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Exchange Rate-Based Stabilization in War-Ravaged Economies: The Case of Lebanon

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Abstract

This article examines exchange rate-based stabilization in an economy that has been badly destroyed by war or other calamities. The article does this in the context of post-civil war Lebanon. Both Iraq and Afghanistan are prime candidates for such a policy. This article first demonstrates the validity of the theory and empirical regularities (initial boom followed by an economic contraction) in the case of Lebanon and argues for the suitability of such programs for war-ravaged economies. It then empirically highlights the role played by the credibility of policy makers in the success or failure of the program and the resulting dynamics of economic variables. The article concludes that the success depends on a political environment that engenders credible policy.

JEL Classification Codes*:* E63, F41, O24, O53

* I would like to thank Jeff Nugent and Selo Imrohoroglu for helpful comments on an earlier version of this article.

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1 Introduction

This article is concerned with exchange rate-based stabilization programs in developing countries. In particular, the focus is on the experience of post-civil war Lebanon (a) to discuss the effectiveness of exchange rate-based stabilizations in economies with destroyed infrastructure, (b) to compare the observations with empirical regularities associated with exchange rate-based stabilizations in general, and (c) to highlight results that might be of interest to countries in similar situations faced with choosing between different stabilization policies. The stabilization program embarked upon by Lebanon following the end of its bloody civil war took a toll on its economic and social infrastructure and aggravated its problems. The experience could prove relevant in the present global environment where several countries, for example, Iraq and Afghanistan, face the challenge of putting their economies on the road to stable and sustainable growth. However, it is useful to emphasize that the focus here is specifically on the Lebanese experience and that generalizations to other cases need to be handled with caution.

Bringing inflation under control will have to be an important target of any policy designed to meet the challenge of stabilization, as there is strong consensus in the economics profession that high inflation is harmful for the growth of economic capacity. High rates of inflation have been a persistent problem in developing countries. Latin American countries have been infamous for their excessively high levels of inflation and have therefore been the focus of studies that have analyzed policies and programs that have been implemented to address this issue. Inflation rates of over 10 percent and even periods with sustained inflation over 25 percent have not been uncommon. While many countries (mostly in South America) have experienced what is now commonly labeled as "chronic" high inflation (Pazos, 1972), several other developing countries have suffered from high inflation associated with large changes in terms of trade and political instability. This phenomenon has been present in Africa and Asia and even in some developed countries like Iceland (Fischer, 1988).

Various approaches have been used in attempting to stabilize high inflation. While numerous countries have tackled the problem using the so-called *populist* programs that entail direct intervention in the wage-price process, others have relied on more *orthodox* policies that attempt to get the fundamentals right. Such policies have involved using money and exchange rates to achieve their objectives. In fact, a combination of the two aforementioned approaches known as *heterodox* policies have also been employed.

Both the populist and heterodox programs are premised, at least in part, on the assumption that the economy possesses a substantial amount of unutilized productive capacity. This assumption, however, is likely to be violated in the case of war-ravaged economies that usually have severely damaged infrastructure. The choice from among the two orthodox policies largely rests upon the kind of after-effects that appear more compatible with the path the policymakers prefer to take to stabilization. While the beginning of exchange rate-based stabilizations are characterized by economic booms and sustained real appreciations, contractions take hold toward the end and beyond. In contrast, evidence suggests that a recession is more likely toward the start of money-based stabilizations. This implies that the choice between the two programs depends upon when the country is willing to bear the costs of disinflation in terms of output losses (Calvo and Vegh, 1999). For developing countries emerging from debilitating wars, exchange rate-based stabilization would hold special appeal stemming from the need to rebuild and rehabilitate and expand economic activity quickly. In fact, exchange rate-based stabilization was the program of choice of the Lebanese government after the end of its civil war in the early 1990s. Comparing the results obtained from the Lebanese experiment to theoretical predictions and empirical observations from experiences of other countries with economic disturbances should therefore help us shed more light on the peculiar case of Lebanon.

The next section discusses the theory and empirical evidence of exchange rate-based stabilization programs followed by a section that analyses the Lebanese program in particular. The article subsequently discusses and examines the role policy credibility as manifested in the political leadership plays in Lebanon in generating the results we observe. The article concludes with lessons for such countries culled from the Lebanese case.

2 Exchange-Rate Based Stabilization: Background

2.1 The Theory

As stated earlier, the two main approaches to stabilization utilized by developing countries suffering from high inflation are money- and exchange rate-based. Given the evidence lending support to the view that money-based stabilization leads to a recession taking place at the beginning of the program (Calvo and Vegh, 1994a) and that exchange rate-based stabilization causes an initial boom and an eventual contraction (Kiguel and Liviatan, 1992; Vegh, 1992), the choice between the two nominal anchors really translates into a choice between bearing the costs of disinflation, in terms of output, "now" versus "later". Clearly, countries that are emerging from the devastation of war and are attempting to stabilize their economies in order to make the economic environment more conducive to subsequent sustained growth have a straightforward choice to make. Since the need for rehabilitation is immediate and pressing under these circumstances, a policy that is likely to cause a recession soon after implementation can be reasonably expected to have lesser appeal than others.

Preference to delay a contraction in an economy with an urgent need to rebuild is not the only reason for choosing the exchange rate as the policy instrument. Exchange rate regimes also allow the authorities to do away with the requirement to have information about money demand or velocity, which are crucial when a monetary anchor is being used and which are also quite difficult to predict in the transition from high to low inflation. Another related issue is that prolonged periods of high inflation often contribute to creating highly dollarised economies.[1] This leads to a situation where the relevant money supply includes foreign currency holdings and deposits and this component is not controlled by domestic policymakers. Therefore, a contraction in domestic money supply is not likely to have a significant effect on liquidity or inflation in countries that are plagued by violence, upheaval, and social instability.

Finally, since the exchange rate is a price as opposed to a quantity, it serves as a much clearer signal to the public of not only what the government intends to do but also what it is actually doing. This, in turn, influences the public's inflationary expectations by giving it an anchor that can be continuously monitored and hence makes the government more credible. All of these considerations make reliance on the exchange rate as opposed to a monetary aggregate more attractive and this is precisely the choice that was made by the Lebanese policymakers following the end of civil war.

A variety of analytical models have attempted to explain the boom-recession cycle in exchange rate-based stabilization programs. One key feature of these models has been their emphasis on the dynamic effects of imperfectly credible policy, which is a consequence of varying expectations about present and future government policies. The main explanations have been put forward by Rodriguez (1982), and Calvo and Vegh (1993a, 1993b).

Rodriguez bases his model on a small open economy where the exchange rate path is pre-announced, the money supply is endogenous, expectations follow a backward-looking process, and capital is perfectly mobile internationally. For given levels of the real interest rate and the real exchange rate, this model determines the inflation rate. In the steady-state equilibrium, the model implies that the domestic real interest rate must be equal to the world interest rate and the long-run inflation rate is equal to the devaluation rate. Backward-looking expectations serve the purpose of generating the observed short-run boom in this model. The initial reduction in the devaluation rate leads to a fall in the nominal interest rate and a downward jump in the real interest rate. This in turn

[1] Dollarisation refers to a situation where domestic currency is substituted for a foreign currency (in most cases, the US dollar) as a unit of account, store of value, and medium of exchange.

leads to an increase in demand for non-traded goods. The contraction in demand results from the appreciation of the real exchange rate that is caused by the upward pressure on domestic prices due to the initial increase in demand for home goods. The explanation provided by this model relies on an arbitrary specification of behavioral functions and expectations formation. However, this formulation with its focus on a backward-looking expectations process appears untenable in the context of war-ravaged economies that are undergoing comprehensive macroeconomic adjustment programs since history in this instance does not serve well the role of providing usable expectations. In addition, Calvo and Vegh (1994b) have argued that the existence of backward-looking expectations may not even be sufficient to explain the initial expansion in output following the implementation of an exchange rate-based stabilization program.

To counter these shortcomings, Calvo and Vegh (1993a, 1993b) provide an explanation based on forward-looking expectations instead. They consider a small open economy that produces traded and non-traded goods. The representative household maximizes the discounted lifetime sum of utility subject to a cash-in-advance constraint and a lifetime resource constraint. Output in the non-traded goods sector is determined by demand. Inflation in this sector is assumed to be negatively related to excess demand, which is defined as the difference between actual output and its long-run level. The price mechanism works on the assumption that firms in the non-traded goods sector determine the prices of their products in an unsynchronized manner, taking the average price prevailing in the economy and the future path of demand into account. Although the price is therefore predetermined at any given period, inflation can jump since it conveys individual prices set by firms. For example, some firms increase their prices when excess demand increases in the non-traded goods sector, which leads to a rise in inflation. Over time, however, this inflation falls since the number of firms that are yet to adjust their prices to the change in excess demand goes down. This implies an inverse relationship between the change in inflation rate and excess demand in the non-traded goods sector. Due to this formulation of prices, the real exchange rate is predetermined in the short run. Finally, the overall inflation rate is written as a weighted average of the devaluation rate and the rate of inflation in home goods prices. The formulation asserts that, for the real exchange rate to remain constant over time, the rate of inflation in home goods prices must be equal to the devaluation rate. Also, for the inflation rate in the non-traded goods sector to remain constant, the consumption of home goods must be equal to the long run output.

Calvo and Vegh use this framework to emphasize the role of credibility in exchange rate-based stabilizations. The authors identify two distinct cases. The first is an economy with full credibility while the other has imperfect credibility. Under full credibility, an announcement by the government of an immediate and permanent reduction in the rate of devaluation convinces private agents of the commitment of the government to indeed keep the devaluation rate low in the indefinite future. This lower devaluation rate causes the nominal interest rate to fall through the uncovered interest parity condition under which the domestic nominal interest rate is equal to the sum of the world nominal interest rate and the devaluation rate. Given full credibility, the agents would expect the domestic nominal interest rate to remain at this lower level forever. Due to the everlasting nature of this drop in nominal interest rates expectations, private agents would have no incentives to engage in intertemporal consumption substitution. Consumption remains constant over time since tradable resources do not change. The overall inflation rate of the economy also falls instantaneously with the drop in the devaluation rate. Therefore, a fully credible exchange rate-based stabilization program reduces the inflation rate instantaneously at no real cost.

The analysis changes somewhat under imperfect credibility where the assumption is that private agents believe that the reduction in devaluation rate would be reversed at some point in the future. This means that the nominal interest rate would be lower until the devaluation rate is expected to stay low. In this period, the effective price of traded goods is also lower leading to a rise in their consumption above the level of initial permanent income. However, once the devaluation rate reverts to a higher level, consumption of traded goods falls below initial permanent income and remains there forever. This occurs to satisfy the intertemporal resource constraint of the economy. The current account deficit increases until the lower devaluation rate is adhered to but jumps into balance once the policy is abandoned. In general, the net effect on inflation in the home goods sector is an initial decrease but a subsequent continuous increase in anticipation of the abandonment of the low devaluation-rate policy. This increase would continue if the policy is indeed abandoned but the inflation rate would drop in the face of a continuation of this policy. The overall inflation rate also follows the same path as inflation in the home goods sector up to the point where a reversion in the devaluation rate is expected. Thus the model predicts inflation inertia under imperfect credibility. Moreover, the drop in inflation is small the lower the credibility of the program.

2.2 Empirical Regularities

The aforementioned models have been attempts to explain what has been observed in Argentina, Brazil, Chile, Israel, Mexico, and Uruguay—countries that embarked on exchange rate-based inflation stabilizations in the recent past and that have served as the basis for identifying the main empirical regularities associated with exchange rate-based programs as identified in Kiguel and Liviatan (1992), Vegh (1992), and Hamann (2001). These are listed below:

- Inflation falls gradually and converges to the rate of devaluation.
- The real economy initially expands following the implementation of the program but eventually contracts.
- The domestic currency appreciates in real terms and depreciates following the collapse of the program.
- The trade and current account balances worsen.
- The effect on real interest rates is ambiguous.

Good recent examples, for comparison, of postwar reconstruction and stabilization come from South East Europe from countries such as Bosnia and Herzegovina. The approach has been credited for bringing about macroeconomic and financial stability to these countries. However, in the case of Bosnia and Herzegovina, growth has been lower than expected averaging around five percent per year according to the World Bank. The saving grace of the policy has been the gradual but unambiguous decline in inflation that, according to the central bank of Bosnia and Herzegovina, hovered around 0.6 percent in 2003. Tracking the empirical regularities mentioned above, the trade and current account balances have worsened and stand around 56 and 30 percent respectively of GDP, again according to the country’s central bank. Another example is that of Croatia that achieved a high level of price stability using the exchange rate as nominal anchor but only at the expense of low growth (averaging around 3.5 percent over the past decade)—which again seems to agree with the empirical regularities listed earlier—but relatively benign current account deficits (averaging around 5.5 percent according to the National Bank of Croatia).

Two broad approaches found in the theoretical literature on exchange rate-based stabilizations are the use of an equilibrium framework to examine these programs (see, for example, Rebelo and Vegh, 1995; Dornbusch, 1982) and the recognition of the importance of persistent high inflation as a significant factor in influencing inflationary dynamics (for example, Calvo and Vegh, 1994; Edwards, 1993).

Using the exchange rate as the nominal anchor to act directly on inflationary expectations appears attractive from a policy-making point of view because they should theoretically increase the chances of lowering inflation at no significant real cost. However, in the late 1970s, the Southern-Cone countries comprising of Argentina, Chile, and Uruguay that launched stabilization programs based on a pre-announced exchange-rate path that exhibited a declining rate of devaluation, policy-makers observed inflation that responded only gradually to changes in the exchange rate. Kiguel and Liviatan (1990) examine the case of these countries and Israel in the 1980s—which actually succeeded in sharply bringing down inflation—to describe the typical aftermath of exchange-rate based stabilization programs as a consumption/output expansion and appreciation of the real exchange rate followed by a consumption/output contraction and a depreciation of the real exchange rate. But theory suggests an almost immediate contraction following the implementation of the program while the observed "business cycle" runs counter to conventional wisdom.

This can be explained by again invoking Calvo and Vegh (1993a, 1993b) and the issue of credibility. As a general rule, stabilization programs lack credibility at the time they are being launched. This is natural given that high inflation is likely to be viewed as a consequence of the failure of existing policy or of political tensions. This is evident from the protracted large differential between domestic and world interest rates in economies these stabilization programs have been implemented. In war-ravaged economies, this issue takes on a unique form. One point this paper investigates is the type of post-stabilization business cycle that occurs in countries in the period following war and whether lack-of-credibility can account for that type of business cycle.

3 Exchange Rate-Based Stabilization in Lebanon

3.1 Post-War Reconstruction in Lebanon

Prior to 1975, the year in which civil war started, the Lebanese economy was the most dynamic in the Middle East region. Among its distinguishing features were low rates of inflation, high economic growth rates, large balance of payments surpluses, small fiscal deficits, and a floating, stable, and fully convertible domestic currency. The liberal economic regime was characterized by limited regulations on the functioning of markets for goods and services, labor, capital, and trade, as well as by low levels of taxes compared to other similar developing countries. Lebanon also served as an important intermediary between Europe and the rest of the Middle East. Its well-educated population gave it a comparative advantage in service sectors like banking and finance, and tourism and this, combined with the factors mentioned earlier, made Lebanon the hub of economic activity in the region.

This legacy was disrupted by the advent of the debilitating civil war that lasted from 1975 to 1990. Following the war that inflicted total damage to physical assets estimated at $25 billion (Gressani and Page, 1999), the Lebanese authorities started on the difficult task of simultaneously stabilizing and rebuilding the country. At the end of the war in 1991, real GDP stood at 3.72 billion Lebanese pounds, down from LP 6.82 billion in 1975, while real per capita income had gone down to less than half of pre-war levels (Eken, et al, 1995). The government played a primary role in reconstruction by first formulating the National Emergency Reconstruction Program and following it up with the Horizon 2000 Program. The idea was to rehabilitate and enhance the country's infrastructure and lay the groundwork for private sector led growth over the medium term.

While the end of the civil war came later, Lebanon managed to lay down the foundations for a peaceful settlement in 1989 with the Taif Accord for National Reconciliation. The conflict eventually came to an end in 1990 and government authority was gradually restored. The years 1991 and 1992 proved to be difficult both politically and economically. Contributing to this situation were the needs for reconstruction of physical, social, and legislative infrastructure. While the Lebanese pound-US dollar exchange rate stabilized in 1991 (to about 880 pounds per dollar according to Banque du Liban), hinting at some economic and political confidence, it dropped rapidly by 64 percent in nine months by September 1992 (Gaspard, 2004). The government was forced to resign in the face of angry labor demonstrations. There was no surprise in these developments given the untenable situation following the end of the civil war, a period characterized by frequent attacks on the exercise of civil and political rights and significant economic uncertainty. From the end of the civil war up until 1992, Lebanon remained in a transitory state, having to undergo political reconstruction, including the reestablishment of its political, military, security, and administrative capabilities. The resignation cleared the way for the first parliamentary elections in 20 years, which were completed at the end of 1992. This, together with the installation of the new government, significantly contributed to the restoration of confidence. Under the premiership of Rafik Hariri, who served as Prime Minister from late 1992 to 2004 with a gap only from 1998 to 2000, political stability improved in 1993. His government set reconstruction as its foremost task and based this on a publicly stressed commitment to stable exchange rates. The billionaire Prime Minister, who also held the portfolio of Finance Minister, had made his fortune in real estate in Saudi Arabia and enjoyed external and internal political support as well as a reputation for being an astute economic manager. These characteristics lent substantial credibility to the government and contributed to the subsequent success of the stabilization program. This type of success is an important distinction that many post-conflict economies in the process of reconstruction often share with each other. The most often cited examples of these are post-World War II Germany and Japan that are discussed with the relevant institutional context by Cowen and Coyne (2005).

"Horizon 2000, for Reconstruction and Development" delineated the reconstruction program to be undertaken by the Lebanese government. This plan proposed the expenditure of $14.3 billion over the period from 1993 to 2002 on sectoral and regional rehabilitation and development. The idea was predicated on the belief that peace would assist in the rehabilitation and upgrading of infrastructure, which would in turn lay the groundwork for the economy to regain its past glory. The private sector was envisioned as the driving force behind this strong economic recovery, returning to Lebanon climbing living standards and its premier pre-war status of a regional hub for trade and finance. The plan was to thrust Lebanon into the category of upper middle-income countries by 2002 by doubling its per capita GDP relative to levels immediately following the collapse of Mr. Hariri's predecessor government. In fact, GDP was to touch 1974 levels in 1995. To see how ambitious this really was, one only needs to note that GDP was a mere 64 percent of its 1974 level in 1992.

The private sector was to play a leading role in the plan by investing at twice the rate of the public sector with the average total rate averaging 31 percent of GDP over the life of the plan. GDP growth over 1993-2002 was expected to be 9.3 percent with international trade playing a major part—exports of goods and non-factor services were to grow at twice the rate of GDP growth. The plan also placed considerable focus on financial targets. The plan anticipated a current fiscal surplus by 1995, the same year in which public sector debt was to peak at 84 percent of GDP, declining thereafter to 39 percent of GDP by 2002. Annual consumer price inflation was to fall to and stay steady at four percent by 1996 from its 1993 level of 15 percent.[2]

The plan, however, lacked a reasonable incorporation of post-war realities and failed to base itself on the availability of existing resources in the economy as well as the badly battered economic structure. The ripple effect of these miscalculations influenced the actual growth in output and exports. The notorious inefficiency of the public sector adversely affected any chances of correcting fiscal imbalances and in the absence of any substantial reform, growth and public spending followed widely divergent paths with the former soon losing steam while the latter continuing its unchecked ascent. As a consequence of these structural and macroeconomic problems and other uncompromising economic developments, the suspension of the implementation of the plan by 1997 came as no surprise.

During the lifetime of the program, however, the Hariri government did have considerable success in both stabilizing macroeconomic indicators as well as in rebuilding infrastructure. His reputation as an astute economic manager was bolstered by his success in attracting domestic and international investment and support for the program. However, this progress, while impressive in its own right, did not meet the objectives as stated by the government. These included a return to the position of the regional financial and commercial center.

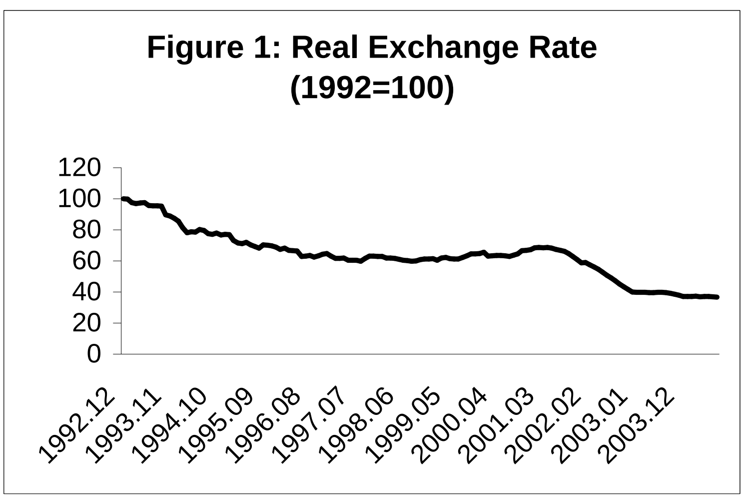
Indications of the plan's impending failure were indeed present early on. As stated earlier, fiscal recklessness had made massive budget deficits a pervasive feature of Lebanon's economic landscape. Mounting public debt levels led to financing problems making the suspension of the Horizon 2000

[2] Inflation actually fell from 131 percent in 1992 to 12 percent in 1994 (Najem, 2000).

program inevitable. While significant physical infrastructure rehabilitation had been completed by this time, social infrastructure projects still needed attention. Given that the latter is crucial in supporting the productive sectors of the economy, it is easy to understand the unimpressive role of the private sector in driving investment and the ultimate abandonment of the plan.[3] Also, Hariri had not been particularly successful in attracting long-term private sector investment with the exception of banking and real estate. However, even this investment had a rather ephemeral effect on the Lebanese economy, which goes some way towards explaining the slump that the economy experienced in 1997, the same year of the demise of the Horizon 2000 plan. The first Hariri government disintegrated in 1998.

