Export Development Strategy, Export Success Stories and Lessons for Africa: The Challenge for Afreximbank

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1. Introduction

It is relevant to ask whether there are special features of Africa that would help explain the massive poverty and inequality that engulfed the continent. Weak initial conditions (such as weak institutions, human capital and extractive colonial history and its attendant institution) at the time of independence; the dependence of almost all African countries on primary commodity production and trade; lack of non-aid financial capital flows and the alarming level of aid-dependency; lack of ownership of policies which are invariably imposed on Africa by donors; prevalence of conflict and poor governance are some of the issues where possible explanations for this sever lack of progress and pervasive poverty might be found. Many countries, especially those in East Asia, extracted themselves from such massive poverty, among other things, by designing and implementing an appropriate industrial and export strategy. In this study an attempt to draw lesson from such economies about their successful export strategy so as to help tackle the challenge of export development in Africa is made. Given such general focus of the study an emphasis is placed on the role the African import and export bank (Afreximbank) could play in addressing the export challenges of Africa is also made.

The rest of the paper is organized as follows. Section two begins by briefly noting the export development strategy pursued in most African countries and the current thinking about export-led growth. This is followed by an examination of successes stories in exporting in Asia and within Africa itself and the lesson that might be drawn from those experiences. This is followed by section three where the export challenges of Africa and the plans, programs and facilities of the Afreximbank is discussed at length. Section four concludes the paper by offering policy directions for Afreximbank both at macro and corporate level..

2. Export Development Strategy, Export Success Stories and Lesson for Africa.

Following political independence, most African countries pursued import substitution strategy (IS). That strategy was not largely successful. In fact the IS strategy has led to a rising demand for foreign exchange and public expenditure (see Alemayehu 2002). As can be inferred from the experience of the newly developed Asian countries discussed below, the IS strategy in itself is not a problem. Perhaps one of the major domestic policy problem associated with the rising public expenditure in Africa was the way in which the import substitution (IS) strategy was conducted. While in principle the IS strategy is a sound one, in Africa, it was carried out in the context of a disarticulated production and consumption structure. By the latter I mean the neglect of industrial and agricultural linkages (as it was based on the urban elite's patterns of consumption); failure to plan the financing of future demands for recurrent cost of intermediate inputs; failure to develop the human capital

[1] I am grateful to one of my student and friend, Dawit Berhanu, for excellent research assistance in the course of writing this paper. Any errors are mine.

required to sustain the IS strategy and failure to transit to export-led growth strategy. These failures seem to be realized now, however.

Rodrik's (1997) examined the failure of many Sub-Saharan African countries to sustain periods of growth and trade expansion. He noted that there are far less disputes on what constitutes, now, realistic trade strategies for countries of Africa. It is claimed that the de-monopolization of trade, streamlining of import regimes, reduction of red tape, implementation of transparent customs procedures, replacement of quantitative restrictions with tariffs, avoid extreme variations in tariff rates and excessively high rate of effective protection, allow exporters duty-free access to imported inputs, refrain from large doses of anti-export bias and refraining from excessive taxing of exports are all essential trade strategies for countries of Africa. He noted that many countries have been reluctant to adopt free trade regimes for fear that trade reforms may not work in Sub-Saharan Africa. Rodrick (1997) underscored that Sub-Saharan Africa needs to be cleansed from the "groundless pessimism" that has contributed to its disillusionment with traditional trade liberalization policies. He emphasized the need to realize that trade policy in Africa works the same that it does elsewhere. However, Rodrik (1997) noted that the role of trade policy in economic development is largely auxiliary [that of providing an enabling economic environment] and should not be considered an end in itself. In fact, Rodrick (1997) regards excessive focus on outward orientation and openness as counterproductive and a distraction from the fundamentals of long-term growth [notably the development of human resources & physical infrastructure, and the need to ensure macroeconomic stability and the rule of law][2].

World Bank also (2000) emphasized the need for most African governments to support, at least in principle, the export orientation of their manufacturing industries with aim of positioning themselves on a dynamic growth trajectory. According to Mengistae and Pattillo (2004), that claim is essentially based on the idea that one can derive significant productivity gains out of exporting. The study by Mengistae and Pattillo (2004) found that export manufacturers in Sub-Saharan Africa have efficiency or total factor productivity, *TFP)* gains over non-exporters. However, the study couldn't establish whether these gains are due to a process of learning by doing or because more efficient producers go into exporting.

Mengistae and Pattillo's (2004) study analyzes manufacturing data from Ethiopia, Ghana and Kenya that are believed to represent the diversity of the region's manufacturing sectors and their orientation towards exporting[3]. Their empirical analysis revealed that efficiency (TFP) of exporting manufacturers is 17 percent higher than for non-exporting firms across the three countries. The authors show that the average premium for direct exporters is close to 22 percent, a figure, the authors' claim, that underestimates the premium for those that export to destinations outside Africa. They found the productivity premium for direct exporters outside Africa that reaches a staggering 42 percent (see Mengistae and Pattillo, 2004: *330-334).* The study, does not claim to determine the causality between productivity and exporting but, the authors' argue, their finding is sufficient enough to warrant a support for open trade and an external trade regime that supports export orientation. Thus, there is a

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[2] Beside the cross-country regressions that the study employed, a summary of country experiences are provided to get some insights into specific reforms that have distinguished some countries as success stories. Two of such cases are Botswana and Mauritius (see below). Rodrick (1997) ascribes Botswana's success to prudent fiscal and macroeconomic policies, well-developed human resources and an early demographic transition that reduced the dependency ratio, apart from the gains from diamond exports. Rodrik (1997) notes that the first factor has contributed the most as it accounts for more than half of Botswana's good performance paired-against the Sub-Saharan average. Similarly, Mauritius's success largely depended on an export-boom in garments to European markets and an associated investment boom at home at its successful export processing zone (EPZ).

[3] Kenya represents one of the strongest export-oriented manufacturing sectors in Africa, with 25 percent of the manufacturing sector actively engaging in export, while Ethiopia represents countries of the region that are actively engaged in import substitution [only 3.7 percent of the establishments engaged in exports]. Ghana represents countries in between the two extremes.

supporting empirical evidence for export-oriented development strategy in Africa at least from productivity perspective.

The importance of openness in general and export-led growth in particular to attain accelerated growth could also be learned from the experience of countries, especially those in East Asia, that were successful in exporting and attaining high rate of growth. There are controversies over the issue of what contributed most to the success of the East Asian economies in exporting and attaining fast growth. According to the survey by Lawrence and Weinstein (2001), Krueger (1993), Hughes (1992) and Balassa (1971) argue that the principal contributor to the East Asian rapid growth was the openness to trade and governments' willingness to limit protection and ensure that "incentives were largely neutral". Contrastingly, among others, Amsden (1989) and Wade (1988) show that the emphasis given to interventionist policies in these economies has changed comparative advantage by "getting prices wrong", while duly acknowledging that the trade performance of the economies was vital. Still another group, represented by Roderik (1995), argues that industrial policies played [the] most important role by creating a particularly favorable environment for domestic investment.

The World Bank (1993) takes an intermediate position in the debate. Although it recognizes that performance in the manufactured goods industry played an indispensable role in stimulating growth, it challenges the view that selective intervention [such as selective industrial policies] was essential in promoting the export competitiveness of industrial policies. As Lawrence and Weinstein (2001) noted, although the World Bank (1993) acknowledges the role of exports as a channel for learning and technological advancement, it fails to recognize similar benefits that accrue from import and import competition. Their study finds that the role of imports was far more superior to the role of exports in determining greater productivity growth.

In sum, notwithstanding the debate about the IS and EP strategy, there is no question about the importance of exports-led growth strategy for African countries today. However, policy makers need to see the IS and EP strategies as complementary, not competitive. Moreover, there is the need to see export growth strategy in the context of broader growth and industrialization strategy. Details about such strategy from experience of countries with a success story could help policy making about export growth strategy in Africa. Thus it is worth examining the experience of such success stories from Asia (section 2.1) and Africa (section 2.2) to draw lessons for trade policy making in Africa (sections 2.3).

2.1 The Lesson from Asia's Success Stories: With A Focus on Taiwan and South Korea

The growth success of Northeast Asian countries (Taiwan, Korea and Hong Kong in particular), and latter Southeast Asia (Malaysia and Indonesia in particular) is unprecedented in the history of industrialization in general and export performance in particular. Industrial products now make 90 percent of total exports in most of these economies. Yet as late as 1955 exports were 85 percent agricultural or processed agricultural exports mostly on rice and sugar. Taiwan is now the 10th and Korea the 13th biggest manufacture exporters in the world. Today, Taiwan and Korea together with Hong-Kong and Singapore are moving speedily into high-wage and high-technology sectors producing about half of the developing countries manufacture exports. Each country's export of manufactured goods is larger than the whole of Latin America's manufactures exports. Taiwan and Korea achieved industrialization in 15 years what took Japan 25 years and Great Britain over 50 years. Moreover, their fast growth is accompanied by unusual equal distribution of income, which was not the case during the industrialization period of today's developed countries. (Wade 2004). In short, in one generation they moved from Agrarian to industrial economy. What is the story behind this success and is there any lesson for Africa? In this section we will focus on the export, as opposed to growth, success story. This issue is discussed by taking the case of Taiwan and Korea. I have

described the major features of this success story by setting them across four thematic areas: (i) initial conditions, (b) trade and industrial policy making, (iii) the political economy of trade policy making and the role of the state and (iii) the dynamics of exporting industries and the role of foreign firms.

Initial Conditions

According to Amsden (2001) Japan's mobilization for war and invasion of Manchuria in 1930 provided a lightning rod for the industrialization of its neighbors. Japan hastily adopted industrial policy to promote manufacturing for war preparation in its colonies, Korea and Taiwan, thereby planting the seeds for their highly successful post war industrial system. Colonial governments in Indonesia and Malaysia responded to Japan's threat with defensive investment, including protection against Japan's exports (Amsden, 2001: 100). This is the foundation for industrialization and exporting success witnessed in the last 2 to 3 decades in these newly developed countries.

Amsden (2001) also noted that the current industrial structure and export success in Korea owes its origin to the industrialization advanced in World War I (WWI) and accelerated with the Manchuria incident in 1931. Following WWI and the associated cut of supplies from Europe, Japanese industries failed to satisfy the demand in colonies. This led to the relaxation of the policy that restricted the creation of industries in Korea that compete with that of Japanese. Following this policy relaxation the following pattern is observed. First, Japanese business groups became major actors on Korean industrialization; second, Japanese investment were much large scale than that of Korean, and the large Korean-owned corporations made an early appearance; third, small industries concentrated in food processing while larger industries covered multiple industries, including iron and steel; forth, most of the capital for expansion came from Japan; finally, most Koreans were working in Japanese firms at different capacity and the colonial government invested on their education while Japanese firms invested on their training. Thus, Korea had accumulated considerable manufacturing experience (workforce, managerial elite, government bureaucracy, cadre of entrepreneurs with project execution skill, and production know-how) by 1960s (Amsden, 2001: 100-105). Like that of Korea, Taiwan's industrialization and export success owes its origin to extensive manufacturing experience before 1960s. Taiwan benefited not only from Japanese mentoring but also from an influx of large number of experienced workers, managers and entrepreneurs from mainland China in 1950s. Like that of Korea, the Japanese led industrialization in Taiwan in 1930s was aimed at helping Tokyo's expansionism. (Amsden, 2001: 105).

