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LIBERALISATION OF TRADE AND FACTOR MOBILITY WITHIN AFRICA AND THE PROMOTION OF EMERGENCE OF COMPLEMENTARITIES AS A BASIS FOR THE EXPANSION OF INTRA-AFRICAN TRADE: CASE STUDY FOR EASTERN AND SOUTHERN AFRICAN SUBREGION

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EXECUTIVE SUMMARY

The shift toward a more liberal trade regime has been in response to the deep crises which have faced the international economy during the past two decades. The shocks took heavy toll on economic performance, as a result, growth fundamentals became poor predictors of growth performance. Liberalization as measured in terms of economic openness was therefore one of the instruments used to respond to the crises. Indeed, the free market paradigm and outward-oriented policies became the central pillars in the formulation of international and national policies. In the process, the whole liberalization programme has been assisted by the new information technology which has exposed citizens world-wide to the existence of opportunities everywhere.

For sub-Saharan Africa, the implementation of liberalization schemes turned out to be a Junas-headed god, in that, while it promised to create an environment which is conducive to economic productivity and growth, the scheme has at the same time subjected the African economies to displacement competition from cheap and second-hand imports. The contradictory outcome of liberalization underlines the need to navigate the whole process with great care.

The recent experience in South East Asia has exposed the weaknesses of unfettered trade and free mobility of factors of production. The roots of crisis in East Asian countries were not in governments profligacy, but in the private sector decisions that made the economies vulnerable to a sudden withdrawal of confidence, exacerbated by the misallocation of resources to speculative real estate investment and the risky form of financing, especially borrowing short-term loan from international market, without commensurate strengthening of regulation and supervision. The lesson is that governments must continue to give a sense of direction and to influence private investment, production and employment decisions. Liberalization per se is not the only panacea for economic growth and development.

Empirical evidence on the impact of liberalization on the economies of the countries of

Eastern and Southern subregion suggests that although tariff reductions and elimination of non-tariff barriers have been achieved by most of the countries, on the average, the results of liberalization remain inconclusive and mixed. While some countries have registered modest growth in exports, the majority have not performed well with respect to growth in output and employment.

In terms of mobility of factors of production, some modest achievements have been recorded with respect to capital mobility (investment) but not in labour mobility. The Republic of South Africa has been able to undertake low level types of investments in mining, food processing, breweries, services like telecommunications and retailing (supermarkets). The South Africa predatory type of investments which strive to transform subregional countries into "supermarkets" will not assist the countries to climb upward the ladder of industrial development, but will undermine the liberalization of regional market and penalize the weak. Apart from South Africa, other countries like Mauritius, Zimbabwe, Kenya, Madagascar, Namibia and Seychelles have also undertaken some modest cross-border investments.

In terms of labour mobility, while there has been a long history of movements of persons in the subregion, the more formalized kind of labour mobility has yet to be worked out. Except for the Republic of South Africa which has formalized the movement of skilled farmers to neighbouring countries like Mozambique and Zambia, the current movement within the region involves temporary contract workers which include unskilled, semi-skilled and professional persons. According to estimates, about 8 million clandestine workers, which constitute 20 percent of the whole population work in South Africa. Steps have now been taken within the context of COMESA and SADC to facilitate the movements of factors of production by adopting "visa relaxation" and creating "regional investment" areas.

Unlike in South East Asia where liberalization occurred after firms were already competitive and when the basic economic fundamentals had also been put in place by the various economies, in Sub-Saharan Africa this is not the case. Most countries' macroeconomic conditions act as disincentive to investment. For example, the debt overhang constitutes a

a deterrent as gains from investment could be taxed in order to service external debt, while trade circuit has developed independently from the productive system. The other constraints which affect liberalization include paucity of technical capabilities, lack of information flows. inadequate and inefficient infrastructural physical facilities, an absence of clearly defined and consistent national and regional policies, and an unstable political climate. All these factors have contributed to the frustration in the implementation of the liberalization programme. The result has been the non-exploitation of the enormous potential of the economies of the subregion. De-industrialization has started to settle in as countries abandon production and become transformed into trading outlets or supermarkets. The member Governments have equally begun to vacate key segments of the productive sector, while the private sector capacity to respond to the fresh challenges hardly exists.

It is against this background that the study concludes by proposing five prerequisites around which a more sustainable liberalization policy scheme could be built. These include: the formulation of a regional industrial policy; the building of entrepreneurial and technological capabilities and capacities that would underpin the development of competitiveness and enhance the transfer of technology; the development of efficient and adequate infrastructural facilities that would back up the process of industrialization; and the promotion of effective regional economic cooperation and integration. These are but a few areas where a great deal of attention should be paid. With vision and organization, the African countries could collectively bargain for more practical programmes that take into account their present level of development within the global context. A swift and prompt action is what is required if the countries of the subregion are to reap benefits of the liberalization process.

INTRODUCTION

The shift towards a more liberal trade regimes has been in response to the crisis – inducing globalization of the past decade or two. The poor economic performance of many developing countries which has been characterized by declining productive potential, has shifted attention to productivity gains as sources of economic growth and development. Trade has therefore been considered key to the liberalization process. Indeed, the whole process has been assisted by the new information technology which has exposed citizens world-wide to the existence of opportunities in other countries. However, globalization has its own advantages and disadvantages, which it has been argued (Hass and Litran, 1998) must be navigated with great care, otherwise many countries might be compelled to backtrack their acceptance of the reforms. This would result in the curtailment of free movement of goods, services and capital, and thus slow down growth and technological innovation.

The triumph of the South East Asian open policy which has seen those countries develop at three times the pace of Latin America and six time that of Africa, and the failure of inward-looking trade strategies (Balassa, 1989; Bhagwati, 1978; Krueger, 1978) have fostered the neo-liberal stance on the free market paradigm. Evidence indicates that countries that adopted outward-oriented policies (trade liberalization) have performed well. This had now become the central condition for the World Bank lending in accordance with the "Washington consensus". However, of late, the promise of unfettered trade to create vast wealth has been thrown into doubt as a result of free-market failures in South East Asia, Russia and even Latin America (Brazil).

Two hypotheses have been advanced to explain the current crisis in South East Asia. The first is that there has been large flow of international capital and the second is that the financial liberalization and capital account openning were undertaken without commensurate strengthening of regulation and supervision. While investment has been crucial to economic growth and productivity, other factors such as factor accumulation, both physical and human capital, appropriate policy mix in the form of social inclusion and the transfer of technology have equally played significant roles (World Bank, 1993).

However, the biggest problem has been the misallocation of investment, most notably to speculative real estate and the risky forms of financing, especially borrowing of short-term loan on international market. Investment as a share of GDP jumped to 40 percent in Korea, Malaysia and Thailand during 1993-96. For example Thailand which used to resist bank lending to real estate and directed credit to what it viewed as more growth-enhancing investment, suffered as a result of liberalization. It is unlikely that the crisis could have occurred without liberalization of capital accounts. Evidence suggests that countries with more closed or at least more closed capital account were hardly touched by the contagion from East Asia (Stiglitz, 1998). But the contagion effects have been compounded by home made problems such as poor fiscal policy performance and the failure to address structural weaknesses both in the financial sector and the real economy (Ruttenstorfer, 1998).

It is against this background that liberalization should not be pursued as an end in itself and as the guiding principle of policies, notwithstanding its positive effects on growth, stability, competition and protection of the consumers; but it should be equally understood that markets do not always seem to be sufficiently aware of country-specific circumstances since even countries with essentially sound policies have been affected by the crisis (Ruttenstorfer, op.cit). On the other hand, many African countries have seen their share of world trade cut in half, gross investment rate drop, the share of manufacturing to GDP decline and their countries turning into consuming and trading economies. The African economies in other words lacked the necessary infrastructural capacities to achieve technological transformation that would enable the region to take advantage of the opportunities created as a result of globalization and liberalization.

The agenda of liberalization in the South draws primarily on the orthodox trade – theoretical critique of state directed development policy, as championed by the multilateral financial institutions. The structural adjustment programmes have been effected through market-oriented measures designed to improve the supply side flexibility and performance. The main instruments used in this regard include trade policy reform (dismantling quantitative restrictions, tariffs), openness to capital and technology flows, unhindered flow of domestic investment and labour across sectors (flexibility of free entry and exit), financial reform to permit the market to determine investment and saving, and public sector disinvestment (Rao,

1977). In this scheme of things, the import-substitution industrialization and state interventions are presumed to distort resource allocation and reduce resource utilization (Rao, op.cit). In other words, the old mercantilist argument of using international trade and the protection of local infant industries, from cheap imports in order to promote import-substitution industrialization, which has been the backbone of inward-oriented policy, has been discarded in favour of a more open system and an outward-oriented development strategy.

It is worth pointing out that for almost all countries which are now developed, the manufacturing has been the key sub-sector of the industry instrumental in raising per capita income (Chenery and Syrquin, 1980). However, since much of manufacturing in Africa is uncompetitive on the basis of either price or quality, it is subject to displacement competition from imports. It is for this reason, amongst others, that some have argued that in the context of limited manufacturing capabilities, extensive trade liberalization raises the possibility of significant de-industrialization within the economies (Lall, 1992, 1995; de Valk. 1995; and Carmody, 1997). It is therefore of no coincidence that the economic performance of much of sub-Saharan Africa has remained disappointing. These mixed results raise the key question about the best strategy which Africa should follow?

While the trend since the end of the 1980's has been to support countries that have opened their markets to capital and foreign investment, and have experienced the fastest growth, the most stunning development is that the transfer of nearly one trillion dollars into the developing economies in the 1990s (Sutherland, 1998) saw sub-Saharan Africa attract just $5 billion between 1990 and 1996. Why has SSA failed to attract such capital and investment and what are the factors which have prevented the SSA countries from reaping the benefits of the liberalization process?

Indeed, while liberalization have many refrains, the refrain which appears to hold much promise, is the expected improvement technical efficiency it is supposed to generate once protective trade barriers are lifted (Rodrik, 1998). The general argument is that liberalization would lead to the improvement of resource allocation in line with social marginal costs and benefits; provide access to better technologies; enable the economy to take

advantage of economies of scale and scope; facilitate greater domestic competitiveness and growth externalities (like the transfer of know how); and create an environment which is conducive to overall economic growth (Dornbusch, 1992).

It is equally argued that for liberalization scheme to work, it has to be supported by free movement of capital (investments) and labour – conditions which could perhaps be better achieved within the context of regional economic arrangements. It is against this background that developing countries have to liberalize their trade regimes, irrespective of their level of development and industrial base (Shafaeddin, 1995). It is therefore, important to explore how liberalization in the context of regional integration is expected to enhance the expansion of intra-regional trade, factor mobility and the exploitation of complementarities.

Since early 1980s economic policy reforms at African level have addressed some of the issues mentioned above. The global trends have introduced changes in the conduct of business. The key trends which have induced great impact include: the growth of regionalism and trade liberalization; the completion of the Uruguay Round of multilateral trade negotiations; and the establishment of the World Trade Organization (WTO), whose global liberalization agenda will have far reaching effect on regional integration and preferential tariff agreements bargained among member States of a particular grouping. It should however be noted that regional and multilateral integration initiatives are complements rather than alternative in the pursuit of more liberal and open trade. In fact WTO complements the liberalization achieved at regional level, while the converse is true in the former case. (WTO, 1995).

The purpose of this study is to explore how liberalization of trade and factor mobility in terms of capital and labour can be better achieved within the context of Eastern and Southern African (ESA) subregion. The second aspect of the study is to investigate whether the liberalization of such factors could be used as basis for promoting complementarities for the expansion of intra-ESA trade. Lastly, is to determine which policy options need to be put in place to facilitate the expansion of intra-ESA trade or to improve the adverse effects of the liberalization process.

