Aid for Trade: Building on Progress to Date

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Aid for Trade: Building on Progress Today for Tomorrow’s Future

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Summary and Recommendations

Aid for trade is financial and technical assistance that facilitates the integration of developing countries into the global economy through initiatives that expand trade. By furthering economic growth and development, the benefits of aid for trade are shared by all trading nations. This includes not only the poor in least developed and other low-income countries, but also citizens in middle income countries and those in the most developed nations of the globe. Trade benefits all nations.

Examples of aid for trade include the financing of transportation and logistics infrastructure (infrastructure is the largest share of official development assistance in aid for trade), assistance to help firms conform to international product standards, capacity building in border management, and implementation of projects that connect rural producers to markets. Aid for trade also spans measures to assist workers, producers and communities in adjusting to changes in trade policies or the terms of trade (e.g., as a result of erosion of trade preference programs).

The global initiative on aid for trade was launched at the 2005 G8 meeting in Gleneagles, Scotland, where leaders committed to a near 50 percent increase in aid for trade funding by 2010 (to US$4 billion). Since 2005, donors and multilateral development banks have increased the overall value of aid for trade and put in place several mechanisms to both channel such aid and to

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1 This paper was prepared for a G-20 / World Bank conference in Busan, Korea, June 4, 2010 and draws on a work program supported by the DFID-funded Global Trade and Financial Architecture project and “Trade Costs and Facilitation project supported through the Multi-Donor Trust Fund on Trade. The authors are respectively, Sector Director, International Trade Department and Lead Economist, Development Research Group. The findings, interpretations, and conclusions expressed here do not necessarily reflect the views of the Executive Directors of The World Bank or the governments they represent. We are grateful to Elisa Gamberoni and Richard Newfarmer for valuable inputs; Shahrokh Fardoust and Ann Harrison for comments on an earlier draft and Marco Antonio Martinez Del Angel, Alberto Portugal Perez and Benjamin J. Taylor for excellent assistance in the preparation of this paper.

2 See http://en.g8russia.ru/docs/16.html. At the December 2005 WTO Ministerial in Hong Kong, a new WTO Aid for Trade Task Force was created to provide recommendations to the WTO Director-General on how to best “operationalize” aid for trade. The Ministerial Declaration also included explicit references to the importance of aid for trade to assist least developed countries (LDCs) “to build the supply-side capacity and trade-related infrastructure that they need to … implement and benefit from WTO Agreements and more broadly to expand their trade. WTO “Hong Kong Ministerial Declaration,” doc wt/MIN(05)/W/3/Rev.2, 18 December 2005.
ensure that it reflects and addresses national priorities. The commitment to aid for trade has been re-iterated repeatedly by major donors at global aid for trade review meetings hosted by the WTO in 2007 and 2009 and in G-8 communiqué. The G-20 Summit in London in April 2009 included a statement of continued support for implementation of the commitments made on aid for trade by members. Delivering on these commitments is particularly important in the current global economic situation: aid for trade that results in improvements in productivity of firms and farmers in poor developing countries can both assist countries in recovering from the crisis and enhance longer-term growth and development prospects.

This paper reviews recent trends in the delivery of aid for trade, its allocation by country and type of assistance and analyses of impact and effectiveness. Since 2005, significant progress has been made by bilateral donors in implementing aid for trade commitments and by developing countries in identifying aid for trade priorities. However, there is still insufficient awareness and understanding in the broader development community of what the aid for trade initiative entails and how it works. There is also very limited data and analysis on the impact of aid for trade on the ground. The G20 is uniquely placed to provide greater clarity on where the aid for trade agenda is moving and how it is being shaped.

By design, there is no central entity or global financial coordination mechanism that takes the lead on or is the focal point for delivering aid for trade. Instead, aid for trade is supplied through existing country-based allocation mechanisms by bilateral donors and international development agencies. The primary vehicles used to raise awareness and monitor progress in delivery of aid for trade by donors are the Enhanced Integrated Framework (EIF) for trade-related technical assistance to the least developed countries (LDCs) and regional and global aid for trade reviews co-organized by the WTO. The main objective of the EIF is to assist LDC governments in identifying trade projects that can be considered in the overall process of defining aid allocation priorities at the national level. The country-centric approach is a major strength of the program. It helps ensure that aid targets priorities identified by governments. However, the recipient country-cum-donor community-centric focus of the initiative reduces the potential impact of the enterprise. Developing mechanisms and concrete initiatives that involve transfer of resources from middle income G20 members (investment, knowledge) as well as the private sector of all G20 members could do much to enhance the effectiveness of aid for trade in supporting trade and employment growth in low-income developing countries.

G20 leadership can make a major difference in enhancing the effectiveness and visibility of the aid for trade effort. In addition to delivering on the financial commitments made in the past, four specific areas are identified for priority consideration by the G20 in this paper:


4 In contrast to other areas recently identified as priorities for development assistance at a global level – such as the Global Agricultural and Food Security Program (GAFSP) established in 2009 with earmarked funding of $1 to $1.5 billion to scale-up agricultural assistance targeted to the food security of low income countries – donors decided there was no need for such a mechanism in the trade area.

5 There have been two global reviews to date, in 2007 and 2009.
(i) Providing a strategic action plan for capacity-building and transfer of knowledge on policies and regulatory options to improve the efficiency of producer services and the rate of return on infrastructure investments;

(ii) Promoting market access for low income countries through a commitment by all G20 members to eliminate import restrictions for LDCs, thus stimulating South-South trade;

(iii) Creation of a new “aid for trade public-private partnership” to leverage the dynamism in the private sector for strengthening trade capacity in the countries that most need it; and

(iv) Launching a G20 strategic global initiative to provide dedicated financial support for monitoring and evaluation of aid for trade – anchored in systematic data collection, research, and analysis.

Why aid for trade matters

A key rationale for launching the aid for trade initiative was that firms in many developing countries may be unable to benefit from existing and prospective market access opportunities that the trading system or specific countries/regions offer – such as preferential (duty-free, quota-free) market access. Poor quality infrastructure and high trade and other operating and transactions costs in particular act to block many of the advantages of reduced barriers to trade achieved in international and bilateral market access talks. A major feature of most aid for trade is that it is aimed at lowering costs and enhancing the productivity of firms in recipient countries. By focusing on boosting investment in infrastructure and complementary measures to create the preconditions for improved access to higher quality, lower cost public and private services, aid for trade can help countries to capture more of the benefits of existing market access opportunities.