An interesting parallel, thus, could be made between the initial condition in Asia and African colonies at the time of political independence. It is tempting to conclude that East Asian countries (such as Korea, Singapore and Hong Kong) that were under colonial rule are well developed today while Africa is not, and there is therefore something wrong with Africa. Such comparisons are not in order because the historical parallel is fundamentally different (see also Acemoglu *et al* 2001)[4]. Hong Kong and Singapore prospered as enterpots owing to direct British colonial interest. Moreover, they are city-states incomparable to African colonies. Probably the only comparable country is Korea and to some degree Taiwan. However, the Japanese colonialism (which was as harsh as the British and France in Africa) had the aim of creating heavy industry and self-sufficiency in its empire, and, hence, has done better than the colonizers in Africa. Some figures may substantiate this point. Taiwan and Korea experienced higher GDP growth than their colonizer (Japan) between 1911-1939; their infrastructure has also developed -Taiwan having 600 kilometers of rails and 3,553 kilometers of road where there were none before. By the end of the colonial period primary school enrolment in Taiwan stood at 71 percent and similar pattern is observed in Korea (which was virtually none in Africa). Owing to geopolitical factors (the cold war) Korea, for instance, obtained US $6 billion grants from USA between 1946-78, compared to US $6.89 billion for the whole of, close to 53, African countries.

[4] Acemoglu *et. Al* (2001) argue that unsuitability of African countries for European settlement have adversely affected the development of institutions and gave rise to growth of extractive, as opposed to developmental, institutions. These are inherited as they are by the post-independent leaders.

US military delivery to the two countries in 1955-78 stood at US $9 billion, the combined figure for Latin America being US $3.2 billion- with all its positive economic impact (see Chowdhury and Islam 1993). In Korea alone aid financed nearly 70 percent of total imports and equaled 75 percent of total fixed capital formation (See Haggard 1990 which also provides the political economy of this event). These points show that this experience is incomparable to the situation in Africa where its initial condition was unfavorable (see Alemayehu 2002). It is in the context of such variation in initial conditions the export-led strategy and its success in Asia and Africa need to be understood.

Trade & Industrial Policy Making

Taiwan's policy makers had a blue print in 1960s that partly explains the export success story in that country. During that time, Taiwan used to import twice the value of its exports which was largely financed by the USAID. This was perceived as alarming aid-dependency by Taiwanese policy makers. One of the strategies to get out of this dependency was the development of exports (Hsueh *et al* 2001). This gave the impetus for the export promotion policy that included (a) devaluation of the Taiwan's currency (the NT dollar), (b) import tax rebates, (c) low-interest export loans, (d) export processing zones, and (e) the statue for encouraging investment. Similar export promotion policies were also pursed in North Korea (see Hsueh *et al* 2001, Collins 1990).

Taiwan's export promotion policy has the desired result. In 1952 Sugar, rice, bananas, and tea accounted for 85 percent of all exports. By 1961 these products still made up 43 percent of exports, but by 1971 they accounted for 6.1 percent only. Textile exports rose form 15.1 percent of all exports in 1961 to 35.4 in 1971. Export of consumer electronics, canned food and plywood were also in a rise. (Hsueh *et al* 2001). By the early 1970s the export promotion policies remained in place and some were extended but the government focused on strengthening heavy industry. This was motivated by both economic (getting a secured intermediate goods) and political (secured supply of inputs was a political, security, issue for Taiwan) factors. Both Taiwan and Korea targeted particular industries for development. But South Korea turned to private firms while Taiwan to state-owned enterprises for this purpose (Hsueh *et al* 2001).

According to Collins (19990) Korea conjured up a combination of macroeconomic stabilization[5], and trade and financial market liberalization policies that propelled the economy onto a path where real growth was impressive. The study makes note of the fact that Korea didn't implement macroeconomic stabilization and restructuring measures at the same time that it freed itself from reliance on foreign borrowing. However, it had the benefit of a continued inflow of capital in the first year of its recovery which helped in reviving growth before the restrictive monetary and fiscal policies took effect.

According to Park (1990), even though Korea and Taiwan share a number of common traits in that both have adopted export-led industrialization and that the governments of both countries have actively participated in a fashion that transcends the traditional role of correcting market failures, the involvement of the governments took different shapes. Whilst the Taiwanese were inclined to be supportive rather than interventionist, Korean governments, on the other hand have been collaborative and at times coercive in their relations with the private sector. The governments of the two economies have struggled to keep pace with the changing circumstances once the export-led

[5] According to Akuyz et al (1998), the characterization of the economies of Northeast Asia as followers of stable macroeconomic policies or low inflationary policies is essentially misleading. There is evidence that the economies were willing to allow some level of inflation in order to boost investors' confidence. When there were pressing needs for restrictive policies measures that sacrifice consumption rather than investment were put into effect. Most importantly, measures were taken to boost the profits of firms above their free market levels. Some of these measures were intended to supplement corporate profits and to guarantee their retention and hence stimulate capital accumulation, an across the board tax exemption and special depreciation allowances [in some cases to specific industries]; trade, financial and competition policies were also used to create economic rents that boosted corporate profits and created additional investable resources (see Akuyz et al,1998).

industrialization regimes have been put in place and thus have experienced brief episodes of inefficiencies. While the Taiwanese government has confined its role to providing social and physical infrastructure and other public goods and its interactions have been characterized by mutual adjustment on the part of the private and public sector, the Korean government provided sort of an institutional cocoon that provided domestic market protection and an implementation of industrial targeting (Park, 1990).

Summarizing the experience of Asian countries, Krueger(1990) contends that even though the export performance of the East Asian exporters and particularly Korea, Hong-Kong, Singapore and Taiwan, was a tremendous achievement, the balance it initially had with their per-capita GNP growth was less than impressive. The author notes that the countries had earlier experiences with inner oriented trade policies and quantitative controls over imports, but in each case the change in trade strategy was followed by a sizeable increase in the rate of growth of output and the marginal productivity of capital as measured by the incremental output-capital ratio. Krueger (1990) argues that the reasons for the congruent performances of national output and export performance lie in the fact that the government was strongly committed to a policy of growth through exporting and to that end it altered the real exchange rate received by exporters, the import regime as it affected re-exporters, and infrastructure were all geared towards export drive and towards guaranteeing the profitability of successful exporting firms. Kruger (1990) also noted that the profits that were made through import restriction were channeled towards exporters, in the early years of the export-strategy. Governments made no attempt to restrict the choice of which products to export and therefore as a rule made efforts to encourage exporters of any sort. This is mainly derived by the fact that the countries had small export base (see Krueger, 1990).

As Krueger (1990) noted, although the afro mentioned factors were important unifying threads there were also noteworthy differences in the country experiences, notably the differences in firm size among Korea, and Singapore, Taiwan and Hong-Kong, on the one hand, and the treatment of foreign investors on the other. The author provides four plausible explanations that contributed to the export-GDP growth of these economies. The first explanation is a typical trade theory story that the economies made a transition from a highly protective trade regime to an export-oriented strategy and in the process realized their comparative advantages. Second, the measures towards export orientation resulted in an increase in the capital-output ratio and guaranteed faster growth even at a constant savings rate. Third, outward-orientation resulted in the realization of economies of scale and the exhaustion of indivisibilities. The fourth explanation is related to the avoidance of the stop-go policies associated with balance of payments difficulties. The study further indicated that it is difficult to disentangle the contribution of trade and export policies to growth because other policies adopted by the super-exporters were also conducive to growth. The study also supports the fact that the same policies have different costs at different stages of development of economies. At low levels of income most economic activity takes place in agriculture and the costs of control over trade, industry and the factor market are fairly small. Until mechanisms are found that permit the satisfactory growth of agricultural output and productivity there can be very little economic growth. This implies a prerequisite for satisfactory growth lies in the provision of infrastructure and incentives for agriculture. But once those are in place a given set of restrictions over trade will exact an even more slowly growing set of industrial activities. Therefore a successful export-oriented strategy would put in place a set of frameworks that result in the adoption of other efficiency and growth-enhancing liberalization policies and in turn these policies permit further gains to be realized from the trade strategy and induce further growth and efficiency (Kruger 1990).

The Political-economy of Trade Policy Making and the Role of the State

There were also a political-economy dimension to the success story of both Taiwan and Korea. The private firms in Korea (the *Chaebols)* were led by Koreans who had close tie to the government and over time came to be major supporters and financers of the governing party and its president. This

was not the case in Taiwan, however. Rather the government (which was mainly mainlander Chinese) expanded its economic power through the formation and expansion of state enterprises (Hsueh *et al* 2001).

In both Taiwan and Korea, the role of the state in the industrial economy and promotion of exports was very large, and this included protecting the domestic market. One factor which is apparent in Taiwan in particular is the fact that the leading sectors after the 1960s were all major exporters and most of them were privately owned. Government policy played a critical role in the boom in export manufactures (Hsueh *et al* 2001). In the 1980s the emphasis in industrial policy shifted away from heavy to technology intensive industries and the issue becomes how to upgrade Taiwan's industry so that they remain internationally competitive. Scientific research was also geared from basic academic research towards applied scientific research that included the establishment of Taiwan's Science-based Industrial Park, reversal of brain drains by introducing appropriate incentive schemes, and a science and technology research plan, including the required budget that the government demanded to be drawn by each relevant ministry. This process was basically similar in Korea too (Hsueh *et al* 2001).

According to Park (1990) the institutional cocoon built during the import substitution era of Korea nurtured the industrialist class a little too much, as it was unable to develop knowledge of foreign markets and hence was unprepared to take higher risks in selling to the international market. It also complicated the intended leap onto an export-oriented economy in the 60s. The government of Korea was thus forced to support a selected few large producers in the targeted industries since the efficiency that is required in export-orientation meant taking on increasing returns technologies that conflicted with the poor resource base that the country had. In the absence of such an elaborate market mechanism, the banking system was used to channel resources to these large firms. The government was drawn into the business decisions of these firms and saw to it that these large firms became successful exporters and consequently expanded into industrial groups that dominated the manufacturing industry. Although Korea's industries could perhaps, according to Park (1990), have succeeded on their own, the government's control over the industry grew and some of the power that the government exercised over the industry was justified as the concentration of economic power in the hands of few conglomerates, even though necessary for efficiency, meant that distributive equity was compromised. The government's support of industrial groups has also created a moral hazard problem as government's role as a *de facto* partner meant that possible government bailouts induced excessive risk taking. Park (1990) labels the 'interweave' of government and the industrial conglomerates that continued to develop past the 1980s as a 'development mercantilism' (Park, 1990).

Contrastingly, according to Park (1990), the Taiwanese economy exhibited high rate of savings, chronic trade surpluses, conservative stance on fiscal and monetary policy, and an egalitarian development philosophy and most importantly an industrial structure characterized by a large number of medium and small-sized firms in manufacturing. This meant that policy makers were mostly denied to exercise two instruments of industrial policy: the control over credit and budgetary allocation for development purposes. The political leadership was, also, determined to avoid the concentration of domestic productive resources in the hands of few private businessmen and therefore the public sector accounted for half of manufacturing value added during the 50s. Park (1990) also concedes that Taiwan took up export-promotion of labour intensive manufacturing products, just as Korea did but the choice of technologies for Taiwan was not similar to Korea's increasing returns since they had at their disposal a large pool of experienced entrepreneurs. Park's (1990) study shows that the Taiwanese industries with their small size of an average of 300 employees accounted for about 60 percent of the manufacturing value added while that share was around 6 percent in Korea. This meant that the Korean experience of direct intervention could not be adopted and therefore the policy makers took measures to provide uniform incentives on the basis of export performance.

