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Module 1

SADCC ENVIRONMENTAL ANALYSIS

SELECTED PORTIONS

of the

SADCC

INTRA-REGIONAL

TRADE STUDY

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PART I

CURRENT SITUATION

For the SADCC as a region, the objective of trade is to increase the production, employment and incomes and to exchange goods to better satisfy the needs for consumption and future development. The aim of intra-regional trade is to increase these benefits, to obtain better trading relationships, to diversify the economy and reduce external dependence, and create a basis for mutually interdependence.Trade patterns in the Southern African region have benefited the previous colonial powers and the regional economic centres such as the Republic of South Africa (RSA). The present level of intra-SADCC trade is low, and their economies are not complementary. The major objective of the SADCC countries is to develop and liberate their economies, develop their mutual complementarity, and increase intra-regional trade, in order inter alia to reduce their dependence on the RSA.

Overall Trade Patterns

While total exports from the nine SADCC countries in 1982 amounted to approximately 5,500 million USD and total imports to approximately 7,200 million USD, the intra-regional trade between the same countries accounted only for between 276 and 316 million USD in that same year. Intra-regional trade thus represents only 5% of the total exports of the SADCC countries, and 4.4% of their total imports. Trade between the SADCC countries and the other countries in the PTA is even more marginal, representing less than 1% of both the exports and imports of SADCC.

South Africa is a major trading partner for many of the SADCC countries, accounting for around 7% of the total exports of the SADCC countries, and as much as 30% of their combined imports.The distribution of export and import markets varies considerably, however, from one countrv to another.

Table 1 shows that intra-SADCC trade is of relatively greater importance for Botswana, Malawi, Mozambique and Zimbabwe, while it is almost insignificant for Angola and Lesotho, and only of moderate importance for Swaziland, Tanzania and Zambia. South Africa is a very important export market for Lesotho, Swaziland, Botswana, Malawi and Zimbabwe. However, South Africa is an even more important source of imports, in particular for Botswana, Lesotho and Swaziland (the BLS countries), but also for Malawi, Zimbabwe, Zambia and Mozambique.

There is no doubt that the main reasons for the existing trade patterns are found in the underdeveloped state of the economies of the SADCC countries, and in the economic structures that were shaped by the previous colonial powers, and later by various economic and political factors. This has resulted in the very limited complementarity between the economies of the SADCC member states. The SADCC countries will still mostly export agricultural products and mineral raw materials for which there is little demand in the region, while they mostly import mineral fuels, capital goods and other manufactured products, that are

TABLE I

Summary Figures for SADCC Intra-Regional Trade, 1979-84 (mill. USD)

Imports From SADCC Countries:

Imports To:	1979	1980	1981	1982	1983	1984
Angola	24	28	28	8	2	25
Botswana	(40)	46	50	43	54	(56)
Lesotho	(0)	0	2	0	1	0
Malawi	17	28	29	(29)	(25)	(23)
Mozambique	14	24	17	25	32	22
Swaziland	(4)	2	4	4	(4)	(2)
Tanzania	9	7	8	35	25	11
Zambia	11	20	63	63	(40)	(42)
Zimbabwe	(26)	49	115	108	86	64
Total	(145)	204	308	315	(269)	(245)

Exports to SADCC Countries

Exports From:	1979	1980	1981	1982	1983	1984
Angola	1	0	0	1	0	6
Botswana	(45)	42	36	54	52	(34)
Lesotho	0	0	0	0	0	(0)
Malawi	8	23	29	23	(22)	(18)
Mozambique	7	7	29	27	5	10
Swaziland	(5)	4	8	8	(7)	(7)
Tanzania	27	20	5	4	4	5
Zambia	24	30	51	36	(33)	(35)
Zimbabwe	(41)	68	139	123	108	115
Total	(158)	194	297	276	(231)	(230)

only to a limited extent produced within the region.

Intra-SADCC Trade

Intra-SADCC trade in 1982 amounted to around 300 million USD. 276 million USD was reported by the exporters based on export prices (fob), and 316 million USD was reported by the importers based on import (cif prices).

Intra-SADCC trade is unevenly distributed among the SADCC countries. Almost half of all intra-SADCC trade originates in Zimbabwe. Since another 30% of the trade is as imports to Zimbabwe, this means that Zimbabwe is a partner to almost 80% of the total intra-SADCC trade, and that only 20% does not in any way involve Zimbabwe (either as an exporter or importer). Botswana, Malawi, Mozambique and Zambia also each represent important parts of the intra-SADCC trade, while the shares of Angola, Lesotho, Swaziland and also Tanzania are rather small.

During the years 1982-84, about 25% of the total intra-regional trade consisted of food products, approximately 10% consisted of other crude materials and 16-17% were fuels and energy products. This means that almost 50% of total intra-SADCC trade were manufactured goods or semi-manufactured. This structure is very different from the overall exports from the SADCC countries, where perhaps 10% consists of manufactured products.

