KEY FINDINGS

The key findings of this Report presented in the following paragraphs are based on the foregoing background; an analysis of extensive review of issues; and ten country case studies. The case studies were directed at gauging the trade policy-making process especially in relation to industrialization.

Both theory and existing empirical evidence suggests that trade, under certain conditions, can be a veritable tool to promote industrial development and structural transformation in Africa. Trade policy, on one hand, through promotion of competition, innovation and efficient utilization of resources can enhance the dynamic efficiency of matured firms and thus foster industrialization. On the other hand, trade policy which exposes infant industries to competition can lead to de-industrialization. A critical factor for trade policy to promote industrialization is the appropriate balancing between promotion of relatively matured sectors and simultaneous protection and support of fragile sectors. No doubt, this is not an easy task but a feasible one that has been successfully performed by most industrialized countries.

A pre-condition for trade policy to foster industrialization is that it must be highly selective. This condition is necessary at least from two perspectives: First, trade-induced industrialization involves huge resource costs, and second, it requires an effective implementation, monitoring and evaluation. While recognizing the role and place of horizontal industrial policies, the vertical (i.e., selective) policies are important in the process of developing dynamic comparative advantage. The hallmarks of an effective selective trade/industrial policy are: it is based on rigorous studies that inform identification of the sectors, it has monitoring and evaluation mechanism in place; and it is insulated from political hijack. However, most countries are not fully engaged in effective selective trade policies for promoting industrialization based on the various policies instituted and implemented.

Trade-induced industrialization is not automatic; it requires concerted efforts at least at two levels. First, integrated and coherent trade and industrial policies, diligently crafted and implemented, carefully and regularly monitored and evaluated is a pre-requisite. Such policies must be tailored towards the overall goals and objectives of a country's national development strategy and plan while recognizing and incorporating challenges and opportunities offered by the external environment. Second, various stakeholders must be on board. An effective method is consultations with various stakeholder groups to ensure that most their concerns are addressed. The evidence from the country case studies suggests the need to step-up coherence between trade policy and the national development strategy and between trade policy and other policies especially industrial policy.

Regional and global trade and production networks open new potential opportunities for Africa's industrialization. Instead of industrializing bottom up, segmented value chains offer the scope to engage in international trade at a specific stage of the production process, thereby harnessing more efficiently one's comparative advantage. In this context, the services sector has come to play a fundamental role in the value addition that takes place at each step along the supply chain, whilst foreign direct investments have emerged as a driver of international trade expansion. For trade policy to effectively foster Africa's industrialization, it must respond effectively to developments in the global production architecture, especially production of intermediate goods rather than just the finished goods, and participation in one or two activities along a value chain instead of all the activities in the chain. Thus, trade policy that promotes trade in intermediates, trade in tasks and trade in services (as services are important components of internationalization of production process), is an essential pre-requisite of modern day industrial development.

Consistent with global trends, intermediate products accounted for the bulk of Africa's merchandise trade, accounting for about 60 per cent of Africa's total merchandise imports and over 80 per cent of its exports. In addition, intermediates represent the most dynamic component of Africa's merchandise trade, increasing fourfold over the last decade; yet Africa only accounts for 2-3 per cent of the global figure. Imports of manufacturing intermediates have expanded remarkably, yet this has largely failed to reverse Africa's premature de-industrialization, and spur the emergence of viable regional supply chains.

Africa's exports of intermediate goods are dominated by mining products and resource-based manufactures such as basic metals or chemicals and fuels; this is consistent with a forward integration into global value chains, but merely as exporter of raw materials and other intermediates embodying limited value addition. Despite its limited size, intra-African trade in intermediates is significantly more diversified than the corresponding trade with the rest of the world. The scope for incipient emergence of regional value chains, particularly in the manufacturing sector, is however still largely untapped due to an array of structural and policy constraints. The shallowness of regional supply chains can be gauged by the fact that Africa sources 88 per cent of its imported inputs from outside the region. Effective participation in GVCs requires investments in sector-specific skills and human capital, as well as infrastructure, financial services and a conducive policy framework. Based on the level of development of these parameters in most African countries, intra-African trade and regional value chains (RVCs) are identified as a platform for learning and enabling economies of scale, thereby facilitating Africa's industrialization and eventual entry into GVCs. This is similar to infant industry argument.

