THE ROLE OF EXPORT DIVERSIFICATION FOR ECONOMIC GROWTH AND EMPLOYMENT CREATION IN AFRICA

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Introduction

Export growth plays an important role in the economy due to its effect on trade growth and economic growth. Therefore, the sustainability of export growth rate is an eligible target for any country. The globalization phenomenon and openness to trade under uncertain circumstances, for example, the global financial crisis in the late 2008, may introduce uncertainties and fluctuations in the export earnings which discourage the investment opportunities. Discouraging investment opportunities leads to instability in export growth which reflects negatively to economic growth. Most research has established that export diversification is the effective remedy for these uncertainties due to its pivotal role in avoiding the shortfalls in export concentration. Most African countries in recent years, has been therefore, making efforts to diversify their economies to processing and manufacturing sectors. In addition to reducing the dependence on few commodities whose prices fluctuates in the international market, diversification into other sectors, especially those more intensive in technology, is prone to trigger knowledge spill overs from the exposure to international markets, management and marketing practices and production processes.

The real test of the AfCFTA will be how quickly African countries can accelerate export diversification and product sophistication and make trade more inclusive. AfCFTA is expected to enable African countries to break into new African markets as they both diversify by export destination and type of goods produced.

The objective of this paper is to discuss major determinants and challenges of export diversification and to propose export diversification and employment strategies for Africa.

This paper is organized as follows. Section one provides brief Empirical review of the relationship between export diversification, employment and economic growth. Section two discusses major determinants. Section three discusses challenges of export diversification. Section four, provides overview of export diversification efforts of selected African countries. Section five briefly discusses lessons on export diversification and employment strategies of emerging market. Finally policy recommendations will be made.

Empirical Review of the Relationship between Export Diversification Employment and Economic Growth

A major implication of classical theories of trade is that African countries would specialize in exporting commodities in which they enjoyed comparative advantage and import manufactured goods. However, one of the early studies on the subject by Michaely (1958) challenged the classical view. His study provided support for export diversification based on the finding that economies with more diversified export structure were more developed in terms of income per capita. The study also found that export diversification yielded greater support for stablising export earnings in the longer run, with favourable implication for employment. This result was later corroborated by Ghosh and Ostry (1994) and Bleany and Greenway (2001). More recently, Mathee and Naude (2008) has provided empirical; evidence to buttress the need for African countries to diversify their exports. Subjective evidence suggests that almost there are no current developed countries with extremely high level of export concentration (Agosin, Alvarez and Bravo - Ortega (2009). Brenton, Newfarmer and Walkenhorst (2007) argued that export diversification makes countries to be less susceptible to adverse terms of trade shocks by stabilizing export revenues. As a result, it becomes easier to channel positive terms of trade shocks into growth, knowledge spill-overs and increasing return to scale, creating learning opportunities principal to new forms of comparative advantage. C. Mudenda, I. Choga and C. Chigamba, (2014) examined the role of export diversification on economic Growth in South Africa. Results of the study reveal that export diversification and trade openness are positively related to economic growth.

Major Determinants of Export Diversification

Prominent among determinants which have been investigated include human capital, exchange rate, geographical location, investment, terms of trade, population and governance factors.

Human Capital: The level of qualifications of the workforce and the efforts made in education have a relevant influence on the capability of a country to diversify, innovate, upgrade to high technology, in production of quality and sophistication of exports and also in promoting product differentiation. Production of new products requires research and development. Human knowledge is important in the research of new, efficient and affordable production method.

Investment: Acquiring new markets for products entails need to expand and diversify exports to high value markets in the industrialised countries. Part of the strategy is to put in place policies that attract more foreign direct investment (FDI) in order to facilitate more technology transfer. This needs to improve business regulations and governance environment for business. FDI was found to be a factor to speed up export diversification in countries that devoted significant amount of investment in education, health, and infrastructure as these will in turn create a better conducive atmosphere for FDI inflows. Domestic private sector investment diversification strategy also helps in shifting the composition of exports from primary products, to manufactured products.

Geographical location: Remoteness increases export concentration. Parteka and Tamberi (2008) using a sample of developed and developing countries found that transport costs discourage export diversification. A lower distance to the main world markets, access to the sea and overall transport costs, determine the ease with which a nation can increase the variety of products exported to the world market.

Terms of Trade: Theoretical and empirical literature suggests that failure to sustain industries with important internal and external economies of scale, and positive externalities of agglomeration of economic activity might limit African continent's efforts towards a more diversified exports. This suggests that efforts towards a regional integration, by increasing the economic size in which Africa business companies can operate, might play an important role to successful export diversification. Elhiraika et al, (2014) Binti (2011) argues that economic integration in East Asian Countries has led to faster export diversification in the region. Again regional integration could facilitate commercial activities through reforming trade through improved customs procedures and cross-border entrepreneurship and trade.

Population: When the population of a country increases in terms of variety of consumers, this will lead to increased production of more diverse products that attend to the need of varied users/consumers. Further, the size of a countries economy, i.e. population, education, health, infrastructure and income per capita are crucial factors that can be used as factor inputs in the manufacture of diversified products.

Exchange Rate: Exchange rate volatility, especially the over valuation of currency can discourage diversification by increasing the prices of exports and undermining the competitiveness of the export sector.

