



Obstacles and Progress at Regional Integration: A REC Perspective

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Panel: Integrating Africa to Propel Inclusive Growth

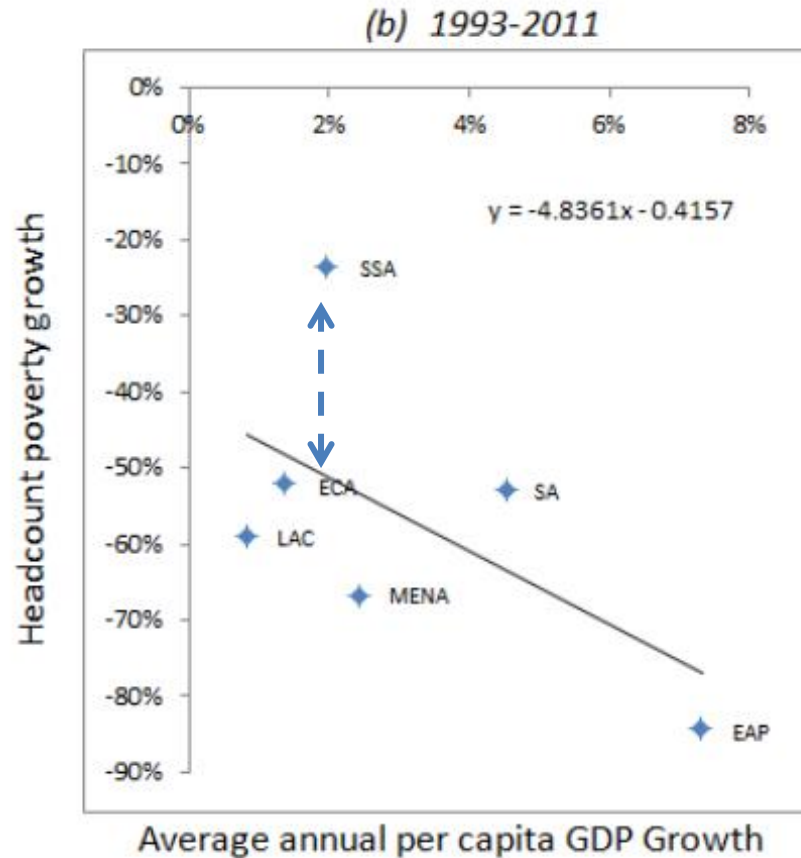
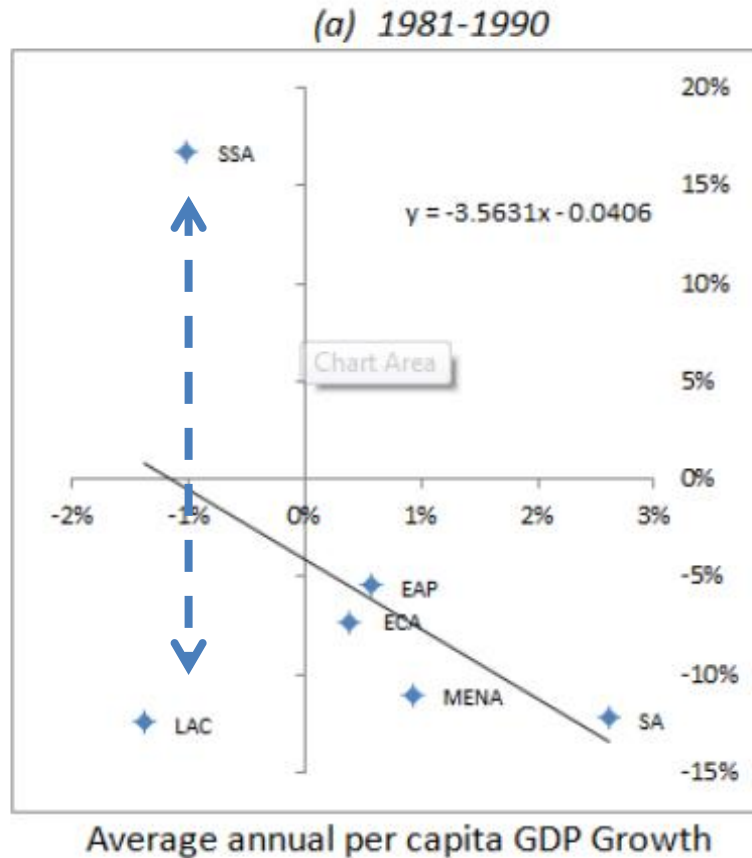
WTO Forum, 2016

