Trade, Growth and Poverty in Africa

Outline

1. The Problem - Poverty and dimensions in Africa
2. Linkages between Trade, economic growth and poverty reduction
3. Evidences
4. Agricultural exports and Poverty reduction
5. Trade Policies and Poverty reduction
Poverty and Its dimensions

- The main challenge—Poverty
- 10 countries have GNP/capita of less than US$ 400
- Most of the people still living on less than US$1 a day are in Sub-Saharan Africa and South Asia (Sala-i-Martin, 2002; Collier and Dollar, 2002)
- Multifaceted—income poverty—Per capita income ranges from USD 230-260 for Somalia and , USD 2 100-3 300 for Egypt, Namibia and Morocco.
- HDI are lower than would be expected
  - Half of the population in Africa lacks access to health services, compared to a little more than 20% in South Asia
  - The average adult illiteracy rate at 42% is more than three times higher than the rate in East Asia and the Pacific
  - Life expectancy after rising over the last decades is plummeting due to the scourge of HIV/AIDS—Africa with less than 10% of world population has about 63% of global HIV/AIDS cases (ECA, 1999)
Poverty dimensions

• The total population of the region is about 888 million (2005 est.)-second largest after Asia
• Projected to grow at an average of 1.7% per annum between 2005-2015-one of the highest growth. World total growth is projected at 1.2% for the same period.
• Poverty in Africa is predominantly rural. More than 70% of the continent’s poor people live in rural areas and depend on agriculture for food and livelihood
• Sub-Saharan Africa-more than 218 million people live in extreme poverty.
Poverty-spatial dimensions

- Western and Middle Africa-rural poor 75%; estimated population-90m.
- Eastern and Southern Africa -rural poor 82% estimated population-130m.
- Ten of the 21 countries in this region have an average annual per capita income less than US$400.
- Northern Africa: % of rural poor vary from 6% in Tunisia to 90% in Somalia and 87% in the Sudan. (IFAD)
Overall, poverty is disproportionately rural

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## Trade, growth and poverty reduction in Africa

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Growth trends

- Africa experienced moderate growth from the mid-1960s until the end of the 1970s
  - In particular SSA experienced accelerated growth supported mainly by a boom in commodity prices and foreign aid
- Economic performance deteriorated rapidly in the 1970s and early 1980s
  - Adverse external developments, structural and institutional bottlenecks and policy errors
Growth trends

• Broad-based economic upturn started in the mid-1990s and has continued into 2000-2003
  • Improvement in performance linked to better macroeconomic and structural policies-low inflation, prudent monetary and fiscal policies, exchange rate management etc. (IMF, 2000)
  • Governance improved considerably in many countries
  • Increased export performance resulting from trade liberalisation and trade policies.
Growth and Poverty reduction

• Overwhelming evidence that high economic growth is a pre-requisite for reducing poverty and inequality

  Employment-led growth raises household income — which can reduce poverty and lead to increased human capabilities

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Reducing Poverty through growth

• The ECA and the Commission for Africa are quite clear on the fact that addressing Africa’s poverty requires more rapid growth.

• According to the Commission on Africa report, the mechanism for increased growth are:
  • More trade and aid
  • An improvement in the investment climate
  • A doubling of expenditure on infrastructure
  • An emphasis on agriculture and on helping small enterprises

• The ECA emphahsises the promotion of trade and regional integration as a core element in fighting poverty.
Macroeconomic Fundamentals of PRSPs in Africa

- Economic growth: accelerated, rapid, strong, sustainable, equity-based, broad-based.
- Macro-economic stability
- Prudent monetary/fiscal/budgetary policies
- Structural reforms: liberalisation and privatisation, civil sector reform
- Development of the private sector (or creating an enabling environment)
- For Africa to cut poverty by half in 2015, a GDP growth of 7% is required (ECA)
Trade and Growth

• In addition to other concomitant factors, trade can be an important source of economic growth
  • International trade can expand markets, facilitate competition and disseminate knowledge, creating opportunities for growth, poverty reduction and human development
  • Trade can also raise productivity and increase exposure to new technologies, which often spurs growth

