THE CHALLENGE OF THE ASIAN DRIVERS TO SSA DEVELOPMENT STRATEGIES

Raphael Kaplinsky,
Department of Policy and Practice,
The Open University,
Milton Keynes,
U.K.

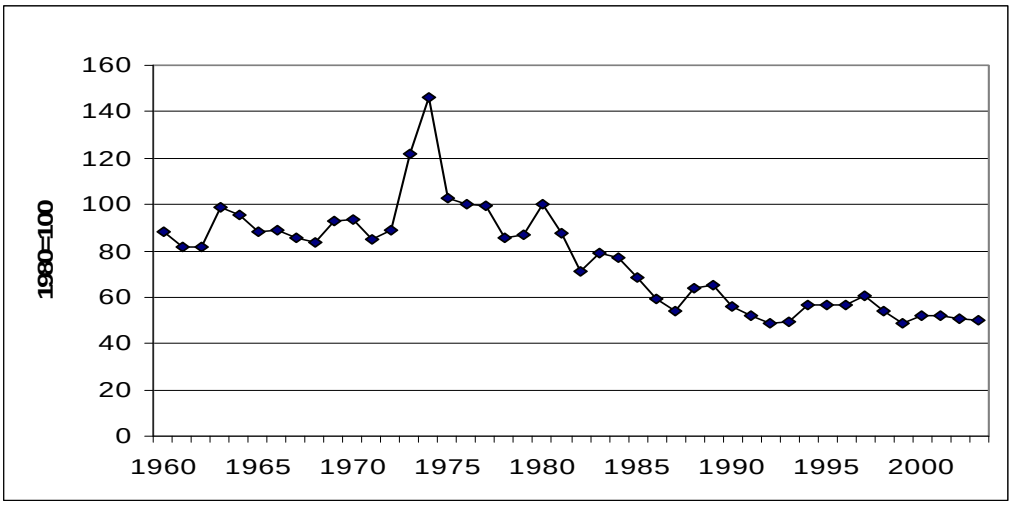
R.Kaplinsky@open.ac.uk

March 2007

1. INDUSTRIALISATION HAS BEEN AT THE CENTRE OF SSA DEVELOPMENT STRATEGIES

Until the 1950s it was widely believed that the terms of trade would turn against manufactures, and in favour of agricultural products. It was Hans Singer, and then Raul Prebisch, who deflated this belief in the early 1950s (Singer, 1950; Prebisch, 1950). They showed that in actual fact, the terms of trade were turning in favour of manufactures and against commodities (Figure 1). In demolishing this orthodoxy, Singer and Prebisch explained these trends in the terms of trade as resulting from a number of factors – the lower income elasticity of demand and higher price elasticity of demand of commodities; the development of synthetic substitutes for primary products; and the fact that commodities were only one of many inputs into final manufactures meant that a proportionate increase in the price of manufactures would have a lower impact on commodity-producer incomes compared to those arising in the production of commodities.

Figure 1: Manufactures-commodities terms of trade, 1960-2004



Source: Drawn from UNCTAD-database

The import of this observation on the terms of trade is that long-run income growth would be fostered by moving out of price-sensitive (and, as Singer-Prebisch observed, price-volatile) primary products into income-elastic and price-inelastic manufactures, in other words by making a strategic commitment towards industrial development. This argument on the terms of trade aligned closely with the emergence of India as an independent economy in 1947. Soon after Independence, India committed itself to a path of industrialisation, heavily influenced by the Soviet drive to industrialisation during the 1930s and 1940s. This commitment to industrialisation was also influenced by the observed reality that countries with high per capita incomes had relatively well-developed industrial sectors. As other low-income economies emerged from colonialism, they too adopted a development strategy focusing on a transition from a primary-based to an industrially-based economy.

From the late 1970s, a twist was given to this widespread strategic commitment to industrialisation. Based on the extraordinary growth-success of Japan and then the Asian Tigers, the strategic agenda was not just a commitment to industrialisation, but to export-oriented industrialisation. This increasingly became a strategic orthodoxy. For example, the World Bank's influential assessment in 2002 of the link between poverty and deepening globalisation forcefully promoted the case for further globalisation, notably through rapid growth in developing country exports of manufactures. Although the Bank recognised that there was some dispute about the evidence, it pulled few punches - "the doubts that one can retain about each individual study threaten to block our view of the overall forest of evidence. Even though no one study has established that openness to trade [in general, and export oriented industrialisation in particular] has unambiguously helped the representative Third World economy, the preponderance of evidence supports this conclusion" (World Bank, 2002: xi).

Heavily influenced by this multilateral- and bilateral-agency policy agenda, and drawing on the successful growth and manufactured export experience of the first generation of Asian NICs, SSA economies have increasingly oriented their long-term growth objectives to a graduation from the export of primary products to the export of manufactures. The demonstration effect of the astonishing recent emergence of China as a major global exporter of manufactures and its relatively successful performance in meeting the $1/day Millennium Development Goal has provided further impetus to this policy consensus.

Mainstream economics provides a theoretical framework to justify outward orientation, particularly with regard to manufactured exports. Productivity growth arises in large part from the division of labour (Smith, 1776) and this is aided by access to large global markets, particularly in the context of technology-induced scale and experience economies (Verdoorn and Moores Laws). Access to new and demanding external markets provides the incentive for innovation (Porter, 1990) and technological change (Clerides, Lach and Tybout, 1998). Notwithstanding frictional adjustments, a dynamic global economy provides the scope for all participants, irrespective of absolute advantage, as long as they specialise in areas of comparative advantage (Ricardo, 1817).

The intellectual rationale for the gains from trade hinges on the validity of Ricardo's invocation to specialise in areas of comparative advantage. However, Ricardo's framework depends crucially on his related assumptions of full employment and immobility of capital. In a world of structural excess capacity and capital mobility, it no longer follows that all countries will necessarily benefit from trade-openness (Kaplinsky, 2005b). The global advance of the two Asian Driver economies of China and India – individually much larger than the Asian forerunners of Japan, Korea, Taiwan, Singapore and Hong Kong, and collectively of even more formidable size – challenges both the small country assumption of trade theory and the assumption of full employment amongst global trading partners (Kaplinsky and Messner, 2007). Given the absolute advantage of the Asian Driver (hereafter AD) economies in

many sectors of relevance to potential SSA exporters, and given the mobility of global producers and buyers searching for least-cost supply, there is constrained space for some other (but of course not all other) participants in the contemporary global economy. SSA manufactured exports – existing and potential - are particularly adversely affected by the AD advance. But so, too, are the manufacturing sectors aligned to the local market.

This paper focuses primarily on SSA's manufactured exports in order to illustrate the challenge posed to SSA's development strategy by the rapid rise of the Chinese economy. Section 2 provides a brief review of SSA's manufacturing performance in general, and its manufactured exports in particular. Section 3 illustrates how (excluding South Africa) SSA's main manufactured exports – clothing - are overwhelmed by Asian (and especially Chinese competition) and explains how this is a reflection of a generalised process in which the global price of manufactures is being undermined by competitive Asian Driver exports. Section 4 contrasts this with the current and likely-prolonged rise in global commodity prices, and in Section 5 the paper identifies SSA economies which gain and lose from these changing terms of trade. This then challenges received wisdom on SSA development strategies which are focused on export oriented manufacturing and the argument which is pursued in Section 6 is to suggest that SSA focuses more on innovation capabilities which span economic sectors. The paper concludes in Section 7 with a brief discussion of the types of policies which are appropriate to meeting this challenge.

2. SSA MANUFACTURED EXPORTS AND THE ASIAN DRIVERS

Overall growth and trade performance

There was a moderate revival in SSA's GDP, industrial and manufacturing growth rates in the early years of the millennium (Table 1). Distinguishing between the first and second half of the period between 1990 (when Structural Adjustment induced liberalisation began to be implemented widely throughout SSA) and 2005, the rate of growth of GDP and industrial value added quickened in the latter period. However, much of this industrial growth can be attributed to a replenishing of infrastructure since the growth of manufacturing value added (MVA) was lower than that of industrial value added, service sector value added and agricultural value added. A second notable conclusion to be drawn from Table 1 is the relatively poor performance of SSA in comparison to that of China and India. With the exception of SSA's agricultural growth relative to that of India, SSA's performance lagged significantly behind that of both China and India across the sectors. However, SSA performed better than the world average in the more recent period in all respects bar growth in MVA.

Table 1: Average Annual Growth of GDP and sectoral value added: SSA, China and India, 1990-97 and 1998-2005

	1990-1997				1998-2005			
	World	**SSA**	**China**	**India**	**World**	**SSA**	**China**	**India**
GDP growth	2.75	1.92	10.56	5.48	2.93	3.70	8.90	6.42
Agricultural value added	1.61	2.53	4.59	2.97	2.34	3.60	3.53	2.35
Industrial value added	2.18	1.28	14.14	6.19	2.22	3.60	9.90	6.23
Manufacturing, value added	-	0.96	11.22	6.63	2.54	2.52	NA	6.05
Services value added	2.96	1.99	9.53	7.21	2.87	3.72	9.60	8.30

Source: Calculated from World Development Indicators (accessed through ESDS in January 2007)

The share of manufacturing in SSA GDP was stable over the period between 1995 and 2005 (Table 2). This ratio was not just lower in absolute terms than in other developing countries in general and China in particular, but in these other regions the ratio grew over time. Not surprisingly, SSA's share of global MVA remained minimal, at less than one per cent over the 1990-2005 period. In contrast, that of China rose from 2.2 to eight per cent (and even more so, if calculated at PPP rates) in the same period (UNIDO International Year Book 2006).

