



Trade Hot Topics

Trading with the Rising South: Challenges and Opportunities for Sub-Saharan Africa

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Background

The rise of developing countries in the global economy has been one of the defining features of globalisation in recent times. Along with their rapid economic growth, trade between developing countries, or the so called South–South trade, has seen a phenomenal rise. Although the relative economic significance of Sub-Saharan Africa remains very small, since the mid-1990s they have also demonstrated an impressive growth record of overall economic activities in general, and trade in goods in particular. The growth momentum in large developing countries has resulted in increased demand for exports from, along with investment and other technical assistance flows to, Sub-Saharan Africa. This issue of *Commonwealth Trade Hot Topics* while highlighting some stylised facts of the nature of their participation in South–South trade, provides some issues for the way forward for Sub-Saharan Africa in achieving structural transformation of their economies.

The rise of the global South

The world economy has witnessed an unprecedented growth of developing countries with their share in global output doubling from

about 20 per cent in the early 2000s to 40 per cent in 2013 (Figure 1). This has also been reflected in their rapidly expanding export volume. In 1990, the combined merchandise exports from all

Figure 1: Share in global GDP

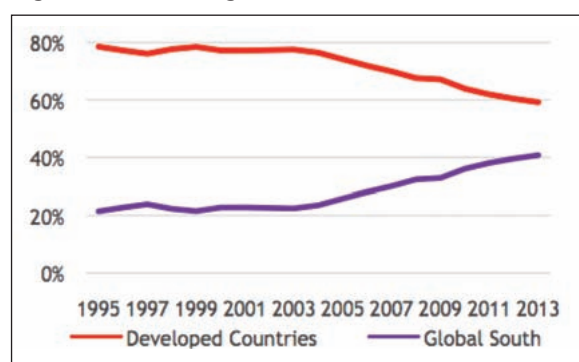
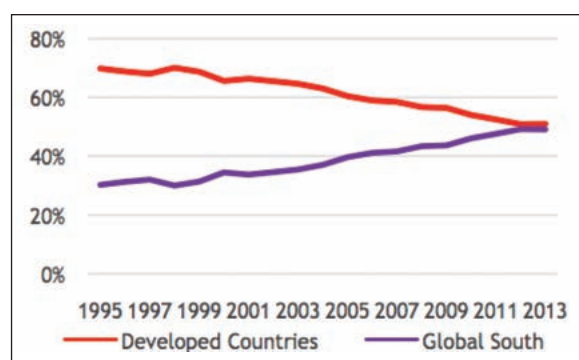


Figure 2: Share in global merchandise exports



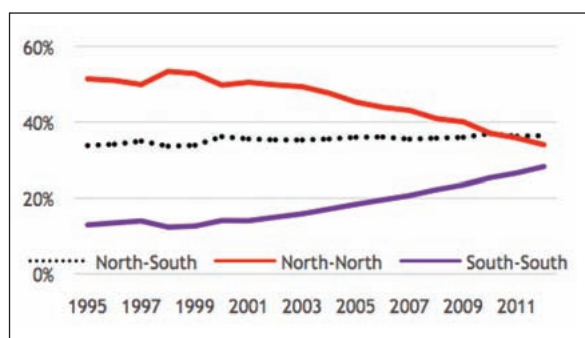
Source: Authors' estimates using UNCTADStat data.

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developing countries stood at US\$850 billion, which reached US\$2 trillion over the next decade and then US\$9 trillion in 2012. Developing economies' combined share in global export trade is now almost 50 per cent (Figure 2). Almost all regions of the South have continued to experience trade and economic growth despite the 2008 global financial crisis and the subsequent recessions in Western developed countries.

An important feature of the rise of the global South is that the trade between developing countries has expanded much faster: the average annual growth of South–South trade since 2000 has been 17 per cent against the world trade growth rate of 10 per cent. This has caused the relative significance of the trade between developed countries (i.e. the North–North trade) to decline from about 53 per cent in the late 1990s to just 34 per cent in 2012 (Figure 3).

Figure 3: Global trade by region



Source: Authors' estimates using UNCTADStat data.

