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Legal Imperatives for Effective Transnational Investment Under the World Trade Organization – A Focus on Africa

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Abstract

The establishment of the WTO heralded a multilateral international institution with a global face. The existence of WTO has led to the liberalization of international trade and investment. The WTO also has well-structured institutions to ensure economic globalization and enforcement of trade regimes amongst member States. This paper has as its aim to examine the role of the World Trade Organisation (WTO) in the promotion of international trade and investment in emerging African economies. The objectives of this paper amongst others include to appraise the historical background of the limitations and constrains of international trade prior to the establishment of the WTO. However, the mistrust and lack of ability for States to put their economic difference aside has stalled trade negotiation rounds. The polemics between developed and developing member States have led to a proliferation of regional economic organisation which policies sometimes run foul with that of WTO. This has the potential of weakening the impact of WTO. The doctrinal research methodology was adopted in this paper as both the primary and secondary sources of law were relied upon. This paper found that the trade relations between emerging economies in Africa is greatly increasing primarily because of the impact of globalization and liberal policies being vigorously pursued by many economies. This paper recommended that for WTO to continue to be effective and not lose its relevance, it must continue to assure its member States, especially the developing countries, of having their interest at heart by ensuring that it does not just promote free but fair trade.

Keywords: WTO, International Trade, GATTs, Most Favoured Nations.
JEL Classifications: E12, E13, E14

1. Introduction

International law largely recognizes the sovereignty of States over their internal affairs. States also exercise unfettered authority over their domestic jurisdiction.[2] These principles are so important and generally recognized in international law that they have gained the prominence of international customary law significance. Consequently, States take full charge and determine what happens within their territory through the exercise of territorial sovereignty. The *stricto senso* application of the above principles of international law would mean that it becomes impossible to achieve what is referred to as international committee of nations. Hence, States have to give away certain percentage of their sovereign right in order for things to work.[3] This is more necessary, as no state

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[2] H G Schermers and N M Blokker, *International Institutional Law* (5th Rev. Ed, Leiden: Martinus Nijhoff Publishers, 2011) 4 - 5

[3] P G Adogamhe, 'Pan-Africanism Revisited: Vision and Reality of African Unity and Development' (2008) 2 (2) *African Review of Integration*, 3.

is an island of itself. For international organizations such as United Nations and the other to be formed, this compromise is required. In fact, the lack of this compromise was largely responsible for the failure of the League of Nations. Narrowing it down to the aspect of trade, States exercise economic sovereignty by determining and controlling the trade within its territory. States determine the kind of goods that come in and out of their territory. A state may decide to seal its borders to prevent any goods from come in or go out of its territory. This had been the economic stance of China and so many communist nations, as they had viewed the importation of foreign goods into their territory as alien incursion, infiltration and adulteration of their uniqueness. The result had been the trade barrier that existed between nations. The down side of this was that States don't get to take benefit of their comparative advantage. There were scarcity and unavailability of certain commodities in the market of States.

The challenge necessitated the removal of trade barriers between States. At first, States have entered into bilateral trade treaties between themselves. This ameliorated the situation to some extent as it established international trade. However, for international trade to develop at a wide scale there was the need for the formation of international organisation through the plurilateral and multilateral treaties. Attempts in this regard after the 2nd World War never yielded result with the failure of States to agree to terms in the formation of International Trade Organisation (ITO). That notwithstanding, a group of States were able to reach a General Agreement on Trade and Tariffs (GATT) in 1947. GATT acted as a place holder and template regulating international trade among signatory parties until the formation of World Trade Organisation (WTO) in 1994[4] during the Uruguay Rounds to replace GATT. In the WTO commissioned Sutherland Report of 2004 it was observed thus:

> In committing to the WTO and its procedures and disciplines, governments are returning to themselves a degree of 'sovereignty' lost through the process of globalization. If governments are losing the capacity to regulate meaningfully at the domestic level, they are reclaiming some control of their economic destinies at the multilateral level.[5]

No doubt, the establishment of WTO has been a great achievement for international trade due the liberalisation of trade and removal of barrier and tariffs that came with it. However, this has not been achieved without challenges. In as much as WTO has played prominent role in boosting international trade and investment and establishment of globalisation, there is still much to be desired.

One of the important characteristics of evolving globalization is the marked increase in world output and trade. Rapid global integration has led to significant economic expansion, notably in industrialized countries, but also in developing countries with outward-oriented economic and trade policies. During the l990s world output expanded at an average annual rate of 2.9 percent, while trade grew by 6.0 percent. For developing countries as a group, relative to the world as a whole, the rate of output growth was much higher at 5 percent. Asia, as a region, recorded an even higher average annual growth rate of 9 percent. Africa,

[4] The organisation became effective from 1st January, 1995.

