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ABSTRACT

Asymmetric Regionalism in Sub-Saharan Africa: Where Do We Stand?*

The Paper reviews the likely economic effects of the Regional Economic Partnership Agreements (REPAs) proposed by the EU to the ACP countries to succeed to the Lomé IV agreements. We argue that, in spite of some likely positive effects because of reciprocity and the North–South partnership, the pronounced asymmetries among the Southern partners will lead to strong redistributive and marginalization effects that will require compensations that are likely to be costly to implement. It is also pointed out that efforts at regional cooperation agreements would avoid some of the shortcomings associated with the proposed discriminatory trade preferences that would accompany the proposed REPAs. And if the REPAs are negotiated, they should be accompanied by compensatory transfers from the EU for tax revenues losses attributable to the agreements.

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NON-TECHNICAL SUMMARY

The European Commission has recently proposed to put EU–ACP trade relations on a reciprocal basis for those ACP (Africa, Caribbean and Pacific) countries wishing to enter into a Regional Economic Partnership Agreement (REPA) with the EU. This proposal for cooperation (to become Lomé V if it is carried out) is to replace Lomé IV. The 'new' elements in the REPA approach to cooperation are: (i) reciprocity in the trade relations between the EU and the ACP countries: an element that was supposed to be present in their trade relations early on, but was abandoned; (ii) encouragement of prior RIAs among the countries that would enter REPAs, for example the UEMOA and Ghana would be encouraged to form an FTA (and encouragement for all ACP to join the WTO); (iii) a preferential trading arrangement (with about 80% to 90% of bilateral trade between the EU and REPA would be abolished over a ten year period (2005–15) with REPA members allowed to 'backload' their reforms, postponing the main tariff reductions until the end of the period.

Drawing on recent work evaluating the regional approach to trade (and other) policies at the theoretical and empirical levels, the Paper takes a critical look at this new proposal for cooperation from the point of view of the ACP countries, whose alternatives, as members of the WTO, are essentially a reliance on non-discriminatory trade policies based on a combination of unilateral and multilateral trade liberalization.

Stage effects. The proposal is to achieve the new form of cooperation in two stages, the first stage involving regional FTAs among the ACP countries. Concerning the first stage, the standard Vinerian analysis of preferential trading arrangements suggests that the potential for trade creation of these regional FTAs is low as these countries have very similar patterns of trade, importing and exporting similar goods. These characteristics imply a very substitutable pattern of trade, which raises concerns of relatively large trade diverting effects of these FTAs.

By and large, the second stage provides one-way market access for EU exporters in ACP markets. Indeed, ACP countries pretty much have zero-duty market access into the EU for manufactures and non-sensitive agricultural products, sensitive agricultural products being, at this stage, excluded from the REPAs. Moreover as the EU has RIAs with all but seven countries in the world, any preferential market access is likely to get translated into lower prices for EU consumers than in accrued rents for ACP producers. Finally, if the REPAs are indeed to substitute rest-of-the-world imports with EU imports, the loss in government revenue could be substantial and unevenly distributed.

Transfers and compensation. Strong asymmetry in size is a particularity of most SSA RIAs with a 'hegemony' in each likely grouping: Kenya dominates the East African Community (EAC), Côte d'Ivoire the UEMOA, Cameroon the Central African Customs Union (CEMAC), South Africa in the South African Development Cooperation (SADC), and Egypt in the proposed Common Market for Eastern and Southern Africa (COMESA)). Furthermore, in each SSA grouping, government revenue from trade taxes is usually around 30% of government revenue, but up to 50% (or 7.3% of GDP) for the UEMOA in 1995. These characteristics suggest the following remarks.

First, the hegemony is likely to be far from the world efficient suppliers with as a consequence much tax revenue transfer to the hegemony that could become quickly politically unsustainable, unless the hegemony also reduces substantially its protection against the outside world.

Second, in the case of a customs union (as is under way for the UEMOA), to avoid transfers to the richest economy, the Common External Tariff (CET) should be set at the level of the country with the lowest tariff so as to remove incentives for inefficient producers to increase their production and sell it in the more protected markets within the FTA.

