



*BOTSWANA INSTITUTE FOR  
DEVELOPMENT POLICY ANALYSIS*

# WORKING PAPER

**The Role of Africa in the Global Economy:  
The Contribution of Regional  
Cooperation, With: Particular Reference  
To Southern Africa**

**Paper Written at the Request of the Vice President and Minister of Finance  
And Development Planning As Background for His Speech to A Conference  
Organised By Partnership Africa in Sweden in June 1997**

**By Charles Harvey  
BIDPA Working Paper No. 11  
June 1997**

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### Abstract

The paper discusses Africa's importance in the world economy. It asserts that Africa's importance has declined over the years. The decline coupled with extreme poverty in most of Africa calls for analysis of possible ways to reverse the negative trend. Together with the prospects for regional cooperation, regional integration of intra-Africa is discussed as one possible way to accelerate African economic growth in Southern Africa

#### Keywords

Regional cooperation  
Regional integration  
Economic growth  
Africa

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Role of Africa in the Global Economy, The:  
Harvey, Charles; BIDPA  
Book 330.4 BOX BIDPA

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<sup>1</sup> Botswana Institute for Development Policy Analysis (BIDPA) is an independent trust set up by a Presidential Decree. It started operations in 1995 as a non-government policy research institution

## **Botswana Institute of Development Policy Analysis**

Working Paper, July 1997<sup>1</sup>

### **The role of Africa<sup>2</sup> in the global economy: the contribution of regional cooperation, with particular reference to Southern Africa**

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#### **1. Introduction**

To a very great extent, Africa's role in the world economy derives from its economic importance to the rest of the world: in international trade and as a destination for international investment. Africa's importance defined in this way is currently very small, and has declined over a long period. This, combined with the extreme poverty in much of Africa, means that every potential way of reversing the negative trend should be analysed. One possibility is greater regional cooperation. This paper concentrates on one particular aspect of regional cooperation, namely regional integration of intra-African trade.

There are many other forms of regional cooperation which also have the potential to accelerate African economic growth. The list is long, but might include water, electricity, transport, the environment, control of disease (both livestock and human), tourism, financial services, crime control and telecommunications.<sup>3</sup> There has been some progress in Southern Africa in some of these sectors. Indeed, it can be argued that genuine progress is more likely by tackling the detailed requirements of cooperation in particular sectors, than in attempting to create ambitious regional trading arrangements. Nevertheless, the creation of regional trading blocs has been and remains a major theme of intra-African cooperation. It absorbs a great deal of the time and resources of African governments, and tends to have a higher profile (perhaps wrongly) than other forms of cooperation. This is the reason for further discussion of it in this paper.

<sup>1</sup> This paper was written at the request of the Vice-President and Minister of Finance and Development Planning, the Honourable Festae Mogae, as background for his speech to a conference in Sweden in June 1997, organised by "Partnership Africa". Minor revisions have been made to the version used by the Vice-President, whose views are not necessarily those expressed in the paper. <sup>2</sup> In this paper, "Africa" is used to mean Sub-Saharan Africa. All the statistics refer to Sub-Saharan Africa, and therefore exclude the countries in North Africa. <sup>3</sup> There is a more comprehensive list, for Southern Africa, in the extensive study by the African Development Bank [1993].

There are objectives of regional cooperation other than increasing economic growth. A second possible objective is to give African countries a more significant voice in their relations, both political and economic, with the rest of the world than would be available to individual countries. It should be noted, though, that for African countries to speak and negotiate as a group, they would have to agree on each issue to be negotiated, and that becomes more difficult the more countries become members of the group.<sup>4</sup> This is part of the rationale for establishing regional cooperation among sub-groups of African countries.

Thirdly, regional cooperation might reduce conflict; indeed, this has been the underlying objective of some attempts at regional cooperation, both in Africa and elsewhere. Much of Africa's economic decline can be attributed to wars, so that if regional cooperation could reduce conflict, it would have a major positive economic impact as well as achieving the more basic objective of reducing the human cost of wars.<sup>5</sup>

Again, these other objectives of regional cooperation are neglected in this paper, which concentrates on the potential for increasing Africa's GDP faster than in the past, and (it must be hoped) faster than other regions in the world, as a prime means of Africa becoming less marginalised in the global economy.

The next section of the paper (Section 2) sets out the relative economic importance of Africa in the global economy, showing that it has declined, and examines the prospects for a reversal of this trend.

Section 3 then discusses the theoretical reasons for the integration of regional trade, whether it provides the expected benefits, and whether it results in greater inequality among member countries (polarisation) or in poorer countries catching up on richer ones (convergence).

Section 4 notes that Southern Africa contains the longest lasting regional trading arrangement in Africa, the Southern African Customs Union (SACU). It notes also that the poorer countries in SACU have converged on the richer economy of South Africa, asks whether SACU's experience has lessons for the rest of Africa, and discusses the prospects for the establishment by SADC of a larger regional trading bloc in Southern Africa.

Section 5 concludes by arguing that Southern Africa may be an exception to the poor record of regional integration in Africa, but notes that open trading with the rest of the world,

<sup>4</sup> This goes some way to explaining why the role of the Organisation of African Unity is so difficult. <sup>5</sup> Note, though, that some of the African economies which declined disastrously did not suffer from wars; their decline can be attributed almost entirely to the economic policies of their governments.

particularly by the slow-growing economy of South Africa, is even more important than regional integration. The latter may be necessary, but is not sufficient for rapid economic growth.