Although manufactured products represent the bulk of imported intermediates, there is little evidence to support the claim that improved access to imported inputs has led to decisive progress of Africa's industrialization. This trade pattern suggests that African producers are increasingly connected to GVCs, but mainly as suppliers of raw materials or other low-end products. The subdued role played by exports of manufacturing intermediates – in particular light manufacturing inputs – concurs with the evidence of persistently limited weight of intra-industry trade in the region, and points to the low level of integration into international production networks, be they regional or global. African countries show high participation rates in GVCs, though at a very low level of the chains. While backward integration has been increasing in many African countries, the larger share of Africa's GVCs participation is still due to forward integration driven by exports of raw materials. This illustrates the fact that African firms operate at the lowest rung of the ladder in GVCs. In the same vein, participation in GVCs per se does not guarantee structural transformation: Africa needs to focus on improving backward integration. Intra-regional trade in processed goods is the first opportunity for African firms to move up the chain. So far, only few firms are driving the growth of Africa's backward integration. GVCs linkages need to be expanded to other firms and areas of the economy.

Global value chains (GVCs) are an important feature in today's global economy and African countries seeking to develop exports and grow their economies need to take them into account. At the same time, the growing importance of information and communications technologies (ICTs) enables African countries to enter several value chains without having to develop the whole production process. Participation in GVCs and competitiveness is linked to having access to priced intermediate imports, with border costs, import tariffs and customs procedures being important factors.

Services play an important role in Africa's economic transformation. They are key inputs to most other businesses, make a direct contribution to GDP and job creation, attract investments into local businesses and are a magnet for FDI. Across African countries, growth in services value added is strongly linked to growth in manufacturing value added. The strong growth of some services sub-sectors in Africa has not always translated into better services for local firms. In many African countries, banks have positioned themselves to lend to large mining projects of foreign investors while local SMEs remain credit-constrained. The services sector can be itself an avenue for economic transformation, particularly for small countries and island states. Not all African countries can develop through manufacturing. The service sector plays an increasingly important role in international trade. Services contribute 50 per cent to Africa's total trade in value added. The term "Servitization" is coined to emphasize the important link between services and participation in value chains.

Preferential schemes have generally been helpful in supporting Africa's trade with preference-giving countries but they have failed to broadly enhance Africa's industrialization so far. Although they remain quite useful and important for Africa looking forward, unilateral trade preferences alone can hardly enable the conditions required for the development of regional value chains.

Fast-tracking the implementation process of Africa's integration, and specifically establishing an African Continental Free Trade Area (CFTA), could go a long way in supporting Africa's industrialization. A CFTA would help increase both intra-African trade and its industrial content; the adoption of trade facilitation measures on top of CFTA reform would considerably enhance further the positive expected outcomes. The level of ambition for Africa's regional integration should be elevated with particularly greater attention given to the development of regional value chains largely untapped within the continent.

The sequencing of trade policy reforms does matter considerably for Africa's industrialization. There is powerful evidence to support that a CFTA should be put in place before other trade agreements are fully implemented by African countries or by the rest of the world (e.g., mega-regional trade agreements[1]) which would not only preserve the anticipated benefits from these agreements but also offset most –if not all– their costs to Africa as well as its industrialization.

African countries need to leverage on the progress that has been made and continue to build robust institutions that maintain and improve the business environment, economic governance and macroeconomic management.

No one-cap-fits-model: From country case studies, different levels of development and the fact that African countries are quite diverse in many dimensions, but most especially in term of endowments, there is no single model that will address issues regarding the trade-industrialization nexus of African countries. It is on this premise that each country or region as the case may be should first determine its best route to structural transformation, if industrialization is favoured and justified by rigorous analysis; the second level entails the determination of the role and place of trade and trade policy. In this vein, individual countries should adopt a trade policy strategy that best suits its initial conditions. However, the diversities create synergies that are yet to be tapped and are only realizable within an effective regional framework.