3.2 Assessment

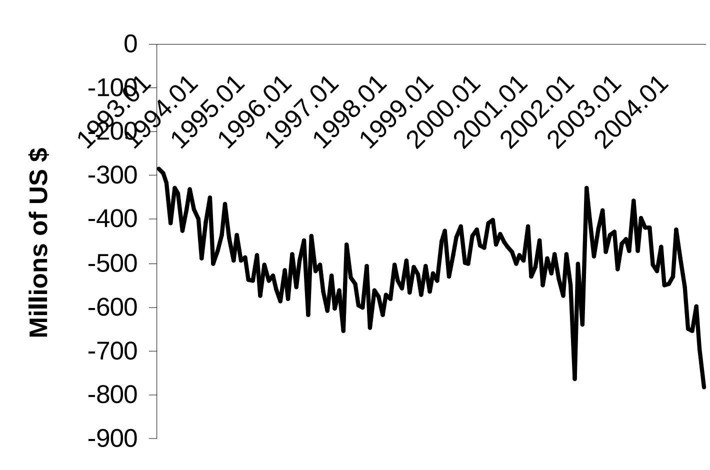
To gauge the influence and effectiveness of this exchange rate-based stabilization and to illustrate the dynamic response of the different variables to the implementation of the policy, profiles over time of these variables are presented below. Figure 1 below presents the monthly real exchange rate values over the past 13 years (1992-2004). The distinguishing feature of real exchange rates here is its continual appreciation over the post-war period, which is unlike the case of other exchange rate-based stabilizations where the program often collapses and the exchange rate reverts to it depreciative tendencies. Generally, the real exchange rate appreciates for three consecutive years following the stabilization before beginning to depreciate. One reason for this is the less than stellar record of success of exchange rate-based programs versus the triumphant episode in Lebanon. Also, a war-ravaged economy is likely to attract substantial foreign capital to rebuild. In fact, Lebanon in particular reformed its tax regime in order to encourage both domestic and foreign investment and spur entrepreneurial activity. This would also explain the appreciation pressure on the Lebanese currency. The trade balance, in general, worsens up to the year in which the real exchange rate reverts. For Lebanon, there was a very slight trend towards improvement almost four years after the implementation of the program following continual decline in the trade balance immediately after the program's implementation, but this has since changed into the largest trade deficit since the end of the civil war (Figure 2).



Source: Author's calculations based on data from Banque du Liban and Banque Audi.

[3] An example of this was the failure to revitalize the previously vibrant tourism sector.

Figure 2: Trade Balance



Source: Banque du Liban.

Figures 3 and 4 present the behavior of the rates of inflation and devaluation respectively. The Lebanese program's achievement of its objective is clear from figure 2, which shows annualized monthly inflation not only being brought under control and down to levels below 10 percent from upwards of 144 percent, but being consistently kept there for almost over a decade. More recently, the inflation rate has dropped further to below 5 percent. However, the observation that sets the case of Lebanon apart from the previous ones is the performance of the devaluation rate. The devaluation rate under past programs has tended to initially go down from about the same levels as inflation followed by a reversal to an upward direction. This has been due to the fact that, more often than not, after a brief period with a fixed exchange rate, policymakers either switch to a more flexible exchange rate or dump the program altogether. While the trend in Lebanon has been similar to an extent, the difference is that the slowing down of the devaluation rate was in fact initially an increase in the appreciation rate. However, the situation changed swiftly and the exchange rate started to experience a decrease in the appreciation rate (or an increase in the devaluation rate). The inflation rate was highly responsive to this initial increase in the rate of appreciation and has remained at desirable levels even after the switch in the direction of the devaluation rate because, after all, the currency has appreciated overall.

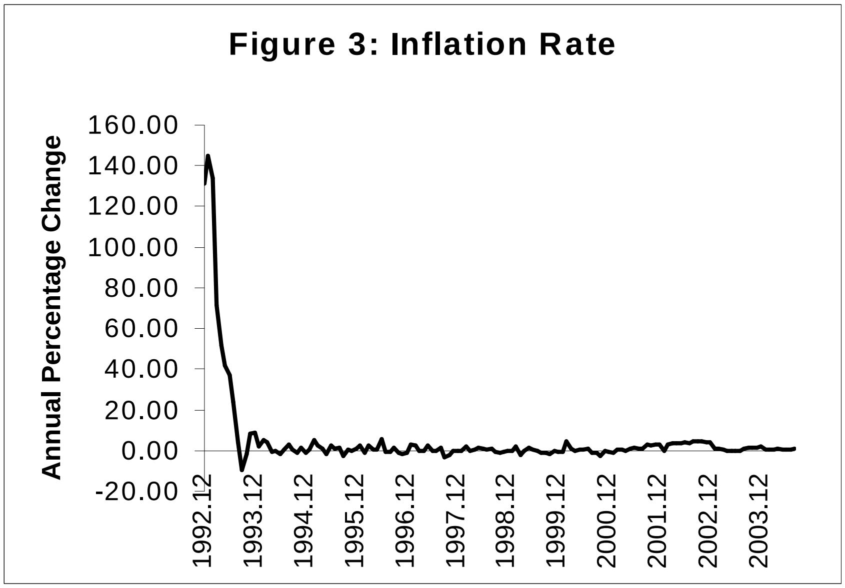


Figure 3: Inflation Rate

Source: Banque Audi Research Department.

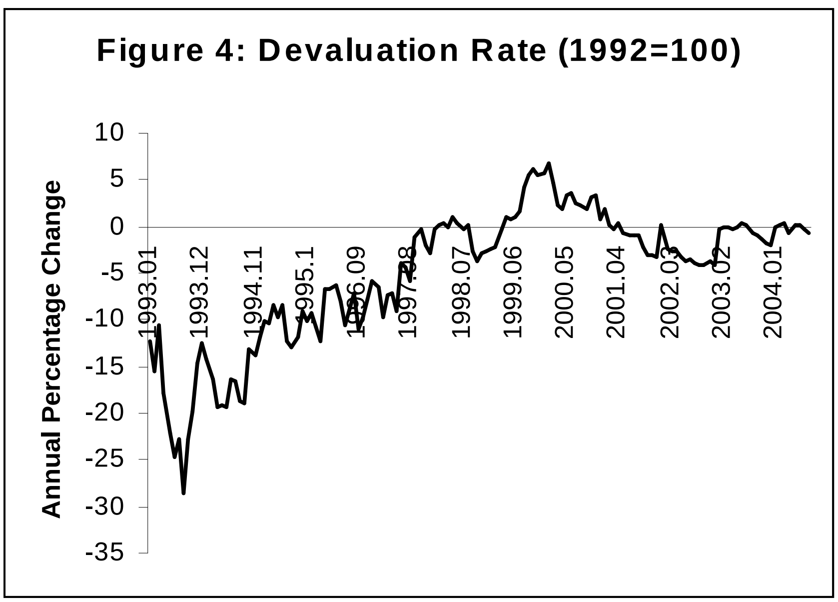
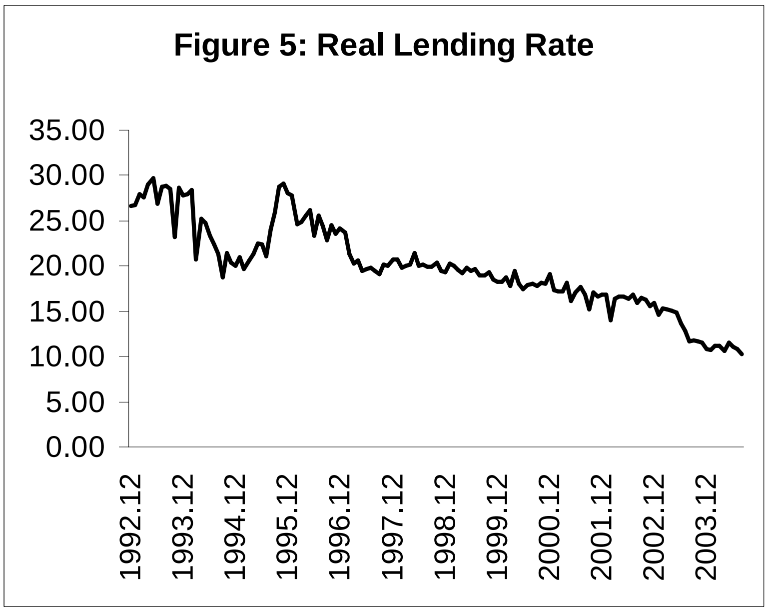


Figure 4: Devaluation Rate (1992=100)

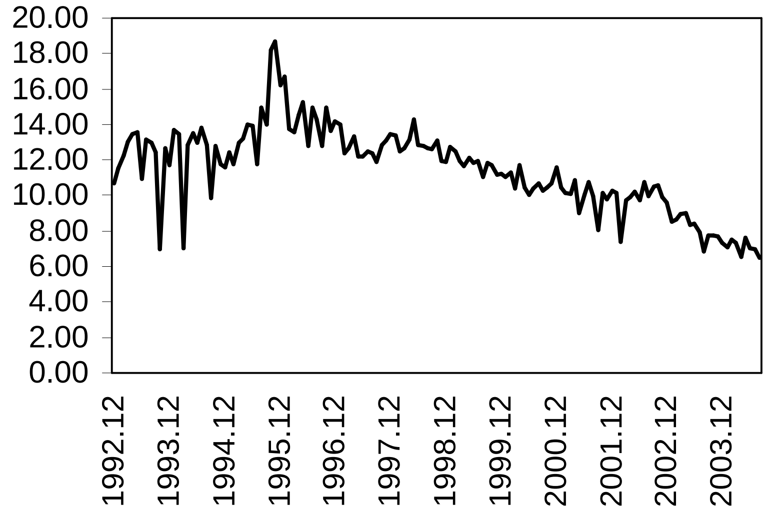
Source: Author's calculations.

The appreciation can be attributed to a rebound after some semblance of order and stability takes hold in a country devastated by war and chaos. As pointed out earlier, the more accommodating tax regime aimed at stimulating investment from domestic as well as from foreign sources that led to higher capital inflows could also have contributed to the appreciation. Another explanation could be the considerably high level of interest rates that prevailed at the beginning of the program and that the government needed to finance its ambitious reconstruction drive following the civil war, another feature common to economies trying to rehabilitate. Figures 5 and 6 below show the behavior of the domestic real lending and deposit rates. The effect on real interest rates has been ambiguous with some previous exchange rate-based stabilization episodes characterized by a sharp rising trend in interest rates immediately following the implementation of the program while others have displayed a decrease in the initial stages. This has been clearer with annual data and even quarterly data has been shown to display the same behavior but with spikes. The corresponding figures for Lebanese monthly data confirm this ambiguity with even more spikes. Real interest rates did not rise immediately following the implementation of the program experiencing only a minor increase after a few years. They have been on a steady declining trend since the mid-nineties.



Source: Author's calculations based on data from Banque du Liban and Banque Audi.

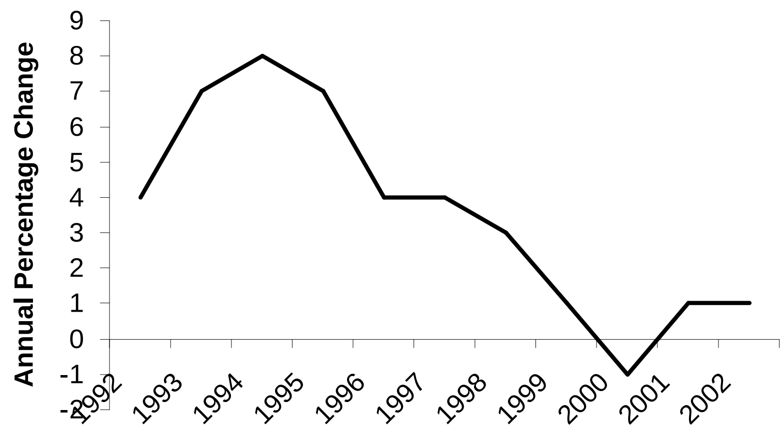
Figure 6: Real Deposit Rate



Source: Author’s calculations based on data from Banque du Liban and Banque Audi.

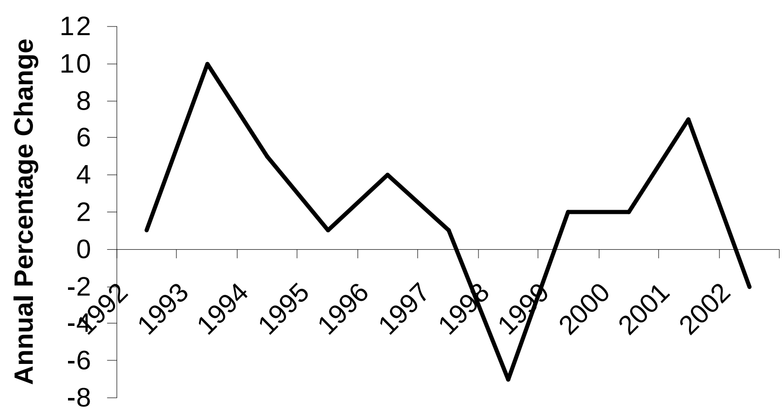
Figures 7 and 8 present evidence related to the boom-recession cycle in the growth of annual real GDP and consumption respectively. In accordance with the stylized facts, real GDP growth increases for a couple of years following the implementation of the program and decreases thereafter. The same pattern is observed in consumption growth. Note, however, that in terms of magnitude, the cycle is more pronounced in the case of consumption. At its peak, consumption growth reaches 10 percent per year while real GDP growth touches 8 percent. Thus we can see that the profiles here closely follow the contours of a boom-recession type cycle that has been attributed to exchange rate-based stabilization programs. Although the Lebanese case is an example of a successful stabilization, recessions have been known to occur in the case of both successful and unsuccessful programs. In unsuccessful cases, a recession typically takes hold before the collapse of a program. The decline in the growth rate here starts about two years after the institution of the program, which is what has been observed on average in previous cases of exchange rate-based stabilizations, such as Uruguay, Chile, Turkey, and Israel (Calvo and Vegh, 1993b, 1999). Hamann (2001) also obtains similar results using a comprehensive panel study.

Figure 7: Annual GDP Growth



Source: *World Development Indicators* Database, World Bank.

Figure 8: Consumption Growth



Source: *World Development Indicators* Database, World Bank.

The profiles in stabilization displayed in the figures are largely consistent with the stylized facts listed earlier. However, there are a few important differing points. The most significant of these that should be taken note of is the absence of a serious recession in the Lebanese case. While the real growth rate did eventually slow down in Lebanon and the country did pass through a mild recession, it never came close to the severity of recessions experienced by other countries that had earlier attempted stabilization via the use of an exchange rate anchor. As pointed out earlier, Lebanon's currency appreciated overall, ultimately settling at a stable nominal exchange rate. Consequently, the real exchange rate has gradually appreciated over time and has been almost constant over the last few years. Real interest rates, after having displayed no real trend in the couple of years immediately following the program, have also been on a steady decline.

4 The Role of Credibility in Stabilization

While the work of Calvo and Vegh described earlier explains the importance of credibility in exchange rate-based stabilizations, it does not provide us with any idea of how statistically significant this role really is. Although investigating this is a far from trivial exercise, simple econometrics can provide some useful insight. In the spirit of Reinhart and Vegh (1994), we run a regression on a dummy variable intended to capture policy credibility and test whether Lebanese inflation is significantly related to the devaluation rate. The sample for the regression contains 140 monthly observations (January 1993-August 2004). We define the credibility dummy as taking on the value of one from January 1993 to December 1995.

This period was chosen since it closely corresponds to the time through which socio-political goodwill and trust in government policy intentions can reasonably be claimed to have persisted. However, the amity started to dissipate with periodic opposition that Hariri had to face from members of his own cabinet and from the members of the Lebanese parliament, not to mention the president, Elias Hrawi, and the powerful Speaker of the House, Nabih Birri. Hariri was forced to compromise with parliament on a number of issues including the 1995 budget. The prime minister's economic programs came under fire from several important members of parliament due to the concern that the Horizon 2000 program would saddle Lebanon with an unmanageable debt burden.

The climax was reached in December 1995 when Hariri announced his resignation, although he later recanted this. The reasons for the move were the constant accusations of corruption directed against him and the refusal by the parliament to pass the 1995 budget. The stated reason for the resignation was to protect reconstruction projects for Beirut's city center. Hariri had, on several previous occasions, used the threat to resign in attempts to break political deadlock. However, the December 1995 limit was chosen for the credibility dummy because the resignation announced in this month had the most visible adverse effect on the economy and particularly the exchange rate—Banque du Liban had to spend an estimated $342 million to stabilize the currency (Najem, 2000). Further reasons for inimical effects on credibility are provided by Shahin (2002) who identifies political instability as a significant reason for the declining confidence of businesses and investors in the Lebanese economy. Not only did the economic environment had to contend with the whims of Prime Minister Hariri and the tumultuous presidential elections of 1995 on the domestic front, it also had to suffer Israeli attacks in 1996 that destroyed key infrastructure.

The estimated regression equation is as follows:

$$INF_t = \alpha_0 + \alpha_1 DEVRATE_t + \alpha_3 CRED_t + \varepsilon_t \,,$$

where *INF* is the Lebanese inflation rate, *DEVRATE* is the devaluation rate, *CRED* is the credibility dummy, and ε is the error term. All variables, except *CRED*, are in logarithms. The results are presented in Table 1 below.

Table 1: Regression Results

	Intercept	Devaluation Rate	Credibility
Coefficient	2.618	0.038	0.431
t-statistic	9.494	0.476	2.382
p-value	<0.001	0.635	0.019

The results show that Credibility has played a strongly statistically significant role in the stabilization process. This lends further support to the role of imperfect credibility in stabilization programs pointed out by Calvo and Vegh and which was discussed earlier. In Lebanon, the inflation rate came down rapidly with the initial decrease in the rate of depreciation (or, more accurately, the initial increase in the appreciation rate) but then remained contained even after the reversion to the subsequent gradual increase in the depreciation rate. The substantial cushion of being able to increase the rate of depreciation (which, in this case, was really a decrease in the rate of appreciation) without actually causing the currency to depreciate is a major reason for inflation to have stayed low. Sensitivity analysis conducted on these results suggests that credibility becomes even more statistically significant if we move up the date to before December of 1995. In fact, that is what we observe if we closely follow the definition used by Calvo and Vegh, which is that Credibility ends once the depreciation rate starts to increase after an initial decrease. This would mean that instead of making the end of 1995 our cut-off for Credibility, we would have to assume it over by the end of 1993, which is also the period by which inflation had effectively been tamed.

5 Conclusion

This article has analyzed Lebanon's post-war exchange rate-based stabilization in order to assess the role and scope of this policy and to shed light on the efficacy of the approach in other economies that have undergone severe economic dislocation. Both Iraq and Afghanistan could be considered for such a policy after having taken their specific institutional characteristics into account. Economic research suggests that the two stabilization approaches based on the use of nominal anchors, namely money- vs. exchange rate-based stabilization, present the policy maker with a choice: either accept a contraction in economic activity right after the implementation of the program (for money-based stabilizations) or after a period of a few years (for exchange rate-based programs). Due to the initial boom immediately following implementation of exchange rate-based stabilizations, this approach should be more suitable for countries emerging out of periods characterized by devastating wars, natural disasters, or other such occurrences that exact a heavy toll in human and material terms and cause fundamental changes to the structure of the economy.

However, there is a further level of analysis that needs to be considered even after an exchange rate-based stabilization is identified as the suitable policy. Earlier research has found the role of credibility to be of paramount importance in determining not only the success or failure of the program but also the dynamics of economic variables. The case of Lebanon demonstrates further the crucial role of credibility as manifested in the early period of leadership of Prime Minister Rafik Hariri. The quick success with which the program was met and its objective of stabilization achieved, are highlights of the exchange rate policy being carried out on the shoulders of credible policy makers. Lebanon's economic slump in 1997 came on the heels of the Prime Minister's evaporating credibility and claimed his government victim. Although the usual disclaimer against far-reaching generalizations applies, the analysis above does suggest the usefulness of considering the credibility of policymakers among their populations if war-ravaged countries like Afghanistan and Iraq are to embark on a program of exchange rate-based stabilization. Therefore, while exchange rate-based stabilization programs hold considerable promise for countries suffering from economic instability, the eventual success of such programs may depend on an absence of chaos and a relatively healthy political environment conducive to policy makers who inspire trust in the population at large.

This paper, while discussing the theory of exchange rate-based stabilizations in general, has not covered models that analyze this policy following a conflict. The reason is a lack of relevant theory in the existing literature. This points to a new and potentially very fruitful area for further research, concerned with the development of political economy models of exchange rate-based stabilizations in postwar economies that incorporate the often-unique institutional features not present in the majority of cases where stabilization is the objective. In that sense, the extensive analysis of the Lebanese case and the discussions on the South East European countries in this article should serve as helpful starting points.

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The Political Economy of Sub-Saharan Africa Land Policies

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Abstract

The quest for African poverty alleviation has become a global issue and governments of rich nations have registered their commitment to the task both through the Millennium Development Goals and other international programs. While poverty is endemic in Africa, extant policies that continue to dictate proceedings in the land sectors of most African nations have been constructed in a way that concentrate benefits and wealth on a few while spreading costs and poverty on a larger segment of the African population. These policies which continue to impose greater restrictions on poverty alleviation have emanated from the peculiar political and economic history of Africa. An understanding of how these political events continue to shape the performance of land markets in these countries within the context of contemporary economic learning is thus key to understanding the policy directions required for success. This paper thus employs public policy and transaction costs insights to explicate the historical political events that have led to the promulgation of such policies together with a conceptual view of their social cost implications.

JEL Classification Codes: P26, Q15, Q24, D23, O55

Key Words: stool lands, land policies, transaction costs, political economy, sub-Saharan Africa

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INTRODUCTION

This paper employs transaction cost analysis and public choice theory to examine political influences that have shaped land policies in sub-Saharan Africa with greater emphasis on Ghana. The conditions that have given rise to poverty in Africa are manifold ranging from corruption, political instability, unfair international trading rules, outdated policies and laws, poor social and economic infrastructure, weak capital and financial markets, poor human resource development systems, malfunctioning land and real estate markets, and so forth. While efforts by rich nations to rid Africa of poverty through debt cancellation and aid donations provide no more than temporal relief, they are appreciated, but only to the extent that they help remove conditions that give legitimacy to poverty in Africa. Otherwise, they warrant no great confidence.

In recent times, perhaps as a response to research under the new institutional economics rubric in the 1970s, there is growing concern about making land tenure contribute meaningfully to the quest for poverty alleviation in Africa. This has inspired a closer look at the workings of land markets and government interventions in the region (Quan, 1997; Toulmin & Quan, 2000; Quan, 2000; Platteau, 2000; Delville, 2000; Okoth-Ogendo, 2000; Cousins, 2000; Palmer, 2000; Wily & Hammond, 2001; Deininger, 2003). It is well established in neoclassical economic theory that, from an efficiency standpoint, land policies, like all forms of government interventions are desirable only on occasions of true market failures and excessive transaction costs (Coase, 1960; Pigou, 1962; Tisdell, 1974). Yet in reality, extensive research (Hogwood & Gunn, 1984; Rose, 1986; Nakamura, 1987; Stone, 1989; Jenkins-Smith, 1990; Lindblom & Woodhouse, 1993; Stone, 1996; Dye, 1998; Sutton, 1999; Parsons, 2003) shows policies, whether in sub-Saharan Africa or in advanced capitalists economies, are determined largely on political and bureaucratic considerations sometimes merely spiced with economic reasons. This implies a prerequisite to understanding these policies is an appreciation of the political and bureaucratic forces that have constructed them. The polar departure here is the usage of economic analysis; in particular, transaction costs theory to explicate the historical origins of the policies that are dictating proceedings on these land markets.

PLURALISM, PUBLIC CHOICE AND TRANSACTION COSTS

The processes by which policies evolve vary markedly between societies and political systems (Cobb & Elder, 1972; Jenkins-Smith, 1990; Rochefort & Cobb, 1994). While it is recognized that the policy processes can be examined from the rationalist and pluralist perspectives, there is no space here to look at both perspectives in an in-depth manner. Thus the pluralist approach is employed solely to examine the land policy processes of sub-Saharan Africa (for a discussion on the rationalist alternative, see Laswell, 1956; Simon, 1957; Mack, 1971; Jenkins, 1978; Hogwood & Gunn, 1984; Rose, 1986).