The need for G-20 leadership on aid for trade is heightened in the current economic environment. There are at least three reasons for this:

- Trade is a powerful mechanism to help countries overcome the shock of the crisis. Given the lack of progress in bringing the WTO Doha Development Round to closure, G20 leadership would provide an important signal that the major players in the world economy recognize the importance of taking actions to expand trade.
- Aid for trade can help countries diversify into new markets and products—helping poor countries benefit from the emergence of a multi-growth pole world economy.
- Aid for trade, allocated effectively, can improve productivity in recipient countries by lowering costs and enhancing competitiveness, thereby enhancing growth prospects.

Trade is a channel for poor countries to recover from the downturn. As economic activity and demand recovers from the financial crisis, consumers and enterprises in importing countries can be expected to be even more sensitive to prices of the goods and services they buy than before. Aid for trade that supports measures to improve the competitiveness of countries with weak trade capacity is therefore important. Moreover, as fiscal and monetary stimuli are gradually

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withdrawn, aid for trade can help maintain demand for goods and services and attract investment in tradable activities. Thus, aid for trade can provide a boost to developing countries during a period when they sorely need it. 7 It can also help reduce pressures for protectionism and increase support for trade reforms in developing countries, further expanding trade prospects by helping to keep markets open globally.

**Aid for trade can help increase diversification.** Trade openness gives rise to risks as well as benefits. The recent crisis was exceptional in being truly global in scope: all countries were negatively affected. However, the crisis also illustrated once again that more diversified economies do better than those that rely on just a few products or markets as the source for their foreign exchange. Diversification can help reduce output volatility (Haddad, Lim and Saborowski, 2010). Many low-income countries are not well diversified – in part because of high trade and other costs that aid for trade can help reduce.

**Aid for trade can enhance productivity in low-income countries.** There is a long-standing debate regarding developing countries’ capacity to effectively absorb increased flows of aid. Allocating assistance to enhance trade capacity can help avoid the macroeconomic problems that can arise as a result of ODA inflows by focusing on lowering trade and other transactions costs and improving the productivity of the economy as a whole. This can act to offset negative competitiveness spillovers generated by aid inflows such as Dutch disease and pressures for real appreciation.

As Reis and Farole (2010) note, the post-crisis “competitiveness policy framework” should tackle the priorities of aligning macroeconomic incentives (e.g.: trade barriers, real exchange rates and labor market policies), reducing at-the-border and behind-the-border trade costs, and overcoming government and market failures (e.g., shortages in trade finance, stimulating technology diffusion, improving product standards). Aid for trade can help low-income countries address this agenda – without targeting specific industries or potentially distorting policies to support product-specific investments. It can do so by improving trade policy coordination; trade facilitation, skill formation, trade-related infrastructure; and administrative procedures (Cali and te Velde, 2008).

**Trends in Aid for Trade**

What is aid for trade? The OECD compiles statistics on official development assistance (ODA) in support of trade. These data distinguish between the following broad categories of support: (1) technical assistance for trade policy and regulations, (2) productive capacity building (including trade development), (3) trade-related infrastructure, and (4) trade related adjustment. Examples of support to trade policy and regulatory reform include projects at the country level to harmonize regulations to international norms. Capacity building and trade development include projects to assist in diversification of exports. Trade-related infrastructure projects include roads, ports, and telecommunications network investments. Trade adjustment assistance involves aid to

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7 Even considering increased aid flows and commitments over the past several years, the World Bank estimates that developing countries confronted a financing shortfall of between US$270 billion and US$700 billion in 2009. External financing needs for developing countries are likely to increase because of the fallout of the crisis.
help with costs associated with trade liberalization, including tariff reduction and preference erosion, for example.

According to the data reported by the OECD, some 25 percent of ODA was directed toward aid-for-trade in 2008, and about 35 percent of aid that donors and governments allocated to particular sectors.8 Bilateral donors provided low-income countries, including LDCs, with about US$15.6 billion in aid for trade in 2008. This amounted to some 40 percent of the total US$39 billion in concessional aid for trade commitments in 2008. The LDCs received about one-fourth of aid for trade commitments. Donors provided about half of aid for trade commitments to middle income countries, mostly from bilateral sources.

The supply of aid for trade has increased over the 2002/2005-2008 period by 21 percent in real terms. Low-income countries saw their share of total aid for trade increase from 44 to 54 percent, while 59 percent (US$ 4.7 billion) of the additional funds went to Sub-Saharan Africa (OECD and WTO, 2009). It is important to note that the OECD definition of aid for trade that is used here is a very broad measure of trade-related assistance and therefore overstates the overall magnitude of aid for trade. It includes all financing of infrastructure with the exception of water and sanitation projects. As infrastructure accounts for a large share of total ODA expenditures, this inflates the aggregate numbers for aid for trade. The reason for the use of a wide definition is that it is very difficult to distinguish to what extent specific forms of infrastructure support trade as opposed to non-tradable activities.9

Trends in aid for trade declined in absolute terms through 2002, after which it rose, reflecting renewed donor interest in growth and developments such as the launch of the Doha Development round (Figure 1). Even so, aid for trade has not kept pace with either total development assistance or that portion allocated to particular activities. Multilateral providers of assistance – aid that is channeled through IDA and the regional development banks – on average allocated a far higher proportion of their concessional aid for trade assistance to low-income countries than do bilateral donors. Some 93 percent of every aid for trade dollar goes to low-income countries (US$6.6 billion of a total of US$7.1 billion in assistance – Figure 2). However, bilateral donors provided 46 percent of their aid for trade to low-income countries. This highlights the importance of multilateral concessional lending for trade – and the urgency from an aid for trade perspective – of successfully completing the replenishment of the International Development Association’s concessional fund for low-income countries (IDA-16).10

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8 This “sectoral allocable aid” excludes funds for debt relief, administrative costs and budget support, as well as resources that are allocated to support trade finance. The G20 mobilized a collective US$250 billion effort to support trade finance during the crisis. Access to such finance is an important determinant of the costs of trade and the ability of exporters to operate.