## 2. Africa's relative economic importance in the global economy

### *(a) Relative importance of Africa's GDP*

Much of the rhetoric concerning the benefits of African economic integration appears to assume that a united Africa would be a major economic force. However, even groups of several countries would carry relatively little weight because Africa's total GDP is so small, in relation to that of the rest of the world. The GDP of the whole of Sub-Saharan Africa in 1994 was just 1.1% of global GDP.<sup>6</sup>

An even more striking comparison, perhaps, is that it was less than the GDP of the Netherlands, which in turn has long regarded its economy as much too small for the country to be economically independent. The Netherlands formed an economic group with Belgium and Luxembourg even before the creation of the European Common Market, of which it was a founder *member*

So even if all the countries in Africa were by some miracle to agree to trade freely with each other, their combined economy would still be smaller than that of the Netherlands, and would not therefore be nearly large enough to generate rapid growth from economies of scale. Moreover, the Netherlands is a small country geographically, with high quality internal transport. Africa has dreadful internal transport. Even if intra-African transport links were hugely improved, the distances would still be vast and internal transport would therefore still be expensive compared to that of smaller and more densely populated economies. Regional integration of itself would not, therefore, deliver significant economies of scale immediately, and thus would not significantly increase Africa's role in the global economy.

### *(b) Africa's market is shrinking, not just relatively but absolutely*

What is even worse is that Africa's importance to the world economy, never very great, has diminished in recent years, by about 7% in real terms between 1980 and 1994. Population continued, of course, to grow (by 3.0% a year from 1980 to 1990, and by 2.7% a year subsequently) so that income per head fell: at an average rate of 1.2% a year from 1980-94. Other developing economies continued to grow, some very rapidly, so that Africa's *share f-f*

<sup>6</sup> Statistics in this Section taken from World Bank *World Development Report 1996*.

the GDP of low and middle income economies fell from 9.2% to 5.3%, in the 14 years to 1994

The widespread failure of African economies to grow has reduced the importance of Africa as a market for the rest of the world. Africa's share of the imports of low and middle income countries fell from 12.2% to 5.7%. Moreover, a significant percentage of imports was financed by aid, which amounted to very large percentages of GDP for several African countries (more than 100% for Mozambique and Rwanda, and more than 30% for a further five countries, in 1994). Overall, aid paid for more than half of Africa's imports in 1994, so that Africa's importance as a market for the rest of the world was even smaller than suggested by the aggregate figures [World Bank, 1996].

(c) End of cold war-related strategic importance: a good thing

*A further factor reducing Africa's significance to the rest of the world has been the ending of the cold war. However, the financial flows to Africa in support of cold war objectives probably did more harm than good, both economic and political. Finance was provided irrespective of the economic policies of the recipient governments, much of it financed weapons rather than economic development, and it stimulated and prolonged wars.*

*It is also well known that at this type of aid delayed the departure of governments which otherwise would not, and should not, have been able to survive so long. Probably the best known example is the maintenance of Mobutu in power for 32 years because the US government supported his opposition to the government, perceived as Marxist, in Angola. Africa is better off without this type of aid, and without this sort of importance in the eyes of the rest of the world*

*It has been argued that the growth of Afro-American and NGO political influence in the USA is acting to prevent Africa from being marginalised, at least in America. However, there is a contrasting view, that the US Government is thoroughly disillusioned with intervention in Africa, especially since the failure of its venture in Somalia, to the point where the UN "has assumed the demonic role that creeping socialism used to play" in US foreign policy [Huliaris, 1996, quoting Blumenthal, 1995: p21*

(d) Neglect of Africa by foreign investors

*In these circumstances, it is not surprising, but extremely worrying, that Africa is almost totally neglected in the global competition for foreign investment. Africa's share, of the huge*

increase in direct foreign investment in developing countries in recent years, is only 2%, considerably less than its share of the GDP of low and middle-income countries. Moreover, most of this very small amount of investment is in mining enclaves. Almost none of it is in manufacturing.

Worse, there is now substantial evidence that foreign investors in manufacturing have been withdrawing from Africa [Benneil, 1995 and 1997]. Theory is in fact ambivalent about the impact of structural adjustment on the manufacturing sector: producers who were protected and were as a result uncompetitive with imports and therefore even more incapable of exporting, should either close or be forced to become competitive. Inevitably, many manufacturers, many of which should never have been established in the first place, probably should close, being incapable of transformation sufficient to become internationally competitive.

On the other hand, structural adjustment is intended to make investment in manufacturing more attractive by making it more profitable. It is therefore extremely disappointing that African countries, struggling with the immediate costs of structural adjustment, are not getting the intended benefits in the form of new investment in the tradable sector to replace the old protected industries.

One particular category of foreign investment is occurring, namely the takeover by South African companies of decayed firms in other African countries, many of them being sold as part of privatisation programmes. This type of investment is very recent, and does not therefore appear yet in the statistics;<sup>7</sup> overall, it amounted to R9 billion (US\$2.6 billion) between 1994 and 1996 (Harvey, 1996: 93). Unfortunately, this investment, together with other foreign purchases of privatised companies at what are seen as low prices, is causing political resentment. There is a danger that the somewhat extreme adoption of liberal economic policies will create a backlash. It would be tragic if the whole costly cycle of nationalist economic policy, leading to nationalisation and the creation of inefficient parastatal monopolies, were to be repeated because the pendulum has been allowed to swing too far in the liberal direction, without learning any lessons from the previous cycle [Harvey, 1993].

*(e) Reasons for pessimism and some limited optimism about future growth*

<sup>7</sup> It is of course intra-African investment, and will not therefore appear in statistics of net foreign investment in Africa.