Outline

- SSA Growth less inclusive than in other regions
- Implications of heterogeneity
- Genetic Diversity a correlate of bilateral trade
- Design: Breadth vs. depth
- Trade costs remain high across RECs...
- ...Few new products in manufactures all to regional destinations
- New products need Domestic Institutions
- A Services-led industrialization?
- Challenges Ahead

SSA Growth Less inclusive

Change in Head Count Ratio (HCR) vs growth (by region, by decade)



Notes: Headcount poverty growth and average annual per capita GDP growth. Regional averages over 1981- 1990 and 1993-2011. The sample is composed of 101 developing countries, including 43 SSA countries. GDP growth rates are weighted by country population size. Poverty line at \$1.25 per day, PPP. Source: Authors' estimations based on PovcalNet and WDI.

HCR elast. by sector (1993-2011) : Agr.(-0.40); Ind.(-1.1) ; Services (-0.71)

Overview

- RECs: Good politics (Martin, Mayer, Thoenig)
- Recent surveys (Melo/Tsikata: Critique of Linear integration model; Newfarmer: need to extend Regional cooperation beyond goods trade)

Narrative:

- Growth in SSA has lacked inclusivity. Why?
- Obstacles (1): 'Roots' (biological & cultural). Low Trust
- Obstacles (2): 'Domestic Institutions' . More important than endowments/ technology for new activities
- Progress (1): Move towards deeper integration
- Progress (2): Trade costs falling in RECs but still high
- Progress (3): Services

Implications of heterogeneity (1)

- Dispersion (size, resources endowments, geography):
 - Agglomeration (core-periphery) → compensation
 - Coastal-Landlocked → Gain towards Landlocked
- Per capita income dispersion (Venables 2003):
 - Kenya (K), Uganda (U) both below average world K/L
→ FTA: gains for K, loss for U → compensation for (U)
 - Portugal (P) and Germany (G) both above average K/L
→ FTA: gains to (P) country closest to mean
- Heterogeneity implementation conundrum (Melo-Tsikata): Potential gains large but require greater compromise and hence intense policy coordination via delegation of authority to supranational body.

Implications of heterogeneity (2)

- Trust important for trade. Strong Intergeneration transmission of biological and cultural traits (Spolaore/Wacziarg)
 - Measures of genetic diversity trump other factors in cross-country correlations of differences in per capita GDP
 - Bilateral Genetic Distance (GD) as proxy for Trust. GD correlates negatively with intensity of bilateral trade (see next slide)

Genetic Diversity correlates with bilateral in manufactures

VARIABLES	(1) Manufacture	(2) Manufacture	(3) Manufacture	(4) Manufacture	(5) Manufacture	(6) Total
ln_dist	-0.740*** (0.0546)	-1.667*** (0.0371)	-1.574*** (0.0403)	-1.570*** (0.0403)	-1.570*** (0.0403)	-1.626*** (0.0422)
comlang_off	-0.457*** (0.122)	1.070*** (0.0771)	1.047*** (0.0767)	1.041*** (0.0767)	1.041*** (0.0767)	0.993*** (0.0753)
fst_distance_weighted	-16.22*** (0.685)	-5.068*** (0.501)	-5.155*** (0.498)	-5.202*** (0.497)	-5.202*** (0.497)	-1.716*** (0.502)
PTA			0.416*** (0.0667)	0.396*** (0.0664)	0.396*** (0.0664)	0.565*** (0.0665)
WTO				1.173*** (0.270)	1.173*** (0.270)	0.901*** (0.260)
Constant	22.02*** (0.445)					
Observations	9,602	9,600	9,545	9,545	9,545	10,145
R-squared	0.110	0.780	0.783	0.784	0.784	0.751
importer	no	yes	yes	yes	yes	yes
exporter	no	yes	yes	yes	yes	yes
bilateral	no	no	no	no	no	no

