

**MAKING THE MOST OF AID:
CHALLENGES FOR AFRICA'S AGRIBUSINESS**

by
Jeff Dayton-Johnson and Kiichiro Fukasaku

- Aid and trade policies – in OECD countries and in developing countries – might reinforce each other to promote development, or they might be substitutes: the sign of the correlation between trade and aid flows depends on the context.
- East Asia's rapid growth demonstrates the important development impact of the trade-aid link.
- While aid has played a strong complementary role for trade development in Viet Nam, for example, the current impasse of African cotton producers is emblematic of trade and aid policies working at cross purposes.
- The experience of six African countries reviewed in this brief highlights the case for development assistance that aims to eliminate bottlenecks preventing a greater and deeper African participation in the global trading system.
- The scaling-up of aid, macroeconomic stability and trade expansion are compatible and the ongoing international "aid for trade" initiative will remain critically relevant for African development in the coming decades.

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Executive Summary

- Aid and trade policies — in OECD countries and in developing countries — might reinforce each other to promote development, or they might be substitutes: the sign of the correlation between trade and aid flows depends on the context.

While aid and trade might be substitutes in the longer term — for example, if increased trade flows reduce the need for development assistance — evidence from many developing countries suggests that in the medium term, aid and trade might be complements. That is, increased aid flows can increase a developing country's trading capacity, and ultimately its trade flows.

- East Asia's rapid growth demonstrates the important development impact of the trade-aid link.

The experience of East Asia's development provides useful examples of complementarities between trade and aid flows, and trade and aid policies. Over the last several decades, foreign aid to the economies of the region, largely in the form of concessional loans, supported trade and economic growth by providing resources for economic infrastructure and human resource development.

International aid also helped to strengthen recipient countries' policy frameworks and institutional fundamentals, as was the case in China's reform experience. More recently, the experience of Viet Nam indicates that the strong degree of ownership of its development agenda has allowed the country to achieve a high degree of donor co-ordination, and the distribution of official development assistance (ODA) funds has largely followed Viet Nam's development preferences.

- While aid has played a strong complementary role for trade development in Viet Nam, for example, the current impasse of African cotton producers is emblematic of trade and aid policies working at cross purposes.

The most recent of the strong performers in the East Asian region is Viet Nam. Among the reasons for its successful export-led development,

in addition to far-reaching domestic reforms, is that OECD countries have been prepared to complement their aid policies with favourable trade conditions for Vietnamese exporters at least until quite recently.

Donors' stance toward Viet Nam in this respect contrasts markedly with the experience of West African cotton producers. On the one hand, African cotton producers receive foreign aid to reform and revitalise the production capacity of the sector. On the other hand, cotton producers face unattractive world prices and trade distortions caused by subsidies to cotton producers in OECD countries.

- The experience of six African countries reviewed in this brief highlights the case for development assistance that aims to eliminate bottlenecks preventing a greater and deeper African participation in the global trading system.

An analysis of two strong macroeconomic performers — **Uganda** and **Mozambique** — demonstrates that higher rates of economic growth and poverty reduction can be achieved in the presence of responsible economic management, expansion of trade and development assistance from abroad. Here, the most important bottlenecks to the expansion of trade have not always high tariffs on their exports in OECD countries: even with essentially tariff-free access to OECD markets, export growth is limited by non-tariff barriers. Finally, though trade liberalisation might have disappointingly small effects in Africa, these countries' recent history shows that aid-trade complementarities are nevertheless important.

Efforts by **Tanzania** and **Zambia** to bolster primary sector exports illustrate lessons for using aid to promote trade capacity. In both countries, as in much of Africa, exports are hampered by low agricultural productivity, associated with traditional smallholder production systems. More aid can be used to link farmers to processing firms, exploiting existing potential to develop agro-food industries. The trade dimension of agriculture and agribusiness has been underscored in both countries: hundreds of thousands of farmers now export tobacco, fresh vegetables and flowers through out-grower schemes. These encouraging developments have occurred, despite relatively small amounts of trade-related technical assistance and capacity building (TRTA/CB) to both countries. Furthermore, little has been channelled to "behind-the-border" constraints — post-harvest handling and processing, preservation and packaging, quality enhancement, meeting technical requirements for entry into OECD markets; increased aid for trade to address these bottlenecks promises to yield a high return.

The experiences of **Senegal** and **Mali** highlight several lessons regarding agro-based private sector development. First, insufficient coordination among different government bodies creates bureaucratic delays and fragmented policies. Though diversification is proceeding, it generally caters to domestic, rather than international, markets. In both countries, significant progress has been made in developing agricultural capacity in recent years, but much remains to be done, including improvements in the flow of information regarding market conditions. Finally, smaller producers are severely constrained by the insufficient provision of financial services and by costly infrastructure, among other reasons.

- This Brief concludes that the scaling-up of aid, macroeconomic stability and trade expansion are compatible and that the ongoing international "aid-for-trade" initiative will remain critically relevant for African development in the coming decades. It also makes several recommendations for policy innovations.

Cotton and Beyond

Few cases of incoherent international policies are as glaring as those that affect African cotton. On the one hand, low-income cotton-producing countries in Africa face unattractive world prices and trade distortions caused by subsidies to cotton producers in developed countries. On the other hand, the same African countries receive foreign aid to reform and revitalise their cotton producing capacity; according to the World Trade Organization (WTO) Secretariat, the global amount of development assistance provided directly and indirectly to the cotton sector totalled \$6.85 billion¹. The stake is particularly high for West African countries where cotton is the driving force of agriculture. In Mali, the biggest cotton-producing country in the region, 3.5 million people — a quarter of the country's population — depend on cotton for their livelihood². Taking West Africa as a whole, some 16 million people are engaged in the cotton sector³.

In this context, four African countries (Benin, Burkina Faso, Chad and Mali) submitted the Sectoral Initiative in Favour of Cotton (hereafter referred to as the C-4 initiative) to the WTO in May 2003. At the Hong Kong, China Ministerial Conference in December 2005, WTO member countries attached high political importance to resolving the cotton issue. They delivered clear results on two of the three pillars of the C-4 initiative, namely, elimination of export subsidies by 2006 and duty- and quota-free access for cotton exports from least developed countries (LDCs). On the other hand, the third pillar of the C-4 initiative, i.e. elimination of trade-distorting domestic subsidies, was left to the ongoing agriculture negotiations. Nevertheless, at the WTO Special High-Level Session on cotton in March 2007, the WTO Director-General reaffirmed the organisation's commitment to an ambitious, expeditious and specific outcome on cotton across all three pillars of the agriculture negotiations. If the trade-related restrictions on cotton-sector development were lifted, then development assistance targeted at the sector would be better able to promote export growth. Thus cotton remains a litmus test for collective efforts to enhance synergies between trade and aid policies for better development outcomes.

The issues extend beyond cotton. African countries more generally seek to diversify their export profiles in order to seize new business opportunities arising from globalisation. The experiences of several countries on the continent demonstrate that diversification opportunities exist and new areas of competitive advantage can be developed⁴. For the

majority of African countries, however, export diversification has yet to occur. The diversification index for Africa as a whole *declined* between 2001 and 2005 (see Annex Table 1). A strong rise in international demand for oil and minerals, fuelled by large dynamic economies such as China and India, has led to greater concentration of the exports of most African countries among a small number of products⁵.

Increased trade opportunities continue to be the most important contribution the WTO can make to African development⁶. It should be noted, however, that sub-Saharan African countries already enjoy considerable access to markets in OECD countries. Many African countries have already been granted non-reciprocal preferential treatment in a variety of GSP (Generalised System of Preferences) schemes, including the European Union's Everything But Arms (EBA) Initiative⁷ and the United States' African Growth and Opportunity Act (AGOA)⁸. Many current or promising potential exports from Africa enjoy virtually duty-free access to OECD markets; tariff barriers are not the biggest problem. More problematic are non-tariff barriers, such as standards, sanitary and phyto-sanitary (SPS) measures and rules of origin regulations. But, even greater obstacles are many "behind-the-border" problems in African countries. These include tackling supply-side constraints: among them, difficulties importing essential materials at world prices to expand exports, enhancing the ability of domestic firms to meet price and quality requirements of global supply chains, building legal and physical infrastructures conducive to international business development. Limited access to finance by local firms, notably small- and medium-sized enterprises (SMEs), is likewise a serious obstacle to both local and overseas business development. Therefore, one of the most important tasks for both bilateral and multilateral donors is to provide the financial and technical assistance needed to help African countries tackle these supply-side constraints.

