AID FOR TRADE: IS IT WORKING?

Trade can be a powerful engine for economic growth and poverty reduction, but harnessing its power is difficult for many developing countries.

This is particularly true for the least developed countries (LDCs), where there is often a lack of capacity – in terms of information, policies, procedures, institutions, and/or infrastructure – to integrate and compete effectively in global markets.

To address these capacity constraints, the WTO has led the call for more and better aid for trade. Recommendations have been made to strengthen both the demand-side and the donor response, while working to better bridge the gap between these at the country, regional and global level.

Furthermore, the WTO and OECD periodically put a spotlight on aid for trade to monitor what is happening, what is not, where improvements are needed and whether aid for trade is having the desired effect.

The Aid-for-Trade Initiative has helped to promote considerable progress in a short time. Partner countries and donor agencies are prioritising trade in their development strategies, and aid-for-trade flows are rising.

In fact, aid for trade increased 62% in real terms between the 2002-05 baseline period and 2008, with commitments in 2008 totalling USD 41.7 billion. The increasing commitments were widely shared among aid-for-trade sectors and across income groups.

Gradual recovery from the severe economic crisis, and continued exploitation of market access opportunities – which a conclusion to the Doha Development Agenda will offer – underscore the case for more and better aid for trade.

Aid for trade can provide a short-term stimulus with long-term impacts on improving the ability of enterprises in low-income countries to respond to trade opportunities. Aid for trade bolsters the contribution of trade to economic growth and poverty reduction.

Maintaining the momentum of aid for trade necessitates deepening the partnership between governments, regional organisations, the private sector, civil society and the development community. The OECD and WTO's work will contribute to this goal and aim to strengthen the positive impact of the Aid-for-Trade Initiative on achieving the Millennium Development Goals.

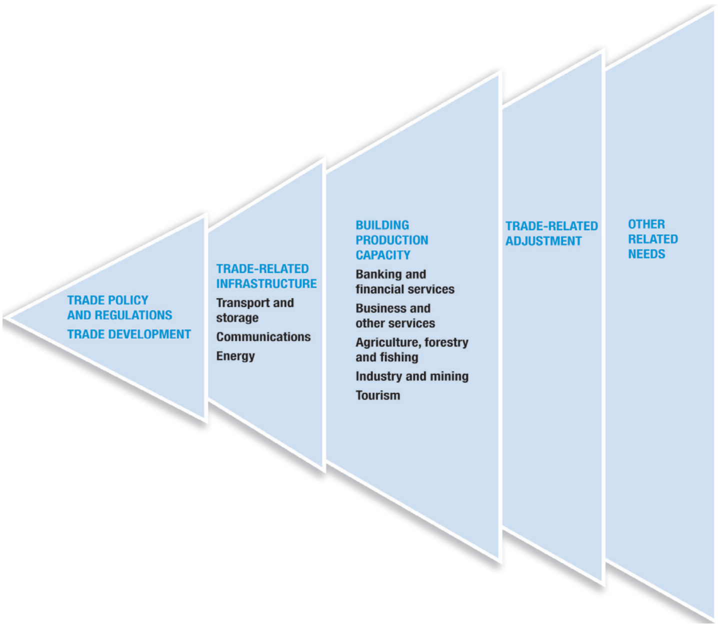
WHAT IS AID FOR TRADE?

The Aid-for-Trade Initiative aims to help developing countries overcome structural and capacity limitations that undermine their ability to maximise the benefits from trade opportunities. Upon concluding its work in 2006, the WTO Task Force on Aid for Trade stated that:

> *"Aid for trade is about assisting developing countries to increase exports of goods and services, to integrate into the multilateral trading system, and to benefit from liberalised trade and increased market access."* [1]

Aid for trade is not a new global development fund, nor a new aid category. On the contrary, aid for trade is an integral part of regular official development assistance (ODA) programmes. Donors have, in fact, been providing substantial amounts of aid to trade-related programmes for many years. All the while, the focus has expanded considerably. During the 1986-1994 Uruguay Round of trade negotiations, trade-related assistance was mainly aimed at technical support to help developing countries negotiate and implement trade agreements. Subsequently, the scope expanded to include building supply-side capacities, for instance in private sector development and trade-related infrastructure. Now, the agenda also includes trade-related structural adjustment programmes and other trade-related needs (*Figure 1*). In other words, aid for trade is a holistic approach which draws various themes together into a single framework.

