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THE IMPACT OF FREE TRADE AND INSTITUTIONAL QAULITY ON ECONOMIC COMMUNITY OF WEST AFRICAN STATES TRADE

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Universiti Utara Malaysia

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By

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ABSTRACT

Regional and Economic integration has become an essential issue for Economic Community of West African States (ECOWAS). Despite the abundant research done on regional trade and its determinants, little has been done to examine the impact of free trade and institutional quality, particularly for ECOWAS, one of the most corrupt, less governed and politically unstable regions on the globe. The main objective of this research is to critically examine the impact of free trade and institutional quality on ECOWAS from 1985 to 2013 using gravity model of trade. Panel Unit Root were employed in order to test for stationarity of the series, Panel Cointegration was employed to test for long run relationship, Poisson Pseudo Maximum Likelihood Fixed Effect (PPML), and Dynamic Instrumental Generalized Method of Moments System and First Differenced (DGMM) were also employed to test further for long run relationship. The results indicate that ECOWAS is a regional force. High political instability and feeble governance have hindered ECOWAS trade performance over the years. Although trade openness and the old colonial and historical ties of ECOWAS have spurred regional trade inflows, financial openness has had a negative and significant impact on ECOWAS regional trade. The study suggests that ECOWAS must address the feeble institutional quality within the region; also, they need to proceed further to the next stage of integration in order to enhance trade, economic growth and development. The results highlight the fundamental significance of properly accounting for endogeneity and heterogeneity bias when trade policy effects are being evaluated.

Keywords: free trade, regional trade agreements, trade flows, ECOWAS

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ABSTRAK

Integrasi serantau dan integrasi ekonomi telah menjadi satu isu penting dalam Economic Community of West African States (ECOWAS). Walaupun terdapat banyak kajian mengenai perdagangan serantau dan faktor-faktor penentunya, namun kajian-kajian lepas hanya menfokus kepada impak perdagangan bebas dan kualiti institusi, seperti ECOWAS yang berada dalam kawasan dunia yang paling korup, tidak dikawal selia serta tidak stabil dari sudut politik. Kajian ini bertujuan meneliti secara kritikal impak perdagangan bebas dan pencapaian ECOWAS dari 1983 hingga 2013. Kajian ini menggunakan model Graviti untuk Punca Unit Panel bagi menguji kepegunan siri. Kointegrasi Panel pula digunakan untuk menguji hubungan jangka masa panjang, manakala Poisson Pseudo Maximum Likelihood Fixed Effect (PPML), dan Kaedah Dynamic Instrumental Generalized Method of Moments System and First Differenced (DGMM) turut digunakan untuk menguji hubungan jangka panjang dengan lebih terperinci. Hasil kajian telah menunjukkan ECOWAS adalah satu kuasa serantau yang terus menerus mengalami pelencongan perdagangan. Keadaan ini adalah disebabkan oleh ketidakstabilan politik yang berterusan, rasuah yang tidak dapat dibendung dan kelemahan tadbir urus. Walaupun keterbukaan perdagangan dan pertalian sejarah dengan kuasa colonial telah membantu ECOWAS untuk merangsang aliran masuk perdagangan serantau, keterbukaan tersebut turut memberi kesan negatif yang signifikan terhadap perdagangan serantau ECOWAS. Kajian ini mencadangkan bahawa ECOWAS perlu menangani ketidakstabilan insitusi ini di peringat serantau selain terus berkembang ke peringkat integrasi yang seterusnya bagi meningkatkan perdagangan, serta pertumbuhan dan kemajuan ekonomi. Hasil kajian menitikberatkan kepentingan untuk mengambilkira bias yang boleh disebabkan oleh faktor endogen dan heterogen (kemajmukan) dalam menilai impak polisi perdagangan.

Kata kunci: perdagangan bebas, perjanjian perdagangan serantau, aliran perdagangan, ECOWAS

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On a final note "O Allah, Owner of Sovereignty, You give sovereignty to whom You will and You take sovereignty away from whom You will. You honour whom You will and You humble whom You will. In Your hand is [all] good. Indeed, You are over all things competent. You cause the night to enter the day, You cause the day to enter the night; You bring the living out of the dead, and You bring the dead out of the living. In addition, You give provision to whom You will without account". May Allah bless us all AMIN.