Table 2 Share of MVA in GDP (At Constant 1995 Prices)

	1995	2000	2004a
Africa[b]	12.1	12.3	12.1
China	34.7	36.7	39
India	16.3	15.7	15.0
Developing Group excl China	19.2	20	20.4
WORLD	19.8	20.1	19.9

Source: UNIDO International Year Book 2006
a Estimate
b For Africa and not SSA.

Changes in the policy regime in SSA favouring greater openness during the 1990s led to a notable increase in the trade/GDP ratio which grew from 52 per cent in 1990 to 68 per cent in 2005. This compares with similar figures of 29 to 75 per cent and 14 to 40 per cent for China and India respectively (the end-date for India is 2004). Much of this growing trade openness was due to an expansion in merchandise trade; in 2005, SSA's merchandise trade/GDP ratio stood at 58 percent, an increase from 41 per cent in 1990. Focusing on the export side of this trade/GDP structure, the rate of growth of SSA's merchandise exports in the most recent period (1998-2004) exceeded that of the global average (but not China or India (Table 3).

Table 3. Average Annual Growth Rates of Merchandise exports and imports

	1990-1997		1998-2004	
	Exports	Imports	Exports	Imports
World	8.1	7.7	8.8	9.0
SSA	4.4	6.0	12.5	8.1
China	17.1	15.8	21.4	26.5
India	11.7	10.5	13.8	14.5

Source: Calculated from UNCTAD (www.unctad.org) accessed in January 2007

This impressive performance with regard to merchandise exports was largely due to the growth of SSA's oil and gas exports. The share of oil and gas in SSA's total exports grew from 39 to 45 percent between 1990 and 2005, whilst the share of manufacturing remained largely stable (Table 4). Oil and gas make the big difference to SSA's overall trade balance. With these commodities, the region had a rapidly growing trade surplus rising from $2.7bn in 1995 to $51.3bn in 2005; excluding oil and gas, SSA's trade deficit grew from $17bn to $38.9bn in the same period.

Table 4. SSA's exports the World (Excluding China) ($m)

	1995	**2000**	**2005**
Oil/Gas as % of Total	33%	37%	45%
Manufactures as % of Total	23%	27%	25%
Trade balance ($m)			
With oil/gas	2,694	33,141	51,357
Without Oil/Gas	-16,975	-8,412	-38,88

Source: Calculated from COMTRADE (Accessed through http://wits.worldbank.org) in January 2007
Data based on SSA as partner and not reporter[1]

Structure of SSA's manufacturing trade

In considering the structure of SSA's manufacturing exports we utilise the Lall-criteria of technological intensity which groups products into five categories – primary commodities, resource-based products, low-technology products, medium-technology products and high-technology products (Lall, 2000). Employing this taxonomy, Table 5 reflects the pattern of SSA's trade with the world, and compares this with India's and China's trade structure. In China's case there was a significant shift up the technological profile over the decade, with the share of high-tech products in total exports reaching 33 per cent in the latter period. India saw a similar shift in profile, albeit at a slower rate of change and into the medium, rather than the high-tech reaches. By contrast, not only was there no shift into medium and high specialisation in SSA exports, but rather a "downward" shift from resource-based processing industries into primary products.[2]

[1] There are widely-recognised problems in the use of COMTRADE data, because of poor reporting by SSA economies. Therefore all COMTRADE data is calculated on the basis of data reported by SSA bilateral trading partners.

[2] The Lall criteria treats oil and gas as a primary product (Lall, 2000).

Table 5: Technological intensity of exports: SSA, China and India, 1990-2005.

China's Export Structure			
	1995	**2000**	**2005**
Primary	10%	7%	4%
Resource Based	11%	9%	8%
Low Tech	46%	41%	32%
Medium Tech	19%	20%	22%
High Tech	13%	22%	33%
India's Export Structure			
	1995	**2000**	**2005**
Primary	20%	15%	12%
Resource Based	27%	29%	36%
Low Tech	38%	39%	30%
Medium Tech	11%	12%	16%
High Tech	5%	5%	5%
SSA's Export Structure			
	1995	**2000**	**2005**
Primary	58%	61%	64%
Resource Based	23%	20%	19%
Low Tech	7%	6%	4%
Medium Tech	7%	9%	9%
High Tech	1.4%	1.5%	1.5%

Source: Calculated from COMTRADE (Accessed through http://wits.worldbank.org) in January 2007

Excluding South Africa, which is a special case deserving of attention on its own, the sectoral composition of SSA's manufactured exports shows a heavy concentration on clothing and textiles. Table 6 sets out the data, beginning with "broad manufactures", that is SITC Sectors 5, 6, 7, and 8 (minus SITC 68 non-ferrous metals). These rose almost fourfold between 1990 and 2005, from $5.8bn to $21.8bn. But this impressive headline growth needs to be adjusted in some key respects. First, the largest component in 2005 was SITC 6872, unset diamonds, accounting for exports of $10.7bn. Second, there were significant "exports" of "railway/tramway" equipment (SITC 79) from Liberia ($1.7bn in 2005, virtually entirely ships) and Senegal (£290m in 2005, virtually entirely aircraft). However, a closer look at the data shows that both these economies were in trade deficit in both trade classifications. Their "exports" thus represent re-exports to the region. Third, included in this "broad manufactures" category are also methanol exports from Equatorial Guinea (SITC 51211), which is effectively a petroleum export, and uranium (SITC 52511) from Namibia and Niger. If we net out these items from the "broad manufactures category" we obtain a narrower classification of "narrow manufactures".

Table 6 shows that clothing and textiles accounted for a combined total of 45 per cent of all "narrow manufactures" exports from SSA excluding South Africa in 2005, and that this had risen from 40.7 per cent in 1990. Within that, the share of clothing rose from 31.5 to 41.5 per cent, and that of textiles fell from 9.5 to 3.2 per cent. (Clothing is much less technologically-complex and

has thinner levels of value added than textiles). The next most significant "narrow manufactures" exports was corkwood manufactures (almost entirely veneer sheets, SITC 63412 and plywood, SITC 63451), followed by iron and steel products (4 per cent, SITC 67) and leather manufactures (3 per cent, SITC 61).

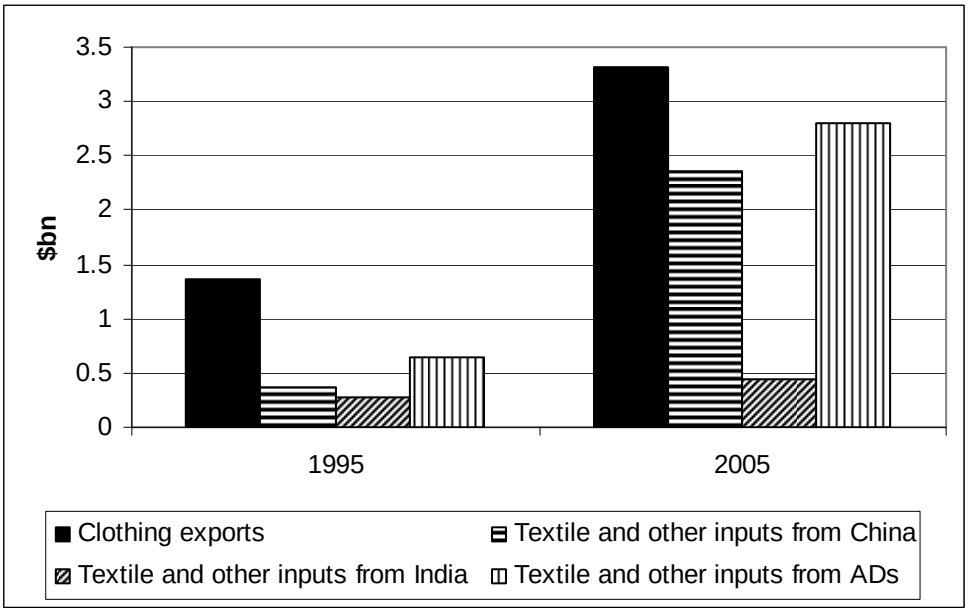
Table 6: "Broad" and "narrow" manufactures and the share of clothing and textiles in SSA (excluding South Africa) exports, 1990, 1995, 2000 and 2005.