Third, given the poorly developed fiscal systems and the estimated size of the revenue loss, increases in VAT rates (a non-too distortionary means to generate government revenue) would be too large to implement. So, unless the EU comes up with compensation, it will be a challenge to find ways of reaching fiscal balance without introducing distortionary compensation schemes, as was the case in the previous PTAs in SSA.

Marginalization. Among the causes of failure of the first wave of South–South regionalism was the inability to agree on the location of industry investment. The new wave of RIAs has moved away from central planning and views regional integration as a way to promote investment, win capital inflows and affect industry location. Foreign direct investment (FDI) from outside countries could increase as a result of the two-stage regional strategy proposed by the EU, though the 'hub-and-spoke' approach to regionalism followed by the EU biases investment towards the hub rather than towards the spokes.

Marginalization of the periphery would also be predicted by 'economic geography' models that suggest that reciprocal liberalization will draw industry into the country with the larger market and away from the smaller countries as centripetal forces operating through demand and cost linkages will dominate centrifugal forces.

Which external anchor? Because of recidivism in the past and because of changes in government policies, it has been argued that North–South RIAs in

SSA could increase credibility. It has been argued that the credibility benefits from RIAs are not as readily available within the multilateral framework of the WTO. While this may be the case, credibility is not an independent characteristic or RIAs (a beneficial RIA is more credible than one that is not beneficial); furthermore, there are other means of signalling and winning credibility as for instance in binding trade policy with the WTO which is not the route followed by most ACP countries so that this opportunity to signal tough-mindedness has not been taken.

However, because the EU is a large market accounting for close to half of ACP trade for some regions, one could argue that the insurance motive of market-access in case of a trade war is relevant. Equally relevant is the motive to avoid the major partners' contingent protection: safeguards and anti-dumping duties. But it is unlikely that the EU will be willing to give up the right to exercise anti-dumping duties against its partners.

Rewards and punishments. For the extra credibility gains to be had from anchoring to the EU rather to the WTO, the negotiations should yield a fairly stringent set of rewards and punishments. Take as an example, the UEMOA which is setting up a CU by 2000 and is engaged in talks for a REPA to be carried out over the period 2005–17 with much backloading (over 50% of the reductions for sensitive products starting in 2013). For the UEMOA as whole, the annual loss of moving to the lower CET level for the first stage integration has been estimated at 0.23% of annual UEMOA GDP. And moving to the REPA by 2017 would give an extra annual loss of 0.59% on annual basis. Given the small GDP of the region ($33 billion in 1997), compensating for government losses during transition to the REPA would only require $19.5 billion on an annual basis from the EU. It seems that the EU should be able to come up with an incentive scheme, conditional on performance that would compensate for government revenue loss during the transition. Such a proposal would also have the added advantage of helping reveal the 'true type' of ACP countries at the negotiating table.

A Greater role for regional cooperation. Finally, the Paper argues that there are two other types of non-discriminatory arrangements that merit attention in SSA. The first is cooperative arrangements (for example the sharing of training costs and of projects with economies of scale like infrastructure or power sharing). The second is cooperation in the management of a common resource that generates externalities in its use and where property rights are uncertain (e.g. river basins). The second type of arrangement is more difficult to achieve, not only because like the first it must be self-enforcing, but also because agreement on property rights must be reached.

0. Introduction

The recent growth in Regional Integration Agreements (RIAs) has been numerically dominated by the European Union's (EU's) activities. Among these are the Europe agreements with countries of Eastern Europe, the renewal of RIAs with Mediterranean countries, and currently, the European Commission's proposal to put EU-ACP trade relations on a reciprocal basis for those ACP (Africa, Caribbean, Pacific) countries wishing to enter into a Regional Economic Partnership Agreement (REPA) with the EU. This proposal for cooperation (to become Lomé V if it is carried out)is to replace Lomé IV.[1] While it is recognized that this proposal is part of the EU's "foreign policy", it is also understood that "one of the key objectives of the EU's development cooperation under the Maastricht Treaty is `the smooth and gradual integration of developing countries into the world economy'. It is widely recognized that regional integration forms an essential part of the strategy for achieving this." (Kennes (1998, p.26)).[2]

These "new" elements in the Lomé V approach to cooperation are: (i) reciprocity in the trade relations between the EU and the ACP countries – an element that was supposed to be present in their trade relations early on, but was abandoned; (ii) encouragement of prior RIAs among the countries that would enter REPAs—for example the UEMOA and Ghana would be encouraged to form an FTA (and encouragement for all ACP to join the WTO); (iii) a preferential trading arrangement (with about 80% to 90% of bilateral trade between the EU and REPA would be abolished over a ten year period (2005-2015) with REPA members allowed to "backload" their reforms, postponing the main tariff reductions till the end of the period.