Park (1990) also noted that, in Taiwan, problems related to scale economies; collection and dissemination of information on foreign consumers' preferences and technological developments were bridged by a large number of traders from mainland China. The latter frequently come with large orders that are subdivided among small firms that gave the Taiwanese access to a large volume of small orders and specialized products with relatively small demand that Korean firms did not accept. However, the Taiwanese did not emulate the Korean success in import substitution, as Taiwanese entrepreneurs were unable and unwilling to commit large capital investments with long gestation periods. Furthermore, the Taiwanese industrial policy regime was not ambitious enough to match Korea's scheme and the attempt to circumvent these problems involving the setting up of an automotive industry by the public sector failed to bear fruits. The important lessons the study draws on are that there is no ideal model for the role of government in the development process and that the institutional and structural characteristics of the two countries have contributed more than the policy activism itself. The differences in the technologies adopted by the two countries bears testament to the fact that structural and institutional forces in the two economies have shaped the form of government intervention. Park (1990) also concedes that even though there is no sufficient evidence to believe that government intervention was efficient after the mid-70s, it is difficult to believe that the private sector alone could have achieved a sustained export drive without direct government intervention.

In sum, as noted by Amsden (2001), the developmental state in the Asian countries was crucial for its industrialization and export expansion. The state set four functions for itself: (i) development banking, (ii) local-content management, (iii) selective seclusion (opening some markets for foreign transactions and closing others), and (iv) national firms formation. Two principles guided this effort (a) to make manufacturing profitable enough to attract private entrepreneurs and (b) induce enterprise to be results-oriented and to redistribute their monopoly profit to the population at large (Amsden, 2001: 125). Similarly, judicious targeting and organization to ensure the efficacy of public policy to encourage primary product diversification and process, exportation and domestic capacity creation (through training, infrastructure provision including research, subsidies, credit provision etc) is made by governments of Southeast Asian countries (Jomo and Rock, 2003).

An interesting political-economy factor that was crucial in most of the newly industrialized countries of Asia was the success in attaining growth with equity that accompanied their openness, which was not the case in Africa (see Alemayehu 2005). Athukorala and Menon (2000) shed some light on the Structuralist-Neoclassical debate on what it took the East Asian economies to achieve growth with equity by summoning the Malaysian experience. Mainstream (neoclassical) economists [illustrated in the works of Krueger (1995), Balassa and Williamson (1987) and Fei *et al.* (1979)]construe this achievement as a natural outcome of export-led-industrialization and suggests that it can be replicated in other countries once the policy fundamentals are right. This paradigm suggests that since the comparative advantage of less developed economies is in the production of labour intensive products, the expansion of manufactured exports results in the expansion of manufactured exports and hence higher employment. Structural economists are a bit reluctant to accept these hypotheses. Athukorala and Menon (2000) cited the works of Amsden and Van Der Hoeven (1996), Helleiner (1994) and Taylor (1991) which provide the anti-thesis to neoclassical conjecture by arguing that the growth with equity outcome is brought by the "favourable initial conditions of these economies and the highly accommodative world market situations at the formative stages of their economic transformation" (see Athukorala and Menon, 2000).

The Structuralist argument is illuminated (see Athukorala and Menon 2000) by the observation that the East Asian economies had a head start in terms of higher educational standards, relative equality in income distribution and broad based income ownership. Furthermore, the rapidly expanding markets of developed countries in the 60s and early 70s stimulated the expansion of labour intensive manufactured exports without requiring any real wage restraint. This meant the economies had enough breathing space to strengthen their industrial capacity, which would not have been the case

had they faced depressed world market conditions, which in turn would have required them to cut costs leading to stagnation in real wage growth and a shift of income from labour to capital. Thus, the global expansion, it can be argued, provided a cocoon for domestic industrial capacity and, what is more, gave East Asian industries sufficient time to select areas of specialization since higher wages or rising exchange rates provide an incentive for firms to move into more productive, higher-value activities (see Athukorala and Menon, 2000).

The Dynamics of the Exporting Industries and the Role of Foreign firms

The dynamic and structure of exporting firms and their interaction with foreign owned firms in Asia were also an interesting issue that needs to be examined.

In Taiwan (see Hsueh et al 2001), by 1990s high technology products, many produced in the Hsichu Science-based Industrial Park, were playing a larger part as the export and industrial sector of the country. There were also virtually no state-owned firms active in exporting, the latter being stuck in the import substituting industries. The government has also played, through privatization, a crucial role in identifying firms which became a foundation for large enterprises in Taiwan. The government and the USAID financing were also crucial. The USAID for instance offered significant capital for about 440 firms in 1952 to 1958 to the tune of 23.7 percent of all capital of these firms (Hsueh *et al* 2001).

The industrial structure and the management of Taiwan's industries in general and its exporting firms in particular are quite small and usually family owned. The small family firms of Taiwan were not strong enough to survive in a global market. They survived within a network of subcontracting medium to large firms who got their orders form foreign buyers, and subcontracting these jobs are done through the pyramid of hierarchical firms. The central firms could either be manufacturing or trading firms. These have the advantage of pooling limited resources to accomplish large production and export tasks making the whole net-work strong even if individual firms could be weak (Hsueh *et al* 2001). This can be read from the experience of the Li-Wei trading firm given in box 1 below. Taiwan politicians were also forced to leave the management of the most important parts of the state-owned sector to competent technocrats and to keep politics and rent seeking out because the country couldn't afford to retain sick public firms.

Box 1: Network of Exporting Firms in Taiwan – the case of the Li-Wei Trading Firm

Li-Wei originated as trading company. When it began, it specialized in designing and assembling final products, and contracted out the production of parts and components of the machines to twenty to thirty satellite firms. In this way, Li-Wei minimized the use of its own resource and achieved a large volume of business. When Li-Wei grew, the number of satellite firms increased to around 150, and some of these satellite firms also grow substantially in size along with Li-Wei. Their relationship was maintained and strengthened through business ties as well as through personal friendship. Except in special cases that required strict specification or delivery date, no formal contracts were necessary….Li-Wei rewarded good satellite firms by giving them bigger orders and a short turn-around period for payment. As Li-Wei's sales volume grew, in order to control better and to upgrade its production, the company gradually increased its own production capability. For those parts requiring higher technology, strict delivery dates and so on, Li-Wei decreased the portion contracted out. In contrast to the 100 percent outside contracting in the early 1980s, by the 1990s Li-Wei contracted out only around 25 percent of its production to satellite firms. (Hsueh *et al* 2001: 95-96).

The role of foreign firms, especially those from Japan, in the export performance of the newly industrialized countries of Asia was also crucial in the success of their exporting activities. This, partly, could be read from the pattern of foreign direct investment (FDI) in the region. Urata's (2001) study investigates the changing structure of foreign trade and FDI in East Asia and its impact on

economic growth. Urata (2001) claims that two factors contributed to the significant expansion in foreign trade and FDI inflows in East Asia that he classifies as internal and external. The principal element in the first was the liberalization of both trade and FDI coupled with stability in the macroeconomic environment [signaled by a relatively stable price levels and an abundant supply of well disciplined, low wage labour] contributed immensely to the expansion of exports and the attraction of FDI inflows. On the other hand, the latter is represented by substantial realignment of exchange rates and technical progress achieved in information technology. Another element that constitutes a marriage between the two factors is the increase in foreign trade and FDI that was facilitated by the increased competition among multinational firms that resulted from liberalization and deregulation in various sectors.

In particular, Urata (2001) observed that the East Asian economies became the sole beneficiaries of a growth in outward FDI by Japanese firms motivated by, what Urata dubs 'wealth effects' that are created by the increase in the value of collateral and liquidity. The increase in liquidity that was introduced into the Japanese economy in a last ditch attempt to catapult the economy out of recession caused by the decline in exports that pushed up the prices of shares and land and created the bubble economy resulted in asset price inflations that further promoted Japanese FDI by making it easier for Japanese firms to obtain loans. The bubble economy also contributed to the expansion of exports from the East Asian economies by creating Japanese demand for imports. Japan's contribution to the rapid expansion of FDI in East Asia and export growth is unprecedented. An investigation of the patterns of intraregional trade and FDI in East Asia from the early 1980's to the mid-1990's shows that intra-East Asian trade in world trade increased significantly from 5 percent in 1980 to 12 percent in 1997. The study also shows that a large part of that trade takes place between Japan and other East Asian economies, amounting to more than half the level observed for East Asia as a whole. But, intraregional trade between the Asian NIEs and for ASEAN is quite dismal amounting to 0.9 and 1.3 percent of global trade, respectively, in 1997 (Urata, 2001).

According to Urata (2001) intra-East Asian trade was more important as a source of imports than as a source a destination for exports, unlike NAFTA where intra-NAFTA trade was important for its exports. The author argues that multinationals that acquire imports within the region and sell exports outside the region contributed to intraregional trade being an 'export platform'. The Urata (2001) study finds that FDI and bilateral trade are positively related, more so in 1980 than in 1994. This is perhaps explained by the lax dependence of East Asian subsidiaries on parent companies. However, Akuyz *et al* (1998) argued that although the economies of East Asia became highly export oriented at a latter stage in their development, that was not so in the beginning. Integration was gradual, strategic and included not only trade but also technological transfers. Furthermore, Akuyz *et al* (1998) argued that although FDI may have been important in Hong-Kong and Singapore the role it played in Japan, Korea and Taiwan is very limited.

According to Jomo and Rock (2003) the link some of the firms of fast growing Asian economies created with foreign companies, was largely successful in boosting the output of agro-industrial firms and their exporting capacity. Such firms not only able to acquire new technology and managerial & marketing skill from their foreign partners, but also managed to penetrate the markets of developed countries such as Japan. The example of the Charoen Pokplahan (CP) Group of Thailand is the case in point and given in box 2. (Jomo and Rock, 2003). Jomo and Rock (2003) also made a subtle distinction between the Northeast and Southeast Asian experience in industrialization and exports. They noted that unlike Northeast Asian (Japan, Korea and Taiwan) companies, firms in Southeast Asia do not have their own industrial, technological and marketing capabilities to produce exports by their own. Instead their exports have come from subsidiaries or companies vertically linked to foreign transnational that have relocated in the region to lower production cost or to overcome import restrictions. Hence, FDI was much more important in Southeast than Northeast Asian countries.

While exporting firms in Northeast Asia developed from import-substituting industries, such firms in Southeast Asia are weakly linked to the rest of the host economies and largely resemble exporting enclaves (see Jomo and Rock, 2003: 165).

Box 2: Rise of Agro-processing Exporting Firms in partnership with Foreign Firms

The Charoen Pokplahan (CP) Group in Thailand got its start in 1921 as a trading company importing seeds and vegetables and exporting pigs and eggs. In 1976 CP moved into poultry farming, following an announcement by the Board of Investment that promotional privileges were available for this activity. CP entered a joint venture with an American company, Arob Acres. The latter provided and continued to provide CP with chicks. CP also established a joint venture with Japanese firms to market frozen chicken meat in Japan. CP pioneered contract farming in Thailand including guaranteeing loans for farmers from the commercial and related banks. By 1979 CP controlled 90 percent of poultry exports and 40 percent of the domestic animal feeds business. CP also used Board of Investment privileges to establish its own trading company, CP Intertrade, and to establish plantations for growth mug beans and maize (Jomo and Tock, 2003: 149).

