Ministry of Foreign Affairs

IOB Study Newsletter
14 04

Autonomy, partnership and beyond: An analysis of policy coherence for Ghana

Over the past decades, awareness has increased among OECD countries that non-aid policies might conflict with aid policies. This realisation has led to a call for better coordination across different policy fields, referred to as Policy Coherence for Development (PCD). Areas of interest include trade, migration, finance and environment. It is difficult to assess the coherency of policies in practice, however.

This IOB study outlines the results of a pilot for analysing the options for coherence of Dutch and EU policies for development objectives in Ghana. The study uses scenarios to estimate the potential effects of Dutch and EU policies. A major conclusion is that in the short run the effects of non-aid policies are quite limited, at least in quantitative terms. Migration policies are an exception. In addition, ending Ghana's free access to the European market would also have a major negative impact on income.

Background

Aware of the cost of incoherence and the benefits of more coherent policies, development partners in EU and OECD increasingly pay attention to the topic of Policy Coherence for Development (PCD). OECD defines PCD as 'working to ensure that the objectives and results of a government's development policies are not undermined by other policies of that government which impact on developing countries, and that these other policies support development objectives, where feasible'.

While PCD is not a new area of focus, it is difficult to assess the coherency of policies in practice. IOB has therefore asked the Centre for World Food Studies at VU University Amsterdam (SOW-VU) and researchers from the University of Ghana to develop a model to assess the options for coherence of Dutch and European policies. This study analyses the short-term impacts of Dutch and EU policies in the areas of aid, trade, agriculture, taxation, migration and the environment for Ghana.

Approach

The study uses counterfactual analysis, 'what if scenarios', to analyse the coherence of Dutch and EU policies. The scenarios reflect specific policy changes by the Netherlands and the EU as well as potential reactions from the Ghanaian government. An Applied Welfare Model is used to check the consistency of the scenarios and to calculate the impact on Ghana.

The study is retrospective: it looks back at Ghana's development in the period 2006-2011 and focuses on the welfare effects. The applied welfare model and the social accounting matrix are useful for analysing substantial policy changes. Nevertheless, results crucially depend upon the underlying economic structure. It must also be emphasised that an assessment of longer term impacts, caused by more dynamic changes in the economy, is outside the scope of the study.

Development cooperation

The Netherlands was one of Ghana's main donors during the period 2006–2011. Average total aid amounted to about EUR 73 million annually, mainly through general budget support and support to the health and environment sectors. The Netherlands also supported initiatives related to education, water, gender, governance and private sector development. In 2007 the Netherlands accounted for 13% of Ghana's total official development assistance (ODA); this has been reduced to 2%.

In order to assess the impact of reduced ODA, the team simulated the effect of an annual reduction of EUR 50 million from 2006 onwards. Assuming that all aid has been spent effectively, this would result in a per capita income in 2011 that would be nominally lower (1.6% over five years). This amounts to a lower real per capita growth rate of almost 0.2%.

Trade

The traditional aid relation between the Netherlands and Ghana is becoming more and more a trade relation. Dutch exports to Ghana have increased from EUR 336 million in 2010 to EUR 1.2 billion in 2012.Exports from Ghana to the Netherlands have increased as well. They mainly consist of cacao. In 2011 and 2012, the export of bauxite and oil gained importance.

For an assessment of the coherence of trade relations, the study analysed the potential impact of the Economic Partnership Agreement (EPA). The EU aims to conclude these agreements with all ACP countries (African, Caribbean and Pacific Group of States). According to the EU, ACP countries will benefit from enhanced market access and increased trade volumes. ACP countries fear that gradually abolishing the protection of national industries might have a negative impact on local companies and reduce fiscal revenue.

The first scenario assumes that Ghana and the EU signed the EPA in 2006 and that Ghana already started liberalising its own imports from the EU from 2006 onwards. Ghana would continue to have free access to the European market. According to the model estimates, there would be a small positive effect of 0.2%, but the effects differ substantially between regions, with the southern regions benefitting and the northern regions suffering.

An alternative scenario assumes that the EU and Ghana would not sign an EPA and that exports of several products to the EU would have faced tariffs from 2008 onwards. This scenario predicts severe losses: nominal per capita incomes in 2011 would be on average 2.9% lower.

Reduced market protection in the EU

Since 1992, the EU has gradually replaced its system of domestic price support in agriculture with a system of income support for farmers. Currently, about 90% of payments are decoupled from production. Nevertheless, reducing EU tariffs on agricultural imports may have an impact on Ghana, even though exporters from the country are exempted from EU tariff restrictions. Ghana's economy may be affected indirectly by changes in world market prices.

To assess the potential impact, the team analysed a scenario with lower import tariffs in the period under consideration (2006–2011).[1] The effects of this scenario on Ghana would be minor. In the short run, Ghanaian and EU farmers would not compete in the same (export) markets. However, changing world food prices might affect consumer behaviour. Higher prices for agricultural produce from Europe tend to reduce consumer demand for manufactured goods and services in Ghana.

[1] The scenario does not include the impact of farmer income support.

Bilateral tax treaty

In the Netherlands, there has been a debate about the impact of tax treaties on developing countries. A recent IOB study concluded that tax avoidance strategies, facilitated by Dutch corporate tax policy, do in fact have a negative impact on tax revenue in these countries.[2] The Netherlands has become one of the main foreign investors in Ghana. To a large extent, these investments are the result of special purpose entities (SPEs) created by multinationals to establish a business-friendly tax climate.

