Promoting and Sustaining Trade and Exchange Reform in Africa: An Analytical Framework

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Abstract

This paper documents the recent progress among SSA economies toward integration with international markets. The purpose is twofold. First, the paper identifies significant economic and political obstacles to sustaining trade liberalization;and second identifies ways that successful liberalizers in SSA and other developing regions have been able to overcome these obstacles. The focus is trade reform as an ongoing process, including the packaging of reform measures, their timing and sequencing, and the political-economy issues central to the viability of reforms. In failed SSA reforms, there is a characteristic pattern in which exchange rate and trade policy reforms are set into motion only to be undercut by delays in their implementation or appreciation of the real exchange rate, or abandoned outright in the face of domestic political opposition. Countries following this pattern thereby forego the benefits of reform and also damage the credibility of any subsequent reforms. How can this cycle of reform followed by policy reversal be overcome? In addition to a range of national policy choices,the potential role of regional trade initiatives and aid conditionality in promoting the move to openness among African countries is examined.

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1. Introduction[1]

Sub-Saharan Africa includes several of the world's fastest growing economies (Botswana, Equatorial Guinea, Lesotho, Mauritius, Mozambique, and Uganda) but many more where per capita income is not only low but also stagnant or falling – sixteen countries had lower per capita real income in 1994 than in 1960 (Rodrik 1998). Although war, disease, and drought have blocked economic progress in some areas, the policy decisions of governments in the region are a dominant factor in accounting for SSA's poor economic performance. Underlying every SSA success story are policies that foster integration into regional and global markets. Most stagnating or shrinking economies have been insulated by highly restrictive trade and exchange rate regimes or have a history of policy reversals that aggravate economic difficulties and undermine the credibility of future reforms. However, increased openness is not an end in itself. A few countries (Mali, The Gambia) have undertaken significant trade reforms without enjoying much improvement in growth.[2] Yet there is strong evidence in SSA and worldwide that an open economy is at least an important concomitant of sustained growth and development if not an immediate cause.[3]

This paper documents the recent progress among SSA economies toward integration with international markets. Our purpose is twofold. First, we want to identify significant economic and political obstacles to sustaining trade liberalization; and second we want to identify ways that successful liberalizers in SSA and other developing regions have been able to overcome these obstacles. Our focus is trade reform as an ongoing process, including the packaging of reform measures, their timing and sequencing, and the political-economy issues central to the viability of reforms. In failed SSA reforms, we see a characteristic pattern in which exchange rate and trade policy reforms are set into motion only to be undercut by delays in their implementation or appreciation of the real exchange rate, or abandoned outright in the face of domestic political opposition. Countries following this pattern thereby forego the benefits of reform and also damage the credibility of any subsequent reforms. How can this cycle of reform followed by policy reversal be overcome? In addition to a range of national policy choices, we examine the potential role of regional trade initiatives and aid conditionality in promoting the move to openness among African countries.

An underlying question is whether African leaders are reluctant reformers, looking for ways to meet aid conditions while avoiding real change, or whether, despite deep commitment to change on their part, adverse political and economic circumstances sabotage their best efforts. In Asia and Latin America, donor assistance supported market-oriented reforms and helped countries overcome the difficulties of adjusting to a new policy regime. In Africa, evidence for this kind of supportive role is far less compelling. Indeed, the record in a number of countries shows decades of financial inflows with little or no improvement in economic performance. This raises the possibility that, rather than facilitating economic or political reform, donor assistance has allowed some recipient countries to postpone needed change and even helped to maintain the viability of corrupt leaders in the interest of preserving political stability in a volatile region. The case of Mobuto Sese Seko in the former Zaire, while perhaps the most notorious example, has unfortunately not been an anomaly in the African context.

Our discussion is arranged as follows. The following section describes the context within which trade and exchange rate reforms are typically being promoted. In many cases, countries in SSA are attempting to encourage trade and exchange rate reform from positions where their external imbalances are large and confidence in the economy and the efficacy of policy is low. They are frequently pursuing these reforms in the context of a donor-supported adjustment program. Most of these programs have far too many activities for African countries to pursue simultaneously. Under these conditions, policy reversals and lack of reform are often pre-programmed.

Sections 3 examines liberalization as a sequential process. It discusses how to get reform started, how to maintain popular support, and the factors that lead to policy reversals. Section 4 addresses how to break the cycle of policy reversals. It highlights the importance of macroeconomic discipline, an appropriate real exchange rate, and a constructive approach to globalization. Section 5 has concluding comments.

2. The Context of Trade and Exchange Rate Reforms

a. The Setting

Over a period in which international trade has played an increasing role in promoting economic growth and development, SSA's share of global exports has fallen dramatically, shrinking from 3.8 percent in 1970 to 1.5 percent in 1995 (World Bank 1998).[4] In part this decline reflects the low GDP growth rates of most African countries relative to average growth worldwide. SSA's share in world GDP fell from 1.6 percent in 1970 to 1.4 percent in 1995. With this slower overall growth, SSA's share of global exports would have shrunk even if the region maintained or increased its degree of openness to trade. However, the degree of openness was not maintained, let alone increased. Of 33 SSA countries for which comparable data are available, 20 showed an actual drop in trade as a share of GDP between the early 1980s and the early 1990s (World Bank 1997b, Table 6.1).[5]

Nor can the collapse of African trade be attributed to increased protection in the OECD market countries. Indeed, due to the activities of the General Agreement of Tariffs and Trade and the World Trade Organization, there has been unilateral lowering of trade barriers in most countries, resulting in a sharp decline in the protectionism faced by African exports over the last two decades. It is simply not true (as many African leaders and officials maintain) that discrimination against African exports by OECD countries has been an important explanation of the slow growth of African trade.

The most important factor in the slow growth of African trade has been the countries' own policies, which have undermined domestic growth, thereby reducing domestic producers' ability to compete internationally and discouraging diversification out of traditional commodity exports (Yeats *et al*. 1997). The key factors holding back SSA exports are restrictive trade practices and inappropriate exchange-rate regimes, together with slow growth or even deterioration of physical infrastructure to facilitate trade. The latter is especially important for the fourteen landlocked countries in the region. Econometric studies (Sachs and Warner 1996, Radelet, Sachs and Lee 1997) find that landlocked status has a statistically significant depressing effect on trade and growth. Such evidence highlights the importance of physical investments and institutional arrangements that can help landlocked countries overcome their comparative disadvantage.

Moreover, while aid donors have increasingly linked grants and loans to policy reforms intended to promote openness, the marginalization of Africa in world trade has not been reversed even for some countries that have been relatively successful in meeting policy conditions imposed by donors. Zambia, cited as a successful liberalizer in Sharer *et al*. (1998) for achieving the trade policy reforms agreed with the International Monetary Fund (IMF) and World Bank for the period 1990-1996, nonetheless had lower ratios of both exports to GDP and imports to GDP in 1995 than in 1980 (World Bank 1997b, Table 4.12). On the export side, this unfavorable trend mainly reflects the sharp decline in the volume of Zambia's major export, copper[6] (World Bank 1997b, Table 4.7). Although Zambia experienced rapid growth in both the value and volume of non-traditional exports, these were inadequate to offset the decline in copper exports. On the import side, volume actually shrank over the same period, reflecting compromises made in achieving the conflicting goals (and IMF conditions) of tariff reduction and revenue enhancement. It also reflected the continued decline in real per capita income due in part to the delayed implementation of parts of other elements of the reform package, such as the sale of the copper mine and delay in civil service reform. The case of Zambia also illustrates another problem typical of African economies. Many depend on one or two primary commodities for the bulk of their foreign-exchange earnings, so that price swings in global markets cause fluctuations in prices, incomes, and government revenues (Rouis, Razzak, and Mollinedo 1994, Table A.4).

b. Progress toward Liberalization in SSA

In an effort to cope with the world's highest per capita debt burdens and raise the rate of economic growth – and in response to strong encouragement from the World Bank, IMF, and bilateral aid agencies – many African countries agreed to undertake economic reforms that always included liberalization of trade and reform of exchange rate regimes. Implementation of these reform programs has been halting, and policy reversals common. The outcome for SSA is a patchwork of experience: some countries have made important advances; others have advanced for a period, then regressed; still others have simply regressed.

To evaluate progress toward openness in the countries of SSA, an important first step is to consider the menu of policy changes potentially included under the general heading of trade liberalization. In the early 1980s, most SSA countries were insulated from world markets by relatively high tariffs, licensing requirements and selected non-tariff barriers, as well as highly restrictive exchange control regimes in the non-CFA countries. However, these multiple distortions were not usually cumulative in their effects on trade flows. Rather, the binding constraint on trade of non-CFA countries was typically quantitative restrictions or exchange controls. The region's high tariff rates were often redundant as a barrier to imports, although important as a source of government revenue (Nash 1993). Exports were likewise constrained by overlapping and often redundant policies including overvalued exchange rates, sub-market prices paid to suppliers by export marketing boards, export bans or licensing, and the required repatriation of foreign exchange proceeds at the official exchange rate.

This pattern of multiple and partially redundant trade disincentives has several important implications for the analysis of trade liberalization in SSA. First, the analysis cannot usefully concentrate on tariffs alone, or even on tariffs and quantitative trade restrictions. Rather, the definition of liberalization must encompass exchange-rate policy and marketing arrangements as well as the narrower range of policies that affect trade directly. Second, tariff reductions in the absence of progress on exchange rate reform and elimination of quantitative restrictions tend to worsen the country's budgetary problems without achieving a compensating boost to allocative efficiency. (As discussed below, IMF advice has stressed a first stage of tariffication of non-tariff measures, viewed as a revenue-enhancing step toward greater policy transparency.) Third, seemingly gradual programs of policy reform may be associated with a pattern of little or no actual adjustment for some period, followed by a sharp drop in domestic industries' insulation from world markets as the final and binding layer of protection is dismantled (Nash 1993). In this case, gradualism intended to reduce adjustment costs or ease political acceptance of reforms is often counterproductive. Finally, the intent of donor conditionality spelled out in terms of any subset of policy measures may be successfully evaded by substitution of other policies. This problem is hardly unique to Africa, but it is perhaps more significant there to the extent that the role of external pressure in shaping policy change is more important, either because of weaker domestic support for reforms or because of the relatively larger scale of ODA in the region.

Based on successful liberalization episodes in Asia and especially Latin America, analysts would be likely to characterize trade reform in terms of substantial across-the-board tariff cuts. However, as shown in Table 1, taxes on international trade are a major source of revenue in SSA accounting for up to half of total revenue in some countries. It is not surprising, therefore, that average tariff rates have fallen relatively little in SSA in comparison to the dramatic reductions achieved in a number of Latin American and East Asian countries. Yet Mauritius, despite an especially high dependence on trade taxes, has been one of SSA's most successful trade liberalizers.[7]

Liberalization episodes in other developing regions have rarely involved increases in average tariff rates or even concertina-type increases in the lowest rates (Michaely *et al.* 1991). In Africa, however, the importance of tariffs in generating government revenue and the large *ex ante* role of quantitative restrictions imply that cuts in average tariffs would be neither necessary nor sufficient for reducing trade distortions. Moreover, in the presence of the pervasive foreign exchange controls and exchange rate manipulation characteristic of countries outside the CFA zone, even large across-the-board tariff cuts might in any case have had little or no effect on actual trade flows unless accompanied by liberalization of the exchange regime.

A further issue is that outward-oriented reforms in a number of Asian and Latin American countries have focused on creating new incentives for exporting, especially of nontraditional export products, and to non-traditional markets. Moreover, it is common for countries to maintain import-substitution policies in some industries while offering export incentives in others, or even to tax traditional exports while promoting nontraditional exports. Most SSA countries have likewise implemented this approach, but with far less evidence of success in achieving the goal of export expansion and diversification. Mauritius is an exception. It developed an export-processing zone long before reducing protection of its import-competing industries.

Export-enhancing policies successful in East Asia included keeping the real exchange rate at a level consistent with profitable exporting and allowing exporters relatively free access to imported inputs at world prices and without administrative delays (Thomas, Nash *et al*. 1991). In contrast, SSA currencies were notably overvalued until reforms in the mid- to late 1980s for non-CFA countries and the January 1994 devaluation of the CFA franc. As shown in Table 2, there was some depreciation of the exchange rates for many countries in the early 1990s. This situation reversed during the latter part of the decade. Over this period, for example, the real exchange rates in Cameroon, Burundi, Democratic Republic of Congo, Côte d'Ivoire, Ghana, Nigeria, and Zambia (to name some) appreciated by more than twenty-five percent (World Bank 2000, Table 5.6). The use of tariff exemptions on imports to encourage export activity has been severely limited in SSA by fiscal problems, administrative delays, and corruption. Furthermore, as shown in recent research on tax compliance, there has been a significant gap between nominal tax rates and effective tax rates (Andrianomanana *et al.* 1998, Table 8; Gray *et al.* 2000, Table 2). Because of their poor track record of implementation, fiscal incentives lack credibility and thus have little if any impact on the behavior of potential exporters – including potential direct investors. Perhaps because tariff exemptions have generally been ineffective in promoting SSA exports, IMF advisors have emphasized their elimination to maintain needed revenue while cutting tariff rates (Sharer *et al*. 1998).

Table 1. International Trade Taxes as a Percent of Total Central Government Revenue

Country	1980	1990	1996	1997	1985-89	1990-97
					annual average	
Angola	..	0.9	4.30	5.6	3	5.2
Benin	..	41.7	40.9	45.5	39	41.5
Botswana	..	13.2	12.3	..	13.1	16.3*
Burkina Faso	..	38.3	47.0	46.9	44.9	43.2
Burundi	30.8	21.0	17.7	24	33	23.5
Cameroon	..	15.4	20.0	17.3	17.7	17.3
Cape Verde	..	43.8	44.5	41.8	40.4	43.9
Central African Rep.	..	39.8	38.9	38	31.9	37.1
Chad	..	24.4	31.2	30.3	26	22.1
Comoros	..	41.8	33.9	43.1	48.4	36.9
Congo	..	16.0	16.3	8.5	21.5	16.6
Côte d'Ivoire	..	26.2	39.6	36.5	34.9	32.9
Equatorial Guinea	..	32.2	19.0	19.8	42	26.5
Eritrea	..	..	19.7	15.2	..	20
Gabon	..	19.2	19.6	18.8	..	19.1
Gambia, The	..	54.0	61.9	59.3	55.2	51.4
Ghana	..	38.7	35.2	27.2	39.1	33.4
Guinea	..	8.7	14.1	15.4	6.4	13.4
Guinea-Bissau	..	25.2	32.9	28	21	28.2
Kenya	..	..	14.9	14.1	..	12.2
Lesotho	..	55.3	50.4	..	57.3	54.8*
Madagascar	..	46.2	53.3	52.9	40.5	47.7
Malawi	..	32.5	39.4	36.9	26.2	35.8
Mali	..	26.4	45.9	49	27.2	42.8
Mauritania	..	28.6	15.9	12	32.9	26.5
Mauritius	..	49.4	36.1	34.3	52.9	42.1
Mozambique	..	21.9	19.9	17.7	..	22.7
Namibia	..	26.5	29.2	29.9	33.5	29.9
Niger	..	39.5	46.7	47.7	34.7	41.8
Rwanda	..	27.5	29.2	32.1	45	31.6
Sao Tome and Principe	..	3.9	21.8	11.8	32.1	7.1
Senegal	..	..	33.7	30	..	30.8
Sierra Leone	..	25.1	42.2	..	29	32.9*
South Africa	..	4.9	3.6	3.4	4.8	3.4
Swaziland	..	..	51.1	..	..	47.6*
Tanzania	..	24.3	27.0	30.4	20.3	24.4
Togo	..	37.9	41.2	44.3	34.4	39.2
Zaire	..	31.7	24.6	23.1	24.7	27.6
Zambia	..	36.1	29.7	28.2	29.8	31.4
Zimbabwe	..	..	17.0	16.7	..	16.9

Note: * Annual average for 1990-96

Source: African Development Indicators, 1998/99, Table7-10

Recent reform programs in SSA have been designed with multiple linked objectives, including macroeconomic stabilization (reducing the domestic fiscal deficit and inflation), correcting domestic market distortions, and promoting openness to trade and inward direct investment. Because so many policy variables potentially affect a country's trade, even the direction of the net change in openness or outward-orientation can be less than obvious. The classic National Bureau for Economic Research (NBER) study of trade reform in developing countries counts as liberalization any policy change that reduces the anti-export bias of a country’s trade regime (Bhagwati 1978; Krueger 1978). By the Bhagwati-Krueger criteria, the explicitly targeted export incentives often used in East Asia qualify as liberalization.