Development assistance that aims to eliminate bottlenecks to greater participation in the global trading system is an example of complementarity between aid and trade policies. Conversely, the current impasse of African cotton producers is emblematic of aid and trade policies working at cross purposes. This *Policy Brief* will discuss the nature of interactions between trade and aid policies in an African context, synthesise lessons from six African case studies (Mali, Mozambique, Senegal, Tanzania, Uganda and Zambia) and draw some implications for the ongoing international aid-for-trade initiative. These case studies have been made public as background documents for the OECD Policy Dialogue with Non-Members on Aid for Trade: from Policy to Practice, in Doha, Qatar on 6-7 November 2006⁹.

Trade and Aid Policies: Exploring the Links

Trade and aid policies interact in different ways. This section recapitulates key features of the interrelation between trade and aid policies in the current African context¹⁰.

First, we look at the trade-aid links from the perspective of the balance of payments. It is important to note that aid flowing from an OECD country to an African country might increase or decrease trade between those countries. On the one hand, aid is considered as increased saving and can finance increased imports in the recipient country. But a dollar of aid would not automatically lead to a dollar of imports from the donor country, unless aid is completely tied to purchasing goods and services from the donor country. Instead, aid flows might increase imports from third countries. On the other hand, aid is an influx of foreign currency that might increase the recipient country's real exchange rate, which might in turn depress the latter's non-tradable exports (e.g. manufactured goods and processed agricultural products); this is the so-called "Dutch disease" effect, the relative importance of which depends critically on how much of aid is spent in the non-tradable sector, such as public service and construction. Evidence of a Dutch disease aggravated by aid is not always apparent in the country cases reviewed in the following section: evidence of real exchange rate appreciation is mixed at best in Uganda, and non-existent for Mozambique.

These complex links between trade and aid arise for two different reasons. First, the discussion so far assumes that aid is fully disbursed in a recipient country. This is not the case in sub-Saharan Africa, however. A recent evaluation report by the International Monetary Fund (IMF) (2007) indicates that the region's countries with a Poverty Reduction and Growth Facility (PRGF) spent an average of only 28 per cent of aid flows during the period of 1999-2005. The remaining 72 per cent was programmed as public savings, often through the retirement of domestic public debt. Therefore, much of aid flowing into sub-Saharan Africa was not converted into higher payments for imports. Second, the causality might run from trade to aid flows. For instance, increased trade links between an OECD and an African country might enhance the urgency of addressing certain supply constraints (e.g. inadequate transport infrastructure) in the latter country, and the donor country exporters might accordingly press their government to increase aid in order to relieve those constraints.

Thus, standard economic reasoning does not allow us to form any prior expectation about the sign of correlation between bilateral aid and trade flows. This does not mean that aid does not matter for trade: quite the contrary, aid can play a critical role in trade expansion in a recipient country. The development experience of East Asian economies over the last several decades suggests that international aid, largely in the form of concessional loans, supported the developing economies' trade and growth through financing economic infrastructure and human resource development (Box 1). International aid also helped to strengthen recipient countries' policy frameworks and institutional fundamentals, as was the case in China's reform experience.

Box 1. What's Different About East Asian Economic Performance?

There is little apparent difference in the degree of economic openness between East Asia and sub-Saharan Africa (Box Table 1). What has made the development experience of East Asia a unique phenomenon is a rapid rise in a new type of foreign direct investment (FDI) since the mid-1980s, namely, export-oriented, manufacturing FDI, particularly of a production-fragmenting type. Many East Asian economies have significantly, and in some cases (such as China) dramatically, altered their attitudes and policies concerning FDI. This alteration is closely linked to a significant shift in growth strategies: FDI can play an important role in the development of new export bases in investment-receiving economies, the restructuring of investment-sending economies, the expansion of trade flows, the transfer of technology and knowledge and hence the growing interdependence of national and regional economies. It also serves as a long-term financial flow to finance current account deficits. Among the developing areas, the East Asia region has been a highly attractive location for the new type of FDI, though foreign investors have increasingly taken a differentiated approach when investing in different countries within the region.

While trade and FDI flows are closely linked through the procurement and sales activities of multinational enterprises (MNEs), the net impact of FDI can be either trade-creating or trade-replacing. In fact, the relationship between trade and FDI flows is very complex at both macroeconomic and firm levels. Nonetheless, FDI flows in East Asia tend to be more trade-creating than trade-replacing, because of the region's growing emphasis on export-oriented manufacturing production.

Box 1 (contd.)

The positive joint effect of trade and FDI on growth is one of the most critical factors underlying the strong growth performance of East Asian economies since the mid-1980s. In other words, a key feature of East Asia's outward-oriented growth model is the emergence of a "trade-FDI nexus"¹¹; liberalisation of trade and investment policy regimes *unilaterally* undertaken by many economies in the region has improved the policy environment, favouring the expansion of both trade and FDI flows. Conversely, strong trade and FDI performance have encouraged governments to sustain outward-oriented trade and investment policies, thereby integrating their economies more closely into the international market. For instance, unilateral tariff reductions for parts and components in machinery industries, together with the extensive use of a duty drawback system (in which authorities refund customs or excise duties paid by the manufacturer upon export of the finished product), have played a pivotal role in the formation of international production and distribution systems, thereby stimulating intra-regional trade and investment in manufactured goods, especially electronic products.

The role of FDI for East Asia's clustered, sequential growth has been quite diverse among the economies of the region, however; some have relied more on FDI than others. For those economies, such as Hong Kong, China; Singapore; Malaysia and, more recently, China and three new members of ASEAN (Cambodia; Lao PDR and Viet Nam), FDI inflows have become increasingly important for their economies. This is in sharp contrast with the experience of Japan, Korea and Chinese Taipei in the early decades of the post-war development, as these economies relied much less on FDI as a package and more on licensing arrangements as a means of importing foreign technology. It is only quite recently (particularly, after the 1997-98 crisis) that FDI inflows have started to rise markedly in Chinese Taipei and Korea, as these economies have eased restrictions or taken measures to encourage such flows.

Looking at the other side of FDI flows, not only Japan but also more advanced developing economies, especially the four Asian newly industrialising economies (NIEs), have emerged as direct investors in the region. These economies are climbing up 'technological ladders' in industrial development and relocating labour-intensive segments of production to less-advanced developing economies. China has benefited enormously from this clustered, sequential development process since the mid-1980s. More recently, it appears that similar forces are at work in driving the Vietnamese economy.

Source: Fukasaku *et al.* (2005), Fukasaku *et al.* eds. (2005) and OECD (2006a)

Box Table 1. **Economic Openness: East Asia and Africa**
(2002-05 Average)

	East Asia	Sub-Saharan Africa
Aid (% of GNI)	0.3	5.6
Merchandise trade (% of GDP)	66.6	54.1
FDI, net inflows (% of GDP)	2.7	2.9
Remittances (% of GDP) ^a	1.5	1.6
Manufactured exports (% of merchandise exports) ^b	80.3	35.3 ^c

Notes:

a) Workers' remittances and compensation of employees, received.

b) SITC Sections 5 to 8, excluding 68 and 891.

c) 2002-2003.

Source: World Bank, World Development Indicators online.

Indeed, some aid spending takes the form of aid *for* trade, with a view to helping realise a developing country's export potential. This is predicated on the idea that aid and trade are complements; in other words, the interactions between these two policies are mutually reinforcing. Aid for trade may be targeted to increase a poor country's trade capacity in a narrow sense (i.e. trade-related technical assistance) or in a broader sense (i.e. building productive capacity and trade-related infrastructure). Kokko *et al.* (2006) presents an insightful case of Viet Nam, exploring how the aid and trade policies of OECD countries have interacted to impact on that country's highly successful development performance (Box 2).