2.2 Is it only Asia? African Success Stories in Exporting & Economic Growth

Botswana's Growth and Mineral Exports

Many studies have expounded on the issue of why Africa was doomed to poverty and have sketched out a number of hypotheses that could explain what Easterly and Levine (1997) labels Africa's growth tragedy (Acemoglu, Johnson and Robinson (2001a) These explanations range from Baros' (1991) negative 'African dummy' to Sachs and Warner's (1995) curse of natural resource abundance. Despite these explanations for Africa's destitution, Acemoglu and Robinson (2001a, 2001b), Botswana (an Africa nation) had the highest per-capita growth in the world in the last 35 years. They investigated what made Botswana different from other African countries.

The Acemoglu and Robinson (2001a, 2001b) study noted that Botswana achieved rapid development following good policies. However, the authors note that Botswana is an exception because good policies were complemented by good institutions-*what they refer to as institutions of private property.* The study criticizes earlier studies that claimed that policies might have been better in Botswana because Botswana is a more equal country [Alesina and Rodrick (1994), Persson and Tabellini (1994), Benabou (2000)]. However, Acemoglu and Robinson (2001a) argued that inequality, both of assets (primarily cattle) and income was high in Botswana and that it bordered that of South Africa and countries of Latin America, such as Brazil and Columbia. The Gini coefficient for two periods: 1985/86 and 1993/1994 being *0.56* and *0.54*, respectively. They also rejects the claim that 'good policies are just a reflection of the fact that government intervention in Botswana was limited [Krueger (1993)]. For Acemoglu and Robinson (2001a) detailed planning and massive government expenditure have been the essential characteristics of the Botswana economy and the degree of socialization of the economy [central government expenditure] is estimated to be around *40 percent*, higher than the African average. In fact, according to Freeman and Lindauer (1999), Botswana exhibits most of the features that are raised as explanations of Africa's growth problems. It is land-locked and mineral dependent-parameters that figure in negatively in Sachs and Warner's growth. According to Harvey and Rosen (1990, cited in Freeman and Lindauer 1999), at independence [in 1966] and prior to its economic takeoff its pool of well-educated citizens is low; and apart from its rail links to South Africa the country's infrastructure was poorly developed, its Gini coefficient of 0.54 indicated a high degree of inequality by any standards, while for the better part of the three

decades it has been surrounded by economies that were embroiled in civil unrest that limited its access to imports and harboured an ominous influx of refugees (Freeman and Lindauer, 1999).

Acemoglu and Robinson (2001a, 2001b) study claims that what has perpetuated the growth in per-capita income all these years is found in institutions of private property. Four factors have contributed significantly to the formation and preservation of these institutions (see Acemoglu and Robinson 2001a, 2001b). The *first* is that Botswana possessed relatively inclusive pre-colonial institutions that put bounds on how the political elite functioned. The *second* is the minimal impact of British colonialism on the traditional institutions that scrutinized how the elite behaved. The *third* factor was that, after independence, the elite in Botswana found it in their best interest to preserve the institutions of private property. While the *fourth* and important factor was that Botswana was rich in diamonds, the export profit of which created enough rents for so that no group found it in its best interest to challenge the status quo. But, the study notes, these factors alone did not determine the fate of the nation and emphasizes the role that the critical decisions of post-independence leaders have assumed. But, the authors note, the argument that the success of Botswana depended on good institutions ["referring to political institutions that allowed commoners to criticize chiefs enabled an unusual degree of participation in the political process and placed restrictions on the political power of the elites"] is only a proximate answer to why Botswana was successful and that one should ask the question: why has Botswana such good institutions when the rest of Africa is devoid of them?

According to Acemoglu and Robinson (2001a, 2001b) well-enforced property rights were in the interest of the Botswana's political elite in the aftermath of independence. The strongest economic and political interest group in Botswana, after independence, was that of cattle owners. At independence the only real prospect for a sector of economy to develop was ranching and this was done successfully by exploiting the EEC market and the subsequent development of infrastructure increased ranching incomes. The study notes that the primary beneficiaries of government policy have been the organized elite. But that was only part of the story and not a unique one at that as some other African countries also came partway. By the mid 70's the income from diamonds outstripped that of ranching income, but the elite did not rush to expropriate the income from diamonds for, particularly, two reasons. One was that the elite did not feel threatened by the prospects of growth, and slim chance that the elite became political losers deterred them from working towards the destruction of the good institutions. The little risk that the Botswana elite faced in pursuing developmental policies was not shared by other African countries, where developmental policies only worked to dispossess traditional political institutions [chiefs for instance] of their power. The second factor was that the constraints placed by institutions such as the *Kgotla*[6] may have ensured the accountability of institutions and may have forced the elite to opt for the enforcement of their property rights. These institutions assured that there were no political instabilities. Colonial rule, however minimal, did not deter post independence leaders such as Seretse Khama and Quett Masire from forging an unlikely coalition between tribal chiefs, cattle owners and the BDP-the ruling party (Acemoglu and Robinson 2001a).

Acemoglu and Robinson (2001a, 2001b) noted that the income from diamonds consolidated the institutions of private property and a relatively democratic polity. The BDP coalition guaranteed that the rents from diamonds were distributed widely so that the opportunity costs of undermining the good institutions and therefore the costs of further rent seeking, for the majority, were high forcing a resolute allegiance to the status quo. The study concludes by arguing that the adoption of good policies has been an essential element of Botswana's growth, which promoted rapid accumulation, investment and a socially efficient exploitation of resource rents. It is noted that these policies resulted from a framework of quintessential institutions of private property that encouraged investment and economic development. Hence, Botswana's growth has been a juxtaposition of good institutions-good policies-resource rents [primarily the export of diamonds, and export incomes from cattle ranching prior to the 70's].

[6] See page Acemoglu and Robinson (2001a, p. 23)

Rodrick (1997) ascribes Botswana's success to prudent fiscal and macroeconomic policies, well-developed human resources and an early demographic transition that reduced the dependency ratio, apart from the gains from diamond exports. Rodrick notes that the first factor has contributed the most as it accounts for more than half of Botswana's good performance paired-against the Sub-Saharan average. The government, by deploying a set of adjustment policies, has managed the diamond boom in an exemplifying manner. The dividends to good governance in macroeconomic management have spilled over to other sectors as well. There has been a consistency in the designing of sensible macroeconomic policies with little or no urban bias. Although the set of measures that the Botswana's government put together were largely the reason for its success, the Botswana government has never operated on the philosophy of laissez-faire [the large *degree of socialization* (government expenditure to GDP) that stood at 50 percent, as we noted above, by the early nineties, was one of the highest in the world[7]. What is perplexing about Botswana growth is that its initial conditions were not favorable, as we noted above. A part of the riddle that Harvey (1992) had figured out is the rural origin of political leadership that contributed to export agriculture escaping the 'wrath of tax policy', unlike other countries of Sub-Saharan Africa where the social origins of the elites are urban and export taxes are exorbitant. Another element of Botswana trade is that it was part of the South African Customs Union (SACU) and therefore did not operate under an independent trade policy. The Botswana government is said to have a share of customs revenue collected by the South African government that amounted to a fifth of Botswana imports. What is more important is that government officials had no control over the revenue on a day-to-day basis and that they did not possess the ability to interfere with the flow of goods from neighboring South Africa, which meant that domestic produces gained little from policy-makers in terms of unfair favors. The absence of the capacity on the part of officials to grant lobbying groups favors of any sort had important policy implications on other fronts as well. Rodrik (1997) cites the case of the large drop in diamond prices in the early 80s that called for the devaluation of the currency and avoiding exchange controls was accomplished swiftly due to the absence of 'entrenched urban interests'.

According to Harvey and Lewis (1990, cited in Freeman and Lindauer 1999), Botswana's growth success, despite unfavorable initial conditions, could be attributed to a number of important points that may have contributed to growth in the southern African state (see Freeman and Lindauer 1999):

- ✓ That economic policies matter-Botswana chose prudent fiscal and macroeconomic direction {in 1998, Botswana ranked among the 50 top countries by Wall street Journal's index of economic freedom}.
- ✓ Heavily dependent on revenues from its diamond mines, but avoided 'Dutch-Disease'-by not engaging in excessive spending of the export windfalls which would have led to an appreciation of the real exchange rate and hurt both agricultural and non-mining industrial growth.
- ✓ It managed a stable exchange rate
- ✓ Its participation in the SACU limited lobbying for favours in the trade arena and spared it from some of the rent seeking and inefficiencies that characterized import substitution schemes elsewhere in SSA [Roderik (1997)]
- ✓ The public sector allocated resources based on economic and social returns and was successful with foreign investors; and state investment in education, especially at the primary level, was among the highest in the region

Export Processing Zones and Exports: The Case of Mauritius and Madagascar

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[7] Although Rodrick labels Botswana's degree of socialization as one of the highest in the world, the OECD average was around 41¼ percent, with experience ranging from 29 percent in Korea to 59 percent in Sweden. Figures for the year 2003 show that Austria, France and Belgium have ratios of public expenditure to GDP 51.6 percent, 54.4 percent and 49.7 percent

Mauritius

According to Rodrik (1997) Mauritius's prospects for growth, in the 1960's, were to say the least slim. Mauritius's success largely depended on an export-boom in garments to European markets and an associated investment boom at home. The Island's economy constituted a successful export processing zone (EPZ) and a highly protected domestic sector with average effective rates for the manufacturing sector reaching a staggering 89 percent making Mauritius a country following a "two-track strategy". Policy makers faced resistance from import substituting industrialists in their attempt to relax the trade regime. Local industrialists were granted tax holidays and protection from imports via tariffs and quantitative restrictions and the formation of the EPZs was the policy makers' way of circumventing the resistance (Rodrik 1997). The political advantage of the two-track strategy was that it never took protection away from import-substituting industrialists, while opening opportunities of trade and employment. But since the 1980s the country has dismantled most of the quantitative restrictions that have been put in place for longer than two decades. The 90s also saw significant tariff reforms that have contributed to a boost in export growth (Rodrik 1997).

According to Nath and Madhoo (2003), the early import substitution strategy of Mauritius was followed by export-led growth strategy. This led to growth of the economy in the 1970s which was basically fueled by the favourable condition for Mauritian sugar industry in the world market. This has led in 1973 to an increase in proceeds and hence money supply. This increase in liquidity gave additional boost to the plans initially set by the government. The EPZ and the tourist industry were further being enhanced due to the investment of sugar boom profits by sugar companies in joint ventures with foreign investors. The effectiveness of the policies implemented, such as tax holidays, exemptions from import duties and preferential access to European markets, the purchase of new machinery and equipment and hiring consultants, direct foreign investment (FDI), and the purchase of new technology licenses for domestic production of new products or the use of new processes was reflected by the excellent economic performance that followed this policy. The number of enterprises in the EPZ increased to 88 in 1977. EPZ exports rose to 20 percent of total exports. FDI from Hong-Kong, France and Britain has contributed a great deal to the development of the Mauritian EPZs (Gray 1994). An international technology transfer took place and local investors also joined in the process. EPZ textiles and clothing firms were largely owned by local investors (55 percent), followed by joint ventures (35 percent) and those fully foreign owned (15 percent) (Fowdar, 1994, cited in Nath and Madhoo, 2003). The local investment was largely financed from the surpluses of the sugar boom. The average annual real growth of the economy was about 8.2 percent for the period 1971-77 with the peak real growth rate of 16.6 percent in 1976 (see Nath and Madhoo, 2003).