9 It should also be noted that the OECD/WTO numbers exclude development assistance provided outside of the framework of the OECD Development Assistance Committee (DAC), and thus do not cover assistance provided by countries such as China.

10 Note: When references are made to CRS data, USD figures are in 2008 constant terms, whereas statistics attributed to OECD/WTO (2009) are in 2006 constant terms.
According to the OECD’s most recent comprehensive report on aid for trade, Asia is the largest recipient of aid for trade. Aid to Africa has been closing in year-by-year in second place. In 2007, Asia received US$10.7 billion, over half of which went to Central and South Asia. Although the volume of aid for trade funds destined for Asia remained stable from 2002 to 2007, the region’s share of total aid for trade funds dropped from 50 percent in the 2002-2005 period to 42 percent in 2007. This is due, in part, to Africa’s increasing share of global aid for trade funds. The region received US$9.5 billion in 2007, representing 38 percent of total aid for trade funds, up from 30 percent in the baseline period. Flows to all other regions were significantly smaller. Latin America received US$2 billion and Oceania received US$1.6 billion in this period. Europe received the least, at US$1.2 billion, and was the only region to register a decrease in aid for trade funds from the baseline period to 2007 (OECD/WTO, 2009).

The increased focus on the trade agenda by developing countries is also reflected in an expansion in trade-related activities and investments by the World Bank Group. A recent review of trade in World Bank country assistance strategies (CASs) found that trade—using the World Bank’s
more narrow definition that excludes most basic infrastructure – is now on the agenda of the majority of the Bank’s clients (65 percent of CASs). These CASs identify trade as an important priority and present assistance programs with a clear focus on one or more of the following thematic areas: regional integration, export diversification, trade facilitation, and market access. This is translating into increased operational support, through ESW, lending, and in some cases, technical assistance to help countries achieve their medium term objectives. World Bank trade-related lending more than doubled since 2002, rising to some $1.4 billion in 2008 from about $550 million in 2002 (Figure 3). Concessional lending to the public sector has increased by more than half (World Bank, 2009). However, the trend in terms of number of projects and countries with trade operations has been declining in recent years, illustrating that expanding aid for trade continues to require high-level attention by policymakers.

**Figure 3: Trends in World Bank Trade Lending, 2001–2009**

The rise in aid-for-trade has occurred against the backdrop of success in reducing import tariffs and removal of other traditional barriers to trade. This is true even considering the long stalled Doha negotiations at the WTO. As formal trade barriers have been eliminated for a significant portion of global trade, countries have focused on other impediments to trade flows – both through domestic and collective action. Global trade reform and capacity building is increasingly anchored in an agenda to minimize trade transaction costs to further leverage comparative and competitive advantages. This shift in the global trade agenda has been accompanied by a significant increase in aid for trade assistance from bilateral donors and multilateral institutions.

As discussed further below, achieving better targeted – and effective – aid for trade would benefit from a less ad hoc multilateral framework for coordination. It is clear, however, that there is a large supply of aid for trade assistance, the majority of which is provided by multilateral institutions and G20 donor countries. The G-20 is well placed to lead in this regard. In 2007, of the top fifteen non-institutional donors of aid for trade ODA, eight are G20 members, including the European Communities (EC). The G20 therefore has an opportunity to provide strong and visible global leadership, in partnership with multilateral institutions and developing countries, to

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shape the aid for trade agenda going forward. Commitments to sustain and grow aid for trade commitments at recent summits has been encouraging,12 but there is a need for a more direct and visible approach in ensuring concrete action plans on aid for trade to help drive the development agenda forward as global recovery continues.

**Does Supply of Aid for Trade Match Demand?**

The distribution of aid for trade is as important as overall amounts. There are a number of different perspectives on the question of whether the supply of aid for trade aligns with the demand and need for aid. One approach is to focus on analysis of poverty reduction strategy papers (PRSPs) to evaluate whether and how countries are integrating trade policy and institutional reforms into development plans. A United Nations Development Program (UNDP) study that reviewed 72 PRSPs found that 85 percent included one or more components devoted to trade (Kosack, 2008). This marks a significant increase from previous analyses – a 2000 study found only about 25 percent of completed PRSPs had a section relating to trade. Moreover, 52 of the 72 PRSPs included in the latest UNDP study related trade policies to poverty profiles. This development, among other more specific differences across various iterations of PRSPs, suggests that countries are increasingly considering linkages between trade and poverty reduction. These findings are similar to other studies, including informal surveys of World Bank Country Assistance Strategies (CASs).13

One of the first attempts to evaluate the balance between supply and demand based on empirical evidence and data was undertaken by Gamberoni and Newfarmer (2009). The authors find that, in general, demand for aid for trade has matched supply, with some exceptions: countries that are most in need of aid for trade – as measured by trade capacity and performance – tend to receive relatively more assistance. Subsequent analysis by World Bank staff that builds on and extends the methodology developed by Gamberoni and Newfarmer has focused on the relative impact of hard versus soft infrastructure investments, aiming to obtain a better understanding where aid for trade funds may be best spent in advancing capacity building goals.

Portugal-Pérez and Wilson (2010a) construct four indicators of trade capacity from a set of primary variables that measure the availability and quality of trade-related infrastructure and regulation (e.g., the fixed line network, quality and capacity of ports, airports, rail, and roads, governance and corruption, costs and time to clear trade consignments, various indicators of the business and investment climate, etc.). Using factor analysis, these variables are condensed into four specific factors that capture distinct features of the trade environment. Two of these indicators are related to the “hard dimension” of trade capacity – Information and Communications Technology (ICT) and Physical Infrastructure – and the other two are measures of the “soft” dimension of trade capacity: a Business Environment Trade Indicator and a Border Management and Customs Efficiency Indicator.