This paper takes a critical look at these new elements from the point of view of the ACP countries, whose alternatives, as members of the WTO, are essentially a

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[1] Granting preferential access has been a cornerstone of the EC's approach in its relations with its former colonies, but so far there has been no reciprocity, and the beneficiaries were not requested to enter in RIAs among themselves. Instead of the proposed Lomé V route to be discussed here, the EU could have opted either for: (i) an extension of the GSP to non-ACP developing countries, perhaps including differential preferences according to per capita income; (ii) bring down MFN tariffs to Lomé levels requesting in exchange that other OECD members also reduce tariffs in sectors of interest to ACP exporters. Stevens et al. (1998) explore the first option, and Winters (1998) gives convincing arguments in support of the second alternative.

[2] Grilli (1993) is the authoritative source on the EU's approach to relations with the ACP countries. Sapir (1998) reviews the dimensions of EU regionalism and Solignac Lecomte (1999) provides a broader perspective taking into account the diplomatic aspects of reciprocity in the REPAs.

reliance on non-discriminatory trade policies based on a combination of unilateral and multilateral trade liberalization. It draws on recent work evaluating the regional approach to trade (and other) policies at the theoretical and empirical levels. Finding new approaches to trade policy in SSA is arguably urgent as a compelling case can be made that the poor performance of SSA countries is partly due to their poor trade performance: falling market shares in world markets and higher than average tariff and non-tariff protection than comparable countries.[3] Also, previous attempts at regionalism, by and large, failed, both in terms of their ambitious objectives and in terms of their accomplishments.

In spite of being able to draw on recent work[4], much of what follows relies on a priori reasoning, and tenuous comparisons with experience elsewhere. It is mostly guesswork, both because it is difficult to judge the likely effects of these proposals, and because it is hard to foresee what the ACP countries would do in the alternative of no REPA. Section 1 looks at some of the implications of the asymmetries within the proposed regional groupings and section 2 at the credibility arguments of North-South agreements. Section 3 argues that the focus on preferential agreements should not detract from the potentially large (and non-controversial) gains to be had from other forms of non-discriminatory cooperation.

1. Asymmetries, transfers and compensations, and marginalization.[5]

Pronounced asymmetries between countries, the small size of each proposed regional bloc, the structure of their foreign trade and of their tariff structure suggest predictions on the likely economic effects of the proposed two-stage regional approach to integration in world markets.

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[3] Over the period 1962-4 to 1991-3, the SSA share of world exports has declined by $11 billion per year. Wang and Winters (1997) show that this is due to a general loss of competitiveness as the share of OECD imports of the “newer” SSA exports has fallen from 9.4% to 6.3%. At the same time, the average tariffs in SSA were 26% compared with 17% for other developing countries and NTB coverage ratios were 34% compared with 18%. For arguments as to why trade reform is difficult in Africa, see Rodrik (1998).

[4] Foroutan (1993) gives a thorough review of the reasons for failure of previous attempts at regional integration in SSA. Oyejide (1996), Wang and Winters (1997), Winters (1998) and World Bank (1999)) provide more recent evaluations.

[5] There is a considerable literature on the trade-diversion and trade-creation aspects of RIAs. See for example Anderson and Blackurst (1993), de Melo and Panagariya (1993) and Bhagwati and Panagariya (1996). The discussion here draws on these sources and on CERDI (1998) and Winters (1998).

Consider the first stage, where countries are to form regional FTAs prior to joining REPAs. The standard Vinerian analysis of preferential trading arrangements suggests that the potential for trade creation of these regional FTAs is low as these countries have very similar patterns of trade, importing and exporting similar goods. These characteristics imply a very substitutable pattern of trade, which raises concerns of relatively large trade diverting effects of these FTAs. Michaely's (1996) trade complementarity index indicates that NAFTA and the EU-15 members have a within-members complementarity index 12 times larger than SSA countries, and MERCOSUR 3 times larger.[6]

Moreover, compared to other developing countries with FTAs, tariff levels and dispersions are high in SSA (averages followed by coefficients of variation in parenthesis) : SSA (19.6%;0.73); Latin America (11.6%;0.56). Usually, the large country in each grouping is the more industrialized with the higher tariff and perhaps the sole producer.[7] So unless, there is simultaneously across-the-board trade liberalization with the rest-of-the-world, there will be a large income transfer in terms of foregone tariff revenue to the dominating country in the group.