	1990	**1995**	**2000**	**2005**
Value of production ($m)				
"Broad Manufactures"	5,820	7,019	13,612	21,849
"Narrow Manufactures" (ie Broad Manufactures net of diamonds, precious stones, re-exports, oil and gas by-products and uranium)	2,319	3,537	6,576	7,354
Apparel	730	1,142	2,622	3,053
Textiles	213	299	443	261
Cork/wood manufactures	190	269	478	641
Share of Narrow manufactures (%)				
Apparel	31.5	32.3	39.9	41.5
Textiles	9.2	8.4	6.7	3.5
Cork/wood manufactures	8.2	7.6	7.3	8.7

Source: Calculated from COMTRADE accessed via http:/wits.worldbank.org in January 2007

A final observation on the structure of non-South African manufactured exports concerns the low levels of value added in these expanded exports of clothing and textiles. Much of this occurs through the processing of imported fabrics and accessories (see below), mostly imported from China (and to a lesser extent from India) (Figure 2). Thus, although clothing exports increased significantly from $1.4bn to $3.3bn over the decade from 1995, there was a larger proportionate increase in imports of textile and other clothing inputs from the ADs.

Figure 2: Value of total global SSA clothing exports and related inputs sourced from ADs



Source: Calculated from COMTRADE (Accessed through http://wits.worldbank.org) in January 2007
Data based on SSA as partner and not reporter

Focusing on the technological content of SSA's trade (and using Lall's criteria of primary-products, resource-based products, and low-, medium- and high-tech products, Lall, 2000), the structure of SSA's trade with the ADs is somewhat different to that of trade with the rest of the world (Table 7). On the export side, trade with China is disproportionately geared to primary commodities (oil, gas) and to India in resource-based products. It is significant that intraregional exports are more technology-intensive than those destined for non-SSA markets. On the import side, SSA sources medium and high technology products from China, and low and medium technology products from India. It is notable that SSA's exports are much more heavily concentrated than its imports. As an example, oil and gas alone account for 69.3 percent of total SSA exports to China, and the largest 10 product categories (HS 4-digit) comprise 81 per cent of all exports. By contrast, on the import side, the 25 largest products only account for just over one-third of all of SSA's imports from China .

Table 7: Technological Intensity of SSA's trade: Share of exports and imports comprising different categories of products, 2005.

	World (excl. China,India	China	India	Intra-SSA
Primary Commodities				
Exports	65%	81%	38%	16%
Imports	8%	3%	13%	42%
Resource Based				
Exports	20%	15%	46%	37%
Imports	19%	9%	25%	27%
Low Technology				
Exports	4%	1%	3%	25%
Imports	10%	40%	22%	8%
Medium Technology				
Exports	10%	2%	11%	14%
Imports	44%	33%	28%	17%
High Technology				
Exports	1.6%	0.1%	1.1%	5%
Imports	19%	16%	12%	3%

Source: Calculated from COMTRADE (Accessed through http://wits.worldbank.org) in January 2007

3. THE ASIAN DRIVERS AND SSA'S CLOTHING AND TEXTILE EXPORTS

As we observed in Section 2, excluding South Africa, close to one-half of SSA's manufacturing exports are made up of clothing and textiles. These exports are overwhelmingly directed to the US (Table 8), and are a response to the introduction of the African Growth and Opportunities Act (AGOA) in 2000. AGOA was introduced in May 2000 and aimed to facilitate SSA export-led growth by extending GSP tariff preferences to a wider range of products (subject to minimum levels of value added). The largest manufacturing sector beneficiary of AGOA has been the clothing and textiles sector, since clothing and textiles has been excluded from the GSP scheme. AGOA incorporated different rules of origin to the GSP. It built on procedures which had been established early in the 1990s in relation to the Caribbean Basin Initiative allowing for the use of US-origin inputs or regional inputs in the calculation of minimum levels of value added (35 percent).

Nevertheless, despite these concessions, other than South Africa and Mauritius, few SSA economies were able to meet these rules of origin in the clothing and textiles sector. Thus, in a further key amendment, AGOA-qualifying countries which were also classified under the UN's "least developed category" (that is, per capita incomes of less than $1,500 in 1998) were also subject to a further amendment to GSP rules of origin. That is, until September 2007 (subsequently amended with modifications to September 2010) they could source their material and accessory inputs from non-AGOA and non-US bases suppliers (up to a restricted share of US clothing imports),

including from China and other Asian economies. In other words, they were freed from the minimum value added requirement.

The impact of AGOA on SSA's global (including intra-regional) clothing and textile exports cannot be underestimated (Table 8). Three major trends can be discerned. First, it led to a rapid expansion of trade. In three low income economies – Kenya, Lesotho and Swaziland – between 1999 and 2004, clothing exports grew from virtually nothing to $495m for Lesotho, $333m for Kenya and $205m for Swaziland. For Lesotho and Swaziland, this comprised the overwhelming bulk of merchandise exports. In two other economies – South Africa and Mauritius – clothing and textile exports grew rapidly until 2003 (to $1bn and $1.6bn respectively), but as the rules of origin derogation did not apply to them, and (in the case of South Africa) the exchange rate rapidly appreciated, exports began to fell sharply after 2003. In the case of Madagascar, exports to the US largely followed the pattern of the industry's principles, many of whom had relocated to Madagascar from Mauritius. Second, the share of exports going to the US was similarly dominating for Kenya, Lesotho and Swaziland, but less so for Madagascar, South Africa and Mauritius[3]. And, third, virtually all exports to the US were under the AGOA preferential scheme.

[3] Mauritius Madagascar and South Africa are differentiated from other AGOA-stimulated SSA clothing industries in that they have had historical links to the EU market. Mauritius has always exported the majority of its clothing output to the EU. Madagascar followed its principal in the post MFA period by significantly switching exports to the EU. SSA producers benefit from significant tariff preferences – exceeding 12 per cent – over Chinese producers. However the rules of origin into the EU are more restrictive than for entry into the US (two-stage over one-stage conversion).

Table 8. Global exports and share of US in exports of major SSA clothing and textile exporting economies

Country	Year	Exports $ '000	US Share (%)	AGOA as Share of Exports to US (%)
Kenya	2000	78,000	89.6	NA
	2001	87,000	92.7	80
	2002	156,000	95.9	96.6
	2003	234,000	95.8	93.7
	2004	333,000	95.4	97.9
	2005	306,000	95.3	98.5
	YTD 2006			97.5
Lesotho	2000	154,000	94.9	NA
	2001	237,000	94.3	60.1
	2002	350,000	97.9	98.9
	2003	429,000	97.7	94.9
	2004	496,000	97.3	98.2
	2005	406,000	96.5	99.4
	YTD 2006			99.4
Madagascar	2000	633,000	18.9	NA
	2001	709,000	27.4	51.8
	2002	387,000	26.1	84.4
	2003	527,000	41.5	94.8
	2004	784,000	45.5	97.2
	2005	771,000	37.0	98.5
	YTD 2006			96.0
Mauritius	2000	1,652,000	16.3	NA
	2001	1,561,000	16.6	16.3
	2002	1,524,000	18.3	41.8
	2003	1,629,000	17.9	50.2
	2004	1,638,000	15.0	65.2
	2005	1,384,000	12.4	85.8
	YTD 2006			92.1
South Africa	2000	867,000	31.0	NA
	2001	864,000	38.3	17.4
	2002	927,000	39.1	46.9
	2003	1,027,000	41.2	48.7
	2004	756,000	44.1	66.3
	2005	571,000	33.8	64.8
	YTD 2006			53.1
Swaziland	2000	56,000	88.4	NA
	2001	74,000	89.0	17.1
	2002	118,000	92.9	82.7
	2003	174,000	97.7	89.9
	2004	205,000	98.3	98.3
	2005	171,000	99.4	99.0
	YTD 2006			99.5

Source: UNSD COMTRADE database, accessed via World Integrated Trade Solution (WITS) 23 January 2007; Country and sectoral data calculated on the basis of US imports; For share of AGOA, for 2001, Gibbon, 2003; for 2004-YTD 2006 values www.agoa.info accessed 23 January 2007

On the 31st December 2004, there was a significant change in the regulation of global trade in clothing and textiles. Until then China and other Asian producers not only faced differential tariffs when exporting to the US and the EU. They were also confronted with quantitative limits to these exports. However, the removal of quotas did not mean a "level playing field" since global trade in clothing and textiles is still regulated by tariffs. In the case of the US, in 2005, the weighted average tariff (for world) for textiles was 6.93 per cent, while that for apparel was 11.36 per cent (TRAINS data based accessed through http://wits.worldbank.org on 24th January 2007)

In assessing the outcome of the two years of quota removal on these six SSA clothing and textile exporters, we concentrate on the clothing sector since with the exception of South Africa, there are negligible direct exports of textiles to the US. In each case we compare export volumes and market shares for all exports. However, since a key to market developments lies in unit price behaviour, we also analyse unit prices at the highest level of trade disaggregation (10-digit HS product categories).

As can be seen from Table 9 and Figure 3, the major trends were that:

- The value of SSA clothing exports to the US dropped by 25 per cent between 2004 and 2006. (January-November for both years) This masked differential country performance. Lesotho experienced a fall in export value of 15 per cent, most of which occurred in 2005; its exports stabilised in 2006. Madagascar, fared worse (a decline of 24 per cent), as did Swaziland (22 per cent). Kenya saw largely unchanged exports (a fall of only three per cent). The biggest casualties were South Africa (a decline of 54 per cent) and Mauritius (a decline of 62 per cent). Significantly neither of these latter two economies were able to utilise the 3rd country fabric derogation.