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13 See Strachan 2009.
Figure 4: Matching Demand with Supply of Aid for Trade

Aid for trade: impacts and effectiveness

There is an extensive literature analyzing the relationship between aid and economic growth. The analytical methods employed in these studies and the results are subject to significant debate. The literature provides a mixed picture as to whether there is a positive relationship between aid and growth. There may be many reasons for this. It may be due to the type of aid delivered (for example, purely humanitarian vs. policy change driven) or reflect differences in absorptive capacity in developing countries. One factor that can explain a lack of a positive relationship between aid and growth is aid-induced appreciation of real exchange rates—with aid inflows inducing Dutch disease. A comprehensive review of this literature is beyond the scope of this

See Rajan and Subramanian (2005) for a survey and new assessment; Cali and te Velde (2009) for a synthesis of the extant literature.


The effect is well known: aid flows may be used to finance expenditures of non-tradable goods and services, leading to a rise of their relative price with respect to tradable goods and thus, to a real appreciation of the exchange rate. This reduces the competitiveness of the exporting sector, as resources are transferred from the tradable to non-tradable sectors and drives up wages and other input costs. Estimates of whether aid induces a Dutch disease phenomenon can vary widely. Much depends on assumptions about the marginal productivity of additional aid and public expenditures, the complementarities between public and private capital, and the degree of flexibility of labor costs and other key resources. See e.g., Radelet, Clemens and Bhavnani (2006).
paper. It is useful, however, to outline, in brief, the complexities in analyzing and understanding the relationships between aid, trade, and growth. Debate continues, in particular, on the causality between aid and trade.  

Until the late 1990s a large share of ODA was tied to trade in the sense that procurement of goods and services financed by aid was tied to sourcing from donor country. Any positive trade-aid relationship, therefore, could be due to policy decisions made in donor countries. Many researchers have indeed found strong links between foreign aid and donor exports. Causality could also run the other direction—from trade to aid—insofar as donors allocate aid to those countries that they have the strongest trade ties with. Analyses that test for the direction of causality generally conclude that it depends on the pair of donor and recipient countries. Whatever the precise channels, the results do suggest a positive relationship between aid and trade.

In light of the commitments and action to increase AFT funding, questions as to how aid-for-trade specifically helps to improve the trading performance of developing countries – and how effective taxpayer funding is in attaining aid for trade objectives – have gained increased prominence. This is especially true in a post-crisis environment characterized by a much tighter fiscal situation in all donor countries. Bilateral donors and international development agencies are actively engaged in efforts to go beyond simple monitoring of the flows and allocations of aid for trade to an assessment and/or analysis of the impact of AFT.

Evaluation is critical to discovering ways to improve the effectiveness of development assistance – and aid for trade is no exception. Evaluation can occur at several levels: do the needy countries get it (the question asked above), are programs taken as a whole effective in expanding output and reducing poverty (programmatic evaluations), are projects achieving their stated goals, say in expanding electric power (project evaluation), and are outcomes different than in comparable situations without the project or different than they would have been in the absence of project interventions (impact evaluation).

Measuring the impact of AFT is challenging. In part this is because of data limitations. Many projects may not have information on defined baselines against which impacts can be assessed. Trade-related development projects often lag behind best practice in not being designed to allow rigorous ex post evaluation of impacts. A major challenge is that often standard impact evaluation methods cannot be applied to aid for trade because the assistance takes the form of general budget support. Frequently it will be difficult to disentangle the impact of AFT projects and programs on welfare, income, and equity (e.g., distributional effects).

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17 Suwa-Eisenmann and Verdier (2007) provide a comprehensive review of this topic.
18 For example, Nilsson (1997) observes for trade between the EU and recipient countries that $1 of aid generated $2.6 of exports from donor to recipient for the period 1975 to 1992. Wagner finds that increasing aid to a country by 1% increases the donor exports to the recipient by 1.33%. Other researchers have explored additional links that may exist between the donor and recipient that may lead to additional trade, such as political or economic considerations (Lloyd et al., 2000). Nelson and Silva (2008) is a recent analysis that obtains much smaller number using a fixed effects gravity model estimation.
19 Morrissey, 1993; Osei et al., 2004.
20 Lloyd et al. (2000) as well as Arvin et al. (2000).
Much of the assessment of AFT to date has been at an aggregated level, focusing on whether trade performance of countries and indicators of trade capacity have improved. What is needed is more detailed analysis of the impact of specific AFT interventions on the ground, which in turn will depend on identifying new ways to support long-term investment in micro-level trade cost and outcome data.

A recent OECD review of project evaluations for trade-related development assistance projects found that project documents often had insufficiently clear measurable objectives (OECD 2006). Quantitative baselines or benchmarks that would allow ex post assessments of the degree of improvement in specific measures of trade performance or trade capacity were frequently not included. This is an important finding in itself because it implies that donors and beneficiaries have to do a better job in identifying objectives. The OECD report concludes that, in half of the evaluations, trade-related assistance contributed to raising awareness of the importance of trade and knowledge of trade issues, while helping to strengthen country dialogues on trade policy. Major project weaknesses that were identified included inadequate needs assessments, weak project management and governance, a lack of integration into an overall trade strategy or development program, weak links to poverty reduction, inadequate donor coordination, and inadequate communication to, and expertise in, field missions.

A 2006 evaluation by the Independent Evaluation Group of World Bank trade projects and programs found that in general trade-related adjustment loans performed better than other adjustment loans (86 percent satisfactory versus 78 percent for non trade loans), while trade-related investment loans performed slightly worse (69 percent versus 72 percent satisfactory) (Independent Evaluation Group, 2006). A follow up review found that in 2007, more than 85 percent of projects were evaluated to have had moderately satisfactory, satisfactory or highly satisfactory outcomes. These generally performed better than non-aid for trade projects (World Bank, 2009).

More programmatic forms of evaluation use cross-country data on the effects of increasing aid for trade in specific areas. Given that aid for trade is targeted at specific types of activities and interventions a more precise identification strategy can be employed to assess the magnitude of effects and direction of causality.