The rise of South–South trade has been mainly driven by the growth in five large developing countries, namely, Brazil, Russia, India, China and South Africa (known as BRICS nations), whose trade accounts for over 65 per cent of all trade involving the developing countries. With a combined GDP of US\$15.8 trillion in 2013, the BRICS countries contributed 21 per cent of the world's GDP and 18 per cent of global exports. According to available projections, the group of largest seven emerging economies (China, India, Brazil, Russia, Indonesia, Mexico and Turkey) is predicted to overtake the group of current G7 economies (France, Germany, Italy, Japan, United Kingdom, USA, and Canada) by 2020 in terms of gross domestic outputs measured in purchasing power parity exchange rates.

Sub-Saharan Africa in global and South–South trade

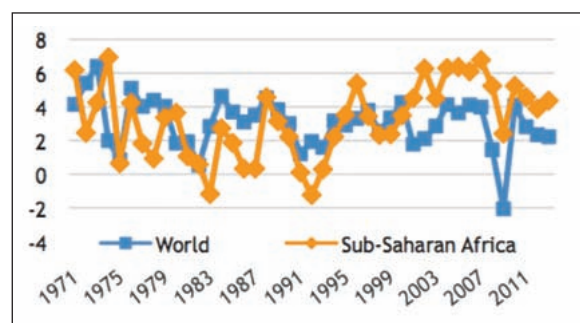
Sub-Saharan Africa (SSA) managed to post robust economic growth over the past two decades.

Particularly during the 2000s, its combined GDP grew at an annual average rate of more than 5 per cent. Over the same period its compound annual growth of per capita GDP was 3.36 per cent, which was more than double that of the world per capita output. Despite the global economic crisis, it maintained quite an impressive output growth rate. Indeed, for the first time since 1970, SSA has outpaced overall global economic performance during a period when the world economy has experienced a downturn (Figure 4).

Table 1: Compound annual growth of GDP per capita (at constant 2005 prices)

	Compound annual growth (%)		
	1970-2000	1970-2012	2000-2012
World	1.52	1.48	1.36
Developing economies	2.57	2.57	4.22
Sub-Saharan Africa (excluding South Africa)	-0.32	0.71	3.36

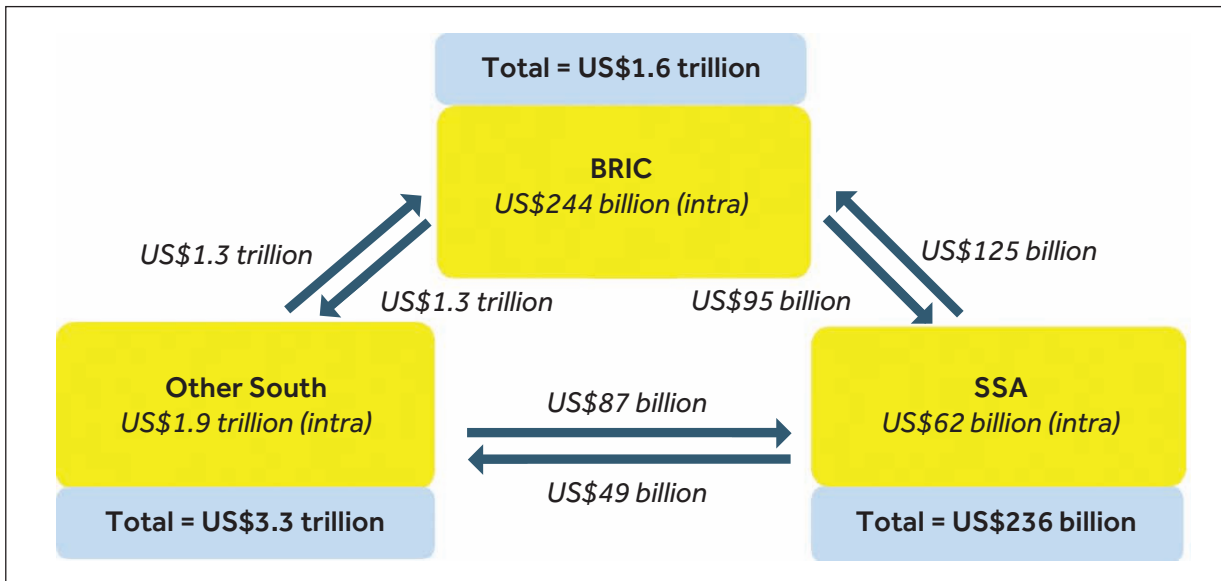
Figure 4: Real GDP growth rates (%): World and Sub-Saharan Africa



SSA has also demonstrated a robust trade performance as its exports grew from US\$25 billion in 1990 to US\$437 billion in 2012. Commodity price hikes and increasing demand for fuels and raw materials, primarily from two large developing countries, China and India, have been important contributors to this growth.