According to Nath and Madhoo (2003), the simultaneous pursuit of import substitution and export promotion strategies led to some policy contradictions. The high rates of growth noted were not sustainable as they rested on the windfall gain of the sugar boom. In addition, part of the sugar boom resource was wasted through extravagant public sector projects, generous wage awards, social transfers and subsidies. Following this, in the post economic euphoria period (1978-83), the average real growth decelerated to 1.7 percent, the balance of payment worsened and inflation rate reached 42 percent in 1980, partly fuelled by world oil crisis in 1979/80 (Nath and Madhoo, 2003).

According to Gray (1994), the late 80s and 90s have not been kind to the Mauritian, as labor-intensive exports [mainly sugar and garments] and investment in the export processing zones declined and they have barely looked in a position to surmount the loss ever since. The study claims that the erosion of competitiveness lies in the inability of productivity to catch-up to wages that have been rising as a result of near full employment. It also claims that export successes have been based on a fragmented incentives environment. But, the perpetuation of the same environment in an economic environment where capital and labor resources are scarce led to a significant misallocation of resources and checked competitiveness. The World Bank was supporting the efforts of Mauritius to

strengthen growth *first* by building the technological capacity to guarantee that productivity is in par with the rise in wages, and *second* improve the suppleness of the markets for labor and capital so that they flow to their most efficient uses (Gray 1994). Mauritian manufacturers have been subject to some quite intense competition from countries that have a competitive advantage in traditional labor-intensive exports. The incapability of Mauritian manufactures to go up in the technological ladder has meant that productivity was unduly sacrificed. At the beginning of the 90s the Mauritian EPZ had a productivity of *$3,247 per man year* compared to a staggering *$12,157* in Singapore's garment industry, while the value added content of exports declined from its 1983 level of *42 percent* to *36 percent* in 1991. These major failures were compounded by a decline in labor costs of only *1 percent*, during the same period [*from 20 percent in 1983 to 19 percent in 1991*] (Gray 1994).

In response to the critical economic situation that began in late 1970s, a typical structural adjustment programme supported by a standby arrangement with IMF was adopted in 1979. The main policy measures implemented were fiscal stabilization, exchange rate re-alignment, cautious wage policies, trade liberalization, financial consolidation and sectoral/supply side policies. Following these measures, the current account of the balance of payment changed from a deficit of 15 percent of GDP to a surplus of 5 percent over the period, 1983-87. The inflation rate dropped to 0.6 percent in 1987 rendering the EPZ sector more competitive. With such favourable conditions, the number of EPZ enterprises increased to 591 (Nath and Madhoo, 2003).

As reported by Nath and Madhoo (2003), in two decades, Mauritius transformed itself from a mono-crop economy, solely dependent on sugar, to a diversified one comprising the manufacturing and services sectors. In 1989, the offshore center was also set up, which have attracted more than $4 billion of offshore funds. The Stock Exchange of Mauritius (SEM) started to operate in the same period. Stimulated by the EPZ, the Freeport was created in 1992 as a part of its strategy to develop as a regional trade center. In 1997 tourism increased by 10 percent, the EPZ by 6 percent, financial services by 5.9 percent and sugar by 5.5 percent. Thus, Mauritius was ranked 29th in the World Competitiveness Report of 1999 outperforming some "Asian Tigers" and 1st among African countries (see Nath and Madhoo, 2003). Similarly, a study by Gray (1994) noted that over a quarter of a century Mauritius has managed to quadruple its per-capita income and virtually eliminate unemployment. As Gray (1994) noted, with a population size of *1.1 million*, heavily dependent on external trade and a rather slender industrial base, Mauritius seeks to follow through the Hong-Kong-Singapore path to growth that is built on the foundations of a competitive regulatory framework and nurture technology support services to create a private sector-led business environment.

Madagascar

The study by Cling *et al* (2004) spotlight on the success of export processing zones in Madagascar and their significant contribution in terms of increased exports and jobs. In the year 2000 the 190 active companies of *Zone Franche*, as the Madagascan EPZs are also known as, employed 75,000 and 100,000 workers in the years 2000 and 2001, respectively. But the performance of the Madagascan EPZs has did not wane; even, after the political crisis that split the government in to two subsided in 2003. The formation of *Zone Franche* in 1990 followed the adoption of an export-led growth strategy emphasized by the structural adjustment policies that Madagascar adopted at the end of the 1980s. AS Cling et al (2004) noted, the regulation that initiated the formation of export-processing zones obliged the companies that decided to join the EPZ to export 95 percent of their production and enabled companies that provide services to *zone*-members to profit from the zone arrangement. In addition, the companies in the zone are exempt from all duties and taxes on exports and imports, and from excise taxes, but are not exempted from the value added tax (reimbursed against proof of export). The companies in the zone are also provided with a two-year profit tax exemption grace period, for intensive basic production companies (farming and fishing), and four-year grace period for industrial and service companies in addition to their special grant to access to credit and free capital transfers. The profit tax following the grace period is also far lower than the rate for companies outside the zone (see Cling *et al,* 2004).

The success of the *zone*, the study of Cling *et al* (2004) claims, was mainly due to the heightened desire of the French to set up businesses in Madagascar that provided a French-speaking environment, a low labor cost , a unit-cost of production that is amongst the lowest in the world, and a lower ranking in the textile quotas imposed by developed countries in multi-fiber arrangements [the quotas of many Asian countries have been saturated]. This later factor was particularly essential in attracting investment from Mauritius. Data for the year 1997 shows that investors of French origin represented 46 percent of the jobs in the zone, while Mauritian, Madagascan and Asian investors made up 28 percent, 11 percent and 7 percent respectively; the rest 8 percent were from various countries of origin. 90 percent of the zone's production in the year 2001 was accounted for by clothing, whereas the remaining 10 percent was made-up by the food processing business, and the crafts and services industry (Cling et al 2004). Both national customs statistics and 'mirror data' from the International Trade Center (ITC) show that both total exports of goods and those of the zone have nearly tripled in the decade 1991-2001. The decade 1991-2002 saw a 15 percent increase in the exports of Sub-Saharan Africa, which only amounts to an average yearly rate of less than 1 percent, whereas the exports of Madagascar grew at an average yearly rate of 11.5 percent, outstripping world trade that grew at the average annual rate of 5 percent. The share of manufacturing products reached nearly half of the total in the year 2001, from its negligible level at the beginning of the decade (Cling *et al* 2004). The Cling et al (2004) study notes that, in the year 2001, nearly half of the total exports of Madagascar came from *Zone Franche*, unparalleled by any least-developed country. The target market of *Zone Franche* is Europe and America. The European market was the source of growth for much of the 90s, but its stagnation at the end of the 90s meant that *Zone Franche* had to depend on other market sources. The AGOA wearing apparel provision that Madagascar qualified for in the year 2001 has provided the substitute source of growth. Madagascar exports to the US have tripled from 1999-2001[8]. Cling *et al* (2004) used three indices to measure the diversification of manufactured exports and found that Madagascar is more diversified than the countries in the sample [including Ghana, Cote D'Ivoire, Senegal, although Madagascar does not appear diversified compared to Mauritius or Senegal]. It is also reported that the average annual growth rate of employment in the zone was 27 percent compared to 4.5 percent for the whole country, for the period 1995-2001. Notwithstanding this success story the issue of *the race to the bottom* in terms of the over-exploitative structure of export-processing zones (such as lack of social legislation that regulates remuneration, the length of working hours, the pace of the work and the encouraging of trade unions etc) is found to be a major problem (see Cling *et al* 2004).

Kenya and Ethiopia: The Rise of Horticultural Exports

In recent years some Sub-Saharan African countries have shown progress in the export of specialized agricultural produce. For instance, the growth of the demand for horticultural products of Kenya in the world market along with its remarkable contribution in the creation of jobs has been very impressive (World Bank, 2003). Adequately remunerative contracts with processing and exporting firms have lured small farmers into supplying horticultural products [especially French beans] while large farms have been successful in the production of cut flowers and have created jobs for thousands of truly poor farmers with little or no land. The urban poor have also found jobs in packaging houses with working conditions far better than their peers find themselves outside the industry. All in all government has been supportive of the efforts of the industry by settling for the role of a facilitator (World Bank, 2003).

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[8] This has resulted in a 2002 recorded trade surplus of $200 million (2001: $250 million) in favor of Madagascar. In 2002, approximately 84 percent (2001: 90 percent) of Madagascar's 'textile and apparel' exports are currently AGOA-eligible, while almost 40 percent of the country's total exports to the U.S. are AGOA compliant (see link to Country Trade Profile at: http://agoa.info/index.php?view=country_info&country=mg.

Although the volume of exports of horticultural products[9] of SSA has grown in recent years with a derived income exceeding $2 billion, SSA's participation rate in the sector [of only 4 percent of the world's total] falls short of its potential. The Kenyan horticultural sector leads by example with approximately 135,000 people directly employed in the sector. Horticultural products have now become Kenya's largest exports surpassing coffee exports. Kenya has now become the largest horticultural products exporter in SSA next to South Africa, the second largest developing country exporter of flowers (next to Columbia), and the second largest supplier of vegetables to the European Union (next to Morocco). The fresh fruit and vegetable, and cut flower exports of Kenya has grown in excess of three hundred fifty percent [from $29 million in 1991 to $164 million in 2000; and from $39 million to $175 million (over the same period) respectively] over the course of a decade. 35 percent of all Kenyan agricultural exports are composed of horticultural products with a total value exceeding $350 million in 2003.

Similarly, the horticulture industry, especially of cut flowers, is booming in Ethiopia, attracting investors from major companies as well as from the neighboring Kenya. An excellent incentive package such as tax-holiday for exporting firms, duty free import of required machineries, and provision of land almost for free as well as availability of cheap credit for exporting firms which could cover about 70 percent of the finance required, together with prudent macro performance of the country, explains the recent boom in investment and exports in the sector. Following this policy, horticultural export in 2003 has increased by 100 percent compared to the level 5 years a go. According to the information from Ethiopian horticulture producers and exporters association, Ethiopia is currently generating $20 million annually form flower exports, only one tenth of coffee exports. But following the expansion by 32 firms (half of them foreign owned) the export income from flowers is expected to reach $100 million by 2007. Projects by another 100 firms from the Netherlands, German, India, Israel who have acquired 450 ha (1,111 acres) of land are expected to generate additional $300 million by 2007. The aggregate income will be nearly 3 times the earning the country currently fetching from its major export item, coffee, which accounts for about 65 percent of its total exports. Certainly the government policy and the countries competitive advantage are bringing a boom in horticultural exports with its various externalities which included the current employment provision for 13,000 people, largely unemployed youth and poor peasants.

In Kenya, a number of factors including rising food safety standards, access to credit, increasing production and marketing costs, it seems, are causing rifts in the system as the horticultural industry increasingly finds the contractual agreement with small holders insufficiently reliable. Recent experiences in Kenya only suggest that the future holds little by way of small-holder participation in the horticultural sector [at least in fresh-vegetable exports and cut flowers]. High transportation costs are also imposing constraints on the Kenyan horticultural industry on its ability to compete with the lower cost/average quality segments of the European Market.

The key lessons that the World bank study on Kenya draws on include: the indispensability of foreign investors and their capacity to adapt to changing circumstances; the political commitment of the government, although at times proved to be shaky and more direct participation of government could have been more fruitful, contractual agreements between firms exporting horticultural products and small holders guaranteed that the rural poor also participated in the sector are few among many (although changes in the trading climate, in recent years, have meant that small holders will could be ultimately sidelined).

2.3 The Lesson for African Trade Policy and the Challenge for Afreximpbank

[9] Horticultural products are defined to include processed fruits and vegetables, fresh fruits and vegetables and cut flowers.