Angola has practically only been exporting petroleum, in deals with Mozambique in 1984 and Tanzania in 1985. Since Angolan crude oil cannot be used by the refineries in the other SADCC countries, the oil has to be exchanged with other qualities on the international market.

Botswana has been exporting meat to Angola (1979 and 1980), and to Mozambique (1981-84). This export is somewhat unstable, depending partly on demand in these two countries, and partly on surplus production in Botswana and the market in the European Economic Community (EEC). Botswana's exports to Zimbabwe consist mainly of copper/nickel matte, textiles and clothing. The value of exports of clothing decreased in 1984, partly due to protectionist measure in Zimbabwe.

Malawi exports mostly agricultural products, such as rice, vegetables and tobacco. In the early 1980's Malawi exported textiles to Zimbabwe, but this export was very small in 1983 and 1984. In 1984 maize was exported to Zimbabwe. There have also been exports of fish as well as clothing and footwear.

Mozambique's exports to the SADCC have been fluctuating greatly. The main exports have been to Zimbabwe in 1981 and 1982, when Zimbabwe was importing refined oil products from Mozambique. Since the re-opening of the oil pipeline from Beira, these imports have no longer been necessary, as the petroleum and diesel is only pumped through Mozambique. Under the trade agreement with Tanzania, Mozambique has been exporting textiles, domestic electrical products, cement and tyres and tubes, but not on a very regular basis. Exports in 1983 and 1984 have been practically nil, probably because of the general problems with production in Mozambique. Similarly, Mozambique's exports of coal to Malawi and cement to Swaziland have decreased almost to zero, because of production problems.

Swaziland's main exports to the SADCC countries have been wood to Zambia, and wood pulp to Zimbabwe (1981 and 1982).

Tanzania has been exporting mainly to Mozambique under their trade agreement, mostly textiles and clothing. In addition, there has been some exports of fish to Zambia.

Zambia which exports almost nothing but copper to the rest of the world, is an exporter of electric energy to Zimbabwe, and small amounts of cement to Botswana and Malawi, zinc to Tanzania and some chemicals to Zimbabwe.

Finally, as the largest exporter, Zimbabwe exports a larger variety of commodities. During the years 1981-83, it was exporting substantial amounts of maize to Angola, malawi, Mozambique, Tanzania and Zambia. This was particularly due to the drought in the importing countries and very good crops in Zimbabwe in 1980/81. The sales were (partly) paid for by international emergency assistance. In 1984, however, the stocks in Zimbabwe were depleted, and it could no longer supply its neighbours. Zimbabwe was also exporting meat to Angola (1984) sugar to Botswana, textiles to Botswana, Malawi (1980-82) and Zambia (1984), coke to Zambia, cement to Botswana, increasing amounts of iron and steel to Botswana, Malawi and Zambia and a number of other products including medicines and pharmaceuticals, soaps, paper and agricultural machinery. Its total exports to the SADCC countries reached a maximum in 1981 with almost 140 million USD, but has since decreased to 115 million USD in 1984, due to a large extent to the fall in maize exports.

In total, commodities make up approximately 70% of the total intra-regional exports. The remaining 30% consists of a number of items where each trade flow is relatively small, or they have not been identified in the available data. It may be important to note this residual, however, as it may also include some items with a good growth potential.

TABLE 2 shows the net balances for 1982 for the SADCC countries in their intra-regional trade.

Only Zimbabwe has a substantial, and growing trade surplus with the rest of the SADCC, while Swaziland has a smaller surplus. Botswana had a surplus in 1982, but this became a large deficit in 1984. On the other hand, both Tanzania and Zambia had large deficits in 1982, but these deficits were reduced in 1984. Both Angola and Mozambique appeared to develop a much greater deficit in 1984.

Net balances with the whole of the PTA (including the SADCC) are not substantially different from the net balances with SADCC only (with the exception of Mozambique). This is not surprising, considering the low level of trade between the SADCC countries

Net Balance in Intra-SADCC Trade, 1982 (millions of USD)

	Net Balance in Multilateral Trade [1]	
	Within SADCC	Within PTA
Angola	-6.8	-6.9
Botswana	+10.9	+10.7
Lesotho	-0.4	-0.5
Malawi	-6.1	-4.8
Mozambique	+1.7	+17.6
Swaziland	+4.4	+7.3
Tanzania	-31.2	-33.6
Zambia	-26.9	-28.5
Zimbabwe	+14.7	+21.6

[1]) Negative figures mean net deficit, positive figures export surplus

and the rest of the PTA. Also, in most cases, the net balance with PTA-nex is in the same direction as with the SADCC as a whole. Trade with the whole of the PTA does therefore not balance better than within the SADCC itself.

