Overview

The Africa Competitiveness Report 2015 comes out at a promising time for the continent: for 15 years growth rates have averaged over 5 percent,[1] and rapid population growth holds the promise of a large emerging consumer market as well as an unprecedented labor force that—if leveraged—can provide significant growth opportunities.[2] Moreover, the expansion of innovative business models, such as mobile technology services, is indicative of the continent's growth potential. However, Africa continues to be largely agrarian, with an economy that is underpinned by resource-driven growth and a large and expanding informal sector.[3] Indeed, more than a decade of consistently high growth rates have not yet trickled down to significant parts of the population: nearly one out of two Africans continue to live in extreme poverty,[4] and income inequality in the region remains among the highest in the world. What is more, across sectors—from agriculture to manufacturing and services—productivity levels remain low. It will be necessary to raise productivity across all sectors of the economy to achieve higher growth and create quality employment, and turn this progress into sustainable and inclusive growth.

The optimal path of development, however, remains uncertain. For decades, the typical path out of poverty was increased agricultural productivity followed by growth in manufacturing. Yet data explored in Chapter 1.1, Assessing Africa's Competitiveness, suggest that Africa's *structural transformation*—defined as the reallocation of economic activity away from the least-productive sectors of the economy to more-productive ones—is proceeding along a very different trajectory. Across the region, agriculture's share of GDP is declining and manufacturing is stagnating, while the service sector, in contrast, is increasing as a share of total employment and GDP, providing critical inputs to boost other economic activities. To inform this debate, this year's *Report* looks at structural transformation in Africa and the region's challenges and opportunities for unlocking new and more-productive activities.

This evolution in Africa's economic structure is happening in parallel with Africa's unique and evolving demographic dynamics: 450 million workers are projected to join the workforce between 2010 and 2035.[5] This presents an unprecedented opportunity in terms of a "demographic dividend," but at the same time it presents challenges because successfully meeting the imperative of job creation becomes even more crucial. Africa's transformation therefore entails the double challenge of productivity growth and massive job creation. What is more, demographic developments will require important and urgent public investments in economic centers and secondary cities: despite the continent's high population growth and rapid urbanization, Africans living in the countryside will remain the majority until the 2030s, and their number will continue to grow well after 2050.[6] This development, which is somewhat unusual compared with other regions, will also require policies that bridge the urban-rural divide while managing Africa's transformation.

Earlier editions of this biennial *Africa Competitiveness Report* have addressed distinct but related themes in considering the most effective ways to boost the continent's competitiveness. The 2011 *Report* examined Africa's human resources and services industries and looked at the efforts required to improve higher education, strengthen women's entrepreneurship, and capitalize on the emerging Travel & Tourism industry. The 2013 *Report* focused on the potential of regional integration as a stepping stone for building economies of scale, increasing competition, and fostering economic diversification. It also discussed constraints and the policy environment required to develop the necessary infrastructure for connecting Africa's markets in a sustainable way. This year's *Report* leverages the expertise and research that has been carried out by its partner organizations—the African Development Bank, the Organisation for Economic Co-operation and Development, the World Bank, and the World Economic Forum—to explore how best to transform Africa's economies. It is based on the assumption that increased competitiveness—by definition—is a critical driver for structural transformation and broad-based growth. By *competitiveness* we mean all of the factors, institutions, and policies that determine a country's level of productivity. Productivity, in turn, sets the sustainable level and path of prosperity that a country can achieve.

Against this backdrop, the *Report* begins with an overview of the region's current economic structure and moves on to outline the competitiveness challenges it now faces.

ASSESSING THE COMPETITIVENESS OF AFRICAN COUNTRIES

Chapter 1.1 of the *Report* analyzes competitiveness across the continent and looks at a broad range of factors that affect productivity in African countries. The Global Competitiveness Index (GCI) identifies the majority of African countries as being among the least competitive in the world and indicates that, despite 15 years of strong growth, Africa's overall competitiveness has remained stagnant.

