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THE EFFECT OF THE TRADE LIBERALIZATION PROGRAM ON GOVERNMENT BUDGET IN AFRICA

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1. Introduction

Trade liberalization is not a precise concept. It implies the application of different trade policies. The elements of trade liberalization (or trade policy reform) include, *inter alia*, removing non-tariff barriers to trade, reforming exchange rate regimes, liberalizing export policies, and harmonizing and reducing import tariffs. The focus in this paper is on the tax revenue impact of the last policy, i.e. the impact of import tariff harmonization and reduction. It is also to be noted that African countries pursue concurrently not one but a multiplicity of trade liberalization programs, the customs revenue implications of which vary. It is, therefore, necessary to define which trade liberalization one is talking about in order to measure its tax revenue implications.

In an earlier study[1] on the above topic, it was argued that the estimated tax revenue losses from the foreign trade liberalization component of the structural adjustment program (SAPs) are indeterminate; that the tax revenue loss from the *full liberalization* of intra-Regional Economic Community (REC) trade is too small or insignificant; and that the tax revenue loss from the *full liberalization* of intra-African and global (or total foreign) trade are relatively larger and difficult to compensate for in the short run. It was further suggested that most of the expected tax revenue losses from the trade liberalization programs can be mitigated by the application of diverse countervailing measures.

2. The pursuit of Diverse Trade Liberalization Programs and Tax Revenue Implications

One of the most important multilateral trading systems in which most African countries are active members is the World Trade Organization (WTO). The WTO[2] has a total membership of 146 countries and an additional 30 observers. African members and observers are respectively 41 and 7. The WTO Agreements cover both benefits and obligations or commitments. These commitments basically refer to the implementation of decisions in regard to trade in goods, services, intellectual properties, investment, competition, standardization and certification, trade and labor standards, trade and environment, food security, public procurement, etc. and other ground-rules of international commerce aimed at enhancing the growth of global trade and economy through equitable sharing of the benefits of free trade.

It is important to note that for African countries, which are members of the Regional Economic Communities (RECs), Article XXIV together with Article V of GATS in the WTO Agreements, require these regions or RECs to include all sectors of goods and substantially all trade in their negotiations and prohibit raising of their trade barriers (both tariff and non-tariff) to members of the WTO who are not members of their respective RECs. The main problem for African countries is not that they are losing tax revenues through their implementation of the WTO negotiated tariff reduction schedules, or

[1] Teshome Mulat, "Trade Liberalization and Government Tax Revenue Loss in Africa", *Journal of World Trade*, Vol. 31, No. 1, February 1997. pp. 161-174.

[2] See the WTO Website (wto.org). The statistics given is as of 4 April 2003.

because they are denied, by these agreements, the opportunity to erect high tariff walls around their RECs (or their respective domestic economies). Notwithstanding supporting provisions or forestalling mechanisms in the WTO Agreements (or the Uruguay Round (UR), as it is called), including waivers, exemptions, assistance to developing and least developed countries, etc, the main problems facing African countries in the WTO negotiations include, *inter alia*, lack of negotiating capacity, inability to implement decisions, supply constraints, and generally failure to participate effectively and reap sustainable benefits from the multilateral trade processes.

The other multilateral trading system to which most sub-Saharan African countries belong is the ACP-EU Partnership Agreement, which is a trade and economic cooperation agreement between African, Caribbean and Pacific (ACP) countries and the members of the European Union (EU). Although the African group of countries in the ACP have indicated recently[3] their needs for compensatory financing from the EU to cover expected tax revenue losses resulting from their obligations to offer most favored nations preferences to EU countries under the WTO rules; tax revenue losses from the ACP-EU trade liberalization program are not the key issues in this arena of multilateral trade negotiations. The main problem is that African countries, which failed to take full advantage of the unreciprocated preferences and trade and development support from the European members under the Lomé Convention (1975-2000) are negotiating to do better under the successor ACP-EU (or Cotonou) Partnership Agreement, which became effective in 2000 and which is expected to be compatible with the WTO rules. African countries as well as other members of the ACP group have concerns and interests (i.e. other than compensation for tax revenue loss arising from their trade liberalization programs), which they would like to be addressed by the partnership agreement. Among these are sensitivity to their developmental needs, elimination of export subsidies and significant reduction of domestic support by EU members for products of interest to ACP countries, revision of Article XXIV on regional trade agreements (RTAs) to include special and differential treatment and take into account different levels of development in applying the principles of transitional time frames, reciprocity, etc.