Box 2. **Lessons from Viet Nam**

Have the policies and actions of individual OECD countries in the trade and aid domains had synergy effects, intended or unintended, on Viet Nam's development since the late 1980s? Overall, the answer is positive. Given Viet Nam's strong degree of ownership of its development agenda, the country has been able to achieve a high degree of donor co-ordination, and the distribution of ODA funds has largely followed the country's development preferences.

Box 2 (contd.)

This notwithstanding, the donor community has put mild pressure on Vietnamese development policy in order to promote certain principles that are supported by most donors. Given Viet Nam's past as a planned economy largely isolated from global markets, donors argue that Viet Nam should turn decisively towards market-oriented policies, domestically as well as internationally. Integration with the world economy and strong export orientation are considered important to generate growth and to alleviate poverty, and some of the ODA funds flowing to Viet Nam have focused on projects with these specific objectives. The Vietnamese leadership has largely accepted these views, and trade liberalisation and internationalisation are important components of the ongoing transition of the Vietnamese economy and society. The results have been highly successful. The average annual export and import growth rates since the early 1990s have been close to 20 per cent, while annual GDP growth has exceeded 7 per cent. Per capita incomes have roughly tripled, and the poverty rate has fallen by almost two-thirds.

One reason for the successful export-led development (apart from Viet Nam's domestic reforms) is that OECD countries have been prepared to complement their ODA policies with favourable trade conditions for Vietnamese firms. Although Viet Nam was not a member of the WTO until January 2007, most OECD countries had offered market access on GSP terms, which means that the nominal tariffs for most manufacturing goods are zero or insignificant. Trade barriers remain higher for agricultural products, in particular processed food products. This is unfortunate, because it limits the possibilities for higher value-added activities in agriculture. In Viet Nam, rural industrialisation and employment creation is an urgent challenge, since 70 per cent of the population live in rural areas. Yet, Viet Nam is not alone in suffering from the inward-oriented agricultural policies of OECD countries, and it shares the same problem with a large number of other developing economies in the region and elsewhere.

Source: Kokko *et al.* (2006)

Box Table 2. **Top Ten Aid-for-Trade Recipient Countries in Asia**
(2002-05 average, \$ million at 2004 constant prices)

1	India	1 392
2	Viet Nam	1 392
3	Indonesia	1 089
4	China	708
5	Bangladesh	662
6	Afghanistan	598
7	Sri Lanka	415
8	Pakistan	408
9	Thailand	348
10	Philippines	315

Placing Trade-Aid Links in an African Context

Despite recent policy initiatives to open up the economies of the continent, sub-Saharan Africa has yet to witness the emergence of a trade-FDI nexus such as was observed in East Asia (and described in Box 1). Instead, sub-Saharan Africa's share of global exports has substantially declined (from 3.4 per cent in 1970 to less than 1.5 per cent in 2005). Many African economies still rely heavily on a narrow range of primary-commodity exports. For various reasons such as the relative land abundance per worker, poor transport infrastructure and underdeveloped logistic services, they will likely remain, at least in the foreseeable future, net exporters of primary, rather than manufactured, products. Agricultural products, mostly unprocessed, will continue to have a considerable weight in their export profile.

Africa's diversification and trade strategies should be reconsidered in light of increasing competition from China, India and other Asian countries in clothing and other labour-intensive manufacturing industries¹². For commodity-dependent African countries, agro-based industrialisation and diversification into higher value-added food products would appear more promising than moving into traditional, labour-intensive manufacturing activities. A combination of different factors, including changing consumer patterns in OECD countries, globalisation of retailing activities and a likely increase in domestic demand in more advanced developing countries (driven in part by urbanisation in those countries), represents significant trade opportunities for African producers in the coming decades.

Even if the development of non-traditional agricultural exports represents a promising opportunity for African countries, the potential gains from traditional export crops also remain sizeable¹³. Growing world trade, fuelled by further trade liberalisation and rising incomes in the developing world, could provide them with an ample opportunity to expand these traditional exports and break into new dynamic markets, including several rapidly expanding Asian markets. Exporters of traditional agricultural products could also benefit significantly from product differentiation, targeting higher-value market niches. This is the case, for instance, of specialty coffee in Tanzania, where initiatives are underway to accomplish certification and improve marketing, which could increase income for coffee growers. Likewise, by raising the average quality of traditional products and establishing grading systems, many countries in the region could secure better rewards for their exports.

The expansion of traditional exports is not without obstacles, however. Many products face tariff peaks (a single tariff or a small group of tariffs that are particularly high). Moreover, the tariff schedules of countries where current and potential markets lie are often marked by tariff escalation, i.e. the tendency for tariffs to be higher on processed goods than on the raw materials from which they are produced. These tariff-related factors discourage development of higher value-added lines of production linked to traditional primary commodity exports. These bottlenecks are compounded by complex non-tariff trade measures, including phyto-sanitary measures and standards.

Nevertheless, development of agro-enterprises holds remarkable potential as the cornerstone of a trade-based growth and poverty reduction strategy. As the interface between markets and rural households, agro-enterprises are key actors in the process of agricultural modernisation and industrialisation, thereby creating synergies between agriculture and industry. Efforts should therefore be made to favour the parallel development of agricultural production and of downstream, agro-based industries and activities. The agribusiness sector in Africa is small and dominated by a few large enterprises¹⁴. The size of Africa's agribusiness is just under \$70 billion, representing approximately 1 to 2 per cent of the world agribusiness, or about the same as that of Thailand and one-quarter of that of Brazil¹⁵.

This is the context in which so many African countries have shown strong interest in "aid for trade" as a mechanism to help build domestic supply capacity (particularly, but not exclusively, in agribusiness) and improve trade-related infrastructure, thereby expanding exports. Aid-for-trade initiatives explicitly recognise that aid and trade policies are complements; a judicious mix of multilateral trade liberalisation which leads to improved market access for African countries and aid spending by developed countries would be more effective than either policy in isolation. In the next section we will take a close look at the experience of several African countries and draw lessons.

Aid, Trade and Development: Lessons from Africa

Though Africa's export performance lags notably behind that of East Asia, there are nevertheless a variety of experiences with aid, trade and development in Africa from which meaningful policy lessons can be drawn. In this section, we distil lessons from six country case studies

co-ordinated by the OECD Development Centre. There are three registers to our analysis, each of them explored in two countries:

- *The macroeconomic link between aid and trade:* At the economy-wide level, are aid and trade substitutes or complements? We address this question with evidence from Mozambique and Uganda.
- *Aid and the strengthening of primary commodity exports:* How have aid-for-trade programmes helped agricultural and other primary producers diversify production and move up value chains to gain more from international trade? We assess these questions in the light of the experiences of Tanzania and Zambia.
- *Private sector development and agribusiness:* At the microeconomic level, can aid for trade foster greater exports by strengthening the capacity of private sector actors to respond to opportunities? We look at the evidence of Mali and Senegal.

It may be worth noting that four of six country studies reviewed below focus on the case of agriculture and agribusiness. The underperformance of agriculture has been a major drag on economic and social development in the continent. Both African governments and the donor community largely neglected the agricultural sector during the 1980s and 1990s. Thanks to the recent NEPAD initiative on agriculture as a sectoral priority, they have begun to refocus policy attention on the importance of agriculture for Africa's long-term growth and poverty reduction¹⁶.

