as well as the lack of complementarity among African economies. Actually African countries are essentially producers of basic raw materials that they sell to industrialised countries. They thus compete with one other.

Countries that join an integration arrangement often expect that its benefits will be divided equally, which is rarely the case, especially in the short run. In some instances the most advanced countries in the group obtain the greatest benefits, which discourages the countries that do not benefit from increased trade or investment. The benefits of integration are often obtained in the long term, when the region is endowed with a common market, that is, integration at the level of production, trade and investment.

Economies of scale within a vast integrated market have particular importance for the African situation in the context of the world economy, characterised by information technology and regional groupings always becoming larger. By profiting from the lessons of Asian and Latin American experience with integration, where intra–regional trade in some organisations reaches 50 per cent of trade with third countries while the highest level in Africa is only 11 per cent, it can be said with certainty that successful integration follows a number of guiding principles that should be used judiciously.

The success of regional integration in the first place depends largely on internal political and economic stability. In fact, each country should enjoy good political and economic health to contribute effectively to the success of regional integration and benefit from it. It is important to underline these fundamental principles at a time when in some African countries there is an upsurge in ethnic conflict and civil war, with a weakening of governance, which in turn leads to economic stagnation. Regional mechanisms to improve political and economic governance are necessary, even though the efforts to achieve stability (political and economic) occur at the national level.

Political principles adopted and implemented in a regional framework to strengthen democracy and human rights, can facilitate political stability at the national level. The member governments of the ECOWAS have adopted such a declaration to forbid all use of force to change democratically elected governments. Furthermore, our organisation has a mechanism for preventing, resolving or handling conflicts to encourage regional peace and security.

High rates of economic growth are indispensable to regional integration. In order to achieve this, African countries should create the conditions for sustainable development of their economies by combating more systematically high fiscal deficits, inflation and overvaluation of the exchange rate of their currencies. Several countries of the continent are doing that. But measures for stability and economic revival are hampered by Africa's foreign debt. A reduction of the stock of debt of African countries would improve the prospects for economic growth. Moreover, a regional pact for stability, growth and convergence still has good chances of improving the fiscal and

financial management of countries in the framework of harmonising macroeconomic policies. That is what the UEMOA and ECOWAS have done by adopting criteria for macroeconomic convergence.

The success of regional development and integration policies also is largely dependent on the degree of openness of African economies. Recently, international financial institutions like the Bretton Woods institutions and the African Development Bank have recommended what can be called an open regionalism, which signifies, first and above all, continuing efforts for liberalisation and simplification of investment and trading regimes under the framework of the WTO rules. Several African countries have progressed in trade liberalisation in recent years, but problems remain in many countries in which cheap imports threaten some infant industries. Integration, openness and technology transfer should be the components of a single approach. As long as trade is a threat to production, there will be strong reserves to opening markets and integration. Trade should not snuff out production. For that reason, technology should be transferred, industries transferred when the destination countries have created all the conditions for that, namely peace and stability, a modern legal system and skilled human resources.

Although liberalising trade on the continent is crucial, it is also important that African producers have easier access to markets of the advanced economies by lowering tariffs on African goods at all stages of production.

The development of a unified regional economic space requires competitive markets, which are predicated on the free circulation of factors of production and upgrading of human capital. Africa should particularly invest in human capital to build a skill–based economy. That means fighting against illiteracy and endemic diseases, and training many mid–level technical managers. Education and health remain primarily the concern of individual countries, but regional programmes of development of human resources are necessary to strengthen national capabilities.

Improvement of the business climate is necessary for the development of the private sector, which may invest major financial resources to utilise economies of scale and business opportunities of a larger market that can increase the return on investments. At present, an inadequate legal and judicial framework for enterprises handicaps the African private sector, and that should be improved. That is mainly the role of governments, which have to improve incentives and investment codes and rationalise the procedures for enterprise creation. To facilitate the private sector's intervention in the process of regional integration, businesspeople should develop networks and organise strong lobbies capable of defending their interests better. The African and foreign private sectors have considerable possibilities of investment in energy, as exemplified by the West African gas pipeline initiated by the ECOWAS, linking Nigerian gas fields with Ghana and going through Benin and Togo. ECOWAS programmes also include the interconnection of electrical networks, the creation of the West African Power Pool and other projects that could interest the private sector like in telecommunications, coastal shipping and air transport. The West African private sector with the participation of ECOWAS has also established the ECOBANK, one of

the most dynamic commercial banks of the region. EWOWAS via the ECOWAS Fund is the majority shareholder. We believe that projects like these can get the private sector involved in the process of regional integration.

In conclusion, regional integration should have a central place in long–term strategic thinking for Africa. Integration is not simple addition. It primarily increases the compatibility of plans, policies and programmes of a group of states to maximise the gains from growth and development. It is also creates the conditions for extending healthy and efficient management standards to a group of countries. The prospects for integration in Africa are better today than in the past. Profound positive changes are occurring in most African countries. Moreover, by proposing Regional Economic Partnership Agreements with regional economic groupings of developing countries, the European Union countries show they are no longer interested in trade or investment in countries with shallow markets. This means Africa no longer has a choice. It must integrate or suffer the consequences of an increasingly integrated world economy. Thus it appears that the strategy for African development should be rethought by taking into account the need for regional integration to adapt to the new world economic and geopolitical situation.

Regional Integration in Africa and the Global Economy

*Rt. Hon. Clare Short MP**

Multilateralism or Regionalism?

The British Government published in 2000 a new White Paper on "Making Globalisation Work for the Poor". It accepts that globalisation is a fact of history, and asks what we all should be doing to bring its benefits to poor countries and poor people. The White Paper advocates multilateralism.

We also recognise and applaud the fact that African countries in the Abuja Treaty committed themselves to integrate their economies, and to forge an economic union. This Treaty advocates regionalism.

What we would like to argue today is that there is no need for Africa to choose between multilateralism and regionalism. These are not two conflicting strategies. On the contrary, in meeting the challenges of globalisation, regional integration and co-operation are vital complements to multilateralism. To give it a name, we believe that Africa should practise "open regionalism". Our reasons for believing this fall under three broad headings: economics, business, and negotiation.

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* Speech delivered on behalf of the UK's Secretary of State for International Development, by Adrian Wood, Chief Economist, Department for International Development

Economics

As regards the economics, expansion of trade among African countries could certainly yield efficiency gains. One reason is that there are striking differences in resource endowments among countries within Africa, more so than in most other regions. Countries with abundant land and scarce labour adjoin others with abundant labour and scarce land, providing the potential for mutually beneficial exchange of different sorts of goods. These and other sorts of gain from specialisation among neighbours have not been realised in Africa because of the persistence of internal trade barriers. COMESA has made remarkable recent progress towards freeing trade among its members. But the SADC trade protocol is not yet implemented, and the large South African market is still protected against imports from neighbouring countries.

Expansion of trade within Africa, however, could not be sufficient for rapid growth. Pursuing internal free trade without also lowering external barriers would be inefficient. It would inflict on African consumers and firms the high cost of producing some goods within Africa which could be imported in exchange for exports produced at a lower cost. The underlying cause of this inefficiency is that Africa, even if it were fully integrated into a single market, would just not be a large enough economy to permit the full range of goods and services to be produced on an optimal scale. This is especially so at present, when sub-Saharan Africa's GDP is roughly equal to that of the Netherlands, but it will continue to be so into the future: even the largest regional economies, such as Europe, benefit from external trade.

An even more important economic reason why Africa must also expand its trade with the rest of the world is that, for all developing countries, much of the gain from trade comes not from increased efficiency of a static kind, but from the transfer of technology and know-how from other countries, particularly developed ones. Tapping into the global pool of knowledge will be crucial if Africa is to increase greatly the productivity of its resources, natural and human, and hence to raise the incomes of its people. These increases in productivity, moreover, will allow increases in trade in all directions simultaneously, within Africa as well as between Africa and the rest of the world. In other words, because Africa's trade is now small — the exports of its 600 million people are scarcely more than those of Malaysia's 20 million people — there is vast scope for both regional and multilateral trade to grow, and less need to worry about possible trade-offs between them.

Business

The second heading under which to make the case for open regionalism is business. Over the past few decades, sub-Saharan Africa has seen its share of world trade shrink drastically. This has not been mainly because of unusually restricted access to foreign markets. All developing countries have suffered from protectionism in

developed countries, but Africa has had preferential, often duty-free, access to many external markets. The main reason for the fall in market share has been lack of competitiveness, caused by insufficient investment in production and infrastructure, expensive and inadequate transport, and high transactions costs of all kinds. Underlying many of these causes in turn is Africa's unfortunate reputation as a difficult and risky place to do business.

Regional co-operation and integration could play a big role in overcoming these problems. This is already happening to some degree. There is co-operation in SADC on transit facilitation; COMESA is working on facilitating cross-border payments and competition policy; and OHADA is harmonising business law and the investment code, and is setting up common commercial courts. These are very positive initiatives. But there is scope for much more co-operation of this kind — to reduce transport costs and delays, simplify customs and regulatory procedures, recognise professional qualifications, and establish common regimes for competition, investment, product standard certification and intellectual property. We salute the Cross-Border Initiative in Eastern and Southern Africa, which encourages these forms of confidence building co-operation.

Regional institutions thus could and should help to raise Africa's profile in world business — improving its image as a host to investment and as a source of goods and services, creating a reputation for legal transparency and predictability, and reducing transactions and compliance costs. All of this is urgent, and faster progress needs to be made. Regional institutions can also play a valuable role in resolving Africa's conflicts, which are badly damaging its economic development. We must work together to improve the effectiveness of UN systems and for the full and speedy implementation of the Brahimi report. In any country peace is the most basic condition for prosperity.

Negotiation

The third aspect of the case for open regionalism concerns negotiation. African regional institutions can help African countries to integrate into the world economy by facilitating their ever more complex institutional relations with the WTO and with external trade partners, particularly the EU.

African countries are a large share of all WTO members. But some are not represented in Geneva, and some need technical support in defining their positions and pursuing their objectives. Help is already available, for example from the ACP Secretariat and the Commonwealth Secretariat; but there is also a role for African regional organisations — both in providing policy steer and co-ordination, and in technical back-up. Similar considerations apply to the proposed new Round of multilateral trade negotiations. To maximise their gains from a new Round African countries need to act together, and African regional institutions could co-ordinate and lead this joint action.

The regulatory agreements of the WTO, to which African countries committed themselves in the Uruguay Round, impose heavy administrative burdens of implementation. However, there are economies of scale in implementing WTO agreements, such as those on customs valuation and technical barriers to trade. Regional organisations can step in on behalf of member states to meet regulatory requirements which might overwhelm the national authorities of small countries.

The Cotonou Agreement with the EU poses a particular future challenge to African regional groupings — that of consolidating to negotiate free trade agreements compatible with the interests of the members of each grouping, enhancing their market access and competitiveness, and assisting them with adjustment. These negotiations will be difficult, complex and important to Africa's future. Its regional institutions must start preparing for them now.

Politics

Will Africa's regional organisations be able to do all these useful things? We think the answer is yes, provided that two conditions are met. One is financial support for extending the scope of their activities, which we believe will be forthcoming. Much assistance has already been provided, particularly by the EU, and new funds have recently been committed, for example for capacity building prior to negotiations to implement the Cotonou Agreement.

The other condition is for Africa's regional institutions to be given the necessary political mandate by their member states. Can the complex web of overlapping groupings be rationalised? Will their member countries allow these institutions to exercise a sufficient degree of leadership in policy formulation and implementation? How will pan-African regional institutions relate to the sub-regional groups which have so far made the running in regional economic integration? How can these institutions durably solve the problems which arise when the benefits of integration are uneven, and when some countries may face losses? These are questions for Africa to answer, and they are hard questions, but we believe that answers can be found.