Robust standard errors in parentheses

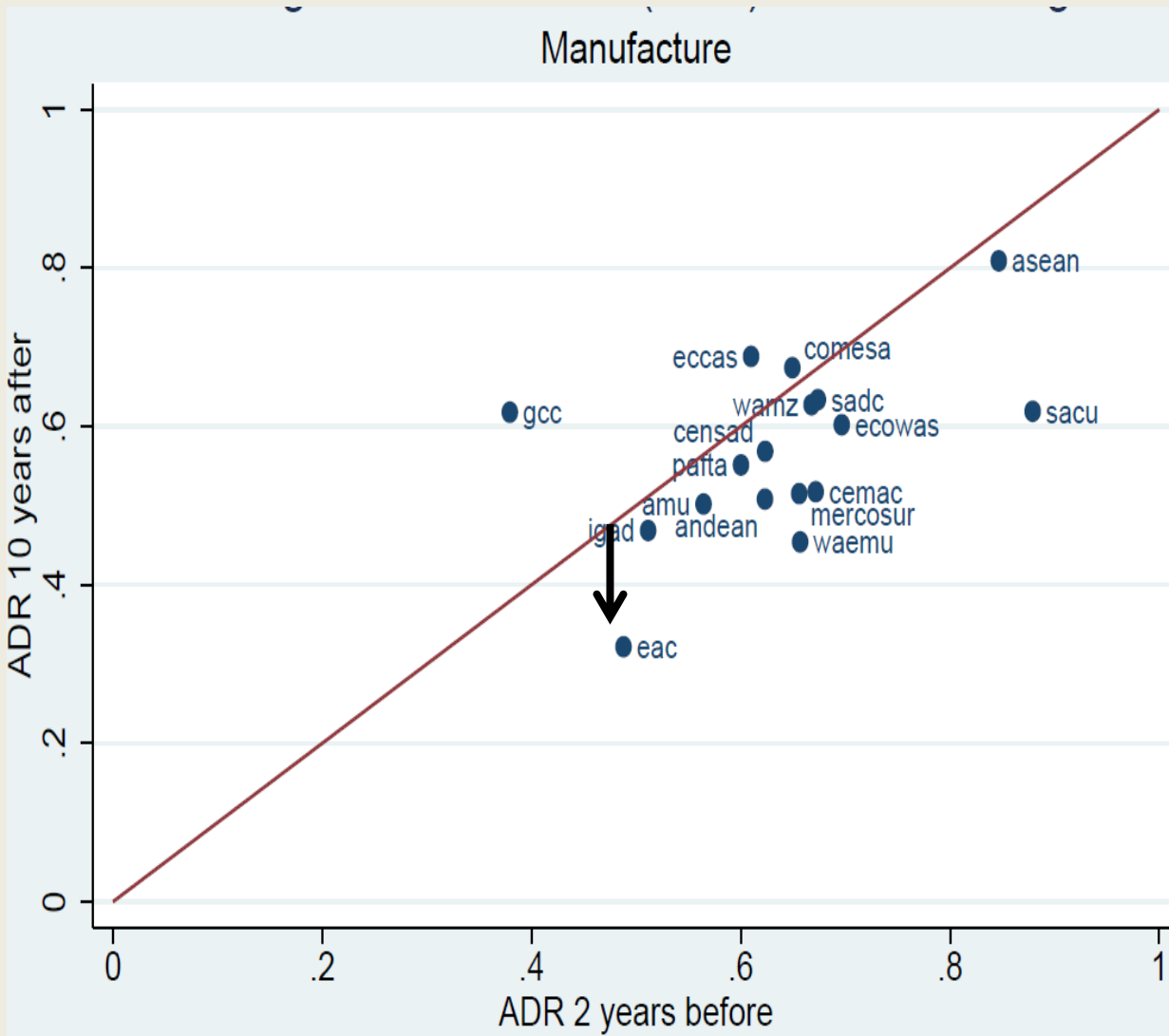
*** p<0.01, ** p<0.05, * p<0.1

Design: Breadth vs. Depth

- Narrow: EAC (Rwanda-Kenya) vs wide: ECOWAS (Liberia-Nigeria). TFTA (28 members)
- Count of LE provisions by depth (WTO+ and WTO-X(LE) provisions): SSA vs- other S/S (Melo-Nouar)