By-and-large, the second stage in which the REPAs will be implemented provide one-way market access for EU exporters in ACP markets. Indeed, ACP countries pretty much have zero-duty market access into the EU for manufactures and non-sensitive agricultural products, sensitive agricultural products being, at this stage, excluded from the REPAs. Currently, post-Uruguay round average tariffs for developing countries exporters are 4.5% for industrial goods and 1.5% for non-agricultural primaries (Finger et al. 1996), so that market access gains will be negligible. Such an outcome is all the more likely that the EU has RIAs with all but seven countries in the world (see Sapir (1998, table 1)) so that any preferential market access is likely to get translated into lower prices for EU consumers than in accrued rents for ACP

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[6] The Michaely trade complementarity index between country i and country j is given by $C_{ij} = 100 - \sum_k \left(\left| m_{ik} - x_{jk} \right| \right) / 2$, where x_{jk} is the share of good k in total exports of country j and m_{ik} is the share of good k in all imports of country i. It reflects the low share of intra-regional trade in SSA of 12% (5% for oil exporters and 16.5 for non-oil exporters) as the region exports 80% of its production to OECD countries (Yeats, 1998), 51% to the EU and 24% to NAFTA) which again raises questions regarding the potential benefits of intra-regional preferential trade agreements.

[7] For example in the UEMOA, Côte d'Ivoire had higher tariffs in 1997 than other members for all broad categories of goods (region-wide averages after the semi-colon). Producer goods (15.1;7.8); intermediates (19.5;10.5); consumer goods (29.6;18.1). Source: CERDI (1998, table 3.).

producers. Finally, if the REPAs are indeed to substitute rest-of-the-world imports with EU imports, the loss in government revenue could be substantial and unevenly distributed (see below).

Transfers and compensation. Strong asymmetry in size is a particularity of most SSA RIAs: Kenya dominates the East African Community (EAC), Côte d'Ivoire the UEMOA, Cameroon the Central African Customs Union (CEMAC), South Africa in the South African Development Cooperation (SADC), and Egypt in the proposed Common Market for Eastern and Southern Africa (COMESA)).[8] In each grouping, there is a "hegemon" whose presence brings the following remarks.

First, the hegemon is likely to be far from the world efficient suppliers (with the exception perhaps of South Africa). In each SSA grouping, government revenue from trade taxes is usually around 30% of government revenue, but up to 50% (or 7.3% of GDP) for the UEMOA in 1995. How much revenue would be transferred from the poorest to the richest? In the case of EAC, Yeats (1998), estimates that the full implementation of an FTA for the EAC would result in 8 to 10% decline in customs collection for Uganda and a 5 to 6% percent decline for Tanzania. Given the dependence of SSA governments on trade taxes, the transfers alluded to above could become quickly politically (or budgetary) unsustainable, unless the hegemon also reduces substantially its protection against the outside world.[9]

Second, in the case of a customs union (as is under way for the UEMOA), one can, in principle at least, avoid transfers to the richest economy if the Common External Tariff (CET) is set at the level of the country with the lowest tariff. Then, there will be no incentives for inefficient producers to increase their production and sell it in the more protected markets within the FTA. As shown by Richardson (1995), this outcome may occur endogenously if governments are conscious of the income transfers related to preferential trade as, in a non-cooperative framework there will be Bertrand-type competition leading to a "race to the bottom" via competition for tariff revenues. In an extension of

[8] One would be tempted to speak of "hegemonic" RIAs though, so far, this is only the case in the case of SACU. Interestingly, this is a typical "North-South" RIA whose experience has relevance in an assessment of the REPAs. Rodrik (1998) argues that Botswana's superior economic performance is largely due to her having delegated her trade policy formulation to South Africa.