Baldwin (1989) distinguishes between *incidence-based* measures of policies affecting trade, such as average tariff rates, and *outcome-based* measures, usually the relative size of trade flows. Because many factors apart from policies toward trade affect openness as measured by the relative importance of trade, outcome-based measures are useful in evaluating change in the openness of a single country rather than in making comparisons across countries. Moreover, a country may reduce its tariffs, thus appearing to liberalize according to one incidence-based measure, yet maintain import licensing arrangements or exchange controls that in effect nullify the reduced import barriers. In this case, an outcome-based measure such as the ratio of trade to gross domestic product (GDP) will show little progress. For most SSA countries, outcome measures may be the only practical means of evaluating changes in policy regimes in a timely manner. While most countries publish aggregate trade data on a reasonably current basis, meaningful incidence-based measures are unavailable or available only with a very long lag.

Pritchett (1996) proposes three concepts of trade liberalization or outward orientation. *Neutrality* refers to a reduced bias in favor of production of import-substitutes, *liberality* to a lower degree of market intervention, and *openness* to an increase in trade intensity. Comparing alternative summary measures of outward orientation from the recent empirical literature on growth and openness, Pritchett shows the indicators to be almost completely unrelated in cross-country data for less-developed countries. This finding suggests that openness has several dimensions. Countries making the best progress according to one measure will not necessarily look as good in terms of another.

Whereas broad reductions in tariffs and non-tariff barriers qualify under all three of Pritchett's concepts, some export-promotion efforts in East Asia have improved neutrality and openness while increasing rather than reducing the extent of market intervention. As elsewhere, the move toward outward orientation in SSA has been far from synonymous with *laissez faire*. Although some SSA countries have liberalized trade and foreign-exchange restrictions while at the same time pursuing other market-oriented reforms, nowhere in SSA has trade reform been imbedded in an all-encompassing movement toward free-market policies such as that in Chile. However, data from a range of sources suggest that some countries, by removing quantitative restrictions, reducing foreign exchange premia, lowering tariff rates and reducing their dispersion, have made progress according to all three types of indicators (UNCTAD 1994; Dean 1994).[8]

Table 2. Exchange Rates by Country, pre-reform and 1997

Country	Date of Reform	Ratio of Parallel Market to Official Ex. Rate (n.c. per USD)					1997 REER
		1980	1985	1990	1995	1997	(1990=100)
Angola		.	..	..	..	1.40	..
Benin	1994*	0.99	0.99	1.04	1.00	1.02	..
Botswana	1986-87	1.03	1.37	1.02	1.01	1.00	..
Burkina Faso	1994*	0.99	0.99	1.04	1.00	1.02	..
Burundi	1986	1.18	1.16	1.09	1.36	1.30	85.6
Cameroon	1989*, 1994*	0.99	0.99	1.04	1.00	1.02	49.7
Cape Verde		..	..	..	1.16	1.07	96.7
Central African Republic	1994*	0.99	0.99	1.04	1.00	1.02	63.1
Chad	1994*	0.99	0.99	1.04	1.00	1.02	66.9
Comoros		0.99	0.99	1.04	1.04	1.07	..
Congo, Democratic Rep.		..	..	..	1.06	..	..
Congo, Republic of	1994*	0.99	0.99	1.04	1.00	1.02	77.6
Côte d'Ivoire	1984-86, 1990*, 1994*	0.99	0.99	1.04	1.00	1.02	77.8
Djibouti		..	1.09	1.08	1.12	1.03	..
Equatorial Guinea	1994*	0.99	0.99	1.04	1.17	1.02	..
Eritrea		..	..	..	..	..	..
Ethiopia		1.35	2.32	2.90	1.74	1.12	..
Gabon	1994*	0.99	0.99	1.04	1.00	1.02	62.4
The Gambia	1985	0.99	0.95	1.05	1.09	1.06	..
Ghana	1983 (1987*)	5.78	2.42	1.11	1.02	1.01	113.3
Guinea		2.20	12.77	1.05	1.03	1.03	93.3
Guinea-Bissau		..	..	..	..	1.02	..
Kenya	1985	1.11	1.05	1.02	1.04	1.06	94.7
Lesotho		..	1.08	1.04	1.02	1.02	92.1
Liberia		..	..	..	42.30	48.50	..
Madagascar	1987*	1.25	1.04	1.06	1.03	1.10	96.3
Malawi	1988*	1.97	1.45	1.21	1.09	1.07	104.6
Mali	1986*, 1994*	0.99	0.99	1.04	1.00	1.02	58.6
Mauritania		1.42	2.17	..	1.07	1.05	79.9
Mauritius		..	0.93	1.06	1.05	1.04	..
Mozambique		2.47	40.53	..	1.09	1.09	67.9
Namibia		..	..	..	..	1.07	101.2
Niger	1994*	0.99	0.99	1.04	1.00	1.02	..
Nigeria	1986-88*	1.65	4.25	1.16	3.58	3.87	193.1
Rwanda		1.24	1.37	1.26	1.02	1.20	65.4
Sao Tome and Principe		..	..	..	1.06	1.60	17.0
Senegal	1986-89*, 1994*	0.99	0.99	1.04	1.00	1.02	59.9
Seychelles		..	..	1.11	1.17	1.22	..
Sierra Leone		1.33	1.51	3.11	0.98	1.18	..
Somalia		1.57	2.66	..	..	..	..
South Africa		1.16	1.08	1.04	1.02	1.02	96.6
Sudan		2.00	1.43	9.69	0.13	..	..
Swaziland		..	1.08	1.04	1.08	1.07	..
Tanzania	1986, 1996*	2.56	3.81	1.50	1.02	1.07	134.5
Togo	1994*	0.99	0.99	1.04	1.00	1.02	..
Uganda	1987*	1020.63	149.74	1.60	1.11	1.09	67.6
Zambia	1991, 1990-95, 1996	1.65	1.53	4.00	1.09	1.19	117.5
Zimbabwe		1.71	1.49	1.35	1.03	1.15	82.6

Sources: ADI 1998/99, World Bank; IMF Staff Country Reports, IMF.

Table 3 has data on the mean tariff, the standard deviation, and the weighted mean tariff on all products for selected countries in SSA. These data show that the average level and standard deviation of the tariff rates is high. The data for South Africa suggest that there has been substantial reform in lowering and evening out the tariff structure. Data from Malawi indicate that the progress has been more modest.

Table 3. Selected Tariff Barriers, Sub-Saharan Africa (All Products)

Country	Year	Mean Tariff	SD of Tariff	Weighted Mean Tariff
Central African Republic	1995	18.6	9.6	17.1
Malawi	1994	30.8	15.5	27.1
	1997	25.3	11.6	23.5
Mauritius	1997	29.1	26.2	31.9
Mozambique	1997	15.6	14.3	14.1
South Africa	1993	19.7	21.9	14.3
	1997	8.7	10.9	6.6
Zambia	1997	13.6	9.3	14.3
Zimbabwe	1997	24.0	23.1	21.7
	1998	22.2	17.8	20.0

Source: World Bank *World Development Indicators* 2000, Table 6.6

Because the inefficiency associated with protection comes in part from "chaotic" incentives (Bhagwati 1978), tariff reform is most beneficial when it is associated with a reduction in the dispersion of rates as well as in their average height. IMF and World Bank advisors have stressed the goals of reducing the number of tariff bands, reducing high tariffs while raising especially low ones, eliminating tariff exemptions, and substituting equivalent tariffs for non-tariff distortions – the last three serving also as ways of maintaining government revenue. This was done in Zambia between 1992 and 1995 with positive effects (Hill 1999). In trade policy reviews of five members of the Southern Africa Customs Union (SACU), the World Trade Organization (WTO) Secretariat points out that SACU's external tariff, determined by South Africa, is both complex and subject to frequent changes. WTO officials judge that a simpler and more stable tariff structure would help SACU members attract more foreign investment (WTO 1998).

A flat tariff schedule such as Chile's gives most domestic production a uniform advantage over competing imports. A flat schedule implies that effective protection rates are the same as nominal rates. A formal commitment to maintaining a flat schedule can help policy makers resist lobbying by producers who seek higher-than-average protection for their outputs or lower-than-average protection for their imported inputs. Where detailed tariff rates are available, dispersion can be measured by the standard deviation. A cruder measure of deviation from a flat schedule is the ratio of the average maximum tariff rate to the average minimum rate. The higher the ratio, the greater is the possibility that effective protection rates have been maintained or even increased despite reductions in both averages.

In addition to direct restrictions on trade flows, the foreign-exchange regime is an important dimension of outward orientation. Devaluation of an overvalued currency fits the Bhagwati-Krueger definition of trade liberalization since it reduces the bias against exports across the board. Similarly, the composite binary measure of openness adopted by Sachs and Warner (1995a) classifies a country as closed if even one of several criteria of significant insulation from global market forces apply. In the Sachs-Warner scheme, removal of trade barriers alone is insufficient to qualify as opening up if the real exchange rate remains so overvalued as to prevent development of export activities along lines of comparative advantage. Other analysts focus on changes in trade policies only and treat exchange rate policy separately if at all.[9]

Of the 13 SSA countries studied by Dean, Desai, and Riedel (1994), four were CFA zone members with currencies already considered overvalued in 1985, the start of the study period. Moreover, these four countries experienced further real appreciation until the devaluation of the CFA franc by 50 percent[10] in January 1994. Of the nine non-CFA countries in the study, all but South Africa had double-digit or triple-digit black market premia from 1980 until the reform year in the period 1986-89, reflecting highly distorted regimes. All eight of these countries undertook varying degrees of exchange rate reforms, in some cases eliminating multiple exchange rates and abolishing most foreign exchange controls. All had sharply reduced premiums in the post-reform period. Moreover, the countries with the highest black market premia prior to reform achieved the largest reductions in their premia. In Ghana, with the largest average premium (984.6 percent) in the period prior to reform, the premium dropped to an average of 16.5 percent in the post-reform period through 1992. For the region as a whole, the overall effect of reform was to sharply reduce the black market premia.

Foreign exchange controls are almost always associated with the maintenance of an overvalued official exchange rate, although the black market premium is likely to overstate the extent of overvaluation.[11] Liberalization of the exchange regime is therefore typically accompanied by a nominal devaluation of the currency. But while adoption of a more liberal exchange regime increases allocative efficiency in international transactions and reduces losses from rent-seeking, it does not ensure that an exchange rate broadly consistent with purchasing power parity will be maintained over time. A market-based exchange rate will reflect capital- as well as current-account transactions. In some East Asian and Latin American countries, private capital inflows have produced a tendency toward real appreciation and an accompanying tendency toward current-account deficit. In SSA, the large size of aid flows combined with debt relief also tends to promote real appreciation, or at least to reduce downward pressure via market forces.

For World Bank-supported reform programs in the 1970s and 1980s, Michaely, Papageorgiou, and Choksi (1991) note that devaluation was a universal element in stabilization packages and a "common – sometimes crucial – instrument of trade liberalizations, even those not associated with stabilization programs." Among the nine non-CFA countries studied by Dean *et al*. (1994), six experienced a decline in the real exchange rate in conjunction with trade policy reforms, with further falls through 1992. Real devaluation should have helped to shift domestic production in favor of tradable goods, thus promoting export growth. But as these countries succeeded in implementing and sustaining market-oriented policy reforms, inflows of private capital and/or official development assistance have contributed to real appreciation and thus slower export growth.

Because the ultimate goal of policy reform is to accelerate economic growth, the most important outcome measure is the rate of growth. Data in Table 4 show that there has been relatively limited success in this regard. While there has been no evidence of a major boost in average growth across Africa, a significant number of countries have continued to grow (albeit at slow rates). Nonetheless, while income growth has been robust in some countries, the same has not been true of export growth. This shows wide variability.

Of course, many types of policy change as well as significant external shocks contributed to overall economic performance in SSA (Easterly and Levine 1995). Perhaps the most important domestic policy influence has been macroeconomic stabilization, including improvement in fiscal balance (Calimitsis, Basu, and Ghura 1999). Even within the category of efficiency-enhancing structural reforms, trade liberalization is only one of a broad spectrum of market-oriented policies implemented since the mid-1980s. However, the data confirm that the sustained trade reforms in some countries (Mauritius, Botswana, Uganda, Ghana) have at least been consistent with higher overall growth rates. For the region as a whole, the weighted average of the annual growth rates was 2.1 percent from 1991 to 1996, compared to 1.7 percent for the previous decade (World Bank 1997a, 1998). Though welcome, this growth spurt has not been sustained. The financial difficulties in Asia in 1997 and Russia and Brazil in 1998 had a major adverse effect on commodity prices. Moreover, there was a general slackening of the commitment to reform across Africa and the emergence of several major trouble spots (Democratic Republic of Congo, Sierra Leone, Côte d'Ivoire, and Eritrea/Ethiopia).

Table 5 dates the initiation of trade reforms in SSA countries as determined in several recent studies using alternative criteria. The table also indicates the influence of IMF and World Bank programs. (Michaely, Papageorgiou, and Choksi 1991). Thomas, Nash et al. (1991) cite external financing between 1979 and 1987 from the World Bank and the IMF as "intended to facilitate trade policy change" in 19 of 37 SSA countries. However, from the late 1980s onward, virtually all SSA reformers have benefited from after-the-fact external technical and financial support from the World Bank and IMF. By early 1997, 37 countries in SSA had joined the WTO.[12] By the latter part of the 1990s, many of these countries were also members of one or more regional trade arrangements (see Table 6).

3. Liberalization as a Sequential Process

Why have some nations in SSA been able to achieve and sustain an open economy while others – often guided by the same received wisdom and even the same advice from foreign experts dispatched by the same agencies – failed to do so? And why has SSA as a whole lagged behind other developing regions in moving toward integration with international markets? The answers lie in the complex interplay of economics and politics that is central to the process of liberalization. Policies are inherently endogenous, shaped by underlying political as well as economic forces. The economic results of implementing each new policy alter the political balance within a country, thus strengthening or weakening the position of reformers.

To consider the characteristics of successful and sustained trade reform, it is helpful to divide the liberalization process into four components: (1) the design of a policy package; (2) its acceptance and endorsement by top policy makers and later by the public; (3) its implementation in specific policy measures and their administration; and (4) the economy's response to changed incentives. Completing the political-economic cycle, the last component influences the degree of support for the reforms from the policy community and the public and thus the perceived need for modification of the package.