In many respects, Africa's competitiveness challenges are the same ones that this *Report* has been highlighting since it was first published in 1998: these are weak institutions, a persistent infrastructure deficit (as explored in detail in the 2013 *Report*), and low levels of health and education that risk leaving the continent's vast human potential untapped. This sense of déjà vu is of concern because the majority of African economies find themselves in a development stage where these basic requirements will be necessary to establish a solid basis for higher-value-added sources of growth. And despite Africa's mobile revolution, the region as a whole is not keeping up with the rapid pace of technological advancements elsewhere. Only one-fifth of the region's population is using the Internet, compared with 30 percent in Southeast Asia, 40 percent in Latin America and the Caribbean, and 80 percent in Organisation for Economic Co-operation and Development (OECD) economies. Even in instances where the Internet is being used, its potential is not being fully harnessed. At the same time, however, much progress has been made and the region is showing a more solid record of macroeconomic performance than it did a decade ago. Despite prevailing governance challenges, it is more stable and better governed now than it has been at any other time since independence, and it classifies as the world's most rapidly reforming region when it comes to its business environment.[7] In spite of these positive trends, Chapter 1.1 shows wide regional disparities in competitiveness across the continent, as captured in findings such as the placement of Mauritius at 39th while Guinea, at 144th, is the lowest-ranked country out of all assessed. The regional divergence is particularly pronounced in the areas of infrastructure and health and primary education as well as financial and macroeconomic performance.

Recognizing the continent's heterogeneity, the chapter explores in greater detail the main competitiveness challenges by classifying Africa's economies into oil and gas exporters, middle-income economies, non-fragile low-income economies, and fragile economies. The data show that oil- and gas-exporting economies perform as poorly as fragile economies in 8 out of the 12 competitiveness pillars, calling into question whether these countries' high economic growth rates are sustainable. The chapter further observes that non-fragile low-income economies do particularly well in the areas of financial, goods, and labor market efficiency. Middle-income economies, while generally faring better, face many of the same competitiveness challenges as their peers, such as an infrastructure deficit and low levels of education. The chapter also looks at "Africa Then and Now." In the last decade, middle-income economies and oil-exporting economies overall register a mixed picture when it comes to improvements in competitiveness, while the majority of fragile and low-income economies register slight improvements. Among all economies, Mauritius has made the biggest strides, superseding South Africa for the first time in 2013.

TRANSFORMING AFRICA'S ECONOMIES

Although past experiences in other regions have emphasized industrialization as the driving force of economic development—as seen, for example, in East and Southeast Asia since the 1960s—data for Africa tell us a different story: agriculture continues to employ over half of the continent's population, but its share of value-added has been falling over the past four decades, dropping from 34 percent in 1965 to just over 20 percent in 2010. Rather than being replaced by an expanding manufacturing sector, as the experiences in other regions would predict, this decline has largely been offset by an expanding service sector, accounting for over 50 percent of GDP—a figure that is close to the share seen in the Association of Southeast Asian Nations. This shift took place largely in the market service sector—most notably in retail, distribution, and other trade services—employing 25 percent of the working-age population.[8] However, labor productivity in both the agriculture sector and the trade service sector—where most agriculture employment has shifted—remains low and should be enhanced. Greater productivity in agriculture and trade services would not only boost economic growth but also support structural transformation by allowing factors of production to move away from the agricultural to the service sector.

The dichotomy of a largely agrarian society underperforming in the basic drivers of competitiveness on one hand, alongside the rapidly growing role of the service sector coupled with a rapidly reforming business environment on the other, raises a question about the sustainability of Africa's path of development, particularly whether development toward a rising service sector that bypasses manufacturing is viable. A fast-growing but generally low-productivity service sector does not offer strong prospects for increased competitiveness.