Aid and Trade: Complements or Substitutes? Evidence from Uganda and Mozambique

The experience of Viet Nam (Box 2) suggests that aid and trade flows (like investment and trade in the case of East Asia summarised in Box 1) are complements rather than substitutes. That is, trade liberalisation and expansion can more effectively contribute to growth and poverty reduction in the presence of aid flows that build capacity. Alternatively, aid flows can more effectively achieve their objectives in the presence of a rational trade policy. Older thinking tended to view these flows as substitutes. On that view, a rich country could liberalise access to its market in order to reduce its aid spending (or increase its aid spending in lieu of trade liberalisation)¹⁷. In the long run, of course, the older thinking could be correct: successful integration into the world trading system might drastically reduce the need for development assistance in Africa. But in the short to medium term, aid might help African countries derive greater

benefits from global trade. Two case studies of strong macroeconomic performers in Africa — Uganda¹⁸ and Mozambique¹⁹— provide evidence on the links between aid and trade flows, and lessons regarding how these interactions can be more ably exploited by policy makers.

First, higher rates of economic growth and poverty reduction are possible in the presence of responsible macroeconomic management, expansion of trade and development assistance from abroad. Uganda is a case in point; successive attention to fiscal control, rationalisation of the market for foreign exchange, improvement in the environment for both domestic and foreign investment have all contributed to economic growth rates in excess of 6 per cent and a reduction of the poverty rate from 56 per cent of the population in 1992 to 38 per cent in 2003. Successful macroeconomic performance in Uganda since the late 1980s has been accompanied by export diversification. (Annex Table 1 reveals that Uganda's export diversification index is above average, but the level of diversification fell between 2001 and 2005.) New export sectors (fish, cut flowers) flourished, while traditional exports (notably coffee) declined. The outward orientation of the economy was consolidated: exports as a share of GDP rose from about 8 per cent in 1987 to over 14 per cent in 2005.

Development assistance to Uganda, meanwhile, increased substantially in the late 1980s, following the departure from power of the despotic Amin and Obote regimes. Aid (in absolute terms and in proportion to GDP or the population) would stagnate, though with some year-to-year volatility, in the 1990s, to rise again after 1999.

Mozambique too has enjoyed consistently strong macroeconomic performance associated with a commitment to reform, following a long and costly civil war. Mozambique's sound economic management has been rewarded with comparatively generous amounts of aid from Development Assistance Committee (DAC) donor countries and multilateral institutions. While ODA may have contributed to the growth of consumption and investment in the Mozambican economy, trade plays an important role as well.

The second lesson from Uganda and Mozambique is that the most important bottlenecks to the expansion of trade are not high tariffs on their exports in OECD countries. Take the case of Mozambique, whose foreign trade position is similar to that of many other African countries. The country enjoys preferential access to important export markets, notably the European Union (through the Everything But Arms initiative) and the United States (through the African Growth and Opportunity

Act). In its neighbourhood, Mozambique benefits from its membership in the Southern African Development Community (SADC)²⁰. Though these trade agreements eliminate or reduce tariffs on a wide range of goods, the development prospects for expanding exports under their aegis are more difficult than they first appear. Export growth is limited by non-tariff barriers including rules of origin (ROO), sanitary and phyto-sanitary (SPS) measures, and safeguards. ROO, critics claim, prevent Mozambique and other developing countries from participating in effective supply chains and from using imported inputs; this constraint is particularly acute for textiles in Mozambique, although the country has been granted a special waiver under the AGOA. Safeguard measures and graduation mechanisms in these agreements offer Mozambique's richer trading partners a way to prevent and harm the expanding export industries at very short notice.

Given that tariffs are already low or non-existent for so many Mozambican exports, further liberalisation is predicted to generate small, if any, benefits for the country. Simulation analysis (based on computable general equilibrium (CGE) models²¹) suggests that the Doha Development Round of WTO negotiations, even if it is renewed, will do little to promote growth in Mozambique. This weak Doha effect arises for two reasons: partly because Mozambique is a net food importer and further liberalisation would raise food prices; and partly because a simultaneous increase in exports by many developing countries would lower the prices of those exports. Mozambique stands to gain from further liberalisation in the larger sub-Saharan African region, given that it already produces a more diversified mix of commodities than most of its neighbours (and barriers to trade remain high, so that there is great scope for further liberalisation), but it is not clear that Mozambique would gain from further integration within the SADC region.

What is striking overall about the estimates of welfare gains to the Mozambican economy is their small size, even in the case of quite large tariff reductions, and their sensitivity to the particular pattern and combination of tariff reductions²².

Third, though deep trade liberalisation might have disappointingly small consequences in Africa, the Uganda and Mozambique case studies suggest that exploiting the complementarities between aid and trade could be a promising strategy. The potential is illustrated by a careful reading of the Ugandan experience. Development assistance has an important effect on exports and imports in Uganda. To begin, aid has increased the import capacity of the Ugandan economy. Furthermore, aid has arguably had an important qualitative effect on Uganda's trade capacity, through the

impact of policy dialogue with donors on economic reforms. Liberalisation of cotton and coffee marketing depended critically upon this dialogue; these reforms, meanwhile, together with reforms of foreign exchange markets, facilitated growers' responses to the coffee boom of the mid-1990s. It must nevertheless be acknowledged that when coffee prices subsequently crashed, the incidence of poverty rose in Uganda. Evidence from other countries, such as Burkina Faso and Ghana, suggests that a partial liberalisation of trade, together with a well-functioning marketing board, could be more conducive to sustained poverty reduction than was Uganda's more liberal approach.

The direct impact of aid on bilateral trade flows can be quantified. Econometric analysis for Uganda suggests that aid has a statistically significant but economically small effect on bilateral exports; in other words, one dollar of additional aid from a donor will on average lead to an increase of the donor's exports to Uganda of 4.5 cents. About half of this effect is due to tied aid (in which development assistance is given on the condition that it be used to purchase goods and services from firms in the donor country). Overall, these are small numbers: the distortionary effects of tying are negligible.

Would aid do more than trade to foster growth in Mozambique? Further CGE modelling by Haaparanta and Kerkelä (2006) analyses the effects of using aid to reduce trading costs (which include administrative costs imposed by Mozambique and its trading partners) — the purported objective of aid for trade. A 10 per cent decrease in trading costs would shift resources in the Mozambican economy to non-traditional sectors, including manufacturing, fisheries and forestry. The positive effects of this restructuring offset, in the simulation, any "Dutch disease" effects of higher export prices. In practice, aid to reduce trading costs should focus on credit availability for growing firms and increased business capacity, as Haaparanta and Kerkelä (2006) identified these as the principal bottlenecks for growth in Mozambique.

Given that a large and growing share of aid to both Mozambique and Uganda takes the form of budget support, the question is not really whether donors' aid policies and trade policies are coherent, but whether African governments' policies are consistent with trade policies. The role of donors is to support African countries as they promote trade in a coherent way.

Adding Value in Primary Sector Exports: Lessons from Tanzania and Zambia²³

How can development assistance promote trade capacity in Africa? One important channel involves adding greater value to primary products in which the continent is rich, but which are all too often exported in unprocessed form. Like all aid programmes, such capacity building initiatives must confront the dual problems of alignment between donors' and recipients' objectives, and harmonisation among donors' efforts.

In this connection, both Tanzania and Zambia exhibit great potential for agricultural and agribusiness development, though still heavily dependent on the export earnings from unprocessed primary commodities. While diversification is more advanced in Tanzania than Zambia (See Annex Table 1), gold and copper, respectively, dominate the recent export development of these two countries.

While current donor programmes (both bilateral and multilateral) in Tanzania still display significant differences with regard to modalities used to deliver aid, there are genuine efforts being made to align their activities with government strategies and policy frameworks, encapsulated in the National Strategy for Growth and Reduction of Poverty, the country's second-generation Poverty Reduction Strategy Paper (PRSP) (locally known as MKUKUTA). Donors are gradually focusing their interventions on those areas in which they are acknowledged to have comparative advantages. Harmonisation efforts are apparent in the steps being taken to improve donor co-ordination.

As for the agricultural sector, Tanzania has undertaken a sector-wide approach to implement its Agricultural Sector Development Strategy (ASDS). This is not in itself a new aid instrument or modality, but rather an attempt to create an environment conducive to enhanced agricultural productivity, improved farm incomes and increased private investment in the sector. The ASDS aims to develop a comprehensive and coherent sector policy with a unified expenditure framework for local and external resources under a common management and reporting system. How to operationalise it and deliver concrete results is a major challenge for all stakeholders in Tanzania.