In order to review some of these issues, the study is organized into six sections. Section I is the introduction to the study. Section II reviews conceptual framework of the liberalization schemes and examines the three concepts involved, namely trade liberalization, factor mobility in terms of labour and capital. The Section attempts to explore the linkages and mechanisms through which regional integration is expected to bring these about. Section III examines the methodological difficulties of assessing the impact of liberalization. The Section also attempts to evaluate the performance of liberalization scheme. The review of empirical evidence in terms of the performance of trade liberalization, and factor mobility is undertaken in Section IV. Section V attempts to explore the movement of factors of production within the subregion. Section VI explores to what extent the concept of complementarities can be used in the expansion of intra-regional trade in Eastern and Southern African subregion, and suggests the basic prerequisites for policy options.

II. CONCEPTUAL FRAMEWORK

Liberalization which involves greater reliance on market for channelling investment and other resources into tradable sector (Shafeaddin 1995) has taken a number of forms and has constituted the core of a more comprehensive set of structural adjustment measures. It is measured by economic openness. It stems from four overlapping sources: anti-statism, poor economic performance, information and the World Bank pressure. However, liberalization is based on five basic assumptions (Rao, 1997) namely; that:

(i) a politically unconstrained market regime is feasible (distributional problems can be resolved without 'distorting the market');

(ii) the market can fully coordinate individual decisions (the state can only get in the way);

(iii) public investment is an inefficient substitute for private investment in growth process (complementarities are negligible);

(iv) the unhindered impact of technology can provide an adequate basis for developing competitiveness (a level playing field imposes no handicap in building up dynamic competitive advantage); and

(v) the free movement of finance, enterprises and labour across the national border will produce internal and external balance (globalization is good for the South

The main instruments for achieving these measures include trade policy reform aimed at dismantling tariff and non-tariff trade restrictions and ensuring currency convertibility; openness to capital and technology flows; unrestricted flow of domestic investment and labour across sectors and national borders; financial reform to permit market to determine investment and saving; and public sector disinvestment. State intervention is seen as distorting resource allocation and reducing resource utilization. Liberalization seeks to reallocate resources from home goods to trade goods, that is, from import-competing to export goods, and from public to the private sector. The real thrust of the argument is that improved resource efficiency is to be secured from the exposure of enterprises to both internal and external competition through a drastic reduction of government intervention in enterprises and markets.

But despite "getting the prices right", there is still a considerable confusion as to exactly what liberalization means and how it should be carried out. One common interpretation of liberalization sets the norm as a regime of totally free trade with no import or export duties and no import licensing or foreign exchange controls, and an exchange rate set purely by the market. While this may be useful as a theoretical construct, as a guide to African policymakers it is not too helpful. Indeed, to proceed with liberalization in the absence of any sense of direction or purpose is likely to prove perverse, dangerous, unrealistic and costly in political terms. The role of governments in influencing private investments, production and employment decisions should be given prominence. The current experience in Eastern and Southern Africa indicates that governments are abdicating their responsibilities and unable to cope with the immediate impact of liberalization process.

The conceptual framework of trade liberalization and factor mobility is linked to the theoretical arguments which underpin the formation of regional economic integration groupings, especially those among the developing countries, whose markets are so small as to permit the full exploitation of resources. Dornbusch (1989) argues that intra-regional liberalization behind high external barriers offers little risk of trade diversion and substantial potential gains. These gains include those derived from industrial complementarity, economies of scale, rents associated with preferential market arrangement, greater product variety, and competition-induced improvements in efficiency.

Intra-regional liberalization behind (temporary) high external tariff barriers is often proposed as providing a "training ground" for firms to gain experience and reap economies of scale, before being exposed to import competition or are ready to move towards the export markets outside the region. Furthermore, intra-regional liberalization is easy to "sell" domestically in view of the reciprocal nature of regional trade concessions. Other authors have argued against promoting preferential trade arrangements among developing countries (Inotai, 1992) since they are made up of many developing countries with small market, low capita incomes and similar factor endowment leading to similar productive structures. The similarity of economies in this respect does not allow for trade expansion based on intra-industry specialization and product differentiation.

Some authors (Greenaway and Milner, 1990) have argued that the question of similarities among developing countries should not be blown out of proportion. Some grouping which display differences in per capita incomes (typically within relatively low levels) and in productive structures among members, suggest the existence of complementarities and the potential for intra-regional trade expansion based on inter-industry specialization. Even in sub-Saharan Africa where per capita incomes and market sizes are smallest among the developing countries, the World Bank (1989) estimates that some $4-5 billion of the region's imports from the rest of the world could potentially be met by supplies from other sub-Saharan African countries already exporting similar products to the rest of the world.

If sub-Saharan Africa could exploit this potential, its share of intra-regional trade could treble to 8%. Regardless of the arguments against regional trading arrangements among developing countries (Mansoor and Inotai, 1991; Langhammer, 1991; de Melo et al, 1992), the experience suggests that the potential gains to be derived from such arrangements can be maximized in accordance with the provision in Article XXIV of GATT which advocates maintenance of an outward orientation; and the provision for across-the-board intra-regional liberalization. These conditions could be better achieved within the context of free trade areas as advocated by the COMESA Secretariat (COM/TC/CT/111/2, 1998).

In sub-Saharan Africa, the process of liberalization of factors of production and trade are faced with more fundamental problems than the issues of reduction and elimination of tariffs and non-tariff barriers, elimination of obstacles; restrictions and constraints to the free movement of labour; elimination of obstacles to the free mobility of capital (investments); and elimination of other restrictions that would undermine the overall effectiveness of the impact of trade and liberalization programmes.

Indeed, the issue of debt burden and the capacity to service external debt now poses greater threat to development and the promotion of investments which underpin liberalization as indicated by the five indicators, debt/export ratio, debt/GNP ratio, debt/service/export ratio, interest/exports, and interest/GNP (Ajayi, 1998). The high debt/export ratio is of great concern due to its negative effects on investment and saving. It is observed that in Sub-Saharan Africa there are two channels through which these negative effects work. First is that, the resources used to service debt, would crowd out public investment and discourage private investment as a result of complementarity between public and private investment. Second, the high ratio of debt/export discourages incentive to initiate programmes that would lead to future growth. While the use of this ratio has been contested (Krugman, 1988), it is however clear that a high debt/export ratio implies that funds are to be transferred abroad in the future, thus raising the implicit cost of domestic capital (Ajayi, op.cit). For example, debt crisis left Latin America without access to market-based foreign finance, while official finance did not come in fully to close the gap (Bruno, 1996). Evidence suggests that there are adverse effects of debt overhang on investment and growth in Africa, since it deters public

investments in both physical and infrastructure as well as on growth-enhancing current spending on health and education (UNCTAD, 1998).

More critically, lack of local entreprenuership and adequate transport and communications facilities including energy and water do undermine the potential to exploit the advantages of liberalization. The ability to be competitive, requires not only high caliber of people with entrepreneurial skills, who will be able acquire the latest technologies and produce quality products that would be competitive at global level; but the availability of cheap and efficient physical infrastructures are also essential. The need to address these shortcomings has heightened the need for governments not to disengage, but to be actively involved in building up these capabilities, capacities and facilities.

2.1 Trade Liberalization

Recently, the regional integration agreements that have been concluded by the developing countries have been linked to the adoption of outward-oriented trade policies, and less concerned with preferential treatment, suggesting that the objectives of regional and multilateral liberalization initiative increasingly coincide. Mansoor and Inotai (1991) argue that the failure of many regional integration schemes in SSA in the 1970s (as measured by their failure to stimulate intra-union trade) was due to the fact that such schemes pursued an import-substitution strategy, which they argue, was inefficient. They therefore view regional integration in the 1990s as a strategy for enhancing export promotion.

It has however been asserted that regional integration could still enhance the success of the union as a whole either in terms of import-substitution or export promotion strategy relative to the equivalent policy pursued unilaterally by each individual member State (Lyakurwa et.al., 1995). This is because, regional integration would result in greater exploitation of economies of scale so long as the countries accept the principle of a geographical concentration of production in particular localities (Krugman, 1991). The effectiveness is likely to be enhanced as a result mobility of factors of production (labour and capital) between countries.

The argument in support of export promotion strategy relates to the fact that however large the size of regional integration scheme is in SSA, the effective size of internal market will always remain small, given the very low level of income in terms of the purchasing power. This implies that, in sectors in which the economies of scale are sufficiently large there will be potentially less possibility for exploiting them in the context of inward-oriented strategy relative to the outward-oriented strategy. The second and the more compelling argument is that, given the limited effective size of the domestic market, internal competition in many industries is likely to be small.

The problem of the limited effective internal market can only be corrected by the adoption of an outward-oriented policy which is likely to give rise to the attainment of higher levels of efficiency through the promotion of international competition. The only condition under which trade will reduce differences in factor prices within an integration grouping, <u>ceteris paribus</u>, is under conditions of production where there are no great dissimilarities among the participating members, because trade liberalization is likely to lead to greater efficiency in production (Balassa, 1961).

The mainstream of economic literature on trade and development suggests that trade liberalization that produces a neutral or outward-oriented trade regime confers certain productivity – enhancing and growth – promoting features in a liberalized economy (Oyejide, 1997). The most important among these are: improvement in efficiencies; increase in competition and product specialization; enhanced capacity of the economy to attract foreign investment, and the creation of a favourable environment for technology transfer (Balassa et al 1975; Rodrik, 1988). The arguments point out that an export promotion strategy, especially in products not previously sold abroad, particularly the manufactured exports (Musonda, 1995) would play a significant role and be enhanced through regional integration. Furthermore, within an open or outward-oriented trade regime, technology can be transferred through direct foreign investment, importation of capital goods that embody current technology, and increased competition which would induce the exporting firms to operate at, or close to the frontiers of technological development. Taking dynamic factors into account, the case for regional integration become much stronger, particularly in the context of export

promotion strategy if the participating countries are prepared to accept the unequal distributional consequences for some members of the scheme.

2.2 Factor Mobility (Capital and labour)

Theoretically the two outcomes of factor mobility normally advanced as resulting from economic integration are:

(i) the improvement of efficiency of resource use by removing scarcities; and

(ii) the equalization of factor pricing.

The arguments in support of the two results are based on the assumption that in any given trade areas, the labour and capital movement will proceed from "depressed" areas to "rich" areas or regions. Further assumption is that, the free flow of factors of production carries with it a number of benefits, the main ones of which include: the maximization of global output and the promotion of efficiency in both labour supplying and receiving countries. The labour receiving countries derive benefit in the form of business managers or technical experts who are likely to provide solutions to certain production bottlenecks and thus open up productivity of enterprises managed by foreign labour, and by possibly imparting technical skills to the local people in the art of managing business. The labour exporting countries are on the other hand likely to receive foreign resources in the form of workers' remittances.

The free movement of factors of production (capital and labour) within the various regional groupings in SSA have been strongly supported on several grounds. Firstly, the free mobility of these factors is an effective way of boosting economic growth by allowing scarce factors to be employed where they are likely to realize the highest returns (Mansoor et al, 1989). Secondly, the free intra-regional factor movement is also an effective method of attenuating inter-country imbalances and minimizing the need for creating compensatory measures, since factors of production (labour) could migrate from the less developed to the more prosperous countries and then remit their earnings to their country of origin. Lastly is

that, it is more fruitful to promote factor mobility among partner countries rather than rely on preferential or free trade arrangement (de Melo et al, 1992).