The pluralists deem public policies as the outcome of free competition between ideas and the interests of many actors (Parsons, 2003). These actors typically comprise public opinion (Hogwood & Gunn, 1984), the media, experts and professionals including think tanks (Parsons, 2003), bureaucrats (Niskanen, 1973), interest groups (Sutton, 1999) and politicians and voters (Downs, 1957). The complexity here stems from the fact that each policy actor tends to hold peculiar ideologies, values and interests that are often in conflict with those of others (Dahl & Lindblom, 1953). Policy formation accordingly turns on pluralism, mutual adjustment, consensus seeking and incrementalism (Lindblom, 1959; 1980; Nakamura, 1987; Stone, 1989; Sabatier & Jenkins-Smith, 1993; Lindblom et al., 1993). Progress is thus made in the policy process only when there are means of resolving conflicts of values, interests and ideologies between policy actors in a way that makes formation of Pareto efficient policies[4] possible.

Public policy studies (McKean, 1965, pp. 496-505; Haveman, 1976, ,pp. .235-250) suggest that in such a process optimal outcome in policy formation is achievable when all actors involved are fully equipped with relevant knowledge and are willing to negotiate and build consensus on

[4] This is the policy that drives the recipient economic system to the point where it is no longer possible to improve the well being on one individual without making at least another individual worse off.

policy choices that offer the ultimate means of maximizing individual and societal welfare. Additionally it requires "a political process in which the full set of impacts of a decision on all citizens, the poor and minority groups as well as those with power, be somehow registered with decision makers" (Haveman, 1976, p.239). The ideal form of the pluralist process can be likened to a "smoothly functioning market system" in which the full costs and gains of any decision as experienced by individuals would be brought to bear on the decision maker (Jenkin –Smith, 1990, p. 30). Such an ideal policy process is based on the assumption of a widely diffused power structure in which each participant has equal influence on problem definition, agenda setting, and policy choice (Parsons, 2003). It is nonetheless well established that such an ideal policy processes is non-existent in reality (Jenkins-Smith, 1990) because unequal distribution of power between policy actors is a pervasive fact of political life (Brams, 1968, p.461). Often, it is the government of the day that dominates the policy process.

Public choice economists (Downs, 1957; Tullock, 1967; Niskanen, 1971; 1973; Buchannan, 1975; McLean, 1987; Mueller, 2004) present a formal objection to the conventional welfare economics view that governments are benevolent actors in the public interest with sacrosanct public policy roles. By using economic principles of rationality, individualism and self interested behaviors to examine behaviors of voters, politicians, voting rules and bureaucracies it is possible to understand or predict the true ends of the policies they formulate and implement (Mueller, 1989). Buchanan and Tullock (1962), Tullock (1965) and Downs (1967) the accredited originators of the ideas of modern public choice theories have laid the basis for the debate on the dangers of politicization of the economic and public policy processes. Particularly, Tullock (1965) and Downs (1967) basing their argument on self-interest maximizing behavior of political actors illustrate the harmful consequences of a government that would become ever more autonomous and sovereign in the policy processes. The extent to which this latter proposition has manifested in the land policy processes of sub-Saharan Africa is examined shortly.

Whilst public choice theory provides a powerful and convincing model for explaining policy processes from an economic angle, it is difficult to test in any meaningful quantitative terms in reality (Parsons, 2003, p.311). Besides, it omits an explicit treatment of how differing levels of transaction costs could produce differing behavioral patterns in policy actors. This is exceptional, given that, following Coase (1960), there is now something of a general agreement among economists that transaction costs form a crucial determinant of the efficiency of any exchange economy (Williamson, 1979; 1981; 1986). Thus without exploring the implications of transaction costs on the so-called political exchange economy it is impossible to imagine how policy problems that present themselves today can be traced to their real sources. The basic thesis of transaction costs theory is that higher transaction costs impede, while lower transaction costs promote, efficiency in any exchange economy. The relevant costs here includes background information search costs, organizing formidable and identifiable policy groups, costs of negotiating policy contents, costs of consensus building particularly in the area of problem definition, agenda setting and selection of alternatives as well as costs of monitoring and enforcement of policies when enacted. Other important costs include the costs of overcoming mistrust, uncertainty, duplicity and opportunism that may exists in the policy processes. Attempt is thus made here to explicitly incorporate these costs in the analysis of the sub-Saharan Africa land policy processes.

A competitive policy process akin to the democratic political regime is conventionally argued to offer the best model for efficient policy formation (Dahl, 1961; Cobb et al., 1972; Rochefort et al., 1994; Jenkins, 1999). This paper takes issue with this position and argues on the contrary, that both competitive and monopolized policy processes offer identical potential for efficient policies if transaction costs were nonexistent. Their relative efficiency depends on their inbuilt comparative transaction costs. Thus a competitive policy process could thus be even more inefficient than a monopolized system if their inbuilt transaction costs are relatively higher.

THE SUB-SAHARAN AFRICA LAND POLICY PROCESSES

Persistently, the African political scene has witnessed the concentration of power in the hands of a minority in power either through invasion, as in the colonial era, or the creation of a one party state through military interventions and despotism in the emergent democratic processes. These political events have culminated in exorbitant transaction costs in the policy processes out of which the region's land policies have emerged. These events are discussed in turn.

The Colonial Regime

Much has been written about the despotic rule of the colonial administration in Africa and how that influenced the determination and definition of problems, agenda settings and the choice of policies (Harris, 1975; Sender and Smith, 1986; Mabogunje, 1987; Platteau, 1992). Suffice to point out in this analysis that, during this period, the exploitative objective of the concept of colonialism (Kaniki, 1985) was the driving force behind the autocratic governance structure instituted out of which much of the initial land policies in the region emerged. The 1895 statement by the then UK Prime Minister, Lord Salisbury (cited in Kaniki, 1985) to the UK Parliament exemplifies the main concerns of the colonial monopoly administration. Lord Salisbury wrote:

> It is our business in all these new countries to make smooth the path for British commerce, British enterprise, the application of British capital, at a time when other paths, other outlets for the commercial energies of our race are being gradually closed by the commercial principles which are gaining more and more adhesion. In a few years it will be our people that will be masters, it will be our commerce that will prevail, it will be our capital that will rule… this is a tremendous power, but it requires one condition. You must enable it to get to the country where its work is to be done.

To accomplish this end there was the need to raise the costs of political opposition so the indigenous Africans who presented the eminent threat to this agenda were precluded from the policy process. The political institutions during this time were made up exclusively of the white minority. Policy decisions were arrived at without reference to the Africans and the Africans could only oppose policies from outside the formal policy making arena. Conflict in policy formation was thus between the social system and the formal decision making body. This meant that transaction costs faced by the Africans in seeking that their views were taken care of in the policy process were enormous. It entailed the formation of viable countervailing forces with strong opinion leaders whose views cannot be ignored even though they operated outside of the formal policy arena. Agenda building and policy formation thus tended on two principal transaction costs. One was the cost at which the countervailing forces could expand issues to gain the attention and support of a wider, even international, interested group and the second being the costs that the colonial powers were likely to incur if they ignored the views of the group.

If the cost of ignoring the views of the expanded audience or international interested group was regarded insignificant in comparison to the gains, the administration had enough motivation to ignore them. However, where it was costly to ignore, the administration was bound to take note of the countervailing forces. As Cobb and Elder (1972) explained, in such a situation issues that are unlikely to be ignored comprise (1) issues that are more socially significant; (2) issues that have long term relevance and (3) issues that lack clear precedent. Although, with regard to land policies all these conditions were present, the critical determinant of whether the views of the opposing forces would have to be taken account of was the ability of the opposing forces to bear the costs of expanding the conflict beyond the local formal policy arena. This was well illustrated when it came to the promulgation of colonial land nationalization policies. In some eastern, central and southern African countries where the opposing forces were unable to bear the full costs of issue expansion, their views did not represent a significant threat to the colonial administration and hence they were conveniently ignored. In these countries, the colonial administration successfully enacted policies that vested all property rights in "vacant lands" in the government of the day for redistribution (Noronha, 1985; Platteau, 1992). This tallies with the public choice view of what harm an overbearing sovereign could fashion.

In particular, in these countries the main beneficiaries of land policies of the colonial regime were the minority white settlers and private firms favored by the metropole (Glickman, 1988 p.

28). A case in point is the land redistribution policies in East Africa under the colonial regime in which contrary to the well-developed peasant agriculture found in Uganda and other African countries at the time of colonization (Kaniki, 1985); the beneficiaries of the redistribution of lands by the administration were the white minority. Such was the generosity of the redistribution policy that at one time Lord Delamere, a European entrepreneur, owned more than 400,000 hectares of land in Kenya (Kaniki, 1985). Similarly, in southern Rhodesia (now Zimbabwe), by 1911, Europeans owned about 7,700,000 hectares and by 1925, they owned 12,500,000 hectares at give away prices (Kaniki, 1985). Kaniki in fact reported that in southern Rhodesia "in 1894 each member of the Victoria and Salisbury columns recruited to crush the Ndebele was promised 6000 acres of farm land". These represent the origins of the violent clashes over land in present-day Zimbabwe.

Rationally, citizens will incur such transaction costs required to oppose such policies when they envisage the potential benefits to be at least commensurate with the costs. In countries such as Ghana, Nigeria and Ivory Coast where the opposing forces incurred the full costs of issue expansion around the 1890s they (the opposing forces) were able, in the case of Ghana for instance, to go all the way to England to protest to the English parliament and monarchy (Rimmer, 1992). Having expanded the issue this much, the colonial administrations in these countries could only ignore their views at extraordinary costs. They thus could not be ignored in fact (Mabogunje, 1989) and the policy of outright land nationalization that took root in eastern, central and southern Africa could not be applied in these West African countries (Rimmer, 1992). But in countries where the transaction costs for opposing such policies were unbearable the citizens became essentially cordoned off the policy process and the process of policy making became a game for those who can afford. In such countries opposing forces were ignored and the colonial administration had free hand in dissipating the land resources to the white minority and European merchants (Sender and Smith, 1986) as exemplified above. Where they could not be ignored the administration gained access only to those lands they acquired at full market prices (Meek, 1949). Policy decisions enacted more than a century ago continue to have economic repercussions on some of these societies many years after the colonial era.

As a result of these policies for instance, land ownership structure in eastern, central and southern Africa is severely skewed in favor of few whites or Europeans. This has engendered postcolonial clamor for more equitable redistribution of land resources by Africans, which are being honored through policy reforms at great costs (Toulmin and Quan, 2000). In some countries such as Zimbabwe the clamor is being honored through forceful takeovers of lands owned by whites leading to violent clashes, loss of lives, political instability and insecurity. Meanwhile in West Africa, the successful opposition presented by the countervailing forces prevented such skewed land ownership structure in these countries. Land ownership is thus more proportionately distributed in these countries and this has not specifically led to remarkable policy reforms and political events.

Interestingly however, across Africa, when it came to policies that regulated the activities and land transactions of indigenous land owners without necessarily nationalizing the lands, the opposing forces that had successfully subverted the earlier land nationalization policies were benign and presented no opposition whatsoever. These later regime of policies appear to be enacted to ensure state surveillance over the activities of land owners with the view to pre-empting and forestalling any activity or transaction that is likely to threaten colonial exploitation or breach of the peace which was vital for their exploitation. Generally, the central theme of these regulative policies followed the recommendations of the West African Committee set up to look into the causes of land litigations in parts of West Africa. The key recommendation of the Committee was that all transfers of interest in land to non-natives by Africans should be considered invalid unless it were by lease for a term of years and were made with the consent of the Governor [5] (Meek, 1949). In Ghana, for instance, this recommendation was implemented

[5] The governor would, they suggested, only give consent after receiving a report from the District Commissioner showing the area and boundaries of the proposed grant, whether the title properly belonged to the community proposing to grant it, whether the community fully assented, whether the consideration

under section 3 of the Concessions Ordinance (No.19 of 1939) as well as the Local Government Ordinance of 1951. In Kenya, the Crown Lands Ordinance of 1902 prohibited land sales between Africans and Europeans altogether (Platteau, 1992, p.97). These regulations were intended to curb the emergent litigation emanating from the then rampant land sales between African landowners and European concessionaires (Platteau, 1992; Woodman, 1996).

Having expended many resources in subverting the nationalization policies, the West African countervailing forces appeared to have exhausted their resources and could not mount similar opposition. Another explanation could be that rationally, the citizens did not see the potential benefits to be commensurate with the costs. A great deal of the lack of opposition to such policies may also relate to the transaction costs faced by the African landowners and countervailing forces in obtaining the relevant information to be able to appreciate the full and long term implications of such regulations of their rights (see Alchian, 1965; Demsetz, 1967; Pejovich, 1997). In the absence of such information, opposing forces saw very little gain in incurring the costs of opposing as those in West Africa had done previously. It is highly probable given the supply of available land that at the time the restriction on their property rights did not reduce their earnings from land significantly. As Meek (1949) reveals most of the transactions were informal and purchasers were comfortable with any form of receipt or site plans, most of which had no bearing with the true triangulations of the land in question. Since these regulative policies were only enforceable when transactions were brought to the attention of public officials, very few of such transactions were subjected to these policies given the state of land documentation. Thus the practical impact may well be very minimal and hence did not warrant the costs of opposition. Indeed it is possible that eminent opposing forces perceived these policies as more beneficial even, as it enabled indigenous landowners to retain ownership of their lands even after they have sold the land.

It is evident from property rights insights (Becker, 1977; Ault & Ruthman, 1979; Pejovich, 1990) that had power in the policy process been fairly distributed and costs of transactions including costs of obtaining relevant information and the costs of opposition been low, landowners would have favored free markets. Thus, they would have opposed such trade restrictions that evidently reduced their rights to free trade.

The Single Party Postcolonial Regimes

Autocratic or monopolized policy processes instituted by colonial regimes became convenient legacies for succeeding postcolonial regimes. Hameso (2002) argues “the post-independence leaders took over the political kingdom in its enticing state”. Yet at independence some five decades ago, all postcolonial African countries emerged as democracies governed by constitutions framed along the lines of what pertained then in the respective imperial countries of the colonial authorities (Bratton & De Walle, 1994). Power within the policy process was diffused and transaction costs were lower than during the colonial era. Soon, “political plurality were decried as bottlenecks to the project of ‘nation-building’ and national unity”(Hameso, 2002). The new African leaders who adopted a socialist ideological stance (Sender and Smith, 1986) faced enormous transaction costs in seeking to impose their views and ideologies on society. But the notion that socialism was the desired objective does not seem to fit well as Europe has had several social democratic governments that have embraced socialism without resorting to dictatorship. As it turned out, the real rationale for the choice of socialism at the time was two fold. First was to meet the growing demands of the emergent African bourgeoisies who had contributed to the achievement of independence and hence were better placed to demand favors from the incumbent. Second was the urgent need for the new nationalist governments to consolidate power over national resources to be able to institute central planning and state direction of resource allocation in accordance with the then mainstream development economics ideologies in vogue (Sender and Smith, 1986). This second agenda also gained credence from the

offered was adequate and the grant would not materially interfere with the community’s requirements in the matter of agriculture, fishing, hunting and the collection of natural products.

then favorable outlook of socialism and state interventions in the Soviet Union and England (Sender and Smith, 1986). As Young puts it:

> development economists, sympathetic to state-led development and dominant modernisation theories readily acknowledged that economic development came first with democratisation expected to follow later (Young, 1996, p. 54).

This second rationale also made it more convenient for the first rationale to be accomplished through distribution of favors to the clients of the state after the state had gained a free hand in the control and allocation of vital resources. Transaction costs that the incumbents would need to incur to accomplish these two agendas were likely to have been very high in a pluralist environment, as it would entail reaching agreement with all countervailing forces on policy agenda and contents as well as overcoming uncertainties in the policy process as explained earlier. Nonetheless in a truly democratic pluralist system where public opinion and the media matter in decision making, the costs of maintaining strong opposition are on the contrary likely to be low. In Ghana, for instance the choice of a socialist agenda by the first post-independent administration led by Nkrumah easily precipitated the formation of an opposition group, the National Liberation Movement (NLM) who immediately successfully represented an important impediment to the socialist goals of Nkrumah (Killick, 1978). The NLM went to the extent of calling for a federal system of government to whittle down the power of Nkrumah. The call eventually led to another election in 1954 three years before independence (Card, 1975).

The costs of formulating these so-called socialist policies from the perspective of the incumbent was thus mammoth and the options left for the government of the day was either to incur the costs of negotiating with the opposition or incur the costs of eliminating the opposition altogether. The second option meant that the transaction costs of opposition were to be raised so high to make it unprofitable to oppose. Since the outcome of any negotiation with the opposing forces was uncertain and potentially unfavorable to the incumbents the first option was unsustainable. The most plausible option left was to raise the transaction costs of opposition and to ultimately eliminate the opposition (Rimmer, 1992). In Ghana the transaction costs of opposition were pegged so high that it became practically impossible for the opposition to partake in the policy process. However, the idea of eliminating opposition is really something that coincides with a desire for totalitarianism and megalomania, not socialism.

This was realized by transforming the multiparty democratic colonial political legacy in which transaction costs was relatively low to a single party system in which the opposition faced virtually all the costs of consensus building. To achieve this goal, in 1960s and 1970s most countries in sub-Saharan Africa transformed their political systems from a pluralist multiparty system to a monopolized one-party system. Such was the commitment to power-hungry dictatorship that during this period, thirty-two of the fifty-four African countries converted from a multiparty political system to a single party political system (Bratton and de Walle, 1994). By the end of this conversion period, power to enact policy became almost exclusively concentrated in the hands of the incumbent with all opposing forces and pressure groups substantially cordoned off the policy process.

Ultimately in countries such as Ghana, this entailed removing the constitutional provisions that mandated decentralized government structures. This was followed by rapid expansion of presidential powers in tandem with the removal of constitutional checks on the executive branch of government and then the imposition of a one party state (Daddieh, 2001). Nevertheless, this path to the single party state was rugged. The process commenced by discrediting political opposition. Indeed political opposition was viewed as despicable (Hameso, 2002). In Malawi the leadership argued: “there is no opposition in heaven. God himself does not want opposition – that is why he chased Satan away. Why should Kamuzu [the then president] have opposition?”(Decalo, 1992, p.10). Chinua Achebe painted the picture of the conversion process in Nigeria more succinctly as: “all argument should cease and the whole people speak with one voice and that any more dissent and argument outside the door of the shelter would subvert and bring down the whole house” (Achebe, 1967 ,p. 37). These were only to prepare the ground for what was to come. Transaction costs of opposition were to be explicitly heightened. The costs of opposition in some countries eventually became literally equivalent to the price of human life and to incur it meant to choose death in place of life. In Ethiopia opposition was met with physical elimination and liquidation (Hameso, 2002). In Ghana, the process was more dramatic and extraordinary and in the event it led to the promulgation of land laws whose concealed agenda was to crash the opposition. Paradoxically these land Acts continue to form the thrusts of land policies in Ghana. The Ghana case is peculiar and needs further elaboration.

The Ghana Case in Perspective

Nkrumah, the first Prime Minister of Ghana, devoted the first nine years of his administration to eliminating the opposition (Card, 1975). At the time of independence, the main leaders of the opposition, the professional elites, had strong family or lineage ties with the Chiefs in the Ashanti and Akim-Abuakwa communities of Ghana (Card, 1975). Chiefs were by custom political leaders of their respective communities as well as the custodians of all the land resources of their respective communities. They thus commanded great influence. Meanwhile their elevated status during the colonial era (Noronha, 1985) placed them in the position of parallel opposing political power (Bretton, 1967; Rimmer, 1992; Firmin-Sellers, 1996). Given the land resources they controlled, the lineage ties the Ashanti and Akim-Abuakwa Chiefs had with the main political opposition parties and the parallel political power they present, they represented an important obstacle to the socialist agenda of Nkrumah. Nkrumah could thus make meaningful headway only if the maneuvers of the chiefs and their allies could be quelled or at least make it too costly for them to engage in policy making or even to lend financial or other supports to other opposition organs. Nkrumah vowed to make sure that some of those who constituted the main obstacle would "runaway and leave their footwear behind" (Kasanga, 2002). Nkrumah pursued this agenda by first infiltrating customary law and practices with politics. During these periods, there were rampant destoolments (removal) of chiefs that were known sympathizers of the opposition in Ghanaian communities such as Kade, Abodom in Akim- Abuakwa (Ghana, 1959). These were followed up with legislation to remove for instance the Offinsohene (Chief of the Offinso community) to a place 30 miles radius from his state while the Gyasehene of Akim Abuakwa was banned from the state and ordered to stay 60 miles away (Ghana, 1959).

Five years ahead of the launch of Nkrumah's first Seven Year development plan and barely a year after formal independence, Nkrumah launched an arsenal of enactments aimed evidently at crashing the opposition. Amid the series of enactments to crush the opposition, ranging from the Preventive Detention Act, under which some opposition members were jailed without trial and The Sedition Act and the Criminal Act, which provided for the death penalty for political crimes without trial by jury, were two land Acts. These land Acts were the Ashanti Stool[6] Lands Acts of 1958 and the Akim Abuakwa (Stool Revenue) Act of 1958. These Acts indeed heightened the transaction costs of the chiefs and the opposition as it essentially took away the fiduciary role of the affected Chiefs over their land and thus stripped them of stool land revenue. Stool land revenue was alleged to be the main source of finance for the opposition. Such was the priority attached to these land Acts that they were enacted under certificate of urgency. The motion for the Akim Abuakwa (Stool Revenue) Act, 1958 bill presents a telling example. The then Minister for Local Government in presenting the bill to parliament for debate and enactment into law stated as follows:

> Notwithstanding anything contained in the Standing Orders of this House if by 11.45 a.m. today the motion for the second reading of the Akim Abuakwa (Stool Revenue) bill has not been disposed of Mr. Speaker do put any question necessary to dispose of it. That the Committee stage be taken immediately after the second reading; that if by 12:40 p.m. the Committee stage has not been

[6] Stools are a category of land owning communities that are made up of a number of families, clans and individuals. Not all families belong to stools and even where they do there is normally a distinction between the lands owned by the family and those owned by the stools.

> disposed of, the chairman do put any question necessary to dispose of it and report the bill forthwith; and that if by 12:50 p.m. the motion for the third reading has not been disposed of Mr. Speaker do put any question necessary to dispose of it (Ghana Parliamentary Debate, 1958).

By this time the Criminal Acts that came along as a package with these land enactments had almost made opposition equal to accepting to be jailed or even killed. Such a high transaction cost was evidently unbearable and the opposition could hardly subject the Act to any scrutiny. Such an important Act was passed by parliament in an hour and a half unexpurgated. Subsequently these Acts together with other succeeding Acts relating to Stool lands were eventually consolidated under the Administration of Lands Act, 1962. Under this new Act the principle was expanded to cover all stool lands in the country. This Act is presently termed "vesting policy" in Ghanaian parlance. The accomplishment of these vesting policies in Ghana has been phenomenal. They vest virtually all the ingredients of property rights in the affected stool lands in the government of the day for redistribution. The rights expropriated from the affected stools include the right to: (1) possess (2) use (3) manage (4) alienate (5) security of tenure (6) bequeath and (7) mortgage. Table 1 depicts the Stool lands affected by the vesting policy in Ghana so far.