In one of the first examinations of the link between aid and trade, Helble, Mann, and Wilson (2009) analyze the effects of various categories of aid for trade – trade development assistance (productive capacity building), trade policy assistance, and infrastructure assistance – by assessing their impact on bilateral trade flows through the use of a gravity equation. The findings suggest there are very high marginal returns to aid for trade targeted at trade policy and regulatory reform projects. Results in this paper, which is being extended in new analysis to examine the relationship between aid, trade performance, and private sector perceptions of priorities, estimate that $1 dollar of aid for trade targeted at trade policy and regulatory reform, could lead to about $700 in trade. While aid allocated in this area will encounter diminishing returns, this type of analysis suggests that the rate of return to aid for trade can be very high.

Cali and te Velde (2008, 2009) undertake a similar type of analysis and find that aid for trade facilitation reduces the cost of trading. A US$1 million increase in aid for trade facilitation is
associated with a 6% reduction in the cost of packing goods, loading them into a container and
transporting the consignment to the port of departure and loading them on a vessel or truck. They
also demonstrate that aid for trade allocated to infrastructure results in an expansion of exports,
especially in the mining and manufacturing sectors, with effects being the greatest in Africa
where infrastructure is weak. Aid for trade that is allocated to productive capacity (as opposed to
infrastructure or facilitation) has no statistically significant effect on exports.

As noted, impact evaluation is still an incipient endeavor in the aid for trade field – work of this
type is far more limited than in health and other fields of development assistance. A recent
example is Brenton and von Uexkull (2009), who undertook an impact evaluation for export
development projects targeted on specific export products. They found that such projects: (a)
have coincided with, or predated, stronger export performance in the targeted commodities; (b)
have had a greater impact on export growth for products with initially high export levels than on
those with low export levels (although this may be because technical assistance is directed
towards industries that are already set to take off); and (c) were likely to be more successful if
they addressed specific market failures or policy shortcomings in activities in which the country
had a long-run capacity for global competitiveness (as was the case in Rwanda’s donor-
supported strategy to move into the high quality, specialty end of the coffee market).

They conclude that, done well, export development programs can succeed: cut flowers had been
a growing export industry in Uganda for a decade when an export development program was
started in 2003. Following the program, export value almost tripled within one year. Although
other Ugandan exports also rose strongly at this time, cut flowers significantly increased their
export share. In the case of Mongolia, a traditional exporter of wool products, exports had
declined and lost share in the export portfolio in the late 1990s and early 2000s. After the
implementation of an Export Development program in 2003, exports of wool products entered a
steady growth path, outperforming overall export growth in 2005.

Taken together, the available literature tends to validate central Paris Principles: aid for trade
can be effective, provided that countries own the program and incorporate trade objectives
thoroughly into their development strategies. Nearly all bilateral and multilateral organizations
are working to improve effectiveness, but not all have recent, comprehensive evaluations of their
programs. With more than 40 bilateral and multilateral agencies involved in trade-related
technical assistance, the scope for learning from each other is great.

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21 Four important bilateral donors have undertaken evaluations relatively recently: USAID, DFID, SIDA, and the
Netherlands.

22 Donors involved in providing assistance for trade-related analysis or programs include the International Monetary
Fund, the International Trade Commission, the United Nations Conference on Trade and Development, the United
Nations Development Program, the World Bank, the World Trade Organization, the Bank for International
Settlements, the Food and Agriculture Organization, the International Standards Organization, the United Nations
Industrial Development Organization, the World Customs Organization, the World Intellectual Property
Organization, several regional groups, and many bilateral donors. See Suwa-Eisenmann and Verdier (2007).
Challenges and priorities looking ahead: maximizing the effectiveness of aid for trade

Ensuring timely and continued disbursements of existing aid for trade commitments to developing countries should be a priority to guarantee the uninterrupted implementation of ongoing AFT programs, thereby helping developing countries mitigate some of the effects of the economic crisis and benefit more fully from the ongoing recovery in trade. We argue, in what follows, that there are a number of areas where action by the G20 can enhance the effectiveness of aid for trade as an instrument to promote inclusive growth. A number of these lend them themselves to concrete initiatives by the G20.

1. Leveraging investments in infrastructure: the services “software” agenda

An increasing number of countries identify infrastructure as a regional priority, as revealed by the self-assessment questionnaires carried out for the OECD-WTO (2009) report. As noted above, infrastructure is the largest category of aid for trade: infrastructure projects account for about 54% of the global aid for trade portfolio. Recent research has found evidence on the potential gains to investment in hard infrastructure, including improved export performance (Francois and Manchin, 2008). There is also evidence of a significant potential for reduced trade transaction costs and increased consumer welfare from investment in infrastructure, such as new ports (Abe and Wilson 2009). Investment in infrastructure may also have a greater impact in countries with lower per capita income in terms of generating a higher marginal impact on export performance (Portugal-Perez and Wilson 2010a).

Investment in infrastructure per se may not be conducive to lower trade costs; however. It must be accompanied by measures that reduce trade costs (Hoekman and Nicita, 2010) and by appropriate regulation – for instance, policies that promote competition in transport services. Improvements in border efficiency and management can also greatly increase the rate of return on investments made to improve hard infrastructure such as roads.

The quality of public and private services can be an important determinant of the size of the payoffs to improvements in hard infrastructure. Services are critical for the competitiveness of firms and farmers because they represent an important share of the total costs of production. Being able to compete in international markets is increasingly determined by access to low-cost and high-quality producer services such as telecommunications, transport and distribution, and finance. Policies that raise operating costs or preclude innovation therefore can be very detrimental to the performance of the national economy.

Developing countries tend to have more and higher barriers to services trade and investment, as shown by the negative correlation between GDP per capita and the Services Trade Restrictiveness Index (STRI), a new measure of the services trade policy stance of countries compiled by Gootiiz and Mattoo (2009) (Figure 5). Removing such restrictions can generate substantial benefits, leading to lower cost and higher quality producer services for firms and farmers in these countries. Global outsourcing and integration into international value chains

23 Raballand and Teravaninthorn (2009) find that a lack of competition in trucking in West and Central Africa results in higher transport prices and lower quality of services compared to more contestable Africa markets.
increasing depend on having access to a variety of services. Recent research also suggests that reforms in services sectors have a positive effect on the productivity of both foreign -- and locally owned manufacturing firms (see Francois and Hoekman, 2009 for a recent survey of the literature).