INCREASING AGRICULTURAL COMPETITIVENESS

Chapter 2.1, Transforming Africa's Agriculture to Improve Competitiveness, begins the discussion of Africa's transformation by looking at the agriculture sector. In spite of its vast expanse of arable land, Africa has the highest incidence of undernourishment of its population worldwide, and the continent imports a large quantity of food staples. The agriculture sector's low productivity, largely characterized by small-scale subsistence production, has not benefited from the green revolution that aided much of the rest of the developing world.[9] The poor performance of the agriculture sector poses a major impediment to Africa's economic development and structural transformation by preventing labor from moving out of that sector into manufacturing and services. Chapter 2.1, therefore, looks at possible ways to unlock the sector's enormous potential and make it more competitive to support the continent's structural transformation process as well as to decrease food insecurity and meaningfully contribute to poverty reduction. The chapter argues that—on a higher level—urgent attention should be given to the development of agricultural value chains integration in order to boost African farmers' benefits and create an agribusiness industry. Value chains would support the recent growth in large commercial agribusinesses (see also Box 1; see Chapter 2.3 for a discussion of global value chains, or GVCs). At the same time, to ensure inclusiveness of the sector, links to small-scale farmers—including through outgrower schemes where smallholder farmers supply products for a larger firm under pre-agreed conditions—should be encouraged. Small-scale farmers, linked to large-scale agribusinesses or organized in groups, would diversify their production into higher-value crops, adopt better production processes, and earn higher output prices. In this way regional value chains can be used as a stepping stone for African farmers to improve their production, enhance marketing processes, and ultimately meet the quality standards of world markets. In addition, a sound regulatory and institutional system, financial instruments suited to the agricultural production cycle, and increased spending in research are vital to encouraging the development and adoption of high-yield crops, including genetically modified ones. All these elements are particularly vital at the national level, as much more effort is needed to meet the 10 percent of national spending on agriculture that was agreed under the terms of the Comprehensive Africa Agriculture Development Programme established by the New Partnership for Africa's Development. Furthermore, land reform will be particularly crucial for increasing access to land, including by women, which is necessary to decrease inequality in the distribution of land and to ensure security of tenure.

Box 1: Global value chains: A definition and method of measurement

Global value chains (GVCs) are the interconnected production process that goods and services undergo from conception and design through production, marketing, and distribution.[1] The primary measures of a country's participation in GVC trade are *backward integration,* which occurs when a country sources foreign inputs for its export production; and *forward integration,* which occurs when a country provides inputs for a foreign country's export production. Combining backward and forward integration gives a measure of a country's total GVC participation.

Note

1 Gereffi and Fernandez-Stark 2011.

THE ROLE OF SERVICES

The increasingly important role of services in economies across Africa is challenging the conventional understanding of the path of structural transformation. Chapter 2.2, Valuing Trade in Services in Africa, looks at new trade statistics for countries in Africa that take into account value-added data and show that service exports are much more significant for Africa than previously thought. Services contribute to exports through two channels: as direct service exports and as inputs into exports from other sectors. By disaggregating value-added data, the importance of services as inputs into other export activities becomes much more evident, especially their contribution as inputs into exports of primary goods and manufacturing. Services, for example, account for 83 percent of the final price of Ethiopian roses in the Netherlands. Distribution and trade services (including hotels and restaurants) and other business services (including ICT and professional services), in particular, tend to have stronger links to other export sectors when measured in value-added. Typically viewed as an area of comparative advantage for more-advanced economies, these trends give the service sector a more prominent role in the development agenda of Africa. A growing service sector can also help improve gender equity in Africa, because the barriers to female employment are lower for services than for manufacturing. Yet service exports from Africa remain a small portion of overall exports and numerous impediments to trade in services exist. To maximize potential gains, countries in Africa need to reduce direct barriers to trade in services as well as indirect ones that result from poor regulation. As countries continue to seize opportunities in the sector, policymakers and economists need to question old assumptions and consider new implications. The role of services in structural transformation must be reexamined, and the link between a growing service sector and poverty reduction in Africa—and whether this a viable export sector for Africa—must be determined.

TAPPING THE POTENTIAL OF GLOBAL VALUE CHAINS (GVCS)

Although not new, cross-border value chains have gained a global dimension through their expansion toward emerging and developing countries (see Box 1). Firms increasingly operate in a context of internationally fragmented production chains. Through GVCs, trade is facilitated by flows of goods, services, investment, and knowledge necessary to produce products in multiple locations—giving rise to what has been called the *trade-investment-service-intellectual property (IP) nexus.*[10] The importance of this nexus for international trade and development has motivated new research efforts that, notably, assess its influence on the links between trade, competitiveness, and development. Recent data suggest that participation in GVCs is associated with economic benefits particularly for developing economies, where value-added trade contributes 28 percent to countries' GDP on average—considerably higher than the contribution of 18 percent in developed economies. Moreover, economies with the fastest-growing GVC participation have GDP per capita growth rates some 2 percent above the average.[11] For Africa, GVCs offer the opportunity to link into a specific part of the production chain based on a country's or sector's comparative advantage rather than providing the fully fledged production chain itself.