Conclusion

In conclusion, regional integration and co-operation in Africa could be an important, indeed essential, stepping stone to the sort of integration into the world economy which is needed to raise incomes and reduce poverty. For Africa to meet the target of halving the proportion of people living in poverty by 2015, it would need to grow at 7 per cent per year. Currently, some African countries are achieving this, but most of them are not. The new Millennium African Partnership is aimed at improving this situation. The British Government is strongly committed to supporting that partnership, in which we believe open regionalism has a vital part to play.

Regional Alternatives and National Options

*Jakaya M. Kikwete**

Africa is mankind's last frontier in the fight against poverty, deprivation and backwardness. The fight is indeed tough and a big challenge. But it is a war that we must fight and win for it is too horrifying to contemplate the consequences of losing. It is a fight that all of us must join in irrespective of the continent or country we live in, creed or colour we belong to. For if development eludes Africa for long, everyone on this planet will suffer its consequences. If, for example, the migration of a few fortune seekers from Africa today causes such a stir in Europe, what would the imminent mass exodus in the few years to come do if poverty were not eradicated? Wars, conflicts and conflict situations with their attendant evils of loss of dear lives, destruction of property and mass displacement of peoples which are prevalent today would increase or worsen in future if the poverty syndrome were not broken for good. But wars and conflicts in Africa, as is always the case, concern everybody in the world and preoccupy people beyond the African continent. The only way to overcome all this is to help Africa attain higher levels of development and eradicate poverty. This is a very serious matter that requires serious attention and intervention. The interest demonstrated by OECD and ADB in this is therefore highly appreciated.

Regional integration in Africa is not a new subject. Africa has a long history of association with regional integration affairs albeit a chequered one with a record of both lofty successes and abysmal failures. One encouraging thing, however, has been the fact that even when failures did occur the parties concerned did not let the spirit die but tried hard to pick up the pieces and walk upright again. This serves to demonstrate the clear understanding, firm commitment and belief on the part of African leaders and peoples in the correctness of regional integration in Africa. By way of example, let us mention the East African Community, which died in 1977 but has been revived and relaunched with much pomp and ululation on 15 January, 2001.

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During the discussions on the creation of the Organisation for African Unity in 1963, regional integration was underscored. The vision of some leaders at the time was to go for a one–step move towards African unity thus creating a United States of Africa. However, some other leaders realistically argued for a gradual approach to African unity. They contended that while continental unity was politically desirable, it was not practically implementable at once. They proposed that Africa would have to achieve unity by stages through political and economic co–operation with regional economic groupings being the building blocks in a step–by–step fashion. The latter view, which was held by the majority, prevailed and was adopted by OAU. In fact, the OAU has worked tirelessly for the creation of regional economic groupings in Africa. The OAU also has been working very closely with all these groupings as part of a strategy for building the Africa Economic Community.

Following this approach, beginning from the 1960s to date, the African continent has witnessed unprecedented creation of regional integration projects. Among the prominent regional integration schemes are: Southern African Development Community (SADC), Economic Community of West African States (ECOWAS), Common Market for Eastern and Southern African States (COMESA), the Maghreb Union, Inter–Governmental Authority on Development (IGAD), East African Community (EAC) and Union of Central African States (UDEAC).

The experience of these regional groupings varies from one group to another. Some have recorded momentous progress while some have recorded modest progress. Some stagnated while some completely died or are about to. SADC, COMESA and ECOWAS prospered. IGAD recorded modest progress while UDEAC and the Maghreb Union stagnated. The East African Community died in 1977, to be revived about two and half decades later. The KBO and CPG are in limbo.

The defunct East Africa Community was a successor organisation to the East African Common Services Organisation founded in 1961 in place of the East African High Commission which was in turn formed in 1947. The East African High Commission was the crystallisation of the many co–operation and integration initiatives undertaken before 1947.

During its lifetime, the East African Community had attained a high level of economic integration. At that time, perhaps, EAC had reached a level which had not been attained by any organisation of its type on the continent. The East African Community had a Customs Union, a joint Income Tax Board and regime, a Monetary Union with a common currency (the East African Shilling) and an East African Currency Board. The railways, airlines, posts, telecommunications and such other services as meteorology were jointly owned and managed under the Community. The East African Development Bank, the University of East Africa and many more were all East African entities of the Community. Briefly, almost the entire legal, social, economic and cultural life of the three countries of Kenya, Uganda and Tanzania was predominantly East African. It was only political life that remained different. This turned out to be the major causal factor to the weakening and eventual demise of the regional integration fabric so painstakingly built over the years beginning from 1900 when Uganda and

Kenya first established a joint customs revenue collection arrangement. It is this arrangement that gave birth to the East African Customs Union in 1919. Later everything was added to it.

That model regional grouping died for a number of reasons but there were four main ones. First and foremost, the variability of economic policies pursued then by the partner states. For ideological reasons, Tanzania was pursuing socialist policies while Kenya was pursuing essentially capitalist policies. After the overthrow of President Milton Obote, Uganda was in the grip of a military dictatorship but with policies which had a bigger capitalist accent. Capitalism and socialism were inherently hostile ideologies, a phenomenon which infested the East African Community and affected its well–being. Secondly, the international political climate of the times was not supportive of regional integration where partners subscribed to contentious and hostile ideologies. In the late 1960s and early 1970s the Cold War rivalry was at its peak. So whenever a division along the East–West divide occurred the tendency had been to push the two sides further apart. Under the circumstances therefore the East African Community became the net loser.

The third important factor that contributed to the weakening and eventual death of the East African Community was the continued perception of disproportionate sharing of benefits occurring from economic integration, and in particular the lack of adequate compensation mechanisms to redress the situation. The problems could not be resolved easily and quickly. It was always dependent upon the goodwill and wisdom of the leaders.

Unfortunately for the East African Community, and this is the fourth major factor, the political atmosphere in East Africa was heavily polluted in the early 1970s. The pollution was caused by the coming into power of dictator Idi Amin in Uganda. President Julius Nyerere opposed the military takeover in Uganda in principle, and vowed never to sit at the same table with Gen. Idi Amin. The relations between Idi Amin and President Jomo Kenyatta of Kenya were not good either. They were what one could characterise as uneasy calm due to Amin's claims over parts of Kenya and Tanzania. At the same time relations between Kenya and Tanzania were strained as both countries engaged in derogatory name–calling against each other for deeper ideological reasons. Under such circumstances, the East African Community's topmost authority could not meet to discuss Community affairs. Many issues remained unresolved until it could not be borne any more, hence the demise of this model of regional integration initiative.

There were also some other factors, which may not have been very critical but cannot be overlooked. Among them was the factor of limited participation of the private sector and the general population as a whole in community affairs. The East African Community was a creation of the three governments and owned and managed by its leaders. Since there was little involvement of the population in the affairs of the Community, the people lacked sense of ownership of the institution and had no say. That way it became easy for a few unscrupulous leaders to kill the organisation for personal reasons.

Even today, the variability of economic policies pursued by partner states, disproportionate sharing of benefits of economic integration and lack of adequate compensation mechanisms to redress the situation, political disharmony between member states and limited participation of the civil society and the private sector, are still areas of serious concern. They are also full of pullback strings that cut across regional integration schemes in Africa. Political instability or conflict in one member state can also have a pullback factor, especially if the conflict impacts negatively on the neighbours.

Selfish pursuit of parochial national interest at the expense of regional interests can be a dangerous factor to guard against in the interest of successful regional economic groupings. For a successful economic grouping, regional interests need to be paramount over national ones. If that is not going to be the case there can be no integration. Of course, the regional interests should be defined in a manner that they don't undermine those of a partner state but act to advance them. This is another important matter to note because, in the final days of the East African Community, it was this factor more than any other which dealt the final blow to the Community. Regional integration may also suffer as the result of flawed conception, defective policy formulation and haphazard execution of policies.

It is essential to assess the result of regional integration and economic co–operation whenever such attempts have been made, so that mistakes of the past do not remain the obstacles of the present only to become the lost opportunities of the future. This is precisely what has been done with the new East African Community. The past was carefully studied and the lessons learnt formed the basis of the design of the new entity.

The primary preoccupation of all of us is to improve living standards of our people by facilitating an adequate and economically, socially and ecologically sustainable development process in our respective countries. On the one hand it is about increasing people's incomes so that they can afford the essential social and economic amenities of livelihood. On the other, it is a matter of affording them adequate and quality social and economic infrastructure and services such as health, education, water, energy, transport and communications.

We are all aware of Africa's weaknesses: economic, financial, technical as well as technological. There are also weaknesses related to a fragile political and social base at both institutional and organisational levels. Regional integration provides an opportunity for us to reduce our weaknesses or even overcome them completely. Also, in the current globalised world, regional integration avails us the opportunity of being possible players and not mere onlookers.

Although there is no doubt about its importance and some successes have been recorded with varying degrees, regional integration in Africa still faces a number of difficult challenges. Economically, there is the problem of small national markets coupled with low effective demand. There is inadequate and inefficient economic infrastructure (roads, railways, ports, inland waterways, power, telecommunications, etc.) and trade imbalances between partner states. There are also problems related to low levels of capital/labour ratios as a result of low capital investments, and too small

flows of foreign direct investments to Africa. Low levels of productivity in agriculture and industry, an underdeveloped services sector and weak capital markets add up to the long list of problems facing the African economies.

Socially, in our countries, people's incomes are low and hence there is widespread poverty. There is also a high incidence of diseases and insufficient and ill–equipped education facilities. Politically, we face challenges through threats to security, civil strife, refugees and fragile democratic systems. Technologically, Africa has recorded low levels of acquisition and application of technology; low levels of capitalisation and application of technology especially in agriculture as well as low levels of resource allocation dedicated to research and development. The low level of computerisation has curtailed Africa's access to the information super highway.

These challenges will be addressed effectively and efficiently if the integration projects we are developing are well co–ordinated, and resources are maximally utilised and well managed. It is expected that our development objectives can be achieved faster by pulling together the scarce resources available and by jointly planning and implementing cross–border projects.

It is an imperative, therefore, that regional integration in Africa should be pursued within the framework of regional development strategies. These strategies should favour rational and joint economic management of scarce resources based on the principle of economies of scale, the formation of viable economic blocs, provision of efficient services and production of goods for bigger regional and global markets. Yet this cannot be accomplished effectively while a large part of Africa is still faced with a multitude of crises. What Africa needs is the establishment of viable political systems, if we want to have collective initiatives that lead, gradually or cumulatively, towards sustainable economic integration. Such initiatives can come primarily from indigenous social forces such as parliamentarians, business organisations, industrialists and traders' associations, professional bodies and trade unions that have concrete interests in the positive outcome of regional integration. Support from understanding external friends would of course be useful.

Africa has a long history of being associated with regional integration and therefore has the necessary experience. This experience should be shared and used so that mistakes of the past are avoided and viable regional integration schemes are created. Therefore, Africa must make sure that the conception is not flawed, that defective policy formulation is avoided and there is no haphazard execution of such policies. Proper care must also be taken in the process of building the economic grouping. It should be realised that this should be a gradual, carefully planned process and that all stakeholders have to be kept well informed and adequately involved.

In conclusion, Africa needs political leadership and people who are willing and committed to the integration process. Africa must develop attractive regional alternatives to national options for development. Africa must have its own agenda for entering the global arena and take new and much more imaginative initiatives for its future development. The expectation of increased benefits as a result of integration compared with the situation without integration is the most fundamental incentive for regional integration in Africa.

Europe’s Commitment to Coherent Regional Initiatives

*Koos Richelle**

The theme of regional integration is crucial for us at the moment when we are starting discussions to implement the Cotonou Agreement, although at this stage our ideas are not as concrete as some of you had hoped and others may have feared.