The African market was never very significant, but in the 1960s and 1970s there was some optimism about future growth, so that there was at least some interest in the potential of the African market, despite its small relative size even then. That optimism has largely disappeared, except for a very small number of countries; moreover, South Africa accounts for some 44% of Sub-Saharan Africa's GDP so that many of those potentially interested in the African market need look no further than South Africa. The rest of Africa has even lost a small advantage it may have had under South Africa's apartheid government, when there was some reluctance to trade with and invest in South Africa and some other African countries gained at South Africa's expense.<sup>8</sup>

Secondly, of the large number of African economies which declined seriously, relatively few have been successfully revived. Recovery is constrained by huge levels of foreign debt service, only half of which is currently being paid, and which is a claim on any increases in export earnings which may be achieved, and on any reversal of the recent decline in aid. There has recently been some action on reducing Africa's debt to the multilateral institutions: for example, Uganda became eligible in April this year to have some of its multilateral debt reduced, under the IMF-Bank initiative for heavily indebted poor countries (HIPC's), because of its good policy track record [IMF Survey, 12 May 1997]. Although this is an important change in the previous absolute refusal of the multilateral lending institutions to consider rescheduling or cancellation of their loans to developing countries, the reduction amounts to only 20% of Uganda's foreign debt in net present value terms.

Thirdly, recovery must be based on export growth, but it has been argued that reversing the decline in Africa's share of world export markets has become more difficult. Africa's main comparative advantages, raw materials and low-paid unskilled labour, are diminishing in importance as a consequence of technical developments, especially in information technology [Daniel, 1996: p89].

Fourthly, economic reforms have in many cases been implemented by the same governments whose policies had to be reversed. This reduces confidence that these governments will persist; their conversion to liberal economic policies is frequently less than wholly convincing. Even where governments have changed, the negative impression created by past policies, and past wars, is not necessarily reversed. The internal social and political forces which supported previous policies continue to be an influence on new governments as well as those which have continued in power.

<sup>8</sup> Swaziland was one country that attracted investment, mainly to enable firms to avoid sanctions: many of those firms have subsequently returned to South Africa.



The World Bank is publicly slightly more optimistic, but then it could hardly forecast further decline when so many countries have agreed to World Bank and IMF conditionality. In March 1997, 25 out of 50 countries in sub-Saharan Africa had IMF programmes [IMF Survey, 21 April 1997]. The Bank has forecast that per capita income will increase by a marginal 0.6% annually in the medium term, but even this forecast is based on a long list of highly optimistic assumptions [World Bank, 1993]. At this rate of progress, even if it is actually achieved, it would take about 40 years for per capita income in Africa to be restored to its level in the mid-1970s [Callaghy, 1995: 43].

There are some other reasons for arguing for that Africa's economy may recover, based on reversal of the main causes of economic decline. Recent research on the determinants of economic growth in Africa, or rather the lack of it, has identified with some degree of confidence the important variables.<sup>9</sup> These are excessive protection of producers (lack of openness), low levels of social capital, the high risks faced by investors and producers, and poor public services.

"Africa stagnated because its governments were captured by a narrow elite which undermined markets and used public services to deliver employment patronage. These policies reduced the returns on assets and increased the already high risks which private agents faced. To cope, private agents moved assets abroad and diverted their social capital into risk-reduction and risk-bearing mechanisms at the expense of social learning." [Collier and Gunning, 1997: pp65-66]

The reason for a certain amount of optimism is that openness to international trade has been enormously increased in a large number of African countries in recent years, and it is argued that the other reasons for stagnation are to some extent a result of lack of openness. These other constraints may therefore be reduced following economic liberalisation. Furthermore, there has been an extraordinary shift towards competitive multi-party elections in Africa; between 1989 and 1995, the proportion of African countries with competitive party systems went from 10% to 75% [Wiseman, 1996].

The extent of capital flight from Africa may also provide a somewhat paradoxical reason for optimism, despite, and perhaps because of, capital flight from Africa having been greater than from any other region of the world.<sup>10</sup> Capital flight was not just privately rational, but "may even have been a socially useful preservation of African wealth during a phase when it is

<sup>9</sup> This research is summarised in Collier and Gunning (1997). <sup>10</sup> Estimates of the composition of African investment show that 37% of it is abroad, compared with 3% in East Asia, even though Africa has a lower level of wealth per worker than other regions [Collier and Gunning, 1997: p3].

retention within the continent would have irreversibly depleted its value" [Collier and Gunning, op cit: 66].

As a consequence of that capital flight, there is a stock of finance which is potentially available for investment in Africa, and which is more likely than non-African owned finance to be invested in Africa. Even African-owned foreign capital, though, requires that governments create economic conditions which make investment attractive. In those African economies which are recovering from economic disaster, for example Ghana and Uganda, there are some indications that capital inflows from abroad have occurred, not from foreign investors but in the form of returning flight capital. The point is that nationals are less likely to be put off by the reputation of countries with bad past records than are newcomers to Africa, and have reasons for investing in their own countries which are not shared by foreigners. The large numbers of educated Africans who currently work outside their own countries are also a potential resource for recovery, again provided that appropriate conditions can be established which makes exiles want to return

In this debate on the prospects for African economic growth and recovery, the most recent statistics are encouraging. The African Development Bank estimates that GDP in Africa grew at 4.8% in 1996, the first time in years that it has been faster than the rate of population growth [African Development Bank, 1996]. and an even more recent estimate is that growth in 1996 was 5.5% [IMF Survey 9 June 1997]. It is much too soon to know whether this is the start of a sustained recovery, based on improved economic policy, or whether it is really caused by such reversible factors as better weather and higher export prices, both of which have played some part. Nevertheless, it is very much better to have some recovery to report, rather than continued decline; recovery has to start somewhere, and it may really have begun.

### 3. Regional integration

#### *(a) Theoretical advantages of regional integration*

The arguments for regional integration, as a means to accelerating economic development, are well known. The rationale most frequently referred to, by African governments, is the increase in size of the domestic market available to regional producers, which in turn is expected to induce investment which would not otherwise have taken place. It is correct that the domestic economies of all African countries, even the relatively large ones, are too small to provide the economies of scale required by some sectors of industry. It has therefore been argued, and widely believed, that integration of African economies, in a series of regional

groups, and eventually in a continent-wide common market, will provide the necessary economies of scale for successful industrialisation.