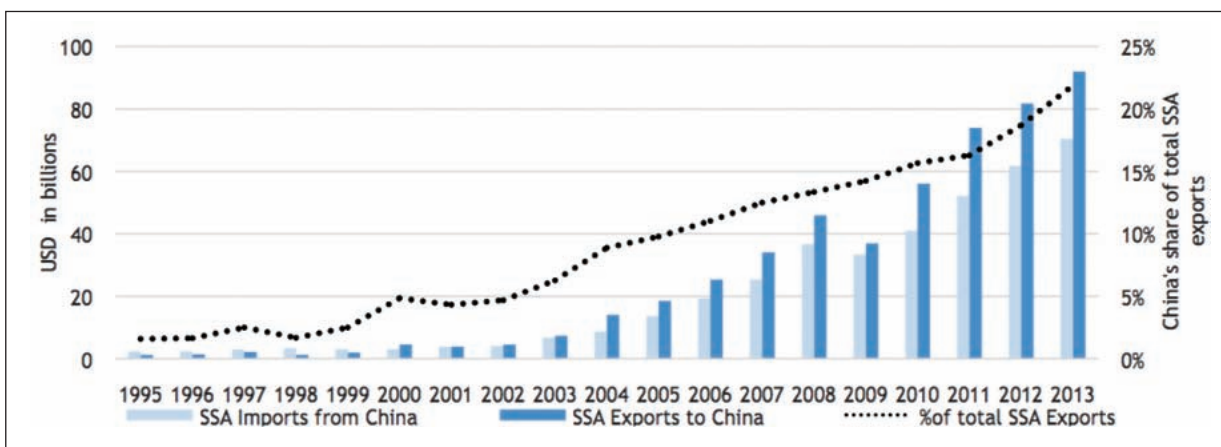
Since 2000, intra-SSA exports and SSA's exports to the rest of the South have had annual average growth rates of 14 and 24 per cent respectively. SSA's exports to the North have grown but at a lower annual average of 13 per cent. Currently, close to 55 per cent of SSA's goods exports are destined to developing countries. In 2012, SSA's exports to traditional developed countries were

Figure 5: South-South export flows 2012



Source: Authors' estimates using UNCTADStat data.

Figure 6: China's trade with Sub-Saharan Africa



Source: Authors' estimates using UNCTADStat data.

US\$200 billion, while the comparable figure for developing countries stood at US\$236 billion.¹ Of this total to the South, US\$125 billion (i.e. 53%) was due to BRIC, US\$62 billion (26%) was intra-SSA exports, and US\$49 billion (21%) went to other Southern countries (Figure 6). Although SSA continues to increase its trade with the South at a relatively high rate, its actual share of all Southern countries' exports remains small, which is estimated at 4.6 per cent for 2012. This is reflective of the fact that trade growth has been widespread for developing countries.

With the rise of developing countries, significant changes have taken place in terms of relative significance of SSA's export destinations. Just over the period 2000-12, the share of developed countries accounting for all goods exported from SSA has declined from 65 per cent to 46 per cent. The share of China on the other hand has seen some

dramatic rise from just 5 per cent to 19 per cent. India's share has also risen considerably, from 4 per cent to 7 per cent. It is interesting to find that the importance of intra-SSA trade is maintained, albeit registering a small rise by 1 percentage point to 14 per cent.² From a very small traded volume of less than US\$10 billion in 2000, China has now become SSA's largest single trading partner with US\$160 billion worth of goods trade in 2013 (Figure 6).