Table 4. Exports and Economic Growth

Country	1997 GDP	1997 Exports*	1997 GNP p.c.	Exports* (% of GDP)		Exports* Growth (%)		GDP Growth (%)	
	(bill. '87 USD)	(bill. '87 USD)	in USD**	1980	1997	1980-90	1990-97	1980-90	1990-97
Angola	7.7	4.8	340	..	67.8	..	7.5	..	-1.6
Benin	2.1	0.4	380	23.0	24.7	-1.4	3.6	3.5	4.1
Botswana	3.2	..	3,260	49.9	..	..	1.1***	10.5	4.7
Burkina Faso	3.0	0.3	240	10.1	13.2	1.3	-0.2	3.2	3.2
Burundi	1.0	0.1	180	8.8	8.1	5.4	-1.3	4.2	-2.8
Cameroon	10.5	2.9	650	26.9	27.0	9.7	1.5	3.1	-0.9
Cape Verde	0.3	0.1	1,090	..	25.4	..	8.7	..	3.4
Central African Rep.	1.3	0.2	320	25.2	20.9	-0.4	0.4	0.9	0.7
Chad	1.9	0.2	240	16.9	16.9	8.8	2.0	4.6	4.2
Comoros	0.2	0.1	400	8.9	22.2	..	10.3	..	-0.1
Congo, Dem. Rep.	4.6	0.9	110	16.5	24.0	9.7	-9.2	1.0	-6.4
Congo, Rep.	2.6	1.8	660	60.0	76.9	7.3	5.4	6.5	0.7
Côte d'Ivoire	12.8	5.9	690	35.0	46.6	8.4	4.3	-0.3	2.4
Djibouti	..	..	..	..	..	..	..	..	..
Equatorial Guinea	0.4	0.9	1,050	..	100.4	..	44.4	..	13.0
Eritrea	..	..	210	..	30.8	..	..	..	..
Ethiopia	9.8	1.0	110	..	15.9	..	4.9	..	3.5
Gabon	5.3	3.0	4,230	64.7	64.0	4.4	5.1	1.0	3.3
The Gambia	0.3	0.2	350	42.7	47.2	6.0	-1.6	2.8	2.4
Ghana	7.9	1.9	370	8.5	24.8	2.2	7.1	2.2	4.4
Guinea	3.1	0.9	570	..	21.3	..	2.4	..	4.0
Guinea-Bissau	0.3	0.1	240	12.6	21.1	2.0	14.5	3.0	3.6
Kenya	10.6	2.6	330	27.9	29.2	4.9	3.9	4.3	2.1
Lesotho	0.8	0.2	670	20.1	..	2.3	7.6	3.7	7.0
Liberia	..	..	..	55.0	..	..	..	..	..
Madagascar	3.0	0.7	250	13.3	22.4	-2.0	4.5	0.6	0.7
Malawi	1.7	0.4	220	24.8	25.1	5.1	4.4	2.1	3.5
Mali	2.8	0.7	260	15.6	25.4	6.8	6.9	1.7	3.0
Mauritania	1.3	0.4	450	37.4	45.3	4.5	-0.5	1.8	3.7
Mauritius	3.2	2.2	3,800	51.1	62.0	8.4	5.8	4.6	5.2
Mozambique	3.1	0.7	90	15.0	18.2	..	17.6	..	4.2
Namibia	2.8	1.8	2,220	76.5	..	..	5.5	..	3.5
Niger	2.6	0.4	200	24.6	16.1	-7.9	-1.1	0.1	1.1
Nigeria	37.1	12.6	260	29.4	40.9	-2.4	6.0	1.8	3.2
Rwanda	1.8	0.1	210	14.4	6.0	1.9	-11.3	2.9	-5.5
Sao Tome & Principe	0.1	..	270	46.5	..	7.9	-3.0***	2.7	1.2
Senegal	5.9	1.8	550	26.9	32.5	4.3	4.8	2.7	2.4
Seychelles	0.4	0.3	6,880	68.0	67.7	..	-1.0	2.8	3.5
Sierra Leone	..	..	..	27.9	..	2.5	-14.1***	1.4	-3.3
Somalia	..	..	..	33.1	..	..	..	1.5	..
South Africa	95.0	39.4	3,400	35.9	27.8	1.5	4.6	2.0	1.2
Sudan	..	..	280	10.6	..	0.1	..	1.3	..
Swaziland	0.9	0.6	1,400	69.4	72.9	11.0	1.4	6.7	3.2
Tanzania	4.7	1.5	210	..	..	..	13.0	..	2.8
Togo	1.6	0.5	330	51.1	32.8	2.8	-1.6	2.4	1.2
Uganda	12.4	1.6	330	19.4	11.0	..	14.4	..	7.2
Zambia	2.4	0.7	380	41.4	29.8	-3.7	-1.1	1.2	-0.4
Zimbabwe	9.4	3.6	750	23.4	37.3	6.8	10.1	4.5	2.1

Notes:* - Exports of Goods and Non-Factor Services
** - Atlas method
*** - Average Annual Percentage Growth 1990-96
Source: African Development Indicators 1998/99, World Bank

Table 5. Trade liberalization in Sub-Saharan Africa

Country	Sachs-Warner (1995a) Date of opening	Dean et al. (1994) Initiation of reforms (1985-1991)	Sharer et al. (1997) Initiation of IMF-supported programs with trade objectives	Thomas and Nash (1991) Recipient of World Bank trade adjustment loan, 1979-87
Angola	Never open	Not covered		
Benin	1989	Not covered	ESAF 1993, no progress toward target (6,6)	
Botswana	1979	Not covered		
Burkina Faso	Never open	Not covered	SAF 1991, ESAF 1993, target achieved (10,7)	
Burundi			ESAF 1991	x
Cameroon	1993	1989		
Cent. Afr. Rep.	Never open	Not covered		x
Chad	Never open	Not covered		
Comoros			SAF 1991, target achieved (10,8)	
Congo	Never open	Not covered		
Côte d'Ivoire	Never open	(1984-86) 1990		x (intensive)
Ethiopia	Never open	Not covered	SAF 1992, target achieved (10,8)	
Gabon	Never open	Not covered		
Gambia	1985	Not covered		
Ghana	1985	1987		x (intensive)
Guinea	1986	Not covered	ESAF 1993, target achieved (5,3)	x
Guinea-Bissau	1987	Not covered		x
Kenya	(1963-67) 1993	1987		x
Lesotho			ESAF 1991, no liberalization targeted (8,8)	
Madagascar	Never open	1987		x
Malawi	Never open	1988		x (intensive)
Mali	1988	1986	ESAF 1992, target achieved (8,5)	
Mauritania	1992	Not covered	ESAF 1992, no liberalization targeted (9,9)	x
Mauritius	1968	Not covered		x (intensive)
Mozambique	Never open	Not covered	ESAF 1990, target achieved (10,6)	
Niger	Never open	Not covered		x
Nigeria	Never open	(1986-1988)		x
Rwanda	Never open	Not covered	ESAF 1991	
Senegal	Never open	(1996-89)		x (intensive)
Sierra Leone	Never open	Not covered	ESAF 1992, no liberalization targeted but some achieved (5,4)	
Somalia	Never open	Not covered		
South Africa	1991			
Tanzania	Never open	1996	ESAF 1991, target achieved (9,5)	x
Togo	Never open	Not covered		x
Uganda	1988	1987		
Zaire	Never open	1990		x
Zambia	1993	Not covered	ESAF 1992, target achieved (7,4)	x
Zimbabwe	Never open	Not covered	EFF 1992, ESAF 1992, reform but short of target (10,8)	x

Notes: Sachs and Warner (1995a) classify a country as open if nontariff barriers cover less than 40 percent of trade, the average tariff rate is less than 40 percent, the black market exchange rate of the domestic currency is less than 20 percent below the official rate, and there is no government monopoly on major exports. Dates in parentheses indicate liberalizations satisfying these criteria that were later reversed. Other dates are based on trade policies only. Dean, Desai, and Riedel (1994) and IDB (1996) cover liberalizations initiated since 1985.

Viewed within this sequential process, a reform package may fail for several reasons. First, the policies themselves may be poorly conceived or inappropriate to the country's economic or political circumstances. Second, the package, though well designed and appropriate, may nonetheless fail to gain the support of a country's political leadership. Third, even an exemplary package that enjoys the support of top policy officials may be aborted if the relevant legislative and administrative bodies are unwilling to implement it. Fourth, elements in the economic environment may prevent markets from responding appropriately to the changed incentives. Finally, the elements of the package, though well-designed and appropriate to the task of trade reform, may be beyond the capacity of individual governments to implement.

The record of SSA shows some progression over these stages. Until the 1980s, widespread doubt still remained concerning the type of policies to follow; proposals for development through import substitution continued to enjoy wide support among SSA economists as well as policy makers. To many, the domestic dislocations from the first oil shock, followed by steep declines in many primary export prices in the late 1970s, vividly demonstrated potential dangers of full integration into international markets. By the late 1970s the intellectual case for open markets was ascendant in multilateral agencies, but many SSA policy makers remained unconvinced. Further oil-price increases, together with the debt crisis that began in 1982, added to their skepticism. These external shocks increased policy makers' distrust of openness and foreign advice, but at the same time increased the leverage of multilateral agencies as the share of aid in GNP increased from a regional weighted average of 3.4 per cent in 1980 to 16.3 percent in 1994. Although the average levels of aid have dropped somewhat since 1994, these flows are orders of magnitude above the aid levels received by low and middle-income countries worldwide (World Bank 2000, Table 6.10).

By the late 1980s, some trade reforms began to be retained in the subset of countries that had managed to achieve macroeconomic stability based on reduced fiscal deficits and an appropriately valued exchange rate. (The last condition ruled out the CFA-franc group, where currencies remained highly overvalued until January 1994.) But in the majority of non-CFA countries, policy makers reversed progress toward openness by raising trade taxes to higher levels and devising new non-tariff barriers, or undermined trade-policy reforms by allowing real exchange rate appreciation and wage increases to undercut the competitiveness of fledgling export industries.

a. Getting Reform Started

In SSA, the fundamental ideas for reform have typically come from abroad. Reform programs are usually assembled and put forward by foreign experts or, more recently, by a new generation of domestic policy makers trained in Western Europe or the United States.[13] But to have a reasonable chance of being implemented, a reform initiative requires support from *some* of a country’s top policy makers, what we now call local ownership. Williamson and Haggard (1994), summarizing views of several development experts, cite the need for visionary leadership and a "sense of history." Gray and McPherson (1999) examined the role of leadership in Africa’s growth process. They found few examples of visionary leadership, or the conditions under which it could emerge and persist.[14] In most African countries, the often protracted closed-door negotiations between national representatives and IMF teams reinforce the widespread perception that funding conditions, and thus reform programs themselves, are essentially imposed from outside, with even top officials having little or no effective control over the outcome (IMF 1998a).

Empirically, crisis conditions sometimes provide the spur needed for major reforms by destroying political support for current policies. This was the case in The Gambia in 1984 (McPherson and Radelet 1995). In 1986, the failure of Nigeria's strict import and foreign-exchange licensing regimes to prevent a foreign-exchange crisis helped undermine the rationale for these policies and weaken the coalition supporting them. This cleared the way for wide-ranging reforms (Thomas, Nash *et al.* 1991). Rodrik (1994) argues that crisis conditions push distributional issues into the background and thus allow trade reforms to go forward. Yet even with per capita income falling, leaders often view reform more in terms of the minimum *quid pro quo* for obtaining financial assistance rather than as an end in itself (possible reasons are discussed below).

Moreover, actions taken in response to a crisis do not necessarily represent a move toward greater openness. On the contrary, many developing countries worldwide rolled back trade reforms in response to the oil shocks of the early 1970s and again during the debt crisis of the early 1980s. Likewise, fiscal problems are most often cited in negotiations with the IMF as the justification for maintaining current trade barriers, and worsening budgetary problems as the justification for delaying or reversing reforms (Sharer *et al.* 1998).[15] Curiously, no African country has managed to initiate reforms without waiting for a full-blown crisis to materialize under old policies.

In addition to leadership, successful reform requires adequate support from legislators and/or administrators to ensure its effective implementation. To create the desired changes in economic behavior, the leader's vision must first be translated into practical policies. However, even reform-minded African governments may lack the necessary technical expertise to implement new policies. While help is readily available from aid agencies in the OECD countries and from multilateral organizations such as the World Bank and IMF, the region's reliance on outside policy advice exacts a significant price. The key role played by foreign experts often alienates local officials and erodes their sense of ownership of the new policies. Moreover, critics of reform usually take advantage of any prominent foreign role to marshal domestic support for their opposition. The persistent appeal of *dirigiste* economic programs in SSA stems partly from their rejection of liberal, market oriented policy advice from foreign experts, especially the IMF. Moreover, the latter's traditional role in dealing with financial crises has contributed to the widespread perception in the developing world that IMF advice is the cause of economic woes rather than the solution to them.[16]

A different type of problem related to policy implementation arises because the administrative burden of a *laissez-faire* approach is much lighter than that of a *dirigiste* economic regime. Much of the resistance to market-oriented reforms may come from government officials whose jobs, salaries, prestige, and often opportunities for graft are endangered, as well as from their opposite numbers in the private sector who have learned how to operate profitably under existing policies. Opposition to reform is thus likely to extend far beyond firms and workers in protected import-competing sectors. Indeed, the IMF's standard advice favoring tariffication of non-tariff trade measures typically faces severe political difficulties. Pure tariffication eliminates rents formerly captured by those charged with administering NTMs (usually a group of powerful officials) and those accustomed to dealing with them. In the short run there may be no obvious winners from tariffication because one type of barrier has been substituted for another.[17]

b. Maintaining Broad Popular Support

Support at the top is necessary but not always sufficient for a policy to be sustained.[18] The importance of broad political support depends on the form of government, especially in the short term. An authoritarian regime may be able to force the population to accept austere policies or to shape public opinion through control over the media. Some development specialists have even raised the controversial notion that early introduction of democratic institutions may doom the prospects for needed economic reforms.[19] Indeed, authoritarian governments launched many of the successful reform efforts in both Latin America and East Asia. In most cases, these reforms have not been reversed by subsequent democratic regimes.[20] In SSA, Uganda's wide-ranging reforms were implemented by an authoritarian regime that came to power in 1986 through a coup. Nonetheless, any new government, whether authoritarian or democratic, usually enjoys an initial period when leaders benefit from greater freedom of maneuver. They also have the luxury of blaming unsatisfactory economic conditions and even initial outcomes on the previous regime (Senegal in 1984, Nigeria in 1985-6, Uganda in 1986, Zambia in 1992, and Zaire/Congo in 1997, though the last opportunity was promptly squandered).

The need to maintain broad political support is one explanation for the popularity of reciprocal liberalization in general and of Reciprocal Trade Arrangements (RTAs) in particular. The public and even many policy makers take a largely mercantilist view of trade reforms. They find it easy to grasp the benefits from increased exports (typically seen as expanded sales and employment) but difficult to see the benefits from increased imports. In a reciprocal agreement, the increased imports can be justified as the price for increased exports. But, given this prevalent misunderstanding of the fundamental nature of gains from trade, belief in the benefits of unilateral liberalization requires a major leap of faith.

The general idea of broadening support for reforms explains why both the World Bank and the IMF have shifted to comprehensive approaches to program development. The recent adoption by the World Bank of its 'comprehensive development framework' (CDF) and by the IMF of the 'poverty reduction and growth strategy' (PRGS) allows all relevant groups from the government, business community and 'civil society' to have their views taken into account. Although the idea of increased consultation is proving to be useful (and stealthily democratic in the more repressive countries) it is both time consuming and exceedingly skill intensive. It also provides an ideal means by which those opposed to reform can delay the process. They can always insist that the *status quo* cannot be changed while consultations are underway. A further problem is that due to the losses associated with HIV/AIDS, the ranks of those with the skills needed to develop the CDF's and PRGS's are thinning out. By default, therefore, this form of program development is becoming more heavily dependent on outsiders.

c. Factors Associated with Policy Reversals

Many factors have either directly held up policy reform or undermined its effects. Circumstances associated with policy reversals in SSA include (but are not limited to):

external shocks, especially commodity price collapses,
over-expansion during booms,
slower than expected debt relief,
resistance by central banks to the removal of exchange controls,
delays in unwinding state-run trading monopolies,
need for revenue holding up tariff reform,
imposition of new non-tariff restrictions such as quality standards for imports,

deterioration of physical infrastructure, especially related to transport,
exchange rate appreciation due to donor aid flows,
activism by ministries of commerce to "promote industrialization",
unwillingness of government officials to eliminate special entitlements for the military,
inability to control or reduce smuggling,
inability to reduce unit labor costs, thereby improving competitiveness,
rising protectionism in developed countries (real or potential),
difficulties in penetrating regional markets, and
incoherence of donor conditions, so that government operates at cross purposes.