WTO +	COMESA/ECOWAS/ SADC	Other S/S (18)
Trade-related (6)	0.94	0.79
Investment-related/GATS/TRIPs (4)	0.56	0.31
Domestic trade-related (SPS, TBT, etc.)(5)	0.40	0.34
WTO-X		
Capital and labour (7)	0.33	0.20
Domestic trade-related (environment, competition, etc.) (5)	0.80	0.16
Others (audiovisual, cultural, cooperation, etc.) (25)	0.27	0.09

Trade Costs remain high (intensive margin)...



$$ADR = ADOT / ADOTP$$

Average Distance Ratio (ADR). Average Distance of Trade (ADOT) divided by frictionless Average Distance Of Trade Potential (ADOTP)

Below 45° suggests that trade costs have fallen more rapidly within REC relative to outside REC

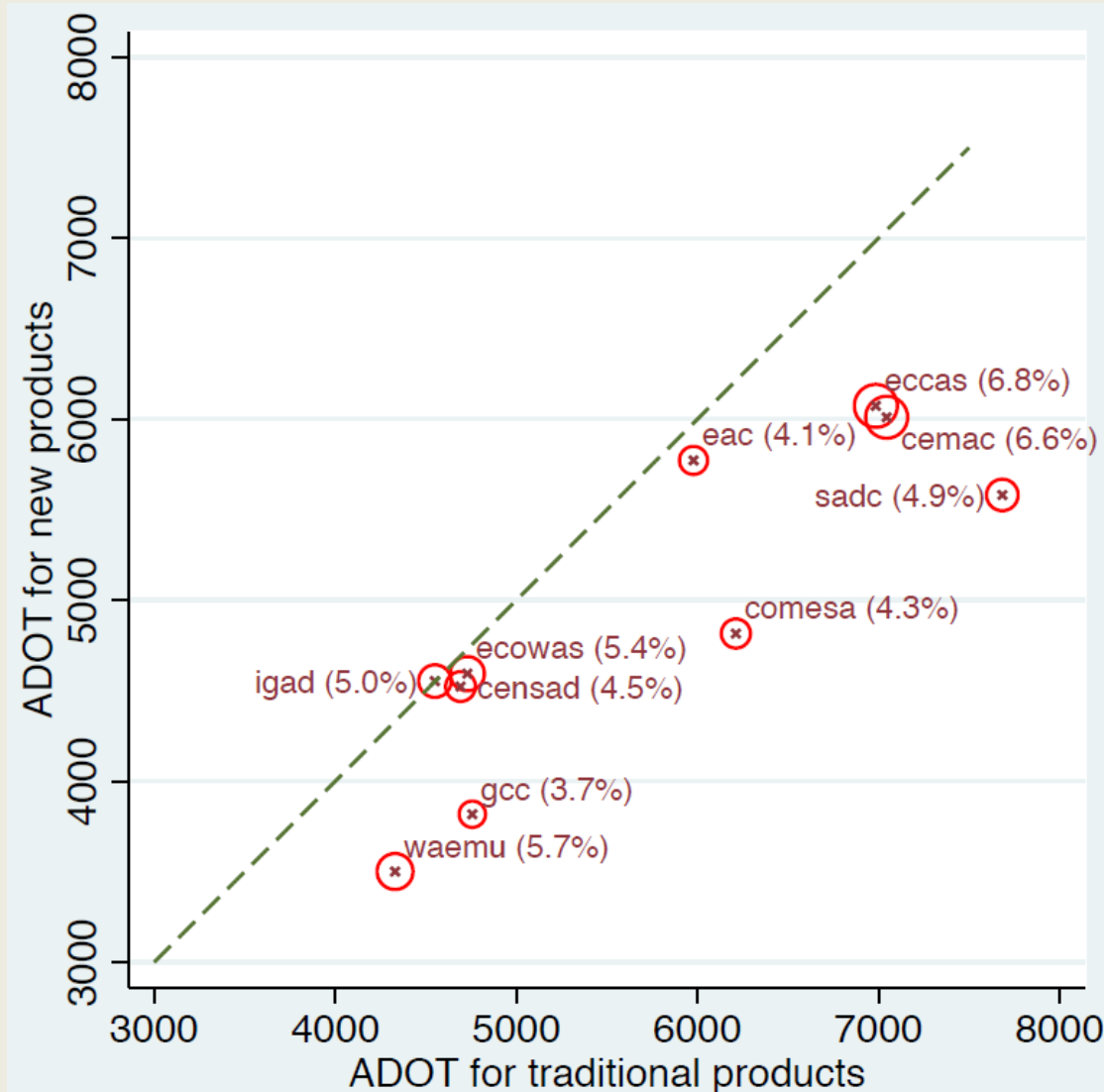
See extra slides

...and few new products mostly destined regionally

New products (manufactures at HS4 level) must be exported for at least 3 consecutive years.