- By contrast, in the same period, the value of China's clothing and textile exports to the US increased by 82 per cent. In the major products exported to the US by AGOA, the value of Chinese exports rose by 161 per cent. (the aggregate export values are for 2004-2006; the changes in unit values are for 2004-2005).[4]

- Unit prices on average remained reasonably stable in key product groupings for individual SSA countries, with Madagascar experiencing the sharpest decline (10 per cent). In contrast, in the same product groupings, the unit value of Chinese exports almost halved. (However, it is not clear to what extent this was due to a reduction in the unit prices of individual products, or China's entry into producing lower-end products within each of these 10-digit product classifications) Need data or reference to Kaplinsky and Morris. Cant just say this.

[4] Because of the degree in churn in exported products (see accompanying text below) it was not feasible to compare unit price performance over the 2006-2004 period.

- In general AGOA economies performed less badly in their major exported items than they did in aggregate, suggesting a process of specialisation. However, alarmingly, in general China's export growth and the rate of price decline in these AGOA-populated sectors were greater than for its overall textile and clothing exports, suggesting potentially heightened competition for SSA products in the future.

- There has been significant churn as exporting firms in SSA have struggled with competition. For example, seven of the 10 largest product items (10-digit classification) exported from AGOA between January-November 2006 were not exported to the US in the same period in 2005, and only six of the 10 major exported items in 2005 were exported in 2006.

- The share of SSA exporters in the US clothing and textiles imports grew between 2001 and 2004, reflecting the combination of quota-access and preferential AGOA trading arrangements. However, the removal of MFA quotas set back this advance, and African exporters experienced a significant fall in their share of the US market after quota removal (Figure 3). By contrast, the share of China in each of these major product markets grew significantly.

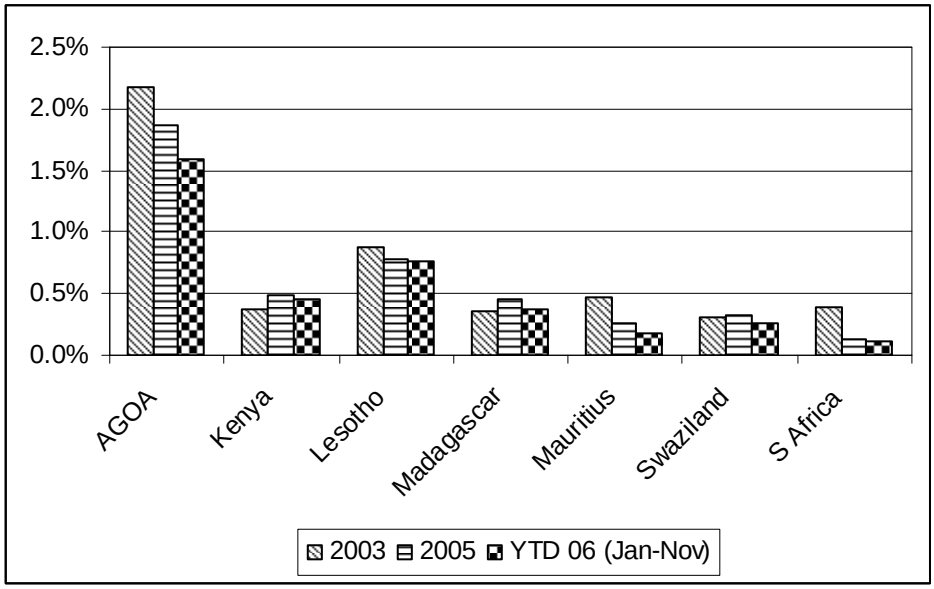
Table 9: Change in value of clothing exports to the US, 2004, 2005 and 2006 (January-November data in all years) (%)

	2005/2004		**2006/2005**		**2006/04**		Change in Unit Price of top 10 products 2005/04	
	SSA	**China**	**SSA**	**China**	**SSA**	**China**	**SSA**	**China**
AGOA	-16.5	56.9	-11.4	14.1	-25.2	82.0	-0.9%	-46%
Kenya	-2.5	77.8	-2.5	13.7	-3.3	106.3	-1.9%	-45%
Lesotho	-14.3	110.8	0.3	20.8	-14.6	160.4	-3.2%	-46%
Madagascar	-14.4	72.0	-14.9	16.3	-24.2	104.1	-9.5%	-44%
Mauritius	-26.4	73.2	-30.6	13.5	-61.6	100.0	-4.6%	-45%
Swaziland	-9.9	93.0	-16.2	15.3	-22.4	128.1	-2.7%	-52%
S Africa	-43.7	63.7	-18.7	11.5	-54.0	85.8	3.0%	-33%

Source: Calculated from http://dataweb.usitc.gov data, accessed on 10th January 2006

[a] Unit prices calculated for top 10 products in 2004 for each AGOA country's exports

Figure 3: AGOA country share of US market in all product categories in which country exports were concentrated in 2003-YTD2006



Source: Calculated from http://dataweb.usitc.gov data, accessed on 10th January 2006
[a] Unit prices calculated for top 10 products in 2004 for each AGOA country's exports

A major consequence of this decline in exports from the AGOA region was the impact on employment and overall economic activity. At its peak, in 2002, Lesotho's clothing exports to the US accounted for virtually all manufactured exports, and were equivalent to 50 percent of GDP. In Kenya in 2003, clothing enterprises accounted for the equivalent of nearly 20 percent of all formal sector manufacturing employment. Table 10 shows the impact of quota removal on employment in 2005. In Swaziland, most severely affected, overall employment almost halved. In Lesotho, in the first half of 2005, eight of the 47 garment exporting factories closed and employment fell by 26 per cent. Even in Kenya (where clothing exports had only fallen by 2.5 percent in 2005), employment declined by nearly ten percent. The impact on South African is more severe than appears from Table 10, since there had been employment loss in the industry in the years preceding quota removal, although the exact figures are difficult to determine (Edwards and Morris 2006). This was a result of competition in third country markets (South Africa had never been able to benefit from the 3rd country fabric provision), an appreciation of the Rand, and the direct impact of Chinese competition in the domestic market.

Table 10: Employment decline in the clothing sector, 2004-2005.

	2004	2005	% decline
Kenya	34,614	31,745	9.3
Lesotho	54,000	40,000	25.9
S Africa	98,000	83,000	15.3
Swaziland	28,000	16,000	42.9

Source: Kenya and Swaziland - Industry and Government interviews; Lesotho- Morris and Sedowski 2006b; South Africa – Edwards and Morris 2006

However, after this initial decline following the removal of MFA quotas in 2005, the position in Lesotho and Kenya stabilised in 2006. In Lesotho's case, employment rose from the trough of 40,000 in mid-2005 to 45,000 in late 2006, still below the 2004 peak of 54,000 in 2004, and the decline in export value was halted. In Kenya, the fall in export values remained low. Interviews with manufactures and buyers in both countries and the US suggest three factors which explain this performance. First, in the case of Lesotho, its DCCS scheme[5] provided subsidies to local producers. Second, the US buyers sourcing from Lesotho were mindful of the possibility of China Safeguards being sustained.[6] Third, in both countries buyers and producers had the expectation that the 3rd country sourcing provision (which had been due to expire in September 2005), would be maintained (as we shall see below, this was broadly correct). And, finally, in the case of Kenya, its currency did not appreciate relative to the US$. (We will return to the significance of these findings in Section 4 below).

Beyond clothing and textiles manufactures

Does this experience of SSA clothing and textile exporters have any significance beyond this sector itself? The answer is "yes", since it reflects a widespread change in the price of traded manufactures, which is of considerable historical significance.

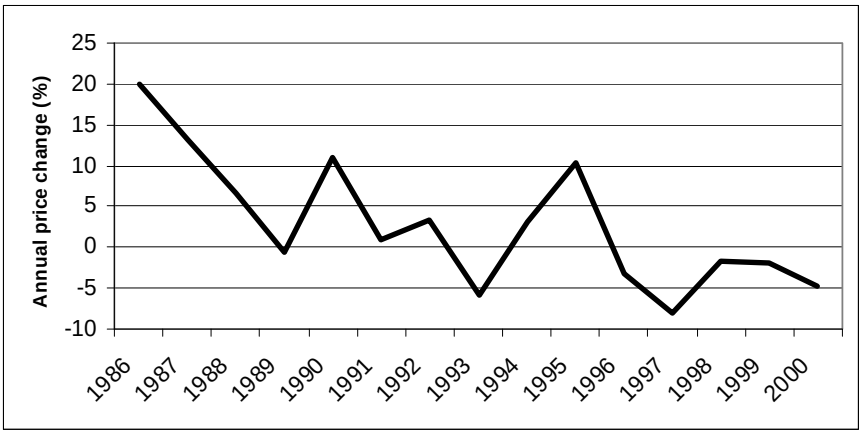
Much of the second half of the twentieth century was a period of inflation in the global economy. Prices of most commodities rose, although (as we have seen – Figure 1) the price rise was faster for manufactures than for primary products. By the 1990s, most economies had begun to get on top of high rates of inflation and for the OECD economies as a whole the rate of inflation at the turn of the millennium was less than three percent. What followed was a period of price deflation in manufactures, beginning with a slowdown in the rate of inflation in the late 1980s, and then after 1998, in absolute nominal prices (Figure 4).

