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Trade and development for Africa’s prosperity: action and direction

Issues note

A. The new policy context

1. Over the last seven years, Africa has consistently outperformed the world economy in terms of growth rates: the average rate in Africa has been 4.7 per cent per year, which is 1.7 per cent higher than that of the world economy. High commodity prices have been a key factor, and oil exporters in particular have grown at rates markedly higher than the regional average. However, greater macroeconomic stability, debt relief, increasing foreign direct investment (FDI) and, in recent years, higher aid flows have also played a role. A number of African countries have moved perceptibly toward reasserting ownership of their own development strategies. In parallel, Africa’s newly-revitalized continental and subregional institutions are poised to make positive contributions to the region’s renaissance. New forms of South–South cooperation and the new geography of international trade are also creating new opportunities as well as challenges for the continent.

2. The surge in economic growth throughout most of Africa has raised the hope that the continent has now passed a turning point. However, there is considerable risk as to the durability and sustainability of recent growth rates. Moreover, poverty remains a formidable challenge.

3. Sub-Saharan Africa is the only region where extreme poverty has been increasing. It is also the only region where, according to current projections, most countries will fall short of achieving the Millennium Development Goal (MDG) targets set for 2015. Employment opportunities are largely unavailable for the region’s predominantly young population, urbanization is accelerating, and the scourge of HIV/AIDS hangs ominously over millions of Africans.

4. Growth rates have to be further raised to a much higher level – a minimum of 7 per cent is the consensus view – and sustained at these higher levels for a considerable period, if significant reductions in poverty and the attainment of most MDG targets are to be realized. Moreover, it is necessary to promote a more inclusive type of economic growth. At present, the effects of growth on Africa’s poverty is limited, as key commodities such as oil and minerals are produced in capital-intensive industries with weak linkages to the rest of the economy. Agricultural productivity remains precariously low in many countries, and more and more farmers are working on ecologically fragile land. Climate change will aggravate this situation.

5. This high-level segment is an opportunity to re-examine the prevailing orthodoxy with regard to African development in the light of recent trends, new opportunities and emerging challenges. It is equally an opportunity to identify actions and directions for Africa’s prosperity with regard to trade and development.

B. Specific issues

6. Trade and development encompass a broad range of issues. This note highlights six, which, according to previous and ongoing research by UNCTAD, are critical for African development and enhancing the role of trade in that process: investment, official development assistance (ODA), trade, commodities, technology and migration.

7. These issues will be discussed separately. In practice, the relationship between trade and development in Africa is strongly affected by the interdependence of trade, financial flows, technology acquisition and migration. At the national level, sustained development depends on a strong investment–export nexus and the development of technological capabilities by domestic firms and farms in existing and emerging sectors. At the global level, the opportunities and challenges of the international environment depend on the interaction of the international trade regime and international financial architecture, including both private and official capital flows. International technology transfer and technology acquisition, which are becoming more and more important as international competition is increasingly knowledge-based, are also intimately related to trade, ODA and FDI. A development-oriented approach to climate change will inevitably bring the issue of technology transfer to the fore.

1. Investment

8. Africa’s weak economic performance over the long term is a reflection of inadequate investment and low productivity growth. Over the last 25 years, investment rates in sub-Saharan Africa have averaged around 18 per cent of gross domestic product (GDP), a performance that compares poorly to most other developing regions. There has been some upward movement in recent years, with the latest (2006) figures showing a rise to about 19.5 per cent. Further efforts need to be made to raise the rates to at least the 25–30 per cent range, which most experts agree are the levels that would help generate the higher growth rates needed for significant poverty reduction. While national development strategies would help set the guidelines for the sectoral allocation of capital expenditures, it is expected that due priority would be given to investment in the productive sectors – to raise production and productivity – and also to finance the expansion and improve the efficiency of infrastructure, including trade-facilitating infrastructure. There is now a New Partnership for Africa’s Development (NEPAD)-led effort to redress the relative neglect of these important sectors.