**Figure 5: Services trade restrictiveness Index (STRI)**

![Graph showing services trade restrictiveness Index (STRI)](image)

A noteworthy feature of the pattern of services trade and investment policies is that landlocked countries apply more restrictive policies than coastal countries. This appears particularly true in the air transport and telecom sectors, in which landlocked countries have no inherent disadvantage (Borchert, Gootiiz, Grover, and Mattoo 2010). While there are many reasons why a country’s landlockedness might lead to a somewhat lower availability of services at a somewhat higher price, restrictive policies contribute to the poor performance in services sectors, beyond the handicap imposed by geography. This suggests that supporting policy reforms to enhance the contestability of “backbone” services in land-locked countries could be a priority area for aid for trade.

To date, it appears that much of the aid for trade effort has put the emphasis on hard infrastructure. Less has been done to improve the services-related policies and regulation that help determine the efficiency of (cost of using) infrastructure networks. This is one area where the support and leadership of the G-20 can make a difference. There are two dimensions to this: (i) ensuring financial aid for trade assistance includes an adequate focus on pro-competitive regulation and other policies that affect the functioning of producer services (Hoekman and Mattoo, 2007); and (ii) doing more to provide access to the knowledge and experience on these matters that exists in the middle-income, emerging market members of the G20.

1. **Expanding south-south integration through trade reform and market access**
Another area where the G-20 can provide important leadership is through expanded market access – especially for the least developed countries – led by reform in middle income countries to expand trading opportunities in a south-south context. This would provide an opportunity to low-income economies both to expand trade, and, as importantly, help them diversify across a larger number of markets.

South-South trade has been growing rapidly in recent years as a result of high rates of economic growth that were achieved by many developing countries. The BRIC countries, for example, have an import share of 12 percent (2008) compared to just 6 percent in 1996. Meanwhile, high-income countries’ share of import demand decreased from 81 percent in 1992 to 72 percent in 2008 (Haddad and Hoekman 2010).

Significant trade barriers remain in many of the dynamic emerging markets. The emphasis in policy fora such as the WTO has been on developed country market access conditions, including achieving duty-free, quota-free access for the LDCs and addressing key constraints that reduce the value of preferential access such as rules of origin. While this is important, it arguably represents a missed opportunity for low-income developing countries that confront high barriers against exports in middle-income countries.

Fugazza and Vanzetti (2008) compare the potential effects of the removal of barriers on South-South trade with the gains from developed country liberalization and from regional free trade areas within Africa, Asia and Latin America using a general equilibrium model, GTAP. Their simulations indicate that the opening up of northern markets would provide annual welfare gains to developing countries of $22 billion. However, the removal of South-South barriers has the potential to generate gains 60 per cent larger. The results imply that giving greater emphasis to removing barriers between developing countries could give a significant boost to trade with low-income countries.

Overall, research suggests that whereas traditionally the bulk of South–North trade flows were in less sophisticated sectors with fewer learning opportunities; this may not be the case today, particularly among the dynamic Asian economies. Klinger (2009) studies the composition of South–South as opposed to South–North trade in recent years to consider whether the South as a market provides developing countries with greater opportunities to transform their productive structures and move to more sophisticated export sectors than the Northern market does. His results show that for many developing countries, including in Africa and Central Asia, exports within the South are more sophisticated and better connected in the product space than exports to the North, whereas the opposite is true for the faster-growing economies of Asia and Eastern Europe (excluding the Commonwealth of Independent States). Klinger also finds that the primary source of cross-country variation in export sophistication and connectedness is between northbound rather than southbound export baskets.

Post-crisis projections are that middle-income markets will grow more rapidly than those of high-income countries. The emergence of multiple growth poles in the South offers low-income countries an opportunity to diversify both across markets and products given that developing country consumers have differentiated preferences and demand. Moreover, increased South-South trade reduces the exposure of developing countries to possible prolonged slow growth markets in Europe, Japan, and the United States. It also mitigates risk associated with increased
market openness and trade-led growth through product and good diversification effects, as mentioned above.

South-South trade has already increased at the extensive and the intensive margins. Exports of LMICs to BRICs rose from 7 percent of the total in 2000 to 12 percent in 2008 (Figure 6). The average value of a transaction from LMICs to BRICs increased 444 percent during the 1996-2008 period, while that from LMICs to HICs rose only 180 percent. However, developing countries still export substantially fewer varieties than high-income or even middle-income countries – there is therefore great scope for further diversification (Figure 7).

Figure 6: Developing Countries Account for an Increasing Share of World Trade (percent share of world trade)

Figure 7: Southern Countries Still Export Fewer Varieties Than Northern Ones (average number of exported varieties at 6-digit HS)

Source: Haddad and Hoekman (2010), drawing on UN-COMTRADE data.
Note: LICs=low-income countries; LMICs=lower middle-income countries; UMICs=upper middle-income countries; and HICs=high-income countries.

Middle-income emerging markets also are a source of knowledge and FDI – which in turn can drive additional trade growth in low-income economies. Harnessing these opportunities is in part a function of putting in place the appropriate policies – including removal of market access barriers. If all OECD countries were to offer 100 percent DFQF, exports of the LDCs could increase by up to $2 billion more than they would under a 97 percent scenario (Bouët et al., 2010). But these export gains would be greater still if major middle-income nations were to offer DFQF access to LDCs—by up to $5 billion – reflecting higher tariffs in these countries.

2. Supporting regional cooperation and integration of markets: capacity building

Although much of the AFT agenda has been national in scope, there has been a recent rise in the demand for assistance to support regional integration. One factor driving this is the recognition that key constraints to a country’s competitiveness may lie outside its borders. This is most directly the case for land-locked countries. There are a number of common priorities for regional integration in areas such as transport infrastructure, road corridors, energy and water, and trade facilitation. Efforts to integrate neighboring markets for goods, services and factors of production (workers, investment) can help stimulate South-South trade by reducing trade costs and allowing economies of scale to be realized. Much of the agenda here revolves around initiatives to lower transactions and operating costs for firms on both side of the border. Lowering such costs in a cooperative (joint) manner does not give rise to the types of welfare-
reducing trade diversion that can arise from preferential reduction of tariffs: lower trade costs benefit all trade partners.