The nine SADCC countries operate different trade regimes, reflecting partly the very different economic conditions prevailing in the various countries. The following is a rough description of the nine countries' trade regime and trade policies, with a particular emphasis on how these conditions affect the countries' capabilities and potentials for participating in intra-regional trade:

The BLS countries: Botswana, Lesotho and Swaziland have several characteristics in common-they all belong to the Southern African Customs Union (SACU) and therefore have a free trade system between them and South Africa. Their common external tariffs, which are in reality decided by South Africa, are characterised by high tariffs on products that are also produced in the RSA, with relatively low tariffs on other products. These countries do not apply any import regulation by quotas or otherwise to ration the use of foreign currencies. Lesotho and Swaziland are members of the Rand Monetary Area (RMA), and use the South African Rand freely for all imports. Botswana has sufficient export revenue and foreign currency reserves to cover current imports. South Africa has a very strong position as the main source of imports; more than 80% of all imports are registered as originating in the RSA (though some may be re-exports). In addition to its developed industrial base, geographic vicinity and relatively good communications, South Africa also benefits from its tariff preferences in the customs union. South Africa's competitive advantage is further strengthened by the fact that most companies in the BLS countries including the main importers are South African owned or dominated.

In reality, therefore, as suppliers to the BLS countries the other SADCC countries have several disadvantages as compared with South Africa. For example: relatively high tariffs (except for Malawi and Zimbabwe to Botswana), geographic distance and inadequate transport facilities (except for Mozambique to Swaziland and Zimbabwe to Botswana), ownership and established business contacts, added to the industrial and economic strength of South Africa. For Angola and Tanzania, that do not trade with South Africa, it may be particularly difficult to enter the BLS markets, because of South African ownership and dominance.

The industrial sector is relatively small in all BLS countries, and it is difficult to develop this within the SACU due to the strong competition from South African producers, and the bias within the SACU to give them tariff protection, while products that are only produced in the BLS countries are not always given a similar protection.

Except for Lesotho, which has very limited export production, both Botswana and Swaziland do nevertheless export to other SADCC countries, and could probably expand their production if the markets were available in the region.

For Malawi the situation is in many ways similar to that of the BLS countries. Malawi is following a relatively open import policy, with few quantitative restrictions. Its balance-of-payments position is not as good as the BLS countries, and therefore some imports are restricted. The Malawian economy also has strong commercial links with South Africa, with which Malawi has a preferential trade agreement. South Africa's position is not quite as strong in Malawi as in the BLS countries: Malawi is not a member of the SACU or RMA, has preferential (free) trade agreements also with Botswana and Zimbabwe, is farther and has higher transport costs to South Africa. South Africa neverthless accounts for 30-35% of Malawi's total imports.

Zimbabwe is in a somewhat better competitive position in Malawi, than in the BLS countries. Malawi's neighbouring countries Mozambique, Tanzania and Zambia also have a potential market in Malawi, if their production capacity improves.

Malawi's imports are affected by the war in Mozambique, and imports are therefore both delayed and more costly, if not destroyed. Since 1983 transport from the Mozambican ports of Beira and Nacala has been difficult if at all possible, while transport from Zimbabwe through the Tete province in Mozambique has required military escorts. Malawi's main alternatives have been road transport through Zambia, and recently a direct road link to Tanzania. These problems with importing through the

Mozambican ports has contributed to making South African products more competitive in Malawi (as compared with other overseas suppliers).

Malawi has a small industrial sector and limited industrial exports. But its few existing industrial products as well as its agricultural products could be exported to the other SADCC countries, if there was a market. Production is limited by its small installed capacity and a small national market, but not by lack of necessary inputs.

All the other five SADCC countries regulate their imports more strongly, mostly with the use of import licensing and other quantitative restrictions.

Zimbabwe has been limiting its imports with an import licencing system, but the reductions in total imports have been moderate (in comparison with the remaining SADCC countries), and import quotas have been increased again in 1985. Botswana and Malawi had an Open General Import Licence (OGIL) status until 1984 when some restrictions were introduced, and imports from these countries were also exempt from tariff duties. These countries therefore have a preferential position in the Zimbabwe market as has South Afdrica, which also has a more limited preferential agreement with Zimbabwe. South Africa's competitive advantage in Zimbabwean economy, and the strong commercial ties that have been established and further strengthened during the Unilateral Declaration of Independence (UDI) period. Zimbabwe obtains approximately 25% of its imports from the RSA, while around 65% come from outside of Africa.

Zimbabwe is the industrially most developed country in SADCC, and is protecting its industries by tariffs and by non-tariff import restrictions. Whle other SADCC countries may be able to supply various inputs to the Zimbabwean economy, as well as non-industrial consumer goods, most industrial (consumer) goods are met with tariffs and a competitive market with products of Zimbabwean or South African origin. Zimbabwe also has an industrial sector which is interested in exporting to the region. The industrial sector has to some extent been affected by the import restrictions which have led to reduced imports of necessary inputs, and thereby reduced production capacity. This is not a major factor in Zimbabwe, however. In good agricultural years, Zimbabwe has a surplus of food grains (and vegetables, seeds) that can be exported. Zimbabwe has sold grain to the World Food Programme and to other donor agencies for the use as emergency assistance to other SADCC countries.