9. Africa has witnessed a rapid increase in inward FDI within the last four years, reaching a peak of about $40 billion in 2006. However, the region’s share of global FDI flows remains about 3 per cent, below its share in the 1970s. These flows are very much concentrated in a few countries and a few sectors. Although some countries –

such as South Africa, Morocco and Egypt – have managed to attract considerable external investment in manufacturing and for the acquisition of existing assets (mergers and acquisitions), the bulk of FDI going into Africa has been focused on the extraction of natural resources, particularly oil and gas. While there are signs of increasing investment in services, in particular in infrastructural services, the share of FDI in the manufacturing sector is on the decline, mainly as a result of the end of the Multi-Fibre Arrangement.

10. While FDI is important, a self-sustaining and dynamic investment process in a country requires both domestic and foreign investment. Both can be complementary, but complementarities do not emerge spontaneously and FDI often lags rather than leads domestic investment. Greater attention needs to be given, therefore, to domestic investment. Despite recent efforts to enhance domestic financial resource mobilization, very low domestic savings and weak domestic financial systems remain significant impediments to vigorous private-sector-led investment, growth and employment generation.

Issues

- What policy measures are necessary for enhancing domestic resource mobilization, improving the intermediation role of the domestic financial system and increasing levels of investment by domestic businesses? Are these different from those necessary for attracting FDI? How can Africa diversify investment into manufacturing and services sectors in order to create productive jobs for the growing urban population?
- How can Africa maximize its benefits from FDI, in particular in the extractive industries? That is, how can it ensure win–win outcomes in terms of higher incomes, job creation, forward–backward linkages in the domestic economy, transfer of technology (or technological upgrading), transfer of skills and know–how, and other positive spillovers?

2. Official development assistance

11. ODA remains a major source of financing for a range of developmental and poverty-reduction policy programmes in many low-income African countries. Despite recent increases, however, total aid flows in 2006 dropped by 5 per cent relative to 2005. Flows in 2006 represented only 0.3 per cent of Organization for Economic Cooperation and Development (OECD) Development Assistance Committee members' combined gross national income – far below the level required to fully attain the Millennium Development Goals by 2015. Only five countries have met or exceeded the United Nations target of devoting 0.7 per cent of their gross national incomes to ODA, and the challenge of meeting the Group of Eight (G8) Gleneagles commitment to double aid to Africa by 2010 and reducing the volatility of aid persists.

12. One ODA-related area where major progress has been recorded is that of debt relief. There has been significant forward movement on bilateral debt write-off under the enhanced Heavily Indebted Poor Countries (HIPC) Initiative and more recently on multilateral debt relief under the Multilateral Debt Relief Initiative (MDRI). But one consequence of the progress made in this regard is that much of the increased flow of ODA has been diverted to the financing of debt relief. Thus, the recent growth in ODA has so far not translated into significant additional financing of development programmes and projects. Much of the incremental resources were channelled to debt write-off and emergency relief.

13. Macroeconomic conditionality and advice are leading to a situation in which much of the aid which is actually received in a country is being used to build up international reserves or pay off domestic debts. The amount available to do real

things on the ground within African countries is thus much less than the amount which donors actually disburse and record as such. This calls for serious discussion at the various forums available for this purpose.

14. In addition, for a number of years, a major focus for ODA has been support of the social sectors; the adoption of the MDGs has further reinforced the primacy of these sectors. It would be both timely and appropriate to re-examine such a stance with a view to also giving due attention to investment in infrastructure as well as in productive sectors. Otherwise, there is a danger that the debt problem will simply recur in the future. But if aid inflows are doubled and used to build up the productive base of African economies, both aid dependence and debt relief dependence can rapidly end.

Issues

- Does the Paris Declaration on Aid Effectiveness address all the issues involved in enhancing the development effectiveness of ODA?
- Is there a need to re-balance the composition of aid?
- How is it possible to achieve greater domestic ownership of policies? Can the demands made by donors be reduced? What types of conditionality are reasonable?
- What role can new donors – from China and other rapidly industrializing countries – play in supporting Africa's development efforts?