There is evidence of the benefits of strengthened regional cooperation. The Asia Pacific Economic Cooperation (APEC) agenda on trade provides one example. Increased transparency can have a positive impact on trade and welfare. Based on a computable general equilibrium model, Abe and Wilson (2008) find that trade in APEC countries would increase by 11 percent and global welfare would expand by $406 billion by reform aiming at raising transparency to the average level in the region.

The simulations suggest that most of the increase in welfare would take place in member economies undertaking reform. Among the reformers, the GDP of Vietnam, Thailand, Russia, and the Philippines would increase approximately 20 percent. There is also evidence to suggest that reform in some of the poorest regions of the world could generate substantial benefits. Improvements in trade facilitation indicators in Africa, for example, to cut trade costs half-way to the best performer in the region for Ethiopia is roughly equivalent to a 7.6% average cut in tariffs faced by Ethiopian exporters in export markets (Portugal-Perez and Wilson, 2009).

Cooperation at the regional level poses specific challenges in that the costs and benefits of projects can be very asymmetrical, with most of the required investments (and thus costs) accruing to a country that gets relatively little benefit from the investment. As this can greatly reduce support for regional projects that are critical to landlocked developing countries, one rationale for aid for trade is to increase the incentives for joint action in areas where benefits are distributed asymmetrically across countries.

For example, landlocked developing countries in Africa, in which more than a quarter of the continent’s population lives, face a substantial competitive disadvantage due to high trade costs (Djankov et al, 2006; Raballand and Teravaninthorn, 2009; Arvis and Raballand, 2010; Arvis et al. 2010). These countries also tend to have lower levels of foreign direct investment.

Portugal-Perez and Wilson (2010b) explore the relationship of trade costs and incoming FDI into developing countries, including landlocked ones. Preliminary estimates show a negative relationship between trade costs and FDI in a North-South context. Indeed, most incoming FDI in developing countries finance operations entails the transport of goods across borders, as in extracting industries, or in industries exporting goods intensive in low-skilled labor. In that context, they argue that domestic trade costs can be seen as a tax on operations and have an impact on FDI attractiveness.

Landlocked developing countries (LLDCs) are particularly damaged as they tend to have higher export costs than their coastal neighbors. For these states, domestic problems are multiplied by those prevailing in transit/coastal countries through negative spillover effects. But there are also externalities for coastal countries: a nationally focused strategy often will not be sufficient to maximize trade and growth opportunities if neighboring markets are ignored. Policy reforms and actions that can lead to significant improvement of the business environment and attract investment are of a public good nature: the associated outputs are non-excludable (it is difficult to prevent countries who may not have contributed to its provision from using it) and non-rival in consumption (use by a neighboring country does not affect the supply or quality of the good); hence the need for a collective action solution at a regional level.
The need for regional cooperation is understood by all stakeholders. However, the range of available instruments to support regional projects and cooperation is limited. This results in the under-provision of financing/assistance for multi-country trade-related projects (Hoekman and Njinkeu, 2010). Weak capacity of existing regional secretariats and pro-reform civil society groups, and the diffuse nature of the benefits of existing integration mechanisms for the private sector have also resulted in a poor implementation track record. Moving the regional integration agenda ahead requires addressing frontally the political economy of regional cooperation and coordination by increasing the incentives for implementation. This requires engagement on different fronts, with a reward/incentive scheme that targets all relevant actors – national governments, sub-national entities, and non-state actors.

Dedicated funds to support regional cooperation, covering both software (regulatory institutions, policy changes) and hardware (infrastructure to support cross-country flows of goods, services and people) could help to fill the gap that currently exists. A concerted focus on identifying and financing regional projects that would help to address the national priorities could also help overcome resistance to beneficial regional market integration (beneficial in the sense of helping to attain the competitiveness objective). A practical way forward would be for a greater proportion of donor funds for aid for trade to be allocated to regional development banks, as well as to multilateral agencies for regional projects.24 Most regional and multilateral institutions already have trust funds through which such resources could be channeled.

The G-20 can make a direct contribution in support of regional integration with high level support for regional integration including an emphasis on knowledge exchange and capacity building led by the middle income developing countries. From APEC to ASEAN to regional institutions in Africa, a new emphasis by the G-20 on knowledge transfer to support the integration of neighboring markets through joint projects would represent an innovative step toward cooperation.

3. Harnessing the private sector as a source of knowledge, capital and information

Given the broad nature of the aid for trade agenda – encompassing areas from border management to regulatory reform and infrastructure investment – there is a sizeable number of stakeholders involved from both the public and private sectors. As such, there is great scope to make effective use of public-private partnerships that capitalize on private sector expertise in prioritizing areas for reform and identifying potential solutions. The United Nations Centre for Trade Facilitation and Electronic Business (UN/CEFACT) put forth a recommendation specifically addressing the purpose, methods of creation and operating structures of such PPP’s in an October 2001 Recommendation.25

Such models have proliferated at the national level, an example being national trade facilitation associations that work to connect stakeholders in the public and private spheres in order to carry

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24 While proposals for earmarked funds are controversial, as earmarking can be inconsistent with aid effectiveness (the activities for which funding is earmarked may not be a priority in individual countries), the creation of a mechanism that earmarks an overall amount for trade does not need to imply that countries must identify trade as a priority; it simply provides greater credibility to countries that if they decide that trade projects are a priority, development assistance will be available.

out work at a broad national level, or in specialized areas such as border management reform (e.g., TradeNet of Singapore and Tradelink of Hong Kong, China). These networks serve as important platforms for developing national strategies and action plans for reform, in addition to providing stakeholders with a mechanism for coordination and harmonization of policy measures across industries and sectors. Much more can and should be done to harness the knowledge and information that exists in the private sector, both as a source of data on constraints to trade and policies or factors that needlessly increase costs of trading, and as a source of potential solutions to specific problems.