[5] H G Schermers and N M Blokker, *International Institutional Law* (5th Rev. Ed, Leiden: Martinus Nijhoff Publishers, 2011) 4 - 5

on the other hand, lagged far behind other regions with a growth rate of about 2.3 percent.[6] With respect to trade, during the same period, the export and import volumes of developing countries grew at a much higher rate than the global average, with several Asian countries recording double-digit growth rates.

It is well known and empirically documented that the rapid expansion in global trade occurred in response to countries' increasing acceptance of openness. Other major contributing factors include the decrease in the unit costs of transport and information technology, including telecommunications; and the globalization of production, with industries moving to areas offering opportunities for lower production cost. The liberalization of global trade has taken many forms, including nondiscriminatory unilateral liberalization, multilateral liberalization, and liberalization in the context of trading blocs (free-trade areas, customs unions, and common markets).[7]

A marked feature of the distribution of the benefits from globalization and liberalization is that the lion's share has gone to those countries and regions that sustained outward-oriented trade and economic policies. In contrast, just a portion of the gain has accrued to countries with weak performance in reform and tenuous links to the global trading system. However, the rising isolation and marginalization of many countries, mostly in the developing world and particularly in Africa, have also been exacerbated by the protectionist policies in industrial countries. These have erected barriers and have constrained market access to the basic commodities produced by developing countries, thus circumscribing the comparative advantage of these countries in global trade.[8]

With specific regard to the continuing marginalization of Africa in the global economic arena, it is important to highlight the structural rigidities of production and the economic environment that have prevented the continent from taking advantage of globalization. First is the significant shift in the composition of global exports away from basic commodities toward manufactures, clearly an area where Africa does not currently enjoy comparative advantage. Second is the rapidly expanding intra-firm and intra-industry trade - an important indicator of the globalization of production. Here also, since Africa's share in global production has been declining, it has been unable to share in this fast-growing aspect of global trade. Third is the rising share of trade in services, which is expanding even faster than trade in goods. Fourth is the balkanized structure of African markets, notwithstanding the creation and existence of several regional integration arrangements.

The establishment of a number of regional economic communities has not led to the creation of large and effective trading blocs with effective, sizeable markets, sufficient to produce scale economies and competition. Last, even though the past decade has witnessed

[6] R J Barro and Others, *Economic Growth* (New York: McGraw-Hill 1995)

[7] L Chia and S Gayi, 'Trade Diversification in Benin: Prospects and Constraints' in C K Patel and S Gayi (eds.), *Trade Diversification in the Least Developed Countries* (Cheltenham, England: Edward Elgar Publishing 1997).

[8] P Collier, 'Africa's External Economic Relations: 1960–90' [1991] (90)(360) *African Affairs*; 339–56.

the expansion of worldwide flows of foreign direct investment (FDI), Africa's share in these flows has been minuscule.[9]

The thesis of this paper is that for Africa to end its global isolation and marginalization and become an important beneficiary of the fast-expanding global trade, the continent must implement appropriate economic and institutional reforms, create large and effective markets with links to the global economy, diversify the agricultural base, and engage in value-added processing of primary products. Successfully implementing the NEPAD agenda and strategy for Africa's development will go a long way toward enhancing Africa's global competitiveness and create an environment conducive for growth and poverty reduction.

2. Regional Integration in Promoting Trade in Africa

By increasing trade and investment, economic cooperation and regional integration create opportunities to reap the gains from globalization. For Africa, a region characterized by small and balkanized States and markets, economic cooperation and regional integration have the potential to create an expanded and unified market, diversify the economic base, and increase competitiveness in the global market. Open regionalism, with expanding regional trading blocs coexisting alongside the global integration of markets, has spurred growth and development in many parts of the world. This is a phenomenon from which Africa stands to gain.[10]

Over the past four decades, Africa, in an attempt to forge political unity and expand markets, has established several regional economic communities. Today the continent's economic and political blocs range from preferential free trade areas, to customs unions, to monetary unions. The main advantages expected from these organizations fall into two broad categories. First, the political benefits include the following:

- Fostering continental unity and development
- Promoting peace and growth with neighbors, thus reducing the prospects of conflicts among members
- Facilitating and deepening the exchange of information among democratic neighbors
- Strengthening regional security through its stabilization effect.
- Second, economic benefits anticipated from African integration institutions include
- Mitigating the economic disadvantages of fragmentation and reducing the attendant constraints on growth and development
- Promoting industrial growth and creating synergy through exploiting the complementarity of the region's economies
- Raising income through innovation and growth
- Promoting growth through increased factor productivity
- Creating trade and avoiding trade diversion.