---

5 The Duty Credit Certificate Scheme subsidises clothing exporters from South African Customs Union member states but is regarded as being WTO non-compliant and was ended in 2005. Hopwever, under pressure from industry and governments of Lesotho, Swaziland, Botswana and Namibia, the South African government belatedly, and late, agreed to an interim extension until March 2007with a proviso that industry come up with a new WTO compliant scheme.

6 The Chinese accession agreement to the WTO, allows for safeguard tariffs and quotas to be applied solely against Chinese textiles and clothing, even when imports exert only a slight adverse impact on the domestic industry. In June 2005, the EU and China reached an agreement that limited 10 categories of Chinese textiles exports to the EU to between 8 and 12.5 percent growth above a specified base period for the next three years. In December 2005, the US. and Chinese trade representatives agreed to a three-year agreement reducing US. imports of Chinese textile and apparel products in all or parts of 34 sensitive categories.

Figure 4: World Manufacturing Export Price, 1986-2000.



Source: Source: IMF, World Economic Outlook Database, September 2003

This falling in the price of manufactures is to a considerable extent a result of rapid industrialisation in East Asia in general, and China in particular (Lall and Albaladejo, 2004). To observe the impact of China's outward oriented industrial growth on global prices, we need to unpick the "manufacturing" category used in much of contemporary trade analysis, including that on the terms of trade. This literature is almost entirely based on the use of aggregated data, mostly using SITC 3- and very occasionally SITC 4 digit classifications. This is not adequate for a detailed examination of prices. The HS trade classification system introduced in the late 1980s has a much finer degree of disaggregation and provides greater scope for the detailed tracking of product prices. At the eight-digit level there are 10,000 different HS product categories. An analysis of these product categories tracked the extent to which prices of EU imports fell in the period 1988-2001 (Kaplinsky, 2005; Kaplinsky and Santos-Paulino, 2005a and 2005b).[7] The EU provides a unique data-set on international trade and is large enough to use as a surrogate for the behaviour of global product prices.

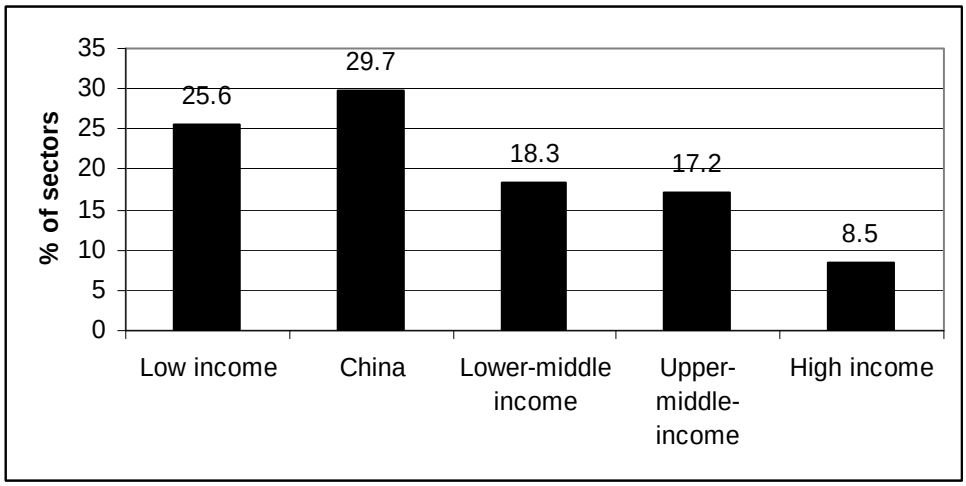
Figure 5 presents the results of this analysis. It focuses on the 151 major product-groupings (classified at the eight-digit level) imported into the EU where developing country exporters were prominent. It reports the proportion of the sectors for which the unit-price of imports from different income-groups (and China) fell between 1988 and 2001. It can be seen from this that in almost one-third of these sectors, the price of Chinese-origin products fell. In the case of products emanating from low-income economies, the proportion of product group in which unit-prices fell was around one-quarter. As a general rule, the higher the per-capita income group of the exporter, the less likely

[7] The data-set used for this detailed analysis of prices at the eight-digit HS level is only available from 1988. In associated work we have attempted to utilise the augmented Dickey-Fuller unit root test in an attempt to determine statistically significant price trends. Unfortunately neither this test, or any others with which we are familiar, can cope with such a short time-series. For a fuller discussion of these imitations and the application of the ADF test to our price data, see Kaplinsky and Santos-Paulino 2005a and 2005b.

unit-prices were to fall. Thus, within a large number of product groups, the prices of products exported into the EU by China and low income economies was more likely to decline than the prices of the same products-groupings sourced from other high income economies.

We draw two conclusions from this price analysis. First, the greater China's participation in global product markets, the more likely prices will fall. And, second, this seems to have a disproportionate impact on the low income country group who face intense competition from Chinese producers.

Figure 5: Percentage of sectors with negative price trends, 1988/9-2000/2001 by country groupings



Based on an analysis of 151 eight-digit products, selected on the basis of their contribution to LDC exports to the EU.
Source: Kaplinsky (2005b)

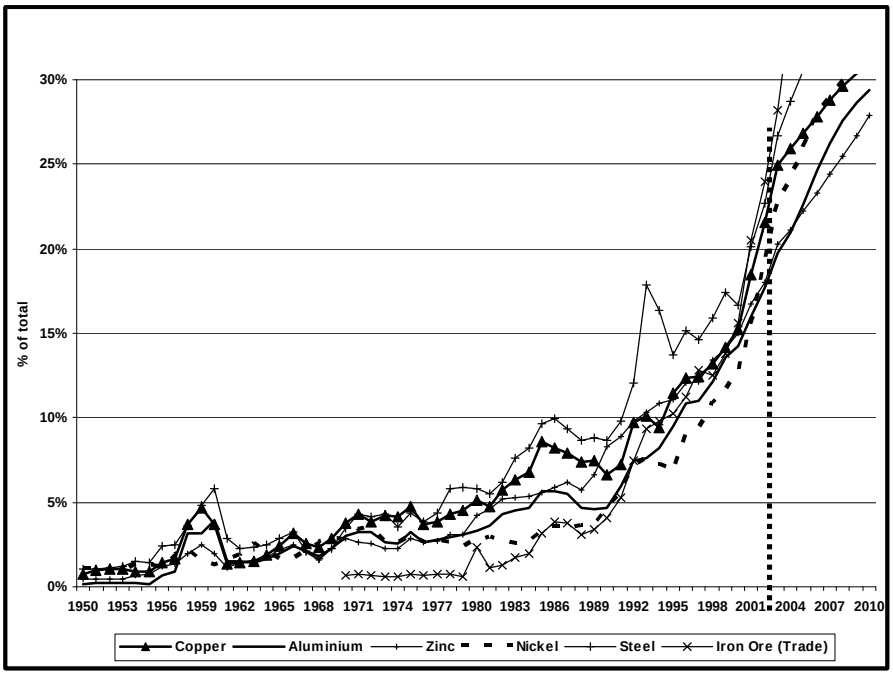
4. THE ASIAN DRIVERS AND SSA'S COMMODITY EXPORTS

At the same time that manufacturing prices were falling towards the end of the 1990s, commodity prices (particularly of oil and gas, and the metal-based commodities used in the production of manufactures) began to rise. A key driver of these rising commodity prices was demand from China's burgeoning manufacturing sector.

Focusing on basic metals as an example, China's demand for imports has been fuelled by three factors. The first has been the rapid growth of domestic demand for household consumer goods and autos (where production has grown at a dramatic pace). Second, there has been very substantial investment in infrastructure, both in the public and private sector, and this has been particularly basic-metal intensive. And, third, many of China's exports have been of metal-based products. Consequently**,** China's share of global demand for the main base metals (aluminium, copper, iron ore, nickel, steel and zinc) grew from seven-ten percent of global demand in 1993 to 20–25 percent in 2003. In the case of steel, its share has grown from less than 10 percent in 1990 to more than 25 percent in 2003, equivalent to three times that of Japan, and more than either the EU or the US (around 20 percent

each). Between 2000 and 2003, China's share of the increase in global demand for aluminium, steel, nickel and copper was 76 percent, 95 percent, 99 percent and 100 percent respectively. As Figure 6 shows, its projected utilisation of these basic metals is likely to grow even further in the future, in part because of its relatively low per-capita consumption of these materials (Table 11) – bear in mind, China accounts for more than 20 percent of global population, and it is inevitable that as incomes grow and the minerals-intensity of consumption grows as it has in other countries, this will continue to lead to rising demand for imported materials.

Figure 6. Actual and projected global share of China's consumption of base metals, 1950-2010.



Source: Macquarie Research Metals and Mining, personal communication (2004)

Table 11: The scope for China's increased consumption of basic metals, 1955-2003.