The World Bank is developing a new Public-Private Partnership on Aid for Trade Facilitation as a platform for an exchange of information and learning in the area of trade facilitation. The project will design and implement practical and achievable trade facilitation projects that lower trade costs by addressing the lack of capacity of developing countries to rapidly move goods and services across borders. A central focus of the work will be to improve the “software” of trade logistics and border management to complement and enhance hard infrastructure investments. In addition, the partnership will leverage private sector expertise in producing real-time trade performance data, which may be used to encourage policy-oriented trade facilitation reform. A broader effort along such lines that could be considered by the G-20 is outlined in the concluding section of this paper.

4. Bolstering monitoring and evaluation of the effectiveness of aid for trade

Action is needed to design and implement new mechanisms to strengthen accountability of stakeholders in the provision of aid for trade. Effective monitoring of delivery of aid for trade and the extent to which it responds to national priorities as defined by recipient governments is critical. Effective monitoring is also important to allow accurate assessments and evaluation of outcomes. Most donors monitor and evaluate their aid for trade programs in accordance with generic evaluation guidelines or with specific guidelines for themes and sectors falling under aid for trade (see OECD/WTO Donor Questionnaire). Much greater efforts are needed to expand monitoring frameworks to support aid effectiveness, including direct engagement of the private sector and civil society in evaluating and ensuring aid for trade flows are directed toward sound and sustainable projects.

More learning could be generated by applying, whenever possible, the kind of impact-evaluation methods now widely used in the evaluation of poverty, health and education projects. The essence of these methods consists of using control groups to benchmark the improvement in the performance of individuals “treated” by particular programs. Clearly, not all trade-related programs can be amenable to such “treatment-effect” methodologies. The easiest are export-promotion programs that target individual firms, such as medical treatments target individual patients (see Volpe and Carballo 2008 for an evaluation of Peru’s export-promotion program).

Even in the limited areas where their application is relatively straightforward, the few applications of “clinical” impact evaluation methods to trade-related programs have so far been

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27 The World Bank is exploring a new initiative to gather data and support analysis on aid for trade effectiveness and monitoring. A number of bilateral development agencies are also starting to invest in this agenda.
limited in scope: They provide no evaluation of spillover effects—even though spillovers are key to the justification of public intervention—and have, like all clinical impact evaluations, uncertain “external validity”, as what works in one setting may not work in another. Notwithstanding these and other caveats that have been extensively discussed in the literature (see for instance Rodrik 2008), they offer a valuable tool to understand what works and what does not. In particular, when carefully thought out, they can help identify which components of assistance programs work best. That is, beyond their contribution to general accountability, they have the power to generate useful knowledge to renew the factual basis on which to base policy advice and donor practice.

A new strategic investment in data and analysis should include work at both the macro and micro levels (Wilson 2010). An agenda in this area would center on a framework for rigorous evaluation of aid-for trade-projects, empirical research on aid impact evaluation, drawing on macro datasets from the CRS OECD databases and micro-data from project datasets at the World Bank and other development institutions. At the macro-level, country and/or regional analyses of aid for trade effectiveness that monitor how sub-types of aid for trade funds, per the OECD CRS classification scheme, are spent in relation to their returns, as measured by increased trade flows. At the micro level, new data on trade costs could be collected from a variety of sources, e.g. surveys from export promotion agencies, customs data, and international career companies. Detailed data can be used to assess policies related to specific aid for trade interventions —e.g. support for industrial upgrading, or certification of firms (ISO 9000), technical assistance for transport logistics, product certification, etc. New assessments should include cross-country evidence and in depth case studies to assess the impact of these interventions.

Moving the Agenda Forward

The G-20 is uniquely positioned to support specific actions to expand global trade. The fragile economic recovery – combined with the need to strengthen the international trading system in support of sustainable and inclusive growth and employment – place the aid for trade initiative at the forefront of policy importance. In addition to living up to the commitments to deliver on the promises that were made in Gleneagles and Hong Kong on expanding aid for trade flows, there are four strategic themes that a G-20 “Action Agenda on Aid for Trade and Development” could support:

1. Establish a G20 platform for capacity-building and transfer of knowledge on policies and regulatory options to improve the efficiency of producer services and the operation of network infrastructure. A coordinated program of assistance and knowledge exchange led by middle income G20 countries could do much to increase the rate of return on aid for trade investments in hard infrastructure by creating a mechanism that will focus on strengthening capacity in low-income countries to put in place the associated complementary “software” inputs – policies, pro-competitive regulation, etc. – that are critical to realize social (equity) objectives as well as improve the efficiency of use of network infrastructure.

2. Complementing the financial aid for trade provided by high-income G20 members with market access reform by middle income G20 members to lower barriers to exports from
poor countries so as to expand south-south trade. Extending duty-free, quota-free access for LDCs to all G20 members, with minimal exceptions, would constitute a concrete initiative that would directly promote the trade and development prospects of the poorest countries in the world, at very low “cost” to the G20 in terms of additional imports.

3. Creation of a new “aid for trade public-private partnership” to leverage the dynamism in the private sector for strengthening trade capacity in the countries that most need it. Given the high payoffs from improving trade facilitation – encompassing areas from border management to regulatory reform and adoption of modern ICT technologies – such a partnership could involve an initiative to capitalize on private sector expertise in prioritizing areas for reform and identifying potential solutions, while leveraging the coordinating capacities of governments and/or multilateral donor institutions. The World Bank is developing a new public-private partnership on aid for trade facilitation that could serve as a model in this regard.

4. A G20 “strategic action plan” to provide dedicated financial support for a concerted program of monitoring and evaluation of aid for trade anchored in systematic data collection and research. All donors and recipients recognize the importance of monitoring and evaluation and analysis of trade outcomes and performance. There is, however, no dedicated funding to ensure consistent collection of data on trade flows, trade policies, and outcomes and the software platforms and databases to make such data generally available. A joint assessment by the ITC, UNCTAD and the World Bank concludes that an amount of $10 million per year would permit the collection of the data needed to monitor trade performance and trade barriers and cover the costs of maintaining an open access data platform and analytical tools. An additional $10 million a year for rigorous evaluations to be undertaken by independent academics and research institutes would begin to make up for the huge lacunae in our collective knowledge regarding the impacts of aid for trade. These amounts add up to less than 0.1 percent of global aid for trade.
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