

## Trade and Economic Development

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### 1. Trade and Growth

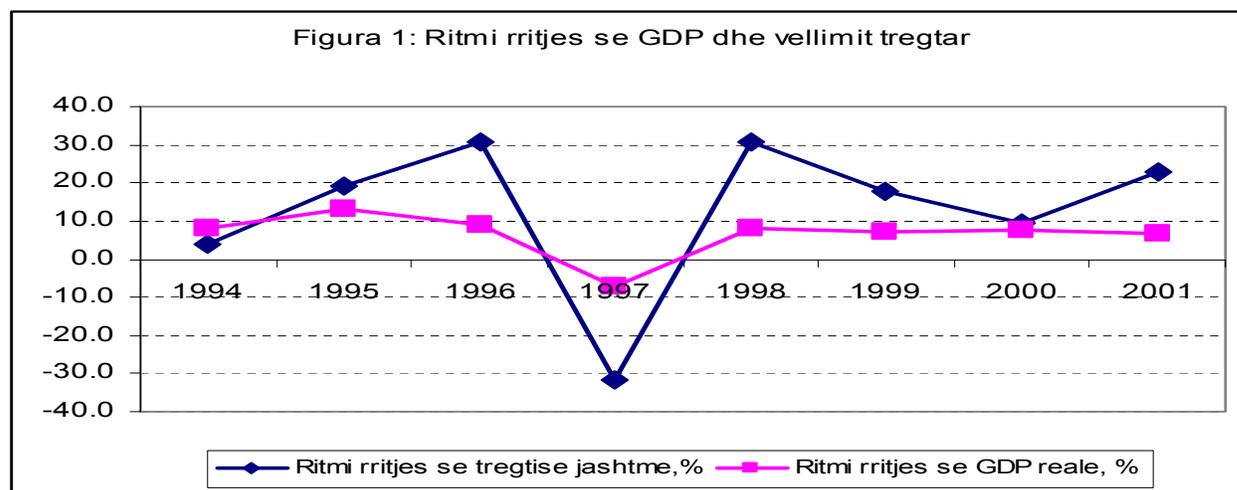
The increased economic interdependency and the strengthening of tendency to globalization have rendered the debate on trade opening, investments, and economic growth among economic researchers increasingly intensive. However, the scene is dominated by the idea that among the above variables there is a positive correlation and that the economic openness and trade liberalization are followed by higher rates of economic development and increased efficiency of factor use, especially for small countries. Trade becomes a key factor for growth in countries with modest development level or which undergo processes of restructuring and transformation as in countries in transition. For the last, the role of trade is of key importance especially on reallocation of resources, becoming a key factor for their efficiency increase.

What offers the Albanian experience of the last ten years concerning the role of trade for economic growth and development?

A simple confrontation of figures on trade volumes growth rates and GDP, reveals a positive correlation between them.

*Table 1*

	1993	1994	1995	1996	1997	1998	1999	2000	2001
In millions of usd									
<b>Foreign Trade Volumes</b>	712.9	742.4	884.6	1157.6	790.3	1031.5	1217.4	1335.3	1642.1
<b>GDP</b>	1228.1	1984.5	2422.1	2677.5	2294.5	3057.8	3676.4	3752.1	4113.7
<b>Trade growth rate,%</b>		4.1	19.2	30.9	-31.7	30.5	18.0	9.7	23.0
<b>Real GDP growth rates, %</b>	9.6	8.3	13.3	9.1	-7	8	7.3	7.8	6.5