The EU is a natural supporter of regional integration initiatives, not just in words, but also by earmarking €1.3 billion over the next five to six years, amounting to around 10 per cent of EU financial support to ACP countries. This is because of our own positive experience. The overall success of European integration over the past half century in terms of economic and social progress and peace went beyond the expectations of the founding fathers. However, the European integration context is highly specific and very different from the situation in developing countries. While there are certainly important lessons to be drawn from the way problems were solved in the European context, I would like to warn against the tendency towards duplication.

The EU at present provides support to virtually all the African integration initiatives. We make every effort to direct this support to initiatives with good prospects for progress and a genuine commitment and ownership. This is not always easy. There have been disappointments, often because the agenda was too ambitious. We should draw lessons from this.

As you know, the new Cotonou Agreement emphasises regional integration both as a development strategy and as a key component of the trade strategy. It is a step towards beneficial integration into the world economy. The Agreement underlines the importance of good performance as a criterion for resource allocation. This is a challenge for all of us, but it will lead to better results.

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The basis for the definition of regional programmes is laid out in Annex IV, article 7 of the Cotonou Agreement, which states:

"The ACP States concerned shall decide on the definition of geographical regions. To the maximum extent possible, regional integration programmes should correspond to programmes of existing regional organisations with a mandate for economic integration. In principle, in case the membership of several relevant regional organisations overlaps, the regional integration programme should correspond to the combined membership of these organisations. In this context, the Community will provide specific support from regional programmes to groups of ACP States who are committed to negotiate economic partnership agreements with the EU."

From the above text we can deduce a number of elements:

i) The initiative for the definition of programming regions lies with the ACP States.

ii) In arriving at this definition, the ACP States should take as a starting point organisations with a mandate for economic integration.

iii) Where there is an overlap in membership, the programming regions should in principle correspond to the combined membership of these organisations.

On the basis of these elements we can deduce a number of guiding principles for the regional programming exercise.

The first of these principles is that, whereas in the past the Commission determined the geographical definition of regional programmes, this is no longer the case. Thus, we cannot assume at this stage that the existing regional programmes will continue. The current regional programmes under the 8th European Development Fund (EDF) are as follows: Caribbean, Pacific, West Africa, Central Africa, East Africa, Southern Africa, Indian Ocean. This is not to say that none of these regional programming definitions will be carried over to the 9th EDF. However, in the absence of a formal decision from the ACP the text of the Agreement does not allow us to assume that 9th EDF programming regions will be same as those of the 8th EDF.

The second guiding principle for the definition of programming regions is that these regions should correspond "to the maximum extent possible" to the membership of organisations with a mandate for economic integration. The situation in the Caribbean and the Pacific is not complex, both regions having essentially only one organisation with the relevant mandate. In Africa however, the list of organisations with a mandate for economic integration is long and many countries are members of several groupings. Nevertheless, on the basis of this principle, it is logical to exclude organisations with a mandate for functional co–operation (river basin management, infrastructure, drought etc.) as a basis for programming regions. There is a multitude of such organisations in Africa, examples being CILSS (Comité Inter–étatique pour la Lutte contre la Sécheresse au Sahel) and OMVS (Organisation pour la Mise en Valeur du Fleuve Sénégal).

The third principle derived from article 7 is more problematic than the two previous ones. In effect, the question of overlapping membership of organisations with a mandate for economic integration has the potential to create a radical change in the current structure of regional programmes. We are at the moment awaiting the results of the discussions on this issue among the states and regional organisations concerned.

We have emphasised the necessity for countries in a region to exercise ownership of regional activities from the outset. In this respect, there is a need for consistency between the national level and the level of regional organisations. In this context the PRSP process should take into account the regional dimension.

In addition, regional integration must be fully coherent with the multilateral trading system, because it is only part of an outward–oriented strategy. This is important in view of the planned new multilateral trade Round, which must fully reflect the needs of the developing countries.

The timetable for moving towards Regional Economic Partnership Agreements (REPAs) is the following: negotiations should start during 2002 and should be concluded not later than the beginning of 2008. REPAs should build on regional integration initiatives of the ACP countries. The result must be WTO compatible.

One of the key requirements towards constructive regional integration is capacity building and institutional strengthening. This also includes analytical capacity. Regional integration of developing countries, provided it is not aiming at forms of regional autarky, is fully compatible with progress of the multilateral trading system. Especially for small economies and for the least developed countries, regional integration provides an opportunity to pool resources, reduce costs and improve capacities in trade and trade–related matters.

Regional integration is not a new subject. African countries have recognised for a long time that they must collaborate to overcome the limitations of their small economic size and to reduce their vulnerability. There are many dimensions of vulnerability, for example the dependence on very few agricultural or mining exports and the lack of infrastructure, especially affecting the land–locked countries. Regional integration is part of a strategy to reposition in order to take advantage of the opportunities resulting from globalisation and to be stronger to handle the various risks and threats.

Moreover, uncoordinated macroeconomic reforms, including trade liberalisation, can be harmful in the neighbourhood. In comparison to unilateral uncoordinated measures, regional integration can be socially and politically more sustainable, because adjustment costs can be limited and spread over time.

A key point to be stressed is that successful regional integration contributes to consolidating peace and stability. This has always been one of the main political objectives driving European integration. It has become increasingly relevant for integration of developing countries.

There are numerous obstacles that delay or prevent successful integration. A number of basic pre–conditions must be fulfilled to make progress. These are in both the political and economic fields. Peace and security, political stability, democracy and good governance are key aspects together with sound macroeconomic management. Over and above there must be shared values and beliefs. Unnecessary to say that it will often take a lot of time to achieve these pre–conditions.

Membership of an integration body should not be quasi automatic following political declarations, but should amount to a real commitment in terms of policies, burden sharing and solidarity. A serious integration initiative would call for a serious negotiation before entry. Enlargement in the EU for instance has always been a fairly lengthy process despite the strong political will to move ahead. This is because it takes time for the new entrants to reach the *acquis communautaire*. In the African region, some organisations grew very quickly, without much consideration of any *acquis*. SADC went over a short period from nine member states to 14. COMESA also rapidly increased its members to more than 20. Moreover there is a very sizeable overlap between both organisations currently comprising nine member states. Lack of coherence in objectives and approach is hampering progress and leads to waste of resources. This is a matter to be dealt with urgently and on a basis of full ownership of the countries involved.

One aspect of commitment is contributing to the budget. It is well–known that many countries do not regularly pay their share of the budget. Even though the situation has improved for example for COMESA, there are cases such as in ECOWAS where member states failed to contribute for a long time. There should be clear consequences or sanctions for member states that do not fulfil their obligations. Examples of sanctions could be that countries who are in arrears can no longer chair meetings or take part in votes, or their nationals could no longer be hired by the secretariat. Of course, it is vital that the burden sharing among member states is fair. Improvements are needed in this respect. Countries who feel that the benefits are not in line with the contribution should consider leaving the organisation. The fact that member states do not fully pay their contribution leads to a frequent situation of donor dependency and diminished sense of ownership.

There should also be a much closer follow–up of the specific agreements that are made in regional integration initiatives. Very often, we see (almost endless) postponement of the implementation of agreements, for example trade liberalisation in ECOWAS, but also in SADC and EAC. There is also hardly any information to assess progress. As you know, preferential trading arrangements call for the application of rules of origin. Information on the application of rules of origin is lacking. Our recommendation is for modest and realistic agreements to be effectively monitored. The time–horizon of the transition period must be reasonable. There should be enough resources for complementary measures to be carried out, for example to train and equip the customs services. A modest and realistic agenda should help to avoid back–tracking or reversal of policies. Such reversal gives bad signals to potential investors.

As an example of insufficient realism, ECOWAS announced in 2000 plans to create a second monetary zone (in addition to the CFA zone) by 2003 and a full ECOWAS monetary union by 2004.

The bottom line of regional integration is that the private sector (entrepreneurs and workers) and civil society in general should be able to collaborate across borders in a mutually beneficial way not impeded by many restrictions. It is the task of the governments to put in place the conducive framework in terms of rights and obligations, and infrastructure. For integration to be successful, it should not be a legal top–down framework or a purely government matter, but it should involve civil society in a meaningful way.

In conclusion, the EU remains committed to collaborate with the countries and organisations to create a more coherent regional economic space of which the benefits will be shared equitably. Regional integration is not a panacea, but is a worthwhile complement to a development strategy focused on human development and poverty alleviation.

Regionalism is controversial and always will be. Those who can enjoy a vast market and unified economic space often point to the failures and difficulties. However, the economic fragmentation of the African continent is such that there is no alternative to moving towards a more harmonised and larger economic space. But the transformation is difficult. Therefore the agenda should be realistic. The EU is ready to contribute to this process. Europe and Africa have a common interest for it to be successful.

Globalisation, Regional Integration, Economic Growth and Democratic Consolidation

*Michael Spicer**

Introduction

"In the Global Economy", Klaus Schwab, President of the World Economic Forum (WEF), has argued: "regional strength is paramount"[1]. Indeed, the development of regional units is synonymous with the age of globalisation and technology in which we live today; along with faster and larger international financial flows, burgeoning global trade volumes, reducing costs for more efficient transport and communication links, and the sometimes more pernicious spread of other transnational influences including crime, people–movements, environmental and health issues. Indeed, it is said that if technology makes globalisation feasible, liberalisation makes it happen[2].

This process of trade liberalisation has taken two, ultimately interlinked roads: global tariff reduction through GATT and the WTO; and regional integration. With regard to the global arena, the volume of international trade increased at twice the rate of growth of world output between 1985–94[3]. World output has expanded fivefold over the last 50 years, while world trade has expanded 16 times[4].

In the case of the latter area, the proportion of intra–regional trade to total trade has been steadily increasing: between 1980–1989 from 51 to 59 per cent in Europe, 33 to 37 per cent in East Asia, and 32 to 36 per cent in North America[5]. Today, 60 per cent of world trade takes place within regional trade blocs.

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The arguments in favour of closer integration should not, however, obscure the immense challenges facing regional units as they strive to overcome political differences and economic insecurities. In Africa, region–building has been a difficult task: intraregional trade accounted on average for just 6 per cent of African trade in 1990 and grew to just 10 per cent in 1999. In the case of the Southern African Development Community (SADC) region, for example, South Africa's market domination coupled with rather marked differences concerning leadership style and respect for democratic values and human rights, has made the regional project both complex and problematic. Similar difficulties have, unfortunately, been replicated throughout Africa — though conversely, it should be added, *these difficulties arguably make regionalism all the more necessary*.

I would like to highlight three issues:

— First, the relationship between regional bodies and development.

— Second, the challenges facing the job of "region–building" in developing countries, particularly in Africa.

— Third, how could we make progress with regional initiatives in Africa?

Regional Integration and Development

There are essentially two schools of thought as to the value of regional economic and political units. The first is that these represent building blocks or a stepping stone to fuller participation in the global economy — of so–called "open" integration. The second is that these units provide essentially a developmental bulwark against deeper global integration — the so–called "closed" integration thesis.

These two approaches are not necessarily mutually exclusive, however. In this regard, it is important to recognise differences between the needs of developing countries, in relatively immature stages of industrialisation, and those of states higher up the industrial chain. These are issues which the post–Seattle World Trade Organisation and regional bodies such as the European Union will have to take into account in the development of liberal trade and developmental regimes. It cannot be just a case of seeking *freer* trade, but *fairer* trade too. The resolution of such issues as market access to the developed world lies, for example, at the heart of President Mbeki's Millennium Africa Recovery Plan.

There are also misgivings about the untoward impact of rapidly liberalising economies, especially in striking a balance, as intimated above, between domestic needs and greater openness — taking into consideration the impact of openness on economic growth along with, *inter alia*, work conditions, gender issues and environmental standards. We should also realise that liberalisation can leave countries more vulnerable to external shocks, particularly those countries where the economic fundamentals are shaky and state institutions weak.