African countries also maintain bilateral trade and cooperation agreements with other African and non-African countries. There is very little known about such agreements between African countries, still less about their implementation and the effects thereof on government budget. By far the most important of the bilateral agreements is perhaps the US's African Growth and Opportunity Act (AGOA). The US has gone beyond offering a temporary and non-reciprocal grant of preferences (i.e. a GSP) for African countries with this Act. In addition to providing African economies market access through this GSP Program, the US provides security to investment and technical and economic assistance for development. Since African countries are offered unreciprocated preferences, which permit their exports to enter the US market untaxed (and this covers virtually all merchandize), no revenue loss is expected from the transaction. However, AGOA's stringent conditionalities and production/supply constraints in African economies have prevented many African countries from effectively participating in the program.

[3] *Trade Negotiations Insights*, Vol. 2, No. 4, August 2003.

Thus regarding the multilateral and bilateral trade agreements, the main problem is with the implementation of those agreements. In theory, the associated trade liberalization programs could entail some customs revenue loss, but in practice the overall net effect on budgetary revenue is expected to be positive. In the long-term trade liberalization causes economic growth, which, in turn, expands the tax-base and hence results in an increase of tax revenues (including customs revenues). In the short-term there are various factors at work, which tend to increase revenues from the taxation of foreign trade (see next section).

There is also the unilateral or domestic trade liberalization program to consider. Most African governments have been pursuing *structural adjustment programs (SAPs)*, which are supported by the World Bank and the International Monetary Fund, for a decade or so, and the foreign trade liberalization component of these SAPs as well as their customs revenue effects have been discussed in the article cited in the introduction of this paper. Briefly,

> There are mixed results from the application of heavier duties on imported finished products, the widening of the gaps between tariffs applied on the imports of raw materials and finished products, and increasing the level of government subsidy as measures to increase domestic production/supply and export growth under SAPs. Government Subsidy is the equivalent of a negative tax revenue collection, while heavier taxation on the import of finished products yields more tax revenue unless there is a compensating drop in the demand for those products. Export tax exemptions result in net loss of tax revenue from exports and some countries are known to have applied such exemptions on selected exports and some others on exports generally. In many reforming African countries, in addition to tax rebates, which are provided in specific acts and investment decrees, duty drawbacks (a reclaim of duties paid on imports used in the production of exported goods) have also been applied to encourage the export of manufactured products. These are expected to result in tax revenue loss in the short run, unless high capacity utilization rates and instantaneous growth of supply or export permitted compensatory growth of government tax revenue collection. The combined tax revenue effect of these fiscal processes cannot be determined *a priori*[4].

Finally, African countries are actively engaged in intra-regional trade. Part of the difficulties in estimating the tax revenue losses from the *liberalization of intra-REC trade* stem from the great diversities of these trading systems and the failure to implement the respective protocols. The most important intra-REC trading system is elaborated in the *African Economic Community (AEC) Treaty*, which was adopted by the Assembly of African Heads of State and government in 1994[5]. According to this blueprint, each

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[4] Teshome Mulat, *Op.cit.*, pp164-165

[5] There are many other sub-regional and other groupings to which varying number of African states belong. Among these are the Union Monetaire ... (UEMOA), which is an association of the French Speaking members of ECOWAS and which has reached the stage of a customs and monetary union; CEMAC aims at achieving the goals of UEMOA in the ECCAS Region by adopting a faster rate of dismantling tariff and non-tariff trade barriers among its members. The East African Community (EAC) is an association of three states, namely, Kenya, Tanzania and Uganda, which have adopted a faster pace of trade liberalization and integration than COMESA. There is also the *Cross Border Initiative* which brings together a group of COMESA, SADC and Indian Ocean island states in implementing a program of liberalization of trade in

member of the African Union [then called the Organization of African Unity (OAU)] belongs to at least a *Regional Economic Community (REC)* and each REC, in turn, is expected to evolve (within a period of 34 years) into a preferential trade area, a free trade association, a customs union, and emerge eventually, through horizontal harmonization of fiscal and monetary policies as well as the development of common institutions, into the African Economic Community. Presently there are seven RECs, which are approved by the policy organs of the African Union: Arab Maghreb Union (AMU), CEN-SAD, Common Market for Eastern and Southern Africa (COMESA), Economic Community of Central African States (ECCAS), Economic Community of West African States (ECOWAS), Intergovernmental Authority on Development (IGAD), and Southern African Development Community (SADC) (see Table 1).