[9] The sustainability of MERCOSUR is largely due to such an approach of simultaneous opening to the outside world: Brazil reduced its tariffs from 80 percent in 1986 to 12 percent in 1995, Argentina from 41 to 11 percent, Uruguay from 36 to 11 and Paraguay from 20 to 9.

Richardson's analysis, Cadot et al (1999), show such an outcome is only likely to happen endogenously when countries are of relatively similar size (i.e. when every member can inundate other members' market). If, countries vary in size (as is the case in SSA) they show that these forces are not at play as the large members may actually have incentives to increase their tariff.

Third, given the poorly developed fiscal systems and the estimated size of the revenue loss, increases in VAT rates would be too large to be implementable. So, unless the EU comes up with compensation, it will be a challenge to find ways of reaching fiscal balance without introducing distortionary compensation as was the case in the previous PTAs in SSA (see Foroutan (1993)).

Fourth, in the case of Franc zone countries, in spite of the relatively high degree of policy coordination in the Franc zone which has prevented large deviation in trade policies in the region, differences in structure are likely to require different patterns of adjustments that will be more difficult to achieve without use of the exchange rate as they belong to a monetary union.[10]

Marginalization. Among the causes of failure of the first wave of South-South regionalism was the inability to agree on the location of industry investment. The new wave of RIAs has moved away from central planning and views regional integration as a way to promote investment, win capital inflows and affect industry location. Foreign direct investment (FDI) from outside countries could increase as a result of the two-stage regional strategy proposed by the EU, though the "hub-and-spoke" approach to regionalism followed by the EU biases investment towards the hub rather than towards the spokes. First, regional FTAs would give duty-free access to a larger market which raises the return on investment.[11] Second, the reciprocity of the REPAs could bring multinationals to redirect investment to SSA as the environment would be perceived as sufficiently stable and

[10] If the experience of integration among unequal partners elsewhere applies, in the case of the MERCOSUR, sectors with significant trade creation will be exempted, the convergence to the CET will be slower than scheduled (in the UEMOA it is scheduled for 2000), and the CET will represent the preferences of the member country that has the greatest production in the sector.

[11] Excluding Egypt and South Africa, the combined GDP of SSA countries barely exceeded that of Belgium in 1995. With such small markets, unit production costs could fall substantially because of unexploited economies of scale.

predictable to bring multinationals to set up export platforms.[12]

Marginalization of the periphery would also be predicted by “economic geography” models that suggest that reciprocal liberalization will draw industry into the country with the larger market and away from the smaller countries as centripetal forces operating through demand and cost linkages will dominate centrifugal forces.[13] Such effects are not universal though (e.g. Portugal and Spain in their accession to the EU) but are likely to be less pronounced in unilateral or multilateral trade liberalization. Thus RIAs in SSA can be expected to lead to further divergence among asymmetric countries and to de-industrialization of the smaller countries. For example, FDI flows into the MERCOSUR have favored Argentina and Brazil.

In SSA, the tensions created by industry agglomeration have already been important during the first wave of RIAs in the 1950s and 1960s. For example, the EAC collapsed in 1977 as it failed to satisfy the poorer members that they were getting a fair share of the gains. Similar tensions are building in the Community again and are likely to develop in all the region groupings in SSA where the dominating economy in the region will reap most of the benefits from the RIA, yet be unable to compensate the losing partners both because of lack of institutions and political will (strife and political tensions are widespread in that part of the world).

2. Which external anchor?

Because of recidivism in the past and because of changes in government policies, it has been argued that North-South RIAs in SSA could increase credibility. Collier and Gunning (1996) argue that for a number of factors including the heavy conditionality on aid-disbursement, SSA countries faces time-consistency problems, that explain why so many reforms in the past have been reversed. A North-South RIA along the proposed

[12] Following the creation of NAFTA, FDI to Mexico increased substantially ($4.3 billion in 1991 to $11 billion in 1994). Likewise, FDI inflow into the EU expanded from ECU 10 billion in 1984 to ECU 63 billion in 1989. One would expect the REPA effect to dominate as the evidence of South-South RIAs on investment and growth shows negligible effects (see Brada and Mendez (1988) and de Melo, Montenegro and Panagariya (1995)).