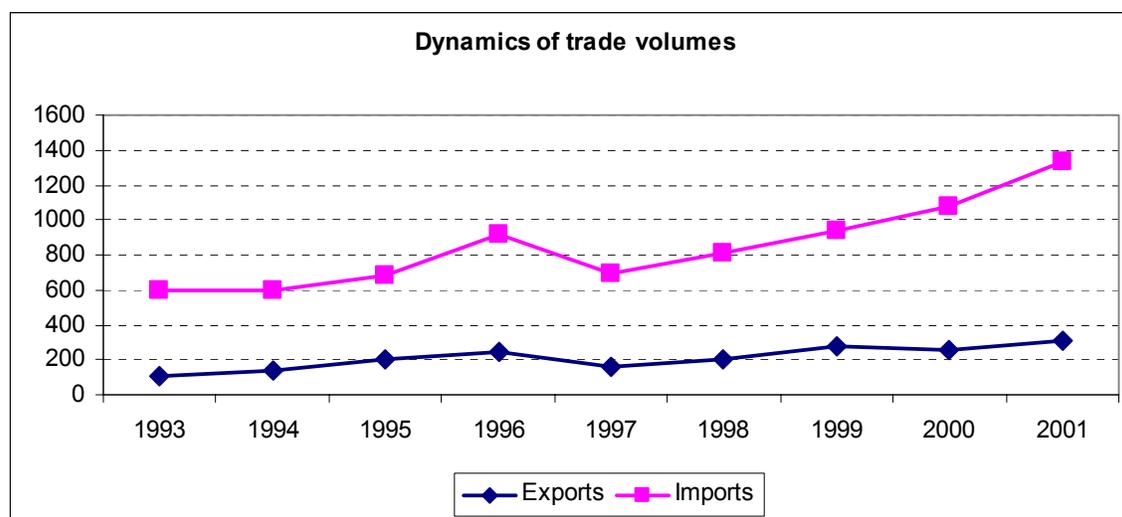
In what measure would we say that trade has positively influenced the relative high rates of economic growth? That trade has influenced a positive reallocation of resources? That trade should be considered as one of pillars of the increase of production efficiency of production resources in general?

Let's consider the first question first. Two moments should be taken into account.

**First:** Directly, trade adds to GDP only the net value of exports. Table 2 and graph 2 shows that net exports during all the period has been largely negative and, moreover, increasing during last years. Thus, at a first glance, it is impossible for positive influence of trade in economic growth. This scenario shows that trade has negatively influenced the economic growth. Adding here also the negative implications on macroeconomic figures of trade deficit, reflected on the budgetary deficit and, as a consequence, on the situation of government debt.

Table 2

<i>In millions of usd</i>	1993	1994	1995	1996	1997	1998	1999	2000	2001
Exports	111.7	141.4	204.8	243.7	158.6	208	274.4	255.9	304.6
Imports	-601.2	-601	-679.8	-922	-693.5	-811.7	-943.0	-1079.3	-1337.5
Trade deficit	-489.5	-459.6	-475	-678.3	-534.9	-603.7	-668.5	-823.4	-1032.9



**Second:** The ratio trade volume/GDP, thus, the level of trade openness, has been very modest compared to that of other neighboring countries. During the year 2000, the level of trade openness on Albania was 59.3%, positioning under the level of other economies of the region. For the year 2001, the trade openness level increased by 63.6%.

Table 3: trade openness

Countries	(X + M)/GDP*, %			
	1998	1999	2000	2001
Albania	41.3	55.2	59.3	63.6
Bosnia Herzegovina	98.4	78.2	77.1	na
Bulgaria	97.7	99.6	122.1	na
Croatia	88.8	89.2	95.8	na
Macedonia	99.8	98	114.4	na
Rumania	56.1	62.6	73.7	na
FR Yugoslavia	66.4	56.0	81.2	na
<b>SEE</b>	<b>72.5</b>	<b>74.8</b>	<b>86.9</b>	<b>na</b>

(\*Export import of goods and services scaled to GDP: Source: Georgi Ranchev, 2001 "Free Trade Zone in Southeast Europe? The Harmonization of Tax and Customs Legislation" Research paper; for Albania indices are calculated based on figures provided by Balance of Payments, publication of the Bank of Albania, 2002)

Obviously, this image is not very optimistic, but for a more detailed, multilevel, and dynamic view a fully analysis is needed. A close view of import and export developments would help for the purpose as well as for providing an answer to raised questions.

## 2. Trade and structural changes in the economy

### • 2.a Imports and economic structure

As shown in table 2 (figure 2), import volume has increased from year to year as well as the weight of imports to PBB. The higher weight of imports to GDP compared with the exports brings into sight a negative and problematic aspect of imports as it relates with high trade deficit. Import's problem is not limited only within this aspect. There is a long chain of other problems related to high level of informality, smuggling and corruption, institutional and administrative weakness, etc. However, there is another aspect of the import, often ignored, but worth dedicating more positive attention.