Theoretically, a complete liberalization of intra-REC trade (i.e. adoption of free trade area association status) would result in customs revenue loss of less than one-tenth of 1 percent of GDP in many cases (see Table 1). In practice, however, the intra-REC trade liberalization program is poorly implemented in all the RECs; although the RECs vary in the degree of their respective implementation of the program. Many countries have membership to more than one Regional Economic Community, which reflects their free-riding behavior. Lack of harmonization of the diverse tariff reduction programs and tedious procedures in processing intra-REC trade flows (including non-tariff barriers and difficulties in making a timely verification of the conditionality of the rules of origin) etc. account for the lack or poor implementation of the trade liberalization programs of the RECs.

However, the argument that a customs revenue loss would occur if members implemented the intra-REC trade liberalization program is not justified. As shown in Table 1, the revenue loss implied by the full liberalization of intra-REC trade is small, and as will be explained later, there are ways to circumvent such losses. What is important to consider is not so much the customs revenue but rather the total budgetary revenues of government. In this regard, there is no indication that the government budgetary revenues or even the revenues from foreign trade taxation have been declining as a result of intra-REC trade liberalization. That is why it becomes difficult to justify the reneging of African governments in implementing the trade liberalization programs in general and the intra-REC trade liberalization program in particular.

The other justification for the taxation of foreign trade (including intra-REC trade) has been the so-called "infant industry argument". Some African governments have argued that they need to tax imports, including imports from their respective REC-membership, in order to provide protection to their domestic industry. This explanation for reneging to implement the REC-trade liberalization program does not also hold water. To begin with most of these members of the RECs have been scaling down their tariff barriers on the basis of WTO agreement, the respective REC trade protocols, SAP, or some other trade

goods and services including immediate abolition of non-tariff trade barriers and rapid reduction of tariffs among reciprocating members. See, *Cross Border Initiative: Eastern and Southern Africa and Indian Ocean*. Volume 3. Co-sponsored by the African Development Bank, European Commission, International Monetary Fund and the World Bank. 1998.

liberalization program (such as the ACP-EU, AGOA, CBI, UEMOA, etc). The effective rate of protection needed to provide adequate protection to their domestic industry is already passed, once they accepted to lower their tariff levels on the basis of one trade and cooperation agreement or another. In other words, the effective rate of protection that would be required to provide adequate cover for domestic industries is too high, if it is to be have had, and current tariff levels are inadequate to provide such protection. Secondly, the lack of industrial growth in most of African countries is caused more by such factors as lack of investment, bad public policy, inadequate supply of skills, poor infrastructural and institutional development in African countries, etc. than by the scalability of the tariff walls.

Indeed, much of the available evidence points not to the resultant tax revenue gains or losses from trade liberalization programs, but rather to the failure to implement such programs or trade policies generally. Some proponents of this view maintain that the trade environment in much of Africa remains constrained[6], and, on the basis of impact assessment of trade policies, they argue that in many African countries nominal protection remains high, many currencies are overvalued, and the procedures and regulations surrounding trade remain slow, burdensome and restrictive. Others[7] concluded that such trading arrangements (as the RECs), in and of themselves, are unlikely to yield appreciable benefits and that they could be detrimental to the members (economies) involved, either because they might encourage import substitution, result in trade diversion, or simply because they absorb scarce administrative and financial resources.

The failure of trade reform in Africa is also seen by some as resulting from inequity and lack of transparency in the statist approach to tax administration pursued by exclusive and undemocratic governments in partially monetized economies[8]. These are shortcomings of government failure; and as Goldsmith[9] concluded, "It is a daunting task to break the mold of public institutions that have hardened around personalized power,

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[6] See, for example, Metzel, J., and L.C. Phillips (July 1998), "Bringing Down Barriers to Trade: The Experience of Trade Policy Reform". (Equity and Growth through Economic Research (EGERD) Discussion Papers Page: http://www.eagerproject.com/dabstracts.html).

[7] Radlet, Steven (July 1999), "Regional Integration and Cooperation in Sub-Saharan Africa: Are Formal Trade Agreements the Right Strategy?" (EGERD Discussion Papers Page).

[8] Wadhawan, S.C., and C. Gray (July 1998). "Enhancing Transparency in Tax Administration: A Survey". (EGERD Discussion Papers Page, *op. cit.*).

[9] Goldsmith, Arthur (July 1998), "Institutions and Economic Growth in Africa". (EGERD Discussion Papers Page, *op. cit.*).