However, the statistics already quoted in the previous section show what a small market would be available to African producers, even if the whole of Africa were to become a single market. The gains from increased economies of scale would therefore be small, and far from providing a large enough market to enable African producers to compete with the rest of the world because of having a large domestic market, even if there were no other factors reducing efficiency. Those sectors of African industry which require economies of scale beyond those provided by the small African market, national or regional, must therefore export to the rest of the world.

This argument is reinforced by the structure of African demand. Much of GDP in Africa is still represented by subsistence output, and therefore creates no monetary demand at all; and a high proportion of monetary demand, much higher than in the developed countries, is limited to a range of the most basic consumer goods (many of which, such as clothing, do not anyway require significant economies of scale).

A second economic reason for pursuing regional integration is that it might generate faster growth, by other means than the creation of economies of scale. Increased trade, even within a region with relatively small total demand, can increase competition. This should generate increased efficiency over what was possible previously. In turn, increased efficiency could be a step towards being sufficiently competitive to export to the rest of the world, although this objective has been less emphasised in the stated objectives of regional integration in Africa than in, for example, Latin America [McCarthy, 1996: p2161].

A third reason for regional cooperation is that it helps member governments to pursue political and diplomatic objectives. It has been argued that regional groups flourished, with heads of state attending, so long as they were indeed useful in this way, but that they withered when the diplomatic gains were small, as in the case of ECCAS, the Economic Community of Central African States [Lancaster, 1995].

*(b) Polarisation: the unequal distribution of benefits*

The success of regional integration is not, unfortunately, assured even if it does deliver increased economies of scale and greater efficiency arising from increased competition. The distribution of benefits is fundamental to whether most attempts at regional integration are sustainable. Unequal distribution, whether actual or merely perceived by the participants, has

frequently been fatal. On this point, there are theoretical arguments on both sides. Integration may benefit richer members more than poorer ones, or the poorer countries may enjoy a process of catching up on the richer ones.

One likely consequence of increased competition is that some producers will increase output at the expense of others. It is theoretically possible that all producers will become more efficient under the stimulus of increased competition, but it is more likely that some producers will fail. Generally speaking, producers in the more advanced economy in any regional group will be more likely to gain, at the expense of producers in the less advanced economies. This polarisation effect is increased by the tendency of new investment to be attracted to the more advanced economy.

Whether or not this actually happens, the less advanced countries tend to believe that the more advanced are deriving more than their share of the gains from regional integration. Even if all members are better off, this perception of unequal gains has destroyed some attempts at regional integration, and prevented others from developing as planned. Obvious examples of regional integration which failed for this reason (among others) are the East African Community and the Federation of Rhodesia and Nyasaland, because of the perceived dominance of Kenya and Southern Rhodesia respectively.

A further disadvantage of pursuing regional integration in the expectation of deriving benefits from increased economies of scale, is the tendency for the member governments to direct new investments to locations chosen for political rather than efficiency reasons, resulting in high costs of production. Governments also grant monopolies to producers intended to serve the new regional market behind protective barriers; these monopolies are supposed to deliver lower cost products because of benefiting from economies of scale. The history of such protected monopolies is that any gains from economies of scale have been more than offset by inefficiency resulting from protection and lack of competition. They provided low quality and expensive products, to the point where they failed to capture the regional market, even with the advantages provided by protection.

Given the high failure rate of regional integration schemes in Africa, and the quite large costs of trying to establish and maintain them, the ratio of expected benefits to expected costs of new attempts at regional integration would seem to be very unfavourable: "in Africa, gains have been modest compared with the resources used in promoting integration" [McCarthy, 1996: p2 11, quoting Ravenhill, 1990: p8 1]. The costs include not just the direct and visible expense of bringing large numbers of people together at international meetings, but the indirect cost of senior government officials being absent from their desks in their own

countries. This cost is particularly heavy for small countries, where the number of able senior officials is inevitably limited, and the number of international meetings is no smaller than for larger countries. Most of the countries in Africa are relatively small and therefore suffer disproportionately from this problem.

*(c) Convergence: do poorer countries catch up with richer ones?*

Against this list of disadvantages, there is some convincing evidence of "convergence" in those regional groups which do survive for long periods, and do implement measures to generate free trade as opposed to making promises at international meetings which are not implemented. In other words, the poorer members of long-lasting customs unions, common markets and free trade areas tend to enjoy faster economic growth than the richer members, so that the income per head of all members tend to converge. This is the opposite of polarisation, which means that the richer members grow faster than, and possibly at the expense of, the poorer ones.

Research on convergence has not found evidence of it occurring in the global economy; on the contrary, there is evidence of increasing inequality between countries at the global level [Cohen, 1995]. There is, though, evidence of convergence in some groups of countries such as those of the European Union, or in regions of large economies such as Japan and the USA [Barrio and Sala-i-Martin, 1991]. It is important to note, though, that regions based on high existing levels of trade are more likely to converge than groups established for other reasons [Ben-David, 1995]. The evidence of convergence in regional groups has been an important stimulus for recent attempts at regional integration.

One measure of convergence (or divergence) is change in the dispersion of income per capita about the average for countries which have been regionally integrated. If member countries are relatively equal, then the dispersion is small, and if they are relatively unequal, the dispersion is large. If convergence takes place over time, the dispersion of incomes per capita gets smaller. This dispersion did indeed get smaller over the last 30 years in two of the longsurviving customs unions, namely the European Union, and the Southern African Customs Union.<sup>11</sup> This is shown in Figures 1 and 2, where the declining line shows reduced dispersion over time, and therefore that the poorer members were catching up on the richer ones.