	Kgs/capita			GDP per capita ($US1995)
	Aluminium	Copper	Steel	
Japan				
1955	0.6	1.2	80	5,559
1975	10.5	7.4	599	21,869
Korea				
1975	1.0	1.3	84	2,891
1995	15.0	8.1	827	10,841
China				
1990	0.7	0.6	59	342
1999	2.3	1.2	108	756
2002	3.3	2.0	160	933
2003	4.0	2.4	200	1,103

Source: Macquarie Metals and Mining, personal communication (2004).

This expansion in Chinese commodity imports has been closely reflected in the global prices of many hard commodities. For example between 2002 and 2004, the price of hot-rolled coil steel rose from around $140/tonne to more than $500/tonne, much higher than the previous post-war peak of $400/tonne in 1994. Prices of spot steam coal (cif Rotterdam) leapt from $27/tonne to $82/tonne between 2002, and 2004, higher than the previous post-war peak of 1981. Hard-coking coal prices jumped from $50/tonne to more than $100/tonne in the same period, a post-war high. Between 2001 and 2004, copper prices more than doubled from around 63 cts/lb to $1.40/lb, although in this case they were still lower than the previous post-war peak on $1.55/lb in 1989. [8]

This thirst for mineral imports is also reflected in the food sector, where falling land availability (a consequence of rising industrialisation) and stagnant agricultural productivity have led to rising food imports. In the first half of 2004, China had a trade deficits on foodstuffs of $3.7bn., including imports of 4.1m tonnes of foodgrains. It is predicted that this deficit will soar in the future - in the case of foodgrains, to around 40m tonnes by 2007 (Financial Times, 23rd August, 2004).

These are undeflated prices and represent a price spur which has been very recent (that is, since 2000). However, they reflect the data presented in Figure 6 above on China's augmentation of global demand in hard commodities. Will they endure? The data in Table 11, allied to China's continued rapid growth, suggests that this is not a short-term blip in commodity prices. Moreover, so far India's very raid growth has not been evidenced in its thirst for imported commodities. But, as in the case of oil and gas, this is changing rapidly, and with 17 percent of global population and an economy and industrial sector

[8] All data from Macquarie Research.

growing at more than eight percent p.a., India's quench for commodity imports will soon place further pressure on global prices.

It is perhaps too early to conclude from these developments that we have witnessed a decisive and/or a long-term shift in the manufactures-commodities terms of trade. But let us assume for the moment that this is the case. If so, what are the consequences for SSA's development strategies which committed economies towards industrialisation in general, and export-oriented manufacturing in particular?

5. WINNERS AND LOSERS ON THE TRADE FRONT

It is schematically possible to predict who the winners and losers might be as a result of these changing terms of trade. Working at a broad level of aggregation it is possible to group traded commodities into two sets. The first are those commodities which the Asian Drivers trade intensively. Some of these they import (for example, oil and primary commodities); others they export (for example, China's manufactures, and India's services). The second comparable dimension relates to SSA's trade structure. This comprises products which SSA imports (for example, manufactures, and in some cases, oil) and those which SSA exports (for example, metal ores and oil).

Grouping traded commodities in this way it is possible to identify "losing" countries and sectors and "winning" countries and sectors within SSA:

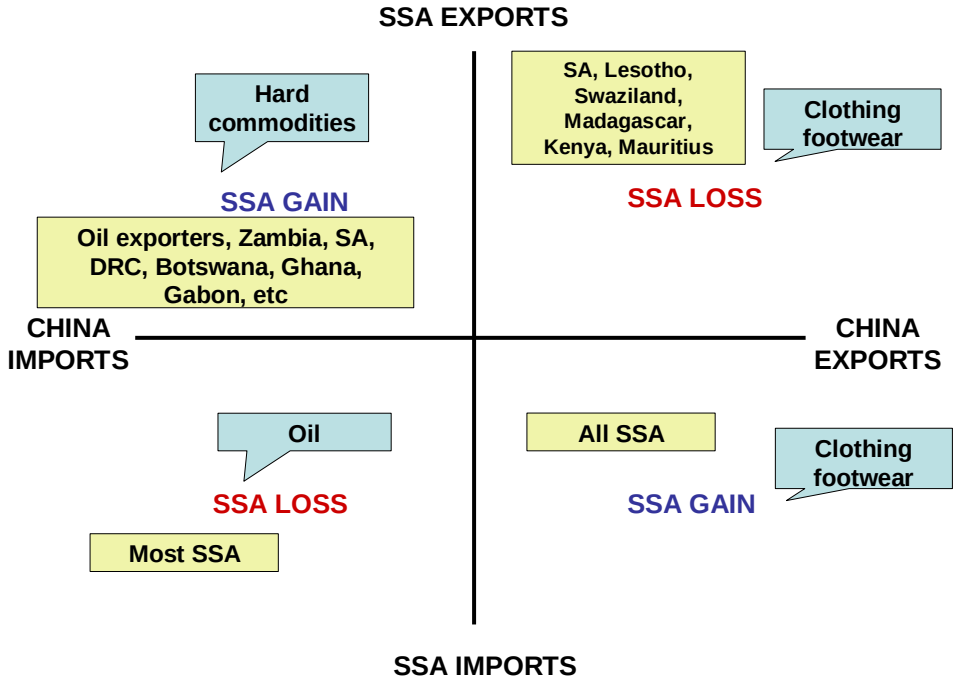
- The winners are those SSA economies which export what the ADs import and import what the ADs export. That is, they gain on the export side from rising demand and rising prices as ADs swell global demand, and they gain on the import side from falling prices resulting from competitive production in the ADs.

- The losers are those SSA economies which export what the ADs export, and import what the ADs import. They have to compete for imports in global markets characterised by rising prices due to enhanced AD demand, and they sell into global markets where competition is intense as a consequence of AD exports.

Figure 7 provides a graphical representation of these winners and losers, using China as an example, and at a very broad level of aggregation to illustrate these principles. The top left quadrant represents SSA countries which export the products which China imports. These are oil and mineral exporters such as Nigeria, Angola, Sudan and Zambia. The bottom right hand quadrant also comprises winners, SSA economies who import what China exports – predominantly cheap consumer goods. Conversely the top right hand quadrant identify losers who export the same products as China – the clothing and textile and other manufactured goods exporters discussed earlier in the paper. The bottom left hand quadrant category identifies another set of losers, those importing the same products which China imports; SSA oil importing economies are an important group here.

It is important to note that Figure 7 also opens up the issue of the extent to which countries are homogenous entities. For example, the gainers who consumer cheap Chinese clothing and textiles and shoes in the bottom right quadrant live in the same countries (and are often sometimes the same people) as the production workers in the top right hand quadrant whose wages and jobs are threatened by cheap Chinese products. Thus “winners” and “losers” are not the same as particular economies.

Figure 7: Identifying winning and losing SSA economies



6. INDUSTRIALISATION OR GENERALISED INNOVATION?

One reason why we might be relativity sanguine about these price trends is that they refer only to the barter terms of trade. The Asian NICs experience has shown that the ability to expand export volumes at a disproportionately higher rate than the fall in relative prices means that falling barter terms of trade may not be a problem as long as the rate of productivity growth is higher than the differential between the barter and income terms of trade (Maizels, 1999). However, this outcome depends on a world in which there are supply constraints, that is, one in which export volumes can continue to grow. The neo-classical trade framework is indeed contingent upon this assumption and provides for a global architecture in which countries find their relatively efficient niche in a world of specialisation and respecialisation. But what happens in a world of global excess capacity? In these circumstances, falling export prices in aggregate does not mean that all producers can compensate with rising export volumes; only those with absolute advantage are able to do so.

There are reasons to believe that the contemporary global economy is indeed in a phase of structural excess capacity, particularly for manufactured products exported by low income countries (Kaplinsky, 2005b). This arises from two factors. First, in many of the buyer-driven consumer goods sectors such as apparel, footwear, furniture and toys (Gereffi, 1994), the rise of developing country exports has by now knocked-out most of productive capacity in the high-income countries. Thus, future export growth from the developing world depends either on sustained and very rapidly growing demand in the high-income countries (unlikely), or the ability to out-compete other developing countries. In this era of global industrial capabilities, East Asia in general, and China in particular, is so competitive that there is little scope for SSA (or other developing countries) to win this competitive battle.

The non-East Asian economies are therefore faced with a severe challenge. Given their inability to compete effectively in the market for global manufactures, wherein lies their development route? Should the widespread commitment to manufacturing be jettisoned? The answer to this lies in the recognition that the key desirable attribute in global production systems is to appropriate rents, that is the ability to gain from activities which are difficult to replicate (Kaplinsky, 2005b). Historically, these scarce capabilities were predominantly to be found in the industrial sector in general, and manufacturing in particular. But, with the rise of China's globally competitive manufacturing sector, we now also know that technological rents are no longer as pervasive as they used to be in manufacturing. Many manufacturing sectors, particularly those in which low income economies play a central role, are characterised by low barriers to entry, falling barter terms of trade, and limited possibilities for rising income terms of trade.

The answer to this policy challenge lies in removing the identity between innovation rents and manufacturing. On the one hand, we know that rents may be low in many industrial sectors. But at the same time, there has been a tendency to underemphasise the rents available in some agricultural and service sectors.