(ADOT) for manufactures (HS-4 level) 2000-08 (Average over all REC members) vs. ADOT of traditional products (1995-00)

Figure in parenthesis is average percentage number of new products over period.



New products need Domestic Institutions

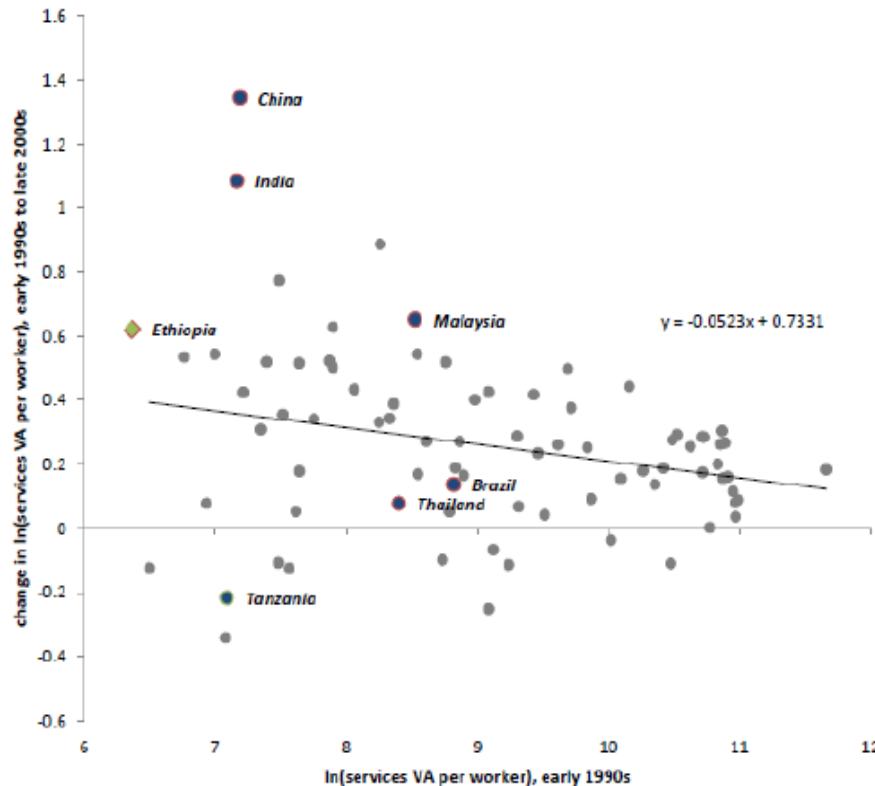
- Comparative Advantage (CA) moves towards more sophisticated and productivity-enhancing goods (Hausman et al. 2007).
- Conditioning on technology, countries with strong Institutions (as proxied by different measures of product, financial and labor mkts. have CA in contract-intensive manufactures
- RCA index often more sensitive to index of domestic institutions than traditional measures of CA (Nunn and Trefler (2015). A factor explaining low number of new manufactures?

A Services-led Industrialisation?

