science & innovation
Department:
Science and Innovation
REPUBLIC OF SOUTH AFRICA

HSRC
Human Sciences
Research Council

POLICY BRIEF

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Trade in intermediates, mission-oriented policies and the African Continental Free Trade Area

Abstract

The fragmentation of production has delivered the phenomenon of production networks that transcend national borders. While the phenomenon of production networks is global, such networks are largely regional and have led to a significant growth of trade in intermediate goods, which has grown in both breadth and depth, notably in the European Union and East Asia. This trade carries potentially beneficial lessons for the nascent African Continental Free Trade Area (AfCFTA) initiative.

Against this plausibility, I call for African governments to intentionally develop capacity and capabilities for participation in the production and assembly of components of defined capital and consumer end-products as a core activity of delivering the AfCFTA. In that respect, I propose the adoption of a mission-orientated policy regime as a critical approach to Africa overcoming numerous contemporary global crises, including financial, climate, health and war challenges that have and will continue to limit the continent's development aspirations. I posit that mission-oriented policies are critical for ensuring that countries worldwide, and Africa especially, strengthen their economic resilience and fully exploit their competitive advantages

Introduction

Through Agenda 2063, and its Africa, Continental Free Trade Area (AfCFTA) programme specifically, African countries seek economic diversification through developing globally competitive manufacturing and services industry bases. Such industrial bases offer economic and social benefits that are evident in industrialised countries in Western Europe, North America, and some parts of Asia including China. Africa needs to emulate this success.

Using the AfCFTA, the African Union seeks to establish globally competitive intra-Africa value chains covering a variety of consumer and capital goods and services. The various regional economic communities (RECs) in the continent are set to anchor this drive. The plan is to gradually decrease tariff and non-tariff barriers to trade, seeking to rachet intra-Africa trade in goods and services. Affirming this drive, the AfCFTA Secretariat has produced the e-Tariff Book, which outlines how members will gradually remove tariffs from 90% of goods as per AfCFTA tariff modalities that are set to eventually allow free access to at least 97% of goods and most services across the African continent . Key in this drive is that these goods and services must carry a large proportion of African value-add. This is the essence of the rules of origin (RoO), which sets criteria and conditions to determine whether goods that are traded between state parties qualify as Africa-originating goods.

Despite all this credible work, there is a paucity of specificity on priority value chains targeted for development. Further, it is not clear what levels of trade countries seek within and between the RECs. Seeking to advise, national (and sub-national) governments and REC secretariats working on industrial development in Africa, I argue that such clarity is critical and necessary to deliver a shared regional focus that efficiently uses scarce resources (financial, human capital, infrastructure, etc.). I posit that this clarity must define the value chains, state the role of each country in the respective chains and set trade targets (volume and monetary), as well as time limits to achieve the set targets – akin to a mission. This is because a defined and shared focus allows for the appropriate allocation of value chain tasks based on prevailing capacities and capabilities that vary between nations. Essentially, this is a call for African countries to contribute intermediate goods and services to final consumer and capital goods made in Africa.

Towards this end, and applying the critical reflection methodology approach, I am calling for the adoption of mission-oriented policies to develop the capacity and capability to manufacture components of both consumer and capital goods and services, as well as assembling these to produce the final products. Fragmented production manifesting as production networks allows for the success of the proposed approach. I maintain that success under this approach is plausible, critically reflecting on the disadvantages and limited success of previous industrialisation approaches including import substitution industrialisation (ISI) and other trade policy regimes approach supported by the Bretton Woods institutions in the 1980s.

Trade in intermediates: the arguments

Proponents of free trade argue that international trade can spur economic growth and development in less developed countries. Simplistically, they posit that trade asserts its positive effect in four ways: (i) it provides capital goods, machinery, raw materials and semi-finished materials, which are key for economic development; (ii) trade enables the spread of technological knowledge, ideas, the importation of know-how, skills, and managerial talent, and entrepreneurship; (iii) it is a vehicle for the international movement of capital especially from the developed to the underdeveloped countries, and (iv) free international trade is the best antimonopoly policy and a guarantee for preserving unrestricted competition (Harbeler, 1988). In this realm and cognisant of related criticisms and practice deviations from these assertions, international trade has developed and benefitted many of today's developed and developing economies.

Notably, contemporary trade is significantly driven by the fragmented production of capital and consumer goods and services. This slicing up of value chains has seen an increased growth of trade in intermediates instead of complete goods and services. Such trade has grown rapidly over the past two decades (United Nations Conference on Trade and Development, 2023). In 2021, it accounted for more than 40% of world trade in goods, exceeding US$ 9 trillion (Ibid). Three fortifying factors inform this production fragmentation: (i) advances in production technology, enabling the industry to slice up the value chain into finer segments (tasks); (ii) innovations in communication and transportation that have contributed to a significant reduction in the cost of service links that are critical to coordinating international operations; and (iii) the growth in the depth and breadth of liberal policies across the world (Li, Song and Zhao, 2018). These factors have jointly driven the fragmentation of production. Notably, Nguyen and Wu (2019) have shown that fragmented production is not confined to countries with similar factors. Instead, countries can be capacitated differently, but can be trading partners in intermediate goods (and services) when the imported inputs in country A are part of exports from countries B, C, D, etc. Specifically, different skills in different countries and observing the principles of comparative advantage, the dispersion of production permits the lowering of marginal production costs (Jones, 2007). In addition, and related to the comparative advantage argument, differences in the incomes enable a production network to exploit the advantages of effective wages adjusted by the quality of labour (Ibid).

Exploiting these factors, the breadth and depth of production networks have grown both globally and regionally. Global production networks are demonstrated in the trade links between Japan, China and the United States of America, and regional links are shown in the cases of trade links in the EU and East Asia covering countries that inter alia China, Indonesia, Malaysia, Singapore, Thailand and the Republic of Korea (Nguyen and Wu, 2019).