Gradual approach to industrialization and upgrading: Lessons from experience of industrialized and emerging countries and from African countries' previous attempt at industrialization, suggest that a gradual approach to upgrading and industrialization is practicable and highly recommended. The flying geese model of catching-up process of industrialization, suggests that African economies should start from labour-intensive sectors and upgrade to medium- and high-technology sectors. Since, African countries are at different levels of industrial development, some will have to start with labour-intensive sectors while others should be upgrading.

POLICY RECOMMENDATIONS

Africa needs to translate the current growth into sustainable and inclusive development. In addition to sustaining and improving business environment, good political and economic governance and management, social development strategies that are consistent with the needs of the industrial and modern sectors are required. Conducive socio-economic conditions, peace and security as well as political will are equally important to ensure Africa structural transformation can effectively take place. African countries need to leverage on the progress that has been made and continue to build robust institutions that maintain and improve the business environment, economic governance and macroeconomic management. This will in turn boost investors' and consumers' confidence and further strengthen the continent's future growth prospects. There is the need to ensure that growth is sustainable and inclusive, and the sources of growth are diversified to reduce vulnerability of African economies to internal and external shocks such as droughts, global consumption shocks, and financial, economic and debt crises. In this regard, appropriate policies that promote inclusive growth, productivity and structural transformation through industrialization, value addition, export diversification, and regional integration remain paramount.

Human capital is central to innovation. Technical and technological progress and entrepreneurship linked to knowledge creation and the educational system is the kernel of a social development strategy aligned to a structural transformation agenda. A social development strategy is necessary, anchored within long term planning processes, strengthening the productive capacities of the labour force through high quality, equity-based education and health policies, complemented by investments in research and development focused on driving industrialization, modern services and structural transformation.

The demographic dynamics and urbanization processes currently in force in Africa present a mixed picture of challenges and opportunities, and the factoring of these social phenomena in a structural transformation agenda is important. Africa needs to strategically take advantage of rising wages in China and other parts of Asia and the imminent relocation of labour intensive industries. This calls for education, training and human development of both the skilled and unskilled labour.

A highly selective trade policy that is based on rigorous empirical analysis, carefully designed to promote efficiency of matured firms and protect budding industry, avoid negative policy externalities and put industrial development over and above other objectives is an important step in the trade-induced industrialization. The implementation and management of such a policy is as important as its design. The implementation must be time-bound, progress towards the set objectives and benchmarks are regularly monitored and evaluated and the process carefully managed to avoid political hijack.

African countries need to rethink trade policy as a means to promote industrial development in order to achieve structural transformation that will promote inclusive, stable and sustainable growth; reduce poverty and generate employment. This message calls for deliberate actions that must permeate all levels of trade and investment negotiations as evidence clearly shows that each successive bilateral, regional and multilateral trade negotiations have reduced and constrained the use of traditional trade policy instruments that were once used by developed countries to promote industrialization. African countries should identify and deploy possible alternative instruments within the world trading system that can be invoked to foster industrialization (i.e., coping strategies). The point is that the world will not wait for African countries to catch up with industrialization, rather African countries need to be smart, interrogate the system and deploy trade policy instruments that will foster their industrialization aspirations. Indeed, this is the path towed by late comers in industrial development especially the newly industrialized countries (NICs). African countries should stop negotiating agreements as if industrialization does not matter. African countries should stem the trend in policy-space erosion especially when negotiating any form of trade and investment agreements by insisting on the need to use such policy instruments to promote industrialization of their economies.

In terms of sequencing of trade policy reforms, deeper and bolder regional integration should be followed by gradual opening-up of African economies with the rest of the word as African countries would then be in a better position to compete internationally. Thus, the use of gradual opening and smart protectionism to promote the emergence of regional value chains as a launching pad for development of industry/high value activities is a right step in the right direction.

