APPLYING THE 'STRATEGIC ECONSYSTEM': TRADE PROMOTION AND ECONOMIC DEVELOPMENT IN AFRICA

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Exceeding the global average in past years with an expectation to further accelerate, Africa is experiencing unprecedented economic growth. Foreign trade contributes considerably to the sustainable development of the continent's economies. The opening up of trade in a multilateral trading system has provided one of the major pillars for growth enjoyed by many developed and emerging countries (Klasen and Bannert, 2015). There are numerous reasons for this development, including trade liberalisation, market-based and political reforms, together with technological innovations. Thousands of African companies create jobs by developing the potential of many different sectors. A growing number of small and medium-sized enterprises (SMEs) in Africa act in a sustainable manner by using natural resources with a degree of consideration. There has been a fundamental change in Africans' thinking in recent years: the future of economic growth, particularly in sub-Saharan Africa, is closely associated with the private sector. Governments outside and on the continent understand the crucial role of private companies in generating more business.

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INTERNATIONAL ACTIVITIES AND ECONOMIC DEVELOPMENT

Internationally active African firms use a variety of strategies to serve customers. They export their products and services to buyers abroad, franchise and licence, or invest by setting up foreign manufacturing operations and regional headquarters. Exporting usually involves lower sunk costs but higher per unit costs in comparison to

Variable	r	B	β	t-ratio	sr2
Ownership	-0.274**	-0.754**	-0.142	-2.689	-0.167
Firm Size	-0.487***	-0.350***	-0.295	-5.180	-0.310
Tax	0.347***	0.117***	0.192	3.573	0.220
Cash Flow	-0.296***	-0.072***	-0.227	-4.505	-0.273
Export	0.340***	0.014***	0.216	4.173	0.254
$R2 = 0.390$ Adj.-R2 = 0.378 F (5, 258) = 32.191***	Significance *(1-tailed)* **p<0.01, ***p<0.001 N = 258				

Table 1: Factors for Export Credit Insurance Demand

investment in a subsidiary. In contrast, firms mostly invest abroad if gains from avoiding trade costs exceed costs of maintaining capacity in multiple markets (Helpman, Melitz and Yeaple, 2004). Export and FDI are major drivers for the multinational firm. These companies account for large amounts of world trade, and exports led to the emergence of multinational firms on a quite unprecedented scale. On the other hand, small and medium-sized companies play an increasingly important role in trade. SMEs introduce product, process or service innovations more often, and foreign operations are a crucial factor for their internationalisation strategy. They often represent the vast majority of businesses and produce substantial taxable turnover. Producing modern technologies such as electrical engineering, precision-engineered components or renewable energies, SMEs are the main drivers for successful economies. In many African countries, innovative SMEs engaged in the export economy have a higher growth rate.

African exporters and investors operate in a global environment characterised by heterogeneous political and legal systems, economic conditions and cultural behaviour. Therefore, internationally active companies are exposed to several dimensions of risk: political risk, commercial risk, legal risk, and currency exposure, as well as cross-cultural risk. Typically, major risks in international business arise from non-payment for political or commercial reasons. Commercial risks include payment defaults by the buyer or insolvency leading to full write-offs or temporarily uncollectable receivables. Political risk refers, for example, to war, riots or a payment moratorium imposed by the government (Klasen, 2014). International trade is also strongly connected with a well-developed and functioning financial environment.

The dynamic growth of trade in Africa over the past decades was only made possible by a rapid expansion in trade finance. The latter is crucial for trading partners in order to bridge the time lag between export order and payment for goods and services produced. Factors such as transaction volume and credit period can considerably increase costs of financing, or even make it difficult to obtain funding at all. Disruptions in trade finance lead to a severe decline in companies' output on a micro level, as well as a contraction in trade on a macro level.