<sup>11</sup> Statistics and Figures in this section are all taken, with permission, from Lynne Thomas "Is South Africa ready for regional monetary integration?" (mimeo, Centre for Research into Economics and Finance in Southern Africa, London School of Economics, 1996; forthcoming in volume of University of Lund conference proceedings).

The same data can be used to demonstrate both the existence and the degree of convergence. This shows whether the member countries which were poorer at the beginning of the period have had consistently higher rates of economic growth than those which were richer initially, and the absolute differences in growth rates. Convergence in both the European Union and SACU is further illustrated in this way in Figures 3 and 4, by the grouping of points about a line that slopes downward from the left, in both cases. Countries which started with a low level of per capita income, well to the left of the average line, had high rates of growth between 1960 and 1990; the poorer was the country initially, the higher was its rate of growth. Poorer countries did indeed, therefore, converge on richer countries in these two regions.

For interest, Figure 5 shows whether convergence (as measured by reduced dispersion of incomes) took place for the SADC countries, five of which were members of SACU, while the other seven were not. The SADC countries were not regionally integrated during this period, so there is no reason to expect that their economies would converge because of this factor. However, it is possible that the dominance of South Africa within the region could have created *de facto* integration. If this had been the case, then the convergence of SACU members should not be attributed to SACU itself, but simply to trading with the dominant economy in the region. In fact, as shown in Figure 5, there is no evidence at all of convergence in SADC; the line fluctuates around a roughly horizontal level, with if anything a slight tendency to rise rather than fall in the second half of the period.

This suggests (but does not of course prove) that the convergence among SACU members can indeed be attributed to some extent to the existence of the Customs Union itself. There are of course other reasons for the rapid growth of the smaller members, most notably the discovery of diamonds in Botswana; and there are other possible reasons for the slow growth of the South African economy, most probably the increasing economic cost of apartheid. Nevertheless, the difference between convergence in SACU, and the absence of convergence in SADC, is striking. It suggests quite strongly that SACU did contribute to convergence which would not have taken place in the absence of a customs union.

#### 4. Regional cooperation in Southern Africa

Given the failure of most previous attempts at regional cooperation in Africa, and the scepticism expressed about the likely success of current and future attempts, it seems important to ask why the Southern African Customs Union (SACU) has lasted for so long. Other regional organisations would presumably like to know whether they can replicate the

benefits which the smaller members have derived from convergence on South Africa's level of income per head, if it is indeed correct that these benefits derive from collective membership of SACU.<sup>12</sup> It is also important to question whether SADC's plans to shift its principal focus, from political and diplomatic objectives to plans for regional economic integration, are realistic, or whether they will result in yet another costly failure.<sup>13</sup>

SACU is clearly not comparable to, for example, the European Union. The original members of the European Common Market had relatively similar levels of per capita income, and those members were sufficiently rich to tolerate short term costs in pursuit of long term gains. They were also rich enough to accommodate, in due course, new members with lower levels of income. The other motives for creating the European union, namely a common desire to prevent future European wars, and a need to unite against the Russian threat, were also clearly not applicable to SACU, which survived despite the deep hostility of the smaller members to the apartheid government in South Africa.

It would seem that SACU survived because it had one dominant member, South Africa, which felt able to provide financial compensation to the smaller members for the disadvantages of the customs union.<sup>14</sup> The most notable disadvantages were the almost complete absence of any policy to encourage new investment in the periphery rather than in South Africa,<sup>15</sup> and the price-raising effect of the common external tariff.

However, the compensation (basically consisting of multiplying the smaller members' share of customs revenue based on their imports by a factor of 1.42) has been calculated to be more than offset by the price-raising effect of the common external tariff.<sup>16</sup> The net effect has been calculated for 1987 as a net loss of 1.24% of Botswana's GDP [Leith, 1992]. Against this,

<sup>12</sup>Note that the SACU Agreement is currently being renegotiated, so that the factors which have given it such a long life may all change. Even so, it will have lasted longer than any other regional trading arrangement in Africa. The future of SACU is further complicated by negotiations between South Africa and the European Union, whose impact on SACU is not currently known. <sup>13</sup>The record of promises made at international meetings about regional cooperation, which have not resulted in any significant action, is considerable. The lack of serious attention in some current regional agreements is demonstrated by some countries belonging to more than one such group, despite their being incompatible. <sup>14</sup>This financial compensation was only provided from 1969, shortly after the three original smaller members had become politically independent; compensation was not provided originally. The Customs Union was created in 1909. The Act which created the Union of South Africa at that time had a clause which said that the three small territories which later became Botswana, Lesotho and Swaziland would eventually be incorporated into South Africa. Fortunately, the Act did not say when, and also required that incorporation should not occur without the consent of the people of each territory. <sup>15</sup>SACU rules allow the smaller members to protect infant industries for a maximum of 8 years, but this has seldom been done, partly because South Africa has used informal pressure to prevent competition with its own industries, and partly because there are anyway inherent disadvantages. These disadvantages were clearly demonstrated by the failure of the only two enterprises protected in Botswana using this rule. <sup>16</sup>The calculations do not take account of the compensation being further eroded, at times of rising imports, by the delay in receiving increased customs union revenue from the common pool.

South Africa is committed to reduce tariffs over a period of years, as a consequence of having joined the World Trade Organisation; this will reduce the price-raising effect of the common external tariff, to the point where, eventually, compensation will be more than the costs. With constant volume and structure of trade, Botswana would have a net gain of about 1.0% of GDP if the average tariff level were to be reduced by 25% [Leith, 1997].

If it is correct that SACU has survived for so long because of compensation from South Africa to the smaller members, then SACU's success would not appear to be replicable elsewhere in Africa. Even an expansion of SACU, to include one or more of the non-SACU members of SADC, would almost certainly not be possible with the same revenue formula applying to new members.