Given the foregone, the question is how (developing) countries can initiate and maintain mutually beneficial links of trade in intermediates. I argue that the market forces of supply and demand may not form such links in Africa – not immediately anyway. Accepting this stylised position suggests a need for a deliberate policy and practice stance towards developing the envisaged intra-Africa linkages in goods and services with a large African value-add. Such a deliberate and orchestrated policy stance stands to increase trade complementarity between countries. Presented as an index, trade complementarity measures the extent to which the export profile of one country matches the import profile of another country. Thus, it is an important indicator of prospects for inter-country and thus intra and inter-regional trade. Practically, trade complementarity is amenable to positive adjustments through public policy. Again, accepting this position, I argue a case for the exclusive and specific design and implementation of initiatives that deliberately support complementary industrial activities across borders in Africa. Essentially, this is a call for adopting a mission-oriented policy approach in developing high levels of trade complementarity between countries. The mission-oriented approach is important for providing direction for growth, guiding business expectations about future growth areas, and catalysing activity. i.e., self-discovery by firms, which would otherwise not happen under a laissez-faire approach (Cappellano and Kurowska-Pysz, 2020).

Mission-oriented policies

Mission-oriented policies comprise a plethora of systemic public policies that draw on frontiers of knowledge to attain specific goals using all available tools and technologies (Cappellano and Kurowska-Pysz, 2020). The policies are about strategically and concretely setting and choosing directions of development. In this realm, Mazzucato states that,

> … direction will require different missions, which provide a focusing device for the different actors and sectors to collaborate to concretely achieve it. Thus, missions require picking the willing: those organisations across the economy (in different sectors, including both the public and private sphere) that are 'willing' to engage with a societally relevant mission. (Mazzucato, 2018;805-806)

Thus, mission-oriented policies allow for the use of a diversity of talent and expertise that at first glance appear to be disparate. The oft-cited examples of the use of mission-oriented policies are the Apollo mission of the United States of America whose target was to send men to and from the moon and the Manhattan Project – a secret World War II government programme in which the USA worked to develop atomic weapons before Nazi Germany. Examining these missions reveals a key characteristic of mission-oriented policies as being ambitious in nature and seeking to address issues of societal value. In addition, such policies are also characterised by having clear direction and having targeted, measurable and time-bound targets. The objectives of the AfCFTA while somewhat clear do lack specifically defined and measurable targets in many aspects. This needs attention, hence this brief.

Interrogating the Apollo mission shows that it required investments and innovation outside its seemingly narrow aerospace focus to include multiple sectors that inter alia included food, medicine materials, biological sciences, geology and ICT – each critical for the mission. This shows that mission-oriented policies are cross-sectoral, cross-actor and cross-disciplinary (Ibid). This allows efforts to act and affect issues beyond the science-push instruments and horizontal instruments. Instead, efforts toward the stated targets must use an array of financial and non-financial instruments to promote the accomplishment of a mission across many different sectors, setting concrete directions for the economy and deploying the necessary network of relevant public and private agents (Cappellano and Kurowska-Pysz, 2020). I argue that the AfCFTA is ripe for such an approach.

In practice, the use of mission policies allows for the development of inter-sectoral complementarities in a space with limited political interference and public scrutiny, but with room for organisational and technological experimentation and learning, meritocratic recruiting of management and space for management principles and cultures that recompense or at least not punishing, risk-taking and experimentation (see Karo, 2018). This is important for allowing the trying of many competing solutions and bottom-up experimentation toward meeting the stated targets. In Africa, restricting political interference is important, especially where such interference has disrupted the development of manufacturing and service linkages that serve the primary production industries – mainly mining, oil and gas, as well as agriculture.

Looking at these, and other attributes of mission-oriented approaches, I concluded with two broad recommendations in the next section.

Conclusion: Mission-oriented policies and production networks

Africa needs deliberate actions to rapidly develop its industrial capacity and capabilities to overcome its state of underdevelopment. The mission-oriented approach is a viable and plausible approach to commence tackling the big problem of limited industrialisation (development) in the continent before other approaches are employed. I recommend the following towards that end.

1. ***African governments need to embrace the concept of production networks and the value of trade in components.*** Presently many African countries are pre-occupied with producing whole goods. This is not always possible in some countries because of limited internal human and technological capacities. Critically, this means that the continent is not active in a trade space that in 2021 was worth almost US$4 trillion. Producing and trading in intermediates overcomes many limitations by allowing countries to focus on what they are capable of – the core of the comparative advantage argument. The slicing up of value chains affords even less-capacitated countries a slice of this pie. The African Union and its members need to address this urgently.

2. ***Governments in the respective REC must identify priority regional value chains for collective development, specifying the role of each country in these value chains, and setting temporal and trade targets (volume and pecuniary) for their development.*** This will assist in focusing actions, policies and resources towards specified targets – the essence of mission-oriented approaches.

Notably, the proposed approach carries connotations of 'interfering' with the sovereignty of countries by allocating activities in the proposed value chains. I counter this view by questioning the obsession with the 'perceived' loss of sovereignty with the value of 'lost' development i.e., industrialisation that the continent has foregone to date. I also note and acknowledge that under the proposed approach gains will not be equal initially. This is expected against a background of differences in skill levels, infrastructure (hard and soft), and the value of intermediates to be traded among other dynamics in the respective value chains. However, any developments made to meet the requirements of mission-oriented approaches as proposed stand to benefit other areas where countries can gain greater value than in the initially targeted value chains. This is the essence of spillovers whose positive impact on economic development is always great. What is important is to begin the process of intentional and focused economic diversification.

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