[13] Centripetal forces include: knowledge spillovers or other beneficial technological externalities; labor market pooling effects; linkages between buyers and sellers as firms will want to locate close to buyers. Centrifugal forces include congestion, pollution or other externalities associated with concentrations of economic activity; competition for immobile factors whose prices are bid up by agglomeration; demand coming from dispersed consumers.

lines would help solve this problem and serve as signaling device in a world of asymmetric information.

Fernandez and Portes (1998) develop the arguments why such benefits from RIAs are not as readily available within the multilateral framework of the WTO. Winters (1998) sees merits to this argument, though he notes that credibility is not an independent characteristic or RIAs (a beneficial RIA is more credible than one that is not beneficial) and also that there are other means of signaling and winning credibility as for instance in binding trade policy with the WTO. Here it is instructive that SSA governments have generally bound their tariffs at several multiples of the rates currently applied.[14] The opportunity to signal tough-mindedness has not been taken.

Because the EU is a large market accounting for close to half of ACP trade for some regions, one could argue that the insurance motive of market-access in case of a trade war is relevant. Equally relevant is the motive to avoid the major partners' contingent protection: safeguards and anti-dumping duties. Winters believes that the EU will not be willing to give up the right to exercise anti-dumping duties against its partners.

Rewards and punishments. While the WTO is not likely to be a good means of achieving enforcement and avoiding recidivism, it is not clear that the EU will be any better, especially in its dealings with former colonies. If Mexico raised its tariffs following the 1994 crisis, it is hard to see how the EU will be able to oppose similar behavior by ACP countries, especially if tariffs are raised against third countries, which is an available option given the very high rates at which tariffs are bound. One could imagine that ACP countries would not dare raise tariffs on EU products, so they would end up raising tariffs at the outside world, but even more so to get the same revenue increase with the well-known deleterious effects on welfare since the costs of protection increase with the square of the tariff level.

For the extra credibility gains to be had from anchoring to the EU rather to the WTO, the negotiations should yield a fairly stringent set of rewards and punishments. Take as an example, the UEMOA which is setting up a CU by 2000 and is engaged in talks for a REPA to be carried out over the period 2005-2017 with much back-loading (over 50% of the reductions for sensitive products starting in 2013).

[14] Cerdi (1998, table 8.1) report the following rates (average tariffs followed by maximum bindings in brackets with a semi-colon separating agriculture and industry: Benin (6.1[119];6.9[69]); Côte d'Ivoire (17.5[221];14.7[260]); Senegal(26.5[180];30.1[180]

CERDI (1998) estimates revenue effects for each country in the region by aggregating separate estimates for each individual product in a standard partial equilibrium demand and supply simulation analysis. The novel aspect of their estimates is the econometric estimation of the relationship between exemption rates and tariff levels which is subsequently built into analysis (thereby lowering revenue loss estimates by about one half).[15]

Based on the CET rates agreed in July 1998 (consumer goods (9,8%); intermediates (10,9%); capital goods (6,9%)), the UEMOA should have a customs union by 2000 with fairly low and uniform tariffs close to the levels of the low-protection country, much as was suggested above. Though the estimates reveal much variance across countries, for the UEMOA as whole, the annual loss of moving to the lower CET level is estimated at 0.23% of annual UEMOA GDP. And moving to the REPA by 2017, would give an extra annual loss of 0.59% on annual basis. Given the small GDP of the region ($33 billion in 1997), compensating for government losses during transition to the REPA would only require $19.5 billion on an annual basis from the EU. It seems that the EU should be able to come up with an incentive scheme, conditional on performance, that would compensate for government revenue loss during the transition. Such a proposal would also have the added of advantage of helping reveal the “true type” of ACP countries at the negotiating table.

3. A Greater role for regional cooperation

Africa has set up over 200 regional cooperation schemes in the last thirty years, most of them involving preferential trading arrangements that are discriminatory. However, there are two other types of non-discriminatory arrangements that merit attention in SSA, even though asymmetries in country sizes, interests, and the general lack of institutional development in the region make them hard to implement. The first is cooperative arrangements (for example the sharing of training costs, and of projects with economies of scale like infrastructure or power sharing), the second is cooperation in the management of a common resource that generates externalities in its use and where property rights are uncertain (e.g. river basins). The second type of arrangement is more difficult to achieve, not only because like the first it must be self-enforcing[16], but also because agreement on

[15] The results are similar to those in Pritchett and Sethi (1994): exemptions are an increasing function of the height of the tariff, and in some cases of the variance of variance.