Such concerns are related also to the need to recognise that tariff liberalisation is but one of a series of economic and political initiatives which need to be implemented to achieve growth, including the establishment of an attractive investment environment, the need to develop technologies and skills, the implementation of a sound macroeconomic and fiscal policy, and the existence of efficient but not overbearing domestic institutions. Thus, *openness alone cannot achieve economic competitiveness*.

But the fact is that countries which trade more grow faster. O*penness can work.* And it works partly because it sends out a signal about what sort of economy the liberalising state wants to have — one that is open not only to trade, but also to ideas, people, skills and investment; one that wants to compete on a global stage; and one that stands for internationally acceptable political values and social practices. These points are particularly relevant to Africa in general, but above all to South and Southern Africa.

Indeed, studies show that developing countries with open economies grew by 4.5 per cent annually in the 1970s and 1980s; but those with closed economies expanded only by 0.7 per cent. Developed, open economies grew by 2.3 per cent annually; closed ones by 0.7 per cent[6]. Closed economies are regarded as those with the features of high import tariff and non–tariff barriers, a socialist economic system, a state monopoly on important exports, and a big gap between official and black–market exchange rates. It is, admittedly, sometimes difficult to work out whether protected economies do badly because they are cosseted, or because they have unsound macroeconomic practices. Yet this does not challenge the essential argument of the free–trade growth thesis in developing countries — that there is a striking correlation between export growth and overall GDP growth.

When assessing the value and practice of integrative attempts, it is also necessary to distinguish between the formal inter–governmental process of regional integration and the value of people–to–people contacts. Indeed, in Southern Africa, while the process of integration between governments has been comparatively problematic and slow, suffering often from a lack of real political will, the integration of people and economies through increased movement, investment and trade has been quick. The involvement of South African companies in Africa is one positive illustration of this process.

For example, since the collapse of apartheid, South African firms have been able to trade and invest without political handicap in Africa. In the trading domain, South Africa's overall trade with Africa increased by 130 per cent from R10.9 billion in 1994 to R25.3 billion in 1998, totalling R22.7 billion in SA exports and R4.3 billion in imports in 1999[7].

To take another example: there has been $3 billion worth of investment made or committed in Africa by Anglo American–controlled subsidiaries since 1999, with at least another $1.5 billion in the offing. This increasing involvement of South African–based firms in Africa has been replicated in other sectors beyond mining, notably in banking, brewing, retailing, cellular communications and insurance.

To sum up on this point: where governments positively embrace liberalisation they will find multinational corporations helping stimulate broad–based development by encouraging the creation of a range of services and institutions that they require to function effectively. This process has been dubbed by Professor Gordon Redding "the thickening of civil society"[8].

Challenges to Region–Building

Put simply, globalisation and the end of the Cold War have made it possible for nations to rediscover and strengthen regional links. In this process, it is acknowledged that economic development cannot occur in isolation. As Omar Kabbaj, President of the African Development Bank, has argued: "With about 800 million consumers, the importance of economic co–operation for Africa derives mainly from the opportunities that emanate from integrating the markets of individual countries on the continent. Large markets matter because they create new investment opportunities, enhance the production of tradable commodities, and encourage the flow of foreign direct investment. Regional integration could also help in building efficient infrastructure, strengthening regional security, improving human capital, and natural resource management"[9].

Yet it is important to recognise a number of critical constraints on regional free trade initiatives, particularly those involving African states (where attempts at regional integration, represented by a flood of acronyms, have mostly proved short–lived).

So what makes regions more likely to integrate successfully? Table 1 helps to identify those factors promoting or, alternatively, detracting from a regional integration imperative, against which it may prove valuable to examine both African and other initiatives[10]:

Table 1. **The Push and Pull of Regional Integration**

Positive Trends	Negative Trends
Geographic propinquity	Small economies, both in terms of population size and GDP
Cultural homogeneity	Relatively low level of trade within the region
Economic (trade and investment) and infrastructure integration and advantage, including: ▪ The greater the proportion of goods imports from the region and from member states in particular, and the smaller the proportion bought from outside this area ▪ The larger the internal market ▪ The lower the costs of transport among states ▪ The greater the diversity of production structures among member states	Heavy dependency on imports and foreign trade, in particular with advanced industrialised countries
Common and related security concerns, and an absence of major political/security disagreements	Shortage of value-added products
Common political values	Low level of industrialisation

Thus the relatively small size of African markets, and their location sometimes remote and disconnected from infrastructure networks, are undoubtedly problematic for regional integration schemes, given especially the large and disparate number of member states involved: for example in the Economic Community of West African States (ECOWAS) with 16 members, the Common Market for Eastern and Southern Africa (COMESA) with 20, and SADC with 14. These weaknesses are exacerbated by problems of duplication of objectives and overlap in terms of membership between regional bodies (such as, for example, COMESA and SADC; and ECOWAS and the francophone Union économique et monétaire ouest–africaine — UEMOA). Furthermore, political leaders lack the will to diminish the areas of national sovereignty over which they preside and regional institutional leadership is rather weak.

It should be acknowledged, however, that there are often sound political reasons behind what appears over–rapid regional expansion, most notably the need for political inclusivity and dialogue in regions which have in the recent past experienced (and in some cases continue to suffer from) conflict and instability. Thus these problems of divergence might (and arguably should) best be addressed by the application of variable geometry membership criteria to encourage the incremental, centrifugal development of similar economic ideologies and trajectories among member states. This approach would by definition take into account the heterogeneous nature of member states. But such strategies require again a strength and sophistication of leadership that has hitherto been lacking.

Conclusion: Making Progress with Regionalism

There are obvious benefits flowing from improved regional co–ordination and co–operation, not least the ending of conflict, the creation of larger and more attractive markets through removal of barriers to trade and investment, increased investment flows, and the development of much–needed infrastructure.

But, as has been noted, there are significant obstacles to this process in Africa, especially the absence of a congruence of democratic and economic values within regions. Indeed, for Africa the major challenge with region integration is simply that, whereas in Europe this process has been the outcome of a shared appreciation of political and economic values and the development of similar national systems, in Africa the regional integration ideal is used as the objective to drive the process. It is, put crudely, arguably a case of putting the cart before the horse.

What is thus needed to make progress in this environment?

- First, there is a need to focus on those issues which can add value to the process of wealth creation which will inevitably and without controversy drive integration. Thus there is a need to identify and focus on those functional issues which impede trade and investment and thus prosperity and stability. Much can be done, for example, to encourage growth in Southern Africa through the development of uniform investment codes and practices; and to improve communication and trade links through improved functioning of border controls.

— Second, related to the above, to find means to link the interests of business, governments and inter–governmental organisations and develop joint approaches. Though progress has been made, politicians almost always allow political considerations primacy and have yet to develop a proper understanding of the business/economic dimension of regional problem solving.

— Third, to find and apply strategies and mechanisms, such as variable geometry, to deal with differences between potential regional partners, but without abandoning integration schemes altogether.

— Fourth, perhaps most importantly, there is a need for a shared appreciation of democratic values without which, put crudely, regional member states cannot talk the same language of tolerance, openness, reform and good governance. The question for all of us today is thus: how can we – in the context of partnerships within and between regions – actively encourage and sometimes intervene to facilitate the spread of such values?

— As a final general comment, all of these are points considered in the Millennium Action Plan whose general outlines were sketched first at Davos in 2000, and more recently in Mali to the leadership of the IMF and World Bank. The details are currently being negotiated between African leaders and it would be premature and presumptuous for an African business leader to say more at this stage than that the plan is ambitious and bold and potentially tremendously exciting. With proper care to detail and taking into account the concerns of business as well as other stakeholders, MAP could well provide a framework for more rapid progress on regional integration initiatives as well as for addressing a number of other continental challenges.

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Poverty, Infrastructure and Coherence

*Hilde F. Johnson**

This intervention will be in five parts. First, something about the context in which infrastructural development has to operate; second, infrastructural problems in Africa; third, infrastructural priorities addressing these problems; fourth, the pitfalls we have to avoid; and, fifth, the preconditions for success.

Poverty reduction is the context in which we have to operate. We have all set ourselves international development goals of halving the number of people in absolute poverty in the world by 2015, and quite a number of these people are in Africa.

Infrastructural development has to be seen in this context and has to be an instrument in reaching this goal. Now, how on earth are we supposed to be able to reach such an ambitious goal? Through four very important instruments.

The first is framework conditions: debt, trade, investment. Twice as much money is used in funding debt servicing than is received in developing countries as development assistance. Similarly, twice as much is lost from income through protectionism than is received in development assistance. Finally, the issue of promotion investment has to be addressed.

The instrument is national policies. The performance of national policies — not only macroeconomically but increasingly pro–poor policies as well: good governance, anti–corruption efforts, investment–friendly environment, etc. — has become recognised as a very important development factor, not least through the World Bank aid assessment report.

Donor performance is the third instrument and has to be improved. Donor performance is devastatingly bad. If you look at how we co–ordinate our business — we, the donor countries — Tanzania has to write a little under 10 000 reports every year with different reporting procedures, different accounting procedures, different

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everything. It is difficult enough for Norwegian ministries to handle 10 000 reports, but for Tanzanian ministries it is almost impossible and is very donor driven. So donor performance has to be improved very substantially.

The fourth factor is the private factor one. On one side private sector development, and on the other civil society, which is a very important watchdog. Politicians, without civil societies looking at them from behind and in front, putting a mirror in front of them, act differently. This is crucial, it goes for any politician anywhere, and it goes for business as well. Civil society is a crucial watchdog and it makes us credible.

Now, infrastructural development has to be linked to all these four factors. Infrastructural development is, for instance, affected by trade barriers. It is definitely affected by national policies, private investment, or lack of it, by donor performance, bad donor performance, and, of course, it is linked to private investment and industrial development. So, if we are to deliver on International Development Goals of reducing poverty in the world, halving it by 2015, we have jointly to deliver on all of these four factors.

So, what then is the role of infrastructure? Infrastructure is both physical, what we usually think of when we talk about infrastructure, meaning transport, road and rail communications, power generation, ITC, water and sanitation and so on; but also intangible. Infrastructure also means education and skills. The World Bank Report of 1992, found through looking at all the different investments in the world that can be done in a poor country, that what gains most economically is giving education to girls, not building a power plant, or a road. Infrastructural development is dependent on skills, on local skills; and the maintenance of physical infrastructures dependent on having a skills base in the population.

Physical infrastructural investment enhances the efficiency of investment in education and health. If there are rural roads to schools, educational development in the area benefits. There is mutual reinforcement.

In addition, the infrastructure in people's heads is harder to destroy by war, which also implies that real efforts have to be made.

Infrastructural Problems — What Do We Face in Africa?

Africa's infrastructure is basically colonial, with a focus on getting one or two primary commodities to the market transported to ports where they can be exported. There is very little domestic and regional development of cross sectoral, cross border, and internal infrastructure. This hampers infrastructural development in Africa.

The continent's infrastructure is poor and expensive. The distances and areas are huge and vast, hampering development, and creating major difficulties with maintenance and rehabilitation. This is a major problem. In addition, Africa's infrastructure lacks private investment and participation. It is almost entirely publicly

owned, and usually with concessional funding, either through soft loans from the World Bank or through donor countries like Norway. This leads to the point that African infrastructural projects are often donor driven, with a bias towards urban areas and the priorities of urban elites. This is a challenge we have to face.

There is need for reforms of infrastructure development in Africa. Reform not only from a trade perspective, from growth point of view, but with a focus on the progress of the poor, the inclusion of the masses in the economy. That means the rural poor who represent 80 per cent of Africa's poor.

The failure of the trickle–down effect has meant that the inclusion of the masses has to be linked to infrastructure.

Infrastructure Priorities

There is a need to prioritise the development of infrastructure that can deliver on poverty reduction, on the IDGs, on the progress of the poor. We know from scientific bases that investment in water and transport delivers most in GDP growth at low income levels — transport and water. We also know that most of the poor are in rural areas. So ensuring agricultural development in production and reprocessing, with the possibility of delivering agricultural products to market is very, very important in a context of poverty reduction. Then providing feeder roads to local district and regional markets is crucial.