In view of the economic opportunities associated with GVCs, Chapter 2.3, Tapping the Potential of Global Value Chains for Africa, explores ways Africa could tap the potential of GVCs in the form of gains associated with enhanced productivity, skills development, and export diversification. As discussed in the 2013 *Africa Competitiveness Report,* Africa's share of global trade remains very small, at around 2 percent of world trade, and exports overall remain highly focused on commodities.[12] This important exposure to commodities renders the region vulnerable to fluctuations in commodity prices, as evidenced by their current fall, possibly also jeopardizing governments' fiscal stability. Export diversification—both in goods and services and also across geographies—therefore remains essential to raising Africa's resilience to external shocks and moving up the value chain. The region's participation in GVCs remains a small (albeit growing) share at 2.2 percent of total GVC trade, of which two-thirds is determined by forward integration related to the continent's rich endowments in natural resources and low levels of industrialization. Further development of GVCs, in particular backward linkages, will depend on the implementation of a broad set of policies with a particular focus on trade facilitation, investment policy, and improved transport infrastructure and access to finance. These policies will have most impact on African small- and medium-sized enterprises, which face the greatest hurdles to GVC integration and whose participation is especially hindered by limited access to finance. Moreover, the chapter argues that accelerating the harmonization and implementation of regional trade agreements should help African firms, in particular small- and medium-sized enterprises, develop a greater capacity to compete on a global scale. The chapter warns, however, that gains from GVC participation will vary with economic sector and structural factors such as the country's level of development and market size. Furthermore, additional data and empirical studies will be needed to fully assess the extent of GVC integration in Africa and its links to development outcomes such as employment.

As the number of consumers in Africa grows, nontraditional crops—such as fruits, vegetables, and fish—that are buyer-driven value chains and where upgrading can occur as retailers seek "ready-to-sell" products that are already packaged for the final market are a particularly promising GVC for Africa.[13] Regional value chains can also provide an important step and learning experience for integrating into global agricultural GVCs, so smallholder farmers especially can learn to meet the high-quality standards for the world market, as noted above.

COMPREHENSIVE POLICY MIX NEEDED

As each of the chapters explores ways, opportunities, and barriers to transforming Africa's economies, it has become clear that the policy space to unleash the continent's tremendous potential is often overlapping. On a higher level, these are efforts to close the infrastructure deficit and leverage the region's human resource potential. At the same time, identifying and implementing a strong regulatory framework within and across sectors as well as reducing barriers to trade will be important. Jointly, the following levers will be the most critical to address many of the challenges explored in the *Report:*

- **Developing transport and ICT infrastructure:** Chapter 2.1 lists inadequate infrastructure—including unreliable energy, an ineffective urban-rural road network, and inefficient ports—as main impediments to better performance of the agriculture sector. Increased spending on rural infrastructure (irrigation, roads, and energy) will help reduce the continent's dependence on rain-fed agriculture by supporting intensified irrigation, increasing resilience to climate change, and improving access to markets for intermediate inputs and agricultural produce. The availability and quality of infrastructure is also an important determinant to unlock (intra-) African trade in general and participation in regional and GVCs specifically (Chapter 2.3). Likewise, developing ICT infrastructure cuts across all sectors: ICTs can streamline production knowledge and market information flows between stakeholders in the agriculture sector by, for example, (1) facilitating the process of land registration and access to credit; (2) ensuring more efficient land use and water management; (3) obtaining weather, crop, and market information;[14] and (4) allowing food and animals to be traced. ICTs are also critical to facilitate the provision of services within countries and across national borders (Chapter 2.2).

- **Increasing the quality of education:** Most importantly, increasing levels and quality of education will be essential to raising productivity across all sectors. Chapter 1.1 shows that, although the continent has made considerable progress in improving access to primary education, enrollment rates in higher education—especially in tertiary institutions—remain disappointingly low. Increasing levels and quality of education, including enhancing skills in biotechnology as a way to increase agricultural productivity, will be important to raising productivity in the agriculture sector (Chapter 2.1). Empirical evidence shows that tertiary education enrollment is an important determinant of services in developing countries, primarily via skills and entrepreneurial activity (Chapter 2.2). Indeed, a highly educated workforce is needed to develop high-value-added service exports such as finance, communication, and business services. With regard to GVCs, improving the quality of education will help increase the attractiveness of African producers and ensure technology and knowledge transfers and spillovers in order for the continent to upgrade along GVCs.

