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The Global Shift in Wealth: What does it mean for African LDCs?

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Executive Statement

"The Global Shift in Wealth" describes the structural transformation of the global economy in which the world's economic centre of gravity has moved towards the east and south, from OECD members to emerging economies. African LDCs are at the centre of this shift. In 2009 emerging partners have overtaken traditional partners in trade with African LDCs. Manufactured exports have followed this shift and go to 52 percent to emerging partners. FDI is still largely provided by traditional partners but will likely follow the trend of trade.

http://pogoprinciple.wordpress.com

So what does all this mean for policy makers?

- Increase regional integration and coordination to strengthen the bargaining power of African LDCs in trade negotiations vis-à-vis their emerging partners; and
- Be aware of the complementarities between emerging and traditional partners and make them the basis of broad engagement strategies.
- Expand South-South peer learning to help design policy based on successful experiences in the South and attract market-seeking FDI.

The Global Shift in Wealth and African LDCs

"The Global Shift in Wealth" is the term coined by the OECD Development Centre in its 2010 Perspectives on Global Development Report (PGD), describing the tremendous "structural transformation of the global economy in which the world's economic centre of gravity has moved towards the east and

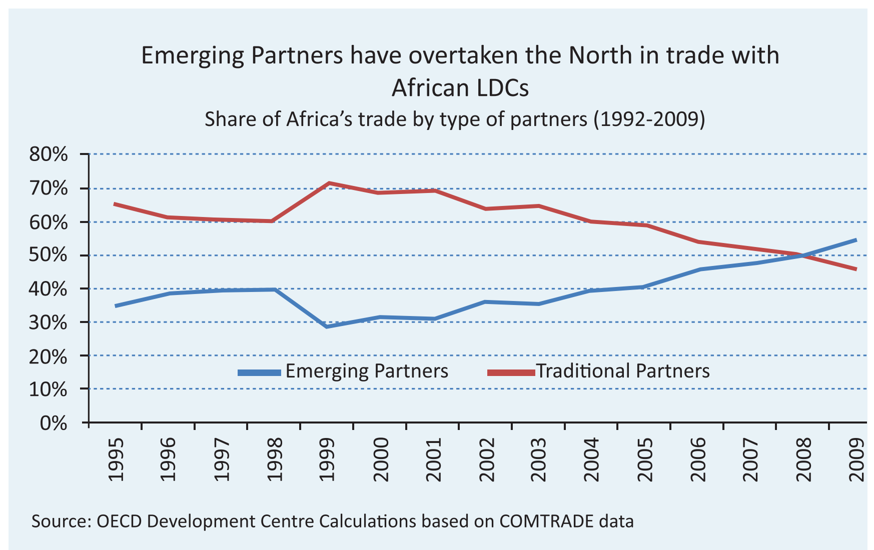
south, from OECD members to emerging economies." The 2000s have been the first decade of strong growth across the developing world. For the first time since the 1970s we could witness a trend towards strong convergence in per capita incomes with the high-income countries. "The number of converging countries (that is, countries doubling the average per capita growth of the high-income OECD countries) more than quintupled during this period (from 12 to 65), and the number of poor countries more than halved (from 55 to 25)."

The PGD 2010 identifies three main dynamics, underlying this global shift in wealth: "First, with the opening of the formerly closed large economies of China, India and the former Soviet Union, an additional 1.5 billion workers joined the open market-oriented economy in the 1990s. This reduced the cost of a range of traded goods and services, and made the take-off possible in a number of converging countries, principally in Asia. But it also led to a global downward pressure on wages, especially for low-skilled labour. Second, growth in the converging countries boosted demand for many commodities, particularly fossil fuels and industrial metals, transferring wealth to commodity exporters and bringing an immediate boost to growth across Africa, the Americas and the Middle East. Third, many converging countries moved from being net debtors to net creditors, keeping global interest rates lower than they might otherwise have been."

For Africa the global shift in wealth means foremost a new set of opportunities in the form of increased demand for African exports, more competition among imported products and more investment capital in search of lucrative locations. But it also presents challenges in the near term: low-skilled labour is cheap and abundant at the global level and many countries in Asia and Latin America offer better business conditions than Africa. Thus, most investors would prefer to locate their production chains in Asia or Latin America and not Africa.

The 2011 African Economic Outlook by the OECD Development Centre, African Development Bank, UNDP and the UN Economic Commission for Africa takes a closer look at Africa's emerging partners and the opportunities and challenges they present for the continent. Africa's overall trade almost tripled over the last decade from USD 246 billion in 2000 to USD 673 billion 2009. Yet its trade with emerging partners, i.e. those countries that were not members of the OECD DAC at the beginning of the decade, more than quadrupled during the same period and accounted for 39 percent in 2009.