There has to be work on domestic markets in infrastructure. Experience shows that development in trade usually starts at home. Those who have developed strong domestic markets are also able to deliver on exports. Domestic markets imply, in a way, breaking these colonial transport corridors, and developing cross–border and cross–country corridors to facilitate internal trade.

In the solution of different infrastructure projects, the ones that deliver most on regional integration should be given priority: cross–border road networks, power generation and so on. Regional organisations such as SADC, ECOWAS, COMESA, had been working to some degree in these areas, but not sufficiently efficiently. At least not from the Norwegian point of view. Norway has supported SADC for many years and would like to see a little more delivery in these areas.

The IMF and the World Bank are working on cross–border projects. Delivery could be somewhat better in this area — as the African Development Bank has pointed out.

The area that should not be forgotten is private investment. Utilisation of private investment in infrastructure development, on the basis of public priorities — and "on the basis of public priorities" is the key phrase — should not be based solely on profit and commercial interest. It should be possible to combine them, but the decisions have to be made on the basis of public priorities in public infrastructure. Otherwise the goals of poverty reduction may become elusive.

The benefit of increasing private investment infrastructure is that it reduces public expense, which is important in a poor country. It also has to be linked to legal, regulatory and institutional frameworks and we know there have been some bodies established, multilateral investments guarantee agencies, partial risk guarantee and so on.

There are thus choices to be made about the areas where private investment is appropriate and those where it is not, and where the government is to be the provider and the deliverer of public services.

Public Policy Change

Policy change is imperative because there is lack of coherence and now none of these efforts will be successful unless there is policy change in developing countries. This means not only trade policies but also the creation of investment–friendly environments.

The Pitfalls

The first risk is donor–driven infrastructural projects. There have been far too many white elephants and they have not yet stopped coming.

A second problem is lack of adaptive technologies. Infrastructural projects have to be adapted to local conditions. They should not be turnkey projects from Japan or France, or wherever, which people don't know how to relate to.

Third, the tying of aid has to end. There are five different technologies in one poor area and they have to get spare parts from five different countries. It becomes a mess, of course, it doesn't succeed. We are fortunately making progress in this area. This is crucial, because tied aid implies 25 to 30 per cent higher costs, according to the World Bank. So we are actually wasting very scarce development assistance funding. We're wasting it. We're pouring it down the drain.

Corruption is a fourth problem. We all know that projects that are tied are more prone to corruption than other projects that are more transparent where there are bidding procedures and so on, but there is a delivery problem both in developing countries and in our economies on the donor's side. We have to address it on both sides; if we don't, we are stealing the money from the poor and it doesn't lead to good infrastructure projects.

Sustainability and maintenance constitutes a fifth challenge. Far too many infrastructure projects have not included proper maintenance programmes. The implication of this is what we see in Tanzania, where the same road becomes the Dutch road, the Danish road, the Finnish road and the Norwegian road. Exactly the

same road and every tenth year it is being built, rebuilt, because there is no maintenance. There is a major problem both on the donor's side with the way this is being done and on the recipient's side through not paying due attention to maintenance.

Finally, there are environmental and social effects. Environmental assessment has to be made and one has to take due care of the social effects of infrastructural programmes. This is very often linked to dams and power generation, but also other infrastructural areas.

With these pitfalls in mind, we can see what kind of pre–conditions for success have to be in place if we are to make infrastructure a crucial tool in poverty reduction and pro–poor growth. The conclusion is that infrastructure development for pro–poor growth needs reform.

We need to take care of donor performance, which is not good enough, and we need a major shift in donor priorities where self–interest in donor countries is not ruling the priorities. There are too many incoherent policies. Now, the OECD could develop criteria to measure donor performance. Not only the performance of our partner countries, but to measure donor performance in the area of poverty reduction. How are we delivering as donors in infrastructure, for instance? Those figures would be very interesting, and it is far from clear that Norway would be at the top.

We also need improved performance and delivery on the partner side, on the part of African countries themselves. They have to address corruption, they have to address how they fail to maintain their projects, they have to address a lot of issues, including the question of investment–friendly environments. So, both parties have to change if we are to succeed and if we are to reform infrastructure development in Africa, not least if they are to benefit the poor and benefit and deliver on the IDGs, which should be our goal.

The Regional Approaches as a Liberating Factor

Hassan Abouyoub

Two factors relating to investment in infrastructure that are often neglected should be underscored. One is the trans–border impact of infrastructure on internal, bilateral and multilateral security, especially for our region and continent. The other is the major effect of trans–border and trans–national infrastructure on the emergence or encouragement of markets of a critical size. Small markets are not of much interest, but their limits are often due to the geographic constraints of being landlocked and particularly a deficit of communications infrastructure.

How can this gap affecting nearly all African countries be overcome? How can this be done when official development assistance is declining, particularly because public opinion in donor countries is questioning the need for governance, which depends on reviving the contribution of rich countries to the financing of growth in developing countries?

A second constraint is due to the linkage of official development assistance. That means that infrastructure having a high local content does not interest many donors, who prefer to finance projects having a high technological content.

Thirdly, we are penalised by poor governance for which we are rather systematically criticised, and also for the difficulties of implementing investment projects, for legal insecurity, complex procedures, and quite simply insufficient infrastructure. Is there any way of escaping from this vicious circle that has continued for 40 years?

The experience of my country and some others shows that projects financed by multilateral institutions have a trans–border or trans–national value. That is true for trans–African roads, which nonetheless have been evaluated by various multilateral and bilateral donors within the scope of single countries, although a regional approach would have surely provided major economies of scale and an alternative mode of financing.

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Privatisation of a number of monopolies could release a wealth of latent savings. That is the case of telecommunications, water and all non–tradable services which remain a state prerogative, because since the 1960s they have been symbols of complete sovereignty. To be able to build on a regional level with integrated regional development zones, however, some economic sovereignty must be given up. Inter–country infrastructure and regional communications are clear illustrations of this renunciation.

A mechanism which is based on privatisations to transfer the revenue of monopolies to qualified enterprises, complemented by multilateral funds that are often difficult to disburse, will allow enterprises that have just invested in Africa to use the capacity for mobilising international private savings. These three sources will permit leverage to maximise the marginal utility of dollars invested in development assistance. Some similar developments are occurring at the level of the European Union.

This alternative way of financing infrastructure based on a system of concessions for services depends on at least three conditions. One is drawing up a series of codes of conduct. The first code of conduct will modify the principle of official development assistance between donors and recipient. Unlinking aid by making it multilateral, if necessary, and combining national and multilateral capacities of mobilisation, will permit a different form of financing infrastructure projects, and probably with increased generosity.

At the regional level, a code of conduct for countries which receive this financing and infrastructure projects would create a confidence–building legal and fiscal framework at the regulatory and good–governance levels, including transparency and encouragement of competition. In other words, a set of rules and regulations to which we will submit so that foreign direct investment will be less risky on the African continent.

The second condition is that we need a relatively sophisticated guarantee mechanism, such as the Multilateral Investment Guarantee Agency (MIGA) or other mechanisms under the Lomé Convention, but adapted to a larger framework for traditional financial operations. For example, the potential offered by the conversion mechanism for the planned and deployed aid can multiply the capacity of recipient states to access the international market for third party multilateral or bilateral guarantees to be defined.

The third condition is that there not only needs to be an *ad hoc* mechanism which can mobilise capital, but also to identify the project beforehand, establish the legal framework, etc., to create synergy between countries within well–defined regions. Is this possible using existing institutions like the African Development Bank? To increase the synergy between the European Development Fund and the capacity for multilateral financing, is it necessary to create a new mechanism for co–ordination, finding the director and negotiating conditionalities, which will permit managing the multinational side of these projects? The question arises because the sectors concerned are telecommunications and water, including the management of water resources and infrastructure of water supply, and their multiple impacts, in particular on the environment.

The road network is also considered a sector of infrastructure, likewise higher education and vocational training. Many constraints faced at the national level of investment in endogenous education and educational institutions, whatever the costs, disappear if at the regional level there is a real division of the capacity for higher education and vocational training. This infrastructure can even take advantage of the great technological advances to permit distance teaching using teleconferences, a sharing of technology. The donor countries can thus join with us in creating alternative methods of transferring knowledge, indispensable for our national or regional resources to assume the management of this infrastructure and investment.

Finally, great visibility and a great correction of the image of Africa are necessary for this type of project. It is necessary to establish a real strategy of institutional communication to correct the prejudices which are among the greatest hindrances to investment.

Enhancing Infrastructure in Africa

*Michael G. Tutty**

EIB Role in Infrastructure

For over 40 years, the European Investment Bank has accumulated wide experience in the financing of infrastructure projects. The European Investment Bank was created in the late 1950s, in order "to contribute to the balanced and steady development of the common market in the interest of the European Community", as is spelled out in the Treaty. In practical terms, this very broad mandate entails providing loans and guarantees to assist the harmonious development of the various European economies by developing the less endowed regions, bridging the gap with the wealthier areas and fostering by the same token regional integration and cohesion.

In the early years of the big European adventure, the European Investment Bank's efforts largely concentrated on the development of the infrastructure sector. The Bank thereby complemented insufficient national resources to finance large domestic projects in transport, energy, telecommunications and water, with a view to making the quality and reliability of utilities in all the member states rise and converge to common standards.

In more recent years, the completion of the internal market resulted in the compelling need to interconnect fully domestic transport and energy networks. This was at the origin of the trans–European networks, the so–called TENs, which are large infrastructure networks interconnecting several member states of the European Union as well as certain Eastern European countries which have applied for membership. Over the last five years, Bank finance for infrastructure projects within the European Union has amounted to some €70 billion, equivalent to 60 per cent of all EIB lending in the European Union.

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Why has the enhancement of infrastructure traditionally represented a priority for the Bank? Because a sound infrastructure basis is a necessary, albeit unfortunately not a sufficient, pre–condition for economic growth and development. Infrastructure contributes to growth acting both through supply and demand. In an aggregate sense, it can be argued that it complements private investment, to the extent that the type and reliability of infrastructure influence the marginal productivity of private capital. At the microeconomic level, an infrastructure providing a high degree of service quality reduces production costs, affecting thereby competitiveness and, as a consequence, profitability, levels of output, income and employment. Adequate infrastructure can contribute furthermore to the economic diversification of the less developed regions. Telecommunications, for instance, provide access to applications of modern technology in many sectors. And transport, particularly in rural or remote areas, facilitates the access to alternative employment and investment or consumption possibilities.

The regional dimension of an infrastructure network can of course only augment this impact. Not only does it make economies of scale possible, but it favours as well the intensification of trade links between the countries concerned.

EIB Operations Outside the EU

Although its operations are concentrated in the European Union, the European Investment Bank has also been given the important remit to contribute to the economic development of the European Union's neighbouring countries and those which are geographically more distant, but with which it has strong historical and cultural ties. In this context, the African continent is of course an obvious area of intervention. And while Bank lending in Africa represents only a small proportion of that in Europe, in absolute terms the EIB's contribution to investment financing remains substantial: over the last five years, operations in Africa totalled almost €5 billion.

The EIB can claim a long–standing presence in Africa, now exceeding 30 years. In *Northern Africa*, its interventions have taken place in the framework of bilateral agreements with each individual country; the same applies to *South Africa*, which has been eligible for Bank finance for the last six years.

In *sub–Saharan Africa*, the Bank has operated first in the framework of the Yaoundé Conventions, subsequently replaced over the last 25 years by four successive Lomé Conventions. And the 4th and last Lomé Convention will be replaced in the coming months by the Cotonou Partnership Agreement, which confers on the Bank a more prominent role not only in Africa, but also in the Caribbean and Pacific countries.