From the economic literature on factor mobility, the theory suggests that free factor mobility when the trade in goods remain restricted or is carried out in the presence of trade-policy distortion, there will be no automatic improvement in the welfare of the whole group, as one of the partners is likely to be worse off after the migration. In general, Wooton (1980) points out that the analysis of the welfare implication of factor mobility in the presence of restricted movement of goods, such as in a common market, is an analysis of a second best situation, on which no general a priori conclusion may be drawn. The outcome will depend on how trade in goods and trade in factor services interact.

For a small union, free factor movement improves welfare if it causes the production within the union to move towards free trade level, that is, higher output of exports and lower output of import substitute goods. Neary (1987) has confirmed that capital mobility increases the welfare cost of tariffs. Johnson (1967) on the hand, shows that for a small country in which there is tariff-distortion and capital-intensive goods, the importation of capital may be immiserizing. The reason is that "increased capital reallocates production towards the industry using that factor intensively, and if that industry is protected, it will waste resources through excess production costs, the shifts … involves increased waste of resources, which may absorb more than the increased potential output per head" (Mansoor et al, 1989).

In SSA where differences in standards of living are enormous, and unemployment rampant, a completely free and unrestricted labour mobility appears to be a remote possibility. Besides the existence of several inefficient, underutilized foreign owned production enterprises in SSA that would survive free market competition, demonstrate that immiserizing capital may be more than an academic curiosity (Foroutan, 1992). It is for this reason that although it has been shown that increased factor mobility in terms of labour many benefit the regional integration scheme as a whole, or the individual members, intra-union redistribution would be necessary for all to gain (Wooton, 1988).

It should however be noted that the issue of labour mobility is more complex because it involves the movement of human beings, which in turn, has socio-political implication. It is for this reason that even the staunchest supporters of free trade and factor mobility often end in advocating protectionism when it comes to immigration. That is why, in the context of North American Free Trade Area (NAFTA) and EC economic integration, the major policy issue on capital and labour mobility is not only how to enhance it, but also on how to use regional integration as a mechanism for slowing down the inflow of labour from potential partners.

III. METHODOLOGY: DIFFICULTIES IN ASSESSING IMPACT OF LIBERALIZATION

3.1 The Methodological Difficulties

The methodological problems in this study are examined from two perspectives. The first perspective deals with the models used in examining past studies. Most of the previous literature on the subject have not undertaken empirical studies with respect to developing countries. However, the aspect which will be of interest to this study are those which relate to timing, sequencing and how the implementation of these programmes have responded in real situation. The second perspective deals with the question of the availability of credible statistical data on which the analysis of the issues considered in this study could be based.

3.1.1 Review of Past Models: Evidence

In embarking on a programme of trade liberalization, governments face issues relating to the timing and sequencing of the reforms (Falvey and Kim, 1992). The difficulty to be faced has to do with which programme should be implemented first. Should the programme start with trade liberalization or macroeconomic stabilization? The second is to address the question of the speed of liberalization. What would the most appropriate pace on which to proceed? Arguments which have been advanced in favour sequencing are based on four points. First is that, if trade and stabilization packages are initiated simultaneously, the

contractionary aspects of the stabilisation programme tend to be linked with trade reform, as such, the public also tend to associate trade reform with unemployment and deflation which accompany the programme. For trade liberalization to be sustainable it may be prudent to leave protection in place until the macro economic crisis is over.

The second argument is that in order to diffuse political opposition to the programme of trade reform, the two reforms should be undertaken sequentially rather than simultaneously. It is observed that trade reform may be more credible if macroeconomy is stable. The third reason is that any adjustment costs imposed on the economy by any policy package are likely to be related to the speed and extent to which the changes are in relation to prices that confront the economic agents. The costs of combined package are likely to be higher than the sum of those associated with sequential implementation. Lastly, some aspects of stabilization package are likely to promote trade reform. In other words, by reducing the excess expenditure over income and therefore the real exchange rate, the stabilisation policy itself goes to some extent towards reversing the anti-export bias.

On the other side of the arguments, evidence suggests that the adjustment costs associated with trade reform are much smaller in magnitude as to affect the initiation of the two programmes simulateneously. Indeed, the fear of building up another political support for the reform, once the economy has gone through a difficult stabilization period is very real. A much more convincing argument put forward (Michaely et al, 1991) is that there is no particular need to stabilize prior to liberalization as long as the policies accompanying liberalization are appropriate to the macroeconomic situation.

The optimal sequencing as to which order the policies or market should be liberalized is one of an empirical issue. Yet experience yields very few lessons for developing countries in this area, with respect to <u>capital and current accounts</u>. The general view based on theory rather than experience is that, liberalization of capital account should be held back until the process of tariff reform is well underway (Falvey and Kim, op.cit). With regards <u>to quantitative restrictions (QRs) and tariffs</u>, the general assumption in the literature is that the initial stages of trade reforms should be accompanied by the removal of QRs on imports and their replacement by tariffs. The argument is that QRs create uncertainty, result in

maintenance of domestic monopolies, and promote rent seeking and corruption in the allocation of the right to import. On export incentives, trade liberalization should promote movement of resources into exportable industries, and that, export promotion should precede tariff reform. On foreign investment, liberalization of capital account is raised by the possibility of inflows or outflows of foreign direct investment. The resource flows that accompany such investment should really assist with the adjustment process.

Lastly, the issue of speed of liberalization involve three major considerations in terms of government revenue, adjustment cost, and the credibility of the whole process. The trade liberalization which involves deep cut in both import and export taxes can be expected to have a negative impact on government revenue. There is however, no empirical evidence to indicate whether trade liberalization will lead to fiscal enhancement or depletion. On adjustment costs, it is generally accepted that any change in policy is likely to generate adjustment costs, both in terms of output forgone while factors are idle, or in resources actually absorbed in this movement. The costs will depend on the extent of inter-industry versus intra-industry adjustment. Lack of credibility creates social cost. Empirical evidence from Kenya indicates that as a result of lack of credibility during the trade reforms between 1976-1992, the 1980 import liberalization was the most costly. It is estimated to have incurred a welfare cost equivalent to almost 1% of annual GDP and almost two and half times the total manufacturing investment of nearly 10% of GDP that year (Reinikka, 1996).

The methodology and models used in the analysis are still surrounded in ambiguities, partly because of the difficulty in discerning empirical trends which still suffer from scarcity of clear cases of trade liberalization. Secondly, the beneficial consequences of reforms are not in evidence. Yet in all likelihood, the success of reform will depend less on the direct consequences of the new trade policies than on the resolution of the macroeconomic difficulties in which these countries presently find themselves. These factors and lack of empirical evidence to prove otherwise make the evaluation of the impact of these reforms much more difficult.

3.1.2 Problems of Data Collection:

While a questionnaire had been prepared for the propose of collecting data, a field mission was also undertaken to the Common Market for Eastern and Southern Africa (COMESA), Southern Africa Development Community (SADC) and to countries namely, Kenya and Zambia. A structured interview was conducted with the various officials of the Governments and of the regional economic groupings in order to obtain additional information. There was difficulty in the collection of data with respect to labour and capital mobility as no systematic stock of data had been compiled by the two secretariats on these factors of production. The explanations given by the two secretariats for the unavailability of data on labour mobility was that the original legal instruments establishing the two regional schemes did not include factor mobility as their objectives. These omission has been subsequently corrected by the legal agreements upgrading the two communities into the common market and community. The available data on labour mobility is the one compiled by the Republic of South Africa, (RSA), especially those relating to mine workers from Botswana, Lesotho, Swaziland and other neighbouring countries. Besides, the published data on international immigration in the form of census by most countries in the subregion are in a form that is not immediately usable.

The same problem was experienced with respect to the collection of data on cross-border investments (CBI) within the subregion. The interviews conducted with the two secretariats and the appropriate ministries or institutions at the country levels, equally yielded negative results. Since CBIs are of recent development, no data had been compiled on them. Perhaps a more correct interpretation may be a reluctance on the part of the concerned government institutions to provide the required data. The COMESA Secretariat on the other hand provided data on intra-CBI trade for the 14 countries. No such data was however, available at the SADC Secretariat as such data are collected by the country which coordinates the investment programme for SADC. The SADC secretariat is only now in the process of putting its statistical department in place. The unavailability of data has therefore rendered it difficult to establish the extent to which the formation of these groupings have influenced the free movement of capital and labour. The study has however used the available data to give broad indications on the movement of these factors of production within the subregion.

The problem of data availability in Africa is a general one, in that the available statistics from different sources for evaluating the different characteristics of SSA countries' economies have major limitations. Although the most detailed source of internationally comparable data on trade are based on COMTRADE data base maintained by the United Nations Statistical Office (UNSO) there are still major shortcomings as the record is based on the very erratic and uneven reporting practices of many SSA countries. The reported data to the UNSO do not necessarily cover the same periods or years and are normally done in aggregates. In order to overcome this problem there is an urgent need for SSA countries to improve the quality, reliability and availability of their statistical data and ensure their regular reporting. This is the only way in which accurate and credible data can be obtained for carrying out useful analysis.

At present, there is no systematic collection or collating of data at national level. Greater reliance on statistical data from the World Bank sources now appears to be the norm. Yet most of these are at best crude estimates. Without proper data, not much will be achieved in giving proper diagnosis of the African socio-economic problems or in formulating proper policy guidelines. It should also be stressed that the institutions within Africa should make it their duty to be the first source of statistical data and information on African countries.

3.1.3 Evaluation of Performance:

Evidence suggests (Pack, 1986) that results from the studies are inconclusive about the hypothesis that countries with external orientation benefit from greater growth as a result of technical efficiency in the component sector of manufacturing. Bhagwati (1988) has equally asserted that there is lack of empirical evidence or theoretical support in favour of export promotion over import-substitution on grounds of scale economies, technical efficiency or innovation. The models (partial equilibrium models) used to analyse the technological catch up go against the arguments put forth by proponents of trade liberalization. The models cast doubt over the productivity-enhancing effects of trade liberalization. Basically, the argument

put forward is the case for selective protection of industries where the catching up potential is largest, and where there exists positive spillover to the rest of the economy (Westphal, 1982).

Some of the models show that trade liberalization will reduce the incentive to increase productivity (under oligopoly situation) as long as domestic output is reduced. Apart from the constraints imposed by the structural adjustment programmes, the formalization of new liberal international trade and capital regimes under World Trade Organization (WTO) make late industrialization much more difficult, in that, less can be made of tariffs to protect local infant industries, while export subsidies which were an essential elements in the East Asian development are prohibited. Trade related investment measures equally make it difficult to impose conditions on multinational investment or favour the development of local capital and the enforcement of intellectual copyright end to undermine the local technological development (Raghavan, 1990).

Furthermore, since liberalization reduces the excess profit available in the home market, it is therefore expected to de-emphasize the strategic motives for under-investment in technology. There is no convincing empirical evidence for developing countries which shows that liberalization is conducive to industrial rationalisation. In SADC, the implication of the rationalisation process in the context of the current situation and operation of the South African economy is that many industrial sectors will experience a deterioration of their trade position within the next few years, while very few will experience improvement (O'Brien, 1997).

What has liberalization achieved? It has been argued that export-oriented development would lead to faster growth of GDP (Balassa, 1982), by removing the traditional bias against export and production of manufactures. The argument is that trade liberalization would lead to the diversification of production and exports in favour of manufactured products. What has therefore been the experience of Eastern and Southern African countries with respect to the liberalization of trade, labour movement and capital?

