

EXECUTIVE SUMMARY

The Aid-for-Trade Initiative has succeeded in raising awareness about the support developing countries, and in particular the least developed, need to overcome the barriers that constrain their ability to benefit from trade expansion and reduce poverty. As a result partner countries are raising the profile of trade in their development strategies and donors are responding by providing increasing resources to build trade capacity – whether in terms of policies, institutions or infrastructure.

This second monitoring report on aid-for-trade documents the success of the Initiative to date. It presents a comprehensive analysis of partner country and donor engagement, trends in aid-for-trade flows and developments related to the current economic crisis. In addition, it highlights the regional dimension of aid for trade and showcases three regional cross border infrastructure projects. Finally, the report provides fact sheets to assess the outcomes and impacts of aid for trade in the developing countries that participated in the monitoring exercise.

The main messages are positive, but the global economic crisis will affect the medium term outlook. Now, more than ever, aid for trade is indispensable for helping suppliers from low income countries build capacity to penetrate global markets. Consequently, aid for trade must remain an essential component of development assistance. The report concludes that maintaining momentum towards the trade expansion and poverty reduction goals of the Initiative requires reinforcing local ownership and advancing the dialogue among stakeholders.

The Aid-for-Trade Initiative has achieved, in a short time, remarkable progress: partner countries are mainstreaming trade in their development strategies and clarifying their needs and priorities; donors are improving aid-for-trade delivery and scaling up resources. In 2007, as was the case in 2006, aid for trade grew by more than 10% in real terms and total new commitments from bilateral and multilateral donors reached USD 25.4 billion, with an additional USD 27.3 billion in non-concessional trade-related financing

The OECD forecasts that world real Gross Domestic Product (GDP) growth will fall to 2.75% this year, while the WTO projects that the volume of world trade will contract by as much as 9%. The global economic recession is evolving rapidly, and low income countries are faced with new challenges, but also opportunities to refocus their development strategies in this changing world economy. The impacts of the crisis on the economic performance of these countries will depend critically on the speed and scale of the international response. This is why the quantity and the quality of aid, including aid for trade, are now more important than ever for economic growth and human welfare.

Donors are on track to meet, or have already met, their 2005 Hong Kong aid-for-trade pledges. The USD 4.3 billion increase in aid for trade was additional and not at the cost of social sector programmes, such as health or education. Based on their indicative forward spending plans, donors project continued growth of aid for trade over the medium term. Furthermore, calculations suggest high disbursements of commitments.

The overall picture is positive...

...but maintaining momentum will be challenging.

Most donors have met their Hong Kong pledges.

Multilaterals are increasingly the preferred delivery channel.

Bilateral donors provided USD 15.8 billion in aid for trade during 2007, well over 60% of total flows, and many disbursed their funds through multilateral agencies. Consequently, multilateral donors tended to allocate a significantly higher share of their sector allocable aid to aid for trade than bilateral donors. Four donors, which are also the largest providers of total ODA (*i.e.* the World Bank, the United States, Japan and the European Commission [EC]) continued to dominate aid-for-trade flows in 2007.

Increasing flows go to low income countries...

Aid-for-trade flows to low income countries are growing faster than to any other income group. Most is spent on addressing infrastructure needs, in particular transport and power, whereas flows to middle income developing countries reflect their priority to build productive capacities, including trade development.

