

THE IMPACT OF TRADE LIBERALIZATION ON ECONOMIC GROWTH; THE CASE OF SUB-SAHARAN AFRICA

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Abstract: The main aim of this research is to explore the effect of trade liberalization on economic growth in sub-Saharan Africa by analyzing certain macro-economic indicators using Ordinary Least Squares approach to estimate regression equations. Many developing countries have substantially liberalized their trade regime over the past three decades, either unilaterally or as part of multilateral initiatives. Nevertheless, trade barriers remain high in many developing countries. One of the concerns that attributes to the reluctance of many of these countries to liberalize their trade regime is the possible worsening of the trade balance.

This research paper is meant to give a recommendation on which macro-economic indicators sub-Saharan African countries should pay particular attention to, implementing the necessary policies to ensure its effectiveness thereby ensuring a step-up in those aspects of the economy in order to promote development. It considers 46 different countries with different economic policies in sub-Saharan Africa for a 14-year period. Most papers considering sub-Saharan African region consider a selected few countries based on certain economic reasons of their choice, and those who consider most countries in the region have different macroeconomic indicators they employ for their modeling. This paper considers if not all, almost all sub-Saharan African countries regardless of their economic status.

Keywords: Trade Liberalization, Economic Growth, Sub-Saharan Africa.

1. INTRODUCTION

Trade is generally considered to have a beneficial impact on economic growth. However, the spatial distribution of the benefits of trade remains questioned and debated. Different theories and empirical analysis often reach contrasting results on the spatial economic impact of trade.

Trade liberalization is defined as the continual elimination and/or removal of hitches created mainly by government policies, regulations and administrative procedures that hamper the free flow of goods, services, and capital from one frontier to another (Agboola, 2004).

According to Wacziarg and Welch's (2008), 49 countries liberalized their economy between 1990 and 2001. For several decades, Sub-Saharan countries pursued import substitution plan and implemented series of trade restrictiveness policies that include high level of tariff, non –tariff barriers, and exchange rate controls along with established state owned enterprises.

Africa is the world's poorest continent (Basu *et al.*, 2005). The economic and social situation in sub-Saharan Africa remains fragile and vulnerable to domestic and external shocks (Ulku, 2004). Investment remains subdued and it is limiting efforts to vary economic structures and enhance growth (Nkurunziza and Bates, 2004). Furthermore, a number of

countries have only emerged from civil wars that have severely affected their development efforts while in other parts of the continent, new-armed conflicts have flared up (Basu *et al.*, 2005).

As seen in many countries, the chief motive of governments particularly in recent years is to obtain high and sustainable economic growth in order to prevail in a competitive world of trade relations (Manni and Afzal, 2012). In attaining this principled goal, countries in Sub-Saharan Africa have boarded themselves in current economic policies which ensure reduction and deletion of trade barriers like tariffs, quotas and import controls just to mention but a few. One common policy that most Sub-Saharan African countries have decided to cling to is trade liberalization of economies (Herath, 2010).

2. LITERATURE REVIEW

2.1 CONDITIONALITY, NATURAL AND INSTITUTIONAL BARRIERS TO TRADE

To argue that technological improvements are country-specific is a rather extreme view; in its place, Basu and Weil (1998) suggest that there are certain groups of countries that share the same technology. Finally, Kneller (2005) argued that distance summarizes the effect of international technology transfer through channels such as international trade and FDI. Some conditional factors discussed by Winters (2004) and others comprise geographic and institutional factors. The geographic variables discovered within productivity regressions have involved latitude, as well as climatic measures such as whether a country is tropical as well as the level of rainfall. These variables might be best thought of as seizing a number of different effects. Most noticeable amongst these is the direct effect of climate on public health and the quality of human resources and might also capture the effect of appropriate technology however, the idea being that the technical frontier does not move out regularly across its surface but is partial towards certain factors of production (Acemoglu and Zilibotti, 2001). The yields to technology may thus differ in a case where the choice of input mix of countries differs too.

2.2 BENEFITS OF OPEN MARKETS

Trade and foreign direct investment are main engines of growth for developed and developing countries equally. Domestic output has steadily been beaten by trade. Trade and investment encouraged market combination and has led to stronger forms of economic interdependence among many nations, as a growing number of developing and former centrally planned economies tend to link to the global economy more closely. One of these is due to individuals and companies engaging in specialization and exchange, where a country will achieve its comparative advantage. The case for open markets respites on strong foundations. It will dedicate its industrial, human, natural and financial resources to be used in the best way. As a result, firms and consumers will have gains alike. Also, there is the solid preference of people the world overshadows for more, rather than a reduced level of choice of freedom. A more open domestic market is actually not a handicap but rather a source of competitive strength. Acquaintance to international trade is an influential spur to efficiency and efficiency in turn, backs economic growth and growing incomes, hence liberalization benefiting citizens in ways that are tangible.