Afolabi Luqman Olanrewaju

2016

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TABLE OF CONTENTS

TITLE PAGE

CERTIFICATION OF THESIS WORK……i

PERMISSION TO USE..... iv

ABSTRACT ……...…v

ABSTRAK vi

ACKNOWLEDGEMENT..... vii

TABLE OF CONTENTS ix

LIST OF TABLES xiv

LIST OF FIGURES xv

LIST OF APPENDICES xvi

LIST OF ABBREVIATIONS xvii

CHAPTER ONE INTRODUCTION 1

1.1 Background 1

1.1.1 An Overview of ECOWAS.....2

1.1.2 ECOWAS –Trade interaction (interregional and intraregional trade).....6

1.2 Problem Statement 14

1.3 Research Questions 19

1.4 Objectives of the study.....20

1.5 Significance of the study.....20

1.6 Scope of Study 21

1.7 Organisation of the Study 22

Universiti Utara Malaysia

CHAPTER TWO LITERATURE REVIEW 23

2.1 Introduction 23

2.1.1 Definitions and Types of Trade Integration 23

2.2 Regional Trade Agreement Definitions 24

2.2.1 Regional Trade Concept 25

2.2.2 Categories of Regional Trade Agreements 25

2.3 Theoretical Framework for Gravity Models 26

2.3.1 Trade costs under gravity model 41

2.3.2 Endogeneity Problem 43

2.3.3 Application of Gravity Models 44

2.3.4 The General Gravity Model of Trade 44

2.3.5 Gravity Trade under Country Specific 46

2.4 Institutional Quality and Trade Links 50

2.5 Empirical Review 53

2. 5.1 Trade Effect of Various Regional Trade Integrations 53

2.5.2 Trade Diversion and Trade Creation 57

2.5.3 Intra-Regional Trade and FDI 59

2.5.4 Regional Union and Development 62

2.5.5 Institutional Quality and Trade 67

2.6 Literature Gap 70

2.7 Conclusion 71

CHAPTER THREE 72

Universiti Utara Malaysia

3.1 Introduction 72

3.2 Model Specification 72

3.2.1 Import, Export and Trade Estimation Models 77

3.2.2 Export Model (Determinant factor and impact of free trade) 78

3.2.3 Import Model 79

3.2.4 Total Trade Model (Determinant factors and Free Trade) 80

3.2.5 Export Model (Institutional quality) 81

3.3 Explanation of the key variables 82

3.4 Method of Estimation 88

3.4.1 Pesaran Panel Unit Root Test 89

3.4.2 Pedroni Tests for Panel Cointegration 92

3.4.3 General Method of Moments (GMM) 95

3.4.4 First Difference GMM and Systematic GMM 98

3.4.5 One Step and Two Step System GMM 100

3.4.6 Justifications for Dynamic Panels 103

3.4.7 The Poisson Pseudo –Maximum Likelihood Estimator 104

3.4.8 Justification for using Gravity Model of International Trade 107

3.5 Synopsis of SWOT 108

3.6 Sample Size and Data Sources 109

3.7 Conclusion 110

CHAPTER FOUR 111

4.1 Introduction 111

Universiti Utara Malaysia

4.2.1 Estimation of the Gravity Model: ECOWAS Intra–trade (Export) 111
4.2.2 Stationarity of the Panel Series 111
4.2.3 Discussion of Results (Export Model) 115
4.3 Estimation of the Gravity Model: ECOWAS Inter-trade (Import) 123
4.3.1 Stationarity of the Panel Series (Import Model) 124
4.3.3 Discussions of Import Model Results 129
4.4 Estimation of the Gravity Model: ECOWAS Trade 134
4.4.1 Stationarity of the Panel Series (Trade Model) 134
4.4.2 Discussions of Trade Model Results 137
4.5 Estimation of the Gravity Model: Impact of Institutional Quality 142
4.5.2 Discussions of Institutional Quality Results (Table 4.7) 145
4.6 Conclusion 149
CHPATER FIVE 151
5.1 Introduction 151
5.2 SWOT Investigation 151
5.3 Evaluating Strengths 152
5.3.1 Market Size 152
5.3.2 Openness to Trade 152
5.3.3 Historical and cultural Benefit 153
5.4 Evaluating Weaknesses 153
5.4.1 Obstacle to Trade 153
5.4.2 Quality of Institutions 154

Universiti Utara Malaysia

5.5 Evaluating Opportunities 155

5.5.1 Economic Diversification 155

5.5.2 Trade Opportunities 156

5.6 Evaluating Threats 157

5.6.1 Political instability 157

5.7 Conclusion 157

CHAPTER SIX 160

6.1 Introduction 160

6.2 Summary 160

6.3 Policy Implication 163

6.4 Recommendation for Future Research 166

6.5 Conclusion 167

REFERENCES 168

Universiti Utara Malaysia

LIST OF TABLES

Tables **Pages**

Table 1.1: Shares of the World Exports and Imports of Various Regional Trading Groups across the Globe (1980–2015).....6