[9] D Dollar, 'Outward Oriented Developing Economies Really Do Grow More Rapidly: Evidence From 95 LDCs, 1976–86' [1992] (40)(3) *Economic Development and Cultural Change*; 523 - 44.

[10] R Medhora, 'Lessons from UMOA' in R. Lavergne (ed.), *Regional Integration and Cooperation in West Africa: A Multidimensional Perspective* (Ottawa: International Development Research Consortium 1997); Z Iqbal, and M S Khan, *Trade Reform and Regional Integration in Africa,* (Washington: International Monetary Fund 1998).

Driven by the desire to reap these benefits from integration, African leaders and governments have created several regional economic communities and trading blocs. In West Africa, for example, the integration arrangements include the Economic Community of West African States (ECOWAS), comprising 15 countries in the sub region; the West African Economic and Monetary Union (WAEMU), consisting of 8 francophone West African countries with a common currency, the CFA franc; and the Mano River Union, comprising Liberia, Sierra Leone, and The Gambia.[11]

In Eastern and Southern Africa, the major integration schemes include the Common Market for Eastern and Southern Africa (COMESA), the Southern African Development Community (SADC), and the Indian Ocean Commission. In Central Africa, there are the Economic Community of Central African States, the Economic and Monetary Community of Central Africa (CEMAC), the Central African Economic Community (CAEMC), and the Economic Community of the Great Lakes Countries. And in North Africa there is the Arab Maghreb Union (AMU). In addition to these intergovernmental integration arrangements, there are several activity-based organizations, such as the Cross-Border Initiative, the Club du Sahel, and the Committee for Drought Control in the Sahel. Today many African countries belong to more than one regional integration scheme. However, it is worth noting that several of these integration schemes have duplicate and overlapping mandates and are very poorly funded. Appendix I shows the evolution of these trading arrangements, and Appendix II highlights the degree of overlap in membership in these organizations.[12]

2.1 Overview of Achievements of Intra-African Trade

Measured against the anticipated gains, the results of Africa's integration efforts can, at best, be described as mixed. It can be claimed that membership in sub regional organizations affords member countries opportunities to cooperate and promote good neighborliness. The Organization of African Unity, recently transformed into the African Union, serves as a forum for African leaders to exchange views on matters of common interest to the continent. The existence and achievements of the ECOWAS Monitoring Group, established to prevent, manage, and resolve conflicts, point to the political benefits that can be realized from cooperation among African countries. There has also been some progress in facilitating the regional mobility of labor, particularly in the ECOWAS sub-region, where a common travel document permits nationals of one member country to enter the other member countries without visa requirements. COMESA and CAEMC have also introduced regional passports, which allow nationals of each member country entry into the other countries without visas.

The results have also been mixed in realizing the economic benefits from integration. The assessment of monetary integration efforts is generally positive. Studies of the Communaute Francophone d'Afrique (CFA), for example, Medhora (1997) and

[11] Medhora (n 5)

[12] F Nigel, and A Yeats, 'Open Economies Work Better! Did Africa's Protectionist Policies Cause Its Marginalization in World Trade?' World Bank Policy Research Working Paper No. 1636 (Washington: World Bank 1996).

Guillaumont,[13] cited in the former, find that the growth performance of its members was better than for the nonfrancophone zone. Symbolizing deeper integration, the WAEMU sub-region's cooperation has extended beyond traditional trade integration to encompass the integration of fiscal, judicial, and monetary management in addition to establishing a functioning compensation trust fund. The zone has also demonstrated some of the benefits and challenges of an integration arrangement involving industrial countries. Under the association arrangements, the zone has been receiving assistance through France in the form of institutional capacity development, budgetary support for fiscal control, and monetary management.

There has also been some experience in monetary cooperation in southern Africa. The level of trade and financial transactions conducted with the South African rand points to the potential benefits that could be realized from the existence of an effective rand area within the Southern African Customs Union. Some analysts believe that the existence of, and perceived benefits from, these functioning monetary zones are instrumental in the current drive to establish a second monetary zone in the ECOWAS sub-region.

