Policy Brief

Perspectives on African Trade Performance and Policy and the Role of the Multilateral Trading System

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Executive Summary

- Africa is on the brink of an economic transformation, and its quality and speed largely depend on policy, the way it is implemented, and the quality of governance.
- In recent years, Africa has grown faster than the world economy and gained in shares of both global GDP and trade, and the challenge is to sustain this trend.
- Commodities dominate the composition of the continent's export base and greater diversification would reduce vulnerability, establishing a platform for Africa's structural transformation.
- The bulk of Africa's trade is geographically concentrated in three markets, and a major opportunity exists for expanding intra-continental trade, which is still little more than one-tenth of total exports.
- Product and geographical concentrations will lessen as domestic economies pick up the pace of diversification from primary commodity production towards manufacturing and services.
- Africa's economic transformation will depend crucially on access to knowledge and technology, and amongst its other attributes, trade is a useful transmission mechanism.
- Increased participation in global and regional value chains allows countries to specialize, add more domestic value and upgrade product sophistication in ways that were previously not possible.
- Good policy design and efficient implementation are essential if governments are to shape progress, helping rather than hindering growth and development.
- The centrality of markets is essential for growth, development and job creation, but policy can contribute as an enabler and in shaping outcomes to meet certain social and economic ends not provided by the market.
- Virtually all governments seek to shape their economies with what are sometimes referred to as industrial policies, but success depends very heavily on the quality of interventions and government capabilities.
- African countries, like many elsewhere, could do much to create a more conducive macro-environment with better infrastructure, and less cost-ridden policy conditions, in order to foster trade, development and growth, including through strengthened intra-African links.
- China's experience of dramatic growth and transformation over three decades has showcased what is possible, at a relatively early stage of economic diversification, with a judicious mix of incentives, facilitated trade, learning, and entrepreneurship.
- Commitment to WTO core values is critical for the structural transformation of Africa.
- WTO accession packages can be a blueprint for long-term policy reform.
- The WTO can serve as an anchor for coherent domestic policy as well as a guarantor of consistent and non-discriminatory policies on the part of trading partners.

Introduction

Africa is hosting a WTO Ministerial Conference for the first time. The decision by WTO members to hold the organization's tenth such gathering in Africa testifies to the continent's growing role in the global economy. Many parts of Africa are on the brink of a transformation. How fast and how successful that transformation turns out to be will depend in no small part on choices made by governments. It will also depend to a degree on the external environment.

The Ministerial Conference, along with the Fourth China Round Table, provide a good occasion to take a step back and reflect on Africa's trade experience and its relationship with the multilateral trading system. What are the continent's achievements and challenges? This policy brief considers these questions, based largely on a series of papers commissioned for the Fourth China Round Table.

A word of caution is in order at the outset. Africa is a very large and diverse place, home to a broad spectrum of realities and experiences. Talking of the continent as a whole inevitably means that we have to focus on communalities, not differences, and some of what is said will be more applicable to some African economies than others.

Africa's trade performance, opportunities, and structural challenges

Trade is a reflection and cause of the health of the domestic economy. In the twenty-first century, Africa's economy has grown at an average of 5 per cent per year, outpacing global GDP growth by a significant margin.

Ten of the 16 fastest growing economies are in Africa. In the last twenty years, Africa's share of global production has risen by 30 per cent and its share of trade by more than one-third. The continent's share of world foreign direct investment has doubled.

These expansion rates are built from a very low base. But they are indicative of an Africa on the move.

In terms of the destination of exports, Africa's trade is skewed against the continent. Only about 10 per cent of Africa's trade is with itself. The lack of intra-African trade represents a significant loss of opportunity.

The continent's core trade destinations are China, the EU and the United States, who between them take a very large share of the total. Just as product diversification of exports is desirable, so too is greater geographical dispersion.

Africa's trade performance has been driven to a large degree by oil and other commodity exports. The commodity price boom fed trade growth. Recent price developments will reverse some of those gains.

Commodity dependency in trade points to a structural challenge facing many African economies. They need to diversify into manufacturing and services, thus building greater economic resilience at home and trading opportunities abroad. Manufacturing and services also provide vital conduits for adding more value domestically, contributing to growth, development and employment.

Some, but by no means all, African economies have already embarked on the path of diversification, building manufacturing capabilities and fostering services activities. It has been estimated that only one-third of Africa's GDP growth record is attributable to economic activity in the natural resource sector.

This suggests that a diversified domestic platform is emerging in a number of economies. If domestic industrial and service industry growth is competitive or has the potential to become so, the diversification can spread to exports. If such activities are uncompetitive, they will eventually be a drain on the entire economy.

Significant trade and diversification opportunities have emerged in recent years with the development of vertically integrated production structures that span multiple borders. Global value chains (GVCs) allow countries to specialize in specific production lines without having to produce entire products.