• Trade liberalisation promotes higher economic growth in the longer term (Sachs-Warner 1995, Dollar and Kray, 2000)
Trade and Growth

• Trade and macroeconomic policies are highly linked
  – Macroeconomic variables such as national income, employment, price level, aggregate investment and consumption (savings) are affected by trade
    • Effect of trade on employment and the price level are indirect. Changes in employment are derived from changes in demand for labour while changes in the price level also depend on the relative changes of domestic aggregate demand and supply.
    • Trade also affects macroeconomic performance in terms of the dynamics of the economy’s growth, stability and distribution.
Trade and Growth

• Imports:
  • may be used as inputs in production-affects the level of output and indirectly employment
  • Imports of consumer goods reflects choices of consumers and hence decisions to spend or save
  • Imports compete with domestic production and hence employment adversely if domestic industries cannot compete

• Exports:
  • Main component of aggregate demand stimulates growth of domestic output and hence income and employment
  • By expanding markets for domestic firms, exports create conditions for production costs to fall as firms gain from economies of scale-productivity increases
  • Hence many countries have relied on exports as an “engine” of growth

• The reverse causality from macroeconomic variables to trade is also true.
  • Domestic growth will stimulate demand for imports
  • Changes in domestic price level will affect competitiveness
  • Trade is sensitive to macroeconomic policies
Is trade important for macroeconomic performance?

- **Empirical evidence:**
  - Most studies testify to the importance of trade for economic growth;
    - Dollar and Kray, 2001; Burnside and Dollar, 1977; Arteta, Eichengreen and Wyplosz, 2001; show that the degree of trade openness is significant in explaining differences in economic growth of countries
    - Most models included trade elements as part of macroeconomic variables that co-determine the explanation of growth performance and were statistically significant
    - Macroeconomic conditions together with open trade policies are found by most economists as critical for explaining faster economic growth
  - Rodriguez and Rodnik (1999) disagree on causality. Flow of causation is not from trade and trade policy to macroeconomic performance but the reverse.
  - Trade liberalisation may also impact on fiscal revenues in countries which are heavily dependent on tariffs as a source of government revenue (Ebrill et al., 1999).
    - In developing countries, budgetary revenues are still heavily dependent on taxes imposed on international trade.
    - This could be problematic for countries with a small domestic tax base, low efficiency of tax collection or poor design of the tax regime.
Are there other direct impacts of trade on Poverty reduction

• So far, we have established that trade by impacting on economic growth could help to reduce poverty directly or indirectly

• But are there other direct impacts of trade on poverty reduction?
Regional Integration (RIAs) and Poverty Reduction

• RIA enables neighbouring African countries to link their small economies to create relatively larger markets, thus allowing for benefits from economies of scale-larger markets;
• The trade creation and diversion effects resulting from the preferential reduction in tariffs
• Member countries of a RIA can present themselves as a united and credible group in international trade negotiations
RIAS and Poverty Reduction

- Enhances the potential for sub-regional specialization and cooperation in a variety of economic and social spheres;
- The deepening of integration within a sub-region may minimize the potential for hostilities between neighbouring countries-toning down political rivalry.
- National-level reforms and other economic policies gain more credibility if closely coordinated and harmonized within regions
RIAs and Poverty reduction—Evidence (Tanzania study: Mboya and Kwalie, 2004)

- **Nexus—Regional integration—FDI inflows**
  - FDI inflows and poverty reduction—
    - evidence weak
    - Sectors with high employment impact of FDI e.g. agriculture received low FDI inflows

- **Trade effects of RIA substantial**
  - Upsurge in exports (especially agric exports) to SADC and EAC from 6% in 1995 to 14% in 2002.
  - Increased diversification of exports

- Most domestic firms now sell in the regional markets—80% of firms surveyed agreed that RI has created an opportunity for trade and investment
Trade Developments in Africa