As these concomitants of policy reversal suggest, reversals arise for a wide variety of reasons that may be technical, bureaucratic, institutional, and often personal (to the leaders). However, the factors listed above can be viewed in terms of broad categories corresponding to the four sequential elements in the liberalization process: (1) defects of policy design, (2) lack of political support, (3) defects of implementation, (4) environmental problems that undermine policy effectiveness.

With respect to policy design, African countries have moved along the same trajectory as other developing regions, focusing their post-independence efforts first on import-substituting industrialization and only since the mid-1980s on market-oriented reforms and export promotion. One implication is that reforming countries must contend with a legacy of highly protected, high-cost manufacturing, often including public enterprises. Part of the protection for industry came in the form of an over-taxed agricultural sector. That, too, has to be reformed, often against resistance of an urban-based population that has become accustomed to the notion of cheap food and fiber.[21] Likewise, reform is needed in the older top-down planning tradition of development finance agencies, export marketing boards, and other government-operated or government-sanctioned intermediaries that substituted for private market transactions between residents and foreign suppliers or buyers. In both cases, existing institutions provide profitable opportunities for those directly involved, and any reform effort must overcome the resistance of entrenched special interests. Reform plans are also restricted in scope because of concerns about fiscal or balance-of-payments considerations (Sharer *et al*. 1998). These concerns are sometimes no more than plausible excuses for maintaining a comfortable *status quo*, especially when governments are unwilling to improve tax compliance, but they may also reflect a policy design that is too narrow to achieve its goals. In general, sustained reform requires a broader approach that includes privatization, fiscal measures such as implementation of a value-added tax, and a shift to a market-guided exchange rate regime, not merely reductions on direct barriers to trade.

The efforts by SSA leaders to promote reforms also tend to be seriously hampered. On the one hand, they lack the expertise within their own agencies. Some countries have only a handful of trained professional economists. Furthermore, due to the spread of HIV/AIDS, the losses among all categories of workers with professional and technical skills have been mounting rapidly. On the other hand, the conditions (often contradictory) that originate from the large number of donor organizations and international agencies seeking to "help" with the reforms often overload the agendas in ways that pre-determine non-compliance. The most important agencies are the IMF and World Bank. Yet, it is only recently that these major players have begun to emphasize the need for an explicitly cooperative role in helping to shape policy (IMF 1998a). But as noted above, the form of cooperation that has emerged frequently overwhelms local capacity. Protracted negotiations over policies and conditions have seriously strained SSA's limited supply of skilled policy makers and administrators. Moreover, the movement by both institutions to more comprehensive approaches are so ambitious that they effectively pre-program the failure of the reforms.

An additional problem in policy design and implementation is the lack of timely and reliable data on policy and performance. Because economic collapse and regional conflict in SSA have contributed to the degeneration of key data-gathering institutions such as central banks and budget offices, decisions regarding reform must often be taken before adequate data become available. McPherson (1995) comments that Zambia's external debt was not fully documented until two years after the initiation of reforms.[22] The situation is even more difficult in the area of trade policy because industry-level detail is essential for policy formation. Yet while UNCTAD (1994) provides detailed information on tariffs and non-tariff barriers by sector through the early 1990s for many Asian and Latin American countries, the corresponding data for African countries are usually available only through the late 1980s or even the mid-1980s. In an assessment of trade reform under IMF and World Bank supported programs from 1990 to 1996, IMF analysts were restricted in their choice of case-study countries by availability of data needed to document the extent of reforms (Sharer *et al*. 1998). This is especially noteworthy because progress toward trade liberalization goals was among the conditions of almost all of the programs.

However, even the best plan, i.e., one that reflects state-of-the-art analysis and reliable data, can still fail at the level of implementation. Such failures may reflect absence of adequate enforcement (e.g., inability or unwillingness to control smuggling) or backsliding through substitution of new barriers for ones that have been removed (e.g., increased quality standards in place of import tariffs that have been cut). Another problem is failure to implement or enforce complementary reforms, such as the introduction of new revenue sources to replace tariffs, failure to remove exchange controls, delays in ending subsidies to high-cost import-competing manufactures, and the postponement of the phase-out of state-run trading monopolies and privatization of public utilities. Moreover, officials looking for easier ways to meet the plan's overall budgetary goals may reduce social spending instead of enforcing more politically difficult cuts in industrial subsidies or civil service wages (IMF 1998a). This may shift the burden of adjustment primarily to those already disadvantaged by their lack of economic and political power.

A final set of barriers to sustained reform are those arising in the external environment, although in some cases these may reflect flawed plans, especially plans that are too narrow in their scope or based on unrealistic expectations. Such external influences include domestic shocks (war, drought) as well as unfavorable changes in terms of trade and foreign interest rates, delays in anticipated debt relief or other ODA, and increased trade barriers or recession in potential export markets. However, the most pervasive factor beyond the direct control of government officials and international agencies is lack of market response to new incentives, typically reflecting lack of confidence among businesses, consumers, and potential foreign investors.

In this regard, reform-minded governments face a classic “prisoner's dilemma.” Due to past policy reversals, local and foreign businesses are hesitant to act immediately when the government announces and enacts specific reforms. They prefer to wait and see whether the government will maintain the reforms.[23] However, perceiving little or no response from the private sector, government officials begin to believe they must step in to achieve the objectives of policy, such as increased manufacturing investment. To the extent that government officials, eager for immediate results, backtrack or modify the reforms, the business sector's skepticism regarding government promises is reinforced. There is no effective way out of this downward spiral of adverse expectations without the government maintaining its commitment to the original reforms. This is especially difficult when key government officials (central bank exchange controllers, ministry of commerce regulators) are themselves not entirely convinced that liberalization and reform are the most effective routes to economic growth and development – and perhaps also have a personal financial interest in restoring controls on economic activity. But even the prospect of economies led by committed reformers may be viewed with some skepticism in a region where abrupt changes of government and breakdown of rule of law have been all too common.

4. Breaking the Cycle: Sustaining Trade and Exchange Reform

a. The Costs of Adjustment

Trade liberalization is an intensely political process for two related but distinct reasons. The first is that costs associated with new policies become quickly apparent while the gains usually lie farther in the future. Adjustment costs along the way can mean a period of lower average living standards, even though there are always some who gain immediately from any change in policy. This is one reason why visionary and committed leadership can be crucial to successful reform. A separate problem is that there are always *permanent* losers from any liberalization. Moreover, *trade* reform entails an especially high ratio of redistribution to total gains (Rodrik 1994). While there is no way to avoid transition costs or an uneven distribution of long-term costs and benefits, appropriate policies may reduce their extent and thus preserve the political viability of reform. Moreover, in light of experience throughout SSA, there is now a wealth of information to contrast these anticipated costs of adjustment with the equally real and (so far) devastating costs of *not* adjusting. Indeed, the marginalization of SSA in the world economy through the collapse of its growth rates is one of the more evident of the latter costs (Collier 1994; World Bank 1995; Yeats *et al.* 1997).

Commitment to an outward-oriented trade strategy requires complementary supporting policies including transportation and communications infrastructure; access to financial capital and to imported capital goods, raw materials, and intermediate inputs; a well functioning labor market, and, above all, maintenance of an appropriate real exchange rate. To the extent that potential exporters respond to the profit opportunities offered by the new policy environment, their political influence increases while that of import-competing producers wanes. This outcome can strengthen political support for liberalization, allowing the reform process to go forward (Krueger 1993). But will potential exporters respond? As noted above, the key to the cycle lies in the credibility of the new policies, and this in turn rests on the ability of the government and of the economy to withstand the dislocations of the period of adjustment. The long record of policy reversals and general disruption in African countries contributes to the continuing reluctance of private investors (and especially foreign investors) to commit their funds to new projects. Only if countries are able to maintain new policies, even in the face of adjustment difficulties, will investor skepticism be overcome, and then only gradually.[24]

Liberalizing countries necessarily experience dislocation costs during the period of adjustment to new policies. These dislocation costs are of two main forms: those associated with necessary changes in the composition of durable capital, and those associated with unemployment of labor or other resources. In the normal case where change in policy has not been fully anticipated, the economy will begin from a given stock of durable sector-specific human and physical capital that is no longer optimal. In the new situation some types of capital will be worth more than its replacement cost, others will be worth less. In general, trade liberalization reduces the value of capital in import-competing industries and raises the value of capital in current or potential export sectors. To the extent that real factor rewards are flexible, all resources can continue to be fully employed as their stocks adjust over time in line with the new relative prices. Required changes in the returns to industry-specific factors are largest soon after the new policy comes into force. In the post-liberalization equilibrium following complete adjustment in the stock of sector-specific capital, the market value of any factor must again be equal to its replacement cost.

In the absence of factor-market distortions, the *laissez-faire* adjustment process will be socially optimal. There is no efficiency gain from speeding up or slowing down the process through government policy, although there may be political reasons to do so. But factor prices are rarely flexible in the short run, and in SSA other factor market distortions are likely to be present as well. Some resources will therefore become unemployed during the transition period, bringing some dimension of the social cost of adjustment into sharp focus and thus undermining political support for the liberalization program. (The annex examines the special impact of trade reform on employment and the resistance it has faced in several countries.) This bolsters the case for some kind of government adjustment assistance program to facilitate the movement of resources into expanding sectors and to compensate those most affected by the change. Even if there is no efficiency justification for such efforts, providing special benefits may be good politics – allowing liberalization to go forward in the face of strong opposition from those adversely affected. A less benign type of adjustment assistance takes the form of subsidies, loans, or technical assistance for firms affected by trade reforms. Since these measures tend to retain resources in declining sectors, they postpone rather than promote adjustment.

Development economists formerly counseled gradual change in policy as a means of reducing costs of adjustment (e.g., Little, Scitovsky, and Scott 1970). This is another area where the conventional wisdom has changed in the light of experience. In practice, gradual policy changes allow more time for opponents of liberalization to marshal their forces. Liberalization delayed can therefore mean liberalization cancelled. In Latin America and East Asia, rapid radical reform has had a better overall record than gradualism. Based on evidence from trade reforms of developing countries in the 1980s, often with support from the IMF and World Bank, Thomas, Nash *et al.* (1991) conclude that “comprehensive, intense, and rapid” reform is usually preferable because its benefits are both larger and earlier than under a more gradual approach. To the extent that gradualism gives rise to uncertainty about full implementation, gradual policies lack credibility. With domestic and foreign investors in doubt as to whether the announced program will ever be fully implemented, the new price signals may elicit little response.

Also undercutting the case for gradualism is recent evidence from Latin America that the aggregate effect of successful trade liberalization on employment can be relatively small even in the short run. Although workers will be displaced from contracting sectors, much of the resulting job loss can be offset by employment expansion in export industries (Edwards 1995). The popular mercantilist accounting of jobs created and jobs lost gives little indication of actual adjustment costs borne by displaced workers, which depend on gross rather than net changes and on worker characteristics. It also takes no account of the real gains from expanded trade – increased efficiency from replacing low-productivity import-competing output with regionally or globally efficient export production.

On the other hand, adjustment costs sometimes affect those already living on the economic margin. External evaluators of IMF-assisted reform programs (IMF 1998a) recommend greater efforts to identify in advance those who are likely to lose from reforms, especially to the extent that some losers are people who are already poor. This would allow public officials to put social safety nets into place before they are actually needed. The evaluators cited the cases of Zambia, where maize farmers remote from markets were suddenly cut off when agricultural marketing was liberalized, and Malawi, where real wages of estate workers were halved through very high inflation while owners reaped a corresponding windfall when tobacco production was liberalized. Past efforts by SSA countries to provide safety nets have been targeted primarily at politically powerful groups such as civil servants rather than the very poor.[25] Moreover, the effectiveness of social programs has typically been impaired by inadequate financing and delays in execution, the latter resulting at least in part from the former.

The reform effort in The Gambia was greatly facilitated by the willingness of the government, within the context of its IMF program, to pay higher groundnut prices (McPherson and Radelet 1995). In its initial stage, the program was supported by a large budget allocation for producer price subsidies. Since most rural households produce groundnuts and most production units are small, the subsidy resulted in a major injection of resources into agriculture. In part the effect was to help re-capitalize the sector after years of low production and adverse price movements. Another approach was the two-track system of reform in Mauritius, which fostered exports in an enclave (using women and new entrants to the labor force) and left import-competing industry protected for a long time.

Few countries in SSA have implemented a safety net for reform independently of large inflows of resources from the donor community. Zambia responded to the drought conditions in 1992 rapidly and effectively. The basic support for the effort, however, came in the form of close to one million metric tons of food and numerous donor-funded distribution schemes. Some of these, e.g., the Program Against Malnutrition (PAM), have continued to function beyond the drought year, but only because of continued donor support. Much has been written about the Ghanaian effort popularly entitled "adjustment with a human face" (Cornia *et al.* 1987). Again, however, the source of continuity came from donors and not from the willingness of the government to commit its own resources to the effort. A final concern with government attempts to promote gradual reform is that due to past policy distortions, a significant amount of adjustment has already occurred. The most obvious examples are declining sectoral income, lower investment, and parallel foreign exchange markets. The challenge for most governments is not to reform a distorted system over which it exercises full control. In practice, the challenge is to remove the government from circumstances where its continued intervention (even if to promote reform) is undermining recovery and growth. Such a situation argues for rapid rather than gradual reform.

b. Maintaining an Appropriate Real Exchange Rate

If promoting growth via an outward-oriented strategy depends in large part on moving prices in the appropriate direction, the most important price in this regard is the exchange rate. Yet until the late 1980s, virtually all SSA currencies were seriously overvalued, with nominal rates maintained through restrictive policies that often compounded the effects of currency overvaluation. In the franc zone, currencies were highly overvalued until 1994. While there has been some overall improvement, one could argue that SSA taken as a whole displays the classic symptoms of an economic entity whose real exchange rate is mis-aligned – export growth is sluggish, overall economic growth is low, external debt is overwhelming, and there are few prospects for a rapid turnaround. An inappropriately strong real exchange rate undercuts the competitiveness of potential exports across-the-board and makes imports look cheap relative to their domestic counterparts, thus discouraging production of tradable goods.[26] Increased unemployment, deterioration of the current account on the balance of payments, and rising external debt frequently accompany appreciation of the real exchange rate. In economies with fixed nominal exchange rates, the common policy response is to resort to (further) protectionist measures. The reversal of past liberalization is typically announced as a temporary measure to protect jobs, revenue, or dwindling international reserves. On other continents successful trade reforms have typically begun with a large nominal devaluation (Thomas, Nash *et al*. 1991; Edwards 1995), and the single economic factor most likely to sabotage a liberalization attempt once in progress is (a return to) overvaluation of the real exchange rate.

SSA’s distorted foreign exchange regimes generally represent a failure to move beyond the confines of the crisis-prone Bretton Woods system of pegged exchange rates. That system was designed by the United States and Britain to meet the needs of the industrial countries. Almost all of them had moved to a system of managed floating by 1973. Even though their financial systems lacked depth and their basic financial institutions were weak, the majority of developing countries in SSA (and elsewhere) continued to peg their exchange rates to a single major currency or to a basket of currencies, with the choice based on trading relationships.[27] Like the industrial countries prior to 1973, non-CFA countries made occasional if sometimes inadequate parity revisions to accommodate changing circumstances. But the exchange rates of franc zone countries remained fixed from 1948 until 1994 despite steadily deteriorating economic conditions beginning in the mid-1970s.