¹ Because of inconsistencies observed in data used from different sources, for example, UNCOMTRADE and UNCTADStat, trade figures in this section have been consistently computed by the authors using UNCTADStat source. The authors' calculations are consistent in the sense that aggregate SSA exports as obtained by summing exports of individual countries can be fully disaggregated into different sources: intra-SSA, SSA to BRIC, SSA to other South, and SSA to developed countries.

² Almost similar changes are also observed in SSA import sources, in which developed countries' share has fallen from 53 per cent to 38 per cent as against China's rising share (from 4% to 15%).

Major trade issues for SSA in South–South trade

The rise of the global South has important implications for SSA. For SSA countries, trade with fast growing developing countries offers opportunities for specialisation, efficiency gains, export market diversification, and investment flows. In response to the rise of the BRIC nations, there has been a recent resurgence in interest on South–South trade and co-operation as a vehicle for promoting trade-led development in the weaker economies. Large developing countries now provide improved market access to the least developed countries (LDCs), a group of 48 countries of which 34 are in Sub-Saharan Africa. For example, China gives non-reciprocal duty-free access to imports from 28 countries in Africa, while India provides tariff-free access for most exports from LDCs in SSA. Over time, many emerging developing countries have also become important sources of technical and financial assistance to many LDCs and SSA.

As can be inferred from the above, Southern countries have already become very important trade partners and sources of growth for SSA, being spectacularly evident in the wake of the recent post-financial crisis economic slowdown in developed countries. At present there are 38 SSA countries that have developing countries as principal trade partners, with more than 50 per cent of their trade (exports and imports) occurring with the global South.

Nevertheless, there are some concerns for many SSA countries arising from the unfolding trade relations with the emerging South. First of all, there is evidence to suggest that the increased trade flows have bypassed a large number of SSA countries. At least six countries have seen their share in South–South trade decline since 1995. For another 35 countries, the share and growth of trade involving Southern partners remain insignificant. There are just five countries that are clearly increasing their share of South–South trade: Angola, Democratic Republic of Congo, Republic of Congo, Ghana, and Mozambique. Indeed, as few as 10 countries currently account for more than 80 per cent of SSA's exports to the South.

The nature of participation in South–South trade has been such that SSA countries predominantly export primary commodities to the global South. This commodity concentration is excessively high

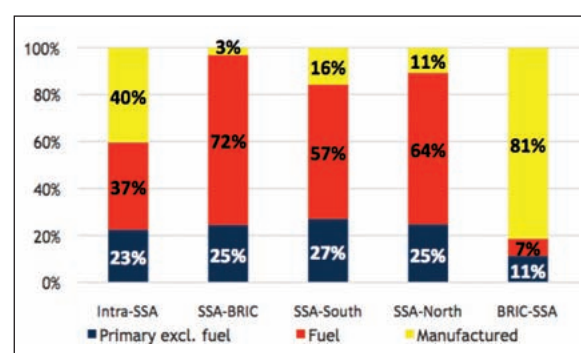
Table 2. Major SSA exporters to global South (average 2010–2012)

Country	% of SSA Exports
South Africa	26.4%
Nigeria	19.6%
Angola	19.3%
Sudan	2.8%
Zambia	2.6%
Congo	2.5%
Ghana	2.4%
D.R.Congo	2.3%
Côte d'Ivoire	2.2%
Kenya	1.8%
Total	82.0%

Source: Authors' estimates using UNCTADStat data.

in the export to large developing countries. Only 3 per cent of all SSA exports to Brazil, Russia, India and China are manufactured goods (Figure 7). The comparable figure for trading with developed countries is 11 per cent. By comparison the intra-SSA export composition appears to be much more diversified, with manufacturing accounting for 40 per cent of exports. Therefore, the increased demand for fuels and industrial raw materials from rapidly growing large developing countries has resulted in export growth of a select few primary sectors and only resource-rich SSA countries have been the major beneficiaries.

Figure 7: Export composition by different groups



While SSA is a major source of raw materials, BRIC countries predominantly supply manufactured goods. As high as 81 per cent of all imports from BRIC to SSA are manufacturing in nature, valued at US\$77 billion in 2012 (33% of all manufactured imports to SSA). This includes items ranging from low-skilled labour intensive products to capital-intensive goods such as machinery, vehicles and pharmaceutical products. There has been some concern that the competition from cheap

manufactured imports sourced from the South has resulted in slower or hindered development of SSA's own manufacturing sector.