FIGURE 1. **AID FOR TRADE: AN EXPANDING AGENDA**



1. Recommendations of the WTO Task Force on Aid for Trade [WT/AFT/1], 27 July 2006.

Trade is not a "sector" – it covers a wide range of activities and encompasses not just goods, but also services. Thus, the scope of aid for trade is likewise broad and not easily defined. For this reason, the Aid-for-Trade Initiative is based on setting objectives and producing results, e.g. building trade capacity, enhancing growth prospects and reducing poverty. It seeks to complement trade reforms (multilateral, regional or national) and promote more equitable distribution of global benefits across and within developing countries. The initiative is guided by the 2005 Paris Declaration on Aid Effectiveness, which emphasises local ownership as one of the key factors for effective aid. Consequently:

> *"Projects and programmes should be considered as aid for trade if these activities have been identified as trade-related development priorities in the recipient country's national development strategies." […] At the same time, clear […] benchmarks are necessary for reliable global monitoring of aid for trade efforts and […] to assess additionality."*

The benchmarks for measuring the volume of aid-for-trade flows and assessing additionality comprise ODA for:

- *Technical trade-related assistance:* for example, helping countries to develop trade strategies, negotiate trade agreements, and implement their outcomes;
- *Trade-related infrastructure:* for example, building roads, ports, and telecommunications networks that connect domestic markets to the global economy;
- *Productive capacity building* (including *trade development*): for example, providing support to allow industries and sectors to build on their comparative advantages and diversify their exports;
- *Trade-related adjustment assistance:* helping developing countries with the costs associated with trade liberalisation such as tariff reductions, preference erosion, or declining terms of trade;
- *Other trade-related needs:* if identified as trade-related development priorities in partner countries' national development strategies.

WHY DOES AID FOR TRADE MATTER?

There is a large and growing body of evidence that there are positive links between openness to trade and economic performance, which – depending on the pace and pattern of growth – is important for achieving sustained poverty reduction. This can be seen in the developing countries that have succeeded in benefitting from the expansion of global markets. Steady reduction in trade barriers – particularly in manufactured goods – has enabled these countries to rapidly integrate into world markets through an export-led industrialisation process, and thereby share in the prosperity generated by globalisation.

Opening up trade regimes and enhancing market access is often not sufficient, however, to enable developing countries – and in particular LDCs – to participate and reap all the potential benefits of trade liberalisation. These countries need help in building their trade-related capacity if they are to benefit. There is no doubt that this may sometimes require painful structural adjustment. Domestically, countries should begin by doing what is right for their economies, such as establishing sound economic frameworks, promoting business-friendly environments, developing human resources, and ensuring that the most vulnerable are protected.

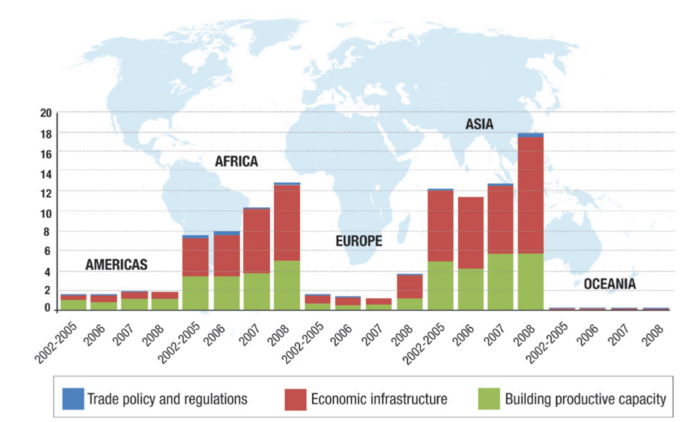
Aid for trade provides a coherent framework for supporting this broad range of objectives. In doing so, it can help developing countries grow and implement comprehensive export-oriented strategies that will benefit the poor. To be successful, these growth strategies need to cover numerous areas – many of them "behind the border". Only by doing so can they ensure that the benefits of export growth are distributed fairly.

Strengthening the linkages between trade and human development is very much part of the broader development agenda. In particular, this is an integral part of the global partnership for development mapped out by the Millennium Development Goals (goal number 8). Aid for trade underpins these objectives by strengthening the positive links between trade, economic growth and poverty reduction.

HOW MUCH AID FOR TRADE IS THERE?

The Aid-for-Trade Initiative has achieved remarkable progress in a short time: partner countries are increasingly prioritising trade in their development strategies and clarifying their needs by developing operational plans. Donors are improving aid-for-trade delivery and scaling up resources. In 2007, aid for trade grew by more than 20% per annum in real terms on the 2002-05 baseline. This was followed by a further 35% increase in 2008. Total new commitments from bilateral and multilateral donors in 2008 reached USD 41.7 billion, with an additional USD 25.7 billion in non-concessional trade-related financing. Furthermore, calculations suggest high disbursements of commitments – i.e. pledges are honoured as money is spent.