Table 1: Estimate of Tax Revenue Loss From the Liberalization of Intra-REC Trade (% of GDP)

	UMA	CENSAD	COMESA	ECCAS	ECOWAS	IGAD	SADC
Algeria	0.0192						
Angola			0.0025	....			0.0469
Bennin		....			0.3362		
Botswana							....
Burkina Faso		0.0592			0.3180		
Burundi			0.1235	0.0221			
Cameroon				0.0332			
Cape Verde					0.1559		
CAR		0.0158		0.0985			
Chad		0.0298		0.0278			
Comoros			0.2125				
Congo				0.0373			
CDR			....	....			....
Cote d'Ivoire					0.7550		
Djibouti		....	....			....	
Egypt		0.0090	0.0060				
Eq. Guinea				0.2708			
Eritrea		....	0			0	
Ethiopia			0.0807			0.0712	
Gabon				0.0373			
Gambia		....			0.6459		
Ghana					0.6250		
Guinea					0.0464		
Guinea Bissau					0.2164		
Kenya			0.1563			0.1086	
Lesotho							....
Liberia					....		
Libya	....	....					
Madagascar			0.0316				
Malawi			0.2891				0.9637
Mali		0.1887			0.7414		
Mauritania	0.2148						
Mauritius			0.1881				0.7224
Morocco	0.0432	0.0471					
Mozambique							0.3472
Namibia			0				....
Niger		0.1516			0.2827		
Nigeria		0.0155			0.0586		
Rwanda			0.0866				
Sao Tome&Princ.				0.0993			
Senegal		0.1109			0.1650		
Seychelles			0.3055				1.2804
Sierra Leone					0.1897		
Somalia		....				....	
Sudan		....	....			....	
Swaziland			0				....
Tanzania							0.0963
Togo		....			1.9094		
Tunisia	0.1276	0.1135					
Uganda			0.2464			0.2376	
Zambia			0.3503				1.0571
Zimbabwe			0.0545				0.3268
S. Africa							0.0218

Source: Calculations based on UNECA Database

arbitrary and unaccountable decision-making, widespread dishonesty, and repression of dissent"

Some others have identified de-linking of strategic considerations in infrastructure as the source of trade policy failure in Africa[10], while others focused on the problems of foreign direct investment flows (FDIs), (which determine directly the success or failure trade policy reform and) which, in turn, are believed to have been the results of government failure in Africa. These failures are reflected in the lack of economic openness, (i.e. minimizing trade and exchange rate controls), administrative inequity, lack or underdevelopment of the rule of law, non-transparency of government operations and high rates of corruption of officials[11].

There is a lot of skepticism regarding the ability of sub-Saharan African countries to turn around recent negative economic trends through the adoption of more outward-oriented policies, faster financial development, and more democratic environments in the short-run[12]. Similar pessimism is expressed on the ability of many African countries to respond in a significant manner to the overtures of the WTO, EU and U.S.A. to support trade liberalization and development programs in Africa[13]. A recent survey of trade policies in Africa corroborated the popular view of "disintegration" and concluded that, "Africa, especially Francophone Africa, is currently under-exploiting its trading opportunities and has witnessed disintegration over time, *a trend that is most pronounced in its trade with the technologically advanced countries*."[14] The viability of the Regional Economic Communities as "trade creating" and regional integration and development enhancing schemes is also doubted by skeptics[15].

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[10] McPherson, Malcolm F. (July 2000), "Strategic Issues in Infrastructure and Trade Policy". (African Economic Policy Discussion Paper Number 26, funded by USAID, Bureau for Africa Office of Sustainable Development, Washington, DC 20523-4600).

[11] Wilhelms, Saski K.S. (July 1998), "Foreign Direct Investment and Its Determinants in Emerging Economies". (EGER Discussion Papers Page, *op.cit.*). see also, Piagato, Maria, "Foreign Direct Investment in Africa: Old Tales and New Evidence". *World Bank Working Papers Series*, September 2001. Ms Pigato, while calling the customary proposition that FDI flows to Africa are too small as "old tales", and while acknowledging that sub-Saharan African countries are still failing to attract foreign investments into activities outside mining and oil, nonetheless, concluded that "reforming" African countries have the potentials to attract FDI, particularly through privatization.

[12] Tsangarides, Charalambos G. (November 2001), "Revisiting Growth and Convergence: is Africa Catching Up?" *World Bank Working Papers, No.10.*

[13] Plunkett, Daniel (September 1999), "Implications for Africa of Initiatives by the WTO, EU and U.S." (EGERD Discussion Papers Page, *op. cit.*). The author concludes that since African countries tend to be poorly equipped to participate in the related negotiations, there is a real danger that some African countries will end up worse off than before.

[14] Subramanian, Arvind and Natalia Tamirisa (March 2001, "Africa's Trade Revisited". *IMF Working Paper*, WP/01/33. This view is corroborated by Qing Wang (December 2001), "Import Reducing Effect of Trade Barriers: A cross-Country Investigation", (*IMF Working Paper* WP/01/216), who, using a large sample of cross-country data, found that both tariff and NTBs are quite significant in restricting imports.