Table 1: Stool Lands Vested In the Government

No.	Location	Region	Instrument	Date	Size
1	Stool Lands in Koforidua	Eastern	E.I[7].195	1/11/61	19.47 km^2
2	Stool Lands in Nkawkaw	Eastern	E.I.195	1/11/61	n/a
3	Efutu &Gomoa Ajumako Lands	Central	E.I. 206	21/11/61	n/a
4	Kumasi Part 1 Lands	Ashanti	Act 123	14/06/62	24.55 km^2
5	Winneba	Central	E.I. 83	6/6/63	I mile radius
6	Accra-Tema	Greater Accra	E.I.108	18/9/64	n/a
7	Inchaban	Western	E.I. 28	20/07/98	n/a
8	30 Stool Lands in Brong Ahafo	Brong Ahafo	E.I.46	18/2/61	n/a

Source: Field survey- compiled from the records of the Lands Commission, Ghana.

In its current form, the policy gives the government direct control over all incomes from the affected Stool lands as well as non-affected Stool lands in the country. To this extent Stools in the country have legal rights to only 22.5% of all revenue from Stool land transaction. That is to say 77.5% of gross stool land revenue (capital and or rental) is deducted at source almost as tax. In this context it is unclear the sense in which Asiama (1990; p.247) argues that the vesting policy "leaves ownership substantially in the landowner's hands".

The Act actually made government through its agencies the mangers of these affected stool lands and empowered it to allocate these lands to potential developers without reference to the expropriated owners and at the discretion of the officials in charge. These lands are allocated on leasehold basis at about 90% rental subsidy. Thus, as a bi-product of this Act it made it possible for benefits by way of land allocation to be concentrated on the privileged few beneficiaries of the allocated lands at the expense of the expropriated owner and a larger segment of the non-benefiting Ghanaian taxpayer. It is now well established in the literature that the main

[7] Executive Instruments or subsidiary legislation

[8] The affected stool lands include: (1) dormaa (2) Nsoatre (3) Sunyani s (4) Fiapre (5) Odumasi No. 1 (6) Awua Dumasi (7) Acherensua (8) Hwidiem (9) Kenyasi (1 & 2) (10) Ntrotroso/Gyedu Wamahinso (11) Mehami (12) Goaso (13) Kukuom (14) Mim (15) Kasapin (16) Akrodie (17) Sankore (18) Ayomso (19) Pomaakrom (20) Seikwa (21) Nchiraa (22) Manji (23) Bredi (24) Branam (25) Subinso (26) Nsawkaw (27) Offuman (28) Tanoboasi (29) Booyam (30) Techiman.

beneficiaries of lands under these policies are the top civil servants and influential figures in Ghanaian society (Asiama, 1990; Antwi, 2000). To underscore the full repercussions of this Act thus it is pertinent that the costs imposed on landowners and the taxpayers as well as the benefits from the management of the revenue and the allocation of these lands are ascertained.

Nkrumah's particular interest in crushing the Chiefs to gain exclusive control over policy making has led to these policies that discriminate against Stools as opposed to family, clan and individual land owners, imposing costs on them. Apart from regulating their incomes, Nkrumah enacted policies that subjected Stool land transactions only to government surveillance and scrutiny. This regulative policy is referred to in Ghana commonly as "Concurrence policy" which was fashioned along the lines of the recommendations of the West African Lands Committee (see footnote 1). This can be explained in the light of the reasons for enacting the vesting policies against the Stools. The concurrence policy has now been given constitutional assent in Article 267(3) of the 1992 constitution though with somewhat different slant towards land use planning.

By this time, the costs of opposition had been made practically unbearable and real opposition had vanished from the scene (Card, 1975). Nkrumah thus could now pursue the socialist's agenda, which as mentioned was itself motivated by the need for self-aggrandizement (Card, 1975; Killick, 1978). An important land policy that underpins socialism is the policy that gives unhindered access to land (Buchannan, 1999). The colonial policies on expropriation was adequate as it had enough safeguards against abuse of government powers in compulsory acquisitions and unfairness in the acquisition process by insisting that all government acquisition must receive certification by the courts. This however was too constraining for the Nkrumah regime as it made arbitrary use of power in the manner envisaged under Nkrumah's socialist agenda practically impossible. This meant the transaction costs of implementing socialism in Ghana by the one-party regime would have been high, entailing the payment of compensation for every piece of land required for socialist production and development agenda or risk hostilities and revolts from the populace. The conundrum that such high transaction costs presented was made explicit in the speech by Nkrumah in launching the seven-year development plan (1963-70). Nkrumah notes:

> …the state will be controlling on behalf of the community the dominant share of the economy. This would have been accomplished without ever having to resort to such expedients as nationalisation, which if carried out with full compensation would only change the ownership of the means of production…and if carried out without such compensation would inevitably incur such a large measure of hostility as to make our development plans very much more difficult to achieve (quoted from Larbi, 1995: 42).

With the costs of overt nationalization clearly unbearable to the government a clever and subtle approach to nationalization had to be found if socialism was to succeed. This meant that a new law was required that offered reduced transaction costs in state land acquisition. The State Lands Act, (Act, 125) of 1962[9], was thus passed. The memorandum to this Act betrays the true intents of this policy. It established that:

> The bill dispenses with the need to obtain a certificate from a court to effect vesting of land in the republic, and provides that a declaration by the president shall constitute the vesting instrument.

Though this Act did not specifically exempt the state from compensation payments, the requirement for compensation payment under the law has been so spuriously contrived to make compulsory acquisition without compensation legally possible. Under this policy it became possible to divorce compulsory acquisition from compensation in such a way that it was possible

[9] Other expropriation laws such as The Lands (Statutory wayleaves) Act, (Act, 186) of 1963 and the Public Conveyancing Act, (Act, 302) of 1965 were also enacted by the regime along similar lines though they have been used infrequently as compared to the State Lands Act.

for government to acquire land and use immediately and pay the compensation at a time of their choosing. Apart from the lack of interest payment on delayed compensation payments (a serious problem in a country where inflation and poverty are endemic) it has been possible under this Act for the government to embargo compensation payments altogether since 1973 (Larbi, 1995). Thus while all expropriation under the colonial policies were paid for, there is a huge domestic debt arising out of unpaid compensation. The actual size of the debt remains unknown but believed to be in the hundreds of millions of dollars (see Hatch, 2001).

Thus during the era of single party political economy, the regulatory and distributive policies started by the colonial autocratic state became widened and strengthened even in countries where due to local oppositions the colonial governments took a more cautious approach to land policy. The policies have also established a culture in which the distribution of vital resources including land during this era became the preserve of the dictatorial regime through coercion rather than consensus (Hameso, 2002). Thus with soaring transaction costs of opposing looming large in the sub-Saharan African policy process, the policies that emerged during this era, as insights from public choice show, were those likely to serve the parochial interest of their originators at the expense of the wider society. What is more disquieting is the policies enacted during this era have proved immutable and they continue to dictate real estate market proceedings in these sub-Saharan Africa countries. Nonetheless a more far reaching consequence of these political regimes is the insurrections and military takeovers that they engendered.

Military Regimes

Events of the single party regimes engendered much anxiety among citizens who had anticipated welfare gains from the achievement of independence (Sender and Smith, 1986). If transaction costs were low, political opposition and pressure groups with the right incentives would emerge to present alternatives and compete for power. This would lead to a change of government at the next elections or even a vote of no-confidence. However, in most of these countries transaction costs of doing so were made almost unbearable and when this culminated essentially in the criminalization of opposition, it was impossible for such a process to emerge. What followed was predictable. If frustration, dissatisfaction, and grievances are sufficiently prolonged or sharply felt, aggression is quite likely, if not certain to occur (Gurr, 1993; 2003). This may have instigated a spate of military takeovers on the continent. Thus a culture of transfer of political power by force in the form of military coups, brutalities, warfare, insurrections, mutinies, severe riots and significant political assassinations (Zolberg, 1968) became the least expensive option. Such was the spate of forced power transfers in Africa under this era that between 1960 and 1985, there were one hundred and thirty one attempted coup d'etats in Africa of which sixty were successful and three countries experienced six successful military coups (Bratton and de Walle, 1994).

Out of the fifty-four independent African countries, only six have not experienced attempted or successful coups since independence (Bratton and de Walle, 1994). By 1970, half of the independent African countries (all of which stated as multiparty democracies) had military governments installed through military coup d'etat (Bratton and de Walle, 1994). The costs of opposition in these regimes became even more unbearable than under the two earlier models: colonial and single party regimes, discussed above. As Chauveau (1997) noted in the case of Ivory Coast, the state could choose at any time to invoke its overreaching rights and did not hesitate to enforce its wishes with threats of prison if necessary when it was challenged.

Policies thus became what the sovereign desired and not necessarily what was good for the country. Like the previous autocratic regimes, the land policies enacted took two main forms: (a) those that gave the government of the day the right to redistribute land resources by taking landownership away from indigenous owners and (b) those that regulated free trade of real estate commodities. An example of (a) is the case of Nigeria, where, like Ghana the colonial government could not confiscate land in view of opposition, the then military regime successfully enacted the Land Use decree of 1978, which was subsequently incorporated in the Constitution of 1979 and 1999 respectively of Nigeria. The decree required certificates of occupancy to be obtained from the government for land held under customary and statutory rights and the payment of rent to the government. In another case, one of the results of the Ethiopian Revolution was nationalization of all urban lands without compensation under the Government Ownership of Urban Land and Extra Houses Proclamation (No. 47 of 1975) (see Asiama, 1990, p.242). In addition, in countries like Ghana, at the time of the military intervention policies existed and continue to exist giving the government virtually free right to bring any land in the country under their control for redistribution. Many more lands were thus confiscated under these policies. By the end of these military interventions twenty out of the forty countries in sub-Saharan Africa had nationalized lands and vested in the respective governments the power to redistribute these lands (Mabungunje, 1989). These policies were passed without much opposition due to the soaring costs of opposition.

Though much of the regulatory land policies enacted under the previous regimes remained in force, some regimes enacted more. For instance one of the fundamental outcomes of the 1966 military interventions in Ghana by the National Liberation Council (NLC) was the promulgation for the first time in the country of a regulative land policy that discriminated against foreigners. The policy, which has now been given constitutional backing under Article 266 of the 1992 constitution of Ghana, restricted the length of time foreigners could own land in the country to fifty years. This policy came as part of a range of discriminatory policies by the regime, which proscribed foreign investors from engaging in business activities such as, retail and wholesale trade below a certain turnover, taxi and trucking services, produce brokerage, baking, printing and the manufacture of cement blocks (Card, 1975). The motive behind this policy appears to have been to prevent foreign competition in particular areas of the economy as a way of propping up local entrepreneurs to take up the running of the economy and to safeguard the country against piecemeal colonization. Yet it imposed significant restrictions on the rights of landowners in the country to free trade. Also during the 1981-1992 military intervention led by Ft Lt Rawlings in Ghana, the right of chiefs to grant freehold rights in land even to usufruct owners who want documentary evidence of their holding was taken away by the government under article 265 of the 1992 constitution of Ghana. These laws significantly attenuated the rights of indigenous land owners and festered poverty.

Emergent Democratic Regimes

After a long period of monopolized policy process and high costs of opposition, there was from 1985 a general trend towards democratization of the policy process in sub-Saharan Africa. It was envisaged by the proponents of democracy for Africa, namely the World Bank and other international development agencies that such a policy process would entail much lower transaction costs and formidable opposition would emerge to provide a check on the arbitrary use of government power over the years. In truth if this happens one expects that real estate policies will move towards redressing true market failures and excessive transaction costs. Inefficient policies would also be recalled to pave the way for the efficient functioning of real estate market. Thus understandably the move was greeted with great optimism. Nzongola-Ntalaja (1997, p.9) writes:

> Since 1988, the people of Africa have risen to replace one-party and military dictatorships with multi-party democracy. From its violent outbreak in October 1985, in the street of Algiers, this new social movement for democracy has manifested itself all over the continent, changing the rules of the political game and bringing about meaningful reforms in the institutions of the post-colonial state.

After more than a decade of experimenting with democracy in Africa, very little improvement has been achieved particularly in the real estate policy environment. Many autocratic policies enacted to crush opposition by imposing restraints have now received constitutional backings. Large state institutions and bureaucracies have been established with full complement of staff and annual budgets to enforce what were ad-hoc measures to raise transaction costs of political opposition.

The question is why has democracy failed to achieve any meaningful outcome as envisaged? Some argue multiparty politics is not the best fit for Africa where socio-political structures and potent identification are more of ethnicity and less of classes (Hameso, 2002). Others dismiss this idea as unfounded as African culture admits of consensus building in decision making. Employing insights of the discussions above it would appear democracy has failed to yield a better outcome because transaction costs of organizing and maintaining viable opposition still remain high in most African countries despite the installation of democracy in these countries. Most of these so-called democracies are thus operating essentially without practical opposition. This has led to the emergence of despotism in democratic systems. Virtually all the then military regimes in countries such as Gambia, Guinea Bissau until the downfall of Nino Viera, Guinea Conakry, Burkina Faso, Niger under Maina Sara, Chad, Togo, Ghana, Egypt, Libya, Mauritania, Sudan and Madagascar metamorphosed quickly to become civilian governments (N'Diaye, 2000). Those gaining monopolist control over the political system through civil wars and mutiny as in Liberia, Ethiopia, Uganda, Mozambique, Angola and Zimbabwe managed to get elected as democratic leaders. Yet these leaders openly declared their discomfort with democracy as a decision making process. Many governments have locked in on power and do anything to remain in power.

It was logical to expect these leaders to find a way, if possible, to circumvent transaction costs for themselves and to maintain a high transaction costs structure for the opposing forces. These leaders had one important opportunity to accomplish that. Being the “last” autocratic regimes, the onus of drafting new constitutions for the incoming democracies was on them. This offered them the opportunity to set the “rules of the game”. Many of them took advantage of this opportunity and entrenched the policies that heightened the transaction costs of the opposing forces into the new national constitutions. In Ghana for instance all the previously enacted land Acts to crush the opposition, namely the vesting policy, and the concurrence policy together with socialist-motivated policies found their way into the national constitution. The Nigerian Land Use Act of 1978 enacted by the military regime to nationalize all lands in the country also found its way into the 1999 Nigerian constitution. Casting these policies in national constitutions meant the opposition and subsequent administration had huge transaction costs to confront if they wished to reform these policies.

Though democracies in Africa bear substantial traits of democratic systems as known in theory (see Dahl, 1989; Przeworski, 1991; Valenzuela, 1992), very little practical changes have occurred in land and real estate policies. The new additions to land policies during this era is the spate of land redistribution programs initiated in southern African and some eastern African countries to confer on the state power to redistribute land resources with a view to reducing inequities in landownership (Quan, 2000). Substantively however, land and real estate policies have remained largely the same as under previous despotic regimes. Government retains a large measure of power to redistribute land resources and regulate activities of land market participants.

The policy processes of sub-Saharan Africa out of which real estate policies have emerged are invariably monopolized by incumbent political forces. It remains to be understood the actual social costs that such a monopolized policy process could be imposing on society.

THE IMPLICATIONS

What emerges from the forgoing is land policies in Ghana and sub-Saharan Africa in general have evolved from a dictatorial policy environment. Many of the policies enacted entrusted the allocation of land resources in the hands of the incumbent who according to public choice theorists are self-interest maximizers. Accordingly access to these lands generally has not been dictated purely by efficient economic considerations but by the pursuit of the parochial interest of those in charge. As Rimmer cited by Killick (1978, p.51) illustrates, the concern of the administration was “the enrichment of the government itself, (i.e. the ruler, of Ministers, of party leaders, of top civil servants, and possibly of numerous subordinate ranks of the public)”. Thus access to these lands has tended to be heavily lopsided in favor of those who control the government in various ways rather than to those who are in real need. Yet in sub-Saharan Africa efficient and equitable access to land represents an important plank in the quest for poverty alleviation. This is because a significant proportion of incomes are derived from agricultural activities. Thus efficient and equitable access to land relates powerfully to the ability of the majority of the population of these countries to generate income, construct meaningful livelihood patterns for themselves and ultimately lift themselves out of poverty. Until this pattern of skewed access to land is corrected the potential for poverty alleviation will remain significantly atrophied.

What is disquieting is these land policies are difficult to reverse. These policies materialized because the transaction costs associated with their subversion was too high. Yet, since they offer the monopolist policy actor maximized utility, the monopolist has greater incentive to retain the policy than to do otherwise. When the monopolist regime that enacted those policies is removed and replaced by another monopolist policy actor, these policies are likely to become convenient tools with which the new actor can maximize its utility since it has a similar incentive structure. They are thus unlikely to recall such policies. In fact, if at the time of their assumption of office the benefits that are offered under those policies have been depleted by the previous regime, they are more likely to widen the remit of the policies or even pass new but similar laws so that more benefits can be obtained.

Even when monopolist regimes are replaced by regimes mindful of the economy that wishes to reform these laws for better economic gains, it may not be that easy because of huge associated transaction costs. The relevant transaction costs in this case comprise the costs of providing information to convince the general populace of the need for the reform, the costs of seeking agreement on the way forward and more importantly the costs of convincing and seeking the consent of the existing body of beneficiaries some of which may be the clients of the incumbent, to consent to the reform of the policies. This existing body of beneficiaries includes politicians, bureaucrats, interest groups, clients, the influential and powerful in society among others. It is likely that such consent may not be forthcoming leading to the possible continuous existence of inefficient policies even in “democratic” systems.

CONCLUSION

Having examined how these political processes have shaped land policies in Africa it is clear there is a need for a more radical approach to poverty alleviation. Perhaps, one such way would be for international development agencies involved in poverty alleviation in Africa to make the enactment of rational land policies that guarantee efficient and equitable access to land and the abatement of transaction costs a condition for any donor supports to these countries.

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Understanding Global Capitalism: Passive Revolution and Double Movement In the Era of Globalization

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Abstract

This paper attempts to provide a framework for understanding the way globalization has reshaped the terrain and parameters of social, economic and political relations both at the national and global levels, and exerted pressure on the resiliency capacities of capitalism. It proposes to examine the ways social relations of domination and subordination are produced, reproduced and maintained while continuously undergoing transformations. Through conceptualizing the evolution of the capitalist world order in a historical perspective and by exploring the changes of relations brought about by the intensification of globalization since the 1990s, the objective is to generate a perspective for understanding such a process based on the application of Gramscian and Polanyian theoretical and analytical categories. The conclusion aims to convey that the process is contingent on both structures and agencies and it also produces the opposite result: i.e. reducing the legitimacy of capitalism's hegemony and especially limiting its resilient capacities.

JEL Classification Codes: F59, P16

Key Words: globalization, capitalism, hegemony, passive revolution, double movement

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INTRODUCTION

Hegemony and passive revolution

The phenomenon whereby capitalist class societies are able to adapt to changes while retaining their essential features of organization and mode of functioning raises important research issues for political and social sciences as well as for social movements. However, to paraphrase a Marxian axiom, if appearance reflected the true nature of a phenomenon, there would be no need for scientific investigation. Applied to the analysis of present-day capitalism, the task at hand is to understand and explain the mechanisms of motion of this socio-economic system – at the national and international levels – as well as the apparent adaptability and limitations of the ruling classes to respond to challenges to their rule without changing the essence and structure of society. In this respect the concepts and methods developed by political and historical sociology have heuristic explanatory and pedagogical value in the context of national society and the international system.

A point that has to be kept in mind is that while the structuralist framework of Marxism[10] is crucial in understanding and defining crisis at the socio-economic level, critics claim that there is a deficiency with regard to the politics of crisis resolution. The apparent dichotomy between structure and agency has thus to be resolved in order to comprehend the dynamism of the capitalist phenomenon. Although the systemic structures of capitalism are important, structuralism does not open up for understanding the variety of capitalist societies (democracy, authoritarianism, and dictatorship) nor for comprehending social change. The need for inclusion of polities, understood as the interaction of social actors and agencies with the societal structures, is decisive for understanding the resilient dynamism of capitalism.

The notion of passive revolution is derived from the conservative tradition going back to Edmund Burke, who argued, that in order to preserve its most essential features, society had to adjust to changes (Sassoon, 1982, p. 15). In modern settings, the concept was further developed by Gramsci, who used it to refer to a style of state politics that preserves control by a leading group on the one hand while instituting economic, social, political and ideological changes on the other. In other words, the concept encapsulates the means by which a dominant class maintains its hegemony by neutralizing the pressures of various contending forces that might otherwise trigger profound structural transformations. Consequently, the defusing process is achieved without undergoing a political revolution that potentially could threaten the dominance of the leading group and the “modus operandi” of the system. It is in this context that the concept of hegemony should be understood as an expression of broadly based consent, manifested in the acceptance of ideas and supported by material resources and institutions.

The incorporation of passive revolution into the conceptualization of the evolution of modern capitalist societies offers, according to the Gramscian perspective, an explanation as to how bourgeois democracy is able to contain the contradictions of the mode of production, upon which class dominance depends, without resorting to open violent coercion. The class struggle that is a component of capitalist formations is characterized by Gramsci as a “war of position”[11]. The point to keep in mind is that Gramsci (1971, p. 106-20) recognized that wars have two sides. Thus he considered “passive revolution” in the context of “war of position” by other means, as a “revolution from above – that sidesteps the need for fundamental restructuring from below.”(Mittelman, 2000, p. 167n.)

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[10] Structural Marxism refers to the view that in capitalist societies, actors are seen as largely constrained by the key societal structures - economy, polity, ideology. These structural forces are seen as having the power of independent influences in the evolution of societies. However, the economy is eventually seen as obtaining the most determinant power in the last instance. In other words, the economic foundation determines the superstructure.

[11] It is a concept used by Gramsci referring to the long period of struggles in which a subordinate class is able to become the hegemonic force by undermining the ideas and values of the ruling classes and initiating a new national-popular collective will under a broad unification of various social forces and groups. It is to be distinguished from what he called “war of maneuver”, i.e. a direct, violent and immediate assault on the state (see Gramsci 1971).

In other words, the hegemony of the bourgeoisie is identified as "political consent…whereby extra-economic modes of domination serve to enforce a 'dominant ideology' favorable to the reproduction of capitalist relations of production" (Martin, 1997, p. 51). At times of potential confrontations, the bourgeoisie has shown a capacity to go beyond narrow immediate short-term interests by making compromises (within certain limits) with a variety of allies, united in a coalition of social forces called *historical bloc* (Gramsci, 1971). In this way, the societal order, which the bourgeois ruling class has created and nurtured through a web of institutions, social relations and ideas, represents a basis of consent (Bottomore, 1983: 201).

While Gramsci ascribed the willingness of the bourgeoisie to accept socio-political and economic reforms to the modalities of its rule, Karl Polanyi looked at the dysfunction of the interdependency between society and market as the reason for the unleashing of tensions that are latent in the relationship. The constant attempt by the capitalist class to escape from the control of the state and society encapsulated in the endeavor to shift the balance in the "war of position" in its favor by imposing a "self-regulating market" leads to a political reaction that seeks to protect society from this utopian project. Thus in the Polanyian interpretation of the history of industrial capitalism, two movements are discerned. The one is the liberation of the market from political and social control, i.e., the "disembedding" of the economy. The other being the second phase of the "double movement" with the re-imposition of political supervision and control of the market in order to safeguard the interests of society (Polanyi, [1944]1957).