This trend of large increases in trade with developing country partners is not limited to Africa's middle income countries. To the contrary, it is even more pronounced for African LDCs, which saw their trade increase from USD billion 30 in 2000 to USD 85 billion in 2009, of which emerging partners accounted for USD 13 billion and USD 53 billion respectively. Thus, by 2009 emerging partners had overtaken the traditional partners in the North and accounted for 54 percent of African LDCs overall trade.



Taking a closer look at who these partners of African LDCs are, reveals China in the lead with 39 percent of the trading volume of African LDCs with emerging partners, followed by Korea with 16 percent, India with 11 percent and Brazil and Turkey with 3 percent each. These shares attest to the fact that shifting wealth is a truly global phenomenon: Although China's is the largest single emerging partner for African LDC, it is outweighed by the sum of the other emerging partners, which taken together, are even more important and account for 61 percent of African LDCs trade with emerging partners.

In foreign direct investment the shifting trend has been much slower and the traditional partners of the North continue to provide three quarters of FDI to African countries. Yet this is likely to change over the coming decade for two major reasons: First, investment often follows trade. A decade ago the shares between Northern and Southern partners in trade were similar to what they are in FDI today. Since then economic contacts between Africa and its emerging partners have been extended at a tremendous speed and volume laying the basis for investment relationship. Second, and more importantly, most excess capital in search of investment opportunities can be found in developing countries. In 2008, developing countries were holding USD 4.2 trillion in foreign currency reserves, more than one and a half times the amount held by rich countries.

Yet given the strong pressure on low-skilled labour and simple manufacturing from these emerging partners, is their rise really good news for African LDCs that possess little value adding industry and might be further de-industrialised by this competition? It is. Although a significant share of African LDC's export success has been driven by commodities, manufactured products gained as well. At an overall share of 10% of exports, in 2009 52% of manufactured product exports by African LDCs went to emerging partners, up from 14% in 2000. Thus instead of suffering from de-industrialisation at a large scale, manufacturing in African LDCs followed the dynamics of shifting wealth and found new customers in emerging partner economies.

The picture that emerges is thus one with African LDCs at the center of the global shift in wealth. Emerging countries have become the most important trading partners, including for manufactured exports, a situation that is still several years off for Africa as a whole. Likewise, emerging partners are beginning to be a significant source of investment, opening up new opportunities for infrastructure and private sector growth in African LDCs.

So what does all this mean for policy makers?

Increase regional integration and coordination to strengthen the bargaining power of African LDCs vis-à-vis their emerging partners. Trade and investment relationships with emerging partners will be one of the main engines of growth for African LDCs. This perspective intimately links the future development of African LDCs to the conditions in the global south. Simulations by the OECD Development Centre (PGD 2010) suggest that, were southern countries to reduce their tariffs on southern trade to the levels applied between northern countries, they would secure a global welfare gain of USD 59 billion. This is worth almost twice as much as a similar reduction in tariffs on their trade with the north. The possibility to access some of these gains for African LDCs will depend on their ability to unite and insist on their shared interest vis-à-vis their trading partners. This will require close coordination and further advances in regional integration.

Be aware of the complementarities between emerging and traditional partners and make them the basis of broad engagement strategies. Emerging partners are central to African LDCs, but so are the traditional partners of the North. They still provide the bulk of investment and are very important trading partners. The EU is by far the most important single trading partner with 26 per-

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cent of all trade of African LDCs in 2009. Moreover, traditional partners and emerging partners come with complementary strengths and thus together create a wider policy space for African LDCs. Asked which partners are typically most effective at meeting the development objectives of their country, a majority of respondents to a survey in the 2011 African Economic Outlook identified emerging partners as most effective in infrastructure and innovation and traditional partners in export promotion and governance issues. To make optimal use of these complementarities on offer, policy makers in African LDCs need to be aware of the different strengths of their partners and engage with all of them. A singular focus on single partners would forego the opportunities offered by others.

Expand South-South peer learning to help design policy based on successful experiences in the South and attract market-seeking FDI. The rise of many developing countries over the last 20 years has been remarkable and largely unexpected at the time. Countries like China and India, but also many smaller successful economies that have achieved middle income status like South Africa, Egypt and Botswana have many lessons to teach. An evident example is China's practice of developing industrial clusters around export processing zones, which China is now expanding to Africa. South Africa has been successful in developing a competitive car industry largely based on investments from traditional partners in the OECD and on specific investment policies promoting this sector. African LDCs should actively seek this expertise and promote peer learning and forums for policy dialogue.

Endnote:

[1] This policy brief is an extraction of the paper "Africa's emerging partners" presented at the International workshop on the "Economic Perspectives of Least Developed Countries" held at EPRC Conference Centre, Kampala-Uganda on May 24-26, 2011. The workshop was organized by Economic Policy Research Centre, Makerere Business School and HTW Berlin – University of Applied Sciences.

[2] The opinions expressed herein are those of the author and not attributable to the institution.

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