[15] See, for example, Jeffrey D. Lewis, Jeffrey, D. Robinson, Sherman Thierfelder, (2002), *Free Trade Agreements and the SADC Economies* (World Bank Africa Region Working Paper Series, No. 27), who argued that South Africa is not a viable "growth pole" and that access to EU markets provides "substantially bigger gains for the other SADC countries, than access to the South African market".

3. The Budgetary Implications of Trade Liberalization Programs: The Evidence

Many African fiscal systems are heavily dependent on extra-budgetary finances, especially foreign grant and loans (see Table 2). These loans and grants account for the GDP growth and are financing public expenditures in these economies, thus making trade and foreign direct investment (FDI) flows less significant determinants. In other fast industrializing regions of the world, trade and investment (and not grants and aid) are most important determinants of economic growth. A recent IMF study argues that "growth (in Africa) has been hampered by economic distortions and institutional deficiencies that have increased the risk of investing in Africa, and lowered the rates of return on capital and labor as well as the growth of total productivity"[16].

In 1990 out of 49 countries (see Table 2), for which data on grants and external credits are reported, 37 countries (or 76 percent) had grant plus credits to GDP ratios of 50 percent or above, while those with ratios in excess of 100 percent of GDP numbered 17 (or 35 percent of the countries). By 2000, the number of countries with grant plus credits in excess of 50 percent of GDP and those in excess of 100 percent of GDP increased, respectively to 41 and 19 countries. Looking at the same trend differently, the mean grant plus credits to GDP ratio rose from 97 percent in 1990 to 108 percent in 2000, although there is high variability of this ratio between countries. The trend toward increased dependency on foreign financing of the African economy (and government expenditures) shows the venerability of African fiscal systems, and constraints in the use of foreign trade taxation as a mode of financing government budgetary expenditures.

The share of tax revenues in the GDP is growing (see Table 3), but by a very low growth rate (from 16 percent of GDP in 1990 to 17 percent of GDP in 2000). The share of tax revenue in the total government revenue (excluding all grants), however, remained a constant (at about 75 percent) over the decade. It is to be noted that unlike most developed economies, developing economies collect most of their tax revenues from indirect taxes, of which foreign trade taxation is a major component.

Foreign trade taxation, which averaged about 5.9 percent of GDP in 1990, increased to 6.4 percent of GDP in 1995 and increased further to 7 percent in 2000. However, the data for individual countries does not show a clear trend in customs revenue collections for most of them (see Table 4). The revenue from foreign trade taxation for 24 countries rises and falls during the decade (1990-2000) without a discernible trend, there is a distinct growth trend observed for 7 countries and a decline for another 12. Thus, whether the slow growth in the mean value of customs revenues resulted from a successful implementation of the customs laws (or the trade liberalization programs) or failure to do so is not evident from the available data. This uncertainty is the more evident when account is taken of the complexities arising from the engagement of African countries in too many and diverse trade liberalization programs and their failure to implement them.

[16] Ernesto Hernandz-Cata (May 2000), *Raising Growth and Investment in Sub-Saharan Africa: What Can be Done?* (IMF Policy Discussion Paper, PDP/00/4), "Abstract".

Table 2: All Grants Plus Total Debts (as percent of GDP)