First, imports have been almost an exclusivity of private business, one of the fields of free private initiative freedom.

Second, imports have played an important role in particular periods (e.g. 1997) and decisive for supplying population's needs.

Third, imports have generally grown from year to year, but also some domestic products have increased their market share during the same period. The increasing demand for imported goods has served as a positive signal for the domestic production. In some sectors, the substitution of imports with domestic production has been noted.

Fourth, although their direct negative effect in economic growth, imports have exercised a positive influence on restructuring tendencies of the economy.

The analysis of imports' structures dynamics brings into view this last positive aspect of it. At Table 4, it is noticeable that the most important weight in the import structure during the period 1995-2001 is still supported by machinery and equipment imports, within the interval 16 - 18% of total, with growing tendencies in the last years. The second important group is textiles in the measure of 9-11% of total imports. The fluctuation of this weigh reflects the developments of the re-export sector. The sector of energy and carburant has grown sensibly because of the last two years' energy crisis reaching 13.8% of total imports from only 5% in the year 1996.

*Table 4: Import structure, in %*

<b>Description</b>	<b>1996</b>	<b>1997</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>
Live animals, animals products	5.0	4.3	5.2	4.4	2.8	2.2
Vegetable products	17.5	13.2	10.1	9.1	8.4	7.6
Animal or vegetable fats and oils	2.9	3.2	3.3	1.9	2.0	1.5
Prepared foodstuffs, beverages, tobacco etc.	9.5	7.3	8.9	11.5	9.0	8.1
Mineral products	5.2	7.6	8.5	8.6	13.1	13.8
Products of the chemical	4.8	5.9	7.5	5.4	5.6	5.4
Plastics and their products	2.3	3.1	3.0	2.8	3.0	2.8
Raw hides and skins, leather, travel goods etc.	2.1	2.2	2.3	2.2	1.8	2.1
Wood and articles of wood	0.8	1.2	1.2	1.7	1.0	0.9
Pulp of wood, paper or paperboard	1.4	1.3	1.6	1.5	1.6	1.5
Textiles and textile articles	9.0	10.4	12.9	12.5	11.9	10.4
Footwear, headgear, umbrellas	6.3	5.7	4.9	3.7	2.6	3.5
Articles of stone, plaster, cement, ceramic products, glass	2.4	3.5	3.5	3.2	3.9	3.7
Natural or cultured pearls, coin	0.1	0.0	0.0	0.1	0.2	0.0
Base metals and articles of base metals	4.8	6.6	6.7	8.0	7.8	8.8
Machinery and mechanical appliance, electrical equipment	<b>16.2</b>	<b>15.8</b>	<b>9.8</b>	<b>11.6</b>	<b>13.8</b>	<b>18.4</b>
Vehicles, aircraft	<b>6.1</b>	<b>4.9</b>	<b>6.7</b>	<b>7.5</b>	<b>7.4</b>	<b>5.3</b>
Optical, photographic, measuring, medical instruments	1.3	1.2	1.1	1.4	1.7	1.5
Miscellaneous manufactured articles	2.1	2.3	2.6	2.5	2.4	2.4
Works of art	0.0	0.0	0.2	0.0	0.0	0.0
<b>Totals</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

The import of machinery and equipments has contributed to increase stocks of fixed capital and innovation of technical base of the economy. Table 5 gives information about the distribution of machinery and equipments imported for each sector of the economy.

*Table 5: imports structure of machineries and equipment, in %*

	<b>1995</b>	<b>1996</b>	<b>1998</b>	<b>1999</b>	<b>2000</b>	<b>2001</b>	<b>total</b>
Agriculture machinery	3.6	4.4	2.5	2.9	2.0	1.8	2.5
Aro-processing industry	10.5	11.3	4.4	4.3	1.9	6.7	5.9
Construction industry	23.3	38.8	34.7	45.6	48.1	17.2	33.4
Engineering	10.7	3.3	4.2	3.3	8.0	4.6	5.3
Furniture industry	5.3	3.6	2.9	2.1	2.2	2.5	2.7
Paper and printing industry	3.2	4.0	4.8	3.4	2.1	1.3	2.6
Textile industry	11.6	7.7	23.9	12.7	8.0	5.8	9.7
Leather and shoes	3.4	4.1	4.4	4.1	2.0	2.5	3.1
ICT	28.4	22.8	18.2	21.8	25.6	57.7	34.8

<b>Total:</b>	100.0	100.0	100.0	100.0	100.0	100.0	100.0
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(Source: calculated based on ACIT Database).