2.2 Formation of the WTO

After the World War II the World Bank and the International Monetary Fund (IMF) were created as international financial institutions. It was intended that a third institution be created to regulate the trade aspect of international economic cooperation among nations. More than fifty countries were part of the negotiations to create International Trade Organisation (ITO) as a specialised organ of the United Nations. The scope of the draft ITO Charter included rules on employment, commodity agreements, restrictive trade practices, international investment, and services. The target had been the creation of ITO at a UN Conference on Trade and Employment in Havana, Cuba in 1947.[14]

Meanwhile, 23 countries had entered into trade negotiations in Geneva in 1947. The agreement was known as the General Agreements on Trade and Tariffs (GATT) and was to come into force on 1st January, 1948. The agreement aims to remove the use of import quotas and to reduce tariffs on goods. GATT was not to be a permanent agreement. However, it continued to hold sway as the major multilateral agreement governing international trade for over 45 years until the establishment of WTO. It was also not an international trade organisation. Yet it gathered approximately 130 signatory parties into the system. GATT continued to extend through various negotiation rounds, supplementary codes and arrangements, interpretations, waivers, reports by dispute-settlement panels and decisions of its council.[15]

Signatory States of GATT took a long walk to form the WTO. This happened in the Uruguay Round of negotiations that lasted from 1986 to1994. The Round was finally completed on 15 April, 1994 wherein 111 out of the 125 participating States signed the final document. 104 States accepted it and it came into force on 1st January, 1995 for eighty-one members which reflected more than 90

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[13] J D Sachs and A M Warner, 'Sources of Slow Growth in African Economies' [1997] (6) *Journal of African Economies*; 335–76.

[14] G A Solanki, 'Globalization and Role of WTO in Promoting Free International Trade' (2012) 3 (1) *Journal of Humanities and Social Science*, 13.

[15] K Anderson, 'World Trade Organization (WTO)' (2010) *Encyclopaedia Britannica Student and Home Edition.* Chicago: Encyclopaedia Britannica.

per cent of international trade. Apart from its success in creating WTO, the round also enlarged the scope of multilateral agreements regulating trade and ensured institutional restructuring. It is also credited to have concluded the General Agreement on Trade in Services (GATS) and the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) thereby bringing services and intellectual property under the regime of multilateral agreements. It also replaced the 1948 GATT with the 1994 version. In replacing GATT, WTO aims to create equitable trade conditions and fairer environment for goods and services to allow the free flow of trade. It recognises the importance of aligning the structural imbalanced economic conditions.[16] WTO was established to ensure substantial reduction of tariffs and other barriers to trade and to the elimination of discriminatory treatment in international trade relations.[17]

2.3 Africa's Share of World Output

During the periods of 1986 to 1993 and 1993 to 2003, the industrial economies was projected to grow at about 3 percent, while developing countries will grow at 5 percent. Developing Asia has been the most dynamic of the developing regions; over 1984–93 the region recorded an annual GDP growth rate of 7.6 percent. The region is projected to grow at 6.8 percent a year for the 10-year period 1994–2003. Comparable figures for Africa are 2.0 percent and 3.4 percent, respectively. Africa's average annual growth rate of about 3.2 percent from 1997 to 2001 made it the third most dynamic region in terms of GDP growth, after Asia and the Middle East.[18] Even though Africa has recovered from a very severe economic contraction during the 1980s, there is still much unused productive capacity. Moreover, to reduce the currently widespread poverty over the next 10 years, Africa must achieve an annual growth rate of about 7 percent if it is to attain the UN Millennium Development Goal of reducing poverty by 50 percent by 2015.

2.4 Africa's Trade Performance

Africa's trade performance shows long-term decline in its competitiveness and share in global trade. It is apparent that Africa is the only region to have experienced a steady decline in its share of global exports over the period 1985–2000. During this period, the value of the region's exports declined by about 50 percent. Imports also declined, from 2.8 percent of world imports in 1985 to a low of 1.8 percent in 1996, rising only marginally to 2 percent in the year 2000. These figures contrast sharply with those posted by other regions. For example, Asia and North America each accounted for nearly a fifth of world exports and imports over the period, while Europe accounted for almost half of total world exports and imports. Between 1997 and 2001, Africa's share in global investment flows also declined by about 44 percent (to $5.3 billion from $9.4 billion). In 1996, Africa's share of total FDI to developing countries was only 2 percent (UNCTAD, 2001). The loss of market share by Africa for its major commodity exports over the last three decades is

[16] T B Ayres, 'The Role of the WTO in Assisting Developing Countries, Especially the BRICS: An Analysis of Doha and Bali' (2015) 3 *Law School International Immersion Program Papers,* p. 1.

[17] See, the Preamble to the WTO Establishment Agreement.