These opportunities for component trade in both goods and services offer new scope for adding value domestically. This is especially relevant in primary commodity production in Africa, where instead of exporting primary products largely in their raw form, further value can be added prior to exportation.

Another genre of GVCs does not determine where to locate on the basis of the presence of underground resource deposits or farming land, but simply on the basis of a favourable operating environment. The challenge in the case of both resource-based and footloose global value chains is for local producers to become involved in a continuing process of upgrading and ultimately the establishment of home-grown, internationally oriented lead firms.

The policy challenges

Strictly speaking, no such thing as policy neutrality exists. Even where a country decides not to intervene in the market, it is effectively taking a policy decision. If there is no escaping policy, it makes it doubly important to ensure that policies are sound and conducive to progress.

Too often, policy can become a millstone around the neck of growth and development. This can be for three main reasons. One is to do with policy design. Either through neglect or poorly formulated policies, costs in the economy are needlessly increased. A second problem may be poor implementation because of a lack of adequate resources, or adequately trained resources, which leads to inefficiencies and added costs.

A third problem can be corruption, which adds costs to production in a variety of ways. It is within the powers of governments to address all these shortcomings and make their own, policy-based contribution to productivity and growth.

In broad terms, policy reform may occur under three different guises. Some policies are enabling or facilitating, in the sense that they remove what might be considered inadvertent costs to doing business. Trade facilitation, customs reform, streamlined regulation, and investment in human and physical infrastructure are among the instruments of enablement.

The second kind of policy reform involves removing or adjusting policies deliberately put in place in pursuit of specific economic, political or social objectives. These policies may have become outdated in terms of their original purpose. Or they may reflect errors of judgement, such as an excessive reliance on import-substituting industrialization, which was a feature of early industrialization efforts in some countries.

The third kind of reform involves bringing new policies to bear. This may respond to changed circumstances or past neglect. In some cases too, new policies might be introduced. Like anywhere else, policy change in Africa is bound to involve a combination of these three kinds of change.

The idea that prosperity born of growth and economic progress is assured with as little policy intervention as possible is more ideological than scientific. It is clear there can be too little or too much intervention.

The reasons for intervention may stem from the external consequences of transactions that are unpriced or incorrectly priced in the market. These so-called externalities and other kinds of market failure may have good or bad consequences, but they both warrant intervention.

This discussion is related to so-called "industrial policy", which has sparked fierce debates, often with a certain ideological overlay. There is nothing wrong in principle with governments deploying policy levers to change resource allocation decisions in an economy. Virtually all governments do it.

The challenge is to do it well. This means that the objectives must be clear and the policies well designed for efficiency and monitored. Adequate government capabilities are a prerequisite for the successful conduct of industrial policies, as is adequate information and analysis for understanding cause and effect.

In Africa's case, as elsewhere, plenty of scope exists for improving and streamlining the regulatory framework for doing business. In other cases too, there will be justification for lessening the impact of certain interventions. It is argued in some quarters, for example, that import tariffs tend to be too high in some sectors.

As far as intra-African trade is concerned, moves are afoot to loosen some of the barriers to exchange across the continent, be they of a fiscal or regulatory nature. These are the ideas driving regional integration initiatives. At the same time, efforts will be needed to enhance continent-wide infrastructure in order to facilitate and lower the costs of transport and communications in particular.

The experience of China in transforming itself into a major global powerhouse in the space of 30 years is instructive. The early model relied largely on combining labour and capital (much of it foreign), and exporting the product. Low wages and a facilitated operating environment were crucial to this success.

Increasingly China has allowed wages to rise and shifted emphasis towards production for the domestic market. This broadening of the production base and domestic consumption opportunities has also been accompanied by an emphasis on the services economy. China's experience and elements of the policy frame it adopted could be instructive for countries in Africa wishing to pursue a similar path.

The role of the WTO

Just as African countries have tended to maintain quite high tariffs on many products, they have been reluctant to commit to maximum tariff levels through WTO "bindings". Where there are bindings, these are often set at levels considerably higher than the relevant applied tariffs. Several reasons can be adduced as to why this may be so, but it does deny the countries concerned an opportunity to use internationally negotiated commitments as a means of locking in policy.

Apart from any gains countries might enjoy as a result of tying down their policy commitments through international obligations, they can also rely on the WTO's system of rules for protection against discrimination and other non-conforming policy behaviour. These possibilities help to level the playing field and ensure a greater degree of certainty regarding the external policy environment.

Many African countries did not accede to the GATT – the WTO's predecessor – through a negotiation. Rather they were "successor" members of the organization following their political independence from colonial powers.

Those countries in Africa and elsewhere that accede to the WTO through a negotiation are frequently required to undertake far-reaching reforms. They benefit from such reforms in various ways, including the enhancement of capacity to compete. African countries that have not been through this process might consider adopting long-term reform programmes similar to a WTO accession package.