Angola has in reality a war economy, and an import licence system which effectively reduces imports of low-priority items. The war greatly affects internal transport in Angola, and makes it very difficult (if not impossible) for Angola to export or import anything by rail or road to or from its SADCC partners. Trade between Angola and other SADCC countries is therefore by sea or air. Angola does not give any particular trade preference to the other SADCC countries except Mozambique. But Angola does not trade at all with South Africa and the RSA is therefore not a competitor on the Angolan market. However, Angola does have trade agreements with non-regional countries that obtain preference for import licences. As a result of the war, Angola's exports now consist mainly of oil and oil products, with very small exports of diamonds and coffee. Angola's agriculture produce is only for the local and national market, and its industry produces at very low capacity for lack of inputs. spare parts and qualified manpower. Under the present war conditions, Angola cannot increase its production for a regional market, nor can it transport any such products by road or rail to the regional market. When peace is restored, however, Angola's position and potential for regional trade will be drastically changed.

For the remaining three countries: Mozambique, Tanzania and Zambia there are also some similarities in their foreign trade regimes. Due to their very serious lack of foreign exchange to cover their import needs, they all strictly allocate their available foreign exchange according to a set of priorities. All three have experienced cases in recent years when they have not been able to pay their creditors or suppliers on time, and acnsiderable part of their total imports are paid for by grants or loans.

The competitive situation is nevertheless different in the three countries: Mozambique and Tanzania are coastal countries giving overseas suppliers an advantage, while in landlocked Zambia its neighbours are in an advantageous position. South Africa is a relatively important supplier both to Mozambique (8-9% of all imports) and to Zambia (15-20% of imports), while Tanzania does not trade with the RSA. While South Africa's economic influence in Mozambique and Zambia is one of some importance, it has a more limited ownership control there. Both Mozambique and Tanzania have trade agreements with overseas (non-regional) partners, who are given preferences for the supplies of certain products.

The productive sectors in all three countries are also strongly affected by the difficult economic situation in these countries, and in particular by the lack of foreign exchange for necessary inputs for agriculture, industry and the transport sector. As a result, industrial production has decreased to 20-30% (or less) of installed capacity and is (with a few exceptions), not sufficient to satisfy local demand, let alone export markets. In addition, agricultural production has suffered from the drought (Mozambique) and from the difficult internal transport situation (Mozambique and Tanzania). Large parts of Mozambique are also badly affected by sabotage and armed attacks from the Renamo groups. When peace is restored in Mozambique, its capacity to increase it production and also its participation in intra-regional trade will be markedly improved.

The trade regimes, the foreign trade situations, and the trade policies of the nine SADCC countries differ considerably. There are, however, two major groups among them: five countries, the BLS plus Malawi and Zimbabwe have a fully or relatively open general import policy, and strong economic ties to South Africa, a major supplier of imports. The other four countries, Angola, Mozambique, Tanzania and Zambia are badly affected by the lack of foreign exchange and/or the ongoing war and sabotage activities and are strictly rationing their limited foreign exchange for imports. Their productive capacity is also reduced.

PART II

TRADE BARRIERS

The main reason for the low level of intra-regional trade is the underdeveloped state of the economies of the SADCC countries, as well as the economic structures shaped by previous colonial powers, and later by various economic and political factors. This has resulted in the very limited complementarity between the economies of the independent majority-ruled countries in Southern Africa. To change this situation is a formidable task, and it can certainly not be achieved through pure trade measures.

Another obstacle is the yet underdeveloped state of the intra-regional transport network between most of the countries in the region. The few railway lines offer direct and easy communication between some of the SADCC countries only. Furthermore some of these lines have been temporarily closed due to the war and sabotage activities in Angola and Mozambique. The road network offers additional transport routes, but road transport is rather expensive over long distances. The road network is also far from adequate. The coastal countries can use sea transport, but there is not a regular service between these countries. Finally, most SADCC capitals are connected by regular air service, but air transport is too expensive for most products. Improved transport facilities are of definite importance to facilitate intra-regional trade, but increased trade at the same time will be necessary in order to make an improved transport system viable.

Additional important factors reducing the full potentiality for intra-regional trade, are the recent drought affecting several countries in the region, the war and sabotage activities and the economic crisis in several of the SADCC countries.

These and other factors have also been described in previous reports to the SADCC on this matter.

The main barriers to increased imports from within the region, as seen by the importers, can thus be summarised by:

- The limited availabililty of essential goods and services.
- To the extent goods and services are available, poor knowledge of availability
- Higher costs or lower quality (believed or real)
- In some cases, higher tariffs.
- Limited credit.
- Uncertain deliveries and possible delays.
- Poor or costly transport.
- Existing established trade connections (including special interests of those involved to maintain it).

But there are also barriers to exports within the region, compared with exports to third countries, as seen by the exporters:

Poor knowledge of market opportunities.

Uncertain market, uncertain payments, delays.

- Small markets, possibly not profitable.
- No essential products to be imported in return (in case of counter-trade).
- Existing established export channels and commitments to other (third) countries.