[18] K Schwab and C Smadja, 'Power and Policy: The New Economic World Order' *The Evolving Global Economy* (Boston: Harvard Business Review Book 1995); A Vamvakidis, 'Regional Integration and Economic Growth' [1998] (12)(2) *World Bank Economic Review*; 251–70.

estimated to have caused annual revenue losses of about $11 billion in 1996 prices (Ng and Yeats, 1996).[19]

3. Intra-African Trade

AMU imports from the WAEMU, for example, averaged about 1.36 percent over the period under consideration, while the WAEMU in turn imports mainly from ECOWAS and the franc zone. Intraregional exports of SADC, ECOWAS, and WAEMU do not differ much from intra-exports.

3.1 Constraints on Regional Integration and Intra-African Trade

Several factors limit the size of intra- and inter-African trade. First is a lack of the structural complementarities necessary for trade creation. Second, Africa's restricted industrial base offers limited scope for economies of scale in production and marketing. Third, the continent's poor and inadequate infrastructure limits trade and raises the cost of the little merchandise that is eventually traded. This, in part, accounts for the high level of informal trade, which is often confined to the common borders of adjacent countries. Fourth, the absence of compensatory mechanisms discourages trade liberalization reforms because of the fear of losing revenue. Similarly, the multiple and overlapping regional trading arrangements, each with its common external tariff, have hindered rather than enhanced trade. Finally, the small size of the trading blocs severely limits economies of scale. Under such circumstances, imports from outside the bloc, most notably from Europe, are encouraged and preferred.[20]

(a) Africa in the Multilateral Trading System

In addition to unilateral actions, there is a pressing need for the multilateral trading system to become equitable and evenhanded. The following paragraphs highlight the strengths and weaknesses of the current multilateral trading system. The World Trade Organization (WTO) was created in 1995 to oversee the General Agreement on Tariffs and Trade (GATT), which had guided rules of international trade since 1947. The GATT's role was to codify and record a series of tariff reductions that its members wished to make, and provide a structure to give credibility to those reductions. A key concept of the GATT, which underpins the present global trading system, is nondiscrimination between different sources of the same imported good. This is achieved by requiring members to give each other "most favored nation" treatment, except in specified circumstances. In addition to administering the GATT's rules, the WTO has far-reaching powers. It requires member countries to subscribe to virtually all its rules rather than allowing them to treat some as optional. To be effective, the WTO must proceed by more or less requiring consensus.[21]

The WTO can enhance the economic well-being of developing countries in four ways. First, if enough members wish, it can organize periodic rounds of tariff negotiations (such as Seattle and Doha). These offer opportunities and incentives to reduce their barriers to

[19] World Bank, *Trade Blocs* (New York: Oxford University Press 2000).
[20] A J Yeats, 'What Can Be Expected from African Regional Trade Arrangements? Some Empirical Evidence' (Unpublished; Washington: World Bank 199).
[21] B Hoekman, 'Trade and the SDGs: Making "Means of Implementation" A reality'' Commonwealth Trade Hot Topics 128. London: Commonwealth Secretariat 2016

trade. Second, it provides support for domestic policy, including providing informational support to members in debates over trading laws. Third, it can protect the rights of members against certain violations of the rules by other members (through court decisions and penalties). And fourth, it provides a forum and mechanism for governments to manage the spillovers from members' trade policies onto their partners. These four avenues provide the framework for assessing the WTO's current rules about regional integration arrangements. This framework is spelled out in GATT Article XXIV (for goods). An "enabling clause" introduced in 1979 significantly relaxes the conditions for creating regional integration arrangements that include only developing countries.[22]

Notwithstanding good intentions, the application of GATT–WTO rules has not been evenhanded. While giving notional support to open trade, the industrial countries and their regional trading arrangements maintain restrictive policies that deny access of goods from developing countries. These restrictions prompted Michael Moore, the Director-General of the WTO, to argue at the 2000 United Nations Conference on Trade and Development that richer nations need to bring down trade barriers to exports from developing countries. He said, "It makes no sense to spend extra billions on enhanced debt relief if, at the same time, the ability of poorer countries to achieve debt sustainability is impeded by lack of access for their exports." Echoing similar sentiments in a recent presentation to the WTO, Wiseman Nkuhlu, Chair of the NEPAD Secretariat, reiterated the need for open access for African goods to the markets of industrialized countries, particularly for those agricultural commodities in which the continent has comparative advantage.[23]

(b) Bilateral Initiatives to Promote African Trade

Arising out of concern for the continued marginalization of Africa since the mid-l990s, several multilateral and bilateral initiatives have emerged. If exploited, these could enhance the economic growth of the region and contribute to reducing its gaping poverty.