	1990	1995	2000	2001
Algeria	45.4	79.1	47.4	40.2
Angola	83.8	228.2	107.4	108.9
Bennin	75.9	83.0	72.7	72.7
Botswana	15.7	15.3	8.2	7.2
Burkina Faso	32.9	65.3	69.0	68.0
Burundi	88.1	119.3	165.4	157.1
Cameroon	59.9	117.8	104.1	83.6
Cape Verde	47.3	52.5	64.2	61.9
CAR	51.1	90.6	97.3	92.8
Chad	38.1	70.1	84.7	74.3
Comoros	82.2	103.9	117.6	115.9
Congo	177.1	284.8	152.1	163.6
CDR	109.7	234.6	76.2	0.0
Cote d'Ivoire	159.8	189.8	115.6	112.1
Djibouti	58.2	58.6	56.0	8.7
Egypt	79.5	56.3	29.8	30.1
Equatorial Guinea	187.5	180.5	18.6	13.0
Eritrea		20.2	68.9	78.7
Ethiopia	128.3	181.7	89.4	96.3
Gabon	67.3	88.0	79.3	78.7
Gambia	122.4	114.0	116.8	122.9
Ghana	68.5	95.6	137.2	133.2
Guinea	91.6	91.8	113.0	111.7
Guinea Bissau	301.8	370.0	387.5	348.7
Kenya	84.8	84.0	63.7	55.1
Lesotho	74.8	78.1	76.8	76.9
Liberia				
Libya				
Madagascar	124.6	139.7	124.8	94.1
Malawi	85.5	165.0	168.4	154.6
Mali	107.9	127.4	135.2	130.4
Mauritania	208.2	221.9	259.3	214.8
Mauritius	41.6	46.4	39.0	38.5
Morocco	97.6	69.7	53.8	49.6
Mozambique	198.5	332.7	196.5	136.7
Namibia	3.2	2.2	0.0	0.0
Niger	75.1	89.1	95.8	84.2
Nigeria	117.4	121.3	76.3	75.5
Rwanda	32.2	90.8	79.2	83.8
Sao Tome & Principe	287.6	561.5	98.2	115.3
Senegal	66.8	89.1	679.9	666.7
Seychelles	46.2	31.8	78.0	76.5
Sierra Leone	184.2	134.3	43.1	44.0
Somalia				
Sudan	112.1	244.7	139.9	122.5
Swaziland	28.5	16.4	22.0	25.8
Tanzania	155.0	142.7	85.6	75.0
Togo	81.9	114.0	117.8	112.2
Tunisia	62.6	60.5	54.9	54.6
Uganda	62.1	66.5	65.1	73.4
Zambia	214.6	205.9	182.7	161.5
Zimbabwe	37.8	72.2	56.9	42.0
S. Africa	0.2	16.8	19.4	21.2
Average (Mean)	**97.21**	**126.30**	**107.81**	**99.30**
Standard Deviation	**67.06**	**102.26**	**105.53**	**101.61**

Source: UNECA

One of the likely outcomes of trade liberalization is that as the relative share of foreign trade taxation (in the total government revenue or total tax revenue) declines through continual scaling down of the tariff barriers to trade, governments tend to switch to heavier taxes on domestic goods and services, in order to maintain overall government revenue levels. But the data in Table 3 does not prove this proposition to be true, since both taxes on domestic goods and services and taxes on international trade have been growing, leaving their relative shares in total tax revenue unchanged throughout the period (1990-2000) of relatively active trade liberalization in Africa.

TABLE 3: THE RELATIVE GOVERNMENT REVENUE SHARE OF FOREIGN TRADE TAXATION*

	1990	1995	2000
Government Revenue Excluding All Grants (% of GDP)	20.05 (8.88)	20.39 (10.80)	21.68 (11.63)
Total Tax Revenue (as percent of GDP)	15.69 (7.81)	15.99 (8.41)	16.89 (9.16)
Taxes on Domestic Goods and Services (% of GDP)	4.10 (2.56)	4.61 (2.87)	5.03 (3.22)
Taxes on International Trade (% of GDP)**	5.88 (4.53)	6.44 (5.67)	7.02 (6.12)
Import Duties (% of GDP)	5.26 (4.52)	6.00 (5.77)	6.78 (6.17)
Export Duties (% of GDP)	0.62 (1.53)	0.44 (0.80)	0.24 (0.66)
All Grants plus Total External Debts (% of GDP)	97.20 (67.51)	126.30 (102.26)	110.00 (105.52)
All Grants (as percent of GDP)	4.10 (5.02)	3.90 (4.82)	4.20 (5.35)
Total External Debt (as percent of GDP)	93.20 (64.66)	122.40 (99.95)	105.80 (104.83)

*The figures in parentheses are standard deviations

**The mean and standard deviation are computed only for countries with (compatible) observations of both imports and exports. (This explains the differences between the results on "Taxes on international trade" as percent of GDP, which are reported in Tables 3 and Table 4).

Source: UNECA

Another expected outcome of the trade liberalization program is that revenues from *export taxation* will tend to decline during the early stages of the program. This is because during the early stages of trade reform, developing countries reduce and in some cases eliminate export taxes in order to encourage exports to their traditional markets. If these reductions and eliminations are generalized to all exportable, the export tax revenue loss could be relatively large or significant. It would also be difficult to make up for this revenue loss through a combination of *reduced* export tax rates (following trade liberalization) and increased exports in the short-run, because, in the short run, it will not be possible to diversify exports and increase the supply/production of exportable from developing African countries. The results in Table 3 are consistent with this hypothesis. Export duties, which averaged 0.6 percent of GDP in 1990, declined to 0.4 percent in 1995 and to 0.2 percent in 2000. However, these are averages (mean values) and to get at actual or definitive trends, it will be necessary to look at the country-level data, which may not always tally with the indications in Table 3.