According to Table 5, we note that the most attractive sector of imported machinery and equipments, so, the sector that has undergone a profound technological innovation has been that of communication and information technology (ICT). For the year 2001, around 58% of machinery and equipments imported belonged to this sector, growing more than two times the level in 2000. For the period 1995-2001, an average of 35% of total imports of machinery and equipments were directed to this industry. In the second place is the industry of constructions with 33% of total. Then after come the textile and shoes industry with 12.8%, agriculture and agro-processing industry 8.4% altogether, etc.

Raw materials for the national industry have had an important part of the imports structure, especially for the exports sector (imports of textile and their articles – around 10% of total imports).

In a not very detailed comparison between the imports structure and the structure of the country's economy, it is possible to come to some more positive positions towards import and its role.

**First**, it is possible to note a strong positive correlation between structural changes of the machinery and equipments and structural changes in the economy, e.g.

- Growth of ICT imports reflects growth of services weight;
- High growth rates of construction sector reflects both growth of machinery and equipments and material used in this sector;
- Growth of textile and leather industry, which is a pillar of our exports, reflects growth of machinery and equipments as well as raw materials for this industry.
- Low and decreasing growth rates of agriculture, low productivity in this sector reflect the low weight of imports of agriculture machinery.

**Second**, through an increasing contribution of capital stock and the technology innovation of respective sectors, import contributes in its “self-limitation”. In the conditions of our economy that is undergoing an important restructuring process, the “import substitution” could be achieved only through “supporting” it. The “support” in this case implies adoption of encouraging imports policies especially for machineries and equipments of modern technology and directed to sectors of high market demand.

**Third**, import of raw materials to be processed for domestic market needs or international markets, is followed by positive effects for both added value and employment.

**Fourth**, imports structure, especially its dynamics serve as a source of signals for the domestic economy and identification of investment opportunities. This has happened for many agricultural products, agro processing products, industry of clothing, furniture etc.

## 2.b Exports: problems and tendencies

Exports are not an aim in itself. An important function of exports, but not the only one, is to generate the required hard currency for financing imports of goods and services. Another important function is the possibility given by exports, as a process for economic restructuring, for the orientation of production sources towards more efficient use and increase competitiveness of the economy.

The specific aspects of our economy as a small economy in transition, gives more importance to this second function of exports. Export “increases” dimensions of the economy creating space for economies of scale. The involvement in the export process on the other hand “creates” possibilities for an effective and efficient process of resource reallocation helping the technological re-equipment of the economy.

How much has export performed these two functions in Albania?

Let us concentrate initially to the first function that of generating hard currency for financing imports. The view is not optimistic. During 2001, only 23% of imports were financed by export revenues. The most important role for filling this gap was played by emigrants’ remittances (which cover half of trade deficit) followed by funding from international institutions and other official transfers. The view becomes more obscure if we refer to narrowing tendencies of international funding and emigrants’ remittances.

The challenge is serious. How can it be approached? How can the trade deficit be narrowed? This is a very difficult question because the situation is also difficult. This remains an open question for as long as the trade deficit will be a serious problem. At last, the question is too complex to dare to give a “concluding” answer. In this situation, what we will try to do in this presentation is to divide it in some important components aiming to open a debate and change ideas with the participants. This, for the reason of reaching common positions that we consider as important both for the policy making process as well as the decision-making process of business involved in trade activity.

Back to the question: how can we narrow the trade deficit?

**1. Limiting imports?** The big dimensions of import compared with export seem to legitimate such position. An attentive analysis shows that possibilities of reducing imports are too “limited”. Why? We think that some factors influence this.

**First**, an explosion opening of the country followed the beginning of transition to the western world. Human contacts multiplied due to emigration and western life style. Needs acknowledged an explosion. Emigration remittances and other revenues have conditioned a steady high level of imported goods demand. Can this demand be limited only with limiting policy? Especially for goods that are not of basic demand. We think that it would impossible. For luxury goods, the demand is elastically related to incomes.