Most countries in both groups resorted repeatedly to increased protection as a response to problems associated with exchange rate overvaluation, but other policies varied according to the exchange-rate regime. In the franc zone, national currencies were kept freely convertible into French francs at a fixed rate, implying that members had to forego an independent monetary policy. Instead, monetary policy decisions were governed by two regional central banks (Duesenberry and Gray 1996). Policy makers in some CFA countries also (partially) adopted the traditional “gold standard” rules, tightening fiscal policy in an effort to restore balance-of-payments equilibrium without a parity change.[28] In the years prior to the long-overdue devaluation of the CFA franc, restrictive macroeconomics policies and increased trade barriers combined to produce declining and even negative growth rates in the CFA countries. In the non-CFA countries, most currencies were officially inconvertible until the late 1980s, with official rates often only a fraction of the parallel exchange rates. Rather than bringing their official rates into line with market conditions, countries with current-account deficits continued to impose further restrictions on access to foreign exchange.[29]

The failure of most SSA countries to maintain appropriate real exchange rates has been a crucial element in the region's slow progress to openness, with complex exchange controls adding to the cost of overvaluation for the non-CFA countries. By the mid-1990s, however, a number of non-CFA countries had scrapped most exchange controls and brought official rates and corresponding real rates more closely into line with market conditions. Some partial correction of the overvaluation of currencies in the franc zone had likewise occurred through the large January 1994 devaluation relative to the French franc.[30] These are significant steps in the right direction for SSA countries, although the problem of maintaining appropriate real rates under changing conditions remains a difficult challenge for all smaller countries, not just those in SSA. Indeed, empirical work covering the 1970s and 1980s showed that a major problem facing countries in SSA that had adjusted their exchange rates was to prevent the real devaluation from being undermined by rapid inflation (Rouis, Razzak, and Mollinedo 1994).

In Latin America and Asia, real appreciation often occurs when the exchange rate is used as a nominal anchor to control domestic inflation. The potential incompatibility of the nominal anchor strategy with maintaining a desired real exchange rate gives rise to the judgment that macroeconomic stabilization needs to be well advanced before trade liberalization has a good chance at success. The repeated reversals of trade reform in Argentina and Brazil were linked to failed stabilization programs. Another threat to an appropriate real exchange rate comes from the capital account. The central objectives of African reforms almost always include ensuring the continuation of aid flows, discouraging capital flight, and attracting foreign direct investment. Success in any combination of these objectives results in upward pressure on the real exchange rate, and thus an additional challenge for a country pursuing export-led growth. This is one reason for the conventional advice that trade reforms should precede capital-account liberalization. However, rather than limiting all capital inflows, developing countries often try to discourage only inflows of short-term liquid capital, thus offering exporters some protection from volatility of the real exchange rate without losing the potential benefits from longer term investments. The record in this area has been poor at best. Attempts by governments to control capital movements have typically backfired through large-scale capital flight and currency substitution.

Until the late 1970s, the credible fixed rates of franc zone countries, along with the implied constraints on monetary expansion, helped keep inflation rates low without obvious negative effects on growth relative to other comparable SSA countries (Devarajan and Rodrik 1991). Overall economic performance for these countries was better than that of their non-CFA neighbors. But in the years leading up to 1994, the benefits of a permanent fixed rate were overshadowed by the costs of overvaluation. The increasingly apparent real overvaluation of national currencies discouraged exporting, generated pressure for new import barriers, and distorted financial flows as a devaluation of the CFA franc came to be widely anticipated. The devaluation of the CFA franc in 1994 made a change in regime less of an immediate issue than it previously had been. Yet, many development advisors (including the present authors) believe that a managed float rather than a fixed rate offers the best compromise between the goals of managing domestic macroeconomic performance and maintaining an appropriate real exchange rate (Duesenberry *et al.* 1996).

c. Macroeconomic Discipline

Only in the past decade have countries in SSA begun to move towards the degree of macroeconomic stability essential for good economic performance. Structural adjustment policies including trade reform were often undermined by the need to reduce budget deficits and to curb inflation in many non-CFA countries. As noted above, measures to reduce inflation may produce an overly strong real exchange rate that taxes potential exporters. Trade reform also poses a fiscal problem since, as noted earlier, SSA countries typically rely on trade taxes, especially taxes on traditional commodity exports, for a substantial share of revenue. Import tariffs have also been a significant source of government revenue for most SSA countries although evidence from recent years shows that many countries have broadened their revenue bases in ways that reduce their relative dependence on trade taxes as a source of central government revenue.

In principle, a move to a simple trade regime with low uniform trade taxes and strong enforcement could raise rather than lower trade's contribution to government revenue, depending on the price elasticity of trade flows and the prior extent of smuggling to avoid high tariffs and burdensome non-tariff barriers.[31] Another potential offset is tariffication of quantitative restrictions, a policy change usually considered to be a move toward trade liberalization because it reduces the role of administrative discretion and boosts tariff revenues. However, it has the political disadvantage of creating losers (former license holders and administrators) without the rapid emergence of obvious winners. In practice, these offsets are rarely sufficient to prevent total tariff collections from falling when trade is liberalized. For this reason World Bank analysts argue that the fiscal deficit should be reduced before trade is liberalized (Thomas, Nash *et al*. 1991). Although the corresponding cuts in expenditure to reduce the budget deficit have often been seen as a “cost” of trade reform, this misses the point. Typically the problem is that the government expenditure is too large relative to the economy’s resource base. The re-imposition of macroeconomic discipline requires that both the size of government expenditure and the allocation of its expenditure and revenue need to be changed (often quite dramatically).[32]

Although tariffication of non-tariff barriers, increases in the lowest tariffs, elimination of tariff exemptions, and better enforcement of existing tariffs are all recommended as ways to begin the process of trade liberalization while enhancing government revenue (Sharer *et al*. 1998), further progress on liberalization requires cuts in tariff rates. These may be compensated by the development of other revenue sources (e.g., value-added or income taxes) and cuts in government expenditure. In Latin America, some temporary but significant budgetary relief on both the revenue and the expenditure side has come from privatization of government-owned companies. Privatization typically produces double fiscal benefits, first from the asset sale and then from avoidance of the budget-breaking operating subsidies to cover the losses generated by government enterprises. Experience in Africa confirms these dual benefits. In The Gambia significant budget savings as well as containment of national debt were achieved through the combination of selling, commercializing, and shutting loss-making state-owned enterprises (McPherson and Radelet 1995). In Zambia, a more elaborate system of cross-subsidies among SOEs had been widely used until the government scrapped the parastatal holding company. The main budget saving came in the elimination of agricultural subsidies which had emerged through a series of distortions on both international and internal competition on the trade in staple grains.[33] Other SSA countries that have undertaken significant privatizations – Malawi, Senegal, Tanzania, Uganda, Burkina Faso, and Ghana – have also seen corresponding improvements in their fiscal position.

d. Increased Inequality

Regardless of the political regime, the sustainability of any policy package eventually rests on its ability to raise, or at least not reduce, the resources available to meet the needs of the population. Experience has shown that it is easier to promote reforms that deliver a rising average living standard than a package that requires sacrifice. The typical measure of comparative economic success across countries is growth in per capita income.[34] But the viability of reforms depends not only on aggregate or average gains but also on their distribution. There is some evidence that for the SSA region as a whole, the income share of the lowest quintile of the population improved significantly between the 1960s and the 1970s. It has not, however, shown much subsequent improvement (World Bank 1997b; 2000, Table 2.8).[35] This is an especially grim outcome given that per capita incomes have fallen extensively across Africa over the last three decades. Although income inequality remains an important policy concern in SSA, a more pressing problem for the region has been the general depression of incomes and intensification of poverty (United Nations 1997, 109).

Furthermore, there is extensive evidence that many of the benefits from market-oriented policies have been shared unevenly. In Uganda, government data indicate that urban workers reaped almost all the benefits of recent reforms, widening income inequality in an economy where, as is typical in Africa, urban incomes were already much higher than those in rural areas (IMF 1998:85; Collier and Reinikka 1999). In Zambia, there has been widespread analysis and discussion of the relative impact of reforms. During the initial stages there was an improvement in distribution due to the elimination of food subsidies. These had primarily benefited urban consumers and were largely financed by lower prices paid to farmers. Yet, while the income share of farmers improved (despite the effects of drought), there were serious regional distribution effects as the move to market prices marginalized some farmers (World Bank 1995). More broadly, recent econometric work covering the period 1970 to 1998 for 39 countries in SSA shows that non-agricultural income grew at the expense of agricultural income.[36] Since the rural population was significantly poorer than those in rural areas, this strengthens the point that the distribution of income has worsened over time.

e. Saving and Investment

A previous generation of development economists saw Simon Kuznets' inverted-U of temporarily increased income inequality as the necessary price of rapid growth. Concentration of income and wealth were assumed to promote essential capital formation by raising the aggregate saving rate. Over recent years this rationalization has been less persuasive (Bruno, Ravaillon and Squire 1995).[37] The high saving rates of East Asia were achieved without increases in inequality. Moreover, in a world of internationally mobile capital, there need be no direct correspondence between domestic saving and domestic capital formation. However, private investors have not yet shown the same kind of interest in Africa that they have demonstrated in other emerging markets with longer track records of sustained reform. There are now many initiatives supported by private organization (such as the Corporate Council for Africa), bilateral agencies (such as the United States Government)[38] and the multi-lateral agencies (particularly the World Bank) to stimulate private investment in Africa. Thus far there has been little success. Flows of foreign direct investment (FDI) remain low and highly concentrated (AfDB 1997; Madavo and Sarbib 1997).

There are many explanations. At one extreme, some commentators see a bias against Africa that comes from uncritically viewing the continent as a whole.[39] This view, however, is not consistent with the *selected* approaches followed by foreign investors who will make the investment when their various criteria for markets, security, and viability are met. Evidence assembled in the first two *African Competitiveness Reports* (WEF/HIID 1998; 2000) provides a detailed assessment of the factors that stimulate and detract from investment in Africa. None of these factors is surprising. They appear on any list of investment criteria relevant for any continent. One factor of concern is security. The history of disruption across Africa (civil wars, refugees, and the unprecedented armed intervention in Congo by several African nations) has had an impact. One of the most important, but least noted as researchers focus on FDI, is that the principal sources of foreign investment, namely local and expatriate Africans who hold billions of dollars outside the continent, are not actively returning to invest in the continent. As the Asian and Latin American experiences show, there will be no surge in FDI until Africans themselves begin bringing their resources home. That will begin when the types of measures described above are in place leading to macroeconomic stability and removing the risks of policy reversal.

Internationally mobile capital provides a barometer of investor sentiment regarding the credibility of reforms. Countries that achieve stable, market-oriented institutions have been able to supplement domestic saving with private capital inflows from abroad. Although most governments rarely appreciate the daily policy report card provided by active financial markets, the concern about losing foreign investment may very well limit officials' impulse to adopt policies with short-term payoffs but longer term costs (McCulloch and Petri 1998). Conversely, while international investors are more likely to by-pass countries without strong market institutions, wealthy SSA savers are highly resourceful in finding means to move their own financial assets abroad (Collier and Gunning 1999). They have been facilitated in this by the convenience associated with the globalization of financial services.[40] This has facilitated capital flight and currency substitution resulting in the internationalization of African surpluses. African countries will begin to gain from these (and other) resources when conditions are such that investors consider the income opportunities and associated risks of longer-term investment to be acceptable.

f. Sequencing of Reforms

In the developing world (as well as the former centrally-planned economies), an import-substitution trade regime has typically been one element in a broad complex of *dirigiste* policies affecting all domestic economic activity. These policies include extensive public ownership, selective subsidies, and government restrictions affecting operation of domestic capital and labor markets as well as the foreign exchange market.[41] Furthermore, many developing countries experienced double- or triple-digit inflation rates during the 1960s and 1970s due to their over-reliance on money creation to finance government deficit spending. Experience suggests that attention to sequencing of economic reforms can help minimize the period of economic distress following liberalization. A large literature has dealt with the issue of sequencing, but without achieving consensus on an optimal or appropriate sequence [42] that is independent of the particular circumstances of a given country.[43] Moreover, the sequencing literature typically treats trade liberalization as a single element in a broader reform program. Questions less often addressed concern the sequencing of the individual policy changes required to complete a country's successful transformation from import substitution to outward-oriented growth, changes sometimes carried out over a period of years or even decades.

Notwithstanding theorists' concentration on the costliness of import restrictions, countries in East Asia and Latin America that have successfully liberalized most often began the process of integrating into global markets through increased incentives for exporters (Perkins 1994). The same is true of Mauritius, which developed export-oriented manufacturing in an export-processing zone long before removing the trade barriers that protected its import-substituting manufacturing sector. In practice, the initial impetus for import liberalization has frequently come from the needs of current or potential *exporters* who look to world markets for capital goods, raw materials, or intermediate inputs. In East Asia and Latin America, measures to facilitate export growth were often enacted in advance of comprehensive trade reforms. These included rebates of import duties on capital equipment and/or intermediate inputs used to produce exports, the establishment of export-processing zones, favorable access to licensed foreign exchange and restricted imports, and other incentives intended to raise the profitability of all or selected export-oriented activities. Subsequent reforms usually include broader measures such as the elimination of import licensing, tariffication of quantitative import restrictions, rationalization of the tariff structure, and elimination of multiple exchange rates used to discourage "nonessential" imports. In SSA, however, issues of credibility and rent-seeking often impede the ability of governments to jump-start the liberalization process through fiscal incentives. Credibility problems also inhibit their ability to promote liberalization according to a time-phased format. Due to the frequency of policy reversals, potential beneficiaries of reforms can never be sure whether the incentives will be continued or withdrawn when the government's circumstances change.

As noted previously, attempts to stimulate exports via tariff exemptions on imports were undermined by fiscal problems, administrative delays, and corruption. This argues for an across-the-board approach that requires a minimum of administrative support, administrative discretion, and funding. The most obvious such measure is a large real devaluation, preferably carried out along with reductions in non-tariff barriers to imports. The advantage of linking these two measures is that real devaluation makes domestic producers more competitive, thus cushioning the effects of removing import barriers.

In fact, the first step in comprehensive reforms has usually been a real devaluation, sometimes along with unification of any multiple exchange rates (Thomas, Nash *et al*. 1991). In some Latin American countries, an early real devaluation tended to make quantitative import restrictions redundant, thereby facilitating their speedy removal. Although Edwards (1995) notes the increased speed and intensity of Latin American trade reform programs in the 1990s, broad tariff reductions have typically been implemented in stages over several years according to a schedule announced at the start.

The goal was less to spur exports than to move domestic relative prices closer to international prices and to eliminate large discrepancies in domestic effective protection rates.

The Lerner Symmetry Theorem implies that removing barriers to imports is equivalent to removing barriers to exports. Nonetheless, there may be dynamic advantages in pursuing export promotion prior to general liberalization on the import side. The most controversial aspect of trade liberalization is not the configuration in the new equilibrium versus the old one, but the path by which the economy moves from one to the other. In the new outward-oriented equilibrium both imports and exports will be much larger. However, the extent of overall economic losses and income redistribution, and hence the difficulty of maintaining adequate political support for needed reforms, all depend critically on whether imports grow sooner or later than exports, i.e., whether the current account improves or deteriorates during the period of adjustment. Marked deterioration of the current account signals a likely return to protection (Michaely, Papageorgiou, and Choksi 1991), thus undermining the credibility of the reforms. Proceeding first with export promotion (including real exchange rate devaluation) also creates a set of early supporters for further reforms, including both local firms with export potential and foreign direct investors establishing export-oriented subsidiaries.

All of this experience suggests that the approach to trade reform has to be adapted to a particular country's circumstances on a case-by-case basis. All policies relevant to the liberalization of trade cannot be changed at once without risking chaos. Nonetheless, there is no optimal sequence of reforms that can be derived in advance and implemented.[44] Any phasing of reforms will need to be administratively feasible. The outcome will be path-dependent. Policy makers will need to take the set of measures that will be effective and credible, and be prepared to adapt their strategy of liberalization as locals and foreigners react to the newly created opportunities for trade and exchange.

g. Reciprocal Trade Agreements (RTAs)

Along with the rest of the world, SSA has experienced a resurgence of regional trade initiatives (Radelet 1997; GCA 1997; Gibb 1998). These have produced new or revamped customs unions with negotiated common external tariffs. Examples include the East African Economic Community and the Economic Community of West African States (ECOWAS). Under the Abuja

Declaration of 1991, African nations agreed in principle to work towards a common market throughout Africa by the year 2020. Other new or restructured arrangements have been free trade areas, including the Common Market of East and Southern African States (COMESA). With South Africa's renunciation of *apartheid*, the revised protocols for the Southern Africa Development Community (SADC) include the intention to create to a free trade area. RTA in Africa are outlined in Table 6.