FOREIGN TRADE AND GOVERNMENT SUPPORT

Companies willing to export often need credit insurance to access credit facilities and manage their receivables risk. This applies, in particular, for large transactions with longer maturities. Government export credit insurance schemes, also known as export credit agencies (ECAs), play an important role in financing export business. Export credit insurance safeguards companies against political and commercial risk of non-payment by a foreign buyer. Short-term credit insurance usually covers consumer or small capital goods, bulk commodities or services for up to 360 days. Medium- and long-term credit insurance covers large capital equipment up to 18 years. Auboin and Engemann (2014) show a significantly positive effect of insured transactions on international trade. Other research has also provided a causal link between the support of credit insurance schemes and merchandise exports (Moser, Nestmann and Wedow, 2006). Authors such as Chor and Manova (2012) have shown the effect of credit on trade. Economic aspects are highly relevant for export credit insurance schemes. The ECAs' impact is mainly associated with the promotion of national exports, and the general objective is to stimulate growth through foreign trade. A causal link between ECA support and merchandise exports, as well as job creation, has been discussed by Felbermayr and Yalcin (2013), and it is a major aim of government or multilateral ECAs to create jobs in the national economy.

WHY COMPANIES DEMAND EXPORT AND POLITICAL RISK INSURANCE

Research on export credit insurance was able to show that a variety of microeconomic motives are relevant for exporters' demand for insurance. Some authors discuss credit insurance as an essential risk management tool for exporters (e.g., Abraham and Dewitt, 2000). In addition to factors derived from the individual export transaction, Table 1 shows the example

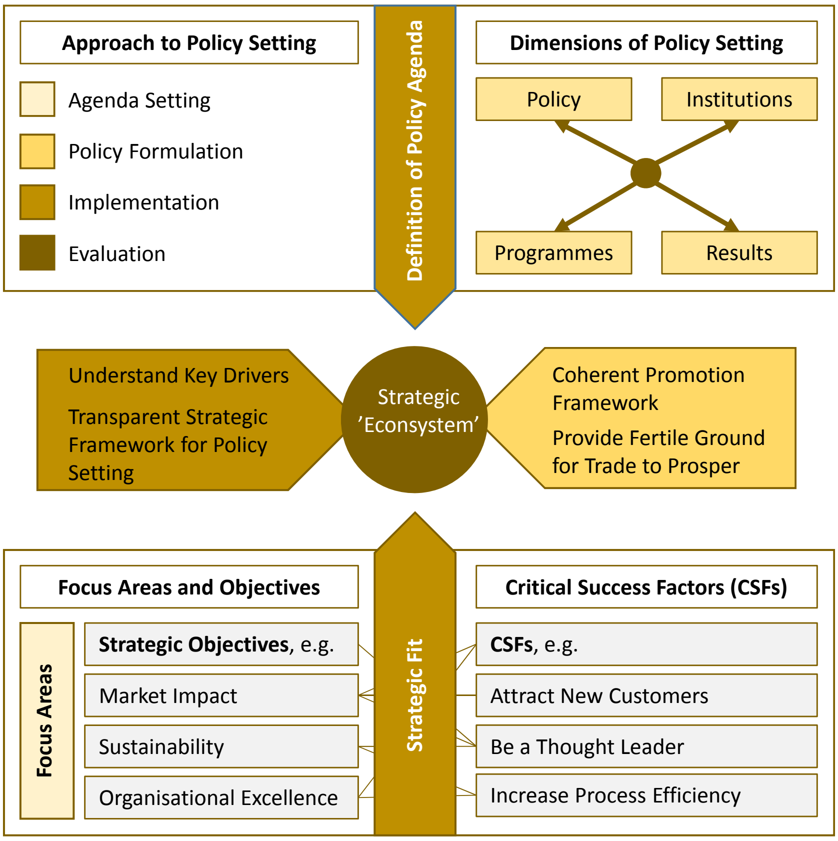

Figure 1: The 'Strategic Econsystem'

of demand of German exporters from the manufacturing industry, which appears to be driven by ownership structure, firm size, tax effects, cash flow and export quota (Klasen, 2014). Insurance is regarded as an important component of risk-averse behaviour and of transferring potential bankruptcy costs. In addition, there are indications that it is a source of real services and reduces the tax burden. Furthermore, the purchase of export credit insurance demand is relevant for financing transactions and for risks related to foreign buyers in risky countries.