A strong increase in foreign direct investment (FDI) by SPEs in 2009 and 2010 suggests that this was caused by the tax treaty that the Netherlands and Ghana signed in 2008. However, this increase coincided with the discovery of oil. Nevertheless, the treaty has an effect on government revenue, as it reduced withholding taxes from 8% to 5%.

If the treaty had gone into effect in 2007, it would have reduced income by 0.04% (during the period 2006–2011). A minor increase in FDI of €15 million annually from 2007 to 2009 would have been enough to offset the negative impact.

Migration

The Netherlands and other EU countries have tightened immigration restrictions, and this may have a major impact on developing countries. Europe is home to about 225,000 first-generation migrants from Ghana. In order to assess the impact of stricter policies, a first scenario assumes that 12,500 (illegal) migrants from Ghana were sent back to Ghana in 2006. This would have resulted in a decrease in per capita income of 0.1 % (because of lower remittances, estimated at EUR 1,500 per person per year).

A second scenario assesses the impact of the brain drain. While European countries have tightened restrictions on low-skilled migration, the EU has made progress facilitating the immigration of highly skilled workers.

The scenario estimates the impact of an assumed brain drain of 10,000 highly skilled migrants in 2006. The simulations show that the consequences of the loss of human capital outweigh the benefits of the additional remittances. While skilled migrants send home EUR 3,000 per person annually, the loss in value added in 2011 would appear to be about EUR 9,000 per migrant. In this scenario, the (nominal) per capita income in Ghana in 2011 would be 0.25% lower. This confirms the conclusion of other studies that the negative effect of the emigration of skilled labour is higher than the combined effect of remittances and unskilled emigration.

[2] IOB (2013). *Evaluation issues in financing for development: Analyzing effects of Dutch corporate tax policy on developing countries.* The Hague: Ministry of Foreign Affairs.

Environment

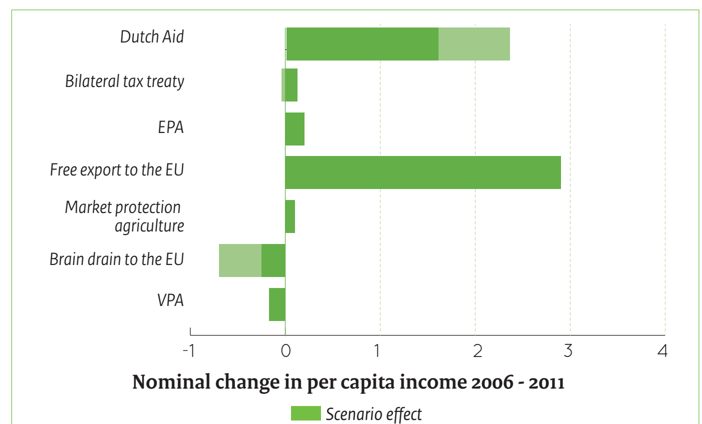
The environment and climate change are gaining importance in Dutch and EU policies. Voluntary Partnership Agreements (VPAs) are an example. In order to stop unwarranted deforestation, the EU has set up VPAs with a number of countries. In 2010, Ghana was the first country to ratify a VPA with the EU. Huge timber exports have led to concerns about the sustainability of Ghana's forestry sector.

In order to assess the short-term effects, the study simulated the direct economic impact of a situation where a licensing system would have been operational already in 2007. This scenario predicts that output would have been 25% lower than it actually was and assumes that export prices would have been 10% higher. The impact on per capita income would be minor in such a short period of time, as the reduction in wood output is largely offset by higher wood prices, and also by the movement of labour to other sectors. Overall in Ghana, the effect in 2011 would be a decrease in per capita income of 0.17%.

Conclusion

The pilot shows that the simulation of counterfactual scenarios with an Applied Welfare Model is useful for analysing coherence options. Figure 1 summarises the results and gives the cumulative nominal effects of Dutch and EU policies over a five-year period (2006–2011).

Figure 1 *Impact of policies for Ghana*



Note: *calculated scenario effects are dark green. The whole bar gives the IOB estimate of the total effect. The scenario for instance was based on a reduction of 65% of total aid and therefore the total effect is higher.*

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IOB Study 394 (May 2014)
Autonomy, partnership and beyond: A counterfactual analysis of policy coherence for Ghana
ISBN 978-90-5328-459-9
This report can be downloaded at:
www.government.nl/foreign-policy-evaluations
www.iob-evaluatie.nl

For Ghana, the short-term impact of non-aid policies of the Netherlands and the EU seems to be rather limited and sometimes even counter-intuitive. This means that one cannot expect more coherent policies to have a strong impact on the country's welfare in the short run. There are two exceptions to this conclusion. First, migration policies that restrict the immigration of unskilled workers but accept the influx of skilled migrants are clearly incoherent and conflict with development objectives. Second, ending Ghana's free access to the European market would have a major negative impact on per capita income. Overall, aid remains one of the most important instruments for poverty reduction in a country like Ghana. It should also be noted that structural effects in the long run have not been analysed.

Published by: Ministry of Foreign Affairs of the Netherlands | Policy and Operations Evaluation Department (IOB)
P.O. Box 20061 | 2500 EB The Hague | The Netherlands | www.government.nl/foreign-policy-evaluations | www.iob-evaluatie.nl
© Ministry of Foreign Affairs of the Netherlands | May 2014 | ISSN: 2214-6407 | 14BUZ624953|E