In the case of Zambia, a number of important challenges stem from the peculiar characteristics of its mineral-based economy. Booming revenues from copper exports, debt forgiveness and scaling-up of aid have caused large capital inflows into its comparatively tiny domestic financial

market, leading to a rapid appreciation of the local currency, the kwacha: this is perhaps the biggest challenge to the country's trade expansion today²⁴. There is fear that the gains made in raising non-traditional (agricultural) exports may be significantly eroded by the kwacha's rising value. Whether this is only a transitory cost has yet to be seen. But there are serious concerns that poverty will be further entrenched, as many small farmers participating in export businesses through out-grower schemes will be affected.

Related to this is the challenge of building trade capacity in an economy susceptible to the "Dutch disease" effect (discussed in the previous section). How to improve the management of commodity-related revenues remains a big issue. There are nevertheless measures that Zambia can take to limit the negative impact of the appreciation of the kwacha, such as maintaining fiscal discipline and refraining from running up domestic debts. Donors, for their part, can make aid disbursement more predictable, allowing more timely government expenditures: delays in paying suppliers of goods and services to the public sector make the country's macroeconomic environment more vulnerable.

The experiences of Tanzania and Zambia highlight several important lessons. First, the fundamental problem in both countries lies in the low productivity of the agricultural sector, which is in turn often attributed to the predominance of the traditional smallholder production system and the inadequate use of fertilisers and extension services. This partly reflects a legacy of the past development strategies in both countries. For instance, in the past, Tanzania sought to maintain 80 per cent of the population in the smallholder production system. The market-oriented reforms of the 1990s removed many obstacles and triggered necessary adjustments. However, the remaining structural and policy constraints and institutional weaknesses have combined to limit the development of commercial farming and contribute to the sluggish productivity growth of the rural sector.

A second lesson concerns the key role aid could play in strengthening the capacity of rural farmers as "micro-entrepreneurs" and in linking them to processing firms, so as to exploit the existing potential to develop agro-food industries. Indeed, agro-based, private-sector growth is an area to which all donors in both countries attach considerable importance, but there is a multiplicity of (often small) interventions, and the majority of these interventions are targeted at increasing rural incomes and improving household and national food security. What is less frequent is support for the development of commercial farming and specific production capabilities

relevant for higher value addition (e.g. compliance with safety and quality standards, packaging, processing and marketing) and the development of new crop varieties.

The renewed attention to the growth and poverty-reduction potential of private business has triggered a significant change in approach. While food security remains high on the agenda, donors acknowledge that a successful agricultural sector should be vibrant and growing at all points along the value chain. They have put an increasing emphasis on diversifying the income sources of rural households and promoting transformation from subsistence to commercial farming. In both countries, donor co-ordination at the sector level is progressive, and donor interventions are consistent with, and supportive to, the priorities set out in nationally driven poverty reduction strategies. They also adhere to the basic principles of the *Paris Declaration on Aid Effectiveness*.

Third, the importance of "trade components" of agriculture and agribusiness should not be overlooked. Trade can be a powerful engine for growth and poverty reduction. Both countries recognise in their development strategies that agricultural trade can have a strong impact on the livelihoods of the poor, who live predominantly in rural areas. In Zambia, between 250 000 and 300 000 small farmers participate in exports through out-grower schemes in the cotton, tobacco, and fresh vegetables and floricultural sectors. This number should be compared with the size of the formal sector which currently employs 500 000 people. No other sector directly affects the lives of poor people in the same way that agriculture does. The mining sector at its peak employs only 35 000 people. Although efforts are underway to develop small-scale projects in the mining and the precious stone sector (for instance, through an EC-funded project), mining remains highly capital-intensive and will thus have less impact on employment even when copper production increases.

Fourth, the amount of trade-related technical assistance and capacity building (TRTA/CB) committed to Tanzania and Zambia has been relatively small. According to the WTO/OECD database, Tanzania and Zambia received some \$103 and \$71 million respectively in TRTA/CB over 2001-04. Only a very small part of such assistance went to finance agro-related projects²⁵. Moreover, there are only modest interventions to address "behind-the-border" constraints, which are recognised as the most serious impediments to building productive capacity and entering into global value chains. The following links in the value chain are seriously underdeveloped and poorly supported in Tanzania: post-harvest handling and processing, preservation and packaging, quality enhancement and

management, meeting SPS and other technical requirements for entry into international markets. Similar concerns are voiced in Zambia as well. Support to these areas, particularly if channelled *via* local organisations that have some proven track record and through reputable exporter associations, stands a good chance of success in improving the countries' agro-product exports.

Fifth, even if assistance to trade development should substantially rise, there would remain deep-seated problems in both countries that may reduce its impact and undermine the long-term sustainability of donor interventions. As stated earlier, the problem in Africa is not insufficient conditions for export success, but the lack of catalytic agents that set this process in motion. As discussed in Box 1, a key factor in the success of several East Asian countries has been the continual upgrading of productive capabilities, which depends critically on the provision of an enabling business environment and the skill formation of managers and workers. To upgrade productive capabilities, these two countries need to place greater emphasis on the improvement of their business environment and the development of organisational and entrepreneurial skills.

Aid can help tackle these constraints and create synergies to attract investment to the agribusiness sector. Ultimately, however, the sustainable development of the sector will depend upon endogenous sources of growth, which cannot be replaced by foreign assistance. Addressing these problems is up to domestic governments and private sectors themselves. Governments can provide a business-friendly policy environment and build the administrative, legal and physical infrastructure, thereby promoting mutually beneficial partnerships between local firms and export-oriented foreign investors. In this context, Zambia's case study points to the importance of enhancing contract enforcement and loan repayments as a necessary condition for attracting investment and developing inter-firm linkages in the agribusiness sector.

Agro-based Private Sector Development: Lessons from Mali and Senegal²⁶

Agriculture (including livestock and fisheries) dominates rural employment and forms the backbone of the national economy in both Senegal and Mali. Case studies of these two countries show that both have strong agricultural and agribusiness potentials, with large irrigation possibilities along the Senegal and Niger Rivers. However, these potentials have yet to be fully exploited. Their agricultural production base is highly

concentrated on traditional export commodities (groundnuts in Senegal and cotton in Mali) faced with unfavourable global market conditions. While agricultural diversification is more advanced in Senegal than in Mali, both countries still need to make concrete efforts to diversify their agricultural sectors horizontally (by expanding the production base from traditional to non-traditional products) and vertically (by processing agricultural commodities along supply chains).

The experiences of Senegal and Mali highlight several lessons regarding agro-based private sector development²⁷. First of all, in the case of Senegal, a limited degree of co-ordination among different government bodies has resulted in a fragmentation of competences and bureaucratic delays and caused difficulties in designing and implementing credible policies and programmes capable of linking agriculture to private sector development and trade. It also appears that the government has not taken due account of the country's agricultural potentials and market constraints, as insufficient consultation with various stakeholders in the field has often led to policy decisions detached from local economic realities.

Senegal's horticultural sector, for example, has high growth potential. However, the government has, at least until recently, neglected its strategic importance, and the sector initially developed thanks only to the private sector's own efforts. A limited degree of co-ordination between the Ministries of Agriculture and Trade has delayed the preparation of an export promotion policy for this sector. Such a co-ordinated policy has been belatedly integrated into the 2006 national Accelerated Growth Strategy (AGS), and not all horticultural products receive due attention, particularly those grown in geographically remote regions. The implementation of the AGS depends largely on the government's capacity to deal with the market constraints facing local agricultural producers and agro-industries, on the one hand, and to create effective co-ordination among several ministries in charge of agriculture, trade, private sector development and infrastructure, on the other.

Compared with Senegal, Mali is less advanced in designing and implementing its own agricultural and trade promotion policies. The Malian government finalised an agricultural trade promotion strategy in 2005 under the aegis of the Integrated Framework for Trade-related Technical Assistance (IF), and set up an overall agricultural development strategy under the Agricultural Guidelines Law (LOA) in 2006. The implementation of these strategies will depend critically on the government's commitment to prioritise its areas of intervention and improve inter-ministerial and donor-to-government co-ordination²⁸.