Thus while not abandoning the structural analytical level, the attempt is made in the thrust of these two approaches – Gramsci and Polanyi - to surmount the dichotomy between structure and agency and emphasize the role of politics in the evolution of capitalism. The combination of both insights is useful to the analysis of the turmoil of the 20th century with its alternation of revolution and counterrevolution, reform and contra-reform as well as war and peace. Following the Great Depression, capitalism worldwide underwent a transformation based on the rejection of laissez-faire capitalism in favor of a more regulated macro-economic system of controlled and rationalized production. This process can be identified as a "passive revolution" which found expression in the reorganization of capitalism in the 1930s and the postwar era through the adoption of the New Deal, Keynesianism and Fordism[12] in the United States and Western Europe. A motivating influence on the ruling elites was that the "war of position" was not going well as capitalism experienced a protracted crisis following World War I and the victory of socialist forces in the Russian "war of movement" following the Bolshevik revolution in 1917. The establishment of the Soviet Union put socialism as a viable alternative socio-economic system on the agenda even though a revolutionary wave was defeated thereafter in parts of Central and Eastern Europe.

While some countries reacted to the crises and potential revolutions in the first half of the 20th century through socio-economic measures whereby preserving parliamentary democracy, the political elites of catching-up countries such as Germany, Italy and Japan resorted to Nazism and Fascism characterized by ultra-nationalism, militarism and contra-imperialism. Nonetheless, the common denominator for the reaction of all industrialized countries to the worldwide crisis of capitalism can be grasped in Polanyi's "double movement", i.e., the attempt to shield societies from the ravages of the world market and pre-empt the consummation of the "war of movement" into revolutions and class wars through retrenchment from the international economy and the implementation of protectionism and self-centered economic policies.

Not to be discounted however is that notwithstanding the differences between the strategies for overcoming the general crisis, it was the "creative destruction" (Schumpeter, 1975) of the Second World War that gave capitalism a new impetus. In the post-war period of reconstruction, the ruling

[12] The New Deal is the term given to the series of reform programs implemented between 1933-37 under President Franklin D. Roosevelt aiming to relieve, recover and reform the US economy affected by the Great Depression. Keynesianism refers to the economic policies in the post-war era initiated by western industrial countries that promote a mixed economy and the role of the state in creating demand and economic growth. Fordism refers to a mode of production – social institutions of mass production - aiming at mass consumption combined with mass production to produce sustained economic growth and material advancement; it is regarded as part of macro economic regulations related to Keynesianism.

classes of Western democracies accepted structural regulations and modifications in the economy's mode of functioning in order to defuse social contradictions and neutralize political mobilization and thus re-legitimize its rule. Seen in this light, the "compromise" involved a trade-off: the establishment of a general consensus with regard to maintaining the existing class stratification. Politically, social consent has since come to be regarded as a component of the system of democratic institutions and liberal ideology whereby the general interests of the population were to a larger extent taken into consideration by the state. This give-and-take strategy was functional to the stability of the social structure. Simultaneously, non-state or semi-state institutions such as education, the media and the church exerted a significant impact on people's consciousness in influencing their ways of living thus contributing to the maintenance of the position and legitimacy of the capitalist ruling class. This pattern of social control, which was part of a truce in the ongoing "war of position" in the post-World War II arrangements, revealed the potency embedded in bourgeois political hegemony. Its skilful competence in winning the "rule of legitimation" through the manufacturing of "false consciousness" (Gramsci, 1971) resulted in the acceptance of the perception of the capitalist political and economic system and social structures as inherently rational and natural.

In other words, the ruling elites were able to depoliticize social conflicts or issues of contention with "a 'prepolitical' process that constructs the public agenda and thus predisposes 'politics' to a narrowed set of choices" (Ross and Trachte, 1990, p. 9). It should be kept in mind that the climate created by the Cold War was not conducive to the formation of a counter ideological hegemony. This political evolution however was preconditioned on an economy characterized by a high degree of employment and social security and consumerism.

Objective and analytical frameworks

As a continuation of the authors' previous researches on the evolution and contradiction of capitalism (Li, 2002; Li and Hersh, 2002; 2004), the intention of this present paper is to apply the Gramsci's extended conceptual and analytical apparatus (hegemony, civil society and historical bloc) in combination with the analytical notions of Karl Polanyi concerning the dialectics of market-society relations to explicate our thesis of globalization's counter-productive effect on the hegemony of the capitalist system:

a) The disproportionate power of transnational capital expressed in its lopsided mobility decreases the "consent basis of hegemony" by having a negative impact on the system's resilient capacities. This transformation is also connected with the post-Cold War geopolitical changes and with the rise of transnational neoliberalism based on the Washington Consensus;
b) Globalization has reshaped the terrain and parameters of social, economic and political relations both at the national and the global levels. Consequently, the relative decline of states' intervention capability and policy-making sovereignty in balancing and neutralizing contradictions reduces the capitalist system's "social basis of hegemony". The system's passive revolution capacity is substantially weakened due to the lack of an *organic* global civil society as a consent-generating mechanism.
c) Globalization is creating a double contradiction on market-society relations: on the one hand it is reawakening the forces for the second phase of the "double movement" in the form of needed self-protective measures in the effort to re-embed the economy, on the other hand, the attempts at regulating the market partakes a serious impact on the welfare and interests of the core powers of the existing international system and of individual societies and people. This contradiction is due to the nature of an established market economy where society is already historically shaped and patterned in such a manner that society is structured to function according to market laws (Polanyi, 1957: 57).

Our analytical frameworks, on which the paper's discussion process is based, proposes an analysis of present-day contradictions in the world structure as related to the questions of legitimacy, hegemony and the embeddedness/disembeddedness[13] of the economy from the following perspectives:

1) At the global level, the historical expansion and legitimization of the capitalist system materialized not exclusively through the productive and technological driving forces but also as the result of the political and military imposition of capitalism on extra-European areas as during colonialism. The present capitalist world order has been primarily maintained under American "hegemonic stability" (*coercion* based on geopolitical and material necessity) in combination with a Cold-War ideological "historical bloc" (*consent* on the basis of anti-communism commonality). The end of the contest between socialism and capitalism together with the rise of US unilateralism and militarism symbolizes the strengthening of coercive realism and the weakening of the consent-based hegemony. American selective international institutionalism (the emphasis on the WTO and the rules of game) in the aftermath of the post-Cold War is part of a strategy aiming at developing international rule-making institutions in order to make all states share the burdens (public goods) of regulating international relations without sacrificing America's own political and military dominance.
2) The intensification of globalization of national economies (market, production and finance) is challenging the foundations of hegemony at the level of nation-state capitalism. On the other hand, it is problematic to discern at the global level a similar scale of integration of state (political society with the key concerns on domestic politics) and civil society ("common sense" in connection with culture and religion). In other words, global capitalism does not really constitute *in organic substance* a "global state" vis-à-vis a necessary counterpart in the form of a "global civil society" which could represent the social basis of hegemony (Germain and Kenny, 1998, p. 15-16).
3) Economic globalization through increased functional integration of markets has promoted a tangible historical bloc of global capital/elite classes as well as less-organically founded global civil societies; this makes it difficult to envisage the Polanyian "double movement", i.e. civil societies responding to the alienation and repression of the market, since both states (a tool promoting economic globalization) and global civil societies in their diversified forms are currently being pulled apart in various directions. On the one hand, states are becoming committed to the internationalization of economic activities (production and finance), while on the other hand, they are organically tied to national structures through a wide range of functions and provisions, not least welfare.
4) Moreover, many "resistance movements" (the second movement of the double movement) found in the self-proclaimed global civil societies are not more than *conjunctural responses* to immediate effect of maldevelopment (poverty, environment, terrorism, etc.) or to general principles of common concern (democracy and human rights, etc.) without any *organic foundation* in having concrete influence in both state politics and market mechanism.

In summary, we maintain that Washington Consensus-based globalization in the short run serves the interest of capital but not of the capitalist system in the long run. The argument is based on the recognition that capital is given excessive power in creating a one-directional relationship in which hegemony becomes ever more defined by the transnational capital class on its own terms and then imposed on the rest of the system. As a consequence, capitalism is bound to loose its resilient capacities and unleash self-destructive tendencies leading to dislocation and disintegration. This notwithstanding, any successful "double movement" against the ravages of neoliberalism remains embryonic due to the contradictory nature of the relationship between *market economy* and *market society* in which the market pattern and logic remains at the heart of

[13] Embeddedment and disembeddedment is connected with the Polanyian notion of "society with market" and "market society". Society-with-market indicates that economic relations (actors and institutions) are separated from non-economic relations. A market society implies that society itself has become an "adjunct" of the market and market relations are embedded in social relations.

the social organization; this means returning to our original query regarding the fate of passive revolution at the age of global capitalism.

US HEGEMONY AND THE POST-WORLD WAR II ORDER

Defending the capitalist world system

In order to situate globalization as part of the world historical process, one has to take into consideration the vital role of the United States since the Second World War in the attempt to save world capitalism from its own demons and potential menaces while maintaining the interests of the American ruling elite.

The international context facing capitalism in the post-World War II period could be described as critical, that is, characterized by danger but also by opportunity. The menaces to the system - perceived or real - were socio-political and economic as well as geopolitical. Having come out of the conflict stronger than any other core country, the US ruling elite had to come to terms with the task of reestablishing viability to the international system – as a single entity – in order to guarantee the interest of American capitalism. The pre-war contradictions within and between the imperialist powers had to be dealt with in the post-war years. Not only were domestic societies facing the challenge of achieving stability through the implementation of "passive revolution" and the second phase of the "double movement" but the international system had to resolve the inherent contradictions of the inter- imperialist structure.

The Second World War ended with the legitimacy of capitalism as a socio-economic system reaching the lowest level. The capitalist ideological hegemony was on the defensive. The different units of national capitalism faced the wrath of the general populations and working classes whose point of reference was located in the first half of the 20th century including World War I, the breakdown of capitalism in Russia and the Bolshevik revolution, the Great Depression, the threat of Nazism and Fascism, and the Second World War. In the immediate post-World War II context there was a current of substantial sympathy for the Soviet Union in both Europe and the colonial world for the contribution of the USSR in the defeat of Nazism, its mitigated support for the national liberation movements and its role-model of non-capitalist development. As far as the colonial world was concerned, its struggle for independence from the capitalist metropoles threatened especially the interests of European countries.

The division of the world into two major blocs soon after the Second World War was conducive to establishing the United States as undisputed leader of the capitalist camp. In order to rescue a weakened capitalism worldwide and counterbalance the challenges from anti-systemic movements, the United Stated took on the responsibility of sustaining the necessary conditions for producing and reproducing capitalism's political and economic order by extending its responsibilities beyond its own territory. The calculated altruism of the US in unilaterally embracing a broad unification of various global forces under the general consent of mutual interest in preserving the functioning of the capitalist world system can be interpreted thorough the prism of a *war of position*.

Since the United States emerged as the dominant political, economic and military power in the international capitalist system, Washington thus played a significant part in structuring post-war world development. For economic and political reasons the American elite committed itself to the revival of a liberal world economy based on an international division of labor, resource and market access that benefited itself and its allies, and to the promotion of the independence of colonies – in opposition to the traditional colonial powers – except where national liberation movements were under socialist leadership. The role played by the United States was identified by the Realist School as "hegemonic stability", i.e. providing the "public goods" in order to maintain the global capitalist system. As an apparent benign hegemon, the American strategy during this period is said to have been based on *structural leadership*, i.e. "the ability to direct the overall shape of world political order" on the basis of resources, capital, technology, military force and economic power (Ikenberry, 1996, p. 389).

A major difference exists in the interpretation of the new structure that arose during this period that delineates problem-solving theory from critical approaches. While Neorealist "hegemonic stability theory" (HST) held the position that an open liberal world economy requires the existence of a dominant political and military power, the Neo-Gramscian perspective broadens the concept of hegemony beyond state dominance to that of a more comprehensive consensual order without however disregarding the importance of leadership (Bieler and Morton, 2003)

Besides the confrontation with the socialist camp that contributed to the global acceptance of US leadership of the "free world" in promoting the restoration of capitalist ideological hegemony under restructured historical blocs - including anti-communist social democratic parties and labor unions - the sustained dominance of the United States required a development strategy for capitalist societies that could re-legitimize national capitalisms while establishing a pattern of international capital accumulation that would facilitate a dominant position for American capitalism.

The significance of a capitalist model of economic activities is that it should encompass the interests of the leading elites also vis-à-vis their working classes. Recognition of the importance of the new structure of production is necessary to comprehend the saliency of the ideological hegemony that was thus able to take root. As Peter Gowan put it:

> A development path is not just about economics. It is also about politics. Capitalist classes must be confident that they have a secure path towards their own enrichment-an effective way of extracting value out of production activity. They must also have a path to the strengthening of the political authority of their state over their populations: economics and politics must combine in what is at bottom an overall social power strategy of development. (Gowan, 2003, p. 34)

Having been sheltered from the war destruction that befell the other advanced industrial nations, American capitalism found itself in an unprecedented position - not only because of its economic resources - it became the bearer of a dynamic type of productive industrial capitalism as well. The traditional form of capitalist surplus value creation had been based on limited internal market and oriented toward exporting the products of advanced industries to foreign markets. This "beggar-thy-neighbor" strategy in the 1930s was an important cause behind the breakdown of the world economy leading to the depression and World War II. In contrast to this pattern, the Fordist type of capitalism pioneered in the United States perceived the advantage for capital accumulation of turning industrial workers into consumers of mass production in national capitalism. Juxtaposing the Fordist pattern – including American modern technologies and capital export – to the general socio-economic and political context of the core capitalist centers characterized by strong labor movements and Keynesian economics based on a degree of class compromise made "passive revolution" possible. The deepening of domestic product markets reduced for a time the pressures of absorption between the core centers (ibid., p. 34).

In Polanyian terms this period could be analyzed as the return of the "double movement" after the era of market liberalization during the first part of the inter-war period. The important issue was to find a countervailing strategy whereby the erosion of social structures was to be stopped through redistribution of the national product in order to provide the necessary social protection to the populations of advanced capitalist societies. As a Swedish political economist puts it: "Thus, modern industrial societies were typically distinguished by a market-redistribution mix" (Hettne, 1995, p. 5). Consequently the post-World War II decades can be conceptualized as a period of, on the one hand, the consolidation of national capitalisms through the Gramscian "passive revolution" and the Polanyian "double movement", and on the other hand, the stabilization of international capitalism through the consolidation of the United States as the hegemon of the world capitalist system.

Based on the marriage of economic liberalism and political realism, the theory of hegemonic stability is premised on the creation and distribution of the public goods. Perceiving states as interest maximizers, realists argue that under normal circumstances, an individual state does not have the incentives to contribute to the public goods because the gains from free-riding outweigh the rewards of cooperation, and the costs of being ridden upon are greater than the benefits from autonomy. Only a hegemonic superpower with sufficient political and economic resources assisted by a military capability is able to provide or induce others to contribute their share to the international common goods, such as "free trade, peace and security, or at least a balance of powers and a sound system of international payments" (Balaam & Veseth, 1996, p. 51). In this context, the most important function of the hegemon is to set forth and enforce the institutionalization of rules for international political and economic relations with a built-in bias in favor of the hegemon as well as securing the continuous functioning of the capitalist world system. The realist interpretations accept the importance of political and military dominance for the maintenance of a liberal world economy while the liberal (or neo-liberal institutionalist position) considers the possibility of reaching a degree of interdependence through the promotion of the self-interest of the trading states. In other words, applying the "invisible hand" of the market to the international political economy.

The post-war world order, designed and maintained by the United States, was capable of imposing discipline on the capitalist system as a whole in the name of "common interest" for all parties. Such "imposition" of hegemonic stability, however, cannot simply be regarded as a by-product of manipulation or coercion. It must also comply with a genuine ability of the leadership to transform economic dominance under a general unification of the camp of capital into political and ideological hegemony. The Bretton Wood institutions can be seen as the result of US initiatives to negotiate and establish international rules so as to prevent redistributive crises and neutralize various "anti-systemic forces"[14]. The incorporated mechanisms of these institutions were also devised to supervise the application of the system's norms (Cox, 1981, p. 145).

It is commonly recognized that following World War II, the United States fulfilled the role of the benevolent hegemon for the core countries by assuming most of the costs for maintaining the capitalist world system, but also by reaping most of the immediate benefits for the US economy and its business elite. This is an important aspect behind the concept of passive revolution. Understanding that its own prosperity was tightly bound to the operation of the global system and the success of allies and former enemies, the United States was willing to maintain the security and prosperity of partner/competitor nations. Benevolence toward a broad alliance was projected as the principal motivation behind the American role in the establishment of the Bretton Woods system, the Marshall Plan, the Korean War, the NATO, the Vietnam War, etc., while the self-serving motives were underplayed in the US hegemony stability discourse.

American post-war foreign and economic policies aimed at fostering developmentalist, authoritarian and anti-Communist states in different parts of the word. As a matter of fact, immediately after World War II and throughout the following decades, American covert and overt interventions took place in Europe, Latin America, Middle East, Asia and Africa in order to bring about "regime changes" or weaken opposition to pro-American governments (Blum, 2003). In Europe, afraid that mass poverty would eventually facilitate Communist expansion, American post-war policy used the "Marshall Aid" program to revive Western European industries with Germany as the center piece. In East Asia the central aim was basically the same: that is rebuilding the Japan-centered capitalist regional economy including South Korea and Taiwan (Hersh, 1993). Under American protection, perceived external military threats and the internal danger of the communist challenge were substantially reduced in both regions. The burden of the allied countries' military expenses was greatly lessened by the American military presence. American military bases not only protected these countries but also provided them with some economic benefits such as employment.

US hegemony and the post-Cold War world order

The challenges facing the US leadership of the world system between the post-World War II era and the end of the Cold War period were resolved in favor of the hegemon. As the political scientist Aijaz Ahmad put it:

> The three objectives for which the US fought a war of position throughout the twentieth century – the containment/disappearance of communist states, its own primacy over the other leading countries, the defeat of Third World nationalism – have been achieved. (Ahmad, 2004, p. 44)

In contrast to classical imperialist powers, full-fledged American hegemony did not show great interest for direct territorial control of other countries while at the same time keeping contradictions

[14] From the perspective of World-system analysis, communist or socialist movements and nationalist movements were regarded as anti-systemic movements (anti-capitalist forces).

with other core nations within an institutionalized political and economic stakeholder framework (Tabb, 2003, p. 27).

Now that the socialist challenge has subsided both internally and geopolitically in national capitalisms and Third World nationalisms, the intra-core relationship is once again becoming a main determinant in the analysis of international capitalism under so-called globalization. The evolution of relations between core capitalist nations has influenced both conventional methodology as well as critical theory building. Geopolitics, as the study of international relations that had been dominant until World War II, encapsulated competition between advanced nations for control of strategic territories and resources. But as a consequence of Nazi-Germany's open acknowledgement of geopolitics in its drive for "Lebensraum" as well as the parallels between the conceptual frameworks of classical geopolitical assumptions and Marxist-Leninist imperialism theories, geopolitics was replaced in the toolbox of conventional studies by the more acceptable notion of International Relations (Klare, 2003). Taking its point of departure in the bipolar world created by the Cold War, the Realist School of IR gained prominence during this period by looking at the management framework of the relations within the "free world" vis-à-vis the socialist bloc.

Within the different school of thoughts in line with Marxism, the decolonization of the Third World in the post-World War II period as well as the institutionalizing of a pattern of cooperation among core nations revived an old discussion from the first decades of the 20th century. At that time, the context of World War I seemed to confirm Lenin's imperialism thesis of competition between rival monopoly firms and states over control of territories and markets; in contrast the Kautsky vision of a higher phase of "ultra-imperialism" [1914], characterized by a form of collective exploitation of the colonial world, seemed to belong to the realm of fantasy. Inter-core relations during the inter-war period did not bring about new evidence to strengthen the Kautsky argument. However, the debate on the possibility and probability of "ultra-imperialism" regained relevancy in the analysis of both the post-World War II and post-Cold War international political economy

After 1945, US capitalism, acting in the interests of world capitalism as a whole, did establish a variant "ultra-imperialist" economic order under its hegemony through a reorganization of the capitalist world economy by creating new conditions for the continuation of capital accumulation. The coordination problem within the world system was satisfactorily resolved by "the existence of a superordinate power, capable of imposing discipline on the system as a whole, in the common interests of all parties" (Anderson, 2002, p. 20-21). Evidence showed that as long as the level of economic growth and capital surplus were maintained, a certain equilibrium between different sections of capital and between states seemed possible.

Back to the future: from ultra-imperialism to imperialism?

The post-Cold War era has not resulted in a unipolar international structure. In fact we live in a world where the notions of both Kautsky [1914] and Lenin [1916] seem appropriate to the analysis of the condition of collusion and competition between core countries and late comers as well as institutionalized "collective imperialism" in relation to the periphery. The present American political and economic strategy can be interpreted as managing global affairs on the basis of a hybrid of both analytical approaches: On the one hand, the United States "has aimed at the unified, liberalized international capitalist community Kautsky envisioned", while on the other hand, "the global role that the United States has undertaken to sustain that community is determined by a worldview very close to Lenin's (Schwarz, 1996, p. 100).

It is nevertheless paradoxical and contrary to previous periods of inter-core relations that the immediate challenge to the post-World War II arrangements was indirectly the result of the reconstruction and strengthening of the economies of Europe and Japan relative to the weakening of the American economy. Having become the largest debtor country at the same time being the biggest market in the world, the United States is dependent on foreign funds to the tune of $2.3 billion a day of current rates (Harvey, 2004, p. 74). In return, the lending countries of Europe and especially Asia are dependent on the US market for their exports; this trade-off worsens further the American trade balance without strengthening the world economy. The paradox is that it is not the outside creditors that are demanding that the US rebalance this lopsidedness, but it is the United States that takes unilateral decisions in contravening the interests of partners and allies. To a certain extent Kautsky's notion may have had some application in the analysis of inter-core relations in the post-World War II era and as a matter of fact the Europeans are still more prone to support some form of ultra-imperialism (Ibid., p. 81). Where Kautsky is perhaps proven incorrect, however, was in his expectation of equality in such an asymmetric alliance (Panitch and Gindin, 2004, p. 9). Cooperation can thus be interpreted as a temporary arrangement while contradiction is a basic constituent of inter-core relations. A war of position at the international level!

In later years, the American political class – refusing to address the structural weakness of its domestic economy – has focused on the country's comparative advantages in the form of an accessible market for foreign exporters, influence in controlling the international financial system as well as military production and power in shaping the international political system. This has affected the debate in the United States where geopolitical considerations concerning the wisdom of empire have been placed on the political agenda. Interestingly, this trend is not exclusively a characteristic of the neoconservative discourse as liberals are also in favor of a more active international role. As William Tabb sees it, the outcome of the present political evolution in the United States will have consequences for the rest of the world for years to come:

> What is actually at issue here is the choice between two U.S. imperial strategies: a hegemony geared primarily to promoting neoliberal globalization on terms particularly favorable to the United States, and an alternative hegemony that steers toward the establishment of a more formal U.S. empire. These two paths represent alternative strategies that an imperial ruling class may choose between, but in many respects they may also be complementary (Tabb, 2003, p. 77)

GLOBAL CAPITALISM AND THE RESTRUCTURING OF SOCIAL FORCES

When discussing the changes that have taken place in the internal social politics of national capitalism as well as the new tendencies in the intra-core relationship, it is necessary to look at the new developments against the backdrop of the societal and geopolitical adjustments caused by the globalization process, which is bringing about modifications to existing social, economic and political structures both nationally and internationally.