Preliminary results of a current global research project on export credit and political risk insurance also show that risk aversion, company size, financing, signalling and stakeholders, regulation and digitalisation are substantial factors driving demand. For example, the exporter's company size influences opportunities to diversify business risk and the transaction cost of risk management. There is also evidence that, particularly for African exporters and investors, the knowledge base in companies is highly relevant, and financial intermediaries involved in financing trade transactions play a decisive role for demand. Furthermore, companies use export credit and political risk insurance to signal their earnings volatility to stakeholders.

SUCCESSFULLY DRIVING PRIVATE SECTOR DEVELOPMENT IN AFRICA

There are two examples for effectively combining private-sector development and government support in Africa through export credit agencies. Traditionally supporting mostly public buyers in African economies, there is now a growing number of insured transactions with private buyers, in particular in sub-Saharan Africa.

Exporters and importers benefit from export credit insurance, as ECAs are able to relieve balance sheets by transferring risk, effectively open African markets and provide acceptable finance conditions for local companies. In many cases, African businesses are able to place orders only because of export credit insurance, as exporters from many different industries are able to manage potential bad debt losses. This again supports economic diversification, which has been at the heart of many African economies for decades.

THE PURCHASE OF EXPORT CREDIT INSURANCE DEMAND IS RELEVANT FOR FINANCING TRANSACTIONS AND FOR RISKS RELATED TO FOREIGN BUYERS IN RISKY COUNTRIES.

ECAs are also important for private-sector development because of another fundamental challenge for Africa: energy supply and climate finance. African companies suffer from the lack of access to reliable electricity supplies. They regularly experience power shortages and service interruptions, resulting in lost sales or damaged equipment. On the other hand, Africa is becoming the 'go-to destination' for renewable energy solutions (see Otieno, 2015). The private sector occupies a substantial portion of the renewable energy finance space and ECAs (often together with international financial institutions) fill existing gaps. As part of the UN's Energy for All (SE4All) initiative, several ECAs support renewable-energy projects in Africa with specific reference to climate finance. This applies, for example, to the US and Danish export credit insurance programmes, but also for the multilateral African export credit agency ATI. Supported with a grant from the European Investment Bank, ATI enhances its underwriting capabilities for renewable-energy transactions in order to boost private-sector investment.

A COHERENT APPROACH: THE 'STRATEGIC ECONSYSTEM'

To further and successfully support private-sector development in Africa by the use of trade and export promotion instruments, a comprehensive policy framework is crucial. Different institutional set-ups for development support show different levels of resilience and effectiveness in coping with the economic conditions to which they are exposed. However, there is strong evidence that managing the interplay of four fundamental building blocks – public policy, focus areas, strategic objectives and critical success factors, as well as institutions – are the key to crafting sustainable and responsive economies. Together with my colleague, Henning Meyer from the LSE, I have labelled this approach to the development of such a supportive economic environment in a Global Policy special issue on economic policy, governance and institutions a 'Strategic Econsystem' (Meyer and Klasen, 2013). The aim is to create a strategic fit, ensuring an effective alignment or specific objectives with internal and external factors influencing their chances of realisation.

In the context of this comprehensive policy framework for private-sector development in Africa and officially supported export credits, this includes the following aspects. For highly industrialised countries, export plays a significant role in the national economy – innovative and integrated government financing instruments have to successfully support the competitiveness of national companies in the global economy. In addition, the objective of ECAs must be to give importers in developing countries access to finance. Using commercially motivated export credits insured by ECAs and governed by global standards ensures coherence between job impact and environmental as well as social protection. Financing and supporting foreign trade with private businesses in Africa occupies a pivotal role, impacting on new product development and job creation in developed countries through economic growth and human development in African countries.

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