Second, the rapid increase in horticultural exports in Senegal since the mid-1990s suggests that horizontal diversification is progressing. This positive development has taken place with continuing donor assistance. Examples of major donor assistance to agricultural diversification include the World Bank's Agricultural Export Promotion Project (AEPP) and Senegal Agricultural Markets Development Programme (PDMAS). Yet, there is large room for improvement in terms of export volumes, variety and competitiveness. Currently, only three products — green beans, mangoes and cherry tomatoes — represent the bulk of Senegal's horticultural exports to European markets. Moreover, with the exception of green beans, for which domestic production is closely linked to export production, exports take up only 2 to 3 per cent of domestic production. Several bottlenecks along the domestic agricultural value chain, from input procurement to production, storage, logistics and marketing, combine to reduce the international competitiveness of the sector.

On the other hand, vertical agricultural diversification has made only limited progress. Although Senegal has developed one of the most advanced food-processing sectors in West Africa, the industrial use of domestically produced agricultural products is rare, except for tomatoes and sugar cane. A few foreign-owned enterprises dominate the country's modern food-processing, which is highly dependent on imported inputs and equipment. Consequently, this sub-sector has generated few spillovers to domestic agriculture and other industrial sectors.

It is only recently that Mali has begun active promotion of horizontal and vertical agricultural diversification, despite the fact that the Niger River offers the country significant agricultural potential. The Malian economy is still highly dependent on three major export commodities, namely cotton, livestock and gold. As for the first two sectors, processing activities have yet to be developed. To improve agricultural competitiveness and foster diversification, the government, with the support of the World Bank, has recently launched an Agricultural Competitiveness and Diversification Programme (PCDA) and selected 23 agricultural products for diversification and upgrading. The PCDA also aims to encourage processing of cotton and livestock resources to develop textiles and hides and skins, as well as other products such as milk, eggs and meat.

Third, over the past several years both Senegal and (to a lesser extent) Mali have made significant progress in supporting the development of productive and marketing capacities in the agricultural sector. However, the small size of their domestic markets hampers the realisation of economies of scale. Nonetheless, there exist some promising cases of agricultural

clusters or agglomeration that would deserve further government support. They include, among others, small-scale producers' organisations located in the *Niayes Region* in Senegal and the *Office du Niger* in Mali. The government should focus more on policies to improve the functioning of domestic agricultural markets and link them to regional and international markets.

In both countries, the agricultural marketing system remains seriously underdeveloped. Producers are not well informed about market conditions, including commercial regulations in domestic, regional and international markets. Even in local markets, dissemination of important market information on price, quantity and quality of produce and the availability of agricultural inputs is still insufficient. Senegal's Market Regulation Agency (ARM) created in 2002 and Mali's Agricultural Market Watch (OMA), which replaced the Market Information System (SIM) in 1998, are expected to assist producers' efforts at marketing their produce. However, there is much room for improvement. Owing to a lack of adequate production planning based on market analysis, as well as storage, preservation and processing facilities, it has been pointed out that more than 30 per cent of total agricultural production is not commercialised and is perishing in the fields.

Fourth, many micro, small and medium-sized enterprises (MSMEs) are active in the agricultural sector, but only a few are engaged – directly or indirectly – in processing and agribusiness activities in the *formal* sector. Recently some positive changes have been witnessed. In Senegal, for instance, MSMEs have been engaged mostly in processing domestic agricultural products, such as local cereals, fruits, milk and vegetable oils, targeting local and informal markets. Other examples include some small enterprises that produce dairy products based on imported milk powder and sell them through local distribution chains (e.g. supermarkets and kiosks at gasoline stations). Such commercial activities have developed strongly and created new food-processing markets, driven by changing urban consumer demands. In Mali, following the government's partial privatisation of a state-owned cottonseed oil firm, *Huilerie Cotonnière du Mali (Huicoma)* in 2005, MSMEs have been progressively involved in cottonseed oil and animal feed production for domestic markets.

Fifth, the insufficient provision of financial services is one of the most significant obstacles to MSMEs. The financial offer available in the commercial banking sector often neglects the demand from MSMEs and farmers. Consequently, 80 per cent of Senegalese MSMEs with fewer than four employees have no access to credit. In Mali, access to financial

services seems to be mainly determined by the size of the company, its access to external auditing services and export orientation. Banks generally ask for high guarantees, while access to micro-credit remains limited. Moreover, a commercial financial sector is almost non-existent in Mali's rural areas. The limited capacity of most small entrepreneurs – especially in rural areas – to comply with the requests of the banking sector, often a reflection of their informal status and absence of book keeping and credit history, further reduces their access to credit.

Last but not least, infrastructure services remain costly and have limited reach, thereby preventing a healthy development of agricultural marketing and agro-processing sectors. Investment in transport infrastructure is on the rise, but the absence of clear strategic linkages with the development of agro-based supply chains may have only a limited impact on market deepening and intra-regional trade. This represents a significant constraint for Mali, given the country's land-locked situation. The cost of land transportation typically accounts for about 30 per cent of the value of Malian exports. Other barriers, such as illegal or legal transport tax charges, add to transportation costs and time. In addition, the development of logistic services (e.g. cold chain, storage, waste disposal) has only recently been integrated into government policies and donor projects.

Senegal has only recently embarked on building trade-related infrastructure to promote agricultural exports. The country faces a number of problems in this undertaking. For instance, a lack of reliable transport infrastructure presents a major obstacle to realising existing horticultural potentials, especially in Casamance. Serious traffic congestion around the Dakar port area makes it hard to manage agricultural and agribusiness supply chains. Furthermore, a combination of poor rural transport infrastructure, limited access to electricity and insufficient equipment, including lorries and cooling facilities, prevents local producers fully exploiting the existing potential. It is thus imperative to design a comprehensive national infrastructure development plan in support of agricultural production, processing and marketing. To make it happen, this would require greater co-ordination among relevant ministries and between ministries and donors with close private-sector consultation.

Implications for the International Aid-for-Trade Initiative

The country experiences reviewed in the previous section suggest some specific recommendations on how to improve the effectiveness and sustainability of aid-for-trade activities:

- Export success in Africa depends principally on African governments' ability to help domestic suppliers respond more readily to the opportunities arising from further trade liberalisation.
- The need for a greater focus on "behind the border" measures, such as standards, sanitary and phyto-sanitary (SPS) regulations and other technical barriers to trade, continues to present a major challenge for African countries.
- Aid for Trade involves complex partnerships among recipient governments, bilateral donors, multilateral and regional agencies, the private sector and other non-governmental organisations. Each of these stakeholders has different priorities, operating arrangements, time frames and financial and human resources. Ensuring frequent information exchange and dialogue among them at the country level is an important step towards a successful operation of Aid for Trade.
- Complicated reporting requirements and other administrative procedures overload the capacity of poor countries. All efforts at streamlining procedures and providing additional and sustainable resources are to be encouraged.
- From the donor's perspective, a delicate balance must be struck between the donor country's own trade policy agenda and the developing country's trade needs. Agriculture is an example of these trade-offs: many OECD countries provide generous support to domestic farmers even as they attempt to build the export capacity of agricultural and agribusiness producers in Africa and elsewhere in the developing world. Furthermore, Aid for Trade is not limited to trade in goods alone. The service sector has also become increasingly important for trade development in African countries.
- Greater attention should also be paid to the sustainability of aid-for-trade interventions. Apart from the viability of specific projects and programmes, which should be carefully assessed, sustainability depends critically on the ability of local actors to take over the project, once donor assistance is phased out. Field interviews conducted in Tanzania and Zambia suggest that this has not always been the case.
- From the aid recipients' perspective, it is fundamental to involve farmers, agribusiness companies and business organisations, together with relevant government agencies. The Agriculture

Consultative Forum in Zambia is a good example of how key stakeholders can interact to inform the design of the overall agricultural strategy and the formulation of specific projects and programmes of more immediate need (e.g. how to respond to food shortages or exchange-rate fluctuations). Adequate funding should be devoted to reinforcing the analytical capacities of these associations and forums, so that they can take a lead in the identification of needs and ways to respond.