- **Reducing barriers to trade:** The reduction of barriers remains a critical component for increasing Africa's competitiveness. Beyond the poor quality of physical infrastructure and high tariffs, estimates shows that 60 to 90 percent of trade costs relate to non-tariff measures (Chapter 2.3). In addition, delays and unpredictability are often a strong impediment to the region's participation in GVCs because many industries rely on just-in-time production and depend on the reliability of the supply of intermediate inputs. Chapter 2.1 provides an example, based on agriculture value chains, where reducing shipping time and costs would significantly reduce losses in perishable food shipping. Key recommendations noted in the last edition of the *Africa Competitiveness Report,* therefore, remain critical for Africa's participation in GVCs. Essential among these are simplifying import-export procedures—including streamlining border administration to reduce the cost of procedures and delays during clearance, and improving the coordination of the clearance process.

- **Strengthening the regulatory framework:** Chapter 2.1 discusses land access based on customary rights that disadvantage women, unequal distribution, and the absence of land markets that are preventing the most efficient farmers from the opportunity to scale up their production. Insecure land tenure also limits farmers' ability to use their land as collateral and thus to access credit markets. In the service sector, key components—such as telecommunications, professional services, and transport services—are relatively restricted in many countries. For example, restrictive policies and disjointed regional regulations have caused a fragmented market in the professional services industry in East Africa, which is further aggravated by strict immigration policies in some countries in the region. Yet lifting restrictiveness alone is not enough without complementary regulatory reform (Chapter 2.2). Similarly, the absence of competition and inefficient regulation in the freight logistics sector add to high transportation costs that pose an important barrier to increased trade and GVC participation, as explored in Chapter 2.3.

Efforts to address all these challenges are underway in some parts of the continent, but in order to truly transform Africa's economies, these efforts must be scaled up and accelerated.

Following the discussions above, the final section of the *Report* provides detailed competitiveness profiles for the 40 African countries included in the World Economic Forum's Global Competitiveness Index that allow for a detailed assessment country-specific context and unique challenges. These profiles present the detailed rankings that underlie the broader global competitiveness rankings.

NOTES

1 Authors' calculation, based on the International Monetary Fund's *World Economic Outlook* (IMF 2015).

2 Growth opportunities are contingent on several factors, such as the critically important issue of the employment of the expanding workforce. Successfully extended employment opportunities would lead to greater economic output and labor income per household, and among other aspects, would increase per capita investments in health, education, and infrastructure, and a move away from the informal to the formal sector. For a complete discussion, see also IMF 2015, Chapter 2.

3 Only one in two young Africans participates in wage-earning jobs; see World Bank 2014a.

4 This figure is 46.8 percent of the population measured against a threshold of US$1.25 dollar a day. See http://povertydata.worldbank.org/poverty/region/SSA for details.

5 IMF 2015.

6 UNESA 2015.

7 World Bank 2014b.

8 These numbers refer to 2010 and cover 11 sub-Saharan and 2 North African economies for which data are available in the GGDC Africa Sector Database (Timmer et al. 2014). The sub-Saharan Africa sample includes Botswana, Ethiopia, Ghana, Kenya, Malawi (1966 data have been used for 1965), Mauritius (1970 for 1965), Nigeria, Senegal (1970 for 1965), South Africa, Tanzania, and Zambia. The North Africa sample includes Egypt and Morocco.

9 The *green revolution* refers to the dramatic rise in the productivity of global agriculture in other parts of the world as a result of chemical advances and the development of high-yield crops, which made possible the production of much larger quantities of food and feed the growing population.

10 Baldwin 2011, 2012. See also Feenstra 2010; Grossman and Rossi-Hansberg 2008; Helpman 2011; and Jones 2000 for an analysis of defragmentation, trade in tasks, and offshoring.

11 UNCTAD 2013.

12 Fuels and mining products account for over half of sub-Saharan exports, compared with only about 10 percent for developing Asia and advanced economies.

13 Traditional cash-crops (such as coffee, cotton, cocoa, sugar, tea, and tobacco) tend to be producer-driven chains with limited scope for functional upgrading, given the tight control by lead producers with higher-value activities—such as processing and manufacturing—that are carried out outside Africa.

14 The Esoko Ghana commodity exchange publishes a weekly cash price index of commodities. Esoko has expanded in a dozen countries and provides price and knowledge data to farmers via mobile text messages.

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