[16] Self-enforcement is necessary because, in contrast to agreements that internalize intranational externalities, international externalities cannot

property rights must be reached. Following are two examples taken from World Bank (1999) and de Melo (1998).

The Southern African Power Pool (SAPP). Inaugurated in 1995, the SAPP represents an interesting case of cooperation in the power sector. Power exchange in the southern part of Africa first arose because of the distribution of power sources in the region: a large reserve of low-cost hydroelectricity in the northern part (especially the Inga Reservoir), large reserves of cheap coal in South Africa, and the Kariba dam (on the border between Zambia and Zimbabwe), which being in the middle of the regional system can play the “buffer” role. The benefits of the pool include reductions or postponements in new requirements for generating capacity and reserves, reductions in fuel costs, and more efficient use of hydroelectricity. A SADC electric power study conducted in 1990-92 estimated a saving of 20% in costs over 1995-2010 amounting to $785 million (estimates would be larger if the Democratic Republic of Congo and South Africa who are members had been included in the study).

The agreements incorporate the SADC Treaty, the SADC Dispute Resolution Tribunal, the SADC energy ministers, and the Technical and Administrative Unit. The energy ministers are responsible for resolving the major policy issues in SAPP and the Technical and Administrative Unit seeking funding according to recommendations of the executive committee. Three factors played a key part in the development of the regional agreement: the availability of complementary power sources, an active regional organization for economic cooperation, and the political will to support increased regional energy trade. Because the SADC served as a focal point for the promotion of regional integration facilitating investments in the needed interconnection projects.

Costs of non-cooperation along the Nile. The ten Nile riparians could gain much annually if the current allocation of 84 billion cubic meters (BCM) water annually to Egypt and Sudan under a 1959 Treaty was renegotiated. It is estimated that if Blue Nile reservoirs were developed, there would be an increase in the annual long-term water yield of between 4 and 5 BCM annually. This is because along the blue Nile evaporation rates are 50% of those downstream and reservoirs in mountainaous terrain use lower surface-to-volume ratios. Likewise elimination of the antiquated Jebel Auria reservoir

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be enforced by a third party so that the agreements must include the mechanisms which by themselves can sustain a cooperative agreement. It is for this reason that, usually, only a few of the parties concerned participate and that the Pareto frontier is not reached in these agreements.

on the White Nile (that serves mostly for hydropower) would yield an reduction in evaporation loss of 2.8 BCM. Rough and ready calculations suggest that a better allocation of water among blue Nile riparians could raise their annual growth rate by between 0.5 and 1 percentage point per annum.

Reaching an agreement is proving very difficult both because the unidirectional nature of upstream-downstream externalities makes it necessary to look for multi-good cooperation (e.g. water and hydropower) as a way of concretizing this positive-sum gain. But introducing side-issues which may help in the case of a high degree of externalities as it provides the necessary rewards for cooperation and the punishment for defection requires a more elaborate institutional framework that is currently absent (though it could emerge in the development of COMESA which could also help build trust)).

These two examples, and there are others, show that there are sizeable gains to be obtained from regional cooperation in SSA. If the case can be made that regional integration on a preferential basis can be good politics as increased trade builds security[17], it also points out that the institutional framework needs to be there (which can come from institutions developed in the course of PTAs as in the case of SADC). Two remarks are pertinent here: first, the proposed REPAs can help develop institutions that resemble those developed in the EU (as has been the case in the Europe Agreements in certain areas). Second, there is a high opportunity cost to negotiations, especially in the human-capital scarce SSA countries. Since the gains from non-discriminatory cooperation are likely to be sizeable, scarce human capital should not be distracted to negotiating cumbersome, costly and time-consuming necessary details that are part of every FTA (such as rules of origin).

[17] Using a standard Vinerian model in which security enters the utility function and is positively related to the volume of trade with neighboring countries, Schiff and Winters (1998) show that giving preferences to a neighbor raises welfare as it diminishes fear and the potential for conflict. They also cite evidence that the propensity for less conflict among democratic countries comes from a causality in which it is trade that reduces conflict rather than the opposite.

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