Unlike the inward-looking regional agreements of the 1960s, these agreements have been formed or revived at the same time that at least some of their members are simultaneously liberalizing trade on a most favored nation (MFN) basis. Even the language of the new agreements has typically been outward-oriented, emphasizing enhancement of international competitiveness, export growth, and receptivity to foreign direct investment. Some observers are unenthusiastic about the regional initiatives, fearing losses from trade diversion, a return to nontransparent protection, rising external trade barriers, and reduced interest in future rounds of multilateral trade negotiations (e.g., Bhagwati and Panagariya 1996). An additional concern in SSA is that negotiating and maintaining regional trade agreements may further tax the limited administrative resources of member countries (Radelet 1997). However, other researchers (e.g. Fernandez 1997) argue that regional agreements may help to maintain the region's movement toward openness by enhancing credibility of reforms, a substantial benefit for the many SSA countries where reform has been repeatedly halted or reversed.

Table 6. Regional Trade Agreements

Eastern and Southern Africa

PTA (Preferential Trade Area for Eastern and Southern African States, founded in 1981, operational from 1984)

Members:	Angola, Botswana, Burundi, Comoros, Djibouti, Eritrea, Ethiopia, Kenya, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, Rwanda, Seychelles, Somalia, Sudan, Swaziland, Tanzania, Uganda, Zambia, Zimbabwe.
Type of arrangement:	Trade and customs union.
Objectives:	Gradual reduction of the tariffs with total elimination by 2000 (initially – 1992.) To remove NTBs, to promote economic development cooperation and policy coordination, to improve the infrastructure and transportation links among the member states, to develop industry.
Characteristics:	The largest regional union in terms of population. Difference exists in the economic stance between Southern and East African states within the union. The deadline for tariff elimination was delayed. Some reduction in the NTBs in several countries was achieved. Intra-regional trade is low. More successful in the economic cooperation. Established a Clearing House (PTACH) and PTA Trade and Development Bank. Formed common market union (COMESA) as its successor and a step toward establishing a monetary union. Currently COMESA and PTA function simultaneously.

COMESA (Common Market for Eastern and Southern Africa, formed in 1994 to replace the PTA)

Members:	Angola, Burundi, Comoros, Congo D.R., Djibouti, Egypt, Eritrea, Ethiopia, Kenya, Madagascar, Malawi, Mauritius, Namibia, Rwanda, Seychelles, Sudan, Swaziland, Tanzania, Uganda, Zambia and Zimbabwe.
Type of arrangement:	Trade and customs union.
Objectives:	To establish a Free Trade Area (FTA) by the year 2000. (First step is to reduce the tariffs in the member states by 80 percent and eliminate NTBs.) To establish a common external tariff by the year 2004 under the following scheme: 0 percent on capital goods, 5 percent on raw materials, 15 percent on intermediate goods and 30 percent on final goods. To promotes free

factor movement, trade liberalization and establish free currency exchange zone.

Characteristics: The newest and most ambitious regional integration organization in Sub-Saharan Africa. A major market place for both external and internal trading. Comprises population of 385 mill. Member countries have preferential access to markets within the European Union under the Lome Convention. Currently, only Comoros, Eritrea, Sudan, Uganda and Zimbabwe have reached the level of 80 percent reduction in the tariff rate; Kenya, Malawi and Mauritius have reached 70 percent reduction. The still unequal tariff rates lead to unequally distributed revenue losses and gains from the union trade among the individual countries in COMESA. Some PTA and SADC member states are reluctant to join the COMESA agreement.

SACU (South African Customs Union, established in 1910, in present form since 1969)

Members: Botswana, Lesotho, Namibia, South Africa and Swaziland.
Type of arrangement: Trade and customs union.
Objectives: To remove trade barriers, promote free factor movement, establish common external tariff and customs organization.
Characteristics: The oldest customs union in SSA. Dominated by South Africa. The union has the highest GDP per capita in SSA. SACU has achieved its main objectives: all trade barriers have been removed, there is free movement of factors and common external tariff and customs organization. Established Revenue Fund to distribute the gains from the union among the member states.

SADC (Southern African Development Community, formed in 1992, succeeded the SADCC Southern African Development Coordination Conference, formed in 1979)

Members: Angola, Botswana, Lesotho, Malawi, Mauritius, Mozambique, Namibia (joined in 1990), South Africa (from 1994), Swaziland, Tanzania, Zambia, Zimbabwe.
Type of arrangement: Trade agreement.
Objectives: To reduce the dependence on South Africa through economic cooperation (SADCC objective.) To facilitate economic policy coordination. To eliminate tariffs within the union by the year 2005.
Characteristics: Promotes economic integration. One of the few SSA trade groups with increasing intra-group trade. Most countries are also members of PTA (COMESA) and/or SACU. The SADC countries signed a protocol in August 1996 to signal their commitment to trade and investment liberalization. SADC has taken steps to promote private sector development in the region. Established various regional organizations to facilitate trade and cooperation in tourism, electrical power production and infrastructure development.

CBI (Cross Border Initiative, established in 1992)

Members: Burundi, Comoros, Ethiopia, Kenya, Madagascar, Malawi, Mauritius, Namibia, Reunion, Rwanda, Seychelles, South Africa (observer), Swaziland, Tanzania, Uganda, Zambia, and Zimbabwe.
Type of arrangement: Auxiliary regional arrangement.
Objectives: To reduce trade barriers and promote factors mobility among the member states. To promote economic integration by facilitating private investment, trade and payments between the countries of East and Southern Africa and the Indian Ocean, which are members of the PTA, SADC and IOC.
Characteristics: Focuses on the involvement of the private sector. Promotes cooperation of domestic, regional, and international organizations in the decision making. Stresses on the reconciliation of the national and regional policy goals. Largely donor financed and donor driven (it was launched by the African Development Bank, the European Commission, the IMF and the World Bank.) Difficulties exist in promoting CBI's medium term goals along the immediate policy concerns and short term reform agenda of countries' policy makers.

EA(E)C (East Africa (Economic) Cooperation, former EAESO - East African Economic Services Organization, founded in 1966, operational until 1977, recently revived by its original members)

Members: Kenya, Tanzania, Uganda.
Type of arrangement: Trade and customs union

Objectives: To promote trade and economic development among member states.
Characteristics: The lowest GDP per capita among the regional organizations in SSA.
Inequality of trade and distribution of union gains among member countries.
Current negotiations to revive the union with more members and renewed structure.

IOC (Indian Ocean Commission, established in 1982)

Members: Comoros, Madagascar, Mauritius, Reunion and Seychelles.
Type of arrangement: Trade agreement.
Objectives: To promote regional cooperation in trade and industrial development.
Characteristics: The commission comprises small economies with similar structure, which hinders their ability to take advantage of the benefits from freer trade and economic cooperation.

West Africa

ECOWAS (Economic Community of West African States, founded in 1975)

Members: Benin, Burkina Faso, Cape Verde (joined in 1977), Côte d'Ivoire, The Gambia, Ghana, Guinea, Guinea-Bissau, Liberia, Mali, Mauritania, Niger, Nigeria, Senegal, Sierra Leone and Togo.
Type of arrangement: Economic and trade agreement.
Objectives: To establish a Free Trade Area. To promote industrialization and economic development among member states.
Characteristics: A union of very diverse economies. Dominated by Nigeria. The only regional economic organization in SSA with collective security and defense arrangements. Adopted ECOWAS Programme on Monetary Cooperation. Established West African Clearing House (WACH) - not joined by Cape Verde. Failed to achieve most of its objectives. Low shares of intra-regional trade. Many barriers to trade remain. Political instability in many of the member states.
Most of the member countries participate in other regional trade and economic unions with sometimes conflicting membership duties.

CEAO (Communauté Economique de l'Afrique de l'Ouest, subset of ECOWAS, founded in 1973, following UDAO and UDEAO – Union Douaniéré et Economique de l'Afrique de

l'Ouest, founded in 1959 and 1966 respectively

Members: Benin, Burkina Faso, Côte d'Ivoire, Guinea (observer), Mali, Mauritania, Niger, Senegal and Togo

(observer).
Type of arrangement: Trade and customs union.
Objectives: To establish a common external tariff, free trade area and customs union.
To promote economic cooperation and development, free movement of factors.
Characteristics: Complements the monetary union UMOA (now UEMOA) in the CFA zone.
Dominated by Côte d'Ivoire and Senegal. Slow growth of intra-regional trade. Established Community Development Fund and Solidarity Fund to assist financially the less developed areas of the region. Has not achieved the objective of common external tariff.

MRU (Mano River Union, formed in 1973)

Members: Guinea, Liberia and Sierra Leone.
Type of arrangement: Trade and customs union.
Objectives: To promote economic cooperation and trade among the members.
Characteristics: The smallest regional union in SSA. Did not succeed in increasing intra-regional trade.
No tariffs among the member countries, but many NTBs and tariff equivalent barriers still exist.
Common external tariff established in 1977. Political instability and uncertainty restricted the regional trade and economic development.

Central Africa

UDEAC (Union Douaniére et Economique de l'Afrique Centrale, founded in 1964, revised in 1975, replaced in 1995 by CEMAC– Economic and Monetary Community of Central Africa)

<u>Members:</u> Cameroon, Central African Republic, Chad, Congo, Equatorial Guinea (from 1985) and Gabon.
<u>Type of arrangement:</u> Trade and customs union.
<u>Objectives:</u> To facilitate freer trade and movements of factors. To establish common external tariff and maintain a monetary union (under BEAC).
<u>Characteristics:</u> The union has one of the highest per capita GNPs in SSA. Dominated by Cameroon. Failed to increase intra-regional trade and remove existing trade barriers. No labor mobility. Failed to develop into a custom union.

CEPGL (Economic Community of the Great Lakes Countries, founded in 1976)

<u>Members:</u> Burundi, Rwanda and Zaire.
<u>Type of arrangement:</u> Trade agreement.
<u>Objectives:</u> To remove trade barriers, facilitate free movements of labor and cooperation in joint projects.
<u>Characteristics:</u> Political instability prevents economic development and cooperation. Very low intra-union trade. None of the union's objectives has been achieved.

ECCA or ECCAS (Economic Community of Central African States, founded in 1983) (also CEEAC – Communauté Economique des États de l'Afrique Centrale)

<u>Members:</u> Angola (observer), Burundi, Cameroon, Central African Republic, Chad, Congo, Equatorial Guinea (from 1985), Gabon, Rwanda, Sao Tome and Principe, and Zaire.
<u>Type of arrangement:</u> Economic grouping.
<u>Objectives:</u> To promote regional economic cooperation and establish a Central African Common Market.

<u>Franc Zone</u>

<u>West African and Central African branches:</u>

UEMOA (Union Economique et Monétaire Ouest Africaine, formed in 1994, replacing UMOA Union Monétaire Ouest Africaine.) Under BCEAO (Banque Centrale des États de l'Afrique de l'Ouest)

<u>Members:</u> Benin, Burkina Faso, Côte d'Ivoire, Mali (since 1984), Niger, Senegal and Togo.

CEMAC (Communauté Economiquet et Monétaire de l'Afrique Central, formed in 1994, replacing UDEAC under BEAC Banque des États de l'Afrique Centrale)

<u>Members:</u> Cameroon, Central African Republic, Chad, Comoros, Congo, Equatorial Guinea (from 1985), Gabon and Guinea Bissau (from 1997.)

(The Franc Zone also includes French Guiana, Guadeloupe, Martinique, Reunion, Mayotte, Saint Pierre and Miquelon, and French Polynesia, New Caledonia, Wallis and Futuna)

<u>Type of arrangement:</u> Monetary union.
<u>Objectives:</u> To complete the monetary and trade integration of the member states.
<u>Characteristics:</u> The CFA Zone common currency - CFA Franc - maintains a fixed parity with the French Franc. The member states share a Central Bank (BCEAO and BEAC for the two branches) with African governance but under French supervision. The convertibility of the CFA Franc is

guaranteed by the French treasury. The French government participates in determining the monetary and exchange rate policy of the CFA states. The economic crisis from the late 80s and early 90s led to devaluation of the CFA Franc against the French Franc in January 1994.

Other Regional Economic Integration and Cooperation Groupings

CE (Conseil d'Entente, founded in 1959)
Members: Benin, Burkina Faso, Côte d'Ivoire, Niger and Togo.

LCBC (Lake Chad Basin Commission, founded in 1964)
Members: Cameroon, Chad, Niger and Nigeria.

NBA (Niger Basic Authority, founded in 1980, dates back to 1963)
Members: Benin, Burkina Faso, Cameroon, Chad, Côte d'Ivoire, Guinea, Mali, Niger and Nigeria.

CILSS (Permanent Inter-State Committee on Drought Control in the Sahel, founded in 1973)
Members: Burkina Faso, Chad, Mali, Niger and Senegal.

OBK (Organization for the Planning and Development of the Kagera River, founded in 1977)
Members: Burundi, Rwanda, Uganda (joined in 1981) and Tanzania.

OMVG (Organization for the Development of the River Gambia, founded in 1978)
Members: The Gambia, Guinea, Guinea-Bissau and Senegal.

OMVS (Organization for the Development of the Senegal River, founded in 1972)
Members: Mali and Senegal.

ALGR (Authority for the Integrated Development of the Liptako-Gourma Region, founded in 1970)
Members: Burkina Faso, Mali and Niger.

IGADD (Inter-Governmental Authority on Drought and Development, founded in 1986)
Members: Djibouti, Eritrea, Ethiopia, Kenya, Somalia, Sudan and Uganda.

AfDB (African Development Bank, also BAD – Banque Africaine de Developpement)
Members: All African countries (except South Africa, Reunion and Mayotte) and 25 non-regional members.

BDEAC (Banque de Developpement de Etats de l'Afrique Centrale)
Members: Cameroon, Central African Republic, Chad, Congo, Equatorial Guinea, France, Gabon, Germany and Kuwait.

EADB (East African Development Bank)
Members: Kenya, Tanzania and Uganda.

WADB (West African Development Bank, also BOAD – Banque Ouest Africaine de Developpement)
Members: Benin, Burkina Faso, Côte d'Ivoire, Mali, Niger, Senegal and Togo.

OAU - Organization of African Unity.
Members: All 50 Sub-Saharan African countries and Algeria, Libya and Sahrawi Arab Democratic Republic.

Sources: *Oyejide et al. 1997, Sahn et al. 1997, US Trade Representative 1997, COMESA nd., IMF various years*

Given the range of potential benefits from and obstacles to successful liberalization discussed in the previous sections, together with the widely held intellectual support for market opening in general, what can be said about the choice between unilateral and reciprocal liberalization? Relative advantages may reflect differences in anticipated size of eventual benefits, costs of adjustment, and political feasibility of reform. But in light of recent patterns of policy change, it may be misleading to cast unilateral and reciprocal liberalization as mutually exclusive alternatives. Rather, they offer complementary strategies for implementing market-oriented structural reform (McCulloch and Petri 1997), an idea that has been termed open regionalism in the Asia-Pacific context.