Trade policy requires complementary policies and various institutional structures to deliver on industrial development

Given that African countries depend on international markets for both inputs and outputs, for the purpose of promoting industrialization trade policy instruments must be carefully selected in order to avoid "negative policy externalities". A thorough thinking-through the process is required to avoid inadvertent effects. Such a policy must promote dynamic efficiency of matured firms and at the same time promote efficiency of infant industry through a temporary shield from the fierce international competition. In the case of infant or budding industry, relative tariff protection combined with different activities directed at developing competitiveness of firms in the industry must be carefully designed and implemented to address the source of externalities. Targets must be set and respected.

Most African countries have embraced development strategies and efforts are being made to ensure that national (including trade and industrial) policies relate very well with the overall national goals and objectives. African countries need to strengthen the links among national development strategies, industrial policy and trade policy. For most African countries, industrial development is just one of the objectives of trade policies. In order for trade policy to foster industrialization, industrial development must be the core objective of trade policy. Thus, for this purpose and to a reasonable extent, coherence between trade and national development strategies are expected to be very high[2]. In addition, the expected sequence is for industrial policy formulation to precede that of trade policy formulation and the latter to aim at promoting the goals and objectives articulated in the former. However, where this sequence is not feasible then a mainstreaming exercise may be required.

Looking at intra-African trade, the weight of manufacturing intermediates is far greater than in the continent's exports to the rest of the world, suggesting a considerable scope for regional supply chains to support Africa's industrialization. Nonetheless, regional value chains are still poorly exploited, and only 12 per cent of Africa's imported intermediates is sourced from the region. A strong production network on the national as well as on the regional level will provide a platform for learning and realizing economies of scale. The leading firms control and set product standards in their value chains that constrains the possibility of local firms to step into higher stages of global value chains. A regional production network should therefore receive greater attention.

Moving up the value chain in agriculture is profitable and needs to be put on the national and regional development agenda. An expansion in these labour-intensive industries generates new jobs that bring a social upgrading. However, given the dominance of leading giant firms in the food value chains, policies need to invest massively in rural industrial clusters development under commodity based industrialization.

Establishing services hubs and regional value chains can help African countries exploit each other's capabilities and boost competitiveness.

African countries should revisit all the various rules of origin (RoO) with a view to relaxing the constraints they imposed on preference utilisation and productive capacity development Indeed, preferential schemes (e.g., AGOA) can surely support Africa's trade; including in manufacturing sectors if the usually stringent rules of origin are relaxed to be adequate and in line with often limited productive capacity of African economies. A more integrated African market can enable the necessary conditions to upgrade productive capacity required to fostering the development of solid regional value chains, and facilitate diversification. The harmonization of rules of origin within the continent and possibly beyond will also be essential in making sure those obstacles to trade as well as to moving up the value chains within the continent are further reduced, thereby strongly supporting Africa's industrialization.

Opening-up Africa's market through reciprocal agreements can also deliver positive benefits to many African countries. Nevertheless, their impact on Africa's industrialization highly depends on initial protection conditions. Africa should, however, seize the opportunity of the economic partnership agreements (EPAs) between some regions and the European Union to strategically determine its external protection structures (e.g., facilitating imports of intermediates to be used in the production of industrial products) with both African and non-African partners. This is critical in rendering more systematic industrialization benefits from bilateral agreements and guaranteeing that regional integration and industrialization efforts are not diluted.

As noted earlier some trade policy instruments that were once used by developed countries to develop their industrial sectors are no longer permissible and new ones have been created. A smart move by African countries desiring to promote industrial development is to audit various agreements that they have signed, with a view to taking advantage of the embedded flexibilities. This process may entail renegotiating the agreements or seek for waivers and concessions. However, an enduring strategy is for African countries to develop capacity (to negotiate, implement, comply with obligations and defend rights) to take advantage of the various trade agreements they have signed. There is no doubt that tariffs are the easiest trade policy instrument to implement and in addition, they also generate revenue for the government. However, other trade policy instruments including para-tariff measures (tariff rate quotas, (TRQs), subsidies (for export and for research and development), contingent trade protective measures (anti-dumping, countervailing, and safeguard measures) are veritable trade policy instruments. Of course, the implementation of these other trade policy instruments is more demanding than that of the tariff measures. Technical capacity needs to be built and appropriate institutions need to be established and rule and regulations need to be enacted in order to invoke them. For trade, to effectively promote industrialization, African countries need to move away from tariff measures only and develop capacity to fully engage in modern trade policy.