IV. REVIEW OF EMPIRICAL EVIDENCE: PERFORMANCE OF TRADE LIBERALIZATION AND FACTOR MOBILITY

4.1 The General Macro-economic Picture

A strong correlation is said to exist between the adoption of adjustment programmes and the falling levels of investment (Killick, 1995). This is related not only to the disincentive effect of macro-economic stability, devaluation, cut back in public sector capital expenditure and high interest which were: 34% for Kenya, 45% for Malawi, 54% for Zambia and 34% for Zimbabwe; but also to trade liberalization as financial resources were now diverted towards the importation of competing luxury goods. For example, when Uganda implemented its adjustment programme in the mid-1980s, nearly half the foreign exchange it auctioned on the weekly market went towards the import of luxuries or for the imports for which there was idle local production capacity (Mamdani, 1991). This resulted in the independent development of the trade circuit from the productive system (Carmody, 1998).

In Zimbabwe, empirical evidence suggests that the economy has not responded favourably to the quick liberalization programme. The result experienced has been in terms of contraction in output and employment, the inflow of imports and rising trade deficit, and consumption boom (Ratts and Torvik, 1998). The structural changes that occurred as a result of liberalization is: de-industrialization which is reflected by a fall in the manufacturing output by more than 20% in 1994 from its 1991 peak. The inflation had reached a peak close to an annual rate of 50%. The structural trend is that Zimbabwe was increasingly becoming a more raw material oriented economy, with the expansion in the exports of agricultural products, horticulture and mining.

In Kenya the employment figures for the manufacturing sector showed a marginal rise from 141,300 in 1980 to 193,600 in 1993. For Zambia the employment figures had declined from 71,300 in 1980 to 67,200 in 1993. This decline was the result of company closures and massive retrenchments. This same trend also applied to Zimbabwe whose employment had declined from 197,100 in 1990 to 185,200 in 1993.

In Zambia, Tanzania and Kenya the textile industries have collapsed as a result of stiff competition faced from the importation of cheap second-hand clothes. Given the limited manufacturing capabilities, extensive liberalization raises the possibilities of significant de-industrialization (Lall, 1992; 1995; Carmody, 1997). The Regional Trade Model for Southern Africa (RTMSA) (Holmes and Evans, 1997) has confirmed that de-industrialization was taking place within Africa as countries resort to trade where returns are higher in short-term than engage in manufacturing where returns are low and long-term.

Despite the World Bank's (1989) vision for Africa of "industrialization by invitation" foreign investment is increasingly concentrated in the developed world and South East Asia (Oman, 1994). In SSA, foreign investments in general and in the manufacturing sector in particular, are scarce due to shrinking market, poor infrastructure, far distances from major markets, low labour productivity, political and macroeconomic instability, and soft currencies all which add to reduce returns to foreign investors if they sell on the local market (Bernell, 1990; Helleiner, 1992).

Indeed, the poor infrastructural facilities in terms of roads, railways, ports, telecommunications, electric power generating and distribution facilities, and water supply facilities constitute serious bottlenecks to the process of economic integration and trade liberalization. It is well accepted that transport, communications, energy and water remain critical inputs in the production of most goods and services. The lowering of the overall cost of these facilities would lead to the promotion of international competitiveness and economic integration by stimulating the exploitation of comparative advantage, the realization of scale economies, and the advantage of geographic location.

By any standards, Africa's infrastructural facilities remain poor in comparison with those of the other regions. In spite of the efforts being undertaken at COMESA, SADC and national levels to improve these facilities, the poor deferral maintenance record in the region increases the rate and severity of deterioration under normal use and multiplies the cost of repairs. This has made it difficult for SSA countries to be able to improve interregional and intraregional trade and to the liberalization of markets. The improvement and the guaranteeing of adequate services in these facilities is one of the basic prerequisites for

industrialization and economic development. African governments will have to bridge the huge gulf between the current level of spending for infrastructural development and the levels needed to maintain and manage a system that can give support to economic growth.

The macroeconomic stability in East Asian region helped exports by easing liberalization of restraints on trade and by facilitating realistic and, in some cases, undervalued exchange rates. Trade liberalization had been part of a policy package that included devaluation, exchange rate unification, fiscal reform and foreign aid or concessional loans to offset a temporarily deteriorating current account. It should however be noted that the implementation of liberalization had not been uniform for the four countries and had occurred after basic economic reforms had been undertaken. For example, the whole process of economic restructuring had involved the creation of six strategic industries – steel, petrochemicals, nonferrous metals, shipbuilding, electronics and machinery, supported with government intervention in terms of tax incentives, detailed engineering, subsidized public services and preferential financing.

The first three sectors were aimed at enhancing self-sufficiency in industrial raw materials while the last three sectors were directed at enhancing technology intensive export industries. The other accompanying measures included land reform, which fostered social and political stability while increasing agricultural production output to provide industrial raw materials and foreign exchange for the importation of machinery and other equipment. The governments also invested heavily in the development of infrastructures like transportation, energy and human resources. In Sub-Saharan Africa, the legislation appears to abrogate the right to land of millions of small holders. In Mozambique for example, the new land legislation will end in confining the majority of the rural people into small communal enclaves while the bulk of the best agricultural and will be sold or leased to private South African investors. This is type of land reform will undermine development.

The importance of human resources in South East Asian economic miracle is forcefully brought out with respect to the policy programme followed in Taiwan. The government decision to focus on high-technology industries (information, biotechnology, electro-optics, machinery and precision instruments, and environmental technology

industries) required a closer coordination of industrial, financial, science and technology, and human resources policies. The government revised its laws to subsidize manufacturers who allocated a percentage of their revenues to research and development (R+D); gave incentives to industries to diversify and improve production techniques; established venture capital; and revised university curricula to strengthen the teaching of science, mathematics, engineering and computer sciences.

In Malaysia whose experience is close to those of most SSA countries provides an insight of how proper economic policy can be effective. The country's import-substitution policy which was similar to those of other developing countries was supported by the New Economic Policy (NEP) launched in 1971. NEP was designed to complement the export-promotion effort. The main NEP exports incentives included taxable income deductions linked to the export performance and domestic input content, tax allowances for export-related promotional expenses, and accelerated depreciation for firms exporting more than 20 percent of their output. In other words, macroeconomic stability and export policies played major roles in the economy.

It should therefore be noted that liberalization in South East Asia only occurred after firms were already competitive, in fact there is now a consensus that dynamic efficiency of the South East Asian industrialization was based on the ability of the state to directly coordinate investment across sectors, reaping thereby, the benefits of demand and supply complementarities. Industrialization was also based on the states' ability to discipline firms through rewards and sanctions to ensure that export targets were met (Amsden, 1989; Wade, 1990). The East Asia developmental state were characterized by "embedded autonomy" which implies the existence of dense network of private – public sector interaction, with the state being on the "driving seat" (Evans, 1989; de Valk, 1996). It is for these reasons that (Stoneman, 1992) argues that structural adjustment must be "depackaged" if it is not to lead to further economic marginalization. The recent experience in East Asia once again underscores the need to impose more market discipline. Soros (1998) asserts that "today's crisis cannot be solved by market forces alone, but that public-policy measures are needed to stabilize the flows of international finance required by the global capitalist system and to keep the inherent instability of financial markets under contol".

4.2 Trade Liberalization: Its Performance

Trade liberalization programmes have been given impetus as a result of various types of stimuli, which are categorized as unilateral and multilateral mechanisms (Oyejide, 1996). The stimuli derive from conditionality imposed as a result of structural adjustment, liberalization efforts associated with either positive shock or a country's "own initiative"; and liberalization efforts implemented in the context of specific regional integration arrangements.

In Eastern and Southern African subregion, all the four aspects of stimuli have been applied, but to very large extent, the trade liberalization process has been undertaken within the framework of the structural adjustment programmes. Almost all the COMESA countries are implementing the SAP. The ECA report ECA/MULPOC/LUS/ICE/III/4 (1994) indicates that the countries of the subregion started to implement SAP at different times, but as far back as 1975. In Kenya and Tanzania the coffee export boom stimulated trade liberalization between 1976 and 1977, while the "self imposed-own-initiative" stimuli occurred in South Africa, Zambia, and Tanzania, where liberalization of trade was aimed at ameliorating the shortages of essential commodities and controlling inflation. In PTA/COMESA, the pursuit of unilateral trade liberalization at the level of each individual country has overshadowed preferential trade liberalization scheme (Oyejide, op.cit:).

A review of the experience of trade liberalization scheme as undertaken and implemented by the different countries in the subregion displays a rather "zig-saw" kind of movement with respect to tariff reductions. In Kenya trade liberalization measures were introduced during the Fourth National Development Plan (1980-1984). The highest tariff rate was reduced from 135% to 60%. Since 1988 the import duties have come down progressively and the maximum tariff rate has been reduced to 25%. The number of non-zero rates currently stand at 3. The number of tariff categories were also reduced from 25 to 12 and tariff rates on non-competing imports have been lowered. The overall production weighted tariffs fell from 62% in 1989/1990 to 45% in 1992. The quantitative control with respect to manufacturing production was lowered from 79% in 1988 to 28% in 1991. In Kenya all quantitative restrictions have been virtually replaced by tariffs. In Tanzania, the Bank of Tanzania (1991) from April 1990 removed the Open General License (OGL) upper ceiling of US$1.0 million

requirement for imports, per annum, while the maximum tariff rate have fallen from 250% to 50%.

In Zambia, the tariff restructure has four levels. These are 0,5,15 and 25 per cent tariff rates. This indicates that the country tariff levels have fallen, as other non-tariff barriers (quotas, exchange control and licensing) have also been eliminated. In Zimbabwe, the objective of the trade liberalization programme was to have most imports (targeted at 85% of the value) free of import licensing or any other form of quantitative import restriction removed by the end of 1995. In 1992, the Government decided to pursue future trade liberalization through the more rapid expansion of the export retention scheme (ERS) rather than through the combination of ERS and open general import license (OGIL) systems.

At the COMESA level the tariff reduction schedules had been revised in 1988 and 1993, but both of the revisions had the zero tariff target by the year 2000. Judging by the current rate of implementation, where six countries Comoros, Eritrea, Kenya, Sudan, Uganda and Zimbabwe have achieved 80%, reduction, two countries Malawi and Mauritius have reduced by 70%, three other countries Burundi, Rwanda and Zambia by 60%, while the rest, excluding the two (Namibia and Swaziland) exempted until end of 1997, have not reduced by a single rate (COMESA, 1998), it would appear that the timetable will not be met. The reasons proffered for non-implementation include, civil war situation; protection of enterprises (sensitive/infant); and the wait-and-see attitude adopted due to the non-compliance by some of the trading partners.

With regards to the elimination of non-tariff barriers, COMESA has made substantial progress in the elimination of most of the concessional non-tariff barriers such as restrictive import and export licensing, foreign exchange allocation, quotas, other prohibitions, and road blocks. Some countries like Kenya, Zambia and Mauritius have liberalized the capital account in order to promote cross-border and direct foreign investment. The use of COMESA Yellow Card has facilitated the elimination and easing of administrative and legal bottlenecks in transport and communication through harmonization of road user charges, axle load, vehicle dimension and telecommunication tariffs (COM/TC/CT/111/4, 1998).

SADC on the other hand is still faced with the inclusion in its legal and institutional structures, appropriate and legitimate anti-dumping, safeguards, and trade restrictions where these may be required for balance of payments and infant industry reasons. A case in point is the recent increase of tariff by Zimbabwe in response to a perceived closure of the measures for the reasons mentioned above.

The liberalization of trade has adversely affected the manufacturing sector and is leading to a call for the reciprocity in duties to be levied on similar products. While the results which has been achieved thus far remain mixed, the need to assess the degree of liberalization within the subregion is still valid in order to see to what extent it has stimulated production.