With respect to the size of benefits, a RTA is likely to cause trade diversion, i.e., substitution of imports from higher-cost partners for goods previously obtained from lower-cost non-partners.[45] The cost associated with trade diversion thus reduces potential gains from liberalization with preferential elements; in a free-trade agreement, these costs may be increased by restrictive rules of origin. By promoting action on the part of countries that might otherwise choose to free-ride, reciprocal liberalization may result in *more* liberalization and thus greater gains at both a global and national level. This, of course, is the logic underlying the multilateral trade negotiations that have helped to reduce many types of barriers to trade in the advanced countries (World Bank 1995a). Essentially the same benefits might be obtained from what could be called strategic unilateralism, a scenario in which one country's unilateral liberalization induces its trading partners to follow its example (Coates and Ludema 1996). This kind of leader-follower behavior may be plausible in a repeated-game context. However, the reverse is also possible: countries may delay trade reform in hope of getting "credit" for their action in a subsequent regional or multilateral negotiation.[46]

While the benefits of trade reform typically take the form of superior efficiency, any liberalization entails adjustment costs that must be measured against the eventual gains from superior efficiency. In the typical case, distorted domestic factor markets exacerbate these costs. The simultaneous opening of several national markets reduces the required extent of dislocation and adjustment for any one of them. An important aspect of this advantage is the reduced need for a lower real exchange rate, an advantage for countries still dealing with high rates of domestic inflation. Lowering the cost of adjustment constitutes an economic benefit and also reduces the political difficulties of implementing and maintaining the liberalized trade regime. Moreover, in East Asia and Latin America, much of the new regional trade has been *intra*-industry trade, presumed to be associated with lower adjustment costs than *inter*-industry trade.

An important advantage of reciprocity is that it reduces the political obstacles to trade reform. Indeed, greater political feasibility appears to be the major reason why countries engage in various types of reciprocal rather than unilateral liberalization. In particular, discriminatory liberalization, although almost always sub-optimal in at least its initial outcome, offers clear benefits to readily identified domestic sectors in the form of trade diversion, thus ensuring the support of export interests that are known to be regionally but perhaps not globally competitive. Unilateral liberalization offers benefits only to the much smaller number of export firms and sectors that appear *ex ante* to be globally competitive. (*Ex poste*, the general equilibrium consequences of a successful liberalization always reveal export potential not apparent in advance.) A reciprocal process, whether regional or multilateral, also enhances public acceptance of liberalization. Reciprocity undercuts the public perception that the country's policy makers are giving something away (market access) with no *quid pro quo*. On the other hand, reciprocal liberalization may mean lengthy delay of needed reforms. This is precisely what South Africa found in its attempt to negotiate a special trade arrangement with the European Union. Announced as a "done deal" in March of 1999, the agreement was held up over brand names for agricultural products. The decision to liberalize unilaterally seems to occur in conjunction with comprehensive across-the-board reforms. In such instances, liberalization by trading partners would be welcome (for the reasons noted above) but the cost of delay is too high. Crisis conditions call for prompt action, and so may be associated with unilateral trade reforms, as in the case of Uganda in the late 1980s, Zambia in the early 1990s, and some of the CFA countries following the devaluation of the CFA franc in January 1994. In practice, however, international institutions and bilateral aid agencies have at most provided external support for countries in crisis willing to commit to even modest steps toward reform.

Participation in international agreements to open markets can raise the viability of reforms by raising the domestic and international political cost of reversing them. Like GATT/WTO membership, RTAs therefore lend greater credibility to reforms, especially in countries whose recent history has included numerous liberalization reversals. In Latin America, Mexico's NAFTA membership was billed explicitly as a way to lock in market-oriented reforms and thus increase their credibility (Tornell and Esquivel 1997). Likewise, establishment of Mercosur helped to bolster the credibility of the latest trade liberalizations in countries such as Argentina and Brazil with prior records of many policy reversals. In SSA, there have been a number of changes. The East African Community, consisting of Kenya, Tanzania, and Uganda, is formally due to launch the community on 30th November 2000. ECOWAS is working directly with the European Union to set in place the conditions for moving towards a common currency. And, COMESA will by 31st October 2000 move to a free trade area with a common external tariff as part of the process of establishing a monetary union by 2004, a customs union by 2002, and a common market before 2025. These are bold plans that, if they can be fully implemented, will help African countries solidify the process of trade and exchange rate reform.

h. The external policy environment

The case for import-substituting industrialization, as developed by Prebisch, Singer, and others, rests in part on export pessimism: the assumption that global markets offer less-developed countries little opportunity for gains through increased exports. Development along lines of international comparative advantage was interpreted narrowly to mean the additional export of raw materials and commodities, since these made up about four-fifths of the value of existing exports from less-developed countries as a group. The basic presumption was that the international prices obtained for these exports would decline over time, exacerbating the gap between rich and poor nations (Edwards 1995). Moreover, their narrow view of outward-oriented growth seemed to offer no role for development of a modern manufacturing sector (Krueger 1997) or, more recently, new service-oriented sectors.

Notwithstanding the past successes of export-led industrialization in Asia and Latin America, the question of global market receptivity to nontraditional exports is omnipresent, and often with good reason. Apparel exports, the first step on the export-led industrialization ladder for a host of countries, has been the most *protected* manufacturing industry in most industrial nations, including the United States.[47] Likewise, some agricultural exports from SSA have been limited by quotas, tariffs, and other restrictions.[48] On the other hand, the Lomé Convention has offered preferential access to the highly protected European market for limited quantities of agricultural commodities as well as manufactured goods. Under the Generalized System of Preferences (GSP) developed in the 1970s, the United States and other industrial countries offer preferential access to many types of manufactured exports from SSA countries. However, these special programs have been limited in scope and subject to periodic revision. Thus, they provide a narrower and less reliable basis for export-oriented investment than trade liberalization that is locked in through WTO negotiations, as discussed below.

The World Bank study of trade policy reform in the 1980s identified growing protectionism in international markets as one of several factors constraining exporters' response (Thomas, Nash *et al*. 1991). Indeed, it is axiomatic that export-oriented development would work better if the rich countries were more willing to adjust out of sectors that have clearly lost their comparative advantage. But, as Sachs and Warner (1995b) conclude, it works even under less than ideal external conditions. Between 1970 and 1989, "[w]ith the...exception of Haiti, there is not a single developing country that had substantially open trade and yet failed to grow by at least 2 percent per year."

Studies focusing instead on countries that have remained insulated from global markets tell a similar story. As noted above, World Bank research into the causes of SSA's declining share in world exports concludes that OECD trade barriers in potential export markets are not to blame: "Rather, the Sub-Saharan African countries' own trade and transport policies incorporate a substantial anti-export bias, which lessens their ability to be competitive in international markets" (Yeats *et al.*1996). As the model in Chapter 5 shows, the greatest bias against exports in Africa has been the lack of growth. If anything, exports from SSA should have gained an advantage in the markets of industrial nations from trade preferences under the Lomé Convention as well as the GSP, but these preferential arrangements were apparently insufficient to offset the anti-export bias of the nations' own policies. Rodrik (1998) concludes that "trade policy in Sub-Saharan Africa works much the same way" as elsewhere; dismantling SSA's high trade restrictions can be expected to improve trade performance significantly, notwithstanding the region's geography and poor infrastructure.

However, as countries reform their own policies, the benefits from import liberalization in important market countries are accordingly increased. In the past, SSA has been marginalized in GATT/WTO negotiations by well-intentioned but ineffective rules on special and differential treatment for less-developed countries. These rules, based on the outdated notion that developing countries benefit by building up their industries behind protective walls, exempted developing countries from the reciprocal liberalization required of wealthier members. Developing countries lost twice, first because of the reduced incentive to eliminate their own trade barriers, and second because bargaining tended to focus on the goods of greatest interest to the industrial countries. In their assessment of Africa's past and future role in multilateral negotiations, Wang and Winters (1997) argue that although SSA countries won fewer concessions in the Uruguay Round than other developing countries, possibly because they offered fewer, they nonetheless emerged from the round facing fewer restrictions. However, Wang and Winters maintain that SSA countries stand to gain through active participation in the next round of negotiations, both giving and requesting concessions.

i. External shocks

All efforts to promote reform are subject to shocks and disruptions. Even so-called healthy economies that are, by definition in external and internal balance, are subject to unanticipated positive and negative perturbations. For an adjusting economy, the basic problem is that negative shocks always stretch the economy beyond what little remains of its “safety margins” whether these are foreign exchange reserves, short-term borrowing capacity, or local investors’ tolerance for more bad news. The challenge for policy makers is to ensure that when shocks occur their policy response avoids (to the extent possible) any retrograde step that will adversely affect the process of reform.

We have already noted that fiscal difficulties in SSA countries have typically prevented the lowering of trade taxes. One of the biggest, but unfortunately most common, policy mistakes in SSA has been to deal with a fiscal shock by raising tariffs. This has two adverse consequences. First, it re-distorts the rates of effective protection within the economy. Second, it undermines confidence in the integrity and continuity of trade reforms. Potential beneficiaries of trade reforms reason (correctly) that fiscal shocks will recur. If the government can raise tariffs in response (even if temporarily), it can do it again.

It is never easy to deal with economic shocks even when policy makers understand that they are inevitable. The basic issue, however, is not the shock itself but the response. Research covering a variety of both positive and negative shocks in SSA (Asea and Reinhart 1997; Bevan, Collier and Gunning 1987) shows that the response by governments to the shocks have typically exaggerated the effects. A major error has been for African governments to treat positive shocks as permanent and negative shocks as temporary. The former leads to governments (e.g. Kenya during the coffee boom in the mid-1980s) to expand expenditure at rates that, when the boom ended, could not be sustained. The latter leads governments, such as Zambia in the mid-1970s, to attempt to finance their imbalances rather than adjust (Lewis and McPherson 1994). In these, and other, circumstances, the effects of the original shock have been amplified rather than attenuated. In Kenya’s case, the over-expenditure boosted the budget deficits, raised inflation and worsened the balance of payments. In Zambia’s case, the lack of adjustment led to a rapid expansion of foreign debt setting in motion a cycle of retrogression from which the economy has yet to recover.

Governments responding effectively to shocks would seek to rebuild their safety margins (foreign exchange reserves and domestic borrowing capacity) when they are positive and adjust as rapidly and broadly as possible.

Many African officials see globalization as a shock. Properly interpreted, the increased globalization of markets presents both opportunities and challenges. The opportunities arise from the ability of African countries to tap broad, dynamic (and essentially) unlimited markets. The challenges arise through the restrictions imposed on the ability of policy makers to attempt illiberal or counterproductive policies (Summers 1995). In this sense, globalization restrains African policy makers in ways that heretofore they have not experienced.

j. Donor Conditionality

The principle of donor conditionality is now well established. Depending upon the forum (the United Nations has been the most common) African leaders have rejected the idea. Notwithstanding the widely held objections, the practice of imposing conditions on assistance remains firmly entrenched in Africa. Since the majority of African countries are unable to service their external debts according to the agreed schedules and most are unable to finance their development plans without extraordinary assistance, some means of assuring creditors (and grantees) that the resources they provide will be used roughly as intended is required. Given their financial circumstances, African governments should expect to have conditions attached to the assistance they receive.

What is not to be expected, and should be changed, however, is the pattern of donor conditions that has emerged over time. Some donors, primarily the World Bank, have attached literally dozens of conditions to particular programs. The result is the *carte blanche principle* (Leibenstein 1980) carried to the extreme. This often produces outcomes directly opposite of what the agency applying the conditions expects. With so many conditions, SSA countries can easily begin playing "games" against the donors. Not all conditions are essential to reform. Countries will fulfill the easiest and hold back on those that are technically more difficult (e.g., introduce a value-added tax in two years) or those that are politically unacceptable (e.g., eliminate subsidies on staple food or collect income tax from agricultural producers).[49] Donor agencies then face the problem of deciding whether or not the conditions that have been met represent a good faith effort at reform. So far, the major aid agencies, both multilateral and bilateral, have tended to adopt a relatively loose definition of what good faith implies. Indeed, with the continual revision of donor support, at the Paris Club, through the G-7 (or G-8), and through the Highly Indebted Poor Country (HIPC) debt initiative of the World Bank and the IMF, African policy makers understand that donor agencies will continue to change the "rules of the game."

This sense of fluidity has undermined both the intent and the practical effect of most donor conditions. SSA countries may miss various conditions and donor programs may be suspended but some compromise will always be reached, although it may take time and it may result in further economic decline. For their part, the donor agencies understand that they are part of the "game" as well. That they continue to seek ways to aid Africa in the face of non-performance and policy reversals reflects their acceptance that African countries have become "wards of the international community" (Krugman 1989:204). It also reflects the fact that foreign aid is a multi-dimensional business that has a dynamic independent of the goal of helping poor countries.

None of this provides the basis for sustainable economic reform. A number of scholars and practitioners (Fernholz *et al.* 1996; Berg 1996; HIID 1997; Hill and McPherson 1998; McPherson and Gray 1999) have argued that African countries and the donor agencies should take steps to work African countries off aid. Such a program would return aid to the position that policy makers once believed was productive: namely, that it represented a reasonable response to well-defined problems, that it be limited over time, and that it be based on the principle of self-help (Bell 1965). At present none of these criteria apply in Africa. It is doubtful that aid will begin to gain the effectiveness commensurate with its size (recently around 12 percent of GDP for countries in SSA outside of Nigeria and South Africa) until these criteria are applied.

k. Overview

There are many reasons why reforms, once formulated, are not fully implemented. Some reforms are difficult politically, some are difficult technically, and some reforms are easy to reverse if the economy experiences a shock. No one doubts that policy reform can be exceedingly difficult. Yet, there are now scores of countries outside Africa (both rich and poor) that have taken the steps needed to transform their economic systems in ways that remove the internal and external imbalances that are blocking growth and development. Apart from Mauritius no African country has experienced such a transformation. Reform has been started in many areas; it has been completed in few. The result is that African countries, instead of experiencing growth and development, continue to struggle to reform.

5. Concluding Comments

What lessons might countries in SSA that are in the process of promoting trade and exchange rate reform draw from our discussion? The experience outside Africa indicates that despite many difficulties, the countries that have persevered with trade and exchange rate reforms have made significant progress. The world economy has given a major boost to economies that have followed a growth and export oriented strategy. The only country in Africa that has a sustained record of such a strategy has been Mauritius. It is one of the most rapidly growing economies in SSA.

The experience elsewhere also highlights the heavy cost to countries that abandon trade and exchange rate reform. Those costs are reflected in lower growth rates and economic instability. They have been most obvious in SSA where the majority of countries has made numerous attempts to reform their trade and exchange rate systems only to back off.

Is the institutional setup in African countries robust enough to promote and sustain reform? Is the leadership sufficient to ensure that reforms are sustained? What are the political dangers of promoting reform and how can these be reduced? What are the compelling political reasons to promote and sustain reform? How would a reform-minded government ensure that the forces seeking to reverse reform are deflected?

Our analysis shows that start-stop trade and exchange rate reform has been a dead-end for African countries. Since trade reform has been fundamental to all efforts to adjust in Africa, getting started has not been the principal difficulty. Problems have arisen in sustaining the reforms. The discussion highlights a number of activities that will increase the probability that reforms will be sustained. These include highlighting the costs of *not* adjusting, maintaining a realistic real exchange rate, enforcing macroeconomic discipline, promoting savings and investment, rationally phasing reforms, promoting reciprocal trade arrangements, and adjusting to the pressures of globalization.

Will any of these measures succeed? The majority of African countries is mired in almost three decades of poor economic performance punctuated by extended periods of stagnation and decline. There have been many efforts to promote reform. Many reform programs have been abandoned. The challenge for all African governments is to move their economies to growth paths that will provide rising standards of living for all their people. After so many mis-cues and so much effort dissipated, the message is clear. Keep the agenda simple and stick to it. For all countries trade and exchange rate reform is one of the key items on that agenda.

Annex: Trade Reform and Labor Rewards

Because it has a direct impact on *effective protection*, i.e., the relative degree to which payments to primary factors can rise or fall due to restrictions on trade, trade reform is relevant to labor issues and employment. At one time, much of the discussion of the potential impact of liberalized trade focused on the temporary or permanent increases in income inequality due to changes in labor earnings relative to the return on capital, especially foreign-owned capital. Today's concern focuses more on the observed increase in the gap between earnings of SSA's skilled and unskilled workers, which some attribute to increased openness.