Globalization and transformations

The transformation of global capitalism denotes a conceptual difference between *internationalization* and *transnationalization* (globalization). The former refers to "the extension of trade and financial flows across national borders", whereas the latter implies that "the globalization of production has entailed the fragmentation and decentralization of complex production chains and the world-wide dispersal and functional integration of the different segments in these chains" (Robinson and Harris, 2000, p. 18-19). Globalization has brought about some fundamental conversions in the "modus operandi" of the capitalist world system in which the system's constitutive rules and regulative capacities are in the process of restructuring and generating new social constellations of actors and agencies. This process can be analyzed by looking at a number of societal relationships:

Labor relations

The situation and status of the working class has, since the industrial revolution, been related to the position of the individual country on the international scene. From its genesis, capitalism developed unevenly in different parts of the world creating a system of dominating and dominated nations. When conditions of capital mobility are geographically limited within the nation-state boundary, it is possible for organized labor to compel capital into allowing it a certain participation in societal rearrangement, and not necessarily remain in a state of passive submission. In Gramscian terms, this path of passive revolution "is 'negotiated' by unequal forces in a complex process through which the subordination and the resistance of the workers are created and recreated" (Simon, 1982, p. 64).

In the context of war of position, the exploitation of working classes in developed countries historically went hand-in-hand with the economic surplus pumped out of the peripheral nations, which led to the improvement of workers' well-being in rich nations. This contributed to weakening global working class solidarity in such a way that "labour organizations in all of the advanced capitalist countries have not only supported their own multinationals in the brutal exploitation of the economies and workers of the poor nations, they have even supported wars in which the workers of one rich nation fought against those of another" (Yates, 2000, p. 49). This has been empirically demonstrated in the case of the American hegemonic position. Modern history of the labor movement in the United States reveals that trade unions have been not only exclusionary in form but also pragmatic and selective in action. The objective of American organized labor solidarity was aimed not at conducting class struggle but at sharing benefits with business by supporting US corporations abroad and strengthening the country's foreign policy regardless of the social costs on workers in other countries (Fletcher, 2003). As a consequence, this imperialist patriotism contributed to the distortion of US trade unions' perception of globalization's impact on the deterioration of their own job opportunities, welfare and social contract as well as on their understanding of the post-9/11 anti-terrorism policies.

This implicit alliance is however coming under pressure. In the present phase of globalization, the internationalization of production and finance permits the use, or threatened use, of capital mobility and relocation of parts or phases of production to countries and regions where low wages and politically-repressed working conditions provide a greater degree of surplus extraction and exploitation. The power of financial and productive capital has thus weakened the bargaining power of trade unions both in developed and developing countries as the result of the changing structure of traditional nation-based industrial production to one being restructured on a world scale.

As a result of the mobility of capital and the global fragmentation and decentralization of accumulation processes and strategies means that class formation also appears to be less rigidly tied to territory and jurisdiction of nation-states in contrast to the traditional societal structure largely based on the dynamic interaction between national capital, workers and the state. According to one opinion, globalization is reorganizing relations to production by which "the proletariat worldwide is also in the process of transnational class formation" (Robinson and Harris, 2000, p. 18-19). Nevertheless, despite the increasing common awareness over the negative impact on jobs and working conditions in the capitalist industrialized nations, it is still questionable whether a bourgeoning transnational working class is able to transcend the limit of a "class-*in*-itself" to become a "class-*for*-itself"[15] because it has not realized the fact that

> The corporations operate only in their own interests. Sometimes these interests will coincide with those of a disadvantaged group, but only by disadvantaging another. For centuries, we have permitted ourselves to ignore the extent to which our welfare is dependent on the denial of other people's. We begin to understand the implications of the system we have created only when it turns against ourselves. (Monbiot, 2003)

A genuine global working class-*for*-itself can be realized when working classes, especially in the North, are able to grasp the initiative in the war of position, whereby workers together create a counter-hegemonic alliance in the hope of challenging the continued dominance of capital. Under the present conditions, the formation of resistance to global capitalism under a collective and shared identity of interests still has a long way to go.

The "historical bloc" of global capital

[15] Class-*in*-itself refers to the general common characteristics of being a worker in relations to the conventional classification based on production relations. Class-*for*-itself refers to the category of self-activity and self-representation, i.e. collective political identity and common struggle. The difference between them is political, i.e. while everyone works for a living, not everyone struggles against injustices embedded in work and fights for a common course.

The condition of globalization is imposing changes that affect the political constellations between the ruled and the ruling elites. This can be seen in the evolution of historical blocs which are in close connection with social movements to deal with specific historical conjunctures or solve concrete problems that have to be confronted by different social groups. In the struggle for hegemony, historical blocs form, dissolve and reform. For instance, in the current context of increasing awareness of the consequences of industrial capitalism on nature, big businesses attempted to mobilize a historical bloc around the theme of sustainable development against what it saw as a threatening counter-culture and movement organized around the powerful idea of the capitalist specificity of ecological crisis.

In the context of international capitalism, competitive capitalist interests may, at least for a time, coalesce into a relatively unified hegemonic bloc. Seen from today's perspective, the situation is perhaps more true than in Kausky's time. The breaking-down of physical barriers promoting the convergence of international capitals means that transnational companies are not only global in what they produce and sell in many parts of the world, but become conglomerates united under similar interests. Former national companies have been merging with those of other countries maintaining a relation of hierarchical dependency to the larger ones. Thus, in the view of some scholars, the transnational capitalist class (TCC) is no longer "Western" but is "global" (Sklair, 1999; 2000).

According to this interpretation, the TCC is becoming the ruling class that controls global decision-making and shapes the development agenda; in other words, a transnational capitalist *historical bloc* has been created. Such a coalition encompasses the North-South dichotomy and consists of various economic and political actors including national elites (parties, media, technocracies and policy-makers), transnational corporations, global financial institutions, and international organizations (Robinson and Harris, 2000). In the new era of corporative capitalism, local and national markets are linked together into forming a global market while national capitals have fused into transnational capital. This bloc is striving to withdraw most of the concessions previously made as a response to labor pressures as well as to socialist and other anti-systemic movements. Its hegemony is said to be so decisive that whether or not its position and ideology is agreed upon by the society as a whole becomes less important. However, what deserves particular attention with the rise of neoliberal globalization is the emergence of financial capital as an engine of capitalist accumulation.

With an estimated worth of $360 trillion (larger than the value of the entire global economy), world financial capitalism is ushering an age of complexities and instabilities (Gilpin, 2001, p. 6-7). The basic principles of finance, and related branches such as insurance, property market, stock market and public finance are not only increasingly integrating national economies into the capitalist world economy but also fundamentally changing the way economic activities are organized and operated. Contrary to conventional economic theory, financial capital, unlike productive capital, does not lead to relatively stable price formation based on a rational assessment over a number of criteria, such as management, products, marketing, or record of profitability. Rather, financial capital is highly speculative by nature and is inherently inclined to avoid the logic of equilibrium in favor of the momentum of self-fulfilling expectations as when a rising stock price attracts buyers who through these purchases further raise the price level to the point of creating a bubble. The East Asian crisis, the Mexican crisis and the Russian crisis were all indications of the grave consequences created by financial speculations that appear to be beyond anyone's capacity to control.

State-capital-civil society relations

Within the formation of national capitalism, the hegemony of capital lies in a recurrent process of passive revolution and double movement in which the state neutralizes emerging contradictions by implementing mechanisms of redistribution, reorganization and arbitration. The state plays a key role in mediating relations between productive forces and production relations. Under crisis circumstances political and economic elites as well as organic intellectuals begin to initiate state interventions to deal with the situation on two fronts: 1) taking-over of the management and enforcement of negotiations in the controlling of society on behalf of the ruling group; 2) intervention in the economy in order to regenerate productive forces and relations of productions.

During the post-Second World War era, the welfare states in Western Europe characterized by full employment tipped the balance of political power in favor of organized labor. Following the collapse of the Bretton Woods system and the American-initiated oil price rise of 1974 (Kissinger, 1982), capital began to regain control over policy-making in many Western nations under the sway of the ideology and practices of neoliberalism. Since then, economic globalization, especially financial and capital market liberalization, has systematically increased the process of the transnationalization of state autonomy in favor of global capital over national welfare social policies. Consequently, neoliberal globalization not only intensifies the global process of the "disembedded economy" - disembedding the market from society (Polanyi, 1944), but also further integrates and assimilates non-capitalist elements as well as non-market societies in its realm.

What is witnessed today is a situation in which transnational corporations, financial institutions and powerful private investors have the capacity to move production to countries or regions where state's policies may be more compliant to their interests. They are thus in a position to influence state foreign politics and development policies. In this general context, the traditional social concerns of nation-states are being hollowed out by the promotion of neoliberal policies leading to a "race to the bottom". In order to accommodate the global economy, states become more and more instrumental to global economic forces penetrating local borders and markets. They behave as organs of capital, destined to create favorable conditions for its maximal expansion. In contrast to this interpretation, some scholars disagree on the above-mentioned relationship between the national state and globalization. They argue that states and globalization are "mutually reflexive and are embedded in, or are co-constitutive of, each other", which implies that globalization generates both constraints and opportunities for states (Hobson and Ramesh, 2002, p. 8).

This notwithstanding, there is a general consensus today that globalization has largely weakened the state as well as national and global civil societies in which the power and dominance of capital resides. The French diplomat and political scientist, Jean-Marie Guehenno, goes as far as to argue that the idea of the nation-state as a political form that spread from Europe over the rest of the world is becoming superfluous to the extent that capital, on the basis of new forms of technological modernization does not need the nation-state anymore (Guehenno in Grunenberg, 1998, p. 414). Nor does capital feel pressured by labor or anti-systemic forces. Other scholars, on the contrary, take an opposite position in claiming that the nation-state remains the primordial actor in both domestic and international economic affairs (Gilpin, 2001). In-between scholars recognize the interplays of continuity and change regarding the relationship between globalization and the state with a keen awareness of the notable changes in the character of the state in terms of capacities, constituencies, policy-making processes and contents, etc. (Scholte, 1997).

The paradox of neoliberallism is that in fact it needs the agency of the state in order to instrumentalize its socio-economic and political strategy and mediate between the contending forces while reducing the legitimacy of the welfare state and economic nationalism as defensive bastions for society. This opens for a critical conceptual discussion of contemporary capitalism. If the traditional functions of the nation-state are becoming blurred, where is the common space of maneuver and where are the boundaries of civil society on which capitalism's hegemony relies? How can civil society be constructed in an international arena where the global "common ground" (the source of consensual power), such as justice, equality, rights and social security are undermined by globalization? Will the state still be capable of abiding by the social contract that binds state and citizens together in a collective society?

The notion of social contract as citizen-state interactions has undergone dramatic transformations whereby the consent and consensus involving obligations of both citizens and government and accountability-control mechanisms are increasingly being marketized. Consequently, the "social" part of the contract is becoming less universal but more selective, while political participation is becoming less inclusive but more exclusive. This implies the fundamental transformation of the essence of the social contract that - in its original meaning - emphasizes social and political rights. The concept of citizenship as a means of political rights and participation is changed into one of economic empowerment defined in terms of consumers and customers. Under the economy-dominated social contract, the market is ideologically perceived not only as a neutral place (institution) for the exchange of goods, resources and services, but also as the most efficient mechanism to regulate society and human relations.

As far as this evolution in the context of developing countries is concerned, the global market contributes to transforming civil society into a kind of "social cushion" as well as objective ally to neoliberalism that strives to empower the market at the expense of state and society. Thus, grass-root organizations across the world with an anti-statist ideology step in among conflicting social forces and function as mediators between local organizations, the free-market state, foreign donors and transnational companies (Petras, 1997, p. 10).

In sum, the evolution of global capitalism and the restructuring of social forces reveal areas of unresolved problems and potential conflict. Hence, apart from the fact that the term "passive revolution" has lost a great deal of significance after decades of transformations, the instrumentality of this notion in the context of nation-state capitalism cannot automatically be applied to the understanding of reformism and resilience of capitalism at the global level at a time when these mechanisms are urgently needed to deal with a number of vital backlashes created by globalization[16]. Global capitalism today does not possess the same kind of hegemonic resilience in which the economic and political orders respond to each other's legitimacy. Furthermore, the analytical categories within global capitalism's political order have not yet been fully developed, which makes it difficult to act either on the basis of "juridical power" (state apparatus) or on the basis of "consent-endowment" (civil society).

Seen from a Gramscian perspective, what may be happening is that the order of capitalism on both the national and international plans appears to be in limbo. The structure of values and give-and-take arrangement characterizing the ideological legitimation of power and control was more important than coercion. However, neoliberalism and globalization are impairing the ideological foundations that dominated the relationships between the ruling elites and the ruled masses. At the national level, Western political elites have experienced a loss of credibility, whereas at the international level we see a decline of US ideological and economic dominance. Viewed in this light, the potentiality for tension or confrontation is present: "A hegemony is a consensual order which can decline as a consequence of a legitimacy deficit, even if the coercive power resources as such should remain intact" (Hettne, 1995: 14-15) Depending on one's way of looking at the crisis, the situation contains seeds of opportunities as well as pitfalls.

WITHER "PASSIVE REVOLUTION" AND "DOUBLE MOVEMENT"?

From its original location in Europe, historical capitalism developed into a global socio-economic and political system. Notwithstanding being parts of this international construction, individual entities had their own borders, structures, actors, regimes of accumulation and laws, while at the same time comprising conflicting forces dialectically upholding the system together while simultaneously weakening it. At the world system level, as Harry Magdoff has pointed out, following Lenin, "centrifugal and centripedal forces … [are] at the very core of the capitalist process" (1993:77). Thus collusion and collision have been part of the relationship between different ruling national elites. At the domestic level, capitalism exhibits features of an organism in motion leading to tensions and crises but also characterized by resilient structural adjustment and adaptation capacities which have proven on the whole capable of sustaining the processes of creating and recreating conditions for production and reproduction while retaining legitimacy as a viable and sustainable socio-economic system.

In the past, capitalism survived from recurrent crises, assisted by both the trench system of civil society and the coercive apparatus of the state helping to provide national bourgeoisies with an unprecedented level of expansion. Not to be forgotten in this context is the "creative destruction" of war that fulfilled the function of resolving structural economic and political crises by mobilizing the

[16] In a lecture given at the London School of Economics, John Gerard Ruggie (6 June 2002) described three key globalization backlashes: 1) Globalization distributes benefits highly unequally; 2) There is a growing imbalance in global rule making; 3) Globalization is generating greater vulnerability to unfamiliar and unpredictable forces leading to economic instability and social dislocation. See the lecture transcript *Taking Embedded Liberalism Global*: *The Corporate Connection* available at:
http://www.lse.ac.uk/collections/globalDimensions/globalisation/takingEmbeddedLiberalism/transcript.htm

nationalism of the populations away from immediate concerns. The realization of "false consciousness" in Gramscian terms!

The regime change that is currently taking place with the transition from "embedded liberalism" to the "disembeddedment of the economy"[17] is threatening the former societal arrangement. But this interpretation might have been based on a wrong reading of this historical period as well as a misconceived understanding of the concept of embeddedness. As an astute critique of the tendency to conceptualize the post-World War II compromise as the fulfillment of Polanyi's expectations of the second phase of the double movement puts it:

> To the extent that embedding is theorised in terms of the capacity of states to act as gate-keepers to the world to regulate finance and trade to maintain the integrity of domestic political compromises, then the 'second great transformation', globalisation, can also be seen as a kind of disembedding. (Bernard, 1997, p. 87)

In essence, this evolution means entering uncharted territory with the world having to cope with transnational and financial globalization as dictated by the hegemony and strategies of neoliberalism. In this context however, the question that arises is whether and how capitalism is able to transgress the historical limits of its *modus operandi* that permits and reinforces capital accumulation without generating counter-hegemonic blocs and anti-systemic movements? The "golden age" of capitalism until the end of the 1960s is characterized as "the compromise of embedded liberalism" (Ruggie. 1982) by critical theory of international political economy and thus as the second phase of the "double movement" of market regulation by the state underpinned by the US-initiated international regime of hegemonic stability; this evolution together with the compromise of "passive revolution" by the bourgeoisie, who accepted the Welfare State, contributed to the reinforcement of the labor movement's reformism. Of course working-class conditions did generally improve during this period while, however, raising popular expectations as to further gains; these prospects coming on top of the fiscal crisis of the state and exhaustion of the Fordist model, were perceived by the ruling classes as threatening the distribution of the economic surplus and capital accumulation. Seen through this prism, neoliberalism acquires its logic as a political project based on an ideology and strategy of reversal. The defeat of the post-World War II social compromise is underprioritized by critical theory of international political economy who fails to comprehend the contingency of the "passive revolution", i.e. that it was only an armistice in an on-going "war of position". Nor does concern that the implementation of a neoliberal socio-political and economic strategy might disturb the previous social harmony seems to have seriously affected the dominant mainstream discourse yet. But given the ambitions of the project of neoliberalism, whose consequences will be a return to a previous era of capitalism, reactions that might menace the entire edifice cannot be ruled out. As Gindin puts it:

> Neoliberal globalization also tends to undermine, or at least weaken the capacities of states to legitimate capitalism itself; the earlier promises of steady material security and growing equality have given way to the demands of competitive insecurity: that of growing control over our lives has been trumped by the requirements of expanded accumulation; free trade agreements expose the centrality of constitutionalizing and guaranteeing property rights over other rights (2003, p. 121)

Strength and limits of reformism from above and below

In political terms, the second phase of the "double movement" brought about through the implementation of Keynesian macroeconomics and the welfare state, could be understood as a

[17] Here, "embedded liberalism" refers to the "passive revolution" process in which reform attempts and economic policies were initiated in order to embed the market within society. "Disembeddedment of the economy" refers to the current era of transnational capitalism in which embedded liberalism is in the process of being challenged and abandoned.

"passive revolution" of the bourgeoisie, i.e. reforms in socio-economic conditions. In contrast, the present offensive of neoliberalism can be conceptualised as the "active counter-revolution" of corporate capitalism. While social-democratic reformism aimed ostensibly at the formation of a corporative alliance between labor, capital and the state, neoliberalism aims at the deconstruction of this structure and the utilization of the state in returning labor to a subaltern political position. While the agency of the state had partially protected society from market forces at the global level, the post-welfare state, in contrast, has become the transmission belt of globalization. That is articulated in the adjustment of domestic societies to the requirements of global capitalism and the redistribution of the economic surplus in favor of the wealthy classes worldwide.

A factor that is not commonly included in the analysis of the transition to neoliberalism is the historical moment of the phenomenon. In the systemic confrontation between capitalism and socialism, the social-democratic model had revealed itself to be a useful instrument. Regardless of one's sympathy or antipathy for state socialism and recognition of the inherent shortcomings of these societies, it has to be recognized that social democratic parties under the influence of the CIA and American organized labor (Blum, 2003) played a significant role in the anti-Communist struggle domestically and internationally. Besides supporting US subversive activities and policies, Social Democracy by offering a crisis-free model of capitalism with a human face prevented the emergence of systemic alternatives at home and reinforced disillusionment and dissent in the socialist camp. At the time of the demise of the latter, the populations of Eastern Europe and Russia were said to have been yearning for a system incorporating the Scandinavian welfare system, the productive efficiency of German industry and the parliamentary democracy of England. This notwithstanding, simultaneously with the transition to market economies of the former planned economies through the medicine of "shock therapy", neoliberalism no longer under pressure from state socialism became actively engaged in the dismantlement of the Welfare State in the West and statist "crony capitalism" in East Asia while promoting the marketization of the former command economies. The ideological, political and socio-economic usefulness of Social Democracy was no longer needed.

During the regime of Keynesianism, the dominant strategy and discourse was based on the provision of full or near-full employment; under neoliberalism, the mantra has become flexibility and insecurity of jobs and the constant competitive struggle for workplaces. In the context of the change of regime, neoliberalism can be interpreted as no more and no less than the attempt at restoration of the self-regulated market (disembedding it from society), i.e. as a reactionary socio-economic and political project of erasing the gains achieved by the working classes in the twentieth century.

The historical experience reveals the limitations of the politics of reforming capitalism. On the theoretical level this demands a relativization of the notions of "passive revolution" and "double movement" which have been promoted by so-called critical international political economy or "open Marxism" as it has been called. (for a critique of this approach se: Drainville 1994 and Burnham 1994). Thus the protection of society by the state in the second phase of the "double movement" and the willingness of the bourgeoisie to accept reforms in carrying out a "passive revolution" resulted in the strengthening of the reformist tendencies of the workers' movement. This took place without altering the essence of the system and leaving in place the conditions for the possibility of a return of the first phase of the "double movement" and "passive counter-revolution" in a modern context.

The dialectics of the "double movement"

The stability and resilience of social power under modern capitalism has rested not just on the coercive apparatus of the state as traditionally understood, but also on eliciting consent through hegemony in consciousness and the non-coercive sphere of "civil society" into forming the "extended state". However, we are currently at a historical moment in which the "disembedded economy" at both the national and international levels is substantially raising the coercive potentiality of capital. The uncontested power of capital is at the same time reducing the consensual capacity of capitalism and creating the fertile soil for a "double movement" in the form of worldwide anti-capitalism and anti-globalization movements joining forces in de-legitimizing the on-going coercion of market capitalism. As expressed by Mittelman, there might be a similarity with the period around the Great Depression:

> Perhaps similar to the global economy of the 1930s, contemporary globalization appears to be approaching a conjucture in which renewed liberal-economic structures will generate large-scale political, social, and economic disruptions, as well as sustainable pressure for self-protection (2000, p. 8)

While the Gramscian political analytical framework guides us to look into the dynamics of social relations and the dialectical roles of different social forces on which capitalism's resilience, sustainability and hegemony is built, Polanyi (1957) draws our attention to the market-society relations encapsulated in the "double movement": on the one hand, the market (fictitious commodities) continuously extends its sphere by marketizing non-economic aspects of human life in the way that human relations are constantly converted into impersonal ones or into acquiring a thing-like character, whose result is the disintegration of social bond which is an essential constituent of humanity; but on the other hand, as humans are not guided solely by economic motivations, they consciously or unconsciously resist marketization by reclaiming their humanity, i.e. sociality, dignity, freedom and sense of security, as well as by reactivating the essential role of the state as the institution that can be used to discipline the market. Thus double movements are embedded in the state-civil society relations as well.