4.2.1. Impact of Trade Liberalization on production

Trade liberalization provides market opportunities which allow for greater exploitation of comparative advantage, capacity utilization, and economies of scale. This process has to be accompanied by the removal of discriminatory practices and reduction of anti-export biases. In attempt to assess the degree of trade liberalization and to measure the extent to which trade liberalization has stimulated production and capacity utilization, three proxies will be used to assess these effects: the import–GDP ratio, export–GDP ratio, and the impact of exchange rates on imports. The import-GDP ratio is used to assess the degree of liberalization of the economies of the subregion. The assumption is that, as trade liberalization progresses, the import-GDP ratio increases. The export-GDP ratio will on the other hand be used to measure the performance of the economies in terms of output and capacity utilization, as the anti-export biases become reduced. The result of regression analysis on the impact of exchange rate on the import will be used to gauge the real impact of liberalization on the economies of the member countries of COMESA, as the lack of the capacity to import will affect production in general.

From Table I it can be seen that a higher degree of liberalization has been achieved by two countries, Seychelles and Mauritius whose import/ GDP ratio rose by 43.3% and 31.4% respectively between 1980 and 1996. The average for the two countries between 1980 and

1996 was 60.6% for Seychelles and 53.9% for Mauritius. The countries which have liberalized their trade by between 50 and 30 percent on the average were Malawi, Zambia and

Table I: Import GDP Ratio of COMESA COUNTRIES 1980-1996

COUNTRY	1980	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	Average
ANGOLA		16	17.6	18.7	22	23.4	31.1	23.6	21.9	24.6	22.7	22.2
BRUNDI	20	19	17.3	15	18.8	16.6	16.7	15.6	19.8	23.7	12.4	17.7
COMOROS	30	23	31.1	36.9	41.9	50.2	50.2	49.3	54.2	73.9	80.4	47.4
D.R. CONGO	12	10	9.9	15.8	18.3	12.6	12.7	16	20.2	26.2	27.9	14
ERITREA		...	...	...	...	...	...	...	...	...	...	...
ETHIOPIA		16	14.4	12.6	13.7	17.5	17.6	14.1	13.3	15.5	14.2	14.9
KENYA	41	21	0	24.2	22.1	19.7	19.7	18.7	28	34.3	34.6	23.9
MADAGASCAR	22	23	13.7	14.2	21.6	16.8	16.8	16.1	16.1	22.9	23.1	18.8
MALAWI	41	25	34	46.5	47.7	44.4	53.8	35.4	45.9	45.9	42	42
MAURITIUS	49	52	64.6	63	72	66.4	65.2	65.4	70	68.3	72.4	53.9
NAMIBIA	1	0.6	0.7	3.2	11.6	7.4	7.9	6.9	6.7	7.7	8.2	5.6
RWANDA	13	17.5	17.2	14.5	13	14.6	12.7	13.5	26	24.3	25.6	15.4
SEYCHELLES	43	38.1	47.6	57.4	60.3	54.4	56.8	66.5	58.5	87.3	96.3	60.6
SUDAN	10	6.4	7.2	8	7.9	8.4	7	6.3	5.7	6	6	7.2
Swaziland	6	5.8	8.5	6.1	10.2	10.2	9.9	14.6	10.6	9.4	9.1	8.3
TANZANIA		23.5	22.8	20.9	26.2	30.4	36.4	33.4	32.6	36.1	37.2	29.2
UGANDA		7.9	6.9	6.3	7.5	5	4.8	5	5.6	6.6	6.3	6.2
ZAMBIA	61	36.8	36.4	54.8	52.8	39.7	42.5	34.8	22.9	36.2	40.5	36.7
ZIMBABWE	5	22.3	16.7	25.5	31.3	32.8	38.6	31	36	36.1	45.2	27
TOTAL COMESA	**...**	**15.4**	**13.3**	**17.8**	**19.8**	**18.7**	**20**	**17.6**	**19**	**21.3**	**21.8**	**18.5**

SOURCE: Table is constructed from COMESA Trade Data Published in COMESA Selected Indicators, march, 1998
... indicates unavailability of data

NB. Eritrea data are combined with those of Ethiopia

Comoros. For Angola, Kenya, Tanzania, and Zimbabwe the average was between 30 and 20 percent. The low level liberalization of between 20 and 10 per cent on the average had been recorded for Congo (DR), Madagascar, Rwanda, Ethiopia and Burundi. The countries with below 10 percent level on the average were Namibia, Sudan, Swaziland and Uganda. For

COMESA as a region the liberalization of trade has been on the lower side. Those on the lower scale of trade liberalization process such as Uganda, Sudan and Namibia can only possibly sustain these through massive inflow of official and private resources.

Table II indicates that Mauritius is one of the three countries in the subregion with the highest export/GDP ratio which averaged about 48.5% between 1980 and 1996. This shows that the country performed well in terms of manufacturing output as well as in export. The other two countries, Angola and Swaziland with average of 41.5% and 43.7% respectively over the same period, perhaps reflect the key role played by the exports of some important primary commodities such as petroleum and sugar. This conclusion is reached when the import/GDP ratio of the two countries are considered to be 22% for Angola and Swaziland. Most countries in the COMESA region have shown inferior ratio of export/GDP because the export structure of the countries continue to be concentrated on a few primary commodities and destinations as their major market outlets. There is also lack of diversification in production.

Table II: Export/GDP Ratio of COMESA Countries 1980-1996

COUNTRY	1980	1987	1988	1989	1990	1991	1992	1993	1994	1995	1996	Average
ANGOLA	...	29.8	31.9	36.8	48	39.3	44.1	49.3	36.3	45.4	54.5	41.5
BRUNDI	7.9	7.7	8.5	6	6	7	5.5	12	15.1	21.2	3.7	9.2
COMOROS	5.9	9.7	13.9	13.3	11.2	14.4	12.9	24.9	26.4	5.3	6.7	13.1
D.R. CONGO	23.2	12.8	14.6	20.3	19.2	24.7	25.6	19.8	23.5	30.6	30	22.2
ERITREA	...	...	...	...	...	...	...	...	...	...	...	...
ETHIOPIA	...	4.9	5.6	6.1	3.7	2.2	2.6	3	3.8	5.2	4.8	4.2
KENYA	22.6	12	12.7	10.9	12.1	10.8	14.2	13.7	17.5	19.3	21	15.2
MADAGASCAR	14.8	12.7	10.3	11.4	12.8	11.5	9.9	9.2	11.6	20.5	21.7	13.3
MALAWI	28	23.9	23.4	22.9	31.1	33.6	37.5	26.2	33.8	30.8	29.9	29.2
MAURITIUS	34.7	46.9	49.8	47	53.4	50.9	52.2	49.6	45.7	50.9	51.9	48.5
NAMIBIA	2.5	1.3	2.3	5.7	25	17.8	11.1	11.3	20.7	16.9	14	11.7
RWANDA	4.2	5.1	4.7	4.2	4.5	4.3	8.7	4.9	7.2	11.5	11.3	6.4
SEYCHELLES	7.6	8.4	28.8	40.8	34.4	42.7	37.6	22.1	30.1	32.7	48	30.3
SUDAN	3.7	3	3.4	3.6	3.1	2.2	1.7	1.8	2.1	2.3	2	2.6
SWAZILAND	56.8	35.7	46.5	41.7	51.8	47.5	49	35.8	41.9	38.1	35.4	43.7
TANZANIA	...	8.4	7.7	6.9	10.7	10.2	11.4	11.6	12.5	15.7	16.9	11.2
UGANDA	...	4.8	4.8	3.8	2.4	2.2	2.1	1.5	3.8	4.5	4.8	3.5
ZAMBIA	60.3	31.3	36.5	28	22.9	45.6	31.8	36.8	31.8	48.8	41.5	37.8
ZIMBABWE	8.6	21.1	23.8	21.4	24.2	19.8	21	21.7	30.4	33.4	34.2	23.6
TOTAL COMESA	**....**	**12.3**	**13.7**	**13.9**	**15.7**	**14.9**	**15.1**	**13.7**	**15.5**	**17.5**	**18.1**	**15.4**

SOURCE: Table is Constructed from COMESA Trade Data Published in COMESA Selected Indicators, March, 1998
... indicates unavailability of data

NB Eritrea data are combined with those of Ethiopia

When the average of export/GDP ratio is compared with import/GDP ratio for the whole of the COMESA region, it can be seen that of export/GDP ratio is lower and averaged 15.4% as compared to 18.5% for import/GDP ratio. The conclusion that can be drawn from these figures is that the COMESA region as a whole has a weak production capacity base. This has in turn been translated into a weak intra-COMESA trade. While the picture remains rather inconclusive, and while trade liberalization may have conferred some positive effects in terms of growth in exports, the small group of countries and the region as a whole had not performed that well with respect to growth in output and employment.

The impact of liberalization as measured by the results of the regression analysis in Table III indicates a mixed outcome. But the Table shows that the results were significant in 9 countries and insignificant in 7 others. In four countries, namely, Seychelles, Zimbabwe, Mauritius and Malawi the t calculation were 7.3; 4.4; 4.0 and 3.9 respectively, indicating that the exchange rates did not constitute a major bottleneck between 1980 and 1996 on the average. Liberalization impact was therefore positive, and stimulated growth and output as productive activities were not constrained with the inability to import. The two countries that performed even better within this group of four countries were Seychelles and Mauritius, where there has been a long history of liberal economic policies. For Zimbabwe and Malawi the picture started to change during the beginnings of the 1990s. In Angola and Ethiopia, liberalization had limited positive impact on economic growth and output mainly because for Angola the exportation of petroleum eased the foreign exchange bottleneck, while for Ethiopia the government had imposed foreign exchange control.

Table III: Results of Regression Analysis Between Exchange Rate and Imports, 1980-1996

	Angola	Burundi	Comoros	D.R. Congo	Ethiopia	Kenya	Madagascar	Malawi	Mauritius	Rwanda	Seychelles	Swaziland	Tanzania	Uganda	Zambia	Zimbabwe
X-coeff.	0.374	0.083	0.475	0.037	0.379	0.433	0.055	0.291	1.768	0.070	3.040	0.967	0.089	0.006	0.005	0.487
St.err.coeff.	0.103	0.118	0.475	0.020	0.129	0.734	0.060	0.075	0.439	0.049	0.418	0.505	0.036	0.035	0.028	0.110
t cal	3.646	0.702	1.000	1.846	2.930	0.590	0.907	3.866	4.024	1.420	7.275	1.915	2.446	0.170	0.183	4.416
to.5(df)	1.753	1.753	1.753	1.753	1.753	1.753	1.753	1.753	1.753	1.753	1.753	1.753	1.753	1.753	1.753	1.753
R^2	0.47	0.03	0.06	0.28	0.36	0.02	0.05	0.50	0.52	0.06	0.10	0.20	0.28	0.002	0.002	0.57
Results	**	*	*	**	**	*	*	**	**	*	**	**	**	*	*	**

N.B. * Not significant
** Significant

Source: Calculations in the Table are made from ECA Statistical Bulletin, various issues.

In Uganda, Zambia, Kenya, Burundi, Comoros, Madagascar and Rwanda liberalization had a negative effect on economic growth either because the countries liberalized too quickly or due to lack of a consistent policy on the management of foreign exchange rates. The correlation between exchange rates and imports show very weak relationship as capured by R^2 ranging between 0.06 and 0.002. In three countries, Tanzania, Swaziland and Congo Democratic Republic liberalization had a very weak impact on economic growth. Even in countries where liberalization appears to have had positive effect, its impact on growth had not been robust enough as the ability to import had somehow been curtailed by frequent changes in economic policy. From Table III it can be concluded that liberalization has on the whole had a negative effect in a large number of countries in the subregion in terms of economic growth and performance. Most countries of the subregion have witnessed economic decline. The positive impact of liberalization has been extremely limited.