What is the lesson that we can draw from these experiences for Africa in general and for Afreximbank in particular? This section will briefly address this issue.

To begin with Asian countries, it is instructive to note that any lesson that we may draw from the Asian (in particular Taiwan and Korea's) experience need to take into account the different between African countries and the Asian successful exporters in terms of (a) variation in initial conditions that owes its origin to the nature of Japanese and European colonialism, (b) the institutional and political difference between the two groups, as well as (c) the global environment such as the cold war which shaped the foreign relation of Taiwan and Korea and its impact on their success story. Notwithstanding such difference, we can draw the following lesson that may help the design and implementation of trade policy (or export development strategy) in Africa:

First, there is a need to note the link between trade policy and industrial policy. Export strategy can not be developed in isolation and need to be set in the context of the countries development strategy in general and the industrialization policy in particular. In this process, outward-orientation will help realize economies of scale and the exhaustion of indivisibilities. It also helps to avoid stop-go policies associated with balance of payments difficulties when exporting is a problem. Second, the role of government in ensuring success in exporting may go beyond policy making. The government not only need to create the enabling condition but also may need to alter the incentive structure in the operation of the free market to ensure the success of exporting. Third, financing exports is one of the most important policy instruments that could be employed by the government. However, financing export loans may differ at different stages of development (such as at shipment and production), and need to be based on export performance.

Fourth, the same policies have different costs at different stages of development of economies. At low levels of development of a country most economic activities take place in agriculture and the costs of control over trade, industry and the factor market are fairly small. Until mechanisms are found that permit the satisfactory growth of agricultural output and productivity there can be very little economic and export growth. This implies a prerequisite for satisfactory growth lies in the provision of infrastructure and incentives for agriculture. However, once those are in place a given set of restrictions over trade will exact an even more slowly growing set of industrial activities. Thus a successful export-oriented strategy would put in place a set of frameworks that result in the adoption of other efficiency and growth-enhancing policies that tally with different level of development.

Finally, our discussion in the previous section showed that that Taiwan took up export-promotion of labour intensive manufacturing products, just as Korea did but the choice of technologies for Taiwan was not similar to that of Korea's. Taiwan took the dominant role of its small firms in to account in the design of its policy. The differences in the technologies adopted by the two countries bears testament to the fact that structural and institutional forces in the two economies have shaped the form of government intervention. Thus, export and industrialization development strategy need to depend on the structural and institutional context of the country in question – in short there is no one-fits all trade policy for all countries in Africa.

Like that of Taiwan and Koea, there are also lessons that we may draw from the (export) success stories of some African countries whose experience is discussed at length in the previous section. This includes:

First, as the experience of Botswana shows the rents from diamond exports were distributed widely so that the opportunity costs of undermining the good institutions and therefore the costs of further rent seeking, for the majority, were high forcing a resolute allegiance to the status quo. In the process Botswana adopted good policies which promoted rapid accumulation, investment and a socially efficient exploitation of resource rents. Thus, fair or socially optimal distribution of rent income from

exports, at least among the elite, seems essential for adopting and sustaining success in exporting. Similarly, the memberships of Botswana in SACU has served to lock-in some of the good policies and served to avoid rent-seeking. Perhaps the lesson from this is the importance of regional groupings such are regional integration schemes and agreements that could serve as agencies of restraint to leave up to commitment by member countries.

Second, Botswana's and Mauritius' experience shows that good economic policies matter. Stable macro polices (including optimal labour policy that monitor productivity and wage growth) are central for successful trade policy. However, such policies are extremely important once a certain level of export growth is attained. Thus, the level of growth and exporting need to be taken on board in assigning weights for policies of macro stability, especially if deviation from such policies (such as inflation financing) could have some better benefits. Moreover, the public sector need to allocated resources based on economic and social returns. It also needs to make wise use of rents from the boom in sugar export revenue.

Third, partnership with foreign firms and countries is central for successful export development strategy. This will help not only to get access to the markets of the developed countries but also as a tool in facilitating technology transfers especially for a country with a brief industrial history and limited technological capability. Such markets could also serve as sources of growth, provided that export rents from such preferential arrangements are not disproportionately taken by firms from the preference offering countries.

Fourth, the role of government is central for a successful export development. This is particularly required in the design and implementation of export promotions strategy that may include the development of export processing zones (EPZ). Its intervention is also required to make firms and companies foreword looking in creating a private sector-led business environment, in diversification of exports, in building productive capacity though enhancing competitiveness and attraction of foreign investment. This could be seen from the contribution of FDI from Hong-Kong, France and Britain to the development of the Mauritian EPZs in the early 80s.

Given these lessons from the experience of countries with successes in exporting, it is instructive to ask what the major challenges of African exports are and how could the Afreximbank contribute towards addressing these challenges? The next section will deal with these issues.

3. Afreximbank and Export Challenges of Africa

3.1 The Export Challenges of Africa

Although the data limitations pose a problem in computing all indicators of openness, it is possible to judge the openness of Africa from the information given in Table 1. Table 1 shows that exports and imports account for about 60 of Africa's GDP (equally divided between exports and imports). Africa's financial integration in the world economy is, however, limited as can be read form the share of FDI in GDP which is about one percent in the last decade. The share of aid (and hence debt creating flows) in the total budget of most African countries is significant, however. Neither Africa could be taken as interventionist in the light of the share of public spending on subsidies (which is about 3.5 percent) and the share of taxes on international trade as the share of revenue, excluding grants, (which is about 12 percent) during this period. Notwithstanding the recent drive towards openness, Africa's trade is besieged by many challenges.

Table 1: Some Indicators of Openness in Africa (Average for the period 1990-2001)

Region	(X+M)/GDP	XGNS/GDI	FDI/GDP	Subs/Exp	TaxInt'l/ Revenue

East and Southern Africa	52.9	25.8	0.6	1.3	9.3
North Africa	60.9	31.7	1.1	6.8	12.1
West Africa	69.8	34.8	1.9	2.5	19.7
Sub Saharan Africa	57.8	28.5	1.0	1.6	12.2
All Africa	58.1	29.0	1.0	3.5	12.2

Source: Based on World Bank's African Development Indicators (2003)

The challenge of African trade is multifaceted. However, it is fundamentally related to the dependence of its exports on primary commodities and the associated problems with it. Table 2 shows the deceleration of the growth of the volume of exports in SSA from about 15 percent per annum in the early days of independence to a negative growth in early 1980s and picking up to 3.5 percent in the last decade. The current level of growth is far below the average for other parts of the world. The share of Sub-Saharan Africa in the total world export values has also steadily declined. This share has declined by more than half in the period 1980 to 2001 (see Table 3).

Table.2 Growth of Export Volume by Region

Region	1965-73	1973-80	1980-86	1993-02
Industrial Countries	9.4	5.4	3.5	6.2
Developing Countries	4.9	4.9	4.4	7.1
SSA*	15.0	0.1	-1.9	3.1

Source: Based on World Bank, World Development Report 1987 for the period 1980-86 and World Bank, Global Economic Prospects 2003 for 1993-02 * the figures for 1993-02 include South Africa

Table.3 Percentage Shares of Africa's Export Values in the World total

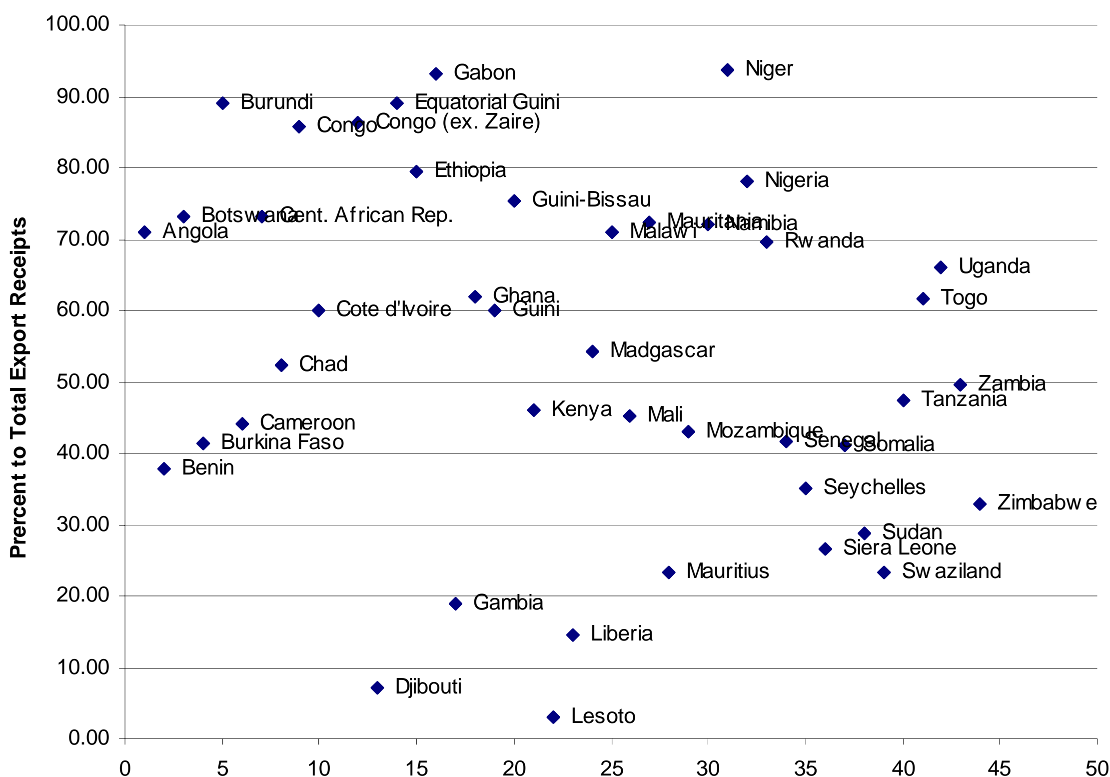
Regions	1970	1975	1980	1985	1990	1995	2000	2001
Developing Countries	22.9	27.5	30.1	25.1	19.7	19.9	23.0	23.5
SSA (of World total)	2.0	2.1	2.2	1.6	1.0	0.8	0.8	0.8
SSA/Developing Countries	8.6	7.4	7.4	6.2	5.2	3.8	3.6	3.5

Source: Based on World Bank, World Development Indicators, 2003.

The structure of African export is characterized by dependence of its exports on primary commodities. Such dependence is making African countries vulnerable to the state of the global economy because such commodities are characterized by low income elasticity of demand, volatile and secular declining prices and generally come from sectors where the scope for technical progress is limited (see, Alemayehu 2002).

For those African countries whose data is reported in UNCTAD's Handbook of International Trade and Development Statistics and Commodity Year Book, more than half of their export earnings come from only three principal primary commodities during the period 1997-99 (see Figure 1). For most small mineral exporting countries this figures rises over 80 percent. Only 8 countries, out of 43, (i.e. Djibouti, Gambia, Lesotho, Liberia, Mauritius, Sierra Leon, Sudan and Swaziland) have a relatively diversified export structure. These are, except The Sudan, largely small island economies. Thus, SSA as a whole depends for about 70 percent of its total export receipts on three major commodities.

Figure 1: Dependence on Three Principal Commodities in Africa (1997-1999)



Source: Based on World Bank, World Development Report, various issues and World Development Indicators, 2003).