Thus, the European Investment Bank is well placed, both because of its expertise in Europe and its long presence in Africa, to contribute to the development of African infrastructure. What form has this contribution taken and how is it likely to evolve in the future?

Over the last five years, Bank finance for infrastructure projects — both national and regional — throughout the continent has amounted to over €3 000 billion, corresponding to approximately 65 per cent of total operations, both in Northern and sub–Saharan Africa. However, while in Northern Africa lending was distributed evenly between the power, communications and water sectors, in sub–Saharan Africa the energy and water sectors received each roughly 40 per cent of the funds, and communications 20 per cent.

Bank finance for infrastructure projects has followed the market evolution, which in many cases has witnessed a shift in national economic strategies towards a progressive disengagement of the state from the development and management of utilities, in favour of the private sector. While until the late 1980s, developing and operating infrastructure traditionally fell within the realm of public investment, the rote of the private sector has become more prominent in recent years, although the phenomenon is more evident in the management of infrastructure through long–term contracts (such as concessions), than in investment.

At the origin of this evolution are two related causes :

— First, the frequent failure by state enterprises to manage utilities efficiently. And indeed, in its appraisal of public utility projects, the Bank was often confronted by the poor quality of management and the precarious financial health of the enterprises. The latter was in turn the result of lax financial management, an inadequate tariff policy, and of excessive technical and non–technical losses leading to a substantial waste of resources such as water or power.

— Second, the states' inability to mobilise the large funds required for developing infrastructure, in the light of the severe budgetary constraints imposed by macroeconomic adjustment programmes.

Thus, the move towards private sector financing reflects on the one hand the interest to establish modern systems managed efficiently and on the other hand the necessity to develop the infrastructure base without drawing on scarce public financial resources.

Interestingly enough, this evolution appears to be more marked in sub–Saharan Africa than in Northern Africa. If we examine loan statistics, we find that, between 1995 and 2000, Bank financing of private sector infrastructure was close to zero in Northern Africa, but accounted for some 10 per cent of infrastructure investment in sub–Saharan Africa. In this region, the Bank is in fact being increasingly approached for the financing of BOOT (Build, Own, Operate, Transfer) projects. This evolution towards private sector investment is well reflected in the Cotonou Agreement, in which the private sector is considered as one of the instruments required to stimulate growth, where the public sector has failed.

Types of Infrastructure Financed in Africa by EIB

The Bank has two categories of funds :

— Its *own resources*, which are funds raised on capital markets on very favourable conditions made possible by its triple A rating; and

— *Member states' budgetary resources*, which are called risk capital in the Bank's jargon, although this term has a different connotation from that used in commercial banking.

Own resources lending must be backed by solid sovereign or commercial guarantees, which limits their use to countries considered creditworthy and which are willing to extend a guarantee; or to projects supported by the guarantee of a bank or corporate institution of international standing. Behind the utilisation of risk capital, on the other hand, lies the awareness of the importance of risk reduction to stimulate investment. About half of all risk capital loans have been made for public infrastructure operations where the perceived risk, at the aggregate or microeconomic level, was too large for an own resource loan.

As far as the type of instruments available is concerned, own resources are lent as ordinary senior loans, while risk capital has proved to be an extremely flexible financial mechanism. It can be structured in different ways such as direct or indirect equity participation (which as a rule is of limited use in the infrastructure sector), quasi–equity, subordinated or conditional loans. Until now, the successive Lomé Conventions have required that loans from both types of resources in sub–Saharan countries (with the exclusion of South Africa) be lent below market rates. However, the practice over time has increasingly been to provide the subsidised resources to the state, for on–lending on market terms to the enterprise in charge of the infrastructure project. Granting the subsidy to the state has a macroeconomic impact, enabling it to reduce the burden of foreign debt and, by the same token, making it possible to avoid creating market distortions at the level of the enterprise. This practice has gained particular significance in recent years with the implementation of the HIPC initiative to relieve the public debt of the poorest countries.

Under the forthcoming Cotonou Agreement, these same resources and instruments will remain available, although the subsidy element will be very much reduced and will remain applicable to infrastructure projects in least developed countries only.

Some examples of infrastructure projects financed in Africa by the European Investment Bank are presented below, in particular regional projects as the focus here is on regional integration.

In *Western Africa*, an interesting example is provided by the construction on the Manantali dam of a hydroelectric power generating plant owned — as is already the case of the dam — by Mali, Mauritania and Senegal. The project, which includes also the interconnection of these three countries' electricity networks, represents an important step towards the creation of a fully interconnected West African power network.

Two other projects in the same region are worth mentioning. The first one, in the transport sector, concerns the rehabilitation of the rail line between Abidjan and Ouagadougou, intended to increase significantly the transfer by rail of passengers and goods from Burkina Faso to the coast, and in the long term, to enhance trade between these two countries. The second one is the connection of a number of Central and Western African countries, such as Benin, Cameroon, Gabon, Senegal, to the SAT3/ West African submarine optical fibre cable. This is a very ambitious project, for which the Bank intends to maintain its support: in the long term, the cable will link Europe to Western and Southern African countries, to be ultimately connected via Mauritius to the cable serving Asia.

In *Southern and Eastern Africa*, it is important to mention the Tazama oil pipeline, a venture jointly owned by the States of Zambia and Tanzania, linking the port of Dar–es–Salaam with a refinery in Zambia. Another interesting example is the very recent rail and port interconnection between Mozambique and Malawi which is still under appraisal.

However, the European Investment Bank's contribution to the enhancement of regional infrastructure can without any doubt be best illustrated by its participation in the financing of electricity generation in Southern Africa. This region is endowed with substantial resources from which to generate electrical energy — notably an abundance of coal, and major hydroelectric potential (and possibly also, for the future, gas). The Southern African Development Community (SADC) countries have adopted a forward–looking approach to the development of electric power resources in the long term, creating among other things the Southern African Power Pool (SAPP), consisting of a region–wide interconnected power network to the benefit of all users of the system. Thus, in addition to permitting the optimisation of power system planning on a regional rather than national basis, the SAPP allows the region to benefit from the supply of efficient, low–price electricity.

The EIB has invested some €500 million in energy development in this region under the successive Lomé Conventions, to support development of the resources both in the national framework, and with a view to optimising power supply on a regional basis. Thus, the Bank has contributed both to the construction of local power plants, ensuring domestic self–sufficiency and reliability of supply, and to their interconnection. Examples of the types of investment projects supported by the Bank include :

— Coal–fired generating facilities in Botswana and Zimbabwe;

— Hydro–power facilities in Lesotho, Malawi, Zimbabwe, Swaziland;

— The strengthening of national transmission and distribution networks in Malawi, Zimbabwe, South Africa;

— The interconnection of South Africa's transmission network with that of Botswana, Mozambique, Namibia and Zimbabwe;

— The creation of a regional utility company jointly owned by Mozambique's, South Africa's and Swaziland's power companies;

— And, last but not least, feasibility studies into hydro–power facilities (in Lesotho and Zambia), and coal–bed methane gas (in Zimbabwe).

Financing of the Southern African power network by the European Investment Bank has been predominantly in the form of long–term loans, up to 20 years, as is appropriate for this type of infrastructure investment. The Bank has used the full range of resources at its disposal to reflect the characteristics of the different countries, for example:

— Ordinary market–rate loans on its own resources in South Africa;

— Loans on its own resources, but carrying an interest subsidy to support institutional capacity–building in Zimbabwe, Botswana and Swaziland;

— Loans on risk capital (usually passed through government) in Lesotho, Malawi, Zambia and Mozambique.

The last case is an interesting one — the risk capital financing to Mozambique for the rehabilitation of the Cahora Bassa–South Africa transmission line was structured so as to contribute to Mozambique increasing its percentage of equity participation in the Hidroeléctrica de Cahora Bassa company (majority–owned by Portugal from the days of the original construction of the dam).

Besides providing finance, what has been the intrinsic value–added the Bank has contributed to these projects? The combination of EIB's "critical mass" of financing in this sector in the Southern Africa region (and its possibly unique geographical coverage), together with its continuing and substantial activities in providing finance to major corporations in the power sector in the European Union itself, have enabled the Bank :

— To provide useful inputs (and sometimes tough conditionalities) into the questions of institutional set–up, tariff policy and structure, etc;

— To provide a useful sounding board for the power companies in the region as regards optimisation of technical design of facilities and network planning;

— To provide inputs, and European experience, into environmental protection measures;

— To encourage companies to widen their procurement procedures to international competition, with beneficial effect on prices and service for the consumer.

And lastly, there is another type of operation fairly atypical for Africa and co–financed with the African Development Bank. Bank financing for infrastructure has progressively adapted itself over the last ten years to the evolution of market conditions. A particularly interesting development, in this context, has been the participation in a fund, the *Africa Infrastructure Fund*, intended to finance exclusively infrastructure projects throughout the African continent. This private investment fund attempts to maximise capital gains by targeting investment in assets which can be quickly sold on European and North American primary markets.

At first sight, this type of intervention may not look very development–oriented and the question can be legitimately asked whether it is an appropriate financing tool for Africa. The answer is undoubtedly yes. If such a fund is successful, and so far nothing seems to be pointing to the contrary, it is the living proof that it is possible to engage in profitable investment in Africa and this can only represent an encouragement to other private foreign investment, possibly in other economic sectors. It is also interesting to note that, although the African Investment Fund has been established to operate in the whole African continent, the largest share of the portfolio is so far in sub–Saharan Africa, demonstrating that opportunities do exist, even though the risk may be greater.

Concluding Remarks

The European Investment Bank has always given a priority rank to the enhancement of infrastructure, a sound infrastructure basis being considered a fundamental prerequisite to sustained economic growth. Nevertheless, a word of caution is called for. In financing infrastructure projects, the Bank pays considerable attention to the quality of the investment, that is to its technical or technological soundness, its financial viability, its impact on the economy, and last but not least, to environmental considerations which in this sector probably more than in others are of fundamental importance. Indeed, while infrastructure is absolutely essential to further development, its construction requires the mobilisation of very substantial financial resources. Because of this, it is essential to ensure that the investment is fully justified and viable and that the human and financial resources required to maintain and operate it are available.

Unfortunately, all over the world we have too many examples of what in certain languages are called "white elephants", in others "cathedrals in the desert", all pointing to investments motivated by non–economic considerations, and left idle or used at a fraction of their capacity. These investments have contributed to the economic distress in which many developing countries have found themselves over the last 20 years and which a large number of them have not overcome yet. Thus, contributing to raising economic conditions does not only involve relieving debt and taking positive measures in favour of poverty alleviation; it also means ensuring that the scarce resources are allocated efficiently without waste.

Integration and Infrastructure in Africa

Nazir Alli

Introduction

The most tumultuous century in human history has ended and a new century has dawned. During this last century we have witnessed recurrent violence at every level — global, regional and local — as well as the escalating scientific–technological revolution that has changed, and is changing, the lives of all the inhabitants of this planet. The nations that entered this revolution first acquired the capacity to exercise power and influence far beyond their borders. It was not guns, but the knowledge, creativity and wealth that lay behind those guns that represented strength.

Irrespective of political system, economic development is now the top priority of virtually every nation in Africa and a new urgency has been attached to it. Political elites understand that their legitimacy depends upon their capacity to deliver economic benefits to their people at a time when those people can witness the achievements of others. They also know that power — domestic and external — is closely tied to the health of their economy. Thus, in the day–to–day relations between nations, economic issues are paramount.

Africa is the most important development challenge for the 21st century. Our continent faces a formidable task in attempting to reach parity on economic welfare and social inclusion with the leading developing regions of the world. We are faced with a multi–layered crisis demanding that we look at new frameworks and languages to understand and overcome this crisis. We are further faced with the crisis of meeting and ensuring access to the basic needs of our society: health, housing, food, education, transport and jobs. The basic needs concept is a reminder to all of us that our goal is to provide all citizens in all our countries the opportunity for a full life. To achieve this goal, our economic recovery, growth and development are the most important ingredients.