It can be concluded from the analysis that the weak production base which has been propelled by the de-industrialization process which has occurred in some countries has undermined the capacity of the region to respond rapidly to the economic challenges that face it. The competitive pressure that has been unleashed by trade liberalization has made it more difficult for firms that had hitherto been sheltered under high tariff walls to cope, especially in the textile industrial subsector. The challenge facing the region is its heavy reliance on external financing which is used to prop up the economies. This may not be sustainable in the long-run, given the shrinking trend in aid external resources as well as its other negative impact.

V. THE MOVEMENT OF FACTORS OF PRODUCTION (LABOUR AND CAPITAL)

5.1 Labour Mobility

This section reviews the two strands that underpin theoretical arguments about liberalization in terms of labour and capital mobility. According to the neo-classical

economic theory, one of the effects of liberalization is `factor price equalization'. As goods, people and capital freely move across national borders there is a tendency for price equalization between countries. While labour should move from low-wage to high-wage countries, capital should move in the opposite direction. This will continue until equilibrium is reached when the remaining wage gap represents the cost of migration between the two countries. Migration then comes to an end.

Evidence from OECD countries suggests that movements of all factors of production contributed to convergence, but that the relative contributions varied for different periods. In the first phase, the major factors was mass migration. In the second phase, convergence was the consequence of investment, trade and economic development that served to reduce the incentives for migration between the OECD countries. The evidence in convergence refers only to the industrial countries. When it comes to the world as a whole, the picture is quite different, in that there appears to have been a considerable divergence between the richest and poorest countries.

In the ASEAN region, while there has been a marked policy push toward lowering tariffs or reducing impediments to movement of persons, the free mobility of persons is shown by the large flows of temporary workers across the region. Indeed, the movement of labour or temporary workers within the ASEAN region conforms to the neo-classical theory which asserts that labour would move from low-income to high-income countries. The current movement of temporary workers in the ASEAN region is from Indonesia, the Philippines and Thailand to Brunei, Malaysia and Singapore. The total number of temporary workers involved in this movement was estimated to be over 123,078 in 1993. This group of temporary workers consist of unskilled, semi-skilled, female and illegal immigrants who seek work in the construction, labour-intensive industries, domestic services and entertainment.

Between 1870 and 1960, the per capita income of the richest country (the United States) rose from US$2,181 to US$16,779. Whereas over the same period, the income of the poorest countries, such as Ethiopia only rose from $250 to $325 (Stalker, 1997). The ratio between the two group of countries rose from 9:1 to over 50:1. This divergence has continued. Pritchett (1996) observes that over the three decades, the ratio of the income of the

richest to the poorest rose by 45%. Human Development Report (1996) estimated that, between 1960 and 1991, the share of global income of the richest 20% of the world's population rose from 70 to 85 percent while that of the poorest declined from 2.3 to 1.4 percent, and that by 1993, of the $23 trillion global GDP, $18 trillion was generated in industrial countries and only $5 trillion in developing countries. While in the past the movement of people helped the economies to move closer together, in recent years political resistance to migration has stifled this process (Stalker, op.cit.).

In Eastern and Southern African subregion, there has been a long history of movement of persons occasioned by several factors which include: poor and weak economies, population pressure on land, and political instability. In other words, there has been three types of this movement, namely: temporary contract workers which include labour and unskilled/semi-skilled group who emigrate for as long as their labour or skills are required in the countries of immigration, or temporary professionals among whom are labour and skilled or professional persons. The second category is clandestine/illegal workers who are often undocumented but who nevertheless move from low-wage to high-wage countries. The third category of movement involves asylum seekers or refugees whose movement is caused by civil wars, the vagaries of climate or famine. For the purposes of this analysis the third category of labour movement although important, is of little interest. The main concern in this study is with labour mobility based on purely economic arguments and designed to promote free labour mobility as a mechanism for factor-price equalization.

In Southern Africa for example, there has been trade in factors of production with South Africa. In 1986 there were 378,125 workers in South Africa from neighboring countries, whose remittances accounted for a considerable part of those countries' capital account inflow (Ncube, 1991). In the former East African community (EAC), labour mobility between the three partner States, Kenya, Uganda and Tanzania has been well documented. The labour movement was from Kenya to Uganda and Tanzania – a reverse flow of labour, contradicting the theoretical expectation which stipulates that labour should move from less developed to relatively more developed countries. (Ochola, 1969).

Table IV which provides a rough picture of the migrant stock and remittances in the ESA, is able to show the trends overtime and the vast economic disparities among the countries of the subregion. The ESA countries with a large stock of immigrants in the descending order include: Djibouti, Malawi, Swaziland, Zimbabwe, Somalia, Comoros and Burundi. The other group of countries with migrants stock accounting for less than one percent of the national population are: Mozambique, Madagascar, Namibia, Kenya and Mauritius. The immigration into ESA countries is due to refugee inflows as shown by column four in the Table as the percentage of female in the migrant stock of individual countries. The last column on remittances indicates that remittances as percentage of foreign exchange earnings were highest in Lesotho, which depends almost entirely on remittances, followed by the Comoros and Mozambique.

Table IV: Migrant stock and remittances in Eastern and Southern African (ESA) countries, 1990-1994

Sub-region and country	Migrant stock, 1990			Remittances	
	Number of Migrants	Percentage of Population	Percentage of Females in Migrant Stock	Year	Percentage of Foreign Exchange Earnings
Eastern Africa					
Burundi	333 409	6.1	50.2	-	-
Comoros	38 520	7.2	56.7	1991	163
Djibouti	67 352	13.4	49.9	-	-
Eritrea*	-	-	-	-	3.7
Ethiopia*	777 270	1.6	49.8	1993	2
Kenya	168 244	0.7	50.1	1992	1.8
Madagascar	35 000	0.3	38.2	1992	-
Malawi	1 104 515	12.1	50.4	-	16.0
Mauritius	8 780	0.8	44.4	-	2.3
Mozambique	7 319	0.1	57.0	1992	-
Rwanda	69 231	1.0	48.0	1991	-
Seychelles	1 358	2.0	45.9	-	-
Somalia	621 897	7.2	49.9	-	-
Uganda	329 990	1.9	43.3	-	-
Unit. Rep. of Tanzania	579 669	2.3	49.6	-	-
Zambia	324 807	4.1	48.7	-	-
Zimbabwe	775 350	8.0	45.0	1993	0.1
Southern Africa					
Botswana	22 032	1.8	44.0	1990	2.5
Lesotho	24 000	1.4	48.0	1994	57.0
Namibia	7 625	0.6	47.6	-	-
South Africa	1 118 369	3.1	32.0	1194	2.4
Swaziland	68 650	9.4	47.2	1194	7.2

Source: United Nations Department for Economic and Social Information and Policy Analysis, Population Division.

* One country (Ethiopia) until 1991 when the two parted ways

Surprisingly the issue of labour mobility has been given very little attention in ESA subregion in comparison with the West African subregion, where the ECOWAS Treaty has since its inception had a specific protocol on labour movement within the ECOWAS

countries. The PTA Treaty had been completely silent on the free movement of persons, labour services, right of establishment and residence unlike that of ECOWAS. Recently, however, the PTA/COMESA Treaty has included in Chapter 28, Article 164, the provision for the free movement of persons, labour services, right of establishment and residence, which now constitute a separate protocol. In SADC, Protocol on free movement of persons and the right of residence and establishment is under negotiations. In the Republic of South Africa, cross border investments including the settlement of South African farmers in the neighbouring countries are considered effective measures to stem the flow of illegal immigrants into South Africa. The omission of labour mobility in the original legal instruments forming these arrangements over-looked the historical trends of labour movements in the subregion which needed to be formalized in the context of SADC and COMESA. Perhaps the explanation for this omission can be argued to derive from the nature and level of economic integration of these schemes, which precluded the labour mobility as a requirement.

The negotiations of Protocols on labour movement in the context of SADC and COMESA are still at different stages. However, the ESA member States have already adopted "visa relaxation" for permitting immigration for at least one month, and in certain cases, ninety days before residence permit would be required. Even though the Protocol relating to the gradual relaxation and elimination of visa requirements within COMESA had been approved since 1985, the aspects of labour mobility that would facilitate the exchange of skills and enhance economic growth and development have not been properly addressed. For example, Kenya has implemented the first phase of COMESA protocol on elimination of visas, and has committed itself to the COMESA time table on free movement of persons, labour and service and the right of establishment and residence which eventually aims at granting of residence to nationals of COMESA countries by the year 2014. Other countries have yet to make their intentions known. In SADC, while the visa-free entry is not a contentious issue, the other parts of the Protocol such as "right of residence" and "right of establishment" still remain thorny issues, on which negotiations might be protracted.

What remains to be done in COMESA and SADC is to formalize the growing wave of free movement of labour in the subregion in order to promote paid employment and self-

employment. For example, Kenyan school teachers, university lecturers, doctors, nurses and businessmen and women have taken advantage of available employment opportunities in and economic buoyancy in Botswana, Namibia and South Africa. Equally, Zambia and Malawi, as a result of experiencing economic doldrums have set on an emigration course, particularly of their highly skilled and educated personnel, who have found homes in Botswana, Namibia and South Africa (Oucho, undated).

These are positive development for regional integration in ESA for two reasons. Firstly, the expectation to expand volume of migrants' remittances to their home country would lead to the equalization or convergence of level of incomes between the member States. Secondly, this kind of labour mobility would strengthen economic integration, by enhancing the transfer of skills and learning process. Indeed, labour mobility is viewed as the binding force for member States with varying human resource bases, capacities and potentials to enhance their utilization in national as well as in intra and inter subregional programmes.

These development are consistent with the ultimate objectives of both COMESA and SADC which consider the dismantling of barriers to trade, labour mobility, and the movement of capital and resources as well as the redistribution of labour as vital aspects of regional market and engine for the operation of the community and as assets which must be allowed to find their own levels. It is against this backdrop that an all out effort must be made to resolve the issue of free movement of labour within the regional communities.

5.2 Capital Mobility

The theory suggests that capital will flow from capital-abundant to capital--scarce countries and thus, raise welfare in both sets of countries alike on the assumption that the marginal product of capital is higher in the latter than the former; and that the free capital movement will permit a more efficient global allocation of savings and direct resources toward their most productive uses. The purpose under this subsection is to analyse the issue of capital mobility in the context of economic regional setting and investment. A number of authors (Balasubramanyam and Greenway, 1992) have pointed out the connection between capital flows and economic integration, with the latter stimulating the former. Regional

integration is said to enhance the attractiveness of a region by creating a larger common market where efficiency and higher levels of income can be achieved, besides eliminating trade and investment barriers.

Theoretically, it is argued that tariff barriers do motivate import-substituting foreign direct investment (FDI), while tariff reduction reduces FDI flows or even stimulate repatriation of foreign owned assets to the home countries of multinational corporations (MNCs) (Blomstrom and Kokko, 1997). The trade agreements or arrangements which reduce or eliminate non-tariff barriers are expected to make exporting a more viable international business mode and discourage FDI, other things being equal. This theoretical assumption would negate the key principles on which regional integration is build vis-à-vis, the stimulation of investment. The early literature on foreign investment tended to regard trade and capital movements as substitutable modes of serving foreign markets (Bhagwati and Tironi, 1980).