FIGURE 2. **GROWING REGIONAL AND SECTORAL AID FOR TRADE**
AVERAGE 2002–05, 2006, 2007 AND 2008
(COMMITMENTS, US DOLLARS, 2008 CONSTANT)



Source: OECD Creditor Reporting System

Donors are also on track to meet their aid-for-trade pledges, which – based on their indicative forward spending plans – will result in continued growth of aid for trade over the medium term.

The largest share of aid for trade continues to go to Asia (with 44%), although flows to Africa (with 35%) are also increasing steadily (*Figure 2*). Overall, the distribution of aid over the different trade-related categories has remained relatively stable over this period: economic infrastructure and productive capacity-building showed similar increases, with strong support going to trade development programmes and declining technical assistance for human and institutional capacity-building in trade policy and regulations.

IS AID FOR TRADE WORKING?

In the face of the worst economic crisis in generations, stakeholders are interested, more than ever, in finding out whether the Aid-for-Trade Initiative is producing the desired results. In particular, do country-owned trade strategies and donor-funded trade-related programmes actually build the capacity to improve trade performance and reduce poverty? How do we know we are on the right track? How can we learn from failure? How can we build a body of best practice? These are the kinds of questions that are being raised by stakeholders in developed and developing countries alike.

Measuring the impact of aid for trade is never going to be easy, given the difficulty in establishing the counterfactual (i.e. testing the opposite hypothesis) and because of the other factors which may come into play (political, economic, social). For this reason, case-studies about the relationship between aid for trade and trade performance present a useful way of establishing what works, what doesn't work, where improvements are needed and what type of impacts aid for trade can have. To date, a limited number of these studies have been conducted – and more are called for. Much more analysis has been undertaken to clarify the links between trade, growth and poverty, but this now needs to be complemented by efforts to measure results and evaluate outcomes.

A number of donors have recently evaluated their programmes and most have concluded that while direct effects on export (growth) volumes are likely, they are complex to substantiate. The most widely cited positive outcomes include improved understanding of the potential contribution trade can make to development, increased awareness and knowledge of trade policy issues, and strengthened national dialogue.

There exists a growing consensus on the real and overall positive benefits countries can gain by opening up their economies, despite differences of opinion among researchers on the questions of "how" and "why". Indeed, the weight of evidence indicates clearly that greater openness is an important element in growth performance and has been a central feature of successful development. By encouraging this opening and addressing the constraints that can prevent its benefits from flowing through the economy, aid for trade has a critical supporting role to play.

WHAT ARE GOOD PRACTICES?

While aid for trade shares many of the same challenges inherent to all aid delivery and management, five broad challenges are particularly pertinent to the effective delivery of aid for trade:

➔ *Getting the co-ordination right: mainstreaming trade into development strategies*

Trade encompasses all sectors of the economy. The complexity of trade and its interdependence with a country's overall development makes mainstreaming essential. The critical issue is how to reflect that interdependence by mainstreaming trade into national development plans and poverty reduction strategies. Most governments recognise the crucial role trade plays. Fewer though have operational strategies that seek to proactively harness the potential of integration into regional and multilateral trading systems for economic growth and development. And if trade is not signalled as a priority in the national strategy, the donor community will focus on other needs which do reflect national priorities. Aid-for-trade needs are not enough; those needs must be expressed in an operationally effective way. This reflects a broader need for a whole-of-government approach and effective dialogue with stakeholders in the formulation of trade and development policy to exploit synergies and minimise inconsistencies between the trade development agenda and other economic and social policies. For LDCs, the Enhanced Integrated Framework can play a central role in this regard[2].

➔ *Getting the diagnostics right: from needs to binding constraints*

Developing countries typically suffer from multifaceted supply-side constraints, such as poor infrastructure, limited access to finance and technology, and lack of human and institutional capacities. It is unrealistic, however, to address these needs all at once for political economy, capacity and financial reasons. In fact, even when external finance is available, domestic absorption capacity is often limited. It is, therefore, imperative that the binding constraints to trade development are prioritised and that aid for trade is structured so that it focuses on addressing the bottlenecks that seem most likely to lift trade and boost productivity. Focusing on priority actions demands political leadership and requires joint analytical work by government officials, private sector representatives, academics and other experts, as well as the active engagement of the development community around a reform agenda.

➔ *Getting the political economy right: the feasibility of reforms*

Successful integration into the world economy demands considerable reforms. There are very few instances where the binding constraints are solely physical, resolved by a small number of large-scale investments in infrastructure. Trade reform can challenge vested interests. In developing their aid-for-trade strategies, reformers should include the objective of strengthening the constituency for reform. Engaging the private sector is critical in this regard. Issues – such as finding the right sequence of reforms, implementing complementary policies to amplify the growth and poverty impact of trade, piloting projects to showcase the benefits, and accompanying reforms with adjustment support – need to be fully integrated into implementation plans in order to ensure the effectiveness of aid for trade.