Four general factors limit trade in regional markets. First the existence of established trading connections, as well as commitments, obligations and incentives within other trade agreements such as the ACP-EEC agreement, the SACU, agreements with CMEA countries, and other special agreements with third countries, which may act as disincentives to increased regional trade. Second the risk involved in intra-regional trade is experienced both by the exporter and the importer, and relates both to the future market, whether payments will be made on time and to the timing of actual delivery, transport delays, etc. Such uncertainties also act as disincentives, and will divert trade towards more stable trading partners, both as suppliers and markets. Third the lack of credit, is an important factor in selecting the suppliers of essential imports. Fourth the high export price on several products from the SADCC countries, partly reflecting high real costs, inefficient production and that the rate of exchange is set in order to maintain low prices on some essential import items results in higher export prices.

It should also be mentioned that the import regimes in several of the SADCC countries combined with the internal policies and rates of foreign exchange, have led to the development of illegal and unregistered trade, both between SADCC countries and with third countries. It is very difficult to estimate the magnitude of this unregistered trade. The volume of this trade may, however, be influenced by changes in the official trade policies.

PART III

GENERAL APPROACHES TO INTRA-REGIONAL TRADE AND ECONOMIC INTEGRATION

The project approach

In the project approach the countries concentrate on the realisation of jointly formulated projects with obvious mutual benefits. The projects are often implemented in a decentralised way, and there is a minimum of inter-state institution building. Likewise there is no pre-planned model for further integration of the co-operating countries.

The project approach avoids across the board liberalisation, but concentrates on specific products, an approach closely related to industrial co-operation. Industrial co-operation projects may involve a matching of underutilised capacities, or specialisation and complementarity agreements related to existing, planned or new industrial ventures. The main objectives of such co-operation are to obtain better economies of scale, and to exploit the existence of comparative advantages.

If industrial co-operation is linked to a multi-year trade contract, prices and minimum quotas can be discussed and decided upon from the outset. This is, however, a difficult exercise depending on future developments in quality, substitutes and availability of foreign exchange.

In general the main obstacle to the project approach is the complex time-consuming negotiations t state, industry and company Level, that must be conducted before the project can go ahead. The advantage of this approach is that the distribution of benefits from co-operation is in principle clear, though this is not necessarily so in practice.

The market integration approach

The theoretical background for the market integration approach was developed by Viner, Meade and Lipsey in the 1950's. They addressed mainly the economic integration problems in already industrialised countries. This is evident from their assumption of perfect markets, full emplyment, constant terms of trade, no transport costs etc. In judging the possible advantages of trade Liberalisation and specific customs unions they concentrated on two factors: trade creation and trade diversion. Trade creation represents the amount of trade created, when low cost products from one country, due to tariff reductions, substitute high cost production in another country within the trade union. Trade diversion represents the trade loss which the countries suffer when hindering, through high external custom duties, high cost regional products from being substituted by low cost products from outside the union. The intention is to be able to quantitatively set the two factors against each other. In this way it can be analysed whether a given regional trading scheme would be beneficial to the participating states or not.

FIGURE 1

Types of Economic Intergration Action
in the Market Integration Approach

Ideal-Types	Degree of Integration				
	Elimination of tariffs and quotas	Common External Tarrif	Free flow of Labour and Capital	Harmonisation of Economic Policies	Unification Of Political Institutions
1. Free Trade Area	(A)				
2. Customs Union	*	(B)			
3. Common Market	*	*	(C)		
4. Economic Union or Community	*	*	*	(D)	
5. Political Union	*	*	*	*	(E)

The PTA, at its present stage, would be found struggling to implement level (A), whereas the EEC should be placed somewhere between levels (C) and (D). The United States would be an example of level (E).

In the market-integration approach the integration process is seen as linear from level (A) to level (E). Market forces set free at one stage have spill-over effects to the next one, making implementation of this an economic necessity. As can be noted, the tight political co-operation and delegation of powers to supranational bodies will only be relevant in the later stages.

Returning to the question of trade creation and trade diversion, it is obvious that regions in which the countries have a lot of trade with each other and a relatively small trade with the rest of the world; and have structures of production that complement each other are likely to gain from regional economic integration. In other words the trade created will be greater than the trade diversed.

However, in most Third World countries we find the opposite situation. The lion's share of external trade is with industrialised countries and only a small part with countries in their own region. Furthermore, the production structures of these countries seldom complement each other. The bulk of Third World exports are raw materials which seldom have a regional

market. Furthermore, these products seldom have tariff problems on the world market where they largely are traded freely.
Thus, it has been argued that regional economic integration cannot be beneficial to the majority of developing countries. This conclusion has, however, been contested in various ways. This critique, together with another aspect of the market integration approach, the polarisation effect, has been the basis for formulating the development integration approach. The critique is directed at the earlier mentioned assumptions regarding perfect markets and full employment. It is argued that these assumptions are basically static and do not correspond to the realities of the Third World, where large underutilized human and material resources prevail. Economic co-operation, it is argued, as seen in a dynamic perspective, creates possibilities for profitable investment, economies of scale, et. The social costs of large unemployment can be far greater than the loss caused by trade diversion. Larger production of manufactured goods and roughly balanced regional trade can also save valuable foreign exchange. The theory of Viner et al. rests on the existing pattern of trade while the critics argue that the rationale of regional integration in the Third World lies in the investment and trading opportunities that are being created.