While the reductions in tariffs and non-tariff barriers are major features of all regional integration schemes, it is less obvious what the simple model would predict, when regional rather than global trade liberalization is considered. The reason is that, investments made by "insiders" and "outsiders" would be affected differently as a result of the formation of regional integration when intra-regional FDI is considered from the "tariff jumping" perspective. In this connection the reduction in investment would be expected to occur because trade liberalization would make exporting more lucrative than FDI as a way of serving the regional market.

But if regional integration results in trade creation, it is likely that changes in the regional production structure would motivate a shift of investment from one participating country to another. It is in this context that intra-regional FDI in some member States could well be created in response to the emergence of new investment opportunities. The extent of cross-border investment will in this regard depend on the relative strength of the firms within the different member countries. The FDI flows would be relatively small if the firms which are best positioned to exploit the situation are already based in the most favoured production location.

The potential impact on intra-regional FDI flows has been termed "investment diversion" and "investment creation" (Kindleberger, 1966), which he defines as a response to "trade creation" and "trade diversion" respectively. Investment "creation" comes about in response by outside firms which lose export market when their former customers turn to suppliers based in the region because regional trade is free from tariffs, while "investment diversion" would contribute to increased intra-regional FDI in some countries. However, given the free trade scenario within the regional integration arrangement, the location of new investments will be determined by the comparative advantage of the countries participating in the regional scheme. To the extent that there are other motives for FDI than tariff-jumping and trade barriers, the exploitation of the intangible assets in terms of technological and marketing expertise is often a major motive for foreign investment. FDI can therefore be effected in the absence of "internalization" and "tariff jumping" motives, as witnessed in the OECD countries.

Empirical evidence suggests (Winters, 1996) that Spain and Portugal benefited from significant increases in inward FDI as a result of their membership in EC, while Greece did not benefit to the same level due to its macro- economic policies which failed to provide an attractive environment for foreign investments. In the case of North-South integration, the experience indicates that Mexico benefited, as the North American share of Mexican export increased from around 70% in late 1980s to over 86% in 1995. Regional integration stimulated significant increases in the inflows of foreign investment from countries outside the NAFTA region (Blomström and Kokko, op.cit.).

In the South-South integration like MERCOSUR, SADC and COMESA the locational advantages for several industries which are likely to arise from the creation of a large common market, is the attractiveness which the regions would create by pooling together their abundant national resources and in some cases their skilled and semi-skilled labour. However, in the context of South-South integration experience tends to show that macro-economic stability is a more important determinant of FDI inflows than the creation of a regional market. But, a more comprehensive integration in the form of a common market is likely to be much more effective in the stimulation of investment responses.

Lastly, the inflow of FDI into the region is likely to be concentrated in some few countries at the expense of the other participating countries, in accordance with the integration theory of economic geography (Krugman, 1991) which stipulates that investment activities will tend to concentrate economic activities in regions or countries with better infrastructural facilities. In Eastern and Southern Africa subregion the countries that fall into this category are South Africa, Mauritius, Zimbabwe, Kenya and Botswana, which are likely to remain as strong locational countries for foreign investment should they improve and sustain their macro-economic stability, and promote consistency and credibility within their reform programmes.

5.2.1 Trends of FDI in the Subregion

Foreign direct investment inflows into Africa stood at $5 billion in 1996. The three largest recipients countries were: Nigeria, Egypt and Morocco. Africa's share of developing countries inflows was 3.8% in 1996 the lowest since the early 1980. On the average, Africa's share of developing inflows has dropped from 11% during 1986-1990 to 5% during 1991-1996, suggesting that Africa has not derived benefits from the increased FDI inflows into the developing countries. This trend is captured in Table V which shows the share of the various groups of developing countries' total in the private capital flows. The Table reveals that private capital flows are concentrated in Latin America and Asia. The Table further reveals that Asia has improved its position vis à vis Latin America.

TABLE V: Distribution of Private Flows of Capital to Developing countries

	1970	1980	1987	1990	1991	1992	1993	1994
Sub-Saharan Africa	0.08	0.09	0.12	0.04	0.03	0.00	0.02	0.02
North Africa	0.07	0.07	0.17	0.00	0.00	0.03	0.02	0.01
Latin America	0.61	0.55	0.40	0.32	0.42	0.35	0.42	0.35
Asia	0.23	0.28	0.29	0.65	0.54	0.62	0.54	0.62
HIPCS	0.07	0.10	0.13	0.03	0.05	0.01	0.03	0.02

Source: World Bank, 1996

The theoretical argument indicates that market size is an important determinant in the flow of FDI. If market size is considered in terms of GDP, it can be seen that Africa's FDI stock in 1995 was 13%, compared to about 13% for Western Europe, 14% for Asia and 18% for Latin America and the Caribbean. If SSA is considered in isolation, the percentage is as high as 17%. The high percentage is however misleading as SSA high ratio is caused by its relatively very low level of the GDP which is low in comparison to those of Western European countries.

In an effort to improve the investment climate, several African countries have removed ownership restrictions, reduced taxation rates, abolished controls and encouraged private sector initiatives. As of 1 January 1997, some 45 African countries had concluded as least one bilateral investment treaty (BIT) and a total of 267 BITs, of which 17 were concluded within the continent. While regional integration agreements are supposed to improve the prospects for investments by attracting MNCs towards the enlarged regional market, what has been the experience in Eastern and Southern African subregion? This will be examined within the context of cross-border investment initiative, and what role the regional markets have played to stimulate both internal and external investments in the region.

5.2.2. Extent of Cross-Border Investment Flows in the Region

The examples of cross-border investments in the region are very few, except for the ones that are originating from South Africa. Within the SADC region, South Africa has experienced a growing investment boom within the region and which has expanded rapidly. The growth has mainly been accounted for by the increased private sector flows into South Africa which stood at US$2.2 billion in 1994, and South Africa's investments in projects across its borders. Republic of South Africa's investment into the region has however been achieved at the expense of its neighbours who have as a result of these activities experienced rising trade deficits. Most of the investments which South Africa carries out in the subregion are in mining, food processing, retailing (supermarkets, breweries) and other services like telecommunications. The South African Breweries have already invested in countries like Zambia, Tanzania, Kenya and Uganda, and have negotiated the establishment of a brewery plant in Ethiopia. Evidence, indicates that South African investments have been at a very low level of industrial scale, and are thus, unable to contribute to the transfer of technology or to human resource development.

In addition to South Africa, only a handful of countries in the subregion have made attempt at carrying out cross-borders investments. Zimbabwe has made cross-border investments in Botswana, Malawi, Mauritius, Mozambique, Namibia and South Africa. The main sector of these investments include banking and finance, transport, storage and freight, manufacturing, mining, hotel industry, building, construction, architecture, retail and marketing, and advertising. Cross-border investments from Mauritius have grown in recent years to an annual value of over US$1.5 million. Mauritius investment are concentrated in the Indian Ocean Islands (IOC) countries which claimed 90% of the investment. The main sectors are tourism and manufacturing. Madagascar remains an important investment destination for Mauritius. The other countries such as Madagascar, Namibia, Seychelles, South Africa and Zimbabwe have also invested in Mauritius.

Kenya has undertaken cross-border investment in Botswana, Rwanda, Uganda and Tanzania in the field of fish processing, banking and other services, and manufacturing. Kenya's investments in Uganda and Tanzania ranks second after Great Britain (Personal

interview 1998). Kenya had also received requests to invest in Burundi (tourism), South Africa (manufacturing) and Sudan (manufacturing). In East Africa the three countries (Kenya, Uganda and Tanzania) were taking steps to have cross listing of shares in the Stock Exchange Markets of the three partner states.

The countries of the subregion have embarked on programmes to attract and promote private investment, both foreign and domestic. To this end they have fully liberalized by removing some of the constraints to investment in the region. However, a good number of countries still restrict the sectors in which foreigners can invest. The only sectors which are open to foreign investors are often in areas involving technological learning. Some countries such as Ethiopia and Uganda still have as a requirement, a minimum of US$500,000 deposit before a foreign investor can undertake any investment. There is however no discrimination with respect to both domestic and foreign investors. This rule applies across the board. There are no preferences given to investors from within the region. Regional and outside investors are treated equally.

In the context of SADC all the foreign investments seem to cluster into South Africa which is being used as a base to supply the regional and world markets (World Investment Report, 1997). The foreign investors are inclined to locate their enterprises within South Africa, with the expectation of using the country as the economic hub of the region while the countries of the subregion expect to use South Africa as a "growth-pole". The discernable trend is that most of the low income countries and with severe structural problems in Eastern and Southern African subregion, are unlikely to attract substantial private capital in the foreseeable future. From the foregoing, it would appear that the formation of regional markets have had limited impact in attracting foreign investment. What then is the alternative?

VI. EXPLOITATION OF COMPLEMENTARITIES FOR INTRA-REGIONAL TRADE EXPANSION

6.1 Subregional Potential for Complementarity

The creation of COMESA and SADC aims to provide the participating member States with the opportunities to reduce the cost of industrialization by exploiting economies of scale through preferential openning of markets with one another (Lyakurwa et al, 1997), and to release the dynamic effects of integration which will result in changes in efficiency and in the ability to exploit economies of scale, specialization, investment opportunities, and to promote growth. Theoretically, trade arrangements are supposed to give smaller economies access to larger markets through trade liberalization.

Indeed, while tremendous scope exists for the promotion and exploitation of complementarities within ESA region in both agricultural and manufacturing sectors, the real bottlenecks appear to be in the absence of the basic prerequisites necessary to bring these about. In the agricultural sector, the subregion is endowed with a wide spectrum of ecological diversity and differences that would not only allow for specialization and diversification in the production of agricultural products, but would also create a basis for the promotion complementarities. The agricultural potential range from livestock, cash crops, fisheries to a wide range of cereals products and tubers. The various climatic zones permit the production of a variety of fruits, vegetables, fibre products, cotton, condiments (gloves, pepper), nuts (cashewnut) and horticultural products. The region has vast water resources that could be harnessed for agricultural production.

In the area of natural resources, the region has a good blend energy, minerals and industrial minerals. The region, especially the central and southern parts of the subregion are known as a mineral "eldorado". The range of mineral resources is vast and diversified, and covers from gemstone to building materials and from rare earth to uranium. Some of the key ones include large deposits of iron ore, copper, nickel, cobalt, manganese, alloy metal which include columbite/tantalite titanium/vanadium, tungsten, zinc, lead, gold and soda ash.

Industrial/agricultural minerals include limestone, clays, phosphate, salt and building materials. In the field of energy resources, the region is endowed with renewable and non-renewable energy resources such as hydroelectric energy, coal, hydrocarbon, natural gas, thermal energy, biogas and solar energy. For example, the natural gas reserves is estimated at approximately 600 billion cubic meters.

The list of potential industries that would be based on the agricultural, natural and mineral resources of the subregion is vast and is as wide as the innovative capacity of the human mind, which is the only limitation in an attempt to build up complementarities within the subregion. To provide an indication of the possible industries that can be built on the basis of exploiting complementarities in agricultural resource would for example include, the livestock products, such as meat, processed milk, ghee, cheese, leather and leather products. The complementary industries in support of the livestock industries, would include the production of animal feed, vaccines and vitamins as well as chemicals for the tanning of leather and machineries and implements for the manufacture of leather and leather products and the canning of animal production.

In the area of fisheries, the subregion has both marine and freshwater fisheries. The industries to be started on the basis of these resources revolve around fish processing. In support of the fishery industries, there will be need to fabricate fishing nets, boats, hooks and fish feed for the development of aquaculture. More recently, fish skins have found a wide worldwide use. In the field of fruit and fruit products, the subregion has already demonstrates the vast potential by undertaking commercial processing and canning of mangoes, oranges, grape fruits, guava, peaches, pawpaw, apples, passion fruits, pineapples, pears, avocado and other wild fruits such as marula.