➔ *Getting the delivery right: the Paris Declaration on Aid Effectiveness*

Experience in both developing and developed countries' public sectors has shown that complex assistance programmes – if designed

2. The Enhanced Integrated Framework is an initiative of six multilateral institutions (IMF, ITC, UNCTAD, UNDP, World Bank, and the WTO). It aims to integrate trade in LDCs development strategy, and to help the delivery of trade-related technical assistance in response to needs identified by each LDC. See *http://www.integratedframework.org/*.

incorrectly – can consume large amounts of administrative resources and overburden already stretched human and institutional capacities. What was originally meant to help, ends up actually hindering. Over the last two decades, the development community has developed a growing body of good practice on delivering aid effectively. The principles set out in the Paris Declaration on Aid Effectiveness – such as local ownership, harmonisation and alignment, management for results, and mutual accountability – should underpin the design and implementation of effective aid-for-trade projects and programmes.

➔ *Getting the regional dimension right: strengthening capacities*

Regional projects – like building cross-border infrastructure – can serve as a powerful catalyst for economic growth. Addressing supply-side constraints at the regional level – such as transport infrastructure, trade facilitation and standards – can encourage economies of scale and reduce vulnerability to external shocks by diversifying export markets. In some regions, however, there is a lack of articulated demands and priorities, coherence between national and regional programmes, or effective co-ordination. All of this impedes the ability of developing countries to fully capture the potential benefits of regional trade. Thus, aid for trade should address regional binding constraints and build institutional and human capacities at the regional level.

WHAT IS NEXT?

The Aid-for-Trade Initiative is succeeding in mobilising more and better aid for trade. Maintaining momentum, however, particularly in light of the economic crisis, hinges on the implementation of the work programme agreed for 2010-11, and more broadly on three priority areas:

➔ *Strengthen the arguments*

It is important to show that aid for trade is worth doing. Gathering evidence of the positive impact of aid for trade on trade performance should be emphasised, which should include results that demonstrate the relationship between openness to trade on the one side, and welfare gains and poverty reduction on the other. Furthermore, it is important to show that aid for trade is part of a larger picture, encompassing international co-operation, improved policy coherence and a whole-of-government approach to economic development and poverty reduction.

➔ *Manage for results*

As highlighted in the joint OECD-WTO Aid for Trade at a Glance 2009 report, progress has been made in the delivery of aid for trade. But more remains to be done. Country ownership (including broadening ownership of aid for trade beyond the trade ministry) and results-based management are far from being systematically applied. The active involvement of the private sector – which is essential to identifying the real binding constraints to trade, as well as to making local officials accountable for results – is also wanting.

➔ *Get the right information*

The 2008 Accra Agenda for Action stresses the need to improve mutual accountability and develop incentives for effectively monitoring and evaluating development results. As more aid resources get channelled into activities aimed at building developing countries' trade capacity, concrete evidence that demonstrates the effectiveness of such activities has become crucial. More needs to be learnt about what does and does not work, and why – building on the experience of developing countries that are both succeeding and seeking to reach out to other developing countries. We need indicators to track the implementation and impact of aid for trade. Moreover, performance information should be an integral part of managing aid-for-trade activities. Getting the right information is, thus, essential.

The OECD and the WTO attach great importance to this agenda and will continue to work closely together and with other stakeholders to make aid for trade an effective tool for a stronger, cleaner and fairer world economy.

FURTHER READING

OECD (2006), *Aid for Trade: Making it Effective*, OECD, Paris.

OECD (2006), *Trading Up: Economic Perspectives on Development Issues in the Multilateral Trading System*, OECD, Paris.

OECD (2007), *Trade-Related Assistance: What Do Recent Evaluations Tell Us?*, OECD, Paris.

OECD/WTO (2007), *Aid for Trade at a Glance 2007*, OECD, Paris.

OECD/WTO (2009), *Aid for Trade at a Glance 2009*, OECD, Paris.

OECD (2009), *Trading out of Poverty: How Aid for Trade can Help*, OECD, Paris.

OECD (2009), *Binding Constraints to Trade Expansion: Aid for Trade Objectives and Diagnostics Tools*, OECD, Paris.

OECD (2010) *Increasing the Impact of Trade Expansion on Growth: Lessons from Trade Reforms for the Design of Aid for Trade*, OECD, Paris.

OECD website: *www.oecd.org/dac/aft*

WTO website: *www.wto.org/english/tratop_e/devel_e/a4t_e/aid4trade_e.htm*

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