As part of United States general policy to support Africa's development, *African Growth and Opportunity Act (AGOA* provides duty-free access to U.S. markets for products originating from African countries. The central goal of the Act is that trade could reduce Africa's aid dependency. AGOA-based duty-free eligibility is qualified on several conditions. This includes a determination of progress toward establishing a market-based economy, rule of law, and political pluralism; elimination of barriers to U.S. trade and investment; protection of intellectual property; efforts to combat corruption; policies to reduce poverty; increased availability of health care and educational opportunities; protection of human rights and worker rights; and elimination of certain child labor practices.

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[22] M Razzaque, and J Keane, *Delivering Inclusive Global Value Chains* (International Trade Working Paper London: Commonwealth Secretariat 2016) <http://www.oecd-ilibrary.org/docserver/download/5jm2jfd5xfmv- accessed 17 May 2020

[23] G A Calvo, and E G Mendoza, 'Rational Herd Behavior and the Globalization of Securities Markets' *Discussion Paper*, 120, Institute for Empirical Macroeconomics, Federal Reserve Bank of Minneapolis, August 1997

As of January 2002, 34 African countries had been certified as meeting the criteria to export to the United States free of quotas and duty for several items.[24] It is too early to measure the impact of AGOA on Africa's access to and participation in global trade, particularly regarding effective access to the U.S. market. It is, however, significant that there is an element of policy lock-in in AGOA since qualifying countries have to meet some reform benchmarks.[25] The Cotonou Partnership Agreement reolaced the Lome Partnership Agreement among African, Caribbean, and Pacific (ACP) States and the European Union was signed in Cotonou, Benin, in 2000. The new agreement covers 77 countries, 48 of which are in Africa, and aims to promote the economic, cultural, and social development of the ACP States with a view to enhancing peace and security and to promoting a stable and democratic political environment. In part, a specific objective of the agreement is to integrate the ACP economies into the world economy, leading to the stimulation of growth and reduction of poverty. The new partnership agreement, the ACP–EU Convention, has four main components viz:

- Reinforcement of the political dimension of relations between ACP States and the European Union
- Poverty reduction within the context of the objectives and strategies agreed at the international level
- An economic and trade cooperation framework
- Rationalization of financial instruments and a system of "rolling programs."

The new agreement's main objective is to promote the progressive integration of the ACP countries into the global economy by enhancing production and the capacity to attract investment and ensuring conformity with WTO rules. The new approach emphasizes trade liberalization, including the adoption of transparent competition policies, the protection of intellectual property rights, and standardization and certification.

3.2 The New Partnership for Africa's Development

NEPAD was formulated by African leaders to meet the mounting challenges facing the continent in an era of globalization, whose trade and growth benefits have so far eluded the continent. It comprises a vision for Africa's development, measurable development objectives, and a strategy for attaining these objectives.[26]

3.3 Importance of Regional Integration

A guiding principle of NEPAD is the need to accelerate and deepen regional and continental economic cooperation and integration. Referring to the challenges of globalization, the official document launching NEPAD recognizes that "an effectively managed integration presents the best prospect for future economic prosperity and poverty

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[24] B Eichengreen, *Toward A New International Financial Architecture: A Practical Post-Asia Agenda* (Washington, DC, Institute for International Economics (IIE) 1999); M Feldstein, 'Refocusing the IMF' [1998] (77)(2) *Foreign Affairs*; 268

[25] V Fitzgerald, 'Global Capital Market Volatility and the Developing Countries: Lessons from the East Asia Crisis' *Centro d'Agliano–Queen Elizabeth House Oxford, Development Studies Working Paper*, 124, December 1998.

[26] S Knack and P Keefer, 'Investment and Economic Performance, Cross-country Tests Using Alternative Institutional Measures' [1995] *Economics and Politics*, 7; S Manzocchi, *Foreign Capital in Developing Economies. Perspectives from the Theory of Economic Growth* (London, Macmillan 1999)

reduction." It asserts: "The integration of national systems of production has made it possible to slice up the value chain in many manufacturing and service sector production processes. At the same time, the enhanced mobility of capital means that borrowers, whether governments or private entities, must compete with each other for capital in global rather than national markets." NEPAD leaves no doubt about recognition of the opportunities from globalization and the role that regional integration can play in facilitating Africa's ability to convert these opportunities into growth, development, and poverty reduction.[27] As the initiative evolves from a conceptual debate to programs to implementation, joint action will be needed on Africa's shared problems. Events in one country have implications for its neighbors. Action on the following critical regional imperatives will go a long way in reducing, if not ending, African marginalization:

- Strengthening the mechanisms for conflict prevention
- Promoting and protecting democracy and human rights in member countries and within sub-regions
- Restoring and maintaining macroeconomic stability, at the country and regional levels
- Establishing transparent legal and regulatory frameworks
- Promoting infrastructure development and common approaches to the provision of regional public goods

NEPAD programs provide many opportunities to deepen regional integration and bring dynamic gains from integration. A successful implementation of NEPAD's Market Access Program will ensure that Africa's interests are adequately addressed through the WTO. Furthermore, NEPAD's designation of the sub-regional integration organizations as focal points for implementing NEPAD programs has laid a solid foundation for market integration. This not only will strengthen regional integration in Africa, but also could well create the groundswell needed to achieve the aspirations of the African Economic Community - the creation of an Africa-wide customs union.[28]

3.4 Africa's Recent Integration Efforts

There is an extensive theoretical and empirical literature on the relationship between globalization and the expansion of world trade. A major conclusion is that free trade matters for growth. Several studies find a positive relationship between free trade and growth during the past two decades (Dollar, 1992; Edwards, 1992; Levine and Renelt, 1992; Barro and Sala-i-Martin, 1995; Sachs and Warner, 1997; and Vamvakidis, 1998).

Although most of the empirical findings are based on evidence from countries that liberalized trade unilaterally, ample evidence also shows that the structure of regional integration arrangements and their relationship with the rest of the world influence the distribution of growth. An unequivocal conclusion is that most developing countries in Africa have been bypassed by the benefits of globalization. Africa's share in global trade and growth has declined since the 1970s, notwithstanding numerous integration schemes. Measured by its share in global output and trade as well as the level of inter-African trade,

[27] D North, 'The Contribution of the New Institutional Economics to an Understanding of the Transition Problem' *UNU/WIDER, Annual Lecture,* 1 1997

[28] D Rodrik, *Has Globalization Gone Too Far?* (Washington, DC, Institute for International Economics 1997)

the continent has made little if any progress.[29] Several reasons have been put forth to explain Africa's poor trade and growth performance. These include

- The lack of a conducive macroeconomic environment, resulting from poor reform performance
- The structure of Africa's production and the lack of complementarity among its economies
- The absence of political stability

The small size of regional integration schemes and their inclusion of developing countries only. This structure of African integration schemes and their concentration on the expected static gains from trade have been identified as a major impediment to the growth of trade and development. This arises from the dominance of primary products in African exports and the inherent and long-standing hub-and-spoke trading arrangements between the continent and its most important trading partner, the European Union. Given the underdevelopment of industry in Africa, the exchange has remained the same—Africa exports primary products and imports finished goods. Consequently, on the basis of the traditional concepts of trade creation and trade diversion, most of Africa's regional integration arrangements cannot generate welfare benefits because the necessary conditions do not exist.

4. Conclusion

In their efforts to overcome the development constraints imposed by the small size of their national economies, African governments have created regional integration schemes. These vary from free trade arrangements to customs unions to common currency zones. Ideally, these schemes should have facilitated integration by creating larger markets with opportunities for economies of scale in production, competition, enhanced investment inflows, and economic growth. The findings of several studies, including this analysis, have shown that integration schemes in Africa have not achieved the expected results. The African economies remain small and not integrated; and in a fast-globalizing world, Africa remains the most isolated and marginalized region. This paper suggests that Africa can achieve better integration results and end its global isolation through several measures. Critical among these is the need for consistent implementation of sound macroeconomic policies and the rationalization and transformation of African integration blocs into effective, open, and large markets that will serve as stepping stones for the global integration of Africa. In addition, Africa needs a stable, conflict free environment if it is to attract and retain investment, particularly FDI, whose global mobility has spurred economic development and growth in other parts of the world during the past two decades. NEPAD's objectives and programs for Africa's development could not have come forward at a better time. The challenge is to transform these programs into actionable development activities and commence their implementation.

[29] A Swoboda, 'Reforming the International Financial Architecture' [1999] (36)(3) *Finance and Development*; A Swoboda, 'Beyond Bretton Woods: What International Monetary and Financial System for the Twenty-first Century?' (2000)

Best efforts notwithstanding, Africa will realize little progress towards ending its isolation unless developed countries remove their current trade barriers, which have circumscribed the comparative advantages that African products would have otherwise enjoyed in these markets. There is a pressing need to make the multilateral trading rules, which are currently biased against primary products, more equitable and evenhanded. In this regard, the NEPAD market access program provides a useful agenda with which to promote African trade.