In the agricultural sector, the list is endless as the production of cereals and cereal products as well as cotton with their derivatives have not even been examined. The production of cotton will lead to the establishment of factories for textiles and other cotton products including the machineries for their fabrication.

The industries to support agriculture and agro-industries would inter alia include the production of all forms of fertilizers, agricultural equipments, tractors, hoes, water pumps, and irrigation pipes and machineries, including packaging materials to be used in the canning of fruits or for the packaging of bulk materials for exportation. No attempt will be made to list the possible industries that could be established on the basis of minerals and other natural resources which are so abundant within the subregion.

What is at stake in the subregion is the paucity of technological know-how that could trigger off the industrialization process. The absence of the mastery of technological know-how constitutes the real bottleneck for the exploitation of complementarities that can be used to spur intra-regional trade. The quality of human capabilities within the subregion has a lot to do with the present status of underdevelopment. The argument should therefore be turned around to answer what policy package needs to be put in place for the development of the subregion – a meso approach..

6.1.1 The Prerequisites for Exploitation of Complementarities

It has been noted that despite the recent liberalization of investment codes in many of the sub-Saharan African countries, the FDI inflows have declined in sharp contrast to other developing regions (Industrial Development Report (IDR), 1996). The manufacturing sector which holds key to the industrial development process remains extremely weak in sub-Saharan Africa, and particularly in the ESA subregion. While the share of global manufacturing production in other developing countries increased from 12% in 1970 to 19.7% in 1995, that of SSA countries declined from 0.6% to 0.3% over the same period – a 50% decline (UNIDO, 1996). For the COMESA and SADC regions only seven countries have a MVA share to GDP of above 20%. The industrial picture which emerges is that most of the COMESA and SADC countries or economies are charaterised by low level of industrialization. The liberalization as pointed out, has resulted in the de-industrialization caused by a mix of restructuring in the face of macro-economic adjustment and the sequencing of liberalization which may have been too fast and not sufficiently planned (O'Brien, 1997).

Everywhere, a radical emphasis on the market economy and privatization have become the rule. States began to vacate key segments of the productive sector, while the private sector capacity to respond to the fresh challenges have been severely tested. Entry of foreign investment in the control of the economies has been the result. In SADC the tendency of investment movement has been in three directions. The first tendency is for firms to move their plants from elsewhere in the region to the Republic of South Africa. The implication is that under free trade regime countries are to be supplied from South Africa. The other implication which draws from the first, is the high risk of transforming other countries into trading stations or supermarkets as far as industrialization is concerned. Zambia is already showing strong signs towards this tendency.

The second tendency is for extra-regional FDIs to move to South Africa due to its market size and the sophistication of its existing industries. This implies that the other SADC countries are likely to be disadvantaged and frustrated in their effort to attract FDIs and upgrade their industrial sector. Theoretically, there is a clustering tendency of industrial investments to South Africa, and polaralisation effect. The third tendency is for South African firms to undertake outside their borders, the kind of industrial activities related to low value added parts of the production chain which embody very little learning process. The implication, it has been argued (O'Brien op.cit.) is the emergence of a regional division of labour or an industrial terrain in which other countries are likely to be relegated to the lower industrial ladder. For COMESA and the larger ESA subregion a similar picture obtains at least with respect to the kind of South African investments which concentrate in the establishment of breweries and "supermarkets".

At a general level, the study has shown that liberalization scheme is being pursued vigorously in the subregion, either through structural adjustment programmes or through unilateral decision at individual country level. The whole process has not been smooth due to political constraints, inappropriate macroeconomic policies, sequencing and pace of implementation. The other adverse effect of the programme has surfaced in the manufacturing sector which has been put into great jeopardy, partly because the sector is uncompetetive in terms of price and quality.

These difficulties notwithstanding, strong political support has been demonstrated towards COMESA and SADC as the only viable instruments that could be used within the subregion to push the development agenda forward. This support has been manifested in the tendency towards the adoption of a more comprehensive trade reforms in the subregion. Intra-regional trade behind (temporary) high external barriers has often been proposed as a means of providing "training ground" for firms to gain experience and to reap the benefits of economies of scale before they can be exposed to import competition or ready to move towards export markets outside the region. While the experience indicates that such approach is wrought with dangers as it is likely to result in inefficiency, emergence of excess capacity and monopolistic tendencies, the low level of industrial development in the subregion still dictates that a "selective form of protection" should be practiced.

The vast diversity in resource endowment in the region support the "selective" protection approach to industrialization because the capacity to expand production on the basis of comparative advantage exists within the subregion and the fact that comparative advantage can be created. This could perhaps be better pursued in the context of unilateral and multilateral liberalization (Greenway and Milner, 1990). Furthermore, there are still large differences among the countries of the subregion which support the potential for complementarities and for intra-regional trade expansion which can be based on inter-industry and intra-industry specialization. For the COMESA region, the countries have the potential to triple their trade in excess of US$6 billion (COMESA, 1995).

Experience suggests (de la Torre and Kelly, 1992) that the potential gains of regional integration can be maximized if at least two conditions are met, namely:

(i) the maintenance of an outward orientation; and

(ii) the provision for across-the-board intra-regional liberalization with automatic timetabling.

These conditions are important on a number of grounds. They will not only minimize the effects of trade diversion, but will also ensure that the countries remain part of the process of

globalization of investment and production which are the main channels of access to the technology transfers. Furthermore, the countries will be in a better position to achieve comparative advantage in a multilateral context by promoting growth while diversifying their productive structures. Even though the study has pointed out that the countries of the subregion have not been integrated within the global system, but that from the long-term perspective such an approach has to be advocated as very little options now exist not to be part of the globalization process. However, the need to define that participation requires that certain prerequisites will have to be met.

The first prerequisite is the formulation of a regional industrial policy. SADC and COMESA have formulated policies and strategies which aim to enhance industrial cooperation and promote specialization and complementarity between industries in the member States. COMESA has specifically called for the diversification of the manufacturing sector as a method of raising the level of the sector's contribution to the GDP, increasing intra-COMESA trade, investment and the reduction of poverty (COM/TC/CI/11/3/, 1998). The overall industrial objectives are to: promote self-sustained and balanced growth; increase the availability of industrial goods and services; improve the competitiveness of the industrial sector; and develop industrialists that would acquire ownership and the management of industries.

The constraint to the implementation of such policies or strategies is that the global investment policies or strategies of the multinational enterprises has exposed the limitations of regionally based policies. However, a case for a regional policy is strengthened by the argument that successful industrialization and the factors that lead to it are not given but deliberately made (Lall and Wangwe, op.cit.) as already pointed out in this study. The policy would have to be the result of deliberate policy. Lall and Wangwe (op.cit.) further suggest that an optimum policy for industrial development is not a "hands-off" approach, but a thoroughly reformed policies which address specific market failures. There will be need to identify selective strategic priority areas for industrial development. This has to be carried out jointly with the government and private sector. It would not be prudent to leave the issue of industrialization in the hand of private sector alone.

The second prerequisite which draws its inspiration from COMESA's specific programme which advocates, inter alia the acceleration of national capacity building; the reversal of the de-industrialization through the creation of new capacities, rehabilitation and development of entrepreneurial capacity in SMI; the upgrading of level of technological capacity, capabilities, technical skills and information flows; the joint exploitation of the natural resources; and the identification and the development of selective areas where the countries of the region have comparative advantage, paying attention to complementarities, resource endowment and specialization, summarize's adequately the broad policy direction. The countries of the subregion will have to pay particular attention to the development of human resources. The need to address this problem is urgent, if the necessary competence required to attain international competitiveness is to be put together. Regional approach can enhance this process.

Recent thinking on competitive advantage asserts that even though the concept is based on productivity, it is not essentially determined by factor costs as emphasized by traditional theories of comparative advantage (Porter, 1995). In fact, Porter (1995) argues that due to low competition entry barriers, competitive advantage predicated on labour costs and natural resources create structures which support average returns on investment specifically because of too many competitors. Most SSA countries are tied down to competing on factor costs and prices and lack the capacity to influence competitive advantage.

It is now known from experience that factor conditions such as labour costs, capital and natural resources are by themselves not adequate, but mere inputs amongst others that are necessary for creating a base for competition. While it may be argued that Africa is only suited for resource-based and low technology activities that do not compete with imports, however, the competitive advantage based purely on factor cost is vulnerable and unsustainable because lower and better factor costs can easily be created or acquired from other sources (Porter, op.cit.). Since competitive advantage is driven by technological differentiation in a manner which produces constant innovation and improvement, this would require the development of advanced factor of production in terms of highly educated people in disciplines specific to the selected areas for building competitive advantage. This would

only be possible and sustainable if the scientific and technical capabilities are home based and if resources are pooled at the regional level for their creation.

The third prerequisite is to harness the transfer of skills and technology which is currently underway in the region in the context of factor mobility facilitated by the creation of regional of common market. The economic integration process creates the capacity to access both higher and lower order factors of production located across the borders to promote the global competitive advantage of the subregion's industries. There is evidence that the region is already demonstrating a situation where higher level factors of competitiveness (skills and technology) migrate to areas where lower level factors are located. This would require countries which are considered as regional "poles of growth" like the Republic of South Africa to adopt a more positive attitude of promoting the transfer of technology through its investment. The type of a predatory investments which strive to transform other countries into mere "supermarkets" should be discouraged. The liberalization of regional market should not be used to penalize the weak, but to assist them to climb upward, the ladder of industrial development.

The heart of the crisis in Africa is that countries cannot sustain consumption over the long term if they do not produce sufficiently high value added commodities to sustain reproduction. This explains why the poor economic performance of many sub-Saharan African countries have been characterized by declining productive potential. The structural adjustment has not stemmed Africa's economic decline exactly because the theory of comparative advantage cannot be operationalized since this would require a number of unworkable assumptions to be met. For example it cannot be assumed that all producers across countries use the same technologies, that technological mastery is unproblematic, or that there are constant returns to scale, or that there is full employment.

It is against this background that when such programmes have been put into practice in Africa, the result has been de-industrialization and immiserization. As stated in the study, the abstract models of comparative advantage do not capture the current complexity of global competition, but that it is the competitive advantage which is dependent on the acquisition of technological capabilities that matters. How can this be brought about? This can only be

effectively built through regional cooperation, which can in turn be used to influence the nature of African economies' insertion into the global market. The measures underway to strengthen regional economic cooperation at sub-regional levels as well as at pan-African level in the context of African Economic Community (AEC) should be accorded all the premium priority they deserve. This would be the fourth prerequisite for building up technological capabilities.

The fifth prerequisite is to invest in the development, maintenance and improvement in the basic physical infrastructural facilities that would assist in the process of economic integration and development. The poor infrastructural facilities add to the cost of production and undermine the competitiveness of the African economies. It is in this context that the provision for adequate and well functioning roads, railways, ports, telecommunications, energy and water facility systems become crucial in the industrialization of the African economies. Without these facilities the prospects of moving the African economies into the next stage of economic development will remain extremely remote. The role of these infrastructures in development need not be overemphasized. The governments must therefore take it upon themselves to make the necessary investments to facilitate their adequacy and smooth operation.

In conclusion, it can be observed that the five prerequisites amongst others, would provide proposals around which policy formulation could be organized. Indeed, Africa's own relative economic insignificance in the global economy should make it a lot easier for the countries of the region to bargain collectively for a more practical programme that takes into account their present level of development.

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