Challenges of Export Diversification

Challenges for Export Diversification are classified in the literature into challenges due to domestic factors; policies and institutional arrangements; and to external factors. Challenges due to domestic factors include: training and quality of labour force; gaps in infrastructure and other logistics; access to and cost of finance; product quality; technology acquisition and adoption; marketing and cost of production. Policy and institutional factors include among others, tariffs, fiscal policy; exchange rate policy; monetary policy; access to and cost of finance; legal enforcement of laws; and lack of appropriate business environment etc.. External factors include among others, meeting international standards, entry barriers to international market; access to information on external market; and cost of operating in foreign markets.

Experiences in National Economic Diversification in Africa

The continents four most advanced economies, namely Egypt, Morocco, South Africa and Tunisia are already broadly diversified. Manufacturing and services together total 83%of their combined GDP. Domestic consumption is the largest contributor to growth in these countries. Cameroun, Ghana, Kenya, Mozambique, Senegal , Tanzania, Uganda and Zambia are some of the transition economies which have began diversifying their sources of growth. Kenya for example increasingly export manufactured goods particularly to other African countries. Expanding intra-Africa trade will be one key factor to the future growth of countries which are in transition to diversify their economies. Speedy implementation of AfCFTA will particularly enhance the diversification of African countries economies.

Lessons from Export Diversification and Employment Strategies of Emerging Markets

There are a number of countries that have made significant progress on export diversification over the years and have reaped the benefits of its positive effect on employment and growth. Some of these countries for example South Korea was either on the same socio-economic development level with most African countries a few decades ago. South Korea had export structures similar to Africa's in the early 1960s. However, the country had experienced profound transformation of its export structure and base, with manufactures and other high value exports dominating its export basket as far back as early 1980s . Key policy measures adopted by South Korea for promotion and diversification of exports were exchange rate unification and devaluation, tax exemption as an incentive to encourage production of a wide variety of commodities for exports, financing through preferential credit schemes, cash subsidy and subsidy for the use of public utilities which were provided to exporters, export -import links scheme to increase knowledge and awareness of export opportunities through Korea Trade Promotion Corporation (KOTRA) established in 1964. As a result, according to World Bank's World Development Indicators database, South Korea ranks consistently in the top ten exporting countries in the world for many years. It has also maintained very low unemployment rates that averaged 2.5% between 1991 and 2016. The country easily and successfully weathered the storm of the Asian financial crisis because it has developed strong capacity for rapid export response and adjustment.

Brazil is another emerging country which successfully diversified its exports. Financial instruments were the main tools used to promote export diversification. Credit and export credit insurance are the two key instruments that the country had widely employed in this respect. Advance payment under foreign exchange contract is another important financial support provided to encourage exporters. The National Bank for Economic and Social Development, popularly known as BNDES, has also been extensively used as an export financing channel to promote export diversification in Brazil. Strong institutional support and investment in R&D were also used to support export diversification. Today Brazil ranks as the 21st largest export economy in the world

Policy Recommendations

The key to ensure the diversification of exports is to ensure that a conducive environment is created in order to minimize the risk of undertaking relatively productive long term investment for it is such investment that is likely to yield export diversification for sustained growth and employment creation in Africa and LDCs. The following are key policy recommendations for different stakeholders on what needs to be done to improve export diversification particularly in Africa and LDCs with positive implication for employment:

a) National Policy makers should develop the following:

(i) A capable, accountable, developmental and transformational state which is conducive to private sector participation in promoting export diversification.

(ii) Strategic national and regional infrastructure by formulating best infrastructure policies that will lower costs of doing business and promote globally competitive exports. These will attract domestic and foreign investment to various sectors for expanding production for commodities for exports. Since many African countries are not big enough, one possible way to handle this challenge is for African countries to collectively promote regional infrastructure, in order to reduce business risks, uncertainties, and export costs. Such cooperation could also contribute to expanding regional markets and deepening regional integration among the countries.

(iii) Innovative financing schemes to provide finance for export oriented firms such as direct credit incentives, and selective subsidies that target export-oriented firms. Priority should be given to potentially new export sectors that hold high promise for expanding the export horizon of African countries in particular and LDCs in general. Such subsidies should be structured in such a way that they do not encourage rent-seeking behaviors but rather benefit working capital

(iv) Developing an integrated African economies into the global value chain(GVS). Africa's share in GVS remains the lowest among all the developing regions of the world. A relatively more convenient starting point is with regional value chain integration as a stepping stone.

(v) Strengthen the institutional and regulatory framework.

(vi) Support SMEs to access export markets.

(vii) Initiate industrial development policies that are capable of facilitating vertical and horizontal export diversification.

(viii) Investing in human capital.

b) Continental, regional and sub-regional Institutions should undertake the following:

(i) Take the lead in coordinating regional infrastructure development;

(ii) Assist member countries to initiate continental export diversification policy;

(iii) Promote trade facilitation;

(iv) Explore innovative financing options that could compliment the traditional export diversification financing instruments, such as structured financing;

c) Private sector businesses should undertake the following:

(i) Take full advantage of export promoting incentives provided by government.

((ii) Initiate public-private-partnership(PPP) export diversification projects and infrastructure financing;

d) Development partners should undertake the following:

(i) Use ODA to build export promoting and diversifying capabilities;

(ii) Finding ways in which to relieve LDCs from WTO rules which constrain these countries such as TRIMS and TRIPS agreements.