With respect to *import taxation*, the indications are that trade liberalization or the systematic lowering (and for a range of merchandise imports the complete elimination) of import tariffs has not resulted in net revenue loss in a number of observed cases. As the evidence in Table 2 shows, the average tax revenue from import taxation has been, in fact, increasing during the decade 1990-2000. There are many factors explaining this development.

The structural adjustment programs (SAPs), which most African countries pursued in the 1980s and 1990s, have been supported by increased level of grants and credits (see Table 2), which, in turn, increased the level of merchandise imports into these countries. The resultant combination of increased volume of imports and possible decrease in the rate of import taxation (as a result of the trade liberalization programs) has helped to sustain, or even increase customs revenues[17]. In some cases there have been increases in the value of imports and associated tariffs (e.g. oil imports). The trade reform measures adopted by most African countries also included drastic reduction of the list of import categories which qualified for import tax exemptions, limiting legislative discretion and access to exemption, both of which tended to increase rather than decrease tax revenues from import trade. Measures were also being taken to strengthen and tighten border controls and improving customs administration and procedures, which resulted in the switching of informal trade (including smuggling and related tax revenue loss) by formal trade and hence increased revenues from the taxation of imports. There has also been a shift in import taxation toward high-duty commodity categories (and away from low-duty ones), which faced greater reduction of the exemption list (i.e. more commodities which previously enjoyed tax exemption are now subject to tax) and increased taxation rates. These also tend to cushion or prevent a decline in import tax revenue levels.

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[17] See, for example, Graham Glenday (2000), *Trade Liberalization and Customs Revenues: Does Trade Liberalization Lead to Lower Customs Revenues? The Case of Kenya.* African Economic Policy Discussion Paper Number 44, Harvard Institute for International Development and funded by USAID. (http://www.eagerproject.com/discussion44.shtml)

Table 4: Taxes on International Trade (Percent of GDP)

	1990	1995	2000	2001
Algeria	2.04	3.68	2.16	3.09
Angola	0.23	1.47	1.39	1.97
Bennin	4.27	6.01	7.90	7.68
Botswana				
Burkina Faso	4.71	5.61	2.31	2.15
Burundi	3.17	5.11	4.66	4.71
Cameroon	2.20	2.52	2.42	2.35
Cape Verde	7.36	9.94	9.82	9.57
CAR	4.26	3.91	3.72	3.87
.Chad	1.63	1.68	2.18	2.45
Comoros	6.77	4.26	5.84	8.13
Congo	4.38	4.53	1.37	2.15
CDR				
Cote d'Ivoire	5.63	8.59	5.17	5.36
Djibouti		7.09	8.85	8.67
Egypt	3.03	3.439	2.78	2.78
Equatorial Guinea		4.83	0.93	0.64
Eritrea		6.44	4.51	5.47
Ethiopia	2.67	4.77	5.16	6.39
Gabon	3.76	5.19	4.44	5.24
Gambia	11.29	9.14	10.66	8.67
Ghana	4.85	4.63	3.63	3.56
Guinea	1.37	1.58	2.20	1.97
Guinea Bissau	4.71	3.48	4.49	5.35
Kenya		4.26	3.39	2.94
Lesotho	20.61	26.30	18.28	19.85
Liberia				
Libya				
Madagascar	5.52	4.73	6.08	4.77
Malawi	6.53	4.63	2.24	2.01
Mali	4.65	5.95	8.02	8.35
Mauritania	7.06	5.40	2.35	2.37
Mauritius	11.36	7.49	6.15	5.10
Morocco	4.73	4.05	3.62	3.30
Mozambique	2.80	2.71	2.21	1.99
Namibia				
Niger	4.03	3.11	4.58	4.67
Nigeria			2.75	4.15
Rwanda	2.78	2.62	1.64	1.85
Sao Tome & Principe	4.35	3.98	4.88	4.84
Senegal		5.10	2.89	2.82
Seychelles	24.66	12.49	10.28	10.76
Sierra Leone	5.17	4.07	5.48	6.36
Somalia				
Sudan		2.71	2.41	2.22
Swaziland				
Tanzania	2.76	3.04	3.02	4.46
Togo	8.57	5.57	5.65	6.10
Tunisia	4.58	4.80	2.83	1.97
Uganda	3.35	4.76	4.85	4.64
Zambia	7.33	5.45	5.94	6.30
Zimbabwe			2.66	3.08
S. Africa	1.28	0.89	0.88	0.91
Average (Mean)	**5.54**	**5.27**	**4.56**	**4.74**
Standard Deviation	**4.78**	**3.95**	**3.21**	**3.33**

<u>Note:</u> The mean (standard deviation) values in this table differ from the corresponding values in Table 3.For explanation see footnote of Table 3

<u>Source:</u> UNECA

During the pre-reform period, foreign trade in much of the developing world and Africa had been constrained by export-import licensing restrictions, foreign exchange rationing, quotas on imports and exports, etc. With trade policy reform and as the lessons[18] from Colombia, Jamaica, Pakistan, Cote d'Ivoire and now Kenya clearly reveal, it had been possible to increase trade and hence government tax receipts from foreign trade by, *inter alia*, lifting of licensing and foreign exchange restrictions, trade liberalization, replacing quantitative restrictions on foreign trade by tariffs, etc.