Table 4.1: Panel Data Unit Root Test Summary……106

Table 4.3: The Dynamic Gravity Panel and Poisson Pseudo-Maximum-Likelihood Estimation Results (1983-2013).....117

Table 4.4: Panel Data Unit Root Test Summary For Import Model.....120

Table 4.6: Dynamic Panel Data Model Using Gravity (1983-2013) 129

Table 4.7: Panel Data Unit Root Test Summary For Trade Model 132

Table 4.9: Dynamic Panel Data Model Using Gravity (1983-2013) 139

Table 4.12: The Dynamic Gravity Panel And Poisson Pseudo-Maximum Likelihood Estimation Results (1997-2013) ……153

Table 4.13: The Dynamic Gravity Panel and Poisson Pseudo-Maximum-Likelihood Estimation Results (1997-2013).....157

Table 5.1 SWOT Analysis Summary.....165

Universiti Utara Malaysia

LIST OF FIGURES

Figure **Page**

Figure1.1 Share of interregional Trading Groups to the World Market 8

Figure 1.2 Share of Foreign Direct Investment Inflow 9

Figure 1.3 Corruption Perception Index of ECOWAS (2005-2013) 11

Figure 4.1 Scatter Plot and Line of Best Fit for Export Versus GDP Combined 107

Figure 4.2 Scatter Plot and line of Best Fit for Export Versus Distance. 109

Figure 4.3 Scatter Plot and Line of Best Fit for Import Versus GDP Combined. 121

Figure 4.4 Scatter Plot and Line of Best Fit for Import Versus Distance. 122

Figure 4.5 Scatter Plot and Line of Best Fit for Export Versus GDP Combined. 144

Figure 4.6 Scatter Plot and Line of Best Fit for Export Versus Distance. 145

Universiti Utara Malaysia

List of Appendices

Universiti Utara Malaysia

List of Abbreviations

AEC	African Economic Community
AMU	Arab Maghreb Union
AU	African Union
ASEAN	Association of Southeast Asian Nations
COMESA	Common Market for Eastern and Southern Africa
ECOWAS	Economic Community of West African States
ECCAS	Economic Community of central African States
CEN-SAD	Community of Sahel –Saharan States
EAC	East African Community
EU	European Union
SACU	Southern African Customs Union
GDP	Gross Domestic Product
SITC	Standard International Trade Classification
RTAs	Regional Trade Arrangements

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RTAs	Regional Trade Agreements
EFTA	European Free Trade Agreement
CM	Common Market
CU	Custom Union
FTA	Free Trade Area
PTA	Preferential Trade Agreements
EMU	Economic and Monetary Union
NAFTA	North American Free Trade Agreement
UNECA	United Nations Economic Commission for Africa
UNCTAD	United Nations Conference on Trade and Development
SAP	Structural Adjustment Program
WAEMU	West African Economic and Monetary Union
WAMZ	West Africa Monetary Zone
WAMI	West Africa Monetary Institute
WTO	World Trade Organisation

Universiti Utara Malaysia

CHAPTER ONE
INTRODUCTION

1.1 Background

International economies have undergone a series of significant developments during the last few decades, including the formation and implementation of bilateral and regional trade agreements. A wave of trade liberalization is quickly reshaping the nature of cross-border transactions. With the re-emergence of neo-liberal philosophy in the 1980s espousing the removal of all forms of trade restrictions, most developing countries did an abrupt U-turn in their major policy thrusts to embrace neo-liberal economic development orthodoxy. In the early part of 1990s, the number of regional trade agreements increased and continued to grow. According to the World Trade Organization (WTO), regional trade agreements (RTAs) can be defined as reciprocal trade agreements among two or more partners and as of June 2014 about 585 notifications of Regional Trade Agreements (RTA) were received while 379 were in force (WTO, 2014).

This explosion of trade agreements was fuelled by several developments. The United States created the bilateral Free Trade Agreement (FTA) with Canada in 1987 and the North American Free Trade Agreement that included, Canada, Mexico and the United States in 1994, and the establishment of the European Union in 1993 helped fan the flames of free trade (Siggel, 2005). The General Agreement on Tariffs and Trade, which began in 1948, morphed into the World Trade Organization in 1995, and the number of RTAs that announced their intentions to joint increased rapidly (WTO, 2014) showing a

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