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* CEO South African National Roads Agency Ltd

Further, we must focus our attention on the public square — the common good that underpins our national and global destinies. The vitality of any public square ultimately depends on how much we care about the quality of our lives together. The neglect of our public infrastructure, or in some cases the lack of it — for example, our bridges, tunnels, water and sewerage systems, highways and railways — reflects not only our shortsightedness, but also the low priority we place on our common life. Faced with these realities, how do we expect ever to constitute a vibrant society?

Integration and Economic Recovery for Africa

The trends and importance of globalisation coupled with economic integration are recognised, but what does integration hold for Africa? Regional economic integration has become a feature of the policy frameworks of many countries and is generally driven by market and/or political imperatives. It is primarily an instrument to pursue the expansion of markets and to remove barriers impeding the flow of goods and services between countries in the bloc or region. This will ultimately lead to economic growth and development, so much needed in Africa.

We in South Africa, together with many of our neighbours, are firmly on our way to economic recovery. Our macroeconomic targets and goals are founded on the attainment of sustained and broad–based development which includes:

— To increase the level of economic activity;

— Generate more employment opportunities;

— Reduce the incidence of poverty;

— Governance;

— Improve the delivery and expand the coverage of basic services;

— Protect the integrity of the environment; and

— Promote the sustainable use of natural resources.

Various economic regions and/or trade blocs have emerged in Africa in the last few years. The emergence of these trade blocs and/or customs unions is to seek the broadening of markets. The SADC will introduce its Free Trade Area in 2004. But why trade blocs? The answer can be found in the benefits:

— Trade creation;

— Trade diversion;

— Larger market bloc allowing countries to take advantage of economies of scale;

— Enhanced competitiveness of firms in the microeconomic sphere;

— Foreign direct investment;

— Joint development of economic activity;

— Co-operative strengthening of the relationship between the bloc and the rest of the world.

Integration also serves as an example of how efficiency gains can be created by overcoming the obstacles in the way of economic development as well as the gains arising out of economies of scale. However, this cannot be achieved without basic infrastructure. Basic infrastructure can be seen as an imperative for economic and social growth. For example, during the early 1990s, the SADC countries started integrating their electricity grids. This integration created economies of scale allowing the region to benefit as a whole. This has led to a saving of $1.6 billion to the region. Current efforts concentrate on transport and communication networks within the SADC region to achieve similar results.

The Need for and Provision of Infrastructure

Sound infrastructure forms the foundation for overall development in any country. Further to this, good and well–maintained infrastructure links between countries and economic regions will go a long way in generating international competitiveness, growth and development in Africa and its economic regions. It is for this reason that South Africa has taken the lead in Spatial Development Initiatives (SDIs). This initiative has culminated in the implementation of the much acclaimed Maputo Development Corridor (between Mozambique and South Africa), followed by other countries with projects such as:

— Platinum Development Corridor;

— Beira Development Corridor;

— Benguela Corridor;

— Malanje Corridor;

— Namibian Corridor;

— Tazara Corridor;

— Trans Kalahari Corridor.

The importance of infrastructure is also clear when we look at its effect on our economies. For example, through transport infrastructure, the transport services in South Africa contribute approximately 5.3 per cent of GDP directly to the economy[1]. Transport is also of vital importance as an intermediate input into many other sectors of the economy such as mining, agriculture, tourism and manufacturing. Finally, and even more important, is the potential of transport infrastructure on a regional basis to unlock the economic potential of countries within economic regions.

The trade of products traded globally is becoming more and more time sensitive. This tendency is not only due to shorter product life cycles but also to the use of just-in-time production management techniques. By providing and improving infrastructure we not only improve our competitiveness and production and delivery times, but it also gives us the opportunity to build better structures of governance to enhance the performance of our economies in areas beyond mere trade.

Meeting the challenges of the new millennium is a daunting task. Although the need for infrastructure remains, the nature of provisioning it will continually change. It will remain a moving target. The three driving forces that will intensify and create contradictions within each other, demanding that we face the challenges each of them will bring, are:

— *Politics* — enormous budget pressures for social spending with limited funds available for infrastructure;

— *Public Administration* — the creation of public sector agencies and public-private partnerships; and

— *Technology* — the development of technologies providing significant opportunities for more effective and efficient infrastructure

The challenge facing governments in Africa is a small budget on the one hand and a large demand on the other. Further, it is not uncommon for the emphasis to be placed on addressing social spending needs and social infrastructure deficiencies. This emphasis needs to be very carefully managed as the curve that describes the decay of inadequately maintained infrastructure becomes dangerously steep if relative neglect persists beyond a few years.

The issue of infrastructure financing and pricing has been an important aspect of economic analysis for a long time. Since the 18th century this aspect has been debated and it was found that the funding of infrastructure should be "tax" based. Now that we have entered the 21st century, infrastructure financing and pricing deserve a new and deeper analysis. We can no longer rely on the state to provide the finances through taxation. It seems that owing to the challenges faced by Africa between providing for the social needs of the communities and remaining globally competitive, the political, public administration and technological climate has never been more conducive for the development of infrastructure based on the user–pay principle rather than being dependent on tax based revenues.

Why Do We Need to Enhance Infrastructure?

Enhancing infrastructure does not only depend on the manner in which we finance and price infrastructure. Institutional transformation and the retaining and enhancing of human capital and skills play just as important a role as the physical infrastructure itself. There can also be no doubt that we need to see quantum changes in management approaches to ensure that every cent spent on infrastructure derives some form of benefit within the framework of a long term vision.

We should also remember that a sound balance should be attained between the social and economic interest of providing infrastructure as it is essential that the gap between the poor and economically advantaged sectors of society must be steadily reduced. One should also recognise that the provision of infrastructure is sometimes driven by the need to provide such infrastructure in rural or disadvantaged areas. However, the focus of such provision of infrastructure should be that with the progress of time and the implementation of other economic interventions the infrastructure itself should develop into infrastructure of economic importance.

The increase in infrastructural capital stock should also recognise the potential of infrastructure to influence and/or enhance other objectives than the need for which it was introduced. Institutional interaction and planning also play a large part in the enhancement and success of infrastructure. Fragmentation and the lack of co-operation between institutions and countries will lead to inefficient use of funding, skills and capacity and could lead to infrastructure development that does not address the needs of our continent and economic regions. Planning should be more business orientated and less bureaucratic in nature. Planning should also focus more on infrastructure as a means of achieving goals rather than as an end.

Although this all sounds good, what does it mean to us to enhance infrastructure? Using transport infrastructure as an example, the importance of access to efficient transport services is important not only for the specific country, but also for the economic region and Africa as a whole. Looking at maritime, rail, air and road transport, we can easily divide the importance for well developed and maintained infrastructure into four economic modes:

— Cross–border trade;

— Consumption of services and goods abroad;

— Commercial presence abroad; and

— Presence of people working abroad supplying services, skills and knowledge.

Without sufficient and efficient regional transport infrastructure links, these four categories of economic activity (also relating to competitiveness) would not be possible. Furthermore, through each of the above economic modes, investment in countries would be very difficult if not impossible. Underpinning this is the growing recognition that outward–orientated, open economies perform better than closed, inward–orientated economies.

Looking at the profile of transport infrastructure, it is noteworthy to mention that road transport represents between two and six per cent of a country’s GDP. In the United Kingdom, it is said that a £1 increase in road transportation costs leads to a reduction of £1.66 in GDP[2]. This shows the importance of well established and maintained infrastructure. Furthermore, in South Africa, as is the case world wide, freight transport by road has become the dominant form of transport (80 per cent compared to 20 per cent by rail). This is specifically significant to Africa as many African countries do not have extensive rail networks. As a result of the trend towards

“intra-continental” movements of goods and services, the lack of necessary infrastructure will inhibit Africa from competing in this market. Intra-regional and intercontinental movement of goods and services will play a much larger role in our future competitiveness and economic survival in the 21st century.

We should, however, not forget maritime transport, which represents 80 per cent of bulk cargo by volume of total world trade. This industry has not only become severely competitive but is also highly inter–modal, shipping firms also owning and operating subsidiary firms handling the transport of goods by road, air and rail from the manufacturer to the port of export. Cross border road and rail infrastructure is here of utmost importance, especially to African countries not having access to ports.

Because of the huge amount of competition and struggle for economic survival of international firms, enterprising individuals and organisations have recognised the huge, untapped potential of Africa and are actively pursuing business ventures across the continent.

Africa’s opportunities, although vulnerable to the risks involved in investing in emerging markets, include:

— oil and gas;

— mining;

— public–private partnerships;

— international trade;

— infrastructure;

— burgeoning financial markets; and

— leisure.

The question remains: how to address our challenges while at the same time enhancing and developing our infrastructure?

What We Need to do to Enhance Infrastructure

One of the main areas in which a government can demonstrate its commitment to enhancing infrastructure is in the creation of supportive policy. The formulation of public policy is a major factor in developing the necessary supportive infrastructure, equitable laws and regulations, and ensuring the independence of the judiciary and universal access. Moreover, having recognised the potential of infrastructure to contribute to, among other things, socioeconomic development, governments in Africa have a duty to ensure that policies assist in reducing the gap between the rich and the poor. We should all be aware that our policies not only increase this gap, but also make it nearly impossible to close.

Apart from a policy framework for development, a prerequisite for growth in Africa is the opening of national markets and the formulation of a coherent set of regulations and tariffs to achieve this. Governments should focus on establishing investment–friendly markets with the necessary frameworks for interventions when required. To attract investors to its market, African public sectors must focus on creating the enabling environment by putting in place clearly articulated policy reform programmes including credible, transparent legal and regulatory frameworks, fair and transparent procedures.

But policies on their own do not serve the needs of our continent. The key is the implementation of policies. The objective is to capture the huge interest in the private finance of infrastructure as the demand for high quality, high capacity infrastructure remains strong, and the traditional suppliers — central, provincial and local governments — experience increasing strain on limited financial resources. The use of public-private partnerships also enables governments to obtain maximum leverage and ensure delivery without compromising fiscal integrity. It is interesting to note that this is true both for regions experiencing rapid economic change and for those with mature economies.

Through innovative funding mechanisms and instruments, with the establishment of public–private partnerships, governments could supply infrastructure within the constraints of budgetary restraints. In terms of job provisioning, projects initiated on the public–private partnerships principle have shown potential to stimulate job creation significantly, especially in the secondary labour market. Recent studies by the Stanford Research Institute have shown that of the 620 000 jobs expected to be created in South Africa within seven years, 90 per cent are directly related to tourism, construction and agriculture . These are manifested in all major infrastructure projects underway in our continent.

Transferring the responsibility of providing infrastructure from government to the private sector implies more than just the transfer of ownership of the facilities. It implies the transfer of some or all decision–making authority. This sea change that we are witnessing in the ethical environment dates back to as far as the early 1990s. Privatisation and/or public–private partnerships transfer into the private sector a large number of social responsibilities previously assumed by the state. The decisions on how best to deal with issues of common good, such as providing loss-making services to rural areas, is no longer assigned to the publicly accountable functionary but up to the businessmen who run the company. The self–interest of business is clearly at odds with the need of the individual or even the common good. We should clearly be aware of the ethics involved in these ventures, i.e. the private sector should have the responsibility for the provisioning of the infrastructure while government stays responsible to the citizens of the country.

As shown elsewhere, it is essential to achieve the right combination of policies. While Africa is clearly on the right track, there is still some way to go.

The Way Ahead

There are deemed to be six main areas where African countries need to achieve greater progress in order to speed up our participation, and claim our rightful place, in the global village. The six areas can be summarised as follows:

Maintaining Macroeconomic Stability and Accelerating Structural Reform

Our emphasis must be to maintain economic stability and to reinforce the implementation of structural policies that will make our economies more flexible, encourage diversification, and reduce vulnerability. These include further reforms in the areas of public enterprise activity and the trade regime. Governments must also ensure that public services — such as transportation networks, electricity, water and telecommunications, and including health services and education — are provided in a reliable and cost-efficient fashion.