**Second,** In the beginning of transition, for a period, the country was almost depending from foreign aid of food. Production almost paralyzed completely. Later, agriculture and other sectors of the economy started to recover. Domestic production gradually started to “substitute” imports (and economic aid). This “substitution” process was not followed by decreasing of imports’ volumes, but at contrary, it increased continuously. Beside domestic production growth, the weight of imported capital goods increased also. Thus, the “import substitution” is happening through their “growth”.

However, there are many possibilities to encourage the imports substitution process. We think that supporting policies should be better oriented for the creation of suitable investment climate. This can be achieved through supporting entrepreneurship and SME, inducing import of machinery, equipment, and other capital goods, advanced technology, and direct foreign investment into the economy. Policies oriented towards improvement of trade infrastructures and support to managerial capacity building of businesses might have a good effect. It can be considered also improvement of policies for incentives to investment financing through remittances or generally, savings rate through formalization of money transfers. Without denying the positive effects of this attempt, we do not think that outcome would be considerable, taking into consideration the very low ratio of business loans/deposits of the banking system. In any case, the boost of savings rate and their orientation towards investments should be related to all other reforming and restructuring processes. Specific policies are not enough.

**Third,** the low level of openness of the economy does not induce for imports limitation. Even if we could think of a raise of export levels to the import ones, again, the low level of openness of the Albanian economy would have been lower than that of other countries of the region. The solution lies not in the limitation of imports, even through “substitution” of it.

**2. Export promotion?** During the beginning of transition period the crumbling of production system of the economy and foreign economic relations, almost paralyzed exports. Later, gradually started the reactivation of production activity and GDP started its growth with very high levels. Exports experienced a certain recovery. For a period, export growth rates were even higher than that of GDP and imports. For the whole period 1993-2001, export grew by 16% yearly while imports by 12%. In any case, this phenomenon is not that encouraging if we compare the absolute levels of exports with those of imports and GDP. Moreover, during last years export growth rates are even declining.

Export related problems are more populated. **First,** exports during this period have been characterized by a low level of diversification, e.g. during 2001, from about 5000 products included in the 6 digit classification of the Harmonized System (HS), only 30 of them represented 83.5% of total exports. This low level of diversification renders exports more vulnerable to changed market conditions.

**Second,** exports have also been characterized by a low level of added value of products that are part of them. Re-exports which consist in clothing and shoes (64% of total export in 2001) is dominated by a limited number of operations where local value added consist

only in labor force. The other export products suffer the same problems including agriculture products, minerals etc.

The exports situation does not make room for enthusiasm. This does not mean that export promotion initiatives would be unfruitful and solving the trade deficit problem is unhelpful. Problems posed by exports are a testimony that its encouragement is not a goal easily achievable. The solving of this problem remains the sole healing alternative of trade deficit while the means to work with the imports side are drastically limited. By promoting exports a contribution is made also for the solution of the main goal of the transition: restructuring of the economy. Between these two, there is a strong positive correlation. From this, we can draw two important conclusions:

**First**, the achievement of the objective of boosting exports needs, first of all, support by policies that have as object the deepening of structural reforms and restructuring processes. Here institutional reforms are of primary importance.

**Second**, specifically oriented policies towards encouragement of exports would be successful only if they consider and support the activation of trade instruments at the measure that these market instruments were created and function.

What specific policies would have been effective for export encouragement? Obviously, this is an open ended question and we hope that this seminar would contribute for the laying of a discussion and valuation platform of possible alternative policies. We think that, in any case, specific alternative policies should take into consideration what was already mentioned and the following:

- The need of businesses for concrete, specific, and potential markets related information;
- The need for concrete “institutional” relations of producers with those markets;
- The need to promote relations of export oriented domestic businesses, foreign businesses, and generally, the encouragement of direct foreign investments;
- Orientation for covering segments “relatively uncovered” of the market such as encouragement of exports with out-of-season products;
- The need for support related with managerial training, finance, infrastructure, institutional facilities, etc.

We think a deep analysis of export dynamics during the years '90 would be necessary. Table 6 shows information on revealed comparative advantages for products that belong to two of principal groups of export, agriculture products and those of food industry.