- International trade prominent in economic activity in Africa
  - Merchandise trade in SSA as a share of GDP increased from 38 to 48% between 1988-89 and 1999-2003.
  - Higher commodity prices, combined with increased export volumes resulted in a marked increase in the region’s export value in 2003.
  - The growth in export earnings sustained the growth of imports which rose by more than 20% in 2003. However, merchandise exports exceeded imports for the fourth consecutive year.
## Share of Africa in World Trade

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## Export Shares

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Composition of Africa’s exports

- Merchandise exports expanded by 23% in 2003
- Mining rose by 24%, manufactures by 22% and agriculture by 16%
- Although the performance of manufactures and agriculture were below mining, the rates exceeded the respective growth rates of world exports.
- Despite the rapid rate of growth of manufactures, export dependency on primary commodities remain striking
- Commercial services was also outstanding in 2003 underlined mainly by expansion of travel receipts
# Composition of Exports - % share of total exports

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Manufacturing and poverty reduction

• High export growth in manufacturing could make it a good sector to support poverty reducing strategies.

• But, only a handful of African countries will be able to achieve this because
  • Slow pace of diversification
  • Competitiveness hampered by
    – Low productivity and inappropriate exchange rates in the move towards the exports of processed goods and manufactures
Mineral exports and Poverty reduction

- Mining has some potential positive poverty impacts:
  - Fiscal impact on foreign exchange
  - Income generation
  - Local economic development
  - Improved land-use planning
  - Source of energy

- However, it also harbours potential negative poverty impacts:
  - Governance, corruption and macroeconomic issues.
  - Environment
  - Health and human development
  - Socio-cultural impact
Mineral exports and Poverty Reduction Potentials

• By far the greatest complain against mining is its inability to generate employment
• Though a net foreign exchange earner, the labour force is often highly skilled and specialised
• The poor do not participate in the economic opportunities of mining but bear the costs and the risks when a mine is situated in the community.
• Solution: Encourage artisanal and small-scale mining
  • Has the potential to employ men and women
  • Has the potential to generate resources for training and education
  • Enhancing local government capabilities.
Tourism and poverty reduction

• Tourism is an important component of commercial services export: most relevant to poverty reduction in Africa is tourism
• Tourism accounts for about one-third of the global trade in services
• Industrialised countries have the largest shares in the market.
• However, the increasing importance of South Asia and the Pacific as tourist destinations is remarkable. Africa with its vast potentials still lag behind in this area.
• Tourism is labour-intensive. According to the World Travel and Tourism Council, it is the most important employer in the world-200m employees
Tourism and Poverty Reduction

- Tourism is envisaged to contribute significantly in achieving the MDG especially poverty alleviation through
  1. Creation of Jobs particularly for the local and poor population
  2. Purchase of goods and services locally
  3. Establishment of SMEs as well as community-run enterprises
  4. Investment in local infrastructure
  5. Access of locals to information and participation in decision making
Tourism and Poverty reduction

- Tourist destinations show that weaker, socially disadvantaged groups are mostly at the losing end as tourism flourishes.
- Tourism could also lead to a loss of jobs especially in the fishing sector and agriculture.
- According to ILO estimates close to 10-15% of the employees in tourism are children and youth under the age of 18.
- Women account for close to 60-70% of the employed but receive 30% less in wages than male counterparts.
Agriculture and Poverty reduction

- Most African countries do not have good prospects in mining and tourism
- Mining and tourism may have weak linkages and high leakages
- Poverty is directly linked to agricultural productivity (Irz, Xavierer et al; 2001).
Agriculture and Poverty

• If physical productivity increases, poverty will diminish because:
  – Agriculture is central to the livelihoods of the rural poor.
    • Even with rapid urbanisation, more than 50% of the poor will be in rural areas by 2005, and depend significantly on agriculture.
  – Agriculture provides two thirds of employment, half of exports, and more than one third of Gross national Income
  – For each point in growth of agricultural yield, the number of those living on less than 1$ per day reduces by between 0.6 and 1.2 %.
  – 63% of the population live in rural areas.
  – 73% of the poor live in rural areas, and most depend on agriculture
  – Agriculture and agro-processing account for 30-40% of GDP in developing countries
  – General economic development requires prior growth and productivity gains in agriculture.
Agriculture and Poverty