For a world of two factors, the Stolper-Samuelson theorem predicts exactly this outcome in countries with abundant supplies of skilled labor like the United States. However, the same model also predicts a shift to a lower ratio of unskilled to skilled labor ratio in production, the opposite of what has been observed in most industrial nations. For this reason, Lawrence and Slaughter (1993) argue that skilled-biased technical change rather than trade lies at the heart of the controversial trend (see Bhagwati 1995). Moreover, the Stolper-Samuelson model predicts a fall in the same differential for countries that have abundant unskilled labor, i.e., less-developed countries. In fact, the skill premium has risen in many of these countries.

One explanation for a rising skill premium in developing countries is that the technology transfer associated with growth of nontraditional exports causes a temporary increase in demand for skilled labor. Even though the exports themselves may be unskilled-labor-intensive in production, skilled labor is needed initially to adapt and implement the imported technologies (Pissarides 1997). Also, the Stolper-Samuelson and factor-price-equalization theorems predict changes in *equilibrium* factor rewards with both factors fully mobile between sectors, and then only under other special conditions. Given the recent pace of policy change in the developing world, the situation can hardly be viewed as representing an equilibrium.

Related concerns are the perceived increase in the volatility of earnings and the increased uncertainty of job tenure associated with participation in international markets (Rodrik 1997). These concerns can to some extent be addressed through a social safety net, and indeed Rodrik demonstrates a high correlation between measures of countries' openness and social spending. Furthermore, he points out that increased international mobility of capital implies that such a safety net cannot be financed primarily through taxes on income from capital. However, as long as openness produces *aggregate* gains to a nation's labor force, social insurance for workers can be financed without increased taxes on capital income.

The recent high unemployment rates in some African countries reflect slow adjustment to trade and macroeconomic reforms in the presence of labor-market distortions. But whatever their causes, increased income inequality and/or volatility can undermine the perceived fairness of outward-oriented policies even if they are accompanied by enhanced growth of per capita income. While countries differ widely in the approaches used to make these changes acceptable to their citizens, it is an issue that must be addressed if integration with international markets is to remain politically viable. Several decades of reform in Mauritius were accompanied by a variety of measures to protect employment and create new jobs, measures that sacrificed allocative efficiency but may have helped to maintain the political viability of the reform process.

One of the countries in SSA which is having the greatest difficulty reconciling the requirements of trade reform (to spur competition and take advantage of new production opportunities) and the removal of labor market restrictions is South Africa. Years of economic regression and disruption sustained by high degrees of trade protection have led to high rates of unemployment of unskilled and semi-skilled labor (Sachs 1996). The way forward for South Africa has to focus on reducing the rate of unemployment. One approach is to liberalize trade. This runs into strong resistance from the farming community (mainly the entrenched large scale, white farmers). It also meets strong resistance from the existing labor unions and the Communist Party (which has traditionally supported the African National Congress). The outcome has been minimal reform (Stryker *et al.* 1998).

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Endnotes

[1] This paper was substantially completed in August 1998. It has been lightly revised for this volume to update some of the data and historical developments.

[2] While Rodrik (1998) attributes the slow growth in these liberalizing countries to "extremely poor human and physical resources," he also notes that Mali's economy revived as soon as the CFA franc was devalued in 1994. As discussed below, changes in trade policy alone may have little effect without accompanying reforms in the foreign-exchange regime.

[3] Harrison (1996) summarizes and evaluates several major econometric studies linking openness and growth. See also OECD (1998).

[4] Although they provide a convenient summary, regional averages can be misleading because of the disparate sizes of national economies. South Africa alone accounts for nearly half of total GDP in SSA but less than 10 percent of its population; South Africa and Nigeria together account for about 60 per cent of the region's total income. Nigeria is also the most populous SSA country, with nearly 20 percent of the region's population. Ethiopia, in 1996 the world's second poorest country after Mozambique, accounts for nearly 10 percent of SSA population.

[5] More recent data confirm this trend. Many African countries had negative export growth over the period 1990 to 1997 (World Bank *World Development Indicators* 2000, Table 4.4).

[6] The decline in copper volume can be traced to the lack of reinvestment in productivity-enhancing capital and a general deterioration in the physical infrastructure (railways, processing plants) of the mining sector.

[7] Current IMF advice counsels early introduction of a value-added tax (VAT) to offset revenue losses from tariff reductions (Sharer *et al.* 1998). In Mauritius, quantitative import restrictions were replaced by tariff equivalents in 1984-85, but progress toward rationalizing the complex tariff structure and reducing average rates was delayed until 1994, when a VAT was introduced.

[8] More recent data on these variables can be obtained from the World Bank’s *African Development Indicators* 2000 CD-ROM. Series on the “parallel market exchange rate” and “ratio of parallel to official rate” show a broad reduction of foreign exchange premia for most countries during the 1980s and 1990s. While individual trends in tariff rates are not widely tabulated (cf. Table 3 in the text), some trends in effective trade taxes can be derived over time using the series “taxes on international trade” and “GDP at market prices” from the above data source.

[9] As in the NBER project, the binary Sachs-Warner openness measure relies on subjective evaluation of information from diverse sources. The IMF measures overall trade restrictiveness on a scale of 1 to 10 based on average tariff rates and the incidence of NTBs, the latter given greater weight on grounds that NTBs are "inherently less transparent and more distortionary" (Sharer *et al*. 1998, 33). Other researchers attempting to establish statistical links between trade and growth have used a variety of statistical measures of openness. Harrison (1996) surveys recent contributions. Outcome measures based on export or import volume or on divergence between domestic and foreign prices implicitly consider effects of both trade and exchange-rate policies.

[10] For Comoros, the devaluation was 25 percent.

[11] This is not the case for heavily-indebted countries with large external arrears. The black market premium typically responds to excess demand for foreign exchange for current market transactions and countries that receive large net aid flows.

[12] The data are available on www.wt/inf/6/rev.5 (3 February 1999).

[13] A feature peculiar to SSA and a few other less-developed countries (e.g., Cuba) is the role in the 1970s and 1980s of the USSR and China in providing policy advice and training abroad of future government officials. The result was to sustain the preference among officials for central planning and *dirigiste* policies.

[14] For some years, President Museveni of Uganda was seen as such a leader. Widely praised for leading his country from “basket case” to “show case,” there has been some recent reassessment of his contribution in light of Uganda’s expansionism in the former Zaire and evidence of mounting corruption within the Museveni regime (Collier and Reinikka 1999).

[15] In 1995, Zambia reversed much that had been achieved in its reform of import and excise duties to cover a “financing gap” that had emerged because of lack of expenditure control (Hill and McPherson 1999).

[16] This view re-surfaced across a broad front with the difficulties in East Asia and Russia (Krugman 1998).

[17] Tariffs are a more transparent form of protection than NTMs and are less likely to protect the domestic market power of import-competing producers. Moreover, tariffs entail less administrative discretion and thus less likelihood of rent-seeking activities that add to the cost of protection. In principle, tariffication is a first step in import liberalization, to be followed by staged reductions in tariff rates. However, revenue-constrained SSA countries often postpone or reverse them. As noted above, Mauritius replaced NTMs by tariffs in 1984-85, but progress on rationalizing the tariff structure and reducing average rates was not undertaken until a decade later, after enactment of a VAT.

[18] An external evaluation of the IMF's Enhanced Structural Adjustment Facility suggested that "ways should be found to better anchor these programs in national consensus and ownership as a way of ensuring the sustainability of these programs" (IMF 1998).

[19] For example, Senegal's stalled economic reform in the 1980s is commonly linked to political pluralism in one of the region's most democratic regimes (Ka and van de Walle 1994). Yet Mauritius, the best example in SSA of successful export-led development, is also a pluralistic democracy governed by a coalition of parties.

[20] If individual voters are unsure whether they will be winners or losers from liberalization, majority voting may reject even a trade reform that benefits the median voter (Rodrik 1996). Myopia and risk aversion exacerbate the problem of getting voters to support efficiency-raising reforms.

[21] In practice, few policy makers were concerned that the supply of cheap food was maintained through foreign aid at the expense of local farmers.

[22] The role of improved data monitoring and analytic capacity in reform is highlighted by Duesenberry and McPherson (1992) and McPherson and Radelet (1995).

[23] This is directly consistent with theories of the “option value.” When reform requires a large commitment that has a major irreversible component, risk-averse decision-makers attach a high value to the option of waiting (Pindyck 1991; Hubbard 1994; Severn 1997).

[24] The external review of the ESAF program (IMF 1998a, 18) points to the need for increased capital inflows into low-income SSA economies once they have achieved a satisfactory policy environment and proposes ways the IMF can “signal that a country has reached the phase in which the macroeconomic policy environment is satisfactory for private investment.” This suggestion implies that private investors are currently passing up profitable opportunities because they lack information on recent policy improvements in SSA economies. More likely, however, potential investors (many of whom are local entrepreneurs with resources abroad) have serious doubts that the reforms will be maintained. Such doubts will not necessarily be laid to rest by IMF certification, especially when countries in SSA have on several occasions adopted and then abandoned IMF programs.

[25] This is countered in part by the support by the IMF and World Bank for programs of maintaining health and education expenditure even in the face of other budget cuts. Such approaches are effective so long as rural health and education programs are supported. Cash-strapped governments in Africa have rarely bothered.

[26] Trade economists have long made the point that an overvalued exchange rate gives a country the appearance of having a comparative disadvantage in most traded goods.

[27] This has (perhaps) been one of the greatest ironies of the post-1973 restructuring of the Bretton Woods arrangements (Eichengreen 1996). The industrial countries that have the deepest financial systems and uniformly most coherent institutional settings do not have the capacity to re-fix their currencies in the face of international capital movements. The developing countries, which have neither advantage, have typically opted for fixed exchange rate systems. Why should it be a surprise that these countries face major problems of persistent real exchange rate overvaluation, periodic balance of payments crises, and the accumulation of foreign debt that cannot be serviced without extraordinary international assistance?

[28] One problem has been that while CFA governments observed restrictions on their own budgets, their state-owned-enterprises typically made large losses and borrowed heavily abroad.

[29] The motive for maintaining a clearly overvalued official rate comes from the associated benefit for those who control access to the limited supply at this rate. The opportunity for rent-seeking with licensing of foreign exchange (typically by central bank officials) is thus similar to that associated with import licensing and other discretionary non-tariff barriers.

[30] Having decided to make a once-for-all realignment of the CFA franc, the challenge for these countries is to ensure that the degree of real devaluation (which averaged around 30 percent) is not undermined over time. So far, most CFA countries have been fiscally prudent. They have not, however, fully rationalized their excessive external debt, reformed their respective civil services, or brought their state-owned enterprises into line. Without purposeful and permanent actions in these (and other) areas of reform, the real devaluation will eventually unravel.

[31] The Gambia's experience in the mid-1980s confirms this. A major crack-down on tax fraud enabled the government to systematically reduce trade taxes (*the* major source of government revenue) without losing aggregate revenue (McPherson and Radelet 1995). A study on tax compliance in Madagascar by a team supported under EAGER/PSGE reached the same conclusion (Andrianamana 1998).

[32] This is especially the case in countries such as Zambia, Senegal, Tanzania, and Zimbabwe where the scope of government expenditure expanded well beyond the economy's capacity to provide necessary services.

[33] Zambia had a single purchasing agency (the National Agricultural Marketing Board) that was responsible for all aspects of crop marketing. Through a system of pan-territorial and pan-seasonal pricing which delivered subsidized fertilizer to farmers and subsidized staple food to urban consumers, the Board habitually lost money, up to 8 percent of GDP per annum on some occasions (World Bank, 1995).

[34] This standard is highly but not perfectly correlated with others that give a better picture of changes in the living conditions of the "typical" member of the population, such as infant mortality, longevity, access to clean water, and literacy. Another recent concern not captured by conventionally measured growth in PCI is degradation of the environment, including inefficiently rapid depletion of natural resources. This concern is addressed in the growing emphasis on *sustainable development*, i.e., development that doesn't mortgage the welfare of future generations (Solow 1992). It is also reflected in the World Bank's focus on estimating "genuine savings" which takes the depletion of resources into account (World Bank *WDI* 2000, Table 3.15).

[35] While much care has been taken in constructing the income (and consumption) distribution data over recent years, there are systematic errors through the increasing ability of the very wealthy to move (and operate) their resources offshore. Globalization of financial markets has allowed the wealthiest members of African societies to benefit from residing in Africa with few of the financial risks this involves. Given these biases, it is especially ominous that recent data suggests that income distributions have worsened.

[36] This is shown in a related for EAGER/PSGE by McPherson and Rakovski (2000).

[37] A body of research has emerged (Gallup, Radelet and Warner 1999; Dollar and Kraay 1999) suggesting that growth is good for the poor. This conclusion emerges from cross-country regressions showing that over time the growth of income in the lower income groups has not been systematically lower than overall income growth. Others such as Gugerty and Timmer (1999), however, have pointed out that this does not hold if the initial distribution of income and wealth is highly skewed.

[38] President Clinton, more than any other U.S. president, has devoted considerable energy and effort to issues related to Africa. In addition to two trips to the continent, he supported the passage by the U.S. Congress of the Africa Growth and Opportunity Bill that seeks to expand U.S./Africa trade and business contacts.

[39] The United States Government has an Inter-Agency Credit Assessment Committee. By its assessment, only a minority of African countries are considered creditworthy and thereby eligible for Export-Import Bank credits and OPIC (Overseas Private Investment Corporation) support. Some see this as a continuation of the anti-Africa bias; others see it as a prudent assessment of the risks.

[40] This is a major area in which African countries have to catch up. With few exceptions (again Mauritius), the financial systems in Africa remain inappropriately narrow. This is evident among most African central bankers, few of whom have adapted to the realities of globalization. This can also be seen in the continuing efforts by central bank officials to control exchange rates or to simultaneously influence the exchange rate, interest rate and stock of foreign reserves. Private citizens, who better appreciate the opportunity costs involved, typically work both sides of the local and global financial system to their advantage (Hill and McPherson 1998; McPherson 1999).

[41] Krueger (1993) points out that the perceived need for these policies may arise from the negative consequences of import substitution. Such cascading of controls, however, is counterproductive.

[42] The lack of theoretical basis of optimal sequencing is discussed in McPherson (1995).

[43] Edwards (1995) summarizes the main findings of the sequencing debate but comments that sequencing of reforms has come to be viewed as largely a political issue. McPherson (1995) likewise argues that, in the case of Zambia, economic performance would have been improved "if only *some* economic reform had been sustained, irrespective of how the policies were sequenced."

[44] The reasons are theoretical and practical. Strotz (1956) showed that when conditions can change it is never optimal to agree to an unwavering adjustment program in advance. Lucas (1976) argued that policy implementation changes the underlying structure of an economy thereby altering its response to policy over time. That is, Strotz showed that one shouldn’t derive an optimal path in advance; Lucas showed that one couldn’t. In practical terms, the uncertainties of implementation require policy makers to adapt their approach to reform as experience accumulates.

[45] In a world of many overlapping preferential arrangements, apparent trade diversion may in fact represent redirection of trade flows along lines of comparative advantage, i.e., correction of previous trade diversion. For example, the creation of the Southern Africa Power Pool provides surplus power producers such as Zambia an opportunity to begin selling power to more lucrative markets such as Botswana and South Africa. Formerly, surplus power was absorbed by Zimbabwe.

[46] In the Uruguay Round, negotiators agreed informally to give developing countries credit for earlier unilateral tariff reductions which were subsequently bound under the GATT/WTO. Finger, Reincke, and Castro (1997) find evidence from the pattern of total and bound concessions that developing country binding of earlier unilateral reductions was "treated at the Round as an action of substantial value."

[47] The Uruguay Round of multilateral trade negotiations produced an agreement to phase out the Multifibre Agreement (MFA), the global network of quantitative restrictions on trade in textiles and apparel, over a ten-year period. However, many trade policy experts are pessimistic about a return to open markets for these important

developing-country exports. They interpret the long phase-out period as indicating a lack of real commitment to liberalization on the part of OECD nations.

[48] As discussed below, the concern about finding export markets underlies much of the interest in RTAs.

[49] All of these conditions (and close to a hundred others) were attached to the World Bank/IMF program for Ethiopia (McPherson 1998).

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