The current intention to convert SADC into a free trade area, with a Trade Protocol signed in 1996, could be just another example of fine-sounding intentions which will not lead anywhere. On the other hand, the majority of SADC countries had a long record of genuine cooperation prior to shifting their objectives to the reduction of trade barriers, which may give it an advantage over some other attempts at regional cooperation. Secondly, most of the member countries of SADC cannot really afford to be excluded from preferential access to the South African market, which is about 80% of SADC's total GDP and is therefore a crucial element in any export strategy which goes beyond the export of primary commodities.<sup>17</sup>

South Africa has large trade surpluses with the other SADC members. These trade surpluses attract a lot of attention. In themselves, they should not be important. It matters little if, for example, Botswana exports mainly to non-regional countries, and imports from South Africa. There is no economic reason for Botswana to be concerned about its bilateral trade deficit with South Africa so long as its overall balance of payments is acceptable. However, those countries which have unsustainable balance of payments deficits tend to concentrate on their trade deficits with South Africa, and to expect preferential access to the South African market in order to improve their overall balance of payments.

This concern with bilateral trading relations with South Africa is increased currently in some SADC members, for example Zambia and Zimbabwe, where unilateral trade liberalisation has resulted in imports from South Africa competing very successfully with domestic production. When domestic manufacturers are closing because they cannot compete with imports, which are mostly from South Africa, trade negotiations acquire a new urgency. It

<sup>17</sup> The problem may lie more with the motivation of South Africa. Whereas a SADC market would be a large increase over the domestic markets of 11 members, it would only increase South Africa's domestic market by 25%, at the cost for South Africa of opening its market to the 11 other SADC members.



has also been argued that South Africa has an interest in importing more from other SADC members, in order to reduce the (mainly illegal) flow of unemployed workers into South Africa; however, even if new trading arrangements could be agreed, any impact on migrant workers would only be effective over a long period.

## 5. Conclusions

If it is correct that the main determinant of Africa's role in the global economy is the relative size of Africa's GDP, then the significance of regional cooperation is the extent to which it will help to reverse economic decline and contribute to rapid rates of economic growth. The record of regional cooperation in Africa is dismal, so that it would not be realistic to expect significant gains from future schemes. Moreover, if regional markets surround themselves with high protective barriers, regional cooperation could make things worse rather than better by protecting inefficient industry incapable of competing in global markets.

Southern Africa may be an exception to this pessimistic view of the success of regional cooperation, because South Africa's neighbouring countries need access for their exports to South Africa's much larger market. Much more important, though, is that the economy of South Africa grow faster than in recent years.<sup>18</sup> There may be some point in converging on a richer economy for economies whose income per head is a small fraction of the target economy. But convergence loses its attractions as convergence nears completion, as is the case to some extent already,<sup>19</sup> and if the target economy is not growing.

Clearly, South Africa needs to converge on more advanced economies, which requires that its economy be opened up to the rest of the world. This is already happening. South Africa is in the process of lowering the common external tariff of SACU as part of its obligations to WTO. This will reduce the benefits for SACU members of preferential access to the South African market, and would reduce the potential benefits for the other members of SADC in a regional trading arrangement. Regional economies would be much better off, however, with lower preferences but rapid growth in the region's largest economy, than with more privileged access to a stagnant economy.

<sup>18</sup> GDP in South Africa grew at only 1.3% per year from 1980 to 1990, and fell by 0.1% per year from 1990 to 1994 [World Bank, 1996]. There are some indications that growth has resumed since 1994. <sup>19</sup> In 1994, GNP per head (at Purchasing Power Parity) in Botswana was 102% of South Africa's, with Namibia 84%, Swaziland 59% and Lesotho 34% [World Bank, 1996]. In 1966, GNP per head as a percentage of South Africa's was Botswana 18%, Swaziland 29% and Lesotho 12% (no statistics available for Namibia) IMF- 19921.

The underlying point is that openness to the global economy is fundamentally more important to Africa than the benefits which or may not arise from regional integration of trade. Other forms of regional cooperation remain important, but that is the subject of another paper.

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# BIDPA Publications

## Working Paper Series

### BIDPA Working paper 1

Granberg, Per

*A Note Concerning the Revision or rebuilding of the MEMBOT Model. Some Preliminary Observations and Suggestions.* BIDPA, 1996. RESTRICTED.

The paper discusses the structure of the existing MEMBOT model (Macroeconomic model for Botswana). The limitations of the current model are identified and a need to revise it is noted.

### BIDPA Working Paper 2

Granberg, Per

*A Study of the Potential Economic Effects of AIDS. Some Preliminary Thoughts.* BIDPA, 1996.

Given the current rate of HIV/AIDS infection in Botswana, there seems a need to analyse its economic impact. It is suggested that BIDPA may take an initiative towards this end. The paper presents some preliminary and tentative ideas about such a project.

### BIDPA Working paper 3

Duncan, Tyrrell (ed.)

*Study on Poverty Alleviation in Botswana: Inception report.* BIDPA, 1996

This inception report sets out the various steps planned in completing the study, which comprises a statistical review of poverty utilising the 1985/86 and 1993/94 Household Income and Expenditure Survey. The study will focus six special areas: Basic Education, Preventative Health, Labour Based Public Works, Destitute Policy, Financial Assistance Policy and Arable Lands Development Programme.

### BIDPA Working Paper 4

Isaksen, Jan.

*Main Ingredients for a Public - Private Sector Strategy for Private Sector Employment Creation in Botswana: Prepared for the Fourth Private Sector Conference on Employment Creation, Francistown 26 - 28 May 1996.*

The paper attempts to draw lessons from policy experiences in Eastern Asia. On the basis of such lessons, the paper suggests a number of practical policy steps which hopefully would be relevant to the policy debate in Botswana. It argues that a resumption of rapid economic growth through diversification and industrialisation are the most important contributions to the acceleration of employment creation in Botswana.