Ensuring Economic Security

Establishing the right framework for economic activity addresses the second requirement of policy, removing the sense of uncertainty that still plagues economic decision–making. The direction and orientation of future policy must be beyond question. This requires the creation of a strong national capacity for policy formulation, implementation and monitoring. Moreover, the transparency, predictability and impartiality of the regulatory and legal systems must be guaranteed. This goes well beyond the respect of private property rights and the enforcement of commercial contracts. It also involves the elimination of arbitrariness, special privileges and *ad hoc* exemptions, even where these are intended to encourage investment.

Reforming Financial Sectors

It has long been argued that an open controlled liberal system of capital movements is beneficial to the world economy. However, rising capital flows place additional burdens on banking regulation and supervision, and require more flexible financial structures. This is an aspect specifically relevant to globalisation that confronts developing countries with a new challenge, namely to accelerate the development and liberalisation of our financial markets, and to enhance the ability of our financial institutions to respond to the changing international environment. Much remains to be done to reform and strengthen Africa’s financial systems.

Achieving Good Governance

Africa should spare no efforts to tackle governance matters and to enhance accountability in government. This means eliminating wasteful or unproductive uses of public funds, and providing the necessary domestic security. In short, governments must create confidence in their role as a valued and trusted partner in the value chain of the continent’s economies.

A Partnership with Civil Society

Africa will need actively to encourage the participation of civil society in the debate on economic policy, and to seek the broad support of the population. To this end, governments will need to pursue a more active information policy, explaining the objectives of policies and soliciting the input of those whom the policies are intended to benefit.

Conclusion

Closer co-operation and interaction in Africa need to be strengthened so that current initiatives and projects support future economic growth and development. However, no single government activity can contribute more to the economy than the provision of infrastructure. Without it, we will have minimal inter–regional trade and commerce with its concomitant impact on the quality of life of the citizens of Africa.

The successful nations of tomorrow are those that are willing to take informed decisions. These decisions must take into account their own specific realities and goals to enable them to engage the global village on their own terms. Africa has a new opportunity to reposition itself in the world economic equation.

This moment offers Africa a broad framework to elaborate a regional consensus on road transport policies and strategies for the improvement of transport services and for effective regional co–operation in the sector. The liberalisation of the transport market, particularly in expanding opportunities for Foreign Direct Investment in the sector, is likely to have positive effects in terms of transfer of technology, introduction of new products, price reductions and quality improvements. Moreover, inter–sectoral linkages will be large, as a myriad of sectors from other services and manufacturing will gain from these.

For small economies like ours, we have to think hard about the world we live in. Our world, and especially Africa, is becoming more complex where time differences and geographical distance have disappeared, a world where borders between countries are little more than picket fences. However, it is also a troubled world where inequalities and poverty abide between and within nations. At the heart of it all, it finally comes down to how we choose to overcome our own fears, prejudices, sectoral interests and biases. It is about how we extend the limits of our potential whilst replenishing and re–affirming our humanity, our values and our beliefs.

Notes

1. Prof W. Naude, draft report on trade in transport services, August 1999, Potchefstroom University

2. "Barriers to Road Transport", the Hague Consulting Group, Cambridge, January 1998.

Political Underpinning for Regional Integration

*Jean–Pierre Jouyet**

The Second Forum of the OECD Development Centre and the African Development Bank is devoted to regional integration, a demanding and often neglected subject, which is nonetheless gradually becoming one of the major themes of our development policies on the African continent. The three main reasons that explain this commitment by France are as follows:

Regional Integration is an Element of Political Stability in Africa

It is unnecessary to list the African countries now or recently affected by conflicts. The last quarterly report of the World Bank's watchdog group reports that 16 of the 36 countries affected by conflicts are found in Africa. This reality takes on added perspective from the fact that 41 of 78 the world's poorest countries eligible for IDA loans are in Africa.

In this framework, it appears that the process of resolving conflicts and building peace is even more difficult than preventing crises. That is why co–operation among regional bodies such as the Organisation of African Unity, the Economic Community of West African States and the South African Development Community has an important role to play. Actually economic and financial integration is decisive for supporting the needed political stability and making it tangible and sustainable. Europe, which has been engaged in this process for several decades after engaging in two world wars in a century, provides particularly compelling evidence of this

* Head of the Treasury, Chairman of the Paris Club

Regional Integration is a Key Tool for Economic Development

African economies remain small and are generally poorly diversified. They are especially vulnerable to fluctuations in raw material prices; they still have insufficient attraction for investors. Private financing has grown considerably in developing countries in recent years, but it remains highly concentrated (ten countries account for 70 per cent of foreign direct investment).

In this context, economic integration has at least three advantages:

— It allows the creation of a larger, more attractive market, permitting economies of scale, thus increasing the return on large infrastructure projects in the transportation, energy and telecommunications sectors;

— Secondly, it allows competition to increase by making it possible for several economic actors to co–exist in the same market, thus generating services of better quality and lower prices for local consumers;

— Finally, it allows countries and economic actors to reduce their vulnerability by a greater diversification of economies and strengthened financial stability;

Critical size, competition and reduced vulnerability thus seem to be the three main advantages of regional integration. They justify the efforts in this direction undertaken by the international community, and primarily by African countries themselves.

From this standpoint, the franc zone has made real achievements:

— Monetary stability obviously contributes to confidence of economic agents;

— Implementing steps to encourage convergence of economic and budgetary policies of countries in the zone;

— Determining sectoral policies that strengthen economic and financial co–operation between the states.

Regional Integration Promotes Better Understanding of the New Challenges of Development by Pooling Knowledge and Experience

New challenges have arisen such as the fight against AIDS or reducing the “digital divide” between the countries of the North and South. By nature these are global questions, and dealing with them requires co–operation by all actors concerned, public or private. The discussion of international public goods during the last meetings of the World Bank and International Monetary Fund is the beginning of multilateral thinking on these questions. This thinking should be extended to the idea of “regional public goods”.

Here are three examples:

— The Treaties of Rome and Maastricht provide Europe with common rules for building a competitive market economy. Some African countries have done the same by creating the *Organisation pour l'Harmonisation en Afrique du Droit des Affaires,* a regional institution responsible for rationalising the rule of business law in Francophone Africa, and overseeing their application. This pooling of knowledge, measures and arbitration capabilities will promote the emergence of greater legal stability, favouring regional economic development.

— The fight against AIDS is by nature a regional issue, "the virus does not respect borders". Two–thirds of the people infected with the virus live in sub–Saharan Africa, and the incidence in some countries exceeds 20 per cent of the adult population. The states faced with the human as well as the economic consequences of the epidemic — especially when they are insufficiently aware of the stakes of the disease — cannot deal with it efficiently in isolation. The steps undertaken by multilateral development banks through regional programmes or sectoral strategies represent the first stage of approaching this question in a global manner. These efforts should be continued and the stakes also warrant initiating real action for regional integration in the social aspects of health policies

— Finally, it will not be possible to reduce the "digital divide" without efficient telecommunications infrastructure, with a reassuring regulatory environment and greater competition.

These priorities were also reiterated during the last formal meeting of the working group established by the G–8, held in South Africa at the beginning of March 2001.

The exchange of experience is decisive for these various development issues. This "sharing of know–how between developing countries" will be an unquestionable benefit of successful regional integration.

In conclusion, multilateral development banks have an indispensable role to play in this domain, though they cannot substitute for the political will of states. Regional integration is now going to be an integral part of the banks' strategy, for example, as shown by the workshop organised by the World Bank in Bamako, 15–16 March 2001. Although the political aim is now clear, its operational implementation still needs strengthening. The multilateral institutions are still far from having explored all the potential of this new approach to development. This objective is even more fundamental for the regional development banks, whose main justification with respect to the World Bank is their greater proximity and consequently a better understanding of the local institutional stakes. The African Development Bank will undoubtedly be at the centre of this new need for regional integration.

Second International Forum on African Perspectives

PROGRAMME

Second International Forum on African Perspectives

Co–chairs of the Forum: Jorge Braga de Macedo, President, OECD Development Centre
Omar Kabbaj, President, African Development Bank

Experts' Seminar

Monday, 26 March 2001

Session I: Regional Integration in Africa

Chair: Omar Kabbaj, President, African Development Bank

Presentation: Nureldin Hussain, Chief Economist, African Development Bank
Naceur Bourenane, Principal Economist, African Development Bank

Discussant: William Lyakurwa, African Economic Research Consortium (AERC), Kenya

Discussant: Walter Kennes, Principal Administrator, Development Directorate–General, European Commission, Belgium

Session II: Lessons from Regional Integration in Latin America

Chair: Jorge Braga de Macedo, President, OECD Development Centre

Presentation: Andrea Goldstein, Senior Economist, OECD Development Centre
Carlos Quenan, Professor, University of Paris III — IHEAL, France

Discussant: Rolf J. Langhammer, Vice President, Kiel Institute of World Economics, Germany

Discussant: Ademola Oyejide, Professor, University of Ibadan, Nigeria

Session III: Investing in Infrastructure

Chair: Adrian Wood, Chief Economist, Department for International Development, UK

Presentation: W. T. Oshikoya, Division Manager, African Development Bank

Discussant: Claude Ménard, Professor, Université de Paris I, France

Discussant: Shemmy C. Simuyemba, InfraAfrica Consultants, Botswana

Session IV: Financial Market Integration

Chair: Henock Kifle, Director, Strategic Planning and Research Department, African Development Bank, and Director of the African Development Institute

Presentation: Keith Jefferis, Deputy–Governor, Bank of Botswana

Discussant: Ulrich Hiemenz, Director for Co–ordination, OECD Development Centre

Discussant: Jean–Paul Gillet, General Manager of Bourse Régionale des Valeurs Mobilières, Côte d'Ivoire

Concluding Remarks: Omar Kabbaj and Jorge Braga de Macedo

Public Conference

Tuesday, 27 March 2001

Forum Co–chairs: Omar Kabbaj, President, African Development Bank
Jorge Braga de Macedo, President, OECD Development Centre

Inaugural Address: Charles Josselin, Minister responsible for Co–operation and Francophonie, at the Ministry of Foreign Affairs, France

Welcoming Remarks: Jorge Braga de Macedo, President, OECD Development Centre

Keynote Address: Omar Kabbaj, President, African Development Bank

Session I: Regional Integration in Africa

Chair: Omar Kabbaj, President, African Development Bank

Lansana Kouyate, Executive Secretary of the Economic Community of West African States (ECOWAS), Nigeria

Clare Short, Secretary of State for International Development, UK (represented by Adrian Wood, Chief Economist, Department for International Development)

Jakaha M. Kikwete, Minister for Foreign Affairs and International Cooperation, Tanzania

Koos Richelle, Director General, Development Directorate–General, European Commission, Belgium

Michael Spicer, Director, Anglo–American Corporation, South Africa

Session II: Enhancing Infrastructure in Africa

Chair: Jorge Braga de Macedo, President, OECD Development Centre

Hilde F. Johnson, Member of Parliament and former Minister of International Development and Human Rights, Norway

Hassan Abouyoub, Ambassador of the Kingdom of Morocco to France

Michael Tutty, Vice–President, European Investment Bank, Luxembourg

Nazir Alli, Chief Executive Officer, South African National Roads Agency

Jean–Pierre Jouyet, Director of the Treasury, Ministry of Economy, Finance and Industry, France

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Co–Chairs of the Forum	Jorge Braga de Macedo, President, OECD Development Centre
	Omar Kabbaj, President, African Development Bank

Authors, Experts and Discussants — Experts' Seminar

Monday, 26 March 2001

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