A last element, or consequence, of the market approach is the polarisation effect. Its essence is the unequal distribution of benefits resulting from regional economic integration. If the utilisation of new economic opportunities is left solely to the market, growth will occur in the areas that are most advanced in terms of industrial and financial infrastructure, communications etc. Countries with an initial advantage will reap the benefits of co-operation, as illustrated by the position of Kenya in the East African Community (EAC), Zimbabwe in the Federation of Rhodesia and Nyasaland and South Africa in the SACU. The less developed areas become pools of stagnation.

The market forces should in the course of time create a counterforce - the spread effect. This refers to the over-congestion of already developed areas resulting in high costs of manpower, land and services, motivating industry to move into lesser developed areas with lower costs. However, it will take a long time for these diseconomies to manifest themselves, especially in an African context, where labour reserves are abundant even in the relatively industrialised areas. Furthermore, from the manifestation of diseconomies to the actual move into another country there is a great distance in time. First the company would probably move to the provinces of the country where it is already located. Consequently, the spread effect offers little hope of offsetting the inequitable distribution of benefits from market integration. Compensatory and corrective mechanisms have therefore been developed, some of which are described below.

The development integration approach

The development integration approach has one feature in common with the market integration approach: its 'globalist' character. However, in two important areas it differs markedly; i.e. with respect to:

1. Political cooperation and intervention;
2. Distribution of benefits.

In the above discussion of the market integration model it was noted that close political cooperation come in at a rather late stage in the integration process. In development integration, political cooperation on a high level is a prerequisite for successful implementation. This is so because conscious intervention by the regional partners in promoting cooperation and interdependence is the main characteristic of the model. It is not left to the market mechanisms to define the sectors and scope of cooperation. This does not mean that the economies of the participating countries must be centrally directed. It only indicates a higher degree of state intervention compared to market integration. Equally, the creation of supra-national institutions might come at an earlier stage than in the market approach in order to secure that the commonly defined plans are carried out successfully.

The efforts to secure an equitable distribution of the benefits from regional co-operation is an example of how the state intervention is meant to function. One may distinguish between compensatory and corrective mechanisms of achieving this.

The main compensatory measure is inter-government budgetary transfers. These may relate to the cost of trade diversion (which is difficult to calculate) or the custom revenues lost. The latter may be calculated by a formula favouring the Least Developed Members (LDMs). This type of compensation formula is used in the SACU and in the Communaute economique de l'Afrique de l'Ouest (CEAO). In the Economic Community of West African States (ECOWAS) a fund is meant to compensate member-states that will lose from the implementation of the trade liberalisation programme.

However, compensatory mechanisms cannot in themselves change an uneven pattern of economic development. Compensation does not create jobs, industries, spin-off effects, etc. Therefore, they must be coupled with corrective measures, which may be summarised as follows:

1. Planned regional industrial development favouring the LDMs;
2. Creating funds or banks that give priority to the LDMs (as for instance: Central American Bank for Economic Integration (CABEI) does for infrastructure and industrial development project);
3. Allowing the LDMs a longer period to abolish or reduce tariffs (as for instance in ECOWAS and the Andean Pact);
4. Allowing the LDMs to offer specially favourable fiscal incentives for investments.

The compensatory and corrective mechanisms can probably offset the polarisation effect of the trade liberalisation if they are fully implemented. The central problem of the development integration approach is, however, whether such a co-operation, involving binding commitments and possibly direct economic support from the more developed among the less developed countries to the least developed among them, would succeed or not. The LDMs naturally want guarantees for increased national production, but the political situation in their more developed regional partners might not allow for such concessions. The more developed countries, such as Nigeria and Ivory Coast in the ECOWAS, Kenya in the EAC and PTA and Zimbabwe in the SADCC and PTA are core states. Very much depend on their political willingness to use their economic potential in promoting regional economic integration and a reasonable distribution of benefits.

PART IV

COUNTER-TRADE ISSUES

In a study from 1982 the United Nations' Economic Commission for Europe (UN, ECE) defined counter-trade as trading arrangements by which specific interlinkages are established between given import and export transactions. It may also be described as a modified modern version of barter trade which dates back to the days when there was a direct exchange of goods without recourse to financial settlement or transfer of funds. In a recent UNCTAD study, prepared by P.N. Agarwala, it has been pointed out that since 1973 there has been a noticeable movement towards bilateralism in the form of buyback, offset, clearing and long-term trade agreements in response to the global recession, high interest rates and a growing protectionist trend. All of these factors serve to aggravate the accute balance of payments difficulties experienced by developing countries in general and their debt service burden in particular, as well as their desire to promote their new products in new markets as a result of a sharp fall in primary commodity prices on the world market.