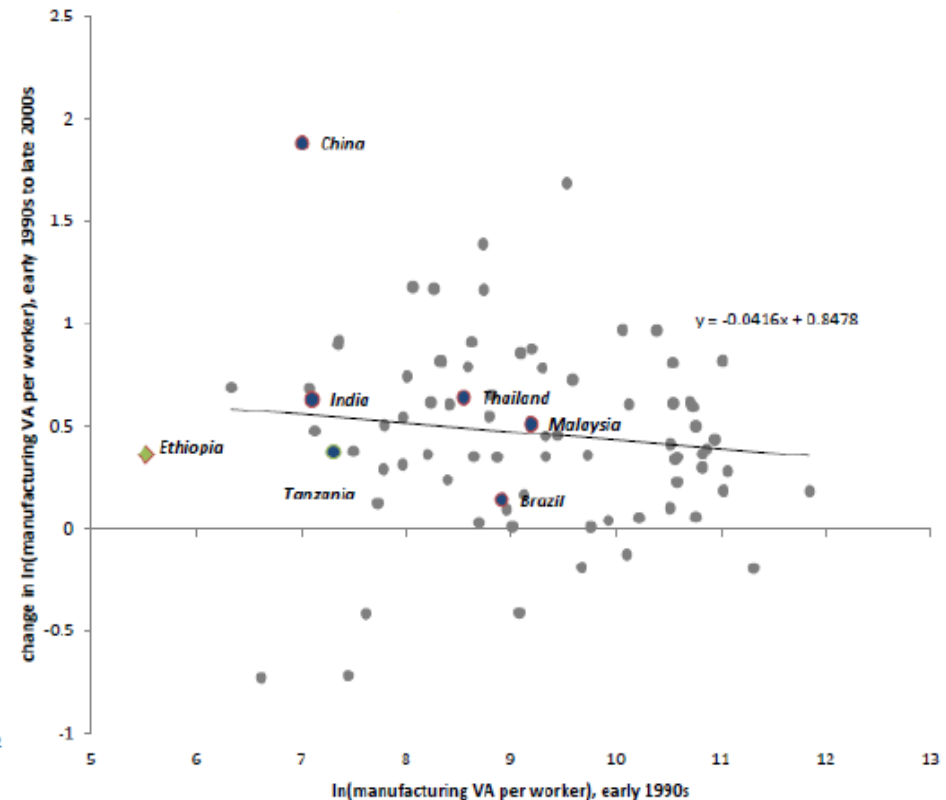
- Linear model of integration across RECs has overlooked gains from liberalization of services within RECs
 - Dihel-Grover (2016). All services are becoming tradable and services trade is booming, yet Africa only accounts for 2% of world Trade in Services.
 - Services sectors have higher labour-productivity growth across 100 countries than manufactures and provide more jobs at early phase of industrialisation (next slide).
- ⇒ Services is a contributor to more inclusive trade-led growth across SSA (higher HCR elasticity than ag.)

Unconditional convergence in Services

(a) Convergence in services productivity



(b) Convergence in manufacturing productivity



Notes: Labor productivity is calculated by the ratio of total sector value-added to total employment in sector. Underlying accounts are in 2005 constant international USD. Values taken from earliest year available from 1990-1993 and latest year available from 2005-2009. Overall conclusions do not change if line is quadratic or cubic in ln(initial VA per worker).

Source: Ghani and O'Connell (2014).

Challenges Ahead

- Gains greatest (economic heterogeneity) where political-economy is most adverse (cultural/compensation).
- Indirect measures of intra-regional trade cost measures still high and few new products: importance of domestic institutions.
- TFTA (breadth rather than depth). Negotiations stumbled in June on SI list (EAC products would have access to SA market).
- Services : higher HCR elasticity to growth and are key inputs for manufacturing, attracting FDI

Extra slides

Some References

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- NUNN, N. and D. Trefler (2015). “Domestic Institutions as a Source of Comparative Advantage”, chp. 5 in Gopinath et al. eds. *Handbook of International Economics*.
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Gravity-inspired Trade Cost Estimates

$$X_{od} = \frac{Y_o Y_d}{Y_W} \phi_{od} ; Y_W = Y_o + Y_d ; \phi_{od} < 1 \quad o = \text{origin}, d = \text{destination}$$

- Costs estimates approximated by average distance ratio
– ADR = (average distance of trade ADOT) / (average potential (i.e. GDP determined) distance of trade ADOTP)
 - $ADOTP = \frac{Y_o Y_d}{Y_W} ; Y_W = Y_o + Y_d$
 - If ADOTP unchanged by RTA \rightarrow ADR \downarrow if ADOT \downarrow a reflection that reduction in regional trade costs greater than reduction for extra regional (for existing partners, i.e. intensive margin)
- Scatter (average of 2 years before and 10 years after): If ADR \downarrow (scatter below 45° line) then relative costs of trading regionally have fallen more rapidly. Case for EAC, WAEMU, MERCOSUR.