The Regional Economic Community (REC) trade agreements also contain provisions, which contribute to lessen tax revenue losses arising from the trade liberalization programs of those agreements. These provisions tend to reduce the cost of entry (as members of the particular REC) and otherwise reduce the adverse impact of the program on government budgetary revenue. The RECs adopted phased schedules of tariff reduction, which gave Member States some flexibility to implement the agreements. This gradual scaling down of the tariffs prevents a drastic drop in tax revenue levels of imports by, among other things, allowing members to implement the trade liberalization and regional integration program at their own pace. The other provision in the REC agreements relates to the "compensation fund" which had been introduced in some RECs with the purpose of compensating members for any revenue loss arising from their implementation of the intra-REC trade liberalization program. The ECOWAS Summit adopted the protocol on "compensation fund" before other RECs[19]. However, because the fund allocation from the members is insufficient, ECOWAS has been seeking IMF support for financial relief over the period of transition "to cover loss of customs revenue resulting from the introduction of an ECOWAS common external tariff (CET)"[20]. In ECCAS the establishment of a compensation fund to facilitate implementation of their trade liberalization program is under consideration, while COMESA is reported to have developed "budgetary assistance measures to minimize revenue gap arising from implementation of CET rates"[21]. In all these cases, implementation reports are hard to come by, but even a partial implementation is expected to reduce customs revenue losses arising from tariff reductions on intra-REC trade.

The Generalized System of Preferences (GSP)[22] program of the Africa Growth and Opportunity Act (AGOA), offers Sub-Saharan African signatories duty and quota-free

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[18] See, for example, the World Bank (1990), *Trade Policy Reforms Under Adjustment Programs*. Operations Evaluation Department. See also V. Thomas, Aazi Matin, and John Nash (1990), *Lessons in Trade Policy*, Policy and Research Series No. 10, the World Bank.

[19] Compensation procedures for loss of revenue suffered by ECOWAS Member States as a result of the liberalization of intra-ECOWAS trade has been adopted by the Assembly of Heads of State and Government in 1980, (Decision A/Dec.19/5/80).

[20] Economic Community of West African States, *Annual Report 2001*. p.54

[21] Common Market for Eastern and Southern Africa (COMESA), *Roadmap to the COMESA Customs Union*, January 2003. p.7

[22] The GSP is a negotiated agreement at UNCTAD II (New Delhi, 1968), which enables developing countries to benefit from a temporary and non-reciprocal grant of preferences by developed countries. Under the scheme, each industrialized country determined its own system of preferences, specifying the goods, the preference rates, and in some cases, the value or volume of goods that should benefit from the specific GSP program.

access to the US market. The US also provides African partners of the Agreement investment and development assistance. The GSP, as explained earlier in the paper, is unreciprocated and covers a wide range of African commodity exports. That and the economic assistance and investment are expected to increase US trade with African countries without adversely affecting the taxation of that trade. The overall tax revenue effect of AGOA is thus expected to be positive.

The WTO Agreement also contains provisions aimed at assisting the developing countries[23] to overcome their balance of payment problems and enhance their industrial development. The revisions of GATT Article XVII have introduced the concept of differential treatment of developing countries. GATT Part IV in its special section on "trade and Development" calls for "best endeavor commitments "from the developed countries including reduction and elimination of barriers to imports from the less developed economies without seeking reciprocal treatment. These provisions are further consolidated into what came to be known as the "enabling clause", which accommodates the differential and more favorable treatment (as a departure from the MFN clause) as well as the principle of non-reciprocity in trade negotiations. There are also the Ministerial Decisions on measures in favor of the Least-Developed Countries, most of which are African. These, the various waivers (longer implementation periods for the developing and least-developed countries) and the technical assistance program are all intended to increase exports from the developing countries, improve their balance of payments, enhance their development and in general precipitate growth in global trade and economy. These, in turn, cause customs revenues from the developing countries (including African countries) to increase both in the short and the long term.

[23] These are explained in the WTO Training Package. See the WTO Website: wto.org