The contemporary debate over the interpretation of the notion of "double movement" in re-embedding the economy lies in whether this concept should denote "societal protectionism" and "political intervention" to control or regulate the market's mode of functioning, or whether it should imply that re-embedding in a given market society can only be achieved through "a complete subjugation of the market" rather than any attempt to control it (Lacher, 1999a, p. 315). The relationship of the "double movement" to the diabolic complexity of market society as a given structure is spelt out by Polanyi himself:

> Our thesis is that the idea of a self-adjusting market implied a stark utopia. Such an institution could not exist for any length of time without annihilating the human and natural substance of society; it would have physically destroyed man and transformed his surroundings into a wilderness. *Inevitably, society took measures to protect itself, but whatever measures it took impaired the self-regulation of the market, disorganized industrial life, and thus endangered society in yet another way*. (1957, p. 3, italic added)

Based on the above understanding of capitalism, the common simplification of Polanyi's market critique within IPE is challenged on the basis of the historical evolution of the industrial revolution, meaning that capitalism's unique character as a form of economic organization has institutionalized the embeddedment of economic rationality and principles in social relations. This implies that the counter-movement is not without problematic consequences and the social democratic model was only a partial decommodification of the economy because of its non-eradication of labor as a commodity. In a contribution aiming to dispel the confusion surrounding the question of the transition from the welfare state to the neoliberal state, Lacher puts it in the following manner, "Precisely because the postwar economy had not been re-embedded, it was possible for the welfare state to succumb so rapidly to the revival of laissez-faire ideology" (Lacher, 1999b, p. 350)

The difficulties of forming a counter-hegemonic historical bloc compelling capitalism to engage a genuine process of "passive revolution", as analyzed earlier, partake the complexity of the "double movement" in regulating the market. Both Gramsci and Polanyi, independently, converged on a similar critique and transcendence of dogmatic Marxism aiming to grasp the dialectics behind state-market-society relations with the dynamism and complexity of society as a key to understand the durability of capitalism in a global order. As Burawoy (2003) pinpoints:

> We can stretch Gramsci and Polanyi to generate new insights into the idea of the transnational society. From a Polanyian perspective, we can think of the way transnational society is forged in response to commodification generally but in particular to the commodification of land, labor, and money. But we must be very careful not to romanticize this transnational society. It, too, is a very uneven political terrain, populated by hierarchies of power, sloping down from

> center to periphery, and having its own fissures and ravines. From a Gramscian perspective,we can think of transnational society in its relation to supranational state-like agencies, but that connection contains struggles against capitalism as often as it provides grounds for its transcendence.

This complements our proposed interpretation of the contradictions of globalization as a dialectical and dynamic unity embedded in the interaction of reciprocal and paradoxical relations, which, on the one hand, opens the door for progressive transformations, while on the other hand, sets the limit of counter-hegemonic protectionism within market society.

In conclusion it can be said that the contemporary expansion of capitalism and the post-Cold War withdrawal of the United States as the only stabilizer of global hegemony together with its unpopular foreign policies after the 9/11 crisis have brought about changes in state-market-society relations all over the world. The new situation has produced the marginalization of consent/consensus-generating elements, i.e. the institutions, practices, and social relations that constantly exist as alternatives or balances of power. Consequently, without consent-building capacity, global capitalism entails a self-denial potential towards dissolution and disintegration, unless a powerful social force is successful in generating a global “double movement” to push neoliberal capitalism to negotiate a substantial process of passive revolution. At the present time, it is still difficult to foresee the possibilities of an effective global counter-hegemonic project able to generate the possibilities of embedding global capitals and markets in shared social values and responsibilities. The key issue (conundrum!) that needs to be understood is the nature of the totalizing force of capitalism vis-à-vis counter-movement in a nexus of hegemony and contradictions.

While the second phase of the double movement and passive revolution are used to explain the evolution of advanced Western industrialized capitalist societies following the Great Depression, not sufficient attention has been paid to the significance of Fascism as a likewise attempt to protect societies from the havoc of the world economy as well as the defusing of pressures due to the class struggle. It is often forgotten, that from the 1930s on, proto-fascism was implemented in numerous European as well as extra-European societies. Also in Western democracies, there was a large current of sympathy for fascist doctrines. The discussion of the transition from welfare capitalism to market fundamentalism blurs, to a certain extent, the present evolution of “real existing capitalism”.

Under the guise of promoting liberal democracy, neoliberalism is in fact reinforcing structural tendencies of economic and political power concentration. This development is most advanced in the case of the United States, where the military-industrial complex and the oil industry together with other corporate interest groups have a strong hold on the seat of power in Washington. This calls to mind the definition of this type of societal regime by Benito Mussolini: “Fascism should more properly be called corporatism because it is the merger of state and corporate power”(quoted by Mills, 2004). When we look at the structural evolution of present-day US capitalism, the prospects of imperialist conflicts due to the increasing demand for oil and the depletion of resources (Klare, 2001), we have to come to the conclusion that a return to the reformism of the social-democratic double movement and the historical compromise of the passive revolution does not have favorable conditions for implementation.

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A PANEL ASSESSMENT OF REAL COVERGENCE IN CEMAC[1].

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Abstract

Some authors support that regionalism among underdeveloped countries will tend to cause divergence of their income levels, and regional integration among rich countries will tend to cause convergence. This paper tests this convergence hypothesis in CEMAC between 1990-2002. Our findings lend support to the "convergence club" defined according to policy choices rather than initial levels of human capital. They show that unilateral and preferential suppression of tariff and non-tariff barriers favor the convergence of per capita incomes and reduce the dispersion of real per capita income levels of partners in the sub-region. These results make the idea of convergence club based on the initial levels of productive technology and GDP per capita relative.

JEL: F42, O47, C33.

Key Words: Trade Reforms, Regional Integration, Convergence, Central Africa.

1. Introduction.

Many of the crucial debates in regional integration are encapsulated in the question of disparity of income levels among the member countries. Economists are interested in knowing whether in a regional grouping the distribution of income changes over time. More specifically, they are interested in whether within a grouping intra-differences in income levels tend to disappear or to increase over time. If they diminish, then there may be less worry about creating compensation schemes such as the Regional and Cohesion Fund Policies in the European Union. If they increase, some of the member states will continuously benefit from their membership while others will be getting a fair share of gains. This may lead to the disintegration of the community as was the case in the UDEAC in 1968, the East African Community (EAC) in 1977, and more recently in the Central American Common Market (CACM). Economists are also interested in knowing whether member countries that are relatively poor today are likely to remain poor in the future. All these concerns are related to the empirical phenomenon called convergence.

The main assumption behind the analysis of convergence in regional integration groupings is that similarity in production and trade structures among countries will ease the integration process. Theoretical models predict that countries will trade more between them and obtain higher gains from trade if they are different (in terms of factor endowments in the Hecksher-Ohlin tradition or in terms of technology in Ricardian models), while according to other models (enhancing imperfect competition and intra-industry trade) trade will occur especially among similar countries. In spite of these different approaches, it is generally agreed that adjustment costs are smaller when integration occurs between countries that are relatively alike. The more similar countries are, the more likely they will be exposed to common shocks (Brülhart, 2000) and greater similarity in production structures is likely to increase business cycle correlations (Krugman, 1993; Imbs, 2001). This means that common macroeconomic and industrial policies will be more effective the larger is the similarity among country members.

[1] CEMAC stands for "Economic and Monetary Community of Central Africa", and covers six countries: Cameroon, Central Africa Republic, Chad, Congo, Equatorial Guinea, and Gabon.

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Another reason to believe that similar countries integrate more easily is that they are more likely to lie in the same diversification cone, and this allows at least the theoretical possibility to achieve factor price equalization through trade (Deardorff, 1994).

Standard neoclassical growth theory predicts that the elimination of trade barriers and free movement of production factors across countries will result not only in the overall welfare increase in the integrated area, but also cause real convergence of countries in the region. However, many authors (Baumol et al, 1994, Henner, 2001; Venables, 1999; Dowrick and Nguyen, 1989, Baumol, 1986) demonstrated that convergence seemed to hold among rich countries. The most frequently cited work in this area is Baumol (1986) who based his research on a sample data of 16 OECD members and obtained a significant negative coefficient of the initial income variable in a classical growth model regression. Hence the result supported the existence of absolute convergence. In another research (Baumol et al, 1994), the outcome of using the same methodology on the sample of over 70 countries was that convergence does not exist. The results of these two empirical studies suggested that there might be a "convergence club", meaning a subset of countries for which convergence applies, while countries outside of the "club" would not necessarily experience convergence vis-à-vis those in the club. According to these authors, only countries with an adequate initial level of human capital endowments can take advantage of modern technology to enjoy the possibility of convergent growth (Baumol et al, 1994, p. 65). A direct implication of this line of reasoning emphasized by Venables (1999, p. 2) is that regionalism among underdeveloped countries will tend to cause divergence of their income levels, and regional integration among rich countries will tend to cause convergence.

However, Sachs and Warner (1995) suggested that poorly managed economies, such as those with the absence of secure property rights, autarkic trade policies, inconvertible currencies, and so forth are unlikely to experience convergence no matter what the underlying production technology or initial level of human capital. Put another way, these authors lend support to the "convergence club" defined according to policy choices rather than initial levels of human capital. They further suggested that poor policy choices are reversible, and not irrevocably linked to low levels of income (p. 5). In their view, burdensome taxes on foreign trade are particularly harmful, since these not only distort economic incentives, but also cut countries off from international flows of knowledge (p. 6). In conclusion, these authors argued that convergent growth can be achieved by all countries that follow a reasonable set of political and economic policies, including civil peace, basic adherence to political and civil rights, and most decisively openness through the absence of trade quotas, export monopolies or inconvertible currencies (p. 23). This conclusion was later confirmed by Varblane and Vahter (2005) who analysed the process of economic convergence in transition economies during 1995-2004 and found that unconditional β - convergence and σ-convergence existed across the countries under consideration within the analysed period.

Our concern in this paper is to test the "convergence club" hypothesis in CEMAC. We are interested in knowing whether regionalism in CEMAC is bound by the characteristics of African economies to always experience divergence of income levels of member countries.

Confronted by the economic crisis of the 1970s and the 1980s, and the mediocrity of the performance of their economies, most CEMAC countries undertook major reforms in the context of S.A.P guided by the Bretton Woods institutions. These reforms in the trade sector aimed to disrupt the protectionist tendencies, which were prevailing in African economies as from 1960s. Thus, apart from the macroeconomic stabilization measures, other efforts were generally deployed on:

- the progressive elimination of quantitative restrictions and price control,[3] simultaneously
- the reduction of tariff barriers and their variability.
- the suppression of exemptions
- the easing or abandonment of contingencies,
- the flexibility of the exchange rate,

[3] In Cameroon, the first series of 105 products were liberalized from quantitative restrictions in 1989/90 and the second series of 22 products in 1990. In Gabon, quantitative restrictions were definitely and officially removed in 1994 with the publication of the Presidential Decree No. 772/PR/MCIRS/MFBP cancelling all licenses and authorization to import or to export.

- the progressive suppression of state monopolies in international trade,
- the privatization or reform of public enterprises.
- the reduction or elimination of non-tariff barriers

These unilateral reforms were reinforced from 1994 by the devaluation of the CFA franc and the preferential tax and customs liberalization. While the former was designed to improve the external competitiveness of exports of the sub-region, the later aimed at eliminating all internal obstacles to cross-border trade among member countries and simplifying the external tariff. Thus, new structures were introduced to deal with domestic sales, intra-CEMAC trade, and trade with the rest of the world.

Regarding the domestic market, various specific taxes were replaced by a turnover tax (TCA) with two rates, a normal and a reduced rate. These rates were fixed freely by each member state within the range of 7% to 18% for the normal rate and 3% to 6% for the reduced rate. In July 1994, the rates fixed were 5% and 15% in Cameroon and Chad, 5% and 10% in CAR, and 5% and 12% in Congo and Equatorial Guinea (Njinkeu et Monkam, 1999; Giorgio Barba Navaretti et al, 1998). Gabon opted for a value added tax at a rate of 18% from April 1995. Besides, all exemptions and privileges attached to the qualification for preferential regimes were canceled (TU[4], TIP[5], Investment codes). The TCA was later replaced by the Value-added Tax (VAT) in Cameroon and Congo applied at the rate of 17% (World Bank, 1998).

With respect to intra-CEMAC trade flows, multiple rates of indirect taxation were simplified, and a generalized Preferential Tariff (GPT) equivalent to 20% of the common External Tariff was introduced. This rate came down to 10% in 1996, and through January 1, 1998, the GPT came to 0% and intra-CEMAC trade was carried out free of import duties.

Vis-à-vis the rest of the world, custom duties were set into a four-tier structure with a 50% top rate (duties had previously been up to 300% in some countries), and quantitative restrictions were eliminated. The four categories of custom duties were replaced by a single system, the Common External Tariff (CET), imposed on all imports from non-member countries. The CET is comprised of two taxes, a customs duty and a temporary surcharge tax. The customs code classifies products into four groups, representing successive levels of product transformation. Simultaneously, the array of tax reduction and exemption offered by preferential regimes as well as by investment codes, were phased out. Imports were classified into four groups and custom duties ranged from 5% to 50% in January 1994 as follows:

i Essential goods 5%
ii Raw materials and capital goods 15%
iii Intermediate and miscellaneous goods 35%
iv Consumer goods 50%

In December 1994 these rates were lowered to 5%, 10% 20% and 30% respectively. The second component of the CET, the temporary surcharge tax with a rate ranging between 0% and 30% was introduced in 1995 on specific products in order to substitute for the protection formerly provided to firms via non-tariff barriers. This tax was canceled in January 1997 in many CEMAC economies.

With regard to institutional blockages, the 1994 CEMAC treaty introduced the principle of a restrictive list of questions for which unanimity in decision-making is necessary. This treaty created a court of justice with jurisdiction over conflicts among member countries.[6] Also, the principle of an autonomous General Secretariat has been accepted. Contributions required from member states are expressed as a percentage of exports to the rest of the world. Staff positions are no longer allocated among member states. Staffs are to be recruited solely on the basis of their competence given the predefined job profiles.

The policy changes described above reflected the recognition that reliance on administrative controls had driven most economic activities outside formal channels, depressed exports, contributed to an inefficient structure of domestic production, and hampered long-run growth.

[4] "Taxe Unique" or Unique Tax
[5] "Taxe Intérieure sur la production" or Internal Tax on Production
[6] This duty was incumbent to the Council of Heads of States in which each member has veto power.

It is worth mentioning that the main characteristic of the fiscal and customs structure of the CEMAC during the pre-reform period was its lack of uniformity across the member countries. Many special taxes and a case by case system of negotiation of tax rates between individual firms and fiscal authorities originally put in place to support the industrialization process rather created an economic environment of corrupt practices within the grouping in which considerable financial resources were spent for the obtainment of licenses, privileges and other administrative advantages instead of supporting productive activities. In some member States, corrupt activities perpetuated by fiscal authorities were intensified during the period of economic crisis since public salaries were cut down (Tybout et al, 1997). These corrupt practices enormously increased the cost of trading within the sub-region (Idem, p. 11). In addition, the inefficiency of sub-regional institutions together with the requirement of a consensus in decision-making led to the stagnation of regional integration initiatives. The situation was aggravated by the fact that the accords of UDEAC[7] had no provision related to the transfer of sovereignty from Member States to the sub-regional body. This institutional limitation, which naturally opened doors to all sorts of distortions in decision-making together with rigid nominal exchange rates, increased the need for reforms in order to revitalize the economies of the sub-region.

The economic reforms, in modifying the incentive structure aimed to reinforce the openness of CEMAC economies. They have doubtlessly consolidated the importance of the private sector compared to the public one in member countries. They are ingredients of a liberalization policy, since practically this refers to the liberalization of imports or the trade policy movement towards the neutrality of relative prices or the substitution of the forms of state intervention, which may create more distortions by those that may create fewer distortions (Collier et al, 1997). Trade liberalization can also be considered as an evolution towards multilateralism when it simultaneously associates the elimination of quantitative restrictions with the reduction of tariff barriers to imports and exports. Generally, trade reforms rely on three approaches based on changes in trade policies, prices and quantities.

Theoretically speaking, the above-described reforms positively affect growth policies and favor the openness of the economy. The process of liberalization creates a regular and judicious environment, which gives to firms the possibility of developing their activities with equal opportunities (Henner 1996). Thus, we distinguish internal liberalization, which facilitates the development of the private entrepreneurship, and external liberalization; both of which assure the better allocation of resources through the market channels. Globally, the liberalization policy gives high priority to market rules. It allows reducing the distortions in the relative price structure and allocates resources where they are rationally used. This favorably impacts on both the regional as well as the international specialization and convergence of income per capita levels of member economies.

With respect to the developments above, it can be established that preferential and unilateral liberalization improves the perspective of regional economic integration in SSA (Jebuni 1997, p.364; Collier and Gunning, 1993, p. 16) and favors the convergence of income levels of member economies (World Bank, 2000, p. 41; Sachs and Warner, 1995). In connection with this evidence, this paper seeks answers for the following questions: after the wave of economic reforms of the 1980s and the 1990s in central African economies, is there a tendency in the CEMAC for less advanced countries to grow more rapidly than the richer countries, and thereby to converge in living standards or income levels? Or instead, are there tendencies for the “rich to get richer and the poor to get poorer”, so that the gap between rich and poor nations tends to widen over time? Is there a tendency for the dispersion of real per capita income across member economies to fall over time? More specifically, the paper examines whether less advanced economies tend to grow faster than wealthy ones within the sub-regional grouping under consideration (β - convergence). It also checks whether the dispersion of real per capita income across member economies tends to fall over time (σ-convergence). These specific objectives rely on the theoretical hypothesis that unilateral and preferential suppression of tariff and non-tariff barriers favor the convergence of per capita revenues and reduce the dispersion of real per capita income levels of partners in the sub-region.

[7] UDEAC (Union Douanière des Etats de l'Afrique Centrale or Central African States customs Union) was transformed in 1994 to give birth to CEMAC

The rest of the paper is articulated around the literature review (section 2), the methodology (section 3), the empirical results (section 4) and finally the conclusion (section 5).

2. Literature Review
2.1.Theoretical review.

Broadly speaking, economic convergence in a regional integration grouping is understood to mean the increasing alignment of the economic variables considered, due to more rapid advances in less favored countries than in the average of the grouping. Two types of economic convergence are usually considered: nominal and real. Nominal convergence refers to the tendency towards a greater uniformity of nominal variables indicative of macroeconomic stability. Real convergence expresses the approximation of the levels of economic welfare, generally proxied by per capita income. Our study focuses on real convergence.

The literature in economic growth has used many definitions of real convergence (Quah, 1993). Meanwhile all definitions turn around two concepts, β - convergence and σ - convergence. There is β - convergence in a cross-section of economies if a negative relationship is found between the growth rate of income per capita and the initial level of income. In other words, β - convergence occurs if poor economies tend to grow faster than wealthy ones. On the contrary, σ -convergence occurs when the trend in the dispersion of the levels of real per capita income is falling over time (Sala-i-Martin, 1995). Though different, these two concepts are related. Suppose there's β-convergence in a group of countries i where i = 1,2, . . . N. In discrete terms, the real annual per capita income for an economy can be defined as follows:

$$\text{Log}(Y_{it}) = a + (1-\beta).\text{Log}(Y_{it-1}) + \mu_{it} \quad (1)$$

Where "a" and β are constants. $0 < \beta < 1$, and μ_{it} is the error term. The requirement $\beta > 0$ implies β-convergence. The annual rate of growth Log (Y_{it} / Y_{it-1}) is inversely proportional to Log (Y_{it-1}). A higher coefficient β corresponds to a great tendency of convergence. The disturbance term captures temporary shocks on the production function, the saving rate, etc. We assume that μ_{it} has mean zero, the same variance δ^2_μ for all economies and is independent over time and across economies.

In order to measure the cross-sectional dispersion of income, we take the sample variance of the Log of income,

$$\sigma_t^{\ 2} = (1/n)\sum_{i=1}^{N}\left[\log(y_{it}) - \mu_t\right]^2 \quad (2)$$

Where μ is the sample mean of Log (Y_{it}). If N is large, then the sample variance is close to the population variance, and we can use (1) to derive the evolution of σ_t over time :

$$\sigma_t^{\ 2} \cong (1-\beta)^2.\sigma_{t-1}^{\ 2} + \delta_\mu^{\ 2} \quad (3)$$

This is a first-order difference equation, which is stable if $0 < \beta < 1$. If there is no β - convergence so that $\beta < 0$, then the cross-sectional variance increases over time. This would simply mean that if there is no β - convergence, there cannot be σ -convergence. In other words, β - convergence is a necessary condition for σ -convergence.

Beside these two concepts, Barro (1991) and Barro and Sala-I-Martin (1991, 1992) introduced the notion of "Conditional Convergence" in which difference between countries is related to their long term per capita income levels. These authors also distinguish conditional from absolute convergence. Thus, a set of economies displays conditional β - convergence if the partial correlation between growth and initial income is negative. In other words, in a cross-sectional regression of growth on initial income where a number of additional variables are held constant, if the coefficient on initial income is negative, then the economies in the data set display conditional β - convergence. If the coefficient on initial income is negative in a univariate regression, then the data set displays absolute β - convergence.

In an economy, the wider the initial gap between the level of per capita GDP and the level of long term per capita income, the faster the growth of the economy. Formally, if country i has $Y_i^{\bullet}$ as a long term per capita income and Y_i as the level of per capita GDP, the growth rate y_i^* is assumed to be a linear function of the gap between $Y_i^{\bullet}$ and Y_i :

$$y_i^* = \beta\,(Y_i^{\bullet} - Y_i) \tag{4}$$

A positive value of β implies a conditional convergence. The level of long term per capita income $Y_i^{\bullet}$ is here represented by certain structural variables such as the initial level of human capital. Barro (1991) estimated equation (4) and found a positive and significant coefficient for β and significant coefficients for the other structural variables. He concludes that a poor country tends to grow more rapidly than a rich country with the condition of having a certain quantity of human capital.

Concerning the theoretical link between regional economic integration and real convergence, the implications of traditional theories of trade are very clear. Let's consider the impact of market integration. The Hecksher-Ohlin model demonstrates that countries export goods rich in factors, which are abundant in their economies and import goods rich in factors whose endowment is weak. In abstraction to transport costs, liberalization tends to equalize prices of goods traded. Thus countries will export the more products that exploit their best factor endowment. The demand for abundant and less expensive factors increases while that of limited and expensive factors falls. The convergence of prices of goods tends to bring about convergence of factor prices. In peripheries where labor is abundant, real salaries will fall while at the centre where labor is limited, they will increase, everything being equal. Capital or labor mobility is made possible between the two poles in conformity with the predictions of Mundell (1957). Labor will migrate from periphery to centre in search of high salaries. The consequence is an increase in wages in the periphery and a fall in wages in the centre. As for capital, it will move from the centre to the periphery in search of better returns. This movement reduces the wages of the centre and increases those of the periphery. The whole movement favors the alleviation of the difference in factor prices between regions and ends up in the convergence of income levels of member countries.

2.2 Empirical Review

During the past two decades, there has been a significant increase in concerns about convergence. Overviews of the convergence literature are found in Durlauf and Quah (1999), and Temple (1999). The reason for the sudden increase was twofold. First the existence of convergence across economies was proposed as the main test of the validity of modern theories of economic growth and as a distinguishing feature between the earlier model (Solow, 1956) and endogenous growth models. The second reason for the evolution of the convergence debate was the ready availability of international comparable GDP data, which permitted the comparison of GDP across a large number of countries and its evolution over time.