### BIDPA Working Paper 5

Granberg, Per.

*A Revised Poverty Datum Line for Botswana.* BIDPA, June, 1996

The paper is part of a larger study of poverty and poverty alleviation in Botswana, undertaken by BIDPA for the Ministry of Finance and Development Planning. The paper presents revised estimates of the Poverty Datum Line (PDL) for Botswana, needed to analyse the household income and expenditure survey for 1993/94 and 1985/86 in terms of poverty.

### BIDPA Working Paper 6

Gergis, Abdalla.

*Regulation, Privatisation and Commitment in Botswana: Paper presented at BNPC's First Stakeholder Consultative Conference on Productivity: Productivity - Key to the future, November 6, 1996.*

The paper notes the challenge facing Botswana, giving particular attention to the changing role of the state and the need to adjust the regulatory environment. Recent economic developments in Botswana are discussed, as are the questions of international competitiveness and the search for a new engine of growth for the economy.

## **BIDPA Working Paper 7**

Fidzani, N.H., P. Makepe and J. Tlhalefang

*The impact of trade liberalisation on Botswana's beef and maize sectors.* BIDPA 1997

The paper examines the Botswana beef and maize sectors in terms of structure, main activities and market distortions. The origins and sources of these distortions are analysed to determine how their removal would bear upon the various stakeholders. The paper also attempts to sketch implications of regional integration.

## **BIDPA Working Paper 8**

Isaksen, Jan.

*Data Requirements and Methodologies for Multi-country Research.*

The paper was presented at a workshop on developing a research agenda for accelerated development in Sub-Saharan Africa held in Harare, Zimbabwe, March 1997. It presents data and methodology for co-operation at national, regional and continental levels in research. It concludes that there is need for international co-operation build on national priority research.

## **BIDPA Working Paper 9**

Gergis, Abdalla

*"To Privatised", What is & How? Paper presented at seminar on "Competition, Productivity and Privatisation: Commonwealth Experiences and for Botswana" organised by BIDPA and BNPC under the sponsorship of the Commonwealth Secretariat, Gaborone 21-23 April, 1997* BIDPA, 1997

The paper was presented at a seminar on Competition, Productivity and Privatisation. It draws on lessons of experience as well as existing knowledge about privatisation, briefly addressing the main issues discussing how privatisation can be planned and implemented successfully.

## **BIDPA Working Paper 10**

Greener, Robert

*The Impact of HIV/AIDS and options for intervention: results of a five -company pilot study.*

BIDPA, 1997

The paper was written for the Botswana National Task Force on AIDS at the workplace. It presents results from a study of the impact of HIV/AIDS, based on a sample of five companies in Botswana. It concludes that the impact to date has been small, because the HIV epidemic is still too recent to have developed into an AIDS epidemic.

## **BIDPA Working Paper 11**

Harvey, Charles.

*The role of Africa in the global Economy: the contribution of regional co-operation, with particular reference to Southern Africa.* BIDPA' 1997

The paper was written at the request of the Vice President and Minister of Finance and Development Planning. The paper notes that Africa's importance in the world economy has declined over the years and argues that this, and the extreme poverty in most of Africa, calls for analysis of ways to reverse the trend. Prospects for regional co-operation and integration are discussed as possible ways to accelerate economic growth in Southern Africa.

## **BIDPA Working Paper 12**

Ditlhong, Molapisi.

*Poverty Assessment and Poverty Alleviation in Botswana* BIDPA 1997

The paper discusses the nature and extent of poverty in Botswana, drawing data from the Study of poverty and poverty alleviation in Botswana conducted by BIDPA for Ministry of Finance and Development Planning.

## **BIDPA Working Paper 13**

Gergis, Abdalla

*Competition, Productivity and Privatisation.* BIDPA 1997.

A summary report of the proceedings of the Seminar on Competition, Productivity and Privatisation.

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*Competition, Productivity and Privatisation.* BIDPA 1997.

A summary report of the proceedings of the Seminar on Competition, Productivity and Privatisation.

## BIDPA working paper No. 14

Lisenda, Lisenda

*Small and Medium-Scale Enterprises in Botswana: Their Characteristics, Sources of finance and Problem* BIDPA, December 1997.

The study analyses the characteristics of Small and Medium-Scale Enterprises (SMEs) in Botswana highlighting the educational background of owners and exposure to business related training, geographic location of enterprises, premises of operation, age of enterprise, and size of enterprise by number of employees, sales and total investment and activity. Also considered are administration and financial sources of the enterprises. Record keeping is assessed by size of enterprise, gender of operator and source of finance of enterprise. Problems faced by SMEs are highlighted.

## BIDPA Working Paper No. 15

Granberg, Per.

*A simple formula for forecasting the Botswana urban population total.* BIDPA, February 1998

The paper establishes a simple relationship between urbanisation and economic growth. The relationship is intended as a simple "annex" to the revised MEMBOT model (forthcoming), capable of providing quantitative estimates illustrating the likely nature of urban population changes under alternative economic scenarios.

## BIDPA Working Paper No. 16

Sesinyi, Magdeline.

*Minimum wages and employment: literature review and background on minimum wages in Botswana.* BIDPA, 1998.

Gives a brief literature review on minimum wages and their possible effects on employment, with particular focus on the likely effects of minimum wage introduction on the two excluded sectors, namely the Domestic and Agricultural Sectors. It briefly outlines research results on minimum wages from past studies, highlighting their main recommendations. The paper concludes that minimum wage increases results in trade-off, and no matter how well intended come with a price in the form of lost jobs for some and increased benefits for others.