With reference to Tussie and Aggio (2011), Malawi and Zambia started trade and economic alterations in the mid-1980s but these were pursued more forcefully during the 1990s. They presently stand out after methodically monitoring the SAP agenda endorsed by the international institutions and relatively speaking, as two of the most liberalized economies in the region. In Zambia's case, a portion of the clarification for its unfortunate economic performance lies in the failure of the international copper price, since it heavily depends on the production and export of this sole commodity. In 2002, copper accounted for nearly 68 per cent of its total exports, contributed about 8 per cent to its GDP and represented a significant source of economic revenue. Additionally, they benefit from privileged access to the two major world markets; the EU and the United States. Modern economic performance has been substandard as a result of their low capacity to create real economic growth. Supply-side restrictions have been one of the major problems, averting them from taking complete advantage of numerous preferential schemes. From the year 1990 to 2002, the value of Zambian non-traditional exports increased from \$90 million to \$360 million, demonstrating an increase in their portion of export earnings from 8 per cent in 1990 to 39 percent in 2002. Nonetheless, the shrinkage in output of formerly protected industries has not been compensated by an adequately dynamic improvement of its export industries.

Social indicators have received negative impact from the reforms. It is necessary for comprehensive improvements to challenge supply-side restrictions and other holdups which include poor infrastructure and transportation. Non-agricultural accomplishments are almost non-existent, and therefore the challenge is to generate and improve an industrial sector that can withstand competition internationally. Poverty lessening remains the main challenge for these countries, all of which are severely reliant on exports for economic development. Furthermore, liberalization under NAMA (Non-Agricultural Market Access) is possible to pose extra challenges if it wears away the preferential access of these countries to vital world markets. The World Bank (2003) summarizes the performance of Zambia’s social and economic indicators as follows: “The country saw significant progress in the area of structural reforms during the 1990s but full macroeconomic stability and sustainable growth proved elusive. All the social and educational indicators deteriorated. Infant mortality rates, adult illiteracy, malnutrition and poverty remained very high.”

3. METHODOLOGY

The mathematical equation of the model is;

$$LnRGDP = \beta_0 + \beta_1 EX + \mu \dots \dots \dots (1)$$

$$LnRGDP = \beta_0 + \beta_2 EX + \beta_3 IM - \beta_1 ER - \beta_4 LnIR + \mu \dots \dots \dots (2)$$

Hypothesis: $H_0: \beta_1 = 0$

$H_0: \beta_1 \neq 0$

Where;

GDP = Gross Domestic Product

EX = Exports

IM = Imports

ER = Exchange Rate

IR = Interest Rate

μ = Error term

β s = represents parameters of variables

4. ANALYSIS OF RESULTS

After running the data with STATA the main independent variable EXPORT RATE came out positive. The stable wealth and high income by some few countries in Africa may have had effect to this. This depicts how the value of export in many countries in Sub-Saharan Africa has a direct impact on their economic growth.

$$GDP = 5.687492 + 0.001146 EX + 0.0024687 IM -$$

(0.7800356) (0.0003253) (0.0012165)

$$4.435038ER - 0.476136 IR$$

(1.894654) (0.197589)

N = 630 R-squared = 0.0537 ADJUSTED R-squared = 0.0476 DFR = 630

4.1 *T-test*

T value = 4.77

Critical Value for a two-tailed test at 5% significant level = 1.960

Since T-value is greater than Critical value, we reject the null.

4.1 *F-test*

F-value = 8.85

Critical Value for a two-tailed at 5% significant level = 2.37

Since F-value is greater than Critical Value, we reject the null

After running the regression model with STATA software, the results clearly indicates that in Sub-Saharan African economy, a unit increase in exports will increase GDP by 0.00246871 and also one unit increase in import will increase GDP by 0.00246871. With reference to other literature as indicated in the previous chapter, this is also a confirmation to the fact that economic growth in Sub-Saharan African countries are mostly dependent on exports and imports, hence a positive relationship.

On the other hand, a unit increase in exchange rate as well as interest rate will reduce GDP by 4.435038 and 0.476136 respectively. It is no surprise that these two macroeconomic indicators don't have a positive correlation between themselves and GDP. Other literatures as referred to, like the study by Abbas et al; 2012, show that there is an insignificant relationship between GDP and exchange rate as well as interest rate.

5. CONCLUSIONS AND RECOMMENDATION

The result of the regression clearly shows exports and imports have positive effect on Gross Domestic Product, while exchange rate and interest rate on the other hand have a negative effect on GDP. Which means the major drive for a boost in economic growth is mainly impacted by exports and imports. This is an indication that countries in sub-Saharan Africa should have their government focus on exports and imports, giving them most of their attention and implementing trade policies around these indicators in order to see major improvement in their economic growth. Both real exports and imports had increased with greater openness, which in turn, had eventually led to economic growth, relating to other variables on the other hand, exchange and inflation rate were did not prove that.

Researches done in this field have been noted to produce a mixed bag of results all over the world (Herath, 2010). In other words, there is however not yet conclusive evidence about the economic impact of trade liberalization on economic growth of countries in sub-Saharan Africa. This is because results vary from one macroeconomic indicator to the other.

The acquisition of concrete figures from data sources has been a limitation. Most of the data bases are not able to give complete and specific annual information about some countries in the region. This led to some gaps left in the data set used to run the model using Stata software.

Consequently, conclusions drawn from this paper depend solely on the quality of model used in the estimation. Having said this, the modeling process however produces some useful insights.

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