3. Trade

15. African economies are generally open. The ratio of trade to GDP in sub-Saharan Africa was equivalent to 69 per cent in 2006, up from 50 per cent in 1991. Equally, tariff barriers are below 15 per cent in most countries. This follows deep and sustained policy reforms over an extended period from the mid-1980s, which have included trade liberalization policy conditionality outside the framework of multilateral negotiations. But despite the high level of openness, African participation in world trade is small and declining. Africa's share of global exports declined from about 6 per cent in 1980 to about 2.7 per cent in 2006.

16. To reverse this pattern of integration-with-marginalization, action is required at national, regional and global levels. At the national level, it is clear now that trade liberalization in itself is insufficient for export development and in particular export diversification. Trade liberalization has reinforced commodity dependence. While the attempts of a number of countries to actively promote non-traditional exports should be acknowledged, diversification would require more determined and long-lasting efforts aimed at moving into activities that have more solid prospects for sustained export growth, domestic value adding and employment generation. Investing in trade-facilitating infrastructure, formulating development-oriented trade policies, export promotion, reforming trade-related regulations and building technological capabilities are among the key steps to be taken to stimulate export growth and improve competitiveness.

17. Regional integration has long been recognized both as the obvious means of binding Africa's small economies together into larger and more viable single markets, and as a stepping stone toward integration into the global trading system. Expanding regional markets by strengthening and deepening African regional integration schemes has thus been a continuing feature of the continent's trade and development agenda. In line with this, Africa's subregional economic communities have all placed priority emphasis on trade integration. Most are in the process of liberalizing their intraregional trade and tariff systems within the framework of free trade area agreements or customs unions. However, in terms of concrete results, cross-border

trade has seen very little growth, mainly due to the persistence of non-tariff and administrative barriers, as well as the inadequacy of essential cross-border infrastructure. The lack of significant progress on the harmonization and rationalization of Africa's numerous integration schemes also complicates and inhibits intraregional trade.

18. With the continuing stalemate of the Doha Round of trade negotiations, the problems Africa faces in the global trading environment are expected to remain unresolved for a while. No action has yet been taken on the commitments undertaken at the 2005 Hong Kong (China) Ministerial Conference to eliminate export subsidies and reduce domestic support – with respect to cotton first and foremost, but also, in due course, for agriculture in general. Thus, Africa's cotton exporters continue to be disadvantaged by the international community's failure to implement the Hong Kong (China) consensus. The barriers to market access for non-agricultural exports, including tariff escalation and peaks, remain unresolved. Meanwhile, non-tariff barriers – in particular ever-stricter technical standards and expanding and more stringent environmental and sanitary requirements – have in effect become insurmountable obstacles to accessing OECD markets.

19. In parallel to the Doha Round of multilateral talks, there have been ongoing negotiations to conclude Economic Partnership Agreements (EPAs) between the European Union and various subregional groupings of sub-Saharan African countries. But the current status and eventual outcome of the EPA negotiations appear to be quite fluid.

Issues

- What are the costs and benefits of non-reciprocal market access for poor African countries? What would be the costs and benefits of the EPAs under the current proposals on the table?
- How can the Doha Round maximize the benefits and minimize the costs of external integration for African countries? How can the impact of non-tariff barriers and contingency trade protection measures on African countries be mitigated?
- What is the role of Aid-for-Trade?

4. Commodities

20. The current boom in the demand and prices of primary commodities has been a welcome development for African commodity producers. Analysis by UNCTAD indicates that the prices of all commodities increased by nearly 90 per cent in dollar terms or 66 per cent in special drawing rights (SDR) terms between 2002 and 2006. The largest increase was for minerals and metals as a group, but although there were some significant exceptions such as cotton, most products in other categories also saw significant price rise. The major emerging economies' growing demand for oil, gas, other minerals and agricultural raw materials is the underlying reason for the boom.