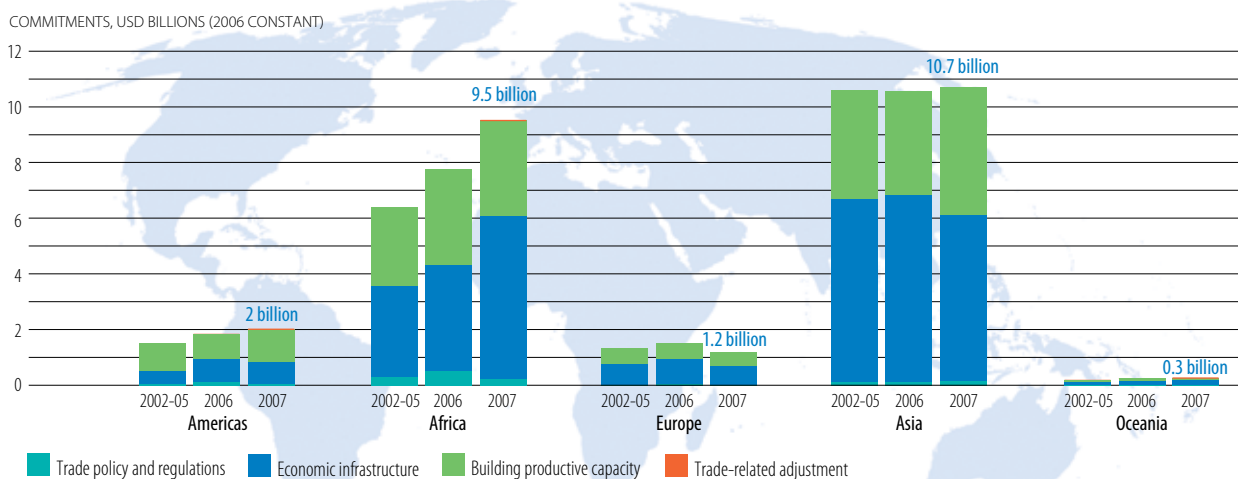
...and Africa...

The largest share of aid for trade goes to Asia, although Africa and especially sub-Saharan Africa are catching up and received most of the additional funds in 2007. With the exception of Europe, other regions (*i.e.* Latin America and the Caribbean, and Oceania) also saw their volumes of aid for trade increase during 2006 and 2007.

Aid for trade: regional and sector distribution

2002-2005 average, 2006, 2007

Commitments, USD billion (2006 constant)



...with stable sector distribution.

Overall, the distribution of aid over the different trade-related categories remained relatively stable. Similar increases were recorded for economic infrastructure and productive capacity building, with strong support for trade development programmes and declining technical assistance for building human and institutional capacity in trade policy and regulations. As a consequence of the economic crisis trade-related structural adjustment programmes, while currently relatively small, are expected to increase over the medium term.

Partner countries are more engaged...

Increasingly, partner countries are becoming more actively involved in the Aid-for-Trade Initiative. In general, they assess as positive the impacts of aid-for-trade programmes and projects on trade performance.