## BIDPA Working Paper No. 17

Jefferis, Keith, Charles Okeahalam and Tebogo Matome

*International Stock Market Linkages in Southern Africa.* BIDPA, 1999

Stock markets are taking on an increasingly prominent role in financial development, and many developing and transition economies are establishing stock markets as part of financial reform processes. In theory stock markets can contribute to the mobilisation of savings and the allocation of investment, but there are questions as to whether this works in practice. One important issue is whether stock markets are efficient (in the financial sense), and a related question is whether share prices reflect economic fundamentals; both of these questions are important in addressing whether stock markets properly allocate capital. Another issue relates to the question of international linkages between markets: with greater integration of capital markets globally, financial market developments appear to be rapidly transmitted between markets around the world. While this can have beneficial impacts, in terms of improving the global allocation and pricing of capital, it may be disruptive if international capital flows are large relative to national markets and economies. This paper addresses pertinent issues in the context of stock markets in three southern African countries: Botswana, Zimbabwe and South Africa.

## BIDPA Working Paper No. 18

Dumcombe, Richard

*The Role of Information and Communication Technology in Small and Medium Enterprise Development in Botswana.* BIDPA, October 1998

The paper analyses the role of information and communication technologies (ICTs) in small and medium enterprise (SME) development in Botswana. It outlines the economic and policy background to SME development, and presents an analysis of the SME sector with regard to firm size, location and market sector. It presents the results of a pilot survey of firms in the SME sector examining the information and communication practices of a small sample of firms. Current developments in information and communication technologies are outlined, and some preliminary findings relating to ICT impact on SMEs are summarised. Finally, some policy considerations are mentioned and the objectives of the main fieldwork phase of the project are outlined

By Harvey, Charles

*The impact on Southern Africa of the financial crises in Asia and Russia* BIDPA, June 1999

The countries of southern Africa have not suffered seriously from "financial contagion", which is the short-term and sometimes devastating impact of financial crises in other countries. The first stage of financial contagion occurs through the markets for foreign exchange, shares and bonds. The second stage, which can be even more devastating, occurs if trouble in financial markets causes a crisis in the country's banking system, as happened in several Asian countries. South Africa's economy is potentially the most vulnerable in Southern Africa to financial contagion, because it has highly developed financial markets which are open to inflows and outflows of foreign capital. However, the economic cost of financial contagion has been limited in South Africa because the country's banking system is sound. Zimbabwe has been similarly protected from the worst effects of financial contagion. Financial markets in the other countries of Southern Africa are very underdeveloped, which limits the first stage of financial contagion; this is fortunate, because some of them have unsound banking systems. All of these countries are actively trying to develop their financial sectors, however, so that their relative immunity to financial contagion may be reduced in the future. This will strengthen the case for maintaining macroeconomic balance, realistic exchange rates, and absolutely sound banking systems.

### BIDPA Working paper 20

Jeferris, Keith *The Long Term Impact of Structural Economic Change on Government Spending*. BIDPA, June 1999

Botswana's current economic objectives centre on diversification away from its historical dependence on diamonds and government. Such diversification will change the structure of the economy, and has important implications for the ability of government to raise revenue through taxation and therefore for its ability to finance its expenditure. This paper explores the likely impact of diversification on government's revenue raising ability and hence on the magnitude of its overall role in the economy. It uses projections over a 20-year period to simulate possible scenarios for taxation and the size of government. The key point is that any diversification will cause government revenues to fall, in relative terms. The diamond sector is extremely profitable, and those profits are taxed at a very high rate; as the economy diversifies, other sectors will emerge that will be less profitable and less highly taxed. The projections in this paper show that under a variety of different assumptions about sectoral growth rates, and taxation and spending, government will have to significantly reduce its role in the economy. Such a change will have major implications for choices to be made about the allocation of public expenditure.

### Publications Series

1. Gaolathe, Ndaba "Botswana's booms and recession experience: a discussion" IN: Salkin J.S., D. Mpabanga, D. Cowan, J. Selwe, M. Wright (eds.) *Aspects of the Botswana Economy*. Gaborone: Lentswe La Lesedi, 1997 pp: 37 - S2.

In the years around 1990, the Botswana economy experienced a period of "boom" conditions, eventually followed by a "burst". The paper sets out to analyse this experience, trying to explain the underlying factors, and to draw out policy lessons.

2. Gergis, Abdalla (ed.)

*Botswana's New Industrial Development Policy BIDPA/MCI*. Gaborone: Government Printer, 1997.

The publication contains the proceedings of the joint BIDPA/MCI seminar held in September 1996. The volume includes the seminar report on group discussions of the draft industrial development policy and the background papers presented by speakers at the seminar. The report summarises the issues raised during the two days of discussions.

3. Gergis, Abdalla (ed.)

*Prospects of EU/MCP relationship with particular reference to Botswana: Conference held at the Grand Palm Hotel, Gaborone 25 - 26 September 1997: Conference highlights* Gaborone: Government Printer 1998.

This document presents highlights of the conference and of papers presented by speakers. The report captures the essence of the debate on the future of Lomé Convention and highlights main issues that emerged from the consultation process.



#### 4. Granberg, Per.

***Exchange rate, inflation and competitive: an analysis of the relationship between Botswana's Exchange and Inflation Rates and its implication for the competitive strength of her producers***

The publication contains findings of the project: Study of Botswana's exchange rate policy. The publication details simple input/output based model for analysing the exchange rate question, and employs it to draw out the implications for various sectors of the economy, under alternative exchange rate scenarios. It goes on to analyse the available statistical evidence, and draw comparison to model results. Finally, it discusses the rationale, and possible revision, of the current exchange rate policy for a broader perspective with special reference to the likely implications of following a significantly different policy.

### Serials

#### ***1. BIDPA Briefing***

A quarterly newsletter, with topical supplements, that provides regular comment and analysis on all aspects of Botswana economy.

#### ***2. The BIDPA Newsletter***

A quarterly newsletter reporting on events, projects and general activities of the Botswana Institute for Development Policy Analysis (BIDPA).