- In terms of programme content, more emphasis should be devoted to addressing gaps in farmers' capacity to improve productivity and linking them up to processors and buyers. Governments, in consultation with donors, should seek to develop comprehensive support packages to cover the whole value chain or a set of co-ordinated interventions that do so in a more comprehensive way. Such an approach is echoed in Zambia's Diagnostic Trade Integration Study (DTIS) and has recently been adopted in some donor-supported projects.

Beyond these specific recommendations, two general comments can be made. First, what is critical for both credibility and accountability of donors is to fulfil the pledges made at the 2005 Gleneagles Summit to double aid to Africa by 2010. Leaders of G8 nations agreed on new aid packages to support the continent's progress, by increasing donor assistance for trade and private sector development under the broader economic growth agenda. A key idea of this is "to stimulate growth, improve the investment climate and to make trade work for Africa, including by helping build Africa's capacity to trade and working to mobilise the extra investment in infrastructure which is needed for business"²⁹.

However, DAC members' net ODA flows in 2006 totalled \$103.9 billion, down 5.1 per cent from 2005, in constant 2005 dollars. ODA is expected to decline slightly again in 2007 as debt relief for Iraq and Nigeria tapers off. This leaves the challenge of meeting the 2005 G8 commitments to scale up aid over the remaining three years (2008-10).

A second key challenge for 2008 is to set up cost-effective monitoring schemes for Aid for Trade at the global, regional and country levels. In this regard, ongoing international monitoring and evaluation efforts, led by the WTO and the OECD, will require further political and financial support (see Box 3). Such efforts will need to address some emerging issues, such as a revision of the CRS (Creditor Reporting System) Purpose Codes to meet the recommendations of the WTO Task Force (e.g. trade-related adjustment and other trade needs), and an extension of the OECD/CRS

database to include important emerging non-DAC donors (e.g. China, India and Thailand) as well as private foundations, where appropriate³⁰.

Box 3. Aid for Trade: What Counts? How Much?

A major OECD-WTO report analyses information in the OECD Creditor Reporting database on Aid-for-Trade initiatives to determine the level and trends in aid for trade programmes by DAC donors in recent years (OECD/WTO 2007). The report furthermore projects different scenarios for future aid-for-trade spending.

The first question that must be answered by such an evaluation is what aid qualifies as "aid-for-trade"? The OECD considered three alternative criteria, each more encompassing than the last, to answer this question:

- **Category I: Trade policy and regulations.** This category includes development assistance intended to help countries negotiate, reform and prepare for closer integration in the multilateral trading system; e.g. analysis and implementation of multilateral trade agreements, trade policy mainstreaming and technical standards, trade facilitation including tariff structures and customs regimes, support to regional trade arrangements and human resources development in trade.
- **Category II: Trade-related infrastructure.** A more inclusive definition of aid for trade would include all aid in Category I, but also assistance to trade-related infrastructure, including transport and storage, communications and energy.
- **Category III: Building productive capacity.** A still broader definition would add to Categories I and II all development assistance that seeks to enhance competitiveness, for example by providing aid for the development of banking and financial services, for upgrading skills in the primary sector, in manufacturing and in services. This category also includes aid-for-trade development: namely, aid intended to help enterprises engage in trade and to improve the business climate; to provide access to trade finance and to promote trade in the productive sectors (agriculture, forestry, fishing, industry, mining, tourism and services).

As the definition of aid for trade grows more inclusive, the greater is the risk of conflating aid for growth and development generally with aid for trade.

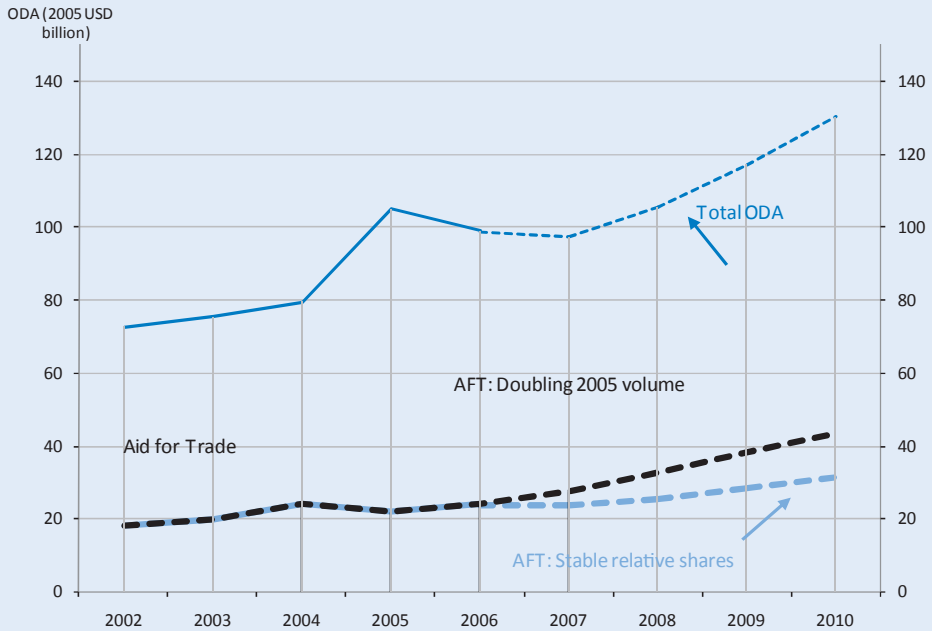
The OECD/WTO study reported that in 2005, assistance committed to the broader aid-for-trade agenda included \$654 million for trade policy and regulations, \$12.2 billion to build trade-related infrastructure and \$8.9 billion to promote productive capacities, for a total of nearly \$22 billion — over 32 per cent of total sector allocable ODA.

Box 3 (contd.)

Trends in aid-for-trade spending (all three categories combined) by DAC donors for 2002-05 are summarised and placed in the context of overall ODA in Box Figure 1. The Figure furthermore presents projections for aid and aid-for-trade spending for 2006-10. The forecasts take as given the commitments to overall scaling up of aid made by DAC donors, and within that setting, present two scenarios. In the first, aid for trade (all three categories) maintains its recent annual growth rate of 6.8 per cent; in this scenario, aid for trade would reach approximately \$31.3 billion (at 2005 constant prices) by 2010. In the second scenario, doubling the 2005 volume of aid for trade by 2010 would result in \$43.4 billion.

Source: OECD (2006b); OECD-WTO (2007).

Box Figure 1. **DAC Members' net ODA 2002-05 and DAC Secretariat simulations of net ODA, 2006-10**



Annex Table 1. **Export Diversification: Africa**

	Diversification Index*		Annual Export Growth (%)
	2001	2005	2001-2005
Morocco	35.3	34.7	12.4
Tunisia	28.5	30.6	11.7
South Africa	33.2	23.1	11.2
Egypt	26.3	22.6	24.7
Swaziland	8.8	18.9	28.4
Tanzania	19.0	18.7	21.1
Eritrea	14.4	15.4	11.0
Kenya	11.3	15.2	9.7
Djibouti	49.0	14.8	-19.5
Zimbabwe	9.8	13.9	0.1
Madagascar	9.2	12.2	0.1
Mauritius	12.6	9.9	1.4
Togo	9.3	7.6	1.7
Uganda	6.2	5.8	13.0
Senegal	12.8	5.7	1.4
Lesotho	5.2	5.6	25.5
Somalia	11.6	5.6	3.1
Côte d'Ivoire	6.8	5.6	8.6
Namibia	7.1	5.2	56.5
Gambia	5.8	4.6	0.1
Ghana	8.2	4.3	9.9
Congo Democratic Republic	2.4	4.1	3.5
Africa (Average)	8.1	4.1	21.4
Ethiopia	5.3	3.6	27.7
Cameroon	4.5	3.6	10.7
Central African Republic	2.4	3.5	-7.7
Seychelles	2.6	3.5	17.4
Guinea	3.4	3.3	6.7
Rwanda	2.6	3.1	4.9
Zambia	4.2	3.1	32.7
Sao Tome and Principe	7.0	3.0	-3.7
Mauritania	3.8	2.9	13.8
Benin	1.8	2.9	-5.2
Malawi	2.9	2.8	5.7

Annex Table 1 (contd.)