Investment, aid and technical assistance in South–South co-operation

Investment is a key driver for economic development and structural transformation, and Southern countries are now becoming increasingly important as development partners. According to one UNCTAD estimate of greenfield investment data, the BRICS' share in foreign direct investment (FDI) in Africa has reached 25 per cent. However, it is difficult to get a comprehensive picture of the nature of investment projects. There is some suggestion that investment flows are being linked to services and manufacturing activities, but most analysts seem to argue that they are mostly related to primary sectors in a few natural resource-rich countries. For example, Chinese investment is thought to be heavily concentrated in oil, infrastructure construction, and mining, with South Africa, Nigeria, Sudan, Angola and Zambia being important beneficiaries. Indian investment has largely been concentrated in Mauritius and a few other East African countries, while among others Senegal and Sudan have also benefited. Starting from a very low base, Russian investment is currently focusing on raw material supplies and accessing local markets. Similarly, it is also reported that the so far limited Brazilian investment is rising namely in African ethanol industry in Angola, Ghana and Mozambique, and in the local services market (e.g. housing projects in Angola and Mozambique).⁴

China and other large developing countries have also become important sources of aid. However, there is limited information on the magnitude and nature of the aid available. According to the data gathered on known projects, Chinese aid commitments in Africa over the past decade could be as high as US\$75 billion. Top recipients of this aid are known to be Angola, Democratic Republic of Congo, Nigeria, Sudan and Zambia. There have been reports that in many African states China has now become the largest source of bilateral aid. India's aid has been provided to Nigeria and Sudan, as well as some West African countries. The aid from Chinese and Indian sources, reported to be more in the form of concessional loans rather than grants, is concentrated in infrastructure or projects related to primary sector development for sourcing raw materials. A significant component of

the aid is characterised by being highly tied in nature and is used as subsidies to the projects of commercial interests.⁵

Way forward for Sub-Saharan Africa

One important issue for SSA in the context of increasing engagement with the relatively advanced Southern partners is to consider the role of trade in development. While the current primary export surges have provided the much needed growth in the region, achieving fundamental development objectives to ensure sustained productive economic activities will require strategic and proactive policy choices. While economic development would imply countries progressing from primary and traditional activities to more productive manufacturing and modern services sectors, in an overwhelming majority of SSA states such a transformation mechanism has not yet had any promising start. Rather, over the past two decades the share of manufacturing in total value added in Africa has declined from 13 per cent to 11 per cent. There is, therefore, the apprehension that the current structure of South–South trade, as elucidated above, will not help SSA achieve economic and export diversification.

Sub-Saharan Africa's previous attempt to break away from the predominantly primary sector oriented static comparative advantage to areas of dynamic comparative advantage came to an end with the implementation of structural adjustment policy reforms. This essentially brought the emphasis back on traditional sources of static comparative advantage, which is manifested in the nature of current trading engagement with the South. As the Washington Consensus has failed to generate growth and structural transformation, so has the doctrine of widespread and blanket protectionism been rejected as a means for achieving them. It is now becoming increasingly clear that in the absence of judicious policy choices, SSA will be trapped into an international specialisation, as largely suppliers of natural resources, which has important consequences.

³ There are 12 SSA countries that have 20 per cent or more of their trade (exports and imports) with China.

⁴ Information on the investment by large developing countries is sourced from UNCTAD (2013), 'The Rise of BRICS and FDI in Africa', *Global Investment Trends Monitor*, unedited version, dated 25 March 2013.

⁵ For an excellent discussion, see Morrissey, O. and Zgou, E. (2011), 'The Impact of China and India on Sub-Saharan Africa: Opportunities, Challenges and Policies', Commonwealth Secretariat: London.