- ...mainstreaming trade...** Nearly all partner countries report having national development strategies and more than half assess that they have fully mainstreamed trade through well-developed operational priorities and action plans. Although independent surveys raise questions about this positive assessment, it is, nevertheless, a clear indication of the growing awareness among partner countries that trade can play a positive role in promoting economic growth and reducing poverty.
- ...and prioritising their needs...** Partner countries identify similar binding constraints. The most common are: i) network infrastructure; ii) competitiveness; iii) export diversification; and iv) trade policy analysis, negotiation and implementation. They increasingly discuss their priorities with donors through a variety of dialogues. Donors note that the success of these dialogues depends critically on the extent to which trade-related priorities have been mainstreamed and operationalised.
- ... but operationalisation remains a challenge.** Without an operational trade-development strategy, it is hard to attract donor support to address specific supply-side constraints. With competing claims on limited resources, especially in times of economic crisis, it will be difficult for donors to sustain increased aid-for-trade flows without an articulated demand from partner countries.
- Donors are responding.** Aid for trade is becoming increasingly important in donor programmes and this momentum is likely to be maintained, or even expanded, over the medium term. For instance, donors are strengthening their capacity to respond to the rising aid-for-trade demand by scaling up aid resources, bolstering in-house expertise and raising awareness among policy-makers and practitioners at headquarters and field levels. Furthermore, donors are aligning around partner countries' procedures and systems, and undertaking more and more joint initiatives as well as triangular co-operation. Partner countries acknowledge these positive trends.
- The regional dimension is gaining momentum...** Partner countries identify common priorities for regional integration, including transport infrastructure, trade facilitation, competitiveness and export diversification, as well as capacity for regional trade negotiations. Donors have also recognised the importance of regional integration and report a rising demand for regional aid for trade. They note their willingness to provide additional support for corresponding activities.
- ... benefitting from increased support and..** In fact, financial support for trade-related global, regional and multi-country programmes – areas which were identified as among the challenges during the first Global Aid-for-Trade Review – doubled since 2005. Most partner countries affirm that they benefit from regional aid for trade and that their binding regional constraints are being addressed.
- ... South-South co-operation...** South-South co-operation has become an important element in the promotion of regional integration initiatives. Four providers of South-South co-operation (*i.e.* Argentina, Brazil, Chile and China) expanded their contribution in this area.¹
- ...but more is needed to enhance the co-ordination.** Working at the regional level, however, poses particular challenges, such as insufficient regional co-operation and concerns about asymmetric costs and benefits. Thus, strengthening regional, human and institutional capacity and improving equitable participation of developing countries in regional initiatives should be a priority to maximise the benefits from these initiatives for regional economic growth and poverty reduction.
- Aid for trade is effective...** Partner countries assess that aid for trade is most effective in the areas of: i) trade policy analysis – negotiation – implementation; ii) trade facilitation; iii) competitiveness; and iv) export diversification. Interestingly, while network infrastructure is identified as one of the priority areas in aid for trade, partner countries did not assess these programmes to be among the most effective.

...but continued progress is needed.

Partner countries noted that progress has been made in the effectiveness of aid for trade, but they also highlighted the need for: i) a stronger donor focus on capacity development; ii) a greater say in the design of aid-for-trade interventions; iii) better predictability of funding; and iv) more extensive use of budget support (or trade sector-wide approaches). These and other aid effectiveness issues are the focus on the Paris Declaration and the Accra Agenda for Action.

The way forward:

The Aid-for-Trade Initiative has succeeded in mobilising more and better aid for trade. It has initiated a dialogue between government ministries, with key national stakeholders and the international aid and trade community. Maintaining momentum, particularly in light of the economic crisis, necessitates, however, a broader dialogue among governments, civil society, private sector and donors. Four priority areas should be addressed:

Aid for trade is worth doing...

First, there is still a need to demonstrate and, more importantly, raise awareness about the potential gains available to developing countries from deepened integration into the global economy. It needs to be shown that aid for trade is worthwhile.

...contributes to wider goals...

Second, stakeholders need to recognise that aid for trade forms part of a larger picture, which encompasses international co-operation, improved policy coherence and a whole-of-government approach to economic development and poverty reduction. It needs to be shown that aid for trade contributes to these wider goals of partner countries.

...has specific targets...

Third, partner countries should identify case-by-case, country-by-country and region-by-region the nature and extent of the binding constraints that are presently preventing them from fully realising the benefits of trade. Aid for trade needs to have identifiable targets.

... and can hit those targets.

Fourth, there needs to be, again, case-by-case, country-by-country and region-by-region a clear identification of how aid for trade will address these constraints. How it will work with, and add value to, initiatives being taken or envisaged by private firms and how it will fit into the evolving framework of multilateral and regional co-operation. It needs to be shown that aid for trade can hit the target.

In conclusion, the Aid-for-Trade Initiative is successful but maintaining momentum requires reinforcing the country and regional component. The Aid for Trade at a Glance fact sheets provide a tool for strengthening on a country-by-country basis the links between demand, response, outcomes of priority programmes and their impact on trade performance. The value of the fact sheets lies in creating incentives, through a sustained dialogue among governments, civil society, private sector and donors, to improve the coherence of aid for trade with overall development strategies around which donors should align their support. In short, the focus on transparency and accountability at the local and regional level will provide incentives for more and better aid for trade.