21. While the outlook for commodities is encouraging, the actual benefits accruing to African countries depend on their share of revenues within the marketing system or value chain. Global supply or value chains have increasingly become important players in commodity trade. Among global commodity chains, Northern-based buyer-driven chains have been gaining more power and more say as to the distribution of value along the chain. As a result, producers and other second-tier participants are increasingly being marginalized. The enforcement of stringent quality standards has contributed to the consolidation of the powers of buyer-controlled chains. At the same time, in developing countries, the dismantling of marketing boards and related market liberalization measures have resulted in weakening producers. The demise of international producer–buyer commodity organizations also had the same effect.

22. With the new scramble for energy and minerals, host countries of extractive industries are increasingly able to negotiate revisions in their contractual agreements with transnational corporations in order to improve their ownership position and to ensure that they get higher shares of the revenues. But they do not necessarily have the information or capacity to renegotiate successfully. Producers of some other commodities have also managed to work out improved terms with their buyers by successfully carving out niche markets, through branding and by branching out into the supply of specialty products. But these are more the exceptions than the rule, as the majority of producer countries and commodities are still subject to buyer-dominated value chains.

Issues

- How can the commodity windfall be used to achieve sustainable development?
- What measures can further strengthen the participation of African countries in South–South trade in commodities?
- What international commodity initiatives can be envisaged to assist African commodity producers?

5. Technology

23. African countries will be increasingly marginalized if they do not increase the knowledge content of their economies and diversify them through learning and innovation. But the technology gap between many African countries and the rest of the world is increasing, and science, technology and innovation capabilities in sub-Saharan Africa, with the exception of South Africa, are very weak. These countries are deeply integrated into the world economy through trade, but technology diffusion and acquisition through international market linkages remains very weak.

24. Technological development is necessary, both within and outside agriculture. Promoting a Green Revolution in basic staples should be a top priority for many African countries. This requires enhanced national and local agricultural research and development. But international competitiveness in manufacturing and services sectors also depends on building technological capabilities in domestic firms. At the early stages, this does not necessarily mean creating products and processes which are new to the world, but rather the effective learning about technologies and technological practices already in use in more technologically advanced countries. However, there may also be a role of developing new “bottom-of-the-pyramid” products which specially cater to the effective demand of poor people.

25. Technological development has long been identified by Africans as a key priority for African development. Through its Consolidated Plan of Action for Science and Technology, NEPAD has identified a common vision, objectives and principles for action. But the international community is only slowly integrating the importance of building science, technology and innovation (STI) capabilities into its support for Africa. Aid for STI is minimal and the elements of a development-friendly intellectual property rights regime are still a contentious issue.

Issues

- How can African Governments integrate STI issues into their development and poverty reduction strategies and stimulate technological catch-up with the rest of the world?
- How can development partners increase aid for science, technology and innovation, and also facilitate technology transfer and the development of local technological capabilities?

- What is the role of South–South cooperation in this process?

6. Migration

26. International migration from Africa to other regions, in particular to developed countries, has increased strongly since the early 1990s and is an emerging area of concern. Migration has both positive and negative consequences for African countries. On the positive side, remittances, if channelled to productive investment, can contribute to long-term growth. Officially recorded remittances to sub-Saharan Africa were estimated at $11 billion in 2007. On the negative side, brain drain can have dire consequences for long-term development prospects. If properly managed by home and host country Governments, the negative effects of international migration could be minimized and its benefits maximized for both groups of countries.

27. Dialogue at the highest political levels may help address the many dimensions of South–North migration. In fact, migration was a major point of discussion at the recent Africa-European Union Summit (Lisbon, December 2007). Even without returning, African Diasporas can effectively participate in the continent's development if appropriate mechanisms are created to harness this largely untapped resource. The African Union, which plans to place the African Diaspora on a par with each of its territorial regions, has been conducting active consultations on strategies aimed at the productive utilization of this external resource.