These non-manufacturing rents are illuminated by the post-war transition from the era of mass production (sometimes referred to as fordism) to mass customisation (sometimes referred to as post-fordism or flexible specialisation) (Piore and Sabel, 1984; Lipietz, 1987; Pine, 1993). The period before the 1970s, said to be the heyday of mass production, reflected a world of post-war reconstruction and shortages. Producers thrived in markets in which Henry Ford had argued of his customers that "they can have a Model T Ford in any colour they like as long as it is black". But as production capability, and incomes grew in the post-war period, so consumers were no longer happy with black Model T Fords. Companies such as BMW and Mercedes-Benz carved out profitable market niches by emphasising individuality and variety. This capability to individualise products rapidly spread across the spectrum of manufactures, with the growth of numerous designer labels.

There is an extensive literature on the role which this differentiation plays in the determination of relative income streams.[9]

But it is only recently that we have come to recognise the opportunities for the de-commodification of a variety of "soft commodities" (Jaffee and Gordon, 1993; Jaffee, 2003: Kaplinsky, 2005a). Two of the most-widely cited cases are horticultural products and coffee. In the case of horticulture, relatively high incomes are earned by producers who are able to tailor their output to the needs of very dynamic markets (Dolan and Humphrey, 2004). For example, Kenyan horticultural producers fly their salads out to UK supermarkets every night, ready-packed and labelled for individual stores. Demand for salads is highly variable depending on the weather (for example, during warm weather, the demand for salads for barbeques mushrooms). The Kenyan producers are so sophisticated in their logistics that they allow their UK supermarket customers to vary their orders for pre-packed salads up to 1400 hours on the day of dispatch.

In the case of coffee, customers are beginning to appreciate the enormous variety of tastes. In the words of a Nestlé's senior executive, "there are as many varieties of coffee, with a greater variation in taste, than there are of wines" (Kaplinsky and Fitter, 2004). Producers who were able to target these niche markets were able to insulate themselves from the devastating fall in global prices in the early 2000s. For example, Jamaican Blue Mountain coffee is a premium product, with Japanese consumers prepared to pay up to $20 per cup. Its growers have been able to escape the severe price pressures which have characterised the industry, particularly in recent years. As the CEO of the Jamaican Coffee Board observed: "Blue Mountain coffee prices are not subject to the factors of supply and demand that affects other commodities. The price is fixed. This is useful in these times when coffee prices are low because of over-supply" (Financial Times, 18th October 2001). In early 2002 Blue Mountain coffee sold at $6-8,000/tonne compared to the London market price for arabicas of around $1,200/tonne.

It is helpful to show how this technological capability focused strategy can in fact be implemented for agricultural commodities by innovative firms. Illy is a privately-held Italian company operating in the quality-intensive segment of the coffee value chain, with a turnover in 2005 of more than $300m (Kaplinsky, 2005a and Business Week, August 7, 2006). It employs 500 people worldwide and is wholly-concentrated on the coffee chain. It performs at the premium end of the market, with excellence, with pre-tax profits of 10.4% on sales (and of course a much higher margin on shareholder funds). (Compare this with the zero profitability of most coffee growers)

Illy's route into coffee was through technological innovation – in the 1930s the founder developed an end-seaming technology for tins which allowed coffee to be stored at 0.3-0.4 atmospheres, and therefore to serve distant markets with fresh coffee. (Their current technology provides coffee storage at 1.5-1.5

[9] For example, see the burgeoning value chain literature which relates this literature to developing countries – http://www.ids.ac.uk/globalvaluechains/

atmospheres, in distinctively shaped and branded aluminium containers which simultaneously fosters positional consumption). Over the years its core competences have changed from tin-making technology to a cluster of related capabilities - coffee-roasting, the management of its global coffee value chain, the manufacture of small espresso machines, and the ability to run a chain of coffee shops.

How does Illy manage to sell coffee at $10/250gm in the US, compared to competitors' prices of $1.50/kg, and how does it manage to pay farmers 30 percent more than the prevailing world bean price? It does so by systematically applying knowledge at every point in the value chain. Coffee is a complex product, with more than 800 components of aroma alone. In some cases this effort involves high-science – for example, the analysis of the percolation process took half-an-hour on a Cray supercomputer. 12% of employees have university degrees and Illy spends 1.5% of sales on R&D. But more to the point is Illy's systematic application of technology and knowledge (generally in disembodied procedures) throughout the chain often involving barely-literate workers, through:

- Heavy investments in understanding the *nature of flavour*. Building on genetic developments they work closely with farmers, since there is a complex interaction between ecology and genes; reducing water content from 65% to 11% provides plenty of scope for moulds and rot; and poor transport leads to coffee degradation. Illy runs courses for both buyers and farmers in countries where they purchase beans.

- Sophisticated *selection of the bean*. Most farmers have little knowledge of what constitutes "quality coffee", and they have to be taught how to recognise this. Bean selection also depends heavily on technology and in cooperation with a machinery supplier Illy developed a patented and scale-intensive sorting machine (costing $150,000 and processed 3-4 tonnes/hr).

- Temperature control in *roasting* This is critical – $C3^0$ at $C200^0$ makes a significant difference to taste - and is not a simple process. Due to non-linearity when the roasting process is scaled-up, it involves heavy investment in sophisticated machinery.

- *Branding*. Packaging was Illy's historic core-competence and remains a key competitive branding advantage. Branding is of key importance and 9-10% of sales is spent on advertising

- Diversification down the chain - one of the family members has built a business manufacturing and selling *espresso machines* for home consumption.

- Assisting coffee houses (accounting for more than a third of sales) which are targeted for *education* since "dirty machines kill the best coffee". Illy also invests heavily in designing "coffee bar concepts", ways of improving the ambience of coffee bars.

A similar story can be told of a particular niche in the wool sector. Escorial wool is derived from the Maghreb sheep, and is characterised by its lustre and fineness. In 1828 100 sheep were taken to Tasmania in New Zealand from the Atlas Mountains. In the late 1990s, a group of New Zealand farmers banded together and spent $NZ6m on promoting the brand and characteristics of this sheep and describe their strategy in the following terms:

> *"The Escorial Company is a living example of the determination of a small group of growers of an old and characteristically quite different fine wool to improve their lot by taking control of the production, supply and marketing under a registered fibre brand, Escorial, right through to the highest end finished goods in EU and the USA. [This is] a first for branding a fibre, with a fascinating story dating back to the 14th century and the Palace of El Escorial in Spain….*
>
> *These sheep [are] a distinctive breed and [possess distinctive] wool quality/characteristics…. [T]hrough the closed controlled farming of them on one farm since 1834, and a few pure documented flocks emanating from that one farm, [we] are the sole pure survivors in the world. We have created 'clean air' between the generic commoditised 'Merino' and Escorial by physical differentiation. An Escorial suit sold by Brioni of Milan sells well above the top cashmere equivalent and many times above an equivalent fine merino. [In fact an Escorail scarf retails for more than €600, positioned well above cashmere].*
>
> *[The role] played by the [coffee] roaster is exactly that of the topmaker in the wool industry, a blender of wools of many origins to produce a consistent, numerically described (using very high tech calibration systems laser, optical fibre measurers etc) to supply their customer, the spinner with a consistent product all year round that masks rather than isolates or promotes specific characteristics ….[In contrast] we grow, select, organise all stages of processing around the world, then select the Houses who can sell Escorial fabrics with our label on each finished piece, which can be genuinely claimed as 'pure' and expresses itself in ways that are unique and the customer can experience. We started at the far end, to create the demand first and have found our place despite the machinations of the very wealthy and powerful brands that have made their money on the back of woolgrowers …" (Personal communication, Chris Stewart. Manager - The Escorial Company Limited, New Zealand)*

Five Scottish weavers formed the Escorial Guild working in close cooperation with a New Zealand company which exclusively markets the output arising from 40,000 sheep producing only 50 tonnes of wool a year. One of the Scottish weaver's designers positions Escorial in the following manner – "Cashmere has lost its cachet. There is now too much of it, and of all different qualities – some of it is extremely rough. You can even get it in GAP" (*Scotland on Sunday 4 July 1999)*

A key characteristic of these niche markets is that they are very demanding at the level of process, particularly with respect to certification. For example, FSC wood products have to be accompanied by a chain-of-custody which follows the product from forestry to the retail store. This sets standards in logging – for example, no cutting for a number of days after it has rained; not undermining biodiversity; respecting the needs and culture of local peoples.

But it also requires specific environmental standards in manufacture, in transport and in retail. In the auto sector and in the electronics sector, buyers set basic standards concerning defective parts (measured in parts per million, and increasingly being targeted at zero parts per million) and delivery, as well as prices. In the horticultural sector, traceability is required at a very detailed level. This allows retailers and producers to identify individual growers and plots of land just in case there should be problems with pesticide residue at the point-of-sale.