5. The Way Forward

To realize dynamic gains, it is argued that integration schemes in Africa must involve deeper integration that will link countries in a mutually beneficial relationship and create a positive synergy from coordinated reforms. In addition to traditional trade integration, this would entail coordinating several policies that have traditionally been viewed as domestic—that is, competition policy, commercial legislation and regulation, investment and tax codes, monetary policy and the creation of a common currency (as exists in the CFA zone), environmental regulation, infrastructure development, labor mobility, product standards, and standards on training and skills certification.

The benefits from regional coordination of reforms in these areas include greater efficiency of resource allocation and production, enhanced prospects for larger investment inflows, technology transfer, and building trust among countries. Several writers,[30] have argued that these benefits are more likely to be realized in an integration arrangement that includes industrial countries because of the prospects for increased investment flow and technology transfer. Above all, it has been argued with cases cited that the former type of trading arrangement is more likely to provide effective restraint, or a policy lock-in mechanism, than the later. It is less clear that industrial countries will be willing to enter into integration arrangements that will confer these anticipated benefits. For their part, developing countries may very well view such arrangements as a backdoor approach to re-colonialization.

Efforts should be made towards trading arrangement including industrial countries is founded on strong partnership initiatives—such as NEPAD or a supranational customs union like the African Economic Community there is a chance of mutual benefits to both regions. The current EU approach of entering into multiple bilateral arrangements with countries with varying trading conditions is unlikely to benefit Africa.[31]

Regardless of the polar relationship in an integration arrangement, the literature on regional integration and the need for policy coordination and harmonization has received wide attention. This is because a contradictory policy stance in one member country can negate the expected outcome in another in the absence of effective regional coordination. For

[30] United Nations, Towards a New International Financial Architecture, Report of the Task Force of the Executive Committee of Economic and Social Affairs, (LC/G.2054), Santiago, Chile, ECLAC, March (1999)

[31] O Krugman, 'Financing vs. Forgiving a Debt Overhang' [1988] (29) *Journal of Development Economics*, 29, pp. 253–68.

instance, as Badiane,[32] observed, in West Africa trade liberalization yielded far poorer outcomes than expected because macroeconomic policy reforms and coordination were not uniformly pursued. A case in point was the revaluation of the Nigerian naira during the early 1990s at about the same time the CFA franc was being devalued. Similarly, Ernest Aryeetey, professor at the University of Ghana, observed that the Ghanaian cedi was allowed to appreciate at about the same time as the CFA franc was being devalued. The importance of a deeper and better-coordinated policy stance, including trade liberalization, can hardly be overemphasized.

There is a growing interest in monetary integration in Africa, even though the interest is not widespread and the implications are not thoroughly understood. Although not a common feature of integration arrangements, monetary integration has several advantages as well as drawbacks. As Aryeeteym[33] points out, when coupled with trade integration, monetary integration will contribute to maximizing intraregional flows because the common currency removes the transaction costs implied in using different currencies. It will also economize on the use of foreign exchange by eliminating its use in intraregional trade. Furthermore, a single currency is likely to promote efficiency through the removal of capital controls and introducing price stability with exchange rate stability. However, inherent risks and costs. Monetary integration is not feasible until there has been a convergence in macroeconomic indicators in the integrating countries. Another disadvantage lies in the loss of the exchange rate as a policy instrument since adjustments can only be undertaken using expenditure-reducing measures. This handicap may be more than offset by the budgetary discipline entailed in monetary integration. The other costs of monetary integration are the loss of the inflation tax and seigniorage and the difficulty in having an autonomous monetary policy.

The discussion on integration and trade has thus far focused on economic issues and relationships. A necessary condition for regionalization is peace and security or, more generally speaking, stability. Political stability is imperative for a nation's ability to attract and keep investment. Regional stability is essential for trans-border investment in infrastructure and telecommunications, which hold the key to industrialization in an era of linked borders and markets. For years, if not decades, African countries have faced internal conflicts that have had severe cross-border spillovers. A region with so many conflicts will not attract FDI away from more stable regions. Thus, if Africa is to stimulate trade and growth, stability must return. In sum, political and economic factors intertwine in regionalization. The challenge is to adapt African integration arrangements in ways that would stimulate dynamic gains, coordinate and sustain deep reforms, and strive toward stability in member countries and the region.

[32] O Badiane, 'National Policies and Impediments to Regional Economic Integration' in R Lavergne (ed.), *Regional Integration and Cooperation in West Africa: A Multidimensional Perspective* (Asmara, Eritrea: Africa World Press 1997).

[33] E Aryeetey, 'Sub-Saharan Experiences with Regional Integration' in Z Iqbal and M S Khan (eds.), *Trade Reform and Regional Integration in Africa*' (Washington: International Monetary Fund 1998).