Issues

- How can both the home and host countries of migrants (legal and illegal) manage migratory flows in a more sustainable and humane manner?
- What policies can host countries adopt to reduce the costs of brain drain in Africa?
- How can commitments on the temporary movement of natural persons (under Mode 4 of the General Agreement on Trade in Services (GATS)) contribute to brain gain, brain circulation and knowledge diffusion in Africa?
- What measures can African countries and host countries adopt to maximize the development impact of remittances?

C. Action and directions

28. African countries and their development partners (traditional and newly emerging bilateral partners as well as multilateral institutions) each have roles in terms of actions to be taken.

29. The primary responsibilities of African countries are to (a) re-examine, re-formulate and implement the strategies, policies and other measures needed to raise their growth rates; (b) promote productivity growth, diversification and export upgrading; (c) create productive employment opportunities; and (d) improve human well-being in line with the achievement of the MDGs. The lessons from the past indicate that a one-size-fits-all approach is counterproductive. There is a need to design development strategies appropriate for specific country contexts and to build the "good enough" governance capabilities which are required to implement such strategies. International trade must be a central element in development and poverty reduction strategies because trade facilitates the key processes of capital accumulation, technological progress and structural change which drive development. These processes are also behind the expansion of productive employment opportunities and rising household incomes. But an integration strategy for linking the national economy with the global economy should not be understood as a substitute for a development strategy. Integration should not be an end in itself, but rather serve the purpose of development.

30. The primary responsibility of development partners is to live up to the commitments of global partnership for development. This means following through on pledges concerning quantity and developmental quality of aid. There is no point in scaling up aid if it is linked to development and poverty reduction strategies which are inappropriate for specific country contexts. This will simply squander the window of opportunity opened by the recent debt relief initiatives and commodity boom. Also, openness to African voices and to African alternatives will greatly enhance development effectiveness in Africa. This means that development partners should provide African countries with the policy leeway to experiment with new approaches, and the space for homegrown development strategies.

31. What globalization means in practice is that development prospects are increasingly dependent on international economic relations of all kinds. African Governments need to elaborate outward-looking development strategies, which take advantage of the opportunities of globalization. At the same time, development partners need to ensure that the international environment enables, rather than constrains, African development. This requires a supportive approach in each of the individual areas of investment, aid, trade, commodities, technology and migration. But beyond this, there is a need for a more joined-up approach to global governance so that actions in specific fields are not counteracted by actions in others, and positive synergies are maximized.

32. As already indicated, the rapid rise of China – and other emerging economies such as India and Brazil – has created actual or potential new markets for African exports, and resulted in increased demand and higher prices for African commodities. The proposed new supply chains involving Africa and some of these new partners could provide more equitable alternatives. At the same time, new investment partnerships are being established. ODA from China is growing in both volume and scope. These and other advanced developing countries (including those that have already acceded to OECD membership) could specifically implement the Hong Kong (China) Ministerial Conference's call for duty-free and quota-free market access and take other new or similar initiatives in support of African countries in general and the least developed countries in particular. It would be a welcome and timely gesture if such initiatives could wholly or partly be aimed at supporting the trade and development agenda of African countries. In addition, it might be appropriate to consider the involvement of the sovereign wealth funds of emerging countries in investment in Africa. The magnitude of these funds and their projected growth are such that the portion earmarked for investment in Africa would be relatively small. But their impact on African development could be considerable. The know-how and expertise available in the private or public sectors of some of the advanced developing countries could be partnered with the financial resources of the sovereign funds to undertake many priority development projects in Africa.

33. The division of responsibilities among multilateral institutions, with respect to assistance to African development, could also be reassessed. The role of UNCTAD in supporting African countries in policy analysis and capacity-building in the areas of trade and development could be further strengthened. Where and when Governments so request, UNCTAD could provide more enhanced and targeted technical assistance and advisory service in the many areas of its unique and special expertise – including investment promotion, trade negotiations, dealing with value chains, export promotion, competitiveness and diversification.