The current situation where African countries are more open and accessible to the rest of the world than to themselves is inimical to regional trade and creation and effectiveness of regional value chains. It is therefore imperative to remove remaining tariff and non-tariff barriers not only by consolidating existing RECs, but more broadly across the whole continent, thereby supporting the emergence of viable regional supply networks. This action will also help to fully exploit and maximize the advantage in the diversities of the continent.

Regional trade agreements (RTAs) have the potential to serve as building blocks of the multilateral trading system. While they can complement multilateral trading systems, they cannot substitute it. However, from an empirical point of view, there is powerful evidence to support the fact that sequencing of trade policy reforms matters considerably. To that end, regionalism can be a truly beneficial component of African nations' trade policy reforms. Nevertheless, not all forms of regionalism have the same impact on Africa's trade and industrialization.

The relatively higher freedom in policy options available and expected from South-South engagements than from North-South partnerships, suggests that African countries would gain more by reinforcing trade ties with developing partners. However, opening-up Africa's market should be progressive and ideally intensified once regional integration has considerably deepened across the continent.

Indeed, regional integration seems to show the most convincing outcomes to supporting vigorously industrialization of African economies. Boosting intra-African trade can be achieved rapidly –though the formation of an African mega-regional trade agreement, namely the CFTA– by removing all tariff barriers on goods still remaining within Africa and tackling those related to services as well.

However, it should be emphasized that trade policy alone cannot deliver on industrial development. Complementary policies and various institutional structures are required for trade policy to optimally foster industrialization and structural transformation. African countries should make efforts to mainstream trade policy into development strategies and ensure coherence among all the national policies especially between trade and industrial policies.

Trade policy alone is not a panacea for Africa's industrial development notwithstanding its important place and role in the industrialization process. There are important roles for complementary policies that are coherent with trade and industrial policies. The scope for complementary policies appears limitless as any policy and or action that promotes industrialization in addition to trade policy is qualified. Perhaps, there is need for a strong consistency between macroeconomic policy especially exchange rate policy and trade policy.

In light of Africa's disproportionately high trade-related costs, trade facilitation issues warrant specific attention to reduce the burden of time-consuming and costly administrative and custom procedures. These groups of red tapes acquire an even higher relevance in the context of GVCs, since goods are likely to be exported and imported several times along the value chains.

Addressing Africa's inadequate physical and virtual infrastructural provision (roads, railways, ports, ICTs) and boost its energy production and distribution networks, to close the competitiveness gap faced by African firms is an important undertaking in the process of making trade and trade policy promote industrialization Policy initiatives at the sectoral level that improve infrastructure and linkages among firms in the value chain (e.g., Mozal project in Mozambique) can increase Africa's backward participation in GVCs. The poor connection between successful sectors and other areas of the economy is a huge constraint for Africa to exploit the full potential from GVCs. Hence, policies need to focus on establishing production networks within the African economies.

Establishing special economic zones (SEZs), trade zones and export processing zones including a national production network or industrial clusters to include more SMEs/SMIs and promote increased linkages to other areas of the economy is an important step in technological transfers, which could be further expanded to neighbouring countries. While many African countries have established SEZs, their operations, especially the link with the rest of the economies, are less effective to promote the required spillover effects to rest of the economies.

National policies have to be complemented by strong regional policies including regional infrastructure, ICTs, logistics and convergence in regulatory policies. National policies have to focus on labour-intensive sectors and should give a higher weight to the agriculture sector in order to bring a social upgrading rather than only an economic upgrading.

ENDNOTES

1 Mega-regional trade agreements (MRTAs) are profound integration partnerships between countries often from different regions; each MRTA usually accounts for a significant share of world trade and GDP.

2 The observed high coherence is attributable to at least two efforts namely: (1) UNDP's mainstreaming trade project and (2) Enhanced Integrated Framework (EIF). The objectives of these efforts emphasize the need for trade policy to be pro-poor.