Relatively recent empirical assessments demonstrate that what countries export and how they specialise matter for their future growth, and economic development requires diversification and not specialisation as such.⁶ It has also been shown that countries specialising in such areas as minerals and natural resource-based products will find it difficult to diversify as these sectors have limited linkages in the economy and very little spillover effects.⁷ Sophisticated products (e.g. metal, machinery, and chemicals) have greatest linkages while products such as garments, textiles, and electronics have their own clusters with somewhat lower linkages. However, export items of a vast majority of SSA, for example, tropical agriculture, mining and oil, forest products, cereals and coffee, are situated almost in isolation. Since countries can move relatively easily through the product space by developing goods similar to those they already produce, SSA will find it harder extending their product variety. Considering the experiences of Chile and South Korea, it has been demonstrated that both countries had similar levels of development. But as South Korea started producing products with greater linkages, it could extend its sophisticated product lines faster than Chile. Therefore, an important lesson is: with a cluster of products in close proximity a natural structural transformation is possible, but with a product set involving largely primary commodities countries would need to make much 'longer jumps' to break into activities with significant linkages.

Now the question is if SSA has enough policy space to support breaking into manufacturing. In some cases, trade preferences, despite their being subject to erosion due to widespread multilateral and regional trade liberalisation, can be used to provide incentives in certain export sectors. Tariff preferences for many African countries under AGOA and EU-EBA preferential schemes particularly for such products as textiles and apparels are still quite significant. These are the sectors where SSA can benefit from export-oriented investment flows from BRICS. It is also important to note that tariffs in many large and fast growing developing countries are still relatively high. Sub-Saharan Africa can attract foreign investment both from developed and developing countries to take advantage of these markets under South–South trade preferential mechanism. In certain cases, this can further be strengthened by making use of suitably designed investment incentive regimes.

Also, the concept of manufacturing production processes has changed with the rise of global value chains (GVCs) in which countries can specialise on certain fragmented tasks within the same final product. Given SSA's being the source of raw materials, they are already part of the GVCs. But they need to move up to specialise in certain manufacturing activities for which many large developing countries can be important drivers. Developing regional supply chains can also be another important way of promoting manufacturing activities. The significance of manufacturing in intra-SSA trade shows promising prospects in this respect. A Commonwealth Secretariat-UNCTAD joint project has provided evidence for potential regional supply chains for Sub-Saharan Africa in such sectors as leather and agro-processing.

SSA should also take advantage of the growth that is taking place due to exports of commodities and mineral resources. There are still huge untapped natural resources, which in combination with their better utilisation can generate fiscal space to trigger judicious policy-driven structural transformation.

The above will however require articulating a pragmatic and analytical trade and industrial policy regime that will address all the relevant issues consistently. The purpose of it will not be to merely provide tariff protection or other fiscal and financial incentives, but also deal with other fundamental policy issues, for example, tackling the Dutch disease syndrome due to natural resource booms, addressing costs of doing business, etc. A part of the strategy will also be proactive engagement with developing country partners so that along with investment in natural resource sectors, priorities are set for developing certain manufacturing activities with linkage effects and other capacity-building support.

Conclusion

While South–South trade and co-operation has been a longstanding development issue, never in the past could it be more relevant and prominent than it is now. The rapidly rising relative

⁶ Rodrik, D (2006), 'Industrial Development: Stylized Facts and Policies', <http://www.hks.harvard.edu/fs/drodrik/Research%20papers/industrial%20development.pdf>. See also Hausmann, R, Hwang, J and Rodrik, D (2007), 'What You Export Matters', *Journal of Economic Growth*, Vol. 12, pp. 1-25.

⁷ This discussion is based on Hidalgo, C A, Klinger, B, Barabási, A-L and Hausmann, R (2007), 'The Product Space Conditions the Development of Nations', *Science*, Vol. 317, 27 July 2007.

significance of a number of large developing economies in the backdrop of economic slowdown in the advanced economies provides an opportune moment to have a fresh look at the ongoing engagement between developing countries and assess the development interest of Sub-Saharan Africa in a right context. Despite having benefited from the rise of the global South, the unfolding

international specialisation that makes SSA suppliers of primary commodities and importers of manufacturing products causes some concern. The scope of structural transformation in Africa needs to be better assessed and supported with a comprehensive and coherent policy mechanism that would also stipulate a proactive engagement with the emerging Southern partners.

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