The familiar studies of the convergence hypothesis at international level build on early contributions by Baumol (1986), Lucas (1988) and Romer (1986). Today there is a large literature drawing on neo-classical and endogenous growth models, whilst employing a range of empirical techniques. The more recent tests for convergence include Barro and Sala-I-Martin (1991), Carlino and Mills (1993, 1996), and Bernard and Jones (1996) for the US. Coulombe and Lee (1995) examine regional convergence processes for Canadian provinces. Mallick and Carayannis (1994) look at

Mexican states and Chatterji and Dewherst (1996) at British countries. The consensus from all these studies is that income convergence has been strong on a regional level.

Based on the European Union experience, it is evident that preferential reforms within regional integration groupings lead to the convergence of levels of income of member countries. This is observable through the improving economies of Ireland, Spain and Portugal who have made enormous progress in reducing the gap in growth, which formerly separated them from the more advanced nations of the EU. The analysis of the dispersion of revenue levels in this group was done by Ben-David (1993) for the period covering the 1980s. The results obtained clearly show a progressive convergence in income levels as from 1947 (creation of Benelux), through 1951 (formation of CECA), 1957 (creation of the EEC), 1962 (elimination of all quotas), 1968 (elimination of all internal tariffs of the EEC) to 1981. As a whole, the difference in the levels of income dropped by two-third during the above period, due especially to the more rapid growth of less advanced economies of the community. As illustration, during the 1980s, the per capita GDPs of Ireland, Spain and Portugal were 61%, 49% and 27% of the per capita GDPs of the larger countries of the EU respectively. During the 1990s, these figures rose to 91%, 67% and 38% respectively (World Bank, 2000). Meanwhile this convergence did not include Greece though she joined the EU long before Spain and Portugal. The main reason put forth is the absence of the necessary reforms in Greece. Thus even though regional integration is potentially beneficial, deep reforms are necessary in the less advanced economies in order to materialize the potentially beneficial effects. This is why we are proposing to test this convergence hypothesis in the CEMAC sub-region at the down of waves of reforms of the 1980s and 1990s.

In Africa, studies on convergence are rather few in spite of the importance of the issue for the region. The work of Jones (2002) on absolute and conditional convergence in ECOWAS finds the existence of both β and σ convergence in the grouping. This study concludes that the member countries of ECOWAS form a convergence club. Dufrenot and Sanon (2005) also test the process of β -conditional convergence of per-capita GDP in the same grouping between 1985 and 2003 under the assumption of parameter heterogeneity and contrary to Jones (2002) they find no evidence of real conditional convergence (p. 16). These authors conclude that in ECOWAS, member states individually follow their long-run growth paths. In this respect they recommend active coordination of policies to reduce the structural heterogeneity. Akanni-Honvo (2003) examines the implications of regional integration agreements on the process of convergence or divergence of member economies in developing regions between 1975 and 2000. The results show that the creation of regional integration groupings in less advanced regions does not automatically lead to absolute convergence across member countries, and that conditional convergence that appears in some regions is weak. Meanwhile, the dynamic of convergence of per-capita GDP that is perceived in SACU in Africa, ASEAN in Asia and MERCOSUR in Latin America is supported by concerted investment policies in infrastructures, complementary production capacities, the diversification of economic structures, and finally the capability of more advanced economies in the groupings to generate the necessary and sufficient spillover effects on other member countries. In addition the frontier effects have a contrasting impact on the economic growth of member states and on the convergence process within the groupings. However, this author cautions against reading too much into his findings, as they need to be confirmed by a model-based analysis in different sub periods that would convincingly shed more lights on the process of real convergence in regional integration groupings in less advanced regions. This caution gives more relevance to this paper in Central Africa.

Nearly two decades have passed since African countries undertook the economic reform program and efforts made so far to study the likely effects of the policy measures on target variables such as, whether less advanced economies tend to grow faster than wealthy ones within the sub-regional groupings under consideration (β - convergence), and whether the dispersion of real per capita income across member economies tends to fall over time (σ - convergence) are rare. However, for the purpose of economic policies, the sub-regional grouping authorities need to know to what extent poor member countries are caching up to wealthy ones as a consequence of economic reforms within the groupings. They also need to know by how much the real income dispersion within the groupings will fall over time. It is on account of this vacuum that the current paper has specific relevance.

3. Methodological Approach

The specialized literature on real convergence has come up with a wealth of different measures and openly debated on their relative merits[8]. The simplest indicator for assessing real convergence between countries (regions) within an area is to test whether the per capita GDP of a country (region) or a set of countries is approaching the average of the area. The two most popular measures are the beta-convergence and sigma-convergence. The former is generally tested by regressing the growth in per capita GDP on its initial level for a given cross-section of countries. In turn, this beta-convergence covers two types of convergence: absolute and conditional (on a factor or a set of factors in addition to the initial level of per capita GDP). In contrast, sigma-convergence designates the reduction in the dispersion of per capita GDPs within a sample of countries.

The basic neo-classical beta-convergence model, as proposed by Barro and Sala-I-Martin (1991, 1992), for the evaluation of convergence or divergence trends across countries or regions adopts the following form:

$$\frac{1}{T}\ln\left(\frac{Y_{i,t}}{Y_{i,t-T}}\right) = \alpha + \ln Y_{i,t-T}\left(\frac{1-e^{\beta t}}{T}\right) + \varepsilon_{i,t-T} \qquad (5)$$

Where $Y_{i,t}$ represents the GDP per capita of the country or region i; T is the period of analysis; β is the coefficient and ε is the error term. A negative value for the slope coefficient β indicates convergence of GDP per capita across territorial units of analysis, in a given time period, while a positive value indicates divergence.

This methodology to test beta-convergence has been criticized for producing biased results. Quah (1993, 1995, 1996) argues that this methodology largely neglects the dynamics of changing national (regional) income distributions and proposes the use of a complex method based on the use of Markov chains to capture the dynamics of the entire cross-country distribution. Boyle and McCarthy (1997, 1999) have suggested the use of the Kendall index of rank concordance, referred to as *gamma*-convergence in addition to *sigma*-convergence in testing *beta*-convergence. More recently Petrakos et al (2001) re-examined from a critical theoretical and empirical viewpoint the convergence literature and provided a new dynamic framework of analysis, which allows for a better understanding of the forces in operation described by the two sides involved in the debate. Unfortunately, its application to the measurement of disparities in the European Union yielded results that were difficult to interpret (Idem).

In general, none of the existing measurement procedures mentioned above is accepted as inherently superior to the others in any circumstances. Probably because of its intuitive appeal, the first approach (beta-convergence) remains the most commonly used. It is also the one to which we refer in this paper.

3.1. Model specification.

We develop an empirical model that will be applied to CEMAC to test for absolute and conditional convergence. This model tries to capture the main immediate determinants of the growth of income per capita. Following the usual procedure in the literature (De la Fuente, 1998), we derive an empirical convergence equation from a log-linear approximation to a simple growth model. We assume that the production side of the economy can be described by a reduced-form aggregate production function of the form:

$$Y_{it} = \theta^{\gamma} K_{it}^{\alpha_k} H_{it}^{\alpha_h} R_{it}^{\alpha_r} (A^{g}{}_{it} L_{it})^{1-\alpha_k-\alpha_h-\alpha_r} \qquad (6)$$

Where Y_{it} is aggregate output in country i at time t, L the level of employment and A_{it} an indicator of the level of technical efficiency, which grows at an exponential rate g. The variables K, H and R

[8] Barro and Sala-i-Martin (1995), Quah (1993, 1996), and Grossman (1996)

denote, respectively, the stocks of physical, human and technological capital, and θ is an indicator of the relative weight of the government sector in the economy.

This formulation is not completely standard since it allows the national output to be a function of the relative size of government. The indicator of the weight of the government sector in the economy is meant to capture in the simplest possible way the fact that public activities may affect productivity in a variety of ways other than through infrastructure investment, which contributes directly to factor accumulation.

From equation (6) we can derive a convergence equation[9] of the form:

$$GYPC_{it} = g + \beta a_{it} - \beta^{*} \ln YPC_{it} + \gamma(\ln\theta_{it} + (\delta + g + n)\ln\theta_{it}) +$$

$$(\delta + g + n)\left[\alpha_k \ln\frac{sk_{it}}{\delta + g + n_{it}} + \alpha_h \ln\frac{sh_{it}}{\delta + g + n_{it}} + \alpha_r \ln\frac{sr_{it}}{\delta + g + n_{it}}\right] \tag{7}$$

Where $GYPC_{it}$ is the growth rate of income per capita in country i during the sub-period which starts at t. lnYPC is the log of income per capita at the beginning of the sub-period, sj_{it} the fraction of GDP invested in capital of type j (j = k, h, r), n_{it} the rate of population growth, a_{it} the log of the indicator of technical efficiency (A_{it}), θ the log of government's share in GDP, and δ the rate of depreciation of capital. β measures the rate of convergence towards a pseudo-steady state, which would be attained asymptotically if the rate of population growth, the share of government expenditures in GDP and the different investment rates remained constant over time. The value of the convergence coefficient will depend on the degree of returns to scale in the reproducible factors (in the different types of capital), with convergence being faster the faster diminishing returns set in.

Equation (3) can be extended to incorporate some important determinants of growth not considered by the theoretical model from which we started. Since we work with data on income per capita rather than output per worker, we control in a simple way for a technological catch-up effect. De la Fuente (1995) argued that, if technology diffuses across countries at a sufficiently rapid pace, those economies which are technically less advanced at the beginning of the period should, other things equal, grow faster than the rest. This effect, however, will gradually exhaust itself as each country approaches an equilibrium level of relative technical efficiency which is determined by its own research and Development effort and the speed of diffusion. To try to capture this effect we include a dummy for initially backwards countries in CEMAC.

After extension, we get a new equation that will be estimated to test for conditional convergence in the regional integration scheme under consideration.

$$\ln \Delta Y_{it} = \beta_0 + \beta_1 \ln Y_{iit-k} + \beta_2 \ln G + \beta_3 PMA + \beta_4 INV + \mu_{it} \tag{8}$$

ΔY_{it} is the GDP per capita growth rate in time t in country i. Y_{it-1} stands for GDP per capita at the beginning of the period that determines either convergence or divergence (β_1 >< 0) G is total government expenditure as a fraction of GDP (β_2 >0). PMA is a dummy that takes 1 for initially backwards countries in the groupings. A positive relationship is expected between PMA and the GDP per capita growth rate ($\beta_3 \succ 0$). INV is capital investment, and μ_{it} is the error term.

3.2. Estimation techniques

Equations (1) and (8) above are estimated for a panel of member states in the grouping under consideration to test for absolute and conditional beta-convergence respectively. Secondly, we compute the standard deviation of the GDP per capita of member countries in the sub-region at the

[9] From equation (6), we first subtract from both sides the income per capita of the beginning of the sub-period. We secondly introduce the logarithm and make necessary transformations.

beginning and at the end of the period. The comparison of the two values of this inequality measure shed light on whether the dispersion of real per capita income across member economies tends to fall over time (σ -convergence).

We have chosen the estimation procedure that doesn't tend to overlook the relative size or importance of each country, treating all observations as equal (cross section weights). This is justified by the disparity that exists among member states in central Africa. Finally, in order to take into consideration the pace of reforms in the sub-region, and the fact that business cycles are not synchronized across member countries, we first cover the whole period 1990-2002, and after we divide it into sub-periods.

3.3. Data collection.

The period of analysis starts in 1990 and ends in 2002. We first of all estimate our models for the entire period, and after we also estimate them for 1990-1994, 1995-2002, and 1998-2002. These three sub-periods correspond to different articulations of the economic reform process in the grouping. First, the unilateral reforms adopted in all the CEMAC member states under the World Bank and IMF Structural Adjustment Programmes (SAPs) in the first half of the 1980s were supposed to affect the factor mobility among the member economies by the year 1990. Second, in January 1994, preferential reform measures were introduced in the grouping, namely the devaluation of the CFA franc and the Tax and Customs reforms. These new measures are supposed to affect the results obtained in 1990-1994 and impact on the convergence process as from 1995. Third, in January 1998, the generalized Preferential Tariff (GPT) introduced in 1994 for intra-CEMAC trade flows, which was equivalent to 20% of the common External Tariff (TEC) was phased out and internal trade in the grouping was carried out free of import duties.

Our data are obtained essentially from the following sources: the World Bank, the IMF, the African Development Bank publications, and the headquarters of CEMAC. These are related to per capita GDP, total government expenditure as a fraction of GDP, and total investment as a share of GDP.

4. Empirical results.

4.1. Absolute convergence.

Table 1 : Results of the regression of the absolute β -convergence.

		C	$\text{Log}(Y_{it-k})$	R^2	$\bar{R}^2$
1990-2002	Coeff	2.483	- 0.187	0.343	0.325
	t-stat	3.84*	-1.96***		
	Prob	0.0005	0.058		
1990-1994	Coeff	3.18*	-0.286	0.682	0.642
	t-stat	4.91*	-3.06*		
	Prob	0.000	0.005		
1995-2002	Coeff	1.897	-0.111	0.52	0.49
	t-stat	1.776***	-0.688		
	Prob	0.087	0.49		
1998-2002	Coeff	16.299	-2.48	0.647	0.445
	t-stat	3.08*	-2.91**		
	Prob	0.008	0.01		

Note: *, ** and *** imply significance at 1, 5 and 10% levels respectively.

We have considered 1970 as the starting period. In this year, the integration accords within the framework of UDEAC, which was later transformed to give birth to CEMAC, were just enacted.

Equation (1) was first estimated for the time intervals of 1990-2002, then for 1990-1994, 1995-2002 and finally 1998-2002. During these periods, our variable of interest, the level of GDP per capita at the beginning of the period has the expected sign. It is significant at 10% between 1990-2002. This means that by examining the global tendency in this time interval, there has been a weak economic catch-up between the less advanced and the more advanced economies of the grouping. Between 1990-1994, convergence is most pronounced since GDP per capita is significant at 1%. Meanwhile during 1995-2002, it has the expected sign but isn't significant. Finally, between 1998-2002, our main variable denotes absolute beta-convergence.

As a whole, the results of the estimation denote the importance of the unilateral as well as multilateral reforms in the integration zone. As such, the reforms undertaken by the CEMAC member States in the context of S.A.P and within the framework of the preferential liberalization have contributed to the narrowing up of the standard of living gaps in the sub-region. These results make the idea of convergence club based on the initial levels of productive technology and GDP per capita relative.

4.2 Conditional beta-convergence.

Equation (8) is estimated for the same periods as mentioned above to observe conditional convergence of development levels within the economic grouping.

Table 2 : Results of the conditional β-convergence.

		C	$Ln(Y_{it-k})$	Log(G)	Log(INV)	PMA	R^2	$\overline{R}^2$
1990-2002	Coeff	0.009	0.112	- 0.72	0.75	0.88	0.382	0.309
	t-stat	0.007	0.78	- 1.74***	3.42*	2.97*		
	Prob	0.99	0.44	0.09	0.002	0.006		
1990-1994	Coeff	18.26	- 2.17	- 0.051	0.139	4.49	0.684	0.672
	t-stat	11.01*	- 9.71*	- 0.129	0.68	10.04*		
	Prob	0.000	0.002	0.9	0.52	0.000		
1995-2002	Coeff	0.21	0.26	- 1.603	1.24	0.53	0.524	0.445
	t-stat	0.141	1.47	- 2.48**	4.66*	1.67		
	Prob	0.888	0.152	0.02	0.001	0.106		
1998-2002	Coeff	20.57	- 2.33	- 2.54	0.773	0.799	0.660	0.546
	t-stat	2.72**	-2.24**	- 3.76*	1.977***	2.05***		
	Prob	0.02	0.04	0.00	0.07	0.06		

Note: *, ** and *** imply significance at 1, 5 and 10% levels respectively.

The results in table 2 show no tendency of conditional beta-convergence during the period 1990-2002 and 1995-2002. The GDP per capita of the beginning of the period doesn't have the expected sign and isn't significant. Meanwhile, in the time interval of 1990-1994 and 1998-2002, there is conditional convergence towards a steady state. Our variable of interest is significant at 1% and 5% respectively.

As far as other variables are concerned, government expenses are significant at 10% between 1990-2002, at 5% between 1995-2002 and finally at 1% between 1998-2002. Meanwhile the coefficient of this variable is negative, which contrasts with the expected sign. This is not very surprising in connection with the literature since many works have had a negative sign for government size (Landau, 1983, 1986, Barro, 1991a, 1991b, Easterly and Rebelo, 1993 Koester and Kormendi, 1989). Meanwhile the coefficients are larger than we would have expected. Dela Fuente (1997b) had a coefficient of similar size and thought of a problem of endogeneity. Other more precautionary investigations of de la Fuente (1997b) led to the conclusion that the results aren't seemingly influenced by a reciprocal causality. This means that an increase in the size of public sector seems to have an important negative effect on the level of GDP per capita, even when the factors of capital accumulation are considered (de la Fuente, 1998). This analysis remains dumb on the mechanism that causes the above raised effects.

Investments which represent a source of capital accumulation has the expected sign for all the periods and is significant at 1% in 1990-2002 and 1995-2002, and 10% in 1998-2002. This variable isn't significant between 1990-1994.

The dummy introduced to capture technological catch-up in certain economies of the grouping has the expected sign in all the periods. It is significant at 1% in 1990-2002 and 1990-1994 and at 10% in 1998-2002. The magnitude of the coefficient shows that the contribution of technology diffusion to the growth of the poor countries of the group was very important at the beginning of the period (around 88%) and regressed with time.

In general, our two models have helped to highlight the importance of economic cycles and unilateral and preferential reforms on absolute and conditional convergence expressed in terms of economic catch-up within the integration zone. We have also highlighted the contribution of technological diffusion within the grouping, of capital accumulation and of the weight of public sector to economic growth of the less advanced economies.

Meanwhile, judged on the basis of the adjusted $\overline{R}^2$, the performance of our models isn't very good. However, in the case of absolute beta-convergence, the value of $\overline{R}^2$ we obtained aren't far from those in the literature.

4.3 Sigma-convergence.

The main objective here is to know whether the economic catch-up phenomenon observed in some sub-periods in the CEMAC sub-region has enhanced the closing-up of development levels of member states in the grouping. In this respect, we have chosen a measure of inequality, which is the standard deviation of GDP per capita in the grouping. It helps to highlight the importance of the dispersion of development levels during the period 1990-2002 with respect to the year considered as the beginning of the period of the analysis.

The results of the calculation show that the trend of the closing-up of the standards of living of the different member countries of the sub-region was not constant. The years following the signing of the integration accords were characterized by a divergence of the standards of living of member economies, captured here by an increase in the standard deviation of GDP per capita from 1200 in 1970 to 2427 in 1975. The level of inequality in the sub-region thus remained high till 1985 when it started decreasing. Between 1985 and 1990, the standards of living closed-up at a speed of about 0.18% per year. This speed increased to 2.44% between 1990-1994 and finally to 3.4% in 1998-2002. It appears that the closing-up speed was rapid in the sub-periods where there has been economic catch-up between the poor and the rich countries of the group. This confirms the fact that beta-convergence is a condition for sigma-convergence.

5. Conclusion.

This paper aimed at testing the "convergence club" hypothesis in CEMAC at the down of waves of reforms of the 1980s and 1990s. It has investigated whether regionalism in CEMAC is bound by the characteristics of African economies to always experience divergence of income levels of member countries. An empirical model to test for absolute and conditional convergence was developed, and two convergence equations from a log-linear approximation to a simple growth model were derived. This model tries to capture the main immediate determinants of the growth of income per capita. The two equations were estimated for a panel of member states in the grouping under consideration.

With respect to absolute convergence, the results show that over the periods of analysis, our variable of interest, the level of GDP per capita at the beginning of the period has the expected sign. It is significant at 10% between 1990-2002, which is indicative of a weak economic catch-up between the less advanced, and the more advanced economies of the grouping. Between 1990-1994, absolute convergence is more pronounced since GDP per capita is significant at 1%. Meanwhile during 1995-2002, it has the expected sign but isn't significant. Finally, between 1998-2002, our main variable denotes absolute beta-convergence.

In general, the results of the estimation denote the importance of the unilateral as well as multilateral reforms in the integration zone. As such, the reforms undertaken by the CEMAC member states in the context of S.A.P and within the framework of the preferential liberalization have contributed to the narrowing up of the standard of living gaps in the sub-region. These results make the idea of convergence club based on the initial levels of productive technology and GDP per capita relative.

With regard to conditional convergence, the results in table 2 show no tendency of conditional beta-convergence during the period 1990-2002 and 1995-2002. Meanwhile, in the time intervals of 1990-1994 and 1998-2002, there is conditional convergence towards a steady state. Our variable of interest is significant at 1% and 5% respectively.

Concerning other determinants of growth, government expenses are significant at 10% between 1990-2002, at 5% between 1995-2002 and finally at 1% between 1998-2002. Meanwhile the coefficient of this variable is negative, which contrasts with the expected sign. This is not very surprising in regards of the literature since many works have had a negative sign for government size (Landau, 1983, 1986, Barro, 1991a, 1991b, Easterly and Rebelo, 1993 Koester and Kormendi, 1989). Also the coefficients are larger than we would have expected. Investments which represent a source of capital accumulation has the expected sign for all the periods and is significant at 1% in 1990-2002 and 1995-2002, and 10% in 1998-2002. This variable isn't significant between 1990-1994. The dummy introduced to capture technological catch-up in certain economies of the grouping has the expected sign in all the periods. It is significant at 1% in 1990-2002 and 1990-1994 and at 10% in 1998-2002. The magnitude of the coefficient shows that the contribution of technology diffusion to the growth of the poor countries of the group was very important at the beginning of the period (around 88%) and regressed with time.

With respect to sigma-convergence, the standard deviation of the GDP per capita of member countries in the sub-region at the beginning and at the end of the period was computed. The comparison of the two values of this inequality measure shed light on whether the dispersion of real per capita income across member economies tends to fall over time (σ - convergence).

The results of the calculation show that the trend of the closing-up of the standards of living of the different member countries of the sub-region was not constant. The years following the signing of the integration accords were characterized by a divergence of the standards of living of member economies, captured here by an increase in the standard deviation of GDP per capita from 1200 in 1970 to 2427 in 1975. The level of inequality in the sub-region thus remained high till 1985 when it started decreasing. Between 1985 and 1990, the standards of living closed-up at a speed of about 0.18% per year. This speed increased to 2.44% between 1990-1994 and finally to 3.4% in 1998-2002. It appears that the closing-up speed was high in the sub-periods where there has been economic catch-up between the poor and the rich countries of the group. This confirms the fact that beta-convergence is a condition for alpha-convergence.

In general our findings in this paper lend support to the "convergence club" defined according to policy choices rather than initial levels of human capital. They confirm our theoretical hypothesis that unilateral and preferential suppression of tariff and non-tariff barriers favors the convergence of per capita incomes and reduces the dispersion of real per capita income levels of partners in the sub-region.

The main economic policy implications of these findings are that more attention should be paid to open policies in all regional integration groupings that cover less advanced economies. The era of isolated tiny national economies has to give way to strategic alliances that harness knowledge and resource-based comparative advantages through integration. This however does not come effortless and at no cost. In the short run, a lot of dedicated and hard work must be put in first. Some decent economic reforms have already been going on. The next step should be to sustain the reform measures unilaterally as well as multilaterally. This would hopefully give a good chance to developing countries in particular to achieve convergent growth and halve poverty as envisaged.

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