	Diversification Index*		Annual Export Growth (%)
	2001	2005	2001-2005
Comoros	1.3	2.6	-8.7
Cape Verde	8.6	2.6	8.1
Sierra Leone	6.8	2.5	35.2
Algeria	5.3	2.1	27.6
Mozambique	2.9	1.8	28.9
Liberia	2.1	1.8	2.6
Gabon	1.7	1.7	13.9
Niger	4.6	1.6	-4.7
Mali	3.2	1.5	1.7
Burkina Faso	4.4	1.4	9.0
Burundi	1.9	1.3	35.2
Botswana	7.5	1.3	369.7
Congo	1.5	1.3	35.7
Sudan	1.7	1.3	45.1
Nigeria	1.3	1.2	27.3
Equatorial Guinea	1.3	1.2	61.4
Guinea Bissau	1.6	1.1	6.0
Chad	1.5	1.1	477.6
Libya	1.4	1.1	29.8
Angola	1.3	1.1	51.0

* The diversification index is defined as the inverse of a Herfindahl index, using disaggregated exports at 4 digit level (SITC 3). A higher index indicates more export diversification. Countries in bold experienced more diversification between 2001 and 2005.

Source: AfDB/OECD African Economic Outlook Statistical Database.

Notes

1. This includes both cotton-specific and non-cotton specific programmes and projects. The latter involve those linked to the cotton sector either through assistance provided to the agricultural sector (e.g. promoting diversification) or through related infrastructure development (e.g. construction of feeder roads, railways and support for the gamut of agricultural activity). See the WTO website; [www.wto.org/\(WT//L/670\)](http://www.wto.org/(WT//L/670)), 15 December 2006).
2. See Behrendt (2007) for a succinct discussion of Mali's cotton sector reform.
3. See OECD (2006c) for detailed discussions on the cotton sector in West Africa. See also ADB-OECD (2007).
4. See Bonaglia and Fukasaku (2002 and 2003) for further discussion.
5. See Goldstein *et al.* (2006).
6. In this regard, the outcome of the WTO negotiations at the Hong Kong, China Ministerial Conference in December 2005 took an important step forward in the right direction but fell short of the specific request of LDCs under the Doha Development Agenda (DDA). While the LDC Group asked for 100 per cent access, the Hong Kong, China Ministerial Declaration mandate was to provide them with duty-free, quota-free market access for 97 per cent of tariff lines. The devil is often in the details, however. The remaining 3 per cent would amount to some 330 tariff lines, which could be large enough for LDCs to be denied *meaningful* market access.
7. The European Commission since early March 2001 has granted duty- and quota-free access to LDC exports under the so-called "Everything But Arms (EBA)" Regulation, though three most sensitive products (fresh bananas, rice and sugar) are not immediately liberalised. While duty-free access came into effect for bananas in January 2006, duties on rice and sugar will be gradually reduced until duty-free access is granted for sugar in July 2009 and for rice in September 2009. In the meantime, duty-free tariff quotas are put in place for rice and sugar.
8. The AGOA was introduced in 2000 to offer African countries preferential access to the US market. It has been revised three times: in 2002 (AGOA II), 2004 (AGOA III) and 2006 (AGOA IV). AGOA IV, which became effective on 20 December 2006, extends the third country fabric provision (with amendments) for five years, from September 2007 till September 2012. Currently 38 African countries are eligible for trade preferences under AGOA (http://www.agoa.gov/agoa_legislation/agoa_legislation4.html).
9. The seven case studies (six African countries and Viet Nam) can be downloaded from: <http://www.oecd.org/dac/trade/doha2006/>
10. The theoretical and empirical research literature in economics on the interrelationship between aid and trade flows and policies is summarised in Suwa-Eisenmann and Verdier (2006).
11. The theoretical and empirical economic research on the interrelations among FDI, trade and aid flows is synthesised by Mayer (2006).
12. See Goldstein *et al.* (2006) for further discussion of the economic ascendancy of China and India and its implications for Africa.

13. See Mayer and Fajarnes (2005) for an insightful discussion of Africa's prospect for exports of primary commodities, given rapid industrialisation and income growth in natural-resource-poor, large Asian developing countries, notably China.
14. A good example of such large-scale enterprise is Homegrown, Kenya's largest horticultural exporter. Homegrown is a highly vertically integrated company: 90 per cent of its crops are grown on its own farms, it controls storage, cooling and logistics from field to packaging stations, and has a joint venture with an airfreight company and a dedicated importer based in the United Kingdom (FAO, 2004).
15. See Jaffee *et al.* (2003). "Agribusiness" encompasses a wide spectrum of on-farm and off-farm activities from production, post-harvest handling, processing, distribution, marketing and other agro-based commercial activities. See also OECD Development Centre (2007, Chapter 3) for a concise review of Africa's agriculture.
16. See NEPAD (2002), World Bank (2007) and OECD (2008).
17. These two versions of the old thinking could be labelled "trade, not aid" and "aid, not trade", respectively. Tovias (2006) argues that European Union aid and trade policies toward its Arab Mediterranean neighbour countries have swung between these two poles.
18. The material on Uganda is a summary of Stavlöt *et al.* (2006), to which the interested reader is referred for fuller details and bibliographic references.
19. The material on Mozambique is a summary of Haaparanta and Kerkelä (2006), to which the interested reader is referred for fuller details and bibliographic references.
20. The SADC member states are Angola, Botswana, the Democratic Republic of Congo, Lesotho, Madagascar, Malawi, Mauritius, Mozambique, Namibia, South Africa, Swaziland, Tanzania, Zambia and Zimbabwe.
21. This analysis is based on data developed by Purdue University's Global Trade Analysis Project (GTAP); the details are provided in Haaparanta and Kerkelä (2006).
22. The case of sugar is a special one in Mozambique. The country enjoys substantial benefits from its access to EU markets at a very favourable price. Reform of the sector, if it reduced prices paid, would hurt Mozambique. But simulation analysis suggests that Mozambican sugar producers are competitive relative to other producers with access to EU markets; Mozambique might well capture market share in the case of sugar sector reform and come out a winner.
23. See Temu (2006) and Chiwele (2006).
24. A major reversal in the exchange-rate market took place when the local currency *appreciated* by about 30 per cent against the dollar between January and December 2005. This has sent shock waves through the agricultural export sector. Cotton ginneries have threatened to close (they had signed contracts with growers at the beginning of the season on the basis of much weaker kwacha rates), and many exporters lament that the reduction in import prices that should counter-balance the stronger kwacha will not be so beneficial for them, since they mainly employ locally sourced inputs, notably labour. The country's foreign exchange market also experienced some volatility during 2006, because of the uncertainty surrounding the elections. Despite periods of depreciation, the kwacha appreciated by almost 20 per cent in 2006 (see African Development Bank/OECD, 2007).
25. These data do *not* include assistance to agricultural development projects and programmes that are not directly trade-related. The country case studies provide a stocktaking of the most important projects implemented in the agricultural sector aiming at strengthening productive capacity, irrespective of their trade-relatedness (see Temu, 2006; and Chiwele; 2006).
26. See Hazard, Barry and Anouan (2006) and Hazard, Barry and Tall (2006).
27. See Matsumoto-Izadifar (2007) for a concise review of the recent experience of these two countries.

28. Although the LOA asks for detailed policies and clearly defines the respective roles and responsibilities of different stakeholders at the sub-sectoral level, the fundamental issue of land property and titling has not been addressed under this law.
29. The quotation is taken from the Chair's summary, available at <http://www.g8.gov.uk>.
30. See Andersson *et al.* (2007) for further discussion.

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