As can be read from Table 4, African countries are also highly dependent on a few developed countries as destination for their exports. The average share of these developed countries, for the period 1955-2002, is about 80 percent (it however shows declining trend). Intra-African trade is also very limited, being about 5 percent, and is confronted by many problems (see Alemayehu and Haile, 2003). Of the developed regions/countries, Europe is the dominant trading partner with an average share of about 60 percent. Thus, although the share of Africa in world trade is limited (as shown, say in Table 3 above), what happens in the rest of the world, in particular in the developed countries, has an enormous impact on Africa given the share of this trade in Africa's GDP (see Alemayehu 2002).

Table 4 African Exports by Destination (percent share to total exports)

Period	Developed Market Economies					Developing countries & Territories	Former Socialist countries
	Europe	USA	Japan	Other Develope	Total Develope		
1955	70	10	1	3	84	12	4
1960	67	8	1	3	79	13	8
1970	70	7	4	1	82	10	8
1980	49	31	2	1	83	14	3
1990	57	19	1	2	79	17	4
1995	51	18	2	3	74	22	4
2000	43	23	2	3	71	25	4
Average	**58.1**	**16.6**	**1.9**	**2.3**	**78.9**	**16.1**	**5.0**

Source: UNCTAD Handbook of International Trade and Development, various issues

The negative impact of dependence on primary commodity exports is reflected in three interdependent phenomena: a decline in terms of trade, instability of export earnings, and absolute decline in levels of demand and over supply by liberalizing developing countries. This is partly shown in Tables 5 that shows

Africa suffers from export and export price instability. The secular decline in Africa's terms of trade, the last two years showing some trend of bouncing bank, is also not a recent phenomenon. It is rather a pattern that persisted from mid 1970s and well document in the literature (See Alemayehu 2002, 2003).

Table. 5 Price Instability* and the decline in price of Selected Primary Commodities

	Price Instability				
Commodity	1962-1980	1982-1990	1991-1994	1998-2001	1977-2001
All Non-Fuel Prim. Com.	15.2	8.8	5.0	4.1	11.6
Food	24.4	13.5	3.7	7.2	15.7
Tropical Beverages	25.5	14.1	20.6	5.1	20.8
Cocoa	27.7	15.1	10.2	15.8	18.6
Coffee	28.4	16.8	29.8	8.0	26.0
Agric Raw Materials	16.6	5.7	4.6	4.4	11.7
Minerals, Ores, Metals	12.3	13.0	6.9	5.8	14.0
	Growth in 1980 Constant Dollar Prices, unless otherwise stated				
Commodity	1962-1980	1982-1990	1991-1994	1998-2001**	1977-2001**
All Non-Fuel Prim. Com.	1.1	-3.1	2.9	-2.1	-2.8
Food	1.0	-2.5	2.6	-0.1	-2.6
Tropical Beverages	2.9	-11.0	15.0	-17.5	-5.6
Cocoa	5.7	-11.7	5.9	-12.6	-6.9
Coffee	2.9	-10.3	17.1	-21.6	-5.1
Agric Raw Materials	0.5	-1.9	2.3	-0.7	-2.0
Minerals, Ores, Metals	-0.5	0.3	-3.1	3.4	-1.9

* The measure of price instability is:

$\frac{1}{n}\sum_{t=1}^{n}\left[\left(\left|Y(t)-\hat{y}(t)\right|\right)/\hat{y}(t)\right]*100$ Where, Y(t) is the observed magnitude of the variable, $\hat{y}(t)$ is the magnitude estimated by fitting an exponential trend to the observed value, and n- is the number of observations (UNCTAD, 2002). ***In 1985 Constant Dollar Prices*

Source: UNCTAD, Commodity Yearbook, Different Issues; and Handbook of Statistics 2002.

In sum, we may note the following as the main challenges of exports in Africa:

a) Dependence on primary commodities whose prices are deteriorating over time and are cyclical in the short run.
b) Lack of diversification owing to deficiency in human (skilled but cheap labour, competent managerial class, efficient bureaucracy and cadre of entrepreneurs) and physical capital (that includes infrastructure). This is further aggravated by low level of technological know-how and domestic research capacity.
c) Low level of both domestic and foreign investment and limited access to finance.
d) Lack of access to market and market information
e) Lack of institutions that ensure socially optimal distribution of rents that came from the exporting sector; as well as institutions that could facilitate trade.

Given these challenges it is worth examining how the lessons from successful exporting countries discussed in the previous section could be used by other African countries to address these challenges? and how could Afreximbank contribute towards meeting these challenges of export development in Africa? These questions could perhaps be adequately answered once the Afreximbank programs, facilities and its current strategy are examined. This is done in the next section.

3.2 Afreximbank and the Export Challenges of Africa

3.2.1 Strategic Plans of Afreximbank and Export Challenge's of Africa

As Afreximbank (2004) noted a preparation of viable strategic plan requires considering the following variables: (a) the customer, (b) competition, and (c) the institution to which the plan relates (i.e., its strength and weakness). Moreover, country and other (especially currency) risks are also important. Given these variables the strategy need to identify the Key Success Factors (KSF) to deploy resource according to the KSF of the market leader or where competitors are not involved, or upset the competitive environment by aggressive measure or invest in areas that are untouched by major competitors. Within such planning framework, the Afreximbank identifies a number of Key Success Factors in its industry. This includes:

(a) knowledge of market, risks, opportunities and ability to mange them
(b) local presence and extensive network globally
(c) ability to tackle obstacles that may come from officials, problems of credit concentration, and
(d) links with high credit quality companies, patience to close lucrative deals and integrity and transparency

The problems the bank faced in the implementation of its first strategic plan include (see Afreximbank, 2004)

(a) problems that emanate from dependency of Africa exports on primary commodities
(b) policy related problems such as taxes, commodity policy change and weakness of institutions in many countries, such as the legal system
(c) risk related problems which may arise from political or economic factors
(d) underdeveloped human capital, banking systems and other financing schemes

Beside these problems of implementation, we note that most of the macro targets of the bank (such as raising Africa's share of the world export) are besieged by structural factors that may not be solved by the Afreximbank alone. However the bank may advise individual country policy makers on the right policy direction. The Afreximbank may also need to work (i) to increase trade financing and syndicated loans, (ii) to encourage export processing zones, export credit agencies and commodity sector regulatory arrangements, (iii) to raise resource mobilization including from remittances, (iv) on enhancing information technology and regional integration schemes (see Afreximbank, 2004), and (v) on establishing (or making used of existing) future commodity markets and partnership with foreign companies to exploit AGOA and EBA kind of preferential markets with the aim of capturing such export rents by African exporters (as opposed host country firms), as well as (vi) developing a research wing engaged in forecasting of world market condition in general commodity market conditions in particular..

3.2.2 Programs and Facilities of the bank and the Export Challenges of Africa

To address the challenges of Africa's exports and to realize its own corporate goals, the Afreximbank uses various programs and facilities. These programs are instruments for realizing the bank's strategic plan. They are also flexible, changing with changing conditions. These programs include the following major categories.

1. Afreximbank Line of Credit Program:
The bank uses this program to work in partnership with African and non-African banks in reaching target beneficiaries, who due to their small size would otherwise not be able to access the Bank's resource directly.

With the growth of the non-traditional exports (such as horticulture), the Afreximbank need to intensively use this facility by linking with development and commercial banks in African countries. This way the risk may be shared by the Afreximbank and the African governments. In particular the import facility under this program that allows small and medium sized export manufacturing enterprises to have accesses to foreign exchange for importation of light equipment and inputs may be pushed further to included export related production activities that may be handled in partnership with local banks and governments.

2. Afreximbank Direct Financing Program

This program makes direct funding to corporate entities in Africa and elsewhere large enough in terms of asset size and trading volume (with balance sheet size of over USD 2 million and annual export turnover of over 10 million). This is a short term credit and basically trade related.

Given the small size of most African corporate firms, it is worth investigating how to expand this program and its facility to small size exporting firms through performance indicators such as credit worthiness, preceding years' export performance and risk sharing arrangement with the government of the country in question.

3. Afreximbank Syndication Program (ASP)

This is a program through which the bank arranges or joins a syndicate or clubs of reputable international or African banks in providing financing to African entities for trade or export project-related activities. In this program the commercial risk is shared fully by the bank and the participants. In this program the bank provides the foreign exchange requirement.

As the experience of the successful Asian exports shows, such export-related projects are usually successful when they are carried in partnership with foreign companies in export destination countries. The latter provide both know-how and market information to the local exporting firms. Thus, the Afreximbank may design this program in such a way that it encourages such partnership. This also helps to minimize the risk of the Afreximbank.

4. Afreximbank Special Risk Program

The bank operates various facilities under this program. The program has an overall objective of enhancing the credit worthiness of African borrowers. Through this arrangement it aims to increase the flow of trade finance to Africa at competitive terms. The program has the following specific facilities:

- Afreximbank Country Risk Guarantee Facility
- Afreximbank Join Bill Discounting/Financing Facility
- Price and Exchange Risk Guarantee Facility; and
- Counter Trade-Linked Guarantee Facility.

These facilities are believed to ease access to credit with better condition for African countries and bring more comfort for lenders.

5. Project-Related Financing Program

This program is meant to support the continent's export diversification effort by providing foreign currency financing to export projects to enable them acquire equipment and raw materials for processing. Africa's raw commodities into semi-manufactures and manufactured products.

The Afreximbank need to draw lesson from the success story documented in this study to implement this facility. As we noted above, the Afreximbank needs to encourage African countries or companies to engage in such projects in partnership with foreign companies in export destination countries or advanced countries.

6. Infrastructural and Services Financing Programme
This programme is designed in response to dramatic change taking place in Africa's infrastructure and other services which are becoming significant elements of trade. Countries that have strong engineering expertise or infrastructural facilities (such as electricity, railway construction, port facility etc) could be encouraged to export these services to other African countries.

Perhaps the Afreximbank may engage first in financing the exports of such services and at latter stage in projects aimed at production of exportable. It may also need to do the marketing to individual companies and parastatals (such Electric and Power Authorities and Power producing Firms) instead of to governments. Governments of both importing and exporting countries may also be brought to share the risk with Afreximbank.

7. Afreximbank Trade Information Programme (AIP)
In this program the bank provides to African banks, exporters and foreign investors with interest in African trade, with relevant information on African economies, commodities and markets. It also publish biannual trade journal to disseminate African trade information.

Under this program, the bank perhaps can also develop an African trade database and an online electronic library on African trade and trade-financing matters. The bank may also need to link with regional knowledge forums (such as the African Economic Research Consortium) and national research centers of interest to strengthen its research work on commodity price, demand and supply forecasting, commodity modeling and issues of trade financing. This information may be accessed online or directed to relevant African banks and Ministries engage in exporting.

4. Conclusion: Afreximbank's Role in Addressing the Export Challenges of Africa

The analysis in this study shows that the export challenges of Africa may not be addressed by addressing constraints that are specific to the export sector alone. It is argued here that the export challenges are challenges of a development strategy in general and industrialization in particular. This will partly determine the role that Afreximbank play in addressing these challenges. There are certain strategic policy directions that the bank could support but may not be able to realize them by itself – referred below as macro policy directions. In the discussion below these are largely drawn from the experience of successful exporting countries examined in the context of this study. There are also certain strategic policy directions that the bank may pursue as a corporate entity – referred below as corporate policy direction. The latter are largely within the realm of the bank and are adequately outlined in the Afreximbank's strategic plans. We will just highlight some of these issues here.

