

OECD POLICY DIALOGUE ON AID FOR TRADE: FROM POLICY TO PRACTICE

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RAPPORTEUR'S REPORT

Capturing the Benefits of Trade--How can Aid help?

This session addressed two recurring challenges facing developing countries: how to create the appropriate policy environment to maximise the benefits from open trade regimes and the steps that can be taken to eliminate bottlenecks to private sector development. Three speakers addressed each challenge.

The Right Policy Environment

The chair began by posing several questions including which domestic factors need to be in place to get the most out of trade reform; what accounts for the fact that some countries are better than others at undertaking irreversible structural adjustments; and, how can aid best improve the domestic policy environment of developing countries? The chair, moreover, pointed to several case studies prepared in the framework of the OECD's Development Centre Policy Coherence for Development project and noted that three of the preliminary findings from them might go some way to answering these questions. First, domestic leadership and political will was found to matter a lot. Ensuring policy coherence within national governments was important too--as were partnerships with domestic and international actors. Finally, working together can help developing countries capitalise on the opportunities created by the world economy, the chair remarked. Based on these case studies, the chair also argued that fears of "Dutch-disease" effects due to the scaling up of aid may be exaggerated. Donors and partner countries should work towards improving co-ordination and aid effectiveness, as agreed in the Paris Declaration.

The first speaker was a chairman of a business association in a LDC. This speaker began by arguing that the perceptions held by the private sector are an important determinant of their level of engagement. Apparently, business people recoil at the terms such as Poverty Reduction Strategy Papers, Donors, and Country-Level Strategies. The emphasis should instead be on wealth and job-creating strategies, collaborating partners, and business participation, respectively. In his country the government spoke to the private sector because certain donors told them to. Moreover, when such dialogues happen there is a tendency for the 20 largest or so companies to get the ear of the government, with small and medium-sized firms excluded. The speaker recommended that dialogue should be conducted with more conviction and inclusiveness.

The shift in international financial institutions' attitude towards private sector development was welcome, he argued. However, in his country some were very suspicious of the profit motive and much needed to be done to change attitudes. Moreover, it was said that donors still did not deliver the right support, despite the enormous leverage that donors are thought to have (they fund 40 percent of the government budget of his country). Aid programmes, including those for Aid for Trade, need to take account of national circumstances and interests. Again private sector engagement was needed here, not least to identify the pressing concerns of business. In his country these concerns included the cost of capital (the speaker reported figures which implied that the real interest rate was approximately 17 percent).

Factors such as these have a direct impact on profitability, on the business environment in general, and on the ability of firms to exploit international commercial opportunities in particular.

The second speaker in this session was an official at a leading international financial institution who drew on his organisation's experience with trade-related aid projects and with aid more generally. He began by noting that being able to describe the elements of a good business environment was easy, however in many cases at least some of those elements were missing. This situation should not lead to paralysis on the part of governments, especially as some reforms can trigger pressure for further reforms, leading potentially to substantial improvements in the business environment over time. However, observing the effectiveness of aid projects in imperfect business environments raises an awkward dilemma. If the environment is fine then aid would not be needed as the private sector would respond to market signals. But if the environment is poor then aid will be less ineffective as the private sector response is likely to be muted. Finding the right package of domestic reforms and external financial support, therefore, is crucial.

This speaker noted that the diversification of exports, a goal of many developing countries, had been shown to be retarded by the number of signatures on official documents needed to export goods and the number of regulatory hoops firms must jump through. Both findings pointed to the need to re-evaluate current trade-related regulations, and that Aid for Trade initiatives can play a useful role in supporting diagnostics, cross-country comparisons and experience sharing, and supporting the implementation of necessary reforms. Taking a different tack, the speaker recognised that sizeable inflows of aid can themselves disrupt economies. In general, the effect of aid inflows on the exchange rate and on exports can be adverse, and one contribution of Aid for Trade projects may be to boost the export base so as to allow more aid overall to be absorbed into an economy. Finally, the speaker argued that any fiscal problems created by trade reform, in particular by lowering tariffs, should be identified early and measures taken to strengthen indirect tax collections.

A representative from a regional development bank was the third speaker in this session. He started by joining others in saying that the DDA needed to be completed and that practical steps should be taken to that end. For many Africans, he argued, the DDA was an invaluable opportunity and one that could do much to reverse the marginalisation of this continent in world trade. Poor infrastructure and declining export capacities were just two causes of Africa's falling share of international trade. External impediments to African trade, such as agricultural subsidies, should be lifted too.

With respect to the Aid for Trade initiative this speaker emphasised that real partnership offered the best form of support. Promoting private sector participation was important in this respect. As many African countries struggled with debt, relief of these burdens could play a useful role too. Tying initiatives to national circumstances would improve aid effectiveness as would investments in human resources. The inefficiency of national infrastructure, in terms of cost, adequacy of cost, efficiency, and speed, needed to be addressed as a priority, especially if a continent like Africa is ever going to reorient itself from export growth towards domestic growth.