• Evidence: large body of literature on the impact of agricultural productivity growth:
  – Irz et al, 2003
  – Hazell and Haddad, 2001
  – Dorosh and Haggblade, 2003-”investment in agriculture generate the highest impacts on the poor”
Food security and poverty reduction

- Hunger is a result of poverty, whatever reduces poverty will reduce hunger
- Food availability depends on
  - First and foremost, agricultural productivity
  - National and international markets and distribution systems
  - International and national trade policies; ensures that food is available to all at reasonable prices
- Production of export and non-food crops can enhance food production
  - Studies have shown a positive correlation between production of non-food and food products in many less developed countries where agric/GDP ratio is > 20%
  - Studies have also confirmed a positive correlation between food production growth and aggregate export growth in these countries.
But agricultural productivity in Africa faces severe problems.

- Secular decline in terms of trade since the early 1980s due to declines in export prices and wide fluctuation in real export prices of primary commodities—coffee, cocoa, cotton, copper etc.
  - Resulted in marginalisation of the region in world trade—Africa’s share of world agric exports declined substantially
  - Resource losses due to terms of trade declines have been a major factor in the poor economic performance in the region
Also declining manufacturing terms of trade

- Recent empirical research (Maizels et al, 1998; Maizels, 1998) has also shown that the expansion of manufacturing exports from developing countries has been associated with downward trend in their terms of trade.
  - Trend more pronounced with respect to exports of labour-intensive manufactures than skills and technology-intensive products
  - Study (34,35) revealed that while net barter terms of trade of developing countries as a whole declined at an average rate of 2.2% per annum from 1979-1994, the decline was largest for LDCs and ACP countries-5.7 and 4.7% respectively
  - For LDCs deterioration in manufacturing terms of trade was more pronounced that the decline in primary commodity terms of trade.

- This is not good news for Africa which is trying to quit dependence on primary commodities by moving into exports of manufactures.
- This “fallacy of composition” i.e. rising export volumes (due to increased supply resulting from improved technology) accompanied by falling export prices threatens most LDCs particularly SSA given its level of development
What role for Trade Reforms?

• Sustained trade reforms doubled growth in the agricultural sector (Michaely, Choksi, Papageorgiou)

• Agricultural trade liberalisation gives much higher aggregate growth rate- 5.75 vs. 1.1% (Valdes).
  • Trade liberalisation- easing tariffs and other import restrictions, reducing or eliminating domestic supports and export subsidies-tends to boost economic growth in the longer term.

• SSA countries with large improvement in macro/trade policies had higher growth rate-3.5% vs. 0.3% for those with deterioration (World Bank)
Trade reforms and poverty reduction

- Huge evidence exists to show that global trade reforms under the WTO can have big poverty reduction effects
  - Developed countries by removing subsidies and improving market access can make it more feasible for Africa to gain from reforms
  - African countries can also undertake reforms that would otherwise expose their economies to unfair competition
  - Welfare results are driven by improvements in the terms of trade (export prices rising more than import prices) and the efficiency effects of the improvements in the allocation of resources between different activities.
- Trade liberalisation can enhance food security by
  - increasing rural growth and reducing rural poverty
  - Keeping food prices affordable
  - Improving access to imported agricultural technology, mostly embedded in inputs
  - Providing cash to buy inputs. (Nash, 2005)
Market access

• Developed countries must make it easier for developing countries to export to their markets by improving market access through reducing tariffs and non-tariff barriers, and providing duty-free and quota free access for all products exported from LDCs
  • Specifically, developed countries must end agricultural export subsidies by 2010 and substantially reduce tariffs against developing country agricultural exports
• African countries must develop their own trade reforms in line with clear development plans