Macro Policy Direction

Africa is marginalized from the global market when judged by the degree of its trade and financial integration with the rest of the world. Given the required high growth/investment target and hence the external financing required to reduce poverty, the limited development of Africa's trade and financial linkage with the rest of the world is a curse, especially in light of the dwindling level of domestic savings. It is also a blessing in the sense of being somewhat insulated from the detrimental impact of the trade and financial markets such as the risks posed by macroeconomic instability and vulnerability. From a policy perspective Africa's orderly integration in the international trade and financial system requires designing appropriate policies to positively influence export growth and financial flows to the continent. Policy makers need to understand the extreme volatility associated with such external market. This requires, among other things, capacity building on the management

of the external sector (trade and finance). This requires export sector development, export diversification, appropriate exchange rate policy, debt management, proper financial regulation and supervision and transparency as well as maintaining a stable macroeconomic environment. The Afreximbank is expected to support such policy across the continent.

The experience of successful exporters shows that partnership with foreign firms is central for the success of exporting. This can be done by encouraging the flow of FDI to Africa by offering incentive to Multinational Corporations both by African countries and its development partners (host countries of such corporations). Much of the preconditions for sustained flows of FDI to Africa rely on the structural transformation of the African economies that will have a positive effect on market size, resource discovery and enabling conditions for high level of growth. Moreover, joint-venture based exploitation of resources is an important area that needs to be explored. The role of the state in bringing export success needs to go beyond policy making to selective state activism. The Afreximbank needs to work towards realizing such policy direction in the continent.

The importance of the world economy to Africa, especially in trade, is significant.[10] However national governments are required to adjust to 'economic reality' and 'market discipline' in order to stimulate exports and promote foreign investment. Certain dangers are ignored, including a 'race to the bottom' as individual countries try to adjust to labour standards, environmental safeguards and tax concessions. Also ignored is the 'fallacy of composition' inherent in the small-country assumption, leading to the over-expansion of commodity supplies and declining prices at the global level. Given the dependence of Africa on few commodities; the dominant effect of trade; the secular deterioration of its terms of trade as well as its volatility, the global market is extremely important for Africa compared to other parts of the world. Economic *perception* is thus as vitally important as economic *reality*. External economic relations need to be examined, therefore as a variable, rather than as a given. Domestic economic events become endogenous to the operation of the global system rather than simply at the behest of policy makers. This shows, on the one hand, how limited the options really are for domestic policymakers in Africa (especially if they act individually and only for short periods) and, on the other, the crucial importance of changing international arrangements – particularly trade and investment rules rather than aid. Africa's insertion into the global system has not been orderly as can be read from its economic history The issue, then, seems to be why Africa has not switched to other export products – manufactures, services or processed raw materials – which offer better growth prospects. However, such a switch requires capital (infrastructure and plant) and skills (or 'human capital') which Africa does not currently possess. Addressing this issue at regional, continental and global level is a policy direction that Afreximbank need to pursue.

What are the lessons for the economic future of Africa?

- First, the African trade and financing problem (which includes the debt problem) is essentially a commodity problem is amply confirmed (see Alemayehu, 2002). Efforts such as debt cancellation will have little lasting effect unless export capacity and prices are raised. The contribution of trade-related financing in which the Afreximbank is engaged is a suitable medium term strategy till the lasting solution is attained.
- Secondly, if an international flow of capital to Africa (such as aid, trade related finance, commercial flows etc) is envisaged, then (a) more of such flows should be channelled towards small export farmers through a strategy of agricultural development so as to promote exports and reduce poverty; and (b) such flows should be accompanied by expansionary policies in order to keep the exchange rate competitive.
- Thirdly, Africa is highly vulnerable to changes in world interest rates, due not to capital market effects but rather to their impact on commodity prices resulting from the activities of speculators. This implies that action can only be taken at an international level as part of the construction of the new 'global financial architecture'.

[10] See Alemayehu (2002) for details on this.

- Fourth, the balance of payment and fiscal deficits of African countries are largely exogenously determined by structure of trade and aid flows, respectively. This has important implications in terms of the need for donors to co-ordinate their actions in order to ensure macroeconomic sustainability, which is a pre-requisite for success in export-led growth, rather than leaving this task to International Financial Institutions (IFIs) alone (Alemayehu, 2002).

These various policy implications imply that trade relations of Africa with the developed countries need to be improved. The question, then, is how? Improved access to northern markets for processed primary commodities, and, in particular, the replacement of the Lome system with improved access to the European and American market (along Everything but Arms of EU and The African Growth and Opportunity Act of the US) as well as the capturing of these rents by African firms would be a first and important step. Commodity price stabilization schemes are currently out of favour, and would require the full co-operation of the major importing translational corporations in order to work at all. However, this is a problem of price volatility around the trend, as well as the declining trend itself. Reducing this volatility would benefit both importers and exporters and thus should not be impossible to achieve through a properly administered buffer stock system. The market mechanism alone cannot achieve this result since hedging ranges are so short, so this would have to be a form of public intervention.

However, the long-term downward direction of the terms of trade is difficult. It would not matter so much if volume was increasing fast enough to raise the income terms of trade (as is happening with labour-intensive manufactures), but this is not, in fact, the case. The market for tropical commodities is oligopolistic and riddled with restrictive practices, e.g., sugar and cotton in the US, bananas and coffee in Europe. Therefore, a producer's cartel may be the only theoretically viable solution. However, in spite of the recent success of OPEC in driving up oil prices, Africa is unlikely to be able to organize such a cartel in view of the worldwide competition in those commodities. Africa, thus, needs to change the mix (or at the very least upgrade the quality) of its primary export products in order to compete within the foreseeable future. This requires investment and joint ventures with foreign companies, domestic investors such as firms, flight capital and households. More than savings, risk is the main problem here, since there is plenty of capital held overseas and also plenty of liquidity within the banking system. However, this cannot be undertaken by each African country in isolation, but rather requires an international (and also regional) agreement on investment rules and stabilization of commodity prices; in other words, the *orderly* insertion of Africa into the global market. Thus the design and implementation of trade polices requires taking this issues on board. Afreximbank could potentially play a significant role in addressing such challenges of the external sector in Africa.

The positive effect of trade liberalization can be enhanced if it is acted on at the right time, or is supported by basic macro stability policies (e.g. Winters, Alan, Neil McCulloch and Andrew McKay, 2002; Bhagwati and Srinivasan, 2002, in Alemayehu 2005). Some desirable trade reforms could turn out to have a maligning effect on society if implemented at the wrong time. Some measures of trade liberalization could be inflationary, if not accompanied by appropriate macro-stabilization policies, which in most cases hurt the poor. Thus, it is important to decide the appropriate timing of the trade reform to minimize the adverse effect on the poor. Integrating poverty diagnostics with trade policies can minimize the effect of trade policies on the poor. Strengthening and creating institutions that ensure the rent from the exporting sector is distributed optimally is also a pre-requisite to sustain trade policies and ensuring export success, as recent economic history of successful exporters such as Botswana shows. The Afreximbank thus need to take such policy direction as part of its macro policy target.

Ownership of policies, such as trade policies, by African countries is crucial. In order to realize the goals of the export development strategies, they must be designed in a way that ensures the

sustainability of recent gains in the social (such as poverty reduction) and macroeconomic sphere and integrating them with trade policy issues. This will take the form of:

i. Ensuring political stability and designing peaceful mechanism of conflict resolution for conflict-prone economies
ii. Pursuing the goal of macroeconomic stability by emphasizing the saving-investment-export nexus, exchange rate alignment, and policy ownership
iii. Investing in human capital formation, physical infrastructure and institution building,
iv. Addressing major structural problems of countries through diversification, and transiting form aid-dependency.
v. And encouraging the government to work on national firm creation, the emergence of a managerial class, efficient bureaucracy and cadre of entrepreneurs.

Finally, despite the general similarity in the pattern of trade and finance among African countries, it is essential to underscore that each country is unique in its own way. Each country has its own political, structural, institutional and historical features that distinguish it from others. This underscores the need to make trade and industrial polices, as the case of Taiwan and Korea shows, tailored made to suit each African country's uniqueness. This has to be the policy direction that should be pursued by Afreximbank and distinguish it from policies of other international financial institutions such as the World Bank and IMF which pursued one-fits-all policies in Africa.

Corporate Policy Direction

The two strategic plans of the Afreximbank (Afreximbank, 1996, 2000) offer an articulated corporate plans, challenges and prospects for the bank as well as targets of the bank. Thus, the corporate policy directions noted below are meant to emphasis some issues not well articulated in those documents. I deliberately left details of the corporate strategy to those documents to avoid unnecessary repetition here. The implementation of the bank's strategic plan as detailed in the strategic plan document is part of the corporate strategy that needs to be pursued vigorously. Readers are also advised to refer to those documents for detailed corporate policy direction.

As the feasibility study of Afreximbank shows African countries do face major constraint in trade finance. This, among other things, has a negative effect on the volume of the continent's trade. This feasibility study also noted that cost of credit is generally high (about 15 percent of the value of imports compared to 1.5 to 2 percent general international standard) for African countries; Africans also pay a margin on trade credit of about 3 percentage points over LIBOR; import cost are generally high for African countries (cereal imports premium being 5-7 percent above the average world market price for a ton); the premium for iron and still import from France being about 20-30 percent (Afreximbank, 1992). Moreover, most foreign suppliers prefer cash settlements, advance payments or sight letter of credit from African importers. Such financing problems are aggravated by institutional problems (such as weak or non-existent of national credit institutions, institutional mechanism to address the trade-finance needs of the growing intra-Africa trade) found in many of these economies (Afreximbank, 1992). The Afreximbank need to direct its programs and facilities to address these trade finance related problems. Bringing down the terms of credit and price of imports of Africa to an international standard could be taken as the corporate targets of the bank.

Trade finance to Africa declined between 1998 and 2001 and recovered in 2003. This recovery largely took the form of syndicated loans with average spread generally being high and the terms being unfavorable to Africa. Moreover, most of such syndicated loans are serving the extractive industries such as the oil sector or other primary commodity exports. It is also instructive to note that import financing was virtually non-existent (See Afreximbank 2004) despite the importance of such imports in export sector development of the Asian successful exporting economies. The recovery in syndicated loans to Africa that is partly explained by the surge in oil export related financing and

privatization of telecoms, seems to offer Afreximbank a recognition that could be attributed to its relative local knowledge, prudence of its operating model and benefits of its preferred creditor status (see Afreximbank, 2004). It is on these advantages the bank needs to build its future strategy. Its strategy needs also to take into account the dismantling of commodity boards following privatization in some countries which adversely affected commodity export, export implications of recurrent drought and conflict, the opportunity offered by the new impetus for regional integration across the continent and the gradual return of international banks to Africa (see Afreximbank, 2004).

Given the importance of partnership with foreign firms and provision of low interest loans to exporting firms in successful exporting countries, the Afreximbank could encourage African countries to pursue such policy. With regard to the former the bank may engage in bridging the information gap between African and foreign firms. With regard to the latter, however, from the bank's perspective a joint venture with individual countries with regard to provision of low interest loan for exports where the spread between the market rate and the export- incentive compatible rate is financed by the African governments is an innovative area that the bank may sell to African countries. The bank may design instruments applicable for different stages of exporting based on export performance of firms and optimal risk sharing arrangement with them. For instance, during the early years of Taiwan's policy the interest rate was 6 percent for loans returned in foreign currency and 11.88 for loans returned in local currency. This policy was initially applicable for products that were ready for shipment but latter extended to all stages of production and was provided based on letter of cried (LC). This is an important area that the bank may explore at length.

Finally, Afreximbank may also need to extend its 'infrastructure and service financing program', to cover the tourism industry which is rapidly growing and has a great potential in generating foreign exchange at relatively low foreign exchange cost.

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