It is in this extensive and demanding process of certification that barriers to entry are constructed and in which primary products are decommodified. This has become an increasingly important characteristic in the markets for very many “soft commodities” and suggests that falling prices are not an inevitable outcome in these product markets which are based on primary products. The impetus for the increase in the prices of niche-based “soft commodities” lies in the growth of per capita incomes in the high-income economies. This is a form of Engels Law reversal, which is reflected in the fact that the most accurate predictor of the per capita incomes of shoppers in UK supermarkets lies in the proportion of fresh fruit and vegetables in their shopping trolleys. Increasingly these fresh fruits and vegetable are sourced from developing economies.

7. FROM STRATEGY TO POLICY

If we thus adjust our strategic lens from industrial development specifically to innovation in all sectors, what policy environment best provides for these development objectives to be met? Here Lall and Teubal provided a very useful theoretical architecture to push forward this agenda. Although they focused on the development of (narrow) technology policy, in so doing they provided a much broader framework for pursuing innovation policies. Lall and Teubal identified three types of policy, namely:

- “functional” policies improving market operations; for example, policies designed to enhance competitive pressures (such as competitions policy; lowering tariffs)

- “horizontal” policies which cross sectors, such as generalised incentives to promote greater R&D and training

- “selective” policies designed to promote the advance of particular sectors (for example, preferential access to capital; sector-specific subsidies) or particular firms (for example, the promotion of “national champions” such as the Proton auto firm in Malaysia).

This policy agenda of course ran against the mainstream during the 1990s. For example, the first half of the 1990s saw a vibrant debate on the efficacy of industrial policy in developing economies, after which there was solidification in the policy environment, both within multilateral agencies and in most developing country governments. The context was one in which the Washington Consensus of the early 1980s had led to the increasingly rapid

spread of structural adjustment programmes in low income economies. These programmes privileged trade policy liberalisation, deregulation, FDI and the dismantling of policy and administrative regimes designed to promote industrial development. In response to this increasingly hegemonic policy agenda, the Japanese representatives in the World Bank sponsored a process of research enquiry into determinants of industrial success in eight "highly performing Asian economies" (HPAEs) – Hong Kong, Indonesia, Japan, Korea, Malaysia, Singapore, Taiwan and Thailand. The intent was to promote the policy agenda that Japan had itself used in its very rapid industrial development, one providing an active market-guiding role for the state in the promotion of selected industries.

The outcome of this industrial policy study (World Bank, 1993), and the process whereby it reached its conclusion is well known, and has been extensively documented (Wade, 1996; Special Issue of World Development 1994). Briefly, the report concluded that the only positive role these governments had played was to promote generic economy-wide incentives in areas such as education and research and development to compensate for market failures. The Report explicitly argued that targeted industrial policies had failed, even though it acknowledged that providing unambiguous "proof" was difficult. At a general level, it concluded that "[o]ur judgement is that in a few economies, mainly in Northeast Asia, in some instances, government interventions resulted in higher and more equal growth than otherwise would have occurred [a sop to the Japanese lobby]. However, the prerequisites for success were so rigorous that policymakers seeking to follow similar paths in other developing countries have often [in reality they meant usually] met with failure" (World Bank, 1993: 6). More specifically, it argued that targeted industrial policies cannot be shown to have had a net positive impact on industrial performance (although, as they point out, this is a matter of belief and judgement). And, secondly, even if it were true that targeted policies might be effective in some environments, the call on administrative expertise was so significant that few developing economies could hope to benefit from their use.

This policy agenda aligns only loosely with current orthodoxy which sees the export-oriented policy framework in SSA as comprising of a mix of Behind the Border (predominantly infrastructure), Beyond the Border (predominantly market access) and Between the Border (predominantly logistics) issues (Broadman, 2007). The focus on innovation capabilities opens up the challenge of moving beyond the improvement in infrastructure to an active industrial policy which focuses on the development of industrial capabilities and the successful insertion of SSA economies in global value chains (Kaplinsky and Morris, 2007). This active industrial policy, as Lall and Teubal point out, will almost always move beyond macroeconomic stability and the correction of market imperfections to a active and appropriately nuanced sectorally-, firm-category- and regionally-specific policies.

References

Broadman, H. (2007), Africa's Silk Road: China and India's New Economic Frontier, Washington DC: The World Bank

Clerides, S, S. Lach, and J. Tybout. 1998. "Is 'Learning-by-Exporting' Important? Micro-Dynamic Evidence from Colombia, Mexico, and Morocco." Quarterly Journal of Economics, 454(3): 903–47.

Dolan, K, C. and J. Humphrey (2000), "Value chains and upgrading: The impact of UK retailers on the fresh fruit and vegetables industry in Africa", Journal of Development Studies, Vol. 37, No. 2, pp. 147-176.

Edwards L, and Morris, M, (2006) "An Evaluation of the Employment Trends in the Clothing & Textile Industry", PRISM Working Paper, Policy Research in International Services and Manufacturing, SALDRU, University of Cape Town. http://www.saldru.uct.ac.za/prism/evaluation-of-employment-trends-25O.pdf

Gereffi, G. (1994), "The Organization of Buyer-Driven Global Commodity Chains: How U. S. Retailers Shape Overseas Production Networks", in G. Gereffi and M. Korzeniewicz (eds.), Commodity Chains and Global Capitalism, London: Praeger.

Jaffee, S. (2003), From Challenge to Opportunity: Transforming Kenya's fresh vegetable trade in the context of emerging food safety and other standards in Europe, Agriculture & Rural Development Discussion Paper 1, Washington: World Bank

Jaffee, S. and P. Gordon (1993), "Exporting high-value food commodities: success stories from developing countries", World Bank Discussion Paper, 198, Washington, D.C.

Kaplinsky, R. (2005a), "Revisiting the Terms of Trade Revisited: Will China Make a Difference?" World Development, (Vol. 34, No. 6, pp. 981-995)

Kaplinsky, R. (2005b), *Globalization, Poverty and Inequality: Between a Rock and a Hard Place*, Cambridge: Polity Press.

Kaplinsky, R. and A. Santos-Paulino (2005a), "A disaggregated analysis of EU imports: The implications for the study of patterns of trade and technology", *Cambridge Journal of Economics*.

Kaplinsky, R. and A. Santos-Paulino (2005b) "Innovation and competitiveness: Trends in unit prices in global trade", *Oxford Development Studies*, Vol. 33, Numbers 3-4, pp. 333-355.

Kaplinsky, R. and D. Messner (2007 forthcoming), "The Impact of the Asian Drivers on the Developing World", Introduction to World Development Special Issue on Asian Drivers and their Impact on Developing Countries

Kaplinsky, R. and M. Morris, (2007), "The Structure of Supply Chains and their Implications for Export Supply", Paper prepared for African Economic Research Consortium, Nairobi: AERC

Kaplinsky, R. and R. Fitter (2004), "Technology and Globalisation: who gains when commodities are de-commodified?", *International Journal of Technology and Globalization*, Vol. 1, No. 1, pp. 1-28.

Lall, S. (2000), "The Technological Structure and Performance of Developing Country Manufactured Exports, 1995-1998, Oxford Development Studies, Vol. 28, No. 3, pp 337-369.

Lall, S. and M. Albaladejo (2004), "China's Competitive Performance: A Threat to East Asian Manufactured Exports*?". World Development*, Vol. 32, No. 9, pp. 1441-1466.

Lall, S. and M. Teubal (1998), "Market Stimulating' Technology Policies in Developing Countries: A Framework with Examples from East Asia", *World Developmen*t, Vol. 26, No. 8, pp. 1369-1385

Lipietz A (1987), Mirages and Miracles: The Crises of Global Fordism, London: Verso.

Maizels, A. (1999), 'The Manufactures Terms of Trade of Developing Countries with the United States, 1981–97', Working Paper 36, Oxford: Finance and Trade Policy Centre, Queen Elizabeth House.

Pine, J. B. (1993), Mass Customization: The New Frontier in Business Competition, Cambridge, Mass: Harvard Business School Press.Piore M. J. and C. Sabel (1984), The Second Industrial Divide: Possibilities for Prosperity, N. York: Basic Books.

Porter, M. E. (1990), The Competitive Advantage of Nations, London: Macmillan.

Prebisch, R. (1950), 'The Economic Development of Latin America and Its Principal Problems', *Economic Bulletin for Latin America 7*, N. York: United Nations.

Ricardo, D. (1817), The Principles of Political Economy and Taxation, London: Dent (Reprinted 1973).

Singer H. W. (1950), 'The Distribution of Gains between Investing and Borrowing Countries', *American Economic Review*, 15, pp. 473-85.

Smith, A. (1776). An Enquiry into the Nature and Cause of The Wealth of Nations. (4th Edition), republished in 1976 by Oxford University Press, and edited by R. H. Campbell and A. S Skinner.

UNIDO (2006), International Year Book 2006, Vienna and New York: UNIDO

Wade, R. (1996), "Japan, the World Bank and the Art of Paradigm Maintenance: The East Asian Miracle in Political Perspective", New Left Review, 211, pp. 3-36.

World Bank (1993), The East Asian Economic Miracle: Economic Growth and Public Policy, N. York: Oxford University Press.

World Bank (2002), Globalization, growth, and poverty: building an inclusive world economy, Policy Research report, Washington: World Bank and Oxford: Oxford University Press.