*Table 6: Revealed comparative advantages on some categories of agriculture and foodstuff products.*

<i>HS</i>	<i>ZERI</i>	1996	1997	1998	1999	2000	2001
1	Live animals	-0.9	-0.8	-1.0	-1.0	-0.9	-0.8
2	Meat and edible meat offal	-1.0	-1.0	-1.0	-1.0	-1.0	-1.0
3	<b>Fish</b>	<b>0.3</b>	<b>0.1</b>	<b>0.0</b>	<b>-0.1</b>	<b>-0.5</b>	<b>-0.5</b>
4	Diary products	-1.0	-1.0	-1.0	-1.0	-0.9	-0.9
5	<b>Products of animal origin</b>	<b>0.7</b>	<b>0.1</b>	<b>0.5</b>	<b>0.4</b>	<b>-0.9</b>	<b>-0.6</b>
6	<b>Live trees and other plants</b>	<b>0.3</b>	<b>0.3</b>	<b>-0.5</b>	<b>-0.8</b>	<b>0.1</b>	<b>-0.9</b>
7	Edible vegetables	-0.6	-0.5	-0.6	-0.7	-0.7	-0.8
8	Edible fruits and nuts	-1.0	-1.0	-1.0	-1.0	-1.0	-1.0
9	Coffee, tea mate and spices	-0.6	-0.2	0.4	-0.6	-0.9	-0.9
10	Cereals	-1.0	-1.0	-1.0	-1.0	-1.0	-1.0
11	Products of the milling industry	-1.0	-1.0	-1.0	-0.9	-1.0	-1.0
12	<i>Oil seeds and oleaginous fruits</i>	<i>0.8</i>	<i>0.9</i>	<i>0.8</i>	<i>0.7</i>	<i>0.7</i>	<i>0.9</i>
13	<i>Lac, natural gums, resins, gum-resins, etc.</i>	<i>0.3</i>	<i>0.6</i>	<i>-0.5</i>	<i>0.5</i>	<i>0.7</i>	<i>0.6</i>
14	Vegetable painting materials	1.0	-1.0	-0.9	-1.0	-1.0	-1.0
15	Animal or vegetable fats and oils	-0.7	-1.0	-1.0	-1.0	-1.0	-1.0
16	<i>Preparations of meat, of fish or of crustaceans, ..</i>	<i>-0.9</i>	<i>0.0</i>	<i>-0.2</i>	<i>0.0</i>	<i>0.3</i>	<i>0.4</i>
17	Sugars and sugar confectionery	-1.0	-1.0	-1.0	-1.0	-1.0	-1.0
18	Cocoa and cocoa preparations	-1.0	-1.0	-1.0	-1.0	-1.0	-1.0
19	Malt extract, food preparations of flour, meal ..	-1.0	-1.0	-1.0	-1.0	-1.0	-1.0
20	Preparations of vegetables, fruits, nuts or other	-0.9	-1.0	-1.0	-0.9	-0.8	-0.8
21	Miscellaneous edible preparations	-1.0	-0.7	-0.9	-0.9	-0.9	-0.9
22	Beverages, spirits and vinegar	-1.0	-1.0	-0.9	-0.9	-0.9	-0.9
23	Residues and waste from the food industry	-1.0	-0.8	-0.9	-1.0	-1.0	-0.7
24	<b>Tobacco and manufactured tobacco substitutes</b>	<b>0.0</b>	<b>0.6</b>	<b>0.2</b>	<b>-0.5</b>	<b>-0.5</b>	<b>-0.6</b>

As it is shown in the table 6 the index of revealed comparative advantages for the majority of products and almost for the whole period examined is negative. A more careful look would identify also some positive tendencies, but still weak. For example, in classes 12 and 13 the revealed comparative advantages in the foreign market are kept, while from the year 2000, food products are accumulating increasing advantages. Detailing of this information down to single products, would be necessary information not only for academic studies but also with practical importance for businesses that aim entering foreign markets.

In conclusion, taking into consideration the two functions of export, we would assess that the economic development strategy of the country, and in this frame the narrowing of trade deficit, should support exports primarily. Policies of import substitution are undoubtedly important but they might be successful and in cohesion with restructuring goals of the economy only if these policies undergo the strategic vision of export promotion.