Several variants of counter-trade arrangements have been identified. It should, however, be pointed out that since the definition of counter-trade is not precise, it follows that there is a certain degree of uncertainty about definitions of the component parts of the subject.

(i) Barter - involves the exchange of goods against goods without any financial payment and excludes third parties. This is seldom practiced in the modern world.

(ii) Counter-purchase - is a common form of counter-trade between western countries and developing countries or between western companies and East European countries and is increasingly being used among developing countries. It involves an export sale undertaken with the provision that payments will be made partly or fully in commodities, to be settled over a specified time. A major problem with this type of counter-trade is a lack of market transparency. This is particularly true for industrial products which have the greatest potential for variable technical specificaitons and hence a more hidden price structure.

(iii) Trade agreement - coupled with bilateral clearing arrangements are currently in general use both in the developing countries and world-wide. Trade agreements between governments are non-binding expressions of intent to exchange a pre-determined range of products of a specified global value. The agreements are generally of multi-year duration, while the protocols are the implementation instruments of shorter duration, generally one year. This involves the establishment between two countries of a book account to record trade of mutually agreed products to be exchanged. A swing credit limit is also established, and this is the maximum amount that the clearing account can be out of balance and may, depending on the agreement, be settled in convertible currency. The Tanzania/Mozambique Trade Agreement may fit this arrangement.

(iv) Compensation deals or buy-back - are in most cases related to a new (export-oriented) investment, and involve the exporter to furnish machinery, equipment supplies and/or technology for the new production line. Payment is received in terms of products made to his specification as a direct result of the items furnished. The actual trade is the potential additional foreign exchange that could be earned by the new production process without ramifications for existing foreign exchange earnings. This form of counter-trade theoretically results in increased access to technology and a new ongoing source of foreign exchange. However, plans for such agreements should be made very carefully so that they are in accordance with overall development policies.

(v) Offset arrangements - typically relate to government purchases of military hardware and commercial aircraft, where the seller agrees to purchase component parts for these goods or related products from the buyer. Such arrangement have normally been known to take place only between the advanced industrialised countries.

The importance of counter-trade

A few examples of counter-trade illustrate the recent involvement of some of the developing countries, particularly African countries.

(i) Counter-trade deal between Nigeria and Brazil involving the exchange of Nigerian oil for Brazilian manufactured goods and raw materials (1 billion USD).

(ii) Counter-trade deal between Angola and Brazil involving the exchange of Angolan oil for the construction of a dam in Angola by Brazilian companies (700 million USD).

(iii) Counter-trade deal between Iran and Brazil involving the exchange of Iranian oil for Brazilian agricultural and manufactured goods (400 million USD).

(iv) Counter-trade deal between Ethiopia and East Germany involving the exchange of Ethiopian coffee for East German tractors.

(v) Counter-trade deal between Zambia and Romania involving the exchange of Zambian copper for Romanian trucks. In this deal the trucks arrived without spare parts and in poor condition.

(vi) Finally, a counter-trade deal between Tanzania and Bulgaria involving the exchange of semi-finished leather from Tanzania for Bulgarian chemicals.

The rationale for counter-trade and possible benefits

The justification for counter-trade has been summed up in the following words: "It is better to exchange merchandise than to sell nothing at all." The main arguments in favour of counter-trade for the developing countries can be summarised as follows:

(i) Financing imports. There seems to be an obvious correlation between the liquidity crisis in Third World countries and the emergence of counter-trade proposals. The debt service burden of some of these countries had become more onerous just at the time when recession set in, decreasing world demand for their exports and prices for their raw materials. To cope with the resulting lack of convertible currency, many developing countries cut imports drastically. This in turn created supply disruptions that were often aggrevated by a rigid system for rationing the means of payment and a lack of flexibility in the economies. In such circumstances counter-trade is an attractive solution, even if it is makeshift, as it marginally increases opportunities to import and imparts a degree of flexibility to an otherwise rigid system.

(ii) Exchange rate policies. Most of the currencies of the Third World countries are inconvertible, and many of these countries maintain overvalued currencies. However, counter-trade may correct the distortion caused by the unsuitable exchange rate, and the exchange control system which in the first place helps to maintain an overvalued currency may actually encourage it. In this case, counter-trade will be the equivalent of an export subsidy, an import tax or a mixture of both.

(iii) Market access. There are occasions when a developing country may have a short term surplus of a particular commodity which it is finding difficult to sell. Counter-trade may be seen as a mechanism whereby the responsibility of finding a buyer is transferred to a third party while a necessary import is obtained at the same time. In the case of non-traditional exports, the country in question may be facing a real struggle in trying to establish export markets. Counter-trade may be seen as a way of acquiring outside resources to bolster the marketing effort. Alternatively, developing countries may see counter-trade as a way of promoting and stabilizing their exports. This, however, has to be taken lightly; the limitations of counter-trade as outlined below, may actually outweigh the anticipated results.

(iv) Developmental reasons. Buy-back forms of counter-trade, i.e. where suppliers of capital equipment are paid in resultant products, contain certain elements of both developmental and marketing motives. A scheme where mining equipment is paid for in the resultant mineral not only contributes to the development of the mining industry but also provides an assured marketing outlet for the product.

Counter-trade has been seen to provide for the perservation or increase of a long-term market share in other developing countries. Experiences of long-term trade agreements in South East Asia appear to confirm this argument.

A country contemplating counter-trade should always bear two possibilities in mind, one a traditional and the other a counter-trade agreement. As far as possible, normal markets should not be touched by products of counter-trade, especially if it is a question of a traditional product or a limited market. Hence, it can be said that while products of export or import interest vary from country to country depending on the level of development and specific needs, non-traditional items such as garments, footwear, instant coffee, packaged tea, tyres and tubes, cement etc. may be considered products of export interest while capital goods such as construction materials, farm implements, transport equipment, power and electric equipment etc. may be considered products of import interest in any counter-trade deal proposal by a developing country.

Who benefits from counter-trade

While this might be the right question to ask from the point of view of the developing countries, it is a very difficult one to give a clearcut answer particularly in the case of counter-trade between western companies and developing countries.

Let us take as example a case where counter-trade is used to sell surplus bulk commodities. This involves the most common counter-trade situation with western companies and one of the most contentious in terms of benefits. Western counter-trade partners usually prefer to obtain bulk commodities because they are easier to sell and very often the developing countries absorb the counter-trade costs through overvalued imports. In recognition of the dangers that exist in counter-trading primary commodities, many developing countries try to insist on additionality, i.e. the commodities can only be counter-traded if they are incremental sales or are sold to a new market. However, it is very difficult to check on the final destination of the products, and world market for the products may be saturated to the extent tht additionality does not take place.

Another example is where counter-trade is used to sell non-traditional and manufactured exports. From the point of view of the developing countries this may appear beneficial. However, most non-traditional exports from the developing African countries face serious problems of maintaining supplies, as a result of foreign exchange difficulties. The products are often of poor quality and not priced competitively, and hence must be subject to high discounts. Non-traditional exports also face greater problems of tariff barriers and other import restrictions.

Having stated this, one question remains. Could the above transactions have been carried out more profitable through conventional trade? The answer may be negative in which case counter-trade may be justified, particularly if the country concerned is enabled to gain access to a market that it could not have otherwise sold into, and more particularly if the country is able to establish a lasting trading relationship.

However, most counter-trade transactions, particularly those involving western companies and developing countries, are carried out through large trading houses which may lead to increased dependence on these trading houses for the marketing of exports from developing countries. In addition, the challenge to improve quality, delivery schedules, packaging, design, aftersales service and spare parts availability become blunted by easy access to these trading houses and specialised switch traders, who are interested neither in product development nor in the establishment of a long-term supplier-customer relationship.

Where counter-trade results in specific development assistance in the form of technical assistance and the establishment of new projects, it masy be beneficial to the developing country as long as such assistance is consistent with the country's development plans.

Counter-trade between developing countries may not have the drawbacks as described in the examples above. Benefits will primarily derive from increased market opportunity and thereby higher production, incomes and employment, and may accrue to both partners.

Arguments against counter-trade

Counter-trade has been seen as a retreat from the multilateral trading system, under which countries should sell their exports to the highest bidder for convertible currency and buy their imports at the most competitive prices. While a counter-trade deal in fact may offer the best available opportunity for an exporter and importer, such deals nevertheless generally make transactions less clear.

As it has been pointed out above, one of the risks of counter-trade operations is that the country does not generally control the destination of its products and possibilities exist of such a country competing with itself. In disposing his merchandise through counter-trade, the producer deprives himself of direct contact with the market which is the basic source of information for the requirements of a product. This is possible if counter-trade is carried out through large trading houses but less so if the producers are involved in the negotiation process.

The International Monetary Fund (IMF) is opposed to counter-trade for two reasons: financial and ideological. Financial, because counter-trade does not produce the dollars with which to pay off debts, and ideological because counter-trade is seen as a strategy that acts against the liberalisation of trade. The IMF believes that counter-trade restricts multilateral trade, although it may work on a bilateral basis. Its perceived effect so far, however, has been to increase total volume of trade.

Counter-trade has also been seen as a method of delaying difficult economic policy decisions within developing countries. For example, a general devaluation might be more appropriate than de facto devaluations on a transaction by transaction basis through counter-trade.

It has further been argued that counter-trade leads to high transaction costs (discounts, commissions, etc.), is time consuming, results in choice limitations, may involve poor quality products (though not necessarily), and reduces transparency which is an important pre-condition for the efficient working of the international trading system. It has also been argued that counter-trade may lead to products being dumped on particular markets which could cause injury to local suppliers and general disruption. Such accusations may be